



Global Weekly

Meanwhile in Washington

Investment
Communication
20 January 2017

Equity indices moved mostly sideways this week, ahead of the inauguration of Donald J. Trump as the 45th President of the United States. Bond markets retreated, with bond yields – moving inversely to prices – edging higher.

Equity markets were rather stable this week, hovering around their all-time highs in the US and 12-month highs in Europe. Statements by central banks were in focus but did not move equity markets much. The Fed confirmed the outlook of several rate hikes and pointed at inflation risks, while the ECB maintained its interest rate policy, as expected. Investors were also looking for clues about international policies. UK Prime Minister Theresa May indicated that the UK's departure from the EU will be a so-called 'hard Brexit'. As a result, share prices of UK large caps that have high international exposure were supported, while companies that have a large base in the UK voiced their concerns. In the US, equity markets were steady ahead of today's (Friday) inaugural speech by president Trump, in which he may provide more details on his stimulatory economic plans. At his press conference last week, Trump failed to provide investors with much information on economic policies.

Equity index performance in local currency

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	428.4	-0.6	1.7
S&P 500	2263.7	-0.5	1.1
AEX Index	485.2	-0.6	0.4
EuroStoxx 50	3298.9	-0.8	0.3
DAX Index	11605.4	-0.2	1.1
Nikkei 225	19137.9	-0.8	0.1
Hang Seng Index	22885.9	-0.2	4.0

Performance data as of Friday, 20 January 2017

Source: Bloomberg

Meanwhile, the earnings season has gotten off to a good start. So far, 20% of companies have reported and their results are in line with analysts' expectations. Company outlook statements gave no reason to question the double-digit earnings growth forecast for 2017. Last week, US banks (Wells Fargo, JPMorgan and Citigroup) reported results that were a bit better than expected, while providing solid outlooks. In Europe, ASML's results also beat estimates. The supplier of semiconductor equipment sounded bullish on the perspectives of its extreme-ultraviolet lithography technique. Leading internet television

company Netflix's results topped analysts' estimates, as subscriber uptake exceeded expectations. Netflix shares rose by 10% after the results were announced.

Next week promises to give more insights into global trends for 2017 as sector bellwethers will report results. (The performance of a company that is considered a 'bellwether' may be indicative for the performance of a broader market.) Bellwethers reporting today or next week include industrials like General Electric, energy companies Schlumberger and Halliburton, and consumer goods companies Procter & Gamble and Unilever.

Bond markets update

Bond yields were up in the later part of the week, as the Federal Reserve hinted towards more rate hikes. In addition, the Fed is contemplating to no longer reinvest coupons and redemptions it receives on a still sizeable amount of USD 2.5 trillion in Treasuries. The Fed's preference for tighter monetary policies comes from a strong US consumer inflation print, even if you strip out volatile items such as oil and food. Therefore, the Fed's aspirations alone would suffice in lifting rates. Trump's fiscal stimulus would then serve as a 'bonus' for even higher rates.

Although German yields were also up this week, the European Central Bank (ECB) indicated on Thursday it will continue its monetary strategy as confirmed in December. Headline inflation in Europe is edging higher. The ECB, however, pointed out that core inflation in the eurozone remains low. We maintain our negative view on core European government bonds.

The purchase of corporate bonds by the ECB has already come down by a third, running ahead of scheduled reduction in total purchases from April onwards. Supply of new corporate bonds remains strong, as issuers aim to refinance their debt before interest rates go up again. Nevertheless, European credit spreads remain flat due to continued investor appetite for risk. Investors are willing to buy European credits, as company fundamentals remain solid: European corporates maintain healthy balance sheets and the number of pending merger & acquisition (M&A) deals has come down. We see credits being fairly valued and await how Trump's plans are translated into policies before we alter our position.

Rating agency DBRS aligned with the major rating agencies and downgraded Italy's credit rating to BBB last week. This action hardly had any impact on sovereign spreads, as the reasons behind the downgrade were well known. This event does not require a change in our portfolio positions, because

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	1.24	4.0	41.2
German Bunds 2-year	-0.70	2.9	-27.9
Japan 2-year	-0.24	-1.4	-22.9
US Treasuries 10-year	2.50	10.4	51.8
German Bunds 10-year	0.40	6.0	-8.5
Japan 10-year	0.06	1.3	-15.4

Spreads

	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	66.10	0.34	-48.36
iTraxx Euro 5-year	69.26	0.92	-30.25
JPM EMBI+	350.78	-4.58	-106.67

