Confidence must be earned

Amundi ASSET MANAGEMENT

Q3 2019

# Global Asset Classes in the Spotlight

## Top-Down Quarterly Assessment

*Strategy Research Team*

# Contents

# 01

# Setting the scene

# A widening gap between valuation and economic/corporate fundamentals

## High Conviction Ideas

- **Central banks** seems to be very concerned about the slowdown in the economic cycle sparked by trade tensions. As a consequence, they have been intensifying their communications about their willingness to act.
- While economic data fill up a mixed bag of signals, we are convinced that the **quality of growth** will likely lead to further economic weakness. However, we don't think a recession is likely in the next 12 months.
- Markets will need a **successful and consistent policy mix** (ie, fiscal and monetary accommodation) to enjoy a further boost.
- **Central banks are in a difficult position**. Market participants require intensified efforts that might come at the cost of credibility erosion for central banks or could increase the perception that central banks are not independent of the government. Furthermore, if central banks read something worrisome such as high refinancing needs on debt burden in the US, they might have to align monetary policy with fiscal policy.

## What to Watch

- US earnings reporting season
- Central bank meetings (Fed, ECB)
- Geopolitical tensions (Iran, Brexit, Italy)

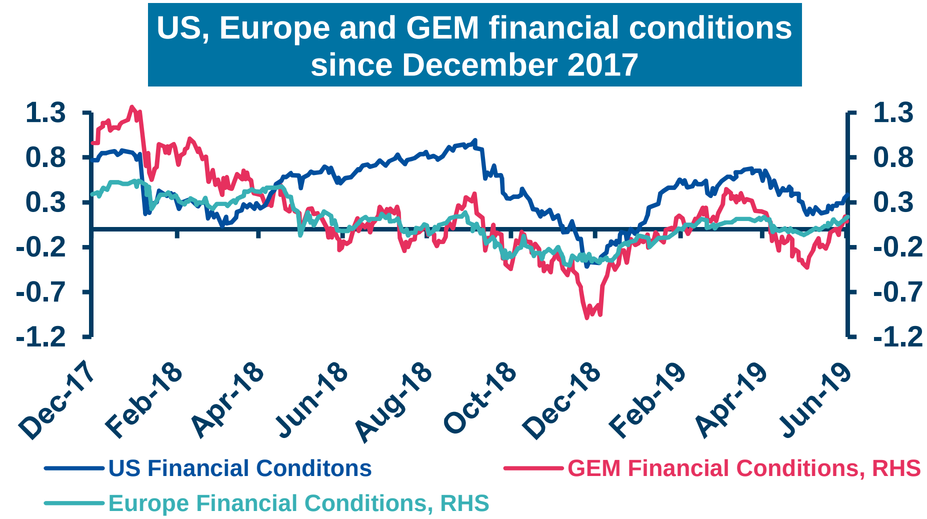
### Overall Assessment

We maintain a defensive stance, with a preference for high-yielding asset classes (IG, EM bonds). Corporate reporting season and monetary policy will be key

### Risks to Our Assessment

- Inflation surprises
- Monetary policy mistakes
- Debt concerns
- Liquidity risk
- Escalating tensions and political risks (trade, Eurozone)

**Global financial conditions bounced back into easing territory** as the markets read positively the constructive G-20 outcome. Tighter spreads, lower stock market volatility, a lower USD, and the perception of lower political risk regarding Italy (CDS ITA-GER) were the main drivers.



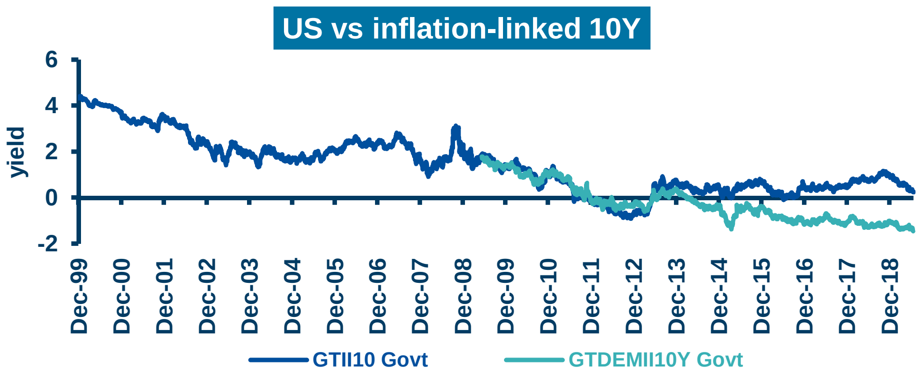

Source: Bloomberg, Datastream, based on Amundi Strategy Research calculations. Data as of 2 July 2019.

*"While overall financial conditions remained supportive of growth, those conditions appeared to be **premised importantly on expectations that the Federal Reserve would ease policy in the near term to help offset the drag on economic growth** stemming from uncertainties about the global outlook and other downside risks".*

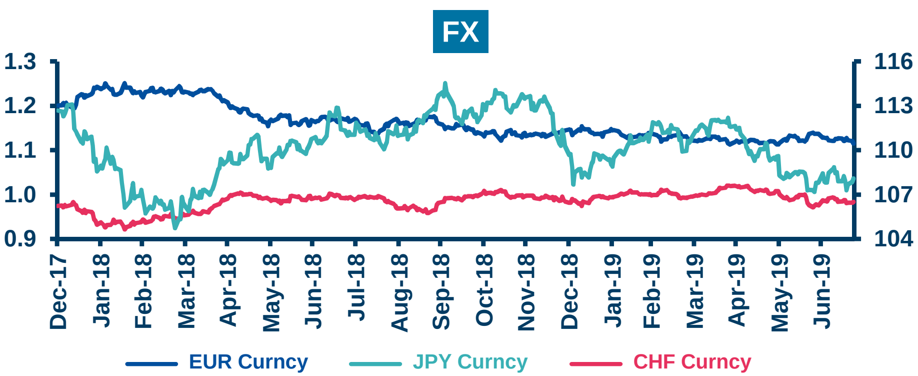
*Fed minutes, July 2019*

# Key Charts

**Real rates drift moved lower.** German real rates are still deep in negative territory and very close to all-time lows. US rates have been drifting lower YTD on falling nominal rates, due to a more dovish Fed.




**A deeper easing stance from central banks globally will affect FX dynamics.** While volatility is compressed, We expect the USD to be exposed to choppy devaluation in such an environment**.** The Swiss franc and the Japanese yen benefited from the negative risk sentiment and will continue to be supported, as US assets are less attractive.




**Volatility in financial markets remains compressed at a low level on a historical basis, notwithstanding the high level of uncertainty.** Central bank actions will likely affect the direction of FX and their levels of volatility.

# Global Asset Classes Views

July 2019

### CROSS ASSET

Remain constructive on risky assets (credit)  as CBs remain quite dovish despite some medium-term concerns regarding the economic outlook. Our central case is still for a late cycle phase, despite the tail risk of a slowdown (probably 20%). The equity rebound in June **closed the undervaluation gap opened in May. Current prices appear to have already discounted our central case 12 months FWD**, though some technical factors call for a rerating of risk in the short term. Q2 reporting season and PMI will be crucial for calling a structural change in risk sentiment.

### EQUITIES

A sharp rebound of equities in June, thanks to dovish turns by the ECB and Fed ("insurance" more than strong reflation), prolonged by the US-China "ceasefire" at the G-20 (only removing a tail risk). Manufacturing recessions without end-cycles are a classic phenomenon and the markets are betting on such an outcome, with P/Es back to the 20-CPI reference in the US, for example. In a positive outcome, there is little leeway to revise earnings up, as IBES is already forecasting +10% for next year on a global level, which should limit the upside. We keep our UW on Japan, which has been well rewarded, but with less conviction; as the G-20 meeting is behind us, the risk of an imminent sharp rebound of the yen is fading, while the possibility of last-minute agreement to postpone the rise of VAT can't be excluded. To balance this position, we open an OW on Pacific ex Japan, which could benefit from an improving economic picture in China in 2H while the relative EPS momentum is already recovering. In terms of styles, we stay quite balanced, preferring Quality to Growth and High Div and Min Vol to Value.

### FIXED INCOME & FX

On top of the accommodative policies delivered at its last meeting, at June's Sintra forum, the ECB "pre-announced" more easing to come. Among possible options available, the reopening of QE looks more likely than additional rate cuts into negative territory, unless a strong appreciation of the EUR takes place and/or the Fed cuts more than expected. Our central scenario is for one 25 bps pre-emptive rate cut in the coming months, with risks tilted towards further cuts in the next quarters, if domestic demand slows more than expected and/or in case of an unwanted tightening in financial conditions. We revised down our targets on US bond yields and expect a bull steepening likely to be triggered by Fed moves on rates. No EDP for the time being, supportive technicals, and the search for yield are likely to keep NTPs well bid. Despite strong recent performance, we maintain our positive view in BTPs. Credit markets are supported by even more favourable technicals, a possible CSPP re-opening, strong inflows, and generally sound fundamentals, together with low default rates. We still prefer high beta (BBs and BBBs) in Europe, and high grade in the US. On FX, if the Fed acts pre-emptively, the overvalued USD could loose ground in H2 2019. We remain negative on USD/JPY due to its hedging properties and given that global FCIs are deteriorating. TLTRO conditions should support peripheral banks and thus attract flows, but still-weak growth numbers, together with Italian political risk (and Brexit) will be a drag for the EUR.

### COMMODITIES

The overall commodity index moved down by 2.8% in June, as **manufacturing weakness hurt commodities demand expectations.** Oil bounced back 8%, due to tensions in the Middle East and OPEC activity, while US inventories stopped drifting higher.

While there are some concerns about economic conditions in the medium term (2020), overall the economic environment is supportive of the asset class. Ultra-dovish central banks and overall dollar weakness put financial conditions back on a supportive track. Gold rallied amid a risk aversion r**evamp and** going forward Fed dovishness will remain the strongest tailwind.

We keep our WTI range at USD55-65/bbl, given the OPEC's flexibility and willingess to stabilise oil and absorb any supply or demand shock.

Easing financial conditions and the end of the Fed's balance sheet reduction should underpin gold in 2019 while USD weakness should help gold valuations. Our **12M target** for gold is **USD1,450/ounce.**

Base metals will be affected by developments in China and a global economic slowdown. Overall, the picture still remains supportive of delivering decent returns as the inventories cycle remains reasonably supportive. We maintain the view that Metals should provide a 4-5% total return on a 12M horizon.





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# 02

# Assessment

## Spotlight on Global Asset Classes

# Cross Asset: seeking carry in a stretched late cycle

## High Conviction Ideas

- We continue to navigate this "late-late" financial cycle (that translates into a preference for risk assets to fixed income), but we are starting to include some deterioration of EPS in our forecast on milder revenue expectations. As a consequence, we forecast a growing probability of a slowdown*, with our forecast now requiring more defensive positioning.
- According to our models, the H1 equity rally closed the undervaluation gap after the December correction, but the rally needs a profits acceleration to be sustainable, which is not our central case, given weak manufacturing PMI.
- Historically, US manufacturing PMI levels (ISM @ 51.7, Markit 50.6) led flattish EPS growth (+3% on avg) in the 12M forward. Current analyst expectations are well above those reference numbers (at a rounded +13% yoy growth). However, should PMI remain weak, further downward revisions are likely and markets are likely too complacent on manufacturing recovery in H2 2019, in our view.
- Current PMI levels are more coherent with what FI market are discounting on Fed actions because historically in such weak PMI environments, the Fed has cut rates by 55bps on average.

## What to Watch

- **Trade** relationships (US/China)/confidence spillovers and eventually growth
- **US EPS reporting season** to confirm continuation of growth
- **Fed rate cuts going forward**

### Overall Assessment

Short-term positive momentum and relative value considerations due to dovish Fed are driving market rallies. Nevertheless, valuation and fundamentals are not supportive at current equity levels.

