

Markets & Investing

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The day in the markets

What you need to know

- Oil price plunges after Trump fires national security adviser Bolton
- Bonds sell off and stock moves are muted ahead of ECB policy meeting
- US and China equities soft following weak jobs and price data

Sovereign bonds sold off while stock moves stayed muted ahead of tomorrow's European Central Bank meeting, where policymakers were expected to unveil stimulus measures aimed at reviving the region's sluggish economies.

The yield on Germany's benchmark 10-year bonds rose more than 3 basis points to minus 0.55 per cent, while the FTSE All-World Index retreated 0.2 per cent.

"The equity rally seems to have stopped," said Peter Garnry, head of equity strategy at Saxo Bank. "It seems investors are waiting for the important ECB meeting before adding more risk."

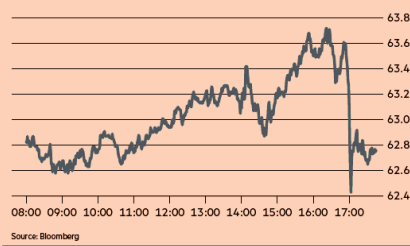
The pan-regional Stoxx Europe 600 edged up 0.1 per cent as investors paused to see just how far policymakers would go to boost growth on the continent.

Milan's FTSE MIB fell 0.6 per cent while the CAC index in Paris ended the day 0.1 per cent higher.

The cautious tone followed on from trading in Asia where the CSI 300 index of Chinese stocks fell 0.3 per cent after reports that the country's producer prices had fallen at their fastest pace in three years.

Oil price falls after exit of national security adviser Bolton

Brent crude price (\$ per barrel)



Source: Bloomberg

Sentiment on Wall Street was equally cautious after employment data revealed that the once-hot US labour market was cooling.

Job openings slid to the lowest level in five months in July, according to the US labour department.

The Dow Jones Industrial Average was flat by midday in New York while the S&P 500 and Nasdaq Composite indices both slid 0.2 per cent.

However, a better employment picture in the UK alongside further stalled progress on a no-deal Brexit

helped keep sterling above \$1.23 against the dollar.

In the three months to July, annual growth in average weekly earnings for employees increased to 4 per cent for total pay, said the Office for National Statistics, up from 3.8 per cent in the three months to June.

Brent, the international benchmark, erased an early 1.9 per cent gain after Donald Trump fired national security adviser John Bolton. WTI's rise also vanished as the US market fell 0.2 per cent to \$57.72 a barrel. **Ray Douglas**

Negative yields leave EM investors with nowhere to hide

Steve Johnson

Markets Insight



Rarely has the choice facing the emerging market investor been so stark. Bonds are so richly priced that around 30 per cent of the entire universe of euro-denominated EM debt with a face value of about €115bn trades at a negative yield, according to investment bank Morgan Stanley.

That has never happened before. Not all of this negatively yielding debt consists of short-maturity bonds issued by the EU sovereigns of eastern and central Europe, which are usually considered "safe" by fixed income investors.

The bundle includes Polish government debt at a maturity as far out as 2026, along with bonds from Indonesia, China and South Korea. The sub-zero club even includes Mexico, which is run by a leftist president who has already renegotiated contracts with foreign investors.

One-fifth of the negative-yielding EM debt comes courtesy of corporate issuers, such is the demand for income from investors grappling with vanishing yields in the eurozone's core.

At the same time, emerging market equities are in desperate need of some friends. Around 30 per cent of stocks in the MSCI EM index trade below their book value, noted Goldman Sachs.

This is the most distressed valuation for a decade and the lowest level ever outside a US recession, Goldman said. The entire MSCI Korea index, a benchmark heavily dependent on the health of global trade and economic growth, has recently dipped below 0.8 times book value this year, reaching its lowest levels since 2001.

Given the state of the world, it is hard to think of an obvious catalyst to bring these glaring anomalies back into order. The European Central Bank seems

determined to unleash another wave of quantitative easing, despite indications that each round of bond-buying delivers less marginal utility than the last.

