



## **The Euro just can't catch a break**

Market Report 19/04/22 - By Sam Balla-Muir

### **USD**

The US dollar strengthened against nearly all other G10 currencies last week, including a roughly 0.6% rise against the euro. The British pound was the only major developed market currency that the US dollar weakened against, and even then only by around 0.2%. Economic data released in the US last week confirmed that price pressures remain strong, with CPI inflation rising to another 40-year high in March. Other data for retail sales and industrial production showed that the US economy remained in good health last month too. That combination of high inflation and a robust economy has further bolstered the case for the Federal Reserve to rapidly raise US interest rates, boosting the dollar's appeal.

Indeed, a couple of key Fed policymakers added further fuel to the fire in speeches last week, suggesting that even if "core" price pressures – which exclude energy and fuel prices – ease from here, they will still press on with plans to raise rates rapidly, so long as core inflation remains above their 2% target. I suspect that growing bets of much tighter monetary policy will continue to push the US dollar higher over the coming months. The Federal Reserve's next policy meeting on 4<sup>th</sup> May, where investors are expecting a further 0.5%-pt rise in US interest rates, could prove to be a key juncture.

### **GBP**

The roughly 0.2% rise in the British pound against the US dollar last week, and 0.9% or so climb against the euro, meant that sterling was the best-performing G10 currency. The pound's resilience may in part reflect how relatively market-friendly Chancellor Rishi Sunak has retained his job, despite recent political scandals. However, much like the US dollar, the pound's gains also reflected how recent economic data supported the case for the Bank of England to press ahead with raising interest rates. This included data showing that UK inflation rose to 7.0% last month – a 30-year high – as well as news that the UK unemployment rate continued to fall in March.

The Bank of England appears set to raise interest rates further over the coming months, and will probably deliver enough monetary tightening to push up the pound a little relative to the euro. However, when it comes to the pound/US dollar exchange rate, I suspect that sterling could weaken, as the Bank of England raises interest rates by less relative to expectations than the US Federal Reserve does. After all, surges in the price of oil and utilities bills, as well as recent tax increases, are hurting real incomes in the UK in a way that is not happening in the US.

## **EUR**

The euro struggled last week, dropping by roughly 0.9% against the British pound and by around 0.6% against the US dollar. This may have reflected ongoing worries about the threat to the Eurozone from Marine Le Pen potentially winning the French presidency later this month. It was announced late on Sunday 10<sup>th</sup> April that she would go head-to-head against President Macron in the second and final round of the French presidential election on 24<sup>th</sup> April. But the other reason for the weakness in the euro was probably the European Central Bank's messaging from its policy meeting, which showed far fewer signals that the Bank is shifting towards tighter monetary policy and higher interest rates than many traders had expected.

Even were it not for French politics, I would still expect the euro to weaken by a bit more relative to the pound and US dollar over the coming months. That ultimately reflects a view that the Eurozone economy remains in a fairly weak position, not least because of its current struggles weaning itself off of Russian energy. Against that backdrop, I think that the euro will struggle as the European Central Bank fails to provide quite as much monetary tightening as investors expect.

## **The Week Ahead**

The coming week has few important economic data releases due in the US, though with next week the final one before the Federal Reserve's customary "blackout period" in the week before its policy meetings, a raft of speeches due from Fed policy makers may prompt some volatility in the US dollar. While UK data on March retail sales and the widely tracked flash PMI activity surveys for April may provide market-moving information on the British economy, a speech by Bank of England Governor Andrew Bailey late on Thursday may prove to be more important for the pound. Finally, the calendar for economic data is also relatively light next week for the Eurozone, with the key story to watch for the

euro likely to be the final week of campaigning for the French presidential elections. Wednesday night's TV debate between President Macron and Marine Le Pen may be a turning point.

#### Last Week's Changes In Exchange Rates

Exchange Rate%- change on week

€ per £ +0.85

\$ per £ +0.21

\$ per € -0.64

#### Key Events

Date	Market	Time (GMT)	Release/Event	Period	Previous	Analysts' Expectation
Thu. 21st	UK	17.30	BOE Governor Bailey speaks	Mar.	-	-
Fri. 22nd	EZ	08.30	German Manufacturing & Services PMI	Mar.	56.9	54.6
Sun. 24th	EZ	-	French Presidential Election (2nd Round)	Apr.	-	-