



*June 13<sup>th</sup> 2016*

***Europe wobbly – bond market ominous – UK poll casts powerful pall – expect report but no action from the US central bank – European banks shall remain under pressure – oil, a lot of wildcards***

***1 - Today's action!***

***European markets off to a shaky start – is it all about the UK?***

*European markets are once again getting out of bed on the wrong foot with the upcoming UK-EU vote – due to its systemic implications – being the major driver. Chinese data has confirmed that the recent recovery is being supported by government capital investment- with retail sales and private investment missing the mark.*

***What is the bond market telling us?***

*Sentiment is not helped by the continued collapse in government bond yields. Investors continue to seek shelter from a “step function” financial assets adjustment following the UK referendum and express their view on both growth and inflation.*

***We expect central banks to hold their fire – banking system still under pressure***

*We expect this context to prompt central banks to continue their easing strategy. This shall lead to both a further distortion in fixed income markets and place pressure on the banking system.*

*Italian banks are once again getting smashed as the difficulties of re-capitalizing ailing banks while seeking to eliminate the link between sovereign and bank risk are once again coming to the fore.*

***And yet more foreign intervention in the UK referendum!***

*The UK-EU poll is prompting a renewed spate of intervention by world political and economic figures and organizations. Following the German minister of finance that it shall not be “business as usual” a further cheerful note has been added by the president of the EU – Donald Tusk.*

***Would a UK exit ring in “The Decline of the West”?***

*We are now hearing that a UK exit shall not only have wide-ranging economic consequences but potentially lead to a Spengler type “Decline of the West” scenario. What is clear is that this might signal the “all clear” for other countries to seek to water down or outright leave the EU.*

***Keen to hear Federal Reserve's report – US economy still going strong?***

*With the UK – EU referendum turning into a cliff-hanger, central bank meetings are getting less attention than customary. We do not expect any moves from the Federal Reserve but shall be focused on their report on the “Rake's progress” of the US economy.*

***The Bank of England is continuing to focus on providing a buffer for a “day after” a UK “leave” vote. Currently, many are forecasting a strong bounce should the “remain” vote triumph. We see a bounce capped by structural problems in the UK economy.***

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### ***Shall not purport to be prophets!***

*Some are arguing that a close victory for the pro-EU camp shall lead to a weakening of the government's position, highlighting the risk of political instability. We do not purport to be prophets and are focused on the potential for a "shock" impacting the global economy and not possible UK domestic squabbles.*

### ***Is the UK poll also impacting energy?***

*Oil prices are also heading south. This is being driven by concerns that the US shale industry may stage a short term rapid production comeback. UK – EU concerns dealing a blow to an already fragile economic framework are also taking a toll.*

***We continue to see several wildcards in the oil space and reiterate our view that even a best case US Dollar 50-60 scenario shall not be sufficient to lift all boats.***

### ***2 – In a nutshell***

***Markets taking fright at UK polls and rush to safety in the fixed income market - UK-EU referendum gaining in importance with some polls showing "leave" winning – UK Prime Minister "very concerned"***

***Heading into US data intense week + Federal Reserve meeting – Oil starting to slip – will it fall further as growth concerns increase?***

### ***Fasten your seat belts!***

*It is now all about the UK-EU referendum. This "binary" event is now seen as the crossroads for short term financial stability and the prospective re-casting of regional and global economic and political order. We reiterate our view that – successful or not –the "leave" campaign has lent respectability to those advocating secession – and anti – EU sentiment.*

***We are seeing increasing desperation by the "remain" camp, with continued foreign intervention to support the status quo having seemingly little impact.***

### ***We shall hear an assessment of the US economy but do not expect action***

*Will the disappointing jobs data and the confluence of event risk and macro concerns last week lead the US central bank to stay its hand? While an increase rate increase is seen as unlikely attention shall be focusing on the "state of the nation" of the US economy. Do we need to get over the UK hump?*

***We expect a re-shifting from cyclical issues to a renewed focus on preventing that potential markets turmoil might be the catalyst for a recession or have systemic impacts.***

### ***Oil market – is this the turning point?***

*Oil prices have remained firm, supported by continued supply disruptions, seasonal factors and the hope that India is poised for a "step function" in fuel consumption. On the US front the debate continues to focus on determining the respective trigger points for an escalation in shale production and / or exploration.*

### ***Two major constraints for concerted action***

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*With regard to the potential for concerted action – we see two constraints. The first is the lift-off in prices from the lows touched in the first quarter. While the second is the continued reluctance of Iran to limit production until its pre-crisis volumes are reached.*

