Weekly Market Summary

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A Lot of Breaking News … But Little Surprises! Markets Remain in a Wait-and-See Mode

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Following rollercoaster market sessions in April - that saw US stock and bond futures trading in wild & wide ranges - investors have resumed their calm this week, brushing off the latest round of market news (*both True & Fake!*). Markets have mostly remained steady, with uncertainty over the future of the Iran nuclear deal – i.e. further clarity on US president Trump's position re the 2015 international nuclear deal that assisted in easing sanctions against Iran in return for curbs on its nuclear activities - helping to keep prices for various asset classes confined to narrow ranges.

Despite this tranquil and positive backdrop, there are an unusual number of potentially high-impact economic (starting with US payroll this afternoon) and non-economic (May 12th deadline for Trump's decision on the Iran nuclear deal, ongoing Mueller investigation, Syria & North Korea's fast changing landscapes) risks that threaten economic stability, the high asset valuations (for both fixed-income and equity markets) as well as the persistence of market complacency (in other terms low levels of volatility).

Till "*something bad*" happens (fingers crossed it won't, though it is safe to anticipate future disasters when the White House chief of staff John Kelly portrays himself as the lone safeguard against catastrophe, curbing the erratic urges of an "idiotic" president who has questionable grasp on policy issues and the functions of government ; *Kelly has called these recent NBC News allegations "total BS", whilst Trump noted that "the White House is running very smoothly"*), we summarize below important - at times curious - news headlines & developments over the past week:

- ***North & South Korean Leaders Finally Meet, Declare End to War:*** It's Over! The leaders of North & South Korea have pledged to end the formal state of war that has persisted between their nations for almost 70 years on an extraordinary day of diplomacy. At a historic summit last week, decades of war and distrust between the two countries were briefly put to one side as Kim Jong Un made the first visit by a North Korean leader to the South and was effusively welcomed by his southern counterpart, President Moon Jae-in. The meeting marks the culmination of rapid diplomacy that has taken the two Koreas from the edge of war to discussing peace within four months (most likely taking the US administration by full surprise!). The two leaders agreed to gradually reduce weapons on both sides, and push for meetings with the US and China to declare the official end of the 1950-1953 Korean war and replace the armistice with a peace treaty. "*We solemnly declare to our 80 million people and the world that there will be no more war on the Korean peninsula and a new era of peace has begun*," they said in a joint statement after the summit, only the third such meeting between leaders of the North and South. "*It is our urgent historic assignment to put an end to this current abnormal state of ceasefire and establish a peace regime*," both leaders added. At a White House meeting with German chancellor Angela Merkel last Friday, Mr Trump hailed the historic meeting, saying: "*This is going to be a great thing for the world*." He added that he was still planning to meet Mr Kim in the next few weeks: "*Hopefully we're going to have great success.*" (*And the Nobel Peace Prize for his work on North Korea - not to forget his wise tweets relating to the "short and fat Rocket Madman" - goes to Mr. TRUMP!!*)

- ***A Boring FOMC Meeting***: Fed officials – meeting on May 2nd – unanimously decided to leave interest rates unchanged at 1.50% - 1.75%, and this week's timetable allowed for no press conference to explain a further rise. But they did lift their assessment of inflationary trends! In what contained relatively few changes, the FOMC noted that inflation has moved close to its target and is expected to run near 2.0% over the medium term. If one word stands out in the text, it is the reference to the committee's "*symmetric*" 2% inflation objective. In other words, policymakers are wary that PCE inflation could run a little hotter than their 2.0% target over the remainder of the year, and appear to be trying to tamp down expectations that such a run would warrant a materially faster pace of rate hikes. Wednesday's announcement did not do anything to warn that a rate hike was imminent in June, but market expectation remains that accelerating growth readings in the near future would be enough to justify another move then. The lack of any firm commitment to a near-term rate hike has seen yields drifting slightly lower (10-year UST last at 2.94%), whilst not providing any meaningful support to US stocks.

