Friday, November 30th 2012

We had a colorful week... Black Friday, then the Fed's beige book… The former came and went and as Black turned to Beige we found a pickup in consumer spending and steady home sales helped lift economic growth in October and early November in most parts of the United States, according to a Federal Reserve survey released Wednesday. The one exception was the Northeast, which was slowed by Superstorm Sandy. Growth improved in nine of the 12 Fed's regional banking districts, the Fed survey said. Growth was weaker in New York, Philadelphia and Boston — areas where Sandy caused widespread disruptions. The survey noted that growth improved despite nervousness about the "fiscal cliff." That's the name for automatic tax increases and spending cuts that could kick in next year if Congress and the Obama administration can't reach a budget deal before then. This story has motorized the equity markets as each optimistic statement from a prominent Senator added many points to the Dow Jones, a sad face from across the aisle with a negative outlook took these points away. Quite amazing in a way, as we all know that some sort of compromise will be reached and that thereafter, no matter how upsetting such a compromise may be for some, the markets will rise as risk has been reduced… We can see this “profound understanding” in the outlooks for 2013- Literally all Wall Street analysts who offered predictions showed expected significant rises for the Standard & Poors 500 index. Even Dr. Doom Gloom and Boom has offered a positive view on equities (his first ever???)…
Well, maybe not all of them- Roubini, the eternal pessimist, is said to predict a 20% fall by year-end, assuming we even get there- He reminded us that December 21st might be the end of time, as the Mayan prophecy expects the end of the world. Well, if the Mayans are to be proven right, we will never know if Roubini’s outlook had merit, nor would we care ☺
Mayan, Federal cliffs notwithstanding, the markets seem to have found their breath and have regained most of their post-election falls. The Dow is back above the 13’000 level, the NASDAQ above 3’000 and the S&P above 1’400 Risk appetite has come back, with the Euro back over $1.30 and the volatility index [VIX] down to 15, trending down towards its lowest levels.

Oil and Gold have both stabilized into tight ranges, trading at $88 and $1’730 or so.
On Tuesday we hear that the EU has agreed a debt deal with Greece, debt to GDP targets in stages. All good? Well, Italian yields fell to several years’ lows as did other troubled peripheral yields.

US GDP for Q3 was +2.7%, slightly below 2.8% expected level with little impact on markets, as much of the “miss” was attributed to Sandy, hopefully a one-off event…
German import prices drop month on month, up only 1.5% year on year, slower inflation than expected helping to prop up the Euro. In effect, there is little to no inflation anywhere in the industrialized world. In real terms, bond yields are not as low as it would seem…

As we move into December and the festive period, the main topic remains political- The US Fiscal Cliff… "Politics is the gentle art of getting votes from the poor and campaign funds from the rich, by promising to protect each from the other" (Oscar Ameringer, American Socialist Politician).

Currencies

- EURUSD traded in a choppy fashion during the week. The pair started off on a strong foot, rising from 1.2970 to 1.3005, as European finance ministers agreed a €34.4bn aid deal for Greece, which could relieve the country of billions of Euros of debt by the end of the decade. The EUR had since lost ground, dropping over a figure to 1.2880 on fiscal cliff worries and Euro M3 rising more than expected, lowering the likelihood for an additional rate cut in the near future. But EURUSD has since reversed its losses and rallied up to 1.3025, as US lawmakers said they are optimistic that a deal will be reached, avoiding a scenario of automatic spending cuts and tax increases, as well as Mario Draghi's supportive comments on the state of the Eurozone and expectation for a Eurozone recovery by mid 2013.
- EURCHF traded in a tight range of 1.2030 – 1.2050 during the week, causing USDCHF to mirror the EURUSD moves and range 0.9250 – 0.9340 for the week. SNB's Jordan spoke in Bern on Wednesday, stating that the SNB does not expect any inflationary pressures and legitimized the CHF cap against the EUR.
- The Japanese Yen was again in focus this week, with USDJPY seeing some weakness mid week to 81.70 as investors returned to the safety of the Yen and away from the fiscal cliff and Eurozone worries. The Yen fell sharply on Friday morning, with USDJPY making new highs of 82.75, on the back of news that Japan's consumer prices have stagnated in October, raising speculation the BOJ will increase stimulus to spur inflation.
- AUD lost ground during the week, seeing some earlier strength up to 1.0490 against the USD on the back of positive news from Europe. The Aussie has lost ground (down to 1.0415 currently) on news of slowing private business investment, and Australia's trade deficit more than doubling in Q3 due to a slump in exports.
- Cable remained relatively steady, currently printing at around 1.0640. The GBP saw a short-lived weakness (down to 1.5970) on Wednesday in anticipation of BOE deputy governor's comments, which said that further bond purchases are still possible, causing the GBP to reverse earlier losses.
- The BRL weakened, starting the week around at 2.08 against the USD, and has gradually weakened to 2.11 in anticipation for the Central bank's announcement on the Selic rate, where rate was left unchanged at 7.25%. USDBRL later consolidated to 2.0990, on news of likelihood that the Brazilian economy grew at the fastest pace in more than two years, thanks to tax breaks that were implemented to stimulate demand.

