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# Q 01 / 2019

## Quarterly Investment Review and Outlook

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# Quarterly Report – Q01/2019

## At a glance

**Review – 1st Quarter of 2019**

### 1. EPS Expansion

- The bull market that began ten years ago has still further to go (long-term).
- The usual catalysts for a bear market are absent: no confirmed signs of a US recession, no EPS peak visible (though increases are less important than in the past), no real macro imbalances (apart from the level of Chinese debt when put in context with the lower GDP growth), and no inflation risk. This view remains valid provided there are no monetary policy mistakes made by central banks.
- EPS discrepancies between brick-and-mortar style companies and new digital orientated ones are important, though.

### 2. List of ongoing concerns

- **Volatility**: Volatility recently increased after worries regarding economic growth resurfaced following disappointing PMIs in March. However, the composite index for the whole EMU appears to be more or less stabilized over the past 4 months, and is consistent with our forecast of GDP growth close to 1% in 2019 (yearly average).
- **Brexit, the situation remains confusing:** Fueled by recent UK officials' pessimistic comments, a hard Brexit is now to be expected. Costs: about 2% of the GDP for the UK and about 1.5% for the EU.
- **Mind the construction cycle gap:** We believe the European residential and non-residential construction cycle is losing momentum, particularly in markets that have fared very well in recent years (e.g., France, Northern Europe and Germany). This slowdown is underlined by our economic forecasts—that is, we expect Eurozone and Swiss economic growth to decline from last year's 1.8% and 2.5% respectively to 1.1% and 0.9%. Moreover, markets outside of Europe, such as the US and Australia, face a similar slowdown. By contrast, infrastructure investment in Europe continues to rise. So, the most attractive investment opportunities we see favor infrastructure activity over private construction.

### 3. Valuation

- **Equity valuations:**
  Global equities have bounced back strongly from their December losses, and global earnings downgrades have started to slow. The rebound has been supported by the dovish turnaround of the Fed and progress on US-China tariff negotiations. **Valuations now appear closer to fair value,** although political and macro risks cannot be fully discounted. Thus, we remain overweight on global equities but are reducing the size of our position.
- **Bond valuations:**
  Interest rate related concerns will remain elevated during 2019. With ongoing soft QE, the speed of monetary normalization and inflation may be misestimated. Bonds could therefore be the opportune risk-off play.

### 4. Central Bank actions

- **ECB:**
  - The ECB is expected to downgrade its economic forecast for the Eurozone in order to justify additional financing for European banks.
- **FED:**
  - The FED has solidified its U-turn in monetary policy on the back of weak economic growth.
  - Zero rate hikes for 2019 are now incorporated, with another one for 2020.

## Key concerns

This is an ongoing register, and we have currently identified at least 8 known potential sources of risk that could impact the market in 2018 and beyond. Each risk is classified with a probability of occurrence ratio (POR), and possible consequences are updated as and when they appear.

**Breakdown in US industrial activity:** POR < 5%

Possible consequences:
- Renewed US stock market consolidation
- EUR appreciates strongly
- Yield curve steepening

**Sharp rise in commodity prices, and in particular, energy:** POR < 5%

Possible consequences:
- EUR GDP underperformance
- General risk-off by investors
- Yield curve flattening

**Revival of the Philips curve (core inflation up):** POR < 10%

Possible consequences:
- Term premiums up
- Yield curve steepening
- Debt (government, corporate, and private) sustainability issues

**Re-introduction of a custom tariff/trade war:** POR > 75%

Possible consequences:
- Disruption of industrial activities around the globe
- Higher prices for consumer staples
- Stock market corrections (based on lower EPS expectations)

**Increase in HY credit spread and increase in default rates:** POR < 5%

Possible consequences:
- US stocks down
- Wider credit spreads for HG issues
- Volatility up

**Downturn in Chinese economic activity:** POR < 5%

Possible consequences:
- Emerging market downturn
- Commodity prices down
- Forced liquidation of US Treasury, accompanied by a weak USD

**Unexpected increase in US public deficit, increase in twin deficit:** POR < 5%

Possible consequences:
- Term premiums up
- US downgrade
- Weak USD

**European elections – Outcome of far right/left parliament:** POR < 25%

Possible consequences:
- Term premiums up
- Abrupt end of European economic recovery
- Weak EUR

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## Investment recommendations by type

**1. Equities:**

**Short-term view:** - Neutral - after a strong 1st quarter performance!

**Medium-term view:**
- **Main:** Strongly positive on new technologies that are enabling the 4th economic revolution (robotics, automation, artificial intelligence, and augmented reality). Additionally, we have a strong view on specialty retailers and non-US oil service companies, as shale oil is topping out.
- **EM:** Valuations are particularly attractive at their current level; a major factor which is often ignored is the fact that Asian populations benefit from pro-future thinking governments and a very supportive framework.

**2. Bonds:**

**Short-term view:** - Neutral

**Medium-term view:**
- **IG:** Risk/return characteristics are muted, despite recent improvements. Our preference goes to short-term bonds (3 to 5 years), if any.
- **TB:** Holding US Treasuries is an effective way to stabilize a portfolio during times of greater uncertainty (macro and political).
- **HG**: EM Bonds offer attractive entry points, as the yield pick-up covers for most of the expected short-term vulnerabilities. We also believe that HG opportunities are of better quality in Europe as compared to the US and some emerging markets.

**3. Credit:**

**Short-term view:** - Neutral because of rich valuation

**Medium-term view:** - Strong overweight in corporate via short-dated investment grade bonds; in particular, we are keen on European credit (better credit quality) vs. the US. Any engagement can be taken via iTraxx Main.

**4. Metals:**

**Short-term view:** - Neutral because of a stronger USD

**Medium-term view:** - Neutral to negative: With political and monetary risks expected to dissipate over time, precious metals are expected to lose their status of refuge asset class.

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**4. Commodities:**

**Short-term view:** - Neutral because of a stronger USD

**Medium-term view:** - Should inflation pick up in an unexpected manner, commodities prices would best reflect the adjusted conditions.

**5. Structured solutions:**

**Short-term view:** - **Proxy-Strategies**: In times of uncertainty, exploiting equity market volatility by means of conditional capital guaranteed structures appears to be an attractive opportunity, as compared to both fixed-income and equity markets.

As a result of the market correction in November and December of 2018, a number of proxy strategies have suffered; as a result, capital protection barriers were deactivated. Given this and in order to reestablish the nominal, a proactive view is key and the restructuring of these products is required. Where possible, such action was undertaken with the same names, yet it will require a dual roll-over.

Where the outcome of a structured solution is uncertain (because of the deterioration of the underlying), it is opportune to close-out the deal and implement a strategy of better quality with the aim of regenerating the nominal. The was the case of ISIN: CH41535076.

