



Investment Strategy

Economy and Financial Markets
November 2018

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Title Picture

Vaduz, Räfis, Sevelen, Fulfirst, Alvier, Gauschla, Gonzen and the Pizol area in the background
Photo: Ursula Gebendinger, Luftbildost, St.Gallen

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Editorial deadline

October 23, 2018

Release

Monthly

Editorial

The US and Turkey have one thing in common

Dear Investor,



Both Turkey and the US are members of NATO. In other respects the two countries differ considerably, particularly when it comes to their economies. The US economy is booming, whereas Turkey is sliding inexorably into deep recession. But they have one thing in common nonetheless on the economic front: Both presidents are opposed to the interest rate policies of their central banks and are pressuring them to refrain from pushing through necessary interest rate rises.

The collapse of the Turkish lira since the start of the year has resulted in a huge rise in the prices of imported goods in Turkey, particularly crude oil. As a result, inflation has risen to a heady 24%. In order to strengthen confidence in its own currency and combat inflation, Turkey's central bank must raise interest rates. But this is something that President Erdogan cannot accept. And with his intransigent stance he has publicly called the central bank's independence into question. As a result, the financial markets have completely lost their confidence in the Turkish currency. The lira has fallen off a cliff, and the economic crisis gripping Turkey is looking grimmer with each week that passes.

Over in the US, President Trump has likewise openly attacked the Fed and its interest rate policy. He fears that higher interest rates will undermine equity markets and act as a brake on economic growth. The argument that the Fed must pursue a more restrictive monetary policy in order to prevent the economy from overheating and an uncontrolled rise in inflation leaves him cold. So far, the financial markets have taken the view that the Fed will assert its indepen-

dence and not let itself be swayed from its chosen monetary policy course. Accordingly, neither the dollar nor capital market interest rates have reacted to President Trump's barbs.

But if Trump continues with these attacks, the Fed's bastion will start to look less impregnable. Certain voices on Capitol Hill and the conservative media will ally themselves to the president's onslaught, sending salvo after salvo against Fed Chair Jerome Powell. And at some point the financial markets will entertain doubts over the Fed's willingness to take the necessary monetary policy steps. At this stage the Turkish scenario will manifest itself in the US too, albeit in a much more diluted form.

Such a scenario could unfold as follows: The dollar loses value as the confidence of investors in US monetary policy wanes. While this may help the US economy, it also increases inflationary pressures. As investors no longer trust the Fed to control inflation, inflationary expectations rise. Higher inflationary expectations have the effect of pushing up longer-term capital market interest rates. As a result, the US experiences higher mortgage rates, higher interest rates for consumer loans, and higher company refinancing costs. And the corollary of all this is a weakening of the economy. Leading ultimately to precisely the outcome that Donald Trump actually wants to prevent with his attacks on the Fed.

A handwritten signature in dark ink, appearing to read 'T. Stucki', written in a cursive style.

Dr. Thomas Stucki
Chief Investment Officer

Economy

Do US politics pose a threat to the booming US economy?

The US economy is performing extremely well. US consumers are looking forward to the holiday season and spending at a level not seen for years. It is almost tempting to dismiss the trade dispute, the impending mid-term elections, and the increasingly heated debate over Trump's presidency as irrelevant factors, incapable of clouding the rosy picture.

The surveys conducted by the Institute for Supply Management, which are a key indicator of US purchasing manager activity, paint a clear picture. The US economy is chugging along at full steam, with growth set to accelerate further over the next few months. Although the Fed is increasingly tightening the interest rate screw, a key lubricant of the current economic boom – namely cheap money – remains very much in place. The labour market is likewise sending out positive signals. At 3.7%, the unemployment rate is at its lowest since the 1970s. Companies are increasingly finding it difficult to source the employees they require. Indeed, some smaller companies have even called a halt to their growth plans, as they simply lack the qualified staff to expand. The US domestic economy appears to be in great shape whichever way you look at it, and prospects are rosy.

Consumers keen to open their wallets

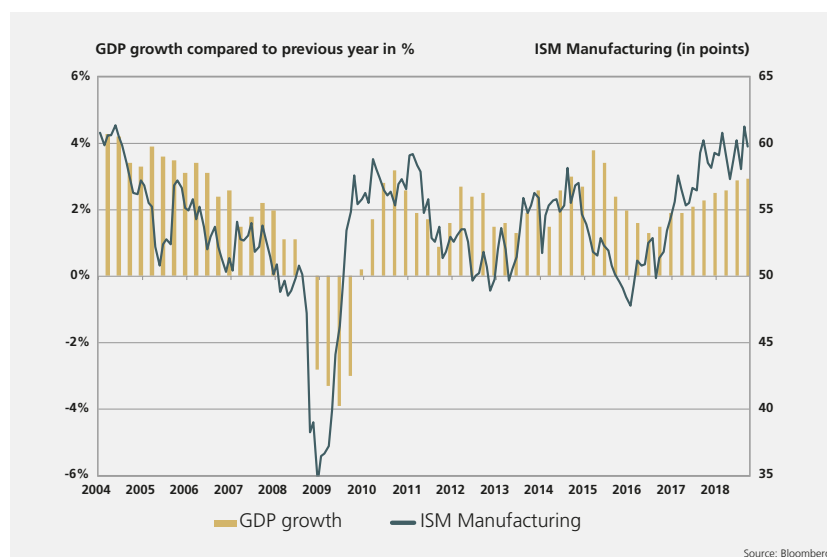
Consumers have good reason to look to the future with optimism, and the most recent survey (Conference Board Consumer Confidence) suggests sentiment is close to the all-time high recorded back in 2000. This is important, particularly as we approach the holiday season that spans the period between Thanksgiving and Christmas. This is the time of year when the cash tills really start ringing, with the average US consumer set to spend around USD 1,000. And when Americans are confident about the future, they are even more willing to open their wallets. The great spending spree in the US traditionally kicks off after Thanksgiving, on the fourth Friday in November. Some stores will be opening at midnight in order to derive the maximum possible benefit from the spending glut. The spending mood can be expected to be particularly exuberant this year, with the corresponding positive repercussions for GDP growth. This in turn

will have a positive impact on sentiment, as retailers will be all the merrier.