Barring a resolution of the US-China trade war, it is hard to see an obvious catalyst to drive meaningfully higher global growth, which would pep up EM equities.

Logic might dictate that some degree of reversion to the mean in both equities and bonds is inevitable, however, even if the path to such an outcome remains murky.

An index operated by Bank of America Merrill Lynch suggested that such a

'Positioning is already very bullish anyway so we have the potential for positive surprises'

moment could be nigh. The bank's Bull & Bear Indicator, based on factors such as asset allocation, flow data, and futures and options pricing has just flipped into "extreme bearish" territory, triggering a contrarian "buy" signal.

According to David Hauner, head of EM cross asset strategy and economics at BofA, this is the 17th time this has happened since 2000. On each of the 16 previous occasions, 10-year Treasury yields rose in the ensuing three months by an average of 50 basis points.

On 10 occasions, global stocks rose in the following quarter with a median return of 6.3 per cent. The previous buy signal, triggered on January 3 this year, saw the S&P 500 stock index rally 17 per cent in the following three months. The latest signal is a far stronger one than that of January, according to BofA.

"There are lots of reasons to be bullish but positioning is already very bullish anyway so we have the potential for positive surprises," Mr Hauner said.

Even Mr Hauner admitted it was hard to tell what "story" might justify any market rebalancing.

He expected the US-China trade war to linger and said it would be hard for either the US Federal Reserve or the ECB to pleasantly surprise investors already expecting large doses of easing.

His best stab at answering this question was to say there were signs that the "massive drop" in global manufacturing purchasing managers' indices appeared to be petering out with activity stabilising at low levels, "just short of falling into a major recession".

What the markets do next is clearly dependent on the macroeconomic backdrop. If the US is heading into recession, as some fear, then there was nothing unusual about large swaths of EM equities trading below book value, amid a general flight to quality.

More likely, perhaps, is that both the global economy and the markets bump along largely as they are, pending any resolution of the trade stand-off.

But any major breakthrough could have an outsized impact on EM assets. Not one would be good for stocks and bad for bonds but the impact would be magnified by the fact the EM equity index has a 75 per cent weighting to Asia — the most trade-sensitive EM region — which is far higher than for the major corresponding bond benchmarks.

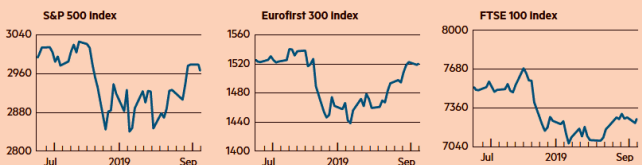
So far, President Donald Trump has caused EM equity investors to grind their teeth in frustration. They are now looking to him to make their asset class great again.

steve.johnson@ft.com

Markets update

	US	Eurozone	Japan	UK	China	Brazil
Stocks	S&P 500	Eurofirst 300	Nikkei 225	FTSE100	Shanghai Comp	Bovespa
Level	2966.22	1520.36	21922.10	7267.95	3021.20	103376.85
% change on day	-0.41	0.10	0.35	0.44	0.12	0.19
Currency	\$ Index (DXY)	€ per \$	¥ per \$	£ per \$	Rmb per \$	Real per \$
Level	98.377	1104	107.285	1.235	7.105	4.114
% change on day	0.098	-0.181	0.117	0.081	-0.334	0.621
Govt. bonds	10-year Treasury	10-year Bund	10-year JGB	10-year Gilf	10-year bond	10-year bond
Yield	1.679	-0.552	-0.230	0.563	3.043	7.394
Basis point change on day	6.430	3.600	3.080	4.800	2.000	-0.600
World index, Commods	FTSE All-World	Oil - Brent	Oil - WTI	Gold	Silver	Metals (LME)
Level	343.08	62.65	57.59	1509.20	18.17	2831.20
% change on day	-0.11	-0.10	-0.78	-0.95	0.14	0.07

