eastspring investments
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MARKET BRIEFING

JUNE EQUITY MARKET REVIEW:

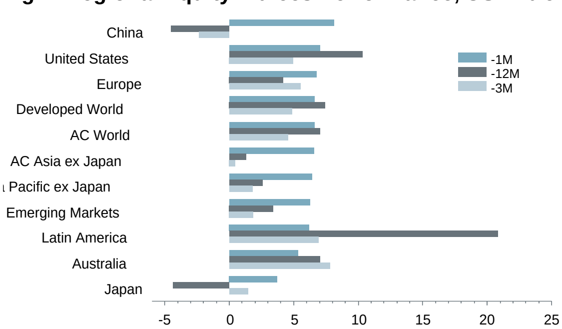
Equity markets bounce back but trade concerns persist

June 2019

The World in five bullet points

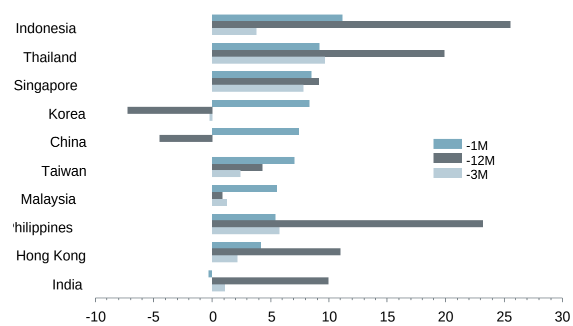
- **Equity markets** bounced back from the sharp falls in May after the US Federal Reserve signaled it would be prepared to cut interest rates to preserve economic growth. The White House's pullback from trade tariffs against Mexico proved to be another driver as did the restart of trade negotiations between the US and China. At the G20 summit in Japan in June end, the presidents of both countries agreed to resume trade talks, giving markets a boost at the start of July's trading month.
- **Tensions in the Gulf** rose sharply when two chemical tankers were attacked and set alight in the Gulf of Oman. The US said Iran was behind the attack, but Iran quickly denied this. Then, a US drone was shot down, and while the US said it had planes in the air for a retaliatory attack, those planes were called back. The result: a 10% spike in crude prices and a serious escalation in geopolitical tension, recovering from falls earlier in the month.
- The **US Federal Reserve** hinted it would be willing to cut rates sooner rather than later, noting the heightened economic uncertainty. Fed Fund Futures indicate two cuts before the end of the year, with many economists penciling in July and October for two 25bps cuts. The Bank of Japan, the European Central Bank (ECB) and the Bank of England also gave varying dovish statements, giving an immediate boost to stocks and sending many bond yields to record or multi-year lows.
- **Turkey's** President Erdogan suffered a political blow when a re-run of the Istanbul mayoral election was won by the same opposition figure who had won the first vote in late March. President Erdogan once said that losing Istanbul meant losing Turkey and re-ran the election claiming fraud first time around. Meanwhile, million-strong public protests in Hong Kong forced the government there to withdraw a controversial extradition bill that would have allowed transfer of fugitives to any jurisdiction that Hong Kong lacks a formal agreement with, including mainland China.
- The White House threatened a 5% **tariff on Mexican imports** in its latest round of negotiation tactics on illegal immigration, before pulling back and saying the two countries had reached a deal. But the threat sent markets into a near panic at the beginning of the month as the tariffs would have meant a significant escalation in the US's trade disputes, potentially affecting $346bn worth of imports – more than double that already imposed on Chinese imports.

