The Week Ahead

March 24th 2017

"Europe: Getting more compelling"

Regular readers of this column will not be surprised to see that the European economy has been improving markedly. After its March meeting, Mario Draghi (the President of ECB), declared victory against deflation and said the Bank "does not anticipate that it will be necessary to lower rates further". Corporate profitability is also gaining momentum with European corporations reporting another quarter of earnings growth. This is the second consecutive quarter of earnings growth after the previous four consecutive quarters of earnings declines. With improved fundamentals, European equities have turned the corner, and the month-to-date MSCI Europe Index is outperforming the US S&P 500 index in both Euro and US-Dollar terms. Some investors have noticed these improvements and we have started to see inflows returning to European equity funds.

> ***"We have started to see inflows returning to European equity funds."***

Investors will now shift their focus to the French Presidential election, which will take place on April 23. Recent opinion polls suggest that Marine Le Pen (who is campaigning for exiting the Eurozone) and Emmanuel Macron (who is pro-European Union) will reach the second round of the French Presidential election, and Macron will win the election at the second round.

The week ahead

Next week, the US will announce the following macro-economic data:

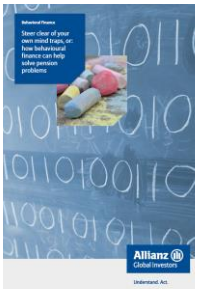
1. 4Q GDP: Boosted by inventories, the market is expecting the final GDP figure for the fourth quarter of 2016 to be revised slightly upward from 1.9% to 2.0%.
2. Personal Spending: Given flat automobile sales and lower heating bills due to unusually warm weather, the market is expecting flat personal spending growth for February.

Investors will look to see if the recent positive surprises from the European macro-economic data can be sustained. The March Harmonised Indices of Consumer Prices (HICP) will be announced next Friday, and the market is expecting flat month-on-month growth. Stabilised commodity prices should also translate into a stable inflation outlook for Europe. The UK will release its final fourth quarter 2016 GDP figure. Supported by strong household consumption, which offset the slowdown from corporate investment, the market is expecting 0.7% growth for the fourth quarter.

Publications

"AllianzGI's House View on Brexit"

The UK's triggering of Article 50 on 29th March is like firing the starting pistol on the process of leaving the EU – but this race will be slow and tortuous, with many dangers along the way. Here is our view on what investors should expect and how they should prepare.



"How behavioural finance can help solve pension problems"

The impact of declining demographics in industrial economies is being exacerbated by low, and even negative, bond yields, as these make it harder to meet pension liabilities. But pension issues could be so simple if the findings of behavioural finance were applied. This case study offers a "how-to" approach to the issue.

Chart of the Week: Europe's earnings revisions momentum remains positive

Source: Allianz Global Investors Global Economics & Strategy, Datastream. Data as of March 22nd. 2017. Ratio of up/down estimates, 3 months moving average. Past performance and forecasts are not a reliable indicator of future results.

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Japan will report industrial production data. Despite an unexpectedly low figure for January, perhaps due to Chinese New Year that dented demand, investors are expecting the February industrial production figure to rebound. China's official Manufacturing PMI reading for March will be announced next week. With conditions in the manufacturing sector remaining on an improving trend, investors are expecting the March reading to be at 51.2, well above the expansion zone of above 50.

Act

Before the first quarter corporate earnings are announced starting next month, investors will focus on earnings revisions and political headlines in addition to the macro data points that were mentioned above. While Europe's earnings revisions index continues to improve, the US revisions index has tapered off since the beginning of the year. Similarly, while European political risk has decreased, the political risk in the US remains elevated. The Trump administration has stated that the corporate tax reform will come after the Affordable Care Act (ACA) has been repealed. Given that the US market has rallied substantially since the President Trump election victory partly due to expectations of a corporate tax reform, any comments from the Trump administration or US Congress that suggest a delay in repealing the ACA may be perceived as negative by investors. With a better earnings outlook, lower political risk, more attractive valuations and higher dividends than in the US, the European story is getting compelling.

