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The Context

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The Context

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Inside this week's edition:

Know the Flows

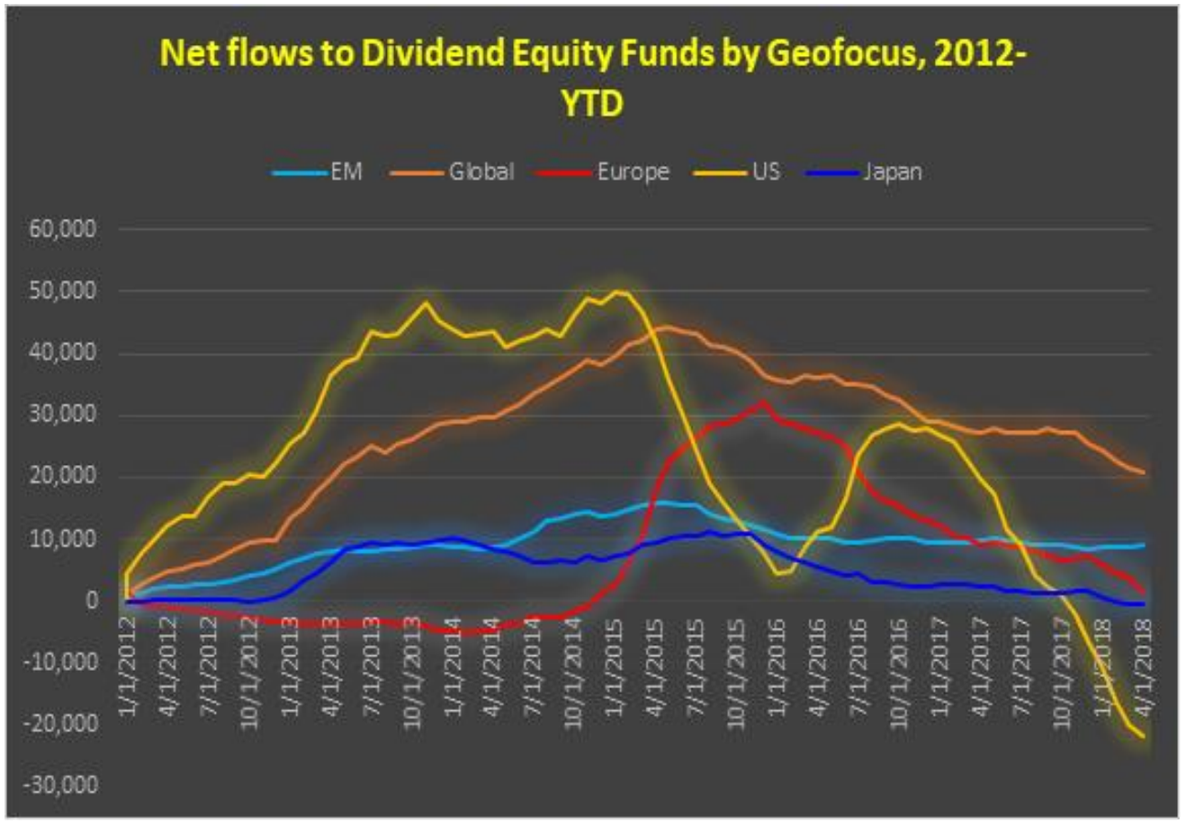
By Cameron Brandt, Director of Research

A number of market drivers hit eye-catching peaks during the fourth week of April. Unfortunately, most of them were the kind that kept mutual fund investors on the sidelines. Against a backdrop that included oil prices at a 40-month high, the yield on 10-year US Treasuries breaking the 3% mark for the first time since 2014 and inflationary expectations in the US at levels last seen in 4Q14 collective flows to EPFR-tracked Bond Funds came in at a modest $2.8 billion while $34 million flowed out of all Equity Funds, $362 million out of Alternative Funds and $14.8 billion out of Money Market Funds.

Investors have yet to completely give up on the synchronized global growth story, with diversified Global and Emerging Markets Equity Funds posting solid inflows for the week ending April 25. But their tolerance for political and policy risk remains at its lowest ebb for some time. The week's bookmarking the re-election of populist Hungarian leader Viktor Orban, for instance, have seen Emerging Europe Equity Funds compile their longest outflow streak since early 3Q17 while the latest redemptions from Emerging Europe Bond Funds were the highest since early 2015.

Despite periodic bouts of yield hunger, Dividend Equity Funds remain out in the cold even though dividend yields for US and European blue chip stocks average 2.1% and 3.6% respectively at a time when some 30% of the Eurozone's sovereign bonds trade at negative or zero yields. The Dividend Equity Funds tracked by EPFR chalked up their sixth consecutive outflow and 26th in the 30 weeks since the beginning of 4Q17.

At the asset class and single country fund levels, Mortgage Backed Bond Funds extended an inflow streak stretching back to the first week of the



year while Total Return Bond Funds snapped their longest run of outflows since 4Q16. India Equity Funds experienced net redemptions for the seventh week running, UK Equity Funds for the sixth time in the past seven weeks and Japan Bond Funds for the 18th consecutive week.

For the fifth week running a majority of the 11 major Sector Fund groups tracked by EPFR posted outflows as investors digested a string of earnings reports, rising US bond yields and the highest oil prices in over three years. During the week ending April 25, Commodities, Healthcare, Energy and Technology Sector Funds recorded inflows ranging from $42 million to $460 million while the other seven groups experienced net redemptions.

