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Degroof Petercam Asset Management SA/NV | rue Guimard 18, 1040 Brussels, Belgium | RPM/RPR Brussels | TVA BE 0886 223 276 |

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OUTLOOK 2023

« *Down the Rabbit Hole* »

28.11.2022



FIXED INCOME OUTLOOK 2023

Sam Vereecke
CIO Fixed Income



- Fixed Income -

SEQUENCE OF MULTIPLE SHOCKS



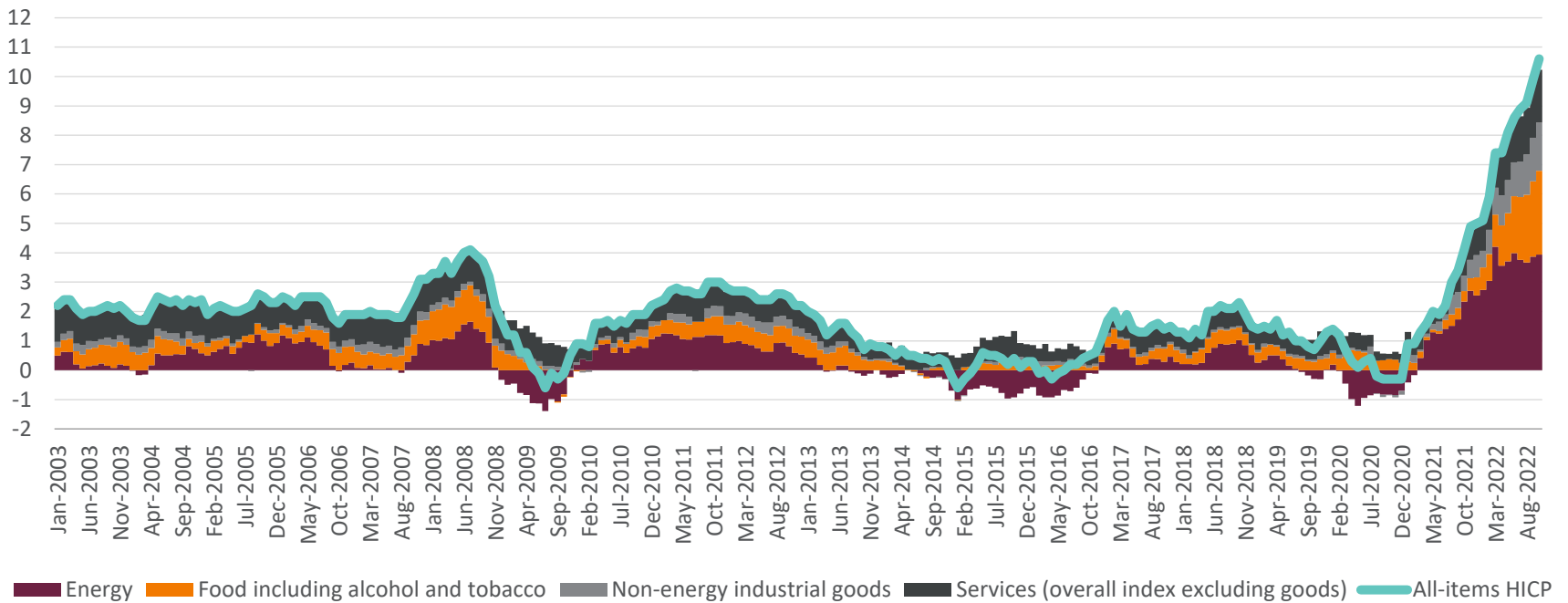
- Covid shock
- Monetary easing shock
- Fiscal easing shock
- Ukraine/energy shock
- Monetary tightening



