Equity markets end the decade on record highs

December 2019

The World in five bullet points

- The US signed off on **Phase I of a trade deal** with China and cancelled tariffs on $160bn of Chinese goods due to take effect on 15 December. The US also left open the door to a reduction in existing tariffs if China purchases more US farm products and, while details of the deal were hard to come by, the agreement in principle lifted a cloud that had been hanging over the global economy all year. The China deal also came just days after the USMCA, the replacement of the NAFTA accord, was finalised between the US, Canada and Mexico.
- The ruling Conservative Party **won the UK election** by a wide margin, giving Prime Minister Johnson a large majority in parliament, and almost guaranteeing the UK will leave the EU on 31 January, albeit with an 23-month transitory period. Clarity on Brexit gave an immediate boost to UK equities and the pound but both saw gains capped on comments by PM Johnson within days of his victory that once again raised the spectre of a no-deal exit (see Equities and Currency sections below).
- The US-China trade deal and UK election removed two of the geopolitical risks that had weighed on markets for almost two years, and immediately released a **"risk-on" global equity rally**. The UK and the rest of Europe benefitted the most, with eurozone supported further from comments from new ECB chief Christine Lagarde who hinted that she may abandon the ECB's long-standing commitment to low interest rates, and introduce a vote on interest rate policy to mirror the dual mandate of the US Federal Reserve.
- **President Trump** became the third president in US history to be impeached by the House of Representatives. The House passed two charges, one covering abuse of power, the second on obstruction of Congress with both votes following party lines. Although a Senate trial has yet to be arranged, it is highly unlikely the Senate will pass the impeachment given its Republican majority with many commentators instead focusing on whether the impeachment would damage the President's re-election chances come November.
- As the month closed, investors began to reflect on what was a bumper year for equities. At the start of the year, weak economic data, trade headwinds, the threat of rising interest rates, and worries over Brexit pointed to an uncertain year ahead but instead the markets had one of their best years since the GFC. There were two catalysts for the US-led rally: first the tax breaks in the US passed last December that allowed for extensive **share buyback** programmes in the US; and second, the **"Powell Pivot"** reflecting the US Fed's decision to halt interest rate rises and instead cut rates. With other central banks around the world following suit, and the unwinding of many of the uncertainties, equity markets around the world rallied to multi-year or all-time highs.

Figure 1. The many records of the S&P 500

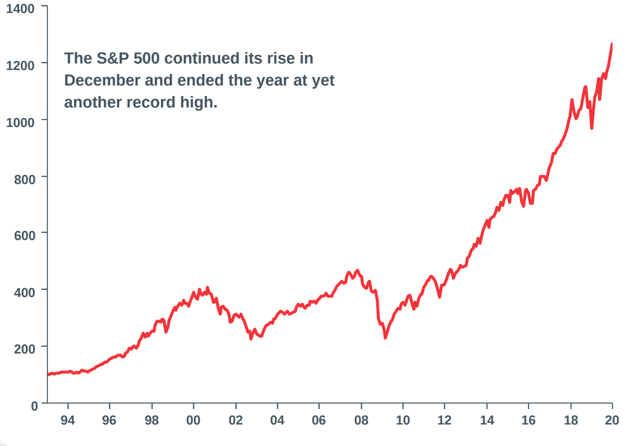
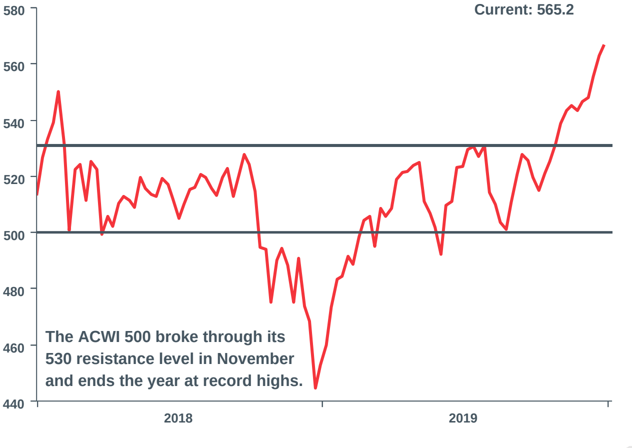


