The Weekly Market View

May 9 2016

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Currency volatility high as markets remain under pressure

Global equities were in the red for a second consecutive week. The retrenchment of equities following the violent recovery rally of February and March was in the cards and we had been warning about it for some time now. The weakening of the US dollar had played an important part in the recovery rally. That same weakening of the greenback also explains the dilemma in which the BoJ and the ECB find themselves as it considerably paralyses their capacity to stimulate their economies. Thus, whilst Euro-zone growth is still keeping up decently well, Japan is again seriously flirting with recession. Markets are now growing wary about this as it can be seen by the increased volatility in the world's most import currency pair with then euro first moving within a week from 1.13 to 1.16 against the US dollar, and then receding within a few days back to 1.14. With China, which on the other hand needs a weaker US dollar, again giving sign of weakness, we see good reasons for continuing currency volatility, and risk assets remaining under pressure.

China data to be centre stage

China exports stabilized last week, whilst imports came down again. The continuing slump in imports, to the tune of a 10% year-over-year reduction, was as usual accompanied by the suspicion that such lower imports are in fact hiding continuing reserve outflows. Whilst that is certainly, to some extent possible, we would suggest that the dovish Federal Reserve stance is – in fact – put a temporary lid on capital outflows. We are more worried by the fact that the ongoing stimulus is not leading to a significant rebound in (sustainable) growth. The unwinding of US dollar weakness should be the trigger for more worries. Markets will thus nervously watch this week's China data, in particular China industrial production, retail sales, and investments for the month of April.

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Past week global markets' performance

Index Snapshot (World Indices)

Index	Latest	Weekly Chg %	YTD %
S&P 500	2,057.1	-0.4	0.6
Dow Jones	17,740.6	-0.2	1.8
Nasdaq	4,736.2	-0.8	-5.4
DAX	9,870.0	-1.7	-8.1
Nikkei 225	16,106.7	-3.4	-15.4
FTSE 100	6,125.7	-1.9	-1.9
Sensex	25,228.5	-1.5	-3.4
Hang Seng	20109.9	-4.5	-8.2
Regional Markets (Sunday to Thursday)			
ADX	4428.6	-2.5	2.8
DFM	3307.6	-5.3	5.0
Tadawul	6656.4	-2.2	-3.7
DSM	9748.8	-4.3	-6.5
MSM30	5979.75	0.6	10.6
BHSE	1112.8	0.2	-8.5
KWSE	5373.2	-0.3	-4.3
MSCI			
MSCI World	1,643.2	-1.7	-1.2
MSCI EM	805.3	-4.1	1.4

Global Commodities, Currencies and Rates

Commodity	Latest	Weekly Chg %	YTD %
ICE Brent USD/bbl	45.4	-5.7	21.7
Nymex WTI USD/bbl	44.7	-2.7	20.6
OPEC Baskt* USD/bbl	41.2	-3.6	31.6
Gold 100 oz USD/t oz	1289.0	-0.4	21.5
Platinum USD/t oz	1079.9	0.3	21.1
Copper USD/MT	4810.0	-4.7	2.3
Alluminium	1585.75	-5.3	5.3
Currencies			
EUR	1.1404	-0.4	5.0
GBP	1.4427	-1.3	-2.1
JPY	107.12	0.6	12.2
CHF	0.9725	1.3	3.0
Rates			
USD Libor 3m	0.6296	-1.1	2.8
USD Libor 12m	1.2242	-0.4	3.9
UAE Eibor 3m	1.0600	0.7	0.5
UAE Eibor 12m	1.6550	1.8	12.2
US 3m Bills	0.1933	-7.3	18.8
US 10yr Treasury	1.7789	-3.0	-21.6

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China troubles likely to re-emerge sooner rather than later

Currency volatility an indicator of global deflationary pressure

The impressive weakening of the US dollar – which has been a boon for China, emerging markets, as well as commodity and energy prices – might have reached its limit. Of course, it would be dangerous to venture into short-term forecasts about currencies. What is troublesome about last week's euro-dollar movement is, however, not the – still uncertain - reversal of a trend. It is rather the volatility in the movements that reveals a growing sense of uncertainty about the monetary policy of major central banks. In this regards it is important to stress that central banks have – over the last years – been an anchor of stability, if not the main driver behind equity markets strength. Not surprisingly, therefore, currency volatility is going hand in hand with downward pressure on equity markets.

