



global weekly

Investment
Communication
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Markets regain their poise

Markets settled down this week, as central bankers managed to ease worries about less accommodative monetary policies. Nonetheless, there is only one eventual direction for long-term rates to go: up.

Central banks calm markets

Global central banks' verbal intervention to calm market worries about less accommodative policy appears to be gaining some traction. Over the past few days, Fed and ECB officials have fallen over themselves to emphasize that rate hikes are a distant prospect, while China's central bank has reassured that it is ready to provide sufficient liquidity to its commercial banking system. As a result, government bond yields have eased on both sides of the Atlantic and equity markets have regained their poise. We think a combination of improving economic data and soothing noises from monetary policymakers should underpin risk appetite over the next few months.

While government bond yields have clearly passed their lows, we see a period of stability in the near term. With the global economy gaining momentum, no one should doubt that the only eventual direction for long-term rates is up.

Bond market update

Bond markets have settled down over the past few days, after continuing to reposition for higher yields last week. Federal Reserve Chairman Ben Bernanke's press conference that followed the FOMC rate decision on 19 June was the key reason. Bernanke's comments were more hawkish than expected and accelerated the surge in US Treasury yields, accompanied by a stronger US dollar versus most other currencies.

All financial markets are currently going through a repositioning phase, and it is hard to tell to what degree markets have priced in higher US borrowing costs and slower growth in developing markets. Despite the more confident tone from the Fed, having upwardly revised its growth forecasts and downwardly adjusted its expectations for unemployment, we believe that the process of winding down the stimulus programs will be long and delicate. Our view is that the Fed will start tapering in December, and it will most likely take

Equity index performance in local currencies

	Value	One week	Year-to-date
MSCI ACWI	355.46	1.2%	4.6%
S&P 500	1613.2	1.6%	13.1%
EuroStoxx 50	2619.86	2.7%	-0.6%
DAX	7990.75	2.5%	4.9%
Nikkei 225	13677.32	3.4%	31.6%
Hang Seng Index	20803.29	2.7%	-8.2%

Important rating changes

Company	From	To
Chevron	Hold	Buy
Vodafone	Buy	Hold
Kinder Morgan	Buy	Buy/RL
Nestle	Hold	Buy
Casino	Buy	Hold

Government bond yields

	Yield	One week	One year
US Treasuries 2-year	0.35%	-3,7 bp	4,6 bp
German Bunds 2-year	0.18%	-9,1 bp	7,5 bp
Japan 2-year	0.13%	0,6 bp	3,2 bp
US Treasuries 10-year	2.47%	-7,2 bp	88,8 bp
German Bunds 10-year	1.72%	-9,2 bp	20,7 bp
Japan 10-year	0.84%	-2,6 bp	3,8 bp

Spreads

Index	Spread	One week	One year
CDX NA IG	85.93	-7.24 bp	-32.29 bp
iTraxx Euro 5-year	117.03	-7.28 bp	-60.61 bp
JPM EMBI+	347.94	-9.67 bp	-33.85 bp

Performance data is as of 12:00 pm Friday, 28 June

Source: Bloomberg

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until mid-2014 before asset purchases come to a complete halt. The first rate hike will probably not occur before the first quarter of 2015. Nevertheless, the prospects of tighter monetary policy have caused a broad repricing across all financial markets.

European bank resolution framework

In Europe, EU finance ministers agreed on a bank resolution framework this week, giving more details on the bail-in regime that will become effective from 2018. The framework should provide member countries with the necessary tools for the resolution of failing banks.

The hierarchy of the bail-in is in line with what could be expected, but some flexibility on a national level has been built in, as desired by France and Sweden. Most importantly, shareholders and creditors are to share losses up to 8% of a failing bank's liabilities, before exemptions can be made and national backstops can be used. Insured deposits under EUR 100,000 and secured debt instruments, such as covered bonds, are exempt from bail-in provisions.

National authorities have some flexibility to exclude certain other liabilities from bail-in provisions as well. National resolution funds will be established, which will be first in line when government backstops are used. Intervention through these funds must be approved by Brussels first, and is limited to 5% of liabilities, unless senior unsecured bondholders are wiped out. Provided this condition is met, the European Stability Mechanism (ESM) would be allowed to recapitalise directly. However, direct ESM bank recapitalisation is only expected to be in place from the end of 2014.

Although we believe that the common resolution framework is constructive, it remains unclear what will happen to banks that have to recapitalise before the structure becomes effective. This risk is substantial, as the stress-test results from the European Banking Authority and ECB will be published mid-2014. As a result of this uncertainty, peripheral banks will likely continue to face considerable risk of deposit flight and elevated credit spreads.

As the framework will take effect from 2018, markets could price it in, as if it will become the mainstream approach from now on. Looking at banks that could become undercapitalised as a result of the 2014 stress test, the credit risk of senior and subordinated bonds of peripheral banks and banks with a large government stake could increase due to more uncertainties. Overall the outcome is positive, as it could initiate EU financial consolidation.

Equity update

Stock markets around the world recovered somewhat through the week, following a dreadful four-week series of losses.