Figure 2. MSCI AC World Index



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

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Equity Markets

- **Global equity markets** ended the year with solid monthly gains almost everywhere with Emerging Markets outperforming Developed Markets by some distance. The catalyst for the rally was a signal the US and China were close to signing a trade deal, although details were largely unknown by month end. Meanwhile, the US dollar came under pressure as investors wagered the US economic outperformance was peaking, helping Emerging Market currencies and equities.
- The **MSCI AC World** index rose 3.6% with the US 2.9% higher, Europe (ex UK) 3.9% better, and the UK outperforming and adding 5.2% after the re-election of Boris Johnson as prime minister removed a Brexit hurdle. Emerging Markets outperformed adding 7.5%, led by Latin America that rose 10.4%, while Emerging Asia gained 7.2%. EMEA also performed well to gain 7.1% as South Africa grew 9.7% after avoiding a credit downgrade by a ratings agency.
- **Latin America's** outperformance was led by its largest market Brazil that saw a 12.5% rise although the region was aided by a 10.9% bounce in **Chile** after the government there promised reform in response to growing unrest. Latam currencies including the peso made a notable comeback over the month too, aiding equity returns.
- Emerging Asia saw **Korea** outperform to gain 10.4%, almost completely offsetting losses in the year to the end of November. **Taiwan** retained its momentum to add another 7.5%, with markets here once again led higher by chipmakers and stocks in the iPhone component chain. MSCI China added 8.3% as a swath of economic data suggested the recent slowdown had at least bottomed, and on hopes the Phase I trade deal with the US would soon be signed. **Hong Kong** once again underperformed however with street protests showing no signs of abating: the MSCI index here increased just 4.0%.
- Elsewhere, **South East Asia** underperformed with **Thailand** again bringing up the rear and adding just 0.9% as the economic slowdown there shows no sign of abating. **Indonesia** was a notable exception and added 7.1% as its central bank kept rates on hold.
- Elsewhere, **Australia** underperformed and added just 1.5% while **New Zealand** rose another 5.2%. For the year, New Zealand proved to be Asia's best performing market, up 39%, and third behind Russia (+53%) and Greece (44%) globally. Other notable performances in 2019 included Taiwan (+38%), the US (+32%), Japan (+20%) and Brazil (+27%) while eurozone stocks added 25%, outperforming the UK (+21%). Undperformers included India (+7.6%), Thailand (+9.8%) and Hong Kong (+10%). See page 7 for a complete table of performance returns in Q4 and 2019.

Figure 3. Regional Equity Indices

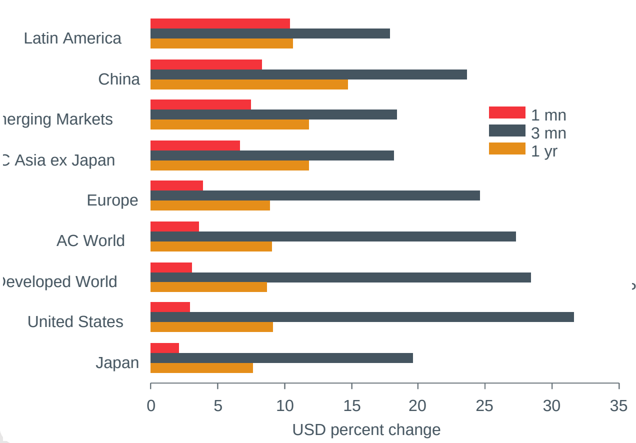
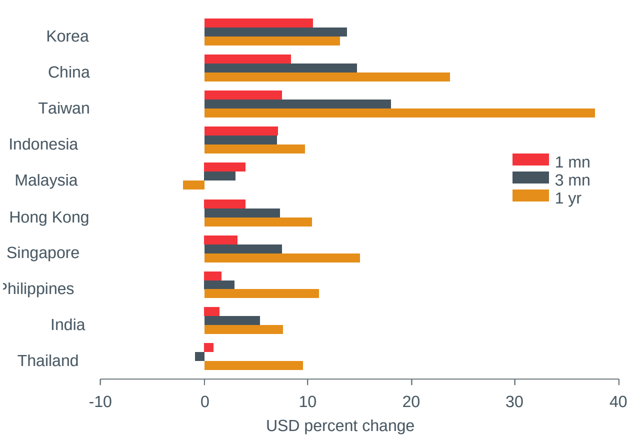


