

Market Commentary

Key Themes Driving Currency Markets

G10 Currency Moves:



Appreciated as US inflation printed above consensus again, challenging Powell's 'seasonality' view and pushing back the markets expected rate cuts this year



Depreciated given a lack of forward guidance from the Bank of Japan over the rate outlook leading to wider rate differentials



Depreciated on the back of another below consensus inflation print and some weakening growth indicators which will keep the SNB wary



Appreciated given a higher-than-expected inflation print, continually tight labor market, and some improvement in China



Appreciated on the back of RBNZ remaining comfortable with the current level of restrictiveness, and some slight uptick in activity data



Appreciated on the back of stronger GDP growth and PMI's signalling a recovery in household consumption, despite the disinflationary trend remains broadly in-tact



Appreciated following a slightly above consensus inflation print and wages, despite some reassurance from policymakers on the disinflationary outlook



Appreciated as a reaccelerating inflation print partially offset some weaker labor market data and more dovish remarks in the central bank decision statement



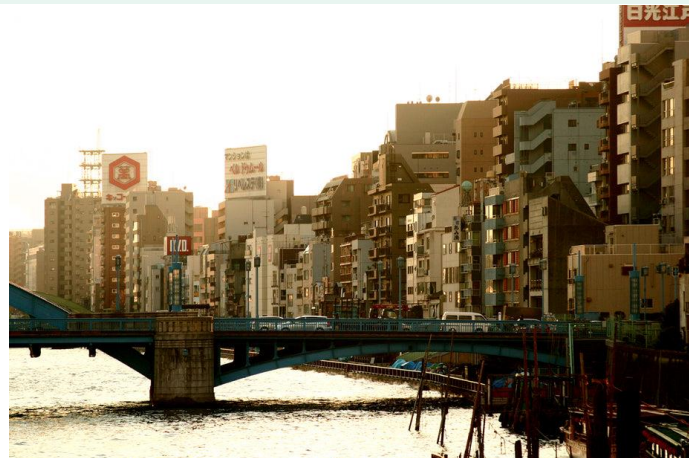
Depreciated following far below consensus inflation and GDP data increasing likelihood of a May rate cut in line with previous communication

Appreciation/depreciation is average against G10 universe

Central Banks: Divergence from the outperforming US?

Overall, G10 central banks have broadly maintained their narrative that underlying inflation trends and economic data are performing in line with expectations, with disinflation continuing and job market tightness unwinding which are feeding into softer growth statistics. However, the US continues to be an economic outperformer, with inflation reaccelerating and labor market strength continuing from demand side pressures, forcing the markets to scale back expectations for rate cuts this year by the Fed.

US inflation printed above-expectations again this year at 3.8% YoY versus 3.7% consensus, signalling an additional break in the disinflationary trend after Chairman Powell had previously defended the previous two surprises as a possible seasonality effect. This was also reinforced by core PCE, the Fed's preferred measure of inflation, which printed 2.8% YoY versus 2.6% expected. The market has pertained these readings to a possibly more structural underlying inflation problem in the US, as the labor market remains buoyant and consumer spending continues to fuel demand-led price increases. This has been reinforced by further labor market releases, where March NFP printed 303K versus 200K consensus and the unemployment rate fell to 3.8% from 3.9%. Powell has subsequently acknowledged that continued US outperformance means that inflation will likely take 'longer than expected' to return to the 2% target, causing a strong upward repricing for Fed policy rates and divergence from other G10 central banks (Figure 1).



The **Bank of Japan** kept the upper bound of the overnight interest rate between 0.0-0.1% and stated that they will continue to buy JGB's 'in line with the March decision' at c. JPY6trn per month. The quarterly outlook report signalled an upward revision to its core inflation outlook for FY 2024 and FY 2025 to 2.8% and 1.9% respectively, with larger upside risks for inflation this year. Governor Ueda signalled that the weak yen was a factor pushing up these inflation risks, though this would typically occur with a time lag and was not a 'major factor' for the inflation trend now. These inflation forecasts potentially signal some further conviction towards tighter monetary policy this year, but the market remained disappointed by the lack of guidance offered as well as no signal for a reduction in JGB purchases. The yen briefly hit 160 versus the dollar towards the end of the month, although later sharply fell below 154 with markets heavily expecting that this was the result of interventions by the Ministry of Finance.