Will political developments weaken economic growth?

But while the US economy is truly radiating self-confidence, a storm is increasingly brewing at the political level. The mid-term elections are looming ever larger. These involve every seat in the House of Representatives (the larger chamber) as well as a third of the seats in the Senate (the smaller chamber) being up for grabs, and there are indications that a shift in power will take place, at least in the House of Representatives. This is not an unusual historical pattern, given that mid-term elections often have the effect of galvanizing protest voters who are unhappy with the policies of the incumbent president. Major shifts of power at this point are anything but uncommon, and often have the effect of clipping the President's wings due to the resulting minority government. Furthermore,

USA: Economic optimism persisting



the popular ratings of President Trump have fallen sharply recently. The chances of the Democrats seizing control of at least the House of Representatives are high. This would have the effect of leading the US into a state of political impasse, with no party – including the President – having the leverage to achieve a great deal on the political front. But what repercussions would such a scenario have for the economy and the markets?

US economy unruffled

In the longer term, economic development is dependent above all on political developments. But in the short term, even a shift in political power would do nothing to change the healthy economic situation. Indeed, the opposite is true – a political stalemate would have the advantage of maintaining the status quo, which would provide companies with the corresponding planning certainty. But with one important caveat: Donald Trump would continue to enjoy a rela-

tively free hand in the area of trade and foreign policy, which could result in turbulence every so often. Strengthened by their majority, the Democrats in the House of Representatives will try to push through an impeachment motion. But even if this comes to pass, the green light would still be required from the Senate, which as the highest political body would have the definitive say over the President's right to remain in office. And it is unlikely that the Democrats will achieve the upper hand on this side of Capitol Hill, let alone the necessary two-thirds majority to push through such a bill. The negative reaction of the financial markets to such a political development would probably only be short-term in nature. Because even in the (currently unlikely) event of the President being impeached, economic policy would not be turned on its head. Quite the opposite – a certain degree of calm would probably be restored, at least after an initial phase of unrest. However, all of this is hypothesis for now. In summary, the impending US mid-term elections are likely to prove a storm in a teacup. The US economy will shrug off developments in Washington.

Conflict with China more critical

A more important factor for the economy is America's trade and foreign policy, and here too the mid-term elections are likely to have a negligible impact. In particular, the intensification of the conflict with China is gradually acquiring a worrying momentum. Moreover, the field of battle now appears to encompass much more than just the conflict over trade. Further tariffs are likely to enter into force in January. From this point onwards, tariffs of 25% will be slapped on Chinese exports with a value of USD 200 bn. These tariffs will feed through negatively into growth figures. As it has now become clear which products will be subject to tariffs, companies will have to take this into account in their guidances and make adjustments to sales and earnings estimates. Although this will not trigger a recession, it will come at a cost of some economic growth, and weigh on expectations accordingly. For the time being, however, the US is predicted to continue to bask in bright sunshine – and so the US consumer will continue to come out to play.

US labour market bolsters confidence



Interest rates and yields

Italy poses challenge to capital markets

In the middle of October, the Italian government sent its latest draft budget to the EU Commission. This envisages a budget deficit of 2.4% of gross domestic product for next year. This has unsettled capital market sentiment and triggered a sharp rise in the risk premium on Italian government bonds.

Italy voted in a new government back in the spring. The two new ruling parties, «MoVimento 5 Stelle» (5 Star Movement) and «Lega» (League), concluded a coalition agreement entitled «Contract for a Government of Change». Among other things, this envisages a minimum income for the unemployed as well as lower taxes. The Italian government is now looking to make good on these promises to the electorate. The problem? The money is not there.

Higher budget deficit agreed

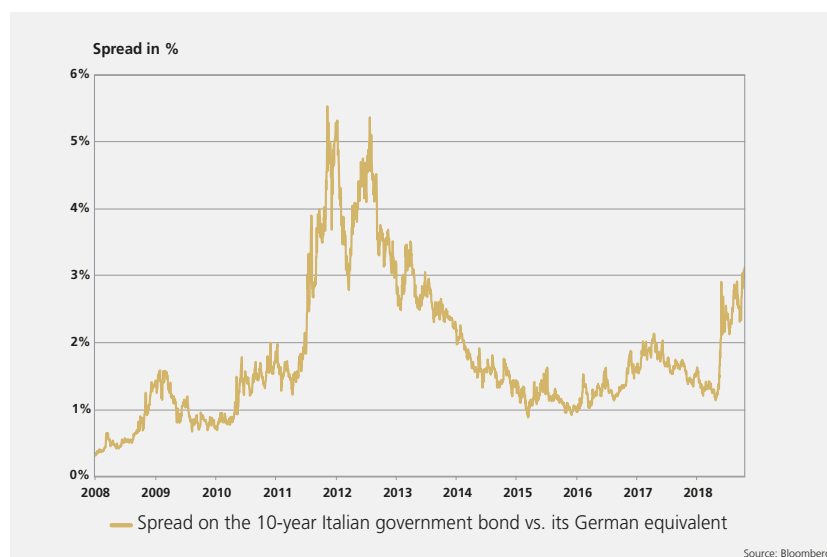
The Italian government has therefore revised its budget for 2019 in recent weeks. In addition to various spending cuts and an expected increase in tax receipts, the Italians have budgeted an increase in the annual deficit to 2.4% of GDP. Although on the one hand this would see Italy remain below the threshold of 3% set out in the EU Stability and Growth Pact, the government deficit budgeted for next year is significantly higher than the figure of 0.8% indicated to the European Union by the previous Italian government. What's more, it also clashes with the recommendations agreed by EU member states only this summer for government budget targets in 2019. According to these recommendations, which are likewise based on the EU Stability Pact, Italy should be reducing its structural deficit (the proportion of the budget deficit not attributable to fluctuations in the economic cycle) by 0.6% next year. By contrast, the recently submitted budget draft would actually entail a rise of 0.8%.

