Weekly Money Market Report
19 September 2021

>NBK Treasury
+965 22216603
tsd_list@nbk.com

Markets Wait For the Fed Amid Tepid Inflation

Highlights

- **Consumer prices in the US rose at a relatively moderate pace in August.**
- **US retail sales reading shows sales bounced back in August.**
- **Markets brace ahead of the Fed's meeting this week.**
- **Inflation in the UK jumped faster in one month than at any time since the Bank of England rate independence.**

United States

Cooling Inflation

Consumer prices in the US rose at a relatively moderate pace in August, hinting that inflationary pressures associated with the economic reopening from COVID lockdowns are easing after hitting a 13 year high. Consumer Price Index (CPI) - the figure published by the Bureau of Labor Statistics - was released on Tuesday where it rose 5.3% in August compared to a year ago. The reading was just shy of the 5.4% increase reported for July, which is the highest reading since 2008. Looking at the month-over-month reading, price gains slowed to 0.3% from July, a distinctly lower reading than the 0.9% jump from May to June and the 0.5% rise from June to July. Core CPI, the reading that excludes volatile items such as food and energy, also clocked a deceleration with the monthly pace falling to a 0.1% increase, the smallest increase since February. On yearly basis, core prices climbed 4% compared with the 4.3% in July.

Most of the price gains seen so far in the year have stemmed from sectors most vulnerable to supply bottlenecks and other pandemic related disruptions. The recent data accompanied with the data from July showed signs that these gains were abating, especially for used car prices and travel expenses, the main drivers of the increases for 2021. July started with signs of the cooldown and August readings came to confirm that price pressures in these sectors are starting to subside. Prices of used cars and trucks still remain 32% higher on annual basis, but that is after dipping 1.5% from July.

The travel industry is now showing signs of the more contagious Delta variant denting business activity. Airline fares dropped 9.1% month-on-month while hotel room rates dropped 2.9%.

Despite a slower growth pace in August, consumers remain braced for higher inflation to continue, with expectations over the short and medium term now at the highest level since 2013, according to data published by the New York Branch of the Federal Reserve on Monday. Over the next year, consumers anticipate inflation of 5.2%, up 0.3% from July in the tenth consecutive monthly increase. Over a three year horizon, they expect gains of 4%.

However, the CPI report did show that some inflationary pressures are building in other sectors, housing included. Owners' equivalent rent, the reading that measures what homes would rent for, rose another 0.3% from July's year-on-year increase, to clock a yearly increase of 2.5% in August.

Retail Rebound

The US retail sales reading published on Thursday showed sales bounced back as Americans stocked up on school supplies in preparation to go back to schools, in addition to spending on home decor in a sign of their willingness to spend.

The Census Bureau said sales were up 0.7% in August compared to July, a 180 degree turn from analyst's expectations for a 0.8% drop following the resurgence of COVID and the dampened consumer confidence due to rising prices. In July, sales fell 1.8% compared to an estimate of a 1.1% drop.

The drivers for the increase in August were demand at department stores as well as home improvement and furniture outlets, as well as stronger spending online. Grocery stores also registered gains, in a sign of continued demand for food consumed at home. Food services sales on the other hand, were flat.

Nevertheless, retail sales remain well above pre-pandemic levels. Major retail chains booked robust quarterly revenues in the early part of summer, bolstered by back to school shopping and homeowners taking up new projects. Consumers also looked to be allocating some of their spending to experiences not reflected in retail sales readings, spending more on travel, accommodation, and tickets to concerts and sporting events as many COVID restrictions wane.

The reading saw yields on both short and longer term US Treasury bonds rising to session highs. The benchmark 10-year note, which yield moves in tandem with economic expectations, was up 0.05% to 1.35%. Shorter dated yields, which move with interest rate expectation, also saw a rise as investors increased their bets that the Federal Reserve may take the first step towards unwinding its pandemic era monetary policy in its meeting next week. The US dollar saw support with the Index closing the week 0.61% higher at 93.195, taking its toll on its peers in the forex market.

