Week Ahead

25th – 29th October 2021

MONEX

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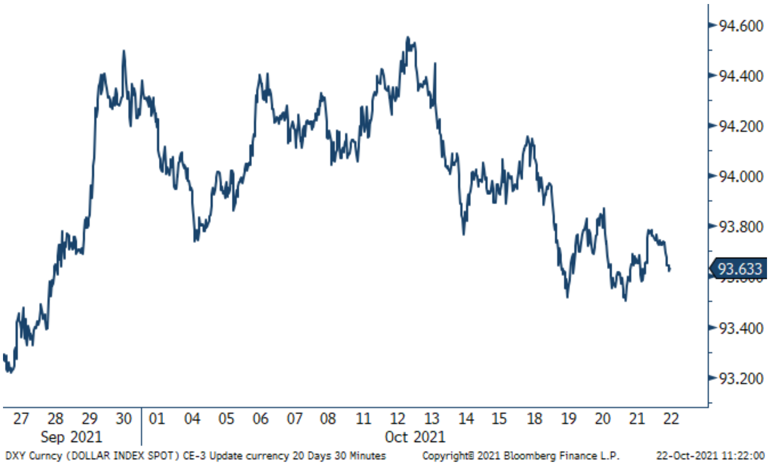
Central banks to take centre stage ahead of crucial GDP readings

Inflation talks from Bank of England Governor Andrew Bailey heightened markets' senses at the start of the week as his comments confirmed action will need to be taken soon, but market pricing continues to differ significantly from economists' views on the BoE's reaction function. The pound rose to new October highs throughout the week, although a bout of USD weakness also contributed to this. A 15bp rate hike from the Hungarian National Bank was not enough to provide support to the forint this week, with USDHUF even rising to Nov 2020 levels. On Thursday, the CBRT turned markets upside down when it announced a surprise 200bp rate cut, which was thoroughly felt by Turkish assets. A flurry of central bank meetings take will place across the globe next week, while Q3 GDP prints from the US and eurozone will take centre stage on Friday. Several countries will also release inflation readings. Among the central bank meetings are the Bank of Canada, the Bank of Japan and the European Central Bank - in order of importance. The BoC is set to continue its tapering process, while the BoJ and ECB are expected to keep policy on hold. The BoJ meeting will, however, catch some eyes as the Bank will release fresh economic forecasts, while the ECB meeting may likely not be market-moving.

USD strength running out of steam with DXY index trading below 94 throughout the week



Calendar (all times BST)

Monday – 25/10

At 09:00, German Ifo indices for October are set to slow down from September's releases in all three indices: expectations, current assessment, and business climate. Delayed growth is the main reason for this, and this will likely be a topic of conversation in the ECB meeting on Thursday as well.

At 14:45, markets will receive the final weekly purchase data from the ECB's Pandemic Emergency Purchase Programme (PEPP) before the policy decision on Thursday. The data should confirm the slowdown in PEPP purchases announced in the September policy meeting.

Monday also marks a bank holiday in Australia and New Zealand.

Tuesday – 26/10

Tuesday's agenda is light on the calendar, with **US consumer confidence for October and US new home sales for September at 15:00** being the only releases of note, while no relevant central bank speakers are scheduled for the day. US new home sales beat expectations last month and increased for a second month, but reports from the Commerce Department indicated demand for housing may have peaked after the pandemic-fuelled buying frenzy.

Wednesday – 27/10

Australia's Q3 CPI is first on the agenda at 01:30 and is expected to rise by 0.8% QoQ, or 3.1% YoY in the headline figure, while the core print is expected to rise 0.5% QoQ and 1.8% YoY. Last quarter, Australia's CPI rose 0.8% while the annual rate rose sharply to 3.8% YoY due to base effects. The core figure remained below the RBA's 2-3% inflation target however, as it printed at 1.63% YoY. The further expected rise in Q3 is primarily driven by rising prices for fuel and motor vehicles, although motor vehicle inflation remains much more muted in Australia than in the US. **At 07:00, German GfK consumer confidence for October** is set to slow down from September's release from 0.3 to a negative 0.3.

