Trying to sift through the **noise**

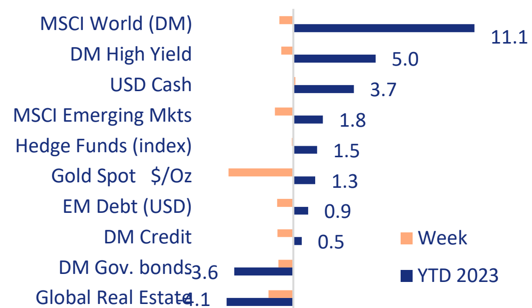
- **Last week, September, and Q3 all ended with negative returns from major asset classes, except cash**
- **Rising interest rates and energy prices are a threat to the global outlook…**
- **… But recent and forthcoming data will help paint a clearer picture**

Last week was another negative one, ending a negative month and the first negative quarter this year for all major asset classes. The weekend however brought positive news. First, the US Congress managed to avert a government shutdown, with a last minute, against-the-odds compromise providing funding until the 17th of November, while omitting to include additional aid for Ukraine, which was apparently needed to secure the vote. Second good news: China's Caixin PMI numbers were released on Sunday. At 50.6 for the manufacturing gauge and 50.2 for services, levels are not astonishing, but they are both in expansion territory, which raises hopes for some stabilization there. China just started their golden week holiday, which means that mainland stock markets will be closed until next Monday.

Back to the big picture. Markets are taking the Fed's "higher for longer" message seriously, while continuing to believe in a US soft-landing. Treasury yields are rising, the dollar is stronger, which, in combination with higher energy prices, means increased pressure on the global economy. Regional divergences are not to be ignored. However, while the outlook is not bright for Europe, the consequence is in an improvement on the inflation front. Signs of stabilization in China, if confirmed, could help Asia, even though it would also support demand for oil.

The year of unpredictability is not over, and markets are extremely nervous. We will focus on the most important fundamental factors: growth, and inflation. Regional PMIs on the one hand, US labor market data on the other will provide some insights this week. We will wait for those before taking any asset allocation decision. We still expect sustained volatility, as markets have recently confirmed their ability to turn quickly, and sharply.

ASSET CLASSES USD % TOT.RETURN, YTD 2023 & LAST WEEK



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Cross-asset Update

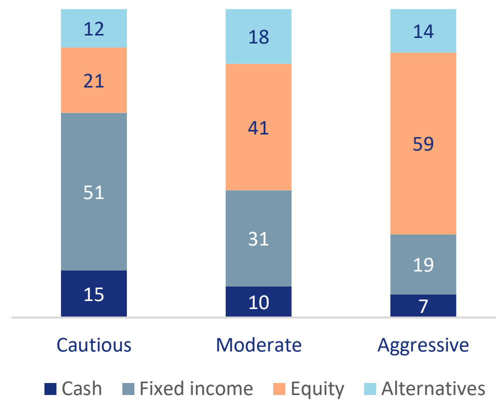
Although the fourth quarter sees equities start on a positive note as a government shutdown is averted, multiple crosscurrents ahead suggest markets could have entered a more sideways phase. Global growth is still bifurcated between US exceptionalism and other major areas where activity rates remain underwhelming, notably Europe and the UK, while China is just stabilising. In itself positive growth is sufficient to keep equities afloat, yet at the same time financial conditions have tightened significantly, due to yields rising fast, a stronger US dollar and elevated crude prices. We do not see a turn for the better unless the growth impulse, for now confined to the United States, broadens out to include China, that means Beijing should go for bigger stimulus measures. Hence, for now we must live with the shortcomings of US exceptionalism, supporting the global economy, even as it brings about more tightening of liquidity. Against this backdrop, exposure within asset classes with a quality bias is more important than exposure to asset classes, as it seems that both yields and the US dollar can have further to rise.

The past week highlighted more of the same about global growth. The gap between hard and soft data remains wide in the United States, with core durable goods orders making new highs, personal expenditure steady, though the consumer confidence release let transpire angst about a future recession. In China positive surprises from retail sales and industrial production, alongside manufacturing confidence inching towards expansion territory, suggest that Beijing's supportive measures are having the intended effects. That in turn may also indicate that the pain threshold for more drastic stimulus packages is high, so for now the trudging along continues in China and the growth impulse remains confined to the United States.

