The Weekly Market View

February 25 2020

ADCB ASSET MANAGEMENT LIMITED

Stocks halt rally

Blame it on the spread of the novel coronavirus COVID-19 outside China, equity market rally came to a halt. During the week ended 21 February, stocks were mixed through Wednesday but corrected on Thursday and Friday as the number of cases reported outside China increased. Technology stocks took the biggest hit on concerns of possible disruptions to their supply chains. DM equities outperformed EM equities although both groups posted losses. Global bonds, on the other hand, experienced a massive rally. In the US, yields declined across the curve, but the decline was more concentrated in the long-dated part of the curve. Demand for duration was evident as the 30Y UST yield tumbled to its all-time lows while the yield curve moved to its flattest level this year, further aggravated by the disappointing preliminary Markit PMI release. In Europe, German bund yields fell to a four-month low on mixed economic data. Amidst the backdrop of safe-haven appetite, search for yield led to outperformance of the periphery bonds with Spanish and Portuguese 30Y yields falling below the 1% level (for details on last week's GCC fixed income performance trends see GCC Fixed Income Weekly, February 23 2020). Elsewhere, in commodities, oil prices rose last week after experiencing a sell-off in previous weeks. Gold did not lose its shine – posted strong returns over the week extending its year-to-date gains. Silver and platinum prices rose too. Industrial metal prices remained under pressure. In the FX space, EUR appreciated against the USD on the relative strength of the European flash PMIs compared to the US flash PMIs for February. However, USD managed to gain further ground against both the GBP and the JPY.

Profit taking or virus scare?

Given the recent sharp move lower in risk assets, investors are now wondering if there is indeed a real virus scare or this is just a sign of some profit taking after a strong rally in the first six weeks of the year. Here are some points to ponder in this context. First, given the strong run up in certain segments of the equity market, there might be some tendency to book profits especially considering the fact that the earnings season has largely concluded in the US. Further, we do think that the markets are very concerned that the coronavirus could easily turn into a pandemic (considering the spread of the virus in Japan, South Korea, Italy and Iran) and potentially derail the nascent recovery in global growth. This for instance, was evident in the market reaction to a disappointing flash PMI in the US which was largely dragged down by the coronavirus concerns. However, we do think that equity market investors are largely ignoring some positive developments. The new COVID-19 cases have been falling at a faster rate in China, while an increasing number of provinces reported zero new cases over the past few days. Industry restarting rates have picked up (for example automobile manufacturing restarting rate reached 75%). Furthermore, policy remains very accommodative globally with more easing bias in China. Valuations of equities do not look stretched when put in the context of persistently lower bond yields. Positioning into equities does not look crowded either.

Therefore, taking the rough with the smooth, we remain constructive on our outlook for equities (neutral in our asset allocation). Within equities we are overweight US by geography. Our continued preference for quality themes and large caps makes our equity investment strategy defensive to any potential shocks. Our preference for consumer-facing technology, services sectors and growth themes is a way to play the strong structural trend of the "new-economy".

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Global markets' performance snaps

Index Snapshot (World Indices)

Index	Latest	Weekly %	YTD %
S&P 500	3,338	-1.3	3.3
Dow Jones	28,992	-1.4	1.6
Nasdaq	9,577	-1.6	6.7
DAX	13,579	-1.2	2.5
Nikkei 225	23,387	-1.3	-1.1
FTSE 100	7,404	-0.1	-1.8
Sensex	41,170	-0.2	-0.2
Hang Seng	27,309	-1.8	-3.1
Regional Markets (Sunday to Thursday)			
ADX	5,037	-1.0	-0.8
DFM	2,738	0.1	-1.0
Tadawul	8,007	1.7	-4.6
DSM	9,934	0.9	-4.7
MSM30	4,192	1.5	5.3
BHSE	1,669	0.4	3.6
KWSE	6,188	-0.3	-1.5
MSCI			
MSCI World	2,420	-1.2	1.9
MSCI EM	1,095	-2.0	-2.7

Global Commodities, Currencies and Rates

Commodity	Latest	Weekly %	YTD %
ICE Brent USD/bbl	58.5	2.1	-11.4
WTI USD/bbl	53.4	2.6	-12.6
Gold USD/t oz	1,643.4	3.7	7.9
Silver USD/t oz	18.5	4.2	3.0
Platinum USD/t oz	975.4	1.0	0.1
Copper USD/MT	5,702.0	-0.6	-7.4
Alluminium	1,701.3	0.3	-4.9
Currencies			
EUR USD	1.08	0.1	-3.4
GBP USD	1.30	-0.6	-2.3
USD JPY	111.61	1.7	2.7
CHF USD	0.98	-0.4	-1.2
Rates			
USD Libor 3m	1.68	-0.7	-12.0
USD Libor 12m	1.73	-3.9	-13.4
UAE Eibor 3m	1.88	-5.1	-15.0
UAE Eibor 12m	2.29	-1.5	-0.0
US 3m Bills	1.55	-1.5	0.1
US 10yr Treasury	1.47	-7.2	-23.3

