

Market Review

2 November 2017

Review of Markets over October 2017

The synchronised global recovery continued in October, as the Global Manufacturing Purchasing Managers' Index (PMI) for September ticked up a fraction to 53.2 ahead of August's 53.1 figure. Global corporate earnings per share (EPS) growth ticked upwards to 13.8% year on year. Developed market equities gained 2.6% in the month making for year-to-date returns of 15.9%, while emerging market (EM) equities gained 3.9% in October, for the highest year-to-date returns of 28.7%. Commodities gained 2.1% with an upward pull from Brent Crude oil, which gained 7% over the month.

Exhibit 1: Asset class and style returns (local currency)

2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	YTD	October 2017
MSCI EM 35.8%	REITS 34.4%	MSCI EM 33.6%	Global Agg 4.8%	MSCI EM 62.8%	REITS 27.6%	REITS 7.3%	REITS 20.1%	Small cap 35.8%	REITS 27.1%	Growth 6.5%	Value 15.1%	MSCI EM 28.7%	MSCI EM 3.9%
Small cap 23.3%	MSCI EM 28.8%	Cmdty 16.2%	Cmdty -35.6%	Small cap 40.8%	Small cap 24.4%	Global Agg 5.6%	Small cap 18.4%	Value 29.7%	Growth 11.5%	Small cap 2.8%	Small cap 14.5%	Growth 21.1%	Growth 3.4%
Cmdty 21.4%	Value 21.2%	Growth 10.5%	REITS -37.3%	Growth 29.4%	Cmdty 16.8%	Value -4.9%	MSCI EM 17.4%	DM Equities 29.6%	DM Equities 10.4%	DM Equities 2.6%	Cmdty 11.8%	DM Equities 15.9%	DM Equities 2.6%
Value 16.7%	DM Equities 16.1%	Global Agg 9.5%	Value -37.7%	REITS 27.4%	MSCI EM 14.4%	DM Equities -5.0%	Growth 16.5%	Growth 29.5%	Value 9.2%	REITS 2.3%	MSCI EM 10.1%	Small cap 15.8%	Small cap 2.2%
DM Equities 16.3%	Small cap 13.6%	DM Equities 5.2%	DM Equities -38.3%	DM Equities 26.5%	Growth 12.7%	Growth -5.1%	DM Equities 16.4%	MSCI EM 3.8%	Small cap 6.7%	Value -1.2%	DM Equities 9.6%	Value 11.0%	Cmdty 2.1%
Growth 16.0%	Growth 11.2%	Value -0.0%	Growth -39.0%	Value 23.6%	DM Equities 10.6%	Small cap -8.7%	Value 16.3%	REITS 3.2%	MSCI EM 5.6%	Global Agg -3.2%	REITS 9.3%	REITS 6.6%	Value 1.7%
REITS 8.3%	Global Agg 6.6%	Small cap -3.8%	Small cap -40.4%	Cmdty 18.9%	Value 8.4%	MSCI EM -12.5%	Global Agg 4.3%	Global Agg -2.6%	Global Agg 0.6%	MSCI EM -5.4%	Growth 4.4%	Global Agg 5.8%	REITS -0.1%
Global Agg -4.5%	Cmdty 2.1%	REITS -17.8%	MSCI EM -45.7%	Global Agg 6.9%	Global Agg 5.5%	Cmdty -13.3%	Cmdty -1.1%	Cmdty -9.5%	Cmdty -17.0%	Cmdty -24.7%	Global Agg 2.1%	Cmdty -0.8%	Global Agg -0.4%

Source: Barclays, Bloomberg, FactSet, FTSE, MSCI, J.P. Morgan Asset Management. REITS: FTSE NAREIT All REITS; Cmdty: Bloomberg UBS Commodity Index; Global Agg: Barclays Global Aggregate; Growth: MSCI World Growth; Value: MSCI World Value; Small cap: MSCI World Small Cap. All indices are total return in local currency. Data as of 31st October 2017.

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European macroeconomic momentum helped the region's equity markets gain nearly 2% in October. The first estimate for third-quarter GDP for the eurozone came in at 0.6% quarter on quarter. Additionally, the regions' unemployment rate fell to an eight-year low of 8.9%. October's PMI manufacturing reading came in strongly at 58.6, up on last month's 58.1. PMI Services came in at 54.9. Consumer confidence improved slightly with October's reading slightly higher than September's.

