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First Abu Dhabi Bank

EM Rates & FX, & Oil - The Traders' Weekly Views

Market Overview: Crunch Time Looms for Brexit

- Risk assets continue to get their groove back with investor sentiment being buoyed late last week by some optimistic headlines with regards to the Sino-U.S. trade talks as well as by the dovish nature of comments from Fed chair, Jerome Powell. Mr. Powell reassured markets that the central bank would be ‘patient’ in tightening monetary policy.
- Other Fed officials also added to the risk appetite fillip as the latest FOMC minutes from the December meeting showed that ‘many’ policy makers now believe that the Fed can ‘afford to be patient about further policy firming’. Federal funds futures are currently pricing in no further rate hikes for 2019, down from 30bps of tightening that was priced in last month. Equity markets reacted positively with major indexes adding to gains from last week while the Dollar remained weak with the Euro hitting a three-month high of 1.1570 to the dollar.
- GBP also managed to register some modest gains last week despite Prime Minister May losing two votes in parliament during the week, including defeat of her finance Bill on Tuesday. Indeed, cable has now pulled back from the $1.2487 low seen in December to $1.2844 as of Friday’s close.

Stay cautious

Source: Bloomberg/FAB

- However, it was perhaps, paradoxically, the second of the two Commons Brexit vote defeats for Mrs. May that fueled last week's strength in GBP. The latter defeat means that the government will now have to come up a 'Brexit Plan B' within three business days if Mrs. May's EU withdrawal deal is rejected by MPs in Tuesday's parliamentary vote this week, as is widely expected to be the case. The government had previously hoped it would have a 21 day grace period to come up with alternative proposals. As such, the shorter time frame and increased pressure for finding a solution is thought to increase the chances of the March 29 deadline being extended, a soft Norway style option being adopted or even a second referendum being called. All options could be back on the table, and for the 'Remainers' that equates to hope.
- The bottom line is that the Brexit saga is far from resolved. In fact, if anything, the situation seems set to turn a lot more opaque and uncertain this week. Uncertainty breeds contempt and will likely keep GBP, Gilts and U.K. risk assets on a back foot in the near-term and as such we would again advocate selling into any meaningful near-term strength in U.K. risk.
- Emerging market currencies also put in solid gains last week, with the Chinese Renminbi putting in its best performance against the dollar in a decade. This comes as China's top economic official is expected to travel to Washington later this month to continue the trade talks. The Rand, Mexican and Argentina Pesos also put in strong gains as the greenback lost ground.
- Meanwhile, crude oil prices rose further with the benchmark Brent crude equaling its record of nine straight days of gains, albeit paring its advance slightly into the close on Friday. The price rose briefly above $62 a barrel on Friday after Saudi Arabia's energy minister vowed to 'stabilize' the market before consolidating back to $60.59 by the close. Nonetheless, the overall weekly gains were sustained as the weaker dollar boosted the appeal of the broader USD-based commodities complex.

(Simon Ballard, Macro Strategist, Market Insights & Strategy)
(Tega Adeda, FX & Rates)

Please find below views on EM Rates & FX, & Oil directly from our traders.

Choppy start to the first full week of trading. US yields have retracted 12bp of the move on the 3rd Jan. 2019 FOMC pricing extremely benign with nothing further from the FED this year. Inversion remains prominent along the curve and every forward now sub 3% (10y5y at 2.99). Lots of issuance for the market to digest in EUR and GBP, with swap spreads continuing to cheapen. For FX, DXY struggling to rally and now sits at the key 95 level.

EM FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
INR	Higher crude prices put pressure back on the INR, and helped push USDINR higher throughout the past trading week. INR is the sole loser amongst Asia's major currencies, depreciating by 1% as crude oil prices rallied by 7%. In addition, India faces a tough challenge to improve its fiscal deficit condition. We are neutral on INR with slight bullish bias in a longer term view.	Neutral 70.00	Bearish 68.00

EM FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
CNH	CNH was the biggest gainer in Asia, appreciating by close to 2% on a w-o-w basis thanks to positive progress in the US-China trade negotiations as well as a cut in the reserve requirement ratio by 1% which boosted investor confidence. USDCNH never looked back at the 6.9000 level again and subsequently plunged briefly below 6.7500 level. It seems players will ignore headlines about China's possible economic slowdown for now and focus on trade talk developments. In summary, we maintain a slight bullish CNH bias on easing trade war concerns.	Neutral 6.7500	Bearish 6.7000
KRW	Some temporary relief for KRW this past week as US-China trade talks were seen to be progressing well. USDKRW fell from 1125 and attempted to test the 1115 level amid improved risk sentiment in Asia. However, further downward movement was limited as the market is still cautious in absence of detailed trade talk information.	Bearish 1115	Bullish 1130
EGP	Little change so far in the EGP interbank market for 2019 which is still drifting around 17.86-17.96. Inflation (CPI) data published in the past week came in at 12% vs 15.7% in November which should be helpful in pushing the yields lower for T-bills. The central bank reserves decreased in December to $42.6bln from $44.5bln previously, most likely because of the Eurobond debt repayment in December and some US dollar repatriations from the T-bills market before the year end. In the later part of the week we saw some significant EGP buying interest in NDFs and the curve moved about 0.5-1% lower. This is on the back of the overall positive sentiment to the emerging markets. Our medium term view is still that the spot market should start to adjust higher but the timing is not clear to us. However most likely it will happen in Q1 of 2019. For now if the broad US dollar weakness proves to be sustainable for 2019, we think that the USDEGP exchange rate would move to 18.30-18.75 at the most in the next few months. On the back of this we like to have steepening trades of being short 1-2 month NDFs and long in 6-12 months.	Neutral to bullish USDEGP 17.85-18.00	Neutral to bullish 18.00-19.00
NGN	The NAFEX fixing continued to print around 365 during this past week. The demand for dollars by local corporates remains lackluster as most of them haven't resumed full operations for the new year as yet. The Central Bank continues to intervene in the FX market whilst Foreign Portfolio Investors became net sellers of dollars after Investor sentiment to Emerging Market improved following more dovish comments from the Federal Reserve during the week. The treasury yield curve remains inverted, with the 1year T-bill currently offered at 17.6%, while the 10y and 20y bonds trade at 15.5% and 15.35% respectively. The inversion continues to be due to the tight monetary policy stance by the Central Bank. We remain very positive on Nigeria and have been buying 3m-6m T-bills as spot has been relatively stable, and the Central Bank continues to build foreign-exchange reserves. The last reading was $43.00bn, about 12-months' worth of import cover and down from a peak of $47.86bn in May 2018.	Neutral NAFEX USDNGN 362-365	Neutral to bullish 362-368

