

Q3 2019



GENERALI
INVESTMENTS

Investment View

The law of diminishing returns



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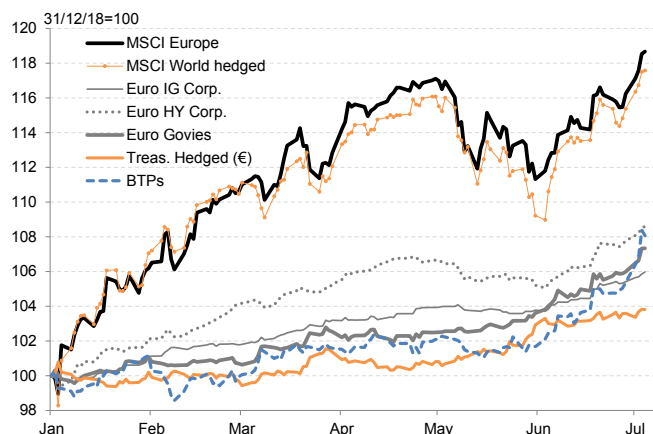
Global View – The law of diminishing returns

- Central banks are about to press the ‘easing’ button again. But the likes of the ECB and BoJ are facing the law of diminishing return, i.e. it is not clear that their actions will effectively re-anchor inflation expectations at higher levels. If, by cutting rates to negative and buying loads of assets they have not succeeded, why would they now?
- With bond yields going lower for longer, investors too face the tough reality of diminishing returns. A record amount of bonds trade below zero (YTM), and the hunt for yield is raging. Except for those predicting a global downturn – we don’t – the investment choices are clear: equities and credit remain preferred habitat.
- Most importantly the US economy is starting to wobble. This is both a concern and a blessing. As President Trump realises that tariffs are causing self-inflicted pain, he is likely to turn less aggressive as he prepares for the US presidential election, in just a bit more than one year. This, and reflation policies, should keep the global economy afloat.
- If tariffs don’t work, why not trying a currency war? We are bearish the USD, and that should be good news to EM markets.

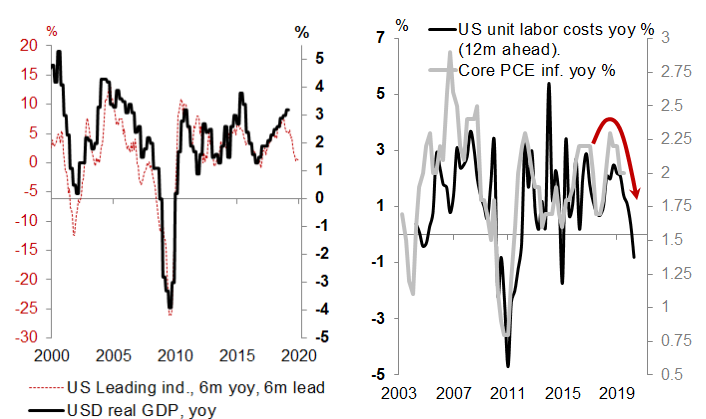
Monetary easing now a near-certainty this summer. The question, especially for the ECB, is how much.

Central banks to the rescue. We warned three months about a [flock of doves](#) returning to the markets. Their return has proved bullish for corporate bonds and equities, as we expected, and vindicated our recommendation to cut exposure to cash. But it also proved more bullish for government bonds than we expected. Indeed disappointing growth and inflation news have put central banks on alert, with renewed trade tensions in May only aggravating their concerns. So easing this summer is now a near certainty. We expect at least two Fed cuts in H2, while the ECB should deliver aggressive forward guidance, a rate cut, deposit tiering and private asset QE (and possibly PSPP2; i.e. including Govies in the pack).

Graph 1: YEAR-TO-DATE TOTAL RETURNS



Graph 2: US GROWTH AND INFLATION ARE SURE TO SLOW OVER COMING MONTHS AND QUARTERS



Fighting heavy headwinds. The global slowdown has become more obvious, after temporary factors distorted Q1 growth to the upside on both sides of the Atlantic. Various uncertainties are taming the ‘animal spirits’, such as hard Brexit fears and Italian fiscal largesse. But the largest drag on growth by far has come from trade tensions, as the US/China war was revived in May (followed by a truce in late June). This has hurt business confidence and capex, particularly in open economies such as Europe and China. As we enter summer, the US economy – a relatively close economy – is also starting to get infected (Graph 2a).

That is both a concern and a blessing in disguise. Of course the more the economic slowdown propagates, the more likely it will morph into a downturn. However in this case that propagation should be a warning bell for president Trump, a sign that his aggressive trade stance is proving self-defeating into the November 2020 US presidential election. With central banks about to press the ‘easing’ button, China’s stimulus starting to play out, Germany likely to consider some form of fiscal support and Trump expected to durably pause the trade war, we expect the global economy to stay on its feet. Let us be clear: this will not be enough to stop central banks from easing. Inflation is too low, and the de-anchoring of market expectations unacceptable. For that matter US inflation is skewed to the downside (Chart 2b), making sure that the risk leans towards more Fed cuts, not less.

The death of beta

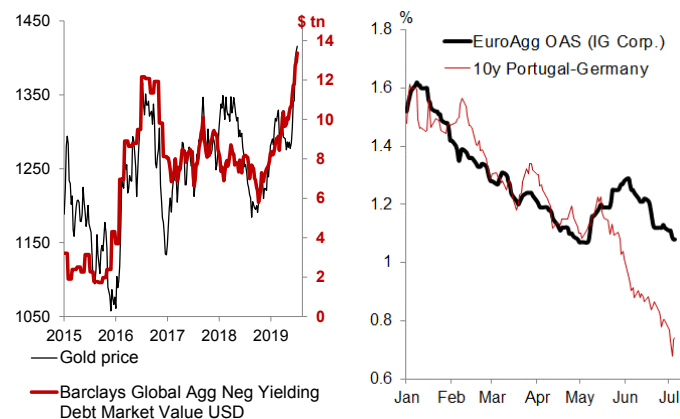
The law of diminishing returns. Central banks – not least the ECB – face a stiff challenge in convincing investors that they can prop up inflation. If cutting rates to -40bp and buying more than €2.5tn of assets failed to bring inflation closer to 2%, even after a strong cyclical upturn in 2017-18, why would the ECB succeed now? Investors have already concluded that the law of diminishing returns has made the likes of the BoJ and ECB impotent: more easing will hardly bring inflation at the desired level. Bond yields will thus be lower for longer; if anything they remain skewed to the downside as central banks duly deliver this summer.

Investors too face diminishing return. Graph 3a shows that nearly \$14trln of bonds now trade with a negative yield to maturity – a new record. There is a limit to how low yields can go, especially at the front end (reversal policy rate, or level at which policy becomes counterproductive), so total return in Fixed Income hardly looks exciting. That said, Credit still offers residual potential for spread compression – as the latter has lagged relative to the sharp narrowing observed in the sovereign space (3b). The near-term potential for equities is limited by the soft economic growth, and the likely downgrade of 2020 profit consensus forecasts. Still, the dividend yield in EUR equities has reached a new high relative to sovereign and corporate bond yields, making the asset class hard to resist. Equities too face a diminished return outlook in the medium term, but even something like 5% looks attractive relative to what fixed income products will deliver.

Central banks will have a hard time convincing anyone that they can prop up inflation

Investors face the certainty of much lower financial returns in the future

Graph 3: NEARLY \$14TN OF NEGATIVE YIELDING BONDS; CREDIT SPREADS HAVE LAGGED NON-CORE SOVEREIGN SPREADS



Graph 4: EQUITIES OFFER BETTER RETURN OUTLOOK THAN BONDS IN THE MEDIUM TERM; USD LOOKS TOPPISH, AND EMFX CHEAP



If tariffs are causing self-inflicted pain, maybe a currency war will work better?

From trade war to currency war? President Trump always likes a good fight. As it appears that tariffs are causing self-inflicted pain, he may be looking for another route. The FX market could be one. As Fed cuts create a positive environment for

USD depreciation, expect Trump to jawbone, or even to order intervention in the FX markets to amplify the move. Recent attacks vs both China and Europe signal increased focus on FX policy. The USD has started to ease off but remains sky high (4b). Further dollar depreciation would be a boon for EM markets, usually very sensitive to the USD stance. The EMBI spread remains large vs HY, even after the recent rally. EM equities are also near lows vs developed markets.

Wild cards. We are not going to lose too much sleep on Italian fiscal woes in the near term, now that the Excessive Deficit Procedure has been avoided and that the ECB is about to throw another life vest. As ever, the main risk lies on the side of the trade war; not only it has also become a tech war (Huawei) but Trump could also attack Europe and auto exports – not our central scenario but something to watch closely. Finally Brexit will be a major focus again in 2H19. Risk of a Hard Brexit will be thicker than in spring, though we still deem a deal or another extension (for elections and/or referendum) more likely than a crash.

