EXCLUSIV

Principal

In alliance with CIMB

البنك الأهلي المتحد
ahli united bank

Multi-Asset perspectives

Courtesy of Principal Global Investors

Compliments of AUB, please enjoy this multi-asset perspective courtesy of:

Principal

Ahli United Bank (AUB) Private Banking selected Principal Islamic Asset Management (Principal) to support client investment needs. A joint venture between Principal Financial Group, a FORTUNE 500® and Nasdaq-listed global financial services company with more than 140 years of experience and expertise in investment, retirement and insurance solutions; and CIMB Group Holdings Berhad, one of Southeast Asia's leading universal banking groups, Principal Islamic is a leading Islamic investment management company offering Shariah-compliant unit trust, discretionary mandates and asset management solutions to individuals and businesses across the world. During the initial phase of the planned collaboration, Principal will provide their core research, investment outlook, market updates, and overall asset allocation advice along with Shariah-compliant portfolio management capabilities.

March 2021

Market Summary

Macro

- **Global COVID cases** rose to 129 million by end-Mar'2021. The 7-day average of new cases jumped to 586k which was 197k higher than the number at the end of Feb'2021. Countries/regions with prominent increases were smaller countries (102k), India (44k and rising rapidly) and Euro-Area (38k of which France along contributed 26k). Mexico, UK, Indonesia, and Malaysia saw new cases decline. Our Global Stringency Index that uses Oxford data, improved to 60 from 69 (100=highest stringency) on increased Reopenings in US, China, UK, Germany, and Malaysia. India went the other way as new cases spiked up. Global vaccinations gathered pace, with 350m new doses administered in Mar'2021 vs. 145m in Feb'2021. The total vaccination count reached 630m (03 April 2021).
- **Economic recovery stayed on track.** US fiscal spending is pushing growth estimates higher. Global manufacturing outlook remains strong. Our global Manufacturing PMI index reached an all-time high. Base effects helped global industrial output to grow 8.5% in Jan'2021 (had contracted -3% in Jan'2020). Global Macro-economic surprises were positive for an eleventh successive month and corporate earnings estimates ticked up further. Global Financial conditions were easy and stable despite higher treasury yields.
- **Global inflation** ticked up to 1.24%yoy (3m average) in Feb'2021, with Feb'2021 reading (1.43%) higher than Jan'2021 (1.24%). Our leading indicator continues to project higher inflation, much like inflation break-evens.
- **Lower volatility** in equities pushed our cross-asset implied volatility indicator to below its long-term average.

Bottom-up

- MSCI AC World's **expected EPS growth** for 2021 was stable at 27%yoy. Earnings revisions remained positive.
- The ratio of **global credit rating upgrades to total changes** edged up to 49% (19% end-2021). Bankruptcy filings in the US declined further.

Valuations

- **Equities stayed expensive on earnings-based measures.** A few markets were cheap on P/B. Very low nominal and real rates, strong growth and continued policy support can sustain richness for some more time.
- **IG and HY** spreads remained expensive.
- **US 10-yr treasuries:** Both of our models i.e. our time-trend model and our macro model peg US treasuries at fair value after the upward movement in yields this year.

Markets

- **Multi-Assets:** Our global multi-asset index returned 0.3% in Mar'2021 to peg YTD'2021 return at 0.60% (last 12-month returns were 31% due to COVID-base effects). Equities were the only positive contributor during the month.
- **Equities** finished with strong returns. 31/40 markets finished in the green with a median local currency return of 3.5%, which took median YTD'2021 return to 6.2% with 32 markets in the green. Return patterns indicate a cyclical bias, with Value outperforming Growth handsomely.
- **Fixed income:** While policy rates edged up marginally, sovereign yields continued their climb (PGAA's Global Sovereign 10-yr yield indicator was ↑18bps to 2.54%, its highest since June'2019). Markets continued to price higher growth/inflation against a supportive monetary backdrop. Credit spreads tightened modestly. Bond returns favored 'Up-in-Yield, low-in-Duration" exposures. US treasuries had their worst quarter since 1981.
- **Currencies:** US$ finished stronger against both DMs and EMs in a month where FX markets traded divergence in growth and rates, both of which supported the US$. It gained against 23 of the 30 currencies we track it against. For 1Q'2021, the US$ gained against 27 currencies, including a home-run against EMs.
- **Commodities:** The GS commodity index (-2%) recorded its first drop in 5 months though 1Q'2021 return was strong at 14%, powered by Energy (21%) while precious metals disappointed (-9%). Speculative open interest in commodities came off highs, with open interest easing to $720bn by end Mar'2021 from a peak of $782bn. Net length dropped ~15% to $115bn.

