



MONEX

Week Ahead

11th - 15th March 2024

Is the tide turning for
the dollar?

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This week has been one to forget for our near-term forecasts. The combination of a confident Powell and downwards revisions to January's NFP print saw the DXY index shift lower by close to a percent. While these outcomes weren't necessarily a surprise to us, the market response was, primarily because we thought guidance from the ECB and the BoC would also follow Powell's, laying the grounds for earlier policy easing than markets expected. Granted, ECB speakers did start to reflect this by the end of the week, with both doves and hawks coming out to keep the prospect of an April cut alive, it was too little too late for our drowning dollar call as most long positions had already been flushed out of the market.

In light of this week's events, the natural question is if we should change our bullish dollar call as the market narrative returns to a soft landing outcome and further yield compression. While our medium-term view will depend on how markets trade through the remainder of the next month, with key inflation data due out of the eurozone and the US alongside another round of PMIs before we fully throw in the towel, our initial inclination is to retain our bullish USD view. This is primarily because higher for longer stances from the BoC and ECB should merely delay the pain for their respective currencies, which account for a significant percentage of the DXY basket. Nevertheless, we have succumbed to the prospect that our near-term views on the dollar are likely too optimistic, that is unless next week's US inflation data strikes a blow to the "everything is great" view markets are now taking due to more likely Fed easing. Next week will also see notable data releases from Brazil, the UK, China and Poland, all of which pose notable questions for their respective currencies. As such, we've opened up the Week Ahead to the trading floor once again, answering some of the most burning questions with next week's events in mind.

ECONOMIC CALENDAR

All times in GMT

Saturday 09/03

Time	Country	Event	Period	Estimate	Prior
01:30	China	CPI YoY	Feb	0.3%	-0.8%

Monday 11/03

Time	Country	Event	Period	Estimate	Prior
00:01	UK	KPMG & REC report on jobs			
07:00	Norway	CPI MoM (YoY)	Feb		0.1% (4.7%)
		Underlying CPI MoM (YoY)	Feb		0.0% (5.3%)
	Turkey	Unemployment rate	Jan		8.8%
09:00	Switzerland	Domestic sight deposits	Mar 8		467.9b
12:00	Canada	Bloomberg Nanos confidence	Mar 8		52.5
15:00	US	New York Fed 1-year inflation expectations	Feb		3.00%
21:45	New Zealand	Card spending total MoM	Feb		2.0%

Tuesday 12/03

Time	Country	Event	Period	Estimate	Prior
00:30	Australia	NAB business confidence	Feb		1
05:00	Sweden	PES unemployment rate	Feb		3.5%
07:00	UK	Employment change 3m/3m	Jan		72k
		Unemployment rate	Jan	3.8%	3.8%
		Weekly earnings ex-bonus 3m/YoY	Jan	6.2%	6.2%
		Change in payrolls	Feb		14.1k
08:00	Sweden	Riksbank's Executive Board speaks at Parliamentary hearing			
10:00	US	NFIB small business optimism	Feb		89.9
11:00	UK	BoE's Catherine Mann speaks			
12:00	India	CPI YoY	Feb	5.07%	5.10%
12:00	Brazil	IBGE CPI MoM (YoY)	Feb	0.78% (4.42%)	0.42% (4.51%)
12:30	US	CPI MoM (YoY)	Feb	0.4% (3.1%)	0.3% (3.1%)
		Core CPI MoM (YoY)	Feb	0.3% (3.7%)	0.4% (3.9%)
		Real average weekly earnings YoY	Feb		-0.1%
22:00	Australia	CBA household spending MoM (YoY)	Feb		3.1% (3.6%)

Wednesday 13/03

Time	Country	Event	Period	Estimate	Prior
07:00	UK	GDP MoM (3m/3m)	Jan	0.2% (-0.1%)	-0.1% (-0.3%)
		Index of services	Jan		-0.1%

Time	Country	Event	Period	Estimate	Prior
07:50	Sweden	Riksbank's Floden speaks			
08:00	Sweden	Riksbank's Breman speaks			
10:00	Eurozone	Industrial production MoM (YoY)	Jan	-1.0% (-2.6%)	2.6% (1.2%)
11:00	US	MBA mortgage applications	Mar 8		9.7%
18:00	New Zealand	RBNZ's Conway speaks about February MPS			
21:45	New Zealand	Net migration	Jan		7260
TBA	Singapore	MAS survey of professional forecasters			

