Private Banking Investment Outlook

December 2022

ERSTE Private Banking

Private Banking Investment Outlook

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Private Banking Investment Outlook

Executive Summary

Dear Readers,

the falling dollar index and volatility favored the recovery of the global equity market index in November. It subsequently rose by +2.4% in EUR terms. Forecasts for sales and earnings growth of the companies in the global equity index improved slightly in November for 2023. Sales should increase +2.0% (y/y) in 2023 and profits should remain stable (2023e: +0.5% y(y)). The expected operating margin should be 17% next year and remain at the 2022 level. With an expected P/E ratio 2023e of 15.1x, the valuation of the global equity market seems reasonable. We expect the global equity market index to rise slightly in December. The gold price rose +3.8% in EUR terms in November. The year-to-date performance in EUR is +6.7%. Gold is thus outperforming the bond and equity asset classes this year. To fight inflation, the Fed will still raise interest rates this year. Nevertheless, real U.S. yields remain in negative territory. This is a factor that supports a positive gold price trend. We expect the gold price to move sideways in December.

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			●		

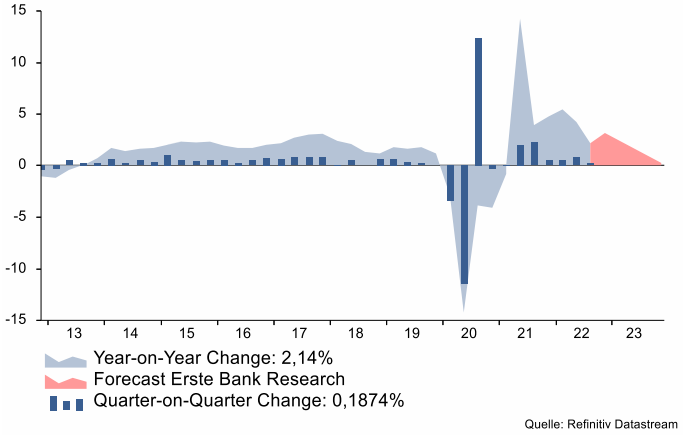
With reference to the chart „Asset Class Attractiveness": please refer to the annex for the underlying index. Forecasts are no reliable indicator for future performance.

Eurozone Economics

Overview

Eurozone Real GDP Growth Rate*

as of Q4 22

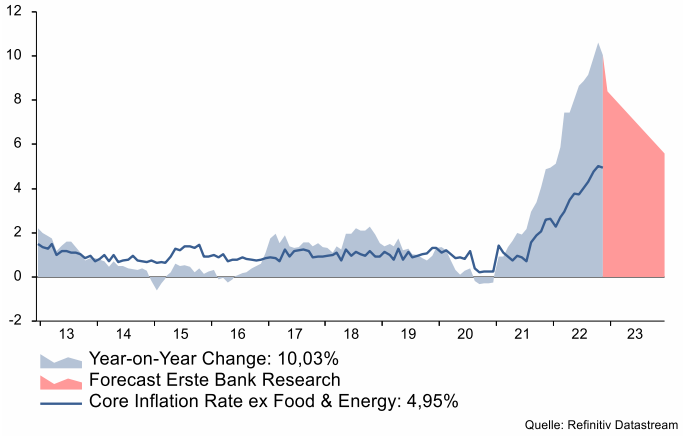


Quelle: Refinitiv Datastream

Based on leading indicators, we expect a slight decline in Eurozone GDP in 4Q. Against the backdrop of an uncertain outlook, we forecast a stabilization of the economy in 1Q23. From 2Q onward, the economy should gradually return to the growth path. Declining inflation momentum should have a supportive impact on the growth outlook during 1H23, as this should dampen interest rate expectations. In addition, falling inflation momentum should dampen real wage losses, from which consumption should benefit. For 2023, we expect GDP growth to decline significantly to 0.3%.

Eurozone Inflation Rate*

as of Dez 22

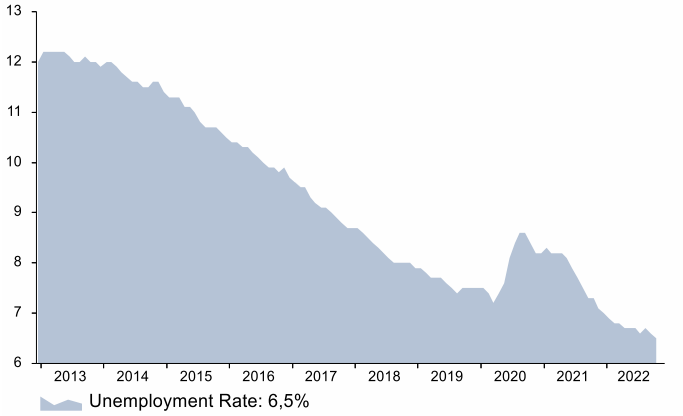


Quelle: Refinitiv Datastream

In November, the inflation rate fell for the first time in a long time and stood at 10.0% y/y (previously 10.6% y/y). The marked drop in the momentum of energy prices was mainly responsible for this decline. By contrast, the momentum of food prices increased once again. Core inflation stabilized at 5.0% y/y. At the global level, there are currently clear signs pointing to a further decline in inflation momentum in the coming months. From a monetary policy perspective, the focus is on the development of core inflation. We expect core inflation to decline more slowly than headline inflation in the coming months.

