INVESTMENT COMMITTEE MINUTES

10 February 2022

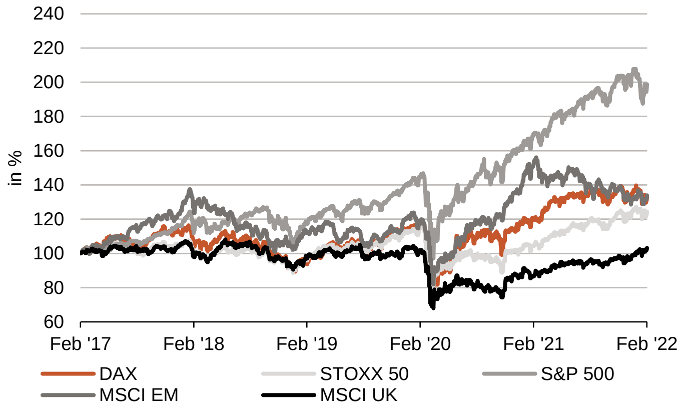
Managers of the Committee

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, 09/02/2017 - 09/02/2022.

Most important assessments at a glance

Economics	• Omicron and high energy costs weigh on the economy in the short term, in Europe more than in the US. Robust upswing from spring: high demand from consumers, companies and countries. Fewer supply bottlenecks. • Inflation remains high, but declines from Q2 – central banks tighten policy; Fed and BoE very quickly, ECB more slowly.
Equities	• Globally, more restrictive central banks caused selling pressure on the equity markets. Russia risk remains. • Fundamentally cheap and defensive equities outperform the market. Balanced portfolio essential in 2022. • We see recovery potential and maintain a moderate overweight in equities. Portfolio hedging will become more important.
Bonds	• Bond sell-off in response to tighter Fed and ECB statements. Government bond exposure still to be avoided. • Corporate bonds suffer from interest rate risks to the economy. Rising spreads make them increasingly attractive. • We underweight bonds and remain cautiously positioned on credit risk. Duration: short.
Commodities	• Gold continues to fluctuate around the USD1,800 per ounce mark. A more restrictive interest rate outlook may lead to price losses. • Crude oil buoyed by lack of demand slump and geopolitical risks. Normalisation remains the base case. • Industrial metals gained on limited inventory and Russia-Ukraine concerns. China provides new tailwind.
Currencies	• ECB President Lagarde's press conference creates good mood for the euro. EUR/USD temporarily rises to almost 1.15. • The pound benefits from tighter monetary policy with an interest rate hike. Post the ECB meeting, however, the euro gains ground. • Initially, the EUR/CHF exchange rate headed for parity, but turned around after the ECB meeting and rose to 1.06.

Current market commentary

Globally, more restrictive central banks – the market expects six interest rate hikes by the Fed in 2022, the ECB is also sounding much more hawkish – as well as the Russia-Ukraine conflict are weighing on markets. Highly valued growth stocks, in particular, came under massive pressure in some cases, while fundamentally favourable value stocks, such as those from the energy or tele-communications sectors, were able to make gains. Defensive stocks were also able to outperform in this volatile environment. Regionally, equities from Europe and especially from the UK fared better than their US counterparts.

There are many indications that the weak phase is merely a cor-rection in a bull market, triggered by a valuation adjustment. A lot has probably already been priced in with regards to interest rate hikes, which is why we see recovery potential for equities in the medium term. The recovery potential is also supported by inflation risks likely to decrease, investor positioning declining significantly, market pessimism being historically high, the Q4 reporting season being solid and equities remaining attractive compared to bonds. However, we think there is a significant market risk in an escalation in the Russian conflict. We are posi-tioning ourselves with a moderate equity overweight with an increased tail risk hedge.

Although yields on safe government bonds have risen noticeably in recent weeks and 10-year German government bonds are again yielding positively, we remain cautious on government bonds. With inflation rates remaining very high, a further rise in yields and thus losses on government bonds cannot be ruled out. If the central banks do indeed raise interest rates significantly, the economy is likely to struggle, which is why spreads on corporate bonds have also risen noticeably recently. Credit risks are thus better paid again.

Gold, however, is holding its own despite the rise in real interest rates and increased geopolitical risks. Crude oil has limited upside opportunities.

