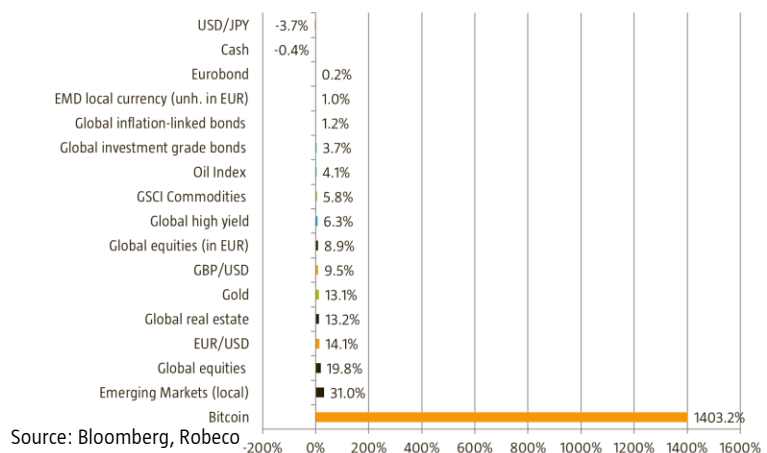


Multi-asset markets outlook

For professional users
January 2018

General overview

Mixed results, mostly a result of the stronger euro



May the force be with us!

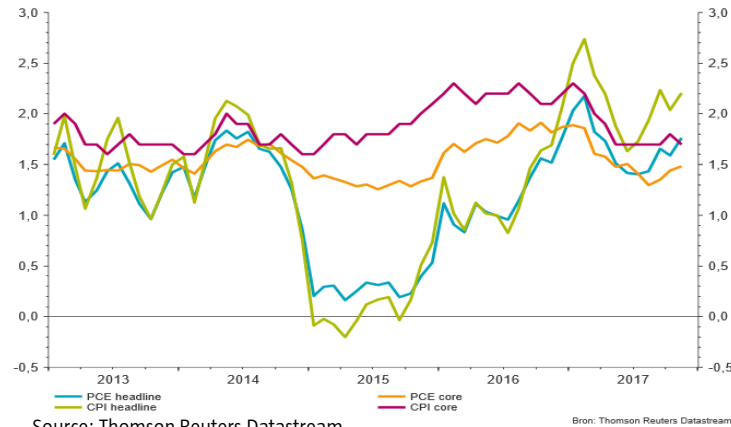
	Portfolio	BM	active	previous
Equities Developed Markets	31.0%	25.0%	6.0%	3.0%
Equities Emerging Markets	5.0%	5.0%		0.0%
Real Estate Equities	5.0%	5.0%		
Commodities	5.0%	5.0%		
Core Gov Bonds 1-10	12.0%	20.0%	-8.0%	-6.0%
Core Gov Bonds 10+	7.5%	7.5%		
Investment Grade Corp Bonds	20.0%	20.0%	0.0%	0.0%
High Yield Corp Bonds	3.0%	5.0%	-2.0%	-1.0%
Emerging Market Bonds LC	9.0%	5.0%	4.0%	4.0%
Cash	2.5%	2.5%		0.0%
EUR/USD	-3.0%	0.0%	-3.0%	0.0%
EUR/JPY	3.0%	0.0%	3.0%	1.0%
EUR/GBP	0.0%	0.0%		0.0%
EUR CASH	0.0%	0.0%		-1.0%

> And the winner is... well, you must have been living under a rock if you missed the real hype of 2017, the cryptocurrencies, with bitcoin acting as the poster boy. If you had had the stomach to live through the extreme volatility in the – erm, asset class? – you would have netted a nice 1,400% return in 2017 alone. For the more serious asset allocators out there, who are aware of not only returns but also risks, emerging markets were the best performing asset (+31% in local terms), while equities as a whole had a solid year (+20% in local terms). The surprising outlier was the euro, which gained 14% against the US dollar. The surprise is linked to the fact that whereas the Fed continued with its plan to raise interest rates in three steps, the ECB is still in full support-until-we-die mode, with the interest rate differential now clearly favoring the US versus the Eurozone. The euro turned out to not be the leading theme this year, as the decline of political uncertainty (various European elections did not end in a populist revolt) and solid economic data from the Eurozone dominated. The strength of the euro acted as a bit of a party pooper for all the non-hedged international assets, which for example hampered emerging market debt. The worst-performing asset class – not surprisingly – has been government bonds.

> 2018 started as 2017 ended, with risky assets moving higher. We do not disagree, as we are still overweight equities, but acknowledge that this low-volatile rally is not something that can last indefinitely. We also continue to be underweight bonds, sticking to our belief that yields will have to trend higher in the year to come. May 2018 be a happy year!

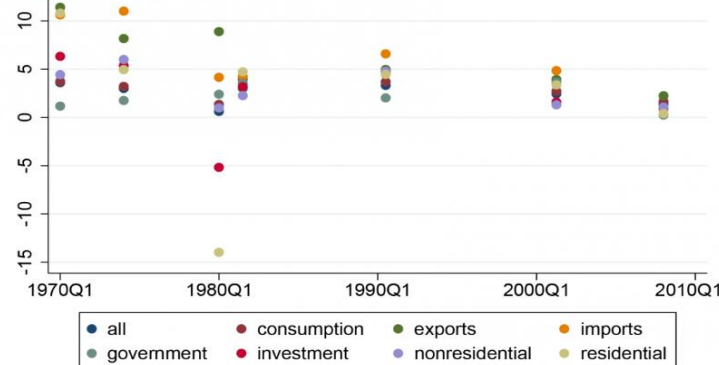
> United States

PCE is trending upwards



An unusually balanced US recovery

Figure 2 Average growth rate, with demand components (in real value, i.e., deflated by their own price deflator) percentage change

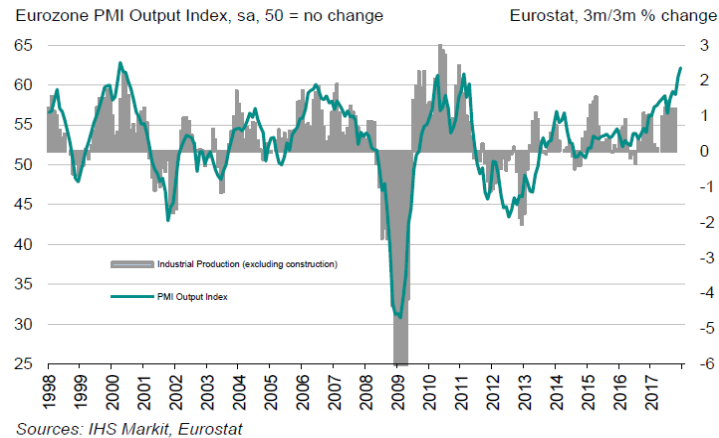


Sources: Bureau of Economic Analysis, demand components, average quarterly percentage change from one year earlier; National Bureau for Economic Research, recession data.

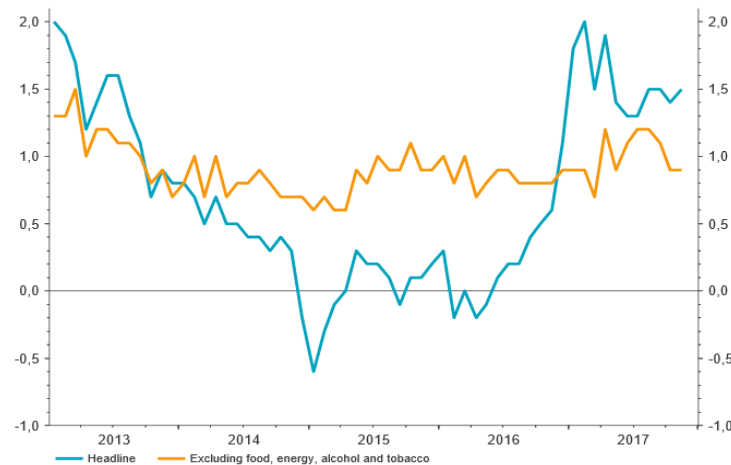
- > The US economy did well in 2017, growing about 2.25% , and economic momentum remains strong. Core inflation was well behaved, though the indicator preferred by the Fed, the PCE core, has bottomed and is now trending higher. The labor market continued to tighten, with wage gains staying subdued. Consumer confidence increased, as illustrated by the continuing decline in the personal savings rate to around 3%.
- > For 2018, the US economy will probably accelerate a bit from current levels, helped by the impact of pro-cyclical tax changes. These are expected to boost business investment, which also benefits from a loosening of the general regulatory environment. Unemployment could fall to as low as 3.5%, a level not seen since the 1960s.
- > A wild card is the speed of tightening by the Fed, as the new Fed chairman from February, Jerome Powell, a former lawyer, is an unknown quantity. With this in mind, and also given the current number of vacancies on the FOMC, including the vice chairmanship, the Fed will probably continue to tighten at a modest speed.
- > Risks to the outlook are mainly political, especially the risk of a trade war with China. The Trump administration initiated a trade case for the first time in over 25 years to fight cheap Chinese aluminum imports. It publicly rejected China’s position that it should legally be considered a ‘market economy’ in the WTO. Its new national security strategy identifies China as a ‘strategic competitor’ and a ‘revisionist power’.

