



Asset Allocation Outlook

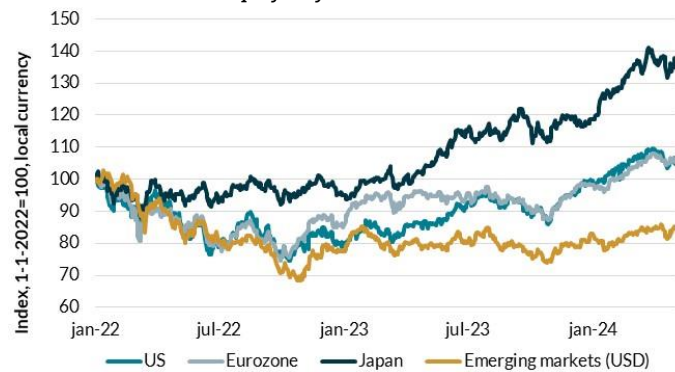
May 2024

- Eurozone economy exits recession, US stable
- Uncertainty surrounding outlook for earnings
- Investment policy unchanged

April was a difficult month for investors as both equities and bonds lost ground, incidentally without causing significant panic. Although an upturn was visible in the VIX index, which measures US equity volatility, it was of shorter duration and less pronounced than in October last year. The MSCI global equity index noted its first monthly downturn since October last year. This downturn derived from industrialised nations. Remarkably enough, given the turbulence in currencies, the emerging market index noted a small upturn. This tells us the origin of the turbulence - interest rate fears in the US - and explains why equities fell more sharply in the US than in the Eurozone or Japan.

index noted a positive result. Oil prices remained more or less unchanged, but the price of gold climbed higher and copper in particular shot up in price. The prospect of diverging monetary policies in the US, where interest rates will be cut at a later date, and many other countries, where interest rates could come down sooner, caused the US dollar to appreciate. The Japanese yen fell especially sharply, but emerging market currencies were also squeezed. This in turn led to wider spreads on bonds issued by these countries. In short, an uncertain investment climate in which we've retained our investment policy with a neutral outlook for equities.

Interest rate fears cause equity rally to stall



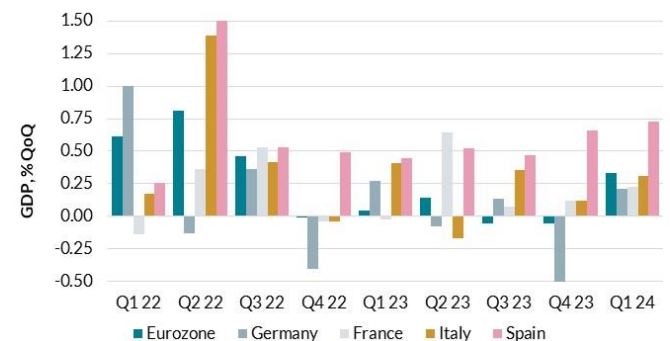
Source: Refinitiv, Van Lanschot Kempen

Bond yields climbed considerably in the US, both at the short and long end of the yield curve. Yields in the Eurozone, UK and to a lesser extent Japan were pulled upwards in their wake, leading to marginally negative returns on government bonds. The same goes for credits, the spreads of which remained virtually unchanged. Real estate likewise noted a weak performance, with the biggest losses again being in the US. The Bloomberg commodity

Eurozone economy picking up, US stable

In the first quarter of this year, the Eurozone economy grew by 0.3% versus the fourth quarter of last year.

Eurozone economy returns to growth after year of stagnation



Source: Refinitiv, Van Lanschot Kempen

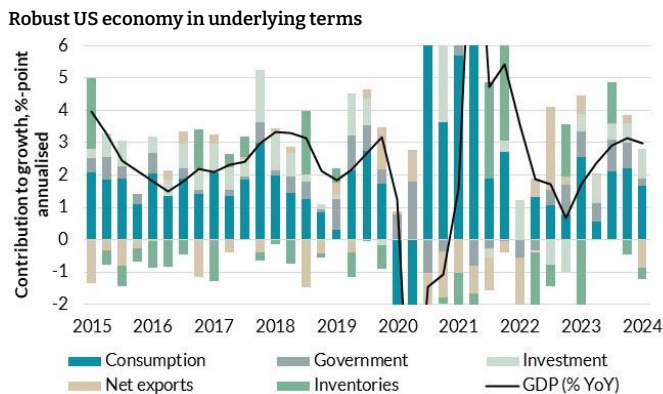
This was slightly higher than economists had expected. A downward adjustment to growth in the fourth quarter of last year meant that the Eurozone just managed to escape a technical recession, i.e. two consecutive quarters of



