

FX Daily: Peak? What peak?

Everything is pointing to the fact that today's well-telegraphed 25bp hike by the Fed will be the penultimate move before ending the cycle. However, Chair Powell and the FOMC may see little interest in sounding materially less hawkish just yet. Ultimately, a push-back against a pivot and rate-cut speculation could hit risk assets and lift the dollar today



Federal Reserve Chair
Jerome Powell

USD: Hawkish Fed can lift the dollar

The dollar enters FOMC day after having shown some resilience over the past few sessions, which was likely the consequence of some defensive positioning ahead of key central bank meetings, which kept risk assets capped. Still, the last important piece of data before the Federal Reserve announcement – yesterday's Employment Cost Index – offered more reasons to think the Fed is indeed close to the peak. Labour costs eased for a fourth consecutive quarter in 4Q, moving from 1.2% to 1.0%, the same levels as the fourth quarter of 2021.

This is likely easing some concerns in Washington about inflation stickiness, and underpins a scenario where slowing price pressures favour less hawkish rhetoric. The question is whether such unwinding in the hawkish narrative will already emerge in today's FOMC announcement. We doubt that.

As discussed in our [FOMC preview](#), we expect a 25bp rate hike today, which is the consensus view and is fully priced in by the swaps market. We think that Fed Chair Jerome Powell and his colleagues simply have little interest in sending strong signals that they are indeed close to the peak, which only risks generating a premature fall in interest rates. A reiteration that ongoing rate increases remain appropriate, inflation is high and that the jobs market remains tight despite slowing growth, seems to us the most likely content of today's communication "package" by Powell.

He will most likely be asked about the current market pricing for around 50bp of easing in the second half of the year. Using the same rationale, Powell still has all the interest in pushing back against rate cut speculation. In practice, we suspect the Fed will end up cutting more than 50bp as the US economic slack deepens, but that is not a story for today's announcement.

So, we are in the camp of expecting Powell to maintain his hawkish rhetoric despite this appearing less appropriate given the backdrop of slowing inflation and growth. This outcome may ultimately have some negative implications for risk and give the dollar some support, as bets on a pivot, and potentially on rate cuts, are scaled back. Any communication missteps or deliberate dovish tilts, on the other hand, can surely revive that dollar bear trend that appears to have halted lately.

We also have some US data to watch today: ISM manufacturing, ADP payrolls and JOLTS jobs openings. Substantial surprises on those releases are likely needed to drive major dollar moves ahead of such a big event like the FOMC.

Francesco Pesole

📌 EUR: Inflation surprise already priced in?

EUR/USD will inevitably be heavily impacted by the post-FOMC reaction today. In line with our view for a positive impact on the dollar, we think the 1.0800 support could be heavily tested after the Fed announcement.

Before that, however, all eyes will be on the eurozone inflation figures, which should show more stickiness than previously thought after evidence of persistent price pressure in Spain and France. We suspect much of this inflation story has now been priced in, and a still quite hawkish pricing for European Central Bank tightening (150bp of hikes by June) suggests the room for further increases in rate expectations – and by extension, for another big ECB-driven EUR rally – has shrunk for now.

We think that EUR/USD will ultimately come out weaker from these two days of central bank activity (here's our [ECB market preview](#)). An exploration of the 1.0700-1.0750 range is surely possible in the near term, even though the longer-term outlook keeps pointing to a dollar decline and EUR/USD strength.

Francesco Pesole

📌 GBP: Downside risks from a hawkish Fed

Stronger ECB rate expectations are likely to be blamed for the strengthening in EUR/GBP beyond the 0.8800 level. As discussed in the EUR section above, we think there is now less scope for the ECB to push the euro even higher, which means more fuel to the EUR/GBP rally may be mostly a function of risk sentiment rather than monetary policy divergence.

Indeed, since the pound tends to be more sensitive to global risk sentiment than the euro, the risks are skewed to the upside for EUR/GBP today given our baseline scenario for a hawkish Fed weighing on risk assets. Cable may drop to the 1.2200 mark today.

Francesco Pesole

📌 SEK: Krona undermined by domestic woes

The Swedish krona has been a negative standout in the G10 space over the past few days, as unstable risk sentiment offered a breeding ground for rising bearish bets linked to a worsening domestic outlook in Sweden. We analyse this theme in more detail in "[Sweden: Krona increasingly pricing in domestic woes](#)". In short, EUR/SEK is currently 2.5% overvalued in the near term as markets appear to be pricing in the increasing likelihood of a pessimistic scenario for the Swedish property market and the economy.

Since we don't believe the risk of a black swan scenario in Sweden has materially increased, we think that SEK will recover gradually over the coming months. Looking at the very short-term however, SEK's sensitivity to risk sentiment still puts it in a vulnerable position today ahead of the Fed announcement.

EUR/SEK is currently trading around 3% below its historic highs (11.68 in 2009), and risks that those levels will be tested in the short-term (although not our base case) have admittedly risen lately. We still target sub-11.00 levels before the summer, as recently discussed in our [EUR/SEK scenario analysis](#).

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