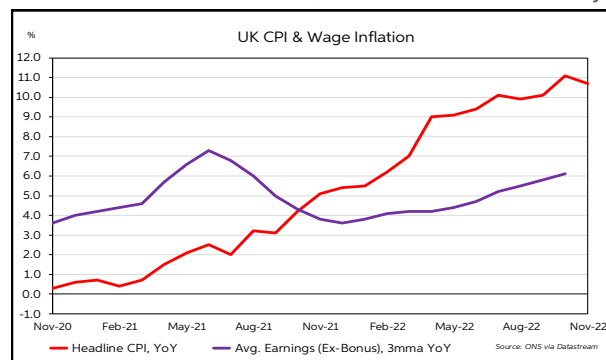


Dollar Losing Some Sparkle

- **Having been very much to the fore for the first three quarters of last year, the dollar lost some ground in the final months of 2022.** A perfect storm of rising US interest rates and Treasury bond yields, and a surge in commodity prices drove the greenback higher. However, the currency gave up some of these gains as other central banks stepped up the pace of tightening in Q4, with 75bps rate hikes becoming the norm. The US has also been one of the first of the main economies to exhibit an easing of inflationary pressures, tempering the extent of further rate hike expectations from the Fed.
- **This reversal of fortunes was initially reflected in EUR/USD moving back up towards parity, having fallen to a low of \$0.95 in late September.** The pair then rose up into the \$1.05-1.06 band over the final two months of 2022. In the early stages of this year, the dollar has continued to soften, with EUR/USD maintaining its upward trajectory, trading up to the \$1.08 threshold. Meanwhile, GBP/USD has rebounded from a low of \$1.04, moving above \$1.20. The dollar has also fallen back sharply against the yen, with the USD/JPY pair going from a high, north of ¥150, to down below ¥129.
- **The coming year seems likely to be characterized by further rate hikes in the opening half of 2023, with monetary policy being put on hold thereafter.** Key central banks have been indicating that a restrictive rate stance will be required for a period of time to squeeze inflationary pressures out of the system. US rates seem set to rise to around 5%, and remain there into 2024, which would be well above rate levels in most other countries. This should be supportive of the dollar.
- **From a euro viewpoint, the ECB has turned quite hawkish and moved to an aggressive rate tightening path.** The ECB's on-going rate hiking cycle should continue to provide a positive dynamic for the currency in the short-term. Thus, the single currency may experience some further upside versus the greenback throughout Q1. However, the war in Ukraine is likely to remain a key risk for the euro, while the economy is in danger of slipping into recession. Given the challenging macro economic conditions that are likely to prevail this year, as well as the on-going concerns about the security of EU energy supplies, and the continuing war in Ukraine, the euro may struggle to make further significant gains against the dollar in the months ahead.
- **Interest rates have been as key driver of currencies in the past number of years.** Thus, if US rate cuts look like coming on to the agenda in 2024, then the dollar could start to lose some ground later on this year. It is important to remember the currency is still at a very elevated level, and therefore has the potential to fall back if US rates move down. Of course, the outlook for monetary policy will very much depend on how inflation evolves.
- **In this regard, UK CPI inflation data due this week will be in focus.** Inflation fell by more than expected in November, to 10.7% y/y, while the core rate eased to 6.3% y/y, down from 11.1% y/y and 6.5% y/y, respectively. The headline rate is projected to inch lower to 10.6% y/y in December, largely due to a fall in fuel costs and a modest softening in food prices. However, the risk to this forecast are to the downside. The core reading is expected to be unchanged at 6.3% y/y. UK rate hike expectations have softened by circa 10bps recently, and may decline further as UK CPI falls back. **It should be noted though, that labour market conditions remain very tight.** Although, the unemployment rate has edged slightly higher in recent months, it remained 0.3 percentage points below its pre-COVID level, at 3.7%, in October. Furthermore, tight conditions in the labour market are placing upward pressure on wages, which were 6.1% y/y higher in October. The forecasts for UK labour market data due this week, are for the jobless rate to be unchanged at 3.7% in November, while an increase in average earnings excluding bonuses to +6.3 y/y is pencilled in.
- **Overall though, the rapid rise in prices in 2022 has squeezed real incomes and weighed on spending, as evidenced by retail sales data.** In volume terms, retail sales have fallen in eight of the past ten months. However, the consensus is for sales to rise by 0.4%, in December, leaving them 4.4% lower in year-on-year terms. Meantime, consumer sentiment is expected to improve again in January, to -40 from -42. However, this is still a very subdued reading, near the all-time low of -49.
- **Retail sales data will also feature in the US this week.** In November, US retail sales fell sharply by 0.6%, while the “control group”, a key measure of core sales, declined by a more modest 0.2%. The downward trend is set to continue in December, with the former falling by 0.8%, and the latter by 0.2%. Similarly, industrial production, which also contracted in November, is anticipated to edge 0.1% lower in December. Meanwhile, a slew of housing market metrics, including, housing starts, existing home sales (Nov) and homebuilder sentiment (Dec) will provide an update on the residential sector.
- **In the Eurozone, the latest ECB monetary policy meeting account will be of interest.** Elsewhere, the Bank of Japan meeting this week will be in focus, given the BoJ surprised the market by widening its yield curve control range last time out.



