



MARKET BRIEFING

MAY EQUITY MARKET REVIEW:

Equity markets fall amid fears of a prolonged US-Sino trade dispute

May 2019

The World in five bullet points

- ▶ **Equity markets** fell around the world in May on fears of a prolonged US-Sino trade dispute and concerns it would start to drag heavily on global growth. Tensions between the two countries rose when the US said it would ban the use of Huawei's 5G technology in its domestic telecoms market and raised tariffs on US\$200bn worth of goods from China, then later said it would impose a 5% tariff on Mexican goods in an attempt to curtail illegal immigration at the countries' border.
- ▶ The **Huawei embargo** caused equities in Emerging Markets to fall sharply with Asian exporters taking the brunt of the selling but the US indicated that China would not be the only country in its trade and tariff cross hairs. As well as the new tariff on Mexican goods, it also stripped India of its preferential trade status and set a 180-day deadline for negotiations with the EU and Japan over car exports. A G20 meeting later in June will likely be a lively affair.
- ▶ Theresa May effectively resigned as Prime Minister of the **UK**, finally succumbing to pressure to give up leadership of the ruling Conservative Party, and thereby handing the premiership of the country to her successor. Failure to deliver an acceptable Brexit deal to the UK's parliament was almost entirely to blame for her demise, particularly as her own party and that of the opposition Labour Party remained deeply divided on what to do next. The UK's bookmakers quickly installed Boris Johnson as favourite to succeed Mrs. May while indicating that either a general election or second referendum were still possible.
- ▶ As one centre-right politician lost her personal game of thrones, so another narrowly won his and was re-elected in **Australia**. Scott Morrison, who had led a minority coalition government as leader of the Liberal Party since August 2018, led the same coalition to a majority of seats in the country's lower House of Representatives. The result was largely regarded as a surprise as the coalition had been behind in the opinion polls for almost three years. Australian equities rose on the election news.
- ▶ More than 600 million people also voted in the general election in **India**, which saw the incumbent prime minister Narendra Modi returned with an increased majority for his Bharatiya Janata Party despite concerns that unemployment and continuing high levels of poverty in rural areas would eat into its majority. Most analysts pointed to Mr. Modi's economic policies to remain unchanged with banking consolidation, infrastructure spending and increased wealth for rural areas remaining a priority.

Fig.1. Regional Equity Indices Performance, USD % change

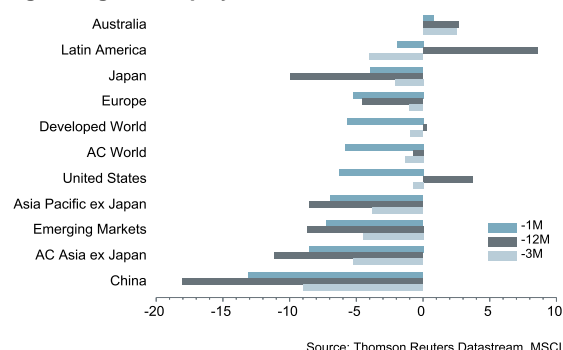
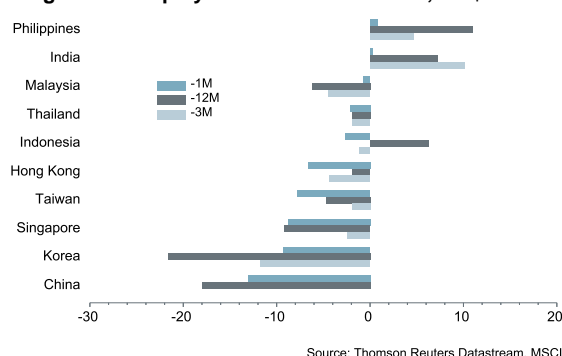


