MyStratWeekly
Market views and strategy

Ostrum ASSET MANAGEMENT

N° 183 / **November 25, 2024**

This document is intended for professional clients in accordance with MIFID

Axel Botte
Head of Market Strategy
axel.botte@ostrum.com

Zouhoure Bousbih
Emerging countries strategist
zouhoure.bousbih@ostrum.com

Aline Goupil-Raguénès
Developed countries strategist
aline.goupil-raguenes@ostrum.com

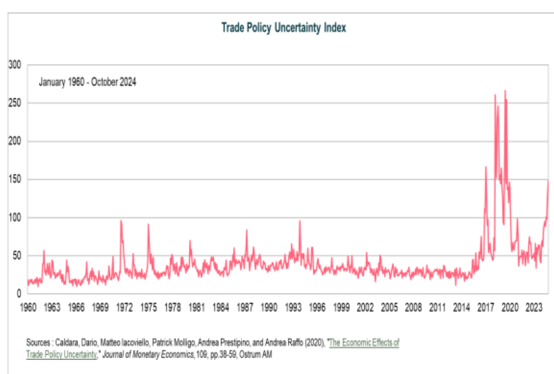
Topic of the week: U.S. equities: Will the music stop?
by Axel Botte

- The U.S. equity market rallied on the news of the election of Donald Trump. The S&P 500 is up 24% so far this year led by the stellar performance of the Magnificent 7 group;
- The Mag7 profit growth has slowed to 25% in the third quarter. Corporate earnings have been flat for the S&P;
- The sustainability of the equity bull market will depend on a range of factors, including valuations, long-term interest rates and the sequencing of policies;
- Trump is calling for unprecedented tariff increases. This brings back memories of the Smoot-Hawley Act which compounded the impact of the 1929 equity market crash and the economic depression;
- The risk of fiscal slippage appears very high under the incoming Trump administration. Higher yields could break the equity rally;
- • The S&P 500's equity risk premium has fallen to 0%. The Technology sector is now trading at negative risk premiums. This draws comparisons to the TMT bubble of late 1990s.

Market review: The temperature is gradually rising.
by Axel Botte

- Military escalation between Russia and Ukraine;
- The Bund plunges below 2.30% after mediocre PMI data;
- Credit and equities trade sideways;
- Gold and the dollar as vectors of risk aversion.

Chart of the week



The trade policy uncertainty index (TPU) is constructed by staff in the International Finance Division of the Federal Reserve Board and measures media attention to news related to trade policy uncertainty. The index reflects automated text-search results of the electronic archives of 7 leading newspapers discussing trade policy uncertainty: Boston Globe, Chicago Tribune, Guardian, Los Angeles Times, New York Times, Wall Street Journal, and Washington Post.

The index is scaled so that 100 indicates that 1% of news articles contain references to TPU.

Figure of the week

15/11

This year, the Equal Pay Day in the EU falls on November 15. For equal work, women earn 13% less than men. For the European Commission, pay transparency is essential to bridge this gap.
Source: European Commission

Topic of the week

U.S. equities: Will the music stop?

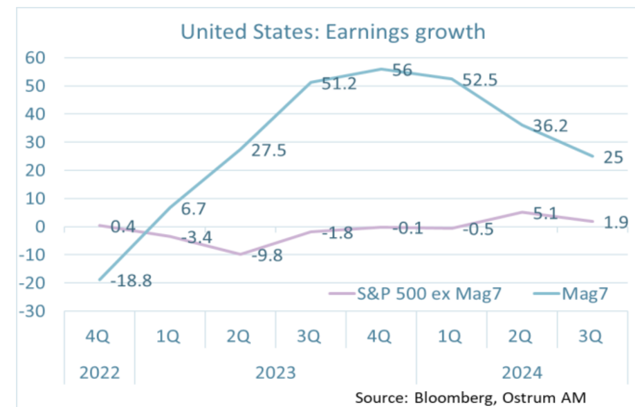
The S&P 500 rallied on the news that Donald Trump won the election. Other markets have experienced losses as investors remain convinced of US exceptionalism in terms of economic growth. The sustainability of the equity bull market will depend on a range of factors, including valuations, long-term interest rates and the sequencing of policies. The latter includes decisions on tariffs, tax cuts and monetary policy.