The Fed is now facing somewhat of a dilemma given the data it has in its hand. The CPI reading of August shows support for team transitory and their narrative that the peak has passed. Meanwhile, the strong retail sales figures support the pro taper side of the argument. Markets will keep a close eye on the Feds FOMC meeting this week, No taper announcement is expected especially after August's lackluster jobs report. The Fed is now expected to keep its options open by restating that tapering this year could be appropriate, while acknowledging the recent weakness in hiring, but markets are still pricing in a taper announcement in 2021.

UK

Falling Retail Sales

Data from the UK showed retail sales unexpectedly contracted for the fourth consecutive month in August, raising concerns over the country's post pandemic recovery. The volume of monthly retail sales in Great Britain fell 0.9% from July to August. The reading follows a sharp contraction in July, while missing the 0.5% expansion forecast by economists.

The data throws doubt in whether or not the Bank of England's Monetary Policy Committee would be in a position to hike its rates as soon as February. But Jonathan Athow, a senior statistician in the Office for National Statistics said the data suggested that "the drop in food stores' sales is linked to an increase in eating out following the lifting of coronavirus restrictions." However, one of the reasons for the drop looked to be supply chain disruptions with around 7% of retailers reporting not being able to secure the materials, goods or services they needed in August. Supply chain issues were especially high with 18% of department stores and 11% of clothing stores.

Food store sales, volumes fell 1.2% in August, showing some evidence of consumers increasing social spending, such as eating at restaurants instead of cooking at home. Non-food stores on the other hand reported a fall of 1%, driven by a contraction at department stores among other stores such as sports equipment and computer outlets. In contrast, automotive fuel sales volumes rose 1.5% as people started to travel more.

Inflation Heat

Earlier in the week, data showed that inflation in the UK jumped faster in one month than at any time since the Bank of England gained its independence to set interest rates, rising 1.2% to reach 3.2% from July to August, the highest level since 2012.

The unexpected surge looks to be undermining the regulator's view that price rises are manageable and temporary. With CPI inflation at more than 1% above the BoE's 2% target, Governor Andrew Baily is now forced to write a letter to the chancellor explaining why prices have risen so quickly and what the central bank intends to do in order to bring back inflation to its target.

For August, the rise in food, transport, recreation, furniture and restaurant prices was more than 1%. With the BoE already expecting inflation to rise to 4% by the end of the year, the rapid acceleration will come as a shock. Gas and electricity bills are set to increase sharply during the fall season, reflecting rises in wholesale prices. Also, value added tax will rise back to its full 12.5% for the hospitality sector at the end of the month and food and clothing prices are also expected to jump in the fall.

Economists are still split on whether inflation will become a significant problem in the months ahead or disappear after a largely one off price rise as the economy opens up following the COVID shock.

Asia Pacific

Reserve Bank of Australia

Philip Lowe, governor of the Reserve Bank of Australia said on Tuesday that COVID lockdowns would cause a sharp contraction in the country's economy. He continued to say that the regulator was confident activity would rebound quickly once restrictions were eased in December as planned. Governor Lowe also reiterated that interest rates are not expected to rise from their record lows until 2024 given the persistently sluggish growth of wages, pouring cold water on any ideas that the RBA would raise its rates soon. The RBA adjusted the trajectory of its government-bond-buying taper the week before in response to a renewed COVID related health crisis that has slowed the economy.

Labor market figures readings were released later in the week showing a drop in the unemployment rate from 4.6% in July to 4.5% in August. The reading came as a shock as the expectations forecasted a drop in additional jobs due to the reintroduction of pandemic restrictions in Sydney.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30070

Rates – 19 September, 2021

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.1814	1.1725	1.1846	1.1725	1.1700	1.1875	1.1749
GBP	1.3838	1.3728	1.3913	1.3738	1.3700	1.3900	1.3757
JPY	109.94	109.11	110.16	109.98	108.00	110.90	109.73
CHF	0.9176	0.9164	0.9325	0.9323	0.9200	0.9400	0.9299