FEBRUARY 2016

MONTHLY OUTLOOK

Christmas Corporation's Research Division

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Did we successfully foresee the trends or were we surprised?

Deflationary boom in prospect as emerging economies face pressure

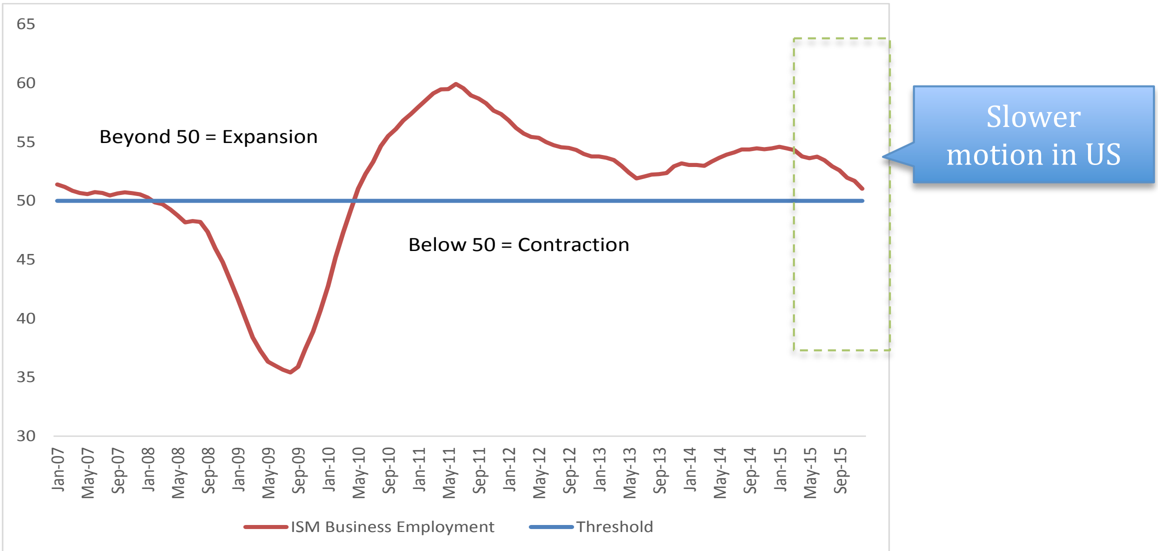
February 2016

Outlook: Be cautious about emerging markets in 2016

The uncertainty on emerging economies prospect, especially from China, and deflationary prospect due to lower energy price will still be the market headline. ECB[1] and BOJ[2] decision to cut interest rate into negative territory is not enough to restore market confidence. Emerging economies that rely on commodity and facing current account deficit will still face pressure, like Brazil, South Africa and Colombia.

Due to global market volatility, the impact from winter storm Jonas, and uncertainty on election outcome will make Fed more cautious to increase benchmark rate. There is a chance that Fed will be more dovish both in term of policy language and policy rate. Several economic activity data has confirmed that there is a sign of slower acceleration, like ISM[3] Business Employment Index that showed smaller gain in employment momentum.

ISM Business Employment Index is approaching contraction threshold



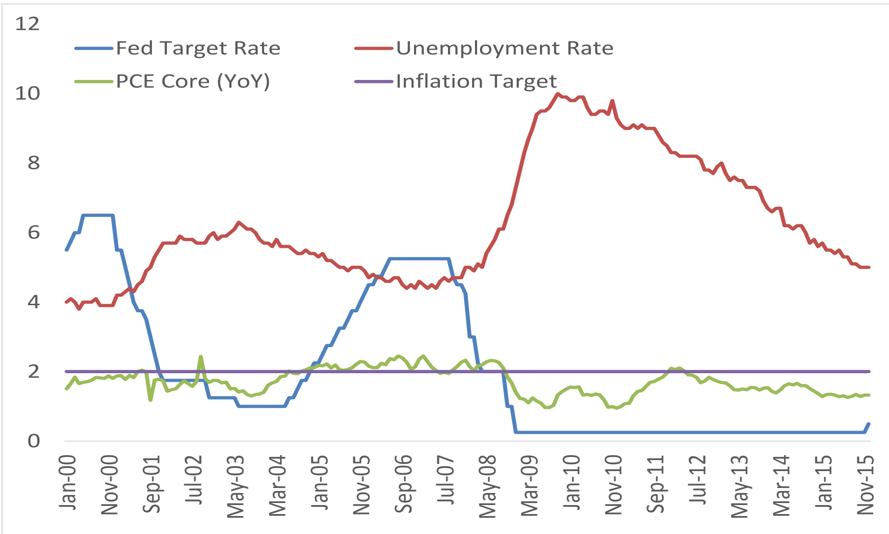
Source: Bloomberg

[1] European Central Bank: The central bank for the euro and administers monetary policy of the Eurozone, which consists of 19 EU member states and is one of the largest currency areas in the world
[2] Bank of Japan: The central bank of Japan
[3] Institute for Supply Management: The oldest, and one of the largest, supply management associations in the world