Corporate America earnings fatigue

Earnings power concentrated in Mag7

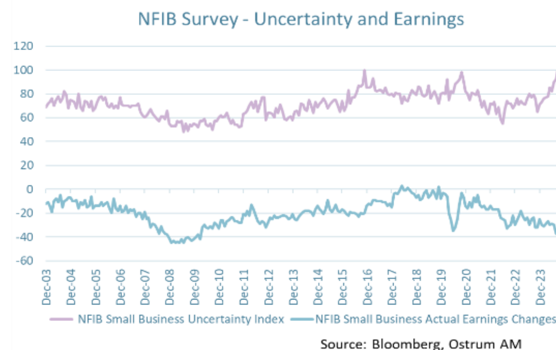
The 3Q 2024 corporate earnings season is now almost complete. As per usual, steep downgrades to EPS consensus in the runup to the release ensured that most EPS surprises came on the upside with an average beat of 7%. That said, actual EPS growth slowed from a year ago.

Moreover, there is a stark difference between earnings of AI-linked firms and the rest of the market. The Magnificent 7 (Mag7) stocks posted earnings growth of 25% year-on-year in the September quarter. Still solid but sharply slower than the 36.2% annual increase recorded in the second quarter. The same is true of sales growth which decelerated from 14.7% to 11.9%.



But that is not the main point. Earnings growth for the rest of the market (S&P 500 ex Mag7) is essentially flat since the end of 2022 with only a modest yearly increase in the third quarter (+1.9%). The topline numbers are also lackluster and exhibit the same kind of discrepancy between the Mag7 and the rest. The broader picture is not different. Profits for the companies included in the Russell 2000 Index have been negative by more than 10% from a year prior.

The earnings outlook appears to be clouded by unprecedented uncertainty. The NFIB survey, which gathers information from small business owners, sheds some light on the uncertainty factor and the corporate earnings outlook. Truth be told, it is hard to link micro surveys of independent business to profits

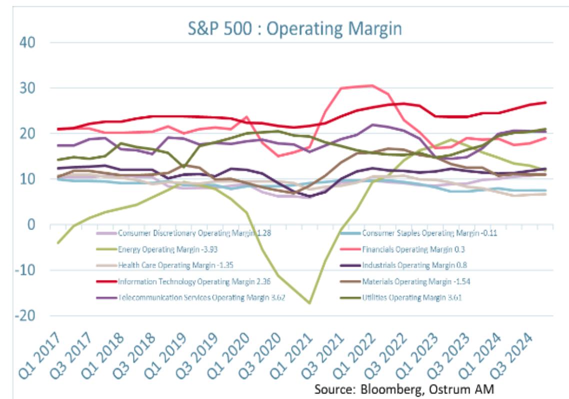


of large multinational firms listed on the equity market. Nevertheless, given current extreme levels, the NFIB survey may still be informative for market participants. The NFIB profit component has been falling sharply in the past year.

As concerns labor costs, the survey has long pointed to compensation pressure and hiring difficulties. The wage data from a top-down perspective were less conclusive. The annual increase in the average hourly earnings is flat about 4%. The employment cost index slowed to a moderate increase of 0.8% on a quarterly basis in the third quarter. However, unit labor costs were revised upwards (to 1.9% in the September quarter) as labor compensation outpaced productivity.

Technology margins contribute considerably to overall profits of the S&P 500

Digging into the profitability data of the S&P 500 sectors, the information technology is posting the highest operating followed by telecommunication services and utilities. The operating margin in information technology is projected to rise steadily above 26% in the final quarter of 2024, which would amount a 236 bp increase over the past 4 quarters. Margins are stable in other industries, and indeed falling in energy, materials, and health care. The four-quarter change in operating margins is indicated in the key in the chart opposite.



