Monthly Asset Allocation

Private Banking Europe Investment Committee

November 15, 2017

In a nutshell

- Equities show solid earnings growth; companies confirm their outlook for the coming quarters
- Government bonds continue to trade in a narrow range
- We are raising tactically the commodity allocation from "underweight" to "neutral"

Global leading indicators continue to be positive – central banks remain in expansion mode on an aggregated basis

The already positive economic picture has improved once again compared to the previous quarter. A further acceleration could be observed especially in the euro zone as the German Ifo index is at its highest level ever measured. Inflation expectations are slightly lower than the expectations of the central banks, but no longer exhibit any deflationary tendencies. This also leads to a situation in which – despite interest rate hikes by the US Federal Reserve Bank (Fed) – global monetary policymakers continue to act expansively on an aggregated basis. Furthermore, there is currently little inflationary pressure from wages. Despite full employment, the most recent US figures were very moderate and give the Fed the flexibility it needs for the coming months. However, it remains to be seen if the US government's fiscal impulse will have a lasting impact on the inflation rate in the US economy, which is already at a very advanced stage of the cycle. We expect the core inflation rate in the USA to move towards 2%.

This outlook leads us to a tactical overweight for equities at the asset allocation level, which is detrimental to the bond ratio, as we tend to expect rising yields at the long end. The alternative investment segment remains underweighted, although we are now moving the commodities segment to a "neutral" positioning. The cash ratio remains overweight as we would like to maintain maximum flexibility in the event of a possible consolidation or correction.

Table 1: Generic Tactical Asset Allocation LGT Private Banking Europe (November 15, 2017)

	Asset Class	SAA	underweight -8% -6% -4% -2%	Strategic (SAA) vs Tactical Asset Allocation (TAA) in USD	+2% +4% +6% +8% overweight	TAA		
		USD				USD	EUR	CHF
Equities	US equities	20.0%				20.0%	15.0%	15.0%
Equities	Europe equities	6.0%				9.0%	12.0%	8.0%
Equities	UK equities	3.0%				3.0%	4.0%	2.0%
Equities	Switzerland equities	1.0%				1.0%	2.0%	8.0%
Equities	Japan equities	4.0%				5.0%	5.0%	5.0%
Equities	APAC ex JP equities	3.0%				2.0%	2.0%	2.0%
Equities	Emerging markets equities	6.0%				6.0%	6.0%	6.0%
Equities	**Total Equities**	**43.0%**				**46.0%**	**46.0%**	**46.0%**
Fixed Income	Government bonds	6.0%				3.0%	3.0%	0.0%
Fixed Income	Inflation-linked bonds	6.0%				6.0%	6.0%	5.0%
Fixed Income	Investment grade bonds	12.0%				12.0%	12.0%	16.0%
Fixed Income	High yield bonds	6.0%				0.0%	0.0%	0.0%
Fixed Income	Subordinated Debt	0.0%				3.0%	3.0%	3.0%
Fixed Income	Emerging markets bonds	6.0%				8.0%	8.0%	8.0%
Fixed Income	**Total Fixed Income**	**36.0%**				**32.0%**	**32.0%**	**32.0%**
Alternatives	Hedge funds	7.0%				6.0%	6.0%	6.0%
Alternatives	Listed private equity	2.0%				0.0%	0.0%	0.0%
Alternatives	Real estate trusts	3.0%				3.0%	3.0%	3.0%
Alternatives	Insurance-linked bonds	3.0%				4.0%	4.0%	4.0%
Alternatives	Commodities	2.0%				2.0%	2.0%	2.0%
Alternatives	Precious metals	2.0%				2.0%	2.0%	2.0%
Alternatives	**Total Alternatives**	**19.0%**				**17.0%**	**17.0%**	**17.0%**
	Cash	**2.0%**				**5.0%**	**5.0%**	**5.0%**
			-8% -6% -4% -2%		+2% +4% +6% +8%			
Currencies	USD	86.5%				85.5%	10.0%	10.0%
Currencies	EUR	0.0%				0.0%	75.1%	0.0%
Currencies	CHF	0.0%				0.0%	0.0%	75.7%
Currencies	GBP	0.0%				0.0%	0.0%	0.0%
Currencies	Others (incl. EM)	13.5%				14.5%	14.9%	14.3%

Source: LGT Investment Services Europe

*all calculations based on a "Balanced Portfolio" in USD including AI. For EUR and CHF portfolios weights differ for subclasses; over- and underweights apply analogously.

Table 2: Current asset allocation preferences

Next meeting: Dec 11, 2017	What we like	What we dislike
Equities	European equity Japanese equity Oil and gas sector stocks Low volatility products	
Bonds	Low duration Emerging Market Local Currency bonds Subordinated debt	Sovereign bonds High yield bonds
Alternative Investments	Insurance linked bonds	Listed private equity
Currencies		

Sources: LGT Investment Services Europe

Equities: solid earnings growth – outlook for the coming quarters confirmed

As the past earnings season has shown, companies have been able to meet and often exceed expectations: on average, more than half of all companies in the S&P 500 were able to beat profit expectations. The sales figures were almost 70%. A continuation of this momentum is also necessary, as the global stock markets are at their highest levels since the outbreak of the financial crisis in 2008/9 and the valuation remains in the upper quartile by historical standards. The outlook for the coming quarters was confirmed by most companies. Given the positive economic environment, this trend can be expected to continue. Volatility is at its lowest level in years. Nevertheless, a correction on the stock markets in the coming months is certainly possible. From today's perspective, this correction should be used to build up further positions as the global synchronous upswing is expected to continue. At the regional level, we see the most potential for European stocks in the global environment due to their valuation and attractive dividends.

Fixed Income: government bonds continue to trade in a narrow range

Even during the fourth quarter of 2017, long-term interest rates in the developed countries barely moved out of their narrow trading range. Quantitative easing by the European Central Bank (ECB) and the Japanese central bank (BoJ) continues to have a too strong impact. However, we believe that this effect should weaken in the coming quarters due to the ECB's tapering and the beginning of the US Fed's reduction of its balance sheet. We expect to see rising interest rates at the long end of the curve, especially in the USA. Against the backdrop of this outlook, we recommend our clients to continue with a pronounced underweight in government bonds, especially in the euro zone and Swiss government bonds. Due to the flat yield curve, we consider bonds with a short maturity or short duration to be suitable. Within the bond ratio, we see potential in emerging market bonds and selectively in subordinated bonds. Historically, the risk premiums for high-yield bonds are at a record low. Investors are no longer receiving an adequate premium for the risk they are taking, which is why we remain strongly underweight in this investment category.

Commodities and currencies: increase commodity weighting to "neutral"

After the drastic drop of the oil price in 2015 and 2016, the commodities sector has been in a classical phase of "basis building" for almost two years. Demand is rising steadily due to the synchronous global recovery and capacity should not be expanded further in the short term. Experience has shown that this should lead to rising prices. In recent quarters, a strong inverse correlation between the US dollar and the performance of commodities was observed. Following the recent gains of the greenback, the Private Banking Investment Committee no longer considers it appropriate to underweight commodities, and tactically increases the ratio from "underweight" to "neutral". In the medium to long term, we expect a weaker US currency due to purchasing power parity and the impetus from the anticipated US government's fiscal stimulus.

If you require further information or advise, please contact your LGT relationship manager.

Author: Thomas Wille, Head Investment Strategy & Communication; Editor: Natija Dolic, Investment Writer

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