BERENBERG
Markets

MONITOR

01 October 2018

Current market commentary

The US has initiated the next stage of the trade dispute and China has responded with retaliatory tariffs. There has been no significant progress in the Brexit negotiations and the problems of some emerging markets remain unsolved. However, neither of these developments caused strong market reactions. The real surprise came towards the end of last week. Italy plans a budget deficit well in excess of initial announcements, sending Italian government bonds and equities into decline. By then, however, investors had already become bullish again, had lowered their hedges and had significantly shifted money from money market ETFs into riskier assets. Emerging market bonds and US equities were the main beneficiaries, driven also by strong US macro data. Japanese equities recently showed particularly strong momentum - the price-weighted Nikkei even surpassed its level of 27 years ago. This trend should continue thanks to positive earnings revisions.

The bi-weekly ***Monitor*** gives you a structured overview of the current capital market environment and highlights important developments:

- Performance
- Positioning
- Sentiment
- Surprise Indicators
- Economics
- Foreign Exchange
- Equities
- Sovereign Bonds & Central Banks
- Corporate Bonds
- Commodities

Short-term outlook

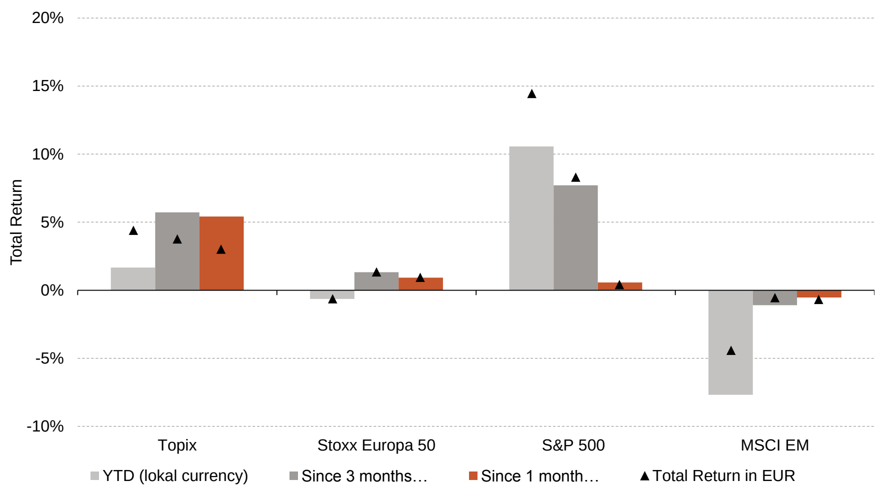
The numerous political risks will fuel volatility spikes in the short-term.

The trade dispute between the US and China persists. But even if the initial US tariff, applying to Chinese goods worth EUR 200 bn from 1 January 2019, was only 10% rather than the originally envisaged 25%, the relief was short lived. Other political risks surrounding Brexit and the budget negotiations in Italy are concerning market participants. Italy's proposal to increase the 2019 budget deficit to 2.4% of GDP has created uncertainty and losses. The US Congressional elections on 6th November could also cause stress in the markets.

The US data will provide information on the dynamics of the US economy.

The ISM index, unemployment rate and US hourly wage data are all important economic data for the U.S. this week. With the final PMI data and incoming orders from German industry, comparatively little economic data is available in Europe. On 15 October, however, the deadline for the euro states to notify the EU Commission of their budget plans for 2019 must be reached.

Japanese catch-up - positive momentum for Japanese equities



- Japanese equities (Topix) are the best region after the US (S&P 500) year to date, following strong recent performance which also makes Japanese equities the top performer on a monthly basis (in local currency & EUR).
- The positive development was accelerated by improved earnings prospects, good economic data, rising consumer spending, stable policies and net cash inflows. The valuation, low correlation to the world market and safe-haven status of the Yen also favour Japanese equities.

Explanations and 5 year performance see page 2.
Source: Bloomberg, As of 28/09/2018

Multi Asset

	4W (31/08/18 - 28/09/18)	YTD (31/12/17 - 28/09/18)	28/09/17 28/09/18	28/09/16 28/09/17	28/09/15 28/09/16	28/09/14 28/09/15	27/09/13 28/09/14
Brent	7.1	34.7	56.5	0.6	-14.0	-52.2	-0.5
Industrial Metals	2.0	-8.7	-1.5	19.6	6.6	-18.9	6.8
MSCI World	0.4	9.1	13.3	11.9	13.2	5.1	19.4
Eonia	0.0	-0.3	-0.4	-0.4	-0.3	-0.1	0.1
USDEUR	0.0	3.4	1.6	-4.8	0.2	12.8	6.6
MSCI Frontier Markets	-0.2	-9.6	-5.9	19.6	0.2	-14.1	38.5
Global Coporates	-0.6	0.8	0.3	-2.5	7.8	9.7	11.3
Global Convertibles	-0.6	7.9	8.0	7.8	9.0	8.1	15.3
MSCI Emerging Markets	-0.7	-4.4	1.5	14.4	19.8	-11.7	11.8
Gold	-0.8	-5.3	-5.9	-7.3	17.0	4.8	-2.8
Global Treasuries	-1.3	1.0	0.3	-8.8	11.4	8.1	6.7
REITs	-2.9	0.8	2.0	-9.2	17.9	12.9	13.2

4-week & YTD; 12-month periods over that last 5 years

MSCI World: MSCI World Net Return; MSCI Emerging Markets: MSCI EM Net Return; MSCI Frontier Markets: MSCI Frontier Markets Net Return;
REITs: MSCI World REITs Index; Global Treasuries: Bloomberg Barclays Global Agg Treasuries TR; Global Corporates: Bloomberg Barclays Global Aggregate Credit TR
Global Convertibles: Bloomberg Barclays Global Convertibles Composite TR; Gold: Gold US Dollar Spot; Brent Crude: Bloomberg Brent Crude Subindex TR;
Industrial Metals: Bloomberg Industrial Metals Subindex TR; Eonia: Eonia Capitalizaiton Index; USDEUR: Price of 1 USD in EUR.

- Over the past four weeks, investors have had difficulty earning money in euro terms. Only Brent oil and industrial metals have gained appreciably in value.
- The trade dispute between the US and China as well as Italy's higher budget deficit weighed on investor sentiment. Both bonds and partly equities have suffered losses in the risk-off environment.

Total return of selected asset classes, in euros and in percent, sorted by 4-week performance.
Source: Bloomberg, Time period: 27/09/2013 – 28/09/2018

Equities

	4W (31/08/18 - 28/09/18)	YTD (31/12/17 - 28/09/18)	28/09/17 28/09/18	28/09/16 28/09/17	28/09/15 28/09/16	28/09/14 28/09/15	27/09/13 28/09/14
MSCI EM Eastern Europe	6.1	6.3	10.4	21.0	14.3	-18.3	-7.9
Topix	3.1	4.7	11.3	9.4	12.9	13.4	7.0
MSCI UK	1.4	0.9	6.6	11.1	19.6	-8.0	5.6
Stoxx Europe 50	0.9	-0.6	0.4	14.6	0.8	-1.4	13.2
Stoxx Europe Cyclicals	0.8	-1.6	-0.6	27.2	1.2	-2.6	10.1
Stoxx Europe Defensives	0.7	5.6	5.3	7.5	2.0	-0.4	22.2
S&P 500	0.4	14.4	20.1	12.2	18.3	9.4	27.5
Euro Stoxx 50	0.3	-0.6	-2.1	22.2	1.3	-3.2	13.3
DAX	-0.9	-5.2	-3.6	21.7	10.1	-0.1	9.6
Stoxx Europe Small 200	-1.4	1.1	3.8	20.4	4.2	10.5	9.5
MSCI EM Asia	-1.9	-3.5	3.3	15.6	19.5	-4.2	16.3
Russell 2000	-2.6	15.4	17.1	14.3	17.2	11.5	12.5

4-week & YTD; 12-month periods over that last 5 years

S&P 500: S&P 500 TR (US-Equity); Stoxx Europe 50: Stoxx Europe 50 TR; Euro Stoxx 50: Euro Stoxx 50 TR; Topix: Topix TR (japanese Equity);
Stoxx Europe Small 200: Stoxx Europe Small 200 TR; Russell 2000: Russell 2000 TR (US Small Caps); Stoxx Europe Cyclicals: Stoxx Europe Cyclicals TR;
Stoxx Europe Defensives: Stoxx Europe Defensives TR; DAX: DAX TR; MSCI United Kindom: MSCI UK TR; MSCI EM Asia: MSCI EM Asia TR;
MSCI EM Eastern Europe: MSCI EM Eastern Europe TR.