EU requests revised budgetary plan

The European Commission has identified in the draft budgetary plan submitted by Italy for 2019 a particularly serious non-compliance issue with the fiscal recommendation addressed to Italy by the Council. In line with the relevant rules, the Commission has adopted an opinion that re-

quests Italy to submit a revised draft budgetary plan within three weeks. The capital market is sceptical, however. The spread on the 10-year Italian government bond – or the gap between this and its German equivalent – has widened from 1.5% to more than 3% since the start of the year. Although we are still some way removed from the peak levels seen during the European debt crisis, things are gradually becoming uncomfortable for Italy. Although the heads of Italy's ruling parties may still be professing optimism, convinced that spreads will not reach the 4% mark, betting against the financial markets has always been a dangerous game. As an additional factor, the rating agencies are yet to have their definitive say. But they are threatening in no uncertain terms to downgrade Italy's credit rating into non-investment-grade territory in the event of Italy insisting on a budget deficit of 2.4%. The 4% mark could well be breached at that point – if not before. ■

Capital markets take sceptical view of Italy



Equity markets

Energy sector enjoying a boost

After a prolonged period of difficulty, the oil and gas industry appears to be on a recovery trajectory. Many oil multinationals are reaping the benefits of the current oil price environment and passing on surplus cash to shareholders in the form of dividends. Oil service providers who have yet to benefit from the recovery offer catch-up potential.

After a number of difficult years, the energy sector is once again on an upward trajectory. Several years of low oil prices and declining earnings, combined with inflexible cost structures, have forced oil multinationals such as Shell, Chevron and Total to initiate cost-cutting programs and curtail investment. As a result of these efficiency measures, many of the major oil groups now have a much leaner and focused set-up, and are benefiting disproportionately from the current recovery in the oil price. Dividend payments, which were previously being paid from corporate coffers or from the issuance of debt securities or new shares, can now be financed with operating cash flow thanks to higher oil prices.

Moreover, in view of their increasing cash surpluses, many multinationals have announced large-scale share buyback programs. For example, Royal Dutch Shell is planning to buy back its own shares to a value of USD 25 billion by 2020.

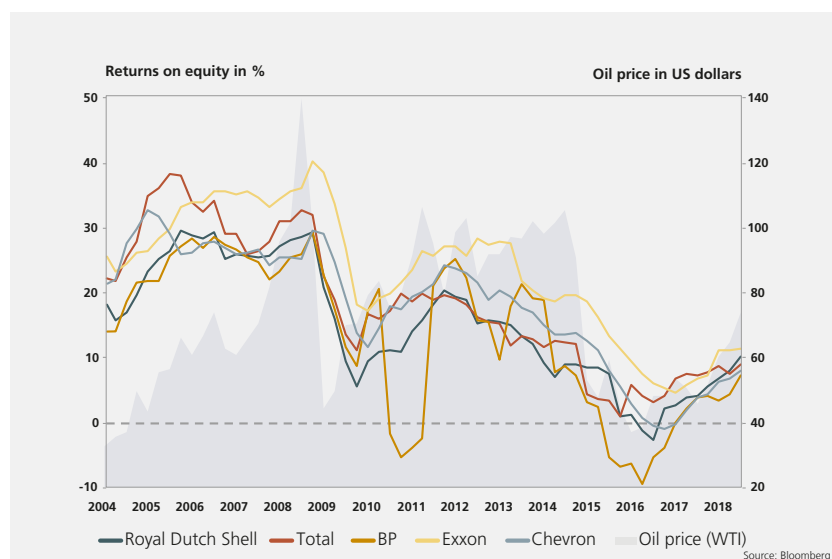
All signposts pointing to growth

Where production volumes are concerned too, all the signposts point to a period of growth for the major oil groups. The significant investments made in the period prior to the oil price slump are now starting to pay off, as the lead times of oil and gas projects are often between 5 and 10 years, and many of the initiated projects are only coming on stream now. For example, BP, Chevron and Total are all anticipating annual production growth of 3-5% by 2020 as a result of various major projects, a figure that is significantly above the average of the last few years. We are also anticipating the price of crude oil to continue to develop positively, despite the significant recovery we have already seen. The demand side is benefiting from the robust economic outlook and persistent hunger for commodities in the emerging markets. On the supply side, US sanctions against key oil producer Iran and declining production in Venezuela are both providing support in the short term.

Improved outlook

Following the price gains of recent months, however, the improved outlook is now also reflected in higher valuations. An interesting player in this context is Royal Dutch Shell. The high dividend yield and the ongoing share buyback program of this British-Dutch oil multinational really catch the eye. Moreover, the company has an excellent positioning with its globally diversified liquid gas company, and has exploited the available synergies that arose through the takeover of BG Group. Schlumberger, the world's largest oil service provider, is also worth a second glance. Due to the subdued investment climate and excess capacity among equipment suppliers, Schlumberger has yet to benefit from the rise in oil prices. However, we are expecting a gradual improvement in the investment climate over the next few quarters, which should have a positive impact on earnings development and therefore also the stock price.

Returns on equity for oil multinationals once again heading north



Currencies

Euro has become more stable

The clouds are darkening over the Eurozone. But so far, neither the budget clash between the EU Commission and Italy, nor the increasing risk of a no-deal Brexit, have done much to erode the value of the euro, including against the franc.

