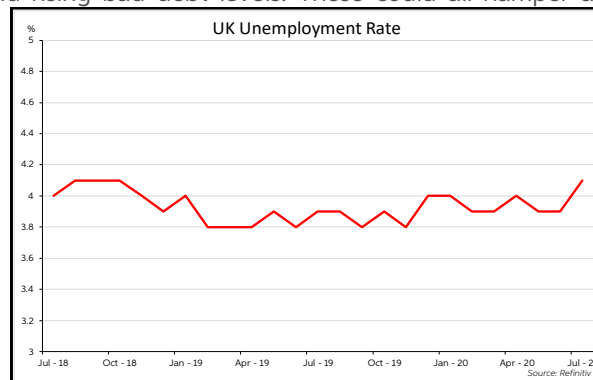


Holding Your Nerve

- **An eerie calm has descended on financial markets, even though major risks to economic activity continue to swirl about.** The number of new Covid cases continues to rise rapidly, especially in Europe, with countries re-imposing restrictions to try and rein in the second wave of the virus. Lockdowns are now being talked about in some countries. Meanwhile, Brexit trade talks remain on a knife-edge. Political uncertainty continues to rise in the US creating difficulties on agreeing a new fiscal stimulus package. There are also concerns that the outcome of the Presidential election could end up being contested in the courts.
- **Meantime, although economic data for the third quarter have generally printed ahead of expectations, there are signs that the recovery is losing momentum.** Service sector activity softened in September, with the Global Services PMI dropping back to 51.6 from 52.0 in August. Job growth in the US also slowed a lot in September, with little more than half the 22 million jobs lost in the recession recovered so far. UK GDP data for August also disappointed to the downside, leaving the level of output more than 9% below its pre-Covid levels. The recovery in economic activity could well stall in the fourth quarter, especially where fiscal supports for the economy are being scaled back, including in the UK and US.
- **Markets, though, don't seem to be phased. Stock markets have regained significant ground over the past fortnight having suffered losses during most of September.** Bond yields remain within narrow ranges, with peripheral spreads actually tightening in the Eurozone. Currency markets have returned to range trading, after first sterling and then the dollar wobbled in September. It would appear that the ample liquidity being provided by central banks through QE, combined with a surge in private sector savings, is helping to shield markets from what seems an elevated risk environment. Investors may also be reassured that central banks will continue to maintain very accommodative monetary policies over the next number of years.
- **However, it is also critical that fiscal policy remains supportive of activity in the near-term.** Ongoing supports for the labour market and those sectors of the economy most impacted by Covid restrictions will be required until next spring at least. Funding costs are very low and private sector savings have gone through the roof, helping to finance public deficits. So fiscal policy can and should remain supportive. A vaccine for the coronavirus is also critical to economic prospects. Such a vaccine is expected to start to be rolled out early next year, but it is likely to be the second half of 2021 before it becomes widely available. The rebound in activity seen over the third quarter was much stronger than expected, but it has been cut short by the second wave to the virus. It suggests a sustained rebound in activity can take root next year if a successful vaccine becomes available.
- **What's more, there is every chance it can be a very robust recovery given the build-up of private savings and the extent of pent-up demand.** What fiscal policy needs to do in the near-term is limit the scarring effects of the recession such as permanently high unemployment, high numbers of business failures and rising bad debt levels. These could all hamper a recovery in activity even as the virus is overcome. Budget deficits won't be long in coming down if the world economy rebounds strongly. There is every prospect that by supporting the economy now, it will pay dividends for public finances in the long term.
- **Data-wise this week the highlight will be the UK labour market report for August.** As evident from the chart, the UK government has shielded the labour market thus far from the impact of coronavirus through its Job Retention Scheme. The forecast is for the unemployment rate to rise in August to 4.3%. BRC retail sales are also due, with another increase expected in September.
- **Across the Atlantic, retail sales are the main release in the US.** Headline sales rose 0.6% in August, below the consensus, as enhanced unemployment benefits were no longer available to many households. The forecast is for a 0.6% increase in September also. Core retail sales (ex-autos) are expected to rise by 0.4%. The Michigan measure of consumer sentiment is expected to have edged up to 81 in October, remaining at a very subdued level. On the supply side, industrial production is forecast to rise by 0.4% in September indicating a levelling off in momentum. Regional manufacturing surveys such as the Philly Fed index and the Empire State index for October are both forecast to slip back, suggesting that the rebound in manufacturing may be losing steam. Meanwhile, it is envisaged that the CPI will rise by 0.2%, with the core CPI also expected to print at 0.2%. This would see both the headline and core rates edge up to 1.4% and 1.8% YoY respectively.
- **There is a more muted look to the Eurozone data calendar.** Industrial production for August is forecast to rise by 0.4%, leaving output 6.8% below its pre-Covid peak. The European Council meeting will take place on the 15-16th of October, with the EU-UK trade talks on the agenda. **On the home front, Budget 2021 will be released on Tuesday.** Further supports are likely for the economy, with another large budget deficit expected in 2021.