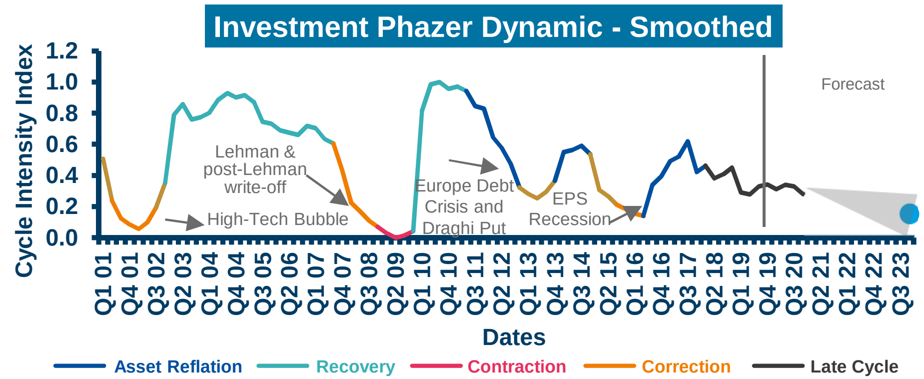
### Risks to Our Assessment

Too complacent markets as the priced in expectations on Fed delivery and manufacturing recovery are very high

Trade war concerns to trigger risky assets re-pricing of bond yields

Geopolitical tensions

While tracking the global economic picture, the **Advanced Investment Phazer** is still calling for a contained slowdown probability for the next 12M even if the downward trend for the next three years is confirmed.




The Advanced Investment Phazer is an analytical tool that deploys cluster-based algorithms (k-means) to wrap macroeconomic and financial variables, using global factors and local determinants. The Cycle Intensity index above summarises the historical turnover among the five identified financial regimes.

Source: Amundi Research elaboration as of end-June 2019.

| | | 12M FORWARD | | | |
|---|---|---|---|---|---|
| | | Avg. | Delta | PROBABILITY | |
| | PMI | EPS OP YOY | Delta Fed Rate | Profit Recession | Rate Cut |
| Reference | <50 | -7% | -125 bps | 65% | 70% |
| | 50-53 | +3% | -55 bps | 43% | 50% |
| | >53 | +17% | +95 bps | 5% | 13% |
| 30 June | ISM | **51.7** | | | |
| 30 June | Markit | **50.6** | | | |
| US op EPS yoy | | **13% E** | | | |
| 17 July | Market pricing Fed cut probability | | | | 100% |

Cluster analysis on US PMI manufacturing index (ISM and Markit) and US Operating EPS S&P 500. Sample: 1948-2019, monthly data).
Source: Amundi Research elaboration as of end-June 2019

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# Q3 2019 Cross Asset Assessment (model-driven)

Cross Asset BOX

| ASSET CLASS | ECONOMIC BACKDROP | VALUATION | RISK SENTIMENT | TECHNICAL | ASSESSMENT |
|---|---|---|---|---|---|
| Cash | | | | | − |
| Core Government Bonds | Medium/Poor | Medium | Medium/Good | Medium/Good | =/+ |
| Core Credit | Medium/Good | Medium | Medium/Poor | Good | =/+ |
| EM Bonds | Medium/Good | Medium | Medium/Poor | Medium/Good | =/+ |
| Global Equities | Medium/Good | Medium/Poor | Medium | Medium | = |
| Commodities | Medium/Good | Medium/Good | Medium | Medium/Good | =/+ |

Poor Medium Good

Source: This cross assessment is based on quarterly forecasts and analytical tools (factors) working on various frequencies. Results are then used for Strategy Research Cross Asset Portfolio allocation, used as a reference in the Multi Asset division. For further information and details, please refer to the Cross Asset Strategy team, Amundi Research.

All Data as of July 2019. Internal calculations.

# **Core Gov Bonds:** central banks in easing mode to keep rates low for longer

## High Conviction Ideas

- **Yields fell, with the decline driven by softer global growth and negative headlines about the trade war. On top of that, declining inflation expectations and central bank dovish rhetoric added downward pressure to core rates.** The German Bund yield moved to negative territory and touched new record lows. The US 10Y yield reached the 2% level, moving 60bps lower since the beginning of the year.
- Over the next 12 months, the **market is pricing in three to four rate cuts** (of 25bps each) **from the Fed and two cuts** (of 10bps each) **to the deposit rate from the ECB.**
- **We have lowered our targets on a one-year-forward horizon.** The US 10Y yield is now expected to reach 1.90-2.10%, with the Fed cutting rates at least once. Bull on the 2-10Y yield is expected to steepen, as the 2Y is seen at 1.40-1.60%. The German 10Y yield should remain in deep negative territory, at -0.25% to -0.15%, as the ECB is likely to deliver another round of QE, but unlikely to cut rates without a stronger EUR. Bull flattening is likely to continue on the German curve.
- **Italian debt to remain supported by the search for yield** and by the avoidance of the Excessive Debt Procedure. We hold a preference for the 5-10Y segment.
- **UK rates still very much dependent on the Brexit outcome.** Heightened political uncertainty to weigh on UK yields, which in the short term are likely to follow the trend lower currently in place on core sovereign rates. BOE on hold until more clarity is available on the future relationship with the EU.

## What to Watch

- Global growth and inflation expectations in the wake of more monetary policy support
- Corporate earnings growth
- Monetary policy delivery: whether market's expectations are going to be met
- Developments in US trade policies (towards China, but also the Eurozone)

### Overall Assessment

- Core yields continue to be driven lower by the expectation of more dovish measures to be undertaken soon by the main central banks
- Core bond yields are therefore set to remain low and peripheral bonds to continue to be supported by the search for yield

### Risks to Our Assessment

- Current trade tensions to worsen and escalation towards the Eurozone
- Political risk in Europe (Brexit, Italian 2020 budget)
- Monetary policy mistakes/mismatch between market's expectations and CBs delivery

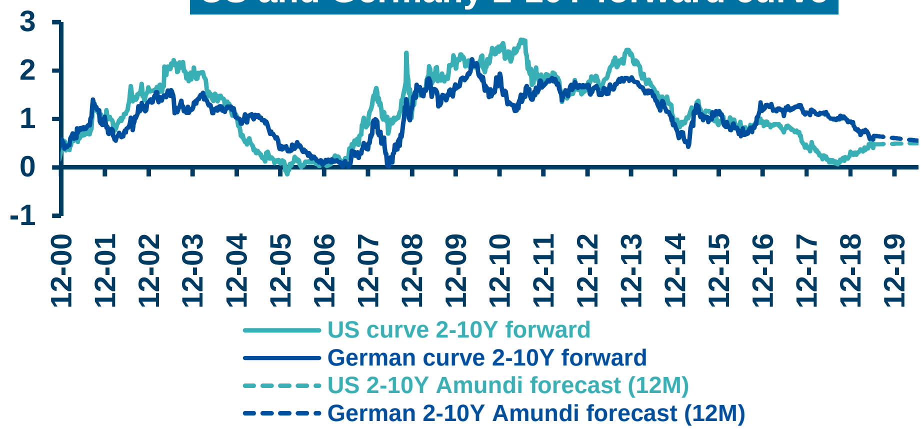
**2Y bond yield forecasts**

| | 28/06/2019 | Amundi + 6m. | Forward + 6m. | Amundi + 12m. | Forward + 12m. |
|---|---|---|---|---|---|
| **US** | 1.75 | 1.50/1.70 | 1.62 | 1.40/1.60 | 1.59 |
| **Germany** | -0.732 | -0.80/-0.70 | -0.78 | -0.80/-0.70 | -0.77 |
| **Japan** | -0.215 | -0.30/-0.20 | -0.24 | -0.30/-0.20 | -0.25 |
| **UK** | 0.617 | 0.55/0.75 | 0.51 | 0.45/0.65 | 0.49 |

**10Y bond yield forecasts**

| | 28/06/2019 | Amundi + 6m. | Forward + 6m. | Amundi + 12m. | Forward + 12m. |
|---|---|---|---|---|---|
| **US** | 2.03 | 1.95/2.15 | 2.06 | 1.90/2.10 | 2.12 |
| **Germany** | -0.31 | -0.20/-0.30 | -0.24 | -0.15/-0.25 | -0.18 |
| **Japan** | -0.16 | -0.20/0.00 | -0.11 | -0.20/0.00 | -0.07 |
| **UK** | 0.84 | 0.90/1.10 | 0.91 | 0.80/1.00 | 0.96 |

**US and Germany 2-10Y forward curve**




Source: Bloomberg, Amundi Research. Data as of 16 July 2019

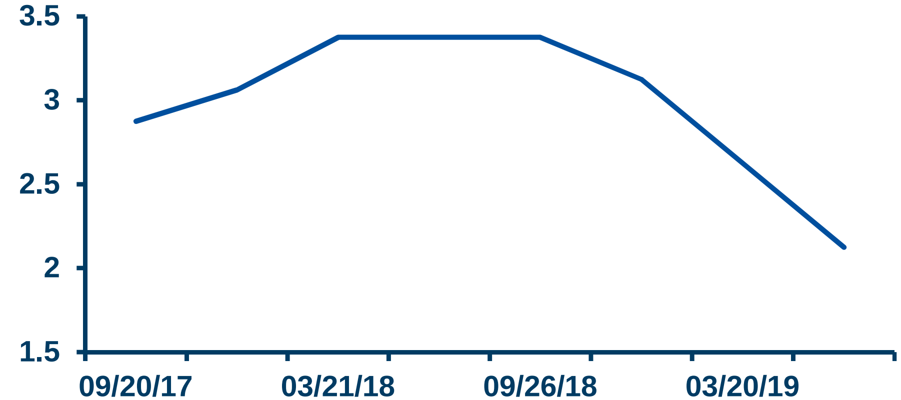
# Monetary policy views

GOVIES BOX

| | Central bank rates forecasts | | | | |
|---|---|---|---|---|---|
| | 28/06/2019 | Amundi + 6m. | Consensus Q4 2019 | Amundi + 12m. | Consensus Q2 2020 |
| **US** | 2.50 | 2.25 | 2.15 | 2.25 | 2.05 |
| **Eurozone** | 0.00 | 0.00 | -0.34 | 0 | -0.34 |
| **Japan** | -0.10 | -0.10 | -0.10 | -0.10 | -0.10 |
| **UK** | 0.75 | 0.75 | 0.80 | 0.75 | 0.90 |

- **Fed:** our central scenario is for one pre-emptive rate cut in July (by 25bps) with risks tilted towards further cuts in the next quarters in order for the Fed to maintain accommodative financial conditions and to keep US growth on track.
- **ECB:** the ECB pre-announced more easing on top the generous delivered TLTRO terms and material changes in forward rates guidance. Among possible options available, the re-opening of QE looks likelier than further rate cuts into negative territory, unless a strong appreciation of the EUR takes place and/or the Fed cuts more than expected. Among QE programmes, CSPP looks the easier to be re-opened.
- **BOE**: given that BoE's monetary policy will very much depend on the outcome of the Brexit deal, chances of a rate cut have increased, as Johnson's stance vs the EU is tougher than May's, and as major central banks turned more dovish.
- **BOJ:** the CB maintained forward guidance on policy rates, stating it would maintain ultra-low rates "at least through around spring 2020". BOJ appears in favour of a steeper yield curve to support the national pension system and fragile regional financial institutions through a reduction of outright purchases of the longer end.

**FOMC Median Dot end-2020**




Source: Bloomberg, Amundi Research

The chart shows that the U-turn in the Fed's stance has been rapid and continued in the last quarter:

Members revised down significantly their forward guidance on rates for 2020-end: in the last two FOMC meetings (March and June), the Fed cut median dots for next year-end by a full percentage point.

Despite this revision, the gap with market-implied rates remains wide.

Source: Bloomberg, Amundi Research. Data as of 5 July 2019

# DM Credit: the ‘desert of yield’ in the Eurozone supports spread products

### High Conviction Ideas

- **Q2 saw a strong recovery in credit markets, mainly driven by the more dovish stances of central banks: the search for yield is back as a driving force of tighter spreads in a low for longer yield scenario.**
- **Technicals** turned more supportive (ECB’s TLTRO reduces future supply from financials, intensifies the yield search, and on a relative basis, supports more periphery financials) while the Fed was credit friendly too, surprising on the dovish side.
- **Diverging fundamentals.** Earnings are still credit friendly in the US, confirming strong profits and supportive EBITDA growth. In the Eurozone, profits are less brilliant than in the US, but credit metrics show that companies’ leverage remains low. US and EUR HY distress ratios fell further in March, remaining consistent with a low default rate regime.
- **Valuations moved closer to fair value in Europe; tighter vs fair value in the US.** At the same time, on a relative basis vs safe havens, they look more attractive in the current “desert of yields”. US HY looks tighter vs other credit segments, US IG included.

