Weekly Update

C0 | EXTERNAL PUBLICATION

Another volatile week on equity markets

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All data retrieved from Bloomberg (25/10/2018).

The equity market sell-off reignited on Wednesday. The S&P500 dropped 3.1% while the US tech-heavy Nasdaq index shed 4.4%, its biggest one-day drop since August 2011. Markets then rebounded on Thursday, and at closure on 25 October, the S&P 500 was down 7.5% versus 1 October. European markets were also dragged lower on Wednesday, with the Euro Stoxx now in negative territory year-to-date.

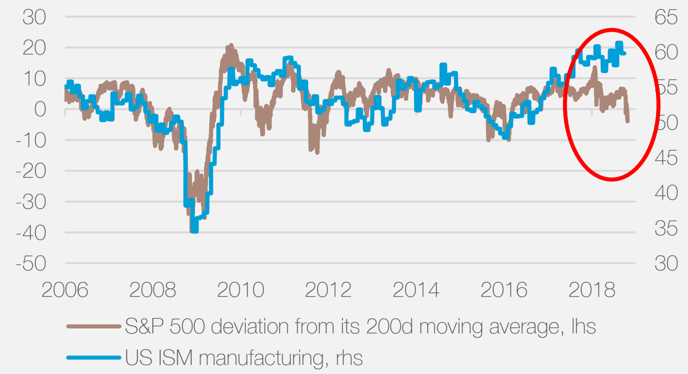
The market correction appears to have been caused by a combination of heightened political uncertainties (US/China, Italy/European Union, and Brexit uncertainties), hawkish US Federal Reserve (reiterated rates hiking), softer growth (notably in China) and mixed third-quarter (Q3) results indicating a possible peak in corporate earnings.

Indeed, we are in the middle of the earnings season in the US, where 46% of all S&P 500 companies have reported Q3 earnings. Initial results point to positive surprises as 83% of the companies have delivered better-than-expected earnings (+6%). Earnings per share (EPS) increased 23% YoY while sales growth printed at 8.8% YoY. So far, all sectors have surprised positively with nine out of 11 sectors posting double-digit EPS growth, notably Financials and Cyclicals. Although corporate profits remain robust, investor sentiment is more mixed as several companies reported profit warnings or negative guidance, which in some cases was related to trade tensions. This has raised concerns that earnings growth could decelerate faster than expected, while margins could be dented by the fading benefits from tax cuts, higher raw material and freight costs, rising wages and higher funding costs.

Despite these headwinds, we believe the equity market sell-off appears excessive. The fundamental backdrop has not changed as global growth is still supported by the US. In China, the authorities appear to have acknowledged the challenges and are taking effective measures to support the economy. The picture is less compelling in the EMU and Japan but the recovery is still rather recent. If the market stress continues until the next FOMC meeting on 8 November, Chairman Powell could be tempted to offer support to the economy should growth start to decelerate. In addition, US corporate profits should continue to grow – albeit at a slower pace – as sales growth remains solid and corporate margins sound.

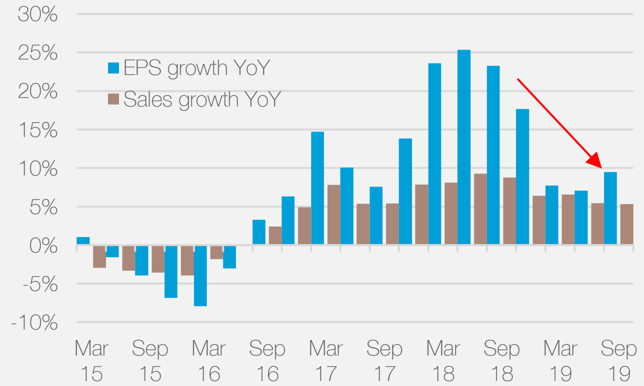
Putting it all together – We think that equities are unlikely to enter a bear market. We suggest keeping a moderate pro-cycle allocation with a preference for US equities versus eurozone and Japanese equities. In fixed income, we maintain a preference for short-dated bonds and high yielding credit in Europe. We stay defensive on long-dates bonds (US Treasuries and German Bund) as interest risks are titled to the upside.

