Weekly Market Summary

January 11th, 2019

A Sharp Reversal in Market Sentiment! How Long Will Current Investors' Optimism Last??

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In my latest weekly write-up, I noted that 2018 was drawing to an end with a big bang! From faltering consumer and business sentiment, to resignations/firing of senior White House officials, a partial US government shutdown and global markets in free fall! Not to forget a US Federal Reserve keen on reverting back to neutral rates & showing its independence - away from political interference and presidential pressures.

Despite this mess, and after having personally witnessed similar mini-crisis over and over again in past years, I suggested that the U.S. economy continues going strong (barring ongoing Presidential noises and White House policy mistakes) and hoped that the US Federal Reserve would stick to their guns in 2019 and run monetary policy in a way that benefits the US & global economy, rather than opt to adjust short and long term rates in a way that benefits greedy investors and rewards deceptive hedge fund managers!

Today, however, anyone returning from short holidays (pick me!) must be rubbing their eyes: A sudden improvement in global risk-sentiment, coupled with fast rebounding equity and commodity prices, has once again brightened market prospects and supported risk-on trading. So, what did change over the past 10 days to support this sharp reversal in investors' mood, at a time various prominent market watchers continue calling for a 2020 global recession??

Patience & Flexibility at the Fed: How quickly the consensus can change! Less than a month back, hawkish comments from Federal Reserve officials appeared to pave the way for further interest rate increases in 2019 and 2020. But so far this year, it seems investors have taken comfort from some slightly more cautious commentary from Fed policymakers. "Patience" is currently the Federal Reserve's new catch phrase, which once again dominated the statements of Fed chair Jay Powell and his colleagues over the past week. St Louis Fed president James Bullard, a new voting member on the board this year, went even further last Wednesday when he suggested the central bank was "*bordering on going too far and possibly tipping the economy into recession*" if it pushed rates up further, according to the Wall Street Journal. The prospect of further rate increases has all but been priced out of the market. The probability of no change to the Fed's target policy rate this year stands at 75 per cent, with a 25% chance for a 25 bps cut in official rates priced for the last quarter of 2019, according to CME Group data based on fed funds futures. At their recent December 19th FOMC meeting, the Fed projected two quarter-point increases for 2019, down from a forecast of three. Additionally, the Fed Chairman has declared that balance sheet reduction, previously said to be "*on autopilot*", was something on which he was now prepared to be flexible. With the Fed now actively managing the divergence of (at least in the US) continued positive economic data and the financial market's pessimistic outlook, this has hit a nerve with the markets - which does no longer have to worry about the US central Bank putting additional pressure on the fragile global economic environment with rash rate hikes.

My guess is that we are still firmly in a world of asymmetric monetary policy where the central bank stabilises plunging markets while refraining from pricking bubbles (The long-awaited Jerome Powell Put?? In other words, a Fed pattern of providing ample liquidity as soon as equity markets selloff or a crisis emerges).

A Stellar US Job Report: The US labour market posted a very strong performance last month, with both hiring and wages topping expectations. The 312,000 jobs created in December was well above expectations (market consensus was for 185,000 new jobs) and even more impressive when combined with the 58,000 in positive revisions seen in the prior two months. The participation rate rose to 63.1%, the highest rate since 2017, but that meant that the unemployment rate ticked up to 3.9% from 3.7% previously. However, the labour market remained tight as evidenced by the 0.4% advance in wages on the month, which was above expectations and left annual wage growth at 3.2%, matching the cyclical high hit in October. For markets, that report was a reminder that the US economy is on more solid footing than previously thought, and stronger hiring and wages could result in a continuation of robust consumer spending throughout 2019.

Progress in China-US trade talks: The U.S. wrapped up three days of mid-level talks with China in Beijing on Wednesday, noting a commitment by President Xi Jinping's government to buy more U.S. agricultural goods, energy and manufactured products. For its part, China said the meetings were "*extensive, in-depth and detailed*," and laid the foundation for a resolution of the conflict. Investors welcomed signs of optimism from the talks, with stocks rising globally after the two economic powers appeared to inch closer to an agreement. The S&P 500 Index rose to the highest in almost a month (up slightly more than 10% from lows traded on December 24th). Whilst the Chinese Ministry of Commerce confirmed yesterday that the two sides "*implemented the consensus*" reached by the two presidents in earlier talks and discussed both trade and structural issues in the meetings, the office of U.S. Trade Representative Robert Lighthizer said it wants any deal to include "*ongoing verification and effective enforcement*" and the U.S. will decide on next steps after officials report back to Washington. The Trump administration is pushing for a way to make sure China delivers on its commitments in any deal the two nations reach to ensure a lasting truce and fully defuse a trade war that has roiled financial markets and dimmed the outlook for global growth (otherwise, we'll be back scrutinizing Trump's trivial tweets ☹ PLEASE NO!).

