# Is The Sell-off Overdone?

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## Introduction

Options traders are betting that the worst start to a year for global equities since 2009 isn't yet over, while the MSCI All Country World Index hit a bear market, that is a fall from peak to trough of at least 20%, last week. The decline in the global stocks benchmark reflects the sense of fear that has heavily weighed on risky assets in recent weeks. The 3 main reasons that explain investors' nervousness are cheap oil prices, increasing fears of a global recession and the ability of global central banks to withstand those powerful forces. The sheer magnitude of these forces has left no stone unturned and even weakened credit markets.

**EQUITY INDICES**

| Indices | CCY | YTD-16 | Jan-16 | CY 2015 |
|---|---|---|---|---|
| MSCI World Index | USD | -10.61% | -6.05% | -2.74% |
| MSCI ACW Index | USD | -10.59% | -6.09% | -4.26% |
| MSCI North America | USD | -10.91% | -5.29% | -2.37% |
| MSCI Europe | USD | -11.40% | -6.65% | -5.32% |
| MSCI Emerging Markets | USD | -10.44% | -6.52% | -16.96% |
| MSCI BRIC | USD | -16.21% | -10.02% | -15.68% |
| MSCI India | USD | -14.04% | -6.93% | -7.42% |
| MSCI China | USD | -19.43% | -12.72% | -10.04% |
| MSCI Frontier Market | USD | -5.44% | -6.84% | -17.32% |
| MSCI Asia Pacific | USD | -14.39% | -8.01% | -4.29% |
| MSCI Asia Pacific ex Japan | USD | -11.94% | -7.85% | -11.97% |

** Source: Bloomberg. All above performances are in USD. Data as at 12th February 2016.*

## BRIC leading the fall...

Shares across emerging markets tumbled in January after economic data from China in December showed that the world's largest second economy is stalling (refer to 'China sets an ugly start for 2016…Why? And What to expect?'). Renewed fears of a global economic slowdown and increased market volatility has led the MSCI BRIC to post a return of -16.2% since the beginning of the year. Among BRIC countries, the sell-off was more pronounced in China which recorded a drop of 19.4% so far.

MSCI India lost 14.0% (as at 12th Feb 2016) after a plunge in Chinese equities in January which led to a global rout. Last week, the BSE Sensex logged its biggest weekly fall in over 6 years (-6.6%) after it entered a bear market on Thursday 11th Feb 2016 and is currently trading at 14.6 times its projected 12 months earnings vs. a multiple of 10.3 for the MSCI Emerging markets Index. However Indian stocks rebounded today from its worst week since 2009 on speculation that the global equities selloff was excessive. On the macroeconomic front, India's manufacturing PMI increased to 51.1 in January from a 28 month low of 49.1 in December after all activity indicators recovered from December's flood related contractions. New export orders rose for a fourth consecutive month, from 51.5 in December to 52.5 in January. December inflation rose to 5.6% year on year (vs. 5.4% in November), its fastest pace in 15 months, due to a surge in food cost.

The MSCI Emerging Markets Latin America Index slipped 7.8% as China's slowdown and weak commodities prices continued to weigh on commodity exporters. Brazil's Bovespa lost 8.2% year to date and is among the worst performer in the region. The country is experiencing a growing budget deficit, political turmoil and a deeper than expected recession.

## Japan- More stimulus to salvage the economy

The highlight of the Asia Pacific region was Japan- in an unexpected move on the last trading day of January, the Bank of Japan (BoJ) introduced negative interest rates and indicated that there is room for further rate cut if necessary. Stock markets across the globe rallied on the news but the rally was short-lived, as risk sentiments weakened following renewed selling in crude oil and weak economic data from China which cemented concerns of a slowdown. Over the past couple of weeks, mounting fears of a global recession worsened investors' sentiment and accentuated a sell-off on the Nikkei 225, Hang Seng Index, MSCI Asia Pacific and ASX 200, bringing the YTD loss (as at 12th Feb 2016) to 21.4%, 16.4%, 14.4% and 10.0% respectively.

However on 15th Feb 2016, global stock markets rallied again, rebounding from a 3-year low, led by Japanese shares (Topix +8.0%), HSI (+3.3%) and the ASX 200 (+1.6%) amid speculation that authorities from Europe to Japan will increase stimulus to stabilize global economic growth and that the recent global market sell-off was excessive.

## Central Banks dampens bleeding?

Developed equity markets were not sheltered from the wrath of investors as fears of a global recession strengthened. However actions from central banks helped to alleviate part of the negative sentiment on the equity markets. Towards the end of the January, the European Central Bank and the Bank of Japan surprised global financial markets through a more accommodative stance on monetary policy. The ECB, although it maintained bank rate unchanged at 0.05% and overnight deposit rate at -0.3%, hinted towards more stimulus measures at its next meeting in March to much of the delight of investors. The biggest monetary policy surprise came from the BOJ which imposed negative interest rate of -0.1% on any new excess reserves. These measures were positively welcomed by market participants and led to a rally in equity markets.

