April 2016

Almost record improvement in sentiment sounds a note of caution

- Currency war affecting global equity markets
- Stock market valuation becoming much more attractive
- Risk appetite indicator: rebound in confidence has been too quick

After the mood had already started to brighten on stock markets from mid-February onwards, another boost came in March from the interventions by central banks. Mario Draghi, President of the European Central Bank (ECB) got the ball rolling. Once again he dug deep into the monetary policy tool chest to make sure markets are supplied with even more liquidity in the coming months. This time – in contrast to the start of the year – equity markets showed an extremely positive response to the news from Frankfurt. European equities performed particularly well, against the backdrop of a weaker euro. Next up was the US Federal Reserve (Fed), which met in mid-March. Its Chair Janet Yellen adopted a much more defensive tone than in previous appearances, assuring markets that any future interest-rate hikes would be modest. Her statements triggered sharp falls in the US dollar versus the euro, Swiss franc and Japanese yen. Once again this clearly demonstrates the measures that central banks are prepared to resort to in the current uncertain economic environment to gain a comparative advantage over their foreign competitors by keeping a weak domestic currency. The shares of US exporters benefited especially from the Fed’s more cautious monetary stance. Swiss equities were the main victims of the global currency war in March. While the S&P 500 Index advanced 6.6% and the Dow Jones EuroStoxx 2.7% in March, the Swiss Market Index (SMI) retreated 0.46%.

Stock market valuation becoming much more attractive

The Eniso asset allocation model used by AMPLIA shows that the monetary environment has been the driving force for equity markets since October 2012. This component continues to generate positive signals for equity investments, albeit to a slightly lesser degree, for precisely 12 months now. This trend has also continued in March. The gradual weakening of the “Monetary” sub-indicator was however compensated to a large extent by the sub-indicator “Valuation”, the second most important fundamental component. Following the sharp correction at the start of the year, valuations normalised on equity markets. The relevant sub-indicator climbed to its highest level since October 2012, giving a positive signal again for equities. Very little has changed in the real economic components “Industry“ and “Consumption”. While sentiment in industry recovered slightly, there was a slight dip in consumption. The fundamental environment is still generally positive for equities. Unfortunately there is still a risk that market developments will continue to be driven more by market psychology than by the fundamental data.

Monetary environment: Central banks across the globe are still following a very loose monetary policy, but the risks of a liquidity glut are increasing. There are signs of inflation starting to creep up in the USA especially. The reason can be traced back mainly to the labour market, as even low-skilled workers are now increasingly able to push through wage demands. However, input prices are moving higher as well, driven by the recovery in commodity prices. Even though the positive impact of the monetary environment has faded in recent months, it continues to act as an important support for equity markets.

Industry: As Europe’s top industrial location, Germany is still on a growth path, but a number of indicators are pointing to a gradual slowing in the pace of growth. By contrast, the situation in the USA is not as austere as last month's figures appeared to suggest. The slowdown in the pace of growth in the industrial sector is likely to be less pronounced than many feared.

Consumption: US consumer sentiment has steadily improved in recent months and has been a key factor for ensuring that the sub-component "Consumption" has so far been consistently positive for equities in 2016 as well. The only fly in the ointment is that actual consumer spending does not yet reflect the big improvement in sentiment.

Valuation: All the world's regions contributed towards the much more attractive valuation of equity markets. This is not just attributable to the price falls at the start of the year. The most recent figures published by many companies for both operating income and net profit were better than many analysts and strategists had expected.

Risk appetite indicator: rebound in confidence has been too quick

The fluctuations during the first quarter of this year were some of the most extreme ever recorded in the history of financial markets. January 2016 was the weakest start posted by stock markets since the Second World War. Investors offloaded their equities in January and February, almost in a state of panic. Investor sentiment dropped so quickly and so sharply, that the risk appetite indicator generated an anti-cyclical buy signal for equities from mid-February onwards, which ensured that both mandates and funds benefited from the subsequent share price recovery. In mid-March the situation was exactly the opposite: the unusually rapid rebound in investors' risk appetite, which was driven by a marked improvement in all five sub-components, resulted in an overbought constellation in equity markets. This confirmed the sell signal that we had still been getting at the end of February due to the unstable market conditions. As a result, we maintain a cautious stance and are only holding half the maximum possible equities quota in the funds and mandates. A fresh buy signal is expected once the quite euphoric investor sentiment reverts to normal. This could happen as early as next week.

Risk appetite indicator: Rebound in sentiment too quick and too much

	Anzahl Indikatoren	Aktuelle Signale	1 Woche	1 Monat	3 Monate
MONEY FLOW	31	Buy	↗	↗	↘
SURPRISE EFFECT	17	Buy	↗	↗	↗
MARKET BREADTH	24	Buy	↗	↗	↘
HEDGING DEMAND	7	Buy	↗	↗	↗
MARKET RISK	37	Sell	↗	↗	↘
OVERBOUGHT / OVERSOLD		neutral			
RISK APPETITE INDICATOR	**116**	**SELL**	↗	↗	↗

Your Contact at Amplia & Co. AG

Mikael Rosenius
Claridenstrasse 34
CH-8022 Zurich
Tel. +41 44 286 17 41
mikael.rosenius@amplia-co.com

Jennifer Erdin
Claridenstrasse 34
CH-8022 Zurich
Tel. +41 44 286 17 42
jenny.erdin@amplia-co.com