USD: Fed sticks to patient approach

We expect the Federal Reserve to retain a cautious bias, reducing projections for interest rate hikes from two to one for this year and likely formally announcing the end to quantitative tightening by year-end

Source: Shutterstock

USD: Fed sticks to its patient approach

As per our FOMC Preview, we expect the Fed to retain a cautious bias, reducing projections for interest rate hikes from two to one for this year and likely formally announcing the end to quantitative tightening by year-end. The GDP growth forecast should be largely unchanged. While market expectations are running high and a dovish tilt is largely expected, the lack of downward revision to the GDP growth outlook (as opposed to the ECB, which cut its growth forecast meaningfully earlier in the month) should be positive for risk assets and continue benefiting LatAm FX. We thus see some modest downside to the trade-weighted dollar later today, with USD likely struggling more against emerging markets FX rather than against G10 low yielders.

EUR: Range-bound EUR/USD, strengthening HUF

We expect EUR/USD to remain in the 1.13-1.14 area today as a cautious Fed will have a larger impact on EM FX. In the central and eastern Europe space, the Hungarian forint continues strengthening and has broken below EUR/HUF 313.00. We look for more HUF strength ahead of next week's central bank meeting as investors continue closing their speculative shorts.

GBP: How long will Article 50 be extended?

UK February CPI is expected to nudge modestly higher today to 1.9% year-on-year, but sterling should remain largely unaffected. The focus remains on Brexit and the EU Council meeting on Thursday and Friday, with growing expectations that Prime Minister Theresa May will ask for an Article 50 extension / Brexit delay. The latest reports suggest that only a short extension will be requested by the UK. This would, in our view, limit GBP upside vs more sterling strength in the case of longer extension, given that the economic uncertainty would remain and the Bank of England would not be able to hike.

BRL: Patient monetary policy

While recent developments on inflation and activity suggest that the outlook for monetary policy in Brazil has turned slightly more dovish, we expect central bankers to keep the SELIC policy rate unchanged at 6.5% today, and in the near term (see BACEN Preview). This is largely due to the lingering uncertainties regarding the approval of social security reform, which continue to loom large for the monetary policy outlook. In fact, so long as approval of this reform is uncertain, policymakers may continue to proceed more cautiously than inflation and economic activity data should allow, and characterise the balance of risks for inflation as asymmetrical, skewed to the upside. Hence, today's decision should have a limited impact on the Brazilian real. If fiscal reforms advance in Congress, the BRL should rally, improving inflation forecasts. And local markets should start testing more forcefully the case for SELIC rate cuts.