Fixed Income

- US yields fell for the week across the board as doubts over Fiscal cliff pushed treasury demand to an 8 year high. US 2 year fell from 0.264% to 0.256%, the 10 year fell from 1.691% to 1.619% and the 30 year from 2.829% to 2.796%.
- Spain 10yr rallied to the highest level since March, pushing yields to as low as 5.20%, on improving prospects for the European financial system. Spain sold €4.09bn of bills on Tuesday, beating its maximum target of €4bn, and by so, selling all the bonds it had planned for the year.

- Italy as well successfully auctioned as much ad €9.5bn of debt during the week, pushing the yield of the 10yr to as low as 4.48%, the lowest rate in two years.
- This week, bonds rallied across the board, with Convertibles, Emerging market bonds and EU sovereigns, being the best performers, rising 0.93%, 0.85% and 0.82% respectively. Leveraged Loans and US sovereigns rose the least (0.24% and 0.26% respectively).

Equities

- Developed equity markets rose this week, with the MSCI World advancing by 0.75%, as of yesterday's close, as rising expectations that US lawmakers will strike a deal to avoid growth-sapping austerity measures lifted the potential for a year-end equity market rally.
- European stocks climbed by 1.11% this week, benefiting from hopes that a deal on Greek debt would be reached (paving the way for 44 billion Euros in rescue loans), which eased near-term risks for struggling Eurozone states, as well as on optimism that US Congress was progressing toward a fiscal agreement that would avert a possible recession.
- US shares rose by 0.48% over the week, boosted by positive economic data and hopes over fiscal cliff talks. On Thursday, the S&P 500 extended gains as GDP grew at a 2.7% annual rate, up from a 2% prior estimate, and as an index of pending home sales climbed 5.2%, exceeding expectations.
- Meanwhile, Japanese stocks advanced by 0.85% for the week, as measured by the Nikkei 225, as optimism over a US fiscal deal lifted sentiment. Also, Japan's exporters regained some ground after a bout of profit-taking on Wednesday, following a recent rally spurred by a weaker yen.
- In terms of sectors, Utility, Industrials and Information Technology led the gains (+1.61%, +1.24% and +1.21% respectively), while Energy, Financials and Telecom lagged (-0.34%, +0.40% and +0.47% respectively).

Emerging Markets

- Emerging Market equities rose by 0.79% for the week, as of yesterday's close. In terms of regions, Latin America was the worst performer (-0.25%), followed by EM Europe (-0.08%) and EM Asia (+1.30%).
- The Shanghai Composite slumped by 2.33% over the week, nearing its lowest level in four years. Paradoxically, Chinese shares slid despite a survey showed that China manufacturing activity expanded for the first time in more than a year, reaffirming an improvement in the Chinese economy.
- Meanwhile, the Brazilian Bovespa rose by 0.48% over the week. The index started the week on a quite negative note, before reversing the trend on Wednesday and rising for two straight days as higher commodity prices boosted the outlook for Brazilian raw-material producers amid optimism over budget talks in the US, Brazil's largest commercial counterpart.

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Commodities

- Commodities dropped by 0.07% this week as of yesterday's close, as measured by the S&P GSCI broad commodity index. Industrial Metals and Agriculture rose strongly over the week (+2.48% and +2.06% respectively), while Precious Metals and Energy were negative (-1.09% and -0.74% respectively).
- Agricultural commodities rose quite strongly over the week, lifted by Wheat and Soybeans. Despite this year's record high prices for soft commodities, global agricultural commodity markets are expected to shift from a squeeze to a surplus in 2013 according to Rabobank's annual commodities outlook. Rabobank predicted that global agricultural prices are likely to advance during the first half of 2013 on tight supplies but weaken during the second half as increased production creates a worldwide surplus.
- Gold fell until Wednesday, before retracing the previous day's sharp fall on Thursday and Friday, as a weaker dollar and renewed optimism that a deal will be reached to resolve the US fiscal crisis boosted appetite for assets seen as higher risk.
- However, the implications of the fiscal cliff for Gold are unclear. Protracted talks – which could heighten risk aversion – may be positive if they spark buying of the metal as a safe haven, but in the short term, hopes for a quick resolution are benefiting Gold as it keeps pace with stocks. The yellow metal currently trades at $1'730 an ounce and seems to hold quite nicely around these levels and as such, it looks that Gold is preparing a new rally which should take us above the 1'800 level shortly.
- Crude Oil futures bounced higher on Thursday on the heels of a three-session losing streak, as optimism over a potential resolution to the US "fiscal cliff" and stronger third-quarter economic growth improved investors' appetite for risk. Crude Oil is about flat for the week and currently trades at $87.90 a barrel.