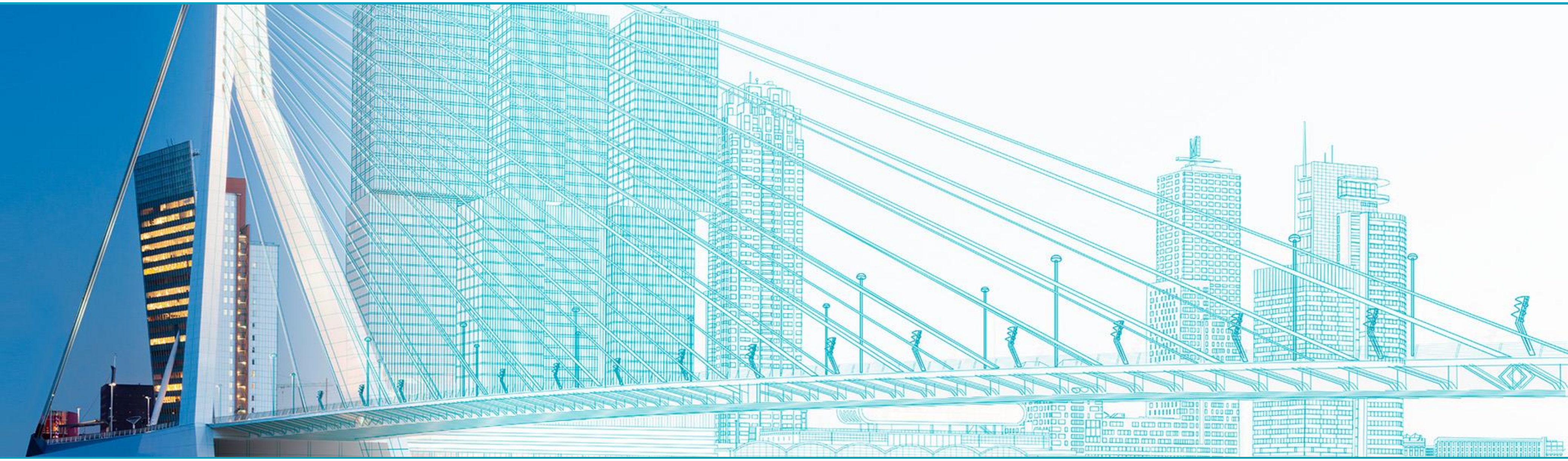
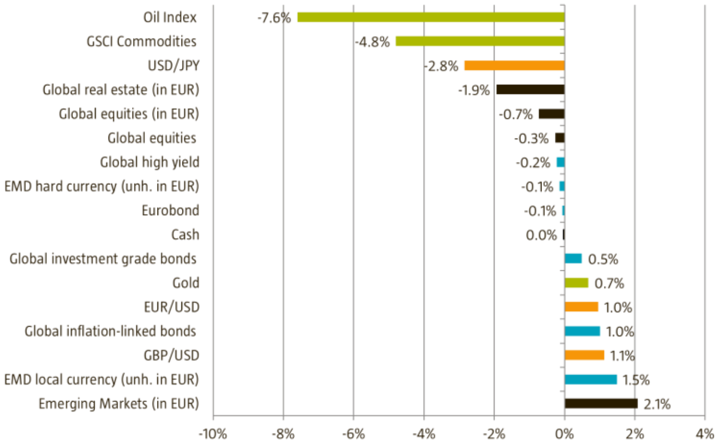


Multi-asset markets outlook

April 2017

General overview

Randomness, with no direction



We are still cautiously positioned

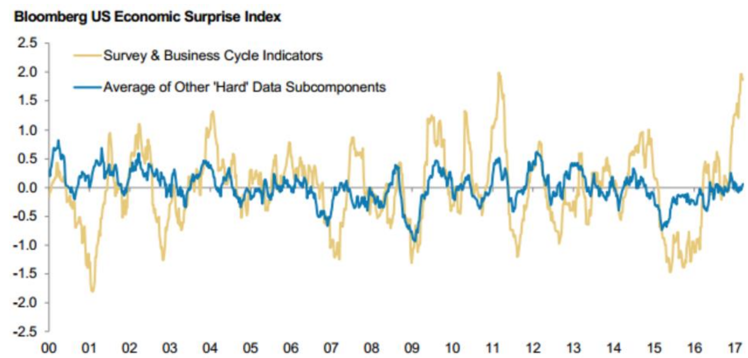
	Portfolio	BM	active
Equities Developed Markets	25.0%	25.0%	
Equities Emerging Markets	5.0%	5.0%	
Real Estate Equities	5.0%	5.0%	
Commodities	5.0%	5.0%	
Core Gov Bonds 1-10	14.0%	20.0%	-6.0%
Core Gov Bonds 10+	7.5%	7.5%	
Investment Grade Corp Bonds	22.0%	20.0%	2.0%
High Yield Corp Bonds	7.0%	5.0%	2.0%
Emerging Market Bonds LC	7.0%	5.0%	2.0%
Cash	2.5%	2.5%	
EUR/USD	-4.0%	0.0%	-4.0%
EUR/JPY	0.0%	0.0%	
EUR/GBP	2.0%	0.0%	2.0%
EUR CASH	2.0%	0.0%	2.0%

- To say there has been an overwhelming theme dominating the financial markets would be overdoing things: the markets have shown a limited to no sense of direction during the past month, so 'domination' has been absent. Having said that, there are two themes that seem to be on the mind of most market participants. The first is the failure of the 'deal maker' Trump to make a deal with his own Republican party, and thereby leaving Obamacare intact. The economic impact may be limited, but it has markets pondering what the bigger implications for the reflation story may be. The second theme is the soft/hard data discussion: the mismatch between the very positive producer and consumer sentiment data seen, and the so-called harder production and consumption data. Risky assets have rallied on the back of the positive sentiment data, but as soon as this fails to materialize in turnover or earnings data, it means that risky markets look vulnerable. We are inclined to think that positive sentiment data will indeed have positive real effects as well, although the current lead-lag seems to be taking (a lot?) longer than normal.

- All in all, more cracks are appearing, but we haven't seen the risk-off market reaction to match it yet. On balance, this is not the environment to aggressively add more risk, so we are sticking to our relatively neutral positioning. We have made no changes to the overall portfolio positioning (neutral on equites and neutral on bonds, but with a strong short position in government bonds versus the riskier parts of the market), but have become more positive on European equities compared to US equities. Additionally, we still have a long position in the US dollar versus both the euro and British pound.

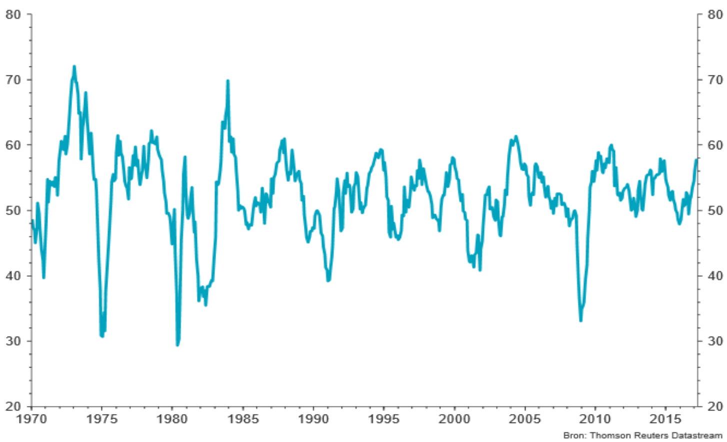
United States

A striking contrast between ‘hard’ and ‘soft’ data



Source: Bloomberg, Morgan Stanley Research

ISM Manufacturing is strong



Source: Datastream

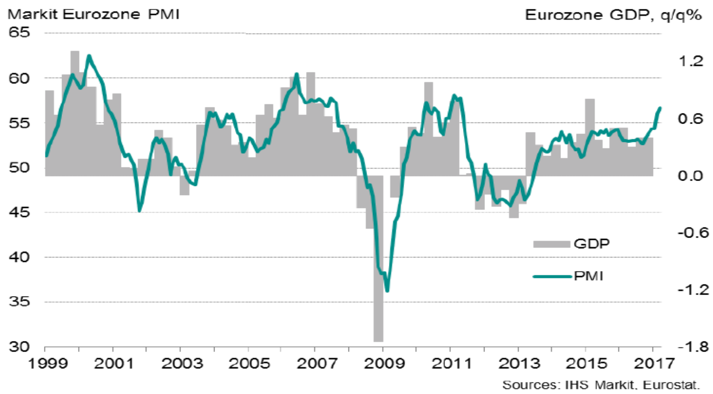
- Data for the US economy shows a striking dichotomy between confidence indicators and ‘hard’ data. Given the generally buoyant producer and consumer confidence, it is also remarkable that the Atlanta Fed forecasting model for GDP still calls for a weak Q1 2017 (1.2% annualized), despite a relatively mild and calm winter. Also striking is a general reluctance of observers of the US economy to upgrade their generally sober GDP forecasts for this year above 2.0%.

