

MONTHLY REVIEW: Chippy Waters

November 2017

The World in five bullet points

- ▶ **Global Equity Markets** scaled new highs in November as solid economic figures, positive corporate earnings outlooks and constructive news on tax reform in the US propelled many markets to new highs. Developed markets outperformed Emerging Markets with the US indices outperforming Europe and yet, despite their subdued month, several Emerging Markets indices hit six-year highs while a few Asian indices rallied to their highest in a decade. The Bulls, for the meantime, stay in charge.
- ▶ **US tax reform** inched closer with several wavering senators declaring their intention to vote through the reform which would see a cut to corporate tax. Passage of the reform came on the first day of December, after the close of markets in the US, but prior to this markets had anticipated the bill getting through with the Dow Jones Industrial Average topping 24,000 for the first time and the S&P 500 hitting a record closing high on the final trading day for November.
- ▶ Political uncertainty returned to **Germany** when coalition talks between Chancellor Angela Merkel's conservative two-party bloc, the *Greens*, and a fourth group – the libertarian group the *Free Democrats* – collapsed. A snap general election in December is now possible although at the time of writing, coalition talks were continuing.
- ▶ Robert Mugabe's near four-decade rule of **Zimbabwe** came to an end after the army effectively seized power. A power struggle between Mr Mugabe's wife Grace, and former vice-president Emmerson Mnangagwa was largely to blame for the intervention, with the latter taking office at the end of the month.
- ▶ Is **Bitcoin** a Tulip in disguise? The largest cryptocurrency surged to more than \$11,000 per coin, around a 70% gain over a single month (depending on which exchange data one uses). At \$10,000, Bloomberg estimates Bitcoin has a price-to-earnings ratio of around 710x, versus a 175x multiple for the Nasdaq at the height of the internet boom.

Fig.1. Equity Indices Performance in USD (%)

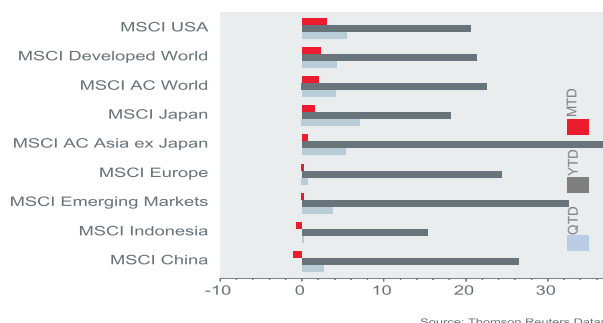
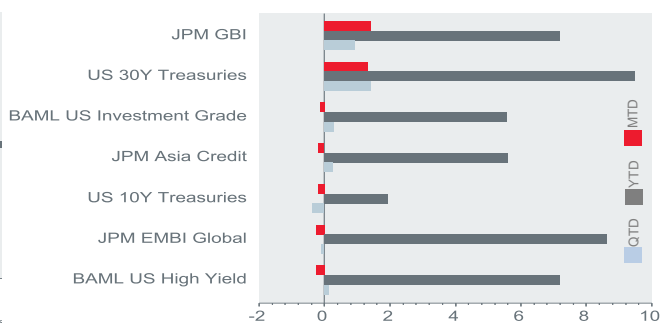


Fig.2. Bond Indices Performance in USD (%)



