

Executive summary

- **Synchronized global economic recovery still on track despite some signs of easing momentum in the US and China**

Global economic backdrop

- A stabilization in oil and other commodity prices together with subdued wage pressures are keeping consumer inflationary pressures contained so far.
- The majority of central banks and governments globally are keen to support growth and look set to remain accommodative, albeit less than in the past. The question remains how both the US Federal Reserve and European Central Bank will unwind their balance sheets and the path of ECB tapering.
- The US economy remains on a strong footing but the cycle is showing signs of a maturing.
- The euro zone economic recovery is becoming increasingly solid. The outcome of the French election has led to a material reduction in perceived political risk in the region.
- Japan's recovery remains fragile despite some pick-up in domestic consumption and exports.
- China's growth is still strong but took a step back in April after a surprisingly strong start to the year.
- The rest of Asia is boosted by a revival in exports.
- The overall earnings season is a bright one, leading analysts to revise up their earnings projections.

Investment conclusions

- **Focussing solely on political dramas lead to miss the most important story, the improvement in the global economic picture.**
- **Overweight risky assets : Equities Europe, US Asia ex-Japan, High Yield, Global Emerging Debt**
- **Underweight Japan equities, DM government bonds**

- Our global asset allocation remains **tilted towards risky assets** (equities, emerging debt and High Yield), as we believe those asset classes should remain underpinned by the first synchronized economic recovery since 2009. After six years of disappointing growth, the world economy is gaining strength amid increases in US, EU and Chinese growth. Growth in emerging economies, coming from a low base, is supported by stable commodity prices and improving global demand.
- A modest increase in US interest rates should not be disruptive to financial markets as long as the higher rates remain in line with expectations. We do not expect a surge in inflation as the impact of Trump's pro-growth policies - if implemented - are unlikely to be felt until next year.
- European equities look well positioned to benefit from new French president Macron's pro-EU tendencies. Macron's positive signal on more cooperation within Europe on the political front will allow the current economic recovery to build further.
- **Equity valuations** are no longer cheap but still look supportive given the low level of interest rates. A slight expansion in valuation multiples still look appropriate if inflation remains moderate between 2-3%.
- **Over the near term** however some profit taking cannot be excluded. The road to higher stock prices is likely to remain bumpy: The macroeconomic environment is complex and political risks abound. It remains to be seen whether Trump's policies will succeed in matching market expectations. The sword of protectionism is hanging and the outlook for the China's economy remains clouded by lingering overcapacity and rising debt. Slow productivity growth around the world is also a concern.
- We believe **buying the dips** will be well-rewarded.

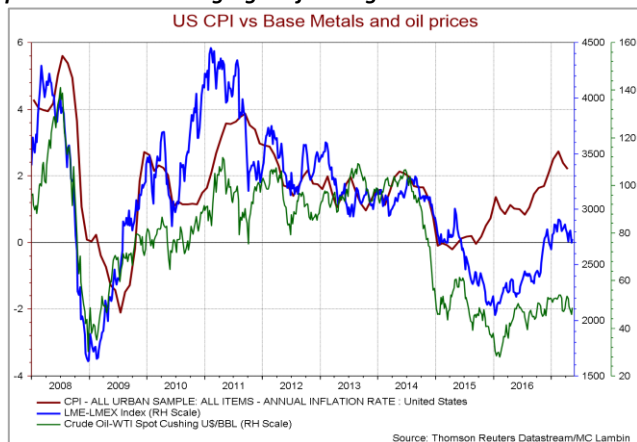
Global economic backdrop

- Positive oil comparison basis is starting to fade, keeping a lid on consumer inflation
- Producer price inflation is close to peaking
- OPEC's production cuts have failed in sending oil prices much higher

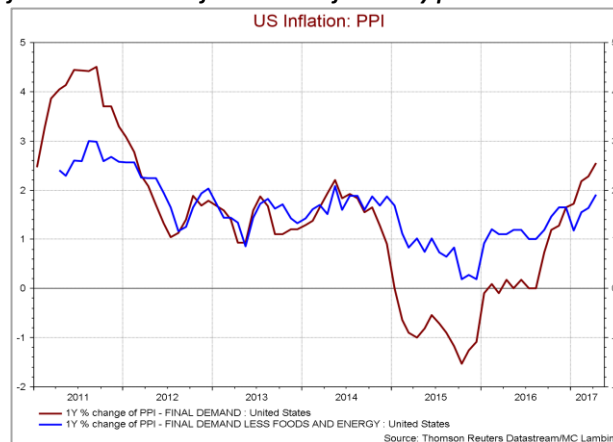
Inflationary pressures close to peak

- The low inflation of 2015 and 2016 was all about commodity prices falling. As soon as the oil price started to rise, both consumer inflation (CPI) and Producer Price inflation (PPI) have also increased. Now that the positive oil comparison basis is coming to an end, upside pressure on inflation is receding.
- **Consumer inflation** has remained quite contained so far. **Producer price inflation** is still rising in most developed countries but cooled in April in China for the first time in seven months as commodities prices tumbled, pressured by fears that Chinese steel production is outweighing demand and threatening a glut of the metal later this year. PPI is the most appropriate indication of domestic pricing power. A company that sells its products internationally will have its pricing power determined by export price inflation as well.
- **Supply glut is keeping a lid on commodity prices.** Oil prices have been locked within a range during Q1 as concerns linger about a glut in the oil market despite OPEC's production cuts. Inventories in many parts of the world are at, or near record highs and US production has been rising. US rig counts have doubled over the past 12 months, undermining efforts led by OPEC to rein output. US shale producers have increased efficiency substantially over the past two years and can now survive at much lower prices and be competitive with other large producers worldwide. If U.S. producers keep on increasing output at the same pace, then rebalancing in the oil markets is likely to get delayed beyond 2017. According to recent Thomson Reuters polls, WTI crude prices are seen to average \$55.29 a barrel in 2017, revised down from previous projections of \$58/bbl in 2017 earlier in March.
- If oil and other commodity prices stabilize around current level, we doubt inflation will surge much from here. Producer prices need to be watched for further indication of sustained inflationary pressures.
- Steel and industrial metal prices should receive further support in 1H18 once US President Trump's infrastructure thrust takes shape.

Now that oil base effects have come through, consumer inflation pressures are showing signs of ebbing



US Producer Prices are still trending up and need to be watched for further indication of sustained inflationary pressure



Central Banks

Monetary policies to stay accommodative albeit less than in the past

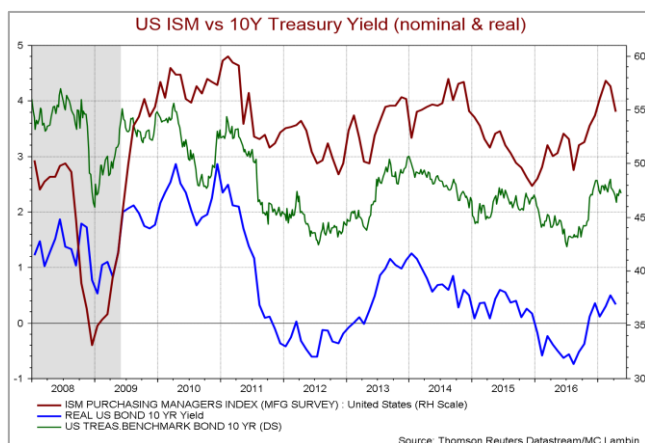
The FED on track for a gradual tightening

- Minutes of the latest policy meeting showed the Federal Reserve is increasingly confident in the trajectory of the US economy allowing for a gradual monetary tightening. The Fed said that the poor first-quarter U.S. growth was likely dampened by temporary factors.
- The median estimate of the long-run interest rate, where monetary policy would be judged as having a neutral effect on the economy, held steady at 3.0%.
- Policymakers are expected to start reducing the Fed's \$4.5 trillion bond portfolio later this year as long as the economic data holds up. Policy makers also appeared to see upside risks to the economy.
- The Fed is widely expected to raise interest rates again at its June 13-14 meeting.

