Bocconi Students Investment Arena Newsletter: October 2023

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ABOUT US:

Bocconi Students Investment Arena was born in 2022 from the idea of bringing together students of different degrees and experience, but all with the same ardent passion for finance. Through dedicated competitions, masterclasses, and a members' forum, we aim to develop a community of students that fosters quantitative and qualitative skills like in-depth practical investments and valuation skills, teambuilding, and analytical skills.

The uniqueness of this association is that members would be able to put their investment knowledge into practice by competing against each other in two main events: portfolio competition and company valuation competition.

Analysts:

Jonas Ben Wenner, Aaditya Sharma, Filippo Mattei, Antonino Di Blasi

Editor:

Giovanni Bursi

Contact us

bsia.it/

as.investmentarena@unibocconi.it

Germany's Economic Woes: A Deepening Downturn

By Jonas Ben Wenner

Introduction: A Nation at a Crossroads

Germany, often hailed as the economic engine of Europe, now faces a pivotal moment. The recent months have witnessed a pronounced slowdown in its economic activity, raising alarm bells among policymakers and investors alike. As we dissect the numbers, we'll unravel the intricate web of challenges that Germany confronts and its potential ripple effects across the broader Eurozone.

The Numbers Speak: PMI and Contraction

This critical gauge of economic health provides an early glimpse into business sentiment. In August, Germany's preliminary Purchasing Managers' Index (PMI) plummeted to 44.7, marking its lowest reading since May 2020. But what does this number signify? It reflects a contraction in both manufacturing and services sectors. When the PMI dips below 50, it signals economic distress—factories slowing down, services retreating. The manufacturing sector has endured a protracted decline for four consecutive months, while services—usually more resilient—also contracted for the first time in eight months.

Behind these numbers lies a more profound story. German factories, renowned for precision engineering and automotive prowess, have hit a rough patch. Supply chain disruptions—those that plagued global industries during the pandemic—have taken their toll. Semiconductors, essential for modern cars and electronics, remain scarce. As a result, production lines stuttered, assembly plants idled, and inventories dwindled.

Recession Risks Looming: A Familiar Precipice

Germany narrowly skirted a winter recession in Q2 2023—a sigh of relief for Europe's largest economy. But the recent data paints a less sanguine picture. The threat of recession looms once again. Why? Because recessions aren't merely statistical events; they impact lives—jobs lost, businesses shuttered, dreams deferred. And Germany isn't an isolated island; it's part of a larger scale—the Eurozone.

Eurozone PMI Decline: A Symphony of Synchronized Woes

The broader Eurozone—a union of 19 countries sharing the euro currency—faces similar headwinds. Its preliminary PMI slid to 47, the lowest since November 2020. Here's where it gets interesting: Germany's services sector shoulders much of the blame for this downturn. Cyrus de la Rubia, Chief Economist at Hamburg Commercial Bank, points to "downward pressure" lead by German services. Inflation within these services has surged due to rising wages—an unintended consequence of post-pandemic labor dynamics.

Inflationary Pressures and Stagflation: A Delicate Balancing Act

Inflation—the bogeyman haunting central bankers worldwide—has knocked on Germany's door too. But it's not just inflation; it's "stagflation." Picture prices rising while growth stumbles—a toxic brew for policymakers. As factories grapple with higher input costs (think raw materials and energy), they pass them on to consumers. Meanwhile, sluggish growth dampens demand.

The European Central Bank (ECB) faces an unenviable task: how to tame inflation without stifling recovery? A task that requires finesse and nerves of steel.

Germany's Role: The Continent's Economic Barometer

Why does all this matter beyond Berlin? Because Germany isn't just another country; it, for decades, has been Europe's compass needle—an indicator pointing north or south for the entire region. When German factories hum with productivity, neighboring countries benefit from supply chains humming in harmony. Conversely, when those factories falter, ripples spread across Brussels, Paris, Rome—the whole European map.

