
Weekly Market Summary

28th of October 2016

Are Financial Markets Totally Unprepared for A November US Fed Rate Hike & a Donald Trump Victory?? Fadi Nasser - Head of Treasury Sales

November 2nd ... US Federal Open Market Committee (FOMC) Meeting: Markets currently priced for unchanged policy (15% probability of a rate hike)

November 8th ... US Presidential Elections (58th President of the United States) - Most Polls favoring a Clinton Victory over Trump.

Federal Reserve policy makers are heading into the November FOMC meeting (next Wednesday) with possibly one main objective: Prepare the markets for an interest-rate increase at the December 14th FOMC meeting. Yet, Fed officials will also face the challenge of modulating their action-oriented rhetoric in order to strike a tone that supports December, but does not imply a steeper policy path next year. The latest "*Fed dot plot*," which the central bank uses to signal its policy outlook, anticipates two rate hikes in 2017. Those are surely not cast in stone, and Fed/market sentiment could fluctuate depending on how quickly the economy begins to exhibit characteristics consistent with reaching full employment. Strong 2017 first-half growth and firming wage pressures could pull rate action forward or even put a third hike on the table, which, in turn, would raise the probability of activity around the March, May and September meetings.

In fact, policy makers have in the past shown varying degrees of willingness to let the economy "*run hot*," but their patience could wear thin in the event -- not implausible -- of certain economic indicators outperforming next year. To be sure, the "*dot plot*" shows a broad consensus among meeting participants around a single rate hike by year-end 2016, but there is significant variation in future years. For example, expectations for the Fed funds rate at the end of 2017 essentially span a 150-bp range (from 0.50-0.75% to 2.0-2.25%), and the range is even wider (250 bps) in 2018! At this point in time, gauging the likely timing and pace of rate hikes in 2017 is clearly a fruitless exercise.

Which brings me to the next more critical topic: The November 8th US presidential election is fast approaching and the race between Donald Trump and Hillary Clinton to become the next US President is in its final 10 days, with the election becoming increasingly bitter. The presidential campaign has seen Trump, once a Republican outsider, close the gap on Clinton before falling back after a series of controversies. Most recently, Clinton has been ahead almost continuously in most polls, though history cautions against reading too much into polls, especially that a lot can still change between now and election day (such as Trump remaining silent, usually a plus for his campaign, and the fact that Hillary Clinton remains unpopular both within her party and among the public at large!).

Just 33% of Americans think Clinton is honest and trustworthy, compared to 35% thinking the same of Trump; 57% of people say they do not share Clinton's values, while the number is even higher for Trump, at 62%. More people think Clinton has the right kind of temperament and personality to be a good president, while Trump has the advantage when people pick the candidate who they think could bring about "*real change*" in Washington.

Add to that mix last year's surprise General Election results in the UK (May 7th 2015, where too close to call election polls were followed by an outright majority win for David Cameron and his Conservative party), as well as the June 2016 astonishing BREXIT vote (UK voters unexpectedly voted in favor of exiting the EU), and you have the perfect recipe for having as little faith as possible in pre-elections pollsters.

Last, there will be few other important events/releases to watch in coming days, including this afternoon preliminary 3rd quarter GDP release in the US (expected to be up 2.6% YoY), Spain's parliamentary investiture vote on Saturday (after which caretaker Prime Minister Mariano Rajoy will be set for confirmation to a second term), Bank of Japan monetary policy statement on November 1st, Bank of England's rate decision on November 3rd and US October payroll on November 4th. For my part, I look forward to the first presidential election in my home country – Lebanon - since 23rd April 2014 (such a great achievement!) – scheduled for Monday 31st October, when Lebanon's parliament is expected to elect former army chief Michel Aoun as president, ending a two-year political impasse that has crippled state institutions and deepened rifts among rival factions.

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