Creative Global Investments

Morning market commentary & charts

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Objectivity

Integrity

Creativity

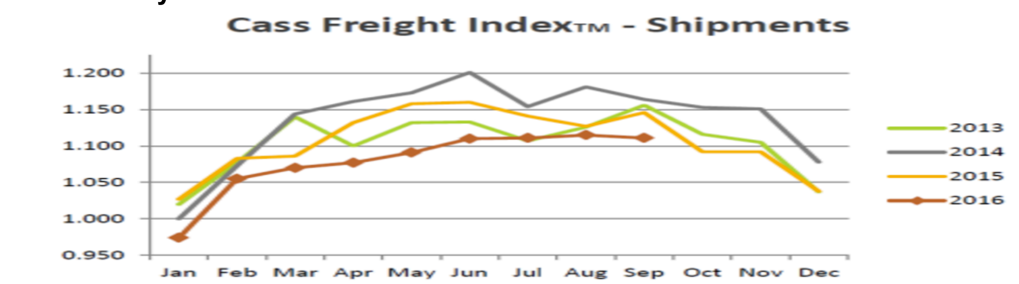
Global Macro Commentary

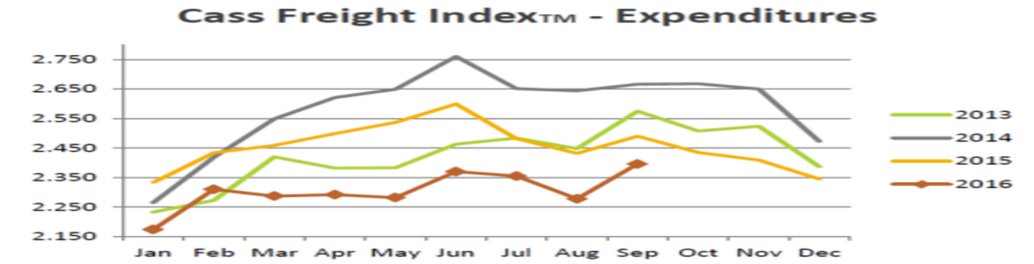
In the Americas, US CPI core inflation fell to 2.2% y-o-y in September from 2.3% y-o-y in August. The Fed's preferred measure for inflation is PCE core inflation, which has been running below the 2% target for 52 consecutive months and the upcoming September figure will make it 53 months. Based on the CPI data, PCE core inflation is likely to have declined back to 1.6% in September after it rose to 1.7% y-o-y in August. When looking at the chart of the 5-year breakeven inflation rate, a bullish setup is emerging. Inflation expectations bottomed earlier this year and has since moved higher, closing in on resistance around 1.6%. The pattern charted over the past couple of years resembles a head-and-shoulders bottoming pattern, the target of which suggests a move to levels above the Fed's target of 2% could materialize.

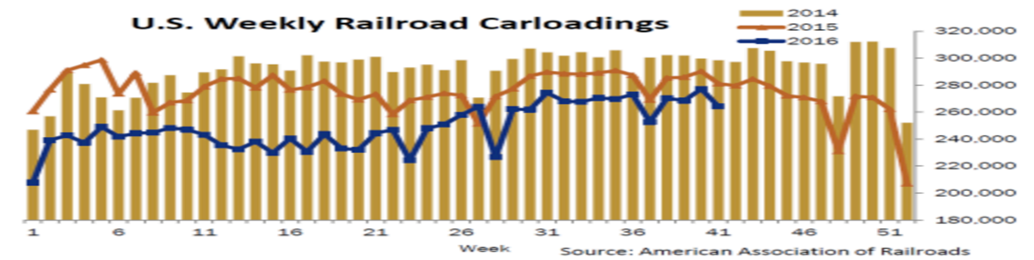
The below-target inflation is the reason why the Fed says the economy has 'room to run', which supports our non-consensus view that the Fed will not hike in December.