**Medium-term view:**

- **Secular Trends:** Strong secular trends such as IIoT go far beyond our everyday lives. IIoT has already started reorganizing the way products and services are managed, not only in delivery to end consumers, but also in how they are handled inside an existing supply-chain. Progress in high-performance computing and big data analyses, as well as the availability of new low-energy consumption sensors, has put IIOT at the tipping point, moving beyond where previously, human intelligence was required. Structured solutions around this topic may be done upon request.
- **Market Neutral:** Longer-term investors may consider market neutral strategies. Dispersion Strategies are non-directional investment opportunities aimed at capturing the absolute performance difference of an underlying equity universe.

## Investment recommendations by theme

### 1. US Technology:

**Short-term view:**
- Tech stocks continued their steady outperformance, mainly driven by the sector's relative re-rating. We expect this to continue, given the sector's strong long-term outlook.

**Medium-term view:**
- Near-term cyclical adjustments are frequent for this sector.
- Asia's populations continue to migrate to cities; according to UN forecasts, the cumulative population in major cities will double between 2010 and 2030. To balance costs of rapidly decreasing resources with rapid urbanization and sustainable growth, many regions are currently laying the foundation to become smart cities in the future. This should bode well for cybersecurity services, which is a key component of every smart city.

### 2. Energy/Oil services:

**Short-term view:**
- This sector is highly correlated to headline news and geopolitical events.
- The recent run-down on the short-term economic outlook impacted equity prices of oil-service companies very negatively. Therefore, it may take longer for them to benefit from the sector's willingness to spend.

**Medium-term view:**
- We expect the barrel price to remain range-bound for the next quarters. This provides a positive tailwind to energy companies, and in particular, to oil services companies.
- The sub-sector (oil field services) is taking advantage of the capex backlog.
- On average, the sector maintains excellent spending discipline, which is capping the medium-term outlook.

### 3. Consumer Staples:

**Short-term view:**
- Consumer staples are mostly defensive stocks; it is therefore anticipated that they will hold up well when the market is expected to consolidate.

**Medium-term view:**
- Organic top-line growth is accelerating more than expected, while companies are passing on raw material inflation. Also, the combination of low interest rates and strong balance sheets provides a platform to engage in M&A. In Personal care, M&A remains a powerful trigger, while sales momentum is strong.

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**4. Economy 4.0**

**Short-term view:** - FANG stocks are vulnerable, due to regulatory threats. In general, this offers investors an ideal opportunity to enter the market for a solid growth opportunity.

**Medium-term view:** - Enterprise spending on IT is set to remain solid, while we expect sluggish semiconductor demand to pick up in 2H as inventories are cleared.

Valuations are elevated, but the sector's premium rating is not out of line with historical averages. One of the main risks is a significant rise in US government bond yields, since this would lead to a de-rating because of the above-average sector P/E.

Within the sector, entertainment related companies are an interesting opportunity for investors to explore. Companies belonging to this group are highly non-cyclical and are among the companies that grow the fastest.

The cloud-entertainment industry is experiencing a rapid transition towards a fully digital world. This, we believe, will be profitable situation for the broader industrial companies, which will be able to take over development concepts.

One should expect that this sub-sector will evolve quickly and that average survival time will be much lower for companies with a non-competitive business model.

## Tougher competition from emerging markets

Overview:

- Companies in developing economies are becoming battle hardened as they vie for growth and plug into advanced technologies.
- Wealth is piling up in areas of economic vitality.
- EMA companies are overcoming hurdles to the adoption of advanced automation technologies ranging from robotics to machine learning, and are steadily improving their processes.
- As developing-economy companies create greater value, personal wealth is increasing at an impressive rate as a result, particularly in emerging Asia.

Developing countries are both an exciting opportunity for new growth and a source of surprisingly tough new global competition. MGI recently looked at 71 emerging economies and identified 18 that consistently outperformed global benchmarks by achieving more than 3.5% per capita GDP growth over 50 years, or 5% growth over 20 years. These included the long-term success stories of China and Malaysia, recent high-growth economies such as India and Vietnam, and less-heralded outperformers such as Ethiopia and Uzbekistan.

One of the most striking findings for global executives is the fierce competitive environment for big companies in most (though not all) of the outperforming economies. Rising to the top and staying there appears to be much harder in developing countries than it is in high-income countries—and only the strongest survive.

For example, according to the MGI analysis, fewer than 45% of companies that reached the top quintile with respect to economic-profit generation between 2001 and 2005 were still there a decade later. By contrast, 62% of incumbents in high-income economies stayed in the top quintile for the same decade.

However, for the successful companies that do manage to stay on top, the rewards are substantial: with respect to value creation, the top 10% of large companies in outperforming emerging countries captured 454% of the net economic profits generated by all companies. That is more than four times the proportion in high-income countries, where the top 10% capture only 106% of all net economic profit.

Another indication of the competitive environment in the 18 outperforming countries is their sheer number of large companies: on average, there were over 160 large companies per trillion dollars of GDP in 2016, as compared with only 80 in other emerging economies and 95 in high-income countries. Such large companies help drive a greater share of exports and bring other important benefits by investing in assets, R&D, and job training.

The standout role of large companies does not happen in a vacuum. MGI finds that their impact comes about in part because of a domestic policy environment that stimulates and encourages competition, along with other policies to promote a pro-growth agenda that is marked by rising productivity, income, and demand

### Another factor in the success or failure of emerging markets involves the global phenomenon of automation

Automation has become a global phenomenon, but developing economies need to be wary of obstacles that may prevent them from realizing all of its benefits.

Automation technologies such as software robotics, machine learning, and natural-language processing are offering new ways to increase productivity and reduce costs in manufacturing and service companies alike. However, the race for an automation edge isn't exclusive to companies in mature economies. For example, according to a recent survey on global automation trends, developing markets from Southeast Asia to Latin America are moving just as aggressively to take advantage of automation.

In fact, executives of 1,300 companies worldwide were queried, revealing that emerging-market firms are deploying automation technologies at a rate as high as or higher than companies in North America, Europe, and developed Asia-Pacific.

Emerging-market firms' rationale for gearing up is similar to that of their counterparts in mature economies. Specifically, concern with the effectiveness (for example, speed and quality) of business processes was the primary reason companies were pursuing automation, cited by 28% of executives in mature markets and 32% in developing markets.

Interestingly, it has crystallized that companies in emerging economies expect more workforce disruption than do those in mature economies. For example, larger numbers of developing-market executives say that they expect to face employee resistance to automation. Furthermore, leaders in developing markets assert that their human resources teams lack the ability to address automation-related skills gaps, which is a must-have capability as workplaces become increasingly digitized.

