EDMOND DE ROTHSCHILD

MARKET FLASH: BONDS ARE BACK IN FAVOUR

• The US Congress has reached an agreement, thus avoiding a government shutdown.

• During his first visit to the US in 6 years, Chinese President Xi Jinping agreed, along with US President Joe Biden, to improve the management of tensions between the world's two largest economies.

• The Fed's decision to hold rates steady at the beginning of the month prompted us to make tactical increases to our equity weightings. Ebbing inflation in the US, notably within the housing market (one third of the CPI, which was slow to ease) and lower yields should support the rebound of risk assets going forward.

The US Congress has reached an agreement, thus avoiding a government shutdown. The plan put forward by the Republican Speaker, Mike Johnson, is to fund some parts of the government through to January 19th and others through to February 2nd. However, this good news should not elude the deeper issue: the Congressional Budget Office (CBO) expects an annual 6% deficit until 2033, and ratings agency Moody's has lowered its outlook on the U.S. credit rating to negative. If the Supreme Court had allowed the government to wipe student debt (its refusal to do so effectively prevented $379 billion of additional spending for the Treasury), the US deficit would have doubled between 2022 and 2023, reaching 7.5% of the country's GDP. Despite full employment and resilient growth, government spending has increased due to inflationary pressures (pension and healthcare cost reassessments), rising interest rates - which are adding to the debt burden, IRA-related subsidies, and military expenses in Ukraine and now the Middle East.

US bonds benefited from the ebb in inflation published on Tuesday and from the latest economic data pointing to a gradual slowdown in the country. Slowing retail sales, declining industrial output, and mixed business confidence survey results dragged oil prices to below $73. In this environment, consensus estimates suggest that the Federal Reserve will not raise its interest rates any further; yield curves are now expecting a 100 bp cut to key rates in 2024, thereby putting an end to the most aggressive interest rate hiking sequence seen in decades. After peaking at 5% at the end of October, yields on 5 and 10-year bonds both fell 60 bp to below 4.40%.

Easing yields and strong earnings publications in the US enabled equity markets to rebound. While analysts were expecting a 0.5% drop in earnings, they were positively surprised by the 4%+ growth in EPS. We therefore expect profitability levels to be just as high in 2023 as they were in 2023 for US companies, driven by the technology, cyclical consumer spending and financial industries. Analysts are now expecting earnings growth of +11% in 2024, despite the weaker macro outlook.

During his first visit to the US in 6 years, Chinese President Xi Jinping agreed, along with US President Joe Biden, to improve the management of tensions between the world's two largest economies. This geopolitical appeasement is welcome in China, where the property slump is worsening despite the government's efforts to rekindle demand: after declining transaction volumes, housing prices are now floundering. The new stimulus measures

implemented in large cities since August have so far failed to revitalise the sector, which is weighing on China's economic recovery.

The Fed's decision to hold rates steady at the beginning of the month prompted us to make tactical increases to our equity weightings. Ebbing inflation in the US, notably within the housing market (one third of the CPI, which was slow to ease) and lower yields should support the rebound of risk assets going forward. We remain positive on duration, which can protect our investments in the event of geopolitical setbacks or an economic slowdown.

EUROPEAN EQUITIES

After the rather lackluster past week, with investors drawn between positive corporate earnings and growing pressures caused by sovereign yields, this week is proving much brighter with central banks playing a major role in stock market performances. Analysts are scrutinising macroeconomic data, including inflation readings and notably the US CPI published on Tuesday, which pointed to a slight retreat and caused sovereign yields to tumble. Furthermore, the prospects of an escalation in the conflict in the Middle East seem increasingly remote now that Teheran has stated it would not engage in the conflict.

These factors are rekindling investor confidence, as reflected in the positive market performances recorded this week. Consequently, the vast majority of index sectors posted positive returns. The main winners were basic resources and real estate, lifted by the respite on interest rates, while energy was the only sector to deliver negative performances, impacted by the sharp drop in the price of Brent oil.

