

Weekly Money Market Report

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Recession Fears Grip Markets

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Highlights

- US sales of existing homes dropped 3.4% to a seasonally adjusted annualized rate of 5.41 million units in May, according to the National Association of Realtors. The figure marked the weakest reading since June 2020.
- In Canada, inflation was driven mainly by a 48% surge in gasoline prices leaving CPI at 7.7% y/y following April's 6.8%. Even excluding volatile items that were elevated since the war in Ukraine, CPI came in above 6%.
- Despite higher prices and economic uncertainties, Canadian retailers recorded a 0.9% sales increase in April.
- Britain's cost of living continues to rise with CPI registering a 9.1% gain y/y and 0.7% m/m in May. The largest upward contributions came from housing and household services.
- The greenback maintained its bullish path while Treasury yields declined.

United States

Powell Addresses Recession Fears

Last week, Federal Reserve Chair Jerome Powell told lawmakers at the Senate Banking Committee that a recession caused by higher interest rates was "certainly a possibility." The blunt rhetoric comes as the Fed faces the challenge of reducing inflation from 40-year highs, creating a risk that the central bank loses credibility with the public if it fails to see meaningful progress. Despite acknowledging the risk, Powell maintained his view that there are still paths to avoid a recession. "We understand the hardship high inflation is causing," Powell said. "We are strongly committed to bringing inflation back down, and we are moving expeditiously to do so. We have both the tools we need and the resolve it will take to restore price stability on behalf of American families and businesses."

Combined, the Fed, White House, and Congress are struggling to bring down inflation. While the Fed has plans to raise rates this year, its tools are limited especially since the central bank has no control over many of the forces driving inflation today. "The events of the last few months, around the world, have made it more difficult for us to achieve what we want," the Fed chair added. Inflation touched a new peak in May illustrating that the Fed's policies may not be as effective. Testifying again on Thursday, Powell said that his commitment to fight inflation is "unconditional." Meanwhile, pressure is growing on the Biden administration to lower prices for American families specifically at the gas pump. Fears of a recession are rising, with Citigroup putting the odds of a new recession at 50%.

Existing Home Sales Fall for Fourth Straight Month

Sales of existing homes dropped 3.4% in May to a seasonally adjusted annualized rate of 5.41 million units, according to the National Association of Realtors. Sales were 8.6% lower on a yearly basis, marking the weakest reading since the early months of the Covid pandemic in June 2020. At the end of May, there were 1.16 million homes for sale, a 12.6% monthly increase and 4.1% yearly decrease. At the current sales pace, that represents a 2.6-month supply. Low supply continued to place pressure on home prices. The median price of a house sold in May was \$407,600, an increase of 14.8% from May 2021 and marking the highest price on record after topping \$400K for the first time.

Markets React

The dollar index maintained its strength, with the index trading above the 101 level for 9 weeks so far. Heavy demand for the greenback sent the EUR/USD and GBP/USD pairs below their 1.06 and 1.23 marks respectively. Meanwhile yields on US Treasury bonds fell as prices went up due to increasing fears of a recession. On Wall

Street, stocks saw some relief following three straight weeks of declines. The S&P 500 and Dow Jones Industrial Average ended the week 3.06% and 2.68% higher respectively.

Canada

CPI Near 40-Year High

Canada's consumer prices increased in May at a pace not seen since 1983, largely driven by a 48% surge in gasoline prices. Annual inflation accelerated to 7.7% in May, well above April's 6.8% and far beyond the Bank of Canada's 5.8% forecast. Excluding prices for energy and food that have rocketed since the war in Ukraine, annual core inflation in Canada remains in the 6% range. Finally, CPI common, which is the central bank's preferred gauge of the economy's performance, matched a July 1991 high of 3.9%. Inflation has now been above the Bank of Canada's 2% target for 15 months. Elevated inflation and the Fed's recent 75 bps hike practically locked in market expectations of a 75 basis point hike for the BOC in July.

The last time the BOC hiked was in 1998 in defense of its currency. So far this year, the central bank has already delivered three hikes sending their target rate to 1.5% while adding it was ready to act "more forcefully" moving forward if needed. "We know inflation is keeping Canadians up at night. It's keeping us up at night," the Bank of Canada's Senior Deputy Governor Carolyn Rogers said in reaction to the figures. "We will not rest easy until we get back down to target... That's why we're raising interest rates, and we're raising them quite aggressively," she added.

Nevertheless, rising interest rates, higher inflation, and slumping consumer confidence in Canada have not yet affected spending in any major way. According to Statistics Canada, retailers recorded a 0.9% sales increase in April, illustrating resiliency that may likely stoke expectations for further increases in borrowing costs by the Bank of Canada. Still, details of the report revealed only six of eleven subsectors posted gains in April, with volumes specifically dropping at new car dealerships and building material stores.

Europe & UK

UK Inflation Rises to 9.1%

Soaring food and energy prices are continuing to deteriorate the UK's cost of living. The consumer price index registered a 9.1% rise in May following a 9% increase in April. On a monthly basis, prices rose by 0.7%, well short of the 2.5% increase in April and indicating inflation may be somewhat slowing. The largest upward contributions came from housing and household services, primarily electricity, gas and other fuels, along with transport.

Just two weeks ago, the Bank of England implemented its fifth consecutive hike to interest rates yet fell short of matching the aggressive action recently taken by the US Federal Reserve and Swiss National Bank. The BOE's bank rate currently sits at a 13-year high of 1.25% with the bank expecting CPI inflation to exceed 11% by October. Alongside external shocks facing the global economy such as food and energy price surges amid the war in Ukraine and supply chain problems due to lingering Covid-19 pandemic bottlenecks, the UK is also navigating the unwinding of the government's historic pandemic-era fiscal support, and the effects of Brexit.

Slump in German Business Activity

Manufacturers in Germany saw business activity slump to its lowest level in 23 months as exports fell and domestic demand came under pressure. The flash PMI for the sector, which makes up about a fifth of the country's economy, dropped to 52 from 54.8. Firms registered their sharpest decline in new orders in two years, while demand for exported goods also fell due to concerns of elevated prices, the war in Ukraine, and Covid disruptions in China. Meanwhile, the services sector PMI also fell below expectations to a 5-month low of 52.4 in June. Despite the drop, a reading above 50 still indicates expansion. Yet, German firms are reporting their lowest confidence towards future business activity in two years, with sentiment turning sour particularly in manufacturing due to fears over inflation, supply, and demand.

Commodities

Oil Rebounds

Prices for oil edged higher towards the end of last week after earlier falls. Investors are weighing the risks of a recession and how fuel demand may be affected by the combination of rising interest rates and tight supplies.

In Russia, President Vladimir Putin said trade and oil exports will be re-routed towards countries of emerging economies following Western sanctions due to the conflict in Ukraine. In May, China's crude oil imports from Russia were up 55% y/y. Meanwhile President Joe Biden called on congress to pass a three-month suspension of the federal gasoline tax to provide temporary relief for families this summer. Despite the Brent crude prices losing 0.67%, the commodity ended the week at \$113.12 per barrel.

Kuwaiti Dinar

USD/KWD closed last week at 0.30630.

Rates – 26 June, 2022

Currencies	Previous Week Levels				This Week's Expected Range		3-Month
	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.0470	1.0467	1.0605	1.0554	1.0360	1.0645	1.0628
GBP	1.2223	1.2159	1.2324	1.2262	1.2065	1.2360	1.2288
JPY	134.89	134.25	136.71	135.17	134.20	137.10	134.32
CHF	0.9717	0.9520	0.9717	0.9578	0.9370	0.9780	0.9519

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