Unstable **equilibrium**

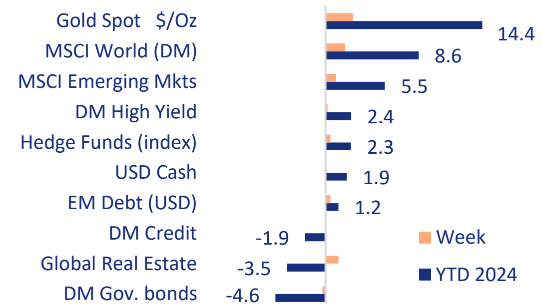
- **It was a quiet week for economic data as corporate earnings continued to shine**
- **The big picture is constructive and relatively balanced though volatility has no reason to abate**
- **Keep an eye on US CPI as well as monthly retail sales and industrial production this week**

Last week provided a welcome relief after the recent avalanche of macro datapoints. The big picture for now is about balance: growth momentum is gently slowing under the impulse of the US decelerating, but healthy emerging regions and signs of life in Europe are providing some robustness to the global picture. Inflation remains too high as compared to central bank targets, yet policymakers have recently turned more risk-adverse, from the Fed at the beginning of the month to the Bank of England last week, the latter further opening the door to a forthcoming cut. The Riksbank of Sweden actually started to cut, and the PBOC, against a totally different backdrop, could also follow suit. Bottom line, with a positive corporate earnings season in Q1, stocks continue to be sought after, helped by a massive rebound in China. US Treasury yields are also in a better place: the current Fed narrative and signs of moderation in activity obviously support demand for bonds, which explains the success of last week's treasury auction.

Are we headed for a tranquil summer? Certainly not. Yes, we are happy to see that markets pay more attention to fundamentals than to just central banks, and fundamentals are not adverse. Still, we are just one economic datapoint or geopolitical event away from another turn in markets' mood. Diversification, patience and discipline are paramount, and necessary conditions to express (our current) reasonable optimism.

We remain overweight cash, bonds of limited duration and equities, especially in emerging markets, funded by a clear underweight in alternatives, except gold. But our active positions remain measured. We expect volatility but see the current backdrop as positive. We will get a more accurate picture on inflation and activity this week, with various CPI and economic data.

ASSET CLASSES USD % TOT.RETURN, 2024 & LAST WEEK



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Cross-asset Update

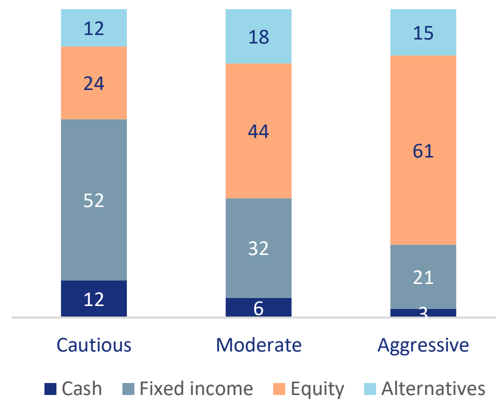
Inflation has become the key variable to watch as it impacts rich equity market multiples via expectations of Fed rate cuts. Of the two much debated scenarios, a soft landing and a no landing one, the former has of late gained traction on softening US macro data. And although stagflation is not contemplated by Fed chair Powell, who quipped at the last press conference that he does not see "the stag or the 'flation", the recent uptick in price pressures has given investors some apprehension about the possibility of a third scenario. Indeed, in the shorter term the inflation rate could record some further upticks, given for instance rising commodity prices. But in the end the effects of rates being high for longer should bite on the economy and allow the disinflation process to continue. Despite some bumps along the way, we still think some form of Goldilocks backdrop remains a base case for now.