Unemployment Rate Eurozone

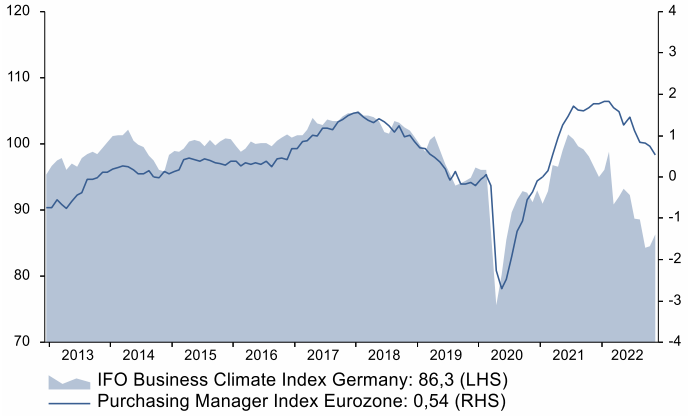
as of Dez 22



Quelle: Refinitiv Datastream

Eurozone Business Climate Indices

as of Dez 22

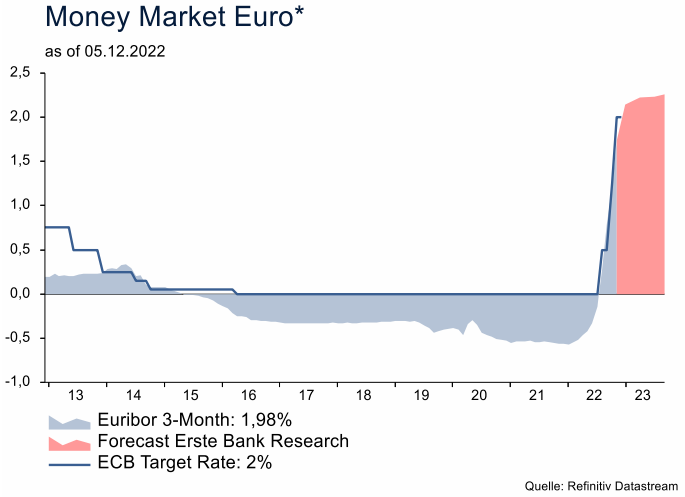


Quelle: Refinitiv Datastream

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

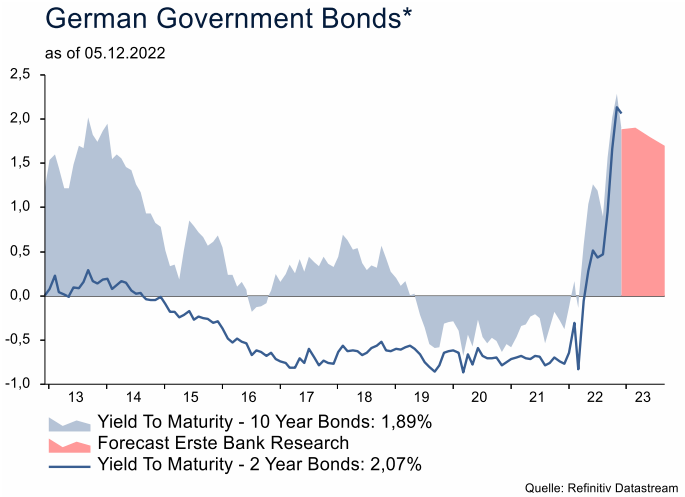
Euro Fixed Income

Money Market and Government Bonds

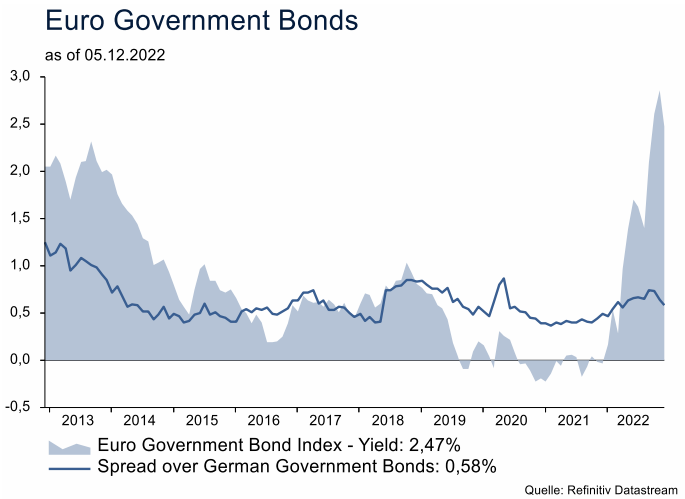


As had been widely expected, the Governing Council raised key interest rates by 75 basis points (bp) at the end of October. Further rate hikes were announced, but there were no indications as to the extent. Even what the decisions will depend on was kept extremely vague. The ECB is concerned with keeping inflation expectations under control, and the outlook for inflation and the economy would be decisive in future decisions. Most recently indications of a 50 bp rate hike in December and thus a slower ECB approach have become more pronounced. We then expect an interest rate hike of a further 25 bp in February.

