Treasury Group
Weekly Money Market Report
17 June 2018

Week of Central Banks

United States

Federal Open Markets Committee

On June 13, 2018 the United Stated Federal Reserve successfully raised its benchmark interest rate from 1.75% to 2.0% as widely expected. Growth and inflation forecasts were also increased for the year. The median projections for economic growth and core inflation in 2018 were both revised higher by 0.1 point to 2.8% and 2.0% respectively. With core inflation expected to reach the Fed's 2.0% target, the FOMC was confident enough to drop earlier statements that it is carefully monitoring actual and expected price readings. Interest rate forecasts released by policymakers now point to a total of four rate rises in 2018, followed by another three in 2019.

The Fed's hawkish policy update displayed increased confidence in the outlook or the US economy. Fed Chair Powell stated that "the decision you see today is another sign that the US economy is in great shape." "The Committee expects that further gradual increases in the target range for the federal funds rate will be consistent with sustained expansion of economic activity, strong labor market conditions, and inflation near the Committee's symmetric 2.0% objective over the medium term."

The Fed's confidence was supported further by official economic figures released last week. Consumer prices in the United States increased by 0.2% in May taking the annual figure to 2.8%. When removing the volatile components of food and energy, the core figure also increased by 0.2% taking the annual rate to 2.2% in line with the Fed's expectations. Looking at consumer activity, The Commerce Department said on Thursday retail sales jumped 0.8% last month in the biggest advance since November 2017. US consumers bought motor vehicles and a range of other goods even as they paid more for gasoline indicating acceleration of economic growth in the second quarter.

While the currency markets reaction was relatively muted after the policy meeting, the US dollar skyrocketed 1.9% the following day after the European Central Bank sent a relatively dovish message as opposed to the Fed's aggressive stance.

Europe

European Central Bank

In Europe, the European Central Bank made two important policy updates when it met Thursday June 14. First, the ECB has finally announced that they will bring an end to its quantitative easing program this year. QE purchases will slow in Q4 to EUR15 billion per month after which purchases will cease at the end of December. The ECB started its QE program in March 2015 in response to deflation risks. The threat of deflation has since diminished notably and there is no longer justification to maintain emergency policy settings. Indeed, President Draghi acknowledged that there has been "substantial progress" in the inflation adjustment which makes the ECB more confident that inflation will return towards their target. It was backed up further by the upward revisions to the ECB's forecasts for inflation. Inflation forecasts for 2018 and 2019 were both revised higher by 0.3% to 1.7%. The inflation forecast for 2020 was also left unchanged at 1.7%. The upward revisions were mainly driven by the higher price of oil whereas the ECB's outlook for underlying inflation appears little changed. Underlying inflation is still expected to rise gradually over the medium-term from current "muted" levels.

Second, the ECB has strengthened its forward rate guidance by stating that rates will remain at present levels "at least through the summer of 2019", and in any case for as long as necessary to ensure that the evolution of inflation remains aligned with the current expectations of a sustained adjustment path". It replaces the ECB's previous forward guidance that rates will remain at present levels for an extended period of time, and "well past" the horizon of net asset purchases. The message was interpreted as an attempt by the ECB to dampen market expectations for rate hikes next year. It also provided a dovish offset to the hawkish decision to end QE.

The euro currency dropped around 2.0% after the meeting in its worst day performance in two years. The reaction came as the interest rate differential between the US and Europe is set to widen if their respective central banks follow through with the guidelines set this week. While the ECB has signaled to keep interest rates low into the summer of 2019, the US Fed is scheduled to hike rates five times by then.

Asia

Bank of Japan

In Asia, the Bank of Japan also convened last week following its western counterparts. However, while the picture in the West was optimistic, the economic situation in Japan was still dim. The BoJ kept monetary policy on hold with an interest rate of minus 0.1%, a cap on 10-year bond yields at around zero and asset purchases of ¥80tn a year. Despite the banks statement that the economy is "expanding moderately" with rising private consumption and higher corporate profits, it still downgraded its inflation expectation to a range between 0.5% and 1.0%. "Japan's economy is seeing labor markets tighten and the output gap improving, but prices aren't rising much. As such, it's most appropriate to patiently maintain our powerful monetary easing," said BoJ governor Kuroda. The policy statement reinforces views that Japan will lag well behind the US and Europe in dialing back its crisis-mode policies.

As a result, the Japanese yen was a little bit weaker after the meeting as lower inflation could mean stimulus for longer. However, market risk aversion gave strength back the yen after global trade war fears were reignited when US President Donald Trump announced $50 billion of Chinese imports the same day.

Kuwait

Kuwaiti Dinar at 0.30195

The USDKWD closed at 0.30195 on Thursday.

Rates – 17 June, 2018

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	High	Low	Close	Minimum	Maximum	Forward
EUR	1.1764	1.1851	1.1541	1.1607	1.1476	1.1728	1.1690
GBP	1.3402	1.3446	1.3209	1.3283	1.3139	1.3403	1.3341
JPY	109.46	110.90	109.20	110.66	109.86	111.46	109.95
CHF	0.9857	0.9988	0.9823	0.9974	0.9900	1.0040	0.9896