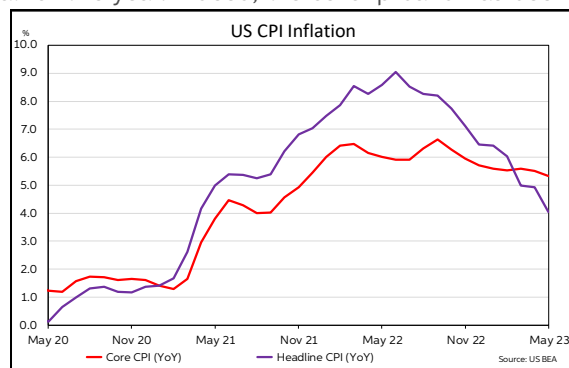


Good First Innings for Sterling

- From a currency viewpoint, one of the biggest surprises over the first half of 2023 has been the strength of sterling.** The pound has made gains against other majors including the dollar and the euro. The magnitude of these gains has been in the order of 4-5%. In level terms, this is reflected in EUR/GBP falling back from the 88p mark, with the pair trading to a low down near to 85p since mid-June. Meanwhile, the stronger tone to sterling was also evident in GBP/USD, with the pair moving up from its early January level of \$1.18, to close to the \$1.28 threshold in the past month.
- One reason for sterling's strong performance year-to-date has been the macro backdrop where the UK economy has proved to be more resilient than had been expected.** The general consensus heading into 2023 was that the UK economy was likely to enter recession this year. Indeed, the BoE, in its November 2022 forecast update, was projecting the UK economy could contract by up to 1.5% this year. Year-to-date though, UK macro data has tended to surprise to the upside of forecasts. Albeit, the UK economy has stagnated rather than contracted, with GDP essentially continuing to flat-line since the second quarter of last year.
- At the same time, over the last number of months, sterling has benefitted from widening interest rate differentials, with the BoE continuing to hike interest rates.** This has been in response to inflation persisting at elevated levels in contrast to marked falls in headline inflation rates elsewhere. Headline CPI remained at 8.7% in the UK in May, when it had been anticipated to fall. By comparison, inflation has fallen to 4% in the US and 5.5% in the Eurozone. Meanwhile, core UK CPI inflation unexpectedly rose to 7.1% in May. As a result, there has been a marked firming in UK rate expectations over the course of the last few months.
- However, the reaction of sterling to the most recent Bank of England meeting and policy announcement in June is noteworthy.** At this meeting, the BoE provided a hawkish surprise hiking by 50bps rather than by 25bps as had been expected. Yet, sterling did not register any gains following the more aggressive rate increase, or indeed, from the most recent marked firming in UK rate expectations. UK rates are now expected to peak at 6.5% early next year, compared to 5.5% in the run up to the June BoE meeting. In contrast, Eurozone rates are seen topping out around 4%, while the market envisages the Fed funds rate reaching a high of 5.50%. Historically, rate increases are a positive for a currency, when they coincide with on-going economic growth. However, continued rate increases amid a stagnant or contracting economy, dealing with elevated levels of inflation tends to play out negatively for a currency. Its appears to be the case that stagflation risks are now hindering any further momentum for sterling from additional rate hikes. At the same time, positioning data shows that the market is 'stretched' long the currency. Therefore, sterling could struggle to make further gains during the second half of this year. Indeed, the 83-84p band has been the floor for EUR/GBP since the Brexit referendum in June 2016.
- This week, a busy UK macro schedule includes the latest monthly labour market and GDP data.** Conditions in the UK labour market remain very tight, and are placing upward pressure on average earnings. The unemployment rate has been edging slightly higher but it was still at a very low level of 3.8% in April. Meantime, average earnings growth excluding bonuses rose for the tenth month in twelve, to 7.2% y/y in April, from 6.8% previously. The unemployment rate is forecast to remain unchanged, at 3.8% in May, while wage growth is projected to soften marginally to +7.1% y/y. A word of warning though, earnings growth has printed ahead of expectations in fourteen of the past sixteen months. In terms of GDP, as mentioned above, the economy has essentially flat-lined since Q2 2022. The most recent monthly data show GDP rebounded by 0.2% in April, having contracted by 0.3% in March. A sharp 0.4% m/m decline is pencilled in for May, as the month included an additional bank holiday for the coronation of King Charles.
- In the US, the main release of note will be CPI inflation for June.** The headline CPI rate declined for the eleventh consecutive month in May, to 4%, its lowest level since March 2021, and down from a peak of 9.1% last June. Core inflation though, is proving to be much stickier. It fell to 5.7% last December, having peaked at 6.6% in September, but remained in a 5.5-5.6% range in early 2023, before falling to 5.3% in May. Furthermore, monthly core-CPI readings maintain strong momentum, rising by 0.4-0.5% since December. The consensus is for another steep decline in headline inflation, to 3.1% in June, with the core rate easing to 5.0% also. Meanwhile, PPI inflation, which has been moving sharply lower since June of last year, is projected to fall to 0.4% from 1.1%, indicating that pipeline inflationary pressures have softened considerably. Elsewhere, the NFIB survey of small businesses will be of interest, as investors try to ascertain the impact of difficulties in parts of the regional banking system on the sector. The Michigan measure of consumer sentiment is expected to register a slight improvement in July, albeit from a weak level.
- Meantime, the latest ECB monetary policy meeting account will garner close attention, as will the final readings of German, French and Italian inflation for June.** Industrial production is forecast to rise by 0.5% in May, having expanded by 1% in April.



