CIO View

Investment Traffic Lights

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Marketing material

Our monthly market analysis and positioning

Björn Jesch
Global Chief
Investment Officer

IN A NUTSHELL

- Sector rotation was one of the main themes last month, particularly on the U.S. equity market. The question now is whether this trend will continue or whether technology stocks will make a comeback.
- The mixed performance of equities contrasts with a very uniform trend on the bond market, with yields falling significantly on both sides of the Atlantic.
- Overweight gold, neutral assessment for oil.

1 / Market overview[1]

1.1 Sector rotation as one of the main themes on the stock market

Sector rotation was the big theme last month, at least on Wall Street, even though the trend only started in mid-July. After a nine-month market rally almost entirely driven by artificial intelligence (AI) and therefore very one-sided, but always up, investors finally started to diversify their equity positions beyond a few mega technology stocks. Easing inflationary pressures in the U.S., major developments in the U.S. election campaign and investor impatience that there isn't yet an "AI killer app" have served as excuses for a repositioning that is certainly still ongoing. In this context the rapid rise of the Russell 2000 stands out. As the U.S. small-cap index has a higher proportion of U.S.-based sales than the S&P 500, we also interpret this move as an initial pricing in of further U.S. corporate tax cuts in a possible Trump 2.0 presidency. But it should also be noted that the scope for a shift from taxes to more government debt issuance could be limited by a likely rise in bond yields, which in turn would put pressure on price/earnings multiples.

Not for the first time this year the major overarching themes in the markets were economic, with a particular focus on inflation and interest rates, and the U.S. election campaign, which took a new and dramatic turn with the withdrawal of Joe Biden. The U.S. inflation data release on July 11 showed the smallest monthly change in the core rate since January 2021 and provided further impetus for rate-cut hopes. And on the last day of the month Fed Chair Jay Powell's latest comments added to this optimism. However, we have also seen a rise in risk aversion. Geopolitics has returned to the forefront, with tensions rising again in the Middle East carrying the economic risk of rises in commodity prices, especially oil.

1.2 Mixed picture for equities, uniformly solid performance for government bonds

In the markets July can be summed up as a mixed month for equities, with yields on global government bonds falling sharply and broad commodity prices plummeting. It is particularly noteworthy that some European equity indices outperformed their U.S. counterparts. At the end of the month, the Dax was up 1.50%, while the EuroStoxx 50 was down slightly, by 0.43%. On

[1] All market data from Bloomberg Finance L.P. as of 8/1/24 unless stated otherwise.

the other side of the Atlantic, the S&P 500 ended July up 1.13% (helped in particular by the last trading day of the month), while the Nasdaq fell slightly by 0.75%. Sector rotation in the second half of the month resulted in the Russell 2000 outperforming the Nasdaq by the largest margin since February 2001.

Government bonds in the single currency area and the U.S., by contrast, all enjoyed a positive month. Yields declined across the maturity spectrum. This was mainly driven by a sudden revival of expectations of interest rate cuts by the European Central Bank (ECB) and the Federal Reserve (Fed), boosting short-term maturities in particular. Two-year Bund yields fell by around 30 basis points in July, while their Treasury counterparts fell by almost 50 basis points. The Bloomberg Commodity Index, which has been on a clear downtrend since June 2022, dropped further and faster in July, losing almost 4.5%.

2 / Outlook and changes

We made some minor tactical changes in July. Although the drivers of stock and bond market movements were varied, the focus in each segment was almost exclusively on what was in the mood of the moment: Big Tech dominated the equity market in the first half of the month, before the sector rotation set in. Bonds focused on expected interest rate cuts in the U.S. and the Eurozone. We are currently neutral on most segments and expect markets to move sideways overall, though there may be some strong short-term fluctuations.

2.1 Fixed Income

On the global bond markets, we assume that the current levels will be more or less maintained in the coming months. We do not expect massive swings in one direction or the other. In the U.S. in particular, yields continue to be driven by expectations of interest rate cuts by the Federal Reserve in the near future. After the Fed meeting on the last day of July, we think the door for a cut in September opened a little wider. But this is still far from a foregone conclusion and continues to depend on how inflation and other data evolve. In the Eurozone expectations for interest rate cuts by the European Central Bank may be a little exaggerated, in our view, but not by much.

