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Markets

INVESTMENT COMMITTEE MINUTES

12 November 2020

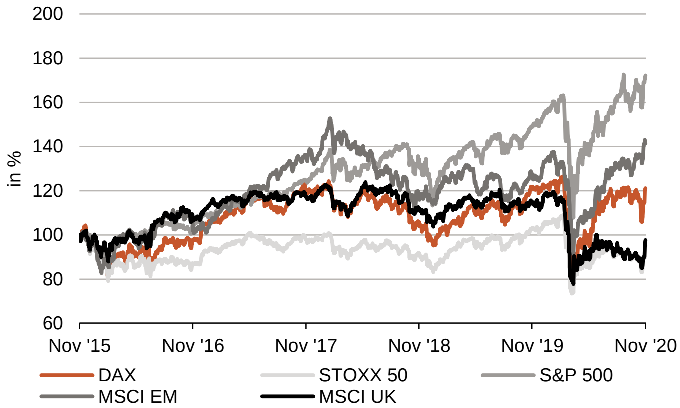
Managers of the Committee

Prof Dr Bernd Meyer
Chief Investment Strategist
Chairman

Dr Holger Schmieding
Chief Economist,
Vice Chairman

The **Committee Members** are listed in the notes.

Development of selected equity indices



Source: Bloomberg, 11/11/2015 - 11/11/2020.

Most important assessments at a glance

Economics	• Bleak pandemic autumn in Europe – but the outlook for 2021 has improved further thanks to Biden's election victory • US after the election: calmer foreign and trade policy is good for the world; a moderate swing to the left domestically • Strong growth in 2021 in large parts of the world with low inflation, monetary and fiscal policy will support the economy
Equities	• The tough October was followed by a strong start in November. Positive vaccine news and the US election drove stocks • Investors are positioning themselves increasingly cyclically. Value stocks and cyclical stocks recovered significantly • We remain positive with a significant overweight in equities and a more cyclical bias
Bonds	• Successes in vaccine development are reducing demand for government bonds. Yields rose significantly • USD and EUR high-yield bonds benefited the most from investors' increased risk appetite • We underweight bonds, divest US Treasuries and focus on credit risks with shorter duration
Commodities	• Gold fell with increased risk appetite. Negative real interest rates and a weak dollar should give a boost again • Crude oil initially weakened considerably, but recently jumped in price thanks to vaccine news. More potential available • Base metals are benefiting from the more climate-friendly US policy and the positive economic trend
Currencies	• The outcome of the US election – President Joe Biden, split Congress – argues for a moderately weaker USD • Renewed, apparently more serious, talks on a Brexit follow-up agreement are giving the GBP a boost • CHF remains in demand as a safe haven. If the appetite for risk increases, the franc will weaken at least slightly

Current market commentary

The market-friendly outcome of the US elections and then the positive COVID-19 vaccine news made investors look for risk again. Both events led to a decrease in uncertainty and volatility. Share prices rose significantly. In the last four weeks, most markets recorded a slight gain despite a tough October and especially since the beginning of November, they have been rising steeply. However, there were winners and losers in the rally. Regionally, European equities in particular gained over 14% in November. In terms of investment styles, there was a rotation from growth to value stocks and from defensive to cyclical stocks. Over the last four weeks, European cyclicals and value stocks have gained over 6%, while growth and defensive stocks have gained less than 3%. Looking ahead, we remain positive. Expansive central bank and fiscal policies, less political uncertainty with Joe Biden as US president and an imminent end to the Brexit drama, high cash ratios of investors, successes in vaccine development and thus a .

sustained economic recovery should continue to support equity markets. With the end of the Brexit drama, UK stocks should also continue to recover. We have therefore further increased our equity overweight by reducing our UK underweight and have also taken a slightly more cyclical approach.

On the bond side, safe haven government bonds were less in demand, while corporate bonds enjoyed a significant fall in spreads. Yields on US government bonds have recently risen to close to 1% and German government bonds are close to -0.5%. In contrast, spreads on USD high-yield bonds have fallen by almost 50bp. We have reduced our position in US government bonds as safe have government bonds are likely to remain under pressure, at least temporarily.

Gold has also been less in demand recently, while crude oil has recovered significantly thanks to its cyclical nature.

