EDMOND DE ROTHSCHILD

MARKET FLASH: LOOKING FOR THE RIGHT TEMPO

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• Admittedly, there are no glaring signs of weakness in recent US economic data even if inflation continues to recede.

• Amid reduced visibility, we have tactically reduced exposure to risk assets. Risk premiums are too low to cope with any disappointment over the disinflation scenario.

Central banks have refocused markets on the pace of future rate cuts. Traders now only expect three cuts by the end of 2024 rather than the six they were hoping for in January. Some are even querying this new scenario: as a result, the dollar rose and real 10-year yields moved back to 2%.

Admittedly, there are no glaring signs of weakness in recent US economic data even if inflation continues to recede. The labour market is particularly strong. The ADP survey said 184,000 new jobs were created in March, JOLTS data backed up this trend and wages rose 10% for people changing jobs. The result has been conflicting comments from Fed officials over the timing of the first rate cut.

Higher rates are fuelling fears that the US deficit will run out of control. Both presidential candidates have no appetite for budgetary discipline: they have plans to cut taxes and Donald Trump might introduce new import levies. Nevertheless, we believe disinflation has further to go and the trend for interest rates is still downwards.

In Europe, overall inflation fell faster than expected to 2.4% but core inflation remained high at 2.9% due to services holding up. European PMI rebounded and moved back above 50 to 50.3 but Germany and France remained in contraction territory at 47.7 and 48.3, respectively.

In Asia, the PMI rebound was more pronounced, especially in China, Japan and Australia. However, ISM in the US and Canadian PMIs missed expectations.

Today's global manufacturing rebound, geopolitical tensions and concerns over sticky inflation have triggered strong sector rotation out of growth stocks and higher oil prices. The banks sector is playing catch up, now that the Credit Suisse drama has been digested and energy stocks are rising.

Amid reduced visibility, we have tactically reduced exposure to risk assets. Risk premiums are too low to cope with any disappointment over the disinflation scenario. We continue to prefer bond market yields and remain overweight duration.

EUROPEAN EQUITIES

Markets fell sharply, putting an end to a string of gains which began in February. Government bond yields, led by Germany's 10-year Bund, retreated slightly when eurozone inflation fell from 2.6% in February to 2.4% in March, or better than the 2.5% expected. But upbeat economic data do not augur well for a rate cut soon and are weighing on risk appetite. Fresh geopolitical tension, especially in the Middle East, is another negative. Brent crude moved above $90 for the first time in 6 months after an OPEC meeting decided to increase production cuts.

Energy naturally led gains thanks to higher oil prices. Banks also benefited from this new scenario of fewer rate cuts and at a reduced pace. The property sector, however, sold off due to its interest rate sensitivity.

UBS has been doing well since buying **Credit Suisse** last year and this week launched a share buyback programme for up to $2 billion, but should be limited to $1 billion, according to the bank..

Solutions30 (digital support) posted full-year results which revealed a marked improvement in profitability in the second half. The figures were much better than expected. Adjusted EBITDA for 2023 jumped 59.6% to €74.6m vs. €66m expected. The adjusted EBITDA margin rose 1.9 points to 7.1% vs. 6.3% expected. Despite these excellent figures, the share fell as Belgium is about to hold elections. The polls are expected to slow the fibre rollout temporarily and fibre is a big market for the company.

Voltalia, in contrast, jumped by close to 10% after 2023 EBITDA came in at €241m or better than the €238m expected. The group is upbeat for this year. Management sees capacity rising 16% to 3.3GW in building and operations, of which 2.5GW in operations.

US EQUITIES

In a relatively thin week for company news, negative geopolitical developments poured cold water on bullish sentiment. After 26 weeks of almost non-stop rises, markets experienced their first correction. The S&P 500 lost 2% over the period, with most of the damage done on Thursday afternoon due to mounting tensions in the Middle East . Brent crude rallied further, adding 3.6% and gold gained 1.8%, reclaiming its safe haven status.

Elsewhere, consumer demand appeared to be softening. **Ulta Beauty**, the largest beauty product chain in the US, issued a profit warning after a dip in sales since February. The news dragged down other stocks in the sector. **Coty** tumbled 6%. Even **Procter & Gamble**, which is positioned in consumer staples, fell 4%. Jobs data, however, remained upbeat. ADP said 184,000 jobs were created in March, or significantly more than the 140,000 expected.

Chip giant **Intel** plunged after posting a higher-than-expected $7bn loss in its foundry business.

EMERGING MARKETS

The MSCI EM Index was up 0.57% this week as of Thursday. Both **China** and **India** gained 1.1%, while **Brazil** underperformed by falling 0.74%.