### What to Watch

- European political risk (Brexit and European elections)
- Global trade tensions
- China and EM growth trends

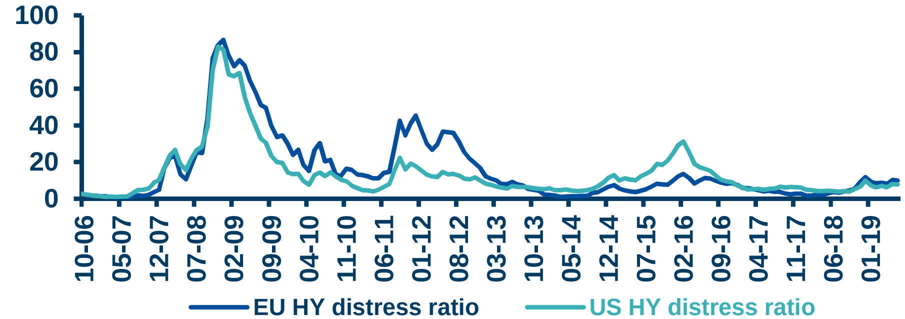
### Overall Assessment

- Monetary policy improved technicals while fundamentals look to offer some stabilisation
- However, we need to keep a strong focus on liquidity.

### Risks to Our Assessment

- Political risk (Brexit, European elections )
- Escalation in protectionism
- Further economic slowdown

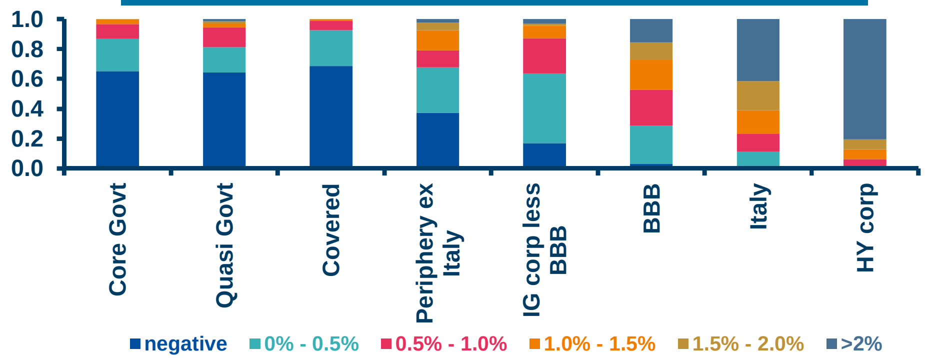
**Accommodative monetary policies keep distress ratios compressed**
In the last four months, European HY default rates remained at 0.9%, the lowest level in 10 years: low distress ratios by historical standards in both US and European markets will support the continuation of a benign default cycle in the next quarters.




Source: Bloomberg, Amundi Research

**In the Eurozone FI market, the “desert of yield” reached uncharted territory:** yield hunting accelerated in Q1 and is likely to stay. Italy, BBB corporates and HY bonds (overall accounted for roughly one-quarter of all outstanding debt) are almost the only remaining providers of positive yield.

**EUR fixed income debt: distribution by yield bucket for each asset class**

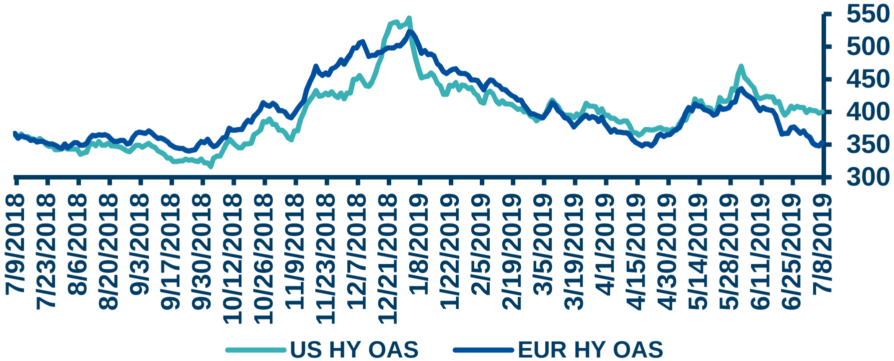



Source: Bloomberg, Amundi Research, as of 28 June 2019.

# Credit markets supported by CBs, search for yield to continue

GOVIES BOX

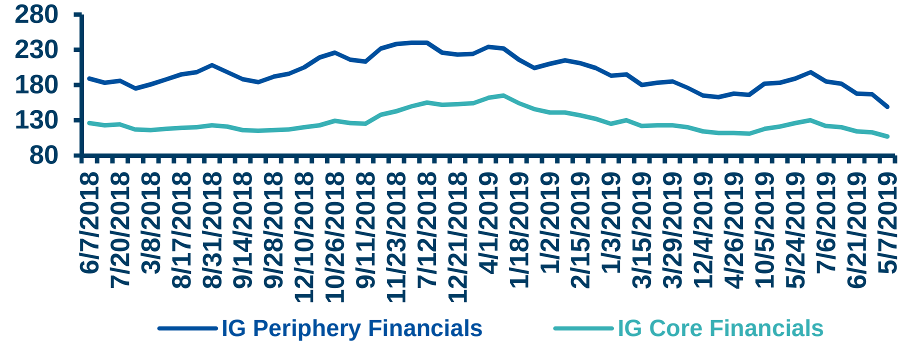
**EUR HY outperformed US HY,** supported by much stronger technical factors: negative rates, more easing from the ECB to come probably in the form of QE, search for yield supporting inflows into the asset class, periphery tightening




Source: Bloomberg, Amundi Research

**Peripheral financials outperforming core financials**

Supported by Italy's performance and search for yield, periphery financials were among the major drivers of positive performance in June, and are likely to continue to outperform in present environment

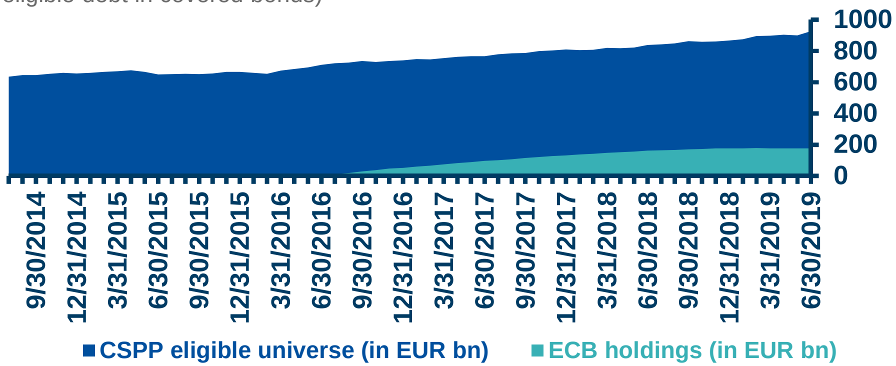



Source: Bloomberg, Amundi Research

**Technicals**

**Plenty of space for the ECB to re-open the CSPP among QE programmes**

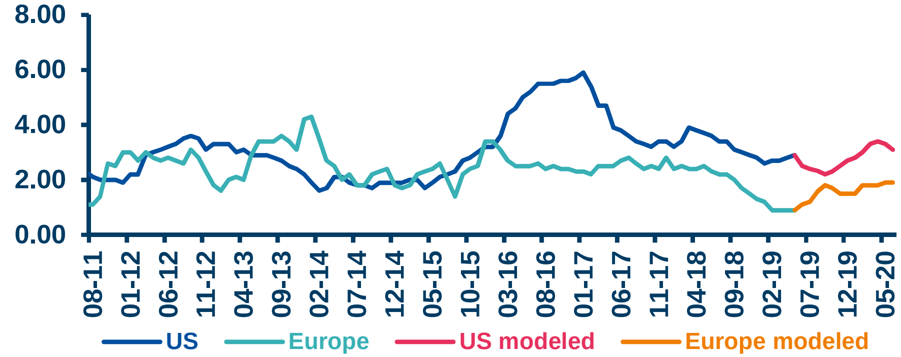
ECB holds less than 20% of the eligible universe of corporate bonds, the lowest proportion among ECB QE programmes (for example, ECB holdings are 40% of eligible debt in covered bonds)




Source: Bloomberg, Amundi Research

**Fundamentals**

Europe looks to be in a better position than the US in terms of prospective default rates: both areas should record only small rises in default rates in the next year




Source: Moody's, Amundi Research

# **DM FX:** USD choppy weakness to materialise in the short term

### High Conviction Ideas

- **DXY:** the USD is expected to weaken in the wake of the first rate cut from the Fed. Narrower rate differentials vs the rest of the G-10 should keep the currency under pressure in H2 2019. However, in the medium term, the USD is likely to remain attractive on a relative basis as the other major central banks are expected to follow suit on delivering policy rate cuts and as it's difficult to see any catalysts for global growth to bounce back.
- **EUR/USD:** the EUR should benefit from Fed easing and from the potential disappointment of market expectations of having a 10bps cut to the deposit rate by the ECB at the September meeting. Light EUR positioning and its undervaluation status reinforce this view (6M target @ 1.16). The dovish ECB stance will, however, work as a cap on any material appreciation. 12M target lowered from 1.17 to 1.14.
- **USD/JPY:** the JPY is expected to appreciate vs the EUR and the USD. A dovish Fed and the increased focus on the extent to which the economy will enter a more severe slowdown phase will keep the JPY bid. 12M target lowered to 105 from 107.
- GBP/USD: as the Brexit outcome is less predictable than ever and domestic conditions deteriorated sharply, we believe the currency cannot experience a sustained move towards its fundamental value. We lowered the 12M target to 1.28 from 1.37.
- When it comes to the Nordics, we maintain a positive view on the NOK: the currency remains undervalued and Norges Bank is the only CB which remains in a hawkish mood across the entire G-10 universe. Uncertainty on trade should put a cap on SEK appreciation in H1 2020.

### What to Watch

- Evidence of global growth bottoming out
- US-China trade negotiations and Brexit developments
- CB policy normalisation

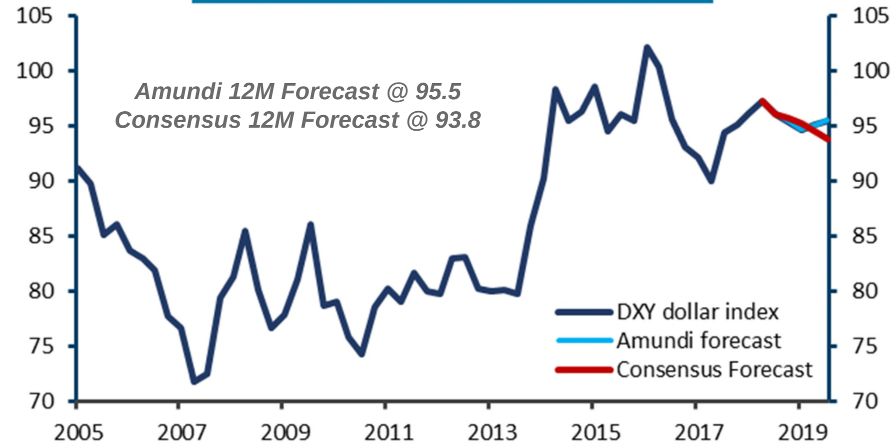
### Overall Assessment

- RoW's growth bottoming out vs US decelerating from 2018's peak and dovish FED the main headwinds to USD in 2019
- Risk positive assessment in H2 2019 to slightly moderate in H1 2020 as it's difficult to foresee catalysts for global growth to bottom out.
- Light positioning, Fed starting its easing cycle and EUR undervaluation would point to ST appreciation (next 6M). JPY to stay supported in the short term and to move higher in H1 2020

### Risks to Our Assessment

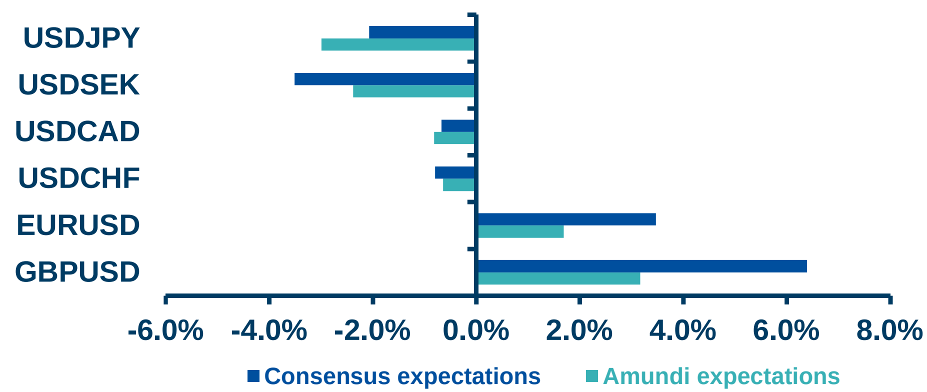
- Global economic recession, pushing the USD higher
- Material slowdown in Eurozone's economic growth
- Fed surprising market's expectations by providing fewer cuts than expected
- No deal Brexit

DXY Index expected to correct lower in H219



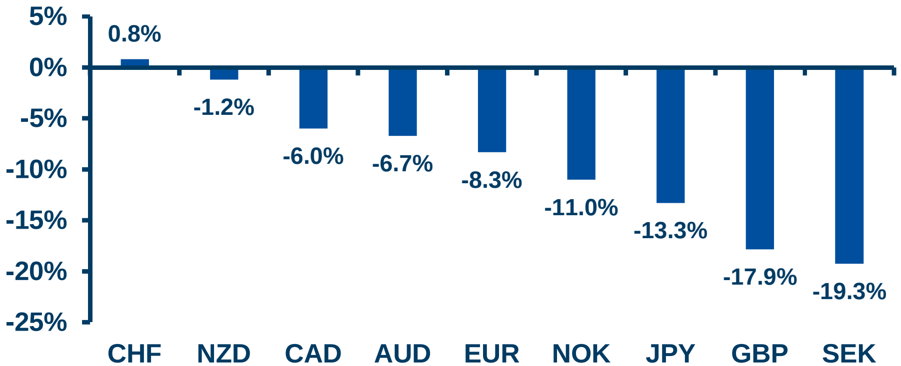

Source: Bloomberg, Amundi Research. Data as of 30 June 2019.

