Market View

update from 09.08.2019

LINVO
LIFE INVESTMENT OFFICE

- Further escalation of US-China trade dispute with 10% tariffs on remaining $300bn of Chinese goods from September 1st, higher threat of Hard Brexit from new UK prime minister Boris Johnson and intensified Iran tensions in Strait of Hormuz are set to further weaken already sluggish global growth. Weaker but still growing employment in services sector, continuous wage growth, more accommodative monetary policies and government stimulus in China help to offset the declining global manufacturing and trade for now.
- In our view, US president Donald Trump needs a trade deal rather sooner than later in order to keep the US economy on growth path, which is essential for his prospect of being re-elected at the end of 2020. Especially against the backdrop of fading fiscal stimulus from Tax Act and current harvest season for the US farmers. However, the trade dispute might escalate further before the deal is reached.
- The chance of the threated Hard Brexit is very small because there is no majority support in the parliament neither from the population. Most feasible is UK exit from EU while remaining in customs union.

- Watch:
  o US-China and Brexit negotiations
  o High risk of real estate bubbles in Canada, Sweden, Australia and Hong Kong
  o Inflation signs in US, Germany, UK and other countries with historically record low unemployment rate
  o Oil price developments especially related to geopolitical risks in Iran, Libya and Venezuela
  o Continuation of America First policy and new trade dispute with European Union
  o Corporate debt overhang and wealth management products in China
  o Geopolitical risks around the world

- Yield curve has much lower predictive power today than in the past due to QE influence on long-term interest rates. On average, it took 22 months from curve inversion to recession.
- Focus on companies with relative stable earnings und low leverage is a key at the current late stage of the cycle.

End of 2019 key economic forecast by Linvo:

- USD/CHF: 0.97
- EUR/USD: 1.15
- USD/JPY: 105
- GBP/USD: 1.32
- XAU/USD: 1400 USD
- BRENT:: 70 USD
- US 10y T: 2.25%

Market view	USA	EUROPE	CHINA	EM Markets
Macro CAUTION	US economic growth is set to moderate to 2.3% in 2019 from 2.9% in 2018 due to closed output gap and fading fiscal stimulus after QII 2019. The manufacturing sector came already to a halt, but improved financial conditions from interest cut by Fed, low inflation, low unemployment and wage growth continue to support the consumption. Depending on data, Fed might cut interest rate by additional 25 bps by the end of the year.	Forecasted Eurozone growth of 1.1% in 2019 is low but is expected to increase to 1.5% next year through recovery in global trade and industrial cycle from the end of 2019. Low unemployment and wage growth with low inflation and even more accommodative monetary policy continue to support the economy. German export-oriented economy is hit hard by declining global trade. Government debt (Italy, Portugal, Greece) is very high but manageable due to very low interest rates and long maturities.	In China, gov. monetary & fiscal stimulus as well as rerouting of exports helped to keep the manufacturing from decline (July Manufacturing PMI 49.9) and to keep the economic growth above 6% in 2019. Recently announced tariffs and possible non-tariff sanctions like cut-off Chinese companies from US technology supply chains will be more negative for the economy, but the gov. still has sufficient room for additional stimulus if needed. The risks from corporate debt overhang are under control for now.	Emerging markets are benefiting from eased global financial conditions, expected US dollar softening and long-term structural growth drivers. The Brazilian economy has disappointed so far due to delays in highly anticipated pension, tax and other structural reforms. Brazil, Mexico and Turkey are expected to get back to growth in 2020. Furthermore, India is expected to gain more growth momentum this and next year.
Equities CAUTION	US equity market is expensive by looking at historical averages for forward, Shiller P/E and P/B ratios. However, with yield of 1.75% p.a. on 10- years treasury the valuations are still relative attractive. Share buyback cycle is mature but is expected to continue in 2019. Nevertheless, trade dispute, strong dollar and strong wage growth are likely to weight on corporate profits. Financials, energy and healthcare look currently particular attractive. CAUTION	European equity market is currently undervalued by looking at historical averages for forward, Shiller P/E and P/B ratios. Share buyback cycle is about to start in Europe. Especially Spain, Germany and UK offer very attractive valuations and dividend yields. To the large extent, the political risks are already priced in. Financials, energy, consumer discretionary and healthcare look currently relative attractive. CAUTION	The valuations in China are currently attractive and will benefit from stabilization in China over the short-term as well as from structural consumption growth. However, the Chinese equity market is very cyclical and exposed to strong imbalances in corporate debt. Therefore, we prefer mainly Chinese technology and consumer-oriented companies with low leverage. STOP	EM equity markets are currently undervalued in comparison to the long-term average P/B and forward P/E ratios and offer high growth potential relative to advanced economy markets. GO
Bonds CAUTION STOP	With still attractive yield, high coverage ratio and reasonable net leverage, US High Yield bonds with medium-term maturity are currently more attractive than US Investment-Grade bonds. Especially BBB-rated bonds carry high risk of fire sale from downgrade in case of recession, because the share of BBB-rated bonds in IG universe has increased from 35% in 2008 to 50% in 2018. CAUTION GO	Thanks to very loose ECB monetary policy, the Eurozone bonds offer only return free risk. STOP CAUTION	Focus mainly on US and EM credit due to very high corporate leverage and governance issues in China. STOP CAUTION	Sovereign EM bonds in USD and local currency as well as EM corporate bonds in local currency offer currently attractive spread over US Treasuries. Government and corporate debt levels remain low in the most EM. GO

GO positive, buy/increase CAUTION neutral, monitor closely STOP negative, sell/reduce position