Markets defy weak economics to reach new highs

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October 2019

The World in five bullet points

- **Equity markets** rose for the second month in a row in October with stocks rallying from a weak start to end higher almost everywhere. The twin drivers of interest rate cuts around the world – or an easing of monetary policy where rates were already very low – and a further thawing in the US-Sino trade dispute combined to offset weaker economic data. For the first time since March, Emerging Markets outperformed Developed Markets with Taiwan and Brazil leading the gains. The US lagged Europe also for the second month running with Germany and France leading over an underperforming UK.
- One of the key drivers for the month was the decision by the **US Federal Reserve** to cut interest rates by another 25 basis points to 1.5%-1.75% but Chair Jerome Powell also signaled that it was to pause on further cuts pending clearer economic data. The decision came as third-quarter GDP figures for the US showed the country grew by just 1.9% with a notable drop in both business investment and consumer spending partly to blame.
- The US sparked condemnation at home and abroad after clearing the way for a **Turkish offensive in northern Syria** against its former Kurdish allies by pulling its troops out of the region. At the end of the month, and despite the withdraw, US forces found and killed the head of ISIS in the same area. But the potential for a White House media coup was overshadowed by the House of Representative's vote to make public hearings into alleged efforts by the President to pressure Ukraine to investigate his political opponents.
- UK Prime Minister Boris Johnson and the EU reached a **new deal on Brexit**. Among the changes both sides agreed to was a complicated customs and regulatory arrangement for Northern Ireland but the move so incensed MPs from the province that they immediately declared their intention to vote against the deal in the UK's parliament. The eventual parliamentary vote fizzled without passing and the government admitted it would miss its own 31st October deadline for leaving; instead a general election will be held in December.
- **The Month of the Protest:** In a year that has seen a surge in the number of street protests and general social unrest, October saw a spike in the number of people taking to the streets. Protesters in Ecuador, Lebanon, Chile and Bolivia, among others, took to the streets to protest fuel prices, tax rises and an increase in metro price tickets, among other causes, while more than a million took to the streets of London to protest against Brexit. In **Hong Kong**, ongoing protests are taking their toll on tourist numbers and investor confidence, leading to its stock market to notably underperform the rest of Asia (Fig 1).

Figure 1. Hong Kong underperforms in 2019

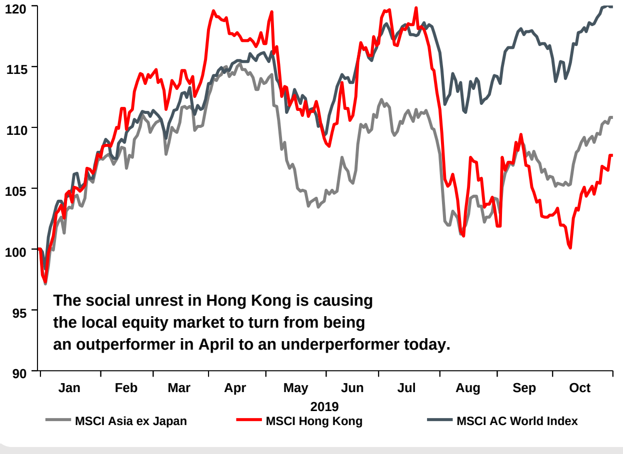
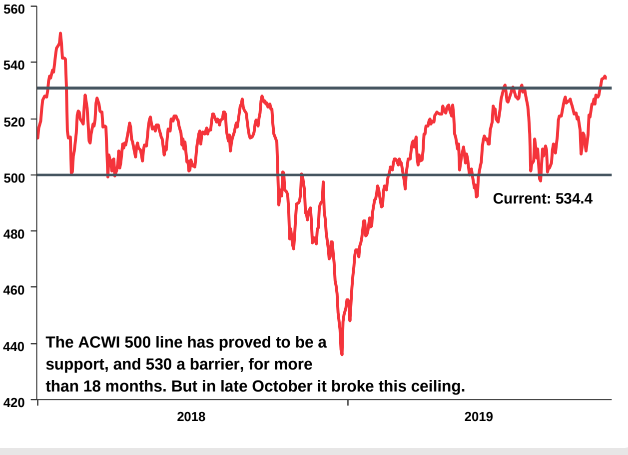


Figure 2. MSCI AC World Index



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of as of 31 October 2019.