	Interest Rate Forecasts			
	Current	End Q3	End Q4	End Q1
		2023	2023	2024
Fed Funds	5.125	5.375	5.375	5.375
ECB Deposit	3.50	4.00	4.00	4.00
BoE Repo	5.00	5.50	5.75	5.75
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 Q3	End Q4	End Q1
		2023	2023	2024
EUR/USD	1.0945	1.10	1.12	1.13
EUR/GBP	0.8533	0.86	0.87	0.87
EUR/JPY	155.63	159	162	160
GBP/USD	1.2824	1.28	1.29	1.30
USD/JPY	142.21	145	145	142

Current Rates Reuters, Forecasts AIB's ERU

Date	UK & Irish Time	Release	Previous	Forecast
This Week:	ECB Speakers:	Lane (Wed)		
	BoE Speakers:	Bailey (Wed)		
	Fed Speakers:	Barr, Daly, Mester, Bostic (Mon); Bullard (TuE); Kashkari, Bostic, Mester, Barkin (Wed); Waller (Thu)		
Mon 10th	CHINA:	02:30 CPI Inflation (June)	-0.2% (+0.2%)	+0.0% (+0.2%)
	CHINA:	02:30 PPI Inflation (June)	(-4.6%)	(-5.0%)
	JPN:	06:00 Economy Watchers Poll (June)	55.0	
	EU-20:	09:30 EU Sentix Index (July)	-17.0	-18.0
Tue 11th	GER:	07:00 Final HICP (June)	+0.4% (+6.8%)	+0.4% (+6.8%)
	UK:	07:00 ILO Unemployment Rate (May)	3.8%	3.8%
	UK:	07:00 Employment Change (May)	+250,000	+158,000
	UK:	07:00 Claimant Count (June)	+23,000	
	UK:	07:00 Average Earnings (May)	(+6.5%)	(+6.8%)
		- Ex-Bonus	(+7.2%)	(+7.1%)
	ITA:	09:00 Industrial Output (May)	-1.9% (-7.2%)	+0.8% (-4.5%)
	GER:	10:00 ZEW Economic Sentiment (July)	-8.5	-10.0
	US:	11:00 NFIB Small Business Optimism (June)	89.4	
Wed 12th	SPA:	08:00 Final HICP (June)	+0.6% (+1.6%)	+0.6% (+1.6%)
	US:	13:30 CPI Inflation (June)	+0.1% (+4.0%)	+0.3% (+3.1%)
		- Core-CPI	+0.4% (+5.3%)	+0.3% (+5.0%)
Thu 13th	UK:	07:00 GDP (May)	+0.2% (+0.6%)	-0.4%
		- 3m/3m	+0.1%	-0.1%
	UK:	07:00 Industrial Output (April)	-0.3% (-1.9%)	-0.4% (-2.3%)
		- Manufacturing Output	-0.3% (-0.9%)	-0.5% (-1.7%)
	UK:	07:00 Goods Trade Balance (April)	-£15.0bn	
		- Non-EU	-£5.0bn	
	FRA:	07:45 Final HICP (June)	+0.2% (+5.3%)	+0.2% (+5.3%)
	EU-20:	10:00 Industrial Production (May)	+1.0% (+0.2%)	+0.5% (-1.1%)
	EU-20:	10:00 ECB Policy Meeting Account (14-15th June)	+1.0% (+0.2%)	+0.3% (-1.1%)
	IRL:	11:00 CPI Inflation (June)	+0.3% (+6.6%)	+0.8% (+6.0%)
		- HICP Inflation	Flash: +0.8% (+4.8%)	+0.8% (+4.8%)
	US:	13:30 Initial Jobless Claims (w/e 3rd July)	+248,000	
	US:	13:30 PPI Final Demand (June)	-0.3% (+1.1%)	+0.2% (+0.4%)
		- Ex-Food & Energy	+0.2% (+2.8%)	+0.2% (+2.6%)
Fri 14th	EU-20:	10:00 Total Trade (May)	-€7.1bn	
		- EuroStat Trade	-€11.7bn	
	IRL:	11:00 Annual National Accounts (2022)		
		- GDP	First Estimate: +12.0%	+12.0%
	IRL:	11:00 National Accounts (Q1 2023)		
		- GDP	First Estimate: -4.6%	-4.6%
	US:	15:00 Prelim. Uni Michigan Consumer Sentiment (July)	64.4	65.5

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