CURRENCY FORECAST
JULY 2020

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JUNE REVIEW & JULY RISK EVENTS & THEMES

POUND STERLING

June turned out to be another subdued month for Sterling, as worries over the economic consequences of the Covid-19 lockdown combined with knife-edge Brexit negotiations prevented the UK currency from rallying. This saw the Pound depreciate around 2 percent against the Euro in Q2, and 0.2 percent against the US Dollar. But it was against the Australian Dollar which the Pound suffered the worst, with GBP/AUD posting an 11 percent slump in Q2.

Sterling suffered a further weakening at the end of June when data showed the UK economy had contracted by 2.2 percent in the first quarter: this was worse than the estimate of a 2 percent contraction. The data represented the greatest stumble in GDP growth in 40 years and has caused concern that the UK may have sustained more damage than initially assumed. In fact, several forecasts made by international organisations indicated the UK may have suffered more than any other developed nation due to the coronavirus restrictions. At the same time, it was revealed that business investment in the UK economy had fallen by 0.3 percent, which was the second consecutive quarter of contraction. These factors combined to kill off Sterling's upside potential.

GBP/USD ended June at $1.24 as UK Prime Minister Boris Johnson announced plans for a 'Rooseveltian New Deal' to boost the economy. The PM promised to 'take a scythe through red tape' and spark a construction boom. Markets seemed to find positive sentiment in his words, despite a number of high-profile job losses in the aviation and retail sectors being announced around the same time. Earlier in the month the Pound had traded at a high of $1.28 on rising risk appetite before falling back again. This was despite a general weakening trend for USD over the month.

It was a similar story with the Euro, with GBP/EUR slipping from €1.12 at the start of the month to €1.10 by the end. The Pound has now been devaluing against the Euro for over three months, even though sentiment towards the Euro on the wider market remains weak.

The Bank of England continued to boost its bond-buying programme, adding another £100bn to the balance sheet in an effort to shore up borrowing in the face of the extra pandemic costs. Total government debt exceeded GDP for the first time in 50 years due to these surging levels of borrowing.

EURO

As markets once again reverted to risk-off mode, the Euro weakened against the US Dollar, despite having risen to a three-month high earlier in the month. By the end of June EUR/GBP was trading at £0.91 while EUR/USD sat at $1.13. The Euro's strength earlier on in the month was attributed to the announcement of a massive European bailout plan totalling €750bn, however confidence faded once political divisions between EU members became apparent.

Sentiment towards the Euro has been suffering from the same barrage of negative economic news that has affected the Pound, even though flash PMIs indicate the Eurozone economy is bouncing back following the Covid-19 lockdown and shows all the signs of a V-shaped recovery albeit in its early stages. Nevertheless, news that the US is preparing to impose $3.1bn of tariffs on EU exports weighed on investor sentiment and reduced the appeal of the single currency.

For the GBP/EUR exchange rate, the negative sentiment towards the Euro was outweighed by the gravity of the UK-EU Brexit talks, with both Boris Johnson and EU chief negotiator Michel Barnier hardening their stances over their respective positions. Mr Barnier said it would likely not be possible for the UK to insulate the City of London from the consequences of Brexit, adding that UK demands were 'unacceptable'. This position rattled market confidence in Sterling, despite Boris Johnson's optimism that a deal would be struck, causing GBP/EUR to sink.

UNITED STATES DOLLAR

June saw support ebb away for the Greenback as markets turned risk-on in the light of an improving world economy, only for that sentiment to evaporate on news that new Covid-19 clusters could lead to further economic shutdowns. This saw the slide in USD put on pause.

Although there was no central bank action in June, with base rates remaining slightly above zero, Federal Reserve Chair Jerome Powell and US Treasury Secretary Steven Mnuchin warned that a resurgence of Covid-19 cases could cause further economic impacts.