Table 1: MACRO FORECASTS (annual changes, in %)

	Growth			Inflation		
	2019f	2020f	2021f	2019f	2020f	2021f
US	2.4	1.7	1.8	1.9	2.0	2.1
Euro area	1.1	1.3	1.3	1.3	1.3	1.4
Germany	0.8	1.3	1.3	1.5	1.4	1.5
France	1.2	1.2	1.8	1.2	1.4	1.6
Italy	0.0	0.6	0.8	0.8	1.1	1.1
Non-EMU	1.3	1.4	1.6	1.9	1.9	1.8
UK	1.3	1.4	1.6	2.0	2.0	1.8
Japan	0.6	0.3	0.8	0.6	0.9	0.8
Asia ex Japan	5.8	5.8	5.8	2.8	2.8	2.7
China	6.2	6.1	5.8	2.6	2.4	2.2
CEE	1.7	2.7	2.8	7.4	5.8	4.8
Latin America	0.3	2.1	2.0	4.0	3.7	3.6
World	3.1	3.2	3.3	2.7	2.6	2.5

Table 2: FINANCIAL FORECASTS (current as of 28 Jun, 3-day average)

10-Year Bond Yields	Current*	3M	6M	12M
US	2.02	2.00	2.05	2.10
Germany	-0.32	-0.35	-0.30	-0.25
Italy	2.12	2.00	2.00	2.00
Japan	-0.15	-0.15	-0.10	-0.05
Forex	Current*	3M	6M	12M
EUR/USD	1.14	1.13	1.16	1.18
USD/JPY	108	107	106	105
EUR/GBP	0.90	0.91	0.85	0.86
Equities	Current*	3M	6M	12M
S&P500	2927	2996	3005	3027
MSCI EMU	122.1	124.8	124.0	123.2

Allocation recommendations

Mixed bag. Our tactical asset allocation decisions have produced slightly positive small excess return so far this year (vs benchmark Strategic Asset Allocation), in a context of very strong asset price performance (Graph 1). Our overweights (OW) in Equities and Credit have been rewarded, though that has been greatly offset by the underweight (UW) in Government bonds, where the relatively long duration of the index has helped produce high returns relative to cash. Thankfully we had totally erased our Cash OW three months ago.

Underweight Govies, with an aggressive curve allocation strategy. We stick to a small UW in Govies overall. This is achieved by strongly underweighting the front end of the EUR curve, where already more than 20bp of ECB cuts are priced in, as well as the “belly” of the curve, already very flat. Instead we overweight the long end of the curves, even at that low level of yields, especially in soft core markets where the 10-30y slope is now steep relative to 2-10y. We prefer non-core markets over soft core.

We continue to prefer Credit (OW) vs Govies, at equivalent duration. Credit spreads have lagged other sectors such as non-core sovereign or cross-asset volatility (which has pulled back aggressively after a short-lived outburst in May). To a large extent credit spreads have tracked, with a small lag, real yields. This is because yield deprivation is making the asset class irresistible, but also because low yields keep financing costs low, helping default rates stay dormant. Expect CSPP2 to offer further support to the asset class. Of course the outlook will change dramatically if and when the global economy eventually falls into recession. Defaults would rise and liquidity in the asset class would quickly vanish. Recent asset management

UW Govies, but OW in the long end (30-year). Prefer non-core over core.

Keep OW in Credit, especially in IG and long dated sectors

Small OW in equities, geographically diversified

crises – e.g. Woodford – show that the rush toward real assets, including private credit, has caused a severe liquidity mismatch, now a great matter of concerns for financial stability. Eventually liquidity in ‘liquid’ credit will also quickly vanish when the global economy bites the dust. But this is not in our books for the foreseeable future. Still, we generally prefer safer credits (IG over HY). In the IG sector we like the long-dated sector, given that the credit spread curve appears irresistibly steep relative to the rates curve (more value in Credit duration).

We raise our so far moderate OW in equity further. Valuation is no longer cheap on an outright basis, but it is very cheap relative to Fixed Income. If the global economy shows signs of stabilisation, as we expect, then returns will stay positive into yearend as there is room for further extension of multiples in a yield-deprived world. Geographical diversification is in the order, given the tariffs threat hanging over the EU. The Swiss, UK and EM markets offer value. We offer more granularity on sectors, styles and geographical allocation in our dedicated section.

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Macroeconomic Outlook

- The global economy is walking a tightrope, with a mature global cycle increasingly exposed to business uncertainties from trade risk. While domestic demand in the advanced economies remains overall solid, striking cracks have appeared. Price pressures are unlikely to pick up materially any time soon.
- Central banks have taken note and sharply reversed course. Rate cuts both for the US and the euro area and even a resumption of the ECB's QE are in the offing.
- The sharp decline in yields and the global compression in risk premia have already helped to ease financial conditions. Together with a slightly favorable outlook for EMs and still robust consumption, we expect the global economy to master the headwinds. But the downside risks from persistent political uncertainties have risen.

Persistent trade uncertainties are increasingly taking their toll on global growth

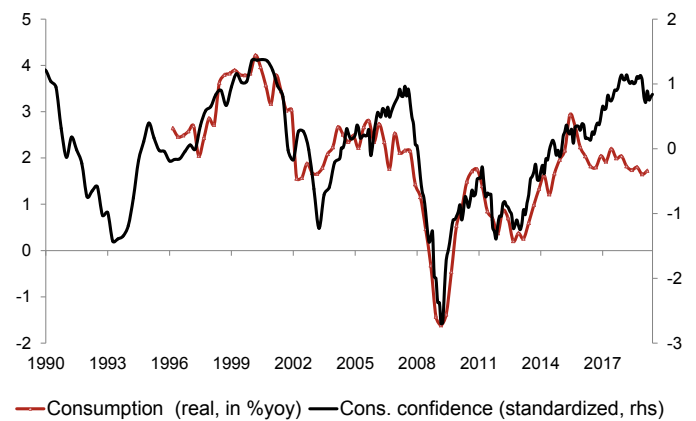
Policy uncertainties are keeping their tight grip on the global economy. The threat of a disorderly Brexit keeps lingering also after the deadline postponement to October 31. The fiscal spat between Italy and the EU Commission has only been deferred to the 2020 budget in autumn. And most prominently, the world is witnessing a roller-coaster ride in trade uncertainties. US President Trump raised existing tariffs on US\$ 200 bn of Chinese imports from 10% to 25% in early May, restricted trade with Chinese Huawei and threatened to also subject the remaining US\$ 300 bn of Chinese shipments to the US with a 25% levy, raising trade war tensions sharply (Graph 1) This latter threat was averted only last minute after Trump and Xi consultations at the G-20 summit, while Trump also softened slightly his stance on Huawei.

Graph 1: TRADE WAR FEAR INDICATOR



equally weighted Stoxx600 vs auto sector, Fathom US China Exposure Index (inv.), JPY/KRW and USD/AUD, end 2017 = 100

Graph 2: CONSUMPTION AND CONSUMER CONFIDENCE



weighted avg. for US, euro area and Japan

While this truce is welcome news for the global economy, the damage from persistent threats and new tariffs are increasingly taking their toll from global growth. Companies, unsure about future export prospects and the stability of international value chains are deferring or canceling investment projects while business sentiment is suffering.

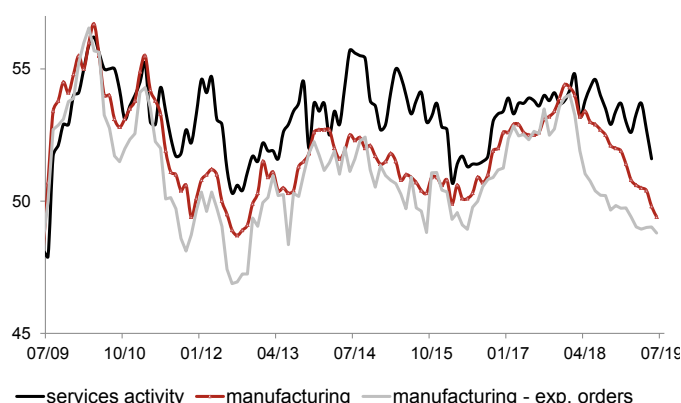
Measures of domestic demand have defied the global industrial downturn for longer, but are now showing increasing cracks

Cracks in the resilience of domestic demand

Domestic demand in the advanced economies has been holding up remarkably well so far, underpinned by strong consumption on solid employment and wage gains (Graph 2). But there are increasingly cracks appearing amid the sharp downturn in trade and industrial production. Services PMIs, for example, are a timely measure of the broadest sector of advanced economies and largely reflect domestic demand. After defying the manufacturing slowdown in 2018 and early this year, more recent readings are showing a disconcerting deterioration (Graph 3). Similarly, leading indicators are pointing to a slowdown, too (Graph 4). In the US, the drag from the fading fiscal stimulus is exacerbated by slowing investment.

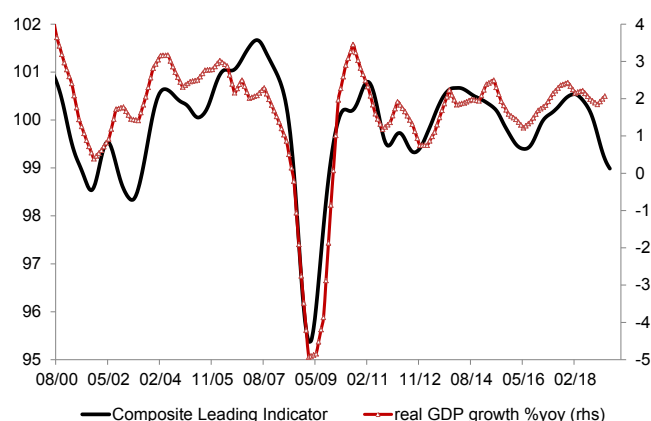
But consumer spending – which accounts for more than two thirds of demand in the US – is likely to hold up well. Also in the euro area, where the headwinds from global trade has been strongly felt – notably in Germany and Italy – we anticipate growth to still hold up decently, even though slightly below potential. We have even slightly upgraded the 2019 growth estimates compared to March. But this is only due to surprisingly strong Q1 readings while the balance of risks to the base outlook has clearly shifted to the worse.

