Weekly Market Summary

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No Straight Answers to Recent Market Carnage .. Better Ask the Red Indian Chief!!
Fadi Nasser (SVP – Head of Treasury Sales)

One surely ought to start worrying when central bankers hint at having little visibility as to the future direction of financial markets, at a time a top forecasting investment bank (I personally prefer referring to them as the house that always wins!) has abandoned most of its projected top trades for 2016 just six weeks into the New Year !!

That was surely the case in the past 48 hours, as world equities descended further into a bear market, trading to levels last since in mid-2014. Oil pared declines after sliding to its lowest level in more than 12-years amid the highest price volatility since 2009, whilst the Japanese yen's biggest two-week gain versus the US dollar since 1998 (during the Asian financial crisis) raised speculation that the Japanese authorities would soon intervene to weaken it. As to G-7 government bond markets, yields there tumbled close to all-time lows (new record lows for Japanese and UK 10-year bond yields) as the turmoil in global markets triggered a major risk aversion trade and powerful flight to safety (the safety of bankrupt governments!!). Gold climbed to its highest level in a year, nearing bull-market territory as investors sought a haven from tumbling stock markets and as yields plummeted globally. Gold spot prices are up 17% YTD to $1,247.27 an ounce, the highest level since February 2015.

Investors ignored two days of testimony from Fed Chair Janet Yellen, whose indication that the Federal Reserve would not rush to raise the US benchmark rates in the face of global market chaos failed to stem a selloff in risk assets from bank shares to crude oil and emerging-market currencies (maybe that has to do with Yellen's comment that "*the jury is out on whether recent data change the economy views*"). "*Central bank policies and the uncertainty around their effectiveness is the big macro concern right now*," said Leo Grohowski, who helps manage more than $184 billion in client assets as chief investment officer of BNY Mellon Wealth Management in New York. "*There is a large disconnect right now between what the Fed might do and what they are saying and what the market is expecting. There is a lot of Fed uncertainty back on the table reminiscent of late last summer.*"

Goldman Sachs to Clients: Whoops, We Were Wrong!!

Just six weeks into 2016, the New York-based investment bank has abandoned five of six recommended top trades for the year. Those recommendations included a strengthening US dollar versus a basket of euro and yen, convergence between yields on Italian bonds and their German counterparts and rising US inflation expectations throughout 2016.

The messes underscore the volatility that has beset global markets, accelerating price swings across currencies, stocks and bonds. Signs the world economy is suffering amid a slowdown in China have fueled unease about the credit worthiness of banks and other corporations, spurring a bid for haven assets such as the yen and the euro. "*Markets have started out this week by aggressively de-risking, apparently owing to fears that the recent slowdown in global growth could descend into recession,*" Charles Himmelberg, GS chief credit strategist, wrote in a note to clients Tuesday. "*Financial credit spreads are spiking, especially in Europe, possibly signaling a reactivation of systemic risk concerns*."

Goldman Sachs closed its call for dollar strength versus an equally weighted basket of the euro and yen on Tuesday, recording a potential loss of about 5%. it also ended a bet on five-year five-year forward Italian sovereign yields versus their German counterparts for a loss of about 5%, Himmelberg wrote in his note. In late January, The NY- based bank was forced out of three of its top picks for the year: A bet on large U.S. banks against the Standard & Poor's 500 Index, a wager on 10-year break-evens, and a call on the Mexican peso and Russian ruble strengthening versus the South African rand and Chilean peso. The latter closed on January 21st for a potential loss of 6.6%. The Bank's one remaining trade is a wager on a basket of 48 non-commodity exporting companies versus a basket of 50 emerging-market bank stocks. That is trading 4.5% above its opening level in November.

Whilst our calls on markets have proven to be similarly poor in past months, we remain amongst the few who pointed out repeatedly - over the past year and a half - that central bankers had not learned a single lesson from the 2007/2008 market crisis and were becoming more stuck in traps from which it will be difficult to exit without a sharp market reaction! (Refer to our May 2015 economic piece "*The New Market Normal: Surreal Events That Keep Recurring*").

Which brings me to the final question for the day: What's next for financial markets? Plummeting oil prices and fears about China and financial stocks have turned trading rooms' screens red around the world. But are markets about to stabilize or is the worst yet to come?! Given current low market visibility and numerous surrounding uncertainties, the following exciting and short story might provide the perfect clue:

"It was autumn, and the Red Indians asked their New Chief if the winter was going to be cold or mild. Since he was a Red Indian chief in a modern society, he couldn't tell what the weather was going to be. Nevertheless, to be on the safe side, he replied to his Tribe that the winter was indeed going to be cold and that the members of the village should collect wood to be prepared. But also being a practical leader, after several days he got an idea. He went to the phone booth, called the National Weather Service and asked 'Is the coming winter going to be cold?' 'It looks like this winter is going to be quite cold indeed,' the weather man responded. So the Chief went back to his people and told them to collect even more wood. A week later, he called the National Weather Service again. 'Is it going to be a very cold winter?' 'Yes,' the man at National Weather Service again replied, 'It is definitely going to be a very cold winter.' The Chief again went back to his people and ordered them to collect every scrap of wood they could find.

Two weeks later, he called the National Weather Service again. 'Are you absolutely sure that the winter is going to be very cold?' 'Absolutely,' the man replied. 'It's going to be one of the coldest winters ever.' 'How can you be so sure?' the Chief asked. The weatherman replied, 'The Red Indians are collecting wood like crazy.' "

Unfortunately, that is how Bond, Equity and Commodity markets work nowadays!!

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