

ECB positives may equate to a high-flying euro

For ECB President Mario Draghi, today is all about managing expectations. Here's what we think he'll say and how markets are likely to react



Source: Andrej Klizan

EUR: Series of small ECB positives may equate to a punchy move higher

- The ECB meeting today will take place at a time when global markets are at a pivotal juncture, which could make for a fairly interesting (or entertaining) press conference with President Mario Draghi. From the ECB chief's perspective, it'll all be about managing expectations and sending nuanced signals. For markets, we'll be looking to infer what role the global external environment (ie stock market volatility and US protectionism) is playing in the ECB's policy reaction function.
- We expect the following combination of developments from the ECB meeting today to be broadly supportive for the EUR: (1) a subtle change in the ECB's forward guidance to keep markets on their toes over the potential end to QE asset purchases this year; (2) no attempts by President Draghi to actively talk down the euro; and (3) an upward revision to

the ECB's growth profile (2018 GDP nudged up to 2.4%), while no change to the CPI profile (2018 at 1.4%).

- While we don't expect any explicit QE end date to be announced today, the ECB dropping its willingness to "increase QE in size and/or duration" would be an implicit step forward towards the end of asset purchases – and might just be enough to appease the dissenting hawks within the Governing Council.
- On the currency front, expect "volatility" in the euro to be cited as a "source of uncertainty" – although this is merely a matter of fact within the context of central bank policymaking. Only direct concerns over the level of the FX – for which we think there are little grounds for justification (pointing to the flat-ish trade-weighted EUR since Feb) – would actually spook EUR investors.
- Looking ahead, markets remain relatively underprepared for the next stages of ECB policy normalisation. The short-term 3-year forward EZ OIS rate is still around 50bps below its level when the ECB began easing in summer 2014. A re-pricing here this summer will set EUR/USD on a path towards 1.30 in 2018.

With the US dollar trading soft, these small positives could amount to a fairly punchy move higher in EUR/USD today – [with a potential test of 1.25 on the cards](#) (key resistance levels to monitor are first 1.2435/45 – and then 1.2505/15).

SEK: Spectre of US protectionism warrants a near-term bearish krona outlook

We have been somewhat [prompted to turn bearish on the Swedish krona](#) – with the spectre of US protectionism and a 'trade war risk premium' weighing on the FX of small-open economies like Sweden. In addition, SEK has all but lost its relative current account surplus advantage versus the EUR – making the currency increasingly vulnerable to global risk factors. Finally, recent SEK weakness is unlikely to see a significant inflation overshoot, thus is unlikely to warrant any Riksbank response. These factors mean we now expect EUR/SEK to hit 10.30 in the coming months.

USD: Uncertainty over Trump tariff objectives lends itself to choppy trading

Various US media reports overnight state that President Trump may or may not sign a Presidential Proclamation on steel and aluminium import tariffs today, while Canada and Mexico may or may not be exempt from any measures. Such ever-changing US trade policy lends itself to a choppy trading environment – with the USD broadly on the back foot given the general White House chaos ([see our note from yesterday](#), Trade Wars – Episode II: Attack of the Cohns). The Canadian dollar saw a partial relief rally on news of tariff exemptions; CAD/MXN downside looks overdone in 2018 (-7.5%) especially given the local economic and political risks.

Author

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com