



February 16th 2016

Europe not impressed by oil discussions with the oil price slipping and renewed concerns on global growth. Global economy shall continue to navigate perilous waters with political risk increasing. The European banking sector is again under pressure – no change in fundamentals.

Action today

Europe thumbs down on oil discussions

European stock markets are voting thumbs down on the major non-event of the day, the decision to freeze but not cut oil production by Saudi Arabia, Russia, Venezuela and Qatar. Markets were expecting a reduction but we see no reason why Saudi Arabia would be willing to subsidize its adversary Iran – Saudi Arabia who calls the shots is focused on not losing market share while practicing elimination pricing to squeeze out the recalcitrant.

Growth concerns once again prominent

The impact of the disappointment is seeping through to the European stock markets with growth concerns once again prominent. We are seeing the macro-sensitive banking sector down as investors realize that there have been no changes in fundamentals. The global economy is once again seen in the thrall of central bank policy, with the more optimistic looking to the ECB meeting in March.

German investor confidence has disappointed. We are not surprised and remain skeptical that deflation can deliver long term sustainable purchasing gains.

Winning by default is not good enough!

With regard to the US, we shall be seeing the Empire State manufacturing data. Investors are looking – if not to strength – to resilience in manufacturing. The manufacturing sector with its strong export component has been buffeted by the chill winds of slowing global growth and a stronger US Dollar. In the meantime, US consumers while spending are not going overboard.

We see the US economy as likely to disappoint – winning by default is not good enough!

The broader picture

We leave behind us another turbulent week – markets are not moving on fundamentals

We are leaving behind us a turbulent week, with investors at the start of the week fleeing in panic and at the end taking their courage in both hands. This reversal has been triggered – in our view – by factors which do not reflect a change in economic fundamentals but by rumors and assurances.

Our base case scenario remains continuing volatility – markets and governments enter into an “unholy alliance”

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Our base case scenario centers on a continuation of volatility, with market sentiment still fragile. The global economy and markets now seem to have entered into an “unholy alliance” which we wanted to see best forgotten. Markets are not driven by positive news but the expectation of central bank and sovereign intervention.

Global economy navigating in uncertain waters – desperately seeking growth prospects

The global economy continues to navigate in uncertain waters, with little prospects for growth. This has been reflected in disappointing corporate results, leading to a sizeable repricing in asset markets. The usually optimistic Federal Reserve has also been forced to recognize the “gathering storm” and the need to consider foreign affairs in their decisions.

Are we at the turning point? Who is afraid – not of Virginia Woolf – but of systemic risk?

Are we at the turning point? We leave behind us another tumultuous week as markets globally lurched. To the “usual suspects” of slowing growth, falling oil prices and monetary policy was added the grim specter of systemic risk.

Transmission mechanism of “The Last Days of Humanity” – rumors as to Deutsche Bank – arch stone of the German economy!

Transmission mechanism was the mooted inability of a leading global banking institution to pay interest on non-senior debt. Markets switched from growth estimates and earnings to fright mode. We have now been informed by a leading rating agency that Deutsche Bank shall be able to make the payments! Be grateful for small mercies!

Markets took courage in both hands at the end of last week – Deutsche Bank shows the money!

Where are we now? Markets put in a bounce on February 12th, boosted by Deutsche Bank’s plan to buy back approximately US Dollars 5 billion of bonds. Sentiment was further abetted by a rise in the oil price and – in the US – signs that the consumer was still breathing.

Deutsche Bank financial “macho act” not the beginning of a Golden Age

Bank stocks have interrupted the recovery started last week, with the focus on their “oversold” status. We do not see the Deutsche Bank announcement as “The End of History” and the beginning of a golden age. European banks are still laden with bad loans- growth is minimal and deflationary pressures stronger than ever.

Oil price – will it erupt? Iran confounds the skeptics

With regard to the oil price – we are not of the view that “one twitter message the spring makes”. The balance is still firmly tilted towards “pumping for cash”. Iran has started shipments to France and shall lose no time in further increasing supply, with shipments to other European countries scheduled.

Debate over recession continues to rage – is this relevant? Can we speak of cyclical phases in a zero interest rate environment?

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Last but not least, we are seeing the debate over the chances of a recession once again in full swing. We reiterate our view that global growth forecasts shall continue to be revised downwards. This shall create further headwinds for global companies struggling to raise prices and boost revenues.

The key issue is not the recession. It is the grim failure of economic policy which after 8 years has still not succeeded in restoring a semblance of self-sustaining growth to the developed economies.

An encouraging word from the ECB!

With the closure of the US markets on February 15th, some cheer from the Euro Zone! The head of the ECB has confirmed in a speech to the European Parliament that the central bank of the single currency area shall “act” in the event that financial turmoil should threaten price stability, an intensification of deflationary pressures.

ECB facing multiple challenges- we see deflationary pressures as entrenched

These pressures would presumably be triggered by:

A further spate of competitive devaluations

Oil remaining at these depressed prices

An equity collapse crushing any residual “wealth effect” and constraining investment and consumption;

Judging by the equity market’s reaction – these events are seen as likely, a grim omen!

Chinese central bank speaks!

The head of the Chinese central bank has given assurances that there is no immediate prospect and no need for any further depreciation of the Chinese currency.

Chinese declarations seen as reducing risk of immediate re-run of 1930’s!

This momentarily reduces the risk of further tremors with regard to currency markets – competitive devaluations and further loss of competitiveness for developed economy companies. However, this reasoning leaves out that currency “management” is but one of the arrows which the Chinese economy can deploy.

The subsidization of loss making state companies shall continue.

The asymmetry in “the rules of the game” continues – “dumping” is in the eye of the beholder!

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