

# global weekly

Investment  
Communication  
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## Taper talk, not taper time

Bond yields briefly spiked this week, after news agency Bloomberg reported that the European Central Bank (ECB) is considering how to scale back or 'taper' its asset purchases. We do not expect the ECB to start tapering any time soon.

The account of the ECB's Governing Council meeting of 7-8 September, published on Thursday, suggested that recent market fears about the central bank winding down its asset purchase programme (quantitative easing) are overdone. Governing Council members noted that "there was still no clear upward trend visible in measures of underlying inflation, which remained low". This is a crucial statement, as the ECB's forward guidance on quantitative easing (from the press statement) is that "it will continue until (we see) a sustained adjustment in the path of inflation consistent with its inflation aim". So clearly this condition is not judged to have been met.

We continue to think that the ECB will expand the duration of its asset purchase programme from March 2017 currently to September 2017 in December. We do think it is logical that when the ECB does decide to end the programme, that it would do so gradually. So tapering would make perfect sense when the time is right. However, the time is not right now.

In the US, by contrast, the time for a rate hike is drawing near. Some Fed policymakers have been warning investors that the next rate hike could be as early as the next meeting in November. The Federal funds futures implied probability of a rate hike in November is only 24% and around 60% in December. We think that a November rate hike is unlikely given the proximity of US elections. We do expect the Fed to

## Equity index performance in local currency

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	417.6	-0.2	4.6
S&P 500	2160.8	0.4	5.7
AEX Index	451.9	-0.1	2.3
EuroStoxx 50	3021.6	0.1	-8.0
DAX Index	10568.8	1.0	-2.2
Nikkei 225	16860.1	2.5	-11.4
Hang Seng Index	23851.8	2.4	8.8

Performance data as of Friday, 7 October 2016

Source: Bloomberg

hike again in December and resume a very slow pace of rate hikes next year.

## Equity markets update

Equity markets were slightly higher this week, with the energy sector leading and the utilities sector lagging. The energy sector gained on hopes that the Organization of the Petroleum Exporting Countries (OPEC) will limit production, which also pushed up oil prices this week.

Shares of Deutsche Bank rebounded strongly after hitting a low of EUR 9.90 last week – a decline of almost 75% from its 2014 peak at EUR 38. Last weekend, Deutsche Bank's chief executive officer said the bank has enough resources to pay any fine from the US Department of Justice (DoJ). Rumours about a possible settlement with the DoJ also added to the relief rally in Deutsche Bank shares. We keep emphasizing, however, that for equity investors, risks related to Deutsche Bank are not over.

Rumours about a possible takeover of Netherlands-based NXP Semiconductors by US chip maker Qualcomm sent both

shares higher. NXP has a strong position in automotive chips. Cash-rich Qualcomm is playing the trend towards vehicles being increasingly equipped with computers and software systems. With the development of autonomous technology that allows a car to know its position on the road, sense other vehicles and obstacles, and guide the car safely to its destination, the need for computing power in a vehicle has accelerated. In addition, chips are increasingly used for infotainment solutions in cars. Qualcomm is one of the star performers in the IT sector this year, with a 33% increase in share price.

On Wednesday, Monsanto published quarterly results. The company experienced a tough year, as farmers struggled with lower prices for agricultural commodities. Price competition from DuPont represented another challenge for Monsanto. Monsanto's management, however, sees markets improving. Monsanto has agreed to a takeover bid from Bayer. The market consensus is apparently sceptical about the deal receiving regulatory approval, as the company's shares remain priced 20% below Bayer's offer.

### Bond markets update

The week started relatively quiet, but on Tuesday leaks from unnamed ECB officials suggested that the central bank was making plans on how to wind down its asset purchases (quantitative easing). This tapering rumour caught the market off guard and bond yields briefly shot up.

We have been saying for a while that central banks are rethinking their policies, as they believe governments should do more to stimulate their economies. Rumours about central banks ending their asset purchase programmes – forcing governments to become more active – can easily lead to yields shooting up. We do not think, however, that this week's story amounts to tapering any time soon.

That said, we cannot rule out any near-term interest rate increases. This as inflation expectations are creeping up. The five-year-forward inflation expectation, the one the Fed watches closely, has increased by 30 basis points in the last three months. This week, some Fed officials signalled that the Fed might increase its policy rate as soon as November. The market is currently assigning only a 24% probability to this. Furthermore, when looking at the average yield forecast of economists consulted by news agency Bloomberg, we do not see any significant rise in interest rate expectations since July.

All in all, there is a lot of complacency in the market that interest rates will not move any time soon, whereas the

### Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	0.852	8.8	22.5
German Bunds 2-year	-0.660	3.3	-40.8
Japan 2-year	-0.278	1.4	-27.8
US Treasuries 10-year	1.749	15.4	-31.9
German Bunds 10-year	0.019	14.1	-57.3
Japan 10-year	-0.064	3.0	-40.0

### Spreads

Index	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	74.26	-0.91	-9.96
iTraxx Euro 5-year	74.23	1.64	-9.23
JPM EMBI+	336.70	-14.41	-77.73

Performance data as of Friday, 7 October 2016

Source: Bloomberg

reasons to expect rising interest rates are – slowly – becoming more compelling.

### Currency outlook

At the start of the week, the US dollar received support from comments by Fed voting member Loretta Mester. Mester, an advocate of monetary policy tightening, said that November is a "live" meeting for raising rates. On Wednesday, non-voting Fed member Jeffrey Lacker, who is also in favour of tighter monetary policy, said that a pre-emptive rate hike is critical for stable inflation. As a result of this comment, the US dollar rallied again. If economic data come in better-than-expected, expectations for a rate hike at the November meeting will increase further. This should push the dollar higher. As a result, EUR/USD could drop to 1.10, while GBP/USD could move in the direction of 1.25.

The British pound plunged around 6% versus the dollar in early trading on Friday. According to Bloomberg, GBP/USD touched a low at 1.1841. Other sources, however, said the pound even hit 1.1378 at a certain point. It is not yet clear what caused this sharp decline. We do know that liquidity in the pound is low when only the Asian markets are open. The pound recovered during the course of the morning.

### Asset allocation

ABN AMRO's Global Investment Committee made no change to the asset allocation at its meeting on 29 September. The allocation continues to consist of a neutral stance to equities, an underweight to bonds and overweight allocations to commodities and real estate. There is a neutral stance to hedge funds.

## Published this week

### Equity Sector Note: consumer staples

We like the consumer staples sector for its defensive nature and exposure to emerging markets. Valuations in the sector look high, but the dividend yield of almost 3% is attractive and sustainable, in our view.

### Bond Markets Monthly: mixing protection and return

Within our underweight allocation to bonds, we are mixing protection and return. We seek protection in specific government bond strategies and investment-grade corporates. Return, in our view, is only to be found in riskier segments, such as high yield and emerging market debt.

### Bond Sector Note: consumer staples – stable but expensive

From a bond perspective, we take a neutral stance towards the consumer staples sector. Most of the issuers we cover still enjoy stable credit quality. However, bonds issued by consumer staples companies are expensive and upside potential is limited.

## Investment Strategy & Portfolio Expertise

### Group Economics

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