



LimmatWealth

World Wide Outlook

4th quarter 2016



Important Events

- Compared to the 2nd quarter, which had ended with the Brexit, the 3rd quarter was rather quiet and equities performed nicely.



Growth

- In July 2016, the IMF reduced its forecasts again. The **world economy** is now expected to grow by **3.1% in 2016 and 3.4% in 2017**. In other words, the IMF is not expecting an acceleration of economic momentum in 2016 (2015: 3.1%). The IMF sees many economic and political risks.



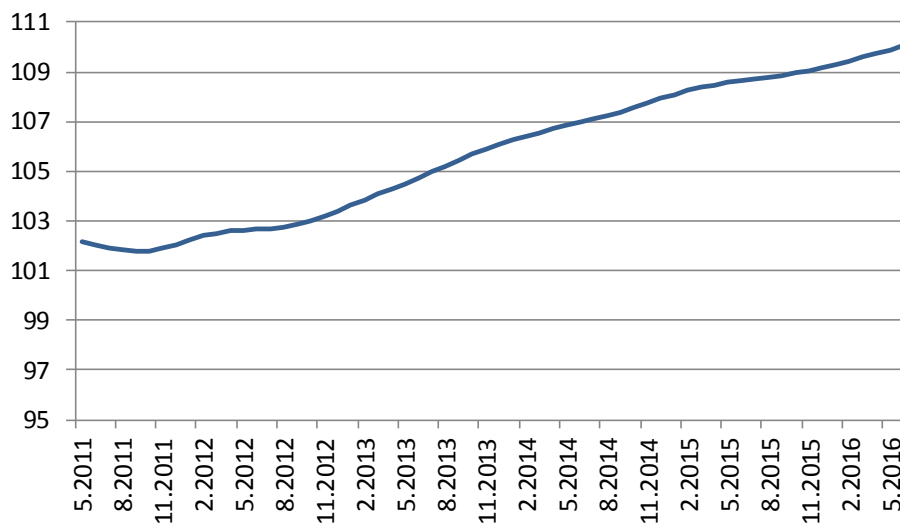
Growth

- In **advanced economies**, the IMF sees more or less constant growth of slightly below 2% (2015: 1.9%, **2016: 1.8%, 2017: 1.8%**). Monetary policy has to remain accommodative. Pressing on with structural reforms remains one of the key necessities for advanced as well as emerging countries.
- Growth in emerging markets is forecasted to rise from 4.0% in 2015 to **4.1% and 4.6% in 2016 and 2017**. The IMF sees exchange rate flexibility as one of the most important means for reducing the impact of potential adverse external shocks.



Growth

- The 'OECD Leading Indicator' points towards slow growth in the quarters ahead:





Growth

LEI (US Leading Indicator) indicates slow growth in the US*



US Recessions since 1960

Start	End	Months	GDP	Trigger
1960.04	1961.02	10	-1.60%	Monetary policy
1969.12	1970.11	11	-0.60%	Vietnam, monetary & fiscal policy
1973.11	1975.03	16	-3.20%	1st oil crisis
1980.01	1980.07	6	-2.20%	Monetary policy
1981.07	1982.11	16	-2.70%	Iran, 2nd oil crisis
1990.07	1991.03	8	-1.40%	Monetary policy
2001.03	2001.11	8	-0.30%	Dot Com, 9/11
2007.12	2009.06	18	-5.10%	Subprime

* False signals only in 1966 und 1995



Growth

Gross Domestic Product (GDP)

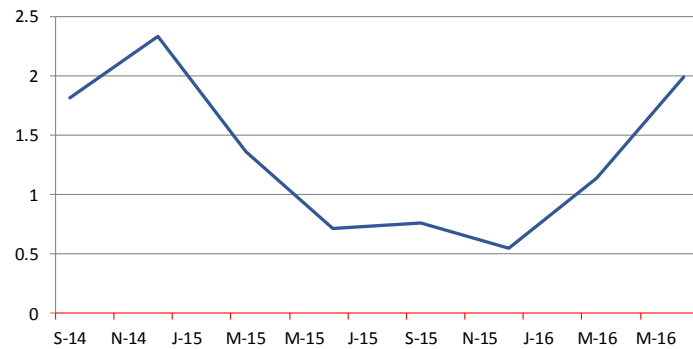
	GDP 13	GDP 14	GDP 15	GDP 16	GDP 17
Switzerland	1.8	1.9	0.9	1.2	1.5
Germany	0.4	1.6	1.5	1.6	1.2
Euro Zone	-0.3	0.9	1.6	1.6	1.4
UK	2.2	2.9	2.2	1.7	1.3
USA	1.5	2.4	2.4	2.2	2.5
Japan	1.4	0.0	0.5	0.3	0.1
Brazil	3.0	0.1	-3.8	-3.3	0.5
Russia	1.3	0.7	-3.7	-1.2	1.0
India	6.6	7.2	7.3	7.4	7.4
China	7.7	7.0	6.9	6.6	6.2

