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FX Daily: Dollar buying returns ahead of FOMC

The greenback has had a good start to the week – in our view, thanks to AI-sentiment stabilisation and some positioning ahead of tomorrow's FOMC announcement. Today, the focus will be on US consumer confidence, as well as Israeli elections and their potential impact on the Middle East equilibrium. In New Zealand, we expect a hawkish 25bp hike overnight



An improved AI-related mood is allowing a firmer dollar ahead of tomorrow's FOMC meeting

USD: Stronger into the Fed decision

The dollar has found good support early this week, as stabilising AI-related sentiment has allowed markets to reconnect with the broader supportive backdrop of a hawkish Federal Reserve and high energy prices. Pre-FOMC positioning may also be kicking in, with the forward-looking FX market viewing Chair Kevin Warsh's reiteration of inflation commitments as reinforcing the structural floor for the dollar. As discussed in our preview, we sympathise with this view and expect a broadly supported dollar this week.

Today, the US calendar is rather busy. The highlight is the Conference Board consumer confidence index, which surprisingly plummeted to 81.9 in September. We expect an 81.5

print; consensus is 81.0. Surprises here aren't likely to be enough to sway tomorrow's Fed tone, but pricing for further tightening has shown some fragility of late, and evidence of deteriorating consumer mood could enter the equation. The other releases are all lower tier: September's durable goods orders and new home sales, as well as the Richmond Fed manufacturing index.

Some focus will also be on early results from today's Israeli election. Polls point to a very tight contest between Prime Minister Benjamin Netanyahu's coalition and the opposition bloc led by Gadi Eisenkot. Both, however, are projected to fall short of a parliamentary majority and would require support from smaller parties.

Eisenkot has campaigned for a slightly more diplomatic approach towards Iran than Netanyahu's, focusing on blocking the nuclear programme while discarding the prospect of regime change in Tehran. A strong showing for the opposition bloc could lead to somewhat lower oil prices and a weaker dollar. However, markets will require much more in terms of peace prospects before pricing out geopolitical risk.

Francesco Pesole

EUR: Falling back on USD strength

After being only modestly touched by last week's new round of French bond turmoil, the euro is understandably getting very little from the OATs relief rally after Moody's kept the rating steady at Aa3 on Friday.

EUR/USD retains a short-term undervaluation of around 1.0-1.5%, widely attributable to France. However, indications are that spreads need to widen quite significantly from the current 153bp to trigger another big EUR drop.

The eurozone calendar is light today. Another strong survey (the Ifo) added to evidence that eurozone resilience is extending into 4Q. We expect a hold on Thursday by the European Central Bank, and expectations for a big dovish shift on the back of France don't look justified in our view.

EUR/USD probably retains some downside risks at these levels as the dominating USD leg may find a bit more support ahead of Wednesday's FOMC. The next key support is at 1.110, the 14 October low. For now, we don't see it breaking below that mark.

Francesco Pesole

NZD: RBNZ to hike overnight

The Reserve Bank of New Zealand announces policy at 01:00am GMT tomorrow. As discussed in our preview, we expect a 25bp hike to 3.0%, in line with consensus and market pricing

(23bp).

Since the dovish September hike, higher energy prices, a weaker New Zealand dollar, and rising global rates have all argued for faster action by the RBNZ, even though 3Q inflation came in below expectations. Officials shifted to a markedly more hawkish tone in the past few weeks, and we see a low chance they will surprise with a hold tomorrow.

We also think the tone of the statement will be hawkish, signalling further tightening ahead. Policymakers may be attempting to validate market expectations for now, even if they have little confidence in delivering the 100bp priced in for the next 12 months. That's because with no new projections being published at this meeting, they won't risk sounding committal on a rate path, and they are probably aiming to prop up the currency to reduce imported inflation.

We see a bit more upside for NZD/USD into year-end, with the hawkish RBNZ playing a role. But we aren't convinced the next hike will come in December in New Zealand, and we are therefore sticking to a 4Q forecast of 0.570.

Francesco Pesole

CEE: Rates reconnecting with higher energy prices

The region opened this week with rates catching up to rising energy prices. The correlation between rates and energy prices has weakened in recent weeks; based on patterns from previous months, CEE rates should be higher. Still, the CEE region cannot escape the bond market turmoil seen in the eurozone, particularly in France, or growing concerns regarding a regional recession. Nevertheless, GDP growth in the region has been somewhat stronger than in the eurozone, and we continue to view inflation as a more pressing issue locally.

Consequently, we believe rates are more likely to follow energy prices upward than to decline due to recession fears. The regional calendar is essentially empty until Friday, when inflation data for Poland and GDP figures for the Czech Republic and Hungary are due to be released.

In the CEE region, FX markets saw some stabilisation yesterday following Friday's sell-off, though negative global conditions remain largely unchanged. In the coming days, the direction will naturally be influenced by the Fed and ECB meetings, as well as any new developments regarding the US-Iran conflict. That said, we believe CEE currencies face greater downside risk than upside potential.

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