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## From policy announcements to central bank speakers

This week, FX markets were dominated by fresh monetary policy announcements. The most notable came from the Federal Reserve, the Bank of England, the Norges Bank and the Central Bank of the Republic of Turkey. Firstly, the [Fed signalled a faster tapering](#) of the QE programme, with Chair Powell stating that the tapering process would likely conclude in the middle of 2022. However, with the median dot plot failing to show a definitive rate hike in 2022, the Treasury curve steepened as the bulk of the hiking cycle is set to take place over the 2-5 year horizon. The impact on the dollar was mixed, with the greenback initially rising but failing to hold onto gains over the course of the week. On Thursday, the [Norges Bank](#) raised their projected hiking path beyond the middle of next year, while the [Bank of England](#) followed in the NB's hawkish footsteps to suggest rate hikes could come as early as November's meeting. The hawkish signals compounded the risk-on pricing in G10 markets that day, while the [CBRT bucked the general tightening trend](#) by lowering the policy rate by 100bps to 18%, sending the lira to fresh all-time lows.

**"Next week's focus quickly shifts from policy announcements to individual central bankers** as a swathe of speakers fill the economic calendar, largely due to the ECB's forum on central banking taking place between the 28th and 29th of September."

Rather than being in Sintra (Portugal) as has been customary, the event will take place online. The topic of the forum is "Beyond the pandemic: the future of monetary policy" and includes speeches from global central bank leaders along with individual Governing Council members.

## Calendar

### Monday – 27/09

Most of the focus on Monday morning will be on the results of **Sunday's German elections**, which usually yields conclusive results within hours of polls closing (see more on [page 4](#)). Beyond the election results, central bank policy will remain in focus, with **ECB President Christine Lagarde speaking in a parliamentary hearing at 12:45 BST**, before the first Fed president since Wednesday's meeting, **Chicago's Charles Evans, speaks to the public at the NABE Conference at 13:00 BST**. Sticking with the Fed, New York Fed President **John Williams is to make opening remarks at 14:00 BST** at the conference on culture and then speak again at the **Economic Club of New York at 17:00 BST**.

The latter event is likely to be the one to deliver the market headlines as the economic outlook is directly discussed. **At 17:15 BST, Lael Brainard**, who like Williams is a prominent figure within the FOMC, is set to speak at the NABE conference, while the **Bank of England's Governor Andrew Bailey rounds up the day at 19:00 BST** as he speaks at the Society of Professional Economists annual dinner following the latest hawkish policy statement and recent rise in inflation.

## Tuesday – 28/09

The focus temporarily diverts from central bankers to economic data on Tuesday, with **German GfK consumer confidence data for October released at 07:00 BST**, while **French consumer confidence data for August is released at 07:45 BST**. The month-on-month changes are set to be slight, with the German index set to deteriorate further from -1.2 to -1.3, while the French measure is set to improve from 99 to 100. **At 10:30 BST, South Africa's Nonfarm Payrolls data is released for Q2** and will be viewed in context of the upwards surprise in Q2 GDP and a dovish SARB.

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Headlines are then set to shift back to the monetary policy space, with **ECB President Christine Lagarde opening the ECB forum on central banking at 13:00 BST**.

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As the ECB event begins, the latest appointment to the **Bank of England, Catherine Mann, is set to speak on the panel at the National Association for Business Economics at 13:50 BST**. If the Bank's latest monetary policy decision is discussed, markets will likely be braced for dovish commentary. Then at **15:00 BST, Fed President Jerome Powell and Treasury Secretary Janet Yellen speak at a Senate Banking Committee**. Direct policy commentary is unlikely, however, the impact of the debt ceiling debacle may rear its head. To conclude the day, **Atlanta Fed President Bostic discusses his economic outlook at 20:00 BST**.

## Wednesday – 29/09

**The Fed's James Bullard kicks off the Wednesday calendar at midnight to discuss the US economy** and monetary policy, something that will be in extra focus for markets after Wednesday's renewal of the FOMC dot plot as they try to gauge who the swing-voters in the 2022 dot plot were, and if these are voting members. Market participants then turn to **eurozone consumer confidence for September at 10:00**, although this may go unnoticed by FX markets as most focus for the euro will be on Sintra. **ECB's Philip Lane chairs the session at the ECB forum at 15:30 BST**. This panel will concern monetary policy, employment and inequality.

