IRISOS
Knowledge is power.

Q 04 / 2018

Quarterly Investment Review and Outlook

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Knowledge is power.

Quarterly Report – Q04/2018

At a glance

Review – 4th Quarter of 2018

1. EPS Expansion

We believe that the sell-off experienced during the 4th quarter 2018 is overdone. The S&P 500 is on track to deliver earnings of 23% per share growth in 2018, while US stocks were down 5% at one point (17.12.2018). Thus, equity valuations have fallen to levels not seen since early 2016.

Trailing EPS Growth Expectations

	% growth	2020	% growth	2019	% growth	2018
11/9/2018	10%	$194.88	9%	$177.25	23%	$162.65
9/28/2018	10%	$195.41	10%	$178.43	23%	$161.91
6/29/2018	9%	$193.36	10%	$176.91	22%	$161.14
3/30/2018		n/a	10%	$173.97	20%	$157.99
12/29/2017		n/a	10%	$162.22	20%	$147.23

2. List of ongoing concerns

A normalization of markets will likely require some positive input on a number of issues, such as Brexit, US/China trade tensions, and last but not least, the dissipation of France's "Gilet jaunes" social unrest.

Our base case scenario considers that some of these issues will persist for a prolonged period of time. Even so, the combination of several factors—stabilizing growth trends, signs of progress in trade talks with China, and evidence from the Federal Reserve that it will be measured in its approach to normalize interest rates—will help investors to find confidence.

3. Valuation

- **Equity valuations:**
  The correction experienced during the 4th quarter 2018 did not follow the traditional risk-off playbook. Defensive sectors such as utilities, consumer staples, and healthcare all trailed the broader market. In contrast, the top-performing sectors and the more economically sensitive financials, industrials, materials, and energy sectors gave back much of the gains. As occurred during previous market corrections, high beta stocks tended to react in a more sensible manner; technology and internet retailers were the sectors of greatest concern.

  Fundamentals:

  a) EPS growth in the US is reaching a plateau. Previously, EPS growth was fueled by share buybacks and strong repatriation flows.
  b) EU equities have the best risk/reward opportunity. Still, Brexit concerns are a major concern affecting the prospect of this upside potential materializing. A hard Brexit will decrease GDP by around 2%, while France's social measures—announced in the run-up to global protests—will reduce GDP by around 0.75%, which brings country's GDP to 0% when neutralizing the inter-government part.
  c) The risk premium for EM and Peripheral EU market continues to increase, leading to a significant compression of earnings multiples.

4. Central Bank actions

- **ECB:** ECB's guidance as to the QE and interest rates remains unchanged.
- **FED:** The FED's path to interest rate increases will depend very much on the recovery of the stock market. Given the stock market consolidation, the interest rate tightening might have come to an end as higher capital costs would fuel a higher market sensibility.

  A weak rate of inflation makes it more difficult for central banks to raise interest rates according to the planned trajectory. Up until now, the decision to hike rates was based on good unemployment figures and relatively solid economic growth. However, data from economic and rate-sensitive sectors such as housing has weakened.

Key concerns

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

Breakdown in US industrial activity: POR < 15%

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

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

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)

➢ The trade war between the US and China is likely to persist for a prolonged period of time. We do believe that the climax of stress has passed, but that the ideological divide will remain in place. The Chinese push for an end to tariffs will not be entertained until US companies gain more flexibility with regards to access to the Chinese market, and until reciprocal agreements are signed. As policies become more and more populist, current barriers are expected to remain in place. However, the impact on the global GDP should remain minimal.

Investment recommendations by type

1. Equities:

Short-term view: - Neutral

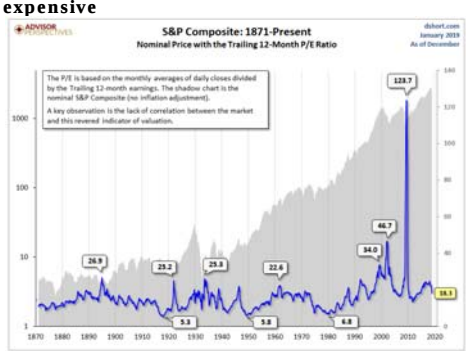
Medium-term view: - **Main:** We have a positive stand on equities in our global asset allocation. Based on still-solid growth expectations, valuations are now highly reasonable. Compared to 12 months ago, sentiment is now much less bullish, as average markets PEs have fallen below long-term averages.

On the negative side, central banks will be exiting QE and therefore, global economic stimuli will disappear over time.

- **EM:** Clearly, Emerging Markets should benefit from a better valuation rating. Considering a medium-term view, 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.

EM markets could surprise to the positive in 2019, as they have shown a constant underperformance over the past years.

Valuations: The S&P500 is no longer that expensive



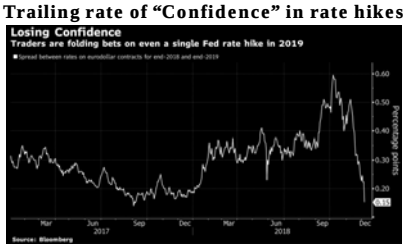
2. Bonds:

Short-term view: - Negative

Medium-term view: - **HG:** Risk/return characteristics are not attractive, despite recent improvements.

- **TB:** Holding US Treasuries is an effective way to stabilize a portfolio during times of greater uncertainty (macro and political).
- **HG**: EM Bonds offer an attractive entry point, as the yield pick-up covers for most of the expected short-term vulnerabilities. In particular, we like bonds related to the "energy deal," i.e., debtors with exposure to "Oil Related Services and Equipment"; oncoming cash-flow generation will drive future credit quality and valuation.

Trailing rate of "Confidence" in rate hikes



3. Credit:

Short-term view: - Neutral because of rich valuation

Medium-term view: - Strong overweight in corporate via short-dated investment grade bonds

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.

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.

Medium-term view: The Global Energy Income Strategy gives investors exposure to offshore oil and gas equipment and service providers. The asset allocation of the certificate is split into two segments. The main part of the portfolio (80%) is invested in fixed income instruments issued by oil and gas drillers, as well as equipment providers. The remaining 20% is invested in a well-diversified range of oil field service companies as optionality, in order to increase the overall return at due date.

We believe that over the next two years, the combined effects of consumption growth and stagnating output capacities—occurring as a result of a lack of exploration efforts from 2014-2016—will drive barrel prices. Because of below average production prices, offshore oil exploration and production have become very profitable in some areas. The investment selection is focused on these particular fields.