On the microeconomic side, French industrial champion **Alstom** seems under increasing pressure after announcing asset sales to slash its debt, while also considering a highly dilutive capital increase if these sales prove insufficient. Meanwhile, the group has also announced plans to cut 1,500 jobs (10% of its headcount). This unwelcome news for investors triggered a major sell-off. On a much more positive note, French car builder **Renault** unveiled the roadmap for its **Ampere** project, an entity dedicated to electric vehicles and software, with an IPO planned for H1 2024. **Ampere** aims to achieve price parity for combustion and electric vehicles by 2027/2028 through a range of 7 vehicles to be launched by 2031 across the European continent. According to **Bloomberg**, **Sanofi** has begun discussions with **R&Co** on plans to spin out its consumer healthcare division. The market value of the latter could exceed $20 billion. Several private equity players seem interested in a potential takeover, and the group is keen to be advised by other banks on the completion of the deal.

In the UK, **Burberry** shares tumbled during the week, affected by the global economic slowdown - a further sign that flagging luxury spending is weighing on the sector.

In Germany, chipmaker Infineon surged after reporting better-than-expected earnings, confirming that demand for semiconductors remains robust, notably from the electromobility and renewable energy industries - particularly in China. Finally, the industrial giant **Siemens** reported its Q4 earnings, with no major surprises, but excellent data including a 4%+ growth in revenue for Q4 2022/23: €21.39 billion versus €20.99 expected. Generally speaking, all of the group's divisions delivered earnings slightly above expectations, particularly digital industries after the firm's software business performed particularly well.

US EQUITIES

US equity markets were upbeat this week following the publication of weak macroeconomic indicators which raised the odds of a soft-landing scenario for the US economy. The Consumer Price Index for october came in lower than expected (stable, versus +0.1% estimated).

Meanwhile, weekly unemployment claims rose to 231K (versus 220K expected), their highest level in 3 months, suggesting that pressure on the labour market is easing. As a result, yields on long-term US Treasuries retreated to 4.40% after peaking at 4.69% at the start of the week.

In this environment, the S&P, NASDAQ and Russell 2000 indices continued to enjoy a positive momentum and gained +3.79%, +4.31% and +5.20% over the past five trading sessions.

On the political front, the meeting between J. Biden and X. Jinping in San Francisco during the Asia-Pacific Economic Cooperation summit (APEC) was constructive for both parties.

Within the energy sector, the downward trend on oil prices is prevailing on signals of high US crude inventories and concerns over weak demand for energy in China. Crude oil prices (WTI) have dropped 5.83%, falling below the $75 threshold. Energy stocks have been impacted, with **Hess Corp** (-0.16**%), Halliburton** (-2.80%) and **Baker Hughes** (-3.40%) posting losses during the week.

With the distribution sector, **Home Depot** (+5.85%) rose after reporting better-than-expected sales, while also narrowing its full-year guidance, quoting the high interest rate environment. **Walmart** (-5.12%) suffered after publishing weaker-than-expected data for its US business.

Digital communications company **Cisco** (-8.06%) stumbled on slower orders for new products, having also reported disappointing estimates for the next quarter due to weaker corporate spending.

Within the automotive sector, tentative agreements on wage increases were signed following the strikes within the Detroit Big Three. **General Motors** workers (+2.88%) were the first to vote in support of the deal negotiated by the United Auto Workers Union (UAW). All eyes are now on the other members of the Big Three, namely **Ford** (+3.36%) and **Stellantis**.

Banking stocks benefited from easing bond yields, with **Bofa** and **Citigroup** up +7.30% and +7.64% respectively during the period.

We have noted that the earnings season is drawing to an end and that the pace of publications has slowed down.

Finally, the Senate has passed the funding bill that had been approved by the House of Representatives to secure the 2024 budget. This has avoided a partial federal government shutdown in the country.

JAPANESE EQUITIES

The NIKKEI 225 and TOPIX indices continued their ascent, gaining 2.38% and 1.43%, respectively. Japanese equity markets rallied, propelled by a significant drop in US government bond yields attributed to a weaker october US Consumer Price Index. This decline boosted investors' confidence in the expectation of interest rates reaching their peak.

