# Bulls still in charge. Just

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August 2019

## The World in six bullet points

- **Equity markets** around the world had a weak month although a rally in the final few days took the sting out of what was looking to be the worst month of the year at one point. Again, the catalysts for the volatility proved to be newsflow on the US-Sino trade dispute and increasing signs of weakness in the global macro economic picture as well as central bank responses. Related to this, US two-year bond yields inverted against the ten-year yield in another sign that the bond market was pointing towards a recession.
- **China** allowed its renminbi to weaken to below the key threshold of RMB7/$1 in an apparent escalation of its trade dispute with the US. The move came after the White House said it would impose a 10% tariff on another USD300bn worth of exports starting in September, and although the threat was later withdrawn, the renminbi remained below 7.0, and later devalued to 11-year lows when the US changed its mind again.
- Protests in **Hong Kong** escalated and became violent at times as discontent over an extradition bill evolved into demands for an enquiry into alleged police brutality. The protests included a sit-in at the city's international airport, which caused flights to be cancelled and, together with further marches in the financial district, had some economists pointing to an escalating hit on the city's economy.
- Fears over a **global economic slowdown** increased further when poor economic data points from Germany and China sent bond yields from both governments sharply lower. Adding to pressure, yields on UK and US 10-year bonds fell below shorter term duration bonds for the first time since the 2008 financial crisis, an inversion that has preceded every recession since the 1980s.
- **Argentina's peso** collapsed alongside its stock market after the country's reform-minded president, Mauricio Macri, surprisingly lost primary elections to a rival closely associated with former president, Cristina Kirchner. Although Mr Macri attempted a damage-limitation relief programme for poorer sections of Argentina's society, most observers think it is 'too little too late', and it will be hard for him to be returned as president in October's elections.
- Britain's exit from the European Union, known as **Brexit**, took another twist when the country's new Prime Minister Boris Johnson prorogued (or suspended) parliament. The move drastically increased the chances of a no-deal Brexit as members of parliament, who on the whole are against leaving without a deal, now have only a few options left and only a handful of days on which to force Mr Johnson to postpone the exit date again, or bring a vote of no confidence against him.

**Figure 1: MSCI China vs yuan**

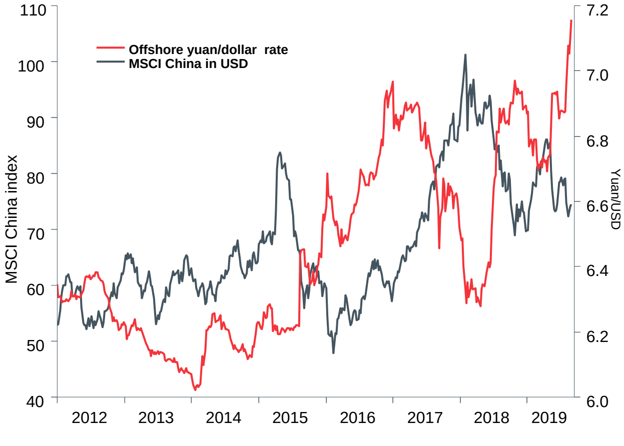
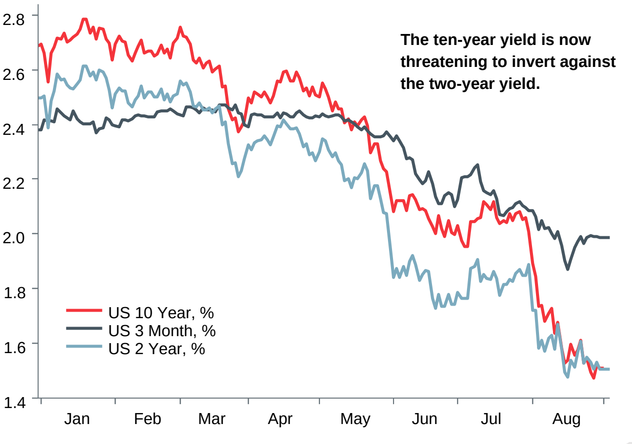