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contraction. This contraction has now been brought to an end. The composition of the growth is not yet known but it looks as if consumer spending contributed positively, especially on services in light of the upturn in the purchasing manager index (PMI) for this sector. What we do know is that growth was strong in Spain at 0.7%, followed by Italy at 0.3% and Germany and France both at 0.2%. Last month we wrote about green shoots in the Eurozone's economy and these are still visible. The PMI for the service sector rose further in April to its highest level since May last year. Germany's Ifo index climbed for the third month in a row and the fairly volatile ZEW index has been moving upwards for six consecutive months. We nevertheless believe that Eurozone growth is unlikely to be exuberant. The Economic Sentiment Index has spent several months hovering at a level that points to a stagnating economy. Consumer confidence improved in April but businesses in industry, retail and construction were in fact less optimistic. The PMI for industry also indicates that businesses in these sectors are pessimistic.

US growth declined to 1.6% in the first quarter versus the fourth quarter of last year when converted to an annual basis. In line with the method usually used in Europe, this translates into growth of 0.4%. This rate of 1.6% was significantly down on the preceding quarters and also lower than expected. However, the underlying data show that the US economy is more robust than this figure would suggest.



This is because trends in stock levels and foreign trade are greatly squeezing growth. Together these two components account for a negative contribution of 1.2 percentage points.

Stock levels and foreign trade tell us less about the strength of the domestic economy and are also fairly volatile. The domestic components of consumer spending, corporate investment and home construction made solid contributions to growth. It remains to be seen whether this robustness is sustainable. In contrast to the global trend, the US PMIs for industry and the service sector fell in April.

And consumer spending increased more sharply than incomes. This means consumers used their savings to keep their spending at the same level. The extremely low savings quota means this isn't tenable, all the more so because consumer confidence declined in April. The latter is undoubtedly linked to the downturns on the equity markets and higher petrol prices but also the worse-than-expected news on inflation in general, higher mortgage rates and signs that the job market is cooling. And given that mortgage rates have again surpassed 7%, it's not likely that home construction will pick up further. As a result, in our view a soft landing is more probable than a scenario in which growth remains very robust. By a soft landing we mean that economic growth continues to decline and the job market slows further but the economy doesn't enter into a recession.

In China, the economy grew by 5.3% in the first quarter versus the first quarter of 2023. The growth target of 5% that the Chinese government has set for 2024 therefore looks to be feasible, as long as the economy doesn't slow too much. March saw a decline in growth in retail sales, industrial production and bank lending, however. When it comes to growth, China is relying too heavily on investment, production and exports. The growing trade tensions between China and the US and Eurozone make this growth model vulnerable. As a result, a slowdown in growth is a risk in China as well, all the more so as the housing market remains extremely weak and the official PMIs for industry and especially the service sector were down as well.

ECB takes the lead

The Eurozone's economic cycle normally lags slightly behind that of the US. Yet the coronavirus pandemic has disrupted many historical economic correlations. Whereas the US government introduced substantial economic stimuli and US consumers eagerly took advantage of these, the Eurozone's economy stagnated in 2023. This reduces the capacity for further growth in the US, as a result of which inflation is coming down more slowly. This is visible in the consumer price index, which climbed by 3.4% on an annual basis in the first quarter. For the US economy as a whole, the increase in prices stood at 3.1%. Both these upturns translate into an acceleration versus the preceding quarter. Wage costs likewise increased more quickly in the first quarter than in the fourth quarter of last year. The high rate of inflation in the US is largely due to housing costs. As rental growth has declined, it's only a matter of time before housing cost growth also decreases, since this is based on rental growth. Persistent wage inflation is a bigger issue but signs that the labour market is cooling, such as the declining number of job vacancies, fewer

employees voluntarily resigning from their jobs and a growing number of announced redundancies, lead us to believe that wage increases will also decline.



