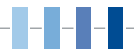
CBH Compagnie Bancaire Helvétique

Quarterly Insight

2018 OUTLOOK



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Imprint

Publication date : December 29, 2017
Prices as of : December 29, 2017

ALLOCATION MONITOR

Total	Asset class	Sub-class	BENCHMARK ALLOCATION	Currency	CBH GROUP STRATEGIC ALLOCATION (Underweight / Neutral / Overweight)	Chg
9.5%	Cash	Libor 3m	5%	USD	7%	
		Euribor 3m		EUR	12%	
47.5%	Government	1 - 5 years	10%	USD	4%	-2%
				EUR	1%	-3%
		5 - 10 years	10%	USD	4%	-2%
				EUR	4%	
	Corporate Inv. Grade	1 - 5 years	15%	USD	13%	-2%
				EUR	11%	5%
		5 - 10 years	10%	USD	6%	-2%
				EUR	6%	
	Corporate High Yield	1 - 5 years	5%	USD	5%	-3%
				EUR	5%	-3%
		5 - 10 years		USD	0%	
				EUR	0%	
	Emerging markets	Hard currency			6%	1%
		Local currency			2%	
	Others	Senior loans			2%	
		Convertible			8%	
36.0%	Equities	North America	15%		15%	2%
		Europe	13%		9%	-2%
		Japan	4%		2%	-2%
		Asia Pacific (ex-Japan)	4%		5%	1%
		China	2%		2%	
		Emerging Markets	2%		3%	
0.0%	Precious metals	Gold	2%		0%	
7.0%	Other investments	Other investments	3%		7%	4%

ALLOCATION COMMENTARY

With continuous and unusual central bank's interventions as well as external political events, to foresee what will happen in 2018 remains a challenging exercise.

Compared to our Strategic Asset Allocation (SAA), and despite recognizing some red flags arguing in favor of a conservative approach, we maintain a constructive aggressive Tactical Asset Allocation (TAA). Indeed, despite a slight underweight in the equity exposure (36% vs 40% for the benchmark), we strongly overweigh risky investments on the bond universe, where we favor High Yield, Emerging Market (both in hard and local currencies) and Convertible bonds. Our TAA has therefore an ex-ante Value at Risk that is slightly higher than the one of the benchmark, but given our low duration positioning and yield cushion, this is seen as an affordable risk.

For our global bond portfolio, we continue to underweigh government bonds and investment grade corporate bonds denominated in euros, a region where we favor the segment of high-yield short dated bonds. In dollars, yields are slightly higher, which allows us to adopt a more constructive bond allocation for US dollar portfolios where we can invest all over the curve and in all segments of the universe (Govies, IG and HY).

In our quest for positive returns, we continue to favor crossover bonds (rated BBB- and BB-), emerging bonds denominated in hard currency and convertible bonds which, although riskier, display an appealing risk / return ratio. We also continue to advise the lower capital structure (subordinated bonds) of companies having strong balance sheets and dominant market positions and favor in this segment large financial institutions. For all these asset classes, we recommend investors to favor global diversified instruments such as mutual funds and exchange traded funds (ETF).

On the Equity side, we maintain a global underweight given the level of risk taken in the bond spectrum. From a geographical point of view we are more conservative in Europe and Japan, neutral in North America and we favori the Asian region and Emerging Markets. At the sector level we continue to see value in large technological companies as well as the financial sector.

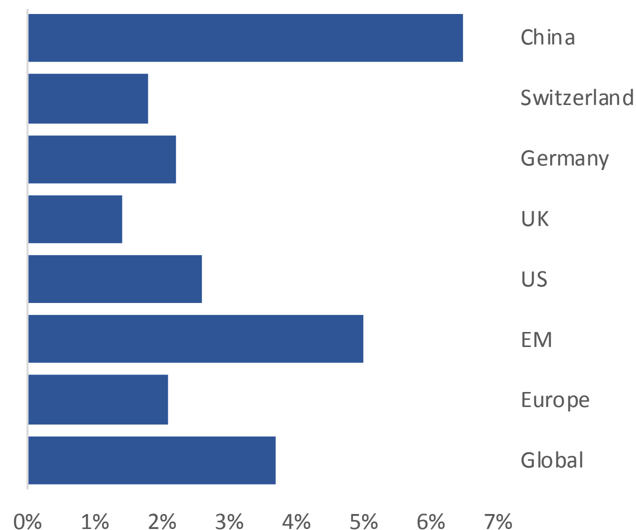
In commodities, we continue to keep a fundamentally negative view in gold, and wait for lower prices in order to tactically open long positions, and have a neutral to mildly positive view in Energy.

MACROECONOMIC OUTLOOK

Our macroeconomic outlook is constructive. We expect the global economic expansion to continue in 2018. With major economies at different stages of the business cycle, the risk of the global economy running too hot is actually limited, but could become a more important risk later in 2019-2020. Even if unemployment rates should continue to fall and output gaps keeping closing, key capacity utilization metrics should remain well below their typical cyclical peaks, even in the US. The global economic growth rate is therefore expected to accelerate marginally in 2018, to 3.7% based on consensus forecasts. EM countries should continue to exhibit a stronger growth outlook compared to DM world.