ECONOMICS

More growth from spring – despite high oil prices, inflation and Omicron

Euro economy takes winter break, new momentum from spring. Demand remains robust in the US and Europe.
High oil prices push inflation up further in early 2022; inflation falls from April or May.
Central banks react to inflation and tighten policy; Fed and BoE quite abruptly and ECB slower.

- **An uncomfortable winter:** The Delta and Omicron waves of the pandemic are slowing down the recovery, the sharp rise in oil and gas prices is burdening consumers and supply bottlenecks are limiting the growth of industrial production. Despite high demand, the economy is therefore weakening, in Europe more than in the US.
- **Positive outlook from spring:** Employment is rising strongly on both sides of the Atlantic. This supports consumer incomes. The high additional savings that households built up during the pandemic are helping them to cushion the high energy prices. Companies and governments want to invest more. Fiscal policy remains expansionary because of the spending programmes already adopted. If supply bottlenecks slowly dissipate, growth may surprise positively again from spring, as in 2021.
- **The end of the pandemic?** After an explosion of registered Covid infections, the number of cases in the UK, the US and many countries in continental Europe is already falling sharply again. Since Germany has successfully kept the wave flat, it will probably last longer here than elsewhere. So far, the burden of Omicron on health systems has been limited. Many countries are (largely) lifting their restrictions. Thanks also to medical advances, it is becoming apparent that the pandemic is turning into an endemic, which continues to be dangerous, but no longer shapes public life and economic activity.
- Domestic demand is weakening in **China**. But policymakers have begun to stimulate the economy somewhat again. As a capital-rich country with a high savings rate, China can provide greater stimulus if needed. The US and Europe are not currently dependent on a growing Chinese market, as their own domestic demand is robust. But a series of hard lockdowns in China as part of the zero-Covid strategy could exacerbate supply-chain problems and delay the recovery in Europe.
- **High inflation in early 2022, decline thereafter:** Supply bottlenecks, extraordinarily strong demand from US consumers for durable goods and, above all, high energy prices have once again pushed inflation up more than expected in January. With the expiry of some special effects, the price climate should calm down again somewhat from spring onwards, with inflation rates at the beginning of 2023 around 2% in the euro area and around 3.5% in the US. After that, inflation is likely to pick up again in the eurozone as well, with higher wage pressures. Inflation remains an issue.

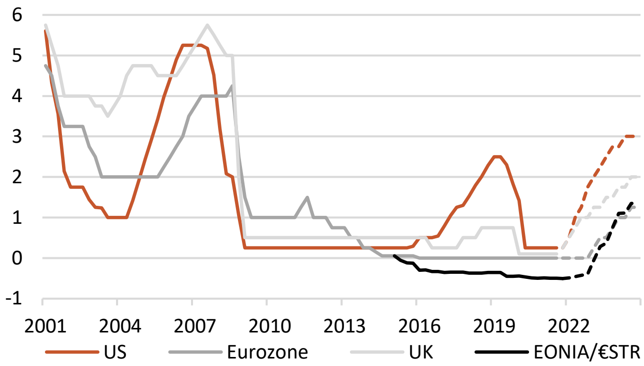
Monetary policy turnaround: US inflation has surprised the Fed again. The Fed is expected to raise its key interest rates rapidly from March 2022, probably with six steps of 0.25% each this year and four more next year. The ECB also initiated the turnaround with a faster reduction of its bond purchases and a first interest rate step by the beginning of 2023 at the latest.

GDP and inflation forecasts (%)

		GDP growth			Inflation		
	Share	2021	2022	2023	2021	2022	2023
World	100.0	4.3	3.4	2.9			
USA	24.5	3.9	3.3	2.7	5.3	3.8	3.5
China	16.4	4.8	4.7	4.3	1.9	2.3	2.3
Japan	5.8	3.4	2.0	1.5	0.5	0.7	0.9
India	3.3	9.0	6.8	6.7			
Latin America	5.9	3.1	2.7	2.4			
Europe	24.4	4.3	2.7	2.1			
Eurozone	15.3	4.5	2.9	2.1	3.5	1.9	2.2
Germany	4.4	4.0	3.1	1.9	3.6	2.0	2.2
France	3.1	4.4	2.8	2.3	2.6	1.9	2.2
Italy	2.3	4.7	2.2	1.5	4.0	1.9	2.1
Spain	1.6	6.6	3.8	2.2	4.3	2.0	2.3
Other Western Europe							
United Kingdom	3.2	4.8	2.5	2.2	5.2	2.5	2.6
Switzerland	0.8	2.8	1.6	1.5	1.1	0.8	0.9
Sweden	0.6	3.0	2.3	2.2	2.2	1.7	2.0
Eastern Europe							
Russia	1.9	3.5	2.3	2.2	6.0	3.8	4.0
Turkey	0.9	3.5	3.0	2.5	24.0	15.0	11.0

