

## OUR MONTHLY MARKET ANALYSIS AND POSITIONING

The year-end rally has already started. Equity-market technicals continue to look supportive. Risks loom ahead, however, as we approach 2020.

### MARKET OVERVIEW

The year-end rally has already started. Everybody seems to be on board, and central banks continue to be happy to help. By starting a new mergers & acquisitions (M&A) spree, even corporates are doing their best to propel stock indices to ever new highs. Of course, investors are playing their part too. For much of the year, they have been "underinvested" in equities, as market jargon has it. Now, the hot money seems to be rushing to join the party, primarily for two reasons, first TINA (there is no alternative) or second her friend FOMO (fear of missing out). Looking at bond rates, one might understand those motives but wonder if none of the party guests are afraid of that party pooper ESRA (everything seems rather expensive). The U.S. yield curve was largely flat, with rates from one month to five years all at around 1.6%

November ended on a quiet note. U.S. equity-market volatility remained around the lowest levels in two years. There were some interesting earnings trends on both sides of the Atlantic. In line with stabilizing macroeconomic indicators for the Eurozone, it appears that corporate profits have steadied too. European earnings had the highest share of results beating estimates in ten quarters, albeit only compared to estimates that had previously been downgraded. That said, European earnings momentum appears to be (fractionally) above U.S. earnings momentum for the first time in nearly three years. This has mainly been due to U.S. earnings losing momentum; while improvements in Europe have been modest. Nonetheless, it is a pattern worth keeping an eye on. In the past, U.S. investors generally tended to give Europe a fresh look whenever Europe was able to deliver trailing earnings in line with or above those of U.S. peers. We may be getting close to that point.

Could things still go wrong in the remaining weeks of 2019? Of course they could! At their current levels, we believe all it would probably take for equity markets to experience another nerve-racking correction would be one bellicose trade-war tweet by the U.S. President. However, positive news

would have the opposite effect. It remains to be seen whether the hoped for de-escalation in the U.S.-Chinese trade conflict will materialize before Christmas. If it does, it would probably give markets another boost. Similarly, Brexit could well return as a risk. Markets have grown increasingly confident that the UK snap general election will produce a comfortable majority for Prime Minister Boris Johnson. In our view, investors may be underestimating the risk of another hung parliament and more months of Brexit delays. Set against such potential risks, however, are technical factors, suggesting many institutional investors may not wish to end the year without further increasing their equity exposure.

### OUTLOOK AND CHANGES

Looking further ahead, we are confident about the development of the global economy and capital markets in the coming year. Although growth might be significantly weaker in some regions, we do not expect a global recession. Contributing to this trend is an accommodative monetary policy from central banks and decreasing political uncertainties. Against this background, we expect the Dax to reach 14,000 points at the end of 2020. We believe the euro will continue to move sideways against the dollar to 1.15, but it is still too early to declare the end of the cycle for the greenback.

We do not expect a sudden rise in inflation, which is why both the U.S. Federal Reserve (Fed) and the European Central Bank (ECB) look set to continue their accommodative monetary policy and expand their balance sheets further. However, we do not see any further interest-rate cuts by either central bank, as such steps are unlikely to have any significant impact on the economy anyway. Monetary policy has reached its limits in this respect.

In 2020, global economic growth is expected to stagnate at 3.1%. For the United States, we think growth will slow down from 2.2% this year to 1.6% in 2020. For the Eurozone, we think growth will decline to 0.9% in 2020. We do not expect much in terms of effective economic stimulus programs.

Among the larger countries, only Germany could afford such measures, and the German government is already pursuing an expansive economic policy as judged by its own standards. In China, we do not expect a hard landing, with growth declining to 5.8% in 2020. Against this trend, we expect an acceleration of growth to 4.4% in emerging markets overall, which would account for 60% of global gross domestic product (GDP) in 2020.

Equity markets look well supported by loose monetary policies and a looming rebound in corporate-earnings growth. While the overall economy has avoided contraction, several industries have entered recessionary territories in 2019 with shrinking revenues and profits. This should make comparisons easier in 2020. Pent-up demand from delayed investment decisions should also modestly accelerate profits in the second half of 2020. Companies are adapting to the digitalization of their business processes and the secular prospects of a low-growth economy.

For the United States, we predict a 5% increase in earnings per share (EPS) for 2020, a 6% increase for Europe and a 9% increase for emerging markets. We believe the greatest upside potential will be for Europe and emerging markets as equity prices tends to follow earnings growth. Looking at individual sectors, we have underweights on equities from the real-estate and utilities sector, while overweighting securities from the IT and global financial sector.

