Weekly Market Brief

AIB Treasury Economic Research Unit

8th - 12th June 2020

Euro Rally Faces Some Big Hurdles

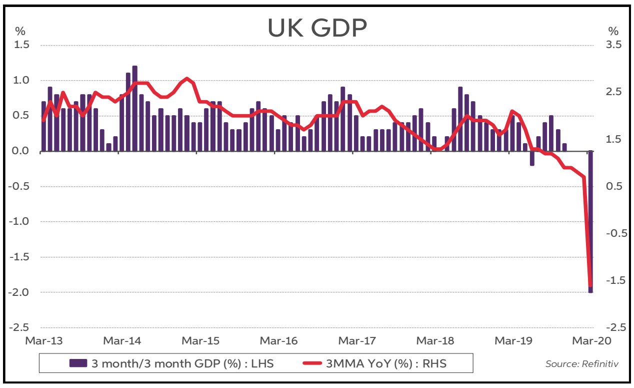
- **The buoyed up sentiment on global financial markets is spilling over into forex rates, with some big currency moves in recent weeks.** The three traditional safe-haven currencies, the Swiss franc, US dollar and especially the yen have come under significant selling pressure. The euro has been a major beneficiary as the ECB, the EC and national governments roll out large-scale stimulus packages – this has also seen European stocks markets play catch-up recently in the global equity rally. The EUR-USD rate has climbed to above $1.13 from $1.08 in mid-May. EUR-YEN has risen from ¥115 to ¥124, a 12-month high. Other currencies have also made significant gains against the greenback and yen. The Aussie dollar has rebounded from lows near $0.55 in mid-March to $0.70. Meanwhile, cable has risen from $1.15 to above $1.26 over the same period, despite growing concerns about the risk of a no-deal, hard Brexit at end 2020. The US currency has fallen from C$1.46 to C$1.35 against the Canadian dollar in the same timeframe.

- **It should be noted that the safe-haven currencies are coming off extremely high levels and, indeed, remain elevated on a historical basis.** The US dollar's trade-weighted index is back to levels that it traded at for much of last year and is still some 10% above the lows it hit in early 2018. Indeed, the EUR-USD rate is only moving back into the $1.12-1.15 trading range that it occupied during the first half of last year. It is hard to call the next big moves in FX markets. The EUR/USD rate has been confined to a narrow corridor of €1.07-1.15 since the autumn of 2018. A return to heightened risk aversion on markets, possibly on fresh concerns over the economic outlook associated with ongoing COVID-19 restrictions, would likely trigger a renewed flight back into safe-haven currencies. This could see the euro fall quickly back below the $1.10 level. On the other hand, if a robust and sustained recovery takes root in the second half of the year, the dollar and yen could continue to lose ground.

- **However, it is going to be difficult for the euro to rise over$1.15, which it has not traded above since Q4 2018.** Indeed, profit taking by traders could soon halt the dollar's slide as market positioning is now quite short the currency. A move above $1.20 would be a tall order for the euro as it has not been above this level since the ECB moved to negative rates in 2014, with the exception of a brief period in H1 2018. The Fed continues to rule out negative rates for the US, while markets expect the ECB to maintain negative rates for much of the coming decade. Negative rates, then, are likely to remain a headwind for the euro, notwithstanding the fact that much of the interest rate differential supporting the dollar has been eroded by Fed rate cuts.

- **The currency we remain most concerned about is sterling, given the lack of progress in the EU-UK trade talks and with the British Government continuing to flatly rule out an extension to the end December deadline to reach a trade deal.** This points to either a very limited 'bare-bones' trade deal with the focus on avoiding tariffs, or no-trade deal at all and UK-EU trade being conducted under WTO rules from next year. The latter would be very negative for sterling. The UK currency has lost considerable ground against the euro since earlier in the year. It could prove to be a difficult second half to the year for sterling if negotiations remain bogged down and it appears that we may be heading for another cliff-edge Brexit date in December. EUR-GBP could head towards last year's Brexit related uncertainty high of 93p in such circumstances.

- **This week, it's the turn of the Federal Reserve to hold its June policy meeting.** No changes are expected to be made to the funds rate, which is effectively at zero. Markets had briefly toyed with the possibility of negative rates, but Chair Powell pushed back against this. Instead, the Fed has stressed that rates will remain lower for longer. With regard to net asset purchases, the central bank has already announced essentially unlimited QE, but markets will be eager to gain any further insight into whether the Fed is willing to officially countenance the possibility of some form of yield curve control. Finally, the central bank will also publish its latest macro projections this week, its first set since December.



