CENTRALNA BANKA CRNE GORE

Financial and Banking Operations Department

- International Reserves Management Division -

International Financial Market Report

(11 – 15 September 2023)

Podgorica, 20 September 2023

FX NEWS

EUR/USD

The **EUR/USD exchange rate** fluctuated during the first three days, averaging 1.0735. The market was waiting for the US inflation data for August (Wednesday), which could influence the Fed's interest rate trend and the ECB meeting (Thursday). On Wednesday, the USD depreciated after releasing that core inflation in the US rose more than expected in August, while headline inflation rose in line with forecasts. The EUR/USD exchange date depreciated the next day to its lowest level since 20 March (1.0632) as the euro depreciated on the prospect that the ECB's interest rate hike was the last in this cycle. On the other hand, the USD was supported by published economic data (higher-than-expected growth in retail sales and the production prices index). At the end of the week, the EUR/USD exchange rate appreciated with minor fluctuations, as the USD depreciated after traders kept a bit aside awaiting the Fed meeting..

EUR/GBP

The **EUR/GBP exchange rate** depreciated for most of Monday, as the sterling depreciated, expecting the BoE to raise interest rates and the UK labour market report. The sterling depreciated against the euro the next day following the release of data on a faster-than-expected slowdown in the UK economy. In Great Britain, GDP data for July showed a 0.5% decrease compared to the expected one of 0.2%. The economy's slowdown resulted from higher interest rates and falling house prices, while the cold and wet weather during July influenced the weaker results of retail sales that month. In the middle of the week, the market expected the BoE to increase the interest rate in September (there were 70% odds of increasing the interest rate by 25bp). On the other hand, it is closely monitored whether the economy's slowdown, which can be attributed to higher interest rates, will continue rates and persistent inflation. The EUR/GBP exchange rate appreciated on Thursday morning, awaiting the ECB meeting. After the meeting, the exchange rate started to depreciate, remaining a trend until the evening due to the euro's depreciation. The EUR/GBP exchange rate appreciated on Friday as recent data showed that the UK economy was slowing down and the labour market was "losing strength".

EUR/JPY

The **EUR/JPY exchange rate** depreciated sharply on Monday as the yen appreciated, expecting the BoJ to end its negative interest rate policy. However, the exchange rate started to rise soon and maintained such a trend until the end of the day, resulting in the exchange rate remaining almost unchanged daily. The next day, the yen depreciated against the euro and the USD as investors awaited key US inflation data. The EUR/JPY exchange rate depreciated on Thursday due to the euro's depreciation that followed the ECB's decision. On Friday, the exchange rate appreciated after the BoJ officials said they must carefully "weigh" positive and negative risks in deciding whether to adjust monetary policy. The yen also depreciated on Friday after the BoJ report showed officials saw a divergence of opinion between what BoJ Governor Kazuo Ueda said in a recent interview and how traders interpreted it. Ueda fuelled speculation that the bank was moving away from ultra-easy policies.

Table 1 - Exchange rates of the most important currencies

	11.09.2023[1]	15.09.2023[2]	% Change
EUR/USD	1.0700	1.0657	-0.40
EUR/GBP	0.85821	0.96072	11.94
EUR/JPY	158.20	157.58	-0.39
EUR/AUD	1.67815	1.65632	-1.30
EUR/CHF	0.95567	0.95689	0.13
USD/JPY	147.83	147.85	0.01
GBP/USD	1.2468	1.2383	-0.68

Table 2 - Overview of the leading central banks' interest rates

Central Bank	Reference interest rate	Reference interest rate level	Next meeting
European Central Bank (ECB)	ECB main refinancing rate	4.50%	26 October 2023
Federal Reserves (Fed)	Federal Funds Target Rate	5.50%	20 September 2023
Bank of Japan (BoJ)	Overnight Call Rate	-0.10%	22 September 2023
Bank of England (BoE)	Official Bank Rate	5.25%	21 September 2023
Swiss National Bank (SNB)	Libor Target Rate	1.75%	21 September 2023
Bank of Canada (BoC)	Target Overnight Rate	5.00%	25 October 2023
Reserve Bank of Australia (RBA)	Cash Rate Target	4.10%	3 October 2023

Intending to speed up the return of inflation to the 2% target, the ECB decided at its meeting to increase the key interest rates by 25 basis points each, so the reference interest rate now stands at 4.50%, the deposit rate at 4%, and the overnight rate on loans at 4.75%. These rates will apply from 20 September. According to the ECB's September forecast, the average inflation for 2023 and 2024 has been revised upwards, mainly due to energy prices, so that it now amounts to 5.6% and 3.2%, respectively, while the inflation for 2025 has been revised downwards and amounts to 2.1%. Projections for economic growth were lowered to 0.7% (2023), 1% (2024) and 1.50% (2025). The Council will continue to follow a data-driven approach to determine the appropriate level of interest rates and the length of the "restrictive period".