	Interest Rate Forecasts			
	Current	End Q1	End Q2	End Q3
	2023	2023	2023	2023
Fed Funds	4.375	5.125	5.125	5.125
ECB Deposit	2.00	3.00	3.50	3.50
BoE Repo	3.50	4.25	4.25	4.25
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 Q1	End Q2	End Q3
	2023	2023	2023	2023
EUR/USD	1.0817	1.07	1.08	1.10
EUR/GBP	0.8867	0.88	0.89	0.90
EUR/JPY	138.26	141	140	140
GBP/USD	1.2199	1.22	1.21	1.22
USD/JPY	127.80	132	130	127

Current Rates Reuters, Forecasts AIB's ERU

Date	UK & Irish Time		Release	Previous	Forecast
This Week:	ECB Speakers:	deGuindos (Tue); Lagarde , Schnabel (Thu); Lagarde (Fri)			
	BoE Speakers:	Bailey (Mon)			
	Fed Speakers:	Williams, George (Tue); Bostic, Logan, Harker (Wed); Collins, Brainard, Williams (Thu); Harker, Waller (Fri)			
	World Economic Forum (Mon 16th - Fri 20th January)				
Mon 16th					
Tue 17th	CHINA:	02:00	GDP (Q4)	+3.9% (+3.9%)	-0.8% (+1.8%)
	CHINA:	02:00	Retail Sales (December)	(-5.9%)	(-7.8%)
	CHINA:	02:00	Industrial Output (December)	(+2.2%)	(+0.5%)
	CHINA:	02:00	Unemployment Rate (December)	5.7%	
	GER:	07:00	Final HICP (December)	-1.2% (+9.6%)	-1.2% (+9.6%)
	UK:	07:00	Claimant Count (December)	+30,500	
	UK:	07:00	Unemployment Rate (November)	3.7%	3.7%
	UK:	07:00	Average Earnings (November)	(+6.1%)	(+6.1%)
			- Ex-Bonus	(+6.1%)	(+6.3%)
	UK:	07:00	Employment Change (October)	+27,000	+10,000
	GER:	10:00	ZEW Economic Sentiment (January)	-23.3	-15.0
	IRL:	11:00	CPI Inflation (December)	+0.3% (+8.9%)	-0.2% (+8.2%)
	US:	13:30	NY Fed Manufacturing (January)	-11.2	-8.7
	JPN:	23:50	Machinery Orders (November)	+5.4% (+0.4%)	-0.9% (+2.4%)
Wed 18th	JPN:		BoJ Rate Decision	-0.10%	-0.10%
	UK:	07:00	CPI (December)	+0.4% (+10.7%)	+0.4% (+10.6%)
			- Core	+0.3% (+6.3%)	+0.4% (+6.3%)
	EU-19:	11:00	Final HICP (December)	-0.3% (+9.2%)	-0.3% (+9.2%)
			- Ex-Food & Energy	+0.7% (+6.9%)	+0.7% (+6.9%)
	IRL:	11:00	Residential Property Prices (November)	+0.4% (+9.8%)	+0.2% (+8.7%)
	US:	13:30	PPI Final Demand (December)	+0.3% (+7.4%)	-0.1% (+6.8%)
			- Ex-Food & Energy	+0.4% (+6.2%)	+0.1% (+5.8%)
	US:	14:15	Retail Sales (December)	-0.6% (+6.5%)	-0.8% (+7.8%)
			- Ex-Autos	-0.2%	
			- Control	-0.2%	-0.2%
	US:	14:15	Industrial Production (December)	-0.2% (+2.5%)	-0.1% (+2.6%)
			- Manufacturing	-0.6%	-0.2%
			- Capacity Utilisation	79.7%	79.6%
US:	15:00	NAHB HomeBuilder Sentiment (January)	31	31	
Thu 19th	EU-19:	12:00	ECB Monetary Policy Account (14-15th Dec)		
	US:	13:30	Housing Starts (December)	+1.43m / -0.5%	+1.36m / -4.8%
			- Building Permits	+1.35m / -10.6%	+1.37m / +1.4%
	US:	13:30	Initial Jobless Claims (w/e 9th January)	+205,000	+214,000
	US:	13:30	Philly Fed Index (January)	-13.8	-11.0
	JPN:	23:30	CPI (December)	(+3.8%)	(+4.0%)
		- Core	(+3.7%)	(+4.0%)	
Fri 20th	UK:	00:01	Gfk Consumer Confidence (January)	-42	-40
	GER:	07:00	Producer Prices (December)	-3.9% (+28.2%)	-1.2% (+20.8%)
	UK:	07:00	Retail Sales (December)	-0.4% (-5.9%)	+0.4% (-4.2%)
			- Ex-Fuel	-0.3% (-5.9%)	+0.4% (-4.4%)
	US:	15:00	Existing Home Sales (December)	+4.09m s.a.a.r.	+3.96m s.a.a.r.

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

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