

FX Daily: Mounting evidence against a March Fed cut

Another surprise drop in jobless claims suggests that a rate cut two months from now looks increasingly unrealistic. Markets, however, remain reluctant to completely rule it out. Today, we'll hear from a few Fed speakers before the blackout period starts. We think the dollar can stay broadly supported into the 31 January FOMC



➔ USD: Rate expectations' gap with data widens

The US jobs markets continues to work against dovish Federal Reserve bets. Yesterday, initial jobless claims dipped again, to 187k. Only once since the pandemic have claims been lower. Continuing claims also came lower than consensus, while housing starts surprised on the upside. Markets remain attached to the prospect of a March cut, now priced with around 50-60% probability, but we really struggle to imagine the Fed cutting in two months' time against the current economic backdrop.

Despite December's moderately above-consensus read, US disinflation has been the benign story for markets, so expect some focus on today's University of Michigan inflation figures, which are expected to be unchanged from last month. Existing home sales for December and TIC flows for

November complete the US calendar today. Today is also the last day for any FOMC member to comment on monetary policy before the blackout period, and Austan Goolsbee, Mary Daly and Michael Barr are scheduled to speak.

We think the dollar can consolidate after the recent gains, continuing to draw some benefits from Christopher Waller's remarks earlier this week, that may have led markets to favour defensive positions heading into the FOMC on 31 January. The only key data release in the US before then is the fourth quarter GDP figures next week, and barring major surprises there, there is no compelling bearish story for the next week or so.

Francesco Pesole

➔ EUR: Fairly valued

European Central Bank President Christine Lagarde will participate in another panel today in Davos – although the ECB is in the quiet period now, meaning that comments on policy are unlikely. The slew of comments from Davos offered further indications that the consensus at the ECB remains less dovish than market pricing.

Markets were unmoved from the minutes of the December ECB meeting yesterday, in which members [steered away from discussing rate cuts](#). Today, the eurozone calendar is empty, and we think EUR/USD can consolidate around 1.8500/1.0900 today. Our short-term fair valued model shows the pair fairly valued at current levels.

Elsewhere in Europe, Riksbank FX sales will pick up again as the reported week is the first one of January, although volumes should be lower than early December as the holiday season wasn't fully over yet. We took that into account in [our estimates](#) for the Riksbank hedging programme to end in early February. Earlier this week, Riksbank's First Deputy Governor Anna Breman warned of risks of inflation revamps, but dropped the tightening bias by saying that there is probably no need to raise rates further. We expect the krona to struggle to find a sustainable appreciation path this quarter as Riksbank FX sales end and the Bank will hardly be able to push a any hawkish narrative further.

Francesco Pesole

⬇️ GBP: Very grim retail sales

UK retail sales for December came in sharply below expectations this morning. The headline print showed a 2.4% year-on-year contraction, while the measure that excludes auto fuel dropped by 2.1% YoY.

The release has thrown cold water on the GBP rally after the CPI-induced gilt selloff this week. Indeed, soft retail sales paint a less optimistic picture for the UK economy, but inflation (especially on services) remains the primary focus of the Bank of England. This means that a further repricing lower in BoE rate expectations would require markets to make a conviction call that the December CPI surprise was just a blip.

This line of reasoning matches ours, and we expect some 100bp of BoE cuts this year. Since we also deem ECB rate cut bets as too aggressive, we are bullish on EUR/GBP into year-end. However, we think that the back up in EUR rates will be gradual and markets will be reluctant to let go of

high-yielding GBP longs so close to the surprise December CPI print. Accordingly, EUR/GBP may struggle to find sustainable support above 0.8600 for now. The 0.8640 is a where 50, 100 and 200-day moving averages converge, and could be the next big resistance.

Francesco Pesole

📉 CEE: More weakness to come

After a busy few days, Friday should be rather quiet in the CEE region. In the calendar today, we only have December PPI data in Poland, where we expect a further drop from -4.7% to -6.0% YoY. However, the FX market still seems to have something to say. EUR/HUF jumped above 382 yesterday for the first time since the start of the year, and as we discussed earlier, we expect more weakness here looking ahead. Rates and FX divergence from the last two weeks combined with the dovish tone of the NBH and political noise from the European Parliament will keep HUF under pressure, in our view. We see stabilisation somewhere around 384 for now, however long HUF positioning may make the situation more tricky in the coming days. On the other hand, we believe that the situation would only start to get uncomfortable for the NBH above the 390 EUR/HUF levels.

The CZK also came under pressure yesterday for the first time following its CEE region peers this week. The markets priced in more CNB rate cuts again despite cautious comments from central bankers and the interest rate differential ticked down a bit against the CZK's favour. We don't expect more weakness here though, and as we indicated earlier this week, 24.700-800 is the range where we see EUR/CZK for these days.

On the other hand, PLN gained some support yesterday for the first time in a week and bounced back below 4.400 EUR/PLN. The lower house of parliament passed a key budget draft and the President indicated support while ruling out the possibility of early elections. This may calm things down for a while, but there are still more than enough open issues that we believe will cause further escalation of political tensions in Poland. Therefore, we remain negative on PLN for the days ahead, although today we could see some gains on the back of the latest news.

Frantisek Taborsky

Authors

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.