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CONTINUED GLOBAL ECONOMIC AND EQUITY REFLATION

Global Investment Committee Outlook

Global Growth Should Continue Firm

We believe that the G-3 and Chinese economies will perform strongly, in line with consensus expectations, while we expect central banks to reduce their accommodation similarly to consensus expectations. With such as the backdrop, we expect bond yields to rise mildly, the USD to be relatively flat and equity markets to rise quite a bit further.

It has certainly been a wild rise since we last met in mid-December, but **MSCI World has risen 3.5% through March 9th, less than we expected yet justifying our previous bullish stance**. The SPX has risen, but is lower than our March-end target, while TOPIX was flattish in USD terms and also well below our target. Elsewhere, MSCI Europe basically met our target in USD terms and the Hang Seng exceeded our bullish target. G-3 bond yields exceeded our targets for end-March, except for Japan, as we estimated only moderate increases. Our December forecast of a 0.7% decline in USD-based global bond returns through March is likely too low, as despite bond price weakness, the weak USD has pushed up the value of overseas bonds. Indeed, the Yen and Euro were much weaker than we expected.

As we predicted in December, G-3 economic has been even stronger than consensus, with the possible exception of Japan; however, our view that China would slow down significantly in the 1H18 might be too pessimistic. Looking forward, US GDP, at a 2.9% Half on Half Seasonally Adjusted Annualized Rate (HoH SAAR) in 2Q18-3Q18 and a 2.7% rate in 4Q18-1Q19, should match consensus expectations. Growth should come from increased personal consumption, fixed asset investment, government spending and inventories, while net trade will likely be a negative factor. Meanwhile, the Eurozone's and Japan's GDP will likely grow at 2.3% and 1.6%, respectively on a HoH SAAR basis in 2Q18-3Q18 and 2.1% and 1.8%, respectively, in 4Q18-1Q19, both approximating consensus expectations. These results should re-assure risk markets and corporate profit estimates should continue to show sturdy growth for CY18. Lastly, China's official GDP should be approximately 6.6% HoH SAAR in both periods. Here too, personal consumption will likely lead the way, while fiscal stimulus will continue to provide much less support.

As for geopolitical issues, we still believe, as have markets so far, that such will be handled without crisis due to the strong economic incentives of all major players, although the situations in North Korea and the Middle East remain at very dangerous levels.

Central Banks: Remaining Relatively Dovish Despite Reflation

We have cut our Fed call to three hikes in 2018, from four, and we expect a 1Q19 hike, as well. This approximates what fixed income markets and economists expect. The ECB and BOJ have remained very dovish and due to the weaker USD and, thus, lower inflation expectations outside the US, we also soften our ECB call and now expect it to end QE in December, with rate hikes starting in 2Q19. Meanwhile, we expect the BOJ to maintain its 10-year JGB target until a 1Q19 hike of 10 bps, with no tapering of its ETF purchases until 2019. As for inflation, we expect the US Core CPI to be 2.1% YoY in September, and as we expect the Brent oil price to be $68 then, we expect the headline CPI to be 2.6% YoY. Overall commodity prices should also move mildly upward, as global growth should keep global commodity demand quite firm, thus more than offsetting the effect of higher interest rates.

Flat USD and Mildly Rising G-3 Bond Yields

Given our scenario, we expect G-3 bond yields to continue rising gradually in the next few quarters. For US 10Y Treasuries, our target for June-end is 2.95%, while those for 10Y JGBs and German Bunds are 0.05% and 0.75%, respectively. In December, we expect 3.05%, 0.10% and 0.85%, respectively. This implies (coupled with our forex targets) that including coupon income, the Citigroup WGBI (index of global bonds) should produce a 0.2% unannualized return from our base date of March 9th through June in USD terms, and -0.2% through December 2018. Thus, we continue to **maintain an unenthusiastic stance on global bonds for USD-based investors**. The WGBI index in Yen terms should mirror these returns and as for JGBs, we target the 10Y to have a 0.1% total unannualized return in Yen terms through March, and -0.4% through December 2018.

