Weekly Market Brief

AIB Treasury Economic Research Unit

2nd – 6th October 2023

When September Ends

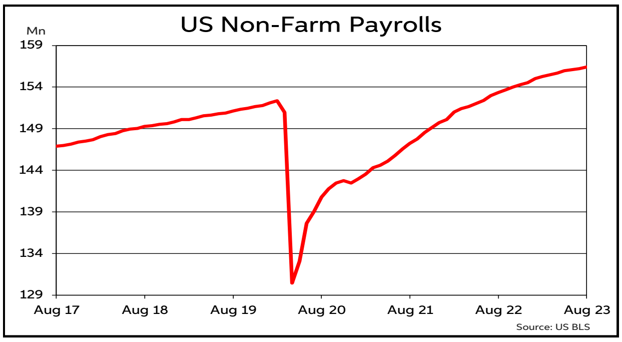
- **September has proved to be the worst month so far in 2023 for bond markets and equities, largely on the back of the "higher-for-longer" mantra from central banks on interest rates.** In particular, a very hawkish line from the Federal Reserve has hammered US markets over the past month. The S&P 500 fell by 5% in September, while ten-year Treasury yields were up by as much as 55bps at one point, hitting 4.65% in the past week, their highest level since 2007. Encouraging US inflation data over the summer had given markets hope that rates may have peaked. Thus, they have been surprised by indications from the Fed that it could hike rates by a further 25bps to a 5.5-5.75% range before the end of the year. Even more damage has been done by Fed guidance that rates are likely to be kept above 5% in 2024. Back in July, the expectation was that US rates would fall to below 4% by the end of next year.

- **It is the scaling back of rate cut expectations that has done the real damage to bonds, with negative knock-on consequences for stock markets.** Other negative factors are also at work. Oil price have unexpectedly risen to close on $100 a barrel, pushing inflation back up again in many economies. There is also a growing realisation that bond issuance will remain at high levels in the face of rising budget deficits as economies slow. The US Federal Budget deficit will be around 6% of GDP this year and is likely to rise to 7% in 2024. Meanwhile, central banks as well as hiking rates, are also engaged in quantitative tightening. This is being done by allowing large amounts of their bonds holdings to mature without replacing them. This means they have to be refinanced in the market, adding to supply pressures.

- **The rise in bond yields since 2020 has been dramatic in the face of the completely changed monetary policy environment.** In the US, ten year yields have risen by over 400bps from their trough of 0.5% three years ago. Ten year UK gilt yields have climbed from 0.1% to 4.5%. In the Eurozone, ten year German yields have risen from -0.6% at end 2020 to near 3%. **Big rises in bond yields have significant consequences.** It puts pressure on public finances as deficits and maturing debt have to be financed at much higher interest rates, with the impact greatest on those economies with the highest deficits and debt levels. Property markets can also come under pressure as mortgages and commercial property loans face much higher financing costs, with associated rising bad debts. The latter could present a major challenge to those US banks that have particularly large exposures to the CRE market.

- Higher yields can also spell trouble for global financial markets as **equities suffer on a relative valuation basis when bond prices fall,** as has been evident in the past month. It can also unsettle currency markets. We have seen fresh gains by the dollar in recent months, both on risk aversion and with US rates rising to particularly high levels. Meanwhile, low yielding currencies can get hammered, as has happened to the yen in the past two years. It is likely to remain a challenging environment for both financial markets and borrowers until rate cuts start to appear on the horizon.

- **Turning to the week ahead, the main release of note will be the US labour market report for September.** Labour market data have softened slightly in recent months. Payroll growth averaged 257k per month in the first half of the year, before slowing to 157k and 187k, in July and August. Furthermore, the unemployment rate rose to 3.8% in August, its highest level since February 2022. Meantime, average earnings growth remained elevated, at 4.3% year-on-year in August. However, this is down from 4.8% last December, and a peak of 5.9% in March 2022. In September, payrolls are forecast to expand by 158k, with average earnings growth remaining at 4.3%. The unemployment rate is expected to inch lower to 3.7%.



- In terms of more lagging US labour market data, **JOLTS job openings for August are due,** having declined to 8.8m in July, its lowest level since March 2021. Openings are projected to fall to 8.5m in August. Meanwhile, **the manufacturing and non-manufacturing ISMs for September are also due.** The manufacturing ISM is expected to remain in contraction mode, while the non-manufacturing ISM is forecast to stay in expansion territory, but fall from 54.5 to 53.6.

- **Elsewhere, the Eurozone unemployment rate for August will be released.** It fell to a new all-time low of 6.4% in May, and stayed at that level in June and July. The consensus is for the jobless rate to remain at 6.4% in August also. In terms of inflation data, a sharp drop in **Eurozone producer price inflation** to –11.6% is anticipated in August, from –7.6%. Meantime, having declined by 0.2% in July, a further contraction of 0.3% in retail sales is pencilled in for August. **On the home front, a busy data schedule includes the latest PMIs, unemployment and Exchequer Returns for September,** with the latter an important release in the run-up to Budget 2024 on October 10th. No major UK data are due this week.

