World Markets Review — October 2016
Global stocks declined modestly as signs of improvement in the U.S. economy raised investor concerns about higher interest rates. Health care stocks fell sharply amid ongoing drug pricing pressures and disappointing earnings reports, while financials rallied on the outlook for rising rates. High-grade bonds lost ground and the U.S. dollar advanced against the euro, the yen and most other currencies.

Index Returns

<table>
<thead>
<tr>
<th></th>
<th>October 2016</th>
<th></th>
<th>YTD 2016</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>U.S. dollar %</td>
<td>Local currency %</td>
<td>U.S. dollar %</td>
<td>Local currency %</td>
</tr>
<tr>
<td>MSCI World</td>
<td>−1.9</td>
<td>−0.7</td>
<td>3.5</td>
<td>3.3</td>
</tr>
<tr>
<td>MSCI EAFE</td>
<td>−2.0</td>
<td>1.2</td>
<td>−0.4</td>
<td>−0.4</td>
</tr>
<tr>
<td>MSCI EM IMI</td>
<td>0.0</td>
<td>0.4</td>
<td>15.0</td>
<td>10.9</td>
</tr>
<tr>
<td>MSCI Europe</td>
<td>−3.3</td>
<td>0.3</td>
<td>−3.3</td>
<td>2.0</td>
</tr>
<tr>
<td>MSCI Pacific ex Japan</td>
<td>−2.1</td>
<td>−1.6</td>
<td>8.5</td>
<td>5.4</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>−1.8</td>
<td>−1.8</td>
<td>5.9</td>
<td>5.9</td>
</tr>
<tr>
<td>MSCI Japan</td>
<td>1.3</td>
<td>5.1</td>
<td>3.9</td>
<td>−9.2</td>
</tr>
<tr>
<td>MSCI UK</td>
<td>−5.2</td>
<td>0.9</td>
<td>−4.4</td>
<td>15.4</td>
</tr>
<tr>
<td>Bloomberg Barclays Global Aggregate</td>
<td>−2.8</td>
<td>—</td>
<td>6.8</td>
<td>—</td>
</tr>
<tr>
<td>Bloomberg Barclays U.S. Aggregate</td>
<td>−0.8</td>
<td>−0.8</td>
<td>5.0</td>
<td>5.0</td>
</tr>
<tr>
<td>J.P. Morgan EMBI Global</td>
<td>−1.5</td>
<td>−1.5</td>
<td>13.4</td>
<td>13.4</td>
</tr>
<tr>
<td>J.P. Morgan GBI–EM Global Diversified</td>
<td>−0.8</td>
<td>−0.3</td>
<td>16.1</td>
<td>10.6</td>
</tr>
</tbody>
</table>

MSCI index returns reflect not dividends. Source: RIMES

North America
U.S. stocks weakened amid interest rate worries and disappointing earnings reports from several companies. The Standard & Poor's 500 Composite Index slipped 2%, while the Dow Jones Industrial Average declined 1%. The tech-heavy Nasdaq composite index decreased 2%. Of the more than 300 S&P companies that reported quarterly earnings in October, 73% beat consensus estimates on earnings, while 55% surpassed analysts' revenue expectations.

Health care stocks fell 7%. Fears that a new presidential administration might seek to curb drug price increases hurt pharmaceutical stocks. Shares of Johnson & Johnson and biopharmaceutical titan Amgen declined as signs emerged that the companies are losing pricing power for their key arthritis treatments. Merck shares retreated on concerns over diminishing margins for diabetes treatments.

Higher yielding rate-sensitive sectors slumped as interest rates rose and speculation grew that the Federal Reserve will raise the federal funds rate in December. Telecommunications stocks dropped 6% and companies in the newly formed real estate sector declined 5%. Consumer staples shares also fell.

Subpar earnings reports and lower industrial and precious metals prices sent industrials and materials shares lower. Honeywell fell 5% after reporting weaker-than-anticipated profit due to lower revenue from its aerospace segment. Shares of freight railroad operator Union Pacific dropped as the company reported a 13% decline in profit on poorer industrial product and coal volumes. Similarly, aluminum manufacturer Alcoa plunged on lower-than-expected third-quarter profit.

Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.
Information technology stocks were mixed as investors weighed modestly improved earnings and solid consumer demand versus an uncertain longer term outlook for some companies. Microsoft shares rose to a new all-time high as the company raised its dividend and growth in cloud services propelled earnings above expectations. In contrast, Intel shares dropped after the company issued revenue forecasts that were lower than anticipated. Elsewhere, higher trading volumes and the prospect of rising interest rates drove financial stocks upward. Bank of America, Goldman Sachs and Citigroup rose as a flurry of post-Brexit activity in financial markets led to more robust trading revenue.