Several factors generate increased momentum for adoption of automation technologies in emerging economies. Many developing-market firms are "born digital," with minimal legacy systems to bridge, such as telecommunications companies bypassing early-stage broadband to adopt advanced high-speed wireless communication. Another potential plus for developing-market companies is that labor costs for implementing automation are lower. Meanwhile, trade frictions have the potential to reduce demand for exports of emerging-market goods and services, so governments are cognizant of the need to automate to remain globally competitive.

Despite differences between mature and developing markets, all players need to think through their management approaches according to priority themes. Invariably, these should include raising the strategic profile of automation at the company and pursuing ongoing investment in automation technologies. Learning to juggle these priorities while also sharpening employee skills and understanding the implications of workplace disruption is an ongoing challenge—but is a management imperative. As a closing note, the main difference between disrupters and incumbents (winners and losers) is that the first focuses on products and how to service prospects to make them become clients, while the second merely focuses on compliance.

**Investment opportunities**

During a recent CEO Asset Management Summit in London, a live poll regarding the outlook for growth revealed that a majority of the 100 or so attendees said emerging Asia (including China but excluding Japan and Australia) would account for more than 25% of global assets under management by 2030, against 11% today. Emerging Asia is already on the rise, accounting for about 37% of net flows over the past five years (more than any other part of the world); and according to industry representatives, this trend is set to accelerate significantly.

Geographic evolution is one of several global trends reshaping an industry that enjoyed record growth in assets under management in 2017, pushing revenue and profits to an all-time high. Other key trends are the new power and sophistication of customers, the embracing of advanced analytics, and the emergence of new "ecosystems" as the combination of analytics, customer information, and data prompt the formation of new business models across traditional business boundaries.

The pressure on revenue margins looks set to continue, with half of the polled executives projecting that these would continue to decline at the same rate as today (less than one basis point), and the other half suggesting they would fall even faster. If the current trend of a broad 5% increase in costs persists, asset growth by 2030 would no longer mitigate other pressures on profitability, and global profit pools would shrink threefold.

The risks for an average regionally focused US or European asset manager with limited exposure to Asia are even more important. By 2030, it may be projected that such a firm would see a 21% drop in its share of global assets, and revenue margins would be down ten basis points. If the firm isn't able to bring its costs down significantly, that would translate into a fall in operating profits of up to 83%.

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**What are our preferences?**

Key takeaways for the second quarter of 2019

**General:**

1. Interest rates are on the rise in developed markets, but close to a plateau
2. US-driven economic cycle to continue (share buybacks are supportive)
3. QE to be reduced to the lowest possible level in G-7 nations
4. Inflation likely to stay below expected levels
5. Possible trade war initiated by the US administration, destroying confidence in the established system
   - Should the US levy 25% tariffs on all imports from China, 2019 EPS expectations for the S&P500 would have to be cut by ~10%. Against this backdrop, it will be difficult for global equities to post positive returns next year; even so, 2020 EPS expectations are very optimistic. Margins should be drained by rising unit labor costs, and share buybacks should be reduced to a marginal level.

**Americas:**

6. No further interest rate increases in 2019; one for 2020
7. Tightening financial conditions and drag on the economy has led the FED to reverse the intended course of action
8. Global economic growth is moderating but not stalling; therefore, a US recession appears unlikely at present.
9. US Equities appear to be expensive; share buybacks generate a kind of self-entertained value appreciation of around 10-12% per annum.
10. In the last week of March, 2019, the US yield curve inverted for the first time since 2007. Usually, recessions and bull-market peaks are preceded by an inverted yield curve. Yet in the past, equity markets continued to rally following this event. On average, the S&P500 made 15% 12 months before the 2y/10y spread hits zero, and 29% from the time that the curve inverted to the peak of the equity market. Nevertheless, this time it might be different for the following reasons: a) it is preceding unprecedented monetary conditions (QE), b) the economic activity is no longer propped up by crutches, as it has been in the past, and c) the yield curve adjustment was long yields are down, while short term yields were stable (the opposite would reflect an increase in inflation, which could be worrisome).

**Asia**:

11. Quality over quantity! This is supported by higher local consumption.
12. China takes a GDP hit because of government policies that focus on consumption and innovation rather than on exports.
13. Chinese monetary supply increases, pointing towards some kind of stimulus.
14. Asian market are resilient vis-à-vis a trade war; with reforms taking shape, financial market de-leveraging, and more constructive growth, the region is expected to surmount the trade war-related set-back.

**Europe:**

15. European consumer sentiment holds up because of domestic fiscal stimuli.
16. European services did not dip in 2018.
17. European manufacturing rebound in the making; expect the first sign of a rebound to come through by the end of the 3rd quarter 2019.
18. Chinese stimuli will positively impact European exporters, mainly Germany and Italy.
19. France’s factory output is impacted negatively by the social movement, “Gilets Jaunes.”
20. The French economy, excepting luxury, is most likely to be squeezed out for a prolonged period of time.
21. ECB started to change communication in view of the first interest rate increase in March/April 2020.

# Sector Analysis

## Basic Materials

The materials sector faces several real or perceived headwinds, including trade policy uncertainty, a stronger US dollar, weaker commodity prices, and a gradual softening of economic indicators in several key regions, including China and the US. Still, we believe that the trend has already peaked and that prime regions for basic materials, such as Brazil, Canada, and Australia should start showing some pick-up.

We favor structural growth stories, given the hesitant demand outlook for several key end-markets, but momentum should stay relatively strong for industrial gases and a few end consumer-focused names, which remain attractive opportunities in our view.

**Investment opportunities:**

Based on strong demand for gas products and an accommodative monetary policy, we expect that this sub-sector will outperform the larger market well into 2019. At present, the companies we like include 1COV, LING, and AKZO.

## Consumer Staples

The sector's defensive merits are reflected in elevated valuations. The sector is the most expensive at MSCI Level, trading even at a premium to IT. As a consequence, the risk of a sector de-rating relative to the wider market is considerable.

We expect earnings-per-share (EPS) growth to accelerate slightly and reach high single digits in 2019. The growth in EPS will be driven by slightly better organic sales growth, as well as margin expansion due to ongoing efficiency programs. Challenges and opportunities will remain the same. In particular, the structural shift to online shopping will continue, and will impact company strategies (e.g., marketing spend). Competition from local brands' and retailers' private label products is also expected to persist. All in all, we expect the competitive environment to remain challenging, but emerging markets should provide attractive growth. We therefore recommend focusing on the following three investment areas:

- European companies with high exposure to emerging markets, which should benefit from raising economic momentum;
- Companies with efficiency-improvement or synergy potential, which offer better earnings growth; and
- Companies which offer attractive dividend yields.

However, the already rich valuation in absolute and relative terms seems to limit further upside potential, and we favor more cyclical sectors. In our view, further rises in interest rates pose a de-rating risk to the steep valuation of the sector, particularly for high dividend yield stocks. In addition, the sector is negatively exposed to euro appreciation.

