July 2022

Contents

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Market outlook

#1 Market & Macro

Market environment expected to remain extremely difficult


Stefan Kreuzkamp

Caught between high inflation, looming recession and the seemingly endless Russian escalation in Ukraine, stock and fixed income markets have both gone to the dogs in the first half of 2022. “We do not expect a short-term U-turn, as long as it is not clear when the inflation and rate-hiking cycle ends,” Stefan Kreuzkamp, DWS Chief Investment Officer, states. “Growth should remain under pressure. This will have repercussions on the development of corporate profits,” Kreuzkamp warns.” We slightly cut back on our economic growth forecasts for Europe and the United States in 2023 and also revised our price targets for the stock markets downwards by five to ten percent.” Stagnating corporate profits alongside rising yields on bond markets are a difficult environment for stocks. Risks are currently particularly high in Europe – the high reliance on Russian energy is painfully felt here. The valuation discounts of European stocks versus their U.S. counterparts are correspondingly high.

Topics driving capital markets

Economy: economic growth expected to lose further steam

_ European consumers are turning increasingly pessimistic. In June, the consumer confidence index as established by the European Commission fell to its lowest level in decades.
_ We significantly cut back our growth expectations for Germany for 2023 to 2.2% (from 3.2%). For the eurozone we expect a growth rate of 1.8% (after 2.2%), and for the United States of 0.8% (previously 2.2%).

Inflation: price pressure should only recede in 2023

_ Inflation remains the key topic in Europe and the United States alike. We forecast inflation to reach 4.9% in the United States and 8.0% in Europe. Inflation rates expected for Japan and China are substantially lower: 1.9 and 2.3% respectively.
_ In 2023, higher key interest rates and sluggish economic growth should result in markedly lower inflation rates in the United States (3.1%) and in the Eurozone (3.7%).

Interest rate policy: Fed prioritizes the fight against inflation

_ Against the background of run-away inflation, the Federal Reserve has changed its stance. Meanwhile, it is clearly focusing on containing inflation, even at the cost of a recession. U.S. key interest rates are expected to climb to 3.25 to 3.5% by the middle of 2023.
_ The European Central Bank might continue to act in a clearly more cautious way than the Fed. In spite of this, we expect substantially higher key interest rates in the Eurozone – 2.0% by the second quarter of 2023.

Sustainability in focus: carbon emissions – putting our oceans at risk

25 percent*

of carbon emissions produced by mankind are absorbed by the earth’s oceans. Rising carbon emissions threaten the ocean’s capability to absorb carbon dioxide.

30 percent*

– this is the amount by which the acidification of the oceans caused by carbon emissions has increased since the industrial revolution, a major hazard to the earth’s ecological balance.

* Source: oceancampus.eu, Acidification of the oceans, as of: 2021

Forecasts are based on assumptions, estimates, views and hypothetical models or analyses which may prove to be incorrect.
Source: DWS Investment GmbH, as of 08 July 2022

#2 Equities

Low valuations might prove to be deceptive

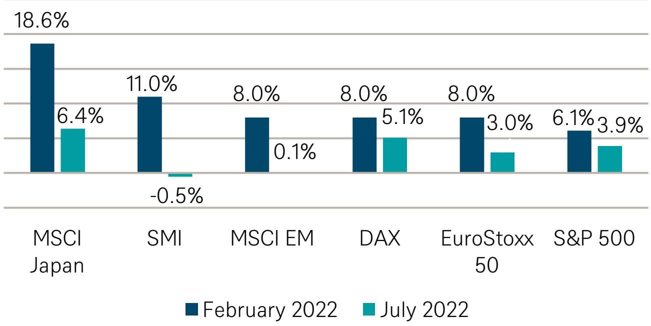
Thomas Schuessler

All in all, the performance of the first six months of the stock year of 2022 is rather disillusioning: figures deep in the red in almost all regions. The top performer is an investment region which most investors deem as rather exotic: the MSCI Latin America recorded only minor losses in the first half of 2022 (-0.3%). Despite massive price losses on most of the other stock markets, it is too early for an all-clear.