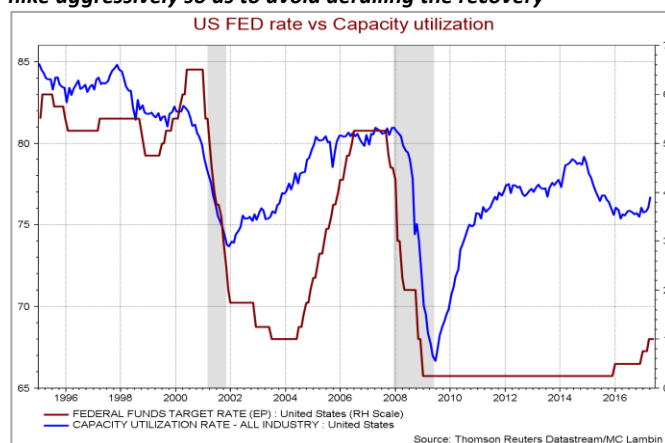
The ECB on hold but tapering looming

- The European Central Bank decided to leave its key interest rates unchanged at its April meeting as inflation continues to undershoot its target but started tapering its Quantitative Easing (QE) program from EUR 80 billion a month to EUR 60 billion.
- While bond purchases are intended to run until the end of the year, or beyond if necessary, President Draghi explicitly acknowledged the vigour of the euro zone economy, now on its best run since the global financial crisis and noted that the risk of a new downturn had receded.
- According to the minutes of its April meeting, the ECB appears closer to normalizing monetary policy.

Toppish US ISM points to a maturing US economic, suggesting interest rates will rise only gradually



Capacity utilization rate is improving but remains well below historical average, suggesting the Fed will remain cautious not to hike aggressively so as to avoid derailing the recovery



Economic backdrop - USA

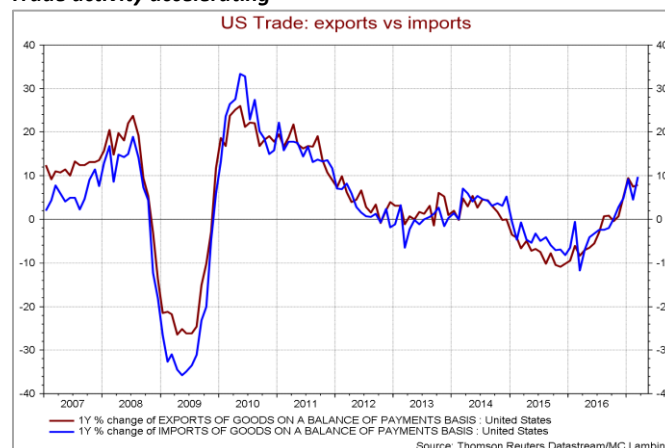
Growth still solid despite some signs of a maturing cycle

- **Productivity** unexpectedly fell in Q1, in line with a near stall in economic growth at the start of the year. Unit labor costs, the price of labor per single unit of output, increased at a 3.0% pace in Q1 after rising at a 1.3% rate in Q4.
- Industrial production for April grew at its fastest pace in over 3 years, capacity utilisation hit a 20-month high and the Conference Board's index of leading economic indicators rose for the 4th straight month, backing the Fed's view that the Q1 weakness was a temporary phenomenon. A drop in the ISM manufacturing (to 54.8 from 57.2 in March) however suggest that the cycle is close to maturing.
- **Job growth** rebounded sharply in April (non-farm payrolls +211K) and the unemployment rate dropped to 4.4% pointing to a tightening labor market that likely seals the case for an interest rate increase next month despite moderate wage growth. The U.S. economy needs to create 75,000 to 100,000 jobs per month to keep up with growth in the working-age population.
- **Domestic consumption** remains solid with retail sales increasing broadly in April.
- **The housing market** recovery remains on track. Housing starts dropped to its the lowest level in five months and building permits also fell in April but Home builder sentiment rose in May to a new historical high. While a slight moderation in housing activity is expected in the near term owing to higher mortgage rates, the picture for 2017-18 remains one of modest trend improvement
- **A moderation in year-on-year inflation** is supporting the view that the Fed will hike only gradually. CPI slowed to +2.2% from 2.4% in March, core CPI down to 1.9% from 2%, PCE down to 1.6% in March from 1.8% in February.
- **Political risks:** Former FBI Director Robert Mueller will now run an investigation into Donald Trump's firing of FBI director James Comey. This not only creates uncertainty, but will also suck up the time and energy of policymakers. As such, it is even less likely any progress can be made on Trump's reform agenda.

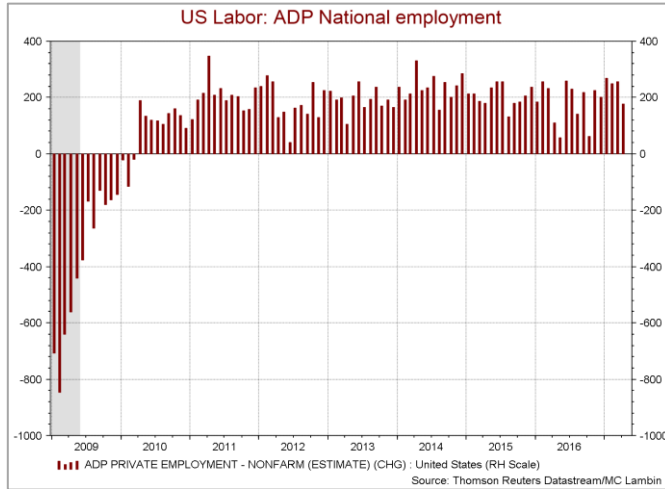
Manufacturing showing signs of peaking



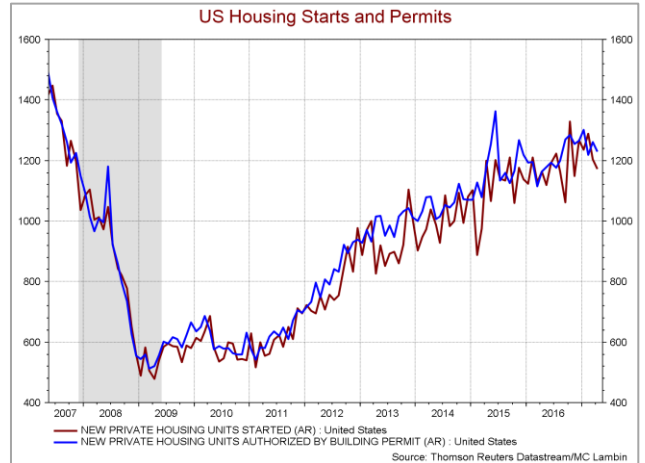
Trade activity accelerating



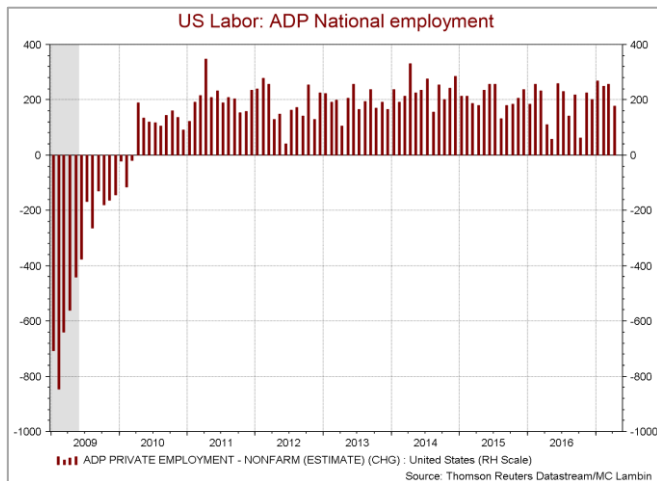
Job creation remains strong



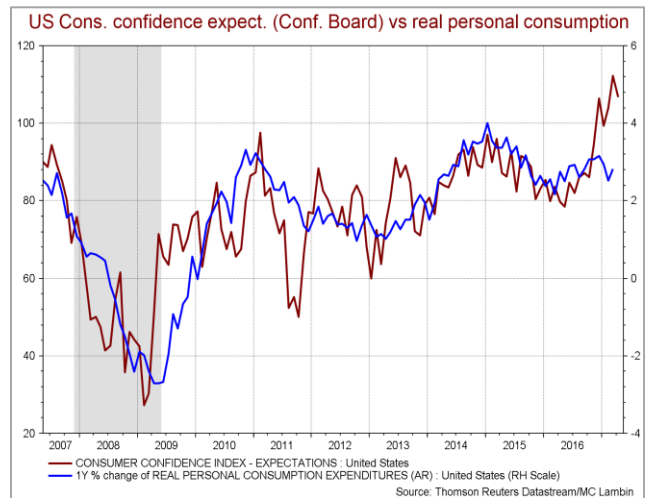
Housing market recovery remains on track



