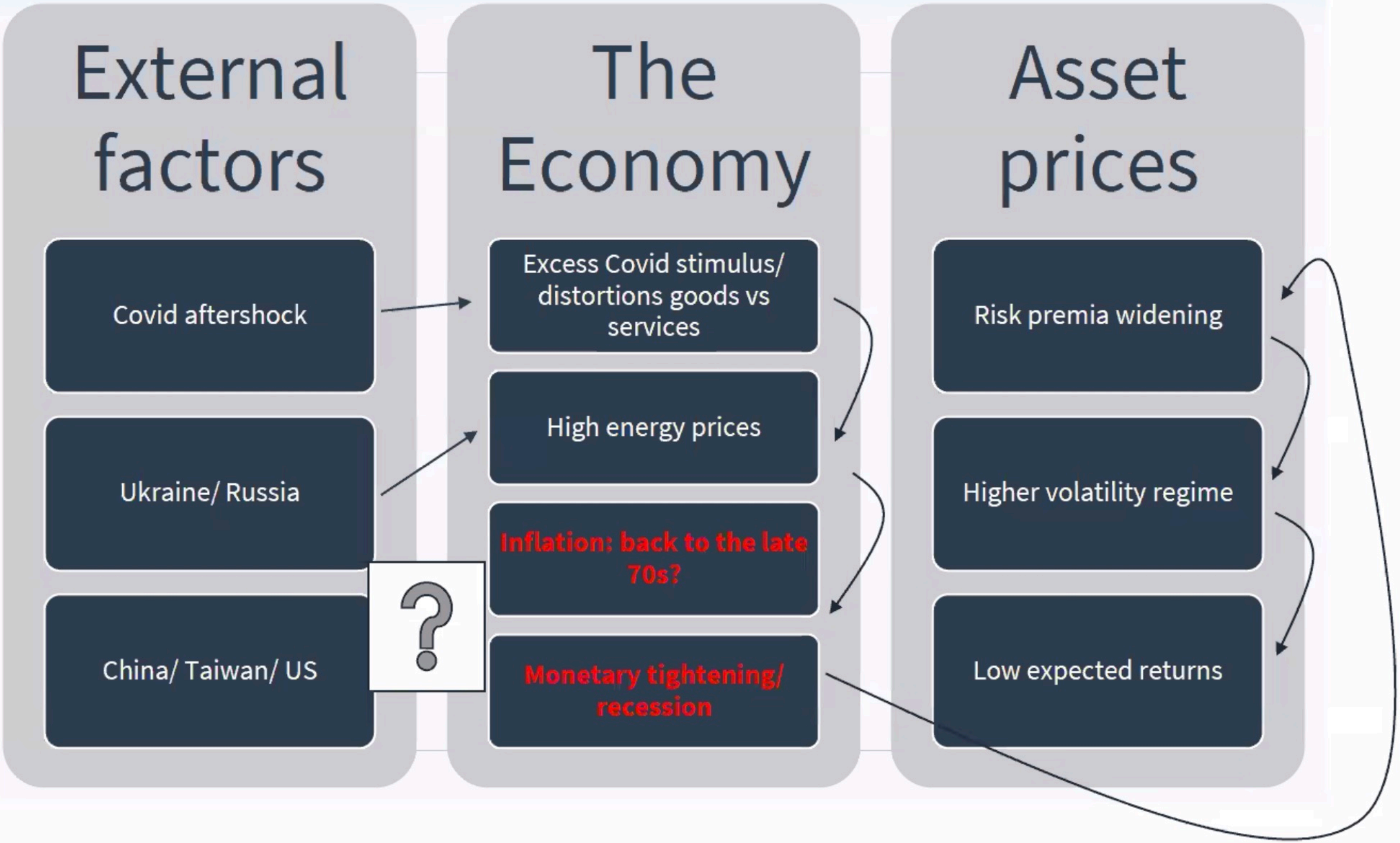
