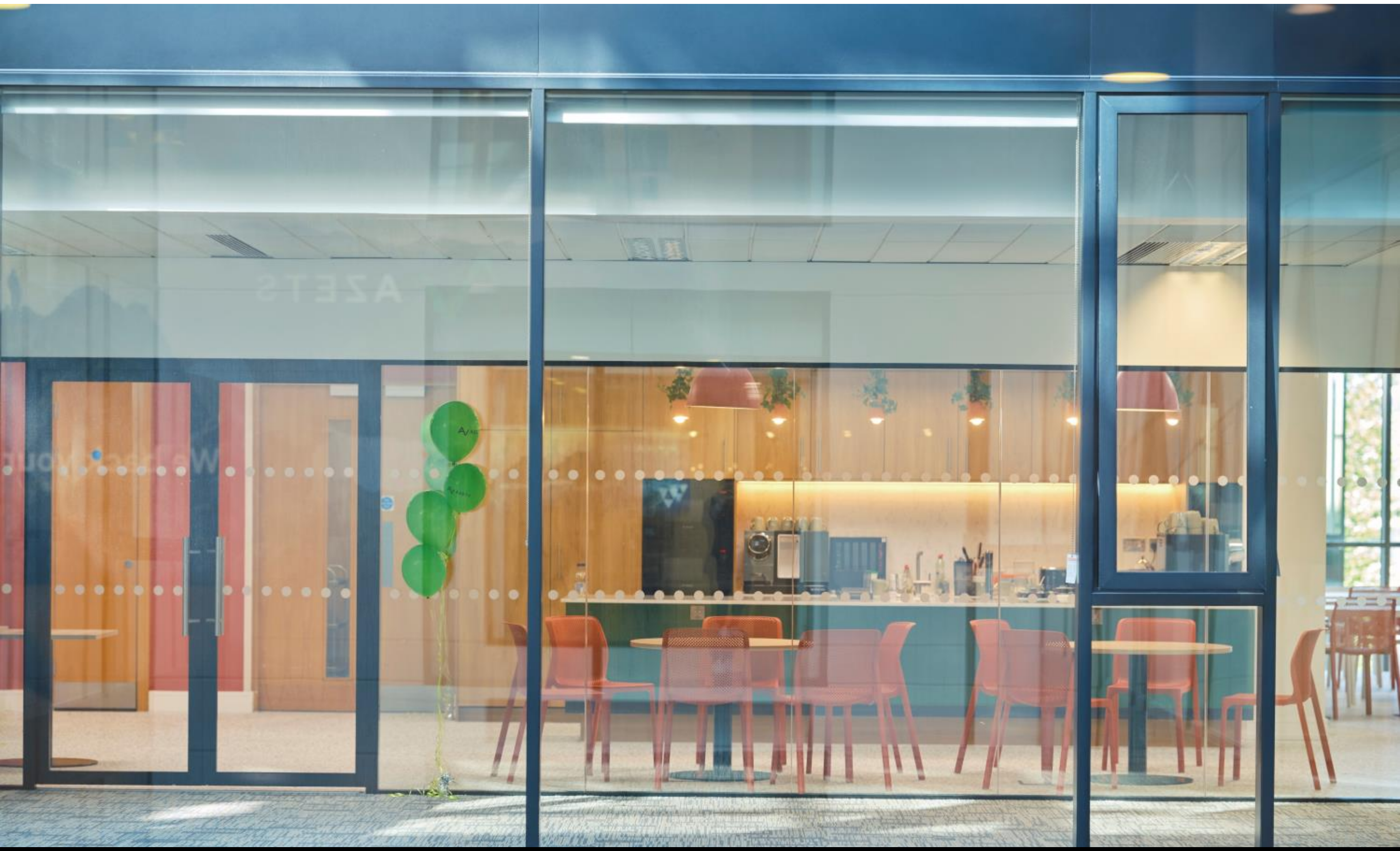
THE TREASURY HUB
Markets Bulletin

Q3 2024 Review



1. Executive Summary

1.1 Introduction

Welcome to the 2024 third quarter 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. Table 1 across sets out the year-to-date movement in a number of key metrics. What is notable is both the continuing increase in value of various asset classes and the gradual easing (for the most part) in longer-term interest rates in response to the slowing of inflation.

The focus of markets in the third quarter continued once again to be on inflation and its impact on the expected timing of interest rate cuts. We have correctly predicted the ECB rate cuts in June and September so far, mainly because we believed that inflation would be slower to fall than expected by others in the market.