US exceptionalism is coming from fiscal dominance. Growth is resilient because government spending is going through the roof, rising at rates only seen during war times, that also has the darker side of increased debt issuance. Yields may rise further in the shorter term with no restraint in fiscal expenditure, a deficit in the crude market expected through Q4 further bolstering inflation expectations and reduced foreign buying of Treasuries due to prohibitive yield-hedging costs.

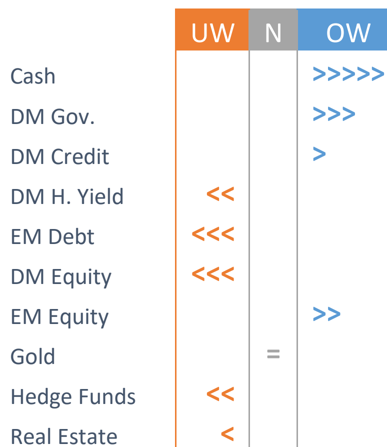
With both lights and shades dominating the outlook and a narrow growth impulse, investors may be tempted to add to their gold positions. We see gold struggling near-term, capped by tighter conditions driven by yields and the dollar. As focus shifts to peak rates when we are closer to the November FOMC meeting and at the same time investors question the sustainability of tight Fed policy, a relief rally can develop. We would see a more sustainable long-term bull market with the eventual implementation of yield-curve-control by the Fed to stave off unsustainably high borrowing costs with exploding US debt. But this would be a sort of end-game scenario for which there is now very limited visibility.

TACTICAL ASSET ALLOCATION: SIMPLIFIED POSITIONING



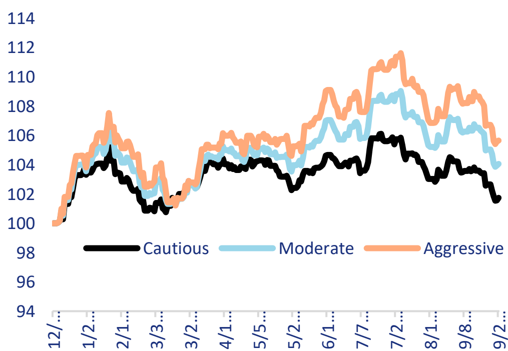
TAA – RELATIVE POSITIONING – MODERATE PROFILE

UW/N/OW: Underweight/Neutral/Overweight



	UW	N	OW
Cash			>>>>>
DM Gov.			>>>
DM Credit			>
DM H. Yield	<<		
EM Debt	<<<		
DM Equity	<<<		
EM Equity			>>
Gold		=	
Hedge Funds	<<		
Real Estate	<		

TAA – 2023 INDICATIVE PERFORMANCE



Source: Bloomberg. CIO Office calculation based on TAA applied to market indices, net total return in USD.

Fixed Income Update

The US Treasury yield curve has bear steepened further. While the 20 September FOMC dot-plot revision was the catalyst, technical factors exacerbated the sell-off. The 10-year crossed the psychological 4.5% barrier last week and remains elevated at 4.61%. The 30-year trades around 4.73%. It was the largest quarterly jump for the 30-year yields in 30 years. We think the Fed is done with tightening. However, several technical factors should keep yields elevated. The ongoing QT, elevated treasury issuance and decrease in foreign central bank demand for Treasuries would force investors to ask for a high term premium that would put a floor on long-dated yields in the short term. We are neutral duration at the moment and prefer the belly of the curve for positioning. We would wait for weaker macro data before increasing our preference for the long-duration trade.

IG corporate credit outperformed both High Yield and Emerging Market Debt last week. Bloomberg Barclays Global credit index spreads widened by 3 bps compared to 9 bps and 7 bps of the HY and EM Debt indices. According to JP Morgan, redemptions among IG credit ETFs rose over the past week ($4.2bn, 2% of AUM), suggesting some caution among the most liquid investors. This is understandable given that IG bond total returns stood at -2.2% in September and that the recent sell-off in equity markets is likely dampening risk appetite.

