GENERAL INVESTMENT CLIMATE

The Economy

The European stock markets concluded the difficult year 2018 with a disappointing quarter. And finally, after three quarters of extraordinary resilience, the US stock markets also caved under the negative news pressure. October marked the start of an oil crash, with oil prices dropping 40% below their 4-year high over the course of the quarter. This extreme reaction was contributed to growing concerns over economic growth in light of the trade war, oversupply in the market and scepticism about additional production cuts by OPEC+.

Arguably the biggest shock for the European economy was the introduction of WLTP: the new emission and fuel consumption tests for passenger cars. The major German car manufacturers weren’t able to get all car models homologated in time, leading to substantial production cuts. As if dealing with WLTP wasn’t bad enough the automotive manufacturers also reported a slowdown in Chinese demand. The reduced car production also affected sectors which aren’t purely focused on automotive, like the semiconductor sector. This couldn’t have come at a worse time as this sector was already dealing with declining consumer electronics sales. Meanwhile the German chemical industry had to cope with the low Rhine water level impeding its transports, thus driving up costs. After a tumultuous first month, the markets managed to stabilize in November. However, oil stocks continued to plummet along with oil prices.

December ended up being even worse than the first two months with harsh corrections, especially for the US stock markets. Profit warnings started rolling in, central banks made unpopular decisions and geopolitical tensions flared up again. Arguably the most notable development on the political front was the arrest of Huawei’s CFO – and daughter of its founder Ren Zhengfei– Meng Wanzhou. Yet another episode in the escalating trade war between the US and China. She was detained in Vancouver at the request of US authorities for covering up violations of sanctions on Iran. China was outraged and the markets immediately feared for the tenuous trade truce brokered at the G20 between Trump and Xi Jinping.

As planned the ECB announced it would stop buying bonds by the end of December. ECB President Draghi showed cautious optimism with regard to the future development of the European economy. However, the central bank did lower its growth forecast for 2018 from 2% to 1.9% and for 2019 from 1.8% to 1.7%. Draghi also announced rates will remain at this level at least until the end of the summer of 2019. Additionally, Draghi confirmed his confidence that the Eurozone would remain close to the 2% inflation target despite the lowered growth prospects.

On the 19th of December their US counterpart decided to increase rates for the fourth time in 2018, much to the dismay of president Trump. The federal funds rate was raised with 25 basis points to a range of 2.25 to 2.5%. On top of that Powell announced two more rate hikes for 2019. Even though this was below the previously planned three hikes, it was still above market expectations given the lowered economic growth forecasts. In the meantime Trump keeps questioning the Fed’s policy publicly.

Finally a word on macroeconomics: The economic expansion on quarterly basis in the Euro Area dropped compared to last quarter from 0.4% to 0.2%. US growth also took a hit, dropping from 4.2% to 3.4%. Inflation in the Euro Area declined from 2.1% to 1.6%. In the US inflation also lost momentum, dropping from 2.7% to 2.2%. Despite signs of an economic slowdown, the unemployment rate in the Euro area continued to decline from 8.2% to 8.1%, the lowest level since November 2008. The US jobless rate continued to hover around a level of 3.9% but even dropped as low as 3.7% .

Currency and Money Markets

The US dollar remained strong and appreciated further against the euro. Possible drivers behind this are the weaker euro after the lowered growth expectations for the Euro Zone and the hawkish stance by the Fed in the US driving up the US dollar. Sterling managed to regain some ground on the euro by the beginning of November but started to slide again as fears of a potential hard Brexit began to grow. Despite the tight timeframe prime minister Theresa May decided to postpone the vote on the Brexit deal. This was seen as a clear admission she did not believe it would survive parliament. After the news the British pound tumbled to its lowest level in 18 months, settling on a level around 1.11 euro per GBP.

