



**LimmatWealth**

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# World Wide Outlook

1st quarter 2017

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## Important Events

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- Contrary to most forecasts, the Republican Donald Trump won the **US elections**. After some turbulences, markets stabilized relatively quickly and started to price in the topics, which Trump had mentioned during his campaign: Lower taxes, less regulation and higher government spending financed by debt. Consequently, equities profited from the expectations of lower taxes and the finance sector outperformed heavily in anticipation of less regulation. Higher government spending and more debt led to higher inflation and interest rate expectations and consequently investors dumped bonds.
- In the **Euro Zone**, the Italian referendum took center stage. The rejection led to the resignation of Minister President Matteo Renzi.



## Growth

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- Mainly due to the Brexit, the IMF (International Monetary Fund) lowered its growth forecast for the **global economy** by 0.1% for 2016 and 2017. After 3.2% in 2015 the IMF sees an expansion of **3.1% in 2016 and 3.4% in 2017**. The IMF sees many economic and political risks.



## Growth

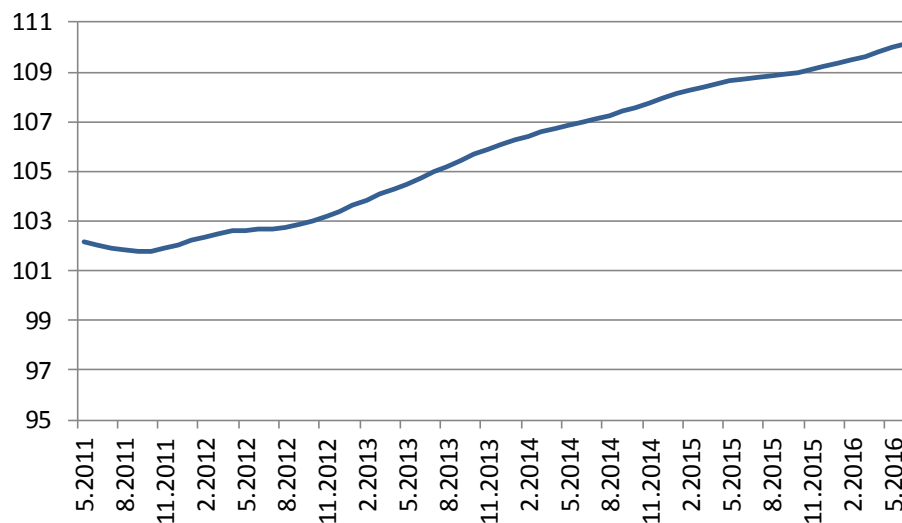
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- In **advanced economies**, the IMF sees more or less constant growth of slightly below 2% (2015: 2.1%, **2016: 1.6%, 2017: 1.8%**). Monetary policy has to remain accommodative. Pressing on with structural reforms remains one of the key necessities for advanced as well as emerging countries.
- Growth in emerging markets is forecasted to rise from 4.0% in 2015 to **4.2% 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)

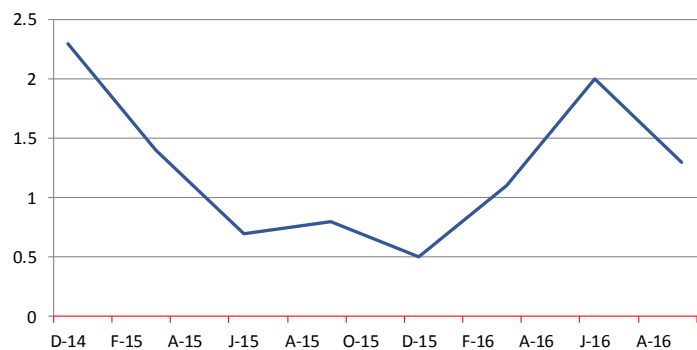
	GDP 13	GDP 14	GDP 15	GDP 16	GDP 17
Switzerland	1.8	1.9	0.8	1.0	1.3
Germany	0.6	1.6	1.5	1.7	1.4
Euro Zone	-0.3	1.1	2.0	1.7	1.5
UK	1.9	3.1	2.2	1.8	1.1
USA	1.7	2.4	2.6	1.6	2.2
Japan	1.4	0.0	0.5	0.5	0.6
Brazil	3.0	0.1	-3.8	-3.3	0.5
Russia	1.3	0.7	-3.7	-0.8	1.1
India	6.6	7.2	7.6	7.6	7.6
China	7.8	7.3	6.9	6.6	6.2