Fig.2. Asia Equity Indices Performance, US\$ % change

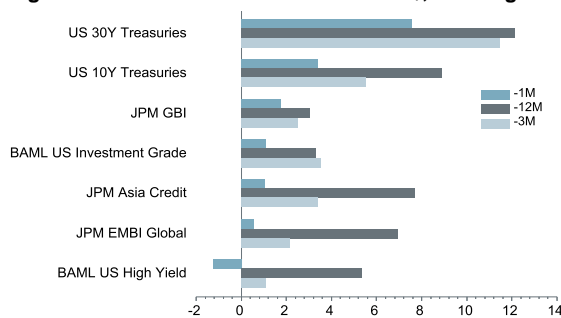


Equity Markets

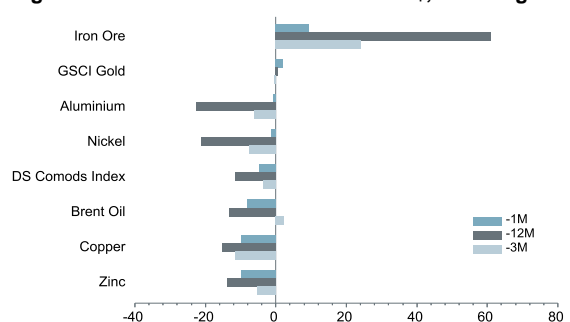
- ▶ **Global equity** markets fell abruptly on the increasing trade tensions around the world with Emerging Markets taking the brunt of the selloff. Exporters in Asia, especially China and Korea, fell sharply leading the MSCI EM index to fall 7.2% and the Asia ex Japan index to underperform and fall 8.5%. Once again, the US outperformed but was not immune to the weakness, falling 6.3%; Japan and European markets both marginally outperformed, shedding of 4.0% and 5.3% respectively.
- ▶ **European** equities modestly outperformed on stronger-than-expected economic news (see below) as well as relief the elections to the European parliament did not see a wholesale swing to the populist right wing as some had feared although the increased influence of the liberal and green groupings will likely make legislating more difficult. Germany saw a 6.1% drop and France fell 5.6%. The UK fell 6.0% with the dollar earners finding a floor on a lower pound post Mrs. May's resignation. Australia was one of the few equity markets to see a gain after the surprise general election result, with the MSCI Australia index up 0.7%.



- Other positive markets included **Russia**, which gained 3.6% with banks and energy stocks proving supporting while the Philippines and India both eked out small gains; the former on a lowering of the core repo rate, the latter on positive election results. Brazil also saw its first positive month since January following pro-government rallies that supported government reforms and helped the greater MSCI Latin America index outperform. But elsewhere the picture was rather bleak.
- Asia's underperformance was dragged mainly by the very sharp decline in **China**, which saw its MSCI index drop 13.1% as the increased trade tensions proved a tipping point for many investors who now see softness in the China economy getting worse, despite the potential for stimulus programmes from Beijing. Technology stocks were hit particularly hard as the focus of the trade talks switched to tech transfers and intellectual property. Earnings in China also fell with EPS revisions still negative at -5.3% albeit off the lows of -8.0% earlier in the year.
- Hong Kong** also fell to close the month 6.7% lower with property and other defensive stocks providing a base however the other north-Asia export-orientated markets fell sharply with **Korea** down another 9.3%; it is now 4% lower for the year and one of the few markets to show a loss year to date. **Taiwan** fell 7.8% as its tech stocks dragged substantially while last month's big winner, **Singapore**, lost almost 9% as its banks gave up many of the gains for the year on worries over their interest margins. Other ASEAN markets fared relatively better as they are less exposed to the tech sector that is the focus of the trade talks.

