N° 459
2 May
2018

BONHÔTE
BANQUIERS DEPUIS 1815

FLASH
BOURSIER

THE CHINA – US DEAL DOES NOT RESOLVE EVERYTHING

Highlights :

China has accepted to reduce its trade deficit with the US

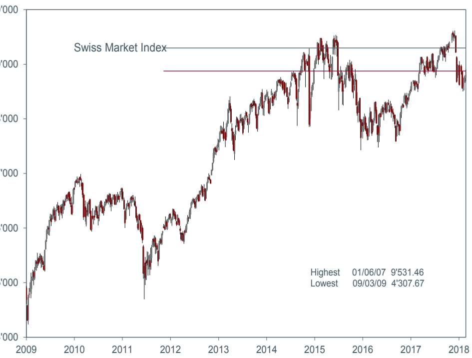
Some emerging markets starting to wobble

Overview

China's recent consent to work on substantially reducing its trade deficit with the US has defused a potentially explosive situation. But cutting this deficit by USD 200 billion annually, starting from 2020, will be no easy task. Some measures can be implemented in a short space of time, such as increasing Chinese imports of oil, gas, soybeans and other commodities. But it will be more difficult to find solutions in industry and manufacturing. Moreover, the extra buying of commodities will do little to reduce America's overall trade deficit, as what is sold to the Chinese will simply not be available to export elsewhere, as it is not physically possible for the US to double or triple oil or grain exports. Manufacturing is where the difference can be made. China's air traffic flows are going through the roof and it will have to buy a large number of aircraft in the years ahead to meet demand. Contracts can quickly amount to tens of billion dollars, and China could decide to give precedence to Boeing over European rival Airbus. The country also announced this morning that it was cutting customs duties on motor vehicle imports by 15-25% from 1 July. In a nutshell, reducing this structural deficit will take time, especially if the US consumer does not get out of the habit of buying cheap Chinese goods.

Trade has become a less contentious issue. In the meantime, however, cracks are starting to appear in some emerging markets, threatening their stability. In recent weeks, the Argentinian peso has shot down by over 15% against the US dollar, while the Turkish lira and Venezuelan bolivar have both lost more than 10% and the Brazilian real and the Mexican peso close to 5%. The instability originates from renewed political turmoil and higher dollar interest rates, which last week broke above 3% as far as the 10-year Treasury yield was concerned. This has led to capital flooding back into dollars, away from those zones deemed riskiest. We can also see investors pulling back to safer countries in Europe, where 10-year yields have increased by between 0.3% and 0.6% on peripheral debt (e.g. Italy, Greece and Spain) since the beginning of the month. In contrast, the same yields have been stable in Germany and France.

It is undoubtedly too early to draw conclusions about these recent moves. But they are worth pointing out because they reflect a slight malaise in the bond market that could contaminate equities if it continues.



The SMI continues making slow gains. Support remains at 8800 points while resistance is still at 9250 points.

Key data

	USD/CHF	EUR/CHF	SMI	EURO STOXX 50	DAX 30	CAC 40	FTSE 100	S&P 500	NASDAQ	NIKKEI	MSCI EMERGING MARKETS
Latest	1.00	1.17	8'940.46	3'573.76	13'077.72	5'614.51	7'778.79	2'712.97	7'354.34	22'930.36	1'137.75
Trend	→	↓	→	→	↑	↑	↑	↑	↑	↑	↓
%YTD	2.43%	0.32%	-4.70%	1.99%	1.24%	5.68%	1.18%	1.47%	6.53%	0.73%	-1.79%

(values from the Friday preceding publication)

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SPOTLIGHT ON STOCKS

Cosmo Pharmaceutical
(ISIN: NL0011832936, price: CHF 126.90)

The share of the company, which develops and produces treatments for gastro-intestinal conditions, has zigzagged in recent days after two announcements by the US FDA.

One of the compounds currently in the approval process, Methylene Blue MMX™, has been blocked by the FDA owing to shortcomings in the paperwork and other information. This compound represents a potential huge step forward in detecting and locating pre-cancerous lesions and polyps inside the colon. The FDA is shortly due to provide more details about what information is missing from the application. If the upshot is more research, the compound could be delayed by about three years. If the request is for more rudimentary information, the delay may be less than a year.

The share plunged by 25% on the news before pulling back by 13% a few days later, when the FDA gave the green light for one of Cosmo's antibiotics, Rifamycin.

Cosmo has a market capitalisation of CHF 1.9 billion and a workforce of 300. Plans suggest that it will not be profitable before 2020 but it still has cash of CHF 170 million. The sharp correction has priced in the uncertainty overhanging MMX and, consequently, represents an investment opportunity at a risk that is asymmetric (-25% + 50%), which will be determined by the outcome of the MMX case.

For those wanting thrills and spills, a speculative buy recommendation can be issued at around CHF 115.

Anheuser-Busch Inbev SA/NV
(ISIN: BE0974293251, price: EUR 80.20)

The group has the world's largest beer portfolio, containing more than 500 brands including Budweiser, Stella, Beck's, Corona, Hoegaarden and Leffe. Inbev bought Anheuser Bush for USD 52 billion in 2008 then SABMiller for USD 100 billion in 2016.

The group's latest quarterly results were broadly in line with expectations. The three leading brands (Budweiser, Stella and Corona) recorded sales growth of nearly 8%. Operating profit was up by 6.6%, rising almost to USD 5 billion.

The share, as with other beverage stocks, has underperformed the market recently and so is now trading on attractive multiples. We think the group could also gain from the upcoming Soccer World Cup in Russia, which will feature 64 matches between 14 June and 15 July. This competition has the biggest viewing figures of all sporting events, with some 3.5 billion expected to be watching this year.

AB InBev is again the official sponsor, and most teams from Latin America – its main market – have qualified. The World Cup could boost sales volumes by 2-3% in the second and third quarters, resulting in a 4% increase in operating profits.

Target: EUR 95.

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