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.

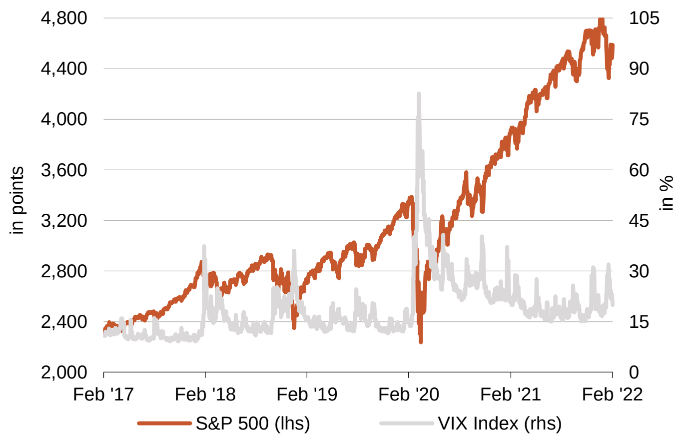
EQUITIES

Correction in a bull market

Globally more restrictive central banks caused selling pressure on the equity markets. Russia risk remains. Fundamentally cheap and defensive equities outperform the market. Balanced portfolio essential in 2022. We see recovery potential and maintain a moderate overweight in equities. Portfolio hedging will become more important.

- **The correction on the stock markets has continued** after the Fed and the BoE have now joined the ECB in adopting a more restrictive tone. Highly valued growth stocks, in particular, came under massive pressure in some cases, while fundamentally favourable value stocks, such as those from the energy or telecommunications sectors, were able to make gains. Regionally, Europe and especially the UK fared better than the US. There are many indications that the weak phase is a correction in a bull market, triggered by a valuation adjustment as a result of rising real yields, while the economy and corporate profits are growing solidly.
- The rally in **growth stocks** was short-lived. **European value stocks** have gained around 1% since mid-January, while **European growth stocks** have lost a good 5%. At the sector level, the energy sector, with a gain of more than 11%, is clearly ahead of the technology sector, which is at the bottom with -9%. In addition, **defensive stocks** (+1%) held up better than **cyclical stocks** (-3%) amid rising growth concerns. **Large-caps** also fared significantly better than **small-caps.**
- Interest rate and geopolitical fears dominate the markets. At least in the case of the former, the market has probably already priced in a lot, which is why we see **recovery potential for equities in the medium term**. This is supported by inflation risks likely diminishing, investor positioning declining significantly, market pessimism being historically high, the Q4 reporting season being solid and equities remaining attractive relative to bonds. However, we think there is a significant market risk in an escalation in the Russian conflict, which is why we believe hedging makes sense.
- We are positioning ourselves with a **moderate overweight in equities** and continue to **tactically supplement our quality growth exposure with balancing positions**.

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 09/02/2017 - 09/02/2022.

Overview of equity markets (short/medium term)

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

		Performance in local currency				
	As of 09/02/2022	ytd	1-year	3-year	P/E	Dividend yield
DAX	15,482	-2.5%	+10.5%	+41.9%	13.8	2.9%
SMI	1,622	-5.0%	+16.9%	+47.2%	18.3	2.7%
MSCI UK	2,169	+4.3%	+23.4%	+19.8%	12.0	3.9%
EURO STOXX 50	4,204	-2.1%	+17.6%	+46.2%	14.8	3.0%
STOXX EUROPE 50	9,199	-0.8%	+22.3%	+41.2%	14.9	3.1%
S&P 500	4,587	-3.6%	+18.9%	+78.3%	20.6	1.4%
MSCI Em. Markets	1,240	+0.7%	-10.0%	+29.3%	12.6	3.1%

