ZURICH

24th March 2014

The week gone by

Global **equities** overall recovered much of the previous week's losses as the Crimean crisis did not escalate in a material way. Markets were somewhat unsettled last Wednesday following comments from the new Fed Chairman, Janet Yellen, that interest rates could start rising six months after the end of QE tapering, likely the Spring of 2015. Equities continue to be supported by the expectation of strong corporate earnings' growth and low interest rates. Valuations, however, are no-longer attractive, while recent economic data has been more mixed.

The global index (in euro terms) rose by 1.8% last week giving a total return year-to-date of minus 0.4%. Most of the major **markets** were in positive territory in local currency terms last week led by Europe (+2.6%) and the US (1.4%); the global index moved above its 50-day moving average and remains well above the key 200-day moving average.

Eurozone **bond** markets fell by 0.2% last week but are up an impressive 4.9% year-to-date led by Spain (+8.1%) and Italy (+6.3%). The German 10-year bond yield rose from 1.55% to 1.63% last week; its 2013 low was around 1.2%. Irish yields are now only 1.4% higher than in Germany. Commodity prices in general fell by just over 1% last week but commodities remain one of the best performing asset classes so far this year (+6.9%).

	Index	1 Week Return 14.03.14 to 21.03.14		Year to Date Return 31.12.13 to 21.03.14	
		Local Currency %	Local Currency %	Euro %	Euro %
Global (euro)	FTSE World	1.8	1.8	-0.4	-0.4
US	S&P 500	1.4	2.1	1.0	1.0
US	NASDAQ	0..7	1.5	2.4	2.4
Europe	FT/S&P Europe Ex.	2.6	2.6	0.7	0.7
Ireland	ISEQ	0.8	0.8	8.3	8.3
UK	FTSE 100	0.5	0.4	-2.8	-3.3
Japan	Topix	-1.6	-1.7	-12.0	-9.4
Hong Kong	Hang Seng	-0.5	0.4	-8.0	-8.1
Australia	S&P/ASX 200	0.2	1.7	-0.3	1.4
Bonds	Merrill Lynch Euro over	-0.2	-0.2	4.9	4.9

The week ahead

- US Q4 2013 GDP growth (Thursday) is expected to be revised higher to 2.7% quarter-on-quarter from the previous estimate of 2.4%. The March Conference Board's confidence index (Tuesday) is forecast to record at modest pick-up to 78.6 (last: 78.1).
- It is expected that the euro area March composite PMI (Monday) will increase slightly to 53.5 (last: 53.3).
- In the UK, it is likely that the final estimate (Friday) of Q4 2013 GDP will remain unrevised at 0.7% quarter-on-quarter.
- In Japan, it is estimated that February nationwide core CPI (excluding fresh foods) (Thursday) grew by 1.3% year-on-year.
- Events in Ukraine and Moldova's pro-Russian separatist Transnistria region will be watched closely.

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 remains on growth and inflation expectations, which remain low. Expectations are for inflation to remain below the 2% target rate. The ECB should remain accommodative and the possibility of QE remains if growth comes in below expectations or deflation concerns mount.

- In the US, consensus expectations continue to be for the Fed to end over half a decade of QE by Sep 2014. The most recent Fed announcements supported this view. 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. However, Yellen's suggestion of an initial rate hike in spring 2015 is possible but the Fed is still likely to remain data dependant ahead of taking any action. These comments should provide US$ strength. US growth is still sub-par by historic standards but, importantly, it is stable with signs of improvement. Inflation remains below target levels and core CPI (ex energy and food) is still relatively benign. However, confidence appears to remain in the US growth story, with GDP to be buoyed by accelerated consumer spending and capital expenditures.

- There is some caution built into estimates given market valuations appear to be fair, the S&P 500 has reached record highs, the Euro Stoxx 600 continues its upward trajectory, persisting since early 2012. Fed tapering could eventually cause a pull back but appears so far to be well baked into expectations causing little reaction to date.

- Export led emerging markets may see some benefit from an accelerating US economy; however, this will be overshadowed by the headwinds facing emerging markets, including rising US interest rates, a stronger US$ and negative sentiment around China. This may keep emerging market equities out of favour in the near term.

- Strategists still 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 and many markets are relatively high. We view market weakness as an opportunity to add to positions

- The Japanese market remains volatile with some weakness in recent weeks. A stabilisation in the exchange rate is sought ahead of seeing Japan outperform. There are continued expectations that the Bank of Japan may announce further stimulus in 2014, but the impact of the increase in domestic consumption tax may need to be assessed by the BoJ ahead of taking action.

- Bond markets remain vulnerable to upside growth surprises. Meanwhile, confidence in the ability of the ECB and policymakers to manage the peripheral debt situation 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 region and Asia Pacific region, neutral in the US, Japan and Europe and overweight Ireland.

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