June 14, 2017

Tactical asset allocation for Q3/2017

Strategy team, LGT Capital Partners

The global reflationary rebound that began in early 2016 remains intact, but momentum is slowing, and the upswing in the tangible economic data has generally lagged the sentiment surge, leaving room for a reality check. Against this background, we have modestly de-risked our portfolios to replenish cash reserves and be better prepared for future investment opportunities.

Below we present the result of LGT Capital Partners' latest quarterly tactical asset allocation (TAA) review, which was concluded last Friday. The TAA represents our market assessment for the next three to six months and is expressed as our investment positioning relative to our strategic allocation (SAA), i.e. our house view for the coming years.

Macroeconomic base scenario remains benign, but…

The global macro backdrop remains benign, with economic growth sufficient and inflation moderate. Moreover, corporate earnings are growing at a stronger than expected pace in all major regions. At the same time, some sentiment indicators may have rushed ahead too quickly, as the actual macro data has often not kept up with these implied expectations. Markets could thus be more susceptible to be reined in by reality at some point in the near future.

To some extent, this is already evident in the US, where the new administration, in office for less than half a year, has yet to deliver on the promised infrastructure investment plan and tax reform. A similar development could be due in the European Union (EU) as well, where a series of europhile election outcomes have triggered an instant collapse of the measurable EU breakup risk premia, helping bolster the already surging regional business and consumer confidence readings to new records.

While our cyclical assessment for the eurozone is clearly positive, it remains to be seen to what degree this sentiment surge will actually translate into tangible economic growth in the near future. Furthermore, inflation in the industrialized world is likely to remain subdued - if not moderate further, as the outlook for energy prices remains tepid in our view, while wage-driven inflation pressures are in their infancy at best. The inflation outlook thus accentuates the loss of the reflationary momentum in the global economy.

Last but not least, the outlook for the emerging markets (EM) continues to be positive, supported by a rebound in global trade and a softer US dollar. Beyond that, the EM space remains very diverse. On the cautious side, Brazil is going through another governance scandal, albeit one that is unlikely to weigh on other markets. China's controlled credit tightening effort, meanwhile, comes with the risk of slamming the brakes too hard again in the near-term. On the positive side, Eastern Europe is supported by the EU upswing, India is progressing with daring reforms, while South Korea benefits from the improved global trade.

Modest shift from equities to EM debt and cash

That being said, we believe that the bull market remains intact, as it is underpinned by robust fundamentals. Corporate earnings are growing at double-digit rates, debt defaults are rare or decreasing, while macro policy settings are appropriate for continued growth.

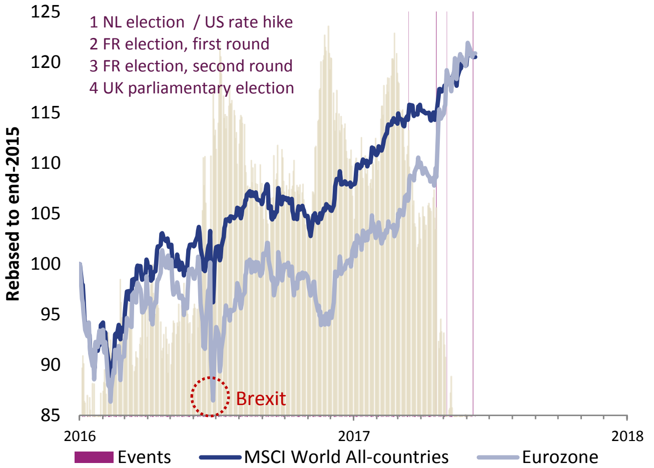
However, investor sentiment and positioning look somewhat stretched in the short-term. Despite the considerable political noise, the reflationary rally that began in early 2016 has been remarkably robust and steady. As a result, equity overweights are now commonplace and investor complacency has risen, while geopolitical tensions persist, particularly in Northeast Asia and the Middle East. We thus see the conditions for a temporary pullback during the summer in place and decided to modestly reduce our most pronounced equity overweights, i.e. our positions in Europe, Japan, and Asia-Pacific. We are keeping most of the proceeds in cash to be better prepared to buy the next meaningful dip, if and when it occurs.