**Investment opportunities:**

Given the overall competitive outlook for the sector, investors should seek companies with strong balance sheets, low financing costs, and a strong focus on products and services. Because of the high absolute valuation and limited upside potential, high yield dividend stocks are at risk; companies to consider include BARN, CARR, DANO, HEIN, NESN, EL, MO, and PM.

## Key figures for Europe:

**Target values:**

| | |
|---|---|
| Present fair value (DJStoxx600): | 380 |
| E12 months value (DJStoxx600): | 425 |
| Upside potential: | +11.8% |

**Key economic ratios:**

| | |
|---|---|
| P/E 2019 (E): | 13.7 |
| P/E 2020 (E): | 12.5 |
| Div. Yield 2019: | 3.6 |
| Div. Yield 2020: | 3.9 |

**Most likely next short-term move:**

| | |
|---|---|
| DJStoxx600 | flat/down |
| DJStoxx50 | flat/down |
| SMI | flat/down |
| DAX | flat/down |

**Key names to look at:**

**Strong intellectual property:**
- Roche
- Novartis
- Amadeus

**High competitiveness:**
- Siemens
- Daimler
- Gemalto
- Richemont
- Swatch

**Sustainable dividends:**
- ABN-Amro
- Imperial Tobacco
- Altria
- Philip Morris

## Technology

Selling quality hardware was once the industry's top priority. However, as a growing number of components become commoditized, companies are finding that the formula for success has to change. Commoditization, along with intensifying global competition and a shift in technology stack value pools, is compelling industrial equipment and machinery companies to allocate resources toward digital that have previously been solely dedicated to hardware.

In response to the limits of hardware-driven growth, industry leaders shifted their business models more toward services, thereby developing new customer-oriented, revenue-boosting business models. The typical case study is probably IBM, which sold off its hardware unit to a group of Chinese investors. In the meantime, a full range of new services have arrived at the market level, with IIoT likely poised to be the most promising business transformation opportunity that the IT sector has created.

As the enabler for the global market of IIoT-enabled business models in the industrial equipment and machinery space, the IT sector is expected to grow substantially. Linking industrial automation and IIoT platforms is considered to be the industry's new frontier. The monetization potential of IIoT platforms and IIoT platform-enabled applications is massive, but implementation is still in its early stages.

Preparing for and implementing IIoT is not without its challenges; namely, the architectural complexity that makes integrating machinery operations especially difficult. Industry architecture standard ISA-95 addresses the complexity rising out of global production and distributed supply chains, but does not address the myriad of data and security issues brought on by countless connected devices. Creating solutions here will be no small feat, but successfully addressing these challenges will open the door to use cases that facilitate a massive business opportunity:

- *Device-management platforms.* IIoT platforms support the development and deployment of applications that manage a potentially vast number of connected devices. These platforms simplify the complexity by zeroing in on the common technology needs of a diverse set of applications, devices, and uses.
- *Industrial automation and shop-floor communication.* IIoT technology presents an opportunity for substantial IIoT revenue growth and margin expansion in industrial equipment and machinery. Platforms, software, and app development are the elements of IIoT that are expected to grow, while others, such as device cloud connectivity, have likely plateaued. Still others, such as hardware without service enablement, are expected to shrink. Industrial automation and shop-floor communication equipment need to be integrated into the platforms of industrial equipment and machinery manufacturers in order to increase the profit margin of the services portfolio. Machine overall equipment effectiveness (OEE) optimization, predictive maintenance, and cross-vendor shop-floor integration are among its most promising applications.

**Investment opportunities:**

We strongly believe that Artificial Intelligence (AI), Machine Learning (ML), Blockchain, VR/AR, IIoT, and bots will shape the future of the industry.

We therefore remain constructive on software companies that are either "cloud native" or that provide tools to manage the transition to the cloud. Select services companies should benefit from increased consulting demands for cloud and digital strategies. Our present preference goes to MSFT, ADBE, VMV, PANW, DAST, SNPS, CYBR, DATA, HUBS, and NEWR. All of these companies play a key role in the bigger IT picture in terms of leading development, implementing disruption, and participating in the general trend to transform products to services.

**The rapid shift from hardware to software** (left bars: 1998, right 2019):


**How new business opportunities will impact future revenue streams:**

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## Telecommunications

This sector includes mobile phone companies, internet service providers, and cable and satellite companies.

The telecom market's structure is rapidly changing. In the past, this sector enjoyed constant share price appreciation and regular dividend increases. In contrast, today's competition is stiff and consumers benefit from an oversupply; consequently, prices are declining. Significantly, the introduction of 5G comes with a huge cost-load that cannot quickly be recouped. Its near-monopolistic landline control is long gone, and this has fundamentally transformed what was once a defensive sector into a highly cyclical one.

We continue to see deteriorating fundamentals across the sector, due to stiff competition, the expensive roll-out of 5G, and rising capital costs.

**Investment opportunities:**

Large-scale equipment upgrades are a frequently recurring case for the telecom sector. For operators with insufficient subscribers, it will ultimately result in negative cash-flows. Finally, we note that from a purely technical point of view, the telecom sector will experience a reshuffling, from which a new Media sector has emerged.

Given these factors and until more light has sheded on the matter, we prefer to remain on the sidelines; customers seeking active exposure should focus their attention on ATT, Centurylink, Drillisch, and KPN.

## Energy

**Unlocking the future growth of deepwater**

Operators in the Gulf of Mexico (GOM) have recently had success by focusing on incremental tie-backs and near-field opportunities, and there remains un-captured upside there. However, recent challenges in deepwater exploration calls into question the scale of the GOM's growth potential. New trends in technology, development, commercial models, and financing—and industry players' responses to these innovations—will determine whether the GOM will return to its former role as a high-margin, cash-generation contributor for the best operators.

Even with the steep growth in onshore unconventional oil and gas production, deepwater fields are projected to remain an important source of future global oil supply, with the GOM representing a sizable part of the mix. If crude-oil prices average $70 per barrel over the long term, 36 million barrels per day of new crude production from unsanctioned projects will be needed to meet demand in 2030. Much of this (30%, or 9.5 million barrels per day) is expected to come from deepwater fields.

This scenario assumes that market share for the Organization of Petroleum Exporting Countries (OPEC) remains constant and that US shale oil output will plateau by the mid-2020s in legacy plays such as the Bakken and Eagle Ford. At lower breakeven prices, shale plays begin to be exhausted. As that happens, the GOM and, more broadly, deepwater will become more attractive relative to the higher-cost onshore shale resources.

