BERENBERG
Markets

INVESTMENT COMMITTEE MINUTES

09 December 2021

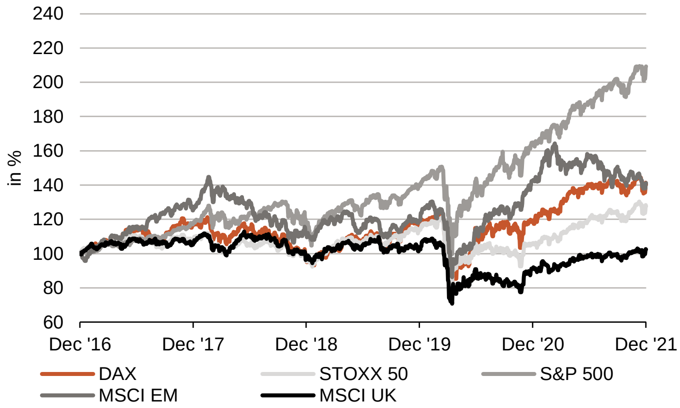
Managers of the Committee

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, 08/12/2016 - 08/12/2021.

Most important assessments at a glance

Economics	• The European economy is losing momentum in the short term. COVID-19, supply bottlenecks and high energy prices weigh. • The outlook for 2022 is positive despite omicron: consumers with pent-up demand, companies want to invest, policy supports. • Inflation: peak in sight, decline in 2022, but wage pressure rising - US Fed initiates monetary policy turnaround, ECB hesitates.
Equities	• Equity markets have corrected on a more hawkish Fed and Covid 19 worries. • Growth stocks were able to prove themselves again. However, with real interest rates rising, this is likely to become more difficult. • We have taken advantage of the correction and slightly increased our equity overweight. We remain cautiously optimistic for now.
Bonds	• Covid 19 worries and growth concerns caused yields on longer-dated government bonds to fall significantly. • EUR corporate bonds only conditionally attractive despite widening spreads. Asian corporate bonds under observation. • We underweight bonds and focus on credit risk and off-benchmark themes; duration short.
Commodities	• Gold continues to fluctuate sideways around USD 1,800 per ounce. Rising real interest rates limit upside opportunities. • Covid and economic worries recently weighed on the oil price, but supply shortages should provide support in the medium-term. • Industrial metals are in wait-and-see mode. Positive economic signals in 2022 could give industrial metals a new boost.
Currencies	• Monetary policy divergence weighs noticeably on the euro. In the meantime, however, the dollar strength has gone too far. • The sideways movement around 0.85 pound per euro is likely to continue. The UK's interest rate advantage seems to be priced in. • The Swiss franc has risen to its highest value since 2015, but the local economy has adjusted in the meantime.

Current market commentary

After ever new highs on the stock markets, there was a significant sell-off at the end of November. The more transmissible Covid 19 virus variant from South Africa and the hawkish US central bank created a risk-off environment. Both significantly increased uncertainty and fuelled growth concerns. In this environment, cyclical stocks lost the most. European equities, for example, temporarily lost more than 8%. We took advantage of this opportunity and tactically increased our equity exposure in Europe slightly. 2022 should be characterised by declining but persistent inflation, more normal earnings and economic growth, and valuation pressures. Fundamentally, the equity markets therefore offer significantly less potential than in 2021. However, the lack of alternatives, high cash holdings, no extreme positioning of systematic investors and good seasonality into the spring still make us positive for the time being. Therefore, it is important to tactically exploit opportunities. We consider this essential in view of the limited upside potential at index level in the medium term. After the recent increase, we are positioning ourselves with a moderate to medium equity overweight.

While the equity market continues to paint an optimistic economic scenario, the bond market is already pricing in a noticeable slowdown in growth with flattening yield curves. The reasons for this picture are probably COVID-19 concerns and uncertainty surrounding central bank policy. Yields on 10-year German government bonds have fallen by about 10bp in the past four weeks and risk premiums on corporate bonds have risen noticeably. However, EUR corporate bonds are still not particularly attractive. After the stabilisation in China, however, the attractiveness of Asian corporate bonds has increased.

Energy commodities and industrial metals had a difficult time due to the COVID-19 concerns but should recover significantly as the economy improves. Gold remains in a sideways trend.

