LimmatWealth

Investment Strategy April 2017

Data & Forecasts

	Growth (%)		Inflation (%)		Currencies (vs. USD)		
	GDP 16	GDP 17	CPI 16	CPI 17	Actual	3 Mo.	12 Mo.
Switzerland	1.0	1.3	-0.4	0.0	1.00	1.02	0.97
Germany	1.7	1.5	0.4	1.5	-	-	-
Euro Area	1.7	1.6	0.3	1.1	1.07	1.05	1.10
UK	1.8	1.5	0.7	2.5	1.25	1.25	1.30
USA	1.6	2.3	1.2	2.3	1.00	1.00	1.00
Japan	0.5	0.8	-0.2	0.5	111	110	110
Brazil	-3.3	0.2	9.0	5.4	3.12	3.10	3.25
Russia	-0.8	1.1	7.2	5.0	56.09	58.00	60.00
India	7.6	7.2	5.5	5.2	64.91	65.00	67.00
China	6.6	6.5	2.1	2.3	6.89	7.00	7.30

	Bonds (10 yrs.)			Profits (%)		Equities		
	Actual	3 Mo.	12 Mo.	EPS 16	EPS 17	Actual	3 Mo.	12 Mo.
Switzerland	-0.10	0.00	0.25	128	11	9'638	↘	↗
Germany	0.33	0.50	0.75	86	9	12'313	↘	↗
Euro Area				52	10	6'898	↘	↗
UK	1.14	1.14	1.50	138	8	7'323	↘	↗
USA	2.40	2.50	3.00	16	12	2'363	↘	↗
Japan	0.08	0.00	0.25	17	10	18'983	↘	↗
Brazil	10.06	10.00	10.00	732	12	64'984	↘	↗
Russia	4.17	4.25	4.25	77	12	538	↗	↗
India	6.61	6.50	6.50	36	18	29'824	↘	↗
China	3.29	3.25	3.25	24	14	2'818	↗	↑

Fed hikes rates by 0.25%

As expected, the American Central bank increased interest rates by 25 basis points to a new target range of 0.75% - 1.0%. Released economic data points towards continuing economic growth and slowly rising inflation: Particularly with regards to wage costs, which have risen by 2.8% year-over-year, we see soaring inflationary pressures. 235’000 new jobs (nonfarm payrolls) and an unemployment rate of only 4.7% support this assumption. The latest inflation rates (consumer prices +2.7%, core rate +2.2%) have reached their targets and further interest rate hikes have to be expected. Current interest rates are still below their normal level. In Europe, inflationary fears are premature, because the core rate (0.7%) is way below the target zone. The increase of the consumer inflation rate (+1.5%) is heavily distorted by volatile food and energy prices. Consequently, fears of a shift away from the expansionary monetary policy by the ECB are premature. To be more precise, we don’t see such a shift before autumn because of elections in many European countries. In the United Kingdom, inflation is relatively high (consumer prices +2.3%, core rate +2%), which does not come as a surprise in light of the devalued currency. Historically low unemployment of 4.7% and afore mentioned price pressures make an interest rate hike more and more likely. In Japan, annualized 4th quarter growth was increased from 1.0% to 1.2%. At the same time, unemployment dropped from 3.0% to 2.8%. Inflation is still out of sight (consumer prices +0.3%, core rate +0.1%). In Brazil, the economic contraction seems to lose steam (4th quarter -2.5% after -2.9% during the 3rd quarter) and also inflation is receding (4.7% vs 5.0%). China reported a slump of the inflation rate from 2.5% to 0.8%, which came as a surprise. Also in Russia, inflation is dropping (consumer prices +4.6%, core rate 5%).

European bonds weaker

The interest rate hike by the Fed was expected and USD bonds did not show a meaningful reaction. In contrast, interest rates in Switzerland and Europe rose slightly and prices declined in the order of about 0.7% (1-10 year bond segment). The interest rate differential between French and German government bonds (10 years), which historically has hovered around 20 to 30 basis points, rose to more than 80 basis points in February. Thanks to declining fears of a victory of Marine Le Pen, the interest rate differential declined to approximately 65 basis points in March. The High Yield index declined slightly (-0.3%), while the emerging market bond index rose another 0.4%. The outlook for investment grade bonds continues to be murky and government bonds are only held for their diversification benefits.

Heavy correction of oil

Despite the Fed hike, the USD gave back some of its losses according to the DXY-Index (-0.8%). Next to the Euro (+0.7%) mainly emerging markets currency climbed versus the USD. We think that the USD is well supported at the current level. The official notification of Britain to withdraw from the European Union did not have a meaningful impact on the Pound Sterling (+0.5%).

While gold advanced by 1%, the oil price dropped by 6%. High US inventories, an ever expanding number of shale oil production sites and doubts about the implementation of announced production cuts by OPEC led to worries of a potential oversupply. The broad commodity index dropped by 2.7%. We continue to hold gold as some kind of a hedge in the case of currency turbulences.

Equity rally continues

The equity rally continued in industrial (+1.2%) as well as in emerging markets (+2.2%). US equities underwent an interim correction, when President Trump's healthcare reform stalled. Nevertheless, over the whole month, the S&P500 ended unchanged (-0.04%). In Holland, the right populist Geert Wilders got 13% of votes and finished only second after Mark Rutte and his 'People's Party for Freedom and Democracy'. Subsequently, the Euro Stoxx soared by more than 5% in March. In the coming weeks, investors will focus on elections in France (April 23) and earnings of US companies for the 1st quarter. While we don't expect Marine Le Pen to win in France, expectations for a rise of US earnings in the order of 9% are demanding. We prefer equity markets, whose central banks pursue an expansionary monetary policy such as in Europe. In our view, chances are quite high that European markets will outperform their American counterparts. We also like emerging markets due to their less demanding valuation and in many cases expansionary monetary policy. We see a slow interest rate increase over the coming quarters, which results in low expected equity returns by historical standards. As a result, equities are only neutrally weighted. We see a high level of carelessness, which in our view is not warranted in light of manifold risks (valuation, politics, protectionism, etc.)

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