Government Bonds

In the U.S. we have lowered our tactical view for two-year Treasuries from +1 to neutral. Here, too, the recent strong performance against the backdrop of the very optimistic Fed picture is the main argument - especially as the economic data, although still tending to be rather weak, now seems to have found a certain bottom. Ultimately, we assume that the U.S. central bankers are preparing a "soft landing" and do not see themselves having to prevent a rapid, marked economic downturn. We remain neutral on ten-year U.S. Treasuries.

In the Eurozone we are sticking to our neutral assessment for two- and ten-year Bunds. In the course of July, the bonds' performance was impressive here too so that yields appear to us to be tactically good for the coming months, though interim fluctuations cannot be ruled out, of course.

Corporate Bonds

European investment-grade corporate bonds have suffered a slight setback and we have raised our view again to +1. By contrast, we lowered our rating on high-yield bonds again to -1. Spreads on these bonds are already very tight and we believe the risk for this segment, both fundamental and political, are not now fully reflected in their prices: the risk/return ratio is not attractive at present.

In the U.S. the stance for investment-grade bonds has been left at -1, while we see high-yield bonds on the other side of the Atlantic as neutral. For bonds with higher credit ratings, we currently see little attraction in either the spreads or the yields on offer – spreads look too narrow.

Emerging Markets

We have become somewhat more cautious on emerging market government bonds and take a neutral stance on their future performance, albeit with a slight upward bias. We continue to judge the performance of the majority of issuers as extremely solid. In Asia we are sticking to our assessment of +1. Stable fundamentals and strong technical support have had a positive impact here and should continue to do so in the foreseeable future. We assume that spreads will remain tight and that investors will want to remain invested due to the attractive yields.

Currencies

In currencies we have reverted to a neutral assessment for the EUR/USD exchange rate as the greenback is holding up better again in an environment of increasing nervousness.

2.2 Equities

Within equities we have adjusted our tactical view on two sectors. Healthcare is upgraded to +1, while Communications is downgraded to neutral. In our view, healthcare should benefit from a continued sector rotation towards growth and innovation, beyond AI. A sector P/E premium of 10% versus global equities is in line with historical averages. However, unlike in previous U.S. election cycles, healthcare reform is not at the forefront of either candidate's policy agenda. U.S. biotech companies should also benefit from falling interest rates in the U.S., which will make their financing conditions more favorable.

Global communications services have outperformed by 18% since our upgrade in early 2023. The sector has served as a low-cost AI alternative to the IT sector (Neutral). Looking ahead, however, we believe that the AI train will only accelerate again if the mega-corporations show strong financial results and there is fresh evidence that the USD 150 billion plus in annual spending on new data centers is going to form soon the basis for new business models and revenue streams.

In the Industrials sector we maintain our neutral assessment but are more optimistic on two sub-sectors. The electrical equipment sub-sector is upgraded due to continued secular growth in electrification, driven by the path to net zero. We have also turned overweight on the transportation sub-sector to benefit from the cyclical recovery in the global economy.

U.S. Market

The reporting season on Wall Street is in full swing and has already brought the first surprises, both negative and positive. In particular, investors are asking themselves whether the big tech stocks, especially the Magnificent 7, will be able to continue to drive the indices up in the future. It also remains to be seen whether the sector rotation will continue and whether small caps will continue to be in demand – all of which is highly dependent on the expectation that Donald Trump will win the election because his tax policies are likely to favor smaller U.S. companies. We are sticking to our assessment of -1 and see the risk of a setback for U.S. equities in the short term.

European /German Market

The doomsday scenario for Europe has not materialized. Instead, the picture is not exactly rosy, but reasonable. Energy prices have fallen significantly from initial highs in 2022 but have picked up again recently. Consumers are still holding up better than expected and 2024 is likely to be the fourth consecutive year of positive earnings growth for retailers. The ECB has started to cut interest rates before the Fed and is expected to continue along the rate-cutting path. In some cases, European equities have outperformed their U.S. counterparts over the past few months, and we are maintaining our overweight view for the time being. The outlook for German equities is slightly more subdued and our stance is neutral. The fortunes of DAX companies reflect international factors and have long ceased to be a reflection of Germany, but they still have to deal with a number of domestic problems and disadvantages that also influence their share prices.

