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CAPITAL

INVESTING PROFESSIONALLY IN THE MIDDLE EAST

Monthly Outlook – November 2019

1. Global and Regional Asset Allocation

Global Asset Allocation

Asset Class	Tactical View (3m horizon)
Equities	Global cyclical slowdown driven by the protectionism stance undertaken by developed economies coupled with overbought market conditions drives our cautious tactical stance on equities. The positives witnessed encompass trend-like growth, positive surprises in corporate earnings and a coordinated central bank dovish stance which could help offset the headwinds.
Fixed Income	Sluggish economic data, unending political drama in the UK and a technical recession looming over the European economy will continue to drive investor sentiment in the markets. While world central banks are relaxing their monetary policy stance to resuscitate global growth, the risk-off mode driven by flight to safety is expected to drive down global yields.
Commodities	Slowdown in global growth backed by the trade pressures, expanding US shale oil production and the persistent geopolitical tensions are expected to apply pressure on oil prices. However, we think oil should stay within the $60-$70 range due to the supply control measures undertaken by the OPEC+. Gold is expected to continue to be a preferred asset on the back of its safe haven status and the diversification benefits derived amid a decreasing interest rate environment.

Mashreq Capital View: Positive Neutral Negative

Regional Asset Allocation

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Region / Country	Fixed Income	Equities	FX
 **GCC**	→ GCC Bonds are currently trading at fair valuations relative to similar EM rated peers. Longer duration IG continues to be in focus	↓ The Saudi story has come to an end. The UAE and Kuwait are our top markets.	→ De-pegging risk has been temporarily averted, albeit remains a risk selectively (for example, Bahrain and Oman).
 **North Africa**	→ Long-dated sovereign bonds provide value for carry positions while we witness fundamentally improving economies.	↑ Earnings growth is positive and the market is cheap. Also, it should benefit from the rate cuts.	→ EGP to remain in a band.
 **Turkey**	↓ Policy stimulus measures and improving data provide support for the sovereign in the short term, although sanctions and policy risks remain a key challenge.	↑ It could be the main beneficiary from 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 (+2.5%)

"Phase One" mini trade deal between the US and China along with positive surprise revisions in key economic data led to a risk-on market sentiment driving the returns in the equity markets.

EM Equities (+4.2%)

EM stock markets soared due to supportive fiscal and monetary stimulus measures. The enormous return was mainly driven by major markets like India, Russia and Brazil.

DM Fixed Income (+0.7%)

Treasuries whipsawed during the month with major sovereign bonds ending relatively flat amid diminishing trade war conditions added by reducing uncertainty on the Brexit negotiations.

EM Fixed Income (+0.4%)

EM bonds rallied during the month supported by widespread central bank dovishness and lower global yields although their rally was anchored due to the geopolitical and economic tensions in Lebanon, Argentina and Venezuela.

+ Positive Returns / – Negative Returns

Outlook

Global growth continues to face headwinds from a downturn in the economic cycle aided by recurrent trade frictions. Muted inflation trends and stable core economic data should continue to drive the economic policy. Expensive valuations and pressure on corporate profitability leads to our neutral stance.

Dovish EM central banks and fiscal policy stimulus in varying degrees witnessed in EM economies are appealing attributes for EMs, although the ongoing trade war uncertainty, soft data releases and the slowing EM growth momentum leads us to maintain our cautious view on the asset class.

Safe havens should be sought after amid a combination of continuing trade uncertainty, consistent weak macro Euro data, Brexit related ambiguity added by the fact that the global pool of perceived safe assets are limited. Central banks are expected to continue to try to boost the benign growth witnessed in the core economic data.