We expect that by 2030, about 20% or 2 million barrels per day of new global deepwater supply will come from the GOM, the largest wedge of new production after Brazil. The GOM's competitiveness on the global cost curve is driven by several factors. An attractive fiscal regime, which has been further improved by recent US corporate tax cuts, could further improve development costs by reducing breakeven costs by another $2 to $3 per barrel. While not certain, additional improvements to the fiscal regime (such as a reduction in the deepwater royalty rate from 18.75% to the equivalent onshore rate of 12.50%) could lead to an additional drop in breakeven costs, valued at an additional approximately $2 per barrel. The GOM also enjoys extensive existing infrastructure that improves economics relative to other emerging growth areas, such as the Brazil subsalt.

## Key figures for USA:

**Target values:**

| | |
|---|---|
| Present fair value S&P 500: | 2834 |
| E12 months value S&P 500: | 2900 |
| Upside potential: | +2.5% |

**Key economic ratios:**

| | |
|---|---|
| P/E 2019 (E): | 17.1 |
| P/E 2020 (E): | 15.3 |
| Div. Yield 2019: | 2.0 |
| Div. Yield 2020: | 2.2 |

**Most likely next short term move:**

| | |
|---|---|
| S&P 500 | down |
| Nasdaq | down |

**Key names to look at:**

**Strong intellectual property**
- VISA
- Mastercard

**Technology:**
- Microsoft
- Micron Technology
- Nvidia
- Apple
- IBM

**Financials:**
- VISA

Despite the positive outlook, it is uncertain from where growth in the basin will come, given exploration challenges and the fact that the majority of recent GOM developments are incremental, near-field developments, rather than the larger Paleogene plays.

Both before and after the 2014 oil price crash, exploration opportunities in the GOM were proving to be challenging, with bottom-tier success rates for exploration wells benchmarked against other basins. One reason for this is that exploration in the GOM deepwater has over time moved to complex reservoirs, such as the Paleogene, where success rates have been particularly dismal (approximately 20% on average, two to three times worse than other deepwater regions). Even when Paleogene exploration has resulted in discoveries with large find sizes, most of these finds have not been developed, given the complexity of the reservoir and the uncertainty of the economics.

Of the approximately 5 billion barrels of oil equivalent of discovered reserves in the GOM that have been brought online since 2005, 70% of the volume has been in the Miocene play, with only 5% coming from the Paleogene. Following the collapse of oil prices in 2014, operators in the GOM prioritized “value over volume.” New reserves that have come online since 2014 have almost exclusively leveraged tie-backs in the Miocene, with shorter cycle developments averaging three years from discovery to production of first oil. Focusing on new subsea tie-back developments has proved successful for many GOM operators, who have been able to leverage existing infrastructure and reduce cycle times. Leading operators, leveraging existing infrastructure, have been able to drive and are investing in deepwater because the economics are attractive enough to compete with current onshore shale prospects.

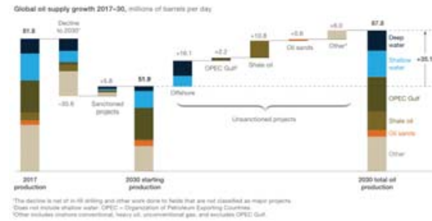
**Investment opportunities:**

We see four trends that should help accelerate exploration and development of the basin, boost operators’ success rates, and increase the amount of production that can compete with onshore shale assets:

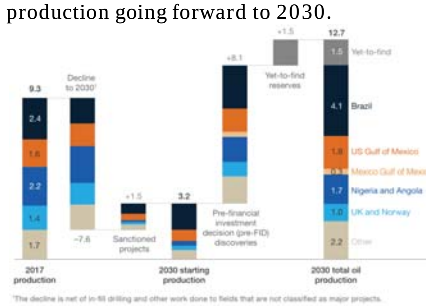
- Game-changing technology (exploration analytics and predictive maintenance analytics);
- New producer-supplier operating models (operator-supplier partnerships to standardize engineering designs, as well as risk-sharing and jointly sharing in the value of an end-to-end project);
- Improvements in the field of capital and operational efficiency (sharing of same support infrastructure); and
- Novel financing approaches (leveraging third-party capital into new projects).

The major names taking advantage of these developments are as follows: SLB, Transocean, SBM Offshore, Petrobras, and Santos (not an exhaustive list).

By 2030, 36 million barrels per day of new production from un-sanctioned projects will be needed to meet demand.




After Brazil, the Gulf of Mexico is projected to supply the largest contribution in deepwater production going forward to 2030.



## Financial Services

**Europe:**
According to Bloomberg, bank earnings estimates for the next two years point to an annual mid-single-digit growth rate. We consider it unlikely that banks will match these expectations, as economic growth is decelerating, revenue streams remain subdued due to the low interest rate environment, and the cost of funding is set to increase due to tightening regulatory requirements, which will force banks to issue more expensive bail-in eligible securities. Conversely, we expect Eurozone bank earnings to remain broadly flattish.

While the recent announcement of a new TLTRO (Targeted Long-Term Refinancing Operations) is certainly positive for the sector (and indirectly for the economy), we are cautiously optimistic, as it was largely priced-in by markets. If this cheap funding facility had not been granted, bank earnings would have suffered significant downgrades, while the economy would have been confronted with lower credit offerings.

The sector is unlikely to outperform until the European Central Bank starts raising interest rates, which we expect from March of 2020 at the earliest. According to our estimates, banks would benefit more than expected at present, i.e. beyond what is currently indicated by management teams. However, any delay in the start of the hiking pattern would be detrimental to the sector’s profitability and performance.

While the low interest rate environment is pressuring revenues, banks’ reported earnings have been sustained by benign credit quality, enabling lower credit-related provisions, a trend we expect to continue. However, investors don’t usually pay for provisioning beats, as they are considered low-quality earnings, particularly at this stage of the economic cycle. Bank valuations look attractive relative to non-financials, but this reflects mediocre profitability. We therefore advise selectivity when investing in the sector.

**Investment opportunities:**

Most of the expected upside for US Banks has been achieved in the last 12 months. However, in Europe, there is still much headroom available, especially for lenders for the continental market. Peripheral operators and banks with strong exposure to LATAM could provide any valid diversification opportunity.

Given that there is isn’t much more profit to wring out of pure financial institutions, we seek exposure beyond the traditional frontiers of the financial sector. Financial service providers such as credit card operators offer an excellent upside opportunity in many ways. Some of them operate worldwide, which makes them even more attractive, as they are less impacted by regional developments. Our key picks: V, MA, PYPL, and ING.

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## Consumer Discretionaries

### US

Coming off of the strongest holiday sales increase in six years, we continue to believe that consumer fundamentals are positive. Unemployment is currently at 3.8%. Wage growth is accelerating and the increase in wages over the past year rose to a 10-year high in February. Interestingly, wage growth is still well below levels seen in other tight labor markets, so accelerated wage growth is likely to continue. Consumer confidence, which rose in February after seeing a drop at the start of the year, still remains strong, and the savings rate is healthy. However, with all of these positive data points, it is difficult to see where an improvement in consumer spending will come from. Higher tax refunds are likely to provide a boost to spending in the first half of the year, but a moderation in growth is likely. That said, even though there is no shortage of headwinds, we do not expect the US to enter a recession in 2019, with a favorable consumer backdrop likely to prevail.

