

## British Pound: Clinging on to a hawkish Bank of England

Will it be a dovish hold or a 25bp rate hike? Anything is possible at today's Bank of England meeting



Source: Bank of England

### GBP: What the BoE says today could set the tone for sterling over summer

What makes today's Bank of England meeting particularly intriguing is that all potential scenarios – from a dovish hold to a 25bp rate hike – are conceivable outcomes. Indeed, this is largely down to what can only be described as sheer confusion over the Bank's post-Brexit policy reaction function. The sharp swing in policy expectations in response to one set of monthly data releases and off-the-cuff comments by Governor Mark Carney – as well as the wild gyrations in GBP markets in recent weeks – should serve as a warning shot to the MPC over the growing policy uncertainty in markets.

A 25bp rate hike today is not a forgone conclusion – and largely depends on which type of MPC shows up today; a risk-averse approach would be to wait-and-see whether the softer 1Q UK GDP data is in fact transitory, though officials could equally opt to 'look through' this and press ahead with a 25bp hike if they remain convinced that their outlook for the jobs market and a fall in

inflation will lead to a boost in real household incomes. The risk-averse approach, however, has been the norm in post-crisis monetary policymaking. If this is the case – and we do see the BoE on hold – GBP's initial reaction will be a function of: (i) the MPC vote split and (ii) the language around the soft 1Q activity data. The combo of a third rate hike dissenter and the post-meeting statement referring to a 'transitory' soft patch would lift GBP/USD up to 1.3700 – as odds of an August BoE rate hike rise (currently 50:50). All our GBP scenarios can be found in our preview note [GBP & BoE: Carney's Chameleon Act](#).

## USD: Tentative signs that the emerging markets vicious circle may be coming to an end

There are early signs that the vicious circle of higher US rates and a strong US dollar, negative emerging market sentiment, sell-off in EM assets and weakness in EM FX (which then loops to fuel a stronger USD) may well be coming to an end. But there are a few lingering negative idiosyncratic stories that may continue to weigh on investor sentiment towards EM assets overall in the coming weeks (the [surprise election outcome in Malaysia](#) joins Turkey and Argentina on the monitoring list). US CPI data today could see a further shake-out in risky assets – especially if we see a print stronger than 2.5% year-on-year consensus, which would likely see the US 10-year yield firmly breach the psychological 3% handle. The US dollar index to consolidate around 93.

## EUR: Watching narrative around eurozone CPI in the ECB's economic bulletin today

The ECB is due to release its monthly Economic Bulletin today (1000 CET) – and of particular interest is the central bank's latest update on the eurozone's inflation prospects following the lower-than-expected April core CPI print (that dipped to 0.7% YoY). ECB watchers will be focusing their attention on commentary around the 'super core' inflation estimate – which strips out items in the CPI basket that are most sensitive to changes in the output gap. Chief Economist Peter Praet hinted that soft CPI outturns are transitory – but investors will need to see evidence in data before buying into a higher EUR/USD story. For now, look for stability above 1.18.

## HUF & CZK: NBH remains king, while Czech CPI won't alter CNB's hawkish bias

As Petr and Peter note in '[NBH is still the king: Fade the move & receive rates](#)' – we see the latest rise in Bubor as driven by technical issues and don't expect it to last. We also get Czech CPI data today; Jakub Seidler is looking for a 1.8% YoY print (also consensus), but doesn't think a small miss – in particular one caused by volatile food prices – will be a game-changer for our hawkish central bank outlook.