

## FX Daily: Markets are trying to help Powell over the 50bp line

We sense markets may be pushing the pricing for tomorrow's FOMC rate cut closer to 50bp in an attempt to influence the Fed decision, which is likely to be a very close one. That might prove effective and deal another blow to the dollar, but our US economist still narrowly favours a 25bp move. Today's calendar includes US retail sales, German ZEW and Canada's CPI



US Federal Reserve  
Chairman Jerome  
Powell

### ➔ USD: Growing 50bp cut bets

Markets have continued to consolidate their bearish dollar positions ahead of tomorrow's FOMC announcement. This FX dynamics is a direct consequence of the steady dovish repricing in rate expectations, with the swap market now attaching around 70% implied probability (43bp) of a 50bp cut tomorrow.

Remember that the last two key data releases (jobs and inflation) did not really point to a half-point cut, and growing dovish bets actually started late last week on the back of some media reports that tomorrow would be a tight decision between 25bp and 50bp. Our economics team is narrowly favouring 25bp, but admit it's a very close call.

One way to read the recent market moves is that investors may be attempting to be the deciding factor in a potentially split FOMC decision. The reasoning here follows that of former FOMC member Bill Dudley, who late last week said that the Fed does not like to surprise markets as he made the case for a 50bp cut. In other words, if markets price in 50bp, the Fed will be more likely to deliver 50bp. Needless to say, this is a dollar-negative mechanism, and we struggle to see a rebound in the greenback today unless retail sales surprise enough to discourage dovish speculators.

The consensus call is that retail sales marginally declined (-0.2% MoM) in August, although the index excluding auto and gas is seen only slowing from +0.4% to +0.3% MoM. Industrial production figures for August are also released and expected at +0.2% MoM after a poor July read.

USD/JPY briefly explored sub-140.0 levels before rebounding yesterday and is currently trading at 140.65. The yen has a 14% weight in the DXY dollar index: a decisive move below 140.0 can see DXY slip through the 100.50 August lows.

*Francesco Pesole*

## ➔ EUR: ZEW pessimism may not hit the euro

The week after an ECB meeting is often filled with various members' comments aimed at fine-tuning the Governing Council's policy message. So far, the remarks have been quite heterogeneous. While Chief Economist Philip Lane said there is a clear path ahead for rate cuts, Slovak central bank chief Peter Kazimir probably summed up the ECB hawks' current view by explicitly ruling out another cut before December. Ultimately, all this post-meeting noise sounds like a signal that President Christine Lagarde's attempt at defaulting to strict data dependency is both hard to enforce and perhaps not unanimously shouldered by GC members.

EUR/USD has found good support on the back of USD softness and has moved in line with our recent expectations. We see no strong reasons for a correction before tomorrow's Fed meeting. The German ZEW figures today will likely be poor again. The current situation index is expected to slip further to -80, and the expectation metric from 19 to 17. But the euro's strong momentum has gone through several concerning eurozone activity prints, and the ZEW should merely confirm the widely-priced notion that Germany's outlook remains grim.

We expect a consolidation in EUR/USD above the 1.110 gravity line into the FOMC risk event.

*Francesco Pesole*

## ➔ CAD: CPI to endorse aggressive dovish bets

Canada's inflation is expected to slow further today. The consensus for August headline CPI is 2.1%, essentially at the Bank of Canada's target mid-point, while all core measures of inflation are seen decelerating by around 0.2%YoY. Remember that core inflation is already well within the BoC's 2-3% target band, and we believe today's print will do very little to discourage the ongoing dovish bets on BoC easing.

If growing expectations for a 50bp Fed cut largely stem from the notion that the FOMC is starting its easing cycle too late, the same cannot be said for the BoC, whose policy rate has already been cut three times and is sitting at 5.25%, 125bp below the Fed funds rate. However, as it often happens, Fed pricing has a huge influence on BoC pricing, and markets have recently moved to price in 75bp worth of cuts in Canada over the next two meetings.

The September policy announcement is next week, and we suspect the BoC may opt for a 25bp even if the Fed cuts 50bp tomorrow and Canada's inflation slows as expected today. We cannot exclude that this will be followed by a 50bp reduction at the December meeting, but we continue to favour 25bp steps by the BoC.

Accordingly, we think that the Canadian dollar can benefit from some hawkish repricing over the coming months. USD/CAD is struggling to make its way steadily below 1.35 and recently jumped back to 1.36 as oil prices fell. Our view remains that Fed easing can ultimately help a multi-quarter USD/CAD decline materialise, but for the moment some stabilisation is more likely, as CAD remains less attractive than many other high-beta currencies.

*Francesco Pesole*

## CEE: Upcoming blackout period in the Czech Republic

Today's calendar in the CEE region is empty except for industrial production in Romania for July this morning. However, we do have a few speakers scheduled. In Hungary, the minister for the economy, who reopened a dispute with the central bank last week, is speaking at a local conference, and we could see more headlines today. Also today, Hungary has a deadline for paying an asylum-related fine imposed by the EU, which the government has criticized in the past.

In the Czech Republic, CNB board members still have the last two days before the blackout period to express their opinions ahead of next week's meeting on Wednesday. Yesterday we saw MPC Holub and Kubicek both preferring a 25bp rate cut for next week's meeting but not providing an outlook for the coming months and next year. We could still see some more MPCs today in the headlines.

In the markets, our positive bias from yesterday worked well in the HUF market and PLN saw some gains as well. However, on both currencies we don't see too much room to rally further from current levels, we still retain a rather bullish bias for HUF even though medium term we see EUR/HUF rather higher, bouncing off 392-393 levels. EUR/CZK remained almost unchanged yesterday around 25.150. The market has not reacted much for now to the CNB statement yesterday. But we still see a stronger CZK as a proxy for paying rates in front of the curve, which may get a boost from the CNB meeting next week given the dovish market pricing.

*Frantisek Taborsky*

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