



global weekly

Investment
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More monetary easing ahead

After dovish remarks at the press conference, we expect the European Central Bank (ECB) to increase its asset-purchasing programme on worries about global growth and inflation

Macro outlook

ECB President Mario Draghi struck a very dovish tone during Thursday's press conference. He said that recent developments pointed to a 'weaker economic recovery and slower increase in inflation rates' than previously expected. In addition, 'downside risks' had emerged for both growth and inflation. He followed up the dovish commentary by announcing downgrades to the ECB's growth and inflation forecasts. Importantly, this also included the inflation projection for 2017, which is currently seen as representing the medium term horizon crucial for policy decisions. The ECB left its monetary policy unchanged, but these are strong signals that the central bank will likely step up its asset-purchasing programme.

Additional monetary easing by the ECB is now our base case scenario (we previously saw a 40% chance). We think that the central bank will most likely do this by stepping up the pace of its monthly purchases and that it needs to increase the eligible universe of assets it will buy. More monetary easing will likely be announced before the end of this year.

The central bank already announced a change in its existing asset-purchasing programme, that may help to expand it going forward. It decided to increase the issue share limit from 25% to 33%, which will give it a little more flexibility in its purchases. More importantly, it opens the door for more changes.

The ECB's remarks supported both equity and government bond markets on Thursday. German 10-year Bund yields declined by around 5 basis points, while the Eurostoxx index was up by almost 3%. Meanwhile, the prospect of more monetary easing also weighed on the euro, with EUR/USD declining to around the 1.11 level.

The US labour market report suggests that the economy remains in good health. There was a miss on the headline

Equity index performance

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	389.3	-2.6	-6.7
S&P 500	1951.1	-1.8	-5.3
AEX Index	438.3	-1.7	3.6
EuroStoxx 50	3270.1	-2.1	2.2
DAX Index	10317.8	-1.4	4.1
Nikkei 225	17792.2	-7.0	4.2
Hang Seng Index	20843.9	-4.6	-11.3

Important rating changes (RL=Recommended List)

Company	From	To
Intel	Buy	Hold
Glencore	Hold	Buy
Inditex	Buy	Hold
Publicis	Hold	Buy
Simon Property Group	Hold	Buy

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	0.687	-3.1	15.3
German Bunds 2-year	-0.236	-2.8	-15.9
Japan 2-year	0.010	-0.4	-6.8
US Treasuries 10-year	2.136	-4.6	-31.5
German Bunds 10-year	0.689	-5.2	-28.0
Japan 10-year	0.354	-2.5	-18.1

Spreads

Index	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	82.64	2.97	26.09
iTraxx Euro 5-year	74.46	2.95	18.66
JPM EMBI+	420.68	-4.12	118.69

Performance data as of Friday, 4 September.

Source: Bloomberg

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non-farm payrolls for August, but at 173.000 it is still a healthy pace. August is a month that is prone to upward revision in any case. In addition, we saw upward revisions to previous months, while the unemployment rate declined significantly and wages firmed. This report would normally have been enough to get the Fed over the line in September. Given market volatility and downside risks related to China and other emerging markets, we think, however, that the Fed will delay the first rate hike to December.

Earlier this week, investor risk appetite took a blow as concerns about the global economic outlook intensified. Equity markets headed lower. This erased some of the gains made after Black Monday. US Treasuries and the Japanese yen were the main beneficiaries. The concerns about the global economy were fueled by a set of weak manufacturing purchasing-managers indices (PMIs). China's official manufacturing PMI dropped to 49.7 in August from 50 in July, taking it to its lowest level since August 2012. The weakness was mirrored in most emerging markets economies. There was also a more moderate slow-down in growth in the advanced economy PMIs, with Markit indices for the eurozone and US slipping.

We continue to see firmer growth ahead, however, as we see three positives going forward. First, domestic demand in the US and the eurozone has been firming. Second, oil prices have come down, and this could also facilitate an easier monetary policy stance globally. Third, the Chinese authorities continue to take a range of measures to support demand.

