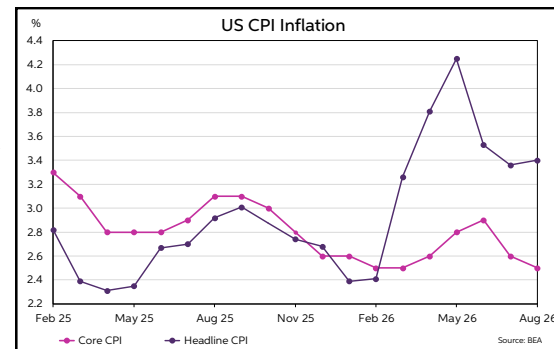


La Vie en Rose

- **European bond markets have continued to be roiled by political uncertainty in recent days, driving a steepening in yield curves, widening spreads for troubled sovereigns, and leading to a depreciation of the euro.** Given the relatively muted trends in headline inflation versus the previous shock in 2022, current market pricing for central bank rates has softened in recent weeks. Nevertheless though, it has drove both the front-end and long-end of the curve since the US-Iran war began. However, underlying this inflationary catalyst, markets are also pricing in greater risk premia on governments with poor records of delivering deficit reduction. France, Italy and the UK continue to stand out, enduring significant increases in borrowing costs, while also seeing spreads widen to safe haven assets such as German bunds.
- **Indeed, political uncertainty in Europe is also now providing a further leg-up to yields.** A snap election called in Spain and street protests in France seeking greater public spending, despite the challenging fiscal arithmetic, are adding to political angst, which was already high following the hollowing out of the centre in a slew of recent regional German elections. French bonds now consistently trade wider than their Italian counterparts, with the 10-year trading between 130-140bps above the German equivalent compared to 100-110bps for Italy. At face value, the widening looks overdone, with both France and Italy running similarly sized deficits of around 5% of GDP, with Italy far surpassing France on its overall debt metric of nearly 140% of GDP versus 118% for its Gallic neighbour.
- **However, the direction of travel matters more for markets.** French fiscal policy has become completely unanchored since President Macron lost his majority in Parliament a few years ago, whereas the political picture in Italy appears stable. There is also a significant risk of a victory for the populist right in the French Presidential election next year, with a firmly anti-EU outlook, which might further weaken European structures at a time of geopolitical uncertainty.
- **The widening in spreads also brings the focus back on the ECB's role, risking a politicisation of the institution.** In 2022, the ECB tweaked the rules around its Pandemic Emergency Purchase Programme (PEPP), to provide greater “flexibility” in how it reinvested the proceeds from the programme. In practice, this allowed the ECB to intervene to underpin the Italian bond market. The central bank subsequently created the Transmission Protection Instrument (TPI), which is a reserve ‘bazooka’ that can, in the ECB's words, “be activated to counter unwarranted, disorderly market dynamics that pose a serious threat to the transmission of monetary policy across the euro area”. **On paper, France would fail the criteria for use of the tool, given it requires compliance with the EU fiscal framework,** but with its perception as “too big to fail”, there could be increasing pressure on the ECB to act if the situation deteriorates further in the coming weeks. Looking further ahead, political instability may remain a driver of bond market volatility in the Euro-area over the coming year. Alongside the aforementioned French Presidential election, elections are due across Europe in 2027, including in Italy and Greece.
- **Turning to the week ahead, the main release of note will be US CPI inflation for September.** In the initial aftermath of the outbreak of the war in the Middle East, headline inflation moved sharply higher, rising from 2.4% in February to 4.2% in May. Similarly, core-CPI also increased, reaching a peak of 2.9% in May, up from 2.5% in February. However, both rates have declined markedly in recent months. The headline rate printed at 3.4% in July and remained at that level in August. Meantime, the core rate fell below its pre-war level to 2.4% in August. However, both rates are projected to rise in September, with the former increasing to 3.7% and the latter to 2.5%.
- **Elsewhere in the US, retail sales and industrial production data for September are also due.** In recent months, the sales data have been somewhat volatile, but the overall trend has been upwards. In July, headline retail sales contracted for the first time since October 2025, falling by 0.6% in the month. However, this was largely due to a change in Amazon Prime Day, which traditionally occurs in July but took place in June this year. Furthermore, headline retail sales rebounded sharply by 1.2% in August. At the same time, the control group measure, a key core sales metric, which strips out expenditure on cars and at fuel stations, jumped by 1.4% in August, following a 0.4% decline in July. A more modest expansion of 0.3% and 0.6% is pencilled in for both rates in September. In terms of production, industrial output is forecast to increase by 0.4% in September, which would be twice the average monthly rise seen so far this year.
- **In the UK, the monthly reading of GDP for August will be in focus.** Recently, growth appears to have gathered steam. In the past two months, GDP has accelerated and printed above the consensus, expanding by 0.3% and 0.4%, respectively, in June and July. However, the consensus is for this momentum to stall in August, as growth is projected to contract by 0.1% in the month. At the same time, a slight 0.1% decline in industrial production is expected in August.