Fireworks are set to conclude the ECB's forum at 16:45 BST, with **BoE Governor Andrew Bailey, BoJ Governor Haruhiko Kuroda, ECB President Christine Lagarde, and Fed Chair Jerome Powell** sitting on the final panel of the event, chaired by Alessandra Galloni, Editor-in-Chief at Reuters. While the conversation title “policy panel” doesn't give much away, it is likely that the conversation will provide some policy and market relevant headlines. The viewership for the conversation is likely to be elevated for this reason.

## Thursday – 30/09

**China's official and Caixin PMIs are set to kick start Thursday's session at 02:00 and 02:45 BST** respectively. The data is set to show a recovery in the manufacturing sector, with the official measure expected to rise from 50.1 to 50.2 and the private series expected to rise from 49.2 to 49.5. Most of the gain in the official composite PMI is due to come from a recovery in the services sector following the containment of August's Covid-19 outbreaks. The official non-manufacturing PMI is set to rise from 47.5 to 50.8. Following on from China's economic output data is the **final Q2 GDP reading from the UK at 07:00 BST** which is set to be unrevised from the preliminary 4.8% print. **French HICP data for September is released at 07:45 BST** and could see inflation rise to close to 3% given the energy regulator announced the cost of gas would jump by 8.7% in September amid the current supply crisis. The impact from rising electricity prices is likely to be delayed until February, however, when the regulator plans to reset the current price cap. **German unemployment data for September at 08:55** is then viewed before the focus shifts to inflation. Net employment is expected to increase by 33,500 in September, which should help bring down the unemployment rate from current post-pandemic lows of 5.5%. **At 10:00 BST, Italian HICP data is released**, which again is likely to be boosted by the recent rise in energy costs. Core measures will be viewed for a better reading of underlying inflation pressures.

Throughout the morning, German regions report CPI readings, however, the nationwide **CPI data at 13:00 BST** is likely to be the one in focus for markets, especially given the recent rise in energy prices in the eurozone and the continuing supply chain disruptions across Europe as a whole.

While the pass-through of market energy prices to households in Germany is relatively more contained than neighbouring countries, headline inflation will still be viewed by markets as concerns over elevated prints begin to intensify.

Moving to North America, the third reading of US GDP for Q2 is pencilled in for 13:30 BST and is expected to see a slight upwards revision from 6.6% to 6.7% on a quarterly annualised basis. Banxico then takes centre stage at 19:00 BST and is widely expected to raise rates for a third consecutive meeting by 25bps following last week's uptick in inflation data. Finishing off the day is New Zealand's ANZ consumer confidence data for September at 22:00 BST. Confidence indices are set to rise from previous months as most of the economy has seen restrictions scaled back to level 2.

## Friday – 01/10

**German retail sales for August are scheduled for release at 07:00 BST** and are set to increase 1.5% MoM after July's 5.1% contraction. **At 09:00 BST, Poland's preliminary CPI for September will be of great focus for EM traders** given Poland's recent spikes in inflation which pushed price growth up to 20-year highs, and the central bank's reluctance to adjust monetary policy as they argue the inflationary pressures are of transitory nature.

This will become increasingly harder to justify if September's print remains elevated, which means the reading poses large downside risks for the zloty. When the August reading printed at the 20-year high, the zloty gained because markets were expecting the National Bank of Poland to turn more hawkish, however, given their recent dovish communication an upside surprise to September's is likely to weigh on the zloty. **Later at 10:00 BST, South African PMIs** are set to slightly decrease down to 56.0 from August's 57.9 reading, but this is unlikely to bear an impact on the South African rand as the currency will take cues from broader risk sentiment in a week full of central bank speakers - unless the PMI figures deviate greatly from the consensus.

Wrapping up the week is **Canadian GDP data for July at 13:30 BST**, which is released alongside **US PCE data for August**. Canada's GDP data may continue to weigh on the loonie following the [shock contraction in Q2](#), as June's reading gave a preliminary estimate that growth continued to contract by 0.4% in July. Focus will rest heavily on both the July reading and the preliminary estimate for August as traders look for signs of a rebound. US PCE data on the contrast is set to hold steady at 4.2% YoY, following the CPI trend that had inflation hold at 5.3% in August earlier in the month.

