The Weekly Market View

June 20 2016

ADCB

Brexit fear rattle markets, Yellen adopts increasingly dovish stance

As Brexit fears mounted, the risk-off mood prevailed massively last week. Equity markets came down massively and the flight to safety boosted Treasuries and gold. Towards the end of the week, however, markets recovered and Treasury yields spiked significantly as the "remain" campaign seemed to regain some momentum. It seems likely that the outcome will remain uncertain until the referendum results will be announced, however. This means that markets will remain volatile almost the entire week. Perhaps as important as the Brexit vote is the "dovish" turnaround by the Federal Reserve. This turnaround might temporarily support a risk-on mood, but it would mainly favour US and emerging equity markets, less so Japanese and European equity markets.

Brexit will not remove uncertainty, Bremain will remove it temporarily

We still expect that the majority of voters will opt for the status quo, i.e. against the UK leaving the EU. This should trigger a temporary relief rally as it would for sure bring back some certainty to investment prospects both in the UK and the EU. It would not, however, resolve the underlying "low growth" issues in Europe and – as a result – it would not change our long-term underweight stance on European equities. We might, however, take a tactical call on European equities so as to profit from a temporary relief rally. If Brexit prevails, we must brace for further significant corrections in global equity markets, in particular in Europe and the UK. They would be compounded if the manufacturing leading indicators for most advanced economies – to be published on Friday – will announce the expected cooling of the current business cycle.

Luciano Jannelli, Ph.D., CFA
Head Investment Strategy
Tel: +971 (0)2 696 2340
luciano.jannelli@adcb.com

Rahmatullah Khan
Economist
Tel: +971 (0)2 696 2843
rahmatullah.khan@adcb.com

Wietse Nijenhuis
Equity Strategist
Tel: +971 (0)2 205 4923
wietse.nijenhuis@adcb.com

Visit Investment Strategy Webpage to read our other reports.

Past week global markets' performance

Index Snapshot (World Indices)

Index	Latest	Weekly Chg %	YTD %
S&P 500	2,071.2	-1.2	1.3
Dow Jones	17,675.2	-1.1	1.4
Nasdaq	4,800.3	-1.9	-4.1
DAX	9,631.4	-2.1	-10.3
Nikkei 225	15,599.7	-6.0	-18.0
FTSE 100	6,021.1	-1.5	-3.5
Sensex	26,625.9	-0.0	1.9
Hang Seng	20170.0	-4.1	-8.0
Regional Markets (Sunday to Thursday)			
ADX	4457.3	-1.3	3.5
DFM	3320.1	-1.9	5.4
Tadawul	6583.1	-1.0	-4.8
DSM	9743.2	-0.5	-6.6
MSM30	5813.71	-1.3	7.5
BHSE	1116.9	-0.2	-8.1
KWSE	5394.8	-0.3	-3.9
MSCI			
MSCI World	1,635.8	-1.8	-1.6
MSCI EM	806.2	-2.1	1.5

Global Commodities, Currencies and Rates

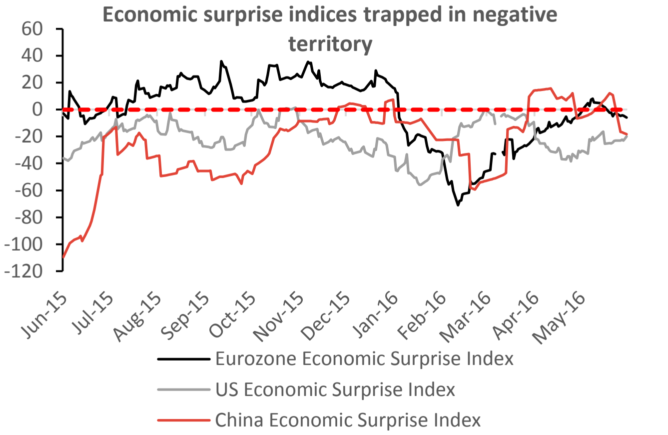
Commodity	Latest	Weekly Chg %	YTD %
ICE Brent USD/bbl	49.2	-2.7	31.9
Nymex WTI USD/bbl	48.0	-2.2	29.5
OPEC Baskt* USD/bbl	44.0	-6.4	40.8
Gold 100 oz USD/t oz	1298.7	1.9	22.4
Platinum USD/t oz	969.9	-2.2	8.8
Copper USD/MT	4521.5	0.4	-3.8
Alluminium	1608	2.5	6.8
Currencies			
EUR	1.1277	0.2	3.8
GBP	1.4358	0.7	-2.6
JPY	104.16	-2.6	15.4
CHF	0.9600	-0.5	4.4
Rates			
USD Libor 3m	0.6444	-1.7	5.2
USD Libor 12m	1.2408	-2.6	5.3
UAE Eibor 3m	1.1393	2.8	8.0
UAE Eibor 12m	1.6930	-0.1	14.8
US 3m Bills	0.2543	4.5	56.3
US 10yr Treasury	1.6078	-2.0	-29.2

Please refer to the disclaimer at the end of this publication

Brexit is not the only problem

We believe that a "remain" victory in the June 23rd Brexit vote would only provide temporary relief to global risk assets as the low growth environment of the last twelve months is likely to persist. This is by now also implicitly recognized by the Federal Reserve, which seems to be edging closer and closer to accepting the reality of perhaps only one rate hike by year end.

