

GIAM Macro & Market Research - Market Commentary

Q2 results look currently decent but earnings revisions remain weak. Dovish monetary policies are to compensate for earnings risk. Remain positive on equities.

- The Q2 reporting season has advanced to cover about 40% in the US and Europe. Both the earnings and sales' growth in the US stayed modestly positive (+3.7% and 5.2% yoy) at around the same level like in the quarter before. The analysts' expectations have been beaten both for earnings and sales.
- The earnings growth in Europe (-3.4%) as well as in the EA (-7.7%) has dropped as a result of higher weight of Energy and Materials (vs the US), which suffered globally. The sales growth has slightly decreased, remaining positive.
- Ex-Energy & Material, EU yearly earnings growth is in positive territory: 9.3% and 3.8% for earnings and sales, respectively.
- For the US index, sales growth is matched by earnings' one which could be seen as an early indication of stalling margin momentum.
- While the picture for Q2 is relatively decent, a prolonged stall in trade frictions and spikes in Brexit risk could maintain the manufacturing earnings momentum in negative territory for longer. That is why further negative revisions are not to be excluded short term.
- Overall, current consensus earnings growth expectations are to be considered still at risk. That said, given the already low revisions of the weakest sectors, the low equity positioning and, most of all, the strong dovish stance of global central banks, we maintain a positive view on equities.
- Initial results of the Indian reporting season point to improving earnings growth, with sales growth remaining solid (at 13%).

US results look decent notwithstanding a softening economic cycle, as testified by the increased negative pre-announcements and negative revisions for Q2.

For the median US stock, the earnings growth is nearly 6% while that of sales is 3.7%. Surprises are +3% for earnings and +0.3% for sales.

For the median sector, the earnings growth is 3.7% and that of sales is 5%, showing a decreasing margin momentum.

Analysis of the median stock: Q2 2019 reporting season

| Median stock | Earnings Growth | | Sales Growth | | availability |
|--------------|-----------------|---------|--------------|---------|--------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 | Q2 2019 |
| | S&P | 7.33 % | 6.53 % | 4.33 % | 3.76 % |
| Stoxx | 5.72 % | 5.54 % | 5.97 % | 5.25 % | 40.0% |
| Euro Stoxx | 1.38 % | 9.39 % | 4.22 % | 4.57 % | 34.2% |
| Topix | (1.44)% | (1.93)% | 2.70 % | 2.42 % | 16.5% |

| Median stock | Earnings Surpr | | Sales Surpr | | availability |
|--------------|----------------|---------|-------------|---------|--------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 | Q2 2019 |
| | S&P | 4.62 % | 2.67 % | 0.34 % | 0.27 % |
| Stoxx | 3.19 % | 3.24 % | 0.63 % | 0.55 % | 40.0% |
| Euro Stoxx | 3.45 % | 5.20 % | 1.05 % | 0.98 % | 34.2% |
| Topix | (6.76)% | 0.83 % | (1.13)% | (0.47)% | 16.5% |

S&P

222 reported 205 reported

| Sector | earnings growth, yoy | | sales growth, yoy | |
|--------------------------------|----------------------|-------------|-------------------|-------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 |
| Energy | -27.4% | -20.2% | -3.1% | -3.8% |
| Materials | -13.3% | -15.0% | -2.7% | -7.8% |
| Industrials | 2.8% | 3.0% | 4.9% | 2.7% |
| Consumer Discretionary | 20.9% | 1.8% | 6.7% | 10.3% |
| Consumer Staples | 0.5% | -0.4% | 3.1% | 3.3% |
| Health Care | 9.8% | 14.6% | 9.3% | 8.4% |
| Financials | 1.7% | 3.6% | 1.1% | 3.1% |
| Information Technology | 0.5% | -1.6% | 2.1% | 1.1% |
| Communication Services | 9.1% | 9.5% | 12.9% | 18.0% |
| Utilities | 11.6% | 13.9% | 1.7% | 0.0% |
| Real Estate | 11.6% | 13.3% | 3.3% | 11.5% |
| S&P | 4.1% | 3.7% | 4.8% | 5.2% |
| Median (all sectors) | 2.8% | 3.0% | 3.1% | 3.1% |
| Median, ex. Energy & Materials | 9.1% | 3.6% | 3.3% | 3.3% |

