INVESTMENT COMMITTEE MINUTES

08 July 2021

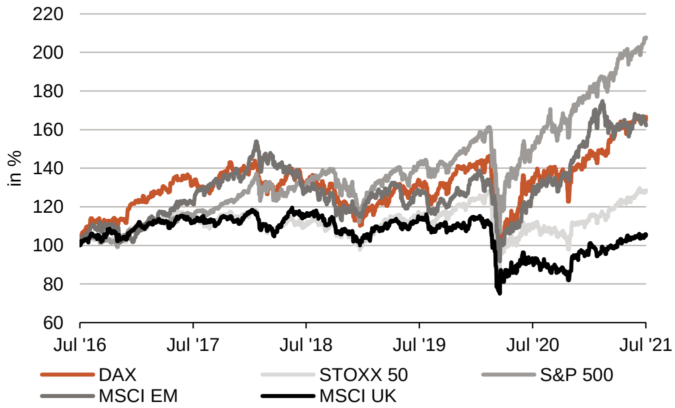
Managers of the Committee

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, 07/07/2016 - 07/07/2021.

Most important assessments at a glance

Economics	• The global recovery is underway. The Delta variant has become the test case, but risks to the economy are manageable. • After the easing of the lockdowns, consumers have pent-up demand, companies want to invest and politicians support. • Inflation returns somewhat more dynamically with the recovery – central banks will only tighten policy gradually.
Equities	• The overall market is experiencing a slight uptrend, with low volatility. US equities again ahead of European counterparts. • Growth stocks have benefitted from declining reflation dynamics. Value hardly appears to react to positive earnings revisions. • We think that there is limited upside potential and have taken a balanced position, with only a slight overweight in equities.
Bonds	• Bond yields recently failed to find their way up, despite good fundamentals and increased inflation. • Hardly any falling risk premiums for corporate bonds. EUR high-yield bonds are attractive against historical comparisons. • We underweight bonds and focus on credit risk and off-benchmark themes. Duration: short.
Commodities	• Rising real interest rates limit the potential for gold. Jewellery and central bank demand continue to provide tailwinds. • The supply situation for oil is tight. The market is likely to remain in deficit and the oil price, therefore, is well supported. • Industrial metals consolidate due to profit-taking. The long-term investment case remains intact.
Currencies	• EUR/USD: the US Federal Reserve (Fed) is strengthening the dollar, but our euro outlook is positive in the medium term. • GBP is in sideways mode after a very strong Q1 – at current levels, EUR/GBP appears to be fairly valued. • CHF is hardly making any headway and no major movements are expected for the time being.

Current market commentary

Equity markets continue to rise – slowly but surely. Both realised and implied volatility are at their lowest levels since the outbreak of the COVID-19 pandemic. This, coupled with positive price momentum, is driving systematic investors – especially valuation-insensitive ones – successively into equities. At the same time, it appears that other investor groups are looking to increasingly hedge their equity exposure and sell upside potential in return. In the absence of material news, the positive trend is likely to continue in the short term, with subdued volatility at the index level. Under the surface, however, the back and forth of different investment styles persists. Recently, growth companies – in particular – have been ahead thanks to falling bond yields, whereas value stocks have been weighed down by COVID-19 fears in regards to the Delta variant. Therefore, on a regional level, the US was recently ahead of Europe again. Style volatility is likely to continue for a while, supported by mixed economic and inflation figures. As the equity markets have already priced in a lot of positive expectations, we think that there will only be limited upside potential until the end of the year. Consequently, we are only slightly overweight equities and have a balanced position within the asset class.

Yields on safe government bonds are falling, despite the Fed's more hawkish tone at the Federal Open Market Committee (FOMC) meeting in mid-June. In view of the high inflation rates (even if only temporary in some cases) and the positive economic environment, this movement is difficult to understand. We expect yields to rise again by the end of the year. Although risk premiums for corporate bonds offer only limited room for manoeuvre, they should continue to fall in light of positive corporate reports – whereby lower credit ratings should be favoured.

Gold fell significantly in the wake of the Fed meeting. However, it was the strengthening dollar – not interest rates – that put precious metal under pressure. Meanwhile, the oil market remains undersupplied, with or without a deal within OPEC+. As a result, the oil price remains well supported, in our view.