GDP expectation

Source: CBH



In DM, the US should continue to exhibit a stronger growth outlook compared to the Old Continent. The US economy is expected to grow 2.6% based on consensus expectations and the FED upgraded its forecast to 2.5% during the last meeting. Unemployment has fallen lower in 2017 (4.1%) and this year the FED expects it to fell to 3.9%. Inflation, which remains low at 1.7%, is expected to gradually converge to the 2% long-run target. This means that consumption is expected to hold up well in future quarters. Moreover, the recently enacted fiscal package, which will result in lower taxes, should help sustain economic growth via higher disposable incomes, and potentially greater corporate investment spending.

In Europe, economic growth should also continue expanding at an above 2% rate in 2018. Latest December flash PMI displayed several multi-year and even record highs for Eurozone countries. The upturn is led by the manufacturing sector, with its PMI rising to very elevated highs of 60.6, 63.3 and 59.3 for the Eurozone, Germany and France respectively. Monetary policy is expected to remain largely dovish in 2018 and this will sustain the economy. DM real interest rates should stay deeply negative and well below their natural equilibrium levels. Global excess liquidity is still expanding and financial conditions are considerably easier than they usually would be at this stage of the cycle. Only the Federal Reserve will actually shrink its balance sheet and engage in active quantitative tightening. All other key central banks (especially the ECB and the BoJ) will likely expand their balance sheets, but at a slower pace. Therefore, with ongoing monetary policy support, easy financial conditions, and rising confidence, the positive feedback loop fueling global growth is operating powerfully in the Euro area and is expected to continue in 2018. That said, over the longer term, we continue to see some structural bottlenecks hindering stronger growth, like rigid labor market, high (peripheral) debt levels and a still fragmented EU framework.

In Japan, the economy is currently marking its longest growth streak in 16 years supported by stronger global demand. GDP has been growing for seven straight quarters with unemployment rate declined to 2.8%, the lowest level for more than 20 years. Nevertheless, both wage growth and inflation remain slow. In 2018, growth is expected to remain positive (+1.3%), but still softer than in other regions. December flash PMI was strong and confidence has improved, also thanks to dovish monetary and fiscal policies. Solid global growth and the rise in Japanese companies' profit should support growth going ahead. However, anemic increases in the wage per worker and persistent concerns about future income appear to weigh on the consumption trend and this is likely to be the case also in 2018.

Finally, EM growth outlook is expected to strengthen further in 2018, with the real GDP growth rate approaching the 5% threshold. EM seems to be in a goldilocks scenario. EM economies are generally earlier in the economic cycle compared to DM and are fully enjoying from the recovery in global trade. This is especially evident in Asia, whose economies are more tilted on exports. Moreover, commodity exporters have also seen an improving macroeconomic environment, which should further strengthen in 2018, also thanks to the reforms adopted in the past. This positive macroeconomic and reform momentum should be reflected in a stronger domestic demand. At the regional level, we expect Asia to remain the leading region in terms of growth dynamics, followed by Latin America and EMEA. Latin America is likely to be the region showing the stronger sequential improvement in growth compared to 2017, driven by a stronger rebound in Brazil. Elections and geopolitical risks could led to periods of increased volatility, also taking into consideration the heterogeneity of EM countries, but we don't foresee a major negative event in 2018.

On the policy front, we expect the FED to continue normalizing gradually its monetary policy. The FED is guiding for three more rate hikes in 2018 (target median: 2.1%), at least two in 2019 (2.7%) and two more in 2020 (3.1%), with the longer term target FED rate at 2.75%. The FED will also reduce the size of its balance sheet. Other major central banks (ECB, BoJ) will however refrain from following the FED and keep ultra-loose monetary policies unchanged. While we expect a number of smaller central banks to raise rates next year, these moves should be quite modest. In fact, strong global growth should enable the FED keeping its gradual normalization path.

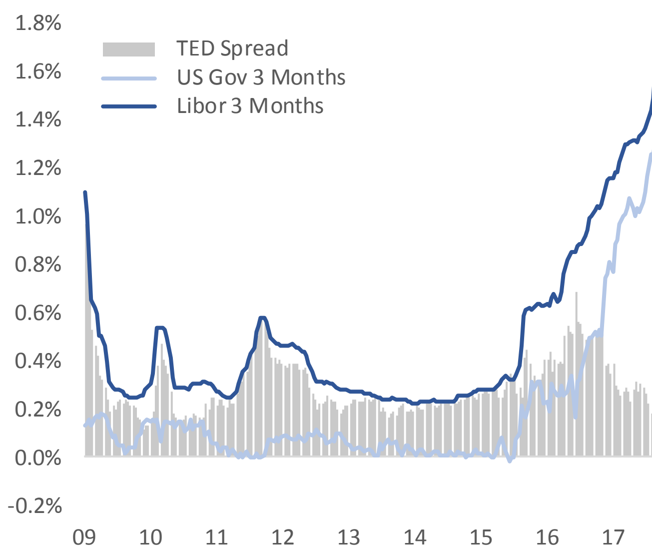
At the same time, low policy rates and balance sheet expansion outside the US tempers upward pressure on global bond yields, supporting favorable financial conditions in the face of Fed rate normalization. If these views prove to be rights, central banks' patience elsewhere will be tested. Next year's global backdrop will increase pressure on a wide range of central banks currently signaling a very gradual normalization path.