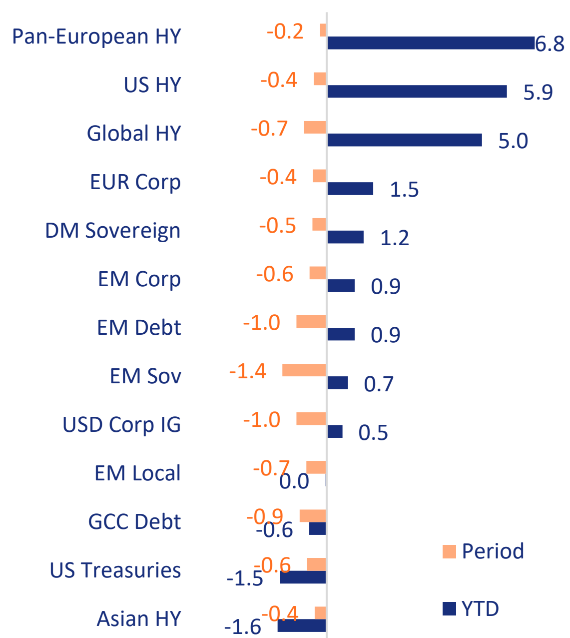
S&P upgraded Oman from BB to BB+ with a stable outlook. Meanwhile, the rating agency affirmed Turkey's rating at B, but its outlook was improved from negative to stable. Considering an overheated economy, large twin deficits, elevated inflation, and rapid money growth, the stable outlook reflects balanced risks to Turkey's creditworthiness from the reimposition of orthodox monetary policy settings. In an effort to disinflate and de-dollarize the economy, the Central Bank, under new leadership, has raised the critical one-week repo rate by 21.5 percentage points since June to 30%. To offset fiscal deterioration, the Treasury has introduced indirect taxes. S&P believes that by 2026, absent renewed political uncertainty, the new team can rebalance Turkey's economy away from external debt-financed consumption and toward more balanced external and fiscal accounts, as well as more acceptable levels of inflation.

With three-quarters of the year over, GCC primary issuance has come out of the doldrums of 2022 and is slightly lower than the 2021 run rate. According to bond radar, YTD issuance above $54bn is higher by 67% over the full year 2022 issuance figure of $32.6bn. UAE issuers have contributed roughly one-third of the issuance. Financials from the UAE have led the bandwagon, contributing 42% to the total, followed by GREs, which amounted to 32% of the total issuance. The tilt to quality remains, with IG issuers selling 85% of the bonds this year. We have also seen an uptick in Sukuk issuance, with the figure crossing $6bn. A new development has been the issuance of AED-denominated bonds by the country's banks, which provides investors with another niche segment within Fixed Income.

FIXED INCOME KEY CONVICTIONS

DEVELOPED MARKETS
OW Quality corporates
OW Government Bonds
UW High Yield
EMERGING MARKETS
Overall UW EM Debt
Favor quality and selectivity
OW Selectively Asia,

FIXED INCOME SUB ASSET CLASS RETURNS (YTD, LAST WEEK)



Source: Bloomberg

Emirates NBD WEALTH MANAGEMENT

Equity Update

A negative week, month and quarter for global equities, however still strong YTD gains, with most regions and sectors positive. At the end of Q3 developed markets are up 11% YTD, with the US leading returns and the Eurozone and Japan in USD terms just a little behind. In local currency Japan equities have had a great 3 quarters with the Nikkei up +24% YTD. US equity returns were boosted by AI driven sentiment gains of the big 7 tech companies. Whilst the tech sector fell c. 6% in September as higher yields impacted high growth sector performance, the Nasdaq is +27% YTD with Nvidia up almost 200%, Meta +150%, Tesla +100%, and on average the big 7 tech are +85%. In 2023 AI has been the greatest disrupter for stock markets. Also, a large difference between the current 36x forward PE for the Magnificent 7 tech stocks and 17x for the rest of the world. Emerging market equities at +1.8% YTD, have the Dubai Index in the lead, +31%, with India +8% in USD terms and China diametrically opposite at -7.3%.

