Daily FX Strategy: Strong dollar policy, the long goodbye

US Treasury Secretary Steven Mnuchin said there's no change to Washington's dollar policy ‘as of now’ and declined to talk about possible intervention to weaken the currency. It will be US policy settings, not jawboning, which make the difference

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USD: Markets are fixated on policy makers, not the data

Comments by Treasury Secretary Steven Mnuchin that there was no change to Washington's dollar policy ‘as of now’ briefly hit the dollar yesterday. In reality, however, it will have to be US policy settings which make the difference. There’s no point trying to talk the dollar lower with loose fiscal and tight monetary policy. That is why it seems the White House is pressuring the Federal Reserve into reversing last year’s 100 basis points of rate hikes. Comments from Fed members John Williams and Richard Clarida have also re-ignited expectations that the Fed starts off with a 50bp rate cut on 31 July – though our team still prefers 25bp. Importantly it is clear that the market has sunk its teeth into the disinflation, secular stagnation story and is only interested in the response from policy makers, rather than current data releases. For the dollar, we’re impressed by the performance of Gold and believe investors will ultimately buy into the Fed's reflationary efforts – which include a weaker dollar. Dollar weakness is also being supported by flows into emerging market local bond markets, where disinflationary trends led to rate cuts in Korea, Indonesia, South Africa & Ukraine yesterday and very likely in Russia and Turkey next week. We doubt US consumer sentiment moves the needle on Fed expectations today, while Fed dove James Bullard may actually pour a little cold water on the chances of a 50bp cut when he speaks art 1710CET. DXY to edge to 96.35.

EUR: New inflation strategy?

News that the ECB may be considering a more symmetrical inflation target briefly hit the EUR yesterday – although there's enough ECB dovishness around already. EUR/USD looks trapped in a 1.1200-1.1300 range for the time being.

GBP: No deal slightly less likely

A vote in parliament yesterday making it harder for any government to prorogue parliament has reduced the chances of a Johnson cabinet heading into October on a 'No Deal' ticket. We had identified 3% of risk premium in GBP on Wednesday, but have little confidence in calling EUR/GBP back to 0.8800.

CHF: EUR/CHF to break lower as ECB QE expectations build

We published an article yesterday warning of a move in EUR/CHF to 1.05 this summer as expectations build of ECB quantitative easing. Effectively our call is that the Swiss National Bank will face the same kind of pressure (ECB money printing) that prompted them to abandon the 1.20 EUR/CHF floor in January 2015. This all comes at a time when eurozone peripheral debt spreads have already tightened significantly and in the case of Italy may have tightened too much. Our team are watching out for signals that Italy's Deputy Prime Minister Matteo Salvini may pull his Liga party out of the government, prompting early elections. Given our view of the dollar topping out this summer, we also see a chance of USD/CHF breaking below 0.97 amidst higher volatility.

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