ECONOMICS

Despite the second wave of the pandemic, the outlook for 2021 has brightened

Strong recovery of the global economy in 2021 after the mega-recession in 2020
Calm trade policy thanks to Biden instead of constant threats under Trump: good prospects for world trade
Second wave of the pandemic hits the Northern Hemisphere – but risks are smaller and more assessable than in March

- **Upswing without inflation:** After the sharp recession in March and April, the lights for the global economy are green for 2021. The early phase of a new upswing is characterised by strong growth, with inflation still very low at first. Monetary and fiscal policy is giving a stronger boost to the economy on both sides of the Atlantic than ever before. Thanks to its own credit stimuli, China remains robust for the time being, despite considerable long-term risks. Strong growth in key consumer countries with low interest rates is also positive for many emerging markets.
- **Severe setback in Europe:** With the cool and dark season, sars-CoV-2 infections in Europe have increased so much that almost all countries have had to cut back on economic activity again. Germany is getting off rather lightly. But in countries such as France, Belgium and the UK, where a large part of the retail sector also had to close down in November, economic output will decline significantly in Q4. However, the setback will be far less severe than in March: the measures are more targeted and will not come as a shock. Instead of interrupted supply chains, the situation in industry is now characterised by strong demand from the US and China.
- **Hope for Christmas – and spring:** In some European countries, the virus situation is stabilizing – see graph. This supports the hope that some restrictions can be relaxed before Christmas. At the latest in spring, when the weather will be warmer and thanks to medical progress, the situation should ease. In Q3, the eurozone has been able to make up almost all the losses from Q2 2020. This suggests that the economy can also recover strongly in spring.
- **Hello Joe:** The winner of the US election stands for a calm foreign and trade policy; Biden will strengthen rather than weaken NATO, the World Trade Organization and the EU and its rules. This is positive for world trade. Even if he also wants to protect US jobs, he is likely to want to join forces with the EU to tackle China rather than threaten and attack in all directions. The trump risk of a real US-EU trade war is likely to be off the table.
- **US Senate in limbo:** Biden, as President, will regulate the labour market and some other parts of the US economy more strictly. This may harm some sectors and especially small businesses. Whether the Democrats can also win a majority in the Senate and thus raise taxes depends on the outcome of two run-off elections on 5 January.

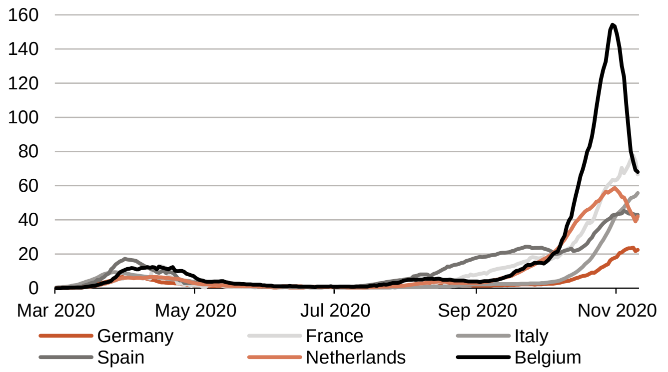
No inflation, low interest rates: In the short term, inflation will fall as demand remains weak. Over the next three to five years, inflation may increase slightly. The US Federal Reserve will allow this. It wants to compensate for the current low inflation by a rate of just over 2% later. This is initially positive for the economy and markets.

GDP and inflation forecasts (%)

		GDP growth			Inflation		
	%	2019	2020	2021	2019	2020	2021
World	100.0	2.3	-3.3	4.0			
US	24.2	2.2	-3.5	3.9	1.8	1.2	1.9
China	15.8	6.2	2.7	9.0	2.9	3.0	2.2
Japan	5.9	0.7	-5.8	3.0	0.5	0.1	0.3
India	3.2	5.0	-2.5	3.5			
Latin America	6.2	1.5	-6.0	3.5			
Europe	25.7	1.2	-7.5	4.9			
Eurozone	16.1	1.3	-7.4	5.0	1.2	0.3	0.8
Germany	4.7	0.6	-5.5	4.3	1.4	0.5	1.5
France	3.3	1.5	-9.5	6.7	1.3	0.4	0.7
Italy	2.4	0.3	-9.1	6.0	0.6	-0.2	0.5
Spain	1.7	2.0	-12.0	7.1	0.8	-0.4	0.5
Rest of western Europe							
UK	3.3	1.3	-11.8	6.4	1.8	0.8	1.1
Switzerland	0.8	0.8	-5.7	4.3	0.6	0.0	0.6
Sweden	0.7	1.3	-6.0	5.0	1.8	0.9	1.3
Eastern Europe							
Russia	1.9	1.0	-5.0	3.5	4.5	2.0	3.0
Turkey	0.9	-1.2	-6.0	3.5	15.2	9.0	8.5

