A slow grind higher

May 2020

The World in five bullet points

- Covid-related Lockdown restrictions began to loosen around the world but the pace of easing varied widely. The US saw all 50 states roll back restrictions in some form while China was forced to re-impose lockdown in its northern Jilin Province. Meanwhile in Europe, Spain said it would consider allowing tourists back from July and Italy said it was taking a ‘calculated risk’ to ease its restrictions. Germany saw sporting events restart but the UK remained largely locked-down by month end. Epidemiologists argued if restrictions were lifted too soon countries or states would soon see a second wave of infections.
- Despite the easing of restrictions, global Covid-19 cases continued to rise albeit it at a continuing slower pace with total infections reaching 5.8 million by the end of May. The US continued to have the most infections (1.8m), followed by Brazil (515k) and Russia (400k). The development of a vaccine continued at pace with AstraZeneca and biotech company Moderna showing promising results on new compounds, while a treatment drug remdesivir made by Gilead was approved for emergency use in several countries.
- China’s government said it would introduce **new security laws in Hong Kong** while the stock market in Hong Kong fell sharply on fears the security law imposition would erode the city’s financial clout. Shanghai’s stock markets also underperformed.
- The imposition of new security laws in Hong Kong contributed to the re-emergence of **US-China tensions** that had been simmering for some weeks as the White House and Beijing played the blame game over the spread of Covid-19. New York-listed/China domiciled ADRs became one target of the White House while the Commerce Department effectively closed Huawei’s access to Asian chip foundries, thereby adding to the tensions.
- **Protests erupted in many US cities** at the end of the month and continued into the first few days of June after the George Floyd incident. The protests spread to Washington where President Trump was briefly led to an underground bunker as crowds gathered close to the White House. Although the protests were largely peaceful, violence in several cities grabbed the headlines and forced the US dollar down 0.7% in the final week.

Figure 1. MSCI AC World Index

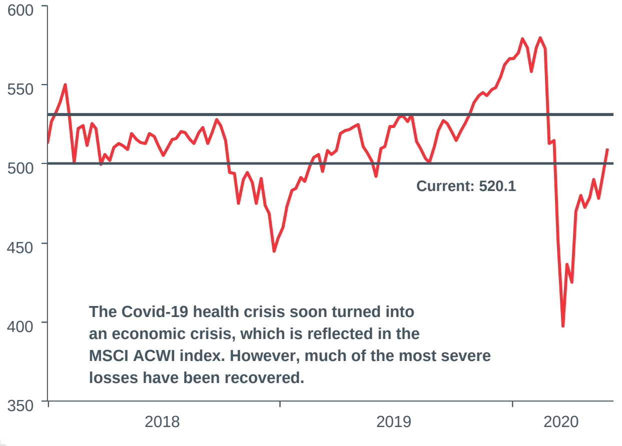
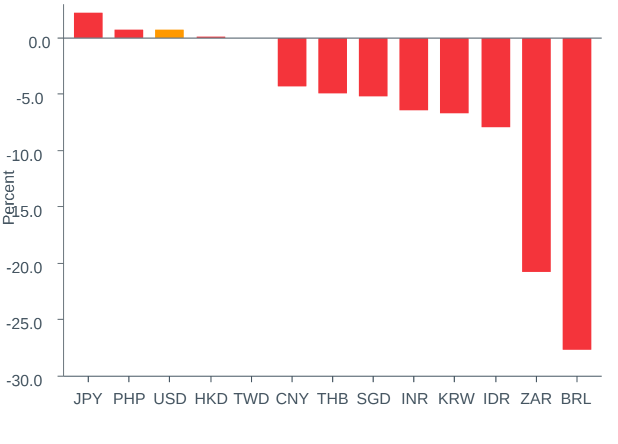


Figure 2. EM Currencies since 20 January



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of as of 31 May 2020.