Emerging Markets

We are maintaining our neutral stance on emerging market equities. Overall, it can be said that the headwinds are becoming stronger. Some election results have disappointed the markets, the rather strong dollar and U.S. interest rates have remained somewhat elevated. The renewed rise in geopolitical risks is also not playing into emerging markets' hands at the moment.

Japan

The Japanese equity market has performed well in the past year. The weak yen is supporting Japanese export earnings, Japanese equities are increasingly seen as a good alternative to Chinese equities and foreign investors have reduced their strong underweighting. Corporate reforms and improvements in shareholder returns are driving the market. We would take advantage of the short-term weakness in selected stocks to build long-term positions, but we remain tactically neutral.

2.3 Alternatives

Gold

The price of gold rose to levels just below USD 2,500 in mid-July before a somewhat more significant setback. However, the precious metal currently seems to be trying to build up some momentum again. Gold’s fortunes are being determined by economic data, in the U.S. in particular, that still does not paint a consistent picture. Fed rate cut expectations are therefore also relatively volatile. We are, however, optimistic in the medium term and have a +1 (positive view) for gold.

Oil

The current trend in crude oil prices reflects a robust supply situation. OPEC (with Russia) is expected to implement its long-term plan to increase production. In addition, the market has currently only priced in a very low risk of a supply disruption. However, as the conflict between Israel and Hezbollah may be set to escalate, there is a risk that Iran could be drawn into a larger regional conflict. The effects of this on global supply are difficult to predict. Meanwhile, demand growth remains an important driver of investor sentiment and a soft China is a negative influence, with Chinese policy support measures gradual and unlikely to be felt for some time. Short-term volatility in oil prices therefore persists and we maintain our neutral stance.

Real Estate

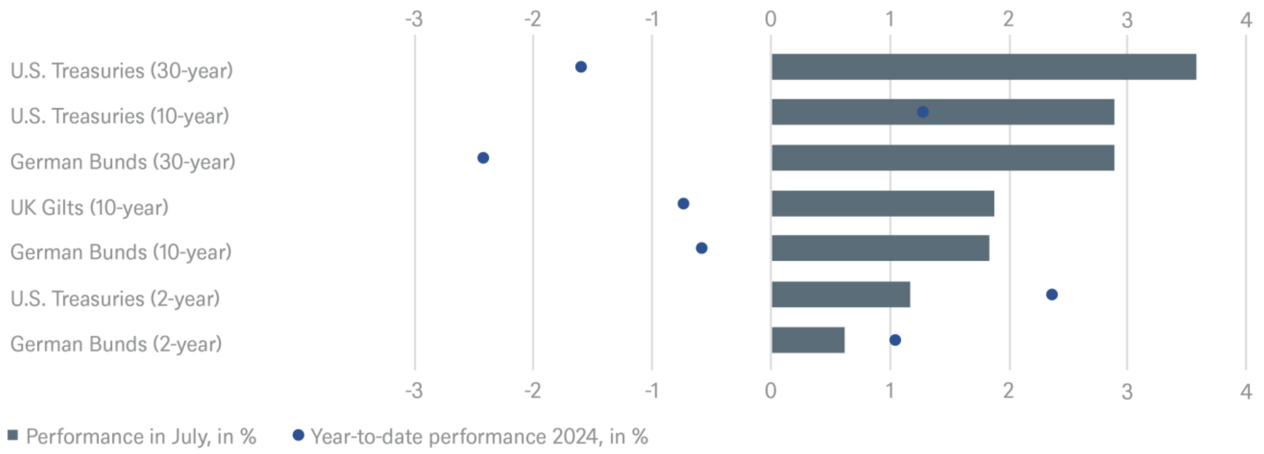
Property prices around the world have stabilized as interest rates appear to have reached a plateau. We believe that the real estate sector can still reap the benefits of the interest rate hikes of recent years, in that fewer construction projects are going ahead and yields are higher. Logistics and residential are among our preferred sectors in Asia, the U.S. and Europe. The environment for office and retail real estate is more nuanced, with both opportunities and risks worldwide. Our view remains neutral.

