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GLOBAL INVESTMENT OUTLOOK 2022

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—VISUAL FRAMEWORK

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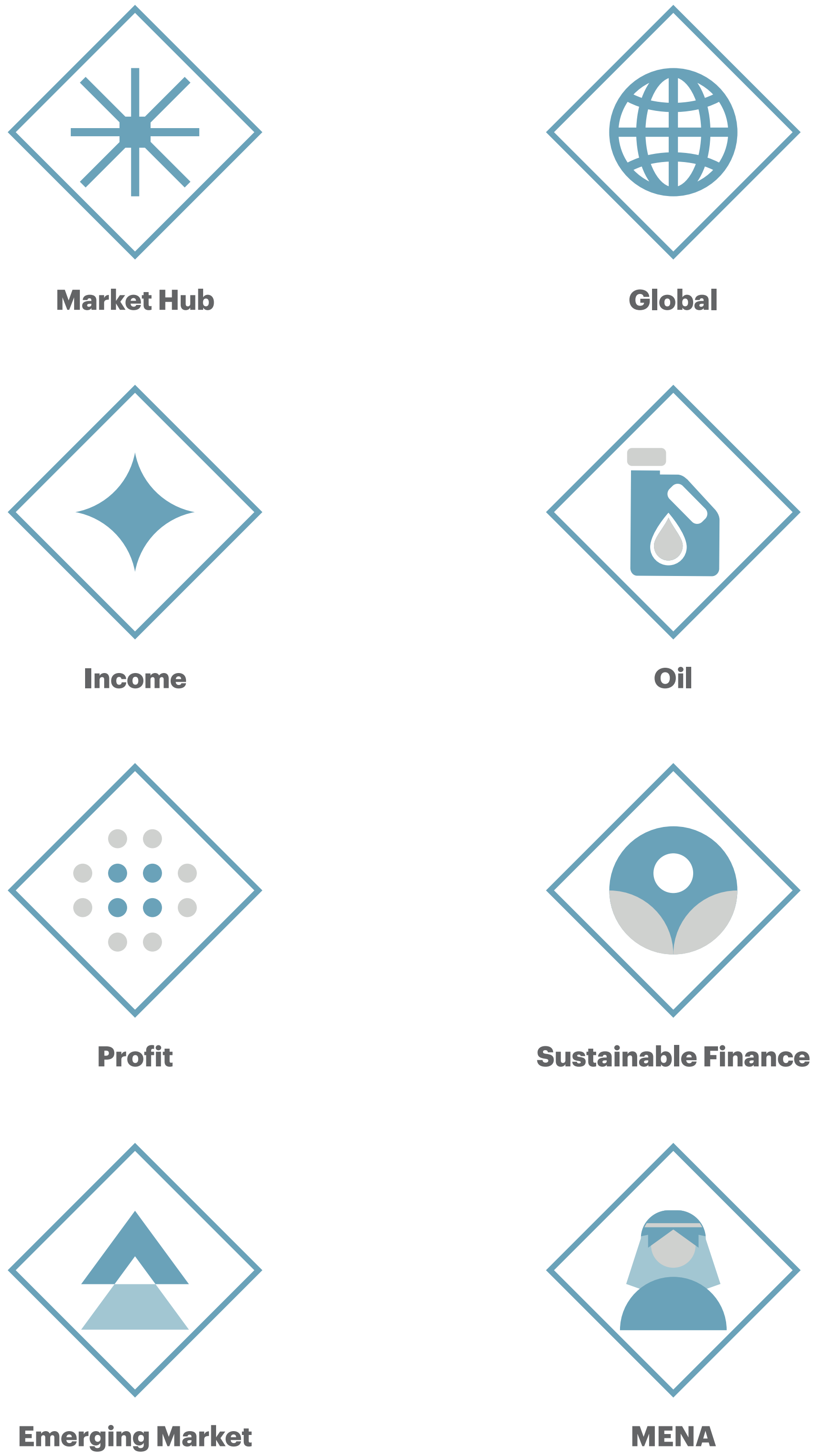


DELIVERING REGIONAL EXCELLENCE
IN CLIENT ADVISORY SERVICES

By Samira Zakour, Head of Global Private Banking and Key Client Group

Welcome to the 8th edition of our annual Global Investment Outlook (GIO). In FAB Private Banking, we are committed to placing our clients first, and to working closely with our investment experts to deliver bespoke advice. Our executives and analysts offer innovative wealth management solutions, derived across numerous geographies – yet drawing strength from them all for the benefit of our clients.

The business of private banking starts with and is about people. Naturally, every analysis regarding risk and reward, time horizons, objectives and how those factors evolve is unique to each client. We also appreciate that investing has become more difficult over the past couple of years, and both us and our have had to become more flexible to adapt to a whole set of unprecedented challenges. However, through all this, we continue to find the best ways to safeguard and grow the wealth of our clients.

As we look ahead to a post-pandemic world, we are still helping clients prepare for future disruptions and the opportunities they may bring. One of them is quite simply the UAE's privileged geographic location. During the pandemic, the world acknowledged that the UAE is one of the best places on earth to be during the pandemic and was reminded of its importance as a global wealth center. FAB intends to continue to leverage on these strengths to look after our clients' interests through whatever 2022 brings, and beyond.

FROM REGIONAL, TO GLOBAL
INVESTMENT EXPERTISE

By Alain Marckus, Head of Asset Management

This edition of FAB's Global Investment Outlook will hopefully act as a roadmap for clients to navigate a world that is returning to 'normal', but which will have undergone some permanent changes. We hope that the following views and forecasts of FAB's experts related to the regional and major global economies, to interest rates, and to many of the key asset classes, will serve, yet again, as a lodestar in what has become a trickier path.

While we have unrivaled views on the global investment context, we continue to offer thought leadership on the markets in the MENA region. That, naturally, includes insightful analysis of the oil market. While FAB is a global bank, our greatest expertise continues to be in our home turf. This year, however, we have widened slightly that remit, opening more space for rising African nations, such as Angola, Ghana, Ivory Coast, Nigeria, Rwanda and Zambia.

We have also addressed some of the questions that permeated several conversations with clients this year, regarding private markets, exchangetraded funds and cryptocurrencies.

We may have gone further than usual this year in our Global Investment Outlook, but more than ever we are especially excited about the road ahead for the local MENA markets, with a special focus on UAE stocks. There is no place like home, after all, and there is no home like the UAE.

THE POST-PANDEMIC WORLD
WILL LOOK DIFFERENT

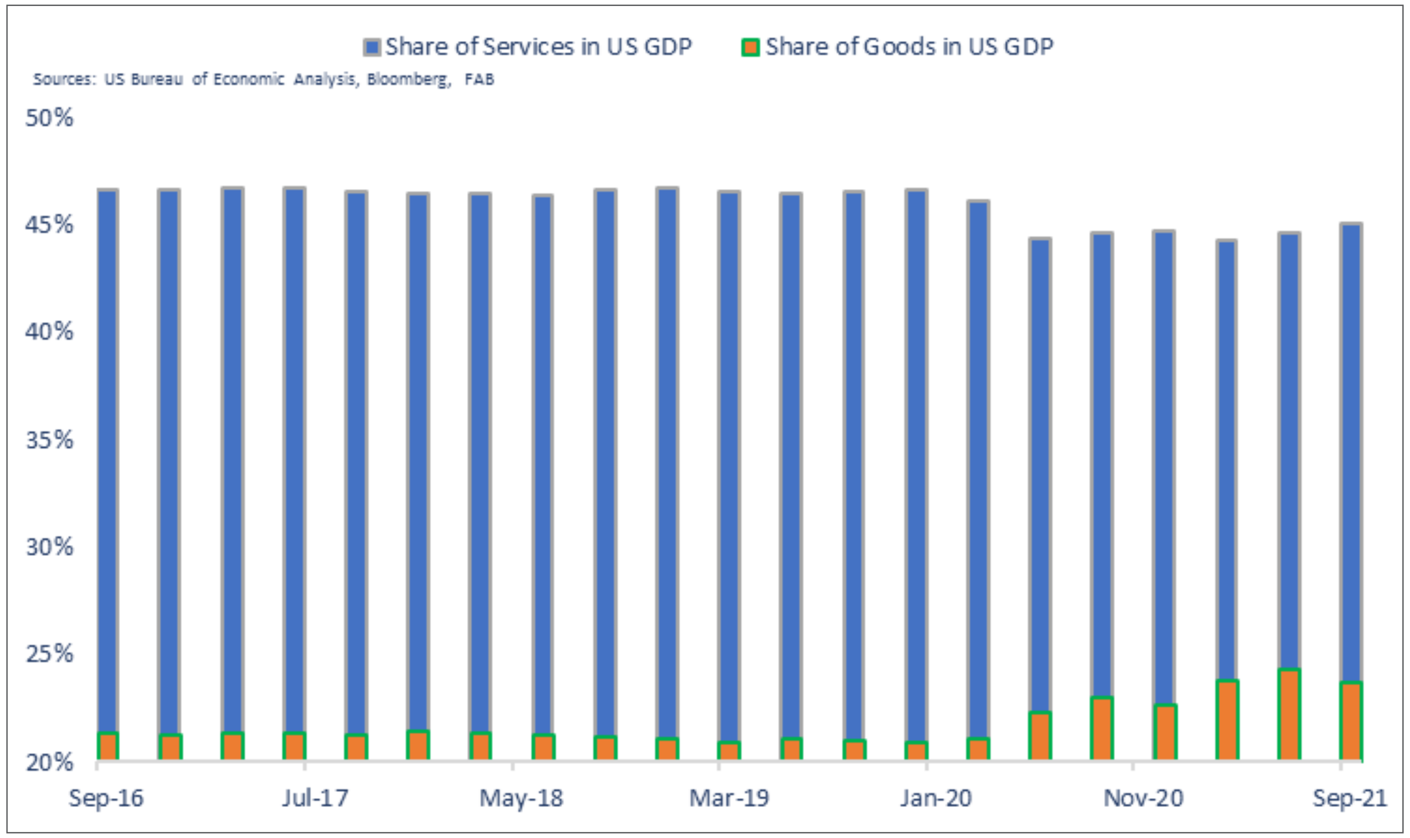
By Chris Langner, Director, Acting Head of Investment Strategy, FAB Private Banking

Around the end of the 1960s, there was a significant turning point in the US economy; the share of services in the country's gross domestic product exceeded the share of goods. In other words, the US moved from being a manufacturing economy to being a services-based one. In the early 1990s, the growing use of computers and the internet accelerated that change.

Between the start of 1991 and the beginning of 2011, the contribution of services to US GDP went from about 39% to 46% according to the Bureau of Economic Analysis, while the portion attributed to goods went from nearly 25% to just over 22%.

In the fourth quarter of 2019, services accounted for 46.6% of US GDP while goods accounted for 20.9%. Then the pandemic happened and, with it, the biggest post-war fiscal stimulus and direct cash transfer programmes in the US. Americans had money in the bank but they could not spend it in restaurants, bars or cinemas so they bought stuff, a lot of stuff.

The result was a temporary shift in the composition of the economy. In the second quarter of 2021, goods accounted for 24.3% of GDP while services represented 44.6%.



Because factories and supply chains had, over the previous 30 years, adapted to their dwindling importance to the economy, they had become more efficient, exploring all kinds of ways to reduce waste, capacity and inventories. The new globalised just-in-time manufacturing systems were not built to respond to a sudden global spike in the demand for goods.

This change, and temporary failure, caused a couple of problems that dominated the investment conversation during 2021. As traditional economic theory suggests, as demand rose faster than supply, prices rose, spurring the fastest US inflation since 1990 in October, a 6.1% year-on-year rise in consumer prices. Such price rises had markets betting that the US Federal Reserve could start hiking interest rates as early as August 2022. As a result, government bond markets had a mostly negative year.

This narrative was not exclusive to the US. In several countries, from large emerging markets such as Brazil to key advanced economies such as Germany, inflation hit multi-decade highs as people spent unprecedented amounts of money as a result of fiscal and monetary stimuli. While the European Central Bank and the Federal Reserve could afford to wait and see whether the reversal of the supply chain and manufacturing shortfall issues would slow down consumer prices, emerging market regulators did not have the same luxury.

Russia increased its benchmark rates by 325 basis points in 2021 as of November, and Brazil hiked its rates by 575 basis points. Given year-on-year inflation rates of 8.13% and 10.67% in Russia and Brazil respectively in October, chances are that the two central banks are going to keep on hiking their rates into 2022. The same is true for several other large emerging market central banks.

And some, such as Singapore, Australia and China, which have not dealt with the inflation, partly because their economies have not reopened fully, will probably face a similar problem at some point in 2022. However, because the economies of Asia are much more skewed to the production of goods than the consumption of services, they benefited from the reopening of the West and are likely to face lower inflation as a result of their own return to normalcy.

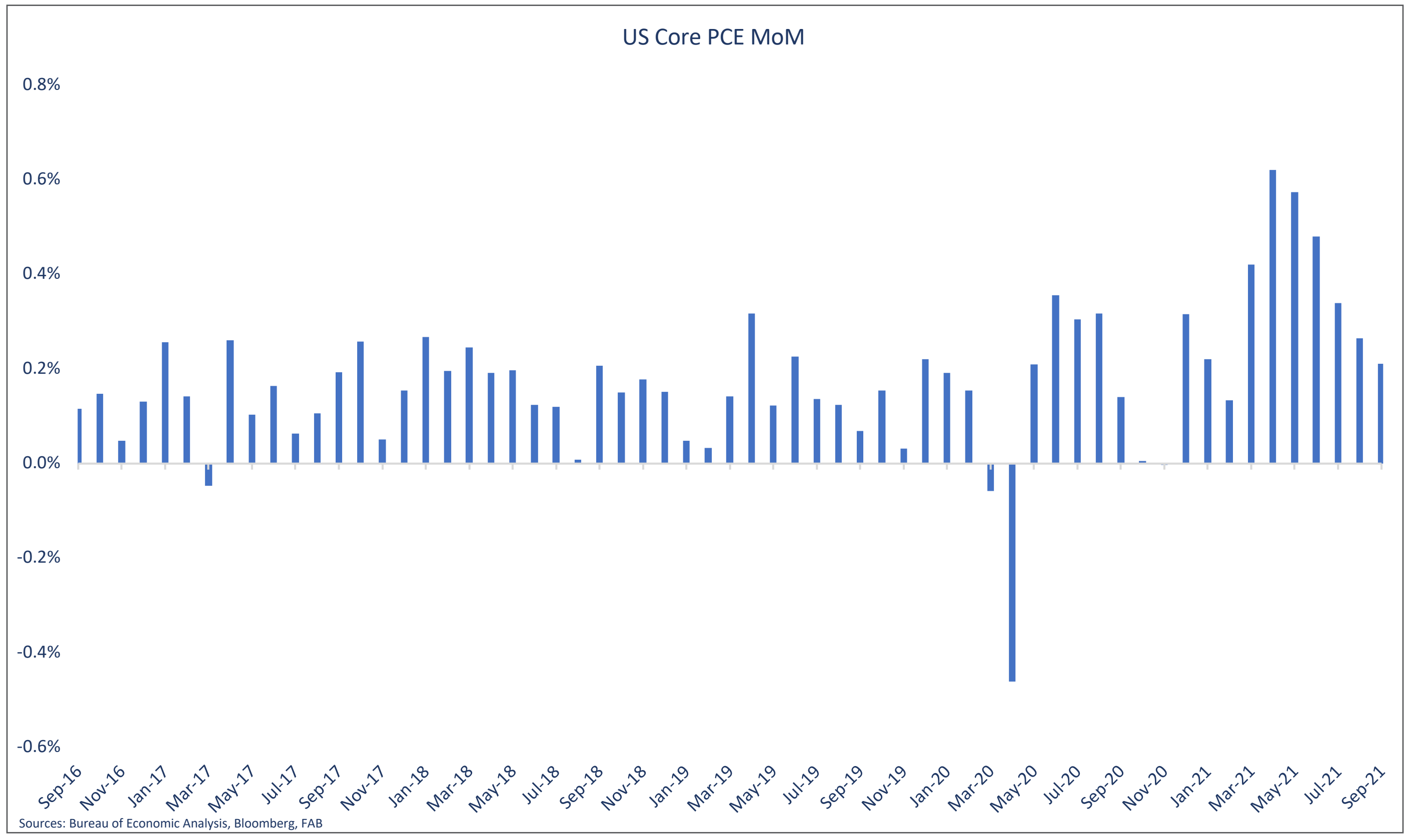
As things go back to normal, supply chains that were disrupted will return and inflation could fizzle out quickly. In fact, the significant effort that factories across the world made to produce more and faster to meet the spike in demand could turn the supply shortfall that marked 2021 into a glut in 2022. If this happens, inflation could very easily fall below the targets of central banks in developed countries.

Emerging markets, however, may see inflation that is a bit stickier. One of the key inputs of consumer price baskets in emerging markets is food. Because energy prices were so high in 2021, particularly for natural gas, fertiliser costs went up significantly, leading many farmers to reduce or even skip the use of fertilisers altogether. This suggests crop yields could remain low in 2022 after two years in which they were impacted by COVID-related issues.

Ultimately, however, the proactive stances of central banks in emerging markets are likely to slow their economies enough that inflation could subside. It may not be just central banks that start to reverse the profligacy that marked the pandemic period. Governments may also be forced to rein in spending as debt burdens have ballooned, and, in some places, they have already started doing so.

The combination of both these forces, tighter spending and higher local rates, could make local emerging market currencies and government bonds attractive to international investors again at some point in 2022, probably in the second half of the year. When this time will come will depend on the evolution of inflation and central bank activity in emerging markets.

Naturally, the key question will be how aggressively the Federal Reserve (and by proxy the ECB) withdraws monetary accommodation in 2022. Emerging markets usually suffer when US interest rates are rising.



There is reason to believe the Fed will be cautious about how fast it hikes rates. The composition of the rate-setting body, the Federal Open Market Committee, for one, is likely to become even more dovish, especially in a year when the hold Democrats have on Congress could be lost.

The US economy is also likely to decelerate further in 2022 given that the economic high of fiscal stimulus equating to 25% of GDP will have waned. In fact, while US personal savings hit an all-time high of US$ 6.4 trillion in April 2020 as a result of the first rescue package in the US with, another peak in March 2021 after the last rescue package, they were back at US$ 1.3 trillion in September, a number only slightly higher than the US$ 969 billion average in the decade preceding the pandemic.

This drawdown in savings means that US consumers, who have been among the drivers of the highest inflation rates in 30 years, have run out of extra cash to buy stuff. And, as the economy reopens fully, they will spend more on sandwiches at the office and dinner dates, shifting the GDP back into kilter.

While the share of US (and global) GDP derived from services is likely to go back to what it was before the pandemic, some changes are probably permanent. The increase in productivity from the wider adoption of certain technologies that allowed people to work from home now during the pandemic is likely to persist. The more common practice of working from home also increased productivity in the economy, as the second quarter of 2020 showed in numbers. This may continue and it will have an impact on several asset classes, from the stocks of technology companies to the price of commercial real estate.

All this, along with a perhaps tighter fiscal policy (if President Joe Biden is able to increase wealth and capital gains taxes), could mean less inflation this year in the US. And, if that does happen, Federal Reserve Chairman Jerome Powell will have proven prescient in saying that the Fed could afford to wait and see whether inflation really stuck around.

Naturally, if this scenario proves entirely wrong, the Fed will simply increase rates faster to fight inflation. In this case, risk assets could suffer temporarily but they will then become even more attractive. For so many reasons, the inflation boogeyman could very well be just last year's nightmare by the end of 2022.

*Click **here** for the disclaimer.*

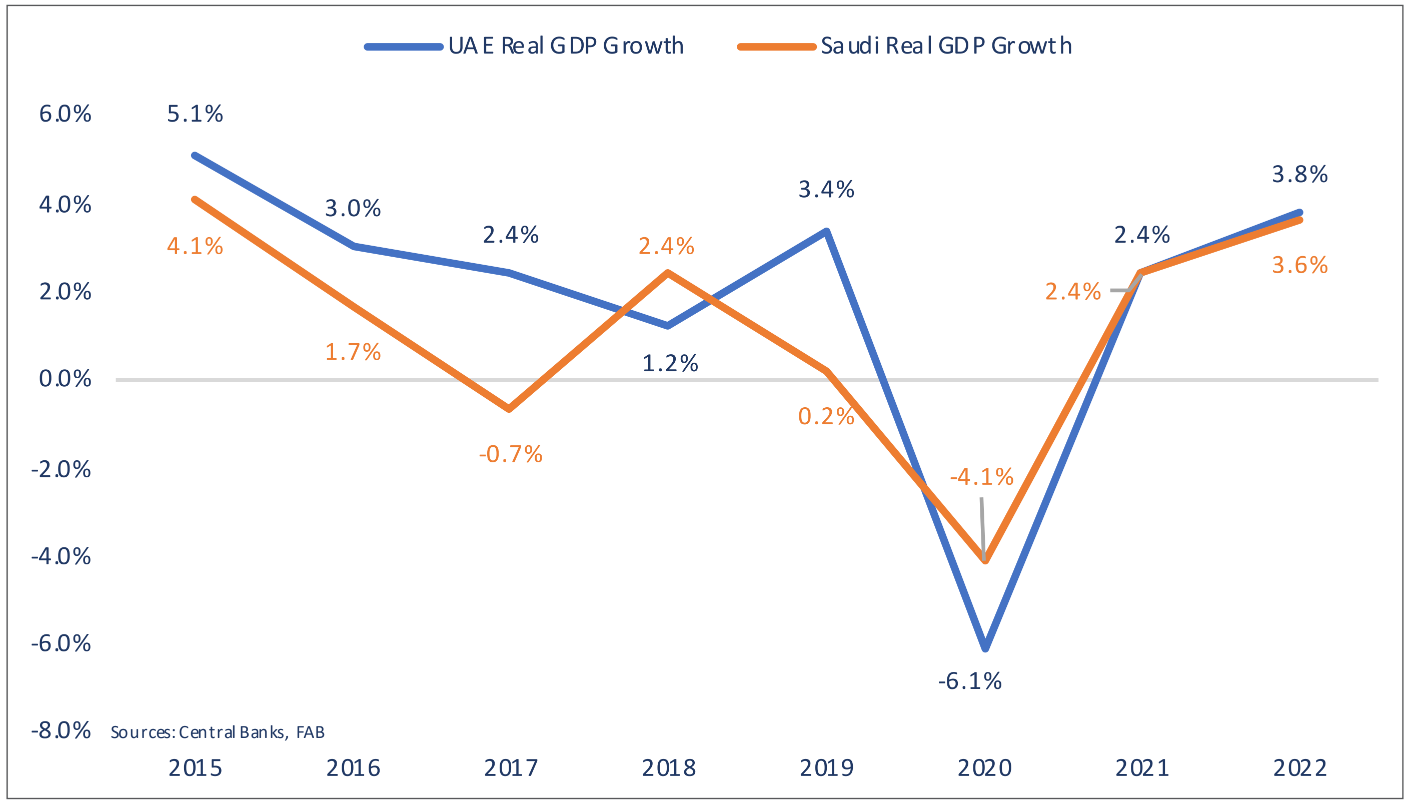
DEVELOPMENTS IN MIDDLE EAST AND AFRICA

GCC MACRO OUTLOOK 2022:
FROM TROUGH TO PEAK AND BACK TO U

By Simon Ballard, Chief Economist, FAB Market Insights and Strategy

After the anticipated rebound in economic activity across the Gulf Cooperation Council (GCC) region in 2021, when growth recovered sharply from the recessionary nadir of the cycle in Q2 2020, the six GCC countries should see further positive advances in economic growth in 2022. Beyond that, we anticipate an easing in the rate of improvement and that the trajectory of the medium-term economic advance will be more of a 'shallow U shape' in nature. We believe that this will be the most sustainable outcome for reflation across the region.

UAE vs KSA GDP 'It's all about U'

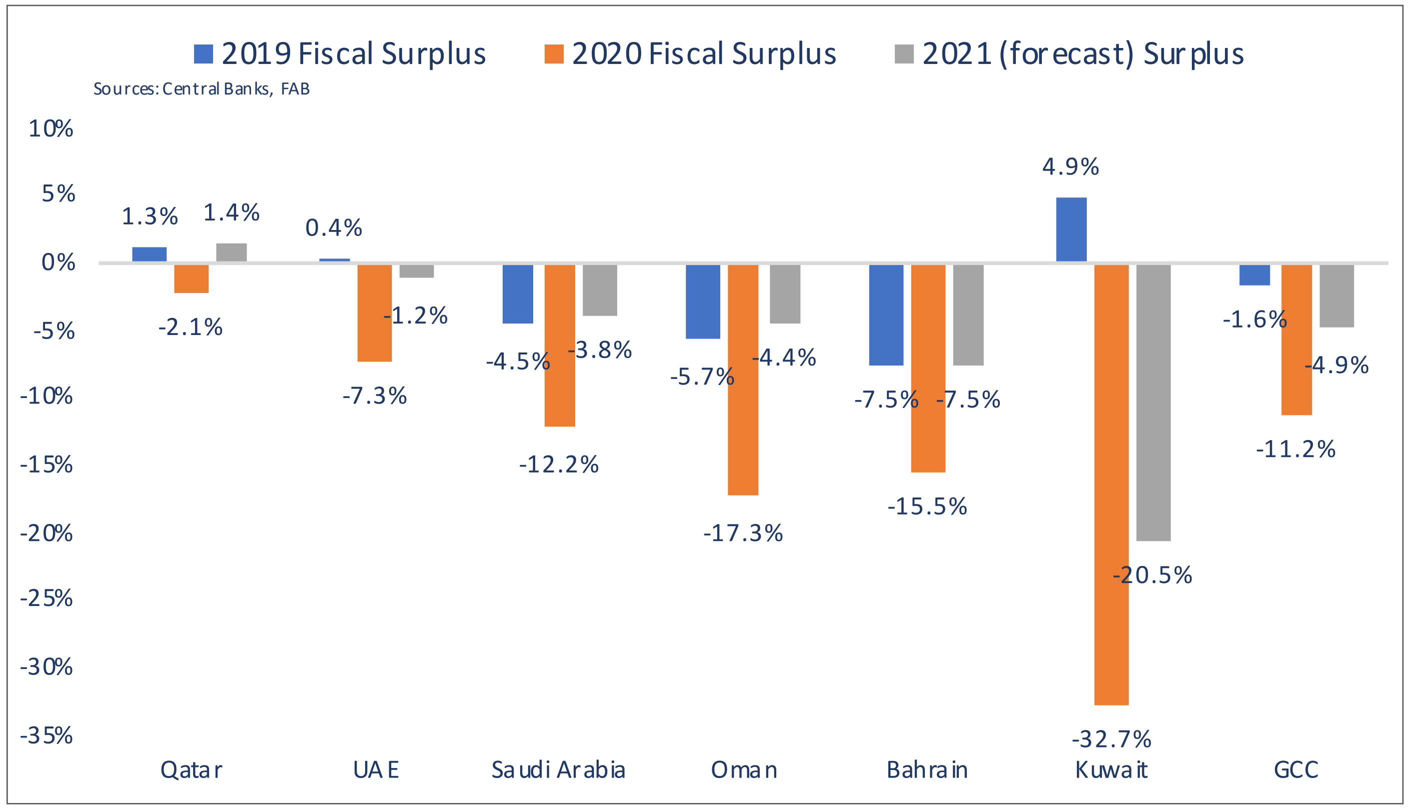


Economic performance across the region is forecast to strengthen as a result of the widespread vaccination programme that has helped to revive domestic activity and consumption and supported the re-opening of tourism -- which is particularly important to the United Arab Emirates (the UAE) --, and of the implementation of deeper structural reforms.

On balance, we believe that the aggregate GCC economy expanded by 2.1% during 2021. As global reflation continues to gain cautious momentum over the coming months, GCC economic growth should improve further and settle around a 4.4% growth rate for 2022. In the context of OPEC+ oil production cuts possibly ending by mid-2022, we assume that the private sector will be particularly important to the overall annual economic growth rate, particularly in Saudi Arabia (KSA), the UAE and Qatar.

With oil prices remaining buoyant, the fiscal and external sovereign positions in the region are expected to improve substantially over the coming years; the UAE and KSA expect their fiscal deficit positions of 2021 to move back towards balance or into surplus during 2022. In aggregate, we believe that while the fiscal deficits of KSA, Oman and Bahrain should continue to narrow during 2022, the fiscal positions of the UAE, Qatar and Kuwait should improve and return to a (small) surplus over the coming months.

GCC government fiscal balance positions 'The post-pandemic (gradual) road to recovery'



That said, at least across the major economies of the UAE and KSA, we expect to see the maintenance of modestly expansionary fiscal strategies that will be made possible by the large financial buffers, spare capacity and enhanced government revenues from firm oil prices.

As is the case in many regions around the world at present, inflation will remain a key threat to the monetary and fiscal status quo across the GCC during much of early 2022. However, while elevated commodity valuations will bolster price pressures, we continue to subscribe to the view that the latter will begin to recede as 2022 evolves and as we move further away from the inflation low point seen in the first half of 2020.

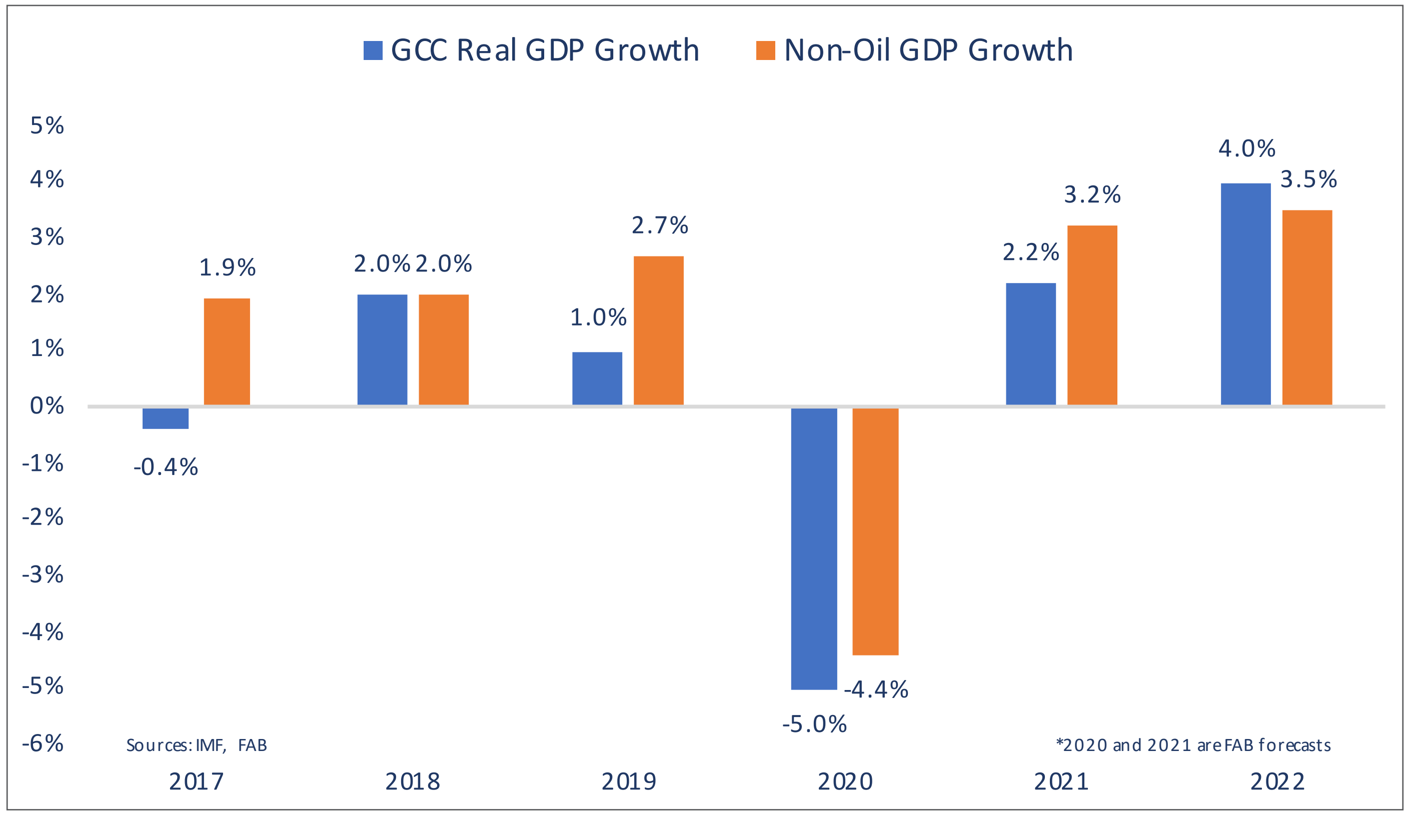
Moreover, we would conjecture that generic inflation pressures should remain relatively contained over the coming months as a result of pegged exchange rates across the region (with the exception of Kuwait, of course). Inflation can vary greatly from member state to member state though, albeit running on average between 2%-3% in 2021, buoyed by the strength in the oil price. Consequently, we do not anticipate any change in GCC central banks' policy rates during 2022; they will remain anchored to and continue to track US rates.

Structural reform will remain a key focus for governments across the region and a key foundation for improving economies during the coming year in the wake of what has unarguably been major progress on that front over the past several years. We have seen some major improvements in the business environment, including the promotion of a more favourable regulatory landscape across much of the GCC region in recent years and this, coupled with an acceleration in digital transformation, should help to further bolster the outlook for businesses and SMEs in the region. Similarly, strategies to promote new investments, including the relaxation of residency rules and longer-term Golden visas for expatriates, should help to enhance the UAE's status on the global corporate stage and to promote the country as a global hub for business and finance and an attractive tourist destination.

That said, there is a clear need for further reforms across the region, particularly across the non-financial sectors. While the GCC's financial environment continues to look robust to us, benefitting from a high-quality asset base, strong capitalisation and adequate liquidity, in the non-financial space, reforms will be key to achieving individual countries' economic diversification aspirations, but they will also serve as the foundations for improving and sustaining economic growth rates over the medium-term.

At the country level, Moody's Investors Service affirmed its A1 long-term issuer and senior unsecured ratings for Saudi Arabia on November 5th, 2021. At the same time, Moody's revised the outlook from negative to stable. To us, this reflects what we have long held as a positive macro fundamental outlook for the major GCC sovereigns (KSA and the UAE) through 2022.

GCC GDP growth trend
'A cautiously optimistic horizon'



Indeed this structural strength was also reflected in Fitch's affirmation of the UAE's AA credit rating in November, 2021, with the agency attributing the rating of the federal government to the country's moderate consolidated public debt, strong net external asset position and high GDP per capita. Recognising the ongoing global macro challenges to the reflation narrative, while we generally expect GCC sovereign fundamentals to remain robust over the coming years, which in turn will help to drive improving FDI flows into the region, we do anticipate a degree of continuing consolidation in growth rates during these still early stages of rebound from the economic nadir of the pandemic.

And, in this respect, we also note the subliminal risk to the outlook that could stem from any weakening of fiscal discipline if higher oil prices were to result in complacency, especially if it were to coincide with a weakening in the pace of economic growth. While inadvisable, this is a pro-cyclical strategy that one might be sympathetic to at the time and one that we have seen evidence of before, although (the UAE and KSA) governments do seem committed to medium-term fiscal responsibility as they aim to redress the costs and ballooning public debt incurred during the pandemic.