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Equity Markets

- **Global equity markets** regained more lost ground in May as economic stimulus programmes and a gradual re-opening of economies around the world – or at least the plans for such re-openings – provided support for most markets. But gains were tempered by a re-emergence of tensions between the US and China, especially over the new security law in Hong Kong. Large industrial economies in developed markets led the gainers with Japan adding 5.9%, Germany 8.9% and the US 5.2%, giving the MSCI Developed Markets index a 4.9% gain.
- **Emerging Markets**, ex Hong Kong, ground their way higher with the MSCI EM index adding 0.8%. **Latin America** led the way after gaining 6.5%, largely as a result of Brazil's 8.5% return on supportive comments from the central bank on intervention in the FX market and as commodity prices continued to recover while, at the same time, shrugging off a surge in Covid infections. A 19.9% gain in Argentina was partially offset by a 5.4% fall in Chile as a surge in Covid cases caused Santiago to go into complete lockdown. **EMEA** gained 3.8% with Russia up 8.7% on higher crude prices and a stronger ruble, and Turkey saw a 6% gain as the lira appreciated.
- **Asia's** returns were very mixed with the Asia ex Japan index losing 1.1% but the Asia Pacific ex Japan index losing just 0.3%, reflecting Australia's outperformance. **Hong Kong** fell 8.4% after Beijing said it would impose a new security law, raising fears of capital flight from the city. **Shanghai's** markets were also weighed by the same news and on the increasing tensions with the US, as well as some weak economic data, leading the MSCI China H share index to fall 0.5%. The A Shares index held on to a 3.3% gain however with both markets seeing a rotation into cyclicals. **Taiwan** also fell on news the White House was looking to extend its technology ban on Huawei that would affect its chipmakers as well as on Apple's decision not to give a full-year guidance.
- Elsewhere in Asia, performances were equally diverse with **India** down 2.8% as banks dragged on a stimulus package that failed to include a restructuring of its debt as well as a three-month moratorium on loan repayments. **Singapore** underperformed to lose 3.2% on the increasing trade dispute rhetoric but **Thailand** gained another 4.4% to add to April's 16% gain as interest rates were cut again. **Korea** also put on another 2.2% as the central bank cut rates by 25bps although gains here were capped by the weak Chinese economic data and a re-spike in Covid cases.
- **Australia** gained another 4.6%, tracking more developed markets, as its currency gained against the US dollar, and shrugging off an increase in tensions between it and China over trade and the Covid outbreak.

Figure 3. Regional Equity Indices

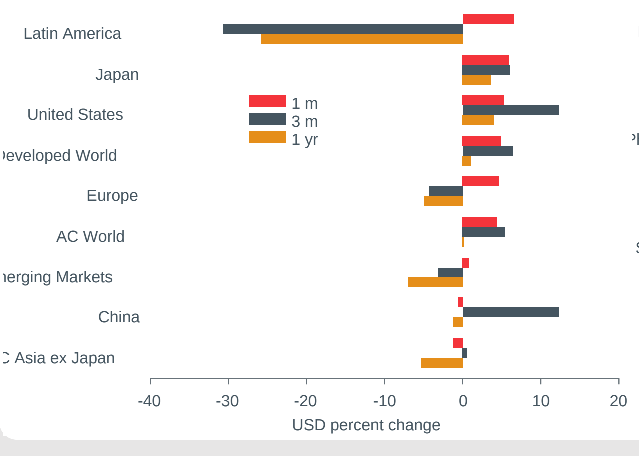
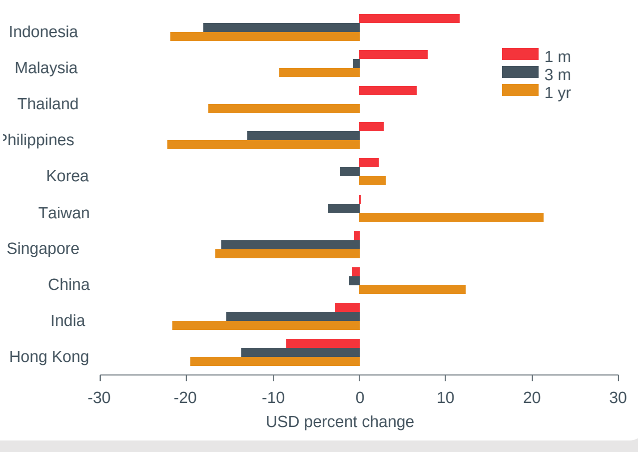


