

Monthly Newsletter

May 4th, 2021

"Societies in decline have no use for visionaries." — Anaïs Nin

"The greatest lesson in life is to know that even fools are right sometimes" — Winston Churchill

Clues from Recent Asset Classes' Behavior

Macro: China Decelerating, US Peaking and Europe Gaining Momentum

Oil: Potential Recovery in H2

MENA: Are We Seeing a Bottom in the UAE Real Estate Market?

Introduction

An overabundance of negative headlines regarding the resurgence of the Covid-19 virus and its variants around the world, notably in emerging countries with fresh lockdowns in India, did not derail the spring of hope from a surge in vaccinations globally, which is boosting optimism among consumers, improving mobility trends and prompting equity market rallies especially in the US and Europe.

Beyond improving health conditions in key systemic regions in the world such as the US and Europe, improving soft and hard macro data in terms of unemployment, spending and confidence indices show that the global rebound from depressed levels last year is taking shape. The earnings season has been generous which was illustrated with the excess beats recorded. From a big picture perspective, policies remain supportive in general, central banks are still following an easing mode, the US is framing its extra stimulus packages while Europe is putting its recovery fund into action. All in all, macro and earnings outlooks in addition to policy stance appear to be on surface supportive to markets and are encouraging a positive direction.

The strong fundamental backdrop would keep us comfortable albeit cautious in buying the dip in the market despite potential corrections. We think that looking beneath the surface, few factors that would warrant some prudence and dictate a change in style and imply certain sectorial and geographical rotations are worth noting.

Looking into growth, China is decelerating on the back of a peaking credit impulse, less supportive fiscal stimulus and PMIs losing momentum. The US is in the process of reaching a peak in the summer supported by reopening and stimulus packages, while the recovery in Europe is gathering pace boosted by vaccinations and reassuring monetary/fiscal policies.

Digging deeper, it appears that policies in China and the US are no longer fully accommodating. China refrained from adding extra liquidity but more importantly it is seeking to curb excessive credit and tighten regulations over giant tech companies. In the US, the government is pursuing tax hikes on individuals and corporates to fund its social and infrastructure programs. Some regulatory tightening may follow while the stance of the foreign policy in China, Russia and Middle East is yet to get shape.

Looking into markets, it was noticeable that a sell-off took place after each earnings beat, this may mean that markets are fully priced and incapable to respond to the good data which may lead to corrections or consolidations. Market participants may be worried about the pace of growth and margin sustainability. The recent Q1 GDP data revealed that the supply relied on inventory drawdown to keep pace with the extra demand. In addition, management teams were expressing concerns regarding rising input costs. The retreat in sovereign yields may indicate that pension funds were chasing lucrative returns, but investors are also raising the bar for growth expectations. Trading volume has been on a downward trend recently which means that the momentum is fading slowly. No one can have an accurate timing but usually as the momentum fades, retail investors start to get out of the market, depriving it of the necessary support that buoyed the market in previous months.

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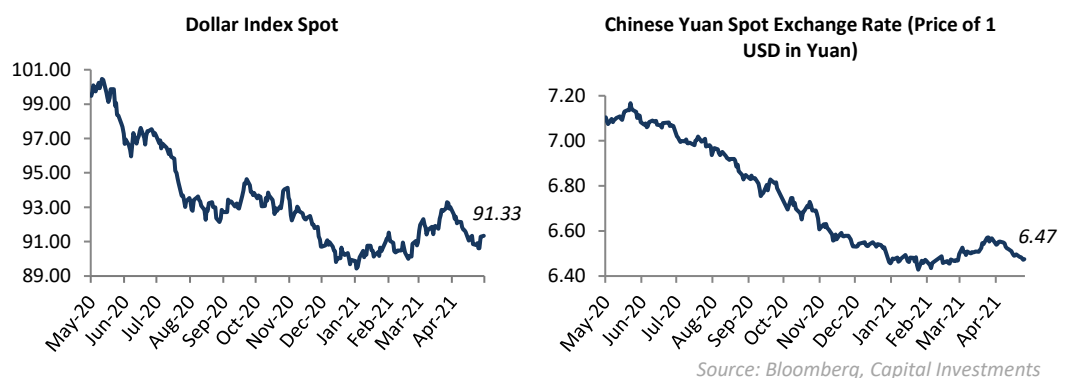
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The direction in real yields is a major unknown currently and is usually impacted by growth and inflation outlooks and monetary policy. The initial sharp rebound in economic activity from the depressed levels of the Covid-19 crisis pushed real yields higher which in turn impacted nominal yields. Currently, the situation is blurry. Amid peak growth expectations, there are sustained long-term inflation pressures that are filtering through the system gradually due to rising commodity prices and wages, as companies in the US are deliberately raising their minimum wage to \$15 per hour and the government has ordered government agencies to adopt the same minimum wage in public contracts starting next year. In addition, supply side reform in China (curbing steel exports and decarbonization) are inflationary in nature. The direction in real yields would affect cross asset class behavior with an expectation of consolidation over the near term.