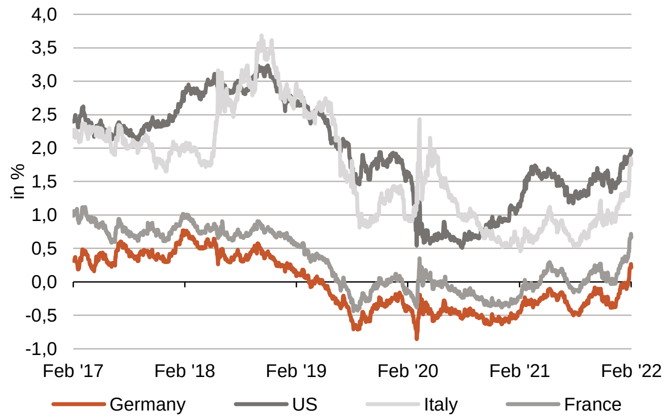
BONDS

Interest rates and risk premiums under pressure

Bond sell-off in response to tighter Fed and ECB statements. Government bond exposure still to be avoided. Corporate bonds suffer from interest rate risks to the economy. Rising spreads make them increasingly attractive. We underweight bonds and remain cautiously positioned on credit risk. Duration: short.

- More restrictive statements by the US Federal Reserve and surprisingly good US labour market data continued to drive the ongoing sell-off in global bond markets. The global stock of negative-yielding bonds has fallen to its lowest level since 2015. Markets now expect six 25 basis point rate hikes in the US this year, with the first 50 basis point rate hike as early as March. The yield on the **10-year US government bond** temporarily rose to 1.96%, its highest level since July 2019.
- Markets are now also pricing in a tighter interest rate policy at the ECB. ECB President Lagarde adopted a tougher tone on inflation risks, setting the stage for a faster pace of tapering as early as March and possibly earlier rate hikes than 2023. The market expects a first rate hike by the ECB in December this year. Yields on **10-year German government bonds** reached their highest level since January 2019 at around 0.23%.
- Risk premiums on **corporate bonds** experienced an upward spike, as a significant tightening of interest rate policy by central banks poses risks to the economy. A slowdown in growth would damage the solvency of companies. Due to the widening of spreads and the rise in interest rates, **credit risks** appear more attractive again, but we remain in a watchful position.
- **Emerging market bonds** are being supported by the economic recovery on the one hand, and are facing headwinds from rising US interest rates on the other hand. We favour **local currency bonds** due to lower interest rate sensitivity.
- **We underweight bonds.** We are positioned with a simple duration underweight and remain neutral on credit risks for the time being.

Yields on 10-year government bonds



Source: Bloomberg, 09/02/2017 - 09/02/2022.

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 09/02/2022	ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	246.37	-3.2%	-5.7%	+4.2%
Covered bonds (iBOXX Euro Germany Covered)	198.24	-2.3%	-4.1%	-1.0%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	155.65	-3.4%	-4.4%	+2.3%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	156.69	-2.2%	-2.9%	+2.6%
Emerging market bonds (J.P. Morgan EMBI Global Diversified unhedged Return EUR)	580.17	-3.8%	+1.3%	+9.1%
High-yield bonds (ICE BofA Global High Yield Index)	442.10	-2.7%	-2.2%	+16.4%

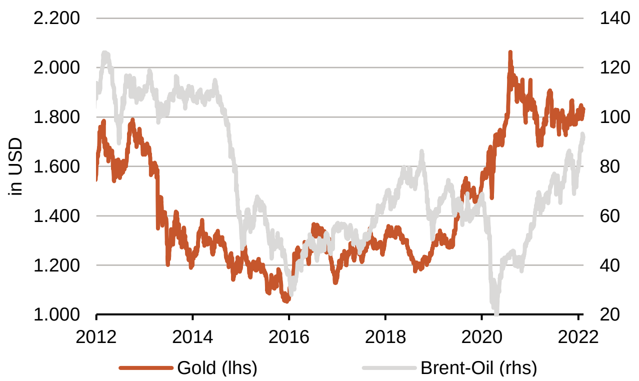
COMMODITIES

Industrial metals with opportunities

Gold remains stable in view of the rise in real interest rates.
Opportunities and risks balance out for crude oil.
China and political risks support industrial metals.

