BERENBERG
Markets

INVESTMENT COMMITTEE MINUTES

25 July 2024

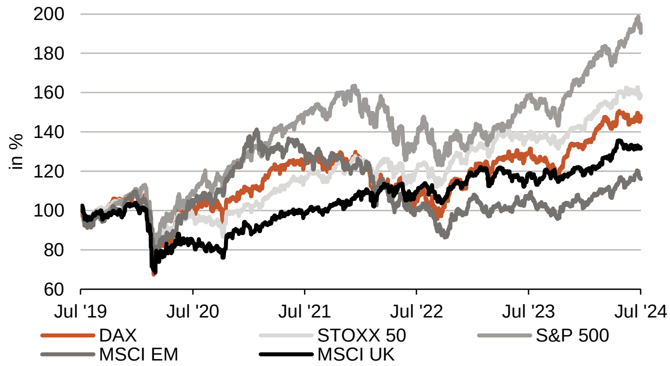
Managers of the Committee

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, 24/07/2019 - 24/07/2024.

Most important assessments at a glance

Economics	• Hesitant upturn in Europe, economic slowdown in the USA, China's growth disappointing. • Inflation rates are only declining very slowly, but are likely to fall slightly in the coming months. • In September, the ECB is expected to cut its key interest rates again and the Fed will also herald a turnaround in interest rates.
Equities	• The equity markets have recently gained significantly in breadth, with a rotation towards small caps. • The reporting season will shed light on whether market breadth could widen further on fundamental grounds. • High index levels, US elections, reporting season and seasonality argue for a small underweight in equities in the short term.
Bonds	• Following the ECB's interest rate pause in July, the markets expect the ECB and the Fed to cut interest rates in September. • Increased rate volatility and inverse rate structure on both sides of the Atlantic continue to favor duration close to neutral. • IG segment valued more attractively than high-yield bonds. EM local currency bonds preferred.
Commodities	• Gold at all-time high, but drivers have recently turned around. Interest from financial investors increases as interest rates fall. • Crude in solid starting position despite economic pessimism, but remains sideways for now on reactive OPEC+. • Industrial metals suffer from China's weakness. However, supply remains tight. Recent weakness offers catch-up potential.
Currencies	• Recently, the euro has risen slightly due to diminishing French risk and possibly an earlier interest rate turnaround in the US. • There could be short-term fluctuations in the euro-dollar exchange rate around the US presidential elections. • Overall, however, we expect the exchange rate to move sideways until the end of the year.

Current market commentary

The stock markets were characterised by a strong rotation in July. The S&P 500 initially benefited from positive seasonality in early July, the Russell 2000 traded at a record low against the Nasdaq, at a 23-year low against the S&P 500, and US market breadth was at a 20-year low. Cooler US inflation data then triggered a significant market rotation last week - away from megacaps, technology, growth and momentum in favour of small caps and value. Market breadth improved accordingly, and the equally weighted S&P outperformed. Hopes of a soft landing, expectations of an imminent interest rate turnaround by the US Federal Reserve and the rise of the 'Trump trade' contributed to the market narrative. Nevertheless, a major debate centres on the sustainability of these rotations, which could depend to a large extent on the fulfilment of earnings expectations of big tech companies and an increase in market breadth in the course of the current reporting season. In addition, the high overall positioning in equities, weak summer seasonality and upcoming US elections harbour risks. We therefore feel comfortable with a positioning close to but below neutral over the summer.

The cooler US inflation figures and a return of calm after the French elections led to declines in yields on safe government bonds on both sides of the Atlantic. We are maintaining our preference for covered bonds over government bonds, EUR-IG financial bonds and emerging market bonds from the local currency segment.

Gold has performed on a par with US equities since the start of the year (in EUR, vs. S&P 500 TR). Initial US interest rate cuts and rising investor demand should support gold. Crude oil's supply-demand structure currently appears balanced, making a continuation of the sideways movement likely. The long-term trend for industrial metals remains intact despite the current weakness in China.