S&P

222 reported 205 reported

| Sector | earnings surprise % | | sales surprise % | |
|--------------------------------|---------------------|-------------|------------------|-------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 |
| Energy | 2.8% | 4.6% | -2.7% | 8.1% |
| Materials | 6.2% | 0.9% | -1.8% | -1.9% |
| Industrials | 5.1% | 5.1% | 0.5% | 0.5% |
| Consumer Discretionary | 24.0% | -0.1% | 0.3% | 3.6% |
| Consumer Staples | 3.7% | 5.1% | 0.4% | 0.5% |
| Health Care | 3.1% | 5.9% | 1.5% | 0.9% |
| Financials | 5.7% | 3.7% | 1.4% | 1.3% |
| Information Technology | 7.3% | 7.7% | 0.4% | 1.4% |
| Communication Services | 8.4% | 4.0% | -0.3% | 0.8% |
| Utilities | 4.5% | 8.9% | -3.4% | -4.3% |
| Real Estate | 2.6% | 2.1% | -1.3% | 3.5% |
| S&P | 6.6% | 4.6% | 0.4% | 1.4% |
| Median (all sectors) | 5.1% | 4.6% | 0.3% | 0.9% |
| Median, ex. Energy & Materials | 5.1% | 5.1% | 0.4% | 0.9% |

Exhibit 9. Earnings Pre-Announcements

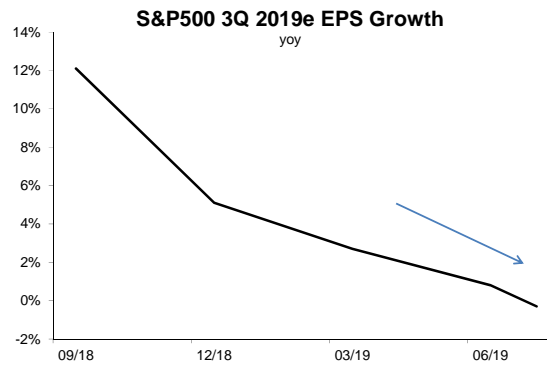
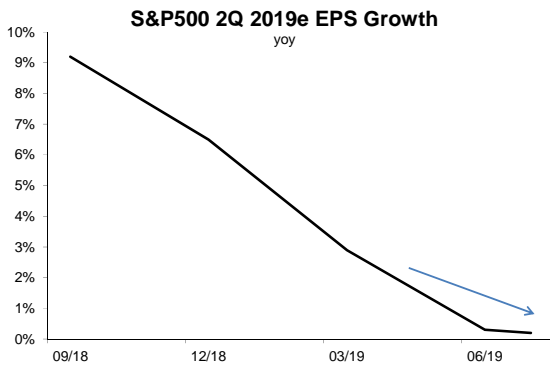
| Type | 2Q2019 | | 2Q2018 | | 1Q2019 | |
|-----------|---------|---------|---------|---------|---------|---------|
| | Total # | Total % | Total # | Total % | Total # | Total % |
| Positive | 23 | 18.7% | 51 | 37.5% | 32 | 25.4% |
| In-Line | 13 | 10.6% | 16 | 11.8% | 9 | 7.1% |
| Negative | 87 | 70.7% | 69 | 50.7% | 85 | 67.5% |
| Total | 123 | | 136 | | 126 | |
| N/P Ratio | 3.8 | | 1.4 | | 2.7 | |

