Current market commentary

Recently, the recovery in stock markets has persisted, boosted by the ECB's and Fed's easing measures. A conciliatory tone in the trade dispute has also contributed to this. However, the economic data continues to be mixed. In China, they remained weak, while the US economy still appears robust. Analysts have reduced their earnings estimates, despite momentum slowing. As a result, stock market valuations have risen. US equities are now valued again at a P/E ratio of 18.2 - as in January and September 2018. Below the surface, the market is vulnerable. Momentum stocks suffered, while value stocks were able to make strong gains. Will the stock markets be able to leave the volatile sideways channel upwards? This is likely to be determined by the upcoming economic data, the Q3 reporting season, and the continuation of the trade dispute. So far, we do not believe that the signals from these directions are sufficient.

Short-term outlook

Due to the expansionary monetary policy of the central banks, the (trade) political risks and economic data have recently receded into the background. Many stock indices have recently approached their highs of July, but a sustained upward breakout has not yet been achieved.

Tomorrow, Tuesday, the German ifo business climate and US consumer confidence index will provide information about further economic development. On Friday, the incomes and expenditures of private US households as well as incoming orders for durable goods in the US will provide an insight into how robust the US economy is holding up. Next week, the Q3 reporting season will pick up speed and the focus should be more on the corporate sector. However, this will most likely only be the case until the beginning of October when trade talks between the US and China will continue. Investors' expectations of a "deal" in the coming months are high. The trade war will continue to have a strong impact on the markets.

There has been a rotation into value stocks, thanks to rising yields

Recently, value stocks outperformed growth companies. Rising yields and one-sided positioning (strong value underweight of most market participants) helped. In the short term, the rotation could continue if macro data improves.

However, the picture has looked different in recent years: growth has clearly beaten value. High, stable earnings growth remains rare in a low growth environment and is rewarded by investors. In the medium term, growth should continue to outperform accordingly.

Source: Bloomberg, Time period: 20/09/2014 - 20/09/2019
### Multi Asset

#### 4-week & YTD

<table>
<thead>
<tr>
<th>Category</th>
<th>YTD (31/12/18 - 20/09/19)</th>
<th>12-month periods over that last 5 years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brent</td>
<td>-2.8</td>
<td>-18.2 - 52.3 - 18.2 - 52.6</td>
</tr>
<tr>
<td>MSCI Emerging Markets</td>
<td>4.1</td>
<td>23.0 - 12.3 - 12.4 - 23.0</td>
</tr>
<tr>
<td>MSCI World</td>
<td>8.3</td>
<td>6.3 - 23.2 - 6.3 - 23.2</td>
</tr>
<tr>
<td>REITs</td>
<td>2.5</td>
<td>15.9 - 2.5 - 15.9 - 2.5</td>
</tr>
<tr>
<td>Global Convertibles</td>
<td>0.1</td>
<td>4.1 - 0.1 - 4.1 - 0.1</td>
</tr>
<tr>
<td>USD/EUR</td>
<td>-0.3</td>
<td>-9.9 - -0.3 - -9.9 - -0.3</td>
</tr>
<tr>
<td>Gold</td>
<td>0.9</td>
<td>13.8 - 0.9 - 13.8 - 0.9</td>
</tr>
<tr>
<td>Global Corporates</td>
<td>0.0</td>
<td>0.0 - 0.0 - 0.0 - 0.0</td>
</tr>
<tr>
<td>Eonia</td>
<td>-0.1</td>
<td>-3.5 - -0.1 - -3.5 - -0.1</td>
</tr>
<tr>
<td>Global Treasuries</td>
<td>0.0</td>
<td>-0.1 - 0.0 - -0.1 - 0.0</td>
</tr>
<tr>
<td>MSCI Frontier Markets</td>
<td>-2.9</td>
<td>-13.8 - -2.9 - -13.8 - -2.9</td>
</tr>
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</table>