Forecast: somewhat negative



Yields on the bond market continued their decline in recent weeks. Medium and longer maturities moved the most. The reason was that lower interest rate steps by the respective central banks are becoming apparent in the Eurozone and the US. This is the first step toward an eventual end to interest rate hikes. For the markets, this means a reduction in interest rate risks; mid- and long-term maturities benefited from this. However, the markets are quite far ahead of developments in terms of both economic indicators and monetary policy. We therefore expect the bond market to move sideways in the coming months.



Significant price losses since the beginning of the year. Driving factor: Sharp rise in key interest rate hike expectations priced into the market. At the beginning of the year, an effective key interest rate of -0.39% was still priced in for December 2022. By early December, this figure had risen to just under 2%. Until the beginning of May, this was accompanied by an increase in the future inflation rates priced into the market (10-year Germany: from 1.8% to just under 3%). However, from May onward, the further increase in key rate hike expectations led to a decline in priced-in inflation (currently: around 2.3%). Since hopes of declining inflation rates began to emerge in mid-October, government bonds have shown price increases. Even the yield spreads for country credit risk are falling again.

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.
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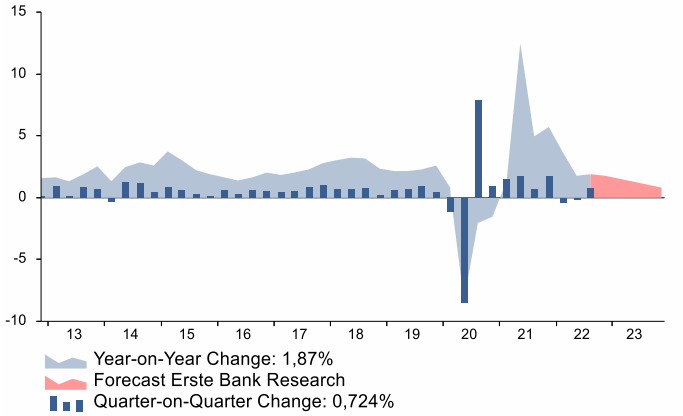
US Economics

Overview

US Real GDP Growth Rate*

as of Q4 22

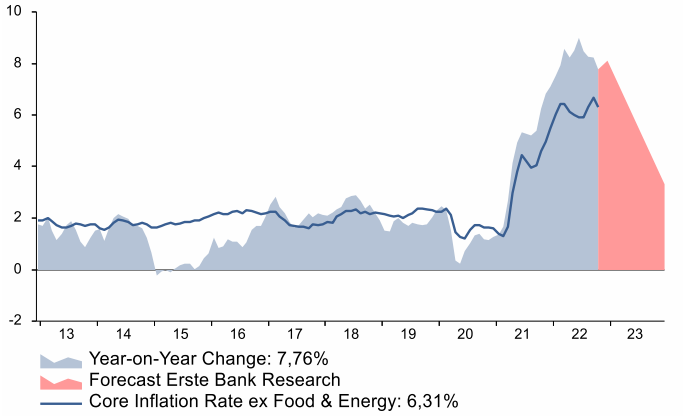


Quelle: Refinitiv Datastream

Private consumption developed surprisingly well in October. However, we only see a short-term flare-up and our outlook remains cautious. Households are and will continue to be confronted with very high inflation and a real estate market that is clearly in a downturn. Support still comes from a very strong labor market. Although the inflation rate should fall significantly in the course of next year, the labor market should cool at the same time, so we do not expect an economic upturn in 2023. Instead, we expect the economy to remain weak.

US Inflation Rate*

as of Okt 22

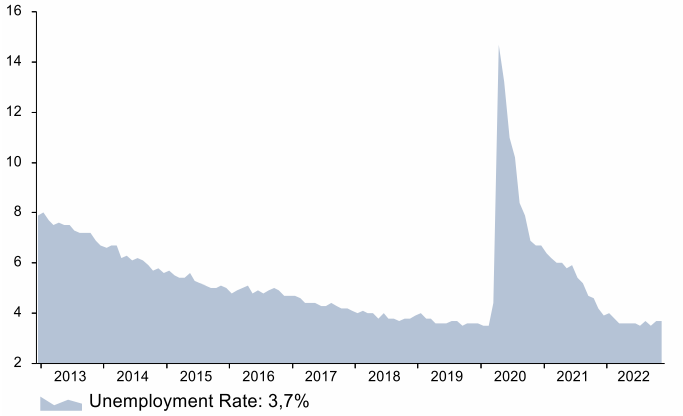


Quelle: Refinitiv Datastream

After a significant decline in inflation in October, we expect a sideways movement for the next two months. Only the January data should show the next noticeable decline, which should then start a trend of declining inflation rates. Due to base effects, energy prices will make no or even a negative contribution from the spring onward, and we expect a similar development for food. The other components are more difficult to assess, but should reflect the economic downturn, especially in the real estate market later in 2023. Overall, we expect inflation to fall significantly in 2023.