Fig.1. Regional Equity Indices Performance, USD % change



Source: Thomson Reuters Datastream, MSCI

Fig.2. Asia Equity Indices Performance, US$ % change



Source: Thomson Reuters Datastream, MSCI

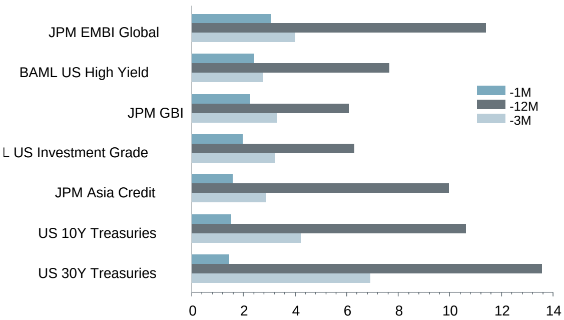
Equity Markets

- **Global equity** markets responded well to the triple drivers of potential rate cuts, Sino-US trade talks resuming and the pullback on Mexican tariffs, with almost all country-based MSCI indices seeing gains. India was the exception post an outperformance in April and sudden spike in oil prices towards the end of the month and fell 0.3%. The US finished 7% higher, once again outperforming most other regions as well as the Emerging Markets index which finished 6.3% up, despite a lower US dollar.
- **European** equities modestly underperformed the US but hints from the European Central Bank (ECB) that it was again open to considering asset purchases lent support, giving **France** and **Germany** a boost, and despite weak industrial output data from the latter. **Italy** outperformed and returned 9.9% as the country obtained a reprieve from European Commission disciplinary procedures on its budget deficit. The **UK** underperformed to return just 5.5% on weaker economic data and as a pro-Brexiter, Boris Johnson, closed in on the premiership and pushed the pound lower.

Source: Eastspring Investments. Chart data from Thomson Reuters Datastream as at 30 June 2019. For representative indices and acronym details please refer to notes in the appendix.

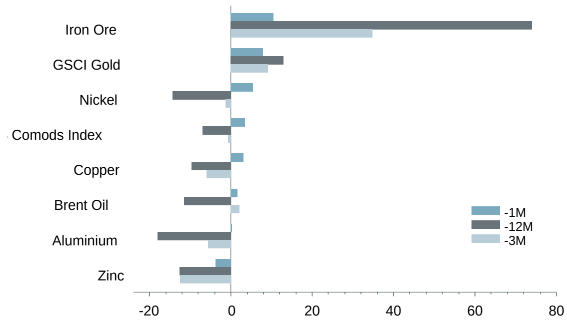
- Emerging Market regional indices were all higher with none taking the lead or outperforming in any meaningful way. **Asia ex Japan** was 6.7% higher, **EMEA** 5.9% and **Latin America** 6.2% higher with the Brazil market once more pulling that region higher as social security reform inched forward. Most emerging markets benefited from the lower dollar with the exception of India as tensions surrounding trade negotiations eased and traders looked to the G20 summit for the next catalyst.
- Asian markets were pulled higher by the easing of trade tensions and the lower dollar. **Singapore** was the best performing market as trading partner China announced economic stimulus plans and **Thailand** also outperformed, returning 9.6% on signs of political stability. **China** gained 8.1% after Beijing relaxed finance rules that would allow municipal governments to issue bonds for infrastructure projects and **Korea** was a notable outperformer on hopes Beijing would follow through with further economic stimulus. The region's underperformers were **Malaysia**, up just 2.9% and **Philippines**, up 2.2%, as weak economic data and trade war uncertainty weighed.
- Elsewhere, **Japan** underperformed and Gulf tensions threatened exporters with auto stocks dragging the index lower. **Australian** stocks tracked other developed markets higher with mining stocks gaining on the Beijing stimulus plans. **Russia** benefitted from the higher oil price and saw a 9.0% return and **Turkey** gained 7.6% as its opposition party won the Istanbul mayoral election.

