Weekly Money Market Report
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Mixed US Data Fuels Less Hawkish FED Expectations

Highlights

- **Inflation in the US continues to simmer, keeping the Federal Reserve on track to hike interest rates by 75 bps in their upcoming meeting. Yet expectations of a smaller 50 bps hike in December are starting to grow amid the recent slowdown in economic activity.**
- **The European Central Bank (ECB) raised interest rates again last week and announced it was changing the terms of its low-cost loans to commercial banks in a bid to reduce its bloated balance sheet and curb historically high inflation.**
- **The Bank of Japan kept its short-term interest rate target unchanged at -0.1% and reiterated its pledge to guide the 10-year government bond yield around 0%.**
- **The UK's former Chancellor Rishi Sunak has become the country's third Prime Minister this year. Markets have responded positively with the pound recovering and gilts rallying significantly.**

United States

Dollar Under Pressure

The dollar traded near a one-month low against its major peers last week as signs of an economic slowdown continue to mount in the United States. The market is still predicting another 75 bps hike by the FED this week, yet expectations of a smaller 50 bps hike in December are starting to grow amid the recent slowdown in economic activity. In tandem with expectations of reduced hawkishness from the FED and deteriorating economic activity, U.S. 10-year Treasury yields descended from October's multi year high of 4.338%, further pressuring the greenback. Although expectations of a less aggressive Fed are on the table, inflation figures released on Friday indicated that the fight against inflation is far from over and rate hikes could continue for longer. The Dollar Index, which measures the currency's performance against a basket of its major peers, closed the week at 110.752 after opening the week at 112.137.

PCE Core Inflation Data Rises in September

Inflation in the US continues to simmer, keeping the Federal Reserve on track to hike interest rates by 75 bps in their upcoming meeting. The personal consumption expenditures (PCE) price index rose 0.3% last month after a similar gain in August. Annually, the PCE price index increased 6.2%, matching August's rise. Excluding volatile food and energy components, the core PCE price index climbed 0.5% after increasing by the same margin in August. On an annual basis, the core PCE climbed 5.1% in September after increasing 4.9% in August.

Inflation Concerns Dampen Consumer Confidence

U.S. consumer confidence retreated in October after two straight monthly increases amid heightened concerns over inflation and a possible recession next year. The Conference Board's consumer confidence index fell to 102.5 in October from 107.8 last month, and lower than the expected 106.5. The report showed that the Federal Reserve's aggressive interest rate hikes are starting to cool the labor market, with a decline in the share of consumers viewing jobs as "plentiful" and a rise in those saying employment was "hard to get." Nevertheless, the report also showed that consumers are ready to spend on some big-ticket items within the next six months, such as homes and motor vehicles, which might provide some stability for the economy in the near term.

House Prices cool down for a second consecutive month

U.S. house price growth slowed more than expected in August amid record low supply following ultra-high pandemic driven demand, material scarcity and record high borrowing costs. The S&P Case Shiller national home price index dropped 0.9% on a seasonally adjusted basis after slipping 0.5% in July. House prices increased 13.0% on a year-over-year basis in August, slowing from July's rise of 15.6%.

US Economy Expands in Q3

Last week's U.S. GDP figure indicated a return to economic growth in the third quarter thanks to a narrowing trade deficit. However, the report showed that domestic demand was at its weakest in two years because of the Federal Reserve's aggressive interest rate hikes. Furthermore, residential investment contracted for a sixth consecutive quarter, highlighting the sector's struggle amid soaring mortgage rates. The return to growth after two straight quarterly declines in GDP offered evidence that the economy was not in a recession. Gross domestic product increased at a 2.6% annualized rate last quarter after contracting at a 0.6% pace in the second quarter. Economists expected GDP growth would rebound at a 2.4% rate.

Europe

The European Central Bank Hikes as Expected

The European Central Bank (ECB) raised interest rates again last week and announced it was changing the terms of its low-cost loans to commercial banks in a bid to reduce its bloated balance sheet and curb historically high inflation. The central bank raised its deposit rate by a further 75 basis points to 1.5%, the highest rate since 2009. Until as recently as July, ECB rates had been in negative territory for eight years. "The Governing Council took today's decision, and expects to raise interest rates further, to ensure the timely return of inflation to its 2% medium-term inflation target," the ECB said in a statement.