- Part of this reluctance can probably be explained by the lack of success of the new administration in implementing its policy agenda. Part of the upbeat sentiment is likely to be inspired by the hope for massive tax cuts for households and companies, drastic deregulation for the energy and financial sectors, and massive investments in infrastructure. However, progress especially on infrastructure and taxes is unlikely in any case this year. The failure to dismantle Obamacare illustrated huge divisions within the Republican party. And on taxes, consensus is lacking, with the Republican leader of the House pushing for highly controversial measures like a Border Adjustment Tax and an end to the tax deductibility of interest payments. Republicans are also divided on the need for budget discipline.

- Still, we consider it highly unlikely that the generally upbeat mood, a steadily improving labor market, and a strong industrial sector as illustrated by the rising ISM manufacturing index (admittedly soft data) will not materialize into a GDP growth rate higher than 2.0% in the coming quarters, barring the outbreak of devastating trade wars. So far the new Administration is operating cautiously on this chapter and it could turn out to be no more than a ‘paper tiger’.

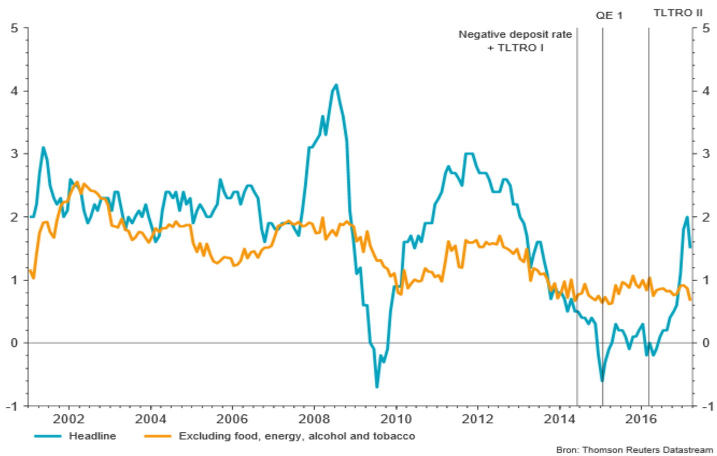
Europe

Eurozone growth is at a six-year high



Source: Markit, Eurostat

Headline and core inflation are both lower



Source: Datastream

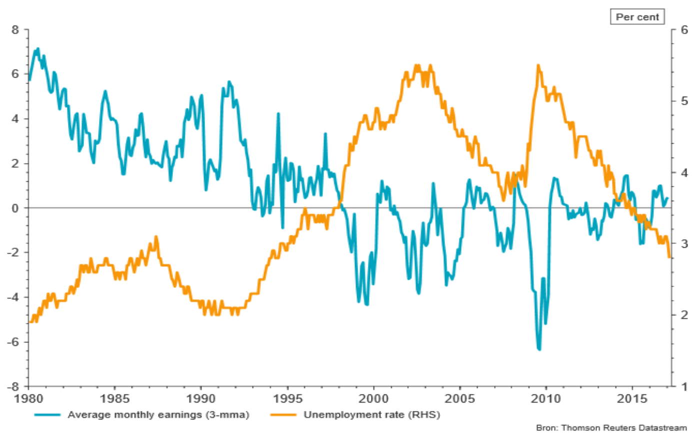
- The Eurozone economy continued to strengthen further in March, as illustrated by the composite Markit purchasing managers index signaling an impressive quarterly growth rate of 0.6%. Surging order books have also led to the strongest employment growth in 10 years for the manufacturing and service sectors.

- Robust growth is of course increasing inflationary pressures, as illustrated by rising input prices (at their highest level since March 2011). The relatively weak euro exacerbated the effect of the rise of prices for commodities, not only for oil, but also in food and metals. It takes time for these effects to work through the system as core inflation – despite all the aforementioned developments – *declined* in March (temporarily due to the Easter effect) to a level of 0.7% on a yearly basis. This diminished the pressure on the European Central Bank to rain in its QE program further, and/or to contemplate hiking its negative deposit rate. We expect the ECB to be on hold for the time being in any case until after the second round of the forthcoming French presidential elections (7 May, 2017). But its initial strategy to keep its policies unchanged for the remainder of 2017 is probably untenable in the light of buoyant growth.

- Risks for the upbeat picture on growth are mainly political, with the upcoming French presidential elections getting the most attention. There a defeat of far-right candidate Marine Le Pen is consistently predicted by the polls, although nervousness in the bond market continues to increase. Much less attention for the time being has been given to the political developments in Italy, where the populist Eurosceptic Five Star Movement is currently leading in the polls.

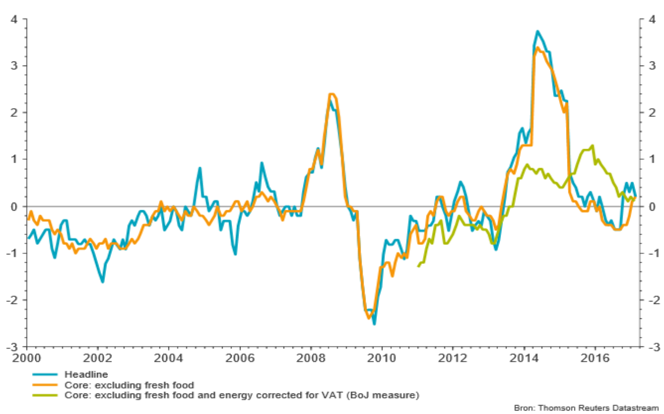
Japan

An incredibly low unemployment rate is still not feeding into earnings



Source: Datastream

Some price momentum due to the weak yen and higher oil price



Source: Datastream

- The Japanese economy continues to strengthen. Growth is broad-based, with both the manufacturing and service sectors enjoying an upswing. As a consequence, the labor market continues to improve. The unemployment rate declined in February to an incredible low of 2.8%, the lowest in more than 22 years. Consumers, however, remained reluctant to spend. Household spending, declined 3.8% on a yearly basis, though a leap year effect and relatively bad weather makes this figure look worse than the underlying trend.

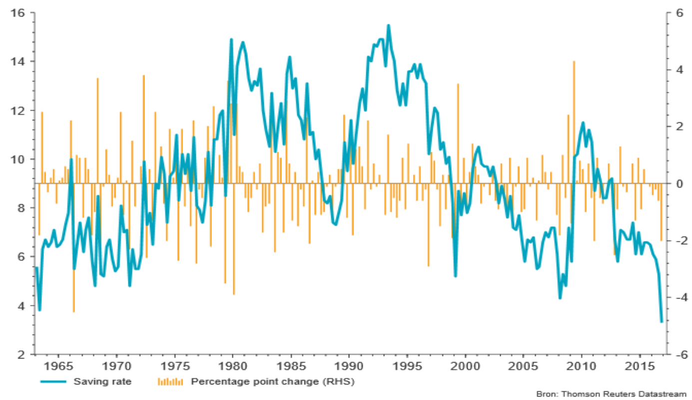
- The strength of domestic demand remains a worry for the Japanese economy, and wage growth isn't expected to accelerate markedly, despite the incredibly low unemployment rate. In March, some of Japan's top companies announced their lowest wage increases in four years. The Japanese economy continues to lean on external demand and needs a low yen, potentially straining relations with the new US Administration.

- The weakness in the yen and the rise in the price of oil has broken the disinflationary trend of Japan's inflation indicators. But the preferred indicator by the Bank of Japan (BoJ), the so-called 'core ' CPI, remains weak, declining to 0.1%. The BoJ Governor Harohiko Kuroda has consequently left the BoJ's massive 80 trillion yen annual asset-purchase scheme unchanged, and has said the bank would press on with its plan to keep the yield on government 10-year bonds around zero, despite expected rate rises by the US Federal Reserve.

- Speculation is growing that Kuroda will be reappointed in April 2018 for another five years, after the ruling Liberal Democratic Party's recent decision potentially allowing Prime Minister Shinzo Abe to remain in power until 2021.

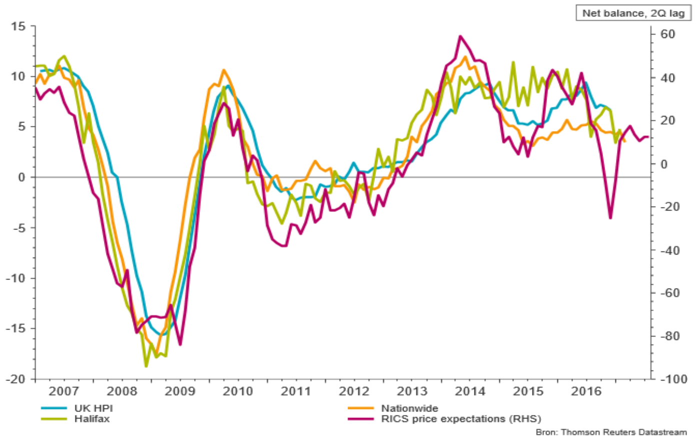
Brexit

An unsustainable consumer boom



Source: Datastream

House prices are sliding



Source: Datastream

- The UK government triggered Article 50 of the Lisbon Treaty and is now set to leave the EU in two years' time. The opening bid of the EU for a settlement on the net liabilities of the UK is EUR 60 billion, or 3% of UK GDP. Over a 10-year period it doesn't amount to much, but this could still prove to be political dynamite given UK public opinion.