US Unemployment Rate

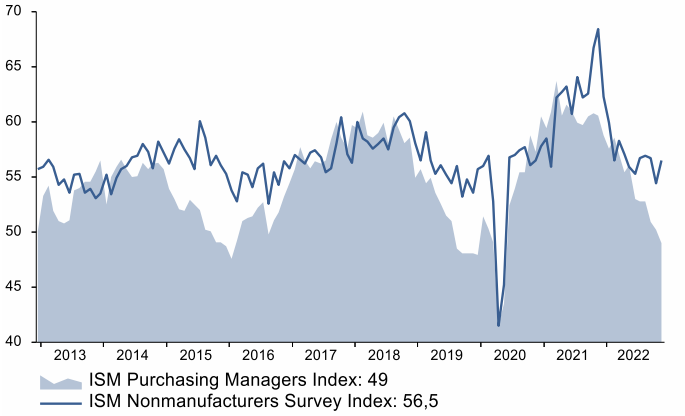
as of Nov 22



Quelle: Refinitiv Datastream

US ISM Purchasing Managers Index

as of Nov 22



Quelle: Refinitiv Datastream

With reference to the graphs (pictured above): forecasts are not a reliable indicator for future performance.
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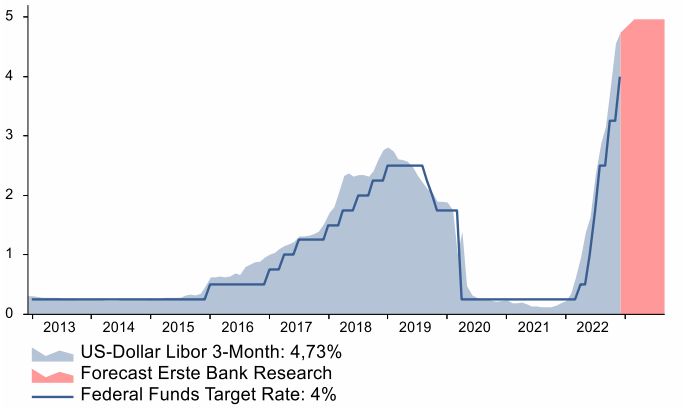
US Fixed Income

Money Market and Government Bonds

Money Market US*

as of 05.12.2022

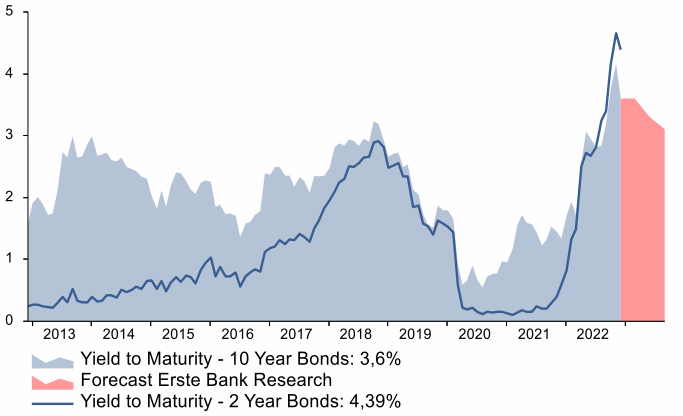


Quelle: Refinitiv Datastream

Recent US inflation data and statements by Fed Chairman Powell suggest a slower approach by the US Federal Reserve in December. After four rate hikes of 75 basis points (bp) each since June, the upcoming rate hike should be 50bp. We expect the end of rate hikes to come in early February with another hike of the same magnitude. The range of the key interest rate should then be just below 5% and, from the central bank's perspective, restrictive enough to bring inflation back to 2%. Risks exist with regard to the speed of the decline in inflation and thus for the exact end of the interest rate hikes.

US Government Bonds*

as of 05.12.2022

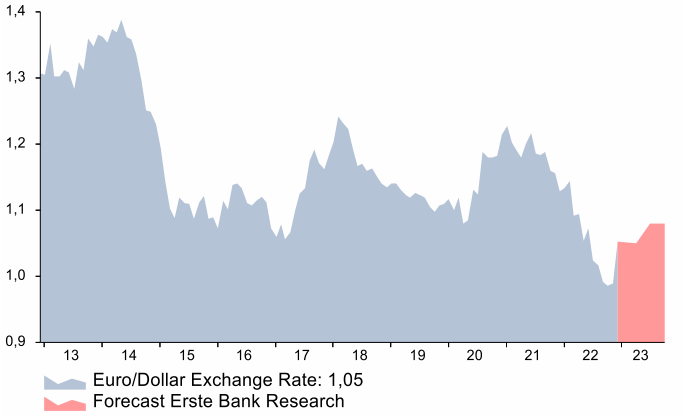


Quelle: Refinitiv Datastream

A number of indications suggesting slower rate hikes and thus making the peak of the interest rate cycle foreseeable led to lower yields on the US bond market. Medium and longer maturities showed the strongest movements. However, we also see in the US that the market has run ahead of macroeconomic developments. While we expect inflation to fall significantly, there are risks to the pace that suggest temporary counter-movements in the market. Thus, overall, we expect a sideways movement in the bond market during the coming months.