- Fixed Income -

KEY CONCERN IS UNDERSTANDING INFLATION

Breakdown of European HICP Inflation Contributions



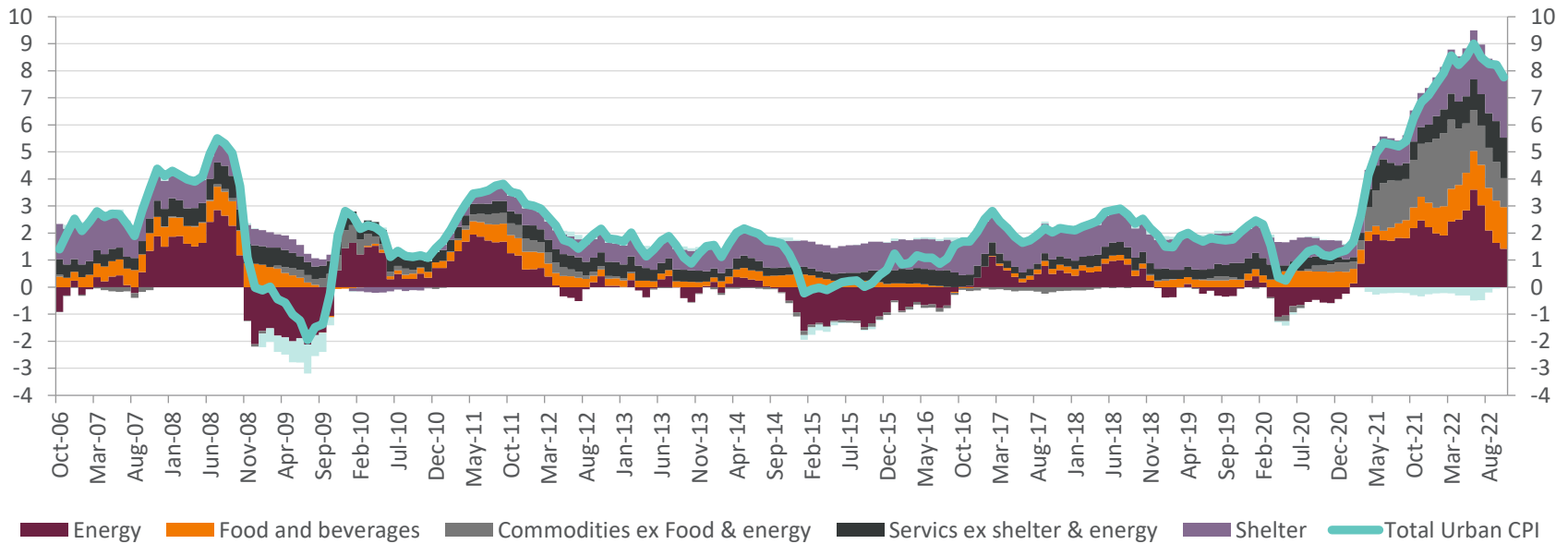
Source: Eurostat, 21 November 2022



KEY CONCERN IS UNDERSTANDING INFLATION

US inflation dynamic is starting to diverge

Breakdown of US Inflation Contributions



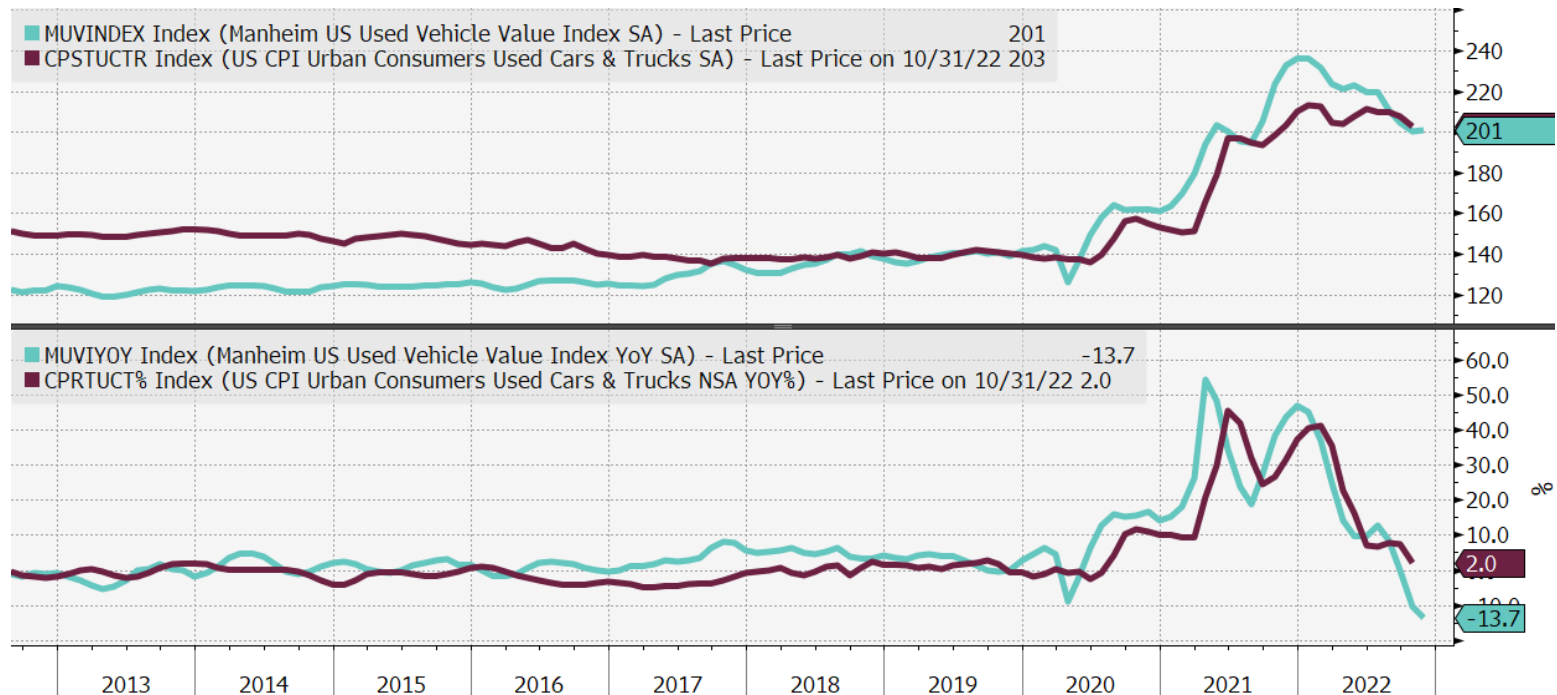
Source: BLS, 21 November 2022



BASIS EFFECTS KICKING IN

Large driver of goods inflation in the US about to turn

US Used Car Prices – Top Graph Index, Bottom YoY



Source: Bloomberg, BLS, Manheim Auctions

MUVINDEX Index (Manheim US Used Vehicle Value Index SA) US CPI Used Cars Manheim Monthly 18AUG2012-20NOV2022

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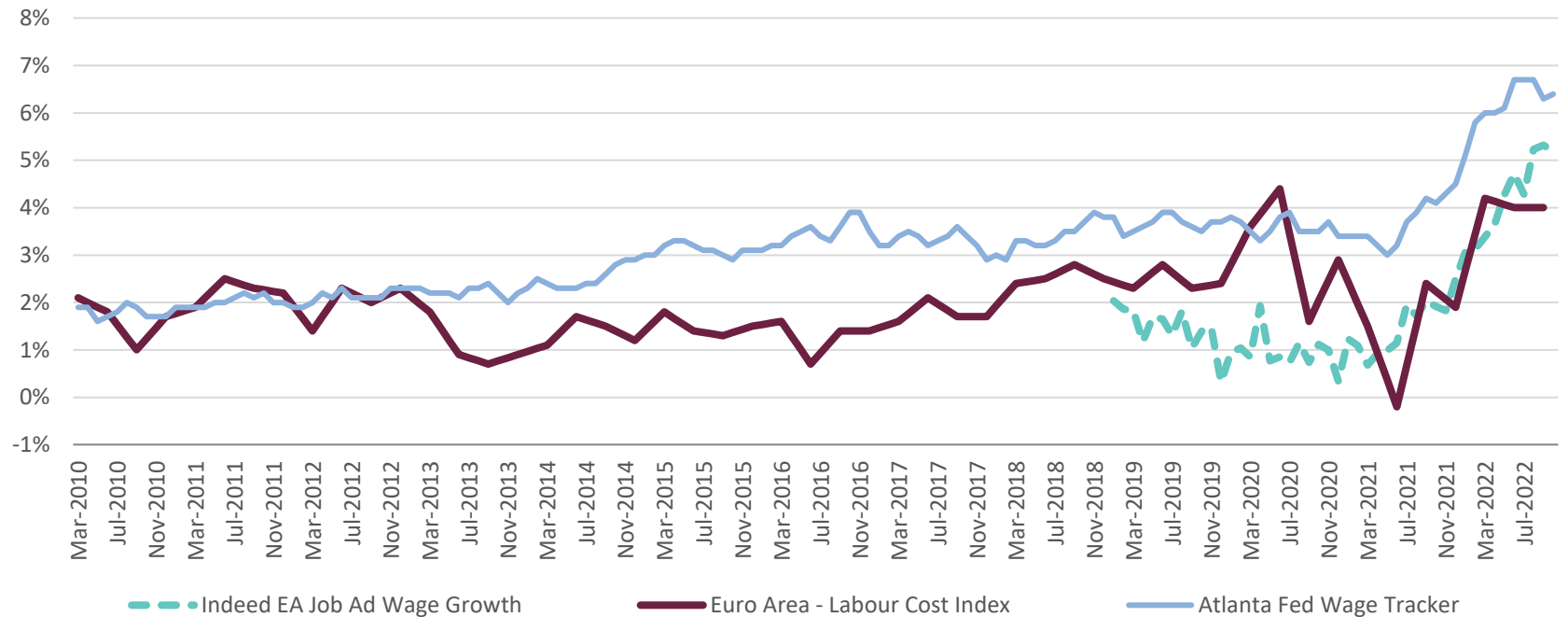
Source: Bloomberg, BLS, Manheim Auctions



