The Weekly Market View

January 23 2023

ADCB ASSET MANAGEMENT LIMITED

A logical dilemma

Is bad news for the economy good news for the markets, or is it still bad news? Financial markets – after having performed strongly over the past couple of weeks – are now facing this dilemma. Last week, markets received a lot of information pointing in different directions, making it difficult to understand which regime they are in. On the economic data front, Chinese data (Q4'22 GDP, industrial production, retail sales, and fixed asset investment) surprised the consensus expectations on the upside, while US data (retail sales, industrial production, and housing activity) disappointed. Giving some respite for the US was the better-than-expected job market data, and lower-than-expected producer price inflation. Elsewhere too data was mixed. In Germany, ZEW survey expectations were better-than-expected but PPI was higher than expected. In the UK, job market was strong, housing market weakened, and consumer confidence declined. Against this backdrop, signals and actions from central bankers were mixed too. Speaking earlier in the week ECB president Christine Lagarde, Federal Reserve vice-chair Lael Brainard, and Kansas City Fed's Esther George have all reiterated the importance of staying course with hawkish monetary policy. However, some dovish rhetoric came in the form of comments from Fed governor Christopher Waller who backed slowing interest rate increases to a quarter-point at the next Fed policy meeting in February. Turning to signals from the corporate earnings season, based on data from Refinitiv, of the 55 companies in the S&P 500 that have reported earnings to date for Q4'22, 63.6% have reported earnings above analyst estimates. This compares to a long-term average of 66.3% and prior four quarter average of 75.5%. Also, the week was rather clouded by several high-profile companies, such as Microsoft and Alphabet, announcing that they would cut tens of thousands of jobs over the next months. Digesting all this information, financial markets turned a bit volatile last week. Both VIX and MOVE indices rose during the week albeit from relatively low levels. However, our measure of FX market volatility dropped below its long-term average as USD hit a seven-month low during the week. Yields on 10Y USTs touched their four-month lows before rebounding towards end of the week. Global equities posted marginal loss last week after two consecutive weeks of strong gains. Gold prices rose for the fifth straight week on weakness in the broader USD. Weakness in the USD and improving demand outlook from China helped oil prices and industrial commodities.

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Can equities climb the wall of worry in 2023?

Deteriorating growth-inflation mix caused equity markets to drop by c20% during 2022, the biggest decline since 2008. Developed market equities lost 19% while emerging market equity losses touched 22%. Following a bear market year, the outlook can look rather challenging. However, looking back at the history, we notice that over the past 75 years, S&P 500 index has experienced nine drawdowns in excess of 10%. In seven of these nine instances, the index rose by an average of 18% in the following year. The two exceptions followed the extreme events of the oil price shock (1973) and dotcom bubble (2001). Even for other equity indices two consecutive years of losses have been rare. So to that extent, history remains supportive of a positive return year for equities. But the question is if this time is different? For this we look at the two drivers of equity returns – valuations and earnings. First looking at valuations, most of the price drawdown of 2022 came from the contraction in valuation multiples. On our assessment, equity market valuations seem to reflect both higher interest rates and rise in recession probabilities to a large extent. The earnings picture might be a bit challenging this year. For instance, I/B/E/S consensus expects MSCI ACWI earnings to grow 3% in 2023. Whilst this may not be much, we see limited downside risks. Yet in the event our worst-case scenario of a recession does occur, earnings will have scope to fall further. We are carefully watching Q4'22 earnings season for evidence on future trends. Given this situation, we recommend a neutral position on equities and prefer Asian markets; healthcare and industrial global sectors; and large cap and quality factors. For details, see our 2023 Outlook: Peaks and valleys, January 2023.

Global markets' performance snapshot*

Index Snapshot (World Indices)*

Index	Latest	Weekly %	YTD %
S&P 500	3,973	-0.7	3.5
Dow Jones	33,375	-2.7	0.7
Nasdaq	11,140	0.6	6.4
DAX	15,034	-0.4	8.0
Nikkei 225	26,554	1.7	1.8
FTSE 100	7,771	-0.9	4.3
Sensex	60,622	0.6	-0.4
Hang Seng	22,045	1.4	11.4
Regional Markets			
ADX	10,187	-0.2	-0.2
DFM	3,353	0.9	0.5
Tadawul**	10,682	-0.4	1.3
DSM**	10,811	-1.4	1.2
MSM30**	4,798	-1.4	-1.5
BHSE**	1,927	1.9	1.7
KWSE**	7,257	2.0	-0.5
MSCI			
MSCI World	2,725	-0.4	4.7
MSCI EM	1,036	0.6	8.4

