INVESTING PROFESSIONALLY IN THE MIDDLE EAST

Monthly Outlook – July 2019

1. Global and Regional Asset Allocation

Global Asset Allocation

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Asset Class	Tactical View (3m horizon)
Equities	Global growth continues to synch downwards but is crucially holding around trend for most of the main markets including the US where there is an increasing likelihood of an “insurance rate cut” that could extend equities advance a little further from here.
Fixed Income	Renewed dovish rhetoric from the Fed and the ECB reaffirms our view that a rate cut is coming in Q3, extending the runway for bonds to continue rallying into the second half of the year, particularly EMD which should be a big beneficiary of central bank easing.
Commodities	Demand risks are building and trade tension has risen, bond markets suggest a broader economic slowdown and preliminary oil demand for April suggests further weakness. We fear this will overtake supply outages and keep the oil prices pressured until US reaches a settlement on the trade disputes with its trade partners. Our oil price forecast is $65-$70 range for Brent.

Mashreq Capital View: Positive Neutral Negative

Regional Asset Allocation

Region / Country	Fixed Income	Equities	FX
 GCC	Bond spreads are supported by the YTD jump in oil prices & the ongoing GCC EMBI inclusion theme.	Index inclusions in focus will support KSA and Kuwait equity markets.	De-pegging risk has been temporarily averted, albeit remains a risk selectively (example: Bahrain and Oman).
 North Africa	Short-dated bonds provide value for carry positions while we see varying degrees of improving economies.	Earnings growth is positive and the market is cheap, also will benefit from the recovery in the EM.	EGP to remain in a band.
 Turkey	We expect a slow, volatile recovery as there is little scope for monetary easing given still-high inflation and a lira likely to remain vulnerable to bouts of geopolitical risk aversion.	Main beneficiary from the recovery in EM and also the monetary easing in the US.	We expect continued volatility with the lira in 2H2019.

Mashreq Capital View: Positive Neutral Negative

2. Global Portfolios

Global Assets – Monthly Commentary

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Overview

DM Equities (+6.6%)

Global equities rebounded following an easing of trade tensions between the US & Mexico at the beginning of the month & then a conciliatory G20 meeting between the US & China at month-end.

EM Equities (+6.2%)

Three of the four BRICs—Brazil, Russia & China—posted plus 4% returns with India being the only laggard as investors took profit following a strong showing post Modi's re-election win in May.

DM Fixed Income (+2.2%)

US & European treasuries rallied amid increasing expectations of central bank policy easing from the Fed to the ECB as exemplified by German 10-year yields finishing the month at negative 33 bps.

EM Fixed Income (+3.4%)

Renewed dovish rhetoric from central banks in combination with an easing trade tensions provided a perfect mix for EMD to post strong returns.

\+ Positive Returns / – Negative Returns

Outlook

Global growth continues to synch downwards but crucially remains around trend for the main market of the US where a still-strong economy leads us to maintain our cautiously constructive stance on risk assets.

Chinese policy stimulus combined with the Fed's dovish turn provides a strong tailwind for EMs, though headwinds remain in the form of still-unresolved trade tensions.

The Fed is getting closer to a pre-emptive cut following its removal of the word "patient" from its latest statement, reaffirming our view that a rate cut is coming in Q3, extending the bond rally further.

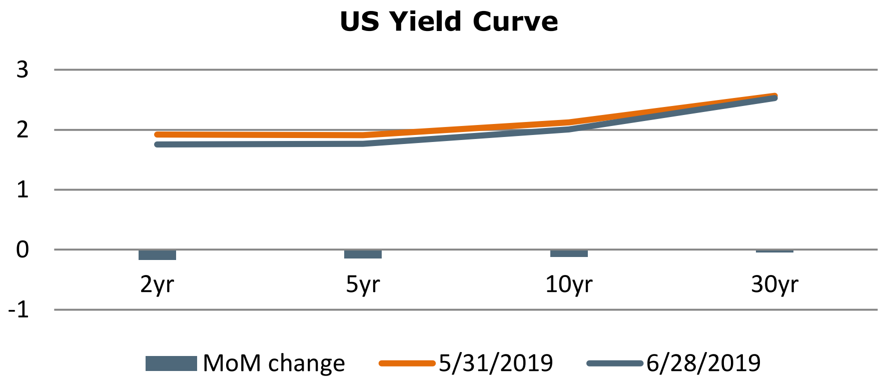
The current market-friendly mix of slowing growth, benign inflation & accommodative central banks continues to provide a supportive backdrop for EM fixed income.

