



28th April 2014

The week gone by

Global **equities** overall were flat on the week notwithstanding continued tensions in Ukraine. Markets are in the middle of a generally positive Q1 results season. Equities continue to be supported by the expectation of strong corporate earnings' growth and low interest rates. Valuations, however, are no-longer attractive.

The global index (in euro terms) was unchanged last week giving a total return year-to-date of 1.0%. The only noticeable moves amongst the major **markets** in local currency terms last week were in Australia (+1.4%) and in Hong Kong (-2.4%); the global index held above its 50-day moving average and remains well above the key 200-day moving average.

Eurozone **bond** markets rose by 0.3% last week and are up an impressive 7.1% year-to-date led by Spain (+11.0%) and Italy (+9.2%). The German 10-year bond yield fell slightly from 1.50% to 1.48% last week; its 2013 low was around 1.2%. Equivalent US yields are at 2.66%. Eurozone bond prices, although somewhat expensive, have benefited from deflationary concerns and speculation that the ECB may introduce some form of QE.

	Index	1 Week Return 18.04.14 to 25.04.14		Year to Date Return 31.12.13 to 25.04.14	
		Local Currency %	Euro %	Local Currency %	Euro %
Global (euro)	FTSE World	0.0	0.0	1.0	1.0
US	S&P 500	-0.1	-0.2	0.8	0.5
Europe	FT/S&P Europe Ex. U.K.	-0.1	-0.1	2.1	2.1
Ireland	ISEQ	-0.6	-0.6	7.1	7.1
UK	FTSE 100	0.9	0.8	-0.9	0.1
Japan	Topix	-0.3	-0.2	-10.2	-7.8
Hong Kong	Hang Seng	-2.4	-2.5	-4.6	-5.0
Australia	S&P/ASX 200	1.4	0.6	3.3	7.0
Bonds	Merrill Lynch Euro over 5 year	0.3	0.3	7.1	7.1

Source: Bloomberg

The week ahead

- This week is one of the busiest in the US Q1 earnings season. Industrial, financial and healthcare names will be in focus. It is likely that the FOMC (Wednesday) will decide to taper the pace of its asset purchases by another \$10bn. It is expected that GDP growth will be at 1.1% quarter-on-quarter saar in the advance Q1 estimate.
- It is projected that euro area 'flash' April HICP inflation (Wednesday) will climb to 0.8% year-on-year (last: 0.5%).
- In the UK, it is expected that Q1 real GDP (Tuesday) grew 0.9% quarter-on-quarter consistent with 3.2% year-on-year growth.
- In Japan, it is estimated that March Industrial Production (Wednesday) increased 0.5% month-on-month (last: -2.3%).
- Russian/Ukrainian tensions remain on the radar screen.

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.
- 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, despite recent volatility, 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.
- Despite recent volatility seen in the US and Europe, the outlook for the US and Eurozone remains unchanged. Recent moves in the markets showed a shift away from higher beta to lower beta stocks and sectors, despite the stock and sector fundamentals remaining unchanged. Appetite for risk still remains.
- In the US, consensus expectations continue to be for the Fed to end over half a decade of QE by Sep 2014. 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. Although Yellen's suggestion of an initial rate hike in spring 2015 remains possible, 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. This strength is evident in recent manufacturing, jobs and consumer spending data and reported earnings from the start of Q1 earnings season. A continuation of such broad based strength will eventually lead to a more normalized rate environment. Inflation remains below target levels and core CPI (ex energy and food) is still relatively benign. Overall, 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 had reached record highs during Q1. Fed tapering could eventually cause a pull back but appears so far to be well baked into expectations causing little reaction to date. Shorter term, market moves may continue to see some small effects from investor positioning and style factor shifts (as seen lately. Geopolitical risk will continue to feed investor fears somewhat with the triple threat of US/Russian tensions over the Ukraine, North Korea's nuclear threats and China's decelerating growth rate.
- 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.
- The Japanese market remains volatile with some weakness in recent weeks. A stabilisation in the exchange rate is sought ahead of seeing Japan outperform. Monetary policy is expected to remain loose for some time to come and there are continued expectations that the Bank of Japan may announce further stimulus in 2014. The latest consumer tax hike doesn't appear to have had a significant impact on inflation in the region so far. Multiples in this region are the low versus other developed market peers and there is upside potential to earnings estimates broadly.
- 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. Bond markets remain vulnerable to upside growth surprises. Confidence in the ability of the ECB and policymakers to manage the peripheral debt situation remains high. In particular the trajectory of Eurozone inflation is of paramount importance. The ECB has reiterated their commitment to managing inflation through use of unconventional policy tools if necessary. Their unambiguous language in relation to forward guidance also underlined their intentions to maintain accommodative monetary policy going forward. However, there are still many challenges to be negotiated in peripheral countries as credit growth remains challenged.
- 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 tech stocks and overweight industrials and consumer goods. Geographically, the funds are underweight the UK and Asia Pacific region, neutral in the US and Japan, overweight Ireland and slightly overweight Europe.

This outlook does not constitute an offer and should not be taken as a recommendation from Zurich Life. Advice should always be sought from an appropriately qualified professional.

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