

# ASSET ALLOCATION MONTHLY

BNPP AM – Multi Asset, Quantitative and Solutions (MAQS)



## LESS DOWNSIDE RISK, BUT DON'T CHASE MARKETS

### KEY THEMES & MACRO ENVIRONMENT

- **Less fragile goldilocks** – with economic data bouncing back, central banks remaining accommodative and US-China trade tensions stabilising, goldilocks conditions are firming up. We see the coronavirus as transient for markets.
- **Risks remain, but tails are less fat** – we still see the two main risks as a slowdown or a reflationary environment, but the probabilities are now lower.
- **Short term risk/reward is unattractive** – we don't want to chase markets. Our market dynamic toolbox signals vulnerabilities in the near term.

### ASSET ALLOCATION: ASSET VIEWS

- **Equities: waiting to buy the dip** – our base case remains supportive but short-term risk/reward is unattractive. The latest earnings reports will be key.
- **Goldilocks trades: long emerging market USD debt and EMU REITs** – we continue to like carry assets, supported by the prevailing goldilocks conditions.
- **Rates: short core EUR and long US breakeven inflation** – we still see fixed income markets as rich and reflation as the big risk.
- **FX: long USD and long JPY** – we see an asymmetry in the USD outlook stemming from our risk scenarios. The JPY looks cheap and is a risk-off hedge.
- **Long gold** – we see gold as supported in the current situation where central bank policy remains loose, but also see it performing in our main risk scenarios.
- **De-globalisation trades** – we are long CAC/DAX and long USD/CNY as we position ourselves for our strategically bearish view on de-globalisation.

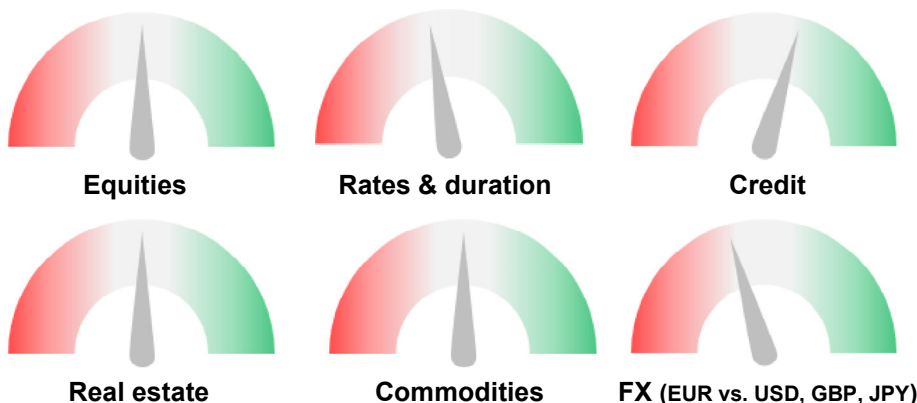
### ASSET ALLOCATION: PORTFOLIO CORNER

- **Risk utilisation** – Having taken profits on our equity overweight, the active risk in our portfolios is currently modest, in line with our 'buy the equity dip' strategy.
- **Factor exposures from core views** – given the offsetting factor profiles of some trades and as we are neutral equities, our factor exposures are muted.
- **Specific/tactical trades** – we have implemented four trades outside of our MFA portfolio optimiser; these help diversify our portfolios.

**Maximilian MOLDASCHL**  
Senior Multi-Asset Strategist, MAQS  
[maximilian.moldaschl@bnpparibas.com](mailto:maximilian.moldaschl@bnpparibas.com)  
+44 20 7063 7247

**Guillermo FELICES**  
Head of Research and Strategy, MAQS  
[guillermo.felices@bnpparibas.com](mailto:guillermo.felices@bnpparibas.com)  
+44 20 7063 7196

#### Core asset class views\*



#### Risk utilisation\*\*



\* The core asset class views dashboard reflects the key views of the Investment Committee of the Multi-Asset team at MAQS. Other specific/tactical trades may be implemented in addition and are listed at the end of this publication. \*\* Risk utilisation/active risk is a measure of the tracking error (as a % of maximum tracking error) of an unconstrained theoretical portfolio, derived from core asset class views and from additional specific/tactical trades.



**BNP PARIBAS**  
**ASSET MANAGEMENT**

The asset manager  
for a changing  
world

## MARKET REVIEW

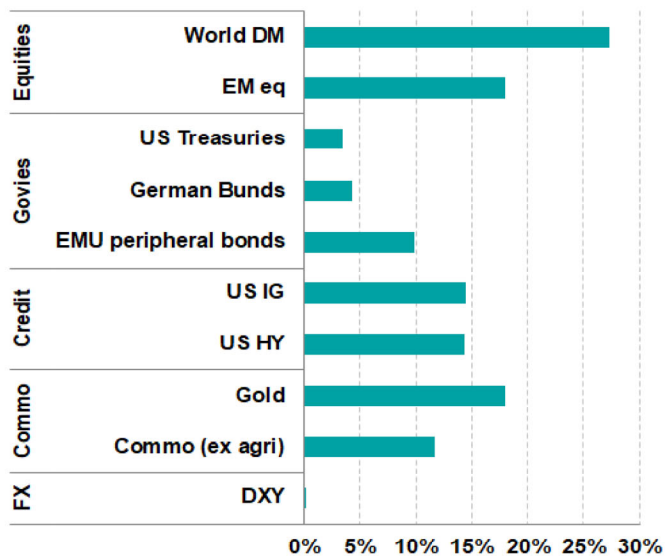
### 2019

Despite investor scepticism, 2019 was a bull market for every asset class (Figure 1). Indeed, assets benefited from the strongly dovish stance of the main central banks, starting with the 'pivot' in the US Federal Reserve's stance in January and the ECB's decision to resume quantitative easing (QE).

The first half of 2019 was characterised by a rally in government bonds and a flattening of the US treasury curve. This reversed in August, with yields falling to all-time lows in a number of countries. From the summer onwards, recession fears faded. This led to a pro-cyclical rotation in assets, which boosted equities especially.

The US-China trade dispute was a key factor for most of 2019, but tensions de-escalated in December. In addition, uncertainty over UK politics declined after the Tory party victory in December. The year ended on a high note for risky assets as macroeconomic data in the US, Europe and China stabilised.

**Figure 1: 2019: bull market despite investors' fears**



Source: Bloomberg and BNPP AM, as of 31/01/2020

### January 2020

Investor sentiment remained optimistic for most of January (Figure 2), although in the latter part of the month fears over the spread of the coronavirus reversed some of the prior equity gains. Indeed, while developed equity markets climbed by 1.1%, emerging counterparties dropped by 2.5%.

During the first half of January, a further easing of US-China trade tensions supported sentiment, and on January 15, the countries signed a 'phase-one' agreement. As part of the deal, over the next two years, China will buy from the US an additional USD 80 billion of manufactured products, USD 50

billion more in energy supply, USD 35 billion worth of services and USD 32 billion in agricultural goods. The deal does not roll back existing tariffs, but the US administration dropped its reference to China as a currency manipulator.

Investors' sentiment turned negative in the second half of January as fears around the spread of the coronavirus outbreak triggered a correction in equities and a migration towards bonds. US Treasuries and German Bunds rose by 2.2% and 2.4% respectively; also EMU 'peripheral' bonds posted a positive performance (2.4%), led by a rally of BTPs on the back of regional elections outcome. Corporate US investment-grade bonds rose further (2.2%) after their late-2019 trend higher, while US high-yield steadied.

Geopolitically, tensions between US and Iran escalated at the beginning of the year, when the US air force killed Iranian general Soleimani. In response to the attack, Iran fired missiles on US-Iraqi airbases. Tensions eased after US lawmakers voted to limit president Trump's powers, favouring sanctions over a military escalation.

