

Any bounce in sterling to be temporary

A better than expected uptick in UK wage growth should not be interpreted as a trend.



Source: iStockphoto

Temporary relief

While GBP is finding some relief after a slightly better than expected jobs report, we expect this to be temporary as any knock-on effects for Bank of England policy are minimal. The small positive surprise in wage growth should not be interpreted as a trend, rather a small deviation around the 2% average growth rate for 2017. Counterintuitively, the ongoing strength in job gains is a dovish development - at least in the near-term - as it contradicts the BoE's assumption that the labour market is close to full capacity. A greater degree of slack and possible downside risks to the 4.5% NAIRU estimate is another reason to retain a cautious policy approach.

Our forecasts

We continue to see EUR/GBP trading in the 0.90-0.92 range in the near-term and believe a move to parity remains a long-shot at this stage. Greater risks of a dovish ECB tapering, to avoid any excessive tightening of financial conditions, coupled with diminishing (or postponed) cliff-edge Brexit tail risks may keep this EUR/GBP trend higher contained. For GBP/USD, short-term UK-US rate differentials will remain the key driver and with markets having now adjusted to a "wait-and-see" BoE policy approach, we expect any widening or narrowing in UK-US rate differentials to be a function of US data and Fed policy expectations. Our view of a recovery in US data should weigh on GBP/USD in the near-term towards 1.26-1.27.

Author

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com