

# WEEKLY UPDATE

## Rainy days for eurozone banks

Given the significant underperformance of eurozone banks last year, the sector is now one of the most attractively valued with an average price-to-book ratio at 0.6, whereas US banks trade at 1.3 (source: MSCI, 8 February 2019). Although banks in both areas encountered numerous challenges in the wake of the global financial crisis, eurozone banks still face significant hurdles. Their underperformance is no surprise.

**Regulatory environment.** Bank profitability has been significantly dented by a much stricter regulatory environment. Preventing excessive risk taking and fostering a sound and transparent banking system made great sense after the crisis. But the rising tide of new regulations, lower leverage, higher capital ratios and more stringent funding rules have structurally lowered profitability.

**Litigation.** Financial penalties have been a persistent drag on profits for eurozone banks over the past decade. This risk may be receding, but investors remain sceptical for now.

**Economic downturns.** These tend to inflate the size of non-performing loans on balance sheets, as was seen after the 2008-2009 and 2012-2013 recessions. Across the eurozone, outstanding bad loans still stand at 4.2% of total loans, versus around 1% in the US. In the periphery, where banks were hit hardest (Spain's housing bubble, slow structural growth in Italy, depression in Greece), they are still struggling to fix their balance sheets. The European Central Bank's (ECB) Single Supervisory Mechanism recently set more stringent targets to improve the bad loan disposal process. But much remains to be done.

**Low interest rates.** The current rates environment is weighing on banks' profitability. The ECB's deposit rate has been in negative territory since June 2014 (-0.4% since March 2016). Banks are therefore suffering from a negative tax on their deposits at the ECB, with a knock-on impact on profitability. The Quantitative Easing (QE) programme has also lowered long-term yields significantly. Indeed, net interest margins for eurozone banks were only 1.5% in Q3 2018, less than half of the 3.5% in the US.

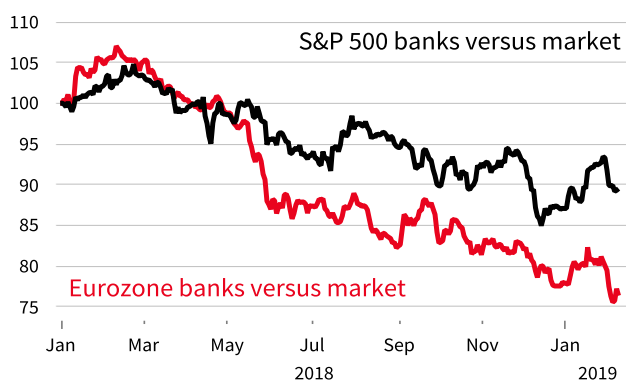
**Enhanced competition.** The US banking sector has undergone rapid consolidation. In the eurozone, the sector is much more fragmented with myriad domestic competitors – regional banks in Germany, municipal banks in Italy, mutually-owned banks in France etc. And recent speculation that Germany's two largest listed banks might merge suggests that there is more appetite for domestic tie-ups rather than cross-border mergers at present.

**Technological changes.** The ongoing digitalisation of the banking sector is also a challenge. With the emergence of new internet competitors providing low-cost services, banks' margins are under pressure while they are forced to beef up IT spending to keep up.

**Bottom-line.** Eurozone banks' current valuations seem rather attractive, but upside potential may be limited in the short term and we maintain a neutral stance. However, any indication of a shift upwards in interest rates or a further reshaping of business models could offer potential for a rebound.