Fig 3. Bond Indices Performance in US\$, %change

Source: Thomson Reuters Datastream, Bank of America Merrill Lynch, JP Morgan

Fig 4. Commodities Performance in US\$, % change

Source: Thomson Reuters Datastream

Fixed Income

- US Treasury yields** touched lows in May not seen since March and the curve inverted for the second time this year, with three-month T-bills yielding more than ten-year debt; the latter ended 38bps lower at 2.12% as investors speculated the Fed may cut rates at least once this year with some indicators showing as many as two cuts. Core European bond yields also fell as populist parties made gains in EU parliament elections along with more left-leaning parties with the centre ground losing out.
- In **Asia**, government bond yields similarly trended lower over the month. Indian government bonds fared well as investors added duration on the prospect of further rate cuts. Also lifting sentiment were hopes of policy continuity after Prime Minister Modi's BJP won a second term by a landslide. Philippine bonds also outperformed as the central bank there lowered its overnight borrowing rate to 4.50% at its May policy meeting. Indonesia proved an exception, with domestic rates rising on the back of negative risk appetite. April data also showed Indonesia's trade balance falling into a deficit, foreign-exchange reserves dipping and inflation inching higher – data that also weighed heavily on the equity market.
- Asian US dollar credit markets delivered positive returns on the back of firmer US Treasuries, with investment-grade credits outperforming high-yield, however, spreads widened because of trade war concerns. The US blacklist of China's Huawei fuelled worries that more Chinese tech companies could be targeted. Separately, sentiment on the mainland was hurt by the government's takeover of Baoshang Bank due to its worsening credit profile.

Commodities

- Oil prices** continued their march higher at the beginning of the month, only to fall sharply in the third week on fears of the US-Sino trade dispute would worsen and harm global growth prospects. That caused crude to have its worst week since the start of the year when the weak economic data especially from China (see below) combined with comments from Saudi Arabia that said it would look to ease tensions in the middle east. Higher than expected US inventory data also added pressure to prices.
- Copper** prices hit a low point for the year as fears of a prolonged US-Sino trade dispute sent the US dollar higher and copper lower. By the final week of May, it had fallen six weeks in a row. **Aluminium** prices hit their highest level in six months following a refinery shutdown in China but sold off sharply in the final week to end the month slightly lower. **Iron ore** prices also hit fresh five-year highs and crossed the \$100 per tonne level after poor weather in Brazil added to weather-related disruption in Australia, and the closure of mines in Brazil earlier this year, to send prices higher.
- Gold** was also slightly stronger as investors sought the traditional safe-haven asset classes after the equity market declines. But elsewhere metal prices were weaker as investors began to fear the trade dispute would start to affect global economic growth. Nickel and zinc prices fell and lithium prices also fell as a key mine in Chile delayed an expansion. **LNG** prices also fell to three-year lows as record production out of the US and falling exports weighed.

Source: Eastspring Investments. Chart data from Thomson Reuters Datastream as at 31 May 2019. For representative indices and acronym details please refer to notes in the appendix.



Currencies

- ▶ **The US dollar** rose again with the dollar index now up more than 4% in the year to date. The White House's move to impose further tariffs on China and new ones on Mexican imports supported the gains against both other developed currencies such as the euro and pound, and more substantially against emerging markets. Bucking the trend was the Japanese **yen** that showed its safe haven status and rose against the dollar with fears over the weakening global economy also providing support. The Presidential summit between the US and Japan also passed off without incident on trade, almost giving the yen a boost. The UK **pound** fell 3.1% as political uncertainties there rose sharply and the euro fell 0.4% on better-than-expected EU parliament results.
- ▶ **Emerging market** currencies fell once again during May with the rise in the dollar largely to blame for the declines and seeing the EM basket falling 1.2%. Among the largest decliners against the US dollar were Latin American currencies with the Mexican peso falling 3.4% on worries the US would spread its tariff increases to Mexico, while Columbia and Chile currencies also fell. On the plus side, Turkey's lira edged higher by more than 2% as the central bank stepped in to stop the currency's slide by re-opening the one-week repo auction market, and Thailand's bhat rose 1.2% as the countries saw equity fund inflows as political tensions eased and MSCI looked to rebalance its index.
- ▶ In **Asia**, the **Korean** won was again one of the weaker currencies as macro economic data points showed no sign of improvement, and the central bank governor said he expected the economy to recover in H2. The bank kept the country's repo rate at 1.75% when some in the market were looking for a cut. However the trade dispute weighed most on **China's** renminbi which fell another 2.5%, to near 2018 lows and brush against the important 7.0/USD level.
- ▶ Elsewhere in emerging markets, **Argentina's** peso fell again after former president Cristina Kirchner said she was contemplating running for the vice presidential role in the country's upcoming elections but the losses were limited after MSCI said it would accept Argentinian equities into its key Emerging Market index. **Russia's** ruble slipped 1.2% as oil prices dropped sharply in the second half of the month and **South Africa's** rand also declined as Cyril Ramaphosa was re-elected as president.