## German election preview

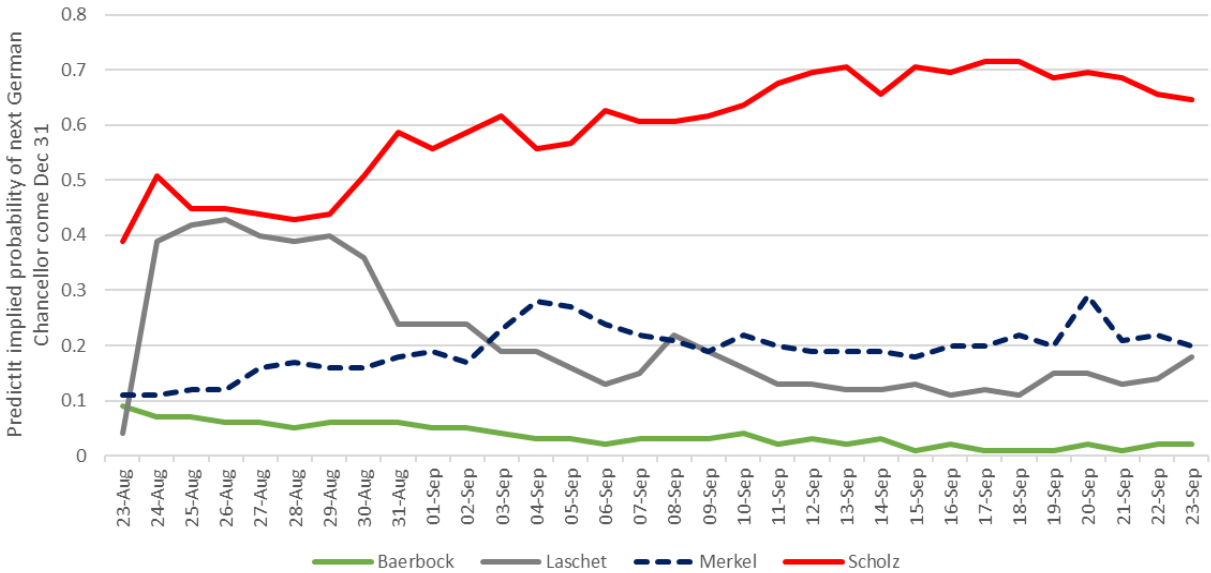
### A clear path for markets seems an unlikely scenario

Germany's federal elections haven't yielded a clear path to form a government since 2009, where the CDU/CSU - FDP coalition was formed within a month of polling stations closing. Since then, plurality and tactical voting have increased, resulting in longer and more arduous coalition negotiations. The 2021 Federal Election is set to extend this theme. Without a decisively popular political party in the current polls, multiple coalition options remain on the table, especially given the collapse in the CDU/CSU's polling and the unlikely chance that they will form a two-party coalition with the SPD following the 2017 disaster. While the SPD's Olaf Scholz looks destined to gain the popular vote, even his path to becoming Chancellor isn't a foregone conclusion. As Volker Bouffier, the premier of the state of Hesse and CDU bigwig, stated, "of course, second-placed parties can also try to form a government". This dawned on FDP leader Christian Lindner over the weekend when he reminded his party of the 1976 election, where the CDU/CSU came first by a comfortable margin and yet it was the SPD's Helmut Schmidt who stayed as Chancellor following a coalition with the FDP.

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With polling incredibly tight heading into Sunday's election and a copious number of coalition blends on the table, the market read through is likely to be difficult.  
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The election outcome should give some clarity on the potential policy path, and thus cause an initial repricing in some asset classes along with a reduction in expected volatility, however, lengthy coalition talks could leave a lingering cloud of uncertainty. This is reflected in the cynicism priced into betting markets, where the probability of Angela Merkel staying on as Chancellor into 2022 amid a political vacuum remains elevated.

**Betting markets continue to see Scholz as the next Chancellor, but a political vacuum with Merkel leading a caretaker government is still seen as the main alternative**