More importantly, to avoid idle time, there will an increased demand for quality service activities. Therefore, geared-up oil service companies will be able to demand higher mandate prices; in consequence, as free cash flows are generated, their financial stability should improve.

In line with barrel price development, the industry's momentum is expected to be very positive in the coming two years, and industry valuation multiples are expected to revert to historic levels.

- **Market Neutral:** Longer-term investors might 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:

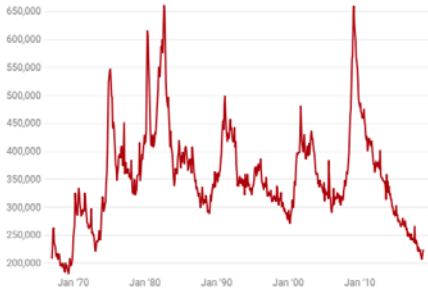
Short-term view:

- EPS revisions continue to be strong, but products and consumer behavior are of a strong cyclical nature. Because of this and due to growth concerns, investors tend to unload these stocks first.

Medium-term view:

- Most developed stock markets are close to the upper end of their 10Y range.
- On average, the US looks expensive; however, pockets of good value and growth do continue to exist (e.g., IT, Oil Related Service and Equipment).
- Japan and the EM are among the cheapest markets vs. their 10Y metrics.

Lowest initial unemployment claims since 1970s



Source: U.S. Employment and Training Administration, retrieved from FRED • Get the data

2. Energy/Oil services:

Short-term view:

- This sector is highly correlated to headline news and geopolitical events.

Medium-term view:

- We expect the barrel price to remain range-bound for the next quarters [USD 45 to USD 65 pb]. This provides a positive tailwind to energy companies and in particular, to oil services companies.
- The sub-sector (oil field services) is taking advantage from capex backlog, so FCF should be excellent for the next three (3) years.

3. Social Media

Short-term view:

- After years of unprecedented growth and optimism, social network companies are putting on the brakes.

Medium-term view:

- A number of initiatives such as time-counting features may slow movement down (even growth); this might be the price consumers have to pay to stay in the market longer term. We expect to see more speed bumps in 2019 as social network companies show the desired effects of keeping users happy.

4. Economy 4.0

Short-term view:

- FANG stocks are vulnerable due to regulatory threats.

Medium-term view:

- Investing in robotics and automation is participating in a long-term secular growth trend. However, product life cycles are short, and going forward, will become even shorter. We believe that these investment opportunities are authentic and without hype, and that they provide real upside potential for investors. IIOT translates into real and very immediate applications that improve industrial processes of any kind into higher productivity and better product quality, in addition to empowering end consumers.

2019 - The world in numbers

A) By topic:

World GDP and trade:
The trade war between America and China is impacting world's GDP figures. Beyond that, the world economy will mirror conditions in America and China. Their respective economies are mostly very healthy at least for the first six (6) months; however, there is vulnerability for that overall positive scenario. If this vulnerability proves true, it should curb growth in the 2nd half of 2019.

Chinese consumers might have their spirits dimmed by tighter monetary policy and a crackdown on the shadow financing system. The FED is expected to continue to hike rates, while BOJ is expected to start any time in the near future. Finally, the US initiated trade protectionist policies will prompt countries to new trading patterns, but international trade is not to go.

Federal-funds rates:
Banking rules of Basel 3 take effect as of 01.01.2019. This, coupled with tightening monetary policies (as central banks unwind QE) could gyrate stock market valuations further.

Global Economic Growth:
Protectionism hurts all industries world-wide–there is no winner. Expected global growth is set be 4% below the long-term growth average.

Oil Prices
OPEC and Russia open up oil exports, thereby jeopardizing US onshore shale oil production. US shale oil producers have an average output price of USD 55 to 60 pb, while elsewhere, average production prices are as low as USD 30 pb.

Infrastructure
World-wide infrastructure investment opportunities amount to about USD 20 trn. Half of this occurs in Asia.

e-Commerce
Consumers are in spending mode, but traditional brick-and-mortar players continue to crumble. E-Commerce spending is up by 21%, while retailers experience only a weak 3% organic sales growth.

5G
Web access is becoming common around the entire globe. The expansive roll-out of 5G begins, upon which expenditures related to IT and communication climb by 5%.

Travelling
Worldwide, there will 1.5 bn travelers in 2019, thereby generating some USD 1.5 trn in revenues. While France is one of the top destinations per square metre, China provides the largest source of travelers.

Green energy
The Dieselgate scandal spurred on the passage of new regulations which make the use of electric cars more attractive. However, the production of green energy is not sufficient to cover the increased demand. Therefore, fossil energies will remain indispensable for the years to come.

Healthcare spending
For the first time in history, healthcare spending per person in EM will increase more than in DM.

2020 - The world in numbers

B) By business activities

Automobiles

Trade tariffs on metals, components, and vehicles will continue to trouble carmakers in 2019. The end-effect is that car companies will need to rethink alliances, supply routes, and productions plans. Asia will make and consume half of all vehicles, as production moves closer to consumers to avoid tariffs. Carmakers are pushing for self-driving technologies that reach the point where drivers become passengers. However, while the technology is available, consumers have not yet embraced self-driving cars. Nevertheless, 2019 may be the year where testing of autonomous trucks for the delivery of goods begins.

Defense and aerospace

Forecasts for aircraft manufactures are brilliant; deliveries of large aircrafts are to rise by 8% in 2019—only the IT sector can do better in terms of planned deliveries. Airbus is pushing out about 63 new A320 jets every a month, while Boeing does 57 narrow-frame 737 planes a month. After years of spending cuts, defense budgets are on the rise in Europe and in the States. Key focus is given to agileweapons. New market entrants use robotics and AI to help produce more cheaply than traditional arms-makers. The spending spree on agile defense systems will favor disruptors.

Energy

The future path of the barrel price could be bumpy. Saudi Arabia is best positioned to impact the price in either direction. Provided prices stay above USD 60, US shale oil production will reach new records. At the same time, a prolonged period of oil prices below USD 50 will drive most US onshore drillers out of business. Natural gas is an increasingly attractive asset. Emerging markets crave LNG in a sustainable manner. Europe will benefit more stable delivery routes as Nord-Stream 2 is expected to be finalized in 2019. Green energy is another hot topic for 2019; wind generated power will overtake hydropower in the year ahead.

