Private Banking Investment Outlook

June 2022

ERSTE Private Banking

Private Banking Investment Outlook

Index of Contents

Private Banking Investment Outlook

Executive Summary

Dear Readers,

In Q1 2022, the euro zone economy has already suffered significantly from high inflation and the further negative effects of the Ukraine war. Consumption in particular has already been hit hard by high inflation. Industry continues to suffer from supply chain problems as well as the significant increase in energy prices. In contrast, the service sector is optimistic about the future following the end of the COVID restriction measures. Given the weak growth in 1Q, we have lowered our GDP growth forecast for 2022 to 2.8%. For 2023, we expect GDP growth of 2.6%. The rapid rise in US government bond yields led to a decline in the gold price in May. It fell by -4.9% in EUR terms. In the medium term, however, the continued negative real bond yields in the USA and Europe have a supportive effect on the gold price. The slowdown in global corporate earnings momentum this year and an expected slowdown in global economic growth have led to an increase in equity market volatility. This favors a positive development of the gold price. This situation should continue in the medium term. Geopolitical uncertainties also remain elevated. We expect the gold price to rise moderately in June.

Attractiveness of asset classes
Short-term estimates of Erste Bank (updated quarterly)

Segment	Asset Class	--	-	neutral	+	++
Bonds Investment Grade	Euro Money Market		●			
	Euro Government Bonds Investment Grade	⇨	●			
	Euro Corporate Bonds		●			
	US Corporate Bonds			●		
Bonds High Yield	Euro High Yield			●	⇦	
	US High Yield				●	
	Emerging Sovereigns Hard Currency				●	
	Emerging Corporates Hard Currency				●	
	CEE Sovereigns Local Currency			●		
	Emerging Sovereigns Local Currency				●	
Equities	Developed Markets				●	
	Emerging Markets			●	⇦	
Other	Gold			●		
	Real Estate			●		
dged in EUR	Commodities			●		
	Alternative Investments Low Vol			●		
	Alternative Investments High Vol			●		

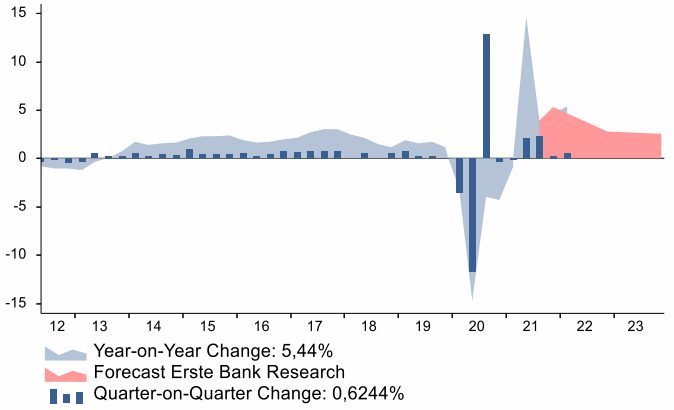
With reference to the chart „Asset Class Attractiveness": please refer to the annex for the underlying index. Forecasts are no reliable indicator for future performance.

Eurozone Economics

Overview

Eurozone Real GDP Growth Rate*

as of Q2 22

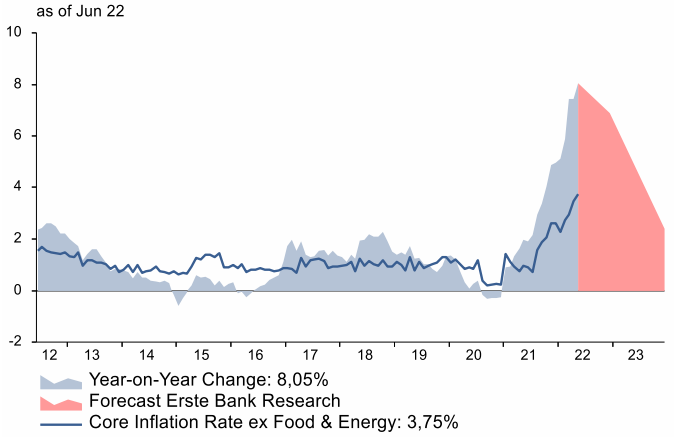


Quelle: Refinitiv Datastream

In 1Q22, the Eurozone economy already suffered significantly from high inflation and the further negative effects of the Ukraine war. Consumption in particular has already been hit hard by high inflation. Industry continues to suffer from supply chain problems as well as the significant increase in energy prices. In contrast, the service sector is optimistic about the future following the end of the COVID restriction measures. Given the weak growth in 1Q, we have lowered our GDP growth forecast for 2022 to 2.8%. For 2023, we expect GDP growth of 2.6%.

Eurozone Inflation Rate*

as of Jun 22

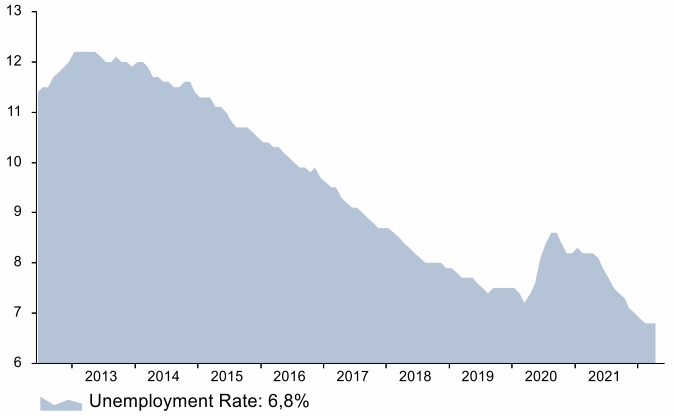


Quelle: Refinitiv Datastream

In May, inflation rose to a new record high of 8.1% y/y. While upward pressure from energy prices has stabilized, price pressure from food and core inflation has continued to rise. In the near term, we expect upward pressure from food prices and core inflation to persist. The development of wages as well as producer prices is crucial for the further course of core inflation. In particular, the evolution of core inflation will be important for the further stance of monetary policy. By contrast, upward pressure from energy prices should ease gradually at least in the second half of the year.

Unemployment Rate Eurozone

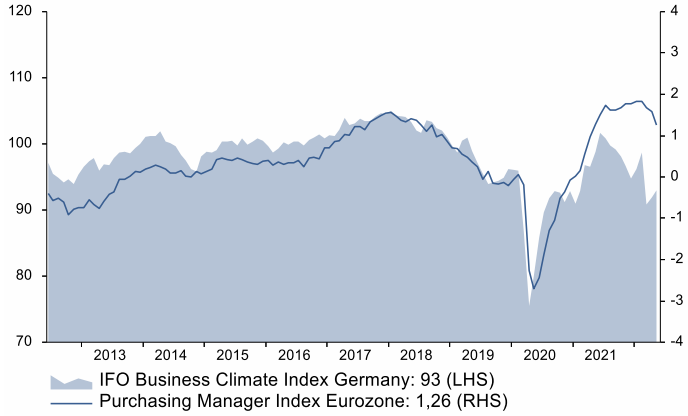
as of Jun 22



Quelle: Refinitiv Datastream

Eurozone Business Climate Indices

as of Jun 22



Quelle: Refinitiv Datastream

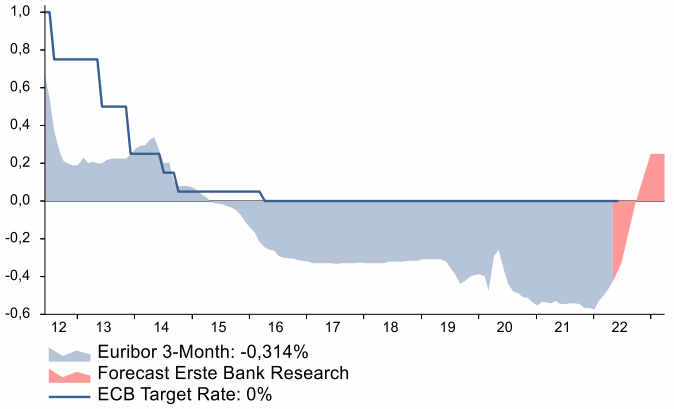
With reference to the graphs (pictured above): forecasts are not a reliable indicator for future performance.
* Forecasts are no reliable indicator for future performance.

Euro Fixed Income

Money Market and Government Bonds

Money Market Euro*

as of 07.06.2022



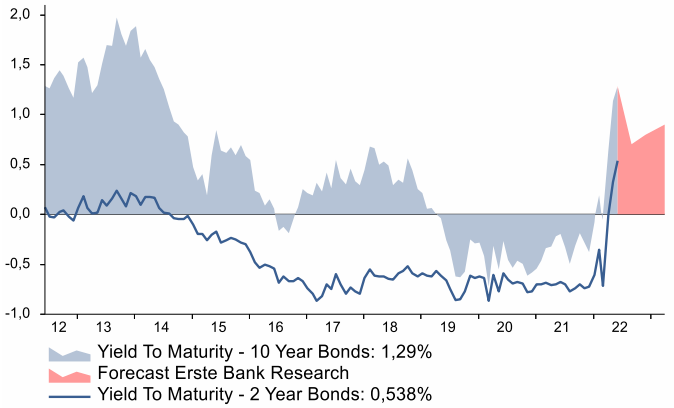
Quelle: Refinitiv Datastream

In June, the ECB will almost certainly decide to quickly end its securities purchases, opening the door for a first interest rate hike in July. We expect the deposit rate to be raised by 25bp. Interest rate steps of the same magnitude should follow in September and December, at which time the refinancing rate should also be raised. The ECB has to confront rising inflationary pressures, according to recent data. At the same time, however, there are increasing signs that the economy is weakening. Which of these forces will be stronger is very uncertain, as is the ECB's monetary policy stance during the coming quarters.