Global Commodities, Currencies and Rates*

Commodity	Latest	Weekly %	YTD %
Brent USD/bbl	87.6	2.8	2.0
WTI USD/bbl	81.3	1.8	1.3
Gold USD/t oz	1,928.6	0.9	6.2
Silver USD/t oz	23.9	-1.0	0.5
Platinum USD/t oz	1,024.0	-3.1	-0.7
Copper USD/MT	9,307.8	1.5	11.3
Alluminium	2,582.3	0.6	9.9
Currencies			
EUR USD	1.09	0.2	1.4
GBP USD	1.24	1.4	2.5
USD JPY	129.59	1.3	-1.2
USD CHF	0.92	-0.7	-0.4
Rates	**Latest**	**Weekly (bp)**	**YTD (bp)**
USD Libor 3m	4.82	2.3	4.8
USD Libor 12m	5.35	-1.0	-13.5
UAE Eibor 3m	4.48	-4.1	17.1
UAE Eibor 12m	5.16	15.0	11.6
US 3m Bills	4.57	6.0	27.0
US 10yr Treasury	3.49	-2.7	-34.7

Source: Bloomberg, and ADCB Asset Management
Notes: *Data as of January 20 2023 unless stated otherwise; **Data as of January 19 2023.

Summary market outlook

Global Yields	Yields on 10Y USTs touched their four-month lows before rebounding towards end of the week. Yields on German 10Y government bonds fell through the initial part of the week but rose sharply afterwards to end the week marginally higher as ECB officials indicated larger rate hikes to come. Yields on 10Y JGBs fell sharply as BoJ stayed course with its yield curve control in contradiction to market expectations. Bond yields and prices are inversely correlated. i.e. yields rise when prices fall and vice versa. Overall, we recommend adding duration on USTs (7-10Y segment) as growth slowdown occurs and recession fears rise.
Stress and Risk Indicators	Volatility increased last week as financial markets digested economic data releases, comments from monetary policy makers, and corporate earnings releases. Both VIX and MOVE indices rose during the week, albeit from relatively low levels. SKEW index, a measure of tail risks remained low. However, our measure of FX market volatility dropped below its long-term average. We expect financial market volatility to stay elevated as the monetary policy normalizes and markets weigh recession probabilities.
Equity Markets	
Local Equity Markets	MSCI GCC index posted marginal loss and underperformed global equities last week despite the strength in oil prices. Amongst major markets, Kuwait and Dubai posted gains while Qatar, Saudi and Abu Dhabi registered losses. We stay neutral GCC equities within our global equity framework. Stable to higher oil prices, potential for revival in growth prospects, and scope for reversing the underperformance of the past several years are all balanced by lack of structural growth plays in the equity market indices.
Global Equity Markets	Global equities posted marginal loss last week after two consecutive weeks of strong gains. EMs continued to outperform DMs. Within EM, markets in Asia outperformed their smaller peers in LatAm and EMEA. Within the developed world, Canada and UK outperformed while Japan and US underperformed in USD terms. Sector wise, communication services, and IT outperformed the most while utilities and consumer staples underperformed the most. We are moderately overweight US, UK, and Asia Pacific; underweight Eurozone and EMs outside Asia. By sector we prefer healthcare, and industrials. Our strategic preference is for large cap non-cyclical growth with focus on quality. Our other high conviction ideas include clean energy themes (for medium to long-term); aerospace & defence, food security, energy security, and cybersecurity as plays on rising geopolitical tensions and deglobalization; and consumer services, airlines, and hotels, restaurants & leisure as plays on re-opening.
Technology Segments	Nasdaq-100 index gained 0.7% over the week while HK tech index was rather flat. Within technology, we prefer non-cyclical growth over cyclical growth (tech hardware, semiconductors etc.) over a 12-month horizon.
Commodities	
Precious Metals	Gold prices rose for the fifth straight week on weakness in the broader USD. Silver and platinum prices fell marginally. We are overweight gold as a hedge against potential inflation, growth, and geopolitical risks.
Energy	Weakness in the USD and improving demand outlook from China helped oil prices rise for the second straight week. Overall, over the medium-term we believe that oil prices will remain sustained as the market balances into the new normal.
Industrial Metals	Industrial metal prices rose on improving Chinese demand outlook. USD weakness helped. Another commodity super-cycle is difficult, yet demand for commodities linked to “green infrastructure” is likely to sustain.
Currencies	
EURUSD	Weakness in the broader USD which hit a seven-month low during the week helped EUR gain further relative ground. We expect euro to stabilize and record a better performance in 2023 compared to 2022.
Critical levels	R2 1.0957 · R1 1.0906 · S1 1.0786 · S2 1.0717
GBPUSD	GBP strengthened against the USD in part due to the weakness in the latter and in part due to still elevated inflation in the UK. We expect GBP to weaken against EUR and stay flat versus the USD.
Critical levels	R2 1.2600 · R1 1.2499 · S1 1.2233 · S2 1.2068
USDJPY	After falling sharply in recent months, USDJPY rose strongly last week as BoJ’s status quo disappointed markets. JPY is likely to strengthen in 2023 as interest rate differentials tighten, and as broad USD weakens.
Critical levels	R2 133.82 · R1 131.71 · S1 127.36 · S2 125.12

