

# Week Ahead

Focus: Bank of England intervenes, EU Energy market

Analysts:

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## UK – Bank of England forced to intervene on markets

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Last week, the new British Prime Minister Elisabeth Truss unveiled her plan to stimulate the UK economy with significant tax cuts. In principle, well-designed tax cuts are an effective instrument to improve the long-term growth prospects of an economy. This is because the private sector is more efficient and productive than the state in using the funds it frees up. Moreover, tax cuts attract more foreign investment capital, which raises labour productivity additionally. In the face of high inflation rates and the Bank of England's efforts to achieve exactly the opposite, namely to cool the economy, by tightening monetary policy, this move is controversial.

The financial markets have reacted by selling off the British pound, especially against the US dollar, as well as long-dated British government bonds. The Bank of England has seen a threat to financial stability from the violent movements in the bond market and has therefore announced a temporary intervention in the market for long-dated government bonds. It will buy unlimited amounts of long-dated British government bonds until October 14 in order to remedy the dysfunction in the bond market. The Bank of England is sticking to its basic goal of reducing its balance sheet by GBP 80bn a year.

The circumstances show how nervously the financial markets can react in the current tense situation with the energy crisis and high, sometimes double-digit inflation rates. This is also a warning signal for Italy where the new government of Georgia Meloni will elaborate its government programme in the coming weeks.

For the time being, the Bank of England has been able to stabilize the situation. In interviews, however, Truss has announced that she intends to stick to her plans despite the market turbulence. Any further deterioration of the situation in the UK could have negative consequences for the Eurozone. On the one hand, this is due to its essential importance as a trading partner despite Brexit, and on the other, London remains an important financial center for the global economy. Against this background, the intervention of the Bank of England to preserve financial stability in the UK is essential for the global financial markets and thus also for the Eurozone.

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Note: Past performance is not necessarily indicative of future results

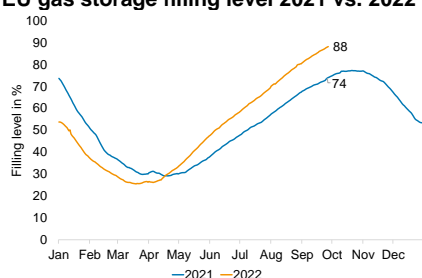
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## EU - Sabotage unsettles Europe's energy markets

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The recent act of sabotage, with explosions creating several leaks in the Nordstream I and Nordstream II gas pipelines, has caused a significant short-term increase in European gas prices. Although both pipelines currently play no role at all in supplying gas to Europe, this has nevertheless caused great uncertainty among market participants.

**EU gas storage filling level 2021 vs. 2022**



Source: agsi+, Erste Group Research

Probably because of the justified concern that similar acts of sabotage could occur at other points of critical EU infrastructure (oil and gas pipelines, electricity or telecommunications cables). Whoever was responsible for this act of sabotage, what remains for the EU is that the uncertainty has caused energy prices to rise again, at least in the short term. This damages the European economy and increases the pressure on companies, households and ultimately the member states.

A delay in the fall of Europe's gas prices increases the downside risks to the economic outlook, in our view. At the same time, upside risks to our current inflation forecast increase, especially for 2023. EU countries should therefore take decisive action to better protect critical infrastructure from sabotage in the current environment. This should reassure market participants and hopefully prevent similar incidents in the future.

Apart from that, the EU is making very good progress in filling gas storage facilities, even with significantly reduced Russian supplies. The filling level at the end of September this year is 88%, well above the level at the end of September 2021 of only 74%. Although the winter months will be challenging, the scheduled preparations by member states should provide some comfort to financial markets.

Moreover, the dramatic increase in energy prices has now reached households and small and medium-sized enterprises, after a significant time lag, from a few months ago. In our estimation, this has increased the likelihood of noticeable savings in gas and electricity consumption during the winter months. This should have an additional dampening effect on price development. In this environment, a long cold winter nevertheless represents a considerable risk for Europe's economy.

## Economic calendar

Ctry	Date	Time	Release	Period	Consens	Prior
<b>Eurozone</b>						
EA	3-Oct	10:00	PMI Index	Sep F		48.5 Index
DE	3-Oct	9:55	PMI Index	Sep F		48.3 Index
FR	3-Oct	9:50	PMI Index	Sep F		47.8 Index
IT	3-Oct	9:45	PMI Index	Sep		48.0 Index
<b>USA</b>						
	3-Oct	16:00	PMI Index	Sep	52.3 Index	52.8 Index
	5-Oct	14:15	ADP Employment	Sep	203.8 Tsd	132.0 Tsd
	7-Oct	14:30	Wages y/y	Sep	5.1%	5.2%
	7-Oct	14:30	Unempl. Rate	Sep	3.7%	3.7%
	7-Oct	14:30	Chg. Non-Farm Payrolls	Sep	260.1 Tsd	315.0 Tsd

### China

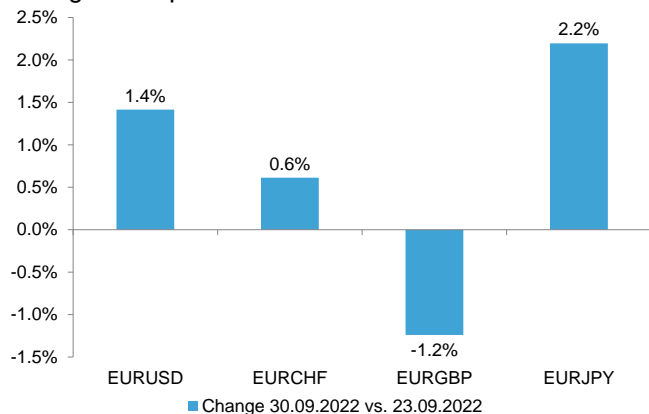
## Central bank events

	Date	Time	Representative	Forum	Location
<b>ECB</b>	4-Oct	17:00	Christine Lagarde	Discussion	Central Bank of Cyprus
<b>Fed</b>	6-Oct	22:00	Christopher Waller	Speech	Mark C. Berger Workshop, Kentucky