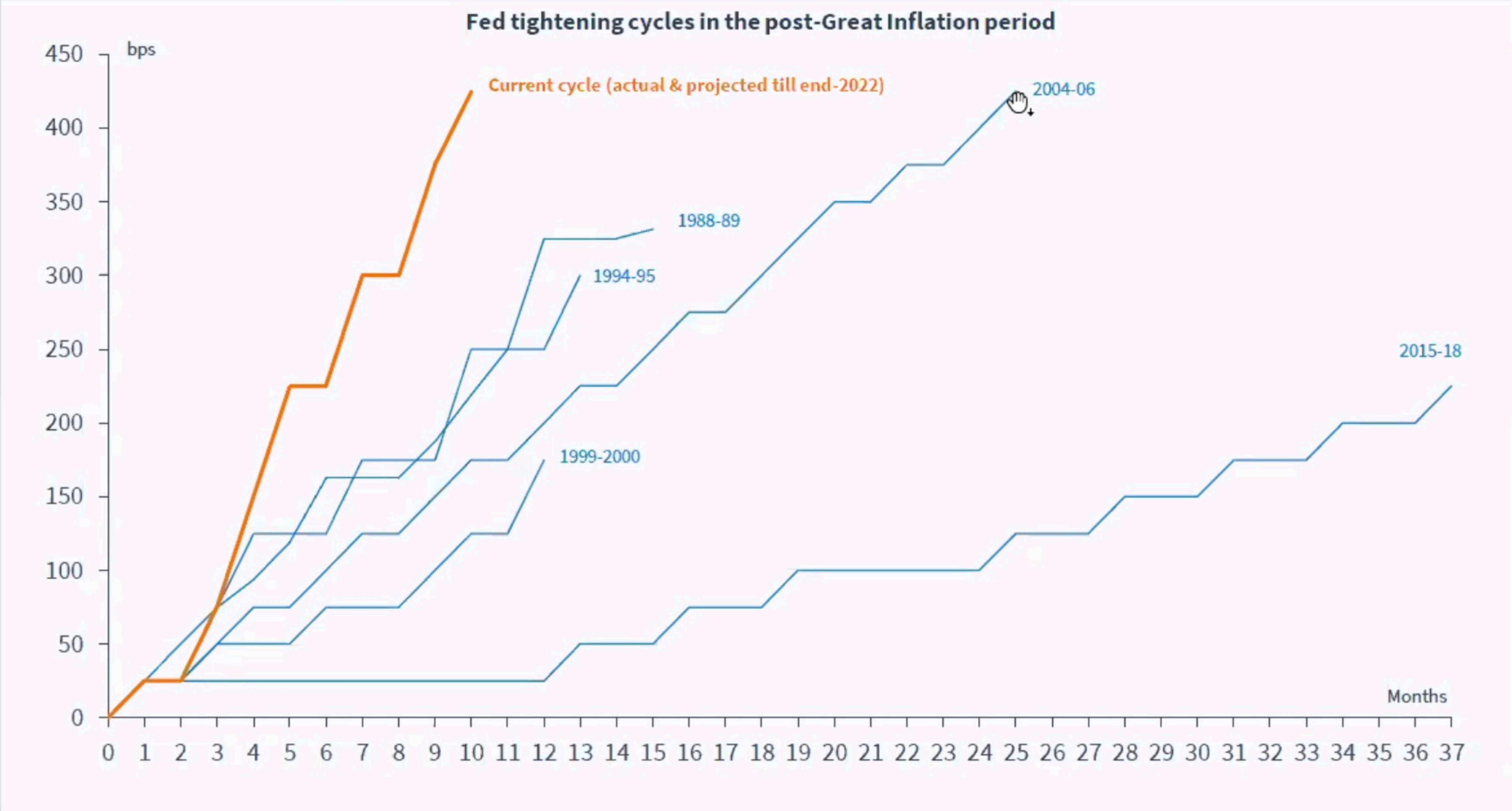