The risk of escalation in the Middle East and concerns around the economic implications of the coronavirus strongly affected commodity markets: oil rose initially, but prices retraced aggressively when virus fears spread. Gold kept rallying (3.8%), but the broad commodities index fell sharply by 7.8%, led by a double-digit drop of the energy sector (-14.1%).

In currency markets, after weakening in December, the US dollar recovered against the euro (1.6%) and sterling (1.1%). The pound remained in the spotlight and rallied back somewhat after the Bank of England kept rates on hold, against some expecting a cut to policy rates.

Among the other central banks, ECB President Lagarde held monetary policy steady, as expected. She acknowledged that macroeconomic data had stabilised amid signs of a moderate increase in inflation. She mentioned that the overall risk to the growth outlook had become less pronounced. Likewise, no change was announced by Fed Chairman Powell, who said that the current level of rates is appropriate to support a sustained expansion of economic activity. The People's Bank of China cut its reserve ratio for commercial lenders by 50bp, releasing USD 115 billion of liquidity into the financial system.

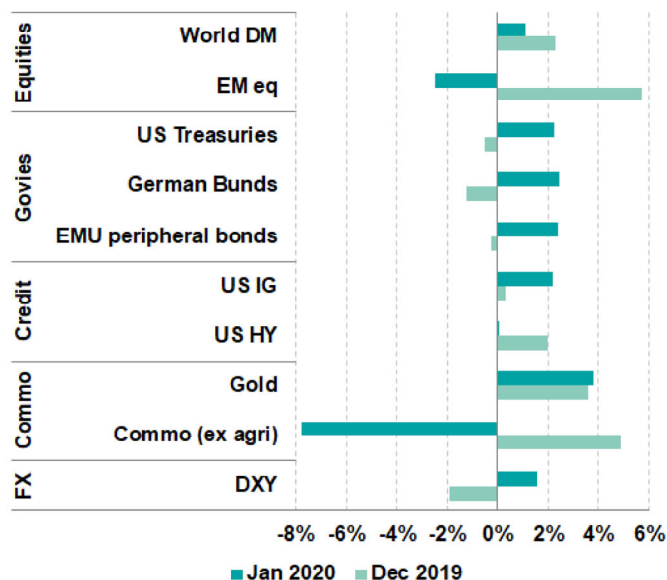
On the data side, the latest US figures showed a contraction of manufacturing activity, with the ISM index dropping to 47.2 from 48.1, but the services index edged up to 55.0 from 53.9.

In Europe, the composite PMI index disappointed: the main output index was unchanged at 50.9 (vs. the 51.2 consensus forecast). The manufacturing PMI rose from 46.3 to a strong 47.8 (vs. 46.8 consensus). In Germany, the PMI readings improved significantly: the manufacturing activity index rose from 43.7 to 45.2. There was a strong bounce in the services index from 52.9 to 54.2. The French economy was affected by

strikes: the services index fell to 51.7 from 52.4, but manufacturing still expanded, inching up to 51.7 from 50.4.

In China, trade data surprised to-the-upside: export growth picked up to 7.6% YoY (vs. 2.9% c.f., from -1.3%) and import growth surging to 16.3% (vs. 9.6% c.f., from 0.3%). Industrial production grew at a better-than-expected 6.9% vs. 5.9% c.f. Q4 GDP growth was in line with expectations at 6.0% YoY.

**Figure 2: Equities keep rallying in the first month of 2020**



Source: Bloomberg and BNPP AM, as of 31/01/2020

## A LESS FRAGILE GOLDILOCKS

Regular readers will be familiar with our ‘fragile goldilocks’ base case. It underpinned our investment decisions for most of 2019. We also outlined it in our 2020 outlook ([see here](#)). This base case is predicated on a ‘not too hot and not too cold’ economic backdrop in terms of the growth/inflation mix, and thus, crucially, a world where central bank policy remains loose. Any tightening in monetary policy is far out in the future and depends on inflation rising to central bank targets and potentially overshooting those for some time.

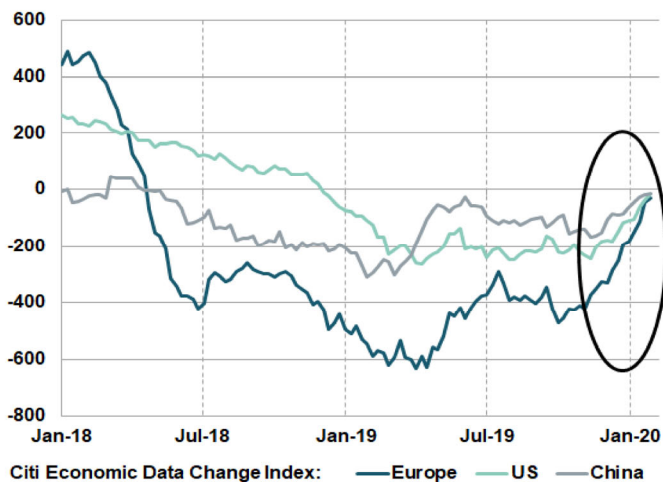
We classified this environment as fragile due to lingering tail risks with reasonable probabilities. Since late last year, and especially early in 2020, the conditions behind goldilocks have firmed up. Put differently, the probability of our base case has increased and the tail risks have diminished. We are essentially in a ‘less fragile goldilocks’ now.

Of course, markets have rallied strongly on the back of these developments (see our prior discussion and Figure 2). Below we dissect the pillars under our base case and set them against current market pricing/valuations.

### Data continues to stabilise...

After broad disappointment in key macroeconomic releases since December 2018, data has stabilised in recent months and even started improving in some areas. This stabilisation/improvement concerns a broad array of indicators and countries – as can be seen in the aggregate data indices in Figure 3.

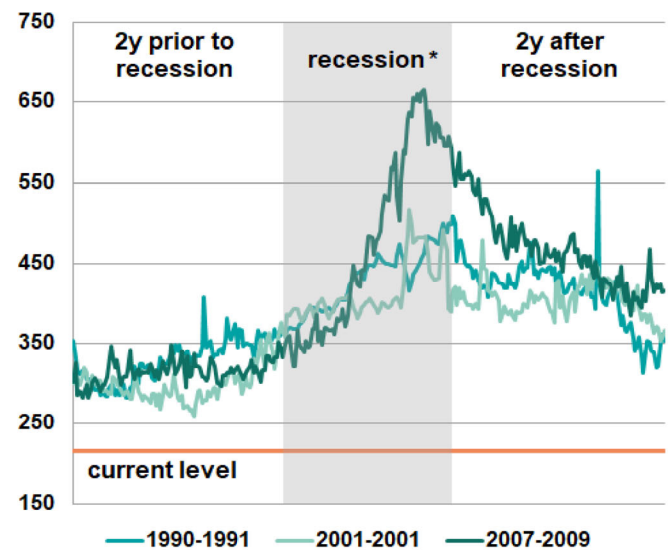
**Figure 3: Data has continued to stabilise...**



Source: Bloomberg and BNPP AM, as of 31/01/2020

In the US, domestic data is upbeat. As we outlined in prior months, two key components of the economy – the labour market and the consumer – are solid. They are not showing any dynamics similar to those seen in other pre-recessionary episodes. In fact, consumer confidence is near its cyclical highs, while initial jobless claims are near their lows (Figure 4).