### Equities

#### 4-week & YTD

<table>
<thead>
<tr>
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<th>YTD (31/12/18 - 20/09/19)</th>
<th>12-month periods over that last 5 years</th>
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</thead>
<tbody>
<tr>
<td>Stoxx Europe Cyclicals</td>
<td>17.3</td>
<td>-1.4 - 2.2 - 25.5 - 3.9 - 0.0</td>
</tr>
<tr>
<td>Russell 2000</td>
<td>21.5</td>
<td>-1.7 - 23.0 - 11.0 - 9.2 - 16.0</td>
</tr>
<tr>
<td>DAX</td>
<td>18.1</td>
<td>1.1 - 1.9 - 20.9 - 4.8 - 1.2</td>
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<tr>
<td>MSCI EM Eastern Europe</td>
<td>25.0</td>
<td>7.0 - 5.5 - 19.8 - 8.4 - 14.8</td>
</tr>
<tr>
<td>Euro Stoxx 50</td>
<td>21.9</td>
<td>7.0 - 0.9 - 22.0 - 3.3 - 1.0</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>26.0</td>
<td>11.3 - 21.6 - 11.3 - 13.7 - 12.2</td>
</tr>
<tr>
<td>Topix</td>
<td>16.7</td>
<td>3.1 - 10.7 - 9.9 - 10.4 - 14.8</td>
</tr>
<tr>
<td>MSCI EM Asia</td>
<td>12.5</td>
<td>5.4 - 0.4 - 18.9 - 13.6 - 1.4</td>
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<tr>
<td>Stoxx Europe 50</td>
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<td>9.9 - 1.1 - 13.4 - 2.8 - 0.3</td>
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<tr>
<td>Stoxx Europe Small 200</td>
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<td>1.6 - 6.2 - 19.2 - 0.3 - 1.2</td>
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<tr>
<td>Stoxx Europe Defensive</td>
<td>17.1</td>
<td>11.6 - 4.4 - 6.5 - 1.3 - 2.5</td>
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</table>

### Fixed Income

#### 4-week & YTD

<table>
<thead>
<tr>
<th>Category</th>
<th>YTD (31/12/18 - 20/09/19)</th>
<th>12-month periods over that last 5 years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gilts</td>
<td>12.5</td>
<td>13.7 - 0.1 - 6.0 - 3.7 - 17.5</td>
</tr>
<tr>
<td>BTPs</td>
<td>13.3</td>
<td>15.1 - 2.1 - 2.8 - 5.8 - 5.5</td>
</tr>
<tr>
<td>USD High Yield</td>
<td>12.8</td>
<td>14.7 - 5.2 - 1.1 - 9.3 - 10.3</td>
</tr>
<tr>
<td>EM Local Currency Bonds</td>
<td>9.8</td>
<td>17.2 - 4.5 - 0.7 - 13.6 - 3.7</td>
</tr>
<tr>
<td>EUR High Yield</td>
<td>8.2</td>
<td>4.2 - 0.7 - 6.4 - 4.8 - 0.5</td>
</tr>
<tr>
<td>USD Corporates</td>
<td>16.7</td>
<td>20.2 - 0.8 - 4.6 - 9.1 - 14.8</td>
</tr>
<tr>
<td>EUR Inflation Linkers</td>
<td>8.6</td>
<td>7.1 - 1.4 - 0.6 - 5.1 - 0.0</td>
</tr>
<tr>
<td>EM Hard Currency Bonds</td>
<td>11.2</td>
<td>7.9 - 5.4 - 3.1 - 10.4 - 1.1</td>
</tr>
<tr>
<td>Treasuries</td>
<td>-0.5</td>
<td>17.5 - 0.1 - 7.8 - 5.9 - 17.1</td>
</tr>
<tr>
<td>EUR Financials</td>
<td>5.9</td>
<td>5.5 - 0.2 - 2.0 - 5.3 - 0.7</td>
</tr>
<tr>
<td>EUR Non-Financials</td>
<td>6.8</td>
<td>6.1 - 0.0 - 0.1 - 7.0 - 0.1</td>
</tr>
<tr>
<td>Bunds</td>
<td>5.9</td>
<td>7.7 - 0.5 - 3.0 - 5.9 - 3.8</td>
</tr>
</tbody>
</table>

### Performance

- Over the last four weeks, most asset classes have risen. Brent oil performed best, followed by emerging markets equities. Oil benefited from the shortage of Saudi oil due to the drone attack.
- Global government bonds on the other hand, lost value due to rising bond yields.
- Cyclical equities have recently performed significantly better than their defensive counterparts. This outperformance was triggered by rising bond yields and a one-sided positioning of market participants who have avoided cyclical equities in recent months.
- German equities were also among the outperformers, while EM Asian equities underperformed.
- The new Italian government and the ECB’s loosening measures, including interest rate cuts, helped Italian bonds above all. They rose by 2.7 percent in the last four weeks.
- German government bonds lost value. Demand for safe havens recently declined, boosted by easing tendencies in the trade conflict.

