

The dollar's handbrake turn

It's been a big day in FX markets where a wholly weak US jobs report has pulled the rug from under Jerome Powell's hawkish stoicism and stopped the dollar's rally in its tracks. It looks highly likely that the dollar has marked out a significant corrective high



The US jobs report has stopped the dollar rally in its tracks

The solid labour market that wasn't

We should have known something was up when Federal Reserve dissenters Chris Waller and Michelle Bowman released rare joint statements 30 minutes ahead of the jobs data, explaining their dovish position. One could be forgiven for thinking this was an attempt to exert maximum pressure on Chair Powell should the jobs numbers prove weak – which they were. As [James Knightley discusses here](#), the huge back-month revisions now undermine the Fed's key stance that the labour market has been solid and that a pre-emptive rate cut was not needed.

The huge drop in short-dated rates (now compounded by a resoundingly soft set of ISM manufacturing data) has triggered 9bp of bullish steepening in the US Treasury curve on the view that the Fed will be forced to act in September. As James writes, it looks hard to argue with a Fed cut then unless there are some sharp upside surprises in the inflation data or this soft jobs data somehow reverses in the August release.

Corrective dollar high looks to be in place

Wednesday's bearish flattening in the curve, which sent the dollar 1% higher across the board, seems like a distant memory. And that's fair because today's data has provided a reset on Fed

thinking. Leading the dollar lower today has been USD/JPY, where the soft payrolls report has knocked 1.8% off the S&P 500 so far – presumably on the view that US domestic demand might not be quite as resilient as first thought – and perhaps faces further challenges as US businesses are forced to pass tariff hikes through to consumers this quarter.

The story for coming months will be which of the two opposing forces dominates: e.g. will labour market data deteriorate enough to cement the September rate cut and a deeper easing cycle? Or will the pick-up in tariff-driven inflation force the Fed to continue favouring modestly restrictive policy? The size of today's backward revisions in the data suggests the momentum will be with the former.

If equities stay offered, it will be the likes of USD/JPY and USD/CHF which lead the dollar lower again. However, calling a top in US equities on the back of some softish payroll data – and a Fed potentially cutting rates – remains a dangerous game given the powerful forces in play. That's why we think there could be continued interest in emerging market currencies and [dollar-funded carry trade strategies as we discuss here](#).

What seems a little clearer to us is that a corrective high is in place for the dollar – e.g. just below 1.14 for EUR/USD and close to 151 in USD/JPY. These weren't too far from the levels we discussed in [July's FX talking publication](#). We hadn't expected EUR/USD to push back into the 1.18/20 until much later in the year. But depending on whether the labour market data deteriorates further – enough for the Fed to increasingly look through the temporary pick-up in inflation – those higher levels could be seen much sooner.

We'll also keep a close look on the FX option market where a continued rise in three-month traded volatility and the risk reversals being bid up even further in favour of euro calls will tell us that the EUR/USD rally has legs. For reference, the three-month risk reversal skew for euro calls is now 0.43% versus a bullish peak in May of over 1%.

Author

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial

Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.