The euro depreciated dramatically against the franc during the euro crisis between 2010 and 2012, with EUR/CHF plummeting from 1.50 to 1.04 between 2010 and September 2011, when the Swiss National Bank applied the emergency brake by setting a minimum exchange rate for this currency pair of 1.20. At the same time, the yields on the sovereign bonds of the debt-laden nations of the Eurozone rose dramatically during this period: By the end of 2011, Italy was having to pay more than 7% for 10-year funding.

Things set to get tough for Italy

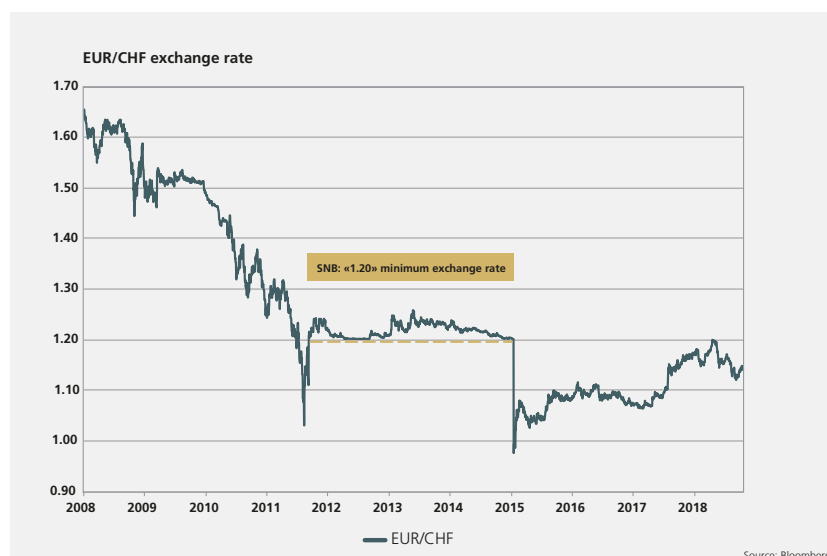
The dispute between the Italian government and the EU over Italy's draft budget for 2019 was not difficult to foresee. The Italians want to deliver on their rosy promises to voters – such as a basic income for the unemployed and a lower retirement age. But as the funding for such initiatives is simply not in place, the Italians are now planning on a budget deficit of 2.4% of GDP next year, rather than the original 0.8% promised to the EU. In a first reaction, the European Commission has requested changes in Italy's Budget. To maintain its credibility in the area of financial stability, the EU would need to reject this budget proposal. If it backs down, it will open the floodgates for other debt transgressors. The heads of Italy's coalition parties are convinced that they can implement their program. But the financial markets take a different view. The spread (i.e. risk premium) on Italian bonds compared to German bonds widened from 1.5% to more than 3% between May and October of this year. The ratings agencies are now threatening to downgrade Italy's credit rating. This would have the effect of increasing the risk premium on Italian bonds even further. In October, Moody's downgraded Italian government bonds to the very lowest «investment grade» tier. The loss of investment grade status would have serious consequences, as many investors would then be forced to sell their holdings of Italian government bonds. As a com-

pounding factor, the ECB would then no longer be able to buy Italian bonds itself.

Euro in no danger of being dragged down

In contrast to its performance during the euro crisis, EUR has so far remained fairly stable against CHF. The financial problems of one Eurozone country are no longer being viewed as a sign of the euro's imminent demise as a shared currency. The surge in Italian yields is not having an automatic knock-on effect on other sovereign bonds like those of Spain or Portugal, as was the case during the Euro crisis. If the conflict between the Italian government and the EU were to intensify, that would clearly be a negative for the euro. But it would not trigger a collapse in EUR/CHF toward parity. ■

EUR more stable now than during Euro crisis



Commodities

Gold benefits from market turbulence

The stock market correction at the start of October heralded an end to the weak performance of gold over the previous six months. In recent months, gold appeared to have lost its lustre as a secure investment.

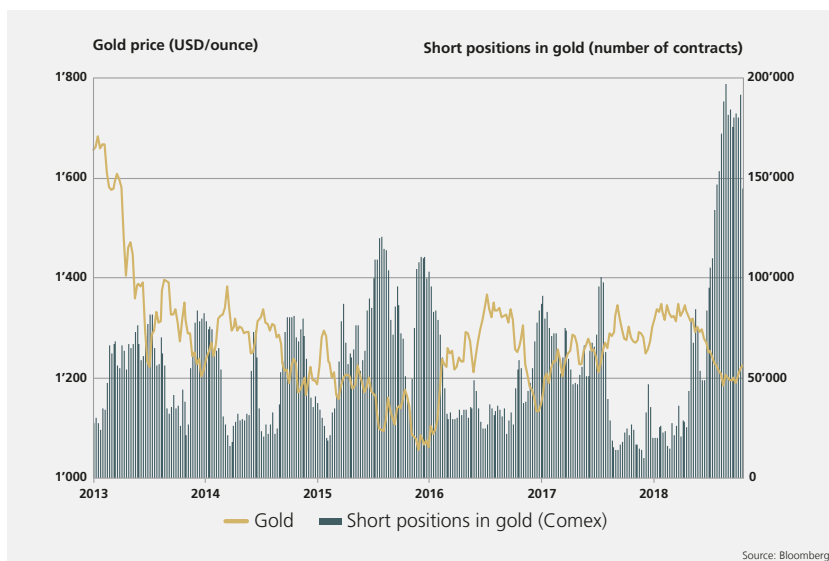
It failed to appreciate either during the Turkey crisis or against the backdrop of potential escalation of the trade war between the US and China. Quite the reverse: It closed lower at the end of September for the sixth month in succession. Nor has it just been the dollar that has weighed on gold. The market for this precious metal has also suffered from weak investor demand, with switching apparent into the booming US stock markets in particular. The picture has changed in recent weeks, however. The latest bout of turbu-

lence in equity markets has triggered a dramatic rise in interest in gold. This much is apparent from the development of listed gold funds. The holdings of these funds, which touched an annual low as recently as the first week of October, are now on the rise and recording inflows. By contrast, pessimism over the prospects for this commodity is still very evident among speculative investors in the futures market. As at October 9, the number of short positions in gold stood at a record high. In the past, a one-sided market positioning of this kind has been a solid indicator of impending counter-movements. Indeed, the latest recovery in the gold price (by some 4%) is likely to have been a painful development for several market players. If short positions were now to be closed out, the gold price would gain an additional short-term stimulus.