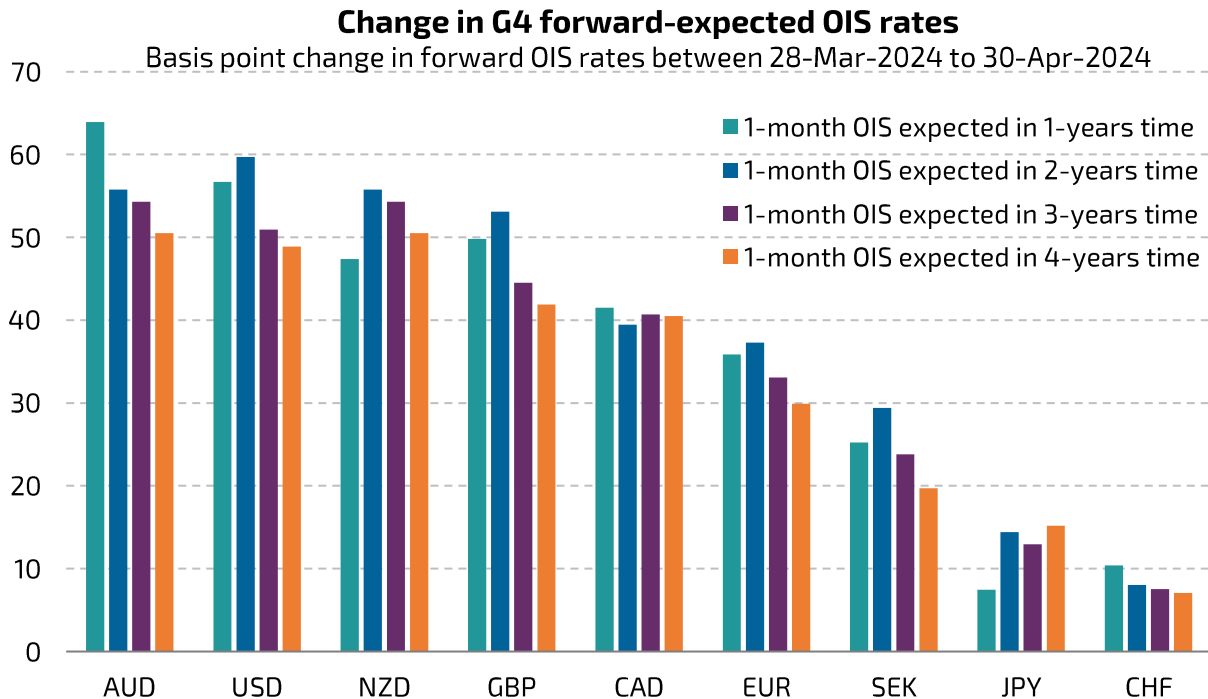


Figure 1: Record, Bloomberg. Data as of April 30th, 2024.

UK inflation eased but slightly above consensus at 3.2% YoY versus 3.1% consensus, with most of the slower disinflation from accommodation and rents. In addition, 3-month average earnings came in at 5.6% YoY versus 5.5% consensus, demonstrating a potentially more difficult challenge for the Bank of England on tackling prices in core services than elsewhere in Europe. However, Bank of England policymakers such as Bailey have continued to state that unlike US inflation dynamics with continued demand-side pressures, the UK is seeing 'strong evidence' of price pressures retreating and a more extensive unwind of supply shocks. In addition, there are signs of underlying economic vulnerabilities such as unemployment rising to 4.2%, falling headline employment measures and Bank of England survey of CFO's signalling lower actual and expected wage settlements.

The **ECB** kept interest rates unchanged on the back of data performing as expected, with lower goods prices driving inflation lower but all measures broadly easing helped by moderating wages. Lagarde continued to signal a data dependent path but gave increased signalling that by June they would likely have enough data to implement the first rate cut if trends continue as expected. Disinflation has not seen the same breaks as it has in the US, with headline inflation printing 2.4% YoY and core at 2.9% for March, undershooting expectations of 2.6% and 3.0% respectively. In addition, wage statistics suggest wage pressures are cooling and will likely be at levels consistent with 2% inflation by June or July 2024. The core inflation reading for April was slightly above expected at 2.7% versus 2.6% consensus however, with domestic demand remaining an upside risk. Q1 GDP growth reinforced this at 0.3% QoQ versus 0.1% consensus on the back of strong household consumption.

Switzerland's inflation rate printed below consensus again at 1.0% YoY versus 1.3% consensus, driven by continued deflation in imported goods as well as broad-based declines in other components. Retail sales and manufacturing PMI's continue to signal ongoing

growth risks which the Governing Board had signalled as reasons for implementing their surprise rate cut the preceding month as well. Given lack of any further communication, the SNB FX intervention proxy continued to signal a neutral stance on currency valuation with limited intervention to strengthen nor weaken the franc.

Australia's inflation printed 3.6% versus 3.4% consensus for Q1 which will maintain pressure on the RBA to keep rates at higher levels for longer. Although some of the previous labor market strength marginally eased with employment change printing -6.6K versus +7.2K consensus, the unemployment rate only ticked up to 3.8% versus 3.9% expected which is keeping the labor market tight. Potential optimism over China developments and waning risk-off sentiment are also providing support for the antipodean.

The **Bank of Canada** kept interest rates on hold at 5.0%, but there were dovish tones in the statements such as 'a broad range of indicators suggest that labor market conditions continue to ease'. This has been supported by a rise in the unemployment rate to 6.1% versus 5.9% expected, and employment change printing well below consensus at -2.2K versus 25K expected. Excess supply in the economy means that the Bank expect headline CPI to move below 2.5% YoY in second half of 2024. However, inflation partially reaccelerated to 2.9% YoY in March which contributed to an upward repricing on rate expectations.

Sweden's inflation printed below consensus at 4.1% versus 4.4% consensus, bolstering market conviction for a rate cut in May which now has more than a 50% probability priced in. This follows on from substantial tweaks to the Riksbank forward guidance which were significantly more dovish on the back of a weaker jobs market and unravelling growth risks for the economy. In addition, the monetary policy statement had cited the currency weakness as one of the major upside risks to inflation. Underlying economic weaknesses from current rate levels were also demonstrated further by Q1 GDP data printing -1.1% YoY versus -0.2% expected.

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Germany

Bockenheimer Anlage 46
60322 Frankfurt am Main
Germany

+49 211 5403 9587

United Kingdom

Morgan House, Madeira Walk
Windsor, Berkshire, SL4 1EP
The Smiths Building, The Office Group,
179 Great Portland Street, London,
W1W 5PL

+44 (0) 1753 852 222

Switzerland

Münsterhof 14
8001 Zürich

+41 43 508 5947