- Over a four week period, the performance of equities varied widely by region and index.
- While equities from Eastern Europe and Japan recorded gains, EM Asia and US small caps were among the losers.
- European large-cap stocks remained comparatively stable, while small-cap stocks as well as the DAX fell.

Total return of selected equity indices, in euros and in percent, sorted by 4-week performance.
Source: Bloomberg, Time period: 27/09/2013 – 28/09/2018

Fixed Income

	4W (31/08/18 - 28/09/18)	YTD (31/12/17 - 28/09/18)	28/09/17 28/09/18	28/09/16 28/09/17	28/09/15 28/09/16	28/09/14 28/09/15	27/09/13 28/09/14
BTPs	1.8	-4.5	-3.6	-3.5	6.2	5.8	16.3
EM Local Currency Bonds	1.2	-2.4	-1.9	-2.1	16.9	-5.5	9.6
EM Hard Currency Bonds	0.5	2.0	0.6	-0.3	14.3	8.3	13.0
USD High Yield	0.4	6.5	4.5	2.7	11.5	9.0	12.5
EUR High Yield	0.1	0.0	0.4	6.2	6.7	-0.4	7.1
EUR Inflation Linkers	-0.1	-0.8	1.0	-1.1	5.5	-0.4	5.2
EUR Financials	-0.2	-0.9	-0.1	1.6	6.1	0.2	7.4
EUR Non-Financials	-0.4	-0.5	0.1	-0.8	8.4	-0.8	7.8
USD Corporates	-0.5	1.2	0.3	-3.1	8.7	14.5	13.6
Bunds	-0.9	0.8	0.9	-4.2	6.6	3.7	6.5
Treasuries	-0.9	-1.7	-1.7	-1.8	4.4	3.7	2.2
Gilts	-1.2	-1.8	-0.7	-6.9	-1.4	14.9	13.6

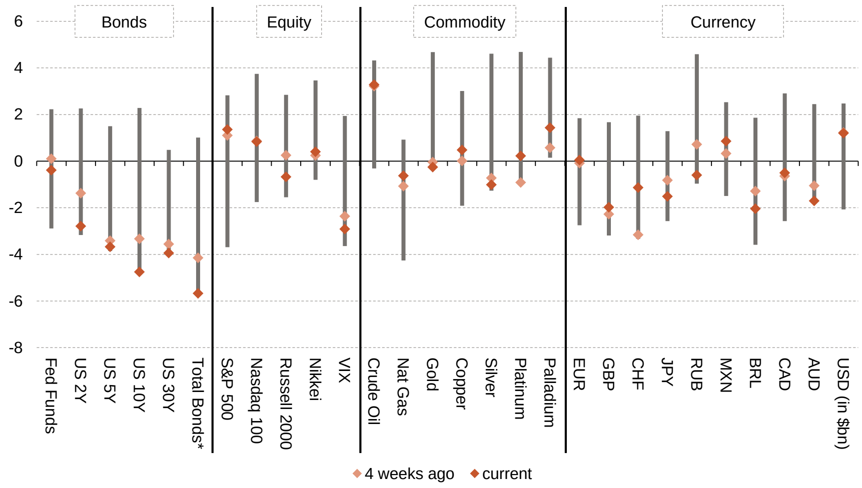
4-week & YTD; 12-month periods over that last 5 years

Bunds: Barclays Germany Govt All Bonds TR; BTPs: Barclays Italy Govt All Bonds TR; Treasuries: Barclays US Treasury TR;
Gilts: Barcl. UK Govt All Bonds TR; EUR Inflation Linkers: Barcl. Euro Govt Inflation-Linked Bond All Maturities TR; EUR Financials: IBOXX Euro Fin. Overall TR;
EUR Non-Financials: IBOXX Euro Non-Fin. Overall TR; EUR High Yield: Markit iBoxx EUR Liquid HY TR; USD Corporates: iBoxx USD Corporates TR;
USD High Yield: IBOXX USD Liquid HY TR; EM Hard Currency: Barcl. EM Hard Currency Agg Govt Related TR; EM Local Currency: Barcl. EM Local Currency Govt TR.

- Thanks in part to a recovery in their currencies, emerging market bonds have finally gained over the last four weeks.
- USD and EUR high-yield bonds have recently been able to remain stable.
- In the meantime, government bonds have suffered across the board with risk-on sentiment. Italy was a temporary outlier, but after the higher than expected deficit for 2019, bonds came under pressure last week.

Total return of selected fixed income indices, in euros and in percent, sorted by 4-week performance.
Source: Bloomberg, Time period: 27/09/2013 – 28/09/2018

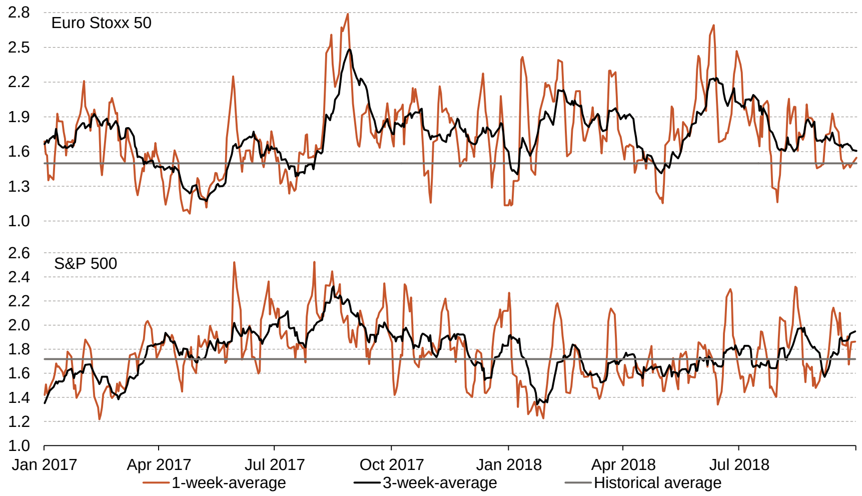
Non-Commercial Positioning



- Speculative investors remain sceptical about US bonds and gold. They have, however, significantly reduced their short positions in platinum.
- The largest net long positions are for crude oil, US equities and USD. The euro positioning remains neutral.

The Commodity Futures Trading Commission (CFTC) publishes the Commitments of Traders Reports every Friday. A distinction is made between "non-commercial" and "commercial traders" positions. Non-commercial traders enter into purely speculative positions. Commercial traders hedge underlying transactions with futures or options. The chart shows the historical, normalized distribution in standard deviations and focuses on the net future position (long positions minus short positions) of non-commercial traders, thus indicating how speculative investors have positioned themselves.
*Duration weighted average bond position.
Source: Bloomberg, CFTC, Time period: 25/09/2008 - 25/09/2018

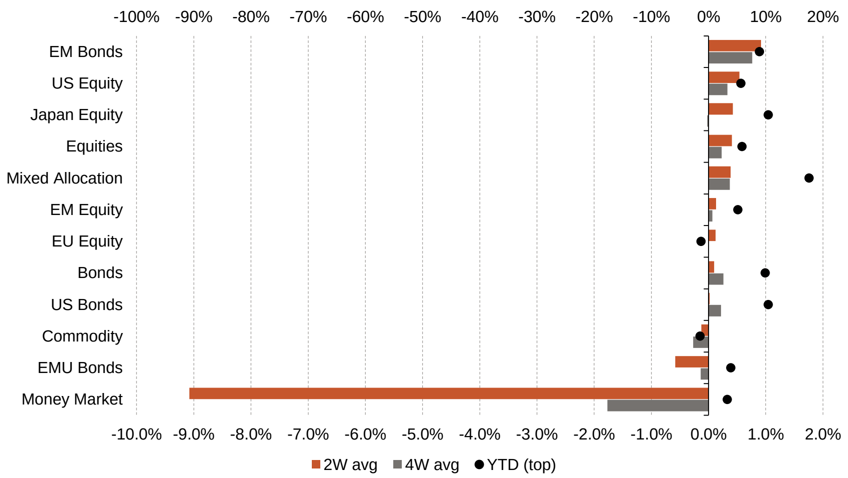
Put-Call Ratio



- As global uncertainties have temporarily calmed, investors have significantly reduced their hedging ratios for the Euro Stoxx 50 over the last week.
- The 1-week-average put call ratio for Euro Stoxx 50 is thus close to its historical average.

