



MARKET FLASH: CONFIDENCE MAKES A TIMID RETURN

- *Opinion polls for the second round of France's parliamentary elections left investors feeling more confident as they forecast a significantly reduced score for the Rassemblement National.*
- *In the UK, Labour's landslide win was cheered by markets as the party has turned more centrist.*
- *Macroeconomic data has made us more confident about US rate cuts so we have increased US duration but are still cautious on French government debt. As for equities, we are still neutral pending better buying levels.*

In the US, labour market tensions continued to ease so inflationary pressure should fall, leaving the Fed free to cut rates this year. The job quits rate, a key component if wages are to stop rising, stabilised at 2.2% and job creations only amounted to 150,000, down from 157,000 before, and lower than the 165,000 expected. Wage growth also eased. Both manufacturing and services ISM came in below 50, another pointer towards slower growth. The Atlanta Fed's GDP Now indicators also continued to fall. As a result, 10-year Treasury yields fell by around 13bp. At the beginning of the week, they had risen as doubts rose over Joe Biden's capacity to maintain his bid for re-election. US data have made investors feel a little more confident and Jerome Powell's Sintra symposium speech recognised that disinflation was on track. That said, he added that other data, notably labour market statistics, would need to move before the Fed initiated monetary easing.

In the eurozone, June inflation fell to 2.5% YoY vs. 2.5% in May, while the service component remained at high level (+4.1 %, stable in June). Underlying inflation was unchanged at 2.9% but analysts were going for 2.8%. The figures suggest no change to monetary policy in July but the ECB had already said it expected the disinflation trajectory to be bumpier in coming months. ECB chair Christine Lagarde, speaking in Sintra, said progress had been made but that the battle against inflation would not be won before the end of 2025.

In France, opinion polls ahead of the second round of the parliamentary elections soothed investor nerves as they suggested a much reduced number of the Rassemblement national wins. This is due to some candidates standing down with the result that three-way play-offs have been reduced from 306 to 89 while four-way play-offs are down from 5 to 2. It now looks difficult for the RN to win the 289 seats needed to secure an absolute majority but the alternative could well be a fragile coalition. The OAT-Bund spread narrowed by around 15bp as election prospects for big-spending parties at both ends of the political spectrum fell but we expect it to stay around 70bp due to France's worsening finances. In the meantime, the CAC 40 and Eurostoxx both rallied, wiping out losses earlier in the week.

In the UK, Labour's victory also went down well with markets as the party has now become more centrist. The Footsie gained ground along with UK gilts.

As macroeconomic data now make us more confident about US rate cuts, we have upped US duration but we remain cautious on French government bonds. We are still neutral on equities and prefer to wait for better buying levels ahead of the results season.

EUROPEAN EQUITIES

Indices had a very good week as political risk in France eased following the first round results in France's parliamentary elections. The Rassemblement National did well but not as well as expected, assuaging worries over France's budget trajectory. As a result, the OAT-Bund spread tumbled to below 70bp after peaking above 80 when President Macron dissolved parliament. Quite logically, the CAC 40 outperformed other European indices as the market had fallen more in previous weeks. Indices like the SMI and FTSE which had acted as safe havens naturally underperformed.

Eurozone inflation slowed to 2.5% YoY, or below the 2.6% expected while underlying inflation stuck at 2.9%. Services inflation remained high at 4.1% ; the subject is a major concern for the ECB and could prove pivotal in discussions over future rate cuts.

Almost all sectors gained over the week except for healthcare which was dragged down by **Novo Nordisk** following comments from Joe Biden on US drug prices being too high. Banks and cyclicals like construction and materials quite naturally led gains as they had sold off after the elections were announced. Energy also gained due to a slight rebound in oil prices following renewed Middle Eastern tensions and the possibility that hurricane Beryl might damage infrastructure in the Gulf of Mexico.

Aixtron reported its second quarter results over the week. Markets were particularly impressed by guidance as the order book is at €176m, or 24% higher than consensus expectations thanks to the SiC division (58% of orders) and GaN (29%). Sales were in line at €123m and the gross margin was unchanged at 43-45%. However, the group said the overall outlook for its markets was softer and some deliveries had been put back to 2025.

Renault said that its Ampère EV unit would now use LFP (Lithium, Iron, Phosphate) batteries rather than the more expensive NMC (Nickel, Manganese, Cobalt) kind. The 20% reduction in costs should help the group compete more easily with Chinese competition. Renault's share price rose as most Western car makers fear the arrival of Chinese cars.

US EQUITIES

In another holiday-shortened week for Independence Day, the Nasdaq 100 gained 2.5% and the S&P 500 ended the period 1.3% higher. The market concentration syndrome returned in force this week.

After the previous week's attention-grabbing Biden-Trump debate, Joe Biden weighed in against GLM-1 drugs, accusing them of being too expensive. He appealed to **Eli Lilly** to cut prices.

Elsewhere, **Tesla** made a big comeback, adding to gains in previous weeks and managing to wipe out all the ground lost in 2024. The rally was driven by electrical vehicles (EV) delivery

figures which fell 5% to 444,000 but were better than the 411,000 expected. The news boosted the entire EV sector after a period of gloom.

