Week Ahead

4th - 8th March 2024

Time to pick up the pace

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INTRODUCTION

The week just gone saw another period of muted dollar price action play out. Peak to trough, the trading range for the DXY index was just 0.6%. That being said, this was hardly a surprise. A barren US data calendar and little new for Fed speakers to talk about meant that subdued greenback volatility was always the most likely outcome. Consequently, the focus for FX markets lay outside the US this week, with consequential data releases out of Japan, Canada and the Eurozone the major focus. In Japan, inflation data was at the centre of attention. CPI readings continued to ease, but less than expected. This keeps the BoJ on track to abandon yield curve control in April, provided Shunto negotiations indicate that inflation has been successfully embedded in wages, a point the BoJ governor Ueda also appeared to confirm this week. In Canada GDP data was the highlight of the week. Whilst a strong headline print initially saw the loonie rally, soft details in the report soon saw this move reversed. In fact, when accounting for the rate of population growth, this week's data still shows a per capita recession is still underway in Canada, which should continue to weigh on price growth. Eurozone inflation was the final big event of the week. That said, it largely proved underwhelming for FX markets. A small beat to the upside still leaves price growth on track to undershoot ECB forecasts, leaving the data broadly net-neutral for markets.

Next week activity should ramp up again for FX traders. Key central banks meetings for both the BoC and ECB are set to steal the limelight alongside a new round of jobs data out of North America on Friday. Both central bank meetings are likely to be dominated by speculation over the prospects of their easing cycles commencing in April. While we think policymakers will be wary to indicate that much, we think they won't discredit any speculation of earlier easing either, with both economies growing far below potential and this cyclical weakness likely to translate into faster disinflation. Following the decisions, the emphasis will then flip to the North American labour market, where US and Canadian jobs data will be scoured to clear up some of the inconsistencies in the January editions. Nevertheless, the data is unlikely to pack the same punch as previous versions given another round of labour market data is due before the Fed and BoC meet in early Q2. Ahead of that, however, the focus will be squarely on Switzerland at the start of the week. Short CHF positioning has been of increased focus since the SNB's dovish turn in December, with that view compounded by softer January inflation despite an increase in tax rates. If February's CPI data shows similarly benign domestic inflation pressures, even as the economy continues to grow at a steady rate, then a 25bp cut from the SNB on March 21st will be viewed as a foregone conclusion by markets, pushing EURCHF into a higher trading range of 0.955-0.97. In addition to the aforementioned events, traders will also receive a fresh budget decision from the UK government, where we expect few giveaways, while developments in Mexico and Poland will be key for the high yielding currencies.

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ECONOMIC CALENDAR

All times in GMT

Monday 04/03

Time	Country	Event	Period	Estimate	Prior
00:00	Australia	Melbourne Institute inflation MoM (YoY)	Feb		0.3% (4.6%)
00:30	Australia	ANZ-Indeed job advertisements MoM	Feb		1.7%
06:25	Switzerland	SNB publishes 2023 results			
07:00	Turkey	CPI MoM (YoY)	Feb	4.00% (66.20%)	6.70% (64.86%)
07:30	Switzerland	CPI MoM (YoY)	Feb	0.5% (1.1%)	0.2% (1.3%)
09:00	Switzerland	Domestic Sight Deposit change	Mar 1		471.4b
09:30	Eurozone	Sentix investor confidence	Mar	-11.0	-12.9
23:30	Japan	Tokyo CPI YoY	Feb	2.5%	1.8%