Two blockbuster deals highlighted an otherwise normal month for mergers and acquisitions. Telecom behemoth AT&T agreed to purchase cable television content provider Time Warner for approximately $85 billion. The proposed acquisition aims to expand AT&T’s content offerings to its wireless and television subscribers. In the consumer staples sector, British American Tobacco offered $47 billion in cash and stock to acquire the remaining stake in Reynolds American it doesn’t already own. If the deal is accepted, it will create the world’s largest publicly traded tobacco company. Reynolds American shares rose.

U.S. economic data was mostly encouraging. Third-quarter gross domestic product registered a 2.9% annualized gain, the fastest rate of growth in two years. September employment data pointed to a healthy labor market with low unemployment and rising wages. Housing data was generally positive as home sales and building permits posted gains in September. Capital expenditures fell modestly, but industrial production increased slightly.

In bond markets, the Bloomberg Barclays U.S. Aggregate Index lost 0.8%. The yield on the benchmark 10-year Treasury note rose 24 basis points to 1.84%. Higher yields across the Treasury curve hurt bond prices in most sectors. Investment-grade corporates declined by 0.8%, while high-yield corporates rose 0.4%. Investment-grade corporate spreads to Treasuries tightened 6 basis points to end the month at 132 basis points.

Inflation expectations have crept higher over the past few months. Yet Treasury Inflation-Protected Securities prices ended October 0.4% lower, due largely to the impact of higher government bond yields. Municipal bonds lost 1.0% in a month of record-setting issuance; the increased supply in combination with rising Treasury yields put downward pressure on muni bond prices.

Europe
European stocks moved sideways, gaining 0.3% overall as signs of improving economic growth were offset by heightened concerns about the U.K.’s departure from the European Union. Investor worries that the Brexit process might ultimately leave Great Britain without access to the EU’s single market led to growing calls for a second referendum. The euro declined 2% against the U.S. dollar.

The euro-zone economy grew modestly in the third quarter, despite concerns that Brexit might take an immediate toll on consumer and business confidence. Economic output in the 19-member euro zone rose at an annualized rate of 1.4% in the July-to-September period – the first full reading since the June 23 Brexit vote. At its October meeting, the European Central Bank held interest rates steady and declined to say whether it would extend its €80 billion-a-month bond-buying program, likely delaying that decision until December.

Economically sensitive stocks generally outpaced defensive sectors, led by an 8% gain in financials. European banks, in particular, benefited from rising global bond yields, driven by investor expectations that the Federal Reserve will hike U.S. interest rates in December. Shares of HSBC, BBVA, Banco Santander and BNP Paribas enjoyed significant gains, rebounding from sharp losses earlier in the year. The sector was also boosted by the ECB’s decision not to cut rates further into negative territory.

Energy and materials stocks moved higher, supported by stabilizing oil prices and a modestly better economic outlook. Energy shares advanced 5% in aggregate, led by oil giants BP, Royal Dutch Shell and Total. In the
materials sector, Glencore shares rallied on rising iron ore prices and continuing asset sales as the mining company attempts to reduce its long-term debt obligations. Shares of rivals Rio Tinto and Anglo American also gained ground.

High-dividend-paying stocks mostly declined. The so-called “bond proxy” sectors, such as real estate and utilities, slipped as market interest rates moved higher. In the consumer staples sector, Nestlé was the largest detractor. The food giant’s shares lost 6% as it warned that it expects global sales growth to slow this year due to consumer resistance to price increases. Anheuser-Busch InBev shares declined sharply after the beverage giant also reduced its growth forecast for the year.

Health care stocks continued to come under pressure in the run-up to the U.S. presidential election, losing 5% in aggregate. Candidates in both major parties have criticized drug pricing practices, contributing to a steep decline in the sector this year. Shares of Novartis, Roche, Novo Nordisk and Astrazeneca were among the largest detractors in the index. Pharmacy benefit management companies also have pushed for lower prices on bulk purchases, which is having an adverse effect on profit margins at some major drug companies.