After passing the Fed's stress tests on capital cushions, major banks said they were intending to raise dividends for the current quarter. **Bank of America** increased its quarterly dividend by 8%.

Manufacturing ISM fell to 48.5 in June from 48.7, a low reading which shows that industrial activity is still falling.

EMERGING MARKETS

The MSCI EM index was up 1.88% in USD this week as of Thursday. All major emerging market indices closed higher. Taiwan (+2.92%) and Brazil (+2.51%) led outperformers. China, Mexico, Korea and India advanced by 2.21%, 2.14%, 1.76% and 1.18%, respectively

In **China**, official manufacturing PMI for June was flat vs. 49.5 in May. Non-manufacturing PMI for June stayed in the expansionary zone at 50.5. Consumption tax reform is to be unveiled after the 3rd Plenum, which could benefit luxury goods and high-end services first. Beijing announced an increase in duty-free purchase limits for travellers entering China from Macau or Hong Kong. Shanghai granted licenses to several companies, including **Baidu's** autonomous driving subsidiary, for the demonstration application of the robo taxi. The European Union is drawing up plans to impose customs duties on cheap goods bought from Chinese online retailers including **Temu** and **Shein**. China is in talk with Switzerland to upgrade the free trade agreement. Several NEV brands reported strong June vehicle sales thanks to trade-in policies. The top 200 developers saw combined sales contraction of 14% YoY in June. **CATL** released new long-life power battery technology for logistics applications.

In **Taiwan**, manufacturing PMI increased to 53.2 in June vs. 50.9. CPI for June rose 2.42% YoY, or above the 2.30% expected. **Foxconn** will invest about \$551m in two new projects in Vietnam to produce smart entertainment products. **Compal Electronics** announced plans to build a factory in Poland to target automotive electronics customers.

In **Korea**, manufacturing PMI for June rose to 52.0 from 51.6 in May. Industrial production for May increased by 3.5% YoY vs. expectations of 3.1%. Exports in June grew 5.1% YoY vs. expectations of 4.4%. **Samsung Electronics** reported strong second quarter preliminary results, with a strong OP beat led by memory price strength. The company confirmed that the qualification process for HBM3E is still ongoing. **SK Hynix** announced plans to invest \$75bn in chips up to 2028. **LG Energy Solution** suspended construction of a battery production line for energy storage systems in its Arizona plant. **Samsung Biologics** won a \$1bn deal with a US pharmaceutical company.

In **India**, manufacturing PMI decreased slightly in June, but remained at a high 58.3 (vs. 58.5 in May). Manufacturing employment rose 54.1, its highest level since the start of the series. Services PMI increased to 60.5 in June from 60.2 in May, driven by new business and employment index. **Ultratech Cement** has purportedly renewed its efforts to acquire **Orient Cement**. **Reliance** is set to re-launch Chinese fast-fashion label Shein in the coming few weeks. **Tata Hitachi Construction Machinery** announced that it would invest Rs 200 cr in its two manufacturing plants. **GE T&D India** won a €26m order from Grid Solutions in Dubai.

In **Brazil**, finance minister Fernando Haddad announced an agreement to cut government expenses by up to R\$26bn in 2025. Manufacturing PMI for June inched up slightly to 52.5 vs 52.1 in May. Industrial production decreased in May by 1% YoY vs. expectations of 1.7%. **Enauta** is in discussions with **Petrobras** to buy the Urugua and Tambau oil and gas fields. **Eletrobras**

repurchased 46.8 million common shares and 7.03m class B preferred shares at the market price.

In **Mexico**, manufacturing PMI for June was 51.1 vs 51.2 in May. Gross fixed investments for April grew by 18.1% YoY vs. 3% in the previous reading. **Google** will set up a data center region in Querétaro to serve its cloud computing business.

CORPORATE DEBT

CREDIT

Worries that either extreme party might win an absolute majority abated after the first round of France's election results and the OAT-Bund spread retreated from a peak of 85bp to 67bp. Even so, it was still 20bp wider than before parliament was dissolved. Elsewhere, European PMIs reinforced the idea of a soft landing scenario. Yields on Germany's 10-year Bund were at 2.60% at Thursday's close, or 10bp higher than in the previous week.

As French political risk waned, credit markets rose and premiums narrowed sharply. The Xover, for example, had fallen below 300bp to 292bp as of Friday morning. And spreads on the investment grade segment narrowed to 108np, recovering all the ground lost previously. It was the same story with French bank debt. Some junior bank bonds had tumbled by 3 to 4 points but they rebounded sharply over the week. Overall IG yields remained at 3.9% as interest rate shifts offset premium movement, with high yield at 6.65%.

Between June 28 and July 4, investment grade returned 0.1% - thanks to resilient credit offsetting interest rates - and is now up 0.62% year to date. Note that strong spread performance has acted as a cushion for investment grade this year as sovereign bonds are down by close to 1.95% YTD. High yield advanced 0.33% over the week, making a strong contribution to overall returns. The segment has now gained 3.45% since January 1st.

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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05/07/2024

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

AMF Registration number GP 04000015

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