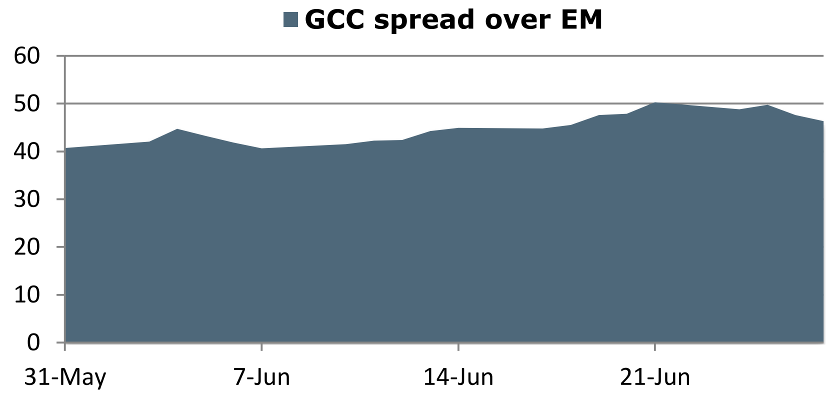
Positive Neutral Negative

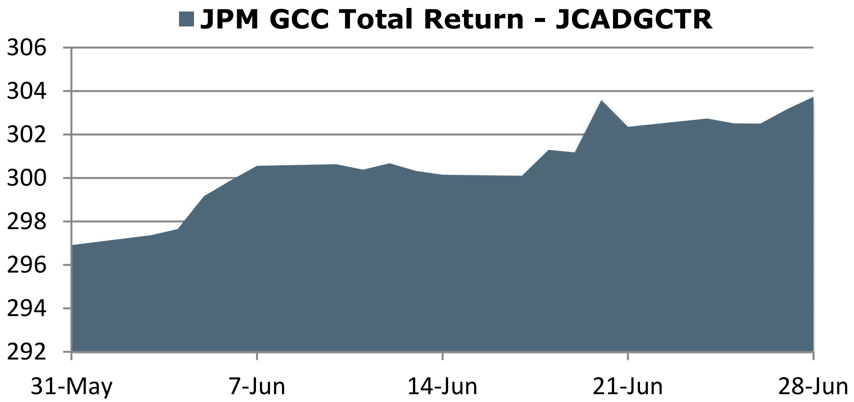
Source Morningstar: DM Equities = MSCI World Index; EM Equities = MSCI Emerging Markets Index; DM Fixed Income = Bloomberg Global Aggregate Index; EM Fixed Income = JP Morgan Emerging Market Bond Index. Overview figures are monthly, unhedged US dollar returns. Outlook forecasts are based on a 3-6 month timeframe.

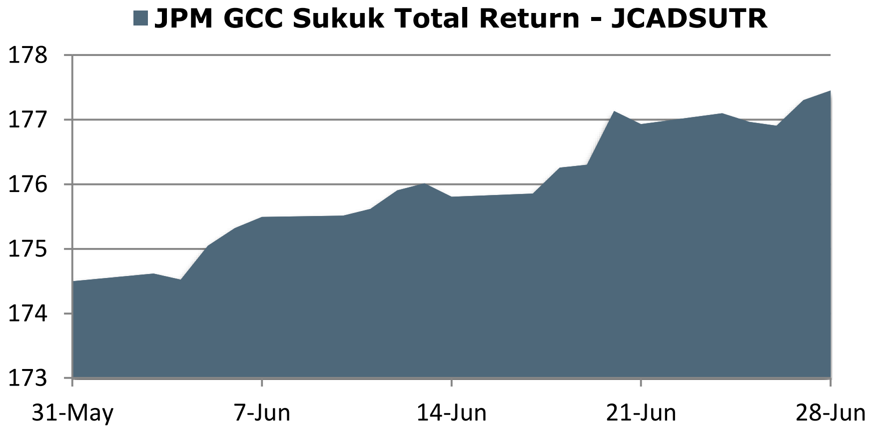
3. MENA Fixed Income

MENA Fixed Income - Markets









Sources: Mashreq Capital, Bloomberg

EM Fixed Income – Monthly Commentary

Overview

EMD rebounded in June with the global EM bond index up 3.4% followed closely by the Middle East bond index at 3.0%.

Central banks loosened policy further in June continuing the YTD trend. India for example cut rates for the third time this year, and changed its monetary policy stance to accommodative. Russia was another big EM constituent to cut in June citing slower growth and weaker inflation. Turkey was a noteworthy outlier keeping rates unchanged at a lofty 24% due to still-elevated inflation.

Geopolitical risk took a temporary reprieve as the US reneged on imposing tariffs on Mexico and agreed to resume trade talks with China amidst an apparent truce at the G20 summit at month-end.

Ratings action resulted in Turkey's long-term debt rating being downgraded from Ba3 to B1 by Moody's. Elsewhere, Mexico's sovereign debt and state-owned company Pemex were both downgraded one notch by Fitch. The downgrade pushed Pemex into high yield, whilst the sovereign still hovers just above junk at BBB.