The put-call ratio is the ratio of traded put options (speculation on falling prices) to call options (speculation on rising prices) across all maturities. The higher (lower) the ratio, the more cautious (optimistic) are the market participants. The data have been available for the S&P 500 since 20 December 1993 and for the Euro Stoxx 50 since 24 February 2006.
Source: Bloomberg, Time period: 20/12/1993 - 28/09/2018

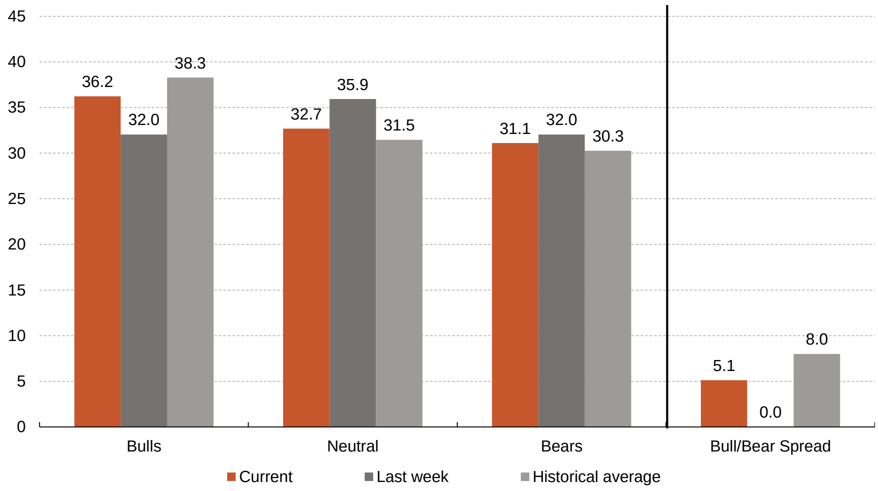
ETF Flows



- Risk-On: Strong outflows from money market ETFs of around 9% over a 2-week average indicate that investors are more willing to take risks.
- After the recent sharp correction, emerging market bonds, which are now relatively cheap, recorded the largest inflows of funds.
- But US equities were also able to attract investors' money with 0.5% of new inflows, fostered by pleasantly surprising US economic data.

Estimated ETF flows in percent of assets under management, sorted by 2-week average.
Source: Bloomberg, Time period: 31/12/2017 - 27/09/2018

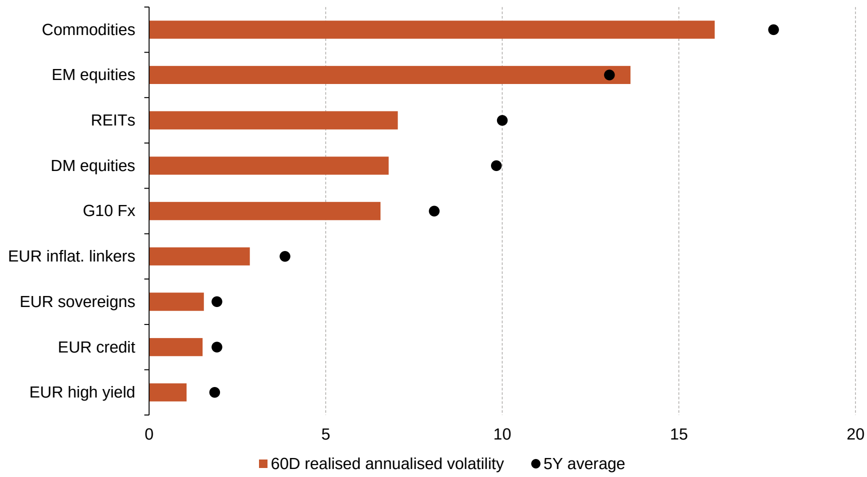
AAII Sentiment Survey (Bulls vs Bears)



- In the US the bulls have again won the upper hand. 36.2 percent of investors view the outlook for the US equity market as positive.
- The number of bears has fallen slightly since last week and remains at over 31 percent.

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, AAII, Time period: 23/07/87 - 27/09/18

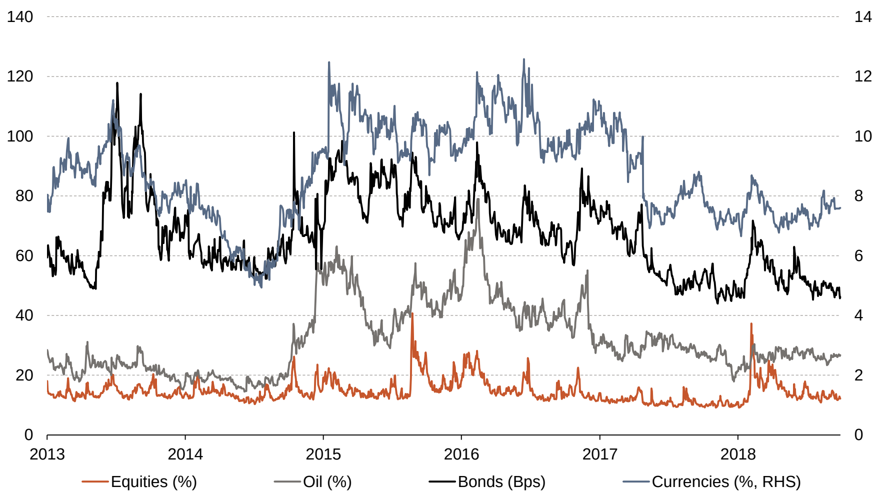
Realised Volatilities



- Realised volatilities for all asset classes have remained historically low recently. One exception was emerging market equities, which suffered from the Turkish and Argentine crises.
- Developed market equities and EUR high-yield bonds in particular recorded a significant decline in realised volatilities compared to two weeks ago.

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: 28/09/2013 - 28/09/2018

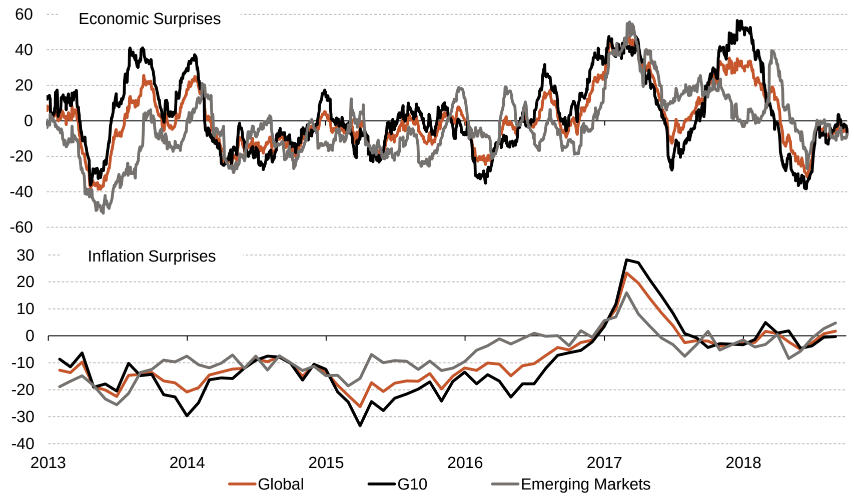
Implied Volatilities



- Implied volatilities remained at similar levels to two weeks ago. The absence of major surprises in Fed policy and political events kept volatility relatively stable and rangebound.
- However, stock market volatility remains above 2017 levels.

The price of options depends on the volatility of the underlying instrument. Implied volatility can therefore be interpreted as a measure of the currently expected fluctuation range of the underlying 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: 01/01/2013 - 28/09/2018

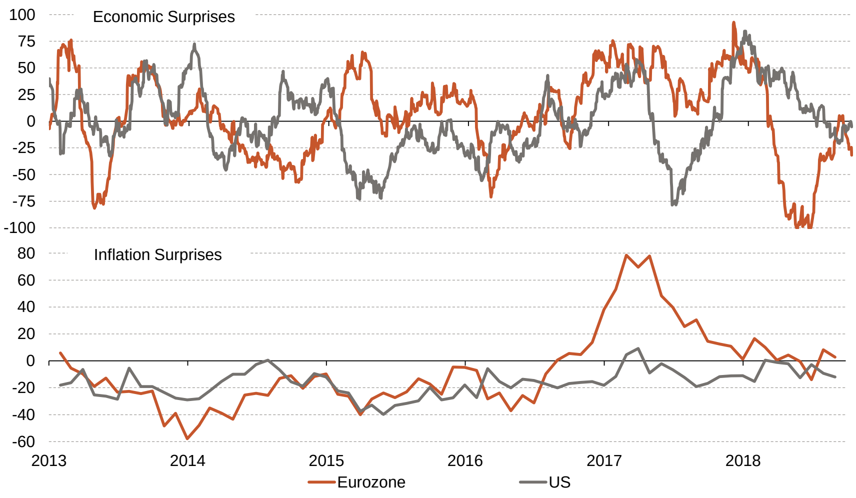
Global



- Positive and negative economic surprises have recently balanced each other out. In the three-month aggregate, however, economic data surprised slightly downwards in all regions.
- There were some disappointments, most notably in emerging markets. In Argentina, for example, the Q2 unemployment rate of 9.6% was higher than expected (9%).
- August inflation in South Africa was surprisingly low at 4.9% (5.2% months earlier).