EM FX	Macroeconomic/Fundamental Analysis	Views (Bearish/Bullish) 2-week Time Frame	Intermediate & Long-term Views (3mth & 12mth Time Frame)
ZAR	It has been a slow past week for the rand in comparison to the first 7-days of the year but the USDZAR pair is grinding its way lower to clear the 13.74-13.80 level (200DMA). The mood in the market is that major central banks such as the Fed and the ECB will end their monetary tightening in 2019. Thus the investors are looking to put their money to work in asset classes with higher interest rates. Thus general US dollar weakness is helping to propel ZAR stronger as it is one of the leading EM currencies out there. Below here further levels to watch are 13.60 followed by 13.10-13.15.	Bearish USDZAR 13.20-14.00	Neutral to bearish 12.50-14.00

FX Options Commentary

- GCC vols have now eased after a period of stress in late December; this easing was mainly driven by a recovery in oil and hence less stress on the forwards. Demand for GCC options are also driven by the buy side and we think interest will return in 2019. We feel being long SAR options offers good risk / reward.
- INR vol is trading around the 8 handle and risk reversals (skew) eased with spot briefly below 70 earlier in the week. We like being long INR topside strikes to take advantage of a potential sell-off in the EM space. USDINR spot may eye the significant 75 level.
- Vols have eased after the flash crash in spot market (on the back of apple earnings news) but are still higher than December levels. GBP vols are the most expensive as the uncertainty around Brexit remains. Commodity currencies like AUD, CNH and CAD are performing spectacularly this week on the back of a weaker USD and mainly due to a rebound rally in oil.

GCC FX Commentary	
SAR	The SAR FX was significantly lower and flatter this week as oil prices continued to recover with Brent trading at $60/bl. Short dated FX Swaps were well-offered all week with day-to-day trading at -0.3 and the curve negative up to the 3 months tenor. $275m+ of long-dated SAR FX call options cleared the market causing spot and long-dated FX swaps to rise, although this move was short-lived and the curve then moved significantly lower to settle at 1Y 58/78, 2Y 210/260 and 3Y 450/550. Spot SAR remained bid trading at 3.7513/16 as banks looked to buy USD to offload their excess SAR liquidity. SAR rates volatility was sharply lower while liquidity has returned following thin trading during the seasonal break.
AED	The AED FX curve remained unchanged on the week with the regional 1Y FX swap at 20/30. AED FX spot is currently trading at 3.6730 mid, unchanged on the week. AED rates volatility levels are stable but this is mainly due to a lack of liquidity. We do not expect AED volatility to follow the SAR move lower as it continued to trade at same level as prior to the decline in oil prices.
KWD	KWD FX swaps have moved significantly higher as liquidity continues to tighten in the shorter dates, causing many to take longer dated FX swaps to fund their positions. Day-to-day funding has moved from being well offered at -1 to being very tight at +0.5 per day. The liquidity drain was due to Central Bank of Kuwait taking larger deposits from local banks in the 1 week window. The 1Y and 2Y FX swaps closed at -75/-45 and -75/+25 up from -110/-70 and -100/Par in the prior week. KWD FX spot is currently trading at 0.30295/05, 5 pips over the CBK fix.
OMR	The Omani FX curve was slightly lower on the week with regional market closing 1Y at 400/450 and 2Y at 800/900. Day-to-day funding continues to be very tight in OMR trading at +1 a day. OMR FX spot is trading at 0.38495/00, a pip lower on the week.
BHD	Longer dated Bahraini FX swaps moved significantly lower, while the liquidity buckets were remained bid. The market settled with 1Y 250/300 and 2Y 500/600. USD/BHD spot remained unchanged at 0.37698/03. The most recent 3-month BHD T-bill issuance yielded investors 4.24%, 1bp lower with coverage at 106% vs. 132% in the prior auction. The 6-month and 12-month issuance yields are 4.40% (-5bps : 199% coverage vs. 118%) and 4.90% (-3bps : 148% coverage vs. 133%), respectively.

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