Figure 4. Asia Equity Indices



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

- In the risk-on environment, global government bond yields were mixed in December. Doubts over a China-US deal had pushed core yields lower at first. But rates reversed course after the rhetoric between Beijing and Washington subsided and both sides pushed ahead with talks that lifted hopes of an imminent Phase I deal. The Federal Reserve's (Fed's) decision to keep policy rates unchanged amid steady economic growth, as well as signals for a pause in the rate-cut cycle in 2020 provided further impetus for higher US yields.
- The two-year US Treasury (UST) yield ended 4 bps lower at 1.6% while the five-year and 10-year UST yields rose 7 bps to 1.7% and 14 bps to 1.9%. In Europe, German bund and UK gilt yields also ended mostly higher after the ruling Conservative Party's decisive win in the parliamentary elections gave Prime Minister Boris Johnson the ability to deliver on his Brexit deal.
- In Emerging Markets, local-currency bonds were more resilient, with modest returns bolstered by generally lower bond yields and broad USD weakness. In Emerging Asia, several central banks, including Indonesia, India and the Philippines paused in cutting rates in tandem with the Fed although the policy environment remained accommodative. The People's Bank of China (PBOC) proved an exception by trimming its 14-day reverse repo rate, following a cut in its 7-day rate in the prior month. Analysts expected further easing from the PBOC in 2020. Outside of Asia, policy rate cuts continued apace, with Brazil, Mexico, Russia and Turkey among those that took action.
- December's performance capped a decent year for global government bonds, where yields generally fell as trade tensions persisted, political risks remained elevated and economic growth slowed, which compelled central banks led by the Fed to abandon policy normalisation and start easing. The 10-year UST yield ended 77 bps lower over the year.
- Despite higher US risk-free rates, emerging-market USD-denominated credits performed well in December, helped partly by tighter spreads, given the improved risk sentiment on hopes that a trade deal would soon be signed. In Asia, high-yield credits outperformed investment-grade bonds in aggregate. Notable outperformance was seen in high-yield sovereigns, where spreads narrowed substantially.
- Over the year, emerging-market USD credits posted healthy returns on the back of lower US rates and tighter spreads. In Asia, primary market activity remained robust, although liquidity stresses and corporate governance issues weighed on some Asian corporates.

Figure 5. Bond Indices Performance in USD

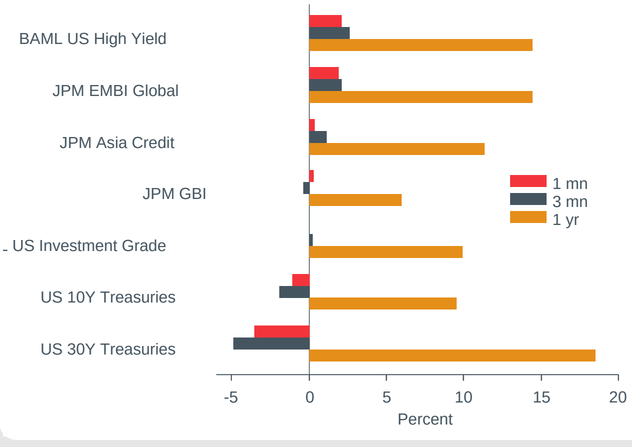
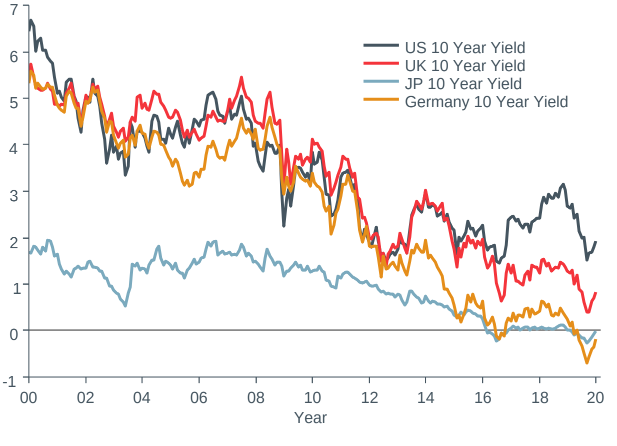


Figure 6. Key Bond Yields (%)



