

Could “Breturn” provide a boost for sterling?

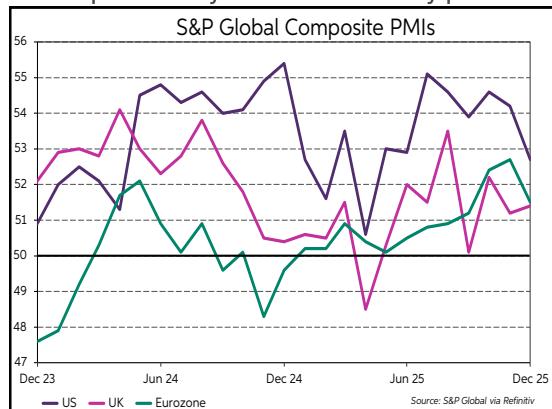
■ **2026 marks the 10-year anniversary of the Brexit referendum in the UK.** Yet, almost a decade on, the debate continues, as highlighted by the recent suggestions from UK PM Starmer of a move back towards Single Market access. In 2016, the UK was the 5th largest economy in the world, roughly about 85% the size of Germany's. It is now the 6th, and about 80% the size of a recently stagnant German economy. Indeed, new research now shows the damage the Brexit vote has caused the UK economy. A paper published in the National Bureau of Economic Research (NBER), estimates that Brexit has reduced UK GDP by between 6-8%, lowered investment by 12-18%, cut employment by 3-4% and dampened productivity by 3-4%. This exceeds predictions made at the time of the referendum, when economists estimated a leave vote could lower GDP by 4-6%.

■ **Brexit has particularly impacted sterling.** In the decade up to the referendum result, EUR/GBP averaged around 80p but frequently traded below that threshold. In the 10 years since, it has not traded near to 80p, and has averaged close to 87p. The depreciation of the pound has not been enough to offset newly erected trade barriers. Goods exports are roughly 15% below their pre-2020 trend. True, services exports have expanded at a healthy pace since the Brexit deal was announced. However, another study from the London School of Economics, estimates that they are roughly 4-6% lower because of Brexit, as the UK's access to the single market has not been offset by increased market share outside of the EU.

■ **Of course, the UK economy still has many strengths.** London remains the second largest financial sector in the world, and its share of lucrative derivative and forex trading has risen in recent years. The fiscal deficit is lower than most G7 peers, including the US and France. Furthermore, the UK has consistently ranked as one of the fastest adopters of AI. However, the main drag on the economy since the Global Financial Crisis has been weak productivity growth, exacerbated by Brexit. The Labour government came to power promising to boost growth, yet it has failed to outline a coherent economic plan to lift productivity.

■ **Meanwhile the “reset” in relations between the EU and UK has so far yielded only marginal results.** The Government's own calculations project that the policies announced to date may add just 0.3% to UK GDP by 2040. A bolder economic strategy could place a new relationship with the EU at its centre. In this regard, PM Starmer's apparent openness to “closer alignment” to the EU's single market is a positive step, ahead of the first 5-year review of the Trade and Co-operation Agreement, expected this year. Greater exposure for UK firms to EU markets could support both growth and productivity. It would also likely provide a boost for sterling - although, a “Breturn” dividend still seems some way off yet.

■ **This week, a busy UK data calendar contains updates on the labour market and the consumer (prices, sales and confidence).** Conditions in the labour market have softened over the past year. The unemployment rate has increased steadily, from 4.4% in January to 5.1% in October, its highest level since January 2021. Against this backdrop, wage inflation has cooled. Average earnings growth fell to +4.7% y/y in the three months to October. The consensus is for the jobless rate to fall to 5.0% in November, and for wage growth to slow to 4.6% y/y. Meantime, headline inflation is projected to rise marginally to 3.3% in December, but the core rate is set to stay at 3.2%. Elsewhere, a 0.1% decline in retail sales is pencilled in for a second successive month in December. Encouragingly, consumer confidence is expected to improve to -16.0 in January, its best reading since August 2024.



■ **In the US, core-PCE inflation, personal consumption and income, as well as the final reading of GDP for Q3 will feature.** Throughout the first three quarters of 2025, core-PCE inflation has been quite sticky. It started the year at 2.8%, fell to a low of 2.6% in April, but peaked at 2.9% in July/August, before edging back to where it began the year, at 2.8% in September. The October data were postponed due to the Government shutdown, but will be released alongside the November report. Expectations are for core-PCE to inch down to 2.7% in November. Similarly, the October and November personal income and consumption updates will be released together. A 0.4% rise in the former and a 0.5% increase in the latter is anticipated in November. The final estimate of US Q3 GDP growth is set to confirm the economy expanded by 4.3% annualised in the quarter.

■ **The flash PMIs for January in the Eurozone, UK and US are also due.** The Eurozone services PMI has been in expansion mode since June, albeit it fell to 52.4 in December. In contrast, the manufacturing PMI has been in contraction territory in three of the last four months. The consensus is for a slight increase in both in January, although the manufacturing survey is set to remain consistent with a further decline in activity. In the UK, the services sector is also outperforming manufacturing, but crucially both sectors have stayed above the key 50 level. This trend is set to continue in January, with the manufacturing PMI edging up to 50.7 and the services PMI to 51.7. Meantime, the US PMIs have printed above 50 in recent months, but they fell to their lowest levels since April and July, respectively, in December. However, an improvement to 52.0 and 52.8 is expected in January.

