Treasury Group
Weekly Money Market Report
30 April 2017

Premature Celebrations?

United States

Failing Promises

Now that the Trump Reflation tail winds have waned with policy paralysis in Washington, markets have started to lose patience with the new administration. While Congress averted a government shutdown this weekend, investors continue to digest the tax reforms announced earlier this week, so far providing little details on the government's intention to be fiscally neutral. Despite the tax cut proposal promised not to blow a massive hole in the US government budget, most economic analyses argued the type of tax cuts being promoted by Trump would likely fuel even larger deficits for a federal government already projected to see its debt steadily rise. Treasury Secretary Steven Mnuchin argued that the lower tax rates would generate so much economic growth that it would hold the deficit in check.

In parallel to the political mess, as data continue to disappoint in the US, Europe continue to prematurely celebrate Macron's first round and potentially the presidential victory with the currency standing out within the G10. European equity markets also rejoiced and are close to two year highs as the probabilities of a Le Pen win seem dramatically low and a united Europe is likely to emerge from this French victory.

In the UK, election campaigning is in full swing while German Chancellor Angela Merkel warned against any "illusions" the UK might have about Brexit talks, to which Theresa May appeared to respond by trying to incite voters into action by saying that EU governments are "lining up to oppose" Britain.

On the policy front, the ECB President Draghi failed to give markets on Thursday any hints prior the second round of the French election while he expressed his optimism over the Eurozone's economy. Nonetheless, he continued to exercise a cautious tone around the inflation target and did not indicate a substantial anticipated change in policy

In summary, on the currency front, the US Dollar ended the week under pressure after the weaker than expected growth data. First quarter GDP grew 0.7% annualized, prompting investors to start adjusting their expectation on overall growth for the year.

The Euro had a positive week on the back of higher than expected inflation as the Eurozone core CPI accelerated to 1.2% from 0.7%. Moreover, as polls continue to point that a Macron win is mostly the base case scenario, the currency managed to reach 5-months high of 1.0950 benefiting from less political risk in Europe, and rising geopolitical risks elsewhere.

The Sterling Pound was mostly stable to positive on the back of the Euro gains despite mostly a bit softer than expected data. Indeed, first quarter GDP came in at 0.3% versus a 0.4% consensus. Moreover, house prices fell unexpectedly in April and mortgage activity was weaker than forecast in March. Consumer confidence also slipped back in April although remains at healthy levels. The pair closed the week at 1.2900.

On the commodities front, prices of gold fell as investors demand for safe haven assets diminished after the first round French election outcome. On another front, a number of major crude-producing countries reached an initial agreement to extend output cuts as persistently high stockpiles weigh on prices. However, OPEC and other major suppliers have failed, after three months of limiting production, to achieve their target of reducing oil inventories below the five-year historical average.

Disappointing Data on all fronts

The US economy grew at its weakest pace in three years in the first quarter as consumer spending barely increased and businesses invested less on inventories.

GDP increased at an annual rate of 0.7% versus an expected 1.3% and a previous increase of 2.1% in the fourth quarter. Consumer spending, which accounts for more than two-thirds of US economic activity, slowed to a 0.3% rate in the first quarter, the slowest pace since the fourth quarter of 2009 and followed the fourth quarter's robust 3.5% growth rate. However, economists believe that with the labor market near full employment and consumer confidence near multi-year highs, the mostly weather-induced sharp slowdown in consumer spending is probably temporary.

Also, durable goods orders rose less than forecast in March as demand for automobiles and machinery all declined. Bookings for goods meant to last at least three years rose 0.7% against expectations of 1.5% while the core figure actually fell 0.2% against an expected 0.4% increase. The figures indicate that the slowdown in auto demand from consumers and tepid business investment weighed on manufacturers in March.

US consumers were less optimistic about the economy in the month of April after reaching the highest level in 16 years in March. The decline in optimism was largely on the back of the failing attempts by Republicans to pass legislations promised during the election campaign. In details, consumer confidence index fell by 4.6 points to 120.30, and individuals saying business conditions are good declined by 2.2%, while those saying business conditions are bad increased by 0.7%.
The index remained at a very high level even though consumers' assessments of current business and labor market conditions were less favorable than in March.

Finally, unemployment benefits increased to a 4-week high last week and Jobless claims increased last week by 14,000 to 257,000 above expectations of 245,000. The four-week average slightly changed at 242,250 from 242,750.