Interest Rate Forecasts

	Current	End Q4 2023	End Q1 2024	End Q2 2024
Fed Funds	5.375	5.625	5.625	5.625
ECB Deposit	4.00	4.00	4.00	4.00
BoE Repo	5.25	5.50	5.50	5.50
BoJ OCR	-0.10	-0.10	-0.10	0.25

Current Rates Reuters, Forecasts AIB's ERU

Exchange Rate Forecasts (Mid-Point of Range)

	Current	End Q4 2023	End Q1 2024	End Q2 2024
EUR/USD	1.0577	1.08	1.09	1.10
EUR/GBP	0.8667	0.87	0.87	0.87
EUR/JPY	157.97	158	154	150
GBP/USD	1.2205	1.24	1.25	1.26
USD/JPY	149.34	146	141	136

Current Rates Reuters, Forecasts AIB's ERU

ECONOMIC DIARY

Monday 2nd - Friday 6th October

AIB Treasury Economic Research

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Date	*UK & Irish Time*		*Release*	*Previous*	*Forecast*
This Week:	**ECB Speakers:**		de Duindos (Mon); Lane (Tue); **Lagarde,** de Guindos, Panetta (Wed); Lane, de Guindos (Thu)		
	BoE Speakers:		Mann (Mon); Broadbent (Thu)		
	Fed Speakers:		**Powell,** Harker, Williams, Mester (Mon); Bostic, Schmid, Goolsbee (Thu); Mester, Barkin Daly (Fri)		
Mon 2nd	***IRL:***	***01:01***	***AIB Manufacturing PMI (September)***	***50.8***	
	UK:	07:00	Nationwide House Prices (September)	-0.8% (-5.3%)	-0.4% (-5.8%)
	EU-20:	09:00	Final HCOB Manufacturing PMI (September)	43.4	43.4
	ITA:	09:00	Unemployment Rate (August)	7.6%	7.7%
	UK:	09:30	Final S&P / CIPS Manufacturing PMI (September)	44.2	44.2
	EU-20:	10:00	Unemployment Rate (August)	6.4%	6.4%
	US:	14:45	Final S&P Manufacturing PMI (September)	48.9	48.9
	US:	15:00	Manufacturing ISM (September)	47.6	47.9
Tue 3rd	**US:**	15:00	JOLTS Job Openings Data (August)	8.8m	8.50m
	IRL:	***16:30***	***Exchequer Returns (September)***	***Sept'22 +€7.9bn***	***+€1.0bn***
			-Ex-NRF Transfer		***+€5.0bn***
Wed 4th	***IRL:***	***01:01***	***AIB Services PMI (September)***	***55.0***	
	JPN:	01:30	Final Jibun Composite PMI (September)	51.8	51.8
			- Final Services PMI	53.3	53.3
	ITA:	08:45	HCOB Composite PMI (September)	48.2	48.3
	FRA:	08:50	Final HCOB Composite PMI (September)	43.5	43.5
	GER:	08:55	Final HCOB Composite PMI (September)	46.2	46.2
	EU-20:	09:00	Final HCOB Composite PMI (September)	47.1	47.1
			- Final Services PMI	48.4	48.4
	UK:	09:30	Final S&P / CIPS Composite PMI (September)	46.8	46.8
			- Final Services PMI	47.2	47.2
	EU-20:	10:00	Producer Prices (August)	-0.5% (-7.6%)	+0.6% (-11.6%)
	EU-20:	10:00	Retail Sales (August)	-0.2% (-1.0%)	-0.3%
	IRL:	***11:00***	***Unemployment Rate (September)***	***4.1%***	***4.1%***
	US:	13:15	ADP National Employment (September)	+177,000	+140,000
	US:	14:45	Final S&P Composite PMI (September)	50.1	50.1
			- Final S&P Services PMI	50.2	50.2
	US:	15:00	Factory Orders (August)	-2.1%	+0.2%
			- Durable Goods	+0.2%	+0.2%
	US:	15:00	Non-Manufacturing ISM (September)	54.5	53.6
Thu 5th	**GER:**	07:00	Trade Balance (August)	+$15.9bn	+$15.8bn
			- Exports	-0.9%	-0.1%
	FRA:	07:45	Industrial Output (August)	+0.8%	-0.4%
	US:	13:30	International Trade (August)	-$65bn	-65.1bn
	US:	13:30	Initial Jobless Claims (w/e 18th September)	205,000	210,000
Fri 6th	**GER:**	07:00	Industrial Orders (August)	-11.7%	+1.5
	UK:	07:00	Halifax House Prices (September)	-1.9% (-4.6%)	
	US:	13:30	Non-Farm Payrolls (September)	+187,000	+158,000
			- Unemployment Rate	3.8%	3.7%
			- Average Earnings	+0.2% (+4.3%)	+0.3% (+4.3%)

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