**Figure 4: ...and as we have argued, especially US labour markets are solid (initial jobless claims around recessions)**

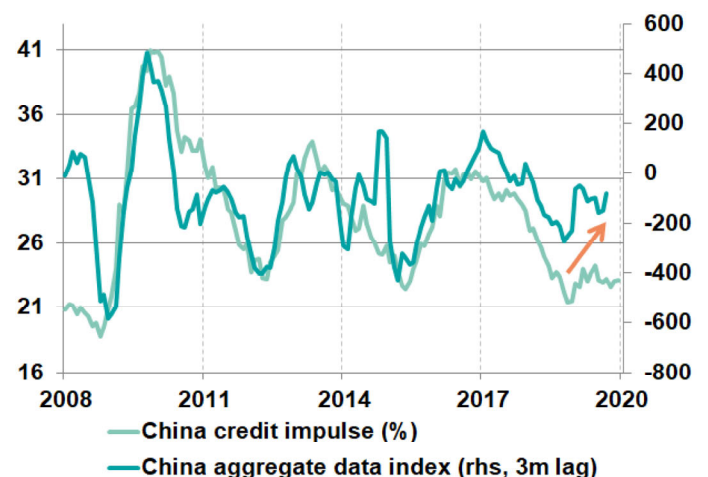


Source: Bloomberg and BNPP AM, as of 31/01/2020

Elsewhere, the Chinese economy is also showing signs of green shoots (Figure 5). See for example the upside surprises in the recently reported retail sales and industrial production data, as well as a further uptick in commodity trade. We see this as an early feed-through from policy-easing in 2019. In our base case we see the coronavirus effects as transient in the medium term.

In the meantime, the US and China have signed a ‘phase 1’ trade deal, which has added to the supportive backdrop. This is a key positive compared to being last year’s main investor concern. This has allowed data to stabilise in manufacturing economies such as Germany as well (see below discussion and Figure 7).

**Figure 5: China economy helped from 2019’s easing**



Source: Bloomberg and BNPP AM, as of 31/01/2020

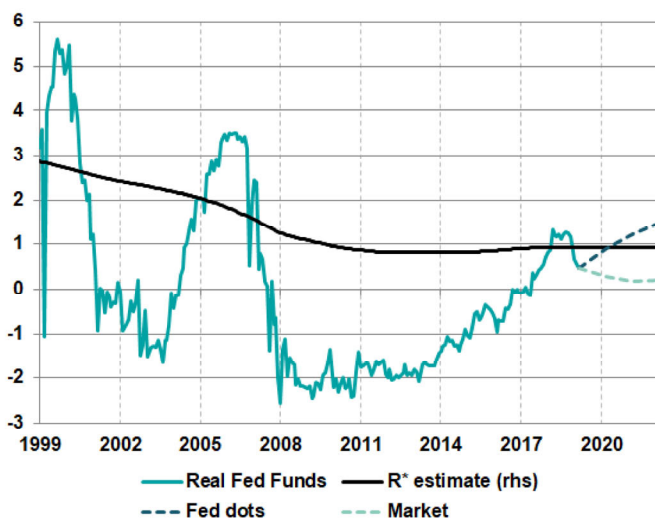


### ...while central bank policy stays loose

Adding to this broadly supportive macroeconomic backdrop, central banks have relaxed policy. The ECB restarted QE last year. New President Lagarde stayed the course at the January policy-setting meeting and kicked off a strategic policy review. On the other hand, the Fed also kept policy unchanged at its January meeting, and as we have shown before, has actually reversed the overtightening of late 2018 (Figure 6).

Overall, we believe that major central banks are unlikely to reverse their easing stances anytime soon. Recent 'noises' from policymakers confirm this. As such, 2020 should be a year of accommodative monetary policy – an important ingredient for a goldilocks environment and the associated market dynamics.

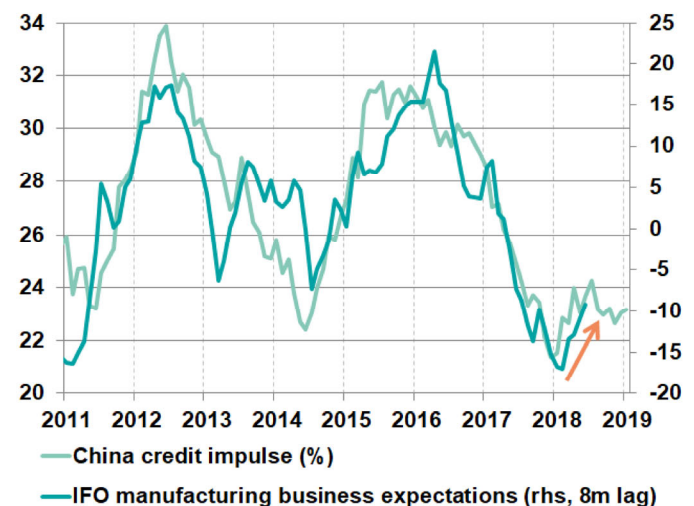
**Figure 6: Fed policy remains accommodative...**



Source: Bloomberg and BNPP AM, as of 31/01/2020

In China, targeted easing continues. While not comparable to earlier strong easing cycles, the sum of the various measures is still considerable. We believe this is an important factor in China's economic stabilisation. Importantly, the Chinese economy is big enough to make a difference to global markets. Indeed, with a lag, we often see Chinese easing efforts bolster the economies of its main trading partners. This time is no different. As shown in Figure 7, German data has improved (with an eight-month lag) as China's credit impulse rose.

**Figure 7: ...And Chinese easing is helping trading partners**



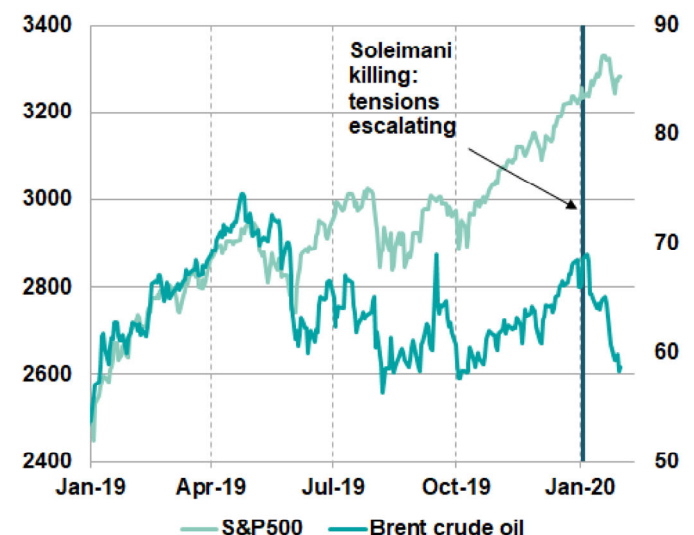
Source: Bloomberg and BNPP AM, as of 31/01/2020

### Iranian tensions just a blip

Earlier this month tensions in the Middle East flared up as the US military killed Iranian general Soleimani during a drone strike in Baghdad. Judging by news reports, concerns from investors went as far as discussing WWIII, with all eyes on how Iran would retaliate.

Oil prices rallied strongly initially, but prices fell again as the conflict cooled. Looking at equity market charts, this latest geopolitical spat is nothing more than a blip (Figure 8) – exemplifying the strength of the broader macro backdrop, and especially the strength of the monetary policy factor.

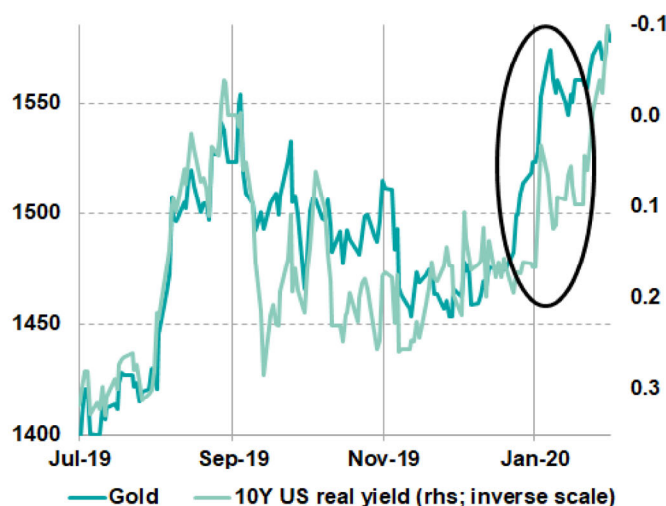
**Figure 8: Oil spike short lived, equities ignored Iran**



Source: Bloomberg and BNPP AM, as of 31/01/2020

In another corner of financial markets, gold rallied on the back of Iranian tensions. As we show in Figure 9, the gains exceeded what the yellow metal's usual driver – lower real yields – would have suggested. Gold quickly embedded a risk premium, in other words. To us, this validates gold as a portfolio diversifier. Indeed, we have been long gold since December and continue to like the asymmetric outlook for the yellow metal under both our base case and some of the risk scenarios on our radar (see discussion below).