Entertainment

According to PwC, media and entertainment related spending will reach USD 2 trn in 2019. Internet video will surpass the performance of paid TV. With a value of USD 24 bn, the Americas are the largest video market on the globe. In 2019, Netflix is facing some competition for the first time, as Disney will launch its own streaming service. Video gaming is also on the rise, with a total market volume of about USD 89 bn (according to Statista). Watch out for iQiyi, the Chinese online-streaming service, a company that is expected to invest massively in original content. Local and international expansion is planned at the same time.

Financial Services

The FED is expected to raise interest rates, pending economic conditions. In fact, it could raise interest rates up to three times in 2019. The blue sky scenario says that total banking assets will rise by up to 5%, to about USD 150 trn. Higher interest rates are offering an opportune tailwind for US Banks; Asian banks will eat into some of these benefits, while European Banks are cash-strapped. In the insurance sector, premium growth is expected to be higher than GDP-growth. FinTech: the world's biggest FinTech company (Alipay) is in China and has about 870 million users. In 2018, Alipay raised USD 14 bn to cover for an expansion into the US and Indian markets.

Food and farming

On the back of bumper harvests across the globe, food prices are expected to rise by just 0.5% in 2019! More and more, AI helps farmers manage unpredictable weather conditions. At the same time, the quality of harvests is improving. Given this, the difference between organically and traditionally grown food is shrinking. Still, fully organic food providers are expanding well above average.

Health care

In 2019, global health care spending is set to increase by USD 63 to USD 1,553 per person. Global health care companies will reach sales volumes in excess of USD 1.3 trn. While the hunt for cheap treatment is the focus of most individuals, the best chance at reducing

health care costs is prevention and a focus on improving lifestyles globally. Rising trade barriers and Brexit could trigger a worldwide shortage of key drugs. The future of the sector will no longer be in relation to any kind of molecules, but rather in the use of robotics, AI, nano-technologies, stem cells, and gene therapies. R&D is expected to rise to USD 177 bn, with the current focus on treatments using CRISPR techniques (altering the human genome). At present, areas of application are limited to blood disorders and muscular dystrophy. Going into 2020, monumental progress is expected.

Infrastructure
China is undertaking a massive spending spree to connect its "boiler-room" to consumers in the rest of Asia, India, and Europe. Spending on the Belt Road initiative is amounting to USD 8 trn, and will include 68 countries. Elsewhere, major projects like London's east-west link (10% capacity increase), which will link the suburbs to the city center, will go live. Meanwhile, there is not much happening in the US, despite the announced USD 1.5 trn in infrastructure spending–most likely an empty election promise. In the Middle East, the UAE is undertaking every effort needed to power-up World Expo 2020, and its neighbor Saudi Arabia will seek up to USD 7.5 bn for 14 infrastructure projects.

IT
The hype around AI will continue in 2019 and will claim a trivial share of IT-related spending. Industry-wide revenues are expected to rise to USD 700 bn, with global spending up by 5%. The fastest acceleration will be observed in the deployment of SAAS business apps, which will generate about 1/7 of the industry's revenues. Hardware providers will remain in the depressed state,, with revenues to grow only marginally (3%); the major driver of that growth is the deployment of Windows 10, which will require newer hardware to make it run well. As cloud services become more and more relevant, prospects for hardware firms will dim.

Raw Material
Raw material prices were a roller-coaster in 2018 as a result of the tariff war, and no change should be expected in 2019. US companies are expected to pay higher input prices from 2019 onward, while elsewhere, input prices are expected to decrease (on the back of an oversupply).

Real Estate
A very mixed take around the globe: On the back of a housing shortage, US home prices are expected to rise by 3.5% in 2019, whereas the opposite will be true in Britain. In continental Europe, a still loose monetary policy is opportune for property investments. However, the market is not immune against disruption. On one hand, VR will proliferate amongst real estate agents, while on the other, AI will help improve the energy efficiency of existing and new buildings.

Retailing
Worldwide retail sales will increase by 3%, while e-commerce related sales will increase by 21%. This game changer is particularly life-threatening for US malls; there are about 6m^2 of sales surface per person in the US, whereas elsewhere, it is only about 0.5m^2.

Emerging market retailing will rise by 5%, while pent-up demand in Russia should lead a 4% sales growth. Latin America will lack any progress, and this on the back of weak commodity output prices.

Telecom
Consumers are voracious for free services such as WeChat and WhatsApp. With the roll-out of 5G, this trend is not expected to change anytime soon, thereby driving fixed-line providers into the doldrums. New smartphones should allow downloads to complete within seconds and make AR and holographic display the new rule.

Travel and tourism
Prices for air-travel are expected to increase by 3% in 2019, while the median hotel room will cost 5% less. Competition for travelers is increasing; the total travel market amounts to about USD 1.5 trn, with about 1/3 going to European providers. Some long-term trends are in the making, such as Dubai's move to become the major hub for East-Africa, and Indonesia's plans for 10 new Bali-like regions and projection of 20 million tourists in 2019. The environmental impact of tourism is a long-term worry—8% of global greenhouse-gas emissions are due to leisure activities.

What are our preferences?

Key takeaways for the 2019

General:

1. Interest rates on the rise in developed markets
2. US-driven economic cycle to continue well into 2019
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

   The increase of trade tariffs on all imports from China resulted in the slashing of 2019 EPS expectations for the S&P 500 by ~10%, partly causing the equity sell-off. In the event there is no resolution on trade, 2020 EPS expectations will need adjustment as well; hence, another wave of equity sell-off could roll in.

   It will be difficult for global companies to post rising returns next year because of higher unit labor costs and higher input prices. Furthermore, only a few companies have sufficient leeway for share buybacks; therefore, this should be reduced to a marginal level.

Americas:

6. Expect two (2) interest rate increase in 2019, three (3) in the event that a constructive outcome on the trade war with China is reached.
7. A further stock market setback could be a drag to consumer confidence and on the economy, leading the FED to reverse the intended course of action.
8. US Equities appear to be at fair level now; in the past, share buybacks generated a kind of self-entertained value appreciation of around 10-12% per annum; however, this is now reduced to a marginal 3-5%. For 2019, we expect that companies will reduce share buyback in general and concentrate more on organic growth!
9. The energy sector appears to be under-invested for the wrong reasons. FANG stocks have captured most investors' attention; yet based on FCF, they are truly overpriced and some downside pressure should be expected. On the other hand, oil field service companies do generate substantial FCF and are priced at the same level as two years ago when they didn't generate any FCF!

