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## Macro data: Dynamics down

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The dynamics of the economy and the markets have declined. Global economic growth is down on a quarter-on-quarter basis, the two most important trends of the past months (appreciation of the US dollar and falling oil price) have come to a halt, inflation is not falling anymore, and the US Fed has put a damper on the expectations of interest hikes. One important exception: the Eurozone has been picking up speed.

### Growth dent in the first quarter

The estimate for real global economic growth in the first quarter of 2015 has been revised downward many times in the past weeks (currently 2% annualised quarterly growth). This was mainly due to the disappointing economic data in the USA, Japan, Brazil, and China. At least some important leading indicators such as the composite leading indicators from the OECD, the purchasing managers indices from Markit, and some surveys regarding consumer sentiment suggest stable growth. In line with this scenario the estimate for the full year of 2015 remains at +2.8%. This implies an acceleration of economic growth from Q2 onwards.

### Recovery in the Eurozone

One region has been standing out with positive surprises. It looks like the Eurozone may have recorded growth of an annualised 2% q/q as early as in Q1. The weaker euro in relation to other currencies, the fallen oil price, the decline in interest rates, the lower savings pressure from the governments, the loosening of the lending terms by banks, and the expansive central bank policy have been supportive.

### Loose ECB policies

The European Central Bank has triggered a drastic decline in bond yields in the Eurozone for surplus capital held by banks with the implementation of the comprehensive bond purchase programme (QE) and the negative interest rate policy. Remarkably, the purchase volume of the ECB exceeds the net issue volume of government bonds in the Eurozone. In such an environment the widening of spreads for country default risk is only temporary, much like it was in March. The reduction of real yields (i.e. nominal yields minus inflation) in the Eurozone is an important transmission channel of the ECB policies. In addition, investors are also pushed into other segments with higher promised yields (e.g. equities, corporate bonds). The rising security prices create an asset price effect. Also, the euro has already depreciated significantly against other currencies. Parts of the surplus capital flow out of the Eurozone. The ECB policy also helps reducing the fragmentation of the financial sector in some Eurozone countries. Lastly, with the QE and the OMT programme (Outright Monetary Transactions; unlimited provision of liquidity for a country in case of emergency) the risk of negative spill-over effects in the event of Greece's exit from the Eurozone has decreased substantially as well.

### Grexit / Graccident

The dispute between Greece and the Eurozone can be called a game of chicken. If neither party yields, Greece leaves the Eurozone, and a depression follows, debt will be written off, and the risk of disintegration of the Eurozone increases. If the Eurozone yields to the demands of Greece (debt reduction, end of austerity), the structural reforms will be postponed to the twelfth of never, and there is negative learning (moral hazard). If only Greece concedes, more years of internal devaluation will follow (reduction of unit labour costs), and unemployment will remain high. Although the parties to the negotiation are starting to display signs of exhaustion, a compromise (i.e. the credible promise of structural reforms, financial aid) would benefit both parties.

### Disinflation is coming to an end

In accordance with expectations, the trend of falling rates of inflation to lower and lower levels did not continue in February. Global inflation was at 1.6% y/y in February. This was mainly due to the stabilisation of the oil price since February in the wake of the strong decline in the previous months. For the rest of the year inflation seems to be accelerating slightly towards 2% y/y.

### Stabilisation of the oil price

Two opposing forces are currently affecting the oil price. The escalation in Yemen suggests an increase in the price of oil, whereas the chance of a positive completion of the negotiations of the P5+1 countries with Iran would indicate a falling oil price. What remains, is an increase in volatility.

### The doves in the Fed

The US central bank put a damper on the market's expectations of interest rate hikes in March by the members of the FOMC's downward revision of the estimate for future Fed funds rates

and the assumption of an increase in productivity. In addition, the significant appreciation of the US dollar and the disappointing economic data have contributed to the dampening of the interest rate outlook. Conclusion: the Fed funds rate will be raised by a maximum of the equivalent of the rise in the rate of inflation (zero real interest rate policy). Due to the pressure exerted by the rising US dollar, this will probably even happen at a lower extent (i.e. one or two hikes this year).

### Stabilisation of the US dollar

Since the indirect foreign exchange interventions by the Fed, the appreciation of the US dollar relative to other currencies has stopped (i.e. since March). The picture of a "currency war" is still valid. With regard to the EUR/USD exchange rate, the increasing current account surplus in the Eurozone suggests an appreciating euro, whereas the diverging monetary policies between the Eurozone and the USA are having the opposite effect. Ultimately, for a further significant strengthening of the euro the QE would have to be expanded, the negative interest rates on deposit accounts by the ECB would have to be cut further, or the expected increase of the Fed funds rate would have to happen sooner than expected. For now the Fed has drawn a line in the sand at EUR/USD of 1.05.

The environment remains constructive for the financial markets for the time being. The question of whether global economic growth will actually accelerate will be crucial to equities. After all, the valuations are not cheap anymore, and liquidity is strong anyway. In the Eurozone bond yields remain very low in spite of the improved economy (surplus liquidity, financial repression). The dampened expectations with regard to interest rate hikes in the USA are directly positive for US bonds and indirectly for the emerging markets.

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