The Weekly Market View

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بنك أبوظبي التجاري
ADCB

Global growth concerns translate into global equity selloff

Despite relative stability in the Renminbi last week, the ripple effect of its devaluation continued as the currency market volatility translated to a sharp selloff in the global equity markets. The immediate trigger was disappointing preliminary manufacturing PMI data for China which confirmed the markets' growth concerns. We suspect that the turmoil will continue for some days as pointed out by many risk indicators. Currency volatility, rising sovereign CDS and pressure on risky assets are clouding the growth outlook for Emerging Asia, as central banks will find it difficult to use monetary easing, rather many central banks could be forced to raise interest rates.

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US data could be under market focus besides Asian currencies

Asian currencies will continue to be under watch as markets look for further cues for risky assets this week. Markets will look for policy actions from the worst affected countries, namely Malaysia and Indonesia, despite Malaysia's clarification that it did not want to peg the currency or impose capital control. Any such action would further fuel regional currency volatility. On the other side, markets will also focus on US data, in particular revised second quarter GDP growth number. A strong positive surprise could calm markets somehow as they ponder to what extent China's problem constitute a real issue for global growth.

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Past week global markets' performance

Index Snapshot (World Indices)

Index	Latest	Weekly Chg %	YTD %
S&P 500	1,970.9	-5.8	-4.3
Dow Jones	16,459.8	-5.8	-7.6
Nasdaq	4,706.0	-6.8	-0.6
DAX 40	10,124.5	-7.8	3.3
Nikkei 225	19,435.8	-5.3	11.4
FTSE 100	6,187.7	-5.5	-5.8
Sensex	27,366.1	-2.5	-0.5
Hang Seng	22409.6	-6.6	-5.1
Regional Markets (Sunday to Thursday)			
ADX	4512.5	-4.6	-0.4
DFM	3709.8	-6.9	-1.7
Tadawul	8012.8	-7.7	-3.8
DSM	11345.5	-4.3	-7.7
MSM30	6089.87	-3.6	-4.0
BHSE	1320.0	-1.1	-7.5
KWSE	6052.6	-3.9	-7.4
MSCI			
MSCI World	1,651.0	-5.3	-3.4
MSCI EM	812.4	-6.0	-15.1

Global Commodities, Currencies and Rates

Commodity	Latest	Weekly Chg %	YTD %
ICE Brent USD/bbl	45.5	-7.3	-20.7
Nymex WTI USD/bbl	40.5	-4.8	-24.1
OPEC Baskt USD/bbl	44.1	-5.3	-15.1
Gold 100 oz USD/t oz	1160.8	4.1	-2.0
Platimum USD/t oz	1019.5	2.7	-15.6
Copper USD/MT	230.4	-2.0	-18.5
Alluminium	1535.25	-1.0	-16.3
Currencies			
EUR	1.1386	2.5	-5.9
GBP	1.5694	0.3	0.8
JPY	122.04	-1.8	-1.9
CHF	0.9466	-3.0	5.0
Rates			
USD Libor 3m	0.3291	1.4	28.8
USD Libor 12m	0.8479	0.4	34.8
UAE Eibor 3m	0.8029	0.9	18.6
UAE Eibor 12m	1.1243	0.6	10.7
US 3m Bills	0.0203	-74.9	-42.8
US 10yr Treasury	2.0365	-7.3	-6.2

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Downward pressure on risky assets not likely to recede soon

Another week of currency depreciation

Despite relative stability in the Chinese Renminbi last week, most emerging market (EM) currencies, in particular Asian EM currencies, remained under pressure. The worst affected currency in the region was the Malaysian Ringgit, despite the fact that the country does not have high trade exposure to China and its current account is in surplus. The currency is facing depreciation due to its reliance on the dollar funding: its foreign liabilities ($768bn) are more than seven times higher than its foreign reserves ($101bn). The second worst performing currency is the Indonesian Rupiah. The country has a moderate current account deficit but almost three times external debt ($298bn) as compared to its foreign reserves ($102bn). As long as financing conditions were favourable such mismatch could be ignored. However, a higher risk from the devaluation of the regional "anchor" currency (the Renminbi) puts that mismatch under a different light.