Forecast: somewhat negative

German Government Bonds*

as of 07.06.2022

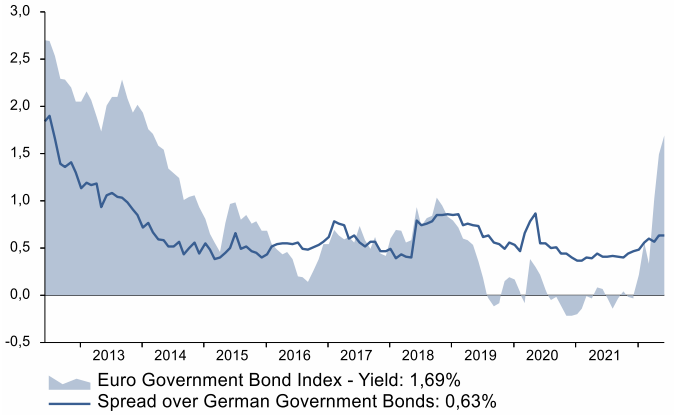


Quelle: Refinitiv Datastream

Over the past few weeks, yields on German government bonds with medium- and long-term maturities stabilized at a high level. From the market's perspective, there was no reason to relax. Only the latest data for May confirmed the persistent inflationary pressure in the Eurozone. Risks were reflected most strongly in short maturities, with yields reaching 2022 highs. We expect weaker economic data to have a dampening effect on medium- and long-term interest rate expectations and thus the corresponding yields on the bond market should fall. Short maturities, on the other hand, should continue to rise as future interest rate hikes are increasingly factored into valuations.

Euro Government Bonds

as of 07.06.2022



Quelle: Refinitiv Datastream

Significant price losses since the beginning of the year. Driving factor: sharp rise in the market's expectations of a key interest rate hike. At the beginning of the year, a three-month interest rate of -0.31% was still priced for December 2022. By June 2, this had risen to 0.92%. This was accompanied by an increase in future inflation rates priced into the market (10-year Germany: from 1.8% to 2.98%) by early May. In May, however, the further increase in key rate hike expectations led to a decline in priced-in inflation (currently: 2.36%). In addition, there was also a widening of yield spreads for country credit risk. With an effective yield of 1.64%, EUR government bonds have now reached their highest level since 2014.

Forecast: negative

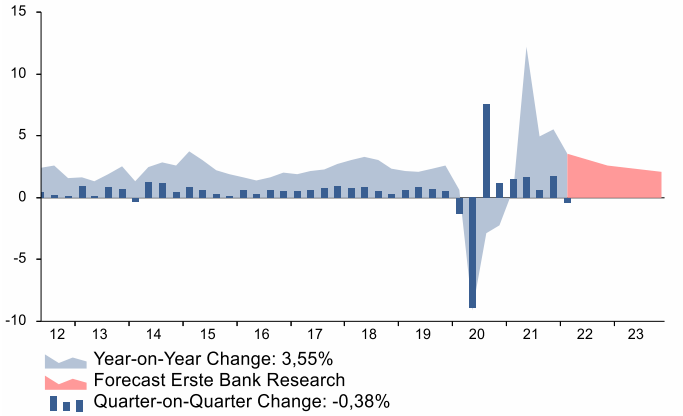
With reference to the graphs (pictured above): forecasts are not a reliable indicator for future performance. Please refer to the annex for the underlying index.
* Forecasts are no reliable indicator for future performance.

US Economics

Overview

US Real GDP Growth Rate*

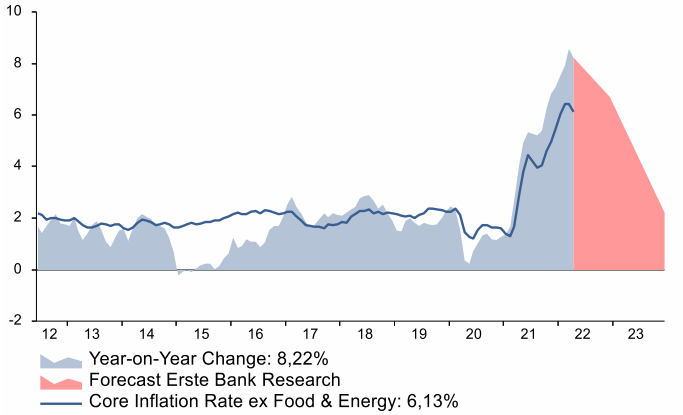
as of Q2 22



The US economy contracted in the first quarter, but this was largely due to foreign trade and inventory changes. By contrast, domestic demand still showed solid growth. The current quarter should be better overall, although uncertainty is high. On the one hand, demand is being supported by high wage increases and the good overall financial situation of American households. On the other hand, high inflation and the sharp rise in interest rates are having a negative impact. All in all, this should result in quarterly growth moving in the direction of the economy's potential, which corresponds to an annual growth rate of around 2%.

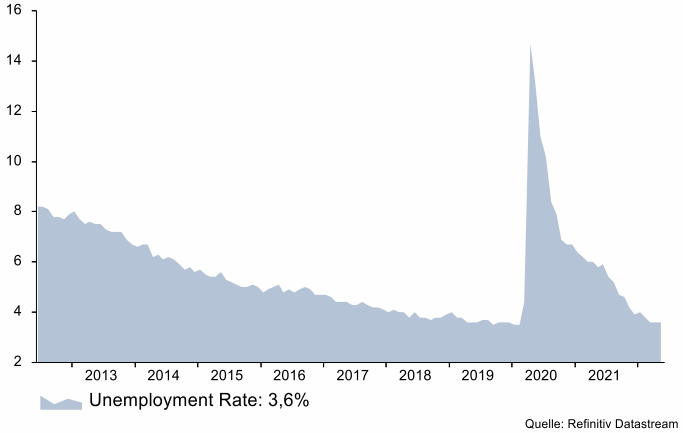
US Inflation Rate*

as of Apr 22



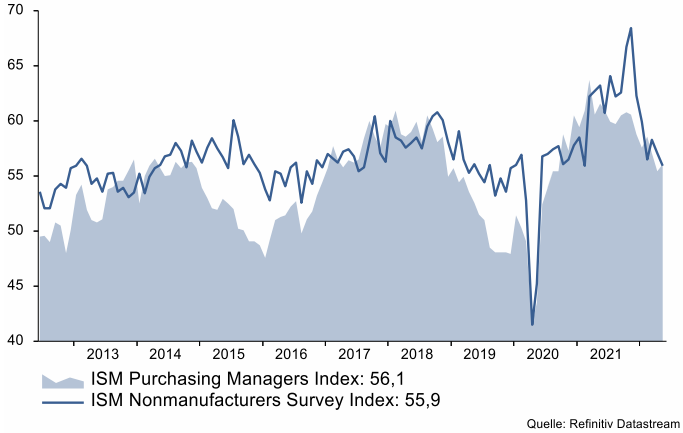
US Unemployment Rate

as of Mai 22



US ISM Purchasing Managers Index

as of Mai 22



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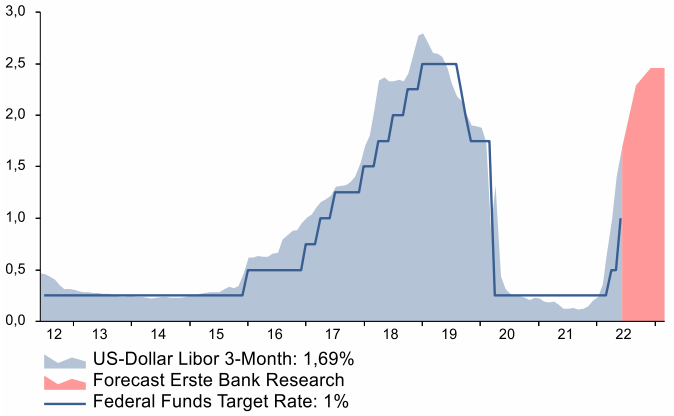
US Fixed Income

Money Market and Government Bonds

Money Market US*

as of 07.06.2022

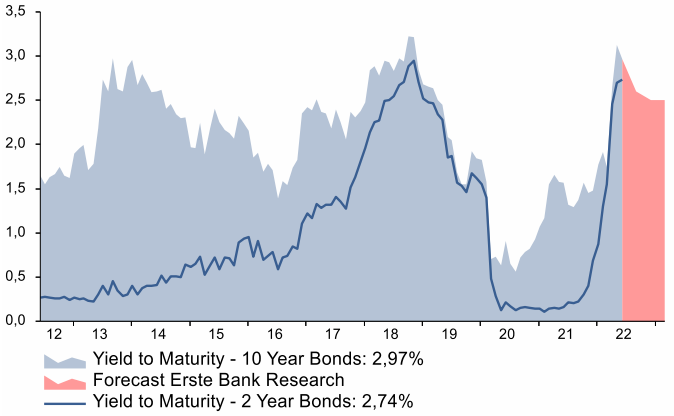


Quelle: Refinitiv Datastream

The signals from the US Fed are clear and suggest a series of further rate hikes. According to Chairman Powell, steps of 50bp are on the table at the upcoming meetings. We expect rate hikes of this magnitude in June and July. Then, from September, the pace should slow to 25bp. The reason for this is that we expect a sustained slowdown in the economy, which should lead to an easing on the labor market and thus a weakening of the factors driving inflation. This trend should continue to the extent that the last interest rate step for the time being should take place in November, after which the Fed will adopt a wait-and-see stance.