Dollar (DXY) CCY 12M expectations – Amundi vs Consensus



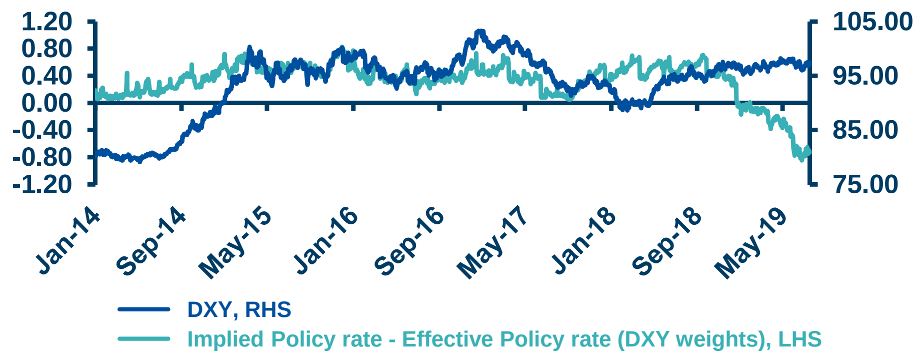
# US to lose ground in short term; difficult to see EUR sustaining upward trend; yen to appreciate further

From pure fundamentals, the USD remains overvalued vs the entire G-10 universe, except the CHF. Should global growth stabilise in the next months, this factor would point to lower a USD.



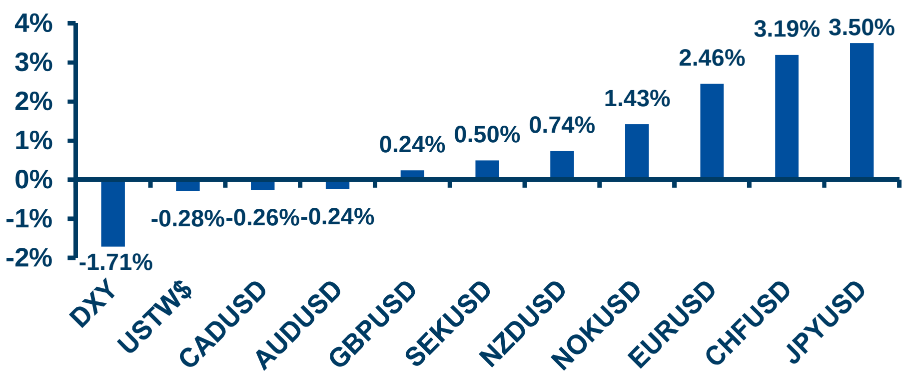

Source: Amundi Research, Bloomberg. Data as of 12 July 2019

Moreover, DXY index remained resilient in H1 2019 (+1.3% YTD, flat in Q2 2019) despite implied policy rate differentials with respect to the DM universe collapsing since the beginning of the year. **We expect DXY to correct in H2, as a more accommodative Fed should offset concerns over global growth in the ST.**




Source: Amundi Research, Bloomberg. Data as of July 16, 2019

**Economic growth that will be essential to understand the USD reaction to YC dynamics. Historically, the USD has tended to weaken in quarters when the US YC bull-steepened.**

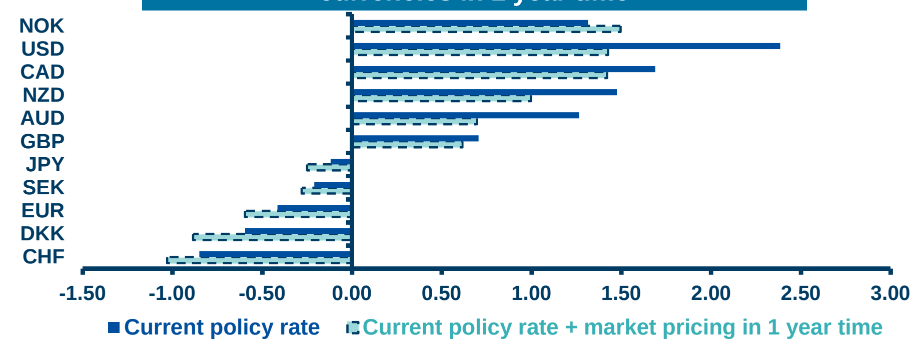



**Average FX performance in quarters with US YC Bull steepened since 1995.**

Source: Amundi Research, Bloomberg. Data as of 30 June 2019

**On the other hand, the USD will maintain its safe heaven asset with still attractive carry (i.e., among the highest yielding currencies in the G-10 space).** This is expected to partially offset USD negative factors.

**G10 FX: USD remaining among the highest yielding currencies in 1 year time**




Source: Bloomberg, Amundi Research. Data as of 28 June 2019

# Global Equity: at a crossroads!

### High Conviction Ideas

After a sharp drop in May, equities rebounded sharply in June, thanks to dovish turns by the ECB and Fed (“insurance” more than a sharp reflation), prolonged by the US-China ceasefire at the G-20 (only removing a tail risk, not a real game changer).

- **The 12M trailing PER of the MSCI World has rebounded** and now anticipates that with the support of the Fed, a manufacturing recession will be short-lived. **The perspective of an earnings revival remains crucial for confirming market expectations in this regard.**
- Our indicators are flagging **close to zero EPS growth this year**, which is not so different from IBES. However, consensus expects +11% for 2020, which leaves little room for positive surprises ahead.
- **We advocate for balanced positioning.** On regions, we prefer Pacific ex Japan to Japan. On styles, we prefer Quality to Growth and High Div and Min Vol to pure Value

### What to Watch

- Further negotiations around tariffs
- Brexit
- USD and industrial commodities
- EPS net up:  will the earnings downgrades stop soon?

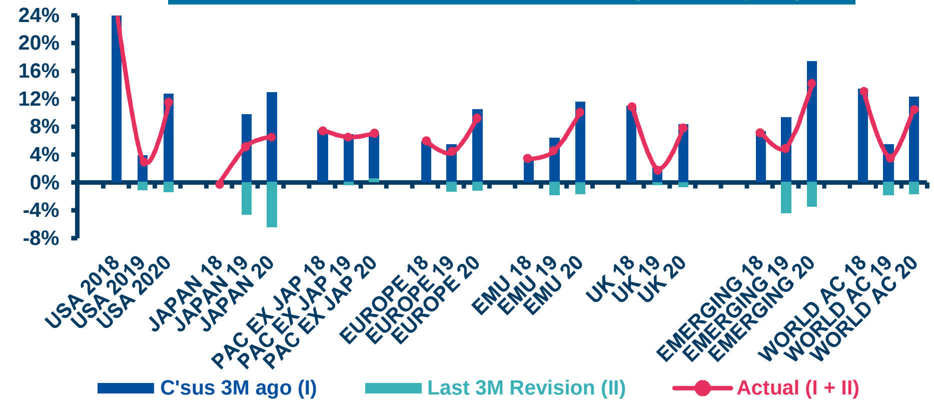
### Overall Assessment

No directional bets. Balanced positioning: prefer Pacific ex Japan to Japan, Quality to Growth, High Div and Min Vol to pure Value

### Risks to Our Assessment

- A very strong rebound of PMI’s
- A very strong monetary policy support

**MSCI indexes IBES consensus EPS growth by region**




Source: IBES consensus, as of 28 June 2019, Amundi Research

### Valuation multiples across regions and vs each market’s fundamental metrics (data as of 5 July 2019)

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| 12M FW PE | 13.1 | 17.2 | 13.0 | 14.0 | 12.9 | 11.2 | 11.6 | 17.6 | 12.6 |
| PBV | 1.8 | 3.5 | 1.2 | 1.6 | 1.5 | 1.2 | 1.2 | 2.9 | 1.7 |
| PSALES | 1.2 | 2.2 | 0.8 | 1.2 | 0.9 | 0.7 | 1.3 | 2.6 | 1.1 |
| PCF | 9.0 | 12.9 | 7.7 | 9.0 | 7.6 | 5.9 | 8.0 | 10.2 | 8.9 |
| DY | 3.6 | 1.9 | 2.5 | 3.2 | 3.2 | 4.1 | 4.4 | 3.1 | 4.5 |
| PEBITDA | 7.0 | 10.4 | 6.4 | 7.2 | 6.0 | 3.5 | 5.6 | 13.1 | 5.8 |

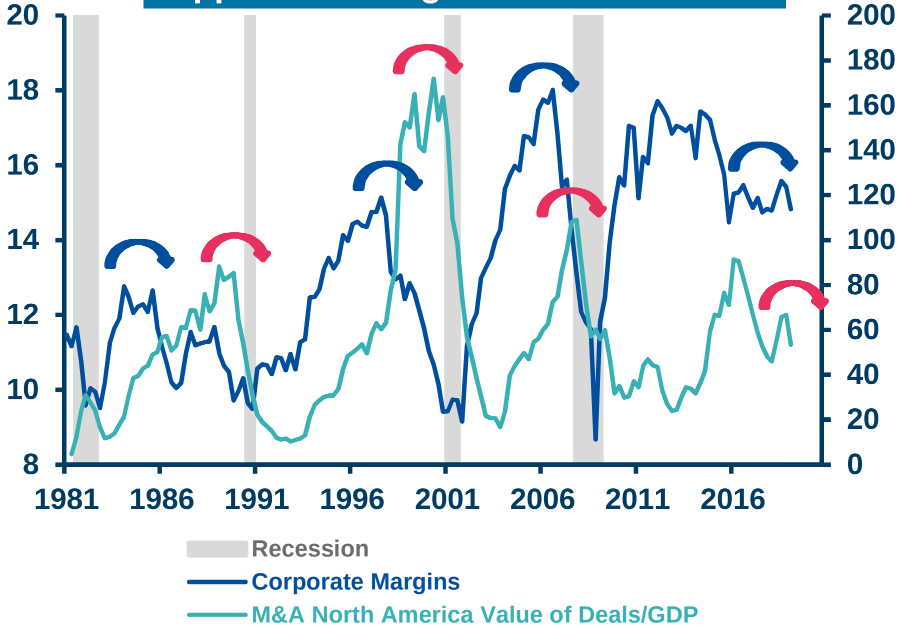
Very cheap   Cheap   Neutral   Expensive   Very expensive

Source: Analysis by Amundi Research. Colour stands for each market relative to its own history over a 10-year period. Ratios are classified by percent rank from 0 (Very cheap) to 100 (Very expensive) with an incremental step of 20. The 12-Month Forward price/earnings (12M FW PE) is the ratio of a company's market share price (share price) compared to its 12M FW earnings. The price/book value (PBV) is the ratio of the share price over its book value of equity. The price/sales (PS) is the ratio of the share price to its revenue per share for the trailing 12 months. The price/cash flow (PCF) compares the share price to its level of annual cash flow. Dividend yield (DY) is the annual dividends per share divided by the share price. The price/EBITDA (PEBITDA) compares the share price to earnings before interest, taxes, depreciation and amortisation. List of indices: S&P 500 for the US, MSCI for the other Countries and Europe

