Weekly Money Market Report
24 January 2020

US Dollar Weaker on Fiscal Stimulus Expectations

>NBK Treasury
+965 22216603
tsd_list@nbk.com

Highlights

- U.S. President Joe Biden calls for further stimulus.
- Bank of England members project recovery in Q2.
- European Central Bank leaves Policies unchanged.
- Bank of Japan updates economic forecasts.
- China maintains growth in 2020.

United States

Policy Guidance from the New Administration

The U.S. dollar weakened broadly against most currencies last week as inaugurated President Joe Biden called for further stimulus. The Biden administration is proposing a new USD 1.9 trillion COVID relief package that includes aid to states, direct checks to individuals, an extension of jobless benefits and further funding for the COVID-19 response. The administration is also reportedly preparing a second, multibillion-dollar recovery plan that would increase spending on infrastructure, green energy, healthcare and education, at least partially funded by higher taxes on the wealthy and corporations.

Former Federal Reserve Chairman and incoming U.S. Treasury Secretary Janet Yellen supported the call for further spending at her confirmation hearing before Congress. Yellen argued that they should take advantage of the historic low interest rate environment to provide more stimulus rather than worry over the rising debt burden. “The interest burden of the debt as a share of GDP is no higher now than it was before the financial crisis in 2008, in spite of the fact that our debt has escalated,” Yellen said. Therefore, she urged the Senate Finance Committee to “act big” now and focus instead on the interest being paid and the returns it will generate by supporting the economy.

The result of this updated policy guidance by the new Biden administration has seen U.S. equites reach new highs while at the same time, restarting the fundamentally lower dollar trend. In short, a massive stimulus boost to the world’s largest economy coupled with low interest rates, incentivizes investors to sink money into higher-yielding currencies on optimism about a rapid economic recovery led by the U.S.

UK & Europe

British Pound Supported

The British pound hit a fresh three year high last week as the general mood of the market turned to risk-on with the potential U.S. stimulus. Sterling was also supported as members of the Bank of England spoke about a “pronounced recovery” for the economy as vaccinations are carried out. Britain is now rolling out vaccines faster than almost anywhere else in the world and the government hopes to be able to ease restrictions significantly by Easter.

BoE’s Chief economist Andy Haldane said last Tuesday he expected Britain’s economy to begin to recover from the second quarter of this year. During a BoE online event the next day, Governor Andrew Bailey echoed Haldane's comments saying "I really do think that we are going to see a pronounced recovery in the economy as the vaccination program, as it is doing now, rolls out."

In the same event, the pound received another boost as Bailey again played down expectations that the central bank would introduce negative interest rates. "We have not taken any decision, in fact we've not actually discussed whether or not to introduce negative rates," Bailey said. "International evidence to date suggested negative interest rates were only effective in specific circumstances," he added.

The BoE is due to publish new growth forecasts on February 4 alongside a report on the feasibility of cutting interest rates below zero to boost growth, as has been done already in the euro zone and Japan.

European Central Bank

The European Central Bank kept policies on hold in their policy meeting last week as widely expected by markets. The Pandemic Emergency Purchase Program (PEPP) was re-confirmed at EUR 1.85 trillion and other policy instruments remained unchanged. The ECB warned that the recent surge in COVID-19 infections posed a risk to the euro zone's recovery and reaffirmed its pledge to keep borrowing costs at record lows to help the economy weather the pandemic.

ECB President Lagarde told a news conference, "The resurgence of the pandemic and the associated intensification of containment measures have likely led to a decline in activity in the fourth quarter of 2020 and are also expected to weigh on activity in the first quarter of this year." However, she was also optimistic about the start of vaccination programs, the UK-EU trade deal, the manufacturing recovery and reduced uncertainty surrounding US politics. On balance, the ECB sees the risks as still tilted to the downside, although less pronounced.

Asia

Bank of Japan

The Bank of Japan also left their policies unchanged and in line with market expectations. The bank did however, update its economic projections. The forecast range for real GDP growth for the current fiscal year was revised down marginally to -5.6% from -5.5% in October while the upcoming fiscal year was revised higher up to 3.9% from 3.6%. Core inflation forecasts were revised marginally higher for the current fiscal year to -0.5% up from -0.6% in October, and for the upcoming fiscal year to 0.5% up from 0.4%.

The updated growth and inflation forecasts will support expectations that the BoJ is unlikely to significantly loosen monetary policy following their March review. The better outlook suggests that any adjustments from the BoJ are more likely to focus on improving the quality of easing rather than the quantity.

Chinese Economy Maintains Growth

The Chinese economy accelerated to a strong finish in 2020, but challenges remain on the domestic consumption side, as the country now faces a renewed impact from COVID-19.

Gross domestic product grew 2.3% in 2020 and 6.5% year-on-year in the fourth quarter making China the only major economy in the world to avoid a contraction last year as many nations struggled to contain the COVID-19 pandemic. China is expected to continue to power ahead of its peers this year, with GDP set to expand at the fastest pace in a decade at 8.4%, according to a Reuter's poll.

The economic powerhouse has been fueled by a surprisingly resilient export sector with Chinese exports growing by more than expected in December as coronavirus disruptions around the world increased demand for Chinese goods even as a stronger yuan made exports more expensive for overseas buyers.

The manufacturing sector also continued to expand with industrial output rising at a faster-than-expected rate of 7.3% last month from a year ago, hitting the highest since March 2019.

Domestically however, momentum in retail sales growth slowed from November, showing household demand continued to face pressure and lagged behind in the recovery. Softer growth in December was due in part to an adjustment in consumer behavior following a stronger boost in November which had extended shopping festivals. Meanwhile, a resurgence of local COVID-19 cases in December has also kept household demand more subdued. For 2020, retail sales contracted 3.9%.

Overall, the mixed economic data was promising enough to reduce the need for further monetary easing by the Bank of China who has promised to scale back some policy support in 2021.

Commodities

Oil Gains Capped by COVID-19

Oil prices hit fresh highs last week before retreating on Friday over worries that new pandemic restrictions in China will curb fuel demand in the world's biggest oil importer. Recovering fuel demand in China underpinned market gains late last year while the United States and Europe lagged, but that source of support is fading as a fresh wave of COVID-19 cases has sparked new restrictions. Benchmark Brent crude closed out the week at $55.41, 1.21% from its open.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30285.

Rates – 24th January, 2021

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	High	Low	Close	Minimum	Maximum	Forward
EUR	1.2083	1.2189	1.2052	1.2167	1.2070	1.2355	1.2194
GBP	1.3592	1.3746	1.3518	1.3684	1.3580	1.3885	1.3691
JPY	103.75	104.08	103.31	103.77	101.80	105.75	103.66
CHF	0.8905	0.8925	0.8835	0.8852	0.8650	0.9055	0.8828