

Week ahead

US Fed – No rate change, forecasts could move markets

EZ – September industry sentiment expected to remain at high level

Analysts:

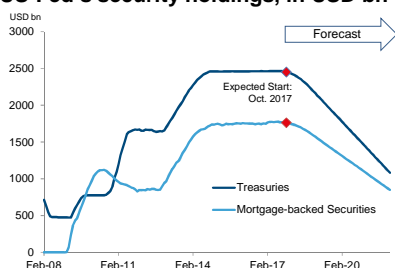
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Will FOMC confirm its forecast of another rate hike before year-end?

The most watched event next week will be the meeting of the US Fed's rate-setting body (FOMC). An interest rate hike is highly unlikely. However, the economic data coming from the US in recent months would not speak against a hike and less support for the economy from interest rates. The data released over the last few weeks showed strong expansion of the economy in 2Q and this is likely to have continued in 3Q, at least until hurricanes Harvey and Irma hit. The devastation caused by the two hurricanes is likely to trigger a severe drop in the economy's growth rate compared to 2Q, although only temporarily. The growth dynamics of the US economy will be decisive; these were only interrupted by the hurricanes and should again lead to a higher pace of growth in 4Q. The inflation indicator most relevant for the FOMC (PCE core inflation) has come down considerably compared to the initial months of the year. However, this was due to one-off impacts from very few product categories, a fact that was also acknowledged by the FOMC. Nonetheless, the main reason why a rate hike next week is highly unlikely is the lack of preparation of the markets by FOMC members for such a step. Since the markets are pricing in a zero probability of a rate hike next week, FOMC members would likely have issued a warning if they were planning otherwise, as happened in January and February of this year, when FOMC members "corrected" market expectations for unchanged rates at the FOMC's March meeting.

US-Fed's security holdings, in USD bn



Sources: Federal Reserve, Erste Group Research

So what do we expect from next week's meeting? It will be exciting, even though interest rates are set to remain on hold. The markets will focus on projections by FOMC members. At the previous meeting in June, the median estimate was equivalent to another rate hike before the end of the year. Should this be confirmed next week, a rate hike at the December meeting would become highly likely. A correction of market expectation would follow, as the markets are currently giving a rate hike in December a probability of slightly less than 50%. Further, the FOMC member's outlook for 2018 will be crucial. The median in June called for three rate hikes next year.

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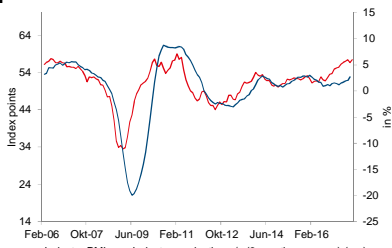
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Indications of past performance are no guarantee of a positive performance in the future

Further, we expect a decision next week on the start of the reduction of the Fed's securities portfolio. The procedure was already announced and foresees a monthly reduction of the portfolio by USD 10bn, which will be achieved by not fully reinvesting principal payments. The monthly amount not reinvested is set to rise by USD 10bn every three months until USD 50bn is reached. At this pace, the so-called balance sheet normalization will take years, even considering that the security holdings will not be reduced to pre-crisis levels, as has been communicated by the FOMC. We expect the start of the whole process to be announced next week for October. We do not expect any significant market impact from this decision, as the FOMC has quite clearly prepared the markets to expect the start of balance sheet normalization before the end of this year.