The Fed has been so far providing yield curve control actions in disguise through keeping the pace of its asset purchase program at USD 120bn per annum. The market expects the Fed will start preparing investors for a potential tapering in the summer of 2021.

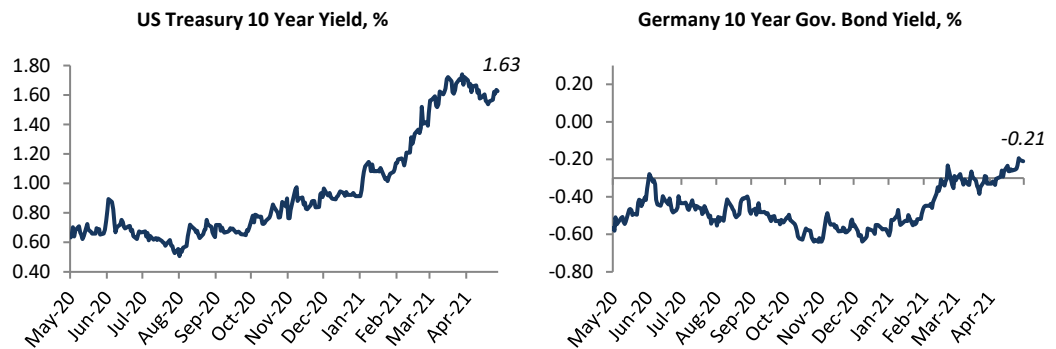
We remain positioned to benefit from reopening plays including companies related to the consumer discretionary sphere. In addition, we continue to like opportunities in energy on the back of a bullish outlook on oil. Gold and silver miners are still core to our allocation. We still have a focus on Europe, but we are selectively looking into emerging markets after the recent drop in key markets.

Clues from Recent Asset Classes' Behavior



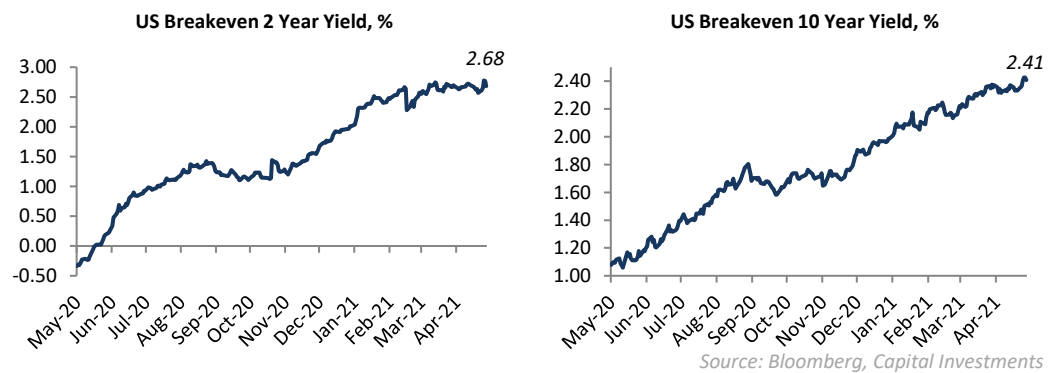
The greenback lost steam along with the retreat in long term yields in the US. The USD is expected to continue its weak trend despite any uptick for several reasons; vaccination rates in Europe are

accelerating and thus the economic recovery in the Old Continent is shaping up, and long term German yields are picking up and narrowing the differential with their counterparts in the US which would support the Euro. The Chinese Yuan is still exhibiting strength supported by a widening trade surplus and suppressed outbound tourism. We are closely watching secondary reserve currencies such as the Canadian and Australian dollar which may appreciate further vis a vis the greenback.



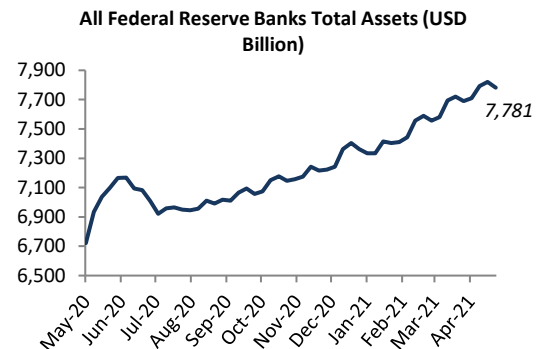
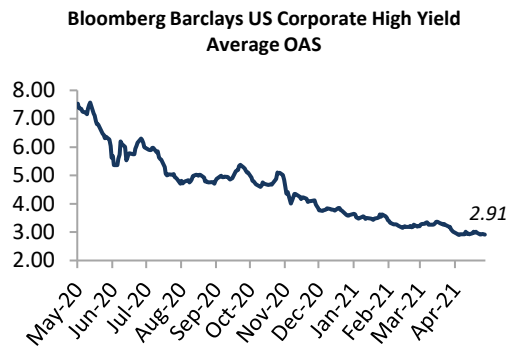
Source: Bloomberg, Capital Investments