Testifying before the House Financial Services Committee, Powell stated, "The path of the [US] economy is highly uncertain," – a sentiment seemingly at odds with President Trump's bullish rhetoric on the economy. Mr Powell's comments were taken by USD bears as evidence that 'bad news' may now also be 'bad news for the US Dollar' in the absence of further risk-on sentiment, and by 30 June the US Dollar Index was trading down at 97.1.

Economic data continued to improve for the US economy, with May's apocalyptic jobs figures rebounding somewhat in June, showing a record-breaking 2.5 million new jobs created. In addition, ISM figures showed the biggest expansion of US industrial activity in 14 months, potentially indicating a strong recovery in the US economy.

KEY DATES

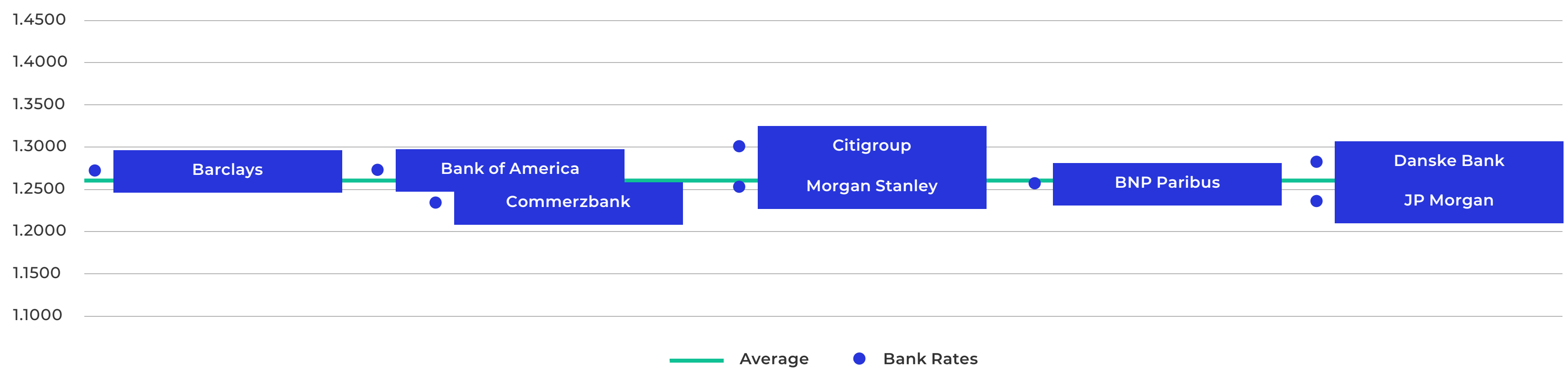
UNITED KINGDOM	
3 July	Markit Services/Composite PMI
14 July	GDP Growth Rate (May)
14 July	Manufacturing Production
15 July	Core Inflation Rate (June)
16 July	Unemployment Rate (May)
23 July	Retail Sales Data (June)

EUROZONE	
3 July	Markit Services/Composite PMI
6 July	Retail Sales (June)
17 July	Core Inflation (June)
17 July	Construction Output (May)
31 July	GDP Growth Rate (Q2)

UNITED STATES	
6 July	Markit Services/Composite PMI
9 July	Initial Jobless Claims (July)
16 July	Retail Sales (June)
29 July	Fed Interest Rate Decision
30 July	GDP Growth (Q2)