The German economy, often hailed as the locomotive of Europe, is facing a crossroads. Recent months have witnessed a pronounced slowdown in its economic activity, raising concerns among policymakers and investors. In this article, we will delve into the intricate challenges that Germany is currently facing and explore the potential ripple effects across the broader Eurozone.

Purchasing Managers' Index (PMI), a critical indicator of economic health, has dropped to 44.7 in Germany in August, the lowest reading since May 2020. This decline reflects a contraction in both the manufacturing and services sectors, indicating economic distress. Manufacturing, known for its precision engineering and automotive prowess, has experienced a continuous decline for four months, primarily due to supply chain disruptions. Semiconductors, crucial for modern cars and electronics, have been in short supply, causing production lines to stutter, assembly plants to idle, and inventories to dwindle.

While Germany narrowly avoided a winter recession in Q2 2023, the recent data paints a less optimistic picture. The possibility of a recession looms, bringing with it the grim reality of job losses, business closures, and dashed dreams. The implications are not limited to Germany alone, as it is an integral part of the Eurozone, a union of 19 countries sharing the euro currency.

The Eurozone, as a whole, is grappling with similar economic challenges. Its preliminary PMI has fallen to 47, the lowest since November 2020. Germany's services sector, in particular, has played a significant role in this downturn. Rising wages within the sector have led to increased inflation, an unintended consequence of post-pandemic labor dynamics. Inflation has become a formidable challenge for the European Central Bank (ECB), as it is not the typical inflation seen elsewhere. It is "stagflation," where prices rise while economic growth falters. This situation creates a delicate balancing act for policymakers, as higher input costs, such as raw materials and energy, are passed on to consumers, while sluggish growth dampens demand.

The ECB faces a challenging task of taming inflation without stifling the ongoing economic recovery. This requires careful and precise decision-making in a volatile economic environment.

As policymakers navigate these turbulent waters, they must strike a balance between economic growth and inflation containment. The decisions made by the ECB regarding interest rates will have far-reaching consequences. The importance of collaboration among European countries cannot be overstated. The fate of individual countries is intertwined with that of their neighbours, and the success of the European project hinges on how well these challenges are addressed collectively.

An Overview and Analysis of ESG Trends and the Sustainable Finance Index

By Aaditya Sharma

In recent years, Environmental, Social, and Governance (ESG) factors have taken centre stage in the financial world, with investors, regulators, and the media scrutinising how companies are performing against their ESG strategies and targets. ESG considerations have become more than just a buzzword; they are now integral to investment and business decisions. In this article, we will delve into the evolving landscape of ESG trends and the valuable insights provided by the Sustainable Finance Index (SFI) based on data prior to Covid-19, in order to elucidate how trends were evolving in a pre-pandemic economy.

ESG in the Financial World & The Role of SFI

ESG criteria encompass a range of factors that evaluate a company's ethical and sustainable practices. They cover environmental factors, such as carbon emissions and climate change risk, social factors like human rights and equality policies, and governance factors like board diversity and compensation arrangements. The relevance of ESG has grown significantly in recent years, influencing investment decisions and even regulatory changes. The Sustainable Finance Index provided by EY offers a unique perspective on the performance of financial services firms concerning ESG criteria. It uses data from more than 1,100 financial institutions and assesses over 200 ESG parameters to create two key metrics: the ESG score and the disclosure rate. These metrics provide a quantitative assessment of ESG performance and transparency in the financial sector.

The 2021 SFI reveals some positive trends in the financial sector's approach to ESG:

1. *Improvements in Disclosures and Performance:* The average disclosure rate increased from 79% in 2020 to 82% in 2021. This indicates that more financial institutions are reporting their ESG data, enhancing transparency.
2. *Enhanced ESG Scores:* The average ESG score also improved, rising from 4.80 to 4.93, showing an upward trend in ESG performance across the industry.
3. *Regional Variation:* European institutions lead the way in ESG, with the highest ESG scores and the best environmental disclosure rates. This is partially due to Europe's robust regulatory environment, which promotes transparency.
4. *Progress in Social Parameters:* Disclosure rates for social parameters, including data protection, workplace safety, and equality policies, have improved, highlighting a commitment to broader social responsibility.