See explanations below.
Source: Bloomberg, Time period: 01/01/2013 - 28/09/2018

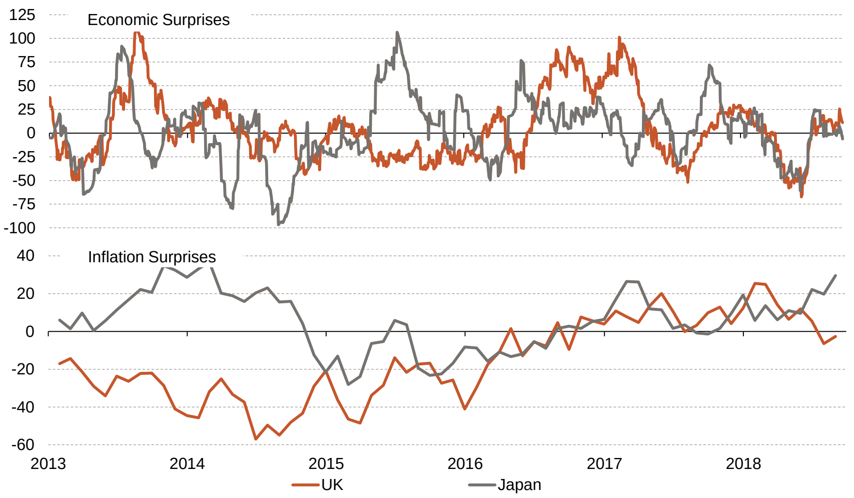
Eurozone and US



- The trade dispute is also hurting Europe. While economic surprises were positive in the USA, in the eurozone they grew negative again.
- Consumer confidence in France and many September industry sentiment surveys (PMIs) in the euro area countries were disappointing. German economic expectations (IFO) and consumer confidence in Italy surprised positively.
- Consumer confidence in the USA rose to 138.4 points, the highest level since October 2000.

See explanations below.
Source: Bloomberg, Time period: 01/01/2013 - 28/09/2018

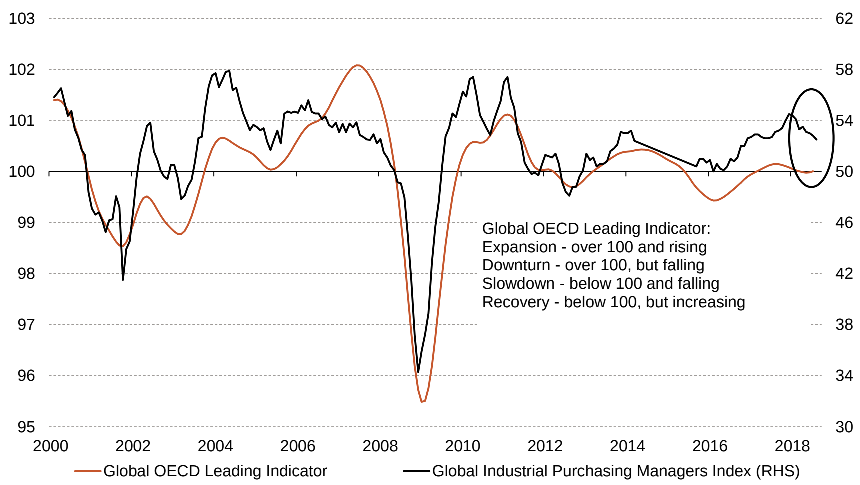
UK and Japan



- Economic surprises were close to zero in both regions. The UK grew by 1.2% (YoY) in Q2 and in Japan unemployment fell to 2.4%.
- August inflation (YoY) in the United Kingdom (2.7%) and Japan (1.3%) surprised significantly to the upside.

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: 01/01/2013 - 28/09/2018

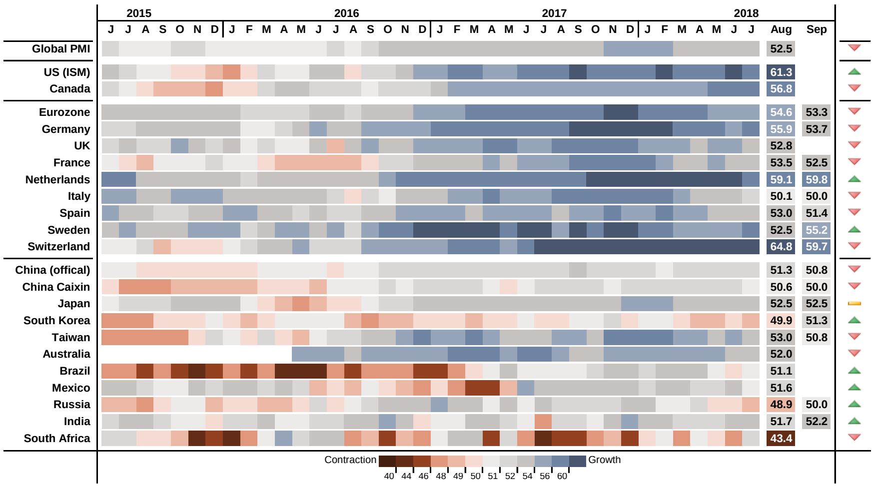
OECD Leading Indicator and Global Purchasing Managers Index



- The trade war and various global crises continue to affect corporate sentiment. The global purchasing managers' index is at its all-year low of 52.5 points.
- Based on the latest September figures from Europe, the global September PMI for industry should be slightly below the August figure.

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: 31/01/2000 - 30/09/2018

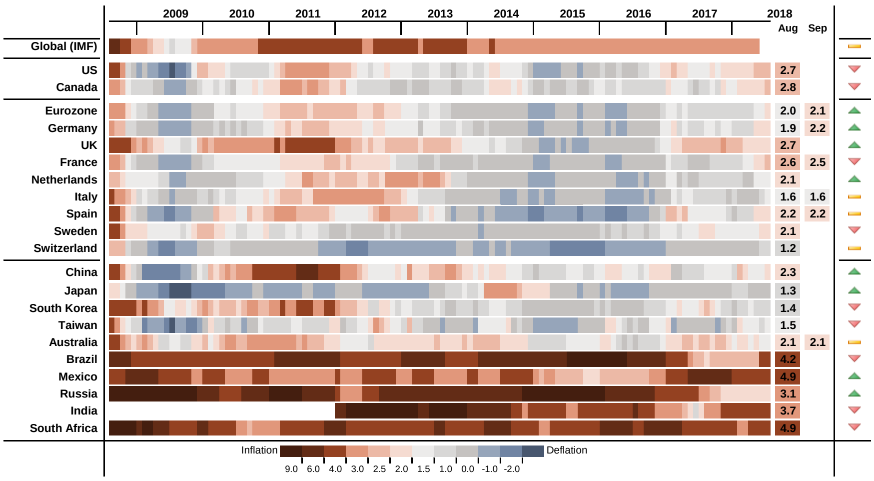
Manufacturing Purchasing Managers Index (Manufacturing PMI)



- Industrial sentiment in Europe continued to trend downwards. German industry fears the consequences of the trade dispute. As a result, the industrial PMI has fallen to 53.7.
- In Japan, sentiment remains robust at 52.5 points.

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: 30/06/2015 - 30/09/2018

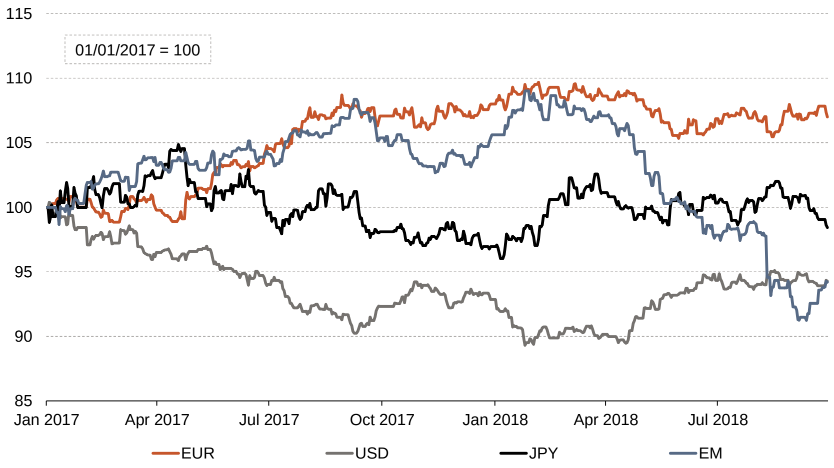
Headline Inflation



- Inflation in Europe is on the rise again due to climbing energy and food prices. August inflation in the UK reached 2.7%. In Germany, September inflation surprisingly rose to 2.2%.
- Inflation is also increasing in Japan. With 1.3%, it has reached its highest level since February. However, it remains far from the 2% target.

