Tactical positioning

February 2018 – market commentary

Increased exposure to European equities

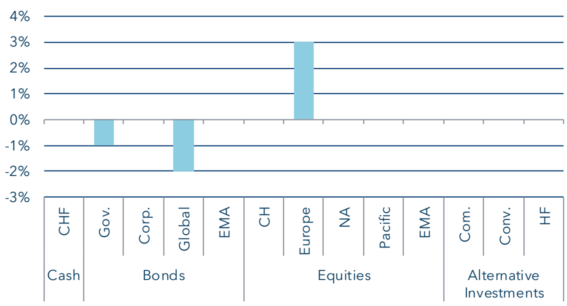
We pointed out last month that the strong equity market advances chalked up in 2017 were driven to a significant extent by continuing low interest rates. But buoyant economic data and rising inflation expectations are now pushing interest rates higher, and that has led to a sharp stock market correction. Nevertheless, we are still positive about the equity outlook and are increasing our exposure to European stocks while staying underweight in bonds.

Upbeat macro data are usually good for equities. But US money markets are now anticipating a steeper climb in key interest rates. The abrupt way in which further rate hikes by the Fed have been priced in on the futures markets has taken equity investors by surprise, resulting in sharp corrections on world stock markets.

We explained in January that we expected US interest rates to move up. Even so, we regard the current stock market setback as an overdue correction rather than the start of a long-term change of trend. So far we see no reason to believe that market turbulence will impact on the economic environment. The dynamism of the global economy remains intact.

We are therefore adjusting our assessment of European equities and raising our exposure to this sector from neutral to overweight. We expect the environment to stay supportive of European stocks. Moreover, rising interest rate expectations in the US should favour the US dollar versus the euro. In the bond markets we expect a moderate backup of yields and are sticking to an underweight position.

Tactical positioning



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Head of Investment Management

Asset allocation

- Equities overweight; bonds underweight
- Alternative investments neutral

Bonds

- Government bonds underweight
- Global bonds underweight

Duration is being kept below benchmark in all reference currencies. We are underweight in government bonds and global bonds and neutrally weighted in emerging market and corporate bonds. We hold a position in inflation-linked bonds.

Equities

- Overweight European Equities

Rising interest rate expectations in the US have resulted in a sharp correction on the world's equity markets. We continue to regard the economic environment as positive and see the current setback as an overdue correction rather than heralding a long-term change of trend. Rising US interest rates should favour the US dollar versus the euro. Relative valuation levels also continue to argue in favour of European equities.

Alternative investments

- Commodities neutral
- Convertible bonds and hedge funds neutral

Currencies

We remain strategically hedged in developed country currencies in order to minimise risk. The USD is partly unhedged in EUR and CHF based portfolios.

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