



بنك الإمارات دبي الوطني
Emirates NBD

CIO OFFICE MORNING MARKET WRAP

22 July 2024

20 seconds summary (very long daily today): last week was negative across asset classes, with a rotation out of tech, into small/mid caps. Data and central banks consistent with our scenario (soft-landing, rate cuts), Chinese plenum a non-event. US elections' heat increased with Biden dropping out, as expected, which is positive for the Democrats but a recipe for volatility on markets, with tech anxiety also set to persist until key corporate results. We're happy to have turned a bit defensive earlier in July. Dollar weaker this morning, Asian markets in the red. Ahead: US Q2 GDP, flash PMIs, 100+ Q2 corporate earnings, and unknown developments in US politics.

Last week started with markets reacting to Trump's assassination attempt, and ended with Biden abandoning his reelection bid, with one of the largest IT disruptions in history in the meantime – on top of various “business as usual” market news. Heavy. As we warned for long in our various publications, H2 is about volatility, especially from politics, and last week didn't disappoint. It began with the “Trump trade” pushing both stocks and interest rates higher, before morphing into a tech rout: Wednesday was about trade restrictions on semiconductors, followed by Friday's mega IT failure. All in, returns were obviously negative. Stocks lost -2% in developed markets, with a strong rotation in the US out of technology (-5%) and large caps in general, and into small and midcaps, which are more domestic and more cyclical, as such exposed to both the “Trump trade” and to future US rate cuts. Emerging markets were down -3% with China underperforming. US Treasury yields had a bear steepening pattern, with an average +10 basis points rise for maturities of 2 years and more. The dollar strengthened +0.2% against trade-weighted counterparts. Brent crude fell -\$2.4 to \$82.6, and gold by a modest -0.4% to \$2,400. Among our asset allocation items, global REITS were the only clear positive contributor, along with cash of course delivering its steady weekly +0.1% return. Outside of it, bitcoin surfed the MAGA wave, up 10k in a week to just below \$67,000.

Before turning to the IT outage and of course US politics: economics were not the center of attention but didn't contradict the current soft-landing scenario. China confirmed softness with lower-than-expected Q2 GDP growth, as well as weak monthly retail sales, but robust industrial production, confirming that growth is currently all about exporting goods. The US had a strong June on all fronts, with both retail sales and industrial production surprising on the upside, all within, of course, an overall moderation trend in 2024, as illustrated by weekly jobless claims coming in higher than forecast. We should have a confirmation this week with the first estimate of US Q2 GDP. Nothing new under the sun in Europe: soft data from surveys (Zew, UK consumer confidence) was indeed soft, while disinflation stalled last month. No surprise then that the ECB meeting was a non-event, with no decision on rates and no clear guidance on future action, while the minutes from the BoE meeting kept on hinting at an August cut. Staying with central banks, various Fed officials delivered a message of increased confidence, yet continued vigilance, about rate cuts– again, nothing new, we still believe it will happen in September, and most likely not in July unless data strongly surprises. Bottom-line, global growth is gently slowing, but is certainly not weak, with still resilient activity and improving regional and sectoral balance. Inflation could rise a bit in goods, as shipping costs are, and as pricing power seems to come back for producers. This is not alarming either, as it is compensated by a deceleration in services prices and overall, in wages. Finally, China's third plenum was not far from a non-event judging by the first official communique, which included all key words (modern, socialist, digital, sustainable ...) but no groundbreaking announcement on real estate, trade, or foreign relations. No catalyst there yet, but it doesn't mean it won't happen: the most interesting feature of the communique is its absence of complacency regarding the current situation, which indicates that the authorities are preparing something.

