Tigress Financial Partners

Macro Snapshot – Chief Economist Jean Ergas

July 25, 2016

July 25th 2016

Political risk rising – A spanner in the works for the Democratic convention? - Waiting for the central banks – Are we waiting for Godot? -"Fistful of Dollars" for the Italian banks? - More platitudes from the G-20 – Beware of the anger of "The Great Displaced"

In a nutshell!

See political risk in the ascendant

Despite the avalanche of US earnings next week we see political risk as increasing and – together with the oil price- see it as being the major market driver. Visibility as to the "shape of things to come" in the UK remains near zero, the situation in Turkey is likely to escalate and the US electoral campaign is getting moving in earnest.

Continued demand for safe haven assets

We expect to see continued demand for safe haven assets and currencies irrespective of absolute return levels. Top rated sovereign bonds in the Euro Zone are starting to be seen as the "natural" home for single currency allocation. US Treasuries remain the one cash yield instrument with investors likely to reap the dual benefit of currency appreciation.

Focus on the US election

Will Wiki leaks decide the US election?

Are we seeing the political risk fulcrum shift to the US? Wiki Leaks be the final arbiter of the US election? The steady leaking of e-mails indicating that the DNC has not conducted a campaign in line with the - already very low standards – of political life may once again ignite doubts as to Clinton's candidacy.

This week!

Shall central banks step up to the plate?

Where to this week – fraught with data and central bank meetings? Shall investors continue to bask in the expected munificence of the lenders of last resort who have mutated into "the takers of the last risk"? Or shall the focus shift from the remedy to the cause?

Germany – not all is lost!

With regard to data markets are encouraged by a lower than expected fall in German business confidence. This is seen as an indicator of lesser than expected fall-out from the UK exit vote. We see this as a possible first indicator very early on in a very long process still fraught with uncertainty.

While markets are continuing to focus on the UK situation, this is one variable in a dynamic situation. Global growth independently of the UK conundrum remains muted and the ultimate effectiveness of monetary policy open to doubt.

Jean Ergas
(646) 780-8880
jergas@tigressfp.com
Twitter: @jean_ergas

Tigress Financial Partners
Member of FINRA / MSRB / SIPC
500 Fifth Avenue
New York, NY 10110
(212) 430-8700
www.tigressfinancialpartners.com

To subscribe to Jean's Global Macro Overview, order customized reports, or gain direct access to Jean, contact research@tigressfp.com.

UK manufacturers not cheering

As to the UK itself, manufacturing confidence is at levels last seen at the trough of the 2009 debacle – what is significant and latches on to the global picture is that expectations for export orders are almost nil. This stands at odds with prevailing orthodoxy that a collapsing currency would trigger a massive export boom.

UK falling into same trap as the Euro Zone

We are seeing the UK fall into the same "trap" as the Euro Zone, where currency devaluation is seen as the solution to a moribund domestic market. The key point is not the currency but that the "pie" is not getting bigger – and as the first wave of economy building in some emerging markets subsides – in some areas getting smaller.

European economies remain closely intertwined

The European economies abstracting from whether they are or are not in the Euro Zone, remain closely intertwined. The UK shall face considerable difficulties as it seeks to simultaneously reduce its dependence on its erstwhile associates while increasing exports to the EM space.

Can these economies - riskier and focused on development cycle imports - compensate for the steady cash flow and low risk of the EU? We see the UK as losing "bread and butter" business and shifting to "lumpy' export flows.

Gearing up for Euro Zone GDP and inflation data

This week we shall also be seeing Euro Zone second quarter GDP and inflation data. We are not holding our breath for either and expect a steady but muted advance and quasi deflationary conditions. Growth was slowing before the UK events and the ensuing uncertainty shall not help going forward.

We disagree with the ECB view that this is not about inflation but inflation expectations. Expectations are useless unless they are translated into action!

"Fistful of Dollars" for the Italian banks?

As concerns the Italian banks we are waiting for the "shoot-out at the OK Corral". Italy has rejected the collective punishment approach and is now contingent on a "state of exception" with regard to EU rules. What is clear is that one of the fundamental aims of the EU banking reform – the separation of sovereign and banking risk shall remain a utopia.

Banking stress tests coming up!