Unpleasant economic and inflation surprises should be reckoned with in the interim. Unemployment seems very resilient on the surface, yet US smaller companies have been reining in hiring plans for a while according to surveys, usually a signal that larger corporates will follow suit down the road. And according to the ISM report the outlook is now muted in manufacturing and services, with both sectors in contraction territory. At the same time, the additional liquidity to be provided by the Federal Reserve starting from June with the reduction of Quantitative tightening should help make the path to an orderly slowdown smoother. On the inflation front, higher commodity prices could weigh on headline indexes, while the core index in the PCE release, due out May 31, could be lifted by rising minimum wages in the food sector.

In Europe and China the growth inflation trade-off is quite different. It remains most favourable in Europe, with growth accelerating from a low base and price pressures still well behaved. Hence, the rising expectations that the ECB will start easing policy in June. It is less favorable in China, where deflation is persistent due to lackluster demand in the private sector. Hence, the determination of the authorities to provide further support to the ailing real estate sector. The third meeting of the Communist party in July, where usually long-term growth prospects are discussed, is the next catalysts investors will be looking to.

Overall, we remain constructive, with the equity rally broadening outside of the United States, a reflection of a fading US exceptionalism providing room for different market narratives.

TACTICAL ASSET ALLOCATION: SIMPLIFIED POSITIONING

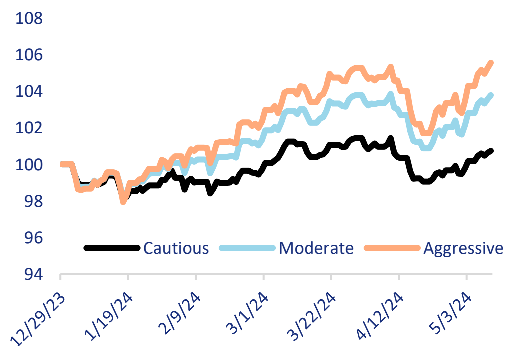


TAA – RELATIVE POSITIONING – MODERATE PROFILE

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 – 2024 INDICATIVE PERFORMANCE



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

Fixed Income Update

Last week was relatively calmer as compared to the previous one. The US Treasury yield curve twisted flatter with the 2-year increasing by more than 3bps, while the 30-year was lower by more than 2.5bps. The US Treasury auctions ran smooth being met with large demand and orderbooks keeping around the average 1-year levels. Initial claims rose from 209k to 231k, the highest since August 2023, though data was affected by seasonal factors and could be an exception. Meanwhile the preliminary University of Michigan survey showed a sizeable drop in consumer sentiment from 77.2 to 67.4, even as short- and medium-term inflation expectations rose to 3.5% and 3.1%, respectively. It remains to be seen if Chairman Powell's comments of "neither stag nor flation" age well.

This week the focus turns to the last barrier against the rate cut, i.e., inflation. The consensus estimate is for a 0.4% headline print. Expect yields to remain volatile. The BOE's Monetary Policy Committee voted 7 to 2 to keep rates unchanged at 5.25%. Bailey said that the BOE will likely need to cut interest rates "over the coming quarters." He said a cut at June's meeting is "neither ruled out nor a fait accompli." Markets now anticipate 63% probability of a rate cut in June. Tuesday's Jobs data assumes significance given the preliminary Q1 GDP estimates for the UK indicated that the country has returned to growth exiting a technical recession in the past two quarters. We also get the Final eurozone CPI print and preliminary Q1 GDP data out on Friday and Thursday respectively.