ECONOMICS

The economic traffic lights are green; the Delta variant appears to be a manageable economic risk

The recovery of the global economy is gaining momentum. The US is ahead, but Europe is catching up.
Catch-up economy fuelled by pent-up demand from consumers and businesses. Supportive monetary and fiscal policy.
Inflation has returned with the recovery – but central banks will only slowly tighten their policies from 2022.

- **Strong recovery:** Life is gradually returning to normal in the US. Supported by an expansive fiscal policy, the recovery is gaining more and more momentum. An extraordinarily expansive monetary policy is contributing to this. At the same time, however, inflation is rising. At around 5 %, the inflation rate in May was more than twice as high as in the eurozone and the UK.
- **Eurozone catching up:** From the end of March to the end of June, COVID-19 case numbers in the eurozone also decreased significantly. After a faltering start, the vaccination campaign has also gained momentum in the EU. The vaccination successes limit the risk that the new increase in case numbers – due to the Delta variant – will lead to new hard lockdowns. Our economic outlook, therefore, remains positive. The economic indicators are almost all pointing upwards and signal a strong recovery.
- **The UK test:** The number of new infections has been rising in the UK since 23 May, despite rapid progress in vaccination. The complete removal of restrictions was postponed by four weeks to 19 July. Indeed, it is mainly people who have not yet been vaccinated who are infected; but, since many of them are young people at relatively low risk and the severe cases remain at a low level, we do not currently expect the medical system to be overloaded. Nevertheless, we are keeping an eye on the risk.
- **After the pandemic, full speed ahead:** Consumers have built up additional savings during the lockdowns, allowing for a strong catch-up economy, while monetary and fiscal policies are supporting demand in the developed world more than ever before. After the first wave of the pandemic, the eurozone had recovered almost all of its Q2 2020 losses in Q3 2020. This would indicate the likelihood of a quick recovery this summer as well.
- **China** remains robust for the time being thanks to its credit stimulus, despite significant long-term risks. Strong growth in key consumer countries is supporting many emerging markets. However, some countries – such as India, Brazil and Turkey – have damaged themselves by mishandling the pandemic.
- **Do not worry about a little more inflation:** one-off effects – such as the return to a normal oil price and higher transport costs – contribute to rising inflation rates. However, as these more uncommon factors fade out, the price climate will calm down again in 2022 – with inflation of around 1.5% in Germany and the EUR area. For the US, however, we also expect stronger price buoyancy in the medium term.

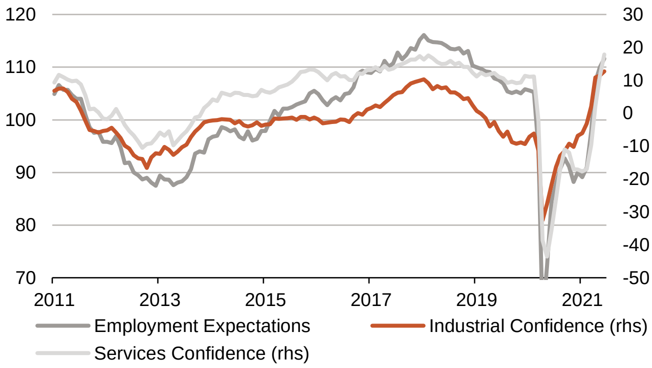
Central banks are slowly moving forward: For the time being, the central banks do not see any acute need for action because the current increase in inflation rates is largely driven by one-off effects. Overall, however, they will come under greater pressure to act if the upward trend in prices solidifies. The Fed and the Bank of England (BoE) are, therefore, proceeding very cautiously in order to test the reaction of the markets. The ECB will follow.

GDP and inflation forecasts (%)

		GDP growth			Inflation		
	%	2020	2021	2022	2020	2021	2022
World	100.0	-3.2	5.2	3.8			
US	24.5	-3.5	7.1	4.6	1.2	3.7	3.3
China	16.4	2.0	8.9	5.3	2.5	1.4	2.2
Japan	5.8	-4.7	3.3	2.2	0.0	0.0	0.6
India	3.3	-7.3	10.0	6.5			
Latin America	5.9	-7.0	4.4	3.3			
Europe	24.4	-6.2	4.8	4.6			
Eurozone	15.3	-6.7	4.7	4.9	0.3	1.9	1.4
Germany	4.4	-5.1	3.9	4.8	0.4	2.7	1.6
France	3.1	-8.0	5.9	4.7	0.5	1.6	1.5
Italy	2.3	-8.9	5.3	4.7	-0.1	1.0	1.2
Spain	1.6	-10.8	5.7	6.9	-0.3	1.9	1.8
Rest of western Europe							
UK	3.2	-9.8	7.0	5.4	0.9	2.0	2.4
Switzerland	0.8	-2.7	3.5	2.8	-0.7	0.4	0.5
Sweden	0.6	-2.9	3.6	3.4	0.5	1.7	1.3
Eastern Europe							
Russia	1.9	-3.0	3.0	2.5	3.3	5.2	4.0
Turkey	0.9	1.6	4.5	3.5	12.3	15.0	12.0

