The Weekly Market View

May 08 2023

ADCB ASSET MANAGEMENT LIMITED

Climbing the wall of worry

Last week started with renewed concerns of the banking sector stress in the US. Over the previous weekend, regulators took control of First Republic bank which was eventually acquired by JPMorgan Chase. Further, the US debt ceiling issues came to the fore with Treasury Secretary Janet Yellen notifying congressional leaders in a letter which brought forward the potential X-date to as early as June 1. Data from the US Department of Labor showed that the number of job openings fell for a third consecutive month in March. However, non-farm payrolls data was a mixed bag – it showed that 253,000 jobs were added (consensus: 180,000). But data for March was revised lower to 165,000 (previously reported: 236,000). Average hourly earnings rose at an annual rate of 4.4% (consensus: 4.2%). Staying with the US, as we expected, the US Fed raised its policy rate by 25bp to 5.00%-5.25% – its highest since 2007; and indicated that rates might now be close to the peak. Reduction of holdings of Treasury securities and agency debt and agency mortgage-backed securities continues as per plan (at the rate of USD95bn per month). Corporate news was much better than expected. According to Refinitiv, of the 419 companies in the S&P 500 that have reported earnings to date for Q1'23, 77.1% have surprised positively (vs. long-term average of 66.3% and prior four quarter average of 73.5%). Across the Atlantic, the European Central Bank (ECB) raised interest rates by 25bp, scaling back from previous 50bp increases. ECB also said it would halt its program of reinvesting money from its bond purchases by July. Inflation in Eurozone showed mixed trends with the headline accelerating but the core number ticking down unexpectedly. Eurozone retail sales for March fell and came in lower than expected. On the PMIs, data out of US and India surprised to the upside while the data from China disappointed. Despite these concerns, financial markets held up relatively well.

When the Fed pauses…

Looking at the past 10 interest rate cycles, the more recent episodes of 1997, 2000, 2006, and 2018 saw Fed pausing interest rate hikes but holding them at that level for at least six months. In the instances of more distant history, the Fed had to cut interest rates soon after hitting a peak. We see two reasons behind this divergence of Fed behavior more recently vs. in distant history. First, lower volatility in growth and inflation during recent decades allowed the central banks to hold on to elevated rates. In the more distant history, volatility was pervasive, so the central banks had to cut interest rates soon after raising them to the peak. The second reason is the levels of interest rates – which are low in recent decades compared to those in the more distant history. For example, the average peak rate in the six instances prior to 1997 was 12.3% while the average of the more recent four episodes is just under 5%. We think this interest rate cycle has characteristics of both pre-1997 and post-1997 episodes. Looking at all 10 historical episodes of Fed pause, we generally find global equities performing strongly across 1-, 3-, 6-, and 12-month periods following the Fed pause. We observe the general outperformance of non-US equity markets, but US market performances tend to be the most consistent. Sector wise, equities of all 11 GICS sectors post gains 12 months after the Fed pause. Turning to fixed income, there too we observe that strong gains followed the Fed pause. EM external bonds and global high yield outperformed strongly in the subsequent 12-month period. Commodities rose marginally 3 months after the Fed pause but fell subsequently. Gold prices showed mixed performances across instances. After having strengthened previously the broader USD stabilized following the last Fed rate hike but EM FX strengthened against the USD. In general, history suggests that risk-on follows the Fed pause. While there are similarities, there are also some differences between the current episode and the previous instances when the Fed paused. For instance, weaker outlook reflected in economic and earnings forecasts, still elevated inflation, banking sector stress, the looming debt ceiling in the US, and elevated geopolitical tensions could dial down the enthusiasm this time.