We shall be seeing the results of the EU banking stress tests this week. The only forecast is that the tests shall once again underestimate the necessary capital boost. In the US banks were recapitalized in the context of an – albeit modestly – recovering economy. The European economy presents a moving target with potentially systemic events still ahead of us.

Global round up

1 – UK situation government starting to flounder!

With regard to the UK we see the UK government as starting to flounder in defining its strategy in the wake of its "Mutiny on the Bounty" decision. The timing of the triggering of article 50 remains nebulous with the uncertainty starting to impact the UK economy – collapse in services to the lowest level since 2009 and manufacturing PMI revisiting 2013!

Can bilateral trade agreements supplant access to EU?

We see declarations as to the willingness of certain countries to enter into bilateral trade agreements with the UK as a means of breaking the prospect of loss to the single EU market gently to a concerned public. There are fewer references to ensuring the status quo. Instead we are being presented a hodgepodge of exemptions and new trade deals.

"Bad moon rising" on the UK property market

As regards the critical property market – backbone of consumption-in the UK we see a "bad moon" rising. This shall be driven on the commercial front by the lesser attraction of London as a headquarters – except for mining houses and groups with colonial connections. The residential front shall be impacted by a likely contraction in lending as the recession hits.

2 – European banking crisis not coming off the boil!

The European banking crisis shall continue to be a volatility driver. Its importance is highlighted by the suggestion by the governor of the ECB to establish a "Marshall Plan" for the Euro Zone banking sector. This call to arms is tantamount to admitting that a private sector recapitalization shall not be forthcoming.

Italy is the front line in the banking crisis

The crisis is at its most acute in Italy where a solution to the banking crisis needs to be found prior to the government's institutional referendum in October. The EU has been reluctant to allow direct "first buffer" use of taxpayer money to shore up the banks – a "catch all" scheme combined with a systemic risk exemption might be a way out.

This is not only about legacy bad loans

We continue to see exemptions and waivers as remedies for a legacy situation. This shall not be adequate for coping with a likely increase in bad loans as economic stagnation persists – a pressure which shall be compounded by the need to meet ever stricter capital requirements.

3- Euro Zone shall continue to bump along the bottom

Turning to the Euro Zone we see the economy as bumping along the bottom, with overall growth low and disparate economic performances. The last PMI data while showing stability or increase on a services, manufacturing and composite basis is still indicating minimal expansion.

Pincer squeeze on capital investment and obsolescence of capital stock

This shall not be sufficient to rekindle inflation and reduce the risk of "silent re-leveraging". The Euro Zone shall need to simultaneously countenance the dual pressures of minimal capital investment and the progressive obsolescence of the capital stock. We see domestic demand as brittle and supported by "windfall" deflation driven pay increases.

4 - Monetary policy shall remain accommodating

ECB shall attempt to supplant fiscal policy

Monetary policy shall likely remain accommodating as the ECB seeks to stand in for fiscal policies still constrained by budget deficits. We see the impact of bond buying as hitting its limits – with zero rates not having succeeded in either boosting inflation or lifted growth.

Federal Reserve shall likely play it safe

We see the Federal Reserve as inclined to play it safe. This choice shall be dictated by the looming US elections and concerns as to a further US Dollar depreciation triggering a "mass of money" flight out of the EM space. With the cost being adjusted by the credit markets – the key concern remains the impact on foreign markets.

Bank of England shall lean towards reducing rates - UK growth trajectory shall be more muted

We expect the Bank of England to progressively cut rates to attempt to lend a boost to a UK economy expected to fall into a "shallow recession". While the recession may be shallow – a view we do not share – we see the key point as being that the recovery shall be equally shallow.

Can a low FX rate offset tariffs?

We see the Bank of England also using the FX rate to mitigate the impact of uncertainty on foreign direct investment decisions. The assumption is that a low enough spot FX rate shall serve as a buffer against lesser unfettered access to foreign markets.

We do not share this view and see job creating and job sustaining foreign direct investment as decreasing or being limited to maintenance levels. One senses the desperation of the "leave" contingent when the possibility of the UK as a giant Singapore free port is mooted!

