BERENBERG *Markets*

INVESTMENT COMMITTEE MINUTES

01 February 2024

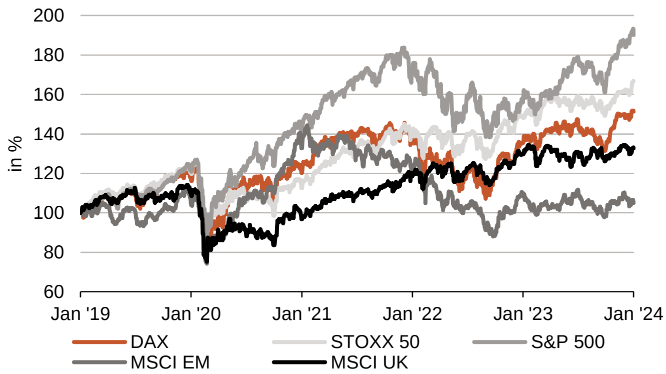
Managers of the Committee

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, 31/01/2019 - 31/01/2024.

Most important assessments at a glance

Economics	• US economy more robust than expected, soft landing ahead. China is slowly stabilising. • Europe: Economy at low point, inventory correction in industry ends at the beginning of 2024, upturn from Easter. • Inflation continues to fall, interest rate turnaround approaches: Fed, ECB and BoE cut interest rates from Q2.
Equities	• Equities with new all-time highs after bumpy start to the year. Market breadth remains low and large caps continue to dominate. • Soft landing scenario remains market consensus. High investor positioning limits upside potential. • We continue to feel comfortable with our balanced positioning. Small caps more attractive again as the economy recovers.
Bonds	• Yields on safe government bonds have risen since the beginning of the year in the face of hawkish central banks. • Increased interest rate volatility on both sides of the Atlantic continues to argue for duration close to neutral. • High yield valuation increasingly unattractive, IG fundamentally well positioned. EM local currency bonds favoured.
Commodities	• Gold remains robust despite the decline in interest rate optimism and continues to offer an attractive addition to the portfolio. • Crude oil rose due to the attacks by the Houthi rebels, but the potential is limited due to sufficient supply. • Chinese stimulus measures support industrial metal prices, rising industrial activity could provide a tailwind.
Currencies	• EUR/USD: Recently dollar strength rather than euro weakness thanks to robust US economy. • EUR/CHF: Slightly stronger since the beginning of the year, but no real trend reversal yet. • Future trends dependent on interest rate policy – European Central Bank sends very mixed signals.

Current market commentary

Equity markets had a bumpy start to the year. Concerns that the interest rate cuts expected by the broad market consensus would be premature and too severe weighed on equity prices. However, the trend reversal following the strong year-end rally was short-lived. The strength of equity markets continued, fuelled by the debate on US QT tapering, the robust US labour market and AI optimism. If the US economy remains robust for longer and the Fed surprises on the dovish side, the strength in equity markets could continue into the typically weak summer season and the run-up to the US elections. However, investor positioning in equities and the risk of higher interest rates for an extended period of time should limit the upside potential.

The bond market also saw a turnaround in bond yields at the turn of the year: The increased probability of a "higher for longer" scenario abruptly ended the decline in bond yields. The recent lack of demand for new issues also put US government bonds under pressure. The renewed rise in oil prices and geopolitical tensions around the Red Sea have recently increased the risk of inflation. This does not make the central banks' situation any easier (recently strong disinflation but rising inflation risks again). Given the optimistic investor sentiment, we are currently comfortable with our broad positioning with overweights in bonds and alternatives.

On the commodities side, gold is proving surprisingly resilient after a consolidation at the start of the year. Given the high geopolitical risks and the low positioning of investors, gold remains an attractive addition to portfolios. Crude oil benefited in the short term from the attacks in the Red Sea, but its fundamental potential remains limited in the medium term. We see upside potential for base metals and copper in particular this year, especially if the manufacturing sector recovers as our economists expect.

ECONOMICS

Interest rate turnaround supports economic hopes

US economy: soft landing ahead, new momentum in the second half of 2024. China is slowly stabilising.
Europe: economy at low point, inventory correction in industry ends in winter, upturn from Easter.
Inflation continues to fall, interest rate turnaround approaches. Fed, ECB and BoE cut interest rates from Q2 2024.

