EDMOND DE ROTHSCHILD

MARKET FLASH: COMPANY RESULTS DISAPPOINT INVESTORS

- ***Joe Biden withdraws from the presidential race in favor of Kamala Harris, introducing uncertainty into the campaign.***
- ***US GDP grows by 2.8% in Q2, reducing the chances of a Fed rate cut in the short term.***
- ***Disappointing results (Tesla, Alphabet, LVMH, Ryanair) lead to a correction in equity markets.***

The week's big event was Joe Biden's decision to withdraw from the presidential race and back Kamala Harris. The vice president was gratified by an immediate surge in funding and support from a large majority of Democrat party delegates. She should be officially declared as candidate at the beginning of August. This switch caused some uncertainty over the election's result, previously considered as very much in Donald Trump's favour. It also raised questions over economic scenarios, and especially Trump's plans for import duties.

Meanwhile, in France, Emmanuel Macron postponed a decision on appointing a prime minister until after the Olympic Games, despite the NFP coalition finally choosing a candidate, Lucie Castets. MPs from the France Unbowed party said they would put forward a bill to cancel last year's Pension Reform Act. The National Rally is also in favour so the possibility it would get approval sent the OAT-Bund spread 5bp higher.

Elsewhere, US economic data stayed mixed. Labour market and inflation data were still trending in line with inflation moving towards the 2% target and growth looking stronger than expected. GDP rose by an annualised 2.8% in the second quarter, or more than the 2% expected, so expectations of a Fed rate cut next week fell. A cut is still seen as possible in September especially as Canada's central bank cut its rates by 25bp this week.

Europe's PMI came in lower than expected, largely due to Germany underperforming as a result of its dependence on China. Worries resurfaced after China's stimulus measures were judged insufficient. The PBoC's 10bp rate cut was seen as proof that the outlook was bleak. The Eurozone composite index nevertheless stayed in positive territory, coming in at 50.1, up from 50.9 previously and 50.9 expected. This chimes with the scenario of gradual ECB cuts.

The Yen gained ground over the week on expectations of Bank of Japan support amid inflation worries.

Equity markets fell due to disappointing reports from companies like Tesla and Alphabet in the US and LVMH and Ryanair in Europe.

We have gone tactically overweight global equities ahead of the Fed's move to cut rates in the fourth quarter. We are still upbeat on fixed income and especially medium-term maturities. We prefer US corporate debt to Euro credit.

EUROPEAN EQUITIES

Indices ended the period slightly higher. With more than 25% of European company figures now in, and expectations for equity per share growth of 5% on average, many companies disappointed expectations. Soft consumer spending is weighing on cyclical sectors. But composite PMI came in at 49.5 vs the 48.8 expected, so there are grounds for optimism. And the ECB's vice chair said wage moderation made him confident of a rate cut in September. The cut is now almost fully discounted and bond yields have fallen.

Highly cyclical sectors suffered the most over the week. **Ryanair**'s poor figures impacted travel and leisure which was the worst performing sector. Autos were next after results at **Stellantis** and **Renault** suffered from weak demand. Even a premium brand like **Porsche** failed to perform. Tech was again under attack following last week's sell-off. **STMicroelectronics**, which has high auto industry exposure, was the worst performing stock.

In contrast, interest rate sensitive sectors like utilities and banks performed well. And healthcare topped returns thanks to **Indivior**, **Lonza** and **Sartorius**.

Ryanair's results were particularly worrying. Profits at the low-cost airline tumbled after prices were slashed by 15% on average over a year in an attempt to boost demand. Like other airlines, Ryanair also had to contend with plane delivery problems and the recent IT outage caused by a **CrowdStrike** software update. Ryanair's figures hit the entire sector even if other airlines were less affected by these issues. **EasyJet**, for example, initially sold off before its figures eventually reassured traders. The UK airline is shaping up for a record summer on strong demand. Close to 75% of seats for the fourth quarter have already been sold. It helps that EasyJet is still managing to keep costs under control, especially with fuel costs trending lower.

LVMH's results fuelled sector-wide concerns. Persistently weak demand in China led to sales of €20.98bn in the second quarter, or less than the €21.55bn expected. EBITDA for the first half of 2024 was €10.62bn, also short of the €11.12bn expected. All divisions were affected and notably watches and jewellery. Kering was dragged down even before the group reported but its figures ended up telling the same story.

