



global weekly

Investment
Communication
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Waiting for confirmation

Financial markets are currently in wait-and-see mode for the US employment report this afternoon, that can support the Fed's path to a rate hike.

Macro update

We have moved our forecast for the Fed's next rate hike forward to December 2016 from March 2017 previously. We now expect two rate hikes in 2017 rather than three previously. This means we continue to expect three rate hikes in total between now and the end of next year. In terms of timing, we think that the Fed meetings of June and December 2017 are likely candidates to announce the subsequent rate hikes.

The reason for the change is the tone of Fed Chair Janet Yellen's speech at the Jackson Hole symposium on 26 August regarding the short-term economic outlook. In her keynote speech, Yellen noted that "...the case for an increase in the federal funds rate had strengthened in recent months." Fed policymakers have been quite divided on their expectations of the path for rate hikes.

A decent non-farm payrolls report on Friday will likely provide Fed policymakers the ammunition to support a rate hike this year. The market-implied odds of a rate hike in December of this year currently stand at around 60%. On top of this, investors are now pricing-in one to two rate hikes in 2017 compared to one previously.

Our forecasts related to the ECB's monetary policy have also been modified. An increase in the monthly asset purchases is no longer expected in September. The central bank is also not expected to move rates further into negative territory. An

Equity index performance in local currency

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	417.4	-0.3	4.5
S&P 500	2170.9	-0.1	6.2
AEX Index	457.0	0.9	3.4
EuroStoxx 50	3017.5	0.9	-7.1
DAX Index	10534.3	-0.4	-1.8
Nikkei 225	16925.7	3.5	-11.1
Hang Seng Index	23266.7	1.6	6.2

Important rating changes

Company	From	To
Credit Suisse	Buy	Hold
Swatch	Buy	Not rated
Morgan Stanley	Buy	Hold
Bank of America	Buy	Hold
Solarcity	Hold	Buy

Performance data as of Friday, 2 September 2016

Source: Bloomberg

expansion of the asset-purchase programme in terms of the type of assets that can be purchased and a lengthening of its term are still expected in September.

Equities update

After US equity markets were close to new highs in mid-August, increased uncertainty over the Federal Reserve's course toward higher rates has somewhat dented sentiment. Equity markets around the world hardly changed during the week, as investors wait for Friday's US job figures.

The Brazilian Bovespa Index was unchanged following the news that Brazilian president Dilma Rousseff has been officially

impeached by the Senate. Her departure was already widely anticipated and Brazilian shares have been rebounding all year. Indeed, the Bovespa Index remains among the best performing stock indices around the world with a year-to-date performance of more than 60% in euro terms.

The financials sector was the strongest performing sector this week. European banks rose on rumours that Deutsche Bank and Commerzbank held merger talks a couple of weeks ago. The weakest performing sectors were energy and materials. The explanation for this underperformance was the 4%-decline in the oil price this week. Other commodities were also lower, partly on the back of a strengthening US dollar.

Apple grabbed the most attention this week. The European Commission decided that the company should pay EUR 13 billion in penalties for unlawful tax arrangements. EU competition commissioner Margrethe Vestager accused Apple of sidestepping taxes by channeling 90% of international profits through units in Ireland to avoid paying taxes. Apple will appeal against the penalty. Assuming that the company would have to pay the EUR 13 billion fine, the impact would be limited as the company has more than USD 200 billion in cash. The Apple shares hardly reacted on the news.

Bond markets update

European fixed income markets will become more focused on political impasses. In the second half of this year, peripheral bonds might very well be under fire. Interest rates in the eurozone edged up a little, but left 10-year Bund yields still in negative territory. Also peripheral spreads, plummeted after Brexit, have started to turn.

This had to do with acting Spanish Prime Minister Mariano Rajoy losing a vote of confidence in the parliament this week. Rajoy now has only days to find a majority, otherwise there is only one chance left to form a government. If he does not succeed, Spain will have elections for the third time in a year.

DBRS, a rating agency, might downgrade Portugal's' debt to junk status soon. In that case, Portuguese bonds will not be eligible for the ECB's asset purchasing programme.

Also Italy will appear on the radar of rating agencies, if its debt/GDP ratio worsens. Italy's current rating is BBB-, one notch away from junk status. Italy will ask Brussels again

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	0.796	-4.8	8.6
German Bunds 2-year	-0.627	-0.7	-41.6
Japan 2-year	-0.188	-0.9	-19.8
US Treasuries 10-year	1.593	-3.8	-59.2
German Bunds 10-year	-0.055	1.9	-83.6
Japan 10-year	-0.050	2.5	-44.0

Spreads

Index	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	73.89	2.88	-9.76
iTraxx Euro 5-year	68.71	1.61	-5.54
JPM EMBI+	354.81	8.50	-68.65

Performance data as of Friday, 2 September 2016

Source: Bloomberg

for extra leeway for its 2017 budget deficit, after receiving a generous one in 2016. The country is to hold a constitutional referendum towards the end of this year, which is increasing worries, in addition to worries about the health of its banks.

Currency outlook

The US dollar index has rallied by 1.3%, now that financial markets have increased the possibility of a Fed rate hike this year based on Yellen's speech last Friday. As a result, precious metal prices, emerging market currencies and currencies of commodity exporters have suffered.

These moves will likely accelerate if the US employment report again exceeds expectations. In that case, financial markets will increase the probability for a rate hike already in September. We think that the chance of a rate hike in September is not that high. Financial markets have currently priced in a 60%-probability for a rate hike by the end of this year. This could increase further and provide some support to the US dollar. However, the upside in the dollar is limited in our view.

Our base scenario suggests that US economic growth will remain moderate, improving only slightly in 2017. The growth/inflation mix is not supportive for the dollar, with inflation expected to be above growth. Meanwhile, real interest rates are forecast to remain negative. Overall, this is not a supportive combination for the dollar and we do not think recent strength marks the beginning of a new dollar rally.

Asset allocation

The Global Investment Committee, at its meeting on Thursday 1 September, left the asset allocation unchanged. The asset allocation calls for a neutral positioning in equities and an underweight allocation to bonds. Commodities and real estate remain overweight; hedge funds have a neutral weighting.

Investment Strategy & Portfolio Expertise Group Economics

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