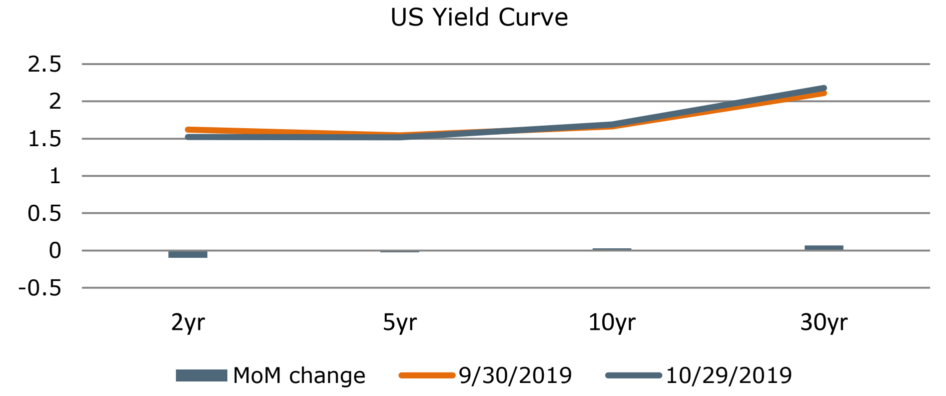
Despite the volatility historically witnessed in EM fixed income, the asset class should be supported by central banks maintaining their easing cycles on the back of weakness in manufacturing data which has hurt EM exporters in particular in addition to the compressing global growth outlook.

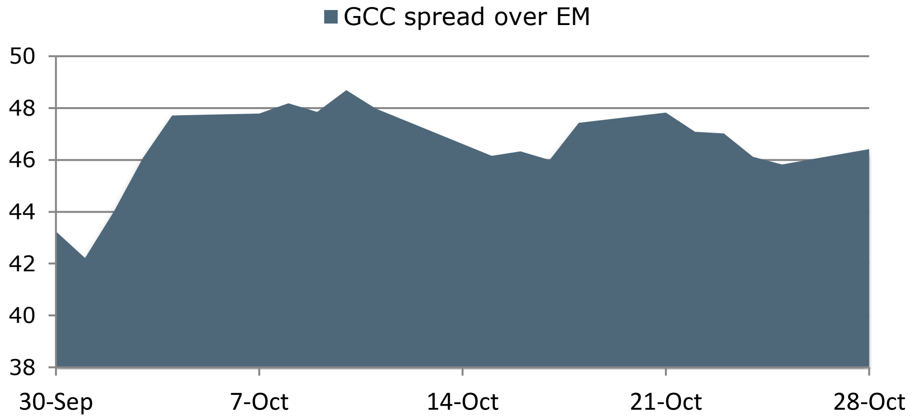
Positive Neutral Negative

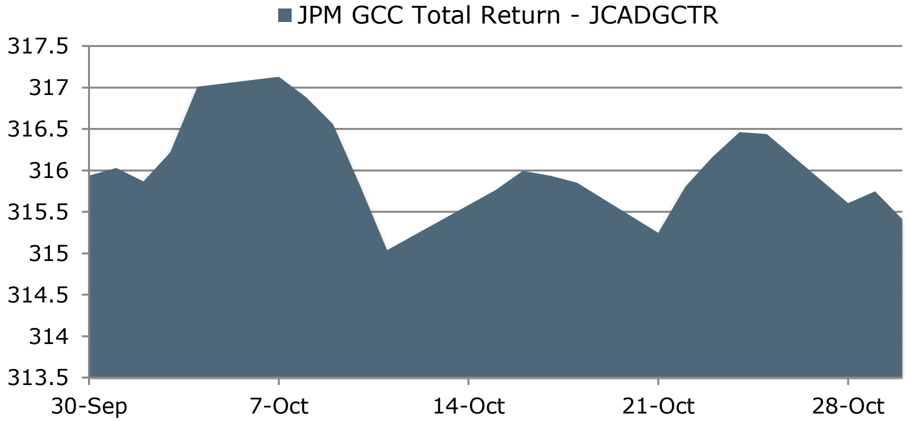
Source Morningstar: DM Equities = MSCI World Index; EM Equities = MSCI Emerging Markets Index; DM Fixed Income = Bloomberg Global Aggregate Index; EM Fixed Income = JP Morgan Emerging Market Bond Index. Overview figures are monthly, unhedged US dollar returns. Outlook forecasts are based on a 3-6 month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

