CENTRALNA BANKA CRNE GORE

Financial and Banking Operations Department

- International Reserves Management Division -

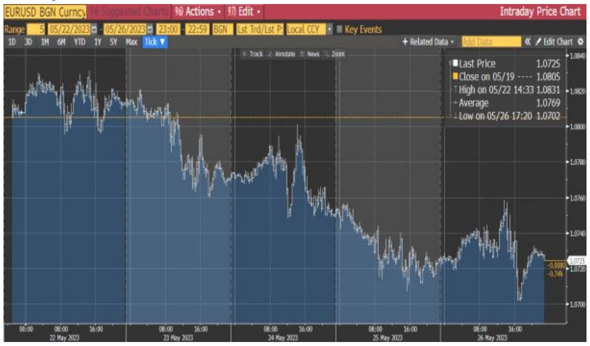
International Financial Market Report

(22 – 26 May 2023)

Podgorica, 31 May 2023

FX NEWS

EUR/USD



This reporting week, the **EUR/USD exchange rate** depreciated from 1.0831 to 1.0702. On Monday, the exchange rate fluctuated slightly and averaged 1.0804. The following day, it depreciated after publishing preliminary data that output activity in the euro area decreased in May, indicating negative economic trends. In the rest of the week, the USD appreciated due to indications that the US economy was resilient and resulting from the growing demand for safe funds because the agreement on the borrowing limit in the USA was still not reached. Credit agency Fitch put the US's AAA rating on "negative watch". Fitch warned on Wednesday that the USA's AAA rating could downgrade if no agreement is reached to raise the national borrowing limit before the Treasury runs out of money to pay the obligations (significant payment obligations are due in early June). On Thursday, the EUR/USD exchange rate fell, expecting an imminent agreement to raise the US borrowing limit. It was also predicted that the Fed would continue with the interest rates rising policy in July and remain high for longer. At the very end of the week, the EUR/USD exchange rate first appreciated to depreciate later. The USD appreciated as the PCE deflator beat expectations, adding pressure on the Fed to raise interest rates.

EUR/GBP

At the weekly level, the **EUR/GBP exchange rate** appreciated. The Chancellor of the Exchequer's chief adviser, Jeremy Hunt, said the BoE should stop raising interest rates because it risked "stifling" Britain's economic recovery. The Chancellor's adviser suggested that the BoE's approach could have an adverse impact on growth, even putting Britain on the course for recession, and added that the BoE could afford more time to bring inflation back on target to keep the economy moving and opening up new jobs. The former BoE Chief Economist Andy Haldane said it was time to "press pause" after 12 consecutive interest rate hikes, warning of the consequences for mortgage holders due to rate hikes. Later, the exchange rate depreciated after releasing data on the production index in the euro area. Despite data showing UK inflation was higher than expected, EUR/GBP rose on Wednesday as sterling depreciated amid investor concerns that high inflation and interest rates would cause the economy to contract. The next day, the EUR/GBP exchange rate depreciated until noon due to BoE Committee member Jonathan Haskell's statement that future interest rate increases could not be ruled out yet. However, the exchange rate returned to its previous level in the afternoon. At the end of the week, the EUR/GBP exchange rate depreciated after announcing that retail sales in the UK increased by 0.8% in April, more than expected (0.4%). Despite ongoing inflationary pressures, consumer spending showed resilience, most likely because it was supported by wage growth. However, analysts warn that future unemployment increases could weaken consumer confidence.

EUR/JPY

The **EUR/JPY exchange rate** recorded weekly appreciation. Early this week, demand for the yen was subdued due to an unexpected factory orders drop in March in Japan. The next day, the exchange rate depreciated as the yen recovered due to the announcement that the composite PMI index in Japan rose from 52.9 to 54.9 in April. The demand for safe funds was also current due to the market participants' focus on negotiations to raise the borrowing limit in the USA. At the end of the week, the EUR/JPY rate rose due to the divergence in monetary policies led by the BoJ and the ECB. The BoJ Governor reiterated that he would continue with monetary easing. On Friday, the EUR/JPY exchange rate had an upward trend towards reaching an agreement between US President Biden and the House of Representatives Speaker Kevin McCarthy on the US debt ceiling.

Table 1 - Exchange rates of the most important currencies

	22.05.2023[1]	26.05.2023[2]	% Change
EUR/USD	1.0805	1.0723	-0.76
EUR/GBP	0.86812	0.8865	2.12
EUR/JPY	148.99	150.84	1.24
EUR/AUD	1.62450	1.64547	1.29
EUR/CHF	0.97213	0.97075	-0.14
USD/JPY	138.55	140.60	1.48
GBP/USD	1.2445	1.2344	-0.81

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

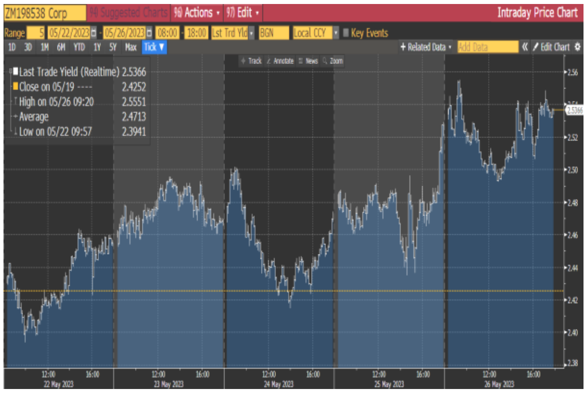
Central Bank	Reference interest rate	Reference interest rate level	Next meeting
European Central Bank (ECB)	ECB main refinancing rate	3.75%	15 June 2023
Federal Reserves (Fed)	Federal Funds Target Rate	5.25%	14 June 2023
Bank of Japan (BoJ)	Overnight Call Rate	-0.10%	16 June 2023
Bank of England (BoE)	Official Bank Rate	4.50%	22 June 2023
Swiss National Bank (SNB)	Libor Target Rate	1.50%	22 June 2023
Bank of Canada (BoC)	Target Overnight Rate	4.50%	7 June 2023
Reserve Bank of Australia (RBA)	Cash Rate Target	3.85%	6 June 2023