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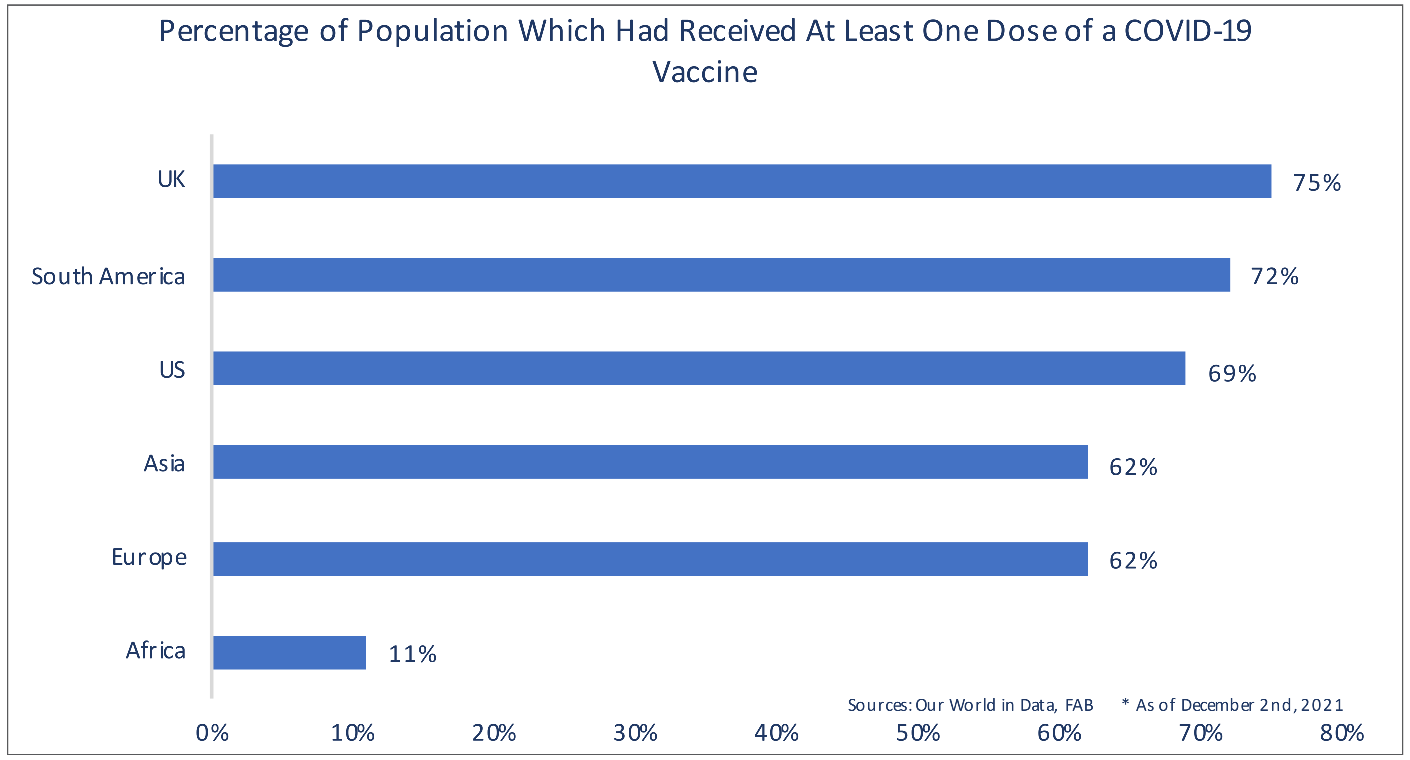
CRUDE OIL MARKET OUTLOOK – 2022

By Glenn Wepener, Executive Director & Senior Strategist Middle East & Africa

Known Unknowns

The World Health Organization's announcement of the discovery of the 'Omicron' COVID-19 variant in November last year reminded us that the battle to end the pandemic is not over just yet. At the time of writing, this variant, although more transmissible, appears not to be as deadly as first thought although, yet again, it highlights the fact that the developed world still needs to do much more to ensure that poorer countries are provided with sufficient supplies of the vaccine as soon as possible. This would reduce the number of deaths, but also the risk of further mutations.



At the same time, COVID-19 is not the only uncertainty to bear in mind when deliberating on an oil price forecast for the year ahead. For example, indirect talks between Washington and Tehran over a potential return to the JCPOA Nuclear Accord restarted last month, although admittedly many analysts believe that the chances of a deal being reached remain around 50/50. Separately, the risk of a major crude supply disruption in fragile countries like Libya remains high, while a rebound in output from the US shale oil patch has been rather sluggish this past year. But will this situation continue in 2022? We discuss these and other key issues to watch in more detail below.

Demand & Supply

According to the EIA's latest 'Short-Term Energy Outlook', which was published in December 2021, the agency estimates that 96.91 million barrels/day of petroleum and liquid fuels were consumed last year, while production averaged 95.63 million barrels/day. The agency expects the market to flip back into a small surplus in 2022, albeit a slim one. OPEC has similar forecasts, anticipating global demand to rise to 100.59 million barrels/day.

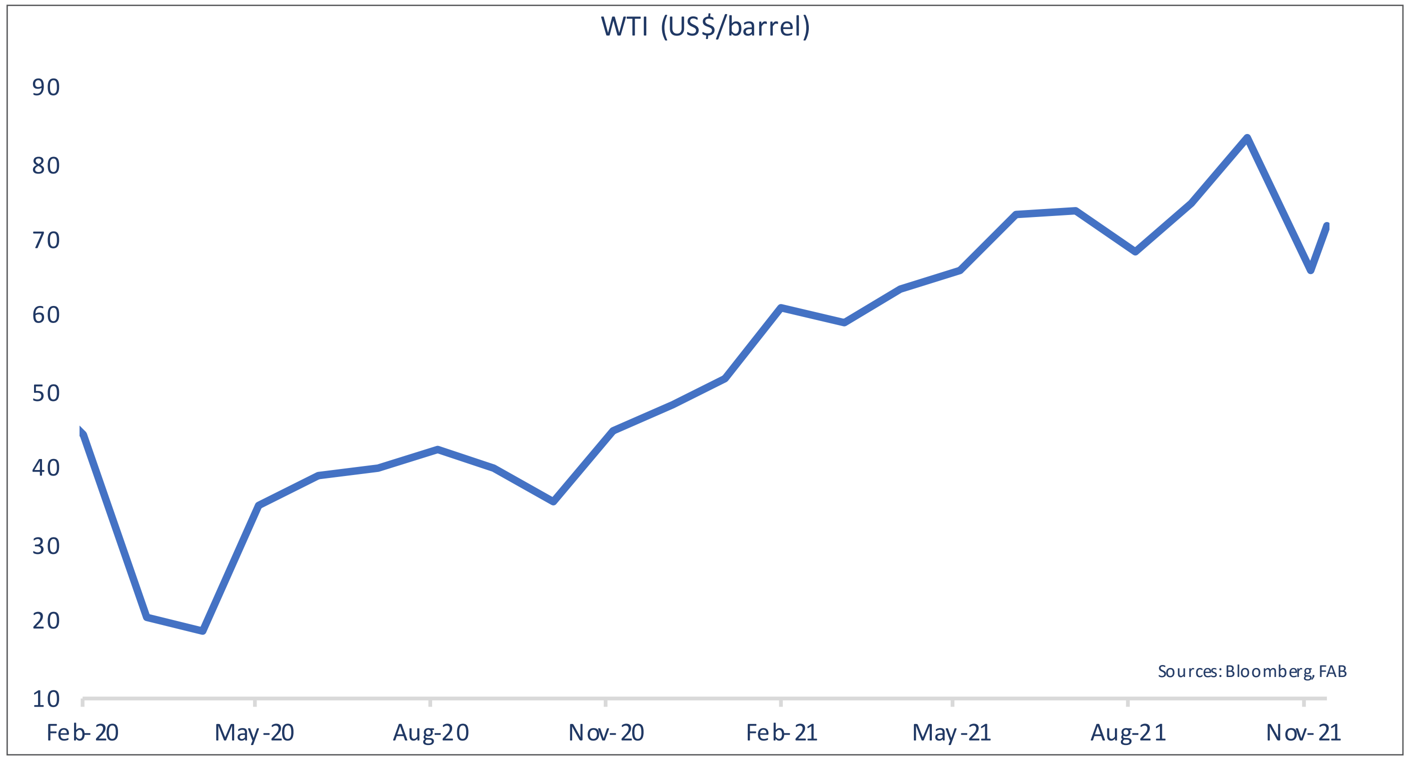
	2020	2021	2022
Total Global Production	93.84 million barrels/day	95.63 million barrels/day	100.93 million barrels/day
Total Global Demand	91.81 million barrels/day	96.91 million barrels/day	100.46 million barrels/day

**December 2021 EIA estimates*

The resumption of the OPEC+ output cut accord (along with the appearance of COVID-19 vaccines) was instrumental in driving the rebound of crude oil prices in 2021 and helped to reduce the overhang in global inventories which are now mostly back below their five-year average. Close adherence to the terms of the agreement by the majority of its signatories has been key to its success and, at their final official meeting for 2021, the grouping agreed to keep their current production schedule in place, while stating that they were ready to act 'at any time' should market conditions change dramatically.

Their decision to continue to follow a cautious approach and not increase production at a faster rate when oil moved above US$80/barrel in November 2021 (despite calls from the US and other major consumers to do so) turned out to be prescient. Just a short time later, the discovery of the more infectious Omicron variant immediately led to fresh travel restrictions and tighter movement guidelines across a number of countries, which in turn saw WTI crash back below US$70. If OPEC+ keeps to their current schedule in the months to come, it means that they will continue to add 400,000 barrels/day to the market until April 2022 when certain members will have their allocations raised slightly for the subsequent months, and then by September the cuts will have been phased out completely. However, one issue to watch will be the performance of two major African producers, namely Nigeria and Angola. They are both still struggling to raise their crude output to even reach their current allocated limits due to various factors, including underinvestment over the past decade and ongoing maintenance problems.

In the US, an overall production increase was relatively sluggish last year when compared to the jump in WTI prices. This is due primarily to the fact that North American shale firms were forced to focus more on costs than output in 2021 following the collapse in crude prices the previous year, which had also driven a number of them into 'Chapter 11' bankruptcy. This situation means that a return to the record US production level of 13.20 million barrels/day achieved in February 2020 is unlikely to be repeated, however the EIA does expect the country's output to rise to 11.85 million barrels/day this year, from an average of 11.18 million barrels/day in 2021.



A Chinese Puzzle

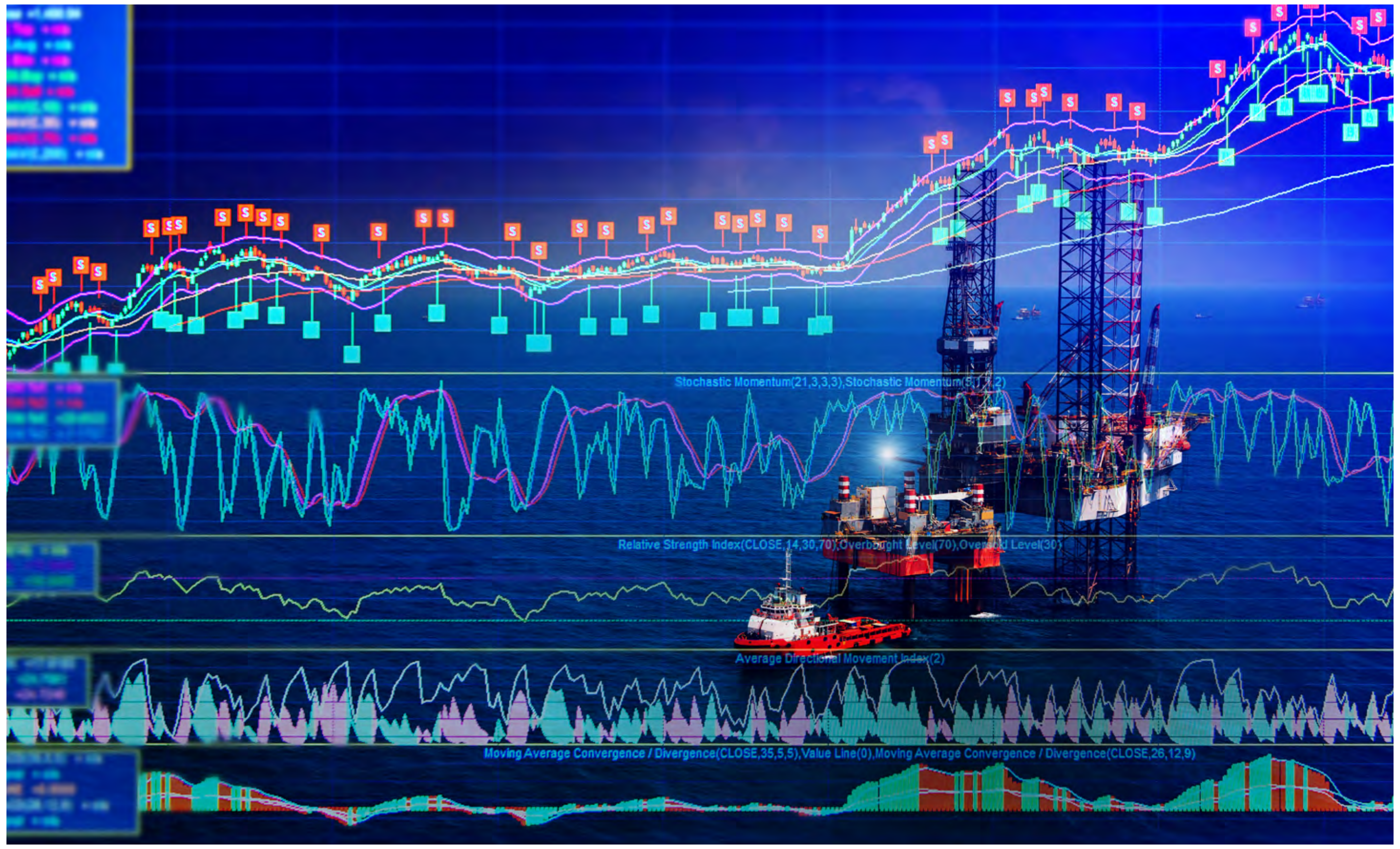
The ongoing reopening of the global economy (especially the travel sector) will continue to support oil demand in 2022, with China, the US and India retaining their positions as the world's top three consumers. However, after many years of breakneck growth and a reasonably quick rebound out of the pandemic, China has been recording more subdued economic data over the past few months. In December last year, this slowdown led the PBOC to reduce its reserve requirement ratio for banks by 0.5 percentage point in another attempt to lower overall financing costs and provide a boost to businesses. The Asian giant is currently battling a number of issues aside from sporadic localised outbreaks of COVID-19, an ongoing trade dispute with the US and the recent property market slump. For example, its natural resources are in decline, which in turn has raised the amount of capital that needs to be invested in order to generate growth. This was highlighted in an official survey published late last year, which calculated that the country's total arable land had shrunk by almost 6% between 2009-2019 compared to the previous decade, due primarily to rapid urbanisation. This could be one of the reasons why China has overtaken both the EU and US to become the world's largest importer of agricultural products. Meanwhile, its working population is shrinking sharply due in part to its former 'one-child' policy, and this situation was underlined in an official government census report published in May 2021. This showed that China's population growth over the past 10 years was the weakest on record, while the number of citizens who are 60 years of age or older has increased to almost a fifth of the total population. Admittedly, Beijing is trying to reverse this trend by amending the child quota for couples, which was raised again last year from two children to three, but these actions will take time to have a material impact.

Of course, these are also symptoms of a maturing economy and so the heady years of an 8%-10% average growth rate appear to be over, with the IMF now predicting China's GDP expansion to be 5.6% in 2022, slipping further to 5.1% by 2025. Lower but more sustainable and inclusive growth in China is a good thing in the long-term, but it will also mean that their crude purchases may not continue to be at the same levels to which we have become used up to now.

CAPEX Conundrum

As we highlighted in the previous GIO, the continuing low level of capital expenditure going into finding and developing new sources of conventional crude oil is potentially laying the ground for a major supply gap in the not-too-distant future. In an article published in July 2021, the Chairman of Wood Mackenzie, Simon Flowers, warned that the amount of CAPEX directed towards upstream oil and gas projects is now down around 50% compared to 2014.

One of the primary drivers behind this is the push towards renewable energy, and the increasing pressure on international oil companies (from both governments and activist investors) to focus more on reducing their carbon emissions and redirecting funds towards clean energy projects. While reducing fossil fuel emissions is an admirable cause, and something that does need to be prioritised in light of the already very visible impact of climate change, it is not a simple straight line and needs to be done in a balanced manner. If it is not, then the world could face regular socioeconomically damaging energy shortages on the road to a greener future. This issue was raised recently by the CEO of Saudi Aramco, Amin Nasser, who was quoted by the Financial Times late last year succinctly stating, "I understand that publicly admitting that oil and gas will play an essential and significant role during the transition and beyond will be hard for some. But admitting this reality will be far easier than dealing with energy insecurity, rampant inflation and social unrest as the prices become intolerably high and seeing net-zero commitments by countries start to unravel". This underinvestment in the conventional oil sector is also putting pressure on spare production capacity, and although there are some exporters such as the UAE and Iraq which have been busy in recent years expanding their ability to increase output, the estimated level of readily-available excess supply has shrunk over the past 12 months. This was highlighted in an IEA report published last October, which suggested that the margin of spare capacity could slip below 4 million barrels/day by the second quarter of this year. A major unexpected and sustained output disruption, such as when Hurricane Ida knocked out production in the Gulf of Mexico last year, could quickly eat into that slim buffer.



Geopolitical Fault Lines

There are various geopolitical risks that could impact the oil market now and in the future. In this section, we will focus on two of these, namely the situations in Iran and Libya, which are both still live and ongoing.

1. The seventh round of indirect talks between the US and Iran on a possible return to the JCPOA agreement restarted last month, but had not made any fresh progress at the time of writing. In fact, the new Raisi administration in Tehran has reportedly stepped back from some of the key compromises made by Iranian negotiators during the first six rounds of discussions, and submitted new demands such as the immediate lifting of US sanctions and a guarantee that no new measures will be imposed on Iran in the future. Despite these major hurdles, an eventual deal cannot be ruled out completely just yet, especially as it appears that the Biden administration remains keen to revive the accord while, on the other hand, Iran's economy desperately needs sanctions to be removed. If an agreement is reached, it would have an almost immediate impact on the oil market. This is because Iran is believed to have around 200 million barrels of crude stored both onshore and offshore according to Reuters, and thus up to 1 million barrels/day could be released over a six-month period, something that is not currently priced in. Conversely, should the talks collapse and Iran continue to pursue its uranium enrichment programme above the limits set within the 2015 accord, then the risk of a direct confrontation rises, although we feel such an outcome remains at the lower end of probability with indirect actions such as increased cyber warfare more likely.
2. In Libya, oil production rebounded from a record low of less than 100,000 barrels/day in 2020 to more than 1.2 million barrels/day in 2021 following the ceasefire agreement. Meanwhile, Fitch Ratings estimates that the country's real GDP expanded by 42% last year from a 36% contraction in 2020. Legislative elections are due to take place in January this year and the hope is that they will proceed peacefully, however, the political and security situation on the ground remains fragile and thus the risk of fresh disruptions to crude output there remains high.

Conclusion & Forecast

As outlined above, there are both potentially strong headwinds and tailwinds facing the oil market in 2022. On balance, we expect oil's generally bullish tone to remain in place, and warn that the ongoing issue of lower capital expenditure on conventional production in the years ahead could eventually trigger a major gap between global demand and supply. Despite the predicted slowdown in China – and barring a major reversal in the war against COVID-19 – we expect Brent crude prices to remain healthy in 2022 and to average US$75/barrel.

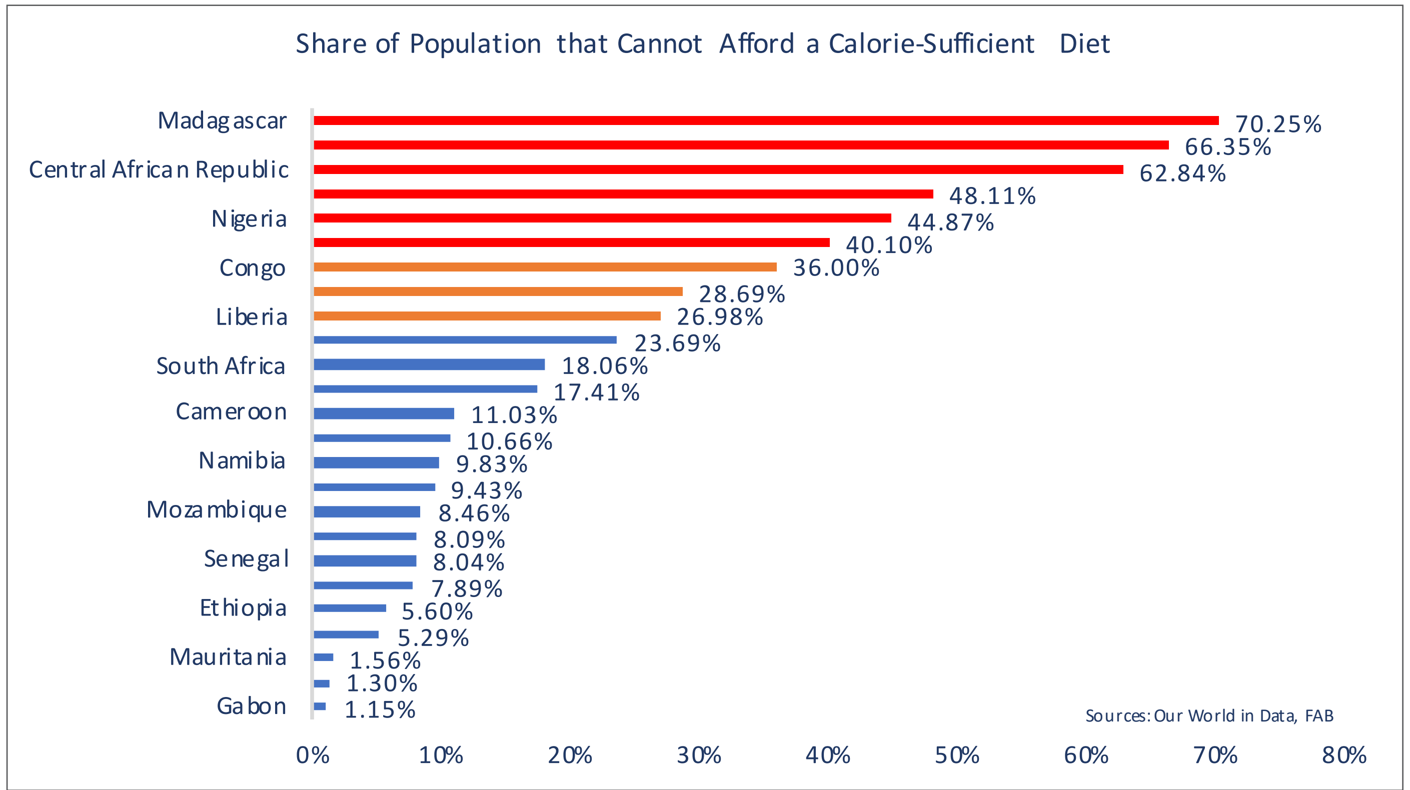
SUB-SAHARAN AFRICA

'ONES TO WATCH'

By Glenn Wepener Executive Director & Senior Strategist Middle East & Africa

The term 'African Renaissance' was first coined by the Senegalese historian Cheikh Anta Diop in essays he wrote between 1946 and 1960. Later, it became a more mainstream mantra after the former South African President Thabo Mbeki used it in an effort to promote political, social and economic renewal, both in his own country and across the world's second largest continent in the late 1990s. Since then, the outcome has been mixed; some countries (such as Rwanda) have made real progress over the past two decades, while others have edged backwards due to various factors including poor governance, corruption, war and climate change.

The latest challenge for African governments to overcome has been the impact of COVID-19, especially as only an estimated 6% of Africa's population had been fully vaccinated at the beginning of November 2021. The pandemic worsened inequality across the SSA region and this, combined with a record rise in basic food prices, poses a real threat, especially to the more fragile states (see chart). These issues aside, the rebound in global trade, the ongoing commodities boom and the recovery of the tourism sector should provide a boost to a number of African economies in 2022, while the continent's young population, along with an increasing adoption of digital services in the consumer banking, agricultural, education and healthcare sectors (led by the already sizeable uptake of mobile technology), provides hope for more sustainable and inclusive economic growth over the next decade.

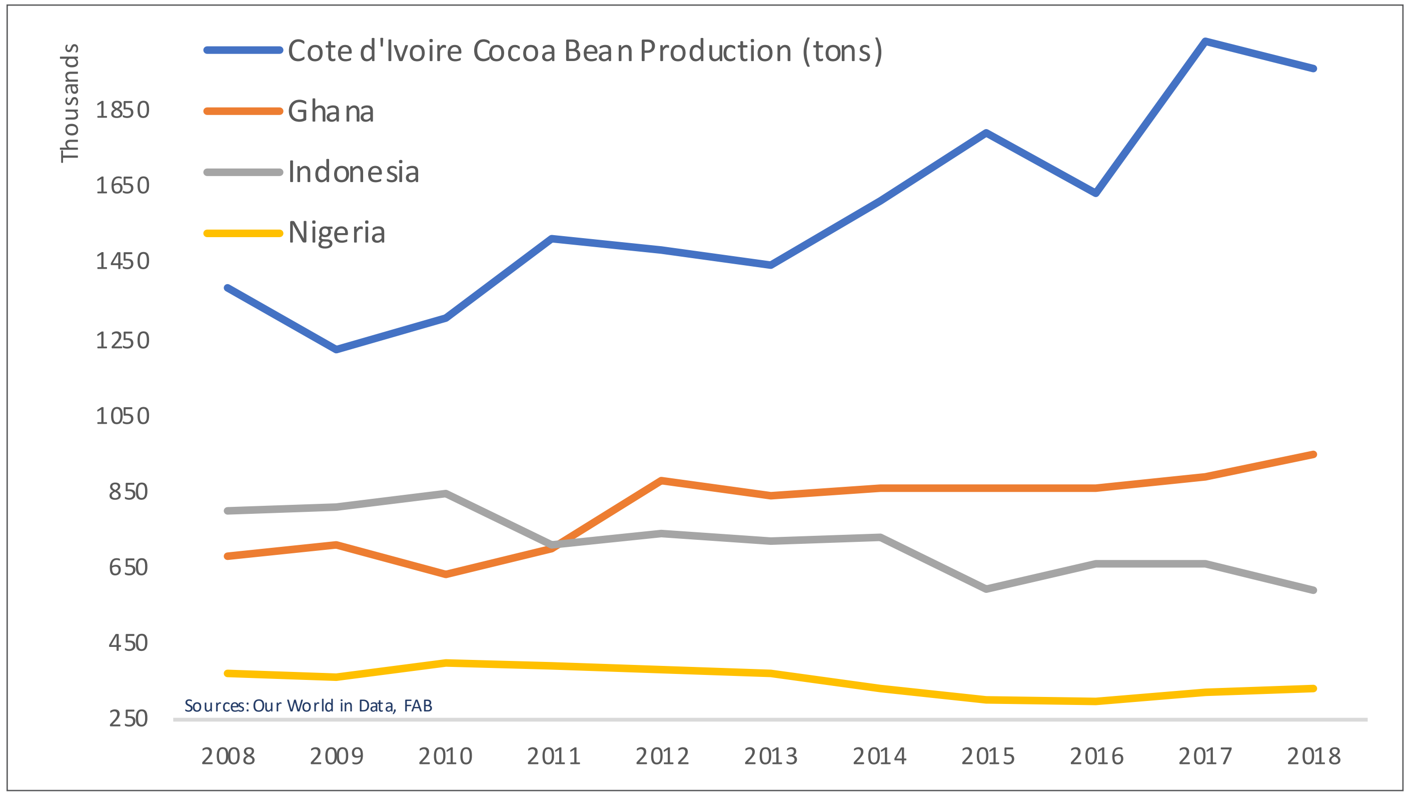


In its latest forecasts, the World Bank expects the SSA region to grow by 3.5% in 2022 from 3.3% last year following a 2% contraction in 2020. So, in this piece, we take a brief look at three countries that are not usually on the mainstream radar for investors but that have outperformed across various metrics in recent years and that have the potential to continue this trend in the near and medium-term.

The Ivory Coast

Situated on the south-west coast of Africa and sandwiched between Ghana, Liberia and Guinea, the Ivory Coast is the world's largest producer of cocoa. Political stability has improved markedly since the end of the civil war in 2011, and this was highlighted in March last year by the peaceful conclusion of parliamentary elections in which all the country's main parties participated for the first time in ten years. Meanwhile, moves by the incumbent President Alassane Ouattara to reconcile with his rivals have also helped to improve the general discourse.

Between 2011 and 2016, the Ivory Coast was one of the fastest growing economies in the world and one of only a handful of countries to have recorded a positive growth rate in 2020. The economy rebounded quickly last year, thanks in part to good rainfall figures that resulted in a strong performance by the agricultural sector. The economy expanded by 6.5% in 2021 and is expected to grow by 7.1% in 2022 according to the state statistics agency.



An astonishing 70% of the world's cocoa beans comes from just four countries. Ranked in order of cocoa production, these are the Ivory Coast, Ghana, Indonesia and Nigeria. The Ivory Coast's economy is driven by the agricultural sector, which is also the primary employer. Aside from coffee and cocoa beans, other important cash crops include palm oil, cotton, cashew nuts, bananas and rubber. However, the government's second four-year 'National Development Plan', which was introduced in 2016, has begun to bear fruit. The manufacturing sector is now the second largest contributor to GDP while the values of construction, telecommunications and services have also increased. In addition, the Italian firm ENI's recent offshore discovery of significant oil and gas deposits, which are estimated to contain up to 2 billion barrels of oil and 2.4 trillion cubic feet of associated gas, could significantly boost government revenues and help to further diversify the economy in the years to come. On the investment front, the government continues to work to improve the business climate. This includes the creation of a new, more efficient investment law, the establishment of a commercial court and the ongoing implementation of e-services for key tasks such as tax filings and payments.

It is also worth noting that the country has one of the region's most reliable power grids, and it even exports some of its electricity production to neighbouring countries. This capacity is soon to be increased and diversified via the 44MW 'Singrobo' hydroelectric power plant (due to begin operations in 2023) and the 390MW 'Atinkou' thermal power station, which will be fuelled by natural gas and which is expected to come on stream in 2024.

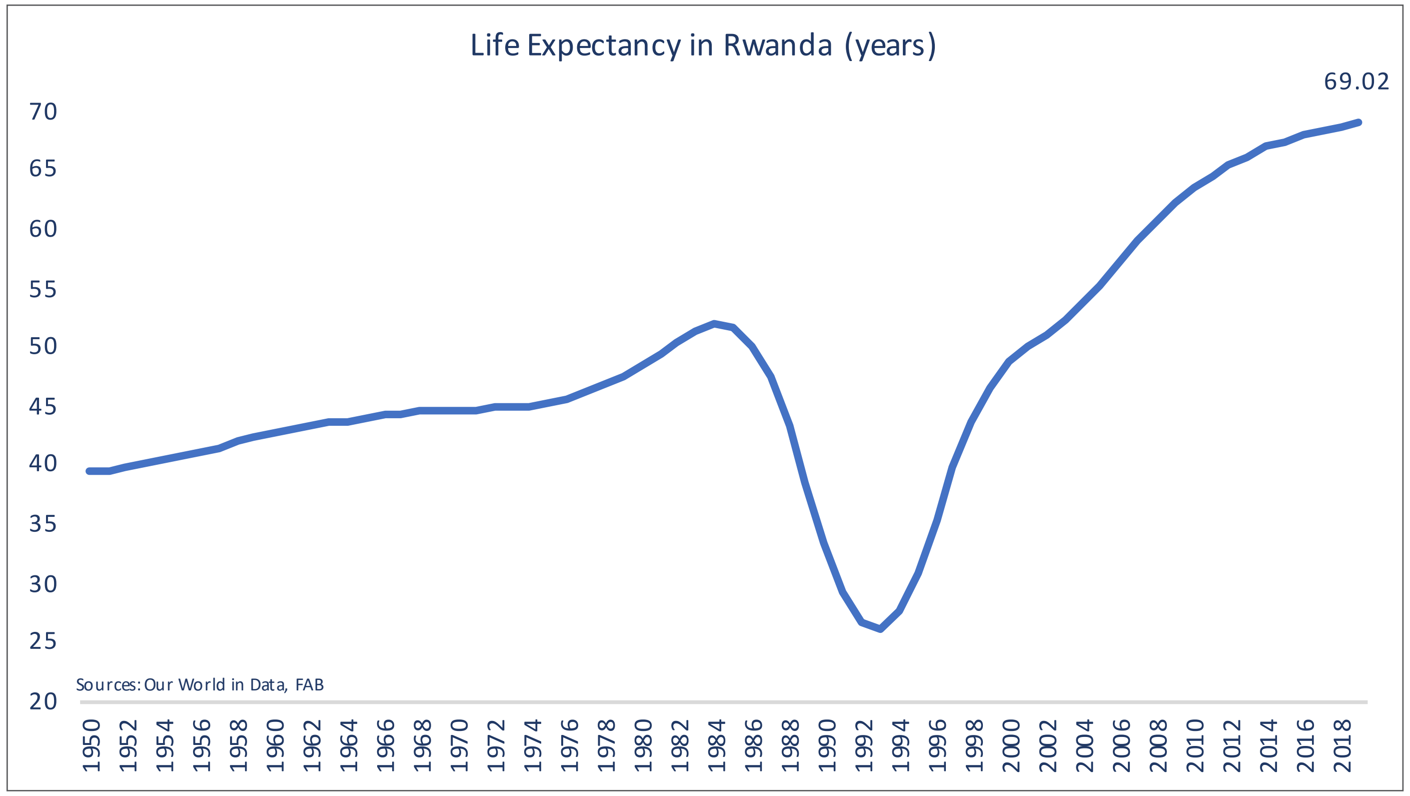
In an effort to shield itself from the economic impact of COVID-19, the government signed up to the G20's debt service suspension initiative and conducted an EUR 1 billion international bond sale in November 2020 to help fund its budget deficit (5.6% of GDP). A third economic development plan for 2021-2025 was launched last year; the government says this plan is aimed at removing 'the remaining barriers to economic and social transformation'. Meanwhile, although inflation rose to its highest level since 2017 late last year, it is still in single digits at 4.7% year-on-year and it also is held lower due to the country's membership in the Central African Franc Zone, which means the currency has effectively been pegged at XOF 655.97 to the Euro since 1999.

Population	Real GDP Growth	Debt-to-GDP	Unemployment	Inflation	FX Reserves	FX Regime
26.3 million	6.5%	49.8%	6.7%	4.7%	n/a	EUR Peg
GDP (PPP)	**Ease of doing business**	**Corruption Ranking**	**Stock Mkt Capitalisation**	**3M T-Bill**	**5Y CDS Level**	**Credit Rating**
US$ 69 billion	110/190 (WB)	146/198 (GCI)	US$ 7.3 billion	2.32%	375.8	BB- (S&P)

Sources: WB/IMF/GCI/Bloomberg/Fitch/S&P/FAB – Note: The above data points are estimates only as of 2 November 2021.

Rwanda

Rwanda, a landlocked country in East Africa, is sadly often remembered for a civil war in the 1990s that triggered a horrific genocide and led to the death of an estimated 800,000 people in just 100 days. Visitors to the country today will discover a completely different place where citizens have worked proactively to confront the emotional and physical scars of this terrible event, rebuilding their shattered economy and turning Rwanda into a real African success story. Official data underlines this swift turnaround, with real GDP growth averaging 7.2% per year between 2009 and 2019 and GDP (PPP) per capita rising from US$356 in 1994 to US$2,200 in 2020. Meanwhile, overall life expectancy jumped from just 26 years in 1993 to 69 years in 2019 according to the UNDP and the World Bank.



From a country that was heavily reliant on subsistence farming, an aggressive reform programme (Vision 2020) over the past two decades has transformed the economy into a somewhat more inclusive and diversified one, although the agricultural sector (now modernised) still remains the largest employer, and the export of products such as timber, fish, coffee, tea, sorghum, potatoes and bananas are vital foreign exchange earners.

Other growing contributors to GDP include the construction industry and manufacturing, which have both been boosted by the government's efforts to remove red tape, the introduction of tax incentives, the establishment of the Rwanda Development Board to fast-track important projects and the passing of strict laws to protect intellectual property rights as well as contractual obligations. Meanwhile, on the infrastructure front, a notable success story has been the installation of a reliable power grid, which provided electricity to the homes of more than 65% of the population in 2019, compared to just 10% in 2009, and the government expects this figure to hit 100% by 2024. A central sewage system is set to become fully operational within the next two years and the first phase of a new state-of-the-art international airport is nearing completion outside Kigali. The airport has the potential to become a key hub for the East African region and will provide a major boost to the country's tourism sector. Innovation and the adoption of new technology have been another key pillar of Rwanda's economic recovery, especially during the past decade, as highlighted by the fact that mobile phone coverage has reportedly reached 100% while internet usage has soared following the rollout of a fibre optic network.

Admittedly, the COVID-19 pandemic did trigger a further rise in public sector debt, which is likely to continue to expand in the near term and to delay moves to reduce the budget deficit. However, economic growth is estimated to have rebounded to 5% in 2021 and will likely move back above 7% in 2022-23. This, in turn, should help to improve government revenues. Meanwhile, inflation, which almost hit 10% year-on-year in 2020, has since declined and looks set to average 3.75% in 2021-22.

