

Mizuho Daily Currency Watch

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MIZUHO

Colin Asher

Senior Economist

colin.asher@mhcb.co.uk | +44 20 7012 5262/+44 7387 139164

Currency	Main focus of the week (S-T view)
EUR	High core inflation, low unemployment to keep the hawks in control
USD	USD surge looking a little stretched
JPY	Solid data to support JPY
GBP	NI deal not likely to provide much upside for GBP

Overnight comment – Mixed Japan data leave JPY little changed

US shares recorded modest gains. Most Asian indices gave up early gains to end only slightly higher. The Topix ended virtually flat. Whilst UST yields edged higher during Asian trade they remain well off yesterday's highs. After the big drop late yesterday, the DXY index nudged higher during Asian trade. Japanese data were mixed, with a very weak industrial production (-4.6%MoM) report offset by a strong retail sales report (+1.9%MoM) and solid housing starts (+6.6%YoY). The production decline was driven by autos and chips. The BoJ's offer to lend ¥1trn 5yr funds to commercial banks drew a little over ¥3trn of bids. 30yr JGBs continued to rally. **USD/JPY was little changed and sits at 136.40 as Europe opens.**

In Europe the main focus is on the Windsor Framework, which detail changes to trading arrangement in Northern Ireland. Whilst the political relationship appears much improved the economic gains from the agreement are small. Yesterday both EUR and GBP rose vs USD but both have given back a little ground in Asian trade. ECB Chief Economist Lane said that the peak in rates may endure for "a fair number of quarters". He also reiterated the importance of core inflation and said there was evidence that high policy rates were having an impact, which puts him at odds with the hawks such as Nagel. **EUR/USD is around 1.0590, while GBP/USD is around 1.2040, as European trade gets underway.**

Today's Major Events and Data Releases

Events over coming 24 hours	Survey/Prev
US – Trade balance (\$bn, Jan)	-91.0/-89.7
US – House prices (%YoY, Dec)	4.70/6.77
US – Consumer confidence (DI, Feb)	108.5/107.1

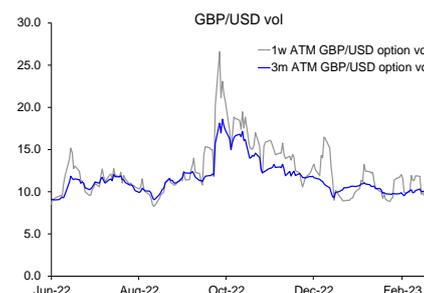
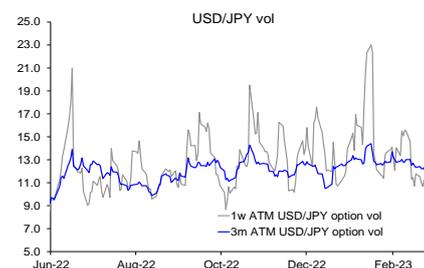
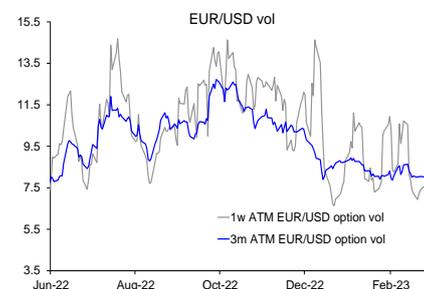
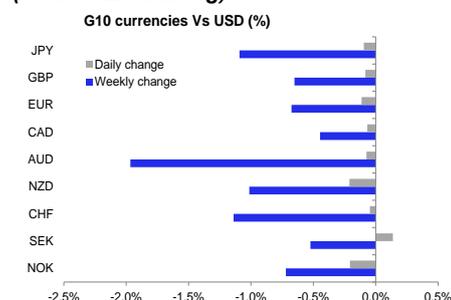
Source: Bloomberg

Europe. National CPI data in France and Spain are due. Neither release is seen delivering good news. On the policy front the ECB Vujcic speaks. His commentary rarely moves markets. For the BoE - Pill and Mann speak. Mann speaks on an EIB panel on the interaction of monetary and fiscal policy and financing conditions. It is an important topic and the speech may have implications beyond policy in the UK.

US. Trade data, house prices and consumer confidence are all due. House prices are falling rapidly. They have printed negative MoM growth for 5 consecutive months. The YoY rate is expected to drop below 5% for the first time since August 2020 and further declines seem likely in coming months. The conference Board consumer confidence is set to push higher given the strength of the labour market. The Fed's Goolsbee, the new President of the Chicago Fed, speaks today. To date his policy commentary has been limited so his comments, to the extent he discusses policy, should be of interest, especially as his name has been floated as a possible replacement for Lael Brainard.