Source: Berenberg

Eurozone business climate



Source: European Commission, 01/01/2011 - 30/06/2021.

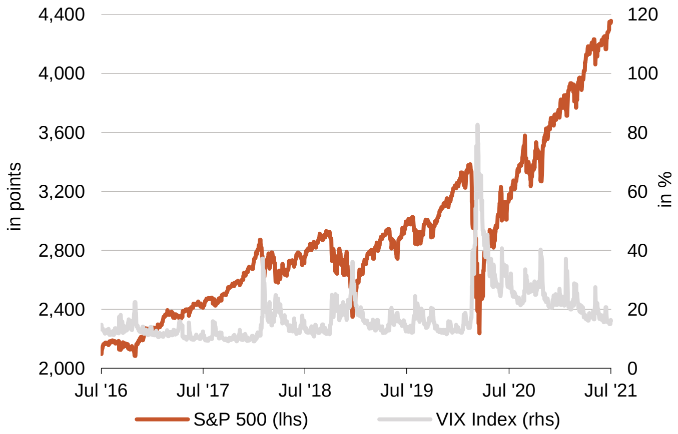
EQUITIES

Under the surface, the back and forth continues

Overall market in slight uptrend, with low volatility. US equities are again ahead of European counterparts. Growth stocks have benefitted from declining reflation dynamics. Value has hardly reacted to positive earnings revisions. We think that there is limited upside potential; we have taken a balanced position, with a slight overweight in equities.

- **The stock markets were able to make broad gains over the last month**. However, there was a change in the regional favourite. While the **eurozone** was still highly favoured by investors in May, **the US** was flavour of the month for June. Despite a slowdown in positive economic surprises, the S&P 500 and the Nasdaq 100 marked new all-time highs every week. With investors holding high levels of liquidity and inflation rising, investment pressure remains high despite expensive valuations. In addition, more and more systematic investment strategies are now increasing their equity allocations, with falling realised – as well as implied – volatility. In the short term, equity markets remain well supported at the index level.
- Under the surface, however, the back and forth of investment styles continues. The FOMC meeting in mid-June ushered in another change of favourite. Curiously, as bond yields fell, **growth stocks** were again in demand globally (+5.0%). On the other hand, **value stocks** declined slightly (-0.3%), although value-heavy sectors – such as energy and basic materials – continue to show the strongest earnings revisions. Positive fundamental news is currently not being rewarded with price gains, which could indicate saturation tendencies. The recently started reporting season should provide insight into whether companies can meet the high expectations of investors.
- The extent of earnings growth for the year as a whole, on the other hand, is still subject to great uncertainty. The further inflation and – subsequent – interest rate path, the severity and extent of COVID-19 infections, as well as potential fiscal programmes and tax increases, are likely to have different affects on the regions and sectors.
- We have a **slight overweight in equities** and **remain balanced.** The regional focus is currently on Europe and the emerging markets.

Performance and volatility of the S&P 500 Index



Source: Bloomberg, 07/07/2016 - 07/07/2021.

Overview of equity markets (short/medium term)

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

		Performance in local currency				
	As of 07/07/2021	ytd	1-year	3-year	P/E	Dividend yield
DAX	15,693	+14.4%	+24.4%	+25.6%	15.0	2.8%
SMI	12,086	+16.0%	+21.9%	+52.8%	18.9	2.8%
MSCI UK	2,010	+13.2%	+19.0%	+3.1%	12.9	4.1%
EURO STOXX 50	4,079	+17.0%	+25.9%	+29.2%	17.8	2.8%
STOXX EUROPE 50	8,548	+16.2%	+19.3%	+25.8%	16.5	3.2%
S&P 500	4,358	+16.9%	+40.7%	+66.9%	22.8	1.4%
MSCI Em. Markets	1,341	+4.9%	+30.1%	+36.8%	14.2	2.5%

