Treasury Group

Weekly Money Market Report

25 November 2018

Certain FED Members Alter Their Hawkish Tone

United States

US Equities in RED

US equity indices have persistently traded in the red zone over the past month and are starting to catch up with the weaknesses witnessed in Asia, Europe and emerging markets. YTD both the Dow Jones and S&P 500 are in negative terrain, reversing descent gains made in Q3 2018. Risk aversion is dominating the US stock markets and intensified after Vice President Pence criticized China. Pence promised to 'more than double' tariffs on Chinese goods unless Beijing changes its strategy. Furthermore, global growth is expected to diminish and FED members are expressing concerns about it. Fears of a peak in corporate earnings growth amidst higher interest expenses and worldwide trade tensions prompted trillions of dollars to be wiped off equities in October. Last month, the Dow Jones Industrial nearly sank 6.5%. As for last week, the index lost 4.35% of its value.

Moving on to the FED, some central bank officials have lately changed their hawkish tone towards increasing interest rates due to worries of weaker global growth and trade war fears. Dallas FED President noted that although domestic US economic performance was robust, it faces downside risks from frailer global economic conditions and fading effects of President Trump's tax reform. FED Vice Chairman Richard Clarida said that the recent monetary policy was near the neutral rate. Lastly, the FED Chair Powell also commented on the possible headwinds to US growth and restated that the US was on an unsustainable fiscal path. These dovish comments may elevate the probability that the FED will not stick to its forecast of 3 interest rate hikes in 2019.

US Consumer Sentiment Diminishes Slightly

The consumer confidence index by the University of Michigan declined to 97.5 this month, its second consecutive decline and slightly more negative than the initial reading of 98.3. The index is currently at a three months low. Looking at the sub-components, current economic conditions diminished to 112.3 and consumer expectations index dropped 1.3%. Rising interest rates and US stock markets continuously trading in the red zone were the elements that triggered the decline in the index. Mortgage refinancing requests tumbled to an 18-year low last week as elevated interest rates have made refinancing more unaffordable for many homeowners. Despite the decline in confidence, the economy appears to be in a decent shape. The labor market is robust, most households are in the best financial conditions in years and the US economy continues on outperforming its peers on most fronts.

Housing Market Pressured by Mortgage Rates

The figure for US home building rebounded last month by 1.5% to 1.228 million. The main factor that supported the rise was the post-hurricane rebuilding; as such the positive momentum in October may be short lived. At the start of the fourth quarter, housing starts remained 2.9% below the level registered in Q3. The details of the recent NAHB builders' confidence report were negative across the board, with both the present and future barometers of demand worsening. A recent survey indicated that sentiment among single-family homebuilders dropped to a more than two-year low in November, while builders reported that clients are taking a pause due to worries over rising interest expenses and home prices. The 30-year fixed mortgage rate is around a 7 years high at 4.94% and the FED is still expected to raise interest rates. In addition to rising interest costs, the housing sector is also being pressured by land and labor shortages, which have caused home prices to inflate.

Looking at the FX market, the US dollar index began last week's session in a negative manner, pulled down by dovish comments from FED officials. Financial markets seem to be contemplating whether the FED will carry through on its dot-plot implied forecast of 3x25bps rate hikes next year. The housing sector data also dragged the buck lower after home builder confidence recorded its sharpest one-month drop in over 4 years. Following the drop, the USD recovered its losses and consolidated throughout the week. The currencies market lacked clear direction due to uncertainty on the political front. The DXY opened Monday's session at 96.488 and ended the weekly session at 96.944.

Commodities

In the commodities complex, oil prices continued their descent into negative territory and are currently in a bear market as both Brent and WTI crude are lower by around 30% since the October high. Last week prices declined further when US crude inventories swelled to their highest level since December, fueling concerns about a global surplus. The oil sector has also been depressed by expectations of slowing global growth in the face of monetary tightening in the US, global trade tensions and most importantly a subdued sanction on Iran. Brent crude oil tumbled last week to the lowest level since October 2017.

To counter the surge in supply, OPEC members are considering a deal to lower production when it meets on December the 6th, however Iran is expected to resist any intended reduction. Russia has also shown no desire it would join any cut. Even though there are talks that OPEC and Russia may again reach a decision to a production cut, the concern is that not all relevant parties will be able to come to an agreement.