Tactical decisions by asset class

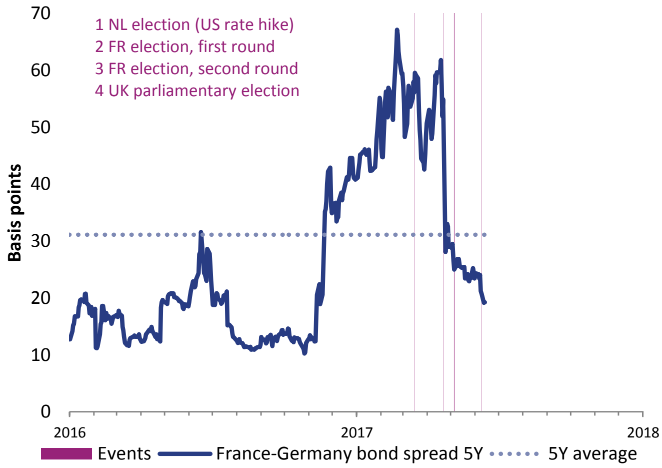
Equities: reduced overall overweight with less pronounced regional preferences

We have trimmed our equity overweight somewhat by shaving off a modest part of each of our hitherto most pronounced active positions, namely Europe, Japan, and Asia-Pacific. The overall segment is still clearly above our neutral (strategic) quota. Europe and Japan continue to be more attractively rated in our assessment than the other markets, although to a somewhat lesser degree than before. The positions in the US and the EM remain unchanged. As before, we keep a clear underweight in listed private equity (LPE), where discounts to net asset values are below historic averages and thus somewhat expensive. We keep our small overweights in listed real estate (REITs) and listed infrastructure (MLPs) because of the high and relatively stable dividend yield these segments offer. Commodity producer equities are left at a small underweight - in line with our cautious view on commodities.

Global and European equities, total return in USD



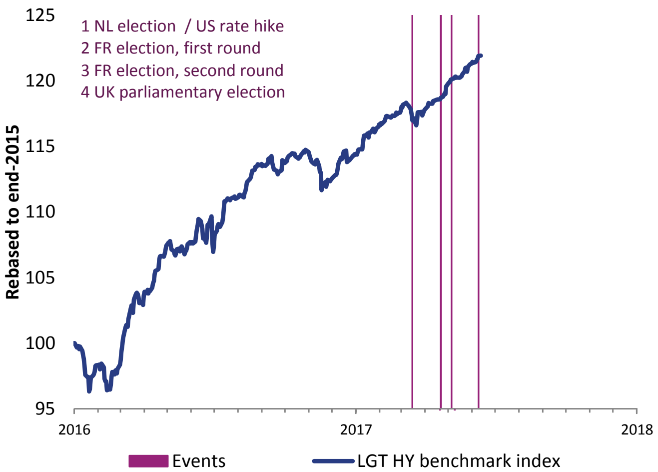
Franco-German 5-year bond yield spread



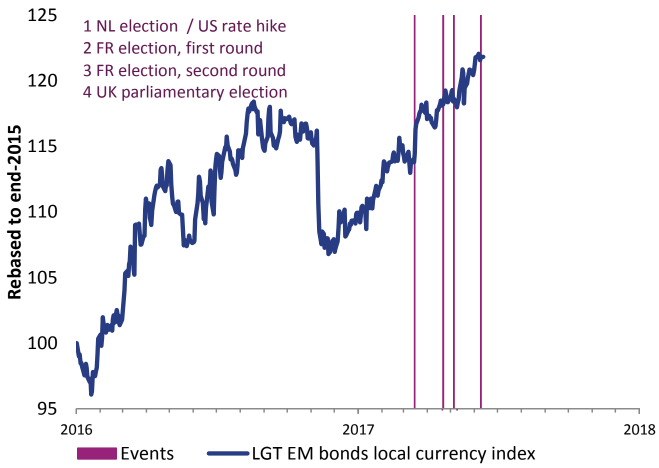
Fixed income: switch from high yield to local currency EM debt

In sovereign debt, we kept our overall underweight and relative short duration and reduced our high yield credit (HY) position to a clear underweight. Continued spread tightening has made the HY space expensive. We find better value in EM bonds issued in local currencies and added to our existing marginally overweight position. This segment benefits from the benign global growth outlook and the softer US dollar. Relatively high real yields and undervalued currencies also offer support.

