



# Julius Bär

1/3

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## CURRENCIES & MORE OUR INSIGHT INTO THE WORLD'S LARGEST MARKET

**Dollar: Yellen's defense of tight financial regulation made her unlikely to be re-appointed**  
**Euro: The mix of Draghi's relative optimism and no concerns on the rising Euro led €/ \$ higher**  
**Peso: Banxico's Minutes of the 10 August meeting showed some concern within the Board**

### Dollar: No rate hints from Janet Yellen

The catalyst for Dollar weakness following Fed Chair Janet Yellen's speech in Jackson Hole did not come from any comment on declining inflation in recent months but on defending tight financial regulation. Yellen said any roll-back of post-financial crises financial reforms should only be "modest" because they have made the banking system safer.

### Not a hawk, not a dove...



Source: B. Rich Hedgeye

With that, she rebutted Republicans in Congress and President Donald Trump who blames regulatory red tape for holding back the U.S. economy. Yellen's passionate defense on post-crisis tightening of financial regulation is probably not going to go down particularly well at the White House. Trump has made rolling back regulation one

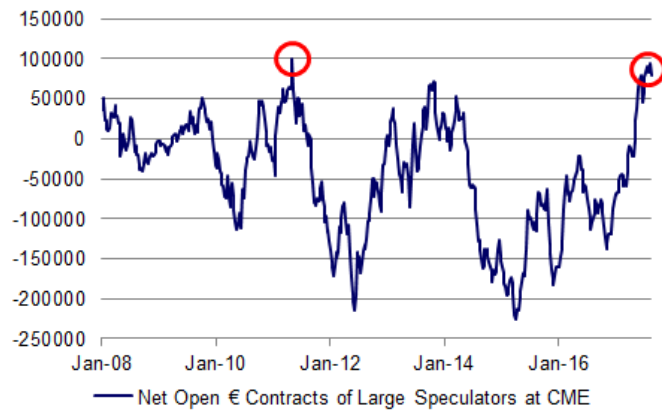
of the center-pieces of his presidency. Therefore, this could well have been her final speech as Fed Chair at the annual gathering of central bankers. That might just make Gary Cohn, the Head of the National Economic Council, the favorite to become the next Fed Chair. As one of his many U-turns, Trump has already made plain his preference for someone who will keep interest rates low and eases financial regulations. Cohn, the ex-Goldman Sachs COO would perfectly fit that profile. We would expect Cohn to weaken the bank stress test, the Volker rule (which limits proprietary trading by banks), and exempt smaller banks of the regulations. The market does not seem to have forgotten what has happened with loose financial rules: FX market sold the Dollar in the wake of Yellen's comments and the assumption that she will be replaced by Cohn.

**Conclusion:** The Dollar continues to make lower lows.

### Euro: What Draghi said and what he did not say

Expectations for decisive comments from ECB President Mario Draghi at the Jackson Hole Symposium were rather low. Some argued he might have been scarred by his recent experience at the ECB's conference in Sintra. Other referred to an ECB statement that Draghi will stick to the topic of the Symposium ("Fostering a Dynamic Global Economy") and delve into the ECB's future monetary policy. The result was a mix of the two assumptions. Draghi said he was confident that inflation would eventually reach the 2-percent target as output rises and the labor market tightens. "The global recovery is firming up," Draghi said, adding that "the consolidation of the recovery is at an early stage" versus that of the U.S. And then, there was the missing piece: He did not mention that the strength of the Euro has served as a break on demand in inflation in the Euro-zone.

**Euro positioning at the CME near record highs**



Source: Bloomberg Finance L.P., Julius Bär

**Conclusion:** The market has taken the combination of Draghi’s relative optimism and no comment on the Euro rally in the past couple of month as bullish for €/\$.

**QUICK NEWS HEADLINES (time in CEST)**

The following three headlines might have an impact on currency markets today:

- Sweden: Retail sales are expected to have risen 3.3% in July y/y (09:30).
- Euro-zone: Money supply M3 is expected to have increased by 4.9% in July y/y (10:00).
- U.S.: Wholesale inventories are expected to have risen 0.3% in July m/m (14:30).

**Peso: Patient and prudent**

While we have been and remain constructive on the Peso this year, we were expecting a correction in recent weeks as we got the impression that the market went ahead of itself (see our 10 and 23 editions). We were expecting a correction of \$/Peso to 18.50 but the overall trend exhibits small setbacks only (see chart below). Banxico’s Minutes of the 10 August meeting show that some concern in the weeks ahead is still warranted. The discussion of the Board concentrated on the uncertainty from the NAFTA negotiations. In terms of CPI, they recognized that some inflationary components have started to decelerate and even reversed their trend. Some members of the Board highlighted that if the recent shock from tomato prices were excluded, headline inflation (up to 6.4 percent in July from 6.3 percent in June) would have decelerated to 6.1 percent. The Board also pointed out that uncertainty on external and internal risks in the year ahead might affect the economy and the Peso. Oil production poses another risk to Mexico’s economy and public finances as oil production

continues to fall and it has failed to stabilize in the past few months. Lower than expected levels of production could put pressure on GDP growth, fiscal and current account balances, so Banxico could face a rather complicated outlook to start cutting rates in the coming quarters.

**\$/Peso in the past 12 months**



Source: Bloomberg Finance L.P., Julius Bär

**Conclusion:** We think the Peso rally since the beginning of the year went a bit too far and recommend waiting for better entry levels.

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