FX Daily: FOMC will not rock the boat for risk assets

With markets functioning well and long-term yields very low, the Federal Reserve is unlikely to take any concrete action later today. But uncertainty over Covid-19 and the next US fiscal stimulus package suggest the central bank will retain its cautious language. Here's what that means for FX

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USD: FOMC will not rock the boat for risk assets

We expect the Fed to keep its cautious bias in place today given the ongoing Covid-19 uncertainties and negotiations on a new US fiscal stimulus package. These factors suggest there is little reason for the Fed to sound more upbeat, while the orderly functioning of markets and suppressed long-dated yields also suggest there is little reason to turn even more dovish at today's meeting. As per our FOMC Preview, our economists expect the committee to keep the Fed funds target rate unchanged at 0-0.25%, leave its QE stance in place and maintain its ongoing forward guidance that the central bank is committed to keeping rates close to zero until it is confident that the US economy weathers the Covid-19 crisis. Such a cautious message should not rock the boat for risk assets, keeping the broad-based soft USD bias in place and helping to facilitate a further fall in the trade-weighted dollar in the remainder of the year, with US presidential election risk premia still to be priced into the dollar.

EUR: Stretched EUR/USD to stay around the 1.1700 level

The expected cautious message from the FOMC should keep EUR/USD hovering around the 1.1700 level today and very likely for the rest of the week as such an outcome is largely expected by markets while plenty of euro-specific good news already seems to be priced into the currency. Indeed, based on our short-term financial fair value model, EUR/USD screens as expensive following its rally over the past week. The stretched short-term valuation in turn points to stability in / lack of meaningful upside to EUR/USD in the near term.

GBP: Limited upside potential

EUR/GBP is back below the 0.9100 level but we see the cross's downside potential as limited as the UK-EU trade negotiation uncertainty continues to weigh on GBP. With EUR/USD upside likely to stall for now, so should the GBP/USD upside, with the latter remaining below the psychological 1.3000 level.

SEK: Domestic data to continue playing second fiddle

In Sweden, the focus today is on the July Economic Tendency Survey. In normal times, this is an important indicator for the local economy and a factor for the Swedish krona's direction, but in current times of Covid-19 uncertainty, its effect on SEK should be fairly limited with the direction of global sentiment being the key for the krona price action. The cautious FOMC suggests limited upside potential to EUR/SEK, with the pair not moving meaningfully above the 10.30 level.

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