CENTRALNA BANKA CRNE GORE

Financial and Banking Operations Department

- International Reserves Management Division -

International Financial Market Report

3 – 7 October 2022

Podgorica, 12 October 2022

FX NEWS

EUR/USD

Source: Bloomberg LP

The **EUR/USD exchange rate** did not register significant changes on Monday. Still, on Tuesday, it appreciated sharply to 0.9999 due to the euro's appreciation as the price of shares on the European stock exchanges rose significantly due to the gas price drop in the region. On the other hand, the USD depreciated due to weaker-than-expected data on the number of jobs in the USA. The next day, and until the end of the week, the EUR/USD exchange rate depreciated. The USD appreciated due to good US service sector data and the position of San Francisco Fed Chair Mary Daly, who was confident that the market was ready for another big interest rate hike in November. Fed board member Christopher Waller said he expected an additional interest rate hike early next year. Chicago Fed Chair Charles Evans said the key interest rate would range from 4.5% to 4.75% until next spring. On Friday, after the publication of strong data from the US labour market, the exchange rate fell as these data fuelled expectations regarding Fed's interest rate increase in November.

EUR/GBP

Source: Bloomberg LP

In this reporting week, the **EUR/GBP exchange rate** trended between 0.86494 and 0.88312, ending almost the same as early this week (around 0.87800). The exchange rate depreciated sharply on Monday, as sterling appreciated after the UK Chancellor of the Exchequer's statement that he would not seek tax cuts for high earners despite a previous announcement, fuelling expectations of scrapping other proposed tax cuts. However, the exchange rate appreciated from Tuesday. The sterling came under pressure as economists began to lower their forecasts for UK economic growth. On Wednesday, Prime Minister Truss gave a speech at the Conservative Party's annual conference. She explained that she was behind the tax cut plan, dispelling hopes that she would abandon the current fiscal strategy. Even though the final data on the index of the British service sector was better than expected (50 vs 49.2), the index was at its lowest level in the last 19 months, so the sterling depreciated for this reason as well. In addition, the credit agency Fitch reduced the UK's credit outlook from stable to negative, warning about public finances due to the announced tax cuts policy. They stated that the "extensive and unfounded fiscal package" could significantly increase the fiscal deficit in the medium term. On Friday, the exchange rate depreciated briefly, as weaker-than-expected German economic data caused the euro to depreciate, but the appreciation trend continued.

EUR/JPY

Source: Bloomberg LP

This reporting week, the **EUR/JPY exchange rate** had a similar trend as the EUR/USD exchange rate. The EUR/JPY exchange rate appreciated on Tuesday. A BoJ member stated that the bank would have to devise a strategy to leave the ultra-loose monetary policy. Japan's Finance Minister stated he was ready to take serious steps in the currency market in any case. The next day, the EUR/JPY exchange rate depreciated. As a weak yen fuels inflation, Japan will take "unprecedented" measures to curb rising electricity bills for households and businesses. At the same time, fears of a global recession pose significant risks to the economy. Prime Minister Kishida said the government would come up with another economic stimulus plan by the end of October, including a rare measure to mitigate the spike in electricity prices directly, Kishida added. The EUR/JPY exchange rate was volatile on Friday and depreciated during the day. Traders weighed whether Japanese authorities would intervene in the market again as USD/JPY moved closer to its level when officials last intervened. On the other hand, the euro depreciated as the Minutes from the last ECB meeting published on Thursday showed that a recession was "increasingly likely".