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Equity Markets

- **Global** equity markets staged a comeback from a very weak start to the month and ended with the US finishing on the penultimate day of trading with a fresh record high. Investors reacted well to the round of central bank policy easing that saw interest rates around the world cut by 25-50bps or other monetary easing policies implemented. Solid corporate results particularly in the US supported gains as did "flash" PMI levels which pointed to a potential bottoming in manufacturing.
- **Europe** gained 3.2% to outperform the **US** (+2.2%) for the second month in a row as industrial heavyweights, especially in Germany, either confirmed outlooks or reported better-than-expected earnings. That led the MSCI **Germany** index to outperform with **France** only just behind. The **UK** underperformed as a new deal with the EU failed to pass its parliament and a new general election was called.
- In **Asia**, a surge in **Taiwan** market bellwether TSMC, as well as other iPhone supply chain stocks, pushed the MSCI Taiwan index to advance 8% with the index now up more than 26% for the year to date. **Korea** also benefitted from the recovering tech sector with a 4.6% gain, although much of this was down to the strong won but still the second month running the country has out-performed the region. Singapore, heavily geared into global trade saw a 5.4% advance. **Hong Kong** saw a recovery from last month's falls to post a 4.7% gain despite indications the territory would fall into recession this year and an interest rate cut on the final day of the month. **China** posted a 4.0% with returns here more subdued as higher-than-expected inflation figures placed a question mark over Beijing's response to the slowing economy.
- Elsewhere in Asia, the non-tech/non-trading countries underperformed with **Indonesia** gaining 2.8%, **Malaysia** just 1.1% but the Philippines gained an impressive 4.7%. A notable underperforming country was **Thailand** (-1.5%) where weak macro economic data and a global 'risk-on' meant safe haven markets such as Thailand saw some underperformance. Finally, India was inline with the rest of Asia with a 4.3% gain.
- Around the world, other notable index moves included **Australia** which underperformed to return just 1.7% as the banking sector there saw some weakness. **Japan** had a stellar month returning 4.9% to end close to one-year highs on a weaker yen, improved fundamentals for tech companies and hopes of a trade deal. Back in EM, **Chile** was the big loser of the month, falling 7% as social unrest gripped the country and **Turkey** continued its volatile year with an 8% dip.

Figure 3. Regional Equity Indices

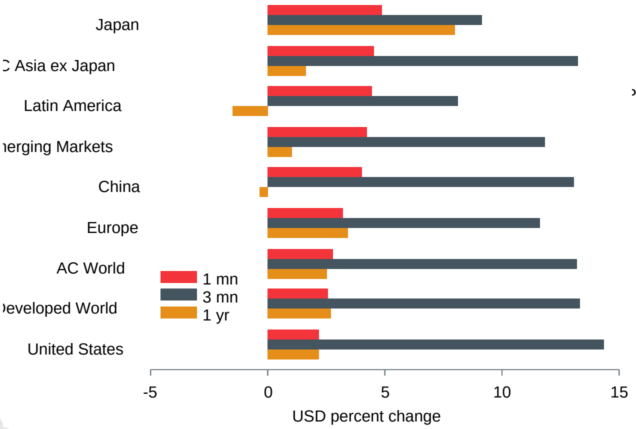
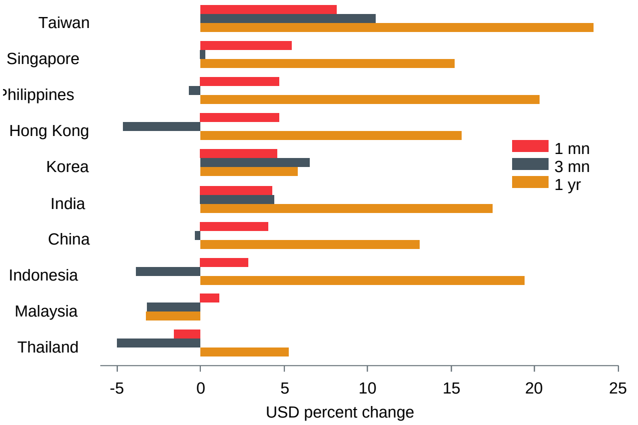