The big monetary policy event of the month was the European Central Bank's (ECB's) October meeting, at which Mario Draghi announced an extension of the bank's quantitative easing (QE) programme for nine months with monthly purchases of EUR 30

billion from January to September 2018. This was an acknowledgement of the solid growth apparent in the region, but also keeps the door open for a further extension to be announced. Despite the impending reduction in monthly bond purchases, euro area sovereign bonds gained 1.1% over the month. The announcement was in line with consensus expectations for the ECB. Inflation readings in the eurozone will be crucial for the QE outlook, given the unexpectedly cooler headline inflation release in October of 1.4% for September's year on year figure.

Catalonia held a referendum on independence on 1 October, which caused Spanish equities to weaken moderately and Spanish yields to spread further out from the German Bund. However, as increasing political uncertainty unfolded over the month, the Catalan regional parliament unilaterally declared independence from Spain after a secret vote. This move led the Spanish authorities to trigger Article 155 of the Constitution and assume direct control of the region. Despite the volatility, Spanish government bonds actually gained 0.9% on the month.

In the UK, CPI year on year for September ticked up to 3.0%—the highest reading in over five years—while core inflation remained at 2.7%. Retail sales growth fell to 1.2% year on year—half of August's reading—as UK consumers felt the inflation and real wages squeeze. However, UK GDP for the third-quarter came in ahead of expectations, with a reading of 0.4% quarter on quarter vs. the predicted 0.3%. The FTSE all share gained 1.7% on the month, while sterling weakened 1.0% against the dollar.

Exhibit 2: World stock market returns (local currency)

2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	YTD	October 2017
Japan TOPIX 45.2%	MSCI EM 28.8%	MSCI Asia ex Japan 38.0%	UK FTSE 100 -28.3%	MSCI Asia ex Japan 67.2%	MSCI Asia ex Japan 15.6%	US S&P 500 2.1%	Japan TOPIX 20.9%	Japan TOPIX 54.4%	US S&P 500 13.7%	Japan TOPIX 12.1%	UK FTSE 100 19.1%	MSCI Asia ex Japan 33.2%	Japan TOPIX 5.4%
MSCI EM 35.8%	MSCI Asia ex Japan 28.6%	MSCI EM 33.6%	US S&P 500 -37.0%	MSCI EM 62.8%	US S&P 500 15.1%	UK FTSE 100 -2.2%	MSCI Europe ex UK 20.0%	US S&P 500 32.4%	Japan TOPIX 10.3%	MSCI Europe ex UK 9.1%	US S&P 500 12.0%	MSCI EM 28.7%	MSCI Asia ex Japan 4.2%
MSCI Europe ex UK 28.6%	MSCI Europe ex UK 22.5%	UK FTSE 100 7.4%	Japan TOPIX -40.6%	MSCI Europe ex UK 29.0%	MSCI EM 14.4%	MSCI Europe ex UK -12.1%	MSCI Asia ex Japan 19.7%	MSCI Europe ex UK 24.2%	MSCI Asia ex Japan 7.7%	US S&P 500 1.4%	MSCI EM 10.1%	Japan TOPIX 18.6%	MSCI EM 3.9%
MSCI Asia ex Japan 24.1%	US S&P 500 15.8%	MSCI Europe ex UK 6.6%	MSCI Europe ex UK -42.7%	UK FTSE 100 27.3%	UK FTSE 100 12.6%	MSCI EM -12.5%	MSCI EM 17.4%	UK FTSE 100 18.7%	MSCI Europe ex UK 7.4%	UK FTSE 100 -1.3%	MSCI Asia ex Japan 6.4%	MSCI Europe ex UK 17.1%	US S&P 500 2.3%
UK FTSE 100 20.8%	UK FTSE 100 14.4%	US S&P 500 5.5%	MSCI EM -45.7%	US S&P 500 26.5%	MSCI Europe ex UK 5.1%	MSCI Asia ex Japan -14.6%	US S&P 500 16.0%	MSCI Asia ex Japan 6.2%	MSCI EM 5.6%	MSCI Asia ex Japan -5.3%	MSCI Europe ex UK 3.2%	US S&P 500 16.9%	MSCI Europe ex UK 2.3%
US S&P 500 4.9%	Japan TOPIX 3.0%	Japan TOPIX -11.1%	MSCI Asia ex Japan -47.7%	Japan TOPIX 7.6%	Japan TOPIX 1.0%	Japan TOPIX -17.0%	UK FTSE 100 10.0%	MSCI EM 3.8%	UK FTSE 100 0.7%	MSCI EM -5.4%	Japan TOPIX 0.3%	UK FTSE 100 8.5%	UK FTSE 100 1.8%

Source: FactSet, FTSE, MSCI, Standard & Poor's, TOPIX, J.P. Morgan Asset Management. All indices are total return in local currency. Data as of 31st October 2017.