Source: Bloomberg, Ostrum AM

What could kill the bull market?

The biggest risk for an equity market driven by growth stocks is an unexpected rise in long-term interest rates. As it stands, upside risk will not stem from Fed policy. The FOMC is currently dialing down its restrictive stance. Fed rates may continue to fall towards 4% by March nearing the high end of the neutral interest rate range. However, fiscal slippage could justify a higher term or sovereign credit premium and, thus a steeper real yield curve. In the summer of 2023, the 10-Yr note yield hit 5% which triggered verbal intervention by Governor Christopher Waller and Dallas Fed President Lorie Logan. Policymakers worried about risks to financial stability, just a few months after the demises of Silicon Valley Bank and Signature Bank. Were long-term rates to rise, corporate earnings streams far out into the future would have a lower present value. Current equity valuations are no longer cheap enough to accommodate higher yields. The gap between the forward earnings yield and the U.S. 10-Yr note yield suggests that the equity risk premium is currently about 0%. As concerns the technology sector, the equity risk premium is down to deeply negative levels last seen during the dotcom bubble of the late 1990s. Valuations are reminiscent of the early days of what Greenspan had called ‘irrational exuberance’.

Source: Bloomberg, Ostrum AM

Tariffs have the potential to be disruptive

Higher tariffs and trade sanctions could disrupt the bull market. The Smoot-Hawley tariff increase on agricultural and industrial goods passed Congress in 1930. The bill aimed at protecting American farmers and other industries from foreign competition. The Smoot-Hawley Act hiked tariffs by about 20% and at least 25 countries responded by increasing their own tariffs on U.S. goods. With hindsight, the Smoot-Hawley Act is now widely blamed for worsening the severity of the Great Depression in the U.S. and around the world. The ensuing deeper depression prolonged the bear market in stocks. In today's world economy, tit-for-tat trade policies would have similar effects. The trade policies proposed by Donald Trump thus represent downside risks for U.S. and global equities.

Conclusion

The U.S. equity market had stellar performances so far this year (+24%). Higher prices combined with lackluster profit growth except for the AI-powered Magnificent 7 has shrunk the equity risk premium over 10-Yr yields to 0%. Valuations now draw comparisons to the dotcom bubble. Moreover, tariff hikes on all countries are reminiscent of the Smoot-Hawley Act, that contributed to extend the downward spiral in the world economy following the 1929 crash.

Axel Botte

Market review

The temperature is gradually rising.

The situation in Ukraine is escalating, leading to a retreat into bonds, the dollar, and gold. Equities are treading water, while credit continues to attract inflows.

The military escalation between Russia and Ukraine, coupled with a decline in economic surveys across the Eurozone, has contributed to a drop in bond yields over the past week. The swap spread, a gauge of risk aversion, has turned positive for the 10-year maturity. However, most asset markets exhibit neither a clear trend nor excessive volatility. In European equity markets, cyclical stocks are underperforming compared to defensive growth stocks. Credit spreads are hovering around 90 basis points over swaps. The dollar remains strong, gold benefits from the troubled international backdrop, and bitcoin appears to factor in the potential support from a future Trump administration. The euro, trading below $1.05, reflects expectations of a 50 basis point cut in the ECB's rate in December.

The European economic landscape remains fragile. Indicators are not uniformly weak, but it is the PMIs that are capturing investors' attention. A decline in services surveys is evident in France (-3.5 points) and Germany. The Eurozone composite PMI stands at 49.7 in November. While the INSEE indicator is somewhat more nuanced, uncertainty surrounding U.S. trade policy prevails. German growth has been revised down to +0.1% for the third quarter. Exports have contracted (-2.4%), and public investment, particularly in construction, has plunged by another 2.9%. The end of destocking provides the only positive contribution to growth. In the United States, housing starts remain insufficient, compounding delays on granted building permits. Existing home sales are stifled by mortgage rates (6.90% for 30 years) significantly higher than the average rate paid by households.

