FI and FX Daily Brief

FI and FX Daily Brief. JPY intervention and rising European yields

Summary

European government bond yields continued to rise yesterday, while it was a more mixed picture in the US. 10Y German government bond yields have now risen 50bp since early July, while 10Y Treasuries has risen almost 40bp. The German curve has steepened between 2-10Y as the 2Y German bond has risen 40bp. The US curve has also steepened some 10bp. Today, we have several Fed speeches ahead of the US labour market report tomorrow.

In the currency market, there is again speculation of intervention in the JPY as it has strengthened from almost 160.5 to 157.7. Japan has already spend some USD 96bn over the past month in defending the JPY according to the Ministry of Finance. EURUSD is trading around the 116-level.

Majors FX

EUR/USD ended yesterday's session back below 1.16 after spiking temporarily higher on rumors of possible JPY intervention during the afternoon. USD short-end rates have moderated relative to EUR this week, and EUR/USD FX forwards have reversed part of the rally seen after Kevin Warhs's Jackson Hole speech last Friday. ADP's August US private sector employment growth fell short of expectations at +38k (cons. +48k), while NY Fed's John Williams noted that it is 'not yet certain' whether the Fed will have to hike rates. Williams has been in the more dovish camp of the FOMC already in the past, but the remarks reminded markets that comments from hawks like Warsh and Hammack do not necessarily represent the views of the entire committee. In this morning's Nordic Outlook, we maintained our call for the first Fed hike in December. Today, we will keep a close eye on the Fed's Waller's remarks in the afternoon. We estimate that there are currently 3-4 hawks who will likely vote in favour of a hike in September, and we believe Waller could be one of the participants that end up deciding the outcome of the meeting. On the data front, we look out for US August Challenger Report for layoff announcements as well as the ISM Services index.

NZD/USD declined yesterday after the Reserve Bank of New Zealand (RBNZ) delivered a dovish 25bp hike. The move itself was widely anticipated and fully priced in ahead of the meeting, but surprisingly, RBNZ revised down their future rate path marginally. The updated rate path indicates two more rate hikes by end-2027, with around 20% implied likelihood for a hike in Q4. Governor Breman elaborated further at the Parliament select committee last night, saying that she 'expects core inflation to increase further' but also that the central bank 'can take time to assess the impact' of higher policy rates. We forecast NZD/USD remaining near current levels around 0.58 over the coming year.

The Bank of Canada (BoC) kept its policy rate unchanged at 2.25% yesterday, as widely expected and fully priced ahead of the meeting. The statement was broadly balanced but leaned slightly hawkish, with the BoC noting increased upside risks to inflation, while new US tariffs have made the growth outlook more uncertain. Markets focused more on the former, pushing BoC hike pricing higher and USD/CAD modestly lower. Still, with core inflation close to target and growth uncertainty elevated, we like our call for the BoC to stay on hold over the next 12M and see USD/CAD on an upward trajectory, supported by wide rate differentials and our constructive USD view.

Majors FI

Continued unrest between the US and Iran pushed European yields higher over yesterday's session. Bund yields gained about 3-4bp across the curve and the 10Y OAT yield crossed 4.25%. Brent crude remained around USD 95/bbl., despite China's President Xi offering temporary relief to energy markets, saying that he would work with Middle Eastern countries to safeguard the security of international shipping lanes and that external powers should abandon their double standards in the region. US Treasuries stayed flat due to weaker than expected ADP private sector employment growth of +38k in August (cons: +48k, prior: +46k), coupled with the Fed's Williams signalling that he does not see any urgency to hike with the trend in inflation slowly moving down. The BoC kept its policy rate unchanged at 2.25%, as widely expected and fully priced ahead of the meeting. The accompanying statement looked broadly balanced but with a slightly hawkish tilt from higher inflation risks.

Today, the Fed's Waller will be on the wires in the afternoon, and the final US Services PMI and Challenger layoffs report are set for release ahead of tomorrow's US Jobs Report. In the euro area, the final PMIs for August are expected to confirm the flash releases.

On supply, France will sell up to EUR 13.5bn in the long end of the curve, while Spain will sell in the 3Y to 9Y segment and the 15Y linker. Ireland is set for its second and last auction in Q3 and it will be interesting to see if the recent upgrade from Moody's to Aa2 (positive) will have an impact on demand at the auction. See more in our Irish Auction preview, 2 September.

Scandies

Danmarks Nationalbank (DN) resumed FX intervention in August. It sold DKK5.6bn in FX intervention on top of the DKK0.7bn intervention that took place in June. It was probably about in line with what the market expected. The upwards pressure EUR/DKK, and thus the need for additional FX intervention, has eased over the past week; hence, we do not think there is grounds for speculating in a near-term 10bp unilateral rate hike. The market discounts a small chance that DN hikes more next Thursday than the 25bp implied from following a similar hike from the ECB.

In conjunction with the Nordic Outlook released this morning, we make an adjustment to our Riksbank call and postpone the timing of our call for a rate hike in September to November. Subsequently, we expect a second hike in February to 2.25% (prev. December). We then expect the Riksbank to stay at 2.25% throughout 2027. Current market pricing is now exceeding our Riksbank call, and by some margin, with close to 100bp priced in for the coming year. From a risk/reward perspective, however, we are less convinced to go against current pricing. Especially as the energy market remains a clear driver of the front-end. On a relative basis, we see arguments for the Riksbank to deliver more hikes from here than the ECB.

The main drivers of recent SEK weakness are a cautious Riksbank, a stronger US dollar, and rising geopolitical tensions in the Middle East. Markets are increasingly pricing additional Riksbank hikes, but until the Riksbank validates those expectations through more hawkish communication and ultimately delivers the hikes we now forecast for November and February, the krona is likely to remain vulnerable. With the ECB set to move before the Riksbank, the policy rate differential could widen to a historically unprecedented 75bp, creating further upside risks to EUR/SEK. Meanwhile, the dollar has turned from a tailwind into a headwind for SEK as investors seek safe-haven assets with escalating geopolitical uncertainty.