

Article | 10 February 2026

FX

FX Daily: JGB stability helps the yen

Some welcome stability in the Japanese bond market is allowing a more positive assessment of the yen to win through. However, it would probably take much earlier Bank of Japan tightening to drive USD/JPY closer to 150. And after a poor performance on Monday, the dollar could derive a little support from a decent US retail sales figure today



➔ USD: Focus on retail sales and the weekly ADP jobs data today

The dollar struggled yesterday and sentiment is poor. One can see that in the FX options markets, where the skew for dollar puts remains very much in demand over the short, medium and longer-term tenors. After yesterday morning's [Chinese news](#), the dollar took another downleg after Kevin Hassett, the chair of the National Economic Council, suggested that the market should 'not panic' over lower jobs numbers. Investors took this to mean that tomorrow's US January jobs data could be disappointing. Also noteworthy overnight were comments from the Fed's Stephen Miran, that recent dollar weakness was not of 'first order' consequence for US inflation. This adds to the view that Washington is quietly pursuing a policy of benign neglect when it comes to the dollar.

Looking ahead, today sees the release of the weekly ADP jobs data, the NFIB small business optimism index and then the December retail sales figure. The retail sales control group is

expected to grow at a reasonably healthy 0.4% month-on-month and can maintain the view that the US consumer is alive and well. This thesis can extend throughout March once what should be a healthy set of tax rebate checks arrives towards the end of this month. And later today we will see the results of the US three-year Treasury auction. This week, the Treasury auctions three-year (\$58bn), 10-year (\$42bn) and 30-year (\$25bn) paper. There are no signs yet of falling foreign demand at US auctions, but with US diversification a hot topic at the moment, any disappointing auction result could hit the dollar.

DXY could well be in the middle of a new 96.50-97.50 range for the next few days and will probably take its cue from labour market releases.

Chris Turner

➔ **EUR: Going steady**

Procyclical currencies remain in demand and that includes the euro. Eurozone sentiment figures continue to nudge higher and that included the February Sentix investor confidence figure which yesterday jumped back to the highs of last year. This appetite for procyclical currencies is also very evident in the emerging market space, where the Chinese renminbi continues to advance steadily. No doubt policymakers in Beijing are welcoming the gains in the renminbi, alongside those for the euro and the Swiss franc, when the status of the dollar is being questioned. The renminbi joined the elevated status of the core reserve currency world when it entered the IMF's Special Drawing Rights a decade ago. It is now reaping the fruits of those labours.

As to EUR/USD, it is not clear whether we should be chasing it higher from current levels just above 1.1900. Buy-side dollar hedging activities are hard to time, and it will probably take a surprisingly soft US NFP report tomorrow to launch an attack on 1.20. In terms of short-term levels, 1.1920/25 is the trigger for 1.1960.

Chris Turner

⬆️ **JPY: Subdued JGBs could allow a yen recovery**

Japanese markets continue to do well after the LDP's resounding success in Sunday's election. JGBs are the key asset class to watch here in terms of whether the election proves a net yen negative or yen positive. So far, JGB yields have been contained and the yen is finding support. At the heart of the story here is how the government plans to fund its JPY5tr temporary consumption tax cut. Some suggestions have been made that it could use its FX reserves – i.e. draw money from the Foreign Exchange Fund Special Account (FEFSA). Conveniently, Japan made about JPY5tr on this account in the prior fiscal year on the back of capital and currency appreciation from its FX holdings of largely US Treasuries. Japan does have large FX reserves and there are precedents of Japan using gains in FX reserves to fund the

government's general account. But tapping FX reserves for budgetary issues is a very sensitive topic, which, for example, the Swiss National Bank does in a very structured way.

Nonetheless, while JGB yields are contained, investors can take a more glass-half-full approach to Japan and the yen. Here, the focus is now on how much foreign capital is directed towards Japanese equities, with some local brokers expecting JPY10trn to be heading Japan's way over the next three months. That will have investors thinking twice about long positions in USD/JPY and could well be a catalyst for USD/JPY to break under 155. Or at least this could allow the yen to follow the likes of the euro and Swiss franc in appreciating when the dollar comes under broad-based pressure.

Chris Turner

CEE: The forint continues to dominate the market

The region opened the week with little activity and lacks more local stories. It will likely be similar today and tomorrow as the first interesting data will be released on Thursday, including January inflation in Hungary. Although all CEE currencies saw some support yesterday from a weaker US dollar and last week's higher rates, in the case of the zloty and koruna, we did not see a deviation from the usual ranges of 4.200-230 EUR/PLN and 24.200-400.

EUR/HUF remains a different story and yesterday we saw another gap lower with new more than two-year lows below 377. We see the forint benefiting from the external situation of a weaker US dollar and some hopes for a peace agreement between Ukraine and Russia. On the domestic side, despite the imminent start of National Bank of Hungary rate cuts, the key rate is currently by far the highest among CEE peers, providing the best carry, after the Czech National Bank and National Bank of Poland delivered most of the cutting cycle.

At the same time, the rate cut in Q1 is fully priced in and even though Thursday's inflation figures should be weak, we believe the forint should not be significantly damaged. The next risk is the NBH meeting in two weeks if the central bank shows too much dovishness. However, the current NBH governor's tone suggests a rather cautious approach to future rate cuts, securing forint stability.

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