BERENBERG Markets

INVESTMENT COMMITTEE MINUTES

12 September 2024

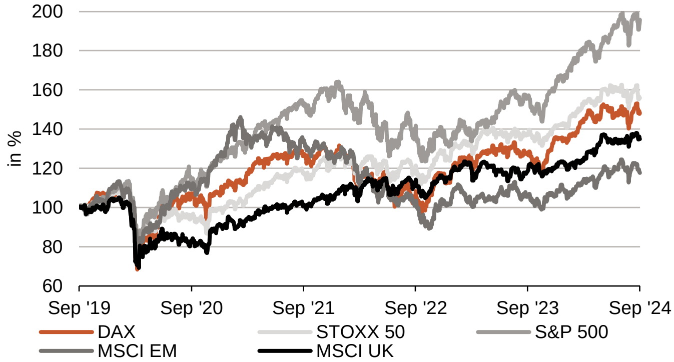
Managers of the Committee

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, 11/09/2019 – 11/09/2024.

Most important assessments at a glance

Economics	• Moderate growth in the eurozone, additional momentum not expected until 2025. • The US economy is slowly cooling down and preparing for a soft landing. • Relatively slow steps expected by the ECB and the Fed on the way down from the interest rate summit.
Equities	• Recession fears, negative seasonality and unwinding of carry trades led to a sell-off in early August • Positive economic and central bank signals, share buyback programmes and low volatility led to a rally. • Negative seasonality and US elections pose risks. Counter-cyclical trading and balanced positioning were favoured.
Bonds	• While a rate cut by the Fed in September is almost certain, the size of the move remains unclear. • Increased interest rate volatility on both sides of the Atlantic argues for duration close to neutral. • IG and HY risk premiums recently widened slightly due to recession concerns. EM local currency bonds still preferred.
Commodities	• Gold at all-time high, but drivers have recently turned. Interest from financial investors increases as interest rates fall. • Crude oil in a solid starting position despite economic pessimism. Negative outlook seems to be priced in. • Industrial metals suffer from weakness in industry. First signs of strength under the surface, especially in China.
Currencies	• The start of the US interest rate turnaround is likely to weaken the US dollar. • There could be short-term fluctuations in the euro-dollar exchange rate around the US presidential elections. • The SNB and ECB moving in lockstep leads to a sideways movement of the euro-franc exchange rate.

Current market commentary

Equity markets completed a V-shaped recovery in August. Fears of a US recession and the unwinding of carry trades initially led to increased volatility and a broad sell-off of risky assets in early August. However, reassuring central bank statements, positive economic data, share buybacks and low volatility led to a rapid recovery in the markets. By the end of August, the S&P 500 was even close to its all-time high. However, even this recovery rally was short-lived. Renewed negative economic surprises fuelled recession fears and led to falling equity markets and interest rates. Defensive and interest-rate sensitive equity sectors outperformed. Cyclical sectors such as automobiles and semiconductors were among the recent losers. Looking ahead, an increased risk of setbacks due to the blackout period ahead of the Q3 reporting season and the US presidential election is likely to weigh on markets from mid-September. In addition, the last two weeks of September are historically the weakest two weeks of the calendar year. We intend to remain counter-cyclical and believe that a balanced positioning is appropriate.

Recent growth concerns have also been reflected in falling bond yields. Yields on 10-year US and German government bonds are now below 3.7% and 2.2% respectively. There is now (too) much interest rate optimism in the bond markets. If our baseline scenario (no recession but slowing growth) materialises, equities and bonds are likely to converge from both sides, meaning that both investments should generate limited positive returns. A neutral duration positioning and an overweight in corporate bonds (high quality) seem appropriate.

On the commodity markets, gold's momentum appears to be unbroken. The precious metal has reached new all-time highs thanks to rising demand from Western financial investors. The cyclical commodities of crude oil and industrial metals require a constructive economic outlook for sustained upside potential.

ECONOMICS

Moderate growth in the eurozone, Germany treads water, USA lands softly

Moderate growth in the eurozone, additional momentum not expected until 2025.
The US economy is slowly cooling off and is making a soft landing.
The ECB and Fed come out of the interest rate summit together.