In fact, growth momentum seems to be stabilizing in the United States itself, while receding in the other two large economic areas of the world, the Euro-zone and China, with their relative surprise indices joining the United States in negative territory.



Source: Bloomberg

China stimulating no more?

The relative weakness of the US dollar – or at least the fact that it is no longer appreciating against the other major currencies – is providing more breathing space to the Chinese authorities. Having said so, China is unlikely to continue to massively stimulate its economy as the ineffectiveness of such a policy – which in practice mainly creates bubbles and supports increasingly inefficient state manufacturing companies – seems increasingly doubtful. This is particularly bad news for Europe and Japan since they already can no longer benefit from a weaker currency.

Source: Bloomberg

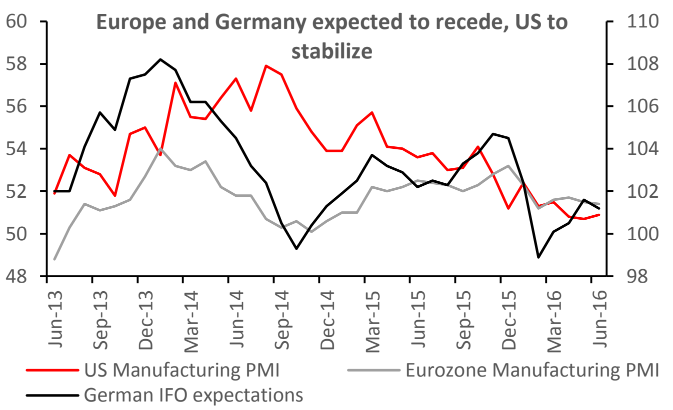
US relatively resilient, China and emerging markets muddling through, Europe and Japan equities to remain under pressure

A scenario whereby the US dollar no longer appreciate and overall financial conditions in the US remain accommodating is relatively good for US equity markets. It does not, however, necessarily entail a significant upside potential since US equities are not cheap and not immune from the slowdown in the US and the world. It might also temporarily favour again emerging markets since the relatively weak US dollar acts as a barrier against continuing capital outflows out of China and also reduces the real value of emerging markets' US dollar denominated debt.

Europe and Japan, on the other hand, seem to be running into a policy short circuit since most of the QE enacted by the ECB and the BoJ was – albeit not officially – most effective through the exchange rate depreciation. That game seems to be now over, unless and until these central banks would resort to even more "unconventional" policies such as so-called "Helicopter Money", i.e. outright debt monetization.

Turbulent week ahead

It is in this context that one must see the upcoming Brexit referendum, the results of which will be known in the morning of Friday. A "Brexit" victory would mean continuing corrections, eventually compounded by weak Euro-zone PMI data on Friday itself. A "Bremain" victory would remove a significant amount of uncertainty and trigger a "relief rally". It would thus overcome Friday's potentially weak PMI data. Slow growth is, however, going to remain a major concern for financial markets in Europe. As such, any relief rally is likely to be short-lived.



Source: Bloomberg

Summary market outlook

Bonds	
Global Yields	US Treasury 10-yr yield moved sharply lower on dovish Fed and increased risk aversion, only to bounce back towards the end of the week. Some further reversal is possible in the very short term but it's unlikely to go near 2% mark now that the Fed is increasingly moving away from a new rate hike.
Stress and Risk Indicators	The VIX index moved up sharply as risk aversion was visible in global financial markets. The major sovereign credit default swaps were also marginally higher for the week. "Brexit" is likely to continue to play out across the global financial market in coming days.

Equity Markets	
Local Equity Markets	GCC equities came again under pressure last week, in line with the oil price. Two opposing factors are playing into the regional markets – first, despite oil gaining in the recent weeks, governments' finances will remain in the consolidation mode across the region. Second, valuation has turned attractive.
Global Equity Markets	All equities were under pressure only to revert towards the end of the week as the "remain" camp seemed to regain some momentum in the upcoming Brexit referendum. Markets are likely to remain volatile with a sharp movement up or down on Friday depending on what the final referendum result will be.

Commodities	
Precious Metals	Gold was stable over the week, ultimately edged down on the improved momentum of the "remain" campaign.
Energy	The oil price moved in the opposite direction as gold, strengthening towards the end of the week with equity markets, as the "remain" outcome is seen as more conducive to continuing economic growth.
Industrial Metals	Industrials metals were stationary. Long term prospects remain however negative with China pushing in the direction of less rather than more consumption of industrial metals.

