Confidence must be earned

Amundi ASSET MANAGEMENT

Asset Class Return Forecasts

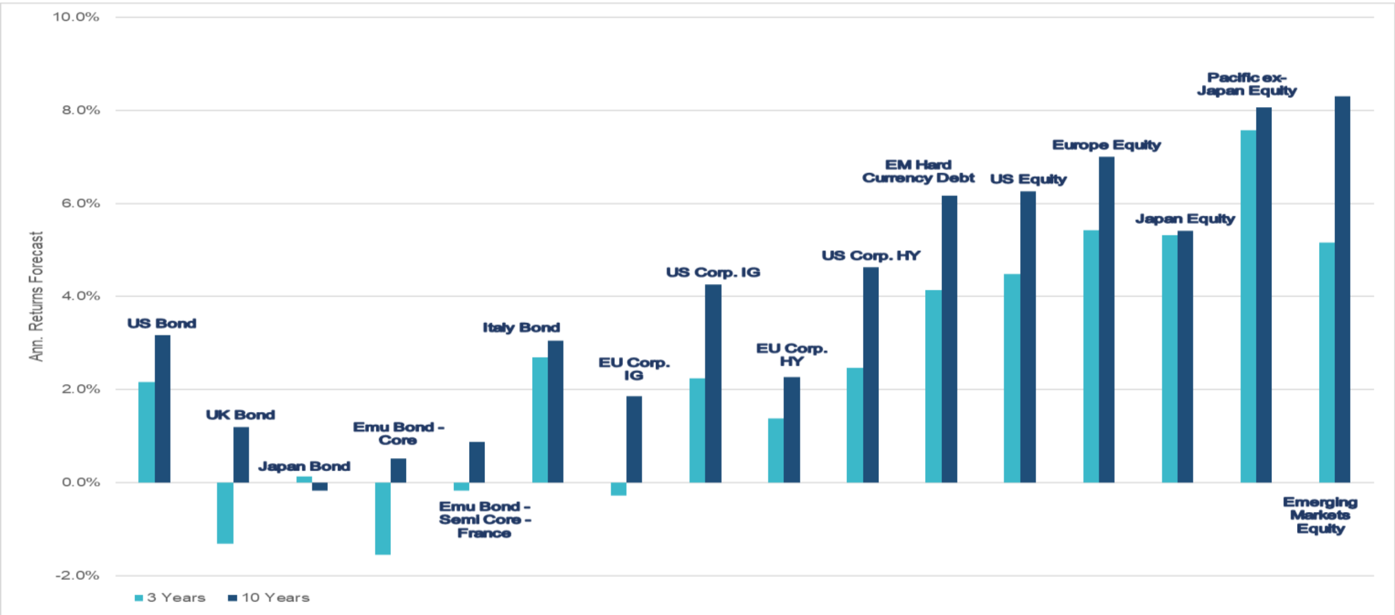
Medium and Long-Term Return Forecasts | Q4 - 2018 *Finalized in October 2018*

We stick to the view that 2018 will be the peak of the global economic cycle. 2019 will most likely be a year of deceleration albeit with still above trend growth, before a further slowdown of growth towards potential in 2020. Central banks will continue withdrawing their stimulus but at different speeds due to growing economic divergences among developed countries. With elevated and persistent uncertainties, the downside risks to our scenario have increased. Liquidity tightening as well as the dominance of politics are key factors to consider as we move towards 2019 and beyond.

As we move away from a market driven by strong and predictable liquidity to a market driven by economic and corporate fundamentals, we expect lower returns on risky assets as economic and profit growth is peaking. We now anticipate a more gradual hiking cycle by the ECB. On the other hand, the sell-off in global rates which put upward pressure on bond yields provided slightly more attractive entry points on the government bonds.

GOVERNMENT BONDS	Convergence to long-term equilibrium bond yields should materially impact government bond returns above all in the medium term horizon
CREDIT	The outlook is for moderate returns in the medium-term and an increase in the asset class volatility consistent with the late phase of the cycle
EQUITIES	Moderating returns in the medium-term. Tighter financial conditions will lead to higher risk premium with a contraction in valuation multiples.

Annualized Return Forecasts



Source: Amundi Asset Management CASM Model, Amundi Asset Management Institutional Advisory and Strategy and Economic Research Teams, Bloomberg. Data as of the 19 October 2018. Macro figures as of last release. Interest rates and spread levels updated as of the 28 September. Equity returns updated as of the 28 September based on MSCI indices. **One year forward views and fair values provided by Research team (macro, yields, spread and equity).** Forecasts for annualised returns are based upon estimates and reflect subjective judgments and assumptions. These results were achieved by means of a mathematical formula and do not reflect the effect of unforeseen economic and market factors on decision making.
The forecast returns are not necessarily indicative of future performance, which could differ substantially.