- 3-month Euribor has fallen over the last quarter in line with the actual (and anticipated) cuts in the ECB Base Rate. The ECB Deposit Rate has been cut from 4.00% to 3.50% and, as the rate is expected to be cut by a further 0.25% at the October meeting, 3-month Euribor has already fallen to 3.25%
- EUR, UK and US yield curves continue to be inverted (i.e. rates decline after 1 year) but the curves are beginning to flatten out as the bottom of the cycle is now being anticipated
- Oil prices have jumped around quite a bit over the past week or two in response to Middle East troubles

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

Table 1. Key Metric Movements: 2024

Heading	Metric	YTD move	From	To
Interest	3-m euribor	-0.68%	3.93%	3.25%
Interest	EUR 3-year	-0.12%	2.55%	2.43%
Interest	GBP 3-year	0.33%	3.92%	4.25%
Interest	USD 3-year	-0.09%	4.01%	3.92%
FX	EUR/GBP	-3.35%	0.8672	0.8391
FX	EUR/USD	-0.56%	1.1042	1.0981
Equities	ISEQ	9.93%	8760	9630
Equities	FTSE 100	7.37%	7733	8303
Equities	Nasdaq	19.59%	16667	19932
Commodities	Brent Crude	4.26%	77.39	80.69
Commodities	Carbon	-20.98%	78	61.65
Commodities	Gold	27.40%	2077	2646
Inflation	EU Core	-0.60%	3.30%	2.70%
Gilts	IE 10-yr	0.21%	2.41%	2.62%
Gilts	GB 10-yr	0.61%	3.60%	4.21%
Gilts	US 10-yr	0.00%	4.02%	4.02%

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.**

- Gold has continued a record run to new heights over the year increasing in price again over Q3
- Stock markets continued to drive higher in 2024 despite a couple of periods of retracement with the Nasdaq still performing very well despite the relatively high multiples that current prices represent
- Government borrowing (gilt) rates have also bounced around a lot as the markets continue to reassess the pace and number of interest rate cuts in 2024
- GBP has remained stronger than probably anticipated by most, mainly due to UK interest rates remaining higher than their EUR equivalent rates.

1.2 Forward-looking Indices

Forward-looking indictors 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.

- ROI manufacturing has remained around the 50 mark for 6 months while the Construction reading has followed a similar pattern with only Services staying in expansion territory
- In the UK, all three readings continue to remain in positive territory and the trends in general have been favourable for most of the past 12 months. Overall, the UK outlook seems to be in better shape than ROI at the moment.

Table 2. Irish and UK PMI readings

	Ireland	**UK**
Manufacturing PMI	**49.4**	**51.5**
Services PMI	**55.7**	**52.4**
Construction PMI	**50.0**	**57.2**

1.3 Inflation

Table 3. Selected Inflation Rates

	CPI/Core Inflation
ROI	**2.92%**
EUROZONE	**2.70%**
UK	**3.60%**
US	**3.20%**

Note: Core figures exclude energy, mortgages and food.

Irish core rate continued on its downward trend over the course of the past 12 months (it was 6.0% in September 2023) and is now at its lowest level since September 2021. The Central Bank of Ireland forecast inflation (HCIP) to drop to 1.60% in 2024 increasing to 1.90% in 2025.

Eurozone core inflation which peaked at 5.7% in March 2023 has been relatively static since March 2024 and the current level of 2.7% was last experienced "on the way up" in February 2022. The ECB expect headline inflation to average 2.50% in 2024 and 2.20% in 2025.

UK core inflation at 3.6% in August is at its highest level in four months. Headline inflation has fallen to 2.2% (but, again, it has been lower at 2.0% in May and June).

Finally US core inflation rate has declined at a more stable rate over the course of the past 12 months but appears to have plateaued in August**.**

See Section 3 for further comment.

2. Foreign Exchange, Oil & Carbon

2.1 EUR/USD

- Graph 1 looks at the EUR/USD rate trend over the past 12 months
- The high/low range in 2024 to date is 5.79% which remains is by historic standards
- The trend, over Q3, has been a weakening USD at its fastest pace in the year, also resulting in it hitting the year-to-date high of EUR/USD1.1213
- This period of weakness coincided with a market view that US interest rates were likely to fall more quickly than previously estimated
- The year-to-date average rate at EUR/USD1.0873 is very similar to the 2023 figure of EUR/USD1.0821 indicating relative stability in the rate to date over the past 21 months
- How it behaves in the run up to and aftermath of the US presidential election could be crucial.

