FX Daily: No good news for the pound

UK retail sales were dismal but the pound is being driven more by uncertainty about UK-EU trade negotiations and speculation about negative interest rates, which the market is now pricing in for later this year

USD: Concerns about US-China relations fully back in focus

Risk sentiment has taken a hit from China's decision to impose national security legislation on Hong Kong, in turn increasing the risk of renewed protests and a further escalation of already heightened tensions with the US. The roughly 5% fall in the Hang Seng equity index overnight has already spilled over into Europe and US futures. One key consequence of the market concern about US-China relations is the drop in oil prices. So far this week, the rebound in oil prices has helped the recovery of previously battered commodity currencies, with the commodities-exposed LatAm FX segment doing particularly well (the Mexican peso reached its strongest level since mid-March). Our commodity team already considered the rally in Brent oil prices to around US$35/bbl as exaggerated and not reflecting the short-term supply and demand dynamics. With oil price gains now stalling, so should the recent recovery in the broader emerging markets FX complex.

EUR: ECB minutes no game changer for the euro

The European Central Bank's minutes of its April meeting should have a limited impact on the euro today as the meeting took place prior to the surprising German constitutional court decision (challenging the legality of the ECB's purchases) while a top-up of the Pandemic Emergency Purchase Programme at the June ECB meeting is now expected. With the eurozone risk premium contained, EUR/USD it to settle around / above 1.09 today.

GBP: The ongoing lack of good news

As expected, UK March retail sales showed a sharp drop today, underscoring the damage from the Covid-19 crisis. Still, in terms of the impact on GBP, the UK data should play second fiddle to (a) uncertainty about UK-EU trade negotiations; and (b) speculation about negative Bank of England interest rates. On the latter, the market is now pricing for interest rates to fall below zero by November this year. With the prospects of negative rates fully on the market's radar and in part priced in by the end of this year and for 2021, the next main hurdle for GBP should be the negative newsflow on trade negotiations and likely end to the UK-EU transition period this year. This should send EUR/GBP to 0.91 in June.

NOK: Weighed down by oil, for now

The fall in the oil price weighed on the Norwegian krone overnight, making it the worst performing European currency (even underperforming the rouble). Still, with the fall in Brent oil prices seen as a correction rather than the start of a new trend, the Norges Bank being done with its easing cycle (the central bank downplayed its preference for either negative rates or quantitative easing) and the NB purchasing NOK (from liquidation of oil fund assets denominated in foreign currencies) to fund the rising domestic fiscal deficit, this points to a constructive NOK outlook for the second half of the year. As for today, EUR/NOK should stay around the 11.00 level.

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