> Europe

Eurozone business optimism hits a record high



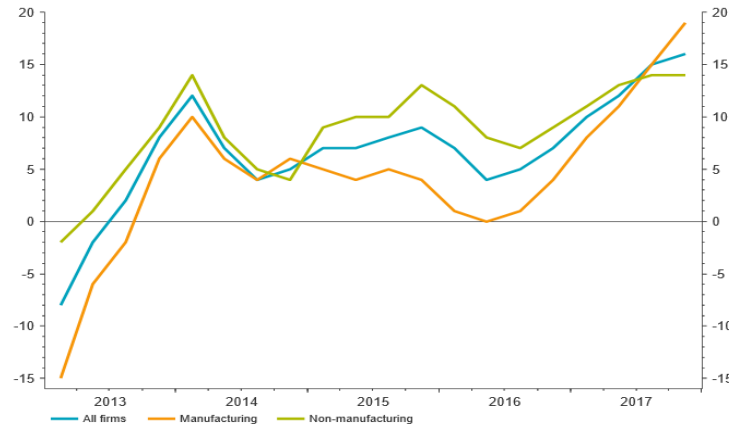
No rebound in core inflation



- > The Eurozone had a good 2017, with growth amounting to 2.5% – far above potential – and core inflation staying well behaved at a mere 1% on average. The latter allowed the European Central Bank to keep its QE program in place for the time being. It has tied its hands until September 2018.
- > Forward-looking indicators suggest that the coming hard economic data will be ‘sizzling’. The Eurozone economy will probably continue to grow at a speed of 2.5% in 2018. A positive factor is that the boom so far is much less driven by credit growth than in earlier upswings.
- > Given the strength of the recovery, It is unlikely that the governing council of the ECB will decide to extend its asset purchases beyond September. The tone of the so-far dovish rhetoric of the ECB president will probably shift in the course of the first half of 2018. A first hike in the refinancing rate will probably still have to wait until 2019.
- > The largest political risk for the Eurozone is who will form the new Italian government after the general elections on March 4. The most disruptive, but not very likely, outcome would be a coalition between the anti-euro forces, such as the Five Star Movement striking a deal with the Northern League and Brothers of Italy. More likely is a hung parliament, with the centrist parties eventually striking a deal.

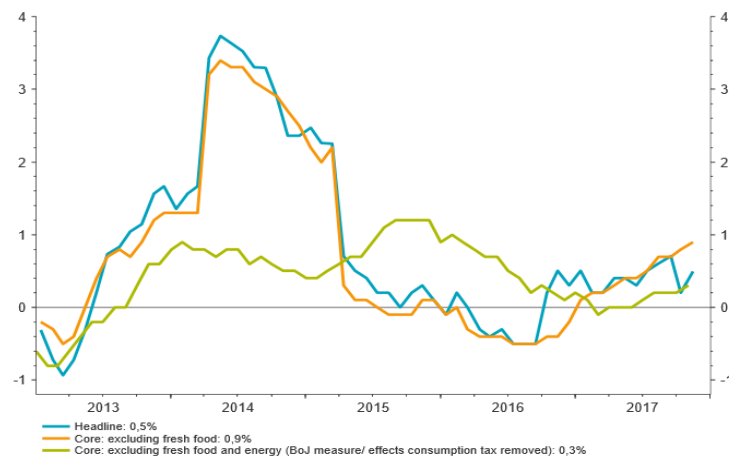
> Japan

Japanese manufacturing sector continues to improve



Source: Thomson Reuters Datastream

Japan's inflation trending upward, BoJ measure subdued

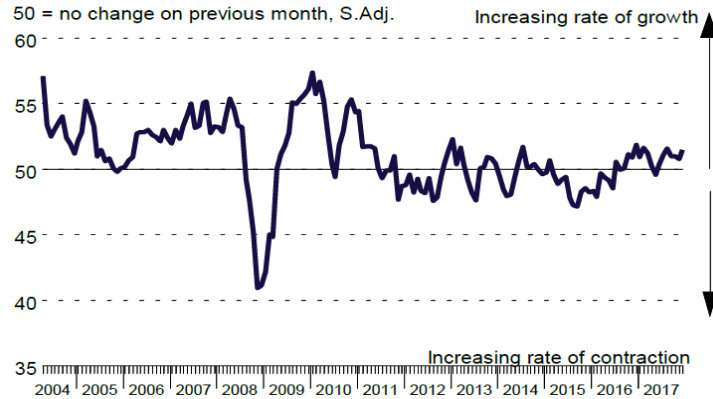


Source: Thomson Reuters Datastream

- > The Japanese economy did well in 2017, growing 1.8%, which is far above a potential which is estimated to be less than 1%. Inflation has started to show an upwards trend, though the actual numbers, especially the one preferred by the Bank of Japan, remain way below the 2.0% target. The unemployment rate continued to decline, reaching 2.7%, setting the stage for better wage gains. Exports grew strongly, helped by the synchronized worldwide economic boom and of course a weak trade-weighted yen.
- > Strong external and internal growth will enable Japan to continue above potential in 2018. Inflation will continue to rise in 2018, as a number of important areas of the Japanese economy are now facing systemic labor shortages, and wages for part-timers are rising nicely.
- > In April 2018, the five-year term of Bank of Japan Governor Haruhiko Kuroda will end. He is generally expected to be reappointed, and this will probably mean that the current aggressive quantitative and qualitative easing (QQE) and yield curve control (YCC) will be continued, contributing to further yen weakness. In the course of 2018, pressure will increase on the BoJ to reduce its extremely accommodative stance. This could result in the BoJ raising its target for 10-year yields slightly upwards in the second half of 2018.
- > Fiscal consolidation remains far off. The government's next test will come in October 2019, when the twice-postponed consumption tax hike from 8% to 10% is planned to be implemented.

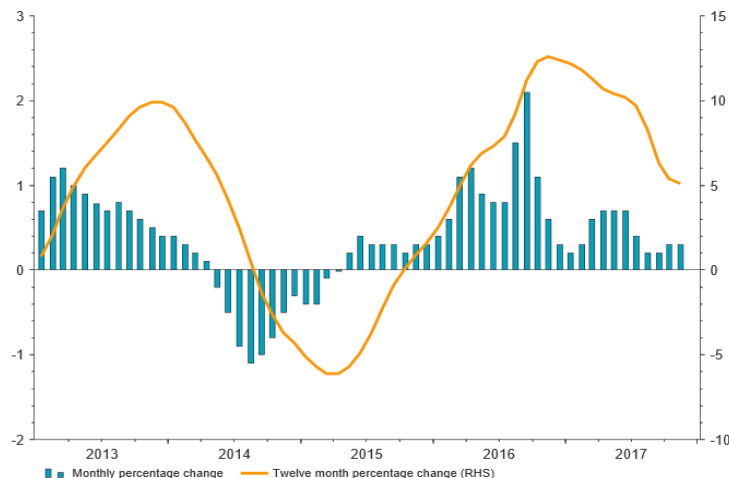
> China

Caixin China general manufacturing PMI is improving



Sources: IHS Markit, Caixin.

Change in new house prices (70 medium and large cities)

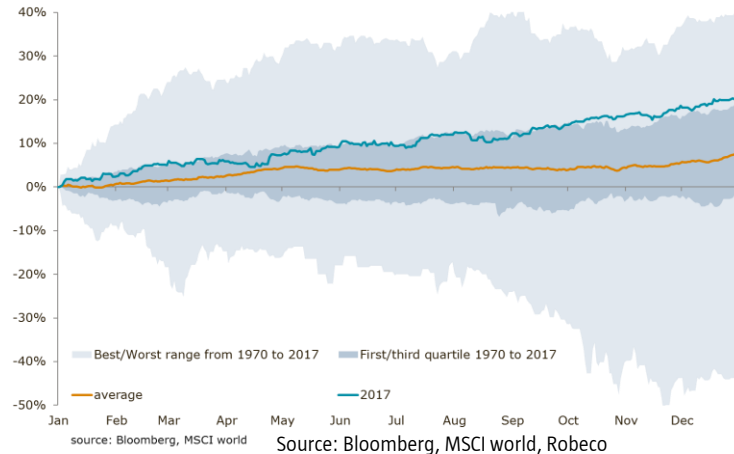


From: Thomson Reuters Datastream

- > The Chinese economy grew strongly in 2017 at a rate of about 6.8%. Growth was driven by expansionary fiscal policy, engineered to create a benign background for the 19th Communist Party Congress. President Xi Jinping consolidated his power base in line with expectations; failing to appoint an obvious successor in the new politburo created the impression that he intends to remain as president (long) after 2020, breaking with recent Chinese precedent. The reappointment of Prime Minister Li Keqiang suggests a broad continuation in economic policies.
- > A well-known problem of these policies is the unsustainable rise in debt. Non-financial sector debt (including federal and local government debt) has reached around 240% of GDP. After the party congress, fiscal stimulus was reduced, and the People’s Bank of China imposed tighter credit policies including higher interest rates. This has resulted in slightly lower growth in bank lending.
- > The rate of increase in housing prices reduced markedly in 2017, understandably given the severe amount of excess capacity. However, as local governments rely heavily on land taxes and give a high priority to social and political stability, it is likely they will step in once again to prevent a further slide.
- > In general we expect the Chinese authorities to kick the can further down the road, which in all likelihood will again result in strong growth (at least 6.5%) without addressing the longer-term debt challenge.

