Weekly Money Market Report
22 July 2018

US Dollar Rally Ends With Trump Comments

United States

US Economic Fundamentals Overshadowed by Trump

The US dollar managed to extend its strength throughout most of the week backed by hawkish sentiments from the Federal Reserve and potential new trade agreements with partners. However, the dollar plummeted on Friday erasing most of its gains after President Trump accused the EU and China of manipulating their currencies.

In his semi-annual congressional testimony, Fed Chairman Jerome Powell told lawmakers that the US job market had continued to strengthen and that the US central bank believed it was best "to keep gradually raising" interest rates. He continued that growth had accelerated in the second quarter of 2018, boosted by "robust job gains, rising after-tax incomes and optimism among households. To the market's relief, Powell did not signal more concern by trade tensions and the flattening yield curve which leaves the Fed on track with their plans.

President Donald Trump's economic adviser Larry Kudlow stated at an investor conference that he was hearing from sources that European Commission President Jean-Claude Juncker will be bringing a "very important" free trade offer when he comes to Washington next week. The comments have raised optimism that the Trump administration may not follow through on threats to impose tariffs on auto imports from the EU. In addition, President Trump told reporters that the US and Mexico are "getting closer" to reaching a trade deal to renegotiate the North American Free Trade Agreement after a "very good session with Mexico, with the new President". He noted that separate talks with Canada could be advanced later. The slight easing of trade tensions combined with clear monetary guidance is encouraging a stable US dollar appreciation.

The US dollar suffered a steep selloff on Friday after Trump accused China and the European Union of manipulating their currencies. He continued saying a stronger dollar and higher interest rates are hurting America's "competitive edge." Undermining the US Fed, he claimed monetary tightening damages the economy and that "the United States should not be penalized for doing well." In his comments, Trump broke decades of tradition that US presidents should avoid commenting directly on the dollar or the path of US monetary policy. In addition, Trump attacked China's trade policies in a Friday interview. He said the US has been "ripped off by China for a long time" and that he was ready to increase tariffs to cover $500 billion worth of Chinese imports. To put things into perspective, that was roughly the value of all US imports from China in 2017. As with most Trump statements, it remains unclear if the comments were made on impulse or to be taken seriously. The US dollar index opened the week at 94.682 rose to a twelve month high of 95.652 before closing at 94.462.

UK & Europe

Sterling Pound Pressured

The British pound was heavily pressured last week losing around 1.45% of its value before rebounding on US President Trump's comments. The fall was driven primarily by heightened political uncertainty revolving around the Brexit issue. British Prime Minister Theresa May narrowly avoided defeat in parliament against pro-EU lawmakers from her own party. Parliament voted 307 to 301 against an amendment to trade legislation that would have forced the UK to try to negotiate a customs union arrangement with the EU if it had failed to negotiate a free trade deal by January 21, 2019. While a customs union and free trade agreement both allow for free trade between the UK and the EU, the key distinction involves their approach to non-treaty nations. A customs union requires all parties to establish identical external tariffs with non-treaty nations, members of a free trade area are free to establish whatever trade agreements with non-signatory nations. Losing the vote would have enraged May's supporters and forced her to go back on her word that Britain will not be part of any customs union after leaving the EU.

The UK also released weaker than expected inflation figures for June. The annual rate of core inflation continued to fall to 1.9% in June which was the lowest rate since January of last year. It now stands well below the peak from January at 2.7%. It provides further evidence that the inflationary impact from the weaker pound has been fading more quickly than expected which has already been acknowledged by the Bank of England. Weaker retail sales also played a role in dampening inflation pressures in June.

While retail sales declined by 0.5% in June, British sales rose the most in over a decade, up 2.1% in the first three months of 2018. Headline inflation was also still broadly in line with the BoE's May forecast. Furthermore, a tight labor market and building evidence of a pick-up in economic growth in Q2 should give the BoE more confidence to continue gradually raising rates with policy still very loose. Market polls from Reuters are still pricing in a 70% chance for an August interest rate hike.

Eurozone Inflation

Eurozone inflation rose to 2.0% year on year in June, from 1.9% in May. The pick-up in inflation was mainly driven by energy prices, up 8.0% on a yearly basis, from 1% in May. Core inflation, however, fell back to 0.9% which is the lowest reading since last December, excluding April (0.8%) which was affected by the volatility generated by the Easter holiday. The fall of core inflation suggests the Euro zone still lacks the 'convincing upward trend' the European Central Bank has been looking to attain before exiting its accommodative policy. But with Mario Draghi having already announced the end of QE in December and economic growth in the zone appears to have firmed in Q2, it remains unlikely for the ECB to shift paths.

Asia

China GDP

Official data showed China's economy grew 6.7% in the second quarter of 2018, down from the 6.8% seen in the last three quarters. The slowdown is attributed to the effects of a multi-year crackdown by Beijing on riskier lending that has driven up corporate borrowing costs. Also, June factory output growth weakened to a two-year low in a worrying sign as a heated trade war with the United States threatens to drop exports. As the risks from the US-China trade war will be a drag on overall growth in the next few years if China's trade surplus against the US narrows substantially, Beijing is likely to continue easing monetary policy going forward.

Kuwait

Kuwaiti Dinar at 0.30250

The USDKWD opened at 0.30250 Sunday Morning.

Rates – 22 July, 2018

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	High	Low	Close	Minimum	Maximum	Forward
EUR	1.1681	1.1744	1.1572	1.1718	1.1505	1.1900	1.1804
GBP	1.3229	1.3292	1.2955	1.3132	1.2945	1.3345	1.3194
JPY	112.39	113.16	111.37	111.39	109.35	113.30	110.73
CHF	1.0021	1.0043	0.9914	0.9924	0.9735	1.0110	0.9851