Germany's 10-year yield is grinding higher backed by optimism regarding reopening and an improved inflation outlook in the Old Continent while the US 10-year yield is consolidating after retreating from the peak registered in March. Should the US growth peak in the summer and the Fed keep up the pace of its asset purchase program, the 10-year yield seems to be capped around 1.8%.



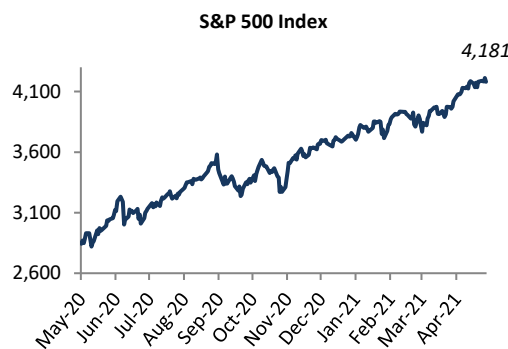
Source: Bloomberg, Capital Investments

The 2-year breakeven yield in the US is showing signs of consolidation since the beginning of the year which indicates that inflationary expectations are contained for the medium term. However, if long term breakeven rates climb higher relative to short term rates, that may indicate that we might have some structural inflationary pressure in the system that will reveal itself over the long run and would favour inflation-sensitive investments such as commodities, gold and cyclicals.



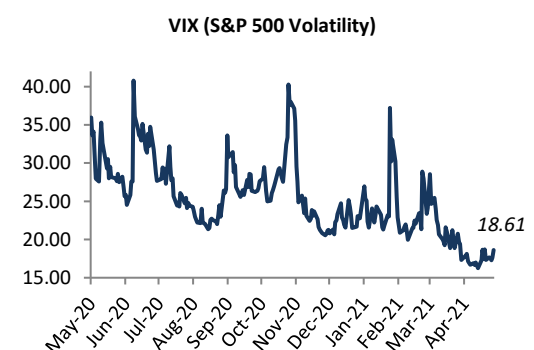
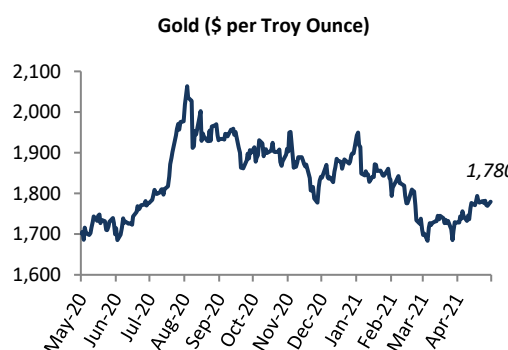
Source: Bloomberg, Capital Investments

Credit spreads are very tight which leaves little room to chase return. Meanwhile, the expansion of the Fed's balance sheet is keeping the financial conditions ultra-loose and explains the yield-chasing mentality that is governing the market.



Source: Bloomberg, Capital Investments

It is remarkable that emerging market indices were not moving in sync with those in advanced economies over the past few months, therefore offering cheaper entry points especially when growth rotates back to the former once vaccinations, reopening and mobility gain more track.



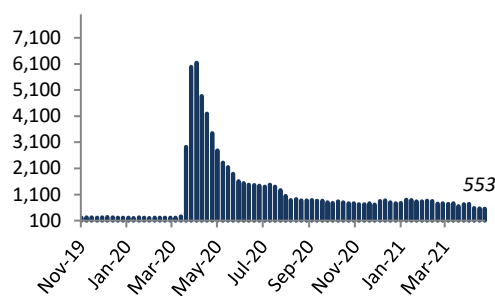
Source: Bloomberg, Capital Investments

The improvement in vaccination rollouts across the board despite the difficult situation in India managed to compress the VIX index, which is a gauge of fear, below the 20-threshold. We are constructive on equities but expect a necessary and healthy correction to rebalance and rotate as strong fundamentals support buying the dip theme. Moving to gold, we think that the price has

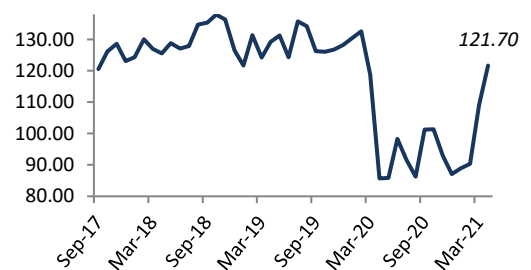
bottomed, and we are constructive on it along with silver, with the next catalyst to come from real yields, a weaker USD, and a revival in jewelry retail demand. Both gold and silver miners represent an attractive opportunity, while we will reposition in industrial metals, notably copper and aluminum, on weakness via appropriate proxies.

