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Investor Info

Investment Commentary

Briefing from the ARVEST Investment Committee

In the second quarter of the year, global equity prices corrected by 0.8% in Swiss francs. This was not least due to the weakness of the US dollar, which fell 4.5% against the Swiss franc and 6.8% against the Euro. This currency shift reflects, inter alia, a change in assessment of the political situation on both sides of the Atlantic. The election of Emmanuel Macron as president of France, supported by an absolute majority of his party "La République en marche", strengthened investor's confidence in Europe. On the other hand, the concrete implementation of "Trumponomics" now meets widespread skepticism. Growth potentials due to corporate tax cuts or infrastructure investments in the US are not expected to be realizable before 2018. The required bi-partisan compromise seems to be a long way off.

As we explained in our last investment commentary in April, the share price gains since the beginning of the year were driven mainly by the global economic upturn after the stabilization of the commodity prices in 2016. This was also reflected in corporate earnings growth in the first quarter 2017. In US-Dollar terms corporate profits rose by 14% in the US and by 27% globally. Oil companies recovered their earnings significantly. However, corporate earnings reports surprised across all sectors and many analysts are expecting further improvements in profitability.

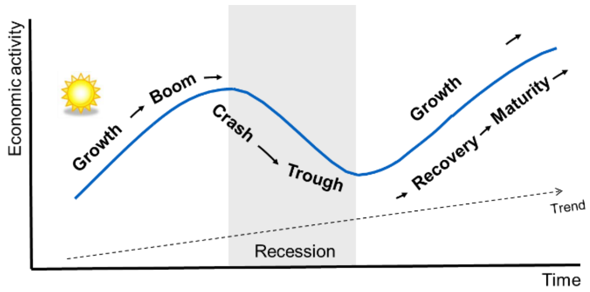
On the other hand, the oil price fell by 17% in US dollars in the first half of 2017. Does this hint at a relapse into the deflationary spiral that endangered the global economy and world trade as we experienced between autumn 2014 and spring 2016? Or, on the contrary, is a low oil price now advantageous to global consumption?

Currently, commodity prices, oil and economic stability in China are key for the cyclical assessment of the global economy by the ARVEST Investment Committee. Investors who were able to attend our "Clever invest" event in Zurich on May 31, 2017 have already received more detailed information from the commodity specialist Markus W. Amstutz, Future Trade AG and from us. Despite recent price fluctuations, the ARVEST Investment Committee still assesses the correction in commodity markets to be basically behind us.

This means that we continue to expect oil to trade in a range between USD 40 and 60.

This assumption presupposes among other things a steady growth in Chinese consumption. In view of the forthcoming elections of the Politburo and the Central Committee at the 19th Communist Party Congress in the autumn of 2017, the General Secretary Xi Jinping, who stands for reelection, will do everything he can to ensure economic stability. It is noteworthy in this regard that in recent months the Chinese government has nevertheless dared to tighten financial conditions, e.g. through interest rate hikes. It was intended to limit financial risks and to slow economic growth. As a result, the five-year yields of the local province bonds rose from 2.7% to 4.4% within 6 months. These measures also halted credit financing of unregulated Wealth Management Products. As an offset and as a first step, China began to open the local, regulated bond market to foreign investors in Hong Kong.

China's debt has risen at a worrying rate in recent years. We do not expect that China's total debt of more than 300% of GDP will decrease in the near future, although a substantial proportion of the creditors and also the debtors are state-owned or state-affiliated entities whose positions could theoretically be offset against each other. Due to the increased level of debt, monetary policy now has a much larger impact on the management of economic cycles than in earlier times. The facts that China has not yet experienced a recession since it opened up to capitalism and that China manages credit directly and anticyclically through its state banks, makes cyclical analysis of monetary policy extremely difficult. We must stand by the fact that China's position in the domestic economic cycle equals the proverbial invisible elephant in the room. We can only follow the developments on a regular basis and remain very cautious about forecasts. But we continue to trust in the expertise and the interests of the Chinese leadership.



Future Prospects

The ARVEST investment committee assesses the global economy as a whole to be in a moderate, synchronous growth phase in all regions. Taking into account the current economic cycle, low interest rates and low inflation, stock market valuations are relatively fair to expensive from a global perspective, depending on the region. We only rarely observe irrational prices which market participants are often prepared to pay during a boom period at the end of an economic cycle. In our opinion, this may be the case for a few US technology companies, where investors are extrapolating the current profit growth to far into the future. However, we continue to prefer shares and liquidity over bonds in the current low interest rate environment.

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On behalf of the Investment Committee
Stefan Kimmel
Chief Investment Officer ARVEST Funds AG

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