Kishore Muktinutalapati
Head - Investment Strategy
Tel: +971 (0)2 696 2358
kishore.muktinutalapati@adcb.com

Prerana Seth
Fixed Income Strategist
Tel: +971 (0)2 696 2878
prerana.seth@adcb.com

Mohammed Al Hemeiri
Analyst
Tel: +971 (0)2 696 2236
mohammed.alhemeiri@adcb.com

Ahmed Al Falahi
Analyst
Tel: +971 (0)2 497 3934
ahmed.a5@adcb.com

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Global markets' performance snapshot*

Index Snapshot (World Indices)*

Index	Latest	Weekly %	YTD %
S&P 500	4,136	-0.8	7.7
Dow Jones	33,674	-1.2	1.6
Nasdaq	12,235	0.1	16.9
DAX	15,961	0.2	14.6
Nikkei 225	29,158	1.0	11.7
FTSE 100	7,778	-1.2	4.4
Sensex	61,054	-0.1	0.4
Hang Seng	20,049	0.8	1.4
Regional Markets			
ADX	9,706	-0.9	-5.0
DFM	3,583	1.1	7.4
Tadawul**	11,119	-1.7	5.4
DSM**	10,640	4.5	-0.4
MSM30**	4,724	0.1	-3.1
BHSE**	1,906	0.1	0.6
KWSE**	7,034	-1.5	-3.6
MSCI			
MSCI World	2,822	-0.5	8.4
MSCI EM	982	0.5	2.6

Global Commodities, Currencies and Rates*

Commodity	Latest	Weekly %	YTD %
Brent USD/bbl	75.3	-5.3	-12.4
WTI USD/bbl	71.3	-7.1	-11.1
Gold USD/t oz	2,011.6	1.1	10.8
Silver USD/t oz	25.6	2.2	7.9
Platinum USD/t oz	1,044.0	-2.8	1.3
Copper USD/MT	8,560.3	-0.2	2.3
Alluminium	2,316.8	-2.2	-1.4
Currencies			
EUR USD	1.10	0.0	2.9
GBP USD	1.26	0.5	4.5
USD JPY	134.85	-1.1	2.8
Rates	**Latest**	**Weekly (bp)**	**YTD (bp)**
SOFR	5.06	25.0	76.0
USD Libor 3m	5.34	3.4	57.0
USD Libor 12m	5.20	-16.7	-28.2
UAE Eibor 3m	5.21	21.7	89.8
UAE Eibor 12m	5.20	-3.2	15.4
US 3m Bills	5.10	15.0	80.0
US 10yr Treasury	3.44	0.7	-39.7

Source: Bloomberg, and ADCB Asset Management
Notes: *Data as of May 05 2023 unless stated otherwise; **Data as of May 04 2023.

Summary market outlook

Global Yields	10Y UST yields fell during the initial days of the week due to bank sector stresses but rose subsequently on strong job market data – ending the week higher. Yields on 10Y German bunds fell to a one-month low. Yields on 2Y USTs and German bunds declined. Yield on 10Y JGBs was largely unchanged over the week. Bond yields and prices are inversely correlated. i.e. yields rise when prices fall and vice versa. Overall, we maintain our slight duration exposure with preference for USTs (7-10Y segment).
Stress and Risk Indicators	VIX index (measure of implied volatility in equities) rose sharply through the initial half of the week but fell subsequently – ending the week marginally higher. MOVE Index (measure of bond volatility) moved higher too. 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 posted losses and underperformed global equities as oil prices declined further over the past week. Within the region Qatar and Dubai stocks posted gains while the heavy-weights Saudi, Abu Dhabi and Kuwait posted 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 losses despite a number of headwinds. EM outperformed DM. Within DM, Japan (shortened trading week) outperformed while US and UK underperformed. Amongst EMs, LatAm and Asia outperformed. Sector wise, IT, healthcare, and utilities posted gains while energy, communication services, and financials sectors posted losses and underperformed. We are overweight North America, and Asia Pacific ex Japan; underweight Europe 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 HK equities and Chinese hotels & leisure (beneficiaries of the post-pandemic reopening of the Chinese economy), Cybersecurity and Chinese Semiconductors (play on rising deglobalisation risks and national security prominence), and US Diversified banks over US Regional banks (Diversified banks in the US do not have same risks that regional banks carry).
Technology Segments	Nasdaq-100 index recorded gains of 0.7% while HK tech index posted marginal loss. In the US, IT sector has been reporting strong positive earnings surprises with more than 90% of the companies there reporting better than expected earnings during Q1'23.
Commodities	
Precious Metals	Resurgent Chinese demand and concerns surrounding US banks push gold prices closer to their record-highs. We are overweight gold as a hedge against potential inflation, growth, and geopolitical risks.
Energy	Oil prices fell for the third straight week on concerns of global growth. Overall, over the medium-term we believe that oil prices will remain sustained as the market balances into the new normal.
Industrial Metals	Concerns of global slowdown and weaker-than-expected Chinese data led to decline in the prices of industrial metals. Another commodity super-cycle is difficult, yet demand for commodities linked to "green infrastructure" is likely to sustain.