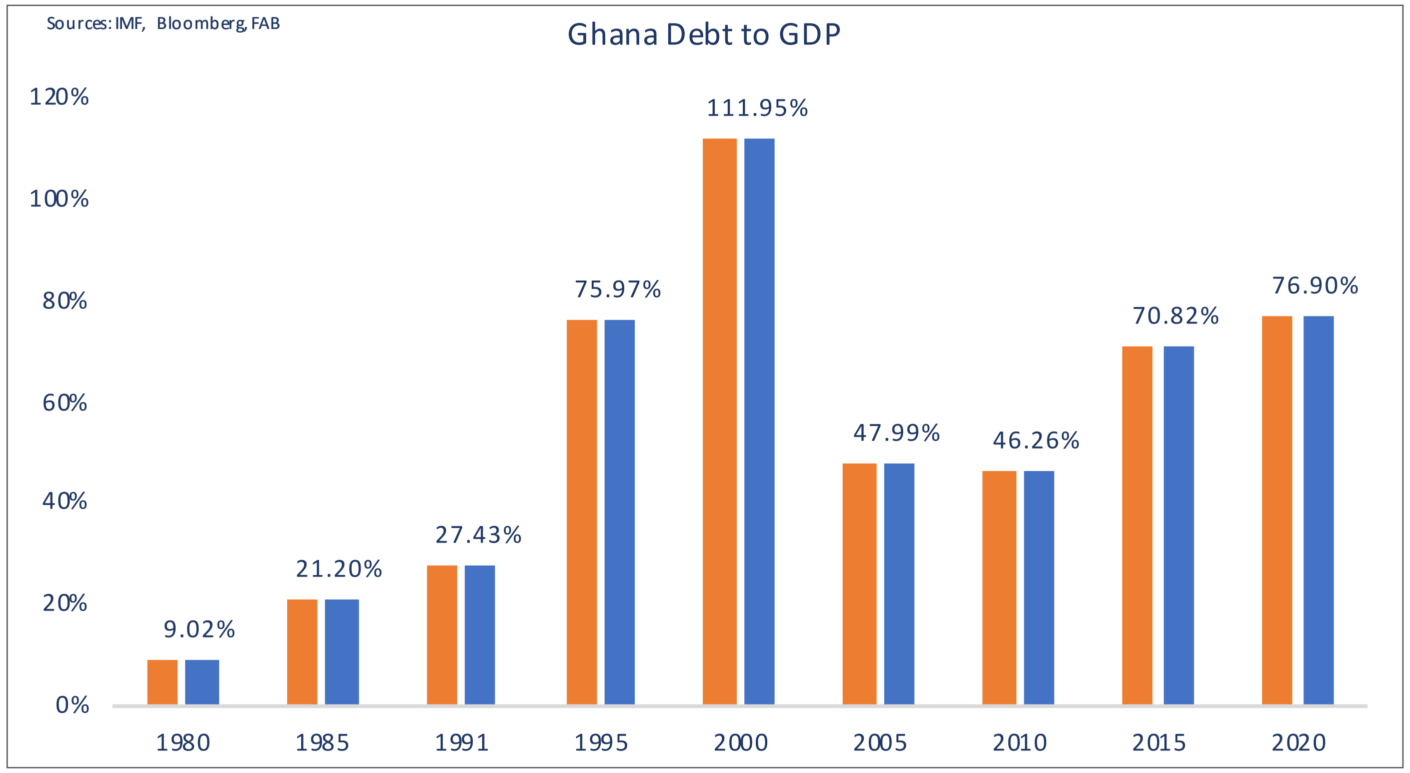
President Paul Kagame has been the head of state since 2000 and his ruling party the Rwandan Patriotic Front currently dominates the political landscape. His administration continues to follow liberal fiscal and market-driven policies and, given the fact that opposition parties are few and far between, these policies are unlikely to change any time soon. In addition, most Rwandans still appear to revere Kagame for the economic progress and security he has brought to the country in the past 21 years, as well as his promotion of women in the public sector (60% of MPs are female) and efforts to protect the environment. The President's current seven-year term is due to end in 2024 but, due to the outcome of a constitutional referendum in 2015, he will be able to stand for two more terms in office.

Population	Real GDP Growth	Debt-to-GDP	Unemployment	Inflation	FX Reserves	FX Regime
13.30 million	5.10%	70%	4.10%	0.70%	US$1.89 billion	Managed float
GDP (Nominal)	**Ease of doing business**	**Corruption Ranking**	**Stock Mkt Capitalisation**	**3M T-Bill**	**5Y CDS Level**	**Credit Rating**
US$15.20 bio	38/190 (WB)	69/198 (GCI)	US$3.20 billion	7.16%	303.40	B+ (S&P)

Sources: WB/IMF/GCI/Bloomberg/Fitch/S&P/FAB – Note: The above data points are estimates only as of 2 November 2021.

Ghana

In October 2021, Rand Merchant Bank ranked Ghana the number one country for investment attractiveness in West Africa, followed by the Ivory Coast and Senegal. This was despite the country's growing debt problem, which is discussed in more detail below. It was also one of the few economies that managed to avoid a contraction in 2020 (+0.4%); it is estimated to have grown by 4.6% last year and could reach 5% in 2022 according to the Central Bank. Ghana still relies relatively heavily on the agricultural, tourism and mining sectors, and cocoa and gold have historically been key exports. However, its once struggling manufacturing industry has made a strong comeback in recent years, supported by a wave of pro-business reforms aimed at boosting the production of value-added products. Meanwhile, the oil and gas sector is also set to expand its influence, especially with the past year's rebound in prices and ENI's recent offshore oil discovery in the 'Eban-1X' block, which the company estimates could hold between 500-700 million barrels of crude. Ghana's first oil and gas resources were only discovered in 2007, but fresh investment is needed to expand production, which currently sits around 185,000 barrels/day. In this regard, the government has reportedly requested parliamentary approval to borrow up to US$1.65 billion to broaden oil and gas exploration and develop stranded assets.

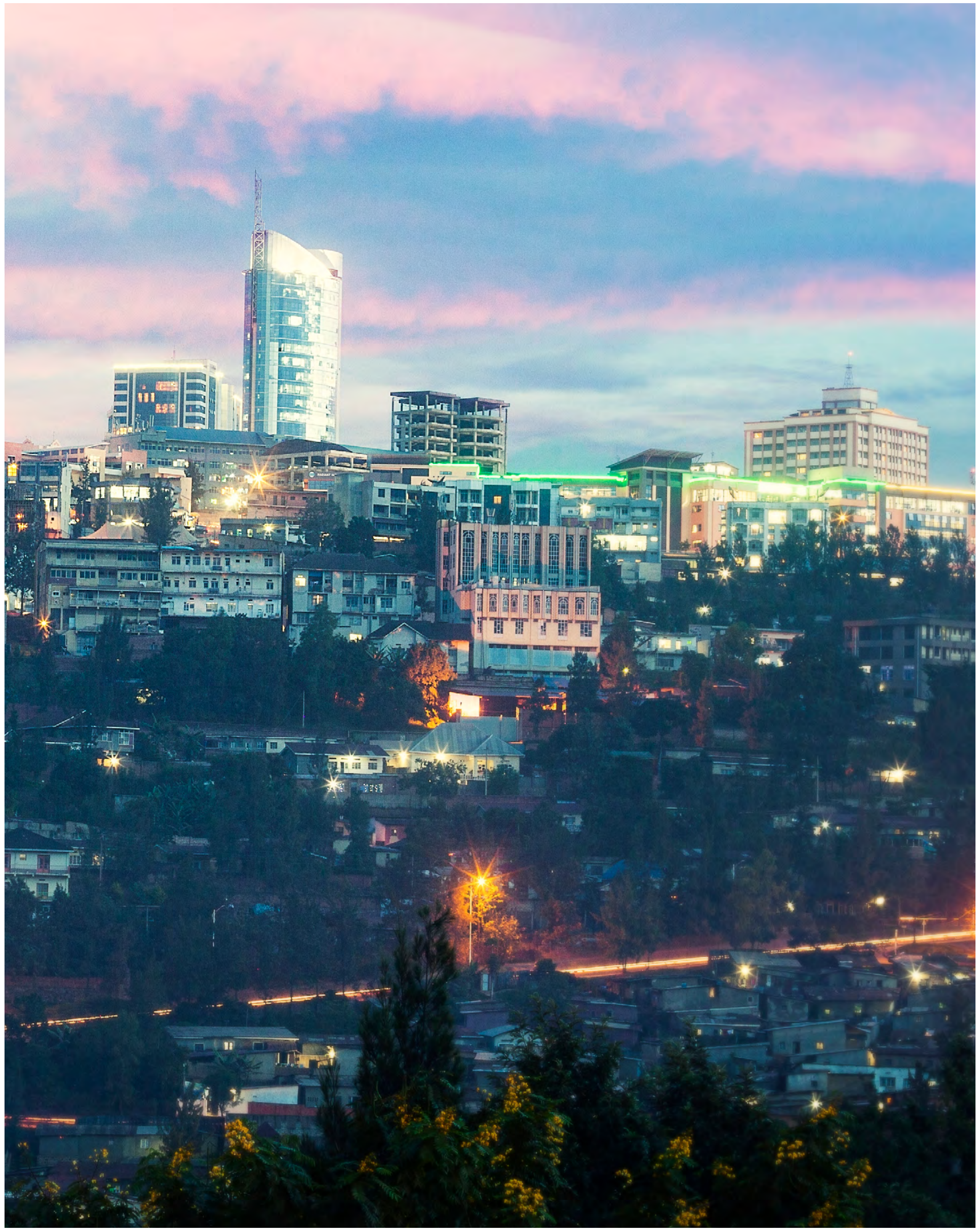


On the downside, Ghana's public debt load remains stubbornly high at more than 75% of GDP. In fact, the country currently spends about 37% of its annual budget on debt-servicing and its external debt level was estimated to be around US$28 billion in July last year, leading both the IMF and the World Bank to call on the government to lower its rate of borrowing as soon as possible. This spooked investors and pushed up the risk premium on Ghana's Eurobonds to more than 900 basis points above comparable US Treasuries in October 2021, while the CDS rose above 1000 basis points one of the highest premiums for the instrument globally aside from countries like Sri Lanka and Argentina. However, in its Q4 2021 Country Report, Fitch Ratings said that while Ghana's current debt level and fiscal deficits should remain a concern for investors (an estimated 20% of local currency sovereign debt is held by non-residents), the ratings agency was 'confident' that the country would record somewhat narrower fiscal deficits and slower growth in public borrowing in the medium-to-long term, adding that 'this will bring the debt burden down somewhat as a percentage of GDP relative to early 2020'. There is of course also a chance that Ghana will return to the IMF for help in the near term. In 2019, the multilateral lender advised the government to extend its maturing Credit Facility Program, but this was rejected. Now, with the cost of Eurobond issuance rising and the impact of COVID-19 accelerating the country's public debt problems, pragmatism may yet persuade the administration to reengage with the IMF.

Meanwhile, since touching 7.5% year-on-year in May last year, the inflation rate has edged back up into double figures and hit 10.6% year-on-year in September 2021, driven primarily by housing, water and electricity prices, although this rise is probably going to be transitory and the contribution of food prices to the overall inflation number has declined somewhat. On the political front, the ruling 'New Patriotic Party' (NPP) managed to retain the Presidency and hold onto a slim parliamentary majority following general elections in December 2020. Ghana is regarded as one of the most politically stable countries in the SSA region, and it has held eight peaceful elections since returning to a multi-party democracy in 1992. However, with the NPP now having only a tiny majority in parliament and the incumbent President Nana Akufo-Addas set to step down in 2024 due to constitutional term limits, there is a risk that the government could sharply increase public spending in the run-up to the next polls.

Population	Real GDP Growth	Debt-to-GDP	Unemployment	Inflation	FX Reserves	FX Regime
31 million	4.90%	77%	4.10%	10.60%	US$11.10 billion	Flexible
GDP (Nominal)	**Ease of doing business**	**Corruption Ranking**	**Stock Mkt Capitalisation**	**3M T-Bill**	**5Y CDS Level**	**Credit Rating**
US$76 billion	118/190 (WB)	77/198 (GCI)	US$9.25 billion	12.50%	1020	B- (S&P)

Sources: WB/IMF/GCI/Bloomberg/Fitch/S&P/FAB – Note: The above data points are estimates only as of 2 November 2021.



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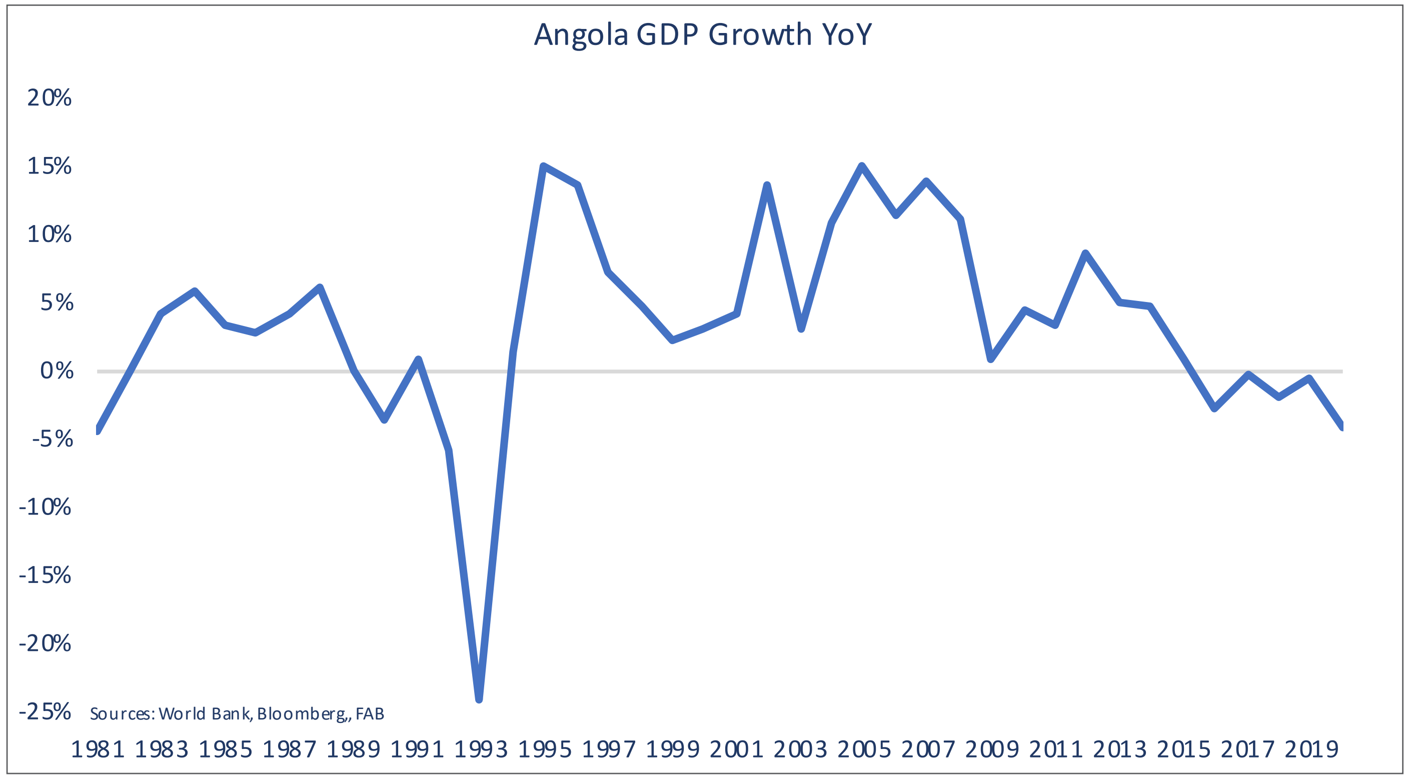
ANGOLA

'RICH & POOR'

By Glenn Wepener, Executive Director and Senior Strategist, Middle East and Africa, Market Insights and Strategy

Angola is Africa's second largest oil producer, although its heavy reliance on crude exports continues to undermine its economic potential. This sub-Saharan country is blessed with a wide array of other natural resources, including significant reserves of metals and minerals, fertile agricultural land and rich fishing grounds, but a 27-year civil war (1975-2002), and governance issues have prevented it from realising its obvious potential thus far.

President Jose Eduardo do Santos' retirement in 2017 after 38 years in power and the appointment of Joao Lourenco as his successor appeared to provide a window of opportunity to set Angola on a new course. As the next general election approaches, we take a fresh look at the state of the nation and whether any progress has been made towards fulfilling Lourenco's promise to create an "economic miracle".



Economic Snapshot

Angola's oil sector currently accounts for more than a third of the country's GDP, 90% of its exports, 98% of its foreign exchange generation and around 75% of the government's revenues. The other main contributing sectors are diamond mining, services, manufacturing and agriculture.

After achieving a record growth rate of 15.02% in 2005, the economy began to slow down, exacerbated in part by the global financial crises but primarily due to the oil market entering a cycle of lower prices starting in 2014 and a decline in Angolan crude output, which pushed the country into recession in 2016. This negative growth path worsened to -4.04% in 2020 as the COVID-19 pandemic and the short but sharp oil price war inflicted even more economic pain. This situation forced the government to increase its level of borrowing; the African Development Bank recently calculated that the country's public debt level had jumped from 57% of GDP in 2015 to over 120% last year. Half of the country's external debt is owed to Chinese creditors, including the China Development Bank, although they recently agreed to a freeze on principal repayments until 2023. Fitch Ratings recently affirmed its long-term foreign-currency issuer default rating on Angola at 'CCC' but highlighted the risk to the country's medium-term debt sustainability and uncertainty around available external financing sources over the next two to three years.

In 2018, the Central Bank abandoned the Kwanza's peg to the US dollar and introduced a flexible exchange rate regime, which has helped to reduce the impact of lower oil prices on its falling FX reserves. However, inflation has risen and was reported to be sitting at 26.5% in September 2021, leading the apex bank to hike its benchmark interest rate from 15.5% to 20% last August for the first time in four years. The official unemployment rate now stands around 34% while youth unemployment reached 57% in the second quarter of 2021.

Politics – Same but different

Joao Lourenco succeeded Jose Eduardo Dos Santos as President of Angola in 2017. Despite the fact that he is also a member of the MPLA, which has ruled Angola since its independence from Portugal in 1975, there were hopes that a fresh leader would bring about some positive changes. These hopes rose following the acceptance speech in which he promised to combat graft and reform the economy dramatically.

In relation to these promises, a number of senior officials have been charged with corruption, including a former Central Bank governor and the ex-President's son Jose Filomeno dos Santos. The latter's sister, Isabel dos Santos, had her business assets frozen in 2019 and is accused of diverting billions of dollars from state companies. She is currently living outside the country and has denied any wrongdoing.

New tendering laws were introduced, resulting in the removal of a long-standing requirement for foreign investors to have a local partner, and a range of reform-minded younger technocrats were placed in key positions. One example of such an appointment was Vera Daves de Sousa who, at just 37, became the youngest Finance Minister in Africa when she assumed the post in late 2019.

The new President has also been far more approachable than his predecessor, conducting interviews with journalists to debate the challenges his government faces, becoming active on social media, and even allowing street protests to take place initially.

In terms of fiscal reform, some progress has been made in the areas of privatisation and the reduction in unnecessary public spending. Although these actions helped the government seal a US$4.5 billion support programme with the IMF in 2018, much more still needs to be done.

On the legal front, the President submitted a number of proposed changes to the country's constitution, such as clarification on the level of political oversight between parliament and the executive branch of government, to parliament earlier this year. One of the other key amendments, which has since been approved, granted independence and stronger regulatory powers to the Central Bank. However, MPs are still trying to reach a consensus on several of these proposed changes, especially those linked to electoral laws, while the revision bill also reaffirms a 2013 ruling by the Constitutional Court that effectively prevents the National Assembly from summoning government ministers for questioning without the President's consent.

The next general election is due to be held this year, and the country's proportional representation electoral system means that voters cast their ballots on a closed list of candidates drawn up by political parties. The 220 seats in the National Assembly are allocated to parties in proportion to the share of votes they receive. The leader of the political party or coalition of parties that receives the majority of the votes is duly appointed President. Despite the ongoing economic malaise, the MPLA is likely to retain power. However, the three main opposition parties (UNITA, CASA-CE and BD) have formally agreed to participate in this year's poll as a coalition called the 'United Patriotic Front'.

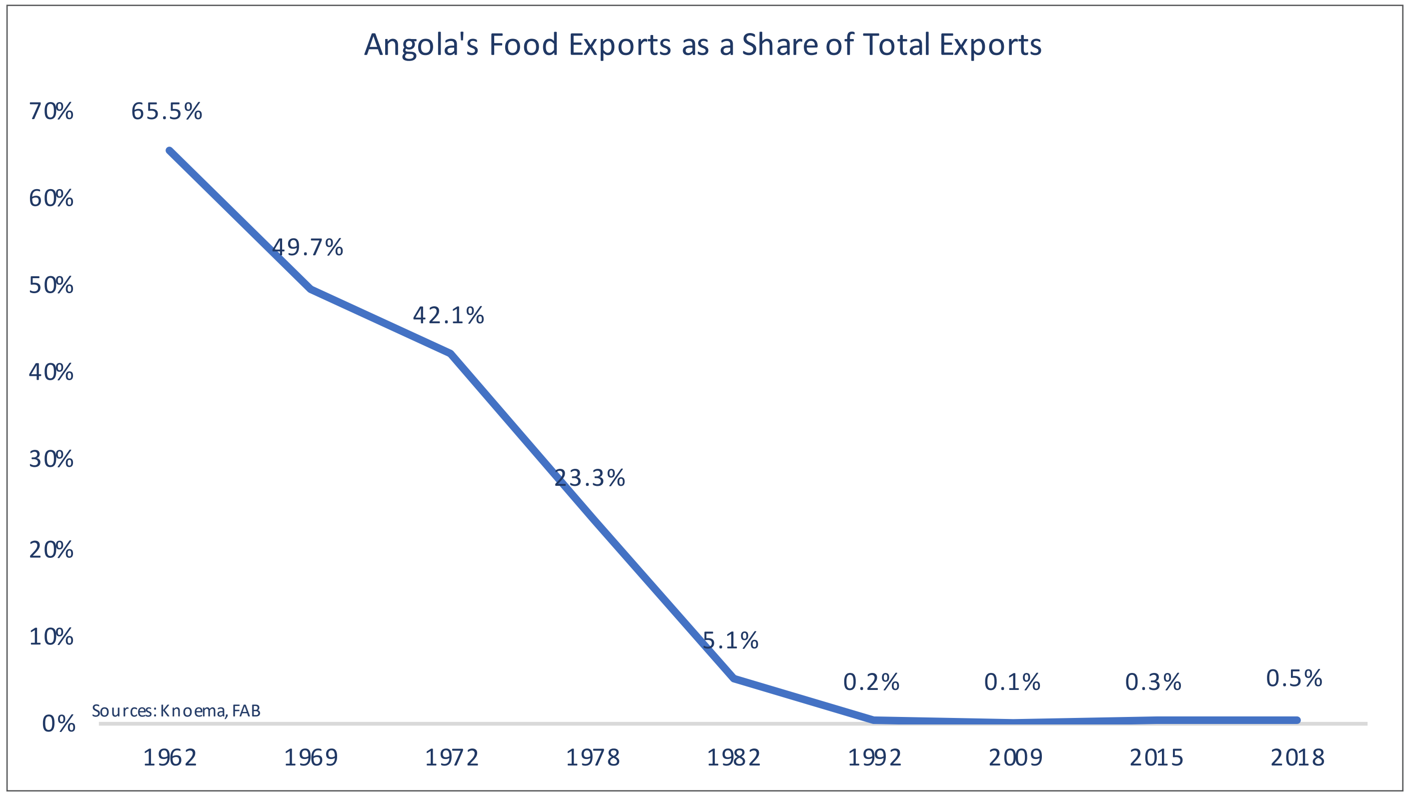
Leading this new coalition is Adalberto Costa Junior, the head of Angola's largest opposition party UNITA, which fought an armed struggle against the government until the 2002 peace agreement.

The opposition's desire to unseat the MPLA from power will probably have been boosted by the surprise landslide victory of Hakainde Hichilema in last year's Presidential elections in Zambia, which appeared to underline the message that even well-entrenched administrations can be removed.

Oil Production – A slippery slope

Oil was first discovered in Angola's Kwanza Valley in 1955. In 1962, large reserves were found offshore and full-scale production began. By 1973, oil had become the country's primary export, and output reached 172,000 barrels/day. However, this was not Angola's only resource; from the late 1920s to the early 1970s, Angola was a major exporter of gold, iron ore, manganese, copper, textiles, maize and fresh fish and the world's fifth largest producer of coffee. It also had a good rail and road network as well as reliable power supplies generated by hydroelectric plants.

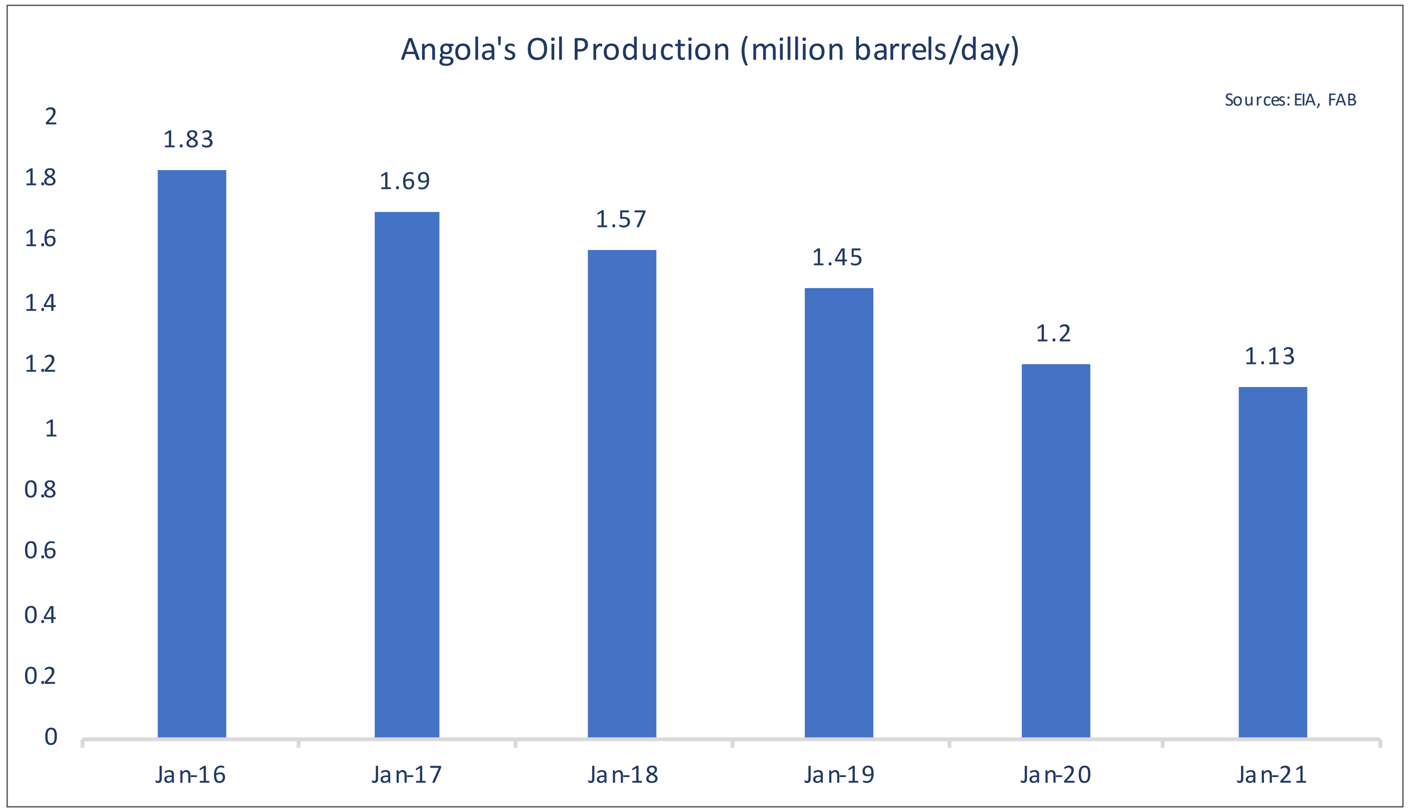
In 1975, Angola achieved independence from Portugal but immediately slipped into a brutal civil war, which led to the exodus of many skilled workers including commercial farmers and severely disrupted the mining, manufacturing and agricultural industries. The newly ensconced MPLA government began to rely heavily on revenues generated by oil and diamond exports. Following the signing of the peace agreement in 2002, new investment began to flow into the country, but the bulk of this was concentrated on the oil and gas sector, especially as crude prices had begun to boom. This meant that agriculture, which had switched to subsistence farming during the war years, remained nascent; Angola still has to import the bulk of its food requirements despite the opportunity to become a major exporter of foodstuffs again. To highlight the extent of this problem, Angola was Africa's third largest importer of US agricultural products in 2019.



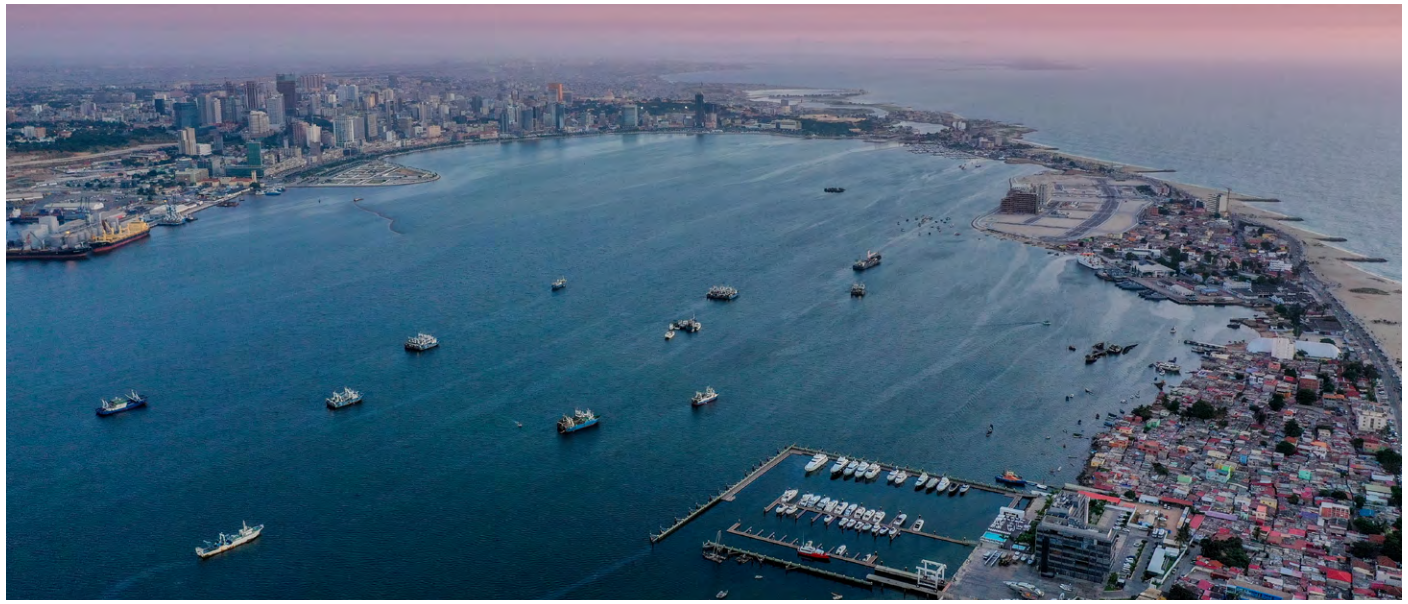
Initially, as oil prices rose above US$100/barrel, Angola's crude output leaped from 745,000 barrels per day in 2000 to a peak of 1.95 million barrels/day in 2006. The consequent rise in revenues spilled over into the rest of the economy, especially construction, manufacturing, financial services and real estate. Many Angolans flocked from the countryside to Luanda as job opportunities reappeared, pushing the city's population from 800,000 at the end of the 1980s to around 4.6 million by 2008, putting major pressure on already fragile basic services such as water, sanitation and power, which were still in need of significant rehabilitation. Meanwhile, the cost of living also increased exponentially (even for the capital's wealthier residents), with Luanda making global headlines after it was listed by ECA International as the world's most expensive city to live in 2007, ahead of Oslo and Tokyo.

Then the Global Financial Crisis hit and the price of Brent plummeted from US$140 in June 2008 to as low as US$45 in December the same year. It would take until the end of 2010 for prices to once again break above the US$100 level before entering another longer down-cycle in 2014. The resultant drop in revenues hit Angola hard and it came as domestic crude production was also beginning to decline, eventually falling to a 17-year low of 1.07 million barrels/day in June 2021, which was also below its allocated limit of 1.298 million barrels/day in the OPEC+ output cut accord. The country's ongoing production problem is due primarily to its aging offshore fields, the challenge of efficiently exploiting new but deeper underwater finds (some of which are only feasible at an oil price of US$100 and above), and exploration spending constraints at the state-owned oil company due to its heavy debt load. In 2019, Sonangol's debt repayments of US$1.8 billion effectively wiped out its revenues despite the sale of certain assets, and KPMG reported that the company's liabilities outweighed its assets that year.

However, the outlook for Angola's oil and gas sector is not entirely bleak, and green shoots are appearing. As oil prices rebounded last year, interest in exploring more of the country's offshore basins picked up again. This interest grew following a fresh appraisal of Angola's oil and gas potential in 2020, which suggested that its reserves equalled 57 billion barrels of oil and 27 trillion cubic feet of gas. This was a significant increase on the previous estimate of 8.2 billion barrels and 13.5 trillion cubic feet. Another attraction is the fact that Angola produces light and medium grade sweet crude oil, which are much preferred by Asian buyers.



Meanwhile, as part of the Lourenco administration's plan to reinvigorate the country's oil industry, the authorities announced the auction of nine onshore oil blocks, three in the terrestrial section of the Lower Congo Basin and six in the terrestrial part of the Kwanza Basin, at the end of 2020. At the same time, the government is moving to develop a domestic refining capacity. This is very important as Angola currently imports almost 80% of its refined petroleum needs. In April last year, the Italian oil company ENI announced that it had made a new deep-water discovery in Angola's Cuica field and it began producing last month. Finally, both Total and ExxonMobil have received the green light to expand some of their deep-water operations, and the latter and Sonangol have reportedly begun to carry out exploration work in the Namibe Basin.



There has been some progress in promoting diversification outside of oil and gas in recent years. In December 2020, the 'Free Trade Zones Act' was passed. The Act is focused primarily on supporting development within the industrial, high-tech and agricultural sectors, using incentives such as lower taxes in order to attract foreign investment. The government has also recognised that the restoration of coffee, cocoa and palm oil production will be a key pillar of its diversification programme. In the early 1970s, Angola was producing 230,000 tonnes of coffee; this had fallen below 5,000 tonnes by 2002. In 2019, production had recovered to 8,700 tons, which is still a long way away from where it needs to be, but there are hopes that an ongoing campaign to reactivate and increase harvest levels together with financial and technical assistance from the European Union will bear fruit sooner rather than later.

After oil, diamond production remains the country's other primary revenue source. Angola is the world's sixth largest producer of these precious stones, and fresh investment is now being channelled into this sector. In the province of Lunda Sul, a new 'diamond hub' is being built. When complete, it will house diamond polishing factories and a technical training centre linked to all aspects of the diamond business. These facilities will reportedly be powered by renewable energy.

Conclusion

Angola still faces a myriad of economic and social challenges, but some progress has been made over the past few years despite a much tougher global environment. The rebound in oil prices over the past year has given the government some short-term breathing room, which will increase its leverage to meet the goals of its ambitious reform programme and generate more sustainable and inclusive growth. Areas to watch in the months ahead include the ongoing process of privatising more than 190 state-owned assets, continued moves to reduce the level of public debt, the creation of a more business-friendly environment, and a deeper commitment to rebuilding key infrastructure and promoting the non-oil sectors so that the country's obvious potential can eventually be realised.

*Click **here** for the disclaimer.*

EGYPT: SOUND FISCAL POLICY AND STRONG GROWTH

By Sagar Patel, Director, FAB Investment Management Research

Egypt is one of the leading economies in Africa, and its strong growth, positive real rates and stable government have increasingly attracted the focus of global investors. With the help of the IMF, the country has managed to improve its fiscal balance, and a privatisation programme has shifted the use of state resources to more needed investments.

The IMF estimates average GDP growth to come in at 5.2% for the fiscal year 2022 and 5.6% for fiscal year 2023. While investors acknowledge that Egypt's improvement in public finances will be gradual and that it has been pushed back due to COVID-19 stimulus measures, the country has made progress since IMF-led structural reforms were first implemented in 2016. The IMF support during the pandemic highlights the confidence in the country's intent and ability to deliver reforms. The potential recovery in tourism and global trade in addition to financing support from regional countries and successful bond issuances have allayed concerns around any short-term funding pressures.

