

Risk Insight

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INSIDE THIS ISSUE:

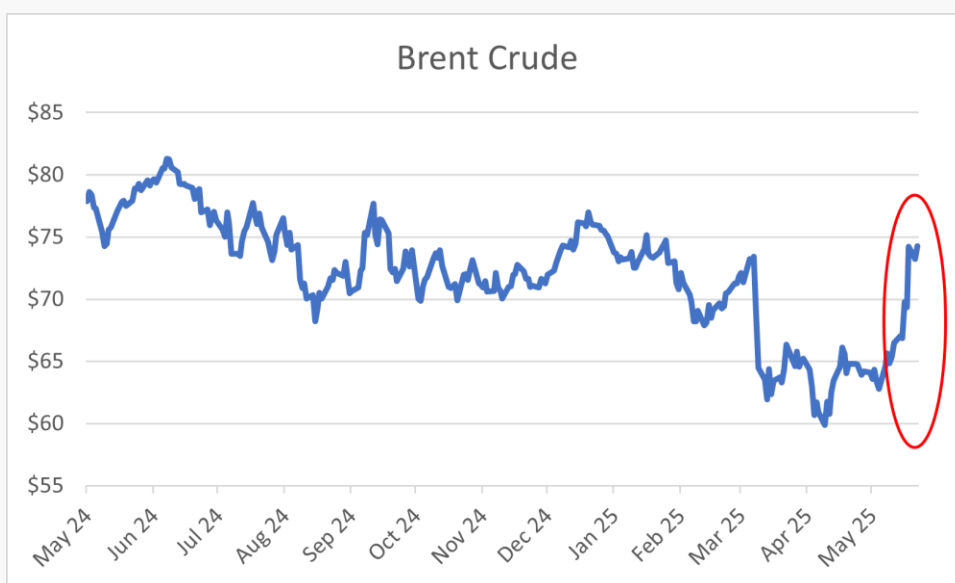
BIG PICTURE > GBPUSD > GBPEUR > EURUSD > USDCAD > ECONOMIC DATA

Could Middle East strife hand the dollar a lifeline?

Authored by **Marc Cogliatti, Global Capital Markets Director**

Israel has grabbed the headlines striking Iran's nuclear facilities and killing several senior military figures. The attack has sharply raised geopolitical tensions and carries the potential to snowball - locally if Iran's allies retaliate, and globally should Russia, China or the United States be pulled in.

Chart 1: Brent Crude Prices Over the Past Year



Source: Validus / Bloomberg

Greenback appears unfazed

Commodity and equity markets reacted exactly as the playbook suggests. Brent crude spiked more than 11 per cent at one point on Friday, while the S&P 500 closed 1.13 per cent lower. Foreign exchange moves, however, were conspicuously muted. In the past, a clear "risk-off" mood would have sparked a dash for US Treasuries and a stronger dollar. Instead, although Treasury yields dipped slightly, the dollar index (DXY) is still within half a per cent of its lowest level since March 2022 - a world away from the rallies of yesteryear.

Two forces appear to be keeping the greenback in check. First, investors may believe that, despite the headlines, hostilities will remain contained. Monday's market action backed that view: oil fell roughly 4 per cent and the S&P erased Friday's loss. Second, the long-standing link between risk sentiment and the dollar has weakened. Since Donald Trump's presidency, uncertainty over US trade policy has driven many investors to trim exposure to US assets, diluting the dollar's haven status.

Both factors are probably at work. It is also telling that the traditional safe-haven currencies - the Japanese yen and Swiss franc - barely twitched last week. Even so, now is hardly the moment for complacency. We see immediate risks.

Escalation

Although Iran has signalled a desire to de-escalate, exchanges continue: Iran has launched multiple waves of drones and missiles, while Israel's strikes killed another senior commander.

For now, traffic flows normally, but if Iran blocks the Strait of Hormuz and Europe's oil supplies are disrupted, inflation could flare and force central banks to raise rates just when they would prefer to cut them to revive sluggish growth.