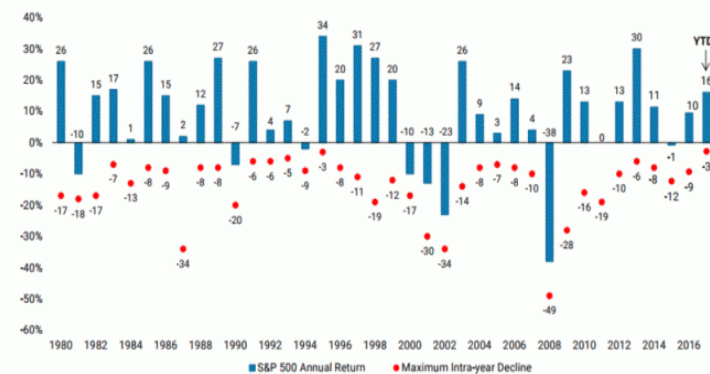
> Equities (I)

Another month, another new all-time high



The no-dip year of 2017

Exhibit 2: Equity Markets Typically Exhibit Much Greater Drawdowns than What We Had in 2017

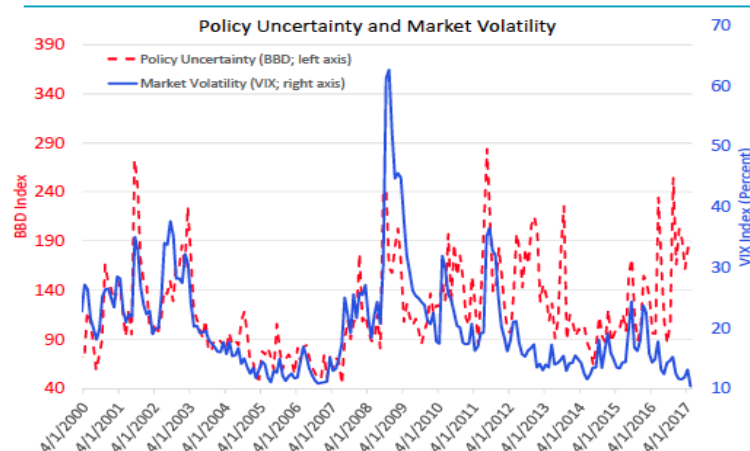


Source: Bloomberg, Robeco

- > One of the most striking features of stock market performance in 2017 has probably been the lack of volatility. Taking the S&P 500 as an example, the index rose by 19%, with the biggest drawdown during the year reaching a maximum of -3%. If only Trump had refrained from tweeting about the 'rocket man', 2017 would have been the lowest loss year on record, robbing 1995 of its title. It was not just the US market though, as the gentle upward sloping trend was seen across the globe.
- > Ten years from now, we will have no problem in explaining this very smooth run. 2017 was a year in which the world economy finally managed to stage a synchronized growth acceleration, and was the first year that the IMF had to raise rather than lower its growth outlook. Europe, the US and even Japan managed to perform above potential, and although the emerging economies (with the exception of China) fell somewhat short in relative terms, momentum clearly picked up as well. Despite the positive growth momentum, inflation – the usual suspect to spoil the party – has been broadly absent, opening the way for most central banks (ECB, BoJ) to keep the monetary floodgates fully open. Goldilocks for everybody: what's not to like?
- > Although this sounds like a plausible storyline which certainly has merit, it does not tell the full story. For one, it ignores the clear increase in political uncertainty seen across the globe. Brexit and especially Trump have shaken up the political status quo in a major way, and has often left bystanders guessing on what the potential implications are >>

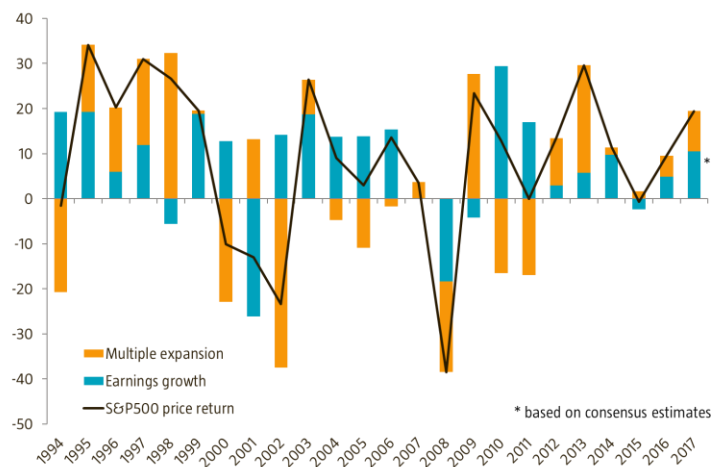
> Equities (II)

Earnings have rebounded, but far less so than stocks



Source: <http://voxeu.org/article/puzzle-high-policy-uncertainty-and-low-market-volatility>

It has been a PE multiple expansion rally

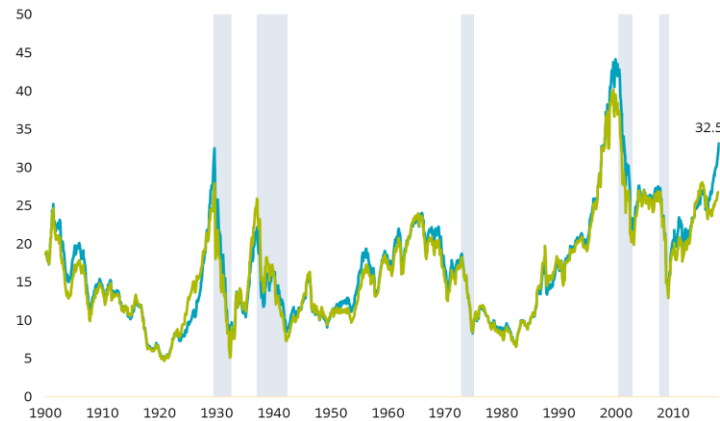


Source: Bloomberg, Robeco

- > going to be. Whereas in the past, stock volatility and political uncertainty went hand in hand, uncertainty was completely ignored in 2017. Even a setback as small as 3% was seen as a good 'buy-the-dip' moment, thereby creating hardly any dips during the year. This low volatility was not just a feature of the stock market, but has been a general element in all financial markets.
- > One part that has been ignored is the valuation of US stock markets. Despite the strong momentum and the positive earnings growth, 2017 was the seventh consecutive year in which the S&P 500 gained (well) in excess of reported earnings. Not surprisingly, the US stock market has become expensive. 2017 started with a regular Shiller PE of 28x and ended at 32.5x. One could claim that this is due to the lagging nature of the earnings component (10-year trailing), or that this number is distorted by the extreme earnings dip in the 2008-2010 period. Even if we correct for the latter factor (by effectively looking at a seven-year Shiller PE), the adjusted level of 26.7x can still be considered lofty. Of course, people will point out that this is linked to the fact that the US market is the only one that has true exposure to the new-economy-internet sector, with its Facebooks, Googles and Amazons, and that this sector is bound to just keep on expanding. True as that may be, we have seen this argument before, and it didn't end well the last time (the 2000-2003 correction). The positive point to make is that whereas the US is expensive, this is certainly not true for European and Japanese markets.

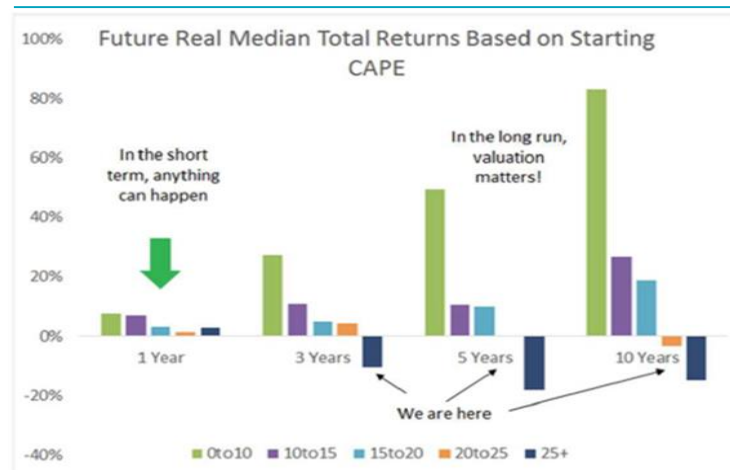
> Equities (III)

The US market has become expensive



Source: Shiller, Robeco — Periods of 40%+ corrections — Shiller PE — Shiller PE (7 years)

