

# Market Review

1 October 2019

## Review of markets over the third quarter of 2019

After a difficult summer for risk assets, investors returned from their holidays in a bullish mood and drove equities higher in September, leaving global equities broadly flat for the quarter. The quarter was marked by a continued slowdown in the global economic data, offset by further monetary easing from the US and Europe.

In the US, the Federal Reserve (Fed) cut interest rates in July and September in an attempt to prolong the economic expansion in the face of a slowdown in the pace of growth and hiring. While the economy continued to add jobs, the pace of growth of aggregate hours worked in the economy has slowed meaningfully. Consumer confidence also declined from elevated levels. US equities delivered 1.7% over the quarter in USD.

### Exhibit 1: Asset class and style returns in local currency

2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	YTD	3Q 2019
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 31.0%	Global Agg -1.2%	REITS 27.4%	REITS 7.2%
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 24.5%	REITS -4.1%	Growth 23.0%	Value 1.7%
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%	Small cap 19.1%	Growth -5.1%	DM Equities 19.0%	DM Equities 1.7%
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%	DM Equities 19.1%	DM Equities -6.9%	Small cap 16.3%	Growth 1.6%
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 14.1%	Value -8.7%	Value 15.1%	Cmdty 1.2%
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 9.3%	MSCI EM -9.7%	MSCI EM 8.1%	Global Agg 0.7%
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 7.4%	Cmdty -11.2%	Global Agg 6.3%	Small cap 0.3%
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 1.7%	Small cap -12.2%	Cmdty 3.1%	MSCI EM -1.9%

Source: Barclays, Bloomberg, FactSet, FTSE, MSCI, J.P. Morgan Asset Management. DM Equities: MSCI World; 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. Past performance is not a reliable indicator of current and future results. Data as of 30 September 2019.

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In Europe, the European Central Bank (ECB) responded to the weaker economic outlook by cutting interest rates further into negative territory, restarting quantitative easing and committing to continue with asset purchases until it achieves its inflation target. This shift from a date-dependent to a state-dependent form of forward guidance is significant in that it could lead to a large expansion in the total size of assets purchased by the central bank over the coming years. While those asset purchases may have a limited effect on their own, if combined with fiscal stimulus from the economies that can afford it, they could help to support growth. But the timing of any fiscal stimulus from Europe remains uncertain.

The ECB's policy easing came against a backdrop of weakening growth, with the business surveys for September painting a picture of an economy that continues to slow, particularly in the manufacturing sector. With growth pushing in one direction and monetary stimulus pushing in the other, European equities delivered 2.5% over the quarter.

In the UK, the seemingly never-ending Brexit saga dragged on, with parliament passing legislation that will force the government to ask for an extension if it can't agree a deal with the EU. This sent sterling higher, before the prime minister suspended parliament, only for the suspension to be ruled unlawful. So, no let-up in the drama, with a highly unpredictable election remaining the most likely outcome if a deal cannot be reached in the coming weeks. UK equities delivered 1.0% over the quarter.

### Exhibit 2: World stock market returns in local currency

2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	YTD	3Q 2019
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 35.9%	US S&P 500 -4.4%	MSCI Europe ex UK 21.1%	Japan TOPIX 3.4%
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 31.0%	UK FTSE 100 -8.7%	US S&P 500 20.6%	MSCI Europe ex UK 2.5%
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 22.2%	MSCI EM -9.7%	UK FTSE 100 14.3%	US S&P 500 1.7%
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%	US S&P 500 21.8%	MSCI Europe ex UK -10.6%	Japan TOPIX 8.8%	UK FTSE 100 1.0%
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%	MSCI Europe ex UK 14.5%	MSCI Asia ex Japan -12.0%	MSCI EM 8.1%	MSCI EM -1.9%
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 11.9%	Japan TOPIX -16.0%	MSCI Asia ex Japan 7.3%	MSCI Asia ex Japan -3.3%

Source: FactSet, FTSE, MSCI, Standard & Poor's, TOPIX, J.P. Morgan Asset Management. All indices are total return in local currency. Past performance is not a reliable indicator of current and future results. Data as of 30 September 2019.

The Bank of England remained on hold as Brexit uncertainty continued to cloud the outlook for the UK economy. With wage growth at 4%, policymakers are conscious that if global and Brexit-related risks subside they may still need to raise rates, whereas if the downside risks highlighted by some of the business surveys materialise they will need to follow the Fed and lower rates. UK government bonds delivered 6.7% over the quarter.

In Japan, the consumption tax hike has just come into place, posing a risk to an economy that is already feeling the effects of the global slowdown in manufacturing. Faced with these risks, Japanese consumer confidence continued to decline this quarter. The Bank of Japan also resisted the temptation to join in the easing game, but said it would review the outlook at its next meeting, perhaps hinting at further easing to come. Japanese equities delivered 3.4% over the quarter.

Of course, the trade war also continued to play a prominent role in financial headlines throughout the quarter. As things currently stand, further tariffs are due to come into place by the end of the year unless renewed talks between the US and China make sufficient progress. Failure to prevent further tariffs could hurt the global economy, so it's set to be another quarter of carefully monitoring the developments on trade.

China's economy continued to slow, with industrial production growing at 4.4%, down from around 7% at the start of 2018. Retail sales also slowed, to 7.5% from close to 10% in early 2018. However, with growth still comfortably above that in the US, and given that the US economy is also slowing as a result of the trade dispute and there is a US election next year, it's far from clear that China will concede to US demands on trade. EM equities delivered -1.9% over the quarter.