Currencies	Last Week % change	YTD % change
Japanese Yen	1.9%	-1.9%
Hong Kong Dollar	0.0%	0.0%
Chinese Renminbi	0.0%	-2.9%
Offshore Chinese Renminbi	-0.1%	-3.7%
Singapore Dollar	-0.1%	-5.9%
Philippine Peso	-1.1%	-4.2%
Indonesian Rupiah	-1.1%	-11.1%
South Korean Won	-1.2%	-8.7%
Indian Rupee	-1.3%	-4.2%
Thai Baht	-1.4%	-7.8%
Taiwanese Dollar	-1.5%	-3.1%
Malaysian Ringgit	-2.1%	-16.1%

Source: Bloomberg

Credit default swaps rose significantly in the recent past

Besides depreciation in currencies, sovereign CDS spreads have risen significantly for many countries in the region. Again, the worst affected countries are Malaysia and Indonesia. On the other hand, sovereign CDS for countries such as India and Philippines held relatively well due to much smaller mismatch in external assets and liabilities.

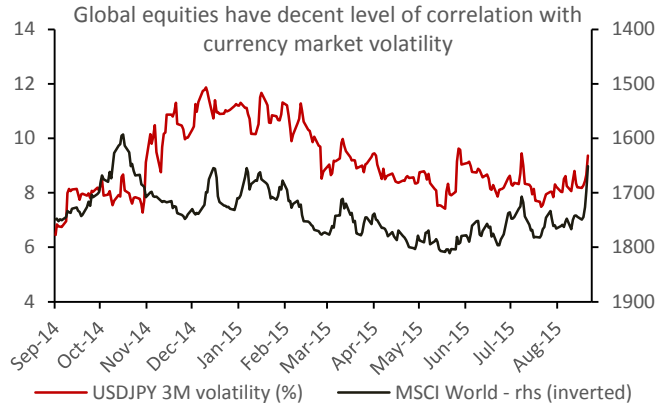
5-year sovereign CDS (in basis points)

Name	Last	1W Change	1M change
Japan	40.0	3.0	-0.5
Australia	44.5	2.5	11.8
New Zealand	44.0	4.0	12.0
South Korea	79.0	17.0	28.0
China	111.7	8.7	15.7
Malaysia	193.4	10.4	63.7
Indonesia	246.2	34.2	74.1
Thailand	163.0	25.0	58.9
India	183.9	3.5	9.9
Philippines	125.0	18.0	28.3
Vietnam	263.0	28.0	51.0
Hong Kong	48.3	0.3	0.3
Pakistan	479.0	34.5	63.6

Source: Bloomberg

Currency volatility increases equity risk

The currency depreciation has been accompanied by the correction in the regional equity markets. This is typically the case when volatility in currency markets translates into the equity volatility. A good indicator for the equity market risk is the rise in implied volatility in the Japanese yen for the currency being a carry trade currency. This is logical as investors move back to the carry currency country for risk aversion reasons. The three-month USDJPY implied volatility has spiked, suggesting heightened risk aversion.



Source: Bloomberg

Implications for interest rate and growth in the region

The currency volatility, the rise in the sovereign CDS and the pressure on the equity markets have adverse implications for the regional growth outlook. With high volatility in the currency markets and rising premiums for securing sovereign debt (CDS), regional central banks will be under pressure to either keep interest rate at current levels, or raise them despite the benign inflationary outlook (due to the sharply declining commodity prices but partly offset by the currency weakness). This will further exert downward pressure on the regional growth outlook which has already been trending lower for the last few years.

