NBK MONEY MARKETS REPORT

Dollar remains subdued despite passage of tax overhaul bill

Britain's economy forecast to slow down

KUWAIT: The US tax reform has been signed into law by President Donald Trump and the majority of alterations in the bill will take effect as of January the first 2018. The interesting issue is that the largest tax reform in US history in terms of size wasn't a market mover. It was evident that the tax factor was already priced in over the course of the year. Lately, the market's tone toward the benefits of the tax cut has been subdued, as they expect the positive effects to be overshadowed by higher interest rates stemming from the enhanced government deficits. The tax reform will cost roughly $1.5 trillion over the next 10 years. The US central bank predicts a "modest lift" to economic growth from the tax modification and that's why the FED increased the growth forecast to 2.5 percent for 2018 from 2.2 percent, afterwards they expect growth to slip back closer to its recent 2 percent average.

In Catalonia, the pro-independence parties won the regional election and retained their majority in the parliament. The separatists' parties won 70 of the 135 seats, while the pro-Spain parties won 57 seats. The results of the election may cause tensions to re-emerge between Madrid and the pro-independence faction eager to exploit the tactical advantage of a favorable election outcome. The overall impact of the vote on the single currency was minimal and Catalonia may find it difficult to develop into an independent state if no other country recognizes its sovereignty. It won't even be able to have its own currency under such circumstances. The EU mostly likely won't support a pro-independent state, especially during ongoing negotiations with the UK. The pro-separatist parties are somewhat divided and the previous independence declaration created tensions between the parties over policy direction.

On the currency front, the dollar index was pressured downwards at the start of the week as markets awaited the outcome of the vote from Congress. The downward direction persisted as the euro's strength took its toll on the greenback and final US GDP reading came in lower than expected. Despite positive news from the tax reform and higher US yields the DXY failed to gain support. The Dollar was the second weakest major currency last week after the Japanese yen and lost 0.55 percent of its value.

As for the single currency, the euro took advantage of the dollar's weakness last Monday and received a boost after inflation moved in the right direction.

The EUR/USD gained momentum throughout the week, until the election results from Catalonia came out. The pair opened the week at 1.1751 and closed on Friday 1.1857. The pound sterling's direction last week was influenced by the majors as it was a light week in terms of economic data. The sterling appreciated sharply at the first day of the week before entering into a consolidative tone, which persisted until Friday.

The safe haven yen was the worst performing major currency last week, pressured by powerful rally in treasury US yields.

The dollar hit a nine-day high against the yen on Thursday, after comments by Governor Haruhiko Kuroda reinforced expectations that the BOJ was in no hurry to move away from its ultra-loose monetary policy. The dollar was supported against the yen after the 10-year yield jumped to a nine-month high as investors worried the tax refurbishment could lead to higher US debt. The US dollar gained 0.53 percent over the yen throughout the week.

In the commodities complex, the price of oil edged higher on Monday, supported by a North Sea pipeline outage and a Nigerian oil worker strike. Moreover, the upward trend continued after US crude oil inventories declined by 5.222 million barrels last week, according to data from the American Petroleum Institute, compared to an expected draw of 3.518 million barrels. Brent crude oil closed the on Friday at $64.95.

US gross domestic product

The final value of all goods and services produced in the third quarter edged lower to 3.2 percent annually, from an earlier estimate of 3.3 percent.

The slight downward movement is attributed to weaker trade and consumer spending. Personal consumption, which makes the biggest contribution to the economy's growth, was revised down to a 2.2 percent from 2.3 percent. Although, this doesn't change the fact that it was the first time since 2014 that the economy enjoyed growth of 3 percent or more for two consecutive quarters. The Federal Reserve lately enlarged its calculation for growth next year to 2.5 percent from 2.2 percent in expectation of a tax change.

Economic figures ranging from the labor market to the housing sector as well as other reports, suggested the economy maintained its solid momentum into the fourth quarter. Looking forward, markets expect a modest boost for the next two years due to changes in the tax model and a pickup in the global economy. In spite of the latest tax amendment, several economists predict a moderate boost to the economy as tax cuts for individuals is skewed towards higher-income households. Several economists believe the lower tax regime will lead to share buybacks and debt repayment rather than a boost in business investment.