Graph 3: GLOBAL PURCHASING MANAGER INDICES



Values below/above 50 signal contraction/expansion

Graph 4: G7 LEADING INDICATOR AND GROWTH



composite leading indicator, amplitude adjusted

EMs are likely to benefit from a peaking USD and recoveries in crisis-hit economies...

...but these improvements will be partially offset by a slowing of Chinese growth

Emerging Markets only marginally brighten the global outlook

Emerging Markets (EMs) will only marginally brighten the global outlook. Crisis-hit Turkey and Argentina will find a bottom. Also, a gradual recovery of South Africa from its sharp Q1 contraction in (-3.2% qoq saar) will ease the drag on global growth. Growth in the resilient CEE region is set to hold up well on persistently strong domestic forces. We also anticipate the drag from the strong US dollar – which weighs on EM activity, see Chart 5 overleaf – to reverse gradually over the coming quarters.

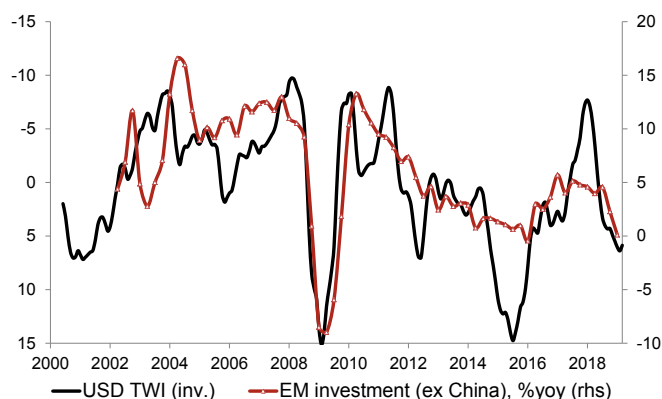
However, these improvements will be partially offset by a continued slowing of the Chinese economy. Monetary and fiscal accommodation notwithstanding, Chinese growth is set to slow down from the 6.4% readings in Q1 over the rest of the year. We anticipate further liquidity injections by the PBoC via reserve requirement cuts for banks, which will help to cushion the headwinds from external demand. But it would probably take a sharper slowdown, e.g. due to the escalation of the trade

Price pressures will remain subdued for longer

conflict with the US, for Chinese authorities to provide a big package of fiscal and monetary stimulus, including cuts in benchmark rates.

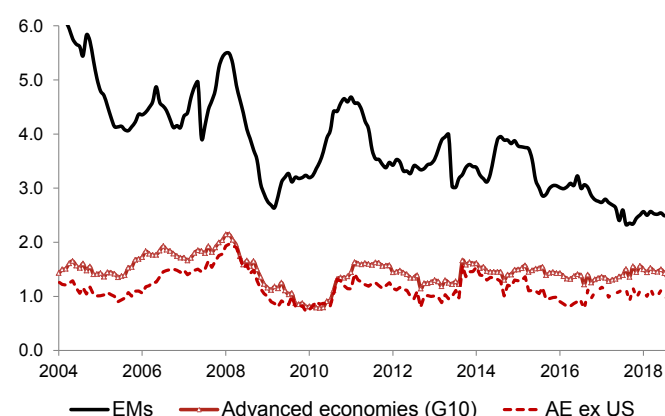
Amid this outlook of still decent, but increasingly challenged growth, price pressures are unlikely to pick up materially any time soon. Global rates of core inflation have been flattish over the past quarters (once we strip out crisis-prone EMs). Firms in advanced economies are increasingly wary of raising prices. This is true even in the US where decent productivity gains help firms to weather mildly rising employment costs. In the euro area, we anticipate core inflation to hover around the last two year's average of 1.2% yoy.

Graph 5: USD AND EM INVESTMENT GROWTH



in % yoy, 3mma, imports weighted by GDP (PPP)

Graph 6: GLOBAL CORE INFLATION



in % yoy, excl. energy and food; weighted by GDP (PPP); EMs ex Argentina, Turkey, Venezuela

The global economy is walking a tightrope, with central banks taking note

A tightrope act supported by increasingly dovish central banks

Overall, the global economy is walking a tightrope act, with a mature global cycle increasingly exposed to policy risks. Central banks have taken note and sharply reversed course. The Fed is now widely expected to cut rates as soon as at its next meeting at the end of July, with further moves to follow. As we lay out in the subsequent Chapter, we are looking for at least two US rate cuts by September. We also anticipate the ECB to cut the deposit rate deeper into negative territory and to re-open its asset purchase programme.

The sharp decline in yields and the global compression in risk premia resulting from the shift by major central banks have already helped to ease financial conditions. Together with a slightly favorable outlook for EMs and still overall solid consumption demand, we expect the global economy to hold up decently while allowing for more accommodative stances by central banks. This seems like a moderate goldilocks scenario, however, with an increasing amount of downside risks attached.

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Central Banks Reversing Course

- In the presence of easing activity, stubbornly low inflation and persistent downside risks, key central banks gave up their intentions to withdraw support and turned into easing mode again.
- In the US, the Fed is increasingly concerned by risks to growth. We expect a 50 bps cut in the fed funds rate by the end of the year, with a first move already at the July meeting. Going forward, the Fed will be more concerned about prolonged misalignment of inflation from its target.
- Following President Draghi's seminal Sintra speech we expect the ECB to announce a broad-based easing package in September, including the purchase of corporate bonds, and to signal its readiness to do even more, if needed.
- The BoJ's decision will be very path dependent, but we see it is now slightly more likely than not that Japan's central bank will also ease policy towards the end of the year.

Over the last quarter, the evolution of the macro data and the tilting of the balance of risks towards less favorable outcomes led to a big shift in the Fed and the ECB stance. The Fed accelerated its dovish pivot, talking explicitly about rate cuts already this year, while the ECB declared its readiness to support the economy should inflation remain below target. The BoJ has made no specific statement yet, but the macroeconomic outlook is consistent with an easying.

Fed ready for "insurance" cuts

Fed to cut rates to minimize the risk of a recession

As the US economy slows down, the risk of a recession increases; this has become the main concern for the Fed. The June meeting witnessed a large shift towards monetary easing, with almost half of the FOMC members in favor of rate cuts this year, as a form of "insurance" against tail risks to growth. We expect the central Bank to deliver a 50 bps reduction by the end of the year. An additional 25 bps cut will be needed in Q1 2020 to cushion the effect of the end of the fiscal stimulus on domestic demand. The softening in the policy stance is also motivated by low inflation, with the core PCE rate stuck below 2% at least until the end of the year and inflation expectations remaining at historical lows.

The economic projections presented in June showed also a substantial downward revision of the long-term level of the fed funds rate, from 2.8% to 2.5%. This will have implications for monetary policy going forward, as it will implicitly reduce the maximum level the policy rate can reach in an upswing. Therefore the size of the cut the Fed would be able to enact to fight a downturn will be more limited. The smaller room for interest rate movements will leave more scope for the use of other tools, first and foremost the size of the balance sheet.

New policy framework likely tilted to a more dovish stance

Moreover, making sure that inflation expectations remain anchored at 2% will require changes to the policy framework. One of the proposals which is getting more traction is that the Fed should target the average inflation over a period of time; in the current context this means allowing for an overshooting in order to compensate for the prolonged shortfall of inflation from the target. Other measures, like extending the forward guidance or targeting the yield curve via asset purchases, will likely tilt policy towards a more dovish stance.

Stubbornly low inflation to trigger ECB easing

Powerful Draghi statement heralds bold ECB policy action

Notwithstanding the closing of the output gap, higher wage growth and producer prices having embarked on a higher trend, underlying inflation in the euro area failed to pick-up meaningfully. Following a period of disinflation from 2014 to 2016, core inflation recovered above the 1% threshold but hovered around at only 1.2% yoy since then. This is at odds with previous expectations of the market as well as the ECB. Market-based inflation expectations fell strongly sparking doubts about the

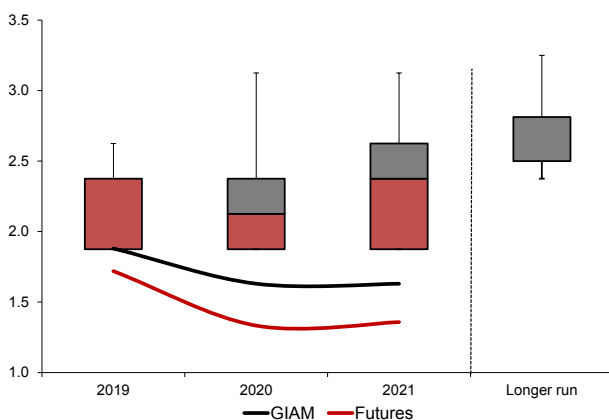
credibility of the ECB's inflation target. In a recent seminal speech at Sintra, ECB President Draghi became quite explicit in stating that *"In the absence of improvement, such that the sustained return of inflation to our aim is threatened, additional stimulus will be required"*.

