

FX Daily: NBH set to tighten further

The uncertainty over the spread of the Delta variant and how local authorities will respond has certainly created a sense of 'short-termism' in FX markets. This week the pendulum has swung pro-risk, but we suspect investors will be reluctant to chase the dollar a lot lower before Jerome Powell's speech this Friday



The Headquarters of Hungary's central Bank

📉 USD: Asian FX regains its poise, pressuring the dollar

The dollar suffered quite a sharp fall yesterday as investors jumped back into risk positions. This swing to a glass-half-full sentiment arrived surprisingly quickly after what seemed a poor environment late last week. Perhaps this environment is best characterised as investors thrashing around for a core theme in thin summer markets - warning that it is dangerous to become too wedded to a view just yet.

Helping the short-term sentiment this week has certainly been the stability/improvement in Asian FX/equity markets. Heavy losses in the likes of the THB and PHP through July and KRW in August were a key driver behind the weak EM environment. Lower cases numbers here and seemingly investors starting to find value in the Asian equity dip have turned sentiment around this week.

The question is whether investors want to add to risk positions ahead of Friday's Jackson Hole event. After all, it seemed like some dovish comments from the Fed's Robert Kaplan on Friday really turned the short-term trend - offering the prospect of a delay in the start of the tapering cycle. We think investors will want to wait to hear on this subject from Jerome Powell on Friday before pushing ahead with another major round of risk-buying, dollar-selling.

The data calendar looks pretty light today and even though overnight markets are keeping the risk-positive mood alive, we doubt investors are ready to push DXY to 92.50 just yet.

➔ EUR: Risk reprieve

The bounce-back in pro-cyclical currencies has provided some support to EUR/USD, yet we should not forget that the euro's status as a funding currency may not be generating the kind of recoveries seen in the past. [We had felt](#) that 1.1750 could be the top of the EUR/USD range this week - thus today's risk positive mood could be a stern test of that view.

Locally the focus will be on the revisions to 2Q21 German GDP figures - just in at an upwardly revised 1.6% QoQ and largely driven by government consumption. However, until the ECB acknowledges that inflation is emerging firmer than their forecast (we see ECB minutes on Thursday), we doubt the EUR can enjoy much independent local support.

Indeed, investors may take the opportunity of the recent uptick in EUR/USD to reset EUR-funded positions in EM - such as short EUR/MXN. Here the MXN has been hit hard by a fire that has shut a quarter of Mexico's oil production. Yet MXN should enjoy good demand on dips and we could see EUR/MXN heading back to 23.50 after its recent spike.

➔ GBP: Trading the ranges

GBP enjoyed a good bounce yesterday - and it wasn't clear why. Perhaps it was the sharp rise in commodities that lifted the Basic Materials components in equity benchmarks - and the FTSE having a high weight to these.

There is no UK data today and GBP will probably be left to thrash around in ranges such as 0.8530-0.8600 for EUR/GBP and 1.3600-1.3750 for Cable.

➔ HUF: NBH set to hike the base rate another 30bp today

Hungary's NBH is widely expected to raise its policy base rate by 30bp to 1.50% today. This will be the third consecutive monthly hike of 30bp as the NBH takes 'firm steps on a monthly basis' to ensure price stability. As we discuss [in our meeting preview](#), inflation is running ahead of NBH projections as is growth.

The question today is whether we will see another hawkish hike - i.e. retaining the word 'monthly' to manage expectations for another 30bp hike in September. That certainly cannot be ruled out, but the market is going into this meeting long HUF (short CZK/HUF has been a popular trade) and also pricing the base rate for 2.00% early next year.

It may be difficult for rate markets to sell off too much further given what is priced in and unless the NBH wants to convince markets that the terminal rate may be in the 2.25/2.50% area, we think it may be difficult for EUR/HUF to push down to 347, let alone 345 on today's meeting. In particular, we think the NBH will prefer to wait for the release of its September inflation report

before its next major communication. We'll also see what the NBH today has to say about its QE scheme, where its stock of assets is approaching the key HUF3trn threshold.

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