



global weekly

Investment
Communication
19 February 2016**A wave of optimism**

This week, financial markets were driven by a wave of optimism, owing to a rise in oil prices and the firm comment from ECB President Mario Draghi that “we will not hesitate to act”.

Asset allocation

The Global Investment Committee at its meeting on 18 February found that the fear of recession is exaggerated, the US Federal Reserve is expected to remain “on hold” in terms of rate hikes in 2016 and central banks worldwide are expected to continue to support growth, still having a number of fiscal and monetary policy measures left to use.

The committee therefore decided it was time to increase equity risk across the board. The increase will be at the expense of cash in cash-rich portfolios (profiles 2, 3 and 4) and, in addition, at the expense of existing exposures to hedge funds in the equity-dominated portfolios (profiles 5 and 6). Portfolio profile 1 remains unchanged.

The asset allocation now calls for an even stronger overweight in equities, and unchanged positions in bonds (underweight), commodities (overweight) and an underweight allocation to real estate in balanced profiles. The allocation to hedge funds remains an overweight, with the exception of the equity-dominated portfolios with a neutral allocation.

For portfolio profile 3, the 5%-increase in equity risk comprises an increase of 3% to return to the tactical asset allocation of 38% of early December and an additional 2% increase in equity risk. As a result, the tactical equity allocation has increased to 40%.

Macro outlook

ABN AMRO Group Economics has lowered its forecasts of global economic growth. Our economists have reduced the 2016 economic growth forecast for the US (to 1.7% from 2%), eurozone (to 1.2% from 1.6%) and emerging markets (to 4.1% from 4.3%). The new scenario sees a longer period of weaker global growth followed by a modest recovery later in the year, but no recession.

Equity index performance

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	371.2	3.9	-7.3
S&P 500	1917.8	2.8	-6.2
AEX Index	414.3	5.6	-6.3
EuroStoxx 50	2892.7	4.9	-11.5
DAX Index	9445.2	5.2	-12.1
Nikkei 225	15967.2	6.6	-17.6
Hang Seng Index	19285.5	5.1	-12.8

Important rating changes (RL=Recommended List; NR=not rated)

Company	From	To
International Business Machines	Buy	Hold
Kinder Morgan	Buy	Hold
Valero Energy	Hold	Buy
Exelon	Hold	Buy
Oracle	NR	Buy

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	0.695	-2.1	7.6
German Bunds 2-year	-0.530	-1.9	-31.2
Japan 2-year	-0.200	-3.5	-22.8
US Treasuries 10-year	1.734	-1.5	-38.1
German Bunds 10-year	0.199	-6.2	-18.0
Japan 10-year	0.005	-7.5	-38.3

Spreads

Index	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	116.77	-5.32	52.41
iTraxx Euro 5-year	110.51	-7.71	56.51
JPM EMBI+	452.08	-34.86	58.02

Performance data as of Friday, 19 February

Source: Bloomberg

In this issue

Asset allocation	1
Macro outlook	1
Equity markets update	2
Bond markets update	2
Currency outlook	2
Published this week	3

Group Economics expects central banks to step up their reflation efforts. Together with a gradual rise in oil prices during the course of the year, central bank actions should help to improve market sentiment, breaking the negative feedback loops to the economy and improving overall financial conditions.

We no longer expect the Federal Reserve to raise interest rates again in 2016. We think it will only resume its rate hike cycle once economic growth strengthens and the economy has absorbed the past tightening of financial conditions.

The European Central Bank (ECB) will step up its monetary stimulus more significantly than we thought before. We now expect the ECB to cut its deposit rate by a cumulative 40 basis points to -0.7% over the coming months. We see the reductions taking place in two steps of 20 basis points, in March and June. Also, we continue to expect the ECB to step up its asset purchasing by EUR 10 billion per month.

Equity markets update

Equities recovered this week after a period of severe losses. European indices outperformed US markets after Draghi reaffirmed that the ECB will do whatever it takes. Also the statement from Fed Chair Janet Yellen indicating less rate hikes helped.

Stocks that fell the last couple of months rebounded fiercely. Glencore for example rose by more than 20% this week and Freeport McMoRan almost by 30%. On a sector level, energy and materials benefitted the most; health care and consumer staples the least.

For German utilities, the discussion on cost allocation of disposing nuclear waste and clean-up continued. A government-assigned commission signalled it may be willing to allocate some of the clean-up costs to the German state. E.ON and RWE rose substantially on this news. The four largest utility companies had reserved more than EUR 38 billion for this purpose. Later that week, RWE negatively surprised the market. The stock lost 15% as RWE cut dividend and presented lower-than-expected results.