Outlook

1. **Growth – an updated outlook**

   The global economy continues its recovery from the COVID-19 related shock, aided by extremely supportive monetary and fiscal policies, and rising vaccinations that raise the prospects of a meaningful economic reopening by 3Q'2021. American households are sitting on record savings, which creates a solid base for continued expansion. The Jan'2021 savings rate of 20.5% will rise as stimulus checks hit accounts and provides a strong base for increased consumption spend over the next several quarters. Our Economic Committee has upgraded its US economic outlook quite significantly, riding these factors. The bazooka US stimulus will continue to drive US demand for domestic and global goods, and unlock demand for services, as vaccine deployment picks up speed. Outside the US, Emerging Markets like Chinese (8-9%) and Indian (10%) recoveries have exceeded expectations, boosting the outlook for global growth. Our average year-on-year real GDP growth forecast for US stands revised to 6.0% for 2021 (previously 4.8%) and 4.8% for 2022 (previously 2.9%). However, there exist several risks that could slow the recovery.

Exhibit LA1: US consumers in pole position

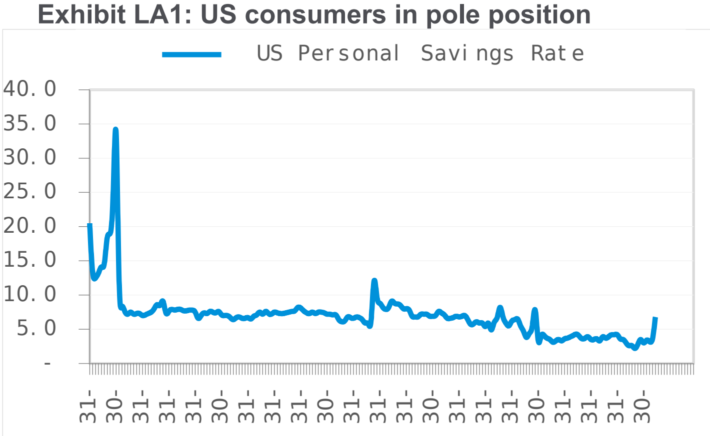
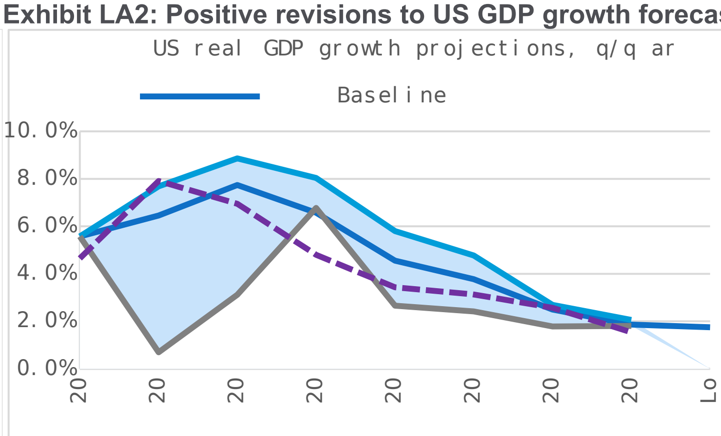


Exhibit LA2: Positive revisions to US GDP growth forecast



Source: Bloomberg/Factset/Principal Global Asset Allocation, PGI Economic Committee.