Housing sector

Last month's gains in new home constructions are inspiring, as they are motivated by single-family home building, which tends to increase economic activity and jobs in a bigger way than apartment construction. Single-family licenses have risen for three consecutive months, suggesting a sustained pipeline of work for developers. The recent data increases the probability that residential construction spending, which negatively impacted Q2 and Q3, will add to the pace of growth in the last quarter of 2017. In details, housing starts rose 3.3 percent to an annualized rate of 1.3 million from 1.29 million seen in October. The latest rate indicates the data is the highest level since October 2016.

Looking at building permits, an indicator of future construction, dipped 1.4 percent to a rate of 1.298 million. The decline is attributed to a fall of 6.4 percent in permits for the construction of multi-family homes. In conclusion, confidence among home builders is at 18 years high, with relatively low mortgage rates. The average rate on 30-year fixed US mortgages is lower by 0.23 percent than a year earlier. The figures reflect a boost from rebuilding and recovery efforts following hurricanes Harvey and Irma after areas in the South had faced the brunt of the damage from flooding and winds.

Euro's strength takes its toll on the greenback

Europe & UK

Morale in German businesses drifted lower this month, over the shape of the new government as Chancellor Angela Merkel struggles to form a firm government. Merkel's party lost supporters to the far right in September's election and her attempt to form a three-way alliance failed last month. After recording an all-time high in November, Ifo business climate index contracted 0.4 points to 117.2, pressured by attitudes toward business prospects over the next six months. Despite the drop in the German Ifo Business Confidence, the present conditions index improved to 125.4 from 124.5 last month. Overall, the Ifo climate index remains near record highs, while growth projection by the government and Bundesbank have been upgraded.

Inflation edges up in Europe

Consumer inflation in the eurozone slightly increased 0.1 percent in November to 1.5 percent y/y, while the core rate remained stagnant at 0.9 percent. The main contributor that supported the rise in headline inflation was oil prices. German inflation rose back to September's level of 1.8 percent annually, having dropped to 1.5 percent in October. The highest annual rates were recorded in Estonia (4.5 percent), Lithuania (4.2 percent) and the United Kingdom (3.1 percent).

The European Central Bank expects consumer price growth to dip before slowly picking up again and to float around the 1.5 percent level until 2020, when it rises to 1.7 percent. The Bank enhanced its growth prospect for 2018 from 1.8 percent to 2.3 percent. Overall, economic indicators are at multi-year highs suggesting the robust momentum will likely continue.

UK's economy

The final calculation of Q3 growth in the United Kingdom revealed that British consumers financed their expenditures by saving less. The saving ratio fell to 5.2 percent from 5.7 percent seen in the second quarter mainly due to consumer prices exceeding wage growth. Households have now been net borrowers for four successive quarters for the first time since records began in 1987.

In details, the economy grew 0.4 percent in Q3, taking the annual rate up to 1.7 percent from an earlier estimate of 1.5 percent. But despite being revised higher, that's still the lowest annual growth in over 4 years. In regards to the IMF, they predict the economy to slow down further next year to 1.5 percent.

The Recruitment and Employment Confederation claimed that fewer UK employers plan to hire extra staff next year on the back of a gloomy outlook. The REC survey revealed the net balance of companies planning to add permanent staff in the next 12 months fell to 16 percent in November from 24 percent a year ago. No companies in the survey said they expect the British economy to improve in 2018.

Asia: No exit in sight

In his last monetary meeting of the year, BoJ Governor Kuroda poured cold water on speculation that the central bank is gunning up to tighten its monetary stance. The Governor claimed "just because I brought up this academic analysis, reversal rate, doesn't mean at all that we need to review or change the yield curve control we've adopted since September last year. The Japanese economy is in great shape in terms of growth, job creation and price expansion is at least moving in the right direction.

The BoJ's tone lately indicates confidence in the strength of the economic recovery as the economy expanded at an annualized 2.5 percent in Q3 2017, to mark a seventh straight quarter of growth. Inflation is still far away from the 2 percent level and there isn't much pressure on Kuroda to elevate rates by the government after he has been called to parliament only 19 days this year. That's down from 51 days last year and is the fewest for any BOJ governor since 2007. The overall data supports the case that the central bank will maintain its negative interest rate model until price growth lands towards the 2 percent target.

In details, the BOJ hasn't amended its monetary policy since September 2016, when it employed its yield-curve control program, setting an interest rate of -0.1 percent on some bank reserves and a target of around 0 percent for 10-year government bond yields.

RBA's monetary policy

The Reserve Bank of Australia's meeting report was released last week after maintaining its cash rate at 1.5 percent on December the 5th. The RBA has restrained itself from tightening monetary policy for the last seven years. As for the labor market, the environment remained positive as overall growth in employment has increased slightly and full-time employment is growing at its fastest pace in a decade. The unemployment is currently at 5.4 percent, the lowest since 2013.