Central banks: continuation of a trend

It is worth taking another look at central bank gold reserves. In addition to the jewellery industry and investor demand, central banks are among the key players in the gold market. In the first half of 2018, they were responsible for 10% of all gold demand. Although the gold holdings of central banks were on a permanent downward trajectory up to 2008, they have since picked up when viewed in overall terms. The gold holdings of the central banks of industrialized nations have remained relatively constant, which means the increase is solely attributable to the emerging markets. The most active buyers here have been China, Russia, and Turkey. According to the data of the World Gold Council, the central bank holdings of these three countries increased by 307% (China), 408% (Russia) and 486% (Turkey) between 2007 and 2017. In a sense this is hardly surprising, as the industrialized nations have historically always sat on the largest gold reserves. This is true not just in absolute terms, but also in relation to currency reserves. Whereas gold accounts for 73.5% of currency reserves in the US, for example, the equivalent figure for Russia is currently just 16.8%. By comparison, the corresponding figures for China (2.2%) and Turkey (10.8%) are still very low. Gold therefore remains potentially important to central banks from the emerging markets on diversification grounds.

Many short positions in gold have been built up recently



Investment Strategy

Is the bear about to emerge from its cave?

After a strong September, equity markets somewhat embarked on a downward trajectory in October. At the same time, bond market yields have risen and geopolitical risks have left their own mark on market developments.

The list of potential risks to equity markets is a long one. In Europe, there was still no Brexit agreement in sight by mid-October, while Italy's budget proposal harboured any amount of potential for conflict. Where the trade/tariff dispute is concerned, neither the US nor China appear to be blinking so far. Quite the opposite – the conflict between the world's two economic heavyweights has essentially intensified, and an agreement appears to be out of reach. Along with China, the other emerging markets likewise do not stand out as beacons of hope. Inflation has spiralled out of control in Turkey, while South American nations such as Brazil and Argentina are hardly making the headlines with positive newsflow. The financial markets are currently overshadowed by a number of political risks which have the potential to put equities markets under further pressure and send daily volatility soaring.

Rise in interest rates unsettles, economy reassures

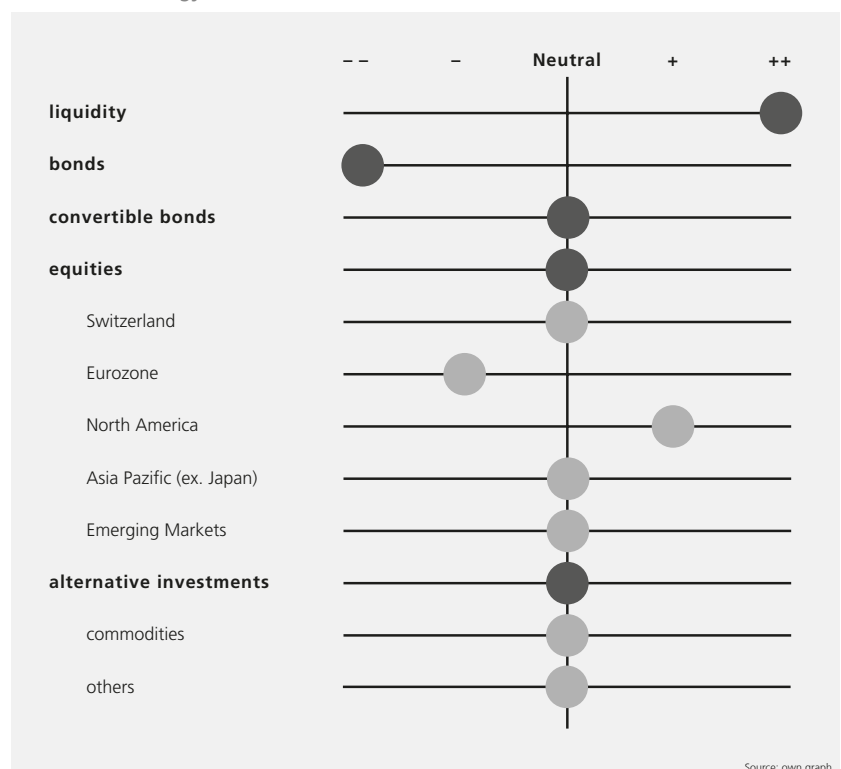
Alongside these geopolitical flashpoints, the interest rate market has also sprung into life over the last few weeks. In mid-October, the yield on the 10-year US Treasury, which has been stuck below the magic 3% mark for so long, finally pushed through this barrier. This rise in capital market interest rates was driven above all by the prospect of further rate hikes on the part of the US central bank (Fed). Fed Chairman Jerome Powell made it clear that the US economy was not only perfectly capable of absorbing further rate rises, it actually needed them. Powell is keen to prevent the currently thriving US economy from overheating through more restrictive monetary policy. A more restrictive stance on the part of the Fed makes complete sense, and is appropriate to the economic situation. For equity markets such a stance has two implications: Firstly, the US economy is in exceptionally good health. The domestic economy is booming, and the strong earnings figures being released by US

banks indicate that other US companies too will deliver convincing results thanks to the favourable economic situation. This will provide equity markets with downside support. Secondly, however, more restrictive monetary policy in the US will gradually remove some of the liquidity enjoyed by the financial markets, and with time this will act as a cap on upside equity market potential.