**Retail:** Not all retail is alike; we believe that one key way for brick-and-mortar retailers to compete against online competition is through differentiated retail concepts. For example, outerwear brand Canada Goose has installed see-through freezers in some of their locations, where customers can try on jackets and test their warmth in a 12-degrees below zero dressing room. Or consider mattress retailer Casper, which has created the "Dreamery," where shoppers can come and take a 45-minute nap in a cool, quiet pod with fresh sheets, pajamas, eye masks and—of course—a Casper mattress. These types of experiences simply cannot be duplicated online, and are a key reason why consumers will continue to shop at brick-and mortar retailers even as e-commerce grows at a faster pace.

### Europe

Economic data still looks good, and valuations appear attractive from a bottom-up perspective. Our preference is for companies with good organic growth opportunities, or potential for successful restructuring and attractive valuations. Upcoming quarterly results should provide more clarity, in particular, on investors' concerns regarding a sharper-than-expected slowdown in Chinese consumption, which had an adverse effect on the recent performance of stocks in the sector.

Overall, the macroeconomic backdrop for consumers is favorable, and financial conditions are also supportive of consumer spending. However, political uncertainty, including ongoing trade tensions, could weigh on business and consumer sentiment.

**Luxury:** Luxury companies reported strong 4Q results. China continues to drive the industry's growth trajectory, something we expect to continue in the medium term, but at a slower pace. Innovation is likely to be at the forefront of efforts to improve the pricing mix. Still, fears about waning pricing power and lower number of new store openings are resulting in lower than expected medium-term growth rates. After strong revenue growth of more than 10% last year, we expect growth to "normalize" to high single digits.

**Retail:** We do not expect retail trends to change significantly in 2019. While underlying growth rates in apparel closely match GDP growth, e-commerce channels will keep gaining market share. For example, around 20% of H&M's operating profits are derived from online sales. The further rollout of new physical and online stores will remain a key growth driver for this segment. A potential downturn in Europe and more pressure on sales in emerging markets pose the highest risks for European retailers. Exchange rates will be a key factor in the earnings growth trend next year.

**Investment opportunities:**

Understanding the changing consumer spen
indications—among these, the recent ret
especially millennials have different spendin
Great Recession. Given this, we favor UUA
others. Fixed income investors may also cons
XS1728696615; it is a 18-month product with
Capital guarantee conditions apply for t
downloaded here.

### Key figures for Asia:

**Target values:**

| | |
|---|---|
| Present fair value MXAPJ: | 664 |
| E12 months value MXAPJ: | 730 |
| Upside potential: | +9.8% |

**Key economic ratios:**

| | |
|---|---|
| P/E 2019 (E): | 13.7 |
| P/E 2020 (E): | 12.1 |
| Div. Yield 2019: | 2.7 |
| Div. Yield 2020: | 2.9 |

**Most likely next short term move:**
MXAPJ up

**Key names to look at:**

- Tencent
- Alibaba

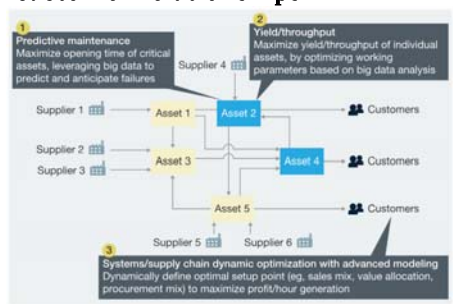
## Industrials

Our preferred stocks reflect companies with a combination of exposure to improving end markets and favorable company specific catalysts, such as restructurings, acquisitions and new products. Within this segment, we opt for companies engaged in e-commerce, energy efficiency, automation and restructuring/M&A.

**US: Industrials stocks have outperformed, but valuations are still below average!** First quarter trends have started out sluggish. While we had already anticipated that the 1Q would have the toughest comparisons of 2019 in terms of growth and costs, the quarter is starting out somewhat weaker than we anticipated. Weaker rail and freight volumes, still declining auto and semiconductor demand, and anecdotal comments from companies point to a first quarter that has been slow out of the gate. Some of the weakness can be attributed to one-time factors like the government shutdown and bad winter weather, but it is becoming more obvious that trade frictions continue to weigh. Weaker trade is taking its toll on the global economy, as is evident in the decline we have seen in global PMI's over the past several month. US Industrial production slowed to a mere 0.1% in February, while manufacturing shrunk for the second straight month.

So far the sluggishness is resulting in only modest cuts in 1Q earnings estimates, but the back-end loaded nature of 2019 earnings has us more concerned. Most companies have cited less of a drag from currency, transportation and raw material costs in the back half of this year. Given the slowing global backdrop, it is more imperative that trade issues are worked out in the near term. Guidance from most companies does not envision a further slowdown in the global economies, and the negative economic momentum could present a risk to earnings estimates later in the year. However, a lot of this near term weakness will be forgotten if we can get trade deal with China soon and investors can focus on a potential economic rebound.

**Advanced analytics maximize on customer relationships**




**Europe:** The European industrials sector continued its good performance so far this year, despite the fact that most companies reported weaker sales growth in the previous quarter. Most end-markets decelerated, negatively impacting organic sales growth of European industrials during the recent earnings season. We expect the sector to bottom out in terms of sales growth in the second half of 2019 before accelerating once again.

After the bounce in the sector's performance following a weak 4Q, we expect the sector to perform in line with the broader market. We believe that while estimates might continue to face shorter-term pressure, as indicated by weak leading indicators in the second half of 2018, recent leading indicators have reached an inflection point. This should lead to stabilization in relative sector performance. From a valuation perspective, the sector is trading at mid-cycle multiples.

Within the sector, we see selected opportunities in the construction sector, which is benefiting from infrastructure investments, but are avoiding names with high exposure to commercial and residential construction due to weaker end-market trends (several European countries have reached their peak). In addition, we still like the commercial aerospace and the railway market, since companies in both end-markets have high visibility due to multi-year order backlogs.

**Investment opportunities:**

Preferred companies are those with a combination of exposure to improving end-markets and favorable company-specific catalysts, such as cost-efficiency programs, restructuring, acquisitions, and new products with high value add. Therefore, primary attention should be given to themes such as e-commerce, energy efficiency, automation, and robotics. Names to look at in the US: BA, CAT, DE, FED, and UT; in Europe: Airbus, Sulzer, Rotork, and Fraport.

## Healthcare

In a late-cycle environment, due to its defensive earnings profile, healthcare acts as a portfolio stabilizer. Relative to the broader market, the sector's earnings momentum has improved over recent quarters, as trade tensions, fading fiscal stimulus and weakening economic indicators have led to downgrades elsewhere. We think aggregate 2019 healthcare earnings forecasts are achievable.