Asia:

10. Quality over quantity! Weaker local consumption should add some short-term volatility.
11. A tepid credit market will result in a weaker housing market and consequently, in lower GDP growth.
12. In the past, we expected Asian market of the resilient in the face of a trade war; however, the governments underestimated the context and virulence of the US administration. Since there is little change to be expected by the Chinese government on IP preservation (but probably some change in current account surplus), new trade routes are the most likely outcome of the current conflict.
13. An ageing population with changing consumer patterns will cause some concerns for SME's profitability.

Europe:

14. The social unrest in France, which occurred on the back of the government's decision to change the pricing policy on diesel oil, is threatening European recovery. We consider scenarios where these events could result in broad-based questioning of government approval ratios across Europe.
15. Concerns regarding the Italian budget are still unresolved: GDP/Debt is at a worrying 130%, and no clear steps have been taken to address the issue.
16. Late cyclicals are expected to recover most in the current economic cycle.
17. Consumer Staples are the most defensive opportunities; while they might suffer from rising interest rates, their downside risk is limited.
18. A high M&A is expected in the Food and Personal Care sector; organic sales are solid, while at the same time high input prices are most overturned to consumers. Momentum in these sub-sectors is strong.

Sector Analysis

Basic Materials

Global mining companies are trading at attractive valuations, and this on the background of trade sanctions. Lately, companies started downgrading their earnings expectations; we believe that this trend will continue well into 2019.

Based on the base case scenario, which considers still favorable economic conditions throughout 2019, the materials sector should continue to benefit from cyclical activity. However, a stronger USD and weaker Chinese GDP could bring the positive trend in this sector to an abrupt end.

Investment opportunities:

Based on the 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 EMN, DWP, and APD

Consumer Staples

While the broad-based consumer staples sector performed well in 2018, its performance varied greatly from sub-sector to sub-sector. We are cautious regarding brewers; a slowing consumption in emerging markets could jeopardize the premium rating they have had for the past 15 years.

2019: Based on improved organic growth and better margin management, we expect that companies will report an EPS expansion. Overall, the challenging environment will remain, particularly in the structural shift to online apps.

We are strongly positive on companies that truly engage in niche online activities. This structural shift will positively impact growth opportunities and ultimately, will generate FCF and EPS growth. Particular attention should be given to the following sectors:

- Companies with high exposure to emerging markets, which should benefit from good economic momentum;
- Companies with efficiency improvement, online strategies, and synergy potential, which offer better earnings growth; and
- Tobacco companies, which offer attractive dividend yields owing to their highly cash-generative business models.

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 AD, ABI, BAT, NESN, EL, MO, and PM.

Key figures for Europe:

Target values:

Present fair value (DJStoxx600):	337
E12 months value (DJStoxx600):	360
Upside potential:	+6.8%

Key economic ratios:

P/E 2019 (E):	13.2
P/E 2020 (E):	12.0
Div. Yield 2019:	3.7
Div. Yield 2020:	4.0

Most likely next short-term move:

DJStoxx600	flat/up
DJStoxx50	flat/up
SMI	flat/up
DAX	flat/up

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

Throughout the 4th quarter of 2018, technology stocks showed very volatile performance, due to rising concerns about a declining demand for smartphones and other consumer electronics. As a result, valuations have reached a more reasonable level of 16x forward P/E. However, we believe the relative premium of 15% against global markets is becoming attractive enough to turn bullish on the sector. One should start considering selective opportunities related to AI, VR, MR, robotics and automation from now on.

While valuations may provide some support next year, it is worth highlighting that earnings growth should decelerate next year. We expect the global tech sector's earnings growth to decelerate from 16% in 2018 to around 10%, given weak consumer IT and emerging market demand. As a result, cash distribution becomes an important driver, as we continue to expect technology companies to buy back shares and increase their dividend payouts. Key risks to the sector on the negative side include weaker-than-expected growth in emerging markets, driven by recent currency headwinds and increased uncertainty around trade tensions. On the positive side, M&A and higher-than-expected cash distribution could act as catalysts.

Against this backdrop, we see that there is a strong outlook for some sub-IT sectors next year. Fields of interest include the following: robotics and automation, SaaS providers, as well as the lead-up to the installation of 5G.

There are some headwinds for the more cyclical semiconductor and hardware companies, due to ongoing destocking and concerns about demand in emerging markets. Software and services companies are relatively better positioned, given their exposure to enterprise IT spending, where we expect demand to remain stable. The ongoing shift to digital technologies like cloud, mobile and big data analytics should continue to drive solid growth prospects. While internet companies should benefit from secular trends, challenges remain on the regulatory front and with regard to costs, as we continue to see rising investment.

Investment opportunities:

Software-related IT spending is expected to remain robust. Industry analyst Gartner expects IT spending (data center + enterprise software + devices + IT services) to grow 7.5% this year, versus 5.5% last year. Software is expected to see the strongest growth, at nearly 9%.

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 ASML, IBM, Nvidia, Salesforce, Tencent, and Visa.

Telecommunications

This industry sector is undergoing some deep structural changes. On one hand, there is the roll-out of an expensive 5G network, and on the other, there are consumers who tend to replace their smartphones less frequently than before. In the most recent move, Samsung and Apple have started targeting markets like India, Indonesia, Brazil, thereby putting pressure on telecom companies to provide decent service so that apps can be serviced. With these new conditions, everyone has to contend with lower profits.

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. Pure land-line providers will probably be pushed out of the market by 2023.

Given these factors and until more light is shed 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

In Q3 of 2018, return on average capital employed (RoACE) among European integrated oil and gas companies stood at close to 10%, with an average Brent price of USD 76. The last time they were this profitable was in Q3 of 2013, when the quarterly average barrel stood at USD 110. This shows that similar results can be achieved despite a 30% lower product price, thanks to cost savings, cost deflation and an increased focus on profitability.

For 2019, this cost discipline should continue, with plenty of scope to adjust share buy-backs based on the oil price. USD 50 is good enough to cover companies' (generous) dividends and investment plans. Any price above that means additional share buy-backs. If our barrel price forecasts of USD 60 for mid-2019 and USD 75 for end-2020 are correct, companies will have more than enough cash to cover their buy-backs plans and more.