Nevertheless, a word of caution before turning overly bullish on markets for 2019! After all, everyone on Wall Street knows strong rallies are common in troubled times. In fact, in eight previous bear markets, the S&P 500 experienced rallies of greater than 2.5% more than 120 times as the benchmark plunged from peak to trough, according to data compiled by Bloomberg. From the collapse of Lehman to the financial crisis bottom in March 2009, the S&P 500 rallied more than 4% on 13 different occasions. Below are some of the disturbing stories we're currently following at our end:

Persisting US Government Shutdown: President Donald Trump abruptly walked out of a White House meeting with Democratic congressional leaders on border security, escalating a bitter stand-off in Washington as the US government shutdown entered its 20th day with no end in sight. Congressional leaders, including Nancy Pelosi, the House speaker, and Chuck Schumer, the Senate minority leader, returned to the White House for more talks on the president's call for a wall along the US-Mexico border. However, the afternoon devolved into partisan bickering and accusation-hurling after both sides refused to cede ground on their positions. On Twitter, Mr Trump confirmed he had cut the meeting short, declaring it *"a total waste of time"*. "*I asked what is going to happen in 30 days if I quickly open things up, are you going to agree Border Security which includes a Wall or Steel Barrier? Nancy said, NO. I said bye-bye, nothing else works*," he wrote. I have the absolute right to do a national emergency if I want. President Donald Trump Outside the White House, Mr Schumer told reporters that Mr Trump had walked out of the meeting after slamming the table, describing Mr Trump's behaviour as "*something unbecoming of the presidency*". Should the shutdown continue through the weekend, it would become the longest US government shutdown on record. A Reuters-Ipsos poll, released on Tuesday, found that a growing number of Americans now blame Mr Trump for the shutdown.

According to the poll, 51% of Americans believe that the president "*deserves most of the blame*" for the shutdown, while 32% believe congressional Democrats do. Worth noting that the US government shutdown deprives markets of key economic data about the state of the US economy at a time when the Federal Reserve has said policy would be particularly "*data dependent*"! (getting very messy ☹).

Weaker-than-Expected End for 2018: As we begin a new year, activity data for the end of 2018 has continued to come in soft, with downside surprises in the US, Eurozone, Japan, the UK, Australia, Asia and Latin America. In the Eurozone, the sharp tick down followed a run of weaker-than-expected data in Germany and France. US activity data also showed an overall negative surprise, following some big downside surprises in ISM Manufacturing and Non-Manufacturing data; Though some of this weakness was partially offset by large upside surprises, such as much stronger than expected Non-Farm payrolls. Even before the December market meltdown, chief financial officers across North America had recession on their minds. In a quarterly report released by accounting and professional services provider Deloitte LLP Thursday, more than half of the CFOs surveyed said they expect a recession in the U.S. by 2020. At the same time, a gauge of the finance chiefs' optimism about their own companies' prospects fell to the lowest level in almost three year (it is notable is that the survey period ended before the worst of the stock rout -- it was conducted from November 7th to November 20th).

Continuing Brexit Saga: The UK House of Commons will vote on Theresa May's Brexit deal next Tuesday, January 15th (or Wednesday, January 16th latest). Beyond that, predicting how events will play out is as hard as ever! Mrs May still looks likely to lose the vote next week, with many Conservative MPs firmly opposed to the backstop arrangement she has agreed. But Downing Street hopes the EU will make some extra concessions between now and next Tuesday - especially over when a trade agreement might be reached. Number 10's hope is that its efforts might reduce the size of the rebellion next week and allow Mrs May to have a further go at getting her deal past the Commons later on. In past days, May has held meetings with Japanese Prime Minister Shinzo Abe in London, with Abe publicly backing May's Brexit deal and offering his "*deepest respect*" for the work his British counterpart has done in securing an agreement with the European Union. "*We truly hope that a no-deal Brexit will be avoided and in fact, that is the whole wish of the whole world*," Abe said at a press conference in Downing Street. "*There is a good deal on the table and for those who want to avoid no deal, backing the deal is the thing to do,*" May said at the press conference.

Last, but not least, worth mentioning that the US President – despite his recent busy schedule - got his revenge on Amazon Inc. founder Jeff Bezos in past days. Mr Trump wished Mr. Bezos luck in his divorce from his wife MacKenzie, predicting the proceedings will be "*a beauty.*" "*I wish him luck*," the twice-divorced Trump told reporters at the White House yesterday as he departed for a trip to the U.S. border with Mexico. "*It's going to be a beauty.*" Trump has a history of publicly attacking Bezos and his company. The president has criticized coverage of his administration by the Bezos-owned Washington Post, and he has pressured the U.S. Postal Service to raise the prices it charges Amazon to ship its packages. Bezos and his wife announced they would divorce last Wednesday. Fortunately for Mrs Bezos, the relationship is ending a little more than a year after her husband became the world's richest person and could leave her with $69 billion if the couple split their fortune equally, making her the world's richest woman! It could also make Microsoft Corp. co-founder Bill Gates, currently worth $92.5 billion, the planet's richest person once again!

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