Fig 3. Bond Indices Performance in US$, %change



Source: Thomson Reuters Datastream, Bank of America Merrill Lynch, JP Morgan

Fig 4. Commodities Performance in US$, % change



Source: Thomson Reuters Datastream

Fixed Income

- Core government bond yields fell further in June, given the unresolved trade tensions and more dovish stance from major central banks. The US Treasury 10-year yield ended 12bps lower at 2%; the curve stayed slightly inverted, with the 3-month T-bills' yield falling 24bps to 2.1%. The Fed gave its strongest signal yet that rate cuts were imminent, dropping its previous pledge to be "patient" and lowering its inflation targets for this year and next.
- In Asia, local rates continued their downward trend, with many central banks acknowledging the need to monitor downside growth risks. Indonesia, the Philippines and India performed well. The Reserve Bank of India cut its benchmark rate for a third time this year, bringing it 25bps lower to 5.75%, while shifting to an accommodative policy stance from neutral. Indonesia and the Philippines kept rates unchanged, although the former cut lenders' reserve requirement ratios by 50bps to boost liquidity. Bank Indonesia's governor added that a rate cut was all but certain but that he was considering the timing and magnitude. Conversely, Chinese bond yields underperformed, despite easing restrictions on the use of bond proceeds for infrastructure projects. The People's Bank of China continued to boost liquidity to support smaller banks.
- Emerging-market USD credits delivered positive returns on the back of firmer US Treasuries and narrower spreads. In Asia, returns and spreads were on par for both investment-grade and high-yield credits, with sovereign bonds doing particularly well given the more accommodative policy environment. Primary market activity was brisk, with new issues reportedly well absorbed.

Commodities

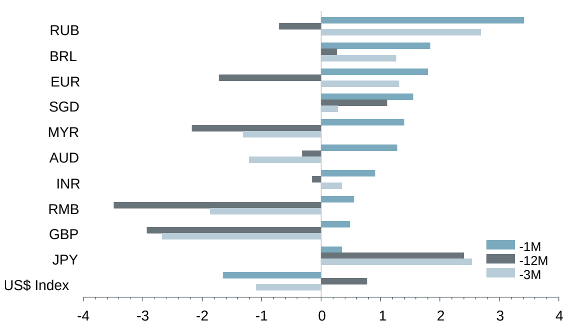
- **Oil prices** were very volatile in June, at first dipping to five-month lows on a build up in US stockpiles and potential tariffs on Mexican imports before rising sharply as geopolitical tensions in the Gulf increased, especially after the downing of a US drone by Iran. A White House offer for talks eased tensions and capped gains but prices were still supported in the second half of the month by the failure by OPEC to set a date for their next meeting, raising doubts on whether the organisation can keep to its programme of output cuts. By the end of the month, Brent was 9.3% higher and the US-based WTI blend was 3.2% higher.
- **US Gasoline** prices spiked after a unit at Philadelphia unit was completely destroyed in a fire but reserves had already risen to hover at five-year highs. **Copper** prices rose on hints of a rate cut in the US as well as a stimulus programme from Beijing supporting infrastructure projects. Early in the month, Shanghai copper contracts were trading at two-year lows on fears of a slowdown in global growth. **Nickel** prices hit month-long highs as mining operations in Indonesia were disrupted by floods.
- **Gold** rose 8.3% during the month and broke above the $1,400 per ounce mark for the first time since September 2013 after the Fed changed course on interest rates, sending the US dollar and bond yields lower. By the end of the month, as tensions in the Gulf increased, gold had reached fresh six-year highs. Iron ore was up by 14.1%; a significant reduction in China's iron ore stockpiles and the ongoing fallout from a Brazil mine disaster pushed prices up notably.

Source: Eastspring Investments. Chart data from Thomson Reuters Datastream as at 30 June 2019. For representative indices and acronym details please refer to notes in the appendix.