Given the aforementioned upside and because they would benefit from a dividend yield cushion if oil were to remain unchanged or go lower, integrated companies continue to be our favorites. We particularly like Galp, Royal Dutch Shell, and Total. The latter is delivering reliable improvements, while Shell still offers some turnaround benefits. Galp is smaller, but its oil volumes are growing strongly.

Furthermore, we like oil field services companies that are supported by a general willingness to spend. But as discipline holds, this is not a broad or strong trend. Still, spending is no longer falling, and more production areas are receiving support. In this particular context we like Ensco, Petrobras, McDermott, and Gaslog, as well as Furgo and Ship Finance.

Oil prices going forward

A barrel price at around $70/bl would represent 3.0% of the 2019 Global GDP, 12% under the average of 1970, which was 3.4%! A return to the mean of 3.4% of the GDP implies an oil price of around $80/bl.

The rate of development is heavily dependent on the available cash flows by producing companies. The available CF tend to be recycled immediately into new wells and the underlying cost of service to drill and fracture the wells. Naturally, in a $60 world, most of the cash flows are required for reinvestment and debt servicing. However, in a $80 world and with efficiency improvements, there is enough profit to see sustained growth and a debt-to-equity ratio of improvement for concerned companies.

Investment opportunities:

Rising demand and limited supply means that oil prices are likely to continue to increase. Demand from EM, as shown above, is increasing in tandem with an improving standard of living.

Periods of under-investment in exploration will ultimately reduce output capacities; in other words, the price of oil will remain high. This, in turn, will benefit oil field service companies that can generate better FCF.

With such positive industry momentum, we expect strong stock performance for the following: SLB, Transocean, SBM Offshore, Petrobras, and Santos (not an exhaustive list).

Key figures for USA:

Target values:

Present fair value S&P 500:	2506
E12 months value S&P 500:	2700
Upside potential:	+7.7%

Key economic ratios:

P/E 2019 (E):	16.1
P/E 2020 (E):	14.9
Div. Yield 2019:	2.1
Div. Yield 2020:	2.2

Most likely next short term move:

S&P 500	flat/up
Nasdaq	flat/up

Key names to look at:

Strong intellectual property
- VISA
- Mastercard

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

Financials:
- VISA

Financial Services

Despite solid reported earnings, the Eurozone banking sector has lagged the market this year, mainly because expectations for an interest rate hike have faded over recent months. We see no short-term trigger for sector outperformance as, in our view, sustained higher earnings will only come with interest rates hikes. Any delay in the start of the hiking pattern would be detrimental for the sector's profitability and therefore, performance.

The sector's profitability is highly sensitive to interest rates. For instance, for some institutions , a 1.0% increase of short-term interest rates can generate up to a 35% increase in achievable profitability.

Banking is an important sector for addressing social and governance issues because it allows for the redistribution of funds in society between savers and borrowers. Selecting banks which take into consideration these concepts in their business decisions should provide an additional boost to the achievable medium-term return on the investment. There is a clear advantage for core Eurozone banks over those in peripheral countries, due to better earnings visibility.

In the USA, the ascent of the American stock markets have been breathtaking, for which the present administration has eagerly taken credit. America's president will not be so minded when gravity reasserts itself. The FED will handle the planned interest increases in the most careful manner. Forecasts range from 2-4%, and all support the unwinding of QE. QE has been supportive of the stock market by an unfathomable amount. Investors will start taking notice of the extent as soon as mid-2019, when the FED will shed up to USD 600 bn in securities from its balance sheet each year.

In the worst-case scenario, the American-listed companies could plunge by about 30%, with ripple effects into the financial sector. Considering the fact that the US EIU (economist intelligence unit) ranks this case as #2 after the trade war (top risk), it is clear that things could get serious for the financial sector in 2019.

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 should be avoided until more clarity is provided regarding Brazil (election outcome).

We like institutions that are expected to be less affected by an eventual recession. Therefore, we focus on end-consumer service providers like lenders, credit card companies and the like. 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.

Consumer Discretionaries

US: Automotive: The auto industry is feeling the heat of steel and aluminum tariffs. It is up for debate whether OEMs can eventually raise prices to compensate. The ratcheting up of broader tariffs between China and the US may impact some components, but won't likely have much impact on finished vehicles, since very few finished vehicles are imported by the US from China. In addition, most vehicles sold by US OEMs in China are made there, with only a few brands exported to China. Thus, the impact will vary depending on the company, with some more exposed than others. Based on recent top-level discussions between the US and China, the US administration postponed its next round of tariffs against Chinese goods, allowing for further negotiations. Plus, it appears that China has agreed to reduce tariffs levied against autos imported from the US. However, the situation is volatile and there is no assurance that agreement will be reached or what the ultimate outcome will be; even so, it is a step in the right direction.

Smart mobility—driving, ride-sharing and electrification: This is a key area on which investors should focus. In a recent announcement, prominent tech investor Softbank took nearly a 20% stake in General Motors' (GM) smart mobility arm. Ford has followed suit, detaching its self-driving vehicle business in a separate wholly-owned entity; to date, however, no outside funds have been invested.

Still, most launch targets for autonomous vehicles, at scale, are generally 4-5 years away. The prospect of technological disruption to the industry is truly exciting. However, they are unlikely to cause the OEM stocks to outperform the consumer discretionary sector benchmark in the near term.

Europe: In 2018, the luxury sector experienced a year of two very different halves. After a strong share price performance in the first half, luxury goods stocks suffered from increased concerns about China in the second half. However, companies continued to report strong results and did not show any slowdown in their business momentum.

In 2019, we expect sales growth to decelerate to high single digits, down from around 12% in 2018. 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. In our view, polarization of brand performance will continue. Our preference is therefore for companies with good organic growth opportunities at attractive valuations.

Key themes for quarters ahead:
e-Commerce/Omni-channel: We believe opportunities around the e-Commerce theme extend beyond merely owning pure-play online shopping or e-Commerce companies. Consumer-focused industries such as retail, apparel, consumer packaged goods and restaurants will benefit as they take an omni-channel approach to business and as more consumers shift their spending online.

Improving consumer environment: Lower unemployment, rising wages and cheap gas should help provide a tailwind for consumer spending as we head into the fall/holiday season.

