FX Monthly Report-GBP

April 2025

FX Monthly Report

Published by:
Sucden Financial Limited
10 April 2025

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GBP Focus

President Trump's latest trade announcement and subsequent pause jolted currency markets, but the pound's reaction diverged from conventional expectations. Despite the UK initially facing lower tariffs than the EU, sterling weakened against the euro in early April—even as it gained ground against the dollar and a broader currency basket. This asymmetric move was primarily driven by a sharp repricing of monetary policy expectations: markets significantly increased the probability of a Bank of England rate cut, while ECB expectations shifted only marginally. The episode underscores how, in currency markets, relative shifts in policy trajectories—not absolute macro fundamentals—often dominate short-term valuation dynamics.

In this month's outlook, we assess how, despite a 90-day pause on most tariffs, the UK's prevailing relative insulation from US tariffs has paradoxically coincided with growing downside pressure on sterling, driven primarily by a sharp repricing of Bank of England rate expectations. We explore how this interacts with the UK's fiscal stance, recent macroeconomic data, and continued trade vulnerabilities—particularly considering changes in US tariffs. With the euro supported by a more measured shift in ECB policy and the EU's cohesive trade response, we ask: what does this divergence mean for the pound in the months ahead?

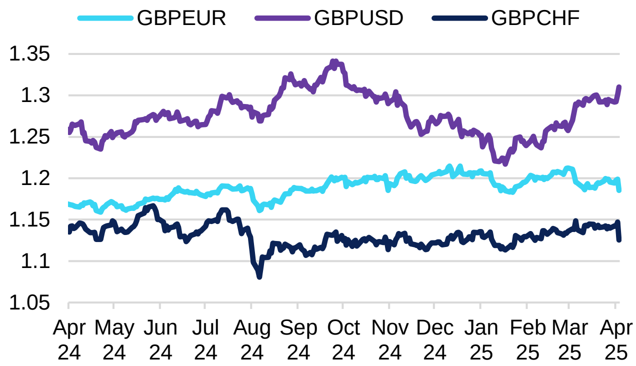
UK Fiscal Policy

In the UK's recent Spring Statement, the government reaffirmed its commitment to fiscal discipline—a stance broadly welcomed by markets and reflected in stable gilt yields. Chancellor Reeves reiterated adherence to strict fiscal rules, unveiling welfare reforms aimed at reducing public spending by approximately £4.8 billion. While this focus on long-term sustainability supports investor confidence in UK assets, the near-term risks to consumer spending and growth may limit upside for GBP, particularly if domestic demand weakens further.

The Treasury projects a steady decline in net borrowing from £105.6 billion in 2025–26 to £70.6 billion by 2029–30, equivalent to a reduction from 4.5% to 2.1% of GDP. This narrative of fiscal responsibility may help anchor sterling in times of volatility, especially as markets continue to prize macro stability in currency valuation. However, any signs of fiscal slippage or political tension around budget execution could reignite pressure on GBP.

Currency Pair Movements

The pound weakened against the euro and franc after the recent tariff announcement.



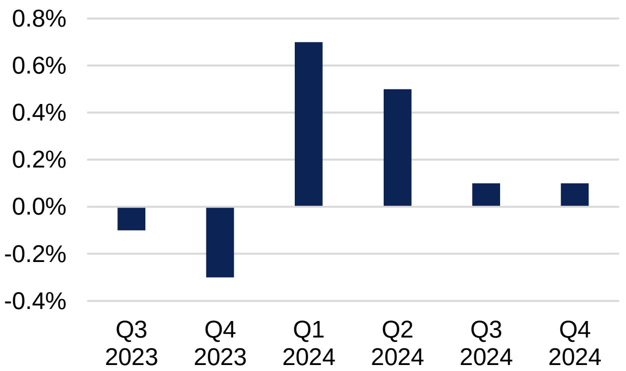
Source: Bloomberg

Domestic Economic Data

Recent macroeconomic data offer tentative support for the pound. UK GDP grew by 0.1% QoQ in Q4 2024, defying expectations of contraction. Inflation eased to 2.8% in February, down from 3.0% in January, with core inflation falling to 3.5%. Services activity, which underpins nearly 80% of UK output, also improved, with the PMI rising to 53.2 in March. While these indicators signal stabilisation, persistent weaknesses in consumer-facing sectors and renewed inflationary risks from tariff-related supply disruptions limit sterling's upside, especially if market sentiment turns risk-off.

