Some profit taking, no change in the **big picture**

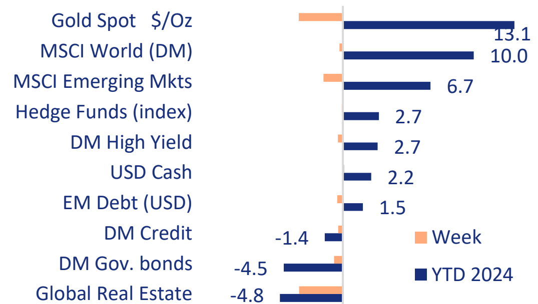
- **Last week was negative across all asset classes except cash, with gold and China underperforming**
- **The Fed's "higher for longer" narrative was probably the catalyst, but economic data was overall positive**
- **This week starts with a US and UK holiday but will end with the crucial monthly US Core PCE release.**

Last week was negative for all asset classes, which we see as a "profit taking" mood, as the recent outperformers such as gold and Chinese stocks were the most affected, and as there was no clear fundamental catalyst. Of course, from the FOMC minutes to various speeches from officials, the Fed's "higher for longer" narrative was cemented. Still, this is not new news, and we keep on expecting no rate cuts until September. US Treasury yields added around +10 basis points across maturities, weighing on the fixed income asset class. Stocks fell -0.3% in developed markets, helped by a positive US close on Friday, and -1.5% in emerging regions with China underperforming. Gold and global listed real estate also suffered, falling -3.4%.

The fundamental picture, however, did not change. If anything, the first estimate of the May PMIs (so called "flash PMIs") were positive. At the broad composite level, which combines manufacturing and services, indicators improved in Japan (52.4), the Eurozone (52.3), India (61.7), and surprised positively in the US (54.4). The UK was the only relative disappointment, especially as core CPI inflation for April came in stronger than forecast. The surprise announcement of general elections in July also complicates the task of the Bank of England. We still expect the ECB to cut rates next month, while the Bank of Japan may consider some carefully calibrated hikes to counter the yen weakness.

The week ahead will be rich in terms of data, culminating on Friday with the always important US core PCE monthly release. The Fed's preferred measure of inflation is expected to be stable at +2.8% year over year. We will also look at consumer confidence in the West, inflation in the Eurozone, various Fed surveys, elections in South Africa and China's official PMIs. Have a great week.

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



MAURICE GRAVIER
Chief Investment Officer
MauriceG@EmiratesNBD.com

ANITA GUPTA
Head of Equity Strategy
AnitaG@EmiratesNBD.com

GIORGIO BORELLI
Head of Asset Allocation
GiorgioB@EmitatesNBD.com

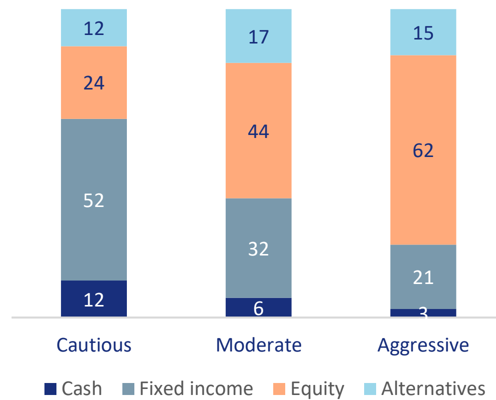
SATYAJIT SINGH, CFA
Head of Fixed Income Strategy
SatyajitSI@EmiratesNBD.com

Cross-asset Update

Gold and Treasuries are both safe havens, though they react in opposite ways to inflationary pressures, the former more often than not benefitting, the latter losing in value. Whether one outperforms the other tells us whether inflation is going to be challenging or not. Recent gold gains suggest that there is rising concerns that the great inflation moderation of the past decade is now behind us, and that more sustained price pressures may be in the offing. And since Richard Nixon dropped the gold standard in the early 70s, that is the convertibility of the US dollar into gold, gold has indeed recently started to outperform US Treasuries in total return terms. Something that had not happened since the mid-80s. Money managers will ask themselves whether Treasury coupons at current levels are compensating investors for the inflation risk taken. We really do not think so. This is telling us that it is appropriate to hold allocations of gold in portfolios high enough to offset the loss of value in Treasuries stemming from future price pressures not yet priced in by the market. This is only one of the many secular factors supporting the case for gold, with others lining up like the swelling of debt levels in the West and de-dollarisation.

The world is becoming more fractured. Economic warfare via tariffs is just a symptom of it. Trade wars point to no easy way back to the previous world order. That order was represented by the ascendancy of global trade under the auspices of the World Trade Organisation. China had been welcomed into that order thinking that it would contribute to its thriving given the sheer size of the country. But China overwhelmed all expectations and turned in the unsurpassable manufacturing juggernaut that nobody could manage to compete with. Nowadays China is keen on what remains of the WTO framework, while the West much less so. Tariffs levied on China starting with President Trump have been maintained and reinforced by President Biden. Europe is thinking of erecting barriers as well. Last week China announced it would retaliate. And the G7 joint communique issued following its meeting during the week-end is particularly harsh against China and is not boding well at all. In this war to the last tariff all countries will stand to lose, yet all the more so the more open areas or countries like Europe, China itself, Japan and Korea. But nobody is immune, and actually who starts to impose tariffs may think of having a weak side to have to shield. American farmers are among the most vulnerable should China importers decide to send their orders elsewhere. Investors are now confronted with a new emerging risk.

