

## FX Daily: Underdogs make a comeback ahead of US CPI

It has been a good week for the underdogs in the G10 FX world. The Japanese yen, Norwegian krone, Swedish krona and Swiss franc led the gains against the dollar over the last week. This may well be a position adjustment against the risk of a benign US CPI print today and a tweak in Bank of Japan policy at the end of the month. Today's CPI reading will therefore be key



Yen

### 📉 USD: Benign CPI could unlock a leg lower lower in the dollar

Another European morning follows another Asian session where USD/JPY has led the dollar lower. The Japanese yen has now appreciated 3.6% against the dollar over the last week, closely followed by NOK (+3.4%), SEK (+2.7%) and CHF (+2.4%). We discussed some of the [push-pull factors driving the dollar](#) in yesterday's update, but the outperformance of these underdog currencies clearly points to some position adjustment at work. The broad-based nature of the rally in these currencies suggests investors may be anticipating a more benign US price environment like the one we saw in November last year when the US started to print core inflation at 0.3% month-on-month after a string of 0.6% releases.

That nicely brings us to today's main event, which is the June CPI release at 14:30CET. Expectations are for a more benign 0.3% MoM core reading - the lowest since last November - and base effects bringing the headline CPI down to just 3.1% YoY - the lowest since March 2021. Assuming no nasty upside surprises here, this may be enough to firm up a view that a 25bp Fed hike may well be the last in the cycle. If so, DXY could make a run at the year's lows near 100.80.

A quick word on the yen. Developments in USD/JPY - especially the sell-off in early Asia - seem to be led by selling in the JGB bond market. Here, 30-year JGB yields are rising - spreads between 30-year US and Japanese government bonds have narrowed 12bp over the last week - and the Nikkei equity index is underperforming. This has all the hallmarks of position adjustment before the 28 July Bank of Japan (BoJ) policy meeting, where expectations are growing that the BoJ could switch to targeting the five-year part of the JGB yield curve - another small step to policy normalisation. In short, then, this USD/JPY move looks driven by the private not public sector (i.e. no intervention) and something like 138.25 looks like a near-term target for USD/JPY assuming today's US CPI data does not surprise on the upside.

*Chris Turner*

## EUR: Going along for the ride

Yesterday's price action was a little strange. EUR/USD opened bid in Europe, but spent the rest of the session edging lower even though the US NFIB pricing intentions survey did dip as we expected. EUR/USD opens Europe bid again today and as above, the US CPI print is going to be the main story. This may be one of the next chances that EUR/USD has of breaking above 1.1100 this month.

One side issue here. Tomorrow sees eurozone finance ministers meet in the [Eurogroup format](#). On the agenda is fiscal policy for 2024, which given the inflation problem, might be more minded to bring forward fiscal consolidation and a return of the Stability and Growth Pact budget constraints. Tighter fiscal policy could see ECB tightening expectations priced lower and perhaps see the euro underperform a little - albeit in a potentially soft dollar environment.

Also, today look out for a speech from ECB Chief Economist Philip Lane at 15:45 CET. Let's see whether he supports market pricing of two more 25bp ECB hikes later this year.

We favour a little more EUR/USD upside today - but that's very much dependent on the US CPI data.

*Chris Turner*

## GBP: 1.30 will be tough for cable

Sterling and UK interest rate markets did eventually respond to the [higher wage data yesterday](#). Today, the Bank of England has just released its [Financial Policy Summary and Record](#). Headlines suggest large banks have passed stress tests while smaller lenders and shadow banks remain a concern though UK households with high debt will remain below their peak of 2007. At first glance, there seems nothing here to urgently constrain the BoE's monetary tightening plans.

US CPI will determine whether GBP/USD dramatically trades through 1.3000 - there is an outside risk to 1.33 should we see a November 22-style move in the dollar. But it is probably better to stay cautious here and after a good rally so far this month, 1.30 could be difficult to break. EUR/GBP has

broken to a new low - but again 0.8500 might provide some psychological support.

*Chris Turner*

## CAD: We expect a BoC hike today

The Bank of Canada surprised markets with a hike in June, and our base case is that policymakers will follow up with another 25bp increase today. [As discussed in our preview](#), the data flow since the June meeting has not pointed unequivocally in the direction of more tightening, but the latest jobs report continued to point to a tight jobs market and we see a higher chance that the BoC will favour two back-to-back hikes after a five-month pause.

The consensus has been split lately but has leaned more in favour of a hike in the past few days. Markets price in around 17bp ahead of today's announcement. There is undoubtedly some upside potential for CAD today in our baseline scenario, especially because the BoC may see the advantage in attaching a dovish statement to a hike, so closing the door to further tightening if needed. USD/CAD could be eyeing the 1.3120 late-June lows, and we like the loonie even more against other procyclical currencies like the Australian dollar or the Swedish krona.

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