

USD: Frontloaded easing cycle now priced in

Remarks from Fed member James Bullard have raised expectations of Fed rate cuts- and the dollar has weakened as a result. But there are good reasons to think the dollar will stay supported



➔ USD: Frontloaded easing cycle now priced in

Market expectations of Fed rate cuts have risen further following [comments from Fed member James Bullard](#) about the need to ease policy in light of slowing growth and the risk of escalating trade wars. While the US dollar weakened in response, we note: (a) plenty is already priced in (64 basis points of cuts for this year, and 35 basis points for 2020 – a frontloaded easing cycle). This makes it more challenging for the Fed to surprise on the dovish side in terms of the 2019 outlook; (b) Bullard is one of the most dovish members of the FOMC and doesn't necessarily reflect the consensus; (c) if trade wars intensify, open economies such as the eurozone are likely to be hit too, which may prevent the US-eurozone growth differential from narrowing significantly. Indeed, and despite the USD underperformance of recent days, one can argue that USD has remained relatively resilient in the context of the sharp fall in US Treasury yields. Also note that back in early 2000 when the Fed started to ease and the US-Rest of World interest rate differential narrowed, the USD stayed supported initially. The key focus of the day will be Fed Chair Jay Powell's remarks at the Chicago Fed conference (14:55 UK Time). Should Powell strike a more cautious tone on the easing cycle (vs dovish Bullard yesterday) USD should find some support.

➔ EUR: Inflation unlikely to cause fireworks

We expect both headline and core eurozone inflation to drop following the Easter distortions. Also, as uncertainty continues, businesses tend to take increased costs into their margins, delaying the recovery of core inflation that the higher wage growth would warrant. This should keep a lid on EUR/USD upside though the key driver for the cross today will be Fed Powell's remarks this afternoon.

⬇️ GBP: More downside but at a slower pace

[As per GBP: More downside but at a slower pace](#), the outlook for sterling remains bleak. The currency is set to continue depreciating but the rise in (a) GBP risk premium; and (b) short speculative positioning now suggest a slower pace of depreciation. On the former, we estimate that 2% worth of risk premia is built into GBP vs EUR. On the latter, speculators yet again started building GBP shorts. While we see scope for even larger risk premia or larger speculative shorts, the pace of depreciation should be less aggressive than that seen in May.

➔ PLN: Stable CPI, but market purely focusing on global factors

Poland May CPI is to remain stable at 2.2% year-on-year as the rise in food prices is likely to be offset by lower gasoline costs and core inflation. However, inflation should still rise in the months thereafter to the 2.5% target by summer. Yet neither the zloty nor domestic rates are currently reacting to domestic CPI, as the fall in yields globally is the key driver of market expectations (market currently pricing a partial NBP cut for 2020). PLN reaction to CPI data should be muted.