Monday, August 22, 2022

Views from the desk

Global Market Overview and Outlook

Issue # 801

Sandeep S Jadwani – ASCI,CIB
Head Of Investment Advisory
Habib Investment Ltd, DIFC

Market Overview

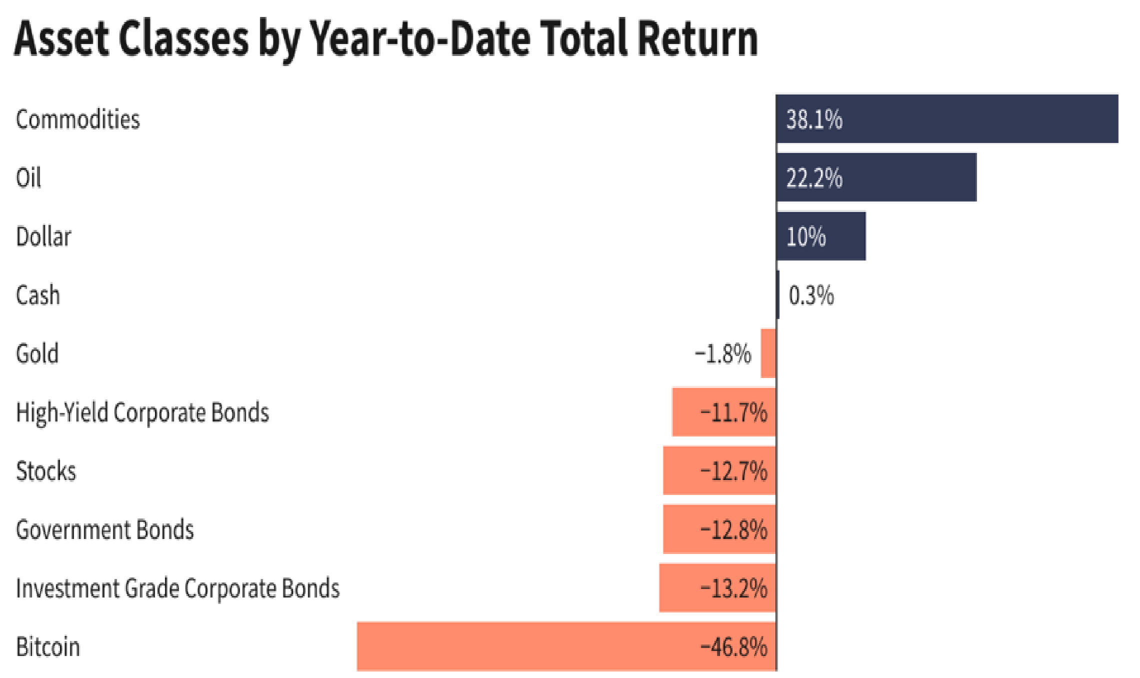
2022 marks the worst start and worst H1 for global markets across Equities and Fixed income across the board. Clear winners were commodities & rightly so with inflation numbers topping the charts there was no debate on this.

Markets have faced a huge list of concerns including **Surging Inflation**, **Central Bank Tightening, Pace of Interest Rate hikes, Covid 19 Lockdown and economic slowdown in China, Escalating and dragged Russia/Ukraine war, Sino US tensions triggered by official US visit to Taiwan, energy supplies into Europe and European winter on the horizon.**

These issues are now well understood by the market participants and the risk is being priced in modestly. With expectations of inflation being peaked in the US released July 2022 (9.1%) followed by 8.5% released in August 2022. While the US has taken reactive steps towards bringing inflation down, other parts of the world like EU and UK have been lagging in their policy response to tackle inflation without dampening growth and fears of a hard landing.

The uncertainties, bring out two possibilities of a slowdown or mild recession in the near term but a full-blown recessionary impact in H2,2023 and a deep recession could trigger a large equity BEAR market. Though the Q2 earnings do not discount the same yet.

Bull v/s Bear : It's Time Out as markets remain on the sidelines untill more date is released to undertand policy stance. What are the odds?



Source : Bank Of America Research (as on 1st August 2022)

Where are we heading ?

Rebalancing and Rotation across asset classes

It is believed that a neutral risk stance relative to the benchmark is appropriate. Given that a global slowdown is anticipated, expect modest positive returns with narrow dispersion in performance between fixed income and equities.

In such an environment, it is prudent to be slight overweight to equities relative to fixed income, with **equity exposure** tilted to defensive sectors, and quality and low volatility stocks. US is preferred over developed markets ex-US, but relatively equally weighted to both developed markets and emerging markets.

Within **fixed income**, prefer quality credit and are neutral on duration with a long tilt eventually. Fixed rate investment grade and municipal bonds are specific areas of potential opportunity.

