FX Daily: Limited activity amid diverging signals

The US market reopens post-Thanksgiving with limited activity expected. The DXY strengthened slightly, correcting Wednesday's sell-off. The Brazilian real hit an all-time low due to disappointing fiscal cuts. German inflation stagnated, supporting dovish ECB pricing, likely weakening the euro. Polish inflation to test dovish market pricing

US markets are set to reopen after the Thanksgiving holiday but trading is likely to be quiet

USD: Market opens after Thanksgiving but limited activity expected

The US market reopens after Thursday's Thanksgiving holiday, but only limited activity can be expected. The calendar is empty and the market should be catching up with the dovish wave from Europe after the German inflation numbers. However, with core PCE released on Wednesday, we could see confirmation of the divergence between Europe and the US here. The DXY strengthened slightly yesterday in limited trading on the US side and erased one quarter of Wednesday's sell-off after hawkish comments from ECB policymaker Isabel Schnabel. Today we should see further correction and a return to previous positions similar to yesterday with the Rest of the World trending more towards the dovish side and the Federal Reserve's December decision still undecided.

Elsewhere, the Brazilian real reached an all-time low after the government presented a long-awaited fiscal cuts proposal that disappointed financial markets, demanding stronger action given the magnitude of the problem. The government's weak resolve seems to have only encouraged markets to be more negative on the currency and build larger short positions, although the real has been under pressure for the past two months, much like the entire EM space. USD/BRL closed slightly above 6.000 yesterday in a thin trading environment, significantly underperforming rather stable Latam currencies. We can expect pressure on the currency to remain in the market, especially if we see a USD bounce. The finance minister admitted to further discussions with President Lula on further adjustments to the fiscal package if needed.

Frantisek Taborsky

EUR: Weaker German inflation supports the return of a weaker euro

German inflation (HICP) surprised to the downside yesterday by stagnating at 2.4% year-on-year, while the market expected a rise to 2.6%, supporting the market view of a 50bp ECB rate cut in December. Although the market added only 1bp to December's rate cut pricing for a total of 30bp, longer-dated rates rallied significantly after the numbers were released. Eurozone inflation numbers are due today with downside potential following yesterday's number and we are getting more central bank comments in the meantime. ECB's Francois Villeroy believes the central bank no longer needs to hold the economy back and can take rates to growth-supportive levels and sees significant scope for rate cuts although it is unclear where the terminal rate is. The ECB's Klaas Knot said the central bank should ignore supply shocks as long as inflation expectations are under control, but act strongly if there is a risk of damage to the economy. So after a clearly hawkish Schnabel, comments from the ECB remain mixed, which is reflected in mixed market pricing.

However, Carsten Brzeski, our head of macro, believes that yesterday's German inflation numbers support the hawks in the ECB and a 25bp rate cut in December seems more likely now. The market, on the other hand, sees it the other way around and we are slowly moving in a dovish direction which should weigh on the EUR, especially after the bounce following Schnabel's comments. On Wednesday EUR/USD bounced down from levels just below 1.060. Yesterday we saw the first dose of correction, and with the US market back in play we should see a continuation of this trend today. The EUR:USD rate differential tightened slightly by 4bp yesterday following the German numbers, indicating EUR/USD heading back towards 1.050.

Frantisek Taborsky

PLN: Inflation print to test dovish market pricing

In Poland, November headline inflation will be published today, as always the first in the CEE region. Our economists expect a decline from 5.0% to 4.6% YoY in line with market expectations. The survey seems to be balanced on both sides. Core inflation should remain unchanged at 4.1%, but risks seem to be to the upside here. The print is particularly interesting in the context of the National Bank of Poland meeting next week. The market remains strongly on the dovish side after the government decided to freeze energy prices next year, pushing headline inflation to the lower end of central bank expectations.

The market at the moment is expecting about a 50% chance of a 25bp rate cut in February and

March looks like a done deal with a 50% chance of a 50bp rate cut. Our economists remain cautious and the baseline is a 25bp rate cut in May with 100bp in total next year. However, the market sees more around 150bp here. So today's inflation print may decide with what view we go into next week's NBP meeting. Comments from the NBP have been very mixed in recent weeks discussing all possible scenarios. Overall though, market pricing seems to be heavily biased to the dovish side and given the extent of the rate move, positioning is probably quite heavy. On the other hand, EUR/PLN has tried to break 4.300 several times in the last few days, the lowest levels since early October. Although we believe CEE currencies are lagging the global trend and should be weaker, Poland's zloty may get a boost from the NBP or inflation in the event of a hawkish surprise and continue to outperform CEE peers as we discussed earlier here.

Frantisek Taborsky

CEE: Hungary chooses new central bank governor

In addition to inflation in Poland this morning, detailed GDP numbers in Turkey for 3Q have already been released and we will see the same release in the Czech Republic, following yesterday's numbers in Poland showing weak household consumption. However, the main focus should be on Hungary, where the PM decided that the current Finance Minister Mihaly Varga will become the Governor of the National Bank of Hungary from March next year. Although the name was widely expected, uncertainty has flared up around the appointment in recent days. We assume that the appointment of a finance minister is fully priced in. However, the alternatives mentioned by journalists were likely to be seen by the market as more dovish options. Therefore, Hungary's forint could get some support this morning.

In the meantime, EUR/HUF briefly touched 415, a new local high yesterday but later lost the gains to close unchanged yesterday. As we discussed here earlier, we believe EUR/HUF is fully reflecting the shift in EUR/USD and the global environment after the US election, and CEE peers are rather lagging. Therefore, we don't see much reason for a significant change in EUR/HUF levels here. On the other hand, positioning is heavily short HUF at the moment in our view and hints at some move from the government or central bank may be a signal to the market to take some profits and allow HUF to rally. However, in the medium term, we expect EUR/HUF to continue up towards 420 in 1Q25.

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