# A mature cycle. What about a last up move in this cycle?

DM Equity BOX

## Toppish US margins and slower M&A

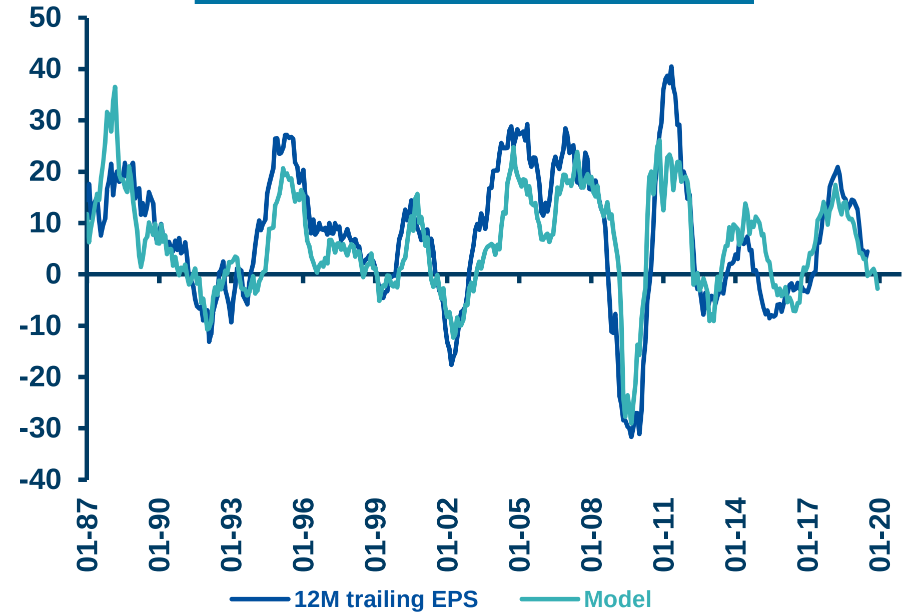



US margins peak in the H2 2018, which is usually a mark of cyclical maturity. This sign is usually confirmed by the weakening of M&A. This is happening this time again.

This configuration can nevertheless leave some time for a prolongation of the cycle. In this respect, the G-20 and the decision of the Fed to provide some insurance cuts are more than welcome.

Source: Datastream, Amundi Research; 8 July 2019

## Earnings prospects for this year




A simple model, based on the CRB industrials, USD, equity/bonds and ISM manufacturing are flagging circa zero earnings growth this year.

For earnings to grow up again next year, the ISM manufacturing index will have to bottom out, as will the CRB industrials, and the USD will have to weaken. Stay tuned.

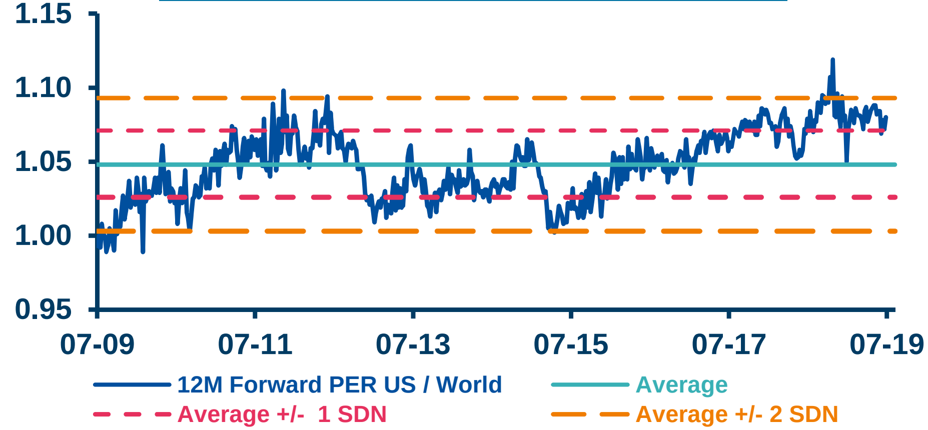
Source: Datastream, Amundi Research; 8 July 2019

# US Equity: still on top of the world!

## High Conviction Ideas

- **Valuation**
  The US market is still outperforming for good reasons, as earnings momentum is still more powerful than elsewhere. This means that if the relative PER remains more than one standard deviation above the average, it has been able to stabilise.
- **Fundamentals**
  The fading of US fiscal reform and the slowdown of the economy have led EPS to be revised sharply down (-4.4% over the last six months). IBES now expects +3% for 2019 and +11% for 2020, slightly above MSCI World (+10.7%)
- **Technicals**
  The S&P 500 is rising to new highs.
- **Style/Size/Factors**
  We keep a balanced positioning, preferring Quality (beware nevertheless of valuations) to Growth, High dividends and Minimum volatility to Value

**S&P 500 / MSCI World: Forward PER**

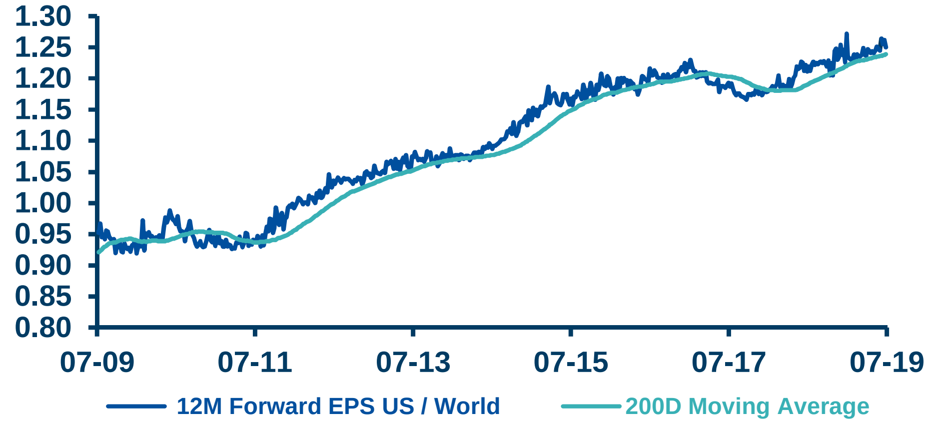



Source: Datastream, Amundi Research; 8 July 2019

## What to Watch

- The current earnings season: will earnings downgrades stop?
- Fed "insurance cut" to come. Will this be enough?
- The development around IT (still leading in the rebound)

**S&P 500 / MSCI World: 12M Forward EPS**




Source: Datastream, Amundi Research; 8 July 2019

### Overall Assessment

Neutral. US EPS momentum and tech leadership are providing some support, but the US remains more expensive than the rest of the world

### Risks to Our Assessment

- If IT was to strongly underperform
- On the opposite, very low rates and ISM for much longer leading to a prolonged outperformance of Growth/Value




Amundi ASSET MANAGEMENT

# EMU: still too early for a European moment

## High Conviction Ideas

- **Valuation**
  The relative PER is still below average, but the political risk (Italian budget, Brexit) requires a risk premium. In this cycle, the MSCI EMU has outperformed for six months on several occasions. Such a moment may be approaching, should a rebound in manufacturing and bond yields happen.
- **Fundamentals**
  Earnings have been revised down even more than in the US (-5.3% over the last six months). Remember that the manufacturing recession (PMI<50) which started in EM has expanded to EMU, but not yet to the US. For 2020, IBES forecasts a rebound of +10% (<US).
- **Technicals**
  MSCI EMU has built new highs for this year.
- **Style/Size/Factors**
  As for the US, a balanced positioning: Quality, Min Vol and High Div.

## What to Watch

- The earnings season: will earrings downgrade stabilise?
- A too strong rebound of the EUR would be a headwind
  Look at ECB reaction
- Political developments (Brexit)
- EMU is vulnerable to external shocks (oil, China, US, trade war)

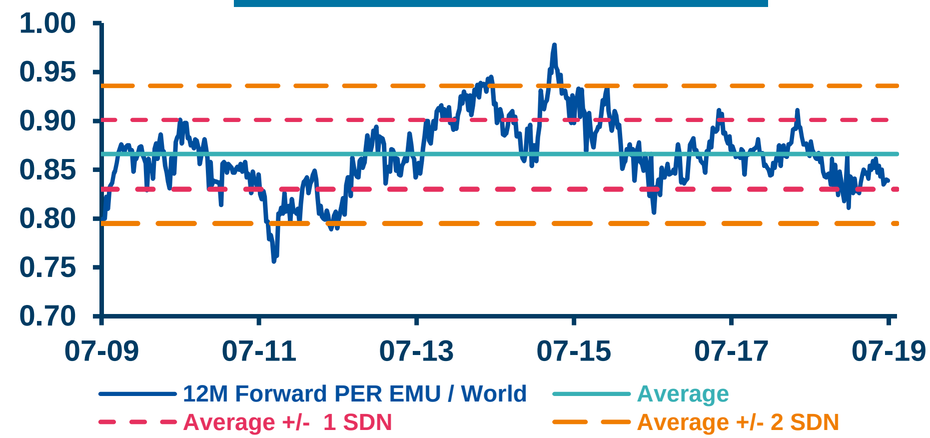
### Overall Assessment

We are Neutral on EMU. Attractive valuation, but catalysts are still missing

### Risks to Our Assessment

- A strong revival of China and global growth
- An external shock or a wrong end-game on Brexit

**MSCI EMU/World Forward PER**




Source: Datastream, Amundi Research; 8 July 2019

**MSCI EMU/World: indices and 12M forward earnings prospects**


Source: Datastream, Amundi Research; 8 July 2019

# UK: Brexit is still uncertain and thus disturbing

### High Conviction Ideas

- **Valuation**
  With a relative P/E two standard deviations below its average, valuation looks attractive, but the political situation (Brexit) still warrants a risk premium.
- **Fundamentals**
  EPS growth should be among the weakest in the world in 2019 (+2%, according to IBES). This typical late-cycle play – a proxy of Energy/ Industrials and with a high DY (5,3%) – would nevertheless suffer if the cheap GBP were to rebound (80% of sales are internationals).
- **Technicals**
  Even if underperforming the MSCI World, the FTSE 100 is building new highs for this year.
- **Style/Size/Factors**
  As elsewhere, Growth is very much outperforming Value.

### What to Watch

- The earnings season
- Bond yields (key, given UK's high DY) and GBP (key for EPS)
- MSCI Europe Energy/Industrials
- Brexit negotiations

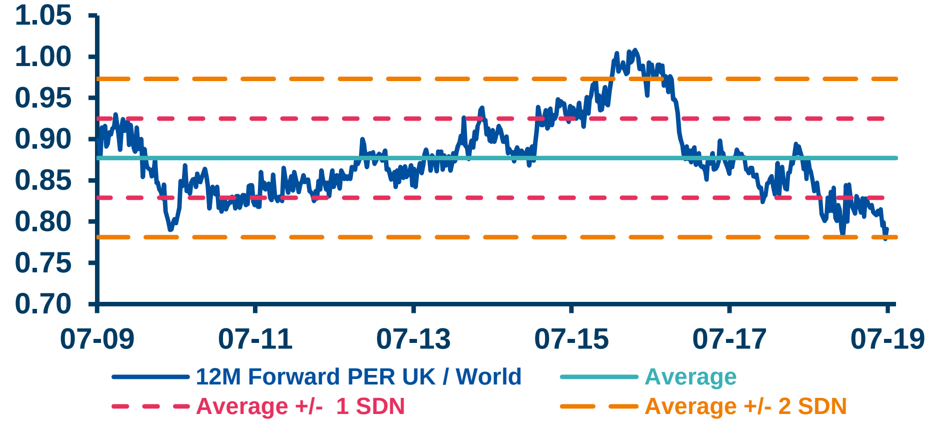
### Overall Assessment

We are neutral on the UK as Brexit outcome is still unknown

### Risks to Our Assessment

- A sharp move of the GBP, one way or the other
- A strong rise in bond yields

**FTSE 100/MSCI World Forward PER**




Source: Datastream, Amundi Research; 8 July 2019

**MSCI UK/ EUROPE and MSCI EUROPE Energy/Industrials**


Source: Datastream, Amundi Research; 8 July 2019

# Japan: underperformer

## High Conviction Ideas

- **Valuation**
  The Japanese market is very cheap. The PER and the P/BV are below average compared to the MSCI World while the political situation is clearer than it is for Europe, and corporate governance has improved.
- **Fundamentals**
  EPS growth has been revised sharply down (by -8% over the last six months). The relative EPS momentum is on a downtrend. Should the VAT hike expected for October be postponed, this could create a positive surprise.
- **Technicals**
  Japan is trending down in relative terms. The relative performance very much depends on the inverse performance of the yen, which is cheap and could rebound on external shocks. (this risk is fading in the short term after the G-20).
- **Style/Size/Factors**
  Growth is the only factor really outperforming. Min Vol is cheap.

