INVESTMENT COMMITTEE MINUTES

13 January 2022

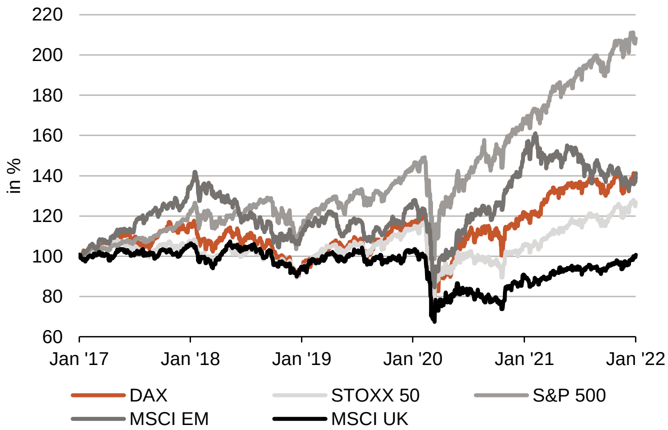
Managers of the Committee

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, 12/01/2017 - 12/01/2022.

Most important assessments at a glance

Economics	• Euro economy takes winter break as omicron and energy costs burden; US economy robust. • Global economy positive in 2022: consumers and companies with pent-up demand. Fewer supply bottlenecks. • Inflation declines in 2022 but remains an issue; central banks tightening policy – the Fed and BoE fast, ECB slow.
Equities	• The start of the year was characterised by interest rate fears and strong style rotation. Europe held up better than the US. • More restrictive central banks in 2022 pose a risk to high valuations such as growth stocks. • We remain cautiously optimistic with a moderate equity overweight, even though the market is likely to remain volatile.
Bonds	• Bond sell-off in response to tighter Fed statements. Yield rise driven by real interest rate rise. • Emerging market bonds caught between economic recovery and rising US interest rates. Spreads have risen. • We underweight bonds and remain cautiously positioned on credit risk. Duration: short.
Commodities	• Gold continues to fluctuate around the USD 1,800 per ounce mark. Rising real interest rates limit upside opportunities. • Rapid recovery in crude oil from Omicron and economic worries. A collapse in demand remains a real risk. • Industrial metals await positive economic signals. Rising energy costs lead to higher production costs.
Currencies	• Monetary policy divergence seems to be priced in. The ECB's hesitant stance has not weighed further on the euro exchange rate. • The pound surprises with a small surge around the turn of the year. The tighter monetary policy is having an effect. • The euro is able to regain ground after being under heavy pressure against the Swiss franc in Q4.

Current market commentary

The start of 2022 was marked by a noticeable rise in nominal and real interest rates, which led to a sell-off in bonds and equities. Both US and German 10-year government bonds reached their highest yield levels since March 2020. This weighed on global growth stocks in particular, which have lost over 3% since the start of the year. Value stocks, on the other hand, which are characterised by a significantly lower valuation level, have been able to make gains. Style volatility will thus continue in 2022 and is unlikely to be over yet, even though we have already seen a major movement. 2022 is likely to be the year of the interest rate turnaround, which should continue to lead to volatility spikes. Nevertheless, we remain cautiously optimistic as economic growth is above trend, earnings growth is positive, investor sentiment is rather pessimistic, systematic investors are underinvested and equities have no alternative. This should ensure further inflows into equities, even though 2022 will be much more challenging than 2021. We are positioning ourselves with a moderate equity overweight with cyclical components.

The rise in bond yields was not unexpected – but the speed surprised many investors. The yield on 10-year German government bonds, for example, has risen by about 30bp in the last four weeks and is now scraping into positive territory. Even if there could be a countermovement in the short term, we do not consider the rise in interest rates to be over yet. However, the market already expects almost four interest rate hikes by the Fed in 2022, which should limit the potential for negative surprises. In this environment, we continue to avoid safe-haven government bonds and focus on special issues and corporate bonds.

For gold, we see limited upside potential due to rising real interest rates. Crude oil remains in demand and industrial metals may see gains in 2022 as well, given high energy costs and therefore production costs.

ECONOMICS

Positive outlook for 2022 – despite inflation and Omicron

Euro economy takes winter break as omicron and energy costs burden; US economy robust.
Global economy positive in 2022: consumers and companies with pent-up demand. Fewer supply bottlenecks.
Inflation declines in 2022 but remains an issue; central banks tightening policy – the Fed and BoE fast, ECB slow.