- **Gold** proved resilient despite the strong rise in real interest rates and continued its sideways movement. After the upward pressure thanks to geopolitical risks, however, it had to give up its gains again after the more restrictive Fed statements. Interest rate sensitivity thus persists.
- **Crude oil** has been buoyed since the beginning of the year by robust demand and supply concerns due to the Russia-Ukraine conflict. There was no collapse in demand despite increased Omicron infections. Low inventories, limited production capacity and a lack of investment activity are likely to continue to support the oil price in the short term, in addition to geopolitical risks, but official sources expect and markets are pricing in a normalisation.
- **Industrial metals** have gained since the beginning of the year due to low inventories and geopolitical risks. In addition to ongoing concerns about Russia, the resurgence of economic optimism in China is also providing tailwind for the industrial metals markets.

Price development



Source: Bloomberg, 09/02/2012 - 02/09/2022.

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

		Performance		
	As of 09/02/2022	ytd	1-year	3-year
Gold USD/ounce	1,833	+0.2%	-0.3%	+39.5%
Silver USD/ounce	23.3	+0.0%	-14.5%	+47.3%
Copper USD/pound	460.3	+3.1%	+23.7%	+63.8%
Brent USD/bbl	91.55	+17.7%	+49.9%	+47.4%

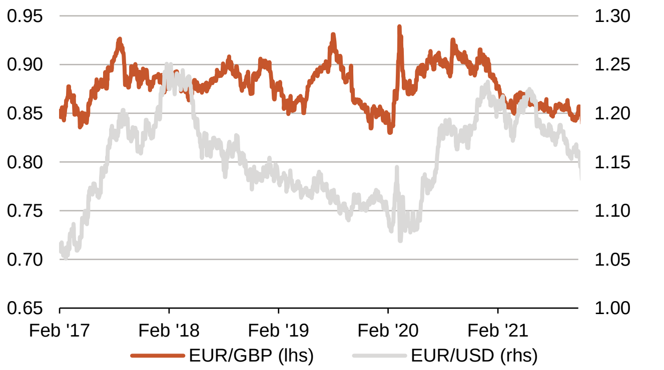
CURRENCIES

ECB President Lagarde turns the tide

EUR/USD: The euro gains strength.
EUR/GBP: ECB surprise dominates.
EUR/CHF: Euro can stop the downturn.

- **EUR/USD:** ECB President Lagarde has softened somewhat after the last monetary policy meeting. Even though monetary policy will continue as planned for the time being, market players took her comments as a signal that the ECB will tighten monetary policy more quickly than previously expected. During the press conference, the euro was therefore able to gain noticeably. Against the US dollar, the exchange rate rose during the press conference from 1.1268 to above the mark of 1.1450 US dollars per euro. Nevertheless, the way up remains rocky for the euro. By the end of the year we forecast it to be at 1.17.
- **EUR/GBP:** The BoE is putting its money where its mouth is and raising the key rate by 25 basis points to 0.50%. In addition, it will no longer reinvest the proceeds from maturing bonds. Nonetheless, the pound's soaring price has been put on hold. Lagarde's surprising statements gave the euro a plus of more than one cent.

Exchange rates



Source: Bloomberg, 09/02/2017 - 09/02/2022.

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	→	↘

		Performance		
	As of 09/02/2022	ytd	1-year	3-year
EUR/USD	1.14	+0.5%	-5.7%	+0.9%
EUR/CHF	1.06	+1.8%	-2.3%	-6.8%
EUR/GBP	0.84	+0.3%	-3.8%	-3.4%
EUR/JPY	131.98	+0.8%	+4.1%	+6.2%

IMPORTANT NOTES

Members of the Investment Committee

Prof Dr Bernd Meyer | Chief Investment Strategist, Chairman
Dr Holger Schmieding | Chief Economist, Vice-Chairman
Matthias Born | Head Portfolio Management Equities
Ulrich Urbahn | Head Multi Asset Strategy & Research
Oliver Brunner | Co-Head Portfolio Management Multi Asset
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Torsten Ziegler | Equities
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Karsten Schneider | Multi Asset Strategist, Minutes

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