> **US durable goods orders at 13:30 BST** will then be eyed by markets after last month's reading showed a sharp increase despite ongoing supply constraints.

At 15:00, markets turn to the Bank of Canada decision. Economic fundamentals point to continued tapering by the BoC, which means the end of QE is in sight. More on this on page 4. **At 17:00, Russian industrial production** will be watched by markets after the previous reading decelerated to a below consensus 4.7% YoY. The slowdown in industrial output points to a cautious mood in manufacturing despite the easing of OPEC+ restrictions on oil output.

Thursday – 28/10

The Bank of Japan announces its policy decision on Thursday (time TBA). While policy is expected to be kept on hold, the Bank will release its latest growth and inflation forecasts. The BoJ may cut its near-term GDP growth forecasts as the economic rebound has been delayed due to an extension in the state of emergency to September 30, while the inflation outlook may be upwardly revised to account for higher energy prices.

At 08:55, Germany's unemployment figures will catch markets' eyes. Germany's successful furlough programme kept domestic unemployment at bay over the last year, which meant that the country saw the smallest uptick in unemployment compared to France, Italy, Spain, the UK and the US. In September, Germany's labour market recovery slowed as the reopening boom lost momentum, but the labour market remains robust compared to other nations. **At 09:00, several Italian confidence indicators** are released while at 10:00, the eurozone comes out with consumer, economic and industrial confidence figures. All of these are set to reflect the slowdown in growth momentum. **At 12:45 BST, the European Central Bank releases its policy decision** followed by the usual press conference 45 minutes later. The ECB may as well have taken annual leave on Thursday, expectations for policy changes are low given September's changes to the pandemic QE programme are still recent and next week's decision does not come with any fresh macroeconomic projections. More on this on page 5.

Friday – 29/10

The last trading day of the week is packed with important data releases for markets, starting with **Japan's jobless rate at 00:30** and **Japan's industrial production at 00:50**. The extension of the state of emergency to the end of September likely means new hirings were limited last month, while industrial output likely also fell in September due to the extended Covid measures. Beyond this, shortages of chips limited shipments of transportation equipment. **Australian retail sales at 01:30** are set to show a 0.3% increase after August's retail sales dived for a third straight month given half the population were trapped in lockdowns. Many restrictions have now been lifted, meaning that markets likely won't be sensitive to any downside surprises to the data as relief is in sight. **Between 06:30 and 10:00, Germany, France, Italy and the eurozone as a whole will release Q3 GDP figures and monthly CPI prints**. These are the highlights of this week's calendar for the eurozone and markets will likely take cues from these releases. **Polish CPI for October at 09:00** will be eyed by markets after the hawkish surprise from the National Bank of Poland earlier in the month following a 20-year high in domestic inflation.

> **Canadian GDP for August is then released at 13:30.** An initial estimate by Statistics Canada showed August's GDP may increase by 0.7% MoM after the 0.1% contraction in July.

Also at 13:30 will be US personal spending data. With both the Canadian and US releases being of note to markets, FX markets may be more difficult to navigate through around the releases as they are released simultaneously. **Finally, Russian unemployment and retail sales figures for September will be watched by markets at 17:00**. The jobless rate is set to remain unchanged at the two-year low of 4.4%, but markets will watch for changes in real wages as these grew slower than expected in July. Retail sales are set to grow by 5.8% vs 5.3% previously.

The Russian economy is on track to post its strongest growth since 2011, but a new downside risk is looming as Russian Covid-related deaths and hospitalisations have been surging and President Putin is now expected to introduce nationwide restrictions.

BoC Preview

BoC QE coming to an end as economic fundamentals encourage normalisation

Economic activity is in decent shape, inflationary pressures look to persist, and the 3 million jobs lost to Covid-19 have been recovered: all arrows are pointing to another taper by the Bank of Canada in next week's policy meeting. We expect QE purchases to be tapered further by another C$1bn per week, with a final taper pencilled in for December.

> "While the economic fundamentals encourage a further taper in October, **we think it would be premature for the BoC to bring its QE programme to a full stop next week."**

The likelihood that growth will remain soft in the very near-term signals to us that the BoC will not opt for ending its QE programme completely next week, but instead will continue its gradual exit. The idea of delayed growth in the context of supply-chain disruptions is likely to be formalised within the Bank's projections, which are released alongside the policy decision.

