

*May 25<sup>th</sup> 2016*

***Markets still in a buoyant mood – Federal Reserve indefatigable – EU is not a free trade agreement – German investors and business people at loggerheads, who is right? European populists are alive and well! Greece shall pay – what about the next time?***

***Markets still in a buoyant mood – flurry of positive news***

*Markets are still in a buoyant mood following the strong showing yesterday. The major drivers include the carry-over from US housing data, stronger oil prices and an agreement on the Greek crisis and rising German business confidence. We are continuing to hear encouraging noises on the UK –EU referendum front, although we need to caution that this could turn on a pin.*

***US international trade in goods shows exports holding. External trade, while not a major support - is not likely to be a major drag on growth.***

***Federal Reserve once again unto the breach!***

*The Federal Reserve has not been remiss to further jump into the fray, with comments from the indefatigable head of the St. Louis Federal Reserve. The tone remains firmly in the lift rates camp. The labor market is again being cited as a catalyst with slower than expected growth the major laggard.*

***This confirms our view that employment and economic growth are no longer synonymous – we are at “full employment” and measured on a financial flexibility basis US consumers are tapped out!***

***US central bank shall do the “heavy lifting” for the ECB***

*With regard to US monetary policy it appears that the consensus estimate is now greater than 50 per cent for a rate increase by July. We see the Federal Reserve as “going it alone” and doing the heavy lifting for the ECB – weakening the Euro boosting exports and generating cash flow to buy US goods.*

***The US central bank is now taking up the role of an informal Marshall plan – engineering currency devaluations for less competitive economies.***

***Asymmetry between US and Euro Zone***

*There is a marked asymmetry between the impact of a rate increase on the US economy – which has diversified and efficient financing channels and is less dependent on exports*

***And:***

*The Euro Zone - where transmission of credit is inefficient and dependence on exports is high. Currency devaluation becomes a means to even out these differences.*

***EU is not a free trade agreement!***

*Our focus with regard to Bullard’s statements centers on what we view as underestimating the UK – EU exit poll. This is seen as a trade agreement issue, subject to re-negotiation. We view this as tantamount to comparing the EU to NAFTA – which it is not!*

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***A leave decision would signal the end of the EU project – which reflected the primacy of politics over economics. Can we countenance a return to EFTA – European Free Trade Agreement?***

***UK referendum – more grim warnings!***

*The UK referendum is continuing to elicit grim warnings – with a British research group predicting that an exit would delay the return to a balanced budget – currently foreseen for 2020. This would entail further austerity – not a pleasant prospect!*

***Despite these forebodings – some still see the chance of a Leave vote as high as 45 per cent, with a short term shock to both sterling and the Euro. This is not about free trade!***

***Who has it right - Business people or investors?***

*Who has it right business people or investors? This is the question raised by the divergence between investor and business confidence in the single currency area's largest economy. While yesterday investors expressed skepticism, today business sees some gradual improvement.*

***Are we seeing a similar phenomenon as in selected emerging markets? Retail investors are swayed by market volatility and exports. Business “capital investors” are geared towards a longer term optic and snapping up industrial assets at bargain prices?***

***Greece shall pay – where is the economic turnaround?***

*On the event risk front, markets are relieved at the agreement to unblock the next tranche of rescue funds to the besieged economy. This shall avoid a default in July. However, we are still after 3 rescues dealing with a cash flow squeeze as opposed to discerning any signs of growth.*

***Rapprochement EU – Turkey – will it survive German elections?***

*With regard to the migrant crisis – there is a thaw in relations between Germany and Turkey, the “gatekeeper” stopping the indiscriminate arrival of refugees. Shall this resumption of discussions survive possible government shifts in Europe?*

***Populist movements shall be decisive in European politics***

*Populist movements may splinter the vote and make formation of coalitions more difficult. Elections in Germany – the center forward of the EU are looming nearer? Is this all about Angela Merkel? The AFD – opposed to Merkel's open policy is nearing 12 per cent.*

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## Research Highlights

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