Weekly Market Summary

30th October 2015

Want to be Surprised?! Start Tracking Financial Markets

Fadi Nasser (SVP – Head of Treasury Sales)

At a time when many traders start looking to wind down positions as the year comes to an end, central bankers continue delivering surprises!

Over the past 10 days alone, we have had a dovish surprise from the European Central Bank, a surprise rate cut from China and hawkish surprises from the US Federal Reserve and the Bank of Japan!

All these unexpected developments are summarized below:

- **The European Central Bank (ECB)** left monetary policy unchanged at its October 22nd meeting, as the ECB President Mario Draghi said the central bank will investigate fresh stimulus to boost the economy and that options include a further reduction in the deposit rate (currently at -0.20%). "*The degree of monetary-policy accommodation will need to be reviewed at our December meeting when new macroeconomic projections will be available,*" Draghi said. "*We want to be vigilant, as people used to say in the old times".* One factor officials must weigh is the timing of the Federal Reserve's first increase in interest rates since 2006. Draghi and his colleagues frequently say the ECB and Fed are on diverging paths: Should the U.S. central bank delay tightening because of the slowing global economy, that would put upward pressures on the euro currency, in turn compelling the ECB to ease further.

- **The US Federal Reserve -** as widely expected – left rates unchanged at its October 28th FOMC meeting. However the Fed did take a step back towards possibly hiking at the December 16th meeting by removing one of the additional barriers it inserted in September. By omitting the reference to "*global economic and financial market developments could restrain activity and put downward pressure on inflation*", the Fed sounds less concerned about the global and financial backdrop than in September, although it continued stating that it was "monitoring" global economic and financial conditions. Also, the statement left the Fed's assessment of economic growth intact at "moderate", at a time many market analysts felt there was a chance that this would be downgraded to modest following the Beige book and a string of largely disappointing data releases. There remained one dissenter (Richmond Fed President Jeffrey Lacker) in favor of an immediate rate hike. The Fed is still looking to see "some" further improvement in the labor market and "reasonable" confidence that inflation is moving back to target before it starts raising rates (October job and inflation reports will be released on November 6th and 17th respectively).

- **Chinese policymakers** cut interest rates on October 30th and took further measures to support lending as policymakers stepped-up efforts to stimulate the economy. The People's Bank of China said the country's benchmark one-year lending rate would be cut by 0.25% to 4.35%, while the one-year deposit rate will also drop to 1.5% from 1.75% (all changes effective Saturday 31st October). Additionally, the PBoC cut the reserve requirement ratio (RRR) for all banks by 50 basis points to 17.5%, with an extra 50 basis point reduction for some lenders. Global stock markets were bolstered by the move, which analysts said was a sign that the world's second largest economy was doing more to meet its growth target of "about 7%" this year. Official figures this week showed China grew at the slowest pace in six years in the third quarter. Gross domestic product (GDP) rose by 6.9% between July and September compared with a year earlier. While this was higher than the 6.8% forecast by economists, it represented the weakest expansion since early 2009. China has now cut rates six times since last November.

- **The Bank of Japan (BoJ)** refrained from action - at is monetary policy meeting on October 30th - voting instead by a majority (8-1) to keep the current pace of annual asset purchases as is at ¥80tn. The BoJ's decision came despite another fall in prices in Japan. Headline inflation slowed two-tenths in September to 0.0% yoy (as expected) and to the lowest level now since May 2013. The core (ex-fresh food) stayed at -0.1% yoy and the core-core (ex food and energy) rose one-tenth to +0.9% yoy. BOJ Governor Haruhiko Kuroda defended the decision to keep policy unchanged, saying that the central bank is not losing credibility and that its actions so far - implementing an unprecedentedly large monetary stimulus program - are having the intended effects. The timing of reaching the inflation target – which past postponed – highly depends on oil, Kuroda told reporters in Tokyo. He also reiterated that the BOJ would not hesitate to adjust policy if necessary.

Disclaimer