UK Annualised Growth QoQ

The UK managed to avoid contraction in Q4 2024.



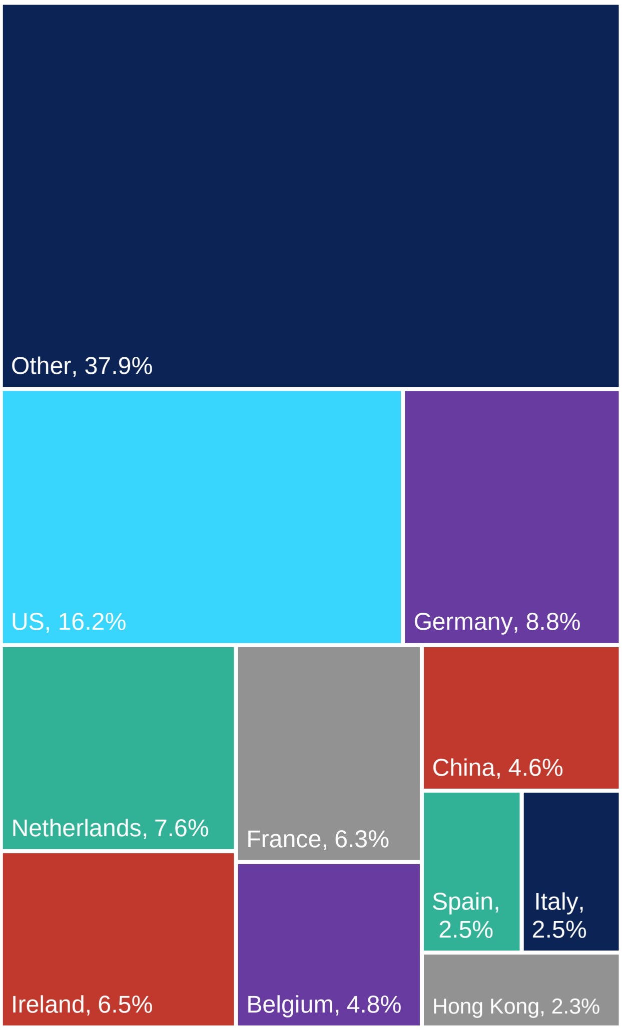
Source: Office for National Statistics

Monetary Policy BoE vs ECB

On the monetary front, the Bank of England held the base rate at 4.5% in March, as policymakers assessed the balance between improving domestic data and rising external risks. Forward swaps now price in a 90% probability of a 25bps rate cut at the 8 May meeting, up from 75% prior to the US tariff announcement. This sharp repricing suggests that the market sees the BoE as more likely to ease than previously thought—a factor that weighs on GBP relative to currencies with more stable central bank trajectories, notably the euro.

In contrast, while the European Central Bank is also expected to cut rates—from 2.5% to 2.25% - market expectations have shifted only marginally, with the probability now just above 70%. This more gradual adjustment reflects confidence in the ECB's guidance and the EU's unified policy response to US tariffs. The narrower policy divergence limits EUR downside and contributes to the pound's underperformance versus the euro, despite the UK's lighter tariff exposure.

Biggest UK Export Markets by %, 2024



Source: Office for National Statistics

Trade Tensions

Initially, currency markets have responded asymmetrically to trade developments. While the UK's smaller tariff burden was seen as a relative advantage, the pound has weakened against the euro. This reflects more aggressive repricing of BoE rate expectations compared to the ECB, and investor discomfort with the UK's fragmented trade strategy post-Brexit. Meanwhile, the euro has gained from the perception of institutional strength and coordinated action—key factors in FX markets when navigating geopolitical uncertainty.

Conversely, the pound has appreciated against the dollar, as Trump's protectionist turn fuelled concerns about the US outlook. Diminishing confidence in the dollar as a safe haven and potential delays in Fed easing have opened space for sterling gains. However, this outperformance is likely to remain fragile, given the UK's own economic sensitivities and policy uncertainties.

President Trump's tariff package adds another layer of complexity for GBP. The UK's exemption from the initial round of tariffs offers relief, but tariffs of 25% on foreign-made cars introduced in April now apply to UK auto exports—undermining one of its key export sectors. The UK exported £8.3 billion in cars to the US over the past year, and the sector's exposure to rising trade barriers is likely to weigh on investor confidence in the pound if retaliatory risks escalate.