SECOND ROUND EFFECTS: **WAGES**

Wages will be an important determinant whether CBs will be successful

Wage Proxies



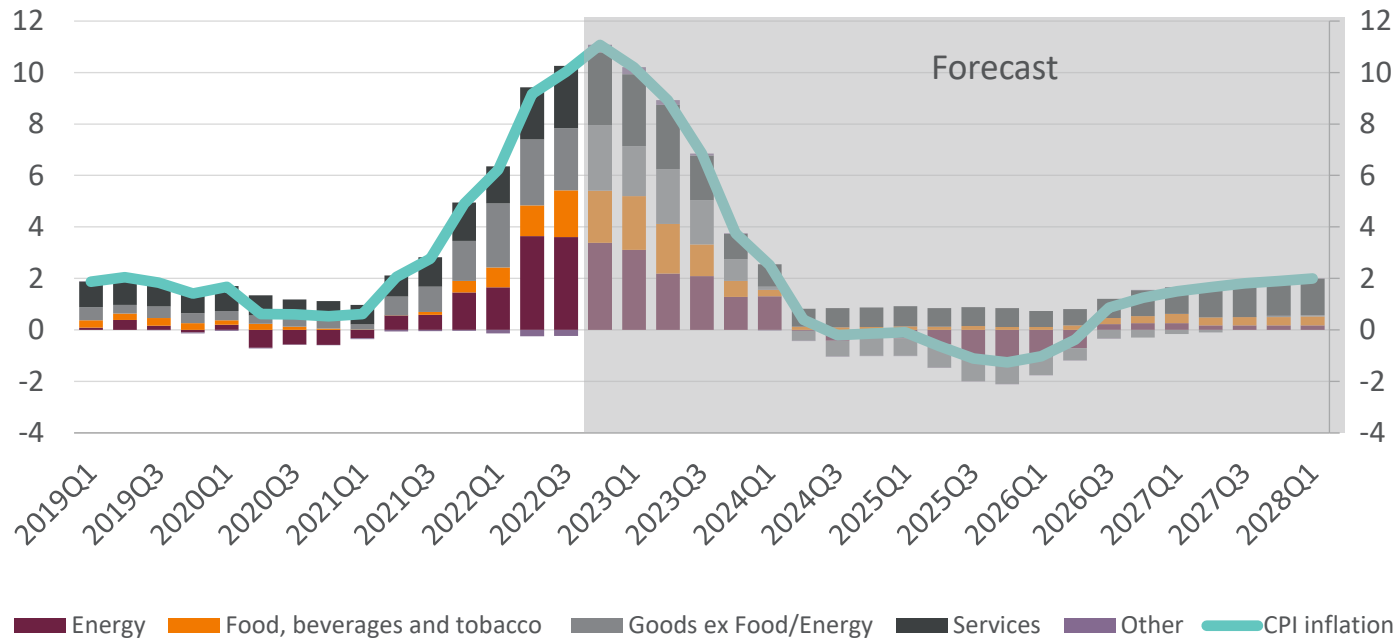
Source: ECB, Eurostat, Atlanta Fed, 21 November 2022



HOW WILL INFLATION **NORMALIZE** POST-BASIS EFFECTS?

Multiple supply-side concerns: reversal of globalization, demographics, climate change and energy transition. These are long term inflation uncertainties.

UK CPI Forecast



Source: OBR, 21 November 2022



NOT ALL **CENTRAL BANK MANDATES** ARE THE SAME

Central banks have different mandates. This will likely lead to different policy reaction curves and monetary policy divergence.



Inflation



Financial Stability



Currency



Unemployment



Growth



Housing Market



REAL YIELDS ARE STARTING TO LOOK ATTRACTIVE

Real Yields – 10-year



Source: Bloomberg

USGGT10Y Index (US Generic Govt TII 10 Yr) US DE JP 10y real yield Weekly 16JUN2009-22NOV2022