- **A soft landing for the US economy:** Although the US Federal Reserve has slammed on the brakes, the US economy continues to hold up better than expected. Interest-sensitive residential construction has already stabilised after a strong correction. Unlike in previous cycles, companies do not have to correct overcapacity, so they are reducing their investments less than before despite high interest rates. The expansive fiscal policy is supporting demand. However, the labour market is losing some momentum. Overall, there are signs of a soft landing with reduced growth in the first half of 2024 before the economy can pick up speed again. Declining inflation is supporting consumer confidence (chart). While the risk of a recession has decreased further, there is an increasing chance that the economy could surprise on the upside again in the election year 2024.
- **Stagnation in Europe:** After the end of the pandemic-related supply bottlenecks, many companies had built up their stocks too much. In view of unexpectedly weak global trade in 2023, they have been reducing their stocks again since May. As a result, they are currently producing less than they are selling. The recession in industry and residential construction is also weighing on consumer sentiment and demand. Overall, the euro economy is stagnating.
- **New upswing in spring:** However, there are increasing signs that the industry has bottomed out. Companies are less pessimistic than they were three months ago. This suggests that the inventory correction will soon come to an end. Although the purchasing power of consumers has been increasing again since the spring with falling inflation and rising wages, they are holding back on purchases. However, if the economy stabilises in the winter and the news situation improves, they will probably spend more again in the spring and thus give the economy some momentum.
- **China weak:** China's long-term problems (demographics, state control, credit overhang) are becoming increasingly apparent. However, China can and wants to prevent the correction in the property market from triggering a major financial crisis. The data suggests that the situation is stabilising.
- **Inflation declining:** Despite the turmoil in the Middle East, inflation has continued to fall in the USA and Europe. Oil prices have reacted only moderately. For the eurozone, we expect inflation of just under 2% in the summer. In Europe, however, inflation may rise again in 2025 if companies are able to pass on rising labour costs to consumers when the economy improves.

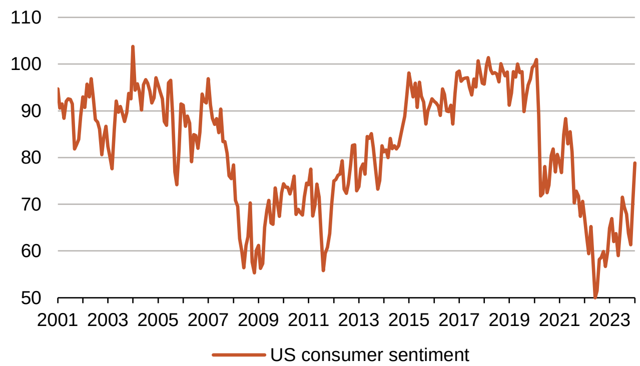
Interest rate turnaround approaching: With inflationary pressure continuing to ease slowly, the US Fed may cut its key interest rate from May 2024, from 5.5% to presumably 4.5% at the end of 2024 and 3.5% at the end of 2025. The ECB will probably follow suit in June at the latest. We now expect a euro money market rate of 3.25% at the end of 2024 and 3.0% at the end of 2025. If wage pressure eases noticeably at the beginning of 2024, the ECB could act as early as April.

GDP and inflation forecasts (%)

		GDP growth			Inflation		
	Share	2023	2024	2025	2023	2024	2025
World	100.0	3.0	2.2	2.5			
US	24.2	2.5	1.8	1.7	4.1	2.8	2.3
China	18.4	5.1	4.3	3.8	0.2	1.7	2.0
Japan	5.2	1.9	0.7	1.1	3.3	2.1	1.9
India	3.3	6.0	6.5	6.0			
Latin America	5.2	2.0	2.2	2.5			
Europe	26.4	1.1	0.8	1.7			
Eurozone	15.2	0.5	0.7	1.7	5.4	2.3	2.3
Germany	4.4	-0.1	0.4	1.6	6.0	2.5	2.3
France	3.1	0.9	0.7	1.7	5.7	2.9	2.5
Italy	2.2	0.7	0.7	1.2	5.9	1.4	2.2
Spain	1.5	2.5	1.8	2.0	3.4	2.3	2.3
Other Western Europe							
United Kingdom	3.2	0.3	0.6	1.7	7.3	2.5	2.1
Switzerland	0.8	0.7	1.1	1.5	2.2	1.5	1.3
Sweden	0.7	-0.5	0.3	2.0	8.5	3.0	2.3
Eastern Europe							
Russia	1.9	2.4	1.5	1.0	6.0	7.0	6.0
Turkey	0.8	4.0	2.5	3.0	54.0	50.0	30.0