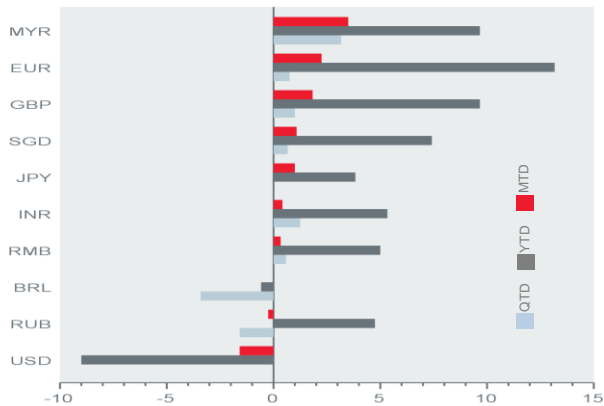
Equity Markets

- ▶ **Global View:** Emerging Market equities rose in US dollar terms in November - but fell in local currency terms – to underperform developing markets and in particularly the US, which in turn offset losses in Europe. Japan rose, China fell, and Latin America fell sharply. The complicated picture of the world's markets in November was reflected in increased volatility with the VIX index spiking late in the month. But in aggregate, global markets rose to continue their bull run – the US\$ MSCI World Index was up 2.2%.
- ▶ **US markets** outperformed largely because of the excitement generated by the prospects of tax reform, which even the most conservative commentators admit is positive for business, banks and the equity markets. The MSCI US index rose 3.0% to largely shrug off negative political developments for the President.
- ▶ **European markets** fell in November, weighed by pockets of political uncertainty in Germany (failure of coalition talks), Italy (election campaigns kicking off), and Spain (prospect of regional elections). The MSCI Europe (ex UK) Index fell 1.7%.



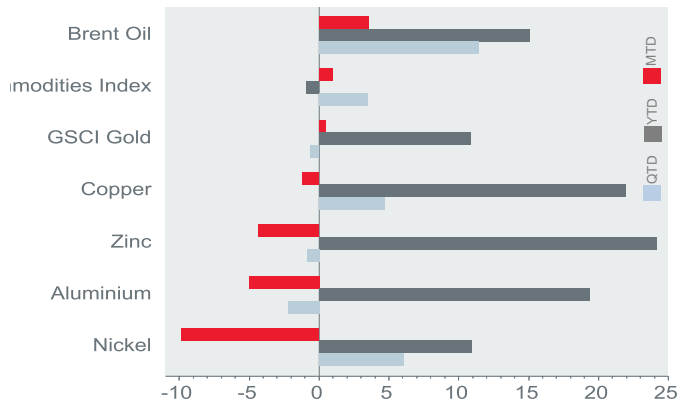
- ▶ **UK markets** also struggled. The modest bounce in the pound at the end of the month on the Brexit divorce bill breakthrough was not enough to offset continuing jitters surrounding overall Brexit negotiations and the strength of Theresa May's premiership.
- ▶ **Emerging Markets** almost everywhere had a volatile month with Hong Kong/China seeing sentiment peak mid-month with technology, insurance and consumer stocks leading, before state media's comments on Moutai's elevated share price caused selling pressure to take charge. Latin America fell sharply and underperformed other EM markets with Brazil suffering from fading hopes of social security reform and Chile falling on tighter than expected presidential elections.

Fig 3. Currencies Performance versus USD (%)



Source: Thomson Reuters Datastream

Fig 5. Commodities Performance in USD (%)



Source: Thomson Reuters Datastream

Currencies

- ▶ The **US dollar** weakened again in October with the yen and euro making modest gains despite some volatility in the dollar market during the month on speculation that interest rates in the US could rise faster than expected.
- ▶ The **UK pound** fell on growing worries over the future of Prime Minister Theresa May after two senior cabinet ministers were forced to leave and a third came under pressure to resign after a foreign policy blunder. News late in the month that the EU and UK had agreed on a 'divorce bill' over Brexit gave support to a modest rally.
- ▶ The **Euro** was boosted by robust German economic growth figures showing GDP growth of 0.8%, ahead of market expectations. The currency then slipped back on news of the failure of Angela Merkel to form a new coalition government after the liberal FDP Party pulled out of negotiations with Angela Merkel's conservative bloc, saying there was "no basis of trust" with Mrs Merkel.
- ▶ The **Aussie dollar** came under pressure when data showed the country's wages did not rise as much as expected in Q3. Later in the month, unemployment data for October showed a fall to 5.4%, its lowest level in almost five years, providing a base.
- ▶ The **Mexican peso** hit eight-month lows during the month as talks over the restructuring of NAFTA again hit the barriers amid tough US demands. At one point, the currency was down as much as 9% against the US dollar since September while the **Canadian dollar** had lost 5% before recovering slightly.

