The Weekly Market View

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Fed undecided, but growth continues to be weak

Last Wednesday's FOMC statement stuck to its basic script that the US economy continues to grow at a moderate pace. At the same time the statement dropped previous references to weakness abroad. It is interesting to observe that once more the renewed speculation about imminent rate hikes is more harmful to emerging markets than to US markets themselves. In fact, whilst the US dollar appreciated against most currencies and yields also picked up, the US equity market quickly recovered from its initial correction. Emerging equity markets on the other hand are down again, as are emerging currencies, whilst EM sovereign CDS spreads are up. Interestingly, third quarter US GDP growth was - at 1.5% annualized - slightly below expectations. True, the figure might have been exceptionally low because of the inventories drawdown, such that a pick-up towards the end of the year looks reasonable. Having said so, it is not at all clear that the US economy can grow above its 2% trend growth rate. With inflation still very depressed, it is therefore yet to be seen whether the Fed would really hike in December.

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Global PMIs and US labour market data to take centre stage

Now that the markets are again seriously considering a Fed rate hike, it will be critical this week to watch the global PMIs, as well as the US labour market. After all, the Fed has throughout stated that it remains data dependent. On the PMI front, the German IFO has gone up, whilst the official China PMI keeps sliding downward. We expect the US ISM and China "Caixin PMI" figures to also point south, possibly to the point that markets will to some extent revert their bet towards the Federal Reserve not hiking in December (currently the bets are evenly spread between "no hike" and "hike"). At the same time we think that the US labour market will continue to indicate modest growth. Continuing uncertainty is likely to keep a lid across markets this week, and possibly some renewed selling pressure on emerging markets.

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Past week global markets' performance

Index Snapshot (World Indices)

Index	Latest	Weekly Chg %	YTD %
S&P 500	2,079.4	0.2	1.0
Dow Jones	17,663.5	0.1	-0.9
Nasdaq	5,053.7	0.4	6.7
DAX	10,850.1	0.5	10.7
Nikkei 225	19,083.1	1.4	9.4
FTSE 100	6,361.1	-1.3	-3.1
Sensex	26,656.8	-3.0	-3.1
Hang Seng	22640.0	-2.2	-4.1
Regional Markets (Sunday to Thursday)			
ADX	4322.0	-3.6	-4.6
DFM	3503.8	-2.4	-7.2
Tadawul	7124.8	-3.5	-14.5
DSM	11604.6	0.2	-5.5
MSM30	5928.15	0.4	-6.5
BHSE	1250.4	-0.3	-12.4
KWSE	5775.4	-0.1	-11.6
MSCI			
MSCI World	1,705.8	-0.0	-0.2
MSCI EM	847.8	-2.4	-11.3

Global Commodities, Currencies and Rates

Commodity	Latest	Weekly Chg %	YTD %
ICE Brent USD/bbl	49.6	3.3	-13.6
Nymex WTI USD/bbl	46.6	4.5	-12.5
OPEC Baskt USD/bbl	44.3	2.1	-14.7
Gold 100 oz USD/t oz	1142.1	-1.9	-3.6
Platimum USD/t oz	985.1	-1.6	-18.4
Copper USD/MT	231.8	-1.4	-18.0
Alluminium	1452.75	-1.0	-20.8
Currencies			
EUR	1.1006	-0.1	-9.0
GBP	1.5428	0.7	-1.0
JPY	120.62	-0.7	-0.7
CHF	0.9879	1.0	0.6
Rates			
USD Libor 3m	0.3341	3.5	30.7
USD Libor 12m	0.8684	4.4	38.1
UAE Eibor 3m	0.8446	-0.1	24.7
UAE Eibor 12m	1.2189	1.8	20.0
US 3m Bills	0.0712	90.2	100.6
US 10yr Treasury	2.1421	2.7	-1.3

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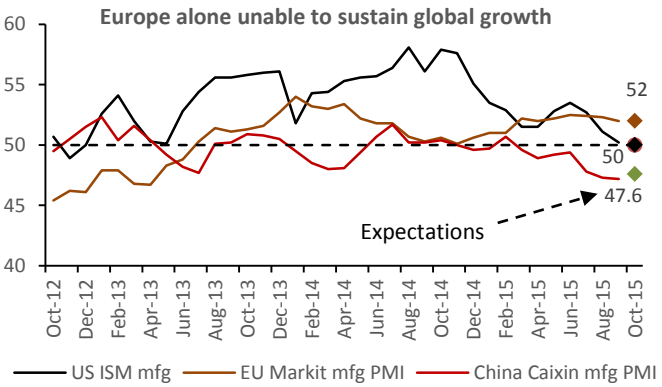
Global PMIs and US labour market to confirm sluggish growth, Fed uncertainty to persist

Monetary divergence again?