## What to Watch

- Chinese economic support
- The earnings season: will the EPS downgrades bottom out?
- If the BoJ were to remove monetary accommodation (impact/yen).
- If the VAT hike were to be postponed (would be positive)

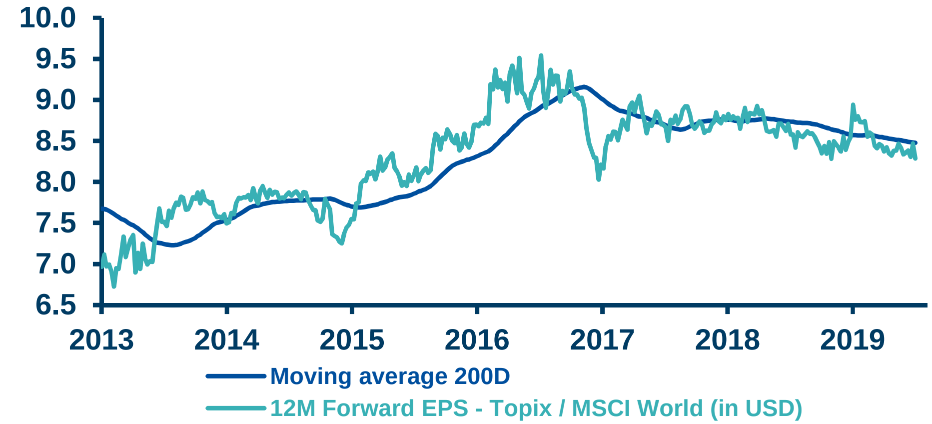
### Overall Assessment

We underweight Japan given the negative relative trend in earnings and the asymmetry of reaction of the yen which could gain more than it can lose

### Risks to Our Assessment

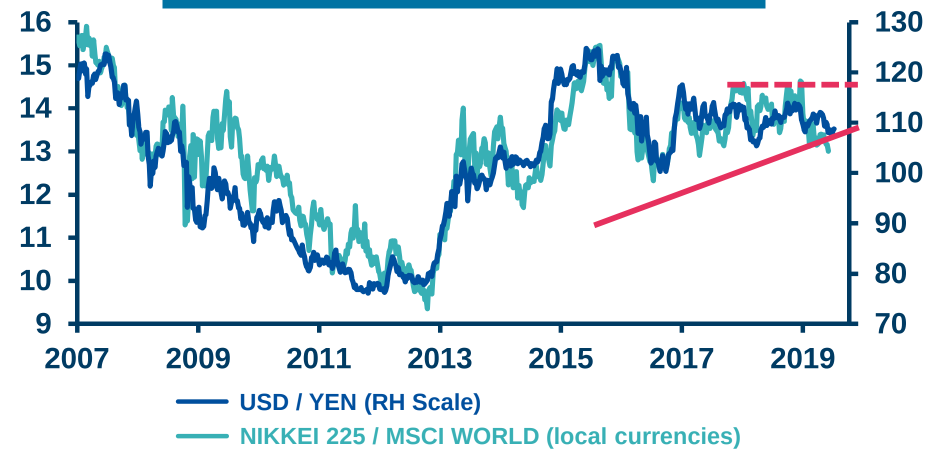
- A sharp decline of the yen (this risk increase after the G-20)
- If the VAT hike were to be postponed (surprising last-minute decision)

**TOPIX/MSCI WORLD 12M forward EPS**




Source: Datastream, Amundi Research; 8 July 2019

**TOPIX/MSCI WORLD and USD/YEN**




Source: Datastream, Amundi Research; 8 July 2019

# Pacific ex Japan Equity: some hope

### High Conviction Ideas

- **Valuation**
  Pacific ex Japan relative PER is neutral in relative terms vs MSCI World. But, the good momentum in terms of relative rerating has some room to expand above the average.
- **Fundamentals**
  The relative trend of EPS is improving. The region could benefit from some recovery from China, some bottoming out of industrial commodities or weakness of the USD. However, EPS momentum is still fragile. The chart to the right illustrates how difficult it was for the earnings momentum to last long in the past.
- **Technicals**
  MSCI Pacific ex Japan has been in a relative downtrend since October 2009. It is tempting to inverse this trend as it did early 2016 for six months and in 2012 for one year.

### What to Watch

- The earnings season, as everywhere
- China/commodity complex/USD
- Further discussions between China and the US on tariffs

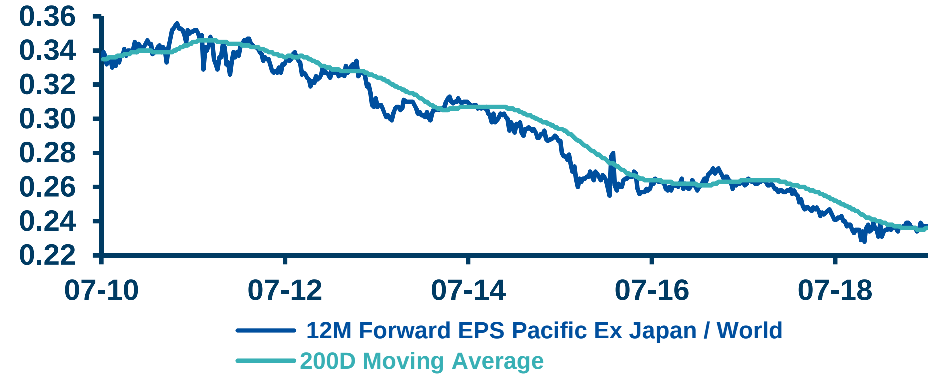
### Overall Assessment

Having a positive watch so far, we upgrade this region, hoping for positive influence from US-China talks and a slightly encouraging G-20 outcome.

### Risks to Our Assessment

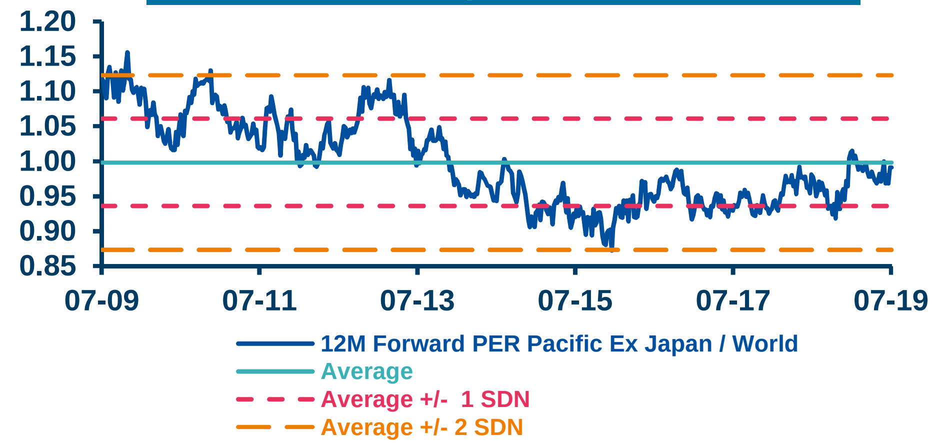
- A strong rise of the USD and/or collapse of commodity prices

**MSCI Pacific ex Japan/MSCI WORLD EPS (in USD)**




Source: Datastream, Amundi Research; 8 July 2019

**MSCI Pacific ex Japan/MSCI WORLD PER**




Source: Datastream, Amundi Research; 8 July 2019

# Emerging Market Equity: selectivity is key

### High Conviction Ideas

- **Valuations:** deterioration in GEM aggregated upside on a 12-month horizon from +4% to -1%, due to the positive performance seen in June. Selectivity is key.
- **Fundamentals.** For the next 12 months, we see a stabilisation of earnings growth to a low-single-digit number (+2.5%). EPS growth consensus expectations are stabilising at +9%. The trailing data are deteriorating (yoy growth at -7%). Earnings revisions are still negative, and the recent recovery has ended. We saw further deterioration in revisions in Latam and Asia, some marginal improvements in EMEA.
- **Sentiment:** GEM positioning (institutional investors) is still light.
- **We prefer to be selective.** Some themes to play: 1) DPS growth increased strongly in GEM and is expected to improve further. DY and DPS growth expectations can be two good factors to play in a late cycle scenario. These two factors are particularly supportive for some countries, like Poland, India, Mexico. 2) We still think that China and domestic stories in Asia are attractive. China is going to accelerate fiscal and monetary stimulus, and this could be particularly positive for the region. But, if trade talks further derail in the next weeks, we would prefer to play some domestic and insulated stories (like Philippines and India).

### What to Watch

- **Protectionism and politics** (geopolitics, reforms and elections, for example, in Brazil and Mexico; trade war tensions). Deceleration in global growth needs to be monitored
- **Commodity prices:** a strong rally could hurt Asia, but a further deceleration coming from a global slowdown is negative for all the asset class
- **Fed** rate hike and USD appreciation

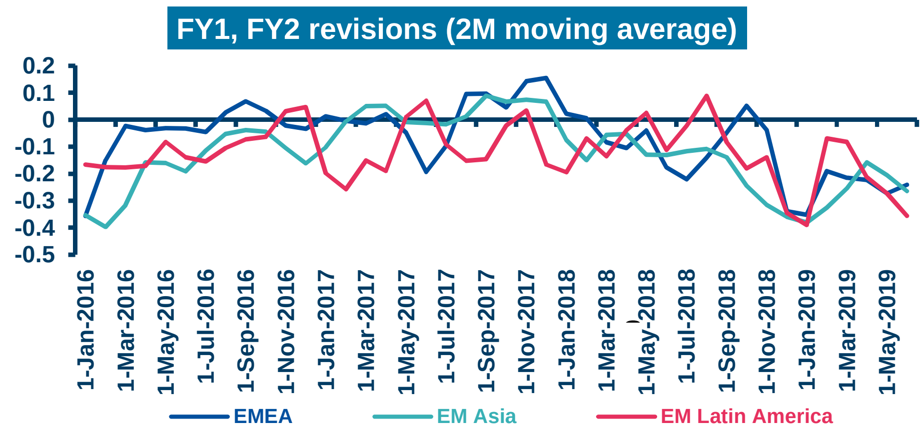
### Overall Assessment

Our overall view on EM equity is mainly neutral from current levels. Selectivity is key

### Risks to Our Assessment

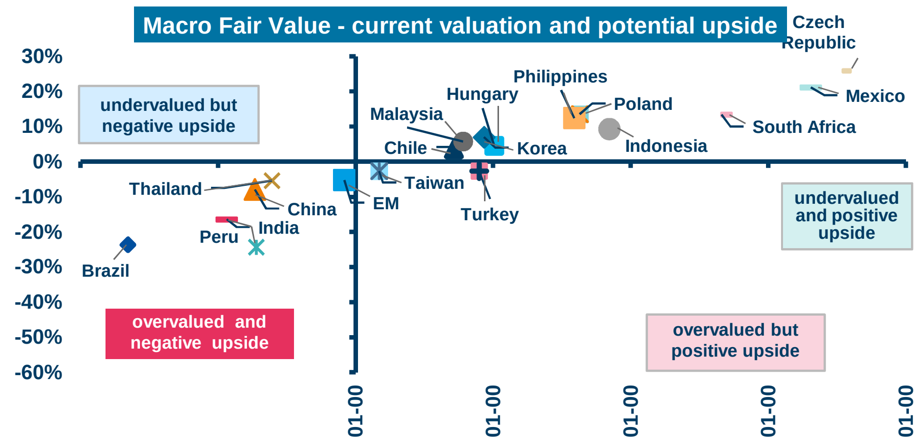
- Protectionism/Trump policies
- Commodity prices
- Slowdown in the global recovery
- Fed policies (strong USD, higher real rates) and GEM hawkishness
- Geopolitics (trade war debate)

**GEM earnings revisions are still suffering**




Source: Analysis by Amundi Research, July 2019. Internal forecasts.

**Valuations are quite widespread across EM countries**




Source: Analysis by Amundi Research, July 2019. Internal forecasts.