Back to Index Page

The 3% Solution

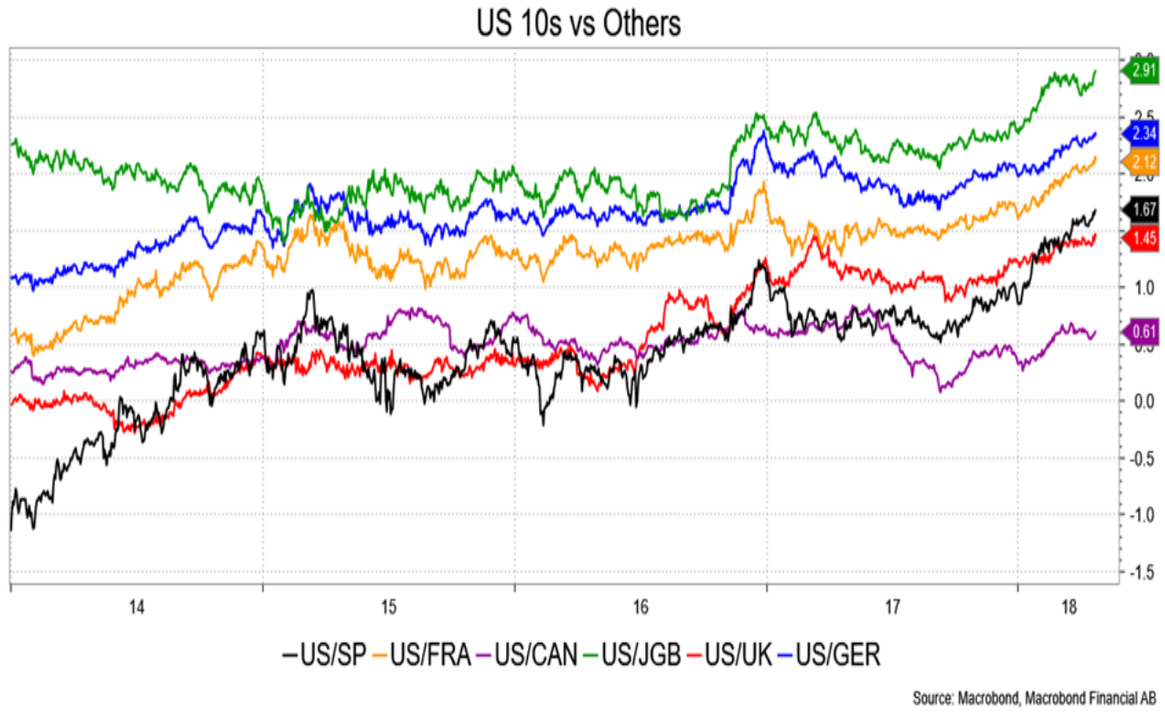
By David Ader, Chief Macro Strategist

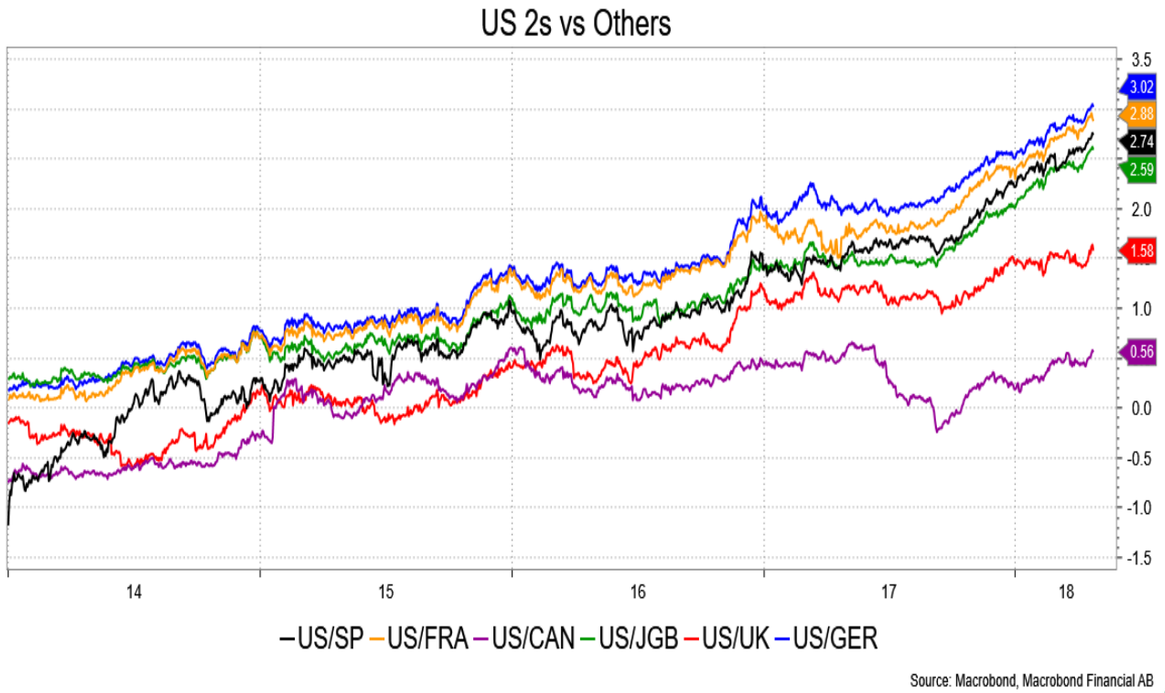
Have you noticed the rate differentials? The US is at multi-year highs versus everyone and the dollar, well, is cheaper too. With no insight other than experience and longevity, I suspect that there is targeted buying interest and that's where benchmark yields may come into play. I refer to 3% 10s or 3.25% 10s. Which makes the upcoming Refunding especially interesting.

This surely helped inspire a "Tail Risk" note in the FT, which teased with this header "Treasury yields 'attractive' as inflation risk dims." The upshot was mention of several investors, Pimco, Fidelity and BNP by name, who are looking at current yields and liking them. The view was that inflation could put some upward pressure on rates short term, but maintained it was really only a gradual gain and the 'bad' news, as well as the Fed is well priced in. Maybe I should adjust my 3.25-3.5% 10-yr target?

(Oh, the headline -- The 3% Solution? -- refers to the Sherlock Holmes story The Sign of Four, where it was revealed that Holmes was a cocaine user, utilizing a 7% solution. When asked by Watson what he was doing Holmes said, "It is cocaine," he said, "a seven-per-cent solution. Would you care to try it?" Holmes used cocaine when he wasn't on the case, bored in other words, and so did it to stimulate his cerebral cortex.

Thus, in my convoluted way, I offer up the 3% to a bond market in need of stimulus at the moment, waiting on new data, inputs or tweets on everything from trade, to North Korea, Iran and to decide for itself what the curve's action is really telling it.)





Back to Index Page

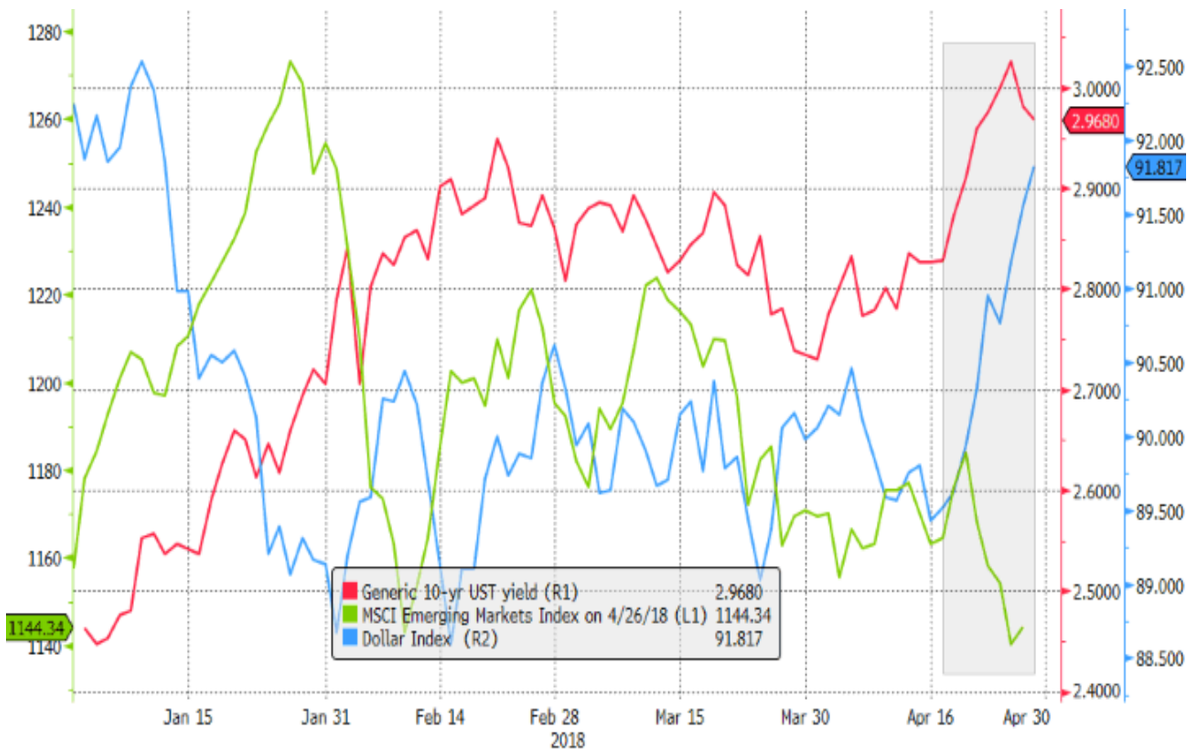
This is an excerpt from Ader's Musings. For the full article, please click HERE.

Outlook Still Constructive Over The Longer-Term For The MSCI EM Index

By Natalie Rivett, Senior Emerging Market Analyst and
Ed Blake, Chief European Fixed Income Technical Analyst

The MSCI EM Index (MXEF) has taken a breather over the last few months, after reaching a 10-year high of 1,273 in January and having almost doubled in value over the past two years.

Investors have had plenty to keep them cautious, with trade war prospects and geopolitical tensions both adding to the ongoing focus on policy tightening – and specifically the prospect of up to four hikes this year from the Fed - that has offered some strength to the US Dollar and helped raise UST yields, with the 10-year breaching 3% last week for the first time in over four years.



This all poses the question as to whether the pause is the start of a deeper correction lower in the EM equities market.

There has been a general acknowledgement from analysts that increasing trade disputes and geopolitical tensions are threatening global growth prospects. These risks posed to the bullish outlooks for global and emerging market growth did not appear present two months ago, when the 10-year UST yield looked to be approaching 3%. Hence, there is a risk that further UST yield upside may have a more significant weight on the MXEF going forward.

Nevertheless, despite these growth risks, the global economy remains robust and headed for its strongest year for growth since 2011. Recall, the IMF does not see a slowdown kicking in until beyond the next couple of years, having recently stood by its projection of faster growth of 3.9% this year and next, while most analyst forecasts for 2018 global growth are still centred around 4%, according to Bloomberg.

Data from EPFR shows that investors have not backed off from EM equities exposure with cumulative net inflows rising to almost USD54bn year-to-date and on course to exceed last year's USD64bn tally. The expected continuation of a global synchronised recovery this year, together with contained inflation are two potential factors driving this appetite for EM equities, alongside improved current account balances and external balance sheets within the region.

In our opinion, the global and Emerging Market growth outlooks are still favourable and so, a 10-year UST yield of 3%+ should not prove to be any threat to EMs, so long as there is no exacerbation of trade war concerns or any significantly faster pace of monetary tightening from the Fed to knock sentiment. We therefore retain a constructive outlook for the MSCI EM Index.