In fact, we share this concern about inflation. Looking ahead, we see factors at work which will cause core inflation to only slightly trend higher next year: Growth has lastingly come down from its peak thereby reducing the cyclical price pressure, the latest fall in oil prices will not reverse in our view and feed through while falling inflation expectations argue in favor of a more muted price-setting behaviour. Additionally, the US-Chinese trade conflict leads to trade diversion towards the euro area, engineered through lower import prices.

Against this backdrop we think that Draghi's latest speech was the announcement of bold ECB action. He deliberately stated that the whole set of instruments was available. We expect the ECB to announce by September a 10 bps deposit rate cut, to move towards a tiered deposit rate system in order to mitigate the fallout from long lasting negative rates on banks, to enhance its forward-guidance (by linking it to inflation) and to resume corporate QE. Depending on the situation and the potential materialization of key risks (e.g. hard Brexit, trade) also sovereign QE could come back on the table already this year.

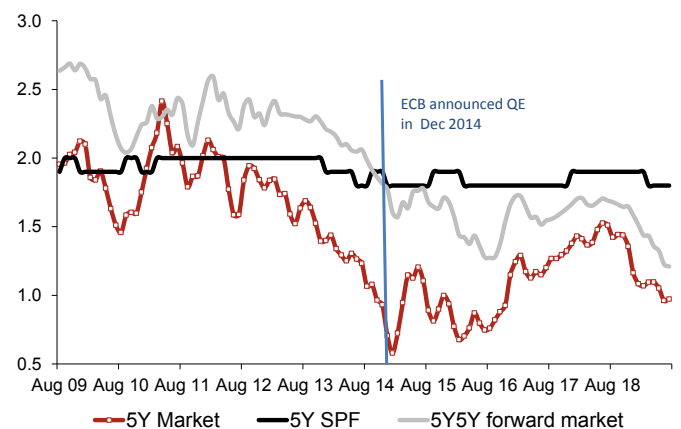
ECB to act in September by lower rates, extension of forward guidance and re-start of corporate QE

Table 1: Fed FUNDS RATE: FOMC PROJECTION AND FORECASTS



Extremes and quartiles of the distribution of FOMC members' views.

Table 2: EURO AREA INFLATION EXPECTATIONS



Market (implicit average inflation expectations from inflation swaps) versus Survey of Professional Forecasters (SPF), monthly data 2

BoJ rate cut has become more likely late this year

BoJ action to be accompanied by measures to mitigate side effects

At its latest meeting, the Bank of Japan (BoJ) policy board gave no obvious hint that it would follow the Fed or ECB soon. However, given our easing expectations for the Fed and ECB, the persistent strength of the yen, a continued cyclical slowing of growth in Japan's dominant trading partners (backfiring on domestic capex) as well as Japan's inflation rate to ease again, the BoJ could also be forced into action. We now see a short term policy rate cut by 20 bps late this year slightly more likely than not. Given the BoJ's already stretched policy tools, any action would be accompanied by measures to mitigate its negative side effects. Among the measures discussed, an extension of the loan program looks the most likely.

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Fixed Income

- The downtrend in core yields continued in Q2. Driven by dovish central banks and mixed economic data yields fell across the curve. Euro area benchmark yields even marked new historical lows.
- Looking ahead, the downtrend is forecast to slow but unlikely to reverse. Given the expected start of an easing cycle by the Fed and new extraordinary measures by the ECB, there is some scope for a further decrease in core yields.
- Southern euro area government bonds performed very well in Q2. Given the expected backstop by the ECB, there is leeway for risk premiums to fall further. While Italian BTPs have the greatest leeway to perform well, the uncertain political situation is forecast to keep its government bond spread on an elevated level.

New historical lows for Bund yields across the curve driven by dovish ECB signals

The downturn in core yields continued and even accelerated in Q2 2019. The lack of a lasting upward movement in inflation rates and on balance weaker economic data than expected triggered lower yields across the board. Both, inflation expectations and real yields contributed to this development. While inflation expectations fell for all maturities in the US and in the euro area, the development is particularly noteworthy in the euro area. With 5-year forward inflation expectations at 1.15% and even close to 1.00% for 10-year inflation expectations, euro area inflation expectations have further detached from the ECB's medium-term inflation target.

Bund yields marked new historical lows almost daily in June. After the speech given by ECB President Draghi at Sintra, financial markets priced further extraordinary monetary policy measures. Accordingly, 10-year Bund yields reached a new historical low at -0.33% at the end of June (26 bps lower than at the end of March). 2-year Bund yields fell as well. They decreased by 15 bps to 0.75%. Over the same period, the US curve bull steepened. 10-year US yields fell from 2.41% to 2.01% and 2-year US yields decreased by even 51 bps to 1.75%.

Central banks to determine market development in Q3

Going forward, central banks are likely to set the tone for government bond markets in Q3 as well. The Fed is seen to start its easing cycle already in July. A first key rate cut by 25 bps will likely be followed by another one in September. This will bring the upper bound of the Fed Funds target to 2.00% during the next three months. Historically, the start of the easing cycle is associated with a further steepening of the 2-year/10-year curve. There should be no exception this time. As long-dated US yields have some further leeway to decrease (not least due to supportive seasonals in Q3), the drop in 2-year yields is forecast to be even more pronounced.

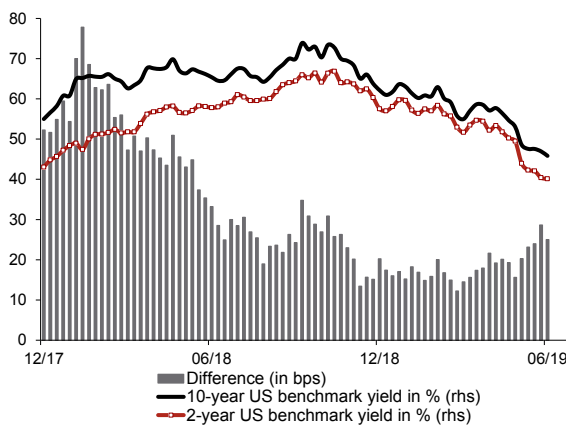
However, in contrast to current market expectations we only expect a shallow easing cycle. While financial markets discount five key rate cuts until the end of 2020, we await a shorter cycle. According to our forecast, the Fed will stop after a third cut in H1 2020. Hence, the scope for short-dated US yields to fall further on a medium-term horizon appears more limited and 10-year Treasury yields are seen to rebound slightly to current levels on a one-year horizon.

Lagarde to continue dovish monetary stance from November onwards – triggering even lower euro area core yields

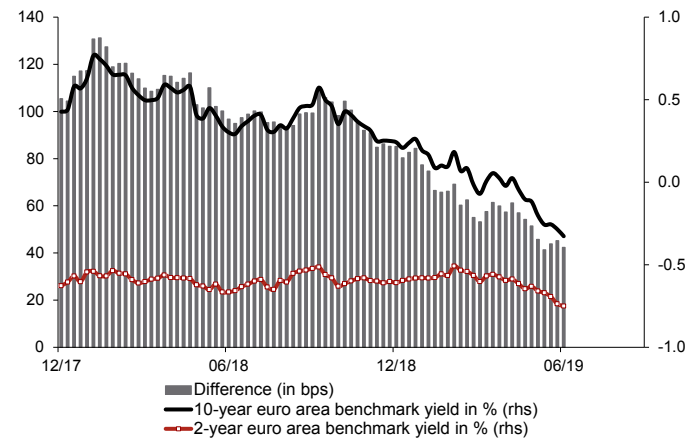
The comments by ECB President Draghi at Sintra will set the stage for euro area government bond markets for the months to come. Although there appear to be some dissenting views in the Governing Council, the likely successor as ECB President, Christine Lagarde, is expected to follow a similar dovish approach from November onwards. Although the central bank is unlikely to restart PSPP (Public Sector Purchase Programme) already in Q3, it will remain in the central bank's tool box for the time being. Depending on the flow of incoming economic data and particularly the inflation environment, the ECB might revert to PSPP 2.0 later on. At

least, financial markets will continue to speculate about a corresponding programme. Notwithstanding, the ECB will most likely implement further extraordinary monetary policy measures in the course of Q3. This will be sufficient to keep euro area core yields on a very low level and even depress them slightly more. Therefore, there is scope for even lower Bund yields on a 3-month horizon and new historical lows will most likely be marked over the course of Q3. For a sustainable yield increase, an upward movement in inflation expectations appears necessary. This is unlikely to be the case in the near term. Still, on a 12-month horizon, the new ECB measures are likely to have an impact. Accordingly, 10-year Bund yields can rise slightly above current levels by the mid of 2020 again.

Graph 1: US: SHORT- AND LONG-DATED GOVERNMENT YIELDS



Graph 2: EA: SHORT- AND LONG-DATED GOVERNMENT YIELDS



Outperformance of peripheral bonds to continue

The performance of Southern European government bonds was impressive in Q2. Driven by falling underlying yields and compressing spreads particularly long-dated government bonds yielded double-digit returns. Although the spread tightening will likely slow in Q3, the trend is not expected to reverse as the backstop by the ECB removed some tail risks. Above all, the search for yield will force investors into lower-rated and longer-dated sovereign bonds.

