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Capital Market Outlook 2023: Upward potential for funds after market corrections

Erste AM Communications

- **Global economy could skirt the recession expected for 2023**
- **Inflation reaches turning point**
- **Bond yields have not been as attractive as now for a long time**
- **Erste AM CEO Bednar: ongoing asset inflows despite challenging market conditions**

After months of market turmoil, the experts of Erste Asset Management (Erste AM) can see light at the end of the tunnel despite the global economic challenges. Erste AM Chief Investment Officer Gerold Permoser explained at the press conference on the Capital Market Outlook 2023 that there was a chance that the predicted recession in 2023 would not hit, or if it did, it would do so only mildly, even though history and theory argued against it. Now is the time to seize the opportunity and take advantage of the new opportunities on the equity and bond markets.

Difficult year on the capital markets

As Permoser explains, economic and geopolitical uncertainties around the world, high inflation, rising yields, and economic fears have brought the markets to their knees. He speaks of a difficult year that left few alternatives for fund investors. *"The only asset class that performed well in 2022 were commodities, a fact from which Erste AM's commodity equity fund (i.e. ERSTE STOCK COMMODITIES) benefited."* The focus of central banks is on the fight against high inflation, which has hit Europe and the US in particular, but China less so.

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There are now first signs that we have seen peak inflation and that the rate will ease significantly in 2023. A small increase in unemployment is necessary for this to happen. Permoser does not see any clear signs of a wage-price spiral. Inflation in Europe is mainly the results of high energy prices and the Ukraine war. Erste AM regards the inflation and recession risk in Europe as higher than in the USA on account of the high energy costs and cost of living. *"If we see an easing in energy costs, inflation will slow down but remain above the central bank target for the time being,"* Permoser said.

Interest rate hikes to last until mid-2023

The high inflation has led to a regime change in central bank policy: the central banks have come under pressure to tighten monetary policy faster than expected. The extremely supportive monetary policy pursued in the wake of the Corona pandemic is now being scaled back step by step. Interest rate increases will probably continue into 2023. Permoser expects Fed fund rates of 5% in the USA and key-lending rates of 3% in Europe by mid-2023. According to academic studies, the economic dampening effects of interest rate hikes would become noticeable with a time lag of about 18 months. Permoser therefore expects dampening effects on growth from the middle of next year, peaking at the turn of 2023/2024.

The comeback of bond yields

As bond yields have already anticipated this development, Erste AM believes that yields are at an attractive level to compensate investors for global risks. The markets for fixed-income investments have more upside potential than they have had for a long time. This is especially true for corporate bonds: in the investment-grade segment, the yield is currently around 4% in the investment grade segment and around 7% for high-yield corporate bonds. As Permoser points out, *"These are attractive spreads, assuming that default rates do not increase significantly."*

"***If we see an easing in energy costs, inflation will slow down but remain above the central bank target for the time being**."*

Gerold Permoser, CIO

The exaggeration on the equity markets after the Corona Crash has come to an end. Due to the strong corrections, valuations are significantly cheaper than at the beginning of the year. *"Equities are not expensive, but they are not cheap either,"* says Permoser and points out that in phases like the current one and given the risks of setbacks in a recession, investments via fund savings plans are a good option, as they allow for a smoother entry price for the investor. An investment in mixed funds, which offer the advantages of shares and bonds as well as a risk buffer, could also pay off.

Bednar: pleased with asset inflows from fund savings plans

The excellent volume increase that Erste Asset Management experienced last year was slowed down by the consequences of the Ukraine war, inflation, and the interest rate reversal. Assets under management (in investment fund and asset management) amounted to EUR 68.4bn as of 31 October 2022 after EUR 76.8bn at the end of 2021).

Erste Am CEO Heinz Bednar is still satisfied with the situation: *"Fund sales in the first ten months were above expectations. After a decade of almost continuous asset growth, we are facing an extremely difficult market situation this year, from which the performance of most fund classes has suffered."*

The inflow of funds from retail clients suggests that investors are not concerned and are keeping an eye on long-term earnings opportunities, says Bednar. *"Fortunately, our clients have remained loyal to the funds in spite of the market adversities and have taken advantage of the lower prices for additional purchases, especially in the case of sustainable funds and, above all, mixed funds"*. This is happening more and more often through regular fund savings plans, which ensure continuous inflows into our funds. Erste AM already has over one million fund savings plans on its books.

"Fortunately, our clients have remained loyal to the funds in spite of the market adversities."

