# MARKET FLASH: EUROPE STANDS TO LOSE FROM DONALD TRUMP'S "AMERICA FIRST" STANCE

- **Donald Trump's clear victory led to the yield curve steepening and the dollar rising**
- **China's economy offers a note of optimism**
- **The outlook in Europe has been weakened by the threat from the US to its exports and its reduced internal capacity to react.**

**Naturally, Donald Trump's clear victory dominated the week. His success had been partially discounted but still led to the yield curve steepening and the dollar rising. This was partly a reaction to the new President's intention to launch a trade war but essentially due to his anti-immigration plans which could make workers harder to find and drive wage inflation. The Republican win also underpinned US equities and them alone - equities elsewhere fell- on hopes of economic stimulus from an expansionary budget. But these hopes could lose some steam if Republicans fail to get complete control of Congress. They have secured the Senate but votes for the House of Representatives are still being counted and the result could be tight. But even if Republicans fail to get a clean sweep, trade and immigration policies are likely to go ahead. Elsewhere, the Republican party's determination to support oil production will mean lower prices at the pump.**

**One effect for Donald Trump's success was to accelerate the collapse of Germany's fragile coalition. The threat to the country's exports from the new US administration failed to solve budget disagreements. The SPD and the Greens wanted a slightly more expansionary budget (+€9bn) but the FDP stuck to its basic opposition to increased spending despite Germany's current problems. Early elections are unlikely to lead to a budget agreement as the rigour-conscious CDU is likely to head up the coalition.**

**The US election result had no impact on the Fed which went ahead with a 25bp cut; the impact of the new administration's policies will take time to appear. The Fed's move was logical considering the slowing labour market and generally more moderate inflation. Analysts had been expecting 100,000 job creations in October but they fell sharply to 12,000 from 223,000 in September, a month which was also hit by hurricanes and the Boeing strike. What's more, the two previous months were revised down to 112,000. Manufacturing ISM also fell to 46.5. Unemployment, nevertheless, was unchanged and wages rose 4%. The persistently resilient services segment, in contrast, saw ISM rebound to 56.**

**The Bank of England also cut its rates by 25bp but is expected to slow the pace of any future moves lower in 2025 as the Labour government's budgetary decisions in favour of the economy could raise inflation by 50bp according to estimates.**

**Elsewhere, China's Caixin PMI returned to expansionary territory (52) with manufacturing at 50.3. Beijing's stimulus measures were disappointing and their impact is unlikely to solve the country's structural problems.**

**The outlook in Europe has been weakened by the threat from the US to its exports. And the eurozone's capacity to react is being undermined by heavyweights Germany and France, both of which are faced with a fragmented political environment which will limit decision-taking. This is why European equity and bond markets parted ways with Wall Street.**

**Due to the rising dollar and negative prospects for global exports, we have decided to raise exposure to US equities, maintain our positive take on Chinese equities and reduce emerging country equities. Our overall position on equities and fixed income is unchanged at neutral. We still like investment grade and emerging country credit.**

## EUROPEAN EQUITIES

European equities ended the period looking for some direction. On the one hand, the week saw somewhat upbeat macroeconomic indicators with eurozone retail sales rising in September. And the Bank of England unsurprisingly cut its rates for the second time by 25bp to 4.75%. The bank, however, warned that it had raised its inflation forecasts for 2025 and 2026 because of the Labour government's budgetary blueprint.

On the other hand, companies reporting quarterly results delivered cautious messages. **Air France**, for example, said it expected higher labour and maintenance costs due to supply side constraints and plane delivery issues. **Ryanair** followed suit by giving lower than expected guidance on the outlook for 2025 due to planes being delivered late and lower fares. The autos sector remained mired in negative territory: **BMW** said profitability had hit a low not seen for four years due to soft Chinese demand, local competition and vehicle recalls to correct a brake system problem. **Ferrari** also cited weak Chinese demand. Factory closures in the sector continued with **Michelin** shutting two sites in France. Management blamed sluggish economic conditions and tougher competition. In consumer discretionary, **Hugo Boss** missed profitability expectations, again due to China. Banks also reported earnings misses. Just like **BNP**, **Crédit Agricole's** performance in insurance and consumer credit was disappointing.

On a brighter note in the software sector, Germany's **Nemetschek** followed on from **SAP** in reporting upbeat figures. As proof of the group's resilient model, like-for-like recurrent revenues jumped more than 25% despite difficult trading conditions in European construction. **Novo Nordisk** reassured investors after cautious indications from Eli Lilly on obesity drugs by beating sales expectations in the same segment.