It will take a while for all this to happen, however. Given the ongoing inflationary pressure, for the time being the Fed has insufficient evidence for cutting interest rates.

Headline inflation was unchanged in the Eurozone at 2.4% in April. Core inflation fell to 2.7%. This is its lowest level since February 2022, but even so the rate of inflation was higher than expected. The fact that core inflation is now coming down is mainly because the sharp price increases in early 2023 have dropped out of the inflation data. After all, inflation is the upturn in prices over a year. On a monthly basis, however, an acceleration is visible in core inflation, despite the moderate economic growth. Nevertheless, given the marginally cooling job market and lower wage growth, we expect inflation to come down further in the Eurozone.

This gives the ECB the opportunity to cut interest rates sooner than the Fed. The ECB has already clearly signalled its intention to reduce rates in June. Its communications on this have been consistent. A cut to interest rates in June has also been priced in by the markets for many months. We believe there's a high chance of the ECB pausing in July to see how inflation and wage costs evolve. It may well take further steps after this but more than three interest rate cuts this year would seem unlikely.

The chances of the Fed cutting interest rates in June are virtually zero. The US economy is too robust and inflation too high for this to happen. In retrospect, Fed Chair Powell's remarks at the end of last year about interest rate cuts were slightly premature. Pushing back the Fed's first interest rate cuts leads to fewer cuts being forecast for this year. One cut to rates has already been priced in but two no longer are. Job market trends continue to play a major role here. Job growth has so far remained strong but in surveys businesses are indicating caution about taking on

new personnel. A weakening job market could revive expectations for the number of interest rate cuts. In this respect, the forecast of a single cut to rates would seem to be on the conservative side. We believe two to three cuts are still possible this year. However, if the job market doesn't slow, it's possible that the Fed won't cut rates this year at all. Some claim that the presidential elections in November are restricting the Fed's freedom to act, but Powell categorically denied this during a press conference on 1 May. He insists that the Fed only does what's right for the US economy and takes no account of political events.

The Chinese central bank is having to contend with a totally different problem, namely deflation. In the first quarter of this year, the price index for the whole economy declined by 1.1% versus the first quarter of last year. China has been experiencing deflation for the past year, but the authorities haven't yet undertaken any decisive steps to put a stop to it. Reserve requirements for banks were reduced slightly last year, which was supposed to enable banks to lend more money. The liquidity this released has been skimmed off another way, however. Interest rates haven't been cut. There are therefore few stimuli for the demand side of the economy, while the policy of stimulating the economy via the supply side is in fact leading to overcapacity and in turn contributing to deflation. In our view, it would be better to stimulate demand. Recent comments show that the central bank isn't that worried but there's growing political pressure for it to act. As a result, cuts to interest rates cannot be ruled out.

As ECB President Lagarde put it recently: we're data-dependent, not Fed-dependent. In saying so she reaffirmed that, like most central banks, the ECB focuses primarily on the domestic economy. Yet interest rates being kept high for longer in the US does have an impact. Rising rates in the US pull Eurozone rates upwards in their wake, for instance because bond investors then think US bonds are more attractive than government bonds issued by Eurozone countries. This tightens monetary conditions, which could encourage central banks to cut interest rates. Such capital flows can also squeeze currencies, however. The euro has so far been largely unaffected this year at a depreciation of 3.2% against the US dollar, but the Japanese yen has already depreciated by nearly 11% and stands at its lowest level since April 1990. Remarks by Japanese monetary policymakers that for the time being interest rates wouldn't be raised further caused the yen to depreciate further. It looks as if the Bank of Japan has already intervened on the currency market and it appears to be applying a limit of 160 yen per US dollar. The weak yen in turn affects China, whose currency has remained stronger. This erodes China's competitive position. Chinese authorities could decide to devalue the renminbi but this didn't turn out that well in 2015. It wouldn't be well-

received in the current geopolitical climate either, as there are already concerns about cheap exports from China. Currencies are also under pressure in other emerging markets such as South Korea, Taiwan, Indonesia and Brazil, which restricts the options for central banks to cut interest rates. This led to some turbulence on the markets for government bonds, where spreads widened.

