Weekly Money Market Report
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Slow and Steady Disinflation of the Inflation Balloon

Highlights

- **Central bankers across the globe are welcoming the recent moderation in inflation but cautioned the fight is far from over. Hawkish choruses continue to emanate from the Federal Reserve and the Reserve Bank of Australia (RBA).**
- **At its first meeting of the year, the Reserve Bank of Australia (RBA) lifted the cash rate by 25bps to 3.35%, the highest level since September 2012.**
- **Despite the recent return of optimism, data from the Eurozone is pointing to gloom in economic activity and consumer spending.**
- **The UK avoided a recession last year by the narrowest of margins after the cost-of-living crisis and industrial action hit the economy in December.**

United States

Hawkish Chorus Continues

A slew of Federal Reserve officials spoke this week and kept the hawkish talk up. Fed Chair Jerome Powell acknowledged that the strong job's report underscores that more work has to be done to ensure inflation hits target. While acknowledging that the disinflationary process has started in the goods sector, it is not as pronounced in the services sector and there is "a long way to go". Powell floated the idea that the 5.1% interest-rate peak forecast by officials is a soft ceiling. He is concerned that the pandemic has had a lasting legacy on the jobs market, which will be structurally tighter for longer due to the absence of potential workers. This is likely to keep inflationary pressures more elevated relative to the pre-pandemic period and argues against an early loosening of monetary policy. Jobless claims on Friday reinforced the idea of a hot labor market, with the 4-week average falling to lowest since April 2022. While inflation is expected to fall sharply through 2023, he is of the view that it will be 2024 before we "get close to 2%". He dismissed the idea of accelerating the run-down of the Fed's huge balance sheet for the time being, which could help nudge longer dated borrowing costs higher.

Following Jerome Powell's comments, more Fed officials reiterated their hawkishness. New York Fed President John Williams maintained that the Fed have more work to do to reach a "sufficiently restrictive stance", and that they will "need to maintain that for a few years to make sure we get inflation to 2%." Fed Governor Christopher Waller acknowledged that it could be a "long fight, with interest rates higher for longer than some are currently expecting." Commenting on the surprise January jobs report, Waller added "Such employment gains mean labor income will also be robust and buoy consumer spending, which could maintain upward pressure on inflation in the months ahead." Minneapolis Fed President Neel Kashkari said that January strong labor-market report shows that US central bank would need to keep raising rates to as much as 5.4%.

The US Dollar Index started the week with a rally crossing the 103 threshold at 103.621 and closed the week at 103.578.

Europe & United Kingdom

Winter Slump in Europe

Several indicators are still pointing to growing confidence after mild winter weather and sufficient gas storage facilities. February data in the Sentix Investor Confidence Index came in better than expected. In the Eurozone, the overall index rose for the fourth time in a row, improving by 9.5 points to 8 points. The increase signals that a recession is off the table, replaced with stagnation for the time being.

Despite the recent return of optimism, the sharp drop in new orders, the inventory buildup in the recent months and the lagged impact of higher energy prices all bode ill for the short-term outlook. Eurozone retail sales in December underlined the weakness in consumer demand at the end of the year amid high inflation. Retail sales dropped 2.7% month-on-month and 2.8% year-on-year.

In the region's largest economy, Germany, a terrible industrial production report confirmed the German economy's sudden and hard halt in December. German industrial production decreased by 3.1% month-on-month from a 0.4% month-on-month drop in November. For the year, industrial production was down by almost 4%. Production in energy-intensive sectors plummeted by 6.1% month-on-month and by almost 20% compared with December last year. Although factory orders grew more than anticipated in December, they are still down 10.1% year-on-year. On the bright side, German inflation slowed in January to the lowest level in five months thanks to further government aid to ease the burden on households from soaring energy costs. CPI dropped to 9.2% in January from 9.6% in December.

After almost reaching the 1.0800 level earlier last week, the euro took a turn downwards and closed the week at 1.0679.

UK Not Out of the Woods Yet

The UK avoided a recession last year by the narrowest of margins after the cost-of-living crisis and industrial action hit the economy in December. Gross domestic product was unchanged in fourth quarter following a revised 0.2% decline in the previous three months. GDP in December alone fell 0.5%. The economy nonetheless was 0.8% smaller than its size at the end of 2019, making the UK the only Group of Seven country that has yet to fully recover output lost during the pandemic. For the whole of 2022, the UK economy grew 4%, slower than the 7.6% pace recorded in 2021 when the nation was recovering from pandemic lockdowns. Chancellor of the Exchequer Jeremy Hunt welcomed the figures but noted the government needs to bear down on inflation, which reached a 41-year high last year. "Our economy is more resilient than many feared," Hunt said in a statement, "However, we are not out the woods yet, particularly when it comes to inflation."