## US EQUITIES

It was the busiest week this year on Wall Street with a slew of company reports and the presidential election results. Donald Trump's victory drove indices to new all-time records with small caps outperforming sharply and hitting highs not seen since October 2021. Banks led gains with advances of close to 10%. The sector benefits from the current yield curve as well as the likelihood of less regulation and more M&A under the new administration. Unprofitable small caps also soared despite higher long bond yields. In contrast, sectors like renewable energy and companies with supply chains dependent on China tumbled

Price shifts were volatile, speculative and sometimes disconnected from fundamentals. Donald Trump's election amplified the trend. **Dentsply Sirona**, for example, cratered by 28% after cutting growth guidance for this year by 2%. Yet **O'Reilly** Auto Parts had a results miss for the fourth time in 20 years and still ended higher. Elsewhere, retirement home group **Brookdale** fell sharply after occupancy rate increases slowed.

Nevertheless, it has been a good earnings season for small caps despite sometimes excessive market reactions to figures. **Toast's** figures suggested improving profitability and the stock jumped 20%. **Doximoty** also saw improved profitability and growth and was indicating a 40% surge in pre-market trading. It was the same story for mobile advertising company **AppLovin**, indicated 46% higher after raising guidance for the umpteenth time. On the other hand, **Match Group** fell 20% despite a return to growth among paying Tinder users. Investors preferred to concentrate on the company's disappointing fourth-quarter guidance. In healthcare, **Illumina** said the outlook was encouraging for genomic sequencing. Management sees growth returning next year.

## EMERGING MARKETS

The MSCI EM index had rebounded by 1.65% this week as of Thursday's close. Brazil and Mexico gained 4.22% and 3.86% and China also regained 3.6% on improving macro data and high expectations of stimulus ahead of the NPC meeting. India (-0.33%) underperformed.

In **China**, October exports were up 12.7% YoY, or notably stronger than expected while imports fell 2.3% YoY. The private sector oriented CaiXin PMI topped estimations at 51.9, up from 50.3 in September. The government announced a stimulus plan after the NPC meeting, with an additional RMB 6 trillion over 3 years to swap local government debt. The total was RMB 10 trillion, including the existing budget, or largely in line with expectations. China announced 15-day visa-free policies for 9 countries, including South Korea. October home transaction prices beat expectations, trending up sequentially in the 50 sample cities. Auto sales data were also constructive in October, with BYD's achieving record sales of more than 500,000 units, +20% YoY.

In **Taiwan**, TSMC's October sales were up 29% YoY. The group expects the first batch of production to be rolled out from the Arizona fab in early December. According to media reports, TSMC will suspend all China client orders for 7nm or more advanced components.

In **Korea**, the opposition agreed to the government's plan to scrap the Financial Investment Income Tax.

In **India**, Sun Pharma announced that the US district court had granted a preliminary injunction against the launch of their Leqselvi treatment. Car maker Mahindra & Mahindra delivered solid double-digit growth, with margin expansion ahead of consensus. Apollo Hospital also announced robust growth, beating consensus expectations on better occupancy rates and operational margin improvement. Power grid's quarterly results were slightly below market expectations but the company revised up significantly its capex plan.

In **Brazil**, the central bank increased interest rates by 50bp. Most of the attention was on the government's spending cuts announcement, which had been delayed. MELI reported a miss, with EBIT falling short as credit scales faster than expected. Petrobras beat on strong cash flow and a higher-than-consensus dividend payment; capex was in line. Lojas Renner saw SSS sales rise 11.5%, or in line with high expectations, but EBITDA missed on higher costs.

**Mexico's** Supreme Court dismissed a ruling intended to limit the scope of a judicial overhaul. OMA reported its traffic figures for October. Consolidated traffic fell by 4.8% YoY, or below expectations. Domestic traffic declined by 7.0% YoY, which was offset by a better international traffic performance of 12.7% YoY. All eyes are on next week's budget proposal.

In **Peru**, Credicorp's third quarter earnings beat high consensus expectations, delivering a robust set of results driven by better asset quality and good cost control.

# CORPORATE DEBT

## CREDIT

Bond markets struggled for direction after Donald Trump's election victory as traders tried to decide on the consequences. The initial reaction was a sharp drop in Euro yields and a big surge in dollar yields. But by the end of the week, after better-than-expected economic data in Europe and a fall back in US yields, trends started converging again. Yields on Germany's 10-year Bund were down 2bp on the week as of Friday lunchtime while 10-year US Treasury yields had fallen 9bp. The big winner this week was the Xover which tightened by almost 25bp. Investment grade had returned 0.28% as of Thursday evening and high yield 0.15%.

The technical situation is still extremely favourable with inflows looking to capitalise on around 6% in yields and relatively limited new issuance. New issues are still offering 6.5% on average so investors can increase fund yields. No change on the results front: industry and autos are still suffering from sluggish demand while services and property continue to enjoy a favourable environment. Hypermarket giant **Auchan** launched a redundancy plan as part of its strategy to revive profitability.

In financials, CoCos gained 0.38%, wiping out the previous week's underperformance. Results from banks remained upbeat.

## 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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