

14 October 2019 /// n°34-2019

Markets holding on to 'good' news

Key Points

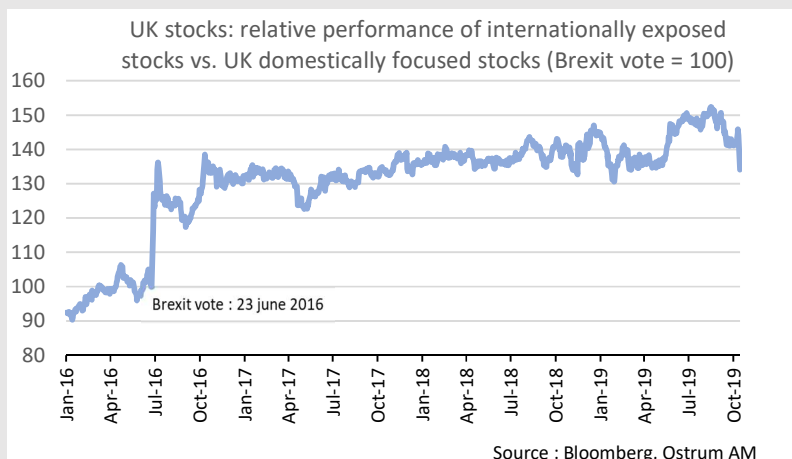
- Investor optimism seen in higher equities, bond yields
- Signs of de-escalation between US and China
- Brexit: hope for a deal slowly returns
- Fed enhances money market interventions

Financial markets have been supported by signs of improvement on both Brexit and the US-China trade war. The rise in tariffs scheduled on October 15th will be postponed. Still, the Trump Administration had blacklisted a total of 8 new Chinese companies early on last week. Markets also ignored trouble in the Middle-East whilst the Fed took monetary easing measures.

The rebound in stocks started on Wednesday. The S&P is up 0.6% for the week. The euro Stoxx 50 gained 2.8%. Sectors sold this year staged a

comeback (basic resources, banks). Investor optimism sends Treasury note yields higher to 1.73%. Bund yields follow Treasuries on the upside (-0.43% peak). Sovereign spreads tightened slightly, with Portugal dipping below the 70bp threshold. Questions on the implementation of QE have had no effect so far. Lower risk aversion also benefitted index-linked bonds, credit and high yield. Spreads in high yield markets narrowed by 16bp to 388bp against Bunds. Sterling briefly hit \$1.27 as market participants eyed a solution on Northern Ireland.

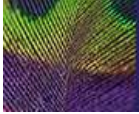
Chart of the week



It is quite challenging to estimate the cost of Brexit for the UK economy.

Stocks with high international sales exposure have clearly outperformed stocks with activity primarily focused on the UK domestic market. The cumulative performance gap amounts to 35% since the 2016 referendum.

That said, in just one trading session last Friday, the gap plunged by 7%, which highlights the extreme sensitivity of markets to the Brexit outcome.



Surprisingly widespread optimism across financial markets

Financial markets have been quite optimistic of late despite a deterioration in the international backdrop. Conflicts have emerged in the Middle-East. The attack on an Iranian tanker attributed to Saudi Arabia is another step towards warfare between the two Gulf nations. Military intervention by Turkey in Syrian Kurdistan is another source of instability in the region.

These developments however crucial for stability have been largely ignored. The apparent de-escalation between China and the US after the announcement of agricultural product purchases propelled markets higher. The tariff hike due on October 15th has been postponed. Market participants also seem to have forgotten about the new blacklist of eight Chinese companies announced by the US government. The phase-one of negotiations leaves aside most important elements pertaining to intellectual property and access to China's domestic markets. Meanwhile, restrictions on Chinese rare earth exports appears unwelcome.

The Brexit process brought the other piece of 'good' news. A new status for Northern Ireland is seen as a path to a deal as the EU summit is set to take place on October 17-18. The outcome of current talks is still highly uncertain.