**Figure 9: Gold rallied in excess of usual driver around Iran**

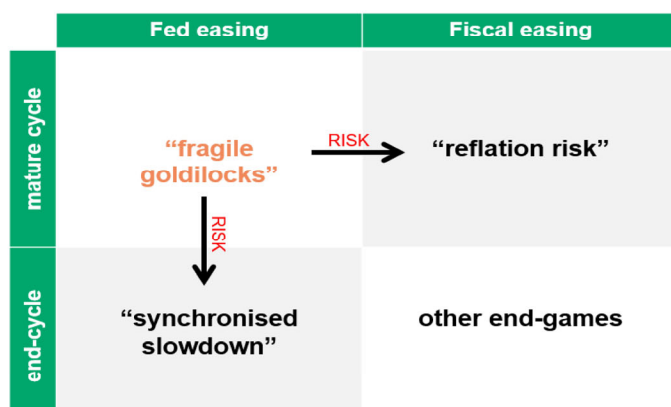


Source: Bloomberg and BNPP AM, as of 31/01/2020

### Risks remain, but tails are becoming less fat

As discussed above, several positives underpin the current environment. That is not to say that there are no risks lurking around the corner. While we feel the probabilities of these risks are actually decreasing, we see two main possible shocks to the status quo – a slowdown and a reflationary environment. Regular readers will be familiar with our matrix in Figure 10. On this basis, we are monitoring incoming cyclical data, inflation-related series and central bank actions closely.

**Figure 10: Key risk scenarios**



Source: BNPP AM, as of 31/01/2020

One asset we find interesting in both our base case and in some risk scenarios is gold. Given its limited supply and zero yield, gold should be supported in the status quo where central banks are still operating QE programmes and yields are negative (Figure 11).

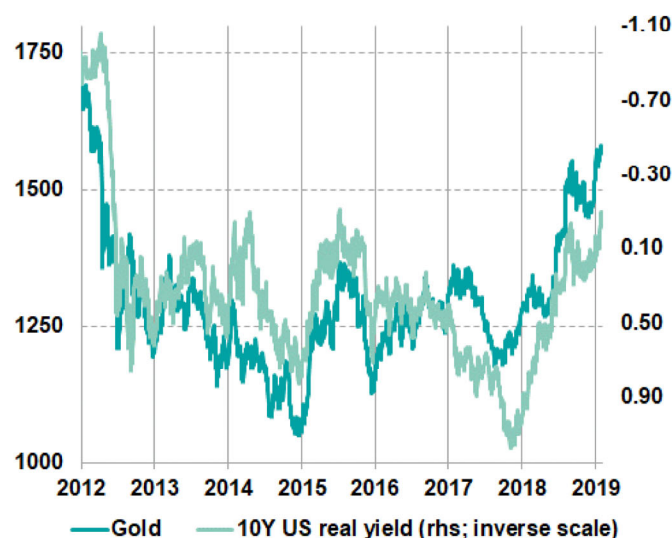
Should the growth backdrop worsen, gold could benefit from its haven characteristics. Furthermore, in our slowdown scenario, major central banks are likely to ease policy further, which would debase fiat currencies. We see this as a continuation of the current paradigm of ‘monetary activism’ that supports the yellow metal.

In addition, given that it is a real asset, an inflationary shock would be gold-supportive. Of course, if growth is supportive, higher real rates may mitigate some of the upside for gold in such a scenario.

A variant of the inflationary shock that is likely to be more supportive of gold is one where the policy end-games involve the monetary financing of fiscal deficits. This would most likely unlock inflation expectations that may eventually mean a loss of value for major currencies. Gold would benefit.

Put differently, the yellow metal has asymmetric drivers, and we see gold as an attractive portfolio diversifier as a result.

**Figure 11: Gold supported by lower real yields**



Source: Bloomberg and BNPP AM, as of 31/01/2020

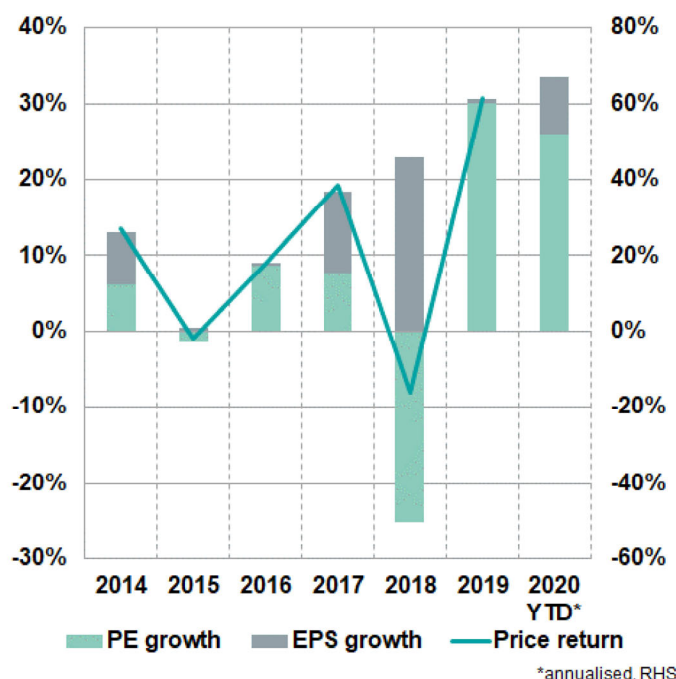
## RISK/REWARD UNATTRACTIVE FOR NOW

On one hand, we have a supportive goldilocks environment and risks with diminishing probabilities. This makes us upbeat on the broad outlook for coming months.

On the other hand, markets have rallied sharply in 2019, and in recent weeks, equities in particular have continued their march higher. Some of the positives are surely in the price, so the risk/reward at current valuations does not look too attractive. Indeed, the forecast equity returns in our base case are in the low single digits, and not worth chasing aggressively.

In fact, looking at the split in the sources of equity returns between earnings and P/E, multiple expansion was the only game in town in 2019, and again in January (Figure 12).

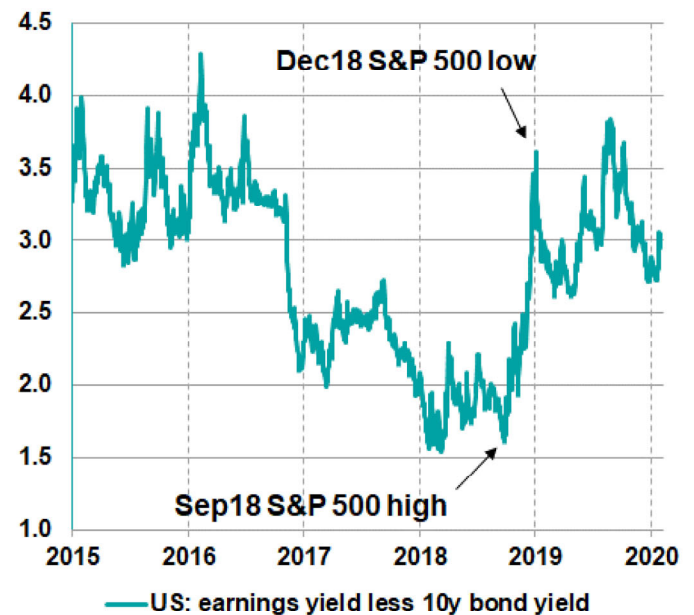
**Figure 12: It has been about multiple expansion**



Source: Bloomberg and BNPP AM, as of 31/01/2020

Outright valuation metrics are becoming richer. However, relative to other asset classes, equities are not in bubble territory by any means. In Figure 13, we compare earnings yields and bond yields. This simple measure of the equity risk premia (the lower the spread, the richer equities) should not block medium-term gains if the market environment remains this positive.