Currencies								
EURUSD	EUR/USD stayed flat as both the US Fed and ECB raised their policy rates by 25bp each. We expect euro to stabilize and record a better performance in 2023 compared to 2022.							
Critical levels	R2	1.1068	R1	1.1056	S1	1.1023	S2	1.1002
GBPUSD	GBP/USD rose close to one-year high. GBP/EUR rose to a one-month high as markets awaited Bank of England decision this week. We expect GBP to weaken against EUR and stay flat versus the USD.							
Critical levels	R2	1.2680	R1	1.2668	S1	1.2634	S2	1.2612
USDJPY	USD/JPY fell sharply on concerns around the banking sector in the US. Yen is likely to strengthen in 2023 as interest rate differentials tighten, and as broad USD weakens.							
Critical levels	R2	135.52	R1	135.09	S1	134.45	S2	134.24

Forthcoming important economic data/events

United States

Date & Time (GST)	Indicator	Period	Expected	Prior
05/08/2023 18:00	Wholesale Inventories MoM	Mar F	0.10%	0.10%
05/09/2023 14:00	NFIB Small Business Optimism	Apr	89.7	90.1
05/10/2023 15:00	MBA Mortgage Applications	5-May	--	-1.20%
05/10/2023 16:30	**CPI YoY**	**Apr**	**5.00%**	**5.00%**
05/10/2023 16:30	**CPI Ex Food and Energy YoY**	**Apr**	**5.40%**	**5.60%**
05/10/2023 22:00	Monthly Budget Statement	Apr	--	-$378.1b
05/11/2023 16:30	**PPI Final Demand MoM**	**Apr**	**0.30%**	**-0.50%**
05/11/2023 16:30	**PPI Ex Food and Energy MoM**	**Apr**	**0.20%**	**-0.10%**
05/11/2023 16:30	Initial Jobless Claims	6-May	--	--
05/11/2023 16:30	Continuing Claims	29-Apr	--	--
05/11/2023 16:30	**PPI Final Demand YoY**	**Apr**	**2.40%**	**2.70%**
05/11/2023 16:30	**PPI Ex Food and Energy YoY**	**Apr**	**3.30%**	**3.40%**
05/12/2023 18:00	**U. of Mich. Sentiment**	**May P**	**62.6**	**63.5**
05/12/2023 18:00	**U. of Mich. Current Conditions**	**May P**	**--**	**68.2**
05/12/2023 18:00	**U. of Mich. Expectations**	**May P**	**--**	**60.5**
05/12/2023 18:00	**U. of Mich. 1 Yr Inflation**	**May P**	**--**	**4.60%**
05/12/2023 18:00	**U. of Mich. 5-10 Yr Inflation**	**May P**	**--**	**3.00%**

Japan

Date & Time (GST)	Indicator	Period	Expected	Prior
05/08/2023 04:30	Jibun Bank Japan PMI Composite	Apr F	--	52.5
05/08/2023 04:30	**Jibun Bank Japan PMI Services**	**Apr F**	**--**	**54.9**
05/09/2023 03:30	Labor Cash Earnings YoY	Mar	1.00%	1.10%
05/09/2023 03:30	Household Spending YoY	Mar	0.80%	1.60%
05/10/2023 09:00	Leading Index CI	Mar P	97.9	98
05/10/2023 09:00	Coincident Index	Mar P	98.8	98.6
05/11/2023 03:50	**BoP Current Account Balance**	**Mar**	**¥2865.3b**	**¥2197.2b**
05/11/2023 03:50	**BoP Current Account Adjusted**	**Mar**	**¥1291.0b**	**¥1089.2b**
05/11/2023 03:50	**Trade Balance BoP Basis**	**Mar**	**-¥450.6b**	**-¥604.1b**
05/12/2023 03:50	**Money Stock M2 YoY**	**Apr**	**--**	**2.60%**
05/12/2023 03:50	Money Stock M3 YoY	Apr	--	2.10%