Fed ups the ante on market intervention

Furthermore, the situation in US money markets convinced the Fed to intervene in the inter-meeting period. The Central Bank will purchase Treasury bills until June 2020 and will conduct repo transactions until January. The objective is to maintain reserve balances at or above their level in early September. Contrary to past QE programmes, the Fed's focus is on its liabilities. The goal is to avoid crowding out of reserves from increased federal deficits. The Fed will purchase \$60b worth of bills in the month to mid-November. Furthermore, the reverse-repo rate (at which the Fed borrows liquidity from the market) was reduced to 1.70%, indeed 5bp below the lower end of the Fed Funds target. The rate reduction entails a foretaste before the widely expected 25bp cut in the Fed Funds range at the end of this month.

Hold on to long duration bias

Against this backdrop of monetary easing, the weekly bounce in US yields (+17bp) may look excessive. The yield on US 10-year notes hit a peak at 1.77% before reaching a weekly close at 1.73% before the long Columbus Day weekend. One should consider raising

exposure in case of renewed market weakness pushing bond yields in the 1.76-1.80% area. Economic data releases, especially household demand, depict growth conditions about potential through 3q19. Retail sales likely expanded at a 0.3% monthly clip in September. Residential investment is responding to lower interest rates.

The absence of a significant term premium nevertheless sparked a rush into money market funds last seen in 2008. This suggests positioning for a steeper curve all the more so that the Fed will again ease policy. The 2s10s spreads is trading at 14bp.

In the euro area, Bund prices fell last week in the wake of T-notes. The account of the September ECB meeting exposed disagreements within the governing council. According to the FT, Mario Draghi deliberately ignored internal research arguing against new asset purchases. QE parameters will be discussed intensely at next week's meeting (October 24), which will be Draghi's last as ECB President. In case of a postponement of QE, swap spreads may have room to tighten. Two-year swap spreads hover about 30bp at present. In parallel, peripheral sovereign spreads barely moved. Portuguese bonds were well bid so that spreads now trade well within 70bp at a 63bp low. Long peripheral bonds is quite consensus among money managers.

As concerns corporate credit, the rise in German bond yields contributed to tighten spreads, especially in the financial sector. The average spread in IG space stands at 110bp over Bunds. High yield erased part of early October spread widening last week. Specific credit stories have weighed on the market in the past few weeks but the equity market upturn did spark a spread rally. That said, default rate may increase in Europe next year according to Moody's to match that of the US (2.1% by 2019 year-end and 3.7% by September 2020).

US earnings to decline in 3q19

Earnings season kicks off this week in the US. Earnings are expected to fall by 3.8% in the third quarter. The energy and basic resources sectors contribute most to the overall decline in profitability. Hence, market will seek a catalyst to make new highs past the 3000 mark on the S&P 500.

In Europe, technical signals point to upside risks whilst earnings expectations remain lacklustre. Banks had a stellar run last week as the yield curve steepened in the euro area.