We expect sector fundamentals to continue to improve. Pharma earnings trends are stable, and clinical data is broadly positive. In med-tech, innovation supports organic growth rates and gross margins, enabling companies to offset low single-digit pricing pressure on older products. Companies with more consumer-oriented portfolios risk slowing growth as the cycle matures, but so far, consumer confidence remains supportive.

With the 2020 US presidential election campaign approaching, politics returns as a sentiment overhang. We expect drug pricing to stay in the headlines, but our base case is that no new legislation will emerge, and the impact on net US pharma revenues will be minimal. Many investors are currently relaxed about the topic, which may create volatility if headlines about healthcare policy increase in frequency, as we expect to happen.

The sector's valuation normalized in 2018 and is now close to average levels. We expect earnings trends to drive relative performance in 2019. Thematically, companies that are able to save costs for the system without undermining the quality of care, along with those creating breakthrough innovations, should have the best long-term outlooks.

**Investment opportunities:**

Healthcare companies typically offer consistent earnings growth, high returns on capital, and growing dividends for income-seeking investors. Pharma constitutes the core of our sector recommendations; we like companies where existing research pipelines with clinical tests at an early phase III level can drive meaningful earnings momentum in the foreseeable future. In medtech, we prefer companies with scope for self-help, given expensive valuations. Companies of interest: AstraZeneca, Bayer, Novartis, Novo Nordisk, Merck, Pfizer, Alexion, Celgene, Straumann.

## Utilities

Utilities are described as "defensive" investments, as they are generally characterized by 1) below-average earnings growth as the economy expands, 2) above-average dividend yield, and 3) below-average earnings sensitivity to reductions in economic growth in the broader US economy (i.e., people still need electricity, even during a recession).

**Europe:** Thanks to the structural trend of energy transition and the target to reduce greenhouse gas emissions, utilities plan to increase capital spending, especially in the field of renewables and energy networks, which is a business with low risks and high earnings visibility. With a pickup in M&A, ongoing restructuring, and power prices turning from a sector headwind to a tailwind, the earnings outlook for 2019 and 2020 looks bright. Consensus earnings growth estimates for Eurozone utilities are currently at around 11% and 12% for 2019 and 2020. Growth hasn't been this strong for many years. Earnings growth expectations for UK utilities are in the mid-single digits, slightly lower than Eurozone peers. The very solid earnings outlook should also support future dividends payments. The utility dividend yield of 5.4% is attractive and relatively safe.

We also see some potential hazards. Political risks have increased significantly, especially in the UK and Italy, where the high price of energy is an ongoing political topic. In Spain, the April 2019 elections could increase political uncertainties for utilities. Meanwhile, European utilities are currently trading on a 2019E P/E of 14.8x. This is a 9% premium as compared to the MSCI Europe index, which can be explained by the positive earnings momentum of the sector and the better earnings visibility when compared to other sectors. This premium is at the upper end of the historical trading range.

**USA:** After market-leading performance for 2018, the S&P utilities sector is up 10.5% on a total return basis year-to-date in 2019. This is underperforming the S&P 500 by 2.1%, as shown in Figure 2. Utilities are outperforming the consumer staples and healthcare sectors, but underperforming all other sectors so far in 2019.

We maintain a moderate underweight on US utilities, based primarily on valuation. However, the sector's underperformance has been more muted than we had expected. We believe a combination of investor concerns about an aging bull market and economic expansion, as well as a declining yield of the 10-Year US Treasury bond, have provided more support for utilities despite expensive relative valuation.

"Defensive" Utilities
Utilities are income-oriented equity investments with a significant portion of their total return being delivered in the form of a dividend. This underpins the strong relationship between the dividend yield on utilities and the yield on the 10-Year US Treasury. The 10-Year UST has declined almost 10 basis points (or 0.1%) year-to-date. This partially explains the better-than-expected performance of the utilities sector. However, looking forward, we see the 10-Year UST yield more likely to rise than fall (10-Year UST yield to trend towards 3.00% over the next 12 months). This could provide an additional headwind to performance for the US utilities sector.

**Investment opportunities:**

Record high temperatures were set last year around much of the world. As a consequence, we expect that political measures to reduce climate-damaging emissions will gain headway in many parts of the world. Thanks to falling costs, supportive politics and regulation, we believe that utilities—in particular, wind and solar—will increase capex to speed up the completion of the smart grid. Finally, we note that wind turbine manufacturers are benefiting from stabilizing selling prices, after a period of margin pressure. Our favorite names: Engie, Iberdrola, Nextera Energy Inc., RWE, Siemens Gamesa Renewable Energy, TPI Composites Inc., and Vestas Wind Systems

# Foreign exchange

## Currencies

Our main scenario is one of great moderation. The US economy is losing its exclusive role as the locomotive of the global economy that it held in 2018. Growth expectations have fallen sharply around the globe, without a significant increase in the probability of a recession in Europe or the US. In fact, neither boom nor bust, deflation nor excessive inflation are expected. In such an environment, the path to normalization of ECB policy is even longer, but structurally intact. We therefore feel comfortable maintaining our long-term target of 1.20.

In the case of a more severe global slowdown, monetary policy actions would become more complicated. The Fed has a lot of room to ease, while the ECB will be rather hesitant to invent new easing measures, even when recession and deflation are around the corner. The different starting positions of the Fed and ECB should therefore drive a sharp appreciation of the euro against the dollar if there is a global recession, at least in the first phase, until the ECB is ready to react.

Aware of this circumstance, investors find it difficult to extend their already substantial USD positions when EURUSD slips into the 1.10 to 1.12 range. We would expect a drop below 1.10 only in the case of a strong idiosyncratic slowdown in the euro area and/or a strong exclusive boost of US growth. Either would be a new and surprising trend. Recent data releases suggest that the euro-zone is recovering from ultra-negative surprises, while the US has had more surprises to the downside.

## Energy/Commodities

### Crude oil:

With oil demand rising in China and domestic crude production down to a multi-year low, imports are likely to continue moving upward over the coming years. The build-up of strategic oil reserves is likely another factor supporting imports, with the Chinese government aiming to build more crude storage facilities in the next few years.

We see China's role in the oil market as sponge-like. That is, elevated Chinese imports soak up excess barrels and help to tighten up the market, as inventories in strategic oil reserves are unlikely to be released anytime soon. That said, some market participants are worried that imports will fall, given the country's slower economic growth. They see the Chinese sponge as being saturated, which will limit its ability to soak up excess barrels. We are more optimistic, expecting Chinese imports to remain elevated because of increased demand over fears that US sanctions against Venezuela and Iran will disrupt supply over the coming months—a situation which would make it more challenging to buy oil for refineries.