In chronological order of the crazy end of last week: Friday's devastating IT outage crippled airports, banks, hospitals, some stock exchanges, affecting millions of machines worldwide in what could be the largest computer failure ever. The irony is that the giant crash was not a cyber-attack, but quite the opposite. It was triggered by a routine update, with a tiny file, from one of the world's biggest makers of cybersecurity software, CrowdStrike. You may know the company, maybe because it is on our recommended list of stocks (and the share price is still up almost 20% so far in 2024 including -11% on Friday), but it's fair to assume that most of us are not aware that the global IT ecosystem, including our own Windows machines, is critically exposed to a few little known vendors, part of a complex matrix which evolves in real time. There are two investment implications. First, on the short-term, volatility should continue for the tech sector (not even mentioning US politics): yes, growth is both desirable and deserves a valuation premium, but high multiples leave little space for any negative event and last week alone brought two, including the willingness of the US administration to impose severe semiconductor exports curbs on non-US companies. No doubt, big tech must deliver on their upcoming quarterly earnings, and it could be a long wait before Nvidia releases theirs in late August. Our equity team made a call weeks ago to take 25% profit on the tech highfliers, it's probably not time to rush back. The other implication is for the longer-term: the global IT ecosystem is as crucial as it is potentially vulnerable, which makes cybersecurity a permanent risk, thus a secular investment theme.

Finally, US politics from an investment perspective. We already flagged the US election in our annual investment outlook as a major source of uncertainty for markets in H2 and reiterated in our midyear

update communications 2 weeks ago. First, Mr. Trump nominated Senator JD Vance as his running mate, who is a MAGA hardliner (even if he once compared Trump with Hitler). The message is: there is only one program, and no compromise. This provided an opportunity for the Democrats, especially to leverage on their main, if not only, key to the heart of the undecided, which is US abortion rights. Still, President Biden had no chance to win, and we were expecting him to drop out. He announced his exit yesterday at 10PM Dubai time, endorsing VP Kamala Harris as the main candidate. Hope is back in the blue camp, with donors reopening their wallets – an astonishing \$50mn collected in less than 12 hours. Her current position makes her a natural choice, and as she is already on the ticket, she has the immense advantage of being able to access the current campaign funding, which is not obvious for others. She stands better chances than Biden: Trump's odds from Real Clear Politics have dropped from 66% to 58%. Still, Kamala Harris is not much more popular than Biden, despite not having her cognitive abilities questioned. Biden's exit could unleash the ambitions of alternative candidates. The bar is high: a credible candidate should have a national popularity, especially with the right demographics, be able to rocket start a campaign, raise millions, win the Democratic convention, then run with reasonable chances of beating a redoubtable opponent. The internal politics within the Democrat party may even be a higher hurdle, with many different currents, and for example probably little chances for a white male to displace Mrs. Harris. Still, an alternative candidate could be nominated on August 19th at the convention, through a relatively complex voting process. Mrs. Harris would anyway gain in popularity if she wins, rather than inherit, her position. At this point, we believe that it is either Kamala Harris with a solid VP, or a groundbreaking "super candidate" such as, our uninformed personal bet for long, Michelle Obama. With regards to markets, it's simply added uncertainty, which means elevated volatility from now on until November at best, as the nightmare possibility of an unclear result still exists.

It happens as we write this morning. The dollar is weaker, but it doesn't help Asian stock markets, unanimously in the red except for Hong-Kong, as the PBOC just reduced a short-term rate for the first time in almost a year. US treasury yields are slightly down in Tokyo trading, to 4.5% for the 2-year, 4.15% for the 5-year and 4.21% for the 10-year. Gold is up +0.3% to \$2,408 and so is Brent at \$80.6. So far, the "Trump rally" in crypto is not derailed, with bitcoin steady at \$68,000.

In terms of economic data, the week ahead will provide a rafale of flash PMIs for all regions from Wednesday onwards, and the first estimate of the US GDP for Q2 on Thursday, with the always important Core PCE being part of this quarterly report, with the June monthly measure detailed the following day. On the corporate side, the earnings season will get super busy with no less than 170 releases in the US alone, including major healthcare companies, blue chips such as Coca Cola, GE, UPS or Colgate, and a first batch of tech names including Alphabet, IBM, and Visa. We should also always be prepared for the unexpected: volatility is here to stay, which is are not unhappy to have cut equities form overweight to neutral earlier in July, with a slightly but clearly more defensive positioning (all details in the CIO Corner section of the Emirates NBD website).

Have a great week!

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