



THE TREASURY HUB

Markets Bulletin

Autumn 2023



1. Executive Summary

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1.1 Introduction

Welcome to the Autumn edition of THE TREASURY HUB Markets Bulletin.

As you are aware, these bulletins cover quite a wide range of topics and are a comprehensive review of all the various interest rate, foreign exchange, commodity and stock markets. In order to continue to refine what we provide to you, with effect from next month we will provide a shorter, sharper bulletin but will remain with this more detailed version every calendar quarter.

The stories of the year have been inflation and (its impact on) interest rate trends. Central Banks have tightened interest rates for months on end across the globe but the markets have been preoccupied for the past few months on when the rate hikes will halt and even when they might start to decline.

- 3-month Euribor has continued to climb in line with ECB Base Rates and is now close to 4.00%. The last time that it was at this level was in November 2008 on its way down from a peak of 5.39%
- EUR, UK and US yield curves are all inverted after 1 year which is consistent with the expectation of a peak in the interest rate cycle in the coming year
- Oil prices have moved materially up and down in the past 12 months. At the end of June, Brent Crude was just under \$73 compared to a current level of over \$86.

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1.2 Markets in a Table: what's up and what's down?

Table 1. Key Metric Movements: 2023

<u>Heading</u>	<u>Metric</u>	<u>YTD move</u>	<u>From</u>	<u>To</u>
<u>Interest</u>	3-m euribor	1.82%	2.16%	3.98%
<u>Interest</u>	EUR 3-year	0.47%	3.23%	3.69%
<u>Interest</u>	GBP 3-year	0.56%	4.54%	5.10%
<u>Interest</u>	USD 3-year	0.55%	3.98%	4.53%
<u>FX</u>	EUR/GBP	-2.41%	0.8850	0.8642
<u>FX</u>	EUR/USD	-0.55%	1.0662	1.0604
<u>Equities</u>	ISEQ	14.55%	7293	8354
<u>Equities</u>	FTSE 100	1.23%	7554	7647
<u>Equities</u>	Nasdaq	39.03%	10862	15101
<u>Commodities</u>	Brent Crude	5.54%	82.10	86.65
<u>Commodities</u>	Carbon	4.28%	81	84.47
<u>Commodities</u>	Gold	2.63%	1823	1871
<u>Commodities</u>	Wheat	-28.77%	775	552
<u>Gilts</u>	IE 10-yr	0.23%	2.98%	3.21%
<u>Gilts</u>	GB 10-yr	0.76%	3.65%	4.41%
<u>Gilts</u>	US 10-yr	0.85%	3.79%	4.64%

Please note that the % moves are in green if the metric has moved upwards and in red if it has moved downwards. It is NOT a statement as to whether this is a positive or negative move as one could be a borrower or depositor, a seller or buyer of currency, etc. Also, the % move for interest rates is in absolute terms while for currency and equities it is expressed in relative terms. **PLEASE NOTE THAT INTEREST RATE TRENDS ARE FROM A DEPOSITOR PERSPECTIVE.**

- Stock markets have eased off over the last quarter but have recovered some of this ground in October
- Wheat prices are 28% down in the year which ought to have a positive impact on food inflation
- Government borrowing (gilt) rates have also moved with Irish rates almost 0.2% off the year-to-date high
- USD has strengthened almost continuously over the past 3 months, from EUR/USD1.12 to EUR/USD1.06
- But GBP continues to operate in the narrow range that it has occupied for most of this year.

1.2 Forward-looking Indices

Forward-looking indicators known as Purchasing Manager Indices or PMIs are useful to monitor the economic outlook for Ireland and the UK. Readings above 50 indicate expansion while below 50 denote contraction.

- Two of the three ROI indicators are now negative with only Services bucking the trend by remaining above 50 and that is also falling
- In the UK, all three measures are in negative territory which does not augur well for the economic outlook for 2024.

