Investors' Outlook

Let's self-isolate and pin our hopes on summer

April 2020

Asset Management

Let’s self-isolate and pin our hopes on summer

Dear readers,

During sporadic outbreaks of the bird flu, we used to shoo our feathered friends indoors. Now it seems the chickens have come home to roost – this time around, it’s us who are confined to narrow quarters. We have turned into an army of ghost workers trying to keep the demons at bay. Some of us will appreciate the additional time with their families, others will miss their colleagues – but all of us face the possibility of human suffering and economic hardship.

Scenario changed to “sharp slowdown”
While our red-hot telecommunication lines still connect us to the outside world and grant access to analyzing tools, let’s recap what happened in the past few weeks. The quick-fire spread of the new coronavirus took us by surprise, upending our moderately optimistic growth scenario for 2020 supported by favorable data until very recently (see the ***March edition of the Investors’ Outlook***). Particularly worrying to us was the unprecedented and almost simultaneous collapse of global supply and demand. Our central scenario for 2020 has changed to a “sharp slowdown”, and we now expect the economy to shrink in most countries (see chart 1). The best we can wish for is a massive yet temporary shock. All other possible developments seem even more dismal.

To put this pandemic and its possible consequences into perspective, we need to take a bird’s eye view covering the 2008-2009 aftermath of the collapse of US investment bank Lehman Brothers, the “Black Monday” event of 1987, and the Great Depression in the 1930s. These three examples stand for the basic categories the health crisis could fall into: an event-driven shock, a cyclical downturn, and a structural breakdown, listed in the order of severity. Technical analysts would point out that the sell-off during the past few weeks mirrors the fall on stock markets during the initial phase of the three examples mentioned above. In theory, each of the three scenarios could come to pass.

Event-driven shock already happening
An event-driven shock is a clearly identifiable incident – the current pandemic, a war, a natural disaster, or a multiple-day power cut – resulting in a market rout, usually followed by a flight to quality. For instance, investors transferred funds into safe havens after the “Black Monday” slump that was triggered not by one, but a series of negative developments. In October 1987, high US trade deficit figures, among others, put pressure on the US dollar as well as stocks, causing a sudden mood swing and eventual panic selling. In such an environment, equities and corporate bonds typically post losses while government bonds, gold, the Swiss franc, and the Japanese yen, gain ground. Event-driven shocks are, for the most part, completely unexpected. For all the harm they can cause, they remain transitory events if governments and central banks respond appropriately.

Will there be a cyclical downturn?
What distinguishes a cyclical crisis from an event-driven one is that the former puts economies and markets under stress for a long time. For instance, the global economy took years to recover after the financial crisis of 2008-2009. A cyclical crisis typically occurs at the peak of an economic cycle, as was the case in the early 2000s, and the financial crisis ten years ago. Whether we are already transitioning from a shock to a cyclical downturn is anybody’s guess. Recent panic selling suggests the more negative outcome, but there have also been notable intraday gains. Were the worse scenario to materialize, the sell-off would continue. In such a case, the outbreak of the new coronavirus would have been the straw that broke the camel’s back, ushering in a period of more than one year of economic woes.

Structural breakdown seems unlikely
The economic doomsday scenario would be something resembling the Great Depression of the 1930s that resulted in mass unemployment and a decade-long bear market. Those catastrophic events were exacerbated by the authorities’ lack of experience and coordination – the

⟶ Input deadline for this edition
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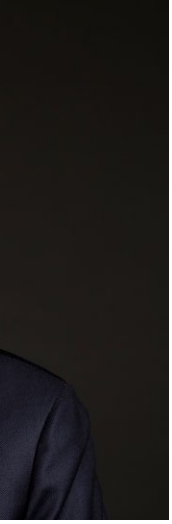


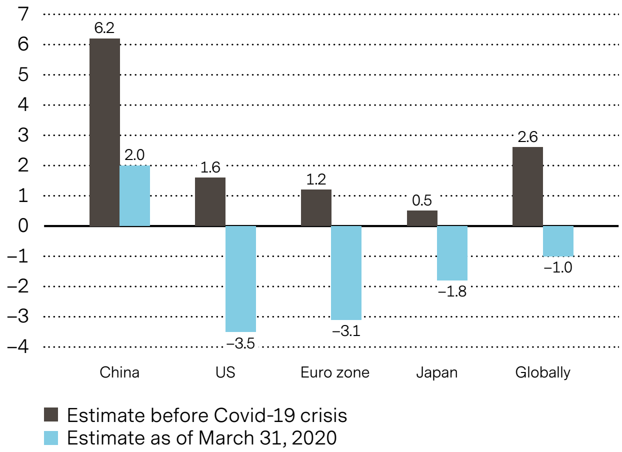
US Federal Reserve, established only a few years previously in 1913, didn't support markets in a way they do today. We currently see no indication of a structural breakdown, partly because decision makers have realized how serious the Covid-19 outbreak is. Hardly a day goes by without some central bank or government announcing huge stimulus packages for their economies (see chart 2). This is the main difference to the 1930s, which will also be remembered for authorities' inaction.