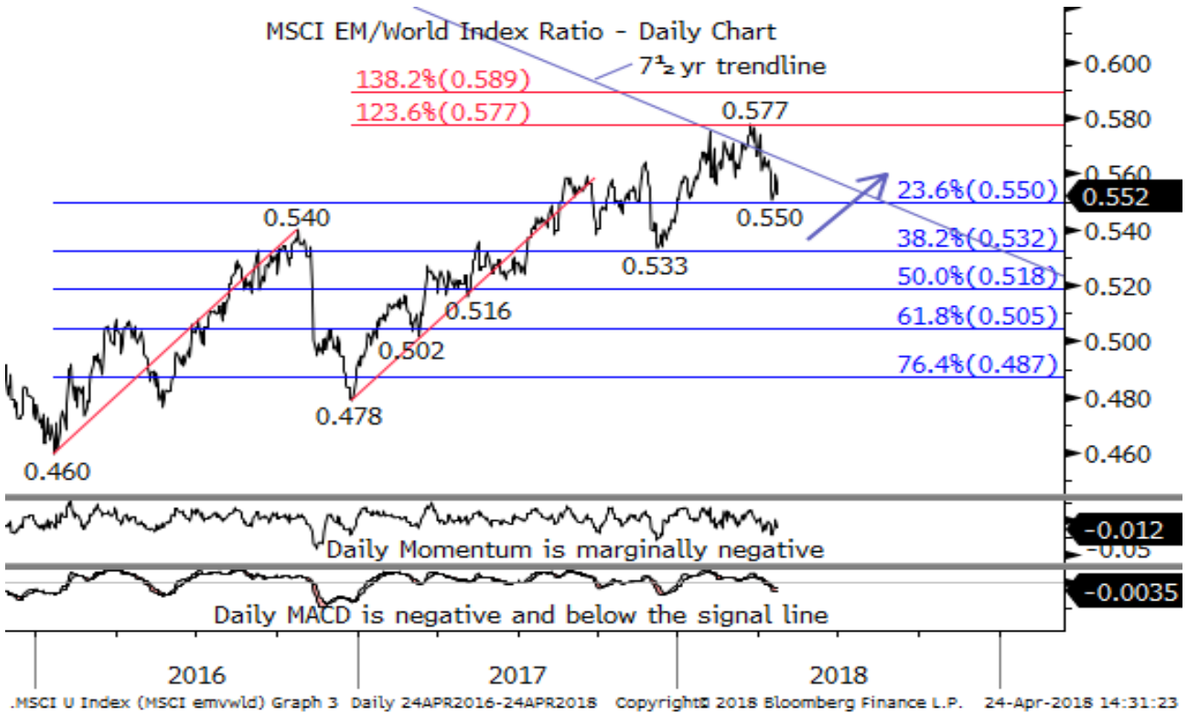
The technical picture broadly supports, with scope for a longer-term uptrend to 1345.18 (2017 high), possibly beyond, though only after a deeper, near-term correction (see below).

Continued p6

Outlook Still Constructive Over The Longer-Term For The MSCI EM Index … Cont'd

- Completed a 9yr bullish triangle in mid-2017 and extended to 1278.53 (2018 high – 29 Jan), before easing to range over 1136.27 (9 Feb low, nr 23.6% retrace of 686.74/1278.53).
- Deteriorating daily/weekly studies suggest a 1136.27 re-test, below which signals a deeper near-term correction of the current 2-1/4yr uptrend from 686.74 (2016 low – 21 Jan).
- However, 1086.54/1098.10 (1x 1278.53/1136.27 off 1228.80 and 7 Dec 17 low) should hold allowing renewed strength through 1228.80 (27 Feb low) re-opening 1278.53.
- Beyond extends the longer-term uptrend for 1345.18 (2017 high – 2 Nov), perhaps 1452.78 (1x 445.94/1211.98 off 686.74).
- Only below 1086.54 risks a deeper-than-expected pullback towards 1039.97/1052.47 (11 Aug 17 higher low and 38.2% of 686.74/1278.53).

Furthermore, the expected recovery in the MSCI EM Index should also help to ensure EM stocks continue to outperform their DM counterparts, bringing about a resumption of the 2.5-year recovery of the MSCI EM/MSCI World Index ratio (see below). This climbed to a near 3-year high of 0.577 in early February of this year, before correcting lower to circa 0.550 this month.

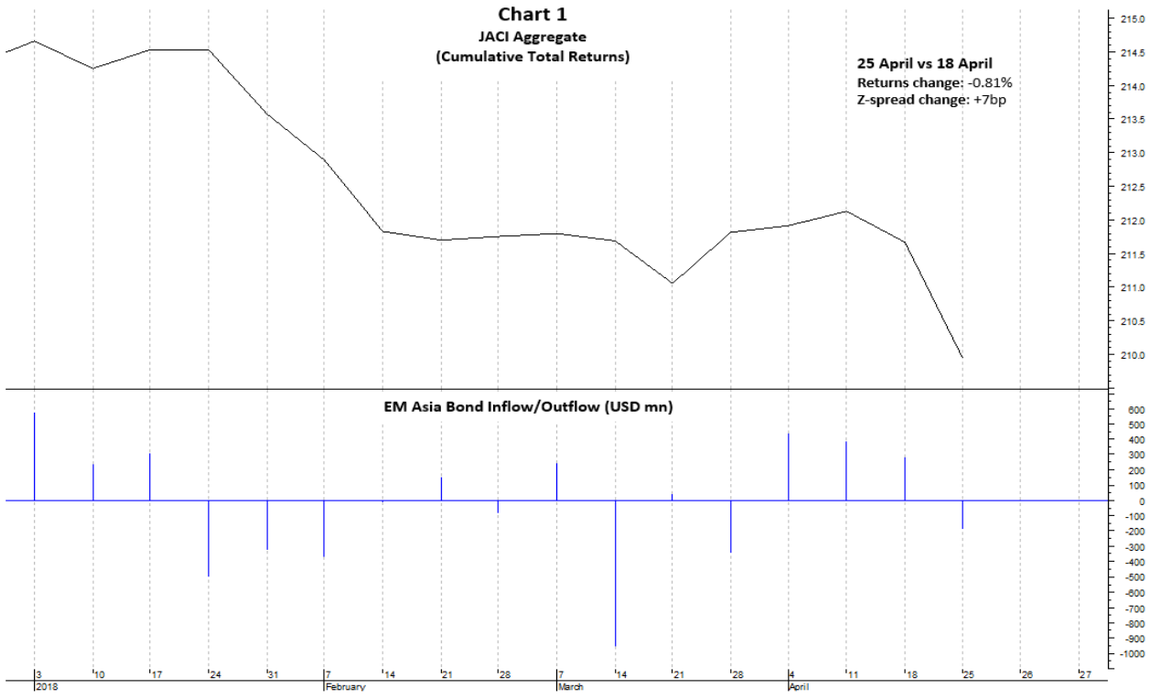


- Extended the 2-1/4yr recovery from 0.460 (2016 low – 21 Jan) through a 7-1/2yr falling trendline to reach 0.577 (22 Mar YTD high), before retreating
- Deteriorating daily studies suggest near term corrective risk towards 0.533 (6 Dec 17 low, nr 38.2% retrace of 0.460/0.577)
- However, while 0.533 holds, constructively aligned longer term studies suggest a resumption of the 2-1/2yr recovery
- A sustained clearance of the 7-1/2yr trendline and then 0.577 opens 0.589/0.591 (1.382x 0.460/0.540 off 0.478 and 2015 high – 27 Apr)
- Only under 0.533 would concern and risk 0516 (5 Mar 17 low, near 50% retrace of 0.460/0.577).