Equity market sell-off seems excessive in respect to US activity
S&P 500 and US ISM Manufacturing



Sources: SGPB, Macrobond data as of 25 October 2018

Corporate profits expected to grow at a slower pace in coming quarters
EPS and Sales growth YoY



Sources: SGPB, Bloomberg data as of 25 October 2018

This week and next

EUROZONE

- After five consecutive months of decline, consumer confidence exceeded expectations and rebounded slightly from -2.9 to -2.7 in October, according to initial estimates.
- Manufacturing confidence (the PMI index) fell from 53.2 to 52.1 in October, after the German indicator hit a 29-month low at 52.3. Services confidence weakened from 54.7 to 53.3, sending the composite indicator down from 54.1 to 52.7.
- Unsurprisingly, the ECB maintained its refinancing and deposit facility rate, at respectively 0.0% and -0.4%.
- The annual growth rate of loans to households stood at 3.1% in September, whereas loans to non-financial corporations rose from 4.2% YoY to 4.3%, the highest rate since the 2008 financial crisis.

Next week's key events		Per.	Prev.	Cons.
30 Oct	GDP YoY (P)	Q3	2.1%	1.8%
31 Oct	Headline inflation YoY	Oct	2.1%	2.1%

UNITED KINGDOM

- Business sentiment deteriorated according to the Confederation of British Industry's (CBI) latest Industrial Trends Survey as the clock ticks down towards Brexit-day. Manufacturing new orders slid at their fastest pace in three years in the quarter to October, reflecting weaknesses both in domestic and export orders. The survey indicated that output growth was stable in the three months to October but was expected to be flat over the coming quarter.
- Mortgage approvals for house purchases dropped to a six-month low of 38.5k in September, down 6.7% YoY.
- Brexit worries has prompted an increase in personal deposits, up 0.9% YoY in September, with a preference for cash for immediate use. Instant access deposit levels grew 3.1% YoY.

Next week's key events		Per.	Prev.	Cons.
31 Oct	GfK consumer confidence	Oct	-9	-10
01 Nov	Manufacturing PMI	Oct	53.8	53

UNITED STATES

- Manufacturing confidence gained ground in October, according to the preliminary PMI estimates up from 55.6 to 55.9. The Services estimate came in up from 53.5 to 54.7, thus sending the composite reading up from 53.9 to 54.8, still well above the crucial 50.0 no-change threshold.
- Durable goods demand (ex. transport) was slower in September, up only by a modest 0.1% MoM after 0.3% (data revised) in August. Non-defence capital goods (ex. aircraft), a closely followed proxy for business spending plans, dipped 0.1% in September after -0.2% (data revised) in August.
- Last week, the number of people filling for unemployment benefits rose from 210k to 215k despite an unchanged 4-week average measure at 212k, i.e. close to historical lows.

Next week's key events		Per.	Prev.	Cons.
02 Nov	Average earnings YoY	Oct	2.8%	23.1%
02 Nov	Trade balance deficit ($bn)	Sep	53.2	52.2

ASIA & EMERGING COUNTRIES

- In Japan, manufacturing confidence edged up from 52.5 to 53.1 in October with an acceleration in output, new orders and employment. According to the report, export sales rose for the first time since May, despite the growing concern around global trade tensions.
- In South Korea, GDP growth decelerated from 2.8% YoY to 2.0% in Q3, slightly lower than expectations but in line with Q2's 0.6% QoQ growth. Higher private consumption and exports offset the plunge in construction investment (-6.4% QoQ).

Next week's key events		Per.	Prev.	Cons.
29 Oct	Japan: Retail sales YoY	Sep	2.7%	2.0%
31 Oct	Japan: Industrial output MoM	Sep	0.2%	-0.2%

Sources: Datastream, Bloomberg, 26 October 2018, Note: YoY = year-on-year; QoQ = quarter-on-quarter; MoM = month-on-month, P = preliminary figure, A = advanced figure, F = final figure seasonally adjusted, ECB = European Central Bank

Our 3-month targets for currencies and commodities

	Thursday close	3mth target
EUR/USD	1.14	1.15
GBP/USD	1.28	1.32
EUR/CHF	1.14	1.09
USD/JPY	112	110
Brent	$77	$80
Gold	$1229	$1220

Forecast figures are not a reliable indicator of future performance

Our 3-month targets are unchanged this week.

Question time

Past performance should not be seen as a guarantee of future returns.

No Q&A this week.

Market performance

Past performance should not be seen as a guarantee of future returns.

