Weekly Market Summary

November 18th, 2016

A Deepening Bond Rout and Strengthening US Dollar .. Not to Mention a Confirmed US Rate Hike in December!

Fadi Nasser - Head of Treasury Sales

Bonds Tumble in excess of US$ 1Trillion as President-Elect trump Seen as Game Changer

The USD index hits a 13-year high, supported by more aggressive pricing of Fed rate hikes

The above breaking headlines – in past days – have raised serious concerns amongst investors & hedge fund managers, at a time the financial community - at large - was positioned for a narrow Clinton victory on November 8th and hence little price movements thereafter (i.e. status quo maintained) . And whilst FX and equity markets quickly regained their footing on Wednesday 9th - apparently concluding that a Donald Trump presidency might not be so bad after all, given its positive implications on fiscal policy and deregulation of the financial industry (repeal of the Dodd-Frank financial reforms) - bond markets continued their sharp sell-off (lower prices = higher yields) on expectations that Mr. Trump's campaign promises – if carried out – would lead to higher growth and inflation in coming years. Those promises would include easing capital requirements on financial institutions, tax cuts, new trade agreements and tariffs and more importantly large spending on infrastructure projects.

As of this morning, UST 10-year Treasury yields are up another 3 basis points, last trading at 2.33% (as a reminder, yields were hovering closer to 1.80% prior to the November 8th US presidential election, and originally dipped to 1.71% when polls started suggesting a Trump win!). That would be the steepest two-week loss for bonds in at least 26 years, as President-elect Donald trump sends inflation expectations surging. The difference between yields on U.S. 10-year notes and same-maturity Treasury Inflation Protected Securities (TIPS), a gauge of trader expectations for consumer prices over the life of the debt, has now risen to 1.97%, the highest level since April 2015 (from slightly under 1.50% just one month back). Ten-year Treasury yields will be 2.50% to 2.75% a year from now if Trump pushes through his proposed tax cuts and fiscal-spending policies, said Michael Kushma, chief investment officer for global fixed income at Morgan Stanley Investment Management (I am guessing that is the same chap at MS who was forecasting 1.50% on 10s UST yields just a while back!).

Elsewhere, the US dollar index climbed to fresh 13-year highs on similar expectations that President-elect Donald Trump's policies will boost US growth and deliver tighter monetary policy (higher yields). The dollar index, a measure of the US currency against a basket of global peers, has rallied to 101.20 this morning - its highest since March 2003 - and is eyeing a 10th straight day of gains, which would be the longest winning streak since 2012. Among developed economy currencies, it is the Euro and Yen that have been notably impacted by the greenback's bounce. The single currency is down to an 11-month low of $1.0582, and suffering its longest losing streak. The Japanese Yen is softer at ¥110.90, its weakest since May, having lost more than 5% since Mr. Trump's election. Some traders are warning that the US dollar bounce looks now very stretched. The Dollar/Yen's 14-day relative strength index, a closely watched momentum measure, is 80.5, well past the dollar "*overbought*" territory threshold of 70. Similarly, the euro/dollar RSI is 22.0, where

any point below 30 suggests the Euro is "*oversold*" (though no one is suggesting here that an overbought or oversold market can't go further into overbought or oversold territory!). Weekly Market Summary
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Another boost for the US Dollar could come on the heels of the upcoming 25 bps rate hike in the US Fed funds rate at the December 14th FOMC meeting (though such outcome should be largely priced in by now!). Speaking before the Joint Economic Committee of Congress yesterday afternoon, US Federal Reserve chairwoman Janet Yellen made it clear that the central bank remained likely to raise its benchmark interest rate at its last meeting for 2016. A rate increase, Yellen said, "*could well become appropriate relatively soon*." The Fed chair added that it was too soon to predict the economic impact of Donald Trump's election as the next President of the United States. Despite repeatedly calling for Congress to join the Fed in its efforts to lift the economy from prolonged doldrums in previous appearances, Yellen suggested this time that the celebrations were premature. "*We don't know what is going to happen…There is a great deal of uncertainty*." Ms. Yellen also set to rest questions about her own plans, with her term as chairwoman ending in February 2018. "*It is fully my intention to serve out my term*," she noted!

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