Source: IMF & Limmat Wealth

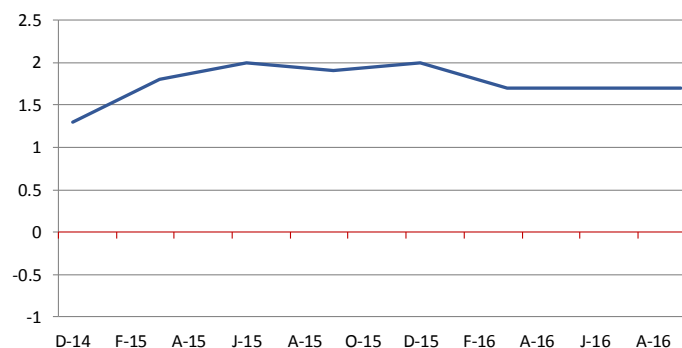


# Growth

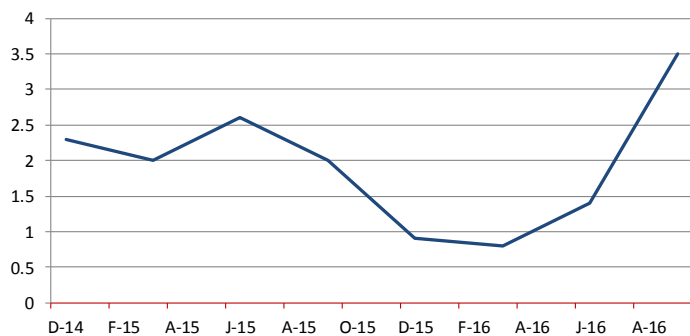
### GDP-Growth Switzerland



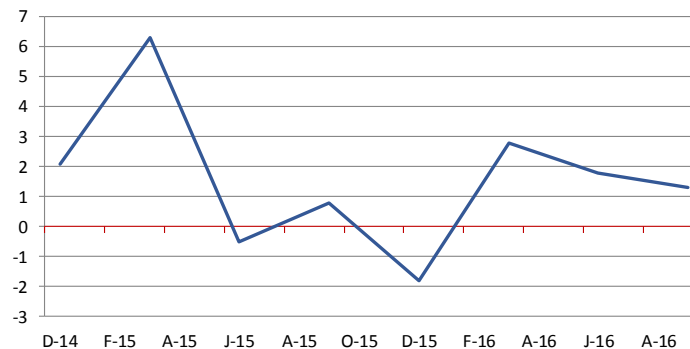
### GDP-Growth Euro Zone



### GDP-Growth USA



### GDP-Growth Japan

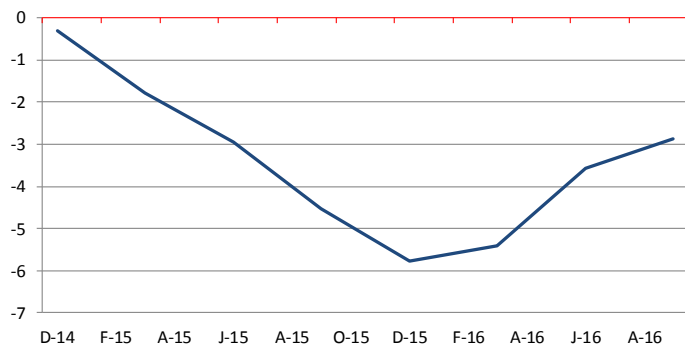




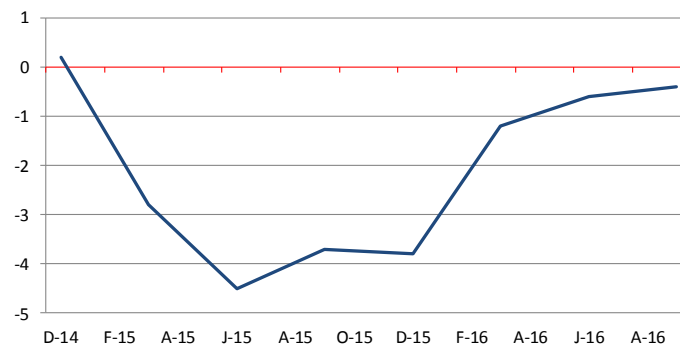


# Growth

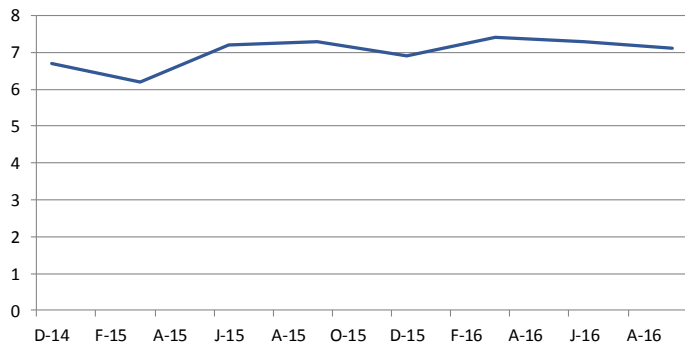
### GDP-Growth Brazil



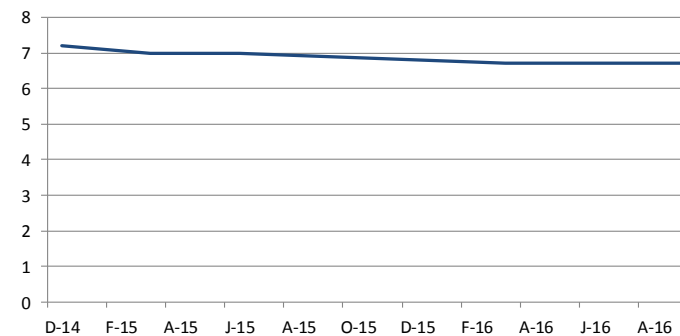
### GDP-Growth Russia



### GDP-Growth India



### GDP-Growth China





# Inflation

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- By historical standards, inflation will remain low in **advanced economies**: After 0.3% in 2015 the IMF sees an increase to **0.8% in 2016 and 1.7% in 2017**.
- **Emerging and developing countries** are in disinflation: After 4.7% in 2015, inflation will decline to **4.5% (2016)** and **4.4% (2017)**.



# Inflation

## Consumer Price Inflation (CPI)

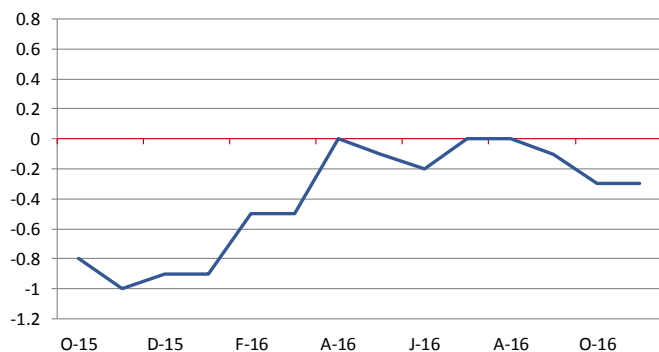
	CPI 13	CPI 14	CPI 15	CPI 16	CPI 17
Switzerland	-0.2	0.0	-1.1	-0.4	0.0
Germany	1.6	0.8	0.1	0.4	1.5
Euro Zone	1.3	0.4	0.0	0.3	1.1
UK	2.6	1.5	0.1	0.7	2.5
USA	1.4	1.4	0.3	1.2	2.3
Japan	0.4	2.7	0.8	-0.2	0.5
Brazil	6.2	6.3	9.0	9.0	5.4
Russia	6.8	7.8	15.5	7.2	5.0
India	9.4	5.9	4.9	5.5	5.2
China	2.6	2.0	1.4	2.1	2.3

Source: IMF & Limmat Wealth

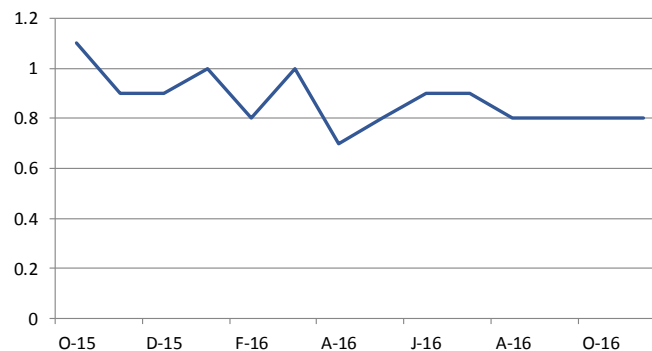


# Inflation

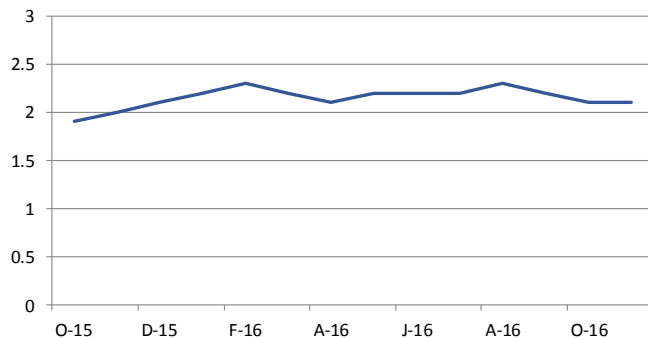
## Inflation Switzerland (core)



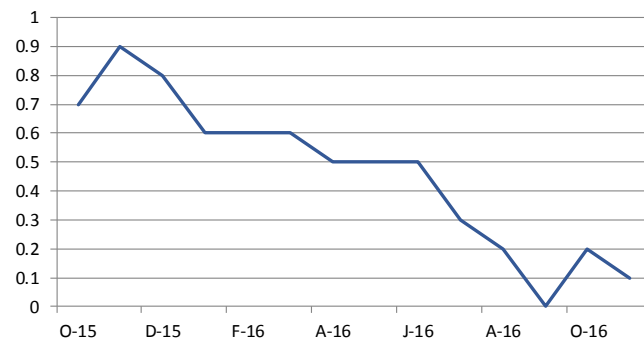
## Inflation Euro Zone (core)



## Inflation USA (core)



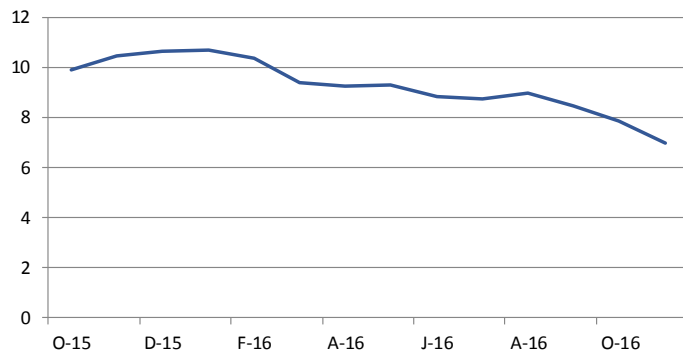
## Inflation Japan (core)



