FX Daily: US CPI may invert the USD/low-yielders trend

US inflation numbers today should fuel the narrative that the economy is starting to overheat, sending Treasury yields and the dollar higher

USD: Inflation impact on UST may provide support to the dollar

The week in FX has started along the lines of the past one, with the dollar marginally weaker amid broadly supported low-yielders and lingering soft momentum for commodity currencies. This has been possible as the main drivers of global markets at the moment – US Treasuries– were only marginally weaker (10Y yields rose 1bp) yesterday. However, the key test for bonds is due today, as the release of US CPI numbers for the month of March is widely expected to show another jump in inflation. Our US economist James Knightley is forecasting headline inflation to rise 0.5% month-on-month and 2.4% year-on-year, broadly in line with consensus. Such figures should further fuel the narrative that the US economy is starting to overheat and will likely add to concerns that the Federal Reserve's firmly dovish message will be increasingly challenged. Our rates team expects the inflation numbers to support an increase in UST 10Y yields that may test the 1.75% level this week. Ultimately, this could cause an inversion in the recent G10 FX dynamics, with the dollar possibly outperforming low yielders (mostly JPY and CHF, but also EUR) on the back of weaker

Treasuries. Meanwhile, the US Treasury's FX Report should be published on Thursday, and may tag Taiwan as a manipulator – but not China – and possibly raise the threshold for the three criteria to receive the manipulator tag, according to some media reports.

EUR: Current levels to be tested

The US inflation report (to be more precise, its impact on UST yields) is set to be the main driver for the EUR/USD today and may cause the pair to test last week's 1.1860 lows. A usually important data point in the eurozone – the German ZEW – should have limited impact today as a positive re-rating of the eurozone recovery outlook appears almost solely reliant on material advancements on the vaccination rollout in the EU and the unlocking of the EU Recovery Fund.

GBP: The rebound should have legs

We were not at all surprised to see sterling's rebound yesterday after last week's correction: the storm that hit the AstraZeneca vaccine has not derailed the UK vaccination plans, leaving prospects of a sharp recovery in the country intact. Also, GBP/USD appeared meaningfully undervalued at the end of last week. We expect the pound to show relatively good resilience to any USD rally today.

NZD: RBNZ's pause to have limited FX implications

As highlighted in "RBNZ preview: Quietly monitoring house prices", the Reserve Bank of New Zealand's meeting tonight should be a quiet one, with limited implications for the New Zealand dollar. The Bank is now under less pressure to normalise policy on the back of surging house prices, after the government intervened with measures to curb investor demand. House prices are set to remain a key variable for NZ monetary policy, but for now, expect the central bank to refrain from strong comments on this topic.

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