### **Price is now subordinated to stability – shall this lull last?**

*We see price levels as subordinated to price stability as the key factor for producers and investors, with the former taking a “wait and see” attitude prior to relaxing their cost cutting. The latter are drawing comfort from a perceived reduction in systemic risk.*

### **3 - Global overview and what's next?**

#### **Do not see global growth as having reached a turning point – recoveries subdued and bereft of long term investment**

*We see few signs of an improvement in global growth prospects and see political uncertainty as acting as a constraint on capital investment. The economic model shall migrate from the classical model posited on the triptych of government spending, consumption and capital investment to limited recoveries driven by “catch up” consumption and discounting.*

***We reiterate our “stand-alone” approach to assessing economic prospects for selected countries. In the absence of global growth expansion shall be subordinated to resilience.***

#### **Political risk shall be the driver from which central banks shall take their cue**

*With the UK-EU referendum rapidly assuming the contours of “Checkpoint Charlie” for global markets we expect central banks to postpone potentially de-stabilizing measures. Macro issues shall take second place to providing a buffer against market volatility.*

#### **Central banks standing by with fire hoses!**

*Several of the major central banks have confirmed that they are standing by in the event of a “Leave” victory. We see as key the distinction between providing interbank liquidity and managing currency adjustment and the disruptions in equity and fixed income markets.*

#### **Convergence between currency market and FX options incomplete**

*Will the central banks succeed in stabilizing equity and fixed income markets? The key event last week was the convergence between European equity markets and sterling FX options. We do not see this process as having run its course.*

#### **ECB launches corporate bond buying - scant avail for equity markets**

*The start of the ECB's corporate bond buying program was not sufficient in a context of rekindled political risk to either stem a massive flight to quality in the fixed income markets or infuse optimism in the equity markets. In a potential pre-systemic situation investor asset selection is reduced to its simplest terms – move to cash or safe fixed income.*

#### **Axis shifting with demographics from young buying on credit to older generation spending investment income!**

*With regard to the Euro Zone – we are once again starting to hear heated criticism of the ultra-low interest rate policy. These critiques are not focused on macro-prudential banking concerns but on the decline in purchasing power.*

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***Low returns on savings crushing consumption – no point in low interest rates if banks do not lend and companies do not invest!***

*Savers and pensioners are seeing their life's savings vanishing. Due to the lopsided demographics – “re-instating” adequate returns may be more important than fighting unemployment. It is estimated that global GDP has been reduced by more than US Dollars 1 trillion since the start of these monetary experiments.*

***Have we found the philosopher's stone – German government bonds?***

*Are German government bonds the new gold? Investors have been scooping them up like hot cakes and seem ready for a second helping! We are seeing 10 year yields at practically zero and no “buyers strike” in contrast to autumn 2015.*

***German economy shall be the last to fall!***

*This may reflect even further reduced inflation and growth expectations - triggering a further rush for yield and risk / return distortions. A passing thought is that a UK exit may be a harbinger of a EU and subsequently Euro Zone break-up. Investors are honing in on the country deemed to survive best.*

***Is the US consumer still with us?***

*With regard to the US we shall be seeing a considerable amount of economic data. This shall include retail sales which are expected to provide some insight into the last hope of the US economy – the domestic consumer.*

***Will the US consumer – despite a recent fall in consumer sentiment – pick up the slack offsetting stagnant manufacturing and flagging capital investment?***

***US shifting from “locomotive” to bulwark – Is the US the sentinel of the market economy?***

*The concept that the US has shifted its role from that of “locomotive” to bulwark against turmoil continues to gain ground. The Treasury secretary sees a US economy still plowing ahead with “robust” consumer spending and falling unemployment.*

***US labor market additions shall add less than their numbers to purchasing power***

*We shall not reiterate our criticism as to the US labor data but insist on the distinction between accounting and economic employment. What we are seeing is the mopping up of the unskilled, commanding low wages and whose re-entry into the labor market has scant impact on purchasing power.*

***Emerging markets benefiting from commodity stabilization – we do not see this as a game changer***

*As regards the emerging markets we are seeing a firming in selected markets following some stabilization in commodity prices. We do not see this as being a “game changer” – with a commodity super-cycle unlikely.*

***The key challenge for several of the EM economies is shifting from managing the commodity cycle to implementing long term reductions in government spending.***

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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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