- ***Mnuchin Sees Solid Treasuries Demand Amid Record U.S. Borrowing*****:** Just when we were done clarifying – in last week's market summary - the damaging impact (on bond prices) caused by a deadly combination of record US budget deficits (over many years to come) and reduced Fed Treasury holdings (i.e. a shrinking central bank balance sheet), U.S. Treasury Secretary Steven Mnuchin stated he was unconcerned about the bond market's ability to absorb rising government debt, after his department said it borrowed a record amount for the first quarter. "*It's a very large, robust market -- it's the most liquid market in the world, and there is a lot of supply*," he said in a Bloomberg TV interview on Monday. "*But I think the market can easily handle it*." Earlier that same day, the Treasury said net borrowing totalled $ 488 billion from January through March, a record for that period and about $ 47 billion more than it had previously estimated. "*By definition supply and demand will equate*," Mnuchin added. [One can only hope it will always equate, or otherwise goodbye repayment of American sovereign debt! ☺]

- ***The Rise & Fall of UK May Interest-Rate-Hike*****:** Expectations for a Bank of England interest-rate increase on May 10th have gone full circle – from an outside bet to a sure thing and then back again. Investors and banks have been regularly revising their calls for a May move (short term rates have been kept unchanged at 0.50% since November 2nd 2017, the last time they were raised by 25 bps). Bets for a pending rate rise gathered pace in early February when BOE Governor Mark Carney signalled in a prepared statement that rates needed to rise "*somewhat earlier and to a somewhat greater extent*" than previously thought. At the March monetary-policy meeting, officials acknowledged that markets were pricing in a high chance of a move in May, but made no attempt to question that view. Then policy maker Gertjan Vlieghe added some hawkish comments to the mix, a week after the meeting, and investors' expectations for a rate rise quickly peaked at more than 90% - the same level they reached the day before November's hike. Nonetheless, traders' enthusiasm was reversed in April when a deluge of soft economic indicators (weak PMI, wage growth, CPI, retail sales and GDP growth) and dovish market views shared by Carney during a BBC interview dampened expectations for an imminent interest-rate increase (sending the pound tumbling – from $ 1.4375 on April 17th to $ 1.3550 this morning, a "*beautiful*" and swift short trade for the savvy investors!).

- ***US-China Trade Talks:*** Two days of U.S.-China trade discussions ended in Beijing earlier today with an agreement to keep on talking, and little else! China's official Xinhua News Agency reported Friday that both sides reached a consensus on some trade issues, without providing details. They also acknowledged major disagreements on some matters and will continue communicating to work toward making more progress. The U.S. delegation, led by Treasury Secretary Steven Mnuchin, asked China to decrease the trade deficit by at least US$ 200 billion by the end of 2020 compared with 2018, according to a document sent ahead of the trade talks in Beijing that was seen by Bloomberg News. Earlier, Mnuchin said that the U.S. and China had been having a "*very good conversation*," without elaborating.

Whilst China has not indicated any detail on what it was prepared to agree to, a senior official sounded a defiant tone ahead of the meeting, and the state news agency warned against "*unreasonable demands*." During the second day of discussions, across town at Beijing's Great Hall of the People, President Xi Jinping indicated China will continue to embrace globalism, saying it wants to actively take part in world governance. Those who reject the world will be rejected by the world, he said in a speech commemorating the 200th anniversary of Karl Marx's birth.

- ***Netanyahu Discloses "Significant" Development on Iran:*** Israeli Prime Minister Benjamin Netanyahu said his country has proof Iran had a secret program to build nuclear weapons, citing what he described as Iranian documents that could help tip President Donald Trump's hand when he decides whether to pull the U.S. out of the Iran nuclear deal. Effectively, president Trump has now the chance to scroll through 55,000 pages of material on project Amad, a secret nuclear weapons program, as well as shelves filled with binders and compact discs of information before deciding on the future of the region (Some big players don't seem to have learned anything from the days US Secretary of State Colin Powell made false claims with regards to the Iraqi chemical weapons program - in his infamous 2003 speech to the United Nations - to justify the US "invasion" of Iraq?). "*Iran lied about never having a nuclear weapons program*," Netanyahu added in a press conference in Tel Aviv, and "*didn't come clean*" to the International Atomic Energy Agency, as required by the 2015 deal limiting its nuclear program (sensible words coming from "Bibi" Netanyahu, the man labelled as a crook in a recent Israeli police report sent to the attorney general, Avihai Mandelblitk!).

This afternoon, market focus will shift to the all-important US payroll release! Bloomberg consensus is for April payrolls to have risen by a strong 192,000 (following a weakfish 103,000 jump in NFP for the month of March). A print in excess of 200,000 would surely seal a 25 bps rate hike for the US o/n Fed funds rate at the upcoming June 13th FOMC meeting (interest rate market already assigning a 90%+ probability for such outcome). As always, it is also worth keeping a close eye on the other important elements of the report, namely the unemployment rate (expected to drop by one-tenth to 4.0% - lowest since December 2000!) average hourly earnings (likely to rise by +0.2% mom & +2.7% yoy, similar to the March print), the participation rate (last at a still depressed 62.9%) and average weekly hours (expected unchanged at 34.5 hours).

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