MONTHLY BAROMETER
PRESCIENT & SUCCINCT ANALYSIS OF WHAT'S OUT THERE

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- If we had to capture the mood at Jackson Hole (the meeting of central bankers) with just one word, it would be: **anxiety**. Despite participants putting on a brave face, there was a sense that central banks' activism has run its course and is now increasingly provoking unwanted side effects (like market distortions, exacerbation of inequalities and so on). While monetary policy can to a certain extent fight deflation, it cannot create economic growth. Therefore, **more central bankers are now calling for fiscal policy to act in symbiosis with monetary policy.**
- New evidence from the Fed suggests that the probability of an interest rate hike may be lower than the markets assume. The reasons are twofold: (1) Participants on the Fed Open Market Committee have dramatically reduced their expectations of what the "natural rate of interest" (the one that is neither too "hot" nor too "cold") should be – **from 4.25% three years ago to 3% today**; (2) A member of the Fed's board of governors has asserted that a rate increase would have to be supported not only by the two prerequisites of strong growth in employment and inflation going back to 2% (as every market participant knows), but also by the absence of "global risk events". The abundance of the latter suggests that a rate increase is further away than we think. **In the foreseeable future, lower growth and very low interest rates are a given**.
- **Across the developed world, new data confirms that productivity growth remains worryingly weak**: non-existent or even negative. In the US, nonfarm business productivity decreased by 0.5% in Q2 (Y-o-Y) - the third consecutive quarter of falling productivity and the longest declining streak in almost 40 years. Weak productivity corrodes living standards. Therefore, if this becomes a structural rather than a cyclical problem, the societal expectations of ever-rising prosperity will have to be ditched, stoking populism and making the politics of political economy fiendishly difficult.
- So far, and despite the drop in confidence, the Eurozone (EZ) is weathering the shock of Brexit better than expected. At 53.3, the EZ August PMI is slightly above consensus, suggesting growth of 0.4% in Q3 (Q-o-Q). This is encouraging but insufficient to revive gloomy European spirits. Contrary to the general sentiment conveyed by the media, **the greatest danger facing the Eurozone is not disintegration** fuelled by Euro-scepticism**, but paralysis and slow death** spurred by Euro-pessimism or Euro-indifference.
- In the UK, improved unemployment and retail sales figures combined with a buoyant stock market seem to vindicate the "Leavers". This is an illusion. What truly matters is the exchange rate. In an economy whose imports amount to 30% of GDP, a currency depreciation of more than 10% implies that **Britons will become poorer as prices start rising faster than wages**. It will be so because, as previously, an improvement in trade powered by a £ depreciation won't happen on a sustained basis (as domestic costs rise faster than those of Britain's trading partners).
- The sudden passion for EM bonds and equities has less to do with their inherent qualities than with the search for yields caused by the $13tr in negative-yielding bonds that are crippling mature markets. EM may currently be the least bad or "default" option for investors, but none of the problems that beset them at the beginning of the year – over-indebtedness, structural impediments, rule of law, etc. – have gone away. **High EM yields, that come with large political and governance risks, are vulnerable to: (1) a rise in US interest rates and (2) geopolitical risks.**
- The jury is still out as to whether the gig economy is a force for good, or the opposite. Today, gig workers – ranging from low-level freelancers to high-end portfolio professionals – represent 35% of the US workforce. **Tomorrow, they will define the dynamic of labour markets around the world**. This could develop in two ways. One in which the "uberization" of work leads to a feudal marketplace ruled by the whims of the lord. Another characterized by a co-op model with individual owners of the means of production. Albeit inadvertently, **the gig economy will provoke more intervention from governments** who will do their utmost to ensure that labour does not lose more ground relative to capital and that gig workers receive some of the benefits that normal employees enjoy.
- **The gig economy is certain to exacerbate inequalities and the "fissured workplace"** (a notion coined by the US labour economist that explains why real wages may remain stagnant despite increases in the minimum wage). Already, artificial intelligence and robotics are making many jobs uncompetitive, while for many hard-pressed workers the sharing economy often resembles a "sharing the scraps" economy. The fact that there is not, as yet, an effective plan or programme to deal with the possibility of more severe inequality should be a cause for serious concern. To paraphrase the Nobel economist Bob Shiller, today's economic inequality may well become tomorrow's political catastrophe (by giving rise to an explosion in populism).
- The peace treaty between the government of Colombia and FARC heralds the end of the last war – between and within countries – in the American hemisphere. It doesn't put an end to all violence of course, but is nonetheless a remarkable achievement. For global investors, this is a bit of a puzzle: at a time when the perception of geopolitical risk is increasing, violence is actually receding around the world. As shown by the data, **the world is much more peaceful today than it has ever been**, but the media distort our understanding and perception by systematically highlighting, or even inflating, events that happened – what does not happen is rarely newsworthy. The real enemies of investors are not terrorism, conflicts and other forms of violence, but rather corruption, the absence of the rule of law, etc.
- In the Middle East, climate change is intensifying summer extremes. According to the UN, **heat now claims 230,000 lives annually in the Arabian Peninsula and the Fertile Crescent**, making it a bigger killer than regional conflicts and exacerbating other risks.
- In the coming weeks, "must-watch" issues include: (1) the Fed's "hiking" path, (2) whether the data confirms that consumers and businesses save more in a low or negative interest rate environment, (3) how China deals with excessive indebtedness, and the policy - political tensions this creates; (3) renewed pressure on overleveraged EM (according to the BIS, between now and 2018 corporate repayments will total $340bn – 40% more than during the past 3 years); (4) the vast array of market-moving geopolitical and societal risks. **For real-time and in-depth analysis on any of these, please contact us.**