Macro: China Decelerating, US Peaking and Europe Gaining Momentum

US Initial Jobless Claims (Thousands)



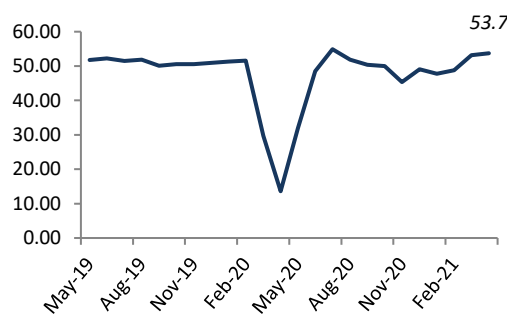
US Conference Board Consumer Confidence Index



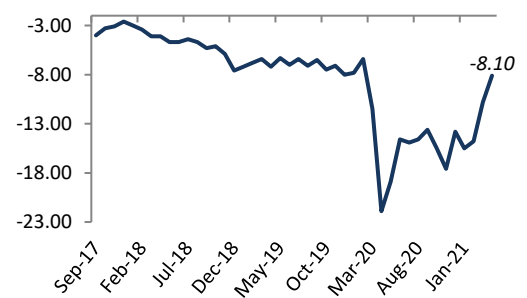
Source: Bloomberg, Capital Investments

US jobless claims are trending lower which means that the economy is on the right track to gain back the jobs lost during the pandemic, while the consumer confidence index managed to restore its pre-pandemic levels. After recording a 6.4% jump in Q1 GDP on a quarterly basis, it is expected for the momentum to continue into the summer supported by stimulus and reopening, before drifting back towards its long-term growth trend in 2022.

Markit Eurozone Composite PMI SA

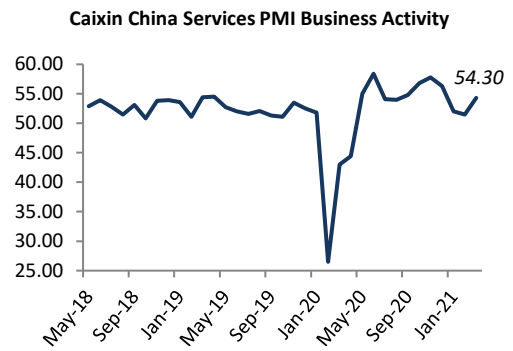


Eurozone Consumer Confidence Indicator



Source: Bloomberg, Capital Investments

Growth is rotating towards Europe, which is benefiting from increasing vaccination rates, easing of lockdown measures, and encouraging mobility indicators. The economic activity is boosted by supportive monetary and fiscal policies. Improved macro backdrops and climbing yields will favor banks, energy companies, and laggard reopening plays in Europe.



Source: Bloomberg, Capital Investments

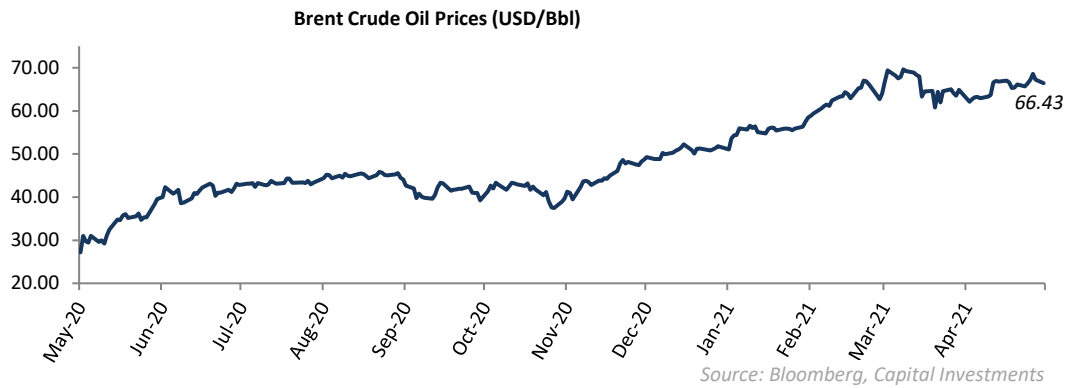
The relatively early economic rebound that China has enjoyed last year is losing steam amid policy tightening as the central bank is refraining from adding liquidity. This, along with a withdrawal of fiscal support, means that China is calibrating its growth trajectory to avoid excesses. We are still constructive on China and on Asia selectively and we see the retreat in equities as a window to start nibbling opportunities.