Source: Eastspring Investments. Chart data from Refinitiv Datastream as of as of 31 December 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) saw a modest decline of -0.4% in December, after a strong November. News flow was generally supportive of risk-on sentiment, driving flows away from safe haven assets. This meant US duration sold off, the US dollar depreciated, and equities rallied especially those in Emerging Markets that tend to benefit from a weaker US dollar.
- Among the **G10 currencies**, the New Zealand dollar and Norwegian krone rallied the most against the dollar, both up by nearly 3% each. Positive news also meant that investors stayed away from the Japanese yen, leaving the yen largely flat against the dollar in December.
- The **UK pound** had an interesting month after Boris Johnson won the general election with a resounding victory. At its peak, the pound had strengthened 3.1% against the dollar, as investors were optimistic that the Brexit uncertainties would soon be out of the way and that Johnson's deal with the EU would be passed by the UK parliament before the end of January. However, within days of his election victory, PM Johnson insisted he would deliver a Brexit with or without a deal, leading to the currency losing most of its post election gains.
- Most **emerging markets' currencies** strengthened amid the US dollar sell-off during the month. The Chilean peso was the main outperformer, gaining nearly 8% against the US dollar after the central bank intervened to arrest the sharp depreciation. Other Latin American currencies benefited from the rally. The Brazilian real, which has been under pressure throughout the year, appreciated by over 3% during the month. The Turkish lira was the only major emerging market currency to weaken against the US dollar, reflecting geopolitical tensions, despite central bank intervention.
- **In Asia,** the Korean won swung higher, reversing losses in November as US and China signed a phase one deal. Other trade-exposed currencies including Taiwanese dollar and Indonesian rupiah also strengthened. The Chinese yuan rallied 30bps, in line with the depreciation of the US dollar.

Figure 7. Currencies Performance vs USD

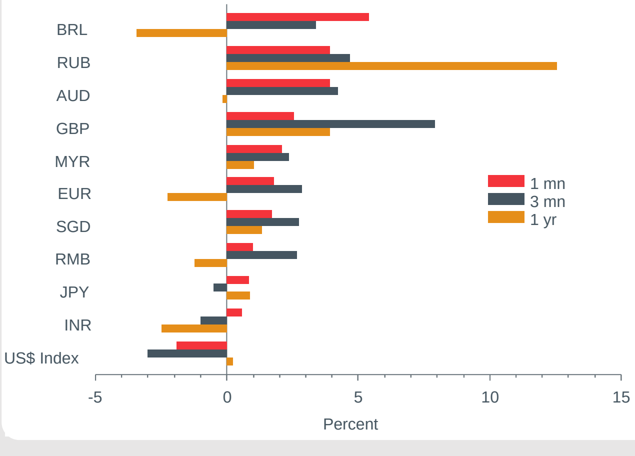
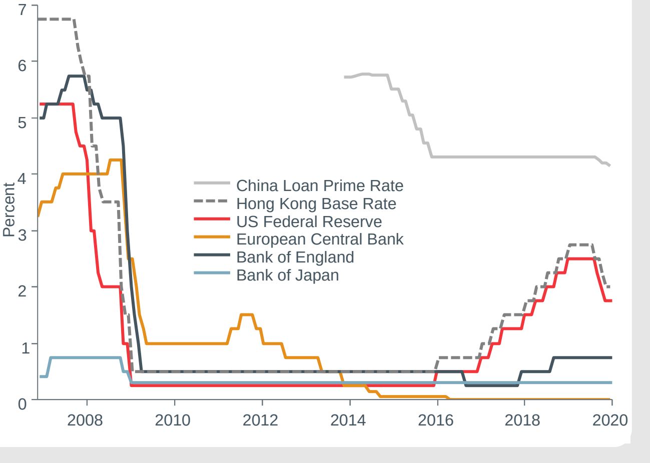


Figure 8. Central Banks Interest Rates



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.

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Commodities

- **Oil** hit the highest level since September late in the month on lower US crude inventories and the trade deal hopes. Oil rallied around 25% over the year supported by supply cuts from OPEC and Russia and a more robust global economic performance than expected despite some weak industrial indicators. Traders also pointed to the lack of volatility in crude prices during 2019 as an indication that the OPEC+ supply deal was working.
- **Gold** prices stopped a three-month rot in the final week of the month to record a first gain in almost three months as traders waited for details of the US-Sino trade deal to take shape. Copper also rose in response to signs of increased construction activity in China as imports of copper concentrate hit record highs in November.
- **Palladium** reached fresh new all-time highs after flash flooding in South Africa caused power outages and mine shutdowns. The metal, used in auto manufacturing, is now closing in on $2,000 per ounce. **Silver** prices also bounced back from recent lows.
- **Iron ore** prices rose as several steel mills in China resumed re-stocking post the steel-making city of Tangshan's decision to lift anti-pollution restrictions. The month capped a stellar year for iron-ore prices that defied the threat of an economic slowdown with any slowdown in demand offset by supply shortages from Brazil.