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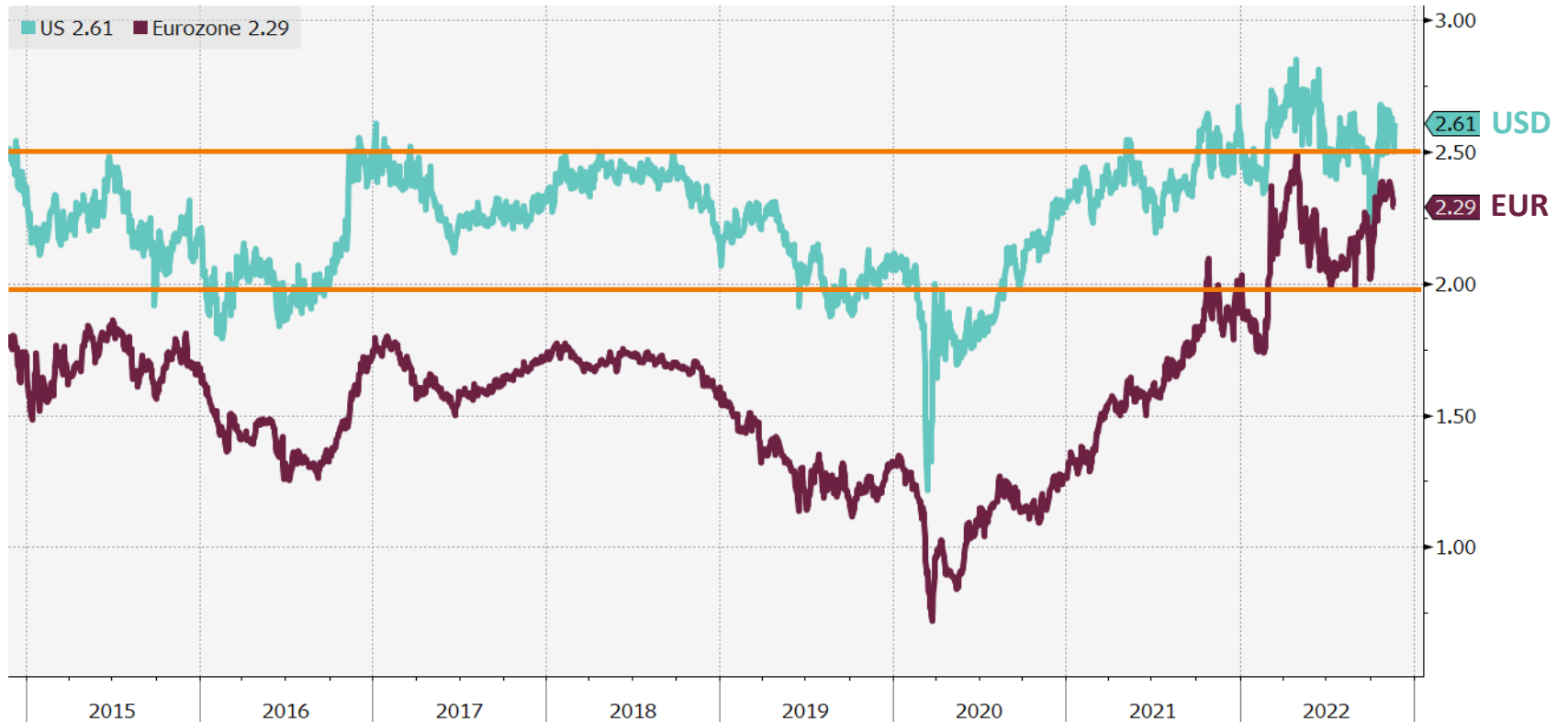
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Source: Bloomberg



INFLATION EXPECTATIONS: NOT THAT HIGH

5Y5Y Forward Inflation Swaps



Source: Bloomberg

FWISUS55 Index (USD Inflation Swap Forward 5Y5Y) 5y5y inflationswap outl Daily 23NOV2014-22NOV2022

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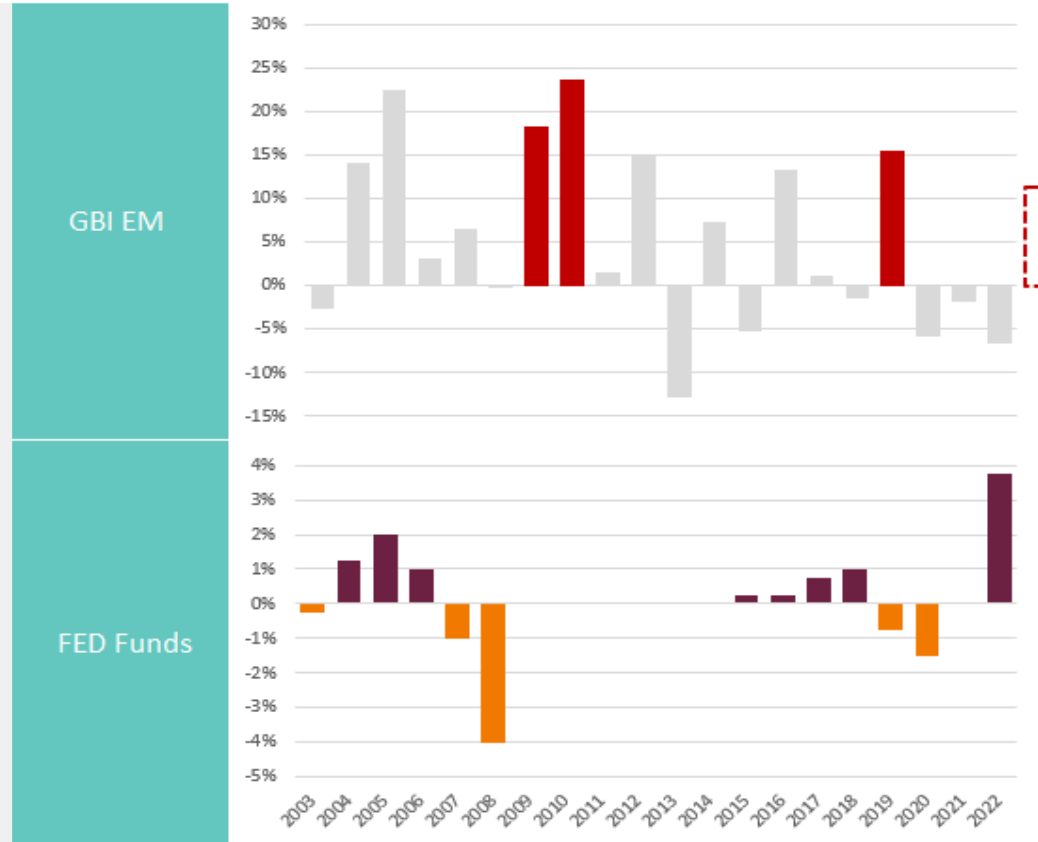
Source: Bloomberg