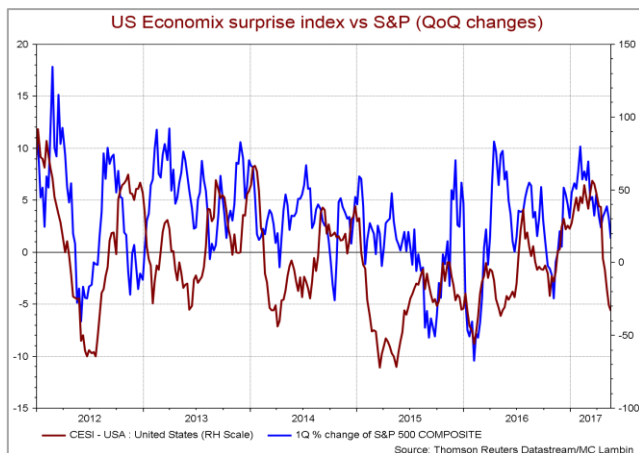
Sustained job creation pointing to tightening labor market conditions



Upbeat consumers boding well for consumption and growth in the months ahead



The decline in US economic surprises suggests US equities look ripe for a pause



Slowing productivity growth remains a concern. History shows that when labor costs at a faster pace than productivity, a recession occurs in the following year

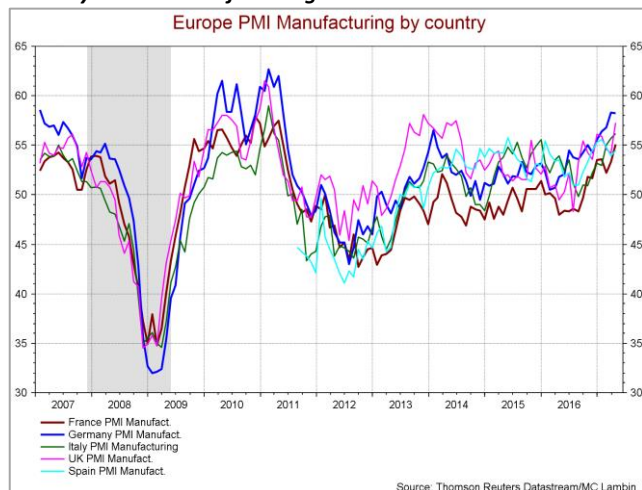


Economic backdrop *Euro zone*

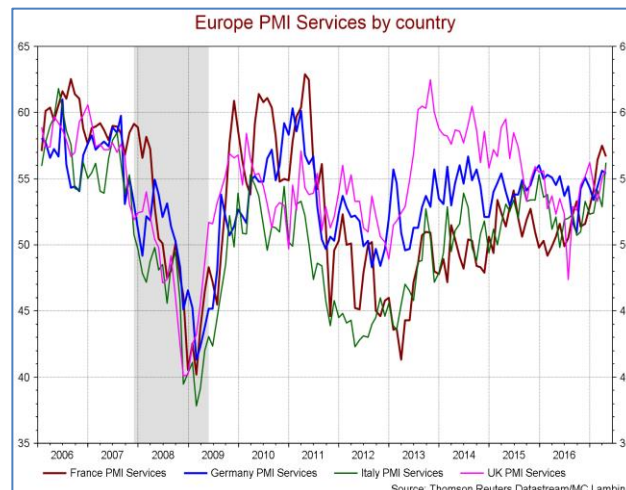
A broad-based and sustained recovery

- **The euro zone outpaced the US economy in Q1** with an annualized growth rate of 1.8%, compared to 0.5% in the US.
- **April PMI data** showed Euro zone activity accelerated further. The final Composite PMI rose to 56.8 (vs a drop to 52.80 in the US), the fastest rate in six years.
- **French business activity** confounded expectations by growing at the fastest pace in nearly six years, despite an uncertain presidential elections. France Final composite PMI rose to 57.4 while German PMI fell to 56.3 from 57.0. A lot of French companies said there was a very positive outlook for business once this election is out of the way. PMI at these levels are consistent with quarterly growth of about 0.7%, a significant acceleration from 0.4% in Q416. This compares with a 0.7% annual pace of growth in the US.
- **The bloc's economic recovery is broadly based.** In Italy, service sector growth was at its fastest rate for almost a decade, while Spain's hit a 20-month high.
- **Political risks are receding.** As widely expected, Emmanuel Macron was chosen as the new French President. The result was even stronger than the previously reliable polls had predicted as most of Melenchon and Fillon voters eventually vote for Macron or abstained rather than voting for Le pen. It remains uncertain how effective Macron will be as a President and if he will get enough support to put his reform plans into practice. Much will depend on the outcome of the Parliamentary election on June 11 and 18 since to govern in France, a parliamentary majority is required. It is important to note, however, that this is especially relevant for his domestic agenda on crucial topics as labour and tax reform, but less so for his ability to more closely cooperate on the European level, most notably with Germany. WE believe the core alliance of the European project has strengthened as a result of the French and might strengthen further after the German elections which seem likely to create a larger role for the SPD.

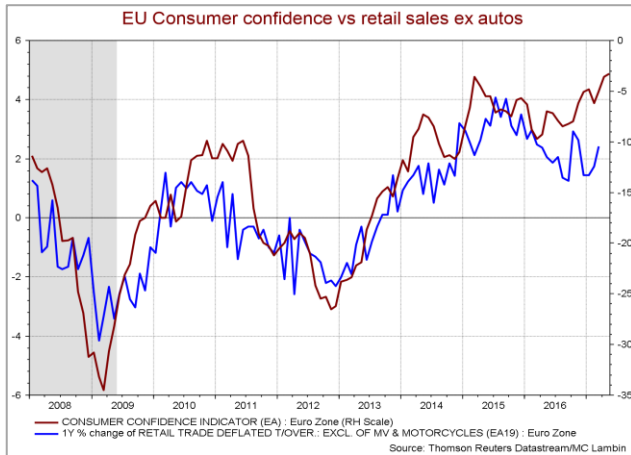
Euro zone recovery is gathering pace, driven by a broad based recovery in both manufacturing