EZ – September industry sentiment (PMI) expected to remain at high level

EZ: Manufacturing-PMI vs. industry production



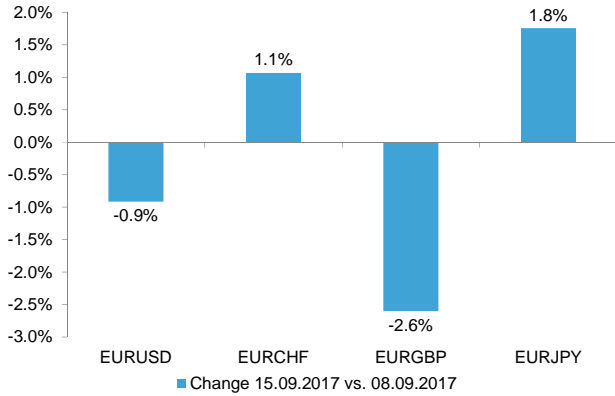
Sources: Bloomberg, Erste Group Research

Next week (September 22), a flash estimate for September industry PMI data for the Eurozone, Germany and France will be released. After a slight decline, sentiment rebounded in August to the record-high levels seen in June. The upswing in August was led by Germany, the Netherlands and Austria. Domestic demand remained robust, whereas foreign demand picked up strongly to levels not seen for 6.5 years. This had a positive impact on order balances as well as job growth. Furthermore, price pressure gained momentum.

We expect Eurozone industry sentiment to remain clearly in expansionary territory in September, although it may slow down somewhat compared to the August data. The global environment remains favorable for the Eurozone, while capital flows to Emerging Markets continued and prices for cyclically sensitive commodities are charging ahead. We expect GDP growth in the Eurozone in 3Q17 of around 2.1% y/y.

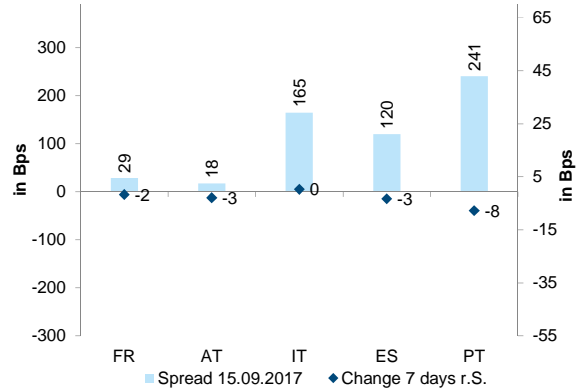
Forex and government bond markets

Exchange rates EUR: USD, CHF, GBP and JPY
change last week
(+ stronger euro / - weaker euro)



