

# STRATEGY WEEKLY

Document intended for professional clients

20 January 2020 /// n°4-2020

## Risky assets keep rising

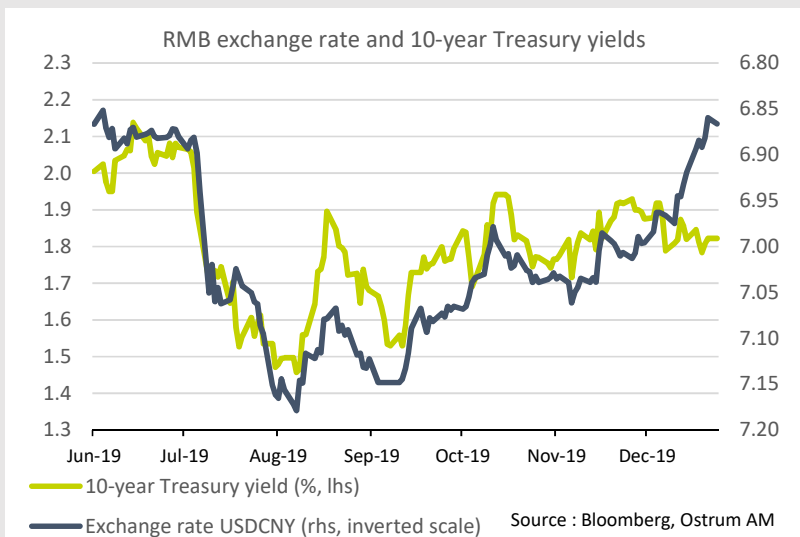
### Key Points

- **US housing signals strength**
- **S&P 500 up near 3,330**
- **Treasury yields steady about 1.80%**
- **Credit markets absorb new issuance without stress**

The rise in risky asset prices that started in September in the wake of Fed intervention is continuing in early 2020. US stock market indices are making new highs. The S&P 500 indeed trades near 3330. European equities are following on the upside (+0.5% last week on Euro Stoxx 50). On the bond side, T-note and Bund yields seem to level out at 1.82% and -0.22% respectively. Gilts outperform as markets price in a BoE rate cut at month end. UK bonds yield 0.62% at Friday's close. Sterling also reacted to the possibility of a rate cut contributing to a stabilization in inflation breakevens. That said, the

fallback in crude prices remains an obstacle to a normalization in inflation expectations. Euro area sovereign spreads recorded some volatility. BTP spreads increased by 7bp to 159bp last week. Moody's maintained its rating on Portugal (Baa3). Credit benefits from the reach-for-yield trend even as issuance picks up. New issue premiums are quite thin. Hence spreads are stable or even slightly down. In parallel, the dollar is regaining strength. The euro is under the \$1.11 threshold. The Japanese yen is trading above 110. In emerging markets, the real is quite weak whilst Mexican peso is rebounding.

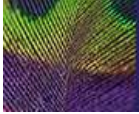
### Chart of the week



Correlation is not causation.

Still, similar trends in US 10-year yields and the CNY exchange rate highlight the importance of the trade conflict in the market narrative. US protectionism weighed on US yields amid dollar strength (hence weaker inflation and growth expectations). Conversely, hope for an agreement late last year sparked a joint rebound in yields and the CNY exchange rate.

Correlation broke down after a trade agreement paved way to the signing of the phase-1 deal on January 15.



## US growth driven by housing

The latest US economic releases seem to validate estimates of 2%+ growth in the fourth quarter. Retail sales picked up significantly in December (+0.5% for the control group series) dissipating fears of a sharper slowdown in consumer spending. Household demand remains the main driver of the US economy. Housing investment is indeed quite upbeat at present. Demand for mortgage credit for house purchases is skyrocketing in early 2020. On the supply side, high homebuilders' confidence (NAHB at 75 in January) hinted at improvement in housing starts (1.6mn in December at annual rate). Fed action since July sparked an upturn in residential investment. In turn, trade deficit has narrowed in the fourth quarter and manufacturing activity is picking up as evidenced by higher readings in both the Empire State and Phil Fed surveys in January. Inflation is rising matching the core rate at 2.3% in December. The energy contribution is picking up so that CPI inflation will accelerate to 2.6-2.7% in January-February.