A special case remain Italian BTPs. Italian government bonds are the only IG bonds which still offer a reasonable yield level. Despite the spread tightening and decrease in underlying yields, it is still almost at 2%. With the ECB potentially entering the market again, this level will be irresistible for many investors in the current low yield environment. What is more, the recent political news flow was reassuring and the tone was more conciliatory. For the time being, an excessive deficit procedure will be avoided as the government pledged to rein in the 2019 deficit. Hence, Italian BTPs have leeway to be among the best performing government bonds in Q3.

Looking further down the road, however, an agreement on the 2020 budget remains a major hurdle. While the government aims at tax cuts, the EU Commission will insist on compliance with the budget rules. Given the high level, the debt ratio remains on the verge of becoming unsustainable. Accordingly, spread levels as of spring 2018 (before the current government took power) will remain out of reach.

BTP yield level irresistible for investors in the low yield environment – continuation of strong performance in Q3

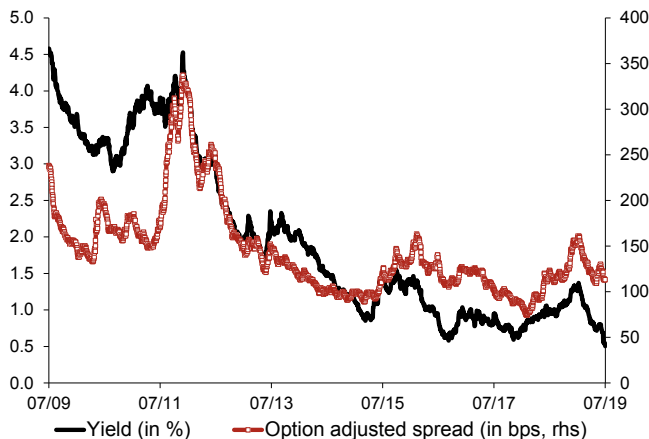
Corporate Bonds

- Euro area corporate bond spreads were on a roller coaster ride in Q2. Two strong months were interrupted by a weak May. Overall, spreads tightened moderately and due to falling underlying yields corporate bonds performed well in Q2.
- The technical situation of euro area corporate bonds remains benign. Moreover, the forecast restart of CSPP will provide additional support for euro area corporate bonds, going forward. Hence, spreads have considerable scope to tighten in Q3.
- Accordingly, the near-term total return outlook is good. However, given the reached yield level the longer-term return view is rather gloomy.

EA corporate bonds on a roller coaster ride in Q2

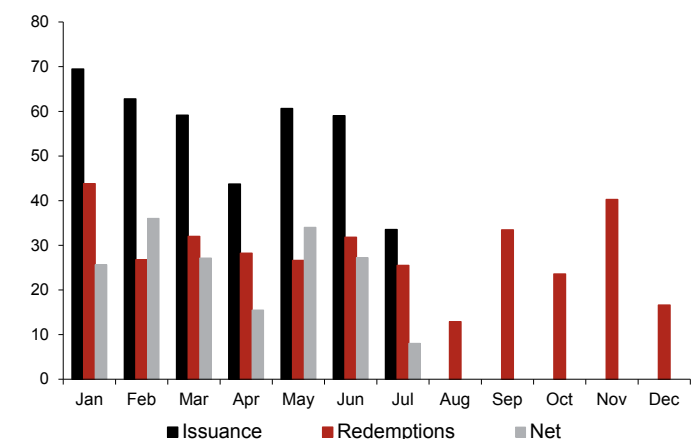
After a good start into the year, corporate bonds continued to perform well in April and spreads marked an annual low at the beginning of May. Triggered by the provisional breakdown of the US/China trade negotiations and the resignation of UK Prime Minister May, increasing the tail risk of a hard Brexit, spreads widened. Eventually, corporate bond spreads compressed again. This was mainly due to a dovish shift of central banks. Not only did the Fed indicate the start of an easing cycle, but ECB President Draghi signaled in a speech given at Sintra further extraordinary monetary policy measures.

Graph 1: EA IG CORPORATE BONDS



Source: Bank of America Merrill Lynch

Graph 2: 2019 EA IG CORPORATES: ISSUANCES AND REDEMPTIONS



In bn EUR, 500m EUR and up

All in, euro area corporate bond spreads tightened by 10 bps in Q2. Financial spreads tightened slightly more than non-financial ones (11 bps versus 9 bps). Euro area HY spreads compressed a bit more by 18 bps. On top of narrowing spreads, the underlying yield decreased as well. Hence, euro area IG corporate bonds yielded a total return of 2.6% in the second quarter (non-financials 2.7% and financials 2.3%). Despite the stronger spread tightening euro area HY corporates achieved only a return of 2.3% in the past quarter (due to a lower duration).

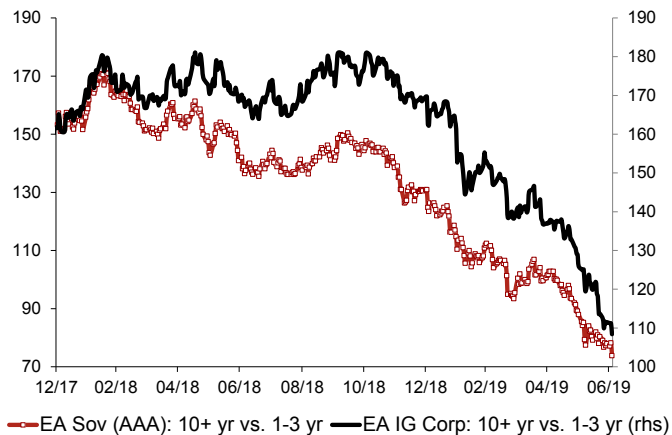
Forthcoming ECB purchases to trigger further spread tightening

Benign technical situation – strong supply taken down smoothly

The technical situation of euro area corporate bonds will support this asset class, going forward. Over the past months, fund inflows have been positive signalling the healthy demand for corporate bonds. This is likely to remain the case as despite the drop in corporate bond yields the decrease was even more pronounced for many other fixed income classes. Hence, the relative attractiveness of corporate bonds

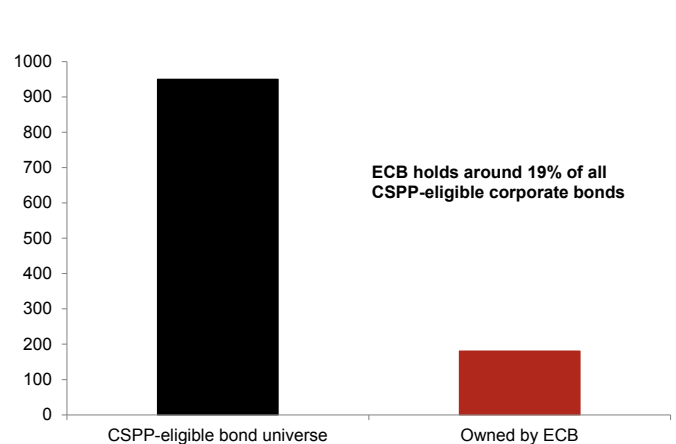
increased. This has helped over the recent months (and will continue to do so) to take down the large supply. Net issuance has been positive in every month and gross supply is running well ahead of last years' volume.

Graph 3: CREDIT CURVE FLATTENING IS LAGGING



Source: Bank of America Merrill Lynch

Graph 4: CSPP 2.0: MUCH LEEWAY FOR PURCHASES



Market value in bn EUR

ECB to determine market development in Q3 – further spread compression likely

A main factor for euro area corporate bonds will be the expected relaunch of the Corporate Sector Purchase Programme (CSPP). Although President Draghi did not explicitly mention it, we expect CSPP 2.0 to be a part of the coming ECB package. Compared to other asset classes there are less constraints. Currently, the ECB owns less than 20% of all eligible corporate bonds. Taking into account a self-imposed limit of 70%, the ECB can theoretically buy almost €500 bn of corporate bonds. While this is only a theoretical magnitude, it shows there is much leeway for corporate bond purchases by the ECB and the central bank is likely to have a strong focus on corporate bond purchases. The above calculations show that there is little need for the ECB to adjust the criteria. Hence, the inclusion of financial bonds and/or buying of HY bonds does not appear to be a necessary condition at this point.

Accordingly, we expect euro area corporate bond spreads to tighten meaningfully in the third quarter – particularly at the long end of the curve. Generally, spreads of long-dated corporate bonds tend to tighten more than spreads of short-dated ones in such an environment. Moreover, the credit curve flattening is lagging the sovereign bond curve. The intensified search for yield will force investors to extend the maturity, triggering a further flattening of the credit curve.

The bad awakening will follow, but not in 2019

Hence, the short-term outlook for euro area corporate bonds appears rather bright as underlying yields are unlikely to rise. However, the longer-term outlook looks more gloomy. While the trade conflict is unlikely to be solved for good anytime soon, the US will increasingly feel the headwinds from a fading fiscal stimulus. Beside these fundamental issues, the achieved corporate yield level will prevent any meaningful return, going forward. At a historically low corporate yield level of 0.50%, future returns will be limited for arithmetical reasons. However, this is unlikely to be a concern for the months to come as 2019 will provide very decent returns. But, looking into 2020 financial markets will have to cope with a low underlying yield level and quite compressed spreads.