### Eurozone banks underperform their US peers

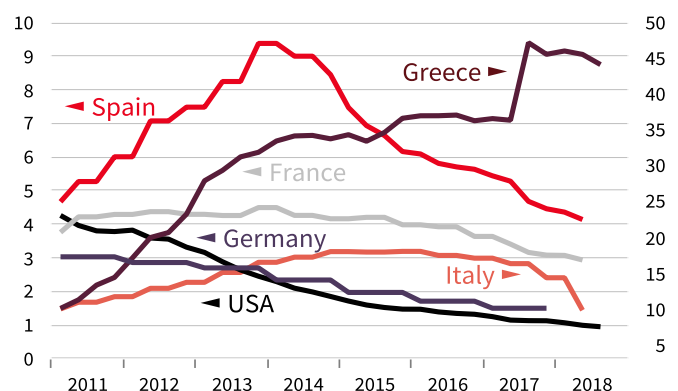
*Euro Stoxx 50 vs banks & S&P500 vs banks*



Sources: SGPB, Macrobond, STOXX, S&P, data as of 07/02/2019

### Non-performing loans jump up

*Non-Performing Loans to Total Gross Loans (%)*



Sources: SGPB, Macrobond, IMF, latest data as of Q3 2018

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

All data taken from Bloomberg, Macrobond (07/02/2019) and IMF, MSCI, EBA and FDIC.

In accordance with the applicable regulation, we inform the reader that this material is qualified as a marketing document.

CA044/FEB/2019

## THIS WEEK AND NEXT

### EUROZONE

- Confidence in services increased unexpectedly to 51.2 in January from the first estimate of 50.8, boosting final Composite PMI to 51.0, above the consensus 50.7.
- Investor sentiment reached a 4-year low, slipping from -1.5 to -3.7 in February.
- As expected, December retail sales fell -1.6% MoM, versus +0.8% the previous month, pushing YoY change down to 0.8% from 1.8%. However, lower inflation and higher wages should support consumption in the near future.

### UNITED KINGDOM

- Contrary to market expectations, confidence declined in both construction and services, printing at 50.6 and 50.1 respectively, close to contraction territory.
- According to the British Retail Consortium, retail sales rebounded from -0.7% YoY to 1.8% in January.
- All nine voting members at the Bank of England's Monetary Policy Committee agreed to maintain the base rate unchanged at 0.75%.



#### Next week's key events

		Per.	Prev.	Cons.
13 Feb	Industrial production MoM	Dec	-1.7%	-0.2%
14 Feb	GDP growth YoY	Q4 (P)	1.2%	1.2%
14 Feb	Germany: GDP growth QoQ	Q4 (P)	-0.2%	0.2%



#### Next week's key events

		Per.	Prev.	Cons.
11 Feb	GDP growth 3M/3M	Dec (P)	0.3%	0.3%
11 Feb	Manufacturing output YoY	Dec	-1.1%	-1.0%
13 Feb	Headline inflation YoY	Jan	2.1%	2.0%

### UNITED STATES

- The ISM Non-Manufacturing confidence index missed expectations for the second consecutive month, at 56.7 in January after 58.0 in December.
- Factory orders fell -0.6% MoM in November, below expectations for a 0.3% rise but an improvement on October's -2.1%.
- The trade deficit narrowed more than expected, from \$55.7bn in October to \$49.3bn in November due to a decline in imports.

### ASIA & EMERGING COUNTRIES

- In Japan, confidence in services edged up from 51.0 to 51.6 in January supported by sustained domestic activity, while in China, confidence in services decreased slightly from 53.9 to 53.6.
- The Indonesian economy contracted 1.7% QoQ in Q4 but expanded 5.2% in 2018 (full-year figures) after 5.1% in 2017.
- In Brazil, December industrial output fell -3.6% YoY, the sharpest fall in six months and the second decline in a row (November: -1.0%).



#### Next week's key events

		Per.	Prev.	Cons.
13 Feb	Headline inflation YoY	Jan	1.9%	1.5%
14 Feb	Initial jobless claims	4 Feb	234k	--
15 Feb	Univ. Michigan consumer sentiment	Feb (P)	91.2	94.0



#### Next week's key events

		Per.	Prev.	Cons.
14 Feb	Japan: GDP growth QoQ	Q4	-0.6%	0.4%
14 Feb	China: Trade balance (\$bn)	Jan	57	32
15 Feb	China: Headline inflation YoY	Jan	1.9%	2.0%

Sources: DataStream, Bloomberg, 8 February 2019

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	1.13	1.13
GBP/USD	1.30	1.30
EUR/CHF	1.14	1.13
USD/JPY	110	112
Brent	\$61.4	\$65
Gold (once)	\$1310	\$1250

Changes made to our 3-month targets this week.