US Government Bonds*

as of 07.06.2022

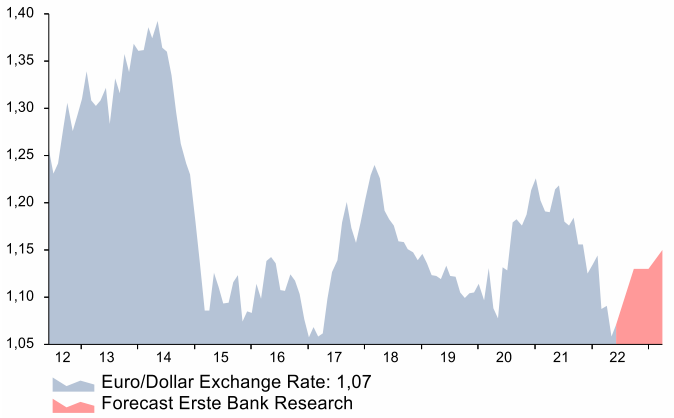


Quelle: Refinitiv Datastream

Following a sharp sell-off, the US bond market has seen a countermovement across all maturities in recent weeks. We see this as being in line with the downside risks to the economy and therefore consider the movement to be sustainable. A further slight decline in yields on medium and longer maturities seems likely to us as soon as the indicators show clear signs of an economic slowdown. In contrast, we expect short maturities to be little changed. The market should enter calmer waters overall after the strong re-pricing.

Euro-Dollar Exchange Rate*

as of 07.06.2022



Quelle: Refinitiv Datastream

After strong gains until mid-May, the dollar weakened again recently. We see this latest move as justified, as the previous strengthening had no fundamental basis, but is likely to have been due to safe-haven inflows. In addition, this recent weakening of the dollar has been underpinned by a narrowing of the bond market yield spread between the US and Germany. The EURUSD should continue to be determined by political tensions and the yield differential. We expect a slow further reduction of the yield differential and at least no escalation of the conflict between the West and Russia, both of which argue for a weaker dollar.

With reference to the graphs (pictured above): forecasts are not a reliable indicator for future performance. Please refer to the annex for the underlying index.
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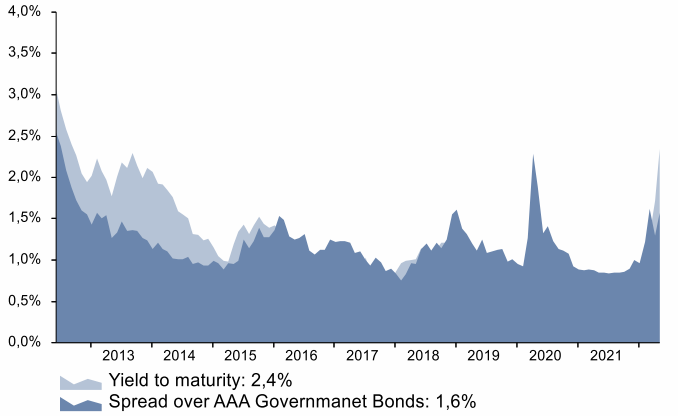
Corporate Bonds

Investment Grade

Euro Corporate Bonds: Yield & Spread

as of 07.06.2022



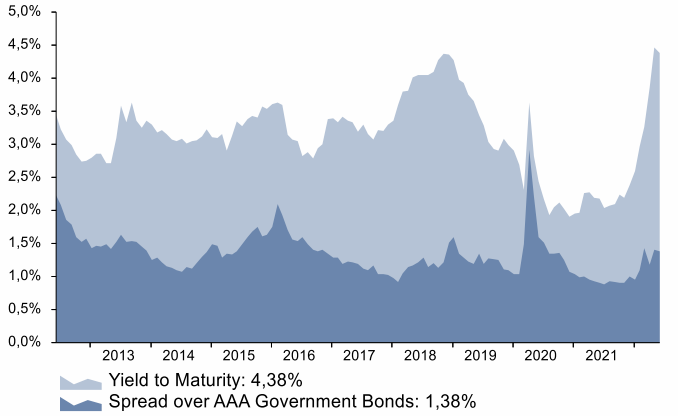
Quelle: Refinitiv Datastream

Risk premiums and yields continued to rise in May. High energy and raw material prices, transport costs and supply bottlenecks as well as the Ukraine war remain major negative factors. In this context, the 1Q reporting season was still relatively good. IG bonds (-1.4%) underperformed HY bonds (-0.9%) on average in May. The former were more affected by rising Bund yields due to their longer maturities and lower coupons. IG hybrid bonds outperformed in May (-0.2%). Defensive sectors (such as telecoms, utilities) are more strongly represented in the hybrid market. IG bonds from these sectors remain recommended for cautious investors.

Forecast: somewhat negative

US Corporate Bonds: Yield & Spread

as of 07.06.2022



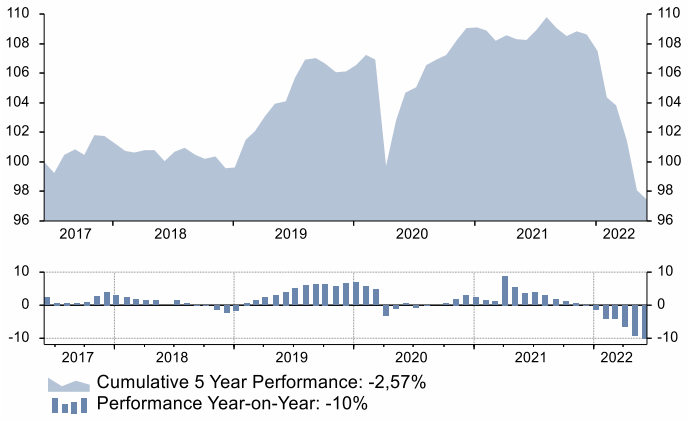
Quelle: Refinitiv Datastream

US IG corporate bonds have shown significant price losses since the beginning of the year. The driving factor behind this is a large increase in key interest rate hike expectations priced into the market. At the beginning of the year, a U.S. key interest rate of 0.82% was still priced for December 2022. By June 2, this had risen to 2.8%. In addition, an increase in the yield spread for credit risk took place. However, the spread level is still slightly below the long-term average (137 bp vs. 157 bp). With an effective yield of around 4.29%, corporate bonds have now reached their highest level since the end of 2018 (excluding March 2020). Negative: key interest rate hikes. Supportive: USA less affected by war in Ukraine than Europe.

Forecast: neutral

Euro Corporate Bonds: Performance

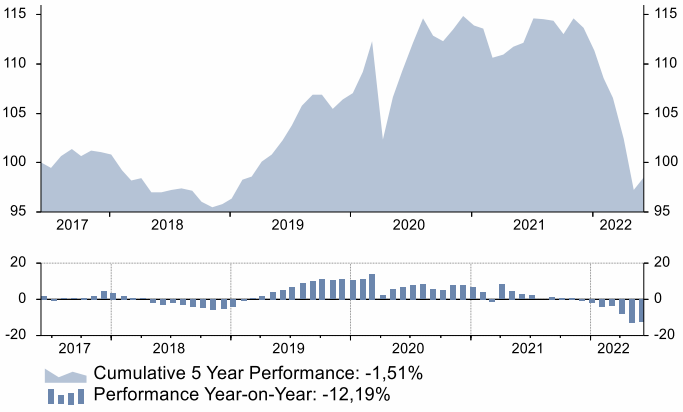
as of 07.06.2022



Quelle: Refinitiv Datastream

US Corporate Bonds: Performance

as of 07.06.2022



Quelle: Refinitiv Datastream

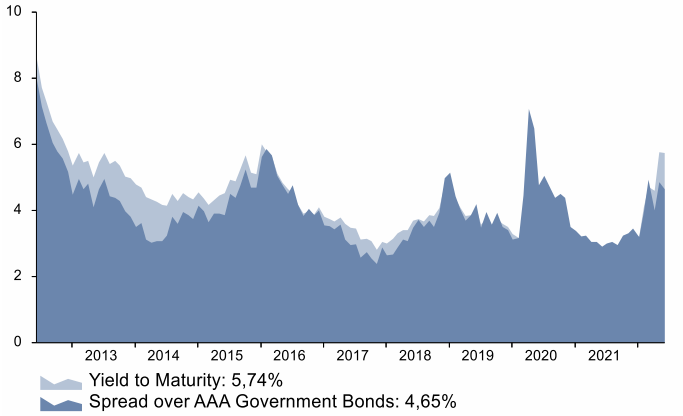
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