As for bond markets, we expect yields to remain low for longer and investors will likely have to take greater risks to generate positive returns. Among sovereign bonds, we have tactically moved U.S. Treasuries back to neutral and we expect a rather low volatility environment until end 2019. German Bunds look set to remain range-bound. The first speech by Christine Lagarde, the new ECB President, was a bit of a non-event, merely emphasizing that the future monetary-policy strategy is under review and that a more stimulative European fiscal policy would make the ECB's task easier. Against this backdrop, we continue to like Italian and Spanish sovereign debt.

On a risk-adjusted basis, euro corporate bonds from issuers with investment-grade credit ratings currently appear particularly attractive. These securities appear to be benefiting not only from investors shifting funds into corporate debt because of negative yields on government bonds, but also from demand from the ECB's bond purchase programs. Corporate bonds from Asian issuers also appear to be ben-

efiting from investors' increased appetite for risk, especially as a great deal of downside is already priced into these securities. As for U.S. high yield, we note that a substantial amount of new issuance has to be digested. That's why we saw some softening in secondaries. We would want to see slightly wider spreads again before going long and thus stay neutral for the time being. On emerging-market corporates and sovereigns, we are also awaiting attractive entry points, as we remain constructive in the longer term.

## THE MULTI-ASSET PERSPECTIVE

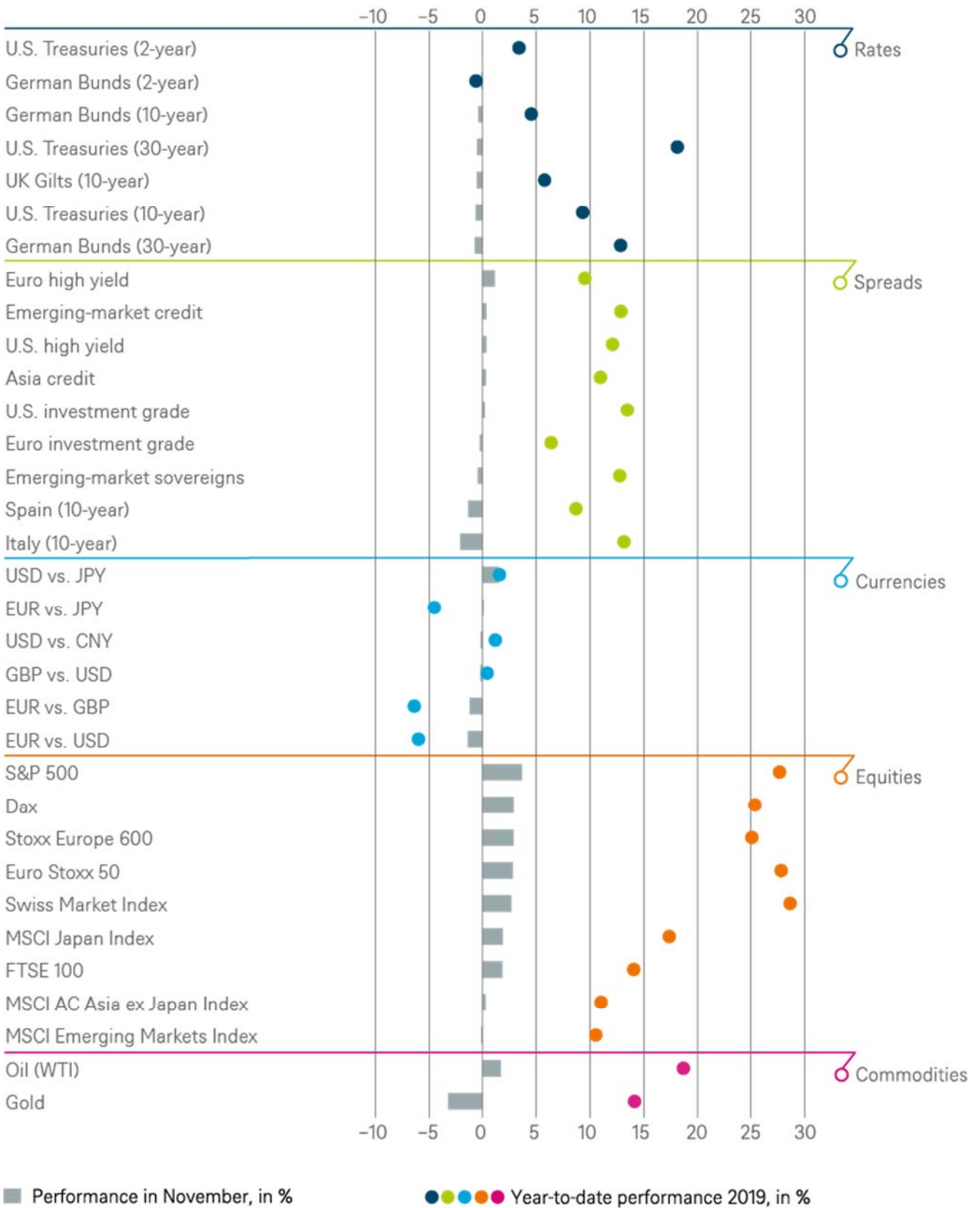
At the end of November, we downgraded the overall portfolio-risk appetite from a mild preference to a mild dislike. A mild dislike leaves sufficient flexibility to adjust equity risk in a more meaningful way if and when required. Clearly, markets have enjoyed another nice rally in the last couple of months on the back of less perceived political uncertainty. At the same time, the macro environment has stabilized somewhat.