**Figure 2. US 2yr, 10yr and 3-month Bond yields**



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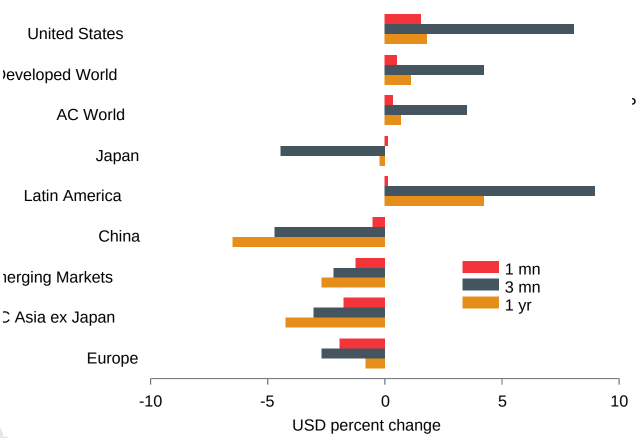
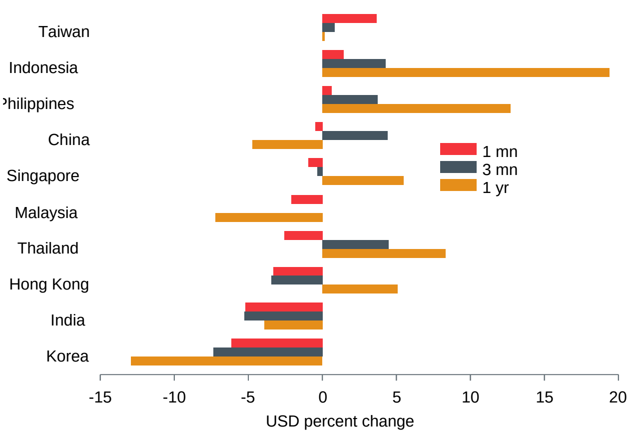
# Equity Markets

- **Global** equity markets fell through August and despite a modest uptick towards the end of the month, almost all major indices finished in the red. The White House's announcement of further tariffs on Chinese imports was the catalyst for the steepest of the falls but equities were already lower on poor macro economic data from China and Europe, as well as the ominous sign that the US two-year bond yield was set to invert against the ten-year yield – an event that has preceded every recession for the past forty years.
- Despite this, **US** equities outperformed their European counterparts with the MSCI US index falling just 1.7% against the Europe Index down 2.5%. The **Developed World** index dropped 2% to outperform **Emerging Markets** which fell 4.8%, pulled down by some very weak returns in Brazil, Hong Kong, and Turkey, although no EM indices were spared the sell off. Deteriorating macro economic data in some large EM countries and the escalating trade dispute appeared to be the catalyst for the sell off.
- The weakening economic data combined with strength in the US dollar to send **Emerging Markets** sharply lower but returns in EMEA and Latin America were notably under those of Asia. In Latam, Brazil fell 9.2% to pull the regional index down by 8.1%. In the **EMEA** region, Turkey fell 10.7%, which combined with some very weak returns from South Africa and Poland, was enough to pull EMEA 7.3% down.
- Meanwhile, **Asian** markets were also weak but some showed signs of resilience. Thailand, Taiwan and India all outperformed but they weren't enough to offset a sharp drop in Hong Kong, as the city's protests began to impact the economy there and Beijing threatened to crack down on the protests. The MSCI Hong Kong index fell by more than 8% versus the MSCI China index that only lost 4.2%. **Korea** also had another weak month despite an interest rate cut by the central bank and ended 5.0% lower.
- Elsewhere, **Australian** stock again outperformed to fall just 4.3% but **New Zealand** finally gave up some of its year-to-date gains to drop 6.8% after a surprise 50bps interest rate cut. **Japan** also outperformed as the yen gained against the dollar with the MSCI Japan index losing only 1.0%. Among some of the developed markets, the **UK** fell 4.7% despite another lurch lower in sterling on the country's Brexit woes, while **Germany** lost 3.0% on weak economic data. **Italy** was a notable outperformer as its government collapsed, leading some to see a route forward in its dispute with the EC on its budget deficit.