Euro-Dollar Exchange Rate*

as of 05.12.2022



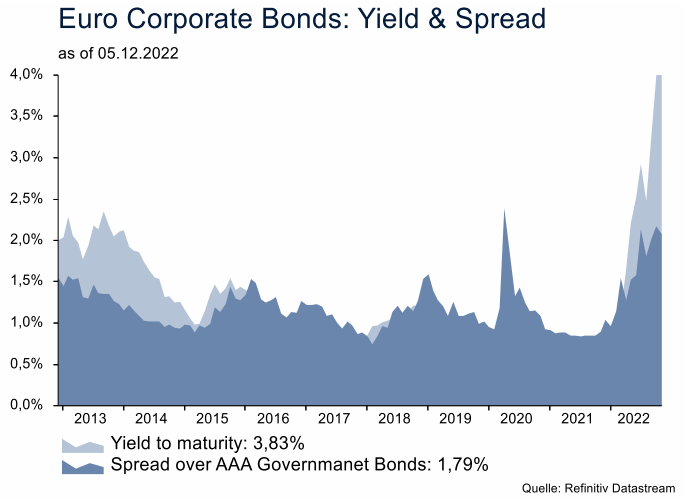
Quelle: Refinitiv Datastream

The dollar weakened significantly during the last few weeks. The reason was the signs of a foreseeable end to US interest rate hikes. Thus, the market ran out of support for the previously very high valuation of the dollar. The movement of the last few weeks took place very quickly and should not continue at this pace in the medium term. During the coming weeks, the price trend could still be quite volatile, since technical indicators still speak in favor of the euro. However, we expect a sideways movement over the coming months, as US interest rates will remain significantly above those in the Eurozone, which should stand in the way of a strong strengthening of the euro.

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..

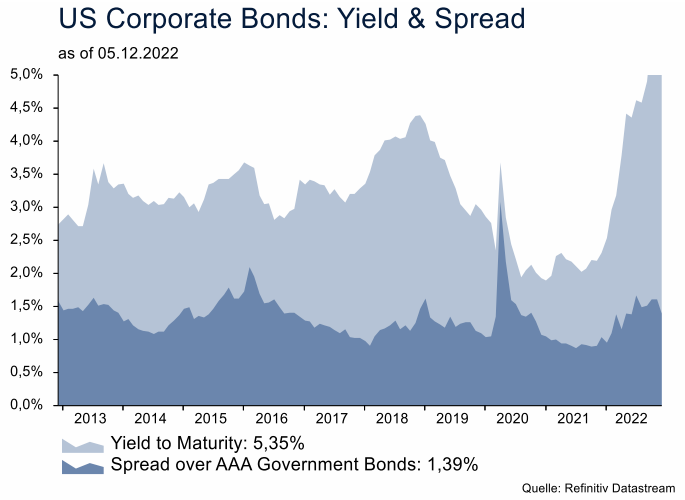
Corporate Bonds

Investment Grade



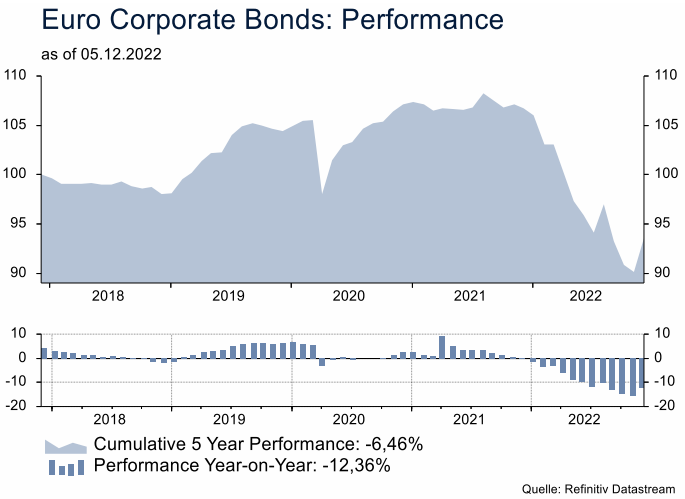
Declining government bond yields and slight spread tightening resulted in a positive performance of IG corporate bonds (+2.9%; HY: +3.7%) in November. A positive driver were the good 3Q results of companies. Gas is slightly increasing in price again. However, a gas shortage should be avoided. As shown by the EZ Purchasing Managers Index, industrial sentiment improved slightly in November. A recession became less likely. Interest rate hikes by the ECB and the Fed in December should be largely priced in. We recommend diversified investments in IG hybrid bonds. They should benefit more than senior bonds from the brightening of the economic outlook.