Interest Rate Forecasts				Exchange Rate Forecasts (Mid-Point of Range)				
Current	End Q1 2026	End Q2 2026	End Q3 2026	Current	End Q1 2026	End Q2 2026	End Q3 2026	
Fed Funds	3.625	3.625	3.375	3.125	EUR/USD	1.1622	1.17	1.18
ECB Deposit	2.00	2.00	2.00	2.00	EUR/GBP	0.8670	0.88	0.88
BoE Repo	3.75	3.75	3.50	3.50	EUR/JPY	183.47	179	179
BoJ OCR	0.75	0.75	0.75	0.75	GBP/USD	1.3399	1.33	1.34
Current Rates Reuters, Forecasts AIB's ERU				USD/JPY	157.85	153	152	
				Current Rates Reuters, Forecasts AIB's ERU				

ECONOMIC DIARY

Monday 19th - Friday 23rd January

Date	UK & Irish Time (GMT+1)	Release	Previous	Forecast
This Week:				
World Economic Forum (19th-23rd January)				
Mon 19th		Martin Luther King Jr. Day (Market Holiday)		
	US:			
	EU-21:	10:00 Final HICP Inflation (December)	-0.4% (+2.0%)	-0.4% (+2.0%)
		- Ex-Food & Energy	-0.4% (+2.3%)	-0.4% (+2.3%)
		- Ex-Food, Energy, Alcohol & Tobacco	+0.3% (+2.3%)	+0.3% (+2.3%)
Tue 20th		Producer Prices (December)	+0.0% (-2.3%)	-0.1% (-2.4%)
	GER:	07:00	5.1%	+5.0%
	UK:	07:00 Unemployment Rate (November)	-38,000	
	UK:	07:00 HMRC Payrolls Change (December)	20,100	
	UK:	07:00 Claimant Count (December)	(+4.7%)	(+4.6%)
	UK:	07:00 Average Earnings Growth (November)	(+4.6%)	(+4.5%)
		- Ex-Bonus		
	GER:	10:00 ZEW Economic Sentiment (January)	45.8	50.0
Wed 21st		CPI Inflation (December)	-0.2% (+3.2%)	+0.4% (+3.3%)
		- Core-CPI	-0.2% (+3.2%)	+0.3% (+3.2%)
		- Services CPI	-0.2% (+4.4%)	(+4.5%)
	UK:	07:00 PPI Input Prices (December)	+0.3% (+1.1%)	+% (+%)
		- PPI Output Price Inflation	+0.1% (+1.1%)	+% (+%)
	UK:	11:00 CBI Trends—Orders (January)	-32.0	
	UK:	11:00 CBI Business Optimism (Q1)	-31.0	
	IRE:	11:00 Residential Property Prices (November)	+0.6% (+7.3%)	+0.5% (+7.0%)
Thu 22nd		ECB Monetary Policy Account (17-18th Dec)		
	EU-21:	10:00		
	UK:	11:00 CBI Distributive trades (January)	-44.0	
	US:	13:30 GDP (Q3: Final Reading)	+4.3% S.a.a.r.	+4.3% S.a.a.r.
	US:	13:30 PCE Prices (Q3: Final Reading)	+2.8x% S.a.a.r.	+2.8% S.a.a.r.
		- Core-PCE Prices	+2.9% S.a.a.r.	+2.9% S.a.a.r.
	US:	13:30 Initial Jobless Claims (w/e 12th January)	+198,000	
	US:	15:00 Personal Income / Consumption (November)	+0.4% / +0.4%	+0.4% / +0.5%
	US:	15:00 PCE prices (November)	+0.3% (+2.8%)	+0.2% (+2.7%)
		- Core-PCE Prices	+0.2% (+2.8%)	+0.2% (+2.7%)
	JPN:	23:50 CPI Inflation (December)	(+2.9%)	
		- Core CPI Inflation	(+3.0%)	(+2.4%)
Fri 23rd		BoJ Interest Rate Announcement	0.75%	0.75%
	JPN:			
	UK:	00:01 Gfk Consumer Confidence (January)	-17.0	
	JPN:	00:30 Flash S&P Composite PMI (January)	51.1	
	UK:	07:00 Retail Sales (December)	-0.1% (+0.6%)	-0.1% (+1.0%)
		- Ex-Fuel	-0.2% (+1.2%)	-0.2% (+1.4%)
	FRA:	07:45 INSEE Business Climate (January)	99.0	98.0
	FRA:	08:15 Flash HCOB Composite PMI (January)	50.0	50.1
	GER:	08:30 Flash HCOB Composite PMI (January)	51.3	51.8
	EU-21:	09:00 Flash HCOB Composite PMI (January)	51.5	51.6
		- Manufacturing / Services	48.8 / 52.4	49.0 / 52.5
	UK:	09:30 Flash Composite PMI (January)	51.4	51.7
		- Manufacturing / Services	50.6 / 51.4	50.7 / 51.7
	US:	14:45 Flash S&P Composite PMI (January)	52.7	52.9
		- Manufacturing / Services	51.8 / 52.5	52.0 / 52.8

♦ Month-on-month changes (year-on-year shown in brackets)

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