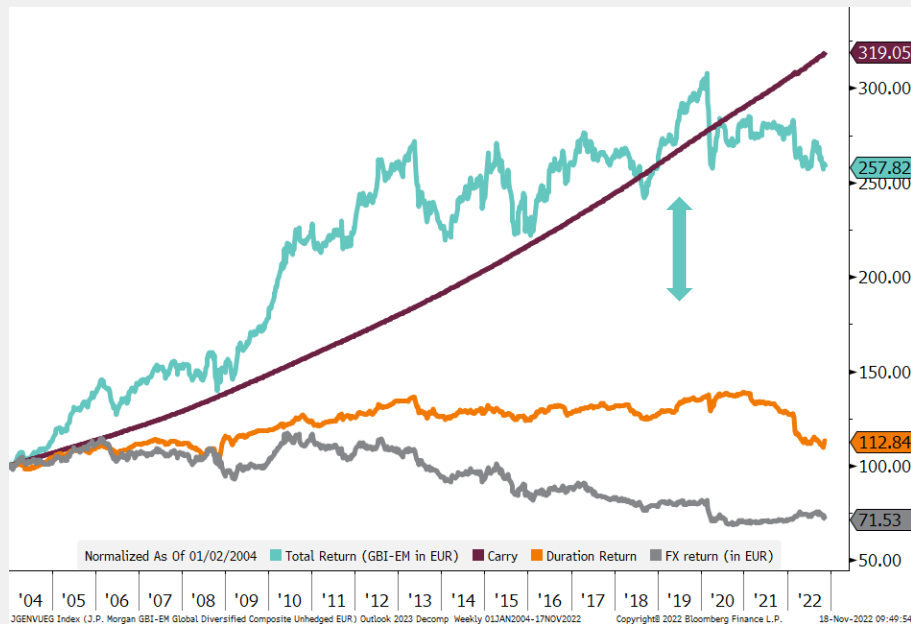
- Fixed Income -

EMERGING MARKETS

Emerging markets realize double digit returns the year(s) following a peak in FED Funds



EMERGING MARKETS: CARRY DOMINANT DRIVER OF RETURN



Source: JGENVUEG Index (J.P. Morgan GBI-EM Global Diversified Unhedged EUR) Outlook 2023

- Emerging markets returns have deviated from long-term path since the 2020 Covid shock
- Expect to close this gap in the next two years
- Emerging markets central banks have been quick in anticipating higher inflation and started hiking well before Developed markets central Banks. This resulted into slowing inflation and slowing growth. Although some might keep rates high for longer (Central Europe), the easing cycle (Latin America) will start in H2 2023. **This is positive for EM local duration.**



KEY MESSAGES

RATES SUMMARY



EURO AND GLOBAL RATES

Closing Underweight



INFLATION LINKED

Overweight(reduced)



EMERGING LOCAL RATES

Overweight

01 Inflation will follow a **difficult and uneasy path to normalisation.**

Wages (second round effects) will create most uncertainty

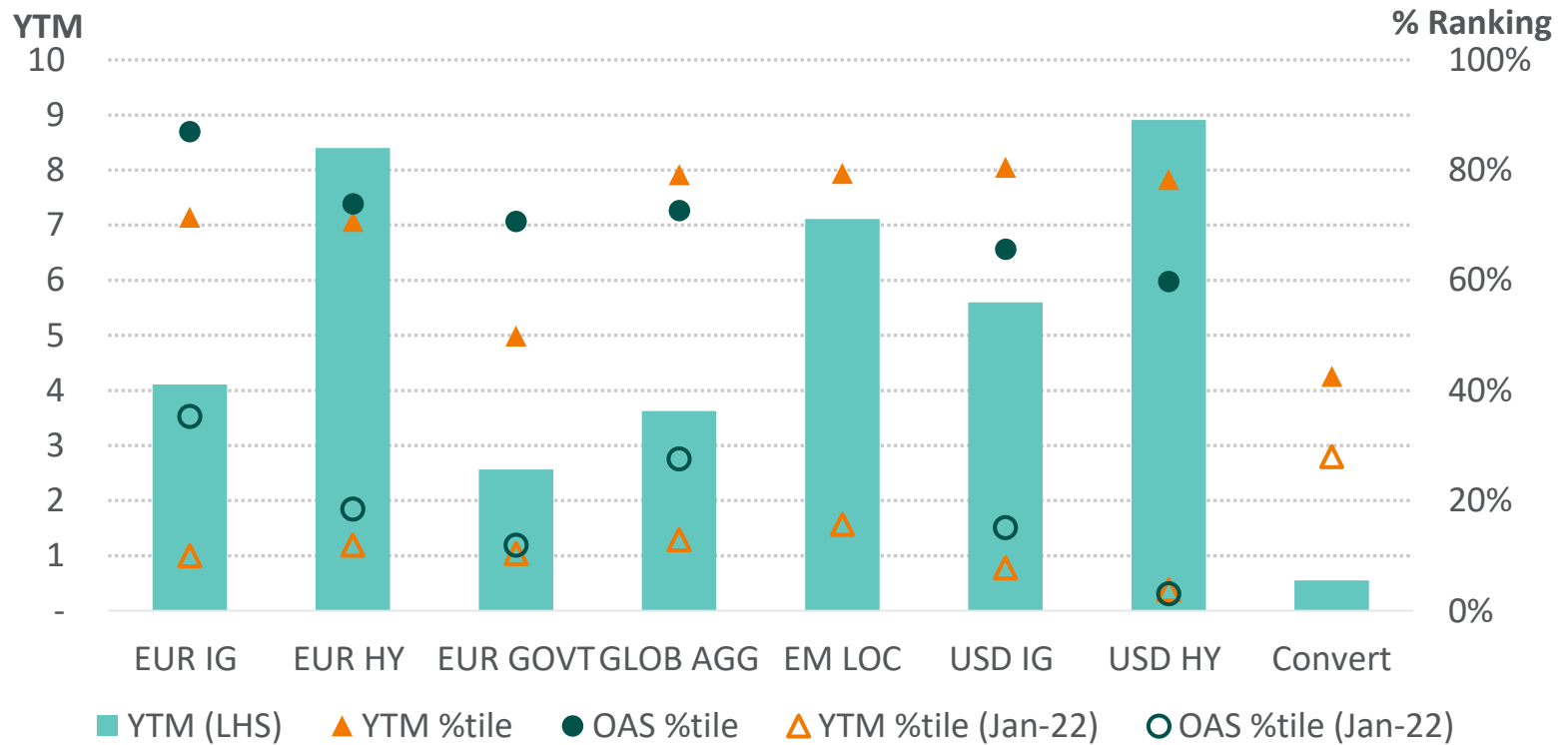
02 We are **closing our underweight duration** by gradually adding duration. In a global context, we will be adding first to the markets with relatively more dovish central banks (e.g. Canada, Australia and New Zealand)

