Macro Snapshot – Chief Economist Jean Ergas

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Update January 26th 2016

Markets are continuing to trade on oil and with the black gold steadying around the stratospheric US Dollar 30 level, we are starting to see some modest sign of life in the US futures. US markets, while primarily macro-driven, are hoping for a positive signal from Apple.

While this would be a tonic for the S+P 500 and possibly indicates some resilience in China, it shall not be the all clear for global growth. Investors remain concerned about the pace of expansion and we are increasingly seeing downgrades to oil price forecasts based on a fall in demand.

Younger generation in market has not seen a commodity bust!

We expect the markets to continue to be guided by oil and commodities and suspect that the surprises are not over. Markets are now dominated by people not old enough to remember commodity cycles. Commodities do not decline but exhaust themselves after a dizzying run and crash!

European markets are attempting to claw back some ground

European markets are attempting to claw back some ground following yesterday's fall and another collapse overnight in China. We are however seeing continued pressure on China linked stocks – such as the car-makers and the luxury good companies.

We reiterate our view that the first wave of creation of the middle class in China has happened. This is comparable to Europe in the 1950's and 1960's and that the next leg up shall not be as quick.

Stream of money exiting China now a torrent!

The stream of money exiting China has turned into a torrent as investors both seek more profitable outlets for their funds and do not wish to suffer FX losses. We expect that faced with the choice between burning further reserves, which are near the US Dollar 3 trillion level and are not all liquid, and letting the market adjust the rate, the Chinese central bank shall opt for the latter.

Markets are not sufficiently discounting the risk of a further "step function" adjustment in the FX rate.

ECB head cautious on inflation and growth outlook

Turning to the Euro Zone, the head of the ECB's comments yesterday once again reflected a cautious outlook on the Euro Zone. The inflation outlook remains muted and we see little reason to expect it to change – with oil prices hovering at recent lows and little being done to stem imported goods deflation, the outlook is not stellar.

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Euro Zone bond investors pricing in deflation – is this a re-run of the 1930's?

*The moderate price outlook is reflected in the record low
yields across a range of maturities for German government debt.
Investors are both worried as to global growth prospects and also as to the deflation in the single currency area.*

The growth outlook remains brittle, with prolonged weakness in the EM sphere having a disproportionate impact. We expect growth forecasts for the single currency zone to be revised downwards.

We shall see several internal "Brexits" in the EU

As concerns, the EU, we are seeing more fault lines appear. Italy's confrontational stance regarding German leadership will not facilitate resolution of the migrant crisis. Regardless of "Brexit", we see each major EU country attempting to renegotiate its position within the union.

Crisis is about the movement of people – not about the movement of capital

The EU is now at a turning point which transcends discussions on tariffs and movement of goods. The issue is now the movement of people, with some countries refusing to subscribe to a quota. A solution prior to the summer is key. With the warmer weather the sight of processions not seen since the medieval crusades shall turn into a torrent.

It is widely believed that the migrant issue – following the terrorist attacks and attacks against women in Germany – is now the key issue in the British referendum on the EU.

Are bank stocks telling us something?

With regard to the US, we are seeing the whittling away of the financial stocks, with Citigroup and Bank of America retracing a lot of the ground gained since the peak of the financial crisis. Can we see bank weakness as an advance signal for a recession?

What about the US economy?

*Bank stocks are falling – says the narrative-because the Federal Reserve shall stave off raising interest rates given the:
Once again volatile global financial markets
Concerns as to the real strength of the US economy
We shall hopefully be better informed this week, following the Federal Reserve meeting and the publication of the first estimate of fourth quarter GDP.*

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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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