بنك أبوظبي الأول
FAB
First Abu Dhabi Bank

US growth set to improve

KEY POINTS:

US non-farm payrolls robust at +223,000 in May, easily beating consensus

Some positive economic seeds being sown for Republicans ahead of November elections

Markets 'travelling hopefully' regarding reinstated Trump-Kim summit, with less concern about tariff issues

Italy formed a government, with two Eurosceptic parties coming together

US Technology stocks outperformed; we remain enthusiastic about the sector

INVESTMENT SUMMARY: Non-farm payrolls (NFPs) in the US increased by 223,000 last month, and the jobless rate fell to the lowest in 48 years, at 3.8%. This is helping to confirm our thesis of a very long economic cycle, and in the short-term suggests the 2.2% GDP growth of the first quarter will be the lowest for the year, with forecasts for the current quarter from the Atlanta Fed indicating a pace of 4.8%, with the comparable forecast from the New York Fed at 3.2%. The news is a tailwind for Republicans in the November elections, especially since the pickup in manufacturing jobs has been strongest in GOP-controlled states. Also, the biggest job gains were in groups that have historically suffered (younger workers and black workers), potential bad news for the Democrats. Black workers' jobless rate last month fell to 5.9%, a percentage point drop over just two months. After the NFP report, commentators again mentioned the possibility of the Fed quickening rate hikes, although we still expect them to stick to the existing plan, with 'gradual increases'. Accelerating growth in the US economy, and heading into 2019, is a contributory factor for the FAB Asset Allocation Committee (AAC) envisaging an overweight position in global equities by the fourth quarter, from the current slight overweight. The AAC met last week and voted to close half of its euro/dollar hedge, on the basis that investors had overstated the immediate political negatives in the Eurozone. **A rally in the euro back to about $1.20 would in all likelihood lead to the Committee putting the whole hedge back on, and given the consensus view of members that stresses in the Eurozone experiment are likely to build over time.**

The Markets: The NFP report helped the S&P 500 close 0.49% higher on the week, offsetting concerns that the trajectory of US rate normalization might be revised upwards. The NFP report detailed a better-than-expected performance from average hourly earnings (+2.7%, year-on-year), spurring optimism about the outlook for the US economy, and helping to drown-out latent worries about the imposition of Trump's tariffs in steel and aluminium on the EU, Canada and Mexico last Friday. In European assets, by the end of the week nervousness regarding Italy was replaced by relief that a new government had finally been appointed there, irrespective of its anti-establishment nature and despite expectations that the new Five Star-League grouping will take a very hard line with EU authorities under a number of headings. The news that Spain's Prime Minister, Mariano Rajoy, conceded defeat in a no-confidence vote wasn't deemed particularly important by investors, probably on the basis that it was expected, and more so because no opposition to membership of the EU or euro exists within Spain's political factions. **The STOXX Europe 600 index closed 1.07% lower on the week, with investors more focused on Deutsche Bank falling 8.38% over the period, than by Eurozone politics.**

In bonds, the US 10-year Treasury yield closed just under three basis points lower, at 2.9022%, off a closing low of 2.7810% earlier in the week. The US two-year Treasury yield closed fractionally lower, at 2.4716%, after a closing low of 2.3191%. In Europe, the yield on the German 10-year Bund closed two basis points lower, at 0.386%, the significance being that a relatively weak economic performance (and political factors) have brought the 'big picture' uptrend in this yield into question. In FX markets, the NFP report led to stability in the dollar (at 94.156 on its index, 0.10% higher) via its firming effect on dollar rates. The euro was marginally higher against the dollar, at $1.1659, while the yen was slightly stronger against the dollar, at ¥109.54. Sterling closed 0.28% firmer, at $1.3346. EM currencies as a class, measured by the MSCI Emerging Markets Currency index, closed just 0.16% lower and demonstrating stability after recent downside. In commodities, Brent crude closed slightly firmer, at $76.79/barrel, although the WTI price was notably weaker (at $65.81), with the spread between them widening to almost $11/barrel, more than twice the normal average. **Lastly, gold reflected easier perceived**

geopolitics, closing 0.68% (or $9) lower, at $1,293.40/oz, remaining friendless.