A point that could exercise some volatility in the future is the composition of the board of the FED. Donald Trump nominated Jerome Powell as new chairman of the FED. The chairman adopted a message of policy continuity, even if he clearly privileges a looser approach to banking system regulation. Trump has so far chosen two new members for the seven-member board and he has the possibility to nominate three more, including the FED vice chairman. This could put some clouds on the real independence of the central bank and some observers are questioning if the new board will really follow the gradual normalization path put forward by their predecessors.

By contrast, the ECB cautioned patience in the face of robust growth, reiterating its "well past the horizon of our net asset purchases" rhetoric that guides toward a first rate adjustment in 2019. In fact, for the Fed and the ECB, accommodative policy stances in the face of forecasts of tight labor markets reflect persistently low core inflation, which is one of central banks' main objectives. However, we think that strong global growth will bolster global goods pricing power and push the global economy beyond current estimates of full employment. However, if these forecasts are right other central banks will be motivated in a similar way and rate normalization will gain traction elsewhere in 2018. We therefore expect that the ECB will start preparing the market during the second half of 2018 for a first interest rate increase in late 2019. Moreover, if the economy will continue to recover, we expect the ECB will start scaling back its QE program in September 2018.

TED Spread

Source: CBH, , Bloomberg Financial L.P.



Finally, in Japan, the central bank's balance sheet is on track to become larger than the size of the overall economy. The BoJ continued its accommodative monetary policy throughout 2017 by controlling the yield curve to maintain its 10-year yields at around zero percent in addition to upholding its asset purchase programme by being an active buyer of ETFs in the equity market. Although this policy may be unsustainable in the longer term, we do not anticipate any change in 2018.

The BoJ is targeting an inflation rate of 2%, but this is a still distant prospect. Even with the adoption of "Abenomics" reforms, which have also resulted in an ultra-expansive fiscal policy, this goal is still difficult to reach. With PM Abe's success during the snap election in October 2017, we expect him to be re-elected as the leader of the LDP in 2018 and Kuroda to continue servicing as the Governor of the BoJ. As such, we anticipate both monetary and fiscal policies to be negative for the Yen, but remain favorable for corporate earnings and the Japanese economy for 2018.

FIXED INCOME

Turning to fixed income markets, we think 2018 will be a more challenging year compared to 2017. The FED is expected to continue to normalize its monetary policy and is signaling three interest increases in 2018, with a final “FOMC dots” median target at 2.125%. Other major central banks will likely maintain ultra-loose monetary policies, but with yields already at very depressed levels and a continuation of the economic recovery, it’s difficult to expect yields will fall much lower from current levels. Instead, risks seem to us more tilted on the upside.

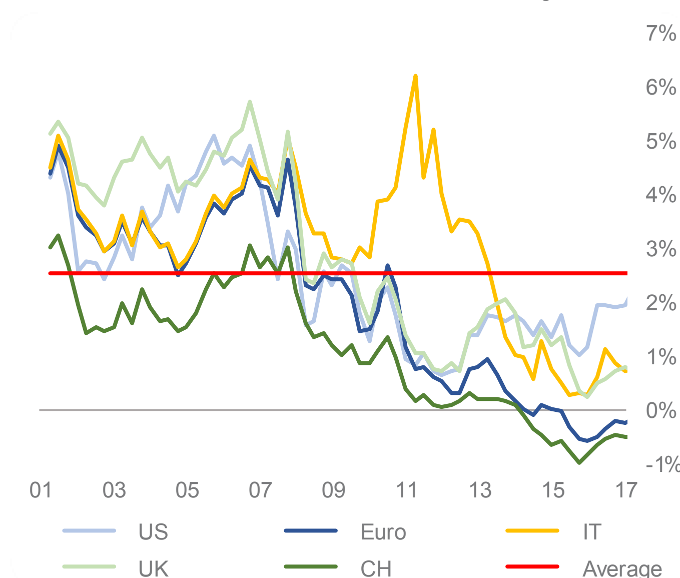
This is why we continue to keep an underweight exposure on government bonds, especially European ones, which are strongly distorted by the ECB quantitative easing. Short term government bonds will be negatively impacted by the reduction in monetary easing and increasing interest rates. Long term government bonds should also be negatively impacted, but in some cases can benefit from a flattening of the yield curve (see US). This could permit to implement some “barbell” strategies in government bonds.

