The Week Ahead: US Fed meeting in focus, US and UK 3Q GDP data to be released

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US: Fed meeting statement in the spotlight

A number of important economic events and data releases are due this week. The Fed will meet on 27-28 October, with interest rates expected to remain on hold. Thus, all eyes will be on the accompanying statement (no post-meeting conference or new projections are scheduled). We believe that any changes to the statement will be subtle, with the FOMC continuing to highlight data dependence. The statement is likely to acknowledge that US data have been more mixed since the September meeting. The Fed will likely want to see indications that the recent weakness in US data (including payrolls and retail sales) was transitory. We continue to see the possibility of a December rate hike if October and November payrolls rebound. Markets will also watch closely for any changes to references on global and financial market developments. These were included in the September statement and cited as the reason for the Fed keeping interest rates on hold.

US and UK: 3Q GDP numbers also important

Also important will be the first releases of US and UK 3Q GDP, alongside US durable goods and personal spending data. The consensus is for US real GDP growth to have moderated to 1.5% q-o-q SAAR from 3.9% in 2Q. The softer growth is expected largely on the back of net exports (with the strong USD) and inventories dragging on headline growth. Excluding these factors, the data are expected to show solid underlying domestic demand, with healthy private consumption activity. Investment is also likely to see support from the residential segment, whilst government spending is expected to contribute positively to growth. In the UK, the consensus is for GDP growth to remain solid at 0.6% q-o-q, albeit marginally weaker than the 0.7% seen in 2Q. In Europe, the data focus will be on inflation statistics for October. A number of ECB members are also scheduled to speak.

Japan: BoJ likely to keep monetary policy steady

Our base case is for the BoJ not to announce any additional monetary easing measures at its 30 October meeting. Recent comments by BoJ officials have not indicated an imminent move despite the weakness in recent data. However, the decision will remain a close call, and the BoJ has a history of surprising the market. This week sees a number of releases for September. If the data disappoint, indicating downside risks to the growth outlook, this will increase the probability of the BoJ considering additional easing. Separately, we expect the Central Bank of Egypt to remain on hold at its October meeting. With the appointment of new central bank governor Tarek Amer from 27 November, monetary policy will likely focus on gradual EGP weakening. Finally, the Chinese Communist Party will hold its fifth plenary session on 26-29 October, at which it is likely to discuss fiscal reforms and investment objectives.

I. Recent Data and Events

A. G4 economies

Eurozone: ECB signals strong possibility of further easing

ECB reviewing all monetary policy instruments; policy to be re-examined at December meeting

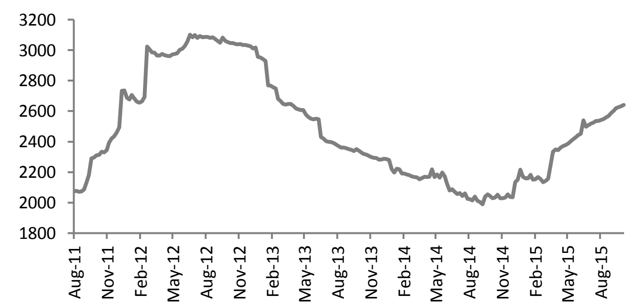
The ECB retained its current monetary policy on 22 October, though significantly, it signalled a strong bias towards implementing additional easing measures. This has raised market expectations that the ECB will announce a scaled up and extended QE programme (currently at EUR60 billion per month, until at least September 2016) at its 3 December meeting. ECB President Mario Draghi stated that ECB will re-examine its monetary stimulus at its December meeting, based on updated staff macroeconomic projections. Additionally, the Governing Council has tasked internal bodies with examining the pros and cons of all available monetary policy instruments, including interest rate cuts (the deposit rate is currently at -0.2%). Draghi highlighted the importance of real interest rates, saying that with inflation expectations weak, real interest rates are higher than desirable.

Current programme may be expanded, including duration and size of monthly asset purchases

The move to the more bearish stance was driven by: i) concerns over the external environment, especially emerging markets; ii) the further decline in commodity prices, signalling downside risks for inflation; and iii) the EUR's recent strengthening. The ECB's announcement last week reduces re-appreciation risks for the EUR ahead of any further easing measures. The EUR has been trading weaker across the board in the aftermath of the ECB's press conference. We expect further monetary loosening to be announced in December, in conjunction with a downward revision to the ECB's inflation forecasts. In line with past communications, we believe that this will likely take the form of expanding the ongoing asset purchase program, both extending the duration (possibly by 12 months beyond September 2016) and increasing the monthly purchases. The ECB's asset purchase programme is relatively small compared to those of other major central banks. The list of assets that the ECB is able to purchase could also be widened, possibly to include investment grade corporate bonds.

