



global weekly

Investment
Communication
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Central banks point the way

This week the Federal Reserve and the ECB both tried to steer markets. The Fed wants to prepare markets for an exit from its highly accommodative monetary policy, while the ECB is studying ways to fight uncomfortably low inflation. The outcomes of PMI surveys in the eurozone, China and the US did not contain any surprises. Chinese equities performed well on positive news from the Communist Party Conference. Bond markets saw a lot of new issuance. The dollar rose, whereas the euro was under pressure.

This week, Fed Chairman Bernanke needed to convince markets that tapering does not automatically mean that interest rates will be hiked, whereas ECB President Draghi tried to temper expectations of a cut in the ECB's deposit rate.

The FOMC minutes of the October meeting show that the Federal Reserve (Fed) is ready to start scaling back its bond purchasing programme in the coming months. This is in line with our expectation that the Fed will start to taper in March 2014. The minutes also revealed that the Fed considers strengthening its forward guidance about keeping interest rates low. Earlier in the week, Fed chairman Bernanke said that rates will remain low until long after the bond purchasing programme has ended. By emphasising this, he hopes that financial markets will not automatically pencil in a rate hike when the Fed starts tapering. We expect US yields to remain close to their current level for the remainder of the year, as the Fed will shift from its bonds buying programme to a stronger forward guidance. Later in 2014 and 2015, we expect US rates to rise, reflecting the growth acceleration of the US economy.

ECB President Mario Draghi tried to cool expectations of an imminent cut in the deposit rate in a speech to a business conference in Berlin on Thursday. Referring to the possibility of a negative deposit rate, he said that this was discussed at the last Governing Council meeting but that "there is no news since then". This is in line with reports suggesting that the ECB had considered the option of a mini deposit rate cut in case the downside risks to inflation would have grown, rather than as an imminent step. The central bank also seems to be giving some thought to quantitative easing in the same way, but is for now still in the orientation phase. We expect interest rates

Equity index performance in local currencies

	Value	One week (%)	Year-to-date (%)
MSCI ACWI	398.78	-0.3	17.4
S&P 500	1795.85	0.3	25.9
EuroStoxx 50	3044.34	0.0	15.9
DAX	9196.08	0.5	21.0
Nikkei 225	15381.72	1.4	48.0
Hang Seng Index	23696.28	2.9	4.6

Important rating changes

Company	From	To
Coca-Cola	Buy	Buy/RL
Deere	Hold	Buy
Swatch	Buy	Hold
Yahoo!	Hold	Sell

Government bond yields

	Yield (%)	One week (bp)	One year (bp)
US Treasuries 2-year	0.274	-1.6	0.4
German Bunds 2-year	0.111	1.1	10.6
Japan 2-year	0.092	0.5	0.4
US Treasuries 10-year	2.787	9.7	110.7
German Bunds 10-year	1.769	7.0	33.9
Japan 10-year	0.618	2.6	-10.7

Spreads

Index	Spread (bp)	One week (bp)	One year (bp)
CDX NA IG	70.39	-1.52	-30.11
iTraxx Euro 5-year	81.10	-1.37	-44.60
JPM EMBI+	350.55	-6.14	76.51

Performance data is as of 12:00 pm Friday, 22 November

Source: Bloomberg

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in Europe to stay low throughout 2014 and 2015, as inflation and economic growth remain subdued.

The eurozone PMI surveys for November confirm that the eurozone's economic recovery remains lacklustre, keeping the pressure on the ECB to ease its monetary policy further. The composite PMI (covering the whole eurozone economy) edged down for the second successive month. At current levels, the composite is consistent with a GDP growth of around 0.2% quarter-on-quarter, which is roughly in line with the growth rates we have seen in the last couple of quarters. China's PMI slipped to 50.4 from 50.9 the month before, but the level remains relatively high, consistent with the economy maintaining recent growth rates in the 7.5-8% region. The Markit US manufacturing PMI increased to 54.3 from 51.8, which marked an eight-month high. We continue to believe that stronger global economic growth lies ahead, led by the US.

Bond markets update

Companies are using the final weeks of the year to tap the primary market. After a slow October, new issuance in the non-financial segment picked up significantly in November. This new supply is well absorbed by investors and did not lead to a re-pricing in the secondary market. Most new bonds came from strong companies in the investment-grade universe and were issued without a significant premium compared to existing bonds.