High Yield Bonds

Corporate Bonds with a Speculative Rating

Euro High Yield: Yield & Spread

as of 07.06.2022



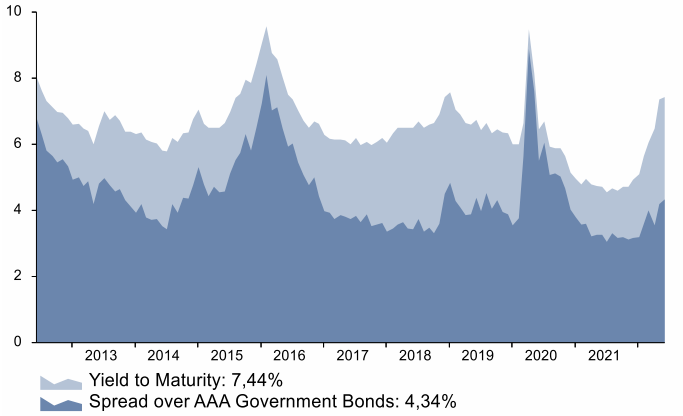
Quelle: Refinitiv Datastream

Leading economic indicators were better than expected in May. This contributed to spread tightening towards the end of the month and to the outperformance of HY bonds (-0.9%) vs. IG bonds (-1.4%). Credit metrics of HY issuers weakened only marginally in 1Q. Their refinancing needs are low in 2022. For now, it is not a problem if the primary market for HY issues closes. True, Moody's expects the default rate to rise. But it should remain low and below the long-term average. As uncertainty remains high in the market, we still prefer bonds from less energy-intensive, defensive sectors.

Forecast: neutral

US High Yield: Yield & Spread

as of 07.06.2022



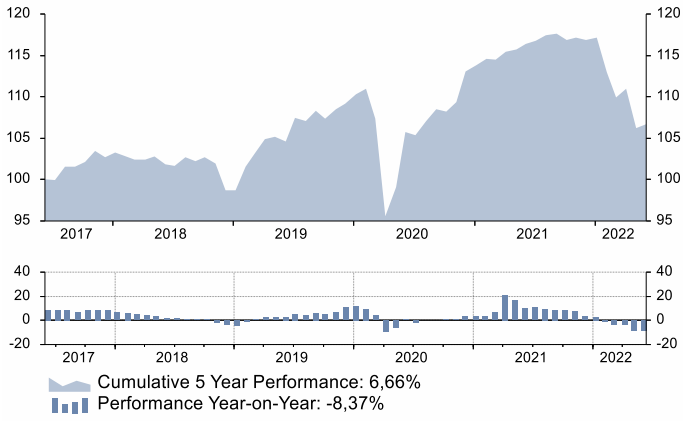
Quelle: Refinitiv Datastream

The determining factor for the development of yields since the beginning of the year has been the increase in key interest rate hike expectations priced into the market. However, the price losses of U.S. high-yield corporate bonds since the beginning of the year have been lower than those of U.S. investment grade corporate bonds. This can be attributed to the significantly low sensitivity (duration) of the percentage yield trend to interest rate increases. In addition, there was only a moderate increase in the yield premium for credit risk. The spread level is well below the long-term average (413 bp vs. 541 bp). With an effective yield of just under 7%, bonds have now reached their highest level since the beginning of 2019 (excluding March 2020).

Forecast: somewhat positive

Euro-High Yield: Performance

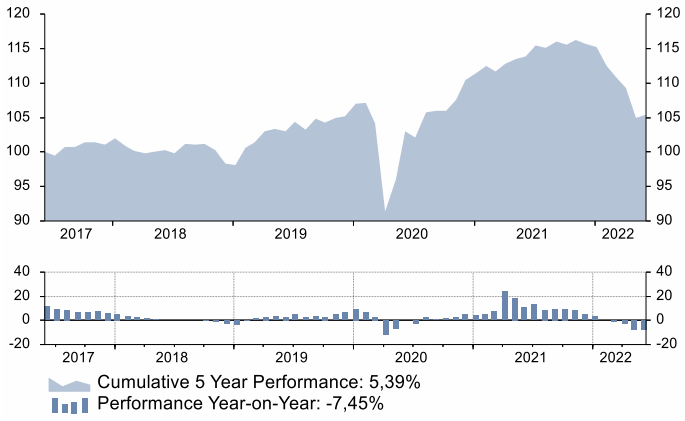
as of 07.06.2022



Quelle: Refinitiv Datastream

US High Yield: Performance

as of 07.06.2022



Quelle: Refinitiv Datastream

With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

BRIC Economics

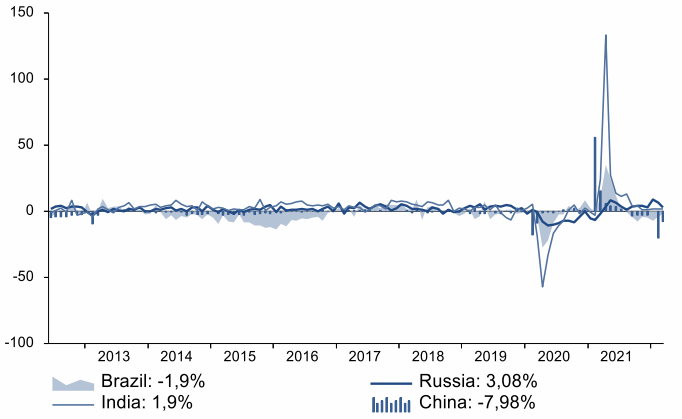
Brazil, Russia, India and China

The impact of the war in Ukraine on real economic growth is not clearly negative in the base scenario. Even before that, stagnation had been assumed (2022: 1.0% p.a.). However, expectations for inflation have risen (Q422: from 5% to 8%). The key interest rate has been raised sharply from 2% to 12.75% since 2021. Further hikes are likely. Unlike many other currencies, the Brazilian real has strengthened significantly against the USD since the beginning of the year (higher interest rates and commodity prices). Local-currency bonds have strengthened slightly, but USD bonds are showing price losses.

The sanctions imposed by the West are hitting the Russian economy hard. Some Russian banks have been excluded from the SWIFT interbank messaging system. A large portion of the Russian Central Bank's foreign currency reserves have been frozen. In addition, foreign companies are pausing or terminating relations with Russia. This means a slump in trade and GDP (labor assumption: -6% this year) as well as a disruption of supply chains. At the same time, capital controls have been imposed. The relationship between the West and Russia has deteriorated further. Finland and Sweden want to join NATO. In early June, the EU adopted import restrictions on crude oil (with exceptions) in the sixth sanctions package. Downside risks remain high.

Industrial Production BRIC

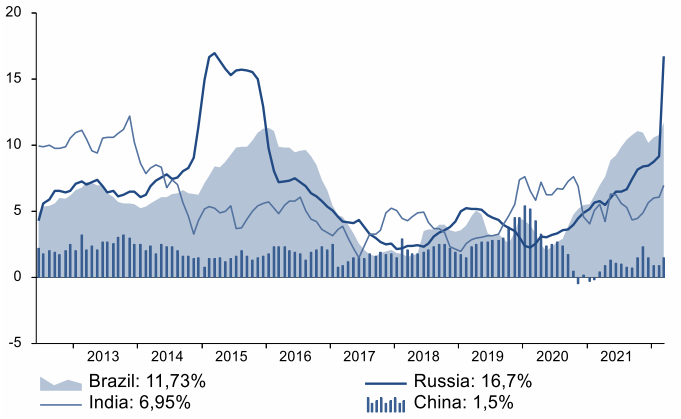
Year-on-Year Change in %, as of Mrz 22



Quelle: Refinitiv Datastream

Inflation Rates BRIC

Year-on-Year Change in %, as of Mrz 22



Quelle: Refinitiv Datastream

The immediate impact of the war in Ukraine is stagflationary. Real GDP growth is expected to be around 2 percentage points lower (2022: 7% p.a.). The recovery phase from the pandemic provides a buffer. However, India is particularly vulnerable as a major energy importer. Inflation could be around 1.5 percentage points higher (2022: 6.5% p.a.). Since the beginning of the year, the Indian rupee has been in a downtrend. At the same time, government bond yields are rising (effective yield: 7.4%, highest since 2019). At the beginning of May, the central bank gave in to the pressure and surprisingly raised the key interest rate from 4% to 4.4%.

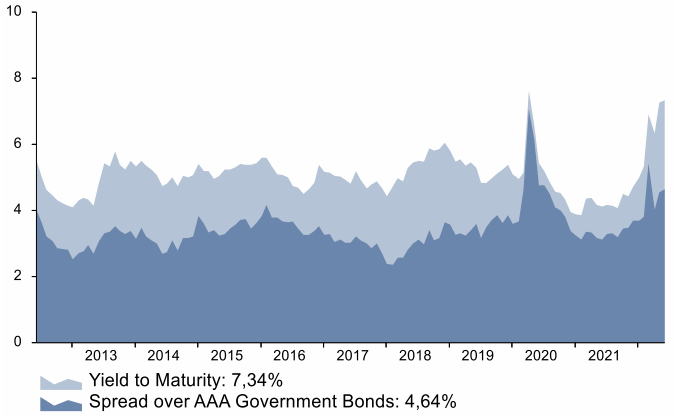
In March and April, the zero tolerance policy toward new infections led to lockdown measures. Hard data for March and April (retail trade, production) suggest a sharp contraction in economic activity. However, survey-based indicators for May already suggest an incipient recovery. The risk that the official target for real economic growth (5.5%) will not be reached this year has increased (expectation: 4%). The official side has announced numerous targeted economic support measures. Government bonds have shown price increases (in local currency) since the beginning of the year. However, there has been a significant weakening of the renminbi against the USD.

