Sterling: It's getting hot in here, but no need to take your positions off

BOE Governor Mark Carney sparks a sterling sell-off but our message remains the same: keep calm and carry on

Source: Bank of England

GBP: It's getting hot in here, but no need to take your positions off just yet

It appears as though GBP bulls have hit the panic button after Governor Mark Carney made the cautious and vague statement that interest rates are likely to rise "this year" – while

- a) Steering clear of talking about specific timings (i.e. May)
- b) Noting that there are also other meetings this year
- c) Pointing out that there are likely to be a range of views within the MPC

We note, however, that this was probably the most hawkish signal the BoE governor could have given three weeks away from a policy meeting and we make two observations about the current policy-setting backdrop that naturally lends itself to a more cautious approach:

1. Current geopolitical tensions and fragile global markets mean that any central banker (not just the BoE chief) will be particularly wary of making any unnecessary policy pre-commitments
2. Ongoing small, yet non-negligible, Brexit uncertainties mean that the long-run policy

> outlook will need to be reassessed on a rolling basis and more senior policymakers will be wary of over-promising and under-delivering on interest rate rises. As Governor Carney also said, the MPC will "sit down calmly and look at it all round" in May.

'Keep calm and carry on' is still our message when it comes to GBP's medium-term bullish trajectory. While the pound (like most us here in the UK) has been feeling the heat this week after a string of data misses and cautious BoE policy comments, we're not inclined to call time on GBP's rally just yet; put differently, it may be getting hot in here, but there's no need to take your positions off just yet.
We now see greater emphasis on today's speech by MPC hawk Micael Saunders (1030 BST); recall he was one of two rate hike dissenters in February, so a dovish backtrack would throw serious doubt over a May BoE rate hike. We think this is unlikely – noting that the fundamental UK economic outlook remains broadly the same as it did in February (if not slightly better if one considers a tighter UK labour market and reduced short-term Brexit uncertainties due to the transition deal). A status quo hawkish Saunders could revive some lost sentiment over a May rate hike and provide support to GBP. We target 1.44 for GBP/USD and 0.87 for EUR/GBP.

USD: Strange week of low Trumpian noise has helped the dollar recover a bit

In a relatively subdued week for geopolitics and protectionism risks, the dollar looks to have enjoyed a shallow relief rally – with the BBDXY index bouncing off its monthly lows (still sub 90). While we have noted the risks from a flat US yield curve, the 10-year yield looks to once again be encroaching the 3% level. Either way, the US curve is pointing to an ominous outlook for risky assets in the near-term – not least as an array of Trumpian uncertainties remain on the table. The week ahead could be about trade risks – with the US Treasury looking into ways to curb Chinese inward investment. We remain watchful over our Twitter feed.

EUR: A lacklustre Mario Draghi may keep EUR/USD trapped in a tight range for now

EUR/USD continues to trade in a tight range – having broadly held the 1.23-1.24 since April 10. Next week's ECB meeting is likely to be fairly dull (see our preview here) – but a cautious Draghi may keep the lid on the single currency for now.

BRL: Growing presidential election risks spells more downside trouble ahead

The Brazilian real continues to trade on a weak footing, which ING's Gustavo Rangel believes is a function of early uncertainty over the presidential elections in October. The markets preferred candidate, Geraldo Alckmin, is polling poorly and there's little clarity on the policies of the other candidates. In the near-term, however, we think Brazilian agricultural exporters will take advantage of the >3.40 levels in USD/BRL to repatriate seasonal earnings. But we doubt any BRL rally lasts long and we now see greater risks of a move above 3.50 as we near the elections – fuelled by persistent political risk that could increase demand for hedging and exacerbate a sell-off in BRL towards previous all-time highs (ie, the 4.00 level).