Fig 5. Currencies Performance versus US\$, % change

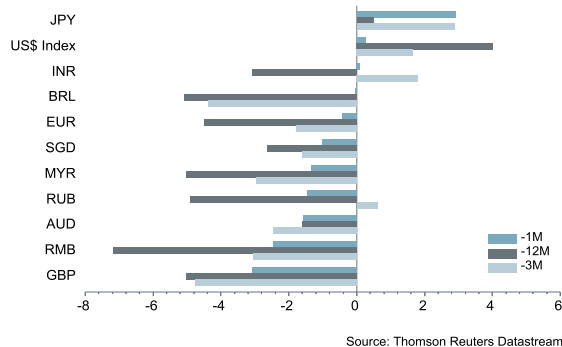
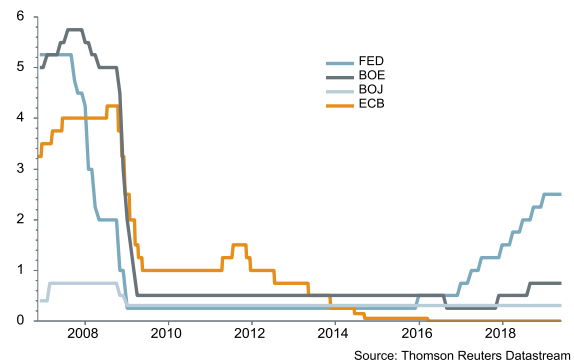


Fig 6. Central Banks Interest Rate, % change



Economics

- ▶ The **US** economy continues to show strength. April job additions totalled over 263,000 with the unemployment rate falling to 3.6%, albeit because of a fall in the participation rate. The Fed left interest rates unchanged although Fed Fund futures pointed to one or even two possible cuts later this year despite wages and inflation remaining subdued. Housing starts were stronger than expected but on the downside, home prices rose just 2.7% in March, while retail sales fell 0.2% in April and manufacturing output fell 0.5%.
- ▶ **Eurozone** GDP bounced back in Q1 with 0.4% growth qoq against expectations of 0.3%. Germany also grew 0.4% as the temporary disruptions to its economy including the car emissions scandal and River Rhine drought abated. Italy exited a technical recession while Spain saw growth accelerate to 0.7%. Euro PMI data also firmed although remained in contraction territory. The UK's manufacturing PMI stayed expansionary but Services contracted slightly. Hopes of a smooth Brexit early in the month allowed the BoE to hint at higher interest rates later in the year just as UK GDP showed 0.5% qoq growth. This was despite inventory build taking a large slice of the growth ahead of what was thought to be Brexit day at the end of March.
- ▶ **China's** PMIs fell slightly in April although both manufacturing and service indicators remain in expansion mode. Industrial production data also missed expectations with 5.4% well under the expected 6.5%. Retail sales grew 7.2%, again below expectations for 8.6%. With further tariffs also being imposed on China's exports, most economists are expecting a further slowdown in broader GDP figures for Q2 and Q3.
- ▶ **Japan's** Q1 GDP growth of 2.1% qoq was higher than expected mainly because of lower imports which pointed to a weak consumer, and an inevitable weakening of growth further down the road. With the consumption tax still on the cards, the BoJ is expected to keep rates on hold for the foreseeable future, although analysts pointed to an escalating trade war as reason to postpone the tax's implementation.