Source: Berenberg

The mood is rising: Survey by the University of Michigan



Q1 1966 = 100; non-seasonally adjusted monthly data. Source: University of Michigan

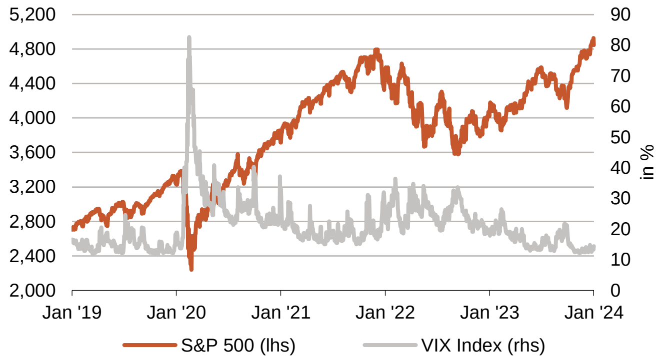
EQUITIES

Equity markets with widening valuations and new all-time highs

Equities with new all-time highs after bumpy start to the year. Market breadth remains low and large caps continue to dominate. Soft landing scenario remains market consensus. High investor positioning limits upside potential.
We continue to feel comfortable with our balanced positioning. Small caps more attractive again as the economy recovers.

- After a bumpy start to the year, the **equity markets** continued the trends of the previous year (low market breadth, large cap growth and tech stocks as the dominant performance drivers) and reached new highs. The S&P 500 even reached a new all-time high in January.
- At European sector level, **technology stocks** have led the way by a clear lead over the last four weeks. **Telecommunications** and **healthcare stocks**, the relative losers of 2023, as well as **cyclical** and **consumer staples** also made slight gains. **Utilities** and **basic materials stocks**, on the other hand, lagged behind. At the style level, **growth stocks** outperformed in Europe over the last four weeks. In Europe and the US, **large caps** also performed better than **small caps**.
- Even if the "Goldilocks" hopes have faded somewhat due to the recent robust US economy and the market's strong expectations of interest rate cuts have been dampened as a result, the consensus on most markets continues to assume a "soft landing" scenario and has already priced this in, at least in part, with an increase in valuations. However, risks such as higher interest rates in the longer term and thus a possible tightening of financing conditions, low market breadth, (overly) high investor optimism, vulnerable positioning and weaker growth prospects in China remain risk factors.
- If US economic data remains robust and the Fed surprises on the dovish side, the strength in equity markets could continue into the typically weak summer season and the run-up to the US elections. However, given the high level of investor positioning in equities and the risk of higher interest rates for some time to come, the upside potential is likely to be limited. For these reasons, we feel currently comfortable with our **broad, balanced positioning**.

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 31/01/2019 - 31/01/2024.

Overview of equity markets (short/medium term)

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

		Total return in local currency				
	As of 31/01/2024	ytd	1-year	3-year	P/E	Dividend yield
DAX	16,904	+0.9%	+11.7%	+25.8%	12.6	3.3%
SMI	3,583	+1.6%	+1.5%	+10.7%	20.2	3.0%
MSCI UK	2,187	-1.2%	+2.0%	+36.7%	11.4	4.0%
EURO STOXX 50	4,648	+3.0%	+15.4%	+46.7%	13.3	3.2%
STOXX EUROPE 50	10,797	+3.0%	+12.3%	+48.2%	14.8	3.2%
S&P 500	9,119	+1.7%	+20.2%	+34.8%	22.8	1.5%
MSCI Em. Markets	976	-4.6%	-2.6%	-20.1%	13.5	3.2%

