DECEMBER 2021

Consensus Outlooks 2022

Investment and Portfolio Advisory

Rothschild & Co
Wealth Management

1

Executive Summary

1.1 Summary of Rothschild & Co and the Street's view

In 2022, the speed of monetary policy will determine market movements

Key Drivers

- Consensus agrees that 2022 will bring macro and policy considerations back to the forefront of investor decision-making, whilst virus concerns and geopolitical tensions take a back seat.

- Divergence in monetary policy between the United States and Europe is the central scenario for Rothschild & Co and most brokers, although some expect the Fed to pivot in the second half of 2022 and push back rate rises to 2023, as easing bottlenecks and more modest inflation in the US allow the Fed to take its time for rate normalisation and focus on full employment, without the economy overheating.

- The speed at which the Fed tapers its QE programme and raises rates will depend on the inflation trajectory and on employment data. In Europe, brokers agree with Rothschild & Co that the ECB will not raise rates in 2022.

- Despite Central Banks gradually tightening policy, liquidity remains abundant and global demand remains strong, favouring continued expansion, which should benefit risk assets such as equities and credit, as well as commodities.

- In the case of households, a mix of pent-up demand, high cash savings, redistributive fiscal policies and continued loose monetary policy favour lower income segments, supporting continued demand for physical goods and commodities (for construction, for example), especially as restrictions and bottlenecks subside.

- In the case of corporates, high cash levels on balance sheets pave the way for continued share buybacks, increased dividend payouts and investments.

- Corporate earnings have been remarkably resilient in 2021, despite higher input costs. One open question for 2022 is whether companies will continue to deliver such robust profits as we move through the cycle and rates rise.

Equities

- Brokers share Rothschild & Co's preference for equities over other assets in 2022, amongst ongoing inflation concerns and expected monetary tightening.
- In terms of regions, views diverge. Consensus favours Japan and Europe over the US, and one broker expects the highest returns from Emerging Markets, whereas we remain positive on the US and EM Asia.

Fixed Income

- Ten-year yields in the US and Europe should move modestly higher, with real yields also rising as inflation moderates.
- Bond valuations remain very high, and a steepening yield curve, especially in Europe, means investors should favour shorter duration bonds.
- Tight spreads leave limited room for further compression.

Commodities

- Brokers point to robust global demand for cyclical commodities, despite a slowdown in China. This should support oil, especially in H1 as inventory levels are at multi-year lows, before supply catches up in H2 and prices moderate.
- The outlook for gold is more muted in the face of rising real yields and a stronger dollar.

Currencies

- Monetary policy divergence between the US and Europe, as well as rising rates in Emerging Markets could see the return of noisier FX markets and the FX carry trade in H1.
- For H2, brokers diverge in views – those predicting faster monetary normalization in the United States see the USD gaining further against peers; those that expect the Fed to pivot as inflation slows and push back interest rate rises to 2023 are more bearish on the USD, especially amid high USD valuation.
- Consensus is bearish on low yielding currencies EUR, CHF and JPY.

2

Our view - Rothschild & Co

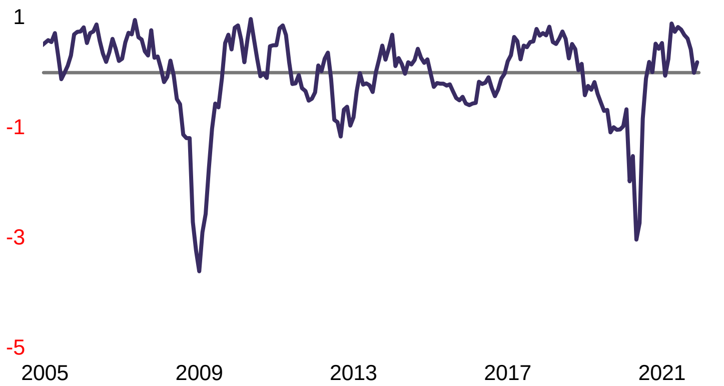
2.1 Economic overview

Above-trend growth may bring tighter policy

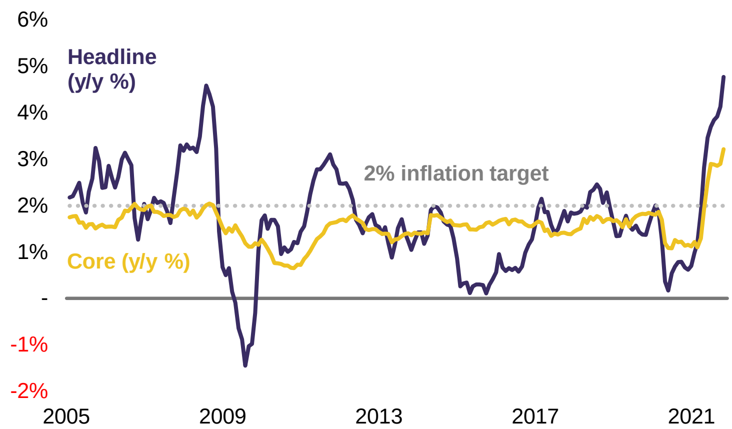
The main post-pandemic rebound is behind us, but underlying inflation risk may persist. Central banks may have to act more decisively than money markets expect.

- Virus permitting – Omicron's arrival has yet to change the economic arithmetic - growth can continue at an above-trend pace. Bottlenecks may ease, and workforce participation may revive; meanwhile, pent-up private demand may continue to be amplified by loose monetary policy and augmented by public spending programmes. Growth may slow, but perhaps not far: the margin of unused capacity may narrow further.
- The inflation that re-emerged in 2021 was hardly a big surprise. It was bigger than we'd expected – shortages and disruptions emerged even with plenty of overall capacity – but we always saw elevated inflation risk as a likely post-pandemic hangover.
- Central banks have been even more willing to allow economies to "run hot" than we'd thought. Much of 2021's surge in consumer prices has admittedly been "transitory": as we write, the Baltic Dry shipping index has halved from its October high, and labour supply seems poised to rebound after the autumn's withdrawal of special pandemic measures. But policy settings remain very generous, and more binding labour constraints may not be that far away. Even as headline rates slow, central banks and investors may become more aware of underlying, ongoing inflation risk.
- Geopolitical stresses continue, but their focus has shifted from western populism, and trade tensions, towards more strategic issues in South East Asia, which may be less likely to have an economic impact.
- The key investment question for 2022, then, may be how best to position for ongoing inflation risk and higher interest rates. The latter might arrive sooner than central bankers themselves expect – at least in the developed world: their emerging market peers are already on the case.