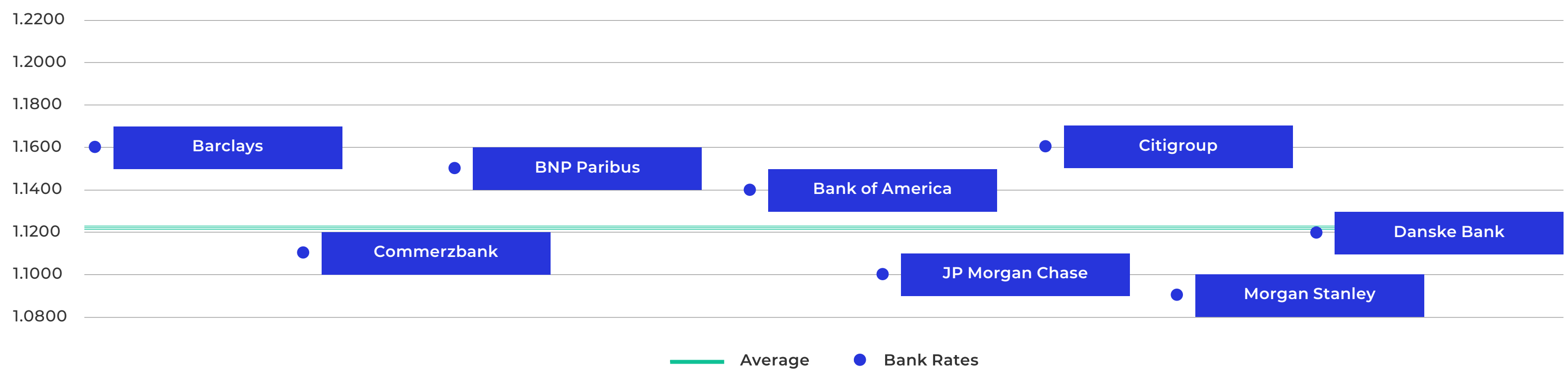
GBP/USD TOP BANK FORECASTS

BANKS	Q2
Barclays	1.2700
BNP Paribus	1.2600
Bank of America	1.2700
Citigroup	1.3000
Commerzbank	1.2400
Danske Bank	1.2800
JP Morgan	1.2400
Morgan Stanley	1.2500



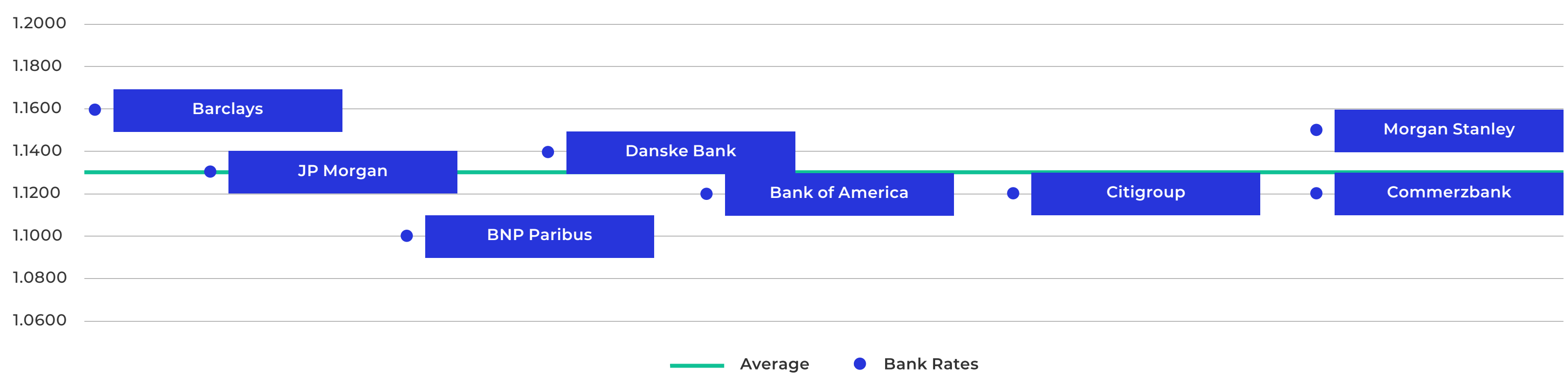
GBP/EUR TOP BANK FORECASTS

BANKS	Q2
Barclays	1.1000
BNP Paribus	1.1500
Bank of America	1.1400
Citigroup	1.1600
Commerzbank	1.1100
Danske Bank	1.1200
JP Morgan Chase	1.1000
Morgan Stanley	1.0900