Source: IMF & Limmat Wealth

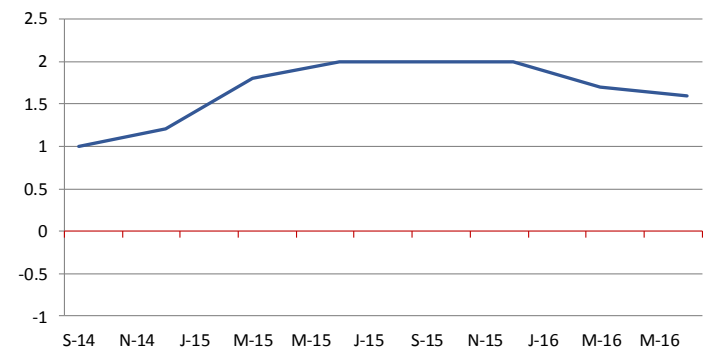


Growth

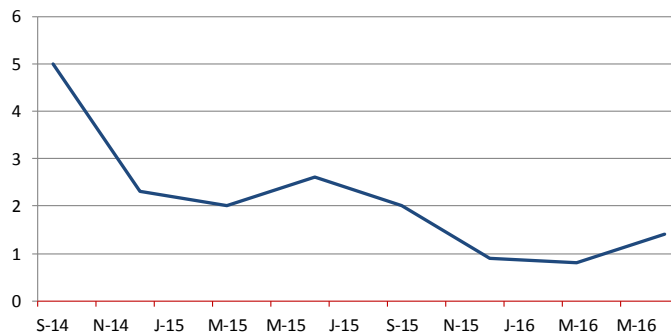
GDP-Growth Switzerland



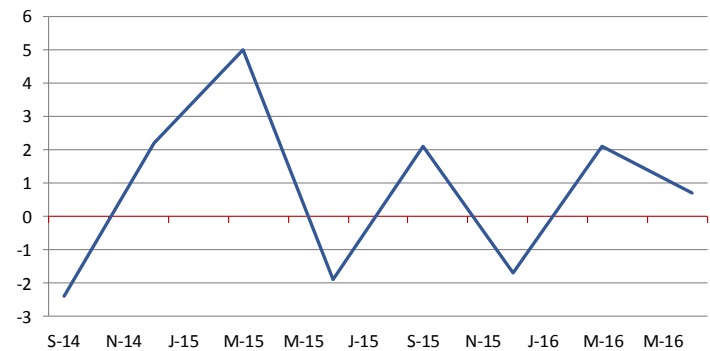
GDP-Growth Euro Zone



GDP-Growth USA



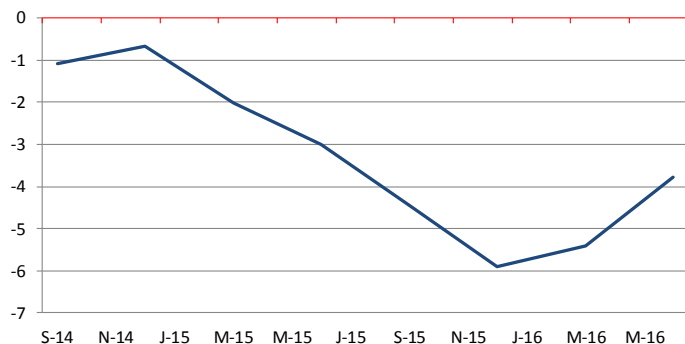
GDP-Growth Japan



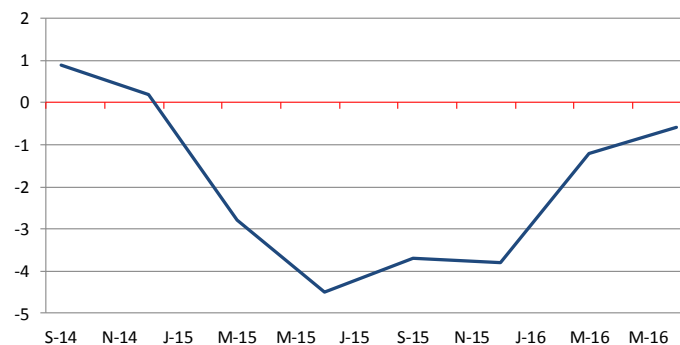


Growth

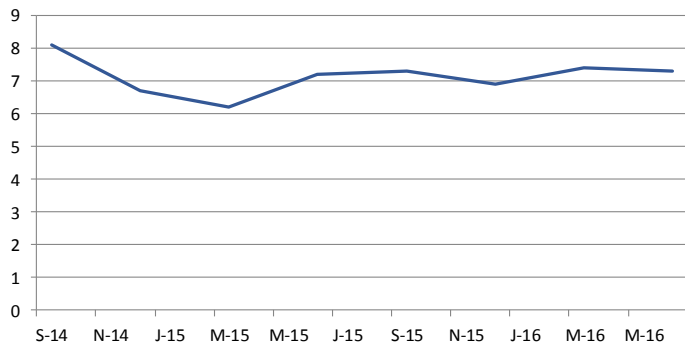
GDP-Growth Brazil



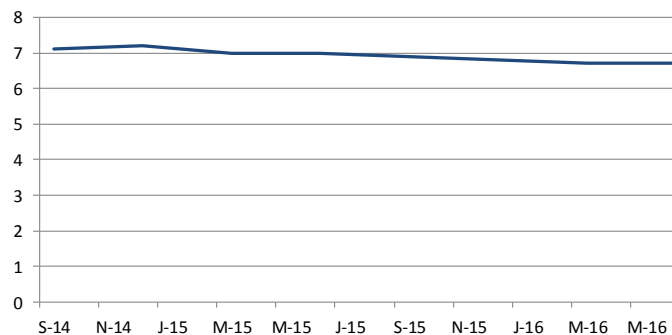
GDP-Growth Russia



GDP-Growth India



GDP-Growth China





Inflation

- By historical standards, inflation will remain low in **advanced economies**: After 0.3% in 2015 the IMF sees an increase to **0.7% in 2016 and 1.5% in 2017**.
- **Emerging and developing countries** are in disinflation: After 4.7% in 2015, inflation will decline to **4.5% (2016)** and **4.2% (2017)**.



Inflation

Consumer Price Inflation (CPI)

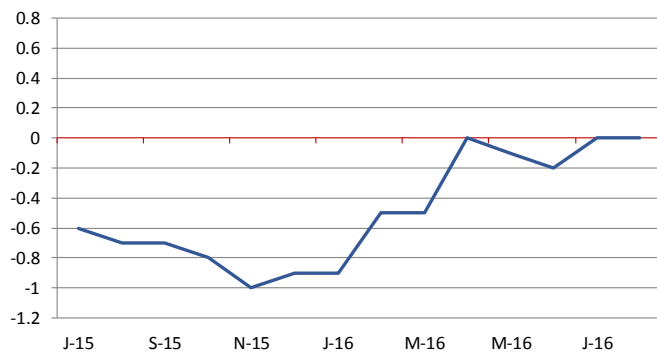
	CPI 13	CPI 14	CPI 15	CPI 16	CPI 17
Switzerland	-0.2	0.0	-1.1	-0.6	-0.1
Germany	1.6	0.8	0.1	0.5	1.4
Euro Zone	1.3	0.4	0.0	0.4	1.1
UK	2.6	1.5	0.1	0.8	1.9
USA	1.4	1.4	0.3	0.7	1.5
Japan	0.4	2.7	0.8	-0.2	1.2
Brazil	6.2	6.3	9.0	8.7	6.1
Russia	6.8	7.8	15.5	8.4	6.5
India	9.4	5.9	4.9	5.3	5.3
China	2.6	2.0	1.4	1.8	2.0

Source: IMF & Limmat Wealth

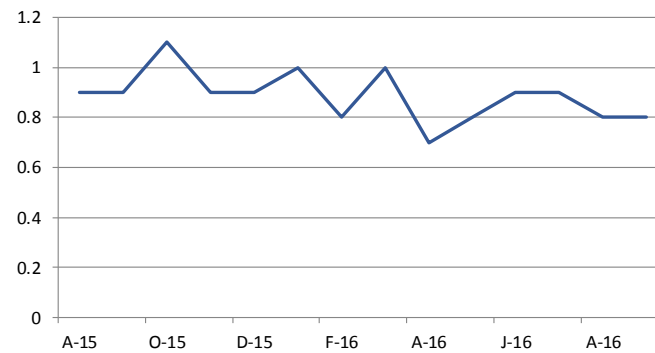


Inflation

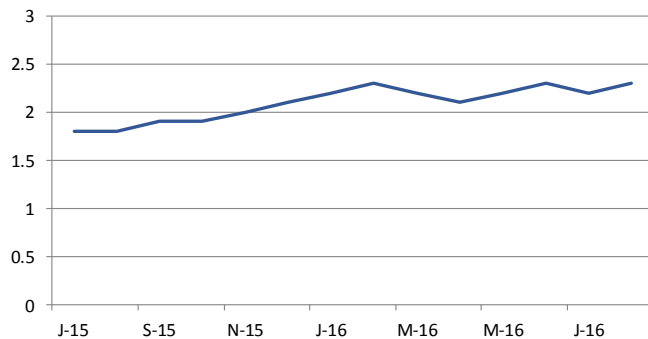
Inflation Switzerland (core)



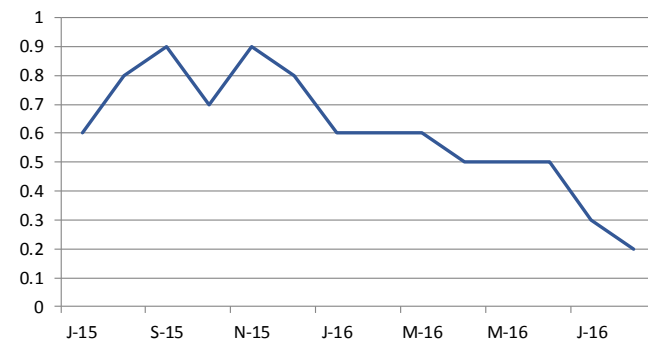
Inflation Euro Zone (core)



Inflation USA (core)



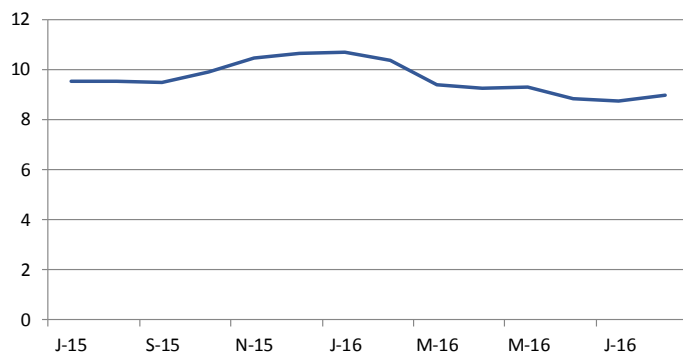
Inflation Japan (core)