The RBA cautioned that the outlook for household consumption continued to be a significant risk due to a modest rise in wages, while household debt levels were extremely high. Household consumption rose 0.1 percent in the three months through September, its weakest pace in five years. The Board judged that retaining the stance of monetary policy at this meeting would be consistent with sustainable growth in the economy and achieving the inflation target over time. In regards to expectations, interbank futures and financial market prices indicate that the cash rate is expected to remain unchanged for the time being.

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The USDKWD opened at 0.30190 yesterday morning.

'Virtual gold' may glitter, but mining it can be really dirty

LONDON: This file photo shows gold plated souvenir Bitcoins arranged for a photograph in London. — AFP

PARIS: As the poster child for the growing ranks of computer-generated currencies, bitcoin's recent stratospheric price rises have propelled it from the chat forum-hosted depths of nerddom into the global consciousness. As it rose from under $1,000 to over $19,500 at one point this year, hordes of tech-savvy punters have rushed in to buy, while any investors can now do the same on the US futures markets.

Bitcoin has been called virtual gold, in part because it is created in a process that insiders call mining. And like real mining, it can be dirty. That's because joining the online gold rush to mine the coins that are streams of computer code requires high-powered rigs that consume considerable amounts of electricity to do the virtual equivalent of blasting through rock by solving a string of highly complex computer algorithms. Depending on how the electricity used for mining is generated, the virtual currency can have a very real impact by adding pollutants into the air and contributing to global warming.

Out of the bedroom

What barely five years ago was a hobby for "bedroom miners" has mushroomed into a massive, but unregulated, industry that some observers fear is a bubble waiting to explode, potentially causing damage similar to the subprime mortgages fiasco that caused the global economic crisis a decade ago.

Mining involves "adding value by dedicating computational resources to verify transactions in a huge public ledger called a 'blockchain'," explained Julian Oliver, a New Zealander who uses wind power to mine ZCash-a bitcoin cousin. The miners are thus providing the computer resources for their currency's trading system to operate.

But the number-crunching to pocket coins requires ever more powerful hardware and the means to keep them running, Oliver told AFP. "At current bitcoin prices things are looking good for miners," he said. "But it's a huge use of energy, whatever the profit margins (and is) not remotely sustainable."

Specialist studies estimate the total annual energy output of the hundreds of thousands of dedicated mining machines worldwide at 35 terawatt hours, according to the Digiconomist website-some 25 percent up on last year. That puts it on the level of energy consumption of Denmark.

Each transaction consumes roughly 100 kWh-the equivalent of running a lightbulb for three months. By contrast, a credit card transaction uses about 0.2 kWh. But focusing on the electricity consumption of cryptocurrency mining "ought not to overshadow pre-existing environmental costs of the traditional financial system," said Oliver, as "cash needs to be printed and transported and banks run off the back of data centres."

Cleaning up

Nadine Damblon, chief executive of HydroMiner, which uses hydroelectric power to mine in the Austrian Alps, said there is a need for greater use of renewables in the industry as Asian miners often rely on coal-generated electricity. Hydroelectric can play a leading role as "one of the most environmentally friendly ways to generate power," she said. Damblon believes the market will help solve the problem. "I think in the case of bitcoin mining the capital will flow into more efficient hardware that will need less energy," said Damblon. The scale of the long-term environmental threat that mining poses is unclear, as is the degree to which it could act as a catalyst for greater take-up of renewables.In its Global Cryptocurrency Benchmarking Study, the Cambridge Centre of Alternative Finance found that nearly three-quarters of all major mining zones are in China and the United States. But the likes of Iceland and Austria are gaining ground. Not only do they offer clean hydroelectric power, but also cold temperatures that help save on cooling computer equipment, which can account for up to a third of energy needs.

What is undeniable, said the report, is that "the mining sector has evolved in a short time from a hobby activity performed on personal computers into a professional and capital-intensive industry with its own value chain."

As for how many bitcoin mines or miners there are now, nobody really knows.

Green vs anarchist

In terms of large-scale mines "there are perhaps about a hundred," said French information technology specialist Marc Bevand. "Maybe (there are) a few thousand smaller ones" using "one or two racks" of machines rather than the tens of thousands in the largest Asian mines, San Francisco-based Bevand told AFP.