Infrastructure

In the infrastructure sector we expect transactions to pick up as interest rates fall, counteracting liquidity bottlenecks because of the difficulties of raising capital. The postponement of interest rate cuts and the resulting reluctance to bring new assets to market is now the most important factor in raising funds. Nevertheless, the picture should brighten in the medium term. The appetite for data centers, on the other hand, continues to grow. Additional AI-driven demand has further strengthened an already well-filled pipeline, but the continuing, growing demand for cloud storage and data sovereignty and the need to overcome capacity constraints are all factors that are likely to further increase demand for data centers. In the foreseeable future, however, we remain neutral.

3 / Past performance of major financial assets

Total return of major financial assets year-to-date and past month



Past performance is not indicative of future returns.
Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 7/31/24

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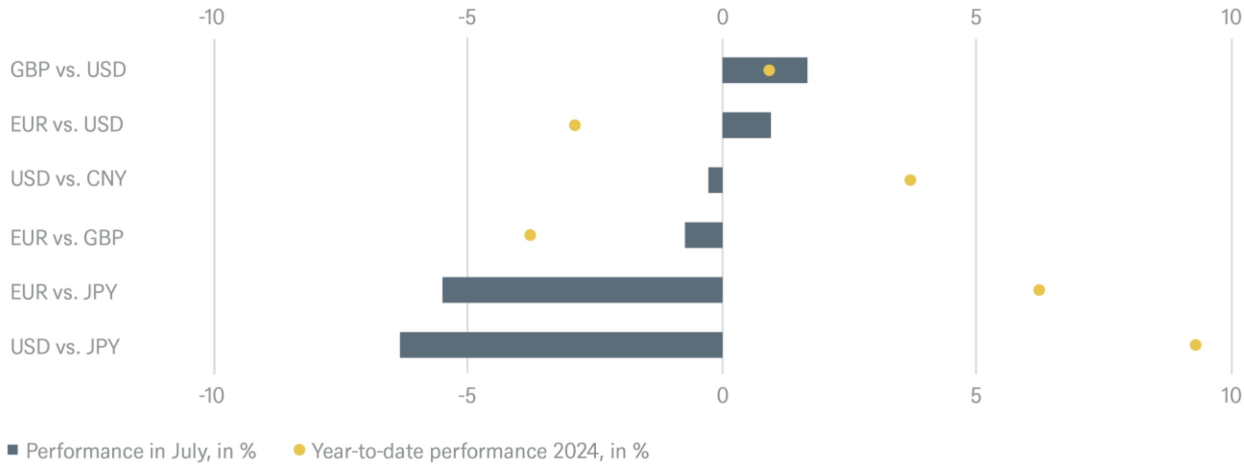

