FX Daily: Trade headlines from Alberta can help the dollar

The main story in FX remains the rapidly evolving Middle East conflict. If oil prices correct further due to perceived limited supply risk, the dollar can follow suit and move lower. However, some USD-supportive trade news may emerge from the G7 summit in Canada. Elsewhere, the Bank of Japan kept rates on hold, with the yen muted on hawkish signals

The G7 Summit in Alberta, Canada, with French President Emmanuel Macron, Canadian PM Mark Carney, US President Donald Trump, and British PM Keir Starmer, among others

USD: Trade versus geopolitical news

The situation in Israel and Iran has shown few signs of de-escalation, and while that is offering intermittent support to the dollar, it has so far failed to generate a major rebound in the greenback. The main geopolitics-FX channel remains oil, whose price action suggests markets believe the worst of the impact may be past us. While a risk premium on crude prices remains warranted for now, investors look minded to gradually scale it back unless they see evidence of serious supply disruptions. The US is attempting to broker some talks between Iran and Israel, and any signs of de-escalation should harm the dollar from here.

What we think is more likely to have a positive USD impact is the G7 summit in Canada. Today, we could see most headlines centred on trade discussions, and Trump has in the past tended to turn less hawkish on protectionism after direct talks with foreign leaders. Any indications that the 90-day tariff pause will be extended should offer decent support to the dollar.

On the data side, the US releases retail sales figures for May after a surprisingly big drop in the Empire index yesterday, which confirmed that there are still mostly negatives from US tariffs for US manufacturers.

We see some upside risks for the dollar today given the possibility of constructive remarks on trade coming from the G7 summit. However, with the FOMC announcement looming tomorrow, there could be more cautiousness in chasing moves in either direction in USD crosses.

Elsewhere, the JPY move is fairly muted, rising against the dollar to 144.46 (vs 145 previously) then staying range-bound, and JGB futures dropped around 0.1% after the Bank of Japan's decision to keep its policy rate at 0.5% and to slow the JGB tapering from April 2026. Both decisions are in line with the market consensus. The BoJ will reduce JGB purchases by 200bn per quarter starting from April 2026. But there was one dissenting voter, and there will be a meeting between the MoF and PDs later this week, which may create more volatility. So, this might have given some cautiousness to the JGB market.

The BoJ's JGB hold on the short end is relatively smaller than the long end, thus quantitative tightening has a much bigger impact on market rates. Slowing QT doesn't necessarily signal a slowdown of rate hikes by the BoJ. To sum up, the BoJ's decision was in line with the market consensus, and the market's initial reaction seems a bit limited.

Francesco Pesole

EUR: ZEW might underwhelm

EUR/USD price action is so far endorsing our call that markets are not ready to take the pair much above 1.160 just yet. The upside risks aren't small though, for instance, if markets are disappointed with the trade headlines from Canada and oil prices correct lower due to perceived abatement in the Middle East turmoil.

Yesterday, ECB Governing Council member Joachim Nagel briefly mentioned the oil rally as a potential risk to price stability, and otherwise reiterated President Christine Lagarde's narrative that the ECB is in a good position with rates. But it is indeed oil prices that are likely to have the biggest impact on rate expectations at the moment. Unless Brent corrects further, markets may not really consider bringing the next cut forward to October.

The euro's contribution to EUR/USD moves remains minimal, but today's release of the ZEW survey in Germany can have some market impact. The "expectations" gauge is seen rebounding further to 35.0, but concerns about the EU-US trade standoff (albeit currently not the primary theme) could cap the upside.

We favour 1.15 rather than 1.16 as a near-term target and have a bearish bias on EUR/USD today. But the quite evident market preference to buy the dips in the pair means risks are still generally skewed to the upside.

Francesco Pesole

CEE: CNB blackout period and budget vote in Hungary

Today's regional focus is on Hungary and the Czech Republic. Wage numbers in Hungary will be released this morning, closely watched by the central bank. Parliament will also vote on the draft state budget for next year, resulting in a 3.7% GDP fiscal deficit.

In the Czech Republic, we should hear the bulk of the Czech National Bank board's opinions ahead of tomorrow's start of the blackout period. Last week, we heard from two board members, including the governor, suggesting a pause in the rate cut cycle in June and an open discussion of a rate cut in August. However, the governor's words suggest a longer pause given the surprisingly high inflation and outlook for the months ahead. We should hear from other board members today and tomorrow, and we expect a hawkish tone here as well.

In CEE markets, we see improving conditions for another FX rally. As we discussed yesterday, some spike in market rates due to the threat of higher energy prices from developments in the Middle East, in our view correctly reflects expectations of more hawkish central banks in the region. At the same time, we do not see a significant flight to quality globally and EM currencies strengthening generally. Moreover, higher EUR/USD clearly favours CEE currencies and we expect more gains here across the board in the days ahead. The CZK in particular should get attention today, supported by hawkish CNB views, which should push EUR/CZK below 24.750.

Frantisek Taborsky

PLN: Zloty remains cheap after election

While the HUF and CZK currencies are near their local strongest levels and have maintained some gains this year, the PLN has underperformed its peers and is essentially the only currency unchanged against the EUR compared to the start of the year. Given the hawkish bias of the National Bank of Poland in recent weeks, we believe the problem is a persistent premium in EUR/PLN coming from political uncertainty post-election. The interest rate differential itself suggests levels roughly around 4.230-240, indicating a 1% PLN rally if the market unwinds this political factor.

We don't expect any immediate impact on fiscal or general government policy, and after last week's successful confidence vote, we don't see much reason for PLN to remain at weaker levels. Moreover, the central bank is suggesting that another rate cut is more likely in September, while the market still prices in decent odds for July. Therefore, we see good reasons for PLN catching up with CEE peers.

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