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It Will Be a December to Remember

The calendar year neatly compartmentalizes life and business. For investors, measures of calendar-year returns often smooth over the rough patches. Unfortunately for those who see it this way, **key policymakers across the world seem to have left much of their unfinished business for the month of December.**

For many investors, judging whether 2015 has been a good or bad year could "come down to the wire" at year end. This is owed to the unusual prevalence of market-moving policy decisions this coming month, combined with benchmark global asset market returns which have hovered near flat so far in 2015. These could easily swing positive or negative given typical volatility, and of course, where one invested in markets which showed very uneven regional performance this year.

Looking ahead:

1) December 3: The European Central Bank's Governing Council is expected to take additional unspecified easing steps. Our expectation is an increase in the €60 billion monthly pace of asset purchases, an extension of the purchase program to clarify that it will not face a "hard stop" in mid-2016, and perhaps cuts in deposit rates deeper into negative territory.

   Expectations for action were strongly cemented by ECB President Draghi's October 22 press conference where he suggested a range of steps would be forthcoming. Unlike "neat increments" of 25 basis point rate movements, unconventional easing steps are much more complex and less certain to forecast. Most importantly, movements in the Euro and other asset prices strongly suggest expectations of significant action at this meeting. A failure to follow through seems quite improbable, but would generate significant volatility in global markets on any actions deemed insufficient.

2) December 4: OPEC meets to discuss production in Vienna. No large changes in Saudi Arabia's strategy are foreseen. However, the Saudi's high level of current production amid a large price drop this year makes this a meeting that could still present two-sided market risks **(see figure 1).** As seen in the past, a mere continuation of current high production levels could see oil prices fade further. On the other hand, the element of surprise could magnify near-term impact if producers were to agree on a significant output cut at this time.

3) December 4: U.S. employment data for November will be released. Short-term interest rate markets price a 76% probability of a 25 basis point interest rate increase from the Fed at its December 15-16 meeting. The employment data, and potentially a speech from Fed Chair Yellen on December 2 could cement or weaken the case for action. We expect an employment gain in November slightly stronger than the consensus expectation of 200,000 jobs. The mirror opposite of downwardly biased August and September employment data, November job gains tend to show above-average gains. A jump in tightening expectations could further strengthen the U.S. dollar to 2015 highs.

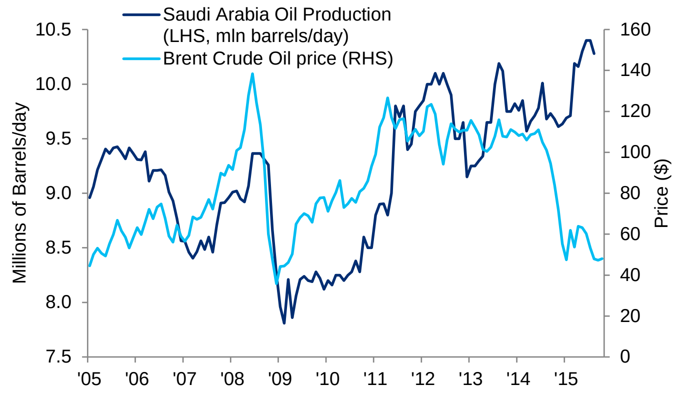
4) December 15-16: The Fed is expected to make its first increase in U.S. interest rates since 2006. It has never begun a new policy tightening cycle in the month of December. This is likely given concerns about year-end market liquidity which the Fed no longer seems deterred by. If the Fed acts, as we expect, it would be the largest central bank policy divergence since at least the early 1990s.

The Fed is likely to reinforce its message that the course forward for U.S. rates will be a very shallow rise. Given a $3.6 trillion expansion of the Fed's balance sheet during the crisis years, we see the coming tightening cycle as relatively benign compared to the scope of its easing steps **(see figure 2)**. However, the economic and financial market recovery seem more mature than many investors believe (please see our Quadrant - November 23, 2015 for full discussion). In terms of the announcement itself, we urge investors not to view the December 16 decision as a discrete event that will play out fully in markets in a single day. As we also discussed previously in detail (please see Global Strategy Bulletin – September 14, 2015), inaction when markets expect a tightening step has proven to be a quite negative event historically for many risk assets.