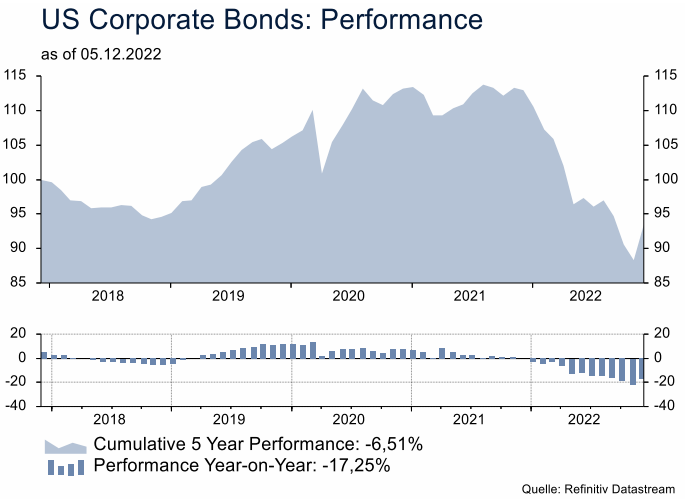
Forecast: somewhat negative



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 early December, this figure had risen to around 4.5%. In addition, there was an increase in the yield premium for credit risk. Since hopes of declining inflation rates began to emerge in mid-October, corporate bonds have shown price increases. Yield premiums for credit risk are also falling again. At 5.4%, the effective yield has already fallen by around 0.75 percentage points since October.

Forecast: neutral





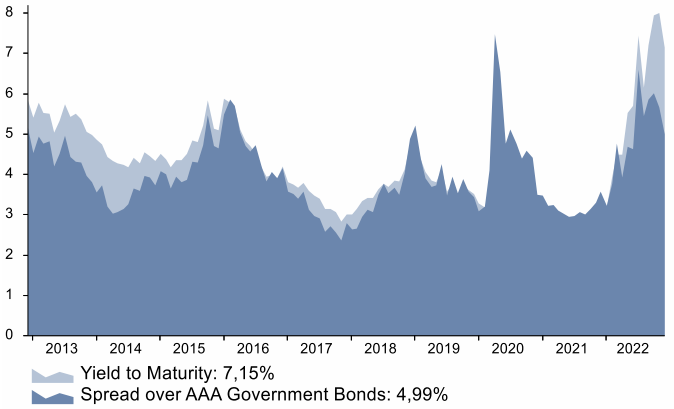
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

High Yield Bonds

Corporate Bonds with a Speculative Rating

Euro High Yield: Yield & Spread

as of 05.12.2022



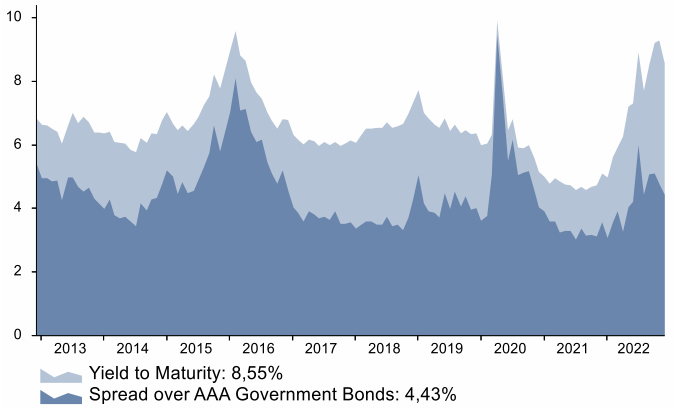
Quelle: Refinitiv Datastream

HY- outperformed IG corporate bonds again in November (HY: +3.7%; IG: +2.9%). The brightening of key leading economic indicators (EZ Purchasing Managers' Index, German ifo Business Climate Index) increased investors' risk appetite and caused risk premiums to decline. Some HY issuers took advantage of this to issue bonds. The coupons are higher than those of the outstanding bonds. Investor demand is high. As very low-rated issuers have only limited refinancing needs in 2023, the weakening of interest coverage ratios and the increase in the default rate should be moderate. We recommend diversified HY investments with a focus on the BB segment.

Forecast: somewhat negative

US High Yield: Yield & Spread

as of 05.12.2022



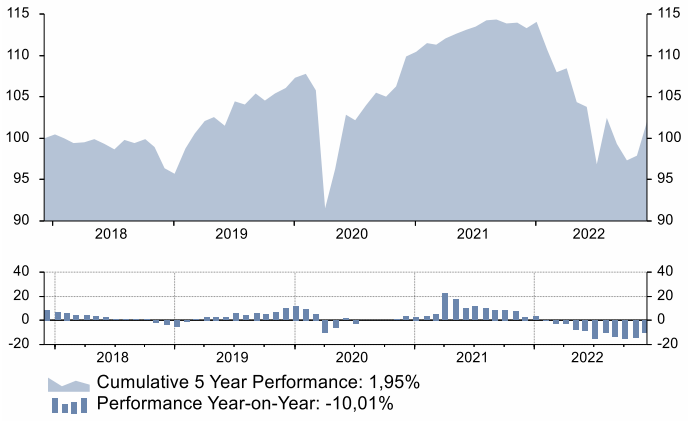
Quelle: Refinitiv Datastream

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 since the beginning of the year are 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 rises. Moreover, there was only a moderate increase in the yield premium for credit risk. Since hopes of declining inflation rates began to emerge in mid-October, high-yield corporate bonds have shown price increases. At 8.5%, the effective yield has already fallen by around a full percentage point since the beginning of October.