03 **Positive on EM local debt**



2022 VALUATION RESET CREATED ATTRACTIVE YIELDS

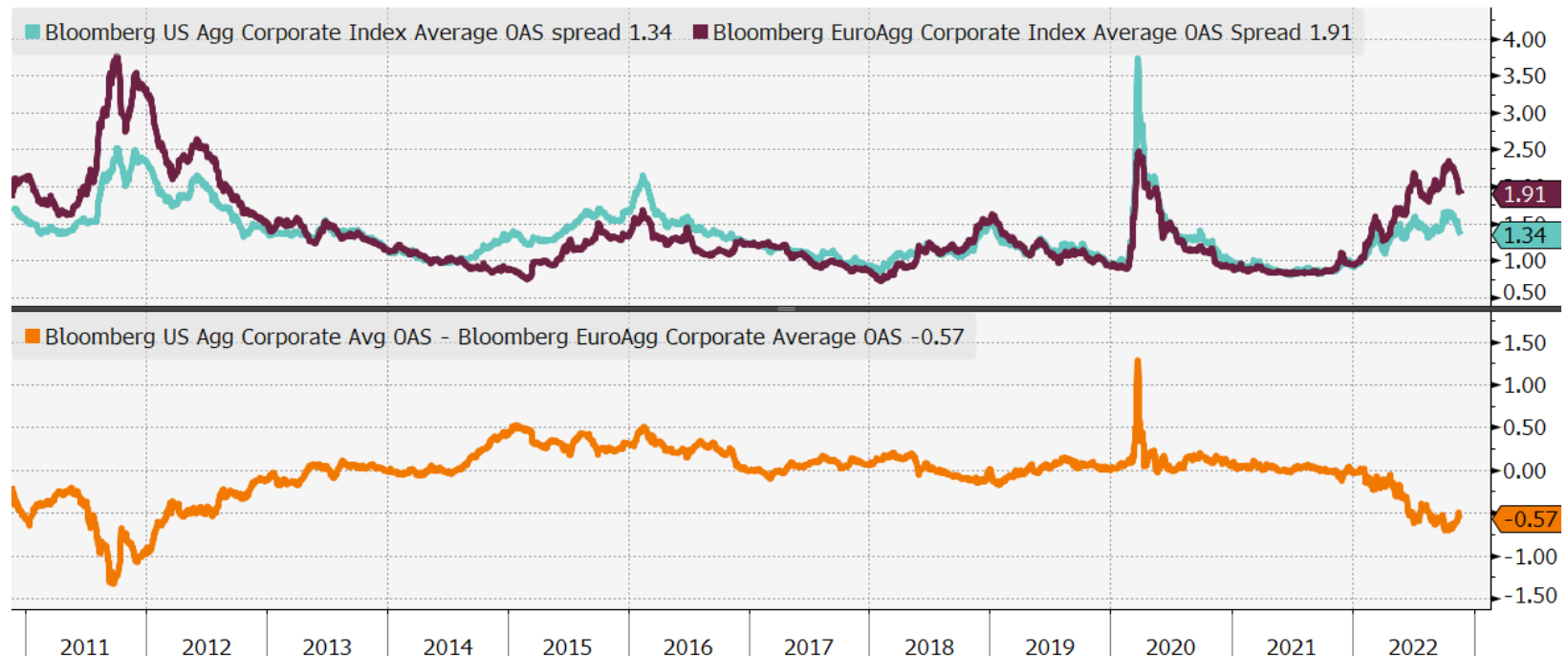
Percentile ranking indicates in a (0-100) format how low (0) or high (100) the current spread/yield is compared to its own history. A 0% indicates an all-time low while a 50% ranking indicates that in the past 20y, the current valuation metric is the 50th percentile when ranked from low to high. All data points are daily



EUR IG CREDIT SPREADS ARE REFLECTING ALREADY A LOT OF NEGATIVE NEWS

IG companies' balance sheets are starting from a better position than during other downturns. If needed, they can use a mix of tools to protect their position: cost reduction, decreasing SBB (share buybacks), asset disposals,

IG Credit Spread: US versus Europe



Source: Bloomberg

LUACOAS Index (Bloomberg US Agg Corporate Avg OAS) US vs EUR credit spread Daily 22NOV2010-22NOV2022