Performance data as of Friday, 20 January 2017
Source: Bloomberg

Corporate earnings calendar

	Date
Schlumberger, General Electric, Procter & Gamble	20 Jan
Halliburton, McDonald's, Yahoo!	23 Jan
Samsung Electronics, Johnson & Johnson, Verizon Communications, SAP, Philips, Du Pont, 3M, Texas Instruments, Alcoa, Stryker	24 Jan
Boeing, Banco Santander, Qualcomm, Rockwell Automation, Abbott Laboratories, Ebay, AT&T, Novartis	25 Jan
Google, Sligro Food Group, LVMH Moët Hennessy Louis Vuitton, Comcast, Praxair, Celgene, Baker Hughes, Intel, Microsoft, Mead Johnson Nutrition, Caterpillar, Ford, Dow Chemical, Starbucks, Unilever	26 Jan
Nextera Energy, Honeywell International, Colgate-Palmolive Company, Chevron	27 Jan

the ECB can continue to support governments should need arise. If you want to read more about our view on Italy: our Bond Markets Quarterly (published on 17 January 2017) includes a special on Italian debt sustainability, in which we explain why an escalation remains unlikely.

Macro update

At Thursday's meeting, the ECB kept its monetary policy rates, its plan for asset purchases and its forward guidance unchanged as expected. In the press conference following the decision, President Mario Draghi advocated accommodative monetary policy. He played down the recent rise in headline inflation and the higher than previously expected outlook for inflation over the next 2-3 quarters. He said that the ECB

would “continue to look through changes in inflation if judged to have no implications for the medium-term outlook for price stability.” This was currently the case, given that there was no convincing upward trend in underlying inflation. In addition, underlying inflationary pressures – and specifically nominal wage growth – remained subdued.

Draghi also said the ECB continued to see the risks to the economic outlook as being skewed to the downside and that a “very substantial degree of monetary accommodation is needed for euro-area pressures to build up and to support headline inflation in the medium term.” All this suggests that the ECB sees no reason to change the current trajectory for asset purchases and Draghi confirmed that the Governing Council had not discussed tapering.

Our base case is that the ECB will continue its asset purchases at the current pace until March 2018, before tapering from April onwards by EUR 10 billion a month. That would bring the programme to an end by September of next year. This is based on the view that core inflation will go up around the turn of 2017-2018.

Currencies outlook

Sterling rebounded strongly across the board because UK Prime Minister Theresa May’s speech on Brexit was somewhat more constructive than feared. GBP/USD rallied by close to 2.2% while EUR/GBP dropped by 1.3%. With May’s speech behind us, there are important releases that will determine the fate of sterling in the short term, such as a UK employment report on Wednesday and retail sales on Friday. Higher-than-expected numbers should result in a further recovery of sterling across the board. Once hard Brexit fears start to fade again and ECB easing and political uncertainty push the euro lower, EUR/GBP could move below 0.80 again.

Ahead of Donald Trump’s inauguration, the US economy continues to gain momentum. A stronger economy, together with Trump’s election pledges on tax cuts and wider fiscal stimulus, has had a positive impact on financial markets. However, uncertainty regarding the policies that Trump will effectively deliver has made markets jittery lately. Uncertainty for the US dollar increased this week, after Trump told the Wall Street Journal that the US dollar is too strong in part because China holds down its currency. However, we think that stronger US growth on the back of stimulus policies, three Fed rate hikes this year, together with the ECB’s accommodative policy and eurozone political uncertainty will likely push the US dollar higher. Therefore, we continue to expect that EUR/USD will break parity and reach 0.95 in the first half of 2017.

Asset allocation

ABN AMRO’s Global Investment Committee, at its meeting on 12 January, decided to maintain its positive view on equities, its cautious stance toward bonds and a large position in cash. Within alternative investments, we remain positive on commodities and real estate, and neutral on hedge funds. We have made two changes within our equity sector positioning. The consumer discretionary sector was increased to positive from neutral; and health care was reduced to neutral from positive.

Published this week

Investment Strategy: Positive start of the year

Sentiment in markets is positive, already since the end of 2016. Market sentiment is buoyed by growing confidence in global economic growth and the effect of a new president in the US who is focused on fiscal stimulus. Also, interest rates are not rising too quickly.

Bond Markets Quarterly: Policies in transition

The new year is starting with the prospect of policies in transition. The normalisation of interest rates, a new policy direction in the US and elections in Europe will attract more attention from bond markets than monetary policy.

Equity sector note: health care (neutral)

The health care sector has an attractive valuation, but is confronted with lacklustre pipelines. Also, increasing focus on cost control will slow medicine spending.

Equity sector note: consumer discretionary

We moved from a neutral to a positive view on consumer discretionary. We expect the sector to benefit from improving economic growth, higher consumer confidence and wage inflation in the US.

Investment Strategy & Portfolio Expertise Group Economics

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