Crowded short-dollar positioning

Virtually every currency strategist now seems to predict further dollar weakness. While that aligns with our long-held view, a one-sided consensus can be a contrarian warning that leaves the market vulnerable to a squeeze.

Our bias remains for a weaker dollar, yet a dose of caution is prudent. EUR/USD still struggles to sustain rallies above 1.16, and GBP/USD feels heavy north of 1.36, although CFTC data show positioning is far from extreme, leaving room on the upside for both pairs.

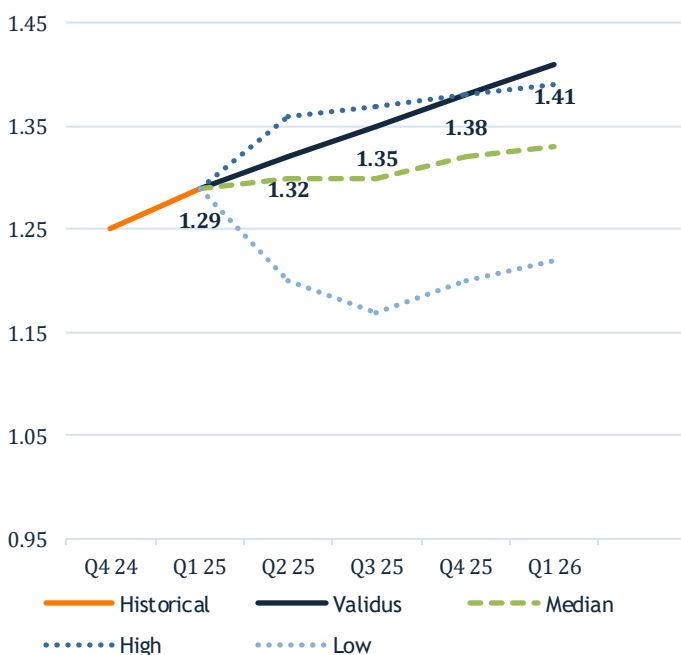
GBP USD

GBPUSD traded flat finishing up just +0.05%. That's after a -0.52% fall today, as fears of an escalation in the Middle East re-ignited with Trump downplaying a ceasefire in Iran, calling instead for "a real end" and permanent elimination of Iran's nuclear programme. On the data front, US initial jobless claims came in at +248k, above forecasts of +242k. Continuing claims rose to 1965k, the highest level since 2021. US retail sales fell -0.9% MoM, worse than forecasts of -0.6%. US industrial production also fell -0.2% MoM, while the empire manufacturing index came in at -16.0 (vs -6.0 expected).

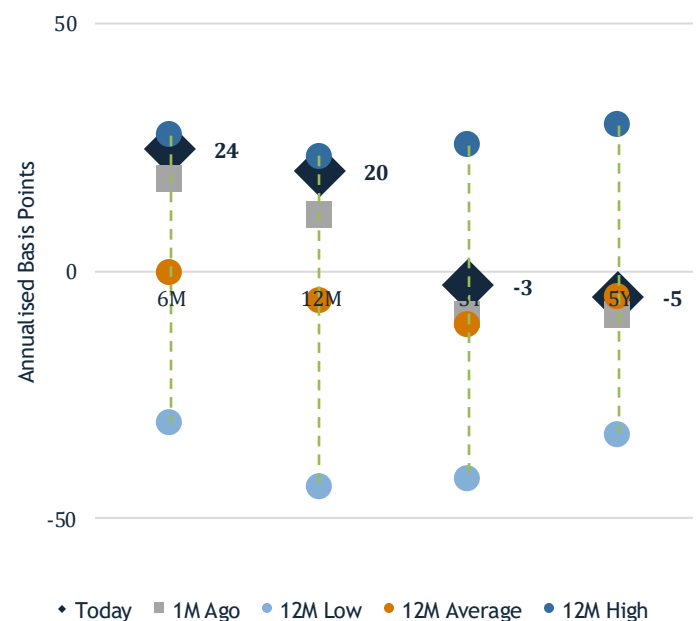
The bright spot was the university of Michigan sentiment survey which rose to 60.5, as trade tensions eased. In the UK, industrial production and manufacturing were also weaker than expected, at -0.6% and -0.9% respectively.