Currencies

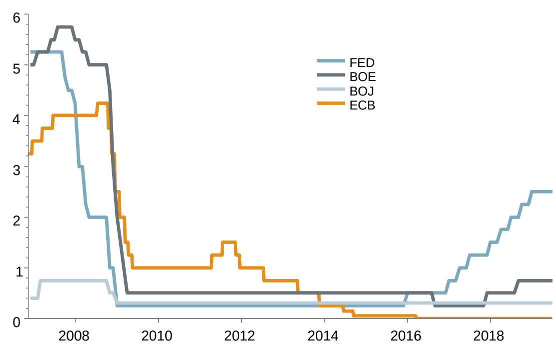
- The **US dollar (USD)** lost momentum in June against all major currencies as Fed expectations of a rate cut increased over the course of the month. June's non-farm payrolls disappointed while the University of Michigan 5-10 year inflation expectations printed a record low of 2.2%. Also, Trump reignited hopes that China-US trade talks may resume at the G20 meeting at the end of June with a tweet. This coupled with the Fed meeting which delivered on dovish expectations led to USD weakness across the board. The US Treasury 10-year yield has been on the decline since May. With the US dollar on the decline, other currencies with safe haven status particularly the Japanese yen failed to rally as much as other currencies, up only 0.4%. The euro gained nearly 2% against the USD. The UK pound also lagged thanks to political uncertainties, gaining only 0.5% against the USD. The Canadian dollar and the New Zealand dollar were up about 3% against the USD; the biggest winners in the G10 space.
- **Emerging market currencies** had a very strong run. Among the biggest winners against the USD were Latin American currencies with the Argentine peso and Colombian peso up more than 5% while the Chilean peso gained more than 4%. The recent pickup in oil prices due to geopolitical tensions helped the Russian ruble reverse most of the previous month's losses. The Central Bank of Russia also cut rates this month. Meanwhile, the Turkish lira failed to pick up momentum after a strong rally at the end of May. Idiosyncratic risks continue to weigh on the currency.
- **In Asia**, the Korean won and Thai baht led the pack gaining more than 3% against the USD as risk sentiment improved. The Korean won continues to be a bellwether for risk appetite and sentiment on Asia. The Thai baht continues to be one of the favourite Asian currencies despite its low yield. The Chinese yuan found support after Trump's tweet that trade talks could resume. In India the RBI cut another 25bps. The currency also gained nearly 1% against the USD.
- Elsewhere in emerging markets, political risks for Argentina's peso have declined. Both declared candidates have indicated that the chances of a major deviation from the current macro adjustment policies have reduced. Also the central bank of Mexico was more dovish than expected at the June meeting. There was one dissenting vote calling for easing.

Fig 5. Currencies Performance versus US$, % change



Source: Thomson Reuters Datastream

Fig 6. Central Banks Interest Rate, % change

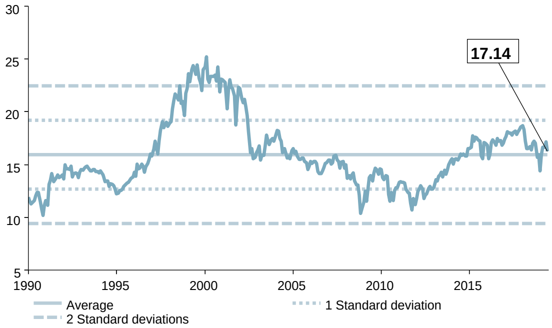


Source: Thomson Reuters Datastream

Economics

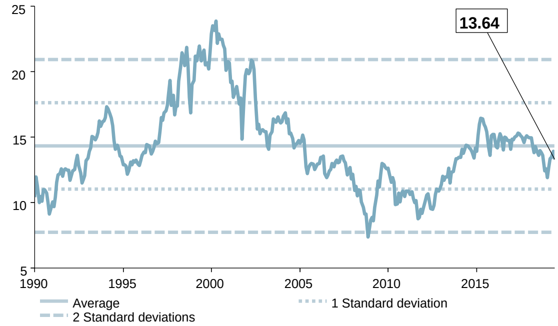
- The economic news from the **US** was overshadowed by the Fed's comments hinting at future interest rate cuts but the data in the run up to the statement pointed to a slowing US economy: Non-farm payrolls added just 75,000 jobs in May, average hourly earnings rose just 0.2% mom, inflation readings were lower than expected and the ISM manufacturing survey fell 0.7 points to a 31-month low of 52.1. Housing data was also weak. On the plus side, the service part of the survey rose to 56.9, reflecting a continuing divergence in the economy. Retail sales and industrial production figures were also higher, and inflation below target.
- The **European Central Bank** said it was looking at re-starting its asset-buying programme as economic data from eurozone countries continued to show weakness. CPI inflation slowed to 1.2% and German industrial output fell by 1.9% mom, both more than expected, and prompting the ECB to say rates would likely stay on hold until well into 2020. Rhetoric around Italy's budget deficit ebbed and flowed with the EC at one point threatening disciplinary action. The UK saw May manufacturing PMI fall to 49.4, the lowest since the month after the Brexit referendum, and industrial output fell 2.7% m-o-m as stockpiling in Q1 ahead of the intended Brexit date came to an end. UK GDP readings for April saw the economy contract by 0.4% m-o-m.
- **China's** economy also continued to show signs of softening, but certainly not to recession levels. Industrial output growth slowed to just 5% in April y-o-y, the smallest growth since 2002. But retail sales grew 8.6% y-o-y in May, rebounding from a sharp decrease in April. Beijing responded to the soft figures by allowing local authorities to issue bonds for infrastructure projects, in another attempt to stimulate the economy.
- **Japan's** central bank also expressed a willingness to be flexible on its key JGB ten-year yield, presently at the bottom of its 20 basis point band.