Box 1: China's Key Strategic Initiatives

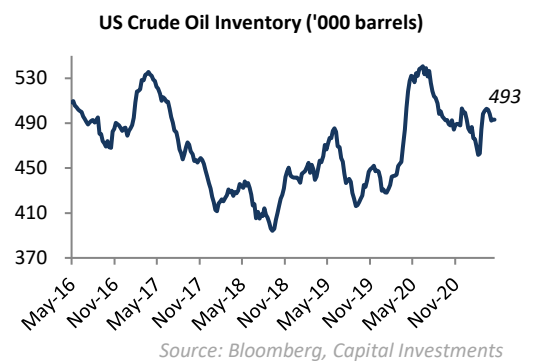
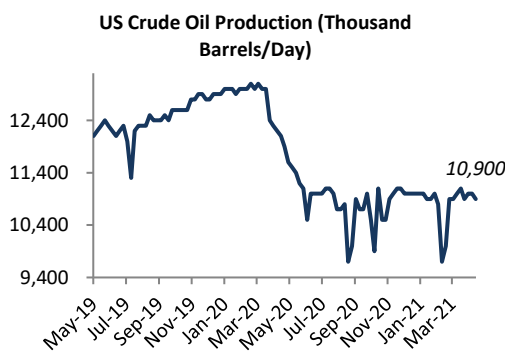
Sector	China's Key Strategic Initiatives
5G	<ul style="list-style-type: none"> • Upgrade and modification of existing infrastructures including engine rooms, power supply systems, towers, and cables. • Development of base stations, core networks, transmission systems and other basic networks for the 5G system. • Establishment of cloud-based 5G new business application platforms to promote collaboration among new service businesses and vertical integration of various industries. • Building an advanced business environment for the manufacturing industry with 5G-based industrial internet.
Artificial Intelligence (AI)	<ul style="list-style-type: none"> • Development of fundamental hardware such as AI chips. • Development of general platforms for intelligent computing. • Establishment of research and development centers for intelligent perception processing and intelligent interaction. • Development of artificial intelligence innovation development test zones.
Internet of Things (IoT)	<p>The Chinese Communist Party (CCP) is transforming the IoT into one of the most potent strategic weapons of the contemporary world — into a form of self-fueling power projection, self-enforcing international rule-setting, and silent, secured global conquest.</p> <ul style="list-style-type: none"> • The concept is bold and simple- China seeks a world-wide, integrated system of information collection and dissemination. Universal sensors gather data, China-penetrated or owned networks carry it, and Beijing-controlled hubs aggregate, analyze, and store it. The overall goal is to “predict, develop, and control” the world. • If China succeeds in its effort, it will be able to hold military, diplomatic, and economic transactions hostage. It will decide the media that global information networks disseminate. Beijing will set standards that reward domestic champions over foreign competitors. It will shape personal, commercial, and government incentives to serve its interests.
Environment (Climate Change)	<p>Green development will strive towards the goal of carbon neutrality. China's 14th Five Year Plan (FYP) reiterated the goal of striving towards carbon neutrality by 2060, and as a midpoint goal, aims to reach peak carbon emissions by 2030.</p> <p>Goals:</p> <ul style="list-style-type: none"> • 18% reduction in CO2 emissions per unit of GDP. • Non-fossil fuels to account for 20% of total energy consumption by 2025. • Better utilization of resources such as focusing on water conservation, reduction of waste and pollutants, as well as improvement in the recycling system are measures which will support the green development. • The application of ‘green’ development to various industries will also be a continued theme for China's long-term growth.
Central Bank Digital Currency (CBDC)	<p>A Central Bank Digital Currency (CBDC) uses an electronic record or digital token to represent the virtual form of a fiat currency of a particular nation (or region). A CBDC is centralized; it is issued and regulated by the competent monetary authority of the country.</p> <ul style="list-style-type: none"> • China started developing its Digital Currency Electronic Payment (DCEP) CBDC in 2014 and tested a pilot in 2020. • RMB 314 trillion in mobile payment volume Jan-Sept 2020, up >135x from FY2012. • Mobile payment penetration: 87% in December 2020 vs. 25% in December 2013. • Over \$300 million in DCEP transactions in the pilot program.