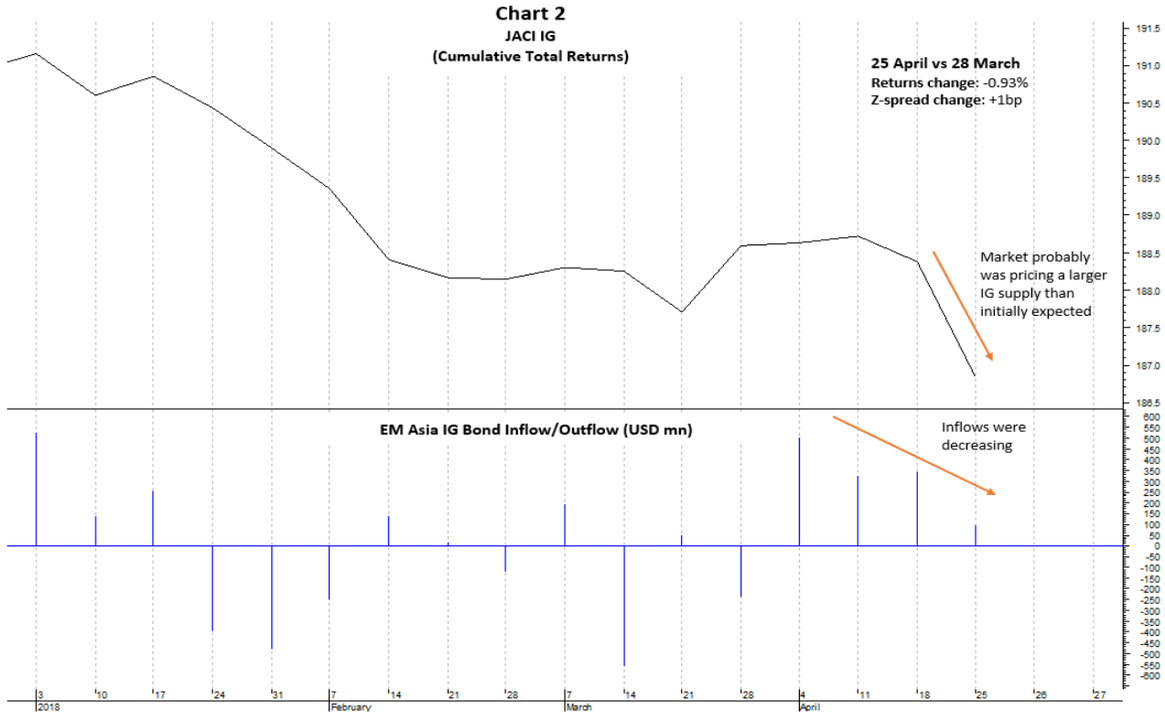
Asian Credit Barometer: IG Supply Forecast Being Raised, Indonesia Hit

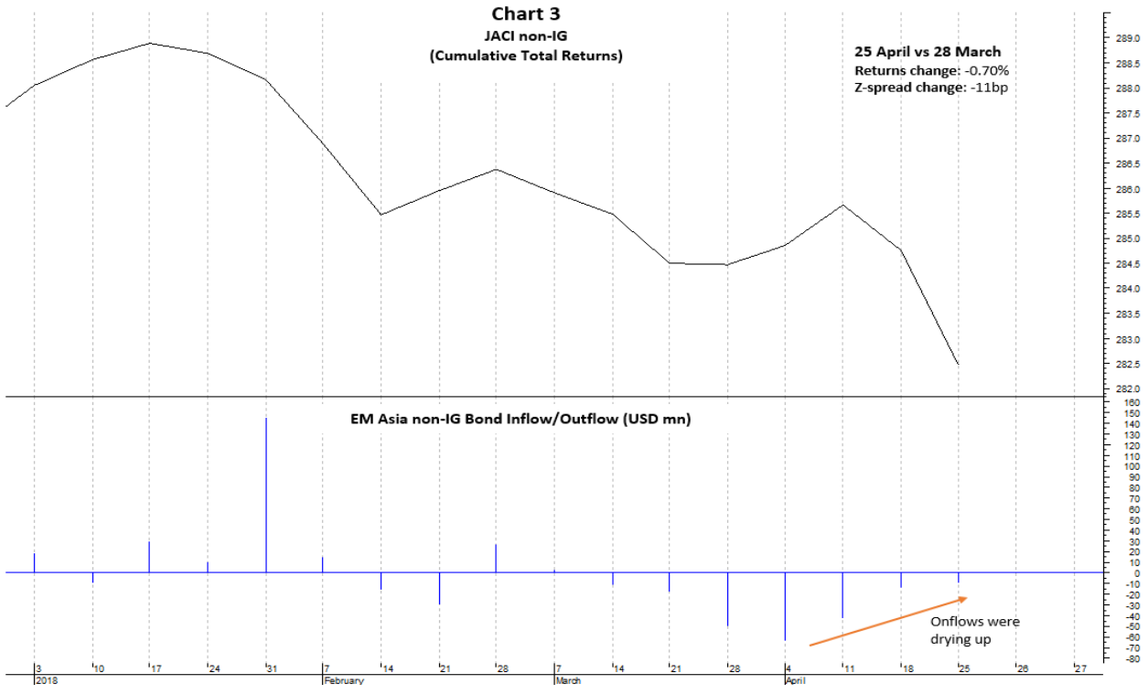
By Tim Cheung Head of China and Riki Zhang EM Analyst

The JP Morgan Asian Credit Index or JACI lost 0.81% in terms of returns (note: z spread +7bp) over the week ended 25 April (chart 1).



HY's outperformance relative to IG turned less obvious over the week. However, over the period starting from late-March, HY has performed considerably better than IG. This suggests the market is probably revising upwards its forecast of EM Asian IG supply this year and especially from China, due to the continued financial deleveraging onshore.



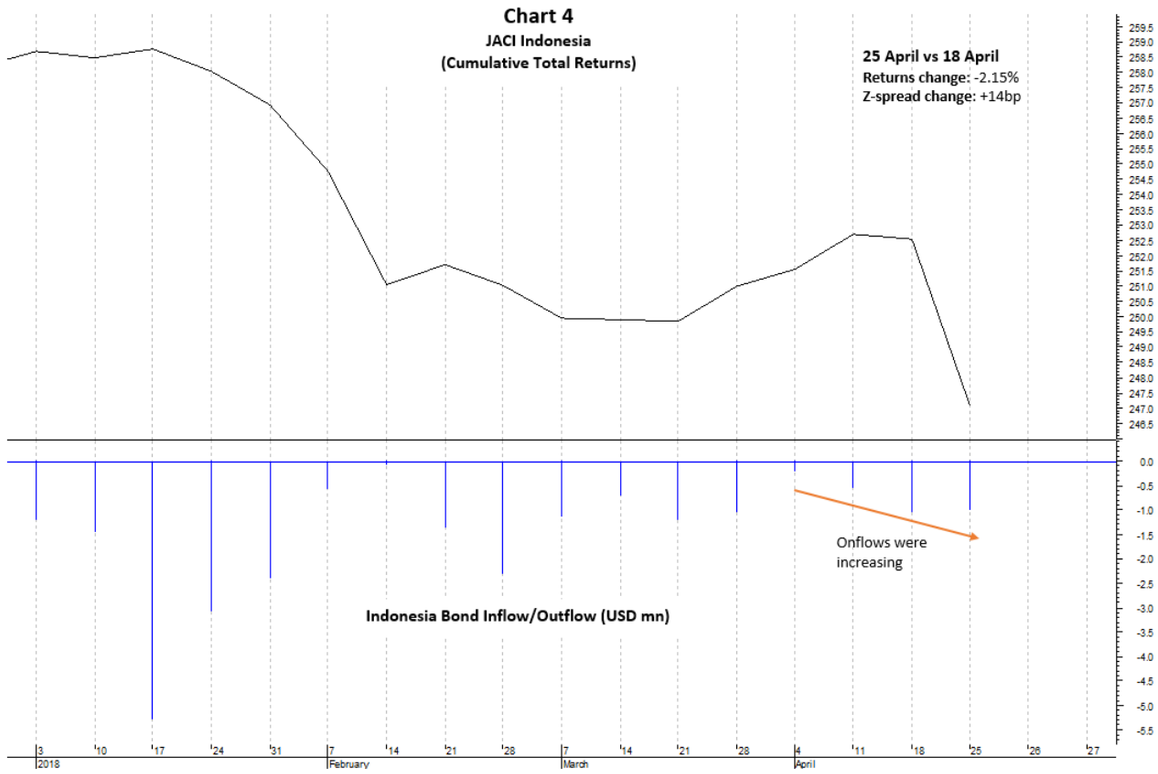


Note: Charts 1 to 4 reflect their potential impact of EPFR fund flow data on Asian secondary market credit performance as measured by the JACI.