Figure 4. Asia Equity Indices



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of 31 October 2019. 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. Quoted returns are MSCI, dollar denominated total returns.

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Fixed Income

- **The global bond markets** saw a mixed performance across the US Treasury (UST) yield curve, with Fed policy action and unresolved trade issues remaining at the forefront of investors' minds. The two-year and five-year UST yields fell by 10bps and 2bps respectively, with both ending at 1.5%. Yields of shorter-dated Treasury bills fell by much more. Conversely, the benchmark 10-year UST yield edged 3bps higher to 1.7%, with yields further out the curve rising by more.
- Deteriorating macro conditions continued to support more accommodative monetary policy, with the two-year UST yield moving lower in step with such expectations. The Fed's month-end interest rate cut – its third this year – was widely expected but Chair Jerome Powell's comment that monetary policy was "in a good place" doused hopes of further easing in the near term.
- Meanwhile, longer-dated maturities rose on the back of an apparent easing in trade tensions that led to improved risk appetite. A temporary truce saw Beijing agreeing to buy more US agricultural products and Washington suspending planned tariff hikes on US$250 billion-worth of Chinese goods. The White House also expressed hopes a partial deal would soon be finalised. Nevertheless, this proved short-lived as trade worries resurfaced at the month-end after Chinese officials reportedly voiced doubts about whether a comprehensive long-term pact with Washington could be reached. Longer-dated UST yields subsequently retraced some of their earlier climbs.
- The easing cycle also continued in most emerging markets in October. In Asia, this helped high-yielding local rates markets such as Indonesia and India outperform other regional counterparts. Bank Indonesia lowered rates for a fourth straight month, bringing the 7-day reverse repurchase rate to 5%, in a pre-emptive move to spur lending and bolster domestic growth. The Reserve Bank of India also cut its key policy rate, to its lowest level in nearly a decade, and added it would keep the accommodative stance for as long as necessary. Indonesian and Indian local rates fell in response.
- Korea lowered policy rates but the domestic bond market underperformed as yields moved higher. In other emerging markets, Brazil, Russia and Turkey all cut rates in response to slower growth, with local bond yields falling in tandem.
- Dollar-denominated credit markets delivered positive returns over the month. Given the optimism over trade talks, credit spreads tightened helping compensate for the mixed performance in US risk-free rates. This led to Asian US dollar high-yield credits to outperform investment-grade credits.

Figure 5. Bond Indices Performance in USD

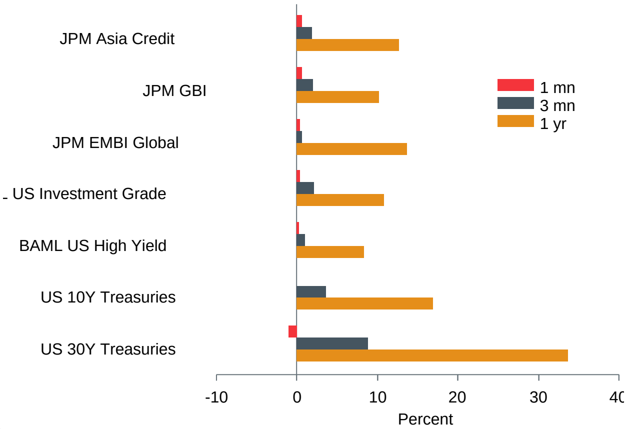
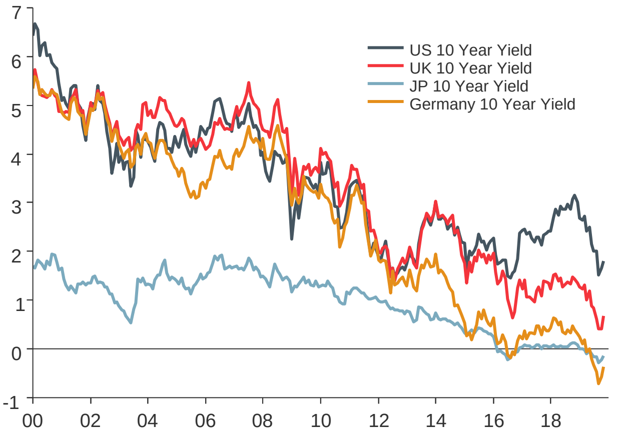