ECONOMICS

Positive outlook for 2022 - despite new risks from Omicron

Euro economy loses momentum at the end of 2021: Delta wave, omicron risks, supply bottlenecks and energy costs weigh.
Outlook 2022 remains positive: supply bottlenecks may ease, consumers and businesses have pent-up demand.
Inflation declines in 2022 but remains an issue - central banks tighten policy - the Fed and BoE fast, the ECB slow.

- **A touch of stagflation:** After a growth spurt in the spring and summer, the European economy is currently losing momentum. New restrictions to curb the delta wave of covid infections are weighing on parts of the service sector. In contrast, US growth regained momentum in the autumn after a weak phase in the summer. On both sides of the Atlantic, however, supply bottlenecks are hampering growth in industry. Some sectors are also suffering from labour shortages.
- **Positive outlook for 2022:** Employment is rising on both sides of the Atlantic. This is supporting private consumers' incomes and consumption. The high additional savings that households built up during the pandemic are helping them to cushion the still high energy prices. Companies and governments want to invest more. Fiscal policy remains expansionary, more so in the US than in Europe. If the supply bottlenecks ease, the economy may surprise positively again in 2022.
- **The omicron risk:** It is not yet possible to predict whether the new and more contagious virus variant will prove so dangerous that many countries will have to react with long and severe restrictions. That would put a short-term strain on the economy. But experience with previous waves suggests that many countries would be able to recover such losses quickly afterwards. Growth would be pushed back a little, but it would not fail.
- **In China**, the government's attempt to persuade investors to behave more cautiously in the real estate sector and not to absorb all losses on the government's account is causing turbulence. But the risk of a real financial crisis remains low. As a capital-rich country with a high savings rate, China can launch a stimulus if needed. As its own domestic demand is robust, the US and Europe are not currently dependent on a growing Chinese market.
- **High inflation in autumn 2021, decline in 2022:** Supply constraints, delivery problems, exceptionally strong US consumer demand for durable goods and high energy prices have pushed inflation up more than expected. However, the inflation peak is in sight (USA) or has probably already been reached (Eurozone). With the expiry of some special effects, the price climate should calm down again in 2022 with year-end inflation rates around 1.6% in the euro area and 3% in the US. After that, however, inflation is likely to rise slowly again in the euro area as well, with stronger wage pressure.

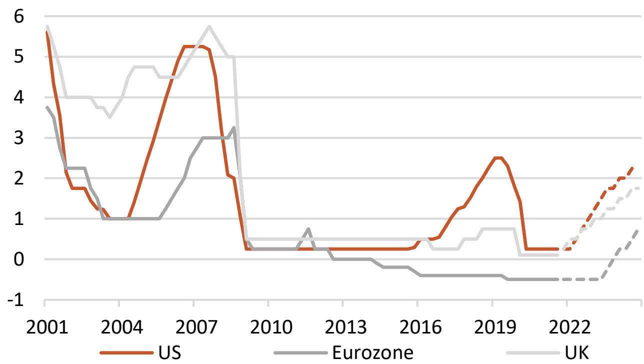
Monetary policy turnaround: Inflation remains well above 2%. The US Fed is expected to end its bond purchases before mid-2022 and raise its key interest rates six times by 0.25% each between June 2022 and the end of 2023. The ECB will reduce its bond purchases in 2022 with less inflationary pressure but will not end them until spring 2023. The first ECB interest rate steps in June and December 2023.

GDP and inflation forecasts (%)

		GDP growth			Inflation		
	Share	2021	2022	2023	2021	2022	2023
World	100.0	2.8	3.9	3.1			
USA	24.5	5.5	4.1	3.3	4.6	4.2	3.1
China	16.4	8.0	5.2	5.1	0.8	1.9	2.3
Japan	5.8	2.2	3.1	1.4	-0.1	1.1	0.7
India	3.3	12.5	6.9	6.8			
Latin America	5.9	4.6	3.1	2.7			
Europe	24.4	4.4	4.6	2.9			
Eurozone	15.3	5.0	4.9	2.9	2.6	2.5	1.9
Germany	4.4	2.7	4.9	2.9	3.2	2.7	2.0
France	3.1	6.8	4.7	2.6	2.1	2.1	1.8
Italy	2.3	6.4	5.0	1.8	1.9	2.4	1.7
Spain	1.6	4.5	6.5	3.3	2.9	2.7	2.0
Other Western Europe							
United Kingdom	3.2	6.8	5.0	2.3	2.4	3.8	2.6
Switzerland	0.8	3.5	2.8	1.6	0.1	0.3	0.8
Sweden	0.6	3.1	3.0	2.3	1.5	1.4	1.7
Eastern Europe							
Russia	1.9	3.8	3.3	2.3	4.5	3.4	3.8
Turkey	0.9	6.0	3.5	3.0	18.5	16.0	13.0