# Emerging Market Bonds (hard currency): no longer cheap, but still attractive

## High Conviction Ideas

- **Valuations:** EMBI DIV spread tightened strongly in June. Our target for the next 12 months is 377 for Diversified index (400 for Global). Expectations of widening are justified by the weakening scenario in terms of global growth (even if the growth differential still turns in favour of EM vs DM in H2 2019), EM government debt increasing and average volatility still sustained (in line with 2018).GCC inclusion, on the other side, will push in the opposite direction, reducing the path of the widening. The same is true for the Venezuela phase-down from EMBI that will happen over five months. EMBIGD Spreads will tighten 45bps, with no total return impact.
- **Selectivity remains key.** In general, we are marginally positive on EM fixed income in HC. The index performed strongly since the beginning of the year, but the asset class remains attractive in a low yield environment. Moreover, EM bonds can deliver in both negative and positive scenarios.
- **Sentiment:** flows remain quite sustained. Hard currency funds received inflows for the eighth week running.

## What to Watch

- Fed policy, US dollar and EM CB tightening
- GCC inclusion
- China macro and monetary policy
- Commodity prices (ie, sentiment)
- Geopolitical risk events: Trade war risks, **contagion of idiosyncratic stories**

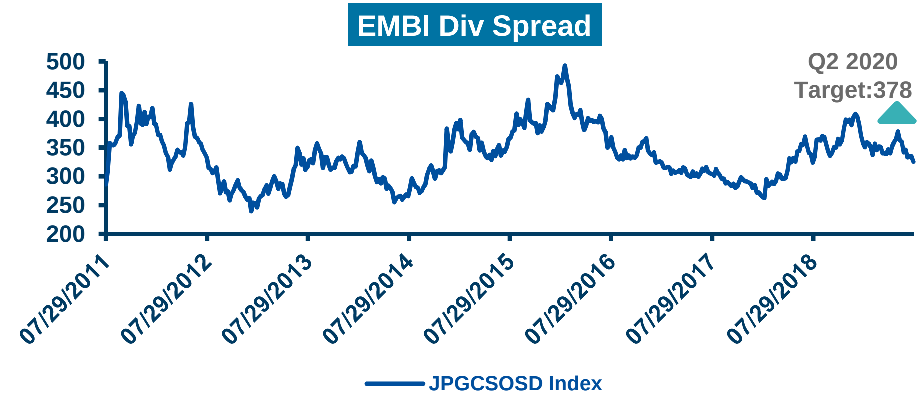
### Overall Assessment

Selection is key for EM bonds, in our view The asset class is still attractive from an income perspective, but exposed to limited upside

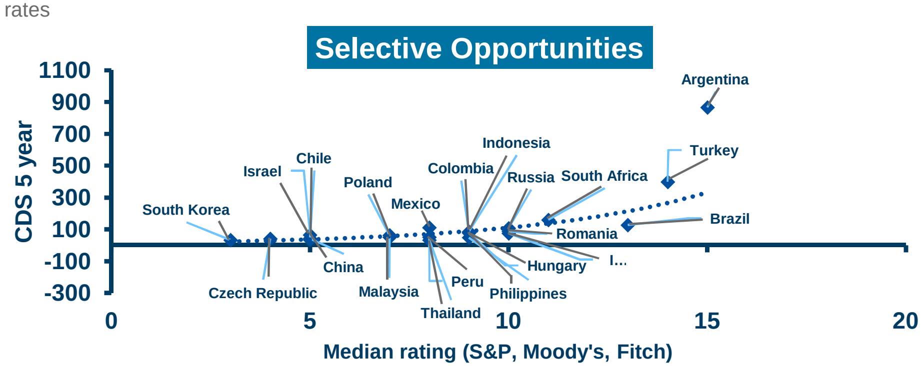
### Risks to Our Assessment

- Aggressive Fed, EM CBs tightening
- Protectionist measures/trade war
- Chinese hard-landing
- Commodity price slowdown
- Geopolitical risks, idiosyncratic contagion

**EMBI Spread is expected to widen but GCC inclusion will push in the opposite direction**




Source: Bloomberg, Analysis by Amundi Research. Data as of July 2019. EMBI = JPMorgan EM Bond Index. Fair value model calculated based on EM Growth expectation in 2018, projected growth differentials (EM –DM), Govt debt projections in EM, VIX and projected short-term and long-term US rates




Source: Bloomberg, Analysis by Amundi Research. Data as of July 2019. We consider the median rating on external debt published by Moody, S&P and Fitch. The horizontal line is the non-linear trend line of EM 5Y CDS. Countries above the blue line are attractive (cheaper) relative to its average rating, while countries below are expensive.

# Improving flows

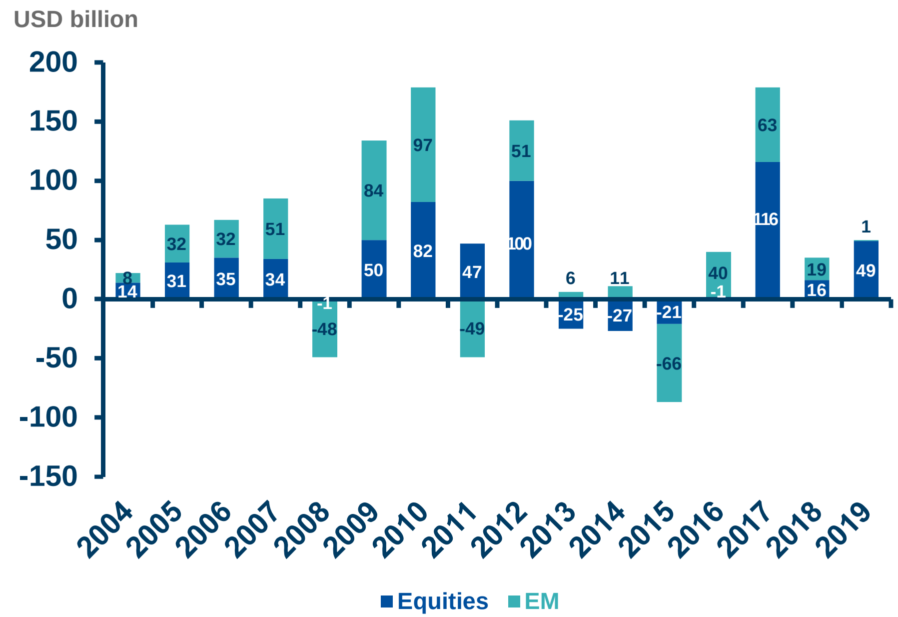
**EM HC BOX**

## Exhibit 1: Weekly Cross-Asset Flows

USD billion

| | Asset | 8w flows (8w ago → current) | This wk | YTD |
|---|---|---|---|---|
| Fund Flows | **EM Bonds and Equities** | | 0.0 | 49.5 |
| | **EM Bonds** | | 1.4 | 48.5 |
| | Hard Ccy | | 1.1 | 40.4 |
| | Local Ccy | | 0.3 | 8.1 |
| | **EM Equities** | | -1.3 | 0.9 |
| | US HG | | 2.1 | 111.7 |
| | US HY | | 0.7 | 15.6 |
| | Global Equities | | 3.1 | -49.6 |
| | **EM Bond and Equity ETFs** | | 0.4 | 18.5 |
| | EM Bond ETFs | | 0.2 | 6.4 |
| | EM Equity ETFs | | 0.2 | 12.1 |
| | **Non-resident EM flows*** | | 0.3 | 26.5 |
| | EM Local Bonds | | 0.8 | 5.6 |
| | EM Equities | | -0.5 | 20.8 |

## Exhibit 2: Annual EM bond and equity fund flows




*Using high frequency non-resident EM portfolio flow data where available. Source – All charts and data in this report: J.P. Morgan, EPFR Global, Bloomberg

### Flows from JPM

Hard currency fund inflows continue to be quite sustained while local currency funds are improving after some outflows in May.

Source: EM Fund Flows Report, JP Morgan, data as of July 2019. The report analyses fund flow trends pertaining to EM as an asset class, focusing on high-frequency dedicated-EM fund flows using a combination of EPFR and JPMorgan data.

# Emerging Market Bonds (local currency): attractive, mainly in H2 2019

### High Conviction Ideas

- **Valuations:** real yields are expected to decrease on a 12-month horizon (GBI diversified weighted) at 1.8%, still higher than for the US. Policy rates should be accommodative in those GEM countries that have room to spend to sustain their economies. No big changes at aggregate level in terms of inflation. On the other side, our more prudent view in terms of EM FX contributes to lower expected returns for EM bonds in LC: GBI-weighted, we see very limited downside for EM FX for the next six months (-0.2%), somewhat more on a 12-month horizon (-0.7%), due also to our scenario of a lower EUR (1.14).
- **In general,** we are cautiously positive on EM fixed income in local currency: the expected returns is lowered by the not encouraging internal view on EM FX, but the yield still remains quite high. Also, volatility will remain high and it will be very important to be selective.
- **Technicals:** flows are improving. They had been negative for some weeks in the second part of May, but are now recovering. EM FX momentum has improved strongly in the last weeks.
- **We remain selective and continue to prefer a Relative Value approach. External vulnerability has to be carefully monitored.**

### What to Watch

- Fed policy and USD.
- Progress with Chinese Inclusion in bond index
- Commodity prices (ie, key for LatAm)
- Geopolitical risk events: Trade war tensions, idiosyncratic stories

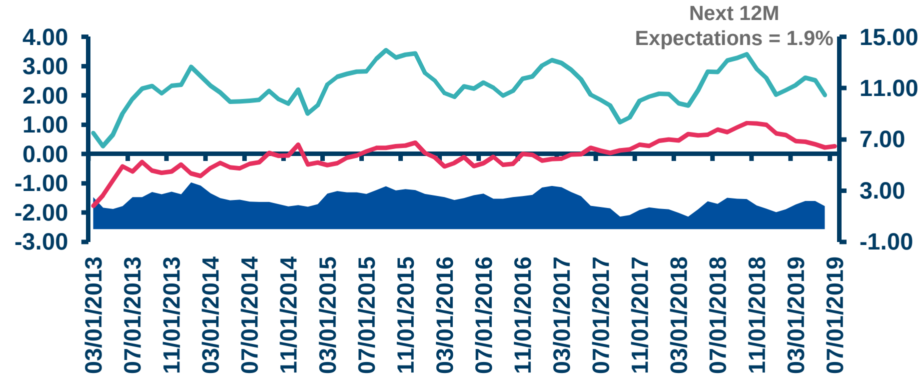
### Overall Assessment

The asset class is attractive from an income perspective and thanks to positive investor sentiment. FX less supportive than some months ago

### Risks to Our Assessment

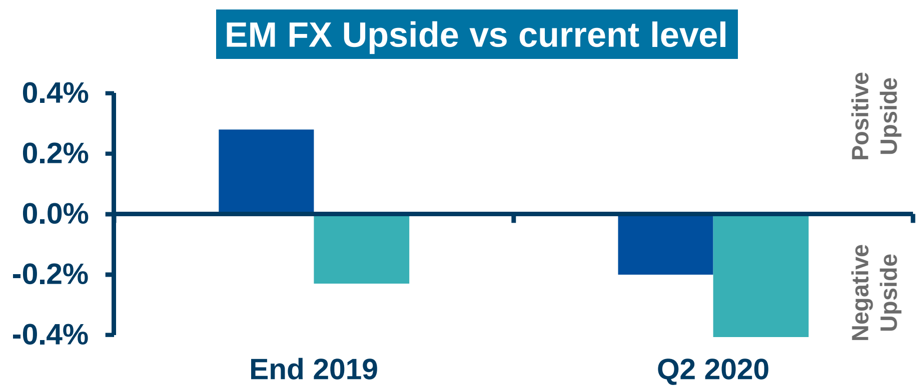
- Aggressive Fed
- Protectionist measures/trade war
- China hard-landing
- Commodity price slowdown
- Geopolitical risks: Russia-US sanctions, US-China trade war
- Idiosyncratic stories

**EM ex-ante real yield (GBI-weighted) vs US5Y real yield: still attractive**




Source: CEIC, Bloomberg, Analysis by Amundi Research. Data as of July 2019. We calculate real rates based on our expected monetary policy outlook and expected inflation and weightings with GBI weights.