Commodities

- ▶ **Crude** jumped to two-and-a-half year highs at the end of the month as Canadian exports to the US dipped, partially the result of a leak in the Keystone pipeline while increasing signs the OPEC states were reining in production also provided support.
- ▶ Most metal prices fell during the month as fears grew of a slowdown in industrial production in China. **Nickel** had one of its worst weeks in five years at the end of November, while **aluminium** also fell sharply.
- ▶ In contrast, the crackdown on steel production in China also meant that inventory levels of **iron ore** have run down over the month, and subsequently prices continued to bounce back from year lows last month.



Fixed Income

- Yields on 2-year US treasuries hit a nine-year high with the spread to the 10-year paper narrowing to the lowest since 2007. At the beginning of the month, economic news was generally upbeat with retail sales beating forecasts and inflation creeping higher.
- US interest rates moved higher in this environment to almost fully price in a Fed rate hike in December, while the market-implied probability of multiple rate hikes in 2018 rose. But later, minutes of the October FOMC meeting revealed several members were concerned that inflation may remain lower than its 2% target for longer than expected. This triggered a softening of the upward trend in US Treasury yields and a broad weakness in the USD.
- Over the month, the 2-year US Treasury yield rose by 18 bps to 1.78%, while the 10-year yield increased by a modest 3 bps to 2.41%.
- In Asia, performance of USD-denominated bonds was weighed by the moderate rises in US interest rates. Strong supply of new issuances, as well as concerns over policy tightening in China, also dampened investor appetite and led to moderate widening in the credit spreads. Overall, the representative JPMorgan Asia Credit index fell by 0.2% in November.

Fig 6. OECD Composite Leading Indicator

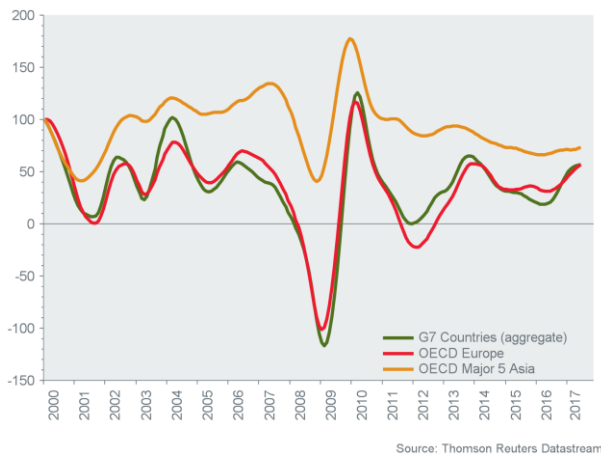
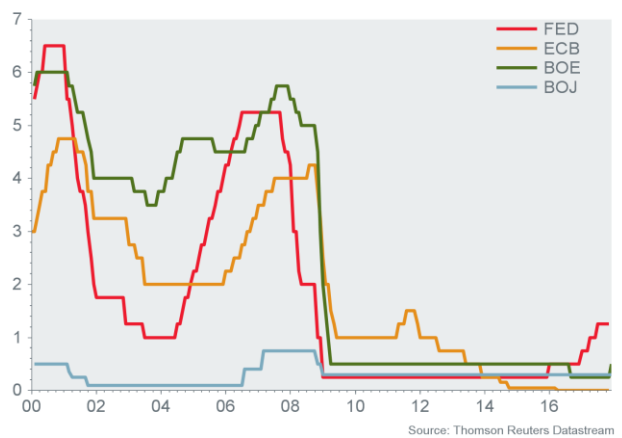


Fig 7. Central Banks Interest Rate (%) (Upper Band)