US oil and gas exploration & production companies continue to struggle with the current low energy price. Like other US exploration & production companies, Anadarko Petroleum, ConocoPhillips and Devon Energy cut their dividends, considerably reduced investments and announced more job cuts in order to adjust cash-flow budgets.

Reporting calendar

Company	Date
Allergan, HSBC	22 Feb
Home Depot, Danone, BHP Billiton, Westfield	23 Feb
Salesforce.com, Hewlett-Packard, Iberdrola, Transocean, Fresenius Medical Care, Peugeot, Delta Lloyd, Wolters Kluwer, Fresenius SE, Suez Environnement Company, Airbus, ASM Int., Noble Group	24 Feb
Apache, Technip, Bayer, Henkel, ProSieben, Bureau Veritas, Aalberts Industries, Heijmans, Reed Elsevier, Compagnie De Saint-Gobain, AXA, Deutsche Telekom, Repsol, Anheuser-Busch Inbev, GDF Suez, Baidu	25 Feb
Telefonica, Vopak, RBS, USG People, BASF, Belgacom, Ten Cate, Bekaert, Fugro, Ackermans van Haaren, Eni Spa	26 Feb

In contrast, online travel company Priceline benefitted from lower oil prices. Its fourth quarter results have beaten analyst forecasts. Lower oil prices resulted in lower ticket prices and a rise in airplane ticket sales. For 2016, the online travel company expects a growth in bookings of 25%.

Bond markets update

A wave of optimism swept over bond markets this week. The markets rose after ECB President Mario Draghi commented before the European parliament on problems in the financial and energy sector. Especially the "we will not hesitate to act" comment excited markets and investors.

Hopefully, Draghi's positive stance will fill the period until the next ECB meeting in March. We expect the March meeting to be an event to watch, as either investors may have too high expectations, or the ECB may over-deliver.

Interest rates remained steady over the course of the week. Credit spreads came down, but they remained at very elevated levels. The volatility and the scarce liquidity that had raised fears of market collapse earlier, receded. In the calm this gives to markets, spreads were able to come down further.

Currency outlook

This week, we have revised our currency forecasts. Our new forecasts reflect the reflation efforts of central banks, global growth outlook and investor sentiment. In the coming months, we expect the euro to move lower towards 1.05 versus the US dollar because of improvement in investor sentiment. Also, the effects of ECB easing on EUR/USD will outweigh the effect of the Fed putting rate hikes on hold.

This week there has been a positive spill-over effect from oil prices to other financial markets. The 15-20% rally in oil prices

since 11 February has resulted in an overall improvement in sentiment in financial markets. As a result, currencies that performed well in a risk-off environment, such as Swiss franc, Japanese yen and the euro suffered. Moreover, currencies of oil-exporting currencies recovered substantially. The Russian ruble and the Mexican peso have both rallied by more than 5% since last Thursday.

Our energy analyst expects that oil prices are currently in the process of bottoming out. This process is often volatile in terms of price action on an intraday level. The crucial level to watch are the previous peaks in oil prices around 35-36 USD per barrel. Above this level, currencies of oil exporting countries are likely to advance sharply.

Published this week

Bond Report: Liquidity Trap in Credit Markets

A balance between buyers and sellers leads to liquidity in bond markets. If this balance is lacking, market liquidity will deteriorate and price swings will occur. Recently, we have witnessed several events – including the closing of high-conviction credit funds such as Third Avenue – where

deteriorating creditworthiness and liquidity conditions acted upon each other in a negative way. These types of events are likely to reoccur, particularly in markets that are sentiment driven, because poor liquidity is here to stay.