In financial markets, the announcement of a shift in Russia's nuclear doctrine in response to Ukrainian strikes on Russian territory has resulted in a flight to safe assets. The T-note eased to 4.34% before climbing back to around 4.40%. The 20-year bond auction, often overlooked by investors, attracted less interest. The ECB appears poised to cut rates as early as December, its sole tool to stimulate demand and counter Donald Trump’s plans. The curve steepening resumes with the release of PMIs. The Bund has dropped to 2.30%. However, Germany’s financing needs, net of the ECB’s portfolio amortization, are significant in 2025 (estimated at €137 billion by Citi). France finds itself in a similar situation, facing €167 billion in market calls amid an even more uncertain political backdrop. The spread on OATs is once again approaching 80 basis points. In credit markets, the decline in German yields has led to an widening of measured spreads. Valuations in the investment-grade segment are oscillating around 90 basis points over swaps. This excess yield continues to attract flows, particularly into actively managed credit funds. The primary market is expected to come to a halt after one last week. There is likely value in the spreads of secured bonds, averaging over 40 basis points.

Equity markets are directionless, with cyclicals underperforming. Nvidia is no longer sufficient to drive markets higher. The dollar and gold reflect a preference for safety.

Axel Botte

Main market indicators

G4 Government Bonds	25-Nov-24	1wk (bp)	1m (bp)	2024 (bp)
EUR Bunds 2y	2.04%	-15	-8	-37
EUR Bunds 10y	2.25%	-13	-5	+22
EUR Bunds 2s10s	20.7bp	+2	+3	+59
USD Treasuries 2y	4.34%	+6	+24	+9
USD Treasuries 10y	4.35%	-7	+11	+47
USD Treasuries 2s10s	0bp	-13	-13	+37
GBP Gilt 10y	4.38%	-9	+14	+84
JPY JGB 10y	1.08%	-1	-10	-51
€ Sovereign Spreads (10y)	**25-Nov-24**	**1wk (bp)**	**1m (bp)**	**2024 (bp)**
France	82bp	+9	+8	+28
Italy	128bp	+8	+2	-40
Spain	74bp	+5	+4	-23
Inflation Break-evens (10y)	**25-Nov-24**	**1wk (bp)**	**1m (bp)**	**2024 (bp)**
EUR 10y Inflation Swap	1.93%	-6	-5	-20
USD 10y Inflation Swap	2.54%	0	+7	+13
GBP 10y Inflation Swap	3.59%	+1	+1	+5
EUR Credit Indices	**25-Nov-24**	**1wk (bp)**	**1m (bp)**	**2024 (bp)**
EUR Corporate Credit OAS	107bp	+7	+3	-31
EUR Agencies OAS	65bp	+5	+4	-5
EUR Securitized - Covered OAS	57bp	+10	+3	-21
EUR Pan-European High Yield OAS	328bp	+6	-14	-71
EUR/USD CDS Indices 5y	**25-Nov-24**	**1wk (bp)**	**1m (bp)**	**2024 (bp)**
iTraxx IG	57bp	+1	0	-2
iTraxx Crossover	304bp	+3	-4	-10
CDX IG	49bp	0	-4	-8
CDX High Yield	300bp	-7	-28	-56
Emerging Markets	**25-Nov-24**	**1wk (bp)**	**1m (bp)**	**2024 (bp)**
JPM EMBI Global Div. Spread	330bp	-3	-13	-54
Currencies	**25-Nov-24**	**1wk (%)**	**1m (%)**	**2024 (%)**
EUR/USD	$1.049	-0.973	-2.853	-5.0
GBP/USD	$1.258	-0.671	-2.939	-1.2
USD/JPY	JPY 154	0.207	-1.341	-8.6
Commodity Futures	**25-Nov-24**	**-1wk ($)**	**-1m ($)**	**2024 (%)**
Crude Brent	$74.9	$1.6	-$0.7	0.3
Gold	$2 679.4	$68.9	-$68.2	29.9
Equity Market Indices	**25-Nov-24**	**-1wk (%)**	**-1m (%)**	**2024 (%)**
S&P 500	5 969	1.68	2.78	25.1
EuroStoxx 50	4 807	0.34	-2.76	6.3
CAC 40	7 267	-0.16	-3.08	-3.7
Nikkei 225	38 780	1.46	2.28	15.9
Shanghai Composite	3 264	-1.81	-1.09	9.7
VIX - Implied Volatility Index	15.12	-2.95	-25.63	21.4