To the week ahead, both the Fed and BoE are due to make their June decisions. UK data will include CPI and retail sales, while US sentiment data and initial jobless claims are due.

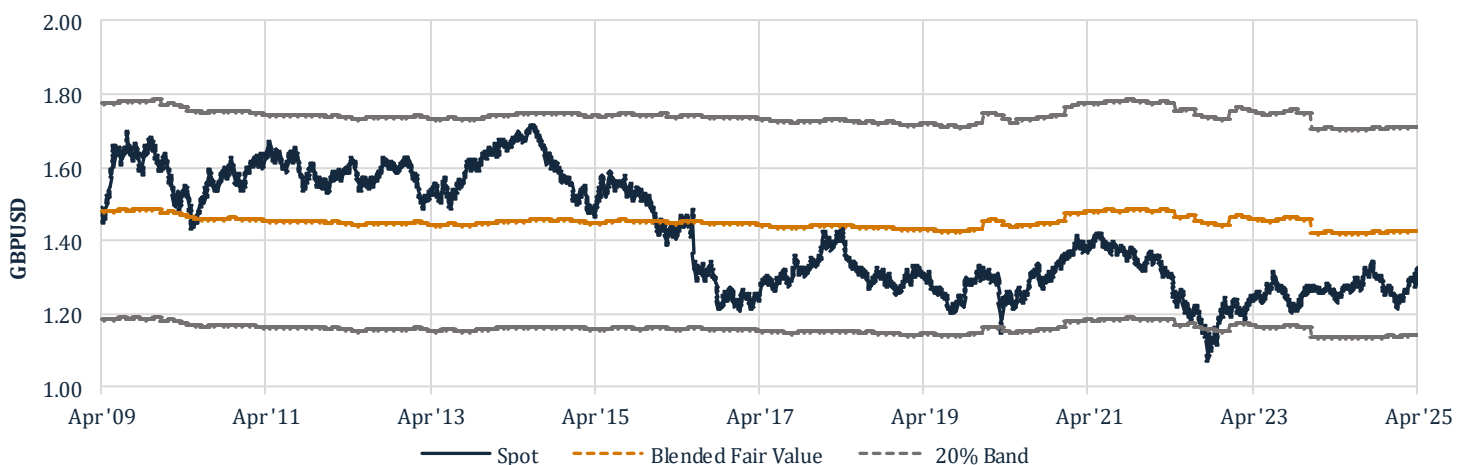
FX Forecasts (Updated 25 April 2025)



Hedging Cost/Pickup* (Impact to sell GBP Forward)



PPP Valuation



According to Purchasing Power Parity, GBPUSD is currently **-5.3% undervalued**.

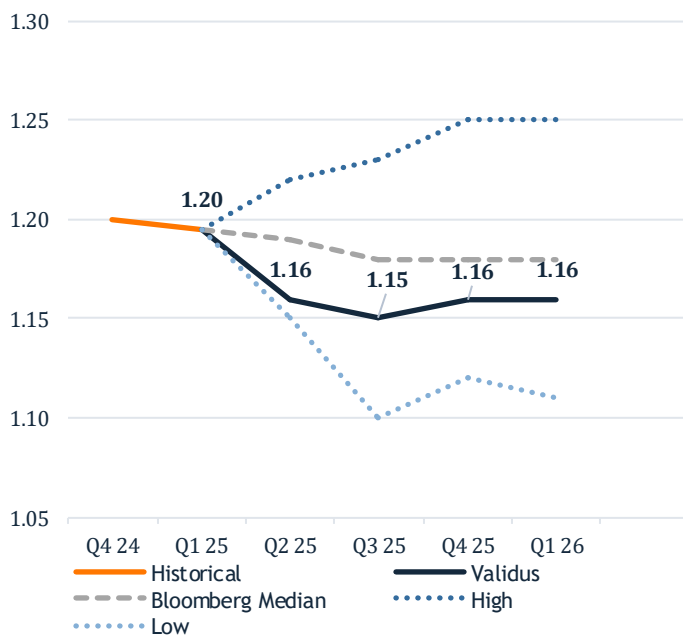
(To determine whether a currency pair is over- or undervalued, we employ a proprietary valuation methodology incorporating CPI, PPI and other metrics)

