

Global Weekly

Troubles for Trump

**Investment
Communication
19 May 2017**

In the US, political turmoil around President Donald Trump continued and his tax reform plans seem further away than ever. As a result, financial markets declined.

Equity markets

This week, the equity market suffered its worst days in eight months. The S&P Index as well as the European Stoxx 600 Index lost around 2%. The New York Times reported that a memo from fired FBI Director James Comey revealed that US President Donald Trump had asked Comey to stop the FBI's investigation into National Security Advisor Michael Flynn's ties to Russia. If this is true, Trump could face difficult times, as the president is not allowed to obstruct these kind of investigations. The likelihood of this scenario is hard to assess. In the meantime, however, Trump will be distracted from important key topics such as tax reforms and infrastructure investments.

In Brazil, it was reported that President Michel Temer was allegedly involved in a cover-up scheme with the jailed former speaker of the Lower House of Congress, Eduardo Cunha. There is probably a recording of Temer approving an illicit

Equity index performance in local currency

	Value	One week change (%) [*]	Year-to-date (%)
MSCI ACWI	456.29	-0.7%	8.2%
S&P 500	2,365.72	-1.1%	5.7%
AEX Index	524.52	-1.9%	8.6%
EuroStoxx 50	3,562.22	-2.1%	8.3%
DAX Index	12,590.06	-1.4%	9.7%
Nikkei 225	19,553.86	-1.7%	2.3%
Hang Seng Index	25,136.52	-0.1%	14.3%

Performance data as of Thursday, 19 May 2017

Source: Bloomberg

payment. If true, his position is unstable and many positive reform policies could be halted. Markets reacted fiercely. The Brazilian real and European-listed Brazil ETFs dropped on Thursday by double-digit numbers.

This week, investors took profit in sectors and regions that have performed well in the last months such as IT and European equity. Tencent and Alibaba, both large Chinese social media

and e-commerce platforms, reported their quarterly results. Tencent's results were far better than expected. Revenue increased by 55% compared with a year ago. In addition to online games, new business lines such as cloud computing showed strong gains, growing from 7% to 15% of total revenue. Alibaba missed on earnings due to higher taxes, but its revenues were 60% higher than last year. E-commerce is still the dominant driver, but new developed businesses based on cloud and artificial intelligence are on the rise.

Bond markets update

Bond prices came down strongly this week. This was chiefly caused by political upheaval in the US. Investors are becoming less convinced that the US administration will be able to deliver the fiscal stimulus it has been promising. Also, ECB officials hinted that normalization of monetary stimulus in the eurozone will continue to be gradual.

The latest episode in the Trump drama will make it even more difficult for fiscal policy to receive the necessary attention. For some time now, markets have taken into account that fiscal stimulus might not happen. So did we and we continue to see fiscal stimulus as icing on the cake. We still remain underweight in core government bonds. Notwithstanding fiscal stimulus, the economic backdrop in the US and Europe still favours riskier bonds. Corporate credits still fare well at reasonable levels of growth. Inflation-linked bonds and duration hedges should work out well when the economic cycle starts to mature and central banks need to tighten more aggressively.

China managed to relieve markets somewhat as the Chinese central bank pushed liquidity into the system and refrained from increasing short-term rates. This confirms our view that the central bank is orchestrating monetary tightening to evade a material impact on the real economy, but still is achieving the necessary de-leveraging to keep away from asset price bubbles.

Currencies outlook

For the euro, we expect more strength versus the US dollar in 2017. EUR/USD has risen by more than 5.5% since the start of this year and the pair has now broken above our year-end forecast of 1.10. We expect more dollar weakness and euro strength this year. A Fed rate hike of 25 basis points (bp) in June is fully discounted and a 25 bp rate hike in September is priced in for around 50%. So while we expect two further rate hikes this year, it is unlikely that this will provide strong support for the US dollar. Meanwhile, the market will continue to focus on ECB tapering and this should support the euro

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	1.293	0.0	40.9
German Bunds 2-year	-0.690	-0.6	-18.2
Japan 2-year	-0.165	1.6	6.5
US Treasuries 10-year	2.248	-7.9	39.8
German Bunds 10-year	0.360	-2.8	19.1
Japan 10-year	0.035	-0.4	11.0

Spreads

	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	64.54	1.81	-20.94
iTraxx Euro 5-year	62.92	-0.14	-17.39
JPM EMBI+	33787	17.64	-44.79

Performance data as of Friday, 19 May 2017

Source: Bloomberg

Reporting calendar

Tingyi (Cayman Isl) Holding	22 May
China resources beer holding, Tata Motors Ltd-Spon ADR	23 May
China state construction int, PVH Corporation, Tiffany & Co, HP Inc.	24 May
Aristocrat Leisure Ltd, Lenovo Group Ltd, Medtronic Plc	25 May

going forward. Moreover, the negative headlines about the Trump administration will probably remain. This could result in another 4% decline in the dollar versus a basket of currencies.

What will likely dampen the strengthening in EUR/USD, however, is a refocus on political uncertainty and poor fundamentals in Italy later this year. Still, our new year-end 2017 forecast is 1.15 (from 1.10). For 2018 we leave our year-end forecast unchanged at 1.20.

Macro update

Eurostat published this week the second estimate for eurozone economic growth in first quarter as well as the rates in the individual countries. Growth in the eurozone remained unchanged from the first estimate, at 0.5% q-o-q, the same rate as in the fourth quarter. At the individual country level, differences remain, with Greece moving back into recession (-0.1% q-o-q), while Spain (0.8% q-o-q) and Portugal (1.0% q-o-q) are outperforming the eurozone by a wide margin. We found that, although differences remain, there has been a broader trend of growth convergence in recent years.

Recent macro data support our view that China's economic growth peaked in the first quarter and is likely to resume a gradual slowdown from the second quarter onwards, as Beijing has stepped up its targeted tightening policies. Purchasing manager's indexes, imports and car sales data for April published earlier this month already indicated that the momentum has turned. The monthly macro data published this week pointed in the same direction. Given Beijing's balanced approach to fine-tuning policy, we still expect growth to resume a gradual slowdown.

Asset allocation

Our overall asset allocation consists of a strong overweight in equities, a large 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: Positive environment for equities

At its meeting on 11 May, ABN AMRO affirmed the existing asset allocation. Equities continue to be favoured over bonds. The view on real estate is also positive and commodities are avoided. A neutral stance is taken toward hedge funds. Within bond portfolios, ABN AMRO suggests taking profits in Italian government bonds and using the proceeds to invest in European inflation-linked bonds.



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