Figure 4. Asia Equity Indices



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of 31 May 2020. For representative indices and acronym details please refer to notes in the appendix. Quoted returns are MSCI, US dollar denominated total returns.

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Fixed Income

- **Government bond yields** were mixed in a month of heightened geopolitical tensions. On top of the Covid-19 pandemic, markets had to digest the deterioration in China-US relations and escalating social unrest in Hong Kong and the US. Economic data diverged, with US underscoring severe disruption in activity from the pandemic, but some Chinese numbers gave hope that a recovery was underway. Against this mixed backdrop, market sentiment remained fragile although this was cushioned by ample liquidity.
- In the **US**, fresh job losses totalling 20.5 million in May alone pushed the domestic unemployment rate to a historic high of 14.7% in April as thousands of businesses closed or furloughed workers. Retail sales and industrial production fell by a record levels while the Federal Reserve again sought to calm markets. While Chairman Jerome Powell warned of more downside risks, he also said the central bank still had ammunition to support the US economy if needed while sections of the economy emerging gradually from lockdown also bolstered hopes of a recovery. As a result, US Treasury yields ended mixed: the two- and five-year yields dipped, the benchmark 10-year yield was largely flat at 0.65% and yields further out the curve rose on the prospect of increased long-duration supply.
- In Asia, local rates markets were mostly firmer on a total-return basis. Indonesia, India and the Philippines led gains on the back of lower domestic government bond yields as emerging-market risk sentiment improved. The Malaysian and Thai markets eked out modest gains as local short and mid-dated yields fell in tandem with policy rate cuts by Bank Negara Malaysia and Bank of Thailand respectively. The strength of the Indonesian rupiah and Thai baht further helped returns in these markets. Bucking the trend were China and Hong Kong, where higher government bond yields weighed on market returns.
- **Emerging Market** USD credit markets continued to rally as spreads tightened, driven by improving Chinese economic data, good liquidity conditions and better risk appetite that drove inflows into the asset class. April data in China, including exports, industrial production, fixed investments and retail sales, proved encouraging and suggested the domestic economy was poised for a recovery as virus containment measures were gradually lifted. This overshadowed fears of a second wave of infections.
- The improved sentiment helped the performance of **Asian high-yield** corporate bonds. Asian investment grade sovereign bonds also performed well. Conversely, Asian investment grade corporate bonds underperformed, amid an increasing number of new issues from this segment.

Figure 5. Bond Indices Performance in USD

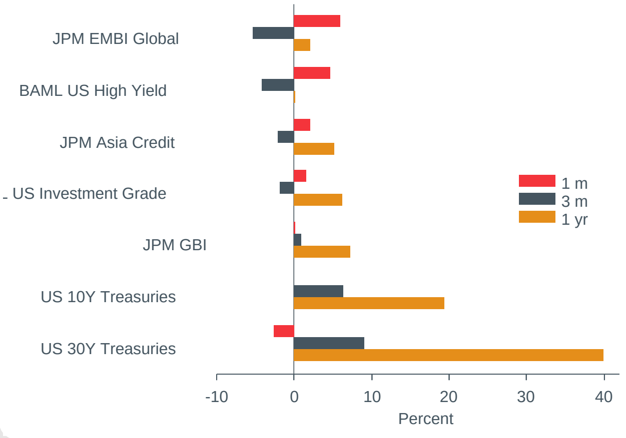

Figure 6. Key Bond Yields (%)

Source: Eastspring Investments. Chart data from Refinitiv Datastream as of as of 31 May 2020. For representative indices and acronym details please refer to notes in the appendix. For representative indices and acronym details please refer to notes in the appendix.

