

Global Weekly

# Room for optimism

**Investment  
Communication  
5 May 2017**

Equity markets gained further territory this week, especially in Europe. Bond yields – moving inversely to prices – also rose, as demand for safe havens declined.

We have recently become more positive over the outlook for stocks. Political risks have now abated, and the economic recovery in Europe is strengthening. We therefore suggest that clients consider building their stock positions in line with renewed optimism for equity markets.

## Macro update

The eurozone economy probably continued to grow robustly in the first quarter of this year. Eurostat, the statistical office of the European Union, on Wednesday published its preliminary estimate of first-quarter GDP growth. According to Eurostat, the eurozone economy grew by 0.5% quarter-on-quarter, which is in line with our expectations.

Zooming in on the components of GDP (which will be published in early June), we think that private consumption growth slowed down in the first quarter, due to a combination of a jump in (food and energy) inflation and modest wage

## Equity index performance in local currency

	Value	One week change (%) <sup>*</sup>	Year-to-date (%)
MSCI ACWI	457.1	0.4	8.3
S&P 500	2,389.5	0.2	6.7
AEX Index	528.4	1.4	9.4
EuroStoxx 50	3,627.9	1.9	10.3
DAX Index	12,647.8	1.7	10.2
Nikkei 225	19,445.7	1.3	1.7
Hang Seng Index	24,683.9	0.3	12.2

<sup>\*</sup>Thursday close compared with Friday last week

Performance data as of Thursday, 4 May 2017

Source: Bloomberg

growth. Still high levels of business confidence and improving corporate profitability should have supported investment in the first quarter of the year. Finally, exports should have benefitted from global trade gathering traction and the decline in the trade-weighted euro since the middle of last year.

In the US, the Federal Reserve (Fed) struck a positive tone in its statement delivered after the 3 May meeting, despite

recent weaker data. The adjustments made to the statement tried to capture the strong underlying economic fundamentals, while suggesting that the economic slowdown is likely to be transitory. We think that with this message, the Fed is trying to leave the door open for a rate hike in June. Ahead of the release, the Federal funds futures – the odds for a rate hike in June – were 70% and after the statement the odds jumped to around 93%. We still expect two rate hikes this year, one in June and another in September.

## Equity markets update

This week, equity markets were mostly dominated by the first-quarter earnings season. So far, the results are encouraging and coming in somewhat ahead of expectations. Especially European companies' results reveal a rather strong picture, with both net earnings and revenues showing solid growth. This could be proof that Europe is indeed gaining more traction. Positive earnings trends are an important reason for our optimistic stance towards equities.

Politics have moved a little bit to the background: Trump's announcement on 'big' tax reforms was considered to be a non-event and the second round of the French elections is expected to have a market-friendly outcome. It seems the swing factor in the elections is not so much if Macron wins, but by what margin. A landslide victory for Macron could give European markets another boost.

In terms of equity performance, Europe and emerging markets maintain their lead over the US, which fits well into our decision to overweight the former two regions. On balance, the fundamental situation continues to be supportive for equity markets, with positive incoming macro data and encouraging earnings developments. Moreover, political risks in Europe are decreasing. A positive equity stance therefore remains warranted, in our view.

## Bond markets update

Bond yields edged further upwards this week, despite inaction by the Fed and ECB. Markets seem convinced – as are we – that rate hikes and communication about tapering will become reality in the foreseeable future. Investors were not deterred by mixed economic data reflected in surveys, spending indicators and supply-driven inflation indices. The bond market is less certain about the outlook for inflation, which is reflected in the cheap price levels of inflation-linked bonds.

