بنك أبوظبي التجاري ADCB

Equity markets turn red as bond market sell-off intensifies

Global equities posted their biggest weekly loss since 2016. Instead of riding on positive earnings results, US equities turned negative in reaction to the sharp jump in US treasury yields. Volatility rose as the equity markets sell-off aggravated and the VIX jumped to the highest level since August 2017. The 10-year US treasury yield rose past the 2.8% level for the first time in almost four years on the back of stronger than expected labor market data. Non-farm payrolls increased by 200k, higher than market expectation. More importantly average hourly earnings, which have been subdued over past year, beat expectations and rose (2.9% yoy) at the fasted pace since 2009. This further fueled market fears that the Fed could adopt a more aggressive stance in hiking rates this year (more than three). The dollar finally caught up with the rising bond yields, but ended the week almost flat. However, the yen depreciated more versus the dollar as the BoJ offered unlimited buying of JGBs in an aim to send a signal to the market that it's far from normalizing monetary policy. A weaker yen helped the Japanese stocks to limit their losses compared to the other markets. Elsewhere, a relatively stronger dollar appetite and market concerns of more Fed rate hikes did not bode well for the gold prices. Oil prices also came under pressure with reports of rising US production and marginal rebound in dollar demand.

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Be wary of a more volatile week ahead

We believe that last Friday's equity market correction was long due given this marked the first weekly sell-off of such a magnitude (-4%) since the beginning of 2016. Having said that, last week's return of volatility is likely to linger this week. While the week ahead is light with the PMI releases to be the only main economic driver. However, taking cues from market's reaction to stronger economic data recently, any positive surprises in PMI could worsen investors' nervousness about a more aggressive Fed. In addition, the ongoing political turmoil in Washington regarding speculation of Trump administration's involvement with Russia could add to the volatility. While we refrain from buying into the correction, we still remain constructive on US equities. Given the backdrop of strong and synchronized global growth and healthy corporate profits, we do not expect the recent sell-off to sustain. In addition, we believe that the Fed will not become aggressive in hiking rates as the recent pick-up in wage inflation has already been priced in their future rate trajectory (the dot plot pointing to three rate hikes this year). In terms of data releases elsewhere, the focus will be mainly on emerging markets where China is scheduled to release January numbers for foreign reserves, CPI and exports. In India, all eyes will be on the RBI MPC meeting where the central bank could strike a hawkish tone.

Past week global markets' performance

Index Snapshot (World Indices)

Index	Latest	Weekly Chg %	YTD %
S&P 500	2,762.1	-3.9	3.3
Dow Jones	25,521.0	-4.1	3.2
Nasdaq	7,240.9	-3.5	4.9
DAX	12,785.2	-4.2	-1.0
Nikkei 225	23,274.5	-1.5	2.2
FTSE 100	7,443.4	-2.9	-3.2
Sensex	35,066.8	-2.7	3.0
Hang Seng	32601.8	-1.7	9.0
Regional Markets (Sunday to Thursday)			
ADX	4612.3	-0.4	4.9
DFM	3412.3	-1.5	1.3
Tadawul	7656.1	1.6	5.9
DSM	9207.0	-2.2	8.0
MSM30	5035.23	0.9	-1.3
BHSE	1357.7	1.1	1.9
KWSE	6685.2	0.8	4.3
MSCI			
MSCI World	2,171.5	-3.4	3.2
MSCI EM	1,230.8	-3.3	6.2

Global Commodities, Currencies and Rates

Commodity	Latest	Weekly Chg %	YTD %
ICE Brent USD/bbl	68.6	-2.8	2.6
Nymex WTI USD/bbl	65.5	-1.0	8.3
Gold USD/t oz	1333.4	-1.2	2.3
Silver USD/t oz	16.6	-4.7	-2.0
Platinum USD/t oz	991.2	-2.0	6.8
Copper USD/MT	7066.0	0.0	-1.3
Alluminium	2212.5	-2.1	-2.0
Currencies			
EUR USD	1.2463	0.3	3.8
GBP USD	1.4118	-0.3	4.5
USD JPY	110.17	1.5	-2.3
CHF USD	0.9314	-0.1	4.6
Rates			
USD Libor 3m	1.7890	1.3	5.6
USD Libor 12m	2.2905	2.0	8.7
UAE Eibor 3m	1.8750	1.0	4.5
UAE Eibor 12m	2.6385	1.1	2.4
US 3m Bills	1.4728	4.3	7.1
US 10yr Treasury	2.8411	6.8	18.1

