FX Daily: Sterling makes its move

Sterling has seen some noticeable underperformance after dovish comments from MPC internal members. We've also just had some comments from the ECB hinting that its policy moves may not be as independent of the Fed after all. Today, we'll be focusing on any modest improvement in the eurozone PMIs. Over in Hungary, a slower pace of easing is expected

USD: Going steady

The dollar has returned to consolidation mode after last week's run on the upside. Friday's March core PCE deflator release remains the biggest number of the week and will determine whether US short-dated yields need to rise any further. Indeed, many investors might find US two-year Treasury yields very attractive at 5% given the dangerous geopolitical backdrop.

For today, we doubt the US April PMIs or new home sales data will have much impact on the dollar. And, at the margin, it may be the threat of large-scale Asian FX intervention that is preventing investors from adding any more dollars to already crowded long dollar positioning.

DXY is set to consolidate in a 105.75-106.50 range, but a bullish bias remains.

Chris Turner

EUR: De Guindos rows back on the divergence theme

Some headlines have emerged this morning following an interview given to Le Monde by the European Central Bank's vice president, Luis de Guindos. He has effectively said that a June rate cut from the ECB is a done deal (barring new shocks of course), but also that what the Fed does is crucial for the global economy and the euro area. He adds that EUR/USD is a channel through which Fed policy affects the euro area and that the ECB will take this into account.

It may be too much to read this as gentle ECB pushback against recent EUR/USD weakness. And our team have written on the subject of how much EUR/USD weakness would be required to have the ECB think twice about a June rate cut. However, the tone of the piece did not seem to be one emphasising ECB independence in decision-making. The bigger implications for the euro may actually come from communication about the scale of the forthcoming easing cycle, which looks quite opaque. For reference, the forward ESTR curve prices the terminal rate in two to three years' time at around 2.25%, which seems about right given the discussion over the real neutral rate in the eurozone being something like 0.25%.

For today, we are looking for some further modest advances in flash PMIs for the eurozone, Germany and France. Given that weak readings here did some damage to the euro last autumn, a modest recovery now could offer the euro a little support. However, we see that expressed more through EUR/GBP (see below) than through EUR/USD.

Technically, EUR/USD looks like it is consolidating before breaking to a new low. If that is the case, expect resistance at 1.0680/10700 to limit intra-day gains.

Chris Turner

In Sweden, Riksbank Governor Erik Thedéen speaks this evening. In his latest comments from 8 April, he stressed the risks of a weaker krona for inflation, and (implicitly) potentially smaller room to cut interest rates. Since then, the trade-weighted SEK has depreciated by another 1.5%. The krona is the worst-performing G10 currency since the start of the month and its decline against similar high-beta currencies like AUD, NZD and even NOK shows that dovish bets on the Riksbank have done some damage. Any comments from Riksbank officials from now until the 8 May meeting will be key in directing market expectations. Our perception was that EUR/SEK at 11.60 was not consistent with a May cut – but with now 18bp in the price, the Riksbank may think it can get away with a relatively hawkish cut without damaging its currency. Unless Thedeen signals the opposite, SEK remains less attractive than its high-beta G10 peers in the short run.

Francesco Pesole

GBP: Internal MPC members get sterling rolling

Sterling saw some decent follow-through selling yesterday on the back of comments made on Friday by the Bank of England's deputy governor, Dave Ramsden. As our UK economist James Smith discusses in this article, it now seems we are hearing from BoE insiders – i.e., not the more vocal external members – that conditions are falling into place for a rate cut. This has shifted the probability of a June BoE cut close to 50% from 25% a week ago.

As we highlight in the linked article, GBP/USD has been enjoying quite a steady relationship with the one-year GBP:USD swap differential. If that differential were to move out by a relatively aggressive 50bp in the dollar's favour, this would suggest that GBP/USD should be trading near 1.21. That looks to be the direction of travel – a direction that might get a nudge today from BoE Chief Economist Huw Pill, who speaks at 1:15pm CET. Before that, however, sterling could face some modest upside risks from the April flash services PMI release (10:30am CET), which has been holding up quite well.

EUR/GBP broke decisively from a three-month trading range yesterday. The FX options market bought into the breakout, where implied volatility was bought up, and the risk reversal skews went bid in favour of euro calls and sterling puts. We have had medium-term EUR/GBP targets in the 0.87/88 region for some time, and yesterday's move finally suggested a new trend may be emerging.

Chris Turner

HUF: NBH expected to slow the pace of easing

The National Bank of Hungary meets today. Our local economist, Peter Virovacz, is looking for a 50bp cut in the key rate, taking it to 7.75%. This marks a slowdown in the pace of rate cuts compared to the two prior adjustments of 100bp and then 75bp. Given a challenging external environment, any hints of larger or deeper rate cuts are probably a forint negative. And here, Peter is interestingly looking at a terminal rate of 6.75% this summer compared to market pricing of the low point in the cycle this year at around 7.25%.

Elsewhere, at 09:00am CET today we will hear from Czech National Bank Governor Ales Michl. Let's see if he drops hints about the size of the next CNB rate cut on 2 May. We are looking for another 50bp rate cut.

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