Oil & coal products and non-ferrous metals sectors rose 13.34% and 5.11% respectively as major companies under these sectors announced solid results due to higher commodity prices including crude oil. Precision instrument sector gained 4.39% led by a sharp rise of **Terumo Corp**., a manufacturer of medical supplies, whose july-september operational profit beat the market consensus. On the other hand, pharmaceuticals sector fell by 2.05% as defensive stocks were generally sold in a risk-on market. Other products sector declined 1.01% mainly led by profit taking sales of **Nintendo Co**., **Ltd**. which rose sharply in the previous week. Air transportation sector decreased 1.00% by profit taking sales as well, as inbound tourism related stocks were bought in the previous week.

ENEOS Holdings Inc., a company mainly engaged in the energy business and oil & gas development business, rose by 11.9% as FY2023 net profit guidance was significantly revised upward. **Terumo Corp**. increased 11.03% due to the reason explained above. **Tokyo Electron Ltd**., a maker mainly producing semiconductor manufacturing equipment, gained 10.28% as high-tech related stocks were bought following the US equity market. Meanwhile, **Shiseido Co**., **Ltd**., a cosmetic company, lost 11.02% as FY2023 operational profit guidance was revised down. **Nitori Holdings Co**., **Ltd**., a company primarily engaged in the sale of furniture and interior goods, fell 6.38% as July-September 2023 operational profit missed the market expectation. **LY Corp**. declined 5.01% by profit taking sales as its share price rose sharply in the previous week.

In the foreign exchange market, the USD/JPY rate experienced volatility. It initially rose to the high-151s due to yen selling in a risk-on market and a temporary increase in US interest rates. Subsequently, the USD saw a decline to the low-150s following a sharp fall in US interest rates. Later, USD/JPY traded sideways and concluded at the high-150s after briefly advancing to the low-151s.

EMERGING MARKETS

The MSCI EM Index moved up 3.6% this week as of Thursday, ahead of DM markets with MSCI World +2.6%. Taiwan, Korea and Brazil outperformed other regions, rising 5.6%, 4.8% and 4.3% in USD term, respectively. China also rose 3.4% while India underperformed, +2.1%.

In China, october TSF data was weaker than expected despite strong bond issuance, the credit boost reflects fiscal stimulus starting to kick in while bank loans to the real economy remained subdued. Industrial production rose 4.6% yoy in october, in line with expectations, and retail sales grew 7% yoy slightly above 7% estimated. PBoC keeps 1-year MLF interest rate unchanged at 2.5%, and it plans to provide at least RMB1 trillon for urban village renovation and affordable housing programs. The double 11 shopping festival data showed consumer backdrop in China remains soft. On the geopolitical front, Biden and Xi meet at APEC for the first time in a year, with generally positive outcome including announce deal on fentanyl crackdown, AI cooperation, resuming high-level military talks, and increasing flights and visa processing. US andChina also aim to restart climate dialogue and agree to restart US-China energy efficiency forum. Internet companies reported their 3Q results, with **Tencent** and **JD**.**com** both beating the consensus on earnings. **Alibaba's** 3Q revenue was in line with expectations, while the spin-off of cloud unit was canceled due to US chip ban's impact. **Weibo** reported in line revenue and non-GAAP earnings beat expectation. **Tencent** Music also had broadly in line numbers with paying user quality better than expected.

Netease's profit was ahead of forecasts, on solid gross & operating margin expansion through mix shift.

In Taiwan, main opposition parties KMT & TPP confirm alliance against the incumbent DPP for the upcoming presidential election.

In Korea, **Hynix** plans W10trn capex for 2024, up 50% YoY, focusing on HBM capacity expansion.

In India, regulator asked banks to increase capital banks and NBFC to increase capital buffer for unsecured loans. Retail inflation drops to 4.87% in october. Deflation persists in WPI, at –0.52%, for the seventh straight month. Imports rose 12.3% yoy vs 15% decline in the previous month , led by gold, petroleum, and electronics while exports rose 6.2% yoy vs a decline of 2.6% previous month, led by pharmaceuticals and electronic. India's trade minister visited **Tesla** plant as Indian government is considering lowering import taxes on EVs. Union coal ministry plans to increase India's coal production to 1.4bn tonnes by 2027. **Hindustan Unilever** to onboard 1.3 million grocery stores on ONDC network. Authorities probe**Apple**, **Amazon** and **Alphabet** units on tax lapses.