Strong hiring in December caps solid year for US jobs

US Employment situation gained momentum for December (Released on January). The Nonfarm Payrolls added 292 thousands more jobs on December, compared to 252 thousands in previous months and market consensus which is about 200 thousands. Unemployment rate stood at 5.00%, which is the lowest level since March 2008. This is the main reason why The Fed was so confident to raise benchmark rate for the first time since global financial crisis in 2008 to 0.25% - 0.50% from 0.00% - 0.25%. However, in term of inflation (PCE[4] core), the inflation is still below Fed's target. This is why the current rate hike will be gradual.

Fed target Rate, Unemployment rate, and PCE Core



Source: Bloomberg

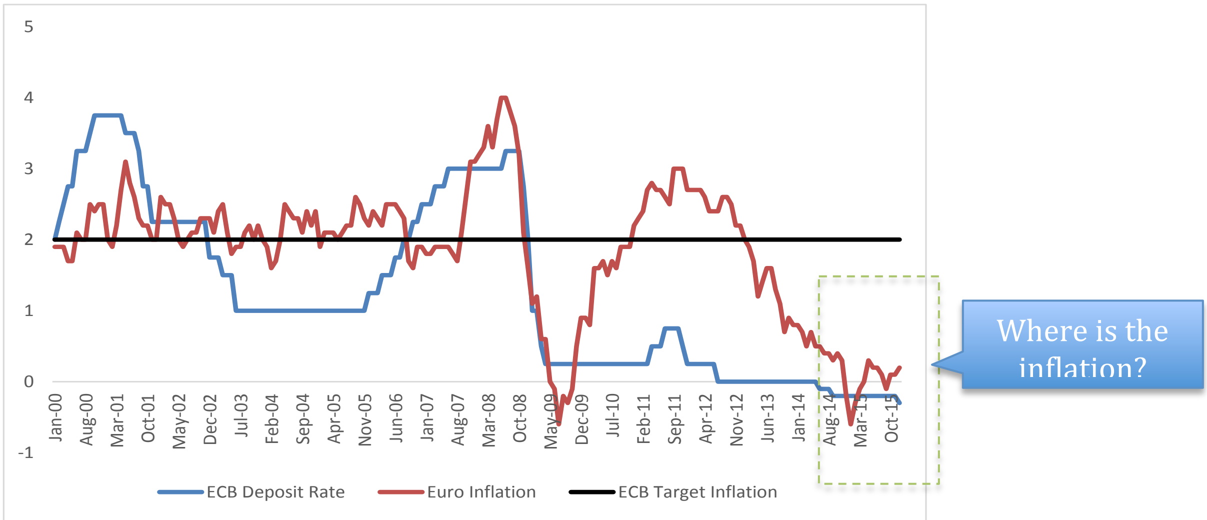
Fed holds interest rate at 0.25% - 0.50% as expected. On economy, Fed sees the economic activity will expand at a moderate pace and labor market will continue to strengthen. On inflation, Fed still believes that inflation will remain low due to declines in oil price. However, Fed starts to pay attention on international condition and will closely monitoring this impact to labor market and inflation. On policy outlook, Fed still believes that the path on interest rate hike will be gradual.

[4] Personal Consumption Expenditure: Component statistic for consumption in gross domestic product (GDP) collected by the US Bureau of Economic Analysis (BEA)

Surprise move on ECB rate cut, BOJ negative interest rate, and IMF global growth forecast cut

ECB's President, Mario Draghi indicated another interest rate cut in near term due to expectation on low inflation environment. Both Mario Draghi and other ECB's members are trying to give a signal that ECB still has plenty tools to boost economic and inflation outlook. Yet, as ECB Deposit Rate already in negative territory (current level of deposit rate is -0.30%), ECB has a limited room to do another significant interest rate cut.

ECB deposit rate and Euro inflation movement vs ECB target inflation



Source: Bloomberg

BOJ surprised market by cutting excess reserve interest rate into negative territory to -0.10%. Moreover, BOJ said that it would do whatever it takes to achieve inflation target. Currently, Japan inflation is stood at 0.20%, or still far below BOJ's target, which is 2.00%. The risk on declining oil price and slower growth in emerging economies especially China has become major concerns for BOJ to cut its interest rate.

IMF cuts world economy outlook on its January 2016 WEO. IMF predicts world economy will grow 3.40% this year and 3.60% next year. This implied a negative revision about 0.20% compared to its previous estimation in October 2015. The major drag from the outlook is coming from negative growth revision in emerging economies.