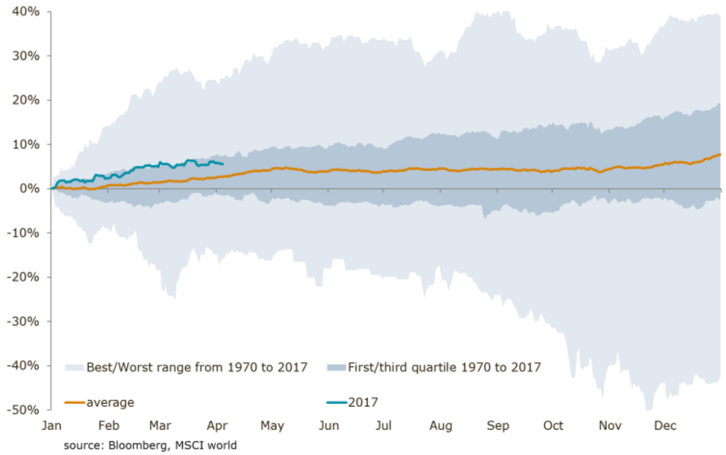
- The UK government is striving for a trade agreement with the EU in two years' time. This looks overly ambitious, as trade agreements generally take much longer to negotiate. Furthermore, although the divorce settlement only takes a qualified majority under the Lisbon Treaty, a trade agreement will have to be ratified unanimously by all individual member states. This increases the likelihood of long and winding negotiations.

- The UK economy has so far held relatively firm, helped by the weakening of the UK pound and a consumer boom, possibly in anticipation of rising inflationary expectations. This boom is clearly unsustainable, as illustrated by the collapse in the consumer savings rate. Rising inflation damages real household income. Now that Article 50 has been invoked, we also expect rising disinvestment and declining foreign direct investment damaging UK GDP growth, given the country's clear intention to leave the largest internal market in the world. The UK housing market also shows signs of weakness.

- The UK itself now looks vulnerable, with Sinn Féin calling for a referendum in Northern Ireland on reunification with the Irish Republic to avoid reinstituting a hard border between the north and south. Scotland is also asking for a new referendum to leave the UK.

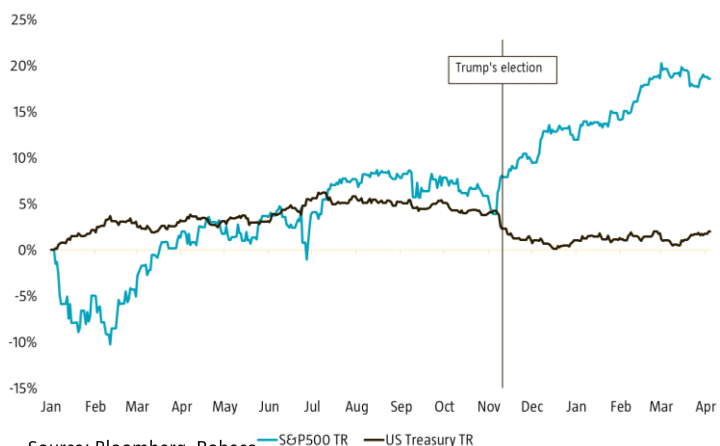
Equities (I)

The drift is still in place



Source: Bloomberg, MSCI world, Robeco

How long will the reflation trade last?



Source: Bloomberg, Robeco

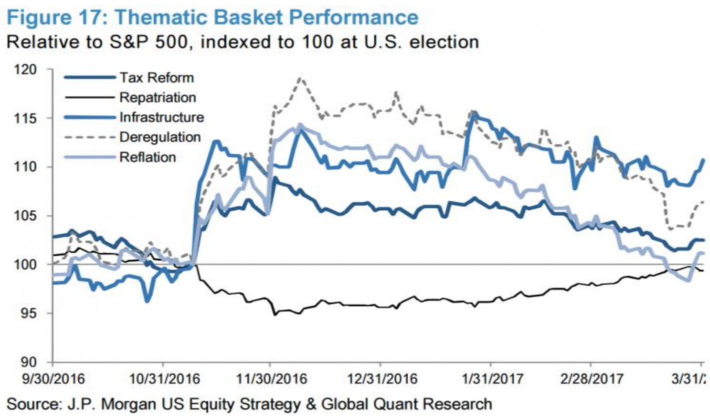
- Climbing the wall of worries. If there is one claim to fame that is clearly linked to stock markets, it is their ability to drift higher despite all the (potentially) bad news that is being thrown at them. The last couple of months have been a good example: rising populism in Europe, Brexit, the uncertainty surrounding the new US President; they all simply failed to have an impact on global stock markets.

- The two causes for the optimism in worldwide stocks are easy to identify in this case. On the one hand we have the reflation hopes, linked to the Trump Presidency. Sure, he may be a bit unorthodox, but his plans for tax cuts and infrastructural spending are sure to give the US economy a boost, which should have positive spillovers to the rest of the world – or so the argument goes. On the other hand we have the growth momentum argument, which is separate from Trump reflation. Macroeconomic data has been surprising on the upside for a number of months now – a trend that has been visible across the world. Europe in particular seems to have turned the economic corner, with unemployment steadily declining (albeit from a high level). As we have said before: "It's the economy, stupid." With a combination of reflation hopes and growth momentum, it is no surprise that stocks have been drifting higher.

- Although the two drivers behind the rally can still be defended, it is hard to deny that some cracks appeared in both storylines last month. To start with the reflation hopes, the fact that the US Republican Party failed to repeal Obamacare is a clear wake-up call that campaigning successfully is somewhat different to governing successfully. The Republicans may hold the majority in both the House and Senate, but it is clear that this does not offer any **>>**

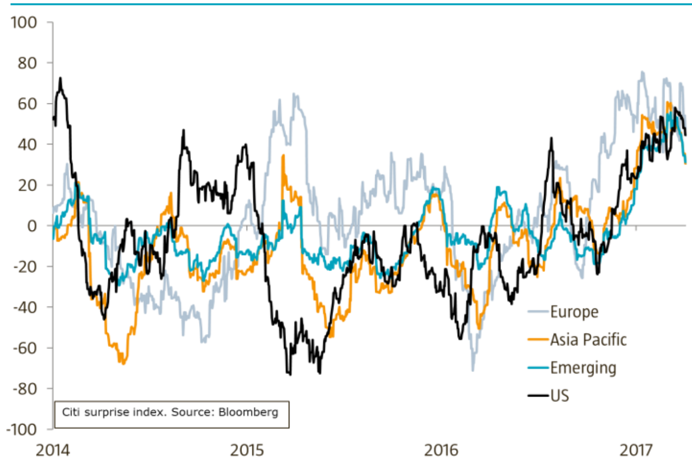
Equities (II)

Those failing Trump trades...



Source: JP Morgan

Citi surprise indices are still up in the clouds



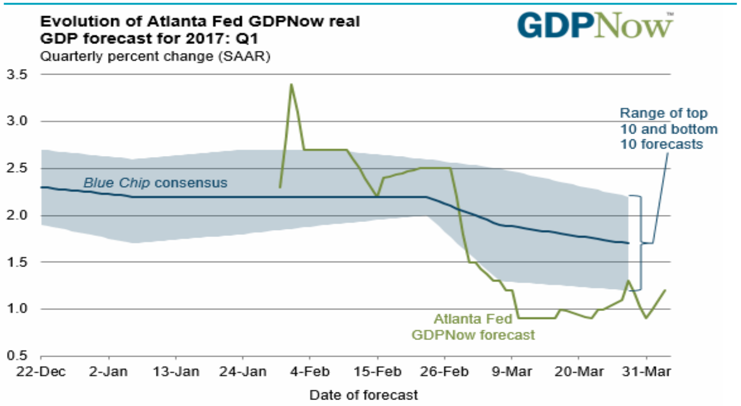
Source: Bloomberg, Robeco

- guarantees that Congress can (and will) implement the Trump agenda. The Republican party is far from being a united group: big differences in opinion between the right-wing Freedom Caucus and the more centrist faction are a risk for the implementation of the ambitious Trump plans. This does not only apply to repealing Obamacare, but is also a risk when it comes to the tax reform plans. The conservative wing of the Republican party has been principally opposed to higher debt, which could mean that the room for an 'easy' expansionary policy (=running a bigger deficit) might be limited. The more that Trump is forced to stick to deficit-neutral changes, the more limited the overall reflation impact will be for the economy as a whole. Reforming taxes and simplifying the system can still be a net positive, but it is of course far less potent than what the market seemed to be expecting back in November. Not surprisingly, the Trump trades have been fading as time has progressed (see chart on the left). The market is clearly less sure of the 'very massive and very strong tax reform' promised by Trump, while the lack of progress on the infrastructural spending dossier does not act as a confidence booster either.