Regarding forex, Fed policy will tighten faster than BOJ policy, but global worries about severe US trade and budget deficits should restrain USD enthusiasm, so we expect the Yen and Euro to be basically flat for the rest of 2018.

Still Positive on Global Equities

Our new scenario continues to be bullish on equities (as it has for nearly the entire period since the Global Financial Crisis), as economic growth should propel earnings growth, while rising interest rates should not curtail valuations much. Aggregating our national forecasts from our base date of March 9th, we forecast that the MSCI World Total Return Index will increase 3.2% (unannualized) through June in USD terms, 5.9% through September and 8.4% through December 2018. **Clearly, this suggests a positive stance on global equities for USD-based investors (and Yen-based investors, as well)**. Of course, there always remain worries about the withdrawal of QE and geopolitical risk, but we believe such will be overcome.

In the US, strong economic growth, both domestic and foreign, coupled with deregulation and accelerated share buybacks (due to the tax break on the repatriation of foreign profits) should easily offset the headwinds from mildly higher interest rates, such that the equity backdrop is strong, especially as CY18 earnings should be particularly strong. Previously, because the tax cuts were not fully approved or understood, analysts had not fully adjusted their EPS forecasts for such, and many waited for corporate guidance in the new year, but they did so in January with great enthusiasm. We had long stated that this was a major anomaly that made the market much less expensive than it appeared. Computer models concentrating on earnings momentum were also enthused by these earnings upgrades, which likely added to the market fervor in January. The SPX EPS estimate for 2018 is now an accurate representation of true expectations and the PER based on such is at a fairly reasonable 17.8 times. Given all of this, we expect the SPX to hit 2833 (2.2% total unannualized return from our base date) at end-June, 2893 at end-September (4.9% return) and 2954 at year-end (7.5% return), which is not far from our target made in mid-December.

European equities also look quite promising to us. Some European macro economic data is showing signs of deceleration from heady growth, but GDP should remain solid, especially by its mature-country standard. Continued low interest rates and strong earnings growth from global economic growth (although hurt a bit by the recently higher EUR) should help its equity market. The European PER on 2018 EPS is quite reasonable and will likely rise somewhat, so we see the Euro Stoxx rising to 395 and the FTSE to 7480 at end-June, and to 407 and 7700 through December, which translates to 5.1 and 8.9% unannualized MSCI Europe returns in USD terms for those periods. Consumer confidence has risen and fears of a banking crisis have nearly completely disappeared, but BREXIT will remain a moderate headwind. Meanwhile, the effect of the recent Italian election is too difficult to gauge yet, but certainly adds some uncertainty. Notably, mildly rising commodity prices, to which UK and European corporations are highly geared via multinational companies, should also boost corporate earnings.

In our last reporting period, Japanese equities were weak in Yen terms, but quite flat in USD terms. Part of this was due fear of the strong Yen, even as 4QCY aggregate earnings surged far above consensus. Japan has high operational gearing to strong global economic growth and corporate governance continues to improve (despite a few hiccups), so we expect TOPIX at end-June to be 1780, with 1867 through December for a total return of 4.3% and 10.4% in USD terms, respectively (virtually the same in Yen terms, as well). The currently low equity valuations, at 14.2 times CY18 EPS, are a major factor in our positive outlook.

As for the Developed Pacific-ex Japan region, we expect Hong Kong and Australian equities to perform very well, leading to a 4.0% unannualized return in USD terms through June and 13.6% through December. Strong global growth, reasonable equity valuations, decent earnings growth and continued low global interest rates all play major roles in these returns.

Lastly, besides all the geopolitical risks, protectionist actions by the US will need to be watched very carefully. Of course, neither Trump nor Chinese officials wish to cause a crisis, and will attempt to avoid such as they have done so far, but emotions are running high and accidents could occur.

Investment Strategy Concluding View

There is no doubt that geopolitical tail risks remain quite large, but the Global Investment Committee remains upbeat because the net impulses for global economic growth and corporate profits continue to improve. Thus, similar to our meetings of the last year, this justifies **a very positive stance on global equities**, particularly within Europe and the Asia Pacific. Meanwhile, global bond yields should rise somewhat, so we **maintain an unenthusiastic stance on global bond returns**.

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