Tigress Financial Partners

Macro Snapshot – Chief Economist Jean Ergas

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Still waiting for central banks – Facebook – "the real economy"? – Oil does not look promising – Federal Reserve no surprises – European banks, is this mission impossible? – UK moving speedily towards a "hard Brexit" and triumph of ideology over economic pragmatism

Will central banks keep delivering?

Will the central banks keep delivering and creating a – for some TINA situation for stocks? With the Federal Reserve reiterating its cautious stance yesterday this is starting to once again be the dominant view. Investors are expecting more generosity from the Bank of Japan and the Bank of England – should one no step up to the plate there may be some disappointment.

Facebook - has this become the "real economy"?

With regard to corporate earnings there shall be no lack of them the rest of this week. Facebook's strong performance is likely to provide a boost. Investors appear to once again be attempting to distinguish between the "real" macro economy and the "new economy" – with the two not necessarily marching to the same beat.

Formerly superfluous now a key lever in dramatic political change

The key is no longer on traditional sectors and essentials but on what was previously deemed to be superfluous. We might though well ask whether – with coups and popular revolts broadcast and organized on the web – social media are now the de-facto politically key communications channel.

See oil price weakness persisting – get ready for another jump in production

We are not surprised by the continued weakness in the oil price. Long skeptical as to "The end of oversupply" we expect the glut to persist as traditional producers keep pumping flat out. Several are putting the building blocks in place for capital investment and a further leap forward creating further pressure.

This is about generating cash not complex risk adjusted models!

The repeated calls for a feline leap towards US Dollars 70 have not proven prescient. The US shale producers took advantage of the recent spike to US Dollars 50 to hedge production and are now cash operating costs positive.

As compared to other sectors this is not about risk adjusted returns and sophisticated formulas but about generating sufficient liquidity to fight another day!

Are not convinced by EBA optimism

We continue to follow the European banking crisis and its manifold ramifications with stress tests results to be announced tomorrow. The issue we are told by the head of the European Banking Authority is not about capital but about bad loans! Whether the two can be separated remains unclear.

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With bad loans at three times the US level – we make the case that even at current capital requirements a large part of the EU banking archipelago is still under water.
Focus on the Federal Reserve meeting

We do not share the Federal Reserve's enthusiasm!

The Federal Reserve meeting yesterday contained few surprises, with the US central bank veering on the side of caution and leaving rates unchanged. We differ as to the Federal Reserve's view of the US economy and do not share their enthusiasm as to either the consumer or the labor market.

It is still somewhat of a mystery why almost full employment has failed to trigger pay increases of any significance.

US central bank opts for the "Monroe Doctrine" – Like Thomas Wolfe's angel "Looks Homeward"!

We see as the key to the Federal Reserve's statement that risks to the US economy have diminished. This confirms our view that they have defaulted to the "Monroe Doctrine" as to the guidelines for policy. Systemic risk is seen as having receded and cyclical swings are deemed acceptable.

We need to bear in mind that this is not tantamount to stating that the US economy is booming – even accepting the modest standards now prevalent - nor that there cannot be further foreign turbulence.

Federal Reserve preparing the ground for an increase later this year

We see the US central bank as gingerly preparing the ground for a rate increase later this year. The driver shall not be a marked improvement in economic performance but the perception that the economy is stabilizing. We are seeing a Federal Reserve which has taken a page from the stock market – set expectations ridiculously low and cheer any progress however slight!

Focus on US macro data

Should we be surprised by durable goods?

We were not surprised by the dismal durable goods data – which is miserable any way you slice it. This is the "The other side of the moon" of companies' massive cash and consumer "big ticket" liquidity being tapped out. Contraction or at best "noise" growth is the consequence of capital investment being put on hold and export markets slowing.

We distinguish between the economic and political electorate

We see this report as further putting the onus on a relatively small part of the US economic as opposed to political electorate to do the heavy lifting. While manufacturing represents less than 15 per cent of the economy historically it has been a bed rock of pricing power. This may not bode well for company profits.

Focus on the UK

UK may follow Lou Reed trade strategy – Shall take a walk on the wild side!
With regard to foreign news, we are seeing further confirmation that the UK may end up with a "hardball" version of Brexit. Rumors are circulating that the Trade Secretary is putting pressure on the UK Prime Minister to "take a walk on the wild side". This shall involve rejecting a custom's union and seek to strike one-off trade deals or a hybrid between the EU-Canada Free Trade Agreement not yet in force- and the EEA.

Both UK and EU negotiators potentially antagonistic

Appointment of a UK not friendly exit negotiator by the EU leaves little wiggle room for the UK to have its cake and eat it! We see a WTO light as opposed to an EEA as the likely outcome with regard to the EU. Currency depreciation shall remain meanwhile both the trade and economic strategy. We see two key issues in this regard:

Industrial companies are not spot FX traders and seek both a convenient asset price / FX rate and the prospect of sustainable export cash flows. With the almost Castro in 1959 atmosphere of UK – Yes – EU No a single market lite solution looks difficult.

Can "competitive devaluation in one country" work?
Should the UK opt for "competitive devaluation in one country" they shall be facing a Hobson's choice. The options shall be: letting imported inflation rip or raising real interest rates and crushing a timid recovery.

We do not see the FX rate as sufficiently low to attract "no matter what" capital investment.

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