Economics

- US data** was mixed. New Orders fell unexpectedly in October weighed by defense and aircraft orders, while the University of Michigan consumer sentiment survey also dipped, against expectations. However, late in the month, consumer confidence surged to 17-year highs for November, while home prices for September rose sharply, further underpinning consumer confidence. Manufacturing PMI also stayed strong at 53.8, above the pivotal 50-point level.
- Eurozone** economic growth remained strong with third-quarter GDP growth data revised up to 2.5%, mostly pulled up by German growth mentioned below, but supported by encouraging figures from Italy and France. PMI data for Eurozone hit a record high of 60.1, unemployment fell to below 9% and consumer confidence hit a 16-year high, while core inflation remained at 0.9%.
- The **German** central bank said the economy there was set to expand in the fourth quarter, saying industrial figures were stronger than expected, while companies were struggling to find workers to satisfy orders. GDP growth figures for Q3 came in at a healthy 2.8%.
- For Emerging Markets, data was also mixed. **China** saw retail sales rising 10% in October and Industrial Production 6.2%, both under market forecasts. **Korea** raised its base rate by 25bps with indications from the central bank that “normalisation” would proceed gradually amid inflation figures that fell again in November. **Taiwan** saw Q3 GDP growth of 3.1%, driven by a surging export sector, unemployment fell again and CPI ticked down 0.3%. **India** received a ratings agency upgrade with Moody citing “continued progress on economic and institutional reforms” for its sovereign debt upgrade. Q3 GDP grew 6.3% year on year, in line with market expectations.



Fig 8. Key Regional Price to Earnings Valuations (x)