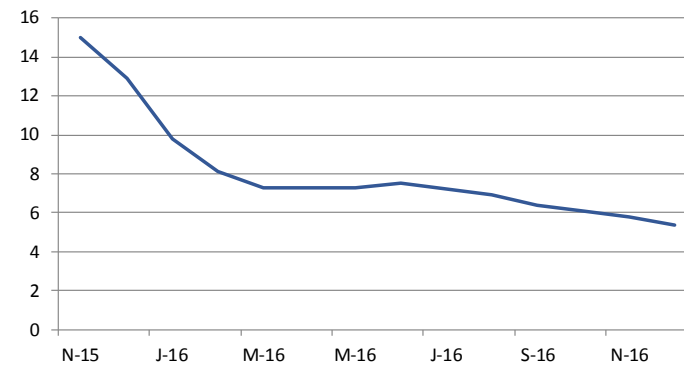


# Inflation

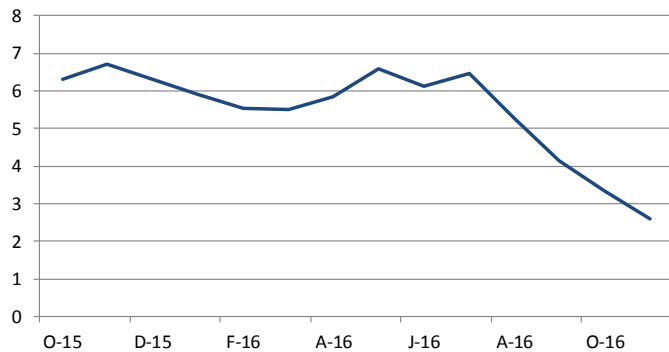
## Inflation Brazil



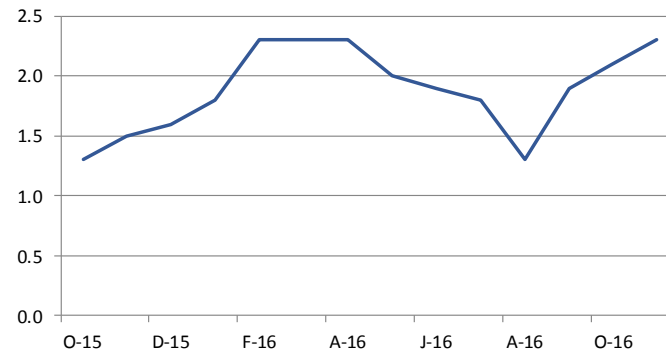
## Inflation Russia



## Inflation India



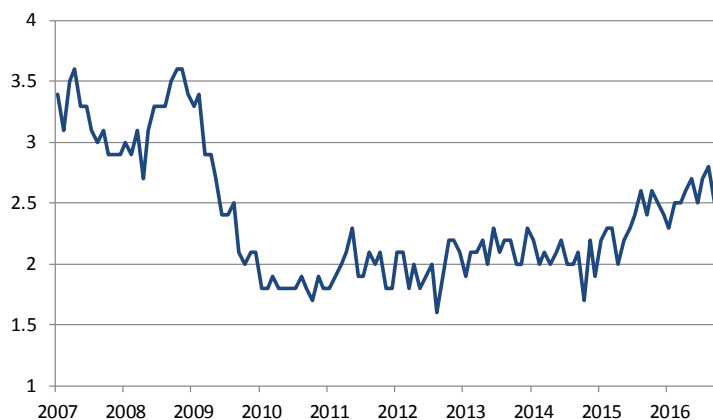
## Inflation China





# Inflation USA

USA:  
Yearly % change average hourly earnings



USA:  
Capacity Utilization %



In contrast to the low capacity utilization rate, rising wages point towards higher inflation potential.



## Monetary Policy

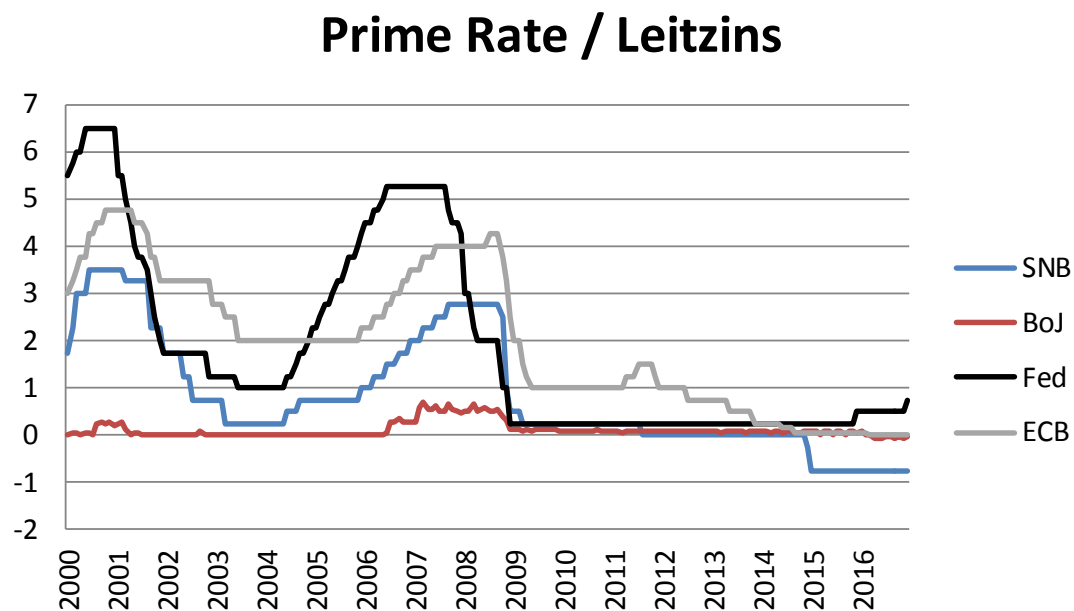
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- The **European Central Bank** announced the extension of its asset-purchase scheme through the end of 2017 but reduced monthly purchases from Euro 80bn to Euro 60bn starting in April.
- As expected, the **US** Central Bank hiked rates by 0.25% to the new target range of 0.5%-0.75%. In 2017, another three steps of 0.25% each have to be expected, which would result in a level of about 1.5% in one years' time.
- 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 ...



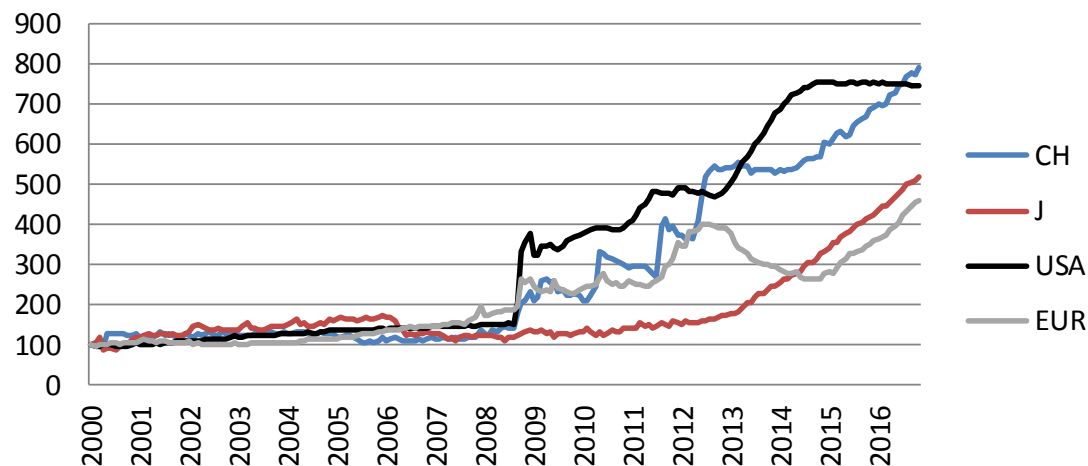




# Monetary Policy

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

## Central Bank Balance Sheets / Zentralbanken Bilanzen





# Monetary Policy

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... 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	9
China / China	15
Norwegen / Norway	32
Schweiz / Switzerland	34
Neuseeland / New Zealand	35
Schweden / Sweden	43
Australien / Australia	44
Indien / India	52
Finnland / Finland	63
Niederlande / Netherlands	65
Deutschland / Germany	71
USA / United States	74
Grossbritannien / United Kingdom	89
Euro Zone / Eurozone	90
Frankreich / France	96
Kanada / Canada	99
Spanien / Spain	99
Irland / Ireland	101
Singapur / Singapore	105
Belgien / Belgium	106
Portugal / Portugal	129
Italien / Italy	133
Griechenland / Greece	177
Japan / Japan	230