Main Market Indicators

G4 Government Bonds	14-Oct-19	-1w k (bp)	-1m (bp)	Ytd (bp)
EUR Bunds 2y	-0.7 %	+7	+0	-9
EUR Bunds 10y	-0.46%	+12	-1	-70
EUR Bunds 2s10s	25 bp	+5	-1	-61
USD Treasuries 2y	1.59 %	+13	-21	-90
USD Treasuries 10y	1.73 %	+17	-17	-96
USD Treasuries 2s10s	14 bp	+4	+4	-6
GBP Gilt 10y	0.64 %	+19	-13	-64
JPY JGB 10y	-0.18 %	+4	-3	-18
€ Sovereign Spreads (10y)	14-Oct-19	-1w k (bp)	-1m (bp)	Ytd (bp)
France	32 bp	+1	+4	-15
Italy	137 bp	-6	+4	-113
Spain	67 bp	-4	-8	-51
Inflation Break-evens (10y)	14-Oct-19	-1w k (bp)	-1m (bp)	Ytd (bp)
EUR OATi	72 bp	+6	-6	-
USD TIPS	156 bp	+5	-12	-15
GBP Gilt Index-Linked	326 bp	-13	-11	+9
EUR Credit Indices	14-Oct-19	-1w k (bp)	-1m (bp)	Ytd (bp)
EUR Corporate Credit OAS	110 bp	-3	-4	-42
EUR Agencies OAS	47 bp	-2	-3	-13
EUR Securitized - Covered OAS	43 bp	0	-2	-20
EUR Pan-European High Yield OAS	388 bp	-16	+23	-125
EUR/USD CDS Indices 5y	14-Oct-19	-1w k (bp)	-1m (bp)	Ytd (bp)
iTraxx IG	55 bp	-3	+8	-33
iTraxx Crossover	244 bp	-8	+0	-110
CDX IG	57 bp	-4	+6	-31
CDX High Yield	347 bp	-12	+31	-104
Emerging Markets	14-Oct-19	-1w k (bp)	-1m (bp)	Ytd (bp)
JPM EMBI Global Div. Spread	333 bp	-17	-1	-82
Currencies	14-Oct-19	-1w k (%)	-1m (%)	Ytd (%)
EUR/USD	\$1.103	+0.69	+0.24	-3.69
GBP/USD	\$1.257	+2.89	+1.14	-1.4
USD/JPY	¥108.38	-1.13	-0.38	+1.18
Commodity Futures	14-Oct-19	-1w k (\$)	-1m (\$)	Ytd (\$)
Crude Brent	\$59.0	\$0.6	-\$0.3	\$3.8
Gold	\$1 492.7	-\$7.5	-\$10.5	\$211.1
Equity Market Indices	14-Oct-19	-1w k (%)	-1m (%)	Ytd (%)
S&P 500	2 968	1.01	-1.29	18.41
EuroStoxx 50	3 556	2.45	0.17	18.49
CAC 40	5 643	2.20	-0.22	19.29
Nikkei 225	21 799	1.82	-0.86	8.91
Shanghai Composite	3 008	3.53	-0.77	20.61
VIX - Implied Volatility Index	14.96	-16.24	8.88	-41.15

Source: Bloomberg, Ostrum Asset Management

Writing



AXEL BOTTE
STRATEGIST
axel.botte@ostrum.com

Legal information

This document is intended for professional clients in accordance with MiFID. It may not be used for any purpose other than that for which it was conceived and may not be copied, distributed or communicated to third parties, in part or in whole, without the prior written authorization of Ostrum Asset Management.

None of the information contained in this document should be interpreted as having any contractual value. This document is produced purely for the purposes of providing indicative information. This document consists of a presentation created and prepared by Ostrum Asset Management based on sources it considers to be reliable. Ostrum Asset Management reserves the right to modify the information presented in this document at any time without notice, and in particular anything relating to the description of the investment process, which under no circumstances constitutes a commitment from Ostrum Asset Management.

Ostrum Asset Management will not be held responsible for any decision taken or not taken on the basis of the information contained in this document, nor in the use that a third party might make of the information.

Figures mentioned refer to previous years. Past performance does not guarantee future results. Any reference to a ranking, a rating or an award provides no guarantee for future performance and is not constant over time. Reference to a ranking and/or an award does not indicate the future performance of the UCITS/AIF or the fund manager.

Under Ostrum Asset Management's social responsibility policy, and in accordance with the treaties signed by the French government, the funds directly managed by Ostrum Asset Management do not invest in any company that manufactures, sells or stocks anti-personnel mines and cluster bombs.

This material has been provided for information purposes only to investment service providers or other Professional Clients, Qualified or Institutional Investors and, when required by local regulation, only at their written request. This material must not be used with Retail Investors.