"We do not expect a situation on the stock markets as dire as in the 1970s. Price/earnings ratios on the U.S. stock market were one-digit then, interest rates jumped to double figures, thus surmounting inflation rates," Thomas Schuessler, Global Co-Head for equities, remarks. But an equity losing 70% of its value is not automatically cheap. In this difficult environment, high-dividend stocks with sound fundamentals remain the most promising in Schuessler's view. The key question against the background of already sharply reduced prices is how corporate earnings are going to develop. The current forecasts of many equity analysts might turn out to be over-optimistic, and the currently low price/earnings ratios might not correspond with future reality. One example is the expected performance of the MSCI World (AC), which is still based an the profit assessments made at the beginning of 2022, i.e. before the Ukrainian crisis. If expected earnings growth rates were revised sharply downwards, lower valuations would all be gone in one swoop.

Substantial cuts with a view to earnings growth

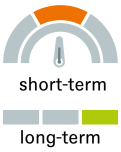
Expected growth of corporate earnings per share on a 12-month horizon



Source: DWS Investment GmbH, as of July 2022

U.S. equities

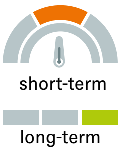
Economic slowdown and lower price target for the S&P 500



- The presumably aggressive rate hiking policy of the Federal Reserve should result in a faltering U.S. economy in the fourth quarter, sliding into a mild recession in the first quarter of 2023.
- Uncertainties around the further path of nominal interest rates and inflation and thus of real rates should exert further pressure on U.S. equities and dampen price potential. The new price target for the S&P 500 by June 2023: 4.200 points (previously 4.400 points).

German Equities

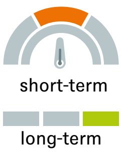
German economy particularly vulnerable to high energy prices



- Germany is hit particularly hard by rapidly rising gas prices. Hardly any other country is similarly dependent on gas imports from Russia.
- The high risk for industry and consumers alike with a view to the supply of energy is also mirrored in the performance of the German stock market index Dax, which has accumulated losses of approximately 20% since the start of this year.
- New target for the Dax by June 2023: 13,900 points (previously: 14,600 points)

Equities Eurozone

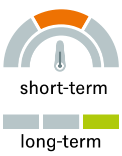
High uncertainty – high-dividend and commodity stocks most promising



- High energy prices and the uncertainty as to whether Russia will completely turn off its gas supplies are an enormous challenge for the European economy.
- Volatility should remain high. High-dividend and commodity stocks are currently most promising.
- The new price target for the Eurostoxx 50 by June 2023: 3.650 points (previously 3.900 points).

Equities Emerging Markets

Development in China an important factor



- Most of the Emerging Markets could not escape the downward slide of the markets, except for Latin America.
- The current price levels seem to discount most of the uncertainties.
- An end to China's zero-COVID policy and new state fiscal measures could set off a recovery.
- The new price target for the MSCI Emerging Markets by June 2023: 1,060 points (previously 1,110 points).

Forecasts are based on assumptions, estimates, views and hypothetical models or analyses which may prove to be incorrect. Past performance is not indicative of future results. Source: DWS Investment GmbH, as of 08 July 2022

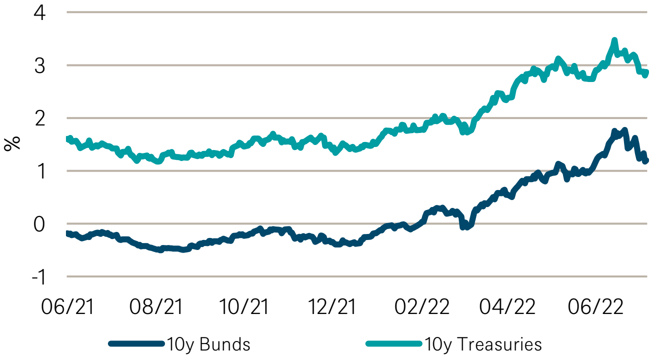
#3 Fixed Income

Opportunities offered by selected corporate bonds

All in all, bonds are deep in the red this year to-date. Irrespective of whether government or corporate bonds, irrespective of whether Europe, Asia or the United States. Is there any hope of improvement? Specific segments could surely offer opportunities.
Due to poorer economic prospects resulting in higher probabilities of default and lower liquidity, yield premiums of corporate over government bonds have massively increased, which in its turn leads to substantial price losses. Even if yield premiums widened even further in the short term – over a twelve-month horizon they are expected to dwindle so that prices will set out on an upward trend. This is particularly true for high-yield bonds from Europe and the United States. Sovereign bonds appear to be less promising.
There are two exceptions here: 2-year U.S. bonds and emerging market bonds. Since Russia's invasion of Ukraine, yields of short-term U.S. bonds have roughly doubled. Yields of 3% are certainly not unattractive. Over a 12-month horizon, we do not expect any substantial further yield rises.