US growth remains weak in spite of a weaker US dollar

The weaker US dollar has been able to stabilize manufacturing in the US. It has, however, not been able to give it a significant growth impetus, as is clear from the manufacturing leading indicators for the month of April.

Source: Bloomberg

Without a more solid pick-up in manufacturing it is unlikely that consumer demand – which continues to disappoint – will do much better, also because the labour market is unlikely to continue to grow at a speed of more than 200'000 new jobs ahead.

China concerns are bigger

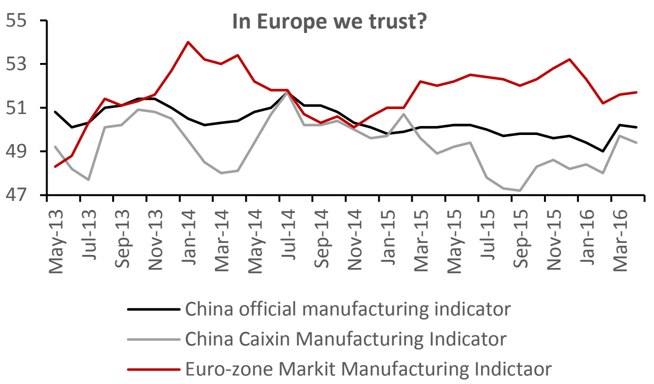
Whilst the weaker US dollar has been a potent factor, of not the main reason, for the stabilization of China and emerging markets, it has not really resulted in a sustainable pick-up of growth in China. The main reason behind the lacklustre pick-up in growth, in our opinion, is the simple fact that most of the stimulus goes to inefficient State-owned enterprises which continue to suffer from decreasing returns to their investments. As such the underlying issues – in particular the continuously growing debt over GDP ratio – will not get resolved and –are on the contrary – likely to come back with a vengeance.

Source: Bloomberg

Thus while year over year GDP growth and industry growth are slowing down gradually, in fact as measured over the prior quarter, the annualized growth in the first months of the year has rapidly reached an impressive low. Furthermore, a lot of the shrinkage in growth can be attributed to less financial intermediation, the result of the equity bubble that is only now emerging in terms of official growth statistics.

As long as Europe holds up, US dollar weakness might persist

Growth in Europe has so far surprised on the upside. To the extent, however, that the weaker greenback is struggling to reignite sustainable growth both in the US and China, the current growth balance seems to us too dependent on Europe only. Lower demand from these countries is bound to have an impact of the Euro-zone (the largest trade surplus holder in the world). It might take some time for markets to realize that, but it is likely to further stoke currency volatility, and downward pressure on equities.



Source: Bloomberg

Summary market outlook

Bonds	
Global Yields	The US Treasury 10yr yield softened a bit last week on weaker economic data releases. The level of retail sales this week will influence the yield which we believe is unlikely to move up significantly. European sovereign yields were mixed with yields in periphery countries ticking up, while in core countries they went down (a sign of risk-aversion).
Stress and Risk Indicators	Despite declines in US equity markets, the VIX index eased on the weekly basis. However, we do not expect it go much lower from the current levels. In spite of some US dollar strengthening, pressure on the EM sovereign CDS spreads continued to ease.

Equity Markets	
Local Equity Markets	The decline in the energy prices from their recent highs and disappointing quarterly results influenced the GCC equity markets. We are cautious in the very near term, but markets should benefit from oil stability.
Global Equity Markets	Global equities rolled over for a second consecutive week with concerns rising on global growth amid disappointing quarterly results. We remain cautious as there is lack of trigger for equities in the near term while its likely that equities continue to slide on economic concerns.