No bear market, but high volatility

The outlook for earnings and economic growth is positive for equities. On the other hand, the numerous risks swirling around will unsettle investors and trigger sharp upward and downward fluctuations in share prices. As the positive fundamental data and the potential crisis flashpoints appear to be more or less balanced, we expect this equilibrium to hold true for equities too. In view of the positive outlook for US earnings and economic growth, we are maintaining our overweight stance in US equities. ■

Investment Strategy

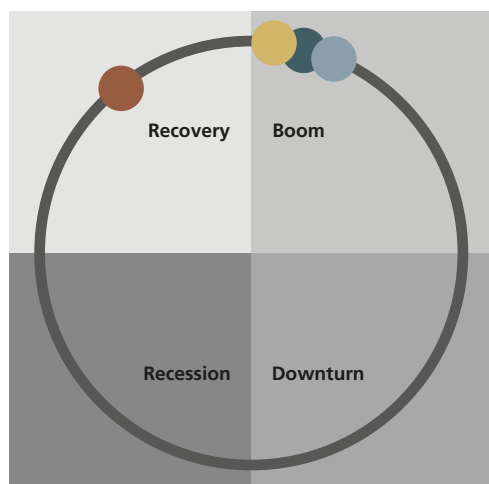


Market overview

Economic data and cycles

Data as of 23 October 2018; Source: Bloomberg, Graphics: own illustration

Economic trend in industrialized countries



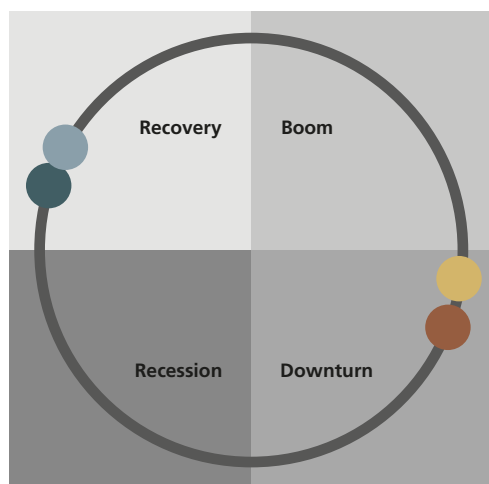
● Switzerland ● USA
● Eurozone ● Germany

	GDP yoy, previous quarter	GDP yoy, current	Assessment	Inflation rate yoy, previous quarter	Inflation rate yoy, current	Assessment	Unemployment rate, previous quarter	Unemployment rate, current	Assessment	PMI, previous quarter	PMI, current	Assessment
Switzerland	3.2 %	3.2 %	positive assessment	1.1 %	1.0 %	neutral assessment	2.6 %	2.5 %	positive assessment	61.6	59.7	positive assessment
USA	2.6 %	2.9 %	positive assessment	2.9 %	2.3 %	positive assessment	4.0 %	3.7 %	positive assessment	60.2	59.8	positive assessment
Eurozone	2.4 %	2.2 %	positive assessment	2.0 %	2.1 %	positive assessment	8.2 %	8.1 %	positive assessment	55.1	52.1	neutral assessment
Germany	2.1 %	2.0 %	positive assessment	2.1 %	2.3 %	positive assessment	5.2 %	5.1 %	positive assessment	56.9	52.3	neutral assessment

■ positive assessment ■ neutral assessment ■ negative assessment

- **Switzerland:** The outlook for the Swiss economy remains good. The strong franc will eat into company earnings to a certain extent, however.
- **USA:** The US economy is in good shape. Leading indicators are at very high levels, pointing to further expansion.
- **Eurozone:** Economic growth is solid, but the phase of expansion is losing momentum. Growth is weakening.
- **Germany:** The outlook remains positive. Companies are optimistic about the future. Momentum is waning, however.

Economic trend in emerging markets



● China ● India
● Brazil ● Russia

	GDP yoy, previous quarter	GDP yoy, current	Assessment	Inflation rate yoy, previous quarter	Inflation rate yoy, current	Assessment	Unemployment rate, previous quarter	Unemployment rate, current	Assessment	PMI, previous month	PMI, current	Assessment
China	6.7 %	6.5 %	neutral assessment	1.9 %	2.5 %	positive assessment	3.9 %	3.8 %	neutral assessment	50.6	50.0	neutral assessment
India	7.6 %	8.0 %	positive assessment	4.9 %	3.8 %	neutral assessment	–	–	–	51.7	52.2	positive assessment
Brazil	1.2 %	1.0 %	neutral assessment	4.4 %	4.5 %	neutral assessment	7.5 %	8.2 %	negative assessment	51.1	50.9	neutral assessment
Russia	1.3 %	1.9 %	neutral assessment	2.3 %	3.4 %	neutral assessment	4.7 %	4.5 %	positive assessment	52.1	53.5	positive assessment

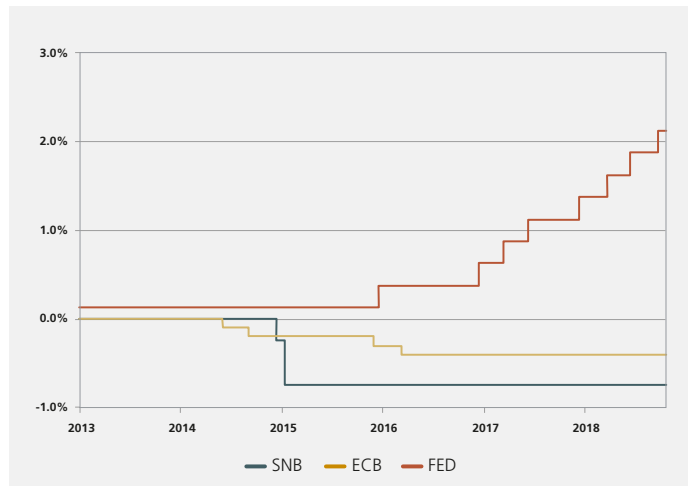
■ positive assessment ■ neutral assessment ■ negative assessment