Source: Market Data Provider, ECB, Federal Reserve, Erste Group Research

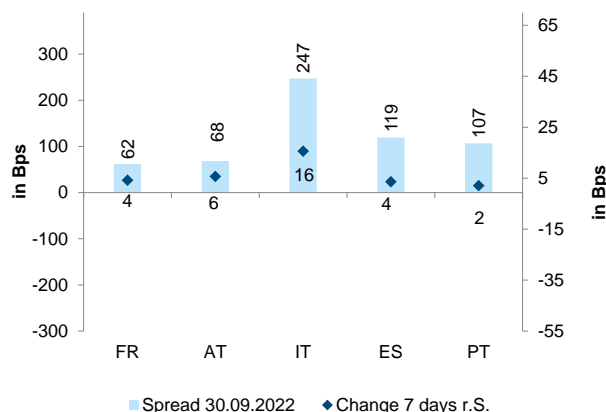
## Forex and government bond markets

### Exchange rates EUR: USD, CHF, GBP and JPY Changes compared to last week



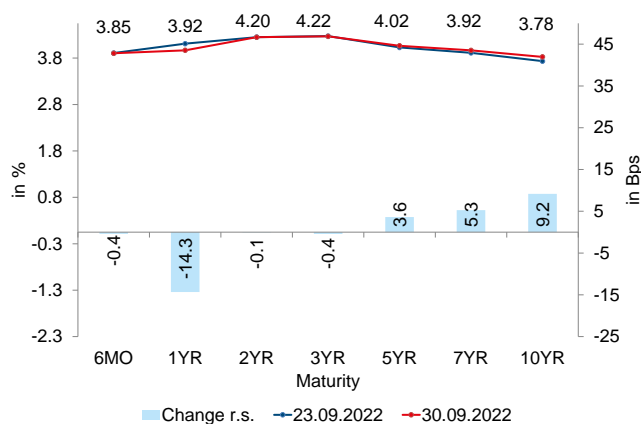
Source: Market Data Provider, Erste Group Research

### Eurozone spreads vs. Germany 10Y government bonds



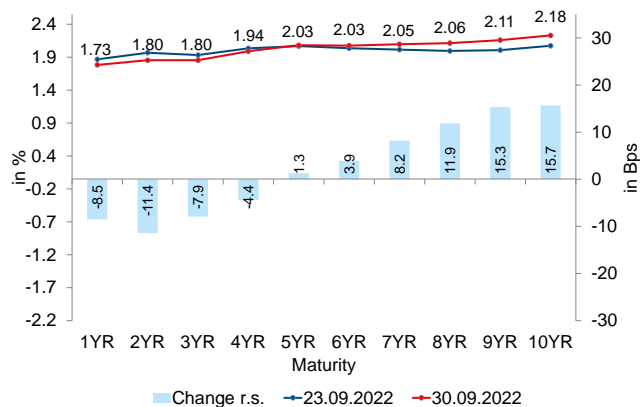
Source: Market Data Provider, Erste Group Research

### US Treasuries yield curve Changes compared to last week



Source: Market Data Provider, Erste Group Research

### DE Bund yield curve Changes compared to last week



Source: Market Data Provider, Erste Group Research

## Forecasts<sup>1</sup>

<b>GDP</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>
<b>Eurozone</b>	-6.5	5.3	2.7	1.0
<b>US</b>	-3.5	5.7	1.6	1.4

<b>Inflation</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>
<b>Eurozone</b>	0.3	2.6	7.9	4.1
<b>US</b>	1.2	4.7	8.0	3.0

<b>Interest rates</b>	<b>current</b>	<b>Dec.22</b>	<b>Mar.23</b>	<b>Jun.23</b>	<b>Sep.23</b>
<b>ECB MRR</b>	1.25	2.25	2.25	2.25	2.25
<b>ECB Deposit Rate</b>	0.75	1.75	2.00	2.00	2.00
<b>3M Euribor</b>	1.16	1.97	1.97	1.97	1.97
<b>Germany Govt. 10Y</b>	2.18	1.80	1.80	1.80	1.80
<b>Swap 10Y</b>	3.14	2.60	2.50	2.40	2.30

<b>Interest rates</b>	<b>current</b>	<b>Dec.22</b>	<b>Mar.23</b>	<b>Jun.23</b>	<b>Sep.23</b>
<b>Fed Funds Target Rate*</b>	3.08	4.13	4.38	4.38	4.38
<b>3M Libor</b>	3.67	4.38	4.46	4.46	4.46
<b>US Govt. 10Y</b>	3.77	3.20	2.90	2.80	2.80
<b>EURUSD</b>	0.98	1.03	1.06	1.07	1.09

\*Mid of target range

*In case of changes to our forecasts compared to the previous issue, arrows show the direction of the change.*

*Source: Market Data Provider, Erste Group Research*

<sup>1</sup> Note: In accordance with regulations, we are obliged to issue the following statement:  
 Forecasts are not a reliable indicator of future performance.

# Erste Group Research

Week Ahead | Major Markets | Eurozone, USA

30. September 2022

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