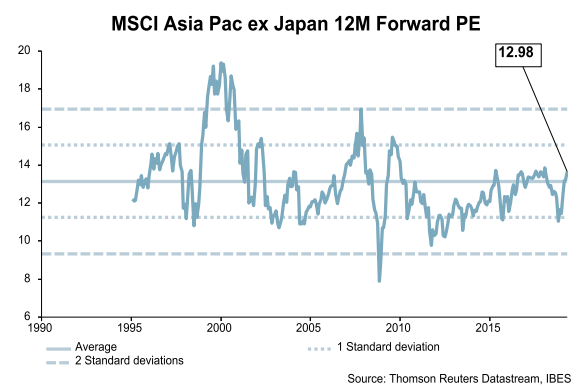
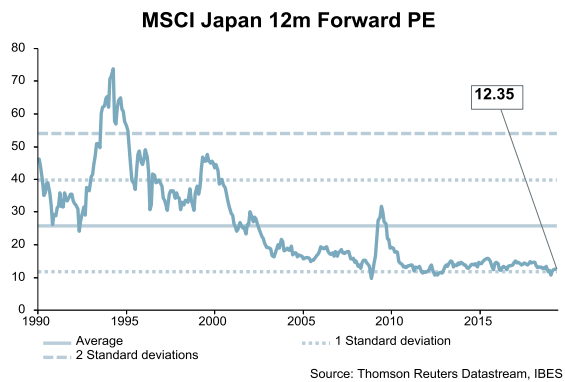
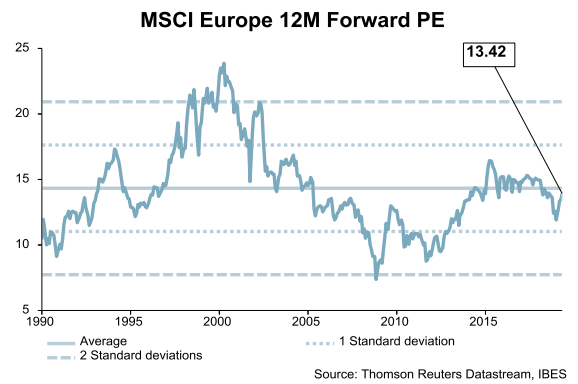
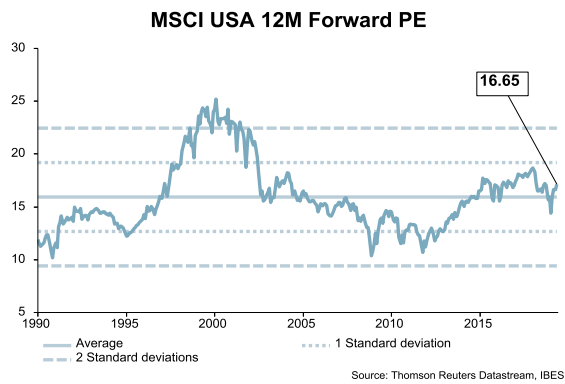
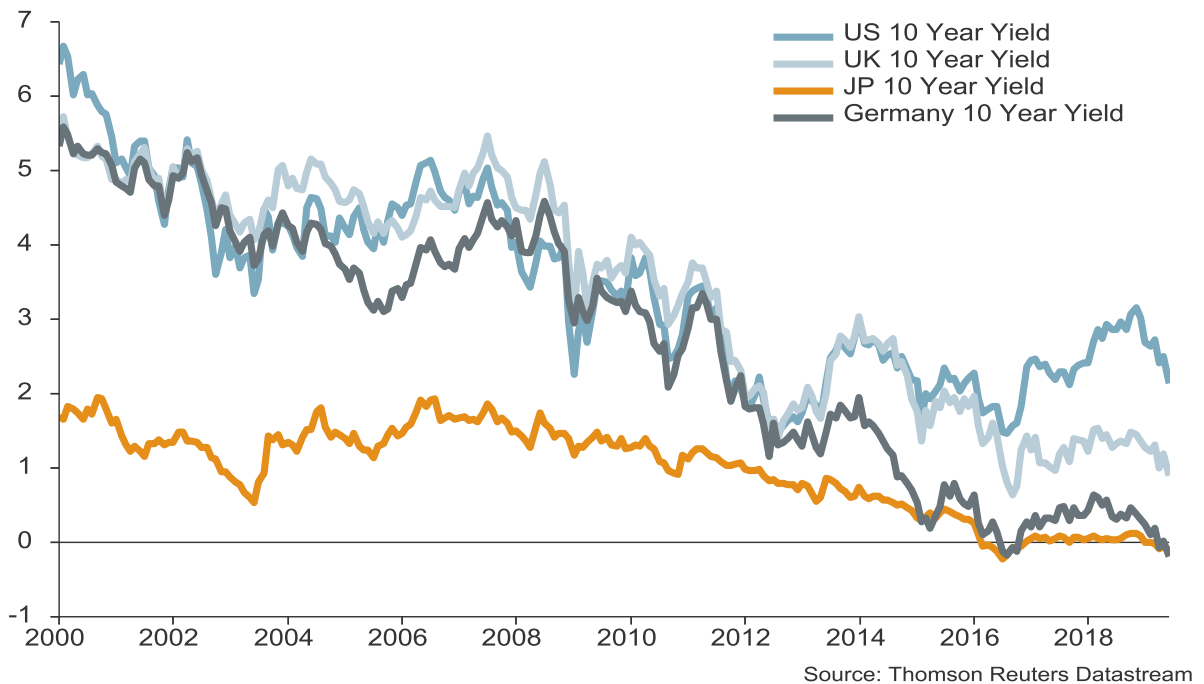