High yield credit, total return in USD



EM local currency bonds, total return in USD



Moderate de-risking our portfolios

Overall, we de-risked our portfolio at the margin by taking profits in equities and high yield bonds. As a consequence, we now hold a higher cash quota which we look to deploy again should an opportunity arise.

Neutralizing US dollar and reaffirming preference for the Swedish krona

In foreign exchange, the Swedish krona (SEK) is kept as our last remaining tactical overweight, held against the overvalued Swiss franc. We had initiated this position on relative valuation grounds and divergent central bank biases last quarter and are now reaffirming this assessment. Meanwhile, the remaining overweight in the US dollar was fully closed.

As a result of the various active positions in Asia-Pacific (excluding Japan) and the EM, the respective regional currencies ("others" in our allocation table) are now generally modestly overweight against the base currencies of the various portfolio strategies.

Market Performance

Equities		Global share	Mkt Cap. in $	Last price	5 days	1 month	3 months	6 months	1 year	Year to date	Trend over past yr
World	BBG World All Country	100%	74,885	214.2	-0.2%	1.7%	4.7%	8.3%	16.0%	10.1%	Rising
Americas											
USA	S&P 500	36.3%	27,173	2,429.4	-0.3%	1.6%	2.4%	6.9%	16.9%	8.5%	Rising
	Nasdaq Composite *	12.9%	9,626	6,175.5	-1.9%	0.9%	5.1%	13.0%	27.4%	14.7%	Rising
	S&P 600 Small Cap *	1.1%	786	862.4	1.9%	2.8%	3.5%	1.6%	22.4%	2.9%	Rising
Canada	TSX	2.8%	2,077	15,383.8	-0.2%	-1.0%	-1.0%	0.0%	9.9%	0.6%	Sideways
Brazil	Bovespa	1.0%	734	61,700.2	-1.2%	-9.6%	-5.9%	4.1%	24.2%	2.4%	Rising
Mexico	Mexbol	0.5%	386	49,128.8	-0.9%	-0.6%	4.3%	4.8%	9.3%	7.6%	Rising
Europe											
Euroland	Euro Stoxx *	8.5%	6,358	382.9	-0.9%	-1.9%	5.1%	10.9%	24.8%	9.3%	Rising
UK	FTSE 100	4.6%	3,414	7,511.9	-0.2%	1.0%	2.0%	7.8%	24.3%	5.2%	Rising
Germany	DAX Price Ix	2.9%	2,187	6,014.4	-1.0%	-1.3%	3.4%	9.5%	27.9%	7.6%	Rising
Switzerl.	Swiss Perf Extra Pr Ix	2.3%	1,702	272.9	-2.2%	-2.4%	6.3%	17.6%	24.5%	15.3%	Rising
Poland	WSE	0.2%	180	2,295.0	0.8%	-3.1%	2.3%	19.6%	28.9%	17.8%	Rising
Russia	Micex	0.7%	540	1,883.3	0.1%	-5.6%	-4.6%	-15.4%	-1.1%	-15.6%	Falling
Asia											
Japan	Nikkei 225	7.6%	5,669	19,898.8	-0.4%	0.1%	1.3%	3.4%	24.2%	4.1%	Rising
Hong Kong	Hang Seng Ix	6.1%	4,566	25,802.9	-0.7%	2.6%	8.3%	15.0%	25.8%	17.3%	Rising
China H	China Enterprises Ix	9.1%	6,779	10,546.2	-0.6%	2.6%	2.8%	8.5%	22.3%	12.3%	Rising
China A	CSI 300	5.2%	3,863	3,582.3	2.6%	5.8%	3.6%	5.2%	16.8%	8.2%	Rising
Australia	ASX 200	1.6%	1,213	5,772.8	0.3%	-1.1%	0.0%	3.8%	8.7%	1.9%	Rising
India	Sensex	2.7%	1,994	31,184.1	0.0%	3.3%	7.7%	16.8%	18.1%	17.1%	Rising
Korea	Kospi	2.0%	1,510	2,375.5	0.3%	3.9%	12.2%	16.7%	20.0%	17.2%	Rising
Taiwan	Taiex	1.5%	1,122	10,128.2	-0.8%	1.4%	4.4%	8.0%	18.6%	9.5%	Rising

All indices: price indices (excl. dividends), in local currency. Market cap in billion USD at current exchange rates refers to country or index where marked with asterisk (*)

