Weekly Market Summary

6th of Nov 2015

It is Confirmed! The Federal Reserve Will Raise US Short Term Rates on December 16th ….. Unless God Decides Otherwise!! Fadi Nasser (SVP – Head of Treasury Sales)

Back in late 2005, and whilst meeting a Palestinian delegation during the Israeli-Palestinian summit at the Egyptian resort of Sharm el-Sheik, US President George W. Bush claimed he was on a mission from God when he launched the invasions of Afghanistan and Iraq (?!).

One of the delegates, Nabil Shaath, who was Palestinian foreign minister at the time, recalled: "President Bush said to all of us: *'I am driven with a mission from God'. God would tell me*, *'George go and fight these terrorists in Afghanistan'*. And I did. And then God would tell me *'George, go and end the tyranny in Iraq'. And I did.*" Mr. Bush went on: "*And now, again, I feel God's words coming to me*, *'Go get the Palestinians their state and get the Israelis their security, and get peace in the Middle East*'. *And, by God, I'm gonna do it*." (Tough luck on that one George!).

Fast forward to November 2015: The US Federal Reserve's most powerful trio – in various testimonies/speeches throughout this week – kept a 25 bps rise in the o/n Fed funds rates firmly on the table at their upcoming December 16th FOMC meeting.

On Wednesday afternoon, Federal Reserve Chair Janet Yellen and New York Fed President William Dudley both said the central bank could boost interest rates as soon as next month, while Fed Vice Chairman Stanley Fischer voiced confidence that inflation is not too far below the central bank's goal. "*At this point, I see the U.S. economy as performing well*," Yellen said on Wednesday in testimony before the House Financial Services Committee in Washington. If economic data continue to point to growth and firmer prices, a December rate hike would be a "*live possibility*," she added. Speaking in New York hours later, Dudley said he agreed with the chair, but "*let us see what the data shows.*" Fischer did not comment on the timing of liftoff, but said that price pressures will move toward the Fed's target.

The Federal Open Market Committee (FOMC) said in its October statement that it will consider raising rates at its "*next meeting*," citing "*solid*" rates of household spending and business investment. The comments from Yellen, Dudley and Fischer, who are considered the three most influential members of the Committee, reinforced the idea that next month is in the crosshairs for an increase if economic progress holds up.

Still, Yellen cautioned that no decision had yet been made on the timing of a rate increase. The Fed chair was appearing before the House committee to testify primarily on the Fed's supervision and regulation of financial institutions. "*What the committee has been expecting is that the economy will continue to grow at a pace that is sufficient to generate further improvements to the labor market and to return inflation to our 2% target over the medium term*," she said.

Markets have interpreted Yellen's remarks as a sign that a rate hike in December is more likely. In the past 48 hours, investors have raised to almost 60% the probability of a rate increase by policy makers' December meeting, according to pricing in the Federal funds futures market. That compares to 32% probability just weeks back, assuming the effective funds rate would average 0.375% after liftoff. As a result, the US dollar has strengthened further, trading near the strongest levels since at least August versus the Euro (1.0870 last) and the Japanese yen (121.95 last).

Nonetheless, one US politician seems to strongly disagree! Janet Yellen can stay on God's path by waiting until springtime to raise interest rates, Brad Sherman told the Federal Reserve chair on Wednesday. "*God's plan is not for things to rise in the autumn, as a matter of fact, that is why we call it fall, nor is it God's plan for things to rise in the winter, through the snow*," Sherman, a Democrat from California, told Janet Yellen during the House Financial Services Committee hearing. "*God's plan is that things rise in the spring. And so if you want to be good with the Almighty, you might want to delay until May*." Sherman more seriously went on to say that he is worried about the risks if the Fed lifts off too early and then has to return to zero, among other issues. While his comments were a little more colorful than the typical rationale for postponing liftoff, they underline an important point: the Fed Chair is coming under Congressional and political pressure as the Fed inches closer to raising rates.

A decidedly dovish Bank of England ("BoE") was the other big theme yesterday, raising questions about a possible pushback in hike expectations - up until the second half of 2016 at the earliest. The Bank of England kept interest rates unchanged (0.50%) by a vote of 8-1 at its meeting on Thursday, as weak inflation make the timing of a first increase ever more uncertain. The meeting was closely watched as Bank of England Governor Mark Carney had previously mentioned the end of the year will bring more clarity as to when rates will rise. The minutes to the meeting – released with the rate announcement - showed policymakers believed the near-term outlook for inflation to be weaker than when last assessed in August, due in part to lower oil prices. In fact, most policymakers assumed that it was more likely than not that inflation would remain below 1% into the second half of 2016 (versus the Bank's target of 2%!). Britain's economic growth remains among the fastest among developed economies and positive domestic economic data in recent weeks has added pressure on policymakers to start raising interest rates. The British pound sold off over a percent versus the Dollar and Euro, and was last trading at 1.5150 and 0.7160 respectively.

This afternoon, all eyes will be on the US October job release* (4:30 pm Bahrain time), given the market's strong belief that the Federal Reserve's decision on whether to keep rates on hold or raise them at its final meeting for 2015 (December 16th FOMC meeting) will hinge in large part on that crucial economic indicator. As always, welcome to random number generator, also known as US Non-Farm payrolls: Bloomberg's consensus is for a 185,000 increase in jobs for the month of October, a slightly lower unemployment rate (5.0% versus 5.1% in September), an unchanged average workweek (at 34.5 hours) and a small pickup in wages (+0.2% MoM/ +2.3% YoY), but it is fair to say that the whisper number (traders' chatter) is slightly higher and closer to +200k increase.

