Dollar is back in demand after turmoil in USDJPY overnight

17th June 2022

GBP

After being whipsawed around in the aftermath of the Bank of England meeting, the pound soon settled on its direction of travel. With rates markets emboldened by the tweak to the Bank's forward guidance that implied a more aggressive path consisting of larger-than-25bp hikes could be in store, the pound continued to travel higher against both euro and dollar. Upon market close, GBPUSD notched another 1.4%, compounding the post-Fed rally of 1.5% on Wednesday. Not only were UK rates emboldened by the BoE meeting minutes as the UK terminal rate drifted up to 3.5%, but sell-side analysts also started to issue notes predicting a 50bp hike at August's meeting. This morning, the pound is struggling to maintain the upward momentum of the past two sessions as market risk conditions shift. Following a spike higher overnight in USDJPY which triggered a broadly stronger dollar in G10 FX markets, the pound has retraced half of yesterday's rally. With May's retail sales data delayed until next Friday, the data calendar is light for the pound for the remainder of the week.

EUR

The single currency has largely followed the broader move in G10 markets against the dollar over the past 24 hours, despite conflicting messages from ECB officials overnight. The most notable headlines from the central bank came from President Lagarde herself, who said that the new anti-crisis tool that staff have been instructed to curate would kick in if borrowing costs for weaker nations rise too high or too fast. This morning, in response to Lagarde's statements, the spread between Italian and German bond yields has partially narrowed. However, despite this being a supportive factor for the euro, the single currency is trading lower this morning as the dollar goes broadly bid heading into the weekend.

USD

Mild dollar depreciation in the wake of Wednesday's Fed meeting was extenuated on Thursday as lower Treasury yields narrowed spreads across G10 rates markets, especially following hawkish pivots from the ECB, the BoE and the SNB over the past week. USD depreciation occurred despite a rout in US equities, which usually supports the dollar on haven flows. Recession risks will now play an integral part in broader market price action, and with the Fed underpinning a broadly highly front-end Treasury yield, the dollar's decline from recent highs shouldn't be too aggressive in the near-term. Today, with turmoil in Japanese markets overnight, the dollar is back trading on the offensive. In the economic calendar, events are light in the US with just Chair Powell's welcoming comments at a dollar conference standing out at 13:45 BST.

CAD

Yesterday was a quiet one for the loonie, with USDCAD retracing 0.45% to trade at roughly the same level it was trading at prior to the Fed's "dovish 75" and subsequent USD selloff on Wednesday. The Canadian dollar's underperformance stemmed from poor risk sentiment as US equities tanked between 3-4% on the day. Today, with risk sentiment remaining poor in markets and the dollar broadly stronger, the loonie continues to weaken. However, given yesterday's isolated CAD weakness in the G10, the loonie's losses this morning are minimal relative to peers.

FX Elsewhere

The Swiss National Bank unexpectedly hiked rates by 50bp on Thursday, taking the interest rate on sight deposits to -0.25%. The rationale behind their decision was to "counter increased inflationary pressure", which in this context denotes a policy of supporting a stronger franc to avoid importing excessive inflation from the eurozone. Governor Jordan went one step further in the SNB's press conference as he introduced two-way risk to the Bank's FX intervention policy, stating that the central bank would consider selling FX to strengthen the franc. This marks a stark shift in the Bank's previous policy, which intervened in FX markets to offset excessive CHF appreciation. In response to the SNB's actions, the Swiss franc appreciated over 2% against both the dollar and euro during yesterday's session. Despite closing marginally lower, the 1.81% rally against the euro still marks the largest one-day drop in EURCHF since 2015. Our call for parity over the coming quarter is alive and well.