Despite the drop of the tariff rate on Europe, the UK's overall trade relationship with the US remains strong and more balanced than that of the EU. In the four quarters to Q3 2024, UK–US bilateral trade totalled £294.1 billion, with a UK surplus of £71.1 billion. In contrast, the EU recorded a goods surplus of €198.2 billion with the US—making it a more visible target for US trade policy. While this may continue to shield the UK from the harshest trade reprisals, the pound remains vulnerable to sector-specific shocks—particularly if tensions escalate or the UK is unable to secure favourable trade terms amid global realignments.

Volatility Analysis

The implied volatility rate for GBP/USD has dropped sharply since the start of this year – from around 11%, when markets began pricing in the potential impact of Trump's return to office, to around 7.0% by March. Even with the tariff announcements, including a broad 10% levy on UK goods, the implied volatility level remains near levels seen in Q4 2024. This steady decline signals that, despite significant activity on the geopolitical and trade front, markets have become less reactive to macroeconomic developments.

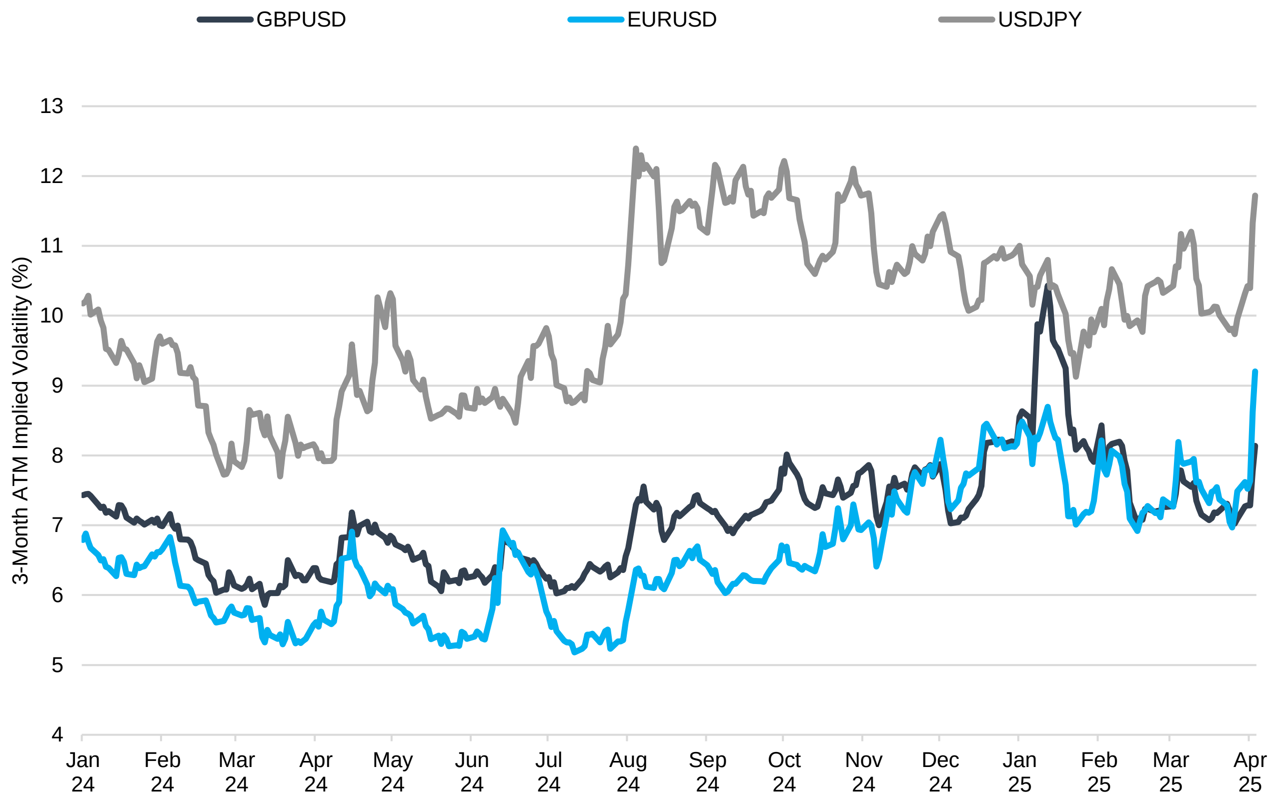
Since February, implied volatility has consistently remained below realised volatility, as markets priced in only modest shifts around the UK budget and other government updates. This indicates that markets did not perceive Sprint Statement changes as having disruptive near-term effects.