- What about the other stock positive, the growth momentum seen in the world? The promising news is that momentum is still positive, if judged by the famous Citi surprise indices (see chart on the left). Producer and consumer confidence indicators have steadily moved higher in recent months, while most labor markets have seen a steady rise of jobs and decline in unemployment. That's as far as the good news goes, however, as there is a clear mismatch between the positive sentiment and (potentially lagging) labor market data on the one hand and the 'hard' economic data on the other hand. This mismatch becomes **>>**

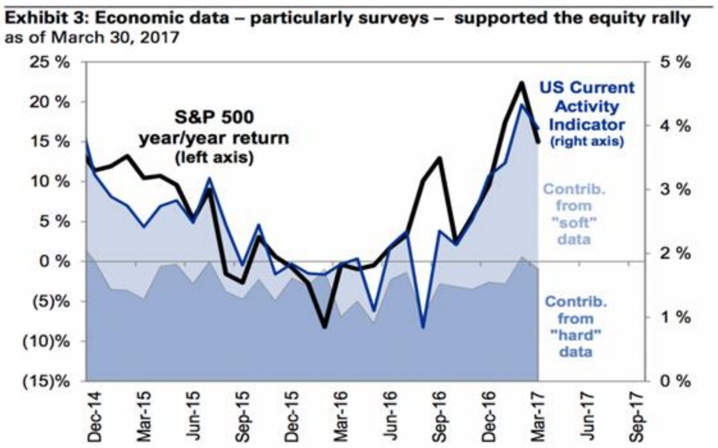
Equities (III)

Underlying data is a lot less supportive than sentiment data appears to be



Sources: *Blue Chip Economic Indicators* and *Blue Chip Financial Forecasts*
Note: The top (bottom) 10 forecast is an average of the highest (lowest) 10 forecasts in the *Blue Chip* survey.

Stock markets have been following the 'soft data' lead



Source: Goldman Sachs Global Investment Research.

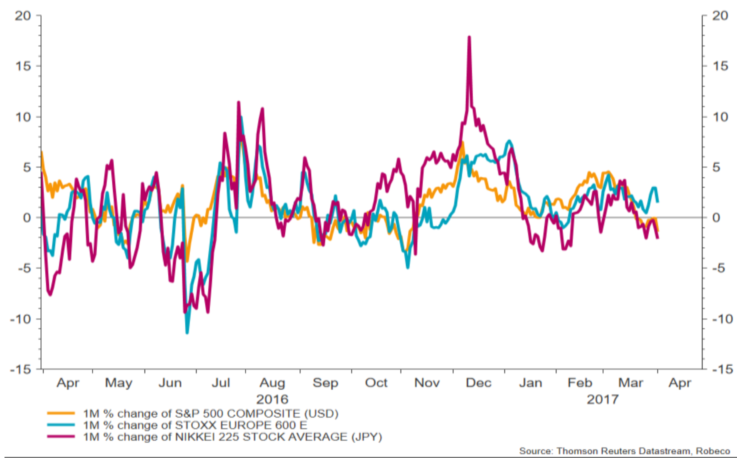
- immediately clear when we look at the latest reading of the Atlanta Fed GDPNow growth tracker, which puts Q1 growth for the US economy at around 1%, in stark contrast to the positive sentiment data. To the defense of the optimistic interpretation, the first-quarter growth report of the US has been a structural (negative) outlier during this expansion phase, so it cannot be excluded that underlying growth is much more supportive. Having said that, much of the reported weakness seems to be linked to low consumer spending, as witnessed for example in weak car sales. As consumer spending accounts for over 70% of US GDP, this is certainly a risk that should be taken into account.

- A second, more positive interpretation would be that the sentiment indicators are leading, so it will only be a matter of time before the 'hard data' starts to improve as well. Based on past experience, we are inclined to think that positive sentiment data will indeed have positive real effects as well, although it appears that the lead-lag is taking (a lot) longer than has normally been the case.

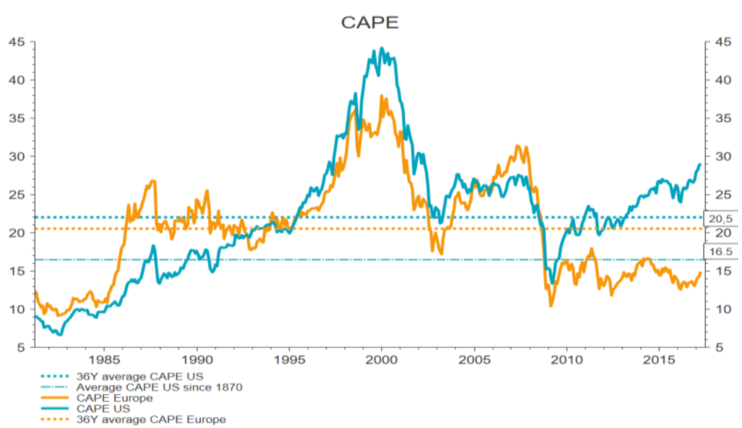
- All in all, although stocks have the ability to climb the wall of worries, it appears to us that this wall became a bit higher last month, without it having had much of an impact on the general performance of stocks. Given greater doubts about reflation, growth, and the timing or size of either, the mismatch between developments and performance has increased, which does not help us to become more bullish on stocks right now. We therefore remain neutral and see better opportunities in relative trades.

Developed Market Equities

European equities are in the lead



CAPE Europe; still cheap, and starting to reflect improved growth momentum



Source: Thomson Reuters Datastream, Robeco

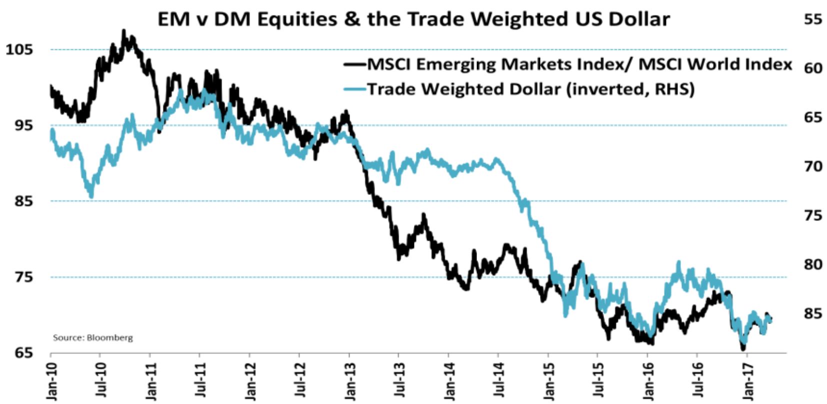
- Developed market equity performance faltered last month as cracks started to appear. A stronger yen did no good for the Nikkei, while US equity investors have still not had their eagerly awaited tax cut announcements. Equity momentum on a one-month basis in local currency therefore weakened, with Japanese equities losing 2.5% in yen, followed by the US's negative monthly return of 1.4% in dollars. Europe was the outlier, remaining resilient with a positive return of 1.4% in euros. Long momentum (12m-1m) favors the US.

- Earnings revision ratios show that analysts have been upgrading developed market corporate earnings for this calendar year after a continuing upbeat flow of sentiment data. In the euro area, the composite producer manufacturing confidence index has risen for six straight months, and is now at a six-year high. Unemployment dropped to 9.5% and the improving labor market is reflected in rising consumer confidence. A steep yield curve in the Eurozone helps financials, while oil prices around USD 50/barrel do not choke off growth. An environment in which economic activity is elevated, but where labor has still low bargaining power, is beneficial for the margin expansion of European corporates.

- From a CAPE perspective, Europe remains cheap, from both an absolute and a relative point of view compared to the US. Economic policy uncertainty has driven European multiples lower against the US since the euro-crisis erupted in 2010. While French elections and EU divorce talks with the UK remain a non-negligible risk for Eurozone equities near term, this is largely reflected in the discount. Against a background of attractive valuations, still dovish monetary policy and notable pick-up in economic activity, we prefer European equities relative to US equities.

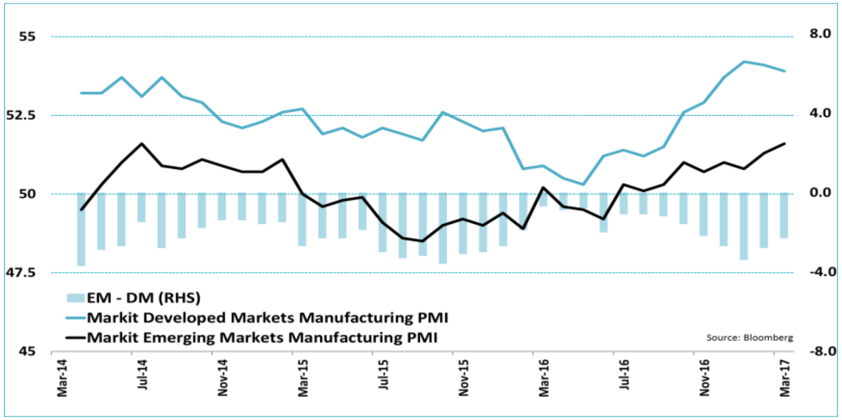
Equities: Emerging vs Developed (I)

Emerging Markets – relative performance



Source: Bloomberg, MSCI Emerging Markets

Emerging vs. developed market manufacturing PMI



Source: Bloomberg

- Emerging market equities outperformed developed market stocks in March and enjoyed a very solid quarter, both from an absolute and a relative perspective. As we described last month, a number of things have improved in recent months, leading us to remove our negative stance on emerging market equities, although some risks remain.

- First, while the US Federal Reserve delivered a dovish statement accompanying what was only the third rate hike in a decade in March, it remains the only major central bank with a tightening stance. We expect the US dollar to regain its momentum, albeit at a slower pace than before.