The ECB also announced some changes to the terms of its Targeted Longer-Term Refinancing Operations (TLTROs). From November 2022, rather than the average deposit rate prevailing since banks took the loans, banks meeting the lending benchmark will pay the average depo rate prevailing from November 2022 until maturity or early repayment. The aim, as Lagarde stated, is to ensure that tighter monetary conditions are transmitted to the real economy, as well as removing "deterrents to early voluntary repayments", which in turn might help reduce the ECB's balance sheet without having to wait until June when the next EUR1.3 trillion repayment is due.

Market Reaction

Traders took the announcement as slightly dovish due to a change in the ECB's forward guidance, from the governing council "expects to raise interest rates further … over the next several meetings" to just "expects to raise rates further", removing "over the next several meetings." The Euro traded at a weekly high of 1.0093 before the ECB announcement and dropped significantly to a low of 0.9956 afterwards. The single currency seesawed around the parity level on Friday only to close the week higher at 0.9963.

Eurozone Economic Activity continues to Deteriorate

The S&P Global euro zone flash composite Purchasing Managers' Index (PMI), seen as a good guide to overall economic health, fell to 47.1 from 48.1 in September, below expectations for 47.5. October marked the fourth month below the 50 mark separating growth from contraction and was the lowest reading since November 2020. Similarly, the regions services & manufacturing PMI dropped to 48.2 and 46.6 respectively, in line with expectations but at their lowest point in 20 months. Factories have been hit hard by rising energy prices and recovering supply chains from the coronavirus pandemic, further pressured by Russia's invasion of Ukraine.

United Kingdom

Pound Gains on the back of the so-called "Sunak Affect"

The UK's former Chancellor Rishi Sunak has become the country's third Prime Minister this year. His selection brings a halt to the instability witnessed in recent British policymaking. Markets have responded positively with the pound recovering and gilts rallying significantly in anticipation that the new Prime Minister will resort to a more conventional approach to restore credibility in the face of the UK's looming economic challenges. Although the markets appear to have welcomed the news, substantial challenges for the UK economy persist in the context of high inflation, a cost of living crisis, fiscal restraint and a probable recession.

The British pound continued its significant recovery this week, reaching a high of 1.1645 against the dollar after opening the week at 1.1332. The pound lost some of its momentum on Friday and closed the week at 1.1610. The currency has recovered significantly from its historic lows hit following the release of the Truss government fiscal event in September, but still the currency is down almost 14% year-to-date.

Economic Activity continues to Weaken

The S&P Global/CIPS flash Composite Purchasing Managers' Index (PMI) showed a contraction in activity for a third month in a row, sinking to a 21-month low of 47.2 from September's 49.1 and below the expected 48.1. The figure indicates that the UK's economy could be on course for a potentially deep recession. The services sector PMI contracted for the first time in 20 months, falling to 47.5 from the neutral level of 50.0 in September. Similarly, the manufacturing figure fell to 45.8 in October from last month's 48.4. The figures highlight the impact on firms from the chaotic period after ex-Prime Minister Liz Truss's government announced unfunded tax cuts in late September that triggered a bond market rout and were eventually reversed.

Japan

Bank of Japan Unmoved by Speculators

As widely expected, the central bank kept its short-term interest rate target unchanged at -0.1% and reiterated its pledge to guide the 10-year government bond yield around 0%, pushing back against market speculation that it will adjust policy as it continues to predict inflation will fall below 2% next year. In a conference after the announcement, Governor Kuroda stated that the market should not expect a rate hike anytime soon. The Bank of Japan (BOJ) decision came just hours after PM Fumio Kishida announced around $200 billion in fresh spending that will likely help the BOJ maintain its policy for longer by relieving some of the pain caused by soaring energy prices, partly inflated by a weaker yen.

The Japanese yen

Early in the week, the Japanese yen traded in a volatile manner against the dollar, reaching a short-lived weekly low of 149.70 on Monday. The yen gained dramatically within minutes to reach 145.28 amid speculation that the BOJ intervened in the market. The pair continued to trade in a wide range throughout the week and closed at 147.45.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30890

Rates – 30th October, 2022

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	0.9865	0.9805	1.0093	0.9963	0.9840	1.0100	1.0042
GBP	1.1354	1.1255	1.1645	1.1610	1.1470	1.1890	1.1653
JPY	147.56	145.10	149.69	147.45	145.40	151.00	145.67
CHF	0.9958	0.9838	1.0032	0.9961	0.9730	1.0150	0.9852