Markets are data and psychology-driven
Before things can start looking up, the rate of new infections with Covid-19 must slow in the coming weeks, especially in Europe and the US. Because corporate bonds will probably need to recover before stocks can rebound, credit spreads and credit default swaps (CDS), a measure for the cost of insuring against a counterparty's default, will be important to watch. Moreover, yields on government bonds issued by southern European countries need to move lower and stay contained. Such data will tell us whether the steps by central banks and governments are effective, and whether markets believe they will ensure sufficient liquidity supply, and keep defaults under control.

Psychology will play an important role: bans and restrictions on our daily lives must be lifted towards summer at the latest, and government-led support needs to be credible enough to reassure the population. After all, who would spend money on anything fancier than food or rent without some confidence of getting paid three months from now? By contrast, a massive increase in defaults and unemployment rates could spook the markets, and concerns over bad loans could infect banks.

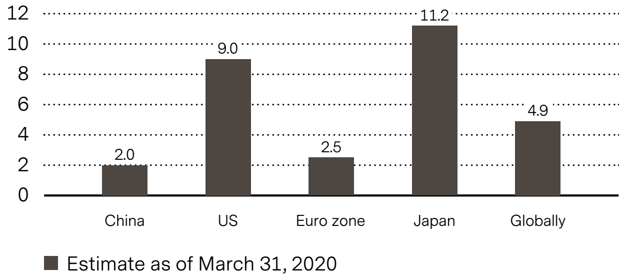
Underweight equities, but take a close look
Earlier in March, we changed our equity positioning to underweight. This unusual stance seemed sensible while traders were hitting the panic button. But given that many shares are now at attractive levels, we have adjusted this negative equity view slightly, going neutral on developed-market stocks but keeping emerging-market ones on underweight. On the fixed income side, we overweight corporate paper versus sovereign bonds. The incoming liquidity flood will reassure companies seeking financing, calming fears of spiraling defaults. This will also benefit the corporate bond market. As we expect the US dollar to weaken over the coming months, and the easy fiscal policies adopted globally to increase governments' debt-to-GDP ratios, we upgrade gold to overweight.

Chart 1: We now expect a global recession, China still seen holding up
Annual rate in %



Source: Vontobel

Chart 2: Japanese government with the highest expenditure to contain Covid-19
In % of GDP



Source: Vontobel

As changes in our investment strategy do not require a physical presence, we will try to keep the doors of our chicken coops tightly shut until further notice. However, we hope to burst into the open in summer as if waking from a bad dream full of black swans and other unwelcome guests.

Stay healthy,

Frank Häusler
Chief Strategist, Vontobel

The virus drags the world into a recessionary tailspin

Economic forecasters are in the habit of taking the long view. This time, they only needed a few days to discard all of their predictions. Meanwhile, investors are rubbing their eyes in amazement as equity prices slump. What began as a supposedly local outbreak of a novel coronavirus in China at the turn of the year has swiftly become a global problem.

There seems to be no doubt that the first half of 2020 will see a sharp economic downturn. What comes next is more interesting. There will be a pronounced recovery in the second half of the year providing that central banks and governments do their part. The economic support packages that have been assembled around the world are a step in the right direction.

Having significantly scaled back the risks in our model portfolios at the start of the crisis, we are cautiously putting out our feelers again. Equities are now only slightly underweighted. We are positive with regard to corporate bonds once again, whereas we are reducing our weighting of sovereign bonds.

	UNDERWEIGHT		NEUTRAL	OVERWEIGHT	
	significantly	slightly		slightly	significantly
1 Liquidity			→		
2 Bonds			→		
3 Equities		↘			
4 Gold				↗	
5 Commodities			→		
6 Alternative strategies			→		

Changes month-on-month:
same, higher, lower

→ ↗ ↘

Reto Cueni, PhD
Senior Economist,
Vontobel Asset Management

Our view of the world and our risk outlook for the next 12 months

A pandemic where the risk of contagion is triggering drastic quarantine measures and making recession inevitable – that is one way economists might sum up the latest developments. While the spread of coronavirus seems to have been halted in China and the economy is slowly getting back on track, economic activity elsewhere looks likely to collapse in the first half of 2020, especially in industrialized countries. We currently expect the restrictions imposed on public life to somewhat contain the pandemic until the middle of the second quarter, after which governments may be able to gradually lift the measures in place around summer time.

Given this, we are anticipating a substantial economic recovery in the second half of the year, provided knock-on effects such as unemployment, bankruptcies and bad loans remain relatively low. We continue to assume this on the basis of the substantial increase in government spending to shore up the economy and the massive support provided by central banks (see Editorial pages 2–3 and Macro Highlights pages 6–7).

