



# Julius Bär

1/3

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

**Euro: ECB President Mario Draghi did not provide details on the future path of QE, decision in October**  
**Krona: The Riksbank kept its Repo Rate unchanged but changed its inflation target to a variation band**  
**Dollar: Declining inflation seems to have eroded FOMC members' confidence, speeches this week show**

### **Euro: The focus now on October**

The Statement release yesterday following the ECB meeting was exactly the same as July's, with interest rates on hold as expected and asset purchases of € 60 billion a month set to go on until the end of this year. As we outlined in yesterday's preview, President Mario Draghi did not provide any details on the future path of QE but said instead that "the bulk of decisions will be taken in October".

### **Mario Draghi answering questions from reporters**



Source: [www.ecb.europa.eu](http://www.ecb.europa.eu)

As assumed, the most interesting part came in the press conference when Draghi was asked about the strength of the Euro. "The recent volatility in the exchange rate represents a source of uncertainty which requires monitoring for the impact on price stability", Draghi answered. Revealing was the price action on this comment as the Euro did not decline on this, but increased to a high of 1.2060 against the Dollar. Apparently, the signal that a decision

on bond purchases is likely next month made it difficult to talk down the Euro. In our view, the market told Draghi that talk is cheap and that it is putting more weight on the upcoming QE actions. In terms of forecast changes, the ECB revised down inflation to 1½ percent for this year from 1.6 percent and at the same time increase GDP growth to 2.2 percent from 1.9 percent previously.

**Conclusion:** Draghi's comments in general, the upward revision of GDP growth and the small reduction of the inflation forecast will likely keep the Euro supported.

### **Krona: Policy unchanged, forecasts revised higher**

The Riksbank left its monetary policy unchanged but adopted an inflation-target band instead of the fixed 2-percent target, as most market participants expected (see our preview yesterday). In the press release, the Riksbank has dropped the wording "now especially important that inflation stabilizes more lastingly close to the target", which could be interpreted as slightly hawkish. Furthermore, there were some revisions to the macro-economic outlook. The inflation forecast was somewhat upward revised, with CPIF to average 2.0 percent this year and 1.9 percent in 2018 (previous 1.8 and 1.7 percent, respectively). GDP growth was also revised up for both 2017 and 2018. However, the Riksbank – again – fell short of making any revisions to its Repo Rate path. We have been arguing for several months that the Riksbank has many reasons to turn away from its loose policy. Resource utilization is high and rising, inflation is running above the target and is expected to stay close to 2 percent in the months ahead. We do not give up on our assessment and expect the change in rhetoric to come at the 26 October meeting where the Riskbank might announce that its QE program will not extend beyond year-end.

**The Krona slightly weaker against the Euro yesterday**



Source: Bloomberg Finance L.P., Julius Bär

**Conclusion:** While the Riksbank seems to try everything from preventing the Krona to appreciate too quickly, we think the downside is very limited. This makes the Krona ideal for investments in Reverse Convertibles.

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

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

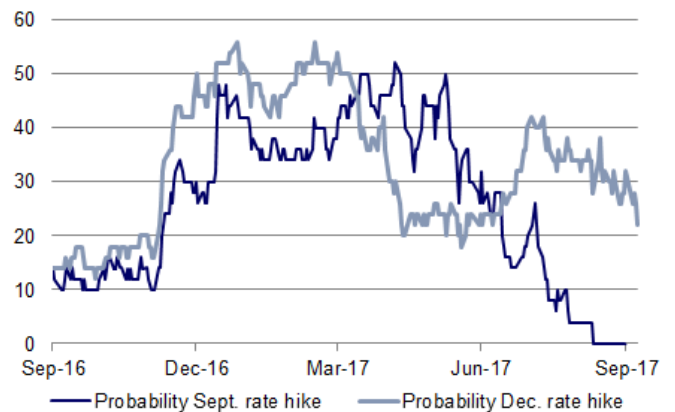
- Japan: The current account surplus for July came at ¥ x.x trillion vs. ¥ 2.0 trillion expected.
- Hungary: CPI is expected to have risen 2½% in August y/y (09:00).
- U.K.: Industrial production is expected to have risen 0.4% in July y/y, the trade deficit for July is expected at £ 12.0 billion (10:30).
- Canada: The unemployment rate is expected to have remained at 6.3% in August (14:30).

**Dollar: On Fed talk this week**

As the black-out period begins on the second Saturday ahead of the next FOMC meeting, traders and investors are trying to get their final clues before the next gathering on 20 September. Early this morning, N.Y. Fed President Bill Dudley concluded a week filled with speeches of FOMC voting members. Speaking in Asia, Dudley said he is “surprised by the persistent inflation shortfall” and that “weak inflation may be partly due to structural shifts”. Looking ahead, Dudley reckoned that the Fed’s rate-hike path should continue to be shallow. Lael Brainard said on Tuesday at the Economic Club of New York that “we should be cautious about tightening policy further until we are confident inflation is on track to achieve our target”. Then, Minneapolis Fed President Neel Kashkari – admittedly an uber-dove – said rate hikes may be “doing real

harm”. On Wednesday, Dallas Fed President Robert Kaplan – a centrist – reiterated his view that the Fed should be patient on rates. Declining inflation since the beginning of the year seems to have eroded the Fed’s confidence. Derived from Fed Funds futures, the probability of a hike in September has declined to zero and December reached only 22 percent (see chart below).

**Probabilities of Fed interest-rate hikes**



Source: Bloomberg Finance L.P., Julius Bär

**Conclusion:** Rates expectations are currently not supportive for the Dollar.

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