Disruptive mobility: Content per vehicle is rising as consumers increasingly demand connectivity and "infotainment" packages. More vehicles now include advanced drive assistance systems ("ADAS") such as autonomous emergency braking, lane assistance, etc., paving the way for the eventual launch of driverless cars. OEMs have also invested in shared riding services, a clear sign that things are really starting to take shape.

Investment opportunities:

Understanding the changing consumer spending paradigm is key! There are strong indications—among these, the recent retail sales report—that consumers and especially millennials have different spending habits now than they did prior to the Great Recession. Given this, we favor UUA, EL, NFLX, N, ADS, and ZAL, among others. Fixed income investors may also consider our new certificate, available under CH0408529433; it is a 2-year product with annual coupons of 7.56%, paid quarterly. Capital guarantee conditions apply for this product; the term-sheet may be downloaded here.

Key figures for Asia:

Target values:

Present fair value MXAPJ:	596
E12 months value MXAPJ:	650
Upside potential:	+9.0%

Key economic ratios:

P/E 2019 (E):	12.2
P/E 2020 (E):	11.3
Div. Yield 2019:	2.9
Div. Yield 2020:	3.1

Most likely next short term move:

MXAPJ	flat/up

Key names to look at:

- Tencent
- Alibaba

Industrials

In the industrial sector, we do see an increased level of volatility for 2019. Therefore, it is opportune to hold on to a well-diversified selection of industry manufacturers and technology-focused suppliers. We have a preference for companies that are not exposed to trade tariffs, as well as those that could benefit if a tariff solution triggers a rebound. This includes companies with positive ESG aspects, as well as earnings-growth and corporate-restructuring stories.

In the past we argued in favor of a diversified selection of European car and tire manufacturers and suppliers with a strong commitment to R&D-driven technology. We stated that corporate restructurings, the future of diesel and the appearance of self-driving cars in a disruptive automotive world (IIoT, robotics, and increased automation) would drive the sector and individual stocks. The ongoing trade war between the US and China has de-rated this trade opportunity more and more, on back of ongoing profit warnings.

For the coming years, volume growth across the entire sector is expected to be limited. Europe might recover, but should present below par results, as will the US. By contrast, Brazil and Russia could potentially grow between 1-5%. China is really the wild card. If China fails to introduce tax incentives, then overall global volume growth will turn negative in 2019. Visibility is currently very low and potential tariff threats are still unresolved. Pricing is not getting easier, and there is no help to be had from commodities or currencies.

The consensus view of the industry's EPS growth is presently at 9%, which is relatively high given that most companies in the sector are at a mid-late cycle stage.

Apart from the automotive industries, we do like the aerospace sub-sector. Strong secular growth trend in travels should drive further demand for airplanes. That adds a multi-year order backlog; this is an almost ideal investment case, with high visibility on earnings growth and a sound bottom-up environment.

The industrial sector has absorbed a number of bubbles and hypes in the recent years, and has always managed to reinvent itself. Currently, the attention is focused on IIoT; we strongly believe that while there is some hype, there is nevertheless a fundamental change underway in how industries design, produce, and sell products. It is in this field that we see some of the best investment opportunities, especially in mid-caps, as these stocks were most affected by the equity market correction in 4Q 2018.

One of the main risks for industrials, in our view, is presented in the high FY02-EPS forecasts. Any de-rating there would evidence a fundamental change to a number of strong long-term secular trends, such as IIoT, Air-travel (tourism), and consumption representing social benefits.

Investment opportunities:

Ultimately, manufacturing transformations will be quicker to plan, thanks to the speed and flexibility of digital tools. Who is on the cutting edge?

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

Healthcare was one of the best performing sectors in 2018, as creeping concerns about the length of the cycle, tighter monetary policy and trade dispute fears saw investors rotate into defensive sectors and value stocks. Fundamentals also improved compared with 2017, with pharma companies seeing stable earnings trends, broadly positive clinical data, and a modest tailwind from the stronger US dollar in 2H. We continue to view med-tech fundamentals as broadly attractive at an industry level.

Turning to 2019, macro outcomes will likely drive the sector's relative performance again. Our base case of continued volatility, steady tightening and slowing–but still positive–economic growth contains both positives and negatives for pharma, which typically underperforms during periods of steadily rising interest rates, but offers insurance against a cyclical downturn. Macro risks for the sector are marginally skewed to the upside, given the stage of the cycle.

Drug pricing remains a controversial topic, with bipartisan support for more curbs on US drug price growth, but with significant disagreement between the major parties about how to achieve the change. Many detailed proposals have been floated, but we assume that the pharma industry is avoiding the worst case scenario. One factor to watch in 2019 will be the evolution of the Democrats' healthcare policy as they gear up for the 2020 presidential elections. We expect healthcare policy to remain in the news, but an element of fatigue has set in and stocks are now less sensitive to headlines.

Therefore, valuations are fair to modestly high, compared to the global market; the sector's good cash flow and dividend growth should be attractive to longer-term investors. Companies than can to save costs for the system, without undermining the quality of care, will gain a competitive advantage. On the other hand, companies with breakthrough technologies should have the best long-term outlooks.

Thinking beyond 2019, one can expect the healthcare industry to undergo considerable changes. While the previous waves of IT adaptation favored the improvement of processes and security, the oncoming wave will again focus on patients' real needs. Healthcare digitization is about understanding what customers really want. By pushing digital healthcare, the industry is facing a number of issues:

1) Digital services for healthcare: Industry surveys show that patients don't use digital services! This is quite correct. A McK report shows that the primary reason for the low rate of customer adaptation to digital healthcare is because existing services either don't meet customer needs or are of poor quality.

2) Conflict of generations: Industry lobbies argue that only younger generations want to use digital services, and therefore digitized healthcare would not reach many of the system's core stakeholders. However, McK's survey demonstrates that in reality, patients from all age groups are more than willing to use digital services for healthcare. In fact, older patients (those over 50) want digital healthcare services nearly as much as do their younger counterparts.

3) Mobile health–Is it a game changer? There is certainly a demand for mobile healthcare applications. The demand is strongest among Generations Z and Y. Health systems should therefore create mobile solutions that target this audience—for example, apps that focus on prenatal health or those that could be classified as lifestyle apps.