Forecast figures are not a reliable indicator of future performance

## MARKET PERFORMANCE

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

Interest rates	Last	1wk	3mth	YTD	12mth
EONIA (EUR)	0 bp	0 bp →	0 bp	0 bp	0 bp
3mth Euribor (EUR)	0 bp	0 bp →	0 bp	0 bp	0 bp
3mth Libor (USD)	0 bp	0 bp →	0 bp	0 bp	0 bp
3mth Libor (GBP)	0 bp	0 bp →	0 bp	0 bp	0 bp
10-year US Treasury bond	265 bp	2 bp ↑	-56 bp	-4 bp	-19 bp
10-year German bond	17 bp	1 bp →	-28 bp	-8 bp	-57 bp
10-year French bond	55 bp	-1 bp →	-26 bp	-16 bp	-43 bp
10-year UK bond	118 bp	-4 bp ↓	-35 bp	-9 bp	-37 bp

Government bonds*	Last	1wk	3mth	YTD	12mth
United States (3-7yr)	0.0 %	→	0.0 %	0.0 %	0.0 %
United Kingdom (3-7yr)	0.0 %	→	0.0 %	0.0 %	0.0 %
Germany (3-7yr)	0.0 %	→	0.0 %	0.0 %	0.0 %
Japan (3-7yr)	0.0 %	→	0.0 %	0.0 %	0.0 %

Credit	Last	1wk	3mth	YTD	12mth
BAML EURO Corp. IG	0.0 %	→	0.0 %	0.0 %	0.0 %
BAML EURO Corp HY	0.0 %	→	0.0 %	0.0 %	0.0 %
BAML GBP Corp IG	0.0 %	→	0.0 %	0.0 %	0.0 %
BAML US IG	0.0 %	→	0.0 %	0.0 %	0.0 %
BAML US HY	0.0 %	→	0.0 %	0.0 %	0.0 %
BAML Global EM Sov. External Plus	0.0 %	→	0.0 %	0.0 %	0.0 %

Exchange rates	Last	1wk	3mth	YTD	12mth
EUR/USD	1.13	-0.9 % ↓	-0.7 %	-1.1 %	-7.5 %
EUR/CHF	1.14	-0.1 % →	-0.7 %	1.0 %	-1.7 %
GBP/USD	1.30	-1.1 % ↓	-1.3 %	1.5 %	-6.7 %
USD/JPY	110	0.9 % ↑	-3.3 %	0.2 %	0.4 %
USD/BRL	3.72	2.0 % ↑	-0.4 %	-4.2 %	13.6 %
USD/CNY	6.74	0.7 % ↑	-2.5 %	-1.9 %	7.6 %
USD/RUB	65.9	0.9 % ↑	-0.4 %	-5.4 %	13.9 %

Equities*	Last	1wk	3mth	YTD	12mth
MSCI AC World	490	-0.1 % ↓	-1.5 %	7.8 %	-2.0 %
Eurostoxx 50	3,151	-0.3 % ↓	-2.4 %	5.3 %	-5.4 %
DAX	11,022	-1.4 % ↓	-4.8 %	4.4 %	-12.5 %
CAC 40	4,986	-0.1 % ↓	-2.6 %	5.4 %	-2.0 %
S&P 500	2,706	0.1 % ↑	-3.3 %	8.1 %	2.9 %
FTSE 100	7,094	1.8 % ↑	0.3 %	5.5 %	1.6 %
SMI	9,036	0.7 % ↑	-0.2 %	7.2 %	4.2 %
Topix	1,569	0.1 % →	-4.8 %	5.0 %	-8.4 %
IBOV Brazil	94,406	-3.1 % ↓	7.6 %	7.4 %	14.1 %
MICEX Russia *	2,510	-0.4 % ↓	2.6 %	6.4 %	11.3 %
MSCI EM	1,042	-0.7 % ↓	4.9 %	8.0 %	-8.7 %
SENSEX 30 India	36,971	2.0 % ↑	5.7 %	2.6 %	9.8 %
Hang Seng (H-K)	27,990	0.2 % ↑	7.2 %	8.3 %	-4.4 %
Shanghai Composite	2,618	1.3 % ↑	-0.9 %	5.0 %	-20.9 %