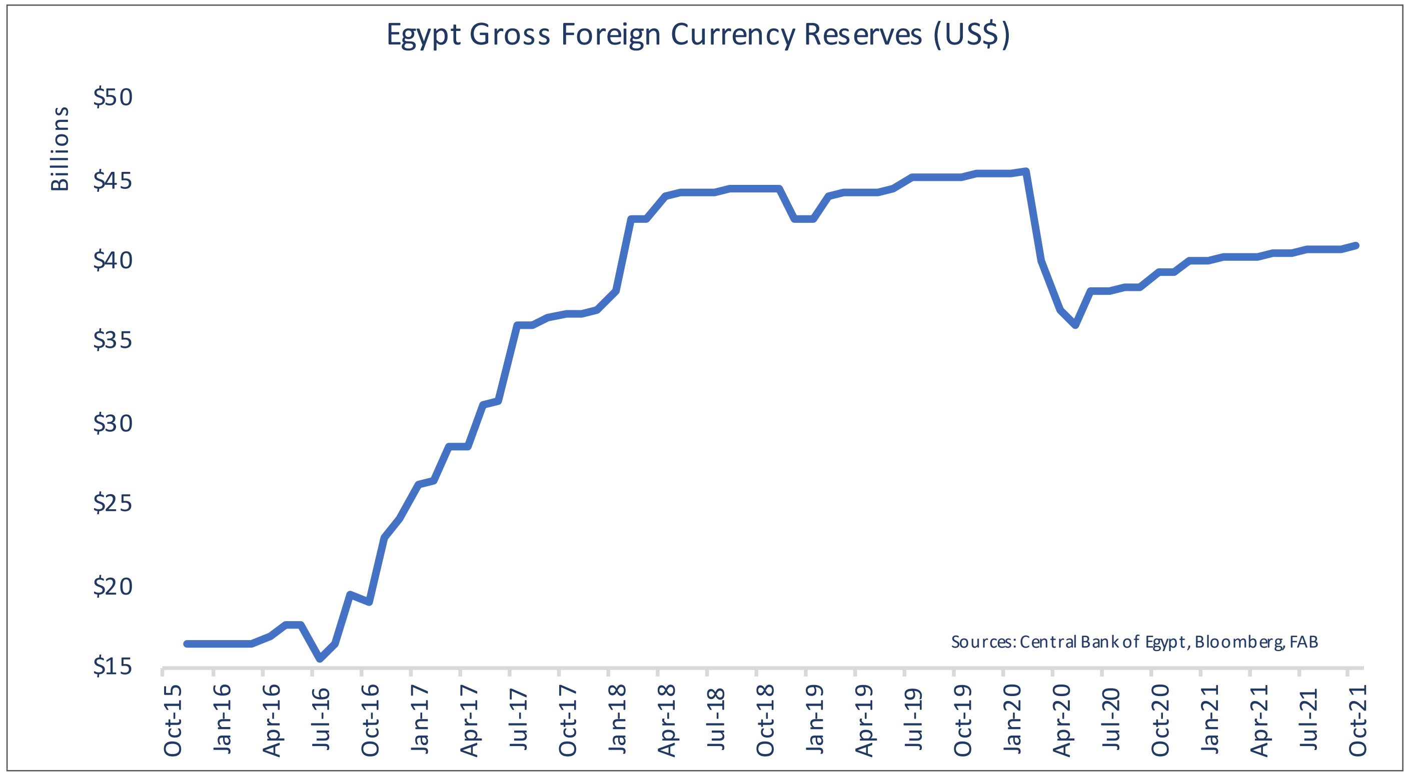
The disbursement of US$5.4 billion in the last fiscal year as part of the IMF's stand-by arrangement provided

much needed fiscal and balance of payments support after tourism virtually came to a halt and the local economy slowed. In addition to facilitating support for vulnerable households and sectors, the arrangement has led to improved fiscal transparency through various disclosure requirements including financials of state-owned enterprises and beneficial ownership of COVID-19 contract awardees, as well as favourable changes in business laws. The country aims to be on track with its fiscal targets to achieve a primary surplus of 2% by 2023 and lower the debt-to-GDP ratio to 75% by 2026, compared to 89.8% at present.

This pragmatic approach has also helped to increase GDP per capita in US dollars by 55% since 2017, according to IMF data. Naturally, this process has been slowed temporarily by the pandemic. The Egyptian economy has been negatively impacted by COVID-19 and the Central Bank of Egypt estimates the economy expanded 3.3% in the year ended in June 2021. This is better than the initial estimate of 2.8%, but a far cry from the 5.56% expansion seen in 2019.

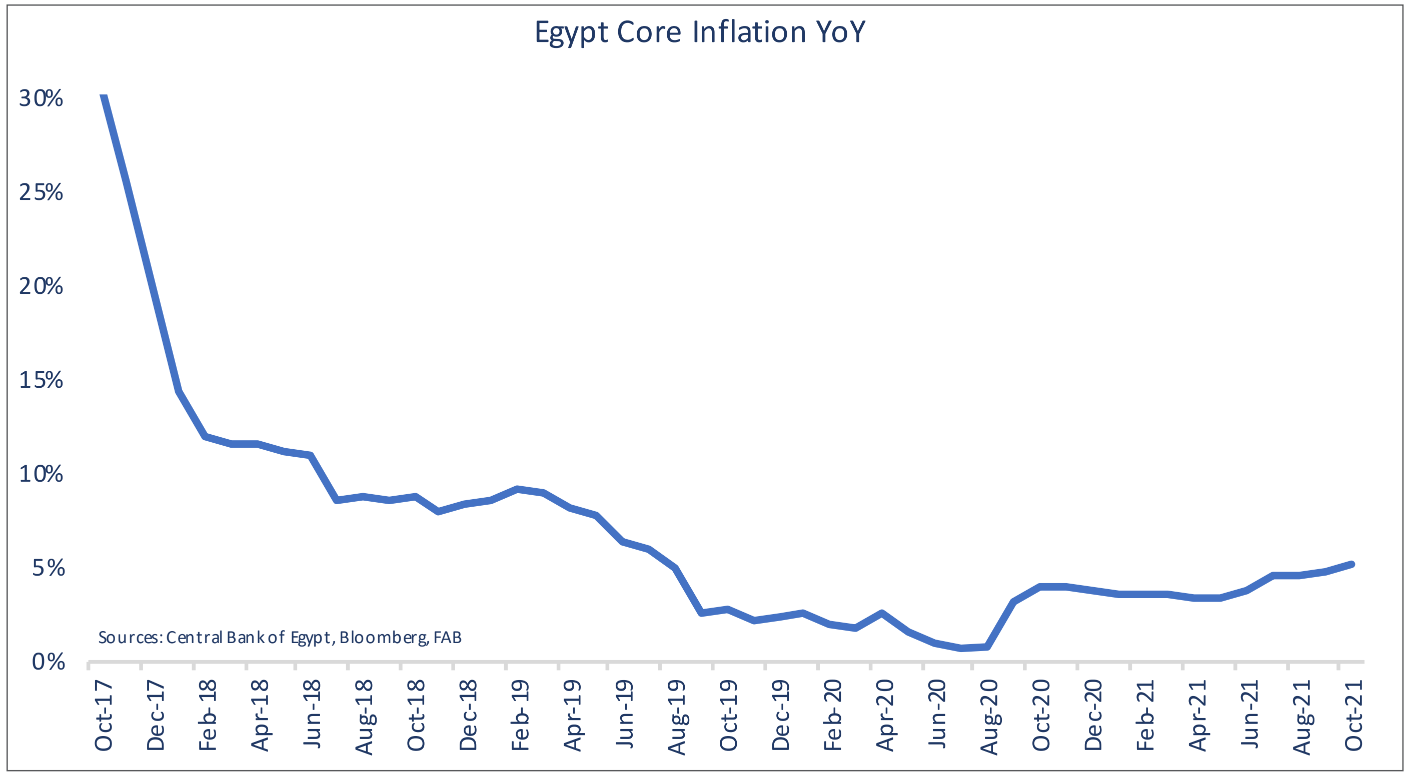
The normalisation of the economy could be volatile, partly thanks to relatively slow vaccination progress, but it should be directionally positive. The government's aim was for 40% of the population to have received at least one dose of a vaccine by 31 December 2021, but only 19% of the population had received one dose by 6 November 2021. The government is undertaking measures such as a selective entry ban for unvaccinated individuals and regular testing to accelerate the pace of immunisation.

The IMF support and an active policy of opportunistic issuance increased foreign currency reserves to US$41 billion in October, an improvement over the US$39.2 billion a year earlier. This provides an eight-month import cover. Some short-term funding concerns have been diluted recently with Saudi Arabia re-depositing US$3 billion with extended maturity terms compared to the deposit that had matured in July 2021. The recent Eurobond issuance of US$3 billion has also covered 50% of targeted net foreign borrowing of US$5-US$6 billion for the current fiscal year.



The healthy reserve position and relatively tame inflation give the central bank some leeway to keep monetary policy loose, but it has maintained a more hawkish position nonetheless. The latest inflation number for September came in at 6.6%, below the central bank's target of 7%, but the institution has maintained a marginally tighter policy to maintain higher real rates as a defence against the impact of Fed tapering and the normalisation of rates in the developed world.

The high real rate policy keeps the carry trade viable, supports reserve accumulation and foreign flows, and anchors the currency. A deviation from this policy would require a lower debt-to-GDP ratio and a high primary surplus.



Such an outcome could only materialise if the tourism industry recovers. Tourism revenues declined to under US$5 billion in 2021 from US$12.6 billion in 2019. The outlook for the industry, however, is promising, with Russian tourists back in good numbers (running 25 flights a week) after a five-year travel ban was removed last August.

That said, Egypt is likely to continue to hold positive real interest rates even when tourism recovers fully. Egypt's external debt-to-GDP ratio stands at 34% and foreigners held about 13.3%, or US$33 billion, of the country's local currency debt as of August 2021.

This could be a point of pressure this year, as previous episodes of Fed tightening or global risk-off periods saw significant withdrawals from Egypt. However, these should eventually reverse due to confidence in its IMF-supported reform programme, high real rates, and a reasonably predictable policy setting compared to some other emerging markets.

WOMEN ARE JUST STARTING TO GET RICHER

By Samira Zakour, Managing Director, Head of Private Banking

Women's purses are getting bigger, and that is not a fashion trend. Ladies controlled more than US$70.2 trillion in assets, or 32% of the world's wealth, before the pandemic, according to Boston Consulting Group. They are expected to grow that at a 5.7% compound annual rate to US$97 trillion by 2024.

When it comes to accelerating the rate at which their wealth grows, women in the Middle East stand out. They are expected to achieve 9% compound average annual growth in the value of their assets in the period to 2024, the fastest among the regions surveyed by Boston Consulting Group. Part of this is the result of recent reforms, which have seen women outnumber men in universities in 15 of 22 Arab countries.

There is something else that sets women in the Middle East apart: entrepreneurship has been the main driving force of growing female wealth here, unlike in the Asia-Pacific and Latin America regions, where holding other kinds of leadership positions has been the driver for making women richer.

Interestingly, a survey conducted by the Economist Intelligence Unit in North America concluded that women who acquired their wealth by establishing successful companies tend to be younger. They also like to have more control over the management of their assets.

While it may be difficult to extrapolate trends from North America to the Middle East and North Africa, women in this region do seem to be taking their fates into their own hands more, and they are likely to want to do the same with their investments. This is important, because women tend to invest in a very different way from men, one that often produces better long-term results.

The psychological and behavioural differences between women and men have long been a subject of study, and it has led to interesting conclusions among academics. For instance, there is a growing number of scholars who claim that if more women held positions of power, there would be fewer wars.

Generally, psychologists agree that women are more averse to risk and that they think more carefully than men before making decisions. This has wide-ranging implications for the financial life and standing of women. For instance, in investment, men trade a lot more, which ultimately reduces their gains when compared to women. However, men tend to take higher risks, which means they sometimes have large losses, but they also have big wins on other occasions.

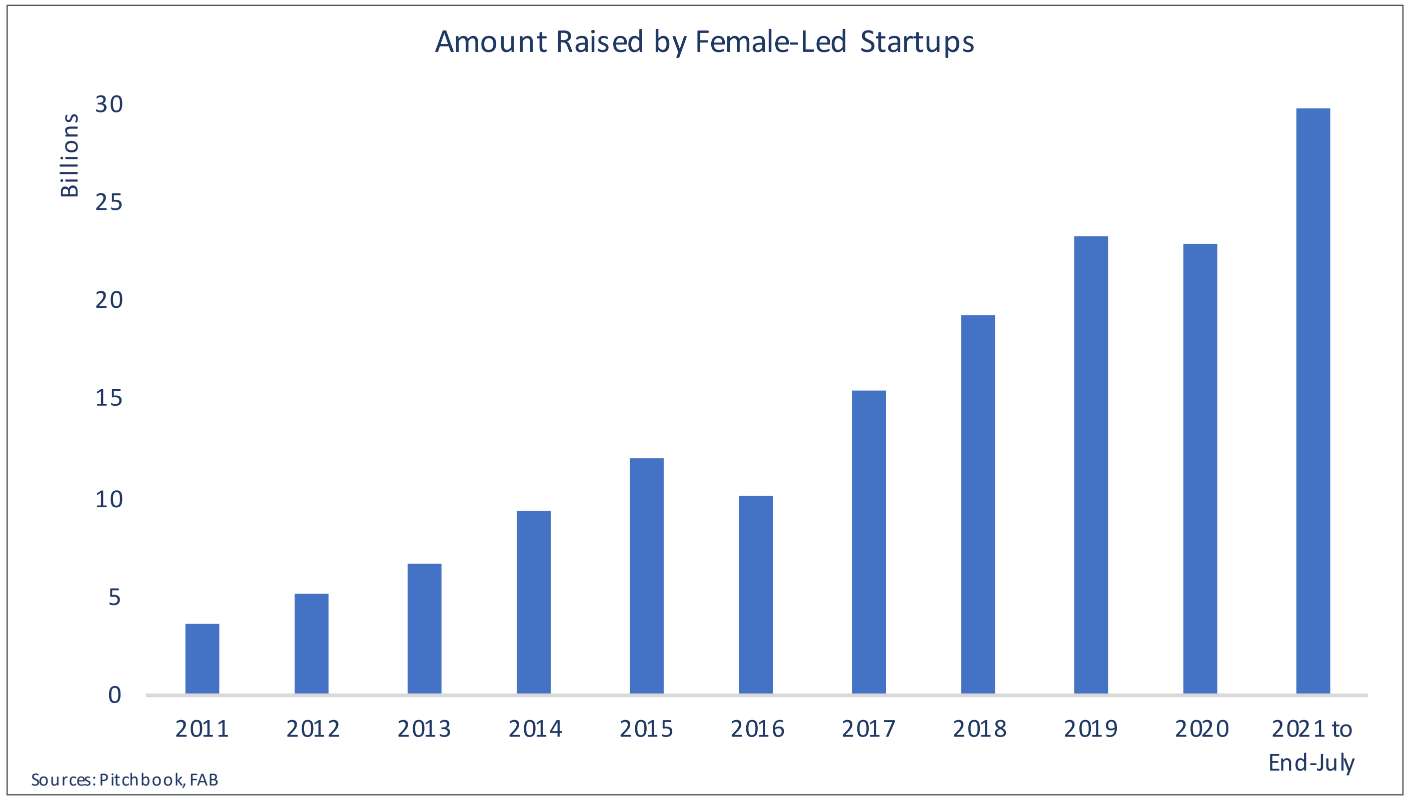
Wealth management across the world still does not seem fully prepared to deal with these subtleties and differences. As a result, most research suggests that women are suspicious of the financial advice they receive and are more likely to listen to financial advice from their partners or other people they trust.

Such behaviour is understandable, but it carries a risk: assets and strategies within a family may end up being more concentrated as a result. This would be a pity, given that women tend to be better investors than men.

Many of the tenets of good investment come naturally to women. They tend to research a subject, asset class or company more thoroughly before making a decision to buy. They take their time too, being less prone to impulse buying or selling, research shows. And once they make their decisions, they are more likely to stay the course. This and trading less than men are habits that can save an investor a lot of money – and that can help to maximise total risk-adjusted returns.

A McKinsey survey found, for instance, that women are nearly ten percentage points less likely than men to say they would take big investment risks for the potential of higher returns. They also tend to focus more on capital protection than on performance and are more likely to choose 'passive' rather than 'active' investment strategies.

Such behaviour means that wealth managers who target and advise female clients need to know their stuff. They have to be ready to answer detailed questions about any investment they are proposing, and they must understand that a woman is less likely to make a decision on the spot. Needless to say, this means that more wealth managers need to be women.



There is another angle to this: when investing directly, women are more likely to invest in other women. This dynamic has been underpinned by the growing number of venture capital firms focusing exclusively on women-led businesses and by the rise of the so-called 'femtech' investment.

However, there are not enough of these specialist funds and women-led startups remain severely underfunded. According to Crunchbase, in 2020, only 2.3% of venture capital funding went to companies led by women. Aside from being a small number, that was worse than the 2.8% registered in 2019, an all-time high.

This is not a coincidence. According to an Axios survey, only 12.4% of decision-makers at US venture capital firms last year were women – a historic record and a huge improvement over the 9.65% registered in February 2019, but still short of women's representation in the global economy.

The proportion is reflected in the number of startups that exceeded US$1 billion in valuation and were founded by women, with only 39 so-called 'unicorns' fitting that description, or 12% of the 327 that Crunchbase had identified as of August last year.

This number does not necessarily match the performance of companies founded by women. Boston Consulting Group found that, on average, female-founded startups generated more than twice the return per dollar invested than similar companies founded by men.

The fact that most of the 39 unicorns identified by Crunchbase appeared over the past three years underlines the notion that funding is the key hurdle for more successful female-led startups. After all, this period coincides with venture capital firms' increased awareness that they need more women contributing to investment decisions.

The two trends, more women on corporate boards and at venture capital firms and their growing entrepreneurial success, are likely to result in the same outcome – more wealthy women. This means that wealth and asset managers need to be ready to offer more solutions acceptable to an increasing number of wealthy women.

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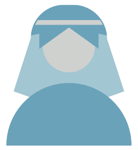
MENA CAPITAL MARKETS OUTLOOK



MENA EQUITIES OUTLOOK 2022

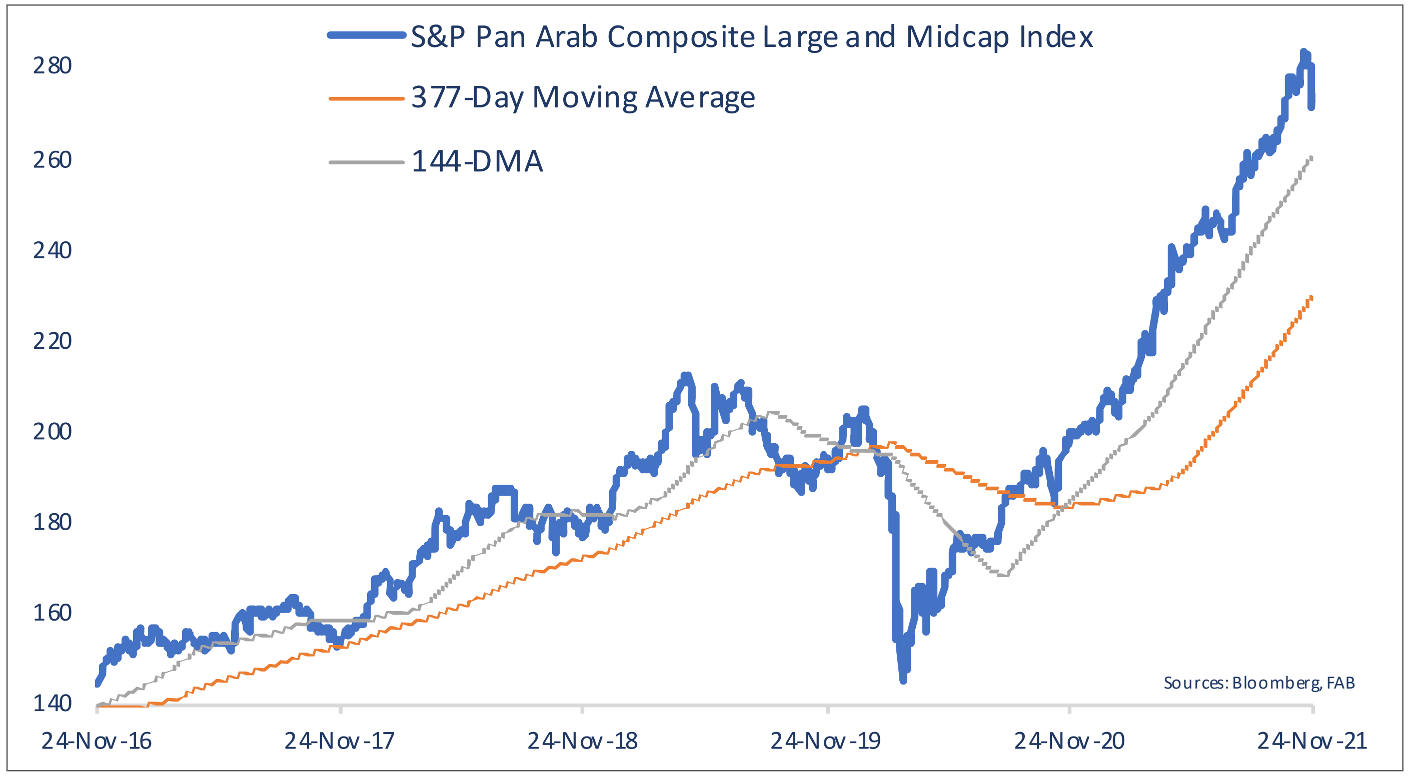
MAKING THEIR MARK WITHIN GLOBAL EQUITIES

By Musa Haddad, Executive Director, Portfolio Manager, FAB Investment Management, and
Rameshwar Tiwary, Executive Director, Portfolio Manager, FAB Investment Management

In 2021, MENA equities as a class delivered a very strong performance compared to global indices after years of underperformance. In fact, they outperformed both the developed and emerging market averages, reflecting a major change in the underlying economic and corporate fundamentals rather than simply higher crude oil prices.

MENA equities, as measured by the S&P Pan Arab Composite LargeMidCap Index, were up by 35.44% for the year to November 24th, 2021, led by Abu Dhabi and followed by Saudi Arabia. The gains were partly driven by higher crude oil prices and quick and effective vaccination campaigns across the region.

During the last year or so, there has been moderate earnings growth although, perhaps more importantly, there was P/E multiple expansion, a sign that global investors have begun to take these markets more seriously. The S&P Pan Arab Composite LargeMidCap Index was trading at a prospective P/E of 15.46x for 2022 based on estimated consensus earnings growth of 10.3%, and 14.1x for 2023 on earnings growth of 9.6% as of the end of November 2021. Average earnings growth in the region can compound in the 9%-11% range, comparing well with developed markets yet with valuations that are attractive in global terms.



MENA equities are entering a new age, and genuine benefits from the diversification away from oil and gas are now taking hold, although hydrocarbons originally financed much economic development and they continue to do so indirectly. MENA equities have, therefore, become worthier of attention from global equity managers.

This was evidenced by the IPO activity, which accelerated sharply in the region last year after years of being lukewarm. Investor appetite appears very strong and is likely to continue. Many more IPOs are in the pipeline, coming mainly from Saudi Arabia and Egypt followed by the UAE.

These new listings improve both supply and demand for future listings, drive better liquidity, create investor optimism, and help the region diversify away from hydrocarbons. This IPO spree will also tend to increase the weighting of the region in emerging market indices, which also increases inflows of passively-managed index funds.

As for the existing stocks, quality banks in Saudi and the UAE look well poised to benefit from a steeper Treasury curve and from more accelerated economic growth. There continues to be rising home ownership and improved potential for corporate business in Saudi, with both elements likely to keep credit demand elevated this year.

In the UAE, banks may benefit from a reduction in the cost of risk as they re-evaluate credit loss models, and a similar possibility exists for Kuwaiti banks. Basically, the higher expected economic growth will result in lower general provisioning, along with higher recoveries of earlier provisions. In Kuwait, banks could benefit from the long-awaited parliamentary approval of mortgage and debt laws too.

The petrochemicals sector is another important driver of MENA equities, in Saudi Arabia in particular. The sector is a huge ‘cyclical swinger’, but its sector earnings may have peaked late last year. Global GDP forecasts are moderating and supply chain disruptions, which contributed to some sharp petrochemicals price increases last year, are expected to normalise as 2022 progresses.

Saudi Arabia

In 2021, the Saudi economy benefitted from higher oil prices, which averaged US$70.5/barrel for Brent for the year to the end of November, compared to only US$46/barrel in 2020. The fiscal deficit for 2021 has officially been revised downwards to 2.7% of GDP, a big improvement on the previous estimate of 4.9%.

While the oil and gas sector expanded, growth in the Saudi economy was actually more driven by non-oil GDP. Overall Saudi GDP growth is estimated to have been 2.6% in 2021, although it is expected to pick up very strongly in 2022 to as high as 7%-7.5% based on official estimates thanks to increased oil production and potentially stable crude prices.

Still, economic diversification has gained momentum in Saudi Arabia with government policies and reforms geared towards reducing the country's dependence on hydrocarbons. Non-oil revenue for the government has been driven by the implementation of a higher value-added tax, which was increased to 15% from 5% in 2020. Accordingly, the value-added tax is expected to have accounted for over 40% of non-oil government revenue in 2021 compared to 25% in 2020 and 19% in 2019.

The government remains committed to increasing home ownership among Saudi nationals with a target of least 70% compared to the current 60%. Mortgage origination and lending to various mega-projects by banks has picked up, resulting in the highest credit growth in the region of close to 15% in 2021.

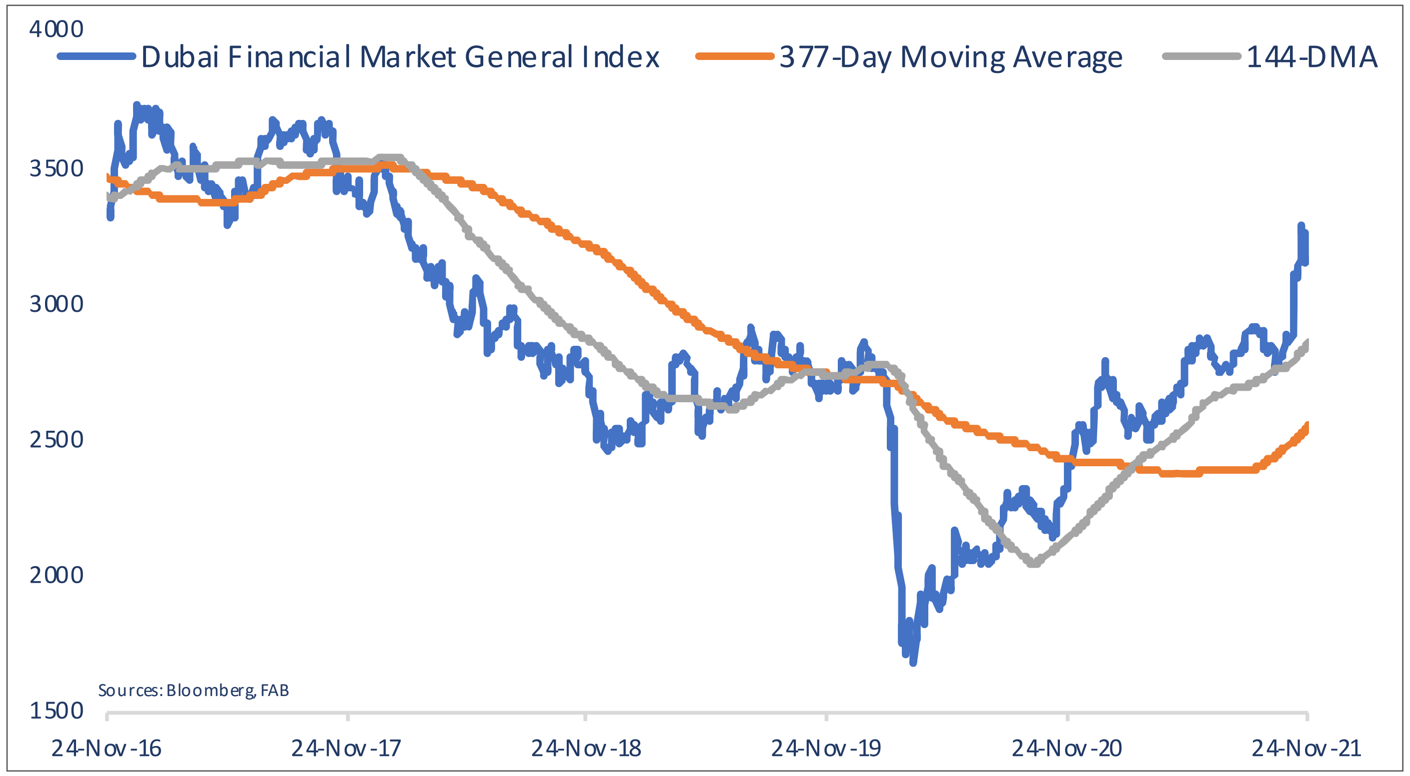
Saudi equities' performance was strong in 2021, and the Tadawul was up by about 30% for the year to November 25th. After such strong performance, it makes sense to be even more selective and expect limited multiple expansion compared to that seen in 2021. Saudi equities are trading on a prospective P/E multiple of 17.7x for 2022, assuming Bloomberg consensus earnings growth of 12% for this year.

United Arab Emirates

The UAE remains a very strong recovery story and the country should stand out in the post-pandemic world. The UAE is a global logistics and transportation hub and a major tourist destination, and it is set to gain significantly from the further normalisation of global economic activity. The vaccination rate in the UAE is one of the highest in the world, and this has been highly supportive of the economic recovery. Expo 2020 Dubai has further strengthened investor confidence.

The real estate market in the UAE was originally impacted by COVID-19 but is now showing good signs of revival with record levels of transactions. The higher demand for real estate has been driven partly by the implementation of many government reforms, including the issuance of long-term visas for expatriates.

In 2021, UAE equities generated high returns. The Abu Dhabi market was up 67.56% and Dubai was up 27.2% for the year to November 25th. Abu Dhabi was trading on a prospective P/E multiple of 17.42x for 2022 based on earnings growth of 6.7% for that year while Dubai was much cheaper, trading at 10.87x for 2022, assuming Bloomberg consensus earnings growth of 23.9%. Similarly, Dubai equities yield 3.89% for 2022, more than a percentage point above Abu Dhabi's yield for this year of 2.77%.



Kuwait

The IMF estimates that Kuwait GDP grew 0.9% in 2021, including non-oil growth of 3%, compared to an overall decline of 8.9% in 2020. In 2022, economic growth is expected to pick up further to 4.3% on the back of normalising economic activity and increased oil production. The ongoing political deadlock between the government and the parliament has resulted in a delay in passing the debt law, restricting Kuwait's ability to borrow from the debt markets. Fortunately, Kuwait had a low debt-to-GDP ratio of 7.9% as of the third quarter of 2021 with a very strong reserve buffer and a low fiscal break-even (including investment income) oil price of around US$61/barrel.

Kuwait is expected to pass a new mortgage law enabling banks to give mortgages directly to customers, which would boost credit and economic growth in the country with at least some similarity to what has occurred in Saudi Arabia.

Kuwait equities are trading at 15.32x prospective earnings for 2022, based on earnings growth (off a low base) of just under 41% for this year.

Qatar

In 2022, Qatar is hosting the FIFA World Cup, providing business opportunities for the hospitality and transportation sectors and investment in infrastructure and stadiums for the event.

Although Qatar has underperformed the regional average, it still rose 17.2% in 2021. Economic growth is expected to pick up in 2022 as the North Field LNG expansion gains traction, which could help valuations. Qatar equities are currently trading on a prospective P/E ratio of 13.3x for 2022, based on Bloomberg consensus earnings growth of 11.71% for that year.

Egypt

Egyptian stocks have lagged behind regional peers in 2021. Economic activity has continued to recover gradually, and the Egyptian pound has remained stable. Revenues from the Suez Canal have recovered to pre-pandemic levels, and tourism has also begun to recover. Compared to history, inflation at just above 6% appears relatively well-controlled, and interest rates are high enough to attract investors seeking carry trades. A new capital expenditure cycle is expected to start gradually as consumer demand recovers with the normalisation of economic activities.

The valuation of Egyptian equities therefore remains attractive, with the local index trading at a 6.58x prospective P/E ratio for 2022, based on consensus earnings growth estimated at 10.8%. Such a low P/E would normally lead to some suspicion; in this case, however, it seems unjustified.

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MENA FIXED INCOME OUTLOOK 2022

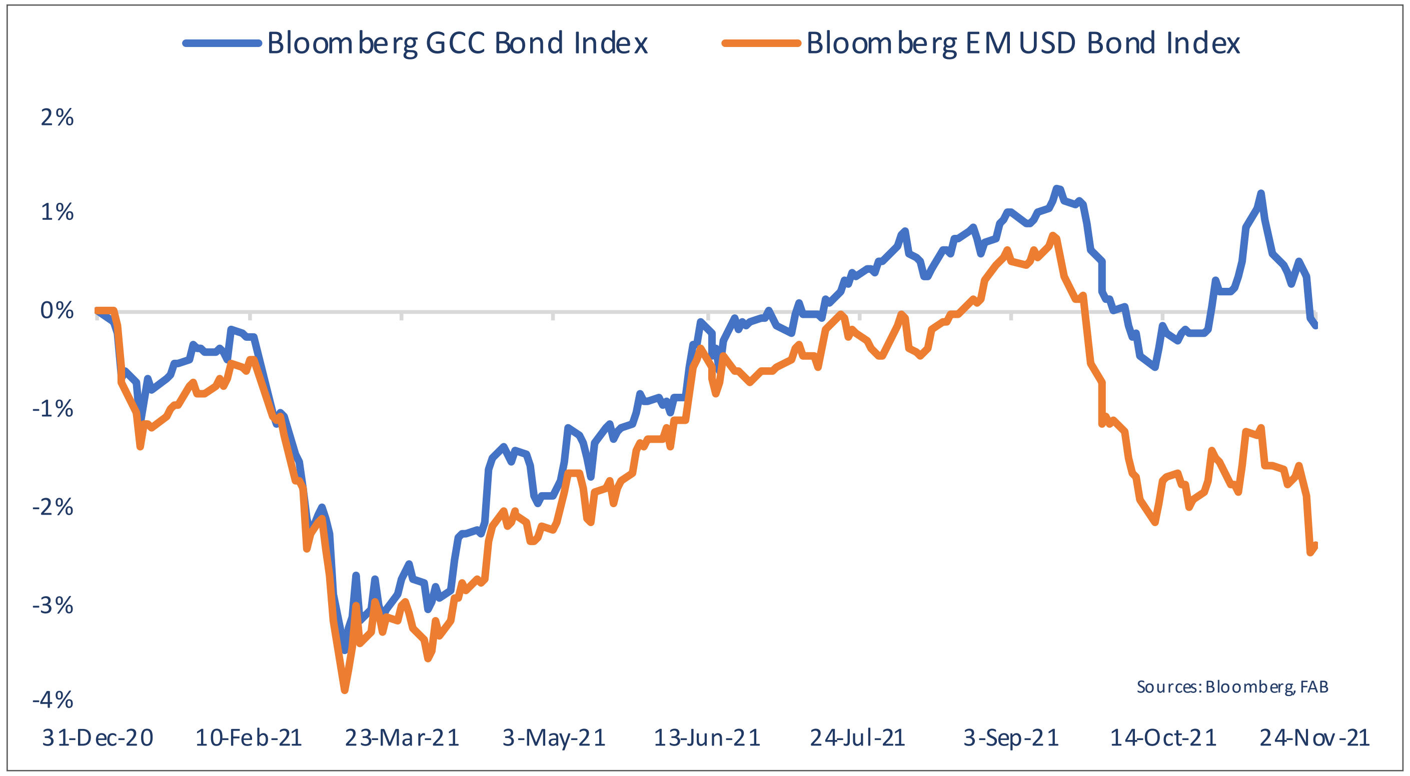
THE REGIONAL MARKETS CONTINUE TO DEEPEN

By Zehan Salleh, Executive Director and Portfolio Manager,
FAB Investment Managament

MENA bond markets enter 2022 on the front foot as the region's economic recovery gathers pace. Successful vaccine rollouts have allowed business activity to reopen faster than in other emerging market countries. Increasing oil output and higher prices will continue to contribute to the region's economic growth and fiscal rebalancing, which bodes well for regional fixed income markets as they continue to expand and develop.

The high-yield credits of Oman and Bahrain were the best performers last year, having delivered 6.6% and 1.4% in returns respectively for the year to mid-November. Together with the UAE, the bonds of these two sovereigns saw their yield premiums drop the most among credits in the region. This was understandable for Oman and Bahrain given that high-yield debt tends to outperform during reflationary times, while the performance of Dubai and Abu Dhabi bonds reflected a mixture of recovery and quality.

While the kind of spread compression seen in 2020 and 2021 may be hard to emulate this year, the picture for MENA fixed income is positive. The IMF has raised its regional GDP growth forecast to 4.1% for 2021 and 2022, the latter being a 0.4% percentage point improvement from the previous forecast. Continued stabilisation of the MENA macroeconomic picture should make global money managers more comfortable investing in what was an under-publicised market until just a few years ago.



The relatively higher yields available in MENA compared to other emerging markets remain underappreciated and should encourage more inflows into the region's markets. With favourable and improving rate and credit outlooks coupled with fundamental improvements (diversification away from hydrocarbons, good 'ease of doing business' scores, widened real estate ownership and residence visa developments), there appear to be substantial reasons to invest in MENA fixed income.

UAE

Higher oil revenues and Expo 2020 Dubai should provide a boost to the UAE's economy over the coming months. By the year's end, the authorities had relaxed almost all pandemic measures, allowing economic activity to accelerate at a faster rate than in most MENA countries.

UAE credit conditions should remain positive overall and credit spreads are likely to grind lower during 2022, especially after the Treasuries market selloff in September and October 2021. Investment grade spreads also widened at the time, providing investors with a favourable entry point into UAE credits. The speed of regional economic recovery and improving prospects for the UAE have not gone unnoticed by the world's major rating agencies, which view Abu Dhabi and the UAE as strong AA credits, and this should entice further capital inflows, leading to possible further spread compression.

