Sucden Financial

FX Monthly Report

May 2021

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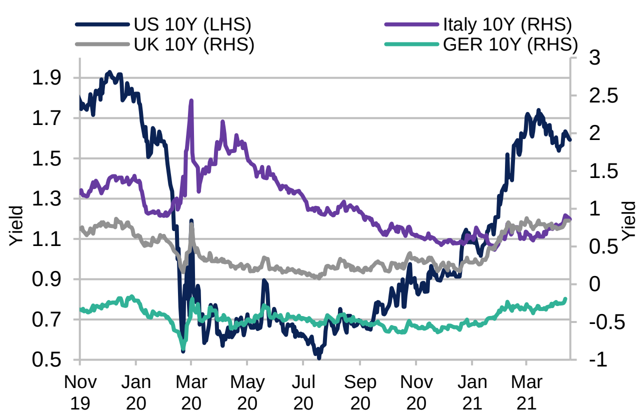
Sterling

Cable has consolidated recent gains, with April performance failing to excite. Cable remains below key resistance at 1.40, but the case for the currency to break this level is building. At the time of writing, the election is a risk, and a strong labour win would provide downside risk. However, the fundamentals will be back in play immediately, and they look strong. We see increasing evidence that the economy is recovering, and fast. Firms are hiring new employees at a rate of knots; job listings have risen and are now 10% below February 2020 levels. Business sentiment is improving, and with it, investment. The UK services business activity reached 60.1 in April, and the economy is looking to maintain this momentum. One thing we have seen in recent months, though, is the increase in part-time roles, but then the economy going back into lockdown and employment struggling once again. Businesses will be hoping that this time around, things will be different.

Retail sales surprised to the upside in March at 5.4% m/m, data suggests that footfall in shops has beaten expectations since shops have opened, and we expect retail sales to improve in the coming weeks. This is due to a significant amount of savings in the UK economy that should aid the recovery, and we expect household balance sheets to be strong. Their expenditure into the economy will be robust as a result. The caveat remains that furlough schemes are creating a false pretence, and when stimulus runs out, unemployment will rise significantly, but for the time being, it will be full steam ahead.

Developed Economy 10-year Yields

UK and US yields have rallied the most, in part due to vaccinations.



Source: Bloomberg

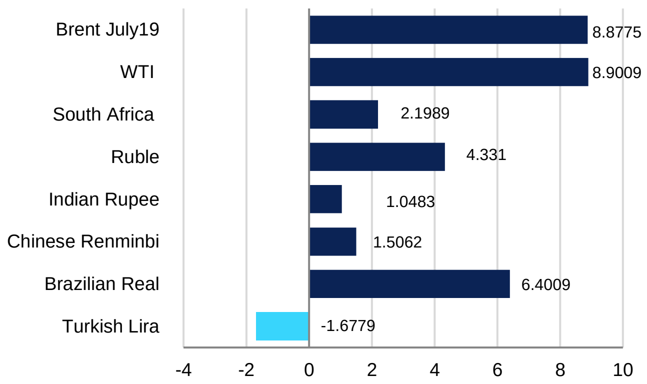
India's Struggles

India's COVID struggle is showing little sign of halting, cases reached 357,000 on May 4th, with deaths at 3,449. The country is running out of oxygen, and countries, including the UK, are sending oxygen, ventilators, and aid. This will significantly damage the economy in the near- and medium-term. The recovery will be slow, and we do not expect robust gains until Q1 2022. The central bank will need to hold its nerve in the near term, inflation is expected to be robust, with March's figure at 5.5% y/y. Food inflation rose 5.2% y/y, up from 4.3% y/y the month prior. Energy and raw material costs have increased, leaving India vulnerable to higher inflation. Energy price increases is a particular factor for India who imports large amounts of oil.

GDP is expected to struggle in 2021; Q3 2021 and Q4 2021 growth is forecast to be 0.5% and 0.9% y/y, but this will not be enough to impact GDP for 2021, which, in our opinion, will be -7.1% y/y. If they are unable to improve economic conditions and get their second wave of COVID under control, there is a significant downside to the economy and INR. Unemployment and consumption have been hit by the second wave. The unemployment rate has increased to 8.4% as of April 18th, with the participation rate at 40.2%, down from 41.2%. Urban unemployment stands at 10.7%; we expect these levels to remain elevated in May and June and possibly longer if the wave is not suppressed.

EM Currencies 1 Month % Change

Indian Rupee is the second worst performing EM currency after Turkish Lira.



