21 February 2018
Article

FX: Short-term noise, long run hope for sterling

UK jobs data and testimony from Bank of England Governor Mark Carney will steer the pound on Wednesday, while FOMC minutes and Eurozone PMIs are also in view

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USD: Structurally weak $ may find little further joy from priced-in Fed story

The FOMC minutes today may curb some of the hype over faster than expected Fed rate hikes, given the obvious divisions within the committee over the outlook for the US economy. With the two-year Treasury yield trading above 2.25%, one could easily argue that markets are all but pricing in the end of the Fed tightening cycle – assuming a 2.50-2.75% terminal rate and accounting for a small negative term premium at the short-end of the curve (-30bps). Difficult to see a structurally weak dollar finding any joy from an already priced in Fed story.

EUR: Signs of a booming Eurozone economy in today's PMIs not exactly a negative

The preliminary Feb Eurozone PMI releases will be of particular relevance for the data-sensitive Euro – our economists are looking for a partial easing in both the manufacturing (59.1) and services (57.6) readings after having hit cyclical highs in recent months. Still, at these elevated levels, any confirmation of booming Eurozone economic activity shouldn't exactly be a negative driver for the currency. Right now, we see EUR/USD corrective moves towards 1.2250-1.2300 as temporary.

GBP: Solid UK data & two types of Brexit agreement may unlock further upside

We wouldn't be surprised if investors were genuinely confused over the short-term direction of travel for the pound given the myriad of different narratives and factors driving the currency right now. Today's eventful UK calendar is only set to ramp up the short-term noise levels. The latest jobs report (0930 GMT) will be closely watched following the BoE's data and Brexit-contingent hawkish signal; solid jobs growth (ING: 185k) and nascent signs of pipeline cost pressures – with headline wage growth staying firm at 2.5% YoY – will be the minimum required to keep markets 50:50 over a May BoE rate hike. A positive surprise in the wage data would see odds of a near-term rate hike trickle higher – although we note that despite the increased sensitivity of short-term UK rates to data surprises, to some degree there still remains a 'Brexit factor' in markets that may inhibit a normal reaction to any positive data (which is not surprising given that long-run Brexit dynamics still trump short-run data in terms of implications for UK asset prices).

This is where the BoE may feel the need to interject and thus we would expect Governor Mark Carney and his colleagues to reiterate their hawkish stance when they testify to Parliament later today (1415 GMT) – which should, ceteris paribus, keep the implied market odds for a May BoE rate hike just where they are (55-60%). Yet yesterday's positive market reaction to news that the EU is willing to take a more 'flexible' approach to trade talks shows the potential for deferred GBP upside in the event of a constructive outcome at the 22-23 March EU leaders summit. There are now two types of Brexit agreement that hold the key to further GBP gains: a transition agreement and an association agreement (which is the EU offering the UK a 'privileged' post-Brexit relationship). In theory, this is good news – but GBP will need to see pen to paper on these 'agreements' before moving significantly higher. Our GBP/$ target for 1Q18 still 1.45 for now.

AUD: 4Q wage data positively surprises, but still weak by historical standards

4Q Australian wage growth data printed slightly above expectations (at 2.1% YoY) – yet as the Feb RBA minutes noted, this still remains muted by historical standards (pre-GFC average was 3.5-4.0%). So long as domestic cost pressures remain absent, near-term RBA rate hike sentiment will also stay non-existent.

Chris Turner
Global Head of Strategy and Head of EMEA and LATAM Research
+44 20 7767 1610
chris.turner@ing.com

Petr Krpata, CFA
Chief EMEA FX and IR Strategist
+44 20 7767 6561
petr.krpata@ing.com

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