FX Daily: Stretched positioning may be sterling's only friend

It is a very busy day for central bank policy meetings in Europe. There are probably some downside risks to the euro and sterling from these event risks, but stretched short positioning may prevent a larger sterling sell-off. We also see some downside risk to the CZK on today's local central bank meeting, where a lower inflation profile could be discussed

A 25bp rate cut is expected at today's Bank of England meeting

USD: CPI should not be a game-changer

The DXY dollar index remains supported above 98.00. Events this week have so far had little meaningful impact on the dollar, including the speech from the Fed's Chris Waller yesterday. He was generally dovish, citing the soft labour market and outlining that the policy rate was still 50-100bp above neutral. Yet he was in no rush to cut rates and the chance of a January Fed rate cut is still priced at just 25%. We favour a cut in March.

Unless the weekly jobless claims number spikes today, we doubt the US data will move the dollar much at all. That includes a reading on the delayed CPI data, where the November headline figure is expected to be 3.1% year-on-year, feeding into the sticky inflation narrative. Yet that looks unlikely to prompt a major re-assessment of the Fed trajectory.

We suspect DXY will be dragged around by the European central bank meetings today. Some downside risk to European currencies could mean that DXY corrects back to the 98.80 area.

Chris Turner

EUR: ECB reality check could weigh

Today's ECB meeting will take centre stage in FX markets. After a hawkish turn last week, investors will be looking to see whether that gets backed up with forecast and rhetoric changes today. Examining those forecasts, the CPI profile is likely the biggest risk to the euro. In September, the ECB's forecasts for headline and core inflation were: 2026, 1.7/1.9, and 2027, 1.8/1.9. The delay in the ETS2 carbon tax could wipe 0.2% off the 2027 headline forecast and a new 2028 CPI forecast somewhere near 1.8% could prove awkward for ECB President Christine Lagarde as she has to explain away an inflation undershoot. There will also be a focus on the growth forecasts: 25/26/27 at 1.2/1.0/1.3 and perhaps some modest upward revisions.

The above could see the short-end of the euro interest rate curve handing back some of the rise in yields seen last week. And that could prompt a brief sell-off in EUR/USD to the 1.1680/1700 area. However, as we mentioned yesterday, there are some large EUR/USD option strikes rolling off in the 1.1750/1800 area over the coming days, which could have an influence on thinning year-end markets.

Elsewhere, we have Riksbank and Norges Bank rate meetings. After September's rate cut to 1.75%, the Riksbank is positioning itself as on hold for a prolonged period. It is probably a little too early for the Riksbank to be encouraging ideas of a hike, but the market will be focusing on the policy rate forecasts, which in September had the policy rate unchanged in 2026, but one hike each in 2027 and 2028. Any upward revision here could give the SEK a brief boost.

In Norway, the Norges Bank seems in no hurry to cut the 4.00% deposit rate. We will also see new policy rate forecasts today. In its most recent Monetary Policy Report, the Norges Bank had one cut per year between 2026-28, with the 2026 cut expected in the second quarter. The market prices 30bp of rate cuts by the May meeting, and it is hard to see the need for Norges Bank to bring that forecasted 2026 rate cut forward to the first quarter. EUR/NOK has already been rallying on the soft oil story, and we expect it to continue to meet good offers above 12.00.

And finally, let's keep a close watch on EUR/HUF. Long forint has been one of the most popular carry trades this year. A big unwind is underway after this week's dovish shift from the National Bank of Hungary. This may have further to run.

Chris Turner

GBP: Positioning might limit the impact of a dovish cut

The Bank of England announces the policy rate at 1300CET today. A 25bp rate cut to 3.75% is widely expected. Consensus is probably for a 5-4 vote as Governor Andrew Bailey switches to the dovish camp, though the risk is of a 6-3 vote, making this a dovish rate cut. Those risks have increased after yesterday's pleasant surprise in November inflation – including a sharp fall in food prices. We look for further rate cuts in February and April, whereas market pricing only sees one cut during that period.

The above all sounds moderately sterling negative. The problem we have is that speculative positioning remains substantially underweight sterling already. Data published last night from the CFTC, covering activity after the November budget, shows asset managers still running a short position worth 38% of open interest (total positioning). Those levels remain on par with the shortest sterling positioning we have seen over the last five years.

The above could create a game plan where EUR/GBP spikes to the 0.8820/8840 area on the BoE rate cut, but comes all the way back – perhaps even to 0.8750 – on the ECB event risk, which takes place 1-2 hours after the BoE announcement and press conference.

Chris Turner

CZK: Lower inflation path provides dovish risk

The Czech National Bank will leave rates unchanged at 3.50% today. The last meeting of the central bank this year will not bring a new forecast and the focus will be on forward guidance for next year. The last few weeks have brought several changes to the CNB inflation forecast. On Tuesday this week, the government decided to subsidise part of the regulated component of energy prices. Added to this are lower market prices for households and the postponement of ETS2 from 2027 to 2028, or rather, the new government's approach of not implementing the legislation at all. This pushes the CNB forecast down by around 0.6pp for headline inflation over the next two years, moving it below the CNB target. Although we believe it is too early for the CNB to change its tone, we see a little dovish risk for today's meeting.

The market has outpriced almost all rate hikes next year in recent days, but leaves one hike in 2027. We believe that even these bets will come under pressure sooner or later and the market should price in the low probability of cuts in this horizon, creating more downside for the CZK in the short term. Yesterday's global risk-off sentiment and CZK rates rally pushed EUR/CZK to 24.400, slightly above our indicated range of 24.300-350 earlier this week. We see stable FX as the most likely for today's meeting after recent moves. However, the risk remains that some dovish signal from the CNB after a change in the headline inflation profile would put further pressure on the currency.

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