Treasury Group

Weekly Money Market Report

12 March 2017

Nonfarm Report Cements March Rates hike

United States

March Rate Hike a Certainty

This week's strong employment report cemented next week's hike now priced as a certain probability. For the skeptical, other than registering solid job gains in most sectors, unemployment rate dropped, participation rate climbed, and the annual growth rate in average hourly earnings bounced back after January's drop.
The other very positive news out of the report was the participation rate edging higher to 63% and the unemployment rate falling from 4.8% to 4.7%. The participation increase accompanied by a drop in unemployment rate is always a melody to Fed members prior to a FOMC interest rate decision.
The only caveat in the report was the fact that February was the warmest ever recorded and the effects showed up in the construction sector where payrolls jumped up by 58,000, the largest monthly increase since 2007. Another sector that seems to have seen the light in the wake of the Trump election is the Factory payrolls increasing by 28,000.

Back to Europe, ECB President Draghi maintained a status quo on the back of encouraging economic data rebound across the Euro zone without signaling any tapering needs for now. If growth momentum continues in the second half of the year following a positive election result in France, then the ECB press conference can recuperate its volatile status as the ECB monetary policy will most likely need to shift to a tapering stance. For now, all eyes turn to the Netherlands on March 15 and France May 7 in order to see if the block can be saved and no major political risk can materialize.

On the currency front, the US dollar index was well bid throughout the week but couldn't break the 102 level again. Although the ECB press conference was a non-event as Draghi did not want to rock the boat prior to the French elections, the currency bounced back higher by the end of Friday to end the week at 1.0678.

Investors continue to shun the Sterling Pound this week. As the currency moved slightly higher following the trade deficit figures release, other economic data did not help as industrial and manufacturing production were also released giving back about half of their prior months' gains.

In the commodities space, gold remained under pressure this week on the back of the strong economic data. The metal closed Friday around the $1,200 level.

Oil prices tumbled by the most in more than a year on Wednesday, after the EIA reported that US crude oil inventories had climbed for a ninth consecutive week. Brent crude ended the day down 5.3%, while crude fell by 5.8%. Prices recovered slightly on Thursday and Friday, but remained low even with the strong US Job report.

Former Fed Chairman Praises the FOMC Actions

In an interview given this week, Former Fed Chairman Ben Bernanke said the Federal Reserve was on "a pretty good track" as it prepares to raise interest rates next week and gradually thereafter. "They want to move enough to make sure that inflation does remain under control, which it is giving every indication of being."
He also added that Fed officials "are communicating that they intend to move next week and intend to continue to gradually normalize interest rates" afterward so long as the economic outlook remains strong, unemployment keeps falling and wage increases pick up. "So far it seems they're on a pretty good path," he said.
Finally, he also mentioned that he expects the Fed to begin reducing its $4.5 trillion balance sheet "about another year or so from now" after it has raised rates further away from the so-called zero lower bound. He endorsed Yellen's strategy of shrinking the balance sheet by allowing the Fed's bond holdings to roll off as they mature and not using it as an active tool of monetary policy.

On the validity of the Trump's administration promises, he advocated a little bit of caution as "a number of the elements of the Trump program are questionable in terms of their legislative prospects and advocated not to expect at some point both a reduction in the corporate tax rate and the income-tax rate. He also said he was "somewhat skeptical" that Congress would pass a big infrastructure program given the opposition of some Republican lawmakers to larger budget deficits.

US Data Solidify the case of a March Hike

According to the ADP employment change report, businesses added 298,000 private-sector jobs in February, significantly above the 189,000 consensus.
Goods-producing industries have been a great source of strength to the ADP in recent months. In February, they recorded a 105k rise and in January a 55k rise, up from monthly averages of 7k in Q4, 9k in Q3, and -2k in Q2 of last year. Construction payrolls have also accounted for 60% of the acceleration between Q4 and Q1 2017 manufacturing accounted for 33%; and energy 8%.
The data indicate that the U.S. job market remains robust in the beginning of 2017.

Outstanding US Nonfarm Report

Job growth increased more than expected in February and wages rose steadily, giving the Federal Reserve the green light to raise interest rates next week. Indeed, nonfarm payrolls rose by 235,000 jobs last month as the construction sector recorded its largest gain in nearly 10 years due to unseasonably warm weather. The economy created 9,000 more jobs in December and January than previously reported.
With the labor market near full employment, wage growth could speed up as companies are forced to raise compensation to retain employees and attract skilled workers. According to economists, wage growth of between 3% and 3.5% is needed to lift inflation to the Fed's 2% target.

Europe & UK

ECB Can't Turn Hawkish Before the French Elections

This week was the ECB's turn to signal a status quo, by reiterating its commitment to a substantial degree of monetary accommodation, while at the same time tweaking its language to acknowledge good data and reduced downside risk.
Markets took it as a sign that Draghi successfully managed a delicate balancing act by maintaining their interest rate easing bias, without extending the long term financing operations. Despite the fact that the ECB's new staff projections contain higher forecasts for growth and inflation, the ECB prefers to wait for the French elections results to potentially change their language during the June 8th meeting.