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Summary market outlook

Bonds	
Global Yields	US treasury yields came under immense pressure with 10yr bond yields jumping past the 2.8% level for the first time in four years. The curve steepened as the long-end sold off on higher inflation concerns. We expect 10yr yield to consolidate below 3% as further uptick in yields will only trigger a buying opportunity for long-duration fixed income investors.
Stress and Risk Indicators	The VIX levels jumped to the highest level since August 2017 as majority of the equity markets reported losses. However, volatility is unlikely to stay low given the backdrop of ongoing geopolitical risks.
Equity Markets	
Local Equity Markets	GCC equity market were mixed on the back of declining oil prices and marginal rebound in dollar. We remain neutral on GCC equities given the potential for further dollar strength and range-bound oil prices. We maintain our tactical call on Saudi equities on the back of their inclusion onto the MSCI watch list for potential promotion into the MSCI Emerging Markets index.
Global Equity Markets	Global equities came under immense selling pressure as steep rise in bond yields and higher inflation fears raised concerns on prospects of corporate profitability. US equities posted their first biggest weekly decline since 2016 as the 10-year treasury yields rose above 2.8%. The sell-off in US equities spilled over to other markets with European equities underperforming the most. On the other hand, Japanese equities reported lower losses on the back of weaker yen. Overall, we continue to believe that strong economic fundamentals along with robust corporate earnings growth will support global equities and recent sell-off was mere healthy correction.
Commodities	
Precious Metals	Gold prices declined, finally tracking the rise in US yields. We remain overweight on gold as a risk hedge against ongoing political and (potential) inflationary risks.
Energy	Oil prices came under pressure on reports of rising US production. A marginal rebound in US dollar also impacted investor appetite. We expect oil to continue trading in the broad range seen over the past 12 months. A break out at the upper end will be challenging given US production will likely act as a ceiling on oil prices.
Industrial Metals	Industrial metals dropped lower as lower gold prices and stronger dollar weighed on the sentiment. Longer-term we do not recommend industrial metals exposure due to concerns around Chinese growth prospects post the Party Congress.
Currencies	
EURUSD	The euro ended the week flat versus the dollar even though strong US job numbers led to late-week dollar rebound. We expect the euro to remain under pressure as the US dollar regains ground.
Critical levels	R2 1.2578 · R1 1.2520 · S1 1.2407 · S2 1.2352
GBPUSD	The pound weakened slightly versus the dollar. We expect sterling to remain under pressure due to political uncertainty, economic weakness and Brexit negotiations.
Critical levels	R2 1.4342 · R1 1.4230 · S1 1.4054 · S2 1.3990
USDJPY	The yen depreciated versus the dollar on the back of BoJ's action on JGB purchases. However, we believe there will remain a bias for yen weakness given divergent monetary policies between Japan and the US.
Critical levels	R2 111.21 · R1 110.69 · S1 109.44 · S2 108.70

Note: R2, R1, S2 and S1 refer to Bloomberg calculated weekly technical resistance and support levels

Forthcoming important economic data

United States

	Indicator	Period	Expected	Prior	Comments
02/05/2018	Markit Composite PMI	Jan F	--	53.8	Light week in terms of data releases. Focus will be on the PMI
02/06/2018	Trade Balance	Dec	-$52.0b	-$50.5b	
02/08/2018	Initial Jobless Claims	3-Feb	233k	230k	
02/09/2018	Wholesale Inventories MoM	Dec F	0.20%	0.20%	

Japan

	Indicator	Period	Expected	Prior	Comments
02/05/2018	Nikkei PMI Composite	Jan	--	52.2	PMI will be the main release.
02/08/2018	BoP Current Account Balance	Dec	¥1059.0b	¥1347.3b	
02/08/2018	Trade Balance BoP Basis	Dec	¥514.3b	¥181.0b	
02/09/2018	Tertiary Industry Index MoM	Dec	0.10%	1.10%	

Eurozone

	Indicator	Period	Expected	Prior	Comments
02/05/2018	Markit Composite PMI	Jan F	58.6	58.6	Attention will be on CPI, PMI, and German trade balance.
02/07/2018	Retail Sales YoY	Dec	1.00%	1.40%	
02/07/2018	CPI YoY	Jan	2.30%	2.50%	
02/07/2018	CPI Core YoY	Jan	2.10%	2.10%	
02/08/2018	Trade Balance (GE)	Dec	21.0b	23.7b	
02/09/2018	Industrial Production YoY	Dec	3.50%	2.50%	

United Kingdom

	Indicator	Period	Expected	Prior	Comments
02/07/2018	Halifax House Prices MoM	Jan	0.20%	-0.60%	Industrial production will be the main focus.
02/09/2018	Industrial Production YoY	Dec	0.40%	2.50%	

China and India

	Indicator	Period	Expected	Prior	Comments
02/05/2018	Nikkei PMI Composite (IN)	Jan	--	53	All eyes will be on China January macro releases and the RBI MPC meeting
02/07/2018	Foreign Reserves (CH)	Jan	$3170.0b	$3139.9b	
02/07/2018	RBI MPC Meeting (IN)	7- Feb	No change	-	
02/08/2018	Exports YoY (CH)	Jan	11.30%	10.90%	
02/09/2018	CPI YoY (CH)	Jan	1.50%	1.80%	
02/10/2018	Money Supply M0 YoY	Jan	3350.0b	1140.0b	
02/10/2018	New Yuan Loans CNY	Jan	2050.0b	584.4b	

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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