**Coalition probabilities**

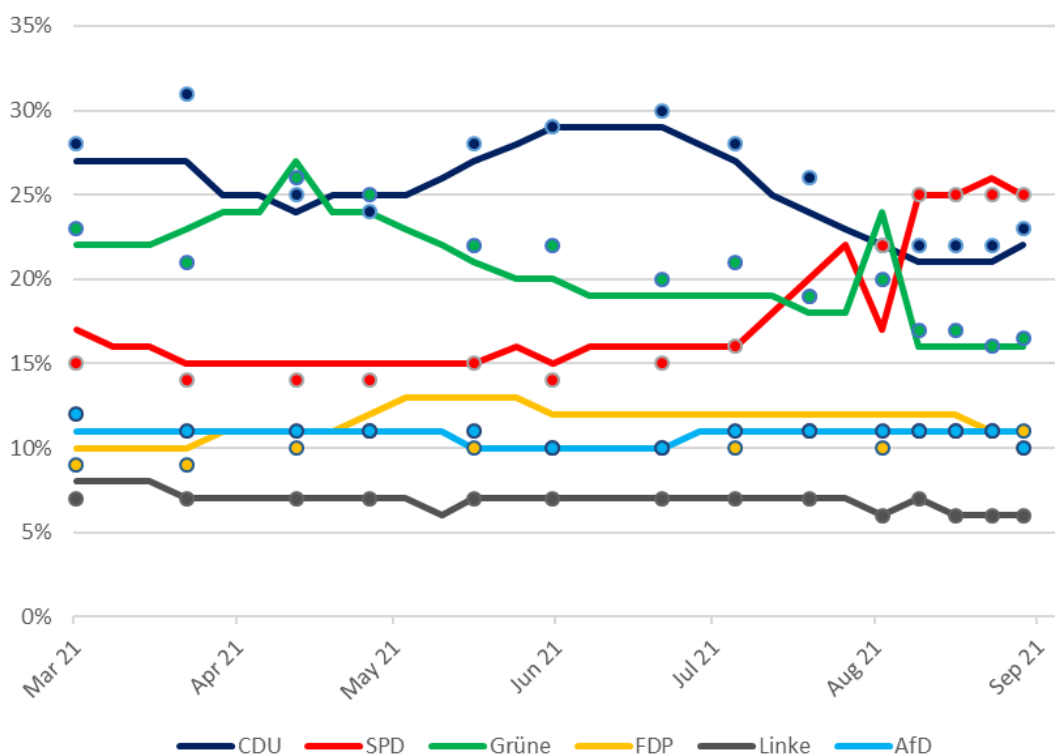
The most likely outcome of the coalition formation process is the Traffic Light coalition, which is formed by the SPD, Greens and FDP. Although the polling margin is only slightly larger compared to the Jamaican coalition (CDU, Greens and FDP), the likelihood of a working Jamaican coalition forming is materially lower given the clashing views on debt and taxation between the CDU/CSU and FDP with the Greens. A third, but least likely, option is the Left coalition consisting of the SPD, Greens and Linke parties. While this is viable, polling suggests it will be difficult for them to achieve the majority of seats. Therefore, a margin of error in current polling would need to occur for this outcome to materialise. The Left coalition is likely to be the swiftest one to form should it garner a majority in the Bundestag, however.

“While polling suggests the Traffic Light coalition is the most likely outcome, its formation still won’t be easy.”

Despite the SPD, Greens and FDP having overlapping policy plans when it comes to investment spending, although the exact methods differ, divergences remain on financing and deficit levels. The SPD intends to preserve the elevated pandemic investment of €50bn/year while the Greens aims to lift investment by another €50bn/year until 2030. While the FDP also aims to keep investment spending elevated, the three parties will have to crunch the numbers together until they are satisfied with the outcome. To allow for these plans to be carried out, the Greens and SPD intend to raise taxes, exploit fiscal room more liberally, or relax the debt brake – a borrowing limit enshrined in Germany’s constitution - entirely. This could cause conflict with the FDP who aim to retain the debt brake after 2022.

In any case, policies under the traffic light coalition will be more fiscally expansive than under the current government, which is positive for eurozone growth as a whole. Further overlaps can be found in welfare policies, where all three parties have ambitious plans to support lower-income groups. Further divergences in policy preferences emerge in the methods proposed to achieve climate goals, for example. The Greens favour a faster rise in CO2 prices and stronger interventions including phasing out combustion engines by 2030, while the SPD is taking a milder approach and wants to make trains more attractive. The FDP would like to see CO2 prices rise also, although their 2060 deadline of CO2 neutrality suggests they are taking a milder approach than the Greens as well. Again, these differences are more related to details and methodology rather than actual goals.