The strong data out of the US in October continued. Unemployment fell further, with September's reading dropping to 4.2%—a level last matched in February 2001. September's non-farm payrolls dipped significantly, as the data showed there were 33,000 fewer jobs for the month compared with the 156,000 added in August. This can be attributed to the effects of Hurricanes Irma and Harvey, thus we would expect to see a bounce-back in next month's reading. The US ISM manufacturing survey came out at 58.7 in October. Although non-farm payrolls fell, the underlying labour market picture remained healthy and showed signs of rising wages: average hourly earnings grew 2.9% year on year compared with the previous month's reading of 2.5%.

The heartbeat of the US economy, the consumer, was alive and well in October. The University of Michigan Sentiment index for October charged upwards to a reading of 100.7, well above a predicted 95.0. Industrial production showed some recovery from

August's reading of -0.7% to 0.3% for September, showing that the effects of the storms look to be short term. The Philly Fed Business outlook for October reinforced the positive outlook for business investment, coming in at 27.9—well above expectations and last month's reading. Overall, these past few years of solid US macroeconomic growth mean companies are able to deliver quarter after quarter of positive earnings results. The third-quarter S&P 500 earnings season kicked off, and at the end of the month, with two-thirds of the index having reported, year on year EPS growth was around 7%, and nearly 5% ex-energy. S&P 500 price levels responded to positive earnings surprises gaining 2.3% over the month, taking the year-to-date rally to 16.9%. The S&P 500 price/earnings ratio ended the month at 18.1.

Exhibit 3: Fixed income sector returns (local currency)

2010	2011	2012	2013	2014	2015	2016	YTD	October 2017
US HY 15.1%	IL 10.2%	Euro HY 23.3%	Euro HY 8.8%	Euro Treas. 13.1%	EM Debt 1.8%	US HY 17.5%	EM Debt 8.5%	Euro HY 1.1%
Euro HY 14.3%	US Treas. 9.8%	EM Debt 18.0%	US HY 7.4%	EM Debt 6.2%	Euro Treas. 1.6%	Euro HY 10.1%	Global IG 7.6%	Euro Treas. 1.1%
EM Debt 11.8%	EM Debt 9.2%	US HY 15.5%	Euro Treas. 2.2%	Euro HY 5.5%	US Treas. 0.8%	EM Debt 9.6%	US HY 7.5%	US HY 0.4%
US Treas. 5.9%	US HY 4.4%	Global IG 11.2%	Global IG 0.3%	US Treas. 5.1%	Euro HY 0.5%	Global IG 4.3%	Euro HY 6.7%	Global IG 0.1%
Global IG 5.8%	Global IG 4.3%	Euro Treas. 11.0%	US Treas. -2.7%	IL 3.4%	Global IG -3.6%	IL 3.9%	IL 5.6%	IL 0.0%
IL 3.0%	Euro Treas. 3.4%	IL 8.5%	IL -3.2%	Global IG 3.1%	US HY -4.6%	Euro Treas. 3.2%	US Treas. 2.1%	US Treas. -0.1%
Euro Treas. 1.1%	Euro HY -1.1%	US Treas. 2.0%	EM Debt -8.3%	US HY 2.5%	IL -5.0%	US Treas. 1.0%	Euro Treas. 0.7%	EM Debt -0.1%

Source: Barclays, BofA/Merrill Lynch, FactSet, J.P. Morgan Economic Research, J.P. Morgan Asset Management. IL: Barclays Global Inflation-Linked; Euro Treas: Barclays Euro Aggregate Government - Treasury; US Treas: Barclays US Aggregate Government - Treasury; Global IG: Barclays Global Aggregate - Corporates; US HY: BofA/Merrill Lynch US HY Constrained; Euro HY: BofA/Merrill Lynch Euro Non-Financial HY Constrained; EM Debt: J.P. Morgan EMBI+. All indices are total return in local currency. Data as of 31st October 2017.

China held its 19th National Party Congress (NPC), at which a change in sentiment was observed. Officials are moving away from a pure focus on numerical growth targets to qualitative measures when formulating policy. While this shift supports our view that the Chinese authorities will now prioritise financial stability, important economic reforms will still continue to be carried out. Comprehensive reforms aimed at distributing wealth more evenly should reinforce positive fundamentals for certain sectors in the emerging markets universe. China's third-quarter GDP was 6.8% year on year vs. 6.9% for the second quarter, in line with expectations. China's October PMI came out softer than expected, but year on year retail sales improved in September, posting 10.3%, ahead of August's 10.1%. CPI year on year for September was in line with expectations of 1.6%. Year on year PPI remained high at 6.9% for September, higher than August's 6.3% reading.