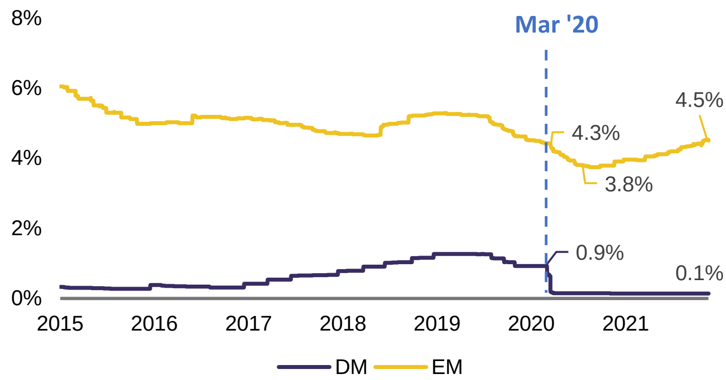
Key cyclical indicators: standard deviations from trend



G7 inflation (YoY %)



Central bank policy rates (%)



Source: Rothschild & Co, DataStream, Bloomberg
Past performance is not indicative of future performance and the value of investments and income from them can fall as well as rise

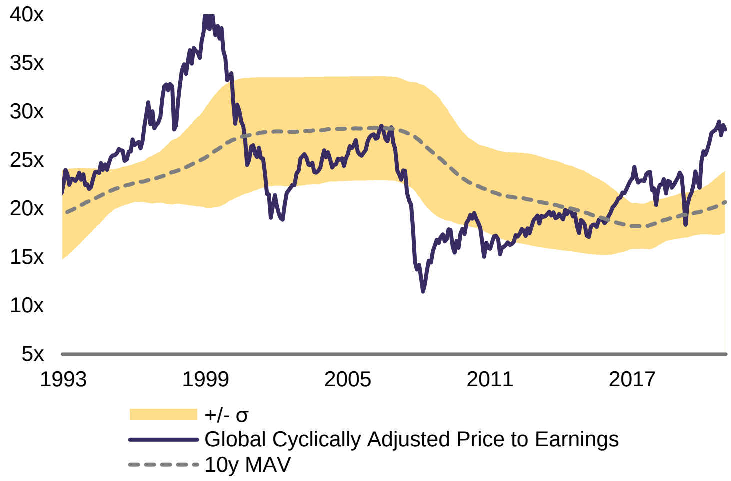
2.2 Stocks still have most headroom

Rising interest rates may hurt most assets, but growth may support stocks

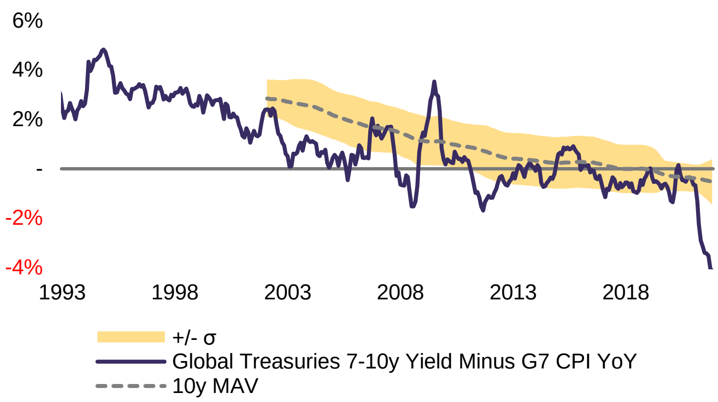
A remarkable rebound in operating profits has been less visible than low interest rates but may have done just as much to boost stock prices. It may help stocks to weather rising rates in 2022.

- Higher inflation expectations have hit conventional bond prices, but the impact has been cushioned by even lower real yields. The resultant valuations make most government bonds unattractive for wealth-preserving portfolios. We think longer-dated bonds are most exposed currently, but as higher policy rates loom closer, real yields may start to rebound across the curve.
- Rising interest rates and bond yields will also hit stocks, by reducing risk appetite and undermining valuations. However, while stocks are expensive, they remain less so than bonds, partly because corporate profitability has been remarkably resilient.
- Operating earnings for S&P 500 companies in 2021 have likely rebounded above the levels that analysts projected before the pandemic. A surge in labour productivity has helped: as we write, US output is above pre-pandemic levels but is produced by 4% fewer workers.
- The picture is clearest in the US, but a similar theme has unfolded across the developed world. Corporate profitability is higher than seemed likely pre-pandemic: return on equity (earnings divided by shareholders' funds) for the developed MSCI index recently hit a 13-year high of 14%.
- Ongoing growth may keep corporate defaults and losses cyclically subdued, and we continue to prefer low-rated investment grade and (in Europe) high yield corporate bonds – and hard currency emerging market bonds – to higher quality bonds. However, spreads have little room to compress much further as government yields rise.
- We think stocks and high yield bonds can still offer inflation-beating long-term returns, but our modelled 10-year returns from a balanced portfolio are the lowest we have calculated to date.

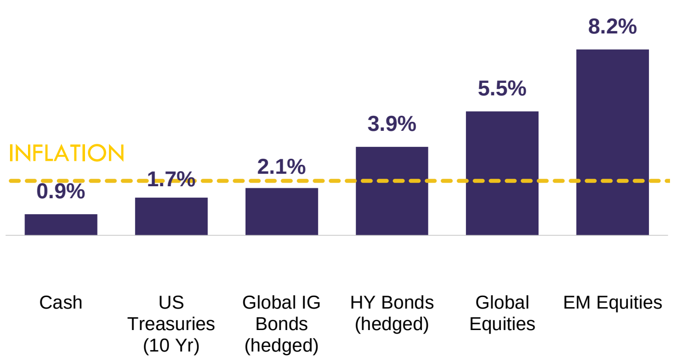
Global stock valuations



Global treasury yields, inflation-adjusted (%)



Forward returns (next 10 years, annualised)