Source: I/B/E/S data from Refinitiv

Exhibit 15. Blended (Reported & Estimated) Quarterly Earnings Growth for 2019Q2

| Sector | Today | 1 Jul | 1 Apr | 1 Jan | 1 Oct | 1 Jul |
|------------------------|-------------|-------------|-------------|-------------|-------------|--------------|
| Consumer Discretionary | -0.2% | 0.0% | 5.3% | 8.3% | 10.5% | 15.4% |
| Consumer Staples | 0.4% | -1.3% | 1.0% | 3.5% | 4.4% | 7.8% |
| Energy | -12.3% | -1.5% | -8.9% | 9.8% | 35.3% | 16.2% |
| Financials | 8.9% | 5.6% | 7.0% | 8.1% | 8.7% | 12.2% |
| Health Care | 5.6% | 3.0% | 3.0% | 4.7% | 3.7% | 8.4% |
| Industrials | -10.4% | -0.2% | 7.6% | 10.3% | 11.4% | 12.9% |
| Materials | -32.8% | -29.6% | -5.5% | -0.6% | 2.3% | 5.7% |
| Real Estate | 1.5% | 1.0% | 2.7% | 4.2% | 5.8% | 6.5% |
| Technology | -5.2% | -7.9% | -5.8% | 0.5% | 5.0% | 7.8% |
| Communication Services | 17.8% | 16.4% | 17.6% | 18.9% | 20.8% | 13.3% |
| Utilities | -0.9% | 2.2% | 1.9% | 2.7% | 0.8% | 4.9% |
| S&P 500 | 0.2% | 0.3% | 2.8% | 6.5% | 9.2% | 10.6% |

Source: I/B/E/S data from Refinitiv

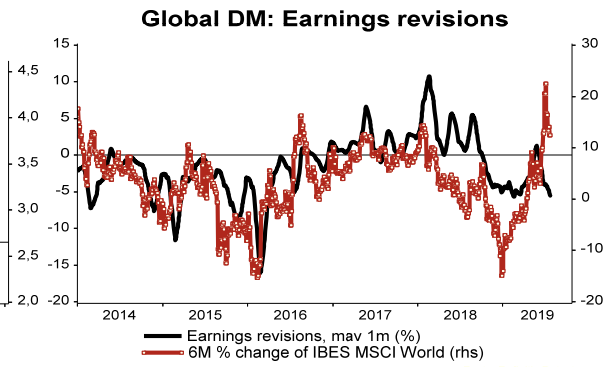
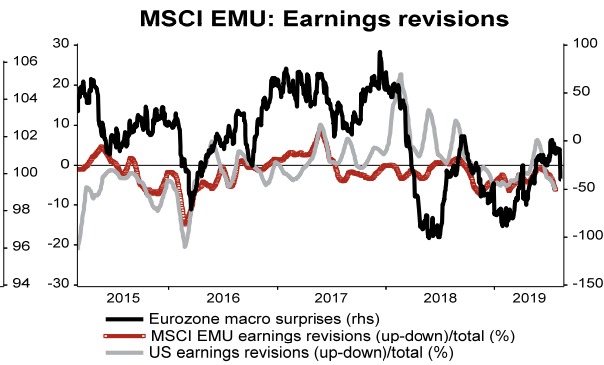
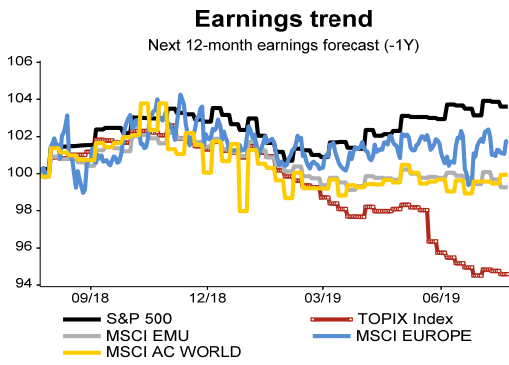