Economics

- The **US** NAHB Housing Market index and Housing Starts data rose in November with personal spending following suit. Industrial Production rose by 1.1% and while this was mostly down to General Motors workers returning from strike action, these and other economic data, pointed to continuing growth for the US economy into 2020.
- **Europe's PMI** were mixed for December with Manufacturing PMI slipping from the previous month but Services expanding marginally. German business morale rose more than expected in December with the Ifo business climate index hit 96.3, a six-month high.
- **Japan** saw industrial output slip in November and witnessed a dip in retail sales, increasing the likelihood of a contraction in GDP for Q4. But against this, Q3 GDP surprised on the upside with 1.8% growth and a business outlook survey also surprised positively.
- **China's** exports in November shrank for the fourth month in a row but imports rose, signaling Beijing's stimulus programmes may be stoking demand. Retail sales growth also accelerated to its fastest pace since June and Industrial Production also picked up.
- **Turkey** cut its key policy rate by 200bps to 12%, slightly above market expectations and hinted that more may be on the table. **Russia** also cut its rates by 25bps to 6.25% as expected, and Mexico also cut rates by the same amount, the fourth such cut this year.

Figure 9. Commodities Performance in USD

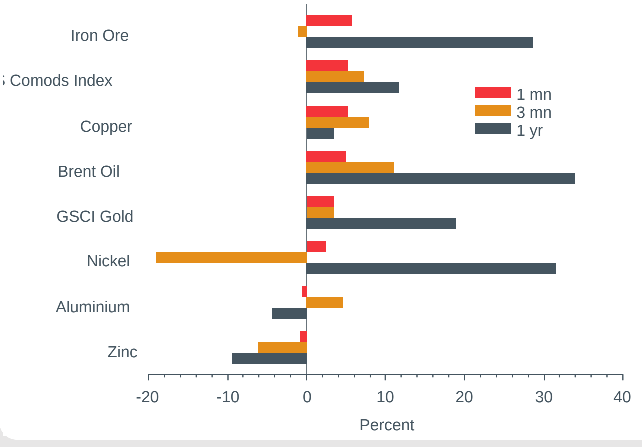
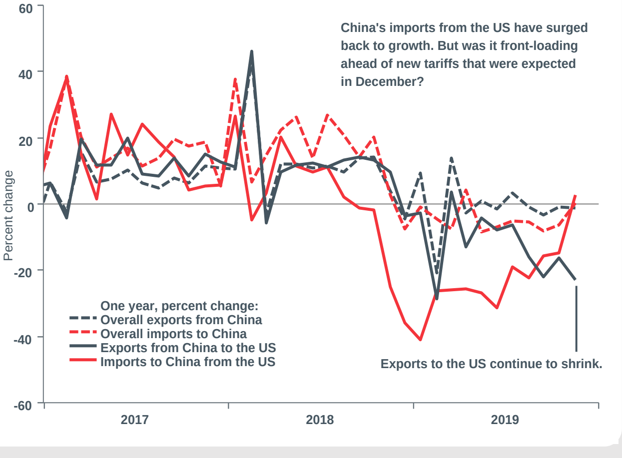


