FX Daily: Low vol environment continues

US jobs numbers continue to cause ripples in a becalmed summer FX market. Expect more of the same today as the market focuses on the weekly initial claims ahead of tomorrow's big NFP report. In Europe, the focus will be on the eurozone's August CPI release. Expectations of a further hike from the ECB are firming up and justify EUR/USD trading at 1.09-1.10

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USD: Thrashing around in a low vol environment

Second-tier US jobs data (JOLTS and ADP) have seen the dollar soften a little this week. However, the data have yet to prove the smoking gun that can mark the end of the Federal Reserve's hawkish stance. Stronger trends will only start to develop should we see a large downside miss on tomorrow's release of the August NFP jobs data or a sharp rise in the unemployment rate. That would undermine the thesis that strong employment consumption can keep the Fed in hawkish mode for a lot longer than most think.

For today, the focus will again be on some second and third-tier jobs data in the form of the weekly initial claims read. We will also see personal income, spending, and the core PCE deflator for July. Consensus actually sees the core PCE deflator rising to 4.2% year-on-year from 4.1% – so hardly a reason for markets to add to dollar short positions.

In general, cross-asset market volatility remains low and there is not much to argue against the Japanese yen or Chinese renminbi-funded carry trade. As we have noted before, 5.30% overnight rates mean the dollar can hold gains in a carry trade environment. Currencies outperforming remain the EM high-yielders, such as those found in the CEE3 region and also Latam. Here, the Mexican peso continues to hold gains and offer near 12% implied yields. The peso should also be helped by the latest remarks from Banxico that, unlike Brazil and Chile, it is not considering rate cuts anytime soon.

Unless we see a sharp spike in the weekly initial claims data today, we suspect DXY does not break too far from a 103.00-103.50 range.

Chris Turner

EUR: Focus on the eurozone August CPI

Flash August CPI data for the eurozone is released at 11:00 am CET today and is expected to show a gradual decline in both headline and core YoY readings to 5.1% and 5.3%, from 5.3% and 5.5% respectively. However, the decline is proving gradual and we are actually starting to see expectations of one more rate hike from the European Central Bank firm up a little. These peak at around 21bp of tightening priced in for January next year. Our macro team feels that the chances of a September rate hike are under-priced (now a 43% probability) meaning that EUR/USD could get a little support from the ECB story over the coming weeks.

Today, also look out for a 09:00 am CET speech from ECB hawk Isabel Schnabel, speaking at a conference on 'Inflation: Drivers and Dynamics'. We will also see the ECB minutes for the July policy meeting released at 1:30 pm CET.

EUR/USD has turned a little more bid over the last few days as US jobs data has softened the front end of the US yield curve and sticky inflation has kept EUR short-dated interest rates supported. Our short-term Financial Fair Value model sees EUR/USD fairly priced near 1.0900 - suggesting a probably range-bound session into tomorrow's US NFP release.

Elsewhere, we note that Switzerland is planning some new large-scale Anti Money Laundering measures for 2024. This may be a slow-burn story, but one which may ultimately weigh on the Swiss franc in 2024.

Chris Turner

JPY: Where is the alarm?

USD/JPY has quietly drifted into the 145-150 intervention zone without triggering many alarm bells in Tokyo. One difference between now and the intervention period last September and October is that FX conditions are much more orderly. For example, one month USD/JPY implied volatility is trading near 9% today versus levels in the 14-15% region during Japanese FX intervention last year. At the same time, there is no sense of a 'sell Japan' mentality emerging, and Japanese authorities may actually tolerate a softer yen given the deflationary forces emerging from China and the weak export markets in Asia and Europe.

Unless we see some financial shock that triggers an unwind of the carry trade, it looks as though USD/JPY can hang around this 145/150 region longer than we had originally forecast. A decisive turn lower may have to wait until the late September and October period when more evidence of a US slowdown should have emerged and speculation will be growing over a Bank of Japan policy change at the meeting in late October.

Chris Turner

NOK: Norges Bank may keep daily purchases at NOK1bn

Norges Bank is due to announce the size of daily FX purchases for September today, and despite lingering expectations of some market participants that FX buying would be scaled down, we expect it to be kept at one billion NOK. That remains a consistent figure with the most recent government estimates for petroleum revenues.

The continuation of NOK selling by Norges Bank is seen by some as a hindrance to the recovery potential of the krone, although the deep undervaluation and dependence on external factors suggest it plays a rather secondary role. Still, we could see some NOK weakness today as some expectations for a trim in FX purchases are unmet.

We continue to like the chances of a NOK rebound. EUR/NOK struggled to break below 11.50 yesterday, with some support also coming from a strong euro, but an environment that sees a bullish US yield curve steepening should see high-beta commodity currencies like NOK perform better than the EUR. We still expect to see EUR/NOK trade close to the 11.00 gauge by the end of this year.

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