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MACRO AND MARKET REVIEW

December 2014

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MACRO REVIEW

In December, notwithstanding the strong US economic data, global growth issues and instability in Russia and Greece, **the main event was the sharp decline in oil prices**, which triggered global concerns over the risks of deflation.

- **Increasing diversity in economic performance**. Way above economists' expectations, the US economy expanded at a 5% annualized pace in the third quarter. The unemployment rate remained steady at 5.8%, while 321'000 jobs were created, up from 209'000 in October, the biggest monthly non-farm payroll gain in nearly three years (accompanied by wage growth). In Europe, the third quarter GDP growth stood at 0.8% year-on-year. In the UK, inflation fell to its lowest level since 2002. Japan's economy contracted -1.9% in the third quarter. Moody's downgraded Japan's credit rating by one notch to A1. China's economic slowdown continued.

- **Major central banks maintained their monetary policy**. The US Federal Reserve dumped its forecast that it will keep low interest rates for a "considerable time" and may tighten monetary policy by the middle of 2015. The ECB lowered growth and inflation forecasts. Less expected was Switzerland's introduction of negative interest rates. To head off inflation and after the ruble suffered its worst drop since 2008, Russia's central bank raised its main interest rate by 650 bps to 17%. In China, the central bank pumped about 400bn Yuan (nearly $65bn) into the country's banking system to boost Chinese banks' lending abilities to spur the economy.

Elsewhere, in Japan, the **large victory of the LDP of Shinzo Abe** (291 out of 475 seats) should allow him to pursue tougher structural reforms. In Europe, the **Greek parliament failed to elect a new president, triggering a snap general election** that could bring the left-wing anti-bailout Syriza party to power.

MARKET REVIEW

In a volatile December with low trading volume and reduced liquidity, financial markets continued to be weighed down by increasing concerns about global growth, falling oil prices, weakness in energy-related credits and instability in Greece.

- **Most equity markets were volatile** and ultimately directionless such as in the US and Japan with the S&P 500 (-0.42%), and the Nikkei 225 (-0.05%) marginally down. In Europe, all markets were down and the MSCI Europe lost -1.45%. Elsewhere, the MSCI World (-1.71%) and especially the MSCI EM (-4.82%) all posted negative returns. While the Shanghai – Shenzhen 300 gained +25.81%, the Russian RTS fell -18.84%. **Volatility re-surfaced**, with the VIX index rising to 19.20, its highest levels since mid-October.

- In fixed income, **top-tier sovereign bonds benefited from their safe haven status**. The yield on the **10-year German Bund reached 0.54%**, the most meagre payout on record, while the UK 30-year GILT reached 2.5% for the first time ever. **In the US, the 10-year Treasury bond was flat** at 2.172, while the **high yield market was hurt** by the weakness in the energy sector. Investment grade credit also lagged. Securitized products such as MBS and CMBS fared better. **European credit spreads widened**.

- In currencies, the **USD strengthened** especially against the EUR (-2.84%) reaching 1.2100, its lowest level since 2012. The Yen weakened (+0.97%) further hitting a seven-year high of 119.78. EM and commodity currencies fell. **The ruble reached an all-time low**, its worst fall since the 1998 crisis.

- In crude oil, the **WTI (-19.47%)** and the **Brent (-18.28%)** fell sharply reaching USD 53.27 and USD 57.33 respectively, levels not seen in the last five years. The Brent fell -50% from USD 115.06 on June 19th. **Gold (+0.76%)** recovered a little at USD1'184.10.

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