Tuesday 05/03

Time	Country	Event	Period	Estimate	Prior
00:01	UK	BRC Sales like-for-like YoY	Feb		1.4%
00:30	Singapore	S&P Global PMI	Feb		54.7
01:45	China	Caixin PMI composite	Feb		52.5
		Caixin PMI services	Feb	52.9	52.7
04:00	Japan	Governor Ueda speaks at Fin/Sum 2024			
08:15	Spain	HCOB composite PMI	Feb		51.5
		HCOB services PMI	Feb		52.1
08:45	Italy	HCOB composite PMI	Feb		50.7
		HCOB services PMI	Feb	52.3	51.2
09:30	South Africa	GDP QoQ (YoY)	Q4	0.3% (0.9%)	-0.2% (-0.7%)
13:00	Brazil	S&P Global composite PMI	Feb		53.2
		S&P Global services PMI	Feb		53.1
14:30	Canada	S&P Global composite PMI	Feb		46.3
		S&P Global services PMI	Feb		45.8
15:00	US	ISM services PMI	Feb	52.9	53.4
		Factory orders	Jan	-2.2%	0.2%

Wednesday 06/03

Time	Country	Event	Period	Estimate	Prior
00:30	Australia	GDP QoQ (YoY)	Q4	0.3% (1.4%)	0.2% (2.1%)
07:00	Germany	Trade balance	Jan	21.0b	22.4b
10:00	Eurozone	Retail sales MoM (YoY)	Jan	0.0% (-1.4%)	-1.1% (-0.8%)
12:00	US	MBA mortgage applications	Mar 1		-5.6%

Time	Country	Event	Period	Estimate	Prior
	Mexico	Consumer confidence	Feb		47.1
13:15	US	ADP employment change	Feb	150k	107k
14:45	Canada	Bank of Canada rate decision		5.00%	5.00%
15:00	US	JOLTS job openings	Jan		9026k
		Fed Chair Powell testifies in Congress			
15:30	Canada	Governor Macklem gives press conference			
19:00	US	Fed Beige Book			
23:30	Japan	Labor cash earnings YoY	Jan	1.3%	0.8%
TBA	Poland	National Bank of Poland base rate		5.75%	5.75%

Thursday 07/03

Time	Country	Event	Period	Estimate	Prior
00:30	Australia	Trade balance (AUD)	Jan	$11.5b	$1.09b
06:45	Switzerland	Unemployment rate	Feb	2.2%	2.2%
07:00	Germany	Factory orders MoM (YoY)	Jan	-6.0% (-4.6%)	8.9% (2.7%)
09:30	UK	DMP 1Y inflation expectations	Feb		3.4%
12:00	Mexico	CPI MoM (YoY)	Feb	(4.42%)	0.89% (4.88%)
		CPI Core MoM (YoY)	Feb		0.40% (4.76%)
13:15	Eurozone	ECB deposit facility rate		4.00%	4.00%
13:30	US	Unit labour costs	4Q F	0.7%	0.5%
13:45	Eurozone	President Lagarde gives press conference			
15:00	US	Fed Chair Powell testifies in Congress			
TBC	China	Trade balance YTD CNY	Feb	1.5%	

Friday 08/03

Time	Country	Event	Period	Estimate	Prior
00:01	UK	REC UK report on jobs			
07:00	Sweden	GDP MoM (YoY)	Jan		-0.3% (-0.1%)
07:30	Hungary	CPI MoM (YoY)	Feb	(4.2%)	0.7% (3.8%)
10:00	Eurozone	GDP QoQ (YoY)	4Q F	0.0% (0.1%)	0.0% (0.1%)
12:00	US	Fed's Williams participates in moderated discussion			
13:00	Poland	NBP minutes			
13:30	US	Nonfarm payrolls	Feb	190k	353k
		Unemployment rate	Feb	3.7%	3.7%
		Average hourly earnings MoM (YoY)	Feb	0.3%	0.6% (4.5%)
	Canada	Net change in employment	Feb	21.4k	37.3k
		Unemployment rate	Feb	5.8%	5.7%
		Hourly wage rate	Feb	5.1%	5.3%