Figure 6. Key Bond Yields (%)



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of as of 31 October 2019. 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) declined around 2% over the month after a strong rally in September. Risk appetite improved which kept the US dollar under pressure and it weakened against all G10 currencies except the Norwegian krone. The UK pound was the best performer once again, gaining more than 5% over the course of the month as concerns over a no deal Brexit diminished after the UK Parliament agreed to Boris Johnson's new Brexit deal in principle but also forced the prime minister to ask for another extension from the EU. A general election was called for early December diminishing the changes of a no deal further and providing further support.
- Meanwhile, the antipodean currencies, the New Zealand dollar and the Australian dollar, as well as the euro, were all up more than 2% against the US dollar. This month was the last European Central Bank (ECB) meeting for its chief Mario Draghi after an eight-year term and while his final meeting was a non event, he once again emphasized the need for expansionary fiscal policy.
- Emerging markets' currencies added to the gains made in September. The Argentine peso was the main outperformer, gaining nearly 7% against the US dollar after Alberto Fernandez was elected the new president. The hope is that he follows a pragmatic and reformist agenda to bring the country out of recession and its debt crisis. The Brazilian real gained more than 3% against after struggling over the past few months while the Turkish lira fell at first on concerns over White House comments regarding the country's intervention in Syria but it regained the losses to end the month almost flat.
- In Asia, the Korean won was the outperformer, up just under 3% against the dollar. The Philippine peso saw similar gains and indeed all Asian currencies were stronger against the dollar except the Japanese yen which was flat. This was a contributing factor to Japan's equity market outperformance.
- Meanwhile, the Chinese yuan was up nearly 2%. Newsflow on the US-Sino trade deal was positive with both countries seemingly close to signing Phase 1 of a deal, which has eased market concerns over the escalation of the trade war.

Figure 7. Currencies Performance vs USD

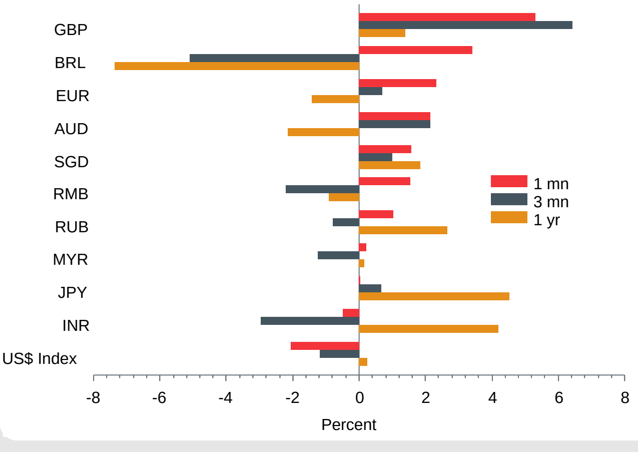
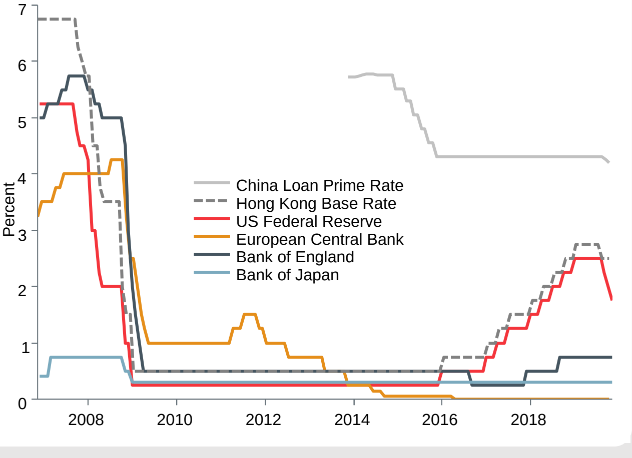


