Weekly Money Market Report
06 January 2019

2019 Takes off with Risk Aversion

United States

Safe Haven Demand Intensifies

As the New Year kicks off, investors worldwide are running towards safe haven assets. Economic indicators out of China and Europe are elevating the probability of a recession due to contractions in their manufacturing industries. Looking at the US, the manufacturing sector recorded the largest drop since the great financial crisis and Apple lowered its revenue forecast by around 10%. The corporation warned that nearly all of the disappointment is attributed to the economic downturn in China which they did not foresee. Global economic concerns have been recently rattling financial markets and especially the US yield curve inversion.

The US treasury yield curve inversion worsened quite seriously in the past 2 weeks. It's clearly inverted as 1-year (2.57%) is greater than the 2-year (2.50%), 3-year (2.48%), 5-year (2.50%) and the 7-year (2.56%). In regards to rate hike expectations, financial markets are now pricing in a greater possibility that the Federal Reserve will cut rates rather than raise them in 2019 and 2020, while the Federal Reserve anticipates raising the cost of interest. The divergence in expectations suggests that investors believe the US central bank will not be able to continue to tighten monetary policy and is effectively saying that at some point in the near future, the central bank is going to have to not only stop hiking, but actively start easing. In the wake of last week's market panic, the best performers were the safe haven Japanese yen, gold, and US government bonds.

A Robust Labor Market

The American economy added 312,000 jobs in December, the fastest rate of hiring in 10 months. Readings for October and November were revised higher by 58,000. Overall, the US economy produced 2.6 million jobs last year compared to 2.2 million in 2017. Despite the decent hiring, the unemployment rate rose from 3.7% to 3.9% as the participation rate edged higher by 0.2% to 63.1%. On the wages front, average hourly earnings inflated by 0.4% m/m, sending the annual rate to the highest level since 2009 at 3.2%.

The labor report was extremely positive and could lessen market worries that the Federal Reserve may be forced to cut interest rates. Nevertheless, the mounting concerns facing the US economy (weakening global demand, diminishing support from the tax cuts, elevated interest expenses, trade war theme, stronger US dollar, government shutdown and a yield curve inversion) continue to cast doubts over whether such strength is sustainable.

US Manufacturing PMI Tumbles

The monthly manufacturing survey out of the US (ISM PMI) has shrunk quite significantly from 59.3 to 54.1, the largest monthly drop since the 2008 financial crisis. The index is currently at its lowest level since November 2016 and just five months ago, the index was at a 14-year high. As for the main factor prompting

All information sourced from Reuters. For further information, please contact NBK Dealing Room on 22462046 (Telephone), 22419720 (Fax) or TSD_LIST@nbk.com . This report is a publication of National Bank of Kuwait. It is designated for information only, National Bank of Kuwait accepts no liability whatsoever for any direct or consequential loss and/or damage arising from its use.

the decline, the New Orders Index registered a reading of 51.1, a decrease of 11 percentage points from 62.1. The Production Index also fell by 6.3 points to 54.3. The manufacturing PMI is still above 50, indicating an expansionary environment. However, the 5.2 points descent seen last month has been exceeded just twice this century, both times during recessions; the first during the 9/11 terror attack and also in the great financial crisis era.

Additional reports such as the five indexes from the Federal Reserve of regional manufacturing all tumbled last month, the first time they've fallen in unity since May 2016. It seems that higher tariffs and the trade war theme are starting to take its toll on the economy. As positivity in US data retreats and with monetary policy officials already stating that they intend to lessen the pace of interest-rate hikes in 2019, gives them more reason to pause on monetary tightening. Last week, Dallas Federal Reserve President said the central bank must preserve current interest rates, while it waits to see how uncertainties globally and domestically play out.

The US dollar index began last week's session on a downward trajectory, pressured by the ongoing government shutdown. However, the USD's negative momentum was short lived as investors rushed to safety assets after PMIs' in the EU and China fell into contraction territory. The latest upbeat US labor report also had a positive effect for the dollar. Before markets closed for the weekend, the dollar's positivity faded after the Federal Reserve Chairman stated that the central bank is not on a preset path of interest rate hikes and suggested that the Bank could pause its policy tightening as it did in 2016. The dollar index depreciated 0.22%, over the past 4 trading sessions. On the political sphere, 25% of the US government has been at a halt for more than 2 weeks and around 800,000 government employees are not receiving any payments from the Federal government. Republicans have so far rejected a proposal from Democrats for a funding bill that would reopen the government, but doesn't offer funds for a wall. Thus, for the time being, there is still no end in sight for the partial shutdown as Democrats are in control of the House, while Republicans govern the Senate. If the political drama persists, it may pressure the dollar into the red zone.

Commodities

Oil Prices Rise on Lower Supply

In the commodities complex, oil prices rebounded on the first trading week of 2019 thanks to diminishing OPEC supplies by the largest amount in almost two years and an improving sentiment on the trade front. In details, OPEC members pumped 32.68 million bpd in December, down by 460,000 bpd from November's reading. The latest figure suggests that some OPEC members have already decreased output production even before the implementation of the 1.2 million bpd cut agreement between OPEC and 10 other oil producing nations. Brent crude oil rose around 7% last week.

