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# ZINNECKER MONTHLY – 01 / 2018

## Review

Fixed income and currency markets remained stable to slightly up over the past month, ignoring the US interest rate hike. The New York and London stock exchanges moved on to record highs driven by newly raised global economic growth forecasts and the US tax reform. The Tokyo stock market after 36 years and several attempts has finally achieved an important cyclical recovery high. Other Asian markets posted new highs as well, while the European equity markets were not able to follow despite very good economic and corporate news. Negative interest rates, the rising Euro, competitive direct investments, the inability of the German political parties to form a new trendsetting government, the elections in Italy on the 5th of March and the political consequences of the Catalonian vote were the reasons to hold them back.

Looking at 2017, despite many disruptive factors on part of politics the global economy, has done much better with +3.6% growth than originally forecasted and with a still surprisingly low inflation. Against all market expectations the US$ not only had already peaked at the end of 2016 but also ever since has lost 10% against a basket of currencies. The Internet of things and the continued digitization so far have offset inflationary pressures stemming from higher wages due to labor shortages and rising commodity, oil and energy prices. The implementation of new high tech production systems has led to a strong recovery of labor productivity and to a further acceleration of the corporate earnings' momentum. In hindsight, for these reasons 2017 was a surprisingly good year for equities.

The returns of the US stock markets from 20%, 25% to 28% (S&P500, DJIA, and NASDAQ) have benefited from an average earnings' growth of 11% as well as from a renewed multiple extension of 9%. The reason was the favorable interest rate environment paired with a higher risk appetite of investors. This favorable constellation has also applied to various emerging markets, especially Asia, while Germany has suffered from a slight P/E contraction over the course of the year. Though earnings have grown by about 13%, the DAX Index just rose by 10%. London and Tokyo experienced similar contractions.

## Economic Outlook

The global economy should again grow by 3.6%+ this year. The US should continue to benefit with an estimated GDP growth of 2.6% after 2.3%. In the month of November, the OECD has raised its 2018 economic growth forecast for the EU and for Germany as the EU driving force, too, but it considerably lags the rest. The reasons are well known. Since 2008, the EU has struggled to implement structural reforms to revive the union economically, while in Asia new economic empires are about to arise. Asia over these years has managed to implement more flexible and competitive economic models, which serve the world markets and their citizens likewise and have created private and public wealth.

In Europe, the socialist and consensus economic models are definitely outdated. Europe will have to find answers to the challenges from outside earlier than later in order to become more competitive and to secure the new markets with a huge growing population. This is where Europe's economic future lies, Russia included.

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This step would also create a necessary balance of powers against the USA. Therefore, a solution for its eternal quarrels and the fiscal union is politically and economically unconditional and should be on every politician's to do list. Without Germany, Spain, Italy forming forward looking governments, following the French example, the economic and social future of Europe could be challenged sooner than later.

**Capital Market Outlook**

As in the past, politicians will again create various stumbling blocks, but with decent growing global economies, still low inflation and interest rates and double digit corporate profit growth the stock markets should continue to do well in 2018.
The US tax reform should help the US and the US subsidiaries of foreign companies to grow their profits by about 15%, compared with 10% in Europe. Given the rising labor shortage, wages will eventually rise in areas where robots cannot immediately replace people. Longer term, however, robots and artificial intelligence will loom and therefore wages should not rise excessively.
As the world has entered the stage of a late cycle economy with an increase in public and private capital-widening and infrastructure investments commodity and energy as often witnessed in the past, prices should start to rise. Together with rising wages, inflation could therefore challenge the magic number of 2% later in the year. Other Western central banks, following the recent path of the USA, should then begin to review their existing still excessive monetary policies.
The outlook for the bond markets with rising short and long-term bond yields looming should then become negative. At that stage of the cycle, it should possibly affect the equity markets with the start of a multiple contraction. Therefore, an active industry and stock selection policy should become even more important than before and should outpace passive investment strategies.
Technology and internet of things, financials, health care and capital goods should remain market drivers, as already witnessed in 2017. Commodity, mining, oil and energy as typical late cycle plays could also return to the focus of investors. Gold and gold stocks, so far not too attractive for non US Dollar investors, could also enjoy a revival, if a sustainable earnings' turnaround should become visible.
Within this investment matrix the US Dollar should start to stabilize from here on and even could strengthen somewhat, should Europe be going through a more difficult political patch or should a change in monetary policies become reality. Pound Sterling should stay mixed over the course of the year with a slightly weaker bias against the Euro and the US Dollar.

01.01.2018

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