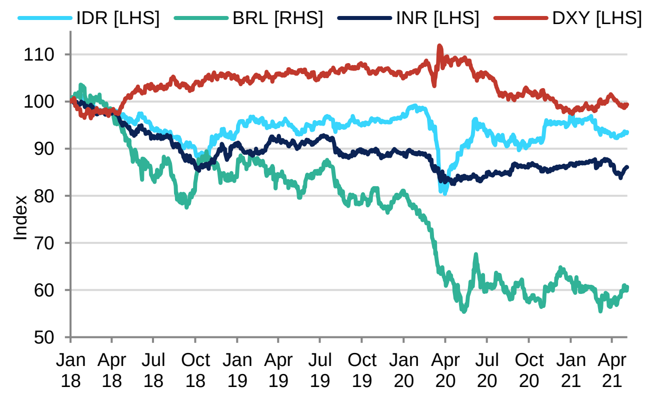
Source: Bloomberg

Consumer confidence has been heavily impacted, Bloomberg high-frequency data shows retail activity declined 30% to April 18th. Consumer sentiment would have fallen further due to the second wave of COVID. Due to more cases in urban areas, we expect rural consumption to be better in these areas. We expect to see demand for jewellery negatively impacted as a result, and this will be seen by reduced gold imports.

Headline economic data in India is not showing the current conditions as they are for March, however, Markit Services and Composite data sets are due today. We expect these to be moderate in the coming months due to the 2nd wave. Economic data will decline in the near term, and stimulus measures will be intact, but this will heavily impact government debt levels. The trade balance was -$14,100 in March, with exports up 60.3% y/y, and imports up 53.7% y/y.

EM Currencies Indexed to January 2018

INR performance is middle of the pack despite the second wave of COVID.



Source: Bloomberg

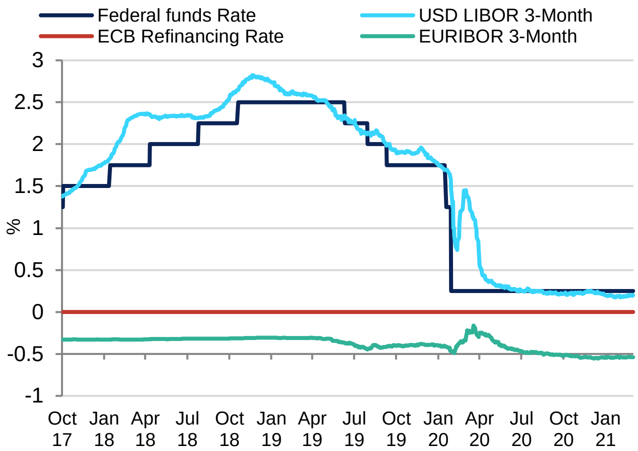
Euro Desk Comments

The euro was broadly unchanged but showed decent strength against the USD during April as forward-looking economic data continued to improve and as Europe's vaccine drive finally clicked into gear; Europe is now projected to be fully vaccinated by year-end. Rising EM risk amid fresh waves of coronavirus also benefitted the EUR as markets tapered back their EM play with EUR as the funding currency.

ECB conference last month was a bit of a non-event as ECB remained committed to conducting its PEPP purchases at an elevated pace during Q2, whilst Lagarde acknowledged Europe's recovery was lagging compared to the US. Therefore, despite the strength in EURUSD during April we expect the cross to remain in the broad range between 1.235/1.17 till Q4. June's ECB meeting will be a key event as we receive new macro projections, especially inflation expectation and will help set a more forward-looking narrative for Q4 onwards.

EU and US Interest Rate vs LIBOR and EURIBOR

EURIBOR has softened in recent weeks, despite refinancing rate holding steady.



Source: Bloomberg

USD Desk Comments

After a decent performance in Q1 the USD has started the quarter on the back foot despite the dollar being bought back during month-end rebalancing, as clear divergences in Central banks paths are materialising. During April's FOMC meeting, the Fed remained as dovish as they could be despite acknowledging a decent economic recovery thus far. Chris Powell also said there had been no discussion on tapering, which is incomplete contrast to BOC and the Norges Bank who are both looking at starting tapering.

The Fed's reluctance to start discussing policy normalisation could see markets re-engaging their USD shorts again. There is already evidence of this as CFTC futures data for the week ending 23/30 Apr showed investors initiating USD shorts for 2 consecutive weeks for the first time since January after weeks of unwinding. The pace of US yield rise has also slowed down and could now lead to a period of trading rangebound, which will make any sort of rally in USD difficult and could pave the way for a selloff.

As we have mentioned previously we do not expect any policy normalisation to materialise till Q4 and the loose monetary policy is likely to weigh on the USD in short term before the start of a new longer-term USD appreciation cycle.

US 10yr Yield vs the Dollar

US yield curve continues to steepen, and the dollar strengthens.

Source: Bloomberg

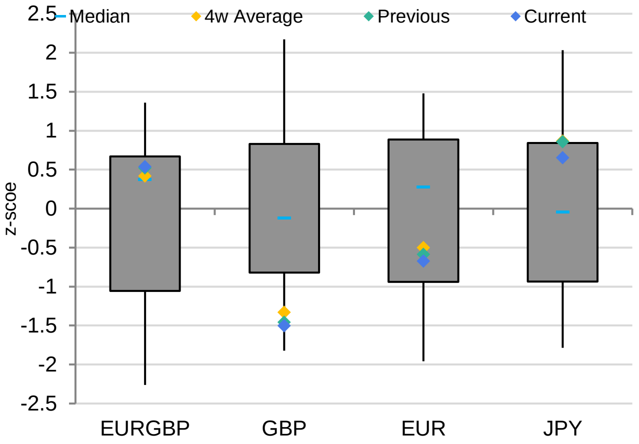
GBP Desk Comments

It has been a relative insipid month for the GBP despite economic data continuing to surprise to the upside, providing further evidence of a robust recovery in the UK. We continue to believe the conditions are favourable for the UK to continue growing faster than its major counterparts after a successful vaccine drive in a post Brexit era. Hence, we maintain our long term view for a rise to 1.50 area in Cable by year-end.