### Figure 3. Regional Equity Indices




### Figure 4. Asia Equity Indices




Source: Eastspring Investments. Chart data from Thomson Reuters Data stream as of 31 August 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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# Fixed Income

- In **global bond markets**, US Treasuries (UST) rallied in August as China-US tensions intensified with tit-for-tat trade tariffs. The flight to safety resulted in a fall in US Treasury yields and a significant flattening of the curve that suggested rising anxiety over the state of the US economy, which overshadowed surprisingly strong domestic retail sales. Both the 2-year and 10-year UST yields ended at 1.5%, after declining by 37 bps and 52 bps respectively.
- Core bond markets elsewhere were similarly firm. **German** bund yields fell to new lows on expectations of a substantial easing package to come in September, as minutes of the European Central Bank's July meeting showed policymakers advocating for a combination of rate cuts, asset purchases and support for lenders to boost growth.
- **Asian** local-currency government bonds also strengthened as the rate-cut cycle continued in the region. Notably, policy moves were seen in Thailand, the Philippines and Indonesia, along with India, which lowered interest rates by an unconventional 35 bps. Elsewhere in emerging markets, Mexico became the latest to surprise with a rate cut, its first in five years. Argentine bonds sold off on the back of the weak performance of President Mauricio Macri at the presidential primaries. The crash in the Argentine peso added to market stress as it raised concerns over the country's ability to repay its USD-denominated debt obligations. Subsequently, the government said it would negotiate with investors and the IMF to extend the maturities of its debt, and that interest and principal payments would not be altered.
- **Emerging-market** USD-denominated credits also delivered positive returns in aggregate, mainly on the back of lower US risk-free rates. Credit spreads widened, however, given the worsening trade tensions. In Asia, risk aversion was exacerbated by the escalating trade dispute between Japan and Korea. In this environment, Asian USD-denominated investment-grade credits rose and outperformed on a total-return basis. Conversely, high-yield credits posted a lower overall return, hampered by substantially wider credit spreads.

**Figure 5. Bond Indices Performance in USD**

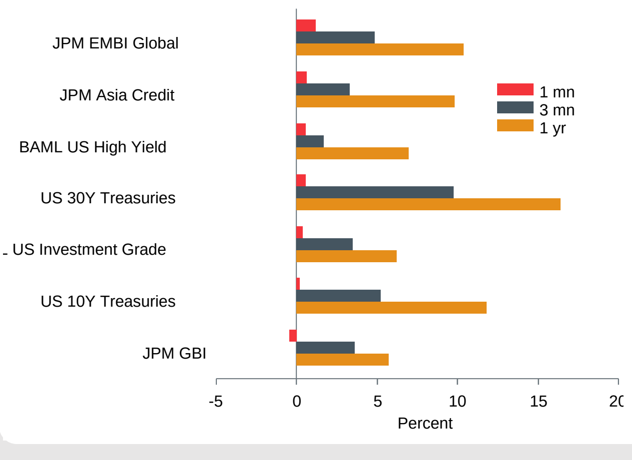
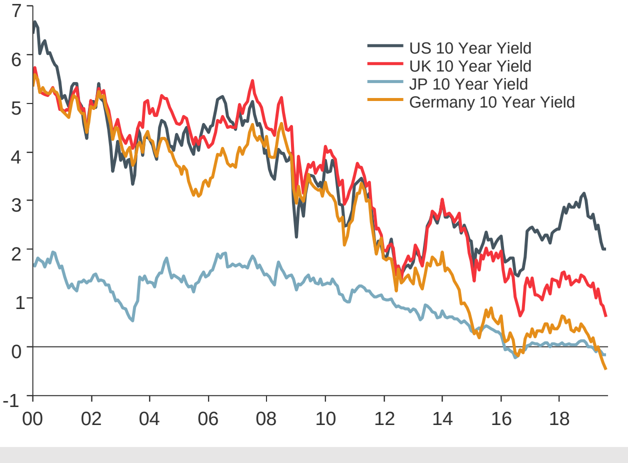



