

## FX Daily: Short-term dollar bearishness remains unconvincing

We remain a bit reluctant to chase the dollar lower. The greenback still has to catch up with recent market dynamics – higher US rates in particular – and the scope for further dovish repricing in the USD curve is not broad. This week's US CPI is undoubtedly a risk event, but we don't see a EUR/USD move above 1.1000 as being very sustainable just yet



### USD: Room for a rebound

Last week saw the dollar trade on the soft side amid mixed data from the US. The latest and most important release, the US payrolls figures for June, came in a bit weaker than expected, but the jobs market likely remains too tight for the Fed to backtrack on a July hike. After all, the headline print was solid (+209k) and with wages remaining high and unemployment moving lower, there aren't many strong dovish arguments to be extrapolated from the June jobs report.

We are still reluctant to chase the dollar lower from this point – not particularly because we expect incoming data (US CPI above all) to surprise on the upside, but because the dollar still has to catch up with some recent market dynamics. Front-end US treasuries arrested their selloff, but remain very close to 5.0%, and 10Y UST are at the 4.0% benchmark level. Equities have also shown some signs of instability since the start of July. All of this should, in theory, put the dollar in a solid position to rebound from the current levels – especially given there isn't much room for a further

dovish re-pricing in the USD swap curve. That currently factors in 35bp of tightening to the peak, still short of the 50bp signalled by the Fed in the latest dot plot.

The big risk event for the dollar this week is the June inflation report on Wednesday. Our economist expects a consensus 0.3% month-on-month core read, which should keep providing encouraging news on the disinflationary story – but should still fall short of tweaking the Fed narrative or convincing markets to price out a July hike.

A downside inflation surprise could see DXY test the 101.00 April lows, but we think that the dollar could instead find some support into the CPI release and stabilise in the second half of the week. Today's calendar includes some Fed speakers: Michael Barr, Mary Daly, Loretta Mester and Raphael Bostic.

Elsewhere, we expect the Bank of Canada to hike by 25bp this week. This is far from a consensus view, with the pool of economists split between a hold and a hike and markets pricing in around 67% of implied probability of an increase. We explain our reasons in our latest Bank of Canada [meeting preview](#).

*Francesco Pesole*

## 📉 EUR: Could trade above 1.10, but a correction looks more likely

EUR/USD will have the chance to break above 1.10 this week, although we struggle to see the pair trade sustainably above that benchmark level just yet. The gap between market pricing on Fed tightening and the FOMC dot plot continues to leave room for hawkish repricing, while the EUR curve fully prices in two more hikes in the eurozone. Indeed, the OIS curve shows the September meeting has 38bp priced in and more upside surprises and/or hawkish ECB commentary could help markets fully price in a hike in September – but there is currently a smaller gap between markets and central bank communication in the eurozone compared to the US.

Our short-term financial fair value model shows that EUR/USD should be trading around 1.0800 based on current market conditions. As mentioned in the dollar section above, the dollar still needs to catch up with the rise in USD rates and that can prove to be a hurdle when attempting a decisive break above 1.10.

On the euro side, markets will watch the ZEW index this week after a long series of disappointing forward-looking indicators in the eurozone. On Thursday, the European Central Bank (ECB) minutes from the June meeting will be published.

We expect mostly USD-driven moves in EUR/USD this week, and see a greater risk of some pull-back towards 1.0800 rather than trading sustainably above 1.1000 – which could however be possible should US CPI surprise on the soft side.

*Francesco Pesole*

## 📉 GBP: Tomorrow's wage data are key

With a month to go until the next Bank of England meeting, policymakers will be watching regular pay growth (average earnings excluding bonuses) tomorrow, which has picked up again lately. The

question is whether that's solely down to firms implementing the 10% increase in the National Living Wage, or a genuine increase in pay pressures. Assuming it's at least partly the former, we think we could get a fractional fall in the annual rate of pay growth in the May reading. Unless the CPI shocks on the upside again on July 19, then the Bank of England could be happy with a 25bp hike in August.

Markets are pricing in 44bp for August and 145bp in total, which leaves ample room for a dovish repricing to hit sterling should data surprise on the downside. EUR/GBP is trading around recent lows and may be facing some upside risks to 0.8600+ this week.

*Francesco Pesole*

## CEE: Recovery after last week's sell-off

This week, we're looking at a lighter calendar. Today we will see the June state budget result in Hungary, which shows the risks of additional bond issuance in the first five months. Wednesday will see the release of labour market data in Romania. On Thursday, June inflation in the rest of the region will be published. In the Czech Republic, we expect a fall from 11.1% to 9.6% year-on-year, slightly below market expectations. In Romania, a further fall from 10.6% to 10.2% YoY is expected. Final inflation numbers will be released on Friday in Poland and current account numbers will also be published in Poland and the Czech Republic.

We saw a significant sell-off in the FX market in the region last week. In our view, the driver was the global story and repricing as local factors remain rather positive. If the global story calms down as indicated by the morning open, we could see fresh gains and a rally in the region this week. Last week's sell-off has eased the steam from overcrowded market positioning in CEE FX, which should facilitate a recovery. We believe that the massive carry will attract buyers again, which should benefit the Hungarian forint the most. We see the next level below 380 EUR/HUF, which should confirm the recovery in FX and attract further inflows. Nevertheless, we're remaining optimistic for the whole region for this week.

*Frantisek Taborsky*

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