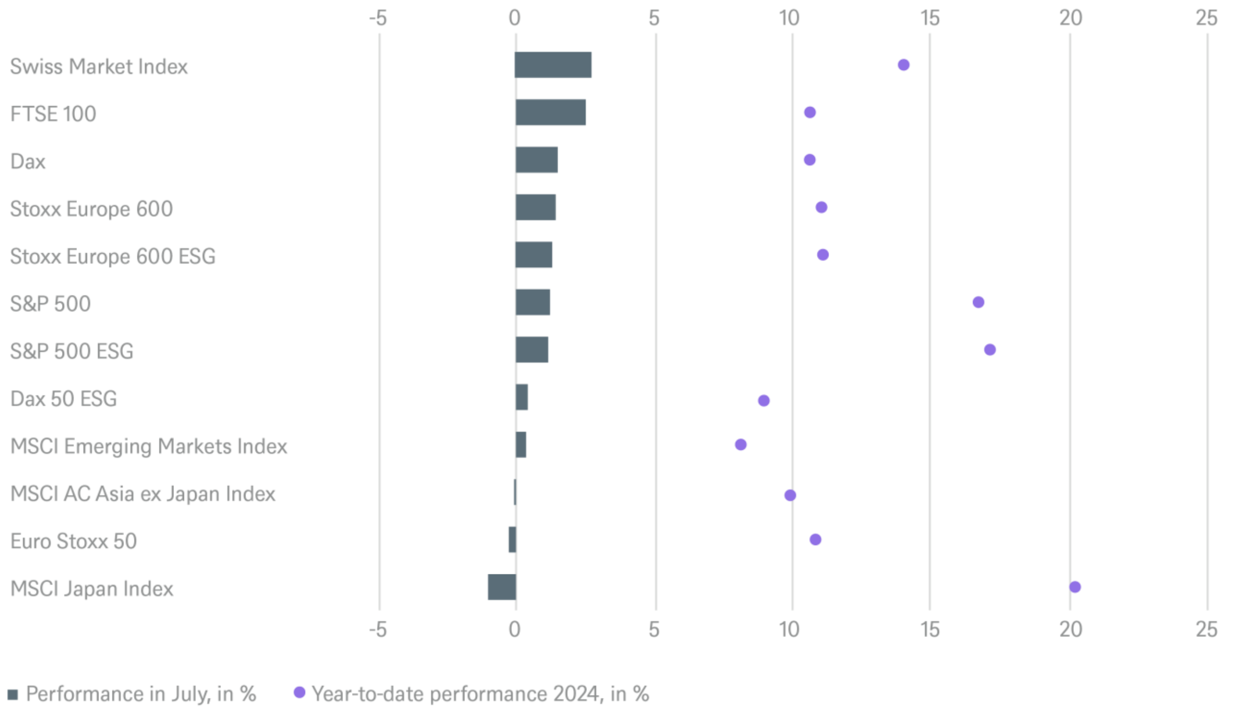

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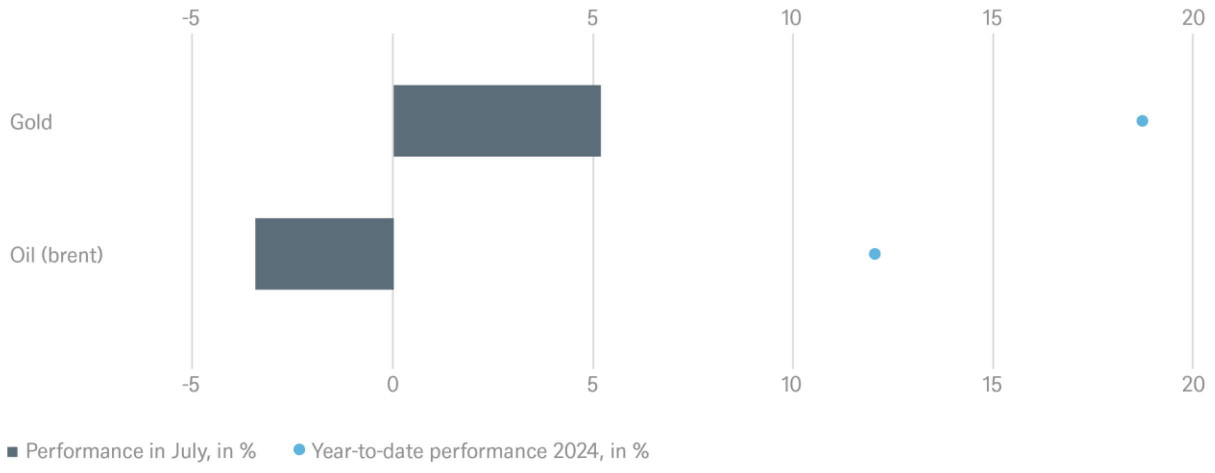

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4 / Tactical and strategic signals

The following exhibit depicts our short-term and long-term positioning.

