Weekly Money Market Report
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Dollar Rises Amid A Hawkish Fed

Highlights

- **Fed officials expect to start raising interest rates in 2023 and are now expecting two interest rate hikes in 2023.**
- **The Fed mentioned the possibility of eventually reducing the pace of its $120bn per month asset purchase program.**
- **US PPI has gained 0.8% in May following a 0.6% increase in April.**
- **Prices of consumer goods in the UK rose 2.1% in the year to May, up from 1.5% in April and the highest level since July 2019.**
- **UK retail sales unexpectedly fell last month for the first time since January.**
- **The Bank of Japan kept its rate targets unchanged and announced that it will maintain its massive stimulus.**

United States

Suddenly Hawkish

Last Wednesday saw a shift in the stance of the Federal Reserve, who has for months been wary of signaling that an end to its ultra-loose monetary policy would be in sight. A hawkish twist saw Federal Reserve chair Jerome Powell announcing at a press conference that Fed officials expected to start raising interest rates in 2023, in addition to beginning talks on eventually reducing the pace of its $120bn per month asset purchase program.

The moment when the Fed might start winding down its support, suddenly looked to be on the horizon. The dot plot is now showing that 13 of the 18 FOMC members predicted a first interest rate increase in 2023, compared to 7 in March's dot plot. Fed officials are now expecting two interest rate hikes in 2023, a year earlier than the forecast just three months ago. Powell went on to explain the changing views during his press conference, saying "Many participants are more comfortable that the economic conditions in the committee's forward guidance will be met somewhat sooner than previously anticipated. And that would be a welcome development."

Powell tried to put some brakes on the notions of a rapidly accelerating timeline toward monetary tightening, saying that the dot plot needed to be taken with a "grain of salt". The Fed has vowed to continue buying Treasuries and agency mortgage-backed securities at the current pace of $120bn a month until it sees "substantial further progress" towards its goal of a more inclusive recovery. Only later would it increase interest rates, after certain economic milestones were met, stressing that that the Fed's monetary policy guidance is not calendar-based but dependent on economic outcomes.

Fed officials are now projecting that the US economy will grow by 7% this year, and 3.3% in 2022, with unemployment rate falling to 3.8% by the end of 2022, down from 5.8% in May. Although they do not see the economy to be overheating, they predict core inflation to jump to 3% this year, but would fall back to 2.1% in 2022 and 2023, a scenario consistent with the Fed's aim of a full recovery.

Higher Prices

The producer price index (PPI) was released on Tuesday where it illustrated a gain in prices paid by producers, which might force companies to increase prices on consumers. The PPI has gained 0.8% in May following a 0.6% increase in April. The main driver to the increase of production costs comes from increased material costs and labor expenses. Additionally, increased demand has depleted inventories combined with transport bottlenecks, which influenced the prices to increase.

Markets React

The shift in the Fed's projections jolted the government bond market, where treasuries of all maturities sold off sharply in the back of the release. The benchmark 10-year note rose 0.08% before cooling down to close the week at 1.443%. The 5-year note closed the week 0.14% up at 0.876%.The 2-year note yield, which is even more sensitive to the timing of Fed rate rises and had budged little so far this year, jumped as well, to close the week at 0.252%.

The Fed's hawkish tone saw the greenback strengthening taking the index up 2% to close the week at 92.225. The dollar's strength took its toll on the single currency, pushing the EUR/USD pair to three months lows closing at 1.1860, with the cable following suit reaching three month lows of 1.3809 against the dollar.

UK

Rising Inflation

UK's inflation saw another jump last month, overshooting economists' forecasts and the Bank of England's target, as the reopening from lockdown drove up prices. Figures released by the Office for National Statistics on Wednesday showed prices of consumer goods rose 2.1% in the year to May, up from 1.5% in April and the highest level since July 2019. The consensus expectation was 1.8%.

Central bankers have expressed confidence that such steep rises will be temporary, driven by short-term supply chain bottlenecks, rising commodity prices and suppressed demand. But some, including BoE chief economist Andy Haldane, have warned against complacency over upside inflation risks. It is worth noting that BoE governor Andrew Bailey said last month he would not hesitate to tighten monetary policy, by raising interest rates from their current 0.1%, if price rises appeared to be consistently outstripping 2%.

Retail Sales Reverse Course

Data released on Friday showed UK retail sales unexpectedly fell last month for the first time since January as consumers spent more on meals and drinks out and less on grocery shopping. The volume of retail sales fell 1.4% in May compared to the previous month, throwing economist's forecasts of a 1.6% increase into the wind.

The decline followed a jump of almost 10% in April, when non-essential shops were allowed to reopen for the first time since early January in most of the country. The largest contribution to the monthly decline in May came from food stores, where sales volumes fell 5.7%. Indoor hospitality reopened on May 17 in many parts of the UK, resulting in many people eating out rather than cooking at home. Non-food stores, in contrast, reported a 2.3% increase. Household goods stores, such as furniture, reported the fastest growth, of 9%.

A Separate report released on Tuesday showed the number of employees in the UK has risen by 197,000 since April, the sixth consecutive monthly increase. The biggest gains for May where among people working in hospitality, mainly young people living in London. The unemployment rate averaged 4.7% over the three months leading to April.

Asia

BOJ Holds Its Ground

In its monetary meeting statement on Friday, the Bank of Japan kept its rate targets unchanged and announced that it will maintain its massive stimulus to support the economy and extended a September deadline for its pandemic relief program, suggesting that Japan will lag well behind the US in ending its crisis mode policies. In a briefing following the policy decision, BoJ governor Haruhiko Kuroda said "In Japan, inflation had not reached 2% even before the pandemic. As such, we must continue with our ultra-loose monetary policy even after the pandemic subsides, in order to achieve our 2% inflation target."

The Regulator surprised markets with the unveiling of a plan to boost funding for fighting climate change, joining a growing number of central banks stepping up efforts to address its economic and financial consequences. The BOJ said it will launch the climate change scheme by the end of this year, and will release a preliminary outline of its plan at its next policy-setting meeting in July.

Kuwait

Kuwaiti Dinar

USD/KWD closed last week at 0.30110

Rates – 20 June, 2021

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.2108	1.1845	1.2148	1.1860	1.1740	1.2000	1.1882
GBP	1.4117	1.3790	1.4132	1.3809	1.3700	1.4000	1.3811
JPY	109.63	109.58	110.81	110.19	109.50	111.00	110.10
CHF	0.8984	0.8964	0.9239	0.9224	0.9100	0.9350	0.9202