For Investment Professionals only

Equities market perspective

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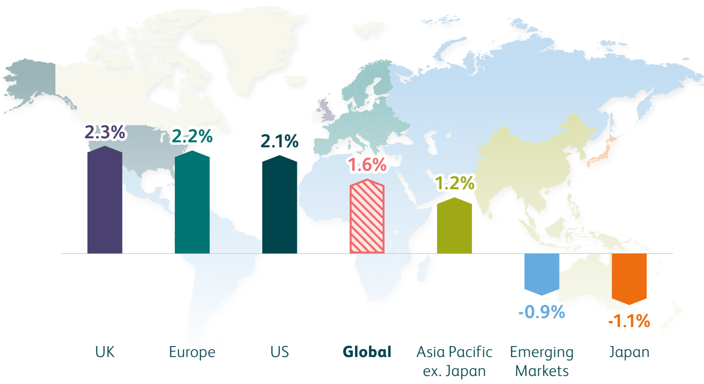
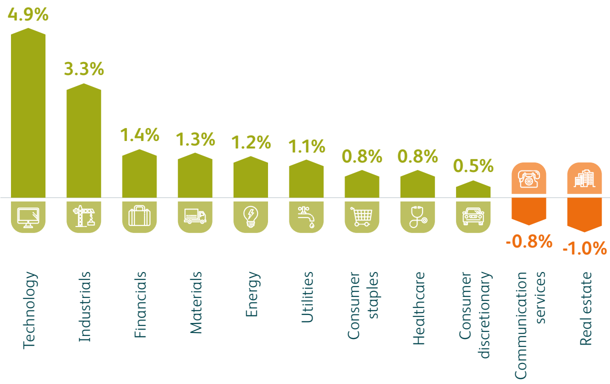
March 2019

Market summary

Regional performance – February 2019



Global sector performance – February 2019



Global equities: Equity markets extended the New Year rally and finished February in positive territory. The MSCI AC World Index delivered year-to-date returns of over 10% (in USD terms), marking the third strongest start to a year on record. Developed markets outperformed emerging markets overall, with the latter delivering marginal returns over the month. From a sector perspective, technology was the stand-out performer in February with software, semiconductors and tech hardware stocks all delivering strong returns. Cyclical sectors such as industrials pulled ahead of more defensive areas of the market, with communication services, consumer staples and healthcare lagging.

UK: Despite the ongoing Brexit saga, UK equities logged gains overall, with mid-cap stocks outperforming large-cap stocks during the month. Sterling strengthened against the US dollar.

Europe: Despite weaker economic indicators and signs of slowing growth in Europe, the region was one of the strongest gainers in February, behind UK mid-caps.

US: The S&P 500 recorded its fifth-best gain to start a year. The progression of the US-China trade talks helped US equities further, especially driven by sectors more exposed to international revenues like technology, materials and industrials.

EM/Asia ex Japan: Chinese shares outperformed as an increase in the Caixin maufacturing gauge and confirmation that MSCI Inc. will raise the weight of Chinese stocks in its global benchmarks buoyed sentiment. LATAM underperformed during the month.

Other: Brent crude was up during the month and has returned just shy of 23% (in USD) year to date. Renewed risk appetite supported global high yield, but weighed on 10-year US Treasuries and German bunds over the month.

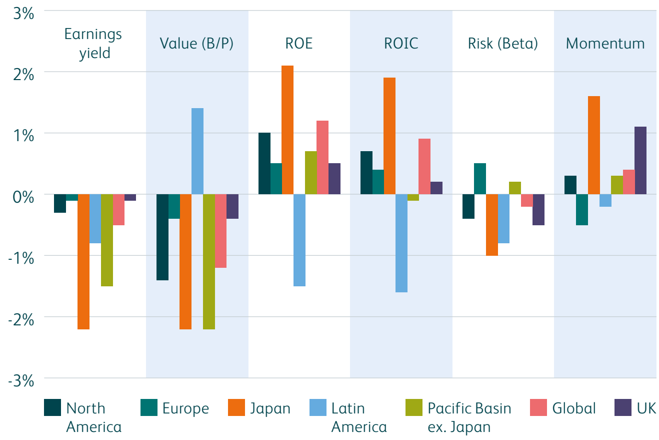
Market data

Total returns (%)	MSCI AC World		FTSE All-Share		S&P 500		MSCI Europe		MSCI Asia Pac x Jap		MSCI EM	
	Feb	YTD	Feb	YTD	Feb	YTD	Feb	YTD	Feb	YTD	Feb	YTD
GBP	1.6	6.2	2.3	6.6	2.1	6.7	2.2	5.5	1.2	5.1	-0.9	4.4
EUR	3.5	11.3	4.1	11.4	4.0	11.9	4.2	10.6	3.1	10.2	1.0	9.4
USD	2.7	10.9	3.4	11.3	3.2	11.5	3.4	10.2	2.3	9.8	0.2	9.0

Valuation	MSCI AC World	FTSE All-Share	S&P 500	MSCI Europe	MSCI Asia Pac x Jap	MSCI EM
(P/B)	2.2x	1.6x	3.3x	1.7x	1.6x	1.6x
(P/E)	16.2x	11.5x	19.5x	14.1x	12.9x	12.3x
(P/E FY1)	15.1x	12.8x	16.9x	13.5x	14.0x	12.5x

Source: Datastream & Factset, MSCI indices, S&P indices for the US, as at 28 February 2019. Total returns in GBP.

Style performance across regions: February 2019



Source: UBS Global Quantitative Research, 28 February 2019. All returns are relative to the relevant Dow Jones Global Indices regional index.