- **China:** China has loosened its monetary policy significantly with a view to countering the current growth weakness. Any escalation of the trade dispute would prove an additional drag.
- **India:** India's economic development remains promising. The central bank has raised interest rates to stabilize the currency, which will weigh on the economy.
- **Brazil:** The recovery phase is still struggling to establish itself. But confidence is back thanks to new «law and order» President Bolsonaro.
- **Russia:** Russia is benefiting from the rise in oil prices. The outlook is slightly positive, but not euphoric.

Interest rates and currencies

Data as of 23 October 2018; Source: Bloomberg, Graphics: own illustration

Key interest rates for selected central banks

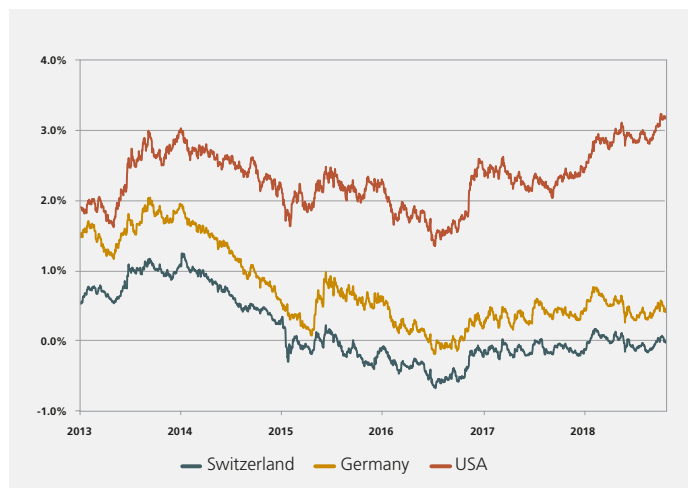


Switzerland: The SNB will continue to align its monetary policy with that of the ECB. It is therefore waiting for the ECB to make its first interest rate move and will raise its key interest rate in September 2019.

Eurozone: The ECB will end its bond-buying programme in December 2018. Key interest rates will remain low even after the end of the bond purchase programme. We expect the ECB's first rate hike to come in September 2019.

USA: Positive economic data, particularly on the domestic economy, will be conducive to further rate hikes. The Fed will therefore continue to raise its key rate gradually. We expect one more interest rate hike in 2018.

Capital markets: yields on individual 10-year government bonds

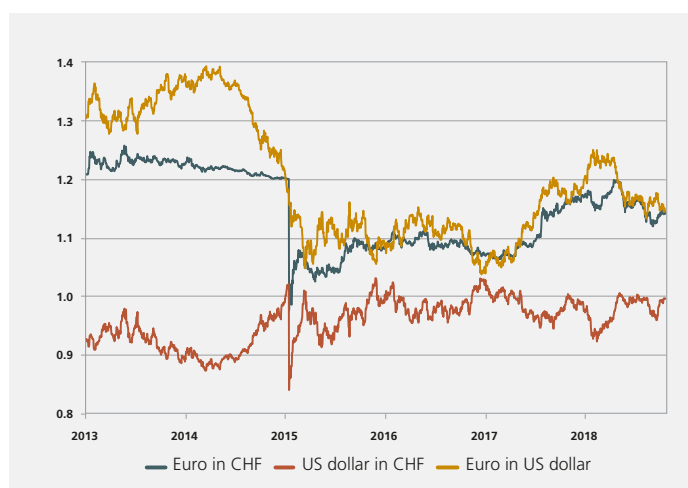


Switzerland: Negative interest rates, low inflation and demand for bonds continue to keep interest rates low. However, attention will increasingly focus on the first SNB key rate increase next year. Capital market interest rates will rise further in the run-up to this first hike in key rates.

Eurozone: The economic outlook is positive, though slightly weaker. An initial ECB interest rate hike is on the cards for the end of summer 2019. The debate over the ECB's first rate increase should bring higher interest rates by mid-2019.

USA: The economic outlook is positive. Further interest rate rises will follow on a quarterly basis. We continue to expect an up-trend in yields due to the rate-hiking cycle and rising inflation.

Currencies: rates for selected currency pairs



EUR/USD: The interest rate advantage is supporting the dollar. However, America's twin deficits and the latent trade conflict remain potential negative factors for the greenback.

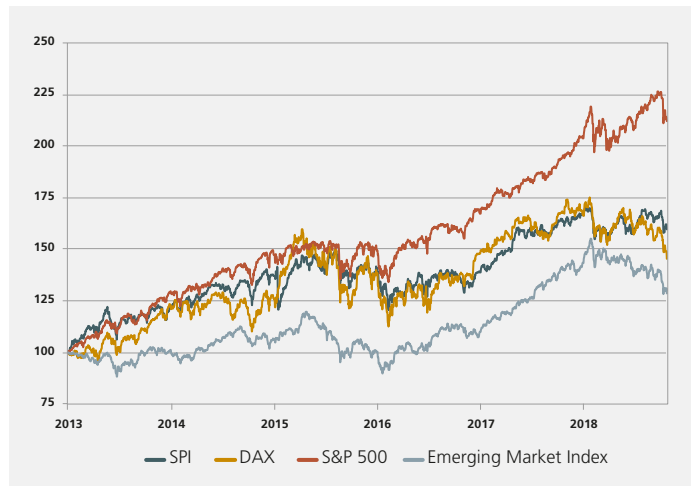
USD/CHF: Further US interest rate hikes favour USD. By contrast, political wrangling is resulting in uncertainty and giving rise to doubts over the development of the US economy.