GBPEUR finished the week down -1.01%. UK industrial production fell -0.6% MoM (vs -0.5% expected) and manufacturing production fell -0.9% MoM (vs -0.7% expected). That follows recent UK data that pointed to both a weaker labour market and inflationary pressures. This stands in contrast to Europe, where inflation has cooled - as finalised German CPI came in at +2.1% YoY this week. German sentiment and growth expectations have also picked up. The German ZEW expectations survey surged to 47.0 from 25.2, and above forecasts of 35.0.

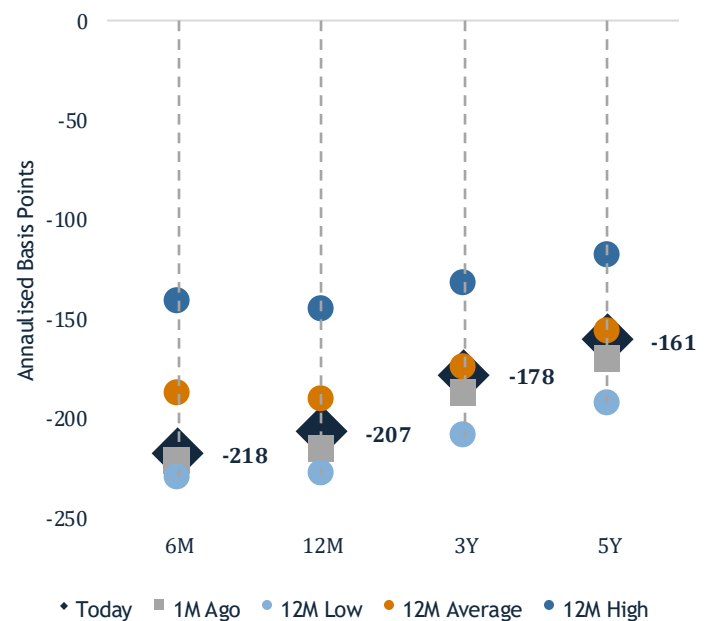
Investors are turning more positive, as fiscal easing under the new government is expected to drive growth. The improved outlook comes despite continued uncertainty over trade policy with the US.

UK CPI is due later this week, ahead of the BoE decision. The UK is also due retail sales data and both services and manufacturing PMI. European PMIs are also due, as is the German IFO Business Climate survey.