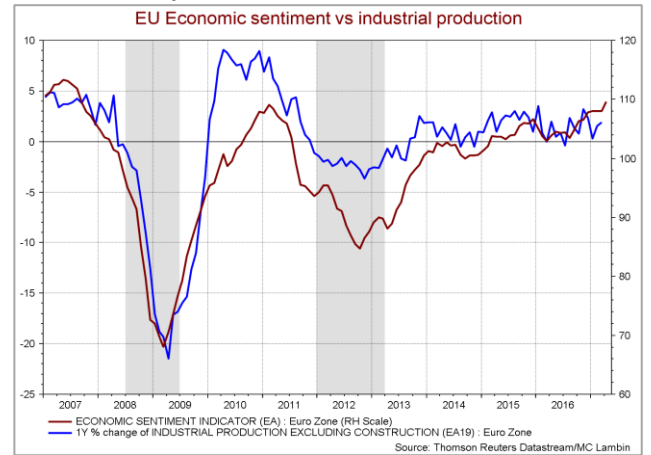
...and services



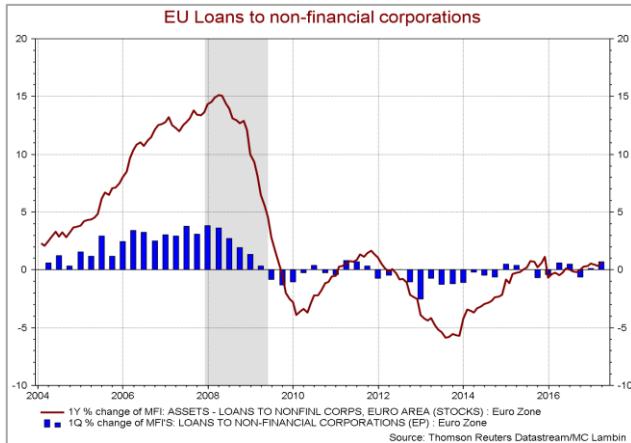
Upbeat consumer confidence is likely to support consumption in the months ahead



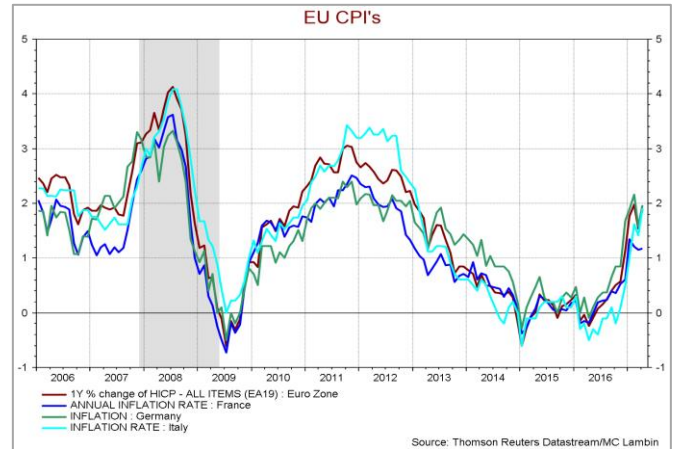
Economic sentiment is improving, boding well for future economic activity



Corporate loans remain subdued



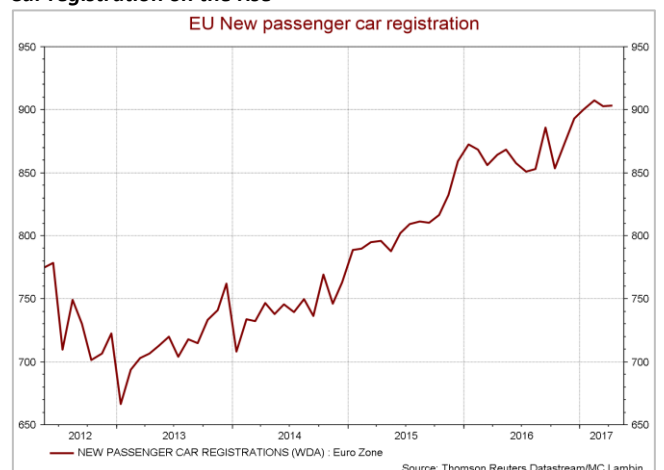
Inflation back to historical average



Euro zone unemployment is trending down



Car registration on the rise

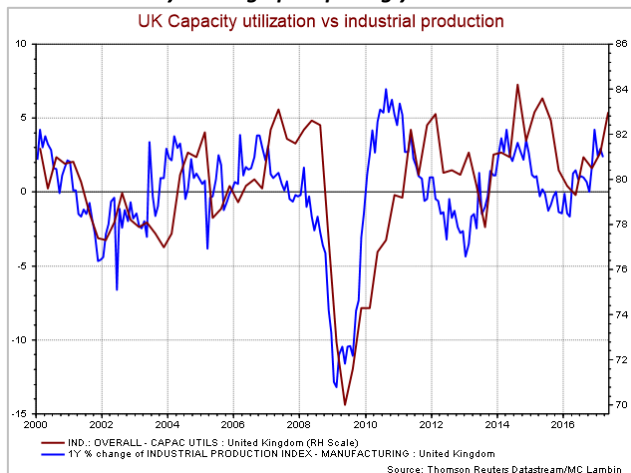


Economic backdrop - UK

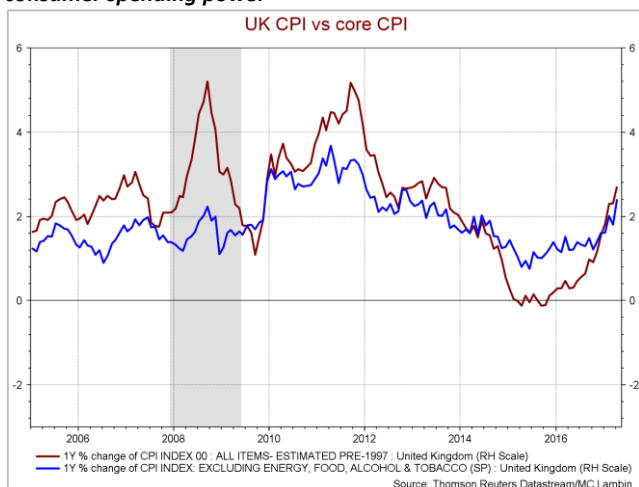
A surprisingly resilient economy

- **Construction industry** accelerated to a four-month high in April, against forecasts in for a slight fall. adding to tentative signs that the economy might be recovering a little momentum after a lacklustre start to 2017.
- **Retail sales volumes** jumped by 2.3% in April, beating expectations and suggesting consumers' mood has become more upbeat in the run-up to a June 8 national election that Prime Minister Theresa May's ruling Conservatives are tipped to win by a wide margin. April's sharp rebound in retail sales bolster hopes that consumer spending will not hamper UK GDP growth as it clearly did in Q1.
- **British pay growth** has fallen behind inflation for the first time in two-and-a-half years, underscoring the growing Brexit squeeze facing many voters ahead of June 8 national election. When adjusted for fast-rising inflation, fell by 0.2%.
- Overall, the data is likely to bolster **the BoE's decision** to keep interest rates just above zero. Despite inflation pushing past its 2% target, the BoE says it has seen no sign of a permanent spike in prices fueled by higher wages.

Industrial activity holding up surprisingly well since the Brexit vote



Inflation boosted by the drop of the sterling, a potential threat to consumer spending power



UK unemployment at historical low



Domestic consumption not yet derailed by the rise of the sterling



Economic backdrop Japan

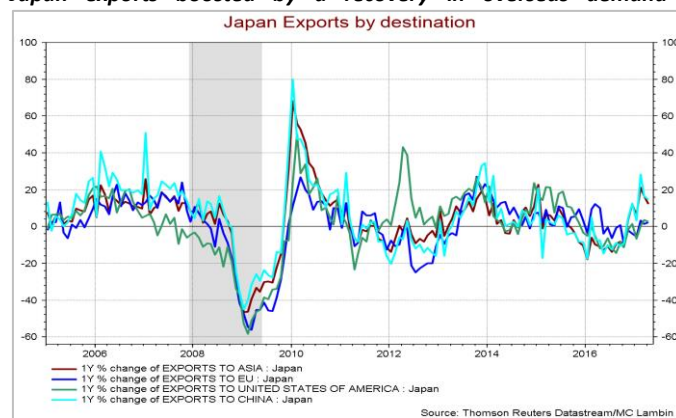
A fragile recovery

- **Q1 GDP** grew by an annualized 2.2 %, exceeding forecast of a 1.7% gain, led by a pickup in net exports and a rebound in private consumption. Capex grew by a mere 0.2%, slowing from a sharp gain in the previous three months as companies have been cautious about implementing capital investment amid uncertainty over global and domestic demand.
- **Exports** rose by 7.5% yoy in April, as shipments of semiconductors and steel expanded on more robust overseas demand. Japan's exports are expected to continue rising as global economic growth gains momentum, but concerns about U.S. President Donald Trump's pledges to adopt protectionist trade policies cloud the outlook for export-reliant Japan.
- **Consumer prices** are barely rising as firms remain wary of increasing wages. Wage earners' total remuneration fell 0.2% in nominal terms qoq in Q1, keeping the BOJ under pressure to maintain its massive stimulus despite improvements in the economy.
- Going forward, economists expect Japan's economy to post continued modest growth in Q2. The average GDP forecast for fiscal 2017 was revised up to 1.37% from 1.30%.
- **The appreciation of the yen** remains the key downside risk to Japan's economy as it trims exporters' profits and thus hurts overall business sentiment, although it lowers import costs for firms and households.