DATA PREVIEWS

UK budget: No room to manoeuvre

March 6th is likely to mark the last fiscal event before the UK heads to the polls for a General Election. Normally this would set the stage for a raft of fiscal giveaways as the Chancellor tries to woo floating voters. Not so much on this occasion though, we think. Broad consensus expects that Jeremy Hunt will have limited room for fiscal manoeuvre in his Spring Budget. Significantly, headroom against the Chancellor's fiscal target was just £13bn in November, barely a rounding error in context. As such, next week's pageantry is set to bring few meaningful changes and a whole lot of window dressing, likely to tell us little new about the UK's future fiscal prospects, but much more about where the government would like to draw battle lines for the upcoming election

"From a market point of view, we still expect some modest giveaways, which should add fractional upside for both growth and the pound. But the key determining factor in what the Chancellor can deliver is set to be latest set of forecasts from the OBR."

We think they could potentially upgrade forecasts for both potential economic growth on the back of higher immigration, and downgrade the profile for Bank Rate, both of which could free up extra cash for the Chancellor to spend. Our prior base case had been for these changes to leave the Chancellor £25-£30bn to give away next week. But recent speculation suggests that the OBR is likely to be even less generous than our initial estimates suggest, meaning the scope for pre-election spending is set to be tightly restricted. In particular, there is a risk that the OBR pencils in a rise for the long run cost of government borrowing, an outcome that could see much of the Chancellor's headroom gain evaporate.

Given this minimal fiscal wiggle room, market attention is most likely to rest on any potential risks around the timing of the election. In our view this is most likely to be held in early Q4, but a budget that supported this rationale would help crystalise this risk for markets, removing a source of potential uncertainty that could have weighed on the pound. That said, whilst not our base case, if the OBR is sufficiently miserly with their projections, it could push the Chancellor to offer no giveaways at all and instead try to hold another fiscal event later in the year in the hopes of a better set of forecasts, pushing back the potential timing for the general election. The lack of additional spending would be a negative surprise for markets under such a scenario too, likely seeing a modest sell-off in the pound. What we don't think is likely, however, is a repeat of the Truss-Kwarteng budget of 2022. The Chancellor appears to have learnt from his predecessor's mistake and is highly unlikely to try ditching his fiscal rules again, though memories of the event could temporarily weigh on sterling next week in advance of the Chancellor's appearance in Parliament.

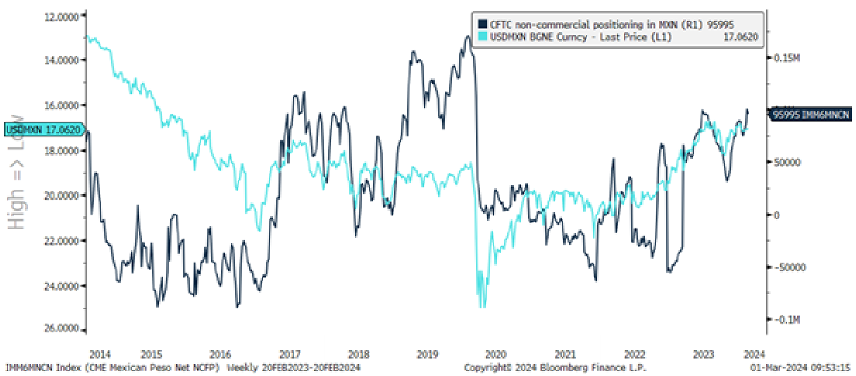
Inflation dynamics in focus for EM FX

Next week, the NBP is due to announce its latest policy decision on March 6th. Based on the recent hawkish commentary emanating from Bank officials, we expect the MPC to hold rates at 5.75%. We had speculated previously that an updated set of inflation forecasts set to be published alongside the decision would allow the NBP to cut rates at this meeting, an outcome that remains a risk to our call. On this point, we still think the Bank will need to significantly downgrade its short-term inflation projections to reflect the recent softer-than-expected evolution of price growth. Significantly, headline price growth was just 3.9% in January, only just outside the NBP's 2.5 +/-1% tolerance band. But this looks likely to be balanced against an emphasis on inflation risks later in the year stemming from the expiry of price controls. These have become a focus for policymakers across recent commentary, with this change in tone suggesting to us that a continued hold in rates is the most likely outcome of the meeting next week. This view is similarly shared by markets too. All 13 economists surveyed by Bloomberg expecting the NBP to keep rates unchanged.