Source: Berenberg

Central bank interest rates



Interest rates in %; dashed: Berenberg forecast; US: Federal funds rate, Eurozone: deposit rate, GB: Bank rate; Sources: Federal Reserve, ECB, BoE, Berenberg; Q1 2001 - Q4 2023.

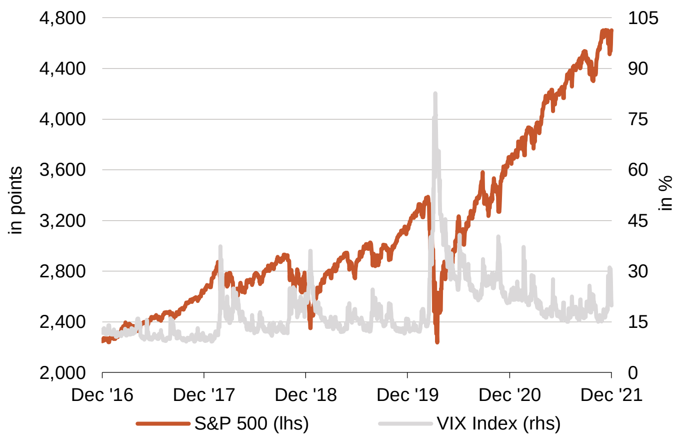
EQUITIES

Seizing opportunities

Equity markets corrected on a more hawkish Fed and Covid 19 concerns.
Growth stocks were able to prove themselves again. but with real rates rising, this is likely to become more difficult.
We have taken advantage of the correction and increased our equity overweight. We remain cautiously optimistic for now.

- **After ever new highs on the stock markets,** there was a sharp sell-off at the end of November. The more transmissible Covid 19 virus variant from South Africa as well as a more hawkish stance by US central bank created a risk-off environment. Both significantly increased uncertainty and fuelled growth concerns. In this environment, cyclical equities lost the most. This is evident at the regional index level. In November, US equities lost 0.7%, while European equities lost more than 2%. In early December, however, it was mainly unprofitable tech stocks that lost value in the context of a more hawkish Fed. Some investors, like us, saw the setback as an opportunity and tactically increased their equity exposure.
- There have also been significant fluctuations in investment styles recently. European **value stocks**, for example, lost just under 4% in November, while **cyclical stocks** lost more than 6%. **Defensive stocks** did not really fare any better, with a loss of around 5%. **Growth stocks** and **large caps**, on the other hand, lost only about 2%. Our high exposure to growth stocks thus helped us to weather the sell-off well.
- **2022** is likely to be characterised by persistent inflation, more normal profit and economic growth, and valuation pressures. Fundamentally, the equity markets therefore offer significantly less potential than in 2021. However, the lack of alternatives, high money holdings, the absence of extreme positioning by systematic investors, and good seasonality at the beginning of the year make us positive for the time being. Therefore, it is important to take advantage of opportunities. We consider this essential in an environment with limited medium-term potential at the index level.
- We position ourselves with a **medium equity overweight** and continue to **tactically supplement our quality-growth exposure with positions of a cyclical nature**.

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 08/12/2016 - 08/12/2021.