4.1 Fixed income

Rates	1 to 3 months	through June 2025
U.S. Treasuries (2-year)	🟡	🟢
U.S. Treasuries (10-year)	🟡	🟢
U.S. Treasuries (30-year)	🟡	🟡
German Bunds (2-year)	🟡	🟡
German Bunds (10-year)	🟡	🟡
German Bunds (30-year)	🟡	🔴
UK Gilts (10-year)	🟡	🟢
Japanese government bonds (2-year)	🟡	🟡
Japanese government bonds (10-year)	🟡	🔴

Spreads	1 to 3 months	through June 2025
Italy (10-year)[1]	🟡	🔴
U.S. investment grade	🔴	🟢
U.S. high yield	🟡	🟢
Euro investment grade[1]	🟢	🟢
Euro high yield[1]	🔴	🟢
Asia credit	🟢	🟢
Emerging-market sovereigns	🟡	🟢

Securitized / specialties	1 to 3 months	through June 2025
Covered bonds[1]	🟡	🟢
U.S. municipal bonds	🟡	🔴
U.S. mortgage-backed securities	🟡	🟢

Currencies	1 to 3 months	through June 2025
EUR vs. USD	🟡	🔴
USD vs. JPY	🟡	🟢
EUR vs. JPY	🟡	🟡
EUR vs. GBP	🔴	🔴
GBP vs. USD	🟡	🔴
USD vs. CNY	🟢	🟢

4.2 Equities

Regions	1 to 3 months[2]	through June 2025
United States[3]	🔴	🟢
Europe[4]	🟢	🟢
Eurozone[5]	🟡	🟢
Germany[6]	🟡	🟢
Switzerland[7]	🟡	🔴
United Kingdom (UK)[8]	🟡	🟡
Emerging markets[9]	🟡	🟢
Asia ex Japan[10]	🟡	🟢
Japan[11]	🟡	🟢

Sectors	1 to 3 months[2]
Consumer staples[12]	🟡
Healthcare[13]	🟢
Communication services[14]	🟡
Utilities[15]	🟡
Consumer discretionary[16]	🟢
Energy[17]	🟡
Financials[18]	🟡
Industrials[19]	🟡
Information technology[20]	🟡
Materials[21]	🟡

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Style	1 to 3 months
U.S. small caps[22]	🟡
European small caps[23]	🟢

4.3 Alternatives

Alternatives	1 to 3 months	through June 2025
Commodities[24]	🟡	🟢
Oil (brent)	🟡	🟡
Gold	🟢	🟢
Carbon		🟢
Infrastructure (listed)	🟡	🟢
Infrastructure (non-listed)		🟡
Real estate (listed)	🟡	🟢
Real estate (non-listed) APAC[25]		🟡
Real estate (non-listed) Europe[25]		🟢
Real estate (non-listed) United States[25]		🟢

[1] Spread over German Bunds. [2] Relative to the MSCI AC World Index (only for the tactical signals),[3] S&P 500, [4] Stoxx Europe 600, [5] Euro Stoxx 50, [6] Dax, [7] Swiss Market Index, [8] FTSE 100, [9] MSCI Emerging Markets Index, [10] MSCI AC Asia ex Japan Index, [11] MSCI Japan Index, [12] MSCI AC World Consumer Staples Index, [13] MSCI AC World Health Care Index, [14] MSCI AC World Communication Services Index, [15] MSCI AC World Utilities Index, [16] MSCI AC World Consumer Discretionary Index, [17] MSCI AC World Energy Index, [18] MSCI AC World Financials Index, [19] MSCI AC World Industrials Index, [20] MSCI AC World Information Technology Index, [21] MSCI AC World Materials Index, [22] Russell 2000 Index relative to the S&P 500, [23] Stoxx Europe Small 200 relative to the Stoxx Europe 600, [24] Relative to the Bloomberg Commodity Index, [25] Long-term investments.

Tactical view (1 to 3 months)

The focus of our tactical view for fixed income is on trends in bond prices.

🟢 Positive view
🟡 Neutral view
🔴 Negative view

Strategic view through June 2025

– The focus of our strategic view for sovereign bonds is on bond prices.
– For corporates, securitized/specialties and emerging-market bonds in U.S. dollars, the signals depict the option-adjusted spread over U.S. Treasuries. For bonds denominated in euros, the illustration depicts the spread in comparison with German Bunds. Both spread and sovereign-bond-yield trends influence the bond value. For investors seeking to profit only from spread trends, a hedge against changing interest rates may be a consideration.
– The colors illustrate the return opportunities for long-only investors.
  – 🟢 Positive return potential for long-only investors
  – 🟡 Limited return opportunity as well as downside risk
  – 🔴 Negative return potential for long-only investors

Glossary

The core is a central or very important part of a region. In the context of the Eurozone, core refers to countries like Germany or France.