Following the recent wave of initial tariff implementation, most FX volatility curves—such as for EUR and JPY—have shown sharp spikes in the near term, followed by a decline further out the curve. The UK, however, remains an exception. While front-end volatility has picked up, the longer end of the curve — covering 2 to 3 years — is also rising. This suggests that while investors absorbed the near-term shocks, they remain worried about the long-term fiscal implications of current government policy and any potential deviations from established spending plans. These risks could weigh on the UK's macroeconomic outlook, feeding through into weaker GBP performance over time.

Forward points currently reflect a moderately bearish near-term view on GBP/USD, with resistance around the 1.30–1.31 zone likely to hold. That said, ongoing domestic challenges in the UK mean the pound could still be hit by sudden bursts of volatility — especially when compared to the euro, where it is starting to look a bit more vulnerable. That said, ongoing domestic challenges in the UK mean the pound could still be hit by sudden bursts of volatility — especially when compared to the euro, where it is starting to look a bit more vulnerable.

3-Month ATM Implied Volatility

As of early April, the implied volatility of GBP/USD is among the lowest in the G10.



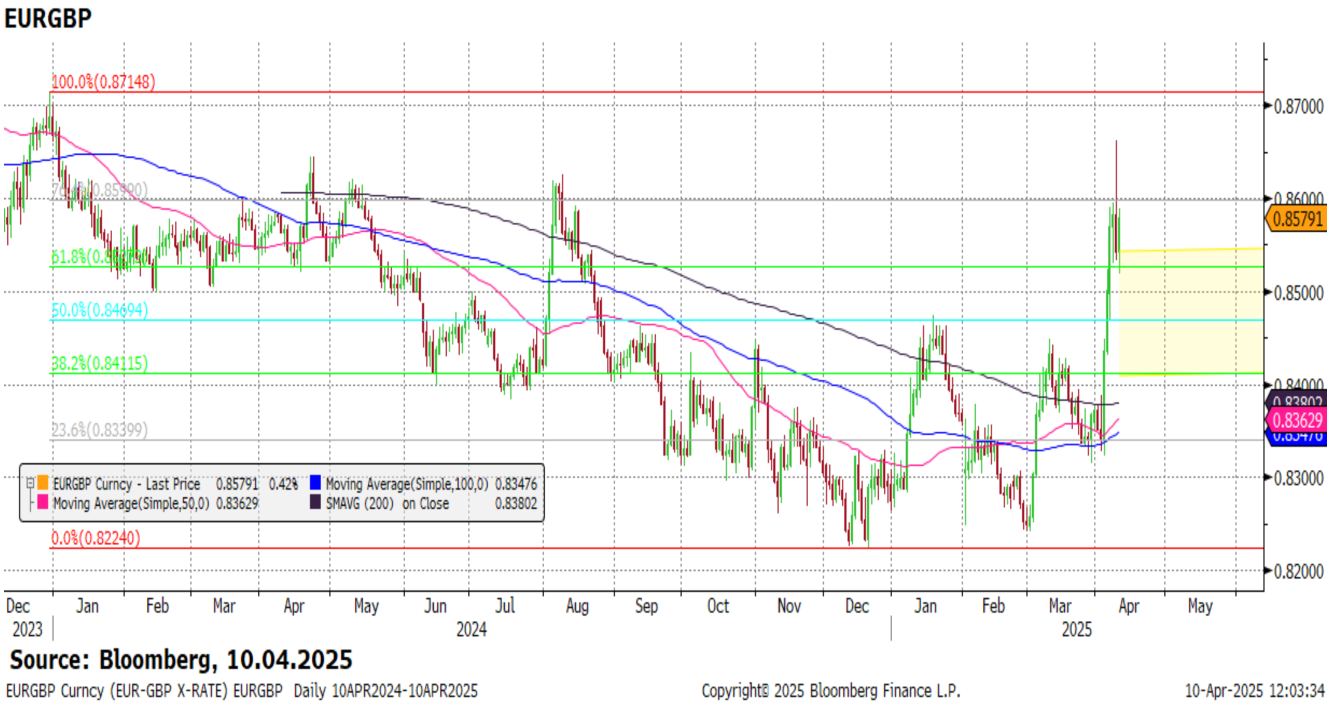
Source: Bloomberg

Our Outlook

The pound finds itself caught between relative macroeconomic resilience and continued external vulnerabilities. While stable public finances and improved data offer support, aggressive rate cut pricing and trade exposure—particularly to US auto tariffs—cloud the outlook. Compared to the euro, policy divergence, political uncertainty, and lack of coordinated trade strategy leave GBP under pressure. Versus the dollar, there is scope for gains in a weak-dollar environment, but this is contingent on global risk appetite and the BoE's tone in May.

Base case:

We expect GBP/EUR to trade range-bound in the near term, anchored around as 0.845 markets digest recent policy shifts and assess the macro implications of the new trade landscape. Relative policy divergence may limit immediate sterling upside, but this should be partially offset by stronger UK–US trade ties and stabilising rate expectations.