However, despite being GBP bullish, something our readers should keep in mind is Cable has not had a positive month in May since 2009. Perhaps this is partially down to May being time for elections and this month could be no different as the UK holds local elections this week; with the key focus being Scotland where an SNP majority could reopen the door to a second referendum for Scottish independence. Another key event to watch is the BOE meeting and any hints for tapering. Both these events have the potential to jeopardise our long term expectations.

Major Currency Commercial Positioning

All positioning remains below the long-term median.



Source: CME, Sucden Financial

Gold

In April, the gold price has found support at $1,700/oz before picking up higher, as muted Treasury yields and a softer dollar supported the precious metal. Indeed, there is further upside to gold as central banks keep interest rates low, pushing yields back down; however, positive economic and virus-related news are likely to cap gold's performance on the upside. Historically, increased fears over inflation have largely been favourable to gold. This time, though, the growth in confidence, especially at the consumer level, and the expectations of a successful outcome from the vaccination programmes have combined to focus investor attention on economic growth prospects; this has boosted longer-term bond yields. All these factors have combined to reduce gold's risk-hedge role and thus put pressure on gold prices.

Gold vs 10yr Yields vs S&P 500 vs Dollar

Both gold and US stocks are picking up higher in April, whilst the dollar loses steam.

Source: Bloomberg

On the other hand, if inflation expectations persist, breaching psychological levels, that could prove supportive for gold. The lack of any agreement on inflation risk, especially, keeps some investors on the fence as policymakers have been downplaying the risks. The recent statement by Treasury Secretary Yellen that the rate may rise at one point to spot the economy from overheating may further intensify the possibility of earlier-than-expected tightening. We see rising inflation to lift the gold price during the third quarter of this year as we start to see economies in full-swing recovery. Still, from a physical demand perspective, a resurgence in virus cases and restrictions on movement and business activity in India is worrying jewellers as it could threaten the revival in sales.

Silver

Silver ETF Holdings vs Spot Price

Softer investor demand, after the Reddit-driven rally, weakened the metal to test $24/oz once again.

Source: Bloomberg

After the Reddit-driven frenzy in February, silver prices pulled back in line with the long-term average. The Fed's accommodative stance in recent weeks has helped cool a rise in Treasury yields that benefitted non-interest-bearing silver. In particular, the outlook for silver in the US is bright with Biden's new infrastructure plan. The president's commitment to accelerate wind and solar deployment is expected to be a key driver in long-term silver demand. In the meantime, silver's performance seems closely tied to gold. When investment demand is low, silver tends to revert to its industrial character, but over the past quarter, it has followed gold movements more closely. We believe silver prices are set to continue to outperform gold through 2021 as it benefits from rising inflation and renewed industrial demand as the global economy bounces back from the COVID-19 pandemic.

Technical Charts

GBPUSD

GBP is consolidating and has formed a descending triangle. On the upside a break of the down trend should see market test recent high and resistance @ 1.43 (50% fib of the move from 03/16 to 03/20) and at 1.4382 (High from April 2018). A break of these level will lead to next leg higher towards 61.8% fib / 1.50 psychological level. This view remains intact while downside support @ 1.35 holds. A sustained close below 1.35 would lead to a larger pull back to 1.32.

EURUSD

EURUSD is trading in a broad range within a Wedge with a potential head and shoulders pattern forming. On the downside a move below lower trend line could see market test last month's 1.1702 level and then support @ 1.16. On the upside a close above upper trendline could pave the way to test highs from start of the year @ 1.2349.

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A suite of reports looking at how the global automobile market is changing, and as vehicle manufacturers look to transition to a more environmental fleet of autos we have outlined how prepared the energy markets in the U.S., China, Japan, and Europe are to aid this transition. Electric vehicles go a long way reduce GHG emissions in the auto market, we are not disputing this, and when you factor in the lifecycle of batteries EVs are a lot greener. However, these reports assess the energy mix in these specific regions and outlines what governments are doing to promote renewable energy and transition away from fossil fuels. Using the energy mix we provide emission analysis for different EVs compared to ICE vehicles in that country.

Coffee Investment Research

This report drills down into the detail of the coffee market and is produced three times a year, we also produce shorter more concise updates. We undertake a macroeconomic assessment of major consuming and producing regions before analysing the recent earnings reports from Starbucks, Nestle, Luckin Coffee, Dunkin Donuts, and Costa. This helps us highlight new sales and marketing techniques and any consumption changes, which has been particularly popular during COVID-19. The largest chunk of this report is where we assess the Supply and Demand outlook using our primary data for the coffee market and where we apply our fundamental models. We showcase our crop forecasts and highlight any changes before providing prices forecasts and trading strategies with futures and options.

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