Weekly Money Market Report
07 October 2018

Dollar Appreciates on Hawkish Rhetoric and Economic Fundamentals

United States

The US economy is currently booming. The unemployment rate is near its lowest level since the 1960's with expectations of dropping further in the coming months. Wage growth has accelerated to its quickest pace in nine years while GDP reported higher than 4% in the second quarter of 2018. The yield on the 10-year treasury just hit its highest level since 2011.

A fast-growing US economy traditionally brings along a fear of inflation. US Federal Reserve Chairman Jerome Powell set to calm such concerns during his speech stating that rising wages and low employment do not necessarily coincide with high inflation and would not force him to hike rates aggressively, adding such correlations have diminished in recent decades. Powell further affirmed his opinion stating that the US Central Bank is still far from its neutral state, which is the rate at which the economy is neither stimulated nor restrained. Powell's hawkish approach bolstered expectations of further rate hikes while the markets witnessed a strong dollar across the board following the statements. The markets implied probability for a fourth rate hike in December is around 80%. The US dollar index gained nearly 1.19% over the past 15 days.

Looking at equities, high yields on US treasury bonds continue to weigh heavily on global equity markets. The yield on 10-year treasury notes hit 3.23% on Thursday, reporting its highest yield since 2011. Stocks fell across the board with the Stoxx Europe 600 Index losing 1.1%, the MSCI Emerging Market Index tumbling 2.5%, and the MSCI Asia Pacific Index dropping 1% to its lowest level in 3 weeks. US stocks fell the most since June as volatility spiked following allegations of China's infiltration with American companies. The S&P dropped to a 3 week low while technology shares suffered the greatest as the Nasdaq 100 Index reported its worst day since June, sliding 2.1%.

Manufacturing & Non-Manufacturing PMI

Looking at US economic fundamentals, US manufacturing eased in September, though still reported a growing trend. The Institute for Supply Management reported activity at 59.8, down 1.5 points from Augusts' 61.3 level that was the highest reported since May 2004. September's figure represents the 25th straight month of the sector reporting levels of expansion.

Non-manufacturing PMI rose to a record high since the index was created in 2008. The PMI rose to 61.6 in September, up from August's 58.5 level and beating market expectations of 58. While the levels appear positive for the economy, such growth can possibly be attributed to companies preparing for the Trump administration's tariffs and retaliatory tariffs in return. Companies have already complained of disruption from tariffs as exports decreased to their slowest level in 10 months. Regardless, data emerged strong and further supported the US dollar.

NAFTA dispute comes to an end

The trilateral pact between the US, Canada, and Mexico known as NAFTA, has been renamed by President Trump as the "United States Mexico Canada Agreement", or USMCA. Following months of uncertainty, the US and Canada have reached an agreement just hours before the deadline, tackling issues related to the dairy sector, dispute settlement mechanisms, car tariffs, and cultural provisions. All three parties will sign the revamped agreement on November 30. However, the vote would not occur until 2019 when a new US congress will form, possibly complicating the deal's prospects if the Democratic Party were to win control of the House of Representatives.

After re-writing the 24-year old NAFTA agreement, president Trump shifted his attention to the European Union. The US has already levied tariffs on imports of EU steel and aluminum while Brussels retailed with tariffs on $3.2 billion worth of US goods. Though the US and EU had agreed to halt negotiations back in July, president Trump has again threated to slap tariffs on the EU's car exports.

A Tightening US Labor Market

Adding to the strong economic data trend for the US, the unemployment rate fell to its lowest level since 1969 for the month of September. The Bureau of Labor Statistics also reported on Friday that non-farm payrolls rose by 134,000, significantly below the 185,000 expectations. However, August's upward revision to the previous month eased concerns as employers added 270,000 jobs. July's figures also revised up to 165,000 from 147,000.

The unemployment rate came in better than expected at 3.7%, below expectations of 3.8%. Average hourly earnings rose in line with expectations by 2.8%. Overall, this week's figures boosted optimism about the US economy's health and are in line with the Fed's expectations of ongoing economic expansion.

