The Weekly Market View

October 04 2021

ADCB ASSET MANAGEMENT LIMITED

Mini taper tantrum?

Last week, markets witnessed three main fears over 1) DM central bank policy exits 2) inflation pressures reigniting and 3) China growth slowdown risks. Fed's hawkish bias continued to make market participants uncomfortable amidst increasing evidence of sticky price pressures. Inflation concerns reignited on the back of the supply chain bottlenecks, also indicated in the latest inflation releases. Core PCE- Fed's preferred gauge of inflation- matched consensus estimates but remained high at 3.6% yoy, driven by goods inflation. In Europe, CPI numbers surprised on the upside, reaching the highest level since September 2008. German inflation data showed the CPI hitting a 29yr high. In addition, domestic fuel prices in the UK continued to surge amidst fuel shortages. Oil prices rose amidst the supply-side concerns, pushing inflation expectations higher. Global equity markets suffered losses on fear of inflation and potentially tighter monetary policy. MSCI ACWI lost more than 2% over the week. EM outperformed DM. Within DM, UK and Canada outperformed while Europe ex UK and Japan underperformed in USD total return terms. By sector, except for energy, all other sectors posted losses. IT, health care, and industrials underperformed the most. In fixed income, Bloomberg Barclays Global Aggregate bond index recorded another week of losses, due to the rally in long-term UST yields. 10yr UST yield climbed to a three-month high. Core Eurozone bond yields and UK gilt yields also jumped on the back of inflation concerns. US IG corporate bond index declined while US HY was relatively resilient on the back of higher oil prices. EM bonds suffered amidst the backdrop of rising UST yield and stronger dollar bias. Gold prices added gains despite the monetary tightness and inflation concerns. Industrial metals remained under pressure due to China growth slowdown concerns.

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Positioning for policy normalisation and inflation risk

Bond markets are getting increasingly apprehensive about the looming taper risk, possibility of earlier policy normalisation and evidence of sticky inflation. Price pressures have not softened even with the base-effects wearing off. Given the supply driven characteristic of inflation pressures, which generally is short-term in nature, the likelihood of stagflation scenario remains low. However, it is also difficult to predict how and when the bottlenecks will start to phase out. Adding to the inflation concerns is the central bank communication regarding policy exits. US Treasury market has experienced increased volatility since the September FOMC meeting. In fact, Bloomberg Barclays US Treasury index is now headed to have the worst year since 2013. While the yield curve has fairly steepened recently, front-end bonds have not escaped from the sell-off. This is mainly with the markets repricing the rate hike expectations after the release of more aggressive median rate projections for 2024 by the Fed. We believe that market is getting aggressive again in pricing earlier rate hikes. The Fed will remain patient after completing the taper process, especially on the back of growth uncertainties which could flare-up over the year. However, long-term bond yields could continue to face volatility as they still remain low compared to the Fed's long-term neutral rate ahead of the Fed taper. As a result, we recommend staying short-duration on USTs amidst the uncertainties over Fed policy and inflation pressures. Elsewhere, we stay neutral on US IG- which could also remain under pressure due to its long-duration characteristics We remain underweight on US HY- which surprisingly has been resilient in the recent sell-off but case for wider spreads remains given the extremely tight valuations. In EM, we stay neutral of EM USD sovereigns and selectively overweight on Brazil USD sovereign, Russia USD sovereign and high-quality GCC sovereigns. In EM corporate, we remain overweight on Asia IG credit.

Global markets' performance snapshot

Index Snapshot (World Indices)

Index	Latest	Weekly %	YTD %
S&P 500	4,357	-2.2	16.0
Dow Jones	34,326	-1.4	12.2
Nasdaq	14,567	-3.2	13.0
DAX	15,156	-2.4	10.5
Nikkei 225	28,771	-4.9	4.8
FTSE 100	7,027	-0.3	8.8
Sensex	58,766	-2.1	23.1
Hang Seng	24,664	1.6	-9.8
Regional Markets (Sunday to Thursday)			
ADX	7,699	-1.6	53.0
DFM	2,845	0.2	13.7
Tadawul	11,496	2.0	32.1
DSM	11,485	2.2	9.8
MSM30	3,943	0.4	7.8
BHSE	1,706	0.2	14.5
KWSE	6,865	-0.2	24.0
MSCI			
MSCI World	3,007	-2.6	12.4
MSCI EM	1,253	-1.5	-3.5

