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12th June 2026

Investor froth scaled back, but not eliminated

US equity positioning remains stretched despite pullback. Hawkish Fed rate expectations after a solid US jobs report and renewed Middle East clashes have triggered a pullback.

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A hawkish repricing of Fed rate expectations following a solid US payrolls report and renewed Middle East hostilities have acted as catalysts for an equity market pullback. Prefer equal-weighted global equity index in the near-term and diversification in the tech sector across semiconductors, hardware, internet, and software.

Pushing back Fed rate cut expectations to next year, tactically shortening bond duration.

The resumption of Middle East hostilities raises the risk of a prolonged blockade of the Hormuz strait through the peak summer demand season. This would leave oil prices potentially elevated for longer. Meanwhile, the US job market has picked up over the past three months. This evolving backdrop is likely to embolden the hawkish members of the Fed to convince new Fed Chair Warsh to drop references to any rate cuts from its post-meeting statement next week. Expect the Fed to hold rates for the rest of the year before cutting next year as oil price-driven inflation subsides only by the middle of 2027. Bond should be considered with 3 to 5 year maturities.

India's measures to help stabilise currency, revive foreign investments

The Reserve Bank of India's measures signal stability for the Indian rupee after the recent sharp depreciation. Tax exemptions and expanded tenors are likely to boost foreign portfolio debt flows, anchoring long-end government bond demand and steepening the Indian government bond yield curve. Equity inflows are likely to benefit from relaxed overseas Indian investment limits but remain driven by valuations and earnings growth in the near-term. Overall, the measures, by stabilising the currency, are likely to revive foreign investor confidence. Large-cap Indian equities, given their greater margin of safety in terms of earnings and valuations, as well as stronger balance sheets will withstand near-term market volatility.

Opportunity in gold for long-term investors

Gold has broken below its 200-day moving average, a key technical support level that had held since October 2023. Gold is now testing the next major support zone around USD 4,100/oz. While the break weakens near-term momentum, the recent weakness is an opportunity rather than a turning point in the structural case for gold. Central bank buying, which remains intact as seen from China's sustained purchases in recent months. The latest weakness offers long-term investors who have been under-allocated to gold to add exposure, given gold's traditional role as a portfolio diversifier. Gold has also outperformed other major assets during periods of stagflation.

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