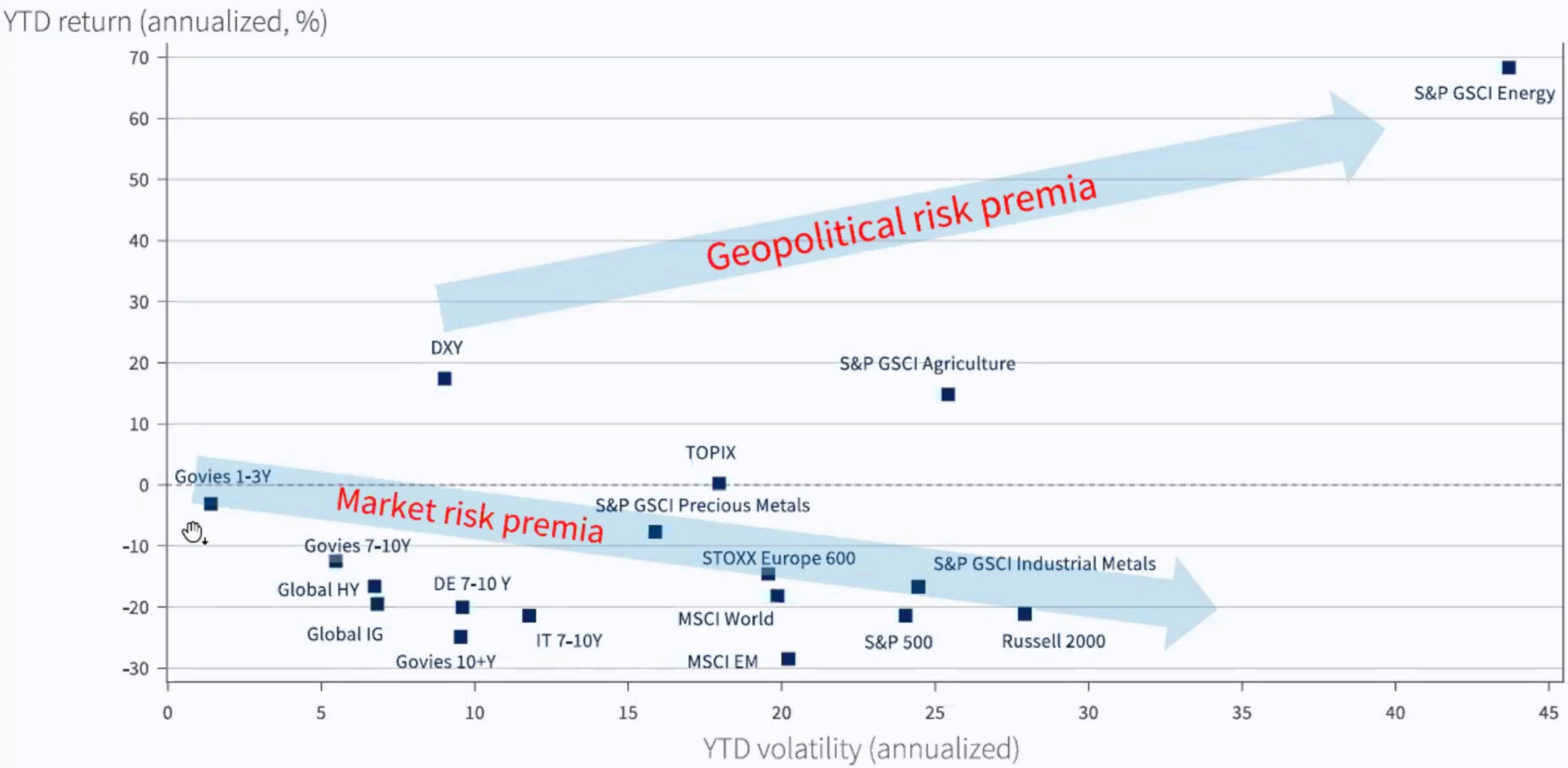

