CENTRALNA BANKA CRNE GORE

Financial and Banking Operations Department

- International Reserves Management Division -

International Financial Market Report

(10 - 14 June 2024)

Podgorica, 19 June 2024

Weekly overview of short news

- After the European parliamentary elections, held from 6 to 9 June, the tremors caused by the results are still echoing across the continent, as some of Europe's most prominent leaders have suffered failure.
- It is noticeable that right-wing and extreme right-wing parties achieved significant success. In France, for instance, President Macron's party won 14.6% of the vote, while far-right Marine Le Pen's party, which campaigned against immigration, won 31.3% of the vote. These results prompted French President Macron to call for early parliamentary elections for 30 June. He aims to prevent the far right from gaining power and has called on political leaders to build a coalition that will govern and act in the service of France. Macron has promised to take a tougher stance on issues such as immigration, security and the judiciary.
- The Social Democrats in Germany also suffered setbacks. Chancellor Olaf Scholz suffered his worst E.U. election result in history. Right-wing parties in Germany won more than 45% of the vote.
- The Italian Prime Minister, Giorgia Meloni, and her right-wing party won 28.7% of the vote.
- The European People's Party, headed by Ursula von der Leyen, won the most seats in the European Parliament. Liberal and green parties suffered significant losses.
- Despite significant wins and losses, neither of the sides emerged with an overall majority in the European Parliament. Consequently, the leaders are now engaged in negotiations to form coalitions that will form the balance of power in Brussels.
- New elections in France incite political uncertainty. There is no clear winner this week on the foreign exchange market between the two most important global currencies, the euro and the dollar. After the dissolution of the National Parliament in France, spread between French and German 10-year yields saw an increase. The spread widened by 29 basis points, to 77 bp, which is the highest level since 2017.
- Reports from the U.S. labour market for May partially give a contradictory picture. Earlier in the week, unexpectedly strong U.S. job growth in May hinted that the Federal Reserve may delay cutting interest rates until September, unlike recent cuts by the ECB and the Bank of Canada. In the U.S. non-manufacturing sector, the number of employees increased by 272,000 instead of the expected 180,000, while the private sector saw an increase by 229,000 instead of 165,000. On the other hand, the data released at the end of the week show that the initial jobless claims increased in the USA by 242 thousand on a weekly basis, which is more than the expected by 225 thousand.
- Inflation in the U.S. surprisingly slowed down from 3.4% to 3.3% in May.
- The Federal Reserve left its key rate unchanged at its two-day meeting, repeating for the seventh time in a row that it will take more time to gain confidence that inflation will return to 2%. The updated economic projections of policymakers (The Summary of Economic Projections - SEP is updated four times a year), released after a two-day meeting in Washington, showed that interest rate cuts are expected to occur only once in 2024 instead of the previously announced three times in March. More decrease is forecast for 2025, reinforcing calls from policymakers to keep borrowing costs at higher levels for longer to curb inflation.
- The Bank of Japan kept the interest rate at the current level and stated that it will reduce the bond purchase programme, but did not provide more details on this matter, and will announce additional details at the next meeting of the central bank.
- The World Bank sees increasing chances for a "soft landing" of the global economy, despite ongoing geopolitical tensions and high interest rates. The global GDP growth forecast for 2024 increased from 2.4% to 2.6%. Growth rates for 2025 and 2026 are expected to reach 2.7%.
- The European Commission is imposing penalty duties on imports of Chinese electric cars, which will take effect as of 4 July. However, it is considered that the EC is harming European interests and European companies in this way, as most of the automobile industry rejects these tariffs, for fear of retaliation. The negative effects of this decision outweigh any potential benefits for the European and especially the German automobile industry.

FX NEWS

EUR/USD

The EUR/USD exchange rate recorded a drop during the first two days of this week. The exchange rate fell because the result of the right-wing parties in the European elections over the weekend influenced the President of France to call for early elections in that country. The exchange rate weakened until the mid-week when it recorded a sharp growth as it was announced that the consumer price index in the U.S. in May amounted to 0.0% on a monthly basis, which is less compared to the previous 0.3%, and on an annual basis the growth was 3.3%, being also less than the previous figure of 3.4%. The Fed regular meeting was held on the same day, after which this exchange rate weakened slightly, but not enough to cancel the growth caused by the inflation data. This exchange rate recorded a constant decline during the remaining two days. The drop came as market participants adjust their positions on the Fed's position that it will keep rates at current levels for an extended period of time and as concerns about the French election remain.