New sovereign issuance came from Sri Lanka, Indonesia, Russia and Peru issuing its first dollar bond since 2015.

Oil finished the month slightly higher at $66 which is also the average price level during the first half of 2019. This is above consensus estimates going into the year and is reducing the fiscal pressure of GCC oil exporters.

Outlook

EM bonds continue to be one of the biggest beneficiaries of DM central bank policy easing. Investors are flocking to EMD given the increasing number of negative-yielding sovereigns from Germany to Japan as a result of renewed dovish rhetoric from the Fed to the ECB.

In June, Jerome Powell stated that the Fed "will act as appropriate to sustain the expansion" and the word "patience" was dropped from the Fed's official statement. This strengthens our view that a rate cut is coming in Q3, which we had already forecasted in our prior month's outlook.

Despite decent economic data in the US, the growth trend is still downward with Q2 GDP forecast to print around trend at 2%. Downward-trending growth in addition to still-benign inflation affords the Fed breathing room to justify a cut in the coming weeks.

The ECB ratcheted-up its own dovish rhetoric in June with Draghi giving strong indications that a renewed round of rate cuts and asset purchases is on the cards.

The Fed and ECB's dovish turn has allowed EM central banks breathing room to tailor monetary policy to domestic economies.

We envisage further rate cuts by EM central banks in the second half of 2019 due to contained inflation expectations complemented by robust growth outlooks.

4. MENA Equities

MENA Equity View

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Sector	GCC	North Africa	Turkey
Banks	Positive	Positive	Negative
Consumer Goods	Negative	Neutral	Negative
Real Estate	Negative	Negative	Neutral
Telecommunications	Neutral	Neutral	Neutral
Materials	Positive	Negative	Positive
Utilities	Neutral	Positive	Neutral

Mashreq Capital View: Positive Neutral Negative

MENA Equities – Monthly Commentary

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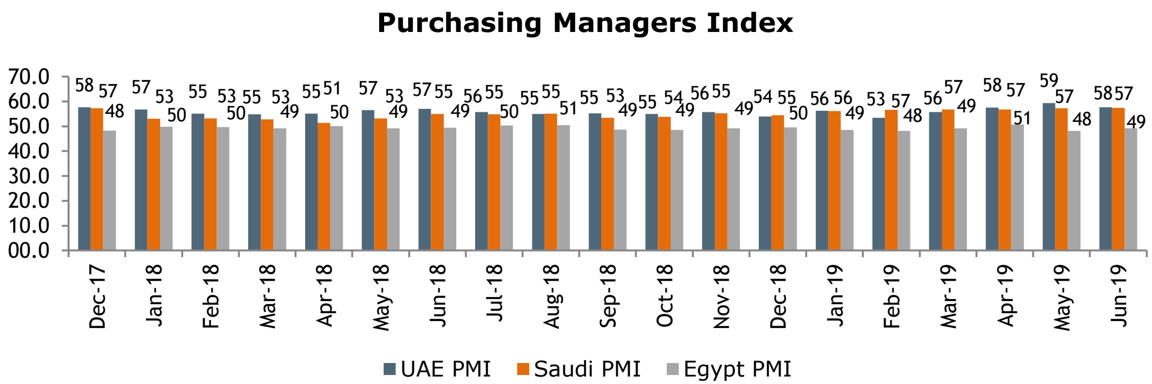
Overview

- MENA rose in June finishing up 2.5% notwithstanding growing concerns over global growth and geopolitics. Saudi and Kuwait were the best performers on anticipation of large foreign inflows. Oil prices also gained by 3.2% on expectation of OPEC+ output cut extension and rising geopolitical tension. MENA markets are up 10.1% for the year outperforming Emerging markets, which are up 9.2% YTD.
- In Saudi, the market jumped by 3.6% led by large-caps, mainly banking and petrochemicals but also select names that are likely to be introduced in MSCI/ FTSE's index. The market is up 12.7% YTD.
- Egyptian shares (Hermes Stock Market Index) were up 2.0% for the month (up 2.6% in USD terms) on anticipation of the tax dispute settlement. The market is up 5.4% YTD.
- Qatar rallied up 1.8% for the month on the back of implementation of stock split in Qatari stocks which provided some lift in investor sentiments. The market has moved into positive territory up 1.5% YTD.
- The UAE finished down 0.8% which was led by Industrials on the US/China trade war escalation coupled with weak sentiment in real estate sector. The UAE overall index is up 0.1% YTD.
- In Kuwait, the market continues to gain and finished June up 2.2% in anticipation of MSCI index inclusion. The market is up 21.1% YTD.