Currencies

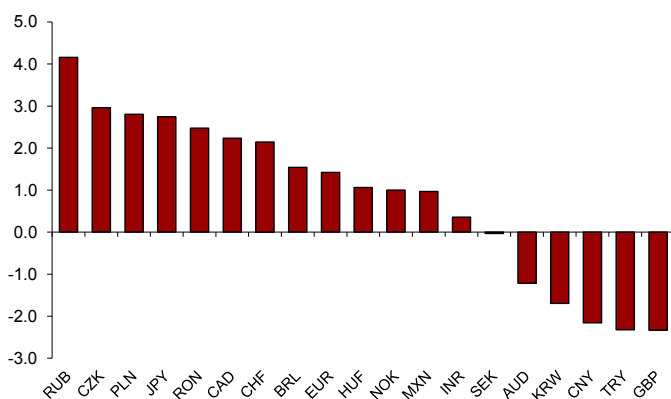
- The US economy has started to feel the headwinds from a fading fiscal stimulus and the adverse effects of trade uncertainties, while the Fed is embracing rate cuts (starting in July). We see the USD generally trending weaker in H2.
- Near term, EUR/USD may yet struggle to gain traction, with persistent trade uncertainties and the potential for meaningful policy accommodation by the ECB keeping a lid on the euro near term.
- We see some upside for the still undervalued JPY, even though USD/JPY already discounts deeper Fed cuts.
- EM currencies remain generally cheap. Trade woes and headwinds to global manufacturing keep weighing, but Fed rate cuts and a general softness in the USD should help to benefit exposure to EM carry.

Global uncertainties have left their mark on exchange rates in Q2, though volatility remains muted. The flight to safety and falling yields boosted JPY and CHF, while CNY and trade-linked currencies like KRW and AUD came under pressure. Renewed concerns about rising risks of a hard-Brexit under a new British PM sent sterling lower, rendering GBP the worst performer among major currencies (Graph 1).

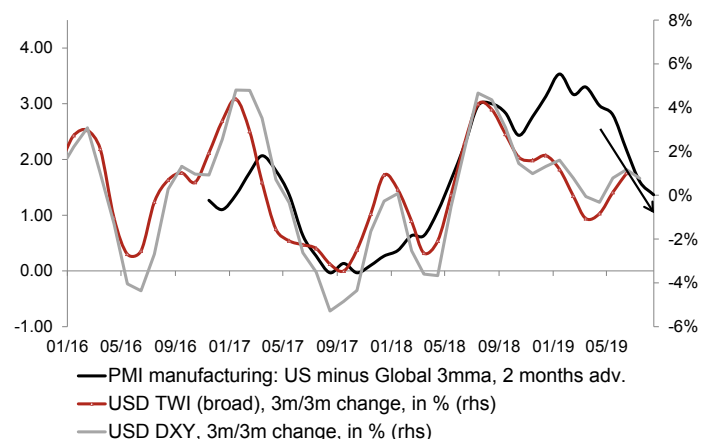
USD is now benefitting much less from global trade uncertainties

For most of last year, the USD tended to benefit from rising trade fears. Safe haven flows and the rationale that the damage from tariffs to the rest of the world would be greater than for the US seemed to be the prevailing rationale. This has changed. The measures put on hold at the G-20 summit (25% on another US\$ 200 bn of imports from China) would impact US consumers much more directly. Also, the Fed has become more susceptible to trade war risks, with Chair Powell mentioning them as a key issue to monitor and to “act as appropriate”. As a consequence, the tides in trade concerns will matter less for the EUR/USD going forward.

Graph 1: FX PERFORMANCE IN Q2



Graph 2: USD and US VS GLOBAL GROWTH



* vs. US dollar between 29/3/2019 and 28/6/2019, in %

While we generally deem the USD past its peak on looming Fed rate cuts, fading economic outperformance (Chart 2) and a widening twin deficit (fiscal/external), EUR/USD will still struggle to gain traction for a while. The euro area (and Germany in particular) is still hostage to slowing global trade and high policy uncertainties. The ECB is on course of cutting and tiering the deposit rate and to resume asset

Short-term benefits from USD carry, but only with tight stop losses

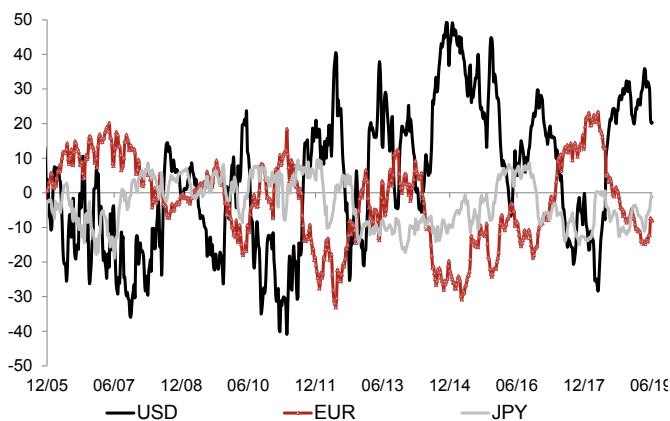
Much of recent JPY strength is owing to plummeting US rate expectations

purchases – which will keep a lid on the EUR. So for a while, a still rather stable EUR/USD may favor taking some exposure on USD for the sake of the carry (2.7% p.a.). For later in H2, however, we still expect the next move to be a leg *higher* in the EUR/USD. And with the USD vulnerable to a reversal of still high speculative positions (Graph 3), any USD exposure will warrant close monitoring and setting tight stop losses.

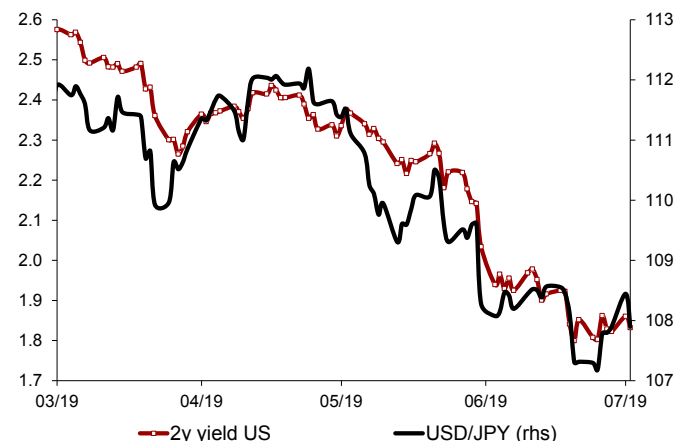
Yen already pricing deeper US rate cuts

The decline in the USD/JPY has already realized much of our yen strength we expected. We still hold a constructive view on JPY for the remainder of the year, not least due to its still undervalued levels. That said, the recent JPY rally is already discounting marked rate cuts by the Fed. Furthermore, with acute trade tensions easing after the resumption of US/China negotiations, safe haven flows into the yen may also ebb. Barring a continued fall in US yields, we thus anticipate the move in USD/JPY to our 12-month target of 105 to be much more gradual and subject to temporary reversals.

Graph 3: SPECULATIVE POSITIONS



Graph 4: USD/JPY AND FED EXPECTATIONS



Value of net positions in bn USD (CFTC data, own calculations)

CNY burdened by trade tensions and headwinds from trade, but a break above 7.00 in USD/CNY is unlikely barring a further trade war escalation.

Dovish Fed and easing USD to benefit EM FX

We anticipate Chinese yuan (CNY) to remain burdened by the trade tensions and the headwinds from global demand. However, barring a sharp escalation of the trade war (with a 10-25% US tariff on all Chinese shippings to the US), the USD/CNY is unlikely to break the threshold of 7.00, given Chinese concerns about the repercussions on Chinese financial markets and capital outflows.

EM FX more broadly are generally cheap and have not matched the recent relief rally in EM bonds. The dovish Fed and more generalized USD weakness will also help EM FX while the slump in global manufacturing and trade uncertainties keep weighing. We see some value from a carry perspective in CZK and PLN (CEE macro resilience, less leeway for monetary easing) and MXN (high carry of more than 8%, while Mexican efforts to comply with Trump's demands on immigration have eased concerns about higher US tariffs).

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Equities

- Equities experienced another good quarter, albeit investors maintained a cautious stance in their sector preference.
- While political risks decreased only marginally, the central bankers reinforced their dovish stance. The spread of dividend yield minus credit yield continued to rise, rendering a higher equity appeal (through lower cost of capital).
- We maintain a positive outlook with total returns of 4-5% in 12 months, suggesting increasing the equity allocation.
- We are less defensive inside the equity space, favoring a slight OW of EMU vs the US (euro hedged), OW EM (India, CEE, and Brazil) and UK and staying neutral on Switzerland and Japan.

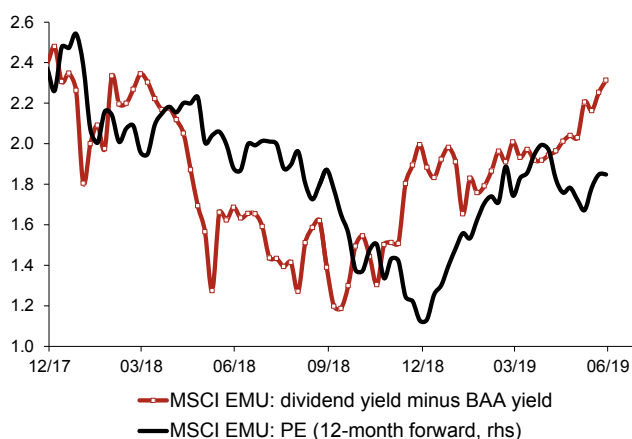
In the last three months equities performed well, although investors maintained a cautious stance in their country and sector preference. While political risks decreased only marginally, the central bankers reinforced their dovish stance, inducing a higher equity appeal. The S&P 500 beats the MSCI EMU index (+4.8% vs 3.8%) and the two defensive markets, FTSE100 and SMI, overperformed (3.9% and 7.3%, respectively), while both the Topix (-2.4%) and the MSCI EM index (-0.7%) underperformed. Finally both Cyclical and Value stocks underperformed the Defensive and Growth ones.