Currencies								
EURUSD	Euro remained largely flat through the last week except briefly spiking downside on Thursday. It will remain largely in the trading range of 1.12-1.14 through this week if we see Briton voting to remain in the EU. However, in the event of Brexit, the currency is expected to come under pressure.							
Critical levels	R2	1.1409	R1	1.1343	S1	1.1171	S2	1.1065
GBPUSD	Similar to the euro, the British pound remained largely flat through the last week before gaining on Friday. The rise in Bremain vote share caused that movement. Gains in Bremain will continue to be positively correlated to the currency until the final outcome. The volatility is likely to continue as we move closer to the referendum.							
Critical levels	R2	1.4628	R1	1.4493	S1	1.4118	S2	1.3878
USDJPY	The Japanese yen continued to appreciate, especially after the BoJ stayed put during it last meeting. The currency is likely to remain in the appreciating trend as we don't see any catalyst for turnaround. Brexit could further strengthen the currency whereas Bremain could temporarily ease the currency strength.							
Critical levels	R2	108.33	R1	106.24	S1	102.81	S2	101.47

Forthcoming important economic data

United States

	Indicator	Period	Expected	Prior	Comments
6/22/2016	Existing Home Sales	May	5.55m	5.45m	Housing related data and durable goods orders will be looked at by markets.
6/23/2016	Markit Manufacturing PMI	Jun P	50.9	50.7	
6/23/2016	New Home Sales	May	560k	619k	
6/24/2016	Durable Goods Orders	May P	-0.4%	3.4%	
6/24/2016	Univ. of Mich. Sentiment	Jun F	94.1	94.3	

Japan

	Indicator	Period	Expected	Prior	Comments
6/21/2016	All Industry Activity Index MoM	Apr	1.2%	0.1%	Industry activity index and PMI will be looked at by markets.
6/23/2016	Nikkei Mfg PMI	Jun P	--	47.7	
6/23/2016	Leading Index CI	Apr F	--	100.5	

Eurozone

	Indicator	Period	Expected	Prior	Comments
6/20/2016	Construction Output	Apr	--	-0.9%	PMIs are to be the main focus of the market.
6/20/2016	ZEW Survey Expectations	Jun	--	16.8	
6/23/2016	Markit Mfg PMI	Jun P	51.4	51.5	
6/23/2016	Markit Services PMI	Jun P	53.2	53.3	

China and India

	Indicator	Period	Expected	Prior	Comments
This Week	Leading Index (CH)	Apr	--	99.10	No important economic data from China and India
This Week	Industrial Profits YoY (CH)	May	--	4.2%	
This Week	Eight Infrastructure industries YoY (IN)	May	--	8.5%	

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

Disclaimer

*This publication is intended for general information purposes only. It should not be construed as an offer, recommendation or solicitation to purchase or dispose of any securities or to enter in any transaction or adopt any hedging, trading or investment strategy. Neither this publication nor anything contained herein shall form the basis of any contract or commitment whatsoever. Distribution of this publication does not oblige Abu Dhabi Commercial Bank PJSC ("**ADCB**") to enter into any transaction.*

The content of this publication should not be considered legal, regulatory, credit, tax or accounting advice. Anyone proposing to rely on or use the information contained in the publication should independently verify and check the accuracy, completeness, reliability and suitability of the information and should obtain independent and specific advice from appropriate professionals or experts regarding information contained in this publication.

Information contained herein is based on various sources, including but not limited to public information, annual reports and statistical data that ADCB considers accurate and reliable. However, ADCB makes no representation or warranty as to the accuracy or completeness of any statement made in or in connection with this publication and accepts no responsibility whatsoever for any loss or damage caused by any act or omission taken as a result of the information contained in this publication. This publication is intended for qualified customers of ADCB.

Charts, graphs and related data or information provided in this publication are intended to serve for illustrative purposes only. The information contained in this publication is prepared as of a particular date and time and will not reflect subsequent changes in the market or changes in any other factors relevant to their determination. All statements as to future matters are not guaranteed to be accurate. ADCB expressly disclaims any obligation to update or revise any forward looking statements to reflect new information, events or circumstances after the date of this publication or to reflect the occurrence of unanticipated events.

ADCB does and may at any time solicit or provide commercial banking, investment banking, credit, advisory or other services to the companies covered in its publications. As a result, recipients of this publication should be aware that any or all of the foregoing services may at time give rise to a conflict of interest that could affect the objectivity of this publication.

Past performance does not guarantee future results. Investment products are not bank deposits and are not guaranteed by ADCB. They are subject to investment risks, including possible loss of principal amount invested. Please refer to ADCB's Terms and Conditions for Investment Services.

This publication is being furnished to you solely for your information and neither it nor any part of it may be used, forwarded, disclosed, distributed or delivered to anyone else. You may not copy, reproduce, display, modify or create derivative works from any data or information contained in this publication.