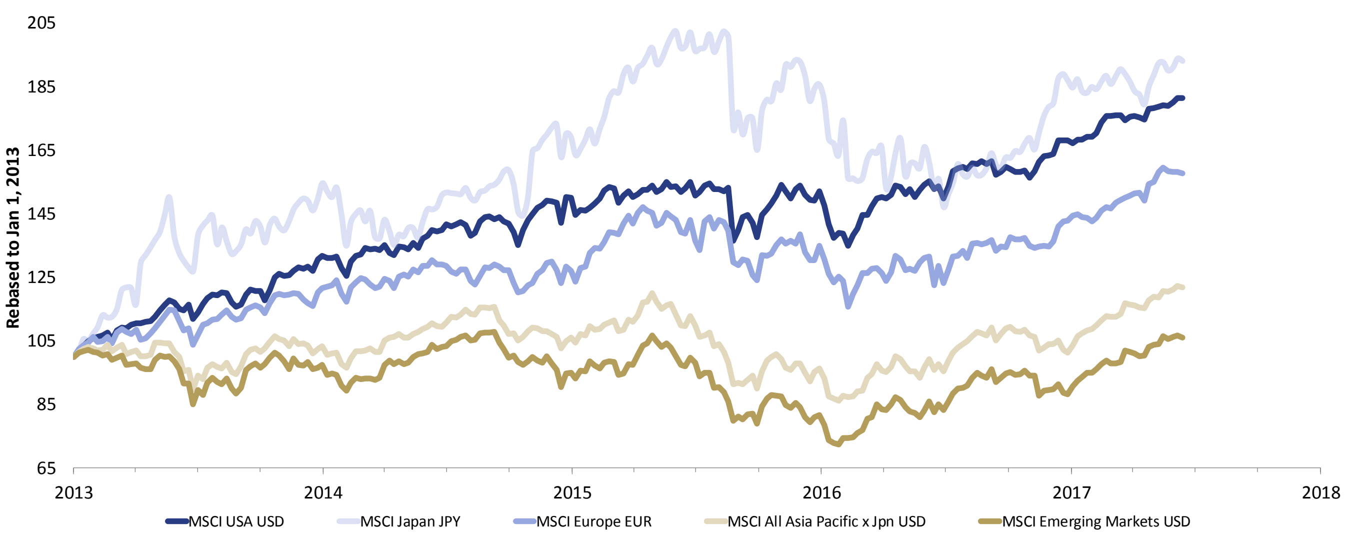
Currencies			Last price	5 days	1 month	3 months	6 months	1 year	Year to date	Trend over past yr
US Dollar, correlation-weighted index		USD	119.5	0.3%	-2.0%	-2.7%	-1.9%	3.0%	-3.8%	Sideways
Euro, correlation-weighted index		USD	100.7	-0.5%	0.6%	2.8%	3.9%	2.0%	3.1%	Rising
Japanese yen, correlation-weighted index		USD	359.2	-0.3%	1.3%	2.1%	3.2%	-0.9%	3.0%	Rising
Swiss franc, correlation-weighted index		USD	353.0	-0.6%	1.5%	1.5%	2.8%	2.4%	1.6%	Rising
Bonds										
US Treasuries **		USD	384.2	-0.2%	0.8%	2.5%	2.4%	-1.3%	2.1%	Rising
EMU Bonds (Germany) **		EUR	232.1	0.8%	1.3%	3.0%	1.7%	-0.7%	0.3%	Rising
UK Gilts **		GBP	659.2	0.4%	0.9%	2.3%	5.5%	5.3%	2.7%	Rising
EM Bonds USD ***		USD	832.1	0.0%	1.2%	4.4%	7.8%	8.5%	6.9%	Rising
EM Bonds Local ***		USD	284.1	0.1%	2.3%	7.3%	11.1%	9.7%	11.0%	Rising
Investment Grade USD +		USD	148.8	-0.2%	1.1%	3.7%	4.6%	2.9%	3.6%	Rising
High Yield USD +		USD	178.5	0.0%	0.7%	3.1%	5.6%	12.7%	5.1%	Rising