Total return of selected asset classes, in euros and in percent, sorted by 4-week performance.
Source: Bloomberg, Time period: 19/09/2014 - 20/09/2019

Total return of selected equity indices, in euros and in percent, sorted by 4-week performance.
Source: Bloomberg, Time period: 19/09/2014 - 20/09/2019

Total return of selected fixed income indices, in euros and in percent, sorted by 4-week performance.
Source: Bloomberg, Time period: 19/09/2014 - 20/09/2019
Non-Commercial Positioning

- Speculative investors have recently significantly reduced their short positions in US bonds. Rising yields weighed on the pronounced positioning.
- Hedge funds are currently the most optimistic for precious metals and RUB, while they are the most pessimistic for the Eurozone and the USA.

Put-Call Ratio

- Put call ratios have fluctuated sharply recently. After the strong stock market recovery, hedging ratios for the Eurozone and the USA were increased again.

ETF Flows

- While money market ETFs recorded strong outflows, the picture for equities was mixed. US equities were in demand in the last two weeks, while European equity ETFs were sold.
- Emerging market ETFs saw neither strong inflows nor outflows.

Estimated ETF flows in percent of assets under management, sorted by 2-week average.
Source: Bloomberg, Time period: 31/12/2018 - 20/09/2019
**AII Sentiment Survey (Bulls vs Bears)**

- Confidence among investors has recently increased thanks to conciliatory words in the trade dispute and central bank easing measures. 35% of US private investors are now optimistic for the next six months, while 28% are pessimistic.

The sentiment survey conducted by the American Association of Individual Investors determines the percentage of private investors who are optimistic, pessimistic or neutral regarding the US equity market outlook for the upcoming six months. It has been carried out since 1987. The survey is conducted from Thursday to Wednesday and the results are published every Thursday. For the stock market, it tends to be supportive when there is a high proportion of bears and a low proportion of bulls. However, it is a negative indicator when there are significantly more optimists than pessimists.

Source: Bloomberg, AII, Time period: 21/07/87 - 20/09/19

**Realised Volatilities**

- In the wake of the drone attacks on Saudi Arabia’s oil production, the fluctuation range for commodities has risen sharply. No other asset class shows such a high volatility and is significantly above its 5-year average.

- EUR high yield bonds, on the other hand, show the lowest volatility, followed by EUR corporate bonds.

Realised volatility (in percent) measures the historical range of variation of a time series and is defined here as the standard deviation of the daily returns over the last 60 trading days. Volatility is often used as a measure of risk.

Source: Bloomberg, Time period: 20/09/2014 - 20/09/2019

**Implied Volatilities**

- The implied volatilities for government bonds and equities have fallen recently, thanks to the central banks’ easing measures.

- Currency volatility, on the other hand, has increased, while oil volatility has shot through the roof.

The price of options depends on the volatility of the underling instrument. Implied volatility can therefore be interpreted as a measure of the currently expected fluctuation range of the underling compared to the market over the remaining term of the option. It is a measure of prevailing uncertainty in the financial markets.

Stocks = VIX Index, Oil = OVX Index, Government Bonds = MOVE Index, Currencies = CVIX Index

Source: Bloomberg, Time period: 01/01/2014 - 20/09/2019
Global

- Global and G10 economic surprises have recently turned positive for the first time in 2019. Predominantly good US economic data in particular contributed to this.
- The economic surprise index for emerging markets also improved, even though China recently disappointed. Retail sales and industrial production in August were below expectations.

See explanations below.
Source: Bloomberg, Time period: 01/01/2014 - 20/09/2019

Eurozone and US

- The economic strength of the USA continues. Consumer sentiment measured by the preliminary University of Michigan Index, retail sales and industrial production in August were better than expected.
- The eurozone is also showing some better data. The ZEW Index in Germany for economic expectations improved significantly in September. However, industrial production in France and Italy was disappointing in July.

See explanations below.
Source: Bloomberg, Time period: 01/01/2014 - 20/08/2019

UK and Japan

- Economic surprises in the UK have recently fought their way into the positive area. Industrial production in July was better than expected, while retail sales in August were disappointing.
- Japan continues to impress with positive economic surprises.

See explanations below.
Source: Bloomberg, Time period: 01/01/2014 - 20/09/2019

Citigroup Economic Surprise Indices are defined as weighted historical, normalized data surprises (actual releases vs. Bloomberg survey median) over the last three months. A positive value of the index indicates that the economic data have exceeded the consensus on balance. The indices are calculated daily based on a rolling three-month period. The indices use a time decay function to replicate the markets limited memory, i.e. the weight of a data surprise decreases over time.

Source: Bloomberg, Time period: 01/01/2014 - 20/09/2019
The OECD leading indicator reached a 9-year low in July and points to a sustained global economic slowdown for the time being. Overall, only 24% of the countries surveyed reported an improvement in the leading indicator in July. This figure has worsened since June and thus does not give the global indicator a tailwind.