Table 2. Irish and UK PMI readings

	<u>Ireland</u>	<u>UK</u>
Manufacturing PMI	49.6	44.3
Services PMI	54.5	49.3
Construction PMI	48.6	45.0

1.3 Inflation

Table 3. Selected Inflation Rates

	<u>CPI/Core Inflation</u>
ROI	6.09%
EUROZONE	4.5%
UK	6.2%
US	4.1%

Core figures are looked at as they exclude energy, mortgages and food.

Irish core rate has fallen for four months in a row from +7.08%. CPI has actually increased for the past two months but food inflation is down from 13.1% in April to 7.8% in September.

Eurozone core inflation which peaked at 5.7% in March fell materially in September to 4.5%. This is why the ECB which has hiked for 10 times in this cycle is expected to stall such hikes at the next meeting at the end of October in what will be the second last meeting of the year.

UK core inflation is now 0.9% back from May's 31-year high. Headline inflation is also down from a peak level of 11.1% to 6.7%. Food inflation is still worryingly high at +13.6%.

The US core inflation rate, with one exception, has slowed every month since September of last year. The headline figure, having fallen for 12 months in a row to 3.0% in June, has climbed again for the past few months to 3.7%. The US continues to see its inflation lower than its major peers.

Whether there is one more hike in any of the interest rates covered here remains to be seen. The inflation data above shows the general trend going the right way but currently falling short of 2%. Economic growth trends don't look great in UK or Eurozone so pressure to cut may come in that guise.

2. Foreign Exchange, Oil & Carbon

2.1 EUR/USD

- We monitor the 5-year trend in Graph 1 to look at the EUR/USD rate trends in more recent times
- The USD strengthening which persisted from mid 2021 to Q3 2022 reversed significantly from Q4 2022 but we have had another recent bout of USD strength over the Summer
- **So, exporters with USD-denominated sales have received an unexpected boost as a result**
- The flip side of this trend is that commodities are mainly priced in USD, especially oil. The EUR-equivalent costs have increased and that is before one considers the trends in the USD prices of said commodities
- See Section 3 for further wider comment.

Graph 1. EUR/USD: 5-year trend



2.2 EUR/GBP

- EUR/GBP has held up despite the poor economic outlook mainly due to the support to the currency given by high interest rates
- Politics will also come into the foreground again in 2024 with a general election
- UK Inflation remains stubbornly high as evidenced in Table 3.
- Given the fairly poor GDP outlook, there must be a real chance that once the Bank of England starts to cut interest rates, the GDP outlook will become a dominant consideration by the markets and GBP could weaken....of course that depends on how the Eurozone also trends relative to the UK
- Germany looks like it is experiencing a downturn and their relative size in the Eurozone will have an impact.

- This graph shows that the current range veers towards a weakening GBP but it is still in a relatively tight range of 2p
- Until there is greater clarity on which Central Bank stops hiking first, it is difficult to ascertain a likely direction.

