



MARKET FLASH: THE ECB COULD EASE ITS STANCE

- The ECB's governors are worried about soft eurozone growth and considering accelerating interest rate cuts to stimulate the European economy.
- In the UK, investors are concerned about the Labour government's intention to change budget rules to allow it to borrow more.
- In China, the initial enthusiasm following the rate cuts earlier this week has already fizzled out.

On the whole, this month's PMIs are reassuring. They suggest services are stabilising at high levels with a slight improvement in manufacturing, even if it is still in contraction territory. Euro area manufacturing PMI rose from 45.1 in September to 45.9, helped by Germany (42.6 vs. 40.6) and new orders in particular. The data lend support to our scenario, i.e. no recession in the eurozone but no significant rebound either.

The ECB's governors are worried about soft eurozone growth and are now discussing whether to take rates more quickly to below neutral levels to boost the economy. As a result, the possibility of a 50bp move when the ECB next meets on December 12 is being touted and short government bond yields are trending lower.

In the UK, activity is a little weaker but investors are more concerned about the Labour government's intention to change budget rules to allow it to borrow more. The project, a contrast with the government's bid for budgetary responsibility when it took office in the summer, sent government bond yields higher.

In China, the enthusiasm triggered by the 25bp cut in 1 and 5-year interest rates at the beginning of the week has already fizzled out. Investors were expecting fiscal measures but will have to be patient as Beijing has postponed any announcements until after the US presidential elections. The IMF's financial stability report reminded investors that China will need more stimulus if it is to tackle its structural challenges.

We are still neutral on equities as a whole but with a preference for Japan and emerging countries. The US earnings season has got off to a good start but geopolitical risks suggest we should be cautious. We are also sticking with our neutral stance on duration ahead of the US elections and also because there has been some improvement in economic surprises, most notably in the US.

EUROPEAN EQUITIES

The earnings season is in full swing but several macroeconomic indicators also featured this week. France's manufacturing and services PMIs retreated from the previous month's score with both in recessionary territory. The composite PMI also came in below Germany's indicator which benefited from more momentum in services. Along with a tricky week for results, the news pulled down European markets over the week.

A bright spot came from **Hermès** which reported robust figures. Its premium brand status and pricing power resulted in an 11.3% increase in like-for-like third-quarter sales, a strong contrast to others in the struggling luxury sector. **Kering**, for example, reported a 16% fall in sales, or worse than the 12% drop analysts had pencilled in. Even so, the share's reaction was moderate.

In consumer staples, **L'Oréal** disappointed investors by only growing by 2.8%, or lower than the 5% expected. Management said headwinds in China were largely responsible but added that it was confident 2025 would see a return to its historic 5% growth pace.

Among companies suffering sell-offs, **Edenred** plunged by almost 15% on fears that a possible luncheon voucher ceiling in Italy would have a serious impact on margins.

Other companies fared better. French property group **Nexity** said there had been a sequential improvement in new home reservations over the third quarter and that its market share had risen in spite of difficult trading conditions. And growth at France's **ID Logistics** came in above 20%, largely because of a 47% jump in the US and new contracts with **Amazon**. The news helped the share bounce by close to 10% and investors also expect a recovery in France after several poor quarters.

US EQUITIES

Wall Street's onward and upward march paused for breath this week: the S&P 500 shed 0.92% and the Nasdaq 100 edged 0.43% lower. The Russell 2000, however, underperformed by shedding 2.63%.

The week's big surprise came from **Tesla** which soared by more than 20% on Thursday on better-than-expected margins, guidance and deliveries. Bear in mind, however, that the company's results have been falling for 2 years. **Tesla** and **General Motors** bucked the trend in the sector. GM once again reported excellent figures and raised earnings guidance for this year thanks to momentum in pickup and EV sales. Interestingly, **Texas Instruments** said it had seen a relative recovery in demand in its autos division, and especially in China. Elsewhere, **Whirlpool** said demand was soft ahead of the election but management expects a recovery towards the end of the year.