**Figure 13: But equity markets are not particularly stretched compared to bonds**



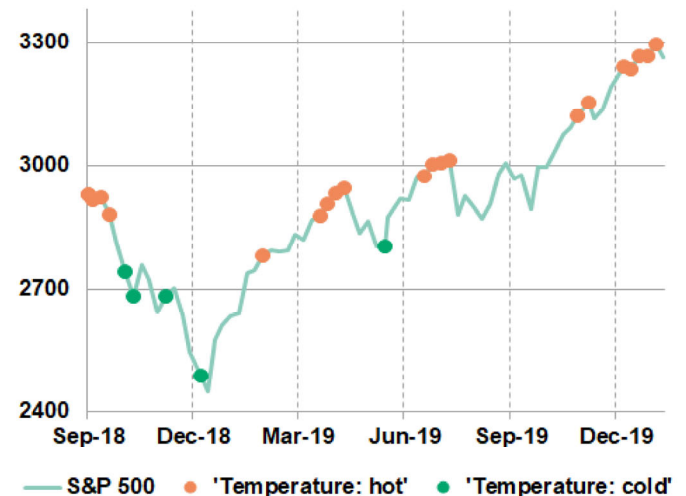
Source: Bloomberg and BNPP AM, as of 31/01/2020

## Proprietary 'Market Dynamic' indicators are cautious

We are more worried about the short term. Here, in the last weeks, our proprietary 'market dynamics' tool box – consisting of 'market technicals' and 'market temperature' signals – have suggested that there is a risk of a pullback in the short run.

For example, in our 'market temperature' pillar, positioning and sentiment inputs were as stretched as they were before equity market corrections in 2019. As a result, the current equity 'market temperature' is hot (Figure 14), dampening risk/reward attractiveness in the short term. In this light, we are watching the equity market correction in recent days closely.

**Figure 14: Our market temperature signals have turned red**



Source: BNPP AM, as of 31/01/2020

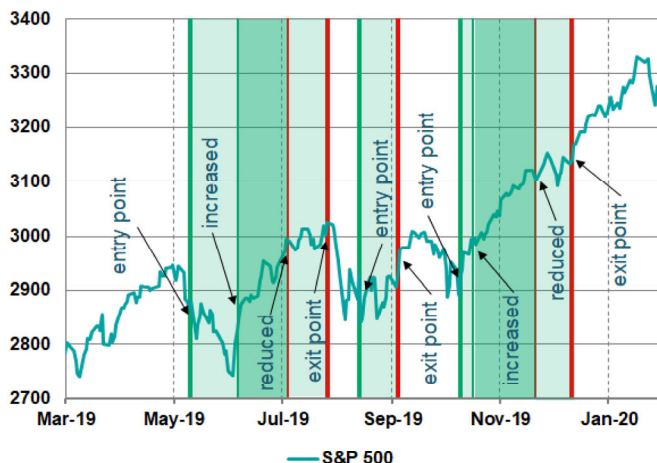
### Waiting to buy dips...

As in 2019, our modus operandi remains 'buy the dip', supported by goldilocks conditions. Indeed, this nimble approach worked well last year (Figure 15), although admittedly, with the benefit of hindsight, we neutralised our overweight too early in December.

Overall, we do not want to chase risky assets aggressively. This is reflected in the fact that our portfolio risk-taking is moderate (see below discussion and Figure 22).

We are watching the very recent equity correction closely.

**Figure 15: Waiting to buy a dip**

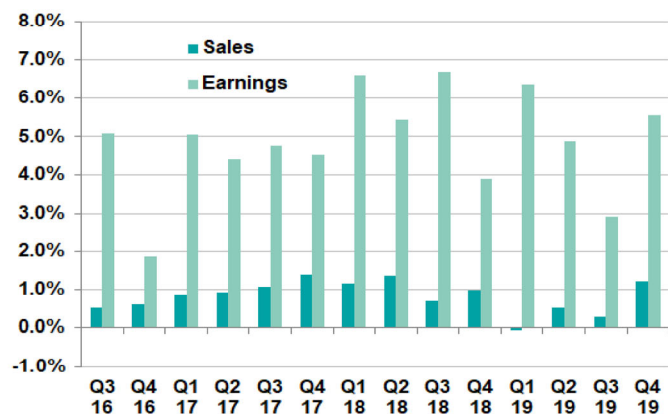


Source: Bloomberg and BNPP AM, as of 31/01/2020

### ...while monitoring earnings

Given the strong multiple expansion of recent months, we think all eyes will be on earnings delivery in 2020. So far, the Q4 2019 earnings reporting seasons has been supportive: 45% of US companies have reported and shown solid surprises on both earnings and sales (Figure 16). How strongly earnings will come through will be a key determinant for 2020 equity returns, and thus it is one of the main elements on our radar.

**Figure 16: Q419 earnings seasons: surprising to the upside**



Source: Bloomberg and BNPP AM, as of 31/01/2020



## ASSET ALLOCATION: ASSET VIEWS

Here we detail our current views across asset classes, and the views stemming from major macro/market themes. Broadly speaking, our modus operandi continues to be nimble and we continue to see merit in diversifying our asset allocation.

A detailed discussion of the portfolio considerations and specific trade implementation around these views can be found further below.

### Equities: waiting to buy the dip

As discussed above, our 'less fragile goldilocks' base case still supports risky assets such as equities. However, January has already seen strong returns fuelled solely by multiple expansion. In addition, our proprietary market dynamics indicators were signalling caution. So, we were not willing to chase equities higher from all-time records.

Instead, having moved to a neutral equity view in December, we are watching for dips to take long positions in 'delta one' space. Regular readers will be familiar with the success of such a strategy in 2019 (see Figure 15), where our market dynamics toolbox was also helpful in timing corrections.

Note that in some of the more flexible multi-asset portfolios, we bought NASDAQ puts in December to position ourselves for a short-term dip. We have since converted these into put spread structures.

### Goldilocks trades: long EM HC debt and EMU REITs

We still expect the factors behind our 'fragile goldilocks' base case, especially continued central bank easing, to prolong the search for yield and to allow carry strategies to perform. We are still looking for attractive entry points in high-carry assets.

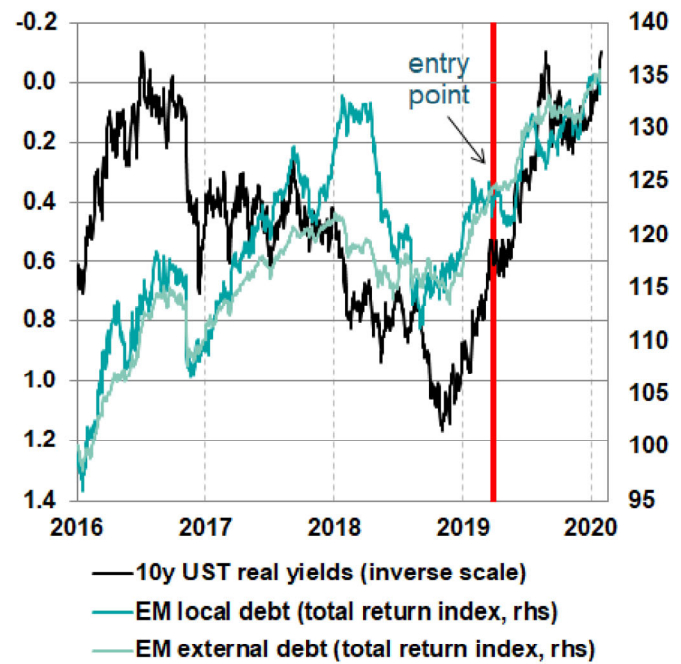
In this light, we are overweight emerging market hard currency debt. We see three positives for this trade when global growth is moderate, as in our 'less fragile goldilocks' base case.