Source: Berenberg

COVID-19 in Europe: new infections



01 March - 10 November 2020. New infections per day, per 100,000 inhabitants; seven-day averages. Source: Johns Hopkins University

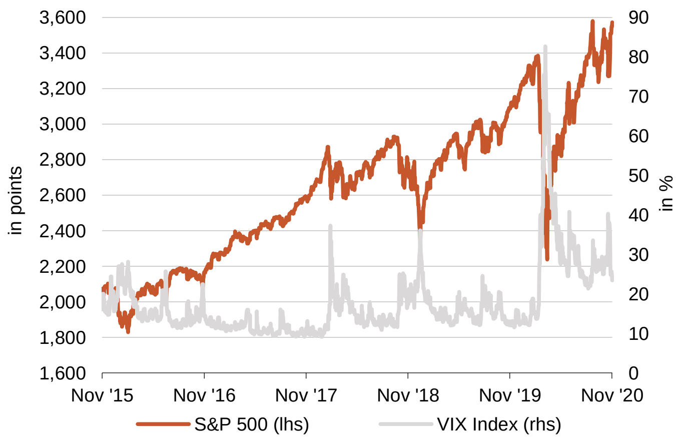
EQUITIES

Increasing cyclical tailwind

The tough October was followed by a strong start in November. Positive vaccine news and the US election drove stocks
Investors are positioning themselves increasingly cyclically. Value stocks and cyclical stocks recovered significantly
We remain positive with a significant overweight in equities and a more cyclical bias

- **The outcome of the US presidential election and positive vaccine news gave a boost to the stock markets.** Both events reduced uncertainty and thus significantly reduced volatility in the markets. Since the beginning of the month, most stock markets have been clearly up. The European market, which is rather cyclical and strongly affected by COVID-19, benefited disproportionately from the vaccine news. In the last four weeks, European and US equities have also made slight gains despite a tough October. This was supported by a markedly better than feared Q3 reporting season in both regions.
- The recent strong market development was accompanied by a rotation from **growth** to **value stocks.** While growth remained in high demand after the US elections, investors increased their value exposure at the latest after the positive vaccine news. In the last four weeks, European **value stocks** have thus outperformed the market by around 6%. The situation is similar for **cyclical** versus **defensive stocks** with a difference of more than 3%. On a sector level in Europe, financial and energy stocks have performed well with returns above 13%. In contrast, **European small caps** underperformed **large caps** by around 2%.
- Expansive central bank and fiscal policy, less political uncertainty thanks to US elections and an imminent end to the Brexit drama, high liquidity holdings by investors, successes in vaccine development and, as a result, a sustained economic recovery are all factors that make us optimistic about the performance of equity markets into 2021.
- We are positioning with a **significant equity overweight, reducing our UK underweight** and **becoming even more cyclical**.

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 11/11/2015 - 11/11/2020.

Overview of equity markets (short/medium term)

Regions	Old	New
US	↗	↗
Europe	↗	↗
Emerging markets	↗	↗
Japan	→	→

		Performance in local currency				
	As of 11/11/2020	ytd	1-year	3-year	P/E	Dividend yield
DAX	13,216	-0.2%	+0.1%	+0.7%	19.3	2.7%
SMI	10,532	+2.5%	+5.6%	+27.3%	20.1	3.0%
MSCI UK	1,795	-14.3%	-11.5%	-5.6%	13.9	3.6%
EURO STOXX 50	3,467	-5.0%	-3.6%	+6.4%	22.3	2.7%
STOXX EUROPE 50	7,305	-6.9%	-4.9%	+6.7%	16.9	3.2%
S&P 500	3,573	+12.3%	+17.9%	+46.6%	25.7	1.7%
MSCI Em. Markets	1,179	+8.1%	+14.8%	+13.4%	18.5	2.4%

