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FX Daily: Fed minutes shouldn't rock the boat

A hawkish dot plot in September suggests today s FOMC minutes shouldn't surprise on the dovish side. At the same time, softish post-meeting data probably raise the bar for a positive dollar reaction today. Eyes should remain on oil, which is back on the rise this morning, and France, which is enjoying some relief in sovereign spreads



The dollar may stabilise around current levels, but risks remain skewed to the upside

USD: Looking for clarity in the minutes

A rare good day for bonds let US stocks rise to new highs and left the safe-haven dollar weaker yesterday. Brent briefly fell below $100/bbl before recovering after reports that Iran had stepped up strikes on tankers in the Strait of Hormuz. Stubbornly high oil prices continue to reflect concerns about further disruptions, even as actual oil flows have improved. With few signs of an imminent deal, energy prices should remain a drag on any meaningful recovery in bonds and, by extension, on a decline in the dollar.

Attention turns back to the Fed today with the release of the September FOMC minutes. Markets are still looking for greater clarity on the data-policy reaction function, particularly which inflation outcomes would justify another hike this year. The minutes should also offer

some insight into any dovish dissent.

However, with the dot plot showing more members expecting two further hikes this year (4) than no further tightening (2), the scope for a dovish surprise appears limited. At the same time, data has been softish since the September hike and markets continue to firmly price a December move, setting a relatively high bar for a positive USD reaction.

We expect some stabilisation around the 102.0 area in DXY, but risks remain on the upside.

Francesco Pesole

EUR: Don't count on a French sentiment rebound

French bonds' premium shrank further yesterday, with the 10y spread to bunds tightening to 125bp. The move appeared to be driven primarily by an improvement in global bond market sentiment and, to a lesser extent, by Marine Le Pen's pledge to reduce the budget deficit sharply to 3.7% of GDP next year. One indication of a lingering French premium is the French-Italian 10y spread, which remains wide at 22bp and has only corrected 5bp from last week's peak.

While it's clear that Le Pen is attempting to establish herself as the market-friendly candidate, our macro team notes that her plan currently rests on ambitious spending-cut targets rather than a fully costed programme, with major uncertainties around how €140bn of savings, particularly on pensions, would be achieved. We therefore aren't convinced her words are enough to drive a material OAT recovery from here.

The euro welcomed tighter spreads, but the rebound has lost steam overnight on the back of higher oil prices. A return towards 1.1150/1.1180 remains the risk today. EUR/CHF has now recovered roughly half of its October losses, but a move beyond 0.940 would likely require a broader improvement in sentiment towards the French fiscal outlook, which still looks premature.

Francesco Pesole

SEK: Softer inflation shouldn't derail November hike plan

Swedish inflation for September surprised slightly on the downside this morning. Headline CPIF rose as expected to 1.5%, led by energy prices, but the core measure excluding energy stayed at 0.5% against expectations of 0.7%.

SEK's reaction has been muted, which is understandable considering the Riksbank has been taking low inflation with a pinch of salt given temporary dampening factors, and above all given the hawkish guidance in September.

We still expect a hike in November (now 18bp priced in), with a follow-up move in February. EUR/SEK has corrected following some idiosyncratic EUR weakness, but the external environment (oil, bonds) remains challenging for SEK, and the prospect of Riksbank hikes isn't enough to lift the currency by itself. We still expect a decline into year-end in EUR/SEK, but our 11.05 target is looking increasingly hard to reach, with 11.10-11.20 now more realistic.

Francesco Pesole

CEE: September inflation rebound

Following the inflation spikes seen in Poland last week and the Czech Republic yesterday, Hungary's figures were released this morning. We saw a rise from this year's low of 1.3% to 1.6%. As in the other countries, the main driver was higher fuel prices, although the increase came in below both market and central bank expectations. In its September forecast, the central bank had projected inflation to rise to 1.7%.

Later today, the National Bank of Poland will decide on monetary policy; we expect it to leave rates unchanged at 3.75%. Although September saw inflation jump to 4.0%, exceeding the tolerance band, new government measures and lower core inflation should allow the central bank to continue waiting. Continued hesitation by the NBP would thus signal a dovish stance, contrasting with current hawkish market pricing that anticipates around 100bps of tightening. Attention will then shift to the governor's press conference tomorrow.

Regional FX saw some relief yesterday amid a global market shift, with the forint emerging as the usual winner. However, ongoing tensions in the Middle East, elevated energy prices, and a strong US dollar keep us leaning towards a dovish outlook. If the NBP strikes a dovish tone in line with our expectations, it will renew pressure on the zloty, pushing it above 4.380.

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