In Brazil, President Lula confirmed the commitment to zero deficit target for next year's budget. **Natura** misses on top line and ebitda but becomes net cash after the sale of **Aesop** and confirms the sale of **Bodyshop**. **NuBank** reported good results, in line with expectations. **Anima** delivered good results driven by deleveraging.

In Chile, **SQM** miss consensus expectation driven by lower prices and volumes. Chilean banks reported their preliminary results for october, banks had a solid recovery in NII, especially for **Santander Chile**.

CORPORATE DEBT

CREDIT

The past week saw bond yields retreating sharply following the publication of the annualised CPI in the United States (3.2%), which highlighted the success of the restrictive policies implemented by central banks. With the job market also starting to show signs of weakness, yields on US 10-year treasuries fell 20 bp during the week, closing at 4.44% on thursday. In Europe, yields on 10-Year German bonds also dropped 15 bp, ending the day at 2.55%. Rather counter-intuitively, these lowering yields have had a positive effect on risk premiums.

Credit premiums have indeed factored in the retreating bond yields as highly positive news, as these will ease pressure on corporate refinancing costs. Within the HY segment, the crossover index contracted by 15 bp during the week, from 410 to 395 bp, breaching the 'psychologically important' level of 400bp, while cash premiums eased from 460 bp to 440 bp. A similar momentum was observed on higher ratings, with a contraction of almost 10 bp over the week, to 145 bp. This fresh appetite for risk also affected more junior debt within bank capital structures, as premiums on CoCos enjoyed a very strong rally during the week, rising by almost 150 bp (from 910 bp to 760 bp).

Following the primary issuances by **UBS** and **SG** last week, and amid a highly favourable environment, several issuers put investors' appetite to the test with new deals that were largely over-subscribed: **Barclays** raised $1.75 billion through an additional tier 1 bond bearing a coupon of 9.625%, with market demand for the bond exceeding 22 billion. Also within Cocos, **Santander** issued a dual-tranche perpetual bond: the first €1.3 billion tranche is callable in 5 years, and the second, for €1.2 billion is callable in 10 years. Combined demand for these bonds, bearing a coupon of 9.625%, was €9 billion. Within the T2 segment, **Bawag** issued a €400 million bond maturing in 2034, with a coupon of 6.75%. Finally, **Veolia** also took advantage of the favourable market conditions to issue a €600 million hybrid bond bearing a coupon of 6%, which continued to underline investors' interest for subordinated structures.

Lifted by rates and premiums, higher quality bonds gained +0.86% during the week (+4.2% YTD), while High-Yield bonds rose +0.64% (+7.5% YTD). Yields on the Investment Grade and High-Yield bond market currently stand at 4.2% and 7.4% respectively, and still offer attractive entry points for carry strategies. In terms of risk/return, we believe the strategy remains highly compelling as it allows us to build predominantly Investment Grade portfolios, returning gross yields of 4.75% over 5 years.

CONVERTIBLES

Lifted by strong consumer spending data in the US, the convertible bond market enjoyed a second consecutive weekly rebound. This report eased fears of excessive central bank tightening and supported the various drivers that contribute to the performance of convertible bonds: equities, credit, and duration.

Many issuers published their earnings this week: **Delivery Hero** was up over 15% this week after upgrading its GMV growth to 5% - 7% for 2023 and reporting positive FCF (free cash flow) for H2 2023.

In contrast, **HelloFresh** delivered a profit warning on weaker-than-expected sales growth and higher costs. However, this should not have a durable impact on sales growth and earnings in 2024.

In the US, cybersecurity firm **Palo Alto** reported lower-than-expected billings for Q1 and narrowed its full-year guidance. The company continues to display robust profitability.

This week saw only one primary issuance, with a 3-month mandatory from **Ni Source Inc**, a utility company providing natural gas transportation, storage, and distribution services, for a total $862 million.

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.

DISCLAIMER

This is a marketing communication.

17/11/2023

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