Weekly Market Summary

20th of Nov 2015

Hurrah To All Fed Promises and More!! Fadi Nasser (SVP – Head of Treasury Sales)

Despite a light risk-off session earlier on Monday - on the back of last weekend's terrorism events – markets have reacted with some calm to both increased global geopolitical tension and hawkish FOMC minutes. Specifically, the minutes of the October Federal Open Market Committee – released on Wednesday evening – pointed to a Fed still on course to raise rates at its December 16th FOMC meeting. *"Most participants anticipate that, based on their assessment of the current economic situation and their outlook for economic activity, the labor market, and inflation, conditions could well be met by the time of the next meeting. And while no final decision has been made, it may well become appropriate to initiate the normalization process at the December FOMC meeting*".

Those comments were echoed overnight by Federal Reserve Vice Chairman Stanley Fischer who said the US central bank has done its best to prepare international markets for its first interest rate increase since 2006 (while again reiterating that no decision has yet been made about the precise timing of liftoff!)."*In the relatively near future probably some major central banks will begin gradually moving away from near-zero interest rates*," Fischer told the Asia Economic Policy Conference at the Federal Reserve Bank of San Francisco. "*We have done everything we can to avoid surprising the markets and governments when we move, to the extent that several emerging market (and other) central bankers have, for some time, been telling the Fed to 'just do it*.'"

Whilst the Fed has been very determined to convince everyone that a December rate hike is coming (on balance, the market is now more or less where the Fed wants and needs it to be prior to its first rate hike in 9-1/2 years), the bond market focus has now shifted to central bankers' assertions that the expected path of the Federal funds rate, rather than the exact timing of the initial increase, will be the determining factor affecting the outlook for growth and inflation, in turn influencing financial conditions and asset prices going forward. In that respect, The Fed Committee reiterated its expectation that, even after employment and inflation are near mandate-consistent levels, economic conditions may, for some time, warrant keeping the target Federal funds rate below levels the Committee views as normal in the longer run.

A number of FOMC participants have stated in past weeks that short-run rates would rise "only gradually" and remain below levels that had been considered normal during previous expansions. "*My best answer – with respect to a gradual pace of policy tightening – is that it does not occur at every meeting. Beyond that, it is difficult to predict what that would look like exactly*", Atlanta Fed President Dennis Lockhart –a voting member on the FOMC this year– said yesterday

(We wonder whether the Fed has a clear vision for an exit strategy?! Or at least has learned lessons from previous policy errors - namely a late start, a slow and predictable pace of rate hikes between early 2004 and mid-2006 that led to various asset bubbles developing over the years and ultimately popping in 2007, the final outcome being one of the worst financial crisis - 2008 & 2009- the world has witnessed!).

One thing is certain: Rising equity and fixed income market valuations - with Treasury, mortgage and corporate bond yields and spread returning towards lows witnessed last winter – at a time central bankers are opting to move slowly on rates, is a sure recipe for overvalued asset markets that will cause more problems when they eventually adjust to economic reality at some point down the road. History has shown the markets' animal spirits need taming before a hard fall and therefore central bankers should always be able to remind investors that they are being too complacent in thinking there are no imminent rate hikes! That would assume central bankers' ability to surprise markets and proceed at times with unexpected monetary adjustments (and most importantly getting away from this perfectly telegraphed profile for rates that did major damage in 2006 and in the NASDAQ bubble of 1999!).

Latest Fed Projections / Market Pricing*

Federal Fund Rate Projections (Fed Dot Plot)

Time	2015 Year-End	2016 Year-End	2017 Year-End	2018 Year-End
September 17th FOMC Meeting	**0.375%**	**1.375%**	**2.625%**	**3.375%**
June 17th FOMC meeting	0.625%	1.625%	2.875%	
March 18th FOMC Meeting	0.625%	1.875%	3.125%	
Current market Pricing (Based on IR Futures)	**0.29%**	**0.83%**	**1.34%**	**1.68%**
*Difference between latest Fed projections & Current Market Pricing**	*8.5 BPS*	*54.5 BPS*	*128.5 BPS*	*169.5 BPS*

**Clearly shows the market's "disconnect" or "little trust" in Fed projections , despite several warnings by various Fed governors over the past weeks that market participants continue to underestimate the future path of Fed fund rates (so far the Fed dot plots have been drifting lower, slowly converging to market pricing!).*

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.