Global Commodities, Currencies and Rates

Commodity	Latest	Weekly %	YTD %
ICE Brent USD/bbl.	79.3	1.5	53.1
Nymex WTI USD/bbl	75.9	2.6	56.4
Gold USD/t oz	1,761.0	0.6	-7.2
Silver USD/t oz	22.5	0.5	-14.6
Platinum USD/t oz	977.1	-0.8	-8.9
Copper USD/MT	9,113.0	-1.7	17.7
Alluminium	2,845.0	-2.2	43.8
Currencies			
EUR USD	1.16	-1.1	-5.1
GBP USD	1.35	-1.0	-0.9
USD JPY	111.05	0.3	7.0
CHF USD	0.93	0.7	-4.9
Rates	**Latest**	**Weekly (bp)**	**YTD(bp)**
USD Libor 3m	0.13	0.1	-10.5
USD Libor 12m	0.23	0.5	-10.7
UAE Eibor 3m	0.36	-8.9	-14.9
UAE Eibor 12m	0.44	0.9	-21.8
US 3m Bills	0.03	0.5	-2.8
US 10yr Treasury	1.46	1.1	54.8

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Summary market outlook

Global Yields	Yields on 10Y US treasuries rose to the highest level in three months on potential taper of asset purchases and eventual interest rate raises. Core Eurozone bond yields and UK gilt yields jumped on inflation concerns. US IG corporate bonds registered losses. Overall, we recommend a lower duration stance (5Y US Treasuries) in anticipation of interest rate volatility in the near term.
Stress and Risk Indicators	VIX index jumped amidst the equity market sell-off. We think the VIX index is unlikely to fall back to the pre-pandemic levels until the virus comes fully under control.
Equity Markets	
Local Equity Markets	Local equity markets held up relatively well amidst the global equity sell-off and outperformed broader equity benchmarks as oil prices continued to rise. Within the region, Saudi Arabia and Qatar equities outperformed while Abu Dhabi and Kuwait equities underperformed last week. Performance across the region was driven by heavy-weight financials sector. We remain neutral GCC equities within our global equity framework. Stable to higher oil prices, potential for revival in growth and scope for reversing the underperformance of 2020 are all balanced by lack of structural growth plays in the equity markets.
Global Equity Markets	Global equity markets came under pressure on fear of inflation and potentially tighter monetary policy. MSCI ACWI lost more than 2% over the week. EM outperformed DM. Within DM, UK and Canada outperformed while Europe ex UK and Japan underperformed in USD total return terms. By sector, except for energy, all other sectors posted losses. IT, health care, and industrials underperformed the most. From a strategy view point, we are moderately overweight US, UK, and Asia Pacific; underweight Eurozone and EMs outside Asia. By sector we prefer industrials, IT, and communication services. Our strategic preference is for large cap non-cyclical growth with focus on quality. 'Build back better' themes including green recovery, digitalization and health care innovation are likely to do well. Yet, in the very near-term, as the new wave of COVID-19 fear subsides, we see opportunities in cyclicals, value, and re-opening sectors.
Technology Segments	Structural themes came under pressure as inflation concerns persisted. Nasdaq-100, an index comprising of new economy thematic plays in the US, lost more than 3% over the past week. HK Tech index, a measure of Chinese technology stocks, lost only 1% and outperformed technology segments elsewhere.
Commodities	
Precious Metals	Gold prices jumped on increased preference for safe-haven assets as USTs sold-off on Fed tightening expectations. We keep our overweight in gold as a hedge against potential risks on the horizon.
Energy	Oil prices jumped on the back of supply side concerns and expectations of higher demand during winter. Overall, we believe that oil prices will remain sustained as the market approaches a balance.
Industrial Metals	Industrial metal prices suffered losses as sentiment towards China growth outlook remained weak. While another commodity super-cycle appears difficult, demand for commodities linked to environmental friendly green infrastructure is likely to sustain.
Currencies	
EURUSD	EUR fell against the USD earlier on the back of stronger dollar bias. Re-opening is a positive for EUR while risk-off sentiment and the easier policy are moderately negative.
Critical levels	**R2** 1.1799 **R1** 1.1698 **S1** 1.1529 **S2** 1.1461
GBPUSD	Cable ended the week marginally weaker. We expect the cable to be driven by how the re-opening plays out over the near-term and to decouple from the EUR.
Critical levels	**R2** 1.3879 **R1** 1.3713 **S1** 1.3396 **S2** 1.3245
USDJPY	Divergence in outlook for monetary policies in the US and Japan caused JPYUSD to fall to its lowest level since July. Over the medium-term, we believe that BoJ yield curve targeting should put downward pressure on JPY.
Critical levels	**R2** 112.76 **R1** 111.91 **S1** 110.37 **S2** 109.68