The UAE Federal Government also recently did its first bond issuance, which is likely to have set the template for the standard debt vehicle for the UAE federation going forward. Accordingly, UAE bonds (Abu Dhabi, Dubai, and Federation) constitute a very attractive proposition in terms of real total returns, especially when compared to similarly-rated sovereigns in European and Western markets.

Kingdom of Saudi Arabia

Like the UAE, we believe the Saudi bond market will continue to benefit from an improving economic and credit background as the country recovers from COVID-19. Increasing revenues from oil production have reduced the government's borrowing needs, which should support bond prices in 2022. As with the UAE, the rating agencies are becoming far more congenial towards Saudi Arabia, having moved the majority of the countries' credits from negative to stable outlooks, which should add further support to the asset class.

Having embarked on an aggressive reform path with its National Transformation Plan, which was first announced in 2016, the country has clearly demonstrated its commitment to fiscal prudence through direct austerity measures and funding initiatives including asset sales and privatisations. Such funding initiatives will facilitate the entry of international investors, and corporate bond issuances could bring in much required capital.

Directed at the private sector, the Shareek program, which encourages capital investment rather than dividend payouts, clearly acknowledges the natural limitation to financing by the sovereign. In addition, with the Public Investment Fund (PIF) ramping up its domestic investment commitments, the government is serious about facilitating growth and the diversification away from hydrocarbons – all of which should be credit-positive. Investment-led growth is more sustainable, and the dominance of Saudi Arabia in regional fixed income markets puts it in a good position to raise foreign capital for certain investments.

Kuwait

The Kuwaiti bond market could remain vulnerable until the country can convince the rating agencies that it has a comprehensive funding strategy in place. As long as Parliament continues to block the government from borrowing after the expiry of the 2017 debt law, the market for Kuwait bonds will remain under a cloud, likely resulting in further negative ratings actions.

Banks, which make up the majority of the credit issuers within Kuwait, however, have performed well through the pandemic and maintained their asset quality. The central bank has continued to appeal to credit investors with its versatile stance, especially regarding the credit quality of the banks under its purview, and this has been positive for overall investor confidence despite the fiscal logjam.

The issuance of bank perpetual notes from Kuwait remains a popular yield play for regional investors, as they have provided a yield pickup of around 200 basis points over the senior unsecured issues of these high credit quality names.

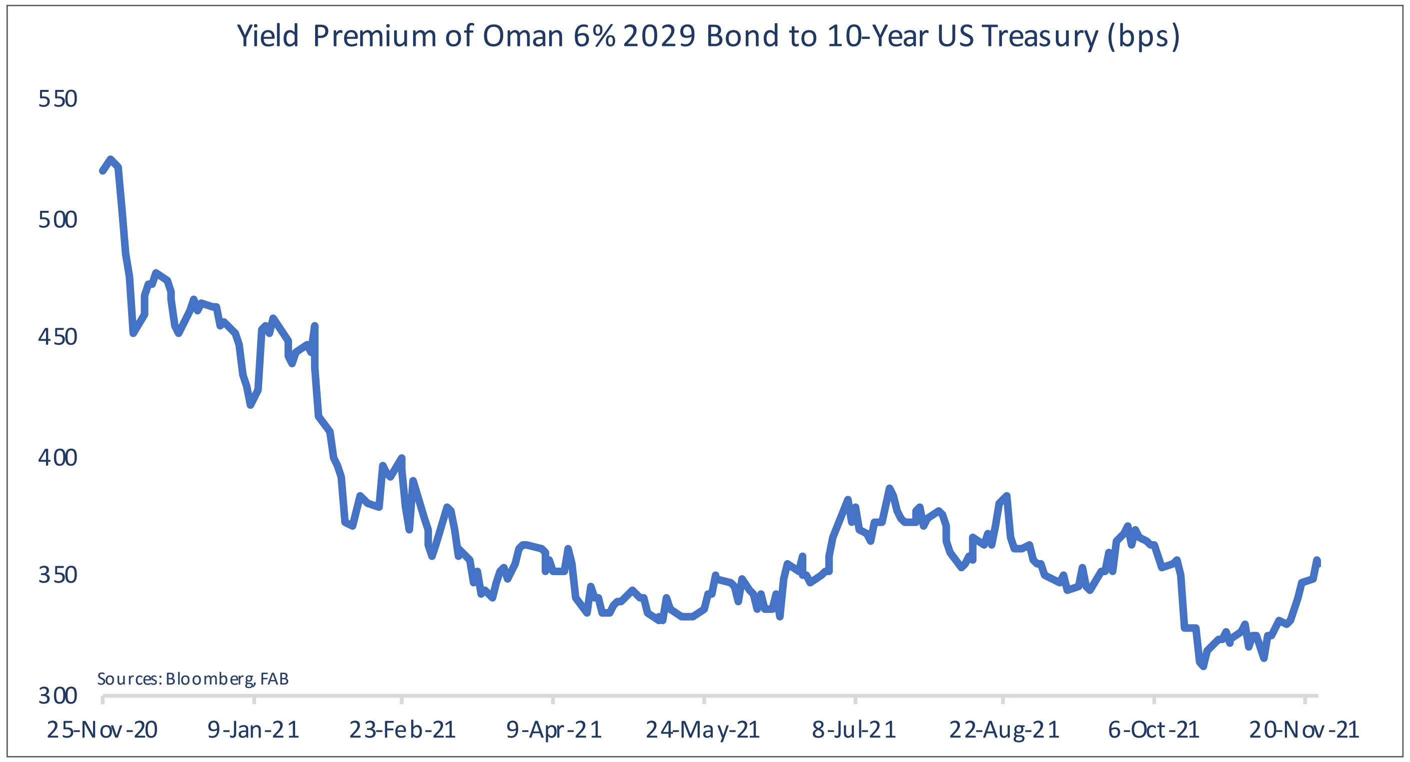
Oman

Oman has enjoyed a renaissance year in terms of performance among regional high-yield credits. Rising crude oil prices have significantly reduced the country's deficit. The government reported a deficit of 1.03 billion Omani Rials in the first nine months of 2021, a 58% drop compared to the same period a year earlier.

After years of reluctance to implement fiscal reforms and austerity measures to curb its twin deficits, Oman finally introduced a value added tax last year and actively cut spending. As a result, rating agencies have moved the outlook on the country's debt to positive.

This helped the yield premium on the country's bonds due in 2032 to tighten by some 80 basis points during the year to the end of November. By November 24th, the premium on these bonds was around 430 basis points, not too far from the spread Oman's 10-year debt paid before the pandemic.

As such, Oman bonds are likely to remain well-supported through 2022 barring any major, unexpected, negative developments in oil markets.



Bahrain

Bahrain has benefited from the recovery in oil prices even if the performance of its bonds has lagged behind those of Oman, the most comparable issuer within the Middle East and North Africa region. The outlook for crude prices remains supportive and so do Bahrain's regional allies, so the country should be able to make progress in balancing its budget by 2024, which should reduce the current yield premiums it is paying in bond markets.

Indeed, the country recently suggested it would consider increasing its value added tax, which would provide more fiscal support to the country.

Given its still high financing needs, Bahrain is likely to remain opportunistic in funding its deficits and refinancing some chunky short-term maturities. The timing of future bond supply will have to be undertaken carefully, however, in what could still be a volatile market environment this year.

Egypt

Economic recovery in Egypt remains slow compared to other major MENA economies. The tourism industry upon which the country relies heavily for fiscal revenue has yet to return to pre-pandemic levels. The country turned to international markets twice during 2021, raising US$6.8 billion in total as it took advantage of lower borrowing costs. This represented significant supply for a country rated in the B category and it added upward pressure to yields.

The IMF expects the country to grow 5.4% in 2022 and 2023, which should help to reduce the country's debt-to-GDP ratio and improve its global credit standing. Therefore, yields could drop this year as the market digests supply and investors continue to hunt for yield.

MENA Bonds and ESG

Despite being viewed by many around the globe as being in primarily a hydrocarbon-based region, Middle East borrowers have been quick to adapt to evolving ESG criteria. MENA governments and corporations are diversifying their economies away from hydrocarbons and improving their reporting on sustainability to maintain future capital inflows.

The UAE and Saudi Arabia recently announced their intentions to be carbon-neutral by 2050 and 2060. While 2050 and 2060 are distant, projects to transition regional economies to 'greener' paths will require substantial financing, much of which should come from bond markets. Indeed, Egypt was one of the first emerging nations to issue a sovereign green bond last year, and such issuance from the region has found healthy investor appetite.

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EMERGING MARKETS OUTLOOK

NIGERIA

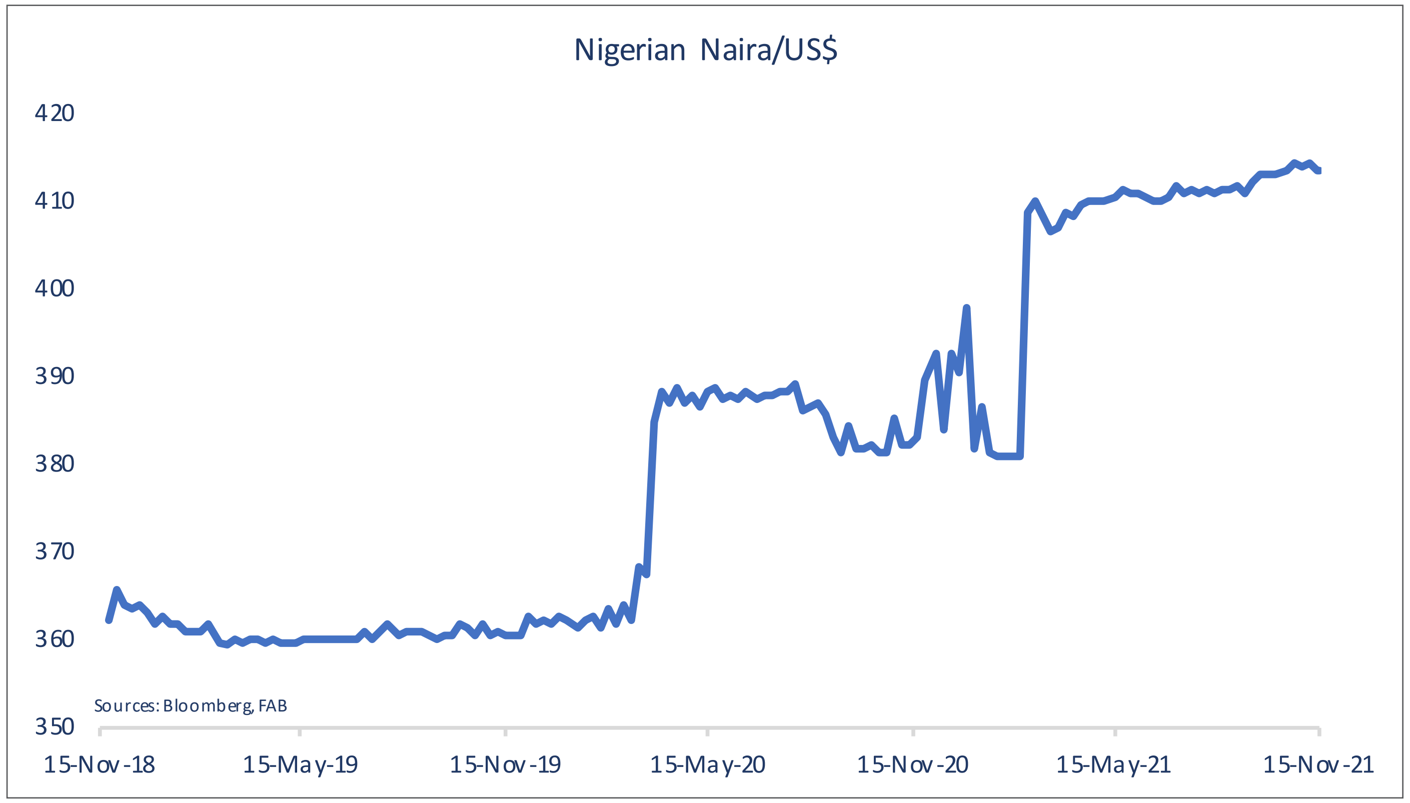
MORE OF THE SAME IN 2022

By Danay Sarypbekov, Executive Director, Global Markets, EM FX and Rates

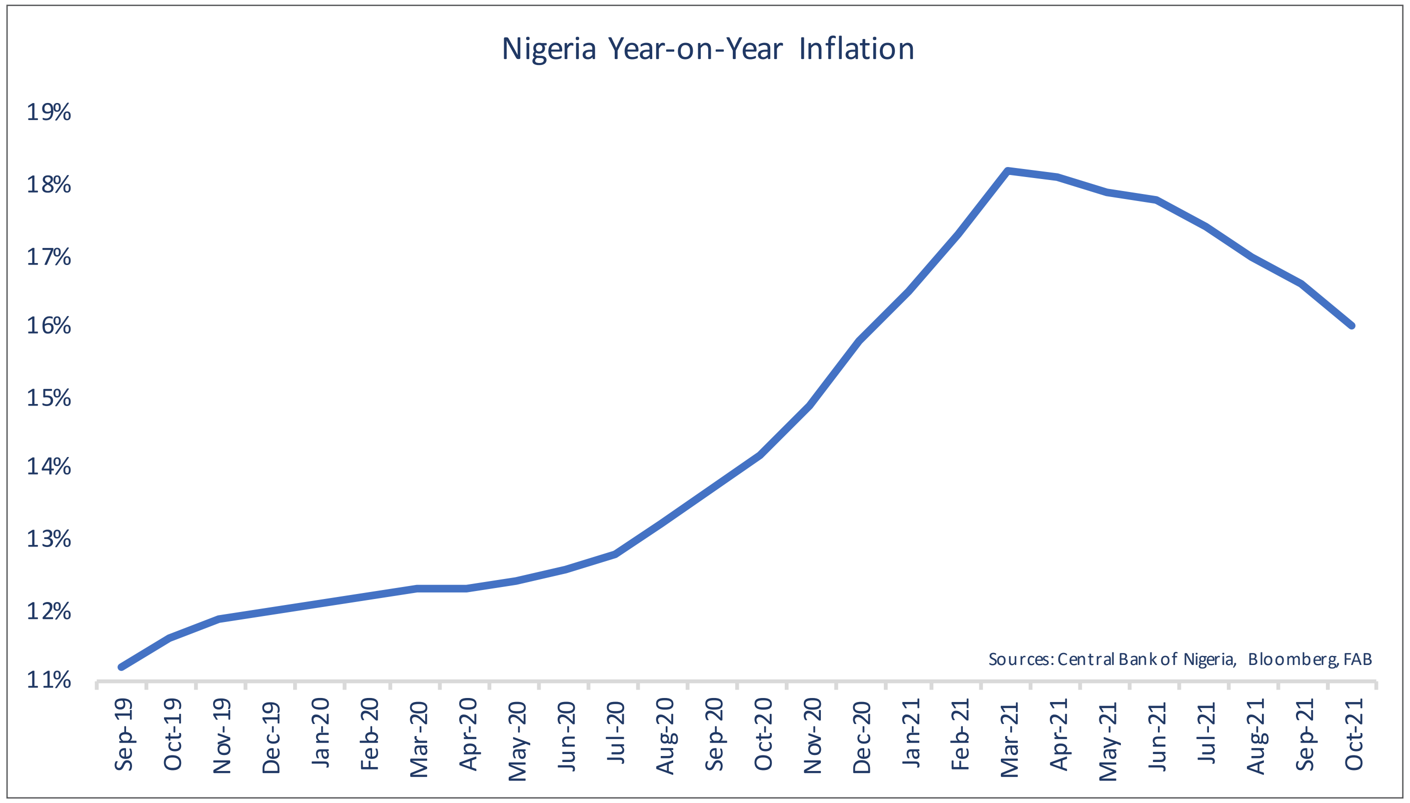
We do not expect major policy changes from the central bank in the largest Sub-Saharan market in 2022. This means that Nigeria will continue to muddle through with its multiple-tier exchange rate market and restricted currency liquidity.

The lack of transparency and the difficulties associated with entering and exiting the naira could prevent many foreign portfolio investors from buying local currency Nigerian assets, and the participation could stay around US$3-5 billion, a level similar to that seen throughout 2021, as opposed to more than US$15 billion in better times.

Higher energy prices are likely to continue supporting the naira and the central bank's foreign currency reserves, which stood at around US$42 billion as of the end of 2021. Despite the rising reserves, the central bank is likely to allow a further gradual depreciation of the local currency to the tune of 5%-10% towards NGN 450-475/US$ during 2022. This would come after the currency depreciated by about 8% against the US dollar since the March 26th, 2020 market sell-off, to about NGN413.75/US$ as of November 15th, 2021.



The central bank has kept negative real interest rates, with the benchmark at 11.5% at the end of 2021. Inflation peaked at 18.13% in March, 2021, and it was at 16% in October. However, if Nigerian inflation fails to fall further and central banks in developed economies start to increase interest rates, the Nigerian central bank could be forced to hike interest rates to fight inflation and remain attractive to global investors in emerging markets.



In any case, more government spending is likely in the fourth quarter of 2022 and the first quarter of 2023 ahead of a general election slated for February 2023. This could entail more borrowing and, by proxy, more pressure on government bonds. However, given the impact of the currency on inflation, the central bank could be more aggressive about selling US dollars domestically around that time as a way of bringing the parallel market rate lower.

Therefore, we believe 2022 could resemble last year for Nigeria in many ways, as this is a giant with immense potential but clay feet.

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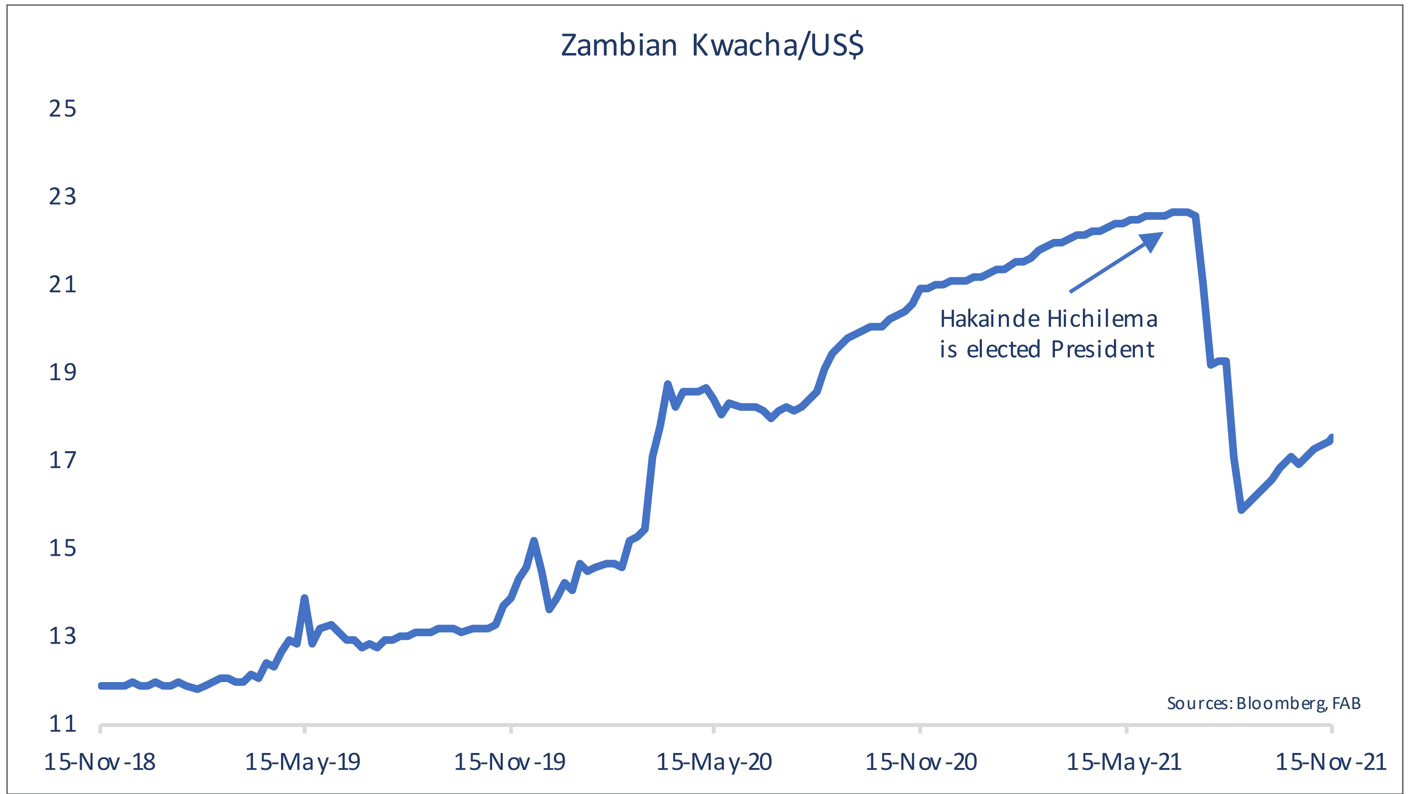
ZAMBIA

HIGH HOPES FOR HAKAINDE HICHILEMA

By Danay Sarypbekov, Executive Director, Global Markets, EM FX and Rates

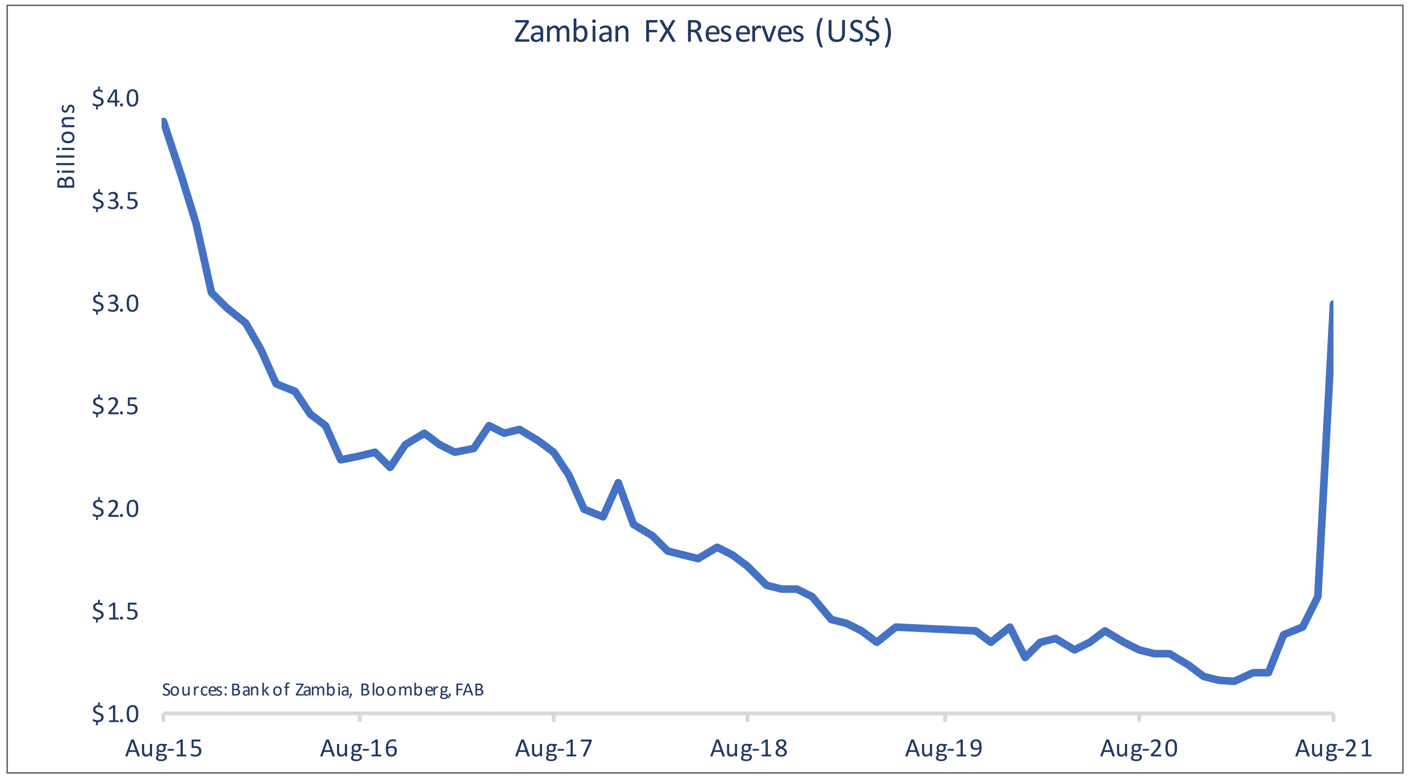
Zambia is probably the African market with the highest potential to make a big comeback in 2022. In 2020, Zambia defaulted on its external debt in the midst of the pandemic, its GDP shrank by almost 5% and the kwacha depreciated by more than 50% versus the US dollar.

Last year, Zambians elected Hakainde Hichilema from the United Party for National Development as President, ending a decade of government by the Patriotic Front party. Hichilema has a business background and has promised to make the country more business-friendly for domestic and foreign-owned companies. He has been holding regular 'meet-the-president' dinners with businesspeople and trying to promote more technocrats to key positions.



His electoral victory was celebrated by markets, and the local currency has strengthened from a record weakness of around ZMW22.75/USD$ to about ZMW16/US$ since former President Edgar Lungu conceded victory to Hichilema. This optimism is partly based on hopes that the new government and the IMF will reach an agreement for a funded reform programme that would facilitate the country's debt restructuring.

The plans to improve the country's financial standing include increasing mining exports. In line with this, the Finance Minister announced last year that Zambia aims to increase copper production, its main source of hard currency, from around 900,000 tons per year presently to 2 million tons in 2026. This would elevate Zambia to the position of third largest copper producer behind Chile and Peru.



In our view, in 2022, the kwacha is expected stabilise in the range of ZMW16- ZMW19/US$, and could potentially appreciate beyond the ZMW16/US$ level if reforms accelerate, copper prices rise, or the IMF agrees on a funded reform programme with the country. Inflation probably peaked in the summer of 2021 and should continue to fall towards a lower range of 10%-15% over the course of this year because of base effects and a more stable currency exchange rate. However, the Bank of Zambia may still need to hike rates by 1-2 percentage points from the current level of 8.5% even if inflation retreats, given that interest rates are currently in deeply negative territory. This would be particularly true if global central banks, especially those in advanced economies, keep hiking rates.

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EMERGING MARKET EQUITIES OUTLOOK:

SOME THINGS LOOK CHEAP FOR A REASON

Abhishek Shukla, Executive Director, Head of Investment Research, FAB Investment Management and
By Rameshwar Tiwary, Executive Director, Portfolio Manager, FAB Investment Management

Historically, EM equities enjoyed a bull market every five or six years, often as a lagged 'high beta' play following positive performance in developed markets. At this time last year, it seemed like EM equities' time had arrived, but that turned out to be a mistake, with the exception of India. With the benefit of hindsight, the last EM equity bull market peaked on 17 February last year led by regulatory developments in China.

Also, while huge global monetary accommodation provided a supportive backdrop for EM economic stabilisation, there was an unequal global rollout of COVID-19 vaccines across EM and, therefore, the economic equality gap within it has worsened.

The US dollar was also a drag on the asset class. It could continue to see moderate strength versus most EM currencies until at least mid-year, after which it may weaken as November's American mid-term elections approach.

The Chinese yuan, which was trading around CNY 6.39/US$ towards the end of November, 2021, having strengthened from close to CNY 7.17/US$ at the end of May, 2020, has been one of the key stabilisers for EM currencies overall. The appreciation has allowed China to avoid the moniker of 'currency manipulator', but could have run its course with the CFETS yuan index hitting all-time highs last year. If the Chinese currency reverses course, that could bring forth another period of EM currency weakness.

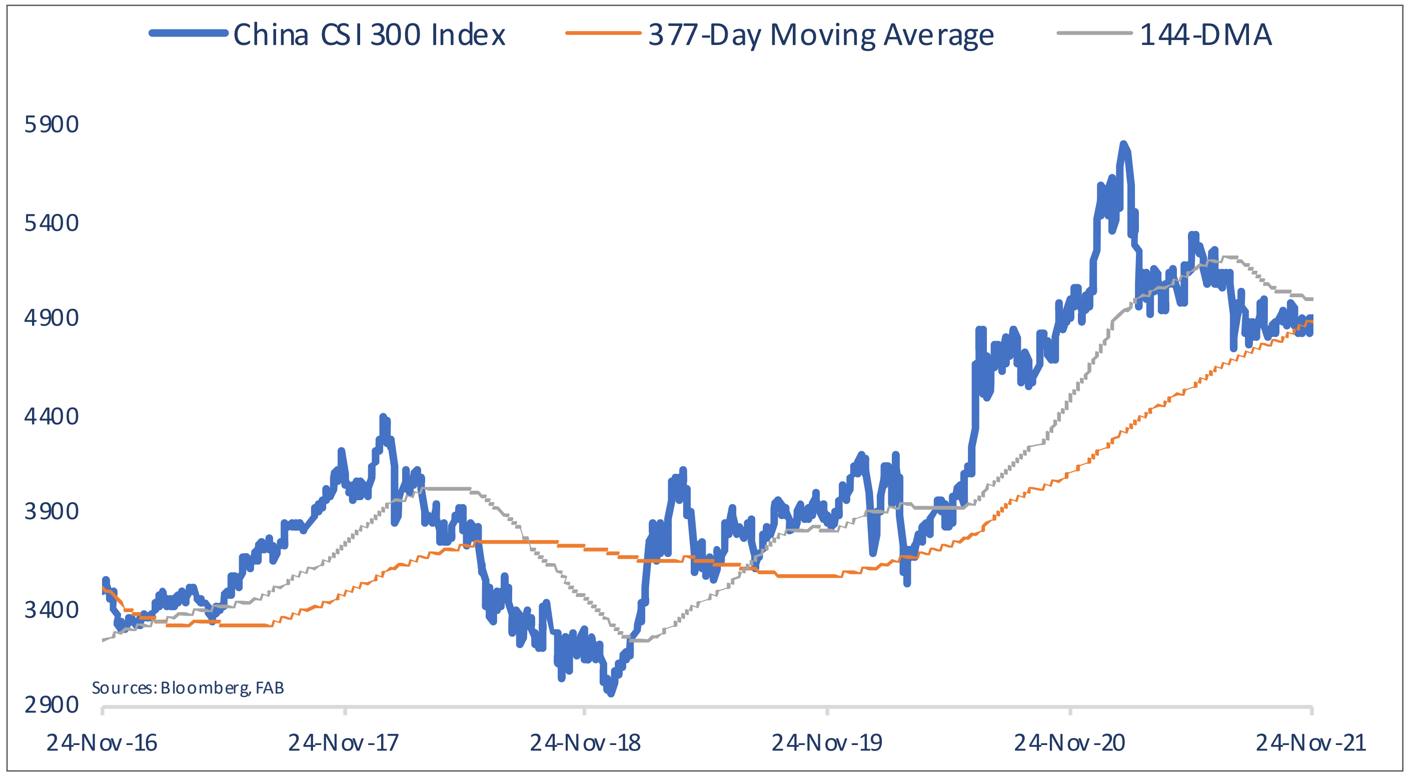
Global allocators should probably always expect EM equities to trade at a large discount to developed country equities, and last year was a salutary reminder of this – the only apparent exception being India. Indeed, around the end of November 2021, the CSI 300 index of Chinese stocks was 6.16% lower in local currency terms and down 4.11% in US dollar terms for the year. Driven by its exposure to semiconductors, Taiwan was 19.5% ahead in local terms. Indian equities were up 24.89% in local terms. At the other end of the scale, Brazil (as measured by the Bovespa Index) was down 13.43% in local terms and 19.94% lower in US dollar terms given the depreciation of the Brazilian real.

In its October update, the IMF wrote that it expected emerging economies to grow 6.4% in 2021 followed by 5.1% in 2022. The IMF, however, is likely to revise its China forecasts downwards as the 8% expansion forecast for 2021 and 5.6% for 2022 were already out of date when they were published. The China Caixin Composite PMI for October came in at 51.5, registering moderate industrial expansion confirmed by the official equivalent data at 50.8, and these taken together might equate to current annualised GDP growth of 2%-3%. Accordingly, EM growth should come closer to the IMF forecasts for advanced economies, which stand at 5.2% and 4.5% for those years respectively.

The Bloomberg consensus earnings estimates for Chinese stocks and hence the MSCI EM Index are by their nature rather faster-moving than GDP data. In late 2021, market earnings expectations for EM equities as a class for 2022 and 2023 were for growth of 5.5% followed by 10.2% for those years for prospective P/E ratios of 12.63x and 11.46x respectively. This compares to 6.5% for developed equities for 2022 followed by 8.1% for 2023.

Expected corporate earnings growth is therefore expected to be one percentage point lower for EM than for developed countries in 2022, and just over two percentage points better in 2023. Based on the consensus, therefore, the discount of EM equities to developed markets from a forward price-to-earnings perspective is 33.6% for 2022 and 34.9% for 2023.

It may sound like a steep discount, but it does not automatically make EM equities cheap. Historically, it was correct to overweight EM equities when their prospective price-to-earnings discount to developed markets reached approximately 25%-26%, and to consider taking profits when the discount shrank to about 17%-18%. However, Chinese equities may have been the key to the gaping discount last year, and there is still plenty of uncertainty about Beijing's policies.



The recent country constituents of EM equities as defined by MSCI are as follows: China (32.47% of the total); Taiwan (14.66%); India (12.05%); South Korea (11.80%); Brazil (3.88%); Russia (3.68%); Saudi Arabia (3.38%); South Africa (3.02%); and Hong Kong (2.12%); followed by the UAE; Qatar; and Kuwait at sub-1% weights.

Although China is by far the largest constituent of EM equities, it represents just 3.76% of global equity capitalisation as measured by the MSCI All Country World Index (down from close to 4.8% a year ago). EM equities therefore represent just under 11.6% of global equity value, a relatively small amount. The sectoral allocation across EM equities is as follows: Internet (14.88%); Semiconductors (13.42%); Banks (12.18%); Oil & Gas (5.25%); Financial Services (4.76%); Telecoms (3.72%); Autos (3.24%); followed by Chemicals; Retail; and Computers.

Even after the fall in the market values of the largest-cap Chinese technology stocks, technology remains dominant, and a far cry from the 'Old EM World' in which basic materials dominated.

China

China's tougher regulation of education and tech companies plus the woes of its property sector have taken a toll on the market. Earnings estimate revision trends for China's CSI 300 Index, for instance, are still weakening, and Bloomberg consensus earnings growth estimates of 15.8% and 13.9% for 2022 and 2023 respectively, which imply forward price-to-earnings ratios of 13.45x and 11.81x for those years, may be too bullish.

Taiwan

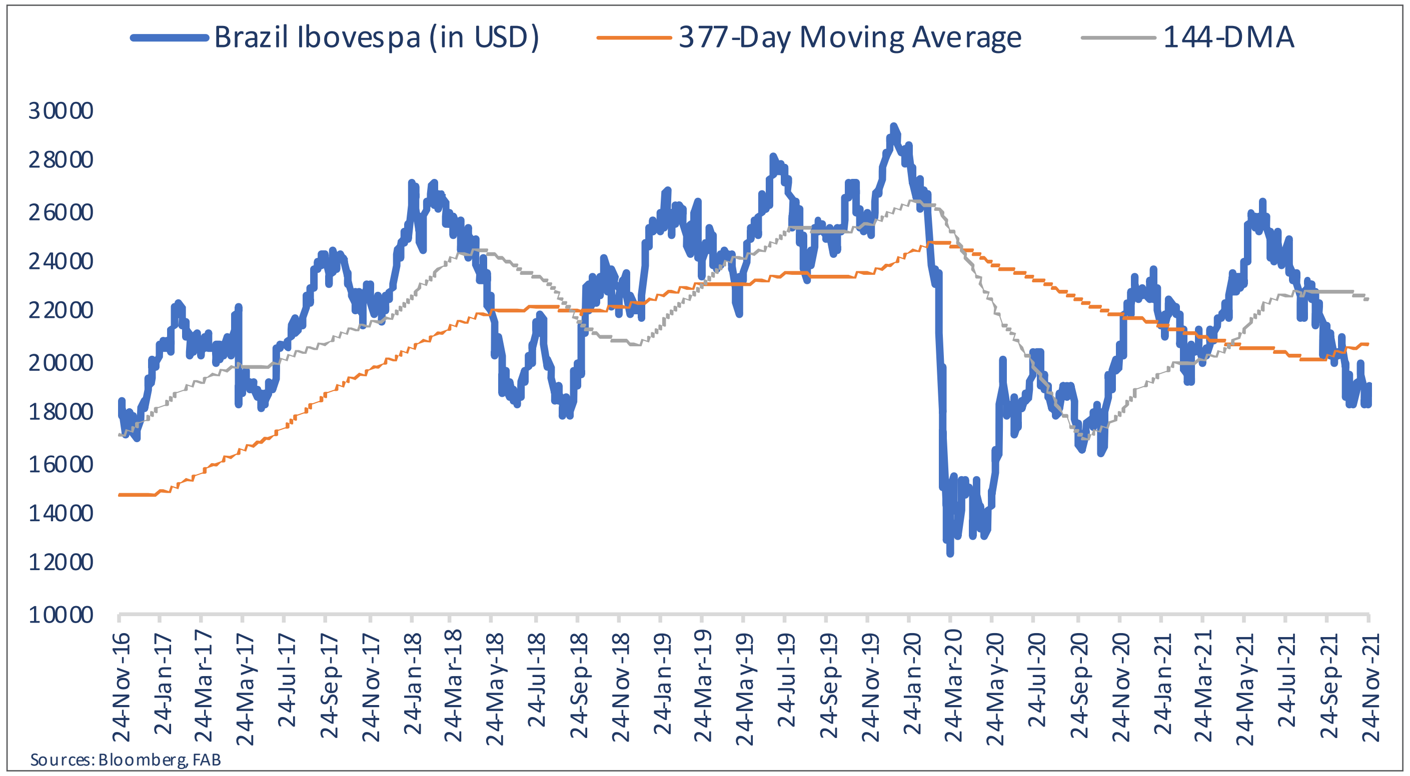
The second-largest member of the MSCI EM is Taiwan. The IMF expected its growth to be 5.9% in 2021, moderating to 3.3% in 2022. As with China, those estimates may be on the high side. According to the Bloomberg consensus, earnings for the MSCI Taiwan Index are expected to drop by 1.07% in 2022 followed by growth of 5.1% in 2023. The resulting P/E ratios are 14.96x for 2022 and 14.23x, respectively. These estimates, driven by semiconductors, make sense, but the appropriate political risk discount for Taiwan is unclear.