Upside scenario for GBP (EUR weakness):

Should UK–US trade negotiations progress favourably, and the BoE adopt a more measured tone than currently priced, GBP could outperform the euro, particularly if the ECB delivers larger-than-expected cut amid deteriorating eurozone growth. In this case, a move back toward 0.83 is plausible, especially if UK data surprise to the upside or political clarity improves.

EURGBP

Source: Bloomberg, 10.04.2025

EURGBP Curncy (EUR-GBP X-RATE) EURGBP Downside Daily 10APR2024-10APR2025 Copyright© 2025 Bloomberg Finance L.P. 10-Apr-2025 11:58:47

Downside scenario for GBP (EUR strength):

If UK trade talks stall or BoE communication turns more dovish than anticipated, GBP could come under renewed pressure, particularly if the ECB tempers its easing stance or eurozone data stabilise. Under this scenario, a drift toward 0.86 is conceivable, though structural eurozone fragilities may cap further gains.

EURGBP

Source: Bloomberg, 10.04.2025

EURGBP Curncy (EUR-GBP X-RATE) EURGBP Upside Daily 10APR2024-10APR2025 Copyright© 2025 Bloomberg Finance L.P. 10-Apr-2025 11:52:47

Desk Comments

GBP

The Spring Statement gave Chancellor Reeves a boost. While the OBR cut near-term growth forecasts, medium-term projections were more optimistic, with potential growth revised higher. Welfare cuts are expected to raise nearly GBP 5bn, restoring some fiscal headroom—though the OBR hasn't factored in trade war risks yet.

The UK's £71.4bn trade surplus with the US in 2023, mostly in services, likely influenced the relatively mild 10% tariff. Though challenging for exporters, it's less severe than tariffs on other nations.

GBP briefly hit 1.3207 after the announcement but has since retraced as the USD gained on safe haven demand and subsequent pause in tariff hike for most economies. Still, GBP remains supported by strong US trade terms, improved services PMI, and a slower expected pace of rate cuts.

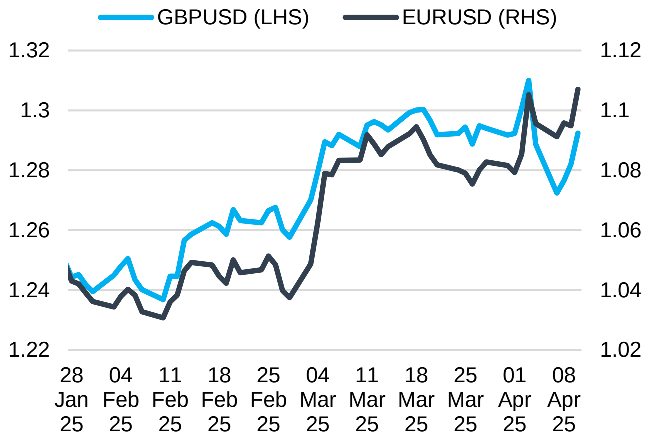
EUR

Initially, Trump's announcement of reciprocal tariffs has cast uncertainty over the eurozone's economic outlook, with consensus pointing to potentially significant negative impacts. Despite this, recent data shows signs of stabilization—composite PMI rose to 50.9 for the third straight month, driven by falling inflation in energy and services.