Within **alternatives**, ESG themed energy, value add real estate, and core plus infrastructure with a staggered buy-in.

Fundamentally, the **Middle East** is in a world of its own, with twin surpluses of 25% to 50%, mid to high single digit GDP growth, relatively subdued inflation, and largescale reform. Furthermore, with 60% of the MSCI Middle East Index being in banks, it is positively geared to any Fed rate hikes. We expect MENA equities to deliver positive return in the 2H of the year. We expect the region to continue to structurally outperform EM on reforms, maintain higher for longer energy prices, and have low foreign positioning. Given the strong fundamentals MENA equities provide defensive market dynamics against the current global backdrop. Relative valuation vs EM equities is still high, however Saudi equities are at a lower forward P/E multiple today than they were earlier in the cycle, mainly due to positive earnings revisions in the chemicals and materials sectors, which has come down the most in valuation. Comfortable with overweight in Saudi, the UAE and Qatar whilst equal weight in Kuwait and Oman, and underweight Egypt and Turkey. (per risk appetite)

Investments 101

Investment Goals

The first step in allocating money towards any investment is to understand your WHY. So, imperative to set one's investment goals and objectives to get clarity on the clarity on strategy. Consult an investment advisor who can hand hold you in this journey

Investment Horizon

Extremely crucial to any investment is, the investment horizon. If the investment horizon is 7yrs-10yrs one can look at equity investments in pursuit of double-digit annualized returns and if the investment horizon is only for a year, then banks deposits will do good

Risk Assessment

A self-risk assessment based on goals & horizon will shed light on one's ability, capability, capacity and willingness to take risk for the set investment goals. This will particularly guide your investment advisor to suggest appropriate avenues that suit your tolerance