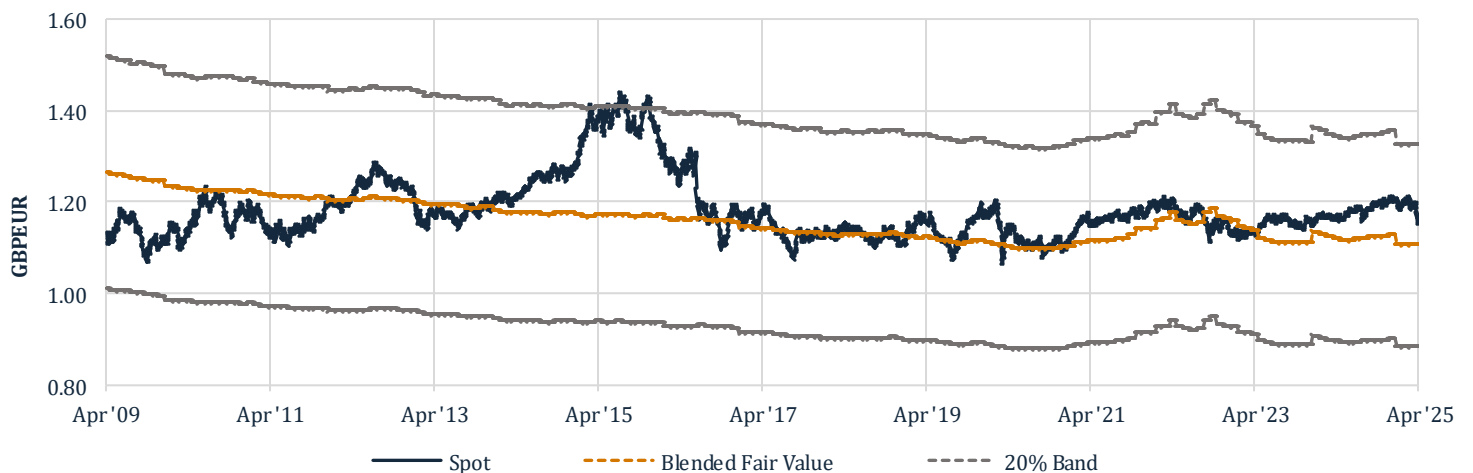
FX Forecasts (Updated 25 April 2025)



Hedging Cost/Pickup* (Impact to sell GBP Forward)



PPP Valuation



According to Purchasing Power Parity, GBPEUR is currently **+2.0% overvalued**.

(To determine whether a currency pair is over- or undervalued, we employ a proprietary valuation methodology incorporating CPI, PPI and other metrics)

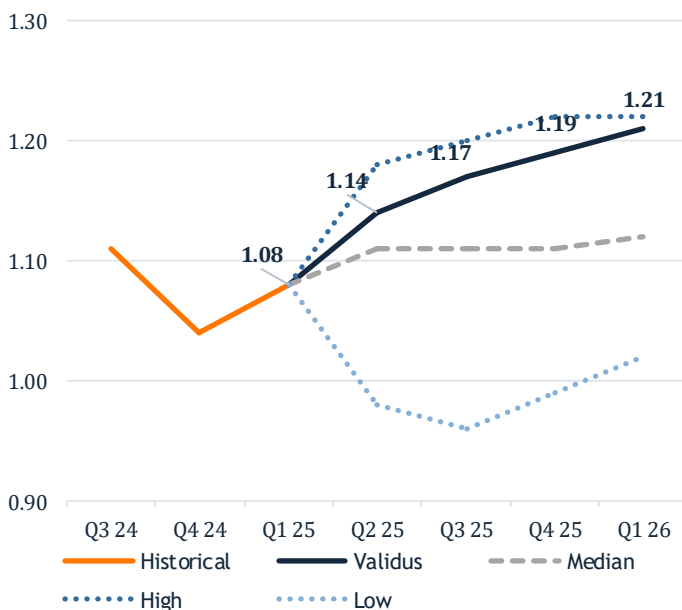
EUR USD

EURUSD rose through the week, finishing up +0.48%. US initial jobless claims came in at 248k (vs 242k expected), exceeding forecasts for the third week in a row. Levels are slightly elevated compared to a year ago. Perhaps more concerning is continuing claims, which surged to 1965k, the highest level since 2021. US retail sales also slumped this week, falling 0.9% MoM (vs -0.6% expected). Spending pullback in cars was the main driver. Despite this, consumer sentiment appeared to pick up, as the university of Michigan survey rose to 60.5 (vs 53.6 expected). Trade de-escalation with China helped both current and future economic expectations to improve.