Market expectations now fully price in a 25 bp ECB rate cut in April, with 2025 rates projected to end at 1.65%.

GBP and EUR vs The Dollar

EUR and GBP continue strengthening against the dollar.



Source: Bloomberg

After initial USD weakness post-announcement, the dollar has rebounded on the news of easing trade tensions, bringing EURUSD back to 1.09. Short-term EURUSD moves still depend on the scale and timing of retaliatory tariffs, while a US recession risk could support EUR in the medium term.

USD

After a brief consolidation, the USD resumed its decline against major currencies, as markets digested the impact of delayed trade policies.

March's stronger-than-expected 228k job gain was offset by recent downward NFP revisions and signs of labour market slowdown, including a rise in unemployment to 4.2%, partly due to stricter immigration enforcement.

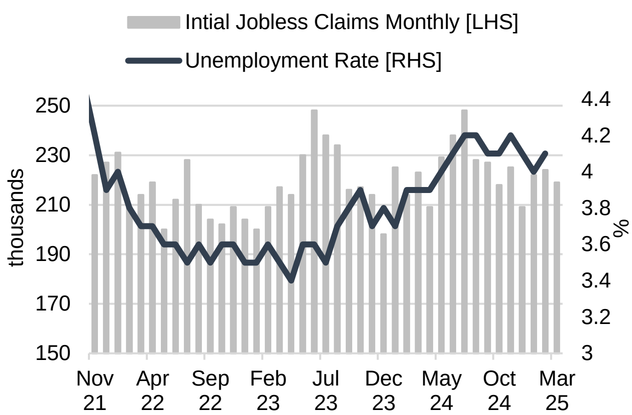
Trump's initial retaliatory tariffs have driven up inflation expectations, with core PCE inflation now forecast to hit 4.7% by end-2025, well above earlier estimates. In response, the Fed downgraded its 2025 GDP growth forecast to 1.7%. Chair Powell called the inflationary impact "transitory" but acknowledged rising recession risks.

Geopolitical tensions have also shifted alliances— most economies are advancing by facing softer tariff rates than previously anticipated, while China faces an even higher rate of 125%.

Markets remain focused on comparative growth, fiscal outlooks, and policy credibility. Although recession concerns weigh on the dollar, safe haven demand offers partial support. Volatility is expected to persist amid ongoing tariff uncertainty.

US Labour Market

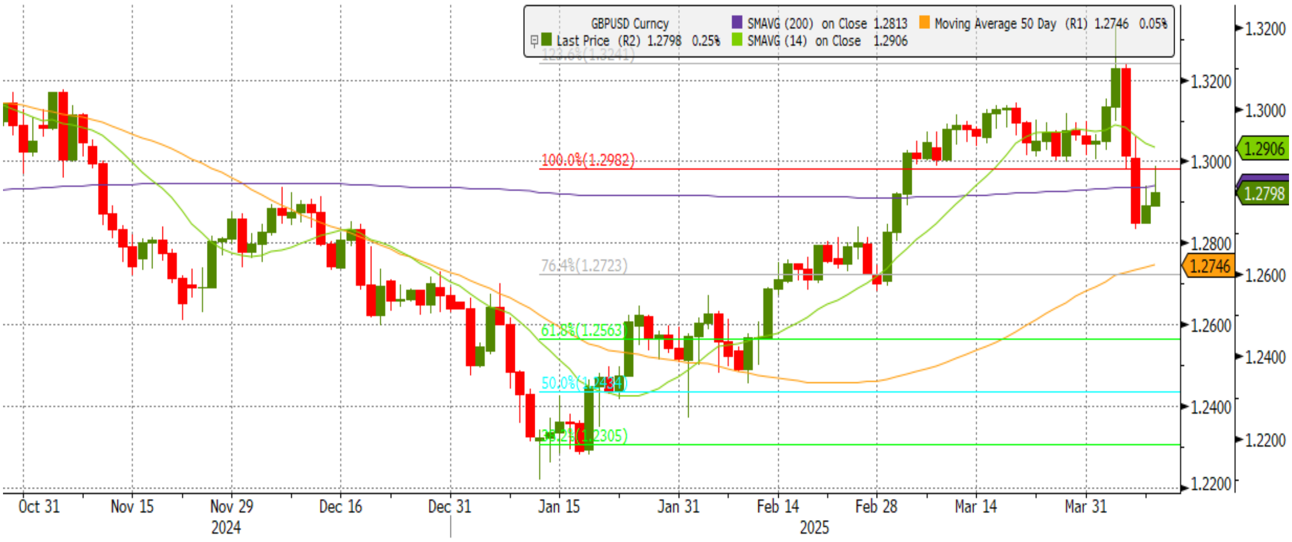
US Labour Market remains resistant.