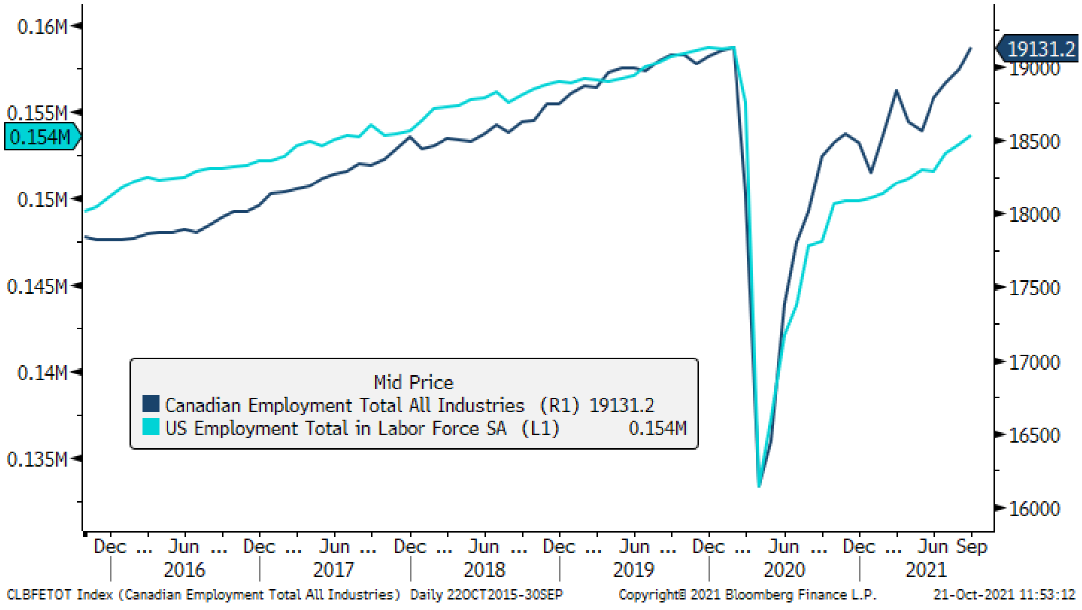
Economy in decent shape but growth looks to be delayed

Statistics Canada reported at the start of October showed that GDP fell by 0.1% MoM in July. While this is a negative reading, markets were positively surprised as it is an improvement from the flash reading of 0.4%. Construction activity and manufacturing declined amid the supply shortages, although for construction specifically it concerned a drop from record highs. The institution's flash reading for August's monthly GDP suggests a 0.7% increase MoM. Though positive, it is not robust enough to drive quarterly growth near the BoC's annualised Q3 forecast of 7.3%. The delay in growth will likely be reflected in the BoC's projections next week, but given that the growth outlook going into 2022 looks more robust, it shouldn't stop the Bank from continuing to normalise its policy. Given Canada's export position in the energy market, the high energy prices will be less of a concern for Canada's inflation compared to energy importers, while it will stimulate domestic GDP growth going into next year.

Labour shortages further building up inflationary pressures

While our house view had always been for the Bank of Canada to continue tapering in October, the Autumn Business Outlook Survey (BOS) released on Monday only further confirmed this view as it had hawkish written all over the report. The BoC highlighted that the worsening labour shortages and supply chain disruptions are leading to higher wages and inflation. Roughly two-thirds of the firms surveyed expect wage growth to be higher over the next year as these labour shortages have intensified over the last twelve months. The labour market has now returned to pre-pandemic levels in terms of employment, however, at the same time the nation is grappling with record numbers of vacancy rates. In an environment of demand being robust and supply struggling to keep up, the labour shortages, which are now starting to lead to wage inflation, could contribute to more prolonged inflation in the medium-term.

