The Weekly Market View

April 4 2016

Yellen words benefit US and emerging equities, hurt Europe and Japan

Mrs. Yellen dovish words have done a lot to reduce market anxiety regarding interest rates. Her indications that the Fed would "proceed cautiously" in lifting interest rates given unfavourable market conditions, weaker than expected growth and an uncertain inflation outlook, have immediately determined a reduction of yields across the curve. They have also resulted in a further weakening of the US dollar against the euro and the Japanese yen. Not surprisingly equity markets – whose main concern remains growth and not an increase in global interest rates that is anyway extremely unlikely – have had a mixed response. Whilst US markets and most emerging markets have made some further gains on the back of a weaker US dollar, European and Japanese equity markets have remained under pressure. Friday's positive US ISM figure and labour market might have assuaged some of the global growth concerns. A closer look at the labour market data, as well as the implications of a weaker US dollar for the current growth momentum in the Euro-zone, tells us that it is more likely that global equity markets will continue to roll-over, if not correct again.

Markets to scrutinize US and China data for growth confirmation

Whilst the immediate reaction of US equity markets to the Friday labour market data was already muted, some further rethinking might well take place this week. Granted, the week will be less loaded with data than last week. Markets are likely to pay particular attention to durable goods orders and factory goods orders in the US, as they ponder whether the recent rebound in the country's manufacturing activity is sustainable. Likewise they will be watching China's forex figures to see if the recent stabilization in capital outflows has held up. They will also want to see if monetary growth in China has kept up with previous stimulus efforts. Finally, last week's increased speculation that Saudi Arabia would be reluctant to freeze production if Iran does not do the same, has already determined renewed downward pressure on the oil price. The oil price will for sure remain in the spotlight as the week unfolds.

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Past week global markets' performance

Index Snapshot (World Indices)

Index	Latest	Weekly Chg %	YTD %
S&P 500	2,072.8	1.8	1.4
Dow Jones	17,792.8	1.6	2.1
Nasdaq	4,914.5	3.0	-1.9
DAX	9,794.6	-0.6	-8.8
Nikkei 225	16,164.2	-4.9	-15.1
FTSE 100	6,146.1	0.6	-1.5
Sensex	25,269.6	-0.3	-3.2
Hang Seng	20498.9	0.8	-6.5
Regional Markets (Sunday to Thursday)			
ADX	4390.4	1.4	1.9
DFM	3355.5	1.1	6.5
Tadawul	6223.1	-2.0	-10.0
DSM	10376.2	0.9	-0.5
MSM30	5467.42	-1.2	1.1
BHSE	1131.1	-2.4	-7.0
KWSE	5228.8	-0.8	-6.9
MSCI			
MSCI World	1,640.1	1.0	-1.4
MSCI EM	826.2	1.7	4.0

Global Commodities, Currencies and Rates

Commodity	Latest	Weekly Chg %	YTD %
ICE Brent USD/bbl	38.7	-4.4	3.7
Nymex WTI USD/bbl	36.8	-6.8	-0.7
OPEC Baskt USD/bbl	34.3	-1.8	9.8
Gold 100 oz USD/t oz	1222.6	0.5	15.2
Platinum USD/t oz	957.1	1.0	7.3
Copper USD/MT	4880.0	-1.0	3.8
Alluminium	1524.25	3.7	1.2
Currencies			
EUR	1.1391	2.0	4.9
GBP	1.4227	0.7	-3.5
JPY	111.69	-1.2	7.6
CHF	0.9580	-2.0	4.6
Rates			
USD Libor 3m	0.6291	0.1	2.7
USD Libor 12m	1.2134	-1.4	3.0
UAE Eibor 3m	1.0251	0.8	-2.8
UAE Eibor 12m	1.5793	0.1	7.1
US 3m Bills	0.2238	-20.0	37.6
US 10yr Treasury	1.7705	-6.8	-22.0

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Start-of-year gloom might have been overdone, so is today’s euphoria

How important is the US labour market really?

The strength of the US labour data is of key importance to the global economic outlook. If – as we suspect – the US labour market is less strong than many think, we can expect US growth to remain sluggish, and Mrs. Yellen to further procrastinate interest rate hikes, even if that could determine some pick-up in inflation (we expect inflation anyway to remain subdued over a medium- to long term horizon). If Mrs. Yellen does so, we can expect the US dollar to remain weak. That is for sure a major concern for Japan. It is also a concern for Mr. Draghi who – having de facto abandoned going further into negative interest rate territory – would have preferred to see a weaker rather than a stronger euro. The consideration that further massive strengthening of the US dollar against the other major currencies was running out of steam, has been throughout one of the main reasons that global growth is likely to remain low. Yes, it might help some commodity exporting countries. Yes, it might give some relief to China. It is also deflating further growth prospects for the Euro-zone (the world’s second largest economy) and Japan (the fourth largest economy). And it is quiet reminder that growth in the US (the world’s largest economy) is likely to remain sluggish.