With the PBoC, the ECB and the BoJ still on a firmly expansionary track, the Fed has now made clear that it might still hike rates in December of this year. We are thus potentially back to the type of monetary policy divergence that - to a large extent - was behind the markets' instability of the past summer, specifically emerging markets' instability. Or are we not? We continue to nurture doubts about the Federal Reserve hiking rates in December. For one thing, a sustainable growth pick-up remains elusive in the US. It's not that US fourth quarter growth will not improve upon the third quarter. That is quite possible, and even likely. The point is another one. With earnings very likely under pressure, a strong US dollar sucking growth away via the external balance, and investments still lagging in spite of the late stage of the current business cycle, it seems that the US economy continues to be unable to muster above trend growth. The combination of sluggish growth and low inflation will make it risky for the Federal Reserve to hike rates, at the same time that China and other emerging markets continue to be afflicted by significant capital outflows. It is better to be prudent than to be sorry, and thus the Federal Reserve would prefer to err to the downside rather than risk triggering a more significant global slowdown.



Source: Bloomberg

US labor market to confirm old problems

With the official unemployment rate at 5.1%, one could argue that the expectation of 180k jobs having been created in October is still confirming the moderate pace of economic growth indicated by the Federal Reserve. The problem is that such economic growth is still unable to determine a serious lift-off in wage growth, more than six years into the expansionary cycle.

Source: Bloomberg

The persistent lack of income growth is keeping a lid on overall economic growth. Indeed, the absence of significant income growth sheds a shadow over the specific job growth that the US economy has so far enjoyed. The overall quality level of jobs has come down, such that the same level of job security no longer reflects the level of income security it once entailed. Many newly created jobs are low pay jobs, often also part-time jobs. The risk of an earnings recession should also be seen in this light. So far companies have been able to grow their earnings thanks to cost reductions in the face of weak revenues. It now looks increasingly likely that the potential for cost squeezing is over, whilst revenues continue to be depressed because of depressed income levels.

In reality, the lack of solid income prospects has determined a record low level for the job participation rate. Only a substantial growth of the labour force would be compatible with higher growth levels and a return to inflationary slack in the economy.

Monetary divergence problematic for emerging markets

The Fed pursuing rate hikes and the ECB increasing QE constitute a dangerous combination for emerging markets in general, and China in particular. Imminent Fed rate hikes determine a pick-up in capital outflows out of China, making it more difficult for the Chinese authorities to stimulate the economy. Increased ECB QE will determine upward pressure on the US dollar, such that also the renminbi will strengthen against the euro. Europe is China's biggest client. Thus even if the Chinese authorities manage to stimulate the economy through more liquidity and lower interest rates, the weaker euro will inevitably constitute a drag on companies profits' and exports. In this sense it will be important to see this week by how much reserves have changed in China. We believe that the Fed hiking rates would be problematic for overall emerging markets. It is more likely, therefore, that Mrs. Yellen will stay put at least until March 2016.

Summary market outlook

Global Yields	A relatively hawkish tone of the FOMC statement and a better than expected composition of the third quarter GDP growth, despite a muted headline number, put upward pressure on US Treasury yields. With important economic releases lined up this week, any positive surprises are likely to push yield further higher in the near term.
Stress and Risk Indicators	The VIX index remained largely flat over the last week. With market probability for the Fed hike this year again on the rise, risk indicators are expected to remain elevated. Sovereign CDS spreads for EMs, particularly from Asia moved up again. Stronger economic indicators from the US are likely to push them further higher in the near term.
Precious Metals	A relatively hawkish Fed statement pulled precious metal price lower. We have maintained a cautious note on the asset class for some time and we remain so.
Local Equity Markets	GCC equity markets closed largely negative last week due to mixed earnings announced by large local companies and the uncertainty around the oil price. We remain cautious on local equities in the near term.
Global Equity Markets	Developed markets' equities were largely resilient last week despite a relatively hawkish FOMC statement. However, with rising concerns for a Fed rate hike this year, EM stocks came under pressure along with their currencies. Volatility in global equity markets, in particular EM equities, is likely to continue, more so if US economic releases prove to be stronger this week.
Energy	The oil price gained last week on favourable data releases – US production in August declined marginally and weekly product inventory numbers declined more than expected. However, we remain cautious in the near term and expect volatility to persist as the price is yet to settle.
Industrial Metals	Notwithstanding the recent gains in industrial metal prices, uncertainty around emerging economies' growth, in particular China's, is likely to continue to weigh on industrial metals.