Graph 2. EUR/GBP: 2023 to date

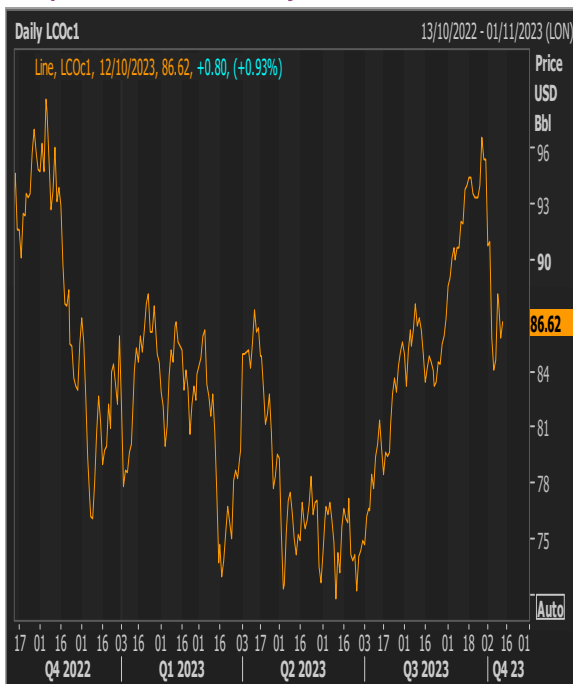


2.3 OIL & CARBON

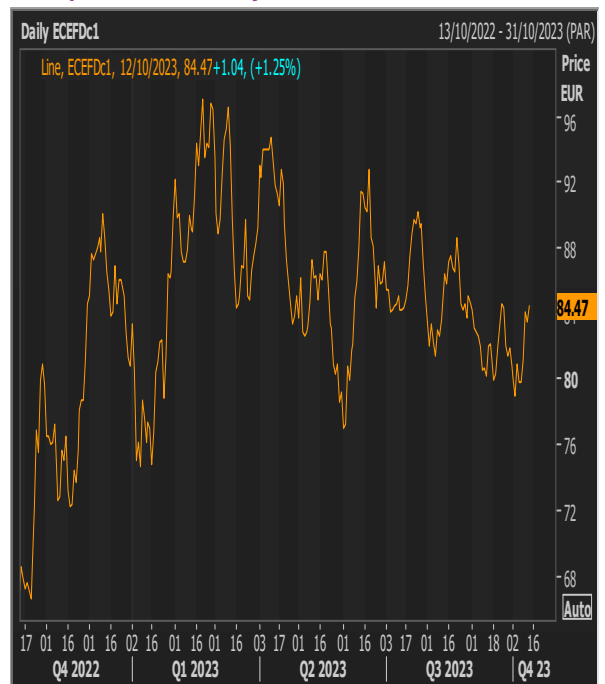
Brent Crude moved in a range of USD 72 to USD 87 for most of the year. Hard to see it breaking back towards USD 72 in the short term (given that it has increased by \$14pbl in 6 weeks).

The price of Carbon shows similar trends with six “peak to trough” moves of circa €8 since February. In general, the range is moving downwards since Q1 2023 but the price is still heading back towards €85 again.

Graph 3. Brent Crude: 1-year trend



Graph 4. Carbon: 1-year trend



3. Interest and Economic Review

3.1 EUR Short-term Rates

Interest rates have dominated so much of the business and economic news in 2023 having been a “non-story” for almost a decade and a half. The Euribor rate that we monitor for the purposes of this bulletin (as it is the most relevant one for variable rate debt) is the 3-month rate.

Key Observations

- The 3-month rate which drives the pricing of variable rate loans has climbed steadily this year in line with hikes in the ECB Base Rate. The ECB has raised the Base Rate on six occasions this year from 2.50% in December 2022 to 4.50% currently
- At the start of the year the markets were forecasting a peak around 3.50% so the rate has overshot significantly
- **We have previously predicted that deposit rates would slowly increase in the second half of the year and that has started to happen after the ECB meeting in August.**

Graph 5. 3-month Euribor: 2023 trend



3.2 EUR medium-term Rates

- We always look at 3-year swap rates as they are a better indicator of the future direction of interest rates
- The EUR fixed rate curve (before margin) is inverted at 1-year meaning that longer-term rates (2-years +) are LOWER than shorter-term rates. The 1-year rate is 4.09% but the 3-year rate is 3.69%
- The ECB after its last meeting that underlying inflation continues to ease and the general interpretation of the comments was that they may hold rates at the next meeting. Bear in mind that they have hiked ten times now since July 2022 which is aggressive. We remain of the view that we will see EUR interest rates remaining in the 3%-4% range for some time.

Graph 6. EUR 3-year swaps: 2-year trend



3.3 Summary

- The all-in cost of debt is now hitting between 7% and 8% on average for most businesses although it can vary between banks and so it is important to talk to us about borrowing rates
- Credit has continued to tighten and making loan applications is more difficult, less is being advanced and lenders are taking much longer to make lending decisions
- **Last month we mentioned that there was an increasing amount of comment on falling real estate prices and the impact on the US banks. Beginning to hear similar comments on this side of the Atlantic too.**