Thursday 14/03

Time	Country	Event	Period	Estimate	Prior
00:01	UK	RICS house price balance	Feb		-18%
07:00	Sweden	CPI MoM (YoY)	Feb	0.3% (4.7%)	-0.1% (5.4%)
		Core CPI MoM (YoY)	Feb	0.7% (3.6%)	-0.5% (4.4%)
07:30	Switzerland	Producer and Import prices MoM (YoY)	Feb		-0.5% (-2.3%)
12:00	Brazil	Retail sales MoM (YoY)	Jan		-1.3% (1.3%)
12:30	Canada	Manufacturing sales MoM	Jan	0.4%	-0.7%
	US	Retail sales control group MoM	Feb		-0.4%
		Producer price inflation MoM (YoY)	Feb	0.3%	0.3% (0.9%)
		Core PPI MoM (YoY)	Fed	0.2%	0.5% (2.0%)
		Initial jobless claims	Mar 9		217k

Friday 15/03

Time	Country	Event	Period	Estimate	Prior
01:20	China	1-year Medium-term Lending Facility		2.50%	2.50%
01:30	China	New home prices MoM	Feb		-0.37%
		Used home prices MoM	Feb		-0.68%
07:00	Sweden	Unemployment rate	Feb		8.5%
09:00	Poland	CPI MoM (YoY)	Feb	0.5% (3.1%)	0.4% (3.9%)
09:30	UK	BoE/Ipsos 1-year inflation expectations	Feb		3.3%
10:00	Italy	Retail sales MoM (YoY)	Jan		-0.1% (0.3%)
12:00	Brazil	IBGE services volume MoM (YoY)	Jan		0.3% (-2.0%)
12:30	US	Empire manufacturing	Mar	-8.0	-2.4
13:00	Poland	Current account balance	Jan	1446m	-24m

QUESTIONS FROM THE FLOOR

GBPUSD is close to 1.28, why is that?

As alluded to, cable has been on a tear in early March, with the currency up close to 2% this month already. That said, this has largely been a dollar story so far. Sterling remains in the middle of the pack when comparing performance amongst other G10 currencies. This rally in G10 FX against the dollar has in turn been driven by market reassessment on the likely path for US rates. Having flirted with the idea of just three Fed rate cuts this year at the end of February, markets are now pricing in closer to four. The move to price in more Fed rate cuts this month has not, however, been matched by a similar move in Bank Rate expectations for 2024. Markets now see 2.6 cuts priced in for the BoE this year. In turn, this leaves the expected spread between UK and US policy rates now looking fairly priced to us, if not a little too wide. Our base case sees five rate cuts for the Fed this year and four from the BoE.

“So whilst we think markets are being overly hawkish in their view of both central banks, we think the difference between the two now looks about right.”

Even so, we would not rule out further short term upside for cable. With the Fed likely to move before the BoE on rates, a market realignment towards more Fed rate cuts as projected under our base case is likely to happen earlier, seeing the expected rate differential temporarily widen, even if we don't believe that it will ultimately be sustained. Such an event could happen this month too. The BoE is likely to give markets little reason to reassess the likely easing path in the UK at their upcoming meeting. Inflation risks remain elevated, as does wage growth, and with no MPR this month there is little need for the MPC to steer markets towards pricing in more rate cuts. This is less true for the Fed, where policymakers need to be more cognizant of the more immediate timing that is likely for policy easing. Indeed, we think this concern led some of Chair Powell's recent commentary to be arguably a little more dovish than expected, a factor contributing to the present widening in spreads. As such, while we think current levels are likely a fair reflection of our underlying view for policy easing in both the UK and US, with risks for the remainder of the month look tilted towards further upside in GBPUSD to us.

We saw fairly positive tones from Chinese policymakers at the “Two Sessions” this week, can we expect further stimulus and another rally in the yuan?

At its “Two Sessions” meeting this week, Premier Li Qiang announced GDP growth, inflation, fiscal and employment targets broadly in line with consensus expectations. Specifically, policymakers aim to achieve GDP growth of “around 5%”, unchanged from 2023, a CPI inflation target/ ceiling of “around 3%”, “more than 12m” of new urban jobs, and a surveyed unemployment rate of “around 5.5%”. The positive messages for markets instead came within the details of Government Work Report, with policymakers prioritising issuing ultra-long special bonds over the next few years to help mitigate concerns over local government funding shortages amid weak land sales, while they no longer outlined “houses are for living in, not speculative” investment, suggesting further easing on the demand side for the property sector following the largest cut in the 5-year LPR rate used to set mortgage rates. Nevertheless, local assets struggled to rally on the news, a response likely motivated by underwhelming stimulus measures following the announcement of similar targets last year.