Fig 8. Key Bond Yields (%)



Source: Eastspring Investments. Chart data from Thomson Reuters Datastream as at 31 May 2019. For representative indices and acronym details please refer to notes in the appendix.



MSCI monthly, quarterly and year-to-date data

	May-19	Apr-19	QTD	Q1 19	YTD	Q4 18	Q3 18	2018
World	-5.8	3.4	-2.6	12.3	9.4	-12.7	4.4	-8.9
Developed World	-5.7	3.6	-2.3	12.6	10.1	-13.3	5.1	-8.2
United States	-6.3	4.0	-2.6	13.9	11.0	-13.7	7.5	-4.5
Europe	-5.3	3.7	-1.7	11.0	9.1	-12.7	0.8	-14.3
Japan	-4.0	1.4	-2.6	6.8	4.0	-14.2	3.8	-12.6
Emerging Markets	-7.2	2.1	-5.3	10.0	4.2	-7.4	-0.9	-14.2
Asia Pac Ex Japan	-6.9	1.8	-5.3	11.5	5.6	-8.8	-1.3	-13.7
Asia Ex Japan	-8.5	1.9	-6.8	11.4	3.9	-8.6	-1.5	-14.1
Latin America	-2.0	0.5	-1.5	7.9	6.3	0.5	4.9	-6.2
Brazil	1.7	-0.7	1.0	8.2	9.3	13.6	6.2	-0.2
EMEA	-3.6	5.2	1.4	5.6	7.1	-4.0	-1.4	-15.5
	Apr-19	Mar-19	Feb-19	Q1 19	YTD	Q4 18	Q3 18	2018
Australia	0.7	1.2	1.9	11.4	13.6	-10.0	-0.9	-11.8
New Zealand	-1.9	0.7	-1.3	16.9	15.4	-6.5	2.6	-3.5
Hong Kong	-6.7	1.1	-5.6	15.6	9.1	-4.5	-0.9	-7.8
China	-13.1	2.2	-11.1	17.7	4.6	-10.7	-7.4	-18.7
Korea	-9.3	0.4	-8.9	5.0	-4.4	-12.8	0.7	-20.5
Taiwan	-7.8	4.0	-4.1	9.0	4.5	-13.7	7.2	-8.2
Thailand	-2.1	2.0	-0.1	7.5	7.4	-10.2	13.7	-5.3
Malaysia	-0.7	-1.0	-1.7	0.3	-1.4	-5.8	3.8	-6.0
Singapore	-8.8	6.3	-3.0	6.2	3.0	-6.7	2.2	-9.4
Indonesia	-2.6	0.9	-1.8	4.3	2.4	9.8	2.0	-8.7
India	0.2	0.6	0.8	7.2	8.0	2.5	-2.3	-7.3
Philippines	0.8	1.5	2.3	8.0	10.5	5.4	1.1	-16.1
	Apr-19	Mar-19	Feb-19	Q1 19	YTD	Q4 18	Q3 18	2018
Mexico	-7.0	5.2	-2.2	5.6	3.3	-18.7	7.0	-15.3
Chile	-8.4	-1.9	-10.1	4.4	-6.2	-8.6	-1.9	-18.9
Hungary	-4.5	1.3	-3.3	6.0	2.5	5.9	4.7	-6.1
Poland	-4.2	1.3	-2.9	-0.6	-3.4	-2.9	11.1	-12.5
Czech Republic	0.2	-1.2	-1.0	3.8	2.8	-8.7	4.0	-2.2
Russia	3.6	3.8	7.6	12.2	20.7	-8.5	6.6	0.5
Turkey	-0.6	-3.6	-4.3	-3.0	-7.1	4.8	-20.5	-41.1
South Africa	-7.1	8.1	0.4	4.6	5.0	-3.7	-7.2	-24.3
Qatar	-5.3	5.3	-0.4	-3.5	-3.9	8.4	12.8	29.8
Saudi Arabia	-8.7	7.6	-1.7	14.9	12.9	-0.7	-2.9	19.2
United Kingdom	-6.0	2.3	-3.9	11.9	7.6	-11.8	-1.6	-14.1
Germany	-6.1	7.0	0.4	7.0	7.5	-15.5	-0.6	-21.6
France	-5.6	4.8	-1.2	10.8	9.5	-15.0	2.9	-11.9
Netherlands	-6.0	5.9	-0.4	13.6	13.1	-11.0	-1.4	-12.8
Austria	-8.0	6.2	-2.3	8.6	6.1	-18.9	0.8	-23.2
Italy	-7.7	2.2	-5.7	14.7	8.1	-11.8	-4.3	-17.0
Spain	-6.1	4.4	-1.9	7.1	5.0	-8.5	-2.3	-15.7