Graph 1. EUR/USD: 12-month trend

2.2 EUR/GBP

- Similar trend for EUR/GBP: the high/low range for 2024 being only 4.49%, although the average rate for 2024 at EUR/GBP0.8517 is 1.9p lower than the 2023 average of EUR/GBP0.8703
- GBP continues to be supported by relatively high interest rates – Table 1 shows that UK 3-year rates are actually higher than at the start of the year which is the opposite of trends in the US and Eurozone
- And, as already indicated in Table 2, PMI trends are favourable with all three surveys in positive/expansion territory

- As the graph below indicates, the exchange rate continues in a downward trend i.e. strengthening GBP within the range of EUR/GBP0.8300 to EUR/GBP0.8600
- The current year average rate of EUR/GBP0.8517 is the lowest that it has been since 2016 which was the year of the Brexit vote which in itself is of significance as GBP has been in the (relative) doldrums since that vote
- GBP may be further supported in due course if, as expected, the new Labour government makes efforts to align the UK more closely with its European neighbours from a trade perspective.

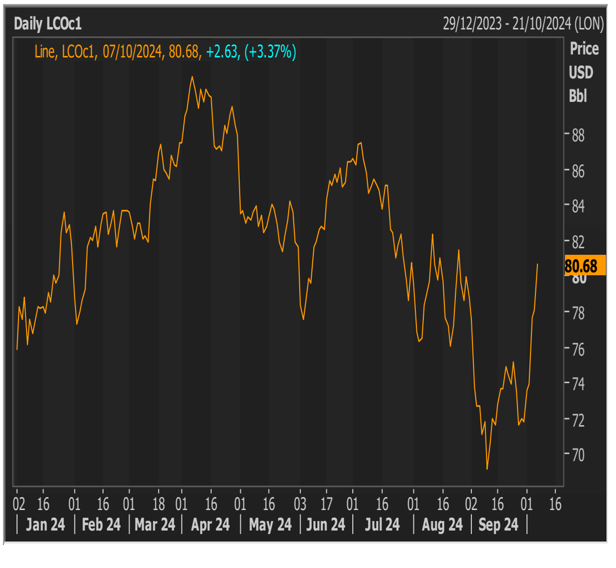
Graph 2. EUR/GBP: 2-year trend

2.3 OIL & CARBON

Brent Crude had fallen quite significantly between April and September mainly due to worries about forecast economic demand globally, especially given a view that the Chinese economic outlook was negative i.e. slowing economy. The price fell below $70Bbl in September but the commencement of the Israeli bombing of Lebanon coupled with the possible threat of an escalation of events with Iran has driven the price back above $80Bbl over the past 2 weeks.

The price of Carbon has been erratic with current levels well below the average price of the past 2 years.

Graph 3. Brent Crude: 2024 trend



Graph 4. Carbon: 2024 trend

3. Interest and Economic Review

3.1 EUR Short-term Rates

Interest rates continue to dominate market events and commentary over Q3 as they have done for all of 2023 and 2024. 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

- As we have noted before, the 3-month Euribor tracks the ECB Base Deposit Rate very tightly. As the former changes every day while the latter only changes on ECB meeting dates, Euribor tends to anticipate the ECB move a few weeks in advance
- The graph below shows 3-month Euribor at 3.25% and this is where we expect the ECB Deposit Rate to be after the ECB meeting in October i.e. another 0.25% cut from 3.50% to 3.25%)
- With no meeting in November, there is only time for one further cut at most in 2024 in December. The markets expects another 0.25%. We think it’s a 50:50 chance as inflation looks like it may stabilize around current levels although the economic outlook is also a little uncertain which would support a view for further cuts.

Graph 5. 3-month Euribor: 24-month 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 3-year fixed rate (before margin) dropped by 1% between the end of June and the end of September hitting a low of 2.12%
- This was a very large move in a short space of time driven by a view that ECB Deposit Base Rate might bottom out at 2.00% rather than 2.50%.

Graph 6. EUR 3-year swaps: 24-month trend

3.3 Summary

- While movements in short-term rates were as expected in the quarter, the scale of the reduction in the longer-term rates was surprising. The reversal that arose since puts the ECB Deposit Base Rate bottoming out at 2.25%
- We previously opined that they will only cut twice in the second half of the year (including September) and we believe that they will cut in October but are less confident of a December cut for now. The data will drive that decision
- While the interest rate curve remains inverted with 1-year, 3-year and 5-year rates (ex margin) at 2.77%, 2.49% and 2.41% respectively, it is beginning to flatten
- This suggests that the bottom of the current interest rate cycle will arise in 2025.