Despite these trends, however, there are naturally some accompanying areas for improvement and potentially purposeful consequences:

1. *Slow Progress on Emissions:* Financial institutions have been slow to make headway in reducing emissions. Disclosing financed emissions and reducing emissions from 2018 to

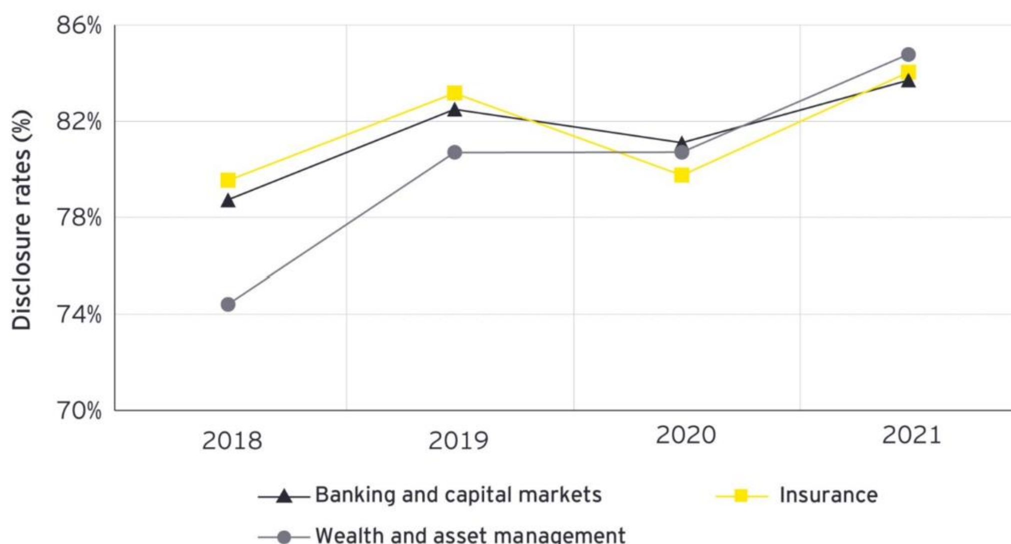
2021 remain problematic. The report highlights a need for greater effort in this area, considering that reducing emissions is critical to addressing climate change.

2. *Product Offerings and Green Strategies:* While some progress has been made, less than half of all financial institutions report offering green products or solutions. Banks, in particular, lag behind in this area. Aligning product offerings with green strategies is essential for sustainable finance.
3. *Greenwashing and Transparency:* The risk of greenwashing, or providing a misleading perception of ESG efforts, threatens the credibility of ESG initiatives. Greater transparency is essential to address this concern and ensure that ESG commitments are genuine.
4. *Limited Disclosures on Environmental Risk:* While there have been improvements, there is still a lack of disclosure regarding environmental risks embedded in value chains, business models, and operations. Enhancing these disclosures is critical for understanding the environmental impact of financial institutions.

The Impact of ESG Trends on the Financial Services Sector

The evolving landscape of ESG trends has had a profound impact on the financial services sector. As we can see in figure one, Although Wealth and AM Firms had the greatest relative improvement and thus take a slight lead in reporting their sustainability figures, the financial services sector as a whole only has a disclosure range of 83.5% to 85%. Investors, analysts, regulators, and the media are thus now closely monitoring companies' ESG performance, with financial institutions being under increased pressure to meet ESG targets and provide transparent disclosures to meet the demands of various stakeholders. Companies with robust ESG propositions have thus gained a competitive edge in the financial sector, with SFI trends showing European institutions, hedging a lead through a strong focus on sustainability targets. This has not necessarily come about voluntarily, however. Regulatory bodies have played a pivotal role in shaping the ESG landscape, with mandatory disclosure rules in Europe leading to more comprehensive reporting. Emerging ESG regulations in the US and Asia are also stimulating demand and influencing company behaviour.