# Indebtedness

## Budget Deficit / Surplus in % of GDP

Source: Bloomberg

Griechenland / Greece	-7.5
Spanien / Spain	-5.1
Japan / Japan	-5.0
Portugal / Portugal	-4.4
Grossbritannien / United Kingdom	-4.3
Indien / India	-4.2
Frankreich / France	-3.5
China / China	-3.4
USA / United States	-3.1
Finnland / Finland	-2.8
Italien / Italy	-2.6
Belgien / Belgium	-2.5
Euro Zone / Eurozone	-2.1
Irland / Ireland	-1.9
Niederlande / Netherlands	-1.9
Kanada / Canada	-1.3
Australien / Australia	-0.9
Schweiz / Switzerland	-0.2
Schweden / Sweden	0.2
Neuseeland / New Zealand	0.0
Deutschland / Germany	0.7
Russland / Russia	0.8
Norwegen / Norway	5.4
Singapur / Singapore	8.6



## Currencies and Gold

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- The US interest rate hike in December led to a stronger USD during the 4<sup>th</sup> quarter. According to the DXY-Index, the USD rose 7% (Year 2017 +3.6%). The strength was broad-based and most currencies lost in comparison to the USD (Swiss Franc -5%, Euro -6.6%, Yen -13%). After a strong gain of more than 10% since early May 2016 (DXY-Index), we see a consolidation phase. Afterwards, a slightly weaker green back is anticipated in comparison to the Euro, as the American currency is rather expensive based on its purchasing power parity and the current account remains negative. This slight weakness will also occur versus the Swiss Franc, since we expect the Swiss Franc to Euro relation to remain unchanged.



## Currencies and Gold

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- Gold was burdened by rising US interest rates and declined by 12% during the 4<sup>th</sup> quarter. Nevertheless, the yellow metal closed the year with an increase in the order of 8.6%. 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, 3<sup>rd</sup> quarter gold demand decreased by 10% to 992.8 tons year-over-year. Strong demand by investors (+103.3 tons) was more than offset by weak jewellery demand (-128.5 tons) and central bank disinvestments (-86.3 tons). Supply rose 4% to 1'172.7 tons.



## Currencies and Gold

	Currencies / Gold		
	Actual	3 Mo.	12 Mo.
USD/CHF	1.03	1.02	0.97
EUR/USD	1.04	1.05	1.10
USD/Yen	118	115	110
GBP/USD	1.22	1.23	1.30
USD/BRL	3.26	3.25	3.50
USD/Rubel	60.68	65.00	70.00
USD/INR	68.33	67.00	70.00
USD/CNY	6.96	7.00	7.30
EUR/CHF	1.07	1.07	1.07
Gold (USD)	1156	1150	1200



# Currencies and Gold

	Current Account in % of GDP
Australia	-4.8
Middle East	-4.7
Turkey	-4.5
United Kingdom	-4.3
Latin America	-3.6
Canada	-3.4
Brazil	-3.2
USA	-2.6
India	-1.1
G10	-0.2
EMEA	0.4
BRICS	1.9
Europe	2.8
China	3.0
Euro Zone	3.1
Japan	3.1
Norway	3.3
Asia	3.4
Russia	5.2
Sweden	5.4
Denmark	7.1
Switzerland	11.5

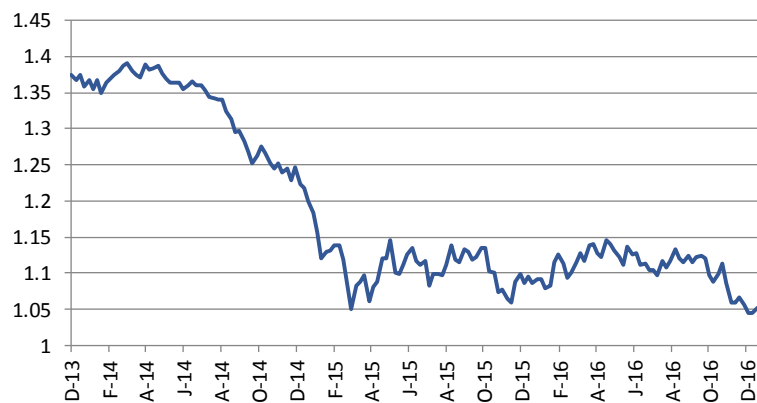
Current Account =  
+ Balance of trade of goods  
+ balance of trade of services  
+ net factor income  
+ net transfer income.





# Currencies and Gold

## Euro per 1 USD



## Gold ounce in USD





## Fixed Income

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- During the **4<sup>th</sup> quarter**, interest rates rose practically worldwide and government bonds lost in value. The largest losses (maturities 1-10 years) resulted in the US (-2.2%) but also European government bonds could not decorrelate (Switzerland -1.1%, Germany -0.7%, UK -1.1%). Emerging markets bond indices dropped even 4.4%. As usual, high yield bonds showed a high correlation to equities and returned 1.4%.
- Looking at the whole year 2017 (maturities 1-10 years), with the exception of Switzerland (-0.2%), government bonds generated positive total returns (Germany +2%, USA +1.1%, UK +4.5%). Equity-like returns were generated by emerging markets (+10%) and high yield bonds (+15%).
- 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

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- In the US, we forecast rising real interest rates and consequently increase our forecast for 10year government bonds yields. As of the end of 2017 we see 3% at the long end. The yield difference of the US to Europe has already reached a very high level by historical standards. Therefore, we don't expect a further widening of these yield-spreads. This means that the increase of interest rates in Europe will be similar in size to the US. Accordingly, our interest rate expectations for Europe also rise (Switzerland 0.25%, Germany 0.75%, UK 1.75% etc.).
- The outlook for bonds remains murky and investments are mainly based on diversification reasons. In the meantime, USD short-term investments have – although small – positive returns, which leads us to reduce bonds in USD portfolios in favor of cash holdings.

**Bonds:** Slightly overweighted (except USD-Portfolios) mainly due to zero or negative yield of cash.



## Fixed Income

	Sovereign Bonds (10 yrs.)		
	Actual	3 Mo.	12 Mo.
Switzerland	-0.11	0.00	0.25
Euro Zone (Germany)	0.24	0.50	0.75
USA	2.50	2.50	3.00
UK	1.32	1.50	1.75
Japan	0.05	0.00	0.25
Brazil	11.24	12.00	12.00
Russia	4.46	4.50	4.25
India	6.45	6.50	6.50
China	3.12	3.25	3.25