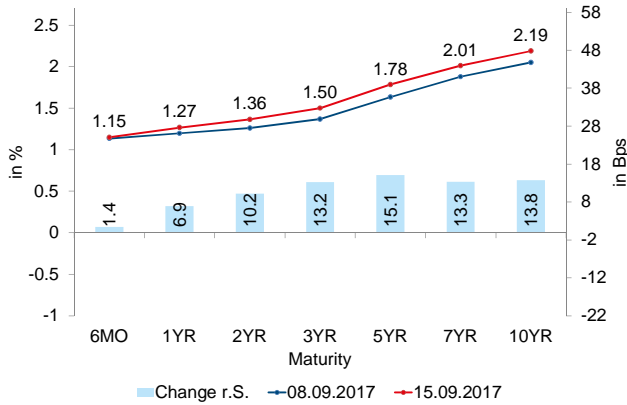
Source: Bloomberg, Erste Group Research

Eurozone – spreads vs. Germany
10Y government bonds



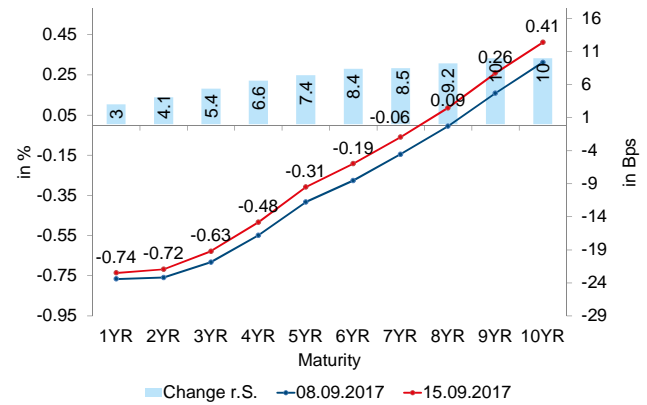
Source: Bloomberg, Erste Group Research

US Treasuries yield curve
change last week



Source: Bloomberg, Erste Group Research

DE Bund yield curve
change last week



Source: Bloomberg, Erste Group Research

Economic calendar

Date	Time	Ctry	Release	Period	Consens	Prior	
15-Sep	n.a.	CN	CNY new loans	Aug	937bn	826bn	
		CN	M2 yoy	Aug	9%	9%	
			US	Ind. Prod. y/y	Aug		2.2%
	11:00	EA	Wages y/y	2Q		1.5%	
		EA	Trade Balance	Jul	21m	22285m	
	14:30	US	Retail Sales mom	Aug	0.1%	0.6%	
	16:00	US	Univ. Michigan Index	Sep P	94.9 index	96.8 index	
18-Sep	9:00	AT	Inflation y/y	Aug		2.0%	
		AT	CPI m/m	Aug		-0.3%	
	10:00	IT	Trade Balance	Jul		4502m	
	11:00	EA	CPI m/m	Aug	0.3%	0.3%	
		EA	Inflation y/y	Aug F	1.5%	1.5%	
19-Sep	10:00	IT	CA Balance (m)	Jul	-1.7 index	5257 m	
		EA	CA Balance (m)	Jul		21 m	
	14:30	US	CA Balance (q)	2Q	-112 m	-117 m	
20-Sep	8:00	DE	PPI y/y	Aug	2.4%	2.3%	
		US	Existing Home Sales	Aug	5.5 m	5.4 m	
	20:00	US	Target Rate	-	1.27%	1.25%	
21-Sep	14:30	US	Jobless Claims	-	310.0 thd	284.0 thd	
		EA	Consumer Conf.	Sep A	-1.6 index	-1.5 index	
22-Sep	8:45	FR	GDP y/y	2Q F		1.7%	
		FR	GDP q/q	2Q F		0.5%	
		EA	CPI y/y	Jul	1.3%	1.3%	
		EA	CPI Core y/y	Jul A	1.1%	1.1%	
	9:00	FR	PMI Manufacturing	Sep P		55.8 index	
	9:30	DE	PMI Manufacturing	Sep P	59.1 index	59.3 index	
	10:00	EA	PMI Manufacturing	Sep P	57.3 index	57.4 index	

Source: Bloomberg, Erste Group Research

FORECASTS¹⁾

GDP	2014	2015	2016	2017	2018
Eurozone	1.2	2.0	1.8	2.0	1.8
US	2.6	2.9	1.5	2.1	2.2

Inflation	2014	2015	2016	2017	2018
Eurozone	0.5	0.1	0.2	1.5	1.5
US	1.6	0.1	1.2	2.1	1.9

Interest rates	current	Dec.17	Mar.18	Jun.18	Sep.18
ECB MRR	0.00	0.00	0.00	0.00	0.00
3M Euribor	-0.33	-0.30	-0.30	-0.30	-0.30
Germany Govt. 10Y	0.41	0.80	1.00	1.20	1.30
Swap 10Y	0.85	1.10	1.30	1.50	1.60

Interest rates	current	Dec.17	Mar.18	Jun.18	Sep.18
Fed Funds Target Rate*	1.16	1.38	1.63	1.88	2.13
3M Libor	1.32	1.70	1.90	2.20	2.40
US Govt. 10Y	2.19	2.50	2.80	2.90	3.00
EURUSD	1.19	1.15	1.13	1.14	1.16

*Mid of target range

Source: Bloomberg, Erste Group Research

¹ By regulations we are obliged to issue the following statement: Forecasts are no reliable indicator for future performance

Erste Group Research

Week ahead | Macro, Fixed Income | Eurozone, USA

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