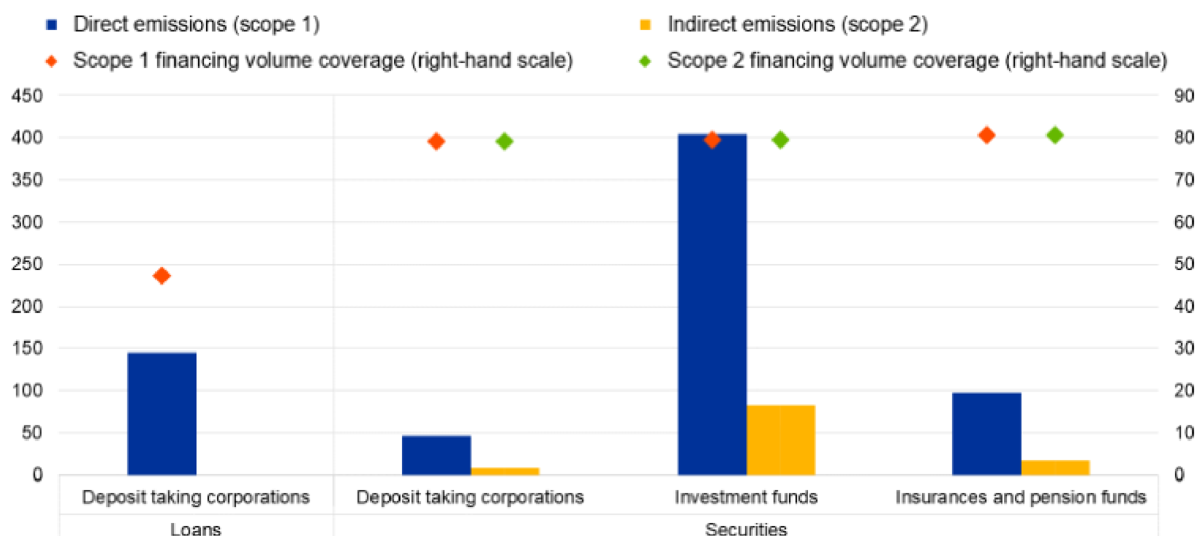
Figure 1: Disclosure Performances of FS by Sector



Source: EY

ESG trends and regulations vary across regions. Europe leads in ESG performance, driven by its stringent regulatory environment. North American institutions are gradually catching up. However, global consistency remains a challenge. As these financial institutions navigate the landscape, several critical areas for ESG strategy come to the forefront:

Figure 2: Financing of Direct and Indirect Emissions by Financial Institutions



Source: ECB

Addressing emissions intensity is a top priority. Financial institutions must increase climate-aligned investments and reduce investments in emissions-intensive projects. Figure two shows us a comprehensive overview of the results FI's have upon the environment, both directly and indirectly. The left-hand scale shows us emissions in millions of tons of CO2 in the EU, whereas the right-hand scale shows us the total financing volume by percentage. Investment funds and securities by far fund the most direct and indirect global emissions with 400mn tons at 80% and 80mn tons at 18% respectively, mirroring accurately their portfolio size in financial markets. The responsible institutions should thus align their product offerings with greener strategies to cater to the growing demand for sustainable investment options. In order to retain this demand, however, greater transparency is essential to mitigate the risk of greenwashing and to build trust among stakeholders.

Financial institutions need to improve disclosures on environmental and social parameters, including risks embedded in their operations and value chains. Collaborative efforts, both private and regulatory, are crucial to enhance the availability, quality, and accessibility of ESG data. Regulatory changes, like the Non-Financial Reporting Directive (NFRD) and Sustainable Finance Disclosure Regulation (SFDR), are expected to further improve data quality.

