Weekly Market Brief

AIB Treasury Economic Research Unit

22nd - 26th November 2021

Euro Under Pressure

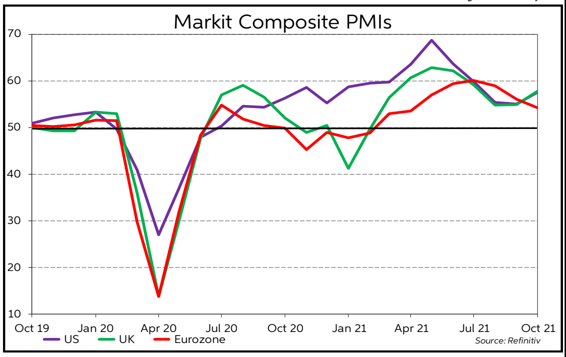
- **Expectations in regard to interest rates are having a perceptible impact on currency markets.** The dollar, in particular, has been on a rising trend since mid-year in the context of the Fed laying the groundwork for QE tapering, but more specifically, the central bank turning hawkish in its projections on interest rates. The current median projection from the Fed is that US rates will start to be hiked from their present level of 0.125% before end 2022, getting to 1% by end 2023 and 1.75% at end 2024. Up until June, the Fed was of the view that there would be no increase in rates out to end 2023. Markets have turned even more hawkish, looking for two 25bps hikes in 2022 and three more the following year, taking rates to 1.375% by end 2023.

- **Interest rate futures contracts have hardened somewhat in the Eurozone also, but nothing like to the same extent as in the US.** Furthermore, while the market is looking for euro rates to start rising before end 2022, the ECB is pouring cold water on the notion. It believes that the current spike higher in prices will prove transitory, and inflation will fall back below target in the next couple of years, suggesting rate tightening will not be required. This more dovish approach from the ECB has seen the euro come under pressure against the dollar. The EUR/USD rate has fallen from $1.22 in early June to around $1.13 in recent days.

- **Interest rates driving currency movements is nothing new in forex markets.** The dollar appreciated very sharply between 2014-2016 and stayed at elevated levels over the rest of the decade, underpinned by relatively high US interest rates. However, it moved steadily lower in the final three quarters of 2020, losing 12% against the other major currencies, as US rates were cut to virtually zero. Eurozone rates remained unchanged so the euro rose last year on the back of a favourable move in interest rate differentials. Meanwhile, the yen has lost considerable ground this year on the hardening of rate hike expectations elsewhere. On the other hand, sterling has benefitted from signals by the BoE that UK rate hikes are on the cards, sooner rather than later. The market expects over 100bps of BoE tightening before end 2022. This has seen the euro fall from 86.5p at end September to around the 84p level more recently.

- **A key question is, will the slide in the euro continue?** Rate hikes seem likely very soon in the UK, which should be supportive of sterling. However, the 83p level is a major support level for the euro, which has not been overcome by sterling since the Brexit referendum in 2016. This support level may continue to hold, even with rate hikes, given the UK economy is lagging behind elsewhere in terms of its economic performance over 2020-21. Meanwhile, against the dollar, there is considerable support for the euro in the $1.10-1.13 range. Beyond that, the $1.08 level offers very strong support, which most notably held in H1 2020. Indeed, one has to go back to 2015-2016 for the last time the pair spent any time below the $1.08 level. Overall then, as we move into next year and the Fed gets nearer to the point of hiking rates, this could bring more downward pressure to bear on the EUR/USD rate. However, a very sharp fall from here in the pair seems unlikely.

- **This week, the release of the latest monetary policy meeting minutes from the ECB and the Fed are likely to further highlight the contrast in tone from both central banks.** Data-wise, the flash PMIs for November in the US, UK and the Eurozone, will be the highlight. A similar pattern to previous months is set to continue, with both sector (manufacturing and services) readings forecast to be little changed across the board. This would leave the indices firmly in expansion mode, above 50, consistent with continued economic growth, albeit at a slower pace than earlier in the year.



- **A host of other survey data are also due in the Eurozone.** Firstly, consumer confidence is forecast to deteriorate slightly in November. It should be noted though, that the index is still above its pre-Covid level. Consumer sentiment indices from the largest three Eurozone economies, Germany, France and Italy are expected to edge lower also, in-line with the bloc wide measure. Business sentiment indices in all three countries, are projected to decline slightly in November as well, including the German Ifo index.

