FX Daily: The sterling week ahead

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USD: Staying supported during the first part of the week

The FOMC meeting (Wednesday) is unlikely to deliver a major surprise, with the Federal Reserve likely remaining on hold and Chair Jerome Powell re-emphasising the data-dependent approach of the committee. Instead, markets may be more focused on the fast approaching 15 December deadline for US tariffs on Chinese exports. Uncertainty about this is likely to keep risk assets muted and the trade-weighted US dollar supported at the start of the week. Either a partial deal or an extension of the deadline on tariffs would help risk currencies into the year end, particularly if general risk sentiment is helped by a market friendly outcome to the UK election on Thursday. But for today, the dollar should stay supported.

EUR: No fireworks from Lagarde

Rangebound EUR/USD trading is set to continue for another week. On the eurozone side, the European Central Bank meeting on Thursday (the first meeting for new ECB President Christine Lagarde) shouldn't bring too many fireworks. We don't expect any clarity on Lagarde's view of the ECB strategic review. The new ECB staff projections will be published and we expect both CPI and growth projections for 2020 to be lowered, supporting the case for the easing package announced in September. A possible market-friendly outcome to the UK general election on Thursday may have a positive effect on EUR/USD but we don't expect the cross the break above the 200-day moving average level of 1.1160.

GBP: Bracing for a big move

The main event of the week for sterling is the general election on Thursday. The market is currently partly pricing in a Conservative victory (the final election debate last Friday and recent polls continue to point to such an outcome), with our short-term final fair value model suggesting a more than 2% Brexit resolution premium currently priced into GBP. Should the Conservative party gain a majority, we expect GBP/USD to move into the 1.34-35 area and EUR/GBP to drop to 0.82/0.83 levels. Conversely, a hung parliament would lead to a full pricing out of the GBP Brexit resolution premium, a rebuilding of sterling speculative shorts and GBP/USD likely dropping to 1.28 (and EUR/GBP rising above 0.8600 this week).

JPY: A week of asymmetric risks

US-China trade negotiations and UK elections will be the key USD/JPY drivers via the risk sentiment channel this week. We see the spillover into the yen as asymmetric, with the yen benefiting more from a non-market-friendly outcome (currently not expected by markets, as evident on the latest GBP price action) vs the expected Conservative party victory.