First, EM debt does well in times of central bank easing and stable or falling real yields (Figure 17).

Second, it is one of the few liquid fixed income asset classes that yields close to 5% in USD terms.

Finally, EM spreads tend to compress when Chinese policy is being eased, which is the case currently. Here, we note that most of the strong returns of 2019 were due to the duration component, which was in turn fuelled by the rally in US Treasuries. EM spreads moved little in comparison, and only recently began to compress as Chinese data has started to stabilise.

Figure 17: 'Goldilocks' & lower real yields support EM debt



Source: Bloomberg and BNPP AM, as of 31/01/2020

Real estate investment trusts (REITs) are another market that should be supported by investors grabbing yield.

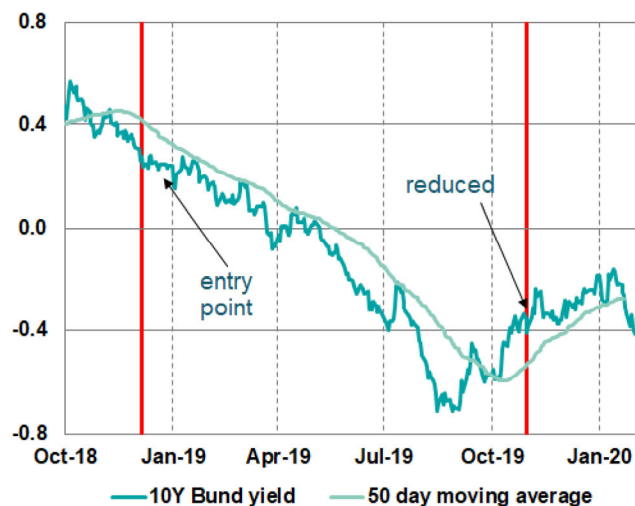
We added a long eurozone REITs position in late 2019. The main rationale is that prices are close to their five-year lows relative to net asset value, that REITs offer an attractive yield, and being a real asset, REITs have defensive characteristics, which are helpful in the case of a downturn or higher inflation.

Note that we have implemented this view as a relative value trade against large-cap equities and core bond markets. This ensures that the exposures of this trade do not significantly counteract our convictions in core asset classes at any point.

### Rates: short core EUR and long US BE inflation

We have been underweight core EMU duration for some time, and have started to see a major inflection point forming in key government bond yields (Figure 18).

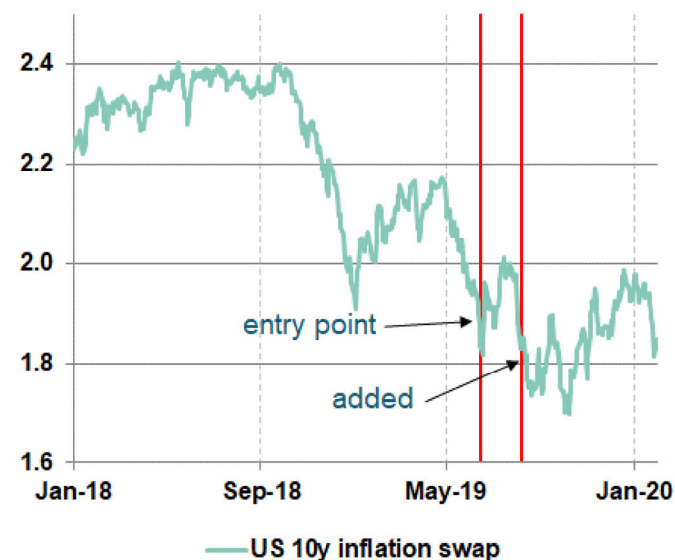
We still see fixed income markets as rich across the board. In particular, the risk from a sustained move to reflation remains large. Having seen muted inflation for decades, bond investors generally see the risk of higher inflation as low. To us, this actually makes the risk/reward for underweights in core government bond markets attractive in the medium to long term.

**Figure 18: Bund yields show signs of an inflection point**

Source: Bloomberg and BNPP AM, as of 31/01/2020

In a similar vein, together with our duration underweight in EMU bonds, we are long US breakeven inflation. This trade originated from a valuation perspective, but it is also a viable hedge to deflation.

Indeed, in recent weeks, this trade did well as data stabilised and the cycle seemingly firmed up, although recently gave up some of the gains again as the coronavirus fears spread (Figure 19).

**Figure 19: Signs of deflation in 10y US breakevens**

Source: Bloomberg and BNPP AM, as of 31/01/2020

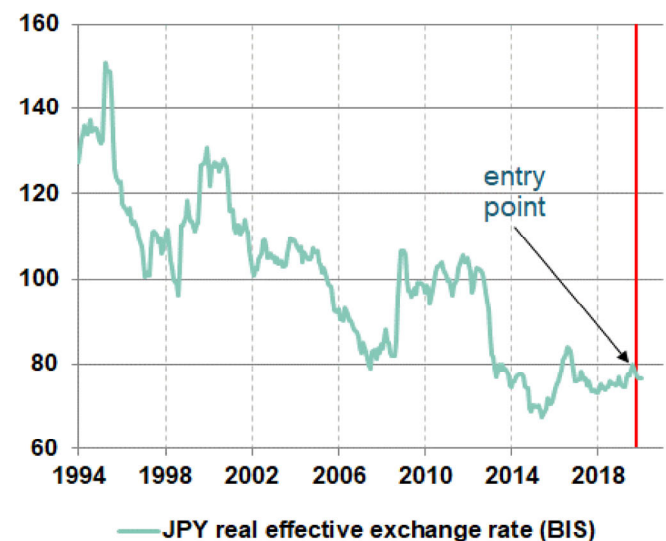
## Currencies: long USD & long JPY

We currently have several active views in FX markets.

In December, we went long the USD versus a basket of 50% EUR and 50% GBP. The rationale is a combination of a strong signal from our dynamic technical analysis and our fundamental views. We see an asymmetry in the outlook for the greenback: limited moves in our base case, but a potential deflation environment would support the US economic cycle and as a result the USD. A long USD position could also defend portfolios in the case of an extreme risk-off event.

Elsewhere in FX, we are long JPY versus EUR. We see scope for the yen to rally in a risk-off market shock, especially given the currency's cheapness (Figure 20). Put differently, with the Bank of Japan already near the absolute lower policy bound, the yen would benefit from its haven characteristics and from a recessionary environment where other central banks would ease rates and thus interest rate differentials would support the yen. The EUR short also acts a hedge to EMU break-up risk.

Finally, we are long USD versus CNY. This trade falls under our de-globalisation theme. We will discuss it below.

**Figure 20: JPY is still a cheap currency**

Source: Bloomberg and BNPP AM, as of 31/01/2020

## Commodities: long gold

In commodities, we are long gold. Above, we already detailed the rationale behind this view. In summary:

- Gold should be supported in an environment where central bank policy is loose and debases fiat currencies – indeed, gold continues to track higher as real yields fall (see Figure 11)
- In risk-off or recession scenarios, and in an inflationary shock, gold could be an attractive asset.
- Gold is a good diversification trade.

## De-globalisation trades: long CAC/DAX and USD/CNY

Despite the US and China signing of the 'phase one' trade deal, we are strategically bearish on de-globalisation in the medium to long term. Two of our trades are specifically geared to Sino-US tensions.