- **New growth impetus for the eurozone not until 2025:** The eurozone economy has come through the first half of the year much better than we had expected. This was mainly due to the southern member states, where a mix of reforms, a slightly expansive fiscal policy (partly based on EU funds) and booming tourism supported the economy. However, the current leading economic indicators do not suggest that economic growth in the eurozone will accelerate significantly in the second half of the year. At the beginning of next year, however, the European Central Bank's key interest rate cuts could provide new impetus for the economy. The fact that falling inflation and rising real wages will encourage consumers in the eurozone to spend more money again in the medium term will also have a positive effect.
- **Growth in the eurozone without Germany:** The economic slump in Germany continues and is increasingly proving to be a drag on growth in Europe. There are many reasons for the weak performance of the largest economy in the eurozone. Firstly, global demand continues to weaken, which is hitting Germany particularly hard as an export nation. In addition, Chinese products are increasingly competing with German products on the global sales markets. Political uncertainty, restrictive financial policies and labor shortages are also having a negative impact. In the coming year, however, falling interest rates and rising real wages should help the German economy to overcome stagnation.
- **The USA makes a soft landing:** US economic growth once again surprised on the upside in the first half of 2024 thanks to an expansive fiscal policy and robust private consumption. However, the restrictive monetary policy is also leaving its mark in the US. In particular, the previously overheated labor market, residential construction and industry have recently cooled down. Fiscal policy will remain expansive, but no major new fiscal packages are expected. This is because neither party is likely to win the White House in the US elections and gain control of both chambers of Congress at the same time. The adoption of new major fiscal packages after the elections therefore seems unlikely from today's perspective. All in all, a certain weakening of the US economy is therefore to be expected in the coming months.

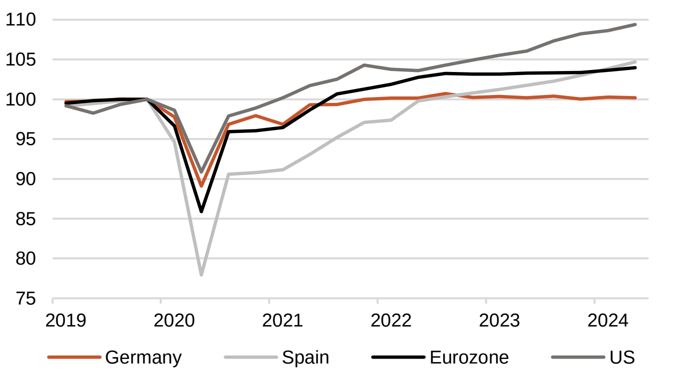
Joint descent from the interest rate peak: The Fed is likely to follow the ECB on September 18 and also make its first rate cut. We expect both central banks to proceed slowly in order to avoid a resurgence of inflation. We expect key interest rates to fall to 2.75% in the eurozone and 4.00-4.25% in the US by summer 2025.

GDP and inflation forecasts (%)

		GDP growth			Inflation		
	Share	2024	2025	2026	2024	2025	2026
World	100.0	2.5	2.5	2.6			
US	26.1	2.5	1.5	2.0	2.9	2.3	2.4
China	16.9	4.7	4.2	4.2	0.5	1.8	2.0
Japan	4.0	-0.1	1.2	1.1	2.5	1.9	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	1.5	1.6			
Eurozone	14.8	0.8	1.4	1.6	2.4	2.2	2.4
Germany	4.3	0.0	0.8	1.3	2.2	2.5	2.3
France	2.9	1.1	1.3	1.4	2.6	2.2	2.4
Italy	2.2	0.8	1.2	1.2	1.2	2.1	2.3
Spain	1.5	2.8	2.2	2.1	3.0	2.6	2.6
Other Western Europe							
United Kingdom	3.2	1.1	1.6	1.7	2.6	2.5	2.5
Switzerland	0.8	1.3	1.5	1.5	1.4	1.3	1.5
Sweden	0.6	0.9	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

The German economy is treading water



Development of real GDP since Q4 2019. Q4 2019 = 100. quarterly data. Source: Eurostat, BEA, Destatis

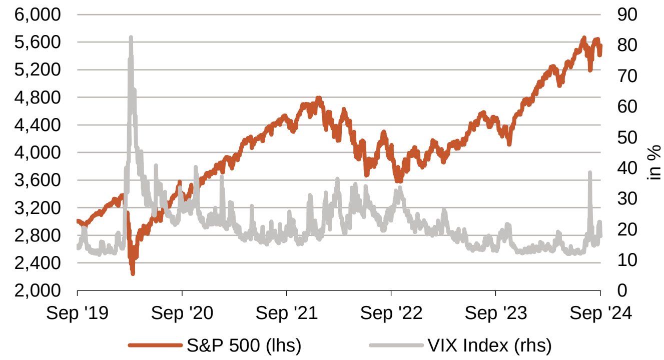
EQUITIES

Anti-cyclical trading favoured

Recession fears, negative seasonality and unwinding of carry trades led to a sell-off in early August
Positive economic and central bank signals, share buyback programmes and low volatility led to a rally.
Negative seasonality and US elections pose risks. Counter-cyclical trading and balanced positioning were favoured

