# Dollar weakens in European session ahead of key CPI report

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## GBP

The pound has seemingly stabilised after Thursday's Bank of England induced sell-off. This has invited speculation around GBPUSD reaching a potential bottom, following a near 8% slump since early April. While we note sterling's resistance to plumbing even lower over the past few sessions, the pound's stability has come amid a lull in the economic calendar. Today's US CPI release could be the first big test for the pound, especially as the dollar is sold against G10 currencies this morning in anticipation of the inflation report showing price growth peaked in March. A stronger than expected reading is likely to test whether markets have seen the bottom in GBPUSD, while a slip in core CPI MoM is likely to give sterling bulls the green light to push the currency back towards ranges seen before Thursday's Bank of England meeting. The pound will then be tested again in quick succession as activity data for Q1 and March is released on Thursday morning. Outside of the economic calendar, political developments must also be eyed as Downing Street is yet again threatening to unilaterally suspend parts of the Northern Ireland protocol" a move that would spark trade frictions with the EU at an unwelcome time for both parties.

## EUR

Similar to the pound, speculation over a bottom in EURUSD has been rife after the currency pair has traded in a 1.5% range since late April amid heightened G10 FX volatility. Again, today's CPI data out of the US will be another test for this narrative, as will the progression of the EU's attempt to conduct a full embargo on Russian oil. In addition to this, EUR traders are monitoring the flurry of central bank communications coming out of the ECB this week. While consensus has largely formed around a rate hike as soon as July's meeting and expectations have firmed around 85bp worth of hiking from the ECB this year, stray comments are likely to still cause market volatility as they have recently from Fed officials. Outside of a celebratory event for Slovenia's central bank, which is hosting speakers such as Lagarde and Muller, ECB board member Schnabel is set to speak at 13:20 at an Austrian central bank event.

## USD

Turnaround Tuesday didn't last long yesterday as the rally in US equities tailed off towards the back-end of the session. Just the tech-heavy NASDAQ index and the S&P 500 posted marginal gains on the day as industrials continued to slump following Monday's broad equity market rout. For FX markets, the swings in equity markets meant the dollar remained firm in a session that was largely defined by tight intraday trading ranges, especially across the European session. The limited intraday volatility was notable, especially after the past few weeks when a percentage point move in G10 currency pairs started to become the norm, while it also occurred at a time when a slew of Fed speakers hit the wires. Broadly speaking, the narrative from the cohort of Fed speakers was that two back-to-back 50bp hikes by the US central bank in June and July are quickly becoming the committee's base case. However, dovish commentary about the path of rates thereafter, especially in the context of how well the Fed can bring inflation back to target without inciting a recession, acted as a counterweight to the near-term message. This meant that Treasury yields traded in a relatively tight range too. Volatility has returned overnight, however, with the greenback sitting under pressure ahead of April's US CPI report at 13:30 BST. Currencies with depressed valuations, such as NOK, AUD and GBP, are leading gains against the dollar this morning. This dynamic could be extended throughout the day should April's CPI data show a sharper than expected slowdown in price growth in the US. With favourable base effects set to come into play today, bringing the year-on-year rates down from 8.5% and 6.5% for the headline and core measures, focus will be on monthly price gains. Core inflation is set to print at 0.4% MoM, up 0.1 percentage points from March's reading, while headline inflation is set to fall from 1.2% MoM to just 0.2% due to the moderation in global energy prices after March's war-induced spike. The pace of price growth within the core measure, and specifically services inflation, will be what determines the market reaction. While a substantial slowdown in price growth in services is a left-hand side tail risk, it could transpire due to the wider than usual forecasting errors. This would prompt a dovish repricing of Fed expectations for the July and September meetings, which would weigh on the greenback in the short term.

## CAD

The Canadian dollar edged lower on Tuesday, moving in tandem with all but one G10 currency against the US dollar. Markets twisted and turned during the day amid a lack of high-impact data but ample "Fedspeak" from top Federal Reserve officials. Early in the day, positive sentiment in equities and equity options-implied volatility spilt into a stronger loonie, but the tides turned after Cleveland Fed President Loretta Mester said a 75 basis point interest rate hike wouldn't be ruled out forever. While that's not inconsistent with Powell's market-moving comments in the post-rate decision press conference last week, who said that 75bps weren't being deliberated "at that time", the comment weighed on the equity market rally and thus the rebound in market risk sentiment. Market participants have repeatedly overreacted to stray comments from central bankers, taking away stronger inferences than intended. On today's calendar, US CPI at 13:30 BST/8:30 ET will be the big event of the week. This morning, the loonie is trading 0.2% higher in anticipation of the release, which could see some of the dollar's shine rub off.