Forecast: neutral

Euro-High Yield: Performance

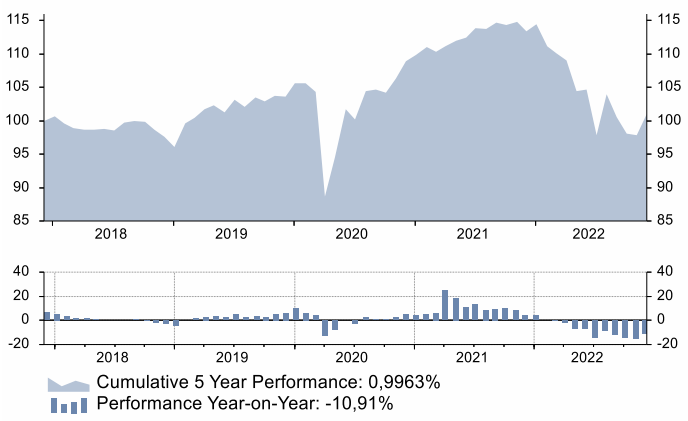
as of 05.12.2022



Quelle: Refinitiv Datastream

US High Yield: Performance

as of 05.12.2022



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

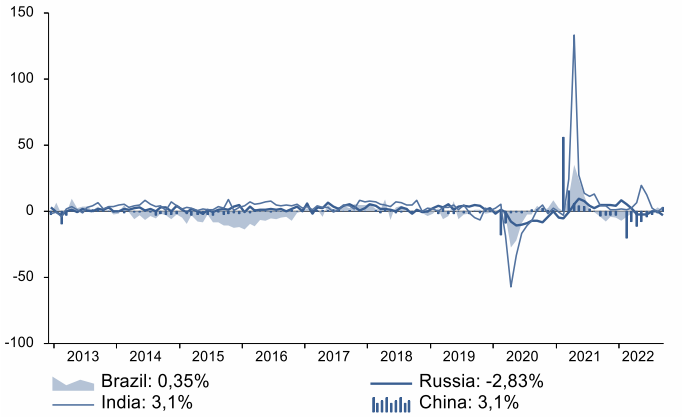
Brazil, Russia, India and China

In contrast to many other countries, the estimate for real economic growth in Brazil has even been revised slightly upward this year (from stagnation to +2.5% pa). Expectations for inflation have also risen only moderately (Q422: from 5% to 6% pa). The key interest rate has been raised sharply from 2% to 13.75% since 2021. This level may represent the peak in this interest rate cycle. Unlike many other currencies, the Brazilian real has strengthened against the USD since the beginning of the year (higher interest rates and commodity prices). Local currency bonds have strengthened, but USD bonds are showing price losses.

The sanctions imposed by the West are hitting the Russian economy hard. GDP is shrinking and supply chains are impaired. However, the GDP slump this year is likely to be less severe than initially assumed (working assumption: -3%). At the same time, capital controls have been introduced. The strengthening of the ruble (increasing trade surplus) has led to a withdrawal of emergency key interest rate hikes (currently: 7.5%). Geopolitics: Relations between the West and Russia have continued to deteriorate (sanctions, gas supply reduction, discussion of oil embargo, attacks on gas pipelines, threat of nuclear weapons, NATO expansion).

Industrial Production BRIC

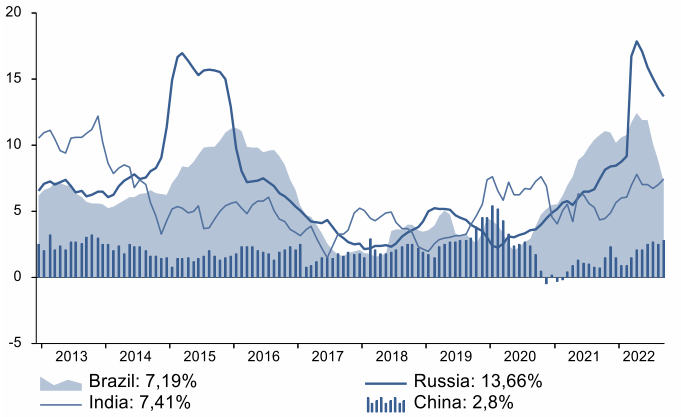
Year-on-Year Change in %, as of Sep 22



Quelle: Refinitiv Datastream

Inflation Rates BRIC

Year-on-Year Change in %, as of Sep 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 (Q4 2022: 6.5% p.a.). The Indian rupee has been in a downtrend since the beginning of the year. The central bank has yielded to the pressure and raised the key interest rate from 4% to a total of 5.9% since May. Of note: The price losses of government bonds between the beginning of the year and mid-June are smaller than the price gains thereafter.