3.4 UK and US Interest Rates

- **Graph 7 below shows that the UK 3-year rate has behaved in a somewhat similar fashion to EUR interest rates with the reversal even more pronounced in the past 3 weeks (up by 0.40%)**
- **Markets got too enthusiastic about the pace of rate cuts it would appear.**

Graph 7. GBP 3-year swaps: 12-month trend

Graph 8. USD 3-year swap rates: 12-month trend

- US longer-term rates have had a volatile ride since 2023. The fall off in rates in Q4 2023 as markets anticipated as many as 7-8 cuts in the US in 2024 was quickly reversed over Q1/Q2 as the number of cuts was continually revised downwards
- And while the inflation trend is going the right way (see Section 1.2 above) and the Fed cut by 0.50% in September and indicated two more 0.25% cuts in the remaining meetings in November and December, other indicators suggest that this may also be too much too soon
- Unemployment data surprised on the upside with the rate falling to 4.1% as the numbers employed grew by 254,000 in September while GDP grew by 3.0% in Q2
- Q2 corporate earnings held up well while the US Stock Market Index is at an all-time high
- Durable goods orders have been very strong over the past 6 months
- All of these indicate that the US could be heading for a soft rather than hard landing at worst although there are also risks on the horizon
- China has been boosted by fresh stimulus but the effects of it are wearing a little thin as their stock markets have tumbled in the past week
- Asset prices (shares) have been undoubtedly helped by the large fiscal stimulus of the US government
- The scale of it is reflected in the fact that the US Debt: GDP ratio is at 122% and the growth in this would be reflected in the fact that the US has not run a budget surplus since 2001. This is not sustainable in the long run, despite the contrary view of many in the US
- **So, there are good reasons for thinking that US interest rates will not fall as far or as fast as the market currently thinks.**

3.5 Summary

- **Yield curves (which graph all interest rates from short to long-term) are changing shape from inverted (where longer-term rates are lower than short-term rates) to flattening and this, in turn, indicates that the financial markets now see the end of the rate cutting cycle arising over the next 12 months or so in the Eurozone, UK and US**
- **The markets remain uncertain as to the timing and scale of the remaining interest rate cuts in all main economies**
- **But current forward/forward annual rates show the bottom of the cycle as being 2.30% in the Eurozone, 3.60% in the US and close to 4.00% in the UK**
- **These remain subject to change as markets continue to re-evaluate data**
- **In addition to all of the above, geo-political events will be critical with the US presidential election outcome not just having ramifications for US economic policy but also on how the war in Ukraine develops, how far Israel goes in its interactions with its neighbours and how the relationship with China develops.**

4. Wealth Management

4.1 Gold

Graph 9. Gold prices: 2024 trend

- Gold is the asset class that continues to surprise in its ascent. It has gone from USD2,000 in Q1 2024 to a current level above USD2,600
- Traditionally it has been seen as a safe haven in the event of financial market uncertainty but as mentioned in previous bulletins, there has also been a drive by Chinese asset holders to liquidate some of their US Government Bond portfolio and switch such holdings into Gold which has also driven the price of Gold higher.

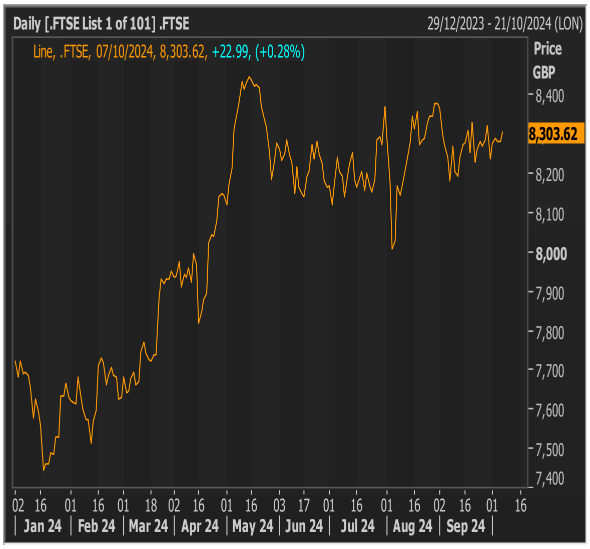
4.3 Equity Markets

Equity markets have had a very solid 2024:

- ISEQ up 9.9%
- FTSE up 7.4%
- NASDAQ up 19.6%.