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Currencies

- The **US dollar index** (DXY) dropped 70bps in May as the risk on sentiment continued and the US saw the emergence of widespread social unrest, trimming year-to-date appreciation of the dollar to 2%. Cyclical currencies such as the Norwegian krone, the Swedish krona and the Australian dollar were among the top performers in the G10 space. The Japanese yen, a classic safe-haven at the height of the Covid crisis, depreciated 60bps against the US dollar as the new infections curve continued to flatten worldwide. The UK pound depreciated the most in the G10 space (-1.7% in May), caused by talk of the Bank of England dropping rates into negative territory, a slower economic reopening in the UK vis-à-vis the rest of Europe, and the slow progress on Brexit negotiations.
- Most **Emerging Markets'** currencies rallied sharply against the US dollar, reversing part of the depreciation seen since March. The Mexican peso had a stellar 7.5% appreciation against the dollar as it gained on mounting US-China tension at a time when its own trade relations with the US were on more solid ground, and despite an increase in new Covid-19 infections.
- Other **high-beta Emerging Market currencies** gained including the Russian ruble, up 6.0% on a higher oil price while the Columbian peso (+6.8%), and South Africa's rand appreciated by around 5%. Argentina remained an underperformer within the EM space, depreciating by 2.5% as the government continues to struggle to meet its debt payments.
- **Asian FX** underperformed rest of EM driven by an escalation of US-China trade tensions and a second wave of new infections as the economies opened. Korea's won fell 1.6% despite economic data starting to show signs of recovery, and China's renminbi was 1.0% higher, both affected by the increase in US-China tensions, with the renminbi/dollar again re-approaching all-time lows of 7.2. On the flip side, the Indonesian rupiah and the Thai baht appreciated by about 1.8% each, but still underperforming Latam currencies.

Figure 7. Currencies Performance vs USD

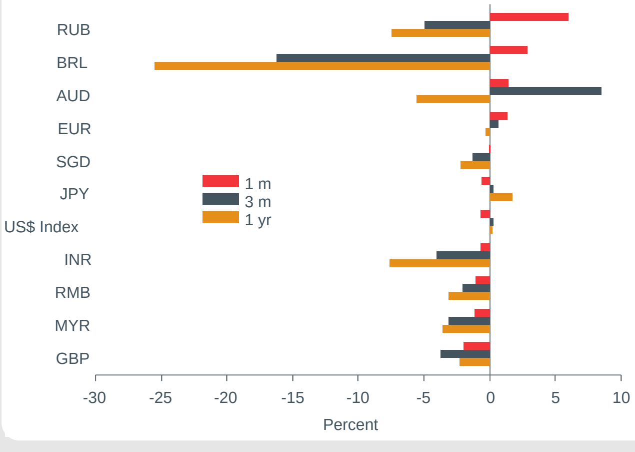
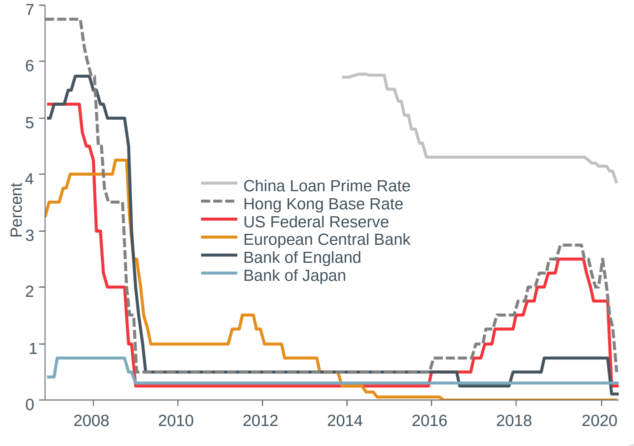