In the euro area, inflation rose to 1.3% yet our forecasts are for a moderation in price gains later on this year. The ECB will meet this week. The inflation objective may be redefined as the ECB's strategic review gets underway. Inflation slowdown in the UK (2.2% RPI) also fanned expectations of a 25bp rate cut at the next MPC meeting.

## Risky assets keep on giving

The macroeconomic backdrop remains favorable to risky assets all the more so monetary conditions foster risk-taking. Dallas Fed President even cautioned against bubble risk in the wake of Fed liquidity injections. Other markets including US CLOs enjoyed a swift turnaround since mid-November after a period of weakness in late summer. Nothing seems to prevent further gains in risky assets, not even trouble in Iran. Equities have no liquid alternatives offering similar upside potential. The S&P 500 index is making new highs each week. The index is trading around 3330 points after another weekly advance of 2%. The technology sector and media stocks drove the index higher. That said, utilities beat the market in spite of low beta. Aggregate earnings growth (-2.5%) indeed appears to be less negative than expected but current market equilibrium requires a sharp improvement in profitability by year-end 2020 (+14.5% expected in 4Q20). Sales growth (+3.9%) suggests that cost control will be key to sustain market valuation multiples. Financials performed less well than the overall market index amid mixed 4q19 earnings releases. In Europe, lower exposure to the technology sector may explain

part of the underperformance vs. the US. Renewed weakness in cyclical stocks or utilities outperformance could turn out to be a bearish signal. The rally in cyclical value stocks may have come to an end as economic growth fails to accelerate significantly.

Government bond yields were stable around 1.80% on US 10-year notes and -0.2% on German Bunds. Gilts outperformed on expectation of monetary easing whilst 10-year JGBs hover about the BoJ target of 0%. The US Treasury's announcement of the reopening of 20-year bond auctions could have steepened the back-end of the curve (10s30s). Steepening pressure was in fact muted. At the end of the day, curve changes will depend on the amount of duration sold to the market with the new benchmark maturity. Auctions sizes beyond \$15b a month could weigh on the back-end. The Fed will still take its share of issuance. In turn, TIPS remain undervalued given current inflation and consensus inflation forecasts. Two-year inflation swap is indeed trading about 1.62%. In addition, emerging debt is still in high demand given the favorable net supply backdrop and relatively attractive spreads (290bp on average in the asset class) compared to underlying US risk-free yields.

In the euro area, bond markets easily absorbed syndicated sovereign bond deals. All transactions have been oversubscribed (for example, demand totaled 50b on the Spanish 10-year bond sale). The successful Portugal bond deal (4b issue of 10-year bond at 0.5%) covers fully a quarter of 2020 gross funding needs. Still Moody's refrained from raising Portugal's sovereign rating from Baa3 on Friday. Italy is facing familiar political battles. BTP volatility may stay elevated as regional elections at the end of January and a constitutional referendum loom.

Credit is also unaffected by the resumption of primary market activity. Demand from the ECB accounts for 15 to 30% of primary issuance. Covered bonds are also sought by investors as bid-to-cover ratio are high historically and new issue premiums are minimal at present. This is also true in unsecured corporate bond markets but gross issuance is slightly lower than a year ago. Credit spreads are thus stable around 63bp vs. swaps. In addition, iTraxx IG spreads (43bp) are slightly tighter than last year's close. Crossover spreads are unchanged at 209bp, although current valuations seem too rich relative to historical default risk.

Currency markets remains characterized par reduced volatility and a pickup in investor demand for the US dollar. Yen weakness is traceable to the broad-based risk-on market environment. Lastly, the downturn in the Brazilian real is worth monitoring. Conversely, the Mexican peso is strengthening.

