

Risk assets gain but broader market not convinced

The People's Bank of China setting the renminbi higher by more than a percent against the greenback when markets opened after a week-long holidays and a dovish Fed – reflected through Mrs. Yellen's testimony in the Congress as well as the FOMC minutes – supported the global equity markets last week. However, confidence was lacking in other segments of the market as sovereign bond yields either remained flat (in the US) or eased (in the Eurozone). There was hardly any positive move in the sovereign CDS spreads while safe-haven currencies, more specifically the Japanese yen, continued to strengthen. Economic releases also did not provide any sense of turnaround in economic outlook, rather they further confirmed our current assessment of sluggish growth. This raises the question of the sustainability of last week's equity market rally.

Growth indicators will come under closer scrutiny

A large set of economic indicators, mainly from developed economies, will be released this week which will probably correct the divergence in different market segments. Stronger data will further support equities, while disappointments will confirm current bond market expectations. Preliminary manufacturing PMIs for the G3 are expected to moderate only slightly, which is line with growth stabilizing at a sluggish rate. Over the past weekend the referendum for Britain's in-or-out EU membership was announced as being held on June 23rd. Whether or not it will impact markets immediately is difficult to say, however, we expect it to be an overhang for risk assets, especially in Europe until there is more clarity on the outcome.

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Past week global markets' performance

Index Snapshot (World Indices)				Global Commodities, Currencies and Rates			
Index	Latest	Weekly Chg %	YTD %	Commodity	Latest	Weekly Chg %	YTD %
S&P 500	1,917.8	2.8	-6.2	ICE Brent USD/bbl	33.0	-1.0	-11.5
Dow Jones	16,392.0	2.6	-5.9	Nymex WTI USD/bbl	29.6	0.7	-20.0
Nasdaq	4,504.4	3.8	-10.0	OPEC Baskt USD/bbl	30.0	12.0	-4.2
DAX	9,388.1	4.7	-12.6	Gold 100 oz USD/t oz	1226.8	-0.9	15.6
Nikkei 225	15,967.2	6.8	-16.1	Platinum USD/t oz	939.4	-1.7	5.4
FTSE 100	5,950.2	4.3	-4.7	Copper USD/MT	4590.0	2.3	-2.4
Sensex	23,709.2	3.1	-9.2	Alluminium	1551.75	3.6	3.1
Hang Seng	19285.5	5.3	-12.0	Currencies			
Regional Markets (Sunday to Thursday)				EUR	1.1130	-1.1	2.5
ADX	4212.9	3.5	-2.2	GBP	1.4406	-0.7	-2.2
DFM	3092.9	3.7	-1.8	JPY	112.63	-0.5	6.7
Tadaw ul	5884.2	3.9	-14.9	CHF	0.9904	1.4	1.2
DSM	9967.3	5.1	-4.4	Rates			
MSM30	5419.32	1.2	0.2	USD Libor 3m	0.6182	0.0	0.9
BHSE	1172.5	0.5	-3.6	USD Libor 12m	1.1398	2.2	-3.2
KWSE	5141.0	0.2	-8.4	UAE Eibor 3m	1.0303	1.2	-2.3
MSCI				UAE Eibor 12m	1.5370	0.0	4.2
MSCI World	1,538.2	3.5	-7.5	US 3m Bills	0.2899	3.6	78.2
MSCI EM	741.0	4.2	-6.7	US 10yr Treasury	1.7449	-0.2	-23.1

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Markets stabilize as growth is expected to remain sluggish

PBoC sets the renminbi reference rate higher

After a week long holiday for the Chinese New Year's celebrations, the People Bank of China tried to turn the tide in global markets, more specifically in its own currency market, by fixing the USDCNY reference rate 1.2% higher. At the same time, the governor of the central bank in an unusual interview supported the currency by saying that the downward pressure on the currency was "out of line with fundamentals". The statement and the action by the PBoC along with a more dovish Federal Reserve – reflected through Mrs. Yellen testimony and the FOMC minutes – supported risk sentiment in global markets. The rebound was also supported by the view many held that the equity markets were oversold during recent sell-off.