TACTICAL ASSET ALLOCATION: SIMPLIFIED POSITIONING

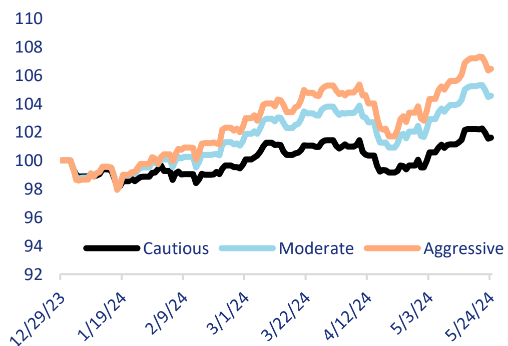


TAA – RELATIVE POSITIONING – MODERATE PROFILE

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

Front-end treasury yields drifted higher last week after a robust flash US PMI print. The composite PMI rose to 54.4 and is the highest reading since April 2022. The 2-year yields shot up by 10 bps post the release and currently hovers around 4.95%. On a weekly basis, the 2-year has gone up by 12 bps, while the 10-year has increased by 4 bps. FOMC minutes released last Wednesday, mentioned that "various participants" would be willing to "tighten policy further should risks to inflation materialize..." In Fedspeak, meaning it's more than two members, yet less than half that expressed this view. The Fed's Beige Book, scheduled for release on May 29, may provide Fed members' insights into the health of the economy. As mentioned in the earlier weeklies, we are neutral duration as we think the bar for a sustained rally is now quite high unless the pace of inflation declines significantly.

There have been a lot of media reports about realized losses of BWAY 2015-1740, a single-asset/single-borrower (SA/SB) CMBS transaction. Specifically, AAA note holders will face modest losses (26% according to Bloomberg) given a weak recovery upon the sale of the collateral, a midtown New York City office building. According to GS, post-GFC, there have not been any AAA CMBS losses. However, recently Single Asset/Single Borrower concentration risk means there would be more such cases. Eight outstanding urban office loans in SA/SB securitizations are currently delinquent out of which losses could near AAA attachment points for three of the deals if 20% recovery expenses are incurred. Distressed sales prices may weigh on outstanding market values, particularly in areas with high concentrations of liquidations but cash and synthetic bond prices indicate that the current impact on the broader CMBS market remains contained.

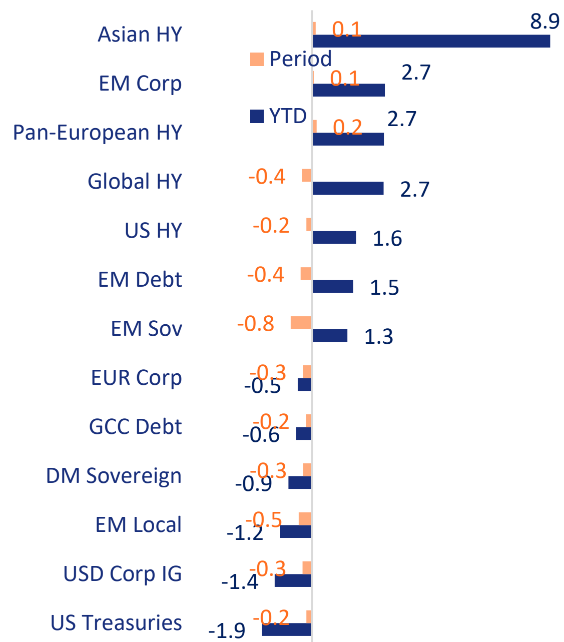
Month-to-date issuance in the USD IG market has already exceeded $117 billion, on pace for the highest monthly total since February. At $799 billion of issuance on the year, 2024 now trails only 2020 as the fastest start to the year ever for USD IG gross supply. Despite this heavy primary market calendar, demand has held up well, as evidenced by the resilience of new issue concessions. GS estimate of the four-week moving average of new issue concessions now sits at around 5bp, down from the 10-15bp range through much of last year.

The GCC issuance engine also chugs on. Bank of Bahrain and Kuwait (BBK), rated B2/B+ by M/F, has issued a mandate announcement for 5-year senior unsecured bonds. Categorized as D-SIB, BBK maintains strong capitalization ratios, with a tier-1 ratio of 27% and a total CAR of 28.1% as of Dec 2023, with total asset base of $10.9Bn. The bank is 52.2% owned by government entities from Bahrain and Kuwait through the Social Insurance Organization (33%) and Kuwait Investment Authority (19.2%). The bank accounts for 10% of domestic banking retail assets in Bahrain. This should generate decent demand among local investors.