Graph 10. ISEQ: 2024 trend

Graph 11. FTSE: 2024 trend



Graph 12. NASDAQ: 2024 trend

US stock market PE ratios (ratio of the average share price to the earnings per share) continue to increase.

Current levels (with comparative figure for 12 months ago) are :

- S&P 500 – 24.35 (20.14)
- Dow Jones Industrial Average – 26.17 (24.43)
- Nasdaq 100 – 31.68 (29.27)

The impact of a small number of large cap companies also distort the data somewhat.

The bottom line is that valuations look very high by historic standards so a correction at some stage shouldn't be a surprise. But what will cause it?

5. Budgeting for 2025

In starting to produce budgets for 2025, companies need to consider a number of economic and financial variables. This section looks at the current outlook for a number of them.

5.1 Interest Rates

This is best examined by looking at forward/forward interest rates. The table below highlights in yellow the current forecast of where 1-year rates (before margin) will be in 1,2 ,3 and 4 years time

Table 4. EUR forward rates

EUR Rates (annual)		Implied rates in			
	Now	1 Year	2 Year	3 Year	4 Year
1 Year	2.770	2.211	2.310	2.350	2.410
2 Year	2.490	2.260	2.330	2.380	2.470
3 Year	2.430	2.288	2.354	2.428	2.478
4 Year	2.410	2.320	2.400	2.448	2.510

This would suggest that short-term rates before margin should be budgeted for 2025 at 2.30% to 2.50% based on the current yield curve

5.2 FX Rates

These are always very difficult to forecast given the relative volatility of them. In their most recent outlook AIB forecast weaking USD in EUR/USD1.11-EUR/USD1.17 range with GBP in a EUR/GBP0.82-EUR/GBP0.88. Bank of Ireland wasn’t much different although they saw the bottom of the GBP range at EUR/GBP0.84. The tables below show the high, low and averages for the past 5 years in EUR/USD and EUR/GBP.

EUR/GBP has been relatively stable over the past few years and with the interest rate differential likely to persist, it is currently difficult to see recent ranges not persisting. EUR/USD is more difficult to call as a result of political consequences of the presidential election outcome but we think that the risk may be on the downside i.e. weaker USD due to political uncertainty.

Table 5. EUR/GBP trends

EUR/GBP	High	Low	High to Low %	Average
2024	0.8682	0.8309	4.49%	0.8517
2023	0.8979	0.8492	5.73%	0.8703
2022	0.9229	0.8201	12.54%	0.8527
2021	0.9085	0.8365	8.61%	0.8601
2020	0.9500	0.8280	14.73%	0.8896

Table 6. EUR/USD trends

EUR/USD	High	Low	High to Low %	Average
2024	1.1213	1.0599	5.79%	1.0873
2023	1.1275	1.0447	7.93%	1.0821
2022	1.1495	0.9534	20.57%	1.0538
2021	1.2349	1.1184	10.42%	1.1832
2020	1.2349	1.0635	16.12%	1.1415

5. Budgeting for 2025

5.3 Economic Outlook

A summary of forecast of key variables as per the Department of Finance underpinning the recent Budget is set out below

Table 7. Forecast Economic Variables 2025

Variable	
Real GDP	3.9%
Real GNI	2.7%
Core Inflation	2.3%
Unemployment	4.5%
Surplus	€9.7bn
Surplus*	€-5.7bn

*** The figure excluding one-off corporation tax contributions**

The above figures are positive and indicate a stable economic outlook. Consumer spending which is a key part of economic demand is forecast at +3.2% in 2025. The outlook for 2026 is broadly comparable.

The one risk (and standout figure for the wrong reasons) in the above is the scale of the one-off corporation tax contributions. This figure is €13.4bn as a surplus of €9.7bn would be a deficit of (€5.7bn) without them. What is also disconcerting is the Department's forecast to 2030 show government debt increasing from €217bn at end 2024 to €234bn by 2030 despite forecast surpluses for each year.

The biggest risk to these corporation tax receipts are probably a Trump election win as he could decide to tax US company profits regardless where they are earned globally (or some variation of that) which would render the low tax rates in Ireland less valuable and attractive. And that could change very quickly although one would expect significant pushback from US corporates not least as it would also reduce their after-tax profits and EPS which would likely impact negatively on share prices.

In summary, the interest rate outlook looks good (lower rates), GBP should hold up but USD could be more volatile while the overall economic outlook is positive but very open to geo-political developments.