Treasury Group

Weekly Money Market Report

23 July 2017

Dollar Lower amid Uncertainty Surrounding US Politics

United States

Dollar Lower; Euro Higher Despite ECB Dovishness

The US dollar continued to trade in a subdued manner against most of its major counterparts last week on the back of heightened uncertainty surrounding the future of the Fed's rate path. Additionally, concerns over Trump's ability to push his agenda in the White House helped push the greenback lower. The lack of confidence in the market is clearly reflected in US 10-year treasury yields which traded at 3-week lows. Meanwhile, equities maintained recent gains on the back of a generally positive earnings season and prospects of a less aggressive Fed interest rate policy.

The market continued to be dictated by central banks and their agendas with regards to the withdrawal of their huge quantitative easing programs. Last week, the European Central Bank meeting and press conference took center stage as investors were eagerly awaiting any hint on when the ECB would start tapering. However, the European Central bank left its ultra-loose monetary policy unchanged and did not even discuss reducing back stimulus, which suggested it may delay an inevitable decision on tapering asset purchases until the latest possible moment.

The BOJ had a similar story as it kept its monetary policy unchanged and has extended the timeframe for reaching its 2% inflation target to fiscal year 2019. Regardless of whether the BOJ acknowledges that inflation won't reach its target as expected, Governor Haruhiko Kuroda won't get anywhere near a policy exit before his five-year term expires in April, Hideo Hayakawa, said in an interview with Bloomberg last week.

On the foreign exchange front, the US dollar declined by 1.42% last week. The dollar index opened the week at 95.088 and reaching as high as 95.348 but the dollar lost all momentum and slipped to 11-month low of 94.180. The market has started to lose faith in "Trumpflation" as the possibility to pass the Republican health care reform bill appears even dimmer. Three Republican Senators voiced opposition to the proposed bill and it does appear that the bill won't have enough votes to pass, casting further doubts on Trump's influence on the White House policies.

Even after a dovish Draghi in the ECB press conference, the Euro was the biggest winner last week gaining 2.13% on the back of solid economic figures and weakness in the dollar. The currency opened the week at 1.1462 and rose as high as 1.1677 on Friday. The euro closed the week at 1.1658.

The Sterling Pound had a different story than the Euro as mixed retail and inflation data hit the market. Furthermore, the softer inflation figure had depressed expectations of an interest rate hike in the short-term. The cable opened the week at 1.3099 and reached a high of 1.3125 but quickly lost all gains and fell to a low of 1.2970. The currency closed the week at 1.2992.

The safe haven Yen traded in a relatively narrow range opening the week at 112.49 and reached a low of 111.46 despite mixed economic data and a cautious BOJ statement. The Yen continues to gain against the greenback as differentials continue to drop on the back of lower US yields. The currency closed the week at 111.10.

In the commodities complex, oil prices had a volatile movement increasing by up to 3.89% as Brent Crude reached a six week high of $50.19. US crude oil inventory decreased by 4.7M as the refineries produced 125,000 barrels per day less than the previous week's average. However, Brent closed the week at $48.06 due to forecasts of a rise in OPEC production for July despite the group's pledge to curb output.

Continued growth in the housing market

The housing market registered the fastest annualized pace in four months according to the Commerce Department data released last Wednesday. Housing starts increased by 8.3% to 1.22 million annualized rate up from 1.12 million reached in May. While building permits, a proxy for future construction, climbed 7.4% to a 1.25 million annualized rate up from May's figure of 1.17 million. Despite three interest rate hikes since December 2016 and increased inflation, the housing market keeps on expanding at a considerably fast pace, which may potentially deem alarming in the near future.

Manufacturing continues to grow but at a slower pace

The Philly Fed Manufacturing index decreased from a reading of 27.6 in June to 19.5 this month. The index has been positive for 12 consecutive months, but July's reading is the lowest since November. Thirty-seven% of the firms indicated increases in activity in July, down from 42% last month. The shipments index decreased 16 points, while the new orders index fell 24 points. Nearly 31% of the respondents reported a rise in new orders this month, down from 45% in June. Both the delivery times and unfilled orders indexes were positive for the ninth consecutive month, suggesting longer delivery times and increases in unfilled orders.

Europe & UK

Dovish Draghi

The European Central Bank left its benchmark refinancing rate unchanged at 0.00%, as expected, on Thursday. President Mario Draghi also said the ECB would continue its monthly asset purchases at the current rate, 60 million euros a month, until December 2017 or beyond, if necessary. Following are highlights of ECB President Mario Draghi's comments at a post-policy meeting press conference. On potential changes to the QE program he said "We need to be persistent and patient because we aren't there yet."

