



EDMOND DE ROTHSCHILD ASSET MANAGEMENT

MARKET FLASH: MOVING BETWEEN GEOPOLITICAL TALKS AND GROWTH PROSPECTS

- **Donald Trump plans to meet Xi Jinping amid growing tensions between the two global powers.**
- **In Japan, the Liberal Democrat party joined a coalition with the reform party Ishin and Sanae Takaichi became prime minister. This appointment sent Japanese equities higher.**
- **The earnings season is proving robust, with 58% of European companies exceeding expectations. The US has done even better with 84% of companies reporting beats. However, a few disappointments among large companies call for caution.**

Donald Trump plans to meet Xi Jinping but has in the meantime increased pressure on China by airing possible restrictions on purchases of critical US software. Even so, a summit would be good news for China's GDP growth. The economy grew by 4.8% in the third quarter, so less than the 5% target due to soft domestic demand. Retail sales, for example, rose 3% when they were expected to be up 4.4%. On the other hand, overseas demand drove growth by lifting industrial production and exports.

Economic data in Europe varied depending on the country. Composite PMI in Germany came in at 53.8, or better than the 51.5 expected, thanks to a rise in services. In France, however, services dragged down composite PMI to 46.8, or below consensus expectations of 48.4. In addition, S&P downgraded France from AA- to A+. The agency expects government debt to rise to 121% of GDP by 2028 and highlighted the risks to budget consolidation. The UK is also beset by budgetary problems. The government wants to remove past imbalances by increasing taxes and making budgetary cuts. Overall inflation is running at 3.8% but the underlying figure has slowed to 3.5% so the Bank of England might consider gradual rate cuts.

Despite the economic backdrop, 58% of European companies have beaten third-quarter expectations. The US has done even better with 84% of companies reporting beats. However, some misses by leading companies suggest caution.

Elsewhere, lack of progress with Vladimir Putin over a peace deal in Ukraine led Donald Trump to announce sanctions against two Russian oil majors. Brent crude rose to \$65 on the news. The move was accentuated by India's decision to review its purchases of Russian oil. European leaders also expect to stop importing Russia's LNG by the end of 2026, a year earlier than expected.

In Japan, the Liberal Democrat party joined a coalition with the reform party Ishin and Sanae Takaichi became prime minister. The appointment sent Japanese equities higher on expectations of favourable budgetary policy and measures to boost consumer purchasing power. According to the latest data, inflation was at 2.9%, down from May's 3.7% peak. Note, however, that the coalition has 231 seats or less than the absolute majority of 233.

Despite the promising start to the earnings season, we are cautious on risk assets due to today's uncertain environment. We remain upbeat on duration, and notably emerging country debt, and are focusing on higher-rated companies.

EUROPEAN EQUITIES

European equity markets continued to perform well. The earnings season has so far been promising. In the Stoxx Europe 600, 21% of companies have reported and 58% have beaten expectations. Meanwhile, Donald Trump continued to impact financial markets. His plan to toughen sanctions against Russia sent energy prices higher. He also suggested the US could introduce extra trade measures against Beijing.

The tech sector slightly underperformed this week after some disappointing news. Third-quarter results at **SAP** were in line but the group revised down annual guidance on growth in its cloud business. And **STMicroelectronics** also sold off after delivering lower-than-expected fourth quarter guidance.

Third-quarter figures at **Renault** beat expectations but the stock fell due to pricing pressures and weakness in European light goods vehicles.

Roche was the first European pharma giant to report. The group raised annual earnings guidance even if currency effects had led to sales missing expectations. Growth at perfumes and cosmetics group **L'Oréal** missed expectations but every sector advanced and accelerated across all regions.

US EQUITIES

Wall Street ended the period higher thanks to the strong probability of a Fed rate cut at the end of October and generally better-than-expected company results. The S&P gained 1.12% and the Nasdaq 100 1.13%. Investors also welcomed the confirmation of a Donald Trump-Xi Jinping summit next week as it could lead to some easing in persistent trade tensions. For the moment, the ongoing shutdown has not dented the market's upbeat mood. After three weeks of a statistical blackout, September's CPI was in focus. Overall inflation came in at an annualised 3.1%, a slight acceleration due to rising energy prices.

It was a mixed week for tech stocks. **Intel** gained 3% on robust results and optimistic prospects for 2023 and **Lam Research** rose 4.3% on strength in the AI data center segment. In contrast, **Texas Instruments** shed 2.5%. **Meta** rose 2.4% but confirmed that around 600 jobs would be lost in its AI products and infrastructure division. The move was seen as a strategic refocusing on short-term profitability faced with structurally high CAPEX.

In more cyclical sectors, results went down well with investors. **General Motors** (+14.5%) and **Ford** (+3.2%) benefited from a rebound in US sales. **Tesla** gained 2.2% despite a results miss. Operating profits tumbled 40% even if sales rose 12% to record levels. In residential property, companies like **PulteGroup** (-2.9%) showcased the structural deficit in US housing but it has yet to show up in volumes. Healthcare had a good week. Results at **Intuitive Surgical** (+23.6%) and **Boston Scientific** (+3.2%) both swept past expectations. **West Pharmaceuticals** (+13.6%) benefited from strong demand from weight-loss GLP-1 treatments. In health insurance, **Molina** (-18%) slashed earnings guidance as higher medical costs continued to weigh on Medicaid and Marketplace profitability.