The OECD Leading Indicator is composed of a series of selected economic indicators whose composition provides a robust signal for future turning points. A turning point in the indicator usually signals a turning point in the economic cycle in 6-9 months. However, lead times are sometimes outside this range and turning points are not always correctly detected.

Source: Bloomberg, Time period: 31/01/1994 - 31/07/2019

The global PMI is below 50 points for the fourth time in a row, although it improved slightly in August.

In August, the US PMI fell below 50 points for the first time since 2016.

The PMI is an overall index that provides a general overview of the economic situation in industry. The PMI is derived from a total of eleven sub-indices, which reflect the change from the previous month. A value of 50 is regarded as neutral, a value of over 50 points as an indicator of rising activity in industry and a value of less than 50 points for falling activity in industry compared with the previous month. The index has an average lead time before actual industrial production of three to six months. The PMI is based on a survey of a relevant selection of purchasing managers regarding the development of parameters such as incoming orders.

Source: Bloomberg, Time period: 31/05/2016 - 31/08/2019

In the US, inflation fell to 1.7% in August. However, excluding volatile energy and food prices, core inflation rose to 2.4%. This is the highest figure since 2008 and indicates emerging inflationary pressure in the US.

In China, inflation remained at the previous month’s level.

Inflation is measured (in percent, year-on-year comparison) using a consumer price index, also known as a shopping basket of goods. This shopping basket contains all goods and services that a household purchases on average per year.

Source: Bloomberg, Time period: 31/08/2009 - 31/08/2019
The monetary measures by the ECB including new bond purchases weighed on the euro and caused it to depreciate slightly on a trade-weighted basis.

The US dollar has recently moved sideways. The Fed’s slightly hawkish interest rate cut has given the US dollar neither a tailwind nor a headwind.

The Japanese yen recently suffered from the increased risk appetite of investors and has depreciated significantly.

A trade-weighted index is used to measure the effective value of an exchange rate against a basket of currencies. The importance of other currencies depends on the share of trade with the country or currency zone.

Source: Bloomberg, Time period: 01/01/2018 - 20/09/2019

Sterling gained nearly 4% against the euro in the last four weeks thanks to the increased probability of avoiding a hard Brexit and the already high short position of investors.

The Russian rouble recently benefited from the rise in oil prices and appreciated by around 3% against the euro.

Performance of selected currencies against the euro, in percent.
Source: Bloomberg, Time period: 31/12/2018 – 20/09/2019

The EUR/USD exchange rate recently remained at around 1.10 dollars per euro. Both the Fed and the ECB lowered interest rates in September. In the medium term, however, the Fed still has considerably more scope for interest rate cuts, which could benefit the euro. Our economists see the EUR/USD exchange rate at 1.13 in the middle of next year.

EUR/USD exchange rate and interest rate differential (in percentage points) of 10-year US Treasuries and 10-year Bunds.
Source: Bloomberg, Time period: 01/01/2014 - 30/06/2020
The European equity sectors have recovered significantly over the last four weeks. Above all, stock values jumped, supported by rising bond yields. Financials were among the biggest winners.

Over the past four weeks, value has outperformed growth by approximately 5 percent. Since the beginning of the year, however, growth companies have outperformed value stocks by 12 percent.

Total return of European equity sectors and European style indices, in euros and in percent, sorted by 4-week performance. The difference between Value and Growth lies in the valuation. A growth stock is highly valued because the component companies provide information on whether profit growth needs to be further revised down. In Germany, there is a risk of an earnings recession if estimates are further reduced.

The highest earnings growth for 2019 is expected for Switzerland, followed by Japan in particular.

Earnings estimates for Europe and the USA have recently stabilised. Most of the latest US economic data surprised positively.

Negative earnings revisions have continued recently - even though the momentum has slowed somewhat.

Analysts lowered their earnings estimates for Latin America, the UK and Japan in particular.

Changes in Consensus Earnings Estimates

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Contribution Analysis

Price-Earnings Ratio (P/E Ratio) of European and US Equities

Historical Distribution: Price/Earnings and Price/Book Ratio

- Over the last few weeks, earnings estimates have declined, while stock markets have risen sharply. As a result, valuations have widened.
- Both European and US equities have gained over the last 12 months, driven by a P/E expansion.

- The P/E ratio for US equities has risen sharply in recent weeks. At 18.2, the US market is now slightly more expensive than the historic P/E ratio, which stands at 16.6. Investors are hoping that the trade conflict will abate and that economic data will stabilise.
- The P/E valuation for European equities has also risen. However, the P/E ratio is close to the historical average.