EUR/USD TOP BANK FORECASTS

BANKS	Q2
Barclays	1.1600
BNP Paribus	1.1000
Bank of America	1.1200
Citigroup	1.1200
Commerzbank	1.1200
Danske Bank	1.1400
JP Morgan	1.1300
Morgan Stanley	1.1500



KEY THEMES

UNITED KINGDOM

Ongoing Brexit negotiations: It has been exactly four years since the referendum on the UK leaving the EU, and negotiations are now stepping up in pace. Prime Minister Boris Johnson is confident that a UK-EU trade deal can be reached by the end of July, with intensive weekly meeting taking place. However, most analysts are less certain about Mr Johnson's optimism and view the odds of such a deal being reached as slim. If no deal is forthcoming in July it is highly likely that Sterling will suffer on FX markets as a result, with traders likely assuming the default scenario of a no-deal Brexit.

Regional resurgences of Covid-19 could hit Pound: Already the UK Midland city of Leicester has been placed into a secondary lockdown following a sudden surge of new coronavirus cases, and the fear is that a number of other high-population cities will follow suit. With so much depending on an economic rebound, Sterling is likely to suffer if it appears a second wave of the virus is resurgent and economic activity is once again curtailed. As the Pound becomes increasingly vulnerable to risk sentiment there could be downside implications should a wider viral outbreak occur and investors retreat to safe havens once again.

Q3 GBP/USD bank averaged forecast: 1.2638

EUROZONE

Eurozone growth outlook. Euro investors expect momentum in the Eurozone economy will continue to build during the month of July and that the bloc will sustain a V-shaped recovery. The current annualised rate of GDP growth is -3.1 percent, so it is seen as vital that leaders of EU member states come together and agree to the proposed stimulus package if such a recovery is to continue. Confidence remains fragile in the Euro, so any sign of disagreement between member states is likely to weaken the currency.

What is the ECB's next policy move? At zero percent, there is little room for adjustment in the Eurozone base rate that would appease markets. On the other hand, the European Central Bank's (ECB) massive stimulus package has the potential to boost growth in the Eurozone, and it is this the market is focusing on at present. If the ECB can convince that it is offering unconditional support to bailing out stricken economies, we can expect the positive sentiment to remain towards the Euro.

What is the Political risk in the region? The post Covid-19 political landscape in Europe is still emerging, with early signs indicating that fractures remain within the bloc, especially with regard to stimulus measures. The next test for the Euro will come on 17 July when leaders of EU member nations meet in Brussels to discuss the proposed Covid-19 bailout package. Last week all 27 leaders failed to agree on the package, revealing old fractures among the bloc members.

Q3 GBP/EUR bank averaged forecast: 1.1213

UNITED STATES

What is the Fed's next policy move likely to be? Currently the annualised growth rate in the US is estimated to be -5 percent, but there could be a shock in store later this month when the Q2 growth figures are expected to show a decline of at least 30 percent. With US interest rates only slightly above zero there is little scope for monetary action by the Federal Reserve, so markets are focusing on stimulus measures designed to boost growth. Any positive growth data is likely to facilitate a risk-on movement in markets.

What are the political risks in the region? There continues to be an upsurge of protests and civil unrest across the US, adding to the sense that political risk is only likely to escalate in the run-up to the November presidential election. Sentiment continues to be driven by shifts between the recovery narrative and fears that a second wave of Covid-19 will once again paralyse the economy. For the time being, direct income support for households and furloughed workers has allowed consumers to carry on spending and firms to keep people on the books, but when these schemes are wound down there is a risk of a spike in unemployment and a hit to consumer spending, both of which have the potential to create economic and political damage.

Q3 GBP/USD bank averaged forecast: 1.1300

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