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

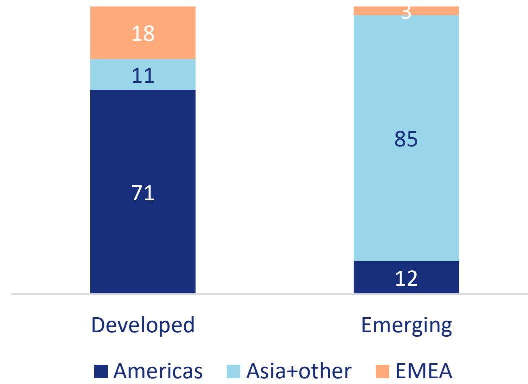
Equity Update

Global equities were mixed last week, starting quietly as markets awaited Nvidia's results, leading to larger movements in the second half of the week, and ended lower as the Fed signalled that policy rates will have to be kept higher for longer. Friday however closed positive after data showed that consumers are not as pessimistic on the inflation trajectory. Developed and emerging markets combined closed -0.4% last week dragged down by China (MSCI China, -4.8%) yet offset by India (MSCI India, +2.1%). The S&P 500 Index closed flat above the 5,300-level last week despite Nvidia's stellar results as all but the technology sector ended in the red for the week.

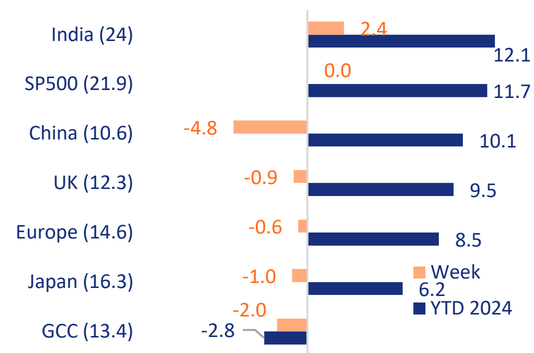
We are now at the end of the earnings season with 96% of the S&P 500 index reported earnings and 78% reported a positive EPS surprise, a robust quarter. Earnings growth for Q1 so far is 6.0% (vs 3.4% in Q1'23). Excluding Nvidia (the largest contributor to earnings), the growth rate for the index would fall from 6.0% to 3.3%. Nvidia posted remarkable financial results for the quarter, showcasing significant growth in earnings and solid outlook. The CEO of Nvidia emphasized the company's pivotal role in the emerging industrial revolution, with many companies and countries partnering with the company to transition from traditional data centers to accelerated computing – AI factories. Nvidia's market valuation is at $2.6 trillion and is up 14.6% last week. The magnificent seven posted Q1 EPS growth of over 51% YoY, compared to the rest of the S&P 500 at -0.2%. Now hedge funds have increased their exposure to a broader set of AI winners, including companies within the infrastructure and utilities sectors.

European stocks ended a lacklustre week with slight declines (MSCI Europe -0.4%), along with the overall mood by worries of higher for longer rates in the face of strong economic data. Within Asia, China's stimulus rally has faded as some investors booked profits, with the MSCI China closing 4.8% lower for the week. Trade and industrial output are rebounding; however retail sales are slowing and house prices are witnessing a deeper contraction. China's AI price war continues to intensify with Tencent lowering pricing on its Large Language Models, slowing the sector's path to profit. The broader EM market fell dragged down by Alibaba which is down 8% last week and makes up 2% of the index. Losses in Chinese tech was offset by gains by Taiwanese and Korean semiconductor stocks on the back of Nvidia's strong report. India equity markets reached an all-time high last week, with the Nifty surpassing the 23,000 mark for the first time on Friday. An announcement by the Reserve Bank of India to give a dividend of Rs 2.11 trillion to the government significantly improved market sentiment. As of Monday morning, Asian stocks rebounded; data showed that China's industrial companies profits rose last month driven by the governments push to upgrade equipment, lifting demand and exports returned to growth.

EQUITY RECOMMENDED REGIONAL POSITIONING

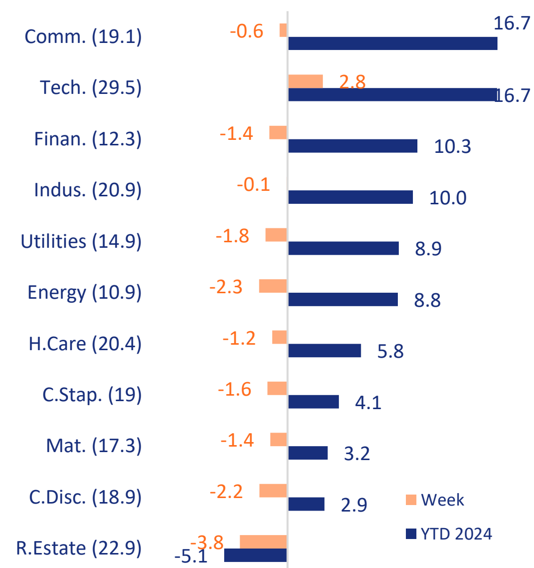


MAJOR INDICES PERFORMANCE (TR, US$), P/E in brackets



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$.

Emirates NBD
WEALTH MANAGEMENT

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