Forthcoming important economic data/events

United States

Date & Time (GST)	Indicator	Period	Expected	Prior
01/24/23 18:45	**S&P Global US Manufacturing PMI**	**Jan P**	**--**	**46.2**
01/24/23 18:45	**S&P Global US Services PMI**	**Jan P**	**--**	**44.7**
01/25/23 16:00	MBA Mortgage Applications	20-Jan	--	27.90%
01/26/23 17:30	**GDP Annualized QoQ**	**4Q A**	**2.90%**	**3.20%**
01/26/23 17:30	Wholesale Inventories MoM	Dec P	--	1.00%
01/26/23 17:30	**Initial Jobless Claims**	**21-Jan**	**--**	**--**
01/26/23 17:30	**Continuing Claims**	**14-Jan**	**--**	**--**
01/26/23 17:30	Durable Goods Orders	Dec P	2.90%	-2.10%
01/26/23 19:00	New Home Sales	Dec	615k	640k
01/27/23 17:30	Personal income	Dec	0.20%	0.40%
01/27/23 17:30	Personal spending	Dec	-0.10%	0.10%
01/27/23 17:30	**PCE Deflator YoY**	**Dec**	**--**	**5.50%**
01/27/23 17:30	**PCE Core Deflator YoY**	**Dec**	**4.40%**	**4.70%**
01/27/23 19:00	**U. of Mich. Sentiment**	**Jan F**	**64.6**	**64.6**
01/27/23 19:00	U. of Mich. Current Conditions	Jan F	--	68.6
01/27/23 19:00	U. of Mich. 1 Yr Inflation	Jan F	--	4.00%
01/27/23 19:00	U. of Mich. 5-10 Yr Inflation	Jan F	--	3.00%

Japan

Date & Time (GST)	Indicator	Period	Expected	Prior
01/24/23 04:30	**Jibun Bank Japan PMI Mfg**	**Jan P**	**--**	**48.9**
01/24/23 04:30	**Jibun Bank Japan PMI Services**	**Jan P**	**--**	**51.1**
01/24/23 09:30	Nationwide Dept Sales YoY	Dec	--	4.50%
01/25/23 09:00	Leading Index CI	Nov F	--	97.6
01/25/23 09:00	Coincident Index	Nov F	--	99.1
01/26/23 03:50	PPI Services YoY	Dec	--	1.70%
01/26/23 10:00	Machine Tool Orders YoY	Dec F	--	1.00%
01/27/23 03:30	**Tokyo CPI YoY**	**Jan**	**4.00%**	**4.00%**
01/27/23 03:30	**Tokyo CPI Ex-Fresh Food, Energy YoY**	**Jan**	**2.90%**	**2.70%**

Eurozone

Date & Time (GST)	Indicator	Period	Expected	Prior
01/24/23 13:00	**Eurozone S&P Global Manufacturing PMI**	**Jan P**	**--**	**47.8**
01/24/23 13:00	Eurozone S&P Global Services PMI	Jan P	--	49.8
01/24/23 11:00	**Germany GfK Consumer Confidence**	**Feb**	**--**	**-37.8**
01/24/23 12:30	**Germany S&P Global/BME Manufacturing PMI**	**Jan P**	**--**	**47.1**
01/24/23 12:15	**France S&P Global Manufacturing PMI**	**Jan P**	**--**	**49.2**
01/25/23 13:00	**Germany IFO Expectations**	**Jan**	**--**	**83.2**
01/27/23 - 02/02/23	Germany Retail Sales MoM	Dec	--	1.10%
01/27/23 11:45	France Consumer Confidence	Jan	--	82

United Kingdom

Date & Time (GST)	Indicator	Period	Expected	Prior
01/24/23 13:30	**S&P Global/CIPS UK Manufacturing PMI**	**Jan P**	**45.3**	**--**
01/24/23 13:30	**S&P Global/CIPS UK Services PMI**	**Jan P**	**49.9**	**--**
01/28/23 - 02/03/23	Nationwide House Px NSA YoY	Jan	2.80%	--

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