Source: Bureau of Labor Statistics, Department of Labor

Technical Analysis

EURUSD

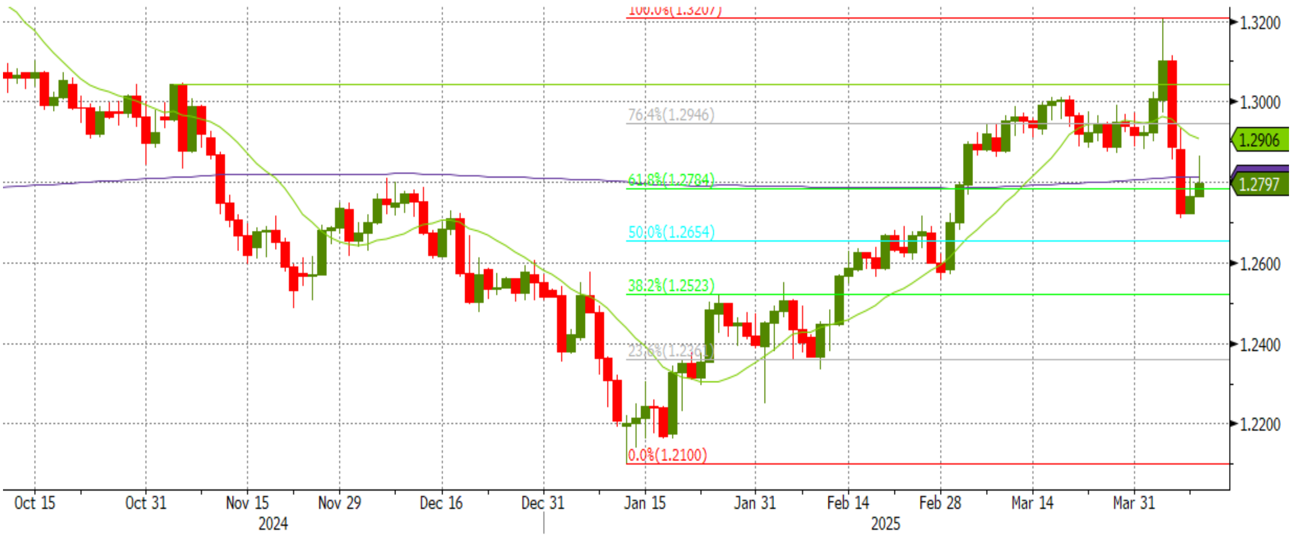


Source: Bloomberg, 09.04.2025

GBPUSD Curncy (GBP-USD X-RATE) EURUSD FX Daily Daily 29OCT2024-09APR2025 Copyright© 2025 Bloomberg Finance L.P. 09-Apr-2025 12:51:00

Following the recent tariffs announcement and subsequent pause, EUR/USD surged to a high of 1.1144, just below the key double top formation resistance at 1.1210. However, heightened market uncertainty drove increased demand for the US dollar as a safe-haven asset, causing bullish momentum in the euro to fade quickly. The next downside target lies at 1.0761, aligning with the 38.2% Fibonacci retracement level, followed by stronger support near the ascending trendline and the 200-day moving average around 1.0670–1.0642. Should these levels hold, the pair would likely complete a cup-and-handle formation—pointing to the potential resumption of the broader bullish trend.

GBPUSD



Source: Bloomberg, 09.04.2025

GBPUSD Curncy (GBP-USD X-RATE) GBPUSD FX Monthly Daily 09OCT2024-09APR2025 Copyright© 2025 Bloomberg Finance L.P. 09-Apr-2025 12:50:38

Market volatility, inflation concerns, aggressive tariff policies, and geopolitical risks have seen GBP/USD trade up to 1.32 before retracing to 1.2700 handle. We are currently at 200 dma support level at 1.2740. Next support comes in the form of 50% fibo at 1.2654. We expect GBP to reverse at these levels and retest the 1.32 high then last year’s high of 1.3435.

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