

Economic & Asset Class Outlook

March/April 2016 Outlook



	World economy	Monetary Policy, Inflation and FX	Bond markets	Equity markets	Alternatives and Commodities
Near Term	<ul style="list-style-type: none"> There are initial signs that U.S. manufacturing may be stabilizing with several regional surveys turning positive. While housing data is solid, consumer spending has been tepid. In Europe, manufacturing has been positive, the labor market is improving and personal consumption is solid. However, geopolitical risks are beginning to weigh on sentiment. Slow global growth has weighed on manufacturing and business confidence in Japan. Emerging markets continue to be challenged by slow global trade, political headwinds and sluggish domestic demand. 	<ul style="list-style-type: none"> Slower U.S. economic growth has resulted in the FOMC downgrading their outlook on growth, inflation and magnitude of Fed funds rate hikes in 2016. The ECB will likely remain in a wait and see mode and let the aggressive actions taken at their March meeting (e.g. negative interest rates, increased QE) filter into the economy. The PBOC and BoJ will keep the door open to take additional stimulus measures to support growth (e.g. QE, rate cuts). The USD should gain momentum vs. the developed markets as Fed policy diverges from other central banks. 	<ul style="list-style-type: none"> Global bond yields will likely remain lower for longer despite the Fed's tightening cycle and modest pick up in inflation. The rise in yields in the near term should be limited due to low commodity prices, central bank QE (ECB and BoJ), geopolitical risks (e.g. Brexit) and concern over at least a modest pullback in risky assets. We remain modestly overweight high yield but active management is recommended. We remain underweight EM debt due to uncertain economic fundamentals, volatile currencies and heavy USD denominated debt burdens. 	<ul style="list-style-type: none"> Most global indices have rallied 10%+ since their Feb. lows. As a result, valuations look stretched, technicals are approaching overbought territory and near term caution may be warranted. We reduced our weighting to global equities by lowering the U.S. (still overweight) and Europe (to neutral). Still favor DM vs. EM. In the near term, global equities may be challenged by weak earnings, geopolitical risks and stretched valuations. Favor select cyclicals over defensives. In EM favor Asia over Latam. 	<ul style="list-style-type: none"> With oil production continuing to come down (rig count near seven year low) and the dollar remaining under pressure, prices have been able to find near term stability. However, it is too early to suggest the bottom in oil prices is behind us. Oil prices will likely be challenged in the near term as the dollar gains strength and the ongoing supply/demand imbalance remains. Gold has been supported by geopolitical events, aggressive central bank actions and slower Fed rate hikes. Increased volatility to favor select hedge funds.
Long Term	<ul style="list-style-type: none"> Tighter financial conditions in some areas (e.g. U.S.), weak global trade and geopolitical risks have led us to downgrade our 2016 global growth forecast (from 3.4% to 3.2%). All developed markets were brought lower led by the U.S. (from 2.4% to 1.9% in 2016) as an inventory drawdown, weak manufacturing and slow exports may weigh on growth this year. Europe and Japan were modestly reduced but aggressive central bank policy should support growth. EM growth should gradually recover as commodity prices find a bottom, reforms take hold and FX volatility subsides. 	<ul style="list-style-type: none"> Ongoing geopolitical risks and lower growth than originally anticipated will likely limit the Fed to raise rates one time this year (likely June meeting) with one post election. This will be highly dependant on the outlook for growth and inflation. A weak Euro and stabilization in commodity prices should help Europe inflation move higher. Growth and interest rate differentials and diverging monetary policy support the dollar long term, especially versus the Euro and Yen. China and India should remain accommodative while Latin American countries have less flexibility due to high inflation. 	<ul style="list-style-type: none"> The rise in long term yields over the next 12 mos will likely be muted as moderate inflation, a "slow" Fed tightening cycle and aggressive stimulus from the ECB and BoJ keep global sovereign yields contained. We recommend a modest short duration to the benchmark due to the expectation of modestly higher yields in the long run. Focus on select credit (e.g. IG and high yield). History suggests credit outperforms sovereigns in tightening cycles. Cautious on EM debt due to the uncertain growth outlook but looking for opportunities to add. Active management advised, especially in high yield. 	<ul style="list-style-type: none"> Over the next 12 months, equities should be supported by improving earnings growth, modest economic growth and accommodative central banks. However, heightened volatility will offer tactical opportunities to adjust positions (e.g. regions, sectors) as warranted. As the economic cycle matures (especially in U.S.), returns should be driven by dividends, buybacks and earnings growth. Favor DM over EM due to more attractive fundamentals, better earnings visibility and greater monetary policy flexibility. In EM, favor Asia vs. Latam due to more attractive fundamentals and policy flexibility. 	<ul style="list-style-type: none"> The combination of heightened volatility, over supply and stronger dollar keeps us underweight commodities. However, an expectation for better global growth (in 2016) and likely production cuts should support a modest rise in oil prices over the next 12 months (Mar 2017 target=\$50). Another way to complement commodity exposure is through investments less sensitive to the price of oil (e.g. MLPs, oil transportation & storage). We favor hedge funds with a focus on equity market neutral. These should benefit from dispersion within equity sectors and regions.

Deutsche Bank
Wealth Management

Footnotes: Outlook as of March 21, 2016 Multi-Asset Investment Committee Meeting and March 22, 2016 Americas Regional Investment Committee
Source: Deutsche Bank Wealth Management

19