Weekly Money Market Report
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US Dollar Slide Still Intact

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Highlights

- **Fed Chairman reveals new inflation strategy.**
- **US equities soar, while bond prices fall.**
- **Dollar demand weakens as low interest rates environment set to stay.**
- **Second preliminary US GDP reconfirms frail state in economy.**
- **GBP/USD remains on an uptrend even as the clock ticks down to the December 31st deadline.**
- **US-China tension diminishes; CNY soars.**

United States

Fed's New Strategy Negatively Impacted the Dollar's Attractiveness

The economic calendar last week was exceptionally light, in spite of it, there was volatility in financial markets. All eyes were focused on the Jackson Hole summit, where the world's most powerful central bank revealed its new strategy on price growth. The Fed is moving towards an "average" 2% inflation target rather than a fixed one and to restore full employment. The S&P 500 and the Dow advanced higher as the new strategy will keep interest rates on the low, which equities cherish. The S&P hit a new record high of 3,509.23 on Friday and gained about 2.60% in value on a weekly basis.

Powell's comments propelled the 10-year US Treasury yield to several months high of 0.7890%, while the 2-year barley edged higher. In order to attain higher inflation than it has managed in recent years, the central bank is probably going to hold short-term rates very low for a long time, which limited the advancement of the 2-year yield. The spread between the aforementioned yields widened to 61 basis points, the highest since mid-May. The steeper yield curve pushed financial equites into the green as banks margins improve as the yield curve steepens. JPMorgan Chase and American Express shares were up more than 3% on Thursday.

In the FX sphere, higher US yields failed to save the greenback from its negative momentum. Financial markets are factoring in greater tolerance for higher inflation, which is a key element in the current narrative of negative US real yields reducing the dollar's attractiveness. In weekly terms, the dollar index is down by 1% against a basket of currencies and is close to the lowest levels since April 2018. The Aussie was one of the best performing currencies supported by a weaker dollar and improving data out of China, which is Australia's largest trading partner. The AUD/USD soared to 0.7368, a near 2-year high.

Fed's Pivotal Shift in Policy Framework

The Federal Reserve made a historic amendment to its inflation objective last week, highlighting the importance of high employment and allowing inflation to overshoot the 2% target. It seems the Fed's new strategy is putting higher weight on strengthening the US labor market and less worries about too-high inflation. All 17 policymakers signed on the new strategy. The Fed's dovish shift in strategy, while stating "downward risks to employment and inflation have increased", further reinforces an era of low rates.

In details, Fed President of Dallas Robert Kaplan mentioned that he would not feel comfortable allowing inflation to stay at 3% for a year and not raise interest rates. Although, he does see 2.25%-2.5% as consistent with the Fed's new strategy. "This is not a formula, this is not a commitment," Kaplan stated.

Overall, the latest strategy is leaning towards an average inflation of 2%, under which the Fed would aim to make up for periods when inflation is too low by allowing periods when inflation is too high.

US Economic Fundamentals

The second reading of US GDP reconfirmed the economic frail state seen back in Q2. US GDP plunged by 37.1% on an annual basis from 5% in Q1. The latest figure is slightly better than the initial estimate of -32.9%, even with that, it was still the worst contraction ever recorded. The drop in GDP was more than triple the previous all-time decline. As for the labor market, demand for unemployment benefits remains elevated. The number of Americans filing for unemployment benefits continues to hover around 1 million for a fourth week in a row and a minimum of 27 million individuals were receiving unemployment benefits under all programs in the week ended August 8. Moreover, the $600 weekly unemployment supplement expired on July 31 and economists forecast the loss of the $600 could cut $50 billion from retail sales in August.

On a more positive note, US orders for durable goods increased 11.2% in July, more than double the 4.4% expected. Core capital goods orders, which excludes aircraft and military hardware, rose 1.9%. Orders have increased for three months in a row mainly driven by the continuous return of auto production, suggesting the manufacturing sector is continuing on a path of robust recovery. Earlier, the Flash Manufacturing PMI index rose to 53.6 following 50.9 for the previous month, representing growth for a sector that accounts for 11% of the US economy. The industry has registered expansions for July and August following contractions at 36.9 and 39.8 for April and May respectively.

Europe & UK

Sterling Resiliency Despite Brexit Deadline Around the Corner

The GBP/USD pair remains on an uptrend from the lows seen back in March even as the clock ticks down to the December 31st deadline. EU's Chief Brexit negotiator Michel Barnier cautioned in the plainest terms that "at this stage, an agreement between the UK and the EU seems unlikely". On the UK side, David Frost UK's Chief Brexit negotiator highlighted that "agreement is still possible, and it is still our goal, but it is clear that it will not be easy to achieve." The unfavorable developments have inflated the risk of a "No Deal" Brexit with time running out.

The Sterling pound has recovered tremendously from the harsh blow it suffered against the dollar back in March, when it fell to a low of 1.1404. The GBP/USD is currently trading at 1.3349 and last week it hit 1.3356, the highest level since December 2019. In the options market, prices suggest GBP faces no big risks in the next six months with only 4 months to go before the Brexit deadline. GBP/USD direction suggests either complacency or confidence that neither side in the talks would advocate more instability into economies already impacted by the pandemic.

Asia

Chinese Yuan Rallies as Trade Deal Still Intact

Diminishing tensions between the US and China has paved the way for a rally in CNY. US and Chinese trade officials reiterated their commitment for a Phase 1 trade deal last week, their first official negotiation since early May - amid concern the deal could be on wobbly ground. "Both sides see progress and are committed to taking the steps necessary to ensure the success of the agreement," the US Trade Representative's office mentioned. China's Commerce Ministry confirmed that both sides had a "constructive dialogue" and agreed to continue pushing forward the Phase 1 trade deal's implementation.

According to Bloomberg calculations, China must purchase around $130 billion of goods and services in the second half of the year to fulfill its terms of the original deal. The developments provide reassurance that the Trump administration still values the "Phase One" trade deal, and will assist to further dampen concerns that it could be ripped up ahead of the Presidential election. The USD/CNY pair depreciated to

6.8604, the lowest level since January this year. Since June, the USD has fallen by 3.51% against the CNY.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30560.

Rates – 30th August, 2020

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.1785	1.1919	1.1761	1.1903	1.1810	1.2085	1.1926
GBP	1.3084	1.3356	1.3049	1.3349	1.3205	1.3530	1.3355
JPY	105.85	106.94	105.18	105.34	103.50	106.95	105.22
CHF	0.9116	0.9127	0.9022	0.9038	0.8840	0.9230	0.9012