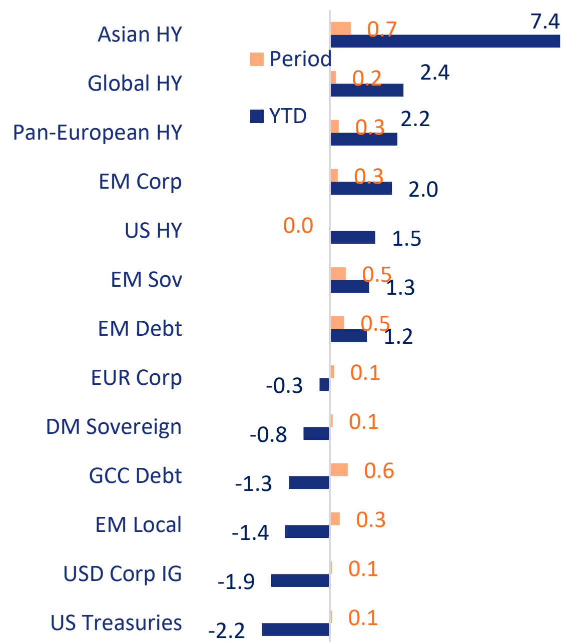
Investment Grade bond yields have drifted lower following the more benign than expected Fed commentary and payrolls report last week. In this quiet week for macro and earnings data the true picture of HG bond technicals was apparent. Spreads rallied despite a surge in issuance, with $51bn of supply in the first three days of the week, marking the largest weekly supply tally since mid-February 2024. One of the most surprising developments in credit markets over the past two years is continued low default rates in HY and leveraged loans despite the much higher coupons brought about by the Fed's policy tightening. Notably, the current default rate on loans is 61bp higher than on HY bonds while historically HY bonds have a 40bp higher default rate. This illustrates that bond issuers have benefitted from fixed coupons while the floating rate coupons have impacted the loan market more on a relative basis.

Last week we saw interesting issuances across the regions. In the GCC, Al Rajhi Bank issued a $1bn USD-denominated AT1 perpetual bond at 6.375%, while Aldar issued a 10-year bond at 5.50%. We saw an exciting opportunity in the developed markets with Barclays issuing a GBP-denominated Perpetual CoCo bond at 8.5%. In Asia, Muthoot Finance priced its 3.75-year bond at 7.125%. Muthoot is a market leader in the niche area of gold loans with around 45% market share in the segment. Muthoot's leading position in the gold loan segment, with strong capital ratios of Tier-1 at 30%, a strong track record, a strong net interest margin of around 10%, and manageable NPAs at 3.6% given significant collateral, provides us with comfort over the issuer.

FIXED INCOME KEY CONVICTIONS (2024)

DEVELOPED MARKETS
Overall overweight DM FI
OW Government Bonds
Neutral corporate (IG & HY)
EMERGING MARKETS
Overall UW EM Debt
Favor quality and selectivity

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



Source: Bloomberg

Emirates NBD WEALTH MANAGEMENT

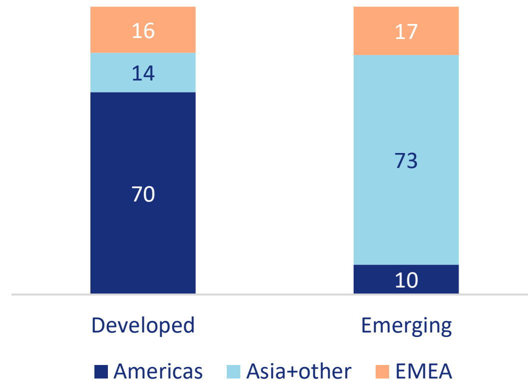
Equity Update

Global equity markets picked up last week following a challenging and volatile month. Global stocks rebounded now fractionally below all-time high levels; the S&P 500 is just 1% away. We are at the late stage of Q1 earnings season and S&P 500 companies continue to beat expectations. As of date, blended growth for 1Q24 is 5.4%, dragged down by three health care companies - Bristol Myers Squibb, Gilead Sciences and Pfizer. Excluding these three companies blended growth for Q1 S&P 500 earnings would have been 9.7%. 92% of the index have reported so far and seven companies are announcing this week. Now analysts have boosted expectations for the upcoming quarter as the economy remains resilient and consumer demand robust. The upwards adjustment for earnings was led by the energy and materials sectors, with strong links to the economic cycle. The advance in stocks is also attributed to the $25 billion sale of 30-year bonds, which saw decent demand. Next week, the biggest US retailers will report, providing insight to consumer strength and the trajectory of economic growth. Nvidia's release, the last of the magnificent seven companies to report, will take place on May 22.