"If this plays out, then Wednesday's meeting should have limited impact on the zloty, though PLNs elevated carry protection should see it continue to outperform peers across CE3 FX."

Similar to the zloty, the Mexican peso also faces a test next week, with risks that February's inflation data could erode MXN's level of expected carry, leaving it susceptible to a significant positioning unwind. This is because there is a risk that Banxico could cut this month, although the minutes of the January meeting highlight that policymakers would need to see substantial improvements in core inflation if this is to be the case given that they viewed inflation risks overall as tilted to the upside. In our view, the likelihood of a March cut still looks slim, seeing as the labour market remains significantly tight, the economy likely continues to operate at an above-potential rate despite the growth slowdown in 4Q23, and data from the first fortnight of February showed core services inflation remains above historical averages. Accordingly, we think Banxico will likely wait until May before easing rates. But there is a risk that any negative surprise in the February data forces markets to position more aggressively for a March cut, leaving the peso vulnerable.

Long positioning in MXN remains stretched as traders seek carry in low vol environment



In terms of the data, while headline inflation is likely to fall further on a year-on-year basis seeing as it fell by -0.10% in the first fortnight of the month and base effects are fairly large at 0.55%, this isn't a foregone conclusion. Notably, the pace of sequential inflation has accelerated since November, and the 2w/2w decline comes off the back of a particularly strong January print of 0.89%. Should headline inflation not fall that much from January's print of 4.88%, the debate over a March cut will likely be closed shut. If expectations are met, however, and headline inflation does in fact fall closer to 4%, the strength of core inflation will prove key.

"Although core disinflation continued in early February, the 2w/2w rise of 0.24% suggests to us that the bar for rate cuts remains high, but this is not an outcome that can be entirely ruled out."

North American jobs: The one before the import one

With both the Bank of Canada and the Federal Reserve set to keep policy on hold in March, and with another round of labour market data due either side of the border before the prospect of rate moves come back into focus in early Q2, next week's jobs reports don't hold that much firepower for markets. That said, they won't necessarily be completely disregarded either.

In the US, traders will be paying particular attention to whether January's bumper employment gain was indeed a case of seasonal factors that econometric models are struggling to smooth out or if labour demand in the US is actually reaccelerating. Initial jobless claims data over the course of February doesn't shed much light on this, with the monthly average rate of initial jobless claims remaining near historic lows and rising only 4k on the month.

"That said, we think a repeat of January's monster print is unlikely, with the data likely to mean-revert towards its 23H2 average pace of 220k or just below. The extent to which the data snaps back will be key for markets, however."

A print north of 200k will likely endorse the current market pricing of the Fed's easing cycle as employment growth would continue outpace labour supply. A number in the region of 180k would likely see trades re-examine the prospect of a May cut, increasing the probability from 28% currently to just shy of a coinflip. In the extreme, which we don't think is likely, a sub-160k reading would likely ignite panic in markets, bringing into question whether the terminal rate in the US is in fact as high as markets have recently begun to believe. The details of the jobs report will also be closely monitored given the composition of January's report was also firm – employment gains were largest in industries oriented towards consumer demand and discretionary spending, while wage growth also printed strong at 0.6% MoM.