Valuation is never a good timing mechanism

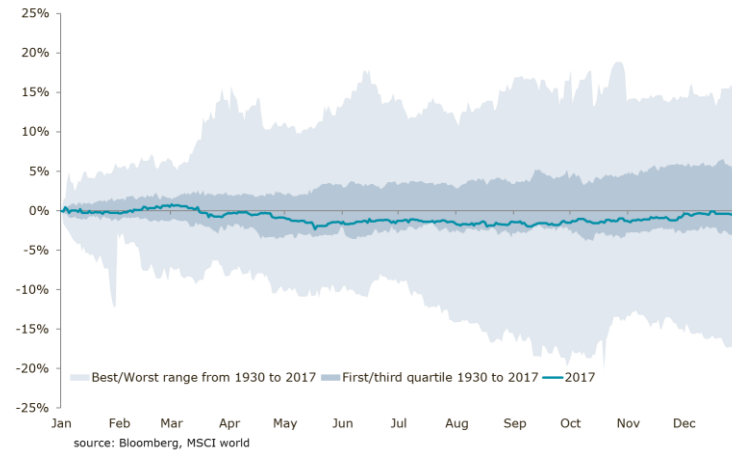


Source: Bloomberg, Robeco

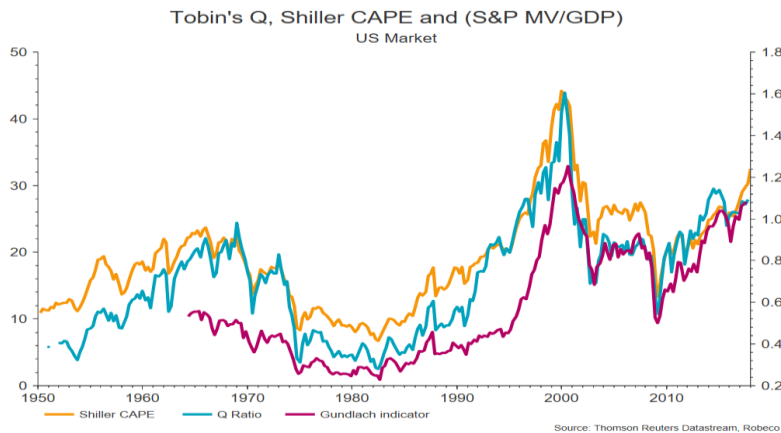
- > The most credible explanation for the continued low volatility and steady rise in stocks is the continued dominance of the supportive central banks. True, the Fed has been in tightening mode, and even the Bank of England was forced to implement a one-time-only rate hike, but both the ECB and the Bank of Japan have kept their engines running at full throttle.
- > So what will 2018 bring? More volatility, for sure. If this sounds like a bold statement, think again: it is statistically almost impossible to get a second year like 2017. With the VIX ending 2017 at an all-time low, it is a bit of a no-brainer to state that volatility is set to rise. Having said that, there are plenty of potential sources of uncertainty that could come to the fore in 2018. The comeback of wage inflation, more rate hikes by the (new?) Fed, a turn in monetary policy by both the ECB and the Bank of Japan, China's debt, the Italian elections, the 'rocket man'; there are plenty of things that could spell trouble in 2018. In fact, we would welcome a bit more volatility, as the current nothing-can-go-wrong feeling in combination with extremely cheap credit is a pretty toxic combination, and one which is bound to lead to a wrong assessment of the risks that are out there.
- > At the same time, as we indicated last year, this is a very momentum-driven market, and as we saw back in 1996-2000, exiting such a market too early can be extremely costly. We therefore continue to be overweight equities.

> **Developed Market Equities**

Despite a weaker dollar, US stocks keep their MSCI weight steady



Well flagged risk: all indicators show US equities are expensive

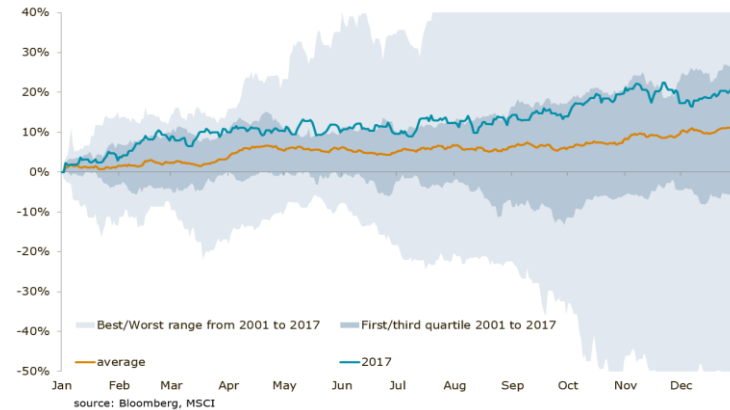


Source: Thomson Reuters Datastream, Robeco

- > It was a remarkable year for developed market equities, as the mature bull market again managed to deliver annual returns above its historical average. Anticipated to be a tough year, given further tightening by the Fed and a busy political agenda, 2017 clearly surprised to the upside for equities. Double-digit returns for major regions were generated at an unremarkably slow but steady pace, with small daily gains and losses. This very low realized equity volatility portrays rational exuberance against a very benign global cyclical backdrop. Equities have become even more expensive, but 2017 did not exhibit outsized price swings that signal a bubble. Earnings per share growth has contributed to overall returns, as corporates saw improved top-line revenue growth and pricing power. The ranking on the basis of annual equity returns in local currency showed the S&P 500 with a gain of 19.4% over the year, just outperforming Japan's return of 19.1%. Europe lagged considerably in local currency terms, returning 7.7%.
- > Looking ahead, we expected global macro momentum to remain largely intact in 2018, underpinning a continued positive stock market momentum. In this late phase of the bull market we focus on regions that have a higher exposure to the global cycle, still have margin upside and are fairly resilient to the modest rise in interest rates that we expect. While forward earnings expectations by analysts have been downgraded in recent months for Japanese and European equities, our above-consensus growth outlook for these regions bodes well for continued strong earnings growth. Relative valuations of these regions compare favorably with the US, which is the most expensive area.

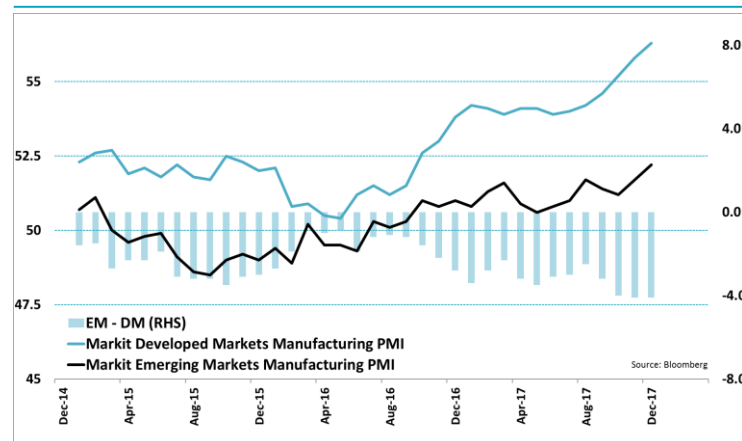
> Equities: Emerging vs Developed (I)

Emerging market equities' annual returns



Source: Bloomberg

Manufacturing PMI – emerging versus developed markets



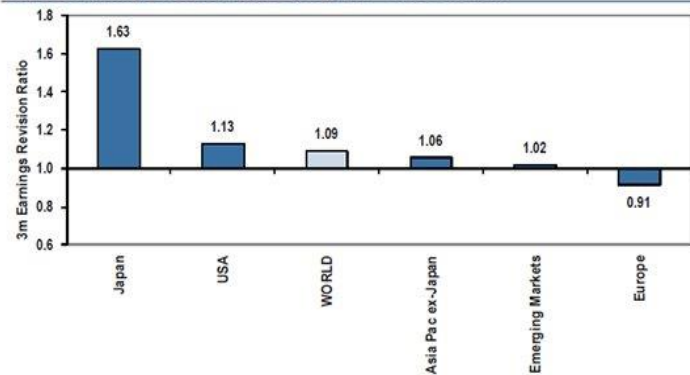
Source: Bloomberg

- > The MSCI Emerging Markets Index realized a return of just over 20% in euro terms in 2017. It was the best year for emerging market equities since 2010, beating the MSCI World Index in euros by a fairly wide margin. Compared to the MSCI World Index hedged to euros however, the difference was a less outspoken 3.5%.
- > In 2017, emerging markets as a group profited from a number of countries that experienced an economic turnaround. Two examples are Brazil and Russia, which also profited from higher commodity prices. Brazil recovered from its worst recession in decades. China, by far the biggest emerging market, also performed very well as its economy proved more resilient than expected, even as the government succeeded in reducing credit growth.
- > In addition, emerging markets also were beneficiaries of central bank policies. Inflation came down significantly last year, which meant emerging central banks could lower rates. More importantly, developed market central banks continued with their stimulus, with the exception of the US Federal Reserve, which kept the liquidity-driven rally going.
- > Finally, a weak US dollar also helped emerging market equities to outperform. Even though the Fed was the first of the major central banks to withdraw liquidity, the greenback lost value against almost every currency.

