

FX Daily: OPEC+ looks more important than Taiwan today

Financial markets have taken in their stride US House Speaker Nancy Pelosi's visit to Taiwan. Equity markets have settled, and pushback from the Fed against a perceived pivot to the end of the tightening cycle has sent US yields higher and kept the dollar relatively strong. The highlight of today's session should be the OPEC+ meeting and its supply impact



➔ USD: Typhoon in a teacup

Nancy Pelosi's visit to Taiwan has triggered the expected ire of Chinese authorities. These have responded with new restrictions on sand exports to Taiwan (to target the construction sector) and also an extension of some bans on fruit exports. Chinese live-fire military drills have been announced for 4-7 August - measures that will keep financial markets on edge.

For the time being, however, investors have taken the Pelosi visit in their stride and Asian equity markets are tracing out small gains. Suggestions that China could be weaponising its US Treasury holdings on the back of Taiwan alone look wide of the mark. We say this because there are many other factors driving the Chinese decline in US Treasury holdings and several factors driving the US

Treasury sell-off overnight.

From the Chinese side, true holdings of US Treasuries have dropped to \$980bn in May from \$1.08trn late last year. Yet this looks more likely a function of Chinese FX intervention to keep USD/CNY stable in a strong dollar environment. After all, Korea's US Treasury holdings have fallen from \$132bn to \$114bn over the same period too. And a further decline in China's US Treasury holdings looks likely as geopolitical spheres of influence sharpen after Russia's invasion of Ukraine and the seizure of Russian FX reserves. See our comment on this subject [here](#).

From the US Treasury side, last night's sell-off looks more related to a raft of comments from Fed speakers that it was 'nowhere near done' when it comes to tightening. Expect similar rhetoric to emerge from Fed speakers today from the likes of James Bullard (1330CET), Patrick Harker (1630), Mary Daly (1715) and Tom Barkin (1745). We would also recommend a read of [Padhraic Garvey's opinion piece](#) on the Fed's historic reluctance to hike should US 10-year Treasury yields be trading below the Fed Funds rate. The conclusion here being that it seems more likely that US 10-year yields head back to 3.00% than the Fed stop tightening at 2.50%.

For today's session, the bigger focus may come on the announcement of fresh supply quotas from OPEC+. So far President Biden's recent trip to Saudi Arabia has yet to produce significant supply increases. Most analysts think the OPEC+ quota for September will be left unchanged. Yet any surprise supply increase (analysts going for increases are looking in the range of 200k to 1mn barrels per day) would hit crude prices, be good for risk assets and probably send the dollar lower. This looks like an outside risk for today.

DXY is currently around 2% off its highs of the year and should probably stay supported around these levels as the Fed pushback continues.

➔ EUR: Consolidation near the lows

Looking at EUR/USD it is worth remembering that the recent bounce from 0.9950 to near 1.0300 has been exclusively a dollar correction - not driven by any re-rating of the euro after, say, the ECB's announcement of its new [Transmission Protection Instrument](#). We say this because the ECB's trade-weighted measure of the euro is sitting at its lows for the year - understandably so, given the challenges that high gas prices pose for Europe's industry and consumers for the remainder of this year. Any fresh hawkishness from the Fed then could easily push EUR/USD back to parity. For today we would favour a 1.0100-1.0200 range with a slight downside bias given the Fed speakers this afternoon.

Elsewhere, we see EUR/CHF trading in the low 0.97s. The Swiss franc is a little stronger [than we thought](#). We had felt that the Swiss National Bank would guide EUR/CHF some 4% lower over the year. Given that the SNB will now be intervening on both sides of EUR/CHF, we doubt it will guide EUR/CHF much lower in the short term. On that subject, look out for Swiss July CPI today, expected to remain at the cycle high of 3.4% year-on-year.

➔ GBP: Gearing up for Super Thursday

EUR/GBP is consolidating near the lows ahead of tomorrow's Bank of England rate decision and the release of its latest inflation report. Please see our full scenario analysis [here](#). The default view is that a 50bp hike can leave EUR/GBP relatively unscathed near 0.8350.

One additional point to add here is that the release of the May inflation report saw the BoE try to push back against market pricing of an aggressive tightening cycle. Since then some BoE speakers have said that the pound has a role to play in monetary policy settings and indeed the trade-weighted pound has rallied 3% from its lows in July (largely on the back of the weaker euro). With gas prices staying high and the dollar likely to stay strong, arguably the BoE would prefer a stronger pound now. Once again the reports of the pound's impending demise look greatly exaggerated.

📌 CEE: That's enough, for now

The Polish zloty and Hungarian forint touched 4.70 EUR/PLN and 397 EUR/HUF yesterday, in line with [our expectations](#). In both cases, these are the strongest values since the beginning of last week and in our view, it is enough for now. For today, we expect a slight retracement of the new gains closer to levels around 4.725 and 399 per euro. However, as we mentioned yesterday, geopolitical risks lurk around every corner and the China-Taiwan escalation is certainly not helping the region. Stronger dollar strength would of course mean bigger losses for CEE currencies. Moreover, their sensitivity is multiplied by the currently strong levels and so the move higher could be swift.

On the data front, today we will see retail sales in Hungary and Romania. Peter Virovacz in Budapest [expects](#) a still strong 10% YoY, above market expectations. Although retail sales are slowing, it should still be a sufficient number to help the forint defend against global pressures.

In the universe where central banks are keeping their currencies under control, i.e. the Czech Republic and Romania, markets are preparing for this week's monetary policy meetings. In Romania, everything seems under control, as always, and the leu remains firmly pegged around EUR/RON 4.925. Markets are expecting a roughly 100bp rate hike, in line with our forecast. In the Czech Republic, markets have erased most expectations of a rate hike in recent days, which has moved the interest rate differential to its lowest levels in a month, adding pressure to the weaker koruna. Thus, EUR/CZK is gradually pushing to the upper part of the 24.60-24.70 band, and we expect the Czech National Bank to be forced to defend the koruna again, but we do not expect a proper test of the central bank's will until [Thursday](#) when the board meets.

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