

FX: High bar for USD strength as regime change looms

Trading is likely to be subdued given the US Presidents' Day market holiday, but the focus this week will shift back to the Fed story and the Jan FOMC minutes



USD: On the cusp of a regime change

As noted in G10 FX Week Ahead: [Can the Fed save the dollar?](#) we are clearly witnessing a weak dollar environment, with early signs that investors are demanding concessions (both in FX and yields) to hold US bonds. Today's price action should be muted given the US market holiday, but starting tomorrow the focus will shift back to the Fed story and the Jan FOMC Minutes (Wed) in particular. While the Fed tone may be a little more hawkish, a lot of Fed tightening is already

priced this year (more than three full 25bp hikes), thus the dollar need not rally. The price action of the past months provides a case in point, whereby the USD decoupled from the materially higher UST yields (both at the front- and the back-end) and the market's hawkish expectations about the path of the Fed. This points to a regime change in the USD ([see FX TalkiNG](#)) and a very high bar for more meaningful USD strength.

EUR: ECB's concerns about euro volatility unlikely to credibly weigh on EUR

The key Eurozone data point of the week is the ECB Minutes (Thu). Although the Governing Council may try to exaggerate concerns over FX volatility, we suspect any EUR/USD correction will be temporary given that the bar for the ECB to credibly talk down the euro is high, due in part to the trade-weighted euro not being particularly strong to begin with ([see ECB's Sisyphean task to credibly talk down the euro](#)).

JPY: Any yen softness against USD to be temporary

While the Japanese yen modestly softened overnight in line with the higher Nikkei, we see the USD/JPY upside as limited. The slightly more hawkish Fed stance does not make much difference for USD and with the FX market increasingly looking at US Treasuries and any signs of waning appetite, JPY seems well positioned. We also note the yen's undervaluation against the USD and the USD/JPY's decreasing sensitivity to risk (suggesting that JPY can do well even in an environment which is benign for risk), both point to more room for the USD/JPY to decline towards 100.

RUB: Benign risk environment bringing USD/RUB closer to the 56.00 level

Russia will report key macro data for January today. Our economists expect a pick-up in real wage growth due to public wage indexation. We expect to see improving momentum in economic activity in coming months. Expect a direct impact on RUB from today's data to be limited. Rather the key drivers of USD/RUB today will be (a) the extent of the general USD softness (b) general risk appetite. Both point to a lower USD/RUB, slowly grinding towards the 56.00 level yet again.

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