Conclusion

The financial services sector is at a critical juncture. ESG considerations are no longer just a choice but a fundamental aspect of doing business in the modern world. As investors, analysts, regulators, and the public continue to place greater emphasis on ESG performance, financial institutions must respond by bolstering their commitments to sustainability and transparency.

The trends highlighted in the SFI demonstrate that companies that take ESG seriously are not only contributing to a better future but are also enhancing their competitive advantage in the market. There are leaders and laggards in the journey towards a more sustainable financial industry, and the gap between these two groups signifies the vast potential for improvement and the need for best practices to be shared and adopted industry-wide.

In conclusion, the ESG landscape is not just a trend but a paradigm shift in finance. Financial institutions have made significant progress, but the journey towards a more sustainable and responsible industry is far from over. It is an imperative step towards addressing global challenges, from climate change to social inequalities.

The economic consequences of the conflict

By Filippo Mattei

The context of the conflict in Israel

The Hamas attack has shaken the already precarious balance in the Middle East Region, leading to another conflict between Palestine and Israel. On Saturday, October 7th, Hamas's armed forces entered the borders of Israel, killing hundreds of young people who were attending a rave party and taking over hundred people hostage, including civilians and military personnel. In response, Israel immediately surrounded the Gaza Strip, threatening to invade the territory. The conflict has been ongoing for three weeks now, resulting in thousands of deaths and significant tensions in international geopolitical relations.

In the rest of the article, we will analyze the economic impact that the war is having on international markets and its potential future consequences.

Financial stability

In the week following the attack, most stock markets closed with positive gains: Milan gained +1.53% in the five trading sessions of the week, London +1.40%, Wall Street +0.90%, and the Nasdaq +0.61%; Asian indices performed even better, with Tokyo gaining +4.26% since the previous Friday, Hong Kong rising by +1.87%, and the MSCI Asia index increasing by +3.02%. Among major financial markets, only Paris (-0.82%) and Frankfurt (-0.3%) experienced a decline during the first week of the conflict.

Initially, the markets behaved unusually. Historically, after the onset of a new conflict, stock markets tend to decline due to growing uncertainty, followed by a subsequent recovery. However, this time was different. Stocks fell only on Monday morning, and by the afternoon, the major stock markets had almost recovered all of their losses, despite closing in the negative.

The reasons for this current stability in equities and the limited market impact at the moment are manifold. Firstly, as reported in a report by the S&P Global Ratings, investors believe that the war may remain confined to Israel and Palestine without involving other local states and international powers. Additionally, the risk of a new European energy crisis seems to be averted as European Union gas reserves are full.

Safe haven assets

Despite the market remaining relatively stable, the VIX index, which measures volatility on Wall Street, has increased by approximately 4% in the last month, albeit remaining around the level of 21 (hence, not a dramatic change). The so-called "fear index" has entered the alert range. The increase in this index is due to the dynamics that affect the market in typical situations of uncertainty. Investors tend to protect their portfolios by investing in so-called safe haven assets.

Firstly, there has been a rise in the price of gold, which has increased from a rate of 55.5 Euros per gram before the Hamas attack to a value exceeding 61 Euros per gram on October 28th (as it is shown in the graph). Along with the price of gold, the price of oil has also risen, touching $93 per barrel after the beginning of the conflict. Similarly, there has been an increase in the value of the U.S. dollar.

Figure 1: Gold Price (€) trend in October 2023

Source: YCharts

Risk of possible escalation

As mentioned earlier, investors believe that the conflict is likely to remain confined between Israel and Palestine, but in recent days the risk of possible Iranian intervention has become increasingly likely. In fact, Iran is Hamas' biggest ally, and recently the leader of Hamas political bureau Ismail Haniyeh and the Iranian Foreign Minister Hossein Amirabdollahian met to discuss means to stop Israeli "brutal crimes" in Gaza, as disclosed in an official note by the Hamas' leader. Moreover, Amirabdollahian added, "the region is like a powder keg. I would like to warn the U.S. and the Israeli puppet regime that if they do not immediately put an end to the crimes against humanity and genocide in Gaza, anything will be possible at any time and the region will spiral out of control." The widening of the conflict is also made increasingly risky by the fact that on the northern front the Israeli army is up against Shiite Hezbollah, Tehran's iron allies.

