

FX Daily: Likely FX intervention from Japan

While not yet official, there are strong indications that Japan intervened in the FX market this morning after USD/JPY touched 160.0. If we follow the same script as 22 September 2022, USD/JPY should remain volatile throughout the session before stabilising around 156-157. This week will be busy with FOMC, US payrolls and eurozone inflation



USD: Data to prove more important than the Fed

The dollar ultimately reconnected with higher yields on Friday, but a market now exploring the narrative of no easing by the Federal Reserve in 2024 should keep the door open for more dollar strength. This is a big week for FX. The Fed announces policy on Wednesday, there are some key US data releases (including payrolls on Friday), and we may have finally seen FX intervention in Japan (JPY section below).

The FOMC starts its two-day meeting tomorrow and, on Wednesday, will almost surely keep rates unchanged as markets will focus on forward-looking language. As discussed in our [Fed preview](#), PCE figures have confirmed that inflation remains too hot, and last month's very strong jobs

figures are likely to prompt a more cautious tone by Chair Jerome Powell on the prospect of rate cuts. Already on 16 April, Powell said data did not give greater confidence on the disinflation path, and we expect him to reiterate that if inflation pressures persist, rates can be kept high for as long as needed. He may be asked about the chances of another hike during the press conference, and markets will be extremely sensitive to how he articulates his answer.

From an FX perspective, we must note that the dollar traded lower after the last three FOMC announcements. The chances of Powell sounding more dovish than market expectations are, however, lower this time. Markets are pricing in 34bp of easing by December, and the momentum is tilted to that being trimmed further to 25bp. Ultimately, though, both rate expectations and the dollar are more strictly tied to data than what cautious Fed communication may signal. Today, the Dallas Fed Manufacturing index should not move the market, but on Wednesday, ADP payrolls, JOLTS job openings and the ISM manufacturing (service index out on Friday) will all be key drivers before the FOMC announcement.

Friday's jobs report is the week's biggest event – probably more important than the Fed meeting. The NFIB small business hiring survey and the ISM employment index are pointing to a slowdown in employment gains in the second quarter, and our economics team expects a 210k payroll print versus 250k consensus. We think the dollar is more likely to lose some ground because of payrolls than because of the Fed if anything. Before key risk events take over, we still favour another leg higher in the greenback. DXY is trading lower after what was probably a round of FX intervention in Japan (more on this below), but downside risks to EUR/USD can fuel a return to the 106.0 mark into the Fed meeting.

Francesco Pesole

EUR: Inflation to endorse June cut

Inflation data in the eurozone will be released in the first half of this week. Spain and Germany publish their April CPI reports this morning, while the eurozone-wide flash estimate is due tomorrow and is expected to remain unchanged at 2.4% year-on-year. The focus, however, will be on core CPI, which is expected to slow further from 2.9% to 2.6% YoY. The eurozone's advanced first quarter GDP figures are also due tomorrow.

We expect inflation figures to confirm the European Central Bank's diverging path from that of the Fed and consolidate expectations that the Governing Council will proceed with a first cut in June. It will be interesting to hear what ECB speakers have to say about the inflation releases this week. Pablo Hernández de Cos, Philip Lane, and Luis de Guindos are all due to speak today.

We had argued that EUR/USD belonged below 1.0700 after the Thursday's first quarter PCE release and still see downside risks for the pair into the Fed meeting on Wednesday after the USD/JPY move overnight triggered a EUR/USD rally. The EUR:USD two-year swap spread has re-widened to -155bp, and the minor correction lower in 10-year UST yields looks insufficient to take a real toll on the dollar. Another slowdown in eurozone core inflation should instead solidify ECB rate cut bets and prompt a weaker euro. The risks appear skewed to a return to sub-1.0700 today or tomorrow.

Francesco Pesole



GBP: Rate expectations firming up

Expect Bank of England rate expectations to be influenced primarily by the Fed and US data this week, as domestic drivers will be quite scarce. The UK calendar includes only some leading figures for March, housing figures for April and the final PMI report, while BoE officials will not be able to comment on monetary policy as the pre-meeting quiet period starts.

The recent rollercoaster in BoE policy comments and a substantial repricing higher in US rates have left the Sonia curve attached (21bp) to the prospect of an August rate cut, but also signal market reluctance to price in additional cuts (44bp of easing by December). That might be leaving sterling in a stronger position than the euro this week – especially considering EUR downside risk for EZ inflation – but we still believe EUR/GBP will ultimately find a more stable upward path as investors price in larger BoE cuts. For now, the pair has erased almost all recent gains and can push back below 0.8550.

Francesco Pesole

JPY: Likely that Japan pulled the trigger on intervention

There are strong indications – but still no officiality – that Japanese authorities intervened in the FX market this morning. USD/JPY touched 160.0 at around 02.30am BST and immediately faced two drops: a smaller one to 159.40, and then at 05.00am BST initiated a big fall to 105.0 (nearly a -3% move). It is now trading around 1.4% off the lows, at 157.20.

Japanese top currency official Masato Kanda replied, “No comment for now,” when questioned about whether he had deployed FX intervention this morning. However, these moves have all the standard characteristics of currency intervention: the “line in the sand” at 160.0, the sharp increase in volume and the size of the move. In this last aspect, the JPY spike may have been exacerbated by thinner liquidity conditions on a Monday morning which is also a Japanese public holiday.

For now, the market dynamics are broadly following those from 22 September 2022, when Japanese authorities intervened with around \$20bn to support the yen. Back then, the USD/JPY initial drop was around 3.5%, followed by a rebound worth around half of the initial move. Shortly after, the pair briefly dropped again below the initial low and rebounded again. At the end of the session, USD/JPY was trading 2.3-2.5% below its pre-intervention level. If we followed the same script this time, USD/JPY would end up trading around 156.50 by the end of today.

Markets will be monitoring any further comments from Japanese officials very closely at this point. First, to have some confirmation that they have intervened, but crucially to hear whether they signal this will be an “intervention campaign” as opposed to a one-off move. The tendency to sell the rally and re-test the officials’ tolerance is something we have seen in other FX intervention instances across the FX market – although the September 2022 experience suggests markets may be reluctant to push it too close to 160.0 again. This is also a week full of US events: a hawkish Fed and strong US data would put significant fresh pressure on the yen.

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