

## FX Daily: US CPI to challenge dollar correction

The dollar has remained under some pressure as the PPI upside surprise failed to offset the more dovish narrative from Fed officials. Today's CPI may, however, be a tougher test for the dollar's short-term bears. Rates remain the dominant driver of CEE FX and inflation surprises are leading to divergence in the region



### USD: CPI to challenge dollar correction

Yesterday's US PPI inflation figures for September surprised on the upside. The headline rate rose 0.5% month-on-month versus the 0.3% consensus while the core rate rose 0.3% MoM versus the expected 0.2%. While it doesn't always have a direct read-through for CPI, it still makes it more likely that today's CPI figures come in at 0.4% MoM for the headline and 0.3% for the core, above the 0.1% or 0.2% MoM readings that would be consistent with year-on-year inflation falling back to the 2% target.

The market reaction to the higher-than-expected PPI reading was quite muted though, as the majority of investors appear to be endorsing the view that minor bumps on the disinflation road can be sustained given that higher market rates now disincentivise the Fed from hiking again. That narrative has effectively been encouraged by a number of Fed speakers now. Yesterday,

Christopher Waller – a hawk – said the FOMC can watch and see what happens before taking further action on rates.

This more dovish rhetoric by the Fed has also partly overshadowed yesterday's FOMC minutes, which signalled that members saw inflation as "unacceptably high". At the same time, the minutes showed that "all participants agreed that policy should remain restrictive for some time", warning that the economic outlook was "highly uncertain". Our US economist notes that there is a feeling the Fed was getting more cautious before the spike in Treasury yields, which also tends to endorse the view that rates have peaked.

As a result, the dollar has stayed mildly pressured. We think today's CPI print is a bigger test for USD short-term bears though, and we warn against attaching hopes of a sustainable dollar decline to declining US yields, as activity data continues to hold the key to the dollar outlook beyond the very near term. The correction in DXY may extend to 105.00, but a return to 106.50 seems more likely, in our view.

*Francesco Pesole*

## **EUR: Eyes on the minutes**

The European Central Bank released the result of its consumer expectations report yesterday, which showed a marginal increase in August's inflation expectations for both 12 months ahead (3.4% to 3.5%) and three years ahead (from 2.4% to 2.5%). These are small changes, but the fact that inflation expectations are still rising despite the ECB's rate hikes supports the hawkish argument.

Markets are, however, pricing close to zero chance of another hike in the eurozone, and the rather cautious tone by ECB speakers is probably helping this dovish view. We'll continue to hear ECB members' remarks today, with Frank Elderson, Francois Villeroy, Robert Holzmann, Klaas Knot, Boris Vujcic, Bostjan Vasle and Fabio Panetta all scheduled to speak.

The ECB will also release the minutes of the September meeting. This will likely be the occasion where the EUR faces some idiosyncratic effect: EUR/USD has been almost entirely a dollar story so far this week. We'll probably see more evidence of a divided governing council, with many members having preferred to hold rates steady in December. There are downside risks for the euro, but not very big considering markets have already priced out tightening expectations.

*Francesco Pesole*

## **GBP: GDP in line with expectations**

UK GDP rose 0.2% MoM in August, in line with consensus, however the previous number was revised slightly lower. Industrial production came in at 1.3% YoY versus the consensus of 1.7%. The pound is unchanged after the release.

The Bank of England's focus remains firmly on inflation and the jobs figures, which will be released next week. Market expectations of another hike this year (two meetings left) are below 50%, with the spillover from the US narrative of "higher rates = no more hikes" also being felt.

Still, the euro remains rather unattractive compared to the higher-yielding pound, and the decline in EUR/GBP may have more room to go from current levels. A move below 0.8600 in the near term

is possible.

Today's UK calendar includes the BoE's credit conditions survey and a speech by the BoE's Chief Economist Hue Pill.

*Francesco Pesole*

## ➔ CEE: Rates remain the main driver of FX

Today we only have data from Romania in the calendar, which was published this morning. Inflation in September fell from 9.4% to 8.8% YoY, only slightly above the market estimate. Q2 GDP was revised down slightly from 1.1% to 1.0%, but QoQ we moved from 0.9% to 1.7% QoQ after the revision. On the other hand, the industrial numbers are negative again.

In FX market, as we mentioned earlier, over the past two weeks, rates seem to be the main driver for CEE FX. So yesterday's move in rates showed where we actually are. It seems that for now the rate receivers will take a break for a while and we might stabilize a bit ahead of the US CPI numbers. After Tuesday's inflation numbers, we see that the CZK followed the rates move and could stabilize around 24.550 EUR/CZK for now.

On the other hand, HUF rates have again jumped down significantly, pushing the NBH into bigger rate cuts, as we discussed yesterday. So, for us, the main message here is that HUF rates are leaving lower rates exposed to further weakness. Just rates indicate levels around 392 EUR/HUF, but a slightly lower US dollar could dampen this room for weakness probably.

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