PUBLIC

Weekly Money Market Report
24 July 2022

>NBK Treasury
+965 22216603
tsd_list@nbk.com

ECB Delivers First Hike in 11 Years

Highlights

- **The European Central Bank opted to join its global peers by delivering its first rate hike in 11 years in an effort to bring down persistent inflation. The bank hiked its deposit facility by 50 bps to 0%, ending a nine-year experiment with negative official interest rates. Meanwhile, PMIs revealed contractions in both services and manufacturing in Europe's largest economy.**
- **US jobless applications rose for a third straight week as hiring slowed amid recession fears. Still, the unemployment rate remains at a 50-year low that was last seen pre-pandemic.**
- **UK inflation reached a 40-year high of 9.4% y/y, mainly driven by a 9.3% surge in the price of motor fuel over the month. Other data revealed expansion in services & manufacturing in contrast to the Eurozone.**
- **New Zealand's annual inflation rose to 7.3% from 6.9% in Q1, illustrating more persistent inflation than the RBNZ had previously anticipated.**
- **The USD declined following three weeks of gains, providing some relief for the battered euro and pound. On Wall Street, tech stocks led gains following positive earnings results. Meanwhile, yields between the 2 & 10 year US Treasuries remain inverted - a historic sign of an upcoming recession.**

United States

Jobless Claims Hit 8-Month High

Applications for US state unemployment insurance rose for a third week to its highest level since November as more companies announced job cuts. Initial unemployment claims increased by 7,000 to 251,000 in the week ending July 16. Meanwhile, continuing claims for state benefits rose by 51,000 to 1.38 million in the week ending July 9, marking the biggest weekly increase since November.

Amid increasing fears of a recession, rising jobless claims will likely continue as the Federal Reserve delivers some of the largest interest-rate hikes in decades, which in turn could curb demand for workers. Still, the unemployment rate remained at 3.6% for a fourth straight month, matching a 50-year low that was last seen right before the pandemic struck in 2020.

Europe

ECB Delivers Unexpected 50bps Increase

The European Central Bank raised its key interest rate by 50 bps last week, marking its first increase in 11 years and the largest since 2000. Traders had expected a smaller hike of 25 bps in accordance with the bank's statement in its last meeting. The decision aligns the ECB with other hawkish central banks and ends an 8-year experiment with subzero borrowing costs. The central bank raised the rate on its deposit facility by 50 bps to 0%. Meanwhile the refinancing rate and the marginal lending rate were also hiked by 50 bps respectively to 0.5% and 0.75%. The surprisingly aggressive action came simultaneously with the approval of a new policy instrument titled "Transmission Protection Instrument", a new bond purchase scheme aimed at helping more indebted euro zone countries and preventing financial fragmentation with the currency bloc.

Speaking after the decision was announced, ECB President Christine Lagarde justified the larger hike saying: "Inflation continues to be undesirably high and is expected to remain above our target for some time. The latest data indicate a slowdown in growth, clouding the outlook for the second half of 2022 and beyond."

The central bank faces a tougher task than most of its global peers. Aside from setting monetary policy for 19 economies, the threat of a recession is greater due to the war in Ukraine, which is swelling food and fuel costs. Germany, Europe's largest economy, is particularly at risk due to its heavy reliance than most on natural gas from Russia, which has limited supplies after sanctions were imposed. Providing some relief, natural gasoline flows through the Nord Stream pipeline resumed last week after maintenance.

Contraction in Business Activity

Economic activity contracted in July as a downturn in manufacturing came alongside an almost stalled service sector growth. Eurozone preliminary figures revealed the composite PMI fell to 49.4 in July from 52.0 in June, breaking below the neutral level of 50 for the first time since February 2021. Excluding pandemic lockdowns, July's contraction marks the first since 2013. Looking at the backbone of the Eurozone economy, German activity saw contractions in both manufacturing and services PMIs with figures matching at 49.2.

Economists were expecting a mild expansion, instead these figures add to signs that a recession might be imminent. The data also highlights the vulnerability of the Eurozone economy that is now facing sudden stimulus withdrawal after the ECB delivered its first rate hike in over a decade. Energy supplies remain a major concern as Russia reduces natural gas flows in response to Western sanctions. "The euro zone economy looks set to contract in the third quarter as business activity slipped into decline in July and forward-looking indicators hint at worse to come in the months ahead," said Chris Williamson, chief business economist at S&P Global. "A steep loss of new orders, falling backlogs of work and gloomier business expectations all point to the rate of decline gathering further momentum as the summer progresses," Williamson added.