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: 30/09/2008 - 30/09/2018

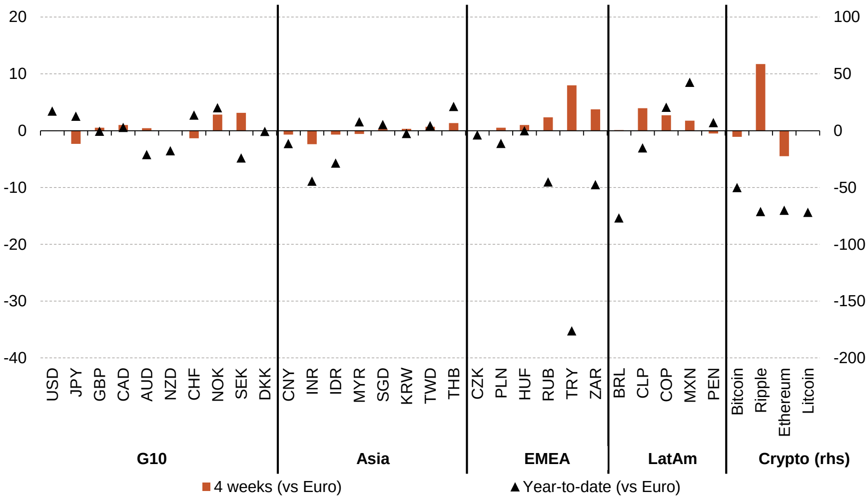
Trade-Weighted Currency Development



- Most recently, the trade-weighted euro fluctuated sideways, with the Italian budget negotiations putting some strain on it.
- The trade-weighted yen was less sought after and depreciated.
- Emerging market currencies have recovered slightly from their low in September. The Turkish lira in particular benefited from the central bank's rate hike.

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: 01/01/2017 - 28/09/2018

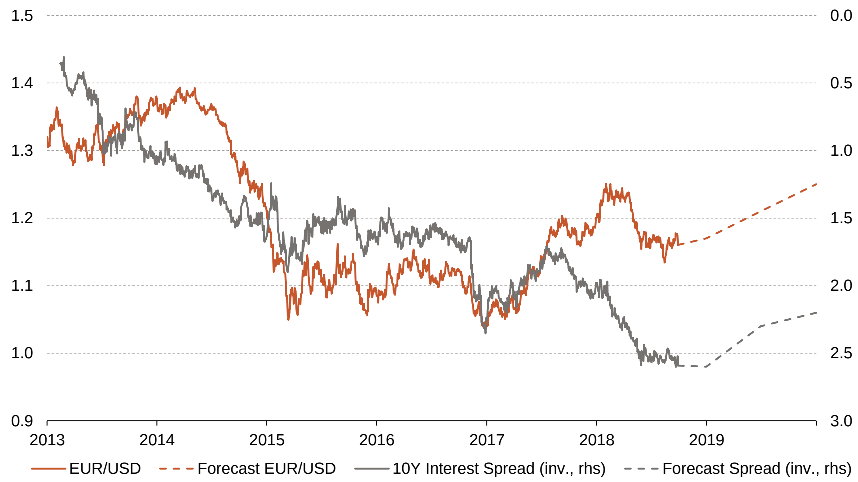
Currency Moves vs Euro



- Over a 4-week period, the Norwegian and Swedish krona appreciated against the euro.
- The Turkish lira appears to be recovering after suffering massive losses. Other emerging market currencies, notably the ruble, the rand and Latin American currencies, also appreciated against the euro.
- The Ripple had a strong rally from low levels.

Performance of selected currencies against the euro, in percent.
Source: Bloomberg, Time period: 01/01/2018 - 28/09/2018

EUR/USD exchange rate and interest rate differential



- The EUR/USD exchange rate recently fluctuated between 1.16 and 1.18. The US dollar benefited from the prospect of further US interest rate hikes, while the euro was burdened by a higher budget deficit in Italy.
- The interest rate differential on 10-year bonds remains high. As the Fed continues its path of interest rate hikes, the yield advantage of US Treasuries is likely to remain.

EUR/USD exchange rate and interest rate differential (in percentage points) of 10-year US Treasuries and 10-year Bunds.
Source: Bloomberg, Time period: 01/01/2013 - 31/12/2019

European Sector & Style Performance

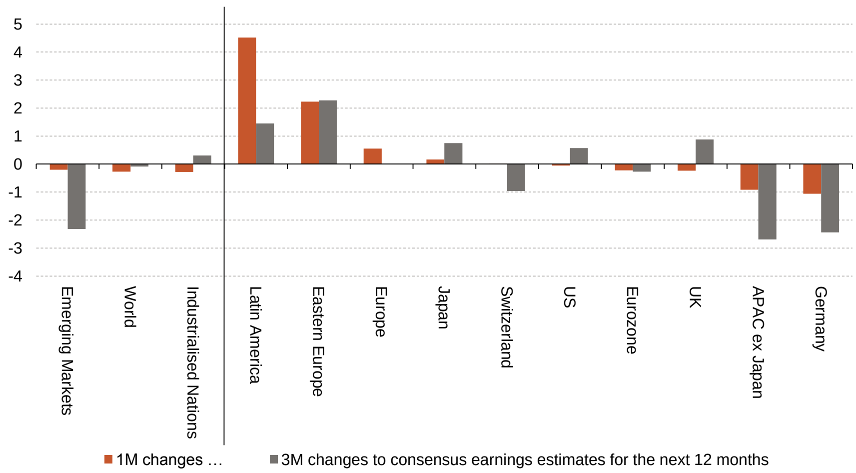
	4W (31/08/18 - 28/09/18)	YTD (31/12/17 - 28/09/18)	28/09/17 28/09/18	28/09/16 28/09/17	28/09/15 28/09/16	28/09/14 28/09/15	27/09/13 28/09/14
	4-week & YTD		12-month periods over that last 5 years				
Energy	5.7	16.8	24.9	21.7	14.1	-26.5	13.6
Materials	2.2	1.1	7.6	23.9	22.7	-15.6	4.8
Value	2.1	-1.1	-0.4	21.2	0.7	-6.7	15.1
Finance	1.9	-6.5	-6.9	34.3	-11.8	-1.1	15.0
Telecommunications	0.4	-12.8	-12.6	1.0	-7.2	12.1	13.2
Health Care	0.1	6.4	2.8	4.5	-3.0	7.9	28.6
Consumer Discretionary	-0.3	0.2	1.9	16.8	-0.3	12.8	4.4
Industrials	-0.5	2.1	2.4	20.9	14.5	2.0	3.5
Utilities	-0.6	1.2	-1.3	7.8	5.8	-8.5	23.8
Growth	-0.9	2.7	4.3	11.0	6.2	8.7	9.9
Consumer Staples	-1.3	-1.9	0.4	1.4	14.3	14.3	9.4
Information Technology	-2.8	10.4	12.1	19.5	20.0	4.2	8.3

Consumer Discretionary: MSCI Europe Consumer Discretionary NR; Consumer Stables: MSCI Europe Cons. Staples NR; Energy: MSCI Europe Energy NR; Finance: MSCI Europe Financials NR; Health Care: MSCI Europe Health Care NR; Industrials: MSCI Europe Industrials NR; Information Tech.: MSCI Europe Inform. Tech. NR; Materials: MSCI Europe Materials NR; Telecommunications: MSCI Europe Telecommunication Services NR; Utilities: MSCI Europe Utilities NR; Value: MSCI Europe Value NR; Growth: MSCI Europe Growth NR.

- Energy has been the best European sector since both the beginning of the year and last month, favoured in part falling US oil inventories.
- Financials and telecommunications have recovered, while IT firms lost value.
- Value equities outperformed growth equities recently.