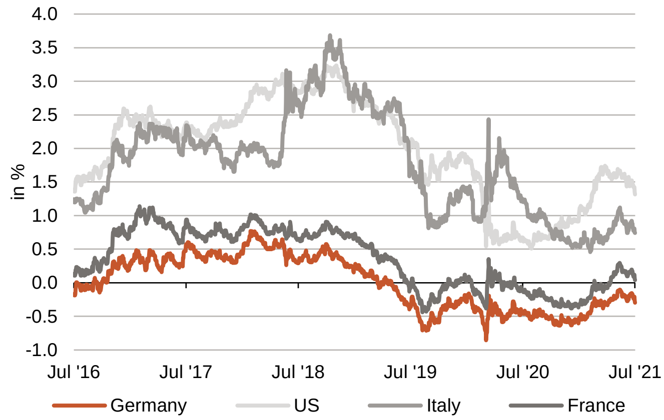
BONDS

Yield rises remain uninspiring

There has been a pause in the rise in yields. Looking ahead, however, yields are likely to rise again. Corporate bonds remain in demand due to positive economic development and thanks to a comparatively shorter duration. We are underweight in bonds and focus on credit risk and off-benchmark themes. Duration: short.

- Yields on **European government bonds** have recently failed to find their way upwards and have been unsettled – despite positive economic fundamentals and increased inflation. For example, **10-year German, French, Italian** and **UK government bond** yields have fallen between 1bp-11bp over the past four weeks. However, we believe that at least another moderate rise in interest rates is likely to come in the medium term.
- **US government bonds** also saw falling yields. The rhetoric of the US central bank seems to be working. Some market participants no longer consider the risk of rising inflation to be acute, as evidenced by falling inflation expectations. In addition, recent rather mixed US labour market data and fears over the COVID-19 Delta variant support the current still expansionary Fed policy. However, if inflation remains high – or even rises – the market could be caught on the wrong foot and interest rates could very well unexpectedly rise quickly.
- The risk premiums for corporate bonds have only fallen significantly for USD high-yield bonds in recent weeks. In contrast, the risk premiums for **EUR high-yield bonds**, **EUR-IG** and **USD-IG corporate bonds have** hardly moved, which makes EUR high-yield bonds – in particular – appear attractive. Especially because they still offer significantly more attractive risk premiums compared to their US counterparts in historical comparison. In **emerging market bonds,** we continue to like local currency bonds from a cyclical perspective and high-yield hard currency bonds due to attractive yields.
- **We are underweight bonds.** We keep our focus on corporate and emerging market bonds and keep the duration comparatively short.

Yields on 10-year government bonds



Source: Bloomberg, 07/07/2016 - 07/07/2021.

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	↗	↗

	As of 07/07/2021	Performance in index currency ytd	1-year	3-year
Government bonds (iBOXX Europe Sovereigns Eurozone)	257.69	-2.2%	+0.6%	+10.0%
Covered bonds (iBOXX Euro Germany Covered)	205.60	-0.9%	-0.2%	+3.4%
Corporate bonds (iBOXX Euro Liquid Corporates 100 Non-Financials)	162.93	-0.1%	+3.2%	+7.9%
Financial bonds (iBOXX Euro Liquid Corporates 100 Financials)	161.37	-0.0%	+2.4%	+6.6%
Emerging market bonds (Bloomberg Barclays EM USD Aggregate TR Index Unhedged)	1,283.58	-0.4%	+5.6%	+20.9%
High-yield bonds (Bloomberg Barclays Global High Yield Total Return Index, USD)	1,547.40	+2.2%	+13.2%	+20.6%

COMMODITIES

Oil remains scarce, the price supported

Real interest rates limit upside potential of gold.
Supply situation on the oil market remains tense.
Industrial metals are taking a temporary breather.

- The **gold price** fell significantly as a result of the FOMC meeting and a subsequently stronger US dollar. In the coming months, (rising) real interest rates – in particular – are likely to limit gold's upside potential, even if rising jewellery and central bank demand should continue to act as tailwinds. At the same time, the much cleaner positioning of investors makes stronger price losses (as happened in Q1) unlikely.
- The **crude oil price** continued its rally at an unabated pace last month. WTI even briefly reached its highest level since 2014. There was recently a conflict within OPEC+, so the urgently needed production increases are still a long time coming. Nevertheless, with or without an agreement between the member countries, the oil market should remain in deficit and the price should be well supported by low inventories.
- **Copper** consolidated recently after hedge funds almost completely liquidated their net long positions.