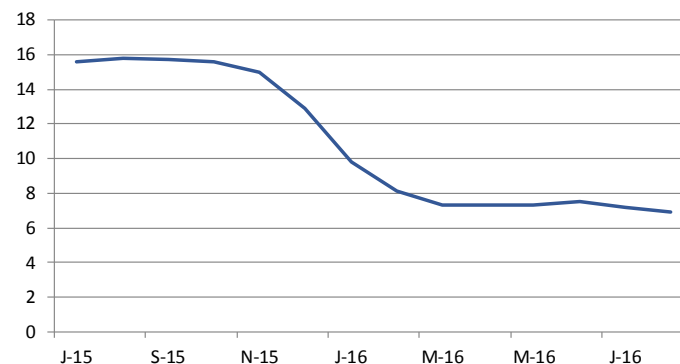


Inflation

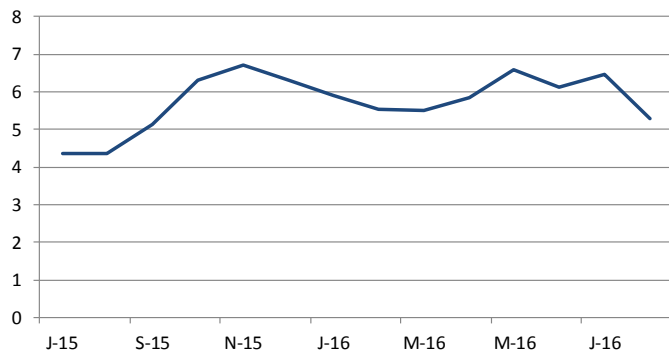
Inflation Brazil



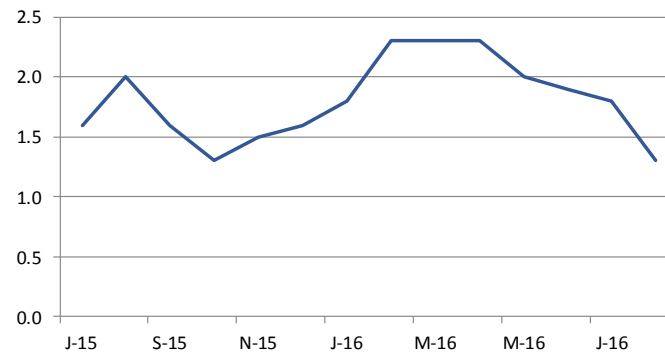
Inflation Russia



Inflation India



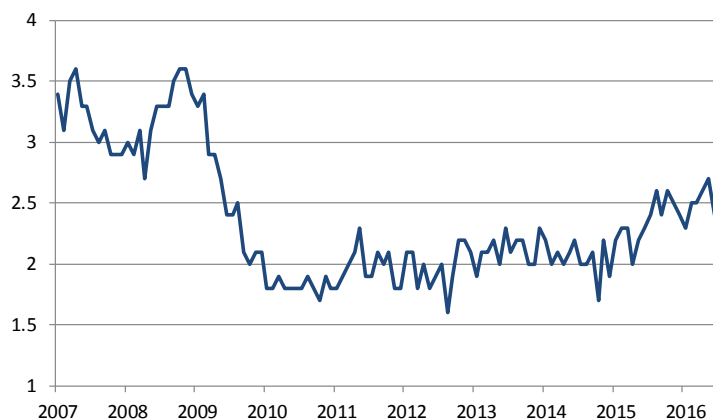
Inflation China



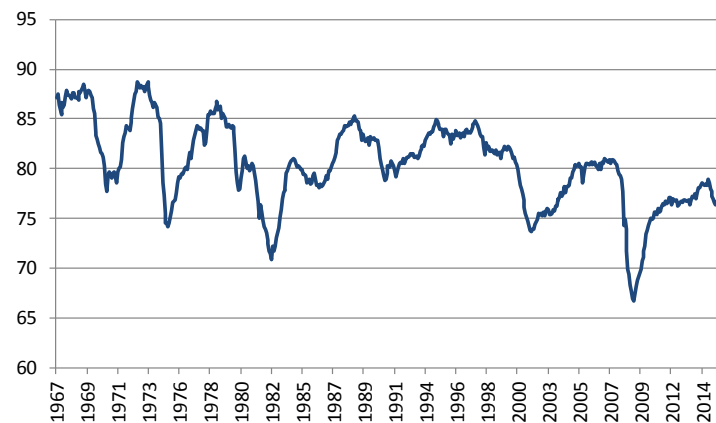


Inflation USA

USA:
Yearly % change average hourly earnings



USA:
Capacity Utilization %



US inflation to remain low as long as hourly earnings and capacity utilization stay at current levels.



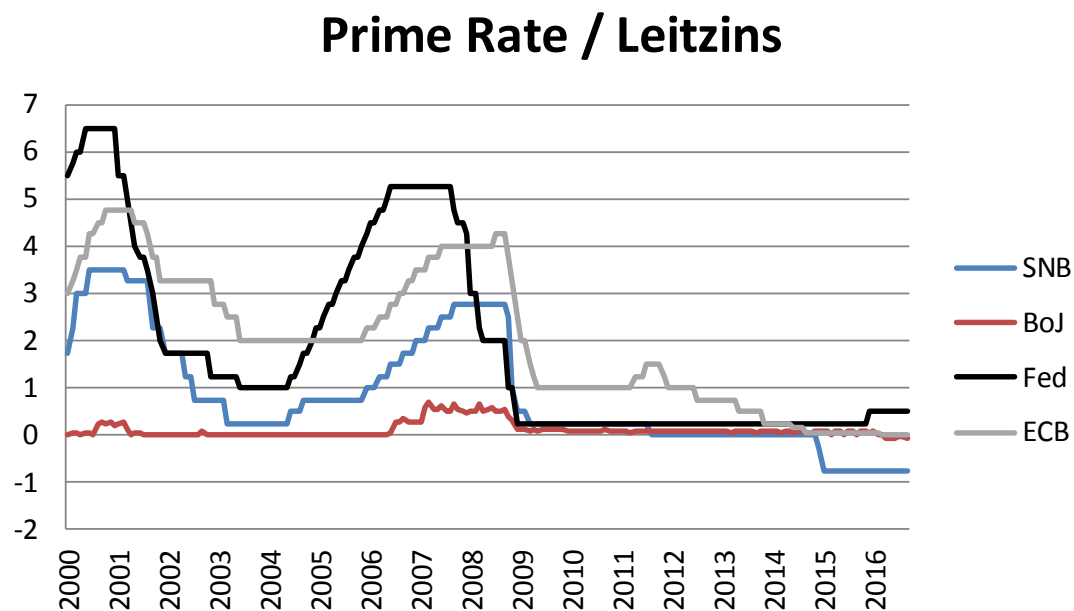
Monetary Policy

- In the 2nd quarter, the **European Central Bank** increased its monthly bond purchasing program from Euro 60bn to Euro 80bn and expanded it to investment grade corporate bonds (no banks). In September, the ECB abstained from an extension of its bond purchasing program, which presumably will end in spring 2017. Nevertheless, monetary policy will remain very expansionary for the foreseeable future.
- In the **US**, the FOMC hiked the 'Fed Funds Rate' on December 2015 by 25 basis points to 0.25%-0.5%. This constituted the first rise in seven years. The importance of this increase is based on historical experience according to which a first interest hike is usually followed by additional ones. Further interest hikes will occur depending on economic data. We are continuing to forecast an interest hike in the order of 25 basis points in December.
- The Japanese Central Bank (BoJ) wants to steer the whole yield curve (i.e. the level and the slope) from now on, which increases the danger of misallocations of capital even further.



Monetary Policy

- The normalization of the extremely expansionary **conventional** monetary policy ...

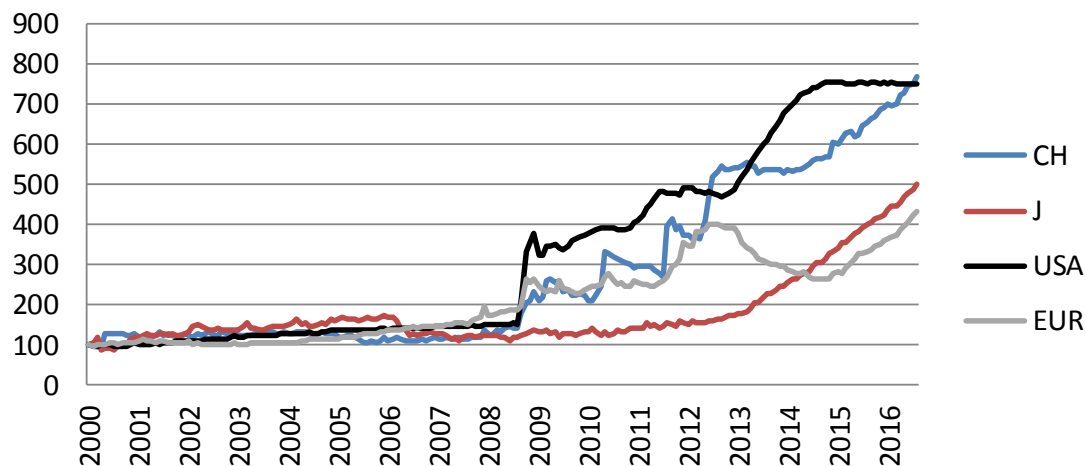




Monetary Policy

... as well as **unconventional** (e.g. bond purchases) monetary policy ...