Interest rates

Interest rates	Last	1wk		3mth	YTD	12mth
EONIA (EUR)	-37 bp	0 bp	→	0 bp	-2 bp	-1 bp
3mth Euribor (EUR)	-32 bp	0 bp	→	0 bp	1 bp	1 bp
3mth Libor (USD)	251 bp	4 bp	↑	17 bp	81 bp	113 bp
3mth Libor (GBP)	81 bp	0 bp	→	2 bp	29 bp	39 bp
10-year US Treasury bond	314 bp	-4 bp	↓	rke	73 bp	69 bp
10-year German bond	40 bp	-3 bp	↓	1 bp	-3 bp	-9 bp
10-year French bond	77 bp	-3 bp	↓	8 bp	-1 bp	-11 bp
10-year UK bond	144 bp	-10 bp	↓	17 bp	26 bp	4 bp

Credit

Credit	1wk		3mth	YTD	12mth
BAML EURO Corp. IG	-0.2%	↓	-0.4 %	-0.6 %	-0.3 %
BAML EURO Corp HY	-0.7%	↓	-0.9 %	-1.3 %	-1.3 %
BAML GBP Corp IG	0.6%	↑	-0.2 %	-1.5 %	0.7 %
BAML US IG	-0.1%	→	-0.7 %	-3.2 %	-2.0 %
BAML US HY	-0.6%	↓	0.1 %	1.0 %	1.1 %
JPM Global EM Sov. Plus	-0.5%	↓	-2.1 %	-6.0 %	-5.0 %

Exchange rates

Exchange rates	Last	1wk		3mth	YTD	12mth
EUR/USD	1.14	-0.7 %	↓	-3.0 %	-5.3 %	-3.7%
EUR/CHF	1.14	-0.3 %	↓	-2.3 %	-2.8 %	-2.7%
GBP/USD	1.28	-1.5 %	↓	-2.8 %	-5.1 %	-3.4%
USD/JPY	112	0.2 %	↑	1.3 %	-0.2 %	-1.2%
USD/BRL	3.71	-0.4 %	↓	0.5 %	11.9 %	14.6%
USD/CNY	6.95	0.2 %	↑	2.6 %	6.8 %	4.7%
USD/RUB	65.6	-0.3 %	↓	4.4 %	13.8 %	13.6%

Government bonds*

Government bonds*	1wk		3mth	YTD	12mth
United States (3-7yr)	0.3 %	↑	0.0 %	-1.1 %	-1.3 %
United Kingdom (3-7yr)	0.5 %	↑	0.3 %	0.1 %	0.8 %
Germany (3-7yr)	0.1 %	↑	-0.1 %	0.5 %	0.2 %
Japan (3-7yr)	0.1 %	↑	-0.1 %	-0.1 %	0.0 %

Equities*

Equities*	Last	1wk		3mth	YTD	12mth
MSCI AC World	481	-2.7 %	↓	-7.3 %	-4.3 %	-0.1 %
Eurostoxx 50	3,164	-1.5 %	↓	-8.5 %	-6.7 %	-8.7 %
DAX	11,307	-2.4 %	↓	-10.1 %	-12.5 %	-12.7 %
CAC 40	5,032	-1.7 %	↓	-7.1 %	-2.5 %	-3.3 %
S&P 500	2,706	-2.3 %	↓	-4.5 %	2.8 %	7.9 %
FTSE 100	7,004	-0.3 %	↓	-7.4 %	-5.6 %	-2.0 %
SMI	8,706	-0.8 %	↓	-3.4 %	-4.0 %	-0.8 %
Topix	1,601	-6.1 %	↓	-7.9 %	-10.2 %	-6.6 %
IBOV Brazil	84,084	0.3 %	↑	4.8 %	10.1 %	9.7 %
MICEX Russia *	2,332	-2.0 %	↓	2.1 %	10.5 %	13.8 %
MSCI EM	949	-2.2 %	↓	-12.3 %	-16.0 %	-12.4 %
SENSEX 30 India	33,690	-3.0 %	↓	-8.3 %	0.8 %	3.2 %
Hang Seng (H-K)	24,994	-1.8 %	↓	-12.8 %	-13.6 %	-8.6 %
Shanghaï Composite	2,604	4.7 %	↑	-10.3 %	-21.3 %	-23.3 %

Commodities

Commodities	Last	1wk		3mth	YTD	12mth
Brent	$77	-3.4 %	↓	4.0 %	15.5 %	31.8 %
Gold	$1,229	0.2 %	↑	0.1 %	-5.7 %	-3.7 %
Silver	$14.6	-0.1 %	→	-6.0 %	-14.0 %	-13.5 %

Source: DataStream, on 25/10/2018. 1wk = 1-week change, 3mth = 3-month change, 12mth = 12-month change, YTD = year-to-date change, YoY = year-on-year change, BAML = Bank of America Merrill Lynch, JPM = JP Morgan, IG = Investment Grade, EM = emerging markets. * Price return for MICEX equity index. Equities; total return in local currency. Government bonds = 3-7 year returns. Figures are rounded.

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