From: US GIO <[redacted]>
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The [redacted]. Morgan View

Looking beyond the stormy weather

- **Asset allocation** — We retain a medium-term value approach, focused on overweights in credit and equities, and based on softening of the fiscal cliff, and gentle rebound in global growth into Q1.
- **Economics** — Better PMIs and US jobs support a coming rebound in growth, but not enough to raise forecasts. We lower Euro area Q1 to flat.
- **Fixed Income** — Our systematic duration signals call for a small short position.
- **Equities** — A cyclicals overweight may be a better way to express a positive view in equity markets than an outright long.
- **Credit** — The HG CDS-Bond basis has turned positive for the first time in 14 months.
- **Currencies** — We list currency implications of different US election outcomes.
- **Commodities** — Port closures and power cuts are delaying the reopening of refineries on the US East Coast, but this should prove short lived.

- **Stocks continue the weekly up-and-down moves** they started early Sep. This week was an up-week for them, while other assets were largely unchanged. Markets remain in a holding pattern as everyone awaits information on where economies are headed and what decisions fiscal policy makers will make. We retain the view that this new information and decisions will prove positive for equities and credit over the next few months, and mildly negative for bonds, but can't be confident on whether this rally happens before or after the New Year.
- **This week's US data flow,** punctuated by today's payrolls report, were a bit better than hoped, moving our tracking exercise for Q3 to 2.4%, versus the 2% flat government estimate released last week. These provide us a good trajectory into the current quarter, but no more than is needed to realize our 2% forecast for Q4. At a world level, our Oct. Global manufacturing PMI advanced for a second straight month by 0.4 points, but remains just below 50. As such, it is in line with our 2% global growth forecast for Q4. Importantly, we again saw a rise in the order index and a fall in inventory index. All this supports our view that a gentle rebound in growth is coming, but does not yet create an upside bias.
- Most of us have been following the **Hurricane Sandy** drama closely this week, and some of us only too closely. New York and neighboring states are still trying to dig out from under the damage. Estimates of ultimate costs keep edging up. The near-term impact will likely be to depress activity for Oct. and early November, but rebuilding should then support growth in coming months. We are thus not changing GDP forecasts. We expect the main near-term impact on markets will be the difficulty in separating signal from Sandy induced noise in US activity data (*Here comes the story of the Hurricane*, Feroli et al., in GDW).
- Markets are now focused on the US **elections, ignoring those in China**. We note that Betting firms give Obama a 2/3rd probability of retaining the White House, and higher for the Democrats to retain control of the Senate. Status quo is thus seen as the most likely scenario, even as the popular vote polls suggest this will a very close contest.

See page 8 for analyst certification and important disclosures.

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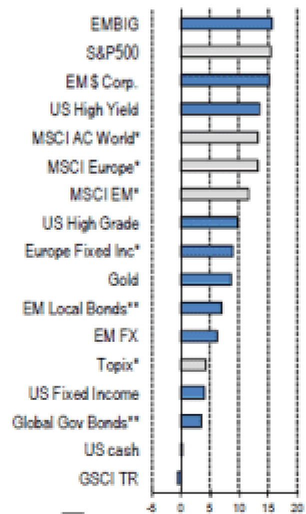
YTD returns through Nov 1
%, equities are in lighter color.



Source: [redacted] Morgan, Bloomberg. See blue box on page 2 for description.
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