Emerging Market Bonds in Euro

Hedged in EUR

Emerging Market Bonds in Hard Currency

Yield & Spread, as of 07.06.2022



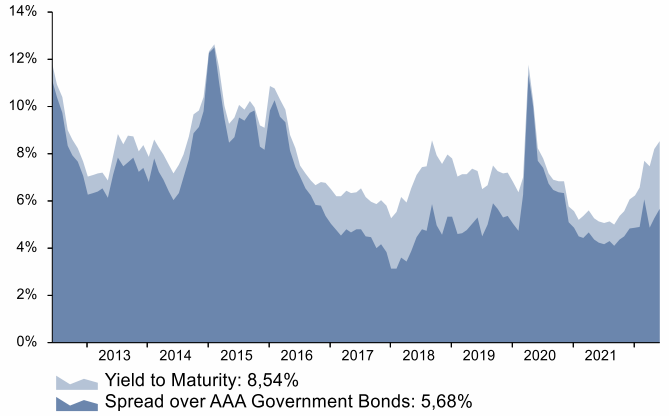
Quelle: Refinitiv Datastream

Negative return trend since the beginning of the year. The determining factor for this was the sharp rise in yields on US government bonds. In addition, there was an increase in the yield premium for credit risk in the first weeks of the war, but this has subsequently narrowed somewhat. The financial environment remains unfriendly. Increased risk aversion on the markets, U.S. key interest rate hikes, increased inflationary pressure means key interest rate hikes in numerous countries. Slight positive: US government bond yields have fallen somewhat recently, as has the US dollar. Higher commodity prices have mixed effects: Negative for importers, support for exporters.

Forecast: somewhat positive

Emerging Corporates in Hard Currency

Yield & Spread, as of 07.06.2022



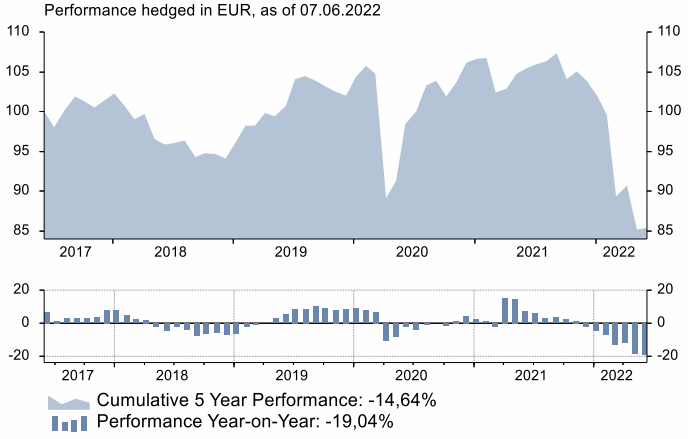
Quelle: Refinitiv Datastream

Negative earnings development since the beginning of the year. Reasons: 1) Increased rate hike expectations and yield increases in the US. Shorter duration compared to EM government bonds helps. 2) China: real estate crisis and lockdown measures. Additional economic support measures announced in response. 3) At least spread widening in response to Ukraine invasion has almost disappeared. The financial environment remains unfriendly. Slightly positive: U.S. dollar and U.S. yields down slightly recently. Higher commodity prices have mixed effects via terms of trade (ratio of export to import prices): Negative for importers, supportive for exporters.

Forecast: somewhat positive

Emerging Market Bonds in Hard Currency

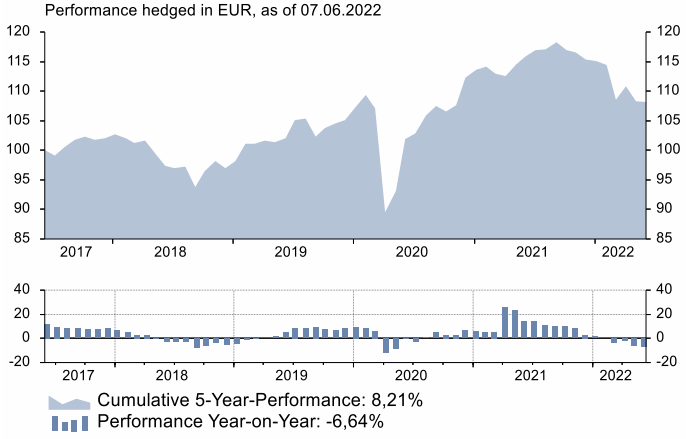
Performance hedged in EUR, as of 07.06.2022



Quelle: Refinitiv Datastream

Emerging Corporates in Hard Currency

Performance hedged in EUR, as of 07.06.2022



Quelle: Refinitiv Datastream

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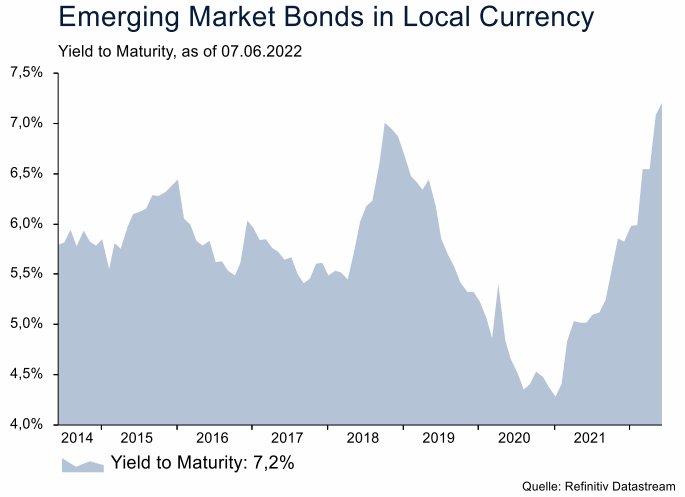
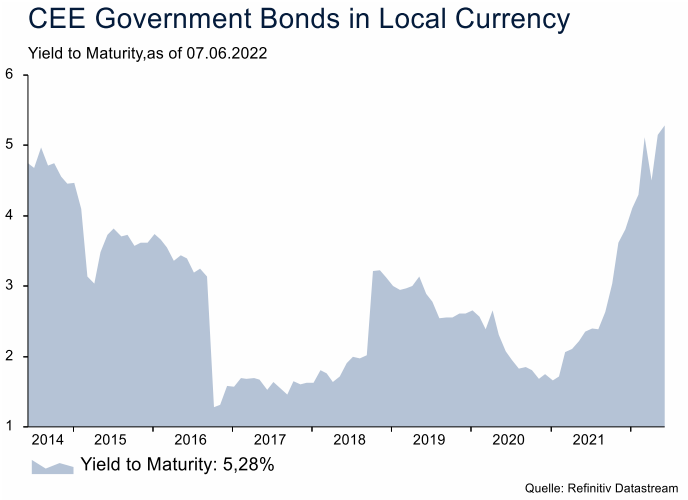
Emerging Market Bonds in Local Currency

Global and Central Europe



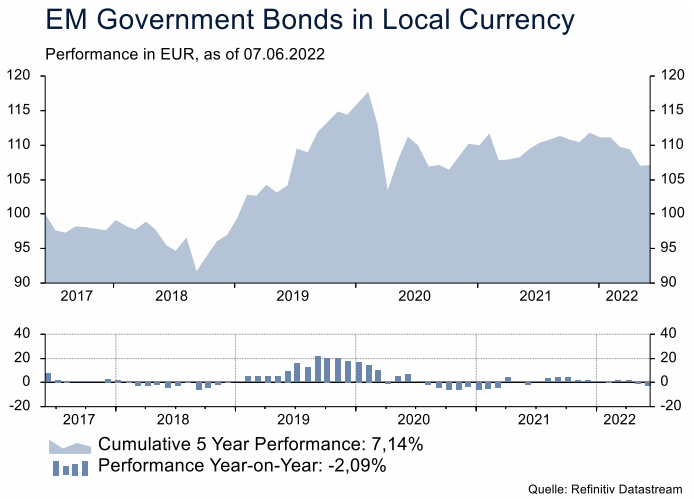
Since the beginning of 2021, key interest rates in the aggregate have risen significantly (from 3% to 4.3%). Numerous central banks have raised key rates due to increasing inflation risks. The aim is to contain a pass-through from the current high inflation rates to inflation expectations and to stabilize the currency. The rise in commodity prices has further increased this pressure. For this reason, yields on local currency bonds have been trending upward since the beginning of 2021 (currently: just over 7%). At least the EM currency basket is trending sideways against the US dollar. The currencies of some commodity exporters (Brazil, Mexico) are showing signs of strengthening.