ECONOMICS

Europe in expansion phase, USA lands softly, structural problems in China

Hesitant upturn in Europe, economic slowdown in the USA, China's growth disappointing.
Inflation rates are only declining very slowly but are likely to fall slightly in the coming months.
In September, the ECB is expected to cut its key rates again and the Fed will also herald a turnaround in interest rates.

- **Hesitant upturn in the eurozone:** all the lights are actually green for the European economy. Interest rates are falling, destocking in the manufacturing sector is largely complete and consumer purchasing power is increasing again due to rising wages and falling inflation. So far, however, consumers are still somewhat reluctant to spend, and foreign demand is also still restrained. However, we expect the upturn to accelerate in the second half of the year. In Q3 and Q4, GDP is likely to increase by 0.4% compared to the previous quarter, resulting in an overall increase of 0.8% for 2024.
- **US economy cools down:** Although the US economy is cooling down somewhat, there is no sign of a slump. However, the high interest rates are having an impact on the economy. Economic indicators have recently been weaker than expected. The mood among both purchasing managers and consumers has deteriorated further. For the year as a whole, we expect GDP to grow by 2.3% - which is still slightly higher than the longer-term trend.
- **China is no longer the growth engine:** at 4.7% in the second quarter, Chinese economic growth fell short of expectations compared to the previous year. The official growth target of 5% for this year is receding ever further into the distance. Influenced by the experiences of the pandemic and the end of a long property boom, pessimistic consumers are holding back on spending. In addition, China's long-term problems (demographics, state control, credit overhang) are becoming increasingly apparent. However, the government and the central bank will not allow a major economic crisis to develop and will continue to intervene in a targeted manner to prevent a more severe slump.
- **Slow decline in inflation:** Falling commodity and food prices and persistent price pressures in services have kept core inflation above headline inflation in both the eurozone and the US. Price pressure is likely to ease further in both economic areas in the coming months, with the inflation rate in the US levelling off at a slightly higher level than in the eurozone. However, rising wages due to labour shortages are expected to increase inflationary pressure again on both sides of the Atlantic from 2026 at the latest.

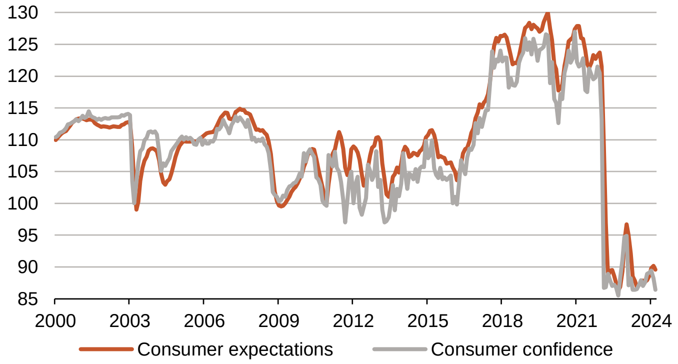
ECB likely to cut interest rates again, Fed to follow suit: While the ECB is expected to cut its key interest rate for a second time by 25 basis points in September, the Fed is likely to follow suit with its first rate cut six days after the ECB meeting. We expect key interest rates to fall to 3.0% in the eurozone and to 4.25 – 4.50% in the US by summer 2025.

GDP and inflation forecasts (%)

		GDP growth			Inflation		
	Share	2024	2025	2026	2024	2025	2026
World	100.0	2.4	2.5	2.6			
US	26.1	2.3	1.7	2.0	3.0	2.5	2.6
China	16.9	4.7	4.2	4.2	0.5	1.8	2.0
Japan	4.0	-0.2	1.2	1.1	2.4	2.0	1.7
India	3.4	7.0	6.5	6.0			
Latin America	6.3	2.2	2.5	2.6			
Europe	24.3	1.0	1.7	1.6			
Eurozone	14.8	0.8	1.6	1.5	2.4	2.2	2.4
Germany	4.3	0.2	1.4	1.3	2.4	2.3	2.4
France	2.9	0.9	1.3	1.4	2.5	2.2	2.4
Italy	2.2	1.0	1.3	1.2	1.1	2.0	2.3
Spain	1.5	2.3	2.0	2.1	3.3	2.6	2.6
Other Western Europe							
United Kingdom	3.2	1.0	1.6	1.7	2.6	2.4	2.5
Switzerland	0.8	1.4	1.5	1.5	1.4	1.3	1.5
Sweden	0.6	1.0	2.0	2.0	3.0	2.2	2.5
Eastern Europe							
Russia	1.9	2.3	1.1	0.5	7.0	6.0	6.0
Turkey	1.1	2.9	3.0	2.5	56.0	28.0	20.0