**Figure 6. Key Bond Yields (%)**




Source: Eastspring Investments. Chart data from Bank of America Merrill Lynch, JP Morgan, Refinitiv Datastream as of 31 August 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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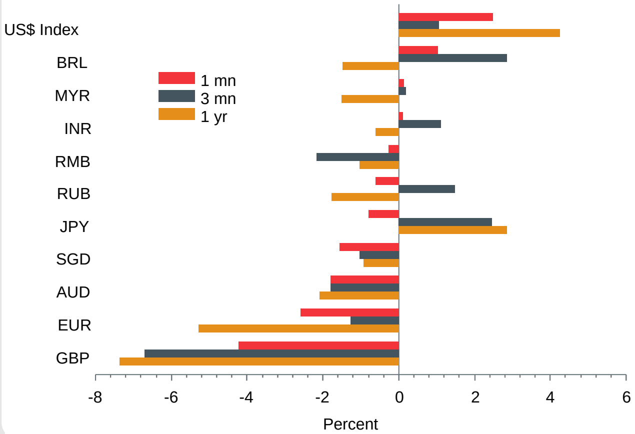
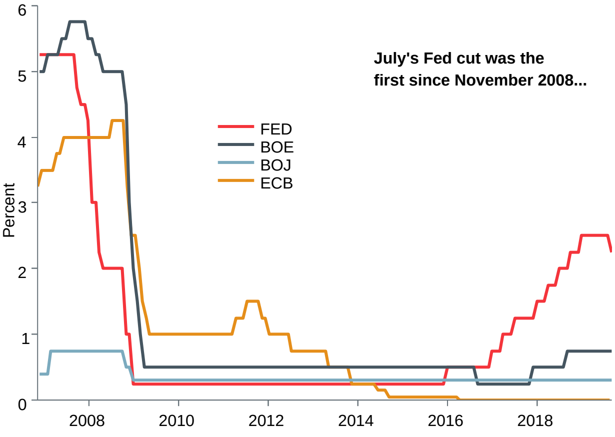
## Currencies

- **US dollar** performance against G10 currencies was mixed in August. The New Zealand dollar and Norwegian kroner saw the biggest declines against the dollar, down between 2-4%. The Reserve Bank of New Zealand surprised markets by cutting policy rates by 50bp, weighing on the currency as well as the equity market there.
- On the plus side, the trade war escalation drove a “flight to safety”, with the Japanese yen and Swiss franc appreciating against the dollar. The UK British pound whipsawed, testing the 1.20 resistance level earlier in the month as probability of a hard Brexit increased, before bouncing back later in the month, to close slightly stronger against the dollar.
- **Emerging markets’ currencies** were unanimously weaker against the dollar given a string of adverse macro events that triggered a risk-off move: a) the Fed was less dovish than expected in July; b) the United States escalated the trade war by imposing a 10% tariff on the remaining $300bn of Chinese exports (and subsequently increased to 15%); and c) the US treasury designated China a currency manipulator as USD/CNY spot crossed the psychologically important 7.0 mark. High carry EM currencies were the worst hit in August with Latin American currencies (Brazilian real, Mexican peso and Columbian peso) depreciating significantly. The Argentine peso dropped nearly 25% of its value after the primary election results indicated a defeat for President Macri. Political risk is likely to continue to dominate Argentine markets’ performance.
- **In Asia,** the trade war escalation led Chinese yuan to cross the psychologically important 7.0-mark against the dollar early in the month. Chinese policymakers emphasized that the depreciation was not “engineered” and instead a result of the trade war, while the US Treasury signaled that China was manipulating its currency to offset the effects of the tariffs.
- The back and forth spat between US and China kept other **Asian currencies** under pressure, particularly those of the small open economies (Korean won, Malaysian ringgit, Singapore dollar). The Indian rupee underperformed given domestic growth concerns and a more dovish central bank; while the Thai baht has been the only EM Asian currency to have appreciated against the dollar, in part led by a gold rally.

