May 2018

Hope for the best, prepare for the worst

- Strong company results alone are not enough for the market
- Weaker economic growth at the wrong time
- Downbeat mood sounds a note of caution

The weather pattern in April was just as unpredictable as the performance of financial markets. At the beginning of the month, stock markets were unsettled by the threat of punitive tariffs. Equities rose or fell depending on the news flow. Shortly thereafter, it seemed as if the Syrian conflict would escalate and push the trade dispute into the background. When this seemed unlikely, markets concentrated instead on quarterly results. Of the Q1 figures published by companies to date, more than 80% beat the very ambitious targets. Overall earnings growth was impressive, at more than 18%, while the market's net profit margin rose to 11.1%, its highest level since the third quarter of 2008. In short, the figures should have reassured investors. Nevertheless, share prices in the USA fell again towards the end of the month. Above all, rising interest rates overseas caused uncertainty. After all, 10-year US Treasury yields broke through the of 3% mark, a level last seen in 2014. The US dollar benefited from this development, firming by more than 1.5% against the euro, while the bond and equity markets found the going tough. On the bottom line, the S&P was virtually unchanged, while the EuroStoxx and Swiss Market Index benefited from the stronger Greenback and gained almost 5% and well over 3% respectively.

Weaker economic growth at the wrong time

It was always obvious that President Trump's policy on trade tariffs would have consequences for economic growth. Even so, it is quite surprising that this should be reflected so quickly in the prospects for the manufacturing industry in the regions mostly affected – Europe and Asia. The subindicator "Industry" therefore fell back relatively heavily from its high level. In addition, even consumers in the USA seem to be unsettled. Both personal spending and consumer confidence deteriorated markedly in just four weeks. The emerging economic downturn comes at an unfavourable time for stock markets, as the headwind indicated by the important subindicator "Monetary Policy Environment" has continued to strengthen. Even so, the Valuation is improving a little in response to good company results in the USA especially. Overall, ENISO's fundamental model for asset allocation is stuck in equities-friendly territory, although a sell signal was only very narrowly avoided. We therefore favour a more defensive portfolio composition, but given the fundamentals we are not yet reducing the equities quota.

Monetary policy environment: The tax relief in the USA will further inflate the budget deficit, which will have to be financed accordingly via government bonds. In addition, there are increased signs of a surge in inflation. This is particularly evident in the producer price outlook, which shows a clear price increase in surveys conducted by the Institute of Supply Management (ISM). Overall, these developments will raise interest-rate expectations, which will be detrimental to the stock market. This month the subindicator is therefore once again much more negative than in the previous month.

Industry: The threat of tariffs is weighing on growth prospects for manufacturing in Europe and Asia. Europe in particular has so far shown the highest growth momentum on a global scale, hence the sharp decline at present in the subindicator.

Consumption: While consumption in Europe remains stable, US consumers are spending less freely. In addition, they view the outlook less positively than a month ago. A bright spot is the US housing market, which is showing higher sales figures for the first time in months.

Valuation: The considerable overvaluation of the US stock market was further reduced thanks to excellent quarterly results reported by companies. Such a weak overvaluation was last seen ten months ago. Despite this, the valuation of equities overall is still too high.

Downbeat mood sounds a note of caution

After weeks of indecision, our Risk Appetite indicator finally gave a sell signal in the second week of April. We therefore reduced our equities quota over the following five trading days. The sell signal still applies. Although there was a slight recovery in the subindicators Market Breadth and Market Risk, both important for risk appetite, they are still giving a buy signal. At the same time, three other subindicators declined again over the course of the month. As a result, although the Risk Appetite indicator improved slightly, investors still do not

Risk Appetite indicator: Only a feeble recovery in the subindicators

	Number of Indicators	***Current Signal***	*1 Week*	*1 Month*	*3 Months*
MONEY FLOW	*31*	Buy	→	↘	↘
SURPRISE EFFECT	*17*	Sell	↗	↘	↘
MARKET BREADTH	*24*	Sell	↗	↗	↘
HEDGING DEMAND	*7*	Buy	↗	→	↘
MARKET RISK	*37*	Sell	→	↗	↘
OVERBOUGHT / OVERSOLD		Neutral			
RISK APPETITE INDICATOR	***116***	SELL	↗	↘	↘

seem to be that confident. The dominant mood was more one of uncertainty, which could immediately trigger price falls in the event of negative news flow. For the first time in nine months, the Risk Appetite indicator is therefore sounding a note of caution again and suggests a defensive portfolio stance.

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