> Equities: Emerging vs Developed (II)

Earnings revisions

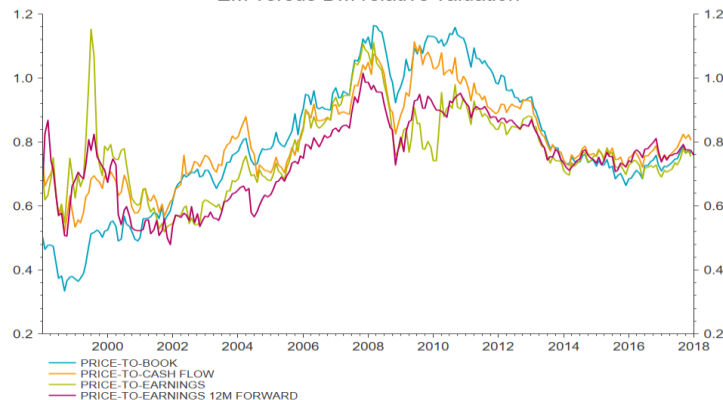
Chart 6: Earnings Revision Ratio by Region – Last 3 Months



Source: BofA Merrill Lynch Global Quantitative Strategy, MSCI, IBES

Valuation

EM versus DM relative valuation



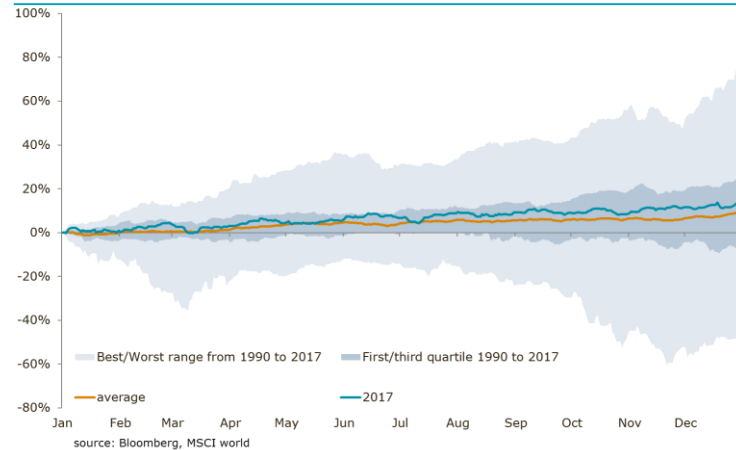
Source: Thomson Reuters Datastream, Robeco

Source: Thomson Reuters Datastream, Robeco

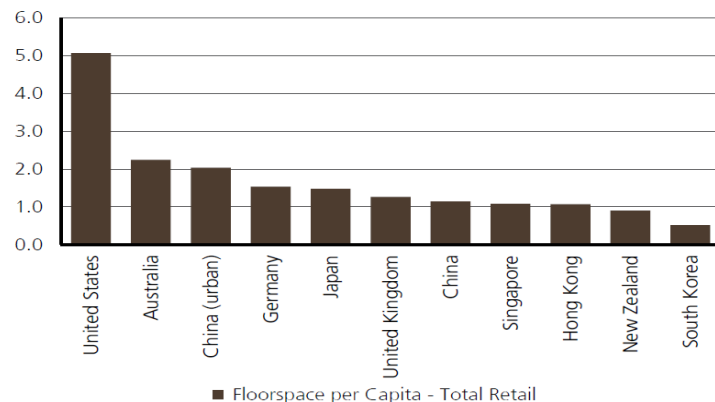
- > While we have become more constructive on emerging market equities, partly driven by strong momentum, we are not fully committed to an overweight yet. First, historically the relative growth momentum between emerging and developed markets has been an important variable driving relative stock market performance. Based on the Manufacturing PMIs, the relative economic momentum of emerging against developed has weakened. We do believe, however, that we are now closer to a stabilization, or perhaps a reversal of this trend.
- > The development in earnings has improved, but still lags many other regions. Expected earnings growth is among the highest in the world, but earnings revisions are barely above 1. Also, higher expected earnings growth is not necessarily a positive, as analysts tend to be overly exited about the new (calendar) year. In most years, earnings growth expectations are revised down in the first half of the year.
- > Despite the outperformance of emerging markets in 2017, valuation remains relatively attractive, although less so than in previous years. As mentioned above, price momentum is a positive, albeit less so against the MSCI World Index hedged to euros. We have some difficulty in assuming that the depreciation of the US dollar will continue, especially at the current pace. Also, we would like to see a change in improvement in relative economic momentum before initiating a long position. That said, more factors have fallen into place to be able to take a more positive stance on emerging market equities.

> Real estate

2017 was an above-average year for real estate, though it didn't feel like it



US retail 'shop-space' in comparison with the rest of the world

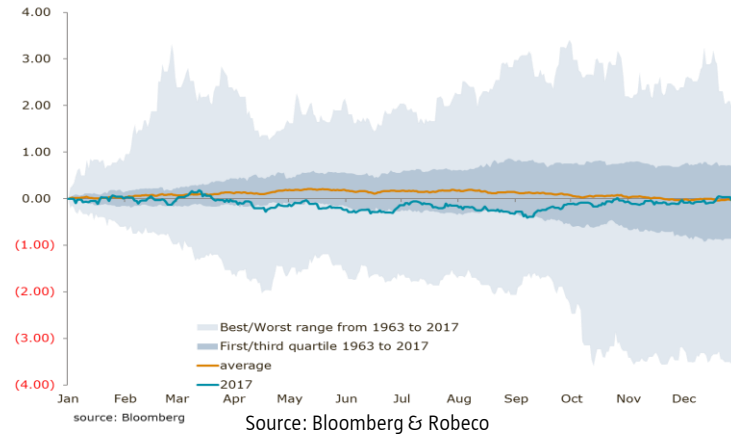


Source: Urbis, ICSC, Japan Council of Shopping Centres, CRE Global Investors, Cushman & Wakefield, UBS estimates

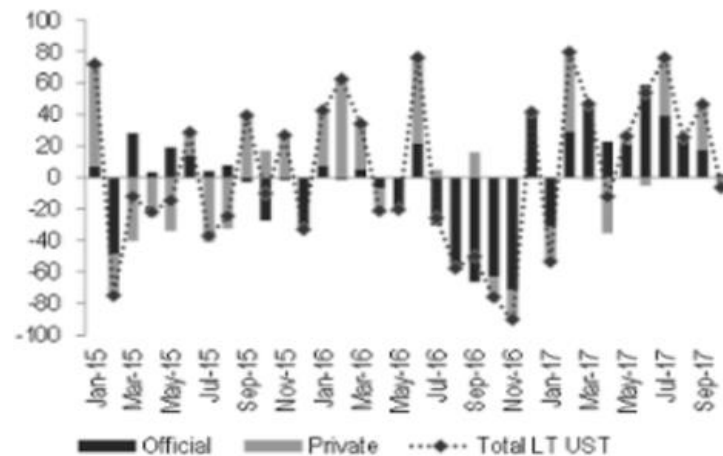
- > Global real estate had a very decent year, with a total return of 13.5% (S&P Developed Property, total return, in US dollars), above the long-term average of 9.5%. The only thing is: it didn't feel that way. Global equities in US dollars returned 22%, so compared to that, the underperformance was significant.
- > The main reason for the underperformance was the poor performance of US real estate. US REITs were impacted by the Fed policy change, with three rate hikes administered in 2017. Added to this were the 'Amazon fears' that shopping malls will be replaced by e-commerce. As US 'shop-space' per capita is twice as high as the rest of the world, and retail REITs make up about 20% of the index (and the US weight of about 60% in the global property index), the effect was mainly noticeable in the US.
- > We expect the US real estate sector to have a difficult year. As the Fed is still tightening, longer-dated yields look vulnerable. The recent tax plans seem to be better for sectors other than real estate. On the other hand, valuations are attractive compared to equities. The dividend yield spread of 2% is at the historical average level.
- > Continental Europe is the most attractive region, while the Japanese REIT market is distorted by BOJ buying. We expect that although the absolute return of real estate might not be bad, compared to equities we think 2018 will be another difficult year in relative terms. We are cautious, but still neutral.

> AAA Bonds (I)

2017 was just an average year for German 10-years



In 2017, foreign holdings of US Treasuries increased



Source: Bloomberg

- > If we take a broad look back at 2017, the main conclusion appears to be that it was a pretty average year. On balance yields doubled, but with a starting yield of 20 basis points in January, that can hardly be called shocking. Throughout the whole year, yields traded in a broad trading range of 20 to 60 bps, with yields ending the year almost bang in the middle of that. Although this is a move away from the negative yields seen in 2016, so far the slope of the rising trend is pretty unimpressive.
- > When we reflect back on the investment choices we made in 2017, with regards to sovereign bonds on a whole we have to be disappointed. We thought that 2017 was going to be the year in which the journey towards normalization of monetary policy would gain traction within the developed world. Unfortunately, this theme didn't materialize as we expected. While indeed the Fed continued on the path it started to tread in 2016, and delivered on its promise to start scaling back its quantitative easing program, the bond market reaction to this was muted. This was kind of reminiscent of the so-called Greenspan conundrum back in the 1990s. Just like then, foreign demand for US Treasuries was massive, complicating the central banks' monetary policy. The gap between where the Fed sees the neutral rate and what the market thinks it is remains wide, although it must be noticed the market moved more towards the Fed's view in the fourth quarter. 2-year rates increased by 40 basis points while the Fed only hiked by 25 basis point this quarter.