Figure 8. Central Banks Interest Rates



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Commodities

- **Crude oil** prices had a very strong month as economies moved to re-open and on unexpected news that Saudi Arabia had committed to deepening production cuts in June. A ramp up in China refinery production and a drop in US stockpiles also lent support to Brent (up 55%) and WTI (up 88%) respectively. However, the gains were ultimately capped by increasing US-China tensions.
- **Gold** hit fresh record peaks during May but gains were more muted than in recent months. Grim economic data and projections of higher inflation supported the gains but these were offset in the second half of the month as lockdown restrictions round the world began to ease.
- **Iron Ore** continued to defy the global economic slowdown and surged to eight-month highs as it continued to benefit from supply concerns in Brazil as the Covid pandemic continued to surge there, as well as on hopes of demand recovery from steel mills. This helped the **S&P Industrial Metals** index to end 3.2% higher.
- **Copper** prices inched higher as China's economy showed signs of accelerating again. **Lead** and **tin** prices recovered from their troughs somewhat and hit multi-week highs on an inventory drawdown outside of China, hinting at a potential supply deficit in the two metals this year.

Economics

- Minutes from the **US Fed's** meeting in April revealed a detailed discussion on various economic stimulus plans but it also rejected negative interest rates. Consumer confidence inched higher in May and New Home sales surprisingly ticked higher in April, but Housing Starts fell by 30%. Another 2.5m people filed for jobless claims taking the total number of jobs losses to 38m.
- **Europe** saw inflation fall to 0.3% yoy in April as the asset purchase programme had yet to hit the 'real' economy. Eurozone manu-facturing PMI was at 39.5 in May, up from April's reading but still showing contraction. The UK saw GDP slide 2% qoq in Q1 as well as a monthly contraction of 5.8% for March, pointing to a larger decline in Q2 GDP.
- **Chinese** industrial production returned to growth in April with a 3.9% rise yoy and the Industrial PMI reading came in at 50.7 versus 49.4 in April. Retail sales fell 7.5% yoy, more than the market was expecting and Beijing also said it would not give a GDP forecast for the full year given the economic uncertainties while actual Q1 GDP fell 6.8% yoy.
- Elsewhere, **Russia** saw GDP growth slow to 1.6% in Q1 from 2.1% in Q4 last year. India's RBI cut rates by 40bps and signaled further cuts ahead. **India** was one of 11 Emerging Market central banks to cut rates in May with the list including Turkey and South Africa that cut by 50bps, and Brazil, which cut by 75bps.

Figure 9. Commodities Performance in USD

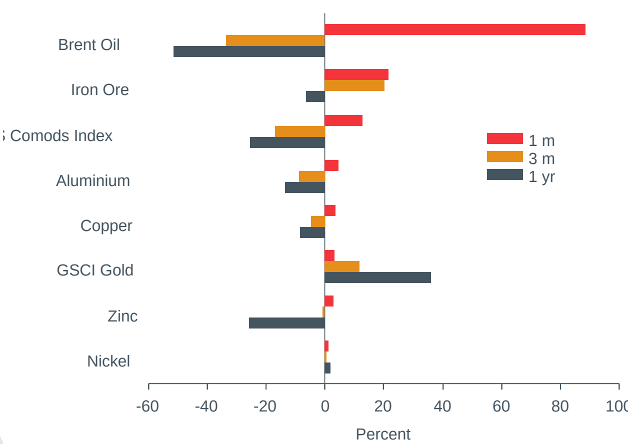
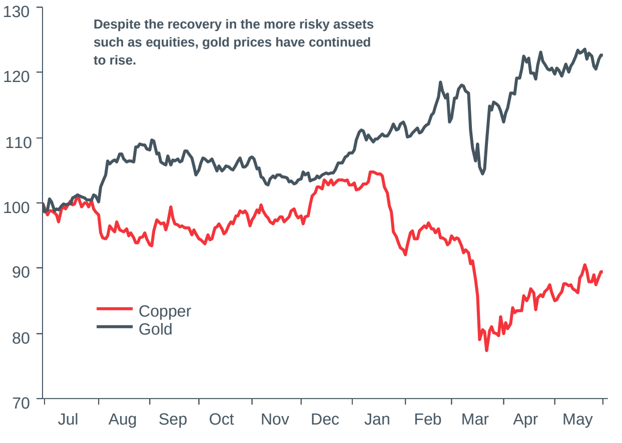