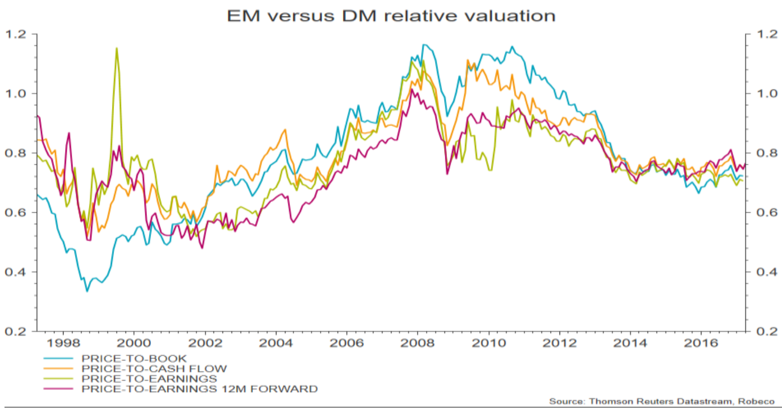
- Second, emerging markets have historically been one of the major beneficiaries of synchronized growth upswings, of the kind we are seeing today. However, as the chart on the left shows, the main improvement has been with developed markets. Manufacturing PMIs have improved markedly in both regions, but economic momentum remains stronger in developed markets. In addition, GDP growth levels have slowed much more in emerging markets, resulting in a relatively small growth gap with developed markets. In the last two months, emerging countries seem to have caught up a little, and we would prefer to see this continue before we become more upbeat.

Equities: Emerging vs Developed (II)

Earnings revisions

Source: Bloomberg

Valuations



Source: Thomson Reuters Datastream

- Third, the Trump factor has so far been benign for emerging markets. The US president is struggling to get legislation through Congress, which could imply a milder impact on trade. However, we just don't know at this point how things will work out.

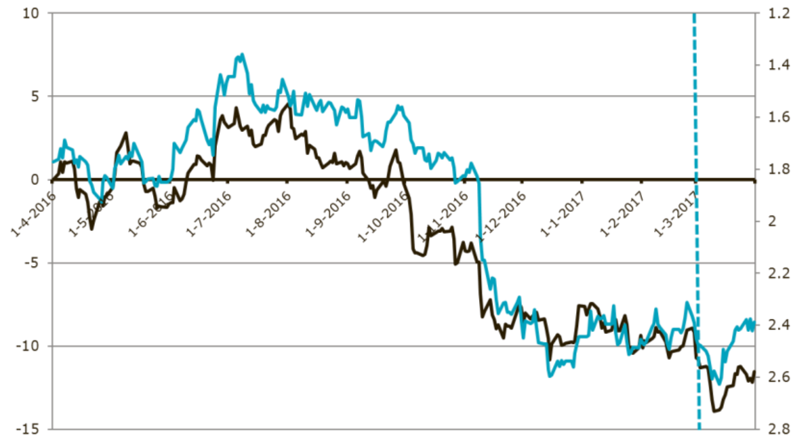
- Fourth, commodity prices lack a catalyst to further rally from here. They have recovered and benefit from higher growth, but the chance of more significant gains looks limited, with shale producers ramping up oil production and China marginally tightening to push back debt accumulation.

- Fifth, on the back on synchronized global growth, earnings are growing globally as well. Here, things could be more persuasive as well. Earnings revisions are moving up, but emerging equities are lagging other regions, staying ahead of only the US. From this angle, European equities looks more attractive.

- Apart from these factors, valuation remains a positive. However, relative valuations are not extreme, and are unlikely to be a sole trigger. So we remain neutral on emerging markets, as we don't think the positives convincingly outweigh the negatives for now.

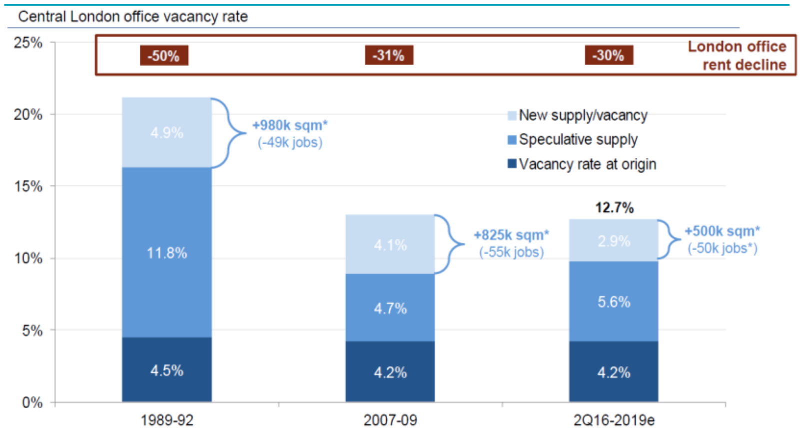
Real estate

Relative real estate performance and US interest rates (in USD)



Source: Bloomberg, S&P

London real estate: expected to look like 2008



- It's becoming a sort of a 'same old story' when we discuss the performance of real estate. Its performance depends heavily on the development of the US Treasury yields, and nothing changed in this relationship during March. In the end, the 10-year rate was – with some volatility – flat last month. The S&P Global Real Estate Index (in US dollars), however, didn't recover in line with lower yields and closed down 1.2%. Compared to global equities (in US dollars), this meant an underperformance of 2.0%. The Fed's rate hike last month was widely expected and didn't have a significant impact on bond markets. The fact that President Trump is having difficulties in implementing his plans is viewed as being more important.

- In the UK, the real estate sector's earnings managed to beat the low expectations in the first quarter. However, the outlook as the Brexit negotiations begin is gloomy, due to rising supply and vacancy rates, combined with falling rents. The comparison with the financial crisis of 2008 comes to mind – "avoid London real estate" seems to be the new mantra.

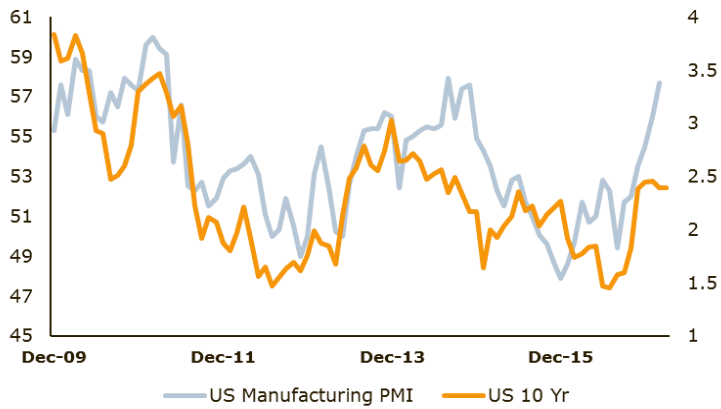
- Outside the UK, valuations in the US and Japan are still stretched. The dividend yield on real estate is still attractive compared to equities and bonds. This offers a kind of buffer. The bond yield will remain the main driver of the real estate performance. We still hold a neutral weight for real estate.

AAA Bonds (I)

Support for the euro currency is marginally above 50% in Italy

Source: Eurobarometer & Robeco

US Manufacturing PMI and US 10-year yields



Source: Bloomberg & Robeco

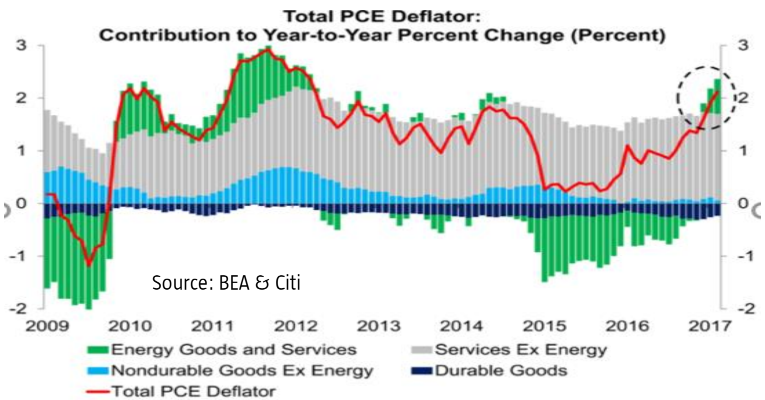
- March was a month of "things that could have happened" but didn't. In the Netherlands, the election outcome did not lead to an increase in euro break-up fears. US Republicans failed to do what they had been promising their constituents for years, namely repealing the Affordable Care Act (better known as Obamacare). And most central banks chose to maintain an easing bias, thereby passing on the opportunity provided by the continued synchronized upswing in growth to adjust policy.

- Given the political events that the Eurozone faces in the coming period (French and German elections), we can understand that the ECB prefers to tread cautiously. Also, the well-flagged lowering of the purchasing program from EUR 80 billion to EUR 60 billion will be implemented in April for the first time, which is a valid reason for the ECB to take a wait-and-see approach.