In fixed income markets, European government bond prices declined amid investor expectations for higher U.S. interest rates. The ECB’s refusal to cut rates or further expand its bond-buying program also weighed on eurozone debt markets. The yield on Germany’s benchmark 10-year note rose 29 basis points to 0.17%. Similar maturities in the U.K. advanced 50 basis points to 1.15%. Meanwhile, sterling continued its precipitous decline, falling 6% against the dollar.

Asia-Pacific

Japanese equities rose amid a weakening currency and mixed economic data. The yen depreciated 4% against the U.S. dollar, providing some relief to exporters and giving the Bank of Japan reason to pause from adding new monetary stimulus measures. The MSCI Japan Index gained 5%, while the MSCI Pacific Index traded 3% higher.

The Bank of Japan pushed the expected date to meet its 2% inflation target into 2019. Prices excluding food and energy were flat in September, a three-year low for the measure, while headline inflation declined 0.5% from the previous year. Despite these concerns, the BOJ did not change its stimulus plans at its first meeting since enacting a long-term interest rate target in late September.

Retail sales and industrial output were both lower than expected in September. Retail sales fell 1.9%, the seventh consecutive monthly decline. Industrial output was unchanged overall. The unemployment rate ticked down to 3.0%, matching its lowest mark since 1995.

Financials had the highest sector return in Japan, gaining 9%. The Bank of Japan’s decision to target a long-term interest rate continued to boost shares of financial firms, as higher rates could improve profitability within the struggling industry. Brokerage firm Nomura Holdings traded up 18%, following strong second quarter profits which were lifted by a surge in its wholesale division, housing mergers and acquisitions advisory business as well as currency and bond trading.

Shares of Japanese exporters climbed higher, supported by the weakening yen. Bicycle component manufacturer Shimano, gained 20% after reporting better-than-expected revenue. Consumer staples was the only sector to trade lower. Kao shares retreated as the household goods maker reported flat operating profit and weaker sales.

Australian equities retreated 2%. The prospect of higher interest rates boosted financials but held back other high-dividend-paying stocks, particularly real estate investment trusts. Private hospital operator Healthscope was a notable detractor, declining 28% following slower-than-expected revenue growth. The MSCI Hong Kong Index fell 1% as several real estate management companies lagged.

Emerging Markets
Emerging markets stocks pulled back following a strong rally earlier this year. The MSCI Emerging Markets Investable Market Index finished essentially flat as investors weighed the likelihood of a U.S. interest rate hike and the outcome of the U.S. presidential election. Energy stocks led gains on hopes OPEC would curb oil output. The dollar gained against most currencies, leading to losses for emerging markets bonds. U.S. dollar–denominated bonds, as measured by the J.P. Morgan EMBI Global index, fell 1.5%; local currency debt, as measured by the J.P. Morgan GBI-EM Global Diversified index, lost 0.8% in dollar terms.

Brazilian equities surged 14% as the new government forged ahead with a measure to cap government spending. The proposal, which won preliminary support from legislators in the first of two votes, was seen as a key victory for President Michel Temer. The measure still has to be ratified by Congress. Brazil’s central bank cut the benchmark interest rate for the first time in four years and commodity prices rose, further supporting gains. Iron ore producer Vale and state-owned oil giant Petrobras soared 37% and 34%, respectively. Pressure eased on Mexican stocks, helped by higher oil prices and a stronger peso. The MSCI Mexico IMI climbed 5%. Top gainers included cement giant Cemex and América Móvil, Latin America’s largest wireless operator. The peso increased 3% against the dollar.

Chinese stocks edged lower following steady gains since June. The MSCI China IMI fell 2%. Economic data was mixed. Growth remained stable at 6.7% during the third quarter, helped by consumer spending and stimulus measures. However, exports fell a more-than-expected 10% in September, while imports declined 1.9% from the year-earlier period. Shares of property developers China Resources Land and China Overseas Land & Investment fell as at least 21 cities introduced purchase restrictions and stricter mortgage lending requirements amid a red-hot real estate market.

Other Asian markets had mixed returns. Korean stocks dropped 5%. Shares of index heavyweight Samsung Electronics fell 1% as it ceased production of its fire-prone Galaxy Note 7 smartphone and lowered its third-quarter profit forecast. Indian equities were essentially flat. While India’s central bank cut interest rates by 25 basis points, a mixed batch of corporate earnings reports raised questions about stock valuations. Stocks in the Philippines declined 3% as President Rodrigo Duterte stepped up his anti-U.S. rhetoric and sought to forge closer business ties with China.