Figure 10: Commodity Prices, 2019-20



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of 31 May 2020.

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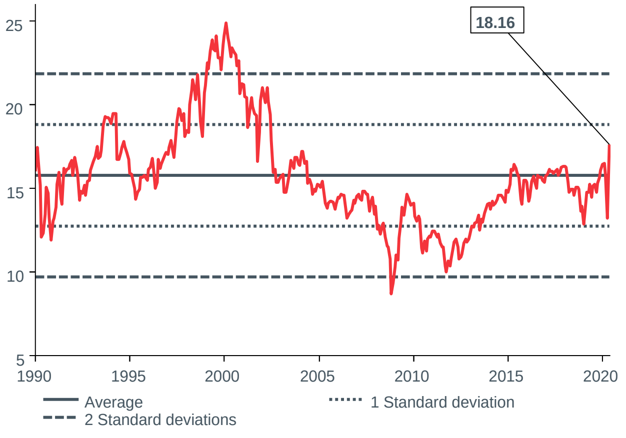
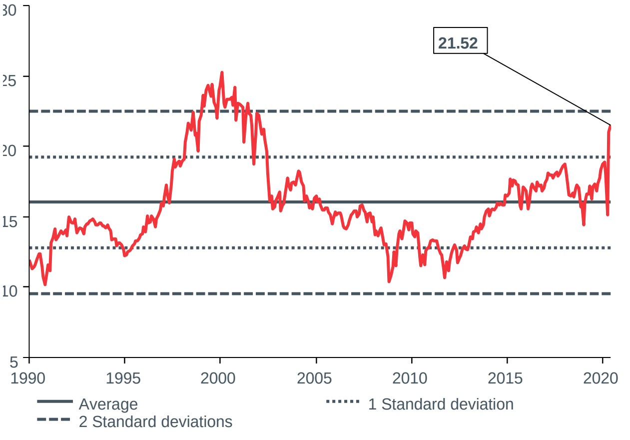
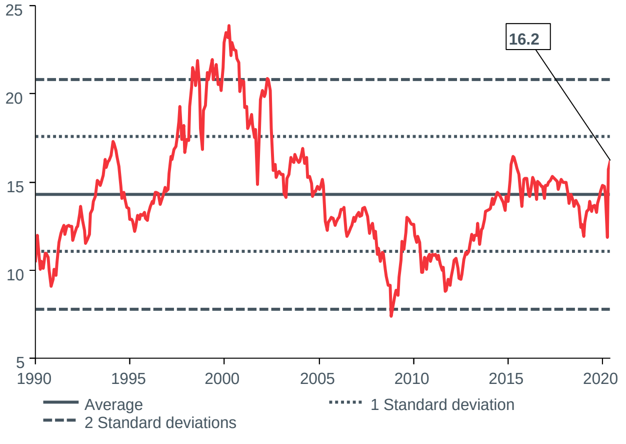
MSCI AC World 12M Forward PE