In the E.U. (outside of the UK and France): Provided by Natixis Investment Managers S.A. or one of its branch offices listed below. Natixis Investment Managers S.A. is a Luxembourg management company that is authorized by the Commission de Surveillance du Secteur Financier and is incorporated under Luxembourg laws and registered under n. B 115843. Registered office of Natixis Investment Managers S.A.: 2, rue Jean Monnet, L-2180 Luxembourg, Grand Duchy of Luxembourg. Italy: Natixis Investment Managers S.A., Succursale Italiana (Bank of Italy Register of Italian Asset Management Companies no. 23458.3). Registered office: Via Larga, 2 - 20122, Milan, Italy. Germany: Natixis Investment Managers S.A., Zweigniederlassung Deutschland (Registration number: HRB 88541). Registered office: Im Trutz Frankfurt 55, Westend Carree, 7. Floor, Frankfurt am Main 60322, Germany. Netherlands: Natixis Investment Managers, Netherlands (Registration number 50774670). Registered office: Stadsplateau 7, 3521AZ Utrecht, the Netherlands. Sweden: Natixis Investment Managers, Nordics Filial (Registration number: 616405-9601 - Swedish Companies Registration Office). Registered office: Kungsgatan 48 5tr, Stockholm 111 35, Sweden. Spain: Natixis Investment Managers, Sucursal en España, Serrano nº90, 8th Floor, 28006, Madrid, Spain.

In France: Provided by Natixis Investment Managers International – a portfolio management company authorized by the Autorité des Marchés Financiers (French Financial Markets Authority - AMF) under no. GP 90-009, and a public limited company (société anonyme) registered in the Paris Trade and Companies Register under no. 329 450 738. Registered office: 43 avenue Pierre Mendès France, 75013 Paris. In Switzerland: Provided for information purposes only by Natixis Investment Managers, Switzerland SArl, Rue du Vieux Collège 10, 1204 Geneva, Switzerland or its representative office in Zurich, Schweizergasse 6, 8001 Zurich.

In the U.K.: Provided by Natixis Investment Managers UK Limited which is authorised and regulated by the UK Financial Conduct Authority (register no. 190258). This material is intended to be communicated to and/or directed at persons (1) in the United Kingdom, and should not to be regarded as an offer to buy or sell, or the solicitation of any offer to buy or sell securities in any other jurisdiction than the United Kingdom; and (2) who are authorised under the Financial Services and Markets Act 2000 (FSMA 2000); or are high net worth businesses with called up share capital or net assets of at least £5 million or in the case of a trust assets of at least £10 million; or any other person to whom the material may otherwise lawfully be distributed in accordance with the FSMA 2000 (Financial Promotion) Order 2005 or the FSMA 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (the "Intended Recipients"). The fund, services or opinions referred to in this material are only available to the Intended Recipients and this material must not be relied nor acted upon by any other persons. Registered Office: Natixis Investment Managers UK Limited, One Carter Lane, London, EC4V 5ER. In the DIFC: Provided in and from the DIFC financial district by Natixis Investment Managers Middle East (DIFC Branch) which is regulated by the DFSA. Related financial products or services are only available to persons who have sufficient financial experience and understanding to participate in financial markets within the DIFC, and qualify as Professional Clients or Market Counterparties as defined by the DFSA. No other person should act upon this material. Registered office: Office 603 - Level 6, Currency House Tower 2, PO Box 118257, DIFC, Dubai, United Arab Emirates.

In Japan: Provided by Natixis Investment Managers Japan Co., Ltd., Registration No.: Director-General of the Kanto Local Financial Bureau (kinsho) No. 425. Content of Business: The Company conducts discretionary asset management business and investment advisory and agency business as a Financial Instruments Business Operator. Registered address: 1-4-5, Roppongi, Minato-ku, Tokyo.

In Taiwan: Provided by Natixis Investment Managers Securities Investment Consulting (Taipei) Co., Ltd., a Securities Investment Consulting Enterprise regulated by the Financial Supervisory Commission of the R.O.C. Registered address: 34F., No. 68, Sec. 5, Zhongxiao East Road, Xinyi Dist., Taipei City 11065, Taiwan (R.O.C.), license number 2018 FSC SICE No. 024, Tel. +886 2 8789 2788.

In Singapore: Provided by Natixis Investment Managers Singapore (name registration no. 53102724D) to distributors and institutional investors for informational purposes only. Natixis Investment Managers Singapore is a division of Ostrum Asset Management Asia Limited (company registration no. 199801044D). Registered address of Natixis Investment Managers Singapore: 5 Shenton Way, #22-05 UIC Building, Singapore 068806.