“Since the GWR was published, PBoC Governor Pan Gongsheng highlighted that there is still room to cut the required reserve ratio for banks seeing as the average RRR is around 7% when speaking at a joint press conference.”

This again suggests that policymakers will prioritise targeted liquidity measures to stimulate growth, as opposed to broader interest rate cuts to stimulate domestic demand. We suspect this will remain the case until the Fed begins its easing cycle as effective cuts to short-term interest rates risk fuelling capital outflow pressures once again, triggering further depreciation of the yuan. This has two readthroughs. Firstly, it should mean the PBoC keeps the 1-year medium term facility rate at 2.5% on Friday, suggesting unchanged loan prime rates the following week. Second, it means a sudden move lower in USDCNY will remain contingent on improving growth data or a sudden shift in Fed expectations. While we can't rule this out, we note that a growth-induced

rally in the yuan is unlikely to be a quick dynamic; while PMIs suggest growth conditions are improving, the signal is muddled somewhat by lunar new year effects and the PBoC's decision to cut the 5-year LPR by the most since its inception isn't suggestive of improving growth conditions. This means a short-term snap lower in USDCNY is largely contingent on expectations of Fed easing, and thus hangs on upcoming inflation data. While we can't rule out such a scenario, a break from the current "soft peg" regime is unlikely in our view. Nevertheless, short-term protection against such an outcome remains cheap given the exceptionally low level of vol.

Implied volatility on a 1-month 25 delta USDCNY put trades close to 5-year lows



The National Bank of Poland Governor just said that inflation has returned to target, why are they not cutting?

The short answer is we think they probably should be, at least on our read of the data. The longer answer is there are several risks and uncertainties over the inflation outlook that are making policymakers nervous, and they are taking a more conservative approach to monetary policy as a result. First off, it is worth checking in with what the latest data says. January CPI dropped sharply, from 6.2% YoY to 3.9% YoY. A large drop had been expected by markets as a sharp rise in CPI from last year's January price reset dropped out of annual calculations. Even so, the most recent set of outturns undershot expectations for a 4.1% reading, a theme of Polish disinflation this cycle. In the 15 releases seen since inflation peaked in October 2022, inflation has only surprised to the upside twice, with prints underperforming expectations by an average of -0.28pp. So whilst we agree with consensus that inflation is set to drop again when February's CPI print is released next week, we suspect that the balance of risks is skewed towards a downside miss when compared to the 3.2% print that

markets are currently looking for. Looking forwards, this is likely to fall further too. We think inflation may drop below the Bank's inflation target temporarily in March and April, as base effects from early 2023 continue to fall out of the annual figures.

Next week's data should confirm that inflation has now fallen to within the NBP's 2.5% +/-1% tolerance band. In fact Governor Glapinski noted as much in his press conference following the NBP decision this week. Not only this, but a new set of NBP forecasts saw a notable downgrade to the Bank's inflation outlook this week. These saw a 50% probability that annual price growth would be in the range of 2.8 - 4.3% in 2024, some way below the November projection of 3.2 - 6.2%. But from May onwards base effects are set to fuel a renewed surge in price growth. Moreover, policymakers have placed significant emphasis on the uncertainties generated by fiscal policy when it comes to the inflation outlook. This includes the expiry of a VAT exemption on food purchases that is due to occur in mid-2024, an event that the NBP estimates will add 0.9% to CPI alone.

"With this and other price freezes set to expire over coming months, this does admittedly risk another round of sharp price rises that could be embedded in underlying inflation dynamics."

However, given our view that inflation risks are skewed to the downside relative to consensus, we are less troubled by the impact of expiring price freezes than policymakers. We also suspect that the government is unlikely to allow all of these policies to expire simultaneously. Not only would it be fantastically unpopular, but politicians are well aware of the inflation risks this would pose. In our view, this likely influenced an intervention by Prime Minister Tusk that took place as the NBP was meeting this week, signalling that whilst he would allow the VAT rise to expire, the government would also look to assemble a package of measures aimed at mitigating the impact of rising prices. Nonetheless, monetary policymakers appear sufficiently concerned by this uncertainty to continue holding rates at the current 5.75% for the time being. We suspect that this will continue to be the case for at least another few months, at least until it is clear that the inflation risks are not quite as bad as many NBP members currently fear.

The BCB has seemingly been on autopilot with its easing cycle, when can we expect this to change?