- **A touch of stagflation:** After a growth spurt in spring and summer, the European economy lost momentum in autumn 2021. Stagnation looms in the winter. The pandemic is burdening parts of the service sector. In addition, the widespread supply bottlenecks are hitting industry-heavy Europe harder than the USA, where the economy is developing strongly. However, some sectors are suffering from labour shortages, more so in the US than in Europe.
- **Positive outlook for 2022:** Employment is rising on both sides of the Atlantic. This supports the incomes of private consumers. The high additional savings that households have built up during the pandemic help them to cushion the expensive 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 slowly ease, growth may surprise positively again in 2022, as it did in 2021. The euro economy should also rebound after the omicron wave, probably in February or March.
- **The Omicron risk**: In the northern hemisphere, omicron has spread rapidly first in the UK and Denmark. In both countries, there are signs that the wave is subsiding again without dramatically overburdening health systems. Despite considerable risks for the coming weeks, this supports the hope that Omicron will not lead to new hard lockdowns in the Eurozone either, despite sharply rising case numbers. Experience with previous waves suggests that many countries could quickly recover short-term losses afterwards. Growth would be pushed back a little, but not out of the picture.
- In **China**, domestic demand is weakening. The government's attempt to limit credit risks contributes to this. But as a capital-rich country with a high savings rate, China can provide stimulus if needed. The US and Europe are not currently dependent on a growing Chinese market as their own domestic demand is robust.
- **High inflation at year-end 2021, declining 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. With the expiry of some special effects, the price climate should calm down again somewhat in 2022, with inflation rates at the end of the year around 2% in the euro area and slightly above 3% in the US. After that, inflation is likely to rise again in the eurozone as well, with higher wage pressure.

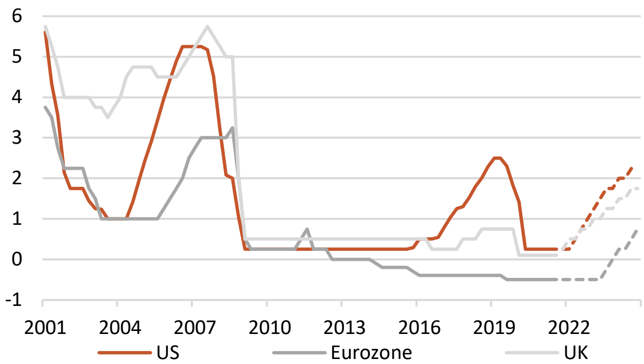
Monetary policy turnaround: US inflation remains well above the Fed's 2% target. The Fed is expected to end its bond purchases in March 2022 and then raise its key rates four times in 2022 and 2023 by 0.25% each. The ECB will reduce its bond purchases in 2022 with less inflationary pressure, but will not end them until early 2023. 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 2024.

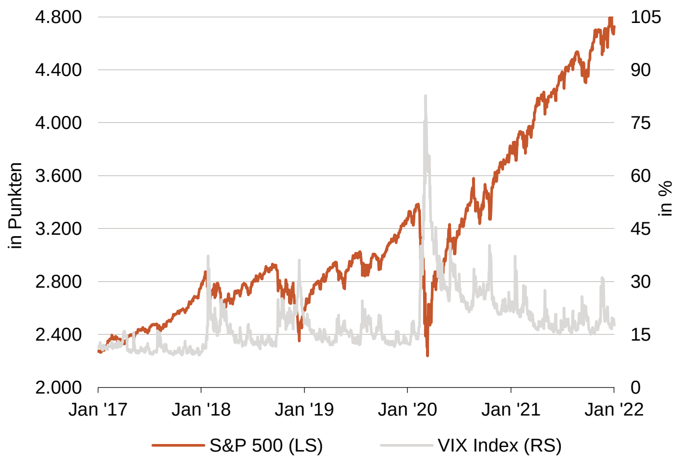
EQUITIES

(Style) volatility shapes the start of the year

The start of the year was characterised by interest rate fears and strong style rotation. Europe held up better than the US. More restrictive central banks in 2022 pose a risk to high valuations such as growth stocks.
We remain cautiously optimistic with a moderate equity overweight, even though the market is likely to remain volatile.

- **After a strong December 2021, the start of 2022 was characterised by volatility in the stock markets.** The rapid rise in real interest rates has weighed on growth stocks in particular. Since the beginning of the year, global growth stocks have lost more than 3%, while value stocks have gained more than 2%. European equities have also held up much better than US equities, partly because the valuation level is significantly lower and thus less susceptible to interest rate movements.
- As we expected, **style volatility** will continue in 2022, the year of more restrictive central banks. The last few days have seen another large and rapid value rotation. European **value stocks**, for example, have gained more than 4% since the beginning of the year, while European **growth stocks** have lost about 4%. At the sector level, the energy sector, with a gain of over 11%, is clearly ahead of the closing light technology sector at -5%. A certain cyclical exposure has thus helped. **Cyclical stocks** were also able to hold up better than **defensive stocks**. **Large caps** fared better than **small caps** in this volatile environment.
- Despite the difficult start to the year, we remain **cautiously optimistic about equities**. The lack of alternatives in equities, above-average economic growth and rising corporate profits should support the markets. Moreover, the equity market is seeing historically strong inflows in January, investor sentiment is far from optimistic and systematic investors remain underinvested. However, valuation headwinds are likely to persist. 2022 is likely to be challenging in any case.
- We are positioning ourselves with a **moderate equity overweight** and continue to tactically add **cyclical positions to our quality-growth exposure.**

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 12/01/2017 - 12/01/2022.

