CARDIF LUX VIE
BNP PARIBAS GROUP

DATE OF WRITING: JULY 3, 2019

GENERAL FUND

CARDIF LUX VIE

The main issues that made the news in 2018 continued to dominate during the early part of 2019. As we enter July, many of the issues we thought would be behind us by now remain unsolved:

- Following the G20 Summit in late June, Donald Trump and Xi Jinping agreed to resume trade talks and bury the hatchet, at least for now. We have come full circle since December, after tensions flared in May when the US President threatened China with imposing further trade sanctions and banning Huawei from the United States. China aside, Donald Trump wants to weaponise tariffs to renegotiate more favourable bilateral agreements with US trading partners. This is manifestly dampening business confidence, with a knock-on effect on global growth, since companies need visibility to commit to new investments.

- In China, although a slowdown is clearly visible in industrial sectors, the economic data is not crumbling. Moreover, the Chinese government and central bank are managing to prevent this slowdown from spreading to the rest of the economy through continued support measures.

- Under pressure from the financial markets and the growing risks of a trade war, the Federal Reserve has decided to suspend further rate hikes. Keen to anchor inflation forecasts around its 2% target, the Fed is expected to cut interest rates once or several times, perhaps starting from the next committee meeting at the end of July. The ECB, which has already relaunched its programme for the refinancing of eurozone banks on favourable terms (TLTRO III), may also decide to loosen monetary policy even further. In any case, Mario Draghi has left a rather "dovish" roadmap to which Christine Lagarde should adhere.

- Procrastination remains the order of the day among the European political class. British MPs failed to ratify the agreement negotiated by Theresa May, whose likely successor in the polls, Boris Johnson, could lead Britain towards a "hard brexit" at the end of October. Moreover, although traditional parties fared quite well in the European elections, EU leaders seem unable to find a compromise likely to win public support. The difficulty in allocating the EU's top jobs is the most striking recent example.

In short, there were few tangible changes during the first half. Indeed, the climate looks set to remain hazy over the coming months, especially as the 2020 presidential election campaign is now under way in the US.

In the United States, during the second half, consumption, the main driver of US growth, is expected to remain resilient, stoked by a robust labour market (with unemployment at 3.6% and solid job creation) as well as a positive wealth effect. In addition, financing conditions are easing both for the real estate sector and corporate refinancing. US GDP growth is expected to remain close to 2%, the Fed's monetary policy dispelling fears of a recession in the months ahead.

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In the eurozone, household demand followed more or less the same trend, buoyed by the fall in unemployment to 7.5%, its lowest level since July 2008. Conversely, weak global trade is weighing on exporting economies, in particular Italy and Germany, whose manufacturing indicators still paint a gloomy picture. Ultimately, thanks to the central bank continuous support, although growth is expected to contract sharply in 2019 compared with 2018, it should not dip below potential growth.

As long as there is no protectionist backlash from the US, the Chinese economy should have a soft landing, with growth expected to remain above 6% in 2019. Indeed, China's growth has become more domestic-focused, as shown by the fact that the contribution to real GDP from domestic consumption has risen from 35% to 62% over the last 15 years. Concerns over debt, while justified, are mitigated by the high level of Chinese savings and close supervision by the monetary authorities.

Other regions will be dependent on this ability of the Chinese economy to counter the negative effects of an uncertain trading environment, as well as fluctuations in the price of the main commodities, especially oil. Oil prices should be propped up by the extension of OPEC+ (including Russia) agreements to cut production and tensions in the Persian Gulf. At the same time, fears surrounding global growth and significant shale oil production in the US are tending to push prices down.

Since the steep retreat of the financial markets at the end of last year, all risky asset classes have rebounded sharply, mainly as a result of the change in tone from central banks, particularly the Fed. Stock markets have therefore regained virtually all the performance lost in 2018. In more detail, global indices, excluding dividends, were dominated by the S&P 500, which was up more than 17%. Meanwhile, European markets rose 14% to 17%, followed by the MSCI EM and Topix with gains of 9.2% and 3.8% respectively. From a sector point of view, technology, industrial, luxury, beverage and food stocks had the highest profile in Europe. The most defensive sectors (health and telecommunications) and stocks with few long-term prospects or considered too risky (banking, automotive, oil, etc.) brought up the rear. However, this does not always reflect companies' profit forecasts for 2019 and 2020, let alone their relative cost.

Bond markets were dominated by the search for yield, fuelled by the sharp decline in long-term risk-free rates. The German 10-year Bund is now in negative territory, falling to a historic low of -0.33% at the end of June. Ironically, this is close to the Eonia, the reference rate for money market investments. In other EU countries, 10-year yields have also plummeted: French treasury bills have shed more than 70 basis points (bps) to -0.01%, while in Italy, the 10-year yield fell 64 bps to 2.10% despite fears of budgetary slippage. The fall in European yields follows that of US yields. It is further amplified by the influx of liquidity from institutional investors, with the ECB now holding more than 30% of eurozone government bonds.