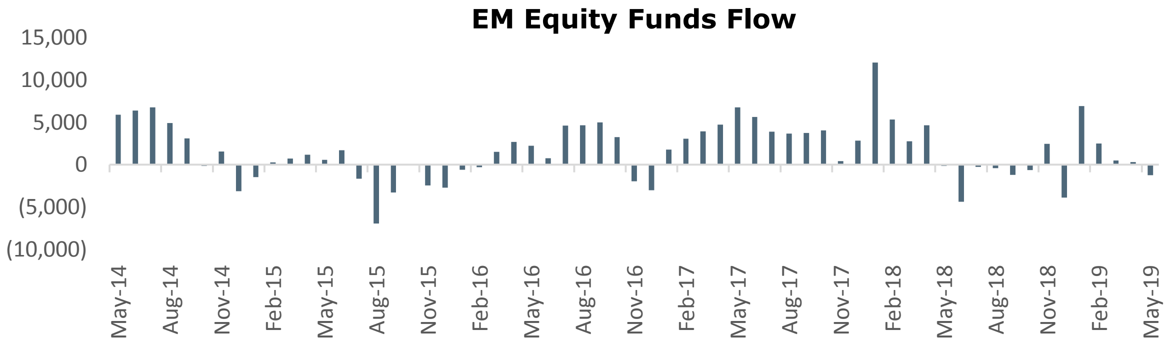
Outlook

- In Saudi, the next 2 to 3 month outlook looks good as a result of the positive MSCI decision. The market experienced large foreign outflows in October, which we believe will slowly make its way back to the market.
- In Egypt, inflation data is expected to ease despite additional utility and fuel subsidy cuts due to high base effects and a stable currency. The CBE should further cut interest rates (expect 100bps) in 2019 after a surprise rate cut of 100bps in February 2019 and help sustain the rally.
- Qatar does not have any catalysts or major risks on the horizon. In terms of valuation, the market is in line with its 5 year average P/E at 14.8x TTM – as a result we see limited upside in this market.
- While the UAE lacks any catalysts, there are select names that are in value territory. Similar to GCC markets, the market is a safe-haven with elevated oil prices.
- With Kuwait being added to MSCI EM's watch list, the market is likely to remain buoyant.
- Global markets are expected to remain positive in short term post positive development on US-China trade talks as the US announced that they will not impose new tariffs on Chinese imports.

MENA Equities

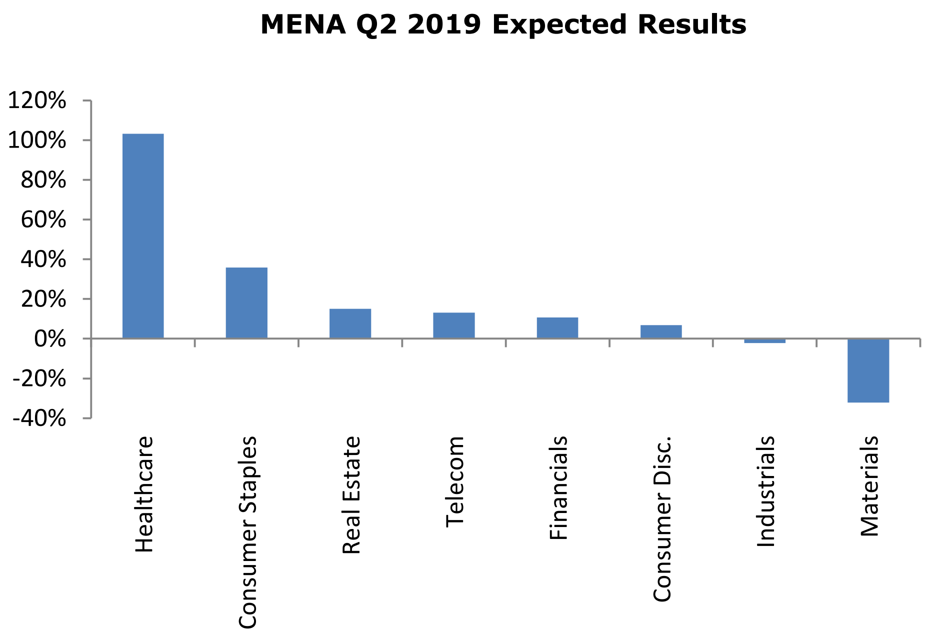


UAE PMIs decreased MoM in June after posting recent highs of 59.4 in May on the back of weaker new orders. Egypt's and Saudi PMI on the other hand remained stable.



May saw a net outflow of USD1.2bn in Emerging Market Equity Funds, vs. net inflows of USD0.3bn in April.

MENA Equities – Chart of the Month



Aggregate MENA earnings are expected to remain stable YoY in Q2 2019. On a sector level, Healthcare is expected to have the highest growth driven by KSA on new capacities coming online followed by Consumer Staples. Materials is expected to have the lowest growth of -32% with weakness coming mainly from KSA and Egypt on weak prices.

Sources: Mashreq Capital, Bloomberg

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