### 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 August 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** prices fell sharply over the month as worries over the health of the global economy weighed on prices. Meanwhile tensions in the Middle East eased somewhat after The White House hinted that it would be willing to meet with Iran. Oil prices are now down almost 10% year to date and are 20% off their highs of last year.
- **Copper** prices fell to two-year lows as the escalating trade conflict between the US and China and a weakening remninbi weakened the outlook for demand. Prices are now 20% off their peak from June 2018 however a slowdown in copper mine production in H2 this year could cause the metal to find a floor.
- **Gold** prices rose early in the month on geo-political tensions especially in the Gulf before falling from their peaks after the comments from Fed Chair Powell on interest rates pushed up the US dollar and weighed on gold prices. Nevertheless, gold is still substantially higher in the year to date (Figure 9) in contrast to copper and oil.
- **Nickel and** tin prices also fell to reflect the worries over demand while aluminium steadied to reflect a output dip. **Iron ore** prices fell almost 30% as traders began to price in a slowing global economic picture and weaker remninbi.

## Economics

- **US** GDP slowed to 2.1% growth in Q2 from 3.1% in Q1 but was well above expectations of 1.8%. For July, the economy had its 121st consecutive month of expansion, surpassing the previous expansion record that began in 1991. Employers added 224,000 jobs and unemployment slightly.
- Other economic figures were more mixed. GDP in **Canada** rose 3.7% above expectations, but final domestic demand fell 0.7% pointing to potential weakness ahead. **India's** GDP growth slowed to just 5.0% year over year, the weakest since 2013 and down from more than 8% in Q1 last year; domestic demand was the main drag on the quarter's poor performance. Brazil's GDP rose 0.4% qoq, while year-on-year growth picked up slightly to 1%.
- In Asia, **Korea's** economy continued to show weakness: exports for the first 20 days of July fell 13.6% yoy, the seventh such monthly decline in a row, with semi-conductor sales down 30%. The central bank subsequently cut rates by 25bps. **Indonesia's** central bank also cut rates by 25bps to 5.75%, and **Russia** cut its rates also by 25bps to 7.25%.**China's** manufacturing data showed another dip but this was overshadowed by the weakening renminbi and new tariffs on US imports.

**Figure 9: Commodity Prices, year to date**

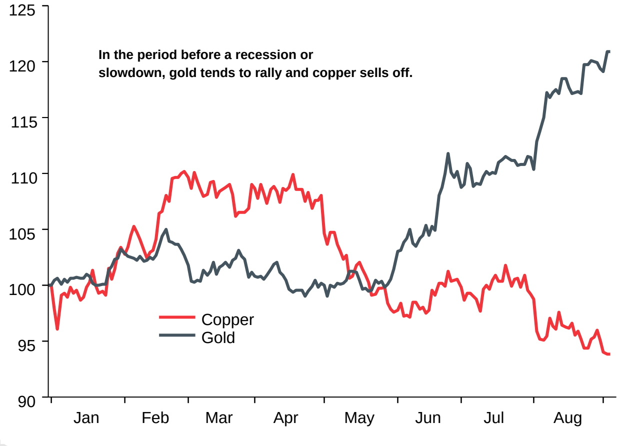
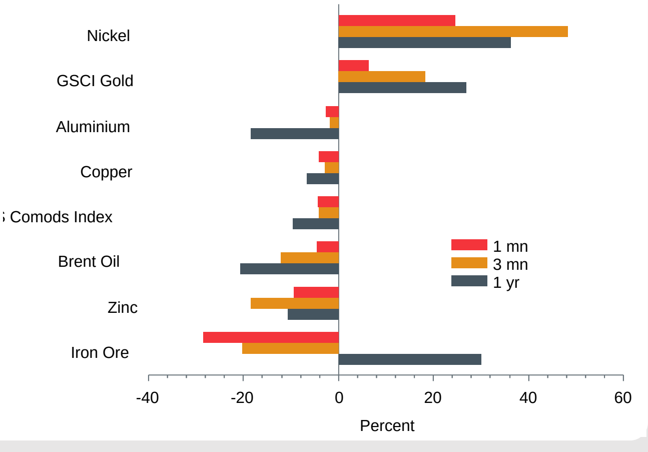