The inflation outlook has weakened significantly because of the collapse in demand and the sharp decline in energy prices. Nonetheless, prices should pick up again as soon as the economy begins to recover in the second half of the year. We expect central banks to maintain their exceptionally relaxed monetary policy even if inflation increases.

Our outlook draws heavily on the assumption that economically significant areas of the world will be able to put a halt to the spread of the coronavirus in the spring, that there will not be stricter restrictions imposed and the flow of goods will not be cut off. Should this prove not to be the case, the potential negative repercussions are almost impossible to conceive. On top of this, a sharper tone in the trade dispute between the United States and its trading partners or in the exit negotiations between the UK and Brussels would also be a bad omen.

GROWTH	INFLATION	CENTRAL BANK
We expect a sharp growth contraction in 1H due to the health crisis, and a gradual recovery in 2H.	Core consumer price index below target with demand shock outweighing supply side decline.	The Fed cut rates to zero, will buy trillions USD worth of assets.
Pandemic will hit growth in 1Q and 2Q, recovery expected towards the summer and in the second half.	Will remain muted 1H on lower energy prices and slump in demand that exceeds supply shock.	Central bank stays put on rates but sets massive liquidity programs.
Pronounced virus-linked 1Q/2Q weakness should be followed by mid-year and 2H rebound.	Lower energy/import prices, and virus shock, push CPI outlook below zero for most of 2020.	While not moving on rates, SNB eases lending rules.
Contraction in 1Q now possible. We expect 2% growth in 2020 with China starting to open up for business.	Inflation rate likely to slow amid worsening global economic outlook.	Aggressive monetary and fiscal stimulus measures lined up.
Economic already hit in 4Q 2019 by VAT increase. Virus impact will also dampen 1H activity.	Core inflation expected to stay close to zero in 2020, deflation risks could reemerge.	A recession in 2020 supports calls for more monetary support.

We are continuing to take a neutral position with regard to cash. As we remain confident that the US dollar will weaken in the medium term, we are maintaining our USD/CHF short position.

Government bonds offer little in the way of return potential in the current environment, and we remain underweight here. By contrast, we are overweighting corporate bonds as this segment will be supported by the measures taken by governments and central banks.

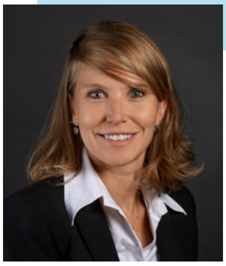
We are slightly increasing our equities weighting while remaining underweight on the whole. We are avoiding emerging markets but increasing our positions in the rest of the world. Investors with a long-term focus are likely to already be spotting attractive investment opportunities here and there.

Gold is newly overweight. With government debt increasing sharply as a result of the economic support measures, attention will be directed to gold as a safe haven. The precious metal is also benefiting from the recent depreciation of the US dollar.

Unlike other asset classes, commodities are seeing very little benefit from the central bank stimulus packages. As long as there is no significant economic recovery and no strong depreciation of the US dollar, we are refraining from overweighting here. This asset class will also feel the impact of the Covid-19 virus in the short term.

In view of heightened political risks at present, alternative strategies can aid diversification. However, taking the higher risk into account, their return is still modest compared to cash investments. Our weighting for alternative strategies is therefore also neutral overall.

Governments protect the people but have to put economies on life support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The crowds have disappeared from public places in Europe as most of the continent has followed Italy's early lockdown. The US is increasingly moving in this direction as well. We have downgraded our growth forecasts, despite measures by governments and central banks around the globe to protect the economy from the fallout of the disease, and mitigate market frictions.

The Covid-19 virus has engulfed the US, which is now registering the largest number of new infections (see chart 1) and is already closing the gap to Europe even in terms of percentage of the population affected. Based on the data of the progression of the coronavirus, authorities around the globe will decide about the duration and severity of the restrictions. Their actions will be pivotal to determine the economic impact of the disease. Therefore, we need to have a baseline view on its further spread to conduct economic forecasts. Relying on medical studies and expert judgement, we decided to work under the assumption that the spread of the disease will probably be contained in most developed countries around the middle of the second quarter 2020. This means that governments would be able to gradually lift the massive restrictions towards the summer, leading to a significant economic recovery in the second half of the year. Asia is already about to take this route, Europe is likely to follow, and North America, where tests and preemptive measures started later, will probably be last.

This led us to revise down our economic forecasts again significantly despite the massive fiscal packages and drastic monetary measures to protect the economy (see charts in the editorial section, page 2–3). Not only do we now expect a very weak first quarter globally, but also a record-low second quarter, which, however, should be followed by a strong growth rebound over the reminder of the year.