Figure 8. Central Banks Interest Rates



Source: Eastspring Investments. Chart data from Thomson Reuters Data stream as of 31 October 2019. 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.

Commodities

- **Oil** prices edged higher over the month but prices were volatile as traders juggled with the price drivers. On the supportive side, progress in trade talks, OPEC cuts and both geopolitical and domestic unrest in oil producing countries drove prices higher and were pitched against the negative drivers of weak economic data especially from China, a build in US inventories and a miss by Russia on its production cut targets. By month end, the bulls just about ran out on top with Brent down 1% and WTI 1% higher.
- **Copper** prices rallied sharply on the back of worsening strikes in Chilean mines and escalating national protests centred on wealth inequality in the country. **Gold** prices also rose into the end of the month as weak US economic data fuelled expectations for another interest rate cut. It held at just above the psychological $1,500 per ounce level by month end.
- **Nickel** prices fell slightly from September's highs as Indonesia began to restrict ore exports ahead of a complete ban scheduled for January. **Palladium** also hit a fresh new record peak as supply shortages continued.
- **Iron ore** fell over the month on concerns over China's economic health as well as data showing stockpiles at Chinese ports hitting six-month highs. For three months, iron ore is down almost 35%.

Economics

- **The US** saw more conflicting evidence of a slowdown with housing sales falling but house prices remaining robust. Orders for durable goods fell in September but this was largely blamed on the strike at General Motors and Boeing's problems. The ISM Manufacturing figure fell below 50 for the first time, indicating contraction, while Q3 GDP rose 1.9%, above expectations but below Q2. In response the Fed lowered rates again as expected but signalled it would now pause in its cutting cycle.
- **Europe's** ECB kept rates on hold again but with European PMIs surprising to the downside, most observers now expect another round of monetary easing.
- **China's** Q3 GDP growth slowed to 6.0% from 6.2% in Q2 and versus the 6.1% the market was expecting. It was the slowest growth figure since 1992. But October's PMI reading China showed a surprise expansion to 51.7. **Hong Kong** signaled it was likely to fall into recession by year end as the social unrest cut into economic growth.
- **Turkey** cut interest rates by 250bps, well above expectations, as the lira stabilised and the economy showed early signs of growth. Central Banks in Russia, Indonesia and Chile also cut rates by 25 or 50 bps joining the group of central banks that have eased in the past two months (Figure 8).

