Yellen and Draghi stars of the EUR - USD show

If Janet Yellen is just a subplot for the US dollar, then Mario Draghi is the director - and lead star - for the euro.

Understandable USD sell-off overreaction to Fed noise

This is arguably the most divided FOMC we've seen since the central bank began normalising policy, with the number one debate being whether the current weakness of US inflation is transitory or transitional. There are two camps within the committee: those that prefer a wait-and-see policy approach given the uncertain inflation outlook and those that are happy to rely on traditional macro relationships like diminishing spare capacity or above-trend growth generating higher future inflation.

We think US data in 2H17 will give us evidence of being somewhere in the middle, which supports our Fed outlook of announcing balance sheet plans in September, and then cautiously hiking again in December. Markets will want confirmation from the incoming US data before fully pricing in a December hike.

> *Gone are the days where central bank officials no longer worry about the market implications of their words.*

Still, we don't think it's profitable chasing broad USD strength on a Fed story. While there will be short-term tactical opportunities like long USD/JPY, the Fed is just one of three factors weighing on the USD. The other two are:

(a) Signs the US economic cycle is beginning to top out in the absence of any pro-growth fiscal stimulus and
(b) What we see as a political risk premium or political uncertainty having an outright adverse effect on the dollar.

Both are how we rationalise the decoupling between USD crosses and short-term interest rate differentials – and why the Fed may just be a subplot for the dollar right now. The bottom line is while the post-minutes USD weakness may be a slight overreaction to Fed noise, it is understandable given a split FOMC and uncertain US political backdrop.

Check out Viraj Patel on CNBC Squawk Box

Cautious ECB means EUR/USD will move lower before moving higher

Reports that President Draghi will not be making any new policy announcements during his Jackson Hole speech next week may have come as a disappointment to EUR bulls hoping for a regime-shifting policy signal from the ECB chief. Since the July ECB meeting, we have been arguing that markets might have got ahead of themselves when it comes to pricing in the ECB's next steps. Less aggressive expectations over the timing and pace of QE tapering chimes with our message that EUR/USD will first move lower before moving higher from these levels.

Without reading too much into yesterday's rumours, the absence of any policy discussion by Draghi does highlight the market-sensitive nature of monetary policymaking. Gone are the days where central bank officials no longer worry about the market implications of their words.

This will be the focus of the July ECB minutes today – with investors watching for whether the Governing Council raise concerns over a premature tightening of financial conditions. While the EUR has so far shown the resilience of a boxer refusing to go down despite taking a few big hits, we believe signs of a more cautious ECB over the coming weeks may see some of this resistance fade. We continue to see scope for a EUR/USD retrace towards 1.15 post-Jackson Hole.

A 'sell on (PM) May and go away' theme for GBP ahead

GBP may be rivalling the USD when it comes to short-term political uncertainty, with a 'sell on (PM) May and go away' type of behaviour emerging ahead of key UK political events in early October. We see this as a short-run phenomenon at best, but understand GBP's attractiveness as a funding currency right now, given the flatter UK curve. GBP/USD downside may be a leveraged way to play a lower EUR/USD, with the added dimension of UK political risks weighing on the pair.