External factors
The Economy
Asset prices
Covid aftershock
Ukraine/ Russia
China/ Taiwan/ US
?
Excess Covid stimulus/ distortions goods vs services
High energy prices
Inflation: back to the late 70s?
Monetary tightening/ recession
Risk premia widening
Higher volatility regime
Low expected returns

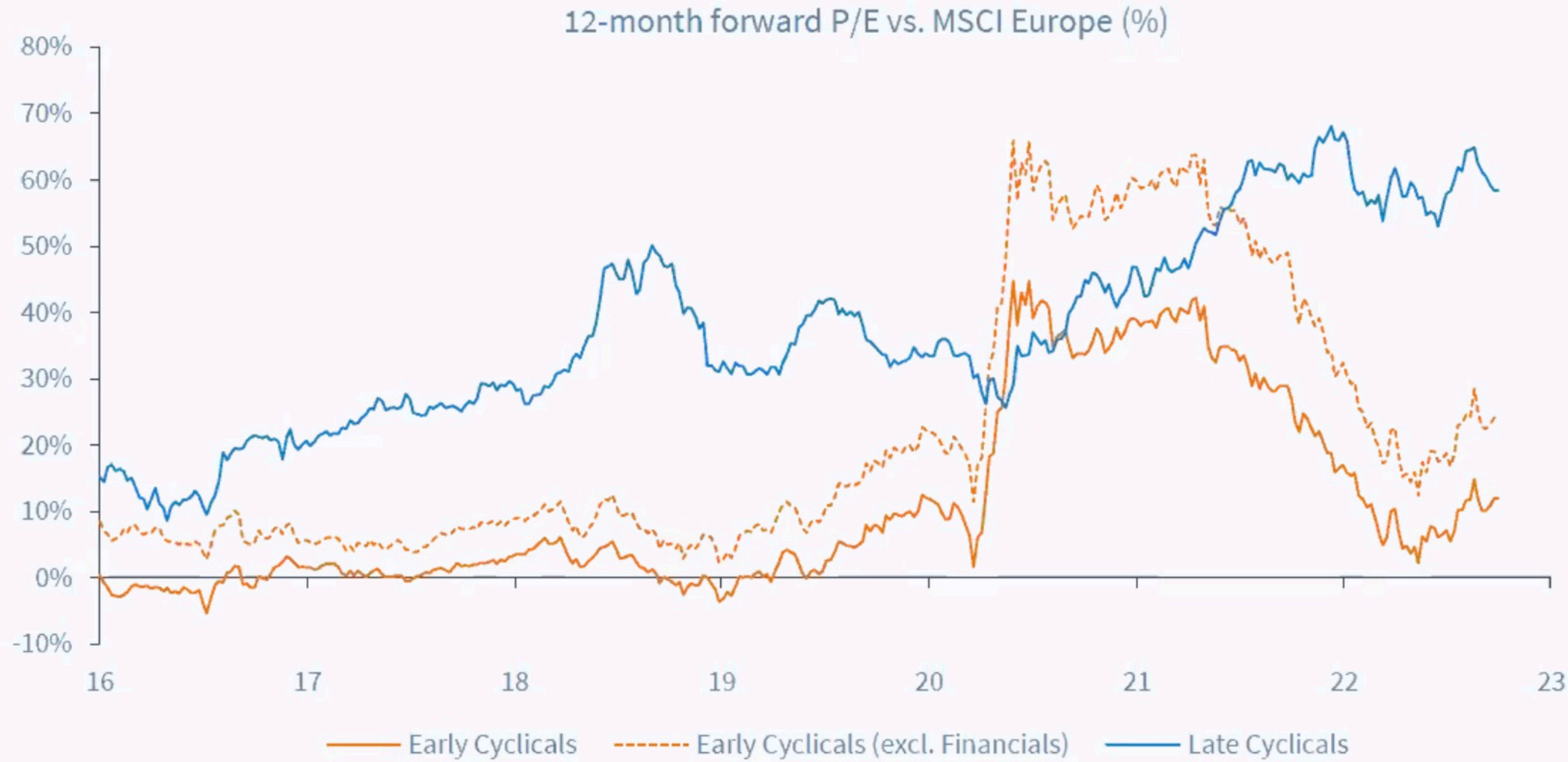
# 2022/23 rates hikes in historical context: bottom to peak