Source: HSBC, Citi, Goldman Sachs, Bloombera, The New Silk Roads, Capital Investments

Oil: Potential Recovery in H2

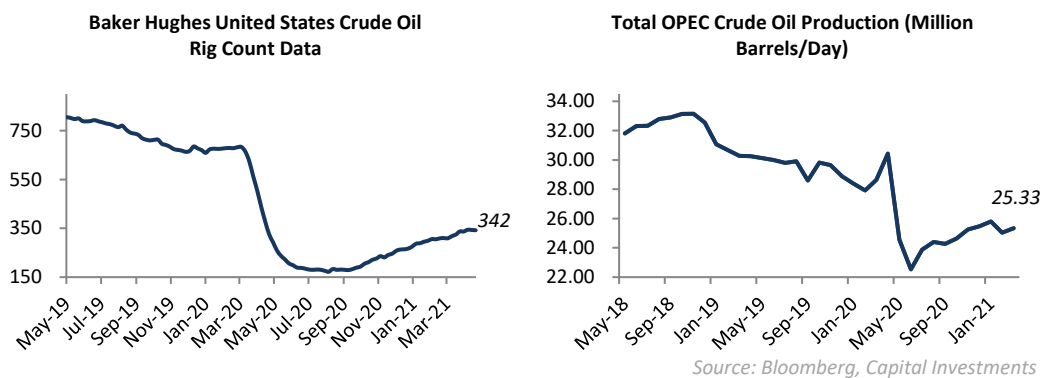


Oil prices swung between gains and losses throughout the month of April as the market assessed an uneven demand outlook amid rising covid-19 cases in some regions, namely India, and as the market braced for an increase in supply by OPEC+ this month. Prices were also torn between mixed inventory data and improved demand outlook by the major oil agencies in the market on the back of accelerating vaccine rollouts and improving economic data in certain regions. However, prices were able to break upwards at the end of April as signs of demand recovering in key markets such as the US and China offset concerns the resurgence in India will dampen consumption in the near-term.



As mentioned, the three major oil agencies – IEA, EIA and OPEC- all increased their demand estimates for 2021, on the back of rapid vaccine rollouts and an improving economic outlook, particularly in the US and China. The three agencies raised their demand forecasts for the year by 150,000 to 200,000 b/d from those they published in March. However, the expected demand recovery is skewed to the second half of this year as the outlook for the immediate future is not so bright. OPEC and the EIA both cut their demand forecasts for the current quarter.

Indeed, pockets of demand recovery have emerged in the US and China. In the US, for instance, the number of miles driven on interstates rose versus the same period in 2019 for the first time since the pandemic began. Meanwhile, Chinese traffic and factory activity has surpassed pre-virus levels, and the country’s strong appetite for crude continued throughout the month of March. The IEA has also stated that the unprecedented oil inventory glut that amassed during the coronavirus pandemic is almost gone, another sign of stronger demand. However, demand in India is exhibiting signs of weakness as a deadly second wave led to renewed lockdowns. Indian fuel and gasoline sales have declined, refineries have cut processing rates, and it is expected that this outbreak will hit oil demand by 550K b/d in May.



OPEC+ has confirmed that it would proceed with plans to add more barrels to the market in May, despite the resurgence of the virus. The group reiterated its confidence in the prospects for global consumption in 2021, but cautioned that the resurgence in India, Brazil and Japan could derail the recovery. OPEC oil output rose in April as higher supply from Iran offset the involuntary cuts and agreed-upon reductions by the group. OPEC pumped 25.17 million b/d in April, up 100,000 b/d from March. Meanwhile, Libyan oil output dropped below 1 million barrels per day for the first time in months as a major port was shut down due to a lack of funds for infrastructure repairs.

The US cut its oil output outlook through next year as OPEC and its allies start to reverse production cuts in the coming months. According to US government statistics, oil production in the United States is expected to reach 11.04 million barrels per day this year, down from last month's estimate of 11.15 million barrels per day following a deep freeze in February that shut down the oil industry in Texas. The EIA also lowered its output forecast for 2022 by 100,00 b/d. However, also an indication that the global economy is heating up again, the Permian Basin, the United States' most abundant shale patch, will produce crude oil at levels not seen since the start of the pandemic. According to the latest data from the EIA, production in the basin will reach 4.466 million barrels per day in May, the highest level in a year, and rig counts have reached a one-year high. In addition,

crude inventories rose by 90,000 barrels in the week ended April 23 versus an analyst forecast of 659,000 barrels.