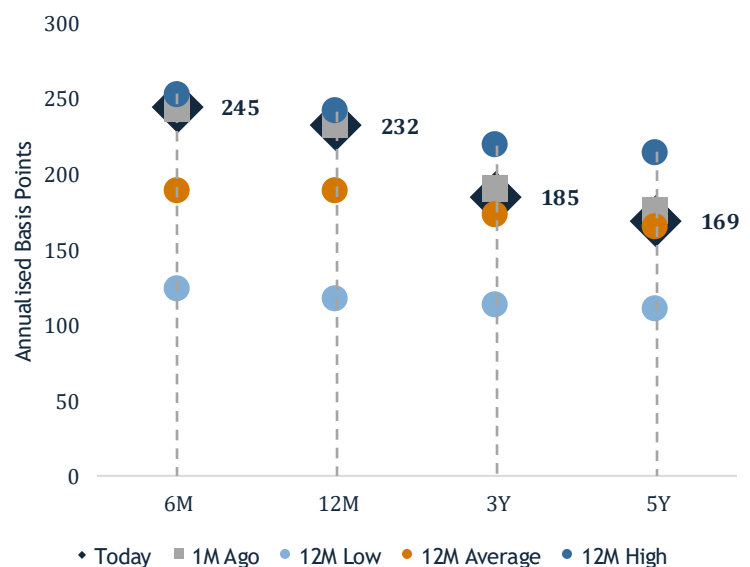
Inflation expectations fell, while views on the labour market improved. It was a similar story in Europe, as the German ZEW survey expectations surged to 47.5 from 25.2, and above forecasts of 35.0. In Germany, growth sentiment has improved, as the positives of fiscal stimulus outweigh the negative trade outlook.

The week ahead will include the Fed rate decisions and US initial jobless claims. In Europe, inflation data and manufacturing PMIs are due. Markets will also be attuned to developments on the Iranian conflict, including possible US involvement.

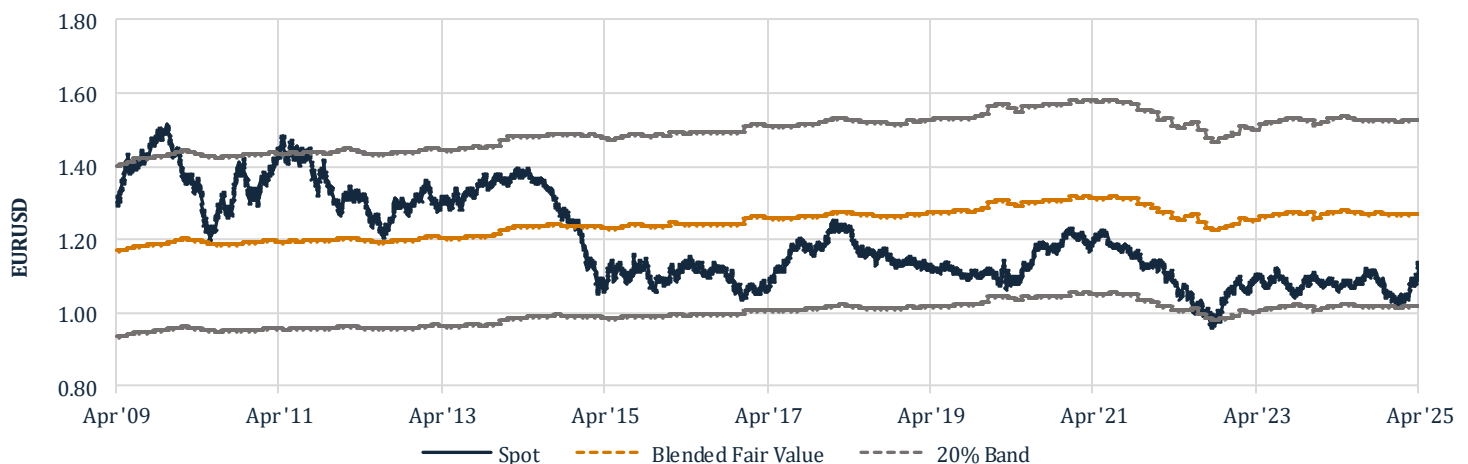
FX Forecasts (Updated 25 April 2025)



Hedging Cost/Pickup* (Impact to sell EUR Forward)



PPP Valuation



According to Purchasing Power Parity, EURUSD is currently **11.0% undervalued**.

