

## FX Daily: Higher-for-longer narratives unfold

A strong services ISM read helped consolidate the notion of higher-for-longer rates in the US, helping the dollar stage another rally. In the UK, Bank of England commentary is shifting away from 2023 hikes to a similar narrative. Meanwhile, the EUR, SEK and other pro-cyclicals remain vulnerable despite better Chinese data



### ➔ USD: 2024 part of the USD curve driving dollar higher

September has so far seen the dollar's bullish momentum cement, and DXY is testing the 105.00 levels this morning – the highest seen since March. We want to stress that the bulk of the dollar strengthening is coming from easing bets in 2024 being scaled back rather than any expectations that the Federal Reserve will hike again this year.

Let's take the pricing of the USD forward rate curve for the two meetings in November 2023 and June 2024 as an example. The former has been stable in pricing in a peak rate of around 5.60-5.65% (less than one hike from the current 5.50%) since the start of July, having been capped by evidence of disinflation and Fed speak that has gradually diverged from the dot plot projections. The June 2024 contract has faced multiple hawkish re-ratings, from a 4.75% bottom in mid-July to the current 5.25%.

A market that continues to push forward the start of Fed monetary easing, embracing a “higher for longer” narrative on the back of US activity data resilience, is offering few reasons to doubt the dollar will stay supported for now. Yesterday, August’s [ISM services index beat expectations](#) and also suggested re-building inflationary pressures, which should keep the Fed away from sounding too dovish as they are expected to keep rates on hold at the September policy meeting.

There are many Fed speakers to watch today: Patrick Harker, Austan Goolsbee, John Williams, Raphael Bostic and Michelle Bowman. On the data side, things are much quieter, and the focus will only be on the weekly jobless claim figures, which are expected to climb to 234k.

We discussed earlier this week how the dollar was overvalued in the near term against all G10 currencies. This is still the case, although a further hawkish repricing in Fed rate expectations would compress the mis-valuation, and the current market conditions can keep the dollar expensive for longer. A consolidation into the 105.00/105.50 in DXY looks plausible at this stage. Overnight, we saw a less pronounced slump in Chinese exports compared to expectations, but the beneficial impact on pro-cyclical currencies is proving quite modest, once again showing how the US activity and dollar story is the predominant one.

*Francesco Pesole*

## ➔ EUR: Trying to survive above 1.0700 into the ECB

Our economics team has published its latest [preview of next week's European Central Bank meeting](#). It's a close call, but we think policymakers will deliver one last 25bp rate hike. As things stand now, markets disagree with this view, pricing in a mere 9bp for September and 15bp to the peak. This means that there will be room for a sizeable rebound in the euro if we are right about the ECB.

We had warned EUR/USD would likely be vulnerable into the ECB meeting, and we are indeed seeing more USD strength keeping the pair pressured. It would already be a positive sign for EUR/USD bulls to see the 1.0700 support hold for another session, possibly indicating that could be the bottom into next week's risk events.

The eurozone calendar includes the final read of the second quarter GDP, as well as a number of ECB speakers, who however should refrain from discussing monetary policy given the quiet period before the ECB meeting kicked off today.

*Francesco Pesole*

## ⬇ GBP: BoE dovish comments hit the pound

EUR/GBP has experienced a good rally in the past two sessions, now trading at around 0.8580 on the back of dovish comments by Bank of England members. Yesterday, BoE Governor Andrew Bailey stressed the downside potential of UK inflation and said that rates were likely near the top of the cycle. He was joined by two other MPC members at the Parliament testimony, Jon Cunliffe and Swati Dhingra, who also stressed inflation is at a turning point and gave few reasons to suggest multiple more hikes are on their way. It appears that the BoE may be transitioning to a higher-for-longer narrative.

Markets are now for the first time starting to cast some doubts about whether the BoE will hike rates at all at the 21 September meeting, with pricing having dropped below 20bp after

yesterday's Parliament testimony. For now, our base case is that they will go ahead with a hike but that it will be the last one, meaning markets will have to price out the additional hike still priced for later this year. EUR/GBP upside potential remains decent in our view.

Today, keep an eye on the BoE decision-making panel survey and on any evidence of abating inflationary pressure.

*Francesco Pesole*

## ⬇️ SEK: Still vulnerable in the near term

We have published two updates on Sweden for both its [economic outlook](#) and [the krona's near and medium-term outlook](#). The key points of our economic and FX updates are:

- The Swedish economy is facing significant headwinds, but investors may have overestimated the magnitude of some downside risks, including in the real estate sector
- The Riksbank should hike rates in September but will need to signal another hike in its rate path to halt the slump in the krona
- Before the Riksbank meeting, EUR/SEK might test 12.00 as the external environment remains very challenging for pro-cyclical currencies
- We still expect a rebound in the krona in 2024, but the timing is very uncertain and is tied to a turn in global FX dynamics (i.e., a turn in the dollar) more than in domestic factors

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