South Korea

The MSCI South Korea Index was trading at 10.55x earnings for 2022 in November, based on a forecast earnings contraction of 4.4%, resulting from continued supply chain disruptions and especially affecting semiconductors (which account for 28.1% of the index). Earnings growth is slated to resume at 9.4% in 2023 for a prospective P/E of 9.64x, with the low P/E probably reflecting cyclicality.

Brazil

The MSCI Brazil Index is, according to the Bloomberg consensus, priced for an earnings contraction of 14.1% in 2022 followed by earnings growth of a lowly 2.7% in 2023 for P/Es of 7.36x and 7.16x respectively. In this instance, part of reason for the P/Es being in single-digits presumably reflects uncertainty regarding the currency outlook derived from the politics around presidential elections in 2022.



India

According to the IMF, India's real GDP is expected to grow at 9.5% and 8.5% in fiscal 2021-22 and 2022-23 respectively, and it could be one of the fastest growing economies globally. India could generate compound growth of as in 5%-6% per year for the next few decades. The country should become a US$5 trillion economy by 2024-25 and, by 2030, it could become the world's third largest after the US and China, a leap from its current position as sixth. The middle class is growing strongly, fuelled by urbanisation, and the economy is benefitting from rapid digitisation and new technologies.

Among emerging and developing countries, India is the largest exporter of services within a grouping known mostly for exports of manufactured goods or commodities. Annual exports of close to US$310 billion are driven primarily by software services. India's foreign reserves are at an all-time high of US$642 billion equivalent, US$60 billion of which was added during the first seven months of fiscal year 2021-22.

Inflation can be a problem at times, and and was running at 4.5% in October, 2021. However, this is a phase that successful emerging countries tend to go through while they develop and assets get allocated. If oil prices move higher, inflation could be higher than is desirable and could lead to higher interest rates. On the other hand, India's economy has been quick to recover from the pandemic with more than 1 billion doses administered and around 500 million people fully vaccinated as of the end of November 2021.

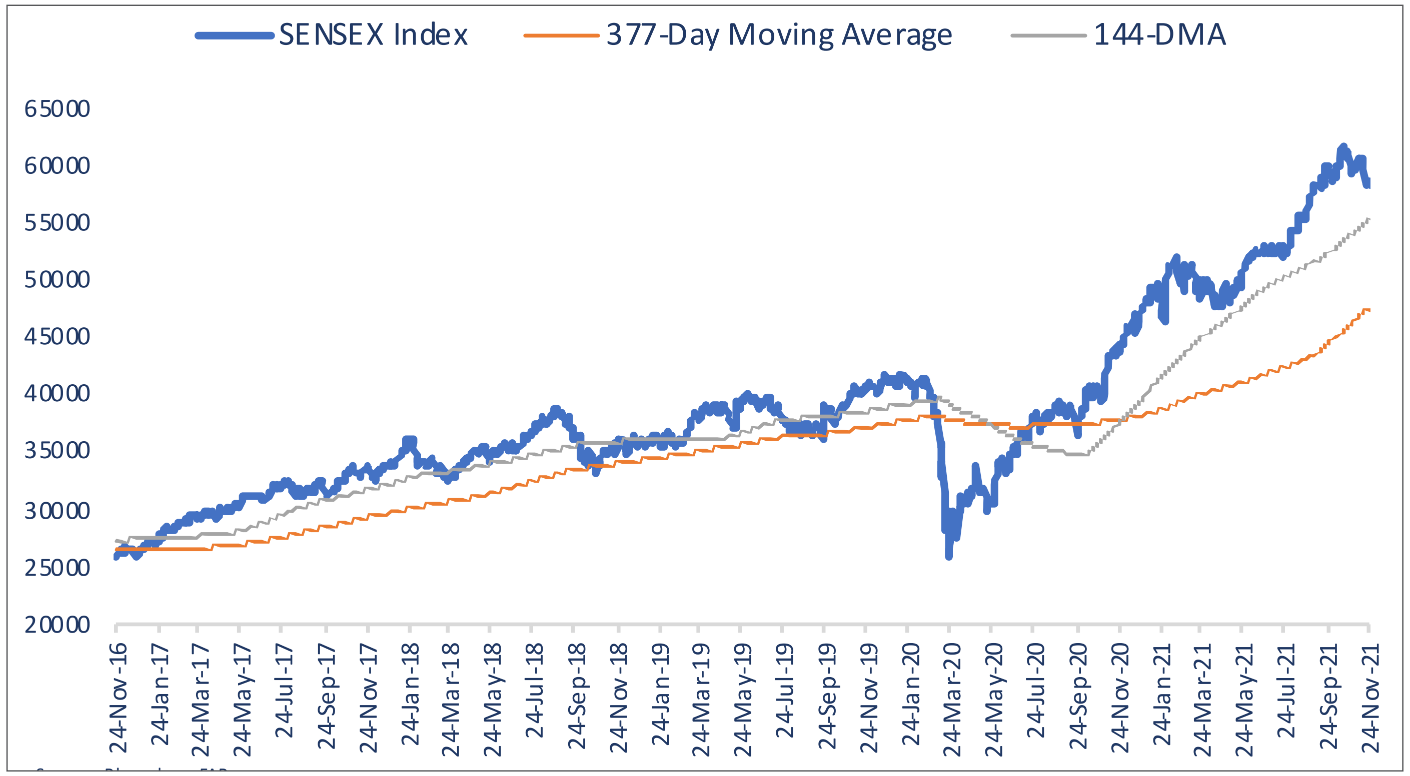
India is generating many exciting business start-ups, and recently had more than 70 'unicorns' (defined as young companies that achieve a valuation in excess of US$1 billion), with the potential for this number to grow continually in the years to come. Unsurprisingly, many of these are new generation technology companies. Indian companies tend to be well-managed and borne out of a uniquely entrepreneurial mindset. India is a global leader in software, pharmaceuticals and automotive-ancillary industries.

An increasing number of first-time investors are entering the market as reflected in the 14.2 million new domestic accounts opened in fiscal 2020-21, taking the total number to 70 million. Furthermore, systematic investment plans alone result in about US$1.3 billion of monthly inflows into mutual funds, and this reduces market volatility. Previously, the market was overly-dependent on net foreign inflows.

Given the high returns on equity (often higher than 20%) achieved by many quoted companies, Indian equities have traded at a premium to other emerging markets and forward P/E ratios of 20x or above for India have become the norm. Seasoned investors know this underlines investor confidence, sound regulation, transparency and good corporate governance.

India was one of the best-performing markets last year, with the S&P BSE SENSEX Index up by 23% in early December. Over the past 10 years, the Indian market has generated close to a 10% compound annual return in US dollar terms, compared to 5% for the MSCI EM Index.

In Indian equities, the Bloomberg consensus for earnings growth on the SENSEX Index stands at 17.4% for 2022-23 followed by 15.6% for 2023-24, resulting in P/E ratios of 21.63x and 18.70x respectively. That does not look expensive, and it merely underlines the growth that is likely.



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EM LOCAL CURRENCY DEBT COULD RETURN TO THE FORE LATER THIS YEAR

By Chris Langner, Acting Head of Investment Strategy, FAB Private Banking

Last year was not the best for bonds, and emerging market debt was not immune to the overall trend. By November 17th of last year, the Bloomberg EM US Dollar Bond index was down by 1.75%, and that was a recovery from last year's low hit on October 12th, when the index was down by 2.15% for the year.

Much of that drop was a result of falling US Treasuries, and an index of the American government bonds compiled by Bloomberg was down 3% for 2021 as of November 17th. As the numbers suggest, however, emerging market bonds outperformed the world's safest securities last year.

Part of the reason for that is because emerging market bonds offer higher yields, and are therefore less sensitive to changes in interest rates. This is an important consideration for the year ahead as analysts are split about the direction of interest rates in the US after inflation in the country hit the highest level in 30 years in the fourth quarter.

Whether the Federal Reserve caves to pressure from markets to hike rates this year will have a major impact on the performance of all emerging market assets, which tend to be quite sensitive dollar benchmark rates. Local currency debt, which fared even worse than foreign currency bonds of developing nations last year, could react even more strongly to a sudden hawkish turn at the Fed given the potential for the dollar to strengthen as a result.

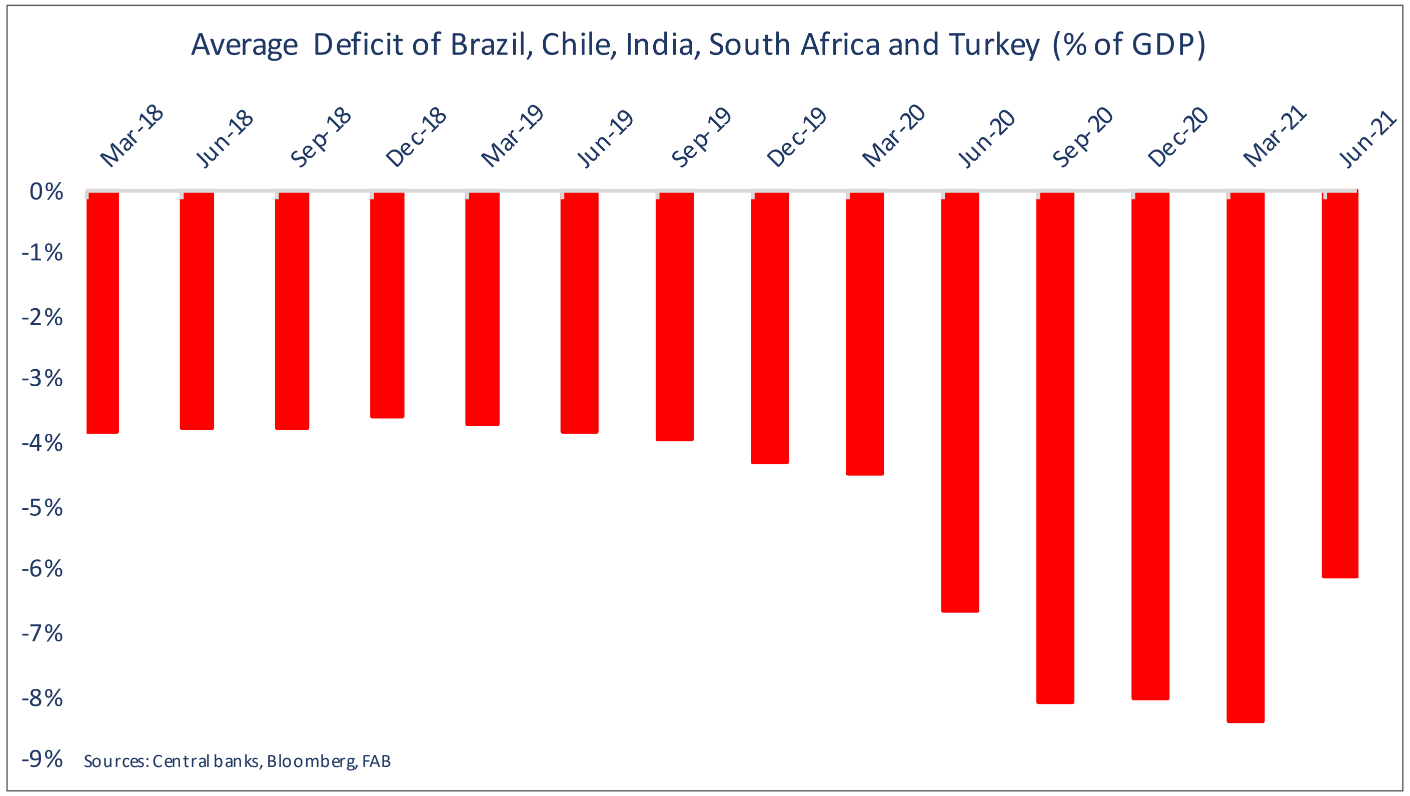
The opposite is also true. The market had priced in three interest rate hikes this year at the end of 2021, and this was reflected in asset prices, from Fed fund futures to the US dollar. If inflation tapers off as it seems it could, and the Fed can hold its fire on interest rate hikes, emerging market bonds are likely to do particularly well. In fact, certain local currency developing nation bonds, which have lagged broader markets for years, could become particularly attractive towards the second half of this year.

This is because many of the developing nations' central banks have already started to hike interest rates, and many of these governments have also started to tighten their purse strings. This means lower growth for now, which may weigh on local equity markets but also mean a progressive improvement of credit metrics. As fiscal and current account deficits become smaller or even convert to surpluses, government bonds of these countries will become more attractive, particularly local currency ones.

Emerging market currencies have suffered since the first quarter of 2018 when the trade war between the US and China began. Between April 3rd, 2018, its previous peak, and November 17th, 2021, the MSCI EM FX index gained only 0.27%, and that was mostly thanks to a 4.73% rally since the end of October 2020 when news of a potential vaccine first hit markets.

For now, the momentum remains against them, particularly as the US dollar has been on a strengthening path as more investors consider the possibility that the Fed will increase rates next year. However, the credit metrics of emerging countries have already started to recover.

Between the end of the first quarter of 2020 when the pandemic began and the same period in 2021, the average budget shortfall of Brazil, Chile, India, South Africa and Turkey nearly doubled to 8.38% of GDP from 4.44% (these countries have more timely data). By the end of the second quarter of 2021, according to the latest data available as of writing, the mean deficit had fallen to 6.12% of GDP.



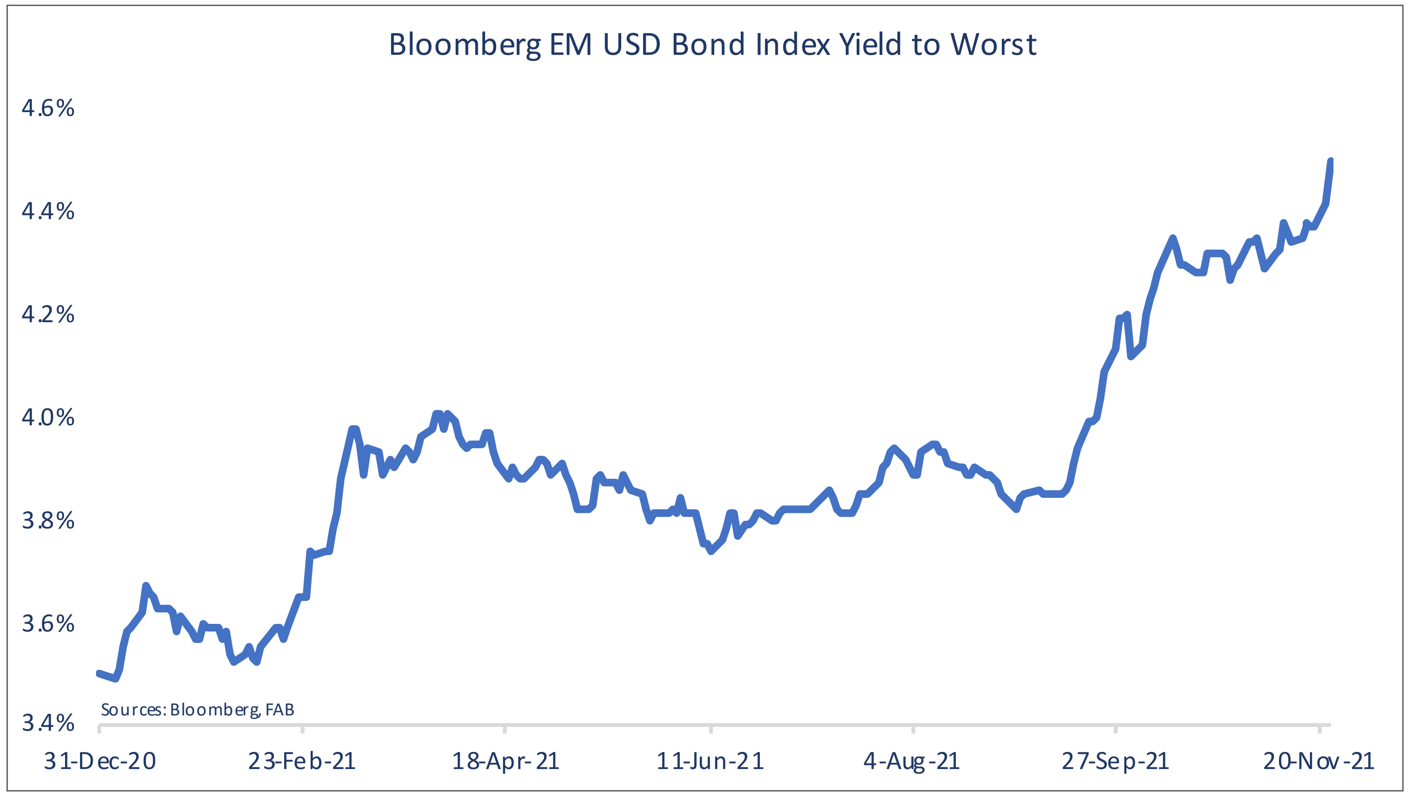
The trouble is that because deficits increased so much, they had a major impact on the debt-to-GDP ratios of these countries. To put this in perspective, South Africa's total government debt amounted to 57.4% of its GDP at the end of the first quarter of 2020 — it jumped to 70.7% one year later. It had started to retreat to 68.8% in the second quarter of 2021, but it still had a long way to go to return to pre-pandemic levels.

The jump is also partly a result of the currency depreciation some of the countries suffered. The Brazilian real, for one, fell 9.07% between March 26th, 2020, when the big COVID sell-off happened, and November 17th, 2021. This made the accounting and servicing of Brazil's foreign debt more expensive.

This higher cost, however, could also curb foreign issuance of additional foreign debt for some emerging market countries this year. That had already begun last year. Between January 1st and November 24th of 2021, Bloomberg recorded 129 sovereign dollar-denominated bond issues amounting to US$132.87 billion. This amount was a nearly 27% drop compared to the US$181.3 billion issued in the same period in 2020 according to Bloomberg data.

This dynamic could mean that the foreign currency debt of emerging markets becomes attractive earlier than local debt. Indeed, the dollar-denominated debt of emerging countries will probably become quite attractive as soon as global markets have some more clarity on the direction of US interest rates.

The yield premium on the Bloomberg Emerging Markets US Dollar index increased by about 50 basis points between February 25th, 2021, when it hit 263 basis points, the lowest since 2018, and late November 2021. In the meantime, the yield on the seven-year US Treasury, the benchmark for the EM USD index, increased by 35 basis points, suggesting the average absolute yield of emerging market dollar debt increased by about 85 basis points in the period. There could be some more to go, but foreign currency developing nation debt was looking increasingly attractive towards the end of 2021 given the prospects of lower issuance, improving credit metrics and higher yields.



To be sure, averages can be tricky, and one of the points of pressure that contributed to the overall increase in emerging market dollar-bond premiums was the situation of Chinese high-yield debt. The troubles of the world's biggest developer, China Evergrande Group, had a major impact on Asian junk bonds, pushing the average yield of the Bloomberg Asian High-Yield Bond Index to 13.57% on November 9th 2021. The index had started to recover and the average yield had dropped to 11.8% by the end of November.

It had spilled into investment-grade too, and the yield premium on the Bloomberg Asia USD Corporate Credit IG rose nearly 50 basis points between September 13th and November 9th of last year. This space, too, had started to recover towards the end of the year.

Yet, Asian bonds could still represent an opportunity despite the recent recovery and even if China is removed. From an economic standpoint, the region is likely to show the strongest growth among developing nations in 2022, given that it was the slowest to reopen and, therefore, is likely to see a boom once full economic activity resumes.

This could also mean a short-term spike in inflation, as was seen in other parts of emerging markets last year, and some monetary tightening in the likes of Indonesia, India or Malaysia. Yet overall, it points to a more positive environment for Asian credit this year. And when Asia does well, all other emerging markets tend to as well.

Again, assuming Asia manages to reopen by the second half and that, at this point, the US dollar has started to reach its apex along with the tightening cycle for many western emerging market central banks, local currency bonds could become a very attractive proposition late this year.

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DEVELOPED MARKETS OUTLOOK

GLOBAL RATES OUTLOOK 2022

FROM FAMINE TO FEAST?

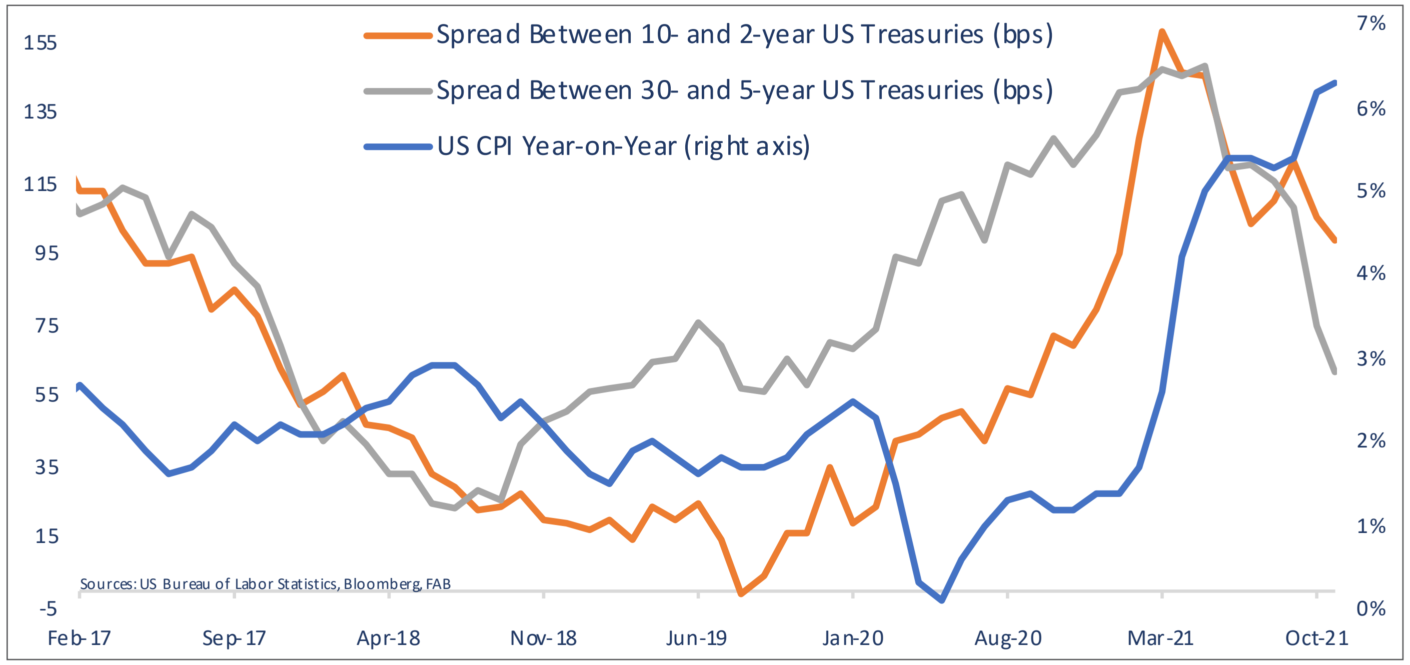
By Simon Ballard, Chief Economist, Market Insights and Strategy, FAB Global Markets

- Rates are poised to bounce off the zero bound even as the pace of reflation eases.
- Generic yields should rise, curves modestly bear-steepen over the course of 2022.
- 'Cautious optimism' should be the buzz phrase of macro conditions.
- When it comes to inflation, 'temporary' is a matter of perception.
- Fed hawks may be cohabitating with ECB doves throughout the coming 12 months.

As we traverse what we hope will continue to prove to be the post-pandemic terrain, global financial markets will position themselves with respect to prospective economic growth and inflation conditions over the coming year. We have long argued that the strongest V-shaped element of the recovery may lie behind us in 2021 and that the trajectory of recovery in the coming quarters may be more shallow U-shaped in nature. We expect this moderating recovery projection to hold true for growth as well as inflation over the coming year.

This said, even assuming that initial rebound momentum fuelled by loose monetary and fiscal stimulus begins to wane in the months ahead, we do expect robust reflationary growth levels to be maintained overall through 2022, subject to the well-documented caveats. The net result of this is that nominal policy rates across most developed economies now appear poised to bounce off the zero bound that is still largely priced into the rates market. This will lead to a gradual rise in generic yields and a modest bear-steepening of yield curves over the course of 2022.

US 2s/10s, 5s/30s yield curve vs. US CPI 'Rethinking reflation'



The foundations for reflation are well known – strong and successful COVID-19 vaccination programmes, a reopening of economic activity and consumption and solid inventory building across most sectors, but so are the risks (virus variants, economic uncertainties, fragile labour market conditions). As such, the inference in this is that the path of least resistance for global rates over the coming quarters should be tentatively higher. 'Cautious optimism' should remain the buzz phrase of the macro rates outlook in 2022.

During the second half of 2021, it seemed that global investor sentiment was steadily being conditioned by central banks for an impending turn in the monetary policy screws. Elevated inflation rates around the globe, while perceived as 'transitory' by several major central banks including the Federal Reserve and ECB, continued to fuel bond market fears that monetary authorities' hands would be forced earlier and more acutely than previously anticipated. At the same time, such anxieties have pushed many market participants to the sidelines, thereby draining the market of liquidity and fuelling outsized volatility across risk assets.

Meanwhile, though, fiscal policy seemed and still seems set to remain ultra-loose during 2022, albeit with governments becoming increasingly cognisant of the structural debt pile that is being accumulated as a result of their emergency pandemic rescue packages. Indeed, it was the recognition of this debt position coupled with current high inflation that led the Federal Reserve to announce the tapering of its asset purchase program at the conclusion of its November 3rd, 2021 FOMC meeting, though it left underlying interest rates unchanged. The Fed aims to have concluded the tapering by early 2022.

At the same time then the Fed was keen to reassure markets that tapering did not predetermine the start of rate tightening. In December, however, the central bank made it clear that it plans to hike rates this year, perhaps starting in March. As reflation gathers momentum, the spectre of possible monetary and fiscal policy 'normalisation' during the course of 2022 will now surely cast an increasingly opaque veil of uncertainty across global markets over the coming months.

With markets having learned to live with and depend on not only a near-zero interest rate environment for much of the past two years but also deep structural stimulus in the form of quantitative easing, fears over how global markets might survive once tighter conditions prevail have begun to grow. With inflationary pressures seemingly building by the day, albeit what is still expected to be largely transient inflation in our view, it is perhaps a natural question to ask.

While the Federal Reserve has begun the process of tapering its asset purchase program, and is signaling a rate lift off soon, it may end up moving slower than the market seems to expect. In the context of fragile reflation and the prospect of easing price pressures over the coming months, we would conjecture that the timeline for more Fed tightening may edge back toward early 2023.

US money market futures in December 2021 saw some 95 basis points of tightening priced into the US curve by the end of 2022.

While current inflationary pressures are unarguably elevated, we still subscribe to the view that they will prove to be transient in 2022. Nonetheless, in order to avoid a more disruptive, hawkish outcome, we believe that it was appropriate for the FOMC to ratchet up the pace of its taper process in the early months of 2022 in order to send the correct 'we've got this' message to the markets. Failing to act swiftly enough after having acted so swiftly in response to the pandemic could lead to future claims that Mr Powell has overseen the greatest policy mistake of modern times. Risk markets would not be sympathetic to such a view.

In broader terms though, as we move further away from the nadir of the economic downturn in Q2 2020 and the low point in terms of price compression, we also expect headline year-on-year inflation rates to recede. Admittedly, the terminal rate of inflation may remain structurally higher than it was pre-pandemic, but we anticipate a gradually less hawkish rhetoric to prevail over the coming quarters nonetheless.

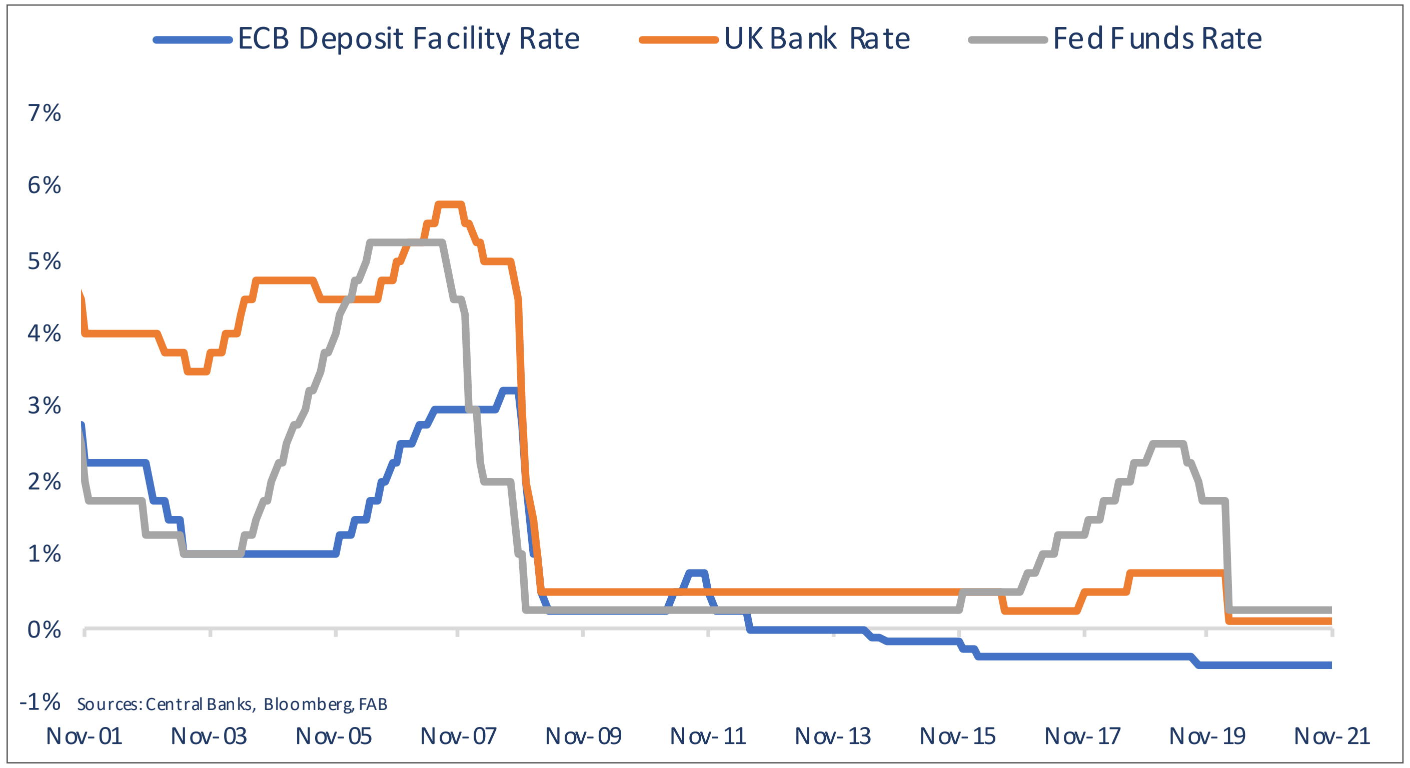
As generic economic conditions make tentative gains the underlying yield curve should edge higher/steeper during the course of 2022 such that the yield on the 10-year Treasury may only just break above the 2% level by the end of the year.

In this context, UAE and broader GCC interest rates also seem set to remain steady during 2022. Expect rates and yields across the region to largely continue tracking their US counterparts, albeit with some modest variation to be expected over time due to oil price fluctuations and regional geopolitics.

In the Euro area, we expect the overarching tone of monetary conditions to remain far more dovish. The ECB has stated quite categorically that it does not expect macro conditions to be strong enough to support tighter monetary policy any time before 2023. We agree and do not expect the ECB to be in a position to pull the rate tightening trigger until Q4 2023 at the earliest. But this dovish spin is not reflected in market pricing, which we feel has recently overshot with expectations of a more hawkish bias from the ECB. Markets should correct over the coming months to withdraw such hawkish assumptions.

Meanwhile, the lack of a coherent communications policy at the Bank of England put investors on alert for a UK rate hike at the November 4th, 2021 meeting, only for the Bank's MPC Committee to vote with a solid 7-2 majority to leave its benchmark bank rate unchanged at 0.1% . UK interest rates will rise in time and government bond yields will react accordingly but, we believe, not as quickly or as hawkishly as many currently anticipate.

Fed funds, ECB refi, BoE Bank Rate
'Anchored well into, if not through, 2022'



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G3 FX OUTLOOK: INTEREST RATE DIFFERENTIALS RETURN TO THE FORE

By Alison Higgins, Managing Director, Head of FX Trading, FAB Global Markets

Risks for 2022 were clearly highlighted around year-end 2021, as inflation expectations and monetary policy tightening cycles were almost eclipsed by the emergence of the Omicron variant and the subsequent implementation of some movement restrictions in parts of Europe. Until there is a global approach to managing the virus, vaccine distribution improves, or the virulence of the pandemic subsides, there is likely to be a shadow lurking over the global recovery, and risk-asset markets could be susceptible to sharp repricing.

However, from a baseline perspective, with the Federal Reserve increasingly convinced of the threat of more enduring inflation and continuing supply-side issues, government bond curves have priced hike expectations, helping the dollar build some momentum into year end. There is still room for a steeper front end for US dollar assets, while other developed markets have potentially overshot in terms of pricing rate hikes. The developed economies of the G7 are also eclipsed by the aggressive steps already being taken by some emerging markets.

For the British pound (GBP) in particular, the aggressive nature of rate hikes priced into the front-end contrasts starkly with the more conservative dollar curve; gilt futures were recently pricing in 3.5 hikes this year, compared to fewer than three for dollar bonds. With multiple FOMC members embracing a faster end to tapering and a cautiously hawkish approach to monetary policy the dollar curve looks mispriced, and any adjustment higher would give further support to the US dollar on its index.

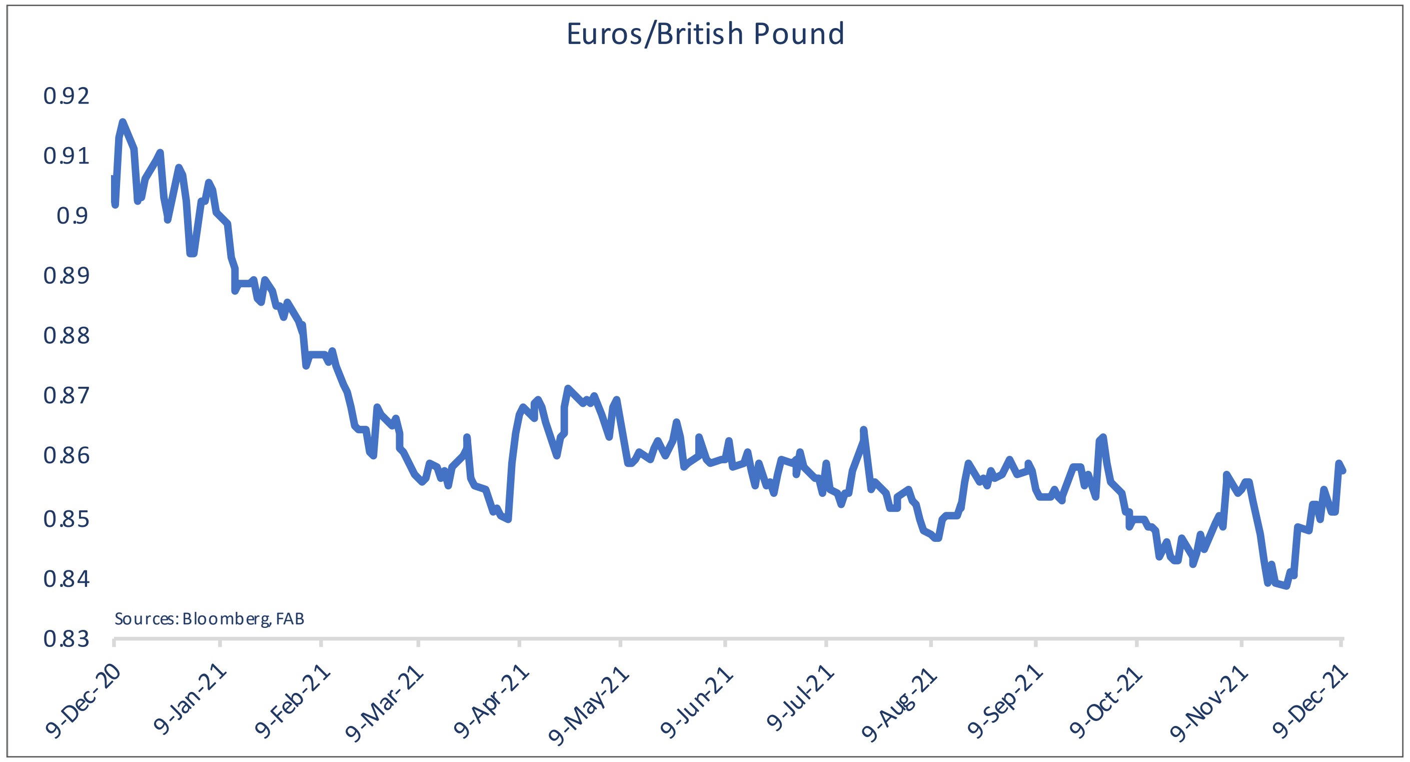
Conversely, the UK rate path has little room for upside from here, and it faces several pressures that could eclipse the economic recovery in the first half of the year. The Brexit fallout continues to rumble on with the Northern Irish border a very sensitive issue, and Northern Ireland Assembly elections in May could cause some further angst and volatility in markets already susceptible to this topic. The increasing pressure to resign on Boris Johnson is unlikely to yield such a result, but the barrage of headlines attacking the incumbent UK government 'sleaze' have weakened his government's position and are also weighing on the pound.

