CENTRALNA BANKA CRNE GORE

Financial and Banking Operations Department

- International Reserves Management Division -

International Financial Market Report

(28 March – 1 April 2022)

Podgorica, 7 April 2022

FX NEWS

EUR/USD

Source: *Bloomberg LP*

At the beginning of the week, the **EUR/USD exchange rate** fluctuated (the average exchange rate was around 1.1003). The USD appreciated due to growing concerns about Russia-Ukraine relations and its economic impact on Europe. Credit agency S&P Global has cut its euro area growth forecast for this year from 4.4% to 3.3%, expecting that high energy prices due to the war in Ukraine would hit household consumption. On Tuesday afternoon, the exchange rate appreciated. The negotiations between Russia and Ukraine in Istanbul did not result in an agreement but "paved" the way for the first face-to-face meeting between the warring parties' presidents, reducing the demand for USD. Russia promised to reduce military operations in the Kyiv area. On Wednesday, the exchange rate continued to appreciate as the euro advanced after unexpectedly high inflation data from Germany and Spain. Traders raised expectations that the ECB would raise rates after inflation data from the region, even as President Christine Lagarde pointed to the gradual policy tightening. Encouraging data on consumer confidence in the US for March indicated that Americans estimate that the situation in the economy is improving, which briefly cast a shadow over the war in Ukraine and inflation, reducing the demand for safer funds. The euro depreciated against the USD the next day after the Russian president said Russia would stop gas contracts if customers did not pay for them in RUB. The euro also depreciated due to German retail sales data that did not meet expectations. At the end of the week, the EUR/USD exchange rate depreciated due to the USD appreciation as rising return on US government bonds and a solid US labour market report boosted Fed's interest rate increase expectations.

EUR/GBP

Source: *Bloomberg LP*

The **EUR/GBP exchange rate** appreciated during the first three days of this reporting period. During the mentioned period, the exchange rate's appreciation occurred after media reports that Russia and Ukraine's representatives made slight progress in the peace negotiations. The exchange rate appreciation also resulted from the news that inflation rose in Germany by 7.6% in March, raising expectations that the ECB would start raising interest rates this year. On Thursday, this exchange rate depreciated after announcing that the UK economy's volume increased more than expected in 2021 Q4 (quarterly growth of 1.3% and 6.6% y-o-y). In addition, the European Commission's announcement that it will impose new sanctions on Russia made the euro depreciate. The EUR/GBP exchange rate did not change significantly on Friday.

EUR/JPY

Source: *Bloomberg LP*

On Monday, the **EUR/JPY exchange rate** rose throughout the day as stock prices rose, and traders "weighed" the consequences of different monetary policies pursued in the USA and Japan. On Wednesday, the exchange rate depreciated as the yen rose due to falling return on US government bonds and oil prices. On Wednesday, the EUR/JPY exchange rate depreciated in the morning before rising in the afternoon as the BoJ intervened to keep interest rates on bonds below the target level to maintain the ultra-loose monetary policy in contrast to most other central banks. The next day, the yen made up for part of the losses as the BoJ pledged to increase planned bond purchases in the second quarter of this year and signalled it would continue to aggressively defend the return cap from a higher global interest rates tide. On Friday, the EUR/JPY exchange rate appreciated as the yen depreciated due to falling stock prices on Asian stock exchanges. A Tankan BoJ survey published on Friday showed that business confidence in Japan weakened in Q1 for the first time in almost two years. It happened due to growing concerns about the impact of the Russian invasion of Ukraine and rising energy costs on the economy.

Table 1 - Exchange rates of the most important currencies

	28.03.2022[1]	01.04.2022[2]	% Change
EUR/USD	1.0983	1.1043	0.55
EUR/GBP	0.83312	0.84204	1.07
EUR/JPY	134.04	135.30	0.94
EUR/AUD	1.46139	1.47311	0.80
EUR/CHF	1.02202	1.02284	0.08
USD/JPY	122.05	122.52	0.39
GBP/USD	1.3182	1.3114	-0.52

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

Central Bank	Reference interest rate name	Reference interest rate level	Next meeting
European Central Bank	ECB main refinancing rate	0.00%	14 April 2022
Federal Reserves	Federal Funds Target Rate	0.50%	4 May 2022
Bank of Japan	Overnight Call Rate	-0.10%	28 April 2022
Bank of England	Official Bank Rate	0.75%	5 May 2022
Swiss National Bank	Libor Target Rate	-0.75%	16 June 2022
Bank of Canada	Target Overnight Rate	0.50%	13 April 2022
Reserve Bank of Australia	Cash Rate Target	0.10%	5 April 2022

Table 3 – ESTR and Euribor

	28.03.2022[1]	01.04.2022[2]	Change in basis points
ESTR	-0.581	-0.5949	-1.39
Euribor 1W	-0.561	-0.564	-0.30
Euribor 1M	-0.546	-0.541	0.50
Euribor 3M	-0.477	-0.461	1.60
Euribor 6M	-0.392	-0.362	3.00
Euribor 12M	-0.142	-0.086	5.60

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

EUROPEAN GOVERNMENT BONDS MARKET

Source: *Bloomberg LP*

The return on 10-year German government bonds fell about 4 basis points from 0.595% to 0.555% this week. Although it depreciated slightly at the beginning of the week, the return grew on Tuesday to 0.732%, the maximum for this week. Negotiations between Russia and Ukraine caused a decreased demand for safe funds leading to increased return. Although it depreciated to 0.60% the same day, it again stood above 0.70% in the middle of the week. At the same time, the return on 2-year German government bonds briefly entered the positive zone, rising to 0.062% for the first time since 2014. The news leading to this trend was the inflation rise to 9.8% in Spain in March, the highest rate since 1985, while inflation of 7.3% in Germany reached its peak in 40 years. Another reason for the return increase was the Russian spokesperson's statement that Russia had no plans to suspend negotiations with Ukraine. At the end of Wednesday, the return began to fall, as ECB's board member Madis Müller said it was too early to tell whether the interest rate would hike this year, but it is "probable". This trend continued the next day, when the 10-year return fell to 0.525%, reaching the minimum value for this week due to lower market expectations of the ECB rate increase as falling energy prices weakened inflation indicators. On Friday, the return fluctuated but without significant daily changes.