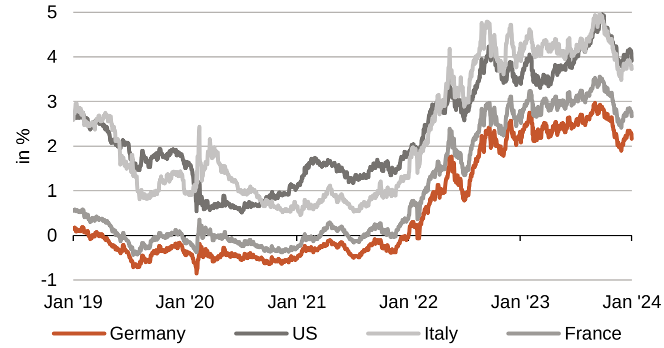
FIXED INCOME

Central banks back in the spotlight, expectations of interest rate cuts recently dampened

Yields on safe government bonds have risen since the beginning of the year in the face of hawkish central banks. Increased interest rate volatility on both sides of the Atlantic continues to argue for duration close to neutral. High yield valuation increasingly unattractive, IG fundamentally well positioned. EM local currency bonds favoured.

- Robust economic data in the USA and rising inflationary risks on both sides of the Atlantic have dampened market participants' expectations of sharp interest rate cuts in the near future since the beginning of the year. Rising real interest rates and inflation expectations, which were once again fuelled by geopolitical tensions in the Red Sea, weighed on **safe government bonds** last month. US government bonds were recently supported by a better-than-expected refinancing announcement by the US Treasury Department. As a result, the yield on **10-year government bonds** in the **USA** was 4.0% and 2.2% in **Germany**. Falling debt ratios and the low level of planned new issues compared to the European core countries, on the other hand, gave government bonds from the peripheral countries a tailwind – the **BTP-Bund spread** narrowed to about 150 bp.
- **Corporate bonds** once again benefited from the further narrowing of spreads in January. In a long-term comparison, the relative valuation of the **IG segment**, combined with solid balance sheets and generous liquidity reserves of most issuers, remains more attractive than the risk premiums in the **HY segment**. The IG segment is also supported by technical factors, above all cash inflows. A short supply of new issues and narrower spreads also supported **emerging market bonds**.
- In the case of safe bonds, we continue to favour **covered bonds and their European counterparts** over government bonds due to the attractive additional yield. In Europe, we favour corporate bonds from the financial sector and avoid cyclical sectors. In emerging markets, we continue to favour the local currency segment. In the hard currency segment, we favour government bonds over IG corporate bonds due to their higher yields and longer duration. Due to the high interest rate volatility, we continue to keep the duration at neutral.

Yields on 10-year government bonds



Source: Bloomberg, 31/01/2019 - 31/01/2024.

Overview of bond markets (medium term)

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

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

	As of 31/01/2024	Performance in index currency ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	221.12	-0.6%	+4.1%	-15.6%
Covered bonds (iBOXX Euro Germany Covered)	185.53	-0.3%	+3.6%	-10.4%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	147.28	-0.2%	+5.7%	-9.6%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	155.20	+0.2%	+6.5%	-3.7%
Emerging market bonds (J.P. Morgan EMBI Global Diversified unhedged Return EUR)	570.91	+0.7%	+6.6%	+0.4%
High-yield bonds (ICE BofA Global High Yield Index)	447.40	+0.1%	+8.9%	-0.3%

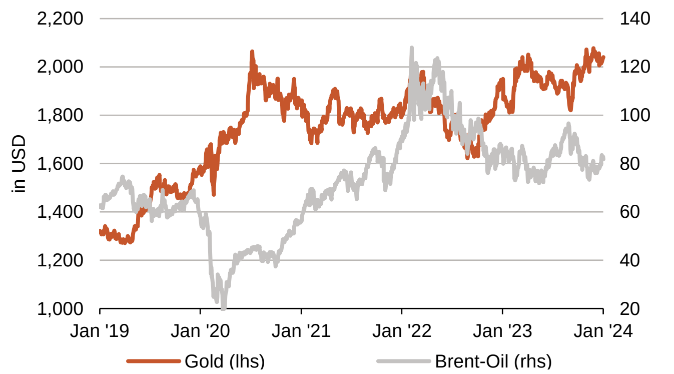
COMMODITIES

Between geopolitics and a robust economy

Gold defies strong US economy.
Crude oil benefits from attacks by Houthi rebels.
Metals supported by hopes of stimulus in China.