EUR/GBP

The EUR/GBP exchange rate weakened slightly at the beginning of the week after the elections that took place over the weekend in Europe and as the President of France called for early elections. The exchange rate increased in mid-week as it was announced that production in Great Britain fell by 1.4% in April, whereas GDP stagnated. This exchange rate experienced a sharp decline on Thursday due to the weakening of the euro in terms of the political uncertainty brought by the elections in France, and as polls showed that the rating of President Macron is at its lowest level since 2018. At the very close of the last day of the week, the exchange rate stopped falling and managed to recover part of the losses from the previous day.

EUR/JPY

During the first three days, **the EUR/JPY exchange rate** fluctuated in a narrow range from 169.33 to 168.46. The first major change in the exchange rate trend occurred on Thursday, when it experienced a sharp decline, as the euro weakened due to the political situation in Europe. The exchange rate rose sharply on Friday as the yen weakened after the Bank of Japan Governor left investors waiting for more details on whether the Bank of Japan will reduce its bond purchase until its July meeting. However, after the Bank of Japan Governor stated at the press conference that the central bank cannot rule out the possibility of an interest rate increase in July, the EUR/JPY exchange rate fell sharply.

Table 1 - Exchange rates of the most important currencies

	10-Jun-2024[1]	14-Jun-2024[2]	% Change
EUR/USD	1.0801	1.0703	-0.91
EUR/GBP	0.84923	0.84383	-0.64
EUR/JPY	169.33	168.43	-0.53
EUR/AUD	1.64110	1.61768	-1.43
EUR/CHF	0.96847	0.95288	-1.61
USD/JPY	156.75	157.40	0.41
GBP/USD	1.2719	1.2687	-0.25

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	4.25%	18 July 2024
Federal Reserves (Fed)	Federal Funds Target Rate	5.50%	31 July 2024
Bank of Japan (BoJ)	Overnight Call Rate	0.00%	31 July 2024
Bank of England (BoE)	Official Bank Rate	5.25%	20 June 2024
Swiss National Bank (SNB)	Libor Target Rate	1.50%	20 June 2024
Bank of Canada (BoC)	Target Overnight Rate	4.75%	24 July 2024
Reserve Bank of Australia (RBA)	Cash Rate Target	4.35%	18 June 2024

Table 3 - ESTR and Euribor

	10-Jun-2024.[1]	14.06.2024.[2]	Change in basis points
ESTR	3.912	3.662	-25.0
Euribor 1W	3.794	3.626	-16.8
Euribor 1M	3.679	3.579	-10.0
Euribor 3M	3.759	3.715	-4.4
Euribor 6M	3.735	3.735	0.0
Euribor 12M	3.701	3.672	-2.9

[1] Opening market value on Monday

[2] Closing market value on Friday

Table 4 - Economic indicators (10 - 14 June 2024)

Country	Indicator	Period	Expected value	Current value	Previous value
Germany	**Consumer price index (CPI)** It estimates the changes in the cost of living, by measuring changes in the price level of market basket of consumer goods and services purchased by an average household.	May Final data MoM% YoY%	 0.1% 2.4%	 0.1% 2.4%	 0.2% 2.4%
Great Britain	**Industrial Production** It measures the output in mining and quarrying, manufacturing and utilities (electricity, gas and water supply).	April MoM% YoY%	 -0.1% 0.3%	 -0.9% -0.4%	 0.2% 0.5%
Italy	**Industrial Production** It measures the output in mining and quarrying, manufacturing and utilities (electricity, gas and water supply).	April MoM% YoY%	 0.2% -2.1%	 -1.0% -2.9%	 -0.5% -3.5%
France	**Consumer price index (CPI)** It estimates the changes in the cost of living, by measuring changes in the price level of market basket of consumer goods and services purchased by an average household.	May Final data MoM% YoY%	 0.2% 2.7%	 0.1% 2.6%	 0.2% 2.7%
Euro area	**Trade Balance SA** The difference between exports and imports of goods and services. This is one of the most represented components of Europe's Balance of Payments, so it gives a valid insight into the pressures to which the European currency is exposed.	April b=bill.	 17.5b	 19.4b	 17.3b
USA	**Consumer price index (CPI)** It estimates the changes in the cost of living, by measuring changes in the price level of market basket of consumer goods and services purchased by an average household. **Initial Jobless Claims** It measures the number of people first time applying for receiving compensation.	May MoM% YoY% F June K=1,000	 0.1% 3.4% 225K	 0.0% 3.3% 242K	 0.3% 3.4% 229K
Japan	**Gross domestic product (GDP)** Measures the final market value of all products and services produced within the country. GDP is the most commonly used indicator of economic activity. **Producer Price Index (PPI)** Measures changes in prices of goods and services after leaving the place of production. Producers transfer higher costs to consumers through retail prices, thus PPI is important as an early inflation indicator.	Q1 QoQ% May MoM% YoY%	 -2.0% 0.5% 2.0%	 -1.8% 0.7% 2.4%	 -2.0% 0.1% 2.4%