Table 1 - Exchange rates of the most important currencies

	03.10.2022[1]	07.10.2022[2]	% Change
EUR/USD	0.9802	0.9744	-0.59
EUR/GBP	0.87751	0.87855	0.12
EUR/JPY	141.88	141.59	-0.20
EUR/AUD	1.53169	1.52872	-0.19
EUR/CHF	0.96740	0.96862	0.13
USD/JPY	144.74	145.250	0.35
GBP/USD	1.1170	1.1086	-0.75

Table 2 - Overview of the reference interest of the leading central banks

Central Bank	Reference interest rate	Reference interest rate level	Next meeting
European Central Bank	ECB main refinancing rate	1.25%	27 October 2022
Federal Reserves	Federal Funds Target Rate	3.25%	2 November 2022
Bank of Japan	Overnight Call Rate	-0.10%	28 October 2022
Bank of England	Official Bank Rate	2.25%	3 November 2022
Swiss National Bank	Libor Target Rate	0.50%	15 December 2022
Bank of Canada	Target Overnight Rate	3.25%	26 October 2022
Reserve Bank of Australia	Cash Rate Target	2.60%	1 November 2022

The Reserve Bank of Australia raised interest rates by 25 basis points, a minor increase than the market expected. That country's central bank decided on a minor increase because the interest rate increased significantly for a short time in the previous period.

Table 3 – ESTR and Euribor

	03.10.2022[1]	07.10.2022[2]	Change in basis points
ESTR	0.6420	0.6560	1.40
Euribor 1W	0.6480	0.6560	0.80
Euribor 1M	0.6790	0.7830	10.40
Euribor 3M	1.1730	1.2880	11.50
Euribor 6M	1.8090	1.8970	8.80
Euribor 12M	2.5560	2.5520	-0.40

[1] Opening market value on Monday
[2] Closing market value on Friday

EUROPEAN GOVERNMENT BONDS MARKET

Source: *Bloomberg LP*

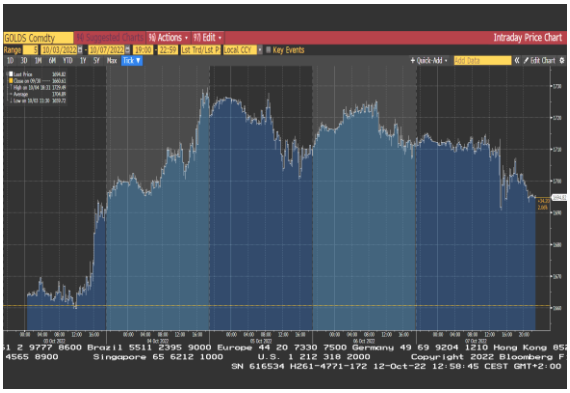
At the very beginning of this reporting period, the return on German 10-year bonds fell after expectations that the ECB would aggressively continue to raise interest rates decreased. At the same time, aggressive interest rate increases by the FED and BoE were not as expected, and the Central Bank of Australia increased the interest rate by only 25 basis points. In the rest of the week, the return on these bonds was constantly growing as the Minutes from the last ECB meeting showed that the central bank would most likely increase the interest rate by 75 basis points at the next meeting. It pushed the return higher throughout this period. At the end of the week, the return on 10-year bonds stood at 2.19%.

US GOVERNMENT BONDS MARKET

Source: *Bloomberg LP*

The return on 10-year US government bonds fell on the first day after announcing that the index measuring production in the US dropped more than forecast, which reduced expectations regarding an aggressive interest rate increase by the FED. During the rest of the week, the return on these bonds rose constantly. The return rise came as the stock market recovered in the USA, and the services index fell less than expected during September. The return rose at the end of the week after announcing that the unemployment rate unexpectedly fell in September in the USA, leaving room for the Fed to make another big interest rate hike. The unemployment rate fell to 3.5%. The return on 10-year US bonds at the end of this period was 3.88%.