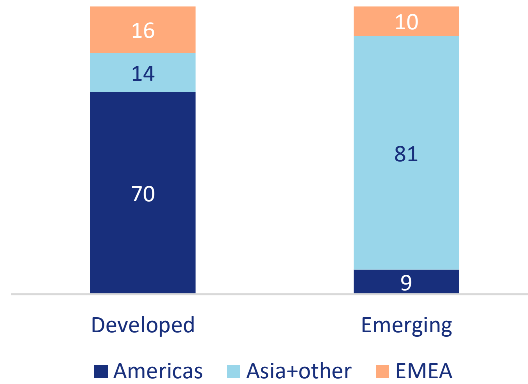
September was not a good month for equity returns barring India, the UAE and the energy sector. In the last two months, US treasury bonds have suffered a steep sell-off, with 10-year yields rising to their highest since 2007, with the reality of "higher-for-longer" for corporates. With 10yr US real rates now 2%+ interest rates are an important determinant of performance. What's relevant is that in the past 100 years the S&P 500 mean return was 8%. This includes all the sell offs and higher interest rate regimes. As per the latest Flowshow report from Bank of America the 21st century price to earnings equity multiple for the S&P 500 is an average of 19x, close to valuation levels currently, then equities are fine; but if new secular trends mean a lower multiple with higher rates that's a worry. However, earnings have turned a corner (flat y/y for Q3 is good), net margins are in the 11.5% range and inflation ticking down, even with higher oil prices. We expect US markets to trade around current levels, with the Q3 earnings the next catalyst.

We are overweight the UAE and India and remain neutral EM Asia. The Dubai market continues to add to gains with the real estate sector rally continuing. No impact from higher interest rates as property sales are not mortgage driven. Plenty of luxury sales but end-user buying by professionals and successful off-plan launches continue. The service economy: hotels, airlines, education are above pre-pandemic levels.

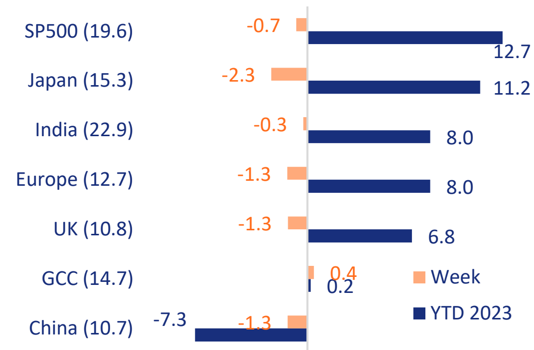
India's GDP growth 7.8% y/y in 2Q23 fundamentally supports Indian equities. Also, China's economic struggles are benefiting Indian equities. However, India's economy is sensitive to the price of oil. The long-awaited inclusion of Indian government debt in JP Morgan's benchmark index for EM sovereign bonds should help lower yields and add to a monetary policy that is expected to turn accommodative if inflation stays in the India's central bank 4-6% target.

China's policy towards both the economy and markets has been more positive in September and recent economic data has beaten expectations. However, a sustained turnaround will require much better growth outcomes with Evergrande debt woes and real estate downturn bad for sentiment. What stands out is Chinas dominance in auto exports, both combustion and EV's.

EQUITY RECOMMENDED REGIONAL POSITIONING

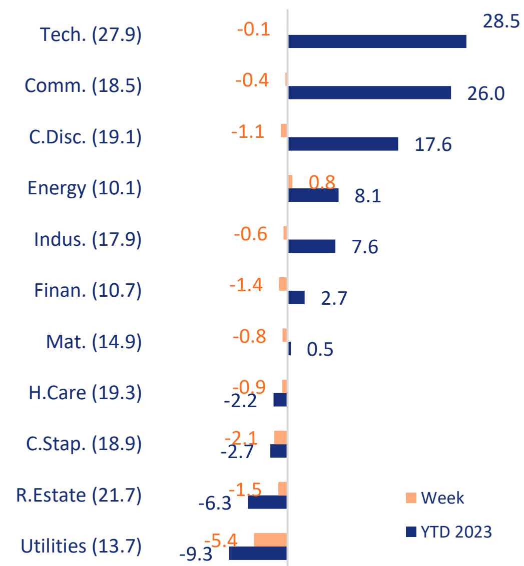


MAJOR INDICES PERFORMANCE (TR, US$) AND 2023PE



Source: Bloomberg consensus. MSCI Indices unless specified.

GLOBAL SECTOR PERFORMANCE (TR, US$) AND 2023PE



Source: Bloomberg consensus. MSCI All Country World sectors US$.

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