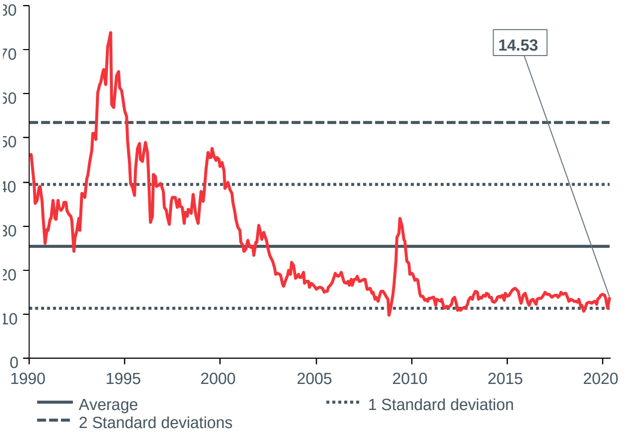
MSCI USA 12M Forward PE



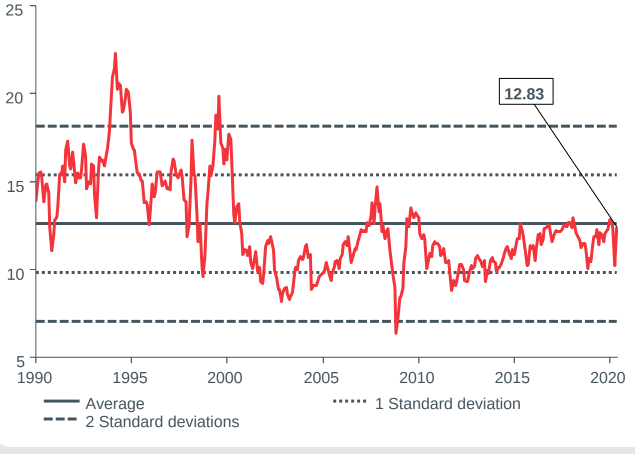
MSCI Europe 12M Forward PE



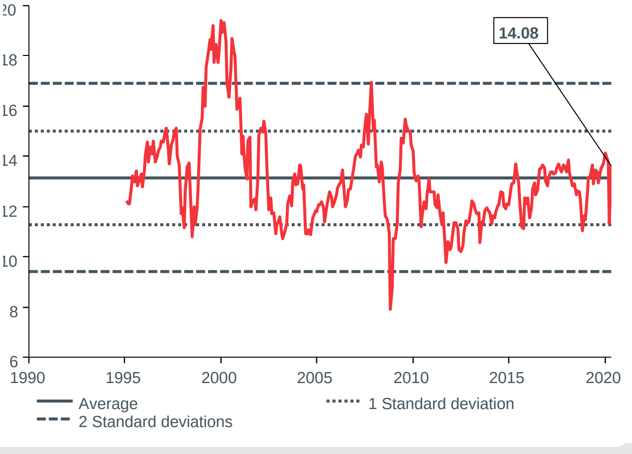
MSCI Japan 12m Forward PE



MSCI Emerging Markets 12M Forward PE



MSCI Asia Pac ex Japan 12M Forward PE



Source: Eastspring Investments. Chart data using IBES estimates from Refinitiv Datastream as of 31 May 2020.

MSCI monthly, quarterly and year-to-date data

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	May-20	Apr-20	Mar-20	QTD	Q1	YTD	2019	2018
World	4.4	10.8	-13.4	15.6	-21.3	-8.9	27.3	-8.9
Developed World	4.9	11.0	-13.2	16.4	-20.9	-8.0	28.4	-8.2
United States	5.2	13.2	-12.7	19.0	-19.6	-4.3	31.6	-4.5
Europe	4.7	6.1	-14.4	11.0	-24.2	-15.9	24.6	-14.3
Japan	5.9	5.4	-7.0	11.6	-16.6	-6.9	20.1	-12.6
Emerging Markets	0.8	9.2	-15.4	10.0	-23.6	-15.9	18.9	-14.2
Asia Pac Ex Japan	-0.3	9.8	-14.0	9.5	-20.7	-13.2	19.5	-13.7
Asia Ex Japan	-1.1	9.0	-12.0	7.7	-18.4	-12.1	18.5	-14.1
Latin America	6.5	6.3	-34.5	13.3	-45.6	-38.4	17.9	-6.2
Brazil	8.5	5.4	-38.2	14.4	-50.2	-43.0	26.7	-0.2
EMEA	3.8	11.0	-21.1	15.2	-33.9	-23.8	16.3	-15.5