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

Forthcoming important economic data/events

United States

	Indicator	Period	Expected	Prior	Comments
10/04/21	Factory Orders	Aug	1.00%	0.40%	Market attention will be on labour market payroll data. Also, durable goods orders, MBA mortgage applications, and initial jobless claims will be important.
10/04/21	Durable Goods Orders	Aug F	1.80%	1.80%	
10/05/21	Trade Balance	Aug	-$70.6b	-$70.1b	
10/05/21	Markit Services PMI	Sep F	54.4	54.4	
10/05/21	Markit Composite PMI	Sep F	--	54.4	
10/05/21	ISM Services Index	Sep	59.9	61.7	
10/06/21	MBA Mortgage Applications	1-Oct	--	-1.10%	
10/07/21	Initial Jobless Claims	2-Oct	350K	362K	
10/08/21	Unemployment Rate	Sep	5.10%	5.20%	
10/08/21	Change in non-farm payrolls	Sep	470k	235k	
10/08/21	Average Hourly Earnings MoM	Sep	0.40%	0.60%	
10/08/21	Labor Force Participation Rate	Sep	61.70%	61.70%	
10/08/21	Underemployment Rate	Sep	--	8.80%	
10/08/21	Wholesale Inventories MoM	Aug	--	2.00%	

Japan

	Indicator	Period	Expected	Prior	Comments
10/05/21	Tokyo CPI YoY	Sep	-0.10%	-0.40%	Inflation releases will be closely watched by the market.
10/05/21	Tokyo CPI Ex-Fresh Food YoY	Sep	0.20%	0.00%	
10/05/21	Jibun Bank PMI Services	Sep F	--	47.4	
10/05/21	Jibun Bank PMI Composite	Sep F	--	47.7	
10/08/21	BoP Current Account Balance	Aug	¥1486.0b	¥1910.8b	

Eurozone

	Indicator	Period	Expected	Prior	Comments
10/05/21	Markit Services PMI	Sep F	56.1	56.3	PPI will be important.
10/05/21	Markit Composite PMI	Sep F	56.1	56.1	
10/05/21	PPI YoY	Aug	13.50%	12.10%	
10/08/21	Unemployment Rate	Sep	6.90%	7.10%	

United Kingdom

	Indicator	Period	Expected	Prior	Comments
10/05/2021	Markit/CIPS Services PMI	Sep F	54.6	54.6	PMI releases will be the main focus.
10/05/2021	Markit/CIPS Composite PMI	Sep F	54.1	54.1	

China and India

	Indicator	Period	Expected	Prior	Comments
10/07/21	China Foreign Reserves	Sep	--	$3232.12b	All eyes will be on China September releases for foreign reserves, and PMI releases. In India the focus will be on RBI meeting.
10/08/21	China Caixin PMI Composite	Sep	--	47.2	
10/08/21	China Caixin PMI Services	49.2	46.7	50.1	
10/08/21	India RBI MPC Meeting	8- Oct	No Change		
10/09/21	China Aggregate Financing CNY	Sep	--	2960.0b	
10/09/21	China New Yuan Loans CNY	Sep	--	1120.0b	

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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