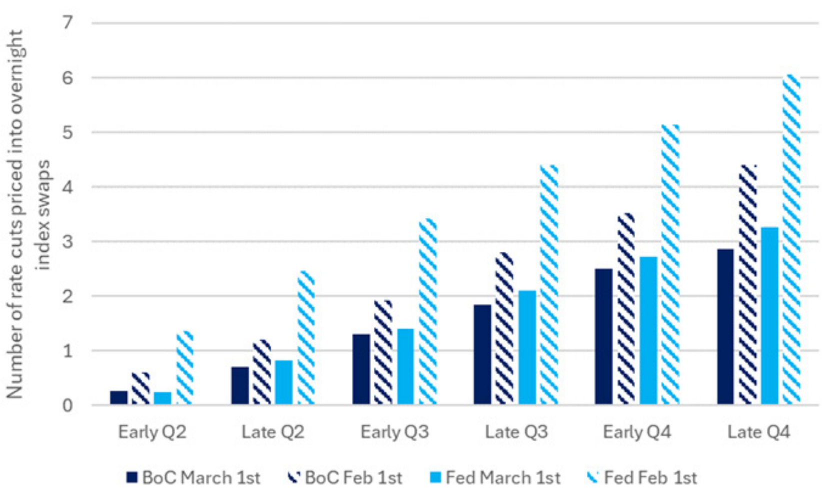
Traders will also be looking for clarification in the Canadian numbers after January saw the once-reliable LFS report succumb to the noisy trend in the Canadian data. Having consistently shown slack re-emerging in the labour market, driven by layoffs in cyclically sensitive industries and employment growth undershooting population growth, January saw 37.3k jobs added. Granted, the composition was soft with all of the net employment increase isolated to part-time positions, and most likely in consumer-services given the recent trend in layoffs, but even so, the conflicting signs within the data suggest the BoC should tread with caution. With all inflation metrics now trending in the same constructive direction, it is now down to the labour market to give the BoC confidence that it can cut rates. As mentioned, this is just the first of two editions that the central bank will have at its disposal before April's decision, but given expectations of Fed easing have recently been delayed, we think the BoC will likely need both labour market reports to point towards significant loosening to have confidence to cut rates, especially as the central bank has been overly cautious to change its policy stance in recent years. Resultantly, we think markets will need to see a decline in the pace of employment, preferably even outright job losses on aggregate, alongside an uptick in the unemployment rate and weaker wage growth to reassess the probability of an April cut, which is priced at just 32% at present.

BANK OF CANADA PREVIEW

Holding out for the data

The Bank of Canada notably dropped its hiking bias back in January, while it also revised down its 2024 Q4 inflation forecast by 0.1pp to 2.4% and expressed fewer concerns around upside inflation risks. Furthermore, Bank staff went to considerable lengths within the accompanying Monetary Policy Report to decompose developments in the housing market and how they are impacting headline inflation. Given that some of the shelter inflation is a mechanical by-product of higher interest rates through the mortgage channel and the remainder is due to structural supply issues, an issue for fiscal as opposed to monetary authorities, the details of the MPR also leant in a dovish manner. Nevertheless, since the January meeting, the odds of an April rate cut have fallen by 30pp to just 32%, while 17bps of cuts have been priced out for this year in total. This is inconsistent with the evolution of the economic data, and rather reflects broader market forces.

More hawkish BoC expectations are a product of market forces, not necessarily stronger domestic data



"Granted, growth measures have outperformed the BoC's projections and the uptrend in the unemployment rate recently stalled, but the headline measures grossly overstate the strength of the Canadian economy."

