

FX Daily: 'Something's got to give' - including the dollar

In what we thought was going to be a quiet week for FX, the dollar has extended its recent losses. Driving those losses have been Fed speeches welcoming signs of slowing economic momentum and lower inflation. Bullish steepening of the US yield curve has come earlier than we thought, as has the dollar sell-off. Look out for US GDP revisions and German CPI today



Fed member Christopher Waller pushed back the market's aggressive pricing of easing in a speech on Tuesday

➔ USD: Fed hawks soften their stance

We had not been expecting it this early, but some of the Federal Reserve hawks now seem to be happy to express a view that the inflation battle is won. Driving the bond market rally and dollar sell-off yesterday was a speech and comments from Fed hawk, Christopher Waller. His speech '[Something Appears to Be Giving](#)' is well worth a read. On 18 October, he suggested that something had to give in that robust US growth and slowing inflation could not co-exist. He concluded yesterday that it was the pace of economic growth that was giving.

Signs that inflation is becoming much less of a concern to investors can be seen in US five-year inflation swaps priced five years forward. These have dropped to 2.51% from 2.79% in mid-October

- when the dollar peaked. While we had not been expecting it this early, we have been glad to see that the dynamics of our 2024 call for a weaker dollar are playing out - in that bullish steepening of the US yield curve has gone hand-in-hand with a dollar sell-off. The US 2-10 year Treasury curve has bull-steepened 12bp this week.

Looking ahead, the big question is whether this is the start of the big cyclical dollar decline we had envisaged developing through the first half of next year. This softer stance from Fed hawks warns that it is probably better not to fight the recent trend. And Fed Chair Jerome Powell's 'Fireside chat' on Friday afternoon will now be eagerly awaited, as will tomorrow's release of the core PCE deflator for October - expected at calm 0.1/0.2% month-on-month readings for headline and core, respectively.

For today's session, the focus will be on revisions to the 3Q23 US GDP data, which initially printed at 4.9% quarter-on-quarter annualised. A modest upward revision is expected. And there are no scheduled Fed speakers until after the European close. DXY has fallen more quickly than we had been expecting but has support around the 102.50 area. We suspect we could see a more consolidative environment today, but the threat of more dollar losses on soft inflation data tomorrow warns that sellers may be lining up at 103.50 now.

Chris Turner

➔ EUR: German CPI in focus

There seems an emerging narrative out there that if the European Central Bank is going to be cutting at the same time as the Fed next year, why does EUR/USD need to rally? Well, yesterday's Fed remarks prompted a large 14bp narrowing in EUR:USD two year swap differentials which serves as a reminder that if and when the Fed gets ready to ease policy, market expectations will swing a lot more on USD rates than EUR interest rates. For example, one could argue that US two-three year market interest rates could fall another 80bp quite quickly if the narrative were to shift towards the Fed taking policy back to the more neutral 3% area.

For today, the focus will be on German CPI - expected to slow to 3.5% from 3.8% year-on-year and presage a softer eurozone inflation release tomorrow. EUR/USD has nudged above 1.10 and now has good intra-day support at the 1.0965 area. Unless we see massive upside revisions to 3Q23 US GDP data today, we doubt EUR/USD needs to come a lot lower. And 1.0965-1.1065 could well be the holding pattern into tomorrow's US PCE inflation data.

Elsewhere, sterling is doing quite well. Cable has resistance around the 1.2720/2740 area and may struggle to break that today unless Bank of England Governor Andrew Bailey has some very hawkish remarks to make later today in response to government plans for looser fiscal policy.

Chris Turner

⬆ NZD: New Zealand bucks the dovish trend

While keeping its official cash rate (OCR) unchanged at 5.50% overnight, the Reserve Bank of New Zealand (RBNZ) did buck the globally dovish trend of central bankers by raising its forecast profile by 40-50bp over the next three years. Driving those revisions was the fact that demand growth was slowing by less than expected - largely due to population growth. The New Zealand dollar liked what it heard from the RBNZ and promptly rallied 1%.

We are positive on NZD/USD into next year - largely on the turn in the US dollar story. But a more hawkish than expected RBNZ can't hurt either. Let's see whether NZD/USD has the legs to push onto resistance at 0.63 in early December.

Chris Turner

CEE: CNB will decide on financial stability toolkit

Today's calendar in the region is almost as empty as in the previous two days. It will be more interesting tomorrow with Polish inflation on the calendar. Today at least, the financial stability meeting of the Czech National Bank may excite the markets. At 3.45pm local time, we will see the decision and press conference of the bank board. The CNB has already cut the countercyclical rate for capital requirements for the banking sector twice this year and it is possible we will see the same today. At the same time, another loosening of mortgage limits is on the table. On the other hand, recent data shows a decent recovery of the credit market in the Czech Republic despite stable central bank rates. So the question is whether or not the bank board will want to loosen conditions more today. At the same time, journalists will have a chance to ask about the current view of the situation and we might even get an update on monetary policy.

Despite the empty calendar, the FX market has been busy. EUR/USD has hit 1.10 and CEE FX has welcomed it with open arms. All three major currencies in the region rallied by 0.35-0.55% to reach new record highs. However, only in the case of Poland's zloty do we also see support on the rates side, which gives us confidence that the new gains are longer-term in nature, and we can expect more. On the other side is the Czech koruna, where FX is still benefiting from last week's paying flow in rates, but we are rather sceptical about the days ahead. Over the last two days, the market has seemed unwilling to price out more rate cuts but we will see more data from the economy soon, which in turn should support new CNB rate cut bets. Therefore, we remain negative on the CZK. Somewhere in between in this story is Hungary's forint where rates remain volatile but follow the core move. Thus, the interest rate differential is basically the only one stable in the region. The view here is not so clear in terms of what to expect next. Rates still point to a weaker HUF but sentiment and EUR/USD are clearly positive. So we are likely to see somewhat of a EUR/HUF pullback higher (though some gains should be retained by the HUF) and a continuation of the rally later.

Frantisek Taborsky

Author

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

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.