## Main Market Indicators

| <b>G4 Government Bonds</b>         | <b>20-Jan-20</b> | <b>-1w k (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
|------------------------------------|------------------|-------------------|-----------------|-----------------|
| EUR Bunds 2y                       | -0.59 %          | +0                | +5              | +2              |
| EUR Bunds 10y                      | -0.21%           | -6                | +3              | -3              |
| <b>EUR Bunds 2s10s</b>             | <b>38 bp</b>     | <b>-6</b>         | <b>-2</b>       | <b>-5</b>       |
| USD Treasuries 2y                  | 1.56 %           | -3                | -7              | -1              |
| USD Treasuries 10y                 | 1.82 %           | -2                | -10             | -10             |
| <b>USD Treasuries 2s10s</b>        | <b>26 bp</b>     | <b>+0</b>         | <b>-3</b>       | <b>-9</b>       |
| GBP Gilt 10y                       | 0.63 %           | -11               | -14             | -18             |
| JPY JGB 10y                        | 0.01 %           | +1                | 0               | +2              |
| <b>€ Sovereign Spreads (10y)</b>   | <b>20-Jan-20</b> | <b>-1w k (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| France                             | 26 bp            | +1                | -5              | -5              |
| Italy                              | 158 bp           | +4                | -8              | -2              |
| Spain                              | 66 bp            | +3                | -3              | +1              |
| <b>Inflation Break-evens (10y)</b> | <b>20-Jan-20</b> | <b>-1w k (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| EUR OATi                           | 100 bp           | -2                | +9              | -               |
| USD TIPS                           | 175 bp           | -2                | -2              | -3              |
| GBP Gilt Index-Linked              | 317 bp           | +1                | +3              | +6              |
| <b>EUR Credit Indices</b>          | <b>20-Jan-20</b> | <b>-1w k (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| EUR Corporate Credit OAS           | 92 bp            | -1                | -2              | -1              |
| EUR Agencies OAS                   | 43 bp            | +0                | -1              | -1              |
| EUR Securitized - Covered OAS      | 39 bp            | +0                | -2              | -2              |
| EUR Pan-European High Yield OAS    | 302 bp           | -3                | -7              | -2              |
| <b>EUR/USD CDS Indices 5y</b>      | <b>20-Jan-20</b> | <b>-1w k (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| iTraxx IG                          | 43 bp            | 0                 | -1              | -1              |
| iTraxx Crossover                   | 208 bp           | +1                | +3              | +2              |
| CDX IG                             | 44 bp            | 0                 | -1              | -1              |
| CDX High Yield                     | 279 bp           | +0                | -4              | -1              |
| <b>Emerging Markets</b>            | <b>20-Jan-20</b> | <b>-1w k (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| JPM EMBI Global Div. Spread        | 290 bp           | -5                | -4              | 0               |
| <b>Currencies</b>                  | <b>20-Jan-20</b> | <b>-1w k (%)</b>  | <b>-1m (%)</b>  | <b>YTD (%)</b>  |
| EUR/USD                            | \$1.108          | -0.5              | +0.05           | -1.29           |
| GBP/USD                            | \$1.299          | -0.04             | -0.06           | -2.05           |
| USD/JPY                            | ¥110.16          | -0.22             | -0.65           | -1.43           |
| <b>Commodity Futures</b>           | <b>20-Jan-20</b> | <b>-1w k (\$)</b> | <b>-1m (\$)</b> | <b>YTD (\$)</b> |
| Crude Brent                        | \$65.3           | \$1.1             | \$0.1           | -\$0.7          |
| Gold                               | \$1 560.7        | \$10.9            | \$83.3          | \$37.9          |
| <b>Equity Market Indices</b>       | <b>20-Jan-20</b> | <b>-1w k (%)</b>  | <b>-1m (%)</b>  | <b>YTD (%)</b>  |
| S&P 500                            | 3 330            | 1.97              | 3.37            | 28.9%           |
| EuroStoxx 50                       | 3 800            | 0.53              | 0.61            | 24.8%           |
| CAC 40                             | 6 079            | 0.71              | 0.95            | 26.4%           |
| Nikkei 225                         | 24 084           | 0.98              | 1.12            | 18.2%           |
| Shanghai Composite                 | 3 096            | -0.63             | 3.02            | 22.3%           |
| VIX - Implied Volatility Index     | 12.10            | -3.66             | -3.28           | -45.8%          |

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, Nederlands (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 Zürich.

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](http://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](http://www.ostrum.com)

Tél. : 01 58 19 09 80