In this environment, the relative attractiveness of credit securities led to a sharp tightening of spreads, with an outperformance of the riskiest segments, notably high yield and subordinated securities.

In the General Fund, we wanted to begin the year with slight overexposure to equity markets and to trim our positions as the rally continued, ending the six months with beta just below 9%. In fixed income, we kept our overall rate sensitivity close to 4.5 by investing net inflows and maturing investments in the primary credit market, which still offered significant issue premiums relative to absolute yield levels. We also took advantage of the flattening of the yield curve to resume purchases of floating rate securities.

In unlisted securities, we invested in infrastructure and private equity funds to maintain our exposure to these asset classes. By contrast, the weighting of real estate has edged down slightly, and we are currently looking at opportunities in the hotel segment to reinvest in this asset class.

Over the coming months, our investment strategy will continue to focus on recurring investments in the primary market for investment-grade bonds, so as to maintain a duration close to the current level. Any significant upturn in risk-free yields will be used to increase our rate sensitivity. We will also take advantage of the yield curve and market expectations that it will remain at very low or even negative levels to raise our exposure to floating rate securities.

Given the strong growth since the beginning of the year, we are maintaining a neutral position in equities. Indeed, while they may be considered slightly overvalued, they are clearly more attractive than the bond markets. The same is true of other risky asset classes, which should continue to receive significant investor support while fixed income investments remain this disadvantageous.

François LUCCHINI
Director of Asset Management

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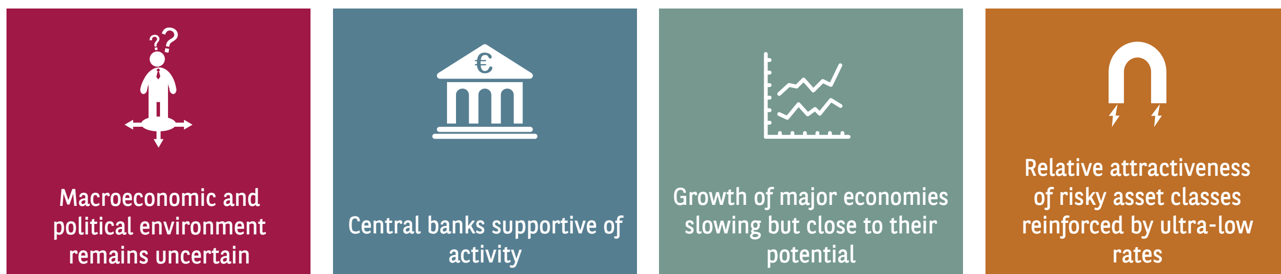
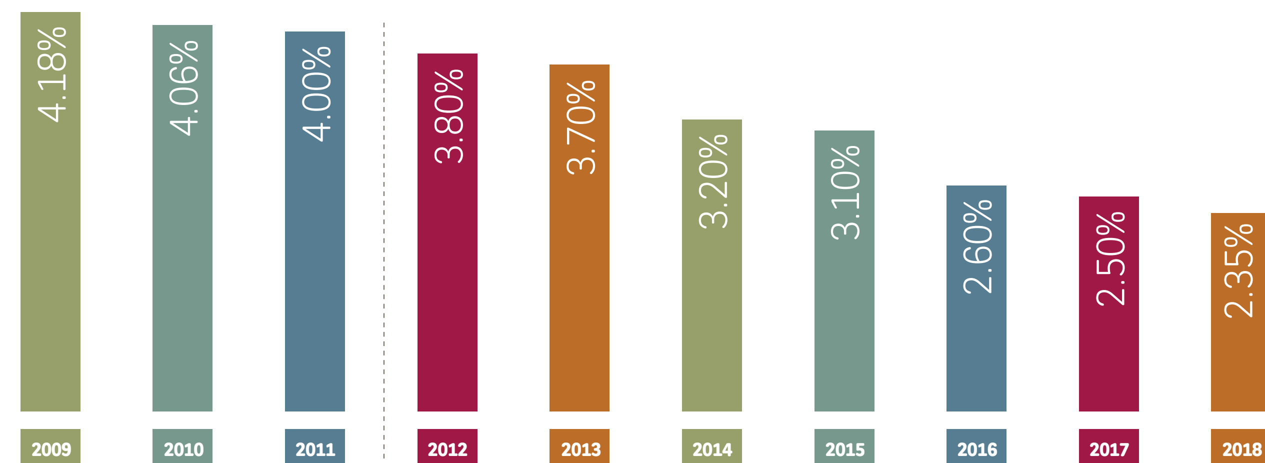
KEY POINTS TO REMEMBER



HISTORY OF THE GENERAL FUND'S GROSS RETURNS[1]



1- The performances reported up to the end of 2011 relate to the General Fund offered by Cardif Lux International (part of BNP Paribas Cardif assets). Since 2012 the General Fund has been under the direct management of Cardif Lux Vie. Details of past returns provide no guarantee or limitation of future returns. Returns do not take account of the management costs for investment instruments.