The push for scale to save on energy costs and go green also risks pushing bitcoin against its libertarian, or even anarchist, founding philosophy. Bitcoin was created to not only allow secure and anonymous transactions, but for the system to be controlled by users and not by a government or corporation.

The push for scale "would concentrate number-crunching power in the hands of the richest or throw into question bitcoin's (decentralised) philosophy," said Teunis Brosens, a senior economist with ING bank. He forecasts that eventually "banks will create private blockchains which will not face the problems of scale or regulation" which bitcoin is coming up against. — AFP

Poland in the EU: Challenging times for a dream come true

WARSAW: Poland's entry into the European Union in 2004 was a dream come true just 15 years after it shed communism, but today its rightwing government is posing an unprecedented challenge to the authority of Brussels in enforcing democratic standards, including the rule of law. Poles are overwhelmingly EU-enthusiastic, with nearly 90 percent backing membership of the bloc that has given the country billions of euros in subsidies, turbo-charging its economic development.

But tensions came to a head this week as the EU launched unprecedented disciplinary proceedings over Warsaw's judicial reforms, which Brussels insists threaten democracy by putting the courts under government control. Warsaw insists the reforms are necessary to root out the last vestiges of communism from the justice system. But Brussels contends that 13 laws adopted by Poland in the space of two years have created a situation where the government "can systematically politically interfere with the composition, powers, the administration and the functioning" of judicial authorities.

The EU's censure could ultimately lead to Poland losing its voting rights in the bloc. Poland dismissed the EU's decision as being "political" while its president, Andrzej Duda, defiantly signed into law two hotly contested judicial reforms just hours after the censure process was launched. He also accused Brussels of lies and hypocrisy for pushing ahead with the disciplinary action.

Clashing ideologies

While agreeing to dialogue with the European Commission, Warsaw has also made it clear that it has no intention of budging on its reforms. Its boldness is likely rooted in the backing it enjoys from fellow EU rebel Hungary.

Budapest has promised to torpedo any possible sanctions against Poland, which require the unanimous agreement of all other EU members.

Warsaw-based political scientist Kazimierz Kik believes the current conflict is rooted in ideological differences between Poland's rightwing populist and nationalist Law and Justice (PiS) party government and the liberal elites that dominate the EU. Poland "is not in conflict with the European Union, but with its neo-liberal elites, Christian Democrats and Social Democrats, who comprise the majority in the European Parliament and the Commission," Kik, who identifies himself as a leftist PiS supporter, told AFP. For him, Poland's clash with Brussels also reflects the tensions between the PiS administration and its political arch-rival the liberal Civic Platform opposition, whose former leader Donald Tusk became EU president in 2014 after serving eight years as the Polish prime minister.

Social gaps

By developing Poland's social welfare system-including a new child allowance and introducing a lower retirement age-the PiS has cast itself as the party working in the interest of poorer Poles, Kik told AFP. PiS voters feel they did not benefit enough from the transition to democracy and the market economy or EU entry. The popular discontent in Poland is part of a larger European and global trend says Kik, pointing to similar socio-economic factors that led to last year's pro-Brexit vote in Britain and the presidential victory of Donald Trump in the United States. The conservative and nationalist views of the PiS government and its supporters on issues ranging from refugees to abortion, are diametrically opposed to those held by liberal elites in western parts of the EU.

According to left-leaning Polish sociologist Slawomir Sierakowski, powerful PiS party leader Jaroslaw Kaczynski "is not hostile towards the EU, but he feels it is getting in the way of the political vision he wants to implement in Poland." Sierakowski also believes the conflict between Warsaw and Brussels is rooted in the conservative mentality of Catholic Poles and the lack of democratic traditions in Poland.

Its turbulent history of foreign domination and war "wasn't an ideal context for the birth of a liberal democracy," Sierakowski said.

Poles are also very attached to the idea of national sovereignty and reject the notion of "Brussels replacing Moscow" in calling the shots for Warsaw, he adds. According to Igor Janke, head of the Warsaw-based Freedom Institute conservative think-tank, the timing of President Duda's signing of the two PiS judicial reforms into law straight after the EU launched its disciplinary action was intended to "demonstrate that there is no turning back". But Janke says PiS leaders do hope to restore normal ties with the European Commission. He quotes a recent policy speech by new PiS Prime Minister Mateusz Morawiecki, a capable ex-banker seen as someone who can mend ties with Brussels. "Dear Europe, the Polish piece fits perfectly in the European puzzle but it should not be placed the wrong way or shoved in by force," Morawiecki told parliament ahead of a confidence vote that he won last week. — AFP