Central Bank Balance Sheets / Zentralbanken Bilanzen





Monetary Policy

... becomes a tightrope walk between

- **overheating** if central banks normalize too late
(inflation and/or formation of bubbles)
- **recession risk** if central banks normalize too early
- **currency risk**



Indebtedness

Public Debt in % of GDP

Source: Bloomberg

(Government debt held by public)

Russland / Russia	14
China / China	17
Schweiz / Switzerland	34
Neuseeland / New Zealand	34
Norwegen / Norway	39
Australien / Australia	44
Schweden / Sweden	44
Indien / India	52
Finnland / Finland	61
Niederlande / Netherlands	69
Deutschland / Germany	72
USA / United States	74
Grossbritannien / United Kingdom	91
Euro Zone / Eurozone	91
Kanada / Canada	95
Frankreich / France	98
Spanien / Spain	101
Irland / Ireland	101
Singapur / Singapore	106
Belgien / Belgium	106
Portugal / Portugal	129
Italien / Italy	136
Griechenland / Greece	171
Japan / Japan	228



Indebtedness

Budget Deficit / Surplus in % of GDP

Source: Bloomberg

Griechenland / Greece	-7.2
Spanien / Spain	-5.1
Japan / Japan	-5.0
Portugal / Portugal	-4.4
Grossbritannien / United Kingdom	-4.4
Indien / India	-4.1
Frankreich / France	-3.5
China / China	-3.4
USA / United States	-2.8
Finnland / Finland	-2.7
Belgien / Belgium	-2.6
Italien / Italy	-2.6
Irland / Ireland	-2.3
Euro Zone / Eurozone	-2.1
Niederlande / Netherlands	-1.8
Kanada / Canada	-1.3
Australien / Australia	-0.9
Schweiz / Switzerland	-0.2
Schweden / Sweden	0.0
Neuseeland / New Zealand	0.0
Deutschland / Germany	0.7
Russland / Russia	0.8
Norwegen / Norway	5.4
Singapur / Singapore	8.6



Currencies and Gold

- According to the DXY-Index, the USD lost 0.7% during last quarter and has dropped 3.2% during 2016. In the wake of the Brexit, the British Pound weakened another 2.6%. Winners – versus the greenback – were the Japanese Yen (+1.8%), the Euro (+1.2%) and the Swiss Franc (+0.5%).
- We are forecasting higher interest rates over the coming months, which will lead to a slightly stronger USD versus Euro. The Swiss Franc will depreciate very slowly towards its purchasing power parity. The British Pound is expected to stabilize at the current level. China is interested in a weaker currency and consequently we are seeing a gradual devaluation of the Renminbi.



Currencies and Gold

- Gold closed the 3rd quarter practically unchanged. We are holding on to our gold position because the yellow metal offers some hedge in light of the current uncertainties. Mainly in the case of currency wars, demand for gold would increase dramatically.
- According to the World Gold Council, 2nd quarter gold demand increased by 15% to 1'050,2 tons year-over-year. The boost came mainly from ETFs and similar products while jewellery demand dropped 14%. Supply rose only 10% to 1'144,6 tons.



Currencies and Gold

	Currencies / Gold		
	Actual	3 Mo.	12 Mo.
USD/CHF	0.98	1.00	1.02
EUR/USD	1.12	1.10	1.08
USD/Yen	102	105	100
GBP/USD	1.28	1.29	1.30
USD/BRL	3.21	3.25	3.60
USD/Rubel	62.45	65.00	70.00
USD/INR	66.55	67.00	70.00
USD/CNY	6.67	6.70	7.00
EUR/CHF	1.09	1.10	1.10
Gold (USD)	1308	1350	1400



Currencies and Gold

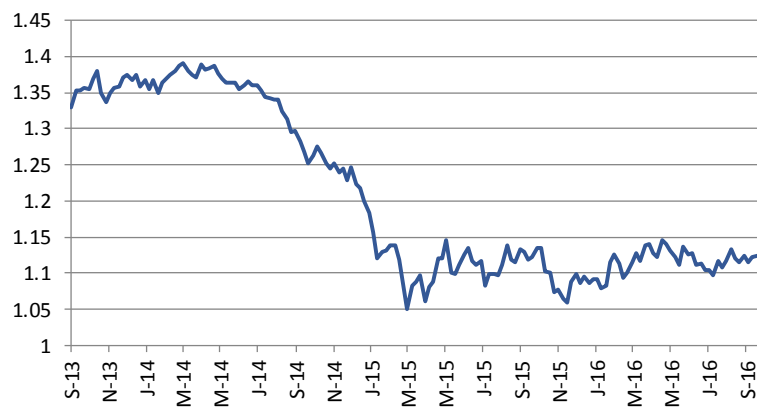
	Current Account in % of GDP
United Kingdom	-5.4
Australia	-4.7
Turkey	-4.5
Latin America	-3.7
Canada	-3.2
Brazil	-3.2
USA	-2.6
Middle East	-1.3
India	-1.1
G10	-0.2
EMEA	0.5
BRICS	1.9
Europe	2.6
China	3.0
Euro Zone	3.2
Japan	3.3
Asia	3.4
Sweden	5.0
Russia	5.3
Norway	6.6
Denmark	7.0
Switzerland	11.2

Current Account =
+ Balance of trade of goods
+ balance of trade of services
+ net factor income
+ net transfer income.

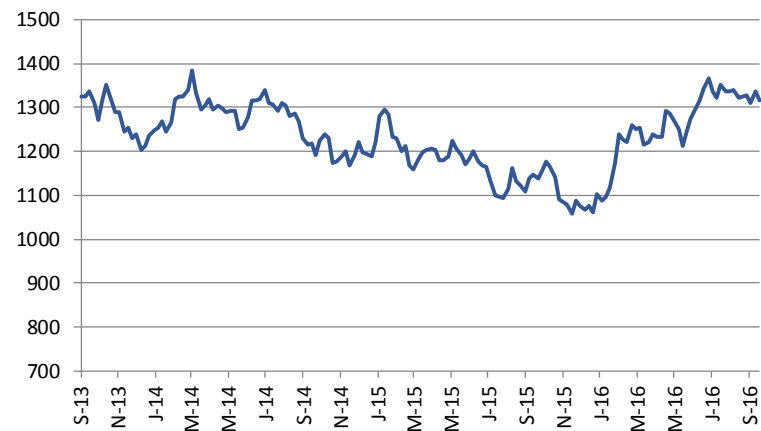


Currencies and Gold

Euro per 1 USD



Gold ounce in USD





Fixed Income

- During the last quarter, high quality government bonds performed heterogeneously: While German (+0.4%) and British government bonds (+0.6%) achieved positive returns, Swiss (-0.7%), US (-0.3%) and Japanese (-0.4%) government bonds lost in value. Emerging market (+3.9%) and High Yield Bonds (+5.1%) showed strong results. Since the start of the year, returns of government bonds (1-10 years) are in positive territory (Switzerland +0.9%, Europe +3.0%, UK +5.7%, USA +3.4%, Japan +1.4%).
- The launch of ETFs (Exchange Traded Funds) on less liquid investments such as leveraged bank loans is a worrying factor in our view. Especially in the 'non-government' segment, liquidity has been disappearing.



Fixed Income

- Our assessment of bond markets has not changed: In light of negative yields to maturity in Swiss Francs and Euros we see slightly negative returns over the coming quarters. Nevertheless, we are holding on to high quality bonds since especially government bonds offer some hedge in the case of a retracement of equity markets. In Pound and USD, yield to maturities are still in positive territory and consequently the situation is less dire.
- We have discovered a Norwegian High Yield Bond Fund with a yield to maturity of 11%. This high yield is the result of the relatively low quality (BB) and the high dependence on oil and gas prices of the portfolio. Due to these high risks, which are comparable to equity investments, we are only considering this product for clients with a high risk tolerance.

Bonds: Slightly overweighted mainly due to zero or negative yield of cash.