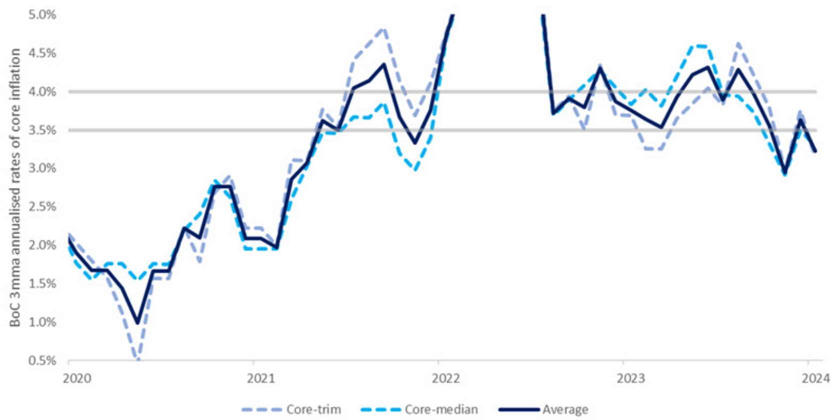
Growth has been propped up by improving export conditions, while the unemployment rate flatlined in January as the influx of available workers generally opted to remain on the sidelines of the labour market; a dynamic that could quickly reverse and induce a substantial amount of slack in the economy. Furthermore, measures of underlying domestic demand and employment conditions have remained weak, suggesting the economy still operates with excess supply. The broad-based improvement in inflation measures in January further evidence this. Consequently, despite the market's confidence of an April rate cut waning in recent weeks, we think the BoC remain on track to start easing in early Q2 as long as the macroeconomic data unfolds in a similar manner to the start of the year.

The fact that the Bank will also have another round of Business and Consumer surveys to hand and April's MPR includes an annual re-estimation of potential output, and thus the famed output gap that the Bank based policy on during the tightening cycle, reinforces our off-consensus view of earlier cuts. This is because the Q1 surveys are likely to show inflation expectations remain anchored, and both firms and consumers bracing for weaker growth in the coming quarters. Furthermore, due to the higher-than-anticipated rate of population growth and recent AI developments, we expect the Bank's estimate of potential growth will rise above 2% over the medium-term, meaning the economy will operate in excess supply for longer than previously anticipated.

"Despite our confidence in an April rate cut, we don't expect the Bank to signal as much next week."

Governing Council members will likely want to retain full optionality heading into April's meeting, owing to how noisy the macroeconomic data has been in recent months and how the inflation data is only just starting to show uniform signs of progress. As such, we expect the policy statement to show limited changes from January, and Governor Macklem to stay non-committal in his first non-MPR press conference, acknowledging the renewed progress in the inflation data but also cautioning that core inflation measures have quickly reversed similar improvements in the past.

Macklem could point towards short-lived inflation progress in Q4 to temper speculation over an April cut



EUROPEAN CENTRAL BANK PREVIEW

Keeping April on the table

After the last two weeks have been largely dominated by eurozone wage and price data, attention next week turns to the reaction of ECB policymakers to these latest outturns, with a policy announcement due on March 7th. While the ECB is almost certainly going to leave both its policy rates and forward guidance unchanged, we think the ECB won't necessarily close the door on an April cut either seeing as staff forecasts are likely to show a faster pace of disinflation relative to December.

"While we think the odds of an April cut should be higher than just 18%, we note that the recent ECB commentary and the latest inflation data isn't necessarily supportive of this."

Nevertheless, a softer tone from President Lagarde on Thursday, emphasising weak near-term growth conditions and the early progress in bringing down wage pressures, should keep April's meeting live. Then, the data will do most of the talking, with weaker growth and inflation prints required for the ECB to pull the trigger before the bookmarked wage data in May.

Recent data has pointed in different directions when it comes to ECB rate cuts

Admittedly, not all of the recent data outturns have definitively supported our projection for the ECB's easing cycle. This is most notably true regarding February's headline inflation data, where aggregate eurozone figures delivered a modest upside beat on expectations. Headline price growth fell 0.1pp less than anticipated, easing from 2.8% YoY in January to 2.6% last month. Meanwhile, core inflation exceeded expectations in a more meaningful manner. Whilst the reading dropped to 3.1% YoY, down from 3.3% the month prior, this was still above the 2.9% print that traders were looking for. In the context of PMIs for February that hinted at a possible pick-up in inflationary pressures on the back of an improving growth outlook, this could be a worry for policymakers. But looking at the individual country breakdowns though suggests to us that these concerns would be premature. Data from France, while continuing to show that the pace of disinflation was progressing favourably on a year-on-year basis, saw monthly readings that were slightly above expectations on a monthly basis. This, however, was likely due to the reintroduction of energy taxes. The corresponding figure for Germany, despite accelerating from January's readings, was below expectations by 0.1 percentage point. In both cases this tells a different story from the flash PMIs, which had seen inflation pressures rebuilding in Germany, but not in France. Furthermore, the latest inflation data shouldn't detract from the fact that inflation continues to track below ECB forecasts, which projected headline CPI at 2.9% for 1Q24, with core at 3.1%.