> AAA Bonds (II)

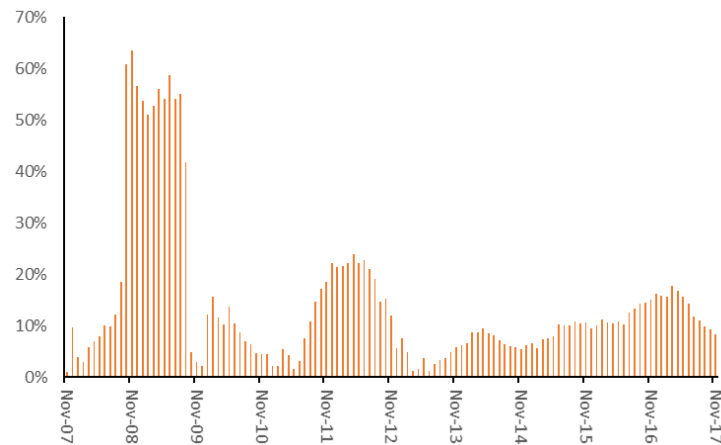
Both the Fed and ECB expect firmer growth but flat inflation

ECB	Change in forecast			Latest forecast			
	2017	2018	2019	2017	2018	2019	2020
GDP	0.20	0.50	0.20	2.4	2.3	1.9	1.7
UER	0.00	-0.20	-0.30	9.1	8.4	7.8	7.3
Inflation	0.00	0.20	0.00	1.5	1.4	1.5	1.7

Federal Reserve	Change in forecast				Latest forecast			
	2017	2018	2019	2020	2017	2018	2019	2020
GDP	0.10	0.40	0.10	0.20	2.5	2.5	2.1	2.0
UER	-0.20	-0.20	-0.20	-0.20	4.1	3.9	3.9	4.0
Inflation	0.00	0.00	0.00	0.00	1.5	1.9	2.0	2.0

Source: BNP, Fed & ECB

Slower YoY growth rates but G-4 central bank balance to GDP is still expanding

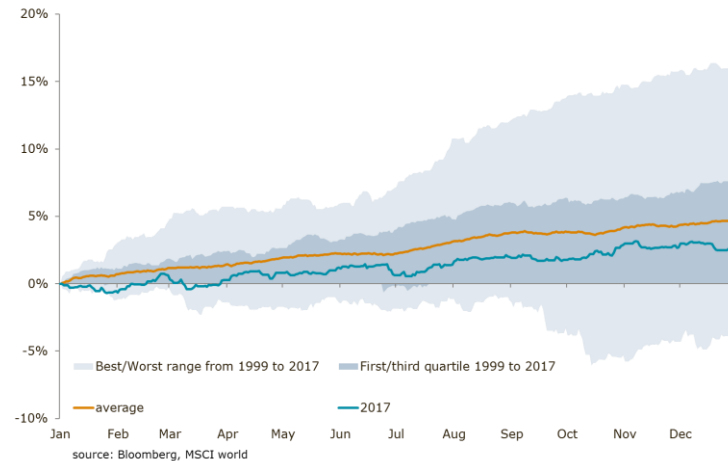


Source: Bloomberg & Robeco

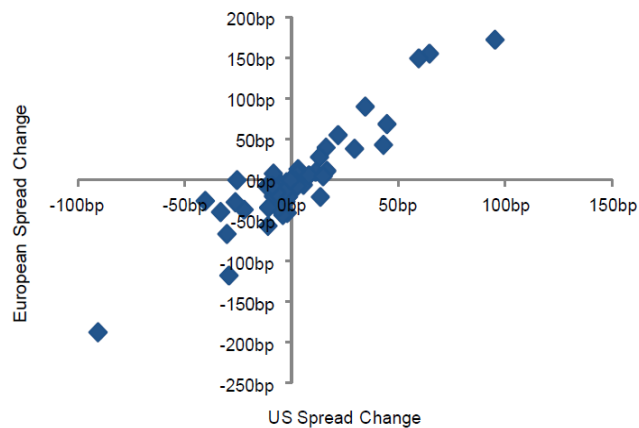
- > While the Fed slowly tiptoed towards tightening, both the Bank of Japan and the ECB confirmed their commitment towards aggressive easing in 2017. We think this was one major reason why rates disappointed this year. So what do we expect for the coming year? More of the same? We stick to the view that yields need to rise. We strongly believe that the days of massive quantitative easing are behind us. In 2018, the balance sheet wind down of the Fed will accelerate, and the ECB is already committed to taking its foot off the gas. The wild card remains Japan, but we got the impression at the end of 2017 that Kuroda might be in the process of rethinking BOJ policy. Added to this, we continue to think that growth will hold up.
- > The question, however, remains if this will be the year that growth starts to create upward inflationary pressures. Inflation remained absent last year and allowed central banks to continue to be relaxed and take it easy. Central banks seem to have already accepted that inflation will not return, as they raised their growth forecasts on the one hand they kept their inflation expectations stable.
- > 'Stable' is pretty close to their respective targets though (with the exception of Japan). We stick to our view that rates are just too low given current economic reality. We accept that inflation is currently not at threatening levels, but inflation is and remains a lagging indicator. The major risk to our call is a sudden return of risk reversion either driven by geopolitics (North Korea) or a growth scare.

> Investment Grade Credits (I)

Performance of European credits has been below average



Historical correlation between European and US credit spreads

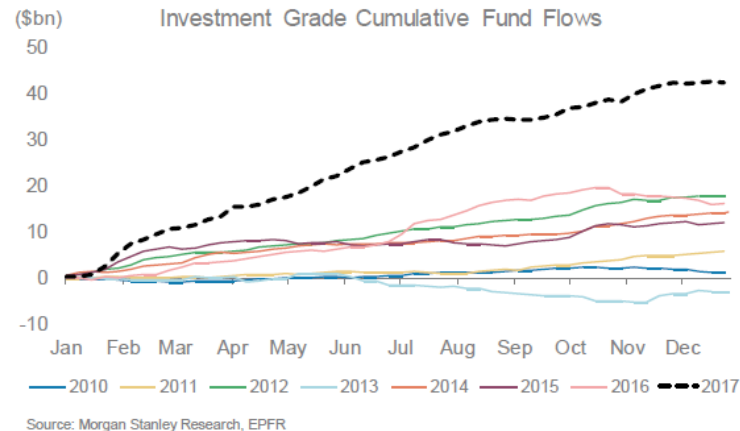


Source: SG Credit research

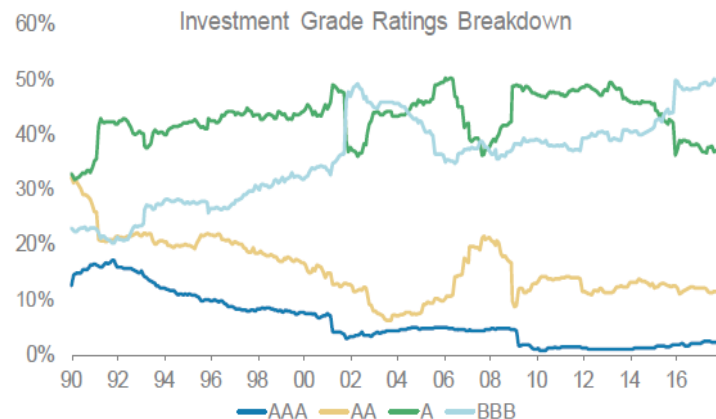
- > It depends on which comparison you make as to whether you have a positive view on credits in 2017 or not. Compared to the long-term average, the total return on European credits was disappointing: 2.4% for 2017 against a 4.7% average. For a lot of investors, however, this was an attractive yield compared to European government bonds or cash, which yielded around 0% or negatively last year. During 2017, spreads tightened gradually from 1.22 to 0.84.
- > So, we start 2018 with low yields and tight spreads. This has happened before and might be the reality for some time to come. However, with these low yields and spreads, the European credit market is expensive. Looking at the credit fundamentals in Europe, these seem fine. Of course, leverage is an issue, but default rates remain very low and European economic data is still good. The CSPP program is still in place, and although the ECB announced a tapering of the current stimulus program, the ECB keeps being friendly for the European corporate bond market for the time being.
- > But there is another technical that is a growing worry: the US corporates that issue euro-denominated bonds because the lower yields in Europe are attractive. This makes the European credit market vulnerable for the problems (high leverage etc.) in the US corporate markets. The correlation between US and European yields and spread movements has historically been high, at around 90%. This time won't be different we think, so possible troubles in the US will almost certainly lead to spread movements in Europe.

