Tigress Financial Partners

Macro Snapshot – Chief Economist Jean Ergas

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Markets debating Federal Reserve decision, while Norway mulls negative rates. Will this spark "contagion" among central banks? Global economy puts up sign "locomotive wanted" – any candidates?

Deutsche Bank disappoints, breaking news slowly! European bank saga not over and Oslo pronouncements shall not help. Not knocked flat by oil talks!

Markets still weighing Federal Reserve decision

Markets are still weighing the Federal Reserve decision, with the US central bank deciding that discretion is the better part of valor. However, the basic orientation remains to gradually raise rates – should the economic data warrant this.

Nevertheless, the central bank's decision has reawakened fears as to an asymmetry of information between the central bank and investors, with regard to foreign risks.

If this side of the pond is still focused on rate increases we are getting a different signal from Norway, where the central bank does not exclude negative rates. We see this as reflecting both the country's specific predicament as an oil exporter and a cautious assessment of the global economy.

The global economy resembles a group of disparate economies, each trying to stimulate growth via a motley assortment of measures while desperately in search of a "locomotive"

Brexit concerns spreading to peripherals

We are continuing to focus on the Brexit debate in the UK. With recent polls putting the "separatists" and EU fans almost tied, this is no longer a theoretical discussion. There are starting to be concerns that a Brexit might:

Will Euro Zone move to "stand-alone" model?

By both removing a key economic support to the EU
Encouraging others to demand wide ranging concessions, weaken the ties between members. This would put the weaker members in a "stand-alone" position.

We need to soberly ask, whether this might not be the shock that some of these countries might need, to force them to speed up the adoption of structural reforms.

Bank of England – shall not budge!

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With regard to the UK, the Bank of England is expected to leave rates unchanged. The major driver appears to be increasing concerns as to the impact of a UK exit from the EU. This shall not be a clean break but shall involve lengthy negotiations and uncertainty.

UK remains lopsided economy

This stance shall be buttressed by doubts as to the robustness of the global economy expressed by the chancellor – US equivalent, Treasury secretary – in his budget speech. The UK economy remains a study in lop-sided growth, with property gains fueled domestic expansion, offsetting weakness in the "real economy" – capital investment and exports.

Oil – keep your eyes on the "float"!

On the oil front, there is considerable excitement being generated by the meeting scheduled for April. The focus remains squarely on a freeze on production but not on exports. This is not a semantic distinction, with oil being the most traded commodity the "float" is critical.

We remain cautious on oil, as without Iran it shall be difficult to cement a solid coalition.

Focus on European banking

Deutsche Bank disappoints

The European bank saga seems to know no end, with Deutsche Bank shares falling almost 7 per cent following some grim news from the CEO. There may well be another loss this year and dividends are being pushed back.

We see banks as continuing to be pressured by:

The need to increase loss reserves, bad loans abound

For ongoing business, margin erosion – which we do not believe shall be fully compensated by ECB munificence

Limited balance sheet growth caused by:

Increasing capital requirements

With the Euro Zone economy not firing on all cylinders, banks shall remain cautious as to counter-party risk.

Focus on the Federal Reserve

US economy B-, growth moderate not modest!

As expected, yesterday the US central bank did not raise rates but gave a B- grade to the US economy and expressed concerns as to the global economy. The long and the short of it - no pun intended – is that the Federal Reserve still foresees moderate – not, this is key, modest – economic growth. This shall create the underpinning for further rate increases, albeit fewer than expected and with a lower ceiling.

Mention of global risks no specific mention of systemic risk – central bank more concerned with sudden fund flows than business cycle

Much is being made of the repeated mention of conditions abroad, with comments as to a slowing – excellent use of understatement – of the global economy. We see as significant that there is no mention of systemic risk or of strains in the emerging markets. While predicting systemic risk is somewhat akin to forecasting earthquakes, the strains in the emerging markets are manifest.

Federal Reserve playing a cautious game – wants to avoid a perfect storm

We see the US central bank as playing a cautious game, moderating increases to reduce the risk of further increasing EM outflows and financial volatility. In certain cases, the stronger US Dollar is compounding the fallout from the collapse in commodity prices. Large debt loads + a stronger US Dollar + low commodity prices can make for a toxic brew!

Low inflation limits balance sheet deleveraging via nominal growth

As concerns the vexing issue of inflation, the 2 per cent threshold has still not been reached. Nevertheless, Yellen & Co. remain confident that it shall be reached by 2018. We see this as both admitting that the US is in a de-facto deflation and that the nominal growth inflation deleveraging strategy is not an option. Corporate pricing power shall remain modest – forcing companies to rethink their capital structure strategies.

Do not buy arguments as to lack of impetus from the "oil dividend"

The head of the Federal Reserve has also addressed the issue of the whereabouts of the "oil dividend" – which has been conspicuous by its absence. We do not buy the argument that the savings have been shifted to other items – but deem it clear that US consumers are still deleveraging and becoming more cautious.

US Dollar weaker but US still only central bank major developed economy raising rates

On the currency front, we are seeing a weaker US Dollar – as the prospect of short term rate increases diminishes. Notwithstanding, we are informed that the April meeting is a "live" meeting. While the divergence trade may have been weakened, we still see the US as the only central bank on a rate increase path.

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