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 company is expected to grow strongly. Value stocks generally have less growth potential and are valued lower.
Source: Bloomberg, Time period: 27/09/2013 – 28/09/2018

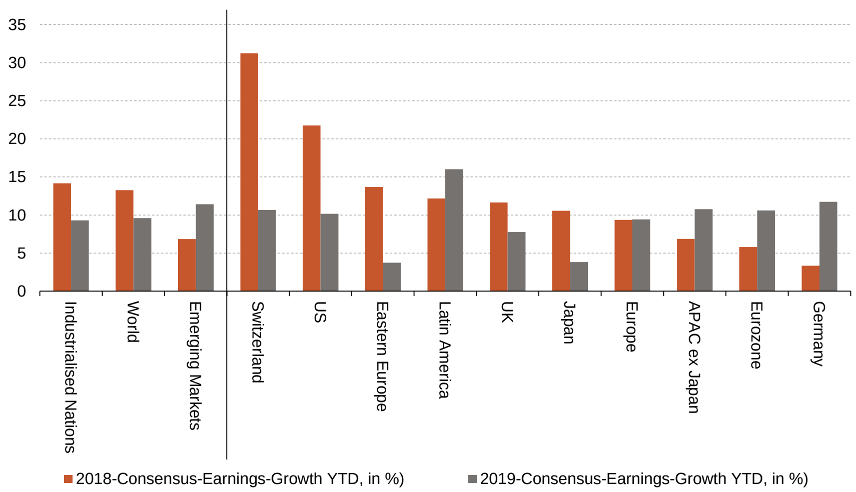
Changes in Consensus Earnings Estimates



- Over the last month, the momentum of earnings downgrades for emerging markets slowed markedly.
- Latin America and Eastern Europe saw the largest positive earnings revisions over the last month.
- Weak economic data in Germany and uncertainties with regards to budget negotiations in Italy have resulted in negative earnings changes in the Eurozone.

1-month and 3-month changes in consensus earnings estimates for the next 12 months, in percent.
APAC ex Japan = Asia Pacific ex Japan
Source: FactSet, as of 28/09/2018

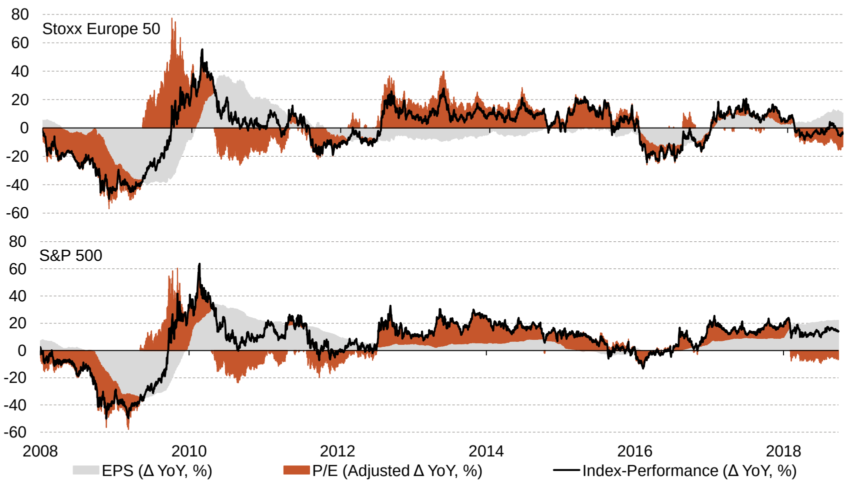
Earnings Growth



- Estimated earnings growth for the Eurozone and Germany has continued to decline over the past two weeks. The consensus for Germany is, thus, below 5%.
- The highest profit growth is expected for Switzerland and the USA.
- The consensus expects solid overall profit growth of over 13% for the world and industrialized countries.

Calendar year earnings growth expected to the consensus for selected equity regions, compared to the previous year and in percent. The earnings estimates of the individual companies are aggregated using the index weights (bottom-up).
APAC ex Japan = Asia Pacific ex Japan
Source: FactSet, as of 28/09/2018

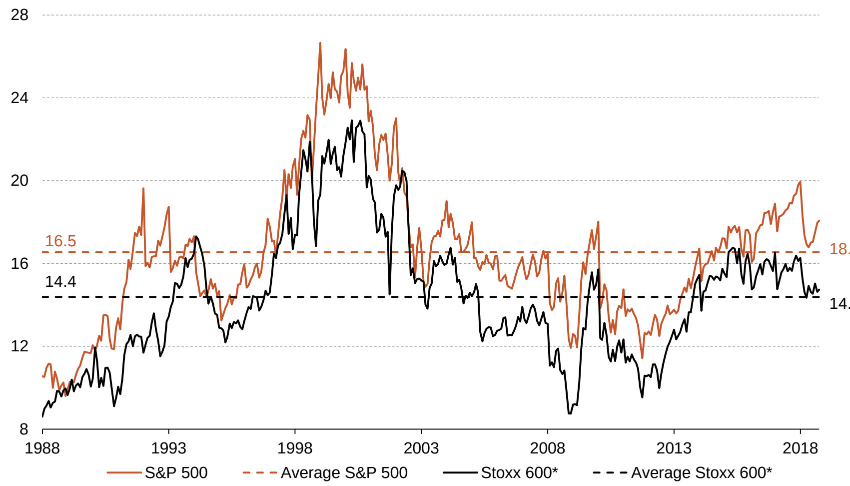
Contribution Analysis



- Valuations for both the Stoxx Europe 50 and the S&P 500 have become significantly more favourable over the past 12 months as earnings estimates have risen more strongly than the respective stock indices.
- For the USA, however, the increase in profits was significantly stronger. The S&P 500 has therefore performed significantly better than the Stoxx Europe 50 over the last 12 months.

Analysis of the stock market drivers over the last 12 months. This takes into account the change in earnings estimates and the change in valuation (price/earnings ratio). EPS = earnings per share
Source: Bloomberg, Time period: 01/01/2008 - 28/09/2018

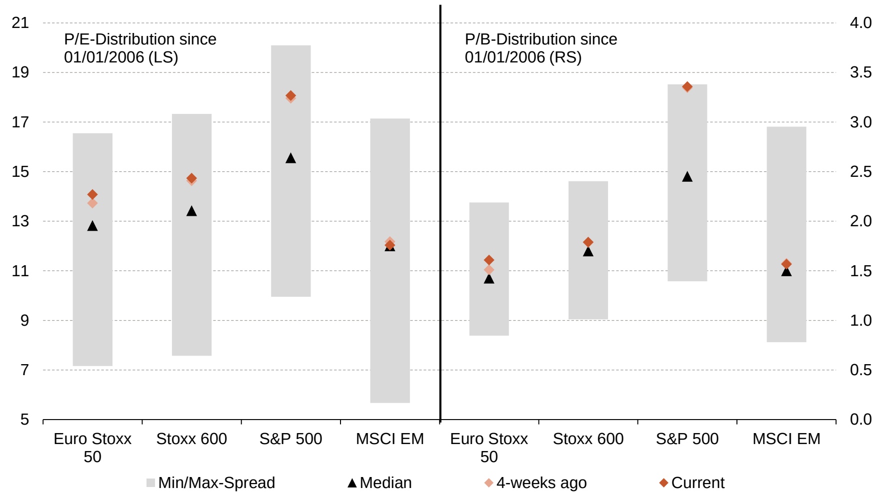
Price-Earnings Ratio (P/E Ratio) of European and US Equities



- The S&P 500 set a new record last week, which resulted in technical follow-up purchases. Due to the strong price gains, the P/E ratio has risen again to 18, which corresponds to the highest value since January.
- European shares are now valued at 14.6 points on a P/E – basis which is fair compared to its own history.

