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Capital market review 2015

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Capital markets experienced significant price fluctuations in 2015. While euro government bonds recorded a relatively good performance contrary to expectations, riskier bond segments such as high-yield corporate bonds were disappointing. Regionally speaking, stock exchanges recorded a very mixed set of performances. Emerging markets such as China and Brazil ended up on the disappointing side, whereas the European equity markets posted significant gains. The important US equity market went sideways (in USD terms).

Investors with US-Dollar exposure benefited from the appreciation of the US-Dollar relative to the EUR. Commodity prices, above all oil, remained locked in their downward trend throughout the entire year. Emerging markets currencies also experienced falling exchange rates.

Global equities in local currency and in Euro (01/2011-12/2015)

1

Source: Thomson Reuters Datastream as of 31.12.2015; the chart does not include any fees; past performance is not a reliable indicator of future performance.

Weak emerging markets and economic recovery in the developed economies

The two driving factors of the markets were the economic weakness in the emerging markets and the continuation of the economic recovery in the developed economies. The weak economic growth in the emerging markets is based on the general slowdown of credit growth. In addition, the profitability of the corporate sector has fallen. The rising cost pressure weighed heavy especially on the large economy of China, which is going through a transformation process towards a service-oriented economy.

These factors depress commodity prices and at the same time affect global industrial production. The global inflation pressure therefore remains very low. In spite of these developments the developed economies have proven resilient. However, the downside risks still increased, as manifested, among other things, by company earnings, which were stagnant, and indeed declining for some sectors.

Development of yield of 10-year-German Government Bonds (01/2011 – 12/2015)

2

Source: Thomson Reuters Datastream as of 31.12.2015; the chart does not include any fees; past performance is not a reliable indicator of future performance.

Monetary policy of the ECB remains expansive

In the Eurozone investors were focusing on four developments:

- Greece was close to leaving the Eurozone. In July, a temporary solution was found on the back of the agreement of a bailout package.
- On the monetary side the implementation of a comprehensive bond purchase programme of the European Central Bank (ECB) and the reduction of the depositary interest rate for commercial banks to -0.3% were remarkable measures. The interest level is to be kept low in order for the excessively low inflation rate to rise towards the inflation target of the central bank of slightly below 2%.
- The rising influx of refugees had no immediate effect on the markets, but was challenging on various levels: among other issues, fringe political parties soared in popularity, which might threaten the very existence of the EU.
- Lastly: the economic recovery in the Eurozone continued.

The USA is ahead on the economic cycle

In the USA the recovery from the Great Recession in 2008 and 2009 had progressed to a stage where the US central bank raised the Fed funds rate by 0.25% percentage points to a new range between 0.25% and 0.50% in December. Since rate hikes in the USA come with global repercussions and the downside risks have increased for the global economy, the markets were nervous towards the end of the year.

The year ahead will be challenging

The year ahead will be challenging due to the framework conditions in place. The way to deal with this situation is for the investor to allocate funds into a broadly diversified portfolio of government bonds, corporate bonds, emerging markets bonds, and equities.

The EAM-Communications-Team wishes you all the best for 2016 as well as lots of success with your investments!

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Paul Severin has worked at Erste Asset Management since April 2008. Until 2012 he was responsible for the company’s product management; he has directed communications and PR activities since April 2012. From 1992 to 2008, he was director of equity fund management and deputy director for institutional funds at Pioneer Investments Austria in Vienna.

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