Source: Board of Governors of the Federal Reserve System, Kepler Cheuvreux


YTD return (annualized, %)
70
60
50
40
30
20
10
0
-10
-20
-30
Geopolitical risk premia
Market risk premia
S&P GSCI Energy
DXY
S&P GSCI Agriculture
TOPIX
Govies 1-3Y
S&P GSCI Precious Metals
Govies 7-10Y
STOXX Europe 600
S&P GSCI Industrial Metals
Global HY
DE 7-10 Y
MSCI World
Global IG
IT 7-10Y
S&P 500
Russell 2000
Govies 10+Y
MSCI EM
0
5
10
15
20
25
30
35
40
45
YTD volatility (annualized)

# The relative valuation of « early » and « late » cyclical sectors in Europe (MSCI universe)

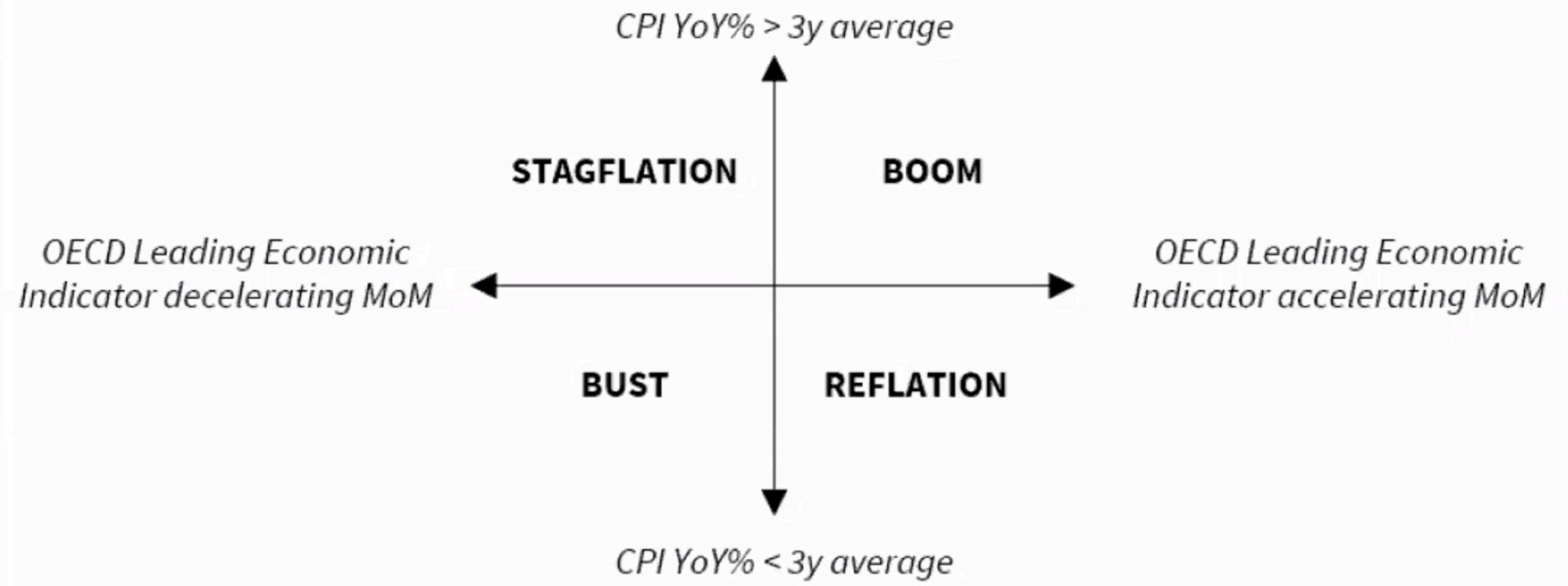



**Early cyclicals** = Autos, Banks, Consumer Services, Diversified Financials, Materials, Retailing, Semiconductors, Transportation (MSCI, equal-weight)

**Late cyclicals** = Commercial & Prof. Svs., Consumer Durables & Apparel, Media & Entertainment, Software & Services (MSCI, equal-weight)

Source: Datastream, Kepler Cheuvreux

## A simple framework for the changes in the economic environment




## The average relative MoM performance by sector in Europe according to four stylised economic & inflation regimes

| Macro environment | Comm. Svs. | Discr. | Staples | Energy | Financials | Health. | Indus. | IT | Mats. | Real Est. | Util. |
|---|---|---|---|---|---|---|---|---|---|---|---|
| *Boom* | -1.09% | -0.01% | -0.29% | 0.11% | 0.54% | -0.12% | 0.06% | 0.16% | 0.63% | 0.23% | -0.29% |
| *Reflation* | -0.07% | 0.62% | -0.87% | -0.31% | 0.25% | -1.05% | 0.83% | 1.23% | 0.53% | -0.31% | -0.79% |
| *Stagflation* | -0.34% | -0.21% | 1.05% | 0.69% | -0.74% | 1.50% | -0.36% | 0.01% | -0.47% | -0.27% | 0.56% |
| *Bust* | 0.43% | -0.36% | 0.94% | -0.31% | -0.34% | 0.91% | -0.24% | -0.18% | 0.06% | 0.09% | 0.60% |