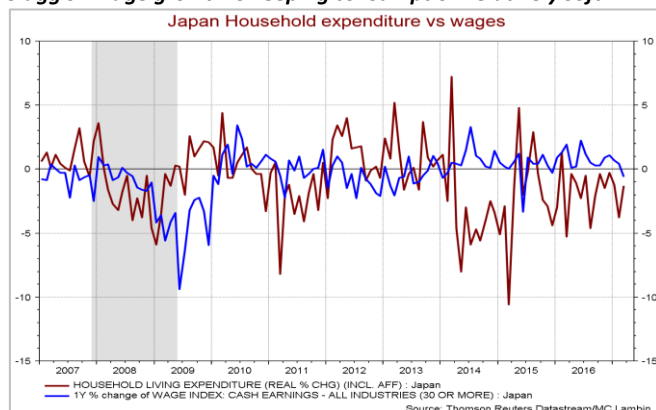
Japan manufacturing has recovered from contraction last year



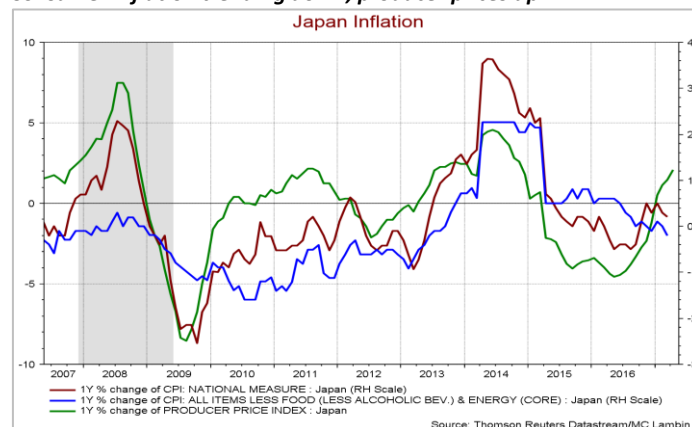
Japan exports boosted by a recovery in overseas demand



Sluggish wage growth is keeping consumption relatively soft



Consumer inflation trending down, producer prices up

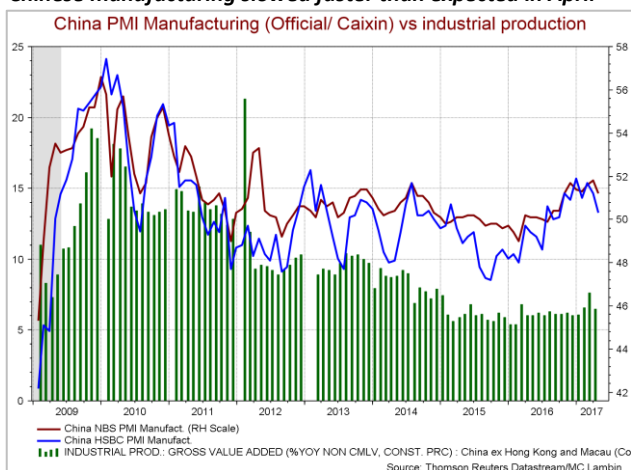


Economic backdrop China

A step back after a surprising strong start to the year

- **Q1 GDP growth** came in at a faster-than-expected rate of 6.9% , the quickest since 2015 on higher government infrastructure spending and a property boom.
- **April data** came in below expectations as policymakers' efforts to contain financial risks after years of debt-fueled stimulus weighed on demand.
- **Official manufacturing PMI** dropped to a six-month low of 51.8. Growth in the services sector slowed slightly to 54.0.
- **Fixed asset investment growth** slowed more than expected. Property sold grew 7.7% yoy in April, the lowest since December 2015 and well short of the 14.7% increase in March as policymakers seek to tighten speculative investment, especially in the property sector. **Infrastructure spending**, however, continued to grow over 23% percent year-on-year in the same period, supported by Beijing's Belt and Road initiative to expand investment links with Asia, Africa and Europe.
- **Retail sales** slowed 10.7% yoy April from 10.9 % in March.
- **Trade data** showed a surprising slowdown in imports. China's imports of crude oil, iron ore and copper all fell by volume compared with March, in line with the slowdown in manufacturing. Exports slowed to 8% yoy from 16.4% in March.
- **M2 Money supply** is declining as worries about speculative bubbles have forced the central bank to tighten short term liquidity. Massive debt - standing at nearly 300% of GDP - and serious budgetary imbalances mean Beijing can't carry on pumping money.
- **Producer prices** cooled in April for the first time in seven months suggesting China's deflation cycle in producer prices may have peaked as a rally in China's commodities markets showed signs of correcting. Iron ore and steel hit multi-month lows on China's future markets in April amid concern over rising inventories.
- **A hard landing however looks unlikely.** Chinese authorities are keen to ensure steady economic growth ahead of the 19th Communist Party Congress later in the year. Chinese leaders have pledged to address financial risks and asset bubbles which may pose a threat to the Asian economic giant if not handled well.

Chinese manufacturing slowed faster than expected in April



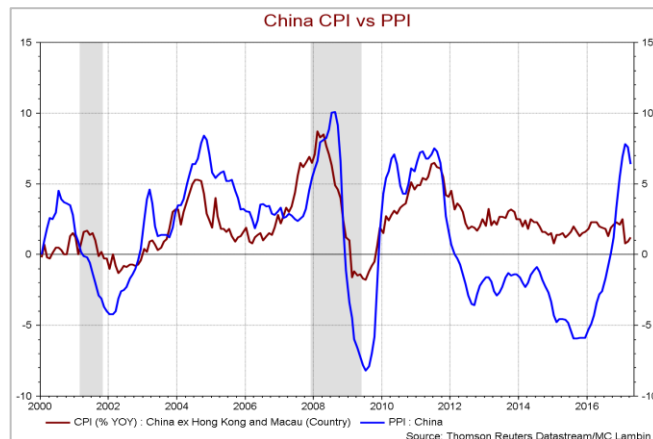
Fixed asset investments hampered by a property slowdown



Services easing momentum as well



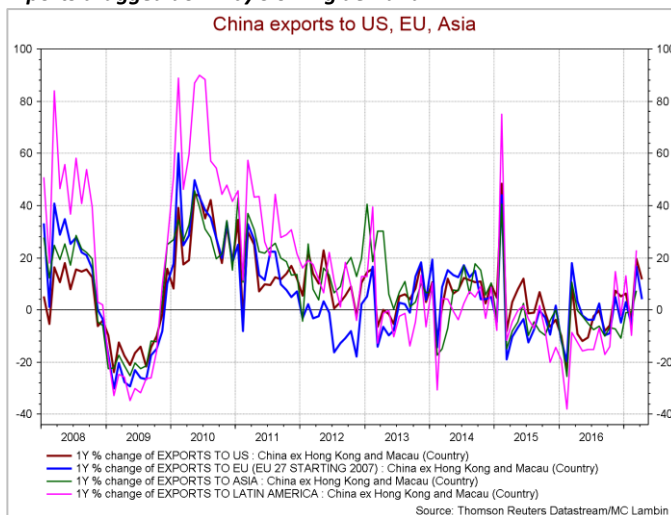
Consumer inflation subdued, producer prices may have probably peaked



