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Dear investor,

- Just a few months ago trade growth was being cited as one of the main causes for a robust streak in the global economy but there are now **fears that we are beginning to see a slowdown in global trade growth linked to the potential trade war**.
- **As corporate profits are highly correlated with the state of the business cycle, this evolution could slow the earnings growth**. While we do not expect the U.S. to soon enter a recession, investors could end up deciding to cut their exposure to U.S. stock market if U.S. earnings begin to stagnate. And as U.S. equities account for 55% of global market capitalization, this could limit the upside for global equity indices.
- **To hedge against elevated risks, we maintain a neutral weighting to global equities**, while favoring developed market stocks over emerging markets and a more balanced allocation between defensive and cyclical sectors.

Thierry Masset, Chief Investment Officer ING Belgium

EQUITIES

Volatility is set for a comeback

While U.S. equity investors have kept their cool during this year's escalation of trade tensions, the warnings are only getting louder. The standout resilience of U.S. stocks is under threat with President Donald Trump authorizing a new round of levies against China. Amid the global retreat from monetary stimulus, this context is less favorable for equities.

U.S. stock price swings were so muted for the past two months that by some measures it was the calmest August and September since 1967! The VIX index, or Wall Street's fear gauge, averaged 12.5, lower than the five-year average of 14.6. More broadly, the cross-assets volatility still sits 45% below its 20-year average! Blame seasonality, but this situation is probably not sustainable. While the end of the U.S. summer season almost always boosts volatility, there are specific factors at play this year that also heighten risks. They include the turmoil in Emerging Markets as well as complicated Italian politics, trade tensions emanating from the Trump administration, midterm elections in the U.S. and less accommodative central banks. All that will probably add to stock-market swings. To hedge against elevated risks, we keep our defensive positioning. For the time being, we maintain a neutral weighting to global equities, while favoring developed market stocks over emerging markets and defensive stocks relative to cyclical ones.

BONDS

10 years after the Lehman Brothers' collapse...

Even if the combined balance sheet of the world's biggest central banks is still $7 trillion higher than when Lehman Brothers collapsed in September 2008, it has decreased by 8% since a $11.4 trillion peak. The impact of this evolution is the most significant in the U.S., where bond traders are loading up on U.S. super-safe cash-like instruments, such as short term Treasury's bills, as bets on the Federal Reserve raising interest rates two more times before year-end reach a new high. This all makes sense. Because of something investors call duration, securities with the shortest maturities lose less of their value when rates rise than longer-term bonds do.

Mario Draghi, the chief monetary authority for the 19 countries that use the euro, confirmed last month that its bond-buying stimulus would be cut to €15 billion a month from €30 billion as of October. The European Central Bank's stimulus exit is part of a global trend: the withdrawal of stimulus from the rich world's major monetary authorities, including the U.S. Federal Reserve, the Bank of England and the Bank of Japan. They loosened monetary policy to support the economy after the global financial crisis that deepened 10 years ago with the bankruptcy of U.S. investment bank Lehman Brothers. Their stimulus withdrawal should have wide-ranging effects. Low rates and bond purchases with newly created money lifted the prices of assets such as stocks and bonds. Raising rates and tightening monetary policy could make conservative holdings such as savings accounts, money market funds and certificates of deposit relatively more attractive for investors compared with riskier assets like stocks. That is why central banks are moving carefully to return rates to more normal levels.

OTHER ASSET CLASSES

Trade war chief worry for commodities

Besides steel and aluminum for which the Donald Trump administration applied tariffs to imports, other raw materials, such as base metals and energy, are vulnerable to escalating trade war as impact of protectionist measures on global trade would dent economic prospects across the world and hurt cyclically exposed assets.

Commodities recorded a monthly loss (-2% in euro) in September, bringing their decline since this year's peak in May to 6% as simmering U.S.-China trade tensions pushed the volatility of natural resources to the highest level since February 2017. The trade dispute between the world's two largest economies continued to rattle markets as the President Donald Trump has authorized a new round of tariffs on an additional $200 billion of Chinese goods, bringing the total to $250 billion and marking a significant new phase in the fight. Should there be a deep trade war, with ramifications for global growth, industrial commodities will be surely negatively affected. It is too early to judge how deep the impact of trade tariffs will be, but the uncertainty it will spread is a bearish signal that won't be easily shaken off.

IN THE NEWS

Italian stocks punished as budget in focus

The Italian stocks' roller-coaster is not expected to stop until there is further clarification from the government regarding the budget and whether it will breach the European Union's deficit limit of 3% of gross domestic product.

Tech jitters on the rise but Shiller is not afraid

It is no secret that a handful of tech-related stocks such as Facebook, Amazon, Apple, Netflix and Google-parent Alphabet have accounted for the bulk of the gains in the S&P 500 index this year. The Nasdaq 100 index that tracks these and similar equities has surged 19% (in euro) compared with 9% for the S&P 500. But last month it was the tech stocks (-2%) that have underperformed the broader market (-1%). Does that mean that the U.S stock market is at the end of its bull run? For Robert Shiller, the Nobel laureate who is famed for his analysis of asset-price bubbles, the answer is no!

Ferraris a better bet than stocks

A day after U.S. stocks smashed out yet another record, a vintage Ferrari went under the hammer for the highest price ever, indicating that we are in a more mature phase of the economic and financial cycle.

More information is available from your ING contact person.

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