Continued p8

Asian Credit Barometer: IG Supply Forecast Being Raised, Indonesia Hit … Cont'd

At the country level, **Indonesia** gave up more than the gain in returns registered in the prior week. Apparently, many investors just wanted to unwind their portfolio regardless of the recent sovereign credit ratings upgrade



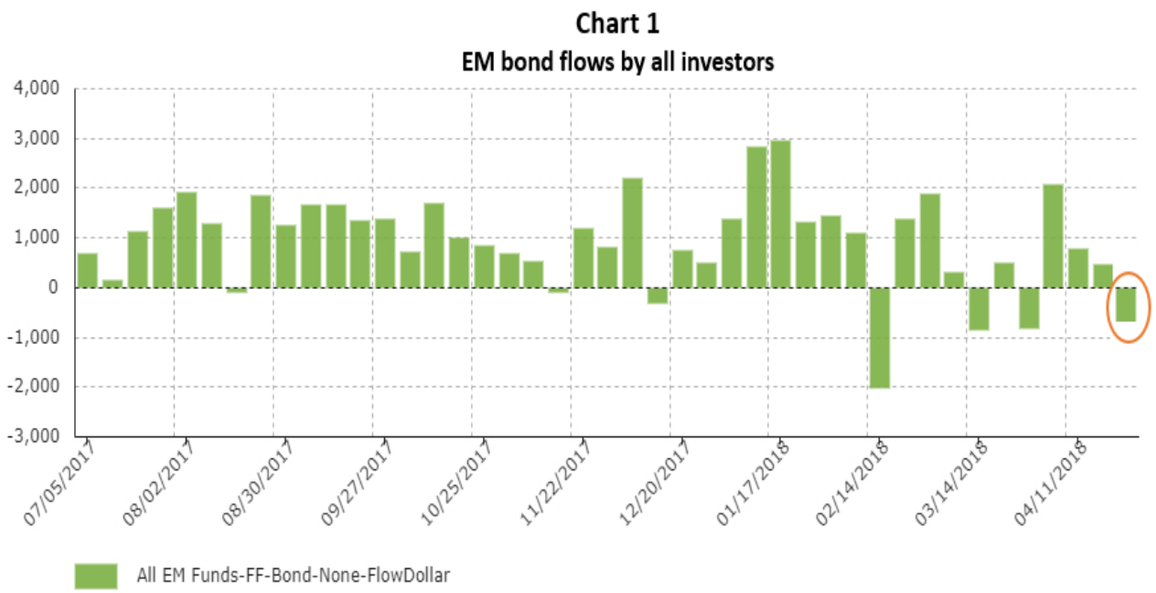
In our view, the disappointing performance of Indonesian bonds in the week ended 25 April should be largely attributed to the sharp fall in IDR vs USD in FX market. Chart 5 shows that Indonesia bond positioning has been shrinking since December 2017. As such, once the ongoing portfolio adjustment is finished, bond allocation to Indonesia might see a U-turn, reflecting the better credit outlook of the country. Despite that, we don't expect any big inflows as valuations there remain demanding.

Data source: BAML

Asian Bond Demand Shrinking Amidst A Run Of Negative Factors

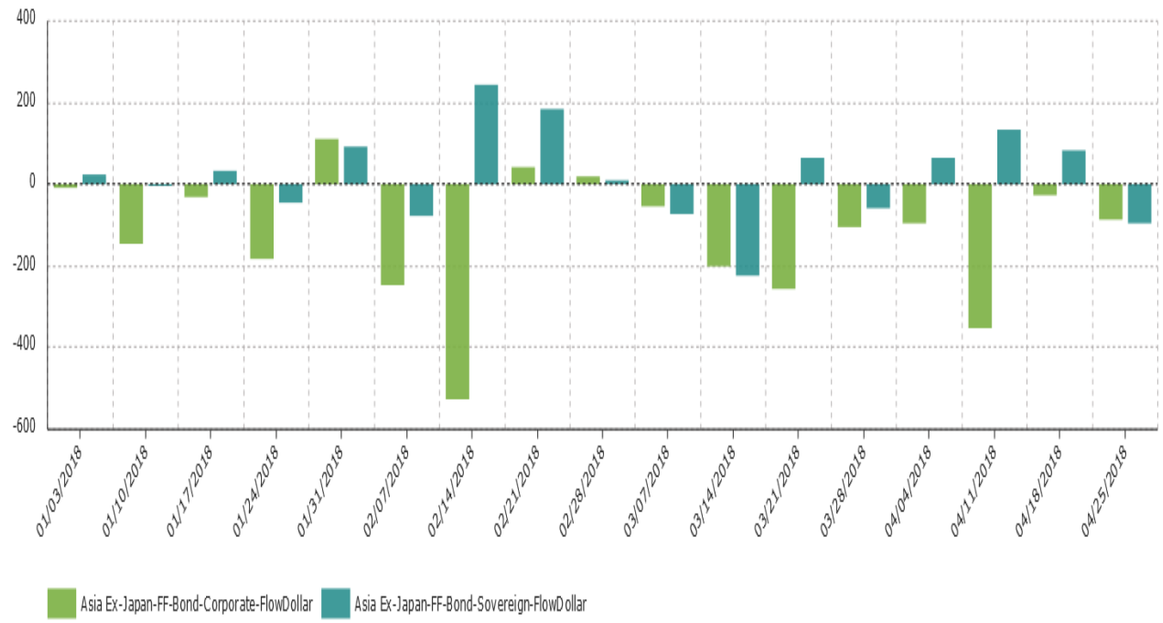
By Tim Cheung Head of China and Riki Zhang EM Analyst

All EM regions suffered bond outflows in the week ended 25 April per latest EPFR data (chart 1). Across-the-board outflows have been rare YTD, reflecting the negative impacts of a couple of factors in play, including higher UST yields.



Asian Bonds in themselves started the year on a negative note due mainly to the stretched valuations in the region. From March, sentiment has deteriorated further amid the escalating US-China trade conflict. In the latest week, EPFR data showed EM Corporate Asia ex-Japan Bond Funds losing USD86mn, an 8th consecutive weekly outflow, whilst EM Sovereign Asia ex-Japan Bond Funds also lost USD93mn, ending a 3-week streak of inflows.

Besides lack of upside potential due to stretched valuations and an increase in volatility amid growing trade tensions between the US and China, Asian credits have also suffered from a shift in technicals as a result of heavy supply. As of 20 April, Asia USD fixed supply had reached USD82bn, shy of the USD88bn printed in the same period last year, but still a large amount. This largely explains the underperformance of Asia versus other EM regions in Q1 2018.



Due to continued financial deleveraging in the onshore market, **China issuers** have been flocking to the offshore bond market for funding. Largely due to the increase in offshore supply from Chinese issuers, the gross EM Asia bond issuance in 2018 is unlikely to be significantly less than that in 2017. There is a good chance that gross supply for 2018 will hit our forecast of USD260-330bn, set in December last year. As far as we are aware, many market participants at the end of 2017 did anticipate 2018 gross supply to fall between USD200-260bn. In light of a potential increase in offshore supply from Chinese issuers, they have no choice but to revise their forecasts upwards. That, we think, will have a negative impact on market sentiment.

Besides that, we also saw unwinding of some structured leveraged notes, which put further pressure on certain pockets of the market e.g. China bank AT1 and corporate hybrids. Meanwhile, offshore demand from private banks has also waned as rising LIBOR increases the costs of holding leveraged positions.

Back to Index Page

India Watch: Fewer Headwinds In Usd/Inr Than Sensex

The Detrimental Effects Of a "Twin Deficit"
Freda Yeo, Emerging Market Analyst

Of the regional Asian economies, those bearing a 'twin deficit' have seen their currencies on a weaker footing in recent times than others. **India's INR** is a case in point, buffeted by rising yields despite the RBI's and the government's best attempts, as the market focuses on growing fiscal and trade deficits driven by higher oil prices, while earlier fiscal stimulus is driving consumer demand and more imports. The expectation of large bond issuance has beaten bond investors into retreat. While super sovereigns and bank analysts continue to see the economy performing above 7% in this fiscal year, there remains underlying doubts as the markets have been disappointed more often than not in recent times.

USD/INR Rallies Strongly Above Bollinger Upper Band
Clarence Poh, Technical Analyst

- Bulls continue to make great strides since the 20 Apr breakout of 65.893 (28 Sep former key reaction high) as recent price action surf above the Bollinger upper band - it is no mean feat considering the 2 standard deviations above the middle band.
- Golden cross of 9/45-DMAs of 14-day RSI and the ADX component of DMI study rising high above the indicative 25 level corroborate with our view of protracted gains ahead.
- As yet, over 61.8% of the Nov 2016-Jan 2018, 68.86.-63.246 decline has been retraced while overbought signals caution a minor but constructive pullback might be warranted.
- We do not expect strong headwinds until the region of 67.325/537 (8 Dec '16 former pivot low/76.4% retracement).
- Only a drop under and/or close below 20-DMA (now at 65.649) would caution an interim top is in place and a correction phase is due.