Europe bears heavy Covid-19 burden
When Italy went into lockdown, few people in Europe realized that this would be their lot in a matter of days. Private consumption in the euro zone has come to a standstill apart from essentials like food, housing, or heating, which makes up approximately 60% of the total. Most of the "non-essential" part (e.g. furniture, clothes, cars) will be lost during quarantine measures. Only about a third of this may come back later due to pent-up demand. With basically the whole euro zone in quarantine, we had to revise our growth forecasts for the euro zone down to

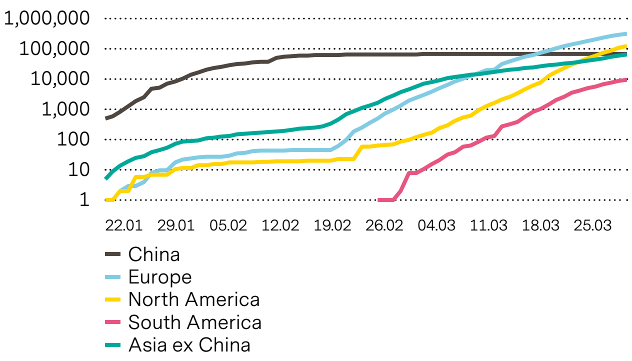
–3.1 % for 2020, even accounting for the plus of around 2.5 percentage points coming from additional fiscal stimulus measures (see chart 2 in the editorial, page 2 – 3), and another estimated 6 percentage-point boost via automatic stabilizers (e.g. short-time work and unemployment benefits. On the monetary side, the European Central Bank's massive emergency package called PEPP will, in combination with previous programs, lead to security purchases worth more than 1 trillion euros. Moreover, the ECB will make available up to 3 trillion euros of liquidity via its refinancing programs.

America readies largest-ever fiscal package
The rapidly worsening Covid-19 situation in America with New York State as one of the hardest hit areas has resulted in an unprecedented sudden stop in economic activity. The number of people registering for US unemployment insurance rocketed to approximately 10 million within two weeks (see chart 2). Given the lack of economic safety nets in the US, Congress and the Trump administration passed a massive fiscal package worth 2 trillion US dollars, or 9.5 % of the country's gross domestic product. It includes direct payments to low-income households, enhanced unemployment insurance and financial support for the most affected industries such as airline companies. An additional support package is currently under discussion. Despite such short-term relief, the US economy is likely to contract strongly in the first half. We expect growth to gradually rebound after the summer only. The US Federal Reserve was an early mover among the world's biggest central banks, slashing key interest rates to zero and arranging its largest-ever extraordinary program to add liquidity into the global market and support credit. The Fed's liquidity creation has already propelled its balance sheet beyond a level of 5 trillion USD in March. We believe the Fed could add another 1 to 2 trillion USD to its books in the coming months through various programs.

Japan low on options – except the fiscal "bazooka"
The Japanese central bank's hands are tied after its long-standing efforts to support the economy and revive inflation had limited impact. Meanwhile, the government of Prime Minister Shinzo Abe appeared to be busy dealing with questions such as whether or not to postpone the 2020 Tokyo Olympics. Now that this issue has been resolved – the games were pushed back to the summer of 2021 – a government-induced stimulus plan amounting to 10 % – 12 % of GDP is being discussed. This will add to the country's already huge debt pile and heighten concerns about long-term fiscal sustainability. However, we think short-term remedies to ward off recession are more urgent at this stage and expect the authorities to go ahead with the plan soon.

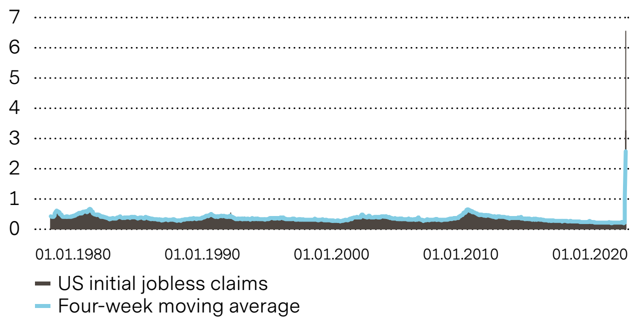
China and emerging Asia coming back to life
As infection rates in China seem to stabilize, authorities are opening production facilities again. Daily activity data points to work resumption rates of approximately 90 % in several industry sectors. Resumption rates in the service industry, for instance in the tourism sector, are rising at a significantly slower pace. The monetary stimulus measures already in place, and the fiscal packages that have been lined up (adding 4 percentage points to GDP growth), should result in a Chinese growth rate of at least 2 % this year, in our opinion. Generally, it appears that Asia will be able to sustain a recovery from the late second quarter 2020 onwards. This region has greater possibilities to support the economy with monetary and fiscal measures than Latin America, for example. In particular, the moderate debt levels in Asia or Eastern Europe enable governments there to set much bigger fiscal packages than their counterparts in South Africa, Brazil or Mexico.

