

## FX Daily: Is disinflation enough to get the dollar lower?

Today's release of US July CPI data will be the highlight of a quiet week. Consensus expects well-behaved 0.2% MoM readings at both the headline and core levels, providing more evidence for the Fed that inflation is coming under control. But robust US activity data and a poor overseas environment question whether the data will drag the dollar lower



### ➔ USD: Price action will be telling

It has been a quiet week for global financial markets. Last week's concerns about the quarterly US Treasury refunding seem to have dissipated after the three and ten-year auctions went well. In fact, last night's \$38bn 10-year auction was awarded at 3.99% - i.e. investors were prepared to accept sub 4% ten-year yields after all to fund the US government deficit. Today's \$23bn 30-year auction could be a little trickier. However, successful auctions and lower interest rate volatility have favoured a return to the FX carry trade. Here the world's favourite benchmark for the carry trade - MXN/JPY - is up about 1.7% since the start of the week.

Whether these benign conditions continue will be determined by today's release of US July CPI.

Recall that the soft CPI releases late last year broke the back of the dollar's eighteen-month rally. Consensus expects 0.2% MoM readings for both headline and core today - consistent with inflation running closer to the Fed's 2% target. Normally we would say that this outcome would be a dollar negative - questioning whether the Fed needs to keep rates at these restrictive 5%+ levels for an extended period after all.

However, US activity data - especially the labour market and consumption data - have been stronger than expected and are likely to keep the Fed on guard for longer. And FX price action after the recent soft 2Q23 Employment Cost Index release hinted that disinflation may not be enough to take the dollar lower on a sustained basis. For that to happen it looks like we will need to see both softer US activity data (look out for jobless claims today) and a much more attractive overseas investment environment than currently on offer in China or Europe today. Expect DXY to continue to trade within a 101.80-102.80 range.

Elsewhere today, look out for a Banxico policy meeting. This follows larger-than-expected cuts in Brazil and Chile over recent weeks. No change is expected, but investors are on the lookout for any hints of easing later this year. November is seen as a popular month for the first cut, but market pricing for the Banxico easing cycle is already fairly aggressive at 300bp+ for the next two years. The peso should continue to perform well, however,

Chris Turner

## ➔ EUR: Sticky European inflation

We have taken the view recently that the market should not be so quick to dismiss the chances of a follow-up 25bp hike from the ECB in September. The market attaches just a 35% probability to that outcome. ING's [own survey of consumers in eight European countries](#) confirms that inflation remains very sticky. Most respondents expect inflation to stay high for three years or more.

EUR/USD today will largely be determined by the US July CPI release. The short-term range is now clearly defined between 1.0925 (the 100-day moving average) and the recent high at 1.1040. Our thesis is that today's consensus CPI number may not be enough to trigger a sustained break of the 1.1040 area.

Chris Turner

## ⬇ GBP: Housing market pessimism starting to show

Earlier today, we saw the release of the RICS UK house price data survey, which showed the most pessimism over UK house prices since early 2009. It will be interesting to see whether this starts to feed more heavily into UK consumer confidence and spending. We also expect it will pressure the pricing of the Bank of England cycle, where another 50bp of tightening is still seen. Next week's release of UK earnings data, plus the July CPI, will be the next major catalyst for this story.

EUR/GBP seems happy to trace out an 0.8600-0.8650 range for the time being. But we are happy with our upside bias towards the 0.88 area for later in the year.

Chris Turner

## 📌 CEE: Another dovish message for CNB

Today's calendar includes the publication of July inflation in the Czech Republic. We expect a further fall from 9.7% to 8.7% YoY in the headline number. The market expects 8.8% and the CNB's new forecast paints 8.9% YoY. Previously released inflation in Poland and Hungary confirmed food prices dropped by 1.2% and 1.4% MoM in July, implying a drop in the Czech Republic as well. At the same time, core inflation, in particular, has surprised to the downside in recent months. Overall, we think the bar for hawkish surprises is high and see the potential for further downside surprises in the Czech Republic today.

In the FX market, EUR/CZK has been surprisingly stable since last week's CNB meeting, when the Board ended the intervention regime. One may wonder if the CNB is not active in the market again. The available central bank balance sheet data only shows us last week. However, these numbers imply zero CNB activity as expected. Thus, we think today's inflation numbers may open the way for the market to test higher EUR/CZK above 24.30 and confirm that the central bank is fine with a weaker koruna.

Elsewhere in the region, we are curious to see what impact yesterday's jump in gas prices up nearly 40% will have. For now, the CEE FX reaction has been muted, but in any case, this is not good news for the region. US inflation will also come into play today, while EUR/USD has been the main driver for HUF and PLN in recent days. Overall, we are on the bearish side for CEE FX today.

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