Continued p11

India Watch: Fewer Headwinds In Usd/Inr Than Sensex … Cont'd

Sensex Rally May Run Out Of Steam Near 34610-35509 Area

Jimmy Lee, Technical Analyst

- Since March 21, we favoured a test at the layers of supports at 32565.16-32364.66 (6 Dec higher low/38.2% of 25717.93-36443.98) and market have since tested 32483.84.

- We were anticipating a further breakdown towards the Aug-Sep 2017 higher floor at 31128.02-31081.83 (also near 50%), where we expected more serious bids from dip buyers. However, dip buyers have set in earlier than we expected, triggering a rally off 32483.84.

- While there are positive indications from this rally, mainly a move back above the 50DMA/a break above the normal RSI bear range ceiling at 60/breach of prior lower high at 34610.79, we remain reluctant to call an end to the selloff from 36443.98 (29 Jan high).

- Momentum has markedly slowed down, right as price action is probing the median line of a 2 year plus rising regression band and into the key resistance zone at 34610.79 (27 Feb lower high) – 35509.39 (76.4% of 36443.98-32483.84).

- We thus remain wary of bears reasserting to resume the sell off from 36443.98.

- A breakdown back below the 50DMA will be the initial sign that the sell off from 36443.98 is yet to be completed, while a move under the 200DMA likely increases the probability of a breakdown below 32483.84 towards our mid-term 31128.02-31081.83 targets

- A move back above 35509.39 (76.4%) likely shifts us back to the bullish viewpoint.

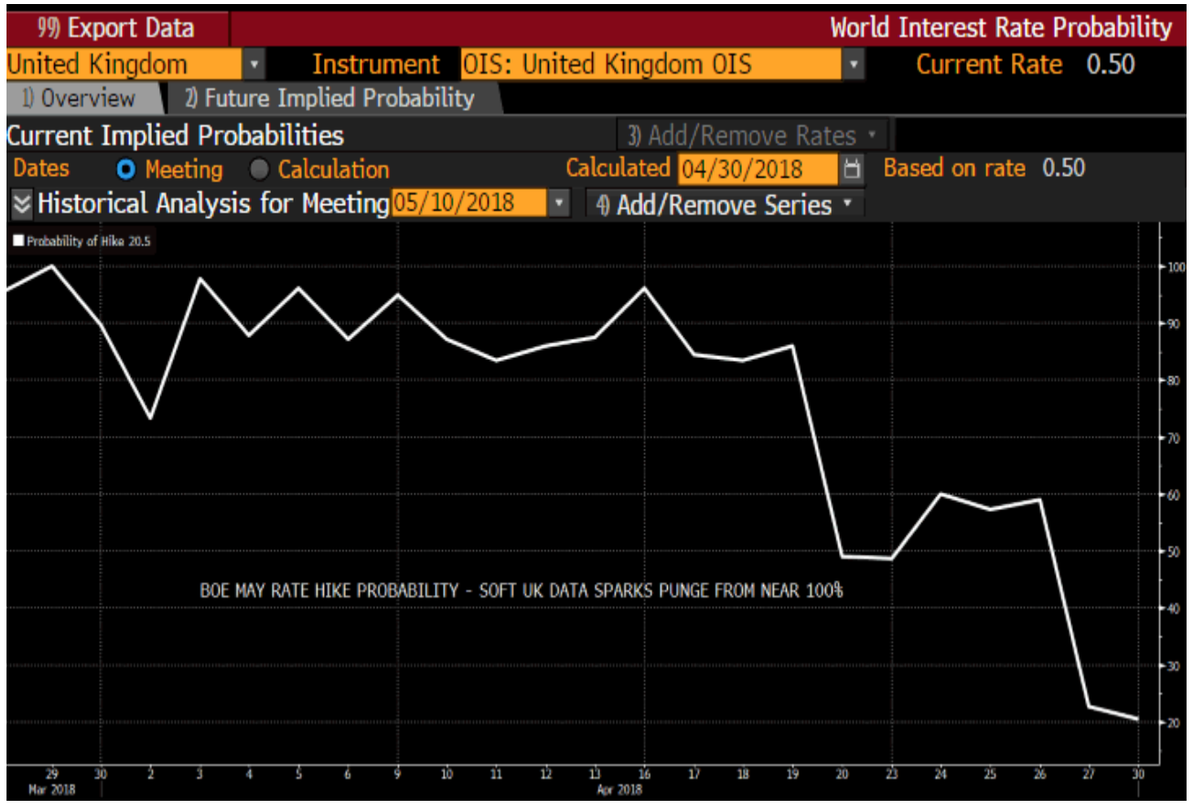
Back to Index Page

The Gbp Week - Bias Is Bearish

By Tony Nyman, Head G10 FX

Expected Gbp/Usd trading range is 1.3630/1.3800.

The decline is continuing, intensifying even. The run coincides with a plunge in BoE May rate hike probability from near 100% March 29 and 95%-plus mid-month to current series lows of approximately 20.0%.



It's been a sorry UK data run of first-tier big misses, i.e. CPI, AWE, retail sales and Friday's shocker of 0.1% q/q Q1 GDP vs the 0.3% median.

On the latter, contacts report the MPC has never hiked when the latest estimate of GDP growth has been below 0.4% q/q.

It doesn't look good for the Pound right now with the backdrop of returning Usd strength and independent losses, including M&A too (Sainsbury to pay Usd 4.0bn-plus to Walmart as part of Asda deal) and Northern Ireland border uncertainty ahead of next EU/UK Brexit talks.

However, before bulls throw in the towel for a test and even break of 1.3500/30 and the 200-dma, we say it's all pretty data dependent still. The BoE are not in a mad rush to normalise, but the 7-2 result last month suggests some Board members are at least keen to hike in 2018.

Earlier the better? Well, that could depend somewhat on this week's PMIs, which are expected to get back on track. The composite is forecast to improve to 53.7 in April versus 52.5 last.

RISK - How good do the PMIs need to be to spark a May rate hike market return?

Back to Index Page

The NOK Week - Bias is Neutral (To Bullish)

By Mark Mitchell, Senior FX Analyst

Expected EUR/NOK trading range 9.5500 to 9.7400.

Last week Eur/Nok made another failed upside attempt, with the pair stopping short up at 9.7222. The more dovish than expected ECB update saw the pair retreat to 9.6286, but now the pair is looking towards this Thursday's Norges Bank decision.

The higher than expected 1.1% rise in Norwegian Mar retail sales calms some fears over the health of the Norwegian consumer and the domestic housing market, but other soft Norwegian data of late (most notably CPI), are likely to mean that the Norges Bank will not hike before the September meeting, that was targeted after the last decision.

One factor though that may exert a lot of influence at Thursday's meeting is the respective policies of Norway's neighbours. The Norges Bank have often mentioned how much of an issue policy is elsewhere, so last week's push back in interest rate expectations by both the Riksbank and the ECB, may mean we see a more measured Norges Bank.

It is now over two months since Eur/Nok traded above 9.7300, despite myriad breaks above 9.7000, so we may see a downside test in response to this latest rejection, with bids seen into 9.5500 a viable target.

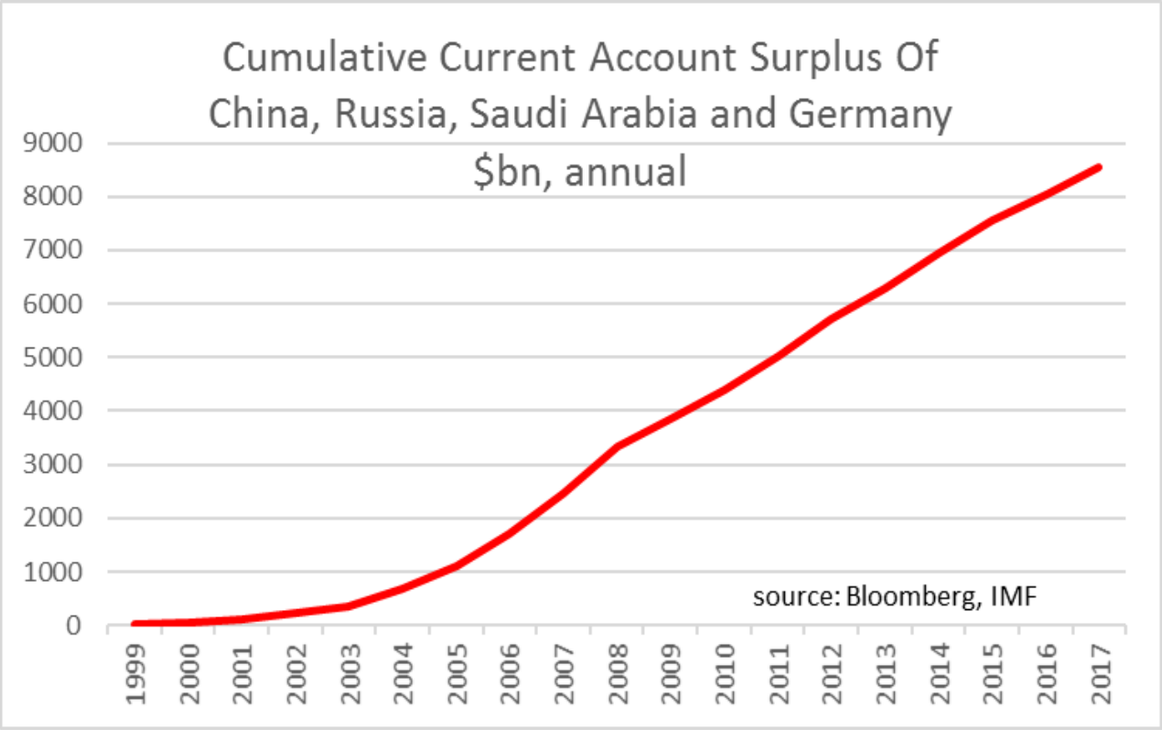
RISKS - The Norges Bank meeting on Thursday is expected to continue to underpin the Krone, but we will be looking to see if the central bank makes any mention of interest rate expectations coming out of its neighbours.