In the defence sector, results underpinned the global rearmament trend, notably for defensive and combat systems. **RTX**, **Northrop Gunman**, **Teledyne** and **Lockheed Martin** all said their order books reflected this move. The only exception is aerospace which is suffering from production lags. **General Dynamics** and its G700 aircraft is a good example.

In the property sector, house builder **Pulte** and flooring specialist **Mohawk** said business was calm over the quarter but both had hopes for an upturn in 2025. **Newmont** (mining) tumbled on fears over costs after the group closed a mine. Results at At&T, the largest telecoms company in the US, were as expected.

The oil services sector saw further consolidation moves with **Transocean** bidding for **Seadrill**. On the other hand, a judge barred **Tapestry's** acquisition of **Mickeal Kors**. After targeting **Pfizer**, activist hedge fund **Starboard** bought a stake in **Kenvue**.

EMERGING MARKETS

The MSCI EM index was down by another 1.78% this week as of Thursday's close. India (-2.65%) underperformed other major regions and China pulled back by 1.59% while Brazil was almost flat (-0.4%).

In **China**, the PBoC cut the 1-year and 5-year LPR rates by 25bp each, or slightly above market expectations. During the BRICS summit in Kazan, President Xi and Indian prime minister Modi reaffirmed the importance of their strategic partnership. September's youth unemployment rate (16-24 year-olds, students excluded) improved to 17.6% from 18.8% in August. **PingAn insurance** reported a good set of results, benefiting from higher investment revenues, an improved combined ratio and strong growth in new business value. **CATL**, the world's largest battery maker, reported a solid earnings beat thanks to a favorable product mix and easing pricing pressure; management said its expected robust demand in the current quarter. **PopMart** delivered another impressive beat both at home and abroad despite China's challenging macro and consumption environment.

In **Taiwan**, September export orders rose 4.6% YoY, or below the 5.6% rise expected.

In **Korea**, **SK Hynix** saw a slight beat in the third quarter, with operating profit at a record high thanks to **HBM** sales jumping over 70% QoQ.

In **India**, results have so far been mixed. Banks and IT services have beaten expectations thanks to better asset quality, stable NIM and a better outlook. However we observed some weakness in companies exposed to rural areas and infrastructure (**Unilever**, **Ultratech miss**). In the internet sector **Zomato**, **Makemytrip** and **PayTm** reported upbeat figures.

In **Indonesia**, the new president unveiled his new cabinet, with the minister of finance, minister of SOEs and health minister being reappointed and several new ministries being created. **BAC** beat expectations on higher loan growth and an improved NIM.

In **Brazil**, IPCA inflation as of October 15 was 0.54%, or slightly above the 0.51% expected.

In **Mexico**, results at **Vesta** were good but below expectations on lower occupancy rates. Management nevertheless upped guidance, citing a stronger pipeline.

CORPORATE DEBT

CREDIT

Weeks go by and look the same on credit markets. It rained new issues in the IG and HY segments this week and all were easily absorbed as inflows continued. New deals included **Webuild**, **AccorInvest**, **Picard**, **Iliad**, **ASK Chemical** and **Almaviva**. Spreads continued to narrow with Euro IG at 103bp -compared to a 5-year average of 120bp- while Euro HY fell to 325bp. The first wave of bank results (**Barclays**, **Bankinter** and **Lloyds**) reflected robust profitability overall with net interest margins holding up despite the downward trend in interest rates.

US and Euro PMIs were generally in line but traders still see at least a 25bp cut from the ECB and Fed before the end of the year. Since October 18, yields on Germany's 10-year Bund have tightened by 6bp to 2.25%. The trend was even more pronounced in the US where 10-year Treasury yields rose by 12bp to 4.2% on expectations Donald Trump might win the election. His plans to raise import tariff barriers and limit immigration are seen as more inflationary.

Euro Investment Grade slipped 0.08% over the period (+4.25% YTD) and euro High Yield was flat (+7.35% YTD).

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.
- 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.

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