Stock Markets

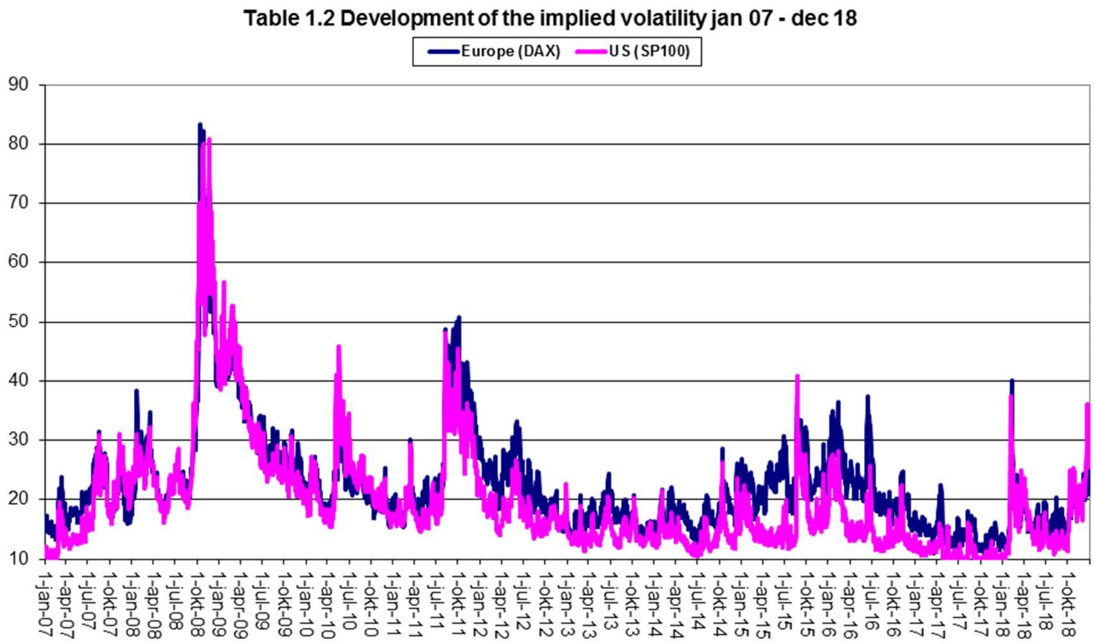
Table 1.1 - General

	31-dec-18	30-sep-18 - 3 mnth	30-jun-18 - 6 mnth	31-mrt-18 - 9 mnth	31-dec-17 - 12 mnth
AEX	487,88	-11,23%	-11,56%	-7,86%	-10,41%
BEL20	3243,63	-12,49%	-12,80%	-15,90%	-18,46%
DAX	10558,96	-13,78%	-14,20%	-12,71%	-18,26%
EU50	3001,42	-11,70%	-11,61%	-10,71%	-14,34%
DJ	23327,46	-11,83%	-3,89%	-3,22%	-5,63%
SP500	2506,85	-13,97%	-7,78%	-5,07%	-6,24%
Nasdaq	6635,28	-17,54%	-11,65%	-6,06%	-3,88%
EUR/USD	1,1469	-1,16%	-1,83%	-6,94%	-4,46%
Euribor 3 months	-0,309	0,009	0,012	0,019	0,020
NL govt 10 year	0,390	-0,190	-0,072	-0,253	-0,139

At last it seems the US investors have faced reality and started cashing in their chips. After two quarters of irrational bullishness the North American indices underwent a severe correction. Nasdaq clearly got the worst of it as its darling FAANG stocks were first in line to get hit. With the trade war starting to make its presence felt, investors became very worried over a possible recession. This made hot growth stocks like the FAANG group a prime target. The S&P500 was slightly better off but still took more of a beating than most of the European indices, which already started sliding the past few quarters. The German DAX had its worst year in a decade with a drop of over 18% since the start of the year. This is no surprise given the issues in the car industry and the trade war being more significant for an export-focused economy. On an annual base the US stock markets performed significantly better with -6.24% for the S&P500 and -3.88% for the Nasdaq. However, it does seem like the correction in the US is only just beginning. What will 2019 bring for the markets? Only time will tell.

Implied Volatility

It seems Wall Street has finally embraced the bear market. October marked the start of widespread selloffs and investors started looking for a reason to sell rather than to remain optimistic. This naturally came with a big spike in volatility and for the first time in a long while we saw US market volatility significantly overshoot that of the European markets. This turmoil is expected to spill over in 2019 to some extent while the trade war negotiations and Brexit deadline still lie ahead.



The Long Term

Again we see the AEX perform significantly better than its European peers, especially on an annual basis with 'only' -10.41% compared to, for example, the Euro Stoxx 50 with -14.34% and the DAX with -18.26%. Of course, as we have mentioned in previous reports, the AEX has a very different composition from other EU indices.