Chart 1: Number of Covid-19 infections in China levelling off, rising elsewhere
Number of confirmed cases, logarithmic scale*



* Constant slope of a curve = constant speed of the spread of the virus
Source: Johns Hopkins University (Git Hub datasample), Vontobel calculations

Chart 2: US jobless claims jump to a record high
In millions



Source: U.S. Department of Labor, Refinitiv Datastream, Vontobel

Central banks' liquidity flood stabilizes volatile bond markets

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Sandrine Perret
Senior Economist,
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The coronavirus pandemic saw government bonds initially rallying amid safe haven inflows. However, concerns about the economic fallout soon led to high volatility and fears of a liquidity squeeze. Various governments' generous and much needed fiscal measures to support the economy, and their debt implications, also sent yields temporarily higher. The steps central bank took will help to keep yields low going forward. We take a cautiously positive view on investment-grade US corporate paper.

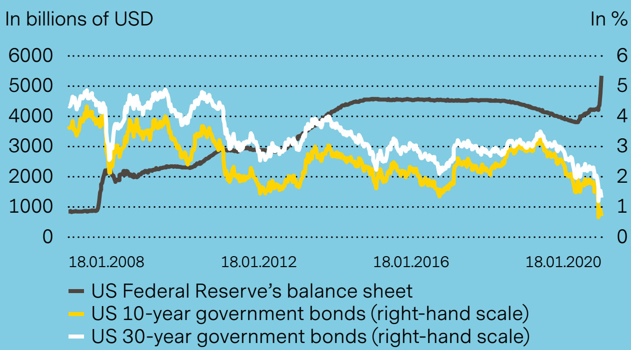
In the past few weeks, central banks around the world stepped up to fix the liquidity shortage that threatened to seize up even the most liquid US and European bond market segments. Monetary easing measures have reached an unprecedented level (see Macro Highlights section page 6 – 7). The US Federal Reserve is now buying unlimited amounts of Treasuries and Mortgage-Backed Securities (MBS) to remove pressure from these markets and ensure that yields stay compressed (see chart 1). We expect yields to move sideways from the current level, a view that has prompted us increase our relative stance on US Treasuries to neutral.

ECB program favors peripheral bonds
The European Central Bank quickly corrected the impression of inaction it left at its scheduled policy meeting mid-March, adopting a new pandemic emergency purchasing program (PEPP). The monetary authority's lifting of a limit on buying no more than 33% of a country's debt enables it to acquire larger amounts of bonds issued by southern European governments. This confirms our previous view that the spreads of these bonds versus "safe" German Bunds will mostly remain under control in the next few months despite rising government spending.

Corporate spreads spike, seen narrowing again
In the corporate bond segment, spreads rose to the highest level since the financial crisis. Moreover, the price of euro area credit default swaps – a protection against corporate default – increased for high-quality companies and issuers of high-yielding debt (see chart 2). The global corporate bond market calmed down after the Fed announced two new programs to provide direct financing to US business in need of liquidity.

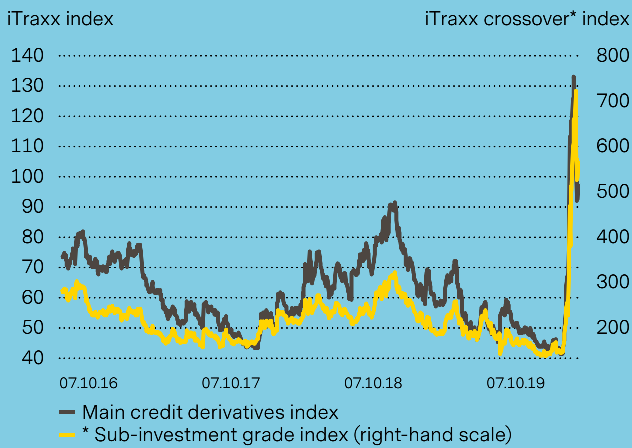
Although spreads remain elevated, we have taken advantage of the attractive valuation to turn positive on high quality investment-grade US corporate debt. However, we will remain highly selective until we see more clearly how the pandemic will develop, and what its impact on the corporate world will be. Systemic risk in credit could reappear if the virus lockdown proves longer than we currently anticipate.

Chart 1: US Federal Reserve's buying spree keeps bond yields down



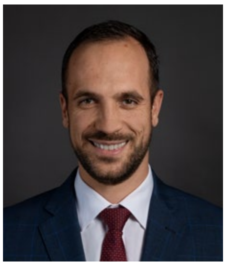
Source: US Federal Reserve, Refinitiv Datastream, Vontobel

Chart 2: The price of credit default swaps spikes in the euro zone



Source: IHS Markit, Refinitiv Datastream, Vontobel

Fortune favors the brave – time to buy equities?



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Stefan Eppenberger
Equity & Commodity Strategist,
Vontobel Asset Management

Following the near-freefall on the stock markets, is now the time for equities? Our analysis of ten different indicators with a different focus suggests that investing could be the right approach. In our opinion, courageous investors should gradually embrace equities, but only if they believe the global economic shock will be temporary.