UK & Europe

ECB Remains on Track to End Bond Buying Program

The European central bank's meeting minutes reiterated that the Bank will proceed in ending the EUR 2.6 trillion bond buying program by year end, even as data out of the single block has slightly weekend. The ECB highlighted that the economic indicators out of the single economy were somewhat weaker than predicted, but remained consistent with an ongoing broad-based expansion. The latest run of frailer economic data is predicted to be a brief glitch by the central bank. As for the risks concerning the ECB, protectionism, weaknesses in emerging markets and financial market volatility remained significant. In regards to inflation, price growth in the EU has been improving gradually and the headline CPI is above 2% at 2.2% year on year. Therefore, the recent tensions globally and euro-zone data coming in below expectations were not enough to alter the ECB's monetary strategy.

Brexit and the Latest Draft

Last week the EU and the UK agreed on a drafted text setting out their future partnership that is due to be approved at a summit meeting on Sunday. The positive news directed the pound to rise more than 1% on relief that Britain will remain close to its largest market and have a flexible partnership with the single economy. However, the upward momentum was short lived as the document is a non-binding statement of intent and there's a possibility that UK officials will vote against the latest draft. If the draft is approved on Sunday's EU summit, the fate of Brexit will be in the hands of the UK parliament and members of the parliament are expected to vote in mid-December.

The leader of the opposition party Jeremey Corbyn didn't hesitate to call the 26-page draft a "waffle" and the Democratic Unionist Party were not impressed by the draft. Given the opposition PM May is facing, it will be difficult for the deal to pass in parliament the first time. The fact that the Sterling pound has not appreciated dramatically, advocates that the market is already anticipating a parliamentary defeat. The pound may be headed into a volatile month until the crucial date in December and its trajectory may depend on Brexit headlines.

EU May Impose Penalties on Italy

The Italian Deputy Prime Minister Matteo Salvini mentioned that he was not open to negotiations over Italy's 2.4% deficit target of GDP, which exceeds EU's guidelines. Hence, the European Commission stated that the Italian government may face penalties for not respecting the EU's fiscal guidelines. It would take time for the penalties to be imposed as there are still numerous steps to be concluded first. EU finance ministers are expected to meet on the 21st of January, which will be the first summit after the Italian budget has been approved. EU finance ministers may then ask a counteractive budget to be implemented within 6 months. If the demand for the amendment is not met by that point in time, then the EU can enforce penalties on Italy.

The euro started the week on a strong footing and did not hesitate to take advantage of the dollar's weakness. However after the rise, the EURUSD entered into a consolidative mode until Thursday as uncertainty over Brexit and Italy's budget were the main themes. On the last trading day, the euro depreciated 0.5% versus the USD after euro-zone PMIs' (Manufacturing & Services) declined. Furthermore, the German private-sector growth eased to its lowest level in almost 4 years. The euro lost 0.6% of its value to the dollar last week.

Asia

Japan's Price Growth Nowhere to be Seen

Japan's inflationary figures continue to disappoint on the downside and makes the BoJ's inflation target harder to achieve. The overall nationwide consumer inflation rose 0.2% to 1.4% y/y. However the central bank's preferred measure of core inflation remained stagnant at 0.4% y/y in October for the third consecutive reading. The pickup in the overall nationwide inflation was due to a sharp jump in fresh food prices, up 10.8% annually. This indicates that domestically generated inflation is nowhere to been seen and the elevated headline inflation was largely due to gains in non-core items. Hence, headline price momentum may decelerate in the coming months towards core inflation, especially with lower oil prices. Japan's economy is likely to remain in a negative interest rate environment in its efforts to uphold the inflation objective.

RBA's Meeting Minutes

The latest meeting minutes from Australia's central bank portrayed a positive picture for the economy, supported by a record low cash rate of 1.5%. Growth forecasts indicated an annual expansion of 3.5% for 2018 and 2019, before slowing to around 3.0% in 2020. The RBA also expects wages and inflation to gradually edge higher. The unemployment rate is anticipated to decline towards 4.75% from 5%. Looking at the negative factors, the central bank's governor mentioned that global trade tensions were a noteworthy risk to the global economy. Overall, economic progress is expected to diminish in 2020, although the pace of growth is projected to remain above potential. The Bank's own assessment suggests that there was no strong case for a policy change. However, the next move was still more likely to be up than down. The Australian dollar only moved slightly higher versus the greenback upon the release of the RBA Minutes, despite being positive.

Kuwait

Kuwaiti Dinar at 0.30380

The USDKWD opened at 0.30380 on Sunday.

Rates – 25th November, 2018

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.1415	1.1324	1.1472	1.1346	1.1140	1.1530	1.1440
GBP	1.2837	1.2761	1.2926	1.2821	1.2630	1.3030	1.2886
JPY	112.79	112.29	113.14	112.94	111.35	114.55	112.05
CHF	0.9998	0.9906	1.0005	0.9969	0.9790	1.0140	0.9882