> Investment Grade Credits (II)

Fund flow in US investment grade credit is at a record high



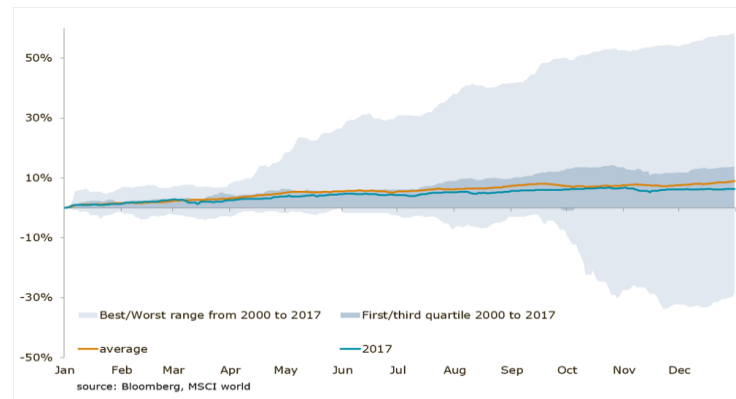
US credit quality is at low levels



- > It should come as no big surprise that the yield and returns on US credit markets look the same as in Europe, albeit on a higher absolute level. Measured in US dollars, the total return on US credits was 6.4%, underperforming the long-term average by 1.5%. The spread tightened from 121 basis points to 94 bps at the end of the year. The attractive yields with relative low risks attracted a lot of new investors, as fund flows more than doubled compared to historical flows.
- > As mentioned several times before: although US economics look good for credits, the technicals do not. Leverage has peaked and is at early 2000s levels. Spreads and yields indicate that US credits are very expensive. Besides that, quality has deteriorated; almost half of the issuance in 2017 was low quality BBB. Fed policy, which like ECB policy has been a key driver of credit performance in recent years, is turning from a tailwind into a headwind. The expected balance sheet tightening and rate hikes for 2018 will almost certainly have negative effects on the credit performance.
- > The starting point for 2018 for US credits is therefore even weaker than for their European counterparts. European credits have at least the ECB as a back-up for the first period of the year, but we don't see room for a further significant tightening of spreads. From a yield perspective, European credits aren't interesting, but they offer a small carry compared to cash. We have a neutral weight for credits, but are increasingly cautious.

> High Yield (I)

High yield – annual return



Source: Bloomberg

Global high yield bond spread

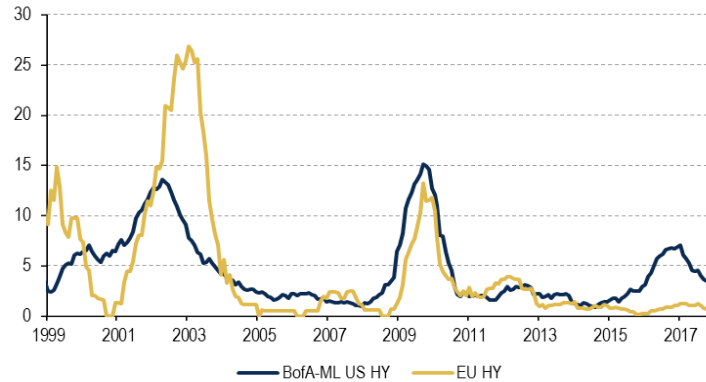


Source: Bloomberg

- > Global high yield bonds realized a return of 6.3% in 2017. This makes them the best performing fixed income-related asset class, beating local currency emerging debt and global government bonds by 5.3% and 5.9% respectively.
- > Most of the return can be attributed to the decline in high yield bond spreads during most of the year. In early January, the spread averaged 425 basis points, ending the year at 339 bps, a total decline of 86 bps. The average spread level is currently among the lowest in history. That said, in the run up to the financial crisis, spreads fell as low as 200 bps.
- > Just like the year before, high yield bonds profited from a continuous search for yield as central banks – with the exception of the Fed – maintained their extremely loose policy stance. In the second part of the year, high yield bond performance was helped by a surprisingly strong economy globally.
- > However, as spreads fell, high yield bonds became more and more expensive. As valuations rose we became less enthusiastic about the asset class, resulting in an underweight position implemented towards the end of 2017. The yield buffer against rising government bond yields (our base case) or a less favorable macro economic conditions (not our base case) decreased substantially last year.

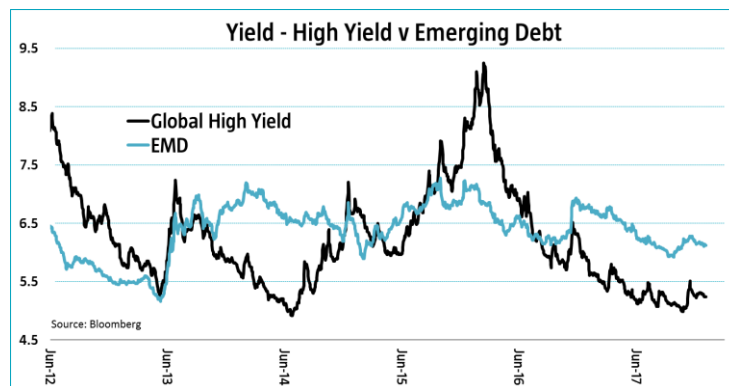
> High Yield (II)

Default rates



Source: BofA Merrill Lynch

High yield – relative attractiveness

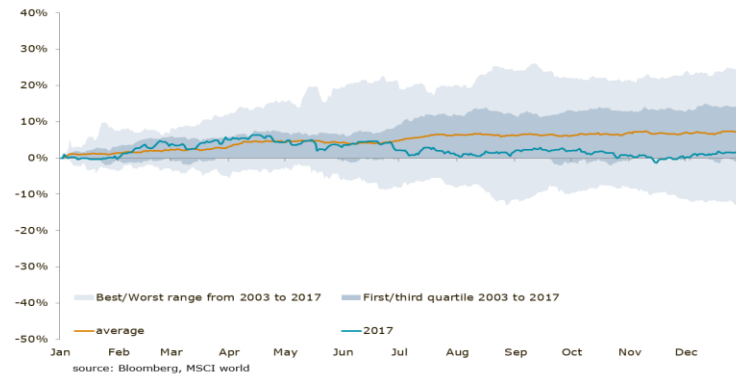


Source: Bloomberg

- > Over the course of 2017, the leverage of high yield companies has crept up, especially in the US. This makes them more vulnerable to rising interest rates. At this point in time however, the maturity wall doesn't look disturbing.
- > As GDP growth is expected to stay firm in 2018, default risks remain muted for now. In Europe, where the average rating of high yield companies is higher, default rates remain close to zero. We expect this to stay this way for the foreseeable future. Default rates in the US are higher, but have fallen considerably in the last 12 months. Recent months saw some specific default cases, though we don't expect this to broaden.
- > That said, we do not rule out some degree of spread widening, especially in the second part of the year, as growth could cool down. If this possible peak in growth momentum coincides with central bank liquidity turning negative (in early 2019), this could pose a challenging environment for high yield bonds.
- > We think other risky asset classes offer a better risk/reward trade-off at this point in time. The running yield on high yield bonds has fallen considerably below the yield on local currency emerging market debt. In addition, the gap between high yield and the earnings yield (inverse PE) of equities has almost closed. We find that Eurozone and Japanese equities and emerging debt are more attractive.

> Emerging Market Debt (I)

Emerging market debt in local currency – spread



Source: Bloomberg

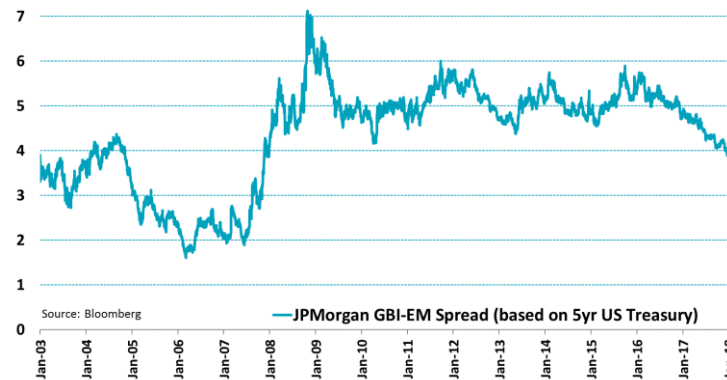
Emerging currency performance



- > Despite the risk-on sentiment in financial markets for pretty much the whole year, local currency emerging market debt struggled in 2017. At the end of December the asset class returned just 1.0% in euros. However, this still beat the return of 0.4% of global government bonds. As we opted to overweight local currency emerging debt at the expense of governments bonds, the overall portfolio effect was positive, but obviously not to the extent that we expected.
- > In 2017, the surprising strength of the euro hit the returns of local currency emerging debt. Emerging currencies depreciated significantly against the euro. As the chart on the bottom left shows, there was a massive gap between the performance of emerging currencies against the US dollar and the euro. Over the course of 2017, emerging currencies gained more than 5% against the dollar, but lost more than 7% against the euro. For comparison, this is more than the running yield on our benchmark index, the J.P. Morgan GBI-EM Diversified Composite Index in euros.
- > However, as mentioned above, the asset class still managed to realize a positive return. As the top chart on the next slide shows, emerging debt spreads measured against the US 5-year Treasury yield fell throughout 2017. As economic growth firmed globally, many emerging countries profited, enabling them to reduce economic imbalances such as current account deficits. The lower spread can also be attributed to the ongoing search for yield that characterized 2017, as well as in the years before.