Source: Berenberg

Chinese consumers - chronically pessimistic



100+ = optimistic. Monthly data. Source: CNBS

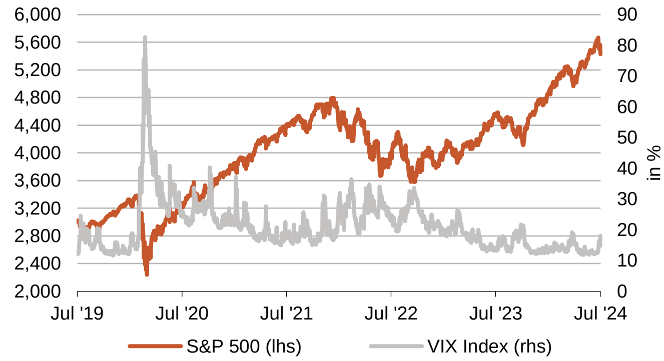
EQUITIES

Stock markets gain in breadth

The equity markets have recently gained significantly in breadth, with a rotation towards small caps.
The reporting season will shed light on whether market breadth could widen further on fundamental grounds.
High index levels, US elections, reporting season and seasonality argue for a small underweight in equities in the short term.

- At the beginning of July, the S&P 500 recorded its longest winning streak since November 2023. Last week, market breadth was once again on the rise. The market rotation out of mega-cap and technology stocks and into small caps was triggered by the fall in the US consumer price index to a three-year low in June, which fuelled expectations of an interest rate cut in September. Despite strong performance in the first two weeks of July, the S&P 500 and Nasdaq fell slightly over the four-week period. In contrast, the equally weighted S&P 500 and Russell 2000 rose.
- At a sector level, European stock markets showed a mixed picture. **Telecommunication**, **financial** and **utility** stocks rose. In contrast, information technology stocks fell sharply, weighed down by Biden's announcement to restrict sales of high-value semiconductors to China. At a style level, European **value** stocks rose while European **growth** stocks fell.
- Despite the market rotation, investors' overall equity positioning remains high. The recent rally in small caps has been driven by retail investors and short covering. Looking ahead, however, technical factors are unlikely to be the main drivers. Instead, we believe that the current Q2 reporting season will be crucial for the further development of market breadth in the US. In Europe, the discount due to political uncertainty has not yet been priced out, even after the French elections, and investors have recently continued to reduce their European positions, which could offer catch-up potential. Given the US elections in November, the high index levels, the ongoing reporting season and the unfavourable seasonality in August, we feel comfortable with a small underweight in equities.

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 24/07/2019 - 24/07/2024.

Overview of equity markets (short/medium term)

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

	As of 24/07/2024	Total return in local currency ytd	1-year	3-year	P/E	Dividend yield
DAX	18,387	+9.8%	+13.6%	+17.3%	13.4	3.2%
SMI	3,899	+10.6%	+9.4%	+2.2%	19.4	3.0%
MSCI UK	2,330	+7.6%	+10.6%	+32.8%	12.0	3.9%
EURO STOXX 50	4,862	+10.6%	+14.6%	+31.0%	13.6	3.4%
STOXX EUROPE 50	11,610	+10.7%	+14.2%	+35.3%	14.9	3.3%
S&P 500	10,263	+14.4%	+20.4%	+27.1%	22.6	1.4%
MSCI Em. Markets	1,082	+7.7%	+9.8%	-9.6%	13.1	2.8%