Emerging market currencies being squeezed by higher US interest rates



Source: Refinitiv, Van Lanschot Kempen

Positive corporate results go unrewarded

The earnings season is already fairly well advanced. In the US, two-thirds of the companies in the S&P500 have already published results over the first quarter of 2024, in the Eurozone about half. US companies are experiencing greater difficulties in meeting revenue expectations than earnings expectations. This shows that businesses are succeeding in keeping their profit margins at more or less the same level. Average earnings growth has so far been 5.1% versus the first quarter of 2023. This is lower than the earnings growth in the final quarter of last year, bucking the trend for upward earnings growth in the second half of last year. Yet earnings are still higher than expected, especially in the consumer discretionary (driven by Amazon) and communications services sectors (driven by Meta and Netflix). Sharp downturns in earnings can be found in the energy, basic industrial and healthcare sectors. The persistently strong growth has prompted analysts to adjust expected earnings for the coming twelve months upwards. Expected earnings growth over the next twelve months now stands at 11.5%. Such levels of earnings growth have historically been achieved when the economy accelerates. However, as the outlook is for a slight slowdown in growth and lower inflation, it could prove difficult for businesses to meet these expectations. It's telling that expected earnings growth over the first quarter was adjusted downwards during the quarter. Companies that caused positive earnings surprises largely went unrewarded on the market, while those that announced negative surprises were punished severely.

This demonstrates that expectations had risen substantially during the strong equity rally prior to this earnings season. We think there's uncertainty about earnings growth in the US. Moreover, US equities are expensive compared to bonds. We therefore retain our neutral position.

US earnings expectations look to be ambitious



Source: Refinitiv, Van Lanschot Kempen

Eurozone businesses are struggling to maintain their profit margins, which is no surprise in light of falling revenues. Revenues have so far dropped by an average of 2.4% and earnings by 14.2% versus the first quarter of 2023. This is in line with expectations for revenues, while the downturn is smaller than expected for earnings. The lower earnings can be found across the board. Only the IT, communications services and utilities sectors reported earnings growth. Eurozone businesses that announced negative surprises also came in for severe punishment, while positive surprises were only rewarded moderately. Expected earnings are no longer being adjusted downwards in the Eurozone. Earnings growth of 5.9% is expected over the next twelve months. This looks to be feasible as the economy is picking up marginally, but the pressure on margins poses a risk. Like in the US, an extremely positive scenario has been priced in following the equity rally of the past few months. We hold a neutral position in the Eurozone as well.

Investment policy unchanged

We've retained our neutral position in equities as part of our investment policy. Although we recognise the persisting robustness of the US economy and see some improvements in the Eurozone, we have our doubts as to whether economic growth, especially nominal growth, will be strong enough to meet earnings expectations. Furthermore, following the equity rally of the past few months an exceedingly positive scenario has now been priced in, making positive surprises less likely. Equities have been affected by interest rate fears in recent weeks. This is in contrast to the first three months of the year in

which rising interest rates and rising equities went hand in hand. However, the higher interest rates climb and the more equity valuations increase versus bonds, the greater the interest rate sensitivity of equities. This point was reached in the last few weeks. The uncertainty surrounding earnings, interest rates and the economic outlook have led us to retain our neutral position in equities.

We believe that bond yields will come down this year, especially at the short end of the yield curve. Despite the uncertainty surrounding inflation, we anticipate cuts to interest rates in the US, UK and Eurozone. As 10-year bond yields are considerably lower than 2-year yields, we only expect yields at the long end of the curve to come down slightly. We think spreads on credits are tight, especially in the US and to a lesser extent in the Eurozone. As a result, we prefer the Eurozone. We see no signs of spreads widening in the near future. Our outlook for high yield bonds is more cautious given that these companies are more aggressively financed and therefore affected more by higher interest rates. Emerging market debt generates an attractive return but the strong US dollar and turbulence this is causing on the currency markets in emerging markets show that there are risks. This is the reason for our neutral position.

We continue to view the uncertainty surrounding interest rates and potential downgrades to property valuations as too high to build a position in this asset class. As for commodities, our doubts mainly relate to the robustness of the Chinese economy.