**Figure 10. Commodities Performance in USD**




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

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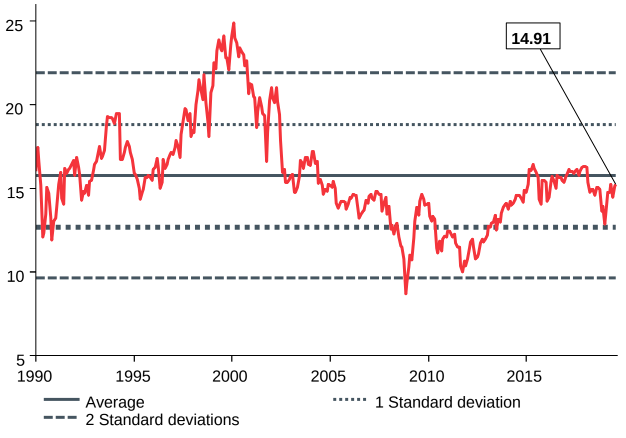
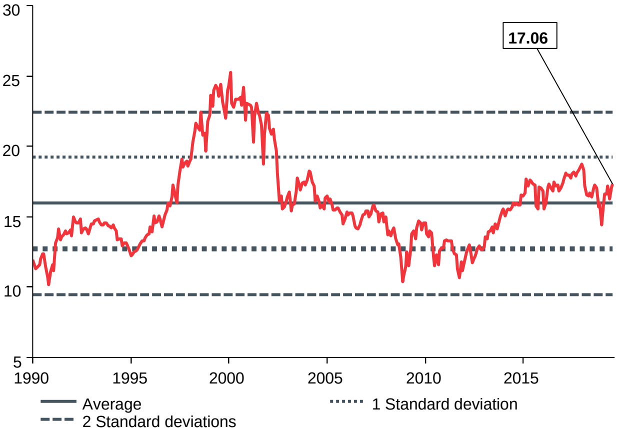
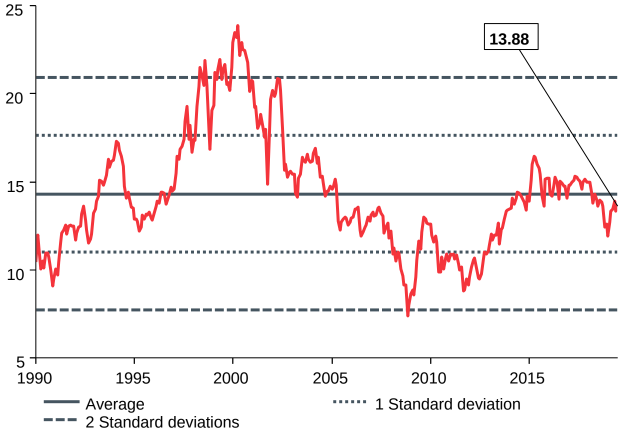
## MSCI AC World 12M Forward PE



