Frank Th. Zinnecker

ZINNECKER MONTHLY 05 / 16

Review

The latest data have lead investors to believe that the global economic slowdown has finally run its course followed by a slow pickup of GDP growth for the larger economies during 2016. Economists believe that the aggressive central bank policies in Europe and Japan have only had a marginal impact on economic growth and therefore the overall criticism of the effectiveness has become louder. The capital markets have responded accordingly. Despite the massive monetary stimulus, government bond yields have not dropped any further and in the USA long bonds yields even went up a little. The stock markets have consolidated with a positive bias to the upside, while the US Dollar has further lost ground against the Yen and the Euro after the latest Bank of Japan decision to halt its monetary policy for now. The price of gold after its April consolidation, as a response to that, has broken out to new recovery highs at months end.

Outlook

It is becoming increasingly clear that the European and Japanese central banks and their governments are today at their wit's end. The 2009 originally introduced excessive monetary and interest rate policy in order to save the banking and financial system has until today not achieved its goals despite of a today's zero-interest rate policy in conjunction with an exuberantly grown monetary base. This policy has led neither to a restauration of the banking system nor to a sustainable recovery of the economies in Japan and the EU, because the governments have failed to accompany this process with the implementation of necessary fiscal and economic reforms.
This policy is now threatening to turn into the opposite. This is particularly evident on the example of Japan. The negative interest rate policy and the unprecedented intervention in the economic system over the excessive purchase of government bonds and Japanese equities has practically invalidated the efficiency of the free market economy. Despite all these monetary measures Japan still is caught in a deflationary recession with no end at sight and the Japanese depositors over time will be facing a creeping expropriation of their savings unless the government finally will start the necessary political reforming process that has been held back for too many years. The Japanese currency system has so far taken no harm, because the country has been able to shield its domestic economy from outside pressures, because they have been able to keep its savings domestically and maintain the export surplus in Japan.
The economic and monetary development, although in a somewhat different shape, meanwhile applies for the countries of the EU, especially Germany, too. As pointed out in last month's report the beneficiaries of the ultra-aggressive monetary and interest rate policy of the ECB have been the public finances in all EU countries. Without the conversion of old and the creation of new debt at ultra-low interest rates together with the tailwinds from rising tax revenues Mr. Schäuble would not have been able neither to achieve his balanced financial budgets nor the Mediterranean

Holzhecke 7 – D 60528 Frankfurt am Main
Telefon (069) 59 79 30 31 - Fax (069) 59 79 34 40 - Mobil (0171) 79 78 174
Email: frankzinnecker@t-online.de

countries would not have solved their debt crises. The other group that has greatly profited from this situation have been the large enterprises, private entrepreneurs and the wealthy individuals through the conversion and issuance of debt at much lower cost. The big losers have been the large hordes of employees and pensioners. The zero interest rate environment hampers the capital preservation of savings and the capital formation of private retirement plans. Political reforms of tax, pension and employment systems have also fallen by the wayside and will be socially and economically unconditional in the future. Otherwise, the gap between the rich and poor is going to widen even further.
The monetary experiment has not only led to an over dominating government influence but also to the further incapacitation of the public. In addition to that, the lack of political action and leadership with regard to the refugee crisis has meanwhile created such a degree of public frustration that the EU citizens have already presented the bill in the latest elections by voting extreme. German and Austrians voters have followed France with a strong support towards the right. The pending Spanish elections should support this trend. In the USA, the protest movement has found a controversial politician in Donald Trump, who presumably will run for presidency as the republican candidate against Ms. Clinton. Then the outcome of the presidential election would be widely open.

Capital market outlook

Therefore, the potential political changes should further increase markets volatilities even if the risk of a Brexit has slightly decreased after Obama's recent visit. Since Europe and Japan will stick to their ultra-light monetary policies, it has become likely that the FED will raise rates only after the election should economic numbers have improved by then. As government bonds and cash barely offer preservation of capital, institutional and private investors will again be confronted with the question where to invest future free reserves. Although the Western equity markets are already highly priced in historic terms, they still seem to be relative attractive against other asset classes, like property and real estate, private equity and objects of art, that have boomed over the last decade.
Therefore, stocks of world market leaders with outstanding business models, strong cash flows and rewarding dividend policies should renew investors’ long-term interest even at these financial valuations. This idea would even be more compelling, if, as the latest economic data suggest a modest revival of the US and the global economies over the remainder of 2016 together with again rising company earnings’ expectations should reignite the stock markets after the latest severe correction.
From a technical market perspective, the US stock market could then reiterate its structural bull market after the Dow Jones (17.770) and the S&P 500 (2.060) would exceed their old highs of 18.350 and 2.135 points. On the back of this, the European markets should also surprise on the upside with the STOXX600 (341) and the DAX (10.040) with readings of about 400 and 12.400 respectively.
Gold (US$ 1.293) has achieved a new reaction high at month end due to newly arising doubts about the efficiency of the global currency and credit markets after the latest decision of the Bank of Japan. It should also be regarded as an investment alternative from now on.

1.5.2016

Holzhecke 7 – D 60528 Frankfurt am Main
Telefon (069) 59 79 30 31 - Fax (069) 59 79 34 40 - Mobil (0171) 79 78 174
Email: frank.zinnecker@zinnecker-consult.com