	Interest Rate Forecasts			
	Current	End Q4	End Q1	End Q2
		2020	2021	2021
Fed Funds	0.125	0.125	0.125	0.125
ECB Deposit	-0.50	-0.50	-0.50	-0.50
BoE Repo	0.10	0.10	0.10	0.10
BoJ OCR	-0.10	-0.10	-0.10	-0.10

Current Rates Reuters, Forecasts AIB's ERU

	Exchange Rate Forecasts (Mid-Point of Range)			
	Current	End Q4	End Q1	End Q2
		2020	2021	2021
EUR/USD	1.1813	1.18	1.20	1.22
EUR/GBP	0.9093	0.88	0.88	0.89
EUR/JPY	124.85	124	126	127
GBP/USD	1.2991	1.34	1.36	1.37
USD/JPY	105.67	105	105	104

Current Rates Reuters, Forecasts AIB's ERU

Date	UK & Irish Time (GMT+1)	Release	Previous	Forecast
This Week:	ECB Speakers:	Lagarde , Panetta, Schnabel, de Guindos (Monday); Lagarde , Panetta, Lane (Wednesday); Lagarde (Thursday)		
	BoE Speakers:	Bailey (Monday), Haldane (Thursday)		
	Fed Speakers:	Clarida (Wednesday)		
	EU-27:	EU Leaders' Summit (Thursday/Friday)		
	IMF:	World Economic Outlook October 2020		
Mon 12th	US:	Market Holiday		
	JPN: 00:50	Core Machinery Orders (September)	(-16.2%)	(-15.6%)
Tue 13th	UK: 00:01	BRC Retail Sales (September)	(+4.7%)	
	GER: 07:00	Final HICP (September)	(-0.2%)	(-0.2%)
	UK: 07:00	ILO Employment (August) - Unemployment	-12,000 4.1%	-18,000 4.3%
	UK: 07:00	Average Weekly Earnings (August) - Ex-Bonus	(-1.0%) (+0.2%)	(-0.5%) (+0.6%)
	UK: 07:00	Claimant Count (September)	+73,700	
	CHINA: 09:30	Trade Balance (September) - Exports	+\$58.93bn (+9.5%)	+\$59.95bn (+10.0%)
	GER: 10:00	ZEW Economic Sentiment (October)	77.4	74.0
	US: 11:00	NFIB Business Optimism (September)	100.2	
	US: 13:30	CPI (September) - Core	+0.4% (+1.3%) +0.4% (+1.7%)	+0.2% (+1.4%) +0.2% (+1.8%)
	IRL:	Budget 2021		
Wed 14th	EU-19: 10:00	Industrial Production (August)	+4.1% (-7.7%)	+0.7% (-7.2%)
	IRL: 11:00	Residential Property Prices (August)	+0.3% (-0.5%)	+0.0% (-0.8%)
	US: 13:30	PPI (September)	-0.2%	+0.2%
Thurs 15th	CHINA: 02:30	PPI (September)	(-2.0%)	(-1.9%)
	CHINA: 02:30	CPI (September)	(+2.4%)	(+2.4%)
	FRA: 07:45	Final HICP (September)	+0.0%	(+0.0%)
	US: 13:30	NY Fed / Empire State Index (October)	17.0	15.0
	US: 13:30	Initial Jobless Claims (w/e 5th October)	840,000	
	US: 13:30	Philly Fed Index (October)	15.0	14.5
Fri 16th	ITA: 09:00	Final HICP (September)	(-0.9%)	(-0.9%)
	EU-19: 10:00	Final HICP (September) - Core	-0.4% (-0.3%) +0.2% (+0.2%)	+0.1% (-0.3%) +0.2% (+0.2%)
	US: 13:30	Retail Sales (September) - Ex-Autos - Ex-Gas, Autos & Building Materials	+0.6% +0.7% -0.1%	+0.6% +0.4%
	US: 13:30	Industrial Production (September) - Capacity Utilisation - Manufacturing Output	+0.4% 71.8% +1.0%	+0.6% 71.9% +0.9%

◆ Month-on-month changes (year-on-year shown in brackets)
All forecasts AIB ERU, historical data in the Economic Diary derived from publicly available sources

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