FX: Don’t panic

We doubt current price action in markets signals the start of a major new trend

USD: We should not be afraid of a market correction

There’s much discussion of a ‘bond rout’ and a sense that investors have broken too quickly from the gates this year in search for returns in risky assets – particularly equities. But the early stages of a bear market in bonds do not have to be bearish for stocks (typically equities like a bit of inflation) and so far the bond market sell-off has been orderly. For example, the MOVE index of implied volatility for a selection of US Treasuries is a little higher, but yet to reach levels seen last October. While we could see a little equity weakness extending into Europe today – and probably a little corrective dollar strength – we doubt current price action marks the start of a major new trend. Beyond the activity data in Europe, the key focus today will be President Trump’s State of the Union address (0300CET). We think he might be a little more protectionist, although that may be counter-balanced with a more conciliatory tone to the Democrats (in order to get funds for his wall) and references to a US$1trn infrastructure package. We’ll be using the performance of the FX funding/safe haven currencies of JPY and CHF to gauge whether the recent correction has a little further to run.

EUR: Eurozone GDP and German CPI to set the tone

EUR/USD is undergoing a modest correction – with quite a few analysts favouring a larger correction lower as it reconnects with yield spreads. It's ironic that these calls are coming at a time when the 5-year German : US curve sovereign spread may be starting to turn in the Euro's favour. We are also sympathetic to the view that reserve managers (who typically have bond duration targets in the 2-5 year area) will start to increase the EUR share in FX reserves over coming years – SNB reports 4Q17 FX reserve allocation tomorrow. EUR/USD may have outside risk to the 1.2220 area, but we are not looking for a major sell-off. Eurozone 4Q17 GDP and German CPI to be watched today.

GBP: Carney speaks at 1630CET

We're tempted to say GBP/USD can hold support at 1.4000 today.

HUF: NBH's dovish rhetoric to modestly weigh on HUF

The Hungarian National Bank is widely expected to stay on hold today. However, following the disappointing market reaction after the first interest rate swap tender two weeks ago and the subsequently announced new fine-tuned conditions for the tenders, the key focus shifts to the wording of the NBH statement. We expect the NBH to reiterate: (a) its conviction behind the IRS programme; (b) its forward rate guidance for flat rates until mid-2019. The latter should be modestly negative for the forint and send EUR/HUF closer to the 311 level.

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