- **Data-wise, the May reading of CPI is due in the US.** The collapse in oil prices, combined with the negative demand shock stemming from the Covid-19 crisis, may see headline inflation edge down to 0.2% from 0.3%. In terms of timelier data, the re-opening of the economy is projected to result in the flash reading of the Michigan consumer sentiment index moving higher in June. **On this side of the Atlantic, the highlight is the monthly estimate of GDP in the UK.** In April, the imposition of a stringent lockdown is projected to result in an unprecedented collapse in output of 18.7% in the month. The PMIs suggest that the services sector bore the brunt of the damage. Although, the output subcomponent of the manufacturing index also plunged in the month, which will be reflected in the industrial production report for April that is also set for release this week. **The April print of industrial production is the main item of interest on the Eurozone calendar.** Output is forecast to have plummeted by 20% in the month on an already depressed March level as factories remained closed due to Covid-19 related restrictions.

Interest Rate Forecasts	Current	End Q2 2020	End Q3 2020	End Q4 2020
Fed Funds	0.125	0.125	0.125	0.125
ECB Deposit	-0.50	-0.50	-0.50	-0.50
BoE Repo	0.10	0.10	0.10	0.10
BoJ OCR	-0.10	-0.10	-0.10	-0.10

Current Rates Reuters, Forecasts AIB's ERU

Exchange Rate Forecasts (Mid-Point of Range)	Current	End Q2 2020	End Q3 2020	End Q4 2020
EUR/USD	1.1301	1.12	1.13	1.13
EUR/GBP	0.8913	0.90	0.92	0.88
EUR/JPY	123.91	122	123	123
GBP/USD	1.2675	1.21	1.23	1.28
USD/JPY	109.64	109	109	109

Current Rates Reuters, Forecasts AIB's ERU

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ECONOMIC DIARY

Monday 8th - Friday 12th June

Date	*UK & Irish Time (GMT+1)*		*Release*	*Previous*	*Forecast*
This Week:	**ECB Speakers:**		**Lagarde** (Monday); de Guindos (Tuesday); de Guindos, Schnabel (Wednesday)		
Mon 8th	**JPN:**	00.50	GDP (Q1: Second Reading)	-3.4% s.a.a.r.	-2.1%
	JPN:	06.00	Economy Watchers' Poll (May)	7.9	
	GER:	07.00	Industrial Output (April)	-9.2%	-16.8%
	EU-19:	09.30	Sentix Index (June)	-41.8	-22.5
Tue 9th	**GER:**	07.00	Trade Balance (April)	€12.8bn	€10.0bn
			- Exports	-11.8%	-25.0%
	FRA:	07.45	Trade Balance (April)	-€3.34bn	
	EU-19:	10.00	Employment (Q1: Final Reading)	-0.2% (+0.3%)	-0.2% (+0.3%)
	EU-19:	10.00	GDP (Q1: Third Reading)	-3.8% (-3.2%)	-3.8% (-3.2%)
	US:	11.00	NFIB Business Optimism (May)	90.90	
Wed 10th	**JPN:**	00.50	Domestic Wholesale Prices (May)	(-2.3%)	(-2.4%)
	JPN:	00.50	Machinery Orders (April)	(-0.7%)	(-14.0%)
	FRA:	07.45	Industrial Output (April)	-16.2%	-20.0%
	US:	13.30	CPI (May)	(+0.3%)	(+0.2%)
			- Core (Ex-Food & Energy)	(+1.4%)	(+1.3%)
	US:	19.00	Fed Interest Rate Announcement	0.00-0.25%	0.00-0.25%
	US:	19.30	Fed Press Conference		
Thurs 11th	**UK:**	00.01	RICS House Price Survey (May)	-21	-24
	ITA:	09.00	Industrial Output (April)	-28.4%	-25.8%
	IRL:	***11.00***	***CPI (May)***	***-0.4% (-0.1%)***	***-0.1% (-0.1%)***
	US:	13.30	Initial Jobless Claims (w/e 6th June)	1,877,000	1,500,000
	US:	13.30	PPI (May)	(-1.2%)	(-1.1%)
Fri 12th	**UK:**	07.00	GDP (3 Months to April)	-2.0% (-5.7%)	-10.0% (-22.3%)
	UK:	07.00	Industrial Output (April)	-4.2% (-8.2%)	-15.0% (-19.3%)
			- Manufacturing	-4.6% (-9.7%)	-15.0% (-19.9%)
	UK:	07.00	Goods Trade Balance (April)	-£12.508bn	-£11.35bn
			- Non-EU	-£4.880bn	
	FRA:	07.45	Final HICP (May)	(+0.2%)	(+0.2%)
	EU-19:	10.00	Industrial Production (April)	-11.3% (-12.9%)	-20.0% (-29.5%)
	US:	15.00	Prelim' Michigan Consumer Sentiment (June)	72.3	74.8

♦ *Month-on-month changes (year-on-year shown in brackets)*
All forecasts AIB ERU, historical data in the Economic Diary derived from publicly available sources

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