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Article

Shifting Brexit odds help pound

The probability of a more market-friendly Brexit outcome is rising-supporting the pound

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GBP: Rising perceived market probability of Article 50 extension

While the failure of the no-confidence vote was largely expected, sterling continues to reap tentative benefits from modestly shifting probabilities of the Brexit outcomes. On the latter, with Prime Minister Theresa May's willingness to move closely towards a cross-party deal (although whether this will be achieved is still uncertain) as well as growing opposition towards a hard Brexit, the odds of a more market-friendly outcome are rising. Indeed, compared to the start of the week, our probability-weighted outcome for sterling has improved (although only modestly), with the EUR/GBP probability-weighted fair value declining from 0.90 prior to the meaningful vote (see [GBP: Brexit and the bumpy ride to its eventual recovery](#)) to 0.89 currently. The latter is clearly not far from the current spot level. As we have argued previously, our base case is for an extension of Article 50 and the rising perceived market probability of such an outcome should, in turn, keep GBP away from this year's lows.



USD: No declining trend in sight

Asian equities and FX came under modest pressure overnight following the news that US prosecutors have started investigating Huawei. Still, the negative spillover into risk assets has been rather modest, and a more meaningful escalation in the US-China trade rhetoric would be needed to weigh on sentiment more aggressively. A cautious Federal Reserve is providing a partial offset to such negative news at this point. The trade-weighted dollar to go modestly higher today.



EUR: Fading reasons to be upbeat on EUR on good domestic factors

In the eurozone, the final reading of December inflation should confirm fading price pressures (with headline CPI back well below the 2% target due the fall in oil prices). Coupled with the recent weak activity data, this suggests the odds of even one 20 basis point deposit hike by the European Central Bank in 4Q19 are falling. As per our [2019 FX Outlook](#), for EUR/USD to embark on a more sustainable uptrend, we have to see structural US dollar weakness as domestic catalysts for euro strength simply aren't in place.

HUF: Bracing for a good year

The National bank of Hungary Vice Governor Marton Nagy signalled yesterday an upcoming Bubor normalisation, dependent on the core CPI dynamics (which we expect to support the rise in the inter-bank rate). In our view, this a significant positive for the Hungarian forint and has materially

improved HUF's medium-term outlook as it tackles one of the key negatives that investors have been concerned about – the NBH being behind the curve. With the NBH now taking back control, these concerns should ease and lead to a meaningful reversal of the still significant speculative positioning. Needless to say, HUF benefits from the solid current account surplus while the currency is cheap on a medium-term basis. We expect EUR/HUF to move to 310 this year and see the forint as the central and eastern Europe outperformer of the year.

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