- In the last four weeks, valuations knew only one direction: upwards. Especially on a price-book ratio basis, US equities now seem to be very ambitious.
- Of all the regions considered here, emerging market equities are the most favorably priced.
- Hopes of a trade deal have led investors to be more optimistic. As a result, yields on safe government bonds have risen significantly, as demand for them has fallen. In the last four weeks, yields on US Treasuries have risen by 19 bp and on German, French and British government bonds by around 15 bp. Only in Italy have yields fallen further, as the new formation of the Italian government was well received by the market.

Effective yield of 10-year government bonds and change in the last four weeks in basis points (in brackets).
Source: Bloomberg, Time period: 01/01/2014 - 20/09/2019

- The steepness of the German and US yield curve has not significantly changed in the past two weeks. The US yield curve remains close to inverting, while the German yield curve is still more than 20 bps away:

The yield curve distinguishes between the so-called short and the long end. The reason for this lies in the way in which factors influence returns. Central banks control the short end of the curve through their monetary policy and key rates. By contrast, the long end is influenced less by central banks than by inflation expectations, supply, demand and risk premia.
Source: Bloomberg, Time period: 01/01/1998 - 20/09/2019

- Following the recent rate cut by the Fed, which was more hawkish than expected, expectations for further rate cuts in 2019 have fallen by around 20 percentage points.

The ECB lowered the deposit rate to -0.5% in September. The probability of a further rate cut in 2019 is now only around 15%. First market participants even see the possibility of an interest rate hike in 2019.

Derivatives on money market rates - such as the Fed funds futures - can be used to determine the probability of a change in the key interest rate priced by the market.
**Credit Spreads Financial and Non-Financial Bonds**

- Risk premiums on USD corporate bonds have fallen by around seven basis points in the last two weeks. In contrast, there has been little change in spreads of EUR corporate bonds.
- For EUR corporate bonds, the retail sector saw the largest spread widening while the capital goods sector saw the largest spread narrowing. As a result, corporate bonds also rotated in the direction of cyclical.

**Credit Spreads High Yield and Emerging Markets Bonds**

- The increased risk appetite in markets and the resulting demand for risk assets has led to a fall in spreads on EM, USD and EUR high-yield bonds. Over a two-week period EM High Yield Bonds fell by over 30 bps, USD High Yield Bonds by around 20 bps and EUR High Yield Bonds by around 10 bps.

**Historical Distribution of Credit Spreads (in bp)**

- The biggest change in spreads was seen in EM high-yield bonds. After a long period of risk premiums approaching the historic median, there was a recent countermove that widened the gap again.

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**Explanations**

- The extent of the risk associated with a corporate bond is shown by its asset swap spread (in basis points). This indicates the yield that the issuer must pay in addition to the swap rate for the respective term to offset its credit risk. See further explanations below.

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**Source:** FactSet, Time period: 01/01/2014 – 20/09/2019
Commodities Performance

- Over a period of four weeks, the precious metals platinum, palladium and silver made significant gains. They had catch-up potential compared to the previously sharp rise in gold prices.

- Energy prices rose as a result of the attacks on Saudi Arabian oil production facilities and a tighter oil supply.

- Industrial metals rose slightly. The weak data on Chinese industrial production and the strong US dollar weighed down until the hope of an agreement in the trade war supported prices.

The attacks on Saudi Arabian production and refinery plants led to a short-term oil price increase of up to 20% at the peak, which then settled at around 10%. However, as Saudi Arabia announced that it would quickly eliminate production losses of 5% of world production, the oil price stabilized.

- In the short term, oil supply is scarce, but this is likely to change in a few months as it is expected that non-OPEC countries continue to expand their production.

Higher oil production and higher inventories tend to depress oil prices and vice versa. An increase in active oil rigs indicates a future increase in oil production.

Source: Bloomberg, Time period: 01/01/2019 - 20/09/2019

Crude Oil

- Even after the Fed's rate cut and the ECB's monetary policy measures, the gold price is still fluctuating sideways around USD 1,500 per ounce.

- Continued low US real interest rates, expansive monetary policy and widespread negative bond yields argue for a higher gold price in the medium term.

The US dollar and the real interest rate, i.e. adjusted for inflation, are among the fundamental price factors of the gold price. Rising real interest rates tend to depress the price of gold, while falling real interest rates have a supportive effect. The same applies to the US dollar. The development of gold ETF holdings reflects the demand for gold from financial investors.

Source: Bloomberg, Time period: 01/01/2014 - 20/09/2019

Gold
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