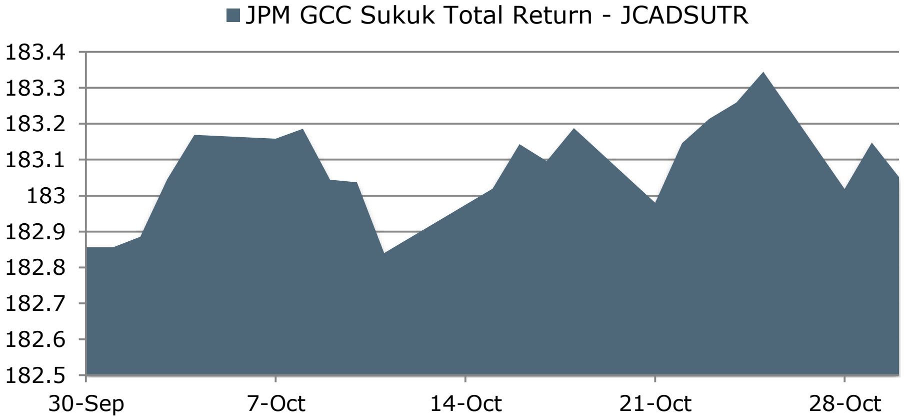
3. MENA Fixed Income

MENA Fixed Income - Markets









Sources: Mashreq Capital, Bloomberg

Overview

EMD resumed its positive performance in October with the global EMBI up by 0.37%. The global benchmark's return was much better compared to the Middle East Index's loss of 0.6% which faced downward price pressure due to the geopolitical situation and unrest in Lebanon.

Global consumption spending accelerated, boosting service sector activity, which offset persistent weakness in manufacturing. However, it appears that the global economy has entered a second and more dangerous phase of slowing.

President Trump and China reached the phase one of their trade deal which was perceived by the market as a major positive catalyst driving the risk-on mode across the asset class. The uncertainty related to trade talks has been a major sentiment drag on EM markets and is expected to continue to drive investor opinions.

Widespread easing of monetary policy by EM central banks following the path laid by the Fed was observed to combat the continued soft growth environment eroding the real rate offered by EM economies. Within DMs and EMs, 65% of countries have cut policy rates this year, the highest proportion since 2009.

Saudi Arabia, Indonesia, Mamoura (Mubadala) and Perusahaan Listrik Negara (PLN) tapped the global bond markets in the last two weeks of October. The pace of supply decelerated compared to September, even the skew has been all IG compared with the HY tilt last month.

Oil remained volatile despite supportive geopolitical headlines which suggested an informal offer was extended to Brazil to join OPEC, raising prospects of deeper output cuts next year. Worries over the trade deal and mixed macro data kept crude on the back foot though a large build in US crude inventories acted as a catalyst for weaker prices.

Outlook

EM bonds should continue to be one of the biggest beneficiaries of DM central bank policy easing stance, although the broadening of the softness in DM activity data and business cycle implications is expected to weigh on the emerging market economies. In a few major economies, including India, Brazil, Mexico, Russia, and South Africa, growth in 2019 is sharply lower for idiosyncratic reasons, but this is expected to improve in 2020.

Headlines on US impeachment risk, Brexit and geopolitical developments in the Middle East are expected to constrain investor risk appetite.

Between now and the 2020 US elections, to gain a victory President Trump will have to use all the tools available in his pocket to avoid a recessionary environment and to boost the lethargy in the global manufacturing scenario. His main controllable tool is the trade policy as fiscal and monetary easing will not be sufficient to undo the damage already enforced on the global economy. We see these as primary reasons for Trump to strive for a trade deal with China.

For the next few months, markets may struggle with what appears to be the end of a reasonably broad and deep global easing cycle after the October-end Fed meeting which signaled a pause causing reduced easing expectations unless global financial conditions materially worsen.

With the tailwind of EMBI inclusion now behind us (the phase-in was completed in September), main risks include waning technicals and softer fundamentals, with oil prices in sub-USD 60/bbl territory. Heavy GCC sovereign issuance this year (USD 39.3bn, up 12% versus full-year 2018), with potentially more issuance ahead, is expected to lead to some supply fatigue.

Favorite overweight's remain GCC ex-Oman, China, India, Brazil, Mexico, Russia, Egypt and Ukraine, while key underweights are Turkey, Argentina and Lebanon.