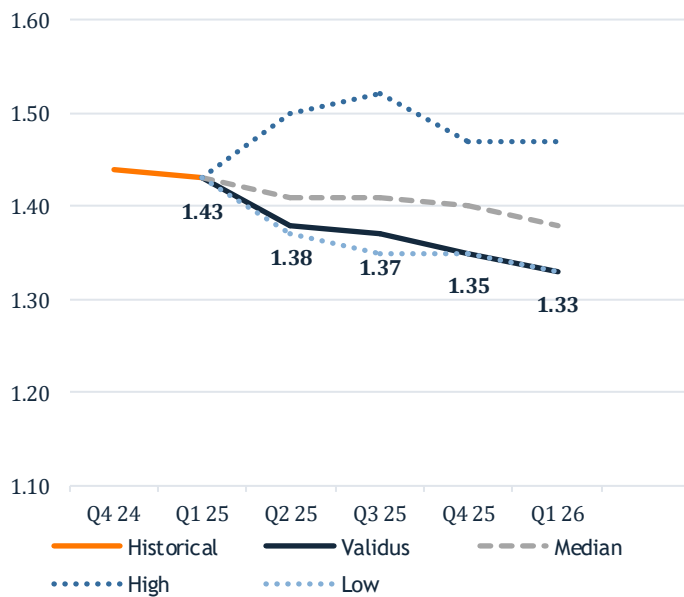
(To determine whether a currency pair is over- or undervalued, we employ a proprietary valuation methodology incorporating CPI, PPI and other metrics)

USDCAD traded flat this week, after the dollar rallied +0.66% following the prospect of a US involvement in the ongoing Iranian conflict. In terms of data, US releases dominated the week: the labour market appears to be softening, with initial jobless claims coming in at 248k, above forecasts of 242k. Continuing claims rose to 1965k, the highest level since 2021. The US Empire manufacturing survey fell sharply to -16.0 (vs -6.0 expected), and industrial production slipped -0.2% (vs no expected change). Retail sales also slumped to -0.9%, beneath forecasts of -0.6%.

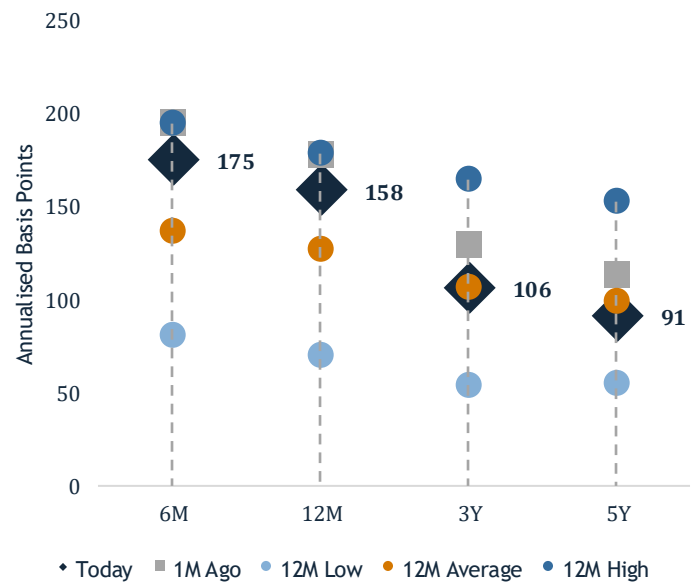
However, US consumer sentiment did pick up, with the university of Michigan sentiment survey improving to 60.5 (vs 53.6 expected). De-escalating trade tensions with China helped boost the outlook.

The week ahead will see the Fed's June interest rate decision, and Canadian CPI data. Markets will also continue to watch the escalating Israel-Iran conflict, especially focusing on any US involvement.