| 27/05/19 - 25/07/19 | | | | | |
|----------------------------------------|-----------------------------------|--------------------|-------------|-------------|-------------|
| Consensus eps estimates: (IBES) | changes (%) since 27/05/19 | | | | |
| | 2018 | 12m fwd eps | 2019 | 2020 | 2021 |
| MSCI AC WORLD | -0.2% | 0.4% | -1.1% | -1.4% | -1.1% |
| MSCI WORLD | -0.1% | 0.3% | -1.1% | -1.4% | -1.3% |
| S&P 500 COMPOSITE | 0.1% | 0.6% | -0.7% | -1.3% | -1.0% |
| FTSE-100 INDEX | 1.1% | 2.4% | 1.0% | 1.0% | 0.3% |
| TOPIX FJ Index | -0.1% | -1.8% | -2.7% | -3.0% | -2.6% |
| SWISS MARKET INDEX | -0.9% | 0.1% | -1.6% | -1.2% | -1.0% |
| MSCI EUROPE | -0.4% | 0.3% | -1.4% | -1.1% | -1.2% |
| MSCI EMU | -0.8% | -0.6% | -2.4% | -1.9% | -1.8% |
| STOXX 50 (EURO) | -0.5% | -0.1% | -1.8% | -1.3% | -1.3% |
| EURO STOXX 50 E | -0.5% | 0.1% | -1.9% | -1.2% | -1.1% |
| MSCI USA IT | -1.3% | -1.0% | -1.4% | -2.9% | -1.9% |
| MSCI EM | -2.0% | 0.0% | -2.1% | -2.2% | -1.8% |

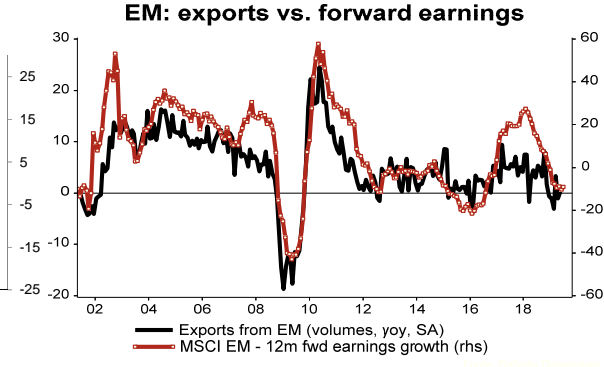
27/05/19 = our last update on the earnings season

Earnings growth estimates for 2020 and 2021 remain sanguine and are still at risk, should trade frictions continue keeping manufacturing and export-oriented sector in doldrums:

| World Markets: Forecast Earnings Growth (IBES Consensus) | | | | |
|-----------------------------------------------------------------|----------------------|------------------|------------------|------------------|
| 25-Jul-2019 | | | | |
| | A12FE vs 2018 | 2019/2018 | 2020/2019 | 2021/2020 |
| MSCI AC WORLD | 9.3% | 3.0% | 10.4% | 9.3% |
| MSCI WORLD | 8.8% | 2.8% | 9.8% | 8.8% |
| S&P 500 COMPOSITE | 9.1% | 2.6% | 10.4% | 9.9% |
| FTSE-100 INDEX | 6.2% | 1.5% | 7.8% | 5.3% |
| TOPIX FJ Index | 8.4% | 5.9% | 6.4% | 7.0% |
| SWISS MARKET INDEX | 11.8% | 5.9% | 9.6% | 7.9% |
| MSCI EUROPE | 9.0% | 3.1% | 9.6% | 7.2% |
| MSCI EMU | 9.3% | 2.8% | 10.5% | 8.1% |
| STOXX 50 (EURO) | 7.5% | 1.9% | 9.3% | 7.4% |
| EURO STOXX 50 E | 10.6% | 4.1% | 10.6% | 7.9% |
| MSCI USA IT | 7.3% | 0.8% | 9.2% | 13.5% |
| MSCI EM | 12.4% | 4.4% | 14.0% | 12.0% |



On the contrary, should trade frictions mitigate in the next months, the early and still fragile stabilization that we see in global export survey could eventually improve, helping to stabilize also analysts' earnings forecasts.