The risk of the conflict widening would have dramatic consequences for the entire world economy. Indeed, the major producers of black gold in the Middle East might decide to act as they did during the 1973 Yom Kippur War, precisely between Israel and some Arab countries (Egypt and Syria). At that juncture, the Arab countries in OPEC (the organization of oil-exporting countries) "artificially" raised the price of crude oil and cut off supplies to pro-Israel countries. If Iran, the world's seventh-largest producer with 3.3 million barrels per day, were to implement the same measure, the price could soar, possibly triggering a global recession.

Inflation: how markets are still affected

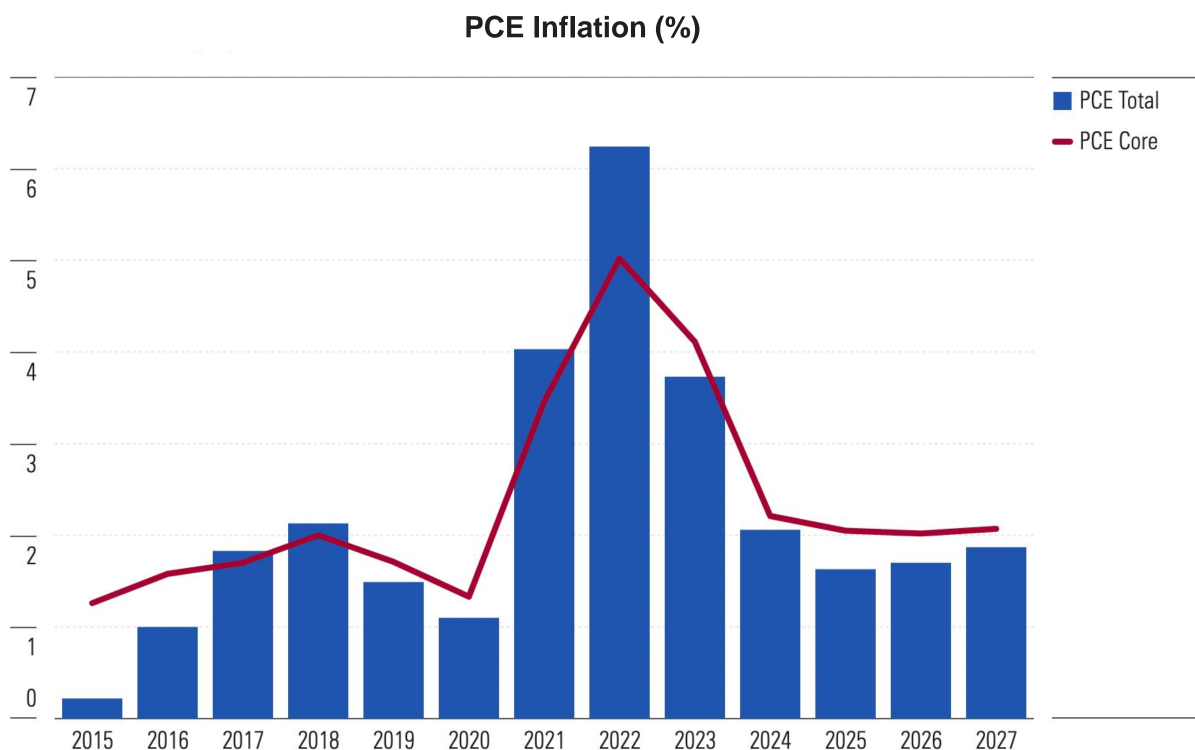
By Antonino Di Blasi

Inflation dynamics

Inflation is the rate of increase in prices for goods and services over time. It is typically measured as a percentage change in a price index, such as the Consumer Price Index (CPI). Inflation can be caused by several factors, including demand-pull inflation and cost-push inflation. Demand-pull inflation occurs when there is too much money chasing too few goods and services. This can happen when the economy is growing rapidly, and consumers and businesses are spending more money. Cost-push inflation occurs when the cost of producing goods and services increases, such as when wages or energy prices rise.