MSCI USA 12M Forward PE



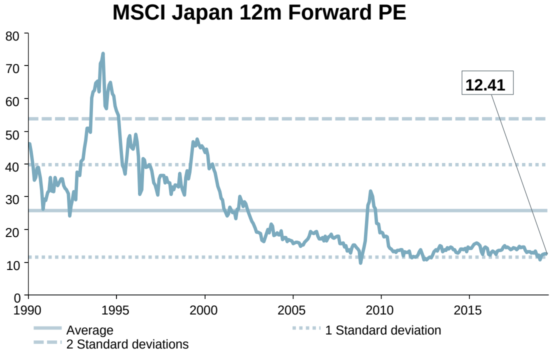
Source: Thomson Reuters Datastream, IBES

MSCI Europe 12M Forward PE



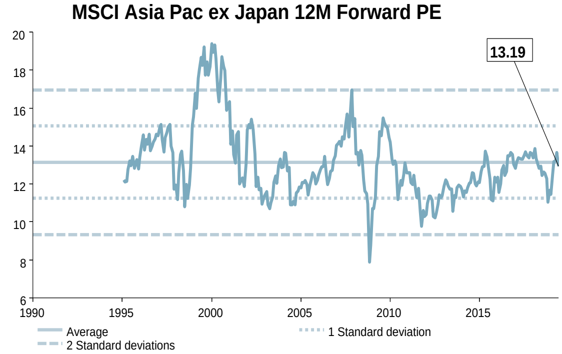
Source: Thomson Reuters Datastream, IBES

MSCI Japan 12m Forward PE



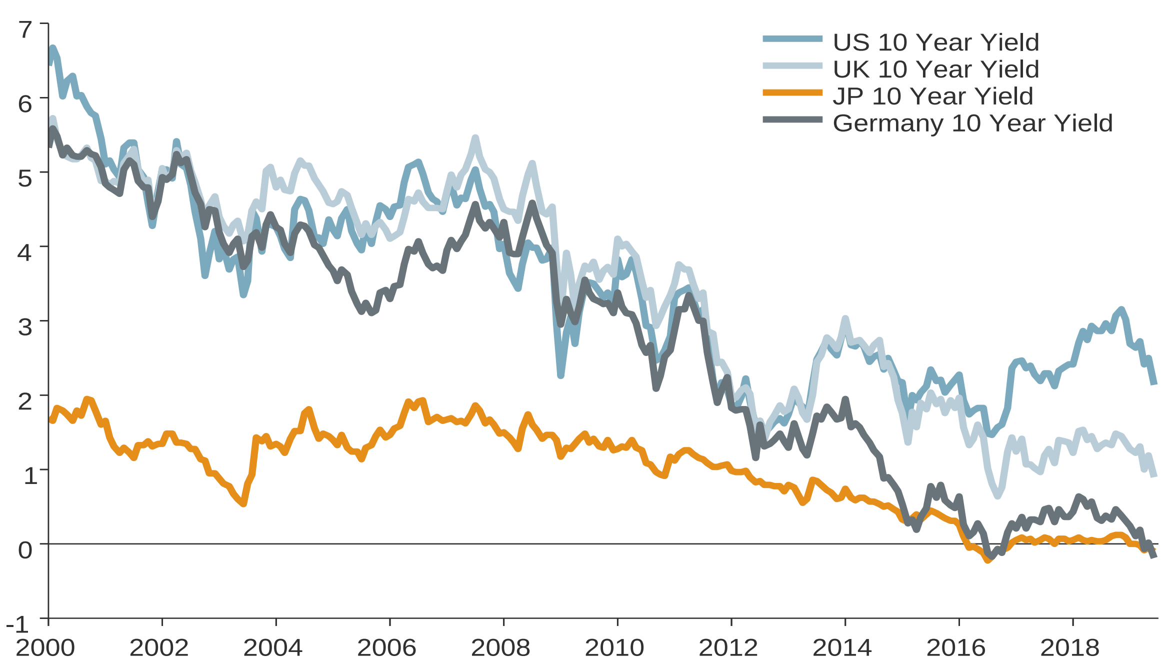
Source: Thomson Reuters Datastream, IBES