Table 3 – ESTR and Euribor

	22.05.2023[1]	26.05.2023[2]	Change in basis points
ESTR	3.151	3.118	-3.28
Euribor 1W	3.129	3.125	-0.40
Euribor 1M	3.134	3.199	6.50
Euribor 3M	3.415	3.462	4.70
Euribor 6M	3.707	3.760	5.30
Euribor 12M	3.878	3.955	7.70

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

EUROPEAN GOVERNMENT BONDS MARKET



The return on 10-year German government bonds increased with minor weekly fluctuations, from 2.39% on Monday to 2.54% at the market close on Friday. According to current information, the money market has already calculated the increase in the ECB's deposit rate, which will peak in September this year. ECB Governing Council member François Villeroy de Galhau stated that the ECB would reach the maximum interest rate level at the following three meetings. However, this does not mean that it will increase the interest rate at each meeting. He pointed out that once that level was reached, the ECB would maintain that level of interest rates for longer. At the same time, another ECB Governing Council member said that the course interest rate increasing trend by that central bank was still not over and that several more interest rate increases are needed to reach a sufficiently restrictive interest rates level.

US GOVERNMENT BONDS MARKET

The return on the 10-year US government bond trended up during most of the reporting week. Fed officials predicted two more possible benchmark interest rates increases, assuming that Fed interest rates would peak this July. The return on 10-year bonds rose by 5 basis points on Monday after these expectations, reaching 3.72%, representing the highest level since 13 March this year. At the end of the day on Tuesday, the return fell slightly as investors turned their focus to negotiations on the US debt limit raising. In the rest of the week, the return on US government bonds continued to rise due to the publication of the Minutes from the last Fed meeting, which caused a weakening of market participants' expectations concerning the interest rate reduction this year. On Friday, the return on 10-year US government bonds reached 3.86%, representing the weekly maximum.

GOLD

The gold price fell during this reporting week, while the USD appreciated. The upper limit of the US debt and the prospect of an interest rate increase by the FED at the June meeting put pressure on the gold price. Investors were weighing the prospects for a US debt ceiling deal and watching the US dollar to gauge demand for gold. US President Joe Biden and the House of Representatives Speaker Kevin McCarthy expressed their belief that their framework agreement will pass the Congress, which will be voted on 31 May.

OIL

During the first three days of this reporting week, the oil price trended up due to Saudi Arabia's warning that OPEC+ could reduce the production volume at the June meeting. This fuel price increase was additionally influenced by the publication of data by the US Government that oil stocks in the US have dropped significantly. On Thursday, the oil price fell after Russia suggested that OPEC+, which contradicts the announcements of some other organisation members, most likely will not change the oil production level at the next (June) meeting. Oil prices rose on Friday as investors followed the progress of negotiations in the USA, which relate to the country's indebtedness level to avoid the default.

Table 4 - Economic indicators (22 - 26 May 2023)

Country	Indicator	Period	Expected value	Current value	Previous value
Euro area	**Consumer Confidence** An assessment of consumer confidence in terms of business conditions, employment and personal income. The Consumer Confidence Index is tied to personal consumption.	May	-16.8	-17.4	-17.5
	PMI Manufacturing PMI surveys tracks opinion among managers at manufacturing, construction and/or services firms.	May P P=preliminary	46.0	44.6	45.8
Germany	**IFO Business climate** It refers to a survey of German companies on the current conditions (state) of business in Germany, and their expectations for the next six months.	May	93.0	91.7	93.6
	GDP Seasonal Adjustments (GDP SA) One of the basic macroeconomic indicators, which represents the calculated value in the market prices of goods and services produced within the country, but excludes the income of citizens and corporations working abroad.	Q1	0.0%	-0.3%	0.0%
	GfK Consumer Confidence This index measures the level of households' confidence in terms of economic performance.	June	-24.0	-24.2	-25.7
USA	**Michigan Consumer Sentiment Index** It is a monthly survey of US consumer confidence conducted by the University of Michigan. The survey is based on telephone interviews collecting information about consumer expectations from the economy.	May	58.0	59.2	57.7
	PCE Core Deflator An economic indicator measures inflation by tracking changes in the prices of goods and services purchased by US consumers, excluding food and energy costs.	April MoM% YoY%	0.3% 4.6%	0.4% 4.7%	0.3% 4.6%
	Initial Jobless Claims This indicator measures the number of people receiving unemployment allowances. Similar to the applicant, the growing number of jobs is accompanied by an economic expansion that could influence inflationary pressures.	May 20 K=1,000	245 K	229 K	242 K
Japan	**Machinery orders** The indicator reflects the investments of companies and business activities. It is compiled from 300 industrial manufacturers.	March MoM%	0.4%	-3.9%	-4.5%
Great Britain	**Retail Sales** This indicator measures changes in retail sales in the UK.	April MoM%	0.4%	0.8%	-1.0%
	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.	April MoM% YoY%	0.7% 8.2%	1.2% 8.7%	0.8% 10.1%