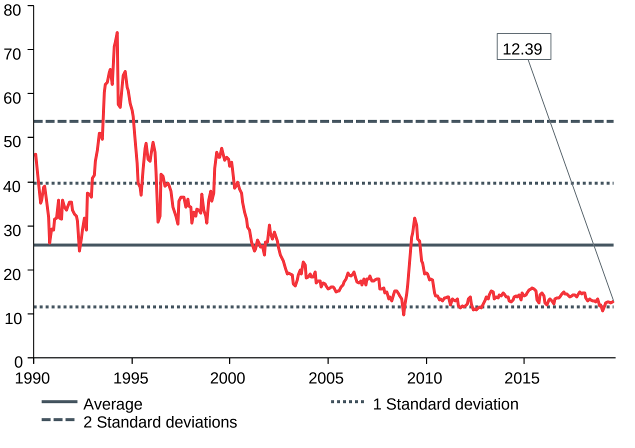

## MSCI USA 12M Forward PE



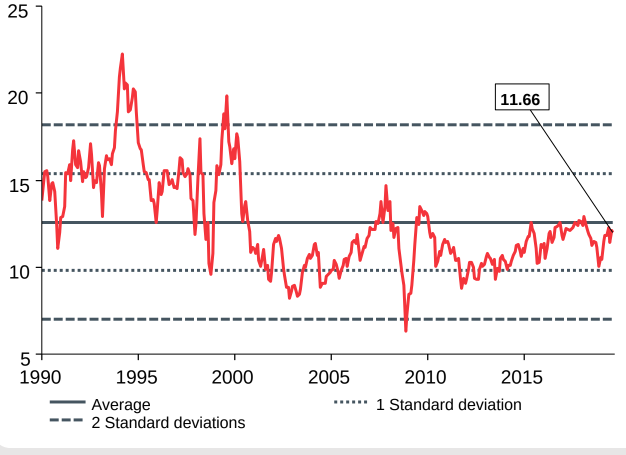

## MSCI Europe 12M Forward PE



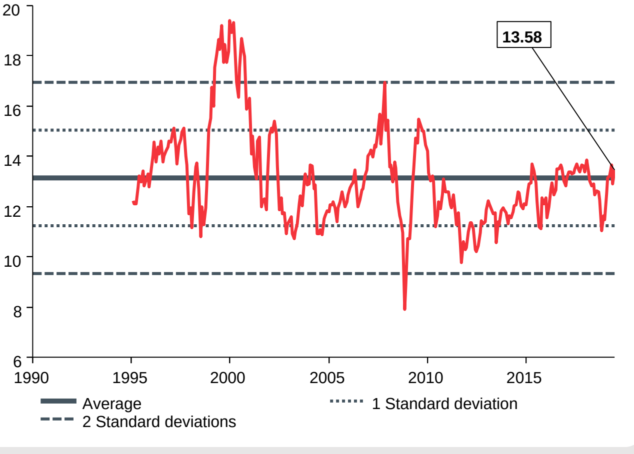

## MSCI Japan 12m Forward PE




## 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 August 2019.

# MSCI monthly, quarterly and year-to-date data

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| | Aug-19 | Jul-19 | QTD | Q2 19 | Q1 19 | H1 19 | YTD | 2018 |
|---|---|---|---|---|---|---|---|---|
| World | -2.3 | 0.3 | -2.0 | 3.8 | 12.3 | 16.6 | 14.3 | -8.9 |
| Developed World | -2.0 | 0.5 | -1.5 | 4.2 | 12.6 | 17.4 | 15.6 | -8.2 |
| United States | -1.7 | 1.5 | -0.2 | 4.3 | 13.9 | 18.8 | 18.5 | -4.5 |
| Europe | -2.5 | -1.9 | -4.4 | 4.9 | 11.0 | 16.5 | 11.4 | -14.3 |
| Japan | -1.0 | 0.1 | -0.9 | 1.0 | 6.8 | 8.0 | 7.0 | -12.6 |
| Emerging Markets | -4.8 | -1.1 | -5.9 | 0.7 | 10.0 | 10.8 | 4.2 | -14.2 |
| Asia Pac Ex Japan | -4.4 | -1.3 | -5.6 | 0.8 | 11.5 | 12.4 | 6.1 | -13.7 |
| Asia Ex Japan | -4.4 | -1.7 | -6.0 | -0.6 | 11.4 | 10.8 | 4.2 | -14.1 |
| Latin America | -8.1 | 0.1 | -8.0 | 4.6 | 7.9 | 12.9 | 3.9 | -6.2 |
| Brazil | -9.2 | 2.6 | -6.9 | 7.2 | 8.2 | 16.0 | 8.0 | -0.2 |
| EMEA | -7.3 | -0.5 | -7.7 | 7.4 | 5.6 | 13.4 | 4.6 | -15.5 |