- Equity markets staged a V-shaped recovery in August. Fears of a US recession and the unwinding of carry trades initially led to increased volatility and a broad sell-off in risky assets at the beginning of the month. However, reassuring central bank statements, positive economic data, share buybacks and low volatility led to a rapid recovery in the markets. By the end of August, the S&P 500 was back at its all-time high and equity markets ended the month on a broadly positive note. Market breadth has also increased over the past two months. However, the recovery rally was short-lived. Renewed negative economic surprises in early September stoked recession fears and led to renewed falls in equity markets and interest rates.
- Defensive and rate-sensitive equity sectors outperformed in Europe over the last four weeks. Cyclical stocks continued to underperform defensive stocks. The European Financials, Telecommunications and Utilities sectors led the way over the last four weeks, while Energy - also in the wake of the recent oil price weakness - and IT brought up the rear. Value stocks outperformed growth stocks.
- Looking ahead, an increased risk of pullbacks from mid-September onwards due to the blackout period ahead of the Q3 reporting season and the tight race in the US election campaign is likely to weigh on markets. However, some of the potential negative impact of the US election on Europe has already been priced in at index level. Moreover, the last two weeks of September are historically the weakest in the calendar year. Looking ahead to the end of the year, the signs are good for a year-end rally: by then the US election should be decided and the Fed should have started its cycle of interest rate cuts. We intend to remain counter-cyclical and believe that balanced positioning makes sense..

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 11/09/2019 - 11/09/2024.

Overview of equity markets (short/medium term)

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

		Total return in local currency				
	As of 11/09/2024	ytd	1-year	3-year	P/E	Dividend yield
DAX	18,330	+9.4%	+16.0%	+17.4%	13.6	3.1%
SMI	3,813	+8.1%	+8.9%	+0.4%	18.9	3.0%
MSCI UK	2,342	+9.1%	+13.8%	+33.5%	12.1	4.1%
EURO STOXX 50	4,764	+8.4%	+15.7%	+26.5%	13.5	3.4%
STOXX EUROPE 50	11,463	+9.3%	+13.2%	+32.9%	14.8	3.4%
S&P 500	10,518	+17.2%	+25.0%	+28.7%	23.3	1.4%
MSCI Em. Markets	1,059	+5.8%	+11.5%	-11.4%	12.8	2.9%

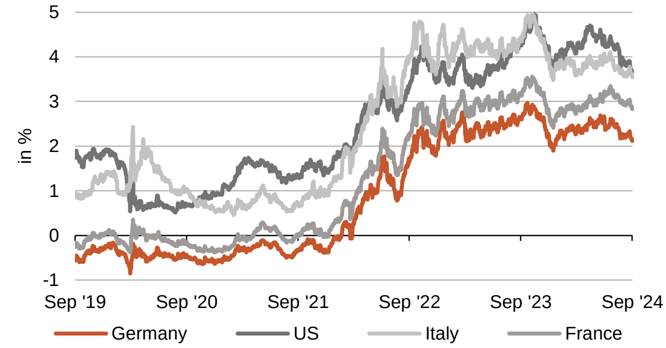
FIXED INCOME

Weakening US labor market gives Fed green light for first rate cut

While a rate cut by the Fed in September is almost certain, the size of the move remains unclear.
Increased interest rate volatility on both sides of the Atlantic argues for duration close to neutral.
IG and HY risk premiums recently widened slightly due to recession concerns. EM local currency bonds preferred.

- Weaker labor market data and concerns about a possible recession in the **US** led to turbulent developments on the markets in August. The expectation of early and rapid interest rate cuts by the Fed caused the yield on 10-year **US government bonds** to fall from 4.2% at the end of July to 3.7% recently. While the Fed's first rate cut in September is as good as certain, the amount of the cut and the further path and pace of interest rate cuts remain unclear. The yield curve has recently turned positive, particularly at the short end. Despite slowing momentum, inflation in both the US and Europe remains a risk factor for the path of interest rate cuts, particularly in view of Donald Trump's possible return to the White House. In anticipation of further interest rate cuts by the ECB, the yield on 10-year **German government bonds** recently fell to 2.1%.
- The narrowing of spreads in **corporate bonds** in recent months has recently come to a halt due to fears of recession. The IG segment continues to offer historically more attractive valuations on a spread basis compared to the HY segment. Both the high-yield and IG segments also continue to be supported by positive inflows of funds, while new issues are being well received by the market after the summer break. **In emerging markets**, high-yield hard currency bonds from commodity-exporting countries offer attractive carry thanks to solid trade balances.
- When it comes to safe bonds, we continue to prefer **covered bonds** to government bonds. In Europe, we are focusing on good qualities from the IG segment. **In EM**, we continue to prefer 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, 11/09/2019 - 11/09/2024.