3.4 UK and US Interest Rates

- BOE Base Rate was as low as 0.10% in March 2020 due to the pandemic but it has been hiked on 14 occasions since December 2021 with the current rate at 5.25%, last seen in February '08
- **As Graph 7 below shows, the UK 3-year rate rose by 1.75% between February and June but is back 1% (i.e. lower) since July.**

Graph 7. GBP 3-year swaps: 2023 trend



Graph 8. USD 3-year swap rates: 2023 trend



- US rates have been quite erratic in the trend this year as market views ebbed and flowed around whether and when inflation might peak
- One of the key features in the US yield curve is that US 1-year rate is currently 5.72% but the implied 1-year rate in 1 year's time is 4.74% which is an almost 1% implied decrease in the 1-year rate over the next twelve months
- The utterances from Fed Governors is increasingly of no more rate hikes which would be welcomed by consumers – consumer sentiment recently fell due to expectations of higher inflation
- We have previously referenced possible problems with US real estate and we continue to hold that view
- The unemployment rate has increase marginally since July (from 3.5% to 3.8%) with over 6 million people unemployed but job vacancies are still estimated at 9.5 million
- And their participation rate (% of adult population working or seeking work) at 62.8% is still low by the standards of other countries
- Housing starts were at their lowest level since July 2020
- Retail sales are back towards longer term levels
- Overall, the IMF most recent forecast put 2023 GDP growth in the US at a decent +2.1% level – below the global average of +3.0% but ahead of Germany (-0.5%), the UK (+0.5%) and Canada (+1.3%). So, the US outlook is broadly positive.

3.5 Summary

- **The expectation of future interest rate trends remains quite different between the major economies: the forecast 1-year rate in 12 months time is 3.63% in the EU, 4.74% in the US and 4.98% in the UK**
- **UK interest rates remain particularly high – all-in cost of funds remaining around 8.5%**
- **All the evidence points to a slowdown in Germany as we previously suggested here**
- **Even the Irish data is showing a slowdown with volumes going through the ports down materially since April, especially in the area of pharma**
- **PMI readings as set out in Section 1 are also deteriorating with all three UK readings now registering contraction in the economy**
- **And we still have a nagging fear that the shadow banking sector in the US could have some underlying issues which, if proven to be correct, would tip over into the mainstream banking sector**
- **In addition to all of the above, the geo-political outlook remains poor**
- **2024 looks like a challenging year on the economic and political front so plan accordingly when constructing your 2024 Budget..**

4. Wealth Management

4.1 Gold

Graph 9. Gold prices: 2023 trend



- We have kept Gold on this bulletin as it's a perceived safe haven in turbulent times. You will note a recent upturn in its price as fears of an economic slowdown increase again.

4.2 Wheat

Graph 10. Wheat prices: 2023 trend



- While wheat prices were subject to some volatility over the Summer, they have resumed their downward trend since the end of July
- Current levels are well below the price that prevailed before the invasion of Ukraine and are actually back at October 2020 levels.

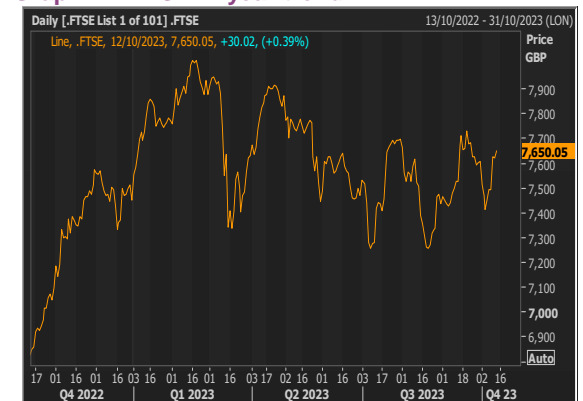
4.3 Equity Markets

- Equity markets rebounded very well after last year's reversal and held up through to the Summer
- However, there has been more volatility in stock market trends in the past 6-8 weeks as investors assess whether the mantra "higher for longer" in relation to interest rates will hold true.

Graph 11. ISEQ: 1-year trend



Graph 12. FTSE: 1-year trend



Graph 13. NASDAQ: 1-year trend