That said, the fundamentals are solid for the UK economy and, barring further COVID shocks, there could be support for the British pound, but it is difficult to see a push much above US$1.35/GBP in the first half of this year. There is even the possibility of a dip back towards US$1.28/GBP, although those levels may instigate buyers.

European bond futures are still lagging in terms of pricing any central bank hikes and are likely to remain passive for most of this year, despite inflationary pressures. Chairwoman Christine Lagarde has a tough job ahead to keep the ECB's rate-setting committee united around the easy policy that has now been in place for well over a decade.

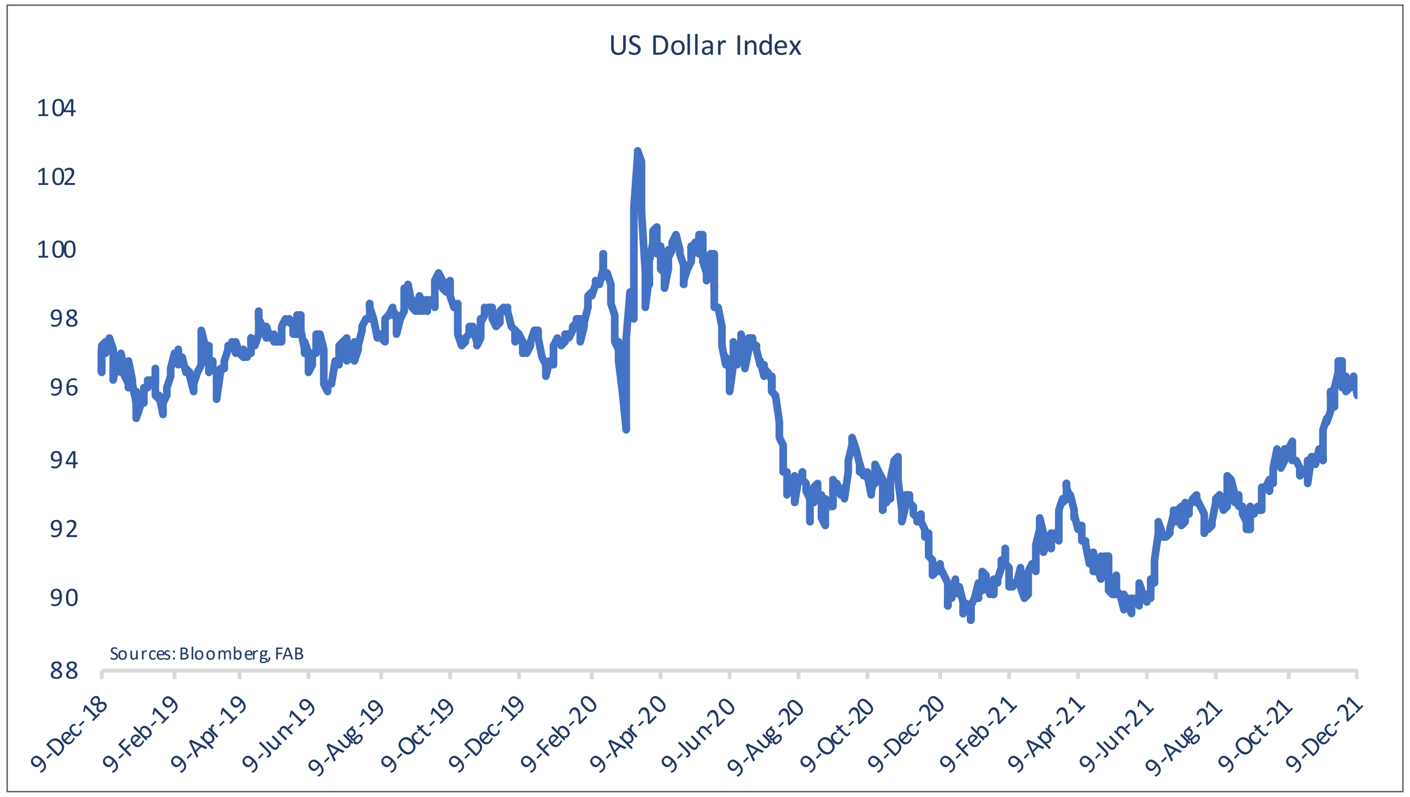
This laissez-faire approach from ECB members is in stark contrast to the rest of the G7 central banks (with the exception of the Bank of Japan), with markets pricing a hike of only 10 basis points in 2022. Negative rates are priced in, even past the four-year forward point. At best, the ECB will end its asset purchase programme in March and the monthly purchases will sit at around EUR 20 billion.

The single currency failed to break the US$1.12/EUR support level on the initial Omicron lockdowns, but since then it has struggled to move away from the US$1.1300-US$1.1350/EUR zone. Potentially continued dollar strength in the first quarter could exert further pressure on the euro, although positive Omicron news would be supportive, in the short-term at least, and a move towards US$1.15/EUR appears possible by March 2022, with an increase in volatility set to stay.



The euro was relatively range-bound in relation to the British pound in the second half of 2021, and is likely to continue in this manner in the first half of this year. The drivers are clear from the perspectives of interest rates and economic growth. Based on historical data, the euro should weaken against the British pound on the advent of any new variant of the virus with good entry levels above EUR 0.86/GBP, and with the possibility to take profits towards EUR 0.845/GBP.

The US Dollar Index has also benefitted from the weaker virus management and aggressive lockdowns seen in Europe with a 2% gain between the start of November and mid-December of 2021, when it was hovering around 96.00. For the first half, there is still potential for upside, although 100.00 would likely be a strong resistance level. However, a gradual move towards these levels during the first quarter is certainly on the cards, given the possibility for an increased pace of hikes from the Fed to rebalance across the basket of currencies that form the US Dollar Index.



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GLOBAL EQUITIES OUTLOOK:

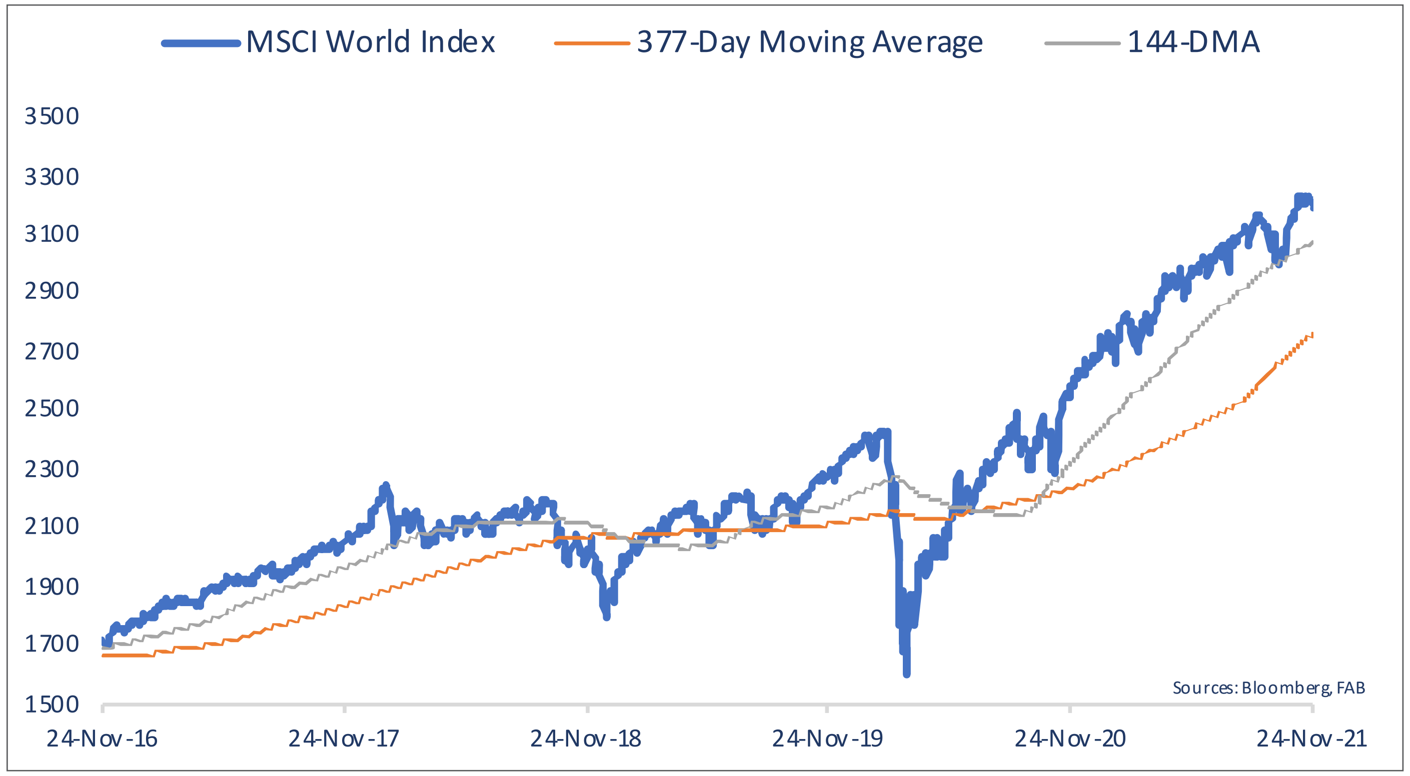
UPSIDE POTENTIAL REMAINS IN 2022 – UP TO A POINT

By Rameshwar Tiwary, Executive Director, Portfolio Manager, FAB Investment Management and
Clint Dove, Director, Investment Research, FAB Investment Management

Last year's FAB Global Investment Outlook stated that "the stars are aligned for good gains in developed world equities in 2021, with potential appreciation of up to 20% from current levels". At the end of November, the MSCI World Index, which excludes emerging markets, was ahead by 20.14% for the year.

The FAB Global Investment Outlook for 2021 also indicated the S&P 500 could go to about 4,400 for a return of 18%, compared to the 'safe' Wall Street consensus of 9% at the time. By November 25th, the S&P 500 was still above 4,500 for a year-to-date return of more than 25%. It had climbed a proverbial 'wall of worry', facilitated by accommodative global monetary conditions. The massive tide of quantitative easing plus the quicker-than-expected progress on the vaccine front ensured that the 'flash' recession of 2020/21 was just that, and that it did not become a depression.

Many of the drivers of last year may be different this year. Global economic growth is decelerating, and the IMF is likely to revise its forecast GDP growth of 4.5% for advanced economies in 2022 (compared to 5.2% in 2021) and 5.1% in developing economies after expansion of 6.4% last year. However, the JP Morgan Global Composite Purchasing Managers Index stood at 54.5 in November after a low of 52.5 in August, so although global growth has slowed, the global economy is nonetheless expanding and reasonably healthy.



At the beginning of 2021, equity analysts were far too cautious in their forecasts, and the reversal of that position provided confidence and enabled investors to justify paying higher prices for stocks. However, the earnings 'beats' are now becoming far less numerous and it looks as though analysts have largely caught up. Major upside potential in earnings has fallen, although this is to be expected after an operationally-geared earnings recovery of such magnitude and as equity markets head into more normal times.

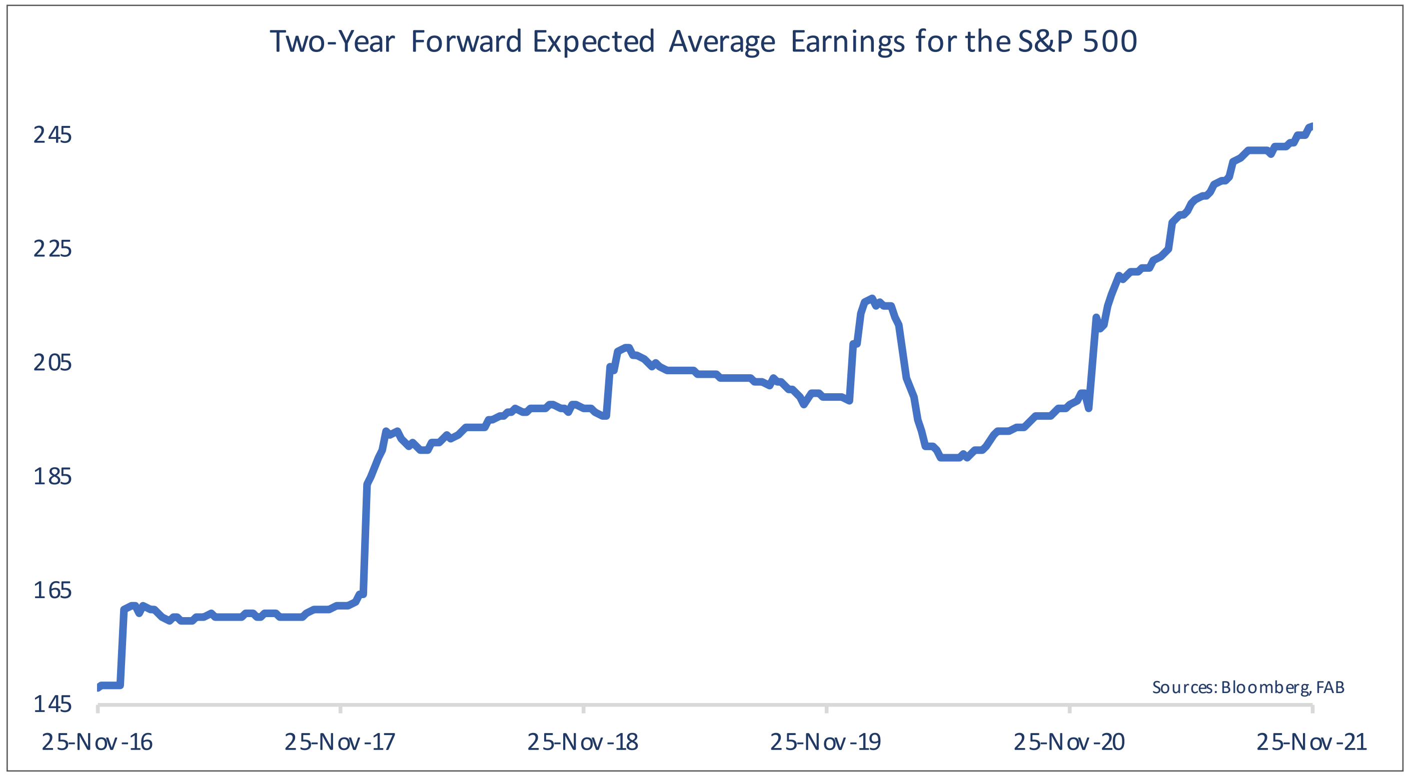
There are also the 'known' risks, which include recurrent COVID mutations, Taiwan, and the difficulties of understanding 'Common Prosperity' in China among others. On the face of it though, much is going right for global equity investors. US listed companies have taken inflation above 6% in their stride, essentially because their pricing power was much greater than expected. Meanwhile, supply chain disruptions are ebbing, and the next cyclical recession is probably more than a few years away.

Last year, the MSCI World Index was led by Energy (up 44.6% for the year to late November), Financials (31.6%), and Information Technology (27.8%), with Staples (9.4%) and Utilities (4.0%) as the laggards. Small-Cap Value outperformed (24.12%), and Mid-Cap Growth lagged (16.43%), although not by much, with major indices showing increasing breadth in their advances.

And, after a period early last year when value was leading, growth recovered to be slightly ahead of value (with gains for the year of 22.85% compared to 20.11%) at the end of November. This year, quality financials, healthcare, and selected technology names could outperform while consumer staples and utilities seem poised to continue to underperform.

Bull markets rarely end quietly, and usually go higher than expected. Despite last year's gains, a 'melt-up' is still possible as 'fear of missing out' takes hold. This, however, could die of exhaustion if the Fed's punch bowl is really removed, even if that of the ECB and BoJ are not. Extreme negative real rates have been a major bonus for equities and should moderate in 2022.

In mid-November, the S&P 500 Index was just above 4,700, trading on a consensus prospective P/E ratio of 20.97x for 2022 and 19.16x for 2023 based on earnings growth estimates of 7.45% and 9.44% respectively. The Bloomberg consensus is for average earnings of US$224.18 on the S&P 500 for 2022 and US$245.30 in 2023. Analysts have been revising earnings upwards although normalisation is likely to become apparent this year.



Going into the second half of 2022, investors will increasingly be using prospective 2023 earnings for their P/E calculations, the estimate for which could edge ahead (to perhaps US$250 for growth of about 11.5%) for a 2023 P/E of 18.8x, equivalent to an earnings yield of 5.32%.

Using FAB's Chief Economist Simon Ballard's forecast of a US 10-year Treasury yield of 2% or less for most of this year, and comparing that to the assumed earnings yield of 5.32%, the basic equity risk premium should be close to 3.32%. In recent years, equities have usually looked cheap versus Treasuries when their risk premium approaches 4.5% and expensive when it falls towards 2.5%.

Conclusions

- During the next 12 months, US corporate earnings are unlikely to do significantly better than what might have been expected in a 'normal' year, although that could now mean earnings growth of 10%-11% rather than the historical 9% annualised rate after the house-cleaning and extra technological innovation that resulted from the pandemic.
- US consumers are coping with the pricing power being exerted by many listed companies and they want to spend, although such abandon cannot continue indefinitely.
- If the likelihood of 'technologically-enhanced' earnings growth (i.e. 10%-11% vs. circa 9% compound historically) proves right, a 2023 P/E of about 21x can be justified, or slightly higher than the forward average.
- The above would equate to about 5,250 on the S&P 500 by the year's end, or 11%-12% above late November levels – potentially via a 'melt-up' sometime in 2022.
- The final third or so of most bull markets do end in this way, clearly without the next cyclical recession ever being in sight, because trees do not grow to the sky.

- A 'greed-induced' run to 5,250 on the S&P could weather a rise in the 10-year Treasury yield to 2%, but probably not much more. In reality, equity valuations would probably be hurt by a rise above 2.5% in the 10-year Treasury yield.
- Globally, investors should emphasise careful stock selection focused on quality. Europe and Japan have some excellent quoted companies, but the return on equity for the STOXX Europe 600 Index tends to be only about half that of the US S&P 500 (and similarly for Japan, which probably continues to be a long-term 'value-trap').
- There are usually good reasons for individual stocks or markets appearing cheap. For instance, UK equities as a class may look tempting, but the country is suffering from Brexit-related disruptions while the Labour Party is now beating Boris Johnson's Conservatives in recent polls, adding to the political uncertainty surrounding this market.

REAL ESTATE OUTLOOK

GLOBAL COMMERCIAL
REAL ESTATE OUTLOOK 2022

By Neal Lindsay, Managing Director, Head of Real Estate Finance, and
Andreas Costa, Executive Director, Global Corporate Finance

Introduction and Reflection

At the time of writing this brief in 2020, many commentators felt that the real estate industry would experience a seismic shift in underlying fundamentals as long-term socioeconomic implications reshaped the way companies and individuals consume, create value and interact. We also commented that, perhaps paradoxically, the UAE would be neatly placed to be a prime beneficiary as the dust settled.

A year later, the economic outlook is better than could reasonably have been hoped for in 2020. This is particularly evident in our domestic market as the exemplary handling of the pandemic has led to a, thus far, pronounced recovery.

Faced with a devastating crisis of uncertain dimensions, global economies sustained epic losses of output and jobs as countries promptly shut down. Confounding, however, expectations of a protracted recession and long recovery gestation, economies have begun to bounce back. In many major economies, economic output is already above pre-COVID levels and employment is projected to recover by early 2022.

It would be an overstatement, of course, to suggest that property markets pivoted without faltering. While positive sentiment is returning, this disguises some genuine and fundamental shifts. Despite overall resilience, some sectors and markets have experienced existential changes, leaving many assets obsolete and needing to be repurposed.

The sector trends that were already evident will continue to play out in 2022. Global industrial investment volumes continue to trade well above their pre-pandemic level, driven by strong investor demand for the sector and rises across most industrial markets since 2020. Conversely, office volumes are 40%-50% below their pre-pandemic level, pushed down by both weak investor sentiment and widespread price falls in the sectors.

Retail, in particular, must embrace fundamental sectoral changes. While convenience stores and destination centres continue to attract investors, the rise of e-commerce has taken a firm grip on consumer spending habits, leading to significant widening of yields for the high street and shopping malls.

Generally, the current yield on real estate remains at historically elevated levels compared to the risk-free rate. When the expected declines in rents and values across most regions start to slow, commentators anticipate the relatively elevated yield from real estate to become highly sought after if rates continue to remain 'lower for longer'.

The Rise of ESG

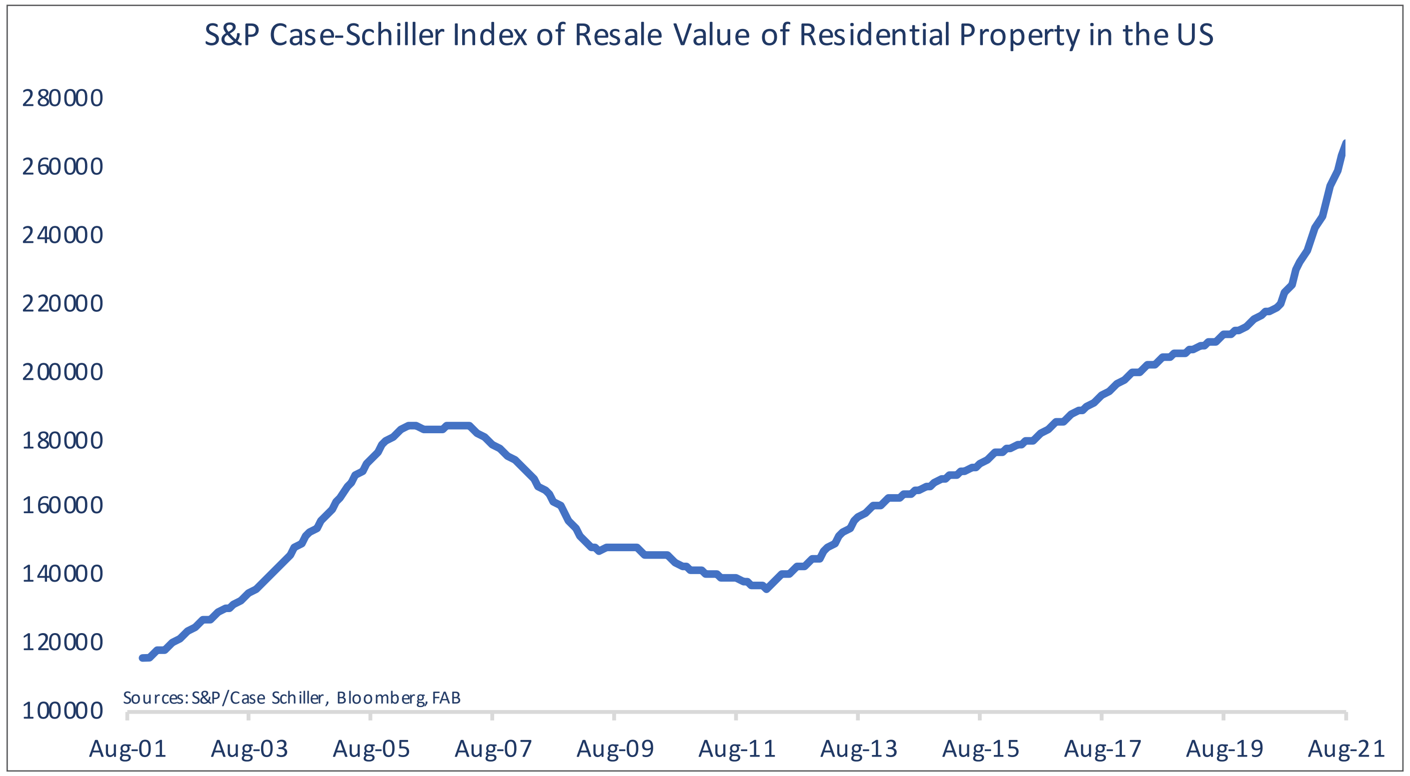
Environmental, Social and Corporate Governance (ESG) has become a defining trend across the sector and will undoubtedly remain a key theme into 2022 and beyond, particularly in the office sector.

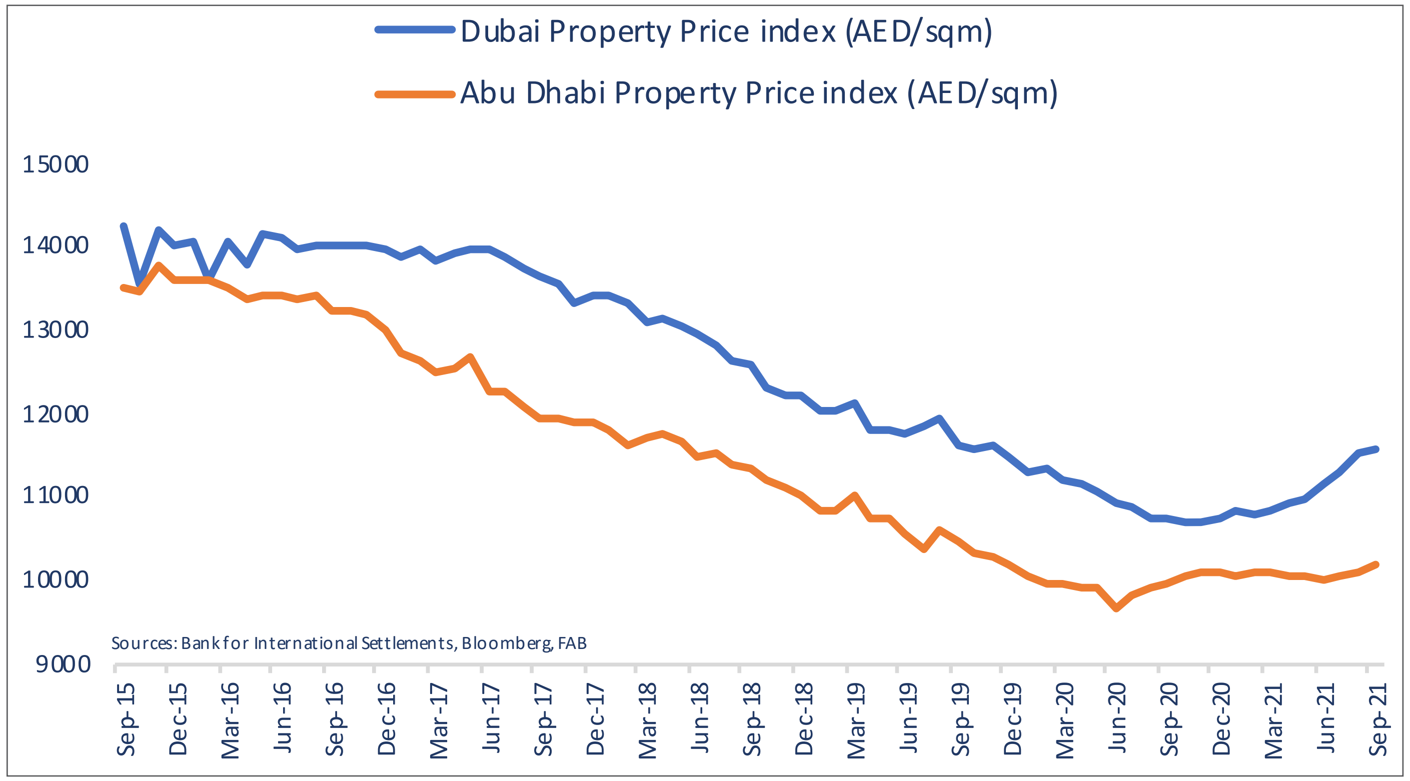
'Climate Risk and Real Estate: Emerging Practices for Market Assessment', a report published by risk consultancy Milliman last year, posed the simple question "How are leading investors factoring market-level climate risk into decision-making?" The answer was overwhelming; in lots of ways, as escalating problems force investors to pay attention. According to PwC, over 80% of respondents consider ESG elements when making operational or investment decisions.

An interesting observation is the rental gap emerging between green buildings and their older, less environmentally friendly counterparts. ESG-sensitive corporate tenants are prepared to pay a premium for buildings that satisfy stakeholders' and employees' requirements and embrace the rapid drive towards ESG compliance.

UAE

Returning to our prediction of 12 months ago, we believe the UAE, and Dubai in particular, is well placed to meet the challenges ahead. Leading economists forecast a very different world over the next two decades. Trends indicate that the centre of economic influence is shifting and the densely populated nations of Asia will likely account for the majority of global activity. In such a scenario, the UAE would be perfectly placed as a geographical bridge.





The Urban 2040 Plan, recent amendments to property and visa laws and, most critically, the composition of growth sectors (including manufacturing, services, digital, financial, hospitality, retirement, care, health and education), account for an increasing share of economic activity, and those are areas in which the country is excelling.

The latest Dubai Commercial Property Price Indices, jointly created by JLL and Dubai Land Department (DLD), were launched at the Cityscape Global Summit. According to the report, around 2,845 commercial property transactions worth AED 33.9 billion were recorded by the DLD during the third quarter of 2021. Transaction volumes were up 1% when compared with the preceding quarter and 34% higher year-on-year.

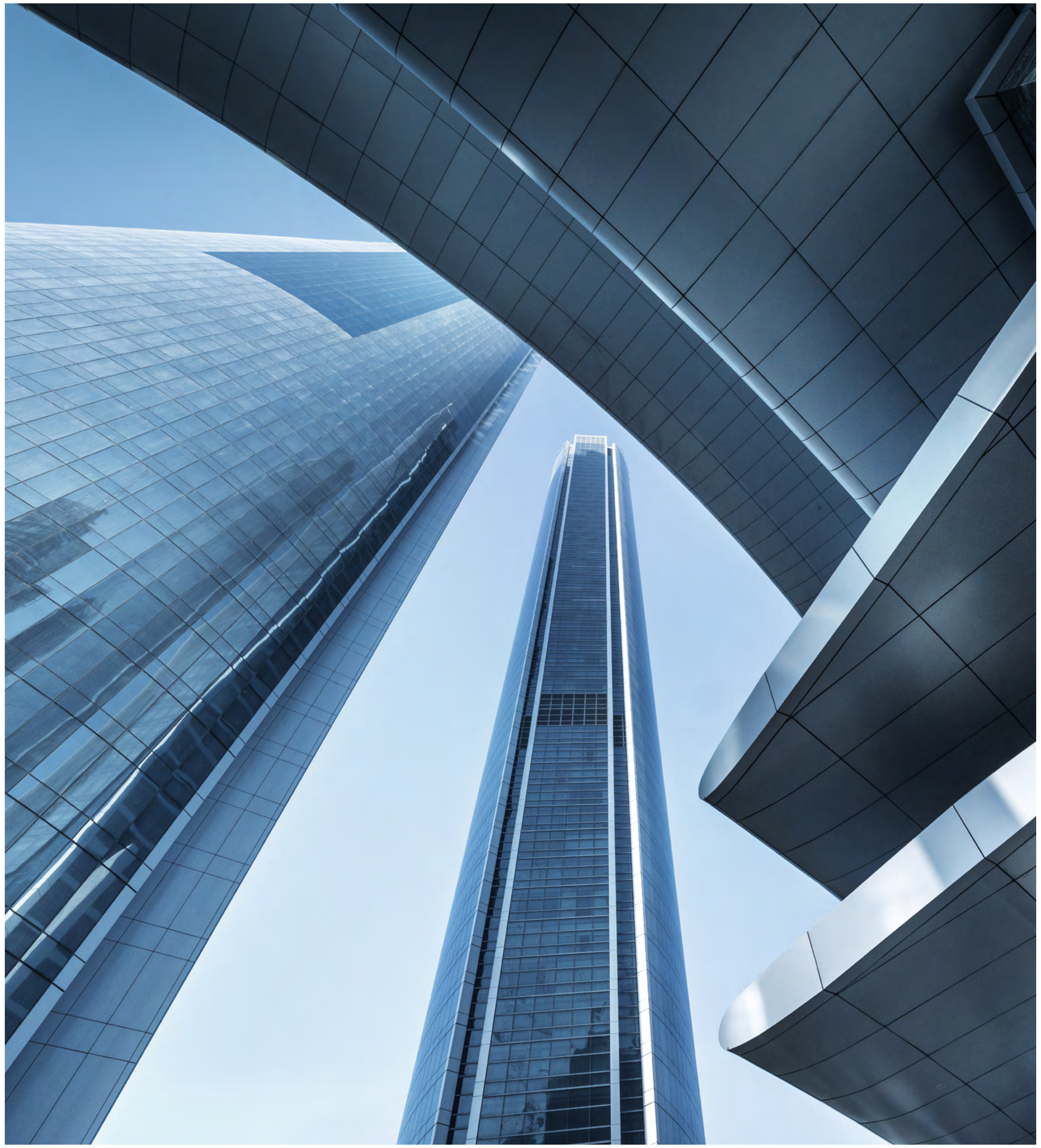
Significant challenges remain, however. The real estate market continues to operate opaquely with limited transactional evidence, rendering market liquidity, investor sentiment and therefore cyclical trend analysis hard to calculate. It is incumbent on all market participants to evolve transactional disciplines so Dubai and Abu Dhabi can truly emerge as leading hubs for global real estate activity. This eventual maturity and transparency is expected to be a key catalyst for inbound global institutional capital.

Conclusion

The months since the pandemic hit presented the real estate sector with a series of unprecedented challenges. Looking forward, the resilience of the economy and of property markets generally have inspired confidence in the industry's collective capacity to adapt to changing market conditions and previously unknown risks.

Progress toward full recovery, however, is likely to remain measured. Current uncertainty is centred on the strength and speed of recovery. Temporarily closed businesses are reopening and seeking employees. However, many businesses are slow to fill open positions – particularly service jobs. Positive news about vaccine distribution, the reopening of schools and continuing fiscal stimulus should continue to support a meaningful rebound in economic growth and a turnaround in aggregate real estate performance, according to PwC.

Investor confidence remains higher in the logistics and multifamily sectors given the persistent, through-cycle tenant demand. Confidence is growing in the leisure and travel sector, supporting optimism for hotels. Commentators anticipate that the pronounced sector divergence will continue for several more quarters. Nevertheless, we anticipate the level of polarisation to be less pronounced going forward as parts of the retail sector improve and industrial price appreciation moderates.