Source: Rothschild & Co, DataStream, Bloomberg
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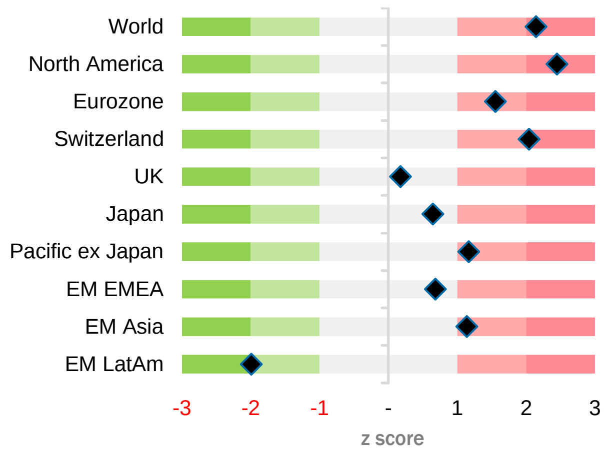
2.3 Equity regions and sectors

We still like the US and EM Asia; and a mix of cyclical and structural growth

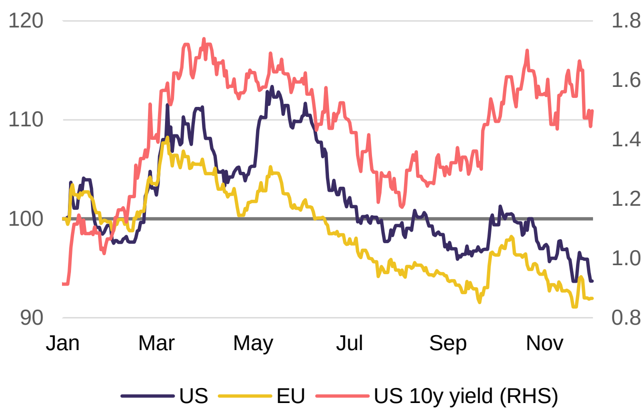
We stay mostly positioned for growth and improved risk appetite, despite renewed outbreaks.

- **US: Overweight.** The US continues to lead the market higher driven by a fast rebound in economic activity and corporate profits. Policy remains supportive for now. The appeal of its outsized technology sector remains undimmed in the post-Covid recovery.
- **Switzerland: Underweight.** Big weightings in healthcare and consumer staples give the Swiss market a defensive and concentrated orientation that we feel is unlikely to appeal in a more recovery-focused climate. We recently moved maximum underweight.
- **Emerging Asia: Overweight.** China's economy is already back to "normal", but property and regulatory-related issues have hit sentiment this year. On a longer-term view, emerging Asia remains by far the most dynamic part of the global economy. Valuations are attractive, and more so given this year's setback.
- **Sector-wise,** during the year we added some cyclical-value exposure, while maintaining some growth sectors and little in the way of defensives. We still favour **consumer discretionary** and **technology**, and **communication services (US),** but now also favour **industrials**, **materials** and **financials (US).** We are least positive on defensive sectors such as **consumer staples**, **utilities** and **real estate**, together with **energy** and **European banks.**

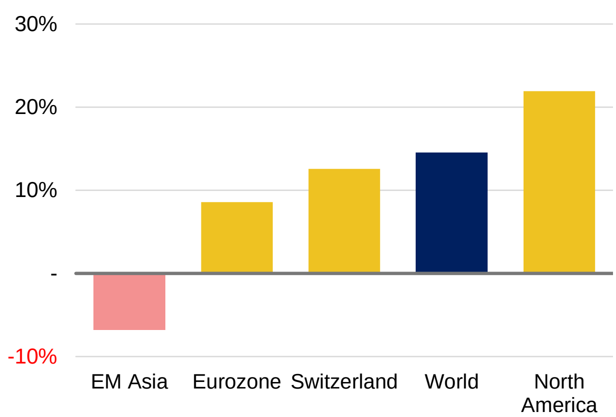
Regional valuation composite (relative to trend)



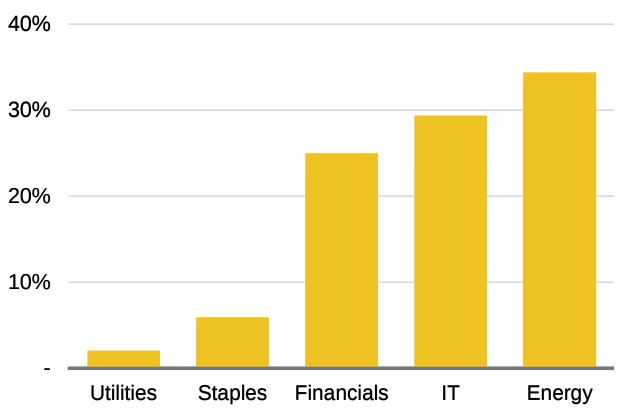
Value vs growth: relative returns (100 = Jan '21)



Selected regional returns (USD, year-to-date)



Selected global sectors returns (USD, year-to-date)



Source: Rothschild & Co, DataStream, Bloomberg

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2.4 Fixed income and currencies

Bonds look very expensive, even after 2021's weakness

Some upturn in longer-term inflation is priced-in, but significantly tighter policy isn't: real yields on many government bonds have fallen to new lows.

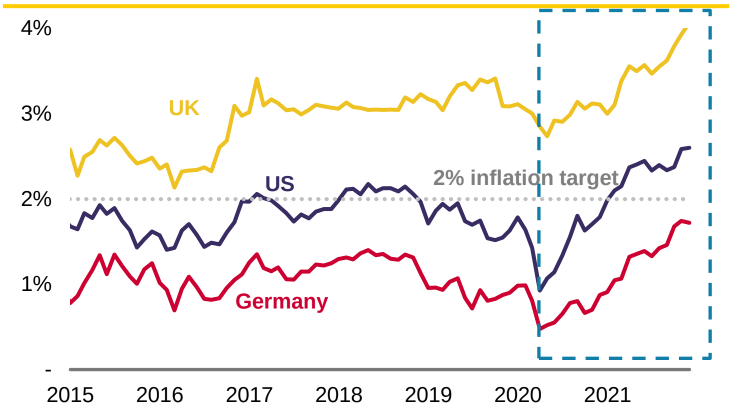
- **Central banks are allowing economies to "run hot"** Monetary policy is deliberately behind the curve. However, as the risk of outright "overheating" rises, yield curves may steepen further until policy rates rise significantly. The Federal Reserve and Bank of England may start raising interest rates soon – many smaller central banks have already begun to do so – with the ECB lagging considerably.