4) Patient expectations: Patients don't want hype, but have basic expectations of their healthcare system should provide. For example, patients expect efficiency, better access to information, integration with other channels, and availability of a real person if the digital service doesn't provide what they need.

5) Comprehensive service: Many institutions believe it is necessary to "go big" before they can achieve anything—they believe they must build a comprehensive platform with offerings along the entire spectrum of customer services. But McK's survey demonstrates that it can be smarter to start small and act fast!

What is our reading on these results?

The healthcare industry's vision on how to provide services is probably not meeting customer requirements or expectations. Unique to healthcare, it is being argued by decision makers that healthcare services should be equally accessible to users from every social strata. This is a fascinating statement of ethos, and healthcare is likely the only economic sector with such an underpinning philosophy. Does Apple, for instance, consider it essential to provide its iPhone to all potential users across the nation? Of course not! Steve Jobs' plan was to deliver a medium that includes diverse opportunities for purchase at different price points, such as phone, radio, listening to music, photos and so on, all in a user friendly manner. The purchase of an item is not mandatory, but people fall in love with apps because they are easy to use and meet real and felt needs.

We believe healthcare providers will fail in modernizing their customer approach, because they doggedly try to deliver their digital services equally to the entire customer base. In consequence, there is plenty of room for disruptors.

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 include the following: AstraZeneca, Bayer, Novartis, Novo Nordisk, Merck, Pfizer, Alexion, Celgene, Straumann.

Utilities

Should battery storage business be on your investment radar?

The use of batteries (mobile and stationary) has increased in the past several years. Rising consumer openness to alternative energy sources, along with the falling costs of these energy sources, are the main reasons behind this increase. However, the hurdle the industry has to overcome is how to recharge batteries quickly. In fact, solving this problem is the key to spurring on widespread use of electric cars.

In short, as storage costs fall and if recharging is made available in rapid manner, there's no need to further explain how the economic landscape will look tomorrow. Businesses that get the timing right (e.g. investing in storage) should be the key beneficiaries of a strong and lasting secular trend.

Often, utility operators are considered to be slow moving institutions that are unwilling to adapt to new technologies. However, at the moment, they have been given a golden opportunity to both stay in business and master the future. Today, facilities who are doing so are almost nonexistent, and when there an opportunity to do so presents itself, the capacity is low. Utility providers do have the network, so in essence, they have to provide the connectors. But, are they ready to prove capable of change?

Similarly, in the past, oil giants have deployed gasoline stations around the world; presently, utilities would be well advised to deploy charging stations worldwide. Installation of on-site batteries which can be charged via the grid when there is a general surplus and made available on demand is a business opportunity that should be developed. This two-cycle process presents a number of advantages:

a) **Sustainability**: Demand and offer can be managed in a better manner, making power generation a more linear event with fewer facilities needed to keep a constant service going. This is not currently the case! A good number of facilities are in an idle status until demand turns up, or until their utilization ratio is highly irregular.
b) **Growth:** The committee of the International Energy Agency stated that for the decade of 2016 to 2025, the Utility sector in the US needed a total new investment of USD 7 trillion in order to maintain its infrastructure. By correctly deploying these investments, new value pools could be created and follow-up investments could lead to robust GDP creation, something developed markets are desperately lacking these days.
c) **Investment returns:** As the world economy has grown, so has demand for power. Even so, the performance of utilities has been dull. The average cumulative return to shareholders of the 50 major publicly listed utilities has been just 1% over the past decade; reinventing their business could be supportive to driving investment returns.
d) **Timing:** Up until now, power distribution has been considered to be boring and tedious work. For this reason, utilities gained monopoly status. However, because efficient mobile storage has now become an opportunity, new players from the financial service sector and oil and gas industry have entered the market. This new competition will drive down prices and therefore the returns of old-fashioned utility operators.
e) **Digitations:** Utilities must adapt more speedily and skillfully than they have done in the past. Disruptors enter the market with the latest technologies on hand, thereby managing products and services in a manner that is relevant to user wishes, which existing utility providers have ignored for too long.

Investment opportunities:

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.

Regarding opportunities in the battery business, please refer to the table on the next page.

List of main battery manufactures and their respective clients

Battery manufacturer	Carmaker / Implementation	Type of battery
A123Systems	Killacycle motorcycle, General Motors Fisker Automotive, Daimler Buses North America	Lithium-ion (lithium iron phosphate)
AESC	Nissan vehicles	Lithium iron
Axeon	Rolls-Royce Motor Cars, Modec, Allied Vehicles, RUF Automobile, Jaguar Cars, Land Rover, Electric Car Corporation	Lithium iron phosphate
Coslight India	Electric Bus LFP batteries, EV LFP Batteries, E car LFP & NMC batteries	Lithium-ion
Axion Power International	ePower Engine Systems	Lead carbon
Bosch/Samsung	Fiat 500e	Lithium-ion
Boston Power	Beijing Automotive Group, Saab Automobile	Lithium-ion
E-One Moli Energy	BMW Mini-E	Lithium-ion
Johnson Controls	Daimler AG, Ford	Lithium-ion
Li-Tec Battery GmbH	Daimler AG and other	Lithium-ion
NEC	Nissan	
Panasonic	Tesla Motors	Lithium-ion
Samsung SD	BMW and Volkswagen	
Sanyo	Honda and Ford hybrid vehicles and Suzuki Swift	NiMH
AESC	Nissan vehicles	Lithium-ion
Tesla	Gigafactory in joint venture with Panasonic	Lithium-ion
LG Chem	General Motors, Renault, Hyundai	Lithium-ion

Foreign exchange

Currencies

The US mid-term elections marked a turning point for the US government. With Democrats gaining control of the House of Representatives, it seems unlikely that new tax cuts will be implemented. On the other hand, if the present US Administration wants to prolong its mandate, it could focus on a large tax deal for the middle-class, who are mostly Democrats. Therefore, the present US administration could gain support from both sides.

Finally, the potential for trouble in passing a budget and a debt ceiling increase may will hurt the USD. These issues are likely to become factors only towards the end of 2019. Federal Reserve rate hikes for 2019 are less of an issue now with markets being relatively negative for a prolonged period of time.

The European Central Bank (ECB) has ended its asset purchases in December of 2018. Its communication could stay cautious into next year given the Eurozone's weaker data recently. We expect the first ECB rate hike in 4Q19. Over the next 6-12 months, we expect Europe to overcome the Italian challenge and for the ECB to become more concrete about policy tightening.

