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Review

During the first quarter, the Western economies returned to reflation mode. Rising employment, growing corporate earnings in nearly every industry and the recovery of inflation to over 2% and 2.7% in the USA caused the Fed already in the month of March to lift interest rates for the third time. The remaining central banks will stick to their adopted policies in order to stimulate the still anemic economic recoveries in their countries.

The stock markets therefore climbed to new highs or recovery highs by the middle of the month. Expectations of a new health care bill, a tax reform in the US and the possibility of a reviving democratic trend in Holland, France and Germany had fueled that move. The elections in Holland and the Saarland, a German state, has partially but not convincingly produced that revival. Only a higher participation of the electorate has helped to keep the populists at bay. In the USA, President Trump is hitting one roadblock after the other, first the immigration ban and now the healthcare bill. Mr. Trump as a political outsider is now facing political reality, which means, he needs to collaborate with both the house and the senate, if he wants to deliver on his campaign promises and to succeed as President. Ms. May from Britain meanwhile has invocated article 50 in Brussels and the tension between Turkey and Germany has reached critical diplomatic levels.

All of that has caused the stock markets to consolidate by the middle of the month, while the bonds have recovered from their lows and the US$ has weakened against its major trading partners. The emerging markets, China and Japan had a relatively quiet month.

Outlook

Politically the month of April will not only be spectacular but also critical for the further direction of the Western capital markets. President Trump will have to prepare his next big projects, the tax reform and the infrastructure program, deliberately, if he does not want to risk failing again. The tax reform is very likely to succeed, because all republican politicians want it. The implementation of a nationwide infrastructure program might be more difficult, as there should be a strong opposition against a massive expansion of the already immense public debt.

France will have the first poll of its presidential election in April and the second ballot on May 7. Germany will have two state elections in early May, which will be an important test for the SPD national candidate Martin Schulz and his party, which has governed the largest German state North-Rhine-Westphalia since 2010. The first test

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has produced a strong vote for Angela Merkel's party. The results of the two national elections - Germany in September - will be historical and trend setting in respect to the will to close the European integration process for good. 25 years after Maastricht with halfheartedly decisions, the time window is slowly closing and this historical project is at risk to fail, more than ever. Therefore, it will be up to Germany and France in the first place to find a binding solution in due time, even it were only to be achieved in the form of the ‘two speeds’. Luckily, all these open questions are happening on the back of a still strengthening world economy in a friendly monetary environment. In addition, investors should enjoy robust corporate first quarter earnings in the next few weeks.

Capital Market Outlook

On top of this, positive political developments in the USA and in Europe should revitalize the equity markets into the summer. The American equity markets as already in the past should further benefit from the long-term structural development in the fields of digitalization, automation, semi-conductors, data storage and the internet of things, like Google, Amazon, Apple and Facebook. These are the new cornerstones of global economic growth towards Industry.4. It should be valued as a strong proxy for the future momentum of the stock markets, in general. In contrast, financials and deep cyclical companies, whose stocks have consolidated since the first days of the year, should also come back to life, when the US government initiatives towards the proposed tax reform and the $1 trillion infrastructure plan should become reality.
The strong US $, slightly weakened commodity prices and stable bond markets have helped the companies, to report strong earnings, especially in Europe. It should continue into the summer. The relatively cheap Euro and relatively attractive European equity valuations have caused US investors to return to the European stock markets for the first time after two years. As the European stock markets have begun to outperform Wall Street and Tokyo in recent weeks, investors should therefore consider new equity investments in this area of the world.
As long as inflation stays comfortably low at around 2% despite increasing wage pressure, investors still might pick up long dated US treasuries as a flight to portfolio security and stability. This trend has also been noticeable in the stock markets, where non-cyclical, stable growers have attracted new investments in recent months. Gold and other commodities should benefit from a slightly weaker US$, but at current supply levels it seems to be unlikely to expect a new bullish trend.

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