Yours,

Charles Ma

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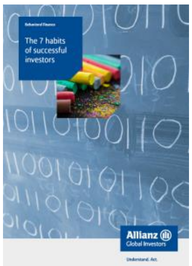
Upcoming Political Events 2017

April:

Apr	IMF Global Outlook
1 Apr	India: Likely to introduce the Goods and Services Tax
7 – 8 Apr	Eurogroup and ECOFIN meetings
13 Apr	BoE minutes
20 Apr	Greece: ECB debt repayment
21 – 27 Apr	IMF/WB spring meeting
23 Apr / 7 May	Presidential elections in France
26 – 27 Apr	BoJ meeting
27 Apr	ECB Council meeting
28 Apr	US: Budget Resolutions

→ Overview political events 2017

Other publications:



Behavioral Finance: "The 7 habits of successful investors"

Investing and accumulating wealth are no trivial matter, especially when investors are torn between avoiding risk and striving for returns. Seven simple habits can help to accumulate capital calmly and composedly. After all, your money should be working for you, not the other way around.

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"USA: Raise the Debt Limit – Or Else"

Suspension of the US government's borrowing limit ended on March 15, resetting to just shy of $20 trillion. In the absence of legislation empowering the government to go deeper into debt, the US Treasury began taking "extraordinary measures" to fund government obligations. These include:

- Suspending investments, and redeeming in advance, the securities of the Thrift Savings Plan's G Fund, the Exchange Stabilization Fund, the Civil Service Retirement and Disability Fund and the Postal Service Retiree Health Benefits Fund;
- Suspending the issuance of new State and Local Government Series securities and savings bonds;
- Exchanging Federal Financing Bank securities for an equal amount of Treasury securities.

Together with revenues from April tax collections, these measures are expected to keep the Treasury under the debt limit and with enough cash to fund the government's existing obligations –but only temporarily.

Depending on how the federal budget process unfolds over the months ahead, Treasury likely will not run out of money until, roughly, September. The exact timing will depend on the spending level set in April in the budget resolution and revenue collections during the spring and summer. Congress likely will agree to a debt ceiling increase statutorily in April when it passes fiscal 2017 and 2018 funding bills, avoiding a contentious debate after the August recess.

Issuance of Treasury securities was largely unaffected the last time Congress enacted extraordinary measures to stay under the borrowing limit, from March to November 2015. Similar dynamics likely will play out this time. Marginal borrowing above maturing Treasury securities will be minimal and the re-issuance of maturing Treasury securities is expected to continue. Net Treasury issuance likely will be adjusted at the time Congress enacts another increase or suspension of the debt ceiling.

Treasury borrowing reaching the debt limit is not unusual. Annually for decades, Congressional factions have wrangled over whether, and how high, to raise the debt limit. Conservatives, especially, often used approaching borrowing limits to argue in favor of an amendment to the US Constitution requiring a balanced budget and against additional spending. Relatively liberal factions typically jockeyed in favor of expanding entitlements.

Since 2001, Congress has raised its level 14 times. Typically, deals to raise the debt limit have been struck in the hours, and sometimes minutes, before the government would go into technical default. On a few occasions, though, failure to reach a decision has shut down the government for up to several weeks.

Unusually contentious debate over the debt ceiling in 2011 resulted in the first-ever downgrade of US Treasury securities by Standard & Poor's. In October 2013, Fitch placed a watch rating on Treasuries for a possible downgrade. The rating agency found increased risk of delayed payments to federal employees and late benefit outlays to entitlement recipients. Fitch removed the rating watch after the debt ceiling was suspended in February 2014. Then, in 2015, Congress voted to suspend the debt limit until March 15, 2017.

Among developed market countries, the US debt to GDP ratio ranks behind only Belgium, Portugal, Italy, Greece and Japan. However, the US benefits from the relative strength of the US dollar and its reserve currency status which dampen financing costs.