Commodities	Last	1wk	3mth	YTD	12mth
Brent	\$61.4	-1.5 % ↓	-14.3 %	15.5 %	-7.0 %
Gold	\$1,310	-0.9 % ↓	6.8 %	2.3 %	-0.9 %
Copper	\$6,228	1.3 % ↑	0.9 %	4.7 %	-8.9 %

Source: DataStream, on 7 February 2019.

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.

## IMPORTANT INFORMATION – PLEASE READ

Societe Generale Private Banking (“SGPB”) is a division of the group Societe Generale S.A., operating through its head office within Societe Generale S.A and its network (subsidiaries, branches or departments of Societe Generale S.A.) located in the countries mentioned hereafter which use the “Societe Generale Private Banking” brand, and which distribute this document.

This document not constitute and under no circumstances should it be considered in whole or in part as an offer, a solicitation, or a contract from any of the Societe Generale Private Banking entities. It is intended to be used by the recipient only and may not be passed on or disclosed to any other persons and/or in any jurisdiction that would render the distribution illegal.

It is the responsibility of any person in possession of this document to inform himself or herself of and to observe all applicable laws and regulations of the relevant jurisdictions. This document is in no way intended to be distributed in or into the United States of America nor directly or indirectly to any U.S. person.

### Financial Promotion

This document is a financial promotion.

### Limitation

Information herein is believed to be reliable but the SGPB does not warrant its completeness or accuracy and it should not be relied on or acted upon without further verification. SGPB disclaims any responsibility to update or make any revisions to this document. Opinions, estimates and expressions of judgment are those of the writer and are subject to change without notice. As such, SGPB, Societe Generale and its other subsidiaries shall not be held liable for any consequences, financial or otherwise, following any action taken or not taken in relation to this document and its contents.

### Past Performance

Past performance should not be seen as an indication of future performance. Investments may be subject to market fluctuations and the price and value of investments and the income derived from them can go down as well as up. Your capital may be at risk and you may not get back the amount you invest. Changes in inflation, interest rates and the rate of exchange may have an adverse effect on the value, price and income of investments.

The Societe Generale Private Banking entities disclaim any responsibility for the updating or revising of this document. The document’s only aim is to offer information to investors, who will take their investment decisions without relying solely on this document. The Societe Generale Private Banking entities disclaim all responsibility for direct or indirect losses related to any use of this document or its content. The Societe Generale Private Banking entities do not offer implicit or explicit guarantees as to the accuracy or exhaustiveness of the information or as to the profitability or performance of the asset classes, countries and markets concerned.

The historical data, information and opinions provided herein have been obtained from, or are based upon, external sources that the Societe Generale Private Banking entities believe to be reliable, but which have not been independently verified. The Societe Generale Private Banking entities shall not be liable for the accuracy, relevance or exhaustiveness of this information.

### Specific warnings per jurisdiction

**France:** Unless otherwise expressly indicated, this document is issued and distributed by Societe Generale, a French bank authorised and supervised by the Autorité de Contrôle Prudentiel et de Résolution, located at 61, rue Taitbout, 75436 Paris Cedex 09 under the prudential supervision of the European Central Bank- ECB, and registered at ORIAS as an insurance intermediary under the number 07 022 493 orias.fr. Societe Generale is a French Société Anonyme with its registered address at 29 boulevard Haussmann, 75009 Paris, with a capital of EUR 1,009,380,011.25 on 31 March 2016 and unique identification number 552 120 222 R.C.S. Paris. Further details are available on request or can be found at [www.privatebanking.societegenerale.fr/](http://www.privatebanking.societegenerale.fr/).