| Sector | Strong UW | UW | N | OW | Strong OW | Rationale | Weight in MSCI EUROPE | P/E (12mf) | P/B (12mf) | Div. yield (12mf) | Beta 2Y |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Communication Services** | | | | ● | | **Defensive, attractive dividend yield, sheltered from energy & supply chains disruptions** | **3.6%** | **13.1** | **1.3** | **4.8%** | **0.77** |
| Media & Entertainment | | ● | | | | Bulk of the sector is cyclical (exposed to the ad spending) but a few large growth stocks still too expensive | 1.0% | 14.2 | 1.5 | 2.9% | 1.08 |
| Telecom Services | | | | ● | | Low-beta, high dividend yield, capex spending cycle behind us, less vulnerable to supply issues | 2.7% | 12.7 | 1.2 | 5.5% | 0.66 |
| **Consumer discretionary** | | ● | | | | **Cyclical nature, scissors effect from inflation (squeeze on revenues & input costs increase)** | **10.4%** | **11.3** | **1.5** | **3.4%** | **1.30** |
| Automobiles & Components | | ○ → | ● | | | Bottom valuation on P/BV. Already depressed global production. Under owned. | 2.5% | 5.0 | 0.7 | 6.3% | 1.36 |
| Consumer Durables & Apparel | | ● | | | | Wealth destruction likely a late cyclical driver, Expensive again after strong Q3 rebound. West-China confrontation | 5.2% | 17.6 | 2.9 | 2.6% | 1.30 |
| Consumer Services | ○ → | ● | | | | Purchasing power squeeze should weigh on leisure demand post-summer, wage growth pressure (labour intensive) | 1.3% | 20.0 | 3.1 | 2.3% | 1.28 |
| Retailing | ○ → | ● | | | | Purchasing power squeeze while input costs surge, large share of expensive online retailers | 1.4% | 20.3 | 1.8 | 2.2% | 1.21 |
| **Consumer Staples** | | | ● ← | ○ | | **Defensive option in the consumer space, more pricing power** | **14.3%** | **17.5** | **3.0** | **3.1%** | **0.67** |
| Food & Staples Retailing | | ● | | | | Defensive but lower pricing power, consumers trading down to private labels, discount retailers gaining market share | 1.0% | 12.6 | 1.4 | 3.9% | 0.67 |
| Food, Beverage & Tobacco | | | ● ← | ○ | | Strong relative performance behind us, reopening post covid helped 1H22, Now close to peak relative valuation | 9.6% | 17.7 | 3.1 | 3.0% | 0.68 |
| Household & Personal Product | | | | ● | | Strong pricing power as F&B but less exposed to reopening tailwinds. Lower oil helps. | 3.7% | 19.2 | 4.1 | 2.9% | 0.68 |
| **Energy** | | | | ● ← | ○ | **Higher O&G prices for longer, key player in energy transition, strong dividends** | **6.5%** | **4.7** | **1.0** | **5.0%** | **1.01** |
| **Financials** | | ● | | | | **Recession fears impacting cost of risk and credit spreads. Huge monetary policy changes create tail risks** | **15.9%** | **7.9** | **0.8** | **5.9%** | **1.21** |
| Banks | | ● | | | | Rising interest rates paying for higher cost of risk on an excel sheet but rising sovereign risks, Waiting for rates peak. | 7.3% | 6.7 | 0.6 | 6.8% | 1.32 |
| Diversified Financials | | ● | | | | Mixed-bag sector, overall vulnerable to downturn in equity markets, private equity tail risks | 3.6% | 10.0 | 0.8 | 3.6% | 1.19 |
| Insurance | | ● | | | | Sector losing its defensive shine as huge rates adjustment creates tail risks | 5.0% | 9.1 | 1.1 | 6.1% | 1.06 |
| **Europe** | | | | | | | - | **11.0** | **1.6** | **3.9%** | - |