- **Most bond valuations remain prohibitive**, in our view. Breakeven inflation rates have risen, but many real yields have fallen to new lows.

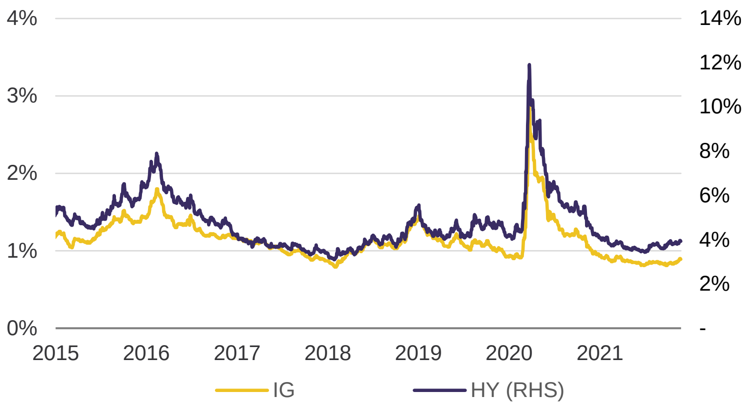
- We expect to favour **short duration** until the monetary normalisation process is firmly underway. Yield curves are not especially steep and have plenty of room to steepen again.

- We **continue to favour lower quality bonds.** The credit cycle remains positive, and their higher yields mean that the chances of inflation-beating returns are greater.

Implied inflation: 10yr breakeven rates (%)



Global credit spreads (OAS, option adjusted spreads)



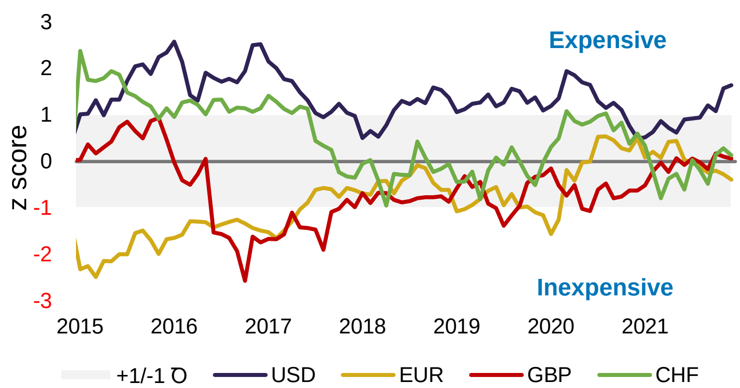
Foreign exchange markets may become noisier in 2022

The major cross rates have been in a remarkably narrow trading range for much of 2021. This could change.

- **FX conviction has been scarce:** Interest rates, inflation rates and valuations had all converged: it was right to be boring on the major currencies in 2021.

- **Some conviction may return:** The policy responses to higher inflation are likely to vary, and carry may return as a market driver. We were not dragged onto the weak dollar bandwagon in early 2021. It feels now as if the euro may become the more vulnerable big currency, as higher inflation puts an inert ECB into focus and (currently) rising contagion poses relatively greater risk, though we do not make that call yet.

Real trade-weighted currency indices (standardised)



- **Emerging markets are most exposed:** Specifically, countries with undiversified economies and idiosyncratic governments are worth mentioning. Some have been attempting to head off any market pressures by raising interest rates before the Fed acts.

Source: Rothschild & Co, DataStream, Bloomberg

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3

Consensus - Equities

3.1 US equities

Sustained demand, high savings levels, and a healthy corporate sector make US equities attractive, despite high valuations, tight labour markets and tightening monetary policy

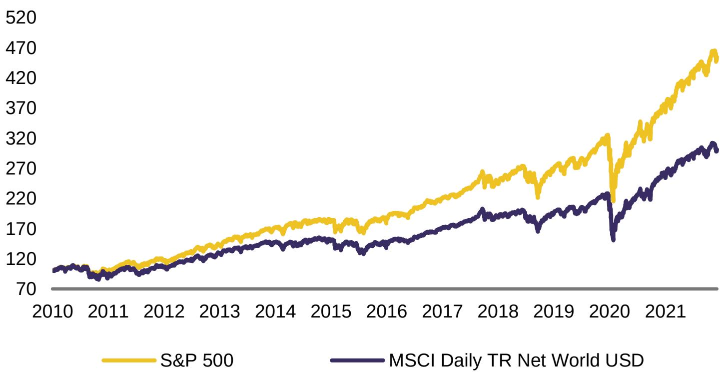
Investment case

- **Relative appeal:** Equities remain attractive versus other asset classes with real rates expected to rise but remain negative. 2021 is on pace to set a new annual record for inflows to US equity mutual funds, and some brokers see this trend continuing.
- **Healthy cash balances**: Elevated household cash balances should further support stock markets. On the corporate side, 2021 buybacks reached a record high (+$1 trillion), as did cash levels on balance sheets. This sets the stage for a large use of cash in 2022 via buybacks and increased dividend yields.
- **Earnings and margins:** Price increases, cost measures and technology helped preserve margins in 2021 despite supply chain issues and rising input costs. Some of these headwinds are expected to ease in 2022, supporting EPS growth. Further, corporate tax reform is expected to be effective only in 2023, not 2022 as previously expected, which should be an additional positive for equities.

Risks

- **Hawkish policy shift:** Monetary policy is expected to be broadly accommodative despite Fed tapering, but a more hawkish turn in Central Bank policy is a risk, especially if dislocations persist (supply chains, labour shortages).
- **Higher inflation, slower growth**: Consumer demand could be impacted by higher-than-expected inflation which could hurt profit margins and in extension might prompt the US Fed to tighten policy more aggressively.
- **Accumulated risks:** Brokers cite sustained margin pressures and cost issues such as higher wages as a risk for equity multiples in 2022, together with slowing demand and reduced appetite from retail investors.