Source: Thomson-Reuters Datastream, MSCI. All data Total Returns, in US dollar terms, as of 31 May 2019

**KEY TERMS**

CA	Current Account
CBR	Central Bank of Russia
COPOM	Central Bank of Brazil
CPI	Consumer Price Index
DM	Developed Markets
ECI	Employment Cost Index
EM	Emerging Markets
EM Currencies	MSCI Emerging Markets Currency Index
EM Equities	MSCI Emerging Markets Index
EM Local Currency Bonds	JP Morgan Emerging Local Currency Bond Index
EM USD Bonds	JP Morgan Emerging Market Bond Index
EMU	European Monetary Union
EU	European Union
Fed	The Federal Reserve Board of the United States
FOMC	Federal Open Market Committee
GDP	Gross Domestic Product
Global Developed Equities	MSCI Developed Markets Index
Global Equities	MSCI All Country World Index
Global Government Bonds	Citigroup World Government Bond Index
IP	Industrial Production
M2	M2 Money
mom	Month on month
PBoC	Peoples Bank of China
qoq	Quarter on quarter
Repo	Repossession
SDRs	Special Drawing Rights
SELIC	Sistema Especial de Liquidação e C.U.S.todia (SELIC) (Special Clearance and Escrow System)
Tankan	Japan Large Business Sentiment Survey
TSF	Total Social Financing
UK	United Kingdom
yoy	Year on year

REPRESENTATIVE INDICIES

Aluminum	S&P GSCI Aluminum Index
Asia Local Bond (ALBI)	HSBC Asia Local Bond Index
Brent Oil	Cash settlement price for the InterContinental Exchange (ICE) Brent Future based on ICE Futures Brent index
Commodities	Datastream Commodities Index
Copper	S&P GSCI Copper Index
EMU 10 Year	Datastream EMU 10 Year
Global Emerging Bond	JPM Global Emerging Bond Index
Gold	S&P GSCI Gold Index
Japan 10 Year	Datastream Japan 10 Year
JACI	JP Morgan Asia Credit Index
MSCI Dev World	MSCI Developed Markets Index
MSCI EM	MSCI Emerging Markets Index
MSCI Europe	MSCI Europe Index
MSCI Japan	MSCI Japan Index
MSCI Latam	MSCI Latin America Index
MSCI Russia	MSCI Russia Index
MSCI U.S.	MSCI U.S. Index
MSCI World	MSCI All Country World Index
Steel (HRC)	TSI Hot Rolled Coil Index
UK 10 Year	Datastream UK 10 Year
U.S. 10 Year Treasuries	Datastream U.S. 10 Year Treasuries
U.S. 30 Year Treasuries	Datastream U.S. 30 Year Treasuries
U.S. High Yield	BAML U.S. High Yield Constrained II
U.S. Investment Grade	BAML Corporate Master
DXY	U.S. Dollar Index
Zinc	S&P GSCI Zinc Index



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