"Should we be investing in equities now?" Almost all our clients are asking the same question. We can help them make the right decision by looking at ten indicators.

There have been worse slumps
Two indicators place the stock market development in a historical context. For example, a comparison of the current slump with the sell-off in 1987, which also came "out of the blue", would suggest investing in equities (see chart 1). A comparison of the performance of equities and long-term bond yields leads to the same conclusion. However, it looks like a less favorable time to buy when comparing with the financial crisis of 2008 – 2009 or the Great Depression of the 1930s, when equities saw even bigger losses.

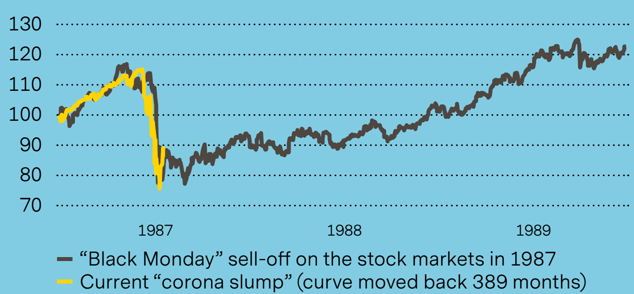
Indicators of economic development suggest a more cautious approach. The leading indicators of future economic performance are still receding. In addition, the spreads for corporate bonds compared with sovereign bonds are continuing to rise, implying pessimism with regard to the prospects for companies. The only solace is provided by the economic stimulus packages worth billions of euros.

Two coronavirus-specific indicators send an ambiguous message. It remains unclear as to when the number of new cases will decline significantly in Italy (the hardest-hit country in the world) and the US (the world's most important economy). By contrast, the reduction in the number of Google searches for "coronavirus" suggests that the anxiety or even panic among the population is slowly decreasing (see chart 2).

"Behavioral indices" give grounds for optimism
Three indicators on human behavior give grounds for confidence on the whole. Our internal sentiment indicator, which measures factors including investor pessimism, has yet to generate a buy signal. However, the development of the put / call ratio, which indicates the extent to which investors are hedging against price slumps, suggests that the worst may be over for equities. The same is true of the extreme price fluctuations, which are likely to settle down again.

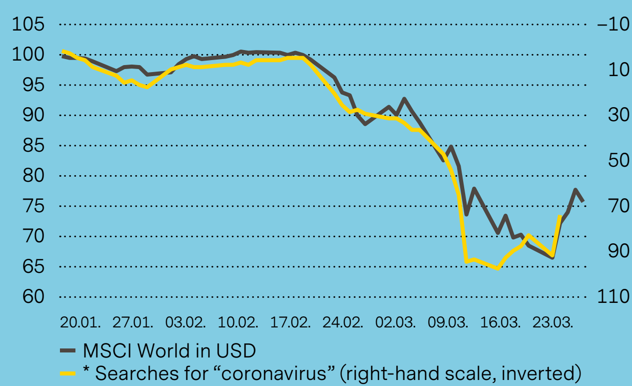
Overall, at least five of these ten indicators currently suggest a relatively positive view of the stock markets. However, we are continuing to exercise prudence and have rolled back our underweighting of equities in only a small number of individual areas for the time being (see pages 2 – 3 and 4 – 5).

Chart 1: Equity sell-off very similar to 1987 – buy signal for investors?



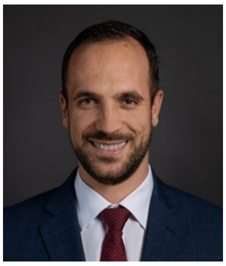
Source: Refinitiv Datastream, Vontobel

Chart 2: The time for equities should come when the "corona panic" begins to subside



Source: Google Trends, Refinitiv Datastream, Vontobel

Gold shakes off initial reluctance during coronavirus crisis



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Stefan Eppenberger
Equity & Commodity Strategist,
Vontobel Asset Management

Gold was initially slow to get in gear when the coronavirus crisis first took hold. However, the precious metal has since regained its reputation as a safe haven on the back of the massive support packages announced by governments and central banks. In our opinion, the outlook for the gold price remains favorable.

The sudden global spread of the novel coronavirus hit the stock markets hard. With the exception of US government bonds, which benefited from interest rate cuts in the US and growing fears of recession across the board, there has been little money to be made on the financial markets. Somewhat surprisingly, gold prices also fell at the same time as equities were being sold en masse. This unusual positive correlation between gold and equities (see chart 1) was previously observed during the financial crisis in 2008.

There are two main reasons for this phenomenon. Firstly, real interest rates (inflation-adjusted interest rates) rose sharply at the start of the Covid-19 crisis, making gold less attractive as an investment option. This occurred in the context of the rapidly deteriorating outlook for inflation. Central banks' liquidity measures were rather hesitant at first and stated curbing nominal interest rates with a lag. Secondly, demand for the US dollar surged, a fact that typically has a negative impact on the price of gold (see chart 2). Fearing a slump in sales because of a recession, companies sought to obtain dollar liquidity as quickly as possible.