Output in manufacturing and construction stalled in December. Overall industrial production rose 0.3% in December, entirely due to cold weather boosting utility output. The dominant services industry shrank by 0.8% in December, more than twice the pace expected. Consumer-facing services dropped 1.2% in the month. That reflected poor retail sales during the month and an escalation of strikes as hundreds of thousands of workers walked off their jobs seeking better pay.

Economic activity has stalled largely as a result of energy-led price pressures on households and businesses. The Bank of England predicted in November last year that the economy was already likely in recession. The narrow miss, which is subject to revision by the Office of National Statistics when more data becomes available, reflects an economy that is stagnating at best in the face of a squeeze on spending power.

The sterling managed to almost touch 1.2200, but failed to pass through, closing the week at 1.2062.

Asia-Pacific

Economic Ammunition as China Reopens

China's consumer inflation accelerated last month with the country reopening and the Lunar New Year holiday spurring demand. The consumer price index rose 2.1% from a year earlier in January, up from 1.8% in December. The driver was higher prices of food, which grew 6.2%, driving the overall CPI figure higher by more than a percentage point. Core inflation, which does not include volatile food and energy prices, rose to 1% — the highest since June — a sign of stronger demand in the economy. Producer prices remain in deflation, which deepened in January. The decline in PPI was more than expected, falling by 0.8% from a year earlier, largely because of softer commodity costs.

The inflation data is likely to give the People's Bank of China room to continue supporting the economy, including through interest rate cuts. In a sign that the central bank is keeping policy relatively loose, it injected some $150 billion in funds into financial markets over the past three days to ease a liquidity squeeze. Unlike some other countries, the Chinese government has the power to influence or control the price of key products including coal and power, through policies such as buying and selling from its strategic reserves.

The Chinese government released a policy outline for building a high-quality country by 2025. The outline is very broad and covers a multitude of areas including the service sector, technology, manufacturing, and social governance. It is a policy outline to grow the private sector and strengthen the government's governance ability and follows that the government should target both the growth rate (around 5%) and quality. However, the economy's overall recovery this year — that is largely expected to rely on a boost in consumption — remains uncertain. A sluggish property market, declining exports and rising geopolitical tensions are significant overhangs that have clouded the outlook.

Inflation in for a Slow Decline Down Under

At its first meeting of the year, the Reserve Bank of Australia (RBA) lifted the cash rate by 25bps to 3.35%, the highest level since September 2012. The RBA undermined any thoughts of easing later this year or early next year, mentioning that further tightening will be needed to crush stubbornly-high inflation. The statement that followed the decision RBA Governor Phillip Lowe suggested he does not expect inflation to return to the top of the 2-3% target until mid-2025. He added, "The Board expects that further increases in interest rates will be needed over the months ahead to ensure that inflation returns to target and that this period of high inflation is only temporary." Lowe's most recent statement came in a sharp contrast from December when the board discussed a possible pause in tightening and traders responded by repricing the rate outlook.

In a sign that higher borrowing costs are finally working to curb spending, Australian retail sales declined for the first time in 2022 in December. Retail sales tumbled by 3.9%, the biggest fall since August 2020. Resilient consumer spending has been a key factor in its confidence that the economy can withstand higher rates.

In comparison to international counterparts, Australia has lagged in its policy response to higher prices, having raised rates by 3.25%, compared with 4% in New Zealand and 4.5% in the United States. The RBA's slower pace reflects Governor Lowe's efforts to bring the economy in for a soft landing. Lowe acknowledged that monetary policy operates with a lag and that there is still uncertainty about the timing and extent of an expected slowdown in household spending. Working in his favor is a housing market where the pace of decline has begun to ease, cooling employment growth in the recent months, and consumer spending showing early signs of slowing. Yet inflation remains uncomfortably high, with core prices in the fourth quarter surging 6.9% — exceeding the RBA's forecast of 6.5%.

The aussie lost its momentum above 0.7000 level and closed the week lower at 0.6918.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30560.

Rates – 12th February, 2023

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.0789	1.0664	1.0798	1.0675	1.0470	1.0790	1.0736
GBP	1.2038	1.1958	1.2193	1.2058	1.1840	1.2150	1.2085
JPY	132.18	129.79	132.90	131.41	130.30	133.50	129.78
CHF	0.9258	0.9159	0.9290	0.9236	0.9140	0.9330	0.9155