- **Gold** is holding up remarkably well in view of the surprisingly strong US economy and the somewhat less optimistic expectations of interest rate cuts in the near future. With investor positioning now low and geopolitical risks high, gold remains an attractive addition to the portfolio.
- **Crude oil** has risen sharply since the beginning of the year. Most recently, attacks by Houthi rebels on oil tankers in the Red Sea have driven up the price. Ships are switching to longer routes, which is driving up delivery times and costs. However, supply remains plentiful thanks to high free capacities, meaning that the potential appears fundamentally limited.
- **Industrial metals** recently benefited from the reduction in the Chinese minimum reserve rate and the surprisingly robust economic data. In addition, "green" demand remains high. Meanwhile, copper producers, for example, are struggling with disruptions. Rising activity in the industry would further support the price trend.

Price development



Source: Bloomberg, 31/01/2019 - 31/01/2024.

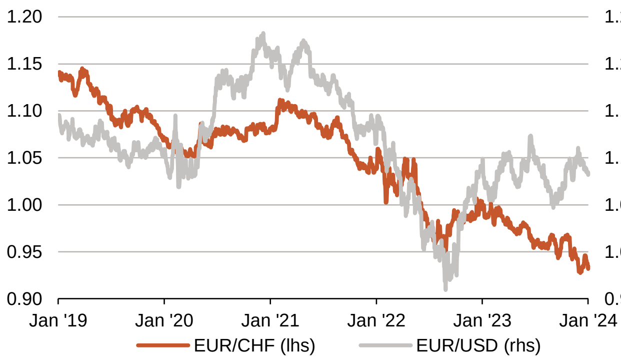
CURRENCIES

US dollar on the rise since the turn of the year

EUR/USD: dollar strength rather than euro weakness.
EUR/GBP: Euro remains at 0.85.
EUR/CHF: Swiss franc strong in long-term comparison.

- **EUR/USD:** The single currency temporarily reached over USD 1.10 per euro, but fell back to 1.08 recently. This movement reflects recent dollar strength rather than euro weakness. The euro remains stable against a broad basket of currencies, while the dollar has appreciated. Future developments will depend on the expected recovery of the euro economy and the timing and extent of interest rate cuts. The European Central Bank has sent mixed signals regarding a first rate cut and although the markets are pricing in 25 basis points for April, June seems more likely.
- **EUR/CHF:** Since the start of the year, the euro has risen slightly to 0.94 against the franc. Compared to the long-term trend of a strengthening franc, however, such corrections are hardly significant. It remains to be seen whether the expected recovery in the eurozone economy over the course of the year will give the euro more lasting support, as we anticipate.

Exchange rates



Source: Bloomberg, 31/01/2019 - 31/01/2024.

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

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 31/01/2024	ytd	1-year	3-year
Gold USD/ounce	2,040	-1.1%	+5.8%	+10.4%
Silver USD/ounce	23.0	-3.5%	-3.3%	-14.9%
Copper USD/pound	390.6	+0.4%	-7.6%	+9.8%
Brent USD/bbl	81.71	+6.1%	-3.3%	+46.2%

		Performance		
	As of 31/01/2024	ytd	1-year	3-year
EUR/USD	1.08	-2.0%	-0.4%	-10.9%
EUR/CHF	0.93	+0.3%	-6.4%	-13.8%
EUR/GBP	0.85	-1.7%	-3.3%	-3.7%
EUR/JPY	158.95	+2.1%	+12.5%	+25.0%

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
Daniel Sutter | Equities
Felix Stern | Fixed Income
Ludwig Kemper | Commodities
Philina Kuhzarani | Minutes
Dr Konstantin Ignatov | Minutes
Katharina Finken | Minutes

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Date: 01 February 2024

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