Overview of equity markets (short/medium term)

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

		Performance in local currency				
	As of 08/12/2021	ytd	1-year	3-year	P/E	Dividend yield
DAX	15,960	+16.3%	+32.0%	+38.6%	15.4	2.5%
SMI	12,383	+19.0%	+27.5%	+51.4%	19.4	2.6%
MSCI UK	2,039	+16.6%	+30.9%	+12.4%	12.2	4.2%
EURO STOXX 50	4,310	+24.3%	+42.6%	+46.6%	16.9	2.7%
STOXX EUROPE 50	9,055	+23.1%	+35.9%	+38.1%	16.2	3.1%
S&P 500	4,661	+25.5%	+40.3%	+80.6%	22.5	1.3%
MSCI Em. Markets	1,262	-0.3%	+15.3%	+36.9%	13.3	2.8%

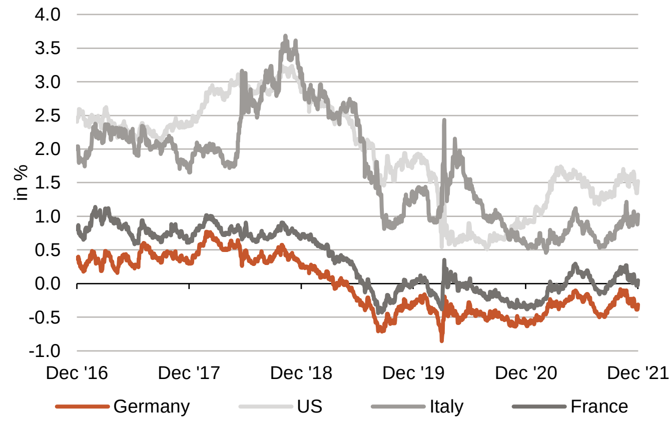
BONDS

Growth concerns dominate

Covid 19 worries and growth concerns caused yields on longer-dated government bonds to fall significantly.
EUR corporate bonds are only conditionally attractive despite widening spreads. Asian corporate bonds under observation.
We underweight bonds and focus on credit risk and off-benchmark themes; duration – short.

- Yields on 10-year **European government bonds** have fallen in recent weeks despite record-breaking inflation figures. Uncertainty about monetary tightening as well as Covid 19 risks and related growth concerns pushed yields down at the long end of the curve. Yield volatility increased significantly. Yields on 10-year **German government bonds**, for example, have fallen about 10 basis points (bps) in the last four weeks. At the short end, seasonal special effects are keeping yields near their lows for the year.
- Yields on 10-year **US government bonds**, on the other hand, are at similar levels to four weeks ago. But here, too, yield volatility was clearly elevated. The yield curve has flattened noticeably in the US despite high inflation expectations and due to the hawkish Fed.
- The **corporate bond market** was also characterised by high inflation figures, central bank rhetoric and COVID-19 fears. Risk premiums have risen across the board in recent weeks. Spreads on **investment-grade corporate bonds** widened by around 10bp, while those on riskier **high-yield bonds** widened by around 15bp. Although yields on EUR corporate bonds are now much more attractive again, we maintain our cautious positioning and wait for the normally supply-intensive start to the year. In **emerging market bonds**, we prefer local currency bonds due to their high yields and low interest rate sensitivity and find **Asian corporate bonds** particularly attractive after the recent stabilisation in China.
- **We underweight bonds**. We maintain our focus on corporate and emerging market bonds and keep duration short.

Yields on 10-year government bonds



Source: Bloomberg, 08/12/2016 - 08/12/2021.

Overview of bond markets (short/medium term)

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

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

		Performance in index currency		
	As of 08/12/2021	ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	255.96	-2.9%	-2.7%	+10.6%
Covered bonds (iBOXX Euro Germany Covered)	203.67	-1.8%	-1.9%	+2.8%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	161.74	-0.8%	-0.2%	+7.8%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	160.59	-0.5%	+0.3%	+6.3%
Emerging market bonds (Bloomberg Barclays EM USD Aggregate TR Index Unhedged)	1,264.48	-1.8%	+2.4%	+19.5%
High-yield bonds (Bloomberg Barclays Global High Yield Total Return Index, USD)	1,530.41	+1.1%	+7.9%	+19.2%

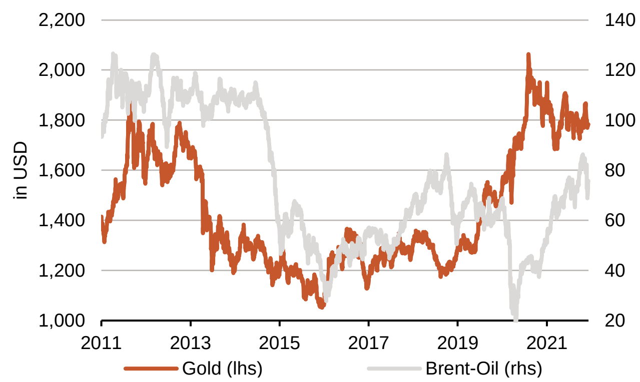
COMMODITIES

Covid worries put commodities under pressure

Strong USD prevents gold appreciation this year.
Crude oil price suffered from covid and economic worries.
Industrial metals await economic signals.