In the US, consensus forecasts foresee 2Y US government bond yields at 2.34% at the end of 2018 (up 45bps from current levels) and 10Y US government yields at 2.88% (up 44 bps), resulting in a further “bear flattening” of the government bond yield curve. This is in contrast with market expectations in Europe. Germany 2Y yields are expected to increase to -0.42% (up 21bps) and 10Y Bund yields are expect to rebound to 0.89% (up 45bps), resulting in a “bear steepening” of the German yield curve. This different behavior is also the consequence of the different economic cycle stage that the two economies are enjoying, with the US already advanced in the economic recovery compared to Europe.

There is a huge debate in the market concerning the shape of the US government yield curve. Historically, a flattening yield curve was the precursor of some major growth weaknesses or a recession over the coming year. For example, a sharp flattening preceded the financial crisis and Great Recession in 2008. We think this time is different, at least in the short-to-medium term, because actual monetary conditions are extremely different to those prevailing in the past. First, looking at the macroeconomic environment, there are no clues indicating an imminent slowdown, nor is the economy in an overheating situation. That should not be surprising, however, that with the unemployment rate sitting at its lowest levels since the turn of the century, we are closer to the end of this business cycle rather than the beginning. We think the probability of a recession is much more important in 2-3 years from now. Second, we think today’s situation is more akin to the curve flattenings in 1994 and 2004, because they both followed extended easing campaigns. In addition, slowing economic growth is typical of late-cycle dynamics and consistent with a flatter curve. Finally, the increase in Treasury’s financing needs will likely be met mostly with increased issuance in the front to intermediate sector of the curve, which should also be supportive of a flatter curve. This is one of the reason why in our asset allocation we have a more important underweight position in short dated government bonds compared to longer terms one.

Passing to credit markets, we think the environment will be much more difficult compared to 2017. In fact, we consider that the potential for further spread compression is limited and instead we see higher risks of a mild spread widening going ahead. We believe that even if fundamentals are improving, much of this improvement is already priced in current valuations. In our view, investment grade (IG) spreads are likely to consolidate near current levels, but are at risks of widening, especially if central banks’ support should be withdrawn faster than currently expected. In fact, central banks’ policies have pushed valuations at levels much more expensive compared to current growth rates in Europe and the US. A swifter reduction of this support would therefore result in a widening in spreads, even if fundamentals remain strong. In a fixed income portfolio, we would also approach investment grade corporate bonds using a barbell strategy. We would target a moderate duration stance (between 3 and 5 years) using a mix of floating rate notes, short duration bonds and much longer duration (7-10 years) bonds. We think that high quality perpetual bonds of strong issuers could also enhance yield of the portfolio without adding too much risks.

5 YEARS INTEREST RATES
Source: CBH, Bloomberg Financial L.P.



High yields (HY) have also reached very expensive levels, especially in Europe, with spreads trading near all-time lows. Yields have little to no room for price appreciation and global central banks are expected to move further away from the dovish policy spectrum. Rates should remain in focus for investors amid prospects for firmer global economic conditions, higher deficits, a rise in inflation expectations, and possibly a more active Fed. Nevertheless, improving consumer and corporate confidence, united to the US tax reform, should aid momentum in the US economy and corporate earnings. Default rates are also expected to remain low in 2018. Finally, compared to other asset classes, HY bond yields and spreads carry reasonable relative value. However, considering all the above, we prefer erring on the cautious side and scale back our exposure on HY to neutral levels. In fact, especially in Europe, valuations are no more compelling and don't provide enough cushion on potential unexpected negative news. It's always difficult to estimate when market momentum may change, and an unanticipated accident could easily tip sentiment decisively into bearish territory considering current valuation levels and investors' positioning. In conclusion, we advise investors to take some further profits, to be selective in their credit allocation and to reduce credit and duration risks in the HY.

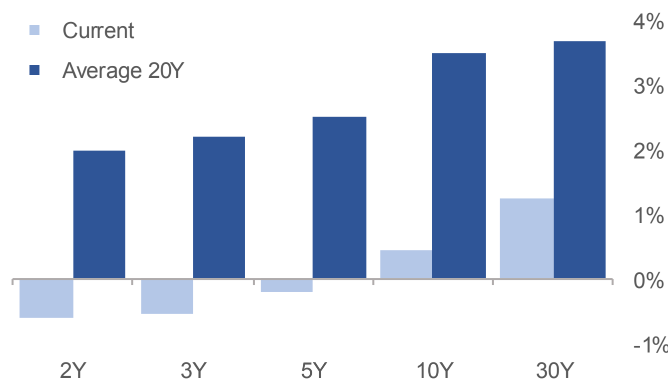
Our preferred fixed income sector remains Emerging Markets (EM). We especially like hard currency debt over local currency. We also prefer being exposed to the corporate sector over the government sector. Our bullish stance on EM bonds is corroborated by two key factors: 1) EM valuations remain attractive on a relative basis and 2) Global macro conditions remain supportive for EM, in particular due to a strengthening global recovery and improving fundamentals. EM continues to offer attractive pick-up over core market yields, though there has been a meaningful spread compression since February 2016. For EM hard currency debt, we see some further spread compression likely, as the positive adjustments in EM fundamentals and attractive relative valuations mean EM credit can digest the gradual repricing in core rates. In terms of regions, we think the best value lies in Latin America, followed by Asia and EMEA. For local currency EM debt, valuations are by far the cheapest, with yield differentials over US Treasuries currently near 400bps (JPM GBI-EM). Improving fundamentals should continue to attract investors' interest into this asset class. Even though inflation is expected to move higher in 2018, it is coming from low levels and, since most economies still have relatively wide output gaps, it is possible to absorb an uptick in inflation without creating excessive tightening pressures. Moreover, the relative value argument in favor of local markets is striking for real yields, where the EM/DM differential is high. A stable to softer USD could also give a positive impetus to the asset class.

