Weekly Market Brief
AIB Treasury Economic Research Unit

16th—20th September 2019

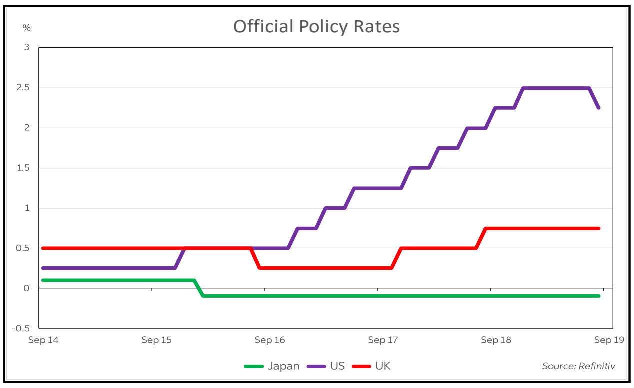
Waiting for Inflation Godot to Appear

- **A marked improvement in risk appetite has been a noticeable feature of financial markets this month, leading to a sharp rise in bond yields with equities making good ground.** It has also seen a noticeable scaling back of rate cut expectations in all markets. Thus, while the ECB certainly delivered on the policy easing front this week, with a rate cut, restarting of an open-ended QE programme, easier terms for TLTRO 3, and dovish forward rate guidance, the positive response in bond markets to the announcements did not last long as the underlying trend of rising yields re-emerged.

- **The improved market sentiment is due to a couple of factors, including data in the US and UK economies starting to come in ahead of expectations, having disappointed year-to-date, and some downside risks to growth receding a little.** In this regard, there are some signs of progress in the US-China trade talks, while a no-deal Brexit is seen as having being taken off the table for end October by the UK Parliament. Indeed, there are growing hopes that the EU and UK might even be able to agree a Brexit deal next month

- **The week ahead sees both the Fed, Bank of England and Bank of Japan hold monetary policy meetings, with another 25bps cut in the US fully discounted by markets.** However, the reaction of bond markets to the ECB meeting shows that even if the Fed delivers, traders may not be impressed. Overall, it would seem that markets had gotten too far ahead of the economic data in pricing in extensive monetary easing. The big picture has not changed, though. It is clear from the forward guidance of the ECB that monetary conditions are set to remain extremely loose for a long time in the Eurozone. The ECB is commencing an open-ended QE programme and has also indicated that rates could be cut further. Policy tightening will not come on to the agenda until the ECB has seen the outlook for underlying inflation "robustly converge" with the 2% inflation target. This is a bit like waiting for Godot. Indeed, based on the ECB's own inflation forecasts, it is years away. Not surprising then, futures contracts indicate that the deposit rate will still be negative at around -0.2% in 2025.

- **In terms of the Fed, it is likely to reference the downside risks facing the global economy, including those linked to US-China trade tensions, in its rationale for the expected rate cut**. There is also some evidence that the US economy is softening, with payrolls, the ISMs and the PMIs all trending downwards. However, as outlined by Fed Chair Powell in a recent speech, overall, the economy remains "in a good place", with the consumer sector performing strongly. On that basis, the Fed is unlikely to indicate that it has embarked on a sustained rate cutting cycle in its updated interest rate projections. Although it may guide that it could cut rates once or twice more. This would see the Fed's view of the likely future path for rates remain out of kilter with the market, which is looking for close to 100bps worth of easing.



- **Elsewhere, the BoE is expected to keep rates on hold as it awaits further clarity on the final outcome of Brexit.** However, markets will look to the meeting minutes for any insight on what impact the recent pick-up in wage inflation may have on policy. Meantime, it is envisaged that the BoJ will also keep rates unchanged, though it could lay the groundwork for a future rate cut given persistently subdued inflation, the weaker outlook for global growth and the appreciation of the yen this year.

- **Data-wise, the US data schedule includes August industrial production.** Output is projected to have increased by just 0.2%, amid weaker global growth. The September reading of the Philly and the NY Fed indices will provide a timelier update on the output side of the economy. We also get a batch of housing market data this week, with housing starts and existing home sales for August due, as well as the September print of the NAHB Sentiment Index.