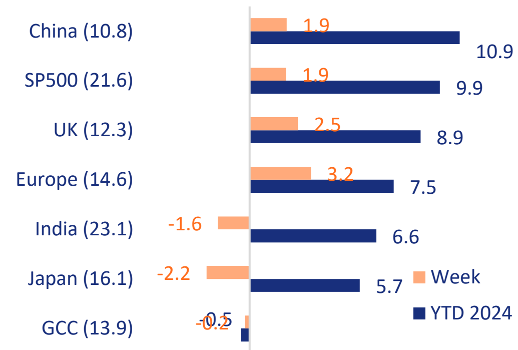
Europe's STOXX 600 hit a fresh record high, up 3.3% last week, supported by the prospect for rate cuts. Corporate earnings are falling on a year over year basis but rise sequentially for the first time since 2022. The MSCI Asia Pacific Index climbed 0.8% for the week. Lead by Hong Kong with news that regulators considering tax on dividends exemption on individual investors, a significant positive for trading volumes. China continues to rally with relatively low valuations and government initiatives to boost the struggling economy, capturing the lead amongst major equity markets. However, President Biden is poised to unveil decisions on China tariffs this week, expected to target key strategic sectors. All eyes are on heavyweights Tencent and Alibaba which will publish results tomorrow, followed by JD.com and Baidu day after. The weaker yen no longer supports Japanese stocks as the main index declined even as the currency headed towards 160, now down to 155. The TOPIX has gained 16% this year in local currency terms, but only 5% in dollars, demonstrating currency risk for foreign investors. Rising costs of imports such as food and energy could hurt growth in real wages and consumer spending.

OpenAI will have a livestream today to announce GPT updates. Travel spending may slow as Airbnb gave lacklustre guidance. TSMC's April sales jumped 60% as sustained AI demand and Q1 showed the smartphone industry returned to growth. Nvidia's shares moved higher ahead of its earnings as TSMC provided clues on AI demand. SK Hynix, another key Nvidia supplier also posted its best quarterly profits in nearly two years, stating that AI demand drove the chip-market into a full recovery cycle. Spinneys had a successful IPO that was oversubscribed by 64 times, representing the highest level of demand for a non-government related IPO in the DFM. Salik has announced Q1 results today posting highest record revenue-generating trips and toll usage, pointing to the continued resilience the Dubai economy.

EQUITY RECOMMENDED REGIONAL POSITIONING

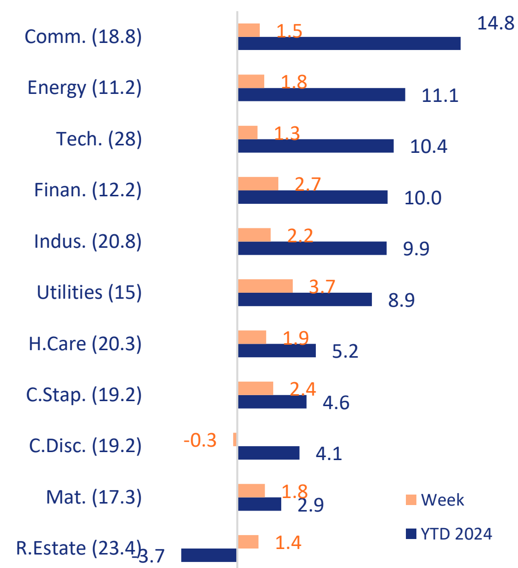


MAJOR INDICES PERFORMANCE (TR, US$), P/E in brackets



Source: Bloomberg consensus. MSCI Indices unless specified.

GLOBAL SECTOR PERFORMANCE (TR, US$), P/E in brackets



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

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