Bond markets update

ABN AMRO Group Economics moved their expectations for the Fed rate hike to December from September. With the latest volatility and questions about global growth and inflation (due to lower oil and commodity prices) it is more likely that the Fed will act in December.

Together with the ECB's move, this is calming European government bonds and credits, such as covered bonds and agency bonds. Furthermore, foreign investment inflows have been supportive for US fixed income in recent months. They are off-setting outflows from foreign central banks, as they are scaling back their foreign exchange reserves and holdings of US Treasuries and German Bunds. The higher quality of current account financing could, however, make the US dollar less vulnerable to short-term volatility and is positive for asset allocation towards the United States.

The cocktail of the decline in energy prices and the move by the Chinese authorities to a more flexible and weaker yuan

could lead to a broader change of foreign-currency policy arrangements. Currencies of energy-dependent economies feel tensions, as well as currencies of countries that are highly dependent on China. The decline in energy prices seems to have negative implications for risky bonds, such as high yield and emerging-market bonds, and less for investment-grade credits.

Now that the China markets are closed at the end of the week, investors have taken the time to reassess current market developments. We think markets will not yet reverse the wider risk premium of high yield or emerging-markets bond, as we think fixed-income investors need some more time to reflect. We expect that government bonds will stay in a certain trading range.

Equity markets update

Following an extremely volatile week, market turbulence eased a little this week. From last week's peak of 51, the VIX Index dropped to 26. The index should decline under 20 to reflect normalizing markets. As the second-quarter earnings season is over now, investor have to await whether the recent turmoil in China is impacting their businesses.

This week, rounds of lay-offs were announced in the energy sector due to the substantially lower oil price. Although the recovering oil price helped the sector this week, we remain cautious about the industry's prospects. We note that cash flows are deteriorating and the question is whether the industry can maintain its attractive dividend yield.

US car sales figures for August that were published this week, were stronger than expected. The annualised selling rate is at 17.8 million, which is some 2% higher than last year. The European auto market also remains in good shape as car sales are up 8% year to date. Nevertheless, car stocks have been lagging strongly in recent months as sentiment continues to be dominated by fears about the state of the Chinese economy.

Currency outlook

The recent waves of risk aversion at financial markets did not result in support for the euro. Instead the yen and the US dollar moved higher. This confirms our view that the spike in EUR/USD in August was not related to safe-haven demand but merely to the closing of euro short positions. In addition, the increased likelihood for additional monetary easing by the ECB has weighed on the euro this week. EUR/USD dropped from 1.1230 before the start of the ECB press conference to a low of 1.1112. We remain bearish on EUR/USD mainly because of monetary policy divergence between the eurozone and the US. Our target for the end of 2015 for EUR/USD is parity.

Asset allocation

The Global Investment Committee, at its meeting on 3 September, confirmed its conviction in the existing asset allocation. It consists of an overweight allocation to equities (profiles 2 to 6) and commodities (profiles 2 to 6) and a strong underweight in bonds (profiles 1 to 5), with no bond allocation in profile 6. Real estate, which is strongly correlated to equities, is underweight (profiles 2 to 6). Hedge funds are now overweight in all profiles. Cash is overweight in profiles 1, 2, 3 and 4 and underweight in profiles 5 and 6.

Next week's calendar

Important dates next week

	Country	Date
Industrial production - % m-o-m	DE	07 Sep
ECB announces weekly QE details	EC	07 Sep
GDP - Q2 final estimate and components, % q-o-q	EC	08 Sep
Fed Reserve consumer credit - USD bn	US	08 Sep
US job openings by industry	US	09 Sep
CPI - % y-o-y	CN	10 Sep
CPI - % y-o-y	DE	11 Sep
Univ. of Michigan cons. confidence - index	US	11 Sep

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