However the comfort of central bank accommodation is not as reliable as it once was and resulted in a brief rally. With central banks' tools struggling to stimulate growth, markets remained volatile. This same volatility combined with a collapse in oil prices, the strength of the US Dollar and the impact of a weakening Chinese economy have led the US Fed chair, Janet Yellen, to review the US Fed's stance on increasing interest rates at its March meeting, as previously announced, and to even consider the possibility of negative interest rates shall the US economy enter a recession or another financial crisis.

Rising fears of a global recession amid lackluster global economic data, weak corporate earnings and increasing credit spreads, have led major global equity indices into a bear territory. Among developed economies, Japan's Nikkei (JPY) fell 28.4% since its peak in June 2015, the Stoxx Europe 600 (EUR) and the ASX 200 (AUD) lost 24.6% and 20.4% respectively since their peak in April 2015.

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## Global sell-off extends to the bond market

The risk-off mode adopted by investors since the beginning of January 2016 tilted the balance of funds from riskier assets to safe haven assets. High yield bonds were a hard hit and experienced the largest losses as investors flocked into safer avenues such as gold and sovereign bonds. Since the beginning of 2016, yields on corporate bonds increased as investors sold their stake in riskier corporates while yields on sovereign bonds fell amid increased demand. The 10 year US treasury yield fell from 2.27% to 1.75%, the UK gilt yield slumped from 1.96% to 1.41% and the 10 year German bund yield dropped from 0.63% to 0.26%. Looking forward, dovish actions from global central bankers are expected to weigh on government bonds as these actions reignite the appetite for riskier assets.

**BOND INDICES**

| Indices | CCY | YTD-16 | Jan-16 | CY 2015 |
|---|---|---|---|---|
| Barclays Global Aggregate Index | USD | 3.41% | 0.87% | -3.15% |
| Barclays Global High Yield Index | USD | -3.26% | -1.49% | -2.72% |

** Source: Bloomberg. All above performances are in USD. Data as at 12th February 2016.*

## Crude oil prices hit new lows…

The dynamics of the oil market remain bearish justifying the ongoing slump of the oil price below the $40/barrel level all down to under $30/barrel level in mid-January before ending at $33.36 per barrel on 12th Feb 2016, registering a year-to-date loss of 10.5%. Escalating tensions between Saudi Arabia and Iran, and the resilient production from non-OPEC suppliers aggravated an already heavily oversupplied oil market. Brent crude oil dropped to a new 12 -year low of $27 a barrel on the 20th January, dragged down by the lifting of sanctions on Iran - OPEC's fifth largest member - which should boost oil shipments. Oil prices have yo-yoed since then and witnessed high levels of volatility over recent weeks, rising to $35/barrel at the start of February before hitting $30/barrel on 11th Feb 2016 and rebounding 11.0% a day later.

The sudden surge in oil price was mostly led by talks of possible production cuts from Russia and OPEC, but also aided by figures showing reduction in the number oil rigs from US producers for eight consecutive weeks to lowest levels since January 2010. Flight to safety caused investors to move funds into bonds and gold, with the latter gaining 16.7% since the beginning of the year.

**COMMODITIES**

| Indices | CCY | YTD-16 | Jan-16 | CY 2015 |
|---|---|---|---|---|
| Gold Spot | USD | 16.67% | 5.38% | -10.41% |
| Silver Spot | USD | 13.73% | 2.97% | -11.86% |
| Crude Oil (Brent) | USD | -10.52% | -6.81% | -34.97% |
| Rogers Commodity Index - General | USD | -6.74% | -3.88% | -26.08% |
| Rogers Commodity Index - Agricultural | USD | -3.70% | -1.61% | -14.58% |

** Source: Bloomberg. All above performances are in USD. Data as at 12th February 2016.*

## Is Currency Jawboning Back?

From Zurich to Tokyo, central bankers are turning up the volumes to make it loud and clear that they are unhappy about the extent to which their currencies are appreciating. The Japanese finance minister, Taro Aso, has recently intervened to warn markets that the authorities in Japan are closely watching out for speculative moves as the Yen surged to a 15-month low high on Thursday 11th February 2016. Swiss National Bank President Jordan reiterated that his Bank is ready to intervene to prevent further appreciation of the CHF. The Central Bank's intervention can take any of the following shapes: currency sales, interest rate cuts or monetary stimulus.

Policy makers around the world are voicing out as investors are fleeing stocks, oil, commodities as well as high yield bonds to safe haven assets, amid fears of a global economic slowdown. Asset managers are looking at safe haven currencies as an asset to park their excess cash, thus driving up volatility in the currency market with the potential of harming growth in these countries…

**FOREX**

| | YTD-16 | Jan-16 | CY 2015 |
|---|---|---|---|
| EUR/USD | 3.63% | -0.29% | -10.22% |
| AUD/USD | -2.39% | -2.77% | -10.87% |
| GBP/USD | -1.58% | -3.34% | -5.40% |
| INR/USD | -2.80% | -2.45% | -4.50% |
| ZAR/USD | -2.57% | -2.59% | -25.22% |
| MYR/USD | 3.13% | 3.53% | -18.56% |
| CNY/USD* | -1.25% | -1.25% | -4.44% |
| JPY/USD | 6.15% | -0.76% | -0.37% |

** Source: Bloomberg. All above performances are in USD. Data as at 12th February 2016, except for CNY/USD which reflects data as at 15th February 2016.*

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