

# Danske Daily

## Fed to cut rates by 25bp or 50bp on 31 July?

### Market movers today

- The data calendar brings no tier 1 releases in today's session. Hence, primary market focus will remain on the earnings season, resurfacing trade war concerns and, not least, FOMC speakers with the Fed's Bullard and Rosengreen set to speak today (see below).

### Selected market news

**Market sentiment** turned swiftly positive yesterday as prominent **FOMC board members of the New York Fed, Williams and Vice Chair Clarida**, delivered very soft remarks highlighting the need for swift action before economic data actually turns for the worse. The remarks at first seemed very coordinated, driving a weaker USD, a drop in front US yields and a sharp rally in the August Fed funds futures, essentially leaving market pricing skewed towards a 50bp July cut rather than the consensus 25bp cut. Meanwhile, this morning, the New York Fed stressed that Williams had not tried to send a specific policy signal, leading to a rebound of more than half the initial drop in US 2Y swap rates, even if the USD FX gains were more modest with EUR/USD, for example, staying around 1.1260.

Where does this leave us in terms of **the Fed and the forthcoming 31 July meeting**? Yesterday's remarks were highly surprising given the Fed's communication earlier this week that seemed to want to limit market pricing of a 50bp July cut. Meanwhile, with little time until the one-week silent period, markets now have a 25bp July cut at 60% and a 50bp cut at 40% probability. We know that historically the Fed has not wanted to surprise markets at the meetings, leaving the coming sessions' FOMC comments crucial. For now, our call remains a 25bp cut at the 31 July meeting and an additional 50bp worth of cuts for the rest of the year. However, we must acknowledge the probability of this call getting modified towards a more aggressive July call if we get further very soft Fed remarks.

A *Bloomberg story* yesterday suggested that **informal analysis has begun at the ECB** about a potential revamp of the inflation target. This mirrors a discussion the Governing Council already started at the June meeting about the need to adopt a more "symmetrical" interpretation of the inflation target, i.e. where the ECB would tolerate inflation above the target to compensate for persistent undershooting in recent years. Although we think such a switch to a more state-dependent and less calendar-based forward guidance could help alleviate the risk of de-anchoring inflation expectations, as it strengthens the easing bias, we do not see such changes as imminent – and is also highly dependent on whether the markets believe the ECB could achieve an overshooting. For now, the ECB's prime focus should be on delivering a convincing easing package at the September meeting. Nevertheless, it could be the advent of a discussion that gains further traction under a Lagarde-led ECB.

Yesterday in the UK, a **majority in the House of Commons** passed an amendment making it harder for the government to prorogue Parliament in the run-up to the current Brexit date of 31 October. While this does not prevent a no deal Brexit outcome (it is still the default option from a legal point of view), it makes it more difficult for Boris Johnson (assuming he wins the leadership contest) to force a no deal Brexit through by sending Parliament home. Some 17 Conservative rebels voted against their own government (which did not include politicians such as Phillip Hammond), supporting our view that it is hard to find a majority for a no deal Brexit outcome. As we have highlighted several times, we may soon have a more pro-Brexit prime minister but it does not change the arithmetic in the Commons.

### Holiday edition

#### Selected readings from Danske Bank

- *FX Edge: The EUR and ECB – rate cuts are all that matter*
- *US-China Trade - Ceasefire a reality but no quick fixes to reach a deal*
- *Euro Area Macro Monitor: ECB's credibility on the line*
- *Japanese Investor Flows into Foreign Sovereign Debt for May 2019*

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## Key figures and events

Friday, July 19, 2019			Period	Danske Bank	Consensus	Previous
1:30	JPY	CPI - national	y/y	Jun	0.7%	0.7%
1:30	JPY	CPI - national ex. fresh food	y/y	Jun	0.6%	0.8%
10:00	EUR	Current account	EUR bn	May		20.9
14:30	CAD	Retail sales	m/m	May	0.3%	0.1%
16:00	USD	University of Michigan Confidence, preliminary	Index	Jul	98.4	98.2
17:05	USD	Fed's Bullard (non-voter, dovish) speaks				
22:30	USD	Fed's Rosengren (non-voter, hawk) speaks				

Source: Bloomberg, Danske Bank

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**Report completed:** 19 July 2019, 06:17 CEST

**Report first disseminated:** 19 July 2019, 07:00 CEST