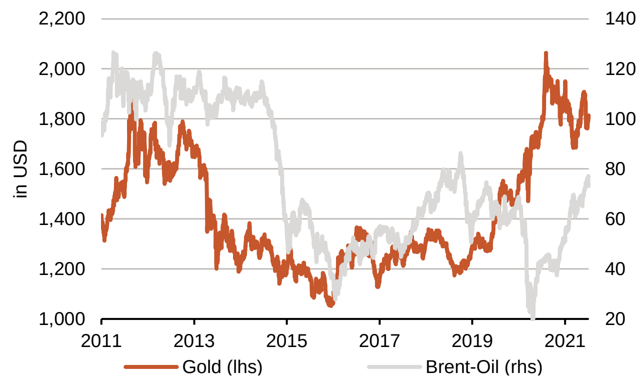
CURRENCIES

EUR/USD dollar rate falls below 1.20 again

EUR/USD: The EUR has further upside potential.
The GBP is fluctuating sideways at a very solid level.
CHF currency gains are again taking place in small steps.

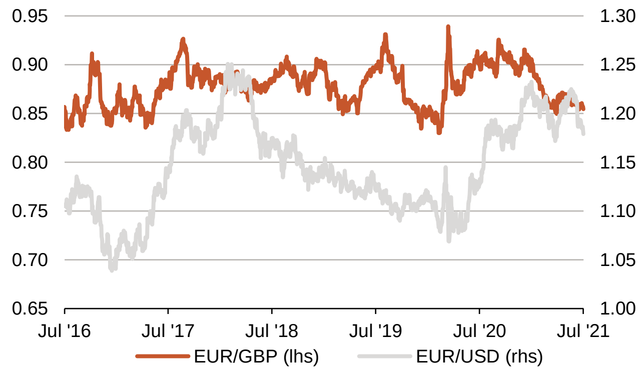
- **EUR/USD:** In mid-June, the Fed ended the rise in the euro exchange rate by signalling an earlier tightening of its monetary policy. The US dollar benefitted, and the EUR fell back again; the exchange rate fell from above 1.22 to below 1.19 US dollars per EUR. We remain optimistic that, for the rest of the year, the EUR will return to the level at 1.22 – or even slightly above. The recovery in Europe appears more sustainable because it is less driven by government spending programmes; as a result, overheating is less likely. It remains to be seen what will emerge from the ECB's strategy review: could there be any surprise impulses for the euro exchange rate from this side?
- **EUR/GBP:** The GBP has continued to settle in the range of 0.86 pounds per EUR – maintaining its considerable gains from Q1. For the time being, we do not recognise any strong trends to support further gains for it; however, positive impulses could come from the BoE.

Price development



Source: Bloomberg, 01/01/2011 - 07/07/2021.

Exchange rates



Source: Bloomberg, 07/07/2016 - 07/07/2021.

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

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 07/07/2021	ytd	1-year	3-year
Gold USD/ounce	1,804	-5.0%	+0.5%	+43.7%
Silver USD/ounce	26.1	-1.0%	+43.1%	+62.9%
Copper USD/pound	432.9	+23.0%	+55.3%	+53.9%
Brent USD/bbl	73.43	+41.8%	+70.5%	-4.8%

		Performance		
	As of 07/07/2021	ytd	1-year	3-year
EUR/USD	1.18	-3.5%	+4.6%	+0.4%
EUR/CHF	1.09	+0.9%	+2.7%	-6.1%
EUR/GBP	0.85	-4.4%	-5.0%	-3.4%
EUR/JPY	130.50	+3.4%	+7.7%	+0.6%

IMPORTANT NOTES

Members of the Investment Committee

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Dr Holger Schmieding | Chief Economist, Vice-Chairman
Matthias Born | Head Portfolio Management Equities, European Equities
Ulrich Urbahn | Head Multi Asset Strategy & Research
Oliver Brunner | Co-Head Portfolio Management Multi Asset
Ansgar Nolte | Co-Head Portfolio Management Multi Asset
Till Budelmann | US Equities
Marco Höchst | Equities
Robert Reichle | Bonds
Ludwig Kemper | Commodities, Minutes

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