Julius Bär

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

Franc: The Franc has weakened in the past 3 months but the SNB will certainly remain on hold today
Pound: The BoE will most likely put more weight on sluggish growth than on CPI at today's meeting
Dollar: After many months of declining inflation, today's CPI print will likely show that it is stabilizing

Franc: On hold for the twelfth time

There is a series of central bank meetings today with the SNB opening it at 09:30, followed by the BoE and Türkiye Cumhuriyet Merkez Bankası, both at 13:00. Bank Rossii will follow tomorrow. Normally, such an accumulation would suggest exciting times, but the first three of the four are expected to stay on hold while the latter will almost certainly cut its policy rate tomorrow.

The opinion of many Swiss citizens

Source: B. Rich / Hedgeye

It has become consensus that the SNB is holding rates unchanged until the ECB ends QE in order to prevent the Franc from starting to rise again. Total Sight Deposits at the SNB are unchanged at SFr 578 billion for 12 consecutive weeks, indicating that the central bank did not have to be active in FX markets since June. Fascinatingly, the Franc even weakened from 1.08 to 1.15 against the Euro during this period while prior to June, the Franc had risen despite FX interventions. With the weaker – or less strong – Franc, more and more pension fund managers and citizens have raised their voices that the SNB should soon give up their NIRP. With yields still negative until the 10-year maturity, pension funds have struggled for quite some time to generate a reasonable yield. Given this difficulty, Swiss voters will go to the polls on 24 September to decide on a reform of retirement provisions. The government proposes a reduction of the minimal conversion rate of currently 6.8 percent to 6.0 percent, meaning a reduction of the future retirement pay from SFr 6'800 per SFr 100'000 paid in capital to SFr 6'000. Currently, a slight majority is opposing this proposition. Negative interest rates are indeed a pain in the neck for asset managers and Swiss savers but the SNB has no other choice than to wait for the ECB to move first.

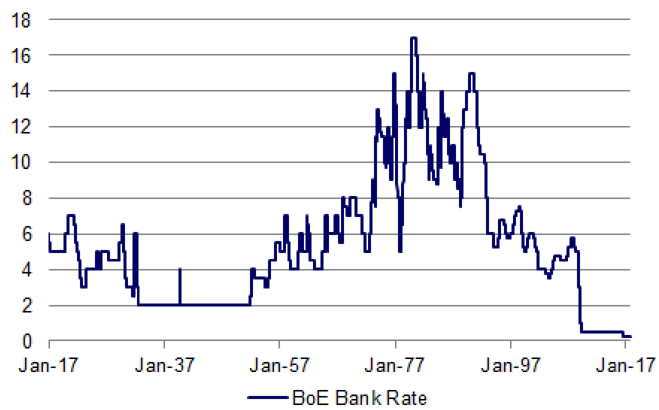
Conclusion: SNB President Thomas Jordan will repeat his usual mantra today.

Pound: Also on hold

The BoE is trapped between rising inflation and deteriorating fundamentals. Given ongoing comments from MPC members, we think it is clear that the emphasis is on the latter and the BoE will look through rising inflation. Yesterday's labor report showed that wage growth remained lackluster despite the unemployment rate falling further to 4.3 percent in July, the lowest since June 1975. Rising inflation with lower wage growth is ultimately deflationary as it squeezes real incomes. Therefore, we think that the risk of a sharper downturn in consumer spending will be the overwhelming concern to the majority of the MPC members. However, inflationary pressures from Sterling weakness in the past couple of months will likely prompt a few MPC members to consider tighter monetary policy. With the arrival of Dave Ramsden as Deputy Governor, we are looking for a 7–2 vote split (the last meeting was 6–2).

Michael Saunders and Ian McCafferty will maintain their vote to hike rates. Ramsden, the former Chief Economic Advisor to the HM Treasury, is unlikely to join them. While he has not made any public statements about his views on monetary policy, he is generally expected to take a fairly middle-ground position. We think the BoE will hold off from raising rates until around the middle of next year.

The BoE's Bank Rate in the past 100 years.



Source: Bloomberg Finance L.P., Julius Bär

Conclusion: We think we have not yet reached the buy-on-dips environment and still recommend staying short the Pound.

QUICK NEWS HEADLINES (time in CEST)

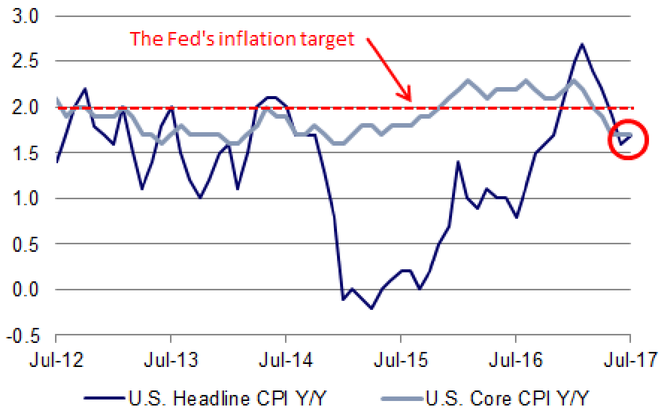
The following three headlines might have an impact on currency markets today:

- Australia: The unemployment rate remained at 5.6% in August, as expected.
- China: Retail sales increased 10.1% in August y/y vs. 10½% expected, industrial production rose 6.0% in the same period vs. 6.8% expected.
- Turkey: The TCMB is expected to leave the 3 benchmark rates unchanged (13:00).

Dollar: Inflation stabilization?

With FOMC members in the black-out period until the 20 September meeting, today's August CPI print will be the only meaningful information. If consensus expectations are right, headline CPI will move 0.1 higher to 1.8 percent and core CPI 0.1 percent lower to 1.6 percent from July's 1.7 percent. While this would not yet be a reversal of the ongoing inflation price pattern, it would at least point towards stabilization ahead of the FOMC meeting and might influence the new staff projections. On 20 September, the Fed will provide their latest Summary of Economic Projections, and another "weakish" print today would likely suggest that the updated projections will show a lower profile for core inflation next year. The decline in core inflation this year has been mostly based on one-off factors such as the collapse in wireless phone service prices, depressed used motor vehicle prices and declining hotel room rates. In August, we did not notice any such relevant price changes, therefore CPI is likely to have stabilized.

Headline and core CPI stabilized after the decline



Source: Bloomberg Finance L.P., Julius Bär

Conclusion: CPI is likely to have stabilized in August, but not more.

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CONTACTS

FX Market Advisory Zurich
+41 (0) 58 888 8484

FX Market Advisory Geneva
+41 (0) 58 885 3551

FX Market PB Solutions Zurich
+41 (0) 58 888 8484

FX Market Advisory Hong Kong
+852 2979 2688

FX Market Advisory Singapore
+65 682 71 790

Author: Jürg Mettler
+41 (0) 58 888 8454

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