Currently, non-US investors hold about 43% of Treasury debt, some two-thirds of which is held by governments. In 2015, for the first time in a decade, non-US investors purchased fewer Treasuries than they sold. That reversal accelerated in 2016, with non-US holdings falling by $201 billion, led by China and Japan. However, there are few signs that the non-US appetite for Treasuries is disappearing, particularly among countries with large trade surpluses. China has been selling its reserves to stabilize the RMB and Japan decided to hold fewer long-term securities in a monetary policy gesture.

Yours,

Steven Malin

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Senior Investment
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Calendar Week 13:

Monday

- Germany:
  - Ifo Business Climate (Mar) (111.0)
  - Ifo Expectations (Mar) (104.0)
  - Ifo Current Assessment (Mar) (118.4)
- Italy:
  - Economic Sentiment (Mar) (104.0)
  - Manufacturing Confidence (Mar) (106.3)
  - Consumer Confidence Index (Mar) (106.6)
- US:
  - Dallas Fed Manf. Activity (Mar) 20.5 (24.5)

Tuesday

- Italy:
  - Industrial Sales WDA (Jan) (9.4% y/y)
- US:
  - Markit Service PMI (Mar) (53.8)
  - Markit Composite PMI (Mar) (54.1)
  - Wholesale Inventories (Feb) (-0.2% m/m)
  - Consumer Confidence 113.0 (114.8)
  - Richmond Fed Manf. Index (Feb) (12)

Wednesday

- France:
  - Consumer Confidence (Mar) (100)
- Japan:
  - Retail Sales (Feb) 0.5% m/m (0.2% m/m)
- US:
  - MBA Mortgage Applications (Mar 24)

Payment Redemptions: France (EUR 6.1m)

Thursday

- China:
  - BoP Balance of Payment (4Q) ($37.6 bn)
- Eurozone:
  - Economic Confidence (Mar) (108)
  - Business Climate Indicator (Mar) (0.82)
  - Industrial Confidence (Mar) (1.3)
- Germany:
  - CPI EU Harmonized (Mar) (2.2% y/y)
  - CPI (Mar) (2.2% y/y)
- US:
  - Initial Jobless Claims(Mar 25)
  - Continuing Claims (Mar 18)
  - GDP Annualized (4Q) 2.0% q/q (1.9% q/q)

Friday

- China:
  - Manufacturing PMI (Mar) 51.2 (51.6)
  - Non-Manufacturing PMI (Mar) (54.2)
- Japan:
  - Jobless Rate (Feb) 3,0% (3.0%)
  - Natl CPI (Feb) (0.4% y/y)
  - Natl CPI ex Fresh Food(Feb) 0.2% y/y (0.1% y/y)
  - Natl CPI ex Fresh Food, Energy (Feb) 0.1% y/y (0.2% y/y)
  - Industrial Production (Feb) 4.0% y/y (3.7% y/y)
  - Construction Orders (Feb) (1.1% y/y)
- UK:
  - GfK Consumer Confidence (Mar) (-6)
  - Current Account Balance (4Q) (-25.5 bn)
  - GDP (4Q) (2.0% y/y)
- Germany:
  - Unemployment Claims Rate SA (Mar) (5.9% y/y)
- Eurozone:
  - CPI Core (Mar) (0.9% y/y)
- Italy:
  - CPI EU Harmonized (Mar) (1.6% y/y)
- France:
  - CPI (Mar) (1.2% y/y)
  - CPI EU Harmonized (Mar) (1.4% y/y)
  - Consumer Spending (Feb) (1.4% y/y)
- US:
  - Personal Spending (Feb) 0.2% (0.2%)
  - PCE Deflator (Feb) (1.9% y/y)
  - PCE Core (Feb) (1.7% y/y)
  - Chicago Purchasing Manager (Mar) (57.0)
  - U. of Mich. Sentiment (Mar) 98.0 (97.6)

Payment Redemptions: Italy (EUR 6.6 m)