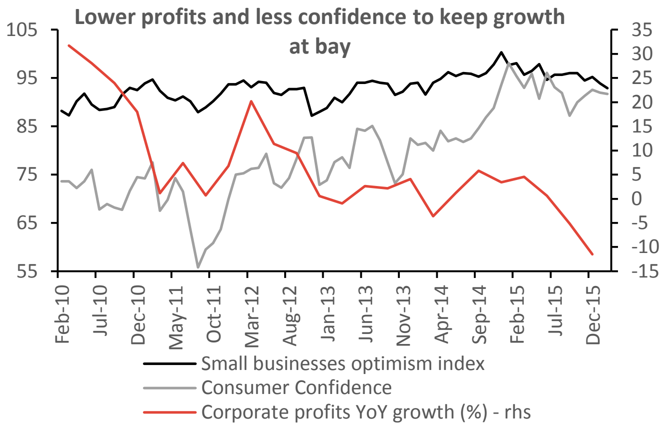
And how strong is the US labour market really?

The good news is that the continuous creation of jobs at a rate above 200’000 per month is now attracting more people back into the labour force, such that the labour participation force has now risen to 63%, that translates into a significant 0.6% jump over the last 6 months and partly explains the increase in the unemployment rate to 5% (because not all those who decided to re-join the labour force by actively looking for a job, necessarily find it). The bad news is that many of the new jobs created are part time jobs as many people struggle to find job stability, and the income certainty that comes with it. Thus the increase in jobs is unlikely to determine a surge in wages, and aggregate consumer demand is likely to remain subdued.

Source: Bloomberg

And when will job creation stop rolling over?

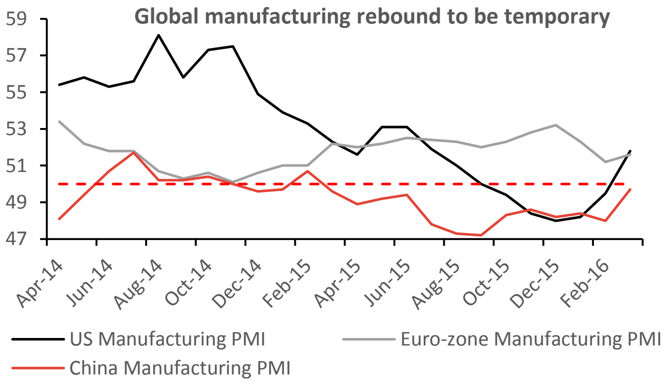
More worrisome is, of course, the consideration that at some point the US labour market might cease to continue to create jobs to the tune of more than 200’000 units a month. In fact, if most jobs are part-time (and in the last month we observed the creation of 135’000 new part-time jobs whose holders where, in fact, looking for a full time job), fewer people will move into the labour force to look for new jobs. Also, subdued consumption growth is already leading to a reduction in small business and consumer confidence, whilst corporate profits are falling.



Source: Bloomberg

Recent rebound in global manufacturing likely to fade

Continuing sluggish growth in the United States – now also recognized by the Federal Reserve – combined with a weaker US dollar is therefore likely to keep the recent manufacturing rebound in check.



Source: Bloomberg

Equity markets unlikely to climb further

In the presence of high US equity valuations, one would expect these legitimate growth concerns to keep a lid on further equity appreciations, and to keep US Treasury yields well anchored.

Summary market outlook

Bonds	
Global Yields	US Treasury 10yr yields trended lower with Mrs. Yellen dovish comment coupled with slightly lower core PCE readings, and a decline in the oil price. Continuing stronger economic data in the very near term might now push yields somewhat higher. European Sovereign yields eased a bit and could go further down, especially in the periphery countries as the ECB continues its purchases.
Stress and Risk Indicators	The VIX Index continued to trend lower as the US equity market gained further and general sentiment in the risk assets improved. Sovereign CDS Spreads, especially in the Asian EMs improved with the easing dollar strength. They could further improve in the very near term.

