LimmatWealth

Investment Strategy September 2016

Data & Forecasts

	Growth (%)		Inflation (%)		Currencies (vs. USD)		
	GDP 16	GDP 17	CPI 16	CPI 17	Actual	3 Mo.	12 Mo.
Switzerland	1.2	1.5	-0.6	-0.1	0.98	1.00	1.02
Germany	1.6	1.2	0.5	1.4	-	-	-
Euro Area	1.6	1.4	0.4	1.1	1.11	1.10	1.08
UK	1.7	1.3	0.8	1.9	1.31	1.29	1.30
USA	2.2	2.5	0.7	1.5	1.00	1.00	1.00
Japan	0.3	0.1	-0.2	1.2	103	105	100
Brazil	-3.3	0.5	8.7	6.1	3.23	3.50	3.60
Russia	-1.2	1.0	8.4	6.5	65.25	65.00	70.00
India	7.4	7.4	5.3	5.3	66.96	67.00	70.00
China	6.6	6.2	1.8	2.0	6.68	6.70	7.00

	Bonds (10 yrs.)			Profits (%)		Equities		
	Actual	3 Mo.	12 Mo.	EPS 16	EPS 17	Actual	3 Mo.	12 Mo.
Switzerland	-0.48	-0.50	0.00	112	10	8'916	8'850	9'200
Germany	-0.06	0.00	0.50	64	12	10'593	10'500	11'000
Euro Area				38	12	5'910	5'850	6'000
UK	1.58	1.75	2.25	88	16	6'782	6'800	6'900
USA	1.58	1.75	2.25	6	13	2'171	2'150	2'200
Japan	-0.05	-0.10	0.00	10	8	16'927	16'400	16'700
Brazil	12.08	12.00	12.00	499	23	57'901	57'500	58'000
Russia	4.35	4.50	4.50	29	16	458	460	490
India	7.11	7.50	7.00	27	19	28'424	27'500	29'000
China	2.81	3.00	3.00	12	13	2'714	2'700	2'900

Japan stagnates

Japan announced another stimulus package in the order of 28.1 trillion Yen (~265bn CHF). Thereof, about 15 trillion Yen are expected from the private sector on which the government has no direct influence. As a result, markets were disappointed. After having grown 1.9% during the 1^{st} quarter, the Japanese economy stagnated with an annualized 0.2% during the 2^{nd} quarter. Inflation (consumer prices -0.4%, core rate +0.3%) and unemployment (3.0%) remained low. In the US, employment data (nonfarm payrolls +255'000) surprised positively again. Unemployment (4.9%) and inflation (consumer prices +0.8%, core rate +2.2%) did not deviate much from earlier announcements. The purchasing manager index (51.5) indicates slow but continued economic growth. Janet Yellen's speech at the meeting in Jackson Hole did not give a hint about the timing of the next interest rate hike. We are expecting the next step mid of December. The Bank of England lowered rates (from 0.5% to 0.25%) for the first time in seven years and announced a bond purchasing program in the order of 70bn GBP (60bn GBP government bonds and 10bn GBP corporates bonds). In the 2^{nd} quarter, the British economy expanded by 2.2% year-over-year. The Euro zone grew at 1.6% during the 2^{nd} quarter, which compares with 1.7% during the 1^{st} quarter. Inflation (consumer prices +0.2%, core rate +0.8%) remained below the target rate of 2%. The purchasing manager index (53.3) points towards further growth. In India, growth declined from 7.9% in the 1^{st} quarter to 7.1% in the 2^{nd} quarter. Meanwhile, the decline of GDP slowed from -5.4% to -3.8% in Brazil. Chinese inflation continued to fall (from 1.9% to 1.8%) and the purchasing manager index improved from 50.3 to 51.9. Russia revised 2^{nd} quarter growth from -1.2% to -0.6%. The purchasing manager index stands at 53.5 points.

Strong performance of British bonds

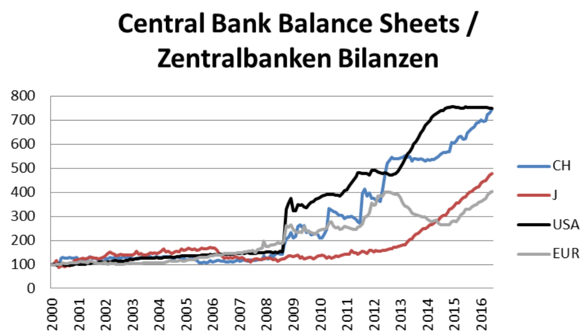
While the yield to maturity of long dated bonds increased in Switzerland (+9 basis points), Germany (+5 basis points) and the US (+13 basis points), they fell in the UK by 5 basis points and helped the British bond index to a gain in the order of 2.8% in August.

Emerging markets debt and high yield bonds also returned approximately 2%. In light of low real and nominal yields the outlook for bonds is rather unattractive. Bonds are mainly held for their diversification benefits.

Oil recovers

Major currencies did not change significantly in August. According to the DXY-Index, the USD remained unchanged. The Euro gained 1.3% in comparison to the Swiss Franc. Owing to higher US rates, we are expecting a slightly stronger USD versus the Euro over the next 12 months. Meanwhile, China will devalue its currency step by step.

The broad commodity index lost 1.8% in August. While oil soared 7.5% thanks to discussions about an OPEC meeting in Algeria, gold lost 3%. Balance sheets of central banks have increased dramatically in the aftermath of the financial crisis. The inability of central banks to normalize the situation could lead to a loss of trust in the fiat money system. In order to hedge this risk we are increasing our gold allocation by 2% to 5%.



Emerging markets continue to rally

US equity markets reached new all-time highs in August and supported the developed world index (+0.2%). Investors allocated additional funds to emerging markets equities (+2.7%). Since mid of June the emerging markets index has gained almost 15% and even more than 30% since mid of February of this year.

The complacency of investors, which is reflected in the low volatility of indices, is irritating us. On the political agenda, Italy plans a referendum, which could shake the European Union to the very foundations. Should voters misuse the referendum to show their dissatisfaction and populist parties gain voters, the exit from the Euro Zone could become a topic with far reaching consequences. Economically, we see rising US interest rates and the lack of profit growth as a challenge for markets. The US reporting season is almost over and earnings seem to have dropped by less than 2% in comparison to expectations of a decrease in the order of 5% year-over-year. The attractiveness of equities is mainly based on the unattractiveness of other asset classes such as bonds. Significantly higher equity prices in the coming months would require additional extreme moves by central banks. Although previous measures were able to avoid a meltdown of the system during the financial crisis, additional actions in the aftermath did not have a lasting effect on economies. As a result of this experience, we do not expect additional programs of this sort. Consequently, we do not see much potential for equities and are remaining slightly underweighted.

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