Weekly Money Market Report
05 December 2021

Powell Retires "Transitory" Inflation

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Highlights

- **US Federal Reserve Chair Powell surprised markets by taking a Hawkish turn, stating the Fed will no longer characterize inflation as "transitory" and opened the door for earlier than expected rate hikes.**
- **US manufacturing activity picked up in November, increasing to 61.1 from 60.8 in October, further supporting higher inflation.**
- **Non-farm employment data disappointed markets last week, adding just 210K jobs versus the 553K expected. The unemployment rate came in at 4.2% versus the 4.5% expected.**
- **Expectations for hikes by the US Federal Reserve were pushed forward following the labor data, with money markets now pricing in 2 rate hikes towards the end of 2022 and 1 hike in the beginning of 2023.**
- **Oil prices climbed after OPEC+ stated it would be ready at short notice to review its production hike policy if demand collapsed.**

Two main themes drove market movements over the past week. The first is the uncertainty caused by the latest Covid-19 variant "Omicron", slowly appearing in different parts of the world. The second was the US Federal Reserve's hawkish shift in rhetoric, with Powell stating the central bank needs to be ready to respond to the possibility that inflation may not recede in the second half of 2022. In response, the greenback witnessed heavy support with the index ending the week at 96.117. Moving to bonds, the yield curve flattened as the 10-year Treasury note lost nearly 23bps off recent highs. Meanwhile, yields on the policy-sensitive two-year note remained near 0.60%.

United States

Powell's Hawkish Tone

Last week, US Federal Reserve Chair Jerome Powell pointed to a strong US economy, stalled workforce growth, and high inflation that is expected to last into mid-2022. "Since the last meeting, we've seen basically elevated inflation pressures, we've seen very strong labor market data without any improvement in labor supply, we've seen strong spending data too," the Fed chief told members of the Senate Banking Committee. Inflation is running at more than twice the Fed's 2% target annually, however the central bank had long maintained its characterization of inflation as "transitory".

In a clear sign that the Fed will soon shift to tighter monetary policy, Powell told congress last week that it's "probably a good time to retire that word." The central bank had been using the term transitory on warnings that year-over-year comparisons and supply chain bottlenecks would lead to the high figures however would soon abate. Those high readings did not fade in the later part of 2021 as expected, accelerating instead with prices soaring 6.2% y/y in October. Even the Fed's preferred measure of inflation (the Personal Consumption Expenditure) rose by 5% y/y in October.

The central bank hoped to fully end its open market purchases of mortgage-backed securities and US Treasuries by the middle of next year under a plan announced at the start of November. However, Powell opened the door to accelerating that timeline last week. Policy makers will meet on December 14-15, where they will decide whether to speed up that timetable. It is now clear that policy makers are preparing to raise interest rates much earlier than anticipated just a few months ago.

Labor Report Pushes Forward Hike Probabilities

Total nonfarm payroll employment rose by 210,000 in November versus expectations for a 553,000 gain. Meanwhile, unemployment fell by 0.4% to 4.2% with the total number of unemployed persons down by 542,000 to 6.9 million. Both measures are down considerably from their highs at the end of the Feb-Apr 2020 recession, however are still well above pre-pandemic levels. The labor force participation rate edged up to 61.8%. Moving forward, analysts will question whether the data is strong enough for the Fed to justify an acceleration of its QE taper in January.

Manufacturing Sector Picks up

Amid strong demand for goods, US manufacturing activity picked up in November, keeping inflation high as factories continue to struggle with pandemic-related shortages of raw materials. The Institute for Supply Management said on Wednesday its index of national factory activity increased to 61.1 last month from 60.8 in October. Digging into the report, a measure of manufacturing employment rose to a seven-month high as the robust demand led to factories hiring more workers. Nevertheless, worker shortages remain a constraint.

Commodities

Oil Prices Climb on OPEC+ Statement

Oil prices climbed last week after OPEC+ stated it could review its production hike policy at short notice if oil demand collapsed due to a rising number of lockdowns. Last Thursday, the group surprised markets when it stuck to plans to add 400,000 barrels per day of supply in January. The decision came despite fears of the US releasing its crude reserves and Omicron's effect on demand. The price for brent crude rose to $71.40 after reaching a low of $65.72 last week.

OPEC+ has been gradually unwinding record cuts agreed upon last year when the pandemic hindered demand, slashing output by about 10 million bpd, or 10% of global supply. Those cuts have since been scaled back to about 3.8 million bpd. Yet, according to the International Energy Agency, OPEC+ has regularly failed to meet its output targets, producing about 700,000 bpd less than planned in both September and October. The group is scheduled to meet on January 4, 2022.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30245.

Rates – 05 December, 2021

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.1307	1.1234	1.1382	1.1313	1.1100	1.1400	1.1344
GBP	1.3340	1.3193	1.3370	1.3231	1.3100	1.3400	1.3243
JPY	113.35	112.52	113.95	112.80	111.00	115.00	112.71
CHF	0.9237	0.9156	0.9272	0.9178	0.9150	0.9425	0.9156