UK & Europe

Frail Manufacturing Data out of Europe

The manufacturing sector in the euro-zone has been on a downward path in the last five months and the latest Purchasing Managers' Index is the weakest data since February 2016 at 51.4. The big-four economies (Germany, France, Italy & Spain) posted the poorest manufacturing PMI readings of all countries monitored during December. Most importantly, for the past three months, Italy has remained in a contractionary territory (PMI below 50) and France also joined the negative environment for the first time in 27 months. The German PMI fell towards 51.5 a 33-month low, while France's reading declined to 49.7. Spain's PMI shrank by 1.5 points to 51.1, the weakest in 28 months. In the last 3 months of 2018, euro-zone manufacturers reported the frailest quarterly performance in terms of production since Q2 2013.

The recent negativity seen in the manufacturing industry could prove transitory, being the consequence of protests in France and the auto sector struggling to adapt to new emissions guidelines. Nevertheless, weak demand and intensifying risk-off atmosphere indicates that any rebound may prove minimal at best, with

All information sourced from Reuters. For further information, please contact NBK Dealing Room on 22462046 (Telephone), 22419720 (Fax) or TSD_LIST@nbk.com . This report is a publication of National Bank of Kuwait. It is designated for information only, National Bank of Kuwait accepts no liability whatsoever for any direct or consequential loss and/or damage arising from its use.

Brexit concerns shadowing over Europe. Overall, the global trade war theme is still in the background and the ECB has tightened its monetary policy.

Disinflation in the Euro-zone

Additional signs of cooling down in the EU block resurfaced last week as the consumer inflation on an annual basis declined to an 8-month low of 1.6% in December from 1.9%. Yet, core inflation remained unchanged at 1%. Hence, it is evident that the softer consumer price growth was mainly depressed by energy prices, which sunk from 9.1% y/y to 5.5% y/y last month.

Energy contributions towards price momentum are now coming off, so the CPI rate may have reached its recent peak of 2.2%. If oil prices remain subdued, while the pace of growth globally is projected to shrink, the CPI could even ease further. In conclusion, the latest reading leaves the European Central Bank in an uncomfortable position with regards to their first rate hike, which is expected to occur during Q3 2019. But then again, with inflation moving away from the 2% objective and an economy that is decelerating, the query is whether the monetary policy setters will see a chance to hike at all.

In the currencies market, the euro was slightly subdued last week as risk aversion was the main theme. Additionally, the euro-zone manufacturing data out of Spain, France, Italy and Germany were weak. The EUR/USD opened the week at 1.1438 and ended at 1.1394.

Asia

China's Manufacturing Sector in Contraction Mode

China's state-owned manufacturing sector shrank to the lowest level since February 2016 to 49.4, while the manufacturing PMI for the private sector also fell into contractionary territory for the first time in 19 month. The manufacturing PMI declined from 50.2 to 49.7 in December. The 50 level is the barrier between growth and contraction. As for the sub-components, both new orders and new export orders were in negative terrain, below the 50 threshold. New export orders diminished for a seventh consecutive reading last month from 47.0 to 46.6. The second largest economy in the world has been facing domestic headwinds even before the intensification of trade tensions with the US. The latest readings indicate a weak demand externally and domestically.

Looking at other economic indicators, recent statistics have also pointed to a weakening economy. Earnings at industrial businesses fell in November for the first time in nearly three years and retail sales, a closely watched indicator of domestic demand, expanded at the slowest pace in 15 years. The persistence of frailer data has already driven the government to launch a sequence of stimulus measures. At the annual economic work conference in December, Chinese officials pledged to decrease taxes, elevate infrastructure spending and loosen monetary policy. Despite the government's effort to support the economy, global growth in 2019 is expected to diminish. China is the largest exporter in the world; hence the government's strategy may not be enough to halt the downward momentum in growth.

The air was filled with risk as the New Year kicked off and the safe haven Japanese yen outperformed all currencies last week. At a certain point, the USD/JPY spot rate collapsed towards 104.87 from 108.87, the lowest level since March 2018 after Apple warned that revenues could come in 10% lower than their initial forecast. However, the move was over exaggerated due to thin liquidity and the sharp fall occurred during the early Asian trading hours. The dollar regained its momentum after the harsh decline, but still managed to close the week lower against the JPY. The yen gained 1.64% against the dollar in the preceding week.

All information sourced from Reuters. For further information, please contact NBK Dealing Room on 22462046 (Telephone), 22419720 (Fax) or TSD_LIST@nbk.com . This report is a publication of National Bank of Kuwait. It is designated for information only, National Bank of Kuwait accepts no liability whatsoever for any direct or consequential loss and/or damage arising from its use.

NBK الوطني

Kuwait

Kuwaiti Dinar at 0.30315

The USDKWD opened at 0.30315 Sunday morning.

Rates – 09 December, 2018

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	High	Low	Close	Minimum	Maximum	Forward
EUR	1.1442	1.1497	1.1307	1.1393	1.1195	1.1595	1.1481
GBP	1.2680	1.2814	1.2436	1.2726	1.2525	1.2930	1.2785
JPY	110.42	110.47	104.96	108.52	106.50	109.50	107.73
CHF	0.9839	0.9919	0.9794	0.9863	0.9665	1.0070	0.9779

All information sourced from Reuters. For further information, please contact NBK Dealing Room on 22462046 (Telephone), 22419720 (Fax) or TSD_LIST@nbk.com . This report is a publication of National Bank of Kuwait. It is designated for information only, National Bank of Kuwait accepts no liability whatsoever for any direct or consequential loss and/or damage arising from its use.