

Global Weekly

Bump in the road

Investment
Communication
24 March 2017

Equity markets retreated this week, with US stocks on Tuesday plunging the most since October. Investors sought refuge in bonds, pushing Treasury yields lower.

The patience of investors is being tested by US President Donald Trump, as growth-supportive initiatives, like Trump's "phenomenal" tax plan and the dismantling of ObamaCare, are still not presented. Stock markets declined globally, with investors taking profits and entering a wait-and-see mode. Financial players retreated most, as the sector was impacted by declining interest rates. The utilities sector was the best performing sector this week. Utility companies tend to benefit from lower interest rates.

The earnings season is coming to an end. This week, Nike and FedEx presented their results. Nike disappointed, as the company is losing market share to Adidas and Under Armour. Nike is known for its ability to leverage its brand name to increase profit margins. But now that online shopping is gaining more attention from consumers, the company is forced to offer more discounts to boost sales. FedEx reported earnings that were below expectations. However, we think

Equity index performance in local currency

	Value	One week change (%)	Year-to-date (%)
MSCI ACWI	447.5	-0.8	6.1
S&P 500	2,346.0	-1.4	4.8
AEX Index	512.6	-0.7	6.1
EuroStoxx 50	3,452.2	0.1	4.9
DAX Index	12,039.7	-0.5	4.9
Nikkei 225	19,085.3	-2.2	-0.2
Hang Seng Index	24,327.7	0.1	10.6

Performance data as of Thursday, 23 March 2017

Source: Bloomberg

the company is moving in the right direction. FedEx's margins are improving, the company has the capability to benefit from its superior infrastructure and the integration of TNT is well on track.

In the Netherlands, chemicals company AkzoNobel was in focus. US-based chemicals player PPG approached AkzoNobel for a second and third time this week, in an attempt to acquire

the Dutch company. All offers were rejected instantly, as Akzo believes current bids do not reflect its actual value and that the takeover proposal would lead to job losses. Investors seem to lose faith in the possibility of a takeover deal, as the stock declined 2% after the last rejection. AkzoNobel currently trades approximately 12% below the latest offer.

Bond markets update

Investors are getting uncertain about Trump's economic ambitions, ending a period of relative calm and rising stock markets. This week, the 'reflation trade' hit a hard bump. When trying to get his pro-growth policies through Congress, Trump may face more difficulties than investors previously expected. Longer-dated US Treasury yields slumped by approximately 10 basis points this week and credit risks increased. US high-yield spreads increased by around 40 basis points this month and are now above 415 basis points.

In Europe, the picture seems to be improving. After the elections in the Netherlands and Marine Le Pen's unconvincing performance in a television debate, worries about the rise of populism in Europe have faded. However, the yield differences between the peripheral countries (including France) and Germany are not yet declining. This probably has to do with recent rumours about the European Central Bank (ECB) considering a different strategy for exiting its accommodative policy.

Currently, the ECB maintains a hyperstimulative policy, including negative policy rates. Speculation has been that the ECB might actually hike interest rates before it ends its quantitative easing measures. The central bank could do this by hiking its deposit rate. The current low level of the deposit rate is problematic for banks, as it hurts their profits and forces them to re-invest their excess cash in predominantly high-quality assets like government bonds. However, the ECB's quantitative easing efforts are reaching their pre-defined limits. This means that, currently, the ECB would not be able to offset a premature tightening of financial conditions caused by higher rates. We therefore continue to expect that the ECB will only start lifting the deposit rate after tapering its quantitative easing programme. Nevertheless, speculation around this topic is pushing up euro yields to some extent. European financial bonds are benefitting as well.

This does not rule out the possibility of another shift in geographical sentiment anytime soon. Trump might still score in the short term, and the political climate in Europe is far from stable. To be continued.

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	1.271	-4.7	40.0
German Bunds 2-year	-0.737	4.5	-25.2
Japan 2-year	-0.264	-0.4	-4.8
US Treasuries 10-year	2.433	-6.8	53.2
German Bunds 10-year	0.436	0.4	25.7
Japan 10-year	0.060	-1.0	15.0

Spreads

	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	67.98	6.73	-15.31
iTraxx Euro 5-year	76.06	6.46	-0.56
JPM EMBI+	333.00	-0.19	-62.25

Performance data as of Friday, 24 March 2017

Source: Bloomberg

Macro update

Francois Villeroy de Galhau, the Governor of the Banque de France and a Governing Council member of the ECB, struck a dovish tone during a speech in Frankfurt on Wednesday. Villeroy mused whether "given this progress, should we stop pursuing an accommodative monetary policy?" He concluded that "at this stage, the answer is clearly no." He noted recent positive developments, arguing that "the recovery is also broadening across euro-area countries, including in France: despite some temporary political uncertainty generated by the upcoming elections, France's economic outlook is improving." On inflation, Villeroy judged that "we have warded off the mortal danger of deflation, and inflation is gradually recovering in the euro area."

However, Villeroy's key argument was that "without monetary stimulus, the recovery in inflation would not yet be self-sustained or durable throughout the euro area." The French central bank governor's comments come against the background of a raging debate between members of the ECB's Governing Council. Ewald Nowotny has made the case for rate hikes before quantitative easing ends, while Ignazio Visco has argued that a shorter period between the end of quantitative easing and the first rate hike might be appropriate. On the other hand, ECB Chief Economist Praet has said there is a strong logic to the current dovish forward guidance, and Villeroy seems to be supporting his stance. We expect the ECB to taper asset purchases during the course of 2018, with the first rate hike following early in 2019.

Currencies outlook

One of the key questions we get asked on currencies is whether we should expect another downward leg in sterling (the British pound). We think most of the weakness is behind us and expect GBP/USD to stabilise around current levels this year. One reason is that we expect Brexit talks to make some progress towards a kind of compromise deal, balancing free trade and free movement of people.

Perhaps more importantly, a lot of bad news is already in the price. Sterling has not hit new lows on a trade-weighted basis (the low was set on 12 October 2016). In fact, sterling has been very resilient in the recent past. It has not weakened substantially when negative Brexit-related news came to the fore again and UK economic data came in weaker than expected. In contrast, sterling tended to respond positively to supportive news such as stronger-than-expected UK data.

As sentiment in financial markets is relatively constructive and political risks are in the US and in the eurozone, sterling is mainly moving on cyclical news. It strengthened on Tuesday's higher-than-expected inflation data, as the economy is pretty resilient. Overall, sterling's behaviour signals that most of the negative news and Brexit uncertainty is reflected in the price.

Asset allocation

ABN AMRO's Global Investment Committee decided to leave the asset allocation unchanged at its meeting on 16 March. The euro hedge on US-dollar denominated portfolios, however, was lifted. This is owing to stabilisation of the dollar and expected range-trading for the euro versus the US dollar. Within the asset allocation, equities are preferred over bonds; and within alternatives, real estate is preferred, while a neutral stance is taken to hedge funds. In February, ABN AMRO recommended reducing commodity holdings to zero.

Published this week

Investment Strategy: Still a preference for stocks

The global economy and equity markets in general continue to be supported by a number of positive factors. ABN AMRO's preference for stocks over bonds remains in place.



Investment Strategy & Portfolio Expertise Group Economics

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