Divergence in the markets' expectations

Note that gains in risk assets last week were not corroborated by a sell-off in relatively safe-haven assets such as US Treasuries and the Japanese yen. Despite the higher print on core inflation in the US, the Treasury 10 year yield moved lower. This means that the two main capital markets are not in sync with each other – which happens many a times in the short term – as the bond market seems to be sceptical about the growth and inflation prospects and thus the interest rate trajectory. Moreover, certain currencies such as the Japanese yen – which is used as a carry trade currency – is a good indicator of the global risk environment. Despite the Bank of Japan reducing interest rates into negative territory at the end of the last month, the currency has been largely strengthening. This suggests that the market seems to be unwinding some of the carry trade – thus suggesting still high risk perception.

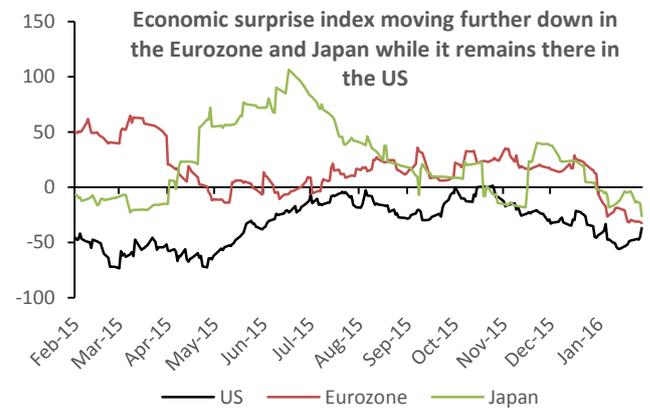


Source: Bloomberg

Economic releases continue to disappoint

Such divergence in the short term is typically corrected by the economic data trend. In this particular case, the bond market seems to be supported by economic releases that have largely been disappointing. The Citi economic surprise indices for the three large economies – the US, the Eurozone and Japan – remain firmly in the negative territory, confirming that economic releases continue to score below market expectations. Just to

note some of the important economic releases last week which were disappointing are fourth quarter GDP growth in Japan (actual -1.4% vs. expectation -0.8%), trade data in China (exports actual -6.6% vs. expected +3.6%) and housing data in the US.

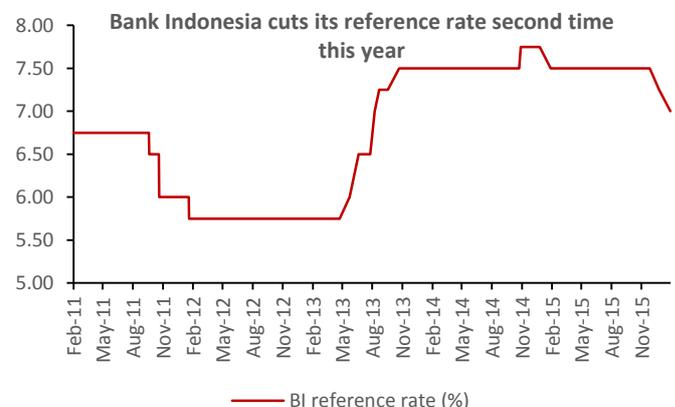


Source: Bloomberg

We thus stick to our base case scenario that global growth will remain sluggish.

Bank Indonesia cuts rate again, we are keeping an eye

Encouraged with significant moderation in inflation and continuing improvement in the current account deficit, Bank Indonesia cut its main policy rate by 25 bps to 7% last week, the second reduction of the same magnitude this year. The Indonesian central bank also got support from the relatively stable currency primarily due to the dovish Fed which has taken pressure away from the Rupiah. A series of reforms, the most recent being the easing of foreign ownership across 35 sectors earlier this month has also supported confidence. Thus the country has been able to reduce borrowing cost unlike many of its peers in EM (Mexico, Argentina and others) which are forced to raise interest rate.