## Politico's Poll of Polls composite vs Forschungsgruppe Wahlen\*

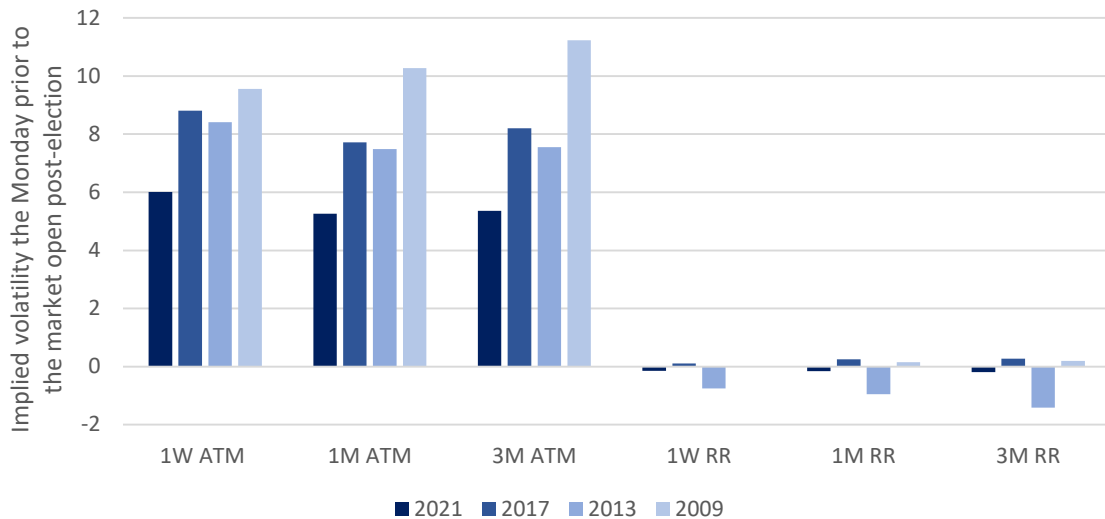


\*Forschungsgruppe Wahlen is the preferred polling method used by ZDF and ARD

## German elections to be instrumental for EURUSD only if they produce a more decisive front-runner

Monday's market open is likely to be a volatile one as traders digest the final results of the German election on Sunday and determine the likeliest coalition options moving forward. Given the tight preliminary polling, numerous coalition combinations are set to be available, despite the most likely option being a traffic light coalition. If the polls are correct, the market reaction come Monday will be limited, largely because the coalition outcome, and thus policy result, remains subject to a high degree of uncertainty. However, any deviation in the final outcome from where preliminary polls are currently printing is likely to not only cause a significant reaction in EURUSD spot, but also reduce near-term implied volatility.

**Options markets remain uninspired by the German election, with EURUSD implied volatility trading lower relative to previous elections while risk reversals also give little indication as to positioning**



*Note: Pricing is taken as of 20/09/2021 such that the 1W horizon covers the market open following the election*

History tells us that the initial EURUSD reaction on the Monday following the German election tends to be negative. However, in elections where a clear path to a coalition is formed due to either the status quo outcome being kept (2002) or a decisive victory by one party (2009), the currency pair tends to post gains over the course of the week. While neither scenario is likely given current polling, signs of a swift conclusion to the period of political uncertainty due to the SPD having numerous coalition options should alleviate some of the political uncertainty surrounding EURUSD.

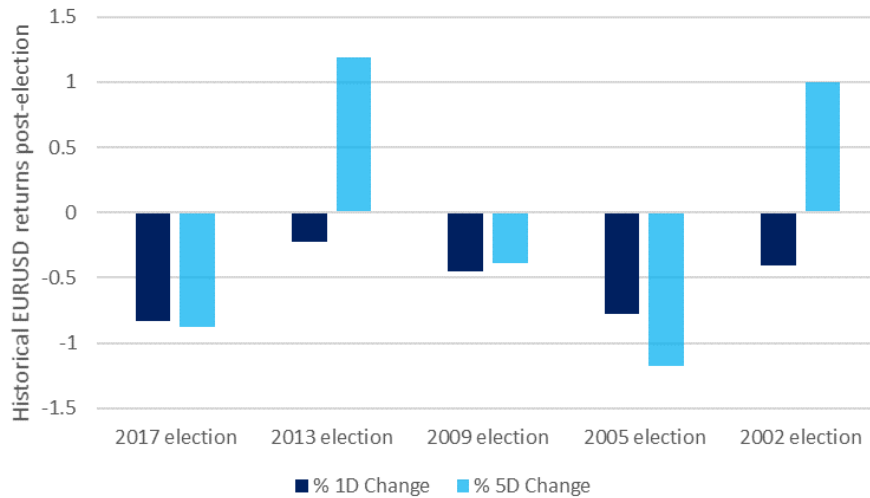


A Traffic Light coalition is likely to bode well for EURUSD given the fiscally expansive nature of the policy mix. Meanwhile, the feasibility of a Left coalition would likely provide the most upside for EURUSD.

This is not only due to the coalition mix having the most overlap in negotiations and the likelihood that policy will be more fiscally expansive, but it would also give the SPD optionality in its coalition choice, which should speed up overall negotiations.

***Beyond the initial reaction, the coalition blend will be pivotal for the eurozone’s growth outlook and ECB policy on the whole. In this regard, more hangs in the balance with respect to the election than just the initial reaction in spot and vol markets.***

**EURUSD's initial reaction to German elections tends to be negative, but decisive results tend to lead to positive returns over the course of the week**



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