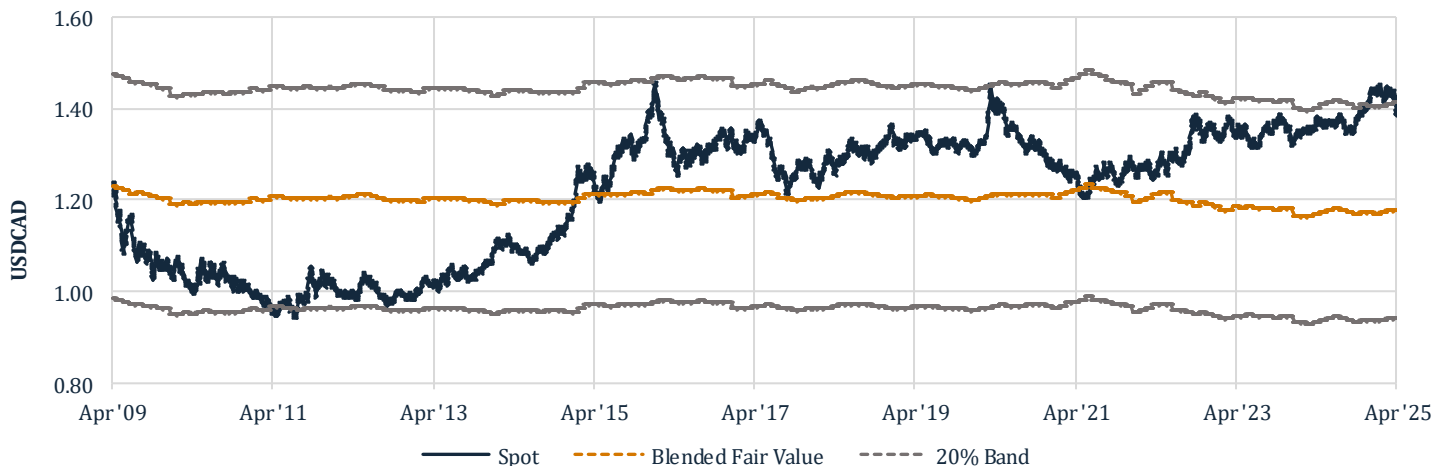
FX Forecasts (Updated 25 April 2025)



Hedging Cost/Pickup* (Impact to sell CAD Forward)



PPP Valuation



According to Purchasing Power Parity, USDCAD is currently **17.5% overvalued**.

(To determine whether a currency pair is over- or undervalued, we employ a proprietary valuation methodology incorporating CPI, PPI and other metrics)

Economic Data & Market Indicators

Economic Matrix

	GDP	CPI	Unem- ployment	Industrial Production	Retail Sales	Current Account % GDP	Budget Balance % GDP	10 Year Yield
USD	-0.20%	2.40%	4.20%	0.60%	3.30%	-3.81%	-6.98%	4.41%
EUR	1.50%	1.90%	6.20%	0.80%	2.30%	2.91%	-3.09%	2.54%
GBP	1.30%	3.50%	4.60%	-0.30%	1.30%	-2.66%	-5.13%	4.55%
CAD	2.22%	1.70%	7.00%	1.96%	5.60%	-0.45%	-0.03%	3.38%

Central Bank Bias

	Current Rate	Last Change	Date of Change	Next Meeting	Likely Outcome
USD	4.50%	-0.25%	19 Dec 24	18 June	Hold (100%)
EUR	2.00%	-0.25%	5 June 25	24 July	Hold (92%)
GBP	4.25%	- 0.25%	8 May 25	19 June	Hold (96%)
CAD	2.75%	-0.25%	12 Mar 25	30 July	Hold (74%)

Economic Calendar

GBP	CPI / Core CPI	Wednesday, June 18
USD	Initial Jobless Claims	Wednesday, June 18
USD	Fed Rate Decision	Wednesday, June 18
GBP	BoE Rate Decision	Thursday, June 19
GBP	Retail Sales Inc Auto Fuel	Friday June 20
USD	Leading Index	Friday June 20
EUR	HCOB Eurozone Manufacturing PMI	Monday June 23
CAD	CPI	Tuesday, June 24