LimmatWealth

Investment Strategy February 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	0.99	1.02	0.97
Germany	1.7	1.5	0.4	1.5	-	-	-
Euro Area	1.7	1.6	0.3	1.1	1.08	1.05	1.10
UK	1.8	1.5	0.7	2.5	1.26	1.23	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	113	115	110
Brazil	-3.3	0.2	9.0	5.4	3.15	3.25	3.50
Russia	-0.8	1.1	7.2	5.0	60.27	60.00	65.00
India	7.6	7.2	5.5	5.2	67.62	67.00	70.00
China	6.6	6.5	2.1	2.3	6.88	7.00	7.30

	Bonds (10 yrs.)			Profits (%)		Equities		
	Actual	3 Mo.	12 Mo.	EPS 16	EPS 17	Actual	3 Mo.	12 Mo.
Switzerland	-0.06	0.00	0.25	127	11	9'063	9'050	9'350
Germany	0.44	0.50	0.75	82	9	11'535	11'500	12'000
Euro Area				51	10	6'346	6'350	6'700
UK	2.48	2.50	3.00	138	8	7'099	7'100	7'400
USA	2.48	2.50	3.00	17	12	2'279	2'275	2'300
Japan	0.09	0.00	0.25	12	11	19'148	19'100	19'000
Brazil	10.92	11.00	11.00	680	20	64'671	64'500	66'500
Russia	4.32	4.50	4.25	66	13	562	560	580
India	6.40	6.50	6.50	17	20	27'672	27'600	28'000
China	3.37	3.25	3.25	24	12	2'838	2'825	2'900

IMF sees slight acceleration of growth

The IMF (International Monetary Fund) published its revised forecasts in January. For 2017, the IMF left its forecast for worldwide growth unchanged at 3.4% (2016: 3.1%) but in 2018 growth will accelerate to 3.6% as a result of good prospects of the emerging economies. As usual, the IMF sees many risks (protectionism, more restrictive monetary policy in comparison to expectations, geopolitics, excessive national debt, setbacks in Chinese growth etc.). In the US, labor data worsened slightly (unemployment rose from 4.6% to 4.7%, private payrolls +144'000 vs. +156'00). Consumer prices rose by 2.1% and have almost reached the level of the core rate (2.2%). First estimates for growth in the 4th quarter stand at an annualized 1.9%, which means a significant slowdown in comparison to the 3rd quarter (+3.5%). Furthermore, President Trump canceled negotiations over the Trans-Pacific-Trade-Agreement. The Euro Zone expanded by 1.8% during the 4th quarter (year-over-year). Unemployment dropped to 9.6%. Consumer prices soared from 1.1% to 1.8%, while the less volatile core rate remained unchanged at 0.9%. In the United Kingdom, the core rate as well as headline inflation stand at 1.6%. During the 4th quarter, the economy grew by an unchanged 2.2% (year-over-year). Prime Minister Theresa May announced that Britain's departure from the EU will be total and decisive (hard Brexit). In Japan, data hardly changed in comparison to the previous month (consumer prices +0.3%, core rate +0.1%, unemployment 3.1%). China estimates 4th quarter growth at 6.8%, which compares to 6.7% during the 3rd quarter. Inflation remains close to 2% (2.1%). In India, inflation declined further (from 3.6% to 3.4%). Additionally, the government announced that the Indian economy had grown by 7.9% during the calendar year 2016, which means another acceleration of the expansion in comparison to 2015 (7.1%).

European interest rates rise further

While yields of 10-year US government bonds hardly changed (+3 basis points), slightly rising interest rates were observed in Europe (Switzerland +13 bp, United Kingdom +18 bp) and especially in Germany (+24 bp). At the same time, the German yield curve steepened (stronger boost at the long end of the curve). Despite this interest rate hike, Swiss 10-year government bonds continue to offer negative yields to maturity (-0.13%). In contrast to high quality government bonds, emerging markets debt (+1.5%) and high yield bonds (+1.5%) performed well. Notwithstanding the higher interest rate level, we are expecting negative total returns for high quality government bonds for the coming year. Government bonds are only held for their diversification benefits.

After the Swiss National Bank decided in January 2015 to abolish the minimum rate of CHF 1.20 per Euro, we had bought USD-Bonds for our Swiss Franc and Euro denominated portfolios. In consideration of our currency and interest rate forecasts, we are realizing gains by selling these positions. Sales proceeds are converted back to the reference currency of the respective portfolio.

Weakish USD

After high gains in the previous months and comments by President Trump that the currency was too strong in his mind, investors took profits in the USD. According to the DXY-Index, the greenback dropped by 2.6% in January. In contrast, Yen (+3.7%), Swiss Franc (+3%) and Euro (+2.7%) advanced. We expect a continued weakness of the USD over the coming months in comparison to the Euro.

The broad commodity index hardly moved in January (+0.1%), while gold profited from Donald Trump's tweets (+5.1%). We see gold as some kind of hedge in the case of currency turbulences.

Strong start of equities into 2017

Currently, investors are negating rising economic policy risk and are focusing on improving growth prospects, which resulted in higher equity prices. Industrial- (+2.5%) as well as emerging equity markets (+5.2%) performed nicely in January. Extrapolations of earnings released so far point towards profit growth of US companies in the order of 4% during the 4th quarter, which would be above expectations. We are sticking to our slightly underweighted equity allocation since in our view, investors are underestimating the manifold political (protectionism, rising populism in the context of elections in Europe etc.) as well as economic risks. The hope for acceleration of growth is based on deregulation, lower tax rates and higher infrastructure spending by the government. Investors are forgetting that the combination of lower taxes and higher spending tends to result in a soaring government deficit, which normally leads to rising bond yields. We are afraid that the improving growth outlook will be leveled out by a more restrictive monetary policy and higher bond yields: Rising yields will lead to a valuation compression (lower price-earnings multiples) thereby offsetting higher earnings.

Limmat Wealth AG Gartenstrasse 32 Postfach 1882 CH-8027 Zürich

T +41 44 208 24 50 F +41 44 208 24 51 info@limmatwealth.com www.limmatwealth.com