Total return development



Source: Rothschild & Co, Bloomberg

2022 Forecasts

	US Equities	Upside
J.P. Morgan	5,050	+8%
Goldman Sachs	5,100	+9%
Morgan Stanley	4,400	-6%

Forecasts as of November 2021, and refer to S&P500 Index as of close **09.12.2021**
Spot price = **4677**

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3.2 European equities

The signs for Europe are positive amid bottlenecks easing, the inflation surge unwinding, persistent fiscal support, and an ECB expected to keep policy rates unchanged

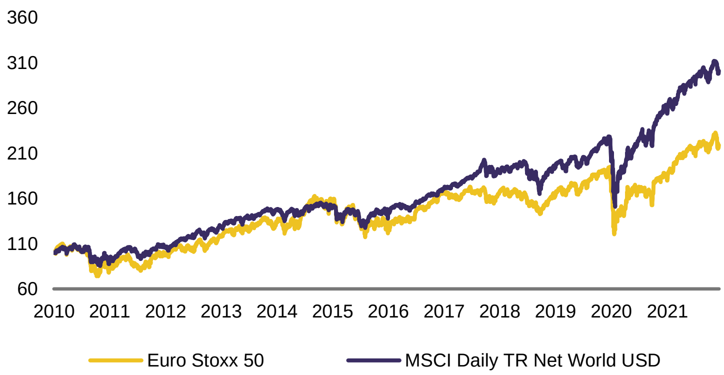
Investment case

- **Ongoing fiscal and ECB measures support European equities:** Consensus expects additional public investment by Germany's new government, an extension of fiscal support in France, and an investment boost for Southern Europe via the Recovery Fund. The ECB is to keep policy rates unchanged and a handover from "PEPP[1]" to an enhanced "APP[1]" in March 2022 will smooth the slowdown in purchases.
- **Inflation and growth moderate, service spending picks up:** The inflation surge will unwind across Europe through 2022 as pandemic one-offs fade – energy, tax cuts and supply bottlenecks. Inflation should move back below target, but with above-trend growth. Despite more moderate growth, brokers highlight significant room for a catch-up in services spending across Europe.
- **Drivers of equity returns still in place:** Low rates, a robust recovery and relatively cheap valuations (compared to US stocks and real Bund yields) should further support equities.

Risks

- **Political headwinds possible:** Italy and France will have elections in 2022, which could reignite political fragmentation. Frictions around Brexit are likely to intensify, although a compromise ultimately looks likely.
- **Southern Europe back in focus:** Disappointing execution of the Recovery Fund or tensions around the reinstatement of EU fiscal rules could heighten Southern European worries, although consensus sees a high bar for debt sustainability concerns in 2022.
- **Potential downside risks:** Brokers cite possible seasonal Covid case pressures, a sharper Chinese slowdown and production disruptions due to energy outages.
- **Green capital expenditure:** The need for more green capex may be under-estimated by companies and investors.

Total return development



Source: Rothschild & Co, Bloomberg

2022 Forecasts

	European Equities	Upside
J.P. Morgan	307	+14%
Goldman Sachs	530	+11%
Morgan Stanley	2,080	+9%

Forecasts as of December 2021, spot prices as of close **09.12.2021**
J.P. Morgan uses MSCI EMU Local Index, spot price = **270**
Goldman Sachs uses STOXX Europe 600 Index. Spot price = **477**
Morgan Stanley uses MSCI Europe Local Index. Spot price = **1906**
[1]**Notes and terminology:** PEPP = Pandemic Emergency Purchase Programme, APP = Asset Purchase Programme.
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3.3 Japanese & Emerging Markets equities

Underperformance of Japanese and EM equities might have come to an end

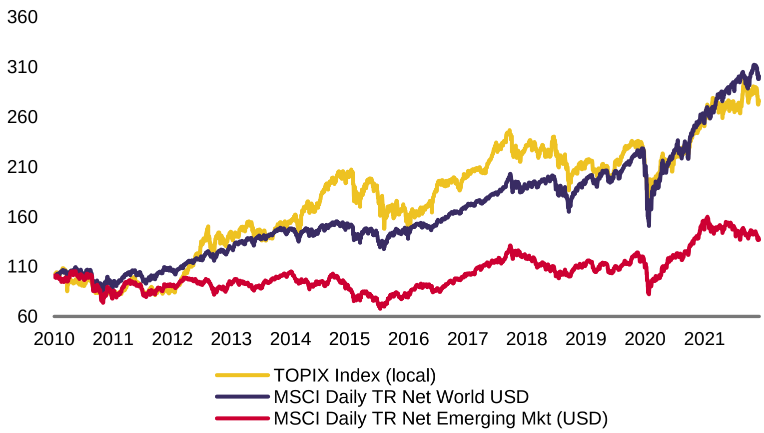
Investment case

- **Japan:** The Japanese economy rebounded strongly in 2021 and is expected to accelerate in 2022, driven mainly by consumption and corporate investments. The new government's positive stance on digitalization and "smart manufacturing" encourages investment to address cyclical and structural labor shortages. Due to high operating leverage, double digit earnings growth is expected. Further, strong earnings growth together with lackluster performance in 2021 has made equities cheaper. Against this backdrop Japanese equities are expected to perform at least as well as EM Equities. Finally, a stronger USD should act as a tailwind for earnings due to a high proportion of exports.
- **Emerging Markets:** After poor performance in 2021, EM equity valuations are cheap in absolute as well as relative terms. Broker outlook for EM is divided: «Bears» highlight slowing economic growth, political uncertainties in many countries, expected tightening of global liquidity and a stronger USD as headwinds. «Bulls» focus on low valuations, a positive effect from supportive Chinese policy and regulatory measures having reached their peak, and money flows returning to EM.

Risks

- **Japan**: Economic recovery could be delayed by supply bottlenecks. As an export-driven economy, positively leveraged to the strong global capex cycle, Japan could suffer should the global economy slow down more than expected.
- **Emerging Markets**: Faster than expected tightening of monetary policy is a major risk. Property sector deleveraging in China, power shortages and tight credit conditions could lead to a stronger than expected growth slowdown. Geopolitical disputes between China and the US, Europe, Taiwan, or Japan could derail markets.