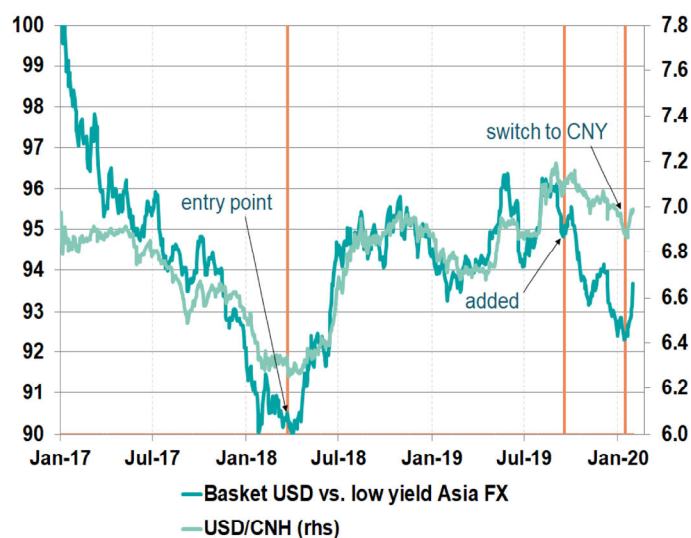
Firstly, long CAC/short DAX. We see German equities as more sensitive to a manufacturing slowdown and trade war than French stocks. Since inception, this trade has done well. We expect it to perform in bouts of escalating geopolitical tensions.

In currency markets, we were long the US dollar versus low-yielding Asian FX crosses to protect portfolios against any renewed flare-ups in geopolitical tensions. Indeed, our basket was correlated to USD/CNY and did well in periods of trade war stress (Figure 21).

After reviewing the return prospects of this trade, and comparing these to the prospects of being long USD/CNY, we see a clearer asymmetry in the CNY. This reflects our views on de-globalisation/trade tensions and China's structural issues that will affect CNY more than the currencies of its Asian counterparts.

As a result, in early January after a significant CNY rally, we switched from being long USD versus a basket of Asian currencies to being long USD versus CNY. We note that USD/CNY has been more volatile than our Asian basket over the last year or so.

**Figure 21: Switching to long USD/CNY**



Source: Bloomberg and BNPP AM, as of 31/01/2020

## ASSET ALLOCATION: PORTFOLIO CORNER

### Risk utilisation

Having taken profits on our equity overweight, the active risk in our portfolios is currently only modest at just above 50% of our target (Figure 22). This is in line with our stance of waiting to 'buy the equity dip' and having the room in portfolios to do so.

The main contributors to our current level of risk utilisation are the various currency trades discussed above.

**Figure 22: Current level of active risk\*: moderate**



\* Risk utilisation/active risk is a measure of the tracking error (as a percentage of maximum tracking error) of an unconstrained theoretical portfolio, derived from core asset class views and from additional specific/tactical trades.

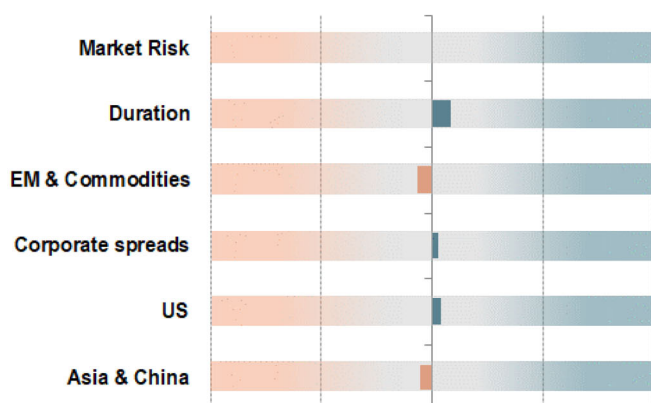
Source: BNPP AM, as of 31/01/2020

### Core views and resulting factor exposures in MFA

*We have introduced our new asset allocation portfolio optimiser – 'MFA' – which uses factor analysis to map core asset views to factor exposures across all our Multi-Asset portfolios, from the flexible to the very constrained. Please see a white paper [here](#) for details. From now, we will also communicate views from a 'factor viewpoint'.*

As with our current risk utilisation, the factor exposures of our core views is also quite limited (Figure 23), especially given the offsetting factor profiles of some trades.

**Figure 23: Current factor exposures\* from core asset views**



\* The factor exposure shown is for an unconstrained theoretical portfolio and derived from core asset class views. These factors will be projected onto individual portfolios considering constraints. Additional specific/tactical trades may be implemented and these will not be visible in the factor profile. They are listed at the end of this publication.

Source: BNPP AM, as of 31/01/2020

Our current **Market Risk** exposure is neutral given that there are no core trades in equities. The positive **Market Risk** stemming from our long in emerging market hard currency debt is almost exactly offset by the negative **Market Risk** exposure of our long USD and long JPY trades. **Duration** is slightly overweight, stemming from our long in EM external debt, but offset by our duration underweight via core EMU bonds.

The other factor exposures are marginal, because some trades offset each other. For example, the long CAC/short DAX in equities has no dominant factor exposures as the factor loadings on the French CAC and German DAX indices are near identical. Equally, we implemented our long in EMU REITs relative to equities and bonds, specifically with the aim of neutralising factor exposures.

### Specific/tactical views implemented outside of MFA

We implement some of our trades outside of our new MFA portfolio optimiser. Such trades are either tactical or specific (i.e. we do not want a trade to be factorised across the book of business) or the asset in question is out of the scope of our optimiser.

From the views discussed above, the following are non-MFA trades:

- Long USD/CNY – specific trade
- Long US breakeven inflation – tactical and specific trade
- Long gold – specific trade
- Long NASDAQ put spreads – tactical and specific trade

Note that these trades thus do not contribute to the above factor analysis and are not factorised to the broad book of business.





## OVERVIEW OF KEY VIEW CHANGES SINCE LAST PUBLICATION

The BNPP AM MAQS team took the following asset allocation decisions:

### DECEMBER:

#### CORE ASSET CLASS VIEWS:

**LONG US EQUITIES** **CLOSED** **11/12/19**

- Our market temperature and timing indicators suggest the risk of a short-term correction. With central bank policy meetings and trade tariff deadlines approaching, we closed our long US equity position and turned neutral.

**LONG USD VS. EUR/GBP** **OPENED** **18/12/19**

- The combination of our technical and fundamental signals suggests a potential deflation environment that would support the US economy and the US dollar. We took a long position in the USD. This is split 50:50 against EUR and GBP.

#### SPECIFIC/TACTICAL VIEWS:

**SHORT US EQUITIES – VIA PUT OPTIONS** **OPENED** **18/12/19**

- Market timing tools suggest a short-term vulnerability of the NASDAQ and S&P500 indices to possible corrections. We opened a short position in US equities, buying put options for flexible portfolios.

### JANUARY:

#### CORE ASSET CLASS VIEWS:

NO CHANGE

#### SPECIFIC/TACTICAL VIEWS:

**LONG USD VS. ASIAN FX BASKET** **CLOSED** **15/01/20**

**LONG USD VS. CNY** **OPENED** **15/01/20**

- Asian economies and monetary policies have begun to stabilise. This should support Asian currencies. In China, after a recent CNY rally, the earnings prospects of a long USD vs. CNY position are looking better given the de globalisation stress. We switched from long USD vs. an Asian currency basket to long USD vs. CNY.

**SHORT US EQUITIES – VIA PUT OPTIONS** **CLOSED** **15/01/20**

**SHORT US EQUITIES – VIA PUT SPREADS** **OPENED** **15/01/20**

- We re-structured the short US equity position via put options for flexible portfolios and switched to a put spread strategy.