Canadian employment back to pre-pandemic levels while US looks to return at a slower pace



Next week's taper should keep the BoC on track to hike rates in the latter half of 2022 at the latest, while expectations are growing for the Bank to announce their first rate increase in the first half of 2022. This is despite slowing economic activity as this is set to be a near-term risk. We expect the normalisation cycle, along with higher crude oil prices, to support the Canadian dollar in the shorter term and partly shield it from the recent USD strength. Once near-term headwinds from inflation and supply chain disruptions subdue, the loonie should continue to rally over the more medium-term following the improvement in the global macro backdrop.

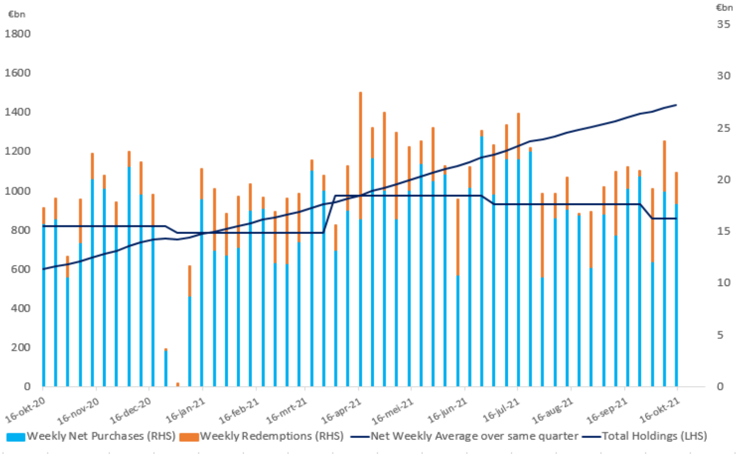
ECB Preview

October's meeting unlikely to move the euro, but markets will take any hints they can get for the December meeting

Next week's European Central Bank decision is unlikely to be a big market event given the recent changes to the ECB's Pandemic Emergency Purchase Programme (PEPP). In September, the central bank announced it would move to a "moderately lower pace" in its PEPP purchases compared to the previous two quarters, based on a joint assessment of financing conditions and the inflation outlook. While next week would be too early to announce any new policy forms, the ECB will have to start laying the foundations for bigger decisions to be made in December. These changes could include increasing the pace of monthly bond-buying through the Asset Purchase Programme (APP) in March when PEPP expires, or additional measures. According to reports, the ECB is studying a new bond-buying programme to replace PEPP and complement APP, to avoid the cliff-edge effect in markets when demand suddenly drops after PEPP has ended. The new programme was discussed by anonymous officials who spoke to Bloomberg on the matter.

The fade-out of PEPP and the ECB's strategy to avoid the cliff-edge effect is unlikely to be discussed in great detail in next week's meeting already, but instead, President Christine Lagarde is likely to focus on the inflation outlook and maintain her view that the recent surges in inflation are unlikely to persist. The ECB's focus on the transitory nature of the current supply chain disruptions and upticks in inflation will make it easier to justify changes to APP, or any additional measures taken after the March expiry of PEPP. In this regard, the October meeting serves as a warm-up event for the December announcements.

ECB reduces PEPP purchases in Q4 below Q2 and Q3 levels as the end of PEPP nears



While the doves at the ECB seem to generally hold Lagarde's views on price pressures, namely that inflation will fade in 2022 and remain below the 2% target, the hawks at the ECB appear to be growing increasingly impatient. September's meeting minutes revealed concerns among the hawks around inflation being more persistent, while they also raised doubts about the central bank's models to capture precisely how the economy is currently recovering. Just as the hawkish members were becoming more vocal about their dissent with the policy outlook, Bundesbank President Jens Weidmann resigned from his position. There may have been different reasons for the Bundesbank President to resign than his views on inflation, however he did leave with one last warning. "It will be crucial not to look one-sidedly at deflationary risks, but not to lose sight of prospective inflationary dangers either," he told the staff before leaving. As the dissent between members of the Governing Council hasn't gone unnoticed by markets, Thursday's Q&A at the press conference will likely challenge Lagarde on her inflation views, especially given the recent gas pains across Europe, while labour shortages add to wage inflation. Beyond that, Thursday's meeting will likely be a placeholder event for markets before they turn to the exciting exit announced in December.