# ECONOMIC & FINANCIAL OUTLOOKS

## MARKETS OVER-COMPLACENT?

**For a change, the summer period was very calm on the markets, as is exemplified by the total subsidence of volatility on the main asset classes. Ultimately, the economic environment has changed very little over the course of the summer. The result of the Brexit referendum did not lead to a collapse of the UK's economic indicators, and there are no signs of dramatic change in the economic trends of Eurozone.**
**Moreover, numerous central banks have continued to support the markets by pursuing a more flexible monetary policy or by preserving an extremely conciliatory approach in their public statements.**
**These various factors have therefore created a favourable climate for risk assets. Does this mean that the risks identified at the start of the summer have all disappeared? What developments can we expect in the economic and financial environment over the next few months?**

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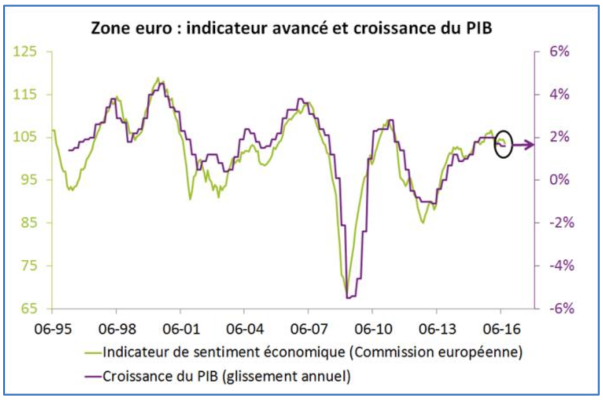
### ▪An economic environment that has changed little over the summer.

***The economic trends of the summer have globally confirmed our main messages of the spring,*** namely:

- with regard to the overall economic situation, the cyclic recovery is continuing, and the global economy is more resilient to uncertainties. The Brexit referendum is expected to lead to slower growth of the United Kingdom but should not plunge the country into recession. In the Eurozone, the business climate is expected to cool slightly under the influence of foreign exchanges, but there is no sign of major disruption, and we can conclude that the economic recovery is continuing. In the United States, growth is relatively balanced, but economic surveys suggest that the elections constitute a factor of caution. Finally, in China, real estate investment is disappointing at this stage, but economic activity remains robust.




- With regard to any expected changes in the policy mix, the margins for manoeuvre in monetary policy are currently limited, so that any "innovation" will now come from budgetary policies. More globally, the acceptance of the "new normal" is leading to a rethink of economic policy.

## ▪Central banks still the focus of everyone's attention

***The statements and actions of central banks over the summer have had a soothing effect on the markets. The uncertainties now reappearing with regard to their next impending actions, in particular in the case of the Fed, are likely to unsettle the markets.***

Our monetary policy forecast has remained unchanged since the beginning of the summer: divergence still prevails.

The Fed is expected to continue its policy of very gradual normalization. We expect it to raise interest rates by the end of the year, whereas the ECB, BoE and BoJ are thought to be envisaging increasingly accommodating monetary conditions.

The coming interventions of the central banks remain crucial and will determine the volatility of the markets.

## ▪An extremely important political agenda heading into 2017

***Although political risks have weighed less on the markets over the last few weeks, the diary for the coming months is very full.***

In Europe, by the end of 2016, the Brexit discussions should be back on the table, with their retinue of public declarations. The referendum on constitutional reform in Italy will be held during the autumn, and Spain has until 31 October to form a government and avoid another round of elections at Christmas.

In the United States, the political agenda will be dominated by the presidential election.

***Various asset classes enjoyed a constructive summer period, with good performance and minimal volatility.***

***The next few months are expected to see a return of volatility, fuelled by the various risk factors that have been put on mute by the markets over the last few weeks.***

**…**

## > OUR FORECASTS FOR ASSET CLASSES UP TO THE END OF THE YEAR

**Fixed income:** we anticipate an environment of very low fixed income rates, with reinforced volatility.

In the US, the anticipated increase in the FED's rate before the end of the year, in combination with an increase in inflation are expected to cause slight tension on long-term rates, increasing to 1.80% for 10-year investments by the end of 2016.