Money supply as a further evidence of slowing demand amid policymakers' effort to tighten speculative investment



Exports dragged down by slowing demand



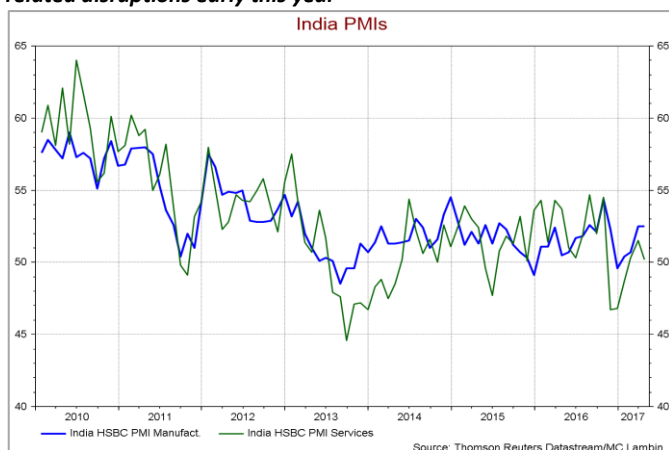
A solid start in Q2 led by exports

Economic backdrop

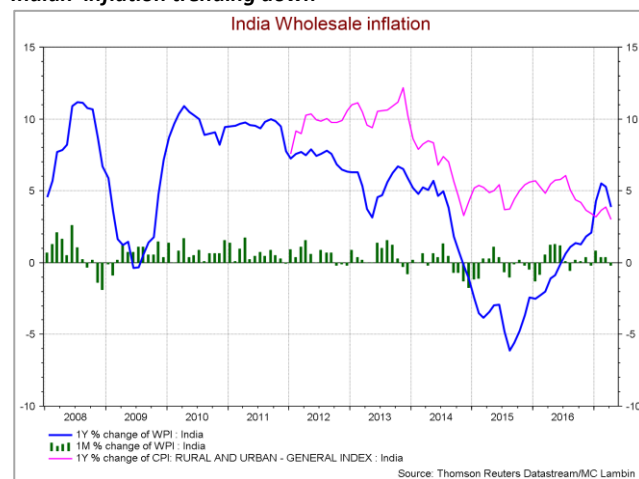
The rest of Asia

- **April manufacturing surveys** showed the recovery remains intact, despite a slide in commodity prices, thanks to robust US and EU demand and a pick-up in regional investment
- Asia's tech cycle resilience, solid services demand, and the rising pace of machinery sales suggest that demand can broaden out further
- **Inflationary pressures** are subsiding, giving the region's central banks scope to keep policy on hold as they wait for the U.S. Federal Reserve's next move.
- **Indonesia** : S&P upgrades sovereign credit outlook to investment grade BBB-, up from the previous junk status of BB+, reflecting improvements in its external balance sheet, including as narrower current account deficit- The upgrade could help boost investment and allow Indonesia to reach economic growth of 5.4-6.1% in 2018 versus 5% or less in recent quarters.

Indian economic activity is recovering from the demonetization-related disruptions early this year



Indian inflation trending down

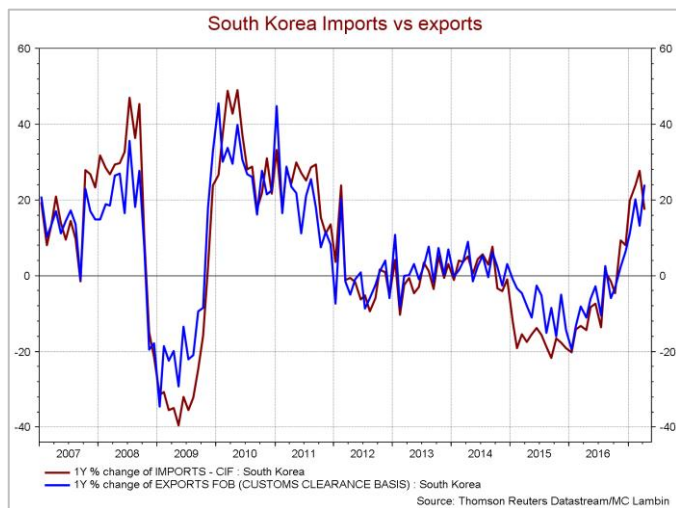


Philippine industrial production boosted by global demand



Indonesian exports supported by a recovery in commodity prices

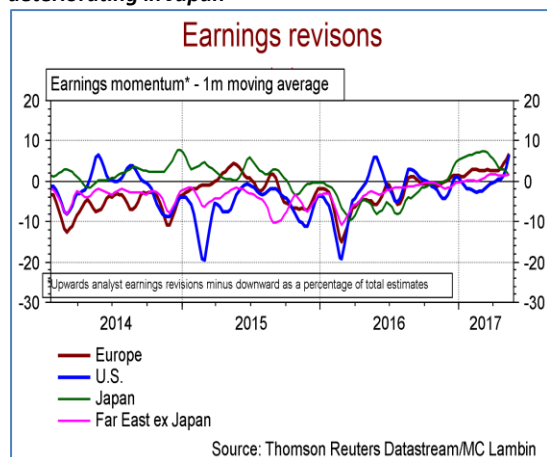




Corporate profit

➤ A strong earning season

Earnings revision has accelerated further in positive territory particularly in the US and Europe, while deteriorating in Japan



A cyclical rebound in earnings

- **Q1 earnings** delivery was the best in six to seven years, with above-average positive surprises and double-digit growth seen in all the main regions. Top line was particularly strong, helped by higher commodity prices, pick-up in inflation and the rebound in global activity. Earnings recovery was seen across the board and cyclicals' earnings beat those of defensives in all the three regions. Financials delivered double-digit EPS growth in the US (18%) and Europe (21%), but disappointed in Japan (-10%).
- **Global EPS revisions** accelerated further into positive territory during the reporting season – to the highest level since 2011 – driving upgrades to FY'17 estimates. FY'17 EPS growth forecasts now stand at 19% for Eurozone, 21% for UK, 13% for Japan, 11.5% for the US and 20% for emerging markets according to IBES estimates.
- **The estimated earnings growth rates for the STOXX 600** for Q1 2017 is +13.6% (+8% ex- energy), from Q1 2016, up from 8% at the start of the earning season.

Exhibit 16. Estimated Earnings Growth for 2017

Sector	Today	1 Apr
Consumer Discretionary	7.2%	6.8%
Consumer Staples	6.0%	5.9%
Energy	402.6%	416.6%
Financials	13.0%	12.6%
Health Care	5.2%	4.7%
Industrials	6.9%	4.7%
Materials	13.0%	12.9%
Real Estate	3.1%	2.8%
Technology	11.9%	10.4%
Telecom	-1.0%	0.6%
Utilities	0.2%	0.0%
S&P 500	11.5%	10.9%

Source: Thomson Reuters I/B/E/S

Exhibit 8C. STOXX 600: CY 2017 Earnings Growth

Sector	Today
Basic Materials	20.2%
Cyclical Consumer Goods & Services	19.1%
Non-Cyclical Consumer Goods & Services	11.8%
Energy	55.1%
Financials	36.0%
Healthcare	4.7%
Industrials	8.0%
Technology	9.0%
Telecommunications Services	2.8%
Utilities	-0.4%
STOXX 600	19.9%
Number of Companies Included in Estimate	506