Fixed Income

	Sovereign Bonds (10 yrs.)		
	Actual	3 Mo.	12 Mo.
Switzerland	-0.55	-0.50	0.00
Euro Zone (Germany)	-0.09	0.00	0.25
USA	1.63	1.75	2.25
UK	0.73	0.75	1.25
Japan	-0.07	-0.10	0.00
Brazil	11.51	12.00	12.00
Russia	3.78	4.00	4.25
India	6.77	7.00	7.00
China	2.74	3.00	3.00



Fixed Income: Yield to Maturity Government Bonds (All Maturities)

Switzerland



Euro Zone



USA



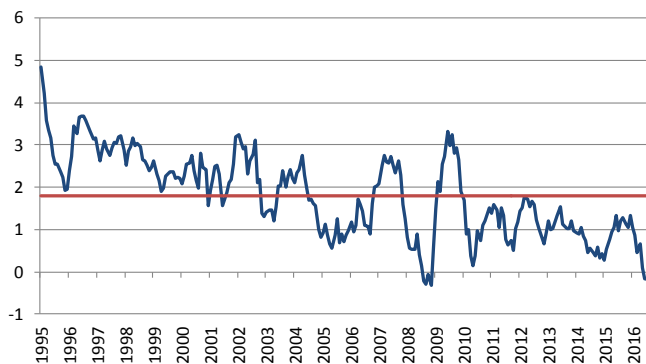
Japan



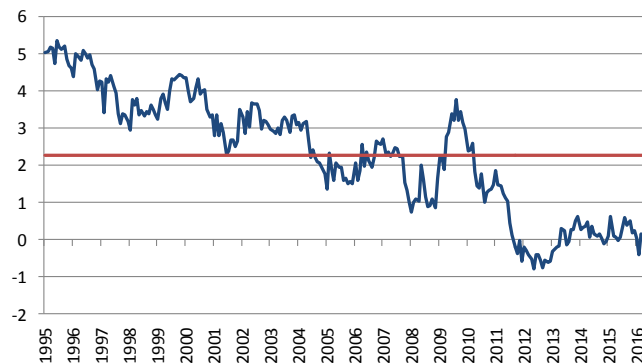


Fixed Income: Government Bonds (All Maturities)

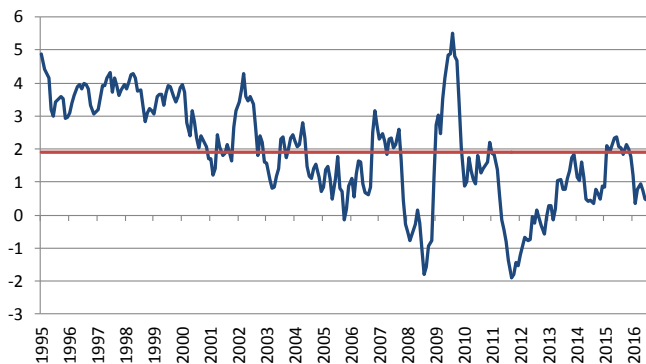
Real Rates Switzerland



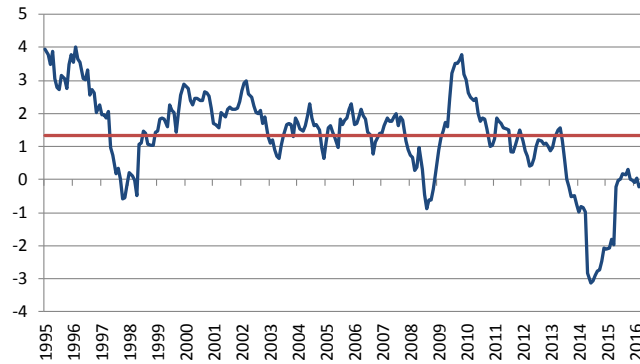
Real Rates Germany



Real Rates USA



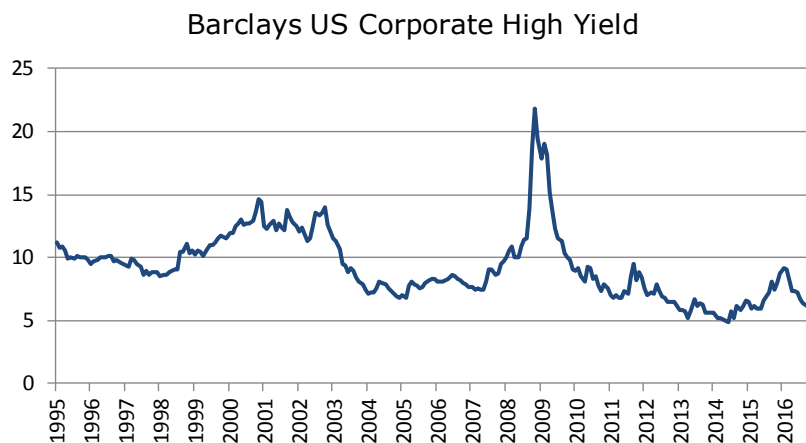
Real Rates Japan



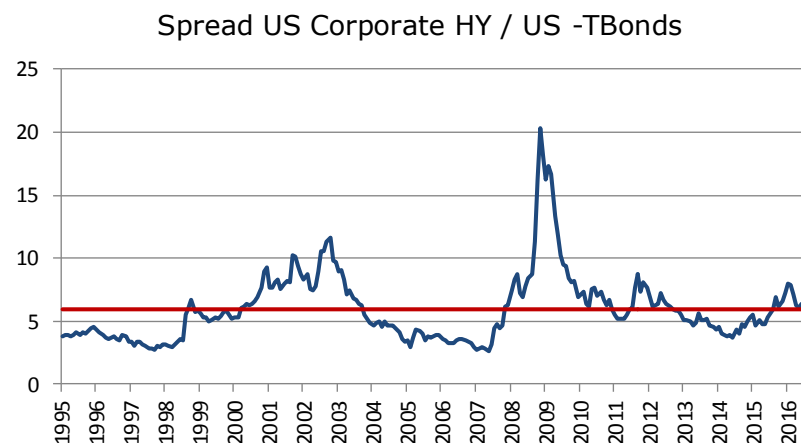


Fixed Income: High Yield

Yield to Maturity



Quality spread

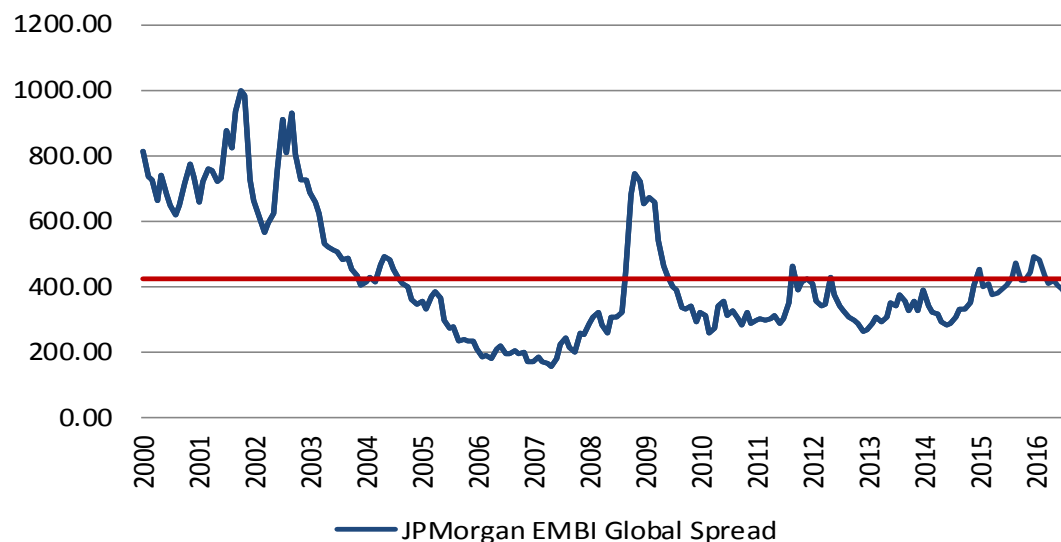


Quality spreads are slightly below their historical average.



Fixed Income: Emerging Market Bonds

Spread of emerging market bonds versus developed markets bonds



Emerging market bond spreads are slightly below the historical averages.



Alternative Investment Strategies (AIS)

Commodities

- Research shows that fully collateralized commodity futures offered the same returns and Sharpe ratio as equities between July 1959 and December 2004. At the same time, commodity futures returns were negatively correlated with equity and bond returns. In addition, commodity futures are positively correlated with inflation, unexpected inflation and changes in expected inflation.

(Gorton and Rouwenhorst. 2004. 'Facts and Fantasies about Commodity Futures')

- After a technical rebound during the 2nd quarter, the broad commodity index continued its descent (-3.9%). Gold (-0.5%) and oil (-0.2%) hardly moved. Year to date, commodities are still up 8.7%, which is also the case for its constituents oil (+29.3%) and gold (+23.9%).



Alternative Investment Strategies (AIS)

- Within commodities we are concentrating on precious metals, mainly gold. Balance sheets of central banks have increased dramatically in the aftermath of the financial crisis (see page 17). The inability of central banks to normalize the situation could lead to a loss of trust in the fiat money system. In other words, we see gold as some hedge against this risk.

