FX Daily: Limited FX implications from oil price jump

US sanctions on Russian oil producers triggered a rally in crude. So far, however, that has only erased October's losses, and it remains unclear whether Russian oil flows will be affected enough to justify structurally higher prices, and, by extension, a stronger USD. So far, the FX impact has been small, partly due to a cautious stance ahead of US CPI

USD: Holding pattern

Based on yesterday's price action, we reiterate our view that the dollar's rebound is getting tired and probably requires some hawkish repricing to keep going. As discussed over the week, we don't think tomorrow's US CPI will offer that opportunity as we expect a consensus 0.3% MoM core print. But surely with 50bp of easing fully priced in by year-end, any hot print could offer good support to the dollar.

FX volatility remains quite subdued in general, and well below the average of the past 12 months. This remains a good environment for carry trades, and the yen's funding appeal could delay the recovery in spot despite markets looking more relaxed about Japan's domestic story.

On geopolitical news, Trump has denied reports that the US will allow Ukraine to use long-range missiles, just as the US has announced new sanctions on Russia, including on oil producers Rosneft and Lukoil, which produce more than 5m barrels per day. Oil prices have rallied around 4% on the news, but the move has merely unwound October's losses so far, and we'd likely need to see Brent heading to 70$ to result in tangible support for USD.

The key question at this stage is whether sanctions effectively reduce Russian oil flows (primarily to India). Back in January, oil markets overreacted to similar news, but the ultimate impact on Russian flows was limited. So it's probably too early to conclude whether these sanctions are enough to shift the range structurally higher for oil prices.

Francesco Pesole

EUR: Heading into a non-event ECB

EUR/USD is hovering around 1.160, a level that, in our view, can work as an anchor again today and possibly for a few more days should US CPI fail to add much to the dollar narrative.

The eurozone calendar only includes consumer confidence data (not market-moving) today, and tomorrow's PMIs may also have limited spillover into FX. Next week's ECB meeting will incidentally be a non-event in our view – as discussed here.

In the rest of Europe, Scandinavian currencies are performing quite well this week, mostly thanks to their high beta to the recovery in risk sentiment. Incidentally, both Sweden and Norway present a combination of decent growth prospects and low debt that favours rotation into their (undervalued) currencies in periods of market calm. We remain generally constructive on SEK and NOK, even if the short-term picture is more mixed than the medium-term one.

Francesco Pesole

CEE: PLN tests new gains despite rates pointing in the opposite direction

Yesterday's retail sales figures in Poland did not excite the market too much, but as our economists discuss, the details confirm the strong form of the economy and GDP in the third quarter. Today, we will see more secondary data in the CEE region, and we are also getting closer to the start of the CNB blackout period from Thursday next week, and the probability of seeing some interviews of the CNB bank board is increasing. The November meeting of the central bank will also bring a new forecast, which we could hear some hints about in the bank board's statements.

EUR/CZK and EUR/HUF saw only some further side moves and CEE lacks a stronger impulse for movement. On the other hand, EUR/PLN surprised with a quick swing down yesterday and, without any significant reason, tested levels below 4.225, the lowest levels since April. PLN erased most of the profit and closed trading again above 4.230 at the end. However, the market shows that PLN has some potential, although rates point rather in the opposite direction.

Chris Turner

TRY: Uncertain size of rate cuts after higher-than-expected inflation

The Central Bank of Turkey will decide on another rate cut today. We expect a 150bp rate cut to 39%; however, the story is more unclear than usual. The latest inflation prints surprised to the upside, indicating a slowdown in rate cuts compared to the previous 250bp.

Higher-than-expected inflation data for September shows the impact of pressure on food prices and challenges in services inflation, while indicators for October imply further upside risks to the outlook. The central bank has a hawkish forward guidance, pledging to tighten policy if the inflation outlook deviates from interim targets. Therefore, the question is whether the bank would stop or adjust the pace of cuts with the recent deterioration in the underlying trend. Given the high level of the policy rate and likely decline in inflation ahead, we expect gradual rate cuts to continue with a 150bp cut to 39% in the October MPC, though risks are tilted to the upside with a lower or no cut.

The OIS and bonds curve saw a strong upward repricing and the market shifted significantly to the hawkish side, where, in our opinion, it is no longer worth chasing the move and the risk of surprises has shifted to the dovish side in our view. On the FX side, the picture remains unchanged and although TRY continues its weakening trend, carry continues to sufficiently compensate for losses from long positions. Although the market has become accustomed to political noise and USD/TRY is not easily shaken these days, this Friday the market expects a court hearing regarding the congress of the opposition CHP party.

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