Figure 9: Commodity Prices, year to date

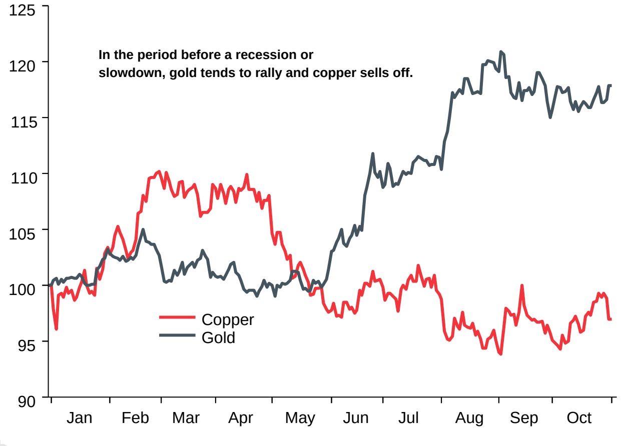
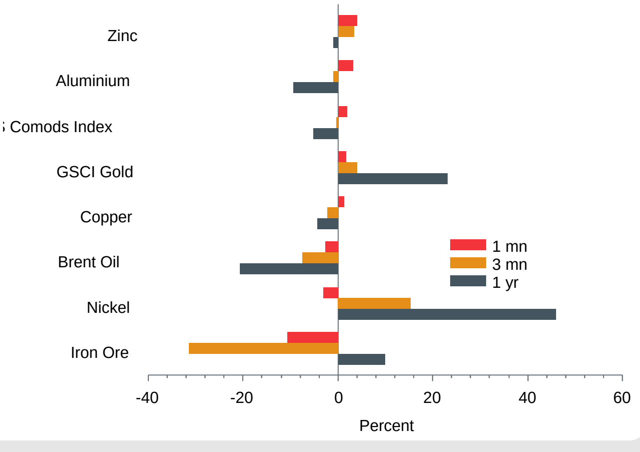


Figure 10. Commodities Performance in USD



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of 31 October 2019.

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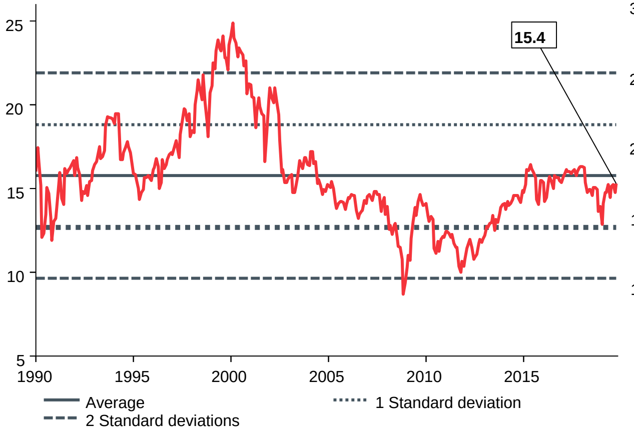
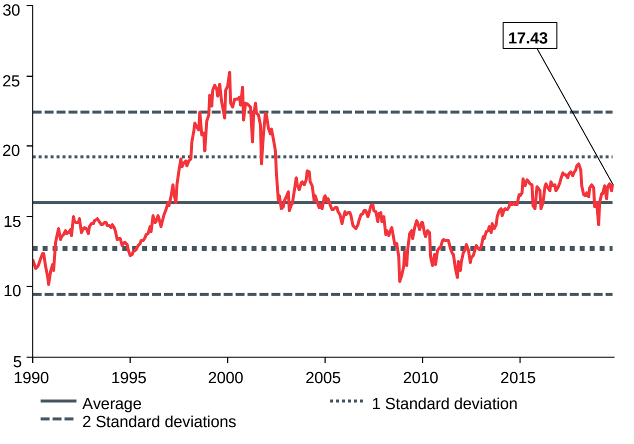
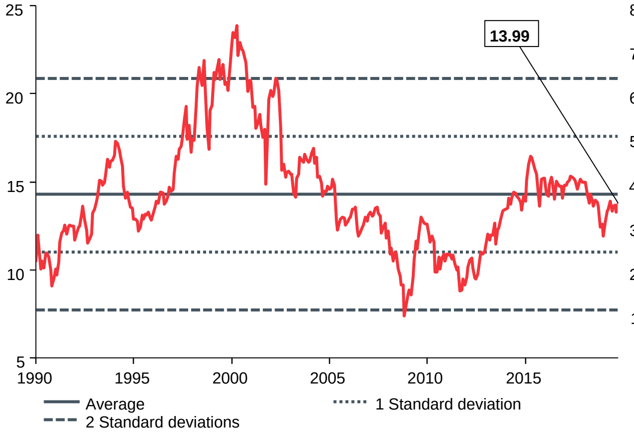
MSCI AC World 12M Forward PE