Table 3 – ESTR and Euribor

	11.09.2023[1]	15.09.2023[2]	Change in basis points
ESTR	3.6530	3.6500	-0.30
Euribor 1W	3.659	3.690	3.10
Euribor 1M	3.682	3.762	8.00
Euribor 3M	3.800	3.878	7.80
Euribor 6M	3.952	4.055	10.30
Euribor 12M	4.086	4.169	8.30

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

EUROPEAN GOVERNMENT BONDS MARKET

This reporting week, the return on 10-year German government bonds rose from 2.64% to 2.68%. The return was stable for the first two days, but it started to rise from Tuesday afternoon. Namely, on that day, it was announced that ECB experts expected the euro area inflation rate to remain high next year (above 3%), which increased expectations that the tenth consecutive interest rate increase could occur at the meeting on Thursday. The return had a downward trend on Wednesday afternoon and the next day. Although the ECB increased the interest rate by 25 basis points as expected, investors' expectations that this monetary institution will start reducing interest rates in the next year have increased. Towards the end of the week, the return increased awaiting the Eurogroup meeting and, as ECB President Lagarde told reporters after the meeting, the interest rate reduction was not discussed at the ECB meeting. An ECB Governing Council member Vasle stated that further interest rate increases cannot be ruled out and that the APP programme reduction could accelerated. At the same time, his colleague, Müller, believed that higher inflation could justify another interest rate increase.

US GOVERNMENT BONDS MARKET

On Monday and Tuesday, the return on the 10-year US Government bonds fluctuated between 4.26% and 4.30%, as investors maintained a cautious approach ahead, awaiting economic data that could impact the Fed's thinking on how much further monetary policy tightening was needed to bring inflation back to the targeted level. The first significant change occurred on Wednesday when it rose to 4.34% in response to US inflation rate data for August. On the same day, the return dropped by 9 basis points. Although the US consumer price index showed prices rose in August at the fastest monthly rate in 14 months due to rising energy prices, core inflation excluding energy and food prices continued to slow, bolstering expectations that the Fed would leave interest rates unchanged at the September meeting. Better-than-expected economic data published by the end of the week (production prices, retail sales), along with rising oil prices, increased expectations that inflation would be stable, which caused a rise in the return in this market by the end of the week. At the very end of the week, the return on 10-year bonds stood at 4.33%.

GOLD

Early this week, the gold price rose due to the USD depreciation. However, this precious metal's price soon fell, maintaining such a trend until Thursday afternoon. The USD depreciation initiated the downward trend, also influenced by awaiting the US inflation data. After publishing inflation slightly higher than expectations, the gold price weakened. The release of better-than-expected data on US producer prices and retail sales also caused the price drop. On Thursday, the price was at a 3-week low, the level that attracted investors, so the price started to recover. By the end of the week, the price rose due to the expectation that the Fed would finish increasing the interest rate, but also as solid Chinese economic data were published (higher-than-expected growth of industrial production and retail sales). The growth also occurred due to increased demand for safe assets due to the Detroit auto industry strike.

OIL

In this reporting week, the oil price rose for the third consecutive week, reaching a 10-month high on Friday. Concerns about supply, primarily due to production cuts by Saudi Arabia and Russia (a total of 1.3 million bbl./day) that will be in effect until the end of the year, mainly affected the trend. The growth was also caused by the publication of better-than-expected Chinese economic data, and the economic conditions in this country were considered crucial for the demand for oil until the end of this year. The price showed declining signs in the middle of the week as the US Government's report showed that oil stocks in the US increased by 4 million barrels in the week preceding this reporting period, twice as much as expected. At the end of the week, the International Energy Agency and OPEC warned that the market would be in deficit at the end of the year.

Table 4 - Economic indicators (11 – 15 September 2023)

Country	Indicator	Period	Expected value	Current value	Previous value
Germany	**ZEW Survey Expectations** This survey measures expectations regarding the economic growth for the next 6 months. Experts are surveyed on whether they expect an improvement or deterioration, thus the difference between the number of positive and negative responses represents the indicator value.	September	-15.0	-11.4	-12.3
Euro area	**ECB Main Refinancing Rate** A central bank sets this target interest rate to influence short-term interest rates as part of its strategy.	14 September	4.25%	4.50%	4.25%
Great Britain	**Monthly GDP** It measures the final market value of all products and services produced within the country monthly.	July MoM%	-0.2%	-0.5%	0.5%
	Industrial output It measures the output of the energy sector, factories and mines. This indicator is significant in the short term as it shows the UK industrial activity's strength. Growing industrial output points to increased production and economic expansion, which is "healthy" for the sterling.	July MoM% YoY%	-0.7% 0.4%	-0.7% 0.4%	1.8% 0.7%
USA	**CPI ex Food & Energy** It estimates changes in the cost of living, measuring changes in the goods and services' prices, excluding food and energy. This index measures the change in prices from the consumer's perspective. It is a key way of measuring changes in buying trends and inflation.	August MoM% YoY%	0.2% 4.3%	0.3% 4.3%	0.2% 4.7%
	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.	August MoM% YoY%	0.6% 3.6%	0.6% 3.7%	0.2% 3.2%
	Initial Jobless Claims It measures the number of people filing for unemployment benefits for the first time.	9 September K=1,000	225K	220 K	216 K
Japan	**Producer Price Index (PPI)** This indicator measures the change in the price paid by domestic producers. The indicator rise is an early inflation indicator.	August MoM% YoY%	0.2% 3.3%	0.3% 3.2%	0.1% 3.6%