Total return development



Source: Rothschild & Co, Bloomberg

2022 Forecasts

	Japanese Equities	Upside
J.P. Morgan	2,200	+11%
Goldman Sachs	2,250	+13%
Morgan Stanley	2,250	+13%

	EM Equities	Upside
J.P. Morgan	1,500	+21%
Goldman Sachs*	720	+14%
Morgan Stanley	1,315	+6%

Forecasts as of December 2021, spot prices as of close **09.12.2021**:
For Japan index used is Topix, spot price = **1,990**
For EM, index used is MSCI Emerging Markets, **= 1,241,**
*) MSCI Asia-Pacific ex Japan ($), spot price **= 634**

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4

Consensus – Government bonds

4.1 US government bonds

The tide turns for the FED as monetary policy is expected to normalize gradually on the back of strong economic recovery and elevated inflation

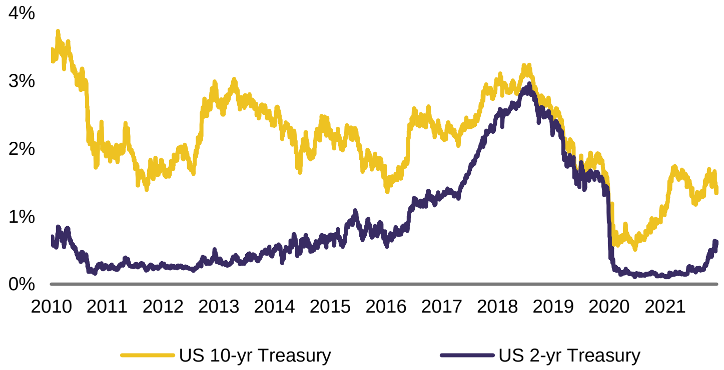
Investment case

- **Tapering is here:** In November 2021, the Fed announced a progressive unwind of its Covid-related asset purchases program that made its balance sheet grow from $4.2 to $8.6trn. The Fed should start hiking interest rates once tapering is completed in June 2022, although brokers differ on dates (from September 2022 to 1Q2023).
- **Macro back to front page:** After two years of Covid interference in monetary policy, vaccinations seem to stabilize the picture and bring macroeconomics back to the front page. The Fed will look at inflation levels, economic recovery and the labour market to decide when to raise rates.
- **Powell reappointment:** Fed Chair Powell was reappointed by Biden for a second 4-year term. That has reassured markets on the fact that monetary policy should move towards normalization, not too fast but not too slow.

Risks

- **Return to pandemic times:** Continued growth is the base case for the expected increase in 10year yields from 1.6% as we write to broker targets seen on the right. Any new variant or major hit in the global economy would make those recede.
- **Even higher inflation:** If bottlenecks do not subside or the US economy enters into a wage inflation spiral, long term yields could be pushed even higher and the Fed might be prompted to act faster, creating turmoil in financial markets.
- **Risks in global politics:** Tension between China and the US and other heightened geopolitical tensions may continue to drive investors towards US government bonds as a safer asset. This would result in higher prices and lower yields.

Price development



Source: Rothschild & Co, Bloomberg

2022 Forecasts

	12m target: 10y US Treasuries
J.P. Morgan	2.25%
Goldman Sachs	2.00%
Morgan Stanley	2.10%

Forecasts as of November 2021, spot price as of **09.12.2021: +1.47%**

4.2 EU government bonds

The ECB diverges from the FED – expect a slower pace of economic stimulus withdrawal in Europe, with interest rate hikes not planned until at least 2023

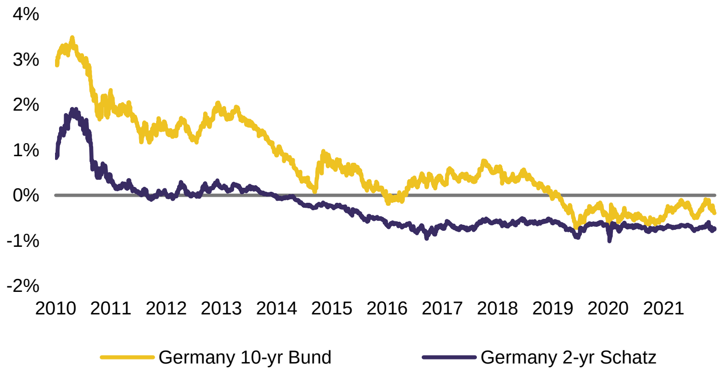
Investment case

- **ECB not in a rush to tighten:** Despite *painful* inflation (sic), Chairman Christine Lagarde confirmed the ECB will not raise rates in 2022. With asset purchases within the EUR 1.85 trillion PEPP[1] expected to finish by March 2022, brokers see a potential extension in order to maintain loose financial conditions.
- **Euro government bond yields to move positive:** Continued improving growth and sustained inflation should drive European yields to positive territory next year. Front-end yields should remain anchored as the market gets comfortable with inflation and the ECB remains supportive. As a result, brokers expect a steepening of the yield curve, where the long end moves faster than the short end.

Risks

- **Political noise to continue:** After a calm 2021 in terms of political events (apart from Germany), Italian and French Presidential elections will be on investors' radars during the first half of 2022. France entails the highest tail risk for markets, with Le Pen or Zemmour as candidates, although Macron continues to lead the polls.
- **Unknowns in the European macro-economic landscape:** Any change of direction in inflation rates, as well as a return of Covid uncertainties could push the ECB to advance or postpone its actions regarding monetary policy.

Price development



Source: Rothschild & Co, Bloomberg

2022 Forecasts

	12m target: 10y Bunds
J.P. Morgan	+0.10%
Goldman Sachs	+0.30%
Morgan Stanley	0.00%

Forecasts as of November 2021, spot price as of **09.12.2021: -0.35%**

[1] PEPP =Pandemic Emergency Purchase Programme

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5

Consensus – Credit

5.1 US credit

Although the credit cycle remains positive, consensus sees limited room for further spread tightening