- **In the UK, the August CPI is due. Higher labour costs are not translating into accelerating inflation.** Indeed, both the headline and core rates of inflation are anticipated to have eased in August. Meanwhile, retail sales are expected to be have been flat in August amid heightened Brexit uncertainty in the month.

- **Turning to the Eurozone, there is a very sparse look to the macro diary this week.** Indeed, the only release of any note is the flash reading of EC consumer confidence for September, which is envisaged to be little changed from its August reading.

Interest Rate Forecasts

	Current	End Q3 2019	End Q4 2019	End Q1 2020
Fed Funds	2.125	1.875	1.625	1.625
ECB Deposit	-0.50	-0.50	-0.60	-0.60
BoE Repo	0.75	0.75	0.75	0.75
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 Q3 2019	End Q4 2019	End Q1 2020
EUR/USD	1.1070	1.11	1.12	1.13
EUR/GBP	0.8894	0.90	0.90	0.90
EUR/JPY	119.61	118	119	119
GBP/USD	1.2446	1.23	1.24	1.26
USD/JPY	108.04	106	106	105

Current Rates Reuters, Forecasts AIB's ERU

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ECONOMIC DIARY

Monday 16th—Friday 20th September 2019

Date	*UK & Irish Time (GMT)*		*Release*	*Previous*	*Forecast*
This Week:	**ECB Speakers:**		Lautenschlager (Thursday)		
	Fed Speakers:		Kaplan, Rosengren (Friday)		
Mon 16th	**CHINA:**	03.00	Industrial Output (August)	(+4.8%)	(+5.2%)
	USA:	13.30	NY Fed / Empire State Index (September)	4.8	3.0
Tue 17th	**GER:**	10.00	ZEW Economic Sentiment Index (September)	-44.1	-38.0
	US:	14.15	Industrial Production (August)	-0.2%	+0.2%
			- Capacity Utilisation	77.5%	77.6%
			- Manufacturing Output	-0.4%	+0.2%
	US:	15.00	NAHB Homebuilders' Sentiment (September)	66	66
Wed 18th	**JPN:**	00.50	Trade Balance (August)	-¥250.7bn	-¥355.9bn
			- Exports	(-1.5%)	(-10.9%)
	UK:	09.30	CPI (August)	(+2.1%)	(+1.9%)
			- Ex-Food & Energy	(+1.9%)	(+1.7%)
	UK:	09.30	PPI Output (August)	(+1.8%)	(+1.7%)
			- Input	(+1.3%)	(-0.1%)
	EU-19:	10.00	Final HICP (August)	(+1.0%)	(+1.0%)
	US:	13.30	Housing Starts (August)	-4.0% / 1.19m	3.2% / 1.23m
			- Building Permits	+6.9% / 1.317m	-1.0% / 1.304m
	US:	19.00	Fed Interest Rate Announcement	2.00-2.25%	1.75-2.00%
	US:	19.30	Fed Press Conference		
Thurs 19th	**JPN:**	03.00	BoJ Interest Rate Announcement	-0.10%	-0.10%
	UK:	09.30	Retail Sales (August)	+0.2% (+3.3%)	+0.0% (+2.9%)
	UK:	12.00	BoE Interest Rate Announcement	0.75%	0.75%
			- Meeting Minutes		
	US:	13.30	Initial Jobless Claims (w/e 9th September)	204,000	210,000
	US:	13.30	Philly Fed Index (September)	16.8	10.0
	US:	15.00	Existing Home Sales (August)	+2.5% / 5.42m	-0.4% / 5.37m
	US:	150.00	Leading Indicators' Index (August)	+0.5%	+0.1%
Fri 20th	**JPN:**	00.30	CPI (August)	(+0.5%)	(+0.5%)
	GER:	07.00	PPI (August)	(+1.1%)	(+0.6%)
	UK:	09.30	PSNB Ex-Interventions (August)	Aug '18: £5.6bn	-£1.32bn
	EU-19:	15.00	Flash Consumer Confidence (September)	-7.1	-7.0

♦ *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