EUR/CHF: The franc is a good indicator of confidence in the eurozone. The euro remains susceptible to negative reactions from the financial markets in the event of political uncertainty.

Equity and commodity markets

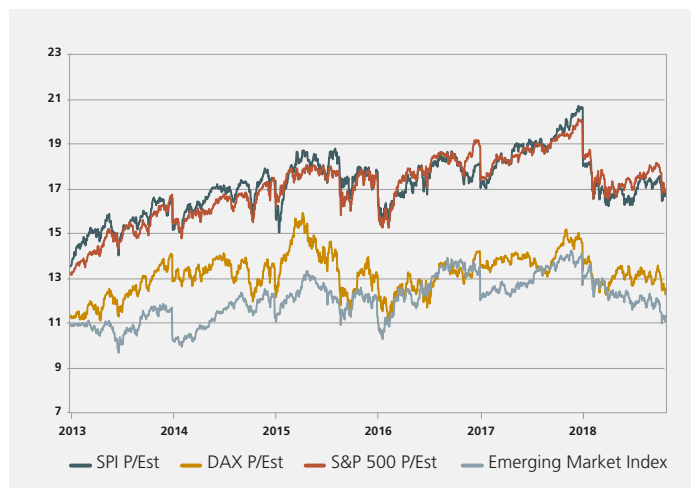
Data as of 23 October 2018; Source: Bloomberg, Graphics: own illustration

Equity markets for selected regions (indexed)



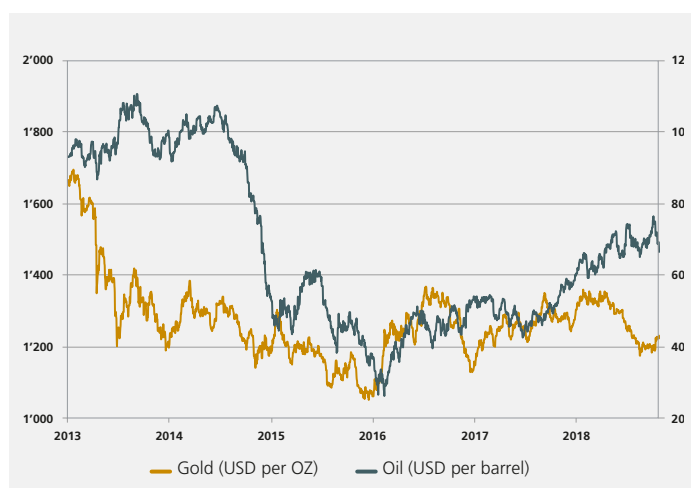
The current market situation is volatile. Rising capital market interest rates, the Italian budget dispute, the US trade dispute with China, and Brexit discussions are leading to **growth fears**. The **outlook** for the current **earnings season** remains positive for now and is supporting equity prices.

Valuations: estimated P/E ratio for selected regions and markets



Valuations have declined as a result of recent stock market falls. All markets continue to exhibit positive estimated **earnings growth**. In the US, estimated earnings growth continues to gain momentum. In the Eurozone and Switzerland it has levelled off, however.

Commodity markets: Price trend for oil and gold



Oil price: The new US sanctions against Iran have triggered a rise in prices. While global demand and falling inventories are improving the outlook for the oil market, record high US oil production is preventing a substantial price increase.

Gold price: Gold has had a difficult time this year, with its status as a «safe haven» no longer the focus of investor attention. Instead, the gold price has been taking its cue from the US dollar in recent months.

Financial markets and forecasts

Closing prices as of 23 October 2018; Source: Bloomberg; Forecast: SGK B

Key interest rates	12 Months ago	3 Months ago	Current	Forecast 3 Months	Forecast 12 Months
SNB	-0.75 %	-0.75 %	-0.75 %	-0.75 %	-0.50 %
ECB	-0.40 %	-0.40 %	-0.40 %	-0.40 %	-0.20 %
FED	1.00 % – 1.25 %	1.75 % – 2.00 %	2.00 % – 2.25 %	2.25 % – 2.50 %	3.00 % – 3.25 %

Capital market yields	12 Months ago	3 Months ago	Current	Forecast band 3 Months	Forecast band 12 Months
10-year Conf.	-0.01 %	-0.03 %	0.00 %	0.05 % – 0.25 %	0.50 % – 0.70 %
10-year German Bund	0.48 %	0.40 %	0.41 %	0.55 % – 0.75 %	1.00 % – 1.20 %
10-year Treasury	2.42 %	2.95 %	3.17 %	3.10 % – 3.40 %	3.50 % – 3.80 %

Currencies	12 Months ago	3 Months ago	Current	Forecast band 3 Months	Forecast band 12 Months
EUR/CHF	1.1656	1.1613	1.1412	1.10 – 1.15	1.08 – 1.13
USD/CHF	0.9911	0.9936	0.9949	0.95 – 1.00	0.95 – 1.00
EUR/USD	1.1761	1.1687	1.1471	1.13 – 1.18	1.11 – 1.16

Commodities	12 Months ago	3 Months ago	Current	Forecast band 3 Months	Forecast band 12 Months
Oil (WTI, USD per barrel)	52	69	66	70 – 80	70 – 80
Gold (USD per oz)	1277	1225	1230	1200 – 1300	1250 – 1350

Equity markets	YTD	Valuation (est. P/E)	Current Index	Trend last 3 Months	Forecast 3 Months
S&P500 (local currency)	4.1 %	16.8	2741	↘	→
EuroStoxx50 (local currency)	-6.4 %	13.2	3141	↘	↘
SMI (local currency)	-2.7 %	15.5	8767	↘	→

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