Artificial intelligence is the theory and development of computer systems able to perform tasks normally requiring human intelligence.

One basis point equals 1/100 of a percentage point.

The Bloomberg Commodity Index (BCOM) traces 23 commodities and reflects commodity futures price movements.

The Dax is a blue-chip stock-market index consisting of the 40 major German companies trading on the Frankfurt Stock Exchange.

Emerging markets (EM) are economies not yet fully developed in terms of, amongst others, market efficiency and liquidity.

The Euro Stoxx 50 is an index that tracks the performance of blue-chip stocks in the Eurozone.

The European Central Bank (ECB) is the central bank for the Eurozone.

The Eurozone is formed of 19 European Union member states that have adopted the euro as their common currency and sole legal tender.

Federal Reserve Bank is a regional bank of the Federal Reserve System, the central banking system of the United States. There are twelve in total.

The FTSE 100 is an index that tracks the performance of the 100 major companies trading on the London Stock Exchange.

High-yield bonds are issued by below-investment-grade-rated issuers and usually offer a relatively high yield.

Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.

Investment grade (IG) refers to a credit rating from a rating agency that indicates that a bond has a relatively low risk of default.

The Japanese yen (JPY) is the official currency of Japan.

Magnificent 7 is a name for the group of the 7 largest stocks in the S&P 500.

The MSCI AC World Communication Services Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Communications Services sector.

The MSCI AC World Consumer Discretionary Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Consumer Discretionary sector.

The MSCI AC World Consumer Staples Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Consumer Staples sector.

The MSCI AC World Energy Index captures large- and mid-cap securities across 23 developed-markets classified in the Energy sector.

The MSCI AC World Financials Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Financials sector.

The MSCI AC World Health Care Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Health Care sector.

The MSCI AC World Index captures large- and mid-cap companies across 23 developed- and 24 emerging-market countries.

The MSCI AC World Industrials Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Industrials sector.

The MSCI AC World Information Technology Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Information Technology sector.

The MSCI AC World Materials Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Materials sector.

The MSCI AC World Utilities Index captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Utilities sector.

The MSCI AC Asia ex Japan Index captures large- and mid-cap representation across 2 of 3 developed-market countries (excluding Japan) and 8 emerging-market countries in Asia.

The MSCI Emerging Markets Index captures large- and mid-cap representation across 23 emerging-market countries.

The MSCI Japan Index is designed to measure the performance of the large- and mid-cap segments of the Japanese market.

The Nasdaq Composite Index is an equity index which contains all common stocks listed on the NASDAQ exchange.

Net zero describes the achievement of a state in which greenhouse gas emissions due to activities within a company's value chain have no net impact on the climate. This is achieved by reducing greenhouse gas emissions in the value chain according to 1.5°C pathways, and by offsetting the impact of remaining greenhouse gas emissions through appropriate removals of CO_2.

The Organization of the Petroleum Exporting Countries (OPEC) is an international organization with the mandate to "coordinate and unify the petroleum policies" of its meanwhile 12 members.

The price-to-earnings (P/E) ratio compares a company's current share price to its earnings per share.

The Russell 2000 Index is an index that captures the 2,000 smallest stocks of the Russell-3000 index, which again comprises 3,000 small- and mid-cap U.S. listed stocks.

The S&P 500 is an index that includes 500 leading U.S. companies capturing approximately 80% coverage of available U.S. market capitalization.

A soft landing is when an economy's rate of growth slows in a controlled fashion without major disruptive effects on employment, external balances etc.

The spread is the difference between the quoted rates of return on two different investments, usually of different credit quality.

The Stoxx Europe 600 is an index representing the performance of 600 listed companies across 18 European countries.

The Swiss Market Index (SMI) is Switzerland's most important equity index, consisting of the 20 largest and most liquid large- and mid-cap stocks.

The U.S. Federal Reserve, often referred to as "the Fed," is the central bank of the United States.

Volatility is the degree of variation of a trading-price series over time. It can be used as a measure of an asset's risk.

Important information – EMEA, APAC & LATAM

Important information – North America

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