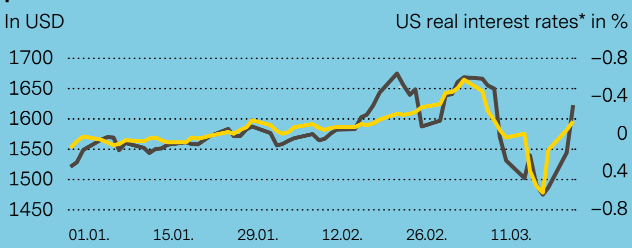
Who will foot the "emergency bill"?

The situation calmed toward the end of March after the US Federal Reserve intensified its support measures again. The dollar immediately weakened, with gold prices witnessing a swift and significant recovery. In addition, many already highly indebted governments wasted no time in spending more money to support the economy, even in the knowledge that their future tax revenues will be considerably lower.

Gold shines over the debt mountains

As the oldest and most tried-and-tested currency, gold is likely to be more popular than ever before as the state coffers lie empty. There are four ways of chipping away at huge debt mountains: surplus revenues, inflation, debt relief, or monetization (see the white paper ***"Modern monetary theory – how do we get down from the debt mountain?"***). With the exception of the first variant – which is becoming increasingly less likely – these all serve to weaken the purchasing power of paper money. This is particularly true of monetization, which involves boosting growth and employment without reducing debt. This theory, which has now become a hot topic again, would turn economic processes on their head and ensure bright prospects for the yellow metal.

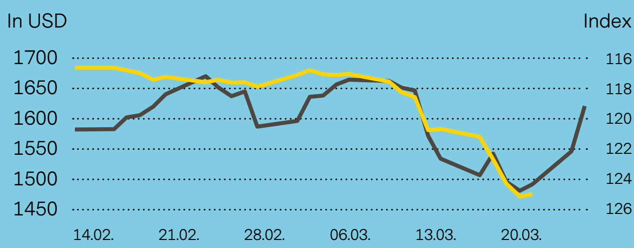
Chart 1: When real interest rates rise, gold comes under pressure – and vice versa



— Gold price per fine ounce
— * Based on inflation-linked US bonds over 10 years (right-hand scale, inverted)

Source: Refinitiv Datastream, Vontobel

Chart 2: Gold typically weakens as demand for the US dollar rises



— Gold price per fine ounce
— Trade-weighted US dollar (right-hand scale, inverted)

Source: Refinitiv Datastream, Vontobel

Dollar bulls are about to swallow their pride

—
Sven Schubert, PhD
Head of Strategy Currencies,
Vontobel Asset Management

While dollar bulls have been stomping their hooves until just recently, they are slowly running out of arguments. This is in line with our forecast of a weakening US dollar, which would benefit emerging-market currencies and the euro. However, we do not expect a rally in these currencies until a return to economic normality is in sight.

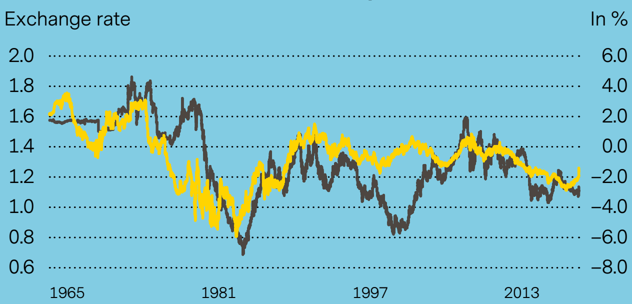
In the recent turmoil, soaring demand for US dollars resulted in shortages. The dollar illiquidity was not as bad as during the financial market crisis over ten years ago, but it caused considerable turbulence on the currency markets. This particularly affected "cyclical" currencies, which depend on a country's exports or commodity prices in general. The beneficiaries of the upheaval included the Swiss franc and the Japanese yen.

Fed gives the dollar a cold shower
Aggressive easing by the US Federal Reserve brought some relief (see Macro Highlights, pages 6 – 7). However, with the stroke of a pen, the Fed also eliminated the dollar's interest rate advantage, the main reason for its recent attractiveness (see chart 1). The greenback is now likely to lag behind the euro and other European currencies such as the Swiss franc over the course of the year. We expect the EUR / CHF rate to range between 1.05 – 1.10 in 2020.

However, exchange rates will hinge on how the US and the euro area perform in relation to each other – and this depends in turn on the further progression of the coronavirus crisis. In Europe, where healthcare systems are probably more robust than in the US, the infection cycle appears more advanced than on the other side of the Atlantic. This would suggest a faster end to the crisis in Europe, which should favor the euro. Looking ahead to the presidential election in November, however, Donald Trump could be tempted to stimulate the economy by all available means.