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

### Switzerland



### Euro Zone



### USA



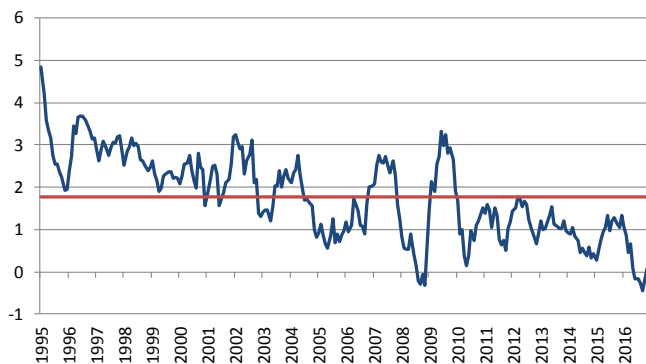
### Japan



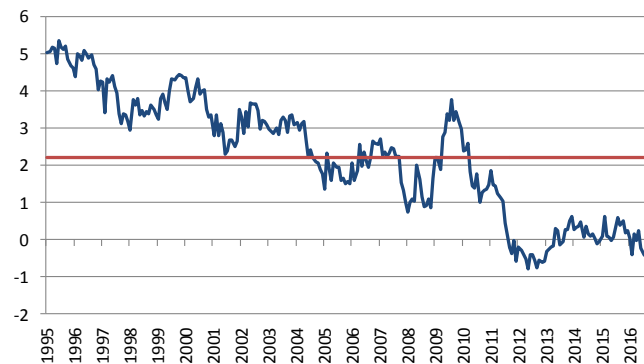


# Fixed Income: Government Bonds (All Maturities)

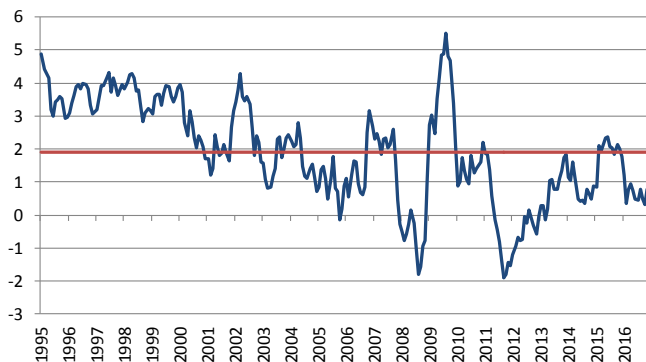
### Real Rates Switzerland



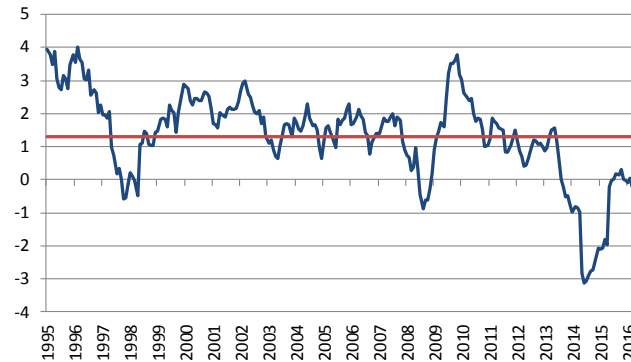
### Real Rates Germany



### Real Rates USA



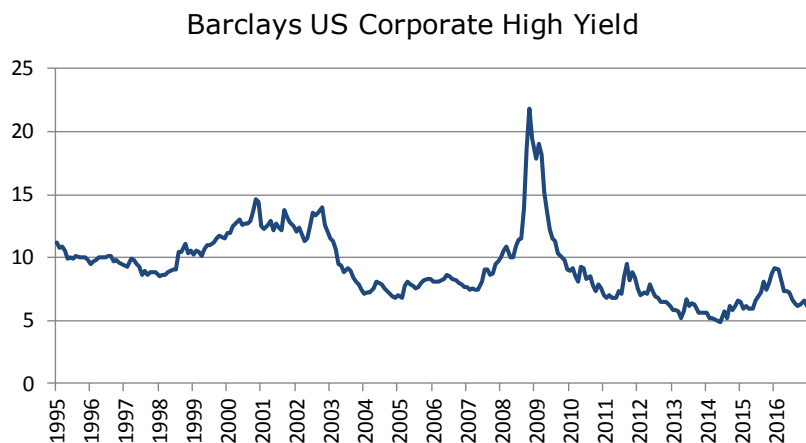
### Real Rates Japan



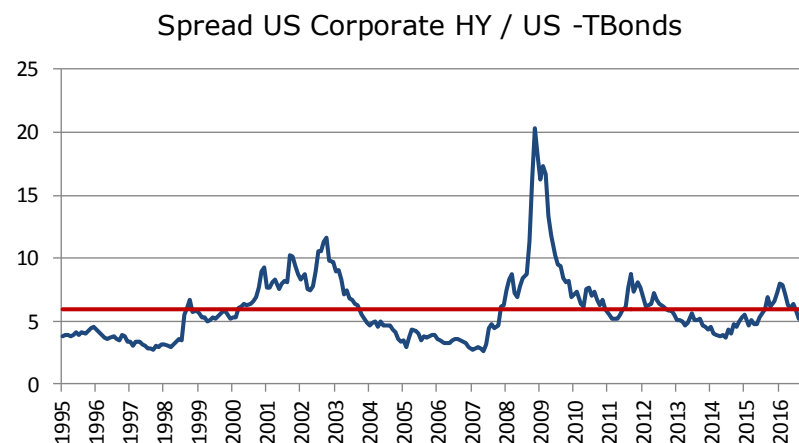


# Fixed Income: High Yield

## Yield to Maturity



## Quality spread

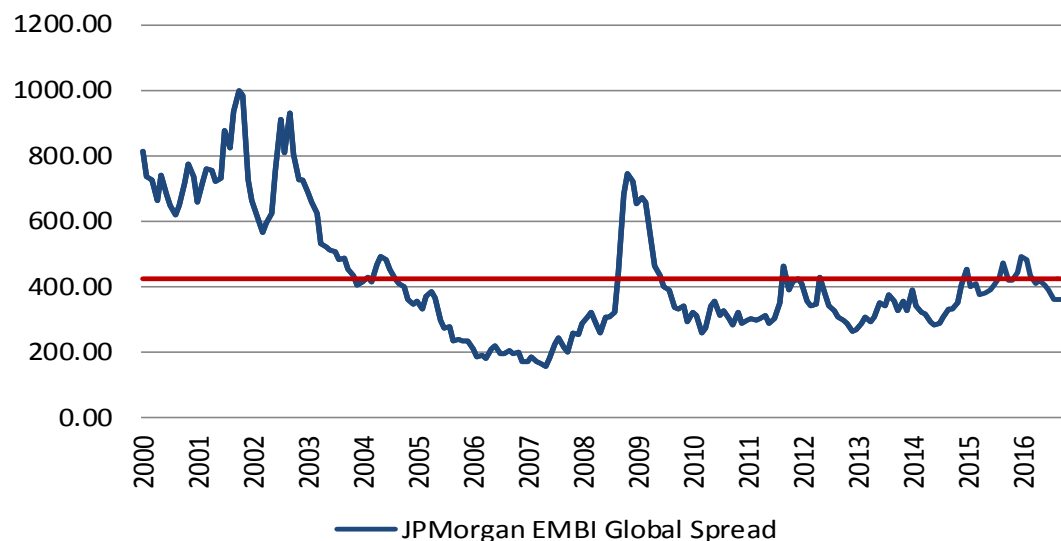


Quality spreads are slightly below their historical average.



## 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)

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## 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')

- Despite a weak gold price (-12%), the broad commodity index rose 2.7% during the 4<sup>th</sup> quarter thanks to an continuing rally of oil prices (11.4%). For the whole year 2017, gold (+8.6%) as well as oil (+45%) rose. The commodity index advanced by 12%.



## Alternative Investment Strategies (AIS)

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- 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)

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## 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

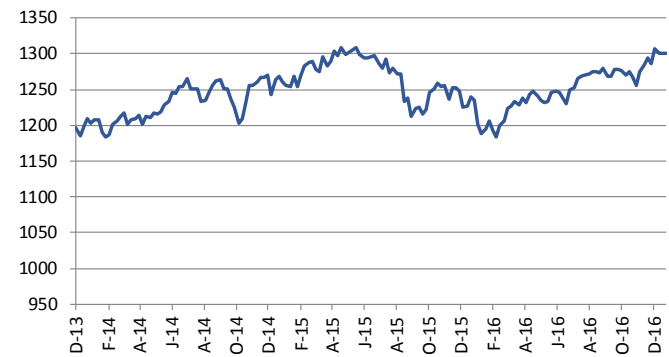


# Alternative Investment Strategies (AIS)

### Bloomberg Commodity Index Total Return



### GS ART (Hedge Funds)



### Oil (West Texas Intermediate)





## Equities: Overview

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- Equities have continued to benefit from a further fall of credit spreads and low inflation. Developed countries rose by 5.4% during the 4<sup>th</sup> quarter, while emerging markets were burdened by fears of a further strengthening of the Dollar and protectionist measures (-3.7%). In 2017, industrial (+8.6%) as well as emerging (+11.4%) markets performed nicely. On a country level large differences were observable and especially the Swiss market disappointed (SPI -1.4%).
- Currently, we see a lack of concern by investors (low volatility, bullish investor sentiment, major US markets at all-time highs), which makes us wary. In addition to the usual political (e.g. Middle East) and economic (e.g. Chinese debt and growth) risks, elections will be held in Holland, France and Germany this year. If populist parties gain share, this would be negative for