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 11/09/2024	ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	226.79	+2.0%	+7.8%	-12.3%
Covered bonds (iBOXX Euro Germany Covered)	190.72	+2.5%	+6.5%	-7.2%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	150.92	+2.3%	+8.2%	-7.4%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	160.64	+3.8%	+8.6%	-0.5%
Emerging market bonds (J.P. Morgan EMBI Global Diversified unhedged Return EUR)	609.63	+7.5%	+12.0%	+2.4%
High-yield bonds (ICE BofA Global High Yield Index)	477.84	+6.9%	+13.8%	+3.2%

COMMODITIES

Cyclical commodities need to catch up

Gold benefits from interest rate cuts.
Negative outlook for oil already priced in.
Metals await rising industrial activity.

- In recent weeks, **gold** has seamlessly built on the performance of previous months and once again reached new all-time highs. Although the previously strong demand from central banks in the Far East has waned, Western investors have started to demand more gold again with a view to interest rate cuts in the near future. This change in drivers should continue to give the gold price a tailwind in the coming months.
- **Crude oil** (Brent) has recently fallen noticeably. However, there was some fundamentally positive news: The oil market is in deficit, Libya is recording high production shortfalls and OPEC+ is postponing its production increases until December. The market seems to be focusing on a weaker demand-supply structure in the future. However, this now seems to be priced in - there is potential to catch up.
- Although **industrial metals** have been surprisingly robust in the face of disappointing PMIs, more activity in the manufacturing sector is needed for prices to rise.

Price development

Source: Bloomberg, 11/09/2019 - 11/09/2024.

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

		Performance		
	As of 11/09/2024	ytd	1-year	3-year
Gold USD/ounce	2,512	+21.8%	+30.7%	+40.5%
Silver USD/ounce	28.7	+20.5%	+24.3%	+20.8%
Copper USD/pound	408.3	+4.9%	+8.3%	-8.2%
Brent USD/bbl	70.61	-8.3%	-22.1%	-3.2%

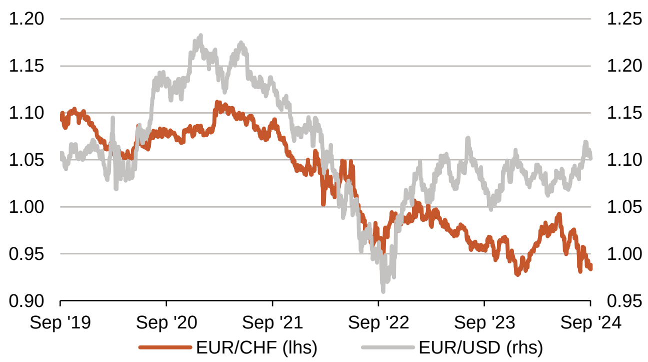
CURRENCIES

Central banks move exchange rates

The Fed's turnaround in rates, which is likely to be somewhat more aggressive than that of the ECB, should result in the US dollar coming under pressure to depreciate.

- **Euro with potential:** Although the US Federal Reserve will initiate the interest rate turnaround somewhat later than the ECB, it is likely to cut its key interest rate faster than the eurozone. For the US dollar, this means continued pressure to depreciate. In addition, the US economy is likely to cool down further in the coming months, while the still hesitant upturn in the eurozone could gain some momentum in the coming year. We therefore expect the euro to appreciate slightly against the greenback in 2025.
- **SNB and ECB in lockstep:** Like the ECB, the Swiss National Bank is also likely to cut interest rates again in September. The interest rate differential will therefore hardly change. A further escalation of the Middle East conflict and the US elections could cause short-term movement in the exchange rate. Overall, however, we expect the euro-franc exchange rate to move sideways until the end of the year.

Exchange rates



Source: Bloomberg, 11/09/2019 - 11/09/2024.

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	→	→

		Performance		
	As of 11/09/2024	ytd	1-year	3-year
EUR/USD	1.10	-0.2%	+2.4%	-6.8%
EUR/CHF	0.94	+1.0%	-2.0%	-13.4%
EUR/GBP	0.84	-2.6%	-1.8%	-1.1%
EUR/JPY	156.78	+0.7%	-0.5%	+20.7%

IMPORTANT NOTES

Members of the Investment Committee

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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
Daniel Sutter | Equities
Maria Ziolkowski | Fixed Income
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