In conclusion, we think that EM bonds will be one of the most attractive fixed income sectors in 2018. To play this heterogeneous asset class, we advise investor to use dedicated investment funds, which will permit to guarantee the necessary diversification and adopt an active asset allocation strategy.

Finally, looking at less traditional fixed income strategies, we continue to like and overweight convertible bonds and US senior loans. The former is likely to capture the "best of the two worlds": the upside potential of equity markets, with the protection provided by the bond floor. The latter will instead profit from the current recovery in the global economy, giving investor a juicy yield, but providing protection against higher interest rates thanks to their floating rate nature.

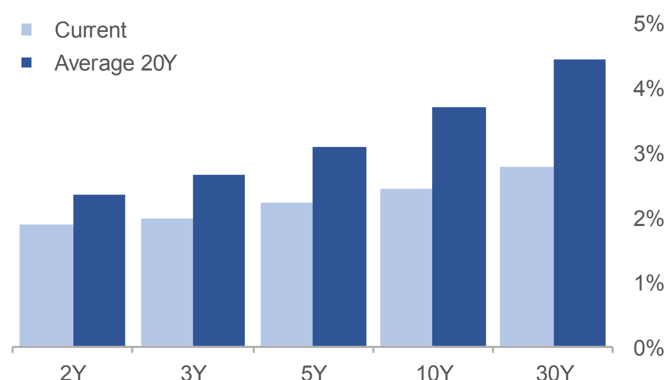
GERMAN INTEREST RATES

Source: CBH, Bloomberg Financial L.P.



UNITED STATED INTEREST RATES

Source: CBH, Bloomberg Financial L.P.



EQUITIES

In this environment, we think equity markets should remain well supported. We don't expect a replay of this year strong rally, because most of the positive newsflows is already priced in. Moreover, valuations are now more expensive compared to last year. That said, the positive global macroeconomic backdrop should remain a strong pillar of future performance, sustaining consumption and companies' earnings. Furthermore, even if valuations are no more compelling compared to the past, equity risk/return potential remains much more interesting compared to those of government bonds and credits. Therefore, we think that high single digit performance could be achievable for global equities in 2018, but the better performance period is likely to be in the first half.

MSCI USA vs P/E RATIO

Source: CBH, Bloomberg Financial L.P.

We stay positive on equities for now as the global macro backdrop is likely to remain supportive over the coming months. However, as the year progresses, a number of factors that have provided oxygen for the markets in recent years will likely reverse. At that point, we expect market volatility to pick up and lead to a more marked equity drawdowns at some point. This is where we would judge if it is the right time to increase more markedly our equity allocation.

In the DM, we continue to privilege US equites over EU ones. The recently enacted US tax reform bill should have positive repercussions on the US economy and financial markets. Moreover, pro-growth policies and a potential partial implementation of the infrastructure agenda proposed by president Trump will clearly have a positive impact on equities. In fact, investment activity should be driven by rising profits, cash repatriation and declining policy uncertainty. US seems also more able to benefit from the continuing “IT revolution” thanks to the higher share of companies operating in the US compared to other DM countries. Business spending on tech products and services should also remain well supported as companies continue to invest in new technologies to boost productivity. Over the longer term, the major challenge that politicians will have to resolve is the ever increasing disconnect between increase in productivity and increase in labor compensation. Until the 70's, these two metrics moved in tandem. This is no more the case and the only real beneficiaries of productivity improvements are business owners and investors. Capital is gaining against labor and this is particularly evident looking at the evolution of global wealth distribution. Wealth inequalities are increasing at the worldwide level, especially in Anglo-Saxon countries, and we believe this is unsustainable over the long term.

In terms of sectors and themes, we therefore think that the IT sector should continue to lead the market and could again register double-digit performances in the future. We believe that we are only at the beginning of this secular trend and more opportunities will appear in the years to come. Companies like Nvidia, Qualcomm, Google, Amazon, only to name a few, are likely to continue shaping this IT revolution and attract investors' interest. Any material correction, like the one that happened during the last months of 2017, will be considered as an opportunity to increase positions in these sectors/companies. Social network companies (like Facebook) should also benefit from the development in EM, which should remain positive.

Other sectors, like the automotive one, are also profiting from this technological revolution. Automotive companies are using an ever-increasing share of technological components in order to boost performances, lower emissions and increase safety. In this sector, we like companies such as VW, BMW and Daimler.