**US employment was later released and snapped back with a vengeance in October, while wage growth accelerated and the jobless rate fell to 5% (lowest since April 2008), boosting the odds that Federal Reserve policy makers will raise borrowing costs next month. The 271,000 gain in payrolls was the biggest this year and exceeded all estimates in a Bloomberg survey of economists (the median forecast called for an increase of 185,000 new jobs)! Average hourly earnings climbed from a year earlier by the most since July 2009 (up 0.4% from the prior month and 2.5% over the 12 months ended in October, the most in more than six years!).*

Disclaimer

It is important that you only use this report if you are the intended recipient of this report and you have satisfied yourself that you are eligible to receive such information. This report is provided to you because you are one of our esteemed customers and have previously shown interest in receiving the type of information contained in this report.

The Treasury and Investment Management department of Gulf International Bank B.S.C. ("GIB") have compiled the information in this report. GIB is incorporated in the Kingdom of Bahrain and is licensed by the Central Bank of Bahrain (the "CBB") as a conventional wholesale bank. GIB's head office is located at Al-Dowali Building, P.O. Box 1017, 3 Palace Avenue, Manama, Kingdom of Bahrain.

This report is intended for the accredited investors, as defined in the Investment Business Code of Conduct published by the CBB. This information has not been reviewed by the CBB or any other regulatory authority in any jurisdiction and neither CBB nor any other regulatory takes any responsibility for the correctness or accuracy for the information contained in this report.

The information contained herein is not directed at or intended for use by any person resident or located in any jurisdiction where (1) the distribution of such information is contrary to the laws of such jurisdiction or (2) such distribution is prohibited without obtaining the necessary licenses or authorizations by the relevant branch, subsidiary or affiliate office of GIB and such licenses or authorizations have not been obtained. The recipient of such information is responsible for ensuring that this information has not been received by it in breach of laws and regulations of any jurisdiction.

This report contains publicly available information only, which has only been complied by GIB. The information provided herein is on "as is" and "as available" basis and without representation or warranty of any kind. GIB hereby disclaims any representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability, fitness for any particular purpose or non-infringement of any of such information. In no event shall GIB or its subsidiaries, affiliates, shareholders or their directors, officers, employees, independent contractors, agents and representatives (collectively, "GIB Representatives") be liable (1) for any inaccuracy, delay, loss of data, interruption in service, error or omission or for any damages resulting there from, or (2) for any direct, indirect, incidental, special, compensatory or consequential damages arising from any use of information or arising from any error (negligent or otherwise) or other circumstance or contingency within or outside the control of GIB or any GIB Representative, in connection with or related to obtaining, collecting, compiling, analyzing, interpreting, communicating, publishing or delivering any such information. The information here is, and must be construed solely as, compilation of information (unless expressly stated otherwise) and not statements of fact as to credit worthiness or recommendations or opinions of GIB.

This report does not provide individually tailored investment advice. Any materials contained herein have no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. The document is provided for information purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. GIB makes every effort to use reliable, comprehensive information, but we do not represent that it is accurate or complete. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the materials, nor are they a complete statement of the securities, markets or developments referred to herein. Recipients should not regard the materials as a substitute for the exercise of their own judgement. Any opinions are subject to change without notice and may differ or be contrary to opinions expressed by other business areas or groups of GIB as a result of using different assumptions and criteria. GIB is not under any obligation to update or keep current the information contained herein.

The value of, and income from, your investments may vary because of changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of companies or other factors. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realised.

The information contained in this report is just for informational purposes. Information does not constitute a solicitation, an offer, or a recommendation to buy or sell any investment instruments, to effect any transactions, or to conclude any legal act of any kind whatsoever. GIB does not intend to provide investment, legal or tax advice through this report and does not represent that any securities or services discussed are suitable for any investor. When making a decision about your investments and business, you should seek the advice of professional advisors.

The report may contain statements that constitute "forward looking statements". While these forward looking statements may represent GIB's judgment and future expectations, a number of risks, uncertainties and other important factors could cause actual developments and results to differ materially from GIB's expectations. GIB is under no obligation to (and expressly disclaims any such obligation to) update or alter its forward-looking statements whether as a result of new information, future events, or otherwise. The historical information is provided for information purposes only. Performance figures are calculated before tax (if any) and after deducting ongoing fees and expenses. The performance figures are historical and past performance is not necessarily an indication of future results. Certain amounts (including %ages) included in this document may have been subject to rounding adjustments. Accordingly, figures may not be an exact arithmetic aggregation of the figures to which they relate. The values and forecasts shown represent our current indicative valuations and forecasts of the relevant transactions, currencies, interest rates, commodities or securities as at the date shown. Any value or forecast shown herein is not an indicative price quotation. We expressly disclaim any responsibility for the accuracy of the values or forecasts shown, any errors or omissions in the report

With the exception of information regarding GIB and save as otherwise specifically indicated, the information set out in this report is based on public information. We have, where possible, indicated the primary source of information. We strongly recommend the recipients consult the primary source of information. Facts and views in this report have not been reviewed by, and may not reflect information known to, professionals in other GIB business areas.

This Report, and the information contained herein (save to the extent that such information is publicly available) is confidential and may not be disclosed by you to any other person outside of your organization without our consent.