MSCI Asia Pac ex Japan 12M Forward PE



Source: Thomson Reuters Datastream, IBES

Fig 8. Key Bond Yields (%)



Source: Thomson Reuters Datastream

Source: Eastspring Investments. Chart data from Thomson Reuters Datastream as at 30 June 2019. For representative indices and acronym details please refer to notes in the appendix.

MSCI monthly, quarterly and year-to-date data

	Jun-19	May-19	Apr-19	Q2 19	Q1 19	YTD	Q4 18	2018
World	6.6	-5.8	3.4	3.8	12.3	16.6	-12.7	-8.9
Developed World	6.6	-5.7	3.6	4.2	12.6	17.4	-13.3	-8.2
United States	7.0	-6.3	4.0	4.3	13.9	18.8	-13.7	-4.5
Europe	6.8	-5.3	3.7	4.9	11.0	16.5	-12.7	-14.3
Japan	3.8	-4.0	1.4	1.0	6.8	8.0	-14.2	-12.6
Emerging Markets	6.3	-7.2	2.1	0.7	10.0	10.8	-7.4	-14.2
Asia Pac Ex Japan	6.4	-6.9	1.8	0.8	11.5	12.4	-8.8	-13.7
Asia Ex Japan	6.7	-8.5	1.9	-0.6	11.4	10.8	-8.6	-14.1
Latin America	6.2	-2.0	0.5	4.6	7.9	12.9	0.5	-6.2
Brazil	6.2	1.7	-0.7	7.2	8.2	16.0	13.6	-0.2
EMEA	5.9	-3.6	5.2	7.4	5.6	13.4	-4.0	-15.5
	Jun-19	**May-19**	**Apr-19**	**Q2 19**	**Q1 19**	**YTD**	**Q4 18**	**2018**
Australia	5.3	0.7	1.2	7.4	11.4	19.6	-10.0	-11.8
New Zealand	5.3	-1.9	0.7	4.0	16.9	21.5	-6.5	-3.5
Hong Kong	7.0	-6.7	1.1	1.0	15.6	16.8	-4.5	-7.8
China	8.1	-13.1	2.2	-3.9	17.7	13.1	-10.7	-18.7
Korea	8.9	-9.3	0.4	-0.9	5.0	4.1	-12.8	-20.5
Taiwan	5.5	-7.8	4.0	1.1	9.0	10.2	-13.7	-8.2
Thailand	9.6	-2.1	2.0	9.4	7.5	17.7	-10.2	-5.3
Malaysia	2.9	-0.7	-1.0	1.2	0.3	1.5	-5.8	-6.0
Singapore	10.3	-8.8	6.3	7.0	6.2	13.6	-6.7	-9.4
Indonesia	5.5	-2.6	0.9	3.7	4.3	8.1	9.8	-8.7
India	-0.3	0.2	0.6	0.5	7.2	7.7	2.5	-7.3
Philippines	2.2	0.8	1.5	4.6	8.0	13.0	5.4	-16.1
	Jun-19	**May-19**	**Apr-19**	**Q2 19**	**Q1 19**	**YTD**	**Q4 18**	**2018**
Mexico	3.5	-7.0	5.2	1.3	5.6	6.9	-18.7	-15.3
Chile	5.8	-8.4	-1.9	-4.9	4.4	-0.7	-8.6	-18.9
Hungary	-0.8	-4.5	1.3	-4.1	6.0	1.7	5.9	-6.1
Poland	6.7	-4.2	1.3	3.6	-0.6	3.0	-2.9	-12.5
Czech Republic	4.9	0.2	-1.2	3.9	3.8	7.9	-8.7	-2.2
Russia	9.0	3.6	3.8	17.3	12.2	31.6	-8.5	0.5
Turkey	7.6	-0.6	-3.6	3.1	-3.0	0.0	4.8	-41.1
South Africa	6.3	-7.1	8.1	6.8	4.6	11.7	-3.7	-24.3
Qatar	1.0	-5.3	5.3	0.6	-3.5	-2.9	8.4	29.8
Saudi Arabia	3.2	-8.7	7.6	1.4	14.9	16.5	-0.7	19.2
United Kingdom	5.0	-6.0	2.3	0.9	11.9	13.0	-11.8	-14.1
Germany	7.4	-6.1	7.0	7.8	7.0	15.4	-15.5	-21.6
France	8.6	-5.6	4.8	7.3	10.8	18.9	-15.0	-11.9
Netherlands	6.5	-6.0	5.9	6.1	13.6	20.5	-11.0	-12.8
Austria	5.5	-8.0	6.2	3.1	8.6	11.9	-18.9	-23.2
Italy	9.9	-7.7	2.2	3.6	14.7	18.9	-11.8	-17.0
Spain	4.9	-6.1	4.4	2.9	7.1	10.2	-8.5	-15.7