Further to the NFP headline data, the retail, health care, and construction sectors were in the vanguard. May's gain compared to expectations of about 188,000, and an average monthly gain of 191,000 over the previous 12 months. Turning to the all-important revisions, March was revised up from +135,000 to +155,000, and April was down from +164,000 to +159,000 - so employment gains in March and April combined were 15,000 more than previously reported; while this is a small number, it's the direction that matters. After revisions, job gains have averaged 179,000 over the last three months. The unemployment rate adjusted for (i.e. adding back in) discouraged workers and the under-employed fell 0.2 of a percentage point, to 7.6%, the lowest since May, 2001; this is a full point lower than the last trough in April, 2000, when it fell to 7.0%. The labor force participation rate, at 62.7%, and the employment-population ratio, at 60.4%, changed little in May so contained no complicating factors. **In conclusion, the labor market is strong, clearly good for boosting the consumption of goods and services, and this is feeding a virtuous US economic cycle via positive multiplier effects.**

Italy emerged with a newly formed government following an interlude in which President Sergio Matarella refused to accept the finance minister suggestion from the ruling coalition of populist parties Five Star Movement and the Northern League. Giuseppe Conte is back in the Prime Minister seat while 31-year old Five Star leader Luigi Di Maio is the new labor and economic minister. Matteo Salvini, who heads the League, will be the interior minister. Salvini is against immigration and has promised tax cuts, while Di Maio wants to increase welfare expenses. How much the two Eurosceptic parties will be able to implement is limited by the power held by President Matarella, whose term ends only in 2020. However, the formation of the government announced over the weekend is likely to bring back some of the volatility experienced earlier last week among Europe's peripheral countries, including Greece, Portugal and Spain. Madrid also faces turmoil as President Mariano Rajoy succumbed to a no-confidence vote. Instead of calling new elections, the People's Party-led coalition chose to have minority party Spanish Labor Socialist Party leader Sanchez take the Presidency. **His weak position is likely to prompt further challenges to the government and calls for new elections, especially from Ciudadanos ('Citizens'), the party that currently leads in polls. Finally, in Slovenia, nationalists were expected to win a weekend election.**

S&P Global Ratings affirmed the Kingdom of Bahrain at B+, with a stable outlook. That was a respite after Fitch Ratings' two-notch downgrade to BB- in March. The agency, however, noted the Kingdom's fiscal deficit, dependence on foreign markets for funding and depleted currency reserves - which the agency estimated at $2.5 billion at the end of April - as risks. Last week, too, the IMF completed its Article IV consultation mission to Bahrain. The preliminary report said policies to increase fiscal revenue, rein in expenditures - all while "protecting the most vulnerable - is urgently needed." The Fund added that the upcoming value added tax should help, but that Bahrain should also consider corporate taxes. Both S&P and the IMF, however, agreed that while there are risks on paper and the Kingdom needs to further its fiscal reforms, risks to the dinar's peg or of a debt restructuring are negligible because of the nation's importance within the Gulf Cooperation Council. In S&P's words: "We expect financial support for Bahrain's exchange rate arrangement from neighboring sovereigns would be forthcoming, if needed." In short, Bahrain has fiscal issues, but agencies and the IMF see little beyond headline risk. **Some of Bahrain's short term bonds are yielding more than 6%, with premiums of as much as 370 basis points over US Treasuries.**

Banks in the Kingdom of Saudi Arabia increased lending in the first quarter at the fastest rate since 2016, and the 1.46% increase in April was also the highest monthly increase since February, 2016, the Saudi Monetary Authority revealed last week. The lending increase and rising interest margins should boost the banks' return on equity, and provide another leg up for the sector, a key component of the KSA stock market. Bank stocks have been responsible for two thirds of the 13.4% gain in the Tadawul All Share Index for the year-to-date. Further good returns for bank stocks are likely to give an additional boost to the nation's index. **That, added to the expected inclusion of KSA in the MSCI Emerging Markets Index, is bullish for the local equity market.**

Alain.Marckus@bankfab.com
Christofer.Langner@fgb.ae

Disclaimer:

This report has been prepared and issued by Products & Services - Wealth & Private Banking ("P&S-WPB") of First Abu Dhabi PJSC ("FAB") outlining particular services provided by P&S-WPB and does not constitute or form part of any offer or invitation to sell, or any solicitation of any offer to purchase or subscribe for, any shares in FAB or otherwise or a recommendation for a particular person to enter into any transaction or to adopt any strategy nor shall it or any part of it form the basis of or be relied on in connection with any contract therefore. This report is incomplete without reference to, and should be viewed solely in conjunction with the associated oral briefing provided by P&S-WPB. The report is proprietary to P&S-WPB and may not be disclosed to any third party or used for any other purpose without the prior written consent of P&S-WPB. The information in this report reflects prevailing conditions and our views as of this date, which are accordingly subject to change. In preparing this report, we have relied upon and assumed, without independent verification, the accuracy and completeness of all the information available from public sources or which was otherwise reviewed by us. In addition, our analysis are not and do not purport to be appraisals of the assets, stock or business of the recipient. Even when this presentation contains a kind of appraisal, it should be considered preliminary, suitable only for the purpose described herein and not be disclosed or otherwise used without the prior written consent of P&S-WPB. FAB clients may already hold positions in the assets subject to this report and may accordingly benefit from the buying or selling of such assets as referred to in this report. This document does not purport to set out any advice, recommendation or representation on the suitability of any investment, transaction or product (as referred to in this document or otherwise), for potential purchasers. Potential purchasers should determine for themselves the relevance of the information contained in this document and the decision to purchase any investment contained herein should be based on such investigation and analysis as they themselves deem necessary. Before entering into any transaction potential purchasers should ensure that they fully understand the potential risks and rewards of that transaction (including, without limitation, all financial, legal, regulatory, tax and accounting consequences of entering into the transaction and an understanding as to how the transaction will perform under changing conditions) and that they independently determine that the transaction is appropriate for them given their objectives, experience, financial and operational resources and other relevant circumstances. Potential purchasers should consider consulting with such advisers and experts as they deem necessary to assist them in making these determinations and should not rely on FAB for such purposes. FAB is acting solely in the capacity of a potential arm's-length contractual counterparty and not as a financial adviser or fiduciary in any transaction unless we have otherwise expressly agreed so to act in writing. FAB does not provide any accounting, tax, regulatory or legal advice. FAB is licensed by the Central Bank of the UAE.

London: *FAB London Branch is Authorized by the Prudential Regulation Authority. Subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from FAB London branch on request. Registered in England & Wales: Company No: FC009142: VAT No: GB245 3301 91.*

Paris: *FAB Paris Branch is licensed by the French Prudential Control Authority as a credit institution. FAB Paris is registered in France under the company number: RCS Paris B 314 939 547.*

Switzerland: *This publication is for your information only and is not intended as an offer, or a solicitation of an offer, to buy or sell any investment or other specific product. Certain services and products are subject to legal restrictions and cannot be offered world-wide on an unrestricted basis and/or may not be eligible for sale to all investors. All information and opinions expressed in this document were obtained from sources believed to be reliable and in good faith, but no representation or warranty, express or implied, is made as to its accuracy or completeness. All information and opinions as well as any prices indicated are currently as of the date of this report, and are subject to change without notice. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. At any time the First Abu Dhabi Bank PJSC and/or FAB Private Bank (Suisse) SA may have a long or short position, or deal as principal or agent, in relevant securities or provide advisory or other services to the issuer of relevant securities or to a company connected with an issuer. Some investments may not be readily realizable since the market in the securities is illiquid and therefore valuing the investment and identifying the risk to which you are exposed may be difficult to quantify. Futures and options trading is considered risky. Past performance of an investment is no guarantee for its future performance. Some investments may be subject to sudden and large falls in value and on realization you may receive back less than you invested or may be required to pay more. Changes in foreign exchange rates may have an adverse effect on the price, value or income of an investment. First Abu Dhabi Bank PJSC expressly prohibits the distribution and transfer of this document to third parties for any reason. First Abu Dhabi Bank PJSC and/or FAB Private Bank (Suisse) SA will not be liable for any claims or lawsuits from any third parties arising from the use or distribution of this document. This report is for distribution only under such circumstances as may be permitted by applicable law. The "Directives on the Independence of Financial Research", issued by the Board of Directors of the Swiss Bankers Association (SBA) do not apply.*

Singapore: *First Abu Dhabi Bank P.J.S.C., Singapore Branch is regulated by the Monetary Authority of Singapore and holds a Wholesale Bank license.*