- Our assessment of the Fed is less positive though. The combination of a last-minute rate hike (FOMC members only talked this up two weeks in advance) and the subsequent very dovish tone struck by Fed Chairwoman Janet Yellen, led to a decline in bond yields, a weaker dollar and a rise in equity prices. The outcome of the rate hike was therefore one of easing financial conditions, rather than of tightening. The only interesting piece of information that the Fed provided was that their inflation target is symmetrical, which to us means that **>>**

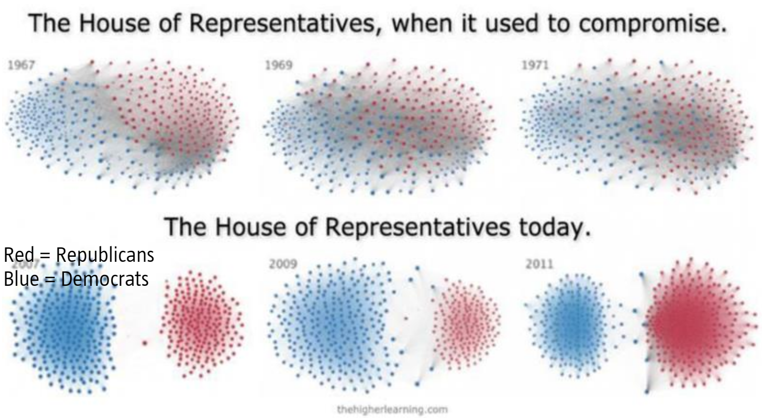
AAA Bonds (II)

The PCE is above 2% but with the help of Energy



Source: BEA & Citi

A less bipartisanship and also no unity between Republicans



Red = Republicans
Blue = Democrats

Source: Thehigherlearning.com & NWM

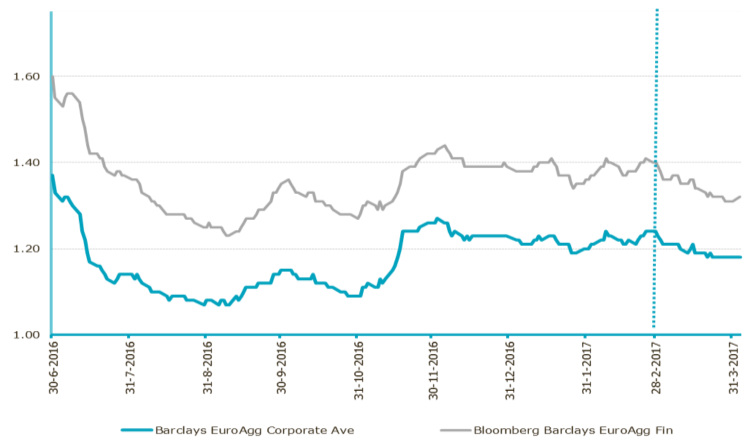
- they will allow an overshoot of inflation above the 2% target and most probably also for an extended time. Just to be clear, we are not calling for central banks to move to a tightening bias, as inflation is still not at levels that one would consider to be threatening. We do, however, think that the current environment doesn't call for emergency policy settings anymore.

- We continue to think that the US holds the key to the future path of rates. Important in this regard is how much of Trump's campaign promises he will ultimately be able to implement. The inability of Republicans to come to an agreement to repeal and replace Obamacare raises serious concerns about the execution of power by Trump and his fellow Republicans. The next test will be how the discussions regarding the US budget go. If this doesn't go in a coordinated and smooth manner, skepticism will grow about Trump's ability to implement tax cuts and tax reform. The level of net stimulus can already be questioned, as no savings can be achieved due to the healthcare reform failure.

- We continue to think that growth will ultimately prevail, but acknowledge that politics can have a strong impact on sentiment, be that positive or negative. We prefer to remain underweight bonds and also prefer to be underweight French and Italian bonds. This our insurance against a possible escalation of political risk in the Eurozone.

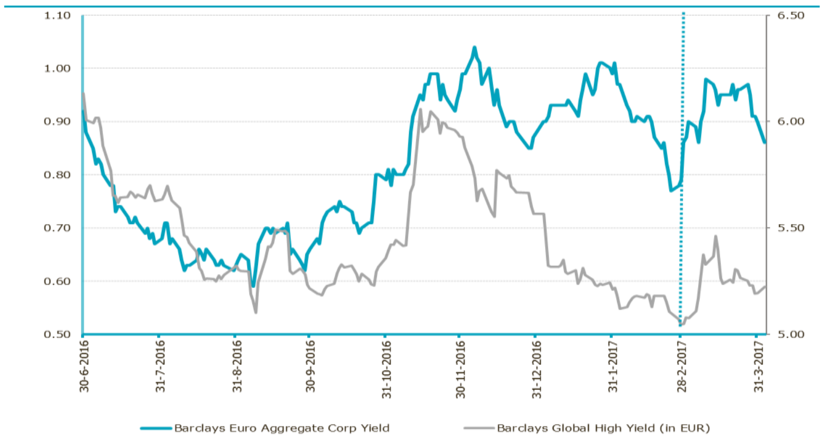
Investment Grade Credits (I)

March: spreads were still flat



Source: Bloomberg, Barclays

Yields in global high yield area are more attractive than in investment grade



Source: Bloomberg, Barclays

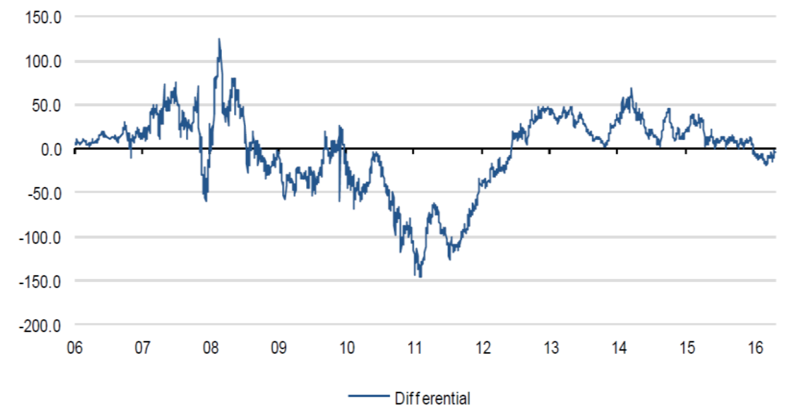
- Since mid-November, the European credit spread has moved within a trading range of 8 basis points (1.18-1.26 bps). The underlying country risk has risen since then, but as the market's fears over the outcome of the French elections later this month seem to be easing, this process also has come to a halt.

- The ECB is still in the market as the most important buyer, although the pace of buying slowed down last month. This is the result of the ECB's December pledge to reduce the size of its bond-buying program from EUR 80 billion to EUR 60 billion. However, nothing official has been said about tapering the CSPP program. Given the current favorable economic developments in Europe, one would expect a reduction of the program to be more likely. Having said that, the timing of the announcement is crucial: we don't expect anything to happen until after the results of the French elections.

- From a yield perspective we think high yield bonds are currently more attractive, so we have shifted a part of our overweight position to them. As spreads are flat, yields in credits move in unison with European government bond yields. The European credits index has a 2-year shorter duration, as well as a higher yield, both of which are positives in an environment of expected rising bond yields. European financials have been excluded from the CSPP program, so tapering has less influence. Given the **>>**

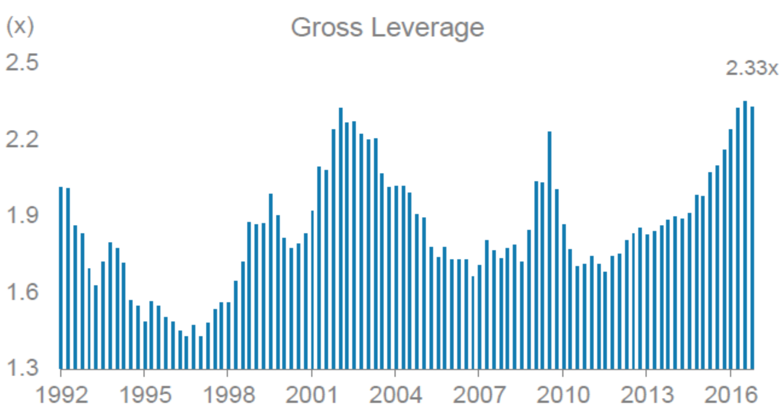
Investment Grade Credits (II)

The corrected yield differential between US and European investment grade bonds



Source: SG Cross Asset Research/Credit

US leverage is at peak levels



Source: Morgan Stanley, Bloomberg

- wider spread they could be an interesting alternative, although the sector is vulnerable to credit events: the Italian banking sector hasn't been particularly healthy for example.

- The yield difference between US and European investment grade bonds is now just below 2.5%. This seems interesting in a search-for-yield environment. However, several risks need to be noted in order to make a fair comparison. Credit quality is lower in the US, index duration is about a year longer, and there is currency risk. Correcting for these factors, the underlying differences are very small, as they have been for over two years now.

- The US economy is in good shape, but top-level leveraged US credits are vulnerable to unexpected economic headwinds. The Fed hiked for the first time this year and is expected to continue the cycle, which historically hasn't been positive for credits. The 'Trump trade' seems to have faded out, and spreads are no longer falling. Given these circumstances, there's little reason why US credits spreads should start another round of tightening. All in all, there are enough reason to be cautious on US credits.