P/E valuation based on earnings estimates for the next twelve months for European and US equities and the respective P/E average since 1988 * For the Stoxx 600, the history prior to 2000 is of MSCI Europe.
Source: Bloomberg, Time period: 31/12/1987 - 28/09/2018

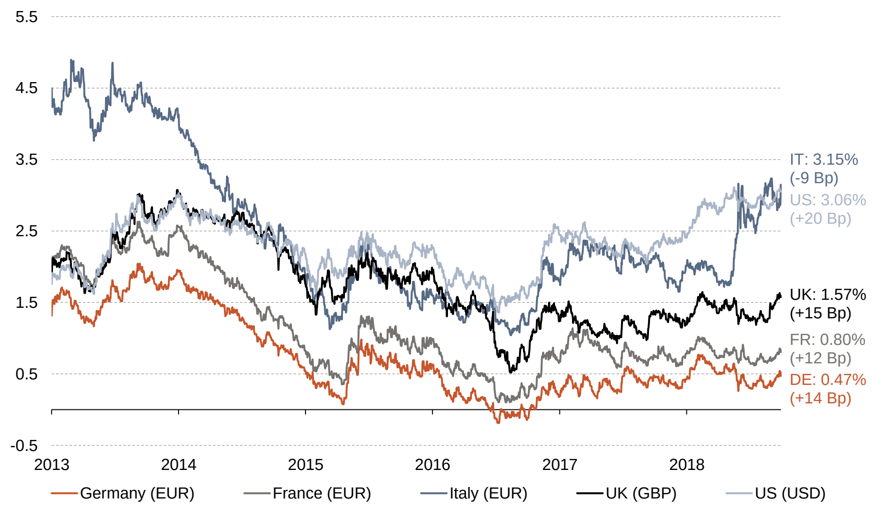
Historical Distribution: Price/Earnings and Price/Book Ratio



- Valuations for European and American equities have recently risen compared to four weeks ago.
- The price/book value ratio of the S&P 500 is at its highest since at least 2006.
- Only emerging market equities are currently valued close to their median and thus appear attractive compared to other regions.

Historical distribution of valuation indicators for selected stock regions since 2006, showing the current value, the observation four weeks ago and the historical median, the maximum (upper limit of the grey bar) and the minimum (lower limit of the grey bar).
Source: Bloomberg, Time period: 01/01/2006 - 28/09/2018

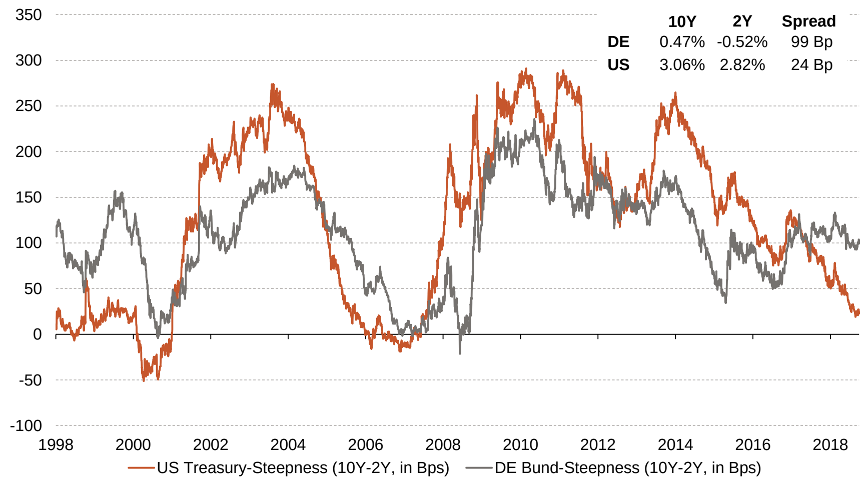
10-Year Government Bond Yields



- Sell-off in Italy: After the announcement of the government budget, Italian government bonds recorded an increase in yields.
- The good economic data gave US yields a boost. They expanded by 20 bp.
- European government bonds were not immune to the US yield pull and also showed rising yields.
- British Gilts could not benefit from the rising uncertainty regarding Brexit with a yield now close to 1.6%.

Effective yield of 10-year government bonds and change in the last four weeks in basis points (in brackets).
Source: Bloomberg, Time period: 01/01/2013 - 28/09/2018

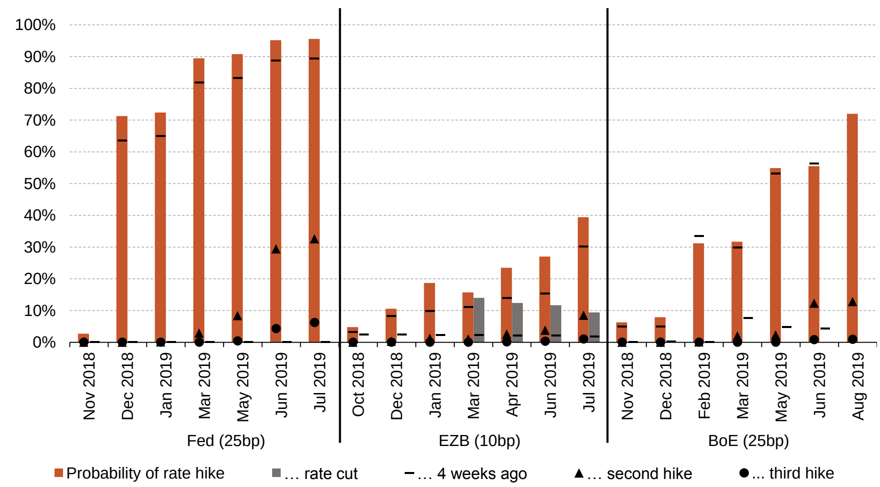
Yield curve steepness (10Y - 2Y)



- Despite the Fed's interest rate hike last week, there was no further flattening of the US yield curve. It remains above 20 basis points.
- The steepness of the German yield curve is back below 100 basis points after the Italian shock on Friday, as safe German 10-year government bonds were in demand.

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 - 28/09/2018

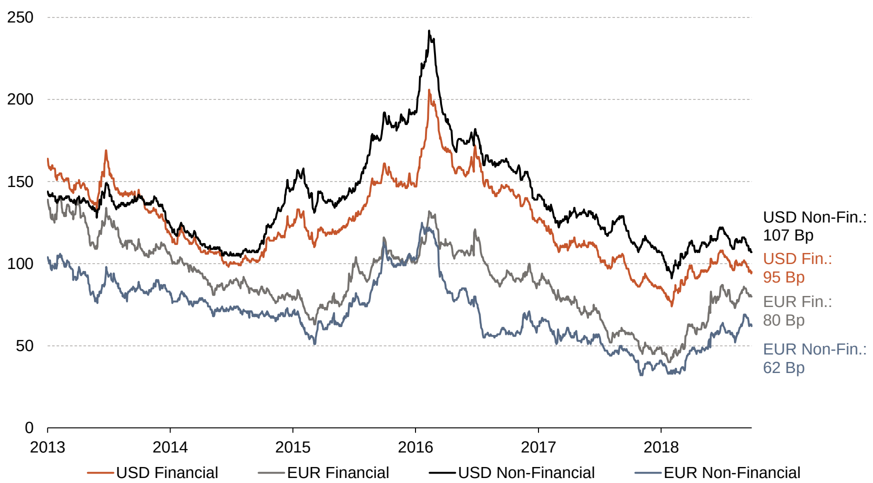
Implicit Probabilities for Changes in Key Interest Rates



- After the interest rate rise in the US to 2% - 2.25% due to continued good US economic data, the probability of a further rise in interest rates in December has risen to over 70%.
- In the eurozone, the likelihood of an interest rate hike has risen to over 35% in summer 2019, following Draghi's statement about rising inflation.

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
Source: Bloomberg, Time period: 31/08/2018 - 28/09/2018

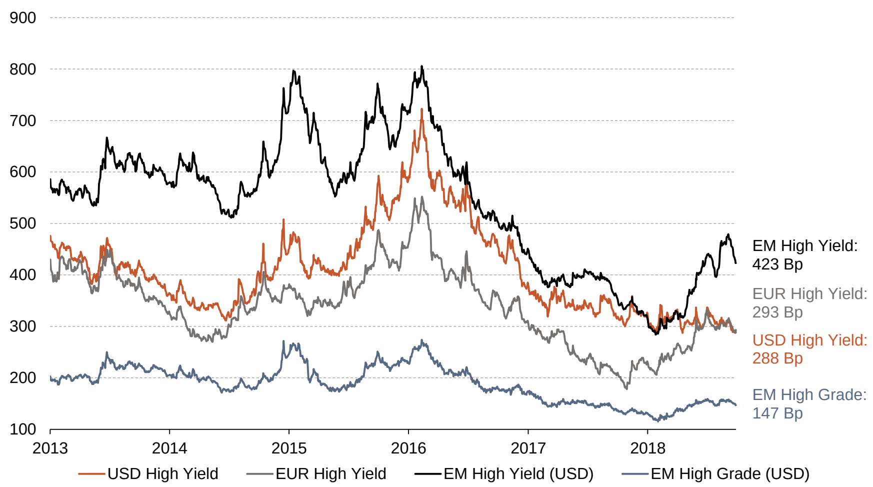
Credit Spreads Financial and Non-Financial Bonds



- Over the last two weeks, risk premia
- have fallen in all segments due to solid economic data and risk-off sentiment.
- In the USA, it was above all the energy and raw materials sectors that drove the spread narrowing.
- In case of EUR non-financial bonds, the real estate, energy and transport industries in particular recorded falling risk premia. As for EUR financial bonds, insurance companies have experienced a slight spread narrowing.

