

## FX Daily: The cyclical versus structural dollar decline

The dollar continues to grind lower in a move probably now best categorised as an orderly dollar bear trend. After a structurally driven decline of the dollar in April, its losses over the last month or so have become cyclical, as earlier Fed easing becomes priced. Look out for US ISM and JOLTS data today, plus a high-profile central bank line-up at Sintra



All eyes are on the ECB's Sintra conference in Portugal today, with special attention on the US Fed's Jerome Powell

### 📌 USD: Focus on US data plus Powell at Sintra

The dollar continues to edge lower in an environment characterised by lower volatility. On the subject of volatility, it's interesting to note that traded volatility levels for equities and debt have fallen further than they have for FX. Here, EUR/USD and USD/JPY traded volatility remains above 8% and 10% respectively over the next couple of months, probably on the view that FX will be the asset class to move most if some of those Liberation Day tariffs re-appear in July. On that subject, reports suggest that the EU is prepared to accept 10% tariffs on most of its exports to the US, while it looks like Washington is currently trying to turn the screw on Japan as it seeks to open up the market for US rice exports. That could explain why USD/JPY is leading the dollar lower overnight.

And following on from the above, the issue of President Trump's tax bill passing through Congress, and what it means for the US fiscal position, is not seen as a big market driver this week. Here, US long-dated Treasury yields remain subdued and the swap spread (Treasuries versus swaps) remains contained. Perhaps it will have to be more news about poor demand at auctions, higher inflation or fears that the President will impose a dovish replacement for Fed Chair Powell that is required to place Treasuries back at centre stage for financial markets.

Also worth saying here is that lower volatility continues to help the carry trade in FX markets, where the Brazilian real, Hungarian forint and Czech koruna have all delivered 5-6% total returns against the dollar over the last month. In the G10 space, it's the euro and the Swiss franc leading the pack. The fact that these two are not the highest yielders suggests the issue of liquid alternatives to the dollar is playing a role here, and that those structural fears remain present. On the subject of structural fears, who knows when the investment committee of a Taiwanese Life Insurer is going to decide to raise its FX hedge ratios on US assets – something that [this BIS paper](#) believes has been an important driver of the dollar decline.

Back to the short term, the dollar has come quite far already and this bear trend probably needs feeding with some macro news. That news comes today in the form of the June ISM manufacturing release and the JOLTS data. On the former, the market will be looking at the trade-off between higher prices paid and lower demand/employment. Any softer prices paid with soft demand/new orders/employment is a dollar negative. Equally, higher prices paid and reasonable demand could be a mild dollar positive. And on the JOLTS data, any downside surprise to the 7300k consensus level could hit the dollar on the view that the resilient jobs market is starting to creak after all.

DXY has taken out some big support levels recently and is now on major channel support (off a 2011 low) – that support level coming in around 96.50. Let's see whether today's US data feeds that bear trend, and also look out for any new comments from Fed Chair Powell speaking at the Sintra conference at 1530CET (see below).

*Chris Turner*

## EUR: Big guns out at Sintra today

As above, the euro has been the top-performing G10 currency over the last month. The ECB is no doubt welcoming this 'global euro' moment, but also must be acknowledging that there is an awful lot of work to be done to attract global funds out of the US. Here, we would say progress on joint EU debt would be the single biggest game-changer.

For today, all eyes will be on the ECB's Sintra conference in Portugal, where the central bank heads from the US, eurozone, UK, Japan and Korea sit on a single panel at 1530CET. Most focus will probably be on Chair Powell and whether he wants to soften his tone on stubbornly high inflation – a dollar negative if he does. From the ECB side, the market prices one further 25bp ECB cut to 1.75% in December. It seems unlikely that President Lagarde will want to interfere in that pricing today.

EUR/USD briefly touched 1.1800 overnight – perhaps on the re-appearance of tariff threats against Japan. Technically, there's not much resistance now until 1.1900. But the trend is a little stretched, and we would warn against buying top-side breakouts. Instead, expect good buying to come in should EUR/USD correct back to the 1.1690/1720 area.

Chris Turner

## 📉 GBP: Focus on welfare vote and Bailey

EUR/GBP remains reasonably well bid as expectations for the BoE policy rate, like the Fed rate, have been priced lower over the last month. The market now prices 55bp of BoE rate cuts by year-end, and let's see what BoE Governor Andrew Bailey has to say about the speed of disinflation (especially in average earnings) and the labour market.

Today, sterling could also face some political risk as Prime Minister Keir Starmer faces a backbench revolt over welfare reforms. The government has already been forced to make about £4bn of concessions to get the bill through – although its passage is not guaranteed. Any failure to get the bill through could hit sterling and gilts on the view that further concessions will have to be made at a time when there is no fiscal headroom.

EUR/GBP could trade over 0.86 should today's vote reject the proposed reform.

Chris Turner

## 📈 CEE: Koruna is the only clearly bullish story in the region

Yesterday's inflation numbers in Poland provided the first slight upside surprise since January, with a rise from 4.0% to 4.1% YoY. The main reason, in our view, is the reversal of the trend in core inflation, which we estimate at 3.4% YoY. Thus, yesterday's number may be another reason for the National Bank of Poland to leave rates unchanged this week and, along with the discussion of next year's government budget, a reason for a hawkish press conference on Thursday. PMI numbers across CEE are due today, which should show some small improvement in sentiment.

Currencies in the region are showing some signs of exhaustion from the rally in the previous days. Although EUR/USD has found a new high and sentiment remains risk-on, we have seen roughly flat CEE currencies in EUR-crosses. We remain generally bullish on CEE currencies but the picture is becoming more mixed after a two-week rally. At the same time, the rates market is rather received, especially in HUF and PLN, narrowing somehow the rate differential. We have discussed EUR/HUF downside limits here before and it seems 399 has enough resistance for now. HUF rates, after moving down over the last three days, suggest a weaker currency, and we could go back above 400. On the other hand, the risk-on mood and stock rally suggest more downside for EUR/HUF, which makes the overall picture mixed. Thus, we are rather neutral at current levels with the possibility of a small upward correction after the rapid decline over the last two weeks.

We also see a small upside for today in EUR/PLN, but here we expect the NBP meeting this week to add support for the zloty. The Czech koruna thus remains the only clear bullish story for us in the CEE region, where we see limited room for weakness given the hawkish central bank and inflation upside risks. Over the weekend, the Czech National Bank governor reiterated his preference to see inflation below 2%, while we see a path above 3% in the coming months.

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