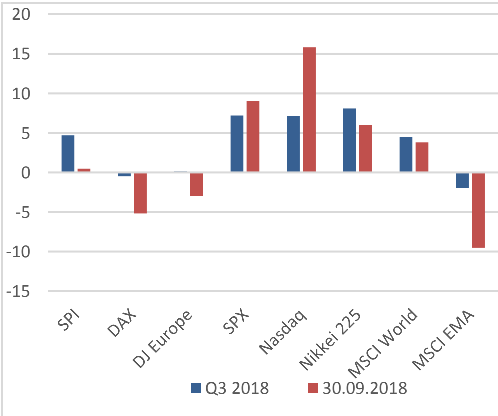
WYSS & PARTNER

Quarterly report September 2018

- The US/China trade dispute escalated further as the scope of goods being hit with punitive tit-for-tat tariffs gradually increased. The biggest concern here for the financial markets is what effect it will have on China's economy and that of other emerging markets. Self-inflicted problems in Turkey, South Africa and Argentina are exacerbating concerns over a fermenting economic crisis.
- The US economy showed continued robust growth, with unemployment falling below the prevailing level before the economic crisis. At the same time, pressure on wages remained modest and core inflation was around the Fed's target level of 2%. Corporate earnings increased by 26% in the second quarter relative to the previous year.
- The economic data for Europe and China were slightly sluggish, with China launching a number of measures to stabilise its economy. The ECB expressed optimism about the European economy and confirmed that quantitative easing would end this year. However, interest rates are unlikely to be adjusted for some time yet.
- In the US, the key interest rate was increased as expected to 2.25%, putting it 2.0% higher than at the end of the country's low-interest-rate policy. Yields on ten-year government bonds increased from 0.8% to 3.1% over this period.
- With the economy strong, risk premiums on USD-denominated bonds issued by private debtors fell by an average of 0.5%, giving an overall yield that was just on the positive side. However, top-grade bonds dipped slightly in the wake of higher interest rates on Treasuries.
- The new Italian government proposed a budget for 2019 that was somewhat different from the EU's expectations, pushing up interest rates on 10-year Italian government bonds to 3.14%. As a result, the spread between Italian and German interest rates doubled to 2.8%.
- The price trend in commodities was largely negative. After nine months, the CRB Index is down 4%, while the price of crude oil (Brent) has largely risen by fears of supply bottlenecks caused by political factors (Iran, Venezuela).
- The main currencies on the forex markets moved only a little. It was the Turkish lira that really stole the show; only being rescued from utter collapse by a dramatic hike in interest rates.
- **Equity performance** in local currency



- The equity markets gained around 4.5% compared with the World Index, while the Emerging Markets Index shed 2% (Asia excluding Japan 4%). The European markets largely broke even, keeping them in the red for the year to date. The US stock markets added 7%. At global level, the healthcare sector and IT industry posted above-average growth, while the commodities and real estate industries lost ground.

Outlook

We are sticking with our baseline scenario of robust economic growth, albeit at a slower pace, controlled inflation and a slight upturn in interest rates. The difficulties in individual EMAs remain isolated cases and will not trigger a chain reaction. The smouldering trade dispute between the US and China remains the biggest uncertainty, although it will have minimal real impact on the global economy (for the time being). While a solution to the dispute could well be found in the near future, the battle raging on various fronts for military, political and technological supremacy is likely to dominate the next few years. These long-term clashes will disappear off the media's short-term radar sooner or later, with a correspondingly positive knock-on effect for the financial markets.

The Democrats look set to regain a majority in the House of Representatives at the midterm elections to the US Congress in November. While this will place certain restrictions on the White House's policymaking, it will have little effect on its overall trajectory.

Looking to Europe, the UK's exit from the EU will remain a hot topic, particularly as all the forms it could take seem feasible but with different implications for the economy and the currency markets. Italy's abandonment of fiscal discipline will affect interest rates for Italian debtors to begin with. At its heart, the issue is less so about the stability of the EU and more so about the struggle in Europe between established parties with their fiscal discipline and upcoming populist parties whose promises can only be financed by new debt. Despite appearances, then, Europe is not taking the same route as the US under Trump. Deregulation and swingeing tax cuts are not the weapon of choice for those at Europe's helm. Given this, US equity markets are likely to continue faring better for some time yet.

October 2018