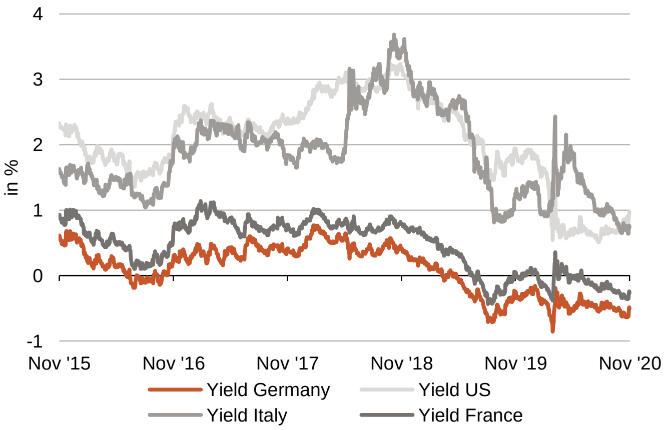
BONDS

Risk appetite on the rise

Successes in vaccine development are reducing demand for government bonds. Yields rose significantly
USD and EUR high yield bonds benefited the most from investors' increased risk appetite
We underweight bonds, divest US Treasuries and focus on credit risks with shorter duration

- The trend of falling yields on **European government bonds** appears to have been broken for the time being. In the last four weeks, **German** and **French** as well as **Italian government bonds** have experienced rising yields. The success of the COVID-19 vaccine development is causing investors to look for more risk, despite high infection rates. Safe haven government bonds were therefore less in demand. The yield on 10-year **German government bonds** rose to over -0.50%.
- Yields on 10-year **US government bonds** have risen significantly over the past four weeks. Increased risk appetite and a future US government with the Democrats are causing demand for Treasuries to fall. Government spending should continue to rise in the future under the new government, which could lead to rising inflation expectations. Treasuries have seen yields widen by 25bp in the last four weeks and most recently yielded 0.98%.
- Spreads on **corporate bonds** have fallen significantly over the past four weeks thanks to increased risk appetite. High-risk investments in particular have benefited from this. **USD high-yield bonds** had the relatively largest spread tightening at over 45bp, compared to almost 40bp for **EUR high-yield bonds. IG corporate bonds** only had a low double-digit spread tightening. For **emerging market hard currency bonds,** we prefer government bonds over corporate bonds.
- **We clearly underweight bonds and are divesting US government bonds.** We maintain our focus on corporate and emerging market bonds at the expense of government bonds and keep maturities comparatively short.

Yields on 10-year government bonds



Source: Bloomberg, 11/11/2015 - 11/11/2020.

Overview of bond markets (short/medium term)

Orientation	Old	New
Duration	Moderate	Short
Government bonds	↘	↘
Corporate bonds	↗	↗
High-yield bonds	↗	↗
Emerging market bonds	↗	↗

Yields (10-year)	Old	New
Germany	↗	↗
UK	↗	↗
US	↗	↗

	As of 11/11/2020	Performance in index currency ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	261.40	+4.2%	+3.7%	+12.0%
Covered bonds (iBOXX Euro Germany Covered)	206.99	+1.6%	+1.2%	+4.3%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	162.47	+2.1%	+2.2%	+6.8%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	160.70	+1.7%	+1.9%	+5.4%
Emerging market bonds (Bloomberg Barclays EM USD Aggregate TR Index Unhedged)	1,255.38	+3.8%	+5.9%	+15.8%
High-yield bonds (Bloomberg Barclays Global High Yield Total Return Index, USD)	1,454.09	+2.8%	+5.5%	+12.6%

COMMODITIES

Crude oil benefits from its cyclical nature

Gold was not in demand in the risk on environment
Oil price with tailwind from several sides
Industrial metals back on the path to strength

- **Gold** was able to break out briefly in the aftermath of the US elections thanks to a weak US dollar, only to fall back below USD1,900 an ounce as investors' risk appetite increased due to positive vaccine news. However, high national debt, negative real interest rates, rising inflation and a weak dollar continue to speak in favour of the precious metal.
- **Crude oil** (Brent) fell at times to as low as USD36 per barrel in October. While demand concerns spread in Europe, Libya announced that it would significantly increase its oil production. With the US election and the vaccine news, oil was then able to rise above the USD40 mark again. As the economic recovery continues, oil should continue to benefit.
- **Industrial metals** have continued to gain recently. With Joe Biden and his more climate-friendly policies, industrial metals should continue to be well supported.