EU results are decent, too, but only when energy and materials are excluded.

Stoxx 600

188 reported 177 reported

| Sector | earnings growth, yoy | | sales growth, yoy | |
|--------------------------------|----------------------|--------------|-------------------|-------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 |
| Energy | -13.3% | -18.7% | 3.9% | 0.1% |
| Materials | -12.1% | -40.2% | 7.5% | -6.9% |
| Industrials | 19.5% | 9.6% | 7.6% | 3.6% |
| Consumer Discretionary | -5.7% | -12.0% | 4.5% | 7.6% |
| Consumer Staples | 6.9% | 15.5% | 1.0% | -4.6% |
| Health Care | 16.7% | 9.3% | 7.0% | 3.8% |
| Financials | 59.7% | 2.2% | -0.4% | 5.6% |
| Information Technology | 15.1% | -0.8% | 8.9% | 7.9% |
| Communication Services | 24.9% | -26.2% | 2.8% | 1.3% |
| Utilities | -4.2% | 63.7% | -13.1% | -0.4% |
| Real Estate | -5.4% | 51.4% | 6.5% | 6.8% |
| Stoxx 600 | 16.5% | -3.4% | 3.0% | 2.2% |
| Median (all sectors) | 6.9% | 2.2% | 4.5% | 3.6% |
| Median, ex. Energy & Materials | 15.1% | 9.3% | 4.5% | 3.8% |
| Median, ex. Fin. | 1.4% | 4.2% | 5.5% | 2.4% |

Stoxx 600

| Sector | earnings surprise | | sales surprise | |
|--------------------------------|-------------------|-------------|----------------|--------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 |
| Energy | -6.1% | 0.3% | 9.1% | 8.4% |
| Materials | -17.5% | -1.9% | 1.1% | -2.3% |
| Industrials | 7.3% | 2.1% | 2.6% | -0.4% |
| Consumer Discretionary | 8.4% | 10.2% | 1.5% | -3.6% |
| Consumer Staples | -1.8% | 7.4% | 0.3% | -3.6% |
| Health Care | 9.4% | 16.0% | -0.3% | 2.5% |
| Financials | 10.0% | 6.1% | 0.7% | 1.8% |
| Information Technology | 14.0% | 3.2% | -3.7% | 2.7% |
| Communication Services | 5.7% | -21.7% | 1.4% | 0.7% |
| Utilities | -2.1% | 10.1% | 0.2% | -9.9% |
| Real Estate | -34.7% | 15.8% | 21.7% | 2.4% |
| Stoxx 600 | 4.6% | 5.4% | 1.8% | -0.6% |
| Median (all sectors) | 5.7% | 6.1% | 1.1% | 0.7% |
| Median, ex. Energy & Materials | 7.3% | 7.4% | 0.7% | 0.7% |
| Median, ex. Fin. | 2.0% | 5.3% | 1.2% | 0.2% |

In sum, while the picture for Q2 is relatively decent, nonetheless a prolonged stall in trade frictions, possibly coupled with potential spikes in Brexit risk, could maintain the manufacturing and export-oriented earnings momentum in negative territory for longer. That is why further negative revisions are not to be excluded.

Overall, current consensus earnings growth expectations are to be considered still at risk. That said, given the already low revisions of the weakest sectors, the low equity positioning and, most of all, the strong dovish stance of global central banks, we maintain a positive view on equities.

The reporting season for the **Indian market** is the most advanced, with 16 companies (35% of the market) having reported their results. The other EM countries are still not seasoned enough to be considered.