Overview of equity markets (short/medium term)

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

		Performance in local currency				
	As of 12/01/2022	ytd	1-year	3-year	P/E	Dividend yield
DAX	16,010	+0.8%	+14.9%	+14.9%	14.4	2.8%
SMI	1,671	-2.2%	+20.1%	+20.1%	19.0	2.6%
MSCI UK	2,135	+2.6%	+17.4%	+17.4%	12.2	4.0%
EURO STOXX 50	4,316	+0.5%	+22.4%	+22.4%	15.5	2.9%
STOXX EUROPE 50	9,302	+0.3%	+23.6%	+23.6%	15.5	3.1%
S&P 500	4,726	-0.8%	+25.8%	+25.8%	21.5	1.4%
MSCI Em. Markets	1,267	+2.9%	-5.0%	-5.0%	12.9	3.1%

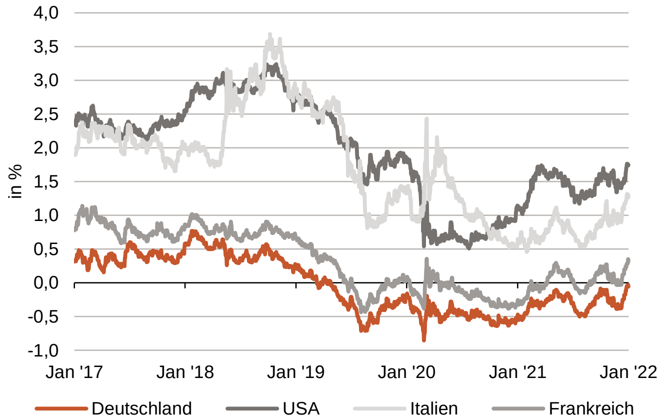
BONDS

Real interest rates on an upward trend

Bond sell-off in response to tighter Fed statements. Yield rise driven by real interest rate rise.
Emerging market bonds caught between economic recovery and rising US interest rates. Spreads have risen.
We underweight bonds and remain cautiously positioned on credit risk. Duration: short.

- The tighter tone of the US Federal Reserve, including in the December Fed minutes, and persistently high inflation readings have led to a sell-off in bonds globally. Markets now expect four rate hikes this year and the start of balance sheet reduction in 2022, but the ECB is unlikely to make the first moves until 2023 at the earliest. Nonetheless, yields on 10-year **German government bonds** reached their highest level since May 2019 at just under 0%.
- In the **US**, the yield on the **10-year government bond** briefly rose to over 1.8%, reaching a high since the beginning of the pandemic. The sell-off in US government bonds was triggered almost exclusively by a rise in real interest rates and not by rising inflation expectations. The yield curve has steepened moderately in the US, even if this has happened from a historically flat level. However, further interest rate movements are likely to be more moderate and slower. Reasons for this are already increased short positions, the already priced interest rate steps and a demand for US government bonds to be kept stable and high by foreign investors and pension funds.
- **Emerging market bonds** are caught between recovery through vaccination progress and rising commodity exports as well as rising US interest rates. We remain loyal to local currency bonds due to rising local interest rates and lower interest rate sensitivity. We also like emerging market corporate bonds from a duration, diversification and carry perspective.
- **We underweight bonds.** We are slightly reducing our duration underweight and remain cautiously positioned on credit risk for the time being as valuations remain expensive.

Yields on 10-year government bonds



Source: Bloomberg, 12/01/2017 - 12/01/2022.

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 12/01/2022	ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	253.15	-0.5%	-3.3%	+7.7%
Covered bonds (iBOXX Euro Germany Covered)	202.40	-0.3%	-2.2%	+1.9%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	160.23	-0.5%	-1.7%	+7.2%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	159.71	-0.4%	-0.8%	+6.7%
Emerging market bonds (Bloomberg Barclays EM USD Aggregate TR Index Unhedged)	1,244.23	-1.8%	-2.1%	+15.0%
High-yield bonds (Bloomberg Barclays Global High Yield Total Return Index, USD)	1,518.15	-0.7%	+0.7%	+17.9%