South African stocks struggled amid a weaker economic growth outlook and political strife that threatens the country’s investment-grade credit rating. Fraud charges were dropped against finance minister Pravin Gordhan on Oct. 31, helping to lift the rand 2% against the dollar. Meanwhile, President Jacob Zuma faced a widening split within his party. The MSCI South Africa IMI lost 1%, with declining prices for precious metals hurting shares of miner AngloGold Ashanti.

Turkish stocks declined 1%. The Turkish lira fell 3% to a record low against the dollar as the slowing economy, military conflicts in the region and political unrest stemming from the failed July coup prompted credit-rating downgrades. Given the lira’s weakness, Turkey’s central bank maintained its key interest rates following several cuts earlier this year to help spur growth. Meanwhile, Russian stocks edged 1% higher amid signs the price of crude oil, Russia’s top export, would be supported by a tentative OPEC agreement to curb output. While Russia is not an OPEC member, President Vladimir Putin was reportedly willing to cooperate with production cuts.

In debt markets, Saudi Arabia sold $17.5 billion of bonds — the largest emerging markets offering on record — to help the country cope with the new oil price environment. The heavily oversubscribed deal included 10-year bonds with a yield of 3.25%. Mexico’s state-owned oil giant Pemex raised $4 billion to buy back existing debt and help with 2017 financing needs, while the Mexican government sold €1.9 billion of eurobonds ($2.07 billion), including eight-year issues offering a 2.2% yield.

Developed market returns are in local currency and include net dividends. Emerging markets returns are in U.S. dollars.

Statements attributed to an individual represent the opinions of that individual as of the date published and do not necessarily reflect the opinions of Capital Group or its affiliates. The information provided is intended to highlight issues and not to be comprehensive or to provide advice. Any reproduction, modification, distribution, transmission or republication of the content, in part or in full, is prohibited.
Barclays Global Aggregate Index represents the global investment-grade fixed income markets. This index is unmanaged, and its results include reinvested distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes. This index was not in existence as of the date Class A shares became available; therefore, lifetime results are not shown.

Barclays U.S. Aggregate Index represents the U.S. investment-grade fixed-rate bond market. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

Dow Jones Industrial Average is a price-weighted index of 30 component common stocks, the components of which are determined by the Averages Committee, which is composed of the managing editor of The Wall Street Journal, the head of Dow Jones Indexes research and the head of CME Group research.

J.P. Morgan Emerging Markets Bond Index Global measures total returns for foreign-currency-denominated emerging markets bonds.

J.P. Morgan Emerging Markets Bond Index Global Diversified measures total returns for foreign-currency-denominated emerging markets bonds, employing limits on the weight of countries with large debt stocks.

MSCI EAFE® (Europe, Australasia, Far East) Index is a free float-adjusted market capitalization weighted index that is designed to measure developed equity market results, excluding the United States and Canada. Results reflect dividends net of withholding taxes. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

MSCI Emerging Markets Investable Markets Index includes large, mid-cap and small-cap segments, targeting a coverage range of close to 99% of the free-float-adjusted market capitalization of more than 20 emerging equity markets. Results reflect dividends gross of withholding taxes through December 31, 2000, and dividends net of withholding taxes thereafter.

MSCI Europe Index is a free float-adjusted market capitalization weighted index that is designed to measure developed equity market results across 15 developed markets countries in Europe. Results reflect dividends net of withholding taxes. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

MSCI Japan Index is a free-float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of Japan. Results reflect dividends net of withholding taxes. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

MSCI Pacific ex Japan is a free-float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of the developed markets in the Pacific region, excluding Japan. It consists of Australia, Hong Kong, New Zealand and Singapore. Results reflect dividends net of withholding taxes. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

MSCI United Kingdom Index is a free float-adjusted market capitalization weighted index that is designed to measure the results of the U.K. market. Results reflect dividends net of withholding taxes. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

MSCI World Index is a free float-adjusted market capitalization weighted index that is designed to measure equity market results of developed markets. The index consists of more than 20 developed market country indexes, including the United States. Results reflect dividends net of withholding taxes. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

Nasdaq Composite is an unmanaged index representing the companies traded on the Nasdaq stock market and the National Market System.

S&P/TSX Composite Index is an unmanaged market capitalization weighted index of stocks traded in the Canadian markets.

S&P 500 Index is a market capitalization-weighted index based on the results of 500 widely held common stocks. This index is unmanaged, and its results include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or U.S. federal income taxes.

Securities offered through American Funds Distributors, Inc.

Lit. No. ITGEFL-103-11160  CGD/10357- 556476