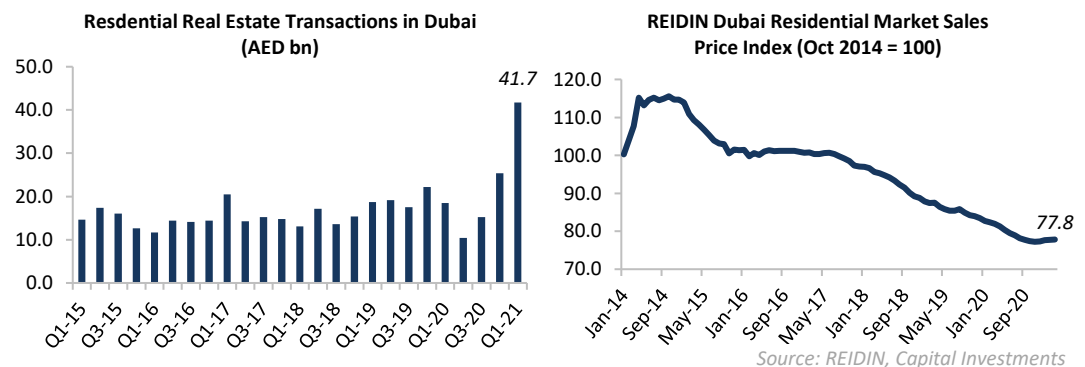
Even as signs of improved energy demand elsewhere continue to pile up, the resurgence of Covid-19 in countries like India is casting a shadow over the global economic recovery. The path to recovery is highly reliant on Covid-19 vaccines being expanded much more than they are now, as well as inoculations proving successful against variants that have fueled second, or even third, waves of infections in some countries.

MENA: Are We Seeing a Bottom in the UAE Real Estate Market?

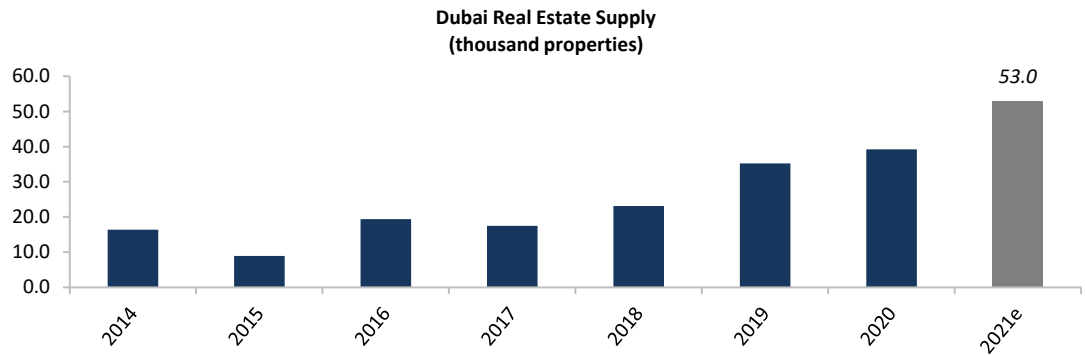
An oversupply in the property market and limited investor appetite have driven down real estate prices by more than 30% in Dubai since their peak in 2014, weighed down further by the coronavirus pandemic.

The increase in loan-to-value (LTV) brought by the UAE government as part of the stimulus package, coupled with historically low interest rates, in addition to an attractive entry point, means that buying property is now more affordable than ever. Property brokers are referring to higher LTV as “the unsung hero” of the success of the Dubai property market in 2020 as it allowed first-time buyers to enter the market through an unprecedented surge in mortgage transactions.

The pandemic created new pockets of demand as some people upsized and moved to villas from apartments for more space, while others downsized after pay cuts or job losses. These were the drivers behind the jump in transaction volumes seen in Q1 2021.



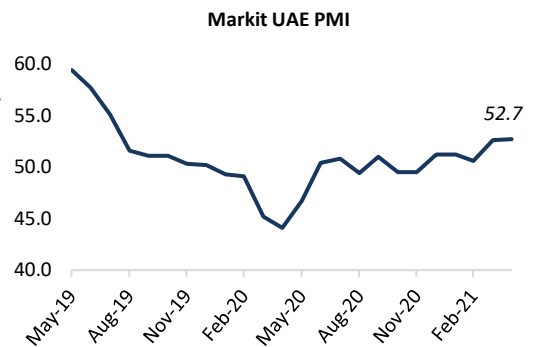
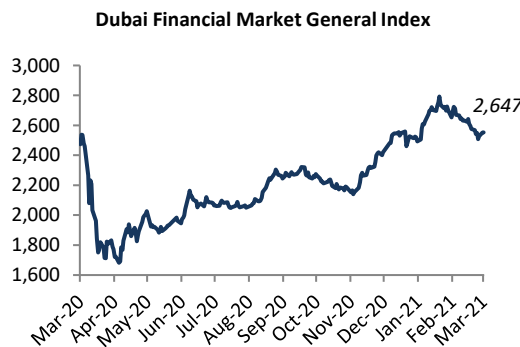
In terms of outlook, the recent series of measures to relax long-term visa and citizenship rules, the upcoming Dubai Expo 2020 (scheduled for October), and a thawing of relations with Qatar are seen as further positives that could boost investment in Dubai and its real estate market. And the way the government has dealt with the pandemic seems to have instilled some investor confidence in the UAE market.