Next week, the release of the February IPCA inflation data will likely bring back the debate on the future of monetary normalisation in Brazil. At its first meeting of the year, the BCB's Monetary Policy Committee (Copom) unanimously decided to cut the Selic rate by 50 basis points for the fifth consecutive time, to the current level of 11.25%. However, while the statement accompanying

the decision was still relatively comfortable with the evolution of core inflation, we believe that this time it was somewhat more conservative in acknowledging that, despite progress, the current situation “requires caution”, implying that there is still work to be done and that it is too early to claim victory. Although the statement also showed that all Directors expected the pace of rate cuts to be maintained for the foreseeable future should the Bank’s baseline scenario materialise, we continue to believe that a slowdown in the pace of rate cuts this year is more likely than ever, especially if the upward price pressures seen in recent months persist.

“The latest inflation reading for January came in higher than economists’ expectations, with headline IPCA falling only marginally from 4.62% in December to 4.51% at the beginning of the year, driven by a higher-than-expected monthly increase of 0.42%.”

Consequently, and despite the fact that the year-on-year reading marked the fourth consecutive decline, we continue to believe that much of this is likely due to positive base effects, a view confirmed by the rebound in the average monthly inflation rate from 0.24% in the third quarter to 0.42% in the fourth quarter. According to the note accompanying the data, all nine categories recorded increases in December, with Food and Beverages again being the fastest growing and contributing most to headline inflation for the second month in a row even though it had suffered sharp declines throughout the year. In addition, core services inflation, a measure closely followed by the BCB, continued to make a large positive contribution in January. Trends in data tend to turn sharply, and with the underlying pace of inflation remaining high, we suspect February’s data should add fuel to the debate over the optimal pace of monetary easing in the coming months.

While this wasn’t reflected in the February meeting’s rate statement, with BCB guidance suggesting that the current pace of rate cuts will be maintained at least until the May decision, Director Diogo Guillén noted this week that the board will henceforth assess whether this signal is appropriate at each meeting. “There seems to be confusion about what is forward guidance and what is interest rate setting [...] our forward guidance is conditional on the expected scenario, which markets ignore”, he said. Our reading of the situation suggests that the BCB has abandoned the previous “there is insufficient evidence to deviate from its current roadmap” approach and that it is looking to the strength of the ex ante rate, currently at 7.5%, to determine the optimal level of rates to keep inflation pressures contained without hampering growth further. Should February’s data cool more than expected, we believe it is possible to see a more determined tone from Copom at the 20 March meeting. However, an in line reading or a positive beat, specifically within domestic components, should raise the prospect of slower BCB easing as soon as Q2, an outcome that should be supportive for the high yielding BRL.

Is it too soon to start thinking about another bout of broad USD depreciation on earlier Fed easing and a soft landing outcome?

Price action in markets this week has generally gone against our expectation of broad USD appreciation. While the idea of Fed easing has received another boost as we expected, following more dovish commentary by Chair Powell and downwards revisions to January’s payrolls number, this hasn’t coincided with similarly dovish guidance by peer central banks, with both the BoC and ECB pushing market expectations of cuts towards June. Additionally, US data outside of the headline payrolls figure showed signs that US growth may be softening. Namely, the ISM services PMI cooled more than expected, with notable declines in employment and prices paid sub-indices. With little data released elsewhere, this suggests that we now find ourselves towards the middle of the US dollar smile, i.e. less US exceptionalism.

As this has corresponded with a more confident tone from Chair Powell, the market narrative has quickly shifted from fretting about “no landing” in the US back towards a “soft landing” outcome, prompting defensive positioning in the dollar to unwind, primarily against high beta and procyclical currencies. While this could extend over a tactical horizon, we are reluctant to turn structurally bearish on the dollar. While US growth may be slowing, ushering earlier Fed easing and dragging Treasury yields lower, higher for longer stances from the likes of the ECB and BoC suggest growth conditions in major DM economies outside of the US are likely to deteriorate, if their forward guidance is fulfilled. This leaves these respective central banks at risk of being forced into faster easing relative to the Fed in 2H24, meaning that while yield compression supports gains against the dollar in the near-term, the pain for currencies like the euro and the loonie is merely being delayed. With EUR and CAD two of the largest components within the DXY index, the prospect of a further DXY rally over the medium-term is not lost, although the dollar may find itself under pressure in the coming weeks. In fact, we think this risk will lead both respective currencies to underperform any subsequent dollar weakness in the short term.

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