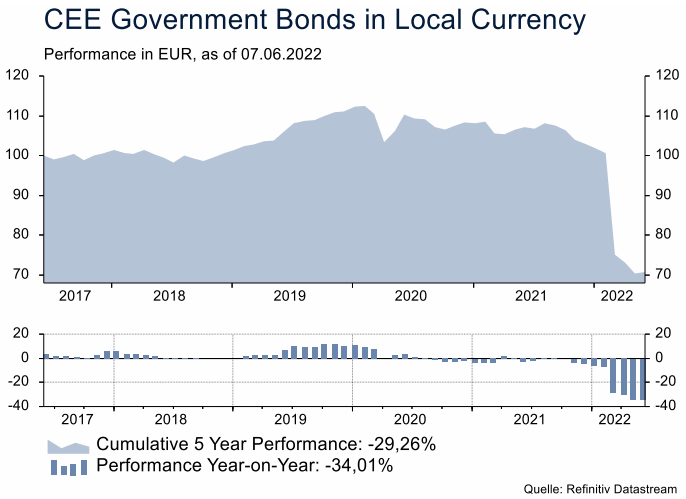
Forecast: somewhat positive



The sharp increases in commodity prices will keep inflation rates at a high level in the coming months (upside risks). High inflation rates are dampening purchasing power. Especially in the event of supply disruptions for energy, the risks of recession would increase. Central banks are under pressure to raise key interest rates (Czech Republic: 5.75%, Hungary, 5.9%, Poland: 5.25%, Romania, 3.75%). This environment has led to a rising trend in yields. The yield curves in Poland, the Czech Republic and Hungary are already partly inverted, i.e., long-dated yields are lower than shorter-dated yields (pricing in key interest rate cuts). Currencies are showing mixed developments (weakening pressure on HUF and TRY).

Forecast: neutral





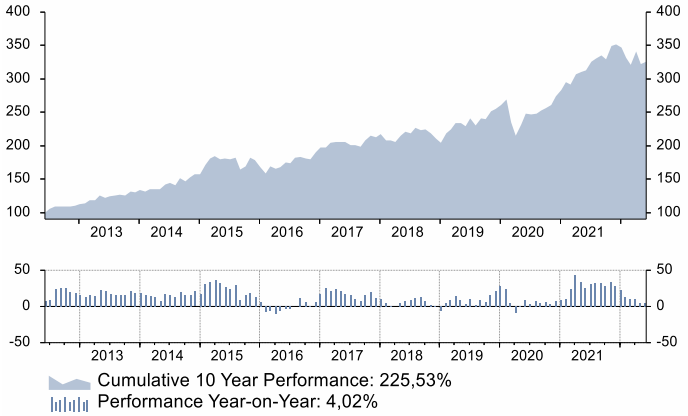
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Equities Developed Markets

Overview

Developed Markets

Performance in EUR, as of 07.06.2022



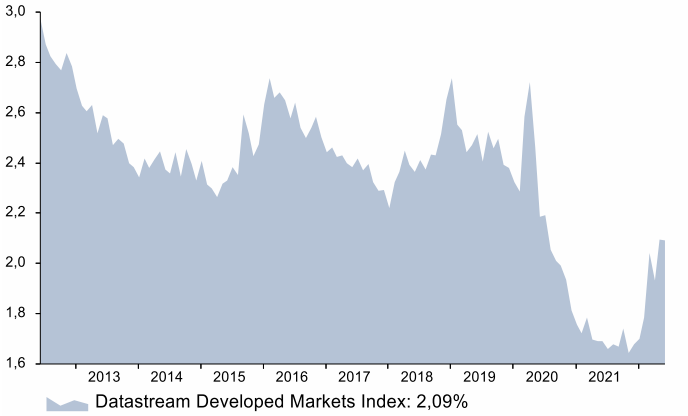
Quelle: Refinitiv Datastream

The global equity index fell by -1.9% in EUR terms in May. The S&P 500 declined by -1.7% in EUR terms. The Stoxx 600 was -1.6% lower in EUR. Rising energy prices, ongoing supply chain issues and the interest rate turnaround in the USA reduced investors' risk appetite. The outlook for corporate sales and earnings growth is positive for 2022. Sales are expected to grow +7.6% (y/y) in 2022 and earnings are expected to increase +7.5% (y/y). The valuation of the global equity market index has declined due to earnings growth and because of the market decline. The P/E ratio expected for 2022 is 15.6x. We expect the global equity market index to move sideways in June.

Forecast: somewhat positive

Dividend Yield

as of 07.06.2022

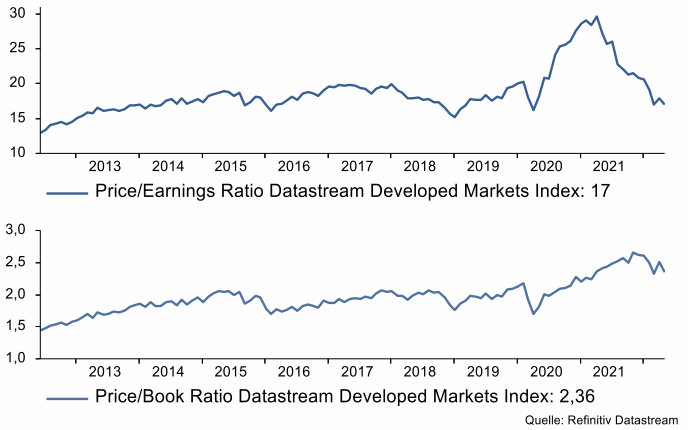


Quelle: Refinitiv Datastream

The reporting season has been positive for 1Q in the US with earnings up +7.1% (y/y). Sales and earnings growth will be lower in 2Q. S&P 500 companies' sales growth should be +10.0% (y/y) and earnings growth +4.1% (y/y). European companies have reported mostly positive earnings surprises in the 1Q reporting season. Profits have increased by about +41% (y/y). Growth rates will be lower going forward, partly due to the negative impact of Russia's war of aggression on Ukraine. For 2Q, earnings growth of +15.0% (y/y) is expected and sales growth of +21% (y/y). We expect a sideways movement of the leading indices in Europe and the USA in June.

Key Indicators

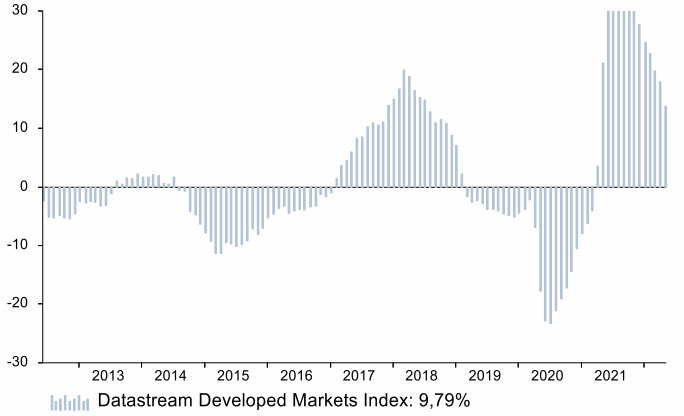
as of 07.06.2022



Quelle: Refinitiv Datastream

Earnings Growth

Earnings Expectation per Share: Year-on-Year Change, as of 07.06.2022



Quelle: Refinitiv Datastream

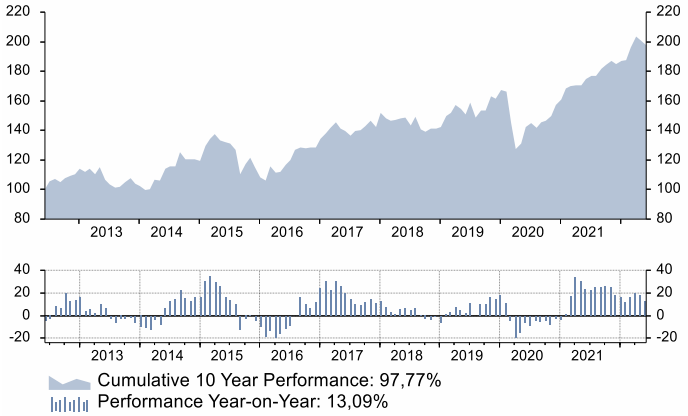
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Equities Emerging Markets

Overview

Emerging Markets

Performance in EUR, as of 07.06.2022



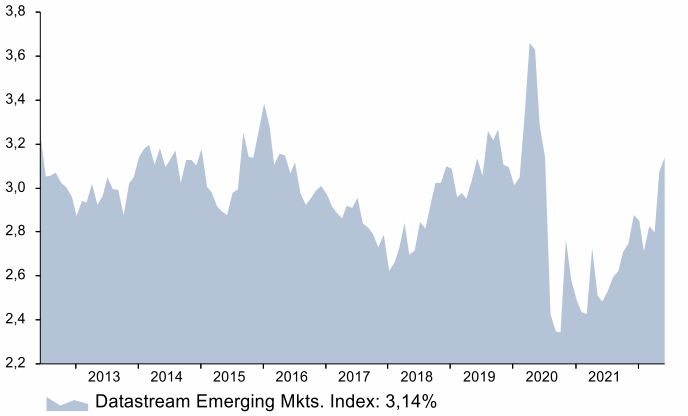
Quelle: Refinitiv Datastream

The global emerging market index fell by -1.6% in EUR terms in May. The commodity-oriented Brazilian benchmark index showed pronounced relative strength to the emerging market index. It gained +5.9% in EUR terms. The Chinese leading index posted a gain of +2.0% in EUR terms. Earnings growth forecasts for the emerging markets have been revised slightly downwards in recent weeks. Currently, earnings are expected to grow +5.0% (y/y) in 2022. The low valuation (2022e P/E: 11.2x) and high dividend yield (2022e: 3.6%) reflect the heightened political and economic risks of investing in emerging markets. We expect the global emerging markets index to move sideways in June.