2. **Inflation**

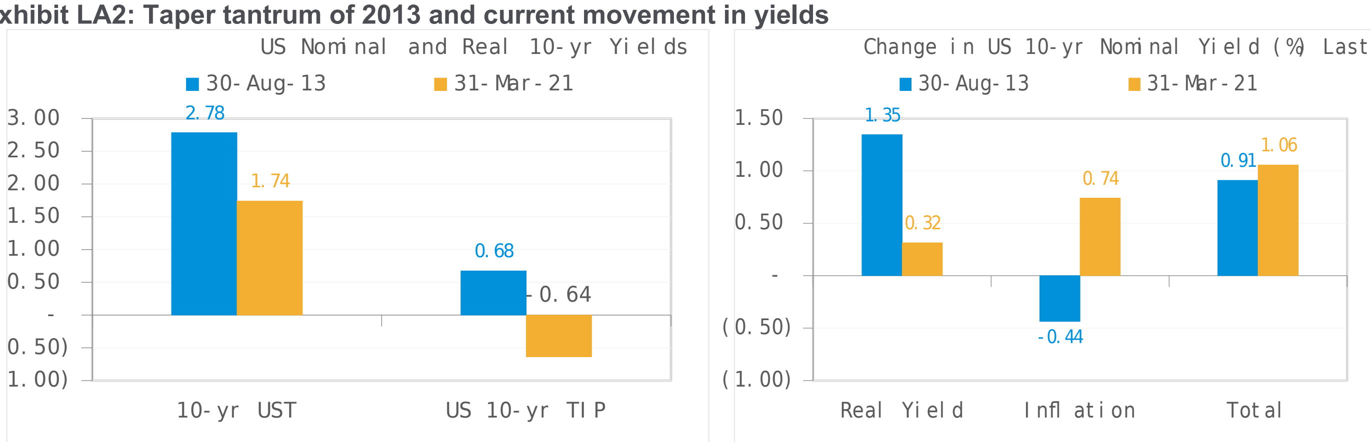
   Our Leading Indicator continues to predict higher headline inflation in 2021, powered by higher commodity prices. At this stage, it is unlikely to be sufficient to push core inflation sustainably above policymaker goals, forcing them into a hawkish policy U-turn. 10-yr CPI Swaps are already pricing consumer inflation @ 2.5% in US, 1.5% in Germany, 3.7% in UK and 2.3% in Australia, which leaves little room for further upside, unless markets start pricing a structural shift in inflation dynamics, powered by a persistently loose monetary-fiscal setting and significant supply-side constraints (tight labor markets, restrictions on movement of labor and shortage of raw materials like semi-conductors and other critical components). At this stage, while we assign a small probability for such a scenario to play out, we are mindful of the risks it could present, were it to play out. For EMs, while higher oil and food prices remain a headwind as their inflation baskets are biased towards food and energy, the current levels of realized inflation (EM CPI was 1.9% in Feb'2021) leave cushion to absorb higher prices before policy settings turn hawkish.

3. **Monetary policy & global financial conditions**

   This remains the most talked about topic. Global monetary policy remains extremely easy but the future path has become a little more uncertain, influenced by the visible growth divergence between US and other DM economies. The talk is increasingly about rate hikes, not cuts in US and several EMs in response to recovering growth and inflation. Steeper curves too imply rising probability of rate hikes. Market pricing shows US$ libor reaching 50bps by end 2022 and 121bps by 2023 as opposed to Fed's forward guidance of no rate hikes through 2023. 1-month US treasuries (a good proxy of Fed funds rate) are expected to breach the long-run Fed funds rate of 2.5% in 2026. The US treasury curve shows the 10-yr forward 10-yr yield at 3.02%, which implies a real yield of 1% assuming Fed's long-term inflation target of 2%. On the other side, ECB and BoJ will remain dovish for a prolonged period, given the much longer distance they must travel to get to inflation goals. We also expect G4 Central Bank balance sheets to rise by $4.1 trillion to US$ 28 trillion (63% of their GDP) in 2021.

   A natural question that comes to the fore is if the current rise in yields can push us **towards the taper-tantrum type market reaction of 2013**. We think the conditions today are different as shown in Exhibit LA2. Both nominal and real US yields are much lower today than in 2013. Back then, the real US yield had jumped 135bps into restrictive territory, while inflation expectation had dropped -44bps, but this time around, the rise in real yield is modest, with recovering inflation expectations explaining 70% of the rise in nominal yield. Also, EMs are better prepared this around, with stronger external accounts, higher FX reserves, and a positive gap of around 240bps between EM and US real yields versus almost 0% back in 2013.

Exhibit LA2: Taper tantrum of 2013 and current movement in yields



Source: Bloomberg/Factset/Principal Global Asset Allocation

4. **Valuations**
   - **Anti-fragile assets** like global safe-haven US treasuries and gold are getting into a fair value zone. Ex-US DM treasuries remain expensive, particularly in Europe.
   - **Equity** valuations remain rich. While valuations should start normalizing as the recovery matures and as interest rates normalize further, equities should still deliver positive returns. Valuation normalization could be delayed if growth continues to surprise on the upside.
   - **Corporate spreads** are in an expensive zone, though less so than equities. With most spreads close to cycle lows, room for them to compress further is minimal.
   - In **Currencies,** the US$ is on the expensive side. Growth and monetary policy divergence raise the bar for the US$ to weaken in the near term.

