Emirates NBD
WEALTH MANAGEMENT

US Politics take **centre stage**

- **Last week was not about fundamentals, but about US politics, policies, and a giant IT failure**
- **All asset classes suffered, with the only exception of Real Estate and US small and midcaps**
- **The week ahead will be rich: flash PMIs, US Q2 GCP and core PCE, and many corporate earnings**

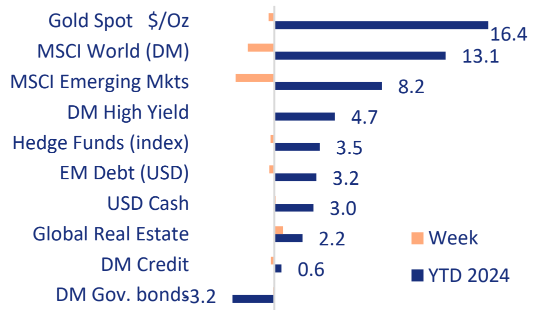
Last week started with the "Trump trade", ended with Biden dropping out, with one of the largest IT disruptions ever in the meantime. Returns were negative across most asset classes, with a massive rotation out of tech mega caps, also hit by trade restrictions on semiconductors, into smaller companies and listed real estate. Still, economic data and central bank newsflow was indeed consistent with the constructive "Goldilocks" scenario of a soft landing, disinflation, and rate cuts.

First, Friday's IT failure, triggered by an issue with a routine cybersecurity update, is a wake-up call on the vulnerability of the global digital ecosystem. For the short-term, it confirms that richly priced tech stocks will be volatile, and that they'd better deliver on their quarterly earnings. For the long-term, cyber risks are real, and cyber security is a secular investment theme.

On US politics, as our readers know, seeing President Biden passing baton to VP Kamala Harris should not come as a surprise, especially after Mr Trump picked a MAGA hardliners as his running mate, which helps Democrats with the undecided, assuming they have the right candidate. However, good news for Democrats may not be great for markets, who value nothing more than visibility. The elections are not a done deal, and certainty on the Democrat candidates will only come out of their convention on August 19th. We had reduced risk earlier in July for this exact reason: increased volatility from political events, and it has started.

The week ahead will be rich, with flash PMIs providing insights in the major economies, followed by the first estimate of US Q2 GDP and core PCE inflation, along with hundreds of corporate earnings, including a first batch of tech names. Prepare for volatility and have a great week.

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



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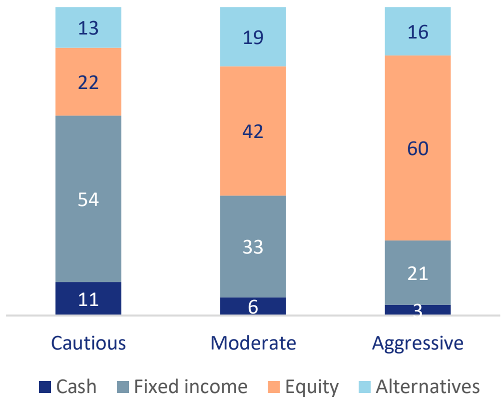
Cross-asset Update

Equities are undergoing a sector rotation to unwind the excesses of the lopsided rally that took large caps to their recent highs mainly on the back of the IT sector's outstanding returns. The performance gap between information technology and the rest of the market has reached excesses last seen only during the dot com bubble and it was only a matter of time, and catalysts coming together, before the shift would be taking place. This time the main catalyst was offered by the earnings season, as IT stocks, though maintaining well above-average bottom-line growth in absolute terms, should see earnings expand at slower rates in the next quarters, as against other sectors that should be catching up with improved earnings, according to projections. The Washington administration planning to enforce even stricter sanctions on US chips to be traded with China reinforced IT's vulnerability. Also, investors are getting more convinced that starting from September the Fed will be cutting rates, even as the economy remains relatively resilient. The earnings differential supported by a solid economy warrants that investors partially sell IT stocks to buy the more cyclical pockets of the market. Rotations do not come without some volatility and this time would be no exception. The last two days of the week saw the rout extend from IT to small caps and the broader market in general. But we do not think this should be seen as a cause for concern, but rather as an indication of overbought conditions. Underneath the surface the market has maintained a bullish bias with an elevated number of advancing issues versus declining issues, that historically anticipated positive returns down the road.

In reaction to rising volatility the dollar is staging a mild rebound, while yields are falling in response to increased investor conviction about the Fed's cuts, the first one priced in with 100% probability by money markets for September this year. We retain the view that as the US economy continues to slow down the yield on the US 10-year note should approach our 4% fair value. Gold counterintuitively is pulling back with equity markets, and we would tend to think that its returns would be capped until volatility subsides and we get closer to the timeline for rate cuts.

So far, the year is unfolding according to the typical election year pattern, with markets on a positive trajectory till the presidential elections come into focus and volatility spikes. Also, risk assets have tended to churn in July to then resume the rally in August. It seems markets may remain on track for this as well.