Fig. 1. Eurozone: ECB's QE programme remains relatively small compared to other major central banks

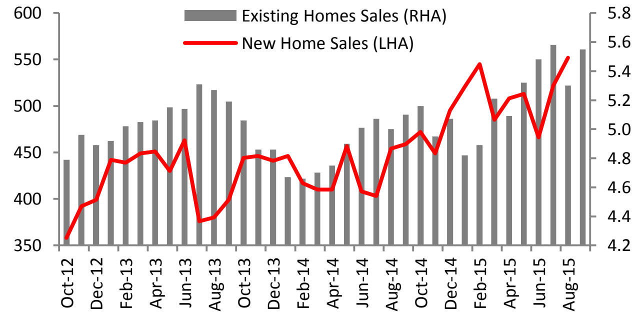
ECB's balance sheet, EUR billion



Source: Bloomberg

Fig. 2. US: Ongoing housing market recovery should support private confidence and residential investment

'000 (LHA); million (RHA)



Source: Bloomberg

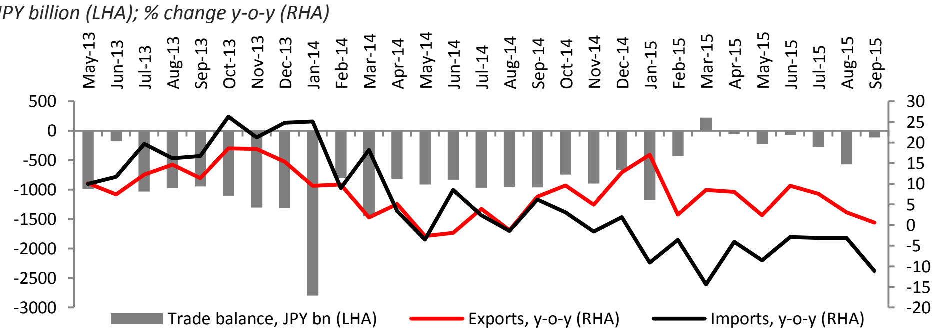
US: Housing starts strong in September, reflecting steady sector improvement

September housing starts beat market expectations substantially, existing home sales rebound

Key housing sector data for September released last week pointed to activity remaining solid. Housing starts rose a healthy 6.5% m-o-m to 1.21 million (SAAR), substantially exceeding the consensus forecast of a 1.14 million increase. This was the sixth consecutive month of housing starts above the 1 million unit level. Rising rental demand was partly behind the strong starts. Meanwhile, sales of previously owned homes rebounded in September, expanding by 4.7% m-o-m to 5.55 million SAAR. This was the second-highest level since February 2007. The data continued to highlight the steady improvement in the housing market despite signs of moderation in other areas of the economy. The housing sector's buoyancy is likely to remain an important source of support for consumer confidence and domestic economic activity.

Fig. 3. Japan: Export growth slows to just 0.6% y-o-y in September, with weaker demand from China

JPY billion (LHA); % change y-o-y (RHA)



Source: Bloomberg

Japan: Exports slow sharply, raising concerns over economy

Export growth slows to just 0.6% y-o-y in September

Japan's trade data for September came in weaker than expected. Export growth slowed to a mere 0.6% y-o-y, versus 3.8% expected by the consensus and the 3.1% y-o-y seen in August. This was the weakest pace of growth since August 2014, and largely reflected the impact of lower Chinese demand. The weak JPY helped to increase the value of exports (by 4.6% y-o-y) in September, though the volume fell -3.9% y-o-y, the third consecutive monthly decline. On a geographic basis, exports to Asia were weak, whilst those to the US and Europe remained relatively strong. Exports to the US were up a solid 10.4% y-o-y, with some of the growth likely due to the weaker JPY. In contrast, exports to Asia fell -0.9% y-o-y, with those to China down -3.5% y-o-y. Meanwhile, imports contracted by -11.1% y-o-y in September, broadly in line with the consensus, on the back of weaker commodity imports. The weak export growth led Japan to report a trade deficit of JPY114.5 billion, versus the consensus expectation of a JPY87 billion surplus.