The Beginning Of The End For The Savings Glut?

By Marcus Dewsnap, Senior Editor/Analyst

That Saudi Arabia is raising large amounts of sovereign debt and looking to sell off a portion of Aramco has far more implications than it first seems as it related to the much vaunted 'Savings Glut'.

The simple implication of the global savings glut is that it is by-and-large responsible for the fall in global bond yields since the 1990s. That is, global savings have been far larger than global investment demand which forces interest rates down to clear the excess savings.



So, an obvious question – is there anything that can/will reverse the excess savings account?

China's 'Belt and Road' infrastructure project is already a destination for the country's savings. Indeed, the nation's current account surplus has fallen from circa 10%/GDP at its peak to just over 1%. An interesting point is that Beijing is asking project partners to settle trade in Yuan. China wants the Yuan to be a reserve currency, perhaps ultimately *THE* reserve currency. A major reason for this is to create currency demand that is not export dependent … perhaps reasoning that it will become a deficit country. Demographics will eventually catch-up as well turning the savers into borrowers.

Demographics are an issue for Germany too with significantly fewer workers likely to enter the workforce than those retiring in the relatively near future. Berlin is also under pressure to 'do more' to stoke internal demand and reduce its budget surplus.

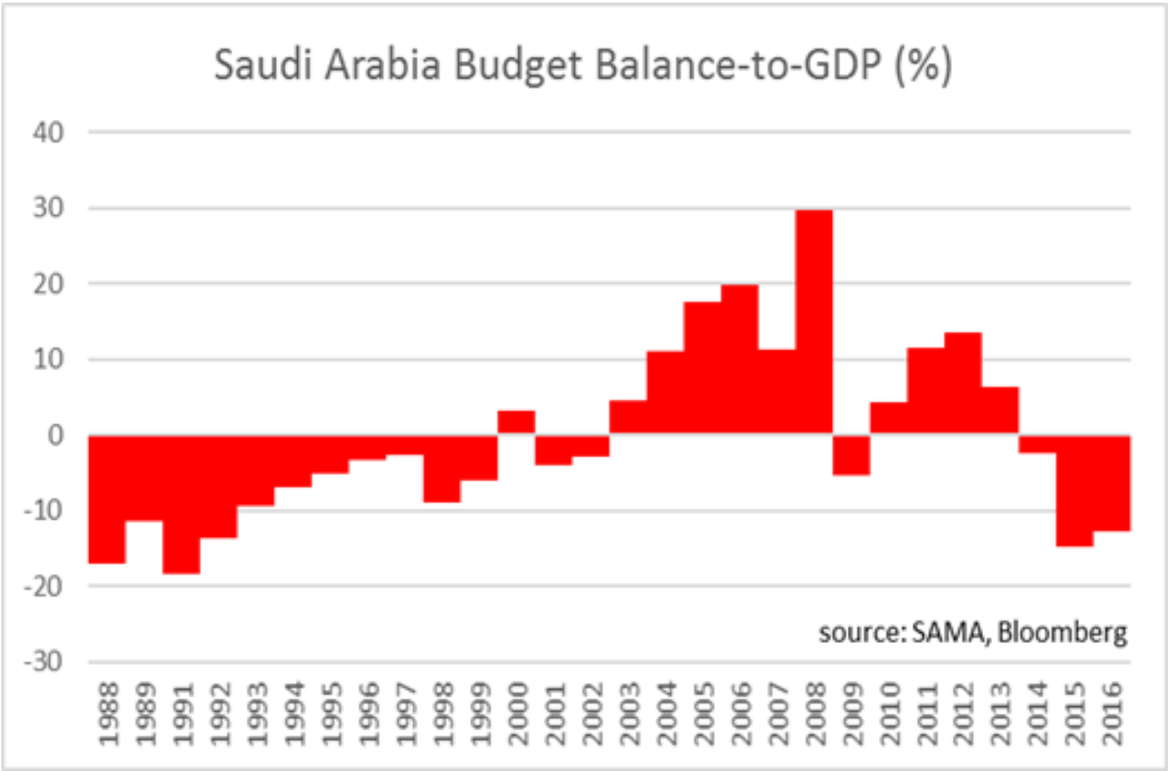
Continued p15

The Beginning Of The End For The Savings Glut? … Cont'd

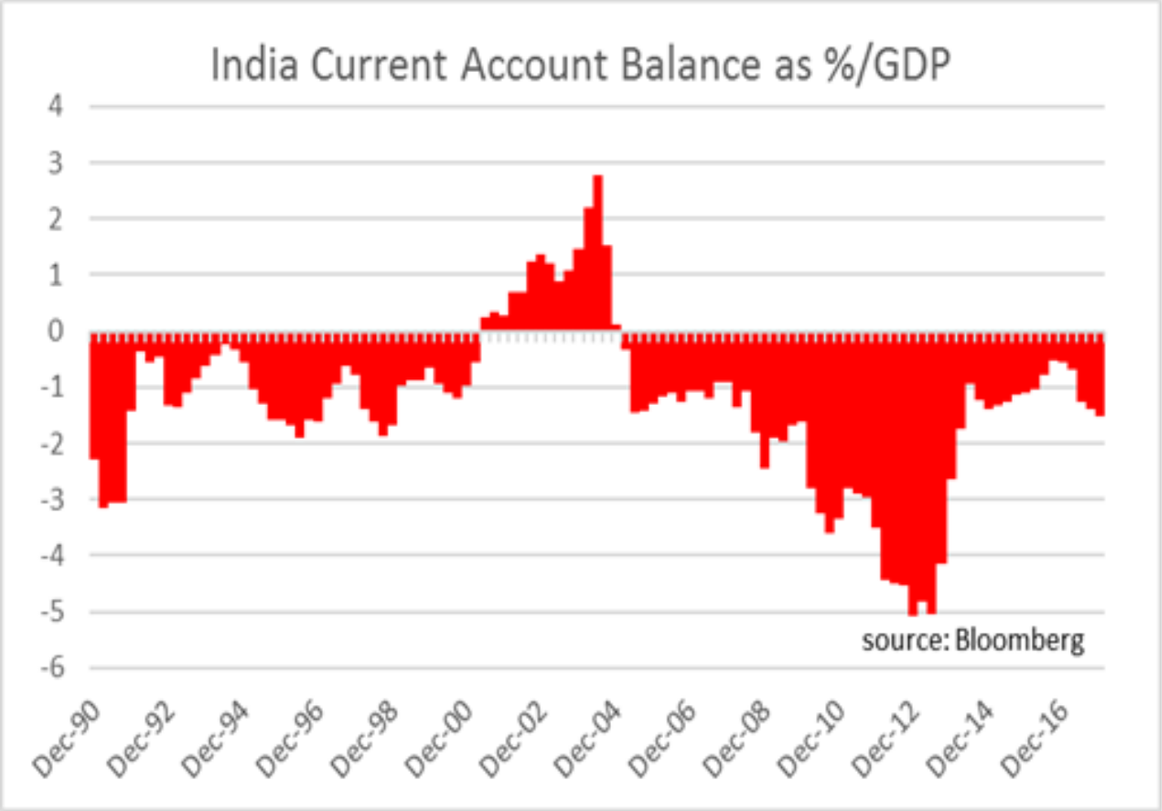
Russia faces demographic problems in the form of a shrinking population and lack of youth although these have been arrested to a certain extent. However, more infants and retirees equals less savings.