Eurozone

Date & Time (GST)	Indicator	Period	Expected	Prior
05/08/2023 10:00	**Germany Industrial Production WDA YoY**	**Mar**	**--**	**0.60%**
05/08/2023 12:30	**Eurozone Sentix Investor Confidence**	**May**	**--**	**-8.7**
05/10/2023 10:00	**Germany CPI YoY**	**Apr F**	**--**	**7.20%**
05/10/2023 10:00	**Germany CPI EU Harmonized YoY**	**Apr F**	**--**	**7.60%**
05/11/2023 05/16	Germany Wholesale Price Index YoY	Apr	--	2.00%
05/12/2023	Germany Current Account Balance	Mar	--	22.6b
05/12/2023 10:45	**France CPI EU Harmonized YoY**	**Apr F**	**--**	**6.90%**
05/12/2023 10:45	**France CPI YoY**	**Apr F**	**--**	**5.90%**

United Kingdom

Date & Time (GST)	Indicator	Period	Expected	Prior
05/11/2023 03:01	RICS House Price Balance	Apr	--	-43%
05/11/2023 15:00	**Bank of England Bank Rate**	**11-May**	**4.50%**	**4.25%**
05/12/2023 10:00	Monthly GDP (MoM)	Mar	--	0.00%
05/12/2023 10:00	**Industrial Production MoM**	**Mar**	**--**	**-0.20%**
05/12/2023 10:00	**Manufacturing Production MoM**	**Mar**	**--**	**0.00%**
05/12/2023 10:00	Index of Services MoM	Mar	--	-0.10%
05/12/2023 10:00	Index of Services 3M/3M	Mar	--	0.10%
05/12/2023 10:00	**GDP QoQ**	**1Q P**	**--**	**0.10%**
05/12/2023 10:00	**GDP YoY**	**1Q P**	**--**	**0.60%**
05/12/2023 10:00	Private Consumption QoQ	1Q P	--	0.20%
05/12/2023 10:00	Government Spending QoQ	1Q P	--	0.50%
05/12/2023 10:00	Exports QoQ	1Q P	--	-1.40%
05/12/2023 10:00	Imports QoQ	1Q P	--	-0.20%
05/12/2023 10:00	Total Business Investment QoQ	1Q P	--	-0.20%
05/12/2023 10:00	Total Business Investment YoY	1Q P	--	10.80%

China and India

Date & Time (GST)	Indicator	Period	Expected	Prior
05/09/2023	China Exports YoY	Apr	8.50%	14.80%
05/09/2023	China Imports YoY	Apr	-0.50%	-1.40%
05/09/2023	China Trade Balance	Apr	$73.00b	$88.19b
05/09/2023 05/15	China Aggregate Financing CNY	Apr	1945.0b	5380.0b
05/09/2023 05/15	**China Money Supply M2 YoY**	**Apr**	**12.60%**	**12.70%**
05/09/2023 05/15	China New Yuan Loans CNY	Apr	1350.0b	3890.0b
05/11/2023 05:30	**China CPI YoY**	**Apr**	**0.30%**	**0.70%**
05/11/2023 05:30	**China PPI YoY**	**Apr**	**-3.20%**	**-2.50%**
05/12/2023	China BoP Current Account Balance	1Q P	--	$103.1b
05/12/2023 16:00	**India Industrial Production YoY**	**Mar**	**--**	**5.60%**
05/12/2023 16:00	**India CPI YoY**	**Apr**	**4.85%**	**5.66%**

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