Market review

Equities

	Index	Past month	Past 3 months	From 31-12-2023
Global (MSCI AC)	1053	-2.1%	2.7%	4.6%
Developed markets (MSCI World)	3322	-2.4%	2.3%	4.8%
Emerging markets (MSCI EM)	1053	0.3%	6.5%	2.8%
United States (S&P500)	5064	-2.7%	2.1%	6.2%
Eurozone (EURO STOXX 50)	506	-2.0%	5.0%	6.7%
United Kingdom (FTSE 100)	8172	3.0%	7.3%	5.7%
Japan (Topix)	2729	0.5%	7.4%	15.3%
Netherlands (AEX)	879	-0.3%	6.8%	11.7%

Government bonds (10-year)

	Yield (%)	Past month (bp)	Past 3 months (bp)	From 31-12-2023 (bp)
United States	4.58	22	55	71
Japan	0.90	15	25	27
Germany	2.55	14	32	52
France	3.05	12	32	49
Italy	3.87	7	6	16
Netherlands	2.85	17	33	53
United Kingdom	4.29	20	37	75

Investment grade credit

	Risk premium (bp)	Past month (bp)	Past 3 months (bp)	From 31-12-2023 (bp)
United States	90	-3	-12	-14
Eurozone	112	0	-18	-23

High yield bonds

	Risk premium (bp)	Past month (bp)	Past 3 months (bp)	From 31-12-2023 (bp)
United States	316	-7	-31	-18
Eurozone	351	-7	-24	-44
Emerging markets (USD)	379	38	-15	-5
Emerging markets (Local currency)	201	4	-15	-34

Real estate

	Past month	Past 3 months	From 31-12-2023
Global	-2.2%	-2.1%	-6.6%
North-America	-3.0%	-4.1%	-7.6%
Europe	1.0%	1.0%	-4.7%

Commodities

	Past month	Past 3 months	From 31-12-2023
Bloomberg index	0.1%	4.3%	2.2%
Base metals	9.3%	13.5%	8.7%
Brent oil (USD per barrel)	83.72	8.0%	7.8%
Gold (USD per troy ounce)	2302	13.1%	11.5%

Returns in local currency

bp = basis point (0.01%)

Data as of 5 May 2024

Source: Refinitiv

Tactical outlook

Asset class	
Equities	Neutral
<p>The global equity index fell in April. This was mainly due to interest rate fears in the US, which experienced the biggest losses, followed by the Pacific region. The downturn in the latter region came partly from Japan, but losses were higher in Australia. Losses in the Eurozone fell between the US and Pacific. Emerging markets closed the month more or less unchanged, which is remarkable given the rather jittery market climate and turbulence in the currencies of these countries. Higher interest rates finally succeeded in bucking the upward trend in equities, although the damage is limited. The higher interest rates rise, however, the greater the risk for equities. Our neutral position reflects the uncertainty surrounding interest rate trends but also the risk of earnings expectations not being met, especially since markets have already anticipated sharply higher earnings. We currently hold a neutral positioning for the underlying regions within equities.</p>	
Government bonds	Overweight
<p>Bond yields climbed sharply in the US in April; 2-year yields by 40 basis points and 10-year yields by 47 basis points. This reflects the robust growth and stubborn inflation in the first quarter. Expectations for interest rate cuts by the Fed have consequently been pushed back. We think the market's forecast of a single cut to rates this year is on the conservative side. If the economy slows further and inflation comes down slightly more, this will create capacity for more cuts. Market interest rates will then also be able to come down, especially at the short end of the yield curve. We hold an overweight in US government bonds but this is mainly due to our underweight in US investment grade credits. Yields changed by a smaller amount in Germany, with upturns of 21 basis points for 2-year yields and 29 basis points for 10-year yields. However, as in the US, this resulted in a negative return on government bonds. Via a number of steps, we've moved to a neutral position in Eurozone government bonds. This reflects our view that yields have already peaked. We nevertheless believe it's too soon to commit further to lower interest rates in the Eurozone. The ECB will probably cut interest rates in June but after this wait and see how the economy and inflation evolve. As 10-year bond yields are considerably lower than 2-year yields, we think yields at the long end of the curve are unlikely to come down much.</p>	
Investment grade credits	Underweight
<p>Spreads on US investment grade credits tightened slightly in April but remained unchanged in the Eurozone. The upturn in underlying yields on government bonds led to bonds from both regions noting losses. We think the tight spreads are at odds with economic indicators that in many cases are pointing to a slowdown in growth in the US and moderate growth in the Eurozone. Furthermore, the higher market interest rates are causing a deterioration in the ratio of corporate results and interest charges. Exposure to commercial real estate poses a risk for some US and German banks. US spreads are more than 35 basis points below the average for the past five years, Eurozone spreads nearly 20 basis points. Spreads currently account for a historically small portion of the interest compensation on credits. This makes them less attractive versus government bonds. Within investment grade credits we have a relative preference for the Eurozone versus the US. Spreads are marginally wider in the Eurozone and interest rate sensitivity is lower.</p>	
High yield credits	Underweight
<p>Although the market for high yield credits didn't entirely escape the interest rate fears that affected US equities in April, spreads only widened very slightly at 6 basis points. In the Eurozone, spreads tightened by a minimal 2 basis points. The lower interest rate sensitivity and higher interest compensation on these bonds meant that they earned a slightly better return than their investment grade counterparts. Like investment grade credits, high yield credits have lost some of their relative attractiveness versus government bonds thanks to the higher yields in the latter asset class. Yet our negative outlook for this asset class primarily derives from the fact that the market for high yield bonds is totally ignoring the possibility of a further slowdown in growth. Rating agency Moody's thinks the global default rate peaked in January but rival agency S&P expects the insolvency rate to rise slightly higher. Spreads stood at 318 basis points in the US at the end of April, in the Eurozone at 350 basis points. This is considerably lower than the average of the past five years for both regions. We view a rising default rate as a downward risk. Companies in this asset class are especially vulnerable to higher interest rates in our opinion. Businesses are often more aggressively financed, frequently also partly via bonds with flexible interest rates and bond durations are shorter on average.</p>	
Emerging market debt	Neutral
<p>Emerging market debt issued in US dollars noted a negative return in April. Spreads widened by 31 basis points, the biggest increase since March 2023. Higher US bond yields also contributed to the negative result. Emerging market debt in local currency likewise earned a negative return. Interest rate fears in the US caused turbulence in emerging market currencies. This makes it more difficult for central banks in these countries to cut policy interest rates, which in turn pushes up market interest rates. We find the interest compensation on emerging market debt issued in US dollars attractive but the uncertainty surrounding inflation and interest rates in industrial nations and the appreciating US dollar pose risks. Bonds listed in local currency could profit from declining inflation, but central banks in these countries have little room for manoeuvre as long as</p>	