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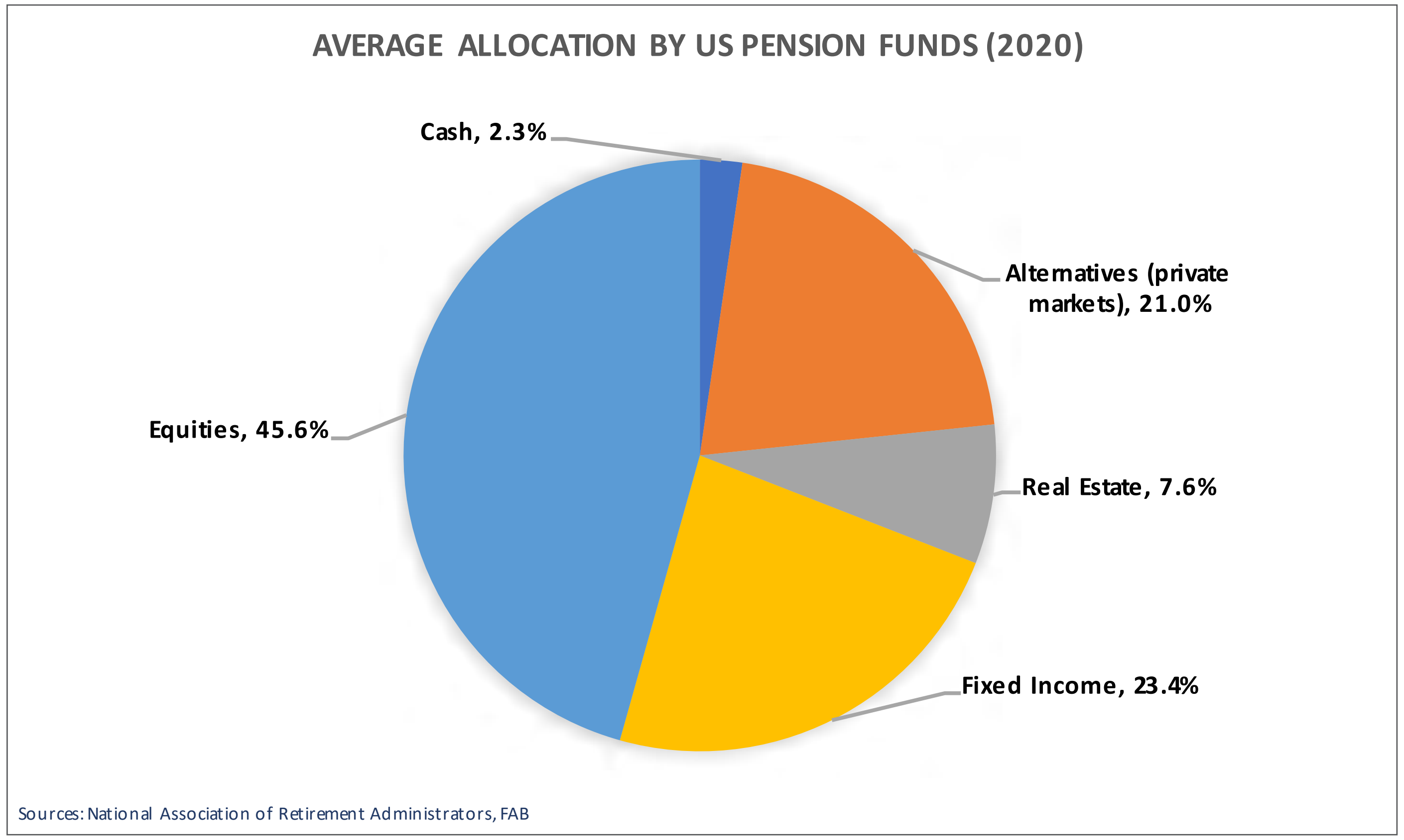
DEVELOPMENTS IN INVESTMENTS

PRIVATE MARKETS – LOW VOLATILITY AND HIGH RETURNS ARE POSSIBLE

By Chris Langner, Director, Acting Head of Investment Strategy

Investors, even those focused on long-term returns, often battle their emotions as they face wild swings in the markets and fear losing hard-earned money. Fear may often get the upper hand, causing investors to lock in losses, while greed can push them into buying assets at high prices. Both result in lower returns over the long run.

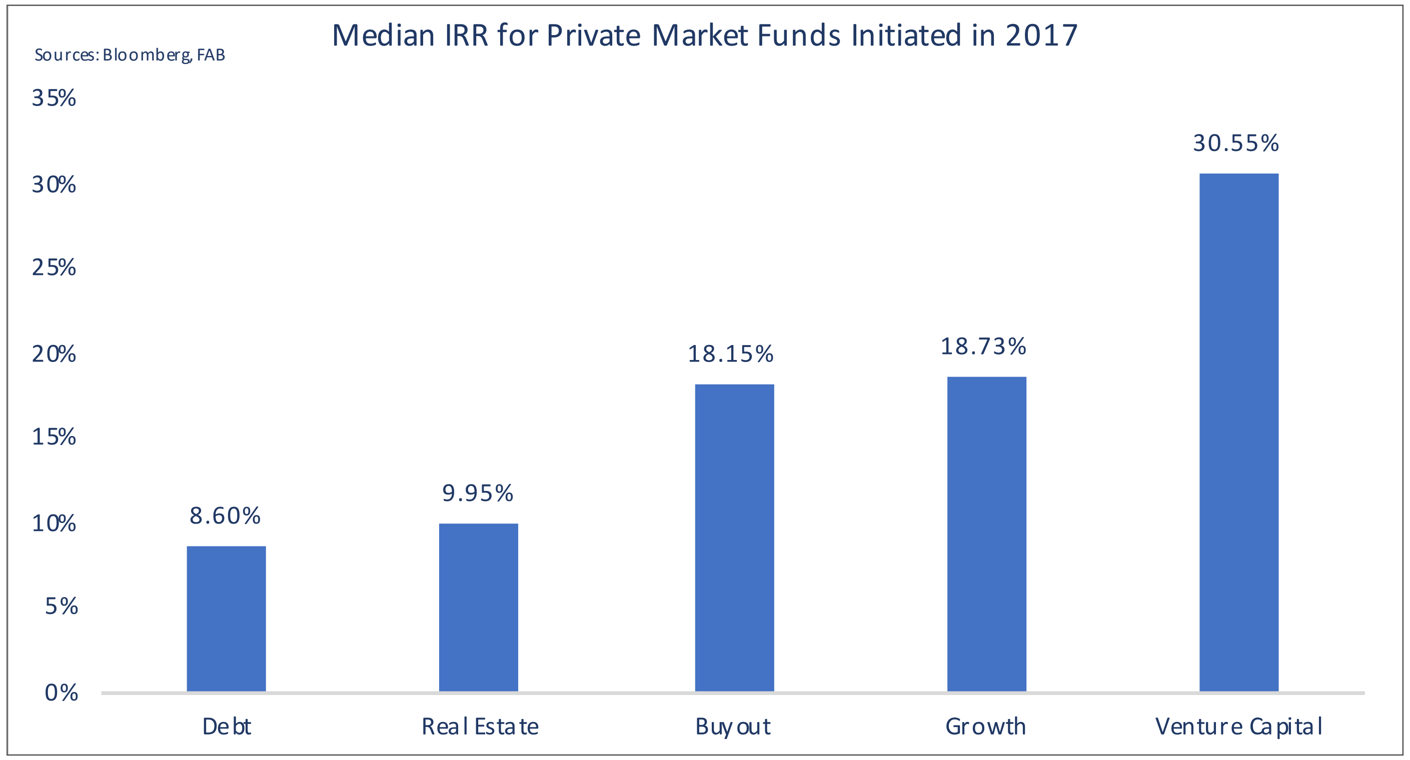
Pension and sovereign wealth funds have known that for decades and have increasingly incorporated private market strategies into their overall asset allocation. In fact, for the first time last year, the average allocation to 'alternatives' (mostly private market funds) exceeded 20% of the reported holdings of US pension funds according to the National Association of State Retirement Administrators (NASRA). This represented a ten-fold increase in the allocation to these strategies from the nearly 2% average NASRA reported in 2001. The rising share of alternatives in the asset allocation strategies of pension funds in the US happened in tandem with a reduction in the expected return of their portfolios to 7.4% from 8% over the same period.



This is not a coincidence. As interest rates were pushed ever lower and the average returns on public market securities fell, pension funds increased their allocations to private market strategies, which can generate equivalent or higher average returns with lower volatility. The median annual return for private equity funds, for instance, was 13.3% between 2007 and September 30th 2020 according to McKinsey & Co., or double the 6.5% average annual compound growth rate of the S&P 500 index over the same period.

The same pattern can be seen across other private market strategies. For instance, private credit funds generally perform better than their fixed income counterparts (in fact, they were up last year when fixed income was generally down). Similarly, direct real estate funds have done better than REITs, while real asset strategies have generally performed better than direct investments in many commodity funds.

The only exception might be selected technology stocks, which have become market darlings in recent years and have powered equity index returns in the US, but even they did not beat their private market counterparts by much. The NASDAQ 100 index had a stellar 228% performance between the end of 2016 and December 1st, 2021, equating to a 34.65% compound annual growth rate compared to a 30.55% average internal rate of return for venture capital funds created in 2017, according to Bloomberg.



The additional gains, however, came with much higher volatility. For instance, in the past two years, the NASDAQ 100 fell by more than 10% three times, and there were three drops of more than 7%. Meanwhile, venture capital firms, for instance, arguably did not face the same ups and downs. Granted, that is partly because the assets they hold are not publicly traded so there is less transparency about returns, but the final outcome is what matters. Investors, however, need to understand these nuances before they venture into the private world. Here are a few key differences to look out for:

Liquidity

Part of the reason that public markets are more volatile is because they are more liquid and operate on the basis of daily price discovery. Investors can buy or sell equities or bonds in a company during the same trading day with settlement taking a few days. Meanwhile, with private market investments, money committed may not be paid back for several years, and investors are likely to have little visibility apart from quarterly (or sometimes even annual) reports they receive from the fund management firm about how cash has been deployed.

There can be at least some liquidity, though. An investor may be able to sell the participation in a fund in the secondary market, but any sale could be at a loss, depending on the stage of the investment deployment and the time to expected redemption.

Availability of cash

The normal investment horizon for private equity programmes tends to be around seven or eight years. That is usually when investors can expect to get their money back, although there may be some payback towards the fourth or fifth year depending on a variety of factors. Private credit funds could be a bit faster as loans made start to earn interest and be repaid, while venture capital can take longer as the underlying businesses funded arrive at possible 'exit' points (for the manager) via IPOs, LBOs or strategic sales.

This is why private market managers talk about internal rates of return instead of yields or straight returns. Funds calculate how much they are going to return to investors based on the cash flows, but these do not happen in a straight line like a bond or involve regular dividends like with a stock. Depending on the strategy, investors may commit the cash and wait several years before they get paid and then suddenly receive a big lump sum.

Different Strategies

Private funds usually try to exploit inefficiencies in funding markets or in company management. Private credit funds might offer loans to companies that are having trouble getting them from banks or bond markets. Buyout funds may take over companies that have steady cashflows but that have not managed to extract maximum value. Venture capital firms seed many start-ups, hoping that a few of them will do fantastically well and make up for the majority that fail.

Investors need to understand these aspects before entering various strategies to avoid getting worried without reason. For instance, a venture capital firm might have seeded several failed companies in its portfolio, but that does not mean it will be unable to return investors' capital plus gains.

Here is a simple guide to some of the most popular strategies:

Buyout

This usually involves acquiring mature companies that have steady cashflow, and using leverage and cash management strategies to improve the equity value of the company. Often private equity firms that focus on buyouts will have identified future strategic buyers or an opportunity to resell the company they acquired in the capital markets after they have improved its cash-generating capability.

Venture Capital

This focuses on companies that are in early stages of growth. Such firms are often focused on technology, given that this is the sector that has seen the highest growth over the past two decades. However, venture capital firms may find opportunities in other areas that do not involve technology, but which should benefit from areas of high growth such as, for instance, a new trend. This was recently the case with firms that invested in companies that offered plant-based alternatives to meat.

Most venture capital firms seek to make several investments in areas they believe will see strong growth, usually in companies that have already received a couple of rounds of financing and have therefore started to mature. Many of the investments will fail, but it only takes one good investment in a vintage to work out and make the entire investment worth it, given the multiples that can be generated.

Credit

Private credit is a broad name for many sub-asset classes, including distressed debt and mezzanine financing. Many private credit firms specialise in offering loans to private equity firms, but some will seek medium-sized companies or those that are going through a tough period and may have difficulties accessing bank credit.

One of the advantages for investors is that these firms usually offer very senior lending, meaning they are at the top of the capital structure in case the borrower ends up in bankruptcy. The result is that even when there are defaults in a portfolio, private credit firms are usually able to recover a significant part of what they lent by taking over assets pledged against the loans.

This strategy also tends to pay investors back faster and to start paying coupons early on. Plus, loans offered by private credit firms are usually based on floating rates, so they are mostly immune to changes in benchmark interest rates.

Real Assets

Again, this category has several sub-classes, including real estate, infrastructure, art, and commodities. As the name suggests, this strategy focuses on tangible assets and trying to acquire them at a discount.

Conclusions

There are many other strategies and subcategories in the private markets space. One thing is common to all though: they target high returns, which are likely to have low correlations to public markets and which therefore deserve a place in most portfolios. And, as global pension funds are increasingly realising, they should probably become an even larger part of the long-term assets that they manage.

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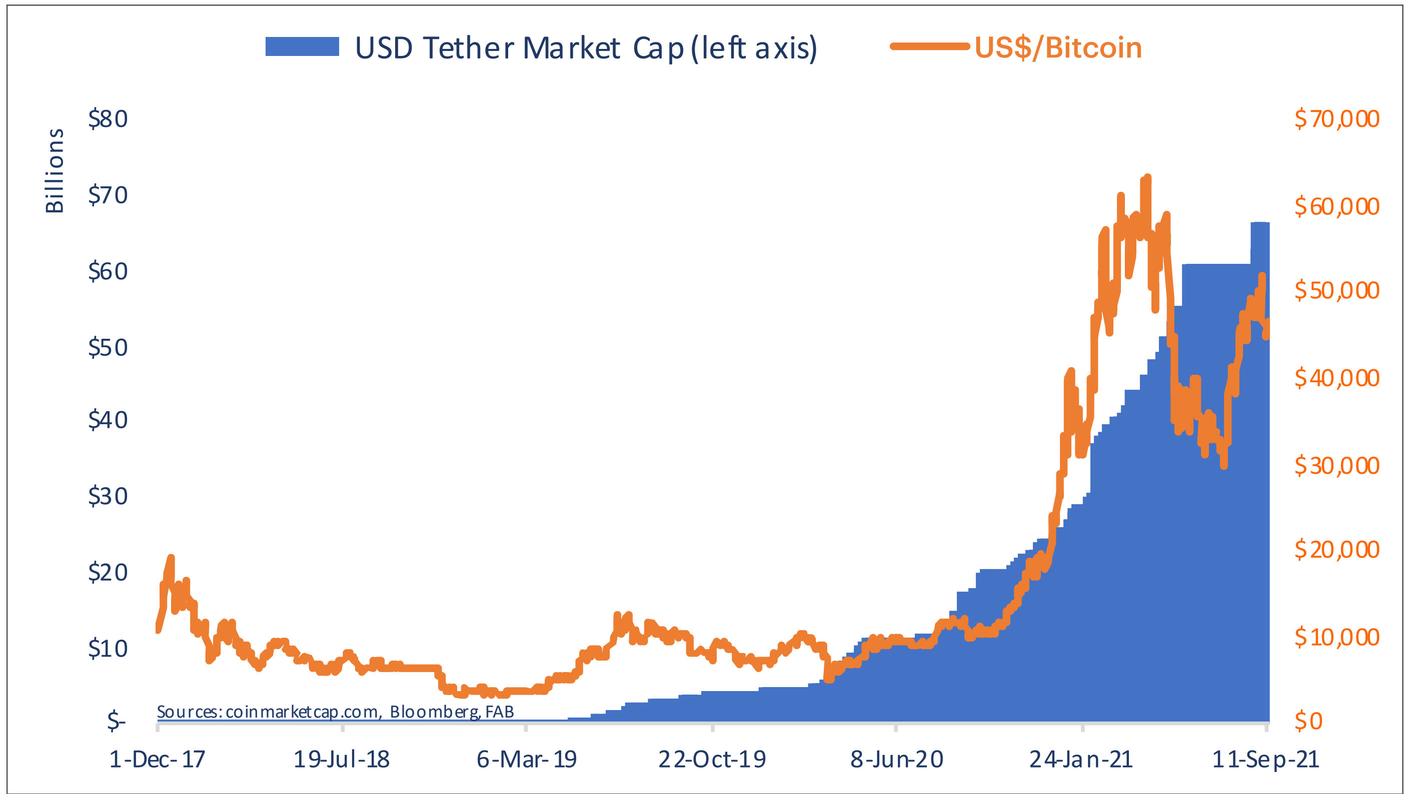
CRYPTOCURRENCIES, WHAT YOU NEED TO KNOW

By Chris Langner, Director, Acting Head of Investment Strategy, and Anisha Makani, Director, Investment Solutions, FAB Private Banking

Cryptocurrencies have attracted a lot of attention lately. That is partly because the price of bitcoin, the grandmother of them all, increased more than seven-fold or 612%, to US$65,868 from US$9,239 in the 18 months leading up to November 15th, 2021.

The move has seen several large corporations and even a nation embrace it (El Salvador made it legal tender in early September, 2021). This sort of movement has created a lot of hype around cryptocurrencies. Though the news flow has increased, very few people understand what cryptocurrencies are.



What is it?

A cryptocurrency is a piece of code, an entry in a distributed ledger. A couple of things make it unique: the entry happens through a cryptographic operation and it cannot be changed.

A look at the history of commercial cryptography may offer a better way to understand a cryptocurrency. Modern commercial cryptography, the kind still used in computers to protect everything from messages to servers and systems, was initially born from the efforts of two American scholars, Diffie Whitefield and Martin Hellman. In the 1970s, they created mathematical ways to ensure a message between two points could only be read by the sender and the receiver.

In the 1980s, such techniques started to be used to validate tolls in automated toll road charging machines in Europe, perhaps the first form of digital

money. In 2008, a paper written by a person using the pseudonym Satoshi Nakamoto established a mathematical way to generate transaction entries, validated in a decentralised manner.

Whitefield, Hellman and Hal Finney (who was one of the early promoters of bitcoin and who, some have suggested, may have been the real Satoshi Nakamoto), have been called 'cyber anarchists' given their work to avoid government intervention in messaging and financial transactions. As for Satoshi Nakamoto, no one knows who he really was.

The decentralised, encrypted ledger system that Nakamoto created became known as blockchain and originated Bitcoin, the first cryptocurrency. It is called blockchain because each transaction is part of a block, and each block has references to the previous block so that all the transactions can be traced to their origin.

In fact, this is one of the great misunderstandings about most cryptocurrencies, with very few exceptions. While the ledger entries are all pseudonymous (they do not include the personal information of the person who made them), they are all public. Anyone can trace a bitcoin back to the first transaction in the chain, and if anyone had the information related to the 'wallets' involved in the transaction, they would be able to establish who received or sent that bitcoin.

Because of this, many countries have established special taskforces that specialise in tracing illegal money that is transferred or transported using cryptocurrencies. Police in countries such as Denmark, Germany or the US can prosecute cryptocurrency exchanges to force them to provide information about wallets used in suspicious transactions.

How much is a cryptocurrency worth?

Only as much as the next person is willing to pay. While bitcoin transacted for US$65,868 in mid-November, 2021, this value was established by transactions in the open market over large cryptocurrency exchanges such as Gemini, Binance and Coinbase. The only reason it has this value is because users of these exchanges are willing to pay this amount in either cash or another cryptocurrency. Unlike a stock, which has future dividends, or a bond, which carries a promise to pay interest or principal, cryptocurrencies usually have no inherent value.

There are now thousands of cryptocurrencies and anyone can create a new one in minutes for a few dollars. If it will have value or not will depend on whether a large exchange lists and trades it and how much visibility it attracts.

Bitcoin and Ethereum have become widely accepted, and hundreds of exchanges across the world have pools of cash that trade in them, making the two an easy way to move money across borders. While regulators once paid little attention to such movements, they often monitor them nowadays.

Another cryptocurrency that has been widely used is USD Tether and its stablecoin peers. This one, however, has become the subject of a lot of controversy lately.

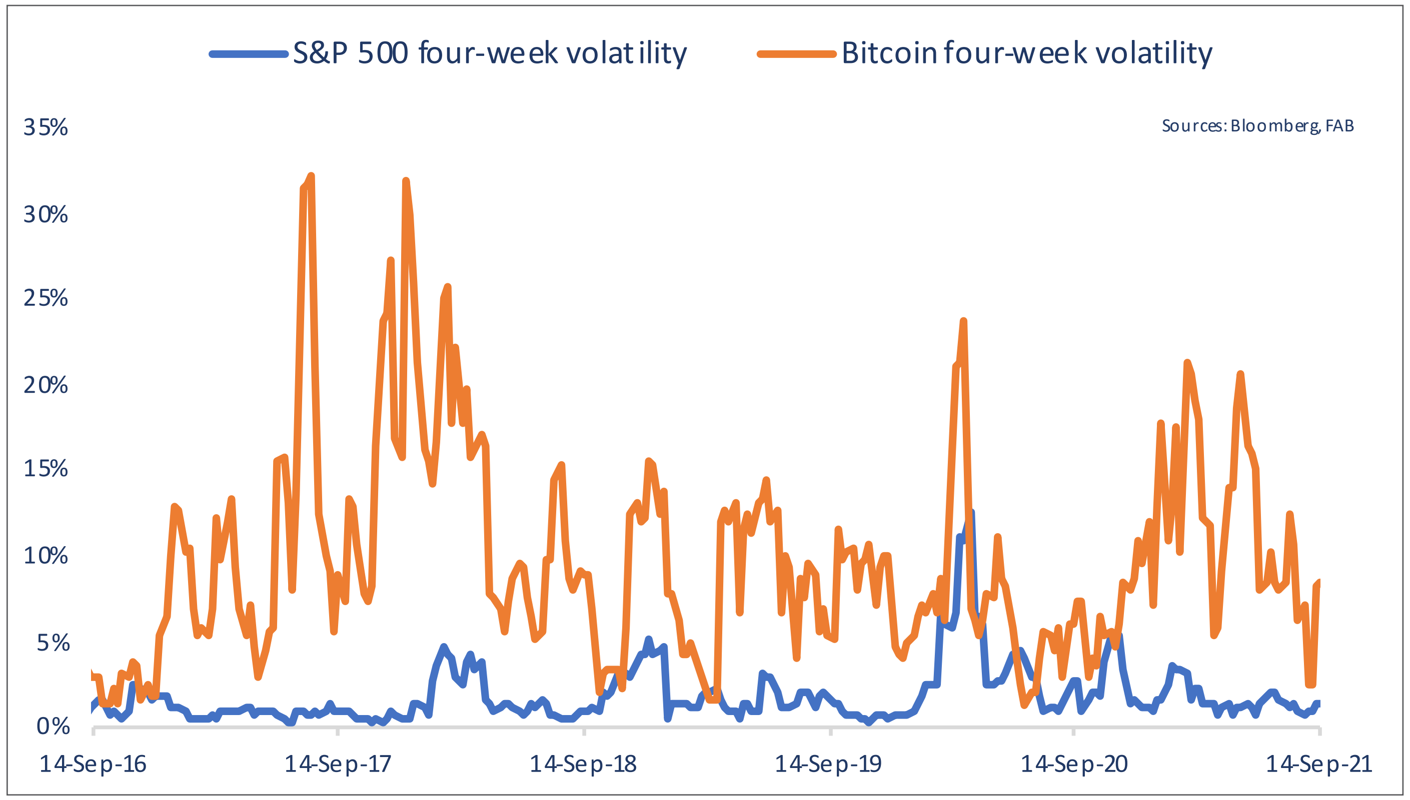
The stablecoin with the largest market cap and trading depth, USD Tether was created by the founders of exchange Bitfinex in 2014, but it really took off after the exchange had trouble honouring some withdrawal requests.

Between May, and December 17th of 2017, bitcoin prices rose to US$19,045 from US$1,439 at the same time as the market cap (the amount of coins circulating) of USD Tether increased to US$1.13 billion from US$55 million. Its market cap was at US$73.89 billion in mid-November. USD Tether is now one of the top three most traded cryptocurrencies, and it is widely used to buy bitcoin and ethereum on exchanges.

According to USD Tether's white paper, every dollar of market capitalisation of USD Tether was meant to be backed by a dollar in a bank. However, following a suit from the New York Attorney General's Office, the company that manages the cryptocurrency admitted that it may not have exactly a dollar for every USD Tether outstanding. This is key, because the company that issues the USD Tether can 'print' as many as it wants. Some researchers have suggested it could, in theory, print USD Tethers that do not have dollars to back them and use these to pump the value of other cryptocurrencies.

In any case, stablecoins have become such a big part of the market that the US Treasury and other US regulators are now debating what risks they pose, and regulation that would allow only licenced financial institutions to issue such cryptocurrency.

One of the problems with cryptocurrencies is that there is hardly any regulation related to them, which means that if something goes wrong, there is no one to whom people can complain. Short of cases of outright fraud, law enforcers have little jurisdiction over cryptocurrencies. While that is exactly what the anarchists who created it wanted, it also poses a conundrum for the common investor. If an investor is unlucky to end up buying a fraudulent cryptocurrency or losing money on a traditional cryptocurrency, it is hard to determine to whom they can even complain.



And though famous investors such as Ray Dalio have said recently that they hold some cryptocurrency, the truth is that Bitcoin, for one, is extremely volatile. Based on its history over the past five years, there is a 95% chance that it will move 23% up or down in any given week. That means that if someone invests US$100 today, there is a good chance that next week the person will have only US$77 – or US$123.

Over the past five years, there were seven weeks in which bitcoin fell more than 20%. Its worst week was in March, 2020 when the cryptocurrency dropped 36%. The opposite is also true. Bitcoin has logged fifteen weeks of gains of more than 20% in the past five years too, with its best one in July 2017, when the cryptocurrency rallied 49.3% in five days.

Finally, even if an investor is lucky to make a lot of money with cryptocurrencies, withdrawal into the real world carries high fees (up to 5% on some exchanges) and can be troublesome. Banks are often averse to anything that has originated from a cryptocurrency transaction and many will not accept a deposit if the client claims he got the money that way. Even cryptocurrency exchanges constantly change the banks they use as a result of the same aversion. It is not for the faint-hearted.

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ETFs
A BASIC GUIDE

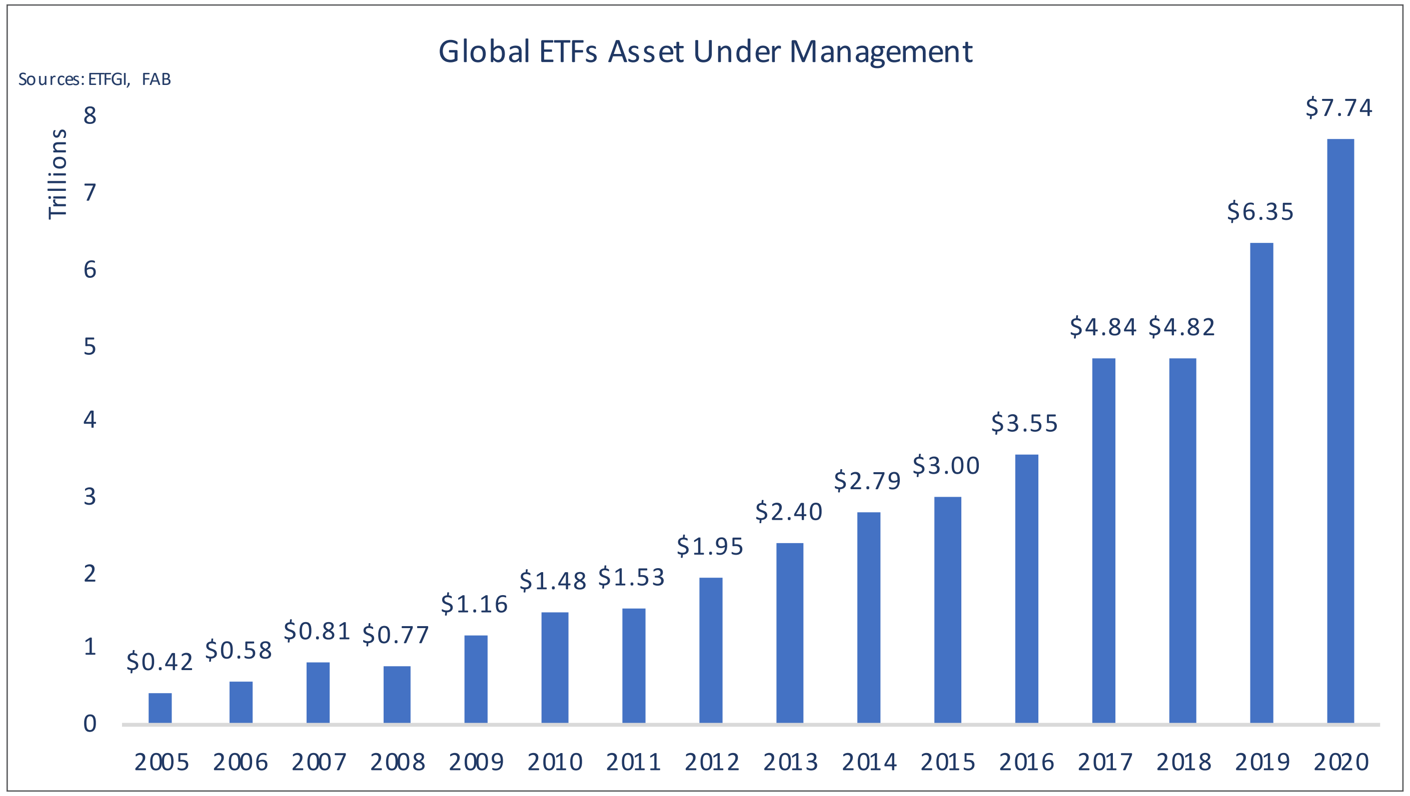
By Chris Langner, Director, Acting Head of Investment Strategy, FAB Private Banking

Exchange-traded funds (ETFs), as the name suggests, are hybrid investment products combining many investment features of mutual funds with the exchange trading associated with common stock. Because they trade on an exchange, ETF prices change throughout the day as and when they are bought and sold, and sometimes their market cap even deviates from the net asset value of their holdings.

The first ETFs were listed in the US in the early 1990s and were mostly focused on tracking stock indices, allowing investors to buy and sell an entire index in a day without spending much. Their existence, and associated options in some markets, also allowed more speculative short-term investments in some markets that were hard or expensive to place before.

Nowadays, however, there are ETFs and exchange-traded products for nearly everything, whether it is taking a leveraged position that the VIX S&P Volatility index will move up or down or even in bitcoin. They are also no longer simply passive vehicles; a growing number of vehicles that are traded have active and specific investment mandates.

This diversification of the nature and mandates of ETFs has helped to boost their participation in the overall market and, according to the Investment Company Institute, in the US alone their assets under management increased US$2.28 trillion in the 12 months leading to October 2021, when total assets of such funds in the country reached a record US$6.96 trillion.



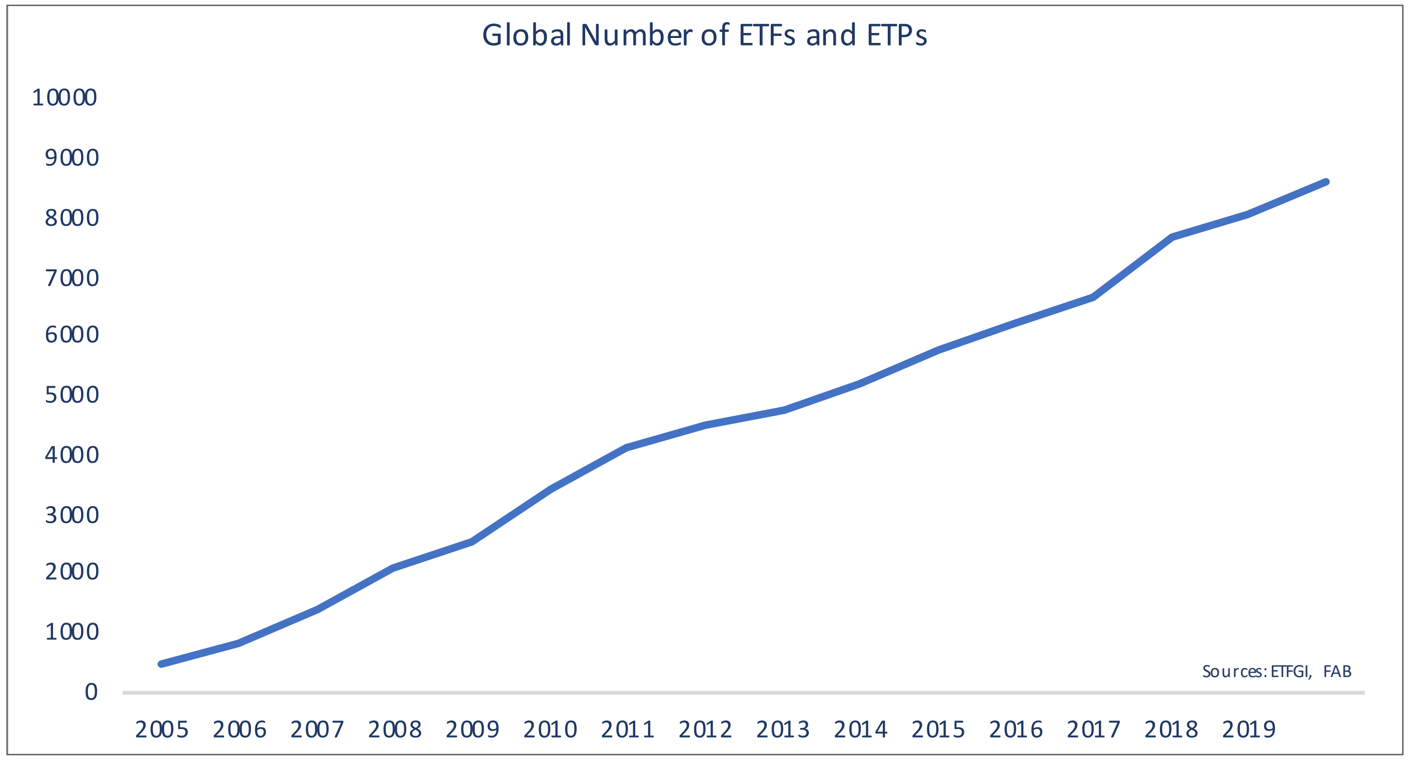
Global ETFs Asset Under Management

There are now nearly 9,000 different products with close to 18,000 listings across the globe, which means the number of ETFs and exchange-traded products has multiplied some 20 times in the past 15 years.

As a result, even investors with small amounts of savings can create almost any kind of diversified portfolio simply using exchange-traded products and funds. They can also do just about anything with an ETF that they can do with a normal stock, from short-selling to selling calls in the markets where options are available.

Nothing comes for free though. When an investor buys an ETF instead of the actual portfolio targeted, there are management costs aside from the normal trading expenses to buy or sell a stock. Plus, the ETF's own expenses will end up being charged to the ultimate investors.

That said, however, ETFs generally have lower management fees than traditional mutual funds in most like-for-like categories, partly because they tend to be able to achieve scale more easily given how simple it is to invest in an ETF.



Global Number of ETFs and ETPs

Some advantages of ETFs

Lower cost: Index-tracking ETFs generally have lower management fees than their non-listed counterparts, although that is not always true. Some ETFs that offer exposure to certain kinds of futures markets, for instance, may have significant management fees and may incur high roll expenses that burden the investors.

Diversification: ETFs have low-cost units that can be bought through a simple brokerage account, allowing investors to create more diversified portfolios without having to commit large sums. There are broad-based ETFs that invest in 5,000 stocks and there are select industry ETFs that invest in 20 stocks, as well as active, thematic, futures-based, single commodity ETFs, and even ETFs of ETFs.

In addition, ETFs can be sold short and, in some cases, have inverse exposure as an investment objective; this feature makes access possible for those seeking to profit from decreases as well as increases in prices of a certain part of the market.

Because of their exchange-traded nature, ETFs offer a level playing field, providing all investors, regardless of the size of their investment holdings or time horizon, with access to a full suite of products across the financial marketplace.

Intraday trading: One of the drawbacks to investing in an open-ended mutual fund is that they are only priced once a day. With an ETF, investors can trade in or out of the fund at various times throughout the trading day.

Transparency: In certain jurisdictions, mutual funds are only required to disclose their holdings on a quarterly basis. Often, investors are left in the dark about what the fund is invested in until the quarterly or annual reports are released. With an ETF, the fund provider is required to post their holdings on their website on a regular basis, and that gives investors almost real-time access to the securities and weightings within the portfolio.

Caveats

While ETFs can be an excellent tool for any portfolio, there are some pitfalls investors need to be aware of.

Underlying liquidity and volatility: Some ETFs are thinly traded and, just like an illiquid stock, they can make it difficult for an investor to close a position. Because they are traded, sometimes ETFs deviate from their net asset value and can trade at a premium or a discount, though in most cases such anomalies are soon corrected by the market.

Some ETFs also invest in securities that are not nearly as liquid as themselves. Some fixed income ETFs, for instance, faced issues during the sell-off in March 2020 as redemptions vastly outpaced their ability to unload their holdings. This has drawn some regulatory scrutiny given the possibility that such ETFs could exacerbate downward movements as they are forced to fire-sell holdings to meet accelerating stock market-led redemptions.

Misunderstandings related to strategy: Some ETFs, which are seen as vehicles to gain exposure to certain commodities or strategies, may hold derivative positions that are expected to emulate the performance of that target investment. This means that the performance will not be exactly the same.

Some oil-based ETFs, for instance, hold futures, and therefore could underperform spot prices because of roll costs and differences in the performance of various derivative contracts. The first "bitcoin ETF" to be approved by the US Securities and Exchange Commission, for instance, does not buy the cryptocurrency; instead, it uses futures contracts traded in Chicago to mirror its performance.

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