5- Remain cautious on commodities – bounced off very low levels

With regard to commodities we remain of the view that the best is behind us. We are seeing a bounce off very low levels – apt for trading but not for reinforcing sovereign balance sheets. Should global growth start to once again balk producers shall need to face the situation with substantially reduced reserves and lesser access to the capital markets.

6 – Focus on Turkey

1970's coup in the "Age of Facebook" – historical disconnect

Turning to the situation in Turkey we reiterate our view that this represents a "disconnect" with history. We are seeing the Turkey of the late 1970's in a global economy and social media + technology. Our concerns that the coup shall be the "Reichstag" fire are being amply confirmed as the government strikes at real and imagined opponents.

Current account shall come under further pressure

From the economic point of view we see the current account deficit issue as becoming more acute. The collapse of the currency and internal focus of the economy shall impact "The kindness of strangers". Foreign investors shall be less willing to cover short term financing gaps and provide longer term foreign direct investment.

We continue to see the "bottom line" as political. The "bottom line" remains the security issue and not the economy. NATO and the struggle against ISIS and Assad remains the key objective.

Focus on the G-20

A lot of "static" from the G-20!

The upshot from the G-20 conference appears to have been that central banks shall counteract the worst consequences of the Brexit - what the parameters for intervention and success might be remains unclear.

When is a recession not a recession?

Is a recession in the UK acceptable but in the Euro Zone not? Or is the focus on avoiding a systemic risk from the banking system? Will the maintaining of a status quo of slow growth and overextended financial markets be deemed the first best outcome?

Focus on globalization and its discontents

Was Marx right? Heretic thought!

The G-20 conference has solemnly resolved to seek to redress the rising income inequality and pauperization – to borrow an expression from Marx – of substantial shares of the working and middle classes. We see the need to point out that the rage in the US is largely because the middle class position of industrial workers has now been demolished.

Beware those who vote for the first time!

The US was singular in that upward mobility often meant a factory job. It shall be extremely difficult to restore this state of affairs. Get ready for some electoral surprises as many of "The Great Displaced" cast their first presidential ballot.

Rise of the "Populist international"

We are seeing for the first time a cross border symmetry in political shifts as those left by the wayside unite in a "populist international". The G-20 are free to preach good intentions –implementing them without imposing trade barriers shall be impossible.

Do not wish to be "allocated"!

With regard to free trade now seen as the "root of all evil" we see the G-20 participants as still steeped in their undergraduate international economics courses of their undergraduate years. We read of finance ministers extolling the long run benefits of free trade and the correct allocation of resources.

We see being "allocated" as a not altogether pleasant experience! It bears a close resemblance to the "shock" therapies visited upon hapless emerging markets!

Advanced economies have bifurcated

Notwithstanding that privilege has never been so well rewarded in advanced economies as today we continue to be intent on seeking to stimulate development in the emerging markets. We are losing track of the fact that advanced economies have bifurcated into a knowledge economy and early stage developing markets. Trusting in the long run is not a solution!

Instead of establishing new "Marshall Plans" abroad, should we want to avoid a return to the world of David Copperfield's London, governments need to set up plans to either retrain or extend support to the displaced.

Focus on the UK country risk

Outflows from UK funds becoming a torrent!

Are we starting to see some realism about the Brexit UK situation following a one month phase of denial? Outflows from UK exposed and managed funds have swelled into a torrent and some are even considering withdrawing funds from UK managed global funds.

We are seeing a wider definition of country risk

Research: (646) 780-8880 research@tigressfp.com
500 Fifth Avenue New York, NY 10110 (212) 430-8700 www.tigressfinancialpartners.com

We are now at the point where country risk has extended from the investment target to domicile of investor. We see this trend as continuing and abetting further outflows from Europe focused funds. A continued "run" on these targets may lead to a reallocation of funds to the US market – overvalued but seen as a necessary evil to maintain asset allocations.

Contacts

Jean Ergas
Chief Economist
(917) 551-6533 Direct
jergas@tigressfp.com

Ivan Feinseth
Chief Investment Officer
(646) 780-8901 Direct
ifeinseth@tigressfp.com

Philip Van Deusen
Director of Research
(646) 862-2909 Direct
pvandeusen@tigressfp.com

Ernest Williams
Institutional Sales & Trading
(646) 862-2912 Direct
ewilliams@tigressfp.com

Lily Li
Managing Director
Global Wealth Management
(646) 780-8903 Direct
lilyli@tigressfp.com

About Jean:

Jean Ergas is the Chief Economist for Tigress Financial Partners LLC (Member FINRA, MSRB,SIPC) based in New York City.