Source: JLL, Capital Investments

Market indicators paint an optimistic picture for 2021, but the recovery will more than likely come from a proper management of supply. Varying estimates of 2021 supply have been released, ranging from 41.5k to 83k (up from 34k-39k last year), and while there is inconsistency surrounding the expected delivery of properties next year, one thing seems to be the consensus; it will be the largest supply in seven years.

2021 will be an interesting year for Dubai’s real estate market; prices of some properties have already begun to increase, others have stabilized, while some dropped, albeit at a slower pace than before. It remains to be seen whether the increased demand will be able to clear the glut as end-users continue to take advantage of favorable conditions.



Source: Bloomberg, Capital Investments

Major Indices	Status as of end		Performance	
	December, 2020	April, 2021	April, 2021	YTD (30 April, 2021)
MENA				
Abu Dhabi	5,045.32	6,046.81	2.27%	19.85%
Bahrain	1,489.78	1,484.85	1.84%	-0.33%
Dubai	2,491.97	2,605.38	2.16%	4.55%
Egypt	10,845.26	10,475.26	-0.88%	-3.41%
Jordan	1,657.22	1,795.35	1.30%	8.34%
Kuwait	6,051.07	6,623.17	4.72%	9.45%
Lebanon	657.89	920.34	5.81%	39.89%
Morocco	11,287.38	11,811.23	2.85%	4.64%
Oman	3,658.77	3,761.01	1.41%	2.79%
Palestine	471.26	479.34	2.82%	1.71%
Qatar	10,435.96	10,911.40	4.90%	4.56%
Saudi Arabia	8,689.53	10,418.98	5.16%	19.90%
Tunisia	6,884.93	7,164.20	1.06%	4.06%
S&P Pan Arab Composite	769.49	892.34	4.28%	15.97%
Dow Jones MENA	581.51	663.61	3.99%	14.12%
Americas				
Dow Jones Industrial	30,606.48	33,874.85	2.71%	10.68%
S&P 500	3,756.07	4,181.17	5.24%	11.32%
NASDAQ Composite	12,888.28	13,962.68	5.40%	8.34%
S&P/Toronto Composite	17,433.36	19,108.33	2.18%	9.61%
Europe				
EURO Stoxx 50	3,552.64	3,974.74	1.42%	11.88%
S&P Europe 350 Index	1,585.57	1,739.05	1.64%	9.68%
FTSE 100 Index/ London	6,460.52	6,969.81	3.82%	7.88%
FTSE MIB Index/ Italy	22,232.90	24,141.16	-2.06%	8.58%
DAX Index/ Germany	13,718.78	15,135.91	0.85%	10.33%
ASIA/Pacific				
NIKKEI 225/ Japan	27,444.17	28,812.63	-1.25%	4.99%
S&P/ASX 200/ Australia	6,587.10	7,025.82	3.46%	6.66%
BRIC				
Brazil/ Bovespa	119,017.20	118,893.80	1.94%	-0.10%
Russia/ RTS	1,387.46	1,485.03	0.54%	7.03%
India/ Bombay Sensitive	47,751.33	48,782.36	-1.47%	2.16%
China/ Shanghai Composite	3,473.07	3,446.86	0.14%	-0.75%
Hong Kong/ Hang Seng	27,231.13	28,724.88	1.22%	5.49%

Source: Bloomberg, Capital Investments

Description	Closing Prices as of end		Performance	
	December. 2020	April. 2021	April. 2021	YTD (30 April. 2021)
Commodities (in USD)				
Brent Spot (Barrel)	51.17	66.53	6.60%	30.02%
WTI Cushing Spot (Barrel)	48.52	63.58	7.47%	31.04%
Natural Gas NYMEX (MMBtu)	2.61	2.93	9.90%	12.26%
Gold Spot (OZ)	1,898.36	1,769.13	3.60%	-6.81%
Silver Spot (OZ)	26.40	25.92	6.14%	-1.84%
Copper LME Spot (MT)	7,749.00	9,829.00	11.85%	26.84%
Corn CBOT Active Month (Bushel)	4.80	6.73	22.97%	40.19%
Wheat CBOT Active Month (Bushel)	6.28	7.35	19.33%	16.95%
Soybean CBOT Active Month (Bushel)	12.98	15.34	7.46%	18.25%
Rough Rice Futures (USD/cwt)	12.40	13.39	1.56%	7.94%
Currencies Spot Exchange Rates Against US Dollar				
Euro	1.22	1.20	2.47%	-1.60%
GBP	1.37	1.38	0.28%	1.11%
CAD	0.79	0.81	2.21%	3.62%
Yen	0.01	0.01	1.28%	-5.49%
CNY	0.15	0.15	1.20%	0.80%

Source: Bloomberg, Capital Investments

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