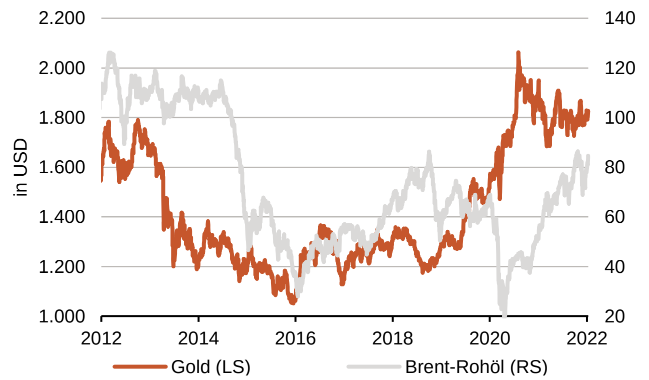
COMMODITIES

Limited opportunities for gold and crude oil

Gold surprisingly robust in view of the rise in interest rates. Opportunities and risks are balanced for crude oil. Economic signals decisive for industrial metals.

- **Gold** was surprisingly robust in the face of the strong rise in real interest rates and continued its sideways movement. This is because part of the interest rate movement was already priced in. However, further increases in real interest rates and decreasing inflation uncertainty limit the upward potential.
- **Crude oil** benefited at the beginning of the year from diminishing Omicron concerns, Kazakhstan unrest and more restrictive Fed statements. A substantial collapse in demand due to Omicron has so far failed to materialise, but remains a real risk as evidenced by declining mobility data and sharply increased gasoline inventories. Together with the decoupling of oil prices from new infections, there is room for disappointment, although this is not our base-case scenario.
- **Industrial metals** held on to sideways movement in recent weeks. On the supply side, high energy prices will lead to higher production costs in 2022. In the medium term, industrial metals should benefit from economic expansion.

Price development



Source: Bloomberg, 01/01/2012 - 12/01/2022.

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

	As of 12/01/2022	Performance ytd	1-year	3-year
Gold USD/ounce	1,826	-0.2%	-1.5%	+41.5%
Silver USD/ounce	23.1	-0.7%	-9.5%	+48.4%
Copper USD/pound	457.7	+2.5%	+26.9%	+71.9%
Brent USD/bbl	84.67	+8.9%	+49.6%	+40.0%

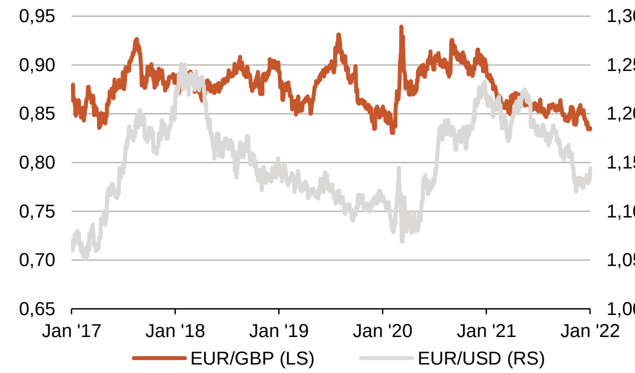
CURRENCIES

EUR/USD bottoms out

EUR/USD: Euro survives ECB meeting unscathed. EUR/GBP: Pound with renewed upswing. EUR/CHF: Euro gains again against the franc.

- **EUR/USD:** The euro has had a difficult time. But now it appears that the common currency has seen its lowest point against the US dollar. Although the US Federal Reserve is tightening its monetary policy more and more and the ECB was still quite hesitant at its December meeting, the euro exchange rate has not suffered any further. The monetary policy divergence seems to have been gradually priced in. The exchange rate has retreated moderately from its low of just under USD1.12 per euro and is now back at a good USD1.14 per euro.
- **EUR/CHF:** The Swiss franc had a bearish fourth quarter of 2021, falling sharply from around 1.08 to 1.03 francs per euro. This pronounced euro weakness took us by surprise and probably went a bit too far. In the first days of the new year, the euro gained a good one and a half cents. That is at least a first step towards more normal exchange rates.

Exchange rates



Source: Bloomberg, 12/01/2017 - 12/01/2022.

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 12/01/2022	Performance ytd	1-year	3-year
EUR/USD	1.14	+0.6%	-6.3%	-0.2%
EUR/CHF	1.05	+0.8%	-3.3%	-7.3%
EUR/GBP	0.84	-0.7%	-6.5%	-6.5%
EUR/JPY	131.16	+0.2%	+3.6%	+5.4%

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
Ulrich Urbahn | Head Multi Asset Strategy & Research
Oliver Brunner | Co-Head Portfolio Management Multi Asset
Ansgar Nolte | Co-Head Portfolio Management Multi Asset
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Ludwig Kemper | Commodities
Marco Höchst | Commodities
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