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Asset Class Views

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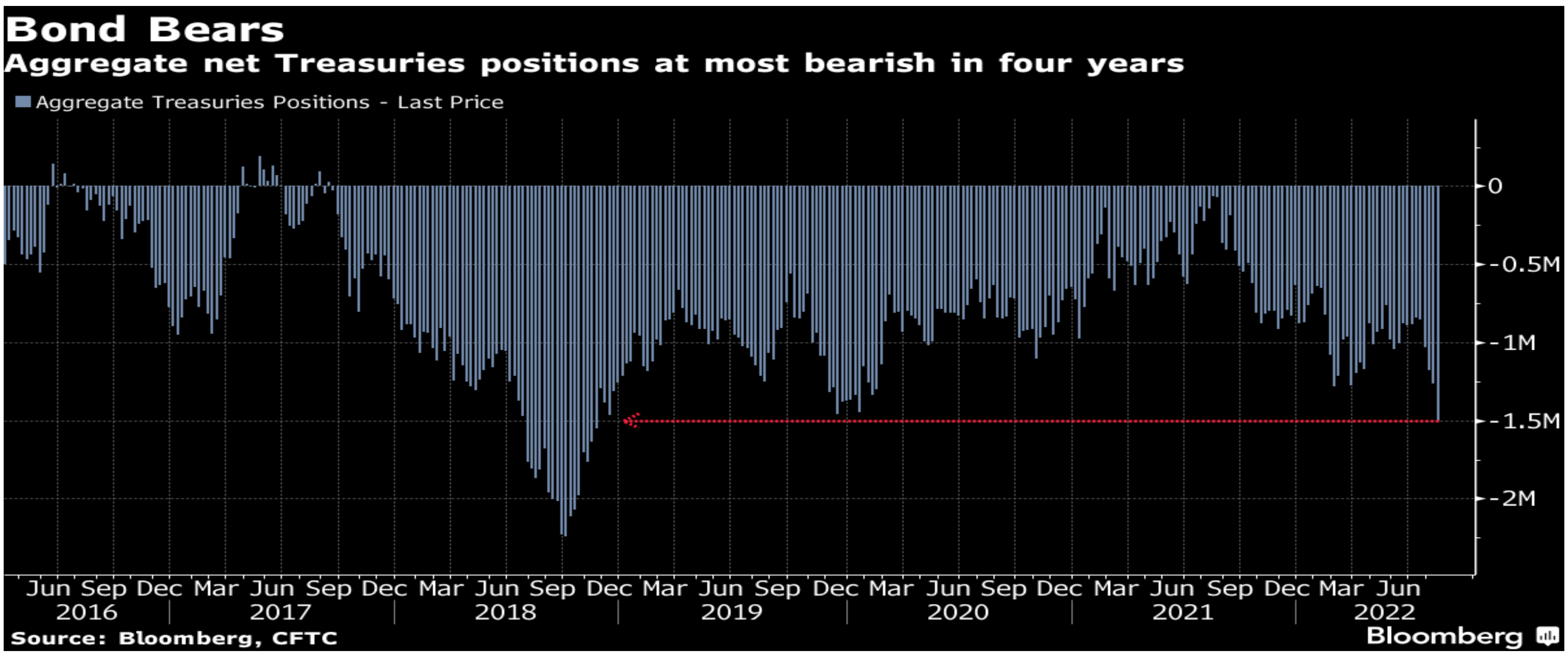
Asset Class	Sub-Class	View	Rationale	Conviction
Main Asset Class	Equities	=	Potential slowdown in global economic growth remains a major risk for equities; Powel's hawkish tone at Jackson Hole meeting firms up to dent equity sentiments.	
	Fixed Income	=	Global CB could eventually pace down the IR hike in Q4,2022 that will benefit Sovereigns and IG long duration to lock in the higher yields. lack of liquidity, dispersion, funding scarcity and a likely rise in the default rate are all factors that lead us to confirm our underweight stance on US and euro high yield.	
	Commodities	=▲	Oil fluctuated as investors weighed lingering concerns about an economic slowdown against bullish signals from the US and OPEC. While fears over a downturn continue to hang over the market. The potential for a nuclear deal and more oil from Iran have added to the bearish sentiment, despite a modest slowdown in the global economy. Geopolitical and economic concerns to favor gold.	
	Currencies	=	USD to remain strong against other currencies due to safe haven perception specially EM currencies as major global central banks start their pace of quantitative tightening	
Equities	USA	=	Healthy but uncertain growth; Data driven policy stance over Inflation. Value pick overgrowth, preference to Financials, Healthcare, Utilities. Sharp slowdown in the housing market	
	EU (Ex UK)	=	Concerns over stagnating economic growth; ECB's unclear policy stance, trade risks, escalating Russia/Ukraine war disrupting Oil/Energy supply into Europe for the winter season & production could be dampened due to energy shortage.	
	UK	=	Inflation increasing at a fast pace, cost of living crisis, political disarray and trade battle with the EU point to a poor outlook to take fresh exposure	
	EM (Ex MENA)	=	EM under pressure from rising inflation, rising oil prices, supply chain (export) disruption, structural reforms. For China, The combination of zero-Covid strategy and the deteriorating property sector continues to drag down the economy, even as export growth remains elevated. With PBOC cutting short term rates, contrary to global CB's , indicates situation is far worse than reported. Valuations are attractive but further outbreaks remain a risk.	
	MENA	=▲	Range bound Oil prices, Rising USD IR and key structural reforms make GCC a key low beta, attractive return allocation.	HIGH
Fixed Income	US Treasuries	=▲	FED Hawkishness fully priced into the treasuries. Demand for duration will grow from these levels as portfolios flow back to rebalance and safe havens	HIGH
	Euro (Bunds)	▼	Bund yields at highest levels but gradually pricing in rake hikes. Yields still not peaked out and uncertainty remains	
	UK Gilts	▼	Lack of policy clarity, red hot inflation and weak economic outlook poses challenges to BOE's further guidance on pace and magnitude of interest rate hikes.	
	US IG	▲	Positive corporate earnings and likely controlled and smaller Fed rate hikes; prefer companies with high interest coverage ratio.	HIGH
	US HY	=	Based on majority analyst consensus, neutral high yield. We prefer up-in-quality credit exposures amid a worsening macro backdrop.	
	Europe IG	▼	Economic and political struggles to weigh on EU credits whilst ECB still remaining hawkish.	LOW
	EM (ex Japan)	▲	We are neutral EM fixed income amid a worsening macro-outlook. Valuations are not compelling enough yet to turn more positive on the asset class, EM local ccy could prove a good play based on tactical risk allocation	
Commodities	Oil	=▲	Global supply disruption to support Oil.	
	Precious Metals	=▲	Heightened geopolitical risks amidst recessionary fears, US-China tension, Russia-Ukraine and market volatility to drive safe haven demand.	
Curriencies	USD	=▲	Bad news on inflation has resulted in good news on USD and any reversal will have an impact on the USD. USD remain the safe haven global currency	
	EUR	▼	Weak economic outlook but technically overvalued USD and valuations can give an upside lift in the mid-term	
	GBP	=	Weak economic outlook, and anticipation of aggressive BOE rate hike until end of 2022;	LOW
	EM	=	Benign USD, compelling currency valuations, consolidating energy/commodity prices may support EM currencies.	