US EQUITIES

Wall Street had another bad week with the Nasdaq tumbling by more than 3%. Wednesday's fall was the biggest since 2022. Meanwhile, markets continued to move away from stock polarisation and the Russell 2000 ended the period 2% higher. Semiconductor and electrification plays as well as **Nvidia** galaxy stocks were the biggest casualties.
During the week, 39% of the S&P 500 index reported results, most of them largely positive with equity per share growth running at 10.4% in the second quarter.

Google's figures were upbeat but the outlook for operating margins in the current quarter was less encouraging. In addition, YouTube's advertising revenue growth decelerated sharply. **Tesla's** gross margin and free cash flow generation missed expectations. And 20% of the quarter's profits came from selling carbon credits. Payment giant **Visa** dipped after volume growth decelerated in the second quarter and in July. However, **ServiceNow** jumped after its results as the group is one of the few companies to have successfully monetised AI.

The **Nasdaq** exchange also did well, beating expectations in each segment thanks to successful cross-selling and solid progress in integrating Adenza. In the autos sector, **GM** reported robust figures and also unveiled a stock buyback programme.

But **Ford** disappointed investors by not going for a buyback; the group prefers to invest more in its unprofitable EV division.

Onshore results at **Halliburton** were disappointing and the group now expects to see less revenue growth in North America this year. However, the outlook for 2025 is rosier thanks to expectations for a natural gas rebound. In similar vein, **Patterson's** second-quarter revenues missed slightly but drilling margins came in better than expected.
In healthcare, **Boston Scientific** reported exceptional results and upped guidance on full year profits by close to 14%. The results were due to successful attempts in recent years to rebalance the portfolio.

EMERGING MARKETS

The MSCI EM index was down by 0.24% in USD this week as of Thursday. Brazil, Mexico and Korea led declines, down 1.19%, 0.88% and 0.37% respectively. China and Taiwan slipped 0.13% and 0.02%. India was more or less flat (+0.03%).

In **China**, the PBoC cut the 1-year MLF rate by 20bp and injected RMB 200bn, a dovish surprise following a 10bp OMO rate cut on Monday. The MOF and NDRC said that RMB 300bn in ultra-long treasury bonds would be allocated to support equipment upgrades and consumer goods purchases. Beijing will finance 90% of the amount while local governments will provide the remaining 10%. **SAIC motor** plans to launch a Robotaxi service in Shanghai by August after receiving license approval this week. **Baoshan steel** doubled its investment in a joint venture with **Aramco** to $1bn.

In **Taiwan**, June export orders rose 3.1% YoY, or below the 12.3% expected. The unemployment rate for June was in line with the 3.34% expected. **TSMC** expects that fabs in Taiwan will maintain normal production despite the possible impact of Typhoon Gaemi. **Hon Hai** is reportedly actively hiring employees for its Chengchow plant for iPhone 16 production and raising wages by 20%.

In **Korea**, 2Q24 GDP growth was 2.3%, or lower than the 2.5% expected. Exports rose by 18.85% YoY in the first 20 days of July, led by robust chip sales. The government published its final tax reform plans to drive its Value-Up initiatives. **SK Hynix** posted its highest quarterly profit since 2018 on strong AI chip demand. The company expects to more than double HBM shipments next year. Quarterly results at **Hyundai Motors** were in line and margin guidance was unchanged. **Samsung Electronics** started mass production of 8-layer HBM3 chips after obtaining **Nvidia**'s qualification.

In **India**, the newly formed government unveiled the budget for this financial year, reducing the fiscal target from 5.1% to 4.9% while maintaining overall capex growth at 16% YoY. The RBI presented a draft LCR with notably a higher runoff for retail deposits. **HDFC Bank** delivered better-than-expected results with NIM improvement on a lower cost of funding. **Reliance** reported a miss on weak retail trading. **Hindustan Unilever** had a better-than-expected quarter, driven by a rural demand recovery and market share gains. Results from **Axis Bank** and **Bajaj Finance** missed on higher credit costs.

In **Brazil**, IPCA-15 inflation grew 4.45% YoY in June, or higher than the 4.37% expected. The current account deficit deteriorated further to 4bn vs 3.4bn in the previous month. **Hapvida** signed a memorandum of understanding with **Riza** to finance two new hospitals. **Vale** posted second-quarter results that slightly missed estimates on higher expenses.