In sum, we are keeping our short-term positive view on the USD and expect EURUSD to hit new lows of around 1.10. Longer term, we see EURUSD rising again. A stronger commitment to policy tightening in Europe, the Fed's approach to the end of its tightening cycle, and deficit-financing issues in the US are likely to support EURUSD starting 2H19.

Energy/Commodities

Crude oil:

Right now, the global oil market appears to be in balance. However, putting the new pipeline out from the Permian basin into service is likely to put an end to this fragile situation. Although OPEC is high unpredictable, the market does not expect the group to return to a period with no quotas. While Saudi Arabia and Russia have indicated their willingness to increase supply to avoid excessive stress in the market, they could potentially go in the opposite direction and flash the market with an oversupply so that US shale oil becomes highly unprofitable.

Infrastructure build is key: Infrastructure build-up prior to starting production is key, especially in fast-growing areas such as the Permian basin and the Midland. Lack of infrastructure means lost sale opportunities, and US shale oil producers have already had their share of experience with that a number of times.

At present, the market does not fear a shift in demand. Oil demand is expected to grow by a robust 1.5 mb/d on average throughout 2019, the main demand coming from Emerging Asia. After all, converting fossil to an actionable energy is still the most cost efficient means of creating energy. Therefore, demand is not expected to turn down unless the world economy enters a prolonged period of recession in which consumers would be required to reassess their consumption.

FX-Rates:

Target values in 3 months:

EUR/USD:	1.1250 - 1.1750
GBP/USD:	1.2000 - 1.3500
USD/CHF:	0.9750 - 1.00

Target values in 12 months:

EUR/USD:	1.20 - 1.25
GBP/USD:	1.10 - 1.35
USD/CHF:	1.00 - 1.05

Purchase power parities:

EUR/USD:	1.30
GBP/USD:	1.61
USD/CHF:	0.92
EUR/CHF:	1.20

Most likely next move:

EUR/USD	down
GBP/USD	down
USD/CHF	down

Target values in 3 months:

Oil:	$50 - $65
Gold:	$1,250

Target values in 12 months:

Oil:	$65 - $80
Gold:	$1,250

Upside potentials:

S&P GSCI	flat
Oil	flat
Gold	flat

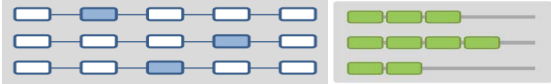
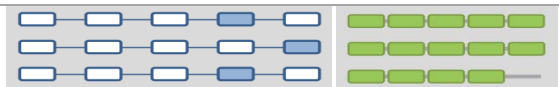
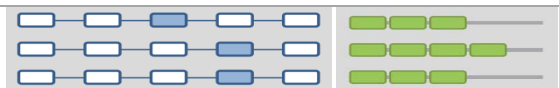
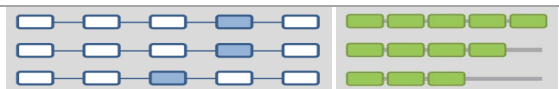
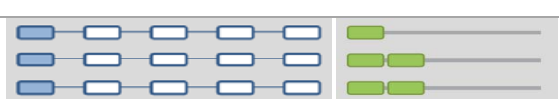
Next most likely move:

S&P GSCI	flat/up
Oil	flat/up
Gold	flat/up

Commodity related stocks:

IRISOS
Knowledge is power.

Asset Allocation Preferences – January, 2019

Sector	Region	Fundamental	Risk/Reward	Investment case
Basic Materials	Americas Europe EM			The US administration-initiated trade war is not just a bluff, and its ramifications may extend well beyond general expectations. Given current knowledge regarding the trade war between the US and China, basic material companies are trading fair value. However, the situation could become more complex if the status-quo persists.
Consumer Staples	Americas Europe EM			Consumer staples companies with diverse geographic exposure and leading brands are expected to grow in developed and emerging markets. In a very competitive landscape, further industry consolidation must be expected. Disruptors are eager to enter into any possible segment, and therefore, valuations are still toppish for the most of the entities.
Consumer Disc.	Americas Europe EM			Based on the overall bottom-up scenario, the macroeconomic backdrop for consumers is favorable, and financial conditions are also supportive of consumer spending. However, weaker equity markets and political uncertainty, including ongoing trade tensions, could weigh on business and consumer sentiment.
Energy	Americas Europe EM			With new International Maritime Organization (IMO) limits on maritime vessels' exhaust emissions coming into force in 2020, the oil industry is gearing up for disruption, as shipping companies choose whether to convert engines to rules-compliant fuel, install scrubbers to continue using heavy fuel oil or switch to liquefied natural gas. Repsol SA, Neste Oyj, BP Plc, Total and Saras SpA are best positioned to handle the changeover to so-called IMO 2020 regulations because of their refinery capacity for cleaner burning products.
Healthcare	Americas Europe EM			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 pipelines can drive meaningful earnings momentum. In med-tech, we prefer companies with scope for self-help, given expensive valuations.
Financial Services	Americas Europe EM			Sustained higher bank earnings should only come with actual interest rates hikes. This is the case for US-based institutions now, and are expected to start materializing for European based banks toward the end of 2019 at the earliest. While benign credit quality may continue to support reported earnings, we see no reason for a sustained sector outperformance. However, some selective stocks offer compelling investment cases.
Industrials	Americas Europe EM			From a bottom-up perspective, we see pros and cons for the sector. One positive factor is that most important end markets are only at their mid-cycle level. However, trade tensions, tariffs, as well as wage and raw material inflation are negatively impacting margins. The valuation offers attractive investments in medium sized companies in the area of IIoT.
IT	Americas Europe EM			This sector's companies experienced significant volatility during Q4/2018. The sector's key areas (e.g., IIOT, connectivity, AI, VR, etc.) remain fully intact. Nevertheless, we expect volatility to remain ultra high—this is in line with prior similar periods. Software and service companies are our preferred play, as they take advantage of recurring revenues.
Telecom.	Americas Europe 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 Europe EM			The sector offers an attractive dividend yield of more than 5%, and is relatively insensitive to the global slowdown and ongoing trade disputes. We are confident that 10% EPS growth is achievable among the sector's large-caps. Regulatory risks persist, particularly in Italy, but in our view these are largely priced in. Valuations are attractive compared with other non-cyclical sectors, such as consumer staples and healthcare.

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

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