Earnings growth at the index level has **increased** from 0.4% in the previous quarter to 4.4% in the current one. This was **largely caused by Financials and Communication Services** (increasing between quarters

from 6.4% to 41.6% and from +10.9% to 90.3%, respectively). The sales growth has, however, slightly decreased but **remained at the solid level** of 13.2% (dropping from 14.3%). Among the sectors, Finance has shown the strongest results in terms of sales growth (+54%). Communication Services have shown the lowest sales growth (-31.5%). Of the 16 Nifty companies that have reposted earnings so far this season, 11 have either met or exceeded analyst expectations. It is **Industrials and Consumer Staples** that have **disappointed**. Overall, the reporting season has **beaten the analysts' expectations on the earnings side by around 1.6%** (as compares to the average of 1.2% over the last 9 available quarters). Sales expectations have been beaten as well (sales surprise of 5.7%) but they have stayed behind the average beat of 7.3% over the last 9 quarters. The analysis of the median stock shows that both **earnings and sales' growth has somewhat increased** (from 12.7% to 15.3% and from 11.5% to 13.6%, respectively).

INDIA 16 reported 16 reported

| Sector | earnings growth, yoy | | sales growth, yoy | |
|--------------------------------|----------------------|-------------|-------------------|--------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 |
| Energy | 9.8% | -0.1% | 21.1% | 21.9% |
| Materials | -36.4% | 17.5% | 4.3% | 16.9% |
| Industrials | - | -14.0% | - | 4.8% |
| Consumer Discretionary | 10.9% | 90.3% | 18.8% | -6.8% |
| Consumer Staples | 12.8% | 0.0% | 11.5% | 0.0% |
| Health Care | - | - | - | - |
| Financials | 6.4% | 41.6% | 17.9% | 54.0% |
| Information Technology | 18.0% | 9.6% | 17.5% | 11.0% |
| Communication Services | -2.6% | 47.1% | -4.4% | -31.5% |
| Utilities | - | - | - | - |
| Market | 0.4% | 4.4% | 14.3% | 13.2% |
| Median (all sectors) | 9.8% | 13.5% | 17.5% | 7.9% |
| Median, ex. Energy & Materials | 10.9% | 25.6% | 17.5% | 2.4% |

INDIA 16 reported 16 reported

| Sector | earnings surprise % | | sales surprise % | |
|--------------------------------|---------------------|-------------|------------------|-------------|
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 |
| Energy | 9.7% | 2.5% | -3.4% | 7.9% |
| Materials | 23.3% | 14.6% | -1.8% | 5.0% |
| Industrials | - | -23.6% | - | -5.4% |
| Consumer Discretionary | -14.6% | 65.4% | -6.7% | 6.6% |
| Consumer Staples | -4.3% | -2.1% | -0.2% | -0.3% |
| Health Care | - | - | - | - |
| Financials | -0.7% | 32.4% | 62.1% | 38.9% |
| Information Technology | 1.6% | 3.4% | 0.4% | -0.6% |
| Communication Services | 62.8% | 49.3% | -8.3% | -32.3% |
| Utilities | - | - | - | - |
| Market | 5.8% | 1.6% | -0.4% | 5.7% |
| Median (all sectors) | 1.6% | 9.0% | -1.8% | 2.4% |
| Median, ex. Energy & Materials | -0.7% | 17.9% | -0.2% | -0.4% |

Analysis of the median stock

| Index | Earnings | | Sales | | availability |
|-------|----------|---------|---------|---------|--------------|
| | Growth | | Growth | | |
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 | Q2 2019 |
| India | 12.67 % | 15.27 % | 11.52 % | 13.65 % | 34.8% |

| Index | Earnings | | Sales | | availability |
|-------|----------|---------|---------|---------|--------------|
| | Surpr | | Surpr | | |
| | Q1 2019 | Q2 2019 | Q1 2019 | Q2 2019 | Q2 2019 |
| India | (0.72)% | 3.93 % | 0.01 % | (0.05)% | 28.3% |

* For India, the financial year ends in March

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