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FX Daily: October Fed hike remains very data dependent

Pricing for an October Fed hike dropped to just below 50% after soft US consumer sentiment and JOLTS yesterday. Expect more front-end rate action today with PCE and ADP releases. However, the slump in long-dated bonds will keep heavily affecting FX. For now, it argues against any material dollar correction



The dollar jumped higher again yesterday despite soft US data

USD: Dollar strengthens despite soft data

The dollar jumped higher again yesterday. Rising back-end yields continue to weigh on global risk sentiment, with low-liquidity, higher-beta currencies bearing most of the brunt. The yen remains the sole exception to the broader dollar strength trend. Beyond the lingering threat of FX intervention, the unwinding of JPY-funded carry trades may also be providing support. The Swiss franc and Swedish krona have likely picked up some of that funding flow. After last Thursday's dovish SNB and hawkish Riksbank decisions, the CHF appears to face the greater downside risk.

At the same time, the dollar received some negative news yesterday. US consumer confidence fell sharply to 81.9 in September, well below expectations, and JOLTS job openings declined to

7,079k in August, also undershooting consensus. The latter reinforces our view that the August payroll print may have been overstated and could be revised lower on Friday.

The impact was visible in front-end rates, which moved lower alongside a modest decline in oil prices. October FOMC pricing fell 5bp to 12bp, its lowest level in around two weeks. That underlines just how data-dependent markets see the October hike decision.

Expect more front-end action today with the release of September ADP payrolls and August personal spending and PCE inflation. Core PCE is expected to rise from 0.2% to 0.3% MoM, in line with our forecast. While this is the Fed's preferred inflation measure, markets are likely to place greater weight on the September CPI release in a couple of weeks. Even so, a 0.4% MoM core PCE print could lift the October hike pricing again close to 20bp if supported by jobs figures too.

Some stabilisation in risk sentiment could take some shine off the dollar rally, but today's data will have a big say. With room for markets to reprice a higher probability of an October Fed hike, it may be premature to call the top in this dollar move.

Francesco Pesole

EUR: Testing new lows

EUR/USD finally fell below the summer lows yesterday. Spot dropped temporarily to 1.1310-20 before paring some losses, trading at 1.1350 this morning. We flagged yesterday how dovish-leaning remarks by Christine Lagarde were leaving the euro in a more vulnerable position, but this drop in EUR/USD appears entirely dollar-driven.

We don't expect another big break lower, as we still think the Fed will hike next only in December. But if US data is hot, the Fed hikes in October and stays hawkish, EUR/USD would be ready for another bearish leap, with risks potentially extending all the way to 1.10. Even lower oil prices might not help, as markets may be quicker to price out ECB tightening than the Fed's.

Let's see what French and German September CPI numbers look like this morning. Hotter-than-expected numbers like those released in Spain yesterday could prompt upcoming ECB speakers to offer a more hawkish tone, perhaps revamping bets on an October hike.

Francesco Pesole

PLN: Inflation surge puts rate hikes in focus

Today's September CPI flash estimate is likely to show a sharp rise in inflation. The expiry of the temporary fuel VAT cut in August, together with higher crude oil prices, pushed fuel costs to new highs in September. Food prices likely remained broadly stable as the previous fall in vegetable prices faded, while core inflation was probably little changed. We estimate headline

CPI increased from 3.4% to 4.2% YoY, clearly exceeding the upper limit of the National Bank of Poland's 2.5% +/-1 percentage point target range.

With global energy prices still rising, our economists yesterday revised their forecast and now expect inflation to remain above the tolerance band for at least four to six months. We expect the NBP to start raising rates early next year, delivering 50bp of hikes in total. However, the November inflation report and global developments will be decisive and could bring forward the first move. Markets already price around 135bp of tightening, far more than our forecast. Today's CPI release could therefore be pivotal: we see upside risk to consensus following several recent positive surprises.

Rates are not currently the main driver of EUR/PLN, but a hawkish CPI surprise could reinforce tightening expectations and strengthen the case for a full rate hike pricing for next week's October meeting. Yesterday's decline in energy prices may at least stabilise the zloty and allow a short-term move towards 4.360. Beyond that, however, the outlook remains bearish amid a stronger US dollar, persistently high energy prices and growing pressure on emerging market currencies.

Frantisek Taborsky

CEE: Energy risks keep forint under pressure

Elsewhere in the region, the calendar is limited to second-tier releases, including Hungary's PPI and the Czech Republic's final GDP data, which should confirm second-quarter growth of 1.9% YoY. Markets will focus instead on what Poland's inflation trend signals for the rest of CEE. Food prices have recently restrained regional inflation; although the expected reversal may come later than anticipated, inflation should still turn higher around year-end.

The broader market backdrop is unchanged, and we remain bearish on CEE currencies amid a stronger US dollar, high energy prices and persistent global uncertainty. EUR/HUF briefly rose above 368 yesterday, its highest level since early September, before retreating. The forint remains particularly vulnerable given crowded long positioning and Hungary's heavy reliance on energy imports. Without a meaningful drop in energy prices, we expect EUR/HUF to test 368–370, although levels near 370 may prompt more hawkish central-bank rhetoric and attract new buyers, in our view.

In Romania, today's government confidence vote is widely expected to fail, opening another chapter in Romania's political saga. Attention will then turn to the constitutional options, including whether a third nomination is possible and how President Dan responds. Markets are likely to expect the swift appointment of a candidate capable of securing a parliamentary majority. The renewed uncertainty could trigger another move higher in EUR/RON, although we would expect any increase to be relatively limited.

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