4. MENA Equities

MENA Equity View

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

- **GCC Banks:** Falling interest rates to negatively impact profitability hence we downgrade to negative from neutral.
- **GCC Consumer Goods:** The decline in Saudi consumer spending has reached its bottom and a decline in expat exodus should help turnaround hence upgrade to neutral.
- **Real Estate:** Falling interest rates will positively benefit interest rates hence we upgrade to neutral from negative.
- **Telecommunications:** High leveraged sector should positively benefit from interest rate cuts leading us to upgrade to positive from neutral.
- **Materials:** Negatively impacted from weaker demand due to US-China trade war hence we downgrade to negative from neutral.
- **Utilities:** Resilient to global volatility due to its defensive business nature resulting positively hence we upgrade to positive from neutral.

Mashreq Capital View: Positive Neutral Negative

MENA Equities – Monthly Commentary

Overview

MENA markets continued their struggle in October. Markets were down by 2.4% and this was mainly led by Saudi Arabia. Oil prices also declined by 0.9% over global growth concerns and MENA markets are up 0.8% for the year, underperforming emerging markets, which are up 7.9% YTD.

In Saudi Arabia, the market declined by 4.3% on the back of the potential Aramco IPO weighing on the liquidity, dragging down banking and petchem stocks by c.5% at a sector level coupled with lackluster 3Q19 earnings. The market is down 1.1% YTD.

Egyptian shares (Hermes Stock Market Index) traded up by 2.3% (3.2% in USD terms) on the back of falling inflation, leading to anticipation of another rate cut and more friendly government policy (reduction of natural gas price … etc.) which boosted the investor sentiment. The market is up 4.9% YTD.

The Qatari market finished down 1.7% as the market lacks any catalyst coupled with uneventful earnings season. The market is down by 1.1% YTD.

The UAE finished up slightly 0.2%, as Dubai’s real estate names led by Emaar Properties weighed on the performance, while performance across banking sector remained resilient on the back of stronger 3Q19 earnings. The UAE overall index is up 0.2% YTD.

In Kuwait, the market returned to positive and is up 0.6% for the month as the investors focused on the upcoming MSCI EM upgrade announcement. The market is up 17.9% YTD.

Outlook

In Saudi Arabia, we expect the weakness to continue after the final phase of inclusion in the MSCI EM index was made effective and valuations look expensive which could weigh on the performance.

In Egypt, inflation has reached single digits despite additional utility and fuel subsidy cuts, due to high base effects and a stable currency. The CBE after cutting 350bps interest rates in YTD 2019, we expect further 50-100bps cut for the remainder of 2019 which should help sustain the rally.

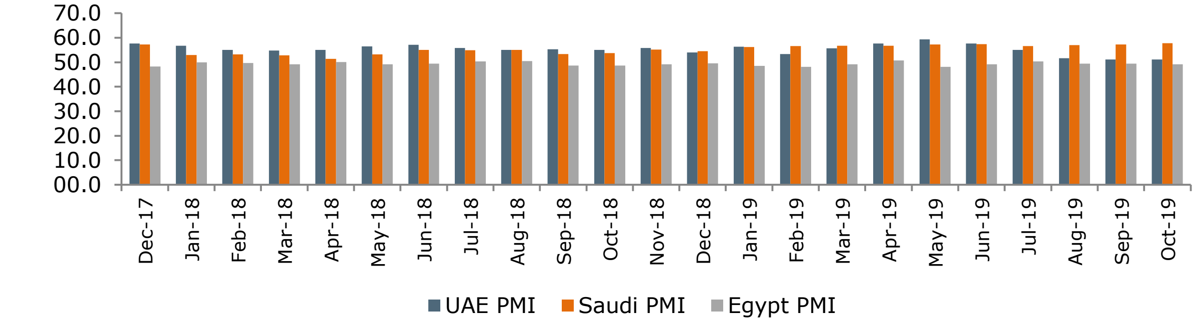
Qatar does not have any catalysts or major risks on the horizon. In terms of valuation, the market is in line with its 5 year average P/E at 14.5x TTM – as a result we see limited upside in this market.

We expect the UAE market to trade positive on the back of FOL increase expectation and some relief in the real estate sector post incremental interest shown by Chinese investors in UAE market.

With Kuwait being added to MSCI EM’s watch list, the market is likely to remain buoyant.