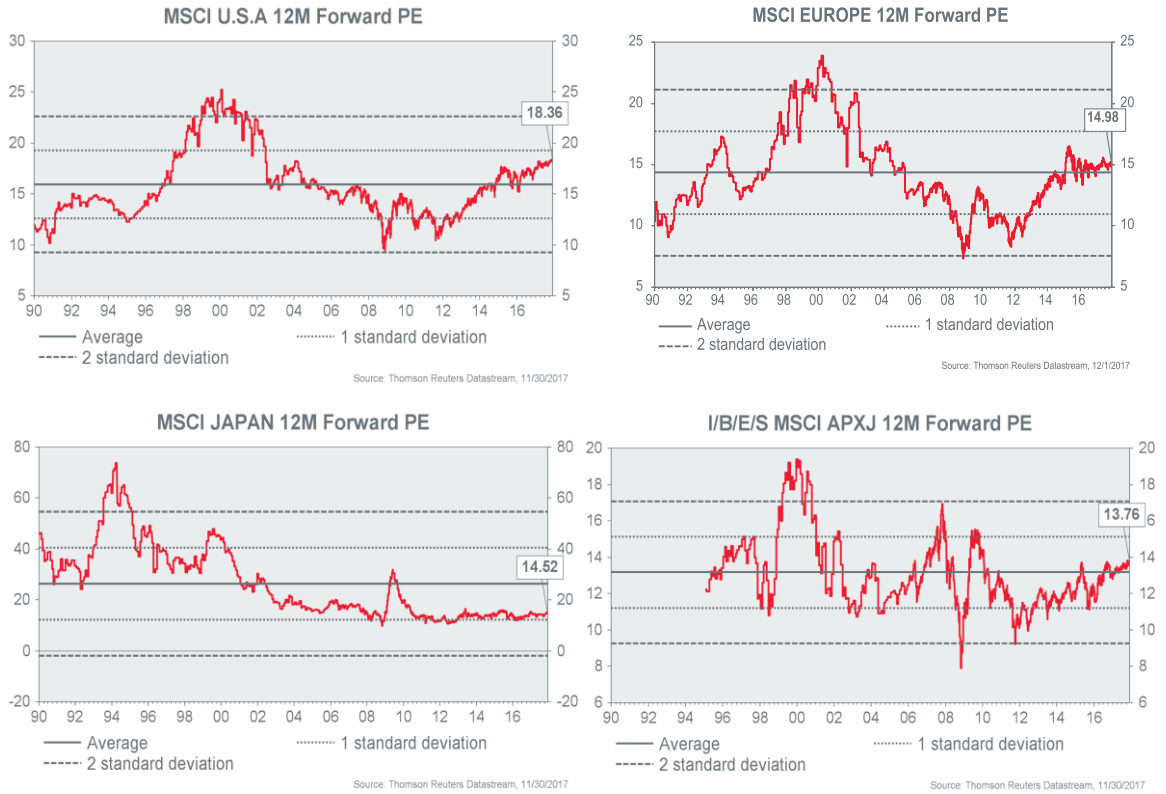
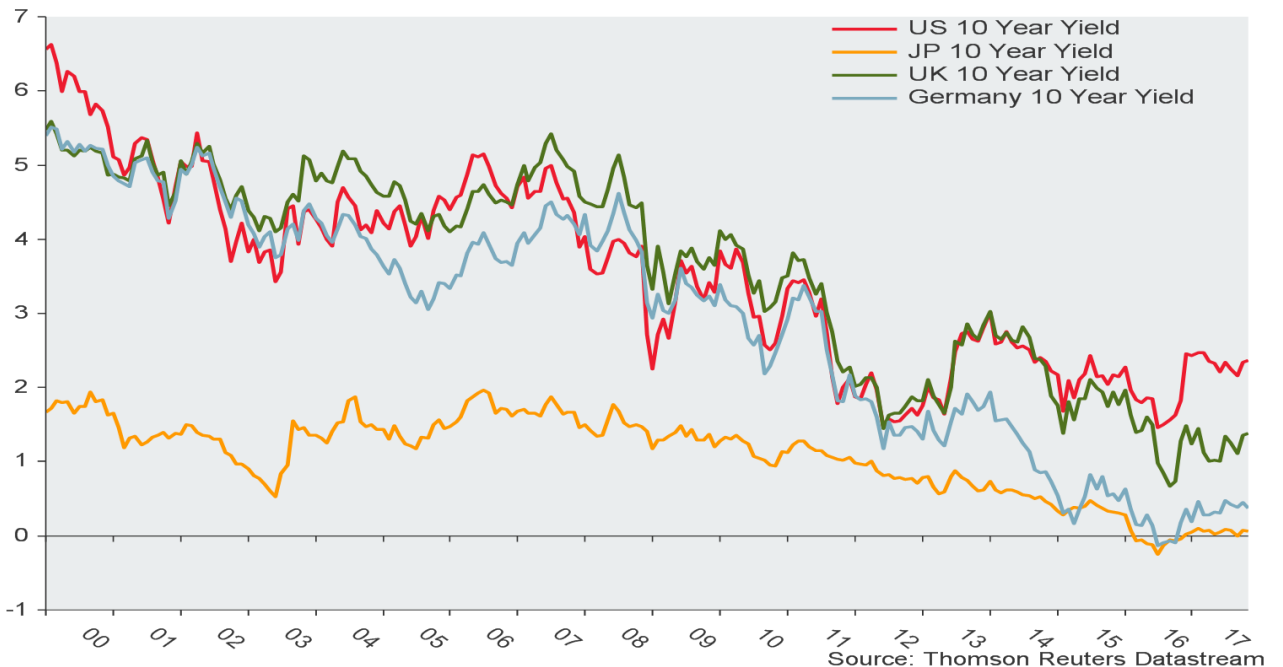


Fig 9. Key Bond Yields (%)



Source: Eastspring Investments. Chart data from Thomson Reuters DataStream as at 30 November 2017. For representative indices and acronym details please refer to notes in the appendix.

**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 CU.S.todia (SELIC) (Special Clearance and Escrow System)
Tankan	Japan Large Business Sentiment Survey
TSF	Total Social Financing
UK	United Kingdom
y/y	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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