Massively rising yields since Ukraine crisis

Yield development of 10-year Treasuries and Bunds



Source: DWS Investment GmbH, as of July 2022

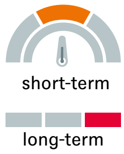
U.S. government bonds (10 years)

Only moderately higher yields expected

_ The rapid yield rise of 10-year treasuries is not expected to continue this way.
_ Long-dated U.S. bonds are expected to yield 3.25% by the end of June 2023.

German government bonds (10 years)

Markedly higher yields expected medium-term



_ Bund yields have substantially recovered against the background of increasing recession fears.
_ By June 2023, we forecast markedly higher yields of 2.25%.

Emerging market sovereign bonds

Definitely interesting long-term

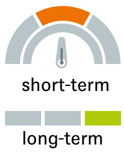
_ Emerging market sovereign bonds have been heavily afflicted by economic uncertainties and higher U.S. rates.
_ Over a longer horizon, the risk/return profile seems to be promising.

Credit

Investment Grade

USA

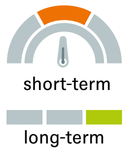
Eurozone



High Yield

USA

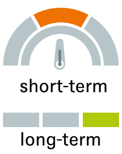
Eurozone



#4 Currencies

Euro/Dollar

Euro under pressure – yield spreads as a drag

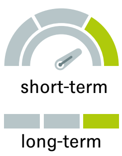


_ The weakness of the euro versus the dollar has continued. An essential reason for this might be the further widening of yield spreads between U.S. and European bonds.
_ Medium-term, yields in the Eurozone are expected to increase and the yield spread to U.S. bonds to diminish slightly. As a result, the euro should rebound against the dollar. We continue to expect a euro/dollar exchange rate of 1.10.

#5 Alternative assets

Gold

Making sense as portfolio diversification



_ Our fundamentally positive assessment of gold remains unchanged. In times of crises, as we are currently experiencing, it is a good option for portfolio diversification. Geopolitical risks, high inflation and low real yields still argue in favour of this precious metal.
_ Of late, the strong dollar has exerted some pressure on gold prices. As soon as the strength of the dollar abates, demand of gold – which is traded in dollars – should be boosted.

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Glossary

Central Bank
A central bank manages a state's currency, money supply and interest rates.

Duration
Measure of the sensitivity of the price of a bond to a change in interest rates

High Yield (HY)
Corporate bonds from issuers with a poor credit rating – these papers generally offer comparatively high interest rates.

Investment Grade (IG)
Corporate bonds that are deemed by rating agencies to have a low risk of default (at least medium credit rating).

Monetary Policy
Economic policy measures that a central bank takes to achieve its goals.

Price-to-earnings (P/E) ratio
The price-to-earnings (P/E) ratio compares a company's current share price to its earnings per share.

Real interest rate
The nominal interest rate adjusted for inflation as measured by the GDP deflator.

Return
Ratio of outgoing payments to incoming payments of an investment.

S&P 500
Index weighted by market capitalisation that represents the 500 leading listed companies in the U.S.

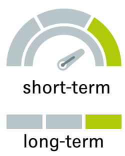
US Federal Reserve (Fed)
The U.S. Federal Reserve, often referred to as "the Fed", is the central bank of the United States.

Legend

The strategic view by June 2023

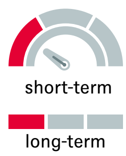
The indicators signal whether DWS expects the asset class in question to develop upwards, sideways or downwards. They indicate both the short-term and the long-term expected earnings potential for investors.

Source: DWS Investment GmbH; CIO Office, as of 08 July 2022



Positive return potential

Potential profits but also risk of loss rather limited



Negative return potential

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