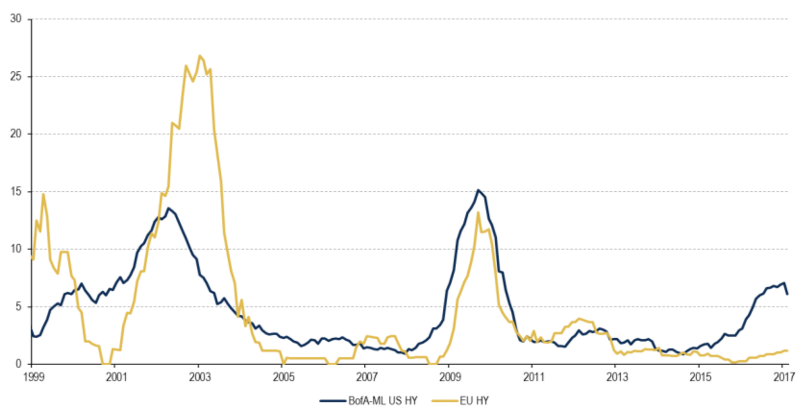
- We have a small overweight position in European credits over government bonds. Risks are increasing in Europe though, as the consequences of a likely QE tapering also has an impact on the CSPP program.

High Yield (I)

Global high yield spread

Source: Bloomberg, Barclays Global High Yield

High yield defaults



Source: BofA-ML

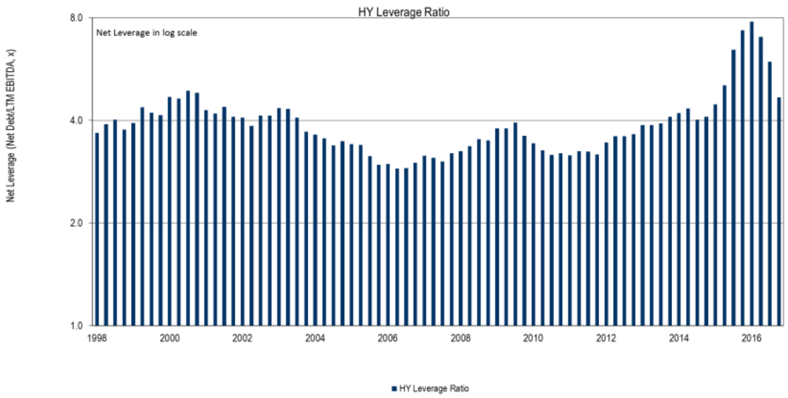
- The spread on global high yield bonds widened marginally to a peak of 393 basis points in March. Despite a small negative return of 0.2% during the month, high yield bonds performed better than credits and government bonds.

- Global economic momentum held up in March, with PMIs consolidating their upbeat values, except for the US ISM Manufacturing Index which declined a bit. Current economic conditions should suit high yield bonds well. In addition, given that government bonds yields are too low for the current economic conditions, investors will continue their search for yield as long as sentiment towards risky asset remains strong.

- As mentioned in previous months, the US default rate has indeed peaked. Oil prices have doubled since their low in February 2016, and this has put an end to the massive wave of defaults in the energy sector. Shale oil companies have proven to be more resilient than was previously thought, partly because of the falling cost of production. This resilience, however, also implies that production will continue to ramp up, as we have seen in the last two months or so. This limits the upside in oil prices, which could in turn put renewed pressure on shale companies. Spreads are already very tight. In Europe defaults are rising, but only very gradually, and remain low on an absolute basis.

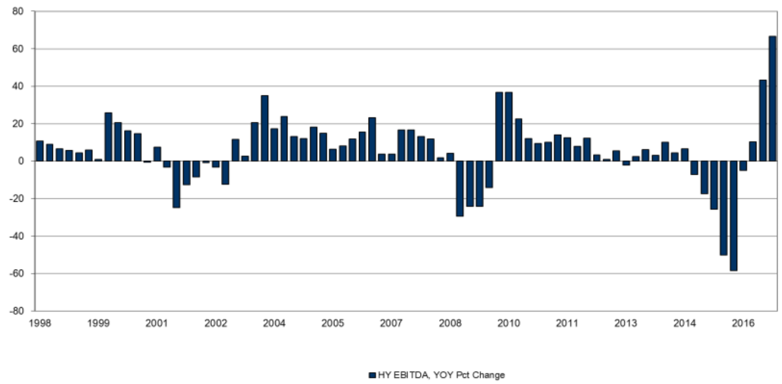
High Yield (II)

Leverage



Source: BofA-ML

Earnings growth

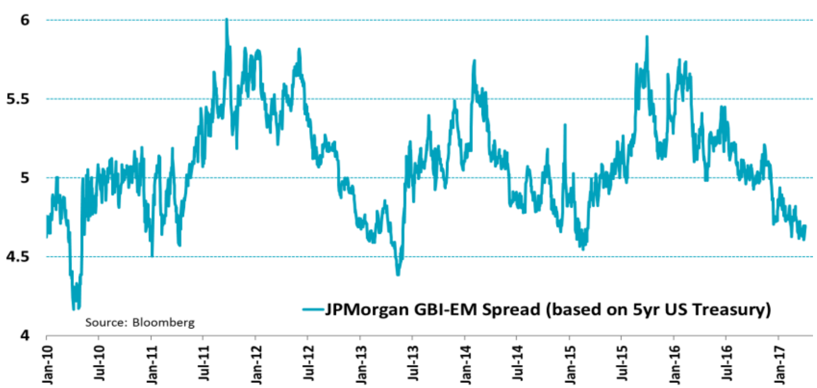


Source: BofA-ML

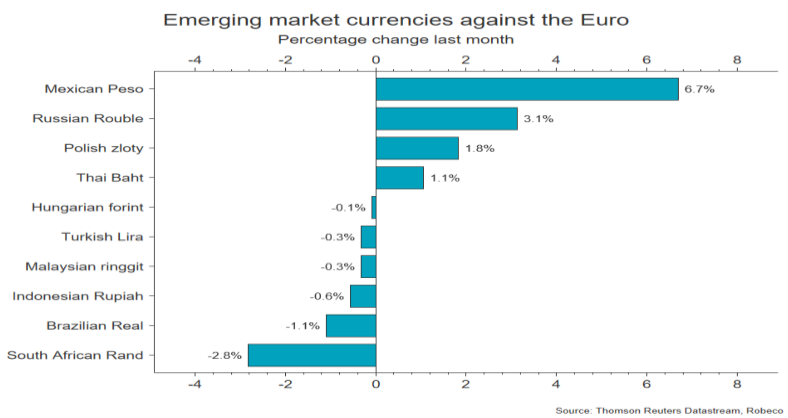
- On average, fundamentals for global high yield bonds are mixed. Valuations look stretched as spreads have tightened massively over the last 12 months. The gap with the earnings yield of stocks has almost vanished. But when compared to other fixed income asset classes, high yield looks more attractive. Government bonds, even in the US, remain extremely expensive, especially if one expects some kind of normalization in the coming years.
- Lower yields have also pushed up duration risk for all bonds, but especially for governments bonds. Little is needed to push returns below zero, and to a lesser extent, this is also the case for credits.
- Leverage of high yield companies is high, but at the same time has been coming down quickly in recent quarters. The long-expected recovery of earnings is an important factor here. Again, some of this is driven by the energy sector. We expect the earnings recovery to continue for some time, giving high yield companies more room to control their leverage ratios.
- We are overweight high yield bonds, albeit hesitantly. Growth and sentiment underpins the endless search for yield, but valuations have become stretched. However, valuations are even more stretched in other parts of the bond market.

Emerging Market Debt (I)

Emerging market debt - spread



Emerging currencies



Source: Thomson Reuters Datastream, Robeco

- Together with emerging market equities, emerging local currency debt was the best performing asset class in March. The spread, compared to the 5-year Treasury yield, fell by 13 basis points, and emerging currencies appreciated a bit more against the US dollar and euro.

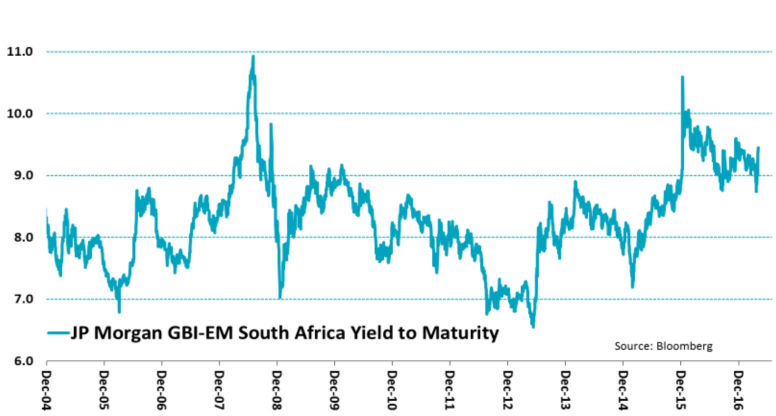
- Of the issues that affect emerging currencies, economic imbalances such as current account deficits have reversed somewhat on the back of faster economic growth globally. We expect this trend to continue in the coming months. In addition, manufacturing PMIs around the globe remain at very healthy levels.