* ▲ Positive, = Neutral, ▼ Cautious, =▲Neutral with a Positive Tilt



Source : *Cormac Mullen*, Bloomberg

Bond Bears

Now could be time to gradually accumulate

Giant investment funds may be ready to pile back into Treasuries, but their bearish fast money counterparts are also growing in confidence, taking heed of the relentless message from Federal Reserve officials that the fight against inflation is nowhere near done. An aggregate gauge of net-short non-commercial positions across all Treasury maturities shows bearish bets have grown to the most since 2018, according to the latest data from the Commodity Futures Trading Commission. Last week saw a spike in bets against five-year Treasuries, which are particularly sensitive to Fed policy. Meanwhile, the 10-year Treasury yield is on the cusp of rising past the closely-watched 3% level once more as investors await Fed Chair Jerome Powell's speech at the annual Jackson Hole symposium this week. Bets on the benchmark note are diverging once again with asset managers net long and leveraged funds net short — reminiscent of the sizeable opposite positions both had in 2019.

"*The US dollar just had its biggest weekly gain since the pandemic and the risks look skewed toward the upside. Stocks, globally as well as in the US, have been moving inversely in line with the dollar, so if the greenback busts out to fresh record highs it's likely equities would make fresh lows. And equities are a lot further away from this cycle's troughs than the dollar is from recent peaks.*"

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The Economic Calendar

			Actual	Previous	Consensus	Forecast
Thursday September 01 2022			Actual	Previous	Consensus	Forecast
01:00 PM	EA	Unemployment Rate JUL		6.6%		6.7%
06:00 PM	US	ISM Manufacturing PMI AUG		52.8		
Friday September 02 2022			Actual	Previous	Consensus	Forecast
04:30 PM	US	Non Farm Payrolls AUG		528K		
04:30 PM	US	Unemployment Rate AUG				
Monday September 05 2022			Actual	Previous	Consensus	Forecast
12:30 PM	GB	S&P Global/CIPS UK Services PMI Final AUG				
Tuesday September 06 2022			Actual	Previous	Consensus	Forecast
06:00 PM	US	ISM Non-Manufacturing PMI AUG		56.7		
Wednesday September 07 2022			Actual	Previous	Consensus	Forecast
04:30 PM	US	Balance of Trade JUL		$-79.6B		
Thursday September 08 2022			Actual	Previous	Consensus	Forecast
04:15 PM	EA	ECB Interest Rate Decision				0.75%
Monday September 12 2022			Actual	Previous	Consensus	Forecast
10:00 AM	GB	GDP MoM JUL		-0.6%		-0.1%
Tuesday September 13 2022			Actual	Previous	Consensus	Forecast
10:00 AM	GB	Unemployment Rate JUL		3.8%		
10:00 AM	GB	Claimant Count Change AUG		-10.5K		-4K
04:30 PM	US	Core Inflation Rate YoY AUG		5.9%		
04:30 PM	US	Inflation Rate YoY AUG		8.5%		
Wednesday September 14 2022			Actual	Previous	Consensus	Forecast
10:00 AM	GB	Inflation Rate YoY AUG		10.1%		
04:30 PM	US	PPI MoM AUG		-0.5%		
Thursday September 15 2022			Actual	Previous	Consensus	Forecast
03:00 PM	GB	BoE Interest Rate Decision				2.25%
04:30 PM	US	Retail Sales MoM AUG		0%		
Friday September 16 2022			Actual	Previous	Consensus	Forecast
10:00 AM	GB	Retail Sales MoM AUG				
06:00 PM	US	Michigan Consumer Sentiment Prel SEP				
Tuesday September 20 2022			Actual	Previous	Consensus	Forecast
04:30 PM	US	Building Permits AUG		1.674M		
04:30 PM	US	Housing Starts AUG		1.446M		
Wednesday September 21 2022			Actual	Previous	Consensus	Forecast
06:00 PM	US	Existing Home Sales AUG				
10:00 PM	US	Fed Interest Rate Decision		2.5%		2.75%
10:00 PM	US	FOMC Economic Projections				
10:30 PM	US	Fed Press Conference				
Friday September 23 2022			Actual	Previous	Consensus	Forecast
03:01 AM	GB	Gfk Consumer Confidence SEP				-35
Tuesday September 27 2022			Actual	Previous	Consensus	Forecast
04:30 PM	US	Durable Goods Orders MoM AUG				
06:00 PM	US	New Home Sales AUG				
Friday September 30 2022			Actual	Previous	Consensus	Forecast
01:00 PM	EA	Inflation Rate YoY Flash SEP				8.7%
01:00 PM	EA	Unemployment Rate AUG				6.8%
04:30 PM	US	Personal Spending MoM AUG				
04:30 PM	US	Personal Income MoM AUG				