Emerging markets unduly punished
In the phase of dollar illiquidity, investors' default reaction was to abandon emerging-market investments. Their currency valuations in terms of purchasing power parity are now lower than they have been since the Asian crisis in 1997 – 1998. The markets' harsh judgment on an array of emerging-market currencies is not justified by the fundamental data. While countries such as Brazil, with their empty coffers, have little room for fiscal measures, there is a much larger group of emerging markets that can indeed put together fiscal packages to revive the economy (see chart 2). Over the course of the year, we therefore expect an attractive total return (interest and currency return) in emerging economies.

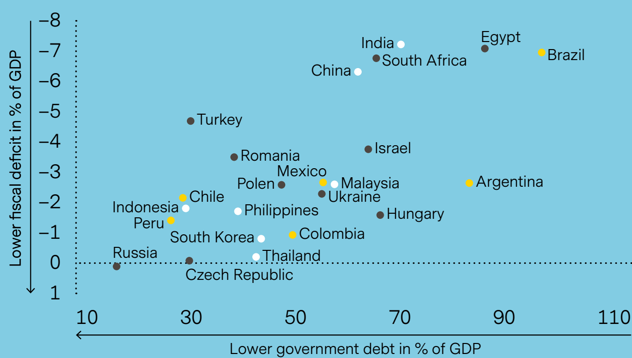
Chart 1: The dollar loses ground when US interest rates become less attractive than European ones



EUR/USD ("synthetic" euro before January 1999)
Yield gap 10y government bonds Germany / US (right-hand scale, US interest rate advantage when negative)

Source: Refinitiv Datastream, Vontobel

Chart 2: Countries without debt and deficit worries such as Russia can launch substantial fiscal packages



Europe, Middle East, and Africa
South America
Asia

Source: Refinitiv Datastream, Vontobel

Economy and financial markets 2018 – 2021

The following list shows the actual values, exchange rates and prices from 2018 to 2019 and our forecasts for 2019 and 2020 for gross domestic product (GDP), inflation / inflationary expectations, key central bank interest rates, ten-year government bonds, exchange rates and commodities.

GDP (IN %)	2018	2019	CURRENT	FORECAST 2020	FORECAST 2021
Euroland	1.9	1.2	1.0	–3.1	5.9
USA	2.9	2.3	2.3	–3.5	3.3
Japan	0.3	0.7	–0.7	–1.8	1.8
United Kingdom	1.3	1.4	1.1	–2.8	4.9
Switzerland	2.7	0.9	1.5	–3.4	7.3
China	6.6	6.1	6.0	2.0	7.2
INFLATION (IN %)					
Euroland	1.8	1.2	1.2	0.5	1.9
USA	2.4	1.8	2.3	0.9	2.1
Japan	1.0	0.5	0.5	0.1	0.3
United Kingdom	2.5	1.8	1.7	0.9	2.2
Switzerland	0.9	0.4	–0.1	–0.5	1.0
China	2.1	2.9	4.5	2.6	2.0

KEY INTEREST RATES (IN %)	2018	2019	CURRENT	FORECAST 3 MONTHS	FORECAST 12 MONTHS
EUR	–0.40	–0.50	–0.50	–0.50	–0.50
USD	2.50	1.75	0.25	0.25	0.25
JPY	–0.10	–0.10	–0.10	–0.20	–0.20
GBP	0.75	0.75	0.10	0.10	0.10
CHF	–0.71	–0.69	–0.75	–0.75	–0.75
AUD	1.50	0.75	0.25	0.25	0.25
CNY	4.35	4.35	4.35	4.00	4.00
10-YEAR GOVERNMENT-BOND YIELD (IN %)					
EUR (Germany)	0.2	–0.2	–0.3	–0.5	–0.3
USD	2.7	1.9	0.8	0.7	1.0
JPY	0.0	0.0	0.0	–0.2	0.0
GBP	1.3	0.8	0.4	0.5	0.8
CHF	–0.2	–0.5	–0.3	–0.7	–0.5
AUD	2.3	1.4	0.9	0.7	0.7
EXCHANGE RATES					
CHF per EUR	1.13	1.09	1.06	1.08	1.05
CHF per USD	0.99	0.97	0.98	0.96	0.88
CHF per 100 JPY	0.90	0.89	0.88	0.90	0.83
CHF per GBP	1.26	1.28	1.16	1.21	1.22
CHF per AUD	0.69	0.68	0.58	0.62	0.57
USD per EUR	1.14	1.12	1.08	1.12	1.20
JPY per USD	110	109	111	107	105
USD per AUD	0.70	0.70	0.59	0.64	0.65
CNY per USD	6.95	6.51	6.86	6.85	7.00
COMMODITIES					
Crude oil (Brent, USD/barrel)	53	66	27	30	45
Gold (USD/troy ounce)	1281	1521	1622	1600	1800
Copper (USD/metric ton)	5949	6149	4811	5000	6250

Source: Thomson Reuters Datastream, Vontobel; closing prices for all data: 24.03.2020

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