Economic indicators point to risks of Japan falling into technical recession

The September trade data meant that quarterly export growth remained almost flat at 0.2% q-o-q in 3Q. The weak export performance likely caused net exports (alongside gross fixed capital formation and inventories) to drag on GDP growth. The consumption component of real GDP was likely positive in 3Q. There are increasing concerns that real GDP will again contract in 3Q, resulting in a technical recession following the negative real GDP growth in 2Q. The weak economic indicators are increasing pressure on the BoJ to introduce further easing measures at its 30 October meeting, though our base case is for policy to remain steady.

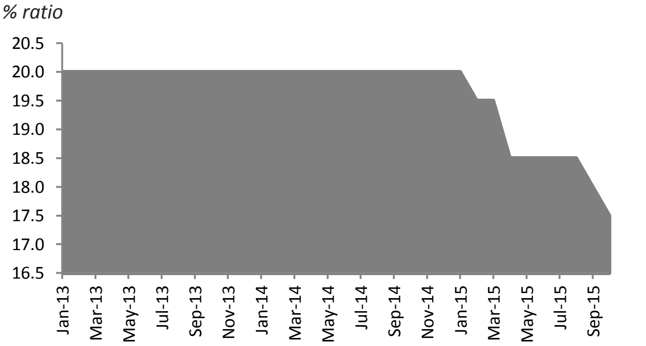
B. Emerging Market Economies

China: Cuts interest rates and reduces RRR

50 bps RRR cut should unlock some CNY600-650 billion for lending

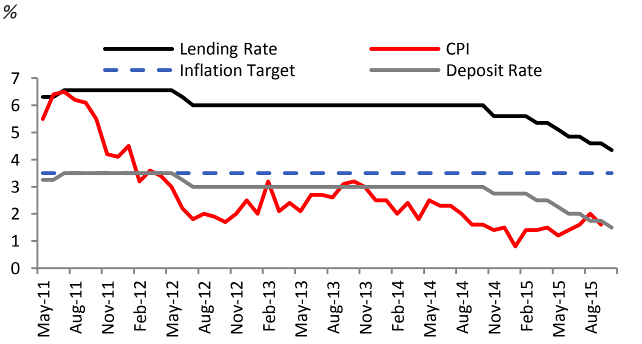
The PBoC again eased monetary policy at the end of last week. The reserve requirement ratio (RRR) for all banks was cut by 50 bps, and by another 50 bps for those that have met macro prudential requirements and made certain levels of micro and rural loans. The universal RRR cut of 50 bps will unlock about CNY600-650 billion of deposits for lending. Moreover, the one-year lending and deposit rates were reduced by 25 bps (effective from 24 October). We had expected a 50-100 bps cut to the RRR and a 25 bps reduction in the benchmark interest rate in 4Q2015. Thus, we still see the potential for a further cut in the RRR in 2015, alongside fiscal expansion to support growth. Moreover, we see further cuts to the benchmark interest rates in 2016.

Fig. 4. China: RRR for large banks cut to 17.5% at end October



Source: Bloomberg

Fig. 5. China: October rate cut the sixth in one year



Source: Bloomberg

These interest rate and RRR cuts followed the release of September and 3Q GDP data earlier last week. The further easing, despite GDP beating consensus expectations, has intensified debate about the accuracy of the data. Some market commentators remain of the view that the official GDP data likely overstate the level of economic expansion.

China: 3Q2015 real GDP growth at 6.9%, marginally beating consensus

Manufacturing sector slowdown partly compensated for by stronger service sector growth

China's economy slowed less than expected in 3Q, supported by resilience in the service sector, and shrugged off the stock market crash. China's real GDP growth printed at 6.9% y-o-y in 3Q2015, slightly higher than the consensus forecast of 6.8%, but down from the 7% expansion seen in 2Q. This was the slowest rate of growth since the financial crisis. On a sector basis, manufacturing growth slowed to 5.8% y-o-y in 3Q, from 6% in 2Q. However, service sector growth accelerated to 8.6% y-o-y in 3Q, from 8.5% in 2Q. We await the release of a more detailed breakdown which separates the financial services sector to see the key drivers of service sector growth. Resilient consumption growth likely supported the service sector growth, in our view.

September data point to further downside risks, though easing measures should provide some support to GDP growth in 4Q

Meanwhile, data for September continued to highlight the headwinds faced by the Chinese economy. Factory output rose 5.7% y-o-y in September (missing forecasts of a 6% rise), whilst fixed asset investment (FAI) increased 10.3% y-o-y in 9M2015, below estimates of 10.8%. Only retail spending came in slightly above the consensus, growing 10.9% y-o-y in September (consensus 10.8%). Previous loosening measures should provide some growth support in 4Q2015 and into 2016. Credit growth has picked up over recent months, and the government has increased spending on infrastructure and eased curbs on the ailing property sector. The latter has helped revive weak home sales and prices, but has not yet reversed the sharp decline in new construction. Data released last week showed that government spending surged almost 27% y-o-y in September.