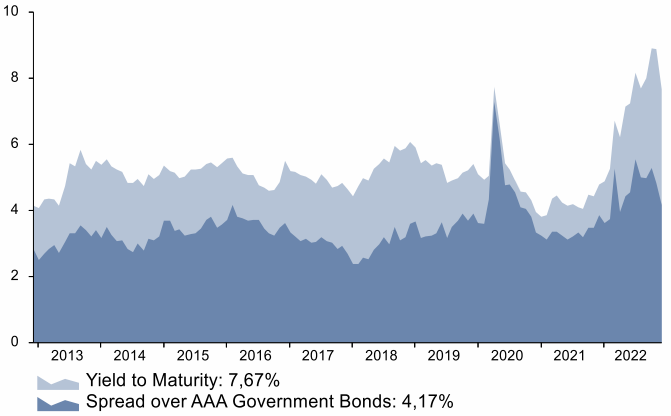
China faces several problems. 1) The zero tolerance policy towards new infections. 2) The real estate crisis. 3) The intensification of tensions between China and the US. 4) The weakening of global demand for goods. Disappointing economic indicators have dampened hopes for a strong economic recovery in H2. Estimates for real GDP growth are 3% in 2022. Numerous targeted economic support measures have been announced by the official side. Government bonds have shown price increases since the beginning of the year (in local currency). The currency remains exposed to weakening pressure against the US dollar, and since October also against the EUR.

Emerging Market Bonds in Euro

Hedged in EUR

Emerging Market Bonds in Hard Currency

Yield & Spread, as of 05.12.2022



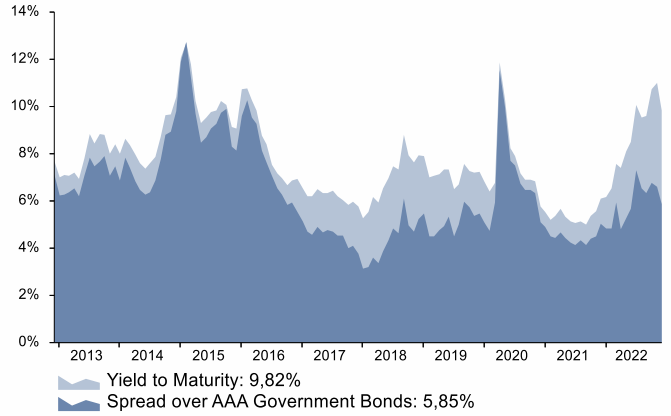
Quelle: Refinitiv Datastream

Negative return trend since the beginning of the year. The determining factor for this was the sharp rise in yields on U.S. government bonds. In addition, there was an increase in the yield spread for credit risk. The financial environment remains unfriendly. Firm U.S. dollar, U.S. rate hikes, increased inflationary pressures means rate hikes in numerous countries, disappointing growth indicators in China, increased recession risks. Higher commodity prices have mixed impact: Negative for importers, support for exporters. Bonds have been showing price increases since hopes of declining inflation rates began to emerge in mid-October. The weakening of USD vs. EM currencies since mid-October also helps.

Forecast: neutral

Emerging Corporates in Hard Currency

Yield & Spread, as of 05.12.2022



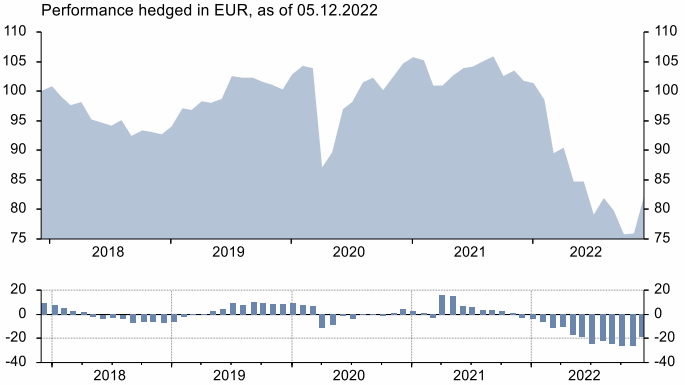
Quelle: Refinitiv Datastream

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 zero-tolerance policy. Additional economic support measures announced in response. 3) At least spread widening in response to Ukraine invasion was only moderate. The financial environment remains unfriendly: inflation and growth risks, key interest rate hikes, firm U.S. dollar. Bonds have been showing price increases since hopes of declining inflation rates began to emerge in mid-October. The weakening of the USD vs. EM currencies since mid-October also helps.

Forecast: neutral

Emerging Market Bonds in Hard Currency

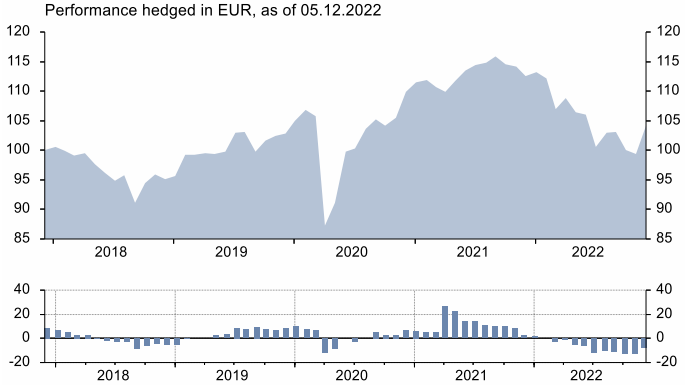
Performance hedged in EUR, as