Asset Class Expected Returns

In the following table, we present our annualized return forecasts across different asset classes, calculated as the average of simulated returns, on different forward looking horizons (from 3 Years to 10 Years).

Assets in local currency	Reference Index	Duration	3 Years	5 Years	10 Years
Cash					
Euro Cash	JPCAEU3M index	0.3	-0.2%	0.2%	0.9%
US Cash	JPCAUS3M index	0.2	2.7%	2.8%	2.9%
Government Bonds					
US Bond	JPMTUS Index	6.2	2.2%	2.6%	3.2%
UK Bond	JPMTUK Index	11.8	-1.3%	-0.6%	1.2%
Japan Bond	Customized Index	8.8	0.1%	0.1%	-0.2%
Emu Bond - Core	JPMTWG index	7.5	-1.5%	-0.9%	0.5%
Emu Bond - Semi Core - France	Customized Index	8.7	-0.2%	0.0%	0.9%
Italy Bond	JPMTIT index	6.4	2.7%	2.4%	3.1%
Spain Bond	Customized Index	9.1	0.1%	0.7%	1.4%
EMU Bond All Maturity	JPMGEMUI Index	7.2	-0.2%	0.2%	1.4%
Barclays Global Treasury	BTSYTRUU Index	7.8	-0.1%	0.3%	1.1%
Credit Investment Grade					
Euro Corporate IG	ER00 index	5.1	-0.3%	0.7%	1.9%
US Corporate IG	C0A0 index	6.9	2.2%	3.3%	4.3%
Barclays Euro Aggregate	LBEATREU Index	6.8	-0.2%	0.3%	1.5%
Barclays US Aggregate	LBUSTRUU Index	6.1	2.2%	2.8%	3.5%
Barclays Global Aggregate	LEGATRUU Index	7.0	1.0%	1.4%	2.1%
Credit High Yield					
Euro Corporate HY	HE00 index	3.8	1.4%	1.8%	2.3%
US Corporate HY	H0A0 index	4.1	2.5%	4.0%	4.6%
Emerging Market Debt					
EM Hard Currency Debt	JPEGCOMP Index	6.7	4.1%	5.6%	6.2%
Convertible Bond					
Europe Index (Eur Hedged)	UCBIFX20 Index		2.0%	2.8%	3.8%
Equities					
US Equity	NDDLUS Index		4.5%	5.1%	6.3%
Europe Equity	NDDLE15 index		5.4%	5.4%	7.0%
Euro zone Equity	NDDLEMU Index		5.7%	5.6%	7.0%
UK Equity	NDDLUK Index		4.9%	4.9%	6.9%
Japan Equity	NDDLJN Index		5.3%	4.8%	5.4%
Pacific ex-Japan Equity	NDDLPXJ Index		7.6%	7.4%	8.1%
Emerging Markets Equity	NDLEEGF index		5.2%	5.6%	8.3%
World Equity	NDDLWI index		4.9%	5.2%	6.4%
AC World Equity	NDLEACWF Index		4.9%	5.3%	6.6%

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The forecast returns are not necessarily indicative of future performance, which could differ substantially.

Monetary Policy

Deceleration in global economic growth

Our macroeconomic expectations are unchanged. relative to last quarter. We stick to the view that 2018 will be the peak of the global economic cycle. As such, 2019 will most likely be a year of deceleration albeit with still above trend growth, before a further slowdown of growth towards potential in 2020. Nonetheless, with elevated and persistent uncertainties, the downside risks to our scenario have increased. Liquidity tightening as well as the dominance of politics are key factors to consider as we move towards 2019.

Central banks are continuing to withdraw their stimulus but at different speeds with growing economic divergences among developed countries.

While economic data surprises seem to have turned negative in Europe and Emerging Markets, the U.S. economy continues to surprise on the upside

United States*:* the strong economy warrants hiking monetary policy rates to at least a neutral level (3%) given (1) above trend growth (2) lax fiscal policy (3) tight labour market (4) inflation at target and (5) easy financial conditions.

Eurozone: after numerous disappointments at the beginning of the year (GDP only rose by 0.8% in H1), and because of persistent and elevated political risk, we revised downwards our projected monetary policy path for the ECB. We anticipate a 1st rate hike in H2 2019 and a more gradual hiking cycle. Beyond short term volatility, we anticipate that GDP will gradually decelerate to long term potential (1.5% or slightly below) over the next 3-4 years as the output gap is now closed and no major excess/bubble is visible. Core inflation will accelerate, but very gradually. It is far from clear that 2% core inflation will be reached in this cycle. While wages are clearly pointing upward, structural disinflationary factors are at play.