Turkey: Interest rates kept on hold

The CBRT retained its existing monetary stance last week, with all key rates unchanged, as expected. The policy rate stayed at 7.5%, and the ON deposit and lending rates remained at 7.25% and 10.75%. Changes to the statement were limited overall, though they signalling tighter monetary policy ahead. The decision by the US Fed at its 17 September meeting to keep rates unchanged has bought the CBRT more time, in our view. However, we continue to expect the CBRT to raise interest rates alongside the US Fed in order to support much needed capital inflows.

II. Economic Calendar

Fig. 6. Upcoming Events and Data Releases

Time*	Country	Data point	Period	Prior	Consensus
Monday 26, Oct					
13:00	Germany	IFO Business Climate	Oct	108.5	107.8
13:00	Germany	IFO Current Assessment	Oct	114	113.5
14:45	Eurozone	ECB Executive Board Member Yves Mersch Speaks in Brussels			
18:00	US	New Home Sales	Sep	552K	550K
18:00	US	New Home Sales, m-o-m	Sep	5.7%	-0.4%
26-29 Oct	China	Chinese Communist Party to Discuss Economic and Social Policy			
Tuesday 27, Oct					
13:30	UK	GDP, q-o-q	3Q A	0.7%	0.6%
13:30	UK	GDP, y-o-y	3Q A	2.4%	2.4%
16:30	US	Durable Goods Orders	Sep	-2.3%	-1.3%
16:30	US	Durables, ex-Transportation	Sep	-0.2%	0%
18:00	US	Consumer Confidence Index	Oct	103	103
20:00	UK	Bank of England's Shafik Speaks in London			
Wednesday 28, Oct					
3:50	Japan	Retail Trade, y-o-y	Sep	0.8%	0.4%
3:50	Japan	Retail Trade, m-o-m	Sep	0%	1.1%
22:00	US	FOMC Rate Decision (Upper Bound)	Oct-28	0.25%	0.25%
22:00	US	FOMC Rate Decision (Lower Bound)	Oct-28	0%	0%
	Saudi Arabia	SAMA Net Foreign Assets, SAR	Sep	2.5B	--
Thursday 29, Oct					
3:50	Japan	Industrial Production, m-o-m	Sep P	-1.2%	-0.5%
3:50	Japan	Industrial Production, y-o-y	Sep P	-0.4%	-2.6%
11:00	UK	Nationwide House Px NSA, y-o-y	Oct	3.8%	3.8%
14:00	Eurozone	Consumer Confidence	Oct F	-7.7	-7.7
16:30	US	Initial Jobless Claims	Oct-24	259K	264K
16:30	US	GDP Annualized, q-o-q	3Q A	3.9%	1.5%
16:30	US	Personal Consumption	3Q A	3.6%	3.3%
18:00	US	Pending Home Sales, m-o-m	Sep	-1.4%	1%
18:00	US	Pending Home Sales NSA, y-o-y	Sep	6.7%	7.4%
	Egypt	Deposit Rate	Oct-29	8.75%	--
	Egypt	Lending Rate	Oct-29	9.75%	--
Friday 30, Oct					
3:30	Japan	Natl CPI, y-o-y	Sep	0.2%	0%
	Japan	BOJ Annual Rise in Monetary Base	Oct-30	¥80T	¥88T
7:00	Japan	Bank of Japan Policy Statement/Kuroda Press Conference			
14:00	Eurozone	Unemployment Rate	Sep	11%	11%
14:00	Eurozone	CPI Estimate, y-o-y	Oct	-0.1%	0%
14:00	Eurozone	CPI Core, y-o-y	Oct A	0.9%	0.9%
16:30	US	Personal Income	Sep	0.3%	0.2%
16:30	US	Personal Spending	Sep	0.4%	0.2%
16:30	US	PCE Deflator, m-o-m	Sep	0%	-0.1%
16:30	US	PCE Deflator, y-o-y	Sep	0.3%	0.2%
16:30	US	PCE Core, m-o-m	Sep	0.1%	0.2%
16:30	US	PCE Core, y-o-y	Sep	1.3%	1.4%
18:00	US	Fed's Williams Speaks in Washington			
18:00	US	U. of Mich. Sentiment	Oct F	92.1	92.5
19:25	US	Fed's George Speaks on Federal Reserve Structure			

* UAE time
Source: Bloomberg

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