## Equities: Overview

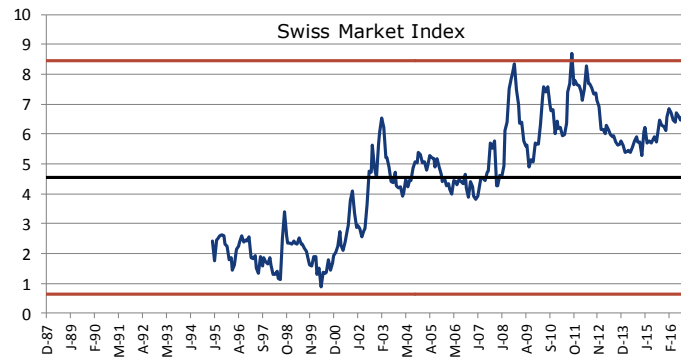
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equities mainly due to rising fears of protectionism. In the US, monetary policy will become more restrictive, which in the past was followed by low returns. During the first quarter, investors will find out that even Donald Trump is not able to elude the economic and political realities. The 'Trump euphoria' will give way to more realistic expectations, which will result in lower equity prices. On the positive side, we see rising earnings in 2017. Earnings have declined since September 2014 and this turnaround will support equity markets. In a nutshell, we are of the opinion that currently equity allocations should not be increased. Holding some cash makes sense in order to be able to increase the equity allocation after a correction. We remain slightly underweighted in equities.

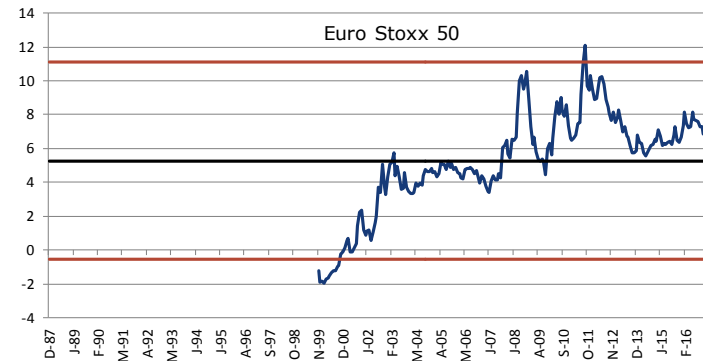
Equities: (Slightly) underweighted



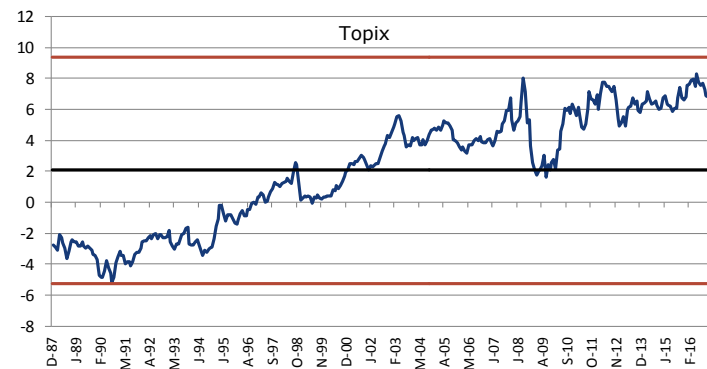
# Equities: Valuation According to Fed-Model



cheap  
↑  
↓  
expensive

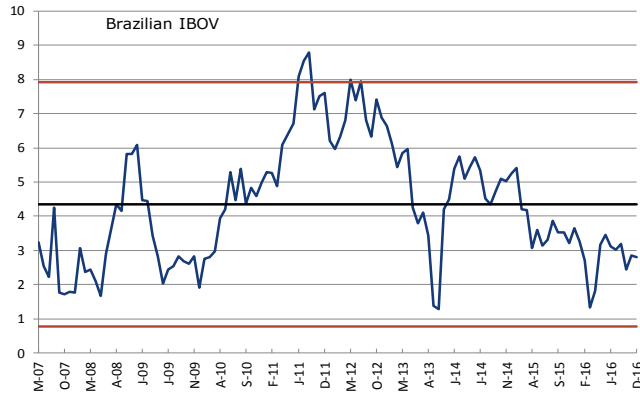


cheap  
↑  
↓  
expensive

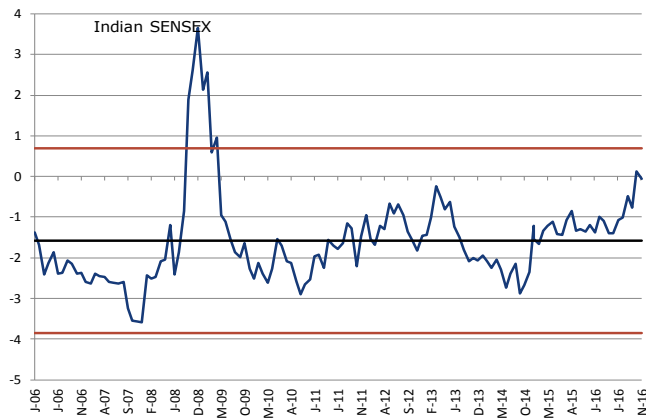
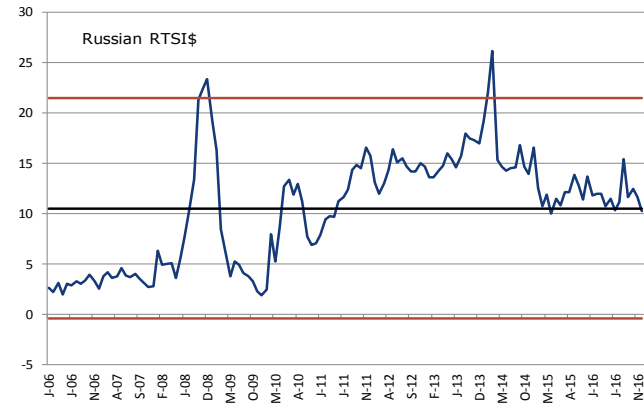




# Equities: Valuation According to Fed-Model



cheap  
↑  
↓  
expensive



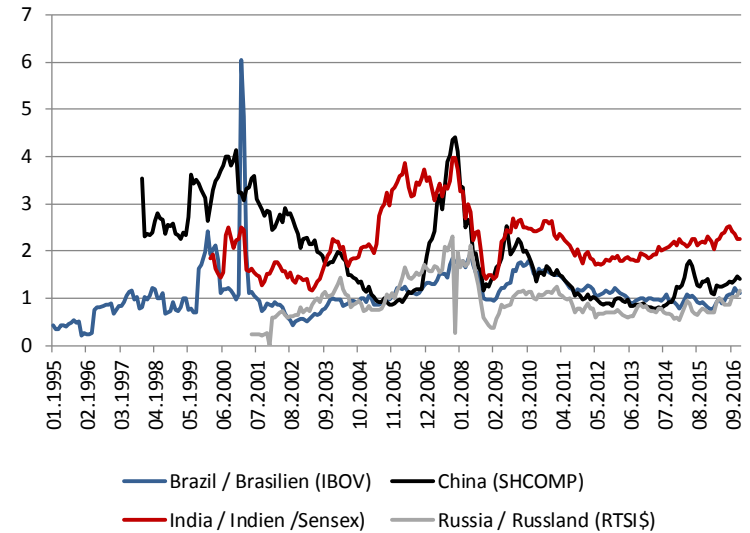
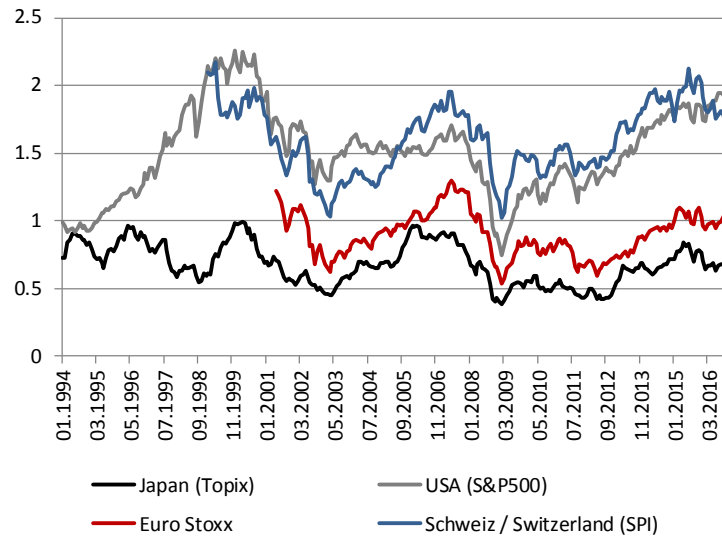
cheap  
↑  
↓  
expensive