TACTICAL ASSET ALLOCATION: SIMPLIFIED POSITIONING

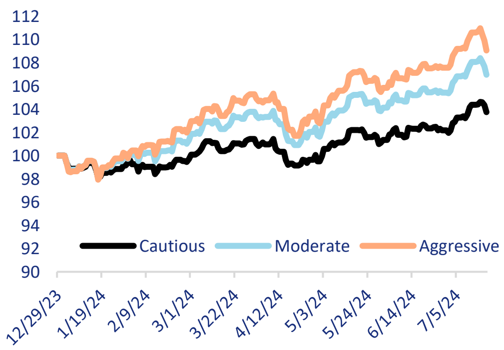


TAA – RELATIVE POSITIONING – MODERATE PROFILE

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

The US Treasury curve bear steepened during the week, with around 3-5bps across the curve, reflecting political volatility and continued anticipation of future Fed rate cuts. The market looked through a solid beat in June US core retail sales (+0.8% YoY vs consensus: +0.2% YoY) and the soft non-dealer demand for the $13 bn 20Y UST auction. Following dovish statements by Jerome Powell and other fed members, all attention is now on the upcoming month-end Fed meeting, with expectations that the Fed will keep rates unchanged, but the market fully pricing in a cut at the September meeting.

The European Central Bank (ECB) kept its interest rates unchanged in a unanimous decision, opting not to provide an explicit signal for September. This aligns with their data-dependent, meeting-by-meeting approach. President Christine Lagarde emphasized during a press conference that the decision for September remains "wide open," reinforcing the ECB's stance on not committing to a specific rate path. In the emerging markets, the Central Bank of Egypt maintained its policy rates at 27.25%, as anticipated. ENBD research forecasts a cumulative 200 basis points of cuts in the fourth quarter. The Central Bank of Turkey (CBRT) is expected to keep rates unchanged tomorrow. Moody's have upgraded Turkey's sovereign rating to B1 from B3, with a positive outlook. Moody's highlighted that the key driver of the upgrade is improvements in governance, more specifically the decisive and increasingly well-established return to orthodox monetary policy. This is yielding first visible results in terms of reducing Turkey's major macroeconomic imbalances.

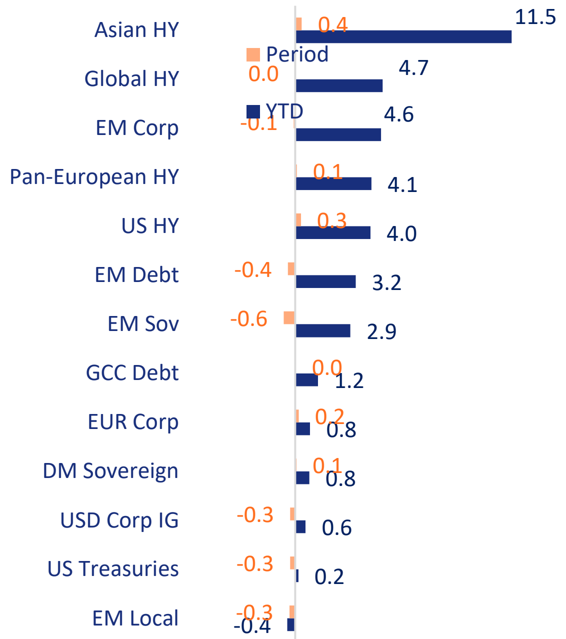
Credit spreads remained stable, with Bloomberg benchmark spreads for emerging market debt widening slightly, while spreads for investment-grade and high-yield indices stayed steady during the week. As per a JPM report, the US investment-grade bond market has revised its supply forecast upwards to $1.45 trillion from the previous $1.3 trillion. Including coupon payments, the net supply for the second half of the year should be close to zero, contrasting with the positive $210 billion net supply in the first half. Credit metrics have shown some deterioration, with leverage near the higher end of its five-year range and interest coverage near the lower end. Despite these trends, ratings have been positive, with the BBB share of the market at an eight-year low. However, JPM anticipates more Fallen Angels than Rising Stars moving forward.

In the GCC region, year-to-date bond issuance has reached approximately $79 billion, surpassing last year's total of $66 billion. Last week's primary issuances included bonds from RAK Bank, GreenSaif, and Masdar. RAK Bank's 5-year senior unsecured bond was priced at 135 basis points above Treasury, translating to 5.44%. Masdar's five-year and ten-year bonds were priced at 5.03% and 5.32%, respectively. GreenSaif, from Saudi Arabia, issued 12-year and 18-year bonds priced at 5.85% and 6.10%, respectively. Additionally, Woori Bank from Asia issued a perpetual AT1 bond at 6.375%, marking the first such issue from an Asia ex-Japan bank this year.