Forecast: neutral

Dividend Yield

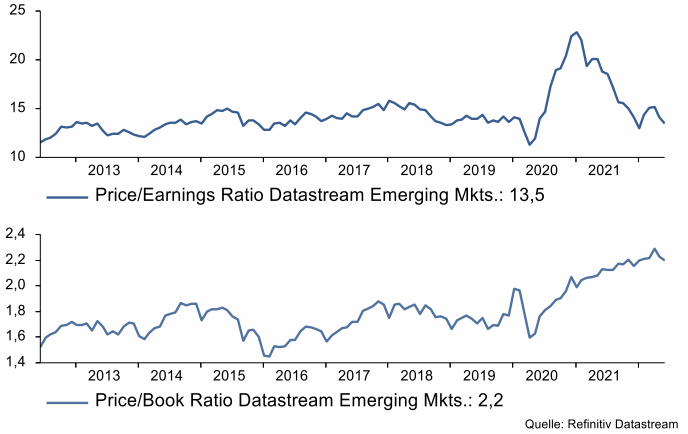
as of 07.06.2022



Quelle: Refinitiv Datastream

Key Indicators

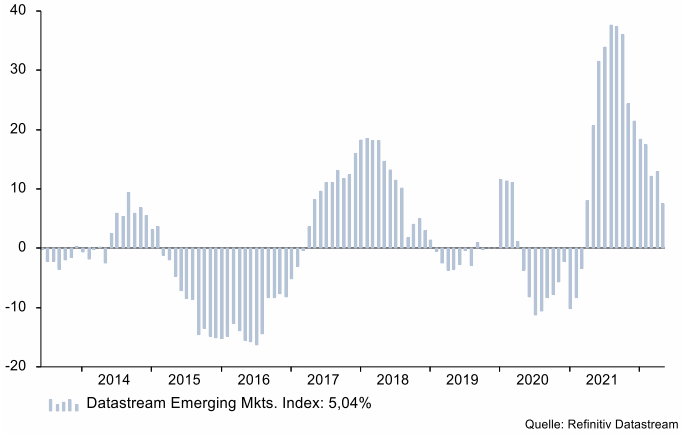
as of 07.06.2022



Quelle: Refinitiv Datastream

Earnings Growth

Earnings Expectation per Share: Year-on-Year Change, as of 07.06.2022



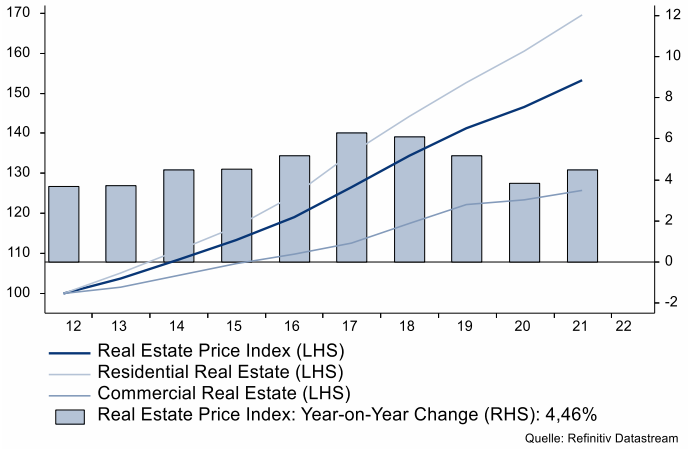
Quelle: Refinitiv Datastream

With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Alternative Investments

Real Estate, Gold and Commodities

German Real Estate

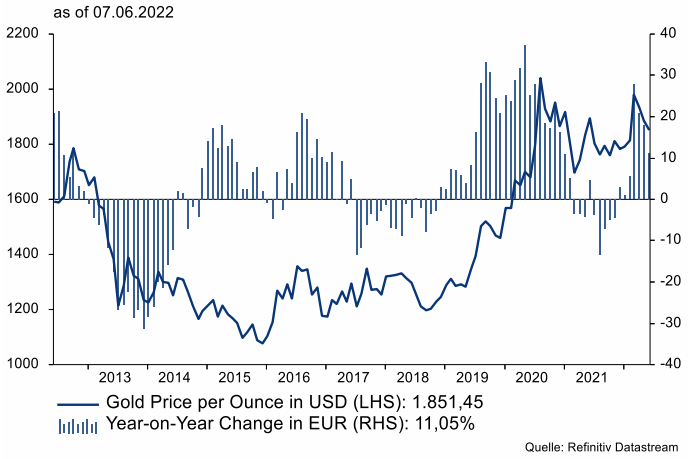


Quelle: Refinitiv Datastream

The rapid rise in yields on US government bonds led to a decline in the price of gold in May. It fell by -4.9% in EUR terms. In the medium term, however, the continued negative real yields in the USA and Europe have a supportive effect on the gold price. The slowdown in global corporate earnings momentum this year and an expected slowdown in global economic growth have led to an increase in equity market volatility. This favors a positive development of the gold price. This situation should continue in the medium term. Geopolitical uncertainties also remain elevated. We expect the gold price to rise moderately in June.

Forecast: neutral

Gold

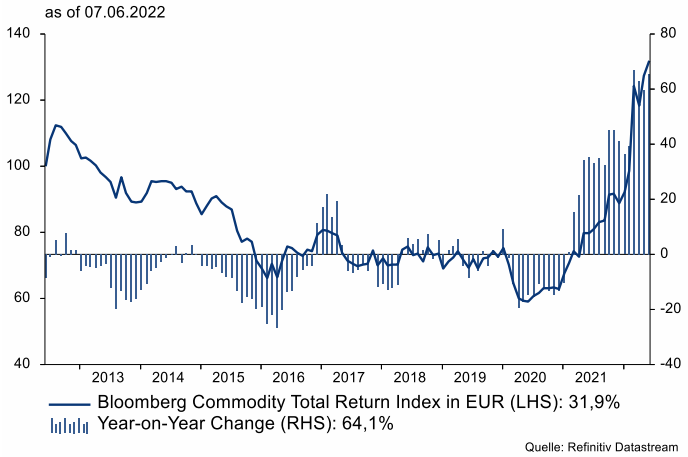


Quelle: Refinitiv Datastream

The commodity sectors are developing inconsistently. The Ukraine crisis has caused pronounced price rises in energy and agricultural goods. Russia is a leading producer of oil, gas and grain. The latter also applies to Ukraine. The sanctions imposed by the West are increasingly affecting the energy sector. Most recently, partial oil embargo by the EU. Actual supply stoppages of gas remain a significant risk. Food prices are being driven upward by the Russian port blockade. This contrasts with a clear downward trend in industrial metals after the price jump in early March. This could have to do with the slump in economic activity in China, caused by the lockdown measures.

Forecast: neutral

Commodities



Quelle: Refinitiv Datastream

In April, the US inflation rate was lower than in the previous month for the first time since summer 2021. The main reason for this was that strong price increases from the previous year dropped out of the calculation. In our view, the turnaround in US inflation has thus begun. However, based on an inflation rate of over 8% and an expected slow decline, inflation in the US will remain high for the foreseeable future. The current price pressure shown by monthly price increases is still too high. A corresponding reduction through a cooling of the economy remains the challenge for the central bank.

Forecast: neutral

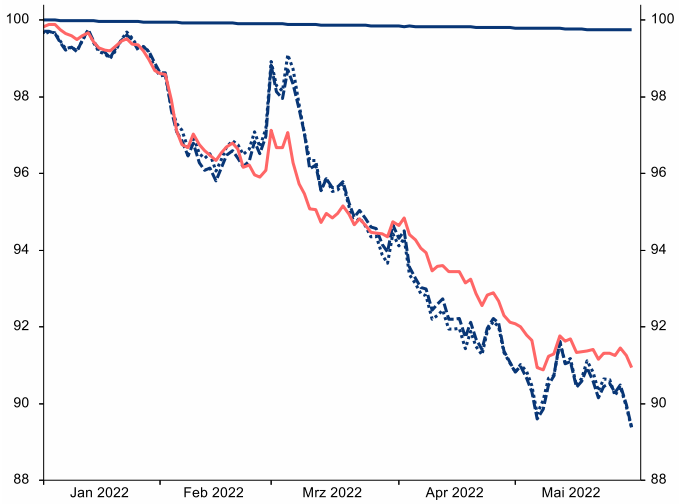
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Overview of Key Asset Classes