Equity markets remain cheap compared to bonds. On a stand-alone basis, equities have reached new all-time highs lately and are getting more and more expensive. With regard to bonds, rate-cut expectations are no longer aggressive but largely priced out or delivered. Diversification benefits look better again with more negative correlation between equities and bonds. Market sentiment and positioning is now more neutral coming from a risk-aversion stance while growth expectations moved up quite strongly.

Overall, we acknowledge a slightly improving macro picture with markets having anticipated this one already and priced out major tail risks on the political front. A mildly cautious stance on overall risk seems appropriate at this point in time of the year, given the exceptional year-to-date cross-asset returns and room for disappointment given market pricing. Within equities, we have not upgraded emerging markets yet given prevailing political risks from Hong Kong protests and the trade conflict. Bond markets, however, seem to signal that investors may be underestimating various tail risks. This confirms our mild preference for duration; we expect range-bound trading in the very short-term. Apart from fixed-income duration, gold and Japanese yen remain potential diversifiers of choice.

## PAST PERFORMANCE OF MAJOR FINANCIAL ASSETS

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



Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 11/30/19

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## TACTICAL AND STRATEGIC SIGNALS

The following exhibits depict our short-term and long-term positioning.

## FIXED INCOME

Rates	1 to 3 months	until December 2020	Spreads	1 to 3 months	until December 2020
U.S. Treasuries (2-year)	●	●	Spain (10-year) <sup>1</sup>	●	●
U.S. Treasuries (10-year)	●	●	Italy (10-year) <sup>1</sup>	●	●
U.S. Treasuries (30-year)	●	●	U.S. investment grade	●	●
German Bunds (2-year)	●	●	U.S. high yield	●	●
German Bunds (10-year)	●	●	Euro investment grade <sup>1</sup>	●	●
German Bunds (30-year)	●	●	Euro high yield <sup>1</sup>	●	●
UK Gilts (10-year)	●	●	Asia credit	●	●
Japan (2-year)	●	●	Emerging-market credit	●	●
Japan (10-year)	●	●	Emerging-market sovereigns	●	●
<b>Securitized / specialties</b>			<b>Currencies</b>		
Covered bonds <sup>1</sup>	●	●	EUR vs. USD	●	●
U.S. municipal bonds	●	●	USD vs. JPY	●	●
U.S. mortgage-backed securities	●	●	EUR vs. JPY	●	●
			EUR vs. GBP	●	●
			GBP vs. USD	●	●
			USD vs. CNY	●	●

## EQUITIES

Regions	1 to 3 months <sup>2</sup>	until December 2020	Sectors	1 to 3 months <sup>2</sup>
United States <sup>3</sup>	●	●	Consumer staples <sup>12</sup>	●
Europe <sup>4</sup>	●	●	Healthcare <sup>13</sup>	●
Eurozone <sup>5</sup>	●	●	Communication services <sup>14</sup>	●
Germany <sup>6</sup>	●	●	Utilities <sup>15</sup>	●
Switzerland <sup>7</sup>	●	●	Consumer discretionary <sup>16</sup>	●
United Kingdom (UK) <sup>8</sup>	●	●	Energy <sup>17</sup>	●
Emerging markets <sup>9</sup>	●	●	Financials <sup>18</sup>	●
Asia ex Japan <sup>10</sup>	●	●	Industrials <sup>19</sup>	●
Japan <sup>11</sup>	●	●	Information technology <sup>20</sup>	●
			Materials <sup>21</sup>	●
			Real estate <sup>22</sup>	●
			<b>Style</b>	
			U.S. small caps <sup>23</sup>	●
			European small caps <sup>24</sup>	●