Summary market outlook

Global Yields	Global bonds, on the other hand, experienced a massive rally. In the US, yields declined across the curve, but the decline was more concentrated in the long-dated part of the curve. Demand for duration was evident as the 30Y UST yield tumbled to its all-time lows while the yield curve moved to its flattest level this year. In Europe, German bund yields fell to a four-month low on mixed economic data while search for yield led to outperformance of the periphery bonds. We believe the long-term US rates will remain in line with the Fed's target Fed fund rate and further curve steepening risks are rising.
Stress and Risk Indicators	VIX rose sharply over the past week as concerns about the spread of COVID-19 outside of China intensified. As we have been arguing, we believe that volatility will likely stay elevated given the range of risks on the horizon. This entire episode of the coronavirus would be a part of our 'high volatility' narrative for 2020 and our risk-barbell positioning.
Equity Markets	
Local Equity Markets	Local markets remained resilient with Saudi equities recovering some losses from previous weeks. We remain neutral on GCC equities given the potential for further dollar strength and range-bound oil prices, but we maintain our overweight call on Saudi equities. We also prefer banks in the regional context.
Global Equity Markets	During the week ended 21 February, stocks were mixed through Wednesday but corrected on Thursday and Friday as the number of cases reported outside China increased. Technology stocks took the biggest hit on concerns of possible disruptions to their supply chains. DM equities outperformed EM equities although both groups posted losses. Overall, we remain neutral on equities with an overweight on US and underweight EU and EM.
Commodities	
Precious Metals	Gold did not lose its shine – posted strong returns over the week extending its year-to-date gains. Silver and platinum prices rose too. We remain overweight on gold as a risk hedge against ongoing political and (potential) inflationary risks.
Energy	Oil prices recovered some of their losses from the previous weeks. Overall, we believe that oil prices are likely to remain sustained as the market is roughly balanced.
Industrial Metals	Industrial metal prices showed a mixed performance but remained weak overall due to intensifying growth concerns. We do not recommend industrial metals exposure as China reigns in demand.
Currencies	
EURUSD	EUR appreciated against the USD on a relative strength of the European flash PMI compared to the US flash PMI for February. We expect the euro to remain stable.
Critical levels	R2 1.0912 · R1 1.0879 · S1 1.0799 · S2 1.0751
GBPUSD	GBP depreciated against the dollar on worries about the potential EU-UK trade deal not being favorable. We expect the cable to be stable with Pound sterling likely to follow the euro rather than USD.
Critical levels	R2 1.3046 · R1 1.3005 · S1 1.2899 · S2 1.2834
USDJPY	The yen depreciated against the dollar as growth concerns in Japan intensified. BoJ yield curve targeting should put continuing downward pressure on the yen.
Critical levels	R2 112.47 · R1 112.04 · S1 111.33 · S2 111.04

Note: R2, R1, S2 and S1 refer to Bloomberg calculated weekly technical resistance and support levels.

Forthcoming important economic data

United States

	Indicator	Period	Expected	Prior	Comments
02/26/2020	MBA Mortgage Applications	21- Feb		-6.40%	GDP and PCE will be the main releases this week.
02/26/2020	New Home Sales	Jan	715K	694K	
02/27/2020	GDP Annualized QoQ	4Q S	2.10%	2.10%	
02/27/2020	Core PCE QoQ	4Q S	1.30%	1.30%	
02/27/2020	Durable Goods Orders	Jan P	-1.50%	2.40%	
02/27/2020	Initial Jobless Claims	22- Feb	211K	210K	
02/28/2020	Wholesale Inventories MoM	Jan P	0.10%	-0.20%	
02/28/2020	U. of Mich. Sentiment	Feb F	100.7	100.9	

Japan

	Indicator	Period	Expected	Prior	Comments
02/28/2020	Tokyo CPI YoY	Feb	0.50%	0.60%	Inflation releases will be closely watched by the market.
02/28/2020	Tokyo CPI Ex-Fresh Food YoY	Feb	0.60%	0.70%	
02/28/2020	Jobless Rate	Jan	2.20%	2.20%	
02/28/2020	Industrial Production MoM	Jan P	0.20%	1.20%	

Eurozone

	Indicator	Period	Expected	Prior	Comments
02/28/2020	CPI YoY	Feb P	1.70%	1.70%	Eurozone CPI and German GDP will be closely tracked by the market.
02/28/2020	German GDP YoY	Dec	1.60%	1.50%	

United Kingdom

	Indicator	Period	Expected	Prior	Comments
02/28/2020	Nationwide House PX MoM	Feb	0.40%	0.50%	-

China and India

	Indicator	Period	Expected	Prior	Comments
02/29/2020	Manufacturing PMI (CH)	Feb	47.4	50	Manufacturing PMI will be important.

Sources

All information in this report has been obtained from the following sources except where indicated otherwise:

1. Bloomberg
2. Wall Street Journal
3. RTT News
4. Reuters
5. Gulfbase
6. Zawya

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