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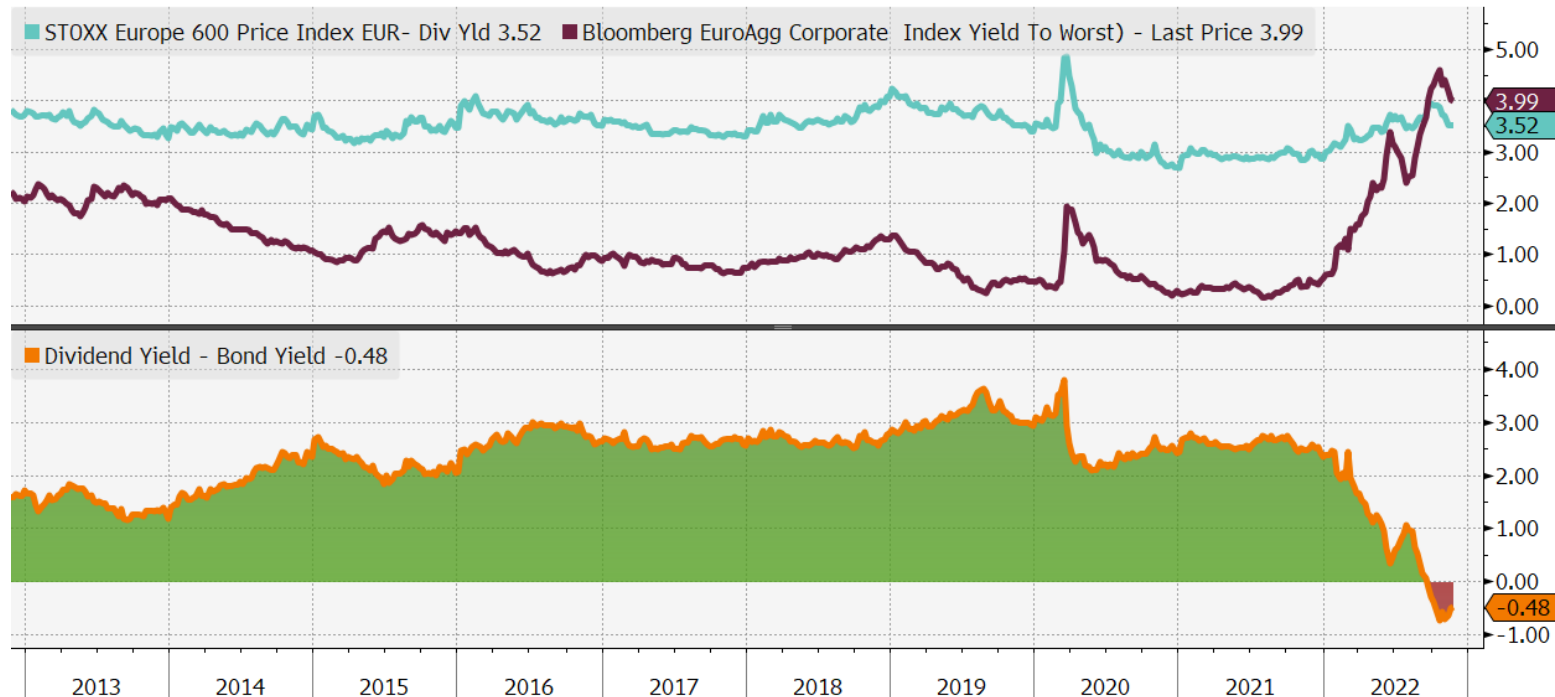
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Source: Bloomberg



EUR IG CREDIT NOT ONLY ATTRACTIVE WITHIN THE FIXED INCOME, BUT ALSO ACROSS OTHER ASSETS CLASSES

Gap between Equity and IG Credit Lowest Since 2010



Source: Bloomberg

SXXP Index (STOX Europe 600 Price Index EUR) Dividend vs Yield Euro Weekly 23NOV2012-21NOV2022

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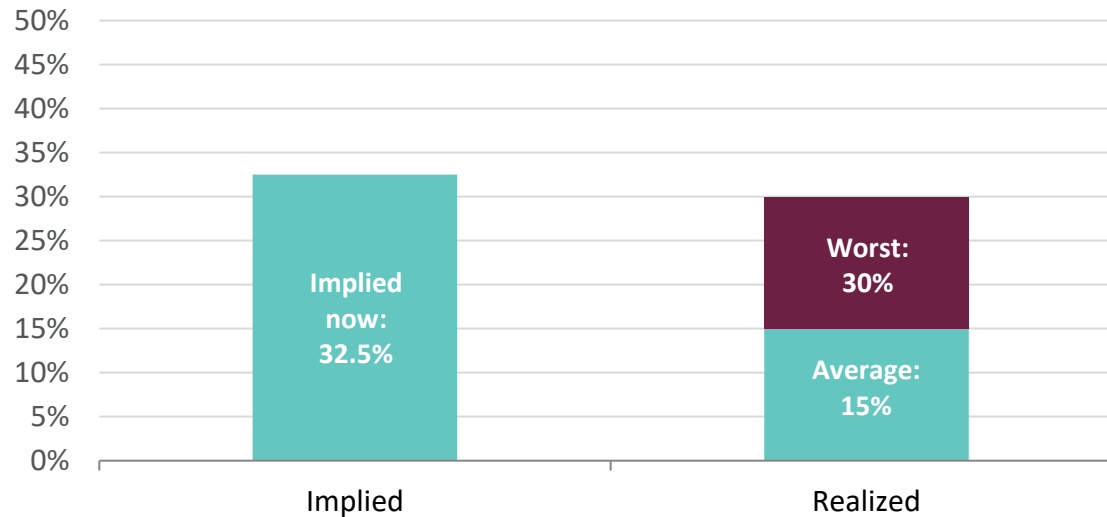
Source: Bloomberg



COVERED FOR A 5-YEAR DEFAULT CYCLE OF 32.5% (VS 15% AVERAGE)

Implied 5 year cumulative default rate at current spread

Spread	0% Recovery	10% Recovery	20% Recovery	30% Recovery	40% Recovery
HY Spread 513	21.6%	23.6%	25.9%	28.9%	32.5%