5. **Sentiments & technical indicators**

   Equity inflows suggest animal spirits are back. Retail participation in markets is high, and risk positioning remains extended.

6. **Summarizing our thoughts on risk assets:**

   We retain a pro-risk stance in our asset allocation framework, even as we recognize the compressed risk premiums. Our checklist of various factors stacks up as under-

   a. **Return-to-Work strategies:** Rising vaccinations is a huge positive though new cases are resurging in some countries. Reopenings are rising too. Overall, this factor stays **"positive".**

b. **Growth:** Both macro and bottom-up growth environments continue to improve. Buffer with savers and more US stimulus make us keep this factor as **"positive".**
c. **Monetary policy** – Central banks may be forced to tighten policy at the margin. Financial conditions, though remain very easy, causing us to keep this factor as **"positive".**
d. **Fiscal policy** – Possibility of additional US fiscal stimulus before the end of the year provides upside risk to growth. Overall, we rate this factor as **"extremely positive"** in the near term. The medium-term outlook remains **"positive"** but could be clouded by higher taxes down the road.
e. **Valuations –** Low risk premiums worry us, but the lack of meaningful returns from risk-free alternatives should keep investors interested in equities and corporate risk assets as long as the forward-looking growth outlook is strong. While we understand that valuation factors don't necessarily play out in the short-term, we are cognizant of their medium-term risks, which causes us to keep this factor at **"negative".**
f. **Technical factors:** Technical indicators are stretched which makes us keep this factor as **"negative"** in the near term.

7. **Key risks**

The key risks to our pro-risk allocation stance are-

- A delayed reopening of the global economy caused by vaccine disappointments (either because people don't take it or because it isn't successful in restraining mutated strains of the virus). Countries like India are experiencing a new virus wave which could delay their growth recoveries.
- Too much of a good thing i.e. short-term growth/inflation boost is misconstrued as structural, forcing central banks to adopt restrictive monetary policies, particularly in the US.
- China's policy stance changes from supportive to restrictive, and they end up restraining large cap technology companies too much in pursuit of broader socialistic goals.
- The US technology sector faces headwinds as regulators try to reign in large-cap technology companies.
- Higher corporate taxes as OECD progresses in plugging loopholes in the global tax system including a global digital tax.
- US-China relationship takes a turn for the worse.
- European elections could throw a curve ball as Scotland (May), Germany (Sep) and France (2022) head to polls.

Binay Chandgothia
Managing Director – Portfolio Manager, Principal Global Investors (Hong Kong) Ltd.

The piece was written with contributions from Han Peng, Raj Singh and Scott Payseur

Risk considerations

Investing involves risk, including possible loss of principal. Past Performance does not guarantee future return. All financial investments involve an element of risk. Therefore, the value of the investment and the income from it will vary and the initial investment amount cannot be guaranteed.

Important information

This material covers general information only and does not take account of any investor's investment objectives or financial situation and should not be construed as specific investment advice, a recommendation, or be relied on in any way as a guarantee, promise, forecast or prediction of future events regarding an investment or the markets in general. The opinions and predictions expressed are subject to change without prior notice. The information presented has been derived from sources believed to be accurate; however, we do not independently verify or guarantee its accuracy or validity. Any reference to a specific investment or security does not constitute a recommendation to buy, sell, or hold such investment or security, nor an indication that the investment manager or its affiliates has recommended a specific security for any client account. Subject to any contrary provisions of applicable law, the investment manager and its affiliates, and their officers, directors, employees, agents, disclaim any express or implied warranty of reliability or accuracy and any responsibility arising in any way (including by reason of negligence) for errors or omissions in the information or data provided.

This material may contain 'forward-looking' information that is not purely historical in nature and may include, among other things, projections and forecasts. There is no guarantee that any forecasts made will come to pass. Reliance upon information in this material is at the sole discretion of the reader.

Proprietary model output is based upon certain assumptions that may change, are not guaranteed and should not be relied upon as a significant basis for an investment decision. Forecasts for each asset class can be conditional on economic scenarios; in the event a scenario comes to pass, actual returns could be significantly higher or lower than forecasted. Because of the inherent limitations of all models, potential investors should not rely exclusively on the model when making an investment decision. Forecasts of financial market trends that are based on current market conditions constitute our judgment and are subject to change without notice.

Indices are unmanaged and do not consider fees, expenses and transaction costs are not available for direct investment. The information provided here is neither tax nor legal advice. Investors should speak to their tax professional for specific information regarding their tax situation.