Currencies: percentage change over month and YTD (Majors vs GBP)

	Aus. Dollar	Yen	Swiss franc	Euro	US Dollar
Feb	-3.5%	-2.9%	-1.5%	-1.9%	-1.1%
YTD	-3.2%	-4.2%	-5.2%	-4.5%	-4.0%

Source: Datastream, 28 February 2019.

Theme of the month: Earnings season – some welcome surprises?

Key points

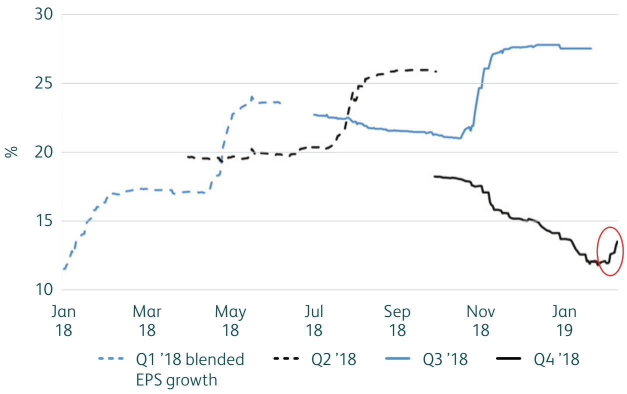
- Downward revisions to 4Q18 consensus earnings forecasts amid signs of slowing growth and 'earnings recession' rhetoric.
- Company results better than feared, with earnings suprises prompting upward revisions to consensus estimates.
- US led the earnings 'beats', but Europe and Japan still surprised to the upside. Company revenues also held up well.
- Earnings growth to moderate, but supportive economic backdrop and a dovish Fed should provide a welcome tailwind.

With the lion's share of fourth-quarter earnings results now behind us, here are some key observations and takeaways.

Investors have become accustomed to a blistering pace of earnings growth in the US. Profits per share are expected to have grown by 23% in 2018, with a compound annual growth rate of 12% over the past 10 years. Recently, however, the momentum has slowed. There has even been talk of an 'earnings recession'.

Amid signs of slowing economic growth, trade worries and concerns about the path of interest rates, we started to see significant downward revisions to earnings forecasts in the fourth quarter.

Evolution in S&P500 quarterly EPS estimates



Source: JP Morgan, Thomson Reuters, Feb 2019. 'Blended' refers to the analysts' forecasts for the remaining unreported companies blended with actual reported EPS.

For S&P500 companies, aggregate year-on-year quarterly earnings growth estimates fell from more than 18% in October last year to less than 12% by mid-January this year. This marked a break in the trend we witnessed throughout 2018, with upward revisions to consensus forecasts. Encouragingly, as companies reported actual fourth-quarter earnings, the 'blended' year-on-year earnings growth rate inflected higher.

In addition, the price action following announcements has been positive, suggesting that investors had been prepared for the worst and over-discounted the weakness. Indeed, markets rewarded positive earnings surprises more than average and punished negative earnings surprises less than average.

In aggregate, companies that reported forecast-beating results were rewarded with the best 'one-day' performance since the beginning of 2016, whilst the magnitude of downward price moves for missing estimates or lowering guidance was smaller in comparison.

This is in stark contrast to last year's first-quarter results, when 80% of S&P500 companies topped forecasts. However, much of the positive news, such as the windfall from Trump's tax reforms, was already priced in. The market reaction to positive surprises was relatively lacklustre, while investors punished those companies that undershot expectations.

Year to date, cyclical sectors have led equity market gains, but earnings beats have been broad-based, with both defensive and cyclical sectors surprising to the upside. In the US, nine sectors recorded positive quarterly EPS growth year on year, five of which posted double-digit growth.

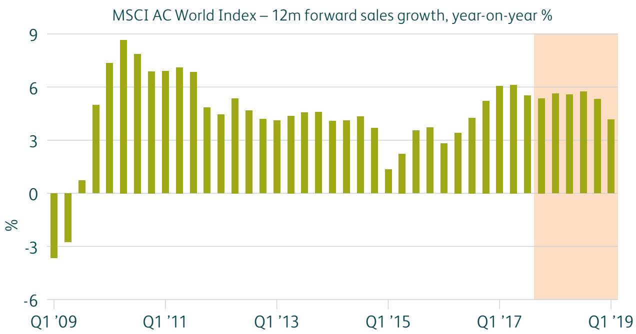
Over 70% of S&P500 companies delivered earnings 'beats'; industrials and technology had the highest percentage of above-consensus earnings, while energy and materials reported the lowest earnings 'beats', with around half of the companies in these sectors topping forecasts. Interestingly, energy companies that did report earnings 'beats' also delivered the biggest earnings surprises.

Earnings for S&P500 companies overall surprised positively by 3%. Results were softer in Europe and Japan, but earnings still surprised to the upside, with more than 50% of companies delivering earnings 'beats'.

Company revenues have also been holding up relatively well. Nearly 60% of S&P500 companies beat sales estimates. Aggregate sales growth came in at around 6% year on year, with all sectors except technology reporting positive growth.

Healthcare and industrials led the sales 'beats'.

Company revenues have been holding up relatively well



Source: M&G Investments, Datastream, 26 February 2019.

In Europe, 65% of Stoxx 600 companies delivered sales 'beats'. The weaker euro has likely helped companies' top line in the fourth quarter, leading to a higher proportion of sales beats in the region versus the US.

While earnings growth is set to moderate in 2019, tracking the more subdued growth outlook, we still expect to see companies (in aggregate) reporting growth. However, selectivity becomes more important as cost pressures start to bite into margins.

The backdrop remains supportive of continued positive earnings and revenue growth, while ongoing accommodative monetary policy – particularly a more dovish Fed – should provide a welcome tailwind for companies and investors alike.