Source: Thomson Reuters I/B/E/S

Valuations

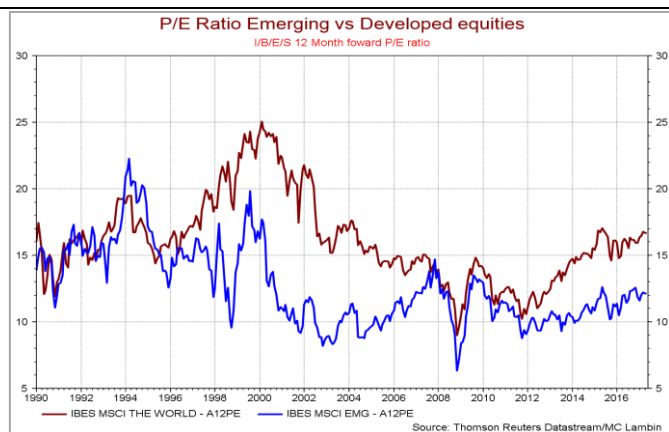
- *Global valuations slightly above average*
- *Still some room for multiple expansion given the low level of real interest rates*

	PE 17	PE 18
EURO STOXX 50 EUR	15.06	13.73
STOXX Europe 600 EUR	15.81	14.45
Deutsche Boerse DAX	13.86	12.84
CAC 40 Index	15.22	13.86
S&P 500 Index	17.74	16.07
Nikkei 225 Index	15.93	17.03

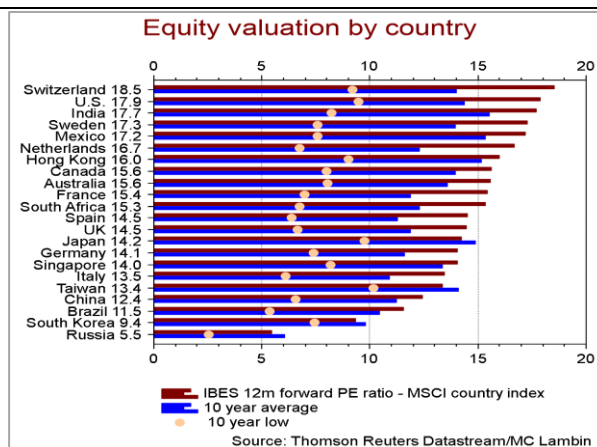
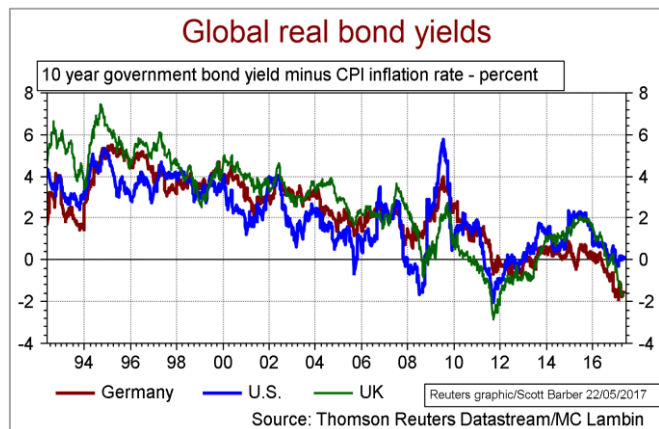
Inflation range (%)	Reasonable PE multiples (source Raymond James)
0-3	18-19
3-4	17
4-5	15.9
5-6	15.4
deflation	13.6

No longer cheap but far from exuberance

- Developed markets exhibit valuations slightly above average but still look reasonable given the low rates environment and contained inflationary pressures. European equities in particular should remain underpinned by still negative real interest rates.
- Provided companies earnings growth accelerate in 2017 as forecast, we think forward PE ratio have still some room to expand as long as inflation remain below 3%.
- Since the election of Donald Trump as US president, world equity markets have rallied substantially, boosted by pledges of tax reforms, reduced regulations and increased infrastructure spending. Details however remain scarce on Trump's plans and investor sentiment has improved faster than the actual activity. Ultimately we need to see those fundamental changes come through to push markets higher.



Low (negative) real interest rates to be a major support for equities



Investment conclusions

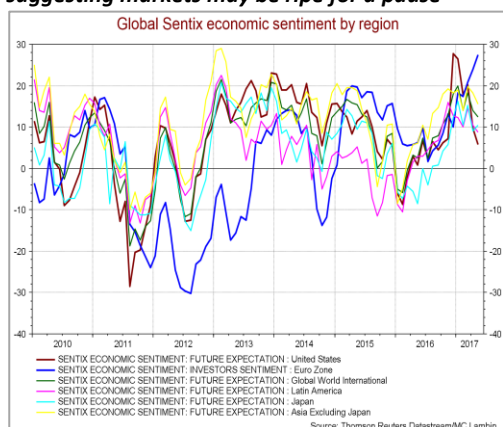
- **Economic conditions are more influential market drivers than politics**
- **Overweight Equities US, Europe, Asia ex-Japan**
- **Underweight Japan**
- **Overweight High Yield US and EU**
- **Overweight EMD**
- **Underweight US Treasuries, EU government Bonds, Corporate IG**

Medium term view: a positive backdrop for risky assets

- Our global asset allocation remains tilted towards risky assets (equities, emerging debt and High Yield),
- The rally in risky assets following the US elections does not just come from potential policy stimulus, but rather reflects improvement in global economic momentum and a cyclical recovery in corporate earnings.
- We believe this positive backdrop will remain in place until year end, although there will be bumps on the road due to uncertainty about the pace of US rate hikes, ECB tapering, President Trump's policies, Brexit negotiations, German elections among others.
- Recent headlines have been dominated by uncertainty surrounding Trump's presidency. The bull market would be at risk only if an impeachment led to a loss of confidence that triggered an economic contraction.
- We believe focusing solely on political dramas leads to miss the most important story, the improvement in the global economic picture. Confidence indicators among both corporate and households remain elevated, suggesting the global economy should stay in a positive momentum in the months ahead, paving the ground for sustained earnings growth, the main driver of equity return. It is fair to say however that upside potential until year end now appears more limited for risky assets given the strong rally since the start of the year (expect +/-5% for MSCI AC World).
- High yield (both USD and EUR) and emerging debt remain our favorite bets in the fixed income universe.

□ Some caution over the near term

Sentiment indicators have reversed trend recently, suggesting markets may be ripe for a pause



- Sentiment indicators have ebbed somewhat over the past few weeks, suggesting markets may be ripe for a pause. Investors may now wait for somewhat to see Trump's pledges of tax reforms, reduced regulations and increased infrastructure spending come through.
- Donald Trump is on his first foreign trip as president, which will take him across the Middle East and Western Europe. This provides an opportunity to draw away attention from his domestic problems and look "presidential", but the consequences of any gaffes could also be magnified by the global spotlight and generate some volatility in the coming weeks.
- Seasonality ("Sell in May and go away") may also dampen the risk-on mode over the near term.
- The ECB may soon prepare the markets for a reduction in monetary easing, a shift that may support the euro versus the US dollar. A stronger euro however may cast doubt about the resilience of euro zone stocks. Around 35% of euro zone corporate revenues come from the US and a 10% rise in the trade-weighted euro reduces earnings per share by 3%.
- We nevertheless do not expect a major correction as many investors are still sitting on piles of cash waiting for any correction to buy the dips, providing a cushion for any short-term market pull back.