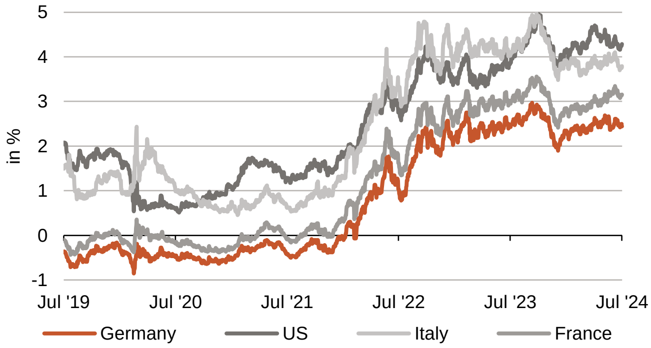
FIXED INCOME

ECB leaves interest rates unchanged as expected, but opens the door for the September rate cut

Following the ECB's interest rate pause in July, the markets expect the ECB and the Fed to cut interest rates in September. Increased rate volatility and inverse rate structure on both sides of the Atlantic continue to favor duration close to neutral. IG segment valued more attractively than high-yield bonds. EM local currency bonds preferred.

- A weaker labour market and lower-than-expected inflation data in the **US** raised market participants' hopes of the Fed's first interest rate cut this year as early as September, with the yield on 10-year **US government bonds** recently standing at 4.23%. Following the better than feared results of the early parliamentary elections in France, the yield on 10-year **German government bonds** recently fell to 2.42%, with the yield curve steepening primarily at the short end in the last month. However, inflation remains a risk factor for the path of interest rate cuts in both the US and Europe, particularly in view of Donald Trump's possible return to the White House. The uncertainty of the rate cut paths continues to cause interest rate volatility and inverted yield curves on both sides of the Atlantic.
- **IG corporate bonds** continue to offer historically more attractive valuations on a spread basis compared to the high-yield segment. Like July, the month of August continues to represent a seasonal opportunity for **corporate bonds** due to the low volume of new issues and low market liquidity. Both the high-yield and IG segments continue to be supported by positive inflows of funds. In **emerging markets**, high-yield hard currency bonds from commodity-exporting countries offer attractive carry due to solid trade balances.
- When it comes to safe bonds, we continue to favour **covered bonds** over government bonds. In Europe, we favour financial bonds from the IG segment. In **emerging markets**, we continue to favour the local currency segment and in hard currency government bonds over corporate bonds due to the higher spreads and attractive carry. Due to interest rate volatility, we continue to leave the duration at the overall bond level at neutral.

Yields on 10-year government bonds



Source: Bloomberg, 24/07/2019 - 24/07/2024.

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	→	→

		Performance in index currency		
	As of 24/07/2024	ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	220.66	-0.8%	+3.5%	-15.1%
Covered bonds (iBOXX Euro Germany Covered)	186.65	+0.3%	+4.2%	-9.5%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	148.47	+0.6%	+5.6%	-9.4%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	158.08	+2.1%	+7.0%	-2.3%
Emerging market bonds (J.P. Morgan EMBI Global Diversified unhedged Return EUR)	598.26	+5.5%	+11.4%	+1.0%
High-yield bonds (ICE BofA Global High Yield Index)	466.93	+4.4%	+11.0%	+1.7%

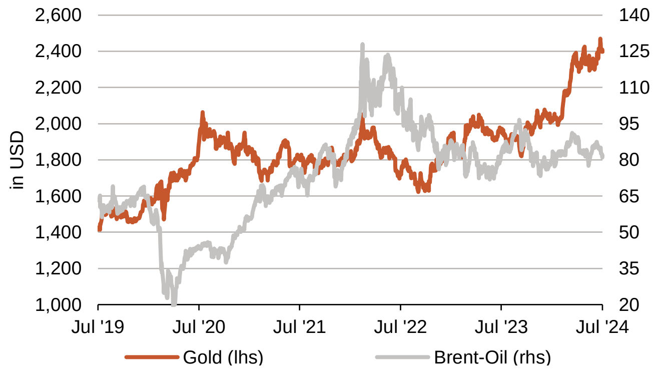
COMMODITIES

In particular (precious) metals with potential

Gold regains the interest of financial investors.
Oil remains in a sideways trend with reactive OPEC+.
Metals remain in short supply despite China's weakness.