- **In the US, the October release of core-PCE inflation will garner close attention.** Core-PCE has been unchanged since June, at 3.6%. However, core-PCE is projected to jump to 4.1% in October, its highest level since December 1990. This is similar to core-CPI which surged to 4.6% on a broad range of price increases in October. Elsewhere, the latest personal income and consumption data are projected to rise by 0.3% and 0.9% respectively in October. **Meanwhile, there is a quiet data schedule in the UK. Comments from a host of BoE members will be monitored closely though.**

Interest Rate Forecasts

	Current	End Q4 2021	End Q1 2022	End Q2 2022
Fed Funds	0.125	0.125	0.125	0.125
ECB Deposit	-0.50	-0.50	-0.50	-0.50
BoE Repo	0.10	0.10	0.25	0.50
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 Q4 2021	End Q1 2022	End Q2 2022
EUR/USD	1.1304	1.12	1.11	1.11
EUR/GBP	0.8403	0.84	0.83	0.83
EUR/JPY	128.72	129	129	130
GBP/USD	1.3450	1.33	1.34	1.34
USD/JPY	113.86	115	116	117

Current Rates Reuters, Forecasts AIB's ERU

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ECONOMIC DIARY

Monday 22nd - Friday 26th November

Date		*UK & Irish Time*	*Release*	*Previous*	*Forecast*
This Week:	**ECB Speakers:**		de Guindos (Mon); de Guindos (Tue); Panetta, Schnabel (Wed); Schnabel, **Lagarde** (Thu); **Lagarde** (Fri)		
	BoE Speakers:		Tenreyro (Wed); **Bailey,** Haskel (Thu); Pill (Fri)		
	Fed Speakers:				
Mon 22nd	**EU-19:**	15:00	Flash Consumer Confidence (November)	-4.8	-5.5
	US:	15:00	Existing Home Sales (October)	+6.3m / +7.0%	+6.2m / -1.4%
Tue 23rd	**FRA:**	08:15	Flash Markit Composite PMI (November)	54.7	53.4
	GER:	08:30	Flash Markit Composite PMI (November)	52.0	51.0
	EU-19:	09:00	Flash Markit Composite PMI (November)	54.2	53.1
			- Manufacturing / Services	58.3 / 54.6	57.2 / 53.6
	UK:	09:00	Flash Markit / CIPS Composite PMI (November)	57.8	57.5
			- Manufacturing / Services	57.8 / 59.1	57.4 / 58.5
	US:	09:30	Flash Markit Composite PMI (November)	57.6	58.0
			- Manufacturing / Services	58.4 / 58.7	59.0 / 59.1
Wed 24th	**FRA:**	07:45	INSEE Business Climate (November)	107	106
	GER:	09:00	German IFO (November)	97.7	96.7
	US:	13:30	Durable Goods (October)	-0.3%	+0.3%
			- Ex-Transport	+0.5%	+0.5%
	US:	13:30	GDP (Q3: Second Reading)	+2.0% s.a.a.r.	+2.1% s.a.a.r.
	US:	13:30	PCE Prices (Q3: Second Reading)	+5.3% s.a.a.r.	+5.3% s.a.a.r.
			- Core PCE Prices (Q3: Second Reading)	+4.5% s.a.a.r.	+4.5% s.a.a.r.
	US:	13:30	Initial Jobless Claims (w/e 15th November)	+268,000	+260,000
	US:	15:00	Personal Income / Consumption	-1.0% / +0.6%	+0.3% / +0.9%
			- Core PCE Prices	+0.2% (+3.6%)	+0.4% (+4.1%)
	US:	15:00	Final Uni. Michigan Consumer Sentiment (Nov)	66.8	67.0
	US:	15:00	New Home Sales (October)	+0.8m / +14.0%	+0.8m / -0.3%
	US:	19:00	FOMC Meeting Minutes (Meeting 2nd-3rd Nov)		
Thu 25th	**US:**		**Thanksgiving (Market Holiday)**		
	GER:	07:00	Gfk Consumer Sentiment (December)	0.9	-0.3
	EU-19:	11:00	ECB Meeting Minutes (Meeting 24th-25th Oct)		
	IRL:	***11:00***	***Labour Force Survey (Q3 2021)***		
			- Unemployment Rate	***6.9%***	***5.4%***
Fri 26th	**FRA:**	07:45	Consumer Confidence (November)	99	98.8
	ITA:	09:00	ISTAT Business Confidence (November)	114.9	114.0
	ITA:	09:00	Consumer Confidence (November)	118.4	
	EU-19:	09:00	M3 Annual Money Growth (November)	(+7.4%)	(+7.4%)

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