Tigress Financial Partners

Macro Snapshot – Chief Economist Jean Ergas

January 12, 2016

Update January 12th 2016

Political risk is once again front page, with terrorist bombing in Istanbul. This is being dismissed by the markets, which are instead focusing on a "truce" in the Chinese saga and oil collapse.

We have our doubts as to the "firepower" of Chinese reserves and continue to see "transition" as a code word for slowing! Our position on oil and commodities remains unchanged and we expect further jolts on both fronts.

Stock markets putting in a bounce

Stock markets are putting in a bounce this morning, with China easing up on the currency devaluation strategy. We continue to see this as a lull rather than a change of course.

Not clear as to metrics used for evaluating success of transition

Whether the Chinese economy is transitioning or what the metrics are to assess the progress of the "sea change" are remains unclear. What is clear is that the Chinese economy is slowing and that this is continuing to cause havoc across all asset classes and currencies.

Cash burn rate of Chinese reserves continues

We continue to see as a critical issue the "weight of money" argument as referred to the size of China's reserves. Reserves have fallen from a peak of close to US Dollars 4 trillion to US Dollars 3.3 trillion in approximately 18 months.

China has burnt through in 18 months equivalent of Saudi FX reserves!

We estimate effective, liquid reserves as about ½ this amount, raising doubts – given the cash burn rate - as to China's ability to keep "raising" its opponents in currency poker. China has spent the equivalent of Saudi Arabian reserves to scant avail.

We consider that the major action on the Chinese currency reserve front is behind us and that investors should reconcile themselves to further bouts of volatility.

We are also seeing intervention to close the gap between the on-shore and the off-shore currency – to discourage speculation. This flies in the face of allowing market mechanisms greater leeway.

Einstein used to justify cheering WTI at 31.50!

With regard to the oil price, we are reminded of the maxim that "everything is relative". WTI is rapidly continuing its descent to the Marianna's trench, at the level previously considered unthinkable of US Dollars 31.50.

See crude moving lower

Markets are recovering because earlier it was even lower! Oil has not in our view completed its descent – fundamentals remain weak, with supply strong on the dual OPEC and non- OPEC front. We expect WTI to trade below US Dollars 30.

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Commodities plumbing new depths

Commodities are continuing to fall, with copper plumbing new lows. Following yesterday's previous sharp falls in some mining stocks, we are seeing a - in our view – temporary respite. We continue to be very cautious on the sector.

No major new buyer

It was buoyed by a one in a hundred years development boost, lifting demand for a wide array of non-oil commodities. The step function shift is now exhausted and there is no buyer out there of China's caliber.

Looking at recovery in Europe?

We are looking at a recovery in the European stock markets. Investors appear to be basing their investment decisions not on growth but on "absolute" value considerations. For the sake of historical comparisons - the French CAC index is barely higher than it was at the end of 1998 and the UK is not far behind.

It is often said that Brazil is the country of tomorrow and always will be – we may well paraphrase this with regard to Europe – Market of tomorrow and always will be!

While we do not exclude a bounce in Europe – we still see a massive amount of structural reform necessary to successfully contest the new competitive environment.

Italy steaming ahead

Somewhat ironically, Italy's center left government appears to be doing a "Nixon's trip to China" move, pushing through some key reforms.

With a fall of 10 per cent in GDP and 25 per cent in industrial production since 2007, one might well argue TINA – there is not alternative. Still, one must give credit where credit is due!

Some labor statistics out today in US

Last but not least, we shall be seeing US labor market statistics today regarding openings and the QUITS rate. We continue to be somewhat skeptical of US labor market "brute" numbers. Jobs creation continues to center on relatively low paid and variable compensation positions, which shall hamper sustainable and broad based increases in purchasing power.

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He is an Adjunct Assistant Professor at New York University's School of Professional Studies and an Adjunct Faculty member at Manhattanville College. In 2014 he received the award for teaching excellence from NYU School of Professional Studies.

He is fluent in English, French, German, Italian, Spanish and Portuguese. He also has a certificate in Arabic – from NYU School of Professional Studies.

His career has spanned the complete range of macro risk analysis - energy / commodities with ENI - Global Fortune 500 17 - leading global natural resources group, capital markets with Swiss Bank Corporation (now UBS) and insurance / reinsurance with the A.M.Best Company. Jean contributes regularly to international media commenting on key macro-economic issues.

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