Draghi also added that "We also were unanimous in communicating no change to the forward guidance and also we were unanimous in setting no precise date for when to discuss changes in the future - in other words, we simply said that our discussions should take place in the autumn." The ECB's president emphasized that we need to think and gather lots of information as there is lots of uncertainty around. He also stressed that the Governing Council doesn't want to be forced to take decisions in an absence of full information

Eurozone annual CPI holds firm

Euro area final annual inflation figure came at 1.3% for June, matching the market's expectations yet lower than the revised 1.4% May figure. It is worth mentioning that in June last year inflation was at 0.1%, but with the ECB's loose monetary policy and asset purchase program helped lift the inflation to a decent 1.3% a year later.

However core CPI excluding energy, food, alcohol and tobacco strengthened to 1.1% y/y compared with 0.9% in May. Of further comfort to the central banker would be the core inflation excluding energy & processed food but including tobacco & alcohol ,ECB's preferred measure of core inflation, came in 1.2% y/y – highest in over two and half years.

UK: Higher Retail Sales, Lower Inflation

UK's inflation unexpectedly slowed down year to year in June. The 2.6% was lower than expectations by 0.3% and thus removing some pressure from the BOE as price growth was getting out of hand. This figure marks the first drop in annual CPI rate since October of last year. Economists had forecasted that the data would hold at the four-year high of 2.95 reached last month. The data undermines arguments for the immediate interest-rate hike that a minority of policy makers supported at the last BOE decision as inflation looked set to veer further above the 2% target. There are also signs economic growth is cooling as consumers, the engine of growth for the past year, start to rein in spending.

In addition, the quantity of goods sold in stores and online rose by 0.6%, more than economists forecast, following a 1.1% decline in May, figures from the Office for National Statistics showed Thursday. Sales rose in almost every category last month. Spending on clothes helped lift sales at department stores by 2.7% and household goods rose 3.3%. Food sales fell 0.5%, partly due to weaker alcohol demand.

Asia

Reserve Bank of Australia Minutes

In its July meeting minutes, the RBA again stated that developments in the labor market warrant careful monitoring. In the detail of the minutes the better growth data (the flow of jobs) is contrasted with high levels of underemployment (to stock of spare capacity). It is notable that the RBA characterized the labor market improvement as removing "some of the downside risk in the Bank's forecast of wage growth".

China's GDP Expands

China's economy expanded faster than expected in the second quarter of 2017, as traditional growth sectors continued to underpin the economy. The National Bureau of Statistics said gross domestic product (GDP) expanded at an annualized 6.9% in the second quarter, unchanged from the previous quarter and well within the government's target range of 6.5% to 7%.

Over the past four quarters, the Chinese economy has relied on government spending and access to cheap credit to fuel a faster than expected expansion. At the same time, efforts to curb a red hot housing market have largely come up short amid a resurgence of demand. Buyers anticipating further restrictions on housing have flooded the market after authorities introduced curbs back in March. Furthermore, Industrial production, the broadest measure of factory output, expanded 7.6% in the 12 months through June. That was well above the previous month's 6.5% growth pace signaling a healthier and more solid economy.

BOJ keeps the policy unchanged

Bank of Japan's meeting last week was uneventful as expected by market participants. The central bank kept the interest rate unchanged at -0.10% and 80 trillion yen QE program in place as well as the 10-year JGB yield target at about 0.00%. In addition, the BOJ admitted defeat of deflation and delayed the timing of reaching their 2% inflation target to fiscal year 2019.
Finally, Bloomberg Intelligence economist Yuki Masujima warned that a big risk ahead for BOJ after two board members leave this week is tunnel vision**.** Takahide Kiuchi and Takehiro Sato routinely challenged the policy board's consensus, and their successors are less likely to oppose Kuroda.

Kuwait

Kuwaiti Dinar at 0.30215

The USDKWD opened at 0.30215 on Sunday morning.

Rates – 23rd July, 2017

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.1462	1.1433	1.1682	1.1661	1.560	1.1850	1.1721
GBP	1.3099	1.2930	1.3125	1.2992	1.2900	1.3170	1.3041
JPY	112.49	112.86	112.86	110.98	109.00	112.30	110.61
CHF	0.9634	0.9436	0.9658	0.9455	0.9270	0.9540	0.9398