

Your weekly market update

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Market Update

11 March 2016

Since the start of January, investors have been on edge as equity markets turned for the worse. Calls for a 2008 style recession were everywhere. Behind all the concern was global GDP. The global economies hit their peak. What has become clear in this weeks data is that emerging economies are to some degree running out of steam, whereas developing nations are transitioning well from monetary policy to fiscal spending. Canada was the first of the developed nations to jump into the fiscal spending mode. The Liberal party has championed this method of growing the economy both at the provincial and Federal level.

Economic data out of America indicates that both jobs, spending and now in the month of February manufacturing numbers are up. The forecast slowed down it did not transpire. Why? The American Federal Reserve did jump the gun and raise interest rates quickly. However it also did not follow through with more interest rate hikes which intern has provided relief to investors. The American Federal Reserve has made it clear that it is fully aware of the global headwinds and the potential impact on GDP. Unemployment is at all time lows of 4.9%. A total of 242,000 new job were added in February along with a reduction in inventory build up and increase in the total goods produced.

Why does China play such a big impact? The amount of raw materials China consumes matters. A drop in Chinese manufacturing consumption would see raw material prices, energy and commodity prices fall. All of which have fallen since the end of the commodities super cycle (China's greatest day of commodity



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consumption).

In the last week, prices have regained for aluminum, steel and stainless steel which are bellwethers that economic momentum is gaining. Oil has been the big red herring. The massive pricing war and markets share battles over oil initiated by Saudi Arabia was not due to a drop in global demand for energy. It is a direct result however of the rapidly changing land scape of energy players. Iran and American energy producers are the big disruptors of oil prices. It appears that for now, the pricing war will take a break maybe. Oil prices will look to stay ground above \$40 in the near term. This price target may look to be a challenge as some oil producing nations may decide to continue selling at the attractive \$40.00 a barrel price.

The EU recovery is continuing but it is nothing to write home about. Growth had picked up. The strongest performance since the upswing started in the spring of 2013. Since then however, the pace of expansion has slackened to 0.4% last spring and an average quarterly rate of 0.3% in the second half of last year. Indeed, Euro-zone GDP in the final quarter of 2015 was still below its pre-crisis peak of early 2008. Whereas America's was almost 10% above its peak of late 2007. The sluggish pace of the recovery has been especially disappointing given the fact that the Euro area has benefited from a double fillip. First, the fall in energy prices caused by the collapse in the oil price acted in much the same way as a tax cut, boosting consumer spending and the main engine of the recovery. Second, the European Central Bank has carried out quantitative easing creating money to buy financial assets together with the introduction of negative interest rates in June 2014, this has brought the Euro dollar down and kept it weak, helping exporters and contributing to a big current-account surplus of 3.7% of GDP in 2015.

The outlook for growth in 2016 now looks uncertain following the sharp falls in European equity markets, particularly of banking shares. This setback to equity markets undermines consumer and business confidence; it is likely to drag down growth. The slowdown in China and emerging economies, which account for a quarter of euro-zone exports, will also harm the recovery by hurting

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exporting companies. Germany will be particularly affected since the Chinese market has been a lucrative one for its exports of investment goods and luxury cars. Despite these brakes a recovery of sorts should remain intact, for three reasons. Renewed declines in oil prices will further boost household budgets. The European Central Bank is poised to loosen monetary policy still further when it's governing council meets in March.

China is a whole different circumstance. Exports have fallen by 25%. Imports are also down. To manage negative sentiment and a belief that China may still hard land it's economy government economic planners released statements. China on Saturday acknowledged it faced a tough battle to keep the world's second largest economy growing by at least 6.5 percent over the next five years while pushing hard to create more jobs and restructuring state-owned enterprises. The comments as Beijing kicked off its 12-day annual national parliament underscored the challenges facing China as its economy transitions from an investment and export focused economy to one based more on services and consumption.

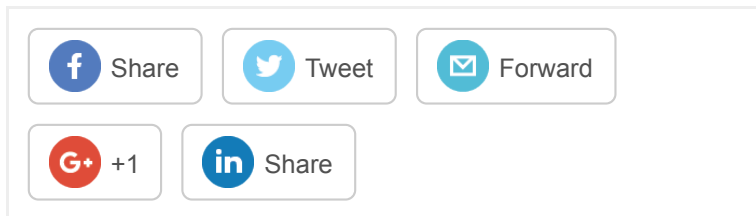
"China will absolutely not experience a hard landing," Xu Shaoshi, head of the National Development and Reform Commission (NDRC), told reporters at a briefing. "These predictions of a hard landing are destined to come to nothing." China's economy grew 6.9 percent in 2015, the slowest pace in a quarter of a century, but still comfortably the fastest among major economies. It has set a growth target of 6.5 percent to 7 percent for this year, introducing a band rather than a hard target as it seeks greater flexibility in juggling growth, job creation and restructuring of a host of "zombie companies" in bloated industries.

Underneath all the planning is a simple strategy to deficit spent to about 3% of GDP. China now too is officially in the fiscal spending strategy.

How does this translate to client strategies? Geographically, America and Canada hold near equal weighting at around 40% with Europe making up the third largest region. Corporations which have the bulk of their customer list focused in North America will perform the best.

Given that governments around the world are looking to engage in infrastructure spending (fiscal stimulus) holdings in industrial services will also grow in our models. Consumer goods and technology have also solid growth. Financial services make the core of the holdings for which we believe Canadian banks and insurers are well positioned.

Unlike the general lifting of all world economies after the 2008 recession, I do not believe the next year ahead will offer economic prosperity for all. It will only be advanced economies that have gone through the pain of monetary reform that will thrive forward. This will allow these nations the ability to spend strategically and grow into a very economically aggressive future. America, Canada, EU, Japan and the UK have all transitioned their economies for the next phase of growth. Emerging economies have failed to do so and must look to take drastic measures now. China being a prime example.



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