Last week's relief in the European periphery – following the first round of the French elections – had some additional room to run, especially in Spain where we also saw encouraging economic data. High-yielding corporate bonds also benefitted

## Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	1.31	4.8	59.2
German Bunds 2-year	-0.72	2.1	-20.7
Japan 2-year	-0.20	0.0	3.9
US Treasuries 10-year	2.36	7.6	61.1
German Bunds 10-year	0.37	5.5	20.9
Japan 10-year	0.02	-0.2	14.5

## Spreads

	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	63.25	-0.79	-21.25
iTraxx Euro 5-year	64.24	-2.36	-14.67
JPM EMBI+	323.83	-2.81	-72.77

Performance data as of Friday, 5 May 2017

Source: Bloomberg

## Reporting calendar

China Steel, Intl Flavors & Fragrances, PostNL	08 May
Adecco Group, Allergan, Commerzbank, Continental, Duke Energy Corp, Electronic Arts Inc, Muenchener Rueckversicherungs, Symrise, Priceline Group	09 May
Koninklijke Ahold Delhaize, Aperam, Ctrip.com International, Eni Spa, HeidelbergCement, Mylan, Suez, Toyota Motor, Twenty-First Century Fox	10 May
AP Moller-Maersk, Aegon, BT Group, Crédit Agricole, Deutsche Post, Deutsche Telekom, Henkel, Lanxess, Mobileye, Petroleo Brasileiro, ProSiebensat.1 Media, Telefonica, Teva Pharmaceutical, Vivendi	11 May
Allianz, ArcelorMittal, Cie Financiere Richemont, Thyssenkrupp	12 May

from better-than-expected earnings data posted by cyclical companies and a lower level of new issues. Basic materials stocks suffered this week from a drop in metal prices. Credit spreads, by contrast, were not affected. This confirms our view that strengthened balance sheets will enable basic materials companies to weather headwinds.

## Currencies special: Norwegian krone

The Norwegian krone had a good start to the year and appreciated by close to 3% in the first two months of 2017. Then, its fortunes changed dramatically. Since 22 February, the Norwegian krone has lost more than 7%. What has happened? First, all possible positive news was reflected in the price and the Norwegian krone did not rise anymore on positive news. As a result, investors started to close some of their long

positions. Second, the oil price came under pressure in March, which resulted in more profit-taking in the Norwegian krone. The krone has a strong tendency to move in tandem with oil prices, as weaker oil prices result in a downward adjustment in expectations about the Norwegian economy and future monetary policy.

Third, on 10 March, inflation came in far below expectations, resulting in a downward adjustment in expectations about monetary tightening this year and next year. Fourth, the 10-year government yield bond spread between Germany and Norway has narrowed, making the krone a less attractive investment. Last but not least, optimism about an EU-friendly election outcome in France has calmed investors' nerves. As a result, the euro has recovered and investors became less motivated to diversify out of the euro into a non-eurozone (European) currency such as the Norwegian krone.

Up to now, we believed that the Norges Bank, Norway's central bank, would deliver two rate hikes of 25 basis points each this year. However, given recent developments, this has become unlikely. Therefore, we now expect that the Norges Bank will hike interest rates early next year. Our new EUR/NOK forecasts reflect this change in view. Our new year-end forecasts for 2017 and 2018 in EUR/NOK are 9.25 (previously 8.5) and 8.5 (previously 8.0), respectively.

Even though the current momentum is negative, we are optimistic about the krone's outlook. For a start, we expect Brent oil prices to rise to USD 60 per barrel before the end of the year. This should give strong support to the Norwegian krone. Moreover, we don't expect a sharp drop in inflation, and we expect the economy to perform well. Furthermore, in the coming weeks and months investors will probably realise that the Norges Bank is likely to raise interest rates before the ECB does. This should also support the krone. What is more, the fundamentals of the Norwegian krone are pretty strong. In short, we would use further weakness in the krone versus the euro as an opportunity to position for strength later this year and next year. At the moment it is too early to position; we are waiting for more extreme conditions. For example if EUR/NOK moves towards 9.75.

## Asset allocation

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

## Published this week

### Investment Strategy: Renewed optimism for equities

ABN AMRO has moved further in favour of equities, advising clients to consider increasing stock holdings, particularly in regions that have lagged the economic recovery and are now catching up. Bond markets remain unattractive, given the prospect of rising bond yields.

## Investment Strategy & Portfolio Expertise Group Economics



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