

## FX Daily: Risk sentiment too fragile for a big dollar correction

The dollar is restrengthening this morning after a soft start to the week. Still, the data flow is not endorsing any unwinding of Fed hawkish bets and further improvements in risk sentiment may become harder to sustain. Today, keep an eye on French and Spanish inflation, and on the Norges Bank FX purchases announcement



UK PM Rishi Sunak and EC President Ursula von der Leyen at a press conference on a new post-Brexit trade arrangement for Northern Ireland

### ➔ USD: Not trusting a big rebound in risk sentiment

The dollar is trading stronger across the board this morning after suffering a correction yesterday that was due to a rebound in global equities and probably some month-end flows. We have recently highlighted how the narrative for the greenback has turned more structurally supportive, meaning that a return to a USD downtrend will take time and may only be very gradual. That is unless incoming data start painting a different picture for the US economic and inflation outlook, which would force some unwinding of recent hawkish bets on the Fed.

This week's key data releases will be the ISM surveys, and in particular Friday's ISM services index, which served as a benchmark for the rapid swings in US growth sentiment over the past two prints. Still, we have some interesting data points to monitor today. The Conference Board consumer confidence indicator is expected to rise after a small contraction in January, the Richmond Fed

Manufacturing Index is also expected to improve, while wholesale inventories may hold at 0.1% month-on-month in the January read.

US data may not move the market dramatically today, so the dollar may be primarily driven by global risk sentiment. We struggle to see a material and sustained recovery in global equities in such a worsening valuation environment, and with data still supporting the Fed's hawks for now, the dollar's short-term bias still appears neutral/modestly bullish. A return above 105.00 in DXY seems possible in the ISM services release on Friday.

*Francesco Pesole*

## ➔ EUR: Regional CPI figures in focus

Inflation figures for January are the main highlight of the week in the eurozone, and today's numbers out of France and Spain may already start moving the market. Remember that inflation rebounded in both of those countries in January, which underpinned the recent ECB hawkish narrative. Today, consensus sees a stabilisation in the EU-harmonised French inflation at 7.0% and a slowdown from 5.9% to 5.7% in Spain.

Unless we see a material surprise on the downside – that would suggest a more widespread easing in price pressures across the eurozone – today's regional CPI figures may fail to dent hawkish expectations for ECB tightening. Markets are currently pricing in around 130-140bp of tightening before reaching the peak. This could offer some floor to the euro, and we expect any re-strengthening of the dollar to see high-beta commodity currencies more at risk than the euro for the time being. Still, the risks of 1.0500 being tested in the near term remain elevated.

*Francesco Pesole*

## ➔ GBP: Impact of new Northern Ireland deal may be only short-lived

The pound is one of the best-performing currencies since the start of the week after the confirmation of a new UK-EU deal on Northern Ireland. The "Windsor Framework" reviews some sticky points of the existing NI protocol, essentially reducing the number of checks on trade between Northern Ireland and the rest of the UK. The direct impact on the UK economy should not be significant, but markets are probably welcoming the conciliatory steps in UK-EU trade relationships.

It seems hard, however, that the pound will find sustained support simply based on the new NI deal. The central bank story should instead remain the most central driver of GBP, and given the lack of data today, markets will watch three Bank of England speakers today: Jon Cunliffe, Huw Pill and Catherine Mann. A 25bp move in March is fully in the price, and the debate appears to be much more centred on whether the Bank will need to keep tightening beyond March: markets are definitely swinging on the hawkish side, expecting a total of 80bp of tightening before reaching a peak.

For now, the global central bank narrative and improving UK data are not giving many reasons to unwind such hawkish expectations, and the pound may continue to prove more resilient than other pro-cyclical currencies.

Francesco Pesole

## ➔ Scandinavia: Grim data in Sweden and Norges Bank FX sales in focus

Swedish growth data came on the soft side this morning. The second print of fourth-quarter data showed a larger contraction (0.9%) than previously estimated (0.6%). Although this is clearly backward-looking data, the ongoing tightening by the Riksbank, a very fragile housing market and high inflation continue to point to a rather grim economic outlook in Sweden. Remember that we are approaching the end of wage negotiations in Sweden, which may suggest even more monetary tightening will be required.

We see the recent good performance of SEK as unsustainable unless data start pointing at an improvement in the growth outlook. A return to 11.10+ in EUR/SEK (paired with elevated volatility) is a tangible possibility in the coming weeks.

In Norway, we'll keep a close eye on Norges Bank's announcement of daily FX purchases for the month of March this morning. Net purchases were increased to 1.9bn NOK for February after three months of reductions from the 4.3bn peak in October 2022. With NOK being the worst-performing currency in G10 this year and risk sentiment instability continuing to pose downside threats (remember the krone is the least liquid currency in G10), some support in the shape of lower FX purchases may come from Norges Bank today. This may avert – or at least delay – another decisive break above 11.00 in EUR/NOK.

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