

FX Daily: Quarter-end flows give some support to the dollar

The dollar had a good run yesterday, which we believe was due to some quarter-end rebalancing effect kicking in and short-squeezing (especially in USD/JPY). Ultimately, US data needs to offer direction to the FX market: we'll closely monitor jobless claims today. Elsewhere, we expect a 25bp rate cut in Switzerland and a surprise 50bp cut in Mexico



The Swiss National Bank is widely expected to cut rates this morning

➔ USD: Focus on jobless claims

The dollar rallied across the board yesterday as quarter-end flows probably favoured a broad positioning adjustment. Based on the latest CFTC figures, we calculate that the dollar was in net-short territory against the other reported G10 currencies on 17 September, but that amounted to a relatively small 4% of open interest. The yen was, however, one of the largest speculative longs (+29% of open interest), and it is not surprising to see some squeezing in the pair around the turn of the quarter. Incidentally, the rates/macro story may not get much more negative for USD/JPY at this stage, given markets are fully pricing in 75bp of Fed cuts over the next two meetings.

Today, the US data calendar is quite busy. The third GDP/PCE second-quarter print should not

surprise, and jobless claims may be the more market-moving release along with August's durable goods orders and the leading index. Last week, initial claims unexpectedly dropped from 230k to 219k, and continuing claims were down from a downwardly revised 1843k to 1829k. The question is whether that was a spurious figure or not: another stronger-than-expected print may trigger speculation of a robust jobs report next Friday, all to the dollar's benefit.

On the Fed's side, Chair Powell will give pre-recorded opening remarks, and there is a long list of other speakers: Collins, Bowman, Williams, Barr, Cook and Kashkari. There should be some extra colour on each member's Dot Plot submission.

The quarter-end flows may continue to offer the dollar some modest support today, barring negative US data surprises, but the positioning picture did not look that heavily skewed to dollar shorts to justify large readjustments. Ultimately, stronger US data is needed to convince markets to abandon 50bp cut bets. That may not happen overnight, and there is still a substantial risk the dollar will stay capped into the US election.

Francesco Pesole

➔ EUR: Rangebound swings ahead

The support from China's stimulus story waned yesterday, and EUR/USD's exploration above 1.1200 proved to be very short-lived amid quarter-end USD buying. We will likely see a bit more range-bound swings around the 1.110-1.120 area in the near term unless US data offers clearer direction to markets. A 2-year EUR:USD swap rate gap tighter than -100bp (now at -95bp) is still arguing against a major correction in the pair.

The eurozone calendar is rather quiet today, but there are three key ECB speakers. President Lagarde will give a welcome address at a conference (but may not touch upon monetary policy), while the dovish-leaning Guindos and hawkish-leaning Schnabel are due to speak later this afternoon.

Elsewhere in Europe, the Swiss National Bank is widely expected to cut rates this morning. Economists' consensus is quite strongly favouring a 25bp reduction, while the market is pricing in 35bp. As discussed in our [SNB preview](#), we expect a 25bp move with more explicit FX intervention references, which can lead to CHF outperformance today.

Francesco Pesole

⬇️ MXN: Banxico to risk a 50bp rate cut

In a highly anticipated event, Banxico meets today to set the policy rate. The vast majority of economists favour a 25bp rate cut taking the policy rate to 10.50%. However, financial markets price a 50% chance of a 50bp rate cut. The thinking here is that Banxico, like the Fed, could deliver a precautionary large cut now that it has switched away from inflation and towards growth concerns. Additionally, some see this as a window of opportunity for a large cut before the US elections, and an uncertain future for trade policy closes the window for such a large reduction later this year.

At the same time, the peso remains vulnerable to the political story. After securing judicial reforms, the government is trying to push a large hike in the minimum wage through Congress. On the former, the rating agency Moody's is now saying that the constitutional reforms could directly

impact Mexico's sovereign credit rating. Moody's currently has Mexico at Baa2, (S&P at BBB) and Mexico's five-year CDS at 120bp is already trading towards a one-notch downgrade.

We think Banxico could risk a 50bp rate cut today to ease high real rates quickly. However, the peso would suffer and our near-term bias for USD/MXN is 19.75 and above 20.00 should a 50bp cut be delivered today.

Chris Turner

➔ CZK: CNB cuts rates but provided nothing new

The Czech National Bank (CNB) reduced interest rates by 25bp to 4.25%, as anticipated. The CNB's press conference offered little new information, disregarding the Federal Reserve's decision and refraining from commenting on market pricing.

Of course, the Fed rate cut and dovish global outlook will be visible in the November forecast in a downward revision of the rates path. On the other hand, the next catalyst is September inflation, which only mechanically points to 2.6% based on the previous deviation from the CNB forecast. That's also what some of our numbers show, despite the drop in fuel and energy prices, which would bring the CNB to an uncomfortable level given another base effect jump in December, raising the chance of inflation returning to 3%. This is why our economists expect a pause in December. I don't think we're that far yet, but the September inflation number (in two weeks) will be key and communication in November may change accordingly.

From that perspective, we face a hawkish risk over the next two months, while the market leans dovish in our opinion. Paying CZK rates seems challenging in the current environment, but an inflation print could change that. Given this hawkish stance, we still anticipate EUR/CZK to decline in the short term, as suggested by the current rates differential.

Frantisek Taborsky

Authors

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Chris Turner

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

chris.turner@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

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