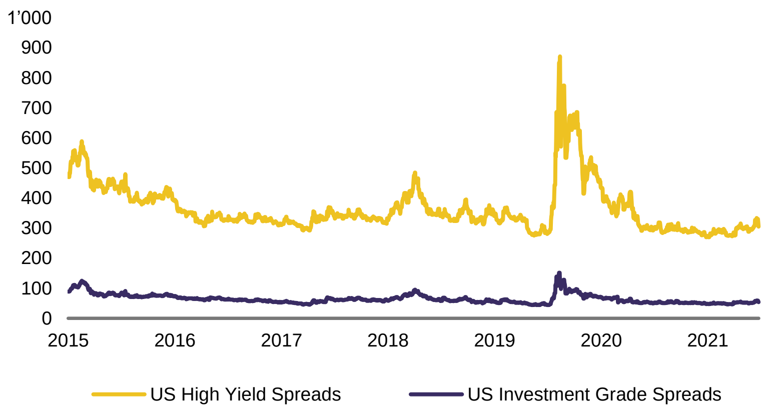
Investment case

- **Above trend economic growth:** GDP growth of +3.9% for next year is expected to be above historical trend (more than 3%) even if below 2021 levels. This should support credit in 2022.
- **Tightening monetary policy:** Consensus expects the Fed to tighten policy by tapering QE purchases to zero and raising rates, starting between Q2 2022 and Q3 2023. A disconnect between the timing and speed of rate rises expected by the market and the actual timing of these rises could cause spreads to widen.
- **Lower inflation benefits credit**: Brokers expect US inflation around 2.4%, which is still higher than in previous years but more moderate than in 2021. Slowing inflation supports bondholders, whilst on the issuer's perspective a healthy inflation level supports credit metrics of levered fixed-rate debt companies, eroding their debt burden.
- **Pricing power helps high quality issuers**: Many companies have been able to pass along rising input costs. The sustainable earnings power of such issuers should reduce the negative impact of inflation.

Risks

- **Expensive valuations:** Credit spread levels are already relatively low after a strong run since the start of the pandemic, especially in Investment Grade. Investors should focus on sector and single name allocation to generate alpha.
- **Rising hedging costs:** With interest rate hikes, hedging costs are likely to move higher. This was the case in 2018 when Fed tightening did not impact the spreads until USDEUR increased hedging costs and foreign demand weakened.
- **Covid variants:** New and more virulent variants could lead to further lockdowns, impacting GDP growth and credit quality.

Price development



Source: Rothschild & Co, Bloomberg

2022 Forecasts (current → target)

	US Investment Grade	US High Yield
J.P. Morgan	117 → 100 [1]	398 → 350 [2]
Goldman Sachs	89 → 103 [3]	285 → 350 [4]
Morgan Stanley	97 → 100 [5]	303 → 330 [6]

[1] JPM US Liquid Index spread, forecast as of 16/11/2021, current level as of **10/12/2021**
[2] JPM US HY index spread Data as of 22/11/2021, current level as of **13/12/2021**
[3,4] iBoxx US Investment Grade and HY index spread, forecasts of 17/11/2021, current level as of **13/12/2021**
[5,6] Bloomberg Barclays US Corporate and HY spread, forecast as of 14/11/2021, current level as of **13/12/2021**

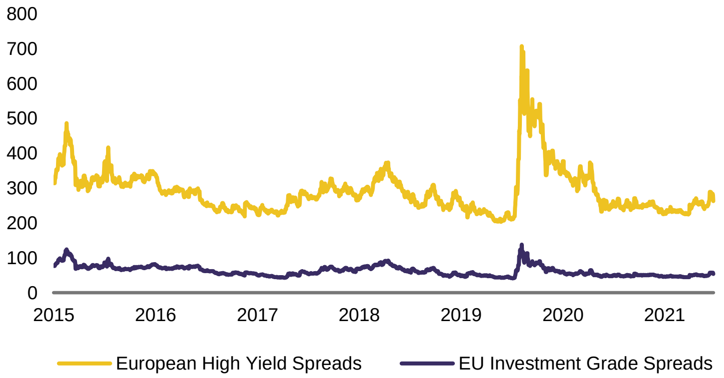
5.2 European credit

Limited room for further tightening, despite a continuing economic recovery and supportive ECB policy

Investment case

- **Accommodative monetary policy continues:** The ECB is likely to maintain its purchase of corporate bonds, albeit at a slower pace. The mid-December 2021 meeting could set the course for policy post PEPP (beyond March 2022).
- **Vaccine deployment and boosters:** Thanks to vaccination campaigns and booster shots, governments rely on less restrictive measures than lockdowns, avoiding further negative economic impacts and supporting credit quality.
- **Lower inflation and accommodative fiscal policy:** Inflationary pressures should moderate in 2022, with core inflation heading towards 1.5%. Upward pressure can persist if supply problems do not ease. Accommodative fiscal policy should continue in 2022, with tightening only expected at a marginal level.

Price development



Source: Rothschild & Co, Bloomberg

Risks

- **Expensive valuations:** Consensus sees limited room for spread tightening (especially in Investment Grade), as the credit spread levels are already low. At current tight spread levels, any negative news flow will likely widen spreads, even if the news is minor.
- **Political elections:** Uncertainty surrounding presidential elections in France and Italy in H1 2022 could result in material spread widening, even though broker base cases point to a second mandate for Macron and to Draghi remaining Prime Minister.
- **Covid variants:** New and more virulent variants could lead to further lockdowns, impacting GDP growth and credit quality.

2022 Forecasts (current → target)

	EU Investment Grade	EU High Yield
J.P. Morgan	114 → 120 [1]	389 → 400 [2]
Goldman Sachs	107 → 112 [3]	329 → 365 [4]
Morgan Stanley	49 → 70 [5]	318 → 375 [6]

[1,2] JPM EU Liquid Index and JPM EU HY Index spread, forecast as of 17/11/2021, current level as of 13/12/2021
[3,4] ICE-BAML IG and HY Index spread, forecasts and current levels of 17/11/2021
[5,6] Bloomberg Barclays US Corporate and HY spread, forecast as of 10/11/2021, current level as of 13/12/2021

6

Consensus – Commodities and Foreign Exchange

6.1 Commodities

Commodities will be driven by cyclical and structural factors, with cyclical macro elements likely to drive oil and more structural issues supporting base metals. The outlook for gold is more muted.