Heinz Bednar, CEO

The assets held by Erste AM are allocated across its various investment categories. Mixed funds account for the largest share at EUR 29.9bn (43%), followed by fixed income funds at EUR 18.1bn (27%), equity funds at EUR 14.7bn (22%), and real estate funds at EUR 5.4bn (8%). The importance of sustainable funds has been growing across all asset classes. Sustainable funds total a volume of EUR 15.4bn at Erste AM. Bednar: *"The trend towards sustainable investment funds is unbroken, although they, too, have incurred losses in the current environment after the strong performance of the last years. This makes us optimistic that the gains will be much higher when markets are well-disposed".*

Bednar therefore continues to consider sustainable funds such as the global equity fund ERSTE RESPONSIBLE STOCK DIVIDEND, the green thematic equity fund ERSTE GREEN INVEST, mixed funds such as YOU INVEST GREEN advanced and, on the fixed-income side, the corporate bond funds ERSTE RESPONSIBLE BOND EURO CORPORATE (investment grade) and ERSTE RESPONSIBLE BOND GLOBAL HIGH YIELD (high-yield segment) as promising funds for 2023.

You can view the entire press conference on the Capital Market Outlook 2023 at this link.

⚠ Risk notes according to 2011 Austrian Investment Fund Act

ERSTE STOCK COMMODITIES may exhibit increased volatility due to the composition of its portfolio: i.e. the unit value can be subject to significant fluctuations both upwards and downwards within short periods of time.

For further information on the sustainable focus of ERSTE GREEN INVEST as well as on the disclosures in accordance with the Disclosure Regulation (Regulation (EU) 2019/2088) and the Taxonomy Regulation (Regulation (EU) 2020/852), please refer to the current Prospectus, section 12 and the Annex "Sustainability Principles". In deciding to invest in ERSTE GREEN INVEST, consideration should be given to any characteristics or objectives of the ERSTE GREEN INVEST as described in the Fund Documents.

⚠ Risk notes according to 2011 Austrian Investment Fund Act

YOU INVEST GREEN advanced may make significant investments in demand deposits or time deposits

with a maximum maturity of 12 months pursuant to section 72 of the

2011 Austrian Investment Fund Act.

YOU INVEST GREEN advanced may make significant investments in investment funds (UCITS, UCI) pursuant to section 71 of the 2011 Austrian Investment Fund Act.

For further information on the sustainable focus of YOU INVEST GREEN advanced as well as on the disclosures in accordance with the Disclosure Regulation (Regulation (EU) 2019/2088) and the Taxonomy Regulation (Regulation (EU) 2020/852), please refer to the current Prospectus, section 12 and the Annex "Sustainability Principles". In deciding to invest in YOU INVEST GREEN advanced, consideration should be given to any characteristics or objectives of the YOU INVEST GREEN advanced as described in the Fund Documents.

⚠ Risk notes according to 2011 Austrian Investment Fund Act

ERSTE REAL ASSETS may make significant investments in investment funds (UCITS, UCI) pursuant to section 71 of the 2011 Austrian Investment Fund Act.

⚠ Risk notes according to 2011 Austrian Investment Fund Act

ERSTE RESPONSIBLE STOCK DIVIDEND may exhibit increased volatility due to the composition of its portfolio: i.e. the unit value can be subject to significant fluctuations both upwards and downwards within short periods of time.

For further information on the sustainable focus of ERSTE RESPONSIBLE STOCK DIVIDEND as well as on the disclosures in accordance with the Disclosure Regulation (Regulation (EU) 2019/2088) and the Taxonomy Regulation (Regulation (EU) 2020/852), please refer to the current Prospectus, section 12 and the Annex "Sustainability Principles". In deciding to invest in ERSTE RESPONSIBLE STOCK DIVIDEND, consideration should be given to any characteristics or objectives of the ERSTE RESPONSIBLE STOCK DIVIDEND as described in the Fund Documents.

For further information on the sustainable focus of ERSTE BOND EURO CORPORATE as well as on the disclosures in accordance with the Disclosure Regulation (Regulation (EU) 2019/2088) and the Taxonomy Regulation (Regulation (EU) 2020/852), please refer to the current Prospectus, section 12 and the Annex "Sustainability Principles". In deciding to invest in ERSTE BOND EURO CORPORATE, consideration should be given to any characteristics or objectives of the ERSTE BOND EURO CORPORATE as described in the Fund Documents.

For further information on the sustainable focus of ERSTE RESPONSIBLE BOND GLOBAL HIGH YIELD as well as on the disclosures in accordance with the Disclosure Regulation (Regulation (EU) 2019/2088) and the Taxonomy Regulation (Regulation (EU) 2020/852), please refer to the current Prospectus, section 12 and the Annex "Sustainability Principles". In deciding to invest in ERSTE RESPONSIBLE BOND GLOBAL HIGH YIELD, consideration should be given to any characteristics or objectives of the ERSTE RESPONSIBLE BOND GLOBAL HIGH YIELD as described in the Fund Documents.

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