Investment conclusions

(continued)

Regional approach : Our main convictions

- **European equities** should benefit from reduced political risks. A period of relative political tranquility should encourage investor inflows – European stocks already enjoyed a record USD 6 billion influx in the week following the French presidential vote. After five years of stagnating earnings, EPS growth return in 2017, helped by a pick-up in GDP growth. A strong US economy is proving a bone to European markets as European companies derive around 40% of their revenues from the US. Brexit negotiations may bring some volatility but the full economic impact of the Brexit will take years to materialize.
- **US equities:** The economy appears well-positioned to remain on a sustained growth path in 2017: increasingly enthusiastic consumers supported by strong labour and housing market suggest household's demand will help economic growth in the months ahead. Trump's pledges for massive infrastructure spending, tax cuts and lighter regulation is quite positive for the US economy and businesses and provide a major support to several sectors like technology, financial services, energy, consumer discretionary, consumer staples, and industrials.
- **Asia ex-Japan equities** remains the most attractive area in the EM world. Generally speaking, most developing countries have better fundamentals than 2-3 years ago. Emerging markets are now growing at their fastest pace in almost three years. EMD fundamentals have strengthened on the back of higher commodity prices and the sharp EM FX depreciation of the past years having resulted in current account improvements. Most EM countries have made further progress on implementing structural reforms in the past year. The anticipated increase in US infrastructure spending helps support certain commodity markets. **India** is our favourite country bet as the country represent the best structural growth story within the emerging world driven by consumption-led growth, favourable demographics, rising income levels, a revival in government expenditure and falling inflation. The government continues to focus on initiatives targeting improvements in efficiency.

Sector approach - Our preferred themes

- **Technology** has been one of the most consistent earnings generators in recent quarters. Enterprise IT spending has remained solid, growing at a mid-single digit pace, driven by strong software spending and data center-related investments in developed markets. Cloud-related investments continue to be robust. Cyber security has above-average growth prospects. With large offshore cash balances, US tech companies will be one of the biggest beneficiaries of the foreign profit tax breaks reform. The US Technology sector is expected to take advantage of high FCF generation to increase dividend growth. In Europe the sector's premium rating reflects above-average ROEs and steady cash flow generation in software. The Technology sector is

Investment conclusions

(continued)

expected to take advantage of high free cash flow generation to increase dividend growth next year to 10%, both in the technology hardware & equipment and the software services. *Apple* and *Microsoft* will make a large contribution to the sector's growth rate. *Visa* is benefitting from the strong expansion in e-commerce. With more than half of the world's Internet users coming from developing markets, e-commerce has ample global growth opportunities.

- **Infrastructure related stocks** (machinery, materials, transportation, construction and house builders) should be supported by Trump's pro-growth agenda, its US fiscal stimulus and its huge financial pledges to upgrade the US infrastructure. The need for infrastructure development is a global phenomenon. While developed countries need to repair, upgrade or completely replace aging infrastructure, emerging countries need to develop new infrastructure to meet the needs of their growing populations, economies and urban centers. This create opportunity for cement companies. Resource-rich countries that benefit from higher commodity prices could invest more in infrastructure.
- **Home improvement** will benefit from a continued recovery in the housing market in the US and Europe. US existing home sales and housing starts are still growing in the mid-to-high single digit range, supported by strong labour market, higher wages and increased household formation. The prospects for European private construction are improving. Home-improvement retailers remain one of the best-insulated sectors from e-commerce threats, as the high weight/value ratio of many products prohibit cost-effective shipping and the specialized knowledge base employees offer is difficult to replicate.
- **Aging population.** The healthcare sector traditionally has been one of the more defensive sectors that benefits from stable demand in mature markets and ongoing growth in emerging markets with strong cash generation and growing dividends. Near term outlook clouded by lingering challenges: debate about drug pricing likely to stay (particularly in the US); patent expiries and generic competition for certain players; rising bond yields (pharma tend to underperform during periods of rising rates). Over the medium term the healthcare sector is set to benefit from a number of factors, including an aging population (especially in more mature markets) and improving access to care in developing markets. US healthcare reforms continue to provide positive benefits for certain healthcare providers, especially those that have historically suffered from bad debts arising from the treatment of uninsured patients. The pharmaceutical segment should remain stable, growth continues to be driven by new product launches as well as entry into new geographies and emerging markets although patent expiries and generic competition will continue to challenge certain players. For healthcare providers, challenges come in the form of government budget constraints and plans to reduce reimbursements for services over time (particularly in the US), thus a need to manage and reduce costs, which has driven recent M&A activity as companies seek to benefit from scale as well as growing the top line.

Investment conclusions

(continued)

❑ Fixed income opportunities

- **High Yield:** Moderate global economic growth should lead to gradual rate hikes, which should be constructive for HY bonds. Given strong corporate fundamentals and the continued stabilization of commodity prices, the US default rate should continue to trend lower this year. Outside the energy sector, defaults are expected to remain well below historical averages (at 3-4% over the next 12 months). Smaller and weaker-rated companies in the energy sector have either restructured or built up liquidity buffer to weather through the next two years. We therefore expect limited further bankruptcies unless prices head back to last year's levels. Current yield at 6.3.0% to maturity and 6.0% to worst is attractive and compensating for the risks associated to the oil price. Monetary support by the ECB is an important tailwind for EUR HY. Current yield at 3.7% to maturity and 3.0% to worst still fairly compensate for the risk. Default rates in Europe are expected to remain low around 2% over 12 months. EU HY offer shorter duration (typically between 3 and 3.5 years) and a better credit quality than their American counterparts. Its lower exposure to commodity-sensitive sectors limits its default risk. Near-term risks from the banking sector.
- **Emerging Debt:** EM sovereign credit quality remains supported by strong public sector balance sheets and low external debt ratios. The sharp EM FX depreciation of the past years having resulted in current account improvements in EM countries. EM economies continue to move through a deleveraging cycle. Yields remain attractive on a relative basis to similar rated developed market bonds. Emerging market spreads were 310 basis points end-March from 342 basis points end-December. The index yield went from 5.8% to 5.47%. EM corporates will continue to benefit from supportive factors like commodity price stabilisation, improving political backdrops and local reform agendas. Issuance by most EM corporates is ultimately opportunistic as these best-in-class companies can usually fund themselves in their local markets when capital market conditions do not suit them. History has shown EM corporates market is quite immune to rising rates and commodity price volatility. EM corporate defaults is likely to have peaked. EM is not heterogeneous asset class, differentiation remains a decisive factor of excess returns. Unless we face extreme scenario including a sudden spike in US rates and outflows, we expect the asset class to outperform other FI assets.

Asset Allocation summary

<i>Short term view</i>			<i>Medium term view</i>		
Global allocation (in %)	current	Neutral	Global allocation (in %)	current	Neutral
Equities US	32.85	28.49	Equities US	32.85	28.49
Equities Europe	23.56	10.23	Equities Europe	23.56	10.23
Equities Japan	0.00	3.92	Equities Japan	0.00	3.92
Equities GEM	8.65	7.37	Equities GEM	8.65	7.37
total equities	65.06	50.00%	total equities	65.06	50.00
Futures US	-12.71	0.00%	Futures US	0.00	0.00
Futures EU	-10.57	0.00%	Futures EU	0.00	0.00
Futures JP	0.00	0.00%	Futures JP	0.00	0.00
Futures EM	0.00	0.00%	Futures EM	0.00	0.00
total futures	-23.28	0.00	total futures	0.00	0.00
Equities net US	20.14	28.49	Equities net US	32.85	28.49
Equities net EU	12.99	10.23	Equities net EU	23.56	10.23
Equities net Japan	0.00	3.92	Equities net Japan	0.00	3.92
Equities net EM	8.65	7.37	Equities net EM	8.65	7.37
Total equities net	41.78	50.00	Total equities net	65.06	50.00
Bonds DM Sovereign	1.29	29.50	Bonds DM Sovereign	1.29	29.50
Bonds DM corporate IG	6.09	14.00	Bonds DM corporate IG	6.09	14.00
Bonds DM Corporate High Yield	14.05%	3.50	Bonds DM Corporate High Yield	14.05	3.50
Bonds EM sovereign + corp	7.39	3.00	Bonds EM sovereign + corp	7.39	3.00
Total bonds net	28.81	50.00	Total bonds net	28.81	50.00
Gold	0.00	0.00	Gold	0.00	0.00
Mixed	0.00	0.00	Mixed	0.00	0.00
Cash	6.13	0.00	Cash	6.13	0.00
Total	100.00	100.00	Total	100.00	100.00

- *The fact that the world can change in unexpected ways underlines the need for a flexible and diversified portfolio*

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