**The Bahamas:** This document has been distributed in The Bahamas to its private clients by Societe Generale Private Banking (Bahamas) Ltd., an entity duly licensed and regulated by the Securities Commission of the Bahamas (the “Securities Commission”). This document is not intended for distribution to persons or entities that are Bahamian citizens or that have been designated as residents of The Bahamas under the Exchange Control Regulations, 1956 of The Bahamas. This document is not, is not intended to be, and under no circumstances is to be construed as a distribution of any securities in The Bahamas. Neither the Securities

Commission nor any similar authority in The Bahamas has reviewed or in any way passed upon this document or the merits of the securities described, or any representations made herein.

**Belgium:** This document has been distributed in Belgium by Societe Generale Private Banking SA/NV, a Belgian credit institution according to Belgian law and controlled and supervised by the National Bank of Belgium (NBB) and the Financial Services and Markets Authority (FSMA), and under the prudential supervision of the European Central Bank- ECB. Societe Generale Private Banking SA/NV is registered as an insurance broker at the FSMA under the number 61033A. Societe Generale Private Banking SA/NV has its registered address at 9000 Ghent, Kortrijksesteenweg 302, registered at the RPM Ghent, under the number VAT BE 0415.835.337. Further details are available on request or can be found at [www.privatebanking.societegenerale.be](http://www.privatebanking.societegenerale.be).

**Dubai:** The present document has been distributed by Societe Generale, DIFC Branch (SG DIFC). Related financial products or services are only available to clients having signed a DIFC Client Agreement with SG DIFC and qualifying as professional clients with liquid assets of over \$1 million, and who have sufficient financial experience and understanding to participate in the relevant financial markets, according to the Dubai Financial Services Authority (DFSA) rules. SG DIFC is duly licensed and regulated by the DFSA to provide arranging and advisory services. SG DIFC does not provide certain products and/or services (such as discretionary portfolio management, managed advisory services, Prime Market Access), but the branch's clients can if necessary have access to these products and/or services at the Societe Generale Private Banking entity holding the client's bank account. The DFSA has neither reviewed nor approved this document. Further details are available on request or can be found at [www.privatebanking.societegenerale.ae](http://www.privatebanking.societegenerale.ae)

**Luxembourg:** This document has been distributed in Luxembourg by Societe Generale Bank and Trust ("SGBT"), a credit institution which is authorised and regulated by the Commission de Surveillance du Secteur Financier, under the prudential supervision of the European Central Bank- ECB, and whose head office is located at 11 avenue Emile Reuter – L 2420 Luxembourg. Further details are available on request or can be found at [www.sgbt.lu](http://www.sgbt.lu). No investment decision whatsoever may result from solely reading this document. SGBT accepts no responsibility for the accuracy or otherwise of information contained in this document. SGBT accepts no liability or otherwise in respect of actions taken by recipients on the basis of this document only and SGBT does not hold itself out as providing any advice, particularly in relation to investment services. The opinions, views and forecasts expressed in this document (including any attachments thereto) reflect the personal views of the author(s) and do not reflect the views of any other person or SGBT unless otherwise mentioned. SGBT has neither verified nor independently analysed the information contained in this document. The Commission de Surveillance du Secteur Financier has neither verified nor analysed the information contained in this document.

**Monaco:** The present document is distributed in Monaco by Societe Generale Private Banking (Monaco) S.A.M., located 13, 15 Bd des Moulins, 98000 Monaco, Principality of Monaco, governed by the 'Autorité de Contrôle Prudentiel et de Résolution' and the 'Commission de Contrôle des Activités Financières'. The Financial products marketed in Monaco can be reserved for qualified investors in accordance with Law No. 1339 of 07/09/2007 and Sovereign Ordinance No 1.285 of 10/09/2007. Further details are available upon request or on [www.privatebanking.societegenerale.mc](http://www.privatebanking.societegenerale.mc).

**Suisse:** This document has been communicated in Suisse by Societe Generale Private Banking (Suisse) SA ("SGPBS"), whose head office is located at rue du Rhône 8, CP 022, CH-1211 Geneva 11. SGPBS is a bank authorized by the Swiss Financial Market Supervisory Authority FINMA. Further details are available on request or can be found at <http://www.privatebanking.societegenerale.ch>.