In **Mexico**, July inflation came in at 5.61%, or well above consensus, driven by higher food inflation and sticky high service inflation. Retail sales for May rose 0.3% YoY, or less than the 2.3% expected. **Banorte** reported mixed results on lower NII and higher credit costs although loan growth was 13% YoY, an improvement on the previous quarter. Results from **Gentera** also missed expectations on higher credit costs.

CORPORATE DEBT

CREDIT

Credit markets continued to make slight gains. Investment grade returned 0.33% (+1.74% YTD) while High Yield edged 0.02% higher (+3.81% YTD). The segment largely brushed off the US equity rotation and the by Nasdaq's decline. Bond yields tightened by 3-4bp while Investment Grade spreads were stable. High Yield spreads widened by 3bp.

Demand for fixed income is still strong – Investment grade took in €1.1bn and High yield €416m – and yields are still very attractive compared to the last 10 years. Investment grade is currently yielding 3.55% and High yield 5.91%.

Spreads in financials continued to tighten, especially in Euro CoCos due to no new issuance and buy-ins at the first available date. This week, **HSBC** and **Swedbank** announced buybacks for AT1 debt which is callable in September 2024. 2024 has so far been devoid of incidents. With August looming, new issuance has practically dried up and fund flows are lower. The ongoing earnings season is looking upbeat with companies raising guidance and the outlook for 2025 -and even 2026- is still positive.

In high yield, France's **Constellium** (aluminium products) sold a euro-denominated 2032 maturity at 5.375% to refinance existing debt. Investors remained focused on second-quarter results. High-yield company results were muted and there were signs of a slowdown in the retail, autos and consumer discretionary sectors. In contrast, healthcare, telecoms and some industrial plays continued to perform well.

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.

• AT1s belong to a family of bank capital securities known as contingent convertibles or "Cocos". Convertible because they can be converted from bonds to shares (or depreciated entirely) and contingent because this conversion only occurs if certain conditions are met, such as the issuing bank's capital strength falling below a predetermined trigger level.

• RT1 (Restricted Tier 1) are perpetual subordinated debt securities redeemable between five and ten years after issue. They are issued by insurers under Solvency II regulations.

• Perpetual non call 10years is a perpetual bond and its first call date is 10 years away.

DISCLAIMER

This is a marketing communication.

26/07/2024

This document is issued by the Edmond de Rothschild Group. It is not legally binding and is intended solely for information purposes. This document may not be communicated to persons located in jurisdictions in which it would be considered as a recommendation, an offer of products or services or a solicitation, and in which case its communication could be in breach of applicable laws and regulations. This document has not been reviewed or approved by a regulator of any jurisdiction. The figures, comments, opinions and/or analyses contained herein reflect the sentiment of the Edmond de Rothschild Group with respect to market trends based on its expertise, economic analyses and the information in its possession at the date on which this document was drawn up and may change at any time without notice. They may no longer be accurate or relevant at the time of reading, owing notably to the publication date of the document or to changes on the market. This document is intended solely to provide general and introductory information to the readers, and notably should not be used as a basis for any decision to buy, sell or hold an investment. Under no circumstances may the Edmond de Rothschild Group be held liable for any decision to invest, divest or hold an investment taken on the basis of these comments and analyses. The Edmond de Rothschild Group therefore recommends that investors obtain the various regulatory descriptions of each financial product before investing, to analyse the risks involved and form their own opinion independently of the Edmond de Rothschild Group. Investors are advised to seek independent advice from specialist advisors before concluding any transactions based on the information contained in this document, notably in order to ensure the suitability of the investment with their financial and tax situation.

Past performance and volatility are not a reliable indicator of future performance and volatility and may vary over time, and may be independently affected by exchange rate fluctuations.

Source of the information: unless otherwise stated, the sources used in the present document are those of the Edmond de Rothschild Group. This document and its content may not be reproduced or used in whole or in part without the permission of the Edmond de Rothschild Group.

EDMOND DE ROTHSCHILD ASSET MANAGEMENT (FRANCE)

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

Société anonyme governed by an executive board and a supervisory board with capital of 11.033.769 euros

AMF Registration number GP 04000015

332.652.536 R.C.S. Paris