

Global Weekly

Ready for take-off

**Investment
Communication
10 March 2017**

The US labour market reported an impressive monthly gain, in line with the US Federal Reserve's expectations. Now, financial markets have fully priced in a US rate hike in March.

Macro update

The US labour market continues to improve. February's ADP job report showed that private employment increased by 298,000 up from an increase of 246,000 in January, one of the strongest monthly gains of the series since inception in 2001. Job gains in activities that previously showed a difficult recovery, have been picking up strongly. Goods-producing employment improved, mainly in construction and manufacturing. Stronger hiring is likely driven by increasing business confidence, particularly among small and medium-sized businesses.

February's ISM manufacturing survey, an indicator of US economic conditions, recently published a slight slowdown in the employment component. Meanwhile, the ISM's services survey showed that job creation edged up slightly compared with the previous month.

Equity index performance in local currency

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	443.21	-0.7	5.1
S&P 500	2,364.87	-0.8	5.6
AEX Index	512.71	1.4	6.1
EuroStoxx 50	3431.92	0.8	4.3
DAX Index	12043.76	0.1	4.9
Nikkei 225	19604.61	0.7	2.6
Hang Seng Index	23568.67	0.1	7.1

Performance data as of Friday, 10 March 2017

Source: Bloomberg

Thursday, the European Central Bank (ECB) left its monetary policy rates and plans for its asset-purchasing programme unchanged, as expected. At the press conference, ECB President Mario Draghi laid the groundwork for a shift in forward guidance. Overall, the press conference suggests that the ECB will embark on a gradual path towards the exit in the coming months. We expect tapering from April 2018 onwards at a pace of EUR 10 billion per month. That would see the programme coming to a halt in September of next year. We

expect the first deposit rate hike in March 2019.

Bond markets outlook

The US Treasury yields curve rose in tandem, and is currently challenging its high levels of the last three months. This can push global bond yields higher. Yields were supported by stronger-than-expected US economic data, including, for example, the surprisingly large increase in jobs. If employment and inflation continue to evolve in line with expectations, Federal Reserve Chair Janet Yellen has signalled that a rate hike in March is likely.

At the moment, we continue to forecast three rate hikes in 2017. We expect a rate hike in March and two more rate hikes in June and September, but the risks are tilted towards a fourth rate hike. In 2018, we expect two rate hikes in June and September. The Fed median 2017 forecast is 1.375% (see the table below).

The Fed's rhetoric has changed from an earlier more patient tone. According to Yellen, the new tone reflects the "same strategy" but with "new tactics." She outlined three basic principles of conducting monetary policy: "goal driven," "forward looking" and "risk sensitive." Yellen said this strategy has been the same throughout the extremely gradual policy accommodation of the past few years. Yet, circumstances have changed, particularly with respect to risks. In the absence of major negative surprises, "the process of scaling back accommodation likely will not be as slow as it was during the past couple of years." The pace of the US Fed rate hikes could start market discussion if other leading central banks such as the Bank of Japan and ECB would join.

While global risks have receded, they have not been completely eliminated. Political jitters in Europe could resurface over the next few months amid elections in the euro area. The same goes for the US, if the Trump administration does not make meaningful progress on tax and regulatory reform in the next few months.

Currency outlook

A few weeks ago, we changed our US dollar view. We think that the uptrend is over. Despite this change, we decided to keep our long position USD versus JPY in place, as we

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	1.378	7.1	44.9
German Bunds 2-year	-0.854	-4.0	-39.9
Japan 2-year	-0.266	2.3	-9.4
US Treasuries 10-year	2.616	13.7	68.2
German Bunds 10-year	0.453	10.0	14.8
Japan 10-year	0.084	1.1	10.8

Spreads

	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	64.47	4.20	-30.07
iTraxx Euro 5-year	71.48	2.18	-12.80
JPM EMBI+	337.85	5.75	-70.22

Performance data as of Friday, 10 March 2017

Source: Bloomberg

Corporate earnings calendar

	Date
USG People	13 Mar
RWE, Prudential, Geberit	14 Mar
Dufry Group, Muenchener Rueckv, E.ON, Bilfinger Berger, Oracle, Cathay Pacific	15 Mar
Lufthansa, Heidelbergcement, Enel, Generali, AMB Generali	16 Mar
Fraport, Tiffany & Co, China Mobile, Beter Bed	17 Mar

expected a recovery in USD/JPY to levels above 115.00. This has materialised. Since the end of February, USD/JPY has rallied to above 115.00, mainly because of a modest rise in US real yields. We think that the upside in the USD/JPY is limited going forward. Therefore, we have closed our long USD versus JPY.

Equities outlook

As we near the end of a solid 2016 earnings-reporting season, equity markets are looking again at policymakers for direction this week. The increasing likelihood of an interest rate hike by the Fed was more seen as a sign of strong underlying growth in the US than as a threat to equity levels. Likewise, European equities were supported by the expectation that the ECB will hold on to an accommodative monetary policy.

Forecast US interest rates

	2016 Q4	2017 Q1	2017 Q2	2017 Q3	2017 Q4	2018 Q1	2018 Q2	2018 Q3	2018 Q4
Policy rate	0.75	1.00	1.25	1.50	1.50	1.50	1.75	2.00	2.00

Source: Private Banking International

US equity markets hovered around their all-time high levels in the past week. Year to date, stock market performance worldwide has been solid and evenly spread across the US, Europe and Asia regions. Concerns over the election in France seem to have eased somewhat. The main drivers -ongoing solid macro data, accelerating earnings and US growth policies- continue to be supportive, and, for investors, these drivers outweigh valuations that are getting stretched.

Last week, the health care sector was impacted by plans to change Obamacare in the US, which added to fears of expected further pressure on drug prices. Also, energy stocks were lower as higher inventory levels weighed on oil prices. In addition, large mergers and acquisitions captured the headlines, as Dutch paints and coatings maker AkzoNobel rejected an unsolicited proposal from US chemicals competitor PPG.

Asset allocation

The current asset allocation consists of a moderate overweight in equities, a strong underweight in bonds and a large overweight in cash. Within alternatives, there is an overweight to real estate, a neutral stance to hedge funds and no allocation to commodities.

Investment Strategy & Portfolio Expertise Group Economics

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