YTD Performance

Fixed Income Investment Grade

Performance YTD as of 31.05.2022

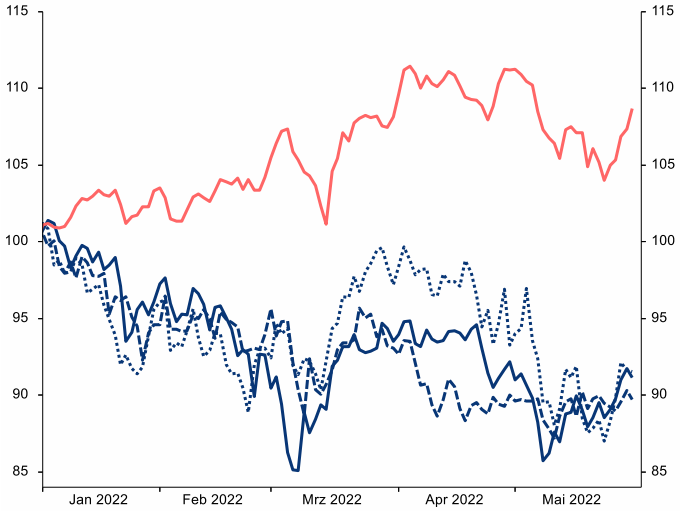


Euro Money Market: -0,26%
Euro Government Bonds AAA-AA: -10,65%
Euro Government Bonds Investment Grade: -10,62%
Euro Corporates Investment Grade: -9,07%

Quelle: Refinitiv Datastream

Equities

Performance YTD as of 31.05.2022

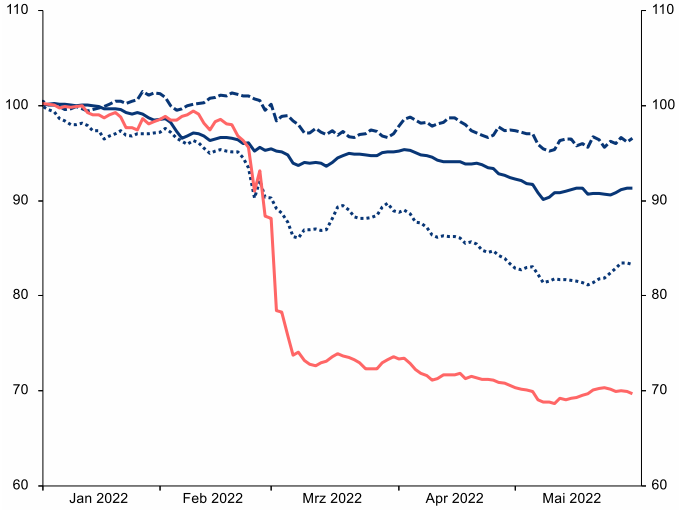


Equities Europe: -8,85%
Equities North America: -8,45%
Equities Japan: -10,27%
Equities Emerging Markets: 8,69%

Quelle: Refinitiv Datastream

Fixed Income High Yield

Performance YTD as of 31.05.2022

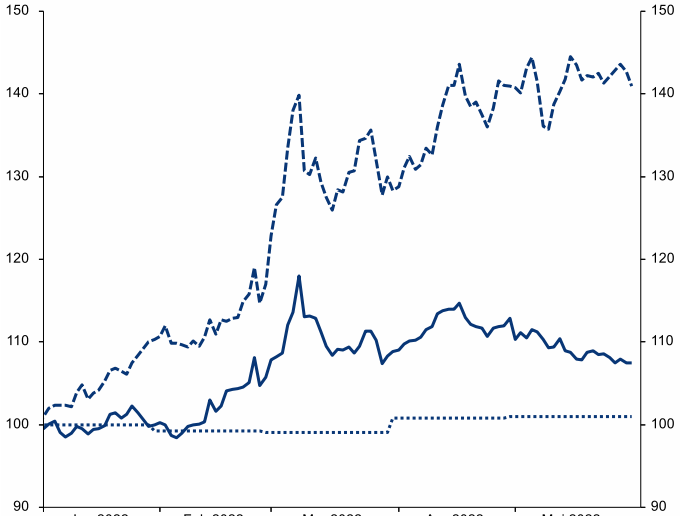


Euro High Yield: -8,72%
Emerging Market Bonds in Hard Currency: -16,70%
Emerging Market Bonds in Local Currency: -3,43%
CEE Government Bonds in Local Currency: -30,31%

Quelle: Refinitiv Datastream

Alternative Investments

Performance YTD as of 31.05.2022



Gold in EUR: 7,49%
Hedge Fund Index: 0,97%
Commodity Index: 40,92%

Quelle: Refinitiv Datastream

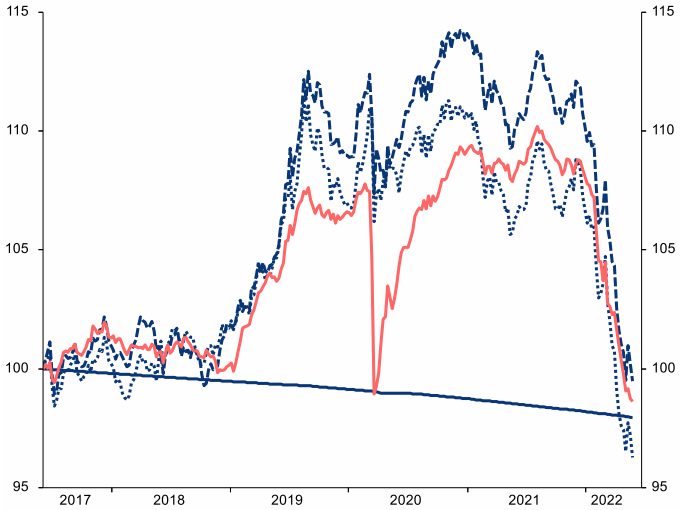
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. This performance representation has little validity due to its short duration. Please refer to the annex for the underlying index.

Overview of Key Asset Classes

5 Year Performance

Fixed Income Investment Grade

5 Year Performance as of 31.05.2022



Euro Money Market: -2,05%
Euro Government Bonds AAA-AA: -4,65%
Euro Government Bonds Investment Grade: -1,49%
Euro Corporates Investment Grade: -1,73%

Quelle: Refinitiv Datastream

Equities

5 Year Performance as of 31.05.2022

Equities Europe: 32,30%
Equities North America: 85,47%
Equities Japan: 18,78%
Equities Emerging Markets: 44,22%

Quelle: Refinitiv Datastream

Fixed Income High Yield

5 Year Performance as of 31.05.2022

Euro High Yield: 7,01%
Emerging Market Bonds in Hard Currency: -13,29%
Emerging Market Bonds in Local Currency: 8,00%
CEE Government Bonds in Local Currency: -28,96%

Quelle: Refinitiv Datastream

Alternative Investments

5 Year Performance as of 31.05.2022

Gold in EUR: 52,98%
Hedge Fund Index: 9,38%
Commodity Index: 76,19%

Quelle: Refinitiv Datastream

With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Index-Guide

Overview

Euro Money Market	• The BofA Merrill Lynch Euro Currency 3-Month LIBOR Constant Maturity Ind - Total Rtn Idx Val
Euro Government Bonds AAA-AA	• The BofA Merrill Lynch AAA-AA Euro Government Index - Total Rtn Idx Val
Euro Government Bonds Investment Grade	• The BofA Merrill Lynch Euro Government Index - Tot RI Val Hedged in Euro
Euro Government Bonds Inflation-Linked	• The BofA Merrill Lynch Euro Inflation-Linked Government Index - Tot RI Val Hedged in Euro
US Mortgage-Backed Securities	• The BofA Merrill Lynch US Mortgage Backed Securities Index - Tot RI Val Hedged in Euro
Euro Corporates Investment Grade	• The BofA Merrill Lynch Euro Corporate Index - Tot RI Val Hedged in Euro
US Corporates	• The BofA Merrill Lynch US Corporate Index - Tot RI Val Hedged in Euro
Euro High Yield	• The BofA Merrill Lynch Euro High Yield Index - Tot RI Val Hedged in Euro
US High Yield	• The BofA Merrill Lynch US High Yield Index - Tot RI Val Hedged in Euro
Emerging Market Bonds in Hard Currency	• The BofA Merrill Lynch Global Emerging Markets Sovereign Plus Index - Tot RI Val Hedged in Euro
Emerging Corporates in Hard Currency	• The BofA Merrill Lynch Global Emerging Markets Credit Index - Tot RI Val Hedged in Euro
Emerging Market Bonds in Local Currency	• The BofA Merrill Lynch Local Debt Markets Plus Index - Total Rtn Idx Val - TOT RETURN IND in Euro
CEE Governmnet Bonds in Local Currency	• The BofA Merrill Lynch Eastern Europe Government Index - Total Rtn Idx Val in Euro
Equites Developed Markets	• Developed Markets Datastream Market - TOT RETURN IND in Euro
Equities Europe	• Europe Datastream Market - TOT RETURN IND in Euro
Equities North America	• North America Datastream Market - TOT RETURN IND in Euro
Equities Japan	• Japan Datastream Market - TOT RETURN IND in Euro
Equities Emerging Markets	• Emerging Markets Datastream Market - TOT RETURN IND in Euro
Real Estate	• REAL INVEST AUSTRIA T - TOT RETURN IND
Gold	• Gold Bullion LBM U$/Troy Ounce in Euro
Hedge Funds	• Credit Suisse All Hedge Euro
Commodities	• Bloomberg- Commodity Ind TR - RETURN IND. (OFCL) in Euro

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As of June 2022

Imprint

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