GOLD



Source: Bloomberg LP

In the first two days of this reporting week, the gold price rose from 1,660 to around 1,730 USD/oz tr. This sharp growth occurred due to the USD depreciation and the fall in return on US government bonds. The price also increased due to the publication of weaker-than-expected US economic data (construction consumption, ISM production, new orders), which reduced expectations regarding an aggressive Fed interest rate increase. However, as of Wednesday, the price began to retreat from the previously reached 3-week high. The data released that day showed that the US economy remains "resilient" (better than expected data on the trade deficit, S&P service and composite index). Hence, traders began to question the Fed's future interest rate hike. Although the price showed signs of recovery later in the week, the downward trend continued as the Minneapolis Fed chairman said that the US monetary authorities had "more work to do" to reduce inflation. They also said that the moment when they would pause the policy of aggressive interest rate increases was "far from over". Chicago Fed chair said the bank must continue with the interest rate increase, which will probably be in the range of 4.5% to 4.75% by the next spring. The price also weakened on Friday due to the publication of stronger-than-expected data from the US labour market (unexpected drop in the unemployment rate, higher than expected growth of payrolls in the non-manufacturing sector). At the weekly level, gold price still increased due to the growth at the beginning of the week.

OIL

Source: Bloomberg LP

Oil price trended up during this reporting week. The focus of the market this week was the OPEC+ meeting and expectations that this group would cut production by 1 million bbl./day, which caused the price to rise. In response to the meeting, OPEC+ announced that it was considering reducing production by more than the mentioned amount. Due to the significant market uncertainty, at the Wednesday meeting, OPEC+ agreed to reduce daily output by as much as 2 million barrels, which will begin to apply in November. It is the most significant output reduction since the occurrence of the coronavirus in 2020. Namely, the demand outlook has worsened, and the price has been falling almost constantly since June. Later in the week, the API (American Petroleum Institute) and EIA (Energy Information Administration) published reports showed that oil stocks in the US fell in the week preceding this reporting period, which additionally caused this fuel's price to rise until the end of the week.

Table 4 – Economic indicators (3 – 7 October 2022)

Current value	Indicator	Period	Expected value	Current value	Previous value
Euro area	**Producer Price Index (PPI)** This index measures changes in sale prices of goods and services used by producers in the euro area. High PPI, together with the high value of other inflation indicators, will force the ECB to strive for an increase in interest rates, while declining PPI may indicate an economic slowdown.	August MoM% YoY%	5.0% 43.2%	5.0% 43.3%	4.0% 37.9%
	Retail Sales This indicator measures changes in retail sales in Japan.	August MoM% YoY%	-0.3% -1.7%	-0.3% -2.0%	0.3% -0.9%
Germany	**Retail Sales** This indicator measures changes in retail sales in Japan.	September MoM%	-1.2%	-1.3%	1.9%
	Factory Orders Factory orders provide a rather comprehensive overview of the manufacturing sector.	August MoM%	-0.7%	-2.4%	-1.1%
France	**Industrial output** It measures the changes in output of production, service and mining sectors.	August MoM% YoY%	0.0% -1.5%	2.4% 1.2%	-1.6% -1.2%
Great Britain	**S&P Global/CIPS UK Services PMI** The index was compiled based on responses to questionnaires sent as a panel to 650 companies from the service sector. Sectors covered include retail (except retail), transportation, information, communications, finance, insurance, real estate and business services. Data collection began in July 1996. Answers are collected in the second half of each month and indicate the direction of changes compared to the previous month. A score above 50 indicates that the services sector is generally expanding, while a score below 50 indicates its general decrease.	September	49.2	50.0	49.2
USA	**Initial Jobless Claims** This indicator measures the number of people receiving unemployment allowances.	24 September K=1,000	204 K	219 K	193 K
	Unemployment Rate The percentage of individuals on the labour market and unemployed, but actively looking for a job. In general, higher unemployment rate weakens the economy and results in lower personal spending.	September	3.7%	3.5%	3.7%
	ISM Service Index This composite index consists of 4 indicators: business activity, new orders, employment, and inventory deliveries. The index value above 50.0 points to expansion, while the one below 50.0 points to a contraction in the non-productive sector.	September	56.0	56.7	56.9

Source: Bloomberg