	Interest Rate Forecasts			
	Current	End Q4	End Q1	End Q2
		2026	2027	2027
Fed Funds	3.875	4.125	4.125	4.125
ECB Deposit	2.50	2.75	2.75	2.75
BoE Repo	3.75	4.00	4.25	4.25
BoJ OCR	1.25	1.25	1.50	1.50
Current Rates Reuters, Forecasts AIB's ERU				

	Exchange Rate Forecasts (Mid-Point of Range)			
	Current	End Q4	End Q1	End Q2
		2026	2027	2027
EUR/USD	1.1193	1.16	1.17	1.17
EUR/GBP	0.8460	0.87	0.87	0.87
EUR/JPY	177.24	182	182	181
GBP/USD	1.3224	1.33	1.34	1.34
USD/JPY	158.32	157	156	155
Current Rates Reuters, Forecasts AIB's ERU				

ECONOMIC DIARY

Monday 12th - Friday 16th October

Date	UK & Irish Time (GMT+1)		Release	Previous	Forecast
This Week:	ECB Speakers:		Lane (Tue); Schnabel, Lagarde (Wed)		
	BoE Speakers:		Breeden, Mann (Mon); Greene, Dhingra (Tue); Breeden, Pill (Wed); Pill, Breeden, Greene (Thu); Bailey (Fri)		
	Fed Speakers:		Hammack (Mon); Waller, Barkin, Collins (Tue); Bowmann, Barkin (Wed); Hammack (Thu); Warsh (Fri)		
			IMF/World Bank Annual Meetings (12th-18th October) EU Leader's Summit (15-16th October)		
Mon 12th	US:		Columbus Day (Partial Market Holiday)		
Tue 13th	IRE:	01:01	AIB Irish Construction PMI (September)	50.7	
	GER:	07:00	Final HICP Inflation (September)	+0.6% (+3.3%)	+0.6% (+3.3%)
	US:	11:00	NFIB Small Business Optimism (September)	98.7	
	US:	15:00	Existing Home Sales (September)	3.98m / -2.0%	3.96m / -0.5%
Wed 14th	SPA:	08:00	Final HICP Inflation (September)	+0.6% (+5.0%)	+0.6% (+5.0%)
	IRE:	11:00	Residential Property Price Index (August)	+0.8% (+5.5%)	
	US:	13:30	CPI Inflation (September) - Core CPI Inflation	+0.4% (+3.4%) +0.3% (+2.4%)	+0.6% (+3.7%) +0.2% (+2.5%)
Thu 15th	UK:	07:00	GDP (August) - 3 month / 3 month	+0.4% (+1.6%) +0.4%	-0.1% (+1.7%) +0.5%
	UK:	07:00	Industrial Output (August) - Manufacturing Output	+0.2% (+0.6%) +0.9% (+2.6%)	-0.1% (+0.7%) -0.1% (+2.4%)
	UK:	07:00	Goods Trade Balance (August) - Non-EU	-£20.96bn -£9.66bn	
	FRA:	07:45	Final HICP Inflation (September)	+0.4% (+3.4%)	+0.4% (+3.4%)
	EU-21:	10:00	Industrial Production (August)	-0.1% (+0.0%)	+0.0% (-0.1%)
	US:	13:30	NY Fed / Empire State Index (October)	7.60	
	US:	13:30	Initial Jobless Claims (w/e 5th October)	+197,000	+200,000
	US:	13:30	Philly Fed Business Index (October)	37.8	26.5
	US:	13:30	PPI Final Demand (September) - Ex-Food & Energy	+0.4% (+5.4%) +0.2% (+4.6%)	+0.4% (+5.3%) +0.3% (+4.4%)
	US:	13:30	Retail Sales (September) - Ex-Autos - Control Group	+1.2% +1.4% +1.4%	+0.3% +0.6% +0.3%
Fri 16th	EU-21:	10:00	Final HICP Inflation (August) - Ex-Food & energy - Ex-Food, Energy, Alcohol & Tobacco	+0.4% (+3.8%) +0.2% (+2.2%) +0.2% (+2.5%)	+0.6% (+3.8%) +0.2% (+2.2%) +0.2% (+2.5%)
	ITA:	10:00	Final HICP Inflation (September)	+2.0% (+4.1%)	+2.0% (+4.1%)
	US:	14:15	Industrial Production (September) - Manufacturing Output - Capacity Utilisation	+0.0% -0.3% 76.3%	+0.4% +0.3% 76.5%

♦ Month-on-month changes (year-on-year shown in brackets)

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