- **Gold** broke out to new all-time highs in July. However, unlike at the beginning of the year, the tailwind did not come from central bank purchases - the PBoC recently paused its gold purchases for the first time since the end of 2022. Instead, the momentum in ETF flows finally seems to be turning. With a view to interest rate cuts in the near future, falling real interest rates, high government debt and numerous (geo)political risks, we remain constructive on gold in the medium term.
- **Crude oil** (Brent) has fallen sharply in recent weeks on weaker economic data from the West, particularly China. However, the fundamentals appear to be sound. This is also indicated by the typical seasonal trend in inventories. Given the reactive production policy of OPEC+, a continuation of the sideways movement seems most likely for the time being.
- **Industrial metals** also suffered significantly from the bad news from China. However, supply is likely to remain tight, meaning that metals offer catch-up potential.

Price development



Source: Bloomberg, 24/07/2019 - 24/07/2024.

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

	As of 24/07/2024	Performance ytd	1-year	3-year
Gold USD/ounce	2,398	+16.2%	+22.7%	+33.0%
Silver USD/ounce	28.9	+21.5%	+18.7%	+14.8%
Copper USD/pound	409.9	+5.4%	+6.7%	-7.0%
Brent USD/bbl	81.71	+6.1%	-1.2%	+10.3%

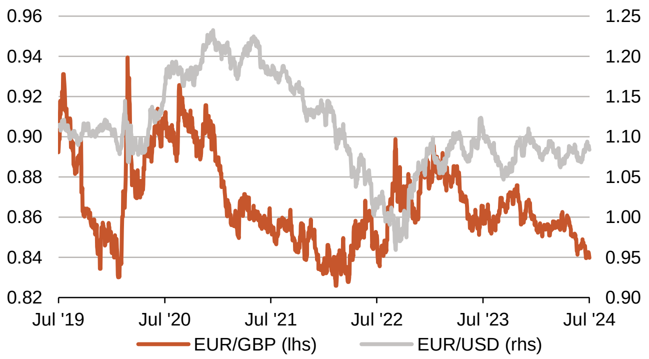
CURRENCIES

Joint descent from the interest rate peak priced in

The easing of risks in France and the turnaround in the US towards a September rate cut have recently given the euro a slight boost.

- **Euro recently with a slight tailwind:** The euro has recovered somewhat against the US dollar in recent weeks. The fact that there are no clear majorities in the new French parliament has also had a positive effect on the euro, making major spending increases appear less likely. This reduces the likelihood of a financial crisis in the eurozone's second-largest economy. In addition, the market has priced in earlier and stronger interest rate cuts by the Fed for 2024 due to the easing price pressure in the US, which will narrow the interest rate differential with the eurozone sooner.
- **Fed joins ECB in cutting interest rates:** The fact that the Fed will join the ECB in cutting interest rates from September has already been priced into the markets and will hardly move the euro-dollar exchange rate. Although the exchange rate could fluctuate somewhat around the US presidential elections, we expect it to move sideways at USD 1.08 per euro until the end of the year.

Exchange rates



Source: Bloomberg, 24/07/2019 - 24/07/2024.

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 24/07/2024	Performance ytd	1-year	3-year
EUR/USD	1.08	-1.8%	-2.0%	-7.9%
EUR/CHF	0.96	+3.3%	-0.3%	-11.3%
EUR/GBP	0.84	-3.1%	-2.6%	-1.9%
EUR/JPY	166.81	+7.1%	+6.6%	+28.2%

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
Dejan Djukic | Head Portfolio Management Multi Asset
Oliver Brunner | Head Multi Asset Income & ESG
Dr Felix Schmidt | Economics
Marco Höchst | Equities
Wei Lon Sung | Fixed Income
Ludwig Kemper | Commodities
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