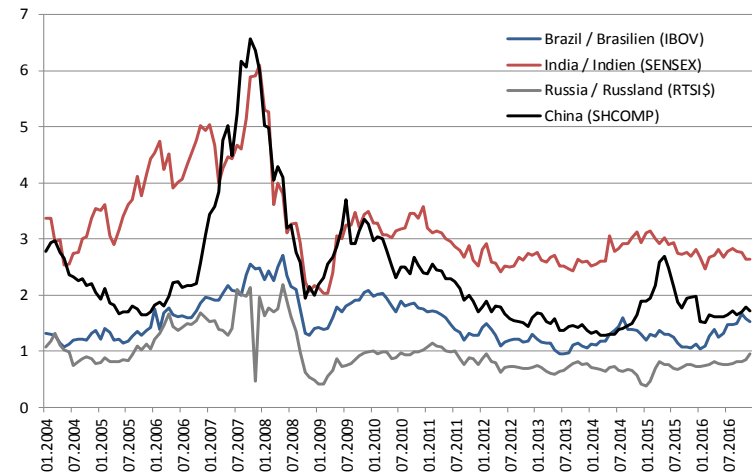
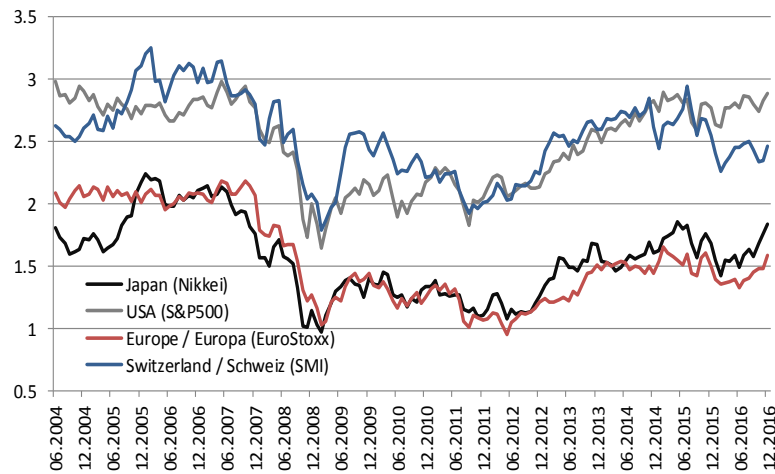


# Equities: Valuation by Price/Sales





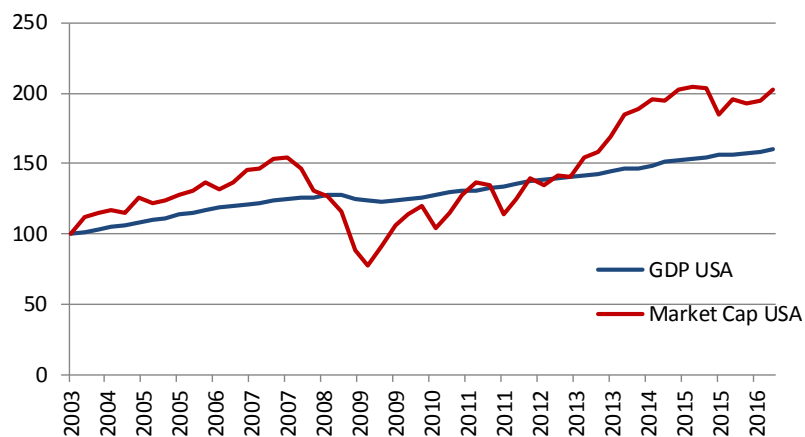
# Equities: Valuation by Price/Book



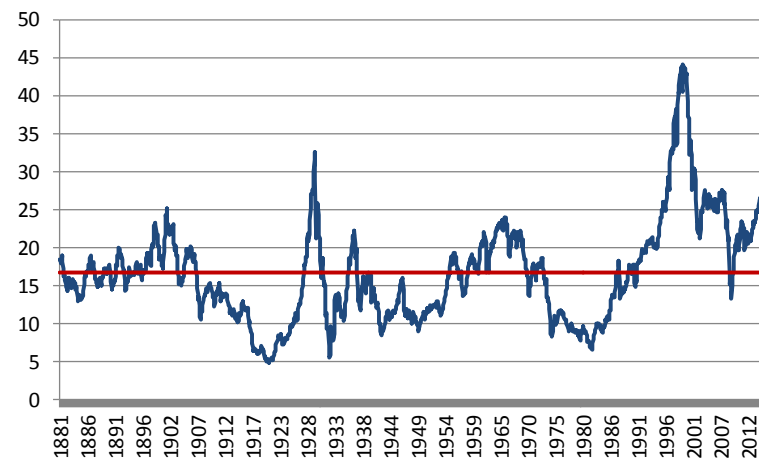


# Equities: Valuation of US Market

## Market Capitalization and GDP



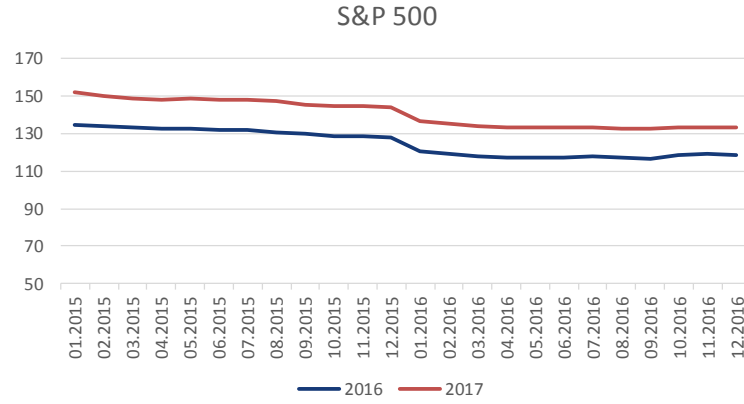
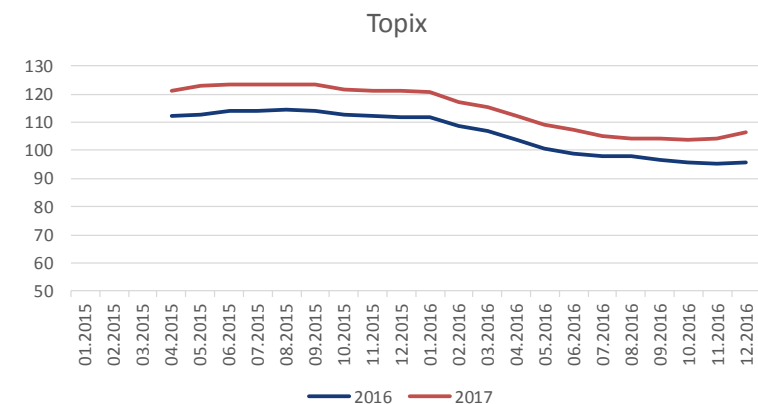
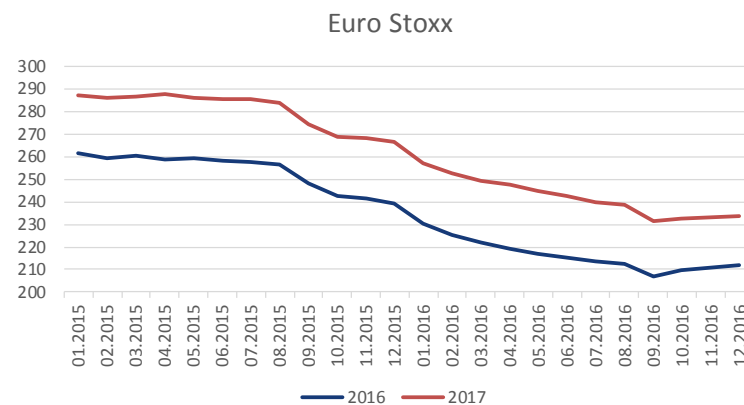
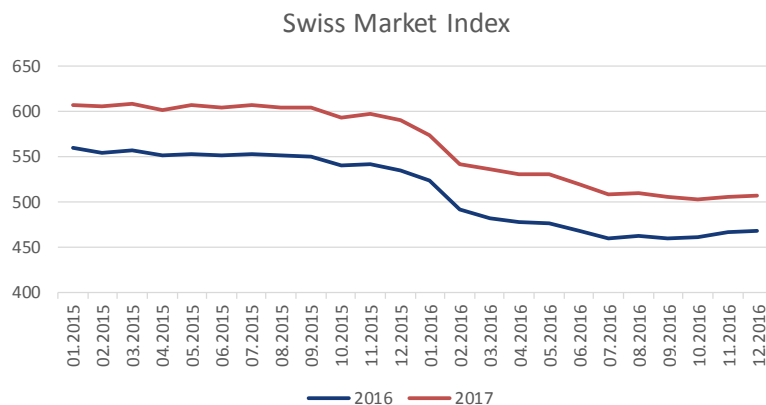
## Shiller PE Ratio \*