| | Aug-19 | Jul-19 | QTD | Q2 19 | Q1 19 | H1 19 | YTD | 2018 |
|---|---|---|---|---|---|---|---|---|
| Australia | -4.3 | 0.6 | -3.7 | 7.4 | 11.4 | 19.6 | 15.2 | -11.8 |
| New Zealand | -6.8 | 4.0 | -3.1 | 4.0 | 16.9 | 21.5 | 17.8 | -3.5 |
| Hong Kong | -8.3 | -3.3 | -11.3 | 1.0 | 15.6 | 16.8 | 3.5 | -7.8 |
| China | -4.2 | -0.5 | -4.7 | -3.9 | 17.7 | 13.1 | 7.8 | -18.7 |
| Korea | -5.0 | -6.2 | -10.9 | -0.9 | 5.0 | 4.1 | -7.3 | -20.5 |
| Taiwan | -2.1 | 3.7 | 1.5 | 1.1 | 9.0 | 10.2 | 11.9 | -8.2 |
| Thailand | -2.5 | -2.6 | -5.0 | 9.4 | 7.5 | 17.7 | 11.8 | -5.3 |
| Malaysia | -3.7 | -2.1 | -5.8 | 1.2 | 0.3 | 1.5 | -4.4 | -6.0 |
| Singapore | -6.0 | -0.9 | -6.9 | 7.0 | 6.2 | 13.6 | 5.8 | -9.4 |
| Indonesia | -3.7 | 1.4 | -2.4 | 3.7 | 4.3 | 8.1 | 5.5 | -8.7 |
| India | -2.9 | -5.2 | -8.0 | 0.5 | 7.2 | 7.7 | -0.9 | -7.3 |
| Philippines | -3.3 | 0.6 | -2.7 | 4.6 | 8.0 | 13.0 | 10.0 | -16.1 |

| | Aug-19 | Jul-19 | QTD | Q2 19 | Q1 19 | H1 19 | YTD | 2018 |
|---|---|---|---|---|---|---|---|---|
| Mexico | -0.4 | -3.8 | -4.2 | 1.3 | 5.6 | 6.9 | 2.4 | -15.3 |
| Chile | -6.4 | -5.0 | -11.1 | -4.9 | 4.4 | -0.7 | -11.7 | -18.9 |
| Hungary | -4.9 | 0.2 | -4.8 | -4.1 | 6.0 | 1.7 | -3.1 | -6.1 |
| Poland | -8.7 | -4.2 | -12.6 | 3.6 | -0.6 | 3.0 | -9.9 | -12.5 |
| Czech Republic | -5.3 | -1.7 | -7.0 | 3.9 | 3.8 | 7.9 | 0.3 | -2.2 |
| Russia | -4.7 | 0.7 | -4.0 | 17.3 | 12.2 | 31.6 | 26.3 | 0.5 |
| Turkey | -10.7 | 11.3 | -0.6 | 3.1 | -3.0 | 0.0 | -0.6 | -41.1 |
| South Africa | -8.9 | -2.8 | -11.4 | 6.8 | 4.6 | 11.7 | -1.1 | -24.3 |
| Qatar | -2.0 | 1.0 | -1.0 | 0.6 | -3.5 | -2.9 | -3.9 | 29.8 |
| Saudi Arabia | -8.8 | -1.0 | -9.7 | 1.4 | 14.9 | 16.5 | 5.2 | 19.2 |
| United Kingdom | -4.7 | -1.8 | -6.4 | 0.9 | 11.9 | 13.0 | 5.7 | -14.1 |
| Germany | -3.0 | -3.5 | -6.3 | 7.8 | 7.0 | 15.4 | 8.1 | -21.6 |
| France | -1.7 | -2.4 | -4.0 | 7.3 | 10.8 | 18.9 | 14.1 | -11.9 |
| Netherlands | -1.0 | 0.9 | -0.1 | 6.1 | 13.6 | 20.5 | 20.4 | -12.8 |
| Austria | -3.6 | -1.7 | -5.3 | 3.1 | 8.6 | 11.9 | 6.1 | -23.2 |
| Italy | -1.4 | -1.3 | -2.7 | 3.6 | 14.7 | 18.9 | 15.7 | -17.0 |
| Spain | -3.5 | -4.2 | -7.5 | 2.9 | 7.1 | 10.2 | 1.9 | -15.7 |
| Greece | -5.3 | 0.4 | -5.0 | 16.4 | 12.8 | 31.3 | 24.8 | -36.7 |
| Portugal | -1.7 | -0.5 | -2.1 | 2.6 | 10.2 | 13.1 | 10.7 | -10.1 |
| Switzerland | 0.3 | -0.7 | -0.4 | 9.0 | 13.5 | 23.7 | 23.2 | -8.2 |

Source: Eastspring Investments. Chart data from Thomson Reuters Data stream as of 31 JAugust 2019. Data and commentary prepared by Peter Bennett.

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