EUROPEAN GOVERNMENT BONDS MARKET

The yields on 10-year German government bonds fell from 2.65% to 2.36% in this reporting week. The maximum value was recorded on Tuesday at the opening of the market, 2.687%, and the minimum on Friday, 2.342%. The fall in German yields this week is caused by the political situation in Europe. Once the right-wing parties won the European Parliament elections, the French president, disappointed with his party's results, called for early parliamentary elections. Concerns about political instability in France, and the threat of political fragmentation, have turned investors to safe assets. An opinion poll in France showed that President Macron's rating fell to its lowest level since 2018. In addition, the poll showed that the leftist political alliance, the Popular Front, could find itself in second place, after the right-wing National Rally of Marine Le Pen, which would push President Macron's "Renaissance" party to a third place. On the other hand, yields on French government bonds rose, thus this week the spread of 10-year French and German government bonds increased by 29bp to 77bp (the highest since 2017). Expectations regarding the reduction of the ECB's interest rate increased slightly this week, so the markets are counting on a reduction of 25bp by October and a reduction of 44bp by the end of the year.

U.S. GOVERNMENT BONDS MARKET

The yields on 10-year U.S. government bonds fell from 4.45% to 4.22% in this reporting week. It reached the maximum value of 4.477% on Monday, and the minimum value of 4.186% on Friday. The main reasons for the fall in yields was this week's U.S. price data. The consumer price index and the producer price index were lower in May compared to April and below forecasts, which indicates easing of inflationary pressures, therefore expectations that the Fed will reduce the interest rate already in September have increased. Although the interest rate remained at the current level at the Fed meeting, market expectations were not significantly changed - with a probability of 61.4%, one 25bp reduction is expected by September, and the probability of at least two reductions by December was 72.5% on Friday. The Fed's latest projections point to one cut this year and four cuts in 2025, while March projections indicated three cuts each this year and the next one. Another cause of the downtrend was strong demand at auctions of 10-year and 30-year U.S. bonds, as well as data on new jobless claims that rose to their highest level in 10 months. At the very end of the week, it was announced that American consumer confidence for June was the lowest in the last seven months, due to concerns about high inflation and slower growth in household income.

GOLD

The price of gold rose from $2289.52 to $2333.04 per ounce in this reporting week. The rising trend prevailed on this market for the first three days. The main reason for this trend was the increase in demand for safe assets due to political instability in France, which could threaten Europe. The price rose due to the announcement of surprisingly weak inflation data in the U.S., but also as the outcome of the Fed meeting was expected, therefore it reached the maximum level for this week of $2341.68 on Wednesday. After the Fed meeting ended on the same day with the interest rate kept at the existing level, the price of gold began to retreat from the previously reached level. The latest Fed projections indicate one reduction in the interest rate this year, because officials, despite data indicating that the process of disinflation in the U.S. continues, are less convinced of progress in this field, which is why the drop in price of this precious metal was also relevant on Thursday. However, the price of gold rose on Friday, as a result of the growing demand for safe assets and growing expectations that the Fed interest rate could be reduced already in September, despite the projections of this monetary institution.

OIL

The price of oil increased from $79.16 to $82.84 per barrel in this reporting week. The highest increase occurred on Monday, due to optimism regarding the increase in demand for fuel due to the summer season. The price growth continued for the rest of the week, but at a slower pace. Data from the American Petroleum Institute, which showed that oil stocks in the U.S. fell in the previous week, is one of the factors for the price increase. The rise in the price on Wednesday was caused by forecasts that there will be a drop in oil inventories at the global level in H2 this year, as well as by the data on the inflation rate in the U.S. but it was limited after the U.S. government release of a report that indicated an unexpected increase in U.S. oil supplies. The price of oil fluctuated for the last two days of the week, but the growing trend prevailed. The reasons for the fluctuation were expectations regarding the reduction of the Fed's interest rate, a decrease in consumer confidence in the USA, the announcement of Russia's plan that it will compensate for the production that exceeded the OPEC+ quota in the period April-May by 2025, new attacks by the Houthis in Arabia and the Red Sea.