**EMFX valuation (GBI-weighted): not supportive for LC bonds**




Source: Bloomberg, Analysis by Amundi Research. We calculate over/under valuation of the EMFX based on Engle and Granger co-integration model with diversified basket of assets and weightings with GBI Weights. Data as of July 2019

# EM Currencies: still limited upside in H2 2019

## High Conviction Ideas

- **Valuations are not attractive anymore on a one-year horizon:** The recent rally in June and our new internal scenario for the next year of very limited depreciation of the USD vs EUR to 1.14, of WTI oil at USD 61/bbl and US10Y at 2% is coherent with a slight depreciation of EM FX vs the USD (close to -0.2% on average for all EM FX). We are more positive in the next months (+0.3%) because we see some weakness for the USD before the end of the year. Moreover, EM FX momentum and commodity momentum are positive and supportive for EM FX in the short term.
- **Growth differential vs US is still there** and is likely to increase in H2 2019 in our base scenario. This is quite a crucial point. A deceleration in global growth would bring other challenges for EM from portfolio outflows and a lack of FDI.
- **Also in terms of USD broad vs EM FX, the signal remains quite flat:** our view of CNY marginal appreciation is counterbalanced by expectation of slight depreciation in the MXN (these have the largest weights in the index).
- **To be selective remains key:** good convergence of positive signals in terms of valuation and carry for the PEN, BRL, PHP. IDR and INR have attractive carry that compensates for stretched valuations.

## What to Watch

- US foreign policy: China, Russia, Mexico
- Commodity prices
- USD and US real rates
- China macro developments

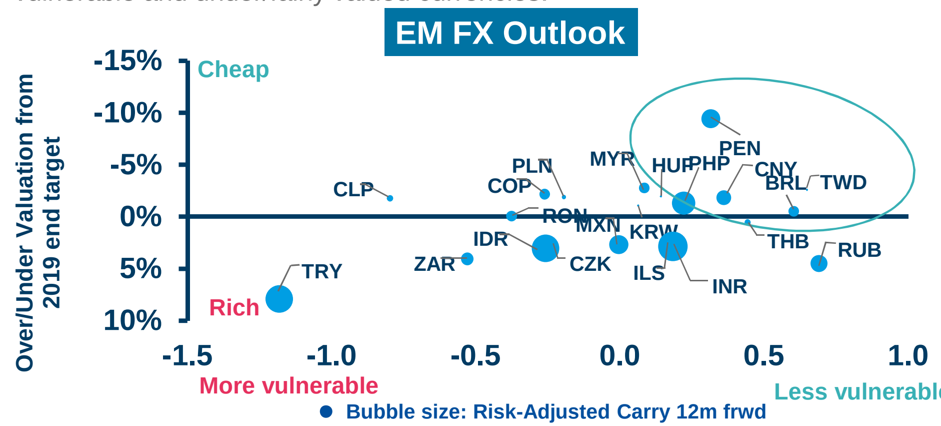
### Overall Assessment

The asset class is still undervalued. Different economic conditions and sensitivities to commodities, EU recovery and Trump's economic programmes could provide relative opportunities within EM currencies

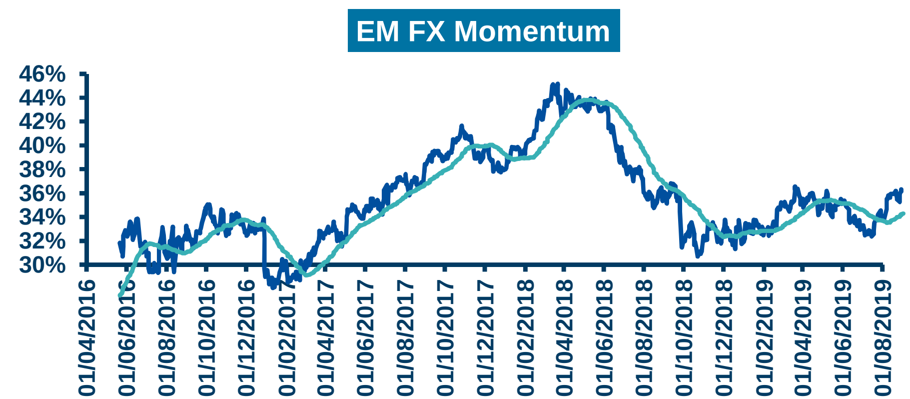
### Risks to Our Assessment

- Idiosyncratic political risks
- Chinese hard landing
- Commodity price decline
- Aggressive Fed
- US-Russia sanctions and other geopolitical developments in the region

**EMFX outlook: p**reference for high carry with low volatility, less externally vulnerable and under/fairly valued currencies.




Source: CEIC, Bloomberg, Analysis by Amundi Research. Data as of July 2019. We calculate over/under valuation of the EMFX based on Engle and Granger co-integration model with diversified basket of assets; Internal EM External vulnerability index and Risk-adjusted carry calculated for 12-m forward yields adjusted with 12M forward volatility.




Source: CEIC, Bloomberg, Analysis by Amundi Research. Data as of July 2019
The EM FX Momentum measures the positive/negative momentum across the EM FX

# Commodities: economic growth and financial conditions remain benign

### High Conviction Ideas

Despite some concerns on economic issues in the medium term (2020), all in, the economic environment is supportive of the asset class. Ultra-dovish CBs and overall dollar weakness return financial conditions back to a supportive track. Gold rallied amid a risk aversion revamp while Fed dovishness will remain the strongest tailwind going forward.

However, It's worth mentioning that commodities underperformed all the other risky assets in H1 and valuations are less compelling than for credit and equities.

We keep our USD 55-65/bbl range for WTI given OPEC flexibility and wiliness to stabilise oil and absorb any supply or demand shock. In fact, production cuts in Saudi Arabia and Iran, and Venezuela supply disruption offset the demand slowdown since August 2018 almost entirely.

Easing financial conditions and the end of a shrinking Fed balance sheet should underpin gold in 2019 while USD weakness should help gold valuations. We have a 12-month target of USD 1,450/ounce.

Base metals will be affected by China and global economic slowdown. All in, the picture still remains supportive for delivering decent returns as the inventories cycle remains reasonably supportive. We maintain the view that Metals should provide a 4-5% total return on a 12-month horizon.

### What to Watch

- OPEC and US oil production, Libya, Venezuela and Iran political issues
- Growth in EM (ie, China), world trade (base metals)
- Central banks' monetary policy normalisation and global real rates (gold)

### Overall Assessment

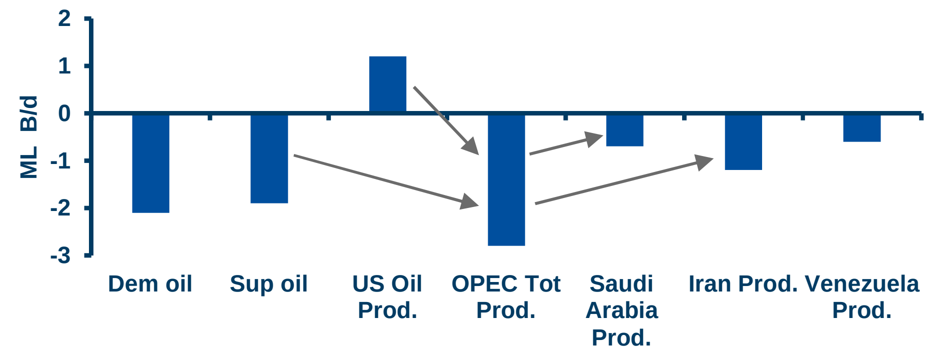
Our overall view on commodities remains moderately constructive

### Risks to Our Assessment

- Protectionism/Trump's policies
- Slowdown in the global recovery
- A Fed policy mistake (strong USD, higher real rates)

**OPEC production cut (forced or not) absorbed both weaker demand and supply and US shale oil production expansion and stabilised oil price**

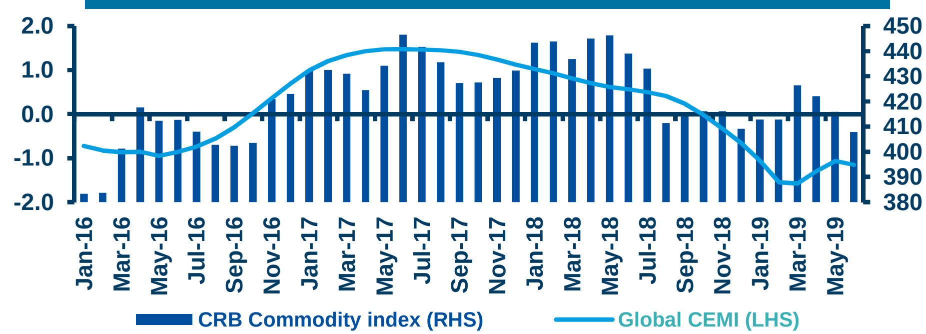
**Change in oil demand, supply and production since August 2018 (ML B/d)**




Source: Bloomberg, Amundi Research, July 2019.

**Global Economic Momentum indicator is flashing tentative stabilisation**

**Global Economic Momentum indicator and commodities**

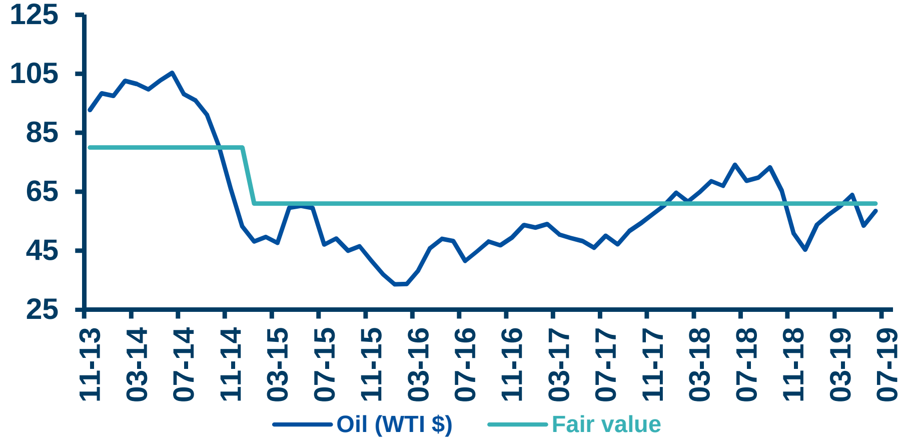



Source: Analysis by Amundi Research. Internal calculation. January 2019 internal indicator based on three regional (US, Eurozone, Japan) baskets of the following variables: Earnings revisions, 10 int. rates, Lei, CPI yoy, PMI surveys, Economic Surprise (EC) surprise index and Inflation surprise index.

# Commodities relatively cheap vs other risky assets

Commodity BOX

- **OPEC production cuts were significant in H1 and confirmed commitment** to stabilise prices above USD 60 for WTI. Inventories and recent shale oil stabilisation should reduce pressure on OPEC to deliver further in H2.
- **Gold still a cheap macro hedge,** as fair value remains above actual levels on weak dollar and Fed extra dovish tone. The target was revised upward to USD1,450 by the end of 2019.
- **Base metals** remain relatively cheap considering inventories cycle.

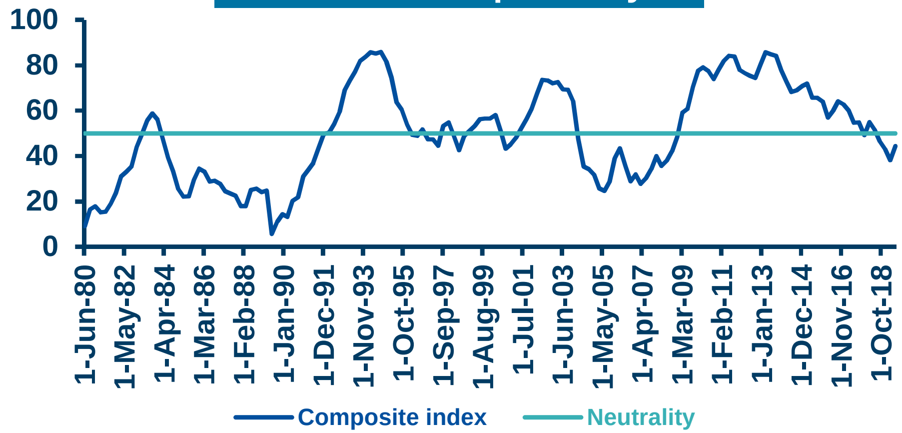



Source: Bloomberg. Analysis by Amundi Research. Internal calculation, July 2019

**Over-/under-valuation of gold vs fair value**


Source: Analysis by Amundi Research. Internal calculation. July 2019

**Inventories composite cycle**




Source: Analysis by Amundi Research. Internal calculation. July 2019

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# Important Information



Document issued by Amundi, “société par actions simplifiée”- SAS with a capital of €1,086,262,605 - Portfolio manager regulated by the AMF under number GP04000036 – Head office: 90 boulevard Pasteur – 75015 Paris – France – 437 574 452 RCS Paris – www.amundi.com

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