| Sector | Strong UW | UW | N | OW | Strong OW | Rationale | Weight in MSCI EUROPE | P/E (12mf) | P/B (12mf) | Div. yield (12mf) | Beta 2Y |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Healthcare** | | | | ● | | **Defensive, earnings visibility, pricing power (Pharmas)** | **15.9%** | **14.7** | **3.2** | **2.9%** | **0.66** |
| Healthcare Equipment & Services | | ● | | | | More cyclical than Pharmas, impacted by logistics issues, high valuation | 1.7% | 16.5 | 1.8 | 2.2% | 0.92 |
| Pharmaceuticals & Biotechnology | | | | | ● | Defensive, earnings quality, low exposure to 'risk themes' (energy, cost inflation, consumer spending), USD sensitivity | 14.2% | 14.5 | 3.5 | 2.9% | 0.62 |
| **Industrials** | | ● | | | | **Large share of cyclical exposure despite structural growth, high valuations** | **14.0%** | **13.5** | **2.4** | **3.3%** | **1.14** |
| Capital Goods | | ● | | | | Overall expensive, manufacturing PMIs expected to decelerate further, Defence stocks attractive | 10.5% | 14.1 | 2.3 | 3.1% | 1.22 |
| Commercial & Professional Services | | ● ← | ● | | | Low beta overall (earnings visibility), but demanding valuation/low dividend support | 2.1% | 18.6 | 5.6 | 2.6% | 0.83 |
| Transportation | | ● → | ● | | | Early cyclical sector, overall sensitive to global trade | 1.4% | 8.1 | 1.6 | 5.1% | 1.05 |
| **Information Technology** | | ● ← | ● | | | **High beta, over-valuation created by Covid not yet fully corrected, China exposure** | **7.0%** | **18.1** | **3.6** | **1.6%** | **1.32** |
| Software & Services | | ● ← | ● | | | Defensive but still high valuations, wage inflation to bite, huge margins gains in recent years | 2.9% | 19.5 | 3.1 | 1.6% | 1.13 |
| Technology, Hardware & Equipment | | | ● | | | Small segment within IT, Lower valuation than rest of IT sector ("more value") | 1.0% | 12.5 | 1.9 | 2.5% | 1.06 |
| Semiconductors | | ● | | | | De-rating not yet over for expensive stocks in the sector, cyclical nature, high inventories at customers | 3.1% | 19.7 | 6.4 | 1.3% | 1.58 |
| **Materials** | | ● | | | | **Industrial commodities are more cyclical, but valuation remains overall cheap** | **7.2%** | **9.2** | **1.4** | **5.3%** | **1.07** |
| Chemicals | | ● | | | | Mixed sector dominated by large defensive stocks subject to rising rates headwinds, Early cyclical for the others | 3.4% | 14.4 | 2.0 | 3.7% | 0.96 |
| Construction Materials | | ● | | | | Huge CO2 emitter, Late-cyclical, US/EU residential slowdown with rising rates, energy squeeze, Infra spending a positive | 0.7% | 9.3 | 0.9 | 4.8% | 1.16 |