Equity Markets	
Local Equity Markets	GCC equities were mixed with the UAE and Qatar markets gaining modestly while remaining regional markets declined. The late last week decline in the oil price would be a negative for the markets to start the week. However, it will largely depend on how oil moves during the upcoming week.
Global Equity Markets	The dovish tone of Mrs. Yellen and largely positive economic releases last week have created positive sentiment in the global equity markets. Easing dollar strength provided comfort to EMs in particular. European and Japanese equity markets were less enthusiastic about the weaker greenback. Going forwards markets are most likely to roll over, unless we register some very positive growth surprises.

Commodities	
Precious Metals	The improvement in the risk sentiment in recent weeks pushed the gold price lower. After the strong surge the precious metal will now be very volatile and its moves will largely depend on how positive the risk sentiment remains over the next weeks. Longer term we see limited upside independently of temporary risk factors.
Energy	Media reports quoting Deputy Crown Prince of Saudi Arabia that the country will not be part of an oil output freeze until other countries including Iran agrees on the freeze, led to a decline in the oil price on Friday. The oil price is likely to remain volatile in the absence of global growth clarity and a clear direction for the US dollar.
Industrial Metals	Industrial metals prices stabilized last week after a sharp run-up in the prior weeks. We don't see any fundamental factors supporting industrial metals prices in the medium term.

Currencies								
EURUSD	A dovish tone by Mrs. Yellen and special mentioning of dollar strength immediately caused the greenback to ease against all major currencies including the euro. However, the currency is close to its upper limit of the range (1.05-1.15) from where it is unlikely to move up in any significant way.							
Critical levels	R2	1.1612	R1	1.1502	S1	1.1217	S2	1.1042
GBPUSD	The cable also gained in the dollar easing environment. However, the "Brexit" issue continued to play a role which capped its gain and, in fact, it rather pulled back substantially from its peak during the week. We believe that the currency pair will remain volatile, largely news-driven on the "Brexit" issue in the near term with a potential upward bias.							
Critical levels	R2	1.4607	R1	1.4417	S1	1.4079	S2	1.3931
USDJPY	The Japanese yen also eased against the dollar and breached the upper range (Yen strength). The currency reaction to the dovish remarks of Mrs. Yellen is more or less done for the moment. Thus the currency is likely to stabilize in the near term.							
Critical levels	R2	114.57	R1	113.13	S1	110.92	S2	110.15

Forthcoming important economic data

United States

	Indicator	Period	Expected	Prior	Comments
4/04/2016	Factory Orders	Feb	-1.8%	1.6%	Factory and durable goods orders along with ISM non-mfg will be important for the markets.
4/04/2016	Durable Goods Orders	Feb F	-2.8%	-2.8%	
4/05/2016	Trade Balance	Feb	-$46.2B	-$45.7B	
4/05/2016	ISM Non-mfg Composite	Mar	54.1	53.4	
4/06/2016	Initial Jobless Claims	Apr 2	270k	276k	
4/07/2016	Wholesale Inventories MoM	Feb	-0.2%	0.2%	

Japan

	Indicator	Period	Expected	Prior	Comments
4/05/2016	Labor Cash Earnings YoY	Feb	0.2%	0.0%	The markets will focus on the PMI services and leading index.
4/05/2016	Nikkei PMI Services	Mar	NA	51.2	
4/05/2016	Leading Index CI	Feb P	99.8	101.8	
4/08/2016	Eco Watcher Survey Current	Mar	46.4	44.6	

Eurozone

	Indicator	Period	Expected	Prior	Comments
4/04/2016	Sentix Investor Confidence	Apr	7.0	5.5	Unemployment rate, PMI services and retail sales will be looked at by the market.
4/04/2016	Unemployment Rate	Feb	10.3%	10.3%	
4/05/2016	Markit PMI Services	Mar F	54.0	54.0	
4/05/2016	Retail Sales MoM	Feb	0.0%	0.4%	

China and India

	Indicators	Period	Expected	Prior	Comments
4/05/2016	Caixin PMI Services (CH)	Mar	--	51.2	China's foreign reserves, new yuan loans and India's RBI interest rate action will be closely watched by the market.
4/07/2016	Foreign Reserves (CH)	Mar	$3205.5B	$3202.3B	
This Week	New Yuan Loans (CH)	Mar	1025B	726B	
This Week	Money Supply M2 YoY (CH)	Mar	13.5%	13.3%	
4/04/2016	RBI Repurchase Rate (IN)	Apr 5	6.50%	6.75%	
4/06/2016	Nikkei PMI Services (IN)	Mar	--	51.4	
This Week	Trade Balance (IN)	Mar	--	-$6.5B	
This Week	Exports YoY (IN)	Mar	--	-5.7%	

Sources

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

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

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