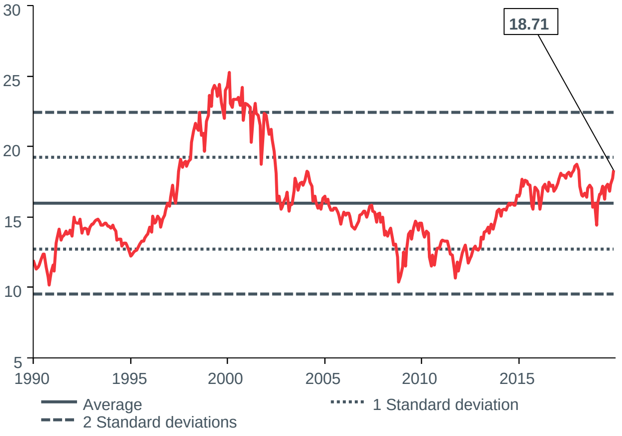
Figure 10. China & US trade



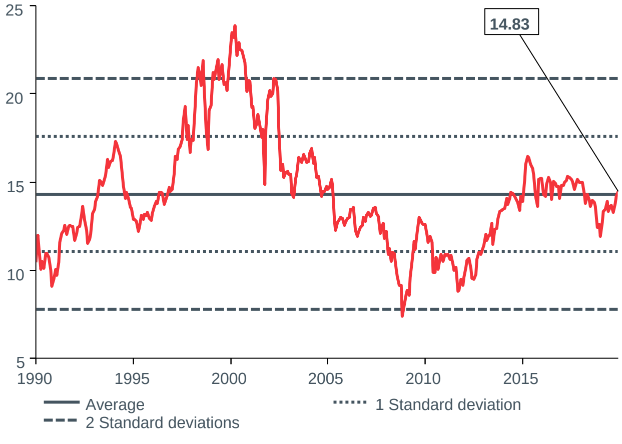
Source: Eastspring Investments. Chart data from Refinitiv Datastream as of 31 December 2019.

MSCI AC World 12M Forward PE

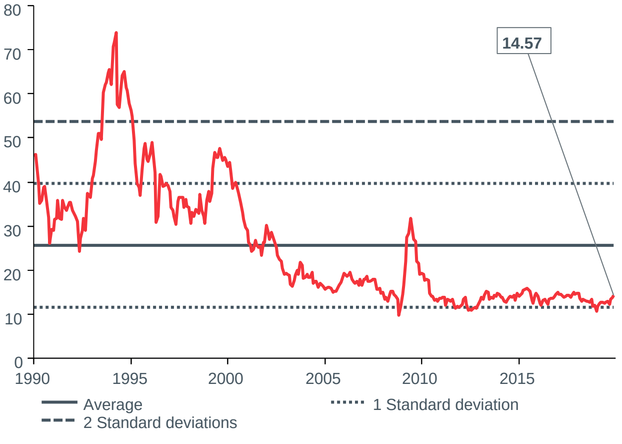
MSCI USA 12M Forward PE



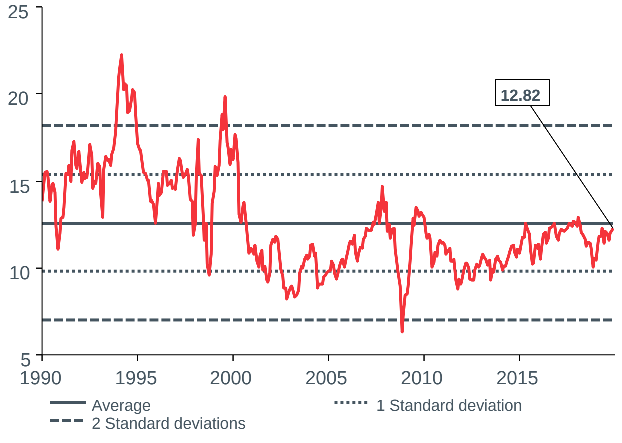
MSCI Europe 12M Forward PE



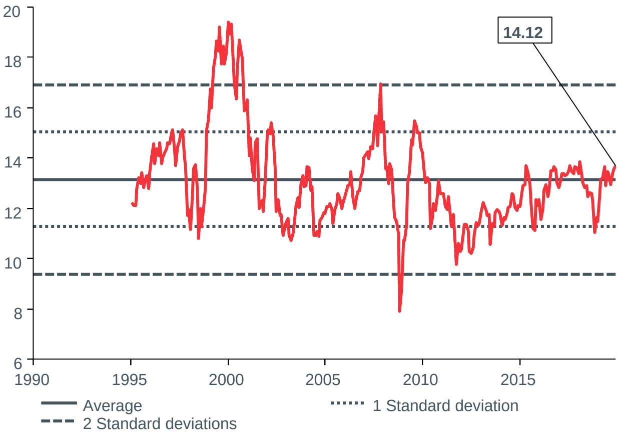
MSCI Japan 12m Forward PE



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 December 2019.