Source: IMF World Economic Outlook, April 2015

Summary market outlook

Global Yields	Global risk aversion, lower oil prices and consequent decline in the market's Fed hike expectations, pushed the US Treasury yield lower. The risk remains to the downside (yield going down) with the ongoing global risk aversion. Peripheral European sovereign yields inched up while German sovereign yields eased a bit over the week. The trend could continue in the very near term.
Stress and Risk Indicators	The VIX index closed to the highest level since Sep 2011, reflecting the high risk equity markets are pricing in. Sovereign CDS for most EMs and periphery Europe moved up. We see the spread moving further up in the near term.
Precious Metals	Gold benefitted again due to the high risk aversion in global equity markets. It could gain even further given the increased global risk perceptions. However, for the longer term, we remain cautious on the precious metal.
Local Equity Markets	GCC equity markets reacted in the obvious direction following another sharp cut in global oil prices. We remain cautious on the local equities in the near term, given the weakness in the oil price. However, the valuation has turned attractive from the medium term perspective.
Global Equity Markets	The strong global risk aversion gripped global equity markets last week due to more uncertainty on the economic outlook for China. We believe that the volatility is likely to continue in the near term while caution is required even in the medium term, given the possibility of global growth disappointments.
Energy	No let-up in the oil price decline, another week of sharp correction. Given the global risk aversion, we suggest caution on the energy prices in the near term.
Industrial Metals	Uncertainty around the Emerging Economies growth, in particular China's, continues to weigh heavily on the industrial metals.

Currencies	**Commentary**	**Critical levels**
EURUSD	A new trend in the currency market – highlighted already last week - the euro now strongly correlated with the global risk aversion got further credence last week as it shot up almost 2.5%. It has reached a point where it is difficult to imagine further appreciation, even as we believe that the risk aversion will continue in the near term.	R2 - 1.1637 R1 - 1.1511 S1 - 1.1139 S2 - 1.0892
GBPUSD	Another week of a flattish movement in the currency pair. We have been highlighting the delicate balance for the currency which will be undone only with a clear diversion between the US and the UK economic data (and thus rate expectations, we are tilted towards USD appreciation). For the moment, the flattish movement is to continue.	R2 - 1.5820 R1 - 1.5757 S1 - 1.5597 S2 - 1.5500
USDJPY	With global risk aversion intensifying, the Japanese yen (a carry currency) reversed its trend to gain last week. It could further gain but we see a limited up-move only as regional currencies tumble and the BoJ's becomes uncomfortable with a stronger currency.	R2 – 125.56 R1 – 123.80 S1 – 121.05 S2 – 120.06

Forthcoming important economic data

United States

	Indicators	Period	Expected	Prior	Comments
08/25/2015	New Home Sales	Jul	510K	482K	Second quarter growth revision is important to see if the number matches the market expectations.
08/26/2015	Durable Goods Orders	Jul	-0.4%	3.4%	
08/27/2015	GDP Annualized QoQ	2Q S	3.2%	2.3%	
08/27/2015	Personal Income	Jul	0.4%	0.4%	
08/28/2015	PCE Core YoY	Jul	1.3%	1.3%	
08/28/2015	Univ. of Mich. Sentiment	Aug F	93.1	92.9	

Japan

	Indicators	Period	Expected	Prior	Comments
08/28/2015	Jobless Rate	Jul	3.4%	3.4%	After the decline in GDP last quarter, market will look if there is any impact on the job market.
08/28/2015	Job-To-Applicant Ratio	Jul	1.19%	1.19%	
08/28/2015	CPI YoY	Jul	0.2%	0.4%	
08/28/2015	Retail Sales MoM	Jul	0.6%	-0.6%	

Euro zone

	Indicators	Period	Expected	Prior	Comments
08/25/2015	GDP SA QoQ (GE)	2Q F	0.4%	0.4%	Revised numbers for second quarter GDP from Eurozone countries will be scrutinized this week.
08/25/2015	IFO Expectations (GE)	Aug	102.0	102.4	
08/27/2015	GDP QoQ (Spain)	2Q F	1.0%	1.0%	
08/28/2015	Business Climate Indicator	Aug	0.34	0.39	
08/28/2015	Industrial Confidence	Aug	-3.2	-2.9	

China and India

	Indicators	Period	Expected	Prior	Comments
08/28/2015	Industrial Profits YoY (China)	Jul	NA	-0.3%	Not many important economic indicators are scheduled to be released this week.
08/28/2015	Leading Index (China)	Jul	NA	98.71	
08/25/2015	Infrastructure Industries growth (India)	Jul	NA	3.0%	

Sources

All information in this report has been obtained from the following sources except where indicated otherwise:

1. Bloomberg
2. Wall Street Journal
3. RTTNews
4. Reuters
5. Gulfbase
6. Zawya

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