



Julius Bär

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

Dollar: Fed speakers yesterday clearly indicate that the FOMC will continue with gradual rate hikes
Pound: Comments from Davis, Barnier, and Tusk are showing how far apart the E.U. and U.K. remain
Koruna: Despite strong economic growth, the Česká Národní Banka will not increase its Repo Rate yet

Dollar: A plethora of Fed speak

Finally, after two weeks of silence from Fed officials due to the black-out period ahead of the FOMC meeting last week, yesterday we had a plethora of Fed speak. Within three hours, Cleveland Fed President Loretta Mester, Governor Lael Brainard, Atlanta Fed President Raphael Bostic and Chair Janet Yellen all spoke at various places.

Raphael Bostic, the new Atlanta Fed President



Source: Rich Pedroncelli / AP

As usual, the main focus was on Yellen's speech, especially as she was talking about "Inflation, Uncertainty, and Monetary Policy". However, we think Bostic's speech was equally relevant as it was his first appearance as a relatively unknown new member. Bostic, who succeeded Dennis Lockhart last April discussed the U.S. economic outlook and monetary policy at the Atlanta Press Club. His main message was that he is pretty comfortable with a Decem-

ber rate hike. "We are expecting a stable, gradual path to 2 percent inflation", he pointed out. Yellen delivered a keynote speech at the National Association for Business Economics in Cleveland. She also indicated a gradual path in terms of rate hike: "Moving too quickly risks overadjusting policy to head off projected developments that may not come to pass. A gradual approach is particularly appropriate in light of subdued inflation and a low neutral interest rate. It "would be imprudent to keep monetary policy on hold until inflation is back to 2 percent" she concluded. Mester was moderating the panel at the NABE conference and did not comment on the Fed monetary policy. Finally, Brainard at the Fed conference on "Disparities in the Labor Market" delved into one of her favorite topics – inequality – and said research shows it may damp spending.

Conclusion: The message of Fed speakers yesterday was that despite weak inflation, the FOMC will continue with gradual rate hikes.

Pound: Illusions

First news flow out of the fourth round of Brexit negotiations shattered the illusion that the U.K. was ready to play by the E.U.'s rules on the divorce bill. Brexit Secretary David Davis made it clear Britain will only pay up if it gets the final deal it wants. "It is obvious that reaching a conclusion on this issue can only be done in the context of a new deep and special partnership with the E.U.", Davis said. His E.U. counterpart Michel Barnier stuck to his position that the bill needs to be sorted out first. European Council President Donald Tusk, who met yesterday with Prime Minister Theresa May after holding talks with Barnier said that there is "not sufficient progress" for negotiations to continue, adding that "we will discuss our

future relations with the U.K. once there is sufficient progress". The comments highlight just how far apart the two sides remain, as they continue to battle over the sequencing of talks.

Cable in the past 12 months



Source: Bloomberg Finance L.P., Julius Bär

Conclusion: We believe the rate-hike component driving the recent Pound rally is fading and Sterling will turn lower due to Brexit-related reality.

QUICK NEWS HEADLINES (time in CEST)

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

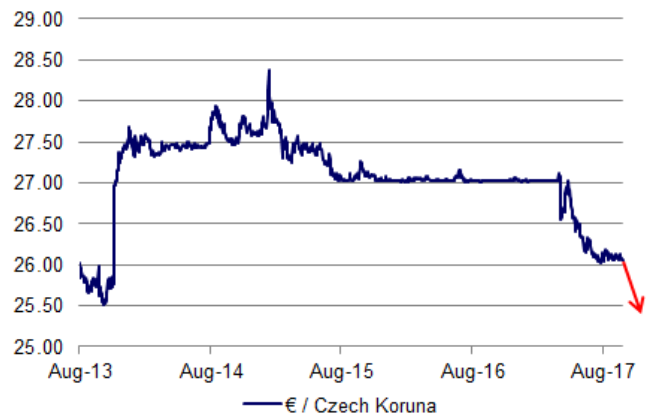
- Hungary: The unemployment rate for August is expected at 4.1% (09:00).
- Euro-zone: Money supply M3 is expected to have increased by 4.6% in August (10:00).
- U.S.: Durable goods orders are expected to have risen 1.0% in August (14:30).

Koruna: Patient or forward-looking?

The Česká Národní Banka is expected to leave its Repo Rate on hold at ¼ percent today. On 3 March, the CNB acknowledged that the strongly increasing fundamentals did not justify keeping the Repo Rate at a record low of 0.05 percent and lifted it for the first time from that level, which was in place since November 2012. CPI has stabilized around the 2½-percent level since the beginning of this year and another hike to ½ percent would be more than appropriate. However, only 2 out of the 20 economists surveyed by Bloomberg forecast a rate hike (Morgan Stanley and HSBC) as Governor Jiří Rusnok cautioned against too swift rate increases at the last meeting. Considering that the Czech economy is growing fast (4.7 percent in Q2 from a year earlier) and the labor market is

tight (the unemployment rate stands at 4.0 percent as of August), this rather dovish approach seems to be mainly targeted to keep the Koruna from rising too fast. After the CNB gave up the 27-floor last April, €/Koruna has been trading sideways around the 26-level since July but we are convinced that it is only a matter of time until it will advance further.

When will the Koruna appreciate again vs. Euro?



Source: Bloomberg Finance L.P., Julius Bär

Conclusion: Long Koruna vs. Euro is a low-risk trade with some – but admittedly – not huge upside potential (probably around 4 percent). Patience is needed.

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