Beyond these key dates, the Bank of Japan holds a policy meeting on December 18. Expectations for action are not as clear, but recent comments suggest a possibility for more Japanese easing, which would strengthen the international policy divergence further. As discussed in Quadrant, **we view the period beyond year end as a firmer one for global markets**. Growth is slow, but expansion is intact. Expectations for central bank support have raised "positioning risks" in markets, but aside from the Fed's token tightening measures, the focus of most macro policies will be on sustaining and strengthening the global expansion. The risks that have built up from a financial market recovery that has seemed asymmetric to the strength of the global economic recovery will be seen in time.

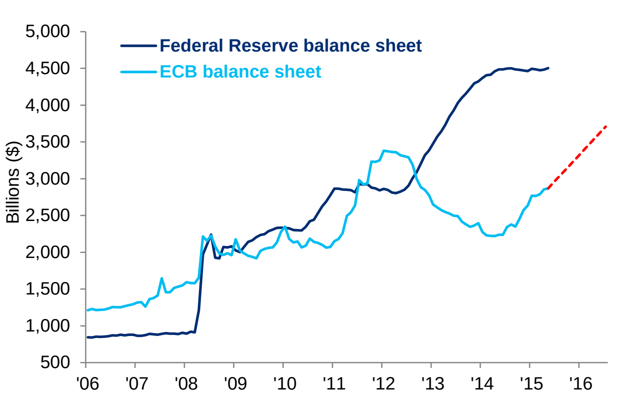
Finally, today, the International Monetary Fund is likely to announce approval of China's Yuan as a currency included in its Standard Drawing Rights (SDR) basket. The actual utilization of the Yuan (Renminbi) by international central banks is to be seen and will likely build just gradually over time. This announcement is considered a mere formality at this point given affirming comments from IMF, U.S. and other officials. While we would assume the same, tail risks do build from strong consensus assumptions.

Figure 1. Saudi Arabia Oil Production



Sources: Haver Analytics as of November 30, 2015.

Figure 2. Fed vs ECB Balance Sheet in USD



Source: Bloomberg as of November 30, 2015. All forecasts are expressions of opinion and are subject to change without notice and are not intended to be a guarantee of future events.

Figure 3. Equity and Bond Market Returns by Quarter

Seasonality of Global and Regional Share Market Performance (Total Returns By Calendar Quarter)							
Index	**1Q Avg**	**2Q Avg**	**3Q Avg**	**4Q Avg**	**4Q Low Return**	**4Q High Return**	**Sample Period**
MSCI World Index	2.4	2.5	-0.4	4.9	-20.7	19.0	26 years
US	2.6	2.4	0.5	4.9	-27.5	17.8	26 years
Europe	3.1	3.0	-0.6	4.8	-22.1	25.1	26 years
UK	1.9	1.4	1.1	5.1	-19.8	22.0	26 years
Japan	2.0	1.5	-2.1	1.6	-22.3	17.6	26 years
Asia Ex-Japan	3.5	3.0	-0.3	6.5	-21.6	48.7	26 years
China	-3.8	7.1	-0.1	3.9	-33.4	47.5	21 years
Latam	4.1	3.6	1.2	6.7	-20.4	31.0	19 years
EM EMEA	4.3	2.2	1.1	6.9	-27.5	34.3	17 years
Seasonality of Global Fixed Income Market Performance (Total Returns By Calendar Quarter)							
Index	**1Q Avg**	**2Q Avg**	**3Q Avg**	**4Q Avg**	**4Q Low Return**	**4Q High Return**	**Sample Period**
US Treasury	0.6	1.3	2.7	1.5	-2.6	8.9	25 years
German Bunds	1.3	0.7	2.4	1.8	-2.5	7.8	25 years
UK Gilts	0.5	1.1	3.4	3.0	-2.2	10.6	25 years
US MBS	1.2	1.4	2.1	1.6	-0.5	5.0	25 years
HG Corps (USD)	1.1	1.8	2.4	1.8	-1.6	5.2	25 years
HY Corps (USD)	3.2	2.4	1.1	2.1	-17.2	8.6	25 years

Source: FactSet, The Yield Book and Bloomberg as of November 30, 2015. Source: MSCI, Standard & Poor's, STOXX Limited, Citi US Treasury Index, Citi German Government Bond index, Citi UK Government Bond Index, Citi US Mortgage (MBS) Index, Citi US High Grade Corporate Bond Index, Citi US High Yield Corporate Bond Index are used as indices above, Citi Private Bank as of 4Q 2014. Performances by quarter for full calendar years going back 25 & 26 years or since inception. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees or sales charges, which would lower performance. Past performance is no guarantee of future returns. Real results may vary.

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