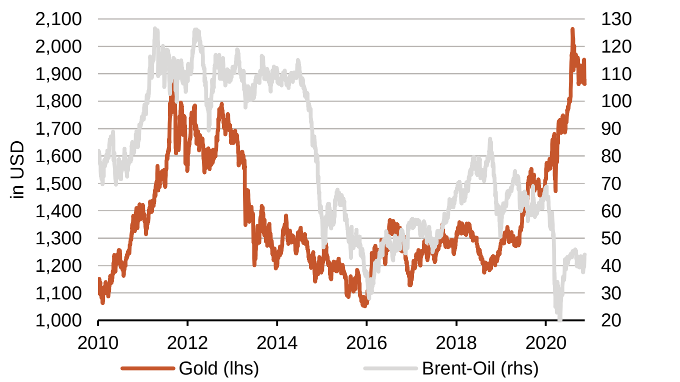
CURRENCIES

Turbulent days for the USD

EUR/USD on an orientation course after US election
GBP benefits from new Brexit talks
Swiss franc loses because of vaccine news

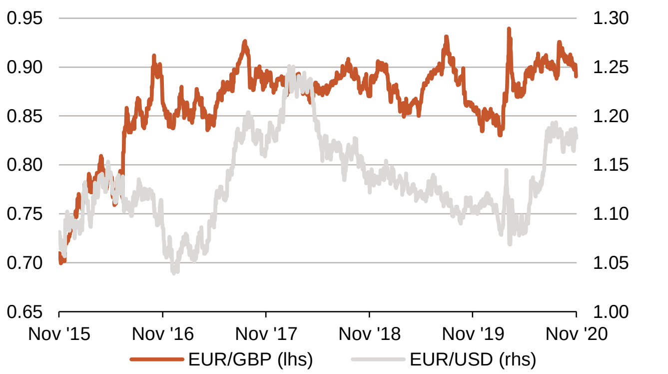
- **EUR/USD:** The presidential election has led to a roller-coaster ride in the EUR/USD exchange rate. The prospect of four more years of Trump briefly led to uncertainty and corresponding strength of the dollar. With Joe Biden's election victory, the euro then appreciated. After the strong swings, the exchange rate is now back at USD1.18 to the EUR. The election results confirm our forecast of an even weaker dollar.
- **EUR/GBP:** The GBP benefits from renewed talks on a Brexit connection agreement. As a result, the EUR falls to GBP0.89 per EUR for the first time since the beginning of September.
- The notification of a vaccine increases the risk appetite. The **Swiss franc** immediately weakens, but remains very strong at 1.08 francs to the EUR.

Price development



Source: Bloomberg, 01/01/2010 - 11/11/2020.

Exchange rates



Source: Bloomberg, 11/11/2015 - 11/11/2020.

Overview of commodities (short/medium term)	Old	New
Gold	↗	↗
Oil (Brent)	↗	↗

Overview of currencies (short/medium term)	Old	New
EUR/USD | Euro/US dollar	↗	↗
EUR/CHF | Euro/Swiss franc	↗	↗
EUR/GBP | Euro/Sterling	→	→
EUR/JPY | Euro/Japanese yen	↗	↗

		Performance		
	As of 11/11/2020	ytd	1-year	3-year
Gold USD/ounce	1,866	+23.0%	+28.2%	+46.3%
Silver USD/ounce	24.3	+36.0%	+44.0%	+43.8%
Copper USD/pound	313.4	+12.0%	+17.6%	+1.9%
Brent USD/bbl	43.80	-33.6%	-29.6%	-31.0%

		Performance		
	As of 11/11/2020	ytd	1-year	3-year
EUR/USD	1.18	+5.0%	+6.7%	+1.0%
EUR/CHF	1.08	-0.5%	-1.4%	-7.0%
EUR/GBP	0.89	+5.3%	+3.8%	+0.7%
EUR/JPY	124.17	+2.0%	+3.2%	-6.2%

IMPORTANT NOTES

Members of the Investment Committee

Prof Dr Bernd Meyer | Chief Investment Strategist, Chairman
Dr Holger Schmieding | Chief Economist, Vice-Chairman
Matthias Born | Head Portfolio Management Equities, European Equities
Ulrich Urbahn | Head Multi Asset Strategy & Research
Oliver Brunner | Co-Head Portfolio Management Multi Asset
Ansgar Nolte | Co-Head Portfolio Management Multi Asset
Marco Höchst | Equities
Till Budelmann | US Equities
Daniel Fuchs | Bonds
Alexander Pichler | Bonds
Ludwig Kemper | Commodities
Karsten Schneider | Multi Asset Strategist, Minutes

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