Saudi Arabia needs to restructure/transform its economy to deal with a rising (mostly young) population. Vision 2030 is the policy set up to do this. The most pertinent issue here is that it will cost a great deal of money … which most likely equals budget deficits sucking up domestic savings leading to imported rather than exported capital.

For both Moscow and Riyadh, much depends on the oil price and sustainability of high enough prices. US shale oil production is a clear threat here, although there are bottlenecks appearing in the supply chain.



If we run with the argument that global excess savings will begin to shrink, then even with current global savings demand levels, there will be more competition for a shrinking savings pool. To attract capital, higher yields will need to be on offer. However, add in growth financing for say India, then there will be more upwards pressure on yields. India, unlike China through its development, already runs a current account deficit so is already borrowing from the rest of the world to finance economic expansion. There are many other nations that also run current account deficits that will need funds in a world where excess savings might dry up.



To avert, current account deficit nations will need to move to surplus. This will mean some pretty dramatic changes to spending habits … yeah, right!

Back to Index Page

AUD/NZD – Rebound From Multi-Year Trendline Points Higher

Technical Analysis by Andrew Dowdell

- Rallying sharply off 1.0488 after buyers returned near 19-month trendline support.
- Weekly Stochastics have crossed higher from oversold levels.
- The 200-Week MA has flattened out, hinting at a potential reversal of the prior multi-year bear trend.
- Clearance of the 1.0763/1.0861 confluence area will firm conviction that a new trend higher is underway.
- Longer-term, a return to the 2017-15 range highs in the 1.1291-1.1430 area is anticipated.
- Back under 1.0583 threatens further congestion/drift lower.

Resistance Levels		
R5	**1.1430**	2 July 2015 high
R4	**1.1291**	24 October 2017 high, near the 23 March 2016 high at 1.1334
R3	**1.1073**	29 January 2018 high
R2	**1.0861**	12 December 2017 low
R1	**1.0763**	22 March 2018 high
Support Levels		
S1	**1.0583**	13 April 2018 high
S2	**1.0488**	12 April 2018 low
S3	**1.0362**	26 June 2016 low
S4	**1.0238**	14 September 2016 low
S5	**1.0021**	6 April 2015 low

STRATEGY SUMMARY

Watch for a stronger recovery to 1.1291. Below 1.0583 threatens further congestion drift lower.

IFI Research's global team of Technical Analysts constantly look for interesting patterns in prevailing price action of a broad range of currency pairs, fixed income and commodity products. We will highlight the most compelling on these pages. For information on the full spectrum covered, please contact your Account Manager.

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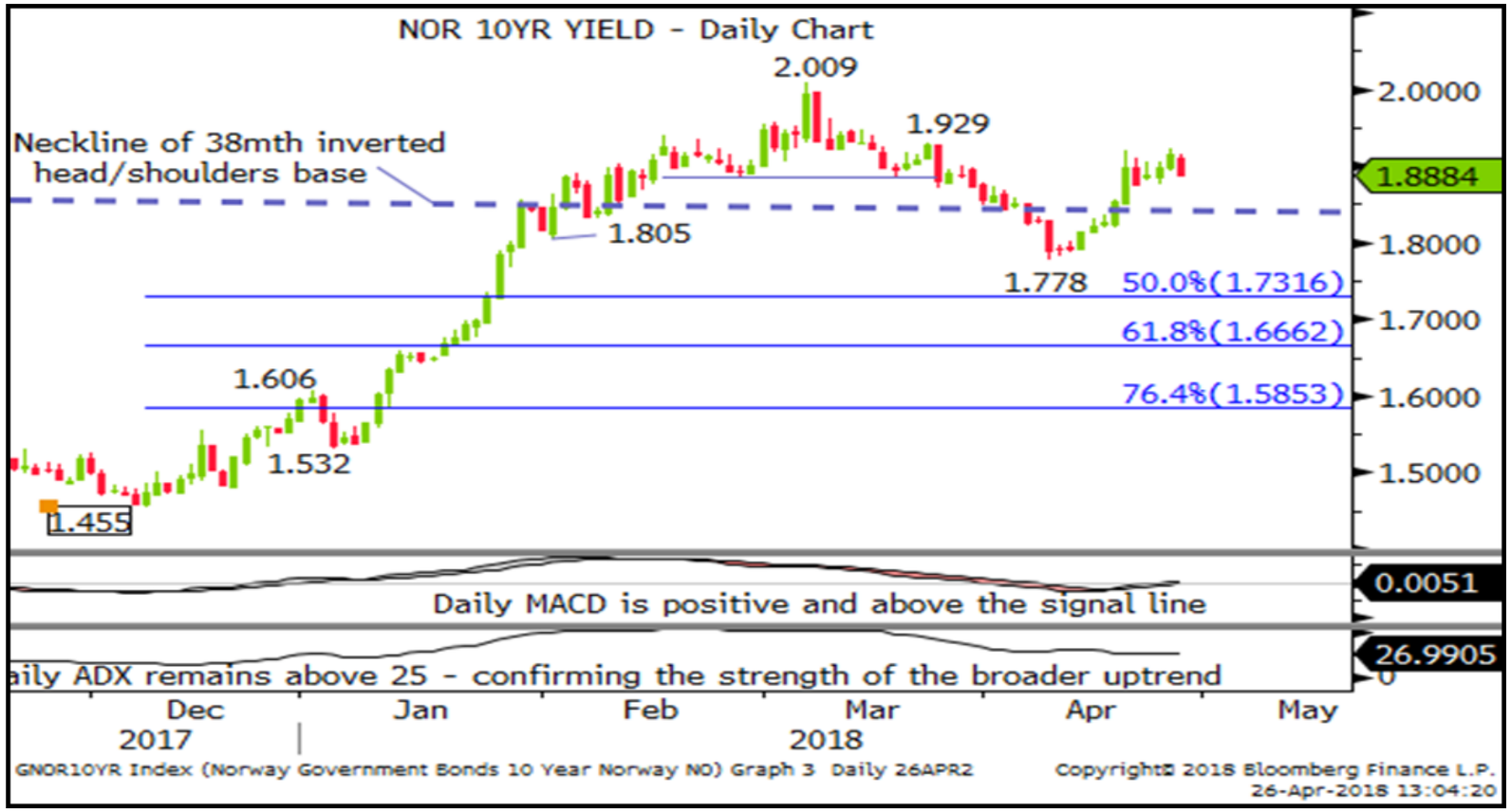
Back to Index Page

Norway 10-Year Yield – 21-Month Yield Recovery Resuming

Technical Analysis by Ed Blake

- Rallied from 1.455 (2017 low) through 1.850 to signal completion of a 38mth inverted head/shoulders base.
- Gains extended to 2.009 (6 Mar peak), before probing back through neckline support to reach 1.778.
- While 1.778 holds, constructive daily-monthly studies suggest a resumption of the 21-month yield recovery.
- A clearance of 2.009 would confirm 1.778 as a major higher low and target Fibonacci levels at 2.093/2.195.
- Only below 1.778 would caution for a deeper near term correction towards 1.699/1.606, before the broader yield recovery resumes.



Resistance Levels		
R5	2.298	3 October 2014 lower high
R4	2.195	27 October 2014 lower high, near .764x 0.864/1.878 off 1.4455 at 2.229
R3	2.093	50% retrace of 3.321/0.864 fall, near .618x 0.864/1.878 off 1.455 at 2.081
R2	2.009	2018 high – 6 March
R1	1.929	21/22 March 2018 highs
Support Levels		
S1	1.778	11 April 2018 low
S2	1.699	7 July 2017 former high, near 61.8% retrace of 1.455/2.009 rally at 1.666
S3	1.606	2 January 2018 former high, near 76.4% retrace of 1.455/2.009 rally at 1.585
S4	1.532	2018 low – 4 January
S5	1.455	2017 low – 7 December

STRATEGY SUMMARY

Buy into any near term yield weakness as we await a resumption of the 21-month yield recovery targeting 2.009/2.093. Place a stop below 1.778.

IFI Research's global team of Technical Analysts constantly look for interesting patterns in prevailing price action of a broad range of currency pairs, fixed income and commodity products. We will highlight the most compelling on these pages. For information on the full spectrum covered, please contact your Account Manager.

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Back to Index Page

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