Commodities: Neutral weighting and concentration on gold



Alternative Investment Strategies (AIS)

Hedge Funds

- Research shows that hedge funds outperformed equities (years 1995-2009) by 3% per year after adjustments for costs, survivorship bias and backfill bias. At the same time, hedge funds offered interesting diversification advantages.

(Ibbotson, Chen and Zhu. 2011. 'The ABCs of Hedge Funds: Alphas, Betas, and Cots'. Financial Analysts Journal, vol. 67, no.1, 15-25)

- Within our AIS-Quota (Alternative Investment Strategies), hedge funds play the largest role and we are focusing on funds, which follow a market neutral strategy.

Hedge Funds: Neutral weighting

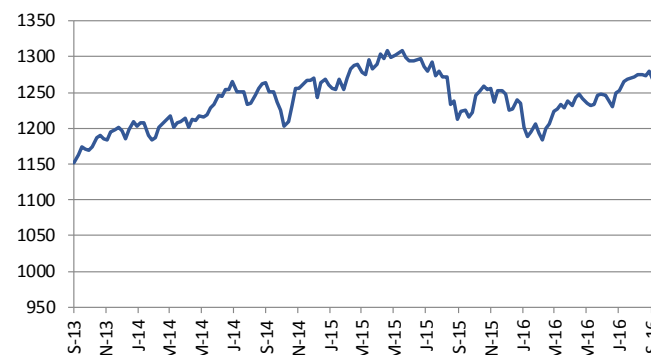


Alternative Investment Strategies (AIS)

Bloomberg Commodity Index Total Return



GS ART (Hedge Funds)



Oil (West Texas Intermediate)





Equities: Overview

- Similar to the 2nd quarter, equity markets benefited from a further fall of credit spreads and low inflation. Developed countries rose by 5.4% during the last quarter, while emerging markets soared even 8.9%. Industry wise, technology and basic industries were the big outperformers. Year to date, developed (+6.6%) as well as emerging markets (+15.7%) are up. Nevertheless, performance was rather mixed and especially Switzerland (-2.3%), Germany (-2.2%), Europe (-5.7%) and Japan (-12.8%) have disappointed so far.
- With regards to financial risks, we see primarily the following: Rising quality spreads (yield differential of bonds with varying quality), valuation compression due to higher interest rates, pressure on profit margins.



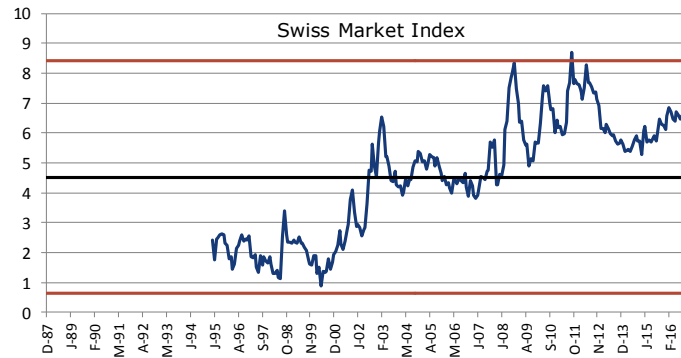
Equities: Overview

- Considering the lack of earnings growth and the prospects of rising interest rates in the US, we are expecting equity markets to continue to trade sideways. In addition to economic challenges, we see political risks in the form of US elections, implementation of the Brexit, refugees in Europe and the claim to power of Russian and China. Furthermore, 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 (ItalExit). Significantly higher equity prices in the coming months would require additional extreme moves by central banks.

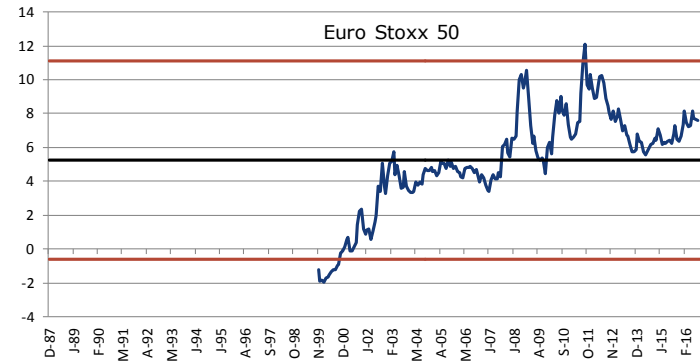
Equities: (Slightly) underweighted



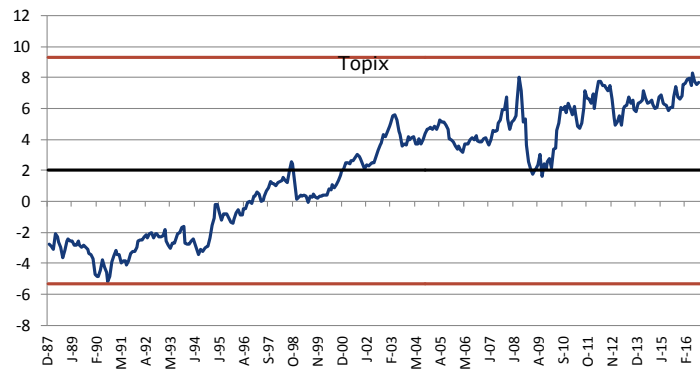
Equities: Valuation According to Fed-Model



cheap
↑
↓
expensive

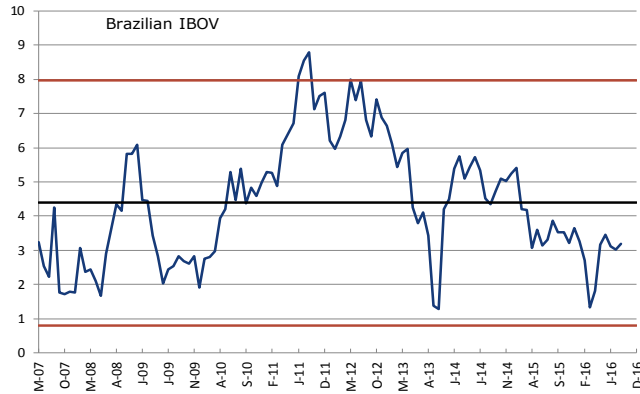


cheap
↑
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expensive

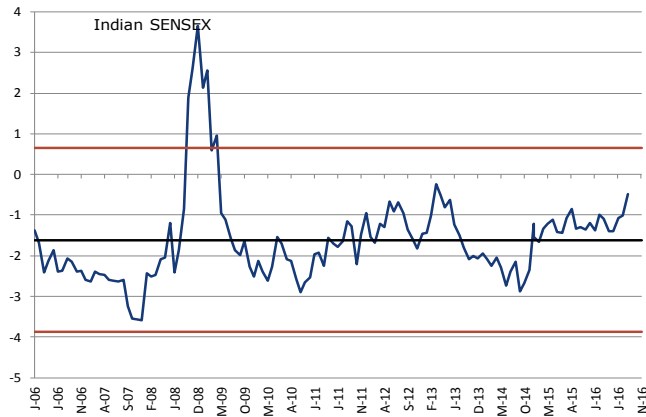
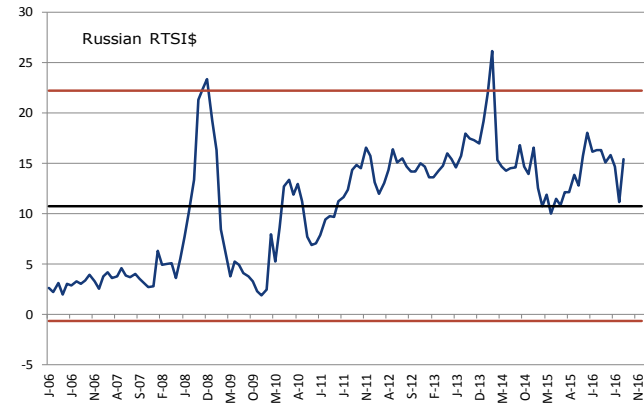




