



Global Weekly

The Dutch and the Fed

Investment
Communication
17 March 2017

The US Federal Reserve rate hike and the positive outcome of Dutch elections were hot topics this week. Financial markets reacted positively but muted.

Macro update

In the Netherlands, ruling party VVD has won the Dutch elections and kept populist Party for Freedom (PVV) at bay. With upcoming elections in France and Germany, the outcome can be seen as a first victory against populism in Europe. The outcome of the elections immediately translated in an appreciation of the euro and equity markets and in a slight appreciation of bonds. The heart of the new cabinet will likely be centrist and formed by VVD, CDA, D66. With this election result, a referendum about the Netherlands leaving the European Union can be ruled out at least during the life of the new government.

In the US, the Federal Reserve (Fed) has raised its policy rates and maintains a gradual pace of rate hikes. As expected, Fed policymakers raised the target range for the federal funds

Equity index performance in local currency

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	421.8	1.5	7.1
S&P 500	2,238.8	0.4	6.4
AEX Index	483.2	1.1	7.0
EuroStoxx 50	3,290.5	1.1	4.9
DAX Index	11,481.1	1.2	5.5
Nikkei 225	19,114.4	-0.4	2.1
Hang Seng Index	22,000.6	3.1	10.5

Performance data as of Friday, 17 March 2017

Source: Bloomberg

rate a quarter point to 0.75-1% in the March meeting. The Fed's forecasts for the target range for interest rates show that the central bank continues to expect two additional rate hikes this year and two rate hikes next year. We expect that the Fed will continue to hike interest rates at a gradual pace, with the central bank hiking two more times this year, in June and September.

Equities outlook

Over the past week, equity markets were predominantly driven by the upcoming Fed meeting and the outcome of the Dutch elections. Regarding the Fed meeting, the focus was not so much on the rate hike itself as well as on the comments surrounding the rate hike. Markets worldwide welcomed that the Fed indicated not to step up the pace of interest rate increases. The Dutch elections also had a positive outcome, as in the end populism did not take hold. As a consequence, equity markets were slightly up.

From a sector perspective, the cyclically driven performance of markets continued at a more moderate pace than before. Financials recouped some lost ground in Europe. Meanwhile, the energy sector lagged as the oil price fell below USD 50. Also, defensive sectors continued to stay behind, albeit to a lesser extent than in earlier months. Both health care and consumer staples showed some reversion to the mean.

On balance, the backdrop for equity markets continues to be supportive. Drivers are robust macro fundamentals pointing to a synchronised global upturn, softly rising interest rates – but still low in absolute terms – and solid double digit earnings growth for 2017 in the pipeline. Political risks, also in Europe, appear to have abated. At the same time, investors continue to be on the lookout for more information on Trump's plans on budget and tax reforms. Announcements on these subjects could potentially be market moving in the weeks to come.

Bond markets outlook

US Treasuries, moving inversely to bond yields, surprisingly rallied after the Fed decision to raise rates. The market actually expected a decline in bond prices. The central banks of Japan and England stayed put, as they wait for core inflation numbers to exceed their thresholds. The central banks' actions and guidance are in line with our view that interest rates will continue to rise, although normalisation will not be straightforward. Investors are therefore advised to continue their underweight in core government bonds.

In Europe, the growth picture is nascent. However, risks related to European populism cannot be completely ignored, despite a short-lived relief rally after the Dutch elections.

Credit spreads on US high yield have crept up by nearly 50 basis points (bp) since early March. Investors are becoming nervous about the risk/reward level. In our view, there is no need for this anxiety, as spreads are still quite off the all-time lows and fundamentals remain reasonable.

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	1.32	-3.3	45.8
German Bunds 2-year	-0.78	5.8	-31.3
Japan 2-year	-0.26	0.6	-4.7
US Treasuries 10-year	2.52	-6.0	61.9
German Bunds 10-year	0.45	-3.4	21.8
Japan 10-year	0.07	-1.4	12.2

Spreads

	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	61.71	-2.69	-21.47
iTraxx Euro 5-year	69.98	-2.12	-1.52
JPM EMBI+	333.19	-4.66	-71.83

Performance data as of Friday, 17 March 2017

Source: Bloomberg

Corporate earnings calendar

	Date
China Steel Corp	20 Mar
BMW, Beijing Capital Intl Airport, Cheung Kong Infrastructure, China Resources Beer, China State Construction, China Telecom Corp, FedEx, Henderson Land Development, Hengan, Huaneng Power, Lennar Corp, Nike Inc, Petroleo Brasileiro, Power Assets Holdings	21 Mar
Cheung Kong Property Holding, China Overseas Land & Invest, China Resources Land, CK Hutchison Holdings, Kuka, Ping An Insurance Group, PVH Corp, Tencent Holdings	22 Mar
Accenture, Aluminum Corp Of China, Anhui Conch Cement, China Life Insurance, China Mobile, China Resources Power, CNOOC, Telecom Italia	23 Mar
China Merchants Bank, China National Building Ma, China Petroleum & Chemical, Great Wall Motor Company, PICC Property & Casualty, Zijin Mining Group	24 Mar

Currency outlook

Ahead of the Fed decision, financial markets were positioned for a 25 bp rate hike and for a stronger tone-of-voice in the statement – by changing the wording and by an upward adjustment in its forecasts. The Fed did not meet these expectations, signalling a gradual approach – with two more rate hikes this year – instead. As a result, US Treasury yields and the US dollar

declined. The US dollar is struggling. It failed to rally on strong data and higher nominal yields, as inflation expectations also rose. Meanwhile, a less strong Fed has weighed on the US dollar. It is likely that the US dollar rally has come to an end and that more downward pressure is building in the near term.

Asset allocation

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

Published this week

Market Comment - Ruling party VVD wins Dutch elections

The VVD win has kept the populist Party for Freedom (PVV) at bay. With upcoming elections in France and Germany, the outcome can be seen as a first victory against populism in Europe.



Bond Sector Note Basic Materials – Steadiness after recovery

Although we did see base metals performing very well, we continue to apply a neutral position for basic material industries as fundamentals move sideways.



Investment Strategy & Portfolio Expertise Group Economics

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