Source: Bloomberg, Ostrum AM

Additional notes

Ostrum Asset Management

Asset management company regulated by AMF under n° GP-18000014 – Limited company with a share capital of 50 938 997 €. 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
This document is intended for professional, 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, which under no circumstances constitutes a commitment from Ostrum Asset Management.
The analyses and opinions referenced herein represent the subjective views of the author(s) as referenced, are as of the date shown and are subject to change without prior notice. There can be no assurance that developments will transpire as may be forecasted in this material. This simulation was carried out for indicative purposes, on the basis of hypothetical investments, and does not constitute a contractual agreement from the part of 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.
Final version dated 25/11/2024

Natixis Investment Managers

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 San Clemente 1, 20122 Milan, Italy. Germany: Natixis Investment Managers S.A., Zweigniederlassung Deutschland (Registration number: HRB 88541). Registered office: Im Trutz Frankfurt 55, Westend Carrée, 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 516405-9601 - Swedish Companies Registration Office). Registered office: Kungsgatan 48 5tr, Stockholm 111 35, Sweden. Spain: Natixis Investment Managers, Sucursal en España. Serrano n°90, 6th Floor, 28006, Madrid, Spain. Belgium: Natixis Investment Managers S.A., Belgian Branch, Louizalaan 120 Avenue Louise, 1000 Brussel/Bruxelles, Belgium.
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 Sàrl, Rue du Vieux Collège 10, 1204 Geneva, Switzerland or its representative office in Zurich, Schweizergasse 6, 8001 Zürich.
In the British Isles: Provided by Natixis Investment Managers UK Limited which is authorised and regulated by the UK Financial Conduct Authority (register no. 190258) - registered office: Natixis Investment Managers UK Limited, One Carter Lane, London, EC4V 5ER. When permitted, the distribution of this material is intended to be made to persons as described as follows: in the United Kingdom: this material is intended to be communicated to and/or directed at investment professionals and professional investors only; in Ireland: this material is intended to be communicated to and/or directed at professional investors only; in Guernsey: this material is intended to be communicated to and/or directed at only financial services providers which hold a license from the Guernsey Financial Services Commission; in Jersey: this material is intended to be communicated to and/or directed at professional investors only; in the Isle of Man: this material is intended to be communicated to and/or directed at only financial services providers which hold a license from the Isle of Man Financial Services Authority or insurers authorised under section 8 of the Insurance Act 2008.
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: Unit L10-02, Level 10 ,ICD Brookfield Place, DIFC, PO Box 506752, 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 2020 FSC SICE No. 025, Tel. +886 2 8789 2788.
In Singapore: Provided by Natixis Investment Managers Singapore Limited (company registration no. 199801044D) to distributors and institutional investors for informational purposes only.
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, 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, securities intermediary, 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. While shares of certain ETFs may be listed in the Sistema Internacional de Cotizaciones (SIC), such listing does not represent a public offering of securities in Mexico, and therefore the accuracy of this information has not been confirmed by the CNBV. 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. Any reference contained herein to "Investment Managers" is made to Natixis Investment Managers and/or any of its investment management subsidiaries, which are also not authorized by or registered with the CNBV or any other Mexican authority.
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.