Asset class

the Fed keeps interest rates high. Moreover, the interest compensation is relatively low versus developed countries and this reduces the relative attractiveness.

Listed real estate

Neutral

The sensitivity of listed real estate to interest rates was again demonstrated in April. The global real estate index dropped more sharply than the global equity index and here, too, US real estate noted the biggest losses. Listed real estate has also noted a negative performance in the US and Europe over 2024 so far. We hold a neutral outlook for this asset class. Valuations are relatively low versus general equities but not versus interest rates. In the short term we don't anticipate interest rates coming down enough and continue to be extremely concerned about financing in the real estate sector. Tighter lending conditions at banks complicate access to (re)financing and exert upward pressure on interest charges. Despite the fact that transactions have recently picked up somewhat, they remain at low levels. Property prices could continue to fall before the number of transactions normalises further.

Commodities

Neutral

Oil prices remained virtually unchanged on balance in April. Despite tensions between Iran and Israel during the month, the geopolitical situation hasn't yet given rise to fears about oil production or oil embargos. The Bloomberg general commodity index noted a small positive return. This was mainly driven by metals, most notably copper and gold. Copper is seen as a barometer for the global economy. Yet April's upturn in the copper price was accompanied by sharply higher stock levels in China, which in itself is not a positive sign. The ailing global industry and worse-than-expected sales of electric vehicles are in our opinion also negative signals for metals, including copper. Gold continued March's price rises but climbed at a slower pace. From a cyclical perspective, we don't think this is the right time to build up a position in commodities. The limited fiscal stimuli in China, which are leading to moderate growth in investment in infrastructure and homes, restrict the potential for upturns in metal prices. The oil market is tight, but oil-producing countries have sufficient capacity to increase production if oil prices rise sharply. The high gold price is primarily the result of expansionary monetary policies and the large amount of liquidity this has created, as well as gold purchases by central banks. Gold is an interesting investment at times of uncertainty but given its high price a large amount of uncertainty and/or lower interest rates have already been priced in.



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