In the US, companies with high tax rates should also benefit from the US tax reform and this is a theme we are playing in our investment funds. In addition, financial stocks will also likely benefit not only from the US tax reform, but also from the normalization of the monetary policy, which should permit to increase their margins. Moreover, changes at the helm of the FED are likely to permit to adopt a less string regulation for financial institutions.

In Europe, we also expect equities to enjoy from the economic growth revival and relatively undemanding valuations. However, we don't believe European equity markets will be able to catch up with their US peers. Even if Europe is cheaper compared to the US, this has always been the case in the past. Moreover, in contrast to the US, the EU growth rate is expected to slow. Furthermore, we think that European equity markets could suffer if the recent strengthening of the EUR should continue in the future. It's difficult to envision that Europe could outperform the US in a strengthening Euro environment. Finally, lower European bond yields should also have a negative effect on financials, compared to their overseas competitors, because margins will be structurally lower. Considering the important weight of financials in EU equity indices, this could be a negative phenomenon. On the positive side, Europe's economic cycle is lagging the US one and some more pent up demand could appear in the future. Moreover, valuations seem to be less demanding compared to those in the US.

In Japan, consensus expectations are very bullish. We only partially share this view. We are still bullish on the micro story of improving corporate governance and shareholder rewards policy in Japan, but from a top-down perspective, we believe that Japanese equities are highly dependent to JPY movements (deprecation is positive) and the potential risk of the BoJ's ETF tapering at some point should not be underestimated. Therefore, we prefer to keep a small underweight position in Japan and would only invest hedging the currency risk.

In Emerging Markets, we think that fundamentals and valuations justify keeping an overweight position. Strong growth, a weaker USD and still attractive relative valuations continue to support EM equities. High and widening growth premium is one of the primary reasons for global investors to allocate into EM equities. There are multiple growth drivers to support EM economic activity in 2018. The solid pick up in global trade supporting 2017 EM growth is morphing into domestic benign EM dynamics, via a sustained rise in private sector confidence and the EM credit impulse turning positive for the first time since 2014. We acknowledge investor concerns over the potential impact on EM from an aggressive Fed hiking cycle, but this is not our base case scenario. Moreover, we note that EM has only underperformed in one Fed hiking cycle: the Greenspan's surprise 1994 one.

2017 has been a remarkable year for Asian equities, and this is likely to be the case also in 2018. The MSCI Asia Pacific Index registering its best annual performance since 2009. Corporate earnings growth for the Asia region outperformed consensus with EPS growing more than 20% for 2017. As such, the equity rally was backed by a strong corporate earning boost rather than a mere P/E expansion. Valuations remain attractive compared to global peers with the 12-month forward P/E trading below 15x for the MSCI Asia Pacific Index going into 2018.

We think that Asia should also benefit from the "IT revolution" that we described above. The importance of this sector in Asian indices is likely to be positive also in the future. Companies like Tencent, Alibaba, Samsung, Taiwan Semiconductor are likely to continue to capture investors' interest thanks to their strong business model.

We also like Latin American equities. We remain confident on Latin America ability to deliver on strong earnings growth in 2018 driven by accelerating economic activity, lower financing costs and relatively cheap valuations. Higher economic activity combined with easy monetary policy should allow for operating leverage to pick up and financing costs to decline, boosting earnings. Brazil seems to us to be positively placed to outperform in the region. Brazil's economy is on a cyclical recovery, even if there is still uncertainty on whether this is going to remain the case, as much depends on the 2018 elections. Growth pick up and falling inflation and interest rates should sustain valuations going ahead. Moreover, there is a good chance that some social security reform will be approved before the elections.

In Eastern Europe, we think that the region could benefit from the economic recovery of the EU. Russia is also likely to enjoy a positive performance, thanks to falling interest rates and improving growth and energy outlook. Elections could led to some volatility, but we don't expect major disruptions. Moreover, Russian equities are attractively valued, as valuations are undemanding. Russia strongly underperformed, closing 2017 in the red against MSCI EM total return above 35%. We think that this leave Russian equites with plenty of potential, especially once elections will be over.

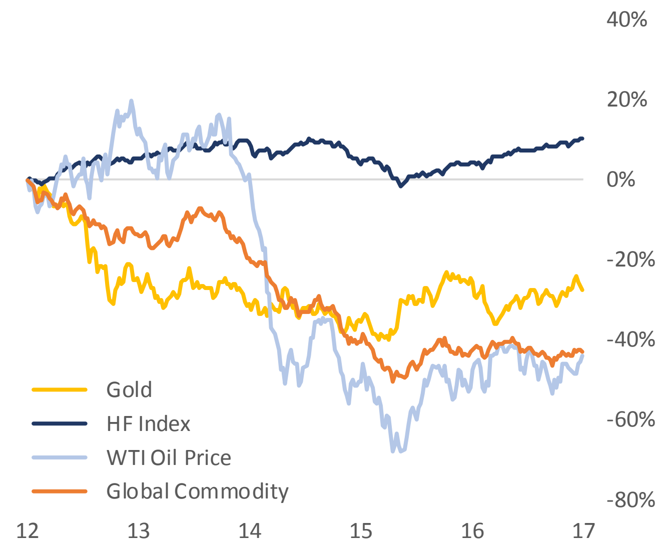
In conclusion, we remain bullish on EM equity markets. Considering the heterogeneity of this asset class and the important political and geopolitical risk that could affect EM countries, we suggest investors to invest in this asset class via dedicated investment funds, which would permit to increase diversification and adopt an active asset allocation.

