

FX Daily: Is equity rotation helping EUR/\$?

EUR/USD is nudging above 1.10 in quiet conditions. US interest rates are a little softer, but key drivers of EUR/USD such as interest rate differentials and energy prices have barely budged. Reports suggest that hedge funds may be rotating away from the narrow rally in US equities towards better valuations in Europe. If so, the dollar could soften further



⬇ USD: Let's see if this dollar softness can extend

The dollar has started the week on the soft side. There has not been too much data but the push factor of the Fed/US interest rate story versus the pull factor of overseas asset markets is slightly working against the dollar. On the former, US short-dated rates came off 10bp in the European afternoon yesterday seemingly on the back of a [New York Fed consumer inflation expectations survey](#) that in the one-year tenor fell to the lowest levels since April 2021. The market seemed to ignore three Fed speakers all sticking to the script that the policy rate would probably need to be hiked another 25bp or 50bp this year.

And in terms of the pull factor, some very modest support measures announced for the Chinese

property sector seem to be raising speculation that broader support for the private sector will be forthcoming this summer. Asian equities are modestly bid today.

However, a story that caught our eye in today's [Financial Times](#) may be partially explaining this soft dollar tone. The report suggests hedge funds have slashed their positions in US equities to the lowest in a decade and are turning their attention to under-valued European equities. Obviously, there are myriad factors that drive FX rates, but one can argue that the dollar trading to the weak side of what interest rate differentials suggest may be partially down to this kind of rotation. Remember that unlike bond market flows, equity flows are normally left FX unhedged.

Back to today and the best chance for this dollar decline to extend a little further will be the release of the NFIB small business optimism data for June. As our US economist James Knightley points out in our [week ahead](#), a further decline in pricing intentions in this survey will add weight to the view that inflation is coming lower. (The main event, however, remains tomorrow's release of June CPI.)

We do not expect big FX moves today, but DXY could continue drifting toward the 101.50 area.

Chris Turner

EUR: Looking at 1.1100

As discussed above, equity flows may be partially explaining why EUR/USD is drifting higher even though some key inputs are barely moving. The default view will be that EUR/USD is unlikely to break above 1.1100 since the Fed is still hawkish and risk assets have yet to adjust to the much more restrictive monetary policy settings around the world. It is probably dangerous to expect a range break-out, but if it were to occur this week, tomorrow's US June CPI figure would probably be the catalyst.

The eurozone calendar is quite light today – just the July ZEW investor expectations survey at 11CET – and we have the lone ECB speaker of Francois Villeroy de Galhau at 10CET who is unlikely to move the needle much on current market pricing of two more 25bp ECB rate hikes by October.

We have been here before and should not get over-eager on a possible range break-out, but we could see EUR/USD drifting closer to the year's highs near 1.1100.

Chris Turner

GBP: Pay data can keep the Bank of England hawkish for longer

GBP/USD has risen to the highest levels since last April on the back of some strong UK wage data for May. As our UK economist James Smith notes, the upward surprise to UK wage growth is partly down to backward revisions. But that is not a huge comfort because looking at the private sector, which is what the Bank of England focuses on, we have seen another big month-on-month increase in pay. Whether that is partly because of the ongoing passthrough of the new National Living Wage (+10% in April), is not clear. But certainly, these are not figures the BoE will want to see and will maintain the market's exceptionally aggressive pricing of the Bank Rate up near 6.40% early next year.

GBP/USD looks set to extend to 1.30 in this soft dollar environment, while EUR/GBP can retest the lows near 0.8520.

Chris Turner

📈 CEE: First sign of recovery

The beginning of the week showed that a good mood is returning to the region. However, CEE FX is still not settled and we expect higher volatility in the days ahead. The local calendar is empty today and again the focus will be on the global story.

We see the Hungarian forint as the main indicator of recovery in the region, having lost around 5% last week. Yesterday, on the other hand, it showed a 1% appreciation, the biggest daily appreciation since April, and returned to 380 EUR/HUF, which we believe may be a trigger for further inflows. Thus, a move below 380 EUR/HUF will be on the table today and we expect gains for the rest of the region as well if the global story permits. The Polish zloty posted some gains yesterday too and still has room to make up for last week's losses. We see the next level at 4.430 EUR/PLN.

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