In **China**, Manufacturing PMI increased to 50.8 in March from 49.1 in February. Non-manufacturing PMI rose to 53.0 from 51.4. Both readings were ahead of expectations. Caixin Composite PMI was 52.7 vs. 52.5 in February. The NDRC held a meeting with six corporations on equipment renewal and consumer goods replacement. The government introduced a new auto loan policy to boost consumption. On the geopolitical front, Treasury Secretary Janet Yellen arrived in **Guangzhou** to kick off her **China** trip. Beijing scrapped anti-dumping and anti-subsidy tariffs on Australian wine. **Xiaomi** launched a sedan EV and received more than 100,000 orders in only 24 hours. **Moutai** reported a fourth-quarter beat driven by strong top-line growth and gross margin expansion. 40% of MSCI China companies had reported their fourth-quarter results as of this week and aggregate revenues were up 7% YoY, a notable improvement on the 2% drop in the third quarter. Earnings were up 2% this quarter and in aggregate beat consensus estimates by 14%, the best ever performance in the past 2 years.

In **Korea**, March exports were up 3.1% YoY with semiconductor exports at a record high: +35% YoY. The president met the leader of striking junior doctors in an attempt to end walkouts. **Samsung's** first-quarter operating results were better than expected thanks to better memory chip prices.

In **India**, Services PMI continued to inch up to 61.2 in March vs. 60.3 in February. Manufacturing PMI remained strong at 59.1, taking composite PMI to 61.8 vs. 61.3 in the previous month. March power generation (ex-RE) was up 8% YoY and the Ministry of Power (MoP) estimates peak demand will reach 256-260GW in April-June 2024. System credit growth (adjusted for the **HDFC** merger) was strong at 16.5% YoY as of February 2024 (vs. 16.2% in January). **Dixon** is in talks to buy a majority stake in the local phone-making unit of China's **Transsion Holdings**. UltraTech announced two new greenfield capacities of 5.2mnt

In **Brazil**, total credit growth showed some improvement in March, driven by private banks. **Hapvida** posted a 104.8% jump in its adjusted net profit for the fourth quarter on a better net add and medical loss ratio.

CORPORATE DEBT

CREDIT

In a holiday-shortened week, risk-free rates continued to rise. US data and Jerome Powell's statements seem to be saying that there is no rush to cut rates. Yields on 10-year US Treasuries retested recent highs, gaining 15bp to 4.32% by Thursday evening. Yields on the equivalent German Bund gained 8bp to 2.35%.

Trading was quiet on credit markets following the previous week's events around companies like **SFR** and **Ardagh**, both of which stabilised this week. Spreads were stable and even slightly tighter at 296bp on the Xover and 110bp in investment grade. High yield spreads were stable at 360bp.

New issuance remained active but with less volume after 2 months of mega deals. **Vonovia**, **Valeo** and **Terna** issued hybrid bonds. Order books remained strong and coupons tightened due to strong demand.

Between March 28 and April 4, IG returned 0.08%, taking YTD gains to 0.47%. High yield edged 0.12% higher and is now up 1.73% since the beginning of 2024 thanks to spreads proving very resilient.

CONVERTIBLES

After an upbeat March, the convertibles market started April in a more cautious mood ahead of the first-quarter results. For the time being, traders are still focusing on macroeconomics and central bank statements.

Financials continued to rally. **BNP Paribas** has now gained more than 20% since its mid-February low. Energy added another 5% this week as WTI oil prices moved above $85. **Total Energies** jumped more than 6% over the week.

After more than $9bn in new issuance in March, the primary market was subdued. There was just one small deal from Switzerland's **Medartis** which raised CHF 115m at 3% due 2031 and with a 27.5% premium.

GLOSSARY

• Investment Grade: bonds rated as high quality by rating agencies.

• High Yield: corporate bonds with a higher default risk than investment grade bonds but which pay out higher coupons.

• Senior debt benefits from specific guarantees. Its repayment takes priority over other debts, known as subordinated debt.

• Debt is considered to be subordinated when its redemption depends on the earlier payment of other creditors. To offset the higher risk, subordinated Senior debt has priority over other debt instruments.

• Tier 2 / Tier 3 : subordinated debt segment.

• Duration: the average life of a bond discounted for all interest and capital flows.

• The spread is the difference between the actuarial rate of return on a bond and the rate of return on a risk-free loan with the same maturity.

• The so-called "Value" stocks are considered to be undervalued.

• Markit publishes the Main iTraxx index (125 leading European stocks), the HiVol (30 highly volatile stocks), and the Xover (CrossOver, 40 liquid and speculative stocks), as well as indices for Asia and the Pacific.

• EBITDA: Earnings before Interest, Taxes, Depreciation, and Amortization.

• Quantitative easing describes unorthodox monetary policy from a central bank in exceptional economic conditions.

• Stress Test: a process which simulates extreme but possible economic and financial conditions so as to assess any impact on banks and measure their resilience to these events.

• The PMI, for "Purchasing Manager's Index", is an indicator of the economic state of a sector.

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EDMOND DE ROTHSCHILD ASSET MANAGEMENT (FRANCE)

47, rue du Faubourg Saint-Honoré 75401 Paris Cedex 08

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332.652.536 R.C.S. Paris