Increasingly dovish stance by central banks drive yields lower, causing markets' fair values to rise.

Central bankers' dovish stance induces a higher equity appeal

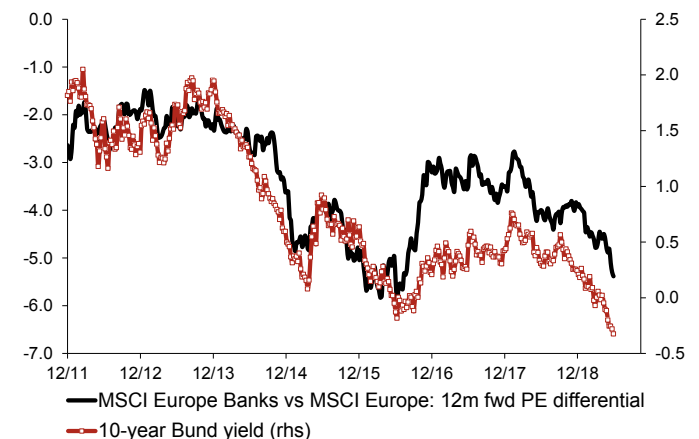
Trade frictions mitigated slightly in the last weeks due to the truce declared at the G20. Brexit and Italian risks linger (being more contained short term in the case of Italy) but, more importantly, global central banks have become increasingly dovish. Such stance triggered lower 10-year rates, sovereign spreads and credit yields. As a

Graph 1: MSCI EMU: RISK PREMIUM



Using BAA yields

Graph 2: EU BANKS RELATIVE PE AND BUND YIELDS



EU Banks' PE differential versus MSCI Europe

US valuations more appealing via lower yields, offset in part by higher risks (politics/growth).

consequence, firms are enjoying a decreasing cost of capital (COE) and global equity fair values have correspondently increased thanks to lower yields. The spread of dividend yield minus credit yield continued to rise rendering a higher equity appeal. Furthermore, equity positioning stays low, with composite tactical indicators ranging from neutral to a buy signal. Less helping are the earnings revisions which are still trying to find a bottom but might be not there yet: we remain below consensus for 2020-2021. Also, in a global context, mid-term valuations are still quite rich in the US.

With central banks remaining supportive, we maintain a positive outlook with decent total returns (4-5%), suggesting increasing the equity allocation.

Getting neutral on the SMI as its relative appeal has diminished after the index's good outperformance.

Add risk tilt: OW FTSE, EM and EMU vs USA. N SMI and Topix

US unit-labor costs and Nipa profits' momentum represent a positive for the next three months. They should remain benign till Q3 2019, then starting to worsen according to our model, and due to still weak global export, capacity utilization momentum and manufacturing confidence. We see only a limited advantage for the EMU vs the US, despite cheaper euro area (EA) valuations, due to higher EA political risks and because the respective GDP growth, adjusted for the TW currency and central banks' assets momentum, still does not bode particularly well for EA PEs.

We are less defensive inside the equity space, favoring a slight OW of EMU vs the US (euro hedged). We stay neutral on Switzerland (from OW) and Japan (accumulate the latter on weakness). Slightly OW EM and UK (low valuations and positioning, plus marginally lower pound in the next three months). We are neutral on cyclicals vs. defensives, and OW only on Utilities and discretionary ex-auto. UW: Real Estate, Materials and IT. Neutral on other sectors. Slightly UW Small cap Growth vs Large cap Value. On styles, we suggest a limited OW on Momentum and Low Leverage (contained valuations and defensive quality). Neutral Quality (rich valuations), and Growth vs Value (the latter is most undervalued but remains hostage to low yields).

EM: to benefit from sentiment boost and weakening USD

Over the quarter, Emerging markets (EM) have decreased by ca. 2% due to increasing trade tensions. Fundamental valuations are relatively cheap: multiples are trading at a discount of 6% vs historical average, while the cyclically-adjusted PE is almost one standard deviation below average. The trade frictions have already had

Table 1: EQUITY MARKETS VALUATION DASHBOARD

Markets	Price / Earnings *		Price / Book *		Price/ Cash Flow *		Dividend Yield *		Avg. Discount, %
	current	hist. avg.	current	hist. avg.	current	hist. avg.	current	hist. avg.	
WORLD	15.9	16.0	2.3	1.9	10.6	8.8	2.6	2.7	10.9
USA	17.3	15.3	3.2	2.4	12.4	9.9	2.0	2.2	19.6
JAPAN	12.7	15.4	1.1	1.3	7.1	7.1	2.6	1.9	-16.1
UK	12.7	13.8	1.7	1.8	8.2	7.9	4.6	4.0	-6.1
SWITZERLAND	16.9	15.4	2.6	2.2	11.6	11.2	3.3	3.3	7.8
EMU	13.4	14.1	1.5	1.5	7.8	6.5	3.6	3.9	5.0
FRANCE	14.1	14.3	1.6	1.5	8.5	7.0	3.5	3.7	8.1
GERMANY	12.9	15.0	1.5	1.5	8.1	6.7	3.4	3.4	1.0
GREECE	14.0	12.8	2.3	1.6	7.5	6.1	4.7	4.0	14.8
ITALY	11.1	15.1	1.2	1.2	5.2	4.7	4.7	4.7	-3.3
PORTUGAL	15.2	12.8	1.8	1.7	5.6	5.9	4.9	4.5	2.6
SPAIN	11.7	12.9	1.2	1.6	5.1	5.1	4.7	5.1	-6.9
EURO STOXX 50	13.5	13.2	1.6	1.5	8.0	6.2	3.8	4.2	12.0
STOXX SMALL	15.9	14.5	1.7	1.7	9.5	8.4	3.1	3.2	7.0
EM, \$	12.3	14.4	1.5	1.6	7.1	7.5	3.1	3.1	-6.8
BRAZIL	12.5	9.1	1.9	1.7	8.0	13.5	3.6	4.3	6.4
RUSSIA	5.6	7.0	0.8	0.9	3.8	4.4	7.6	3.9	-36.1
INDIA	18.3	14.6	2.6	2.7	11.9	11.5	1.7	1.6	5.4
CHINA	11.6	12.9	1.5	1.7	7.2	7.5	2.4	3.0	-2.5

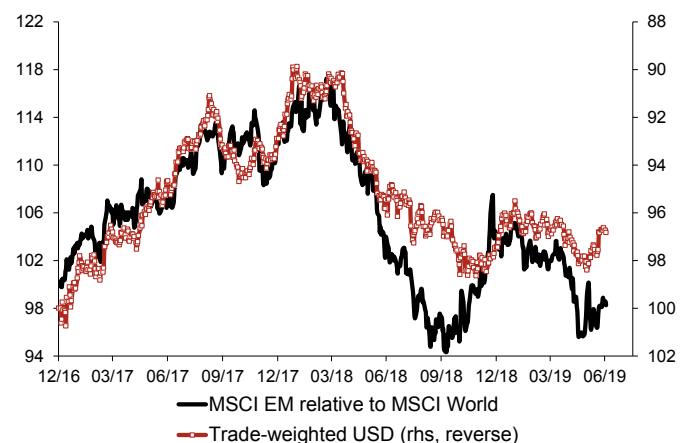
Note: The first four markets (ex. World) are based on the main local indices, the rest on the corresponding MSCI indices.

*Multiples are based on 12m forward estimates; PEs are since 1987, the rest is since 2003.

Discount in % to historical average: blue and negative numbers = undervaluation. Red and positive numbers = overvaluation.

Source: Thomson Reuters Datastream. IRFS estimates

Graph 3: EM RELATIVE TO DM AND TRADE-WEIGHTED USD



EM: a risk-on rally on expectations of Fed easing.

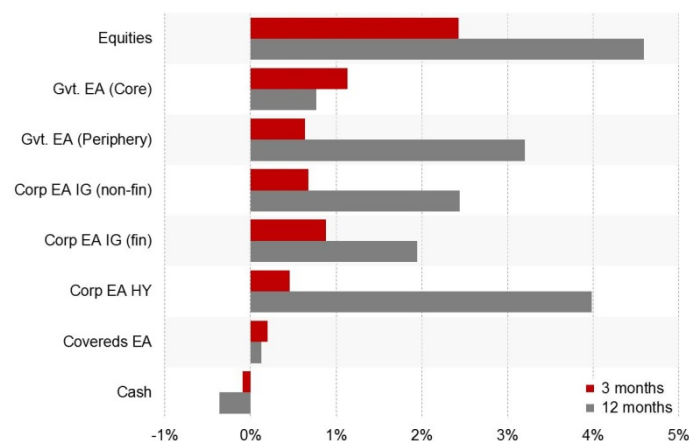
its toll on trade growth and global earnings. As of late, earnings revisions for EMs vs DMs have been revised up and the USD looks peaking. Growing external pressures, low inflation, and increasing expectations for Fed rate cuts point to a new wave of easing by EM central banks. Following the truce reached at G20 between the US and China, the EM equities are to be supported by the boost in sentiment, which is to continue at least in the short term. The weakening dollar represents an important positive driver in the longer term. Other than lower valuations, EM equities are to benefit from a more benign growth outlook vs. advanced economies. Risks come from possible disruptions in the follow-up trade negotiations, thus affecting corporate sentiment and causing short-term market adjustments.