Equity investors licked their wounds after a 10% correction in the MSCI World Index within one month, while Japanese stocks retreated 20% from their highs in local currencies. Buying appetite, however, cautiously returned this week, as the outlook for an improving US economy remains intact.

Company news flow is thin ahead of the earnings season. Vodafone, a UK telecom, announced that it will offer EUR 85 per share for Kabel Deutschland, after weeks of speculation that Liberty Global was also interested. Other news included the announcement by Microsoft and Oracle creating a strategic partnership for cloud computing. And Microsoft also released the test version of its new Windows 8.1 software.

On the earnings front, seeds and genomics player Monsanto reported a 3% decline in third-quarter earnings, as increased seed-production costs overshadowed rising prices for herbicides. The second quarter results of US home builder Lennar were better than expected, as the company benefited from rising demand for new houses. Despite the fact that rising interest rates have put pressure on homebuilder share prices in recent weeks, the CEO of Lennar said that rising rates are a result of an improving economy, which should be beneficial for the housing industry.

The second quarter earnings season is nearing, but next week it will most likely remain quiet. The first bellwethers to report are steel giant Alcoa on 8 July, Chevron on 10 July and the US banks JPMorgan and Wells Fargo on 12 July.

Stocks to watch: Ziggo

We expect Ziggo (EUR 30.20 - Buy), the largest cable operator in the Netherlands, to return to the spotlight following Vodafone's offer for Kabel Deutschland. The Vodafone offer shows the need for telecom operators to control both a fixed and a mobile network. As the market is increasingly moving towards quadruple play (fixed telephony, mobile, broadband internet and TV), high-quality hybrid networks are needed. We believe that Ziggo is likely to become a target as the telecom market consolidates. Assuming Vodafone will be successful in acquiring Kabel Deutschland, we expect Liberty Media to consider taking over Ziggo. Liberty already has reported a 15% stake in Ziggo and a merger between Ziggo and Liberty's UPC could lead to substantial synergies. The cable operators have been the outperformers in the telecom sector year to date, as investors recognise the value of fixed broadband networks.

Asset allocation

The Global Investment Committee was active this week. Within emerging markets debt, the committee prefers short-duration corporates over longer-dated sovereign bonds. On 24 June, it therefore decided to sell the remaining 10% al-

location in emerging markets sovereign bonds (funds). The proceeds were temporarily stored in cash. On 27 June, it decided to reinvest the proceeds from the sale of the emerging markets sovereign allocation into opportunities that are still available within emerging markets bonds (such as credits). The overall tactical asset allocation remains overweight in equity, neutral in property and commodities and with a strong underweight in bonds. Hedge fund allocations occur only in the defensive profiles (overweight) and the more balanced profiles (neutral). For more information, read the two Global Investment Committee Updates published this week.

Currency outlook

Better-than-expected US data helped US dollar sentiment, especially versus other major currencies. Comments from Fed officials to cool interest rate expectations also improved sentiment. The rally in US yields lost momentum, which helped emerging markets currencies. USD/CHF and USD/JPY found upward momentum, as investors were again more open to carry trades. Weaker US data, including weaker-than-expected first quarter GDP, failed to hurt the dollar.

With the Fed sounding more hawkish than expected, the EUR/USD has been on a downward trajectory. A decline in the two-year interest rate spread between Germany and the US has been the main driver. This is also due to ECB officials managing interest rate expectations so well. The EUR/USD dropped from above 1.34 before the FOMC decision last week to the low 1.30s this week, meeting our forecast of 1.30 for the end of June. We now expect the US dollar to start moving upward versus the euro, driven by an improvement in US economic data.

Currency forecasts

	Today	Q2 2013	Year-end 2013
EUR/USD	1.3035	1.25	1.20
GBP/USD	1.5252	1.49	1.45
USD/JPY	98.29	106	110.00

Source: ABN AMRO Group Economics

New publications

Bottom fishing for quality stocks: China Country Note

GDP growth in China is expected to slow down this year, nonetheless we maintain our view that the Chinese economy will stabilise and even pick up slightly in the coming quarters. We consider the recent equity sell-off, fuelled by concerns related to the tapering of quantitative easing, to be overdone and that “bottom-fishing” opportunities have arisen.

GIC Updates

Two Global Investment Committee (GIC) Updates were published this week. The first, on 25 June, concerned the decision by the committee to sell the remaining part of the position in emerging markets sovereign bonds, with the proceeds being invested in cash. The second, published today, detailed how the cash proceeds of the sale were invested into opportunities that are still available within emerging markets bonds (such as credits).

Next week's calendar

Important dates next week

		Date
PMI manufacturing	EC	1 July
Core inflation	EC	1 July
Unemployment	EC	1 July
ISM manufacturing	US	1 July
Tankan Business conditions large companies	JP	1 July
PMI manufacturing	CN	1 July
PMI services	CN	3 July
PMI services	EC	3 July
Retail sales	EC	3 July
ISM non-manufacturing	US	3 July
Trade balance	US	3 July
Policy rate & deposit rate	EC	4 July
Manufacturing orders	GE	5 July
Unemployment	US	5 July

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