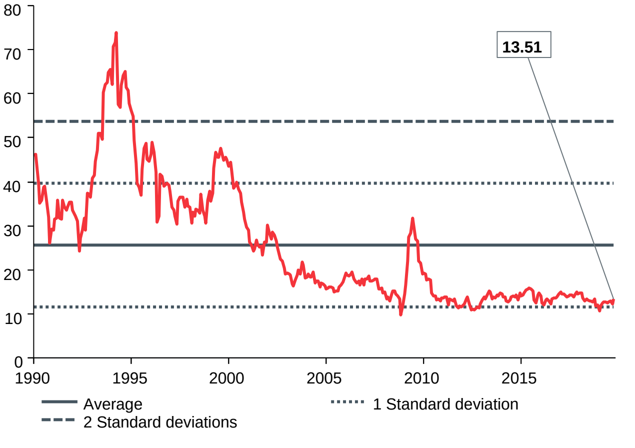
MSCI USA 12M Forward PE



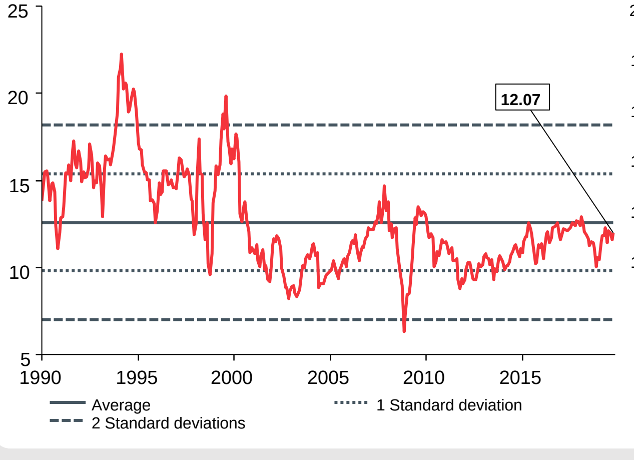
MSCI Europe 12M Forward PE



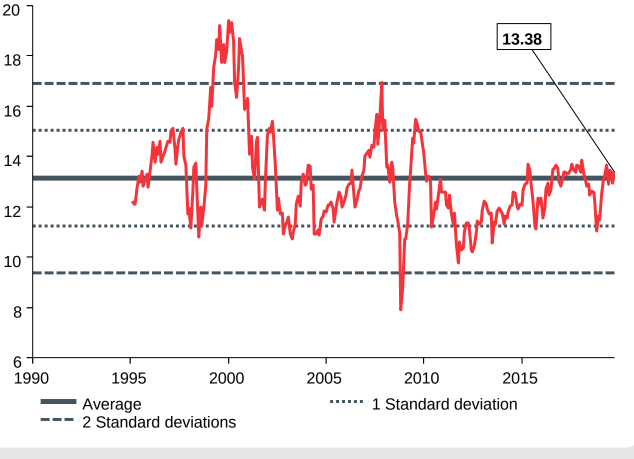
MSCI Japan 12m Forward PE



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 October 2019.

MSCI monthly, quarterly and year-to-date data

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	Oct-19	Sep-19	Aug-19	Q3 19	Q2 19	Q1 19	YTD	2018
World	2.8	2.2	-2.3	0.1	3.8	12.3	19.9	-8.9
Developed World	2.6	2.2	-2.0	0.7	4.2	12.6	21.2	-8.2
United States	2.2	1.8	-1.7	1.6	4.3	13.9	23.3	-4.5
Europe	3.2	2.7	-2.5	-1.8	4.9	11.0	18.1	-14.3
Japan	4.9	4.2	-1.0	3.3	1.0	6.8	16.9	-12.6
Emerging Markets	4.2	1.9	-4.8	-4.1	0.7	10.0	10.7	-14.2
Asia Pac Ex Japan	4.0	1.8	-4.4	-3.9	0.8	11.5	12.4	-13.7
Asia Ex Japan	4.6	1.7	-4.4	-4.4	-0.6	11.4	10.8	-14.1
Latin America	4.5	2.6	-8.1	-5.6	4.6	7.9	11.3	-6.2
Brazil	6.4	2.5	-9.2	-4.5	7.2	8.2	17.8	-0.2
EMEA	2.8	1.0	-7.3	-6.8	7.4	5.6	8.7	-15.5