**Total return, indices of bonds with maturities of more than 1 year ***JP Morgan Indices + Bloomberg Indices

Commodities			Last price	5 days	1 month	3 months	6 months	1 year	Year to date	Trend over past yr
WTI Crude oil (generic future)		USD	46.3	-3.9%	-3.2%	-4.3%	-12.6%	-5.3%	-13.8%	Falling
Industrial Metals Index (S&P GSCI)		USD	145.7	0.6%	0.6%	-1.8%	-0.5%	21.9%	4.7%	Rising
Gold, spot price		USD	1,266.3	-2.2%	2.9%	5.1%	9.3%	-1.4%	10.4%	Rising

Source: Bloomberg. All data based on last traded price at cut off time: 6/13/2017 14:29

Net total return indices of major equity regions



Note: equity positions in the USA, Europe and Japan are always hedged against currency risk in our portfolios as a matter of principle.

Economic and Corporate Snapshots

Macro fundamentals		USA	Euroland	China	Japan	Germany	Britain	Brazil	Russia	Switzerl.
GDP, nominal, 2017 [1]	bn USD	19,417	11,729	11,795	4,841	3,423	2,497	2,141	1,561	659
GDP per capita, 2017 [1]	USD, PPP	59,609	38,322	16,676	42,860	49,815	44,001	15,485	27,466	61,014
Real GDP growth, expected 2017	Consensus	2.2%	1.7%	6.6%	1.3%	1.7%	1.7%	0.7%	1.2%	1.5%
Real GDP growth, expected 2018	Consensus	2.3%	1.6%	6.3%	1.0%	1.6%	1.3%	2.2%	1.6%	1.7%
Real GDP growth last quarter *	q/q annualized	1.2%	2.4%	5.3%	1.0%	2.4%	0.8%	4.3%	-2.3%	1.2%
Unemployment rate [2]		4.3%	9.3%	4.0%	2.8%	5.7%	4.6%	8.2%	5.3%	3.2%
Inflation, core rate (CPI)	y/y	1.5%	2.1%	0.9%	-0.3%	1.6%	3.5%	3.6%	3.8%	0.2%
Purchasing manager indices (comp.)	Neutral = 50	53.6	56.8	51.5	53.4	57.4	54.4	50.4	56.0	55.6
Structural budget balance/GDP 2017	IMF	-4.0%	-1.1%	-3.7%	-3.7%	0.2%	-2.8%	-7.6%	-2.5%	0.2%
Gross government debt/GDP 2017	IMF	108%	91%	49%	239%	65%	89%	81%	17%	45%
Current account balance/GDP 2017	IMF	-2.7%	3.0%	1.3%	4.2%	8.2%	-3.3%	-1.3%	3.3%	10.8%
International currency reserves	bn USD	42	259	3,054	1,189	37	119	185	336	750
			ESM / EFSF							
Govt bond yield 2yr **	p.a.	1.4%	-0.6%	3.6%	-0.1%	-0.7%	0.1%	9.5%	8.4%	-0.9%
Govt bond yield 10yr **	p.a.	2.2%	0.4%	4.1%	0.1%	0.2%	1.0%	8.0%	7.7%	-0.2%
Policy rate (or approximation) °	p.a.	1.00%	-0.40%	4.35%	-0.05%	-0.40%	0.25%	10.25%	8.25%	-0.75%

[1]IMF estimates. *annualized, most recent qtr. [2]PRC ex. migrant workers. ** Currency swap rates for China and Brazil, closest ESM or EFSF bonds for Eurozone. °Max target rate for Fed, SNB

Corporate fundamentals		USA	Euroland	China	Japan	Germany	Britain	Brazil	Russia	Switzerl.
Exchange capitalization*	USD	27,173	7,748	11,346	5,669	2,187	3,414	734	540	1,702
Growth in earnings per share, estimated (MSCI)										
Next fiscal year / current fiscal year	Consensus	12.2%	9.7%	13.8%	6.9%	8.2%	6.8%	9.3%	23.9%	10.4%
FY year after next / next FY	Consensus	10.7%	8.9%	14.0%	7.5%	7.8%	10.2%	20.0%	3.5%	9.5%
Growth in revenue per share, estimated (MSCI)										
Next fiscal year / current fiscal year	Consensus	5.3%	3.8%	11.1%	2.4%	3.2%	2.6%	6.4%	8.2%	3.6%
FY year after next / next FY	Consensus	5.2%	1.5%	9.9%	2.3%	3.0%	5.3%	7.9%	5.5%	2.4%
Valuation metrics (MSCI)										
Price-Earnings Ratio (est forward 12m)	Consensus	19.0	15.4	13.5	14.4	14.2	14.7	11.7	6.2	18.4
Price-Sales Ratio (est forward 12m)	Consensus	2.0	1.1	1.5	0.8	0.9	1.3	1.3	0.8	2.1
Dividend yield	Consensus	2.0%	3.1%	2.1%	2.2%	2.8%	4.2%	3.7%	5.7%	3.3%

