Weekly Market Summary

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There Comes a Time When Confusion Reigns & Markets Tank !!

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The big question of whether the Federal Reserve will raise rates at its September 17th FOMC meeting – coupled with major "risk-off" developing events over the past 72 hours – has hung heavy over financial markets in past days, resulting in heavy losses for both equity and commodity markets.

Market participants – on Wednesday evening - scrutinized minutes of the July 29th Fed meeting, though in retrospect should have realized that heightened risk of too-low inflation (the CRB index – an arithmetic average of 19 commodity futures prices – has dropped in excess of 5% in the past 3 weeks and WTI oil is down 16% during that same period), more fragility in emerging economies and renewed concerns over the health of the world's second largest economy (China) since that last Fed gathering would all together persuade many Fed governors to revisit their economic forecasts and perhaps take a September interest-rate hike off the table when they meet next (in that context, a corporate Treasurer/friend who seriously doubted our stance last week in favor of a September 17th rate hike deserves good credit!)

Here are the key developments that shaped markets this week:

- According to minutes of the July 28th-29th Federal Open Market Committee (FOMC) – released on Wednesday – Federal Reserve officials signaled concern about stubbornly low inflation as well as how soon they would hit their 2% inflation target, even as they acknowledged that the job market improvement is bringing them closer to the first US rate increase in almost a decade. Their debate was silent on whether they should act in September or delay their interest rate hike to gather more evidence that inflation is heading higher. That discussion highlights a dilemma for the data-dependent FOMC: As the job market continues to deliver robust gains, with unemployment at 5.3%, holding interest rates near zero is harder to justify especially that the US expansion enters its seventh year. At the same time, officials want to avoid the error of tightening policy too soon, especially when inflation gauges remain persistently weak and global growth prospects remain dim.

- German and other European lawmakers approved a bailout for Greece. The vote will unlock a third aid program for a total of EUR 86 billion as agreed by Euro area finance ministers a week back (first EUR 13 billion aid tranche handed to Greece yesterday). However fresh doubts have emerged this morning after the overnight resignation of prime minister Alexis Tsipras plunged the country into new political uncertainty. The widely expected move means elections mid-next month, but there are also fears it could slow progress on controversial reforms agreed by the debt-burdened country with creditors as part of the rescue. Moody's credit rating agency warned in a statement that the snap elections "*could elevate programme implementation concerns*" and potentially put further installments of the bailout package at risk.

- China's central bank (PBOC) has been regularly injecting cash in the banking system via reverse repurchase agreements, though that has so far not been enough to offset market liquidity tightness. Without Beijing's clear policy support and the "national team" bailing out, the Shanghai Composite Index has dropped a further 12% this week (though month-to-date losses stand at a smaller 6%...Hurrah!). This morning, a Chinese manufacturing gauge fell to the lowest in more than six years, suggesting the economy will need further policy support to stem a deepening slowdown. The preliminary Purchasing Managers' Index (PMI from Markit Economics) stood at 47.1 in August, compared with a median estimate of 48.2 and the final reading of 47.8 the previous month (numbers below 50 indicate contraction). The release is the first major indicator for August and follows weaker-than-expected data on investment, industrial output, retail sales and exports in July

- Emerging-market currencies continued falling, extending the longest stretch of weekly declines since 2000, as Malaysian assets tumbled, Turkey's lira touched a new record low on security concerns and the Russian ruble (and stocks) further retreated with oil. This week's latest casualty was the Thai baht as a bomb blast in Bangkok added to Thailand's economic woes, further intensifying outflows from local equities (that is not to mention the Kazakhastan's Tenge, which dropped 22% this week after being allowed to freely float.. talk about a free plunge !!)

- The biggest herd of dollar bulls is looking vulnerable as traders' lowered odds for a Fed rate hike in September reduce the appeal of the greenback. The US dollar dropped yesterday to the lowest level since June against the euro as an emerging-market rout pushed U.S. stocks to their biggest decline in 18 months. It fell against most of its 16 major peers, dropping to a low of 1.1297 per euro and 122.81 yen earlier this morning. Hedge funds and other large speculators added dollar longs, or bets that the currency will rise, for an eighth week last week, including against the euro and the yen, the longest stretch since 2010. Net long dollar positions rose to 437,635 contracts in the week ended August 11th, the highest level since the period ended February 3rd, according to the latest data from the Commodity Futures Trading Commission.

- Gold headed for its biggest weekly gain since January as losses in global equities sparked demand for a safe haven. With global equity markets faltering and the US Federal Reserve potentially delaying or putting on hold upcoming US rate hike(s), sentiment towards the yellow metal has turned bullish in recent days. Gold has risen as much as 4.5% this week, reaching a six-week high of 1168, before paring the advance (last trading at $ 1,154). Holdings in exchange-traded products backed by gold increased for a second day, the first consecutive rise since June.

- And if the above negative economic news flow was not enough, North Korean leader Kim Jong Un ordered his army this morning to prepare for war after an exchange of fire with South Korea. Kim declared a "*semi-state of war*" along the border and ordered his troops to be combat ready, North Korea's official Korean Central News Agency said

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