**Exhibit 3: Fixed income government bond returns in local currency**

2013	2014	2015	2016	2017	2018	YTD	3Q 2019
Spain 11.3%	Spain 17.0%	Italy 4.9%	UK 10.7%	US 2.5%	Spain 2.6%	Italy 14.4%	Italy 8.5%
Italy 7.4%	Italy 15.7%	Spain 1.7%	Spain 4.2%	UK 1.9%	Germany 2.3%	UK 12.1%	UK 6.7%
Japan 2.2%	UK 14.1%	Global 1.3%	Germany 4.1%	Global 1.3%	Japan 1.1%	Spain 11.0%	Global 2.8%
Global -0.4%	Germany 10.5%	Japan 1.3%	Japan 3.6%	Spain 1.1%	Global 1.0%	US 8.1%	US 2.6%
Germany -2.3%	Global 8.5%	UK 1.2%	Global 2.9%	Italy 0.8%	US 0.8%	Global 8.0%	Spain 2.2%
US -3.4%	US 6.1%	US 0.9%	US 1.1%	Japan 0.2%	UK 0.6%	Germany 6.5%	Germany 2.2%
UK -4.2%	Japan 4.8%	Germany 0.4%	Italy 0.8%	Germany -1.4%	Italy -1.4%	Japan 3.4%	Japan 0.4%

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. Past performance is not a reliable indicator of current and future results. Data as of 30 September 2019.

Helped by central bank easing and rising concerns about the global growth outlook, it was another good quarter for government bonds, albeit with a temporary sell-off in early September. US Treasuries delivered over 2% in the third quarter. Global IG credit delivered 1.2%, while US high yield returned 1.3% and Euro high yield returned 0.9%.

**Exhibit 4: Fixed income sector returns in local currency**

2013	2014	2015	2016	2017	2018	YTD	3Q 2019
Euro HY 8.8%	Euro Treas. 13.1%	Euro Treas. 1.6%	US HY 17.5%	EM Debt 9.3%	Euro Treas. 1.0%	EM Debt 12.1%	Euro Treas. 3.8%
US HY 7.4%	EM Debt 5.5%	EM Debt 1.2%	EM Debt 10.2%	Global IG 9.1%	US Treas. 0.9%	US HY 11.5%	US Treas. 2.4%
Euro Treas. 2.2%	Euro HY 5.5%	US Treas. 0.8%	Euro HY 10.1%	IL 8.7%	US HY -2.3%	Euro Treas. 10.0%	IL 1.7%
Global IG 0.3%	US Treas. 5.1%	Euro HY 0.5%	Global IG 4.3%	US HY 7.5%	Global IG -3.6%	Global IG 9.6%	EM Debt 1.3%
US Treas. -2.7%	IL 3.4%	Global IG -3.6%	IL 3.9%	Euro HY 6.1%	Euro HY -3.6%	Euro HY 8.5%	US HY 1.3%
IL -3.2%	Global IG 3.1%	US HY -4.6%	Euro Treas. 3.2%	US Treas. 2.3%	IL -4.1%	IL 8.0%	Global IG 1.2%
EM Debt -6.6%	US HY 2.5%	IL -5.0%	US Treas. 1.0%	Euro Treas. 0.2%	EM Debt -4.6%	US Treas. 7.7%	Euro HY 0.9%

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 EMBIG. All indices are total return in local currency. Past performance is not a reliable indicator of current and future results. Data as of 30 September 2019.

Overall, the global economy faces several binary and highly unpredictable risks. Will the trade war escalate? Will a UK election lead to a no-deal Brexit? Will the recent tension in the Middle East escalate and cause another spike in the oil price? And will companies respond to slowing growth and profits by cutting jobs?

Until we have more clarity on the answers to these questions, we continue to believe that it makes sense to avoid overweight positions in equities and credit and to move up in quality within both. Within equities, large cap, quality, value stocks are likely to prove most resilient if the downside risks materialise. Within alternatives, investors may find diversification through investments in infrastructure, global macro strategies and gold. US Treasuries should also provide a hedge if growth rolls over.

**Exhibit 5: Index returns for September 2019 (%)**

INDEX	GBP	USD	JPY	EUR	LOC
<b>Equities (MSCI)</b>					
MSCI World	1.0	2.2	4.0	3.2	2.4
MSCI USA	0.6	1.8	3.6	2.8	1.8
MSCI Europe ex UK	1.0	2.2	4.1	3.3	3.2
MSCI United Kingdom	2.9	4.2	6.1	5.2	2.9
MSCI Japan	3.0	4.2	6.1	5.3	6.1
MSCI AC Asia ex JP	0.5	1.7	3.5	2.7	1.3
MSCI EM Latin America	1.4	2.6	4.5	3.7	2.9
MSCI EM (Emerging Markets)	0.7	1.9	3.8	3.0	1.5
<b>Bonds</b>					
JP Morgan GBI Global (Traded)	-2.5	-1.3	0.5	-0.3	-0.8
JP Morgan GBI United States (Traded)	-2.1	-0.9	0.9	0.1	-0.9
JP Morgan GBI Japan (Traded)	-4.3	-3.2	-1.4	-2.2	-1.4
JP Morgan GBI United Kingdom (Traded)	0.6	1.8	3.6	2.8	0.6
JP Morgan EMU	-2.6	-1.4	0.4	-0.4	-0.4
<b>Currencies</b>					
Sterling	n/a	1.2	3.0	2.2	n/a
US dollar	-1.2	n/a	1.8	1.0	n/a
Yen	-2.9	-1.8	n/a	-0.8	n/a
Euro	-2.2	-1.0	0.8	n/a	n/a

Source: MSCI, FactSet, J.P. Morgan Economic Research, J.P. Morgan Asset Management. Past performance is not a reliable indicator of current and future results. Data as of 30 September 2019.

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