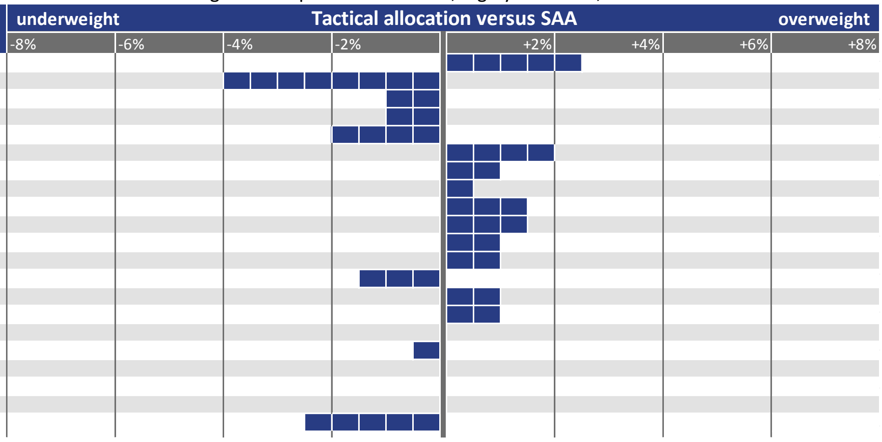
* China includes Hong Kong. Notes: Corporate fundamentals are based on consensus estimates ."Reversal +" denotes a return to profits, "Reversal -" an expected loss next year. Source: Bloomberg.

13.06.2017

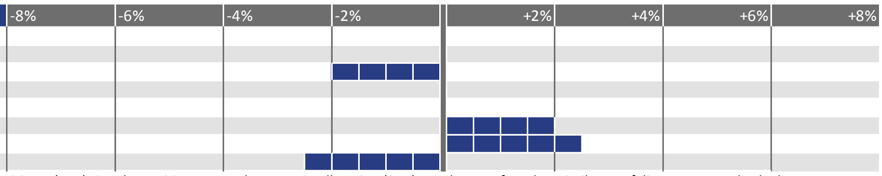
LGT Asset Allocation for Q3/2017 for a balanced model portfolio¹ managed by LGT Capital Partners

Overweight cash, emerging market bonds, equities, and Swedish krona. Underweight developed market bonds, high yield credit, and LPE.

	Asset class	SAA
Fixed income	Short-term investments	0.0%
	Global sovereign bonds	9.0%
	Inflation linked bonds	9.0%
	Investment grade corporates	9.0%
	High yield bonds	7.0%
	Emerging markets bonds	7.0%
Equities	Equities defensive	6.0%
	Equities North America	7.5%
	Equities Europe	4.0%
	Equities Japan	2.5%
	Equities Asia/Pacific ex Japan	2.5%
	Equities emerging markets	7.0%
Real	Commodity producers	3.5%
	Real estate (REITs)	4.0%
	Infrastructure	1.0%
Alternatives	Insurance linked strategies	5.0%
	HF CTA	8.5%
	HF equity long/short	1.8%
	HF event driven	1.0%
	HF relative value	1.8%
	Listed private equity	3.0%



	Currency[2]	SAA
Currencies	USD	88.0%
	EUR	0.0%
	CHF	0.0%
	GBP	0.0%
	JPY	0.0%
	SEK	0.0%
	Others (TAA vs. base currency)	12.0%
	Base currency	



Source: LGT Capital Partners. 1 Based on LGT GIM Balanced (USD). Tactical positions (TAA), i.e. the position versus the stratetic allocation (SAA), can be transferred to similar portfolios as a general rule, but investment restrictions or liquidity considerations may lead to deviations in implementation. 2 Position in other currencies (Others) is against base currency – in this case USD.