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

Equity Update

It's been a volatile week with most indices ending lower except the GCC regions (the UAE and KSA) along with interest rate sensitive sectors i.e., the Russell 200 Index (US mid cap), consumer staples and real estate. Some of the factors behind this move include decelerating inflation and increased confidence the Fed will cut in September, conviction in economic growth, market probability of a Republican sweep on the rise and a decrease in the EPS growth premium of large-cap stocks.

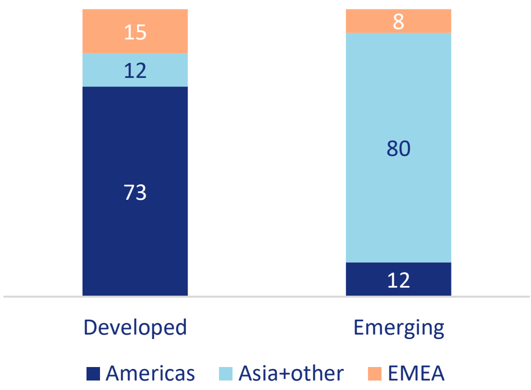
The MSCI UAE Index was up almost 3% last week. Earnings season began with banks and stellar results so far with EPS growth buoyed by loan and deposit growth, along with retail credit and wealth management growth as the UAE economy stays robust. Both oil and non-oil growth contributing to wealth creation and consumption. Real estate, both commercial and residential have had strong rental and sales uptakes with prices still rising.

The week saw the tech sector lower, down from its peak by 7% as are the Mag 7 stocks (though still up +38% YTD) with the semi companies also lower. TSMC affected by the possibility of geopolitics escalation in Taiwan and Nvidia lower on increasing restrictions to exports to China. Focus on dependency on cloud enterprise security as a software update went wrong from Cybersecurity firm Crowdstrike, causing a major global outage across Microsoft Windows users. The CrowdStrike outage highlights need for cyber resilience, security and robust testing. Widespread outages on Microsoft systems, though not a security incident or cyber-attack. Expect the outage to increase calls for cyber resiliency.

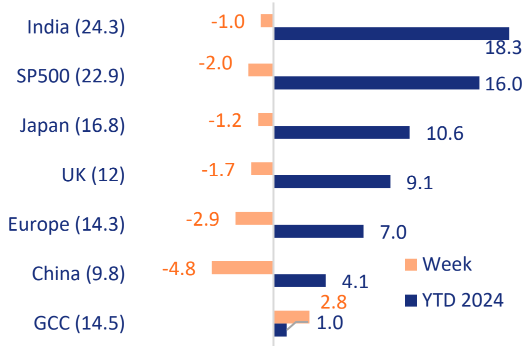
The Nasdaq Index is up 18% this year after last week's -3.6% and the S&P 500 Index 16% in 2024, with much of the advance generated by the largest tech stocks. Interest rate sensitive sectors have been gaining recently, though the rally of small- and mid-caps didn't continue as the end of the week saw some weakness. Not yet the great rotation but the positive impact of lower rates on the smaller companies (which have lower margins and credit ratings) and real estate in the US is now a significant move. So far 15% of the S&P 500 has reported and the top line trends, looking very healthy and the blended earnings growth rate for Q2 S&P 500 EPS at 9.7% SPX ex Mag-7 earnings are projected to be positive at +5% y/y, for the first time in 5 quarters. Heading into the key stretch of tech earnings as 29% of S&P market cap will report this week: Alphabet earnings due Tuesday, with Tesla, Apple, Microsoft, Amazon and Meta following. The Mag7 group (29% earnings growth expected in Q2) has benefited from AI-fuelled optimism and strong revenue growth and no misses will be tolerated. Concerns arising that sales may not rise commensurate with AI investment spending.

Not much impetus for markets from the China Plenum except that to combat the property slowdown, plans will be put in place to accelerate development of "emerging and future industries," such as electric vehicles and solar.

EQUITY RECOMMENDED REGIONAL POSITIONING

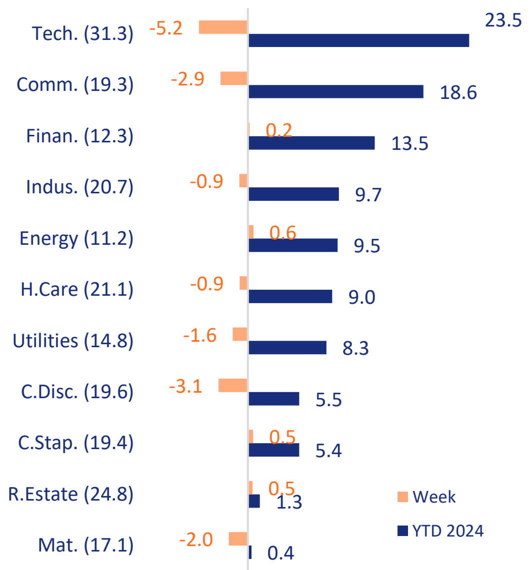


MAJOR INDICES PERFORMANCE (TR, US$), P/E in brackets



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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