<sup>1</sup> Spread over German Bunds, <sup>2</sup> Relative to the MSCI AC World Index, <sup>3</sup> S&P 500, <sup>4</sup> Stoxx Europe 600, <sup>5</sup> EuroStoxx 50, <sup>6</sup> Dax, <sup>7</sup> Swiss Market Index, <sup>8</sup> FTSE 100, <sup>9</sup> MSCI Emerging Markets Index, <sup>10</sup> MSCI AC Asia ex Japan Index, <sup>11</sup> MSCI Japan Index, <sup>12</sup> MSCI AC World Consumer Staples, <sup>13</sup> MSCI AC World Health Care Index, <sup>14</sup> MSCI AC World Communication Services Index, <sup>15</sup> MSCI AC World Utilities Index, <sup>16</sup> MSCI AC World Consumer Discretionary Index, <sup>17</sup> MSCI AC World Energy Index, <sup>18</sup> MSCI AC World Financials Index, <sup>19</sup> MSCI AC World Industrials Index, <sup>20</sup> MSCI AC World Information Technology Index, <sup>21</sup> MSCI AC World Materials Index, <sup>22</sup> MSCI AC World Real Estate Index, <sup>23</sup> Russell 2000 Index relative to the S&P 500, <sup>24</sup> Stoxx Europe Small 200 relative to the Stoxx Europe 600

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## ALTERNATIVES

Alternatives	1 to 3 months	until December 2020
Commodities <sup>1</sup>	●	●
Oil (WTI)	●	●
Gold	●	●
Infrastructure	●	●
Real estate (listed)	●	●
Real estate (non-listed) APAC	●	●
Real estate (non-listed) Europe	●	●
Real estate (non-listed) United States	●	●

<sup>1</sup> Relative to the Bloomberg Commodity Index

## LEGEND

### 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 until December 2020

\_ 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 aim of an **accommodative** monetary policy is to support the economy by means of monetary expansion.

A **balance sheet** summarizes a company's assets, liabilities and shareholder equity.

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

**Brexit** is a combination of the words "Britain" and "Exit" and describes the exit of the United Kingdom of the European Union.

**Bunds** is a commonly used term for bonds issued by the German federal government with a maturity of 10 years.

A **central bank** manages a state's currency, money supply and interest rates.

A **correction** is a decline in stock market prices.

**Correlation** is a measure of how closely two variables move together over time.

The **Dax** is a blue-chip stock-market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange.

**Diversification** refers to the dispersal of investments across asset types, geographies and so on with the aim of reducing risk or boosting risk-adjusted returns.

**Duration** is a measure expressed in years that adds and weights the time periods in which a bond returns cash to its holder. It is used to calculate a bond's sensitivity towards interest-rate changes.

**Earnings per share (EPS)** is calculated as a company's net income minus dividends of preferred stock, all divided by the total number of shares outstanding.

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

The **euro (EUR)** is the common currency of states participating in the Economic and Monetary Union and is the second most held reserve currency in the world after the dollar.

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.

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

**Greenback** is a commonly used expression for the U.S. dollar.

The **gross domestic product (GDP)** is the monetary value of all the finished goods and services produced within a country's borders in a specific time period.

**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.

**Mergers and acquisitions (M&A)** are the two key methods of corporate consolidation. A merger is a combination of two companies to form a new company, while an acquisition is the purchase of one company by another in which no new company is formed.

**Monetary policy** focuses on controlling the supply of money with the ulterior motive of price stability, reducing unemployment, boosting growth, etc. (depending on the central bank's mandate).

**MSCI** is a company providing indices and other analytical tools for investors.

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 Real Estate Index** captures large- and mid-cap securities across 23 developed- and 26 emerging-markets classified in the Real Estate 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.

A **recession** is, technically, when an economy contracts for two successive quarters but is often used in a looser way to indicate declining output.

The **Russell 2000** 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.

**Sovereign bonds** are bonds issued by governments.

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

## GLOSSARY

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

The **Stoxx Europe Small 200** is an index representing the performance of 200 small capitalization companies across 17 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.

**Treasuries** are fixed-interest U.S. government debt securities with different maturities: Treasury bills (1 year maximum), Treasury notes (2 to 10 years), Treasury bonds (20 to 30 years) and Treasury Inflation Protected Securities (TIPS) (5, 10 and 30 years).

The **U.S. dollar (USD)** is the official currency of the United States and its overseas territories.

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.

