Weekly Market Summary

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Confused With Recent Events?? Join the Club!!

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Confusion is a symptom that makes people doubt their ability to think clearly and leave them disoriented and unable to express confident views. At times, it is referred to as disorientation, but in its extreme state it is known as delirium! (Trump's doubling down on a previous baseless tweet that Alabama was in the path of Hurricane Dorian, even after being rebuked by the National Weather Service or his other claim that "*I'm not sure that I've ever heard of a Category Five*" (storm) at a time three Category 5 hurricanes have already hit the mainland U.S. or U.S. territories since he was inaugurated as US president would surely qualify him for the latter ☺).

In past months, we did release several weekly economic updates expressing our surprise and amusement at overstretched asset prices. From "*Messy and Irrational Markets.. Perfect Time to Plan a Summer Holiday!*" to "*Are Central Bankers Still in Control as Bond Mania Continues Ahead*" and "*When One Loses Trust in World's Leaders & Faith in Financial Markets",* we argued throughout about complacency and irrational exuberance returning in such a quick fashion to markets that it was starting to look and feel like 2005-2006 - when nothing would upset the rally in both equity and bond markets and where traders' "*buy the dip*" mentality would always prevail (courtesy of central bankers' implicit put!) And whilst financial markets still discount at least two quarter-point Fed interest-rate cuts by year-end - starting with a 25 bps at the September 18th FOMC meeting – we continued stressing that the unprecedented monetary stimulus from global central banks is simply creating a "*fat and slow*" world, dominated by large companies and plagued by a swarm of "*zombie firms*" - those that should be out of business but survive because of rock-bottom borrowing costs. It is also empowering a horde of zombie investors that continue grabbing stocks and bonds at inflated levels (blame it on their "state-of-the-art" automated Algorithmic Trading Systems!)

Nonetheless, just when investors think they have it all figured out, the market can and typically does bite! That surely was the verdict for fixed-income traders over the past 24-hours; After August's historic drop, it was starting to seem like Treasury yields could only fall; And then came Thursday September 5th, when an enormous surge in rates reminded even well-entrenched bulls that the world's biggest bond market is not a one-way street. The trigger? Optimism about the US-China trade war, spurred by the two nations agreeing to hold high level face-to-face talks next month (silly me, thinking those were planned for this month?!); UK opposition lawmakers - supported by Conservative Party rebels – passing a bill that would block a no-Deal Brexit on October 31st and compel UK Prime Minister Boris Johnson to seek a three-month delay to Britain's departure from the EU if an agreement isn't reached by late next month (if your own brother can't back you, why should anyone else? in reference to Jo Johnson, a business minister in his older brother's government, who dramatically quit the government yesterday, saying he could no longer endure the conflict "*between family loyalty and the national interest*"); Easing tensions on the streets of Hong Kong after HK leader Carrie Lam confirmed that she will formally withdraw the Extradition Bill to "*fully allay public concerns*"; And last but not least, stronger-than-expected US data (solid ADP Employment and ISM Services reports).

Whilst most market participants expect the European Central Bank ("ECB") to add more accommodation this month, investors were also disappointed by the growing resistance among European policy makers (mostly German, Dutch and Austrian) to ECB's President Mario Draghi's bid to reactivate the bond purchase program (QE) in Europe. Add to that the less-than-dovish messages sent by central banks in Sweden, Canada and Australia over the past few days, and one would better comprehend the latest sharp sell-off in bond markets. As a result, yields on US two-year notes jumped as much as 14 basis points, the largest full-day increase in a decade, before pulling back to 11 bps. The selloff was also global; For instance, German 10-year rates jumped higher by 10 bps to -0.58%, whilst 30-year rates briefly turned positive after a month under zero! (a sunny day in winter ☺)

Some investors might want to be sceptical that yield increases will continue (the "*doubting*" herd mentality), especially with the double whammy of news later this afternoon: The monthly U.S. jobs report comes out in 2 hours and Fed Chairman Jerome Powell speaks about monetary policy later in the day (7:30 pm Bahrain time), his last comments before the quiet period leading up to policy makers' September 18th rate decision.

With regards to US payroll data*, Bloomberg consensus is for August payrolls to have risen by a healthy 160,000 (following a "similar" 164,000 jumps in NFP for the month of July). It will also be worth keeping a close eye on the other important elements of the report, namely the unemployment rate (expected to remain unchanged at 3.7%), average hourly earnings (likely to rise by a healthy +0.3% mom & +3.0% yoy), the participation rate (expected unchanged at 63.0%) and average weekly hours (projected to bounce back to 34.4 hours, up from 34.3 the previous month). A strengthening of the labour market would dampen the chances of seeing a 50 bps cut by the Fed anytime soon, whilst keeping alive a smaller rate cut later this month. Worth keeping in mind that today's payroll release is poised to present misleadingly robust results due to temporary hiring ahead of the 2020 census (which could boost August total employment, Non-Farm Payroll number, by close to 40,000 jobs – though the Private Payroll data would be unaffected).

**Markets were geared up for a solid payrolls number after the strong ADP report yesterday. As such, the 130,000 jobs gained in August, some 30K below consensus expectations though still broadly in line with the pace of labor force growth, was viewed as a disappointment – particularly because the headline print was flattered by some public sector hiring related to next year's census. While wage growth was a little better than expected on the month, the annual pace hasn't shown any further signs of acceleration, and therefore won't act as an impediment to another Fed cut later this month.*

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