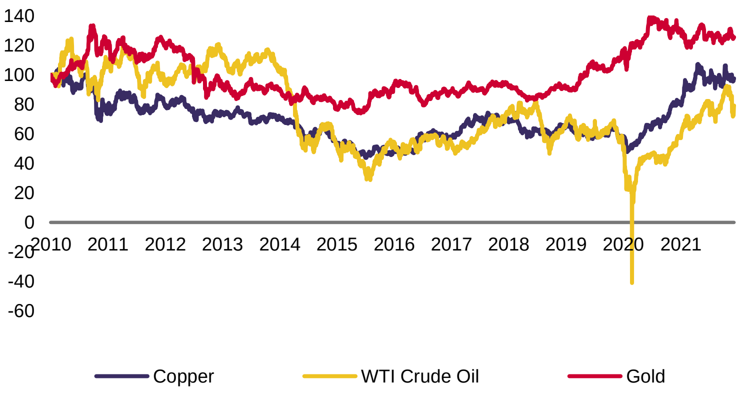
Investment case

- **The return of demand for oil**: Bulls point to accumulated wealth, pent-up demand (especially from lower income households), pro-growth fiscal policy and continued loose monetary policy driving growth in 2022 and supporting oil prices. 2019 oil demand levels will be surpassed by March 2022 with oil supply still weak and inventories low going into the year. Supply is likely to rebound later in the year. Brokers see oil prices rising in H1 as demand exceeds supply, and then falling in H2 as supply catches up.
- **Structural considerations:** Redistribution policies and an ambitious decarbonization agenda centered on green infrastructure in the US, Europe and China support a multi-year demand increase for base metals and energy. Additionally, US-China tensions fueling deglobalization of supply chains in several industries will support commodity prices, especially in the US and Europe where increased input prices are more easily passed on to consumers.
- **Precious metals**: As real yields rise, gold and other precious metals should trend lower, especially if the dollar strengthens and the stagflation narrative subsides.

Risks

- **China:** As the biggest consumer of commodities, China's slowdown, especially in construction, lowers demand for commodities, especially iron ore.
- **Oil supply loosening**: With inventory levels at 5-year lows, oil producers are likely to increase production gradually in 2022, sending oil prices lower in H2.
- **Gold:** One broker expects slowing investment demand but continued high demand from Central Banks and consumers, with strong appetite from Indian and Chinese consumers in particular.

Price development



Source: Rothschild & Co, Bloomberg

2022 Forecasts

	WTI	Upside
J.P. Morgan	$86.00	+20%
Goldman Sachs	$78.25	+9%
Morgan Stanley	-	-
	Brent	**Upside**
J.P. Morgan	$90.00	+20%
Goldman Sachs	$81.25	+8%
Morgan Stanley	$85.00	+13%
	Gold	**Upside**
J.P. Morgan	$1,520	-14%
Goldman Sachs	$2,000	+13%
Morgan Stanley	$1,560	-12%

Forecasts as of December 2021, spot prices as of **9.12.2021: WTI: $71.7 Brent: $75.2 Gold: $1776**
Past performance is not indicative of future performance and the value of investments and income from them can fall as well as rise

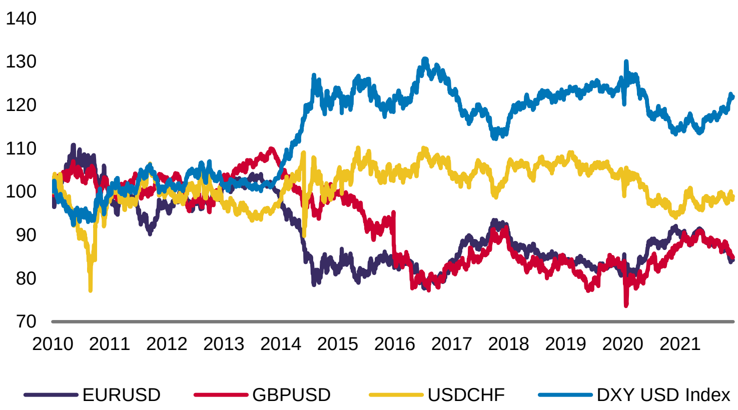
6.2 Foreign exchange

A year of two halves dictated by monetary policy divergence and re-convergence

Investment case

- In currency markets, investors should focus on differentiation based on central bank policy outlook, exposure to commodity prices and tourism, as well as carry. As the year progresses, policy divergence could become policy convergence which would turn USD lower.
- Consensus sees **USD** rangebound for 2022. On the positive side, rising rates should support the USD; on the downside brokers cite a high current valuation (especially versus EM currencies), competitive asset returns elsewhere and the ongoing structural pressure on the role of the dollar in the global economy. The year could play out in two distinct halves: in H1 the USD continues to gently appreciate based on rising interest rate expectations, with a possible pivot lower in H2 as the Fed remains focused on employment rather than inflation and rate hikes are pushed back. Inflation will be the key determinant here and is tricky to predict: if it remains above expectations, rates will rise faster, and the USD will strengthen; if inflation subsides and/or the Fed accepts a US economy running hotter then the USD will weaken on reduced rate hike expectations. If inflation remains as expected, the USD is likely to stay rangebound.
- **EUR, CHF, JPY**: Consensus is muted on low-yielding currencies amongst monetary policy divergence in H1. For H2, the outlook is a bit brighter with EUR, JPY and CHF more sensitive to higher real yields than other G10 currencies. **JPY** is cheap in relative terms but likely to underperform without a clear view on the BoJ's timing to unwind stimulus. **EUR** is expected to grind higher versus **CHF** with rising US and German yields, and in H2 also against the dollar as it weakens.
- **GBP**: A steepening gilt curve provides support for GBP going into 2022, but a tepid growth and data outlook combined with a benign BoE path later in the year are cited as downside risks for H2.

Exchange rate development



Source: Rothschild & Co, Bloomberg

2022 Forecasts

	EUR/USD	GBP/USD	USD/CHF	USD/JPY
J.P. Morgan	1.10	1.32	0.92	116
Goldman Sachs	1.18	1.37	0.92	111
Morgan Stanley	1.18	1.38	0.93	113

Forecasts as of November 2021
Spot prices as of 9.12.2021: EUR/USD 1.13, GBP/USD 1.31, USD/CHF 0.93, USD/JPY 113
Past performance is not indicative of future performance and the value of investments and income from them can fall as well as rise.

Notes and terminology

FED = Federal Reserve
ECB = European Central Bank
OPEC = Organization of the Petroleum Exporting Countries
EM = Emerging Markets
DM = Developed Markets
EPS = Earnings per Share
GFC = Global Financial Crisis
QE = Quantitative Easing
ESG = Environmental, Social and Governance
PEPP = Post Pandemic Purchasing Program
APP = Asset Purchase Programme

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Note: We select, when available, the closest target to the end of 2022, depending on the counterparty (stated as *end of 2022, 4Q2022, 12-month forecast* or, alternatively, *2H2022*). Forecasts might be changed by counterparties depending on market circumstances.