

## FX Daily: The indestructible dollar

Today's US Labor Day holiday means that it has been a quiet start to the week in the world of FX. The dollar remains near its highs despite Friday's US NFP jobs report showing a jobs market moving better into balance and wages softening. That probably owes to poor growth prospects overseas. Second-tier US data releases look unlikely to hit the dollar too hard



### ➔ USD: Little reason to offload dollar positions

The dollar has had a good couple of months. It has been buoyed by domestic strength in the US economy and souring sentiment in key trading partners such as Europe and China. The source of that strong domestic demand in the US has been a tight labour market, which has powered consumption. [Despite US wage growth softening in August](#) and the unemployment rate finally climbing, US Treasury yields actually rose on Friday and the dollar strengthened. Driving that move may have been the rise in the participation rate with people returning to the workforce. This suggests that the narrative may have moved on from the disinflation debate towards the extension of employment, consumption and domestic demand.

This week's [US data calendar](#) looks unlikely to open a decisive new chapter in this narrative – although in the past, the release of the ISM services index (remember that sub-50 reading at the start of the year?) has moved markets. That index is released on Wednesday. There are a few Federal Reserve speakers this week, but market expectations that Fed rates have peaked look set, as do views of a modest 100bp of Fed easing next year (we look for 200bp+). We see little

to challenge a strong dollar this week and could see DXY edging up to the 104.50/70 area.

Elsewhere in the world, the central bank policy focus is on the likes of Australia, Canada, Poland, Chile, and Israel. No change is expected in most, although Poland should be starting its easing cycle this week, and Chile is expected to follow up its 100bp cut in July with another large rate cut.

*Chris Turner*

## ➔ EUR: The return of the 'S' word

Very quietly we are seeing the return of the term 'stagflation' to describe prospects for the eurozone economy. The European Central Bank (ECB) is finally acknowledging that growth is going to be a lot weaker than their official forecasts while core inflation remains sticky above 5%. We think the ECB will push ahead with their final 25bp hike at their September meeting, but many think this will be a mistake.

In the background, eurozone politicians are still debating a return to Maastricht debt and budget deficit criteria, which had been suspended during the pandemic. While this may be good for eurozone government bond markets, its impact on the euro (tighter fiscal, less tight monetary policy) would be negative.

We do not see any range-breaking eurozone data on the agenda this week. However, there are plenty of ECB speakers jostling for position over the final 25bp hike in September. EUR/USD is looking fragile and while it may not go anywhere today, a speculative market that is still long EUR/USD might have to cut positions if modest support levels at 1.0760/85 give way. Intra-day resistance may be found at 1.0820.

*Chris Turner*

## ➔ GBP: A welcome revision to GDP

The UK national data office – the Office for National Statistics (ONS) – gave UK policymakers a welcome boost on Friday by revising up GDP growth in 2021 by 1.7%. That means that the UK returned to pre-pandemic growth much earlier than believed and that the revision leaves Germany exhibiting the weakest post-pandemic performance in the G7. The revision could also provide a little more fiscal headroom for the government, and we would not be surprised if speculation grew over some fiscal giveaways in the Chancellor's Autumn statement due in November.

Sterling has turned marginally better bid against the euro over recent days. Expect it to trade towards the lower end of a 0.8500-0.8600 range in the near term. It is a quiet week for UK data, but there may be some interest in Thursday's release of the Bank of England Decision Make Panel survey. Lower inflation expectations would be welcome but will not be enough to prevent the BoE from hiking 25bp on September 21st.

We do still, however, believe that the market prices about 20bp too much into the BoE tightening cycle and that sterling can soften a little in the fourth quarter.

*Chris Turner*

## ➔ EM: A quick round-up

Despite Chinese property-related stocks rallying on measures to support the sector, there seems no reason to expect a substantial reversal of renminbi weakness anytime soon. This should maintain the sluggish tone of Asian FX, although the Indonesia rupiah could out-perform as the low volatility environment continues to favour the carry trade.

In EMEA, the Bank of Israel meets today to set interest rates. Only 1 of 11 surveyed economists expect a 25bp hike. With USD/ILS trading at 3.80, however, the chances of a hike look under-priced. The highlight of the week should be the [start of Poland's easing cycle on Wednesday](#). This looks to have been reasonably well-telegraphed and should not unduly weigh on the zloty.

In Latam, Chile is expected to follow up July's 100bp rate cut with another 75bp move. Latam real interest rates are all quite positive (especially if you use inflation expectations as the deflator for real rates), meaning that large rate cuts have not hit the currency. Those looking at the Brazil easing cycle will be taking notes on developments in Chile this week. Finally, we think the Mexican peso [can hold onto gains](#) despite Banxico's decision to unwind its forward book.

*Chris Turner*

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