In Hong Kong: Provided by Natixis Investment Managers Hong Kong Limited to institutional/ corporate professional investors only.

In Australia: Provided by Natixis Investment Managers Australia Pty Limited (ABN 60 088 786 289) (AFSL No. 246830) and is intended for the general information of financial advisers and wholesale clients only.

In New Zealand: This document is intended for the general information of New Zealand wholesale investors only and does not constitute financial advice. This is not a regulated offer for the purposes of the Financial Markets Conduct Act 2013 (FMCA) and is only available to New Zealand investors who have certified that they meet the requirements in the FMCA for wholesale investors. Natixis Investment Managers Australia Pty Limited is not a registered financial service provider in New Zealand.

In Latin America: Provided by Natixis Investment Managers S.A.

In Uruguay: Provided by Natixis Investment Managers Uruguay S.A., a duly registered investment advisor, authorised and supervised by the Central Bank of Uruguay. Office: San Lucar 1491, oficina 102B, Montevideo, Uruguay, CP 11500. The sale or offer of any units of a fund qualifies as a private placement pursuant to section 2 of Uruguayan law 18,627.

In Colombia: Provided by Natixis Investment Managers S.A. Oficina de Representación (Colombia) to professional clients for informational purposes only as permitted under Decree 2555 of 2010. Any products, services or investments referred to herein are rendered exclusively outside of Colombia. This material does not constitute a public offering in Colombia and is addressed to less than 100 specifically identified investors.

In Mexico: Provided by Natixis IM Mexico, S. de R.L. de C.V., which is not a regulated financial entity or an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores) and is not registered with the Comisión Nacional Bancaria y de Valores (CNBV) or any other Mexican authority. Any products, services or investments referred to herein that require authorization or license are rendered exclusively outside of Mexico. Natixis Investment Managers is an entity organized under the laws of France and is not authorized by or registered with the CNBV or any other Mexican authority to operate within Mexico as an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores). Any use of the expression or reference contained herein to "Investment Managers" is made to Natixis Investment Managers and/or any of the investment management subsidiaries of Natixis Investment Managers, which are also not authorized by or registered with the CNBV or any other Mexican authority to operate within Mexico as investment managers.

The above referenced entities are business development units of Natixis Investment Managers, the holding company of a diverse line-up of specialised investment management and distribution entities worldwide. The investment management subsidiaries of Natixis Investment Managers conduct any regulated activities only in and from the jurisdictions in which they are licensed or authorized. Their services and the products they manage are not available to all investors in all jurisdictions. It is the responsibility of each investment service provider to ensure that the offering or sale of fund shares or third party investment services to its clients complies with the relevant national law.

The provision of this material and/or reference to specific securities, sectors, or markets within this material does not constitute investment advice, or a recommendation or an offer to buy or to sell any security, or an offer of any regulated financial activity. Investors should consider the investment objectives, risks and expenses of any investment carefully before investing. The analyses, opinions, and certain of the investment themes and processes referenced herein represent the views of the portfolio manager(s) as of the date indicated. These, as well as the portfolio holdings and characteristics shown, are subject to change. There can be no assurance that developments will transpire as may be forecasted in this material. Past performance information presented is not indicative of future performance.

Although Natixis Investment Managers believes the information provided in this material to be reliable, including that from third party sources, it does not guarantee the accuracy, adequacy, or completeness of such information. This material may not be distributed, published, or reproduced, in whole or in part.

All amounts shown are expressed in USD unless otherwise indicated.



www.ostrum.com

Ostrum Asset Management

Asset management company regulated by AMF under n° GP-18000014 – Limited company with a share capital of 27 772 359 euros

Trade register n°525 192 753 Paris – VAT: FR 93 525 192 753 – Registered Office: 43, avenue Pierre Mendès-France, 75013 Paris – www.ostrum.com

Tél. : 01 58 19 09 80