Market Summary

(Source: Bloomberg)



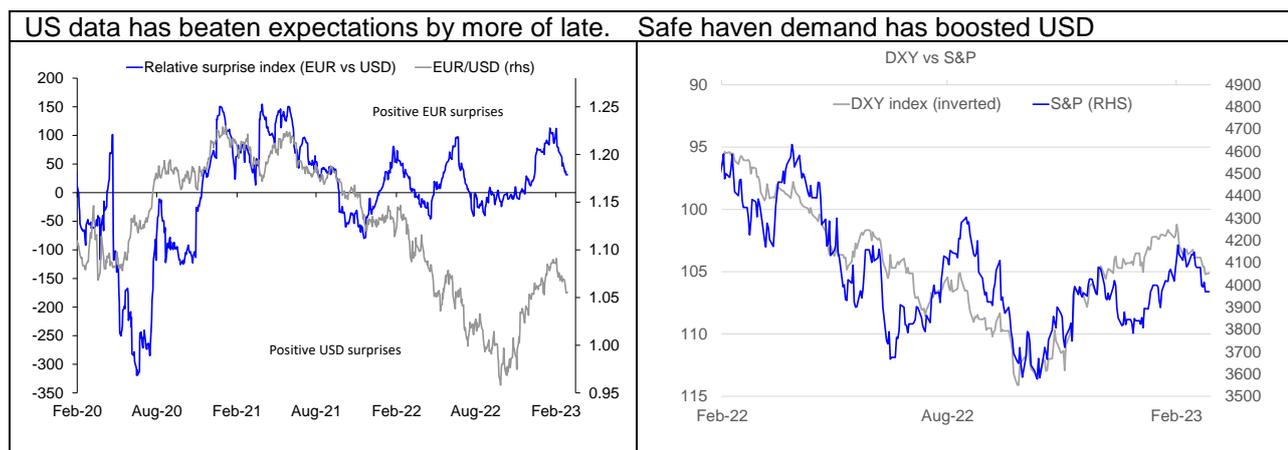
Currency comment(s)

EUR to remain under pressure short term. Better prospects in the medium term

The data in both the US and the Eurozone have been very good this month – kicking off with the rebound in the non-manufacturing ISM in the US, which was followed up by the blockbuster payrolls report for January. A look at the surprise indices (see chart below left) shows that US data have beaten expectations by more in recent sessions and EUR/USD has dipped alongside the relative move in 2yr yields, which has been UST yields rise by more in February. 2yr UST yields are up a little over 60bp over the last month, while 2yr Bund yields are up a little over 40bp. The rise in yields has also hit risk appetite and the S&P has dropped ~2.0% this month, knocking 1/3 off its year to date gains. This slide in risk appetite has provided safe haven support for the US dollar. Finally, US real yields have pushed higher through February, lifting the DXY index.

Whilst on the central bank front, FOMC hawks Mester and Bullard have gained plenty of attention with their call for bigger rate rises, we see them as outliers in the policy debate. In addition, neither vote this year. The bulk of the FOMC seem content to hike in 25bp increments and in our view something close to the December Dot Plot remains the central view of most FOMC members. Markets are pricing in 3 additional hikes. We see just 2 more – in March and May. By the time of the June FOMC we expect that activity will be more obviously softening and inflation risks will have eased somewhat.

In contrast, the ECB policy debate is a lot less settled. The uber hawks such as Nagel continue to see policy as not yet restrictive. Schnabel, who has a solid hawkish bias but is not as hawkish as Nagel, thinks it is possible that rates are not yet restrictive while some of the more dovish members think we are already in restrictive territory. There is a strong consensus on a 50bp hike in March but what comes after is much less certain. The likes of Nagel are pushing for another 50bp. We suspect that Lane and Lagarde will be able to rein in the hawks and will deliver a 25bp hike in May and another in June – taking the depo rate to a peak of 3.5%. In the short run, we envisage that risk appetite will remain muted, while UST yields nudge a little higher but the peak for 2yr USTs seems close and once yields start to drop, the DXY index will struggle to move higher.



Source: Bloomberg

FX forecasts (as of 23 Feb)	Current	Q2 23	Q3 23	Q4 23	Q1 24
USD/JPY	135	129	124	122	120
EUR/USD	1.06	1.09	1.12	1.14	1.15
GBP/USD	1.20	1.23	1.28	1.30	1.32
EUR/GBP	0.88	0.89	0.88	0.88	0.87
EUR/JPY	143	141	139	139	138
GBP/JPY	162	159	159	159	158

Source : Current - Bloomberg; Forecasts – Mizuho

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