- Within emerging currencies, there was quite a bit of currency return divergence, as is often the case. The Mexican peso powered ahead as the country shrugs off the hostile language of Trump during his election campaign. For now, the Trump effect looks more benign than was previously thought. The Russian ruble strengthened as trade data and the economic outlook improved. On average, emerging currencies added 0.45% return to the JPM GBI-EM Global Diversified Index in euros.

- The South African rand dropped, however. President Jacob Zuma decided to fire his finance minister, which was ill-received by markets, partly because the move was unexpected since **>>**

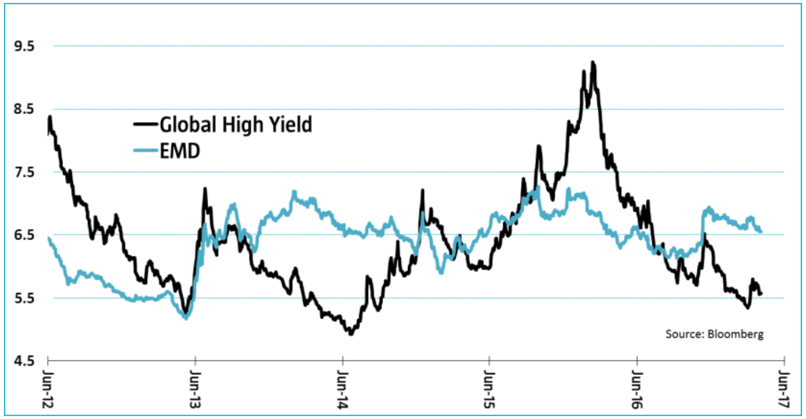
Emerging Market Debt (II)

South Africa - yield to maturity



Source: Bloomberg

Valuation



Source: Bloomberg

- Zuma had failed to reshuffle his cabinet on earlier occasions. The sudden increase in political tensions made Standard and Poor's lower the rating on South Africa's foreign currency debt to junk. This has not happened yet for local currency debt, but obviously the rating outlook has worsened for local debt as well. The attractive yield provides a buffer against recent events, although these are an obvious short-term negative.

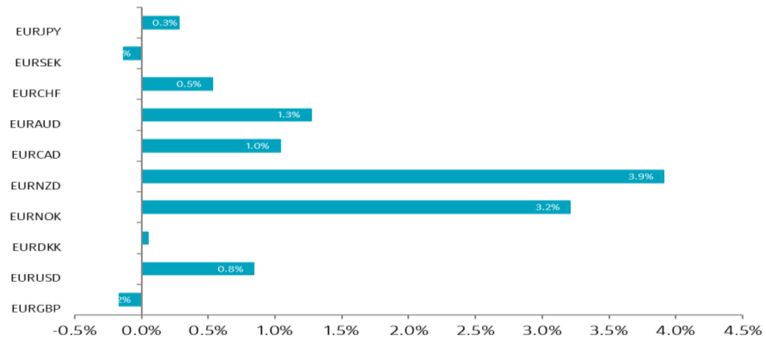
- Given the above, it's important that circumstances in Turkey have stabilized a bit. Turkey has shown, albeit reluctantly, a commitment to protect its currency. In addition, Turkey's economy grew much faster (3.5% YoY) than expected in the last quarter of 2016, offering more room to maneuver.

- Valuation of emerging debt is attractive, especially within the fixed income space. As the chart on the bottom left shows, the running yield is significantly higher than that of high yield bonds. Also, the risk/yield relationship looks attractive compared to government bonds.

- We stick to our overweight in emerging debt. Better economic conditions and the stabilization of emerging market currencies are positives. Also, the yield gap with other fixed income asset classes remains attractive. These factors outweigh inherent risks related to the asset class for now.

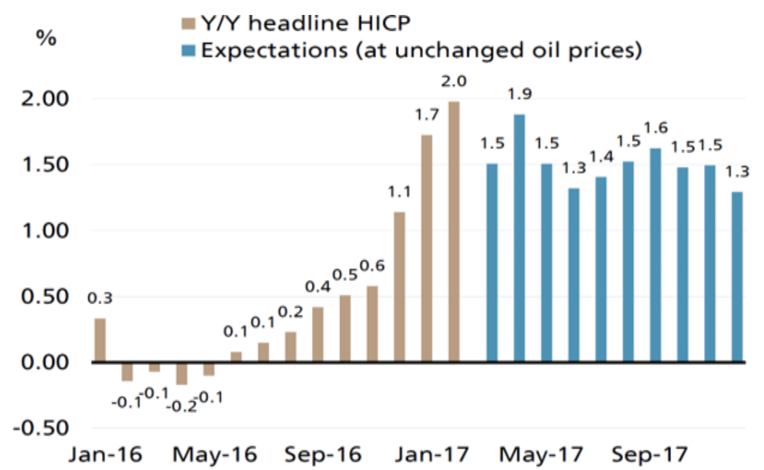
FX (I)

The euro is not the strongest, but still a pretty good performance in March



Source: Bloomberg

HICP projections for the euro area



Source: Bloomberg & UBS

- While the euro wasn't the strongest currency in March within the G-10, the euro only marginally underperformed two currencies, the Swedish krona and British pound.

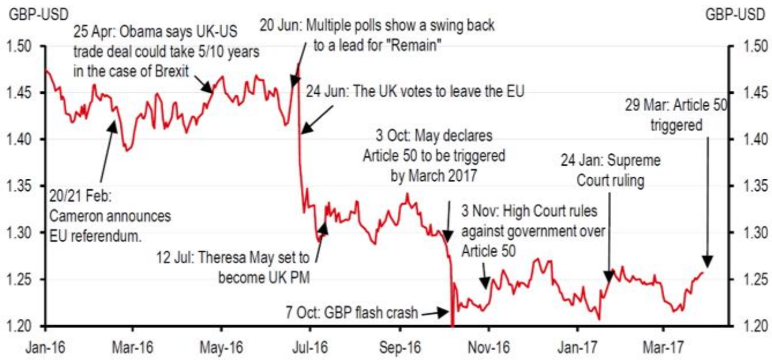
- So why the sudden turnaround in euro sentiment? Its not that we have already passed the peak of political uncertainty. While the outcome of the Dutch elections did bring some relief, we unfortunately still have the French and German elections ahead of us. We also remain focused on developments in Italy, as the situation remains fluid. What we are witnessing is a market that is starting to ponder whether the ECB might be closer to a policy change than was initially thought. While we are sympathetic to that thought (based on the recent data releases), we think the ECB currently has no incentive to adjust its policy, given the aforementioned political events.

- The latest inflation figure came in weaker, but this was expected. It was anticipated that energy base effects would start to become a drag. In addition to that, it is highly likely that we are also witnessing some seasonal noise due to the timing of Easter.

- The US Fed walked back expectations after it had led the market to believe that tighter policy was coming. This loss of rate support took his toll on the dollar as it weakened across the board after the March meeting.

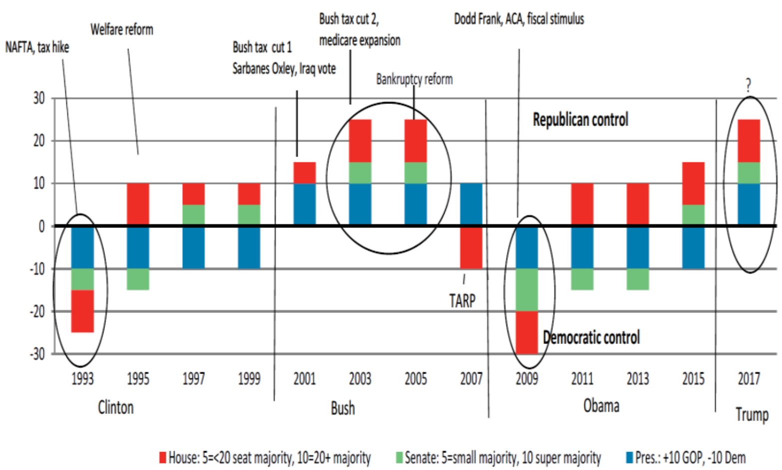
FX (II)

Sterling remains the ultimate gauge for sentiment around Brexit



Source: HSBC & Bloomberg

Control of the House, Senate and Presidency normally leads to major legislation



Source:Macrobond,Bloomberg & BNP

- Added to the woes of the dollar was the healthcare debacle, as 'the dealmaker' Trump failed to unite his Republican party to back the proposal. This isn't good for his Administration's credentials and for the Republicans in general. The question whether the Republican party is able to govern is one that is suddenly on everyone's mind. If they can't, Trump will not be able to keep his campaign promises. We don't have to wait too long to get a bit of clarity on this, as we are heading towards the budget approval process, something which has proven to be a pretty tedious process in the past couple of years. The stakes for the Republicans just got raised, so we will watch carefully to see if they are able to rise to the challenge.

- The UK finally sent the letter triggering Article 50. Now we can start to focus on the actual negotiation process. The initial indications we got from both sides confirmed that this will not be plain sailing. The red lines on both sides seem to be clear, so we will see who blinks first.

- A important lesson from Q1 is that it is essential to strike the correct balance between the importance of macroeconomic momentum on one side, and political/policy uncertainty on the other. For the US dollar we think that economic momentum still trumps politics. For both sterling and the euro, politics outweighs economics. We therefore stick to our current positioning where we prefer the US dollar to both the euro and sterling.

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