US Home Sales Jumped… Surprisingly

Not all data were negative as new home sales in the US rose unexpected in March as markets were predicting a decline. Sales jumped by 5.8% last month to an annual rate of 621,000, the highest rate since July 2016. Year on year new home sales were up by 15.6%, supported by a low mortgage rate environment.
New home constructions have been improving steadily for the past six years. However, they still remain below the levels seen before the housing bubble. Sales have now increased for three straight months defying expectations that low inventories and rising prices would constrain the market.

Europe & UK

Illusions Have to Be Tackle First

European Council President Donald Tusk urged that UK must settle the issues of "people, money and Ireland" before negotiation on future relationship with EU. The UK must also honor its financial obligations to EU before starting talks on trade agreements. This is when future relations could only start once "we have achieved sufficient progress" on these key issues. Tusk also emphasized that it's "not only a matter of tactics, but given the limited time-frame we have to conclude the talks, it is the only possible approach."

German Business More Optimistic

German business confidence increased more than expected in April, hitting its highest in nearly six years, as company executives are more optimistic about the current state of Europe's largest economy. The Munich-based IFO economic institute said its business climate index, based on a monthly survey of some 7,000 firms, rose to 112.9 from 112.4 in March. The reading is the highest since July 2011, came in stronger than market expectations for a value of 112.5.

Additionally, Germany's government slightly expanded its growth prospects for 2017 and 2018 after increased optimism about rising global demand. The government expects growth to accelerate by 1.5% in 2017 and 1.7% in 2018. Both years rose by just 0.1% from the previous forecast in January. In addition, with expectations that the German labor market will add around 1 million new jobs, which will support domestic demand and boost tax revenues.

Higher Annual Inflation

Euro area annual inflation surged to 1.9% in April, up from 1.5% in March. Core CPI also jumped sharply to 1.2%, up from 0.7% and beating expectation of 1.0%. Looking at the main components of the data, energy was again the main driver, increasing 7.5% in April. The other components such as services, food, alcohol & tobacco remained below the 2% mark.

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UK GDP Slows

The preliminary GDP estimates showed that the UK economy has slowed down in the first quarter of 2017. GDP growth fell more than expected to 0.3% in the first quarter from 0.7% in the previous quarter. The main contributor to the slowdown was in services where higher prices hurt the retail trade and accommodation sectors. The services sector, which makes up more than three quarters of the UK economy, slowed to 0.3% from 0.8% in the final quarter of 2016 and marking the weakest performance for two years.

Asia

Bank of Japan Kept Its Policy Unchanged

The Bank of Japan left monetary policy unchanged as expected, the interest rate kept at -0.1% and the 10-year yield target maintained at around 0%. The Bank of Japan showed the most optimistic assessment of the economy in 9-years at its policy meeting and defined recent weakness in inflation as temporary, indicating confidence a continued recovery will help to achieve its price target. It was the first time since March 2008 the BOJ used the word "expansion" to describe the state of the economy, signaling its conviction that the recovery was gaining momentum and that it saw no need for additional stimulus.

Bank of Japan Governor Kuroda voiced confidence that continued improvements in the economy will eventually boost wages and inflation, but conceded that progress has been slow. Moreover, Japan's economy has shown signs of life, as exports rose the most in over two years in March and manufacturers' confidence hit the highest since the global financial crisis a decade ago.

Australian Consumer Price Index Increased But below Expectations

Australian consumer price index increased 0.5% in the first quarter, slightly below market expectations. The major price increases in the quarter were for petrol up 5.7% and electricity up 2.5%, but this was partly offset by a 6.7% drop in fruit prices. It raised the annual CPI rate to 2.1%, and just inside the Reserve Bank's 2 to 3% target band. The annual rate of inflation came above 2% for the first time in 2-years but won't have the Reserve Bank reaching for interest rate hike lever anytime soon with question marks remaining over the strength of the labor market.

Kuwait

Kuwaiti Dinar at 0.30430

The USDKWD opened at 0.30430 on Sunday morning.

Rates – 30 April, 2017

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.0884	1.0819	1.0950	1.0895	1.0800	1.1115	1.0950
GBP	1.2812	1.2769	1.2965	1.2948	1.2855	1.3130	1.2987
JPY	110.04	109.57	111.77	111.53	110.60	113.80	111.14
CHF	0.9917	0.9892	0.9980	0.9950	0.9780	1.0030	0.9898