United Kingdom

Historic Cost-of-Living Crisis

UK inflation hit a new 40-year high in June alongside soaring food and energy prices, further escalating the country's historic cost-of-living crisis. The consumer price index gained 9.4% annually, up from 9.1% in May and slightly above forecasts. On a monthly basis, consumer prices gained 0.8% following a 0.7% rise in the previous month, still far short of the 2.5% monthly increase seen in April. The acceleration was driven by a 9.3% surge in the price of motor fuel over the month. Over the past year, motor fuel prices rose more than 40%, sending gasoline and diesel prices to record high figures.

The Bank of England has so far implemented five consecutive 25 basis point hikes as it attempts to rein in inflation without tipping the economy into a recession. In its upcoming August meeting, BOE Governor Andrew Bailey suggested in a speech last week that the Monetary Policy Committee may consider a more aggressive 50 basis point hike. That would constitute the UK's largest single increase in interest rates for nearly 30 years. Prices are now rising far more quickly than wages, and inflation is expected to top 11% in October when another energy price-hike kicks in. Latest ONS figures revealed real wages over the three months to May experienced their steepest decline since records began.

Bailey stressed that there would be "no ifs or buts" in the central bank's commitment to return inflation to its 2% target. "From the perspective of monetary policy, these times are the largest challenge to the monetary policy regime of inflation targeting that we have seen in the quarter century since the MPC was created in 1997," Bailey said. He added, "That emphatically does not mean the regime has failed. Far from it. The regime was set up for times exactly like these. The regime, founded on central bank independence, is now more important than ever. The worth of any regime is tested in the difficult, not the nice times."

Business Activity Weakens

Britain's business grew at its slowest pace in 17 months as preliminary readings covering both services and manufacturing firms fell to 52.8, their lowest since February 2021. The PMI also showed input cost inflation at a 10-month low, or an 18-month low for manufacturers. Nevertheless, in contrast to the Eurozone, the readings remained in expansionary territory above 50.

Other data published last week showed consumers cut back on their shopping in June and consumer confidence remained at an all-time low. As consumers struggled with high prices, retail sales fell however by a less than expected 0.1% m/m from May according to the Office for National Statistics. Excluding automotive fuel, volumes in June rose by 0.4% m/m. The data may reduce pressure on the Bank of England to deliver a more aggressive interest rate hike next month that would add to the drag on economic activity.

Asia Pacific

New Zealand Prices Running at 3-Decade High

Inflation in New Zealand accelerated more than expected in the second quarter of 2022, fueling bets that the central bank will need to continue on their aggressive rate hike path. Annual inflation rose to 7.3% from 6.9% in Q1, illustrating more persistent inflation than the Reserve Bank of New Zealand had previously anticipated.

In May, the RBNZ forecast inflation would peak at 7% this year then ease back by late 2023. However, just last week, the bank acknowledged there was a "near-term upside risk" to inflation and opted to deliver its third straight half percentage point increase. The official cash rate rose to 2.5%, with the central bank adding that it will keep tightening monetary policy "at pace."

Commodities

OPEC+

Last week, Russia's President Vladimir Putin and Saudi Crown Prince Mohammed bin Salman discussed continued cooperation within OPEC+ in a phone call according to a statement from the Kremlin. "It was emphasized that a further coordination within OPEC+ is important," according to the statement. "It was noted with satisfaction that member states are consistently meeting their obligations to support the necessary balance and stability in the global energy market."

The exchange comes just two weeks before the Organization of Petroleum Exporting Countries and its allies meet to discuss production strategy on August 3rd. Those talks could determine whether the group delivers additional oil, as heavily requested by US President Joe Biden. Oil prices edged higher on Friday after recent selling on the back of weakened demand in the the world's largest consumer of crude, the US. Data released earlier last week revealed US gasoline demand had dropped nearly 8% y/y even during the peak summer driving season. This has placed pressure on the WTI contract, while in contrast the Brent benchmark ended its first weekly gain in six weeks aided by strong Asian demand.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30725.

Rates – 24th July, 2022

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.0083	1.0077	1.0278	1.0210	1.0030	1.0310	1.0280
GBP	1.1874	1.1859	1.2063	1.2002	1.1810	1.2120	1.2030
JPY	138.53	135.56	138.87	136.05	135.15	138.05	135.08
CHF	0.9762	0.9598	0.9791	0.9613	0.9420	0.9820	0.9548