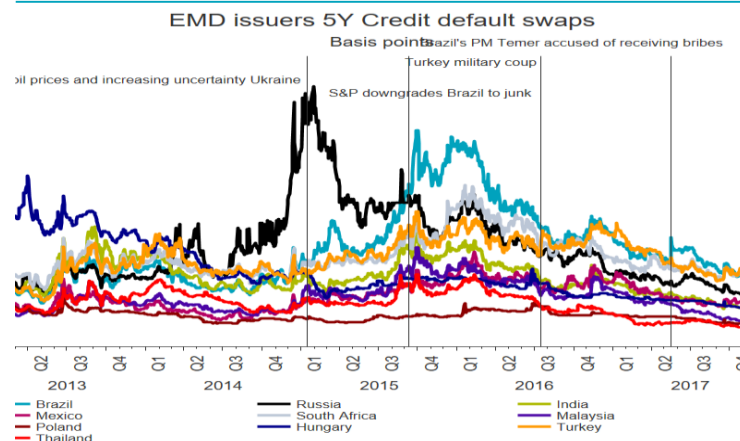
> Emerging Market Debt (II)

Manufacturing PMI: emerging versus developed markets



Source: Bloomberg

High yield versus emerging market debt yield



Source: Bloomberg

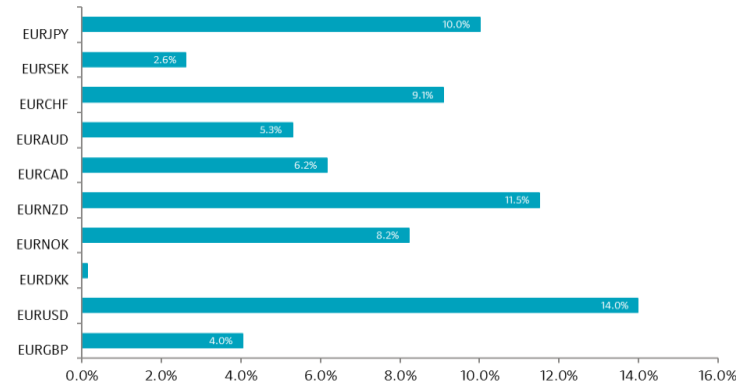
- > We expect global growth to be maintained, if not increased, in the coming quarters, giving emerging countries more room to rebalance their economies. This should further increase the creditworthiness of emerging governments (as shown in the chart on the bottom left), at least on average. Just like we have seen in 2017, with South Africa and Turkey under severe pressure as a result of economic and political tensions, event risk remains elevated for this asset class.

- > Taking into account last year's surprisingly large depreciation, we're inclined to say that emerging currencies should fare better this year. They are not expensive and tend to rise against developed market currencies when global growth accelerates. However, we do realize that this expectation is surrounded by a fair margin of risk.

- > We think the search for yield will go on, at least for the foreseeable future. In combination with a better economy and the positive sentiment towards risky assets, we believe local currency emerging debt should outperform other fixed income asset classes. In addition, valuation looks attractive. As inflation has come down significantly in emerging markets, real rates are much higher than in most developed markets. Eurozone government bonds look particularly vulnerable from a valuation perspective. But we also expect emerging debt to outperform high yield bonds for now.

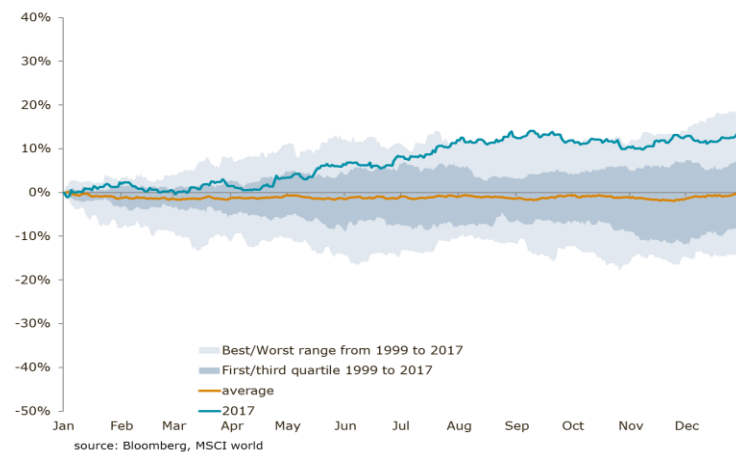
> FX (I)

EUR/USD takes the top spot in 2017



Source: Bloomberg, Robeco

Very strong momentum for EUR/USD in the second half of the year

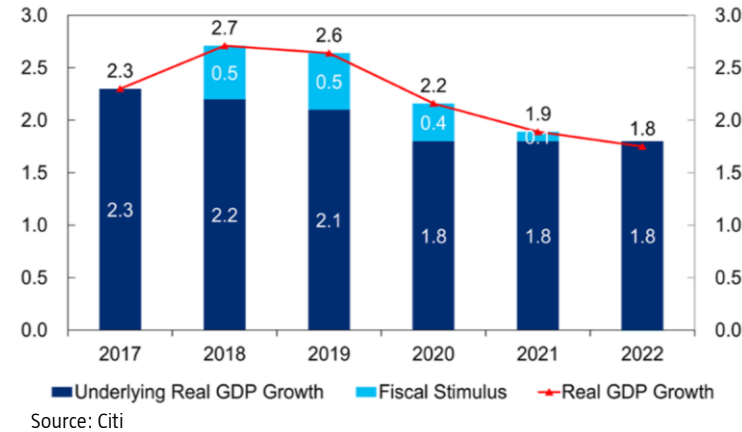


Source: Bloomberg, Robeco

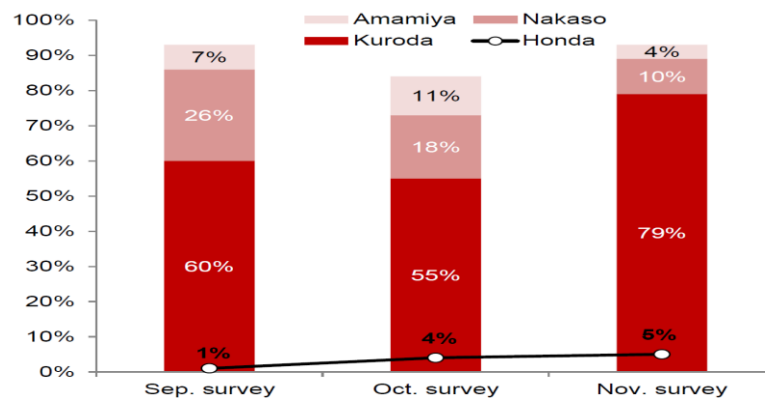
- > 2017 turned out to be the year of the euro. While it strengthened against all its G-10 peers, what stood out was its massive appreciation against the US dollar. For a good part of the first half of last year, the EUR/USD pair meandered between well-defined boundaries. This changed towards the second half of the year. In the third quarter, the euro gathered momentum. If you had told us at the beginning of the year that the euro would end up as the winner of 2017, we would have strongly argued against that, as we thought the stars were better aligned for a continuation of a stronger US dollar.
- > We think that the appreciation of the euro against the dollar could turn out to be an important signpost, as it could flag an expected shift away from monetary policy divergence to policy convergence.
- > A major support for the euro was receding political risk. Since the debt crisis, political risk was something that continued to be associated with the Eurozone. After Brexit and Trump, the market braced for a continuation of this revolt against the establishment. Macron’s win in France however eased those fears, which has supported the euro.
- > What we got wrong was to think that the driver of currencies would continue to be policy divergence: the fate of the EUR/USD would be determined by the fact that the ECB’s monetary policy remains much more accommodative than that of the Fed. While this was indeed >>

> FX (II)

The tax plan will boost US growth



Investor Survey: The market expects Kuroda to be reappointed



Source: Nikkei Quick & Nomura

- > the case, the potency of these drivers diminished in 2017. The market not only seems to have already fully discounted this policy divergence, but also concluded that the chances are rather slim that even the less-dogmatic ECB will be able to find a way to prolong its current policy settings for much longer. The fact that Draghi's eight-year term is also coming to an end in October 2019 may strengthen the view that the end is nigh. So going forward, we need to start taking into account the fact that other drivers will start demanding a bigger role in determining the value of the EUR/USD. One driver that could gain traction is the reacceleration of the differential in the balance of payments.
- > We can't rule out that the dynamics that played out in EUR/USD in 2017 will not start to assert themselves in USD/JPY in 2018. So the chances are real that at some point during 2018, the market will start to reconsider the longevity of the Bank of Japan's current policy settings. The similarities are there – as with Draghi, Kuroda's term is coming to an end (although he will probably be reappointed), inflation is rising to within target, and the economy is picking up.
- > A powerful support for the US dollar for the coming year is the US tax plan. The impact that this will have on the growth/inflation dynamic has the ability to push the Fed to a more hawkish policy. That's why we continue to stick to our current preference for the US dollar at the expense of the yen.

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The sale of the fund qualifies as a private placement pursuant to section 2 of Uruguayan law 18,627. The fund must not be offered or sold to the public in Uruguay, except in circumstances which do not constitute a public offering or distribution under Uruguayan laws and regulations. The fund is not and will not be registered with the Financial Services Superintendency of the Central Bank of Uruguay. The fund corresponds to investment funds that are not investment funds regulated by Uruguayan law 16,774 dated September 27, 1996, as amended.

Additional Information for US offshore investors

The Robeco Capital Growth Funds have not been registered under the United States Investment Company Act of 1940, as amended, nor the United States Securities Act of 1933, as amended. None of the shares may be offered or sold, directly or indirectly in the United States or to any US Person. A US Person is defined as (a) an individual who is a citizen or resident of the United States for federal income tax purposes; (b) a corporation, partnership or other entity created or organized under the laws of or existing in the United States; (c) an estate or trust the income of which is subject to United States federal income tax regardless of whether such income is effectively connected with a United States trade or business.