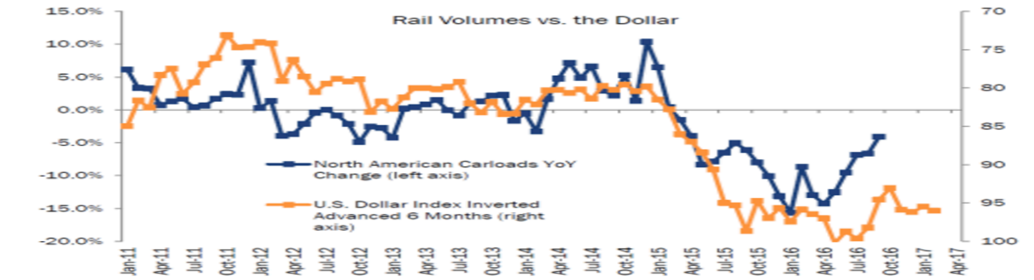
The mythical GDP case build by macro-bulls based on inventories keeps sinking in to the sunset. In particular, auto inventories have soared, and autos have been one of the few bright spots in the economy. Not only the auto sales expectations, but also the overall consumption expectations are too optimistic in our views.

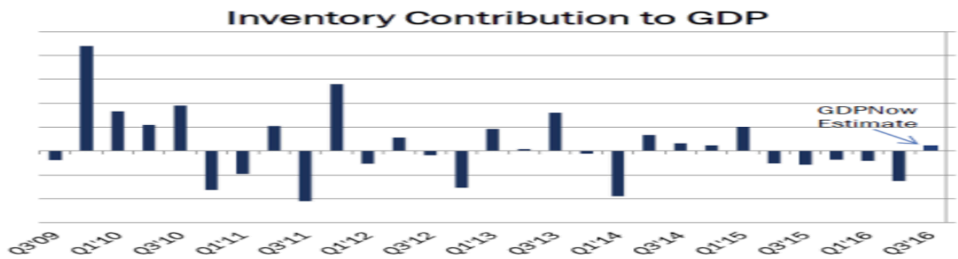
Heading into the Christmas shopping season, the latest reading of the Cass Freight Index shows shipments sank -0.4% for the month and are down -3.1% y-o-y, which leads us to conclude that there are increasing risks towards great holiday sales expectations, i.e. robust Q3 GDP based not only on shipments, but also on many other factors shown below.











Clearly, the US consumer is slowing, as we had been forecasting, and until the November election, which will leave at least half the country in a sour mood, we do not see consumers rush out now and increase spending ahead of the election date. All things considered, things are not shaping up well for Q3 GDP and estimates are falling like a rock, as we were expected in this quarter, and most likely for Q4. **Again, we keep our initial 1.6% GDP growth estimate for 2016 for the US as per our 2016 Global Outlook & Investment Strategy publication since December 2015 (lowest US GDP estimate on the sell-side) although, we see increasing risks for our target to be too high. Clearly, as we had been discussing, the perception of superior US GDP growth in 2016 ended up being just that, a perception, as reality now shows that the US economy in 2016 had likely grown even less than that one of the "Brexit" struck Eurozone.**

So, given the weakening macro picture of the US, then several questions should concern investors:

- Why is there a strong US$?
- Why do the majority of economists still see the FED to hike rates?
- Why are interest rates (government bonds) in the US at a +100bps premia over European equivalent averages?
- Why are US equity market valuations higher by at least 4 to 5 P/E multiple points?
- Why are US equities yielding so much less than European equities, despite a worse macro and currency outlook?

In the UK, September, consumer prices increased 0.2% from the previous month, which came in below the 0.3% increase seen in the previous month. August's figure had marked the highest reading in five months. The increase in September reflected higher prices for clothing, overnight hotel stays and motor fuels. Inflation was 1.0% in September, which was up from August's 0.6% and marked the highest reading since October 2014. The reading came in above the 0.9% expected by the markets. Finally, annual average inflation inched up from 0.3% in August to 0.4% in September, the highest figure in over a year. In August, the Bank of England cut its Base Rate for the first time since March 2009 in order to safeguard the economy and offset some of the negative effects of the Brexit vote. The move will also put upward pressure on inflation. The BoE sees inflation averaging 1.3% in Q4 2016 and 2.1% in Q4 2017. Consensus Forecast expect inflation to average 0.7% in 2016, which is down 0.1 percentage points from last month's forecast. For 2017, the panel forecasts that inflation will average 2.2%