**Yield** is the income return on an investment referring to the interest or dividends received from a security and is usually expressed annually as a percentage based on the investment's cost, its current market value or its face value.

A **yield curve** shows the annualized yields of fixed-income securities across different contract periods as a curve. When it is inverted, bonds with longer maturities have lower yields than those with shorter maturities.

## APPENDIX: PERFORMANCE OVER THE PAST 5 YEARS (12-MONTH PERIODS)

	11/14 - 11/15	11/15 - 11/16	11/16 - 11/17	11/17 - 11/18	11/18 - 11/19
Asia credit	2.7%	5.7%	5.4%	-1.9%	12.5%
Covered bonds	1.4%	1.3%	1.1%	-0.2%	3.7%
Dax	14.0%	-6.5%	22.4%	-13.6%	17.6%
EM Credit	-0.2%	8.6%	8.6%	-2.4%	14.1%
EM Sovereigns	0.2%	7.2%	10.9%	-4.8%	14.3%
Euro high yield	2.4%	5.8%	8.1%	-3.0%	8.7%
Euro investment grade	0.6%	3.2%	3.3%	-1.7%	6.5%
Euro Stoxx 50	11.6%	-9.4%	20.7%	-8.0%	21.1%
FTSE 100	-1.9%	11.1%	12.3%	-0.7%	10.1%
German Bunds (10-year)	3.2%	2.5%	0.4%	1.6%	5.1%
German Bunds (2-year)	0.4%	0.1%	-0.8%	-0.5%	-0.6%
German Bunds (30-year)	5.8%	6.6%	-1.3%	3.8%	14.5%
Italy (10-year)	6.7%	-1.6%	5.0%	-7.3%	17.6%
Japanese government bonds (10-year)	1.8%	2.1%	0.3%	0.1%	1.5%
Japanese government bonds (2-year)	0.1%	0.1%	-0.1%	-0.1%	-0.2%
MSCI AC Asia ex Japan Index	-10.6%	7.1%	35.2%	-9.6%	7.8%
MSCI AC World Communication Services Index	-9.8%	-3.9%	7.5%	-7.1%	12.2%
MSCI AC World Consumer Discretionary Index	4.3%	-2.3%	22.1%	-0.6%	13.2%
MSCI AC World Consumer Staples Index	-0.3%	-2.6%	15.8%	-4.6%	9.3%
MSCI AC World Energy Index	-18.9%	8.5%	3.0%	-3.1%	-6.0%
MSCI AC World Financials Index	-7.7%	3.7%	22.4%	-8.6%	6.3%
MSCI AC World Health Care Index	0.7%	-8.2%	19.9%	9.2%	7.4%
MSCI AC World Industrials Index	-3.5%	6.1%	22.0%	-7.0%	13.0%
MSCI AC World Information Technology Index	2.4%	7.3%	41.5%	1.0%	27.8%
MSCI AC World Materials Index	-17.4%	15.2%	23.6%	-11.6%	6.9%
MSCI AC World Real Estate Index	-5.1%	-1.5%	15.1%	-4.5%	11.5%
MSCI AC World Utilities Index	-12.5%	0.2%	20.1%	-3.7%	11.1%
MSCI Emerging Market Index	-17.0%	8.5%	32.8%	-9.1%	7.3%
MSCI Japan Index	7.6%	1.7%	24.3%	-6.0%	9.3%
Russell 2000	3.5%	12.1%	18.3%	0.6%	7.5%
S&P 500	2.7%	8.1%	22.9%	6.3%	16.1%
Spain (10-year)	4.7%	2.2%	4.2%	1.5%	9.5%
Stoxx Europe 600	14.5%	-8.1%	16.8%	-4.4%	18.3%
Stoxx Europe Small 200	21.8%	-6.6%	21.9%	-5.6%	19.7%
Swiss Market Index	1.3%	-9.2%	22.2%	0.3%	20.0%
U.S. high yield	-3.4%	12.1%	9.2%	0.4%	9.7%
U.S. investment grade	0.0%	4.2%	6.0%	-2.8%	15.2%
U.S. mortgage-backed securities	1.7%	1.6%	2.1%	-0.5%	8.0%
U.S. Treasuries (10-year)	2.0%	0.6%	2.2%	-1.6%	12.3%
U.S. Treasuries (2-year)	0.4%	0.7%	0.4%	0.8%	4.2%
U.S. Treasuries (30-year)	1.8%	1.2%	6.3%	-5.3%	24.6%
UK Gilts (10-year)	2.9%	5.2%	2.2%	2.0%	6.4%

Past performance is not indicative of future returns.

Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 12/2/19



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