Source: Bloomberg

Summary market outlook

Global Yields	US Treasury 10yr yields closed largely flat on a weekly basis as economic data and the FOMC minutes were factors behind the lower adjustment in the Fed funds trajectory. We remain of the view that the yield is unlikely to cross 2% in the very near term. European Sovereign yields also eased a bit which is likely to continue in the current economic environment.	
Stress and Risk Indicators	The VIX index trended lower with an improvement in equity risk sentiment. We do not expect it go down significantly in the near term. Sovereign CDS spreads for major Asian EMs were only slightly down.	
Precious Metals	The gold price saw downward pressure all through last week, before it rallied on Thursday. Long-term we remain cautious on gold, as global pressures are by and large deflationary.	
Local Equity Markets	GCC equity markets closed with gains last week as oil prices were up until Thursday. However, the oil price decline on Friday is likely to keep local markets relatively volatile this week.	
Global Equity Markets	Global equity markets moved further up last week as many believed that markets were oversold. At the same time, the PBoC's currency move also helped to improve sentiment. We believe that such gains are technical rebounds where the general trend in market is downward. We remain cautious on global equities for the moment.	
Energy	Despite the announcement of an oil production freeze by some of the OPEC members, oil prices retreated towards end of the week.	
Industrial Metals	Industrial metals prices were relatively stable during the week, and continue to lack an identifiable catalyst in our view.	
Currencies	Commentary	Critical levels
EURUSD	The euro trended lower all through last week. We believe that the currency is likely to continue with this trend, albeit at a slower pace in the near term.	R2 - 1.1347 R1 - 1.1238 S1 - 1.1044 S2 - 1.0959
GBPUSD	Prime Minister Cameron's claim that he got what he wanted from the Eurozone to remain in the European Union, provides a short term positive for the currency. In fact the situation is as uncertain as ever and might negatively impact both the euro and the pound sterling.	R2 - 1.4735 R1 - 1.4570 S1 - 1.4238 S2 - 1.4071
USDJPY	The Japanese yen retreated early last week as the global risk-off environment eased a bit. However, it soon turned again on strengthening mode. We believe that the BoJ will not feel comfortable with such appreciation. Therefore, we caution against betting on further strength in the yen.	R2 - 115.83 R1 - 114.23 S1 - 111.67 S2 - 110.71

Forthcoming important economic data

United States

	Indicator	Period	Expected	Prior	Comments
02/22/2016	Markit Mfg PMI	Feb P	52.5	52.4	
02/24/2016	Existing Home Sales	Jan	5.34m	5.46m	A good set of important releases from the housing sector to the industrial sector to inflation will be looked at by the market.
02/24/2016	New Homes Sales	Jan	520k	544k	
02/25/2016	Durable Goods Orders	Jan P	2.5%	-5.0%	
02/26/2016	GDP Annualized QoQ	4Q S	0.4%	0.7%	
02/26/2016	Personal Spending	Jan	0.3%	0.0%	
02/26/2016	Univ. of Mich. Sentiment	Feb F	91.0	90.7	
02/26/2016	PCE Core YoY	Jan	1.5%	1.4%	

Japan

	Indicator	Period	Expected	Prior	Comments
02/22/2016	Nikkei Mfg PMI	Feb P	52	52.3	
02/24/2016	Small Business Confidence	Feb	47.1	47.2	PMI and inflation are likely to be the focus of the market.
02/26/2016	CPI Core YoY	Jan	0.7%	0.8%	

Eurozone

	Indicator	Period	Expected	Prior	Comments
02/22/2016	Markit Mfg PMI	Feb A	52.0	52.3	PMI and inflation are likely to be the focus of the market.
02/25/2016	M3 Money Supply YoY	Jan	4.7%	4.7%	
02/25/2016	CPI YoY	Jan F	0.4%	0.2%	
02/25/2016	CPI Core YoY	Jan F	1.0%	1.0%	

China and India

	Indicators	Period	Expected	Prior	Comments
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No important economic data to be released from China and India

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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