Lower interest rates in the medium terms.

In the medium term, we expect equilibrium real policy rates to remain low compared to previous economic cycles because of moderate global nominal growth (low productivity, ageing population, low inflation), while global debt is close to an all-time high.

Global Bonds

Convergence to long-term equilibrium bond yields should materially impact government bond returns above all in the medium term horizon.

The US fixed income market has revised upwards its expectations for future Fed rate hikes but the term premium remains too low. It is even negative according to the latest New-York Fed estimate.

We expect the term premium to rise when we approach the peak of the Fed tightening cycle as uncertainty will grow regarding the consequences of the monetary tightening on growth and inflation. In addition, the shrinking Fed balance sheet and the increase in treasury supply will also drive the term premium higher in the future.

In the longer-run, we therefore see the US 10-year yield approaching 3.50% on the back of a rise in the term premium to around 70 bp. The rising bond yields will negatively impact the returns of US bonds. We expect them to deliver 2% to 2.5% in the medium-term and below 3% over the next 10 years

Expectations on core Eurozone bonds increased slightly relative to Q2 due to higher bond yields and slower normalization path. The strong sell-off in global rates, which put upward pressure on Bund yields, provided a more attractive entry point on the asset class.

The rise of core EMU interest rate is expected to be very slow. In fact, the 10-year Bund (0.5% bps) is currently very far from its long-term projected level (2.4%). We expect a gradual convergence in line with the monetary policy stance.

Global Credit

Spreads are expected to widen

On EU IG and HY Bonds, we maintain our view that spreads will widen in the short and medium term. This will be partially offset by the more benign dynamic on interest rates as we anticipate a slow normalization of the monetary policy.

The US IG and HY spreads are expected to widen further (particularly the HY sector) in an environment of weaker economic and earnings growth and tighter financial conditions. Consequently, we expect a moderate return for US HY in the short to medium- term before a slow normalization of returns in the long run. The IG sector will be less negatively impacted by tighter financial conditions and will outperform HY in the short-term.

Our outlook on EM spreads continue to be that of a widening with increased volatility. Accordingly, hard currency EM bonds returns are expected to decrease in the medium-term before recovering in the long-term.

Global Equities

Moderating returns in the medium-term

As we enter the late phase of the cycle, the profit cycle will start decelerating along with the gradual economic slowdown. The profit cycle will also face several headwinds such as: higher energy costs, tariffs and tighter labour markets.

Less favorable environment for equity valuations.

Gradually increasing US rates are tightening financial conditions globally. The tighter financial conditions will lead to will lead to higher risk premium with a contraction in valuation multiples. We expect a contraction in equity valuations across regions.

Cascade Asset Simulation Model (CASM)

This long-term return forecast report intends to provide some guidance for investor expectations. The time horizon under consideration is 10 years, a period deemed to be an appropriate timeframe, during which long-term trend factors and issues can reasonably be expected to play out, and thus, market returns should accurately reflect this information. We use a Monte-Carlo methodology in order to generate the possible evolutions of different risk-factors for the time horizon considered, representing the future states of these factors under objective measures. The resulting model is then used to price the instruments in line with these factor scenarios.

In order to determine possible interest rate scenarios, we analyse the evolution of the major economic DM regions. We used a cascade-style modelling technique for simulating the different term structure, using risk factors such as the GDP cycle, inflation, real rates and slope for each of the economic regions in question..

Moving into spread-related assets (EM bonds and corporate bonds), we focus on implied volatility, quality, default and recovery rates, together with economic cycles, to estimate a forward looking path for EM bonds (hard currency), EU corporate (IG and HY) and US corporate (IG and HY).

Our framework on equity focuses on earnings growth and price earnings, as a determinant of capital gains and dividend yields, to represent the income effect; these variables are analysed with the macroeconomic pillars of the model (the economic and inflation cycle).

Our medium/long-term model, known as CASM, is updated on a quarterly basis to incorporate new starting points, our short-term outlook along with long-term trends, the significance of which is verified on an annual basis.

Our CASM model focuses on key factors, which drive this evolution over the medium to long-term; the resulting forecasts look at the comparison between current and long term readings for the key factors included in the model.

Note that these are simulated figures only and may not represent actual asset class returns. Actual returns are based on many factors, and may vary substantially from modeled ones.

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