Treasury Group

Weekly Money Market Report

21 January 2018

US Dollar Pressured by Government Shutdown

United States

US Dollar Remains Subdued

The US dollar continued to be pressured last week as fears of a potential government shutdown mounted. President Donald Trump and Republican leaders in Congress were racing to meet a midnight Friday deadline to pass a short-term spending bill to keep the US government open and prevent agencies from shutting down. Without the injection of new money, federal agencies across the United States would be forced to close starting at midnight Friday the 19th, when existing funds expire. In the late-night session, Democrats and Republicans, locked in a bitter dispute over immigration and border security, failed to agree on a last-minute deal to fund its operations. As such, the US government technically ran out of money and shut down its operations putting hundreds of thousands of "non-essential" federal workers on temporary unpaid leave. Democratic and Republican leaders did however, agree to reopen negotiations on Saturday and said were committed to getting a quick agreement.

The US dollar had also been pressured by strengths in other major economies as investors were selling on the view that other central banks will join the Federal Reserve in tightening monetary policy. The Bank of Canada followed suit last week by hiking the benchmark interest rate by 25 basis points while the Bank of Japan trimmed its purchases of long dated Japanese government bonds last week. Although the BOJ is unlikely to exit from its current policy stance anytime soon, the 10 year Japanese bond yield increased 1.1 basis points since the cut. Finally in Europe, the recent release of the European Central Bank's minutes for their December meeting hinted that tighter monetary policy, which includes the possibility of higher interest rates as well as the winding down of asset purchases, could be on the horizon amid strong European economic growth. The prospect of a reduction in the interest rate differential between the Fed and other central banks has helped pressure the US dollar index to a two-year low.

The US dollar index fell to a new low at the start of the week where it remained subdued as fears of the US government shut down loomed. The index fell 2.09% from the previous week's high of 92.640 to close the week at 90.690

The euro on the other hand, posted its fifth consecutive week of gains reaching a two year high of 1.2322. Investors are now focused on the European Central Bank's meeting February the 8th. The EUR/USD pair closed the week at 1.2220.

The British pound was also supported to new highs this week as the Brexit negotiations passed a new hurdle. Theresa May's cabinet has agreed to increase the UK's financial offer to the European Union for the Brexit divorce bill to in an attempt to break the deadlock in negotiations. Media reports suggest the figure is in the region of 40 billion pounds. The GBP/USD pair opened the week at 1.3728 and closed at 1.3856.

The Japanese yen opened the week 1.41% stronger against the US dollar after the Bank of Japan unexpectedly reduced its purchases of Japanese government bonds January the 9th. The move led to speculation that the central bank may be leaning towards tighter monetary policy. Investors will be cautiously waiting for the Bank's next meeting on January the 23rd. The USD/JPY pair closed the week at 110.76.

In the commodities sector, oil slipped off its three year high as analysts warned of a downward correction after prices have gained more than 13% over the past month. Healthy demand growth and OPEC's production cuts have helped fuel price gains during recent weeks. On the other hand, US shale is positioned to break an output level of 10 million barrels per day, a number last reached in 1970 during the US energy crisis. Brent crude was last $68.71 while US West Texas Intermediate closed the week at $63.33.

US Industrial Production

Industrial production in the United States increased at the fastest pace since May. Cold weather during the end of December managed to boost demand for heating, while manufacturing output stayed flat. Meanwhile, the Fed also reported that the capacity utilization rate increased to 77.9%, above market expectations. The rate is a leading indicator of consumer inflation - when producers are nearing full capacity they respond by raising prices, and the higher costs are usually passed on to the consumer.

New York Empire State Manufacturing

Business activity continued to grow at a solid clip in New York State, according to firms responding to the January 2018 Empire State Manufacturing Survey. The headline general business conditions index, at 17.7, was little changed from last month's level. The new orders and shipments indices both showed ongoing growth, although at a slower pace than in December. Unfilled orders and delivery times increased slightly, and inventory levels were higher. Labor market conditions pointed to a modest increase in employment and steady workweeks. Both input prices and selling prices increased at a faster pace than last month. Firms remained very optimistic about future business conditions and capital spending plans were robust.

US Housing & Construction

Housing starts on new US homes eased from the fastest pace in 13 months while permits held steady to finish the strongest year for housing construction in a decade, government figures showed Thursday. Annual totals for permits, starts and completions were all the highest since 2007. The level of permits indicates construction should pick up in the coming months. A separate report on Wednesday showed homebuilders' confidence in January at the second-highest level since 2005. More construction would help ease an inventory crunch that the National Association of Realtors has flagged as an impediment to more sales. However at the same time, last month's tax-cut legislation that curbed deductions for mortgage interest and property taxes could weigh on housing in some states.

Canada

Bank of Canada

The Bank of Canada announced its decision to increase the benchmark interest rate from 1.00% to 1.25%. The decision comes after a run of strong economic data. Nevertheless, the central bank indicated it's in no rush to embark on an aggressive interest rate path as it cited future uncertainties including the fate of the North American Free Trade Agreement. "While the economic outlook is expected to warrant higher interest rates over time, some continued monetary policy accommodation will likely be needed to keep the economy operating close to potential and inflation on target."

Europe & UK

Euro zone Inflation

Euro zone inflation eased in line with expectations in December, according to a revision released by Eurostat. The European Union's statistics office said the consumer price index rose at an annual rate of 1.4% in December, down from 1.5% in November. The rates were in line with expectations but below the ECB target inflation rate of 2%, supporting the central bank's approach to gradually increasing interest rates. Meanwhile inflation rose by 0.4% month-over-month in December, compared to a previous reading of 0.1%. Core inflation, which excludes energy and food prices and is closely watched by the ECB, rose by an annualized 0.9%.

UK Inflation

Consumer prices in the UK eased slightly to 3.0% in December from 3.1% in November. The data comes in line with market expectations as well as the Bank of England's projections that inflation in the UK would peak in November and December before moving back towards the 2% target. Year-on-year the core figure was at 2.5%. The downward effect came mainly from air fares, along with a fall in the prices of a range of recreational goods, particularly games and toys.

Asia

China GDP

China's economy grew faster than expected in the fourth quarter of 2017, as an export recovery helped the country post its first annual acceleration in growth in seven years, defying concerns that intensifying curbs on industry and credit would hurt expansion. Growth for the 2017 full year picked up to 6.9% year-on-year, the first annual acceleration for the economy since 2010 beating expectations. While economists believe fundamentals will remain intact in 2018, some downside risks remain. Risks include more forceful US trade restrictions on Chinese exports, higher borrowing costs, and an increase in environmental regulations that has hurt the industrial sector in many parts of the country. However, the data remains optimistic allowing policymakers some leeway to cut debt and pollution in older industries without stunting growth.

Kuwait

Kuwaiti Dinar at 0.30055

The USD/KWD opened at 0.30055 on Sunday morning.

Rates – 21 January, 2018

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	High	Low	Close	Minimum	Maximum	Forward
EUR	1.2196	1.2322	1.2163	1.2220	1.1995	1.2420	1.2290
GBP	1.3728	1.3945	1.3720	1.3849	1.3655	1.4050	1.3900
JPY	111.05	111.48	110.18	110.76	108.80	112.75	110.22
CHF	0.9678	0.9685	0.9534	0.9628	0.9420	0.9825	0.9565