ZURICH

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The week gone by

Despite some weak earnings' results in Europe, global equities rose strongly last week bouncing upwards off the 200-day moving average. Risk-on sentiment returned as the bull market approaches its fifth anniversary. Although valuations are no-longer attractive, equities are being driven by the expectation of strong corporate earnings' growth, better developed market economic data and low interest rates. International money flows continue to favour European equities.

The global index (in euro terms) rose by almost 2% last week giving a total return year-to-date of minus 0.1%. All of January's losses have now been recovered. Almost all markets were in positive territory last week led by Australia, Hong Kong and Europe.

Eurozone bond markets were flat last week but are up an impressive, and unexpected by many, 3.4% year-to-date led by Spain (+5.8%) and Italy (+3.9%).The German 10-year bond yield rose from 1.66% to 1.68% last week, its 2013 low was around 1.2%. The gold price was sharply higher again last week (+4.4%) and is now up almost 10% year-to-date. The metal had collapsed by 28% during 2013. Short-term interest rates are likely to remain low for an extended period.

	Index	1 Week Return 07.02.14 to 14.02.14	
		Local Currency %	Euro %
Global (euro)	FTSE World	1.9	1.9
US	S&P 500	2.3	1.8
US	NASDAQ	2.9	2.3
Europe	FT/S&P Europe Ex. U.K.	2.7	2.7
Ireland	ISEQ	2.1	2.1
UK	FTSE 100	1.4	2.9
Japan	Topix	-0.4	-0.6
Hong Kong	Hang Seng	3.1	2.6
Australia	S&P/ASX 200	3.7	3.9
Bonds	Merrill Lynch Euro over 5 year	-0.1	-0.1

The week ahead

- US market is closed today for Presidents' Day (Washington's Birthday) holiday. Another significant week for companies in the US reporting quarterly results. The focus will be on Industrials and Energy stocks.
- January FOMC minutes (Wednesday) likely to show that Fed officials view the incoming data as consistent with an acceleration in activity and an improvement in labour market conditions, justifying the decision to taper QE purchases by an additional $10bn per month.
- In the UK, it is likely that the February MPC minutes (Wednesday) will show that members voted unanimously to maintain policy on hold. It is forecast that January CPI inflation (Tuesday) will remain unchanged at 2.0% year-on-year.
- At the Eurogroup meeting (Monday), Greece will again be a major focus.
- In Japan, the preliminary data release (Monday) is likely to reveal that Q4 2013 real GDP growth was around 3.1% quarter-on-quarter.

Global outlook

- The general economic backdrop for 2014 still continues to necessitate a reasonably loose monetary policy in several of the major regions. Central Banks are generally neutral in their stance. Expectations are for more stable debt markets across the EU, given the ECB's credible commitment to preserving the Euro by buying periphery bonds. Focus is therefore on growth and inflation expectations, which remain low. ECB should remain accommodative and may implement more QE if growth comes in below expectations of 1.1% or if deflation concerns mount. Expectations for inflation remain well below the 2% long term target.
- In the US, consensus expectations continue to be for the Fed to end over half a decade of QE by September 2014. The most recent Fed meeting supports confirmed this plan is on track, as recent data weakness was disregarded. The Fed continues to monitor economic data and views unemployment levels as guide, not a trigger rate, given the structural factors skewing the headline number. Despite recent macro, retail and jobless data softness, the S&P continues to move higher through a decent earnings season with much of the softness attributed to a transitory weather effect. Chairwoman of the Fed, Yellen, is perceived to weigh unemployment more heavily than inflation in the Fed goals. Therefore, expectations are for rates to remain low for an extended period beyond the end of QE. US growth is still sub-par by historic standards but, importantly, it is stable with signs of improvement. Inflation remains below target levels. However, confidence remains in the US growth story and emerging markets may not drag equity performance too heavily in 2014.
- Strategists continue to favour equities over bonds, based on relative valuation. Equity markets valuations are at more normal levels and are expected to continue to perform strongly into 2014 as long as growth expectations continue to be met. The broadly positive equity market outlook for 2014 is driven largely by expectations for earnings growth, as valuation multiples in many sectors are relatively high. We view market weakness as an opportunity to add to positions.
- There is some caution built into estimates given market valuations appear to be fair and Fed tapering could potentially cause a pull back. The Japanese market has shown strength recently, with some volatility as the currency strengthens. A stabilisation in the exchange rate is sought ahead of seeing Japan outperform. There is an expectation for strong company earnings at current exchange rates. There are continued expectations that the Bank of Japan may announce further stimulus in early 2014. Sub par emerging market growth rates, US dollar strength, political wrangling over the debt ceiling and the fed taper are likely contributors to market volatility.
- Bond markets remain vulnerable to upside growth surprises. Meanwhile, confidence in the ability of the ECB and policymakers to manage the peripheral debt situation currently remains high. However, there are still many challenges to be negotiated in peripheral countries as credit growth remains challenged. In particular the trajectory of Eurozone inflation is of paramount importance to the ECB.
- Zurich Life funds are close to neutral in bonds versus the manager average with a slight overweight in equities. The funds are underweight energy and utility stocks and overweight consumer goods and industrials. Geographically, the funds are underweight the UK and Pacific region, neutral in the US and Japan, slightly overweight Europe region and Ireland.

Zurich Life Assurance plc
Zurich House, Frascati Road, Blackrock, Co. Dublin, Ireland.
Telephone: 01 283 1301 Fax: 01 283 1578 Website: www.zurichlife.ie