



29th June 2015

## The week gone by

Global **equities** (in euro terms) rose as markets saw some positive light regarding the Greek debt situation; however, the start of this week will see further volatility as the end-game approaches. Euro currency weakness has significantly enhanced returns for eurozone investors in 2015 (see table below). Equities continue to be supported by the low interest rate environment. In addition, equities remain better value relative to other asset classes despite the rise in price earnings multiples and bond yields.

The global index (in euro terms) rose by 1.9% last week giving a total return year-to-date of a plus 14.1%. Technically, despite the rise, the Index remained just below its 50-day moving average but is still almost 8% above the critical 200-day moving average. There was a mixed bag of returns from the major equity **markets** in local currency terms last week ranging from plus 4.4% in Europe to minus 0.9% in Australia.

Eurozone **bond** prices fell back (-0.5%) last week and are now down by 2.5% year-to-date. Bonds have been hurt recently by comments from ECB president Mario Draghi that 'we should get used to periods of higher volatility'. Bond prices in Europe are down by over 7% from their recent peak. The German 10-year bond yield rose sharply from 0.75% to 0.92% last week; it had hit an all-time-low of 0.06% in mid-April. Equivalent US yields rose from 2.26% to 2.47%. **Commodity** prices in general were up by 1.2% (in dollar terms) last week but are down 2.2% so far in 2015.

	Index	1 Week Return 19.06.15 to 26.06.15		Year to Date Return 31.12.14 to 26.06.15	
		Local Currency %	Euro %	Local Currency %	Euro %
Global (euro)	FTSE World (total return)	1.9	1.9	14.1	14.1
US	S&P 500	-0.4	1.3	2.1	10.7
Europe	FT/S&P Europe Ex. U.K.	4.4	4.4	16.8	16.8
Ireland	ISEQ	1.5	1.5	21.9	21.9
UK	FTSE 100	0.6	1.4	2.9	12.7
Japan	Topix	2.2	2.9	18.4	24.3
Hong Kong	Hang Seng	-0.4	1.3	13.0	22.5
Australia	S&P/ASX 200	-0.9	-0.6	2.5	4.2
Bonds	Merrill Lynch Euro over 5 year	-0.5	-0.5	-2.5	-2.5

## The week ahead

- In the US June employment report (Thursday), it is expected that non-farm payrolls will rise by 227k (last: 280k) and the unemployment rate to print at 5.4% (last: 5.5%).
- In Europe, Greece will hold centre stage. We look for euro area June flash HICP inflation (Tuesday) to print at 0.2% year-on-year (last: 0.3%).
- In the UK, it is expected that Q1 GDP (Tuesday) will come in at 2.5% year-on-year (last: 2.4%).
- In Japan, it is forecast that the June BoJ Tankan Diffusion Index for large manufacturers (Tuesday) to remain at 12.

# Global Outlook



## United States

- Economic data is showing incremental signs of improvement in the US with the Economic Surprise index rebounding from low levels in June. Consumer confidence remains high, personal consumption data for May came in stronger than expected and new & existing home sales data reports exceeded expectations for the May period.
- The S&P 500 Index continues to hover close to its highs, trading within a tight range. The set up for the second half of 2015 looks favorable on many fronts – economic data reads indicate the economic recovery is still on track, a strong Q2 earnings season could reinforce this and provide confidence that US equity valuations are reasonable whilst also helping boost earnings outlooks marginally having seen huge cuts to estimates year to date (mainly energy related and FX related).
- Given the US lagged Global Equity markets during 1H 2015, there could be a rebound play. However, caution remains given the expansionary monetary policies within Europe and Japan helping boost equity markets (similar to the impact the S&P experienced with over the 5 years with the now completed quantitative easing). Both regions are earlier in their “recovery cycles” versus the U.S making them relatively more attractive. The strong USD continues to be a challenge and as the Fed looks to raise rates, the dollar could strengthen further, hurting company earnings. Bears would see valuation of U.S equities as stretched, despite the low interest rate regime which should allow for some premium in valuation levels.
- Nearer term, decreasing confidence in the cohesiveness of the Euro Area will drive volatility.