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.

Jean is a member of the American Institute of Certified Public Accountants and has an MBA and an Advanced Professional Certificate in Accounting from New York University's Stern School. He has also passed the FINRA Series 7 examination.

Research Report Disclaimer

This report is produced for informational purposes only and is not a solicitation to buy or sell any securities or services from any companies or issuers mentioned herein or to participate in any particular trading strategy or in any jurisdiction in which such an offer or solicitation would violate applicable laws or regulations.

Tigress research is distributed in the United States by Tigress Financial Partners LLC a registered broker dealer with the Securities and Exchange Commission (SEC) and a member of the Financial Industry Regulatory Authority (FINRA) and in Brazil by Gradual Investmentos, Gradual CCTVM S/A, a financial institution authorized by the Central Bank of Brazil.

The information contained herein has been obtained or derived from sources believed to be reliable but its accuracy and completeness is not guaranteed and should not be the sole basis of any investment decision but only to be used as a factor in the investment decision process.

This report does not provide individually tailored investment advice and has been prepared without regard to the individual financial circumstances and investment objectives of any person(s) receiving it. The analysis and conclusions herein are not a complete analysis of every material fact respecting any company, industry, or security. The opinions expressed in this report reflect the judgment of the author(s) at this date and are subject to change without further notice. Tigress Financial Partners is under no obligation to provide updates to recipients of any previously issued reports or recommendations.

The market value and expected income from any investment may vary because of changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of the underlying companies or other factors. Past performance is not indicative of future performance. Estimates of future performance, research ratings and target prices are based on assumptions that may not be realized. Unless otherwise stated, the cover page provides the most recently available closing price on the primary exchange for the subject company's securities/instruments.

Securities are offered through Tigress Financial Partners LLC a SEC Registered Broker Dealer and a member of FINRA / MSRB / SIPC which clears its securities transactions and provides custody of client accounts on a fully disclosed basis through Pershing LLC, a subsidiary of The Bank of New York Mellon.

Securities in your account are protected up to $500,000 of which $250,000 can be for claims for cash awaiting reinvestment. Please note that SIPC does not protect against loss due to market fluctuation. For additional information please go to www.sipc.org.

In addition to SIPC protection, Pershing provides Tigress Financial Partners LLC client accounts coverage in excess of SIPC limits from Lloyd’s of London, in conjunction with other insurance companies. The excess of SIPC coverage provides an aggregate loss limit of $1 billion for eligible securities over all client accounts and a per-client loss limit of $1.9 million for cash awaiting reinvestment within the aggregate loss limit of $1 billion. The excess of SIPC coverage does not protect against loss due to market fluctuation. For additional information please go to www.lloyds.com.

Pershing’s excess of SIPC coverage is provided by Lloyd’s of London in conjunction with XL Specialty Insurance Co., Axis Specialty Europe Ltd., Great Lakes Reinsurance (UK) PLC and Ironshore Specialty Insurance Co.

About Tigress Financial Partners LLC

Tigress Financial Partners is a specialized financial services firm providing expertise and services in investment banking, investment research, asset management, corporate advisory and trade execution services.

Tigress Financial Partners provides its services to corporate entities, institutional investors, high-net worth individual investors, public and private pensions, federal, state and municipal governments.

Tigress Financial Partners LLC is a registered broker dealer with the Securities and Exchange Commission (SEC) and a member of the Financial Industry Regulatory Authority (FINRA), the Municipal Securities Rulemaking Board (MSRB) and the Securities Investor Protection Corporation (SIPC).

Tigress Financial Partners LLC is a Woman-Owned Business Enterprise (WBE) and is nationally certified by WBENC, the Women’s Business Enterprise National Council.

Tigress Financial Partners LLC is a wholly-owned subsidiary of Tigress Holdings LLC and Gradual Holding Financeira S.A.

For further information please go to www.tigressfinancialpartners.com.