MSCI monthly, quarterly and year-to-date data

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	Dec-19	Nov-19	Q4 19	Q3 19	Q2 19	Q1 19	2019	2018
World	3.6	2.5	9.1	0.1	3.8	12.3	27.3	-8.9
Developed World	3.0	2.8	8.7	0.7	4.2	12.6	28.4	-8.2
United States	2.9	3.8	9.1	1.6	4.3	13.9	31.6	-4.5
Europe	3.9	1.5	8.9	-1.8	4.9	11.0	24.6	-14.3
Japan	2.1	0.6	7.7	3.3	1.0	6.8	20.1	-12.6
Emerging Markets	7.5	-0.1	11.9	-4.1	0.7	10.0	18.9	-14.2
Asia Pac Ex Japan	5.8	0.4	10.6	-3.9	0.8	11.5	19.5	-13.7
Asia Ex Japan	6.7	0.2	11.8	-4.4	-0.6	11.4	18.5	-14.1
Latin America	10.4	-4.1	10.6	-5.6	4.6	7.9	17.9	-6.2
Brazil	12.5	-4.4	14.4	-4.5	7.2	8.2	26.7	-0.2
EMEA	7.1	-0.1	10.0	-6.8	7.4	5.6	16.3	-15.5

	Dec-19	Nov-19	Q4 19	Q3 19	Q2 19	Q1 19	2019	2018
Australia	1.5	1.0	4.4	-1.4	7.4	11.4	23.1	-11.8
New Zealand	5.2	9.5	17.5	-2.8	4.0	16.9	38.8	-3.5
Hong Kong	4.0	-1.5	7.3	-11.9	1.0	15.6	10.3	-7.8
China	8.3	1.8	14.7	-4.7	-3.9	17.7	23.7	-18.7
Korea	10.4	-1.5	13.7	-4.5	-0.9	5.0	13.1	-20.5
Taiwan	7.5	1.5	18.0	5.9	1.1	9.0	37.7	-8.2
Thailand	0.9	-0.2	-0.8	-5.9	9.4	7.5	9.8	-5.3
Malaysia	4.0	-2.0	3.1	-6.3	1.2	0.3	-2.0	-6.0
Singapore	3.2	-1.3	7.5	-5.8	7.0	6.2	15.0	-9.4
Indonesia	7.1	-2.8	7.0	-5.2	3.7	4.3	9.7	-8.7
India	1.5	-0.6	5.3	-5.2	0.5	7.2	7.6	-7.3
Philippines	1.6	-3.3	3.0	-4.6	4.6	8.0	11.0	-16.1

	Dec-19	Nov-19	Q4 19	Q3 19	Q2 19	Q1 19	2019	2018
Mexico	4.8	-2.0	6.3	-1.6	1.3	5.6	11.8	-15.3
Chile	10.9	-11.5	-8.8	-7.3	-4.9	4.4	-16.0	-18.9
Hungary	9.7	1.3	22.2	-3.9	-4.1	6.0	19.4	-6.1
Poland	2.7	-4.4	4.1	-11.7	3.6	-0.6	-5.3	-12.5
Czech Republic	5.8	-0.1	9.2	-9.5	3.9	3.8	6.6	-2.2
Russia	8.4	-0.7	17.1	-0.9	17.3	12.2	52.7	0.5
Turkey	1.9	7.0	0.0	11.7	3.1	-3.0	11.7	-41.1
South Africa	9.7	0.0	13.2	-12.4	6.8	4.6	10.7	-24.3
Qatar	4.3	-0.1	2.2	-0.2	0.6	-3.5	-1.0	29.8
Saudi Arabia	6.1	1.7	3.3	-9.3	1.4	14.9	9.1	19.2
United Kingdom	5.2	1.7	10.0	-2.5	0.9	11.9	21.1	-14.1
Germany	1.9	1.8	9.9	-4.0	7.8	7.0	21.7	-21.6
France	3.0	1.7	8.6	-1.6	7.3	10.8	27.0	-11.9
Netherlands	3.7	2.3	7.4	2.5	6.1	13.6	32.7	-12.8
Austria	3.6	-1.2	9.1	-3.0	3.1	8.6	18.4	-23.2
Italy	2.7	0.6	8.1	0.1	3.6	14.7	28.7	-17.0
Spain	4.2	-0.4	6.2	-3.8	2.9	7.1	12.7	-15.7
Greece	2.9	1.7	12.7	-3.0	16.4	12.8	43.6	-36.7
Portugal	4.8	-0.9	8.7	1.8	2.6	10.2	25.2	-10.1
Switzerland	4.4	1.2	7.6	0.3	9.0	13.5	33.6	-8.2

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

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