

FX Viewpoint

Currencies
Global

GBP under pressure ahead of UK budget

- ◆ GBP was largely unchanged after Burnham's speech, which outlined a broad long-term vision for the economy
- ◆ GBP-USD remains pressured by stronger US data and narrowing UK-US rate differentials
- ◆ We believe the USD will strengthen gradually versus the GBP unless the Budget surprises positively

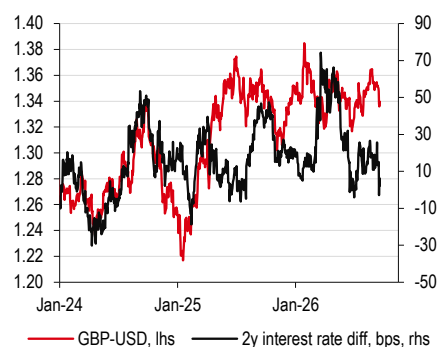
GBP was largely unmoved against both the USD and EUR by UK Prime Minister Andy Burnham's keynote speech to the Labour Party conference on 29 September. The speech set out a **broad long-term vision for the economy**, including greater regional devolution and energy market reform, but provided little detail on either the economic growth or fiscal strategy ahead of the Budget on 28 October.

The lack of an immediate market reaction is telling. **Investors appear more focused on the forces currently driving GBP-USD** such as resilient US economic data, a more hawkish FOMC, and the narrowing support provided by UK-US interest-rate differentials. GBP-USD has fallen this month to its lowest level since June, with the US side of the equation doing much of the work.

GBP was largely unchanged after Burnham's keynote speech

Cyclical forces continue to drive GBP-USD

1. GBP-USD rich versus rate differentials



2. Rising gilt yields heighten fiscal policy uncertainty ahead of budget



The UK backdrop remains less supportive, with HSBC Economics expecting growth to slow and a cautious Bank of England ahead of its 5 November meeting. Recent speeches by more dovish Monetary Policy Committee members indicate a rate hike is increasingly likely. Markets are pricing around 21bp of tightening for November but that is heavily dependent on energy markets and the Middle East.

For GBP-USD to find greater domestic support, **the budget will need to provide a positive surprise**. Burnham's proposals may eventually support GBP if they improve productivity, unlock regional investment and raise the UK's growth potential.

Until the government clarifies how it will manage public debt while encouraging private sector expansion, **GBP-USD is likely to remain governed by cyclical factors**. The 28 October Budget may reveal more details but US data, Federal Reserve policy and energy prices, are likely to set the tone for GBP-USD. We expect the **USD to strengthen gradually against the GBP** in the near term.

The UK outlook remains relatively weak versus the US

GBP could get a boost if the Budget surprises positively

We expect the USD to grind higher against GBP

Disclosure appendix

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