	May-20	Apr-20	Mar-20	QTD	Q1	YTD	2019	2018
Australia	4.6	15.3	-25.1	20.6	-33.2	-19.5	23.1	-11.8
New Zealand	3.1	10.5	-11.2	13.9	-16.3	-4.7	38.8	-3.5
Hong Kong	-8.4	7.3	-12.2	-1.7	-17.3	-18.7	10.3	-7.8
China	-0.5	6.3	-6.6	5.8	-10.2	-5.0	23.7	-18.7
Korea	2.2	8.2	-11.5	10.6	-22.4	-14.2	13.1	-20.5
Taiwan	-2.5	14.1	-13.4	11.2	-19.0	-9.9	37.7	-8.2
Thailand	4.4	16.1	-17.4	21.3	-33.7	-19.6	9.8	-5.3
Malaysia	4.8	5.5	-10.2	10.6	-19.2	-10.6	-2.0	-6.0
Singapore	-3.2	8.4	-19.9	5.0	-28.2	-24.6	15.0	-9.4
Indonesia	3.3	12.2	-29.3	16.0	-39.4	-29.8	9.7	-8.7
India	-2.8	16.1	-25.1	12.9	-31.1	-22.2	7.6	-7.3
Philippines	1.6	9.0	-21.4	10.8	-32.0	-24.6	11.0	-16.1

	May-20	Apr-20	Mar-20	QTD	Q1	YTD	2019	2018
Mexico	6.5	4.3	-29.2	11.1	-35.4	-28.3	11.8	-15.3
Chile	-5.4	16.2	-17.8	9.9	-33.4	-26.7	-16.0	-18.9
Hungary	6.9	6.6	-26.5	14.0	-39.0	-30.5	19.4	-6.1
Poland	8.2	9.2	-19.9	18.1	-36.5	-25.0	-5.3	-12.5
Czech Republic	4.1	11.2	-27.5	15.8	-38.5	-28.8	6.6	-2.2
Russia	8.7	11.5	-23.3	21.2	-36.3	-22.8	52.7	0.5
Turkey	5.9	4.5	-19.0	10.7	-30.0	-22.6	11.7	-41.1
South Africa	2.0	13.2	-24.8	15.5	-40.3	-31.1	10.7	-24.3
Qatar	2.2	4.9	-10.8	7.2	-17.3	-11.3	-1.0	29.8
Saudi Arabia	0.1	10.6	-13.7	10.7	-23.1	-14.8	9.1	19.2
United Kingdom	1.1	5.1	-16.0	6.3	-28.8	-24.3	21.1	-14.1
Germany	8.9	9.8	-17.0	19.6	-27.0	-12.6	21.7	-21.6
France	5.1	4.4	-17.6	9.8	-27.5	-20.4	27.0	-11.9
Netherlands	7.3	8.7	-11.2	16.6	-20.6	-7.4	32.7	-12.8
Austria	1.7	10.6	-28.0	12.4	-38.2	-30.5	18.4	-23.2
Italy	5.9	1.9	-22.5	7.9	-29.2	-23.6	28.7	-17.0
Spain	4.3	1.5	-22.1	5.9	-29.7	-25.6	12.7	-15.7
Greece	4.7	9.0	-26.0	14.1	-45.1	-37.4	43.6	-36.7
Portugal	11.0	1.4	-11.0	12.5	-13.1	-2.2	25.2	-10.1
Switzerland	2.9	5.2	-4.2	8.2	-11.1	-3.8	33.6	-8.2

Source: Eastspring Investments. Chart data from Refinitiv Datastream as of 31 May 2020. Data and commentary prepared by Peter Bennett.

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