\* PE based on real EPS over 10 year period



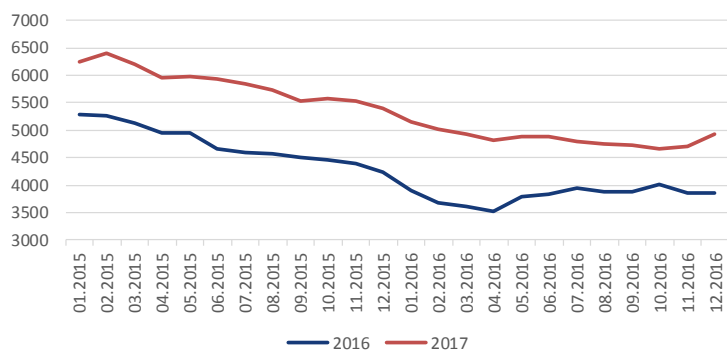
# Equities: Earnings-Revisions



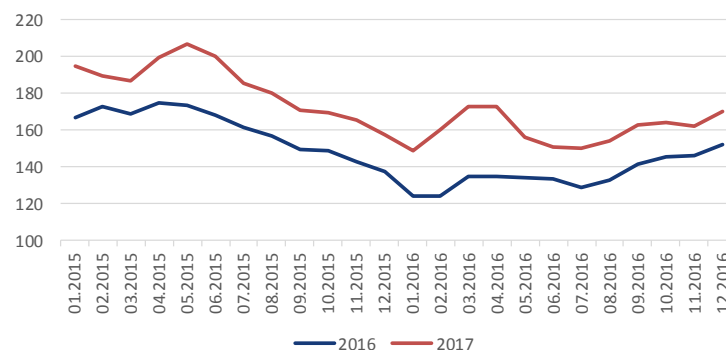


# Equities: Earnings-Revisions

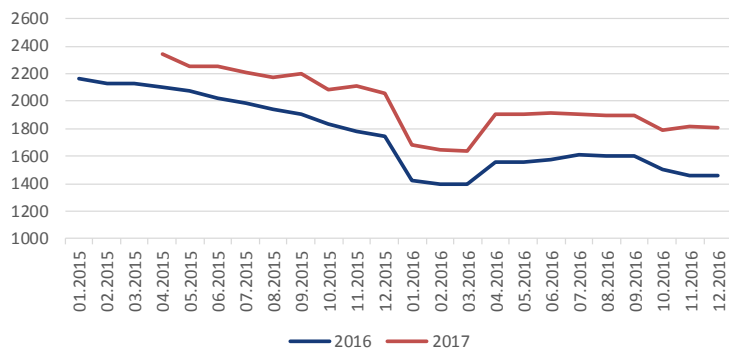
### Brazil Bovespa



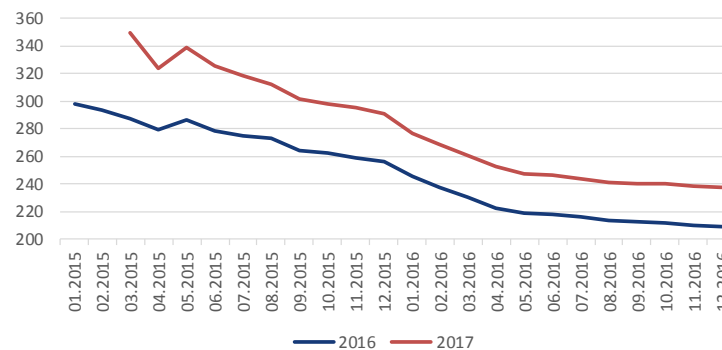
### Russian Traded Index \$



### Bombay Sensex



### Shanghai Composite





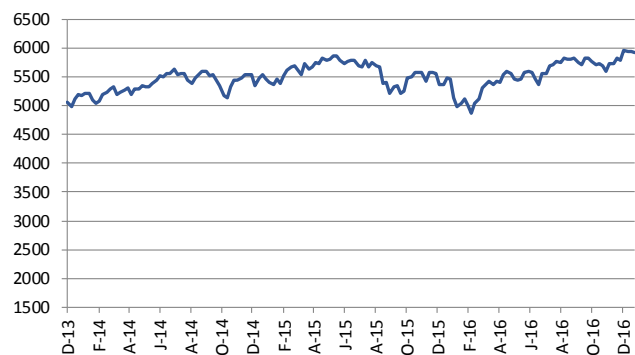
## Equities: Forecast

	Equities		
	Actual	3 Mo.	12 Mo.
Switzerland (SPI)	9'048	8'900	9'350
Germany (DAX)	11'609	11'500	12'000
Euro Zone (Euro Stoxx 50)	6'512	6'450	6'700
UK (FTSE 100)	7'178	7'100	7'400
USA (S&P500)	2'239	2'225	2'250
Japan (Topix)	19'114	19'000	19'000
Brazil (Bovespa)	60'266	57'500	60'000
Russia (MSCI Russia)	564	560	580
India (Sensex)	26'643	26'600	28'000
China (CSI Total Return)	2'794	2'775	2'900



# Equities: Developed and Emerging Markets

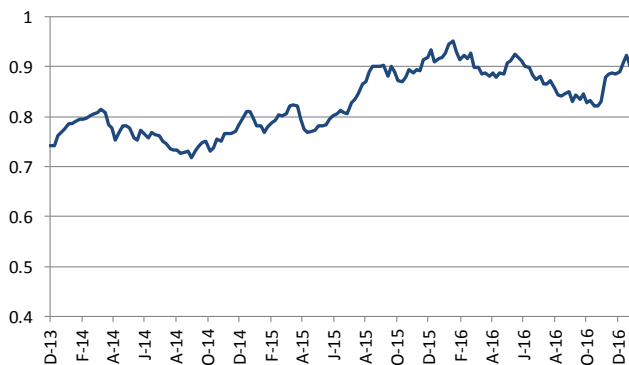
### Dow Jones Developed Markets



### Dow Jones Emerging Markets



### Relative Performance



Outperformance Developed Markets



Outperformance Emerging Markets



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