**Target values in 3 months:**

| | |
|---|---|
| EUR/USD: | 1.1000 - 1.1500 |
| GBP/USD: | 1.3000 - 1.3500 |
| USD/CHF: | 0.9750 - 1.00 |

**Target values in 12 months:**

| | |
|---|---|
| EUR/USD: | 1.20 - 1.25 |
| GBP/USD: | 1.35 - 1.40 |
| USD/CHF: | 1.00 - 1.05 |

**Purchase power parities:**

| | |
|---|---|
| EUR/USD: | 1.29 |
| GBP/USD: | 1.56 |
| USD/CHF: | 0.94 |
| EUR/CHF: | 1.20 |

**Most likely next move:**

| | |
|---|---|
| EUR/USD | down |
| GBP/USD | down |
| USD/CHF | down |

**Target values in 3 months:**

| | |
|---|---|
| Oil: | $55 - $75 |
| Gold: | $1,250 |

**Target values in 12 months:**

| | |
|---|---|
| Oil: | $85 - $100 |
| Gold: | $1,350 |

**Upside potentials:**

| | |
|---|---|
| S&P GSCI | down |
| Oil | down |
| Gold | down |

**Next most likely move:**

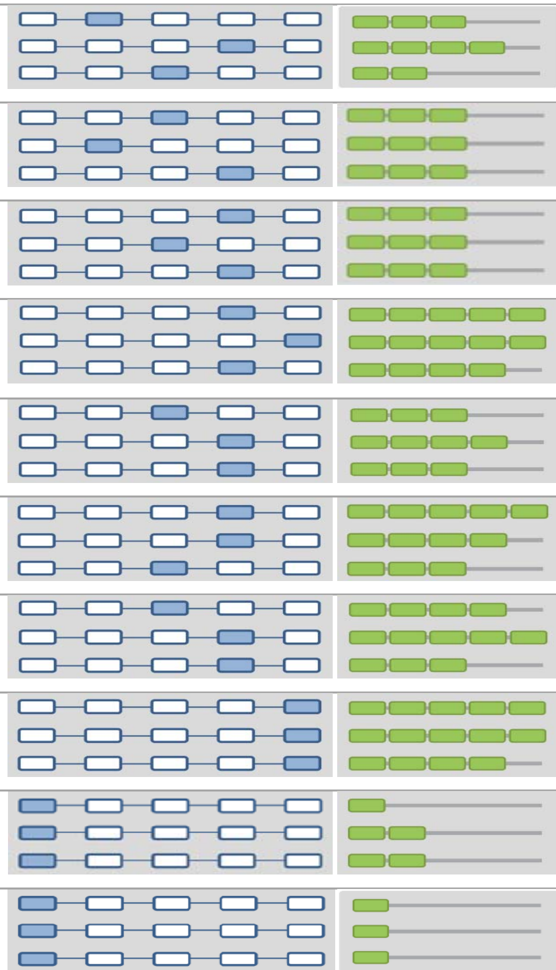
| | |
|---|---|
| S&P GSCI | flat |
| Oil | flat |
| Gold | flat |

**Commodity related stocks:**

# Asset Allocation Preferences – April, 2019

| Sector | Region | Investment case |
|---|---|---|
| Basic Materials | Americas<br>Europe<br>EM | The US administration-initiated trade war is not just a bluff, and its ramifications may extend well beyond general expectations. On the other hand, for the Chinese government to give in would require a complete change to the system. With China being the boiler room for the world's economy, the basic materials sector is clearly exposed to the new game plan. |
| Consumer Staples | Americas<br>Europe<br>EM | Organic top-line growth is accelerating more than expected, while companies are passing on raw material inflation. Also, the combination of low interest rates and strong balance sheets provides a platform to engage in M&A. In Personal care, M&A remains a powerful trigger, while sales momentum is strong. |
| Consumer Disc. | Americas<br>Europe<br>EM | The two main subsectors of automobiles and luxury goods show sharply divergent trends. The car sector's net profits are suffering from rising costs and slowing sales growth, while the luxury goods sector has benefitted from double-digit organic growth and high profit margins. But the benign environment for luxury goods is as good as it gets, in our view, and elevated valuations leave ample scope for a sector rerating. |
| Energy | Americas<br>Europe<br>EM | Key takeaways from this sector: a) Operators now prioritize disciplined capital spending, with the 2019 budget being lower than in 2018; b) For a number of operators, growth was deemphasized in favor of returns and cash flow generation; and c) Free cash flow yield (cash flow from operations less capex) is a metric that investors are looking to in order to gauge the investment merits of the operators within the energy sector, as well as versus other sectors within the broader market. |
| Healthcare | Americas<br>Europe<br>EM | Healthcare companies typically offer consistent earnings growth, high returns on capital, and growing dividends for income-seeking investors. We prefer companies with improving growth prospects, as well as self-help stories in med-tech. We have a large-cap bias, given the late stage of the cycle. On the biotechnology side, some late phase 3 projects were cancelled; we are expecting some more mean reversion to come. |
| Financial Services | Americas<br>Europe<br>EM | Improving economic growth across the globe, driven largely by still-healthy US consumers, is set to provide a good backdrop for financial services stocks overall. The main beneficiaries can be found within the segment of diversified financials, as they benefit from the secular shift (online payments framework, which enables capital optimization potential). European operators suffer from over-regulation. |
| Industrials | Americas<br>Europe<br>EM | In the 2018 downturn, industrial sector related stocks suffered the most. Yet, consumer sentiment is strong across the globe, and surprisingly, consumer sentiment held up very well in Europe, where consumers react very rapidly to changing conditions. With China entering into a new stimulus program, Germany, Italy, and the United States of America are expected to rebound the most. |
| IT | Americas<br>Europe<br>EM | This sector's companies recently experienced significant volatility; although the sector's key areas (e.g., IIOT, connectivity, etc.) remain fully intact, we nevertheless expect volatility to remain high. The sector is currently trading with a Fwd PE of close to 18. This is in line with average premiums over the past two decades. Software and service companies are our preferred play, as they take advantage of recurring revenues. |
| Telecom. | Americas<br>Europe<br>EM | Telecommunication is a capital-intensive business; therefore, the most recent underperformance can be attributed to rising interest rates and still stiff competition for new customers. Given that a new infrastructure deployment is in the works (upgrade to 5G), we would not expect the sector to suddenly start outperforming in a market-neutral environment. |
| Utilities | Americas<br>Europe<br>EM | Near-term attractiveness of the sector has changed. After two years of constant improvement of fundamentals, power producers benefited from rising wholesale power prices, a trend that is now expected to continue. |

Fundamental / Risk/Reward



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**Sources:**
Analysis and comments: Bloomberg, Reuters, Natixis, UBS, BNP-Parisbas
Data and graphical items: Bloomberg, Reuters

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