UK & Europe

Political Turmoil in Italy

The Euro experienced a volatile week as political turmoil began with the Italian populist coalition government announcing their preparation of a new controversial budget proposal. The running coalition has planned to run a deficit of 2.4% of GDP next year, which more than triples the previous government's target, and 2.2% in 2020. The announcement shook markets as the Euro fell, losing 1% throughout the week. Currently, the Euro is trading around 1.1523.

Brexit nearing its final stage with no major resolutions

Prime Minister Theresa May failed to provide any news of advancement on Brexit negotiations during the Tory Party Conference speech. Though she pledged to accept no deal rather than a bad one, the Sterling barely moved in response. What may also have added to the Sterling's resilience are comments made by the UK Brexit negotiator Dominic Raab, as he confidently stated that they will be able to submit a deal by November.

Nonetheless, the final Brexit outcome remains highly uncertain as Ms. May sticks to her Chequers deal plan, which may solve the Irish border issue. However, it relies on the UK staying within the single market for goods and has grown to be unpopular even among her party. A harder break has been called for which would see the UK leaving the single market, free to negotiate a free trade deal with the EU and the rest of the world. Looking forward, EU leaders are set to meet at the European Council in Brussels on October 18-19.

UK Manufacturing

The Manufacturing sector activity in the UK economy unexpectedly saw an upturn in September, beating expectations of a drop to 52.5 and instead rising to 53.8 following an upwardly revised figure of 53 in August. Output and new order growth both accelerated, while business optimism improved as over 53% of companies expect production to increase over the next year. Looking at the broader picture however, the manufacturing sector has contracted significantly compared to a strong performance of growth in 2017, mainly due to the effect of Brexit uncertainty. Still, the sterling remained the most resilient currency against the strengthening US dollar.

Asia

China's hacking scandal

The world's two largest economies are at a face-off after news of China hacking US companies dragged investor sentiment. The MSCI AC Asia Pacific Infotech Index hit its lowest level since July 2017 after a Bloomberg News article was released on Friday. The article claimed that Beijing had hacked American computer networks using a microchip built by its spies. US investigators found that China's People's Liberation Army had inserted the chips during manufacturing. China's computer maker at the center of the allegations Lenovo Group Ltd dropped 23%, reporting its biggest loss in almost a decade. Paired with a months-long tariff dispute, the latest developments raise the question of China's place in the supply chain to the US consumer.

Japan's Household Consumption

Japan's household spending and base pay rose in August to their highest levels in years. Household spending recorded its biggest jump in 3 years, rising 2.8% in August. Base pay also saw its biggest rise since 1997, climbing 1.4% over the year. Consumer spending is seen as key to the self-sustaining recovery attempted by the BOJ as bigger pay raises this year are expected to help households face challenges such as higher oil prices and a further decline in the yen. The dollar was higher against the yen for the fourth consecutive week and the pair was last trading at 113.74.

Commodities

As for the commodities complex, oil prices tumbled 3% on Thursday on the prospect of increased production from Saudi Arabia and Russia. Recently, oil prices had gone up to four-year highs as US sanctions on Iran and supply losses from Venezuela contributed to the high priced market. In an attempt to counteract soaring prices, Saudi Energy Minister Khalid al-Falih announced on Thursday that the Organization of the Petroleum Exporting Countries was able to raise output by 1.3 million barrels per day.
The kingdom also plans to invest $20 billion to expand its spare oil production capacity.

Markets now brace for US sanctions on Iran's oil exports that will take effect on November 4. The main concern is that less supply will affect Asian buyers who are usually reliant on Iranian imports. Adding to the markets pressure, a strengthening dollar makes dollar-denominated oil more expensive for buyers with other currencies. Brent crude fell 1.02% to $84.16 a barrel this past week, while US West Texas Intermediate faced a 1.06% loss, settling at $74.33 a barrel.

Kuwait

Kuwaiti Dinar

USD/KWD opened at 0.30335 on Sunday morning.

Rates – 7th October, 2018

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.1603	1.1462	1.1623	1.1523	1.1325	1.1730	1.1617
GBP	1.3030	1.2919	1.3124	1.3122	1.2920	1.3320	1.3187
JPY	113.74	113.50	114.54	113.71	111.70	115.70	112.89
CHF	0.9811	0.9805	0.9955	0.9916	0.9725	1.0125	0.9831