COMMODITIES AND PRECIOUS METALS

Passing now in review commodity markets, we expect some more volatility in the coming quarters. In Energy, we expect Brent to average around $/bbl 60-65 and WTI to average $/bbl 55-60 in 2018. We assume that in the absence of market balance, OPEC will agree in June, or possibly in November, to extend the cuts through to the end of 1Q19 as the current agreement is originally designed to expire at the end of 1Q18. We factor in the commitment on the inclusion of Libya and Nigeria in the revised OPEC. Even if stronger growth should drive an increase in oil demand, we think that markets is still seeing abundant supply, especially from stabilizing unconventional producers, and stocks to remain in line with long term averages. Therefore, we expect energy prices to consolidate inside a wide range near current levels going ahead.

COMMODITIES RETURNS

Source: CBH, Bloomberg Financial L.P.



In Base and Precious Metals, we think that the global expansion could be sustained through next year, but the moderation in Chinese growth could add volatility to the complex. In precious metals, given solid economic growth, a possible bottoming out in inflation and the potential further FED repricing, US real rates should rise pushing prices lower. Gold will continue to be mainly driven by investment demand rather than by gold fundamental developments. We remain tactically short gold and wait for better entry levels ($/oz 1’100-1’150).

In Agricultural commodities, 2018 could presents a more conducive environment for agriculture commodity prices to push off the recent lows and for volatility to rise. That said, weather risks also cloud the outlook on the production side, after consistent record large crops in the US and Brazil have built a degree of supply-side comfort. We are neutral to marginally positive this commodity subsector.

Finally, turning to foreign exchange markets, we expect more volatility going ahead. We expect the USD to tighten against the EUR during the first half of 2018. This hypothesis is principally driven by growing interest rates differential, followed by EUR long positioning in futures markets and already very high economic readings out of Europe, which are expected to moderate in coming months. Over the second half, we think that the expectations that the ECB will start normalizing its monetary policy should sustain the EUR in forex markets.

RECAP

We expect the global economy to strengthen further from current levels.

We start the year with a more cautious stance, with a slight underweight in the equity exposure (36% vs 40% for the benchmark).

We privilege EM equities over DM ones.

In DM, we keep a market-weight exposure on the US and underweight exposure in Europe and Japan.

We compensate the underweight in equity with an overweight exposure in Convertible bonds and (higher beta) EM bonds and US senior loans.

At the sector level, we continue to see value in large technological companies as well as in the financial and energy sectors.

For our global bond portfolio, we continue to underweight government bonds and investment grade corporate bonds, especially those denominated in euros.

We also scaled back our exposure on HY bonds and prefer to adopt a neutral view.

We maintain our overweight stance on EM bonds.

We favor crossover bonds (rated BBB- and BB-), emerging bonds denominated in hard currency and convertible bonds.

We also advise to invest in the lower capital structure (subordinated bonds) of companies having strong balance sheets and dominant market positions and favor in this segment large financial institutions.

In commodities, we continue to keep a fundamentally negative view in gold, and wait for lower prices in order to tactically open new long positions, and have a neutral to mildly positive view in Energy.

CURRENCIES MARKET EXPECTATIONS

The table below provides an overview of market forecasts for major currencies. It is composed of dozens of individual forecast providers and delivers a consensus forecast. These consensus forecasts represent a median number and all forecasts evaluated correspond to calendar quarter-end dates.

			Q118	Q218	Q318	Q418	Q419
MAJOR CURRENCIES	EURUSD	1.20	1.17	1.18	1.20	1.22	1.25
	EURCHF	1.17	1.16	1.17	1.18	1.18	1.20
	EURGBP	0.89	0.89	0.90	0.90	0.90	0.90
	EURJPY	135	133	134	135	135	137
	EURNOK	9.83	9.43	9.30	9.25	9.20	8.95
	USDCAD	1.25	1.27	1.26	1.25	1.24	1.22
	USDCHF	0.98	0.99	0.99	0.98	0.98	0.96
	USDJPY	113	114	115	114	112	110
	USDCNY	6.51	6.65	6.64	6.65	6.55	6.51
	GBPUSD	1.35	1.32	1.32	1.34	1.36	1.39
	NZDUSD	0.71	0.69	0.70	0.70	0.72	0.73
	AUDUSD	0.78	0.76	0.77	0.78	0.79	0.81
OTHER CURRENCIES	USDMXN	19.7	19.0	19.0	18.8	18.8	18.1
	USDBRL	3.31	3.30	3.30	3.35	3.30	3.25
	USDARS	18.84	18.00	18.30	18.60	18.79	20.67
	USDTRY	3.79	3.95	3.98	4.00	4.03	4.30
	USDILS	3.47	3.54	3.54	3.50	3.45	3.40
	USDHKD	7.81	7.80	7.80	7.80	7.80	7.80
	USDINR	63.9	64.6	65.0	65.0	65.0	64.0
	USDRUB	57.8	59.0	58.0	58.0	59.2	61.6
	USDPLN	3.49	3.60	3.53	3.47	3.46	3.31

Source: CBH, Bloomberg Financial L.P.

