



LimmatWealth

Investment Strategy August 2016

Data & Forecasts (all data as of July 22, 2016)

	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	0.99	1.00	1.02
Germany	1.6	1.2	0.5	1.4	-	-	-
Euro Area	1.6	1.4	0.4	1.1	1.10	1.10	1.08
UK	1.7	1.3	0.8	1.9	1.32	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	106	105	100
Brazil	-3.3	0.5	8.7	6.1	3.27	3.50	3.60
Russia	-1.2	1.0	8.4	6.5	64.29	65.00	70.00
India	7.4	7.4	5.3	5.3	67.12	67.00	70.00
China	6.6	6.2	1.8	2.0	6.67	6.70	7.00

	Bonds (10 yrs.)			Profits (%)		Equities		
	Actual	3 Mo.	12 Mo.	EPS 16	EPS 17	Actual	3 Mo.	12 Mo.
Switzerland	-0.50	-0.50	0.00	112	11	8'860	8'750	9'200
Germany	-0.02	0.00	0.50	68	10	10'156	10'000	10'500
Euro Area				39	12	5'797	5'800	6'000
UK	1.54	1.75	2.25	87	17	6'700	6'650	6'900
USA	1.54	1.75	2.25	6	13	2'165	2'150	2'200
Japan	-0.22	-0.10	0.00	8	11	16'589	16'400	16'700
Brazil	11.83	12.00	12.00	511	22	56'641	56'000	56'000
Russia	4.35	4.50	4.50	28	16	460	460	480
India	7.25	7.50	7.00	28	19	27'681	27'500	29'000
China	2.81	3.00	3.00	15	13	2'667	2'650	2'900

China continues to grow strongly

The United Kingdom (UK) surprised with a majority 'YES' to withdraw from the European Union (Brexit). The impact on economic data is hard to tell primarily because no details of the exit process are set yet. The International Monetary Fund (IMF) lowered its growth forecast for the UK by 0.2% to 1.7% for the current year and by 0.9% to 1.3% for the coming year. The IMF does not expect a recession. Inflation (Consumer prices +0.5%, core rate +1.4%) and unemployment (4.9%) were in line with previous releases. Surprisingly, the Bank of England (BoE) did not lower interest rates but mentioned the possibility of such a step in August. In the Euro Zone, economic data did not deviate much from earlier announcements (consumer prices +0.1%, core rate +0.9%, unemployment 10.1%). Despite Brexit, the IMF forecasts growth of 1.4% in 2017 (-0.2%). In the US, 265'000 new jobs surprised positively. Because the number of unemployed people look-

ing actively for a job increased, unemployment rose from 4.7% to 4.9%. Inflation (consumer prices +1.0%, core rate +2.3%) did not change drastically. An interest hike by the Fed is not in the cards as of the end of July. Japanese economic data was in line with expectations (Unemployment 3.2%, inflation -0.4%, core rate +0.6%). Japanese President Abe's coalition party celebrated a victory on the occasion of the election of the Upper House and Abe promised to stimulate the economy further. In Brazil, the PMI (Purchasing Manager Index) showed further strength (42.3), reflecting rising optimism of the corporate sector. Inflation rose from 11.3% to 12.3%, while unemployment remained at 11.2%. In Russia, unemployment declined to 5.4%, while inflation remained in the area of 7.5%. China grew by another 6.7% during the 2nd quarter mainly thanks to large government investments. Inflation dropped from 2.0% to 1.9%.

Strong performance of British bonds

Despite Standard & Poor's cutting the rating of the UK from AAA to AA the relevant index returned 4.4% over the month (July 21 vs. June 20). The Rating agency S&P is expecting a deterioration of the British economy. Interest rates also dropped in other geo-

graphic markets but to a lesser extent. The outlook for bonds is murky. Bonds are held exclusively for their diversification benefits. Mainly government bonds offer some protection in the case of equity market crashes.

British Pound weak

Brexit sent the Pound tumbling and over the month a loss of about 10% versus the USD occurred. Meanwhile, the US Dollar profited from uncertainty and rose 3.6% according to the DXY-Index. While the Euro lost 2.5% in comparison to the USD, it remained stable versus the Swiss Franc (-0.1%). Uncertainties with regards to the implementation of Brexit limit the potential of the English Pound and the Euro. As a result, we are expecting a slightly stronger USD. Although the Swiss Franc is heavily overvalued in comparison to the Euro, the alignment to the purchasing power parity will take longer than previously expected because of Brexit. The Yen has ap-

preciated too quickly and we are expecting a technical counter reaction on the downside.

Gold (+3.2%) benefited from rising uncertainty. The broad commodity index was burdened by weak oil prices (-9.4%) and dropped by 5%. Commodity fundamentals have not improved in our view. In light of weak economic growth, we are continuing to underweight this asset class. Within commodities, we are concentrating on gold, which offers some hedge in light of the current uncertainties. Mainly in the case of currency wars, demand for gold would increase dramatically.

Brexit-Losses mostly recovered

Mainly in Europe, Brexit led to heavy losses in the short term. Within two trading sessions, the Euro Stoxx lost more than 10% before a slow recovery set in. Over the month, developed markets rose 2.5% and emerging markets soared even 6.9%. The weak Pound Sterling sent British stocks 8% higher. Considering high risks, declining corporate profits on a worldwide basis since September 2014 and rather high absolute valuations of equity markets, we are expecting a range bound market. We see substantial political (implementation of Brexit, US elections, refugee influx in Europe, rising claim to power of China and Russia etc.) as well as economic (economic activity) risks. Significantly higher equity prices – mainly in the US – would need additional extreme measures of central banks. Since we are not willing to bet on further dovish actions by central banks, we are continuing to underweight equities.

After large setbacks in the order of 30% within the past year, we are of the opinion that biotech companies offer interesting potential. In comparison to 'traditional' pharma companies, biotech offers higher revenue growth (10%-15% vs. 0%-5%) at lower valuations (PE 2017 14x vs. 16x). We are going to invest in a biotech fund within the coming days. As a result, our equity allocation will rise slightly (but remain underweighted).

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