| Containers & Packag., Paper & Forest Prod. | | ● | | | | Cyclical sector, correlation between manufacturing PMIs and pulp prices | 0.7% | 12.4 | 1.4 | 3.8% | 1.17 |
| Metals & Mining | | | ● | | | Underlying industrial metals prices are sensitive to economic downturn but energy transition support, deep value already | 2.3% | 5.7 | 1.1 | 8.2% | 1.19 |
| **Real Estate** | | | | ● | | **Real yields rebound hurting the sector, but 40% assets price correction already in share prices, Defensive cashflows** | **0.9%** | **11.4** | **0.6** | **6.1%** | **1.02** |
| **Utilities** | | | ● | | | **Defensive in principle but sector upside down with gas supply crisis, high dividend yield** | **4.3%** | **13.7** | **1.6** | **5.2%** | **0.79** |
| **Europe** | | | | | | | - | **11.0** | **1.6** | **3.9%** | - |

# Strategic balanced asset allocation (*)

| | | |
|---|---|---|
| **EQUITIES (UW) 40%** | US 15% (-5)<br>Europe 10% (+5)<br>EM ex-China 15% | • Monetary tightening cycle is still some months away from the peak Valuation aren't so attractive yet, except in Europe. An earnings recession looms<br>• US equities downgraded to UW, European equities upgraded to Neutral, we are Overweight on EM (ex-China)<br>• EM: higher growth, lower inflation than in DM. Monetary tightening coming already to an end |
| **SOVEREIGN BONDS (sOW) 30%** | US 10% (-5)<br>Japan 0% (-5)<br>UK (10%)<br>Germany 5%<br>France 5% | • Overweight Govies. We are shifting from Treasuries to Gilts<br>• Our stance on duration stand close to Neutral (~10y)<br>• The looming growth deceleration has inverted yield curves. No steepening in sight for the time being |
| **CREDIT OW 15% (+5%)** | IG $ 6.5% (=)<br>IG € 8.5% (+5%) | • Our stance on credit was upgraded to OW, a preference for IG vs. HY<br>• IG credit should benefit from wide spreads and limited risk<br>• HY is exposed to the growth slowdown and the rise in default rates |
| **COMMODITIES N 5% (-5%)** | Gold 0% (-5%)<br>Commodities 5% (=) | • Commodities are an hedge vs. geopolitical risks<br>• The rise in real yields is expected to remain a headwind for Gold |
| **CASH OW 10%** | | • OW cash in current market conditions that are likely to remain volatile<br>• Prefer cash in USD for the carry |
| **FX** | | • We maintain a long USD stance, consistent with our Defensive positioning but we eased the long USD bias after the rally in Q3 |