FX: Dollar benign decline extends

Why the dollar remains on the back foot

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Watching the Dollar Index

Without much fanfare, the DXY, the dollar index, has traded down to levels not seen since January 2015 – fittingly unwinding the gains that it had enjoyed at that time on the start of ECB QE. We would still characterise this as a benign decline, (ie.driven by growth opportunities overseas) rather than a painful adjustment on, say, the threat of US protectionism. Following last week's focus on China potentially selling US Treasuries, we'll see November TIC data on Wednesday, providing a window on the latest Chinese holdings data. As we highlighted last week, we think this story will be noise around core trends. Instead, there is enough good news in the rest of the world to keep the dollar on the back foot and a quiet week for US data (IP Wed, Housing starts Thurs and confidence Frid) looks unlikely to change the trend. DXY has support at 90.30 but looks headed to 90

EUR: Will the ECB want to slow the EUR rally?

ECB minutes proved the unlikely trigger for EUR strength last week and it will be interesting to see whether ECB officials try to cool speculation of any near-term adjustments in policy language. We note that Weidmann and Coeure speak at an IMF event on Thursday. We still have a slight preference that EUR/USD consolidates, rather than immediately pushes to new highs, but clearly, there is a risk of under-estimating the powerful dollar bear trend. EUR/USD has resistance at 1.2250 and then 1.2360.

GBP: CPI the highlight this week

GBP is matching EUR strength quite well, despite a few negative UK headlines (e.g. Carillion heading towards administration). Tuesday's CPI data will help define the Bank of England view. Our economists think it could tick down slightly, but core still at 2.5/2.6% YoY could see the market firm up expectations of a May hike. Cable looks headed towards resistance at 1.3835 en route to a 1.40 1Q target.

Israeli Shekel: Little the BoI can do about the strong ILS

USD/ILS has today broken below the 2014 low of 3.40 amidst a broadly weaker dollar. The Bank of Israel has stepped back into the market recently, intervening to the tune of US$100mn in December and buying 'large amounts' of FX in January. While Washington may in general be frowning on large scale FX intervention, it may take a more lenient approach in the case of Israel, where the BoI will still argue that it is battling very low inflation. That said, we doubt the BoI will be prepared to cut rates with an economy near full capacity and a government having just passed an expansionary budget. We've cut our one year $/ILS target to 3.25, having held a 3.40 view for the majority of last year.