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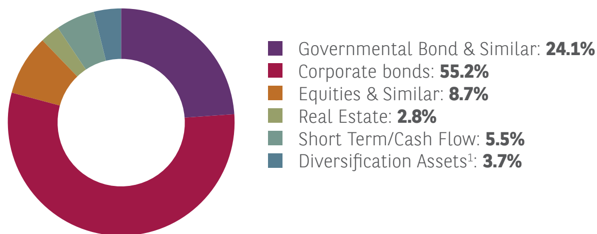
MANAGEMENT OF THE CARDIF LUX VIE'S GENERAL FUND AS AT 30/06/2019

Capitalisation of the General Fund in stock market value: 9.5 billion EUR.

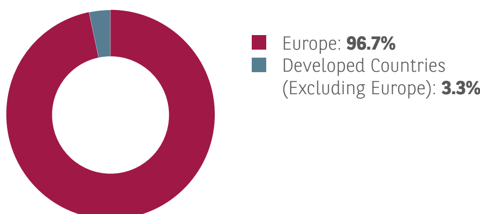
COMPOSITION OF THE CARDIF LUX VIE'S GENERAL FUND



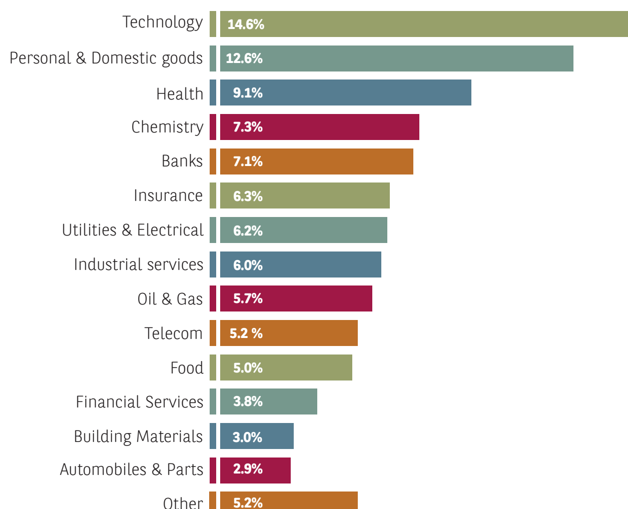
COMPOSITION OF THE EQUITIES COMPARTMENT

Share risk exposure around 9% (beta).

EQUITIES COMPARTMENT DETAIL BY GEOGRAPHIC ZONE



EQUITIES COMPARTMENT DETAIL BY SECTOR



COMPOSITION OF THE BOND COMPARTMENT

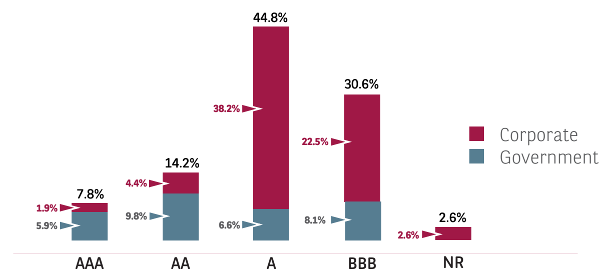
The global sensitivity to the rates of our portfolio is close to 4.6.

BOND COMPARTMENT DETAIL BY RATING

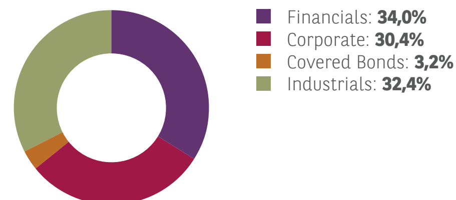
The bond portfolio has an excellent quality rating with an average rating of "A".

Rating[3] of the Government State Bonds in portfolio at 30.06.2019:

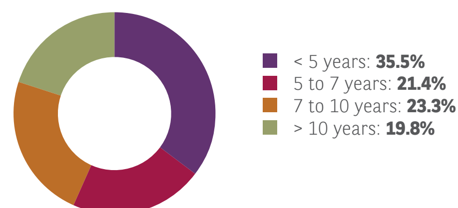
AAA: Luxembourg, Germany, Netherlands and European agencies
AA: Finland, France, Belgium and Austria
A: Slovakia, Spain, Poland, Ireland and Czech Republic
BBB: Italy and Mexico



BOND COMPARTMENT DETAIL BY ISSUERS



REPAYMENT SCHEDULE OF THE BOND COMPARTMENT



1- Emerging debt, high yield and alternative Funds.
2- Median rating of the 3 agencies Standard & Poor's, Fitch and Moody's.

CARDIF LUX VIE Société Anonyme | Siège social : 23-25 avenue de la Porte-Neuve - L-2227 Luxembourg | Adresse postale : B.P. 691 - L-2016 Luxembourg
TVA : LU163 196 59 | RCS Luxembourg N° B47240 | Tél. : +352 26 214 - 1 | Fax : +352 26 214 - 9371 | info@cardifluxvie.lu | www.cardifluxvie.lu

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