US GOVERNMENT BONDS MARKET

Source: *Bloomberg LP*

This reporting week, the return on 10-year US government bonds fell from 2.47% to 2.38%. The return reached its maximum value of 2.55% on Monday, but it soon began to drop. Negotiations between Russia and Ukraine caused a decreased demand for safe funds. Thus, this return was growing again at the beginning of Tuesday. However, a downward return trend prevailed for the rest of the week. The optimism about Russia and Ukraine and expectations that the US President would announce a plan to reduce the rising energy prices impact caused falling oil prices and inflationary measures expectations. The return rose slightly on Friday, following a favourable US labour market data release, which boosted expectations regarding the Fed's interest rate increases. Namely, employers created 431 thousand new jobs in March, less than expected. At the same time, the February data were revised upwards, while the inflation rate fell from 3.7% to 3.6%. The return on 2-year bonds reached a 3-year high of 2.45% on that day. This week, the US bond market was characterised by the inversions of some return curve parts. On Monday, 5-year returns briefly exceeded 30-year return, the first inversion of this part of the curve since 2006. The same happened on Tuesday, Thursday and Friday, with the then 2-year returns also briefly exceeding the 10-year return for the first time since 2019. Historically, return curve inversions preceded the recession. However, economists pointed out that this indicator did not guarantee a recession. It could take more than a year, some say up to two years, from return curve inversion to economic deterioration. In addition, some neutral market observers warn that this signal could now be less accurate, given the return disturbances caused by central banks' measures to keep interest rates low.

GOLD

Source: Bloomberg LP

The gold price fell on Monday. It declined as the USD appreciated against a basket of currencies, reducing demand for this precious metal. On Tuesday morning, the gold price dropped as the media reported slight progress in the Russia-Ukraine negotiations, reflected in the declined demand for safe funds. However, the USD appreciated against most currencies on Tuesday afternoon. In the middle of the week, the gold price continued to rise after increasing concerns about whether the Russia-Ukraine conflict would end. The same reason influenced the gold price to increase on Thursday. On Friday, positive US payrolls growth data by 431 thousand caused the gold price to drop slightly.

OIL

Source: Bloomberg LP

The oil price decreased this week. The price fell as China imposed additional restrictions due to the coronavirus spread. The oil price rose slightly in the middle of the week after the increased possibility that Western countries would impose new sanctions on Russia. However, the oil price downward trend soon continued as the USA announced the largest ever release of crude oil from national reserves. In contrast, OPEC and its allies would stick to a previous agreement to increase production in May. Biden's strategic reserves release objective was to create a bridge for US supplies by autumn when domestic production is projected to grow, the White House said.

Table 4 - Economic indicators (28 March – 1 April 2022)

Current value	Indicator	Euro area	Expected value	Current value	Previous value
Euro area	**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. **Consumer price index (CPI)** It estimates the cost of living changes by measuring changes in the price level of market basket of consumer goods and services purchased by an average household. Therefore, it is the key inflation measure in the euro area.	February March MoM%	6.7% 1.8%	6.8% 2.5%	6.8% 0.9%
Germany	**Consumer price index (CPI)** It estimates the cost of living changes by measuring changes in the price level of market basket of consumer goods and services purchased by an average household. Therefore, it is the key inflation measure in the euro area. **Retail Sales** This indicator measures changes in retail sales in Germany.	March MoM% (YoY%) February MoM%	1.6% (6.2%) 0.5%	2.5% (7.3%) 0.3%	0.9% (5.1%) 2.0%
Spain	**Consumer price index (CPI)** It estimates the cost of living changes by measuring changes in the price level of market basket of consumer goods and services purchased by an average household. Therefore, it is the key inflation measure in the euro area.	March MoM% (YoY%)	1.3% (8.0%)	3.0% (9.8%)	0.8% (7.6%)
France	**Consumer price index (CPI)** It estimates the cost of living changes by measuring changes in the price level of market basket of consumer goods and services purchased by an average household. Therefore, it is the key inflation measure in the euro area.	March MoM% (YoY%)	1.3% (4.3%)	1.4% (4.5%)	0.8% (3.6%)
USA	**Unemployment Rate** It shows the total percentage of those considered unemployed in the United States. Given that the Fed must keep unemployment under control, its high rate puts pressure on interest rates (in terms of their reduction), as the Fed will then seek ways to improve the situation on the labour market.	March	3.7%	3.6%	3.8%
Great Britain	**Gross domestic product (GDP)** It measures the value of products and services produced inside the country. GDP is the most comprehensive measure of economic output and provides a key insight into the main drivers of an economy.	Q4 QoQ% (YoY%)	1.0% (6.5%)	1.3% (6.6%)	1.0% (6.5%)
Japan	**Retail Sales** This indicator measures changes in retail sales in Japan.	February	-0.3%	-0.8%	-1.9%

Source: Bloomberg