In Asia, China's economic growth steadied in Q3 at 6.7%. The GDP price deflator rose to a two-year high of 1.1%. Retail sales in China were up 10.7%, while urban investment grew 8.2%. The main driver was still the public sector with private investments increasing only 2.5% y/y. Industrial production rose 6.1% y/y below consensus expectations of 6.4% y/y. The Chinese government is aiming for growth of between 6.5% and 7% this year. Despite a rocky start, the economy grew 6.7% in 1H as the government cranked up infrastructure spending and state banks extended a record amount of credit, although credit growth had been slowing as policymakers moving to rein in surging property prices. We see increasing government policy implementation and macro evidence that the recovery is likely to last for more than another quarter or two.

Chart 1: Official GDP & CE China Activity Proxy (% y/y)

Chart 2: Value-added (GDP basis, % y/y)

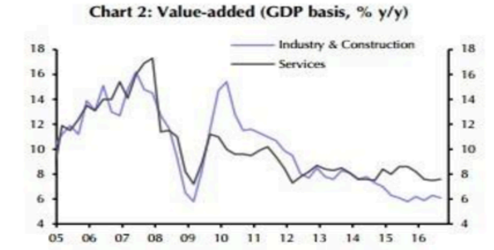


Chart 3: Industrial Value-added & Electricity Output (% y/y)

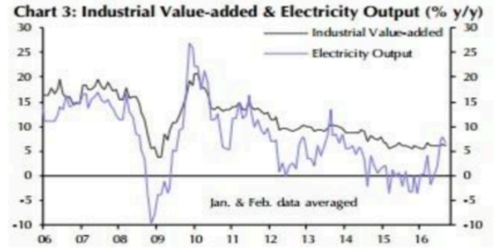


Chart 4: Industrial Output Volumes (% y/y)

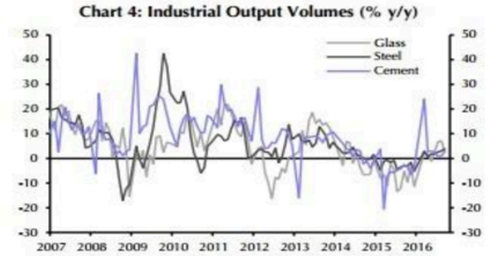


Chart 5: Industrial Output Volumes (% y/y)

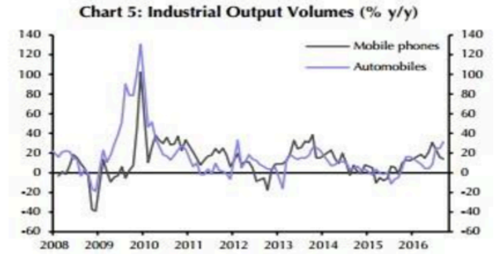


Chart 6: Urban Fixed Investment (% y/y)

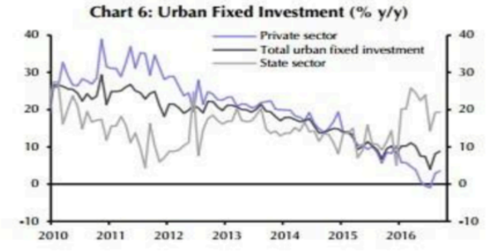
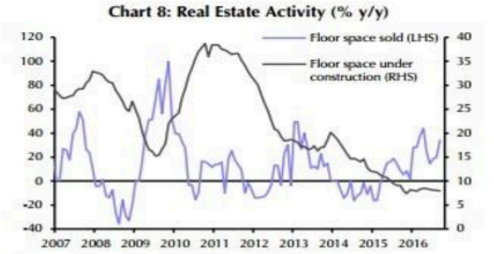


Chart 7: Urban Fixed Investment (% y/y)

Chart 8: Real Estate Activity (% y/y)



Equities Commentary

More technical evidence that the S&P 500 Index reached a seasonal low last Thursday at 2,114.72. Short-term momentum indicators have started to recover from oversold levels. Strength yesterday was triggered by better than consensus Q3 earnings by a wide variety of S&P 500 companies.

We are expecting for continuing strength in Chinese equity markets, particularly after the better than expected GDP and other macro data released for Q3 earlier today.

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