Central banks typically target a low, but positive rate of inflation. This is because they believe that some inflation is necessary to keep the economy growing and healthy. However, too much inflation can be harmful, as it can lead to uncertainty and instability. Inflation matters because it can affect everyone in the economy. For consumers, inflation can mean that their money buys less over time. For businesses, inflation can make it more expensive to produce goods and services. For investors, inflation can erode the value of their investments over time. For policymakers, inflation is a key concern because it can have a significant impact on the overall economy.

PCE Inflation (%)



Source: Bureau of Economic Analysis

In 2022, inflation surged to its highest point in over four decades, largely due to the collision of robust consumer demand with significant supply limitations, resulting in a sharp increase in prices, particularly in the food, energy, and durable goods sectors. However, this trend is

expected to reverse as the Federal Reserve's interest-rate hikes cool down demand and supply constraints gradually dissipate. Consequently, a substantial deflationary impact is anticipated, leading to a projected decrease in inflation from 6.2% in 2022 to 3.7% in 2023, with further stabilization at an average of 1.8% from 2024 to 2027, falling below the Federal Reserve's targeted 2.0% rate.

Markets and interest rates

Increasing interest rates is a commonly employed monetary policy tool to slow down inflation. When inflation is on the rise, increasing interest rates can discourage borrowing and spending, which, in turn, helps to temper the overall demand in the economy. By making borrowing more expensive, individuals and businesses are less inclined to take out loans, leading to reduced spending and investment. This decrease in spending can help alleviate the upward pressure on prices, thereby contributing to the stabilization of inflation rates.

The impact of rising interest rates on stock prices in the market is largely attributed to the inverse relationship between interest rates and the present value of future cash flows. As interest rates increase, the cost of borrowing for companies rises, leading to higher expenses and potentially lower profits. This expectation of reduced profitability can prompt investors to reassess the attractiveness of equities compared to other investment options, causing a potential shift in investment patterns. Consequently, the anticipation of higher borrowing costs and reduced corporate earnings can trigger a decline in stock prices, reflecting the altered market sentiment and risk perceptions.

Despite the Federal Reserve leaving the door open for a potential rate hike in 2023, Fed Chair Jerome Powell's recent statements emphasize the likelihood of sustained elevated rates in the near future. With inflation standing at 3.7% for the 12-month period ending in August, the Fed remains steadfast in its commitment to achieving its long-term inflation target of 2%. This dedication to price stability, though potentially challenging for certain sectors of the economy, reflects the Fed's unwavering determination.

While the evolving interest rate landscape poses challenges for stocks, the potential for market resilience persists. Analysts like Freedman note that the performance of companies remains a critical variable in this environment. As inflation rates decline, there is optimism that stock valuations may appear more reasonable, potentially paving the way for improved market conditions.

Despite this, short-term stock market volatility remains a possibility. For stocks to witness an upward trajectory, investor confidence must be supported by the belief that earnings will outpace current projections and offer more enticing growth prospects compared to the presently elevated yields on fixed income instruments. These combined factors will play a pivotal role in shaping the market's future trajectory, particularly in the context of evolving interest rates and inflation dynamics.

Considerations

It's best to wait before investing your money in the stock market, especially with the current wars and contingencies. Hold cash or bonds in the short term to protect your money from inflation. Once the markets have stabilized in the first half of 2024, that will be a good time to start investing regularly. Keep in mind that the stock market has grown unexpectedly since the beginning of the year, so it's normal to expect a period of profit-taking, which could last until the end of the year.