Economic Growth Happening in the Euro zone

The final reading of Europe's GDP came as expected in the fourth quarter of 2016. Overall 2016 growth came in at 1.7%, on the back of a strong momentum according to rising business output and higher consumer sentiment. Indeed, household spending has been powering the Euro zone's economies over the last year and rose by 0.4% in the quarter, while investments were up by 0.6%. The only laggard was the usual Greece contracting by a worse than expected 1.2% in the fourth quarter. Exports were up 1.5%, while imports climbed 2% from a 0.1% decline in Q3.

Although economists continue to expect political uncertainties and rising inflation to put the brakes on economic growth later on in the year, the Eurozone reaps the rewards of low interest rates and a brightening global economy in the beginning of 2017

UK "Brexit" Set for a Nasty Fight

In the wake of the "article 50" trigger, the German government told ministry staff this week that its primary aim in the upcoming Brexit negotiations is to stop the U.K. from dividing the European Union. According to the document drafted by the German Foreign Ministry, Germany's "foremost priority" during and after the negotiations with the U.K. is the continued unity of the 27 remaining EU nations.

In addition, Norway's energy and EU affairs minister was also critical of the situation saying that policy makers in Oslo will be forced to look in from the outside when the U.K. starts talks on its divorce and then attempts to forge a new relationship with Europe. He also added "that it's very difficult to find someone who's a winner from all of this"

Adding to May's headache, after repeatedly threatening to hold a second referendum on Scottish independence, the tone in Scotland has hardened in recent weeks. Brexit could represent a great opportunity for Nicola Sturgeon to hold another vote on independence before the UK leaves the EU. Clearly if this case materializes, it is likely to add uncertainties to the UK economy and the Sterling Pound.

Back on the economic front, the RICS (Royal Institution of Chartered Surveyors) of UK house price balance came in at +24 for February, unchanged from a revised +24 in January and ahead of the consensus estimate of 23. In details, housing market in the UK remained inactive in February, although falling supply continued to prop up price gains.
Stagnation in households' incomes, the stabilization in mortgage rates and the uncertainty emanating from the potential “Brexit” were the main drivers behind the unchanged prices. Also, according to the report, new buyers seem to have gradually lost interest since September and near-term expectations remain positive but point to a relatively modest rise in activity in the months to come.

Asia

Chinese Data Sending Mixed Signals

China’s inflation rose by 0.8% over the year in February against expectations of +1.7%, and fell by 0.2% on a monthly basis against expectations of +0.6%. Food prices were down by 4.3% mainly due to the timing of the Lunar New Year end of festivities.
The Product Price index increased on the other hand by 7.8% over the year in February, ahead of the +7.7% market estimate and the fastest of growth since September 2008

On the currency front, PBoC Governor Zhou Xiaochuan said that "as the Chinese economy stabilizes and becomes healthier, and the nation makes achievements in the supply-side reforms, and global investors become more confident in China’s economy, the yuan’s exchange rate will naturally be on a trend to stabilize. At the same time, we don’t have major changes to our related policies but we will be more precise when implementing and regulating the market. Therefore, under such circumstances, the yuan’s exchange rate will be relatively stable."

Japan’s Could Deliver Positive Surprises in 2017

Japan fourth quarter GDP was revised up to 1.2% on a yearly basis and +0.3% on a quarterly basis, but missed estimates of +1.6% and +0.4%. The increase was driven by the capital expenditure component of GDP, which rose by 2.0% over the quarter, the fastest pace of growth since Q1 2014.
Against expectations, Japan also reported a current account surplus of JPY65.5 billion in January, below the median forecast for a surplus of JPY239.0 billion, which seems to be omen of good news towards the export driven economy.

BoJ`s Board member Takako Masai said that the BoJ will “maintain highly accommodative financial conditions, with a view to achieving the price stability target of 2%, and ensure the overcoming of deflation. The Bank’s assessment is that Japan’s economy is expected to turn to a moderate expansion

Reserve Bank of Australia Over optimistic

The RBA left its cash rate as expected unchanged at 1.5% this week. In its statement, the central bank said that the improvement in global growth has led to higher commodity prices which in turn is “providing a significant boost to Australia's national income”. Regarding the exchange rate, the RBA noted that an appreciating exchange rate would complicate the transition following the end of the mining investment boom.

According to the RBA, the labor market “point to continued expansion in employment over the period ahead”. The Bank expects underlying inflation to remain low for some time “with growth in labor costs remaining subdued”. However, “headline inflation is expected to pick up over the course of 2017 to be above 2%, with the rise in underlying inflation expected to be a bit more gradual.”

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Kuwait

Kuwaiti Dinar at 0.30550

The USDKWD opened at 0.305٥٠ on Sunday morning.

Rates – 12 March, 2017

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.0614	1.0523	1.0699	1.0699	1.0535	1.0850	1.0723
GBP	1.2293	1.2134	1.2300	1.2169	1.2085	1.2425	1.2194
JPY	114.00	113.53	115.5	114.74	113.35	116.20	114.27
CHF	1.0081	1.0069	1.0170	1.0107	1.0005	1.0250	1.0057