LimmatWealth

Investment Strategy November 2016

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	1.00	1.02
Germany	1.7	1.4	0.4	1.5	-	-	-
Euro Area	1.7	1.5	0.3	1.1	1.10	1.10	1.08
UK	1.5	1.1	0.7	2.5	1.23	1.25	1.30
USA	1.6	2.2	1.2	2.3	1.00	1.00	1.00
Japan	0.5	0.6	-0.2	0.5	105	105	100
Brazil	-3.3	0.5	9.0	5.4	3.19	3.25	3.60
Russia	-0.8	1.1	7.2	5.0	63.18	65.00	70.00
India	7.6	7.6	5.5	5.2	66.70	67.00	70.00
China	6.6	6.2	2.1	2.3	6.78	6.70	7.00

	Bonds (10 yrs.)			Profits (%)		Equities		
	Actual	3 Mo.	12 Mo.	EPS 16	EPS 17	Actual	3 Mo.	12 Mo.
Switzer-land	-0.38	-0.25	0.00	111	9	8'579	8'700	9'200
Germany	0.18	0.25	0.50	70	9	10'665	10'700	11'400
Euro Area				36	11	5'984	6'000	6'400
UK	1.85	1.75	2.25	99	17	6'954	7'000	7'400
USA	1.85	1.75	2.25	7	12	2'126	2'100	2'200
Japan	-0.05	-0.10	0.00	10	7	17'442	17'000	18'000
Brazil	11.40	12.00	12.00	520	16	64'925	65'000	66'000
Russia	4.01	4.00	4.25	41	13	479	470	500
India	6.80	6.75	6.75	20	19	27'995	27'500	29'000
China	2.74	2.75	2.75	11	14	2'740	2'700	2'900

IMF sees lower growth

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 now sees an expansion of 3.1% in 2016 and 3.4% in 2017. While expected inflation for the year 2017 was revised downwards for Japan, Russia and Brazil, it was increased for the United Kingdom and the US (from 1.5% to 2.3%). Annualized US growth increased to 2.9%, which marks the highest growth rate for the last two years. Nevertheless, growth profited from higher inventories (0.6%). Also, on a year-over-year basis, real GDP expanded only by 1.5%. The purchasing manager index rose from 52.3 to 54.9 and signals a slight acceleration of economic activities. Inflation amounts to 1.5% (consumer prices) respectively to 2.2% for the core rate. We are continuing to expect an interest rate hike in December by 25 basis points. The Euro-zone expanded by 1.6% during the 3rd quarter (2nd quarter 1.6%). Like in the US, the purchasing manager index (53.7 after 52.6) is also pointing towards a more dynamic development in the coming weeks. Inflation has remained subdued (consumer prices +0.5%, core rate +0.8%). 3rd quarter GDP accelerated in the United Kingdom from 2.1% to 2.3%. While consumer prices rose from 0.6% to 1%, the core rate remained more or less unchanged (1.5% vs. 1.3%). Japan announced data in line with the previous month (unemployment 3%, consumer prices -0.5%, core rate 0%). The Bank of Japan reconfirmed its inflation target of 2% but did not announce additional stimulation measures of any kind. China grew again at a rate of 6.7% during the 3rd quarter, while inflation rose slightly from 1.3% to 1.9%. Data from Brazil and Russia did not deviate meaningfully from those announced a month ago. India surprised markets by reducing the prime rate by 25 basis points to 6.25%.

Rising bond yields

In October, 10 year yields to maturities on government bonds rose in the Eurozone (+28 basis points), the US (+23 basis points) and Switzerland (+15 basis points) and consequently led to small losses. Since July, US yields (10 year government bonds) have risen from 1.36% to 1.83%, which resulted in a loss of almost 4%. While high yield bonds closed the month unchanged, emerging markets weakened by 1.4%. Despite the slightly higher interest rate level bonds remain relatively unattractive and are solely held for diversification benefits.

Strong USD and weak Pound

According to the DXY-Index, the USD strengthened again in October (+3.1%). We attribute this to the rising probability of an interest rate hike in December. Meanwhile, the Euro lost 2.3%, the Yen 3.3% and the pound weakened even by 5.6% in comparison to the greenback. Fear of a 'hard BREXIT' (extensive encapsulation from the EU) was the main culprit for the heavy loss of the British currency. Based on our expectations of higher US interest rates, we are continuing to expect further strength of the US Dollar. Nevertheless, a Trump victory would result in a weaker USD.

In October, the broad commodity index lost 0.5%. Oil (-2.9%) was burdened by a rising number of OPEC countries, which declared that they were not willing to reduce their exploration quota. Gold (-2.9%) suffered from profit taking. Gold is held as a hedge in the case of currency turbulences.

Continued outperformance of emerging markets equities

In October, emerging markets (+0.9%) outperformed developed markets (-2.2%) again. While European markets (Euro Stoxx +1.8%) closed positively, US equities (S&P500 -1.9%) weighted negatively on the world equity index. In light of high merger and acquisition activities (e.g. ATT/TimeWarner, Qualcom/NXP etc.) and the pleasant earnings season, we are surprised by the underperformance of the US equity market. Instead of contracting by 2-3%, the latest data point towards profit growth in the order of 2-3%. Investors seem to refrain from additional commitments in light of uncertainties with regards to the interest rate policy of the Fed and US elections on November 8. In light of the current circumstances, the constitution of the US Congress – Republicans currently hold the majority in the House of Representatives and the Senate – will be at least as important as the election of the President. Our main scenario does not incorporate a significant impact on the S&P500 by the elections. The development of the SMI (-3.8%) was rather disappointing after the Swiss pharmaceutical stocks with their heavy weight in the SMI released weakish results. Although Swiss equities look relatively attractive now, we don't see a trigger for significantly higher prices currently. The constitutional referendum in Italy (December) constitute a risk, which in our view is not reflected in current European equity prices. Consequently, we are refraining from increasing our equity allocation and remain slightly underweighted. In the case of setbacks of worldwide equity markets we would presumably increase our allocation to Swiss stocks.