In the Eurozone, the German 10-year rate is expected to hover around zero within a relatively large range of variation. A positive inflation trend will lead to a slight tension on European rates, which should be offset by the very large amounts of liquidity in search of investment by the end of the year.

| | M | | Prévisions Groupama AM | |
|---|---|---|---|---|
| Données de Marché | 08/09/2016 | Variation YTD | déc.-16 | juin-17 |
| *US* | | | | |
| Taux Fed Funds | 0,50 | 0,00 | 0,75 | 1,00 |
| Tnote 10 ans | 1,54 | -0,05 | 1,80 | 1,90 |
| Euro | | | | |
| Taux Refi | 0,00 | -0,73 | 0,00 | 0,00 |
| OAT 10 ans | 0,17 | -0,82 | 0,30 | 0,50 |
| Bund 10 ans | -0,12 | -0,75 | 0,00 | 0,20 |

**Credit:** the important decisions of the Fed, the Italian referendum, the American elections and the start of Brexit negotiations are expected to lead to a return to risk aversion, at a time when the levels attained for spreads and volatility are at their lowest since the start of the year, with the support of the ECB's purchase programme.
Credit spreads are therefore expected to follow the trends of risk aversion, although we do not anticipate any extreme tension, since the interventionism of the central banks (in particular the ECB and BOE) should limit the risk of any major increase in risk premiums.

**Shares:** the sustained trend of high potential growth without any expected upward revisions of profit growth constitutes an argument for maintaining share targets close to current levels up to the end of 2016. Although we anticipate only minor movements in share indexes, this final quarter of the year is unlikely to be an entirely smooth ride on share markets, and we anticipate phases of consolidation.

| Données de Marché | M 08/09/2016 | Variations depuis le 31/12/2015 | Prévisions Groupama AM décembre-16 | | juin-17 | |
|---|---|---|---|---|---|---|
| France (CAC 40) | 4542 | -2% | 4600 | 1% | 4700 | 3% |
| Zone Euro (EuroStoxx) | 332 | -4% | 340 | 2% | 345 | 4% |
| Royaume-Uni (FTSE 100) | 6859 | 10% | 6900 | 1% | 6900 | 1% |
| Etats-Unis (S&P 500) | 2181 | 7% | 2200 | 1% | 2250 | 3% |

## >IMPLICATIONS FOR OUR MANAGEMENT STRATEGIES

**Core rates**: our portfolios remains predominantly geared towards caution, as is reflected by a slight under-exposure. This approach is accompanied by a slight flattening position on long-end curves: the search for yield remains a driving force (with negative German rates on debts with a maturity up to 10-years), while the purchases of the ECB and BoE constitute a support for long-term debts.
Over-exposure in inflation-indexed bonds is maintained. Valuations still consistently integrate very negative inflation in 2016: the ECB's purchases of nominal debts alone prevent any major surge in anticipations of inflation, but the fact that the HICP € inflation index will be close to 1% by the end of 2016 should be noted.
In terms of country allowances in the Eurozone, we remain moderately positive on these peripheral risk premium levels: positive carry is the main argument, and we thereby preserve margins of manoeuvre to take advantage of volatility peaks.

**Credit:** our positioning gives priority to non-directional carry strategies. We therefore prefer exposure to securities having an attractive yield and new bond issues with premiums. The intermediate maturity segments are under-weighted due to their low relative value. We are establishing protective purchases to limit the global exposure of our portfolios, taking into account spread levels, while anticipating a return of their volatility.

**Shares:** in a market context that is difficult to predict and contains significant hidden risks, we are adopting a balanced and watchful position. We are therefore aiming for maximum diversification of our asset risks. We are maintaining a strong preference for niche growth leaders.
We are rebalancing the positioning of our funds with the purchase of financial sector stocks, in particular in banks, for which we had

maintained a cautious approach for several months, and we are taking our profits on our defensive stocks. Selectivity is the key here, and we are keeping the stocks that offer that best growth prospects.
We are continuing to reinforce securities that are undervalued due to their fundamentals, in particular shares in companies sensitive to emergent markets (raw materials and industrials).

**Allocation:** we are maintaining a position that is close to delta-neutral, with a preference for credit over State borrowing.
Within this overall share allocation strategy, we are rebalancing the geographical allocation between the US and the Eurozone. We are reducing low-volatility strategies and reintroducing exposure to American small and mid caps.
In fixed income allocation, risk is concentrated on credit, via an exposure to "high-yield" and "investment grade" euro bonds and on emergent debt in hard currencies.
For the purposes of risk management, we are increasing exposure to fixed income markets and also preserving exposure to the dollar. These last two strategies will enable us to partly compensate for the main portfolio risks taken in periods of revived risk aversion.

The anticipated consolidation phases of share markets will be utilized to progressively reinforce the risk in our allocations.

## Notice



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