Equities: Valuation According to Fed-Model



cheap
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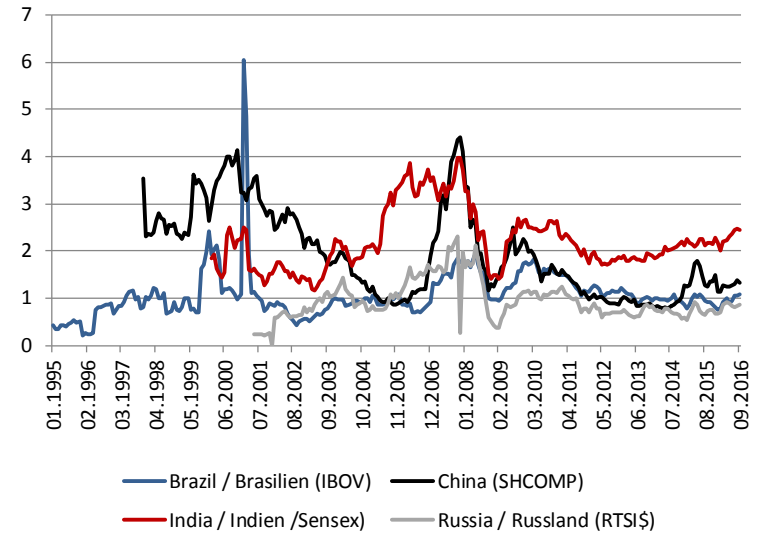
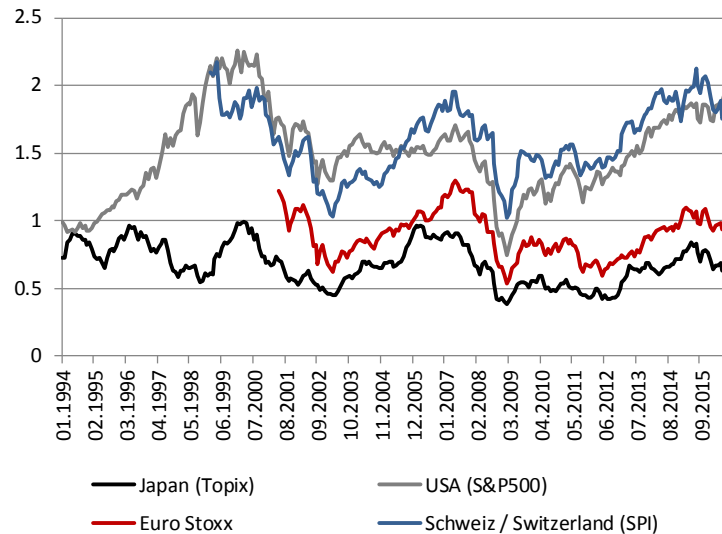


cheap
↑
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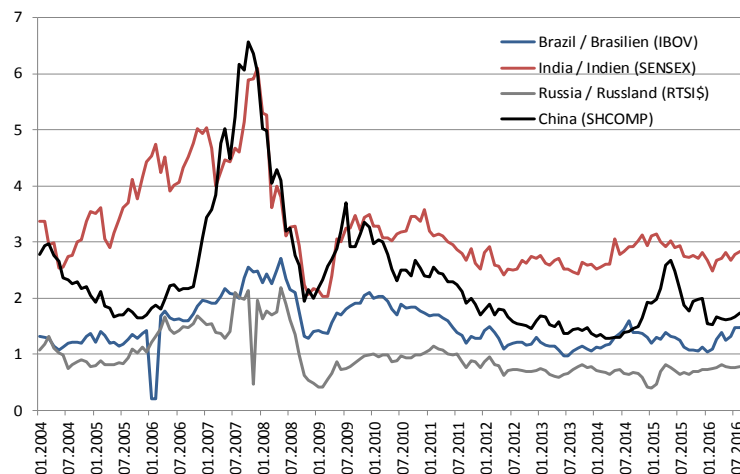
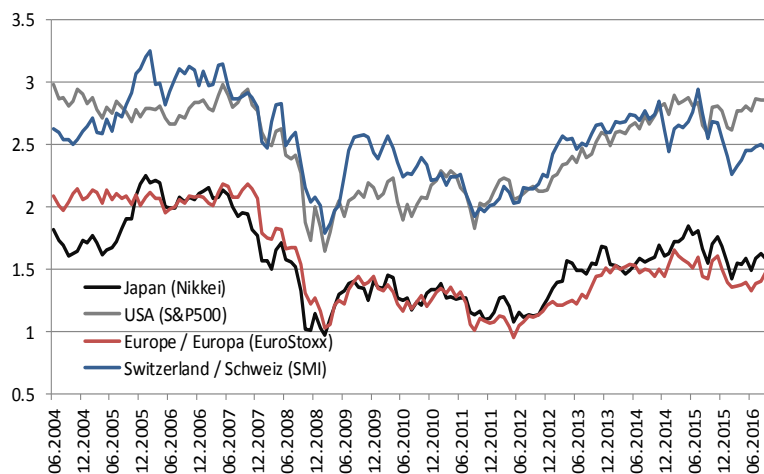