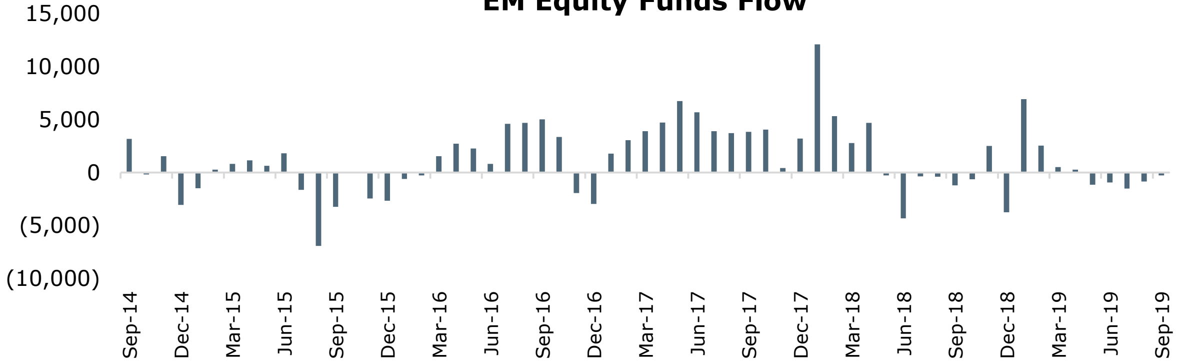
Main risks are still centered around high geopolitical tension in the MENA region and also the correlation with global equities which we think should correct further as the global GDP growth is softening with no catalyst in the near future to improve the sentiments or productivity.

Purchasing Managers Index



Saudi Arabia's PMIs increased to 57.8 on the back of strong orders while UAE PMIs remained flat at 51.1. Egypt's PMIs fell to 49.2 in October on the back of weaker new orders.

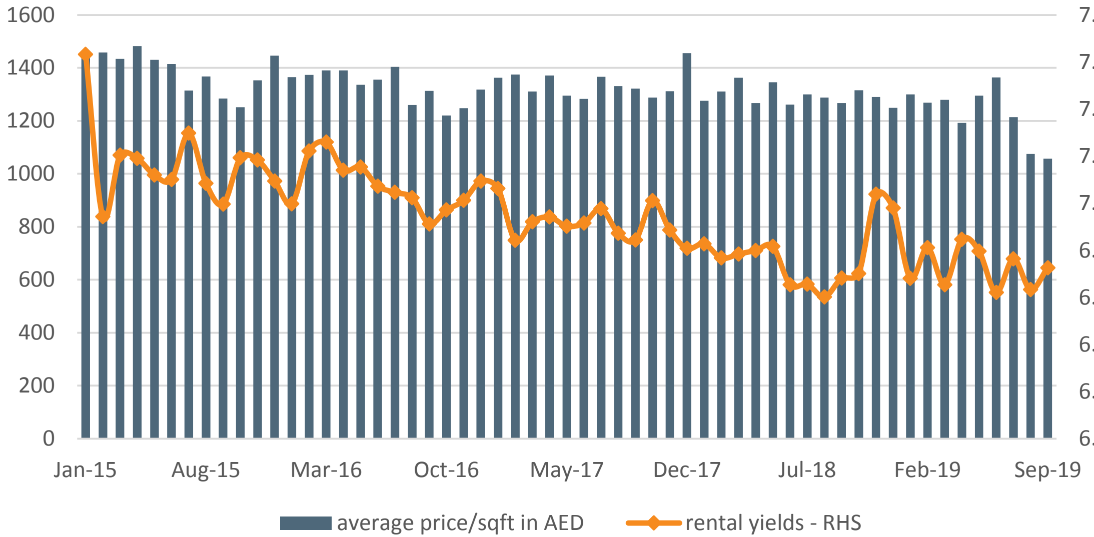
EM Equity Funds Flow



September saw a net outflow of USD0.3bn vs. net outflows of USD0.9bn in August, in Emerging Market Equity Funds.

MENA Equities – Chart of the Month

Dubai Property Prices vs. Rental Yields



Selling prices continue to slide in Dubai; rental market under renewed pressure. Overall property prices in Dubai have reduced by c.30% since 2015 while rental yields reaching 6.7% (c.30 bps below its 10Y average of 7.0%).

Sources: Mashreq Capital, REIDIN

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