Monthly Asset Allocation
Private Banking Europe Investment Committee

April 11, 2018

In a nutshell

- **Positive macroeconomic picture remains, but the upswing shows signs of a potential emerging dip**
- **With the US corporate reporting season, equity investors might focus again on fundamental earnings development**
- **A possible short-term rally in the US dollar could be used to reduce positions in the greenback**

Possible trade conflict and geopolitical tensions increase uncertainty

The macroeconomic data continue to paint a friendly picture of the global economic environment. However, a consolidation of certain leading indicators at a high level can be observed. The coming months will show whether this is a temporary dip in the upswing in developed countries. It is during this phase that the risk of a possible global trade conflict comes into play with an unknown outcome from today's perspective. As a matter of fact, such confrontations rarely produce winners and are likely to have a negative impact on global GDP growth. We do, however, not expect the situation to escalate, but see this as merely political manoeuvres with the aim to put the respective players in a better negotiation position. Geopolitical tensions, in particular the recent sanctions against Russia, further increase uncertainty. These factors are likely to influence capital markets in the short term and keep volatility high. At asset allocation level, we maintain our positive attitude towards equities. Against the backdrop of an anticipated solid company earnings season, stocks continue to offer yield potential in the current late-cycle economic environment, even though headwinds have become stronger in particular areas. The overdue normalization of central bank policies and a possible rise in inflation, above all in the USA, hold additional potential to weigh on equities. At the same time, we confirm our underweight in bonds and alternative investments. Liquidity remains overweight compared to strategic allocation in order to maintain the highest possible flexibility.

Table 1: Generic Tactical Asset Allocation LGT Private Banking Europe (April 11, 2018)

	Asset Class	SAA	underweight — strategic (SAA) vs tactical allokation (TAA) in USD — overweight	TAA		
		USD	-8% -6% -4% -2% +2% +4% +6% +8%	USD	EUR	CHF
Equities	US equities	20.0%		20.0%	15.0%	15.0%
	Europe equities	6.0%		8.0%	11.0%	7.0%
	UK equities	3.0%		0.0%	1.0%	0.0%
	Switzerland equities	1.0%		3.0%	4.0%	9.0%
	Japan equities	4.0%		4.0%	4.0%	4.0%
	APAC ex JP equities	3.0%		3.0%	3.0%	3.0%
	Emerging markets equities	6.0%		8.0%	8.0%	8.0%
	Total Equities	**43.0%**		**46.0%**	**46.0%**	**46.0%**
Fixed Income	Government bonds	6.0%		3.0%	3.0%	0.0%
	Inflation-linked bonds	6.0%		6.0%	6.0%	5.0%
	Investment grade bonds	12.0%		12.0%	12.0%	16.0%
	High yield bonds	6.0%		0.0%	0.0%	0.0%
	Subordinated Debt	0.0%		3.0%	3.0%	3.0%
	Emerging markets bonds	6.0%		8.0%	8.0%	8.0%
	Total Fixed Income	**36.0%**		**32.0%**	**32.0%**	**32.0%**
Alternatives	Hedge funds	7.0%		6.0%	6.0%	6.0%
	Listed private equity	2.0%		0.0%	0.0%	0.0%
	Real estate trusts	3.0%		3.0%	3.0%	3.0%
	Insurance-linked bonds	3.0%		4.0%	4.0%	4.0%
	Commodities	2.0%		2.0%	2.0%	2.0%
	Precious metals	2.0%		2.0%	2.0%	2.0%
	Total Alternatives	**19.0%**		**17.0%**	**17.0%**	**17.0%**
	Cash	**2.0%**		**5.0%**	**5.0%**	**5.0%**
			-8% -6% -4% -2% +2% +4% +6% +8%			
Currencies	USD	86.5%		80.5%	10.0%	10.0%
	EUR	0.0%		0.0%	70.1%	0.0%
	CHF	0.0%		0.0%	0.0%	70.7%
	JPY	0.0%		2.0%	2.0%	2.0%
	Others (incl. EM)	13.5%		17.5%	17.9%	17.3%

Source: LGT Investment Services Europe

*all calculations based on a "Balanced Portfolio" in USD including AI. For EUR and CHF portfolios weights differ for subclasses; over- and underweights apply analogously.

Table 2: Current asset allocation preferences

Next meeting: May 14, 2018	What we like	What we dislike
Equities	▪ European equities ▪ Swiss equities ▪ Emerging markets equities	▪ UK equities
Bonds	▪ Low duration ▪ Emerging Market Local Currency bonds ▪ Subordinated debt	▪ Sovereign bonds ▪ High yield bonds
Alternative Investments	▪ Insurance linked bonds	▪ Listed private equity
Currencies		

Sources: LGT Investment Services Europe

Equities: focus on US earnings

Currently, the focus of stock market participants is strongly influenced by geopolitical events, but the upcoming US corporate reporting season could once again draw investors' attention to fundamental earnings developments. The adopted US corporate tax reform had a substantial positive impact on the sales and earnings estimates of US companies. Now the moment of truth is approaching and companies will have to not only report a solid first quarter, but also to set clear guidelines for the second quarter, as well as the remainder of 2018. In this respect, we anticipate large price swings, with negative earnings surprises rather leading to stronger price declines than positive earnings figures leading to higher prices. In general we maintain our positive assessment for equities, but expect the price increases of recent years to consolidate in the coming months. This is why we are recommending an anti-cyclical behavior, thus building up the portfolio and increasing risk in weaker phases. After stronger phases, however, profits should also be realized in favor of cash in order to increase flexibility at the asset allocation level. Within equities, Europe, Switzerland and emerging markets remain our preferred regions.

Fixed Income: consolidation after initial rise in yields

The ingredients for a further rise in US interest rates along the entire yield curve are in place. Now that the US labor market has been at levels of full employment for some time and wage inflation is likely to start rising, the output gap between effective and potential GDP growth has also closed. Here too, scarce capacities will create upward pressure on prices in the medium term. With a possible trade dispute, now there is another factor that could boost inflation and thus interest rates at the long end. From a purely economic point of view, punitive tariffs and import restrictions are inflationary and should therefore further accelerate the rise in interest rates. This is why we prefer a short duration, as the US yield curve is extremely flat and investors are not adequately compensated for a longer duration. At the same time, we continue to see potential in subordinated paper and emerging market bonds.

Currencies: possible short term rally in the US dollar could be used to reduce positions

The US dollar has been in a classic phase of consolidation for almost two months following the sharp depreciation in the past calendar year. In the short term, the greenback may move in the opposite direction, but in the medium to long term the bias for the US currency remains negative. The political uncertainty, the saber-rattling in the trade conflict as well as the enormous trade deficit are weighing on the US dollar. Following the recent fiscal stimulus and planed infrastructure spending by the US government, the sustainable financing of this huge mountain of debt will certainly remain a matter of discussion in the medium term. Only a significant global economic slowdown – which is not our main scenario – could boost the US dollar. The Japanese yen continues to enjoy relative attractiveness: if the exchange rate exceeds 110 yen against the US dollar, we would tend to further increase our position.

If you require further information or advise, please contact your LGT relationship manager.

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