This document has been prepared for professional use and is not intended for distribution to or use by any person or entity in any jurisdiction or country where such distribution or use would be contrary to local law or regulation.

Principal℠

MM10579-24 | 04/2021 | 1590523 – 042022

Ahli United Bank B.S.C.

Bahrain: Certain of the information discussed herein has been obtained from sources that Ahli United Bank B.S.C. deems to be reliable but Ahli United Bank B.S.C. makes no representations about the accuracy, completeness or timeliness of any information prepared by a third party and assumes no liability for the reliance thereon. The opinions and predictions expressed in the materials are subject to change without prior notice and has not been prepared by or with the involvement of Ahli United Bank B.S.C.; however, Ahli United Bank B.S.C. does not independently verify or guarantee its accuracy or validity and any reference to a specific investment or security does not constitute a recommendation to buy, sell, or hold such investment or security, nor an indication that Ahli United Bank B.S.C. or its affiliates has recommended a specific security for any client account. Subject to any contrary provisions of applicable law, Ahli United Bank B.S.C. and its affiliates, and their officers, directors, employees, agents, disclaim any express or implied warranty of reliability or accuracy and any responsibility arising in any way (including by reason of negligence) for errors or omissions in the information or data provided. IMPORTANT – If you are in any doubt about the contents of this document you should seek independent professional advice. AUB will not act and has not acted as your legal, tax, regulatory accounting or investment advisor or owe any fiduciary duties to you in connection with this, and/or any related transaction and no reliance may be placed on AUB for investment advice or recommendations and/or solicitation of any sort. Remember that all investments carry varying levels of risk and that the value of your investment may go up or down depending on market movements. Investment Products are not considered Deposits and therefore not covered by the Kingdom of Bahrain's Deposit Protection Scheme. Investors should ensure they understand the risks of investing and read the terms and conditions carefully. If the investor has a complaint about the Bank or any part of the service offered he may in the first instance make a complaint to the Relationship Manager and if he or she fails to resolve the matter then it should be referred to the Customer Complaints Officer contactable at the Bank on +973 17 58 6113 or write to the Customer Complaints Officer, or refer to a simple and easy-to-use guide on customer complaints procedures available at Ahli United Bank B.S.C., Building 2495, Road 2832, Al-Seef District 428, PO Box 2424, Manama, Kingdom of Bahrain /www.ahliunited.com/bh.

Egypt: Certain of the information discussed herein has been obtained from sources that Ahli United Bank (Egypt) S.A.E. deems to be reliable but Ahli United Bank (Egypt) S.A.E. makes no representations about or guarantee the accuracy, completeness or timeliness of any information prepared by a third party and assumes no liability for the reliance thereon. The opinions and predictions expressed in the materials are of general nature – not specific to your investments – and are subject to change without prior notice and has not been prepared by or with the involvement of Ahli United Bank (Egypt) S.A.E.; however, Ahli United Bank (Egypt) S.A.E. does not independently verify or guarantee its accuracy or validity and any reference to a specific investment or security does not constitute a recommendation to buy, sell, or hold such investment or security, nor an indication that Ahli United Bank (Egypt) S.A.E. or its affiliates has recommended a specific security for any client account. Ahli United Bank (Egypt) S.A.E. strongly recommends that you seek, subject to any contrary provisions of applicable law, Ahli United Bank (Egypt) S.A.E. and its affiliates, and their officers, directors, employees, agents, disclaim any express or implied warranty of reliability or accuracy and any responsibility arising in any way (including by reason of negligence) for errors or omissions in the information or data provided. IMPORTANT – Ahli United Bank (Egypt) S.A.E. urges you to seek independent professional advice when considering any investment decision. Ahli United Bank (Egypt) S.A.E. will not act and has not acted as your legal, tax, regulatory accounting or investment advisor or owe any fiduciary duties to you in connection with this, and/or any related transaction and no reliance may be placed on Ahli United Bank (Egypt) S.A.E. for investment advice or recommendations and/or solicitation of any sort. Remember that all investments carry varying levels of risk and that the value of your investment may go up or down depending on market movements. Investors should ensure they understand the risks of investing and read the terms and conditions carefully. If the investor has a complaint about the Bank or any part of the service offered, he/she can contact our Hotline on 19072 or send an email message to the following address "EGYPTCustomer.Protectionrights@ahliunited.com" or fill out the online complaint form through "CONTACT US" link on the bank website https://www.ahliunited.com/eg/. Complaint boxes are also available in all AUBE Branch network.