Asset Allocation

- Global growth uncertainties, falling inflation expectations and a continued dovish shift by major central banks will keep core yields at depressed levels.
- The growing search for yield is expected to lend support to risk assets. Particularly credit and equity should continue to get tailwind for the time being. But also USD-denominated spread products are expected to benefit.
- We thus recommend to increase the overweight in these asset classes and to reduce the underweight in core government as well as quasi government bonds.
- In turn, the overweight in cash and inflation linked bonds should be reverted into a straight underweight.

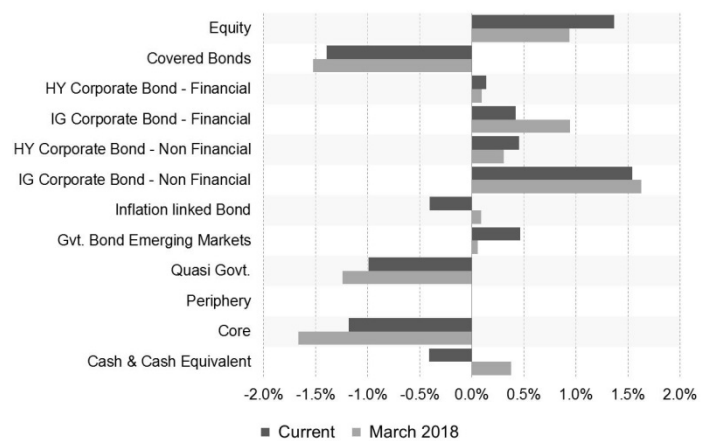
The increasingly accommodative tilt by central banks had a firm grip on fixed income markets and is expected to continue to do so for the time being. Especially the recent comments by ECB President Draghi triggered another drop in euro area core government bond yields which is unlikely to revert any time soon, thus bringing total return expectations for medium- and long-dated core govies back into positive territory. Corporate bonds are expected to benefit either from a potential inclusion in the next ECB purchases (IG) or at least from the chase for higher yields (HY). The latter is also true for equities which are expected to roughly deliver between two and three percent hedged into euro on a three-month horizon. In case of USD-denominated government bonds a weaker EUR/USD, a dovish Fed, and also the

Graph 1: AGGREGATED TOTAL RETURN FORECASTS



Hedged into EUR; Periphery = Italy

Graph 2: ACTIVE POSITIONS VS LAST QUARTER



In pp; Periphery = Italy

hunt for yield are anticipated to trigger tighter spreads.

Tactical pro-risk stance to be maintained

Under these conditions, short-dated bonds and cash turn out to be the least attractive asset classes whereas long-dated fixed income assets, EM government bonds (USD), and equities appear to be the most promising investments in the near term. Apart from cash and inflation linkers the recommended tactical positioning resembles pretty much the last quarter's one. That said, within the fixed income segments there is now a clear preference for the long maturity buckets which should be overweighted throughout. Bottom line, this implies to go tactically slightly long duration.

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Forecasts

GROWTH

	2018	2019f	2020f	2021f
US	2.9	2.4	1.7	1.8
<i>Euro area</i>	1.9	1.1	1.3	1.3
Germany	1.5	0.8	1.3	1.3
France	1.6	1.2	1.2	1.8
Italy	0.9	0.0	0.6	0.8
<i>Non-EMU</i>	1.5	1.4	1.5	1.7
UK	1.4	1.4	1.5	1.7
Switzerland	2.5	1.2	1.5	1.6
Japan	0.8	0.6	0.3	0.8
<i>Asia ex Japan</i>	6.2	5.8	5.8	5.8
China	6.6	6.3	6.2	5.8
Central/Eastern Europe	3.3	1.7	2.7	2.8
Latin America	0.3	0.3	2.1	2.0
World	3.6	3.1	3.2	3.3

INFLATION

	2018	2019f	2020f	2021f
US	2.4	1.9	2.0	2.1
<i>Euro area</i>	1.7	1.3	1.3	1.4
Germany	1.8	1.5	1.4	1.5
France	1.9	1.2	1.4	1.6
Italy	1.1	0.8	1.1	1.1
<i>Non-EMU</i>	2.3	1.9	1.9	1.7
UK	2.5	2.0	2.0	1.7
Switzerland	0.9	0.6	0.8	1.0
Japan	1.0	0.6	0.9	0.8
<i>Asia ex Japan</i>	2.6	2.8	2.8	2.7
China	2.1	2.6	2.4	2.2
Central/Eastern Europe	6.1	7.4	5.8	4.8
Latin America	4.0	4.0	3.7	3.6
World	2.7	2.7	2.6	2.5

Regional and world aggregates revised to 2015 IMF PPP weights; Latin America Inflation excluding Argentina and Venezuela

FINANCIAL MARKETS

3-month LIBOR					Corporate Bond Spreads				
	Current	3M	6M	12M		Current	3M	6M	12M
USD	2.32	2.15	1.90	1.70	<i>BofAML Non-Financial</i>	111	95	95	90
EUR	-0.39	-0.40	-0.40	-0.40	<i>BofAML Financial</i>	118	105	105	100
JPY	-0.07	-0.05	-0.20	-0.20	Forex	Current	3M	6M	12M
GBP	0.77	0.80	0.80	0.80	EUR/USD	1.14	1.13	1.16	1.18
CHF	-0.73	-0.75	-0.75	-0.75	USD/JPY	108	107	106	105
10Y Government Bonds	Current	3M	6M	12M	EUR/JPY	123	121	123	124
US	2.02	2.00	2.05	2.10	GBP/USD	1.27	1.25	1.36	1.37
<i>Euro-Area</i>	-0.32	-0.35	-0.30	-0.25	EUR/GBP	0.90	0.91	0.85	0.86
France	0.01	-0.05	0.00	0.05	EUR/CHF	1.11	1.11	1.12	1.13
Italy	2.12	2.00	2.00	2.00	Equities	Current	3M	6M	12M
Japan	-0.15	-0.15	-0.10	-0.05	S&P500	2927	2996	3005	3027
UK	0.83	0.85	0.90	0.95	MSCI EMU	122.1	124.8	124.0	123.2
Switzerland	-0.53	-0.45	-0.40	-0.30	TOPIX	1546	1570	1570	1566
Spreads	Current	3M	6M	12M	FTSE	7415	7550	7530	7470
GIIPS	162	155	150	145	SMI	9865	10040	10000	9880
<i>BofAML Covered Bonds</i>	49	45	45	45					
<i>BofAML EM Gvt. Bonds (in USD)</i>	288	280	290	305					

As of 28.06.19 (3-day-average)

FORECAST-INTERVAL* – 3-MONTHS HORIZON

Government Bonds (10Y)	US	1.78	2.00	2.22
	Germany	-0.42	-0.35	-0.28
	UK	0.69	0.85	1.01
	Switzerland	-0.58	-0.45	-0.31
	10Y-GIIPS Spread	121	155	189
Spreads	BofAML Covered Bonds	37	45	53
	BofAML IG Non Financial	81	95	109
	BofAML IG Financial	90	105	120
	BofAML EM (in USD)	251	280	309
Forex	EUR/USD	1.10	1.13	1.16
	USD/JPY	103	107	111
	EUR/GBP	0.88	0.91	0.93
	EUR/CHF	1.09	1.11	1.13
Equities	S&P500	2,857	2,996	3,135
	MSCI EMU	118.3	124.8	131.3
	TOPIX	1,478	1,570	1,662
	FTSE 100	7,192	7,550	7,908
	SMI	9,601	10,040	10,479

FORECAST-INTERVAL* – 12-MONTHS HORIZON

Government Bonds (10Y)	US	1.62	2.10	2.58
	Germany	-0.38	-0.25	-0.12
	UK	0.62	0.95	1.28
	Switzerland	-0.55	-0.30	-0.05
	10Y-GIIPS Spread	84	145	206
Spreads	BofAML Covered Bonds	28	45	62
	BofAML IG Non Financial	64	90	116
	BofAML IG Financial	72	100	128
	BofAML EM (in USD)	247	305	363
Forex	EUR/USD	1.11	1.18	1.25
	USD/JPY	97	105	113
	EUR/GBP	1.11	1.18	1.25
	EUR/CHF	97	105	113
Equities	S&P500	0.80	0.86	0.92
	MSCI EMU	1.07	1.13	1.19
	TOPIX	2,769	3,027	3,285
	FTSE 100	109.2	123.2	137.2
	SMI	1,366	1,566	1,766

*The forecast range for the assets is predetermined by their historical volatility. The volatility calculation is based on a 5 year history of percentage changes, equally weighted in the case of the 12-month forecast and exponentially weighted in the case of the three month forecast. The length of the bars within each asset group is proportional to the relative deviations from their mean forecasts.

Imprint

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Issued by:

Generali Insurance Asset Management
Macro & Market Research

Version completed on July 5th, 2019

Sources for charts and tables:

Thomson Reuters Datastream, Bloomberg, own calculations

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