## Euro Area, Europe & UK

- European equity market volatility persists – Greece’s failure to agree to the latest package from the Troika drove the ECB to refuse to expand the ELA funding to Greek banks. The Greek Government will hold a snap referendum on July 5th on whether to accept this package. Tsipras will actively campaign for a “No” vote ahead of this (i.e. Default & leave E.M.U). Capital restrictions are in place and all Greek Banks are closed. Tuesday should see a Greek default on their 1.5b IMF payment and impairment of ~54b in government debt held by banks. The ECB will need to consider their position the ELA funding also.
- The implications for the rest of the Eurozone region, whilst real, are not as worrisome as would have been perceived a few months ago with the “debtor nations” (Spain, Italy etc.) seeing a fade in anti-EU type, “separatist” political parties (e.g. Podemos in Spain). There may be a flight to safety in the short-term with German Bunds and US Treasuries being bought. European equity markets have not been complacent and Greek headline-driven volatility will continue.
- Aside from resolution of the Greek situation, further catalysts to lift European equity markets include credible policy reform in France and Italy. Interest rates are expected to stay low for an extended period. If QE does stimulate growth in the region, this should see banks easing credit standards over time driving momentum in the growth.
- Inflation in the UK remains lackluster and Q2 inflation expectation was revised lower. The outlook for the back half of the year looks for a pick-up in inflation and the gradual oil price recovery will help.

## Rest of World

- The gradual recovery continues in Japan, broadly, and is supported by the continued expansion of the monetary base, the resulting weaker Yen and stronger economic data reads. Growth in private consumption (60% of GDP) should pick up throughout 2015, supported by data showing a rise in real wages recently. Recent data showed a drop in export volumes to Asia despite weak JPY, not surprising given the broad weakness

across most Emerging markets. BoJ did not announce any further easing at their most recent meeting. Equity valuations in the region look attractive, relatively. Earnings revisions have been trending flat in recent weeks and the latest economic data paints a broadly positive picture of the economy.

- Emerging markets remain weak and range bound for the most part. Weaker commodity prices are a headwind and weaker currency means the USD denominated debt burden has risen, increasing the riskiness of these markets further.

## Central Bank Watch:

- The general economic backdrop for 2015 still continues to necessitate a reasonably loose monetary policy in several of the major regions. Some divergence is evident, with the US being closest to tightening policy.
- In the US, the Fed is expected to withdraw some of their policy accommodation with rate rises on the horizon. At last week’s meeting, the Fed’s tone was incrementally more dovish but they were more upbeat in their description of the economic situation. The “dots” (Median Member Forecast) moved down for 2015 and 2016 but now 7 members expect <2 hikes in 2015, versus only 2 members previously. There was no change to forward guidance i.e. they remain data dependent. The theme of the meeting seemed to convey that the trajectory of hikes is more important than the timing of the first move and the path of hikes will be gradual.
- Earlier in 2014, ECB announced an open ended Quantitative Easing program. The ECB will commence buying €60bn of private and public sector securities every month until from March to end-September 2016 at least. President Draghi said the program will “be conducted until we see a sustained adjustment in the path of inflation which is consistent with (our) aim of achieving inflation rates below, but close to, 2% over the medium term”. The program will represent at least €1.1tn of asset purchases, possibly more if inflation and growth fails to pick up. Negotiations with Greece remain the focus of the ECB member states and the market.
- The MPC unanimously support an unchanged policy stance at the moment. The BoE downgraded its growth forecast but maintains its expectation on labor force slack. Fiscal policy is expected to be a headwind to GDP growth as the Conservatives’ implement a more restrictive fiscal policy.
- Japanese monetary policy is expected to remain loose for some time to come. The BoJ did not make any changes to policy in their latest meeting. Inflation still remains well below 2% target.

## Positioning

- Zurich Life funds are overweight in equities and underweight bonds versus the manager average.
- Zurich Life funds favor Irish and Spanish over German and Belgian bonds.
- In equities, we are
  - underweight UK, North America
  - neutral Europe ex Ireland, neutral Asia ex Japan
  - Overweight Ireland and Japan(All the above are relative to the manager average)
- Sector weights (at aggregate level) are: underweight energy and utilities, and overweight consumer goods and industrials.

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

## Zurich Life Assurance plc

Zurich House, Frascati Road, Blackrock, Co. Dublin, Ireland.

Telephone: 01 283 1301 Fax: 01 283 1578 Website: [www.zurichlife.ie](http://www.zurichlife.ie)

Zurich Life Assurance plc is regulated by the Central Bank of Ireland.

Intended for distribution within the Republic of Ireland.