Currencies	**Commentary**	**Critical levels**
EURUSD	After a week of Mr. Draghi's push, the euro got further pushed lower by the relatively hawkish FOMC statement. Since then the currency staged a technical recovery. However, we believe that the risk for a sharper depreciation has once again increased, given the monetary policy dynamics in the two economic blocs.	R2 - 1.1199 R1 - 1.1102 S1 - 1.0903 S2 - 1.0801
GBPUSD	The currency pair has largely moved by the relative strength of economic releases in the recent weeks. The situation has not changed much despite a relatively hawkish FOMC statement. The BoE meeting is important this week. We believe that the currency pair is unlikely to move in either direction significantly in the near term.	R2 - 1.5605 R1 - 1.5516 S1 - 1.5291 S2 - 1.5155
USDJPY	The currency pair remained in a trading zone for some time despite events changing the monetary policy and economic outlook in the two countries. Therefore, we do not see any immediate reasons for any significant move either way. Higher global risk perceptions could push the currency slightly higher (stronger) temporarily.	R2 – 122.24 R1 – 121.43 S1 – 119.94 S2 – 119.26

Forthcoming important economic data

United States

	Indicators	Period	Expected	Prior	Comments
11/02/2015	Markit Mfg PMI	Oct F	54.0	54.0	After a relatively hawkish FOMC statement, markets will look at all upcoming important data, in particular the job market data, to build expectations for an eventual Fed rate hike.
11/02/2015	ISM Manufacturing	Oct	50.0	50.2	
11/03/2015	Factory Orders	Sep	-0.9%	-1.7%	
11/04/2015	ISM Non-mfg	Oct	56.5	56.9	
11/06/2015	Change in Nonfarm Payroll	Oct	180k	142k	
11/06/2015	Unemployment Rate	Oct	5.1%	5.1%	
11/06/2015	Avg Hourly Earnings YoY	Oct	2.3%	2.2%	

Japan

	Indicators	Period	Expected	Prior	Comments
11/02/2015	Nikkei Mfg PMI	Oct F	NA	52.5	Preliminary manufacturing PMI reflected some rebound, markets will see if that wil be confirmed by the final release.
11/02/2015	Vehicle Sales YoY	Oct	NA	-3.0%	
11/06/2015	Leading Index	Sep P	101.9	103.5	

Euro zone

	Indicators	Period	Expected	Prior	Comments
11/02/2015	Markit Mfg PMI	Oct F	52.0	52.0	Markets will see if there is any surprise in economic data from the Eurozone, especially from Germany.
11/05/2015	Retail Sales MoM	Sep	0.2%	0.0%	
11/02/2015	Markit/BME Mfg PMI (Germany)	Oct F	51.6	51.6	
11/05/2015	Factory Orders MoM (Germany)	Sep	1.0%	-1.8%	
11/05/2015	Industrial Production (Germany)	Sep	0.5%	-1.2%	

China and India

	Indicators	Period	Expected	Prior	Comments
11/02/2015	Caixin Mfg PMI (China)	Oct	47.6	47.2	Markets will focus on China's external trade data along with change in its foreign reserves.
11/07/2015	Foreign Reserves (China)	Oct	$3470B	$3514B	
11/08/2015	Trade Balance (China)	Oct	$59.5B	$60.3B	
11/08/2015	Exports YoY (China)	Oct	-2.8%	-3.7%	
11/08/2015	Imports (China)	Oct	-13.7%	-20.4%	
11/02/2015	Nikkei Mfg PMI (India)	Oct	NA	51.2	

Sources

All information in this report has been obtained from the following sources except where indicated otherwise:

1. Bloomberg
2. Wall Street Journal
3. RTTNews
4. Reuters
5. Gulfbase
6. Zawya

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