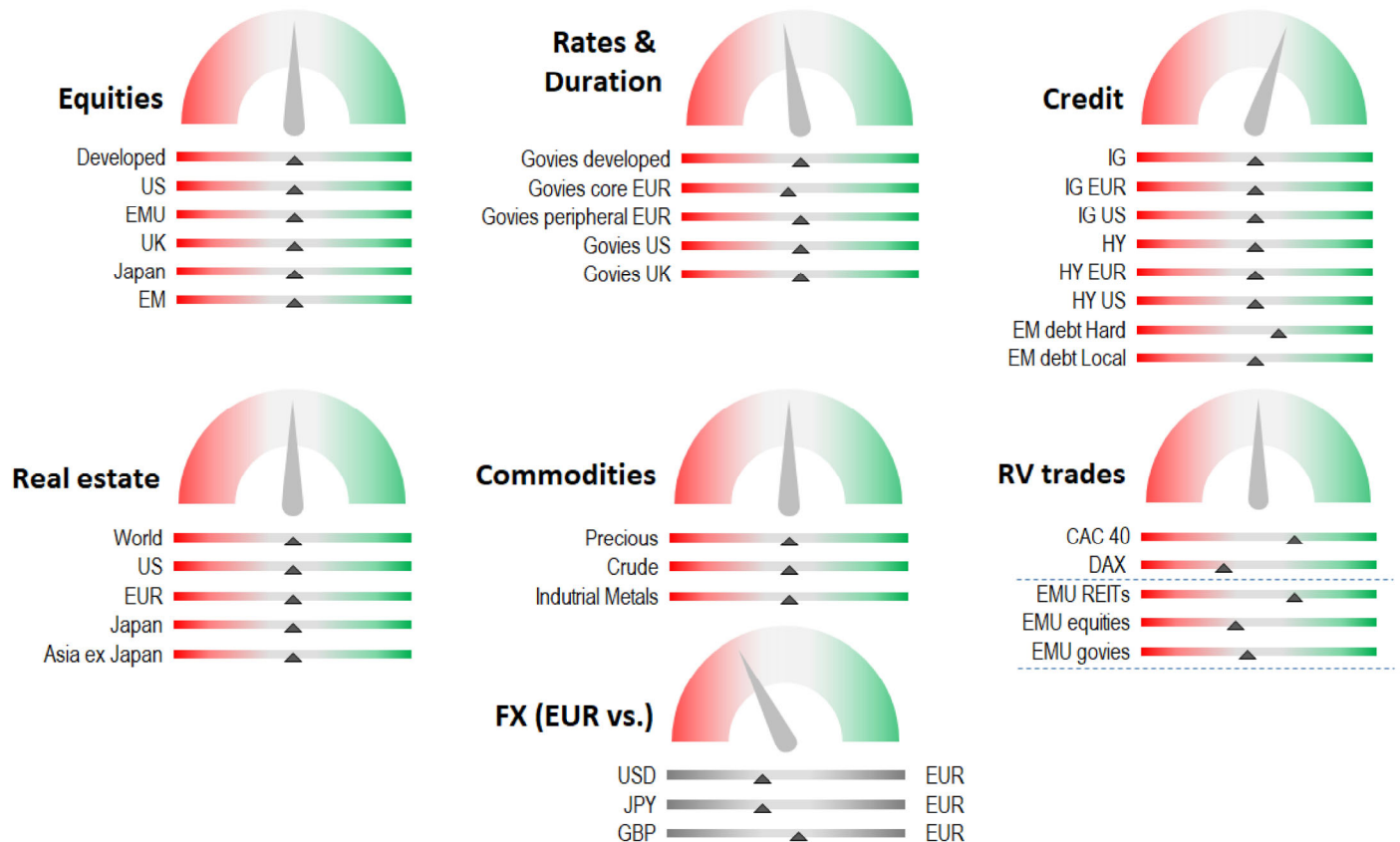
## RISK UTILISATION<sup>1</sup>

Active risk

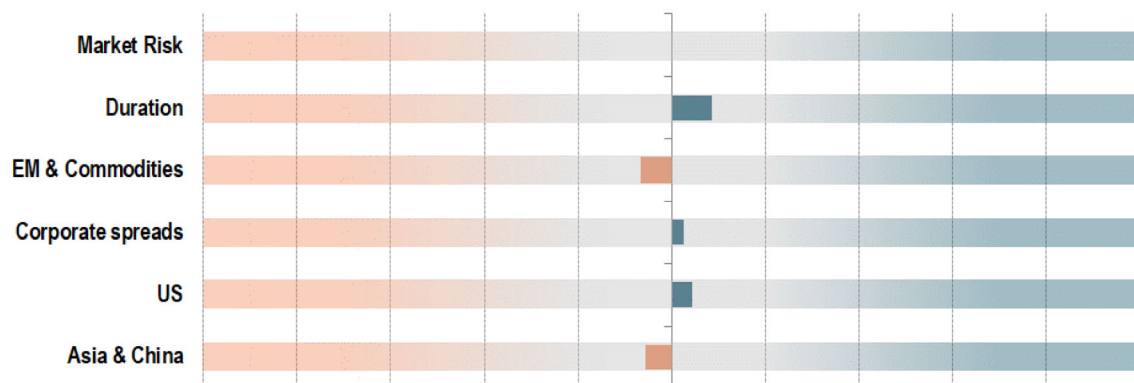


## CORE ASSET CLASS VIEWS & FACTOR EXPOSURE

Core asset class views<sup>2</sup>



Factor exposure<sup>3</sup>



<sup>1</sup> Risk utilisation/ active risk is a measure of the tracking error (as a % of maximum tracking error) of an unconstrained theoretical portfolio, derived from core asset class views and from additional specific/tactical trades.

<sup>2</sup> The core asset class views dashboard reflects the key views of the Investment Committee of the Multi-Asset team at MAQS.

<sup>3</sup> The factor exposure shown is for an unconstrained theoretical portfolio, derived from core asset class views. These factors will be projected onto individual portfolios considering constraints. Other specific/tactical trades may be implemented in addition and will not be visible in the factor profile

SPECIFIC/TACTICAL TRADES<sup>4</sup>

Trade	Asset class	Specific/Tactical
Long USD vs. CNY	FX	Specific
Long US Breakeven inflation	Rates & duration	Tactical & specific
Long gold	Commodities	Specific
Long NASDAQ put spreads	Equities	Tactical & specific

<sup>4</sup> Specific/tactical trades are implemented in addition to the core asset class views and will not be visible in the factor profiles shown elsewhere in the document.

Views expressed are those of the Investment Committee of MAQS, as of January 2020. Individual portfolio management teams outside of MAQS may hold different views and may make different investment decisions for different clients.

## DISCLAIMER

**BNP PARIBAS ASSET MANAGEMENT UK Limited, “the investment company”, is authorised and regulated by the Financial Conduct Authority. Registered in England No: 02474627, registered office: 5 Aldermanbury Square, London, England, EC2V 7BP, United Kingdom.**

This material is issued and has been prepared by the investment company. This material is produced for information purposes only and does not constitute:

1. an offer to buy nor a solicitation to sell, nor shall it form the basis of or be relied upon in connection with any contract or commitment whatsoever or
2. investment advice.

Opinions included in this material constitute the judgment of the investment company at the time specified and may be subject to change without notice. The investment company is not obliged to update or alter the information or opinions contained within this material. Investors should consult their own legal and tax advisors in respect of legal, accounting, domicile and tax advice prior to investing in the financial instrument(s) in order to make an independent determination of the suitability and consequences of an investment therein, if permitted. Please note that different types of investments, if contained within this material, involve varying degrees of risk and there can be no assurance that any specific investment may either be suitable, appropriate or profitable for an investor's investment portfolio.

Given the economic and market risks, there can be no assurance that the financial instrument(s) will achieve its/their investment objectives. Returns may be affected by, amongst other things, investment strategies or objectives of the financial instrument(s) and material market and economic conditions, including interest rates, market terms and general market conditions. The different strategies applied to the financial instruments may have a significant effect on the results portrayed in this material.

This document is directed only at person(s) who have professional experience in matters relating to investments (“relevant persons”). Any investment or investment activity to which this document relates is available only to and will be engaged in only with Professional Clients as defined in the rules of the Financial Conduct Authority. Any person who is not a relevant person should not act or rely on this document or any of its contents.

All information referred to in the present document is available on [www.bnpparibas-am.com](http://www.bnpparibas-am.com).

As at January 2020.

© BNP Paribas Asset Management UK Limited 2020