	Oct-19	Sep-19	Aug-19	Q3 19	Q2 19	Q1 19	YTD	2018
Australia	1.7	2.4	-4.3	-1.4	7.4	11.4	20.1	-11.8
New Zealand	2.0	0.3	-6.8	-2.8	4.0	16.9	20.5	-3.5
Hong Kong	4.7	-0.7	-8.3	-11.9	1.0	15.6	7.7	-7.8
China	4.0	-0.0	-4.2	-4.7	-3.9	17.7	12.1	-18.7
Korea	4.6	7.2	-5.0	-4.5	-0.9	5.0	4.0	-20.5
Taiwan	8.1	4.3	-2.1	5.9	1.1	9.0	26.2	-8.2
Thailand	-1.5	-1.0	-2.5	-5.9	9.4	7.5	9.0	-5.3
Malaysia	1.1	-0.6	-3.7	-6.3	1.2	0.3	-3.8	-6.0
Singapore	5.4	1.2	-6.0	-5.8	7.0	6.2	12.9	-9.4
Indonesia	2.8	-2.9	-3.7	-5.2	3.7	4.3	5.4	-8.7
India	4.3	3.1	-2.9	-5.2	0.5	7.2	6.6	-7.3
Philippines	4.7	-2.0	-3.3	-4.6	4.6	8.0	13.0	-16.1

	Oct-19	Sep-19	Aug-19	Q3 19	Q2 19	Q1 19	YTD	2018
Mexico	3.5	2.6	-0.4	-1.6	1.3	5.6	8.9	-15.3
Chile	-7.0	4.3	-6.4	-7.3	-4.9	4.4	-14.4	-18.9
Hungary	10.0	0.9	-4.9	-3.9	-4.1	6.0	7.5	-6.1
Poland	6.0	1.0	-8.7	-11.7	3.6	-0.6	-3.6	-12.5
Czech Republic	3.3	-2.7	-5.3	-9.5	3.9	3.8	0.8	-2.2
Russia	8.7	3.3	-4.7	-0.9	17.3	12.2	41.8	0.5
Turkey	-8.3	12.3	-10.7	11.7	3.1	-3.0	2.5	-41.1
South Africa	3.2	-1.2	-8.9	-12.4	6.8	4.6	0.9	-24.3
Qatar	-1.9	0.7	-2.0	-0.2	0.6	-3.5	-5.0	29.8
Saudi Arabia	-4.3	0.4	-8.8	-9.3	1.4	14.9	1.1	19.2
United Kingdom	2.8	4.2	-4.7	-2.5	0.9	11.9	13.2	-14.1
Germany	5.9	2.5	-3.0	-4.0	7.8	7.0	17.3	-21.6
France	3.6	2.5	-1.7	-1.6	7.3	10.8	21.2	-11.9
Netherlands	1.2	2.6	-1.0	2.5	6.1	13.6	25.0	-12.8
Austria	6.6	2.4	-3.6	-3.0	3.1	8.6	15.7	-23.2
Italy	4.6	2.9	-1.4	0.1	3.6	14.7	24.5	-17.0
Spain	2.4	4.1	-3.5	-3.8	2.9	7.1	8.6	-15.7
Greece	7.8	2.1	-5.3	-3.0	16.4	12.8	37.3	-36.7
Portugal	4.6	4.1	-1.7	1.8	2.6	10.2	20.5	-10.1
Switzerland	1.8	0.7	0.3	0.3	9.0	13.5	26.4	-8.2

Source: Eastspring Investments. Chart data from Refinitiv Datastream as of 31 October 2019. Data and commentary prepared by Peter Bennett.

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