EDMOND DE ROTHSCHILD

MARKET FLASH: AS PEACE TALKS BETWEEN RUSSIA AND UKRAINE START, DONALD TRUMP REMAINS UNPREDICTABLE.

- **Hopes of a resolution to the Ukrainian conflict buoyed European equities at the beginning of the week, but Donald Trump's tariff announcements and criticism of Zelensky then caused European and Asian stocks to fall.**
- **Donald Trump threatened to escalate the trade war with additional taxes on cars, semiconductors and pharmaceuticals.**
- **The FOMC minutes revealed concerns that Donald Trump's trade and migration policies might fuel inflation.**

Russian and American officials met in Saudi Arabia to start discussions on stopping the war between Russia and Ukraine. No European countries were invited so France's president organised an emergency meeting in Paris. The worry is that Donald Trump will give into Moscow's demands for US troops to withdraw from central Europe, a move that would undermine the continent's security. But Europe is still divided: France, the UK and Sweden are for a peace mission in Ukraine while Spain, Germany and Denmark think sending troops in would be premature. Poland, which has the largest European army in headcount, ruled out any military involvement. Tensions increased with Donald Trump's surprising attacks on Volodymyr Zelensky after the Ukrainian president refused to transfer ownership of 50% of his country's essential mineral resources to the US on the grounds that Washington was not guaranteeing enough protection. But despite this tension, Ukraine's president eventually took a more conciliatory approach by claiming the two countries had a solid relationship and that he was committed to finding some common ground. Elsewhere, Donald Trump confirmed that 25% tariffs would be levied on car imports from the beginning of April with pharmaceutical products and semiconductors to follow at some later date. On markets, hopes for an end to the conflict boosted European stocks to start the week. But Donald Trump's tariffs and his criticism of Zelensky then dragged European and Asian markets lower. Wall Street was more resilient.

The FOMC minutes revealed concerns that Donald Trump's' trade and migration policies might fuel inflation. As a result, inflationary risk is now a bigger worry than any labour market deterioration. Several Fed officials also said that it might be sensible to mark a pause in shrinking the Fed's balance sheet or slow its pace until the debt ceiling was raised. In Europe, concerns mounted after ECB hawk Isabel Schnabel's comments on a possible end to rate cuts. Government bond yields rose. They had already moved higher after Ursula von der Leyen had suggested excluding defence spending from government deficits, a move that could aggravate debt and deficits. Yields on Germany's 10-year Bund rose to 2.55%. Friedrich Merz, whose party is tipped to come first in this Sunday's parliamentary elections, is in favour of loosening budget rules to gain more flexibility. But a divided Bundestag is likely and that could force the CDU/CSU to form a coalition government with several parties, making it difficult to take immediate action.

In Japan, accelerating inflation and strong growth in the fourth quarter of 2024 -on exports and investment- could lead the Bank of Japan to raise rates. However, the bank's governor

Kazuo Ueda said the bank might resume buying government bonds to stop the currency appreciating too much. In the UK, unemployment was unchanged at 4.4% but overall inflation rose to 3% and underlying inflation to 3.7%. The Bank of England's governor is nevertheless confident that inflation will fall back this year.

Given today's geopolitical uncertainty and Donald Trump's unpredictable policies, we still prefer protected equities as they should cushion any serious market falls. We have a slight preference for Chinese equities as Beijing seems committed to rolling out economic stimulus. In fixed income, we continue to prefer corporate debt to government bonds.

EUROPEAN EQUITIES

European markets continued to surge thanks to financials, healthcare and defence. Financials gained on central bank calls for an easing in European banking regulations. Defence gained on news concerning the Ukraine conflict after European Commission head Ursula von der Leyen suggested excluding defence spending from government deficit calculations. This should mean a surge in defence budgets. Saab, Leonardo, Thales and Rheinmetall all gained on the news as did Exosens which recently listed in Paris. In macroeconomic indicators, PMIs showed no real signs activity was recovering. France came in at 44.5 but Germany edged surprisingly into expansionary territory at 51.

More than 50% of companies have now reported fourth-quarter results. **Renault**'s figures came in slightly better than expected for the second half of 2024 but management disappointed markets with a cautious indication of the outlook for this year. **Capgemini** tumbled after disappointing guidance on growth, margins and free cash flow in 2025. **Carrefour** is still struggling in Europe and abandoned its share buyback programme. A review of all its businesses is under way. On the plus side, **Gaztransport & Technigaz (GTT)**, the leader in LNG storage solutions, released impressive 2024 results and strong guidance for this year. The stock soared to a record high. **Kingspan** also beat expectations in 2024 and sounded an optimistic note for 2025. In AI news, Germany's **STMicroelectronics** gained ground after announcing the launch of a new AI infrastructure chip.

US EQUITIES

In a holiday-shortened week, Wall Street continued to slip. The S&P 500 lost 0.18%, the Nasdaq 100 0.42% and the Russell 2000 1.25%.

Healthcare stocks continued to head higher with **Baxter** jumping 7.18% after beating sales expectations and providing encouraging guidance for 2025. **Biomarin** (+5.97%) also had a good fourth quarter and management said it expected to see strong growth and profitability. And despite a slight sales miss in its third quarter, **Medtronic** (+2.17%) expects EPS and like-for-like growth to accelerate.

Last week's uncertainty over consumer spending rose further. **Walmart** was down -6.57% due to US tariff policies that could weigh on consumer spending. These worries were much more in evidence in the consumer discretionary sector where **Wingstop** (-19.26%) disappointed markets with its guidance. **Toast** (-3.94%) was also dragged down despite its upbeat figures. The trend was similar in the e-commerce sub-section. Marketplace group **Etsy** (-10.28%) reported lower-than-expected sales and **Wix** (-10.59%) was, like Toast, a victim of investors expecting a slowdown even if the group posted good figures.

In tech sector news, **Intel** (-4.75%) could be split up between **TSMC** (-0.45%) et **Broadcom** (-0.78%). The latter would benefit from production capacity to reinforce US chip production independence. Given the uncertainties over the future of TikTok, **Akamai Technologies (**-1.3%) will have to go through another year of transition. Management was cautious in its guidance and said 3 years would be needed to help growth re-accelerate.

In construction, the fourth quarter at **Trimble** (-2.57%) showcased the importance of data centres and energy markets for growth in the non-residential market. Management referred to order book weakness and the CFO at **Procore** (-5.98%) told JP Morgan that the same situation had led to its very cautious guidance. That said, should momentum improve, these pessimistic comments could turn into positive surprises in coming quarters.

EMERGING MARKETS

The MSCI EM index had edged 0.6% higher as of Thursday's close. China (-0.5%) took a breather after the recent rally. India and Korea rebounded by 1% and 3.3%, respectively. Mexico (+0.2%) closed almost flat.

In **China**, new TSF and loans rose more than expected in January, the highest monthly level on record. The data breakdown showed that policymakers pumped more money into the corporate sector and front-loaded fiscal spending. However, loan demand from households remained weak. January NEV wholesale jumped 29.4% YoY, and new home prices slipped 0.07% MoM, or slower than in December. Xi Jinping hosted a rare closed-door symposium with business leaders on Monday that signaled a substantial change in tone to boost enterprise confidence. The State Council issued plans to help foreign investors carry out M&A in China, including removing all market access restrictions for foreign investors in manufacturing. **Tencent** said it was integrating **Deepseek**'s AI model in its testing search function. **Alibaba**'s fourth-quarter results beat market expectations for both e-commerce and cloud business. Management unveiled a 3-year capex cycle, its largest ever, to build AI and cloud infrastructure to capture rising demand. Bilibili also delivered robust fourth-quarter results fuelled by games and advertising while results at **NetEase** were in line with no new mobile games. **Baidu** posted weaker fourth-quarter revenues dragged down by advertising. Management said it was shifting its ErnieBot 4.5 AI model to open-source and would integrate DeepSeek and Ernie bots into its search engine.

In **Korea**, **Samsung** cancelled $2bn in treasury stock as part of its buyback plan to enhance shareholder value. An investor group is planning one of the world's largest data centers for AI in South Korea; it will cost as much as $35bn and pack up to 3GW in power.

In **India**, **Tesla** stepped up hiring in the country after the Musk-Modi meeting and is reportedly to ship a few thousand cars in the coming months. **Mahindra & Mahindra** received 30,000 EV bookings, or less than expected. **Titan** said it would make another attempt to acquire a significant stake in **Damas Jewellery**.

In **Indonesia**, January's trade surplus was above economist's estimates, with exports rising 4.68% YoY while imports fell by a disappointing 2.67%. President Prabowo unveiled a budget efficiency plan in three phases.

In **LATAM**, **Meli**'s fourth quarter crushed EBIT, EBIT margin and net profit expectations. The better-than-expected operating margin was down to: i) strong execution and cost management in the logistic network; ii) efficiency in collection and; iii) operational leverage.

In **Brazil**, **Lojas Renner** reported decent sales growth in the fourth quarter but EBITDA fell short of expectations. The company announced a new buyback programme for up to 7% of outstanding shares.

In **Mexico**, **Vesta** announced a good set of results, with occupancy rates ahead of expectations but guidance disappointed.

CORPORATE DEBT

CREDIT

Investors spent the week digesting US vice-president JD Vance's speech in Munich on February 14 and wondering what the consequences would be for Ukraine, Europe and, in fact, the world.

Government bond yields rose after Europe reacted by organising a mini-summit in Paris and countries signalled that defence spending would be increased.

But spreads remained tight as technical factors like inflows and easily absorbed new issuance continued to offset volatility.

Reporting for financials continued apace with upbeat figures but with no real impact on credit markets. In new issuance, euro-denominated AT1 deals from ABN Amro and UniCredit were oversubscribed as was a USD issue from Barclays. CCF (ex MyMoneyGroup which belongs to Cerberus) raised €250m with a T2 at 250bp above the swap curve. In M&A , **Banco BPM** sweetened its bid on **Anima** and also offered to withdraw some suspensive conditions. As a result, the chance of the bid succeeding improved, thereby reinforcing **Banco BPM**'s defence against being taken over by **UniCredit**.

In high yield, spreads were underpinned by thin new issuance with only one new deal over the week.

In emerging country debt, Uzbekistan raised UZS 7.5 trillion.

And there were more corporate hybrid debt deals from groups like **Exelon**, **CMS Energy** and **TransCanada Pipelines** following Moody's update of its criteria for awarding equity credit to corporate hybrid bonds.

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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