Commodities	
Precious Metals	The gold price remained largely flat over the week after a solid gain over the last four months. The global risk environment will continue to drive the precious metal price in the near term. However, long-term we remain cautious on gold, as global pressures are by and large deflationary.
Energy	The oil price gave up some of its recent gains last week. However, the factors working in opposite directions – signs of a moderating oversupply situation on one hand, and softer global growth data on the other are likely to keep the price volatile in the near term.
Industrial Metals	Industrial metals prices also retreated last week after a good run in prior weeks. We remain cautious on the sustainability of recent gains primarily due to their close connection with China's growth.

Currencies								
EURUSD	A volatile week for the currency as market re-assessed the dollar weakness. The currency is back to its range of 1.05-1.15 and likely to move further lower after its recent strength, primarily because we believe that the US dollar weakness is more or less done.							
Critical levels	R2	1.1699	R1	1.1551	S1	1.1321	S2	1.1239
GBPUSD	The British pound reached close to its highs in 2016 before giving up some of its gains last week. The currency pair is likely to be volatile with the downward bias (GBP) due to the overhang of "Brexit" referendum in just over a month time.							
Critical levels	R2	1.4892	R1	1.4660	S1	1.4305	S2	1.4182
USDJPY	The Japanese yen remained largely stable with less than a percent decline against the dollar last week. We believe that the current strength in the yen will ease slowly as Japan's economic growth dwindles and BoJ starts focusing again on further stimulus.							
Critical levels	R2	108.67	R1	107.90	S1	105.95	S2	104.77

ADCB بنك أبوظبي التجاري

Forthcoming important economic data

United States

	Indicator	Period	Expected	Prior	Comments
5/10/2016	Wholesale Inventories MoM	Mar	0.1%	-0.5%	Retail sales will looked at closely by the market to get a clue of any rebound in the second quarter growth.
5/13/2016	Retail Sales MoM	Apr	0.8%	-0.4%	
5/13/2016	Retail Sales Ex-auto MoM	Apr	0.5%	0.1%	
5/13/2016	PPI Ex-food and Energy YoY	Apr	0.9%	1.0%	
5/13/2016	Univ. of Mich. Sentiment	Pay P	89.5	89.0	

Japan

	Indicator	Period	Expected	Prior	Comments
5/09/2016	Labour Cash Earnings YoY	Mar	0.6%	0.7%	Data releases are expected to continue to show subdued outlook for the economy.
5/12/2016	Eco Watchers Survey – Current	Apr	44.9	45.4	
5/12/2016	Eco Watchers Survey – Outlook	Apr	46.2	46.7	
5/13/2016	Tertiary Industry Index MoM	Mar	-0.2%	-0.1%	

Eurozone

	Indicator	Period	Expected	Prior	Comments
5/09/2016	Sentix Investor Confidence	May	6.0	5.7	Second reading of the first quarter growth is expected to confirm the stronger growth rate.
5/12/2016	Industrial Production SA MoM	Mar	0.0%	-0.8%	
5/13/2016	GDP SA QoQ	1Q P	0.6%	0.6%	
5/09/2016	Factory Orders MoM (GE)	Mar	0.6%	-1.2%	
5/13/2016	GDP SA QoQ (GE)	1Q P	0.6%	0.3%	

China and India

	Indicators	Period	Expected	Prior	Comments
5/10/2016	CPI YoY (CH)	Apr	2.3%	2.3%	Important set of data from the two large EM economies this week.
5/10/2016	PPI YoY (CH)	Apr	-3.7%	-4.3%	
5/10/2016	New Yuan Loans (CH)	Apr	815B	1370B	
5/14/2016	Industrial Production YoY (CH)	Apr	6.5%	6.8%	
5/14/2016	Retail Sales YoY (CH)	Apr	10.6%	10.5%	
5/14/2016	Fixed Assets Ex Rural YTD YoY (CH)	Apr	11.0%	10.7%	
This week	Local Car Sales (IN)	Apr	--	175730	
This week	Trade Balance (IN)	Apr	--	$5.1B	
This week	Exports YoY (IN)	Apr	--	-5.5%	
05/12/2016	CPI YoY (IN)	Apr	--	4.83%	
05/12/2016	Industrial Production YoY (IN)	Mar	--	2.0%	

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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