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Review

Against all odds, the Western capital markets have produced positive returns last month. The equity markets, supposedly too expensive and overbought, have achieved new highs under the leadership of Wall Street. European government bonds have entered a counter rally against the expectation of a further interest rate hike of the Fed. Geopolitics, Brexit, Syria, the new US administration and the upcoming EU elections, have at best played an inferior roll. Only the vexed and presumably unresolvable Greek problem has again triggered a flight to safety into the Swiss Franc and into high graded government bonds.

Market participants collectively must have gotten many market influencing factors wrong and obviously had been caught on the wrong foot. Investors also underestimated the strengthening global economy and the strong corporate earnings revival of global leading companies. They have already beaten this year cautious brokers estimates. The leading US stock indices have achieved new all-time highs along with increasing market breadth and quality, which have forced all categories of investors to return to the equity markets. Evidently, they have been and presumably still are under-invested in risk assets and therefore they have to catch up over time with the proceeding market performance. This phenomenon should be even more valid for Continental investors, where in general investment strategies are less risk orientated.

Outlook

Politics as in the recent past should only play an inferior roll, although they could cause increased market volatilities from time to time. Investors should therefore concentrate more on the future development of the world economy and on the future earnings power of those companies that are not only globally exposed but also are dominant national players in the beginning restructuring process of their economies. It will start with the USA, where the new administration is about to roll out their plans in the weeks ahead and later in the EU, once the elections will be history.

The world economy, DM as well as EM, is in a better shape than originally anticipated and should surprise on the up side the further we move into 2017. Central banks in Japan and in Europe will be further supportive with their still loose monetary policies. The world economy is on its way back to reflation leaving behind last years' deflation fears. The US economy, consumer driven, is nearly at full employment. In addition, it should profit from the various announced stimulus programs later this year. As the US-inflation target of 2% has almost been reached, the Fed might already decide earlier than expected on another interest rate increase already in March - another sign that the US economy is back on track.

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The improving EM-economies will create additional demand for goods and services from the large export nations like Germany on top of their own economic recoveries. European earnings should therefore get an additional push on top of the benefits from a still positive low interest environment and from lower production cost through improved productivity and rising output.

Capital market outlook

Although equity market valuations are somewhat extended and politics weigh, the allover investment picture should remain positive into 2017. The victory of Mr. Trump and his first 5 weeks in office have been a wakeup call for EU policy makers and to the same degree for those Continental citizens who will elect their new governments in the months ahead. They are less ready for a political game change than their American fellows were. Therefore, the feared shift to the right should be ebbing and in the end, Holland, France and Germany will remain politically stable and as cornerstones of the EU predictable.

The Continental capital markets supposedly have not yet priced in the political benefits as well as any positive surprises at the economic front. As long as the all over interest rate and inflation environment remains positive, investors of all categories and investment styles for the lack of other rewarding asset classes should be biased furthermore towards investments in risk assets. It should give the equity markets repeatedly a new boost until the various portfolios will be risk balanced. International diversification diminishes portfolio risk and an overweight of European over American stocks could be a valuable alternative.

In respect of the periods after 1963, 1985 or 1996, this process could be long lasting and as in the past, it will be difficult to predict the end of this bull market that has already been in existence since 2009, as we all know.

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