Equities: Valuation by Price/Sales





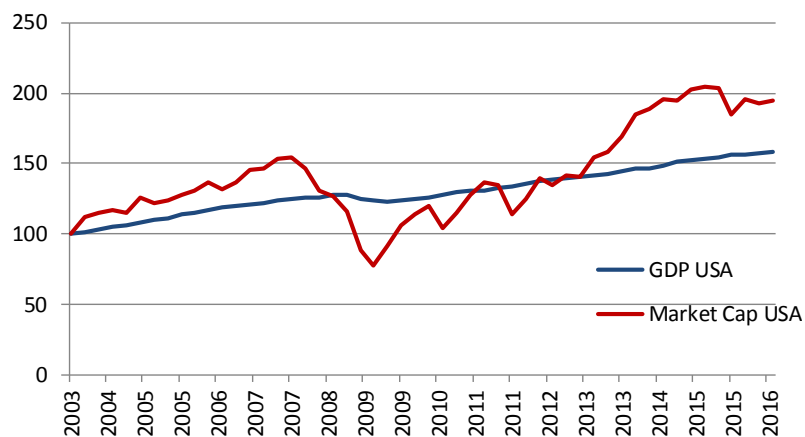
Equities: Valuation by Price/Book



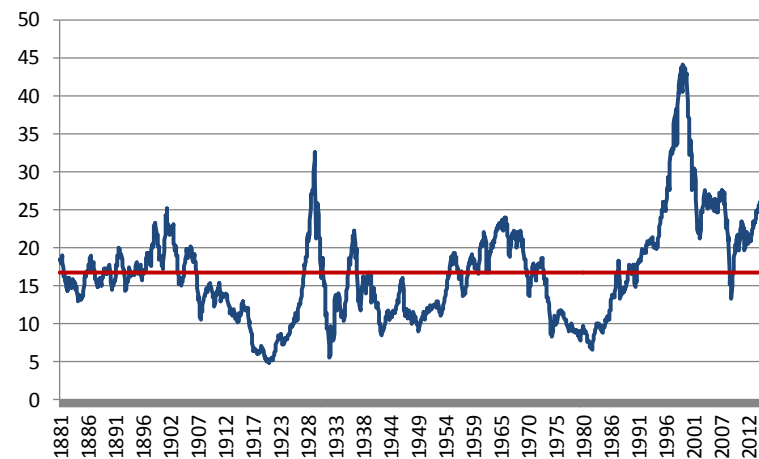


Equities: Valuation of US Market

Market Capitalization and GDP



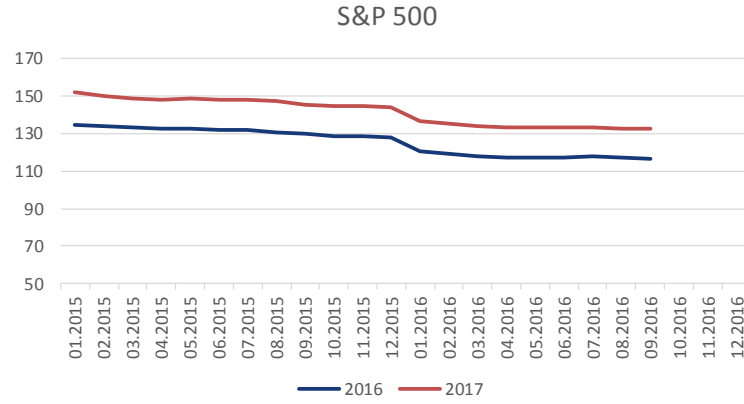
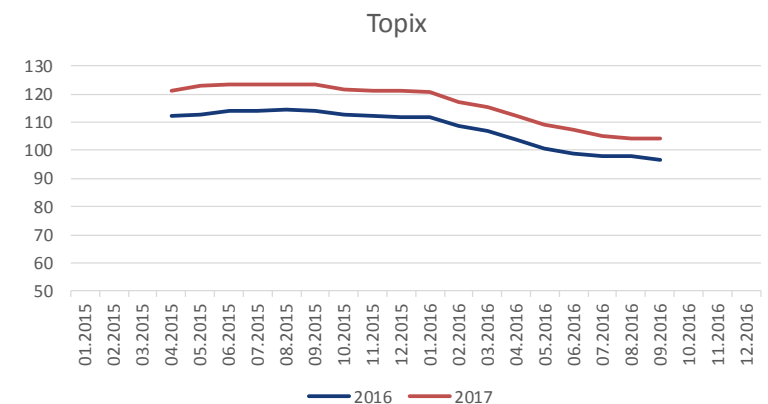
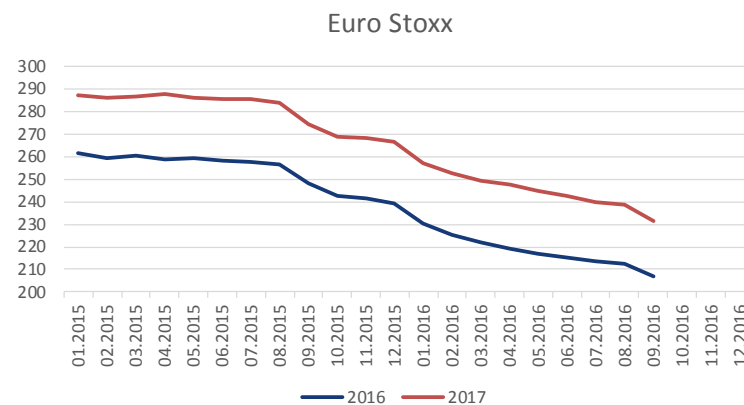
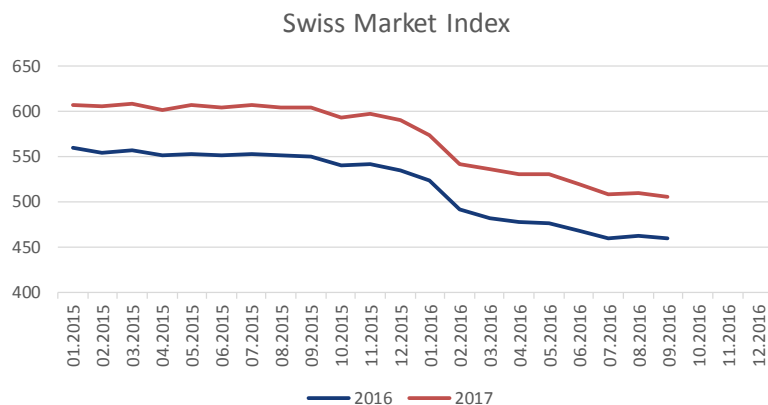
Shiller PE Ratio *



* PE based on real EPS over 10 year period



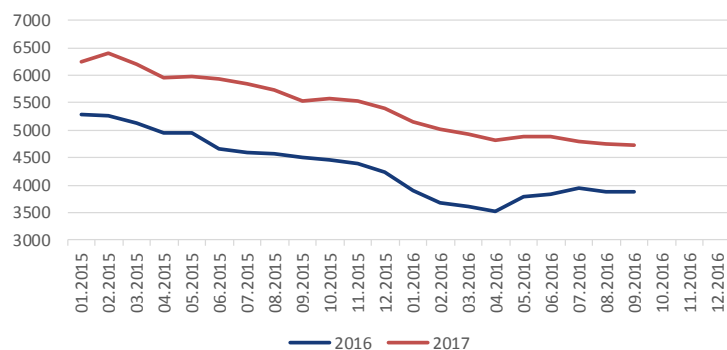
Equities: Earnings-Revisions



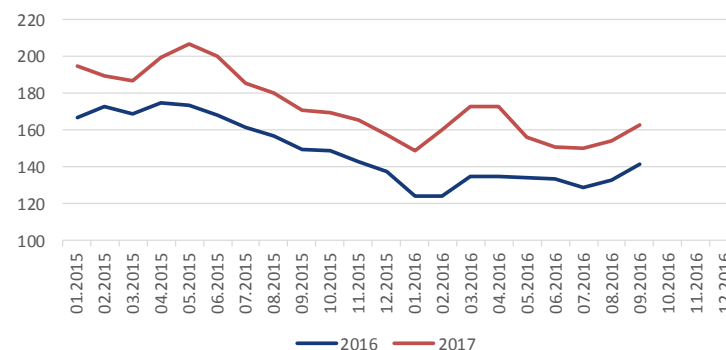


Equities: Earnings-Revisions

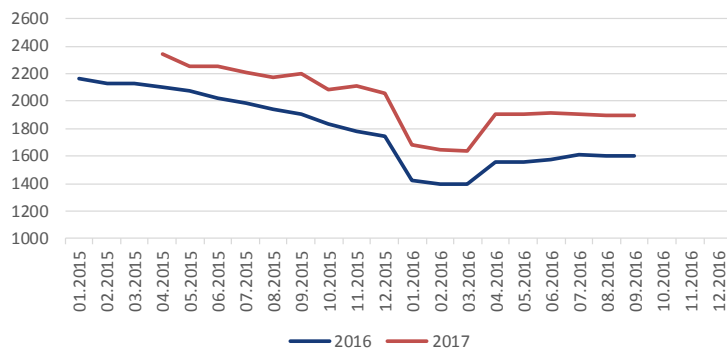
Brazil Bovespa



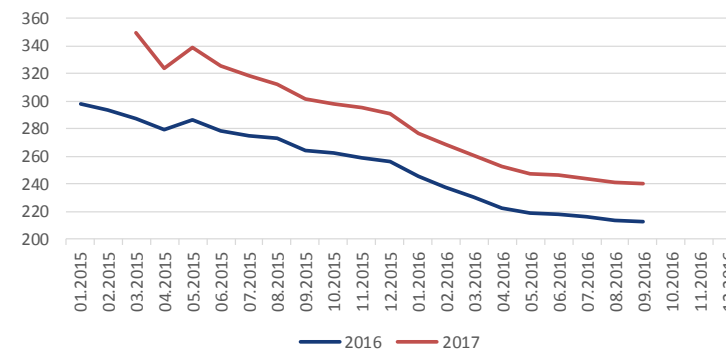
Russian Traded Index \$



Bombay Sensex



Shanghai Composite





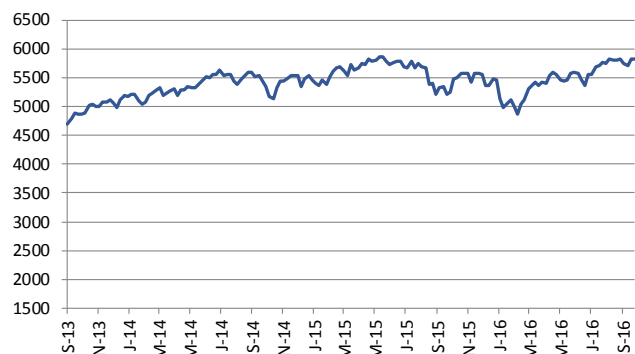
Equities: Forecast

	Equities		
	Actual	3 Mo.	12 Mo.
Switzerland (SPI)	8'918	8'850	9'200
Germany (DAX)	10'511	10'500	11'000
Euro Zone (Euro Stoxx 50)	5'868	5'850	6'000
UK (FTSE 100)	6'984	6'800	6'900
USA (S&P500)	2'161	2'150	2'200
Japan (Topix)	16'689	16'400	16'700
Brazil (Bovespa)	59'461	57'500	58'000
Russia (MSCI Russia)	483	470	500
India (Sensex)	28'300	27'500	29'000
China (CSI Total Return)	2'660	2'700	2'900



Equities: Developed and Emerging Markets

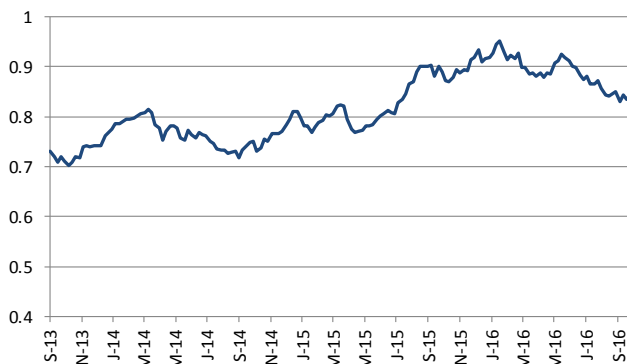
Dow Jones Developed Markets



Dow Jones Emerging Markets



Relative Performance



Outperformance Developed Markets



Outperformance Emerging Markets



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