- The sideways movement of **gold** continues. The precious metal is currently caught between high inflation expectations and the strong US dollar, which has prevented a significant appreciation of gold this year.
- **Crude oil** has come under strong pressure in the wake of the increase in new covid infections and the associated uncertainties for the global demand outlook. The sell-off was exacerbated by vulnerable positioning. The oil price should regain ground as the fourth wave of the pandemic subsides. On the supply side, the reluctance to invest is likely to lead to a gradual tightening of supply in the medium term.
- **Industrial metals** fluctuated volatile sideways in November. If we return to a phase of economic expansion in the coming months, which is in line with our expectations, then industrial metals should gain ground again.

Price development



Source: Bloomberg, 01/01/2011 - 08/12/2021.

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

	As of 08/12/2021	Performance ytd	1-year	3-year
Gold USD/ounce	1,770	-6.8%	-7.3%	+43.6%
Silver USD/ounce	23.5	-10.9%	-2.9%	+59.8%
Copper USD/pound	432.1	+22.8%	+39.7%	+53.9%
Brent USD/bbl	81.99	+58.3%	+106.5%	+12.6%

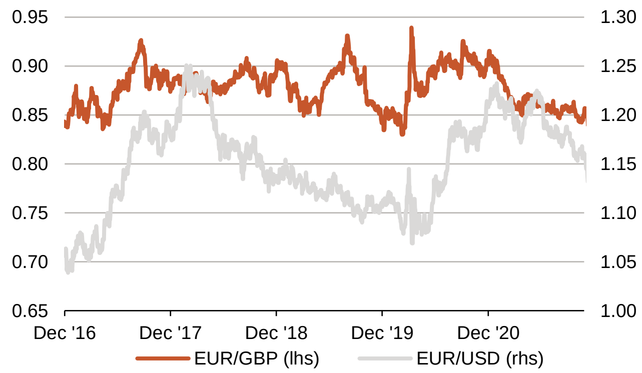
CURRENCIES

Monetary policy divergence weighs on the euro

EUR/USD: Euro weaker than expected.
EUR/GBP: Sideways trend continues.
EUR/CHF: Swiss franc reaches post-2015 high.

- **EUR/USD:** The ECB's wait-and-see attitude is now proving to be a considerable burden for the euro exchange rate. While the US Federal Reserve, the Bank of England and other central banks are initiating a change of course in monetary policy, the ECB is remaining emphatically calm. Since it considers inflation to be temporary, it will keep its key interest rate at 0% well beyond next year. Moreover, at its meeting on 16 December, the ECB is likely to turn its attention back to economic risks because of the current COVID-19 news situation. This would not help the euro exchange rate.
- **EUR/CHF:** The Swiss franc has risen strongly. Nevertheless, the Swiss National Bank has only taken moderate countermeasures. Overall, the unease about the strength of the franc is limited. This is often justified by the significantly higher eurozone inflation, which offsets the exchange rate effect. More importantly, the Swiss economy can now cope with the strong franc.

Exchange rates



Source: Bloomberg, 08/12/2016 - 08/12/2021.

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	→	→

	As of 08/12/2021	Performance ytd	1-year	3-year
EUR/USD	1.16	-4.9%	-0.9%	+2.0%
EUR/CHF	1.06	-2.1%	-1.0%	-7.3%
EUR/GBP	0.85	-5.1%	-5.4%	-3.4%
EUR/JPY	132.38	+4.9%	+8.1%	+2.7%

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
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Robert Reichle | Bonds
Ludwig Kemper | Commodities
Marco Höchst | Commodities
Karsten Schneider | Multi Asset Strategist, Minutes

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