MARKET RETURNS

	Name	QTD *	2017	2016	2015	2014	2013	2012	2011
Cash	LIBOR 3m Total Return	0.3%	1.1%	0.6%	0.2%	0.1%	0.2%	0.4%	0.2%
	EURIBOR 3m Total Return	-0.1%	-0.4%	-0.2%	-0.1%	0.3%	0.2%	1.0%	1.4%
Government bonds	US 3-5	-0.7%	0.9%	1.3%	1.6%	2.2%	-1.0%	1.6%	6.5%
	Eurozone 3-5	0.0%	0.1%	1.5%	1.8%	5.6%	2.4%	8.7%	1.3%
	US 7-10	-0.4%	2.4%	0.8%	1.7%	8.8%	-5.9%	4.0%	15.2%
	Eurozone 7-10	1.0%	1.5%	3.5%	2.1%	16.9%	2.9%	14.9%	2.2%
Corporate bonds IG	USD Corp 1-5	-0.2%	2.5%	2.9%	1.2%	2.1%	1.5%	6.2%	3.1%
	EUR Corp 1-5	0.2%	1.2%	2.3%	0.6%	3.6%	2.3%	8.2%	2.8%
	USD Corp 5-10	0.3%	5.5%	5.6%	0.9%	7.3%	-1.6%	11.6%	8.0%
	EUR Corp 5-10	0.6%	2.4%	4.7%	-0.6%	8.4%	2.4%	13.6%	1.5%
Corporate bonds HY	USD Corp 1-5	0.4%	7.0%	16.5%	-4.5%	1.9%	7.6%	15.2%	4.8%
	EUR Corp 1-5	0.3%	4.1%	6.9%	-0.2%	3.7%	7.6%	22.0%	-0.5%
	USD Corp 5-10	1.7%	7.6%	7.3%	1.8%	4.8%	16.9%	15.8%	-4.3%
	EUR Corp 5-10	1.0%	7.4%	11.1%	0.8%	7.4%	9.8%	30.1%	-2.9%
EM bonds (in $)	Hard currency	0.6%	8.1%	9.9%	1.3%	4.8%	-4.1%	17.9%	7.0%
	Local currency	1.9%	14.0%	5.9%	-10.4%	-1.9%	-4.3%	15.1%	0.3%
	Chinese Yuan	1.3%	4.7%	-4.7%	3.6%	8.0%	0.0%	4.7%	10.1%
Other	S&P Senior Loan Index	1.1%	4.1%	10.2%	-0.7%	1.6%	5.3%	9.7%	1.5%
	Global Convertible	0.5%	7.1%	4.6%	-0.8%	3.8%	15.0%	15.4%	
Equities	North America	7%	20%	9%	-1%	11%	30%	14%	0%
	Europe	0%	7%	0%	5%	4%	16%	13%	-11%
	Japan	9%	18%	-3%	8%	8%	52%	19%	-21%
	Asia Pacific (ex Japan)	8%	38%	3%	-11%	2%	1%	19%	-19%
	China	10%	32%	-7%	-7%	62%	-15%	11%	-19%
	Emerging Markets	7%	34%	9%	-17%	-5%	-5%	15%	-20%
Other investments	HFRX Alternative	1%	6%	3%	-4%	-1%	7%	4%	-9%
	VIX	5%	-29%	-23%	-5%	40%	-24%	-23%	32%
	G7 Currency Volatility	-15%	-36%	22%	-6%	14%	5%	-34%	-2%
	DJ Global Commodity	4%	1%	11%	-25%	-17%	-10%	-1%	-13%
	Gold	2%	13.5%	8%	-11%	-1%	-28%	7%	10%
	Industrial metals	10%	28%	20%	-27%	-7%	-14%	1%	-24%
	Agriculture index	-3%	-12%	2%	-16%	-9%	-14%	4%	-14%
	WTI Oil	16%	12%	45%	-30%	-46%	7%	-7%	8%
Currencies (vs. $)	Dollar Index	-1%	-10%	4%	9%	13%	0%	-1%	1%
	EM Currency Index	0%	6%	0%	-16%	-12%	-7%	3%	-10%
	Euro	1%	14%	-3%	-10%	-12%	4%	2%	-3%
	British Pounds	1%	10%	-16%	-5%	-6%	2%	4%	0%
	Swiss Francs	-1%	4%	-2%	-1%	-11%	3%	3%	0%
	Japanese Yen	0%	4%	3%	0%	-12%	-18%	-11%	6%
	Australian Dollar	0%	8%	-1%	-11%	-9%	-14%	2%	0%

* Last quarter
** Year to date

Source: CBH, Bloomberg Financial L.P.

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