Telecom Italia was downgraded by S&P to sub-investment grade, after management failed to convince the rating agency with its plan to strengthen its balance sheet. Counter-intuitively, credit spreads of Telecom Italia tightened. This can be largely explained by the fact that this downgrade was well anticipated by the market. Telecom Italia bonds will now be added to the high-yield benchmarks and subsequently to high-yield investment portfolios. We see Telecom Italia as a BB+ credit in the next 18 months and assign a neutral rating. Telecom Italia is on our Opportunistic Credit List.

Equity update

Equity markets moved somewhat higher over the week. Chinese stocks, Hong Kong-listed H shares in particular, staged a very convincing rally of some 7%, as more details of the decisions made at the Communist Party Conference were revealed. They show that the country is moving in the direction of a market-oriented economy, with greater freedom for financial institutions, less subsidies for state-controlled companies and a wider currency fluctuation band. The one-child policy will be further relaxed to stem the adverse demographic developments. Higher wealth levels will also help in turning the demographic trend. Baby product makers (baby milk, diapers, baby care products, etc.) were immediately marked up. The longer-term effects of a growing population on consumer demand are, of course, also very positive.

Although it may seem that equity markets are winding down and getting ready for the Christmas break, behind the scenes there is still a lot of action. A host of new companies are being listed on the market, with Twitter drawing the most attention. Hilton Hotels is also preparing for a public listing. Parallel to this, large, 'dusty' conglomerates are waking up to the calls of investors and are, sometimes reluctantly, beginning to focus on their core again, in a reversal of the strategy that made them big in the first place, by divesting non-related businesses. Examples are 'Big Pharma' companies, such as Pfizer (Hold), which is preparing for a likely break up into two or three different entities, and Novartis (Hold), which just announced a large share buy-back programme. Another example is energy company Devon Energy (Buy/RL), which is spinning off undervalued parts of its business. So, besides the more obvious stocks that will benefit from good growth prospects as the global economy moves into a new expansion phase, there is also much to gain from the trend of unlocking shareholder value. This trend has the advantage that it is less sensitive to market sentiment, which can be very volatile.

Currency outlook

At the start of the week, the dollar was on the defensive, because markets expected the Fed to keep interest rates low for longer. Recent comments from Fed officials generally pointed in this direction. Sentiment changed, however, after St. Louis Fed President James Bullard stated that a tapering of the bond buying programme is on the table for next month. His comments surprised currency markets and have led the dollar to rise ever since. It is interesting to note that the recovery of the dollar went hand in hand with a rise in 10-year US Treasury yields. This reflected that overall market sentiment did not deteriorate substantially and the dollar could recover. In 2014 and 2015 we expect a strong appreciation of the US currency, based on a combination of a strong US and global economy, higher US yields, the Fed to start hiking rates (in 2015) and positive investor sentiment.

The euro came under heavy pressure on speculation that the ECB Governing Council would be considering cutting its deposit rate by ten basis points – taking it to -0.1%, in case downside risks to price stability strengthen. Overall, the euro dropped only modestly, because at the start of the week the euro had advanced versus most currencies.

Currency forecasts

	Today	Q4 2013	Year-end 2014
EUR/USD	1.3460	1.35	1.20
GBP/USD	1.6117	1.63	1.52
USD/JPY	100.95	100	110

Source: ABN AMRO Group Economics

Asset allocation

No change to the overall asset allocation was made this week. The asset allocation continues to reflect a strong overweight in equities, a strong underweight in bonds, neutral allocations to property and commodities and a hedge fund allocation only in the defensive (overweight) and the more balanced (neutral) profiles. Within equities, all regions are neutral, except for an overweight in European equities and an underweight in North America.

Next week's calendar

Important dates next week

		Date
Pending home sales	US	25 Nov
Housing starts	US	26 Nov
House price index (FHFA & Case Shiller)	US	26 Nov
Conference Board consumer confidence	US	26 Nov
Initial jobless claims	US	27 Nov
New durable goods orders	US	27 Nov
Chicago Fed business confidence	US	27 Nov
Uni Michigan consumer confidence	US	27 Nov
Consumer confidence	EC	28 Nov
Economic sentiment monitor	EC	28 Nov
CPI	JP	29 Nov
Industrial production	JP	29 Nov
CPI	EC	29 Nov
Unemployment	EC	29 Nov

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