Source: Thomson-Reuters Datastream, MSCI. All data Total Returns, in US dollar terms, as of 30 June 2019

KEY TERMS	
CA	Current Account
CBR	Central Bank of Russia
COPOM	Central Bank of Brazil
CPI	Consumer Price Index
DM	Developed Markets
ECI	Employment Cost Index
EM	Emerging Markets
EM Currencies	MSCI Emerging Markets Currency Index
EM Equities	MSCI Emerging Markets Index
EM Local Currency Bonds	JP Morgan Emerging Local Currency Bond Index
EM USD Bonds	JP Morgan Emerging Market Bond Index
EMU	European Monetary Union
EU	European Union
Fed	The Federal Reserve Board of the United States
FOMC	Federal Open Market Committee
GDP	Gross Domestic Product
Global Developed Equities	MSCI Developed Markets Index
Global Equities	MSCI All Country World Index
Global Government Bonds	Citigroup World Government Bond Index
IP	Industrial Production
M2	M2 Money
mom	Month on month
PBoC	Peoples Bank of China
qoq	Quarter on quarter
Repo	Repossession
SDRs	Special Drawing Rights
SELIC	Sistema Especial de Liquidação e CU.S.todia (SELIC) (Special Clearance and Escrow System)
Tankan	Japan Large Business Sentiment Survey
TSF	Total Social Financing
UK	United Kingdom
yoy	Year on year

REPRESENTATIVE INDICIES	
Aluminum	S&P GSCI Aluminum Index
Asia Local Bond (ALBI)	HSBC Asia Local Bond Index
Brent Oil	Cash settlement price for the InterContinental Exchange (ICE) Brent Future based on ICE Futures Brent index
Commodities	Datastream Commodities Index
Copper	S&P GSCI Copper Index
EMU 10 Year	Datastream EMU 10 Year
Global Emerging Bond	JPM Global Emerging Bond Index
Gold	S&P GSCI Gold Index
Japan 10 Year	Datastream Japan 10 Year
JACI	JP Morgan Asia Credit Index
MSCI Dev World	MSCI Developed Markets Index
MSCI EM	MSCI Emerging Markets Index
MSCI Europe	MSCI Europe Index
MSCI Japan	MSCI Japan Index
MSCI Latam	MSCI Latin America Index
MSCI Russia	MSCI Russia Index
MSCI U.S.	MSCI U.S. Index
MSCI World	MSCI All Country World Index
Steel (HRC)	TSI Hot Rolled Coil Index
UK 10 Year	Datastream UK 10 Year
U.S. 10 Year Treasuries	Datastream U.S. 10 Year Treasuries
U.S. 30 Year Treasuries	Datastream U.S. 30 Year Treasuries
U.S. High Yield	BAML U.S. High Yield Constrained II
U.S. Investment Grade	BAML Corporate Master
DXY	U.S. Dollar Index
Zinc	S&P GSCI Zinc Index

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