Contributors

Investment Strategy & Portfolio Expertise

Ralph Wessels - ralph.wessels@nl.abnamro.com

Maurits Heldring - maurits.heldring@nl.abnamro.com

Edith Thouin - edith.thouin@nl.abnamro.com

Roel Barnhoorn - roel.barnhoorn@nl.abnamro.com

Jaap Rijnders - jaap.rijnders@nl.abnamro.com

Willem Bouwman - willem.bouwman@nl.abnamro.com

Chris Huys - chris.huys@nl.abnamro.com

Group Economics

Georgette Boele - georgette.boele@nl.abnamro.com

Roy Teo - roy.teo@nl.abnamro.com

Nick Kounis - nick.kounis@nl.abnamro.com

Aline Schuiling - aline.schuiling@nl.abnamro.com

Maritza Cabezas - maritza.cabezas@nl.abnamro.com

Disclaimer

© Copyright 2016 ABN AMRO Bank N.V. and affiliated companies ("ABN AMRO"), Gustav Mahlerlaan 10, 1082 PP Amsterdam / P.O. box 283, 1000 EA Amsterdam, The Netherlands. All rights reserved. This material is provided for informational purposes only and does not constitute an offer to sell or a solicitation to buy any security or other financial instrument. While based on information believed to be reliable, no guarantee is given that it is accurate or complete. While we endeavour to update on a reasonable basis the information and opinions contained herein, there may be regulatory, compliance or other reasons that prevent us from doing so. The opinions, forecasts, assumptions, estimates, derived valuations and target price(s) contained in this material are as of the date indicated and are subject to change at any time without prior notice. The investments referred to in this material may not be appropriate or suitable for the specific investment objectives, financial situation, knowledge, experience, or individual needs of recipients and should not be relied upon in substitution for the exercise of independent judgement. ABN AMRO or its officers, directors, employee benefit programs or co-workers, including persons which were involved in preparing or issuing this material, may from time to time hold long- or short-positions in securities, warrants, futures, options, derivatives or other financial instruments referred to in this material. ABN AMRO may offer and render at any time investment banking-, commercial banking-, credit-, advice-, and other services to the issuer of any security referred to in this material. Pursuant to offering and rendering such services, ABN AMRO may come into possession of information not included in this material and ABN AMRO may prior or immediately after publication thereof have acted based on such information. In the past year, ABN AMRO may have acted as lead manager or co-lead manager with regard to a public offering of securities from issuers as mentioned in this material. The stated price of any securities mentioned herein is as of the date indicated and is not a representation that any transaction can be effected at this price. Neither ABN AMRO nor other persons shall be liable for any direct, indirect, special, incidental, consequential, punitive or exemplary damages, including lost profits arising in any way from the information contained in this material. This material is for the use of intended recipients only and the contents may not be reproduced, redistributed, or copied in whole or in part for any purpose without ABN AMRO's prior express consent. This document is solely intended for dissemination amongst private/retail customers in a PC country. Distribution to private/retail customers in any jurisdiction that would require registration or licensing of the distributor which the distributor does not currently have, is not permitted. Material means all research information contained in any form including but not limited to hard copy, electronic form, presentations, e-mail, SMS or WAP.

US Securities Law

ABN AMRO Bank N.V. is not a registered broker-dealer under the U.S. Securities Exchange Act of 1934, as amended (the "1934 Act") and under applicable state laws in the United States. In addition, ABN AMRO Bank N.V. is not a registered investment adviser under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act" and together with the 1934 Act, the "Acts"),

and under applicable state laws in the United States. Accordingly, absent specific exemption under the Acts, any brokerage and investment advisory services provided by ABN AMRO Bank N.V., including (without limitation) the products and services described herein are not intended for U.S. persons. Neither this document, nor any copy thereof may be sent to or taken into the United States or distributed in the United States or to a US person.

Other jurisdictions

Without limiting the generality of the foregoing, the offering, sale and/or distribution of the products or services described herein is not intended in any jurisdiction to any person to whom it is unlawful to make such an offer, sale and/or distribution. Persons into whose possession this document or any copy thereof may come, must inform themselves about, and observe, any legal restrictions on the distribution of this document and the offering, sale and/or distribution of the products and services described herein. ABN AMRO cannot be held responsible for any damages or losses that occur from transactions and/or services in defiance with the restrictions aforementioned.

Sustainability Indicator Disclaimer

ABN AMRO Bank N.V. has taken all reasonable care to ensure the indicators are reliable, however, the information is unaudited and subject to amendment. ABN AMRO Bank is not liable for any damage that constitute from the (direct or indirect) use of the indicators. The indicators alone do not constitute a recommendation in relation to a specific company or an offer to buy or sell investments. It should be noted that the indicators represent an opinion at a specific period of time considering a number of different sustainability considerations. The sustainability indicator is only an indication regarding the sustainability of a company within its own sector.

Company disclosures

ABN AMRO may beneficially hold a major shareholding or a significant financial interest of the debt of this company. ABN AMRO currently maintains a market in the security of this company and otherwise purchases and sells securities of this company as principal. ABN AMRO has received compensation for investment banking services from this company, its subsidiaries or affiliates during the previous 12 months. All disclosures made herein refer to ABN AMRO and its affiliates, including ABN AMRO Incorporated, which is regulated in the United States by the NYSE, NASD and SIPC.

Personal disclosures

The information in this opinion is not intended as individual investment advice or as a recommendation to invest in certain investments products. The opinion is based on investment research of ABN AMRO Research and Strategy. The analysts have no personal interest in the companies included in this publication. Their remuneration for this work is not, was not and will not be related directly or indirectly to the specific recommendations or views expressed in this opinion.