"Whilst the inflation data might be offering something of a muddy read through, wage data has been more conclusive. "

The Bundesbank's release of German negotiated wage data came in slightly below expectations, printing 3.6% growth for 4Q23, just before eurozone figures for the same period showed a marginal slowdown in wage growth from 4.7% in 3Q23 to 4.5% in 4Q23. While these were still too high for the ECB's 2% medium-term inflation target in isolation, we believe it is the start of a downward trend for negotiated wage growth set to play out in 2024. Significantly, this is a key piece of evidence that policymakers have been waiting for given the upside risks that could have been posed to the inflation outlook by elevated wage growth. Whilst there has been some insistence from ECB officials that confirmation would be needed from Q1 figures, published in May, we are less certain. Soft growth and easing inflation both point to the slide in wage growth being sustained, making the need to wait for the next round of figures unnecessary in our view.

ECB staff forecasts should receive a notable downgrade

That said, it will not just be recent data releases that ECB policymakers are looking at when they meet next week. Notably, ECB staff are due to deliver an updated set of economic projections and given that the likely cut-off date for the market assumptions was February 15th, they will not incorporate the latest set of hot inflation prints. As such, we expect large downgrades to the expected profiles for inflation and growth. In the case of the former, this will not only need to reflect data up to January undershooting the December projections, but also that falling wage growth means that the eurozone is now on a sustained disinflation path as well. The latter will need to reflect another three rounds of PMI releases that once again underwhelmed, a fact we think warrants a significant downgrade to growth projections covering the first half of this year. All told, this should pose a challenge to hawks on the Governing Council that would like to highlight sticky inflation pressures, with these broadly set to evaporate in this next round of staff forecasts.

All options should remain on the table next week

In terms of the meeting itself, we think there is a decent number of policymakers that might favour a rate cut in advance of Q1 wage data being available, at least based on recent commentary. Granted, several ECB hawks have hit the airwaves in the past week, including the National Bank of Slovakia's Kazimir and the Bank of Lithuania's Simkus, with both declaring a preference the ECB delivers its first rate cut in June. But this looks like the hawks are drawing up battle lines in advance of next week's meeting in an attempt to head off a potential dovish pivot to us. Admittedly, they have also been accompanied by the Bank of Greece's Stournas, normally seen as a dove. But this is looks like an outlier in our eyes when considering the remainder of the ECB's dovish contingent are unmoved. Several have noted a preference for gradual easing in recent weeks, linking this with an earlier start to rate cut. Most notably, comments by Centeno at the end of January explicitly ruled out the need to wait for wage data in May, all but confirming his preference for the Bank to ease rates earlier than June.

"Given this split in views, we fully expect the ECB to leave open the door to an April rate cut next week. In fact, we think prudent risk management should necessitate this."

If policymakers think that an April rate cut is at least a possibility, then it would be unwise to leave markets pricing this at just a one-in-four chance and expecting just three full rate cuts for the year as a whole.

"An April rate cut in this context would smell of panic, undermining ECB credibility, and sending shockwaves through markets as a result."

As such, we think the balance of views amongst the Governing Council warrants at least an implicit consideration of a rate cut in April somewhere in next week's communications. That said, with February's inflation overshoot fresh in the mind, this suggests that risks are for a relatively cautious tone from the Governing Council. As such, they will likely emphasise then Bank's data-dependent approach and a desire to see further slowdown in the wage data once again. This should mean that a summer rate cut remains the base case for markets, but without closing the door on a rate cut at the meeting in April that we continue to expect.

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