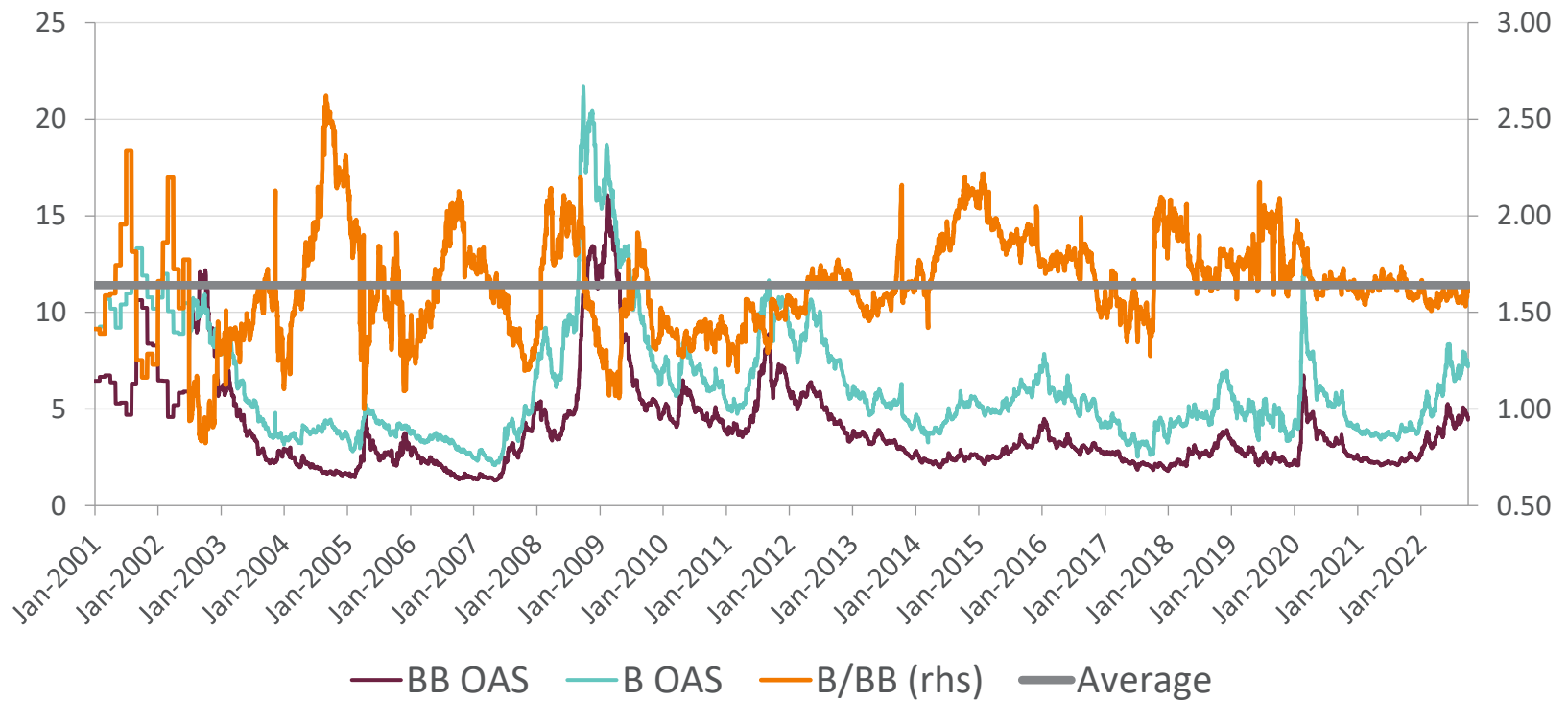


Source: DPAM, 21.11.2022



SINGLE B SCREENS SOMEWHAT EXPENSIVE VS BB

Valuation in line, but risks outsized



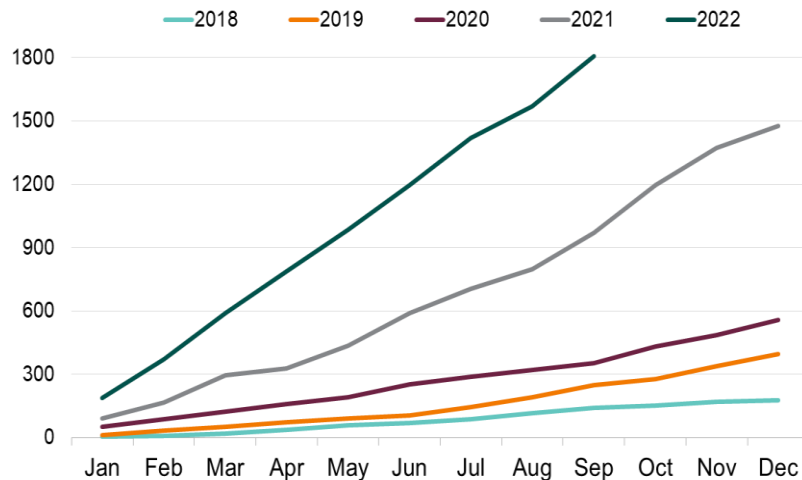
Source: DPAM 6.11.2022



- 2022 was a difficult year but outlook seems bright -

ESG MARKET

- **SBTi commitments have continued to soar.** Which should be fertile ground for issuance over the coming quarters. Markets discriminate well between SLB frameworks.
- Policy makers and **investors embracing the net zero holistic view.** Boon for climate leaders



Source: DPAM, BNEF, SBTi, 30.09.2022

Number of new science-based emission target commitments per calendar year



Source: ECB, NGFS, DPAM, 30.10.2022



KEY MESSAGES

EUROPEAN CREDIT

Credit spreads have become very attractive (overweight)

- Earnings have been coming in better than anticipated and the resilience in the corporate sector combined with the fiscal stimulus should slowly but surely entice investors to reap the decade high valuations in EUR credit markets.

We are more cautious on high yield (neutral)

- Significant spread-value has been created, despite the risk of a recession ahead. We are overweight investment grade credit, and neutral on high yield and convertibles.

GLOBAL CREDIT

European credit spreads are particularly attractive. In the US we prefer pure treasury exposure, given the higher yields and lower spreads



INVESTMENT
GRADE
Overweight



HIGH YIELD &
CONVERTIBLE BONDS
Neutral



THANKS TO YOUR PARTICIPATION TO OUR OUTLOOK 2023,
DPAM WILL DONATE THEIR GOODIE-BUDGET
TO “THE OCEAN CLEANUP”

The Ocean Cleanup, a non-profit organization, is developing advanced technologies to rid the world's oceans of plastic.



CLEAN UP what is already polluting our oceans



INTERCEPT plastic on its way to the ocean via rivers




SCIENTIFIC RESEARCH
to understand the problem and develop cleanup solutions





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HEAD OFFICE BELGIUM


 dpamfunds.com


 +32 2 287 91 11

 dpam@degroofpetercam.com

 /company/dpam

 degroofpetercam.com


 Rue Guimard 18,
1040 Brussels
Belgium

 publications.dpamfunds.com


 /degroofpetercam


LOCAL OFFICES

 Wiesenhüttenplatz 25,
60329 Frankfurt am Main
+49 69 56 60 82 531


 Paseo de la Castellana 141,
Planta 19, 28046 Madrid
+34 91 5720 366

 Rue de Lisbonne 44,
F-75008 Paris
+33 1 73 44 57 60

 **Affiliate** – Bld Georges-Favon 20,
1204 Geneva
+41 22 929 72 23

 **Joint venture** – Syncicap Asset Management*
66/F, The Center, 99 Queen's Road Central, Hong Kong
+852 3842 8200

 Corso Europa 15,
20122 Milano
+39 02 12412 4673

 Rue Eugène Ruppert 14,
L - 2453 Luxembourg
+352 45 18 581

 De Entree 234 unit 5.1,
1101 EE Amsterdam
+31 2 05 73 54 05