Strong global growth and EM expansion were underlying drivers for EM equities. EM equities continued on their positive year, increasing 3.9% over the month.

In Japan, the elections were a focus for markets. Voters handed a majority to incumbent Japanese Prime Minister Shinzo Abe's Liberal Democratic Party in Japan's snap election. During the campaign, Prime Minister Abe made several promises about fiscal policy to

voters, including using part of the revenue from the upcoming consumption tax hike to increase labour force participation and to invest in improving Japan's human capital. Broadly speaking, the result means continuity for the Japanese economic and political landscape. October's manufacturing PMI fell slightly to 52.8 from 52.9 the previous month. Third-quarter Tankan business conditions for manufacturing rose from 11 to 15, non-manufacturing also rose from 13 to 14. Japan's TOPIX was the best performing equity index, posting gains of 5.4% in October alone, taking its year-to-date return to 18.6%.

Exhibit 4: Fixed income government bond returns (local currency)

2010	2011	2012	2013	2014	2015	2016	YTD	October 2017
UK 7.5%	UK 16.8%	Italy 21.3%	Spain 11.3%	Spain 17.0%	Italy 4.9%	UK 10.7%	US 2.2%	Italy 2.0%
Germany 6.4%	US 9.9%	Spain 6.0%	Italy 7.4%	Italy 15.7%	Spain 1.7%	Spain 4.2%	Italy 1.8%	Spain 0.9%
US 6.1%	Germany 9.8%	Germany 4.5%	Japan 2.2%	UK 14.1%	Global 1.3%	Germany 4.1%	Spain 1.5%	Germany 0.6%
Global 4.2%	Spain 6.6%	Global 4.1%	Global -0.4%	Germany 10.5%	Japan 1.3%	Japan 3.6%	Global 1.2%	Global 0.3%
Japan 2.5%	Global 6.3%	UK 2.6%	Germany -2.3%	Global 8.5%	UK 1.2%	Global 2.9%	UK 0.1%	UK 0.3%
Italy -0.6%	Japan 2.3%	US 2.2%	US -3.4%	US 6.1%	US 0.9%	US 1.1%	Japan -0.2%	Japan 0.0%
Spain -4.2%	Italy -5.9%	Japan 1.8%	UK -4.2%	Japan 4.8%	Germany 0.4%	Italy 0.8%	Germany -0.8%	US -0.1%

Source: FactSet, J.P. Morgan Economic Research, J.P. Morgan Asset Management. All indices are J.P. Morgan GBIs (Government Bond Indices). All indices are total return in local currency. Data as of 31 October 2017.

Exhibit 5: Index returns for August (%)

INDEX	GBP	USD	JPY	EUR	LOC
Equities (MSCI)					
MSCI World Index	3.0	1.9	2.9	3.4	2.6
MSCI USA	3.3	2.3	3.3	3.8	2.3
MSCI Europe ex UK	1.5	0.4	1.4	1.9	2.3
MSCI United Kingdom	1.6	0.6	1.6	2.1	1.6
MSCI Japan	5.7	4.6	5.6	6.2	5.6
MSCI AC Asia ex JP	5.8	4.7	5.7	6.3	4.2
MSCI EM Latin America	-2.6	-3.6	-2.7	-2.2	-0.3
MSCI EM (Emerging Markets)	4.6	3.5	4.5	5.0	3.9
Bonds					
JP Morgan GBI Global (Traded)	0.6	-0.4	0.5	1.0	0.3
JP Morgan GBI United States (Traded)	0.9	-0.1	0.8	1.4	-0.1
JP Morgan GBI Japan (Traded)	0.1	-0.9	0.0	0.5	0.0
JP Morgan GBI United Kingdom (Traded)	0.3	-0.8	0.2	0.7	0.3
JP Morgan EMU	0.7	-0.4	0.6	1.1	1.1
Currencies					
Sterling	n/a	-1.0	-0.1	0.4	n/a
US dollar	1.0	n/a	0.9	1.5	n/a
Yen	0.1	-0.9	n/a	0.5	n/a
Euro	-0.4	-1.5	-0.5	n/a	n/a

Source: MSCI, FactSet, J.P. Morgan Economic Research, J.P. Morgan Asset Management. Data as of 31 October 2017.

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