Main equity markets



Biggest movers

	US	Eurozone	UK
Up	Nektar Therapeutics 9.35	Seadrill 24.21	lid Sports Fashion 8.79
Liq	7.14	Casino Gulchard 4.47	Barclays 4.90
Quantia Services 6.48	Saint Gobain 4.11	Lloyds Banking 4.26	
State Street 5.54	Randstad 3.96	Inf Consolidated Airlines S.a. 4.06	
Schlumberger 5.08	Norsk Hydro 3.92	Micro Focus Int 4.01	
Down	Marketaxess Holdings -6.56	Edf -6.77	Just Eat -6.58
Chipotle Mexican Grill -5.55	Airbus -3.58	Aveva -5.03	
Msci -4.27	Coloplast -3.11	Sage -6.10	
Sba Communications -4.23	Reed Elsevier -2.89	Experian -4.08	
Cadence Design Systems -4.05	Novo Nordisk -2.86	London Stock Exchange -3.90	

Wall Street

Wendy's tumbled after revealing plans to relaunch a breakfast menu across the US next year.

Management booked a one-off \$20m cost for 2019 to support the expansion as well as backing away from 2020 targets ahead of an investor day next month.

The burger chain operator has attempted to break the crowded, low-margin US breakfast market in 2012 but abandoned the strategy at nearly all of its restaurants within a year. "The breakfast launch introduces a layer of operational and financial risk we had not previously contemplated," said BMO.

Chipotle Mexican Grill fell after New York City officials sued it for alleged violations of its Fair Workweek law.

Schlumberger rose after a Morgan Stanley upgrade of the oil services group. It said a restructuring under Olivier Le Peuch, the new chief executive, could improve free cash flow even without higher oil prices and contract values.

Mallinckrodt, whose potential opioid liabilities have reportedly forced it to consider seeking bankruptcy protection, rebounded after selling a manufacturing subsidiary to private equity for \$250m.

Merit Medical faded after Raymond James turned cautious on the device maker. **Byrce Elder**

Eurozone

EDF retreated after warning that its nuclear engineering unit, Framatome, had found flaws in reactor components including some that were in service.

The French utility said it had started an in-depth investigation to identify all components and reactors affected.

Ferrari led a drop for the year-to-date's best-performing stocks, which traders blamed on a rotation towards lower valued sectors such as property, airlines and banks as bond yields rose.

Payment companies also suffered in the switch, with Germany's Wirecard lower after JPMorgan Cazenove started coverage with a "neutral" rating.

DSV, the Danish freight transport and logistics group, weakened after Bernstein Research started coverage with an "underperform" rating.

It said the integration of Panalpina, the Swiss peer that DSV bought last month for about £3.5bn, was likely to cause integration.

Electrolux edged higher after setting out plans to cut almost 1,700 jobs.

Bic, the maker of lighters, razors and pens, gained after an Exane upgrade. Medium-term growth looked tough given "structural headwinds against lighters" from vaping but the risk was in the price, it said. **Byrce Elder**

London

Competition worries weighed on Rentokil after US-listed peer ServiceMaster expanded its European operations with the purchase of Nomor, the continent's fourth-biggest pest-control company.

The wider market was held back by sterling strength and sector rotation away from growth stocks such as Aveva, the software maker.

Barclays and Lloyds Banking Group led the financials higher as bond yields rose while perceptions of a lessening no-deal Brexit risk moved easyJet and British Airways owner IAG upwards.

Just Eat dropped in tandem with Takeaway.com, its Amsterdam-listed predator.

The fall came after Naspers-backed peer Delivery Hero hedged part of its 15.5 per cent stake in Takeaway.com using an equity collar agreement, which added another layer of complication to counterbid hopes around Just Eat.

Traders also noted web traffic analysis from Citigroup suggesting Just Eat was losing market share in the UK, Canada and potentially Brazil.

Purplebricks gained on a Dealporter retreat of talk that Axel Springer, the estate agent's 27 per cent shareholder, was interested in a full takeover. **Byrce Elder**

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