This document (i) does not provide any opinion or recommendation about a company or a security, or (ii) has been prepared outside of Suisse by SGPB. Therefore, the Directives of the Swiss Bankers Association (SBA) on the Independence of Financial Research do not apply to this document.

This document has not been prepared by SGPBS. SGPBS has neither verified nor independently analyzed the information contained in this document. SGPBS accepts no responsibility for the accuracy or otherwise of information contained in this document. The opinions, views and forecasts expressed in this document reflect the personal views of the relevant author(s) and shall not engage SGPBS' liability.

This document is not a prospectus within the meaning of articles 652a and 1156 of the Swiss Code of Obligations.

**United Kingdom:** This document has been distributed in the United Kingdom by SG Kleinwort Hambros Bank Limited, which is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

The company is incorporated in England & Wales under number 964058 and its registered address is 5<sup>th</sup> Floor, 8 St. James's Square, London SW1Y 4JU ("SGPB Hambros").

**Jersey:** This document has been distributed in Jersey by SG Kleinwort Hambros Bank (Channel Islands) Limited ("SGH CI Limited"), which is regulated by the Jersey Financial Services Commission ("JFSC") for banking, investment, funds services and money services business. The company is also authorised and regulated by the UK Financial Conduct Authority ("FCA") in respect of UK regulated mortgage business. The firm reference number is 310344. The company is incorporated in Jersey under number 2693 and its registered address is PO Box 78, SG Hambros House, 18 Esplanade, St Helier, Jersey JE4 8PR. This document has not been authorised or reviewed by the JFSC or FCA.

**Guernsey:** This document has been distributed in or from within the Bailiwick of Guernsey by SG Kleinwort Hambros Bank (Channel Islands) Limited – Guernsey Branch, which is regulated by the Guernsey Financial Services Commission ("GFSC") for banking, investment and money services business and by the Jersey Financial Services Commission ("JFSC") for banking, investment, fund services and money services business. Its address is PO Box 6, Hambro House, St Julian's Avenue, St Peter Port, Guernsey, GY1 3AE.

SG Kleinwort Hambros Bank (CI) Limited (including the branch) is also authorised and regulated by the UK Financial Conduct Authority ("FCA") in respect of UK regulated mortgage business. The firm reference number is 310344. The company is incorporated in Jersey under number 2693 and its registered address is PO Box 78, SG Hambros House, 18 Esplanade, St Helier, Jersey JE4 8PR. This document has not been authorised or reviewed by the JFSC, GFSC or FCA.

**Gibraltar:** This document has been distributed in Gibraltar by SG Kleinwort Hambros Bank (Gibraltar) Limited, which is authorised and regulated by the Gibraltar Financial Services Commission for the conduct of banking, investment and insurance mediation business.

The company is incorporated in Gibraltar under number 01294 and its registered address is 32 Line Wall Road, Gibraltar.

Societe Generale Private Banking Hambros is part of the wealth management arm of the Societe Generale Group, Societe Generale Private Banking. Societe Generale is a French bank authorised in France by the Autorité de Contrôle Prudentiel et de Résolution, located at 61, rue Taitbout, 75436 Paris Cedex 09, and under the prudential supervision of the European Central Bank - ECB. It is also authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. Further information on the SGPB Hambros Group including additional legal and regulatory details can be found on [www.privatebanking.societegenerale.com/hambros](http://www.privatebanking.societegenerale.com/hambros)

**Notice to US Investors:** This document is not intended for US Persons under the US Securities Act of 1933, as amended and under the various laws of the States of the US of America.

<http://www.privatebanking.societegenerale.com>.

© Copyright Societe Generale Group 2019. All rights reserved. Any unauthorised use, duplication, redistribution or disclosure in whole or in part is prohibited without the prior consent of Societe Generale.

The key symbols, Societe Generale, Societe Generale Private Banking are registered trademarks of SG. All rights reserved.