Explanations see middle and bottom illustration.
Source: FactSet, Time period: 01/01/2013 - 28/09/2018

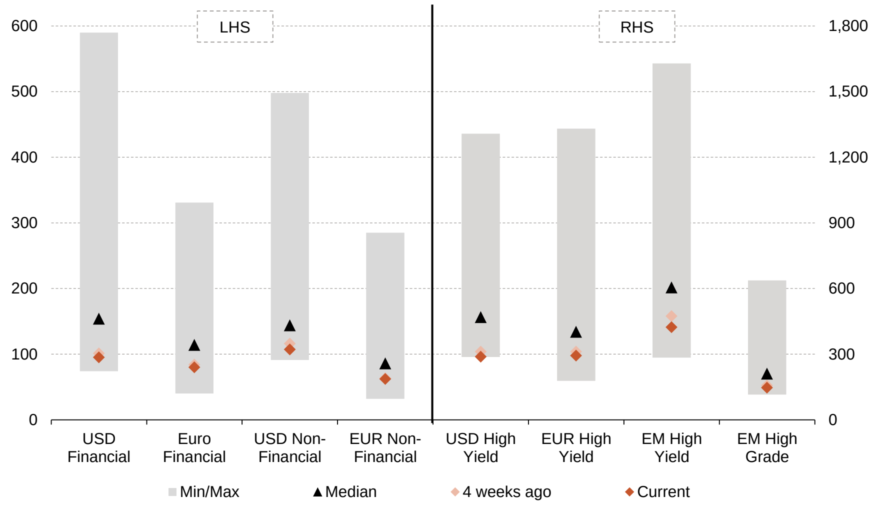
Credit Spreads High Yield and Emerging Markets Bonds



- EUR and USD high-yield bonds are neck and neck. EUR High Yield Bonds have seen a spread narrowing of 9 basis points in the last two weeks and temporarily had a lower risk premia than USD High Yield Bonds.
- EM high-yield bonds also recorded somewhat lower risk premia in a 2-week comparison, thanks to a weaker USD and the easing of the crises in Turkey and Argentina.

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.
Source: FactSet, Time period: 01/01/2013 - 28/09/2018

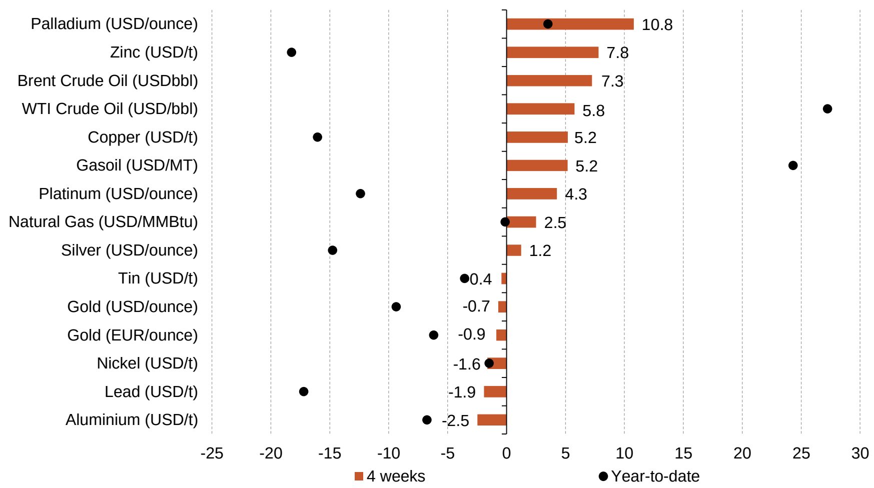
Historical Distribution of Credit Spreads (in bp)



- Risk premia for EM high-yield bonds have changed direction, having significantly moved away from their historical median.
- Risk premia on USD high yield bonds have reached a new 10-year low based on good economic data and earnings prospects.

USD Financial = ICE BofAML US Financial; EUR Financial = ICE BofAML Euro Financial; USD Non-Financial = ICE BofAML US Non-Financial; EUR Non-Financial = ICE BofAML Euro Non-Financial; USD High Yield = ICE BofAML US High Yield; EM High Yield = ICE BofAML High Yield Emerging Markets Corporate Plus; EM High Grade = ICE BofAML High Grade Emerging Markets Corporate Plus. The EM indices shown here are hard currency bonds.
Source: FactSet, Time period: 28/09/2008 - 28/09/2018

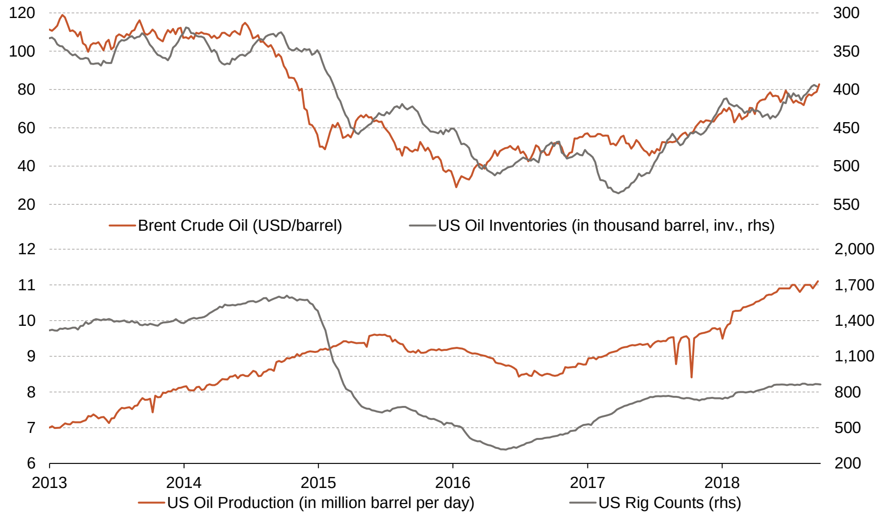
Commodities Performance



- Palladium has continued its uptrend, leading the winners list for the last four weeks.
- Energy and raw materials prices have also risen, driven by concerns about falling Iranian exports.
- Industrial metals have been burdened by ongoing trade disputes between the US and China, with copper a positive outlier.

Total return of selected commodity prices, in percent, sorted by 4-week performance.
Source: Bloomberg, Time period: 01/01/2018 - 28/09/2018

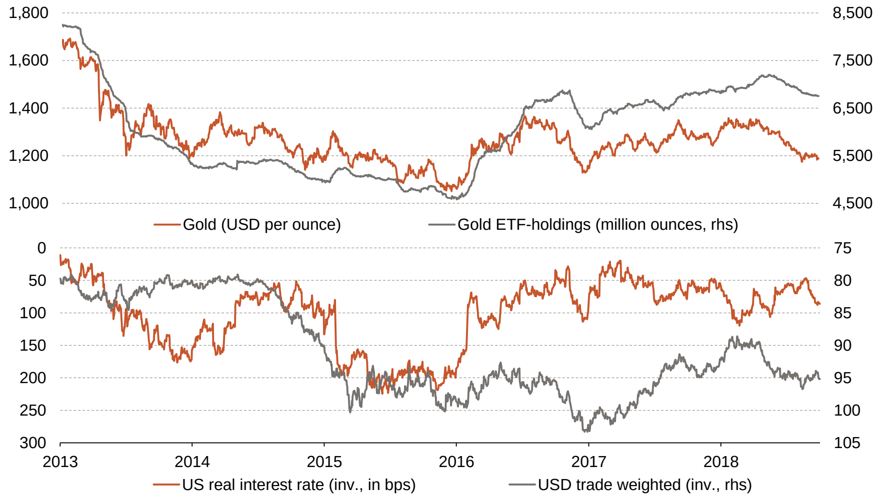
Crude Oil



- The positive momentum of oil prices continued. At USD 82 per barrel, the price of Brent crude has reached its highest level in 4 years and WTI oil is also trading at well over USD 70.
- Low inventories, robust demand and concerns about a supply deficit when US sanctions against Iran enter into force in November drove prices up.

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: 01/01/2013 - 28/09/2018

Gold



- The gold price was burdened by the prospect of a further tightening of US monetary policy and fell below the important level of 1,200 US dollars per ounce.
- The net short positions of speculative financial investors remain at high levels. Possible short coverings offer potential for recovery here.

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: 01/01/2013 - 28/09/2018

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