After the previous week's sell-off, the gold ounce stabilised at \$4,130.

EMERGING MARKETS

The MSCI EM index had advanced by 1.46% in USD as of Thursday. China, Brazil, Korea, India, and Taiwan were up 3.09%, 2.90%, 1.04%, 0.86% and 0.29%, respectively. Mexico slipped 0.31%.

In **China**, third-quarter GDP growth slid to 4.8% YoY. September retail sales rose 3% YoY, the slowest pace so far this year. Industrial production was the bright spot, up 6.5% YoY and ahead of the 5% expected. Third-quarter fixed asset investment dropped 0.5% YoY after rising 2.8% in the first half. The 4th Plenum guidelines were released with key strategic goals to accelerate innovation and technology self-sufficiency, along with boosting domestic demand and especially consumption. Donald Trump said he would meet Xi Jinping in South Korea on October 30 on the sidelines of a summit in Asia. **Nexperia's** China unit resumed chip sales to domestic distributors, but all transactions need to settle in renminbi. **Popmart** reported a solid quarter with sales comfortably beating elevated expectations. **CATL** also reported strong results as expected, with net income up 41% YoY. **Alibaba** introduced its new computing pooling system Aegaeon, dramatically reducing reliance on Nvidia GPU by 82% for AI models. Bilibili's new game launch was a success and has now sold over 500,000 copies since its October 16 launch.

In **Taiwan**, September exports jumped 30.5%, or ahead of estimates of 18.7%. **TSMC** applied for permission to construct a new plant for the production of new high-speed wafers.

In **Korea**, the central bank held the base rate stable at 2.50%. South Korea and the US are likely to agree on cutting auto tariffs from 25% to 15% at the Gyeongju APEC Summit. **Hanwha** teamed up with **Diehl Defence** to expand radar exports to Europe. Memory producers indicated DRAM price increases could be higher than consensus expectations. A committee member indicated that they would start to discuss mandatory treasury share cancellation and dividend tax right after national audit and they are aiming to revise both of them before year-end. All eyes are on next week's APEC summit.

In **India**, September industrial output rose 3% YoY vs. the 6.3% previously. Retail sales for the festive season increased strongly on an elevated base, +17% YoY for passenger vehicles and +20% for two-wheelers. Media reports said India and the US were inching closer to a deal, with tariffs likely to be reduced to 15-16%, from the current 50%. **Reliance** reported a solid beat driven by telecoms and retail. **HDFC** and **ICICI** reported better-than-expected NIMs - asset quality improvement was the highlight. **HUL** reported an underwhelming quarter and the new CEO outlined a strategy for volume-led growth.

In **Indonesia**, the government announced cash handouts to 35 million low-end households, for a total of \$1.9bn. **BCA** reported better-than-expected results and gave upbeat guidance.

In **Brazil**, **Meli** and **Grupo Casas Bahia** announced a JV. **WEG** reported better than expected EBITDA margins, with good pricing power to reprice higher import tariffs in the US and announced an investment acceleration plan to expand manufacturing capacity in Mexico amid rising trade barriers. **Vale's** iron ore output reached its highest level in seven years. **Ambipar** filed for bankruptcy protection on R\$11bn in debt. Lula confirmed he was a candidate for the 2026 Presidential election.

In **Mexico**, August retail sales rose 2.4% YoY in August. CPI for the first 15 days of October rose 0.28% YoY or lower than the 0.38% estimated. August economic activity rose 0.57% MoM,

or ahead of expectations of 0.20%. Authorities granted **Revolut** a banking licence in Mexico. Vesta reported better than expected results, as higher rent growth offset lower occupancy rates. **OMA** also reported a good set of results, with strong cash generation. In Argentina, people will vote in the midterm elections over the weekend, a key test for Javier Milei's government

CORPORATE DEBT

Markets had been uncertain and choppy for a few weeks but this week the Xover was stable below 270bp. There appears to be little to derail today's upbeat sentiment.

Nevertheless, there are a few warning signals like the relative widening of B-rated companies towards BB with decompression and on average a 200bp premium on B compared to BB. In addition, investors have put some companies, in the autos and chemicals sector for example, under watch.

That said, this week's results suggest the worst is never certain and that markets tend to overstate bad news. Results from **Renault**, **Ford** and **Valeo** for example, beat expectations and attenuated prevailing sector pessimism. But in the closely watched chemicals sector, **Ineos** and **Synthomer** reported poor figures even if they were not as bad as expected. EBITDA slumped by around 40%, automatically increasing leverage but to bearable levels for a cycle low.

BNP Paribas provided another good indicator of market sentiment. The share tanked by close to 10% but CoCos lost 25-35 cents and senior debt was unchanged.

New issuance remained active with hybrid deals from **SoftBank**, **BAT**, **AroundTown** and **Abertis** with an RT1 from **Achmea** (financial services). Valuations remained underpinned by abundant inflows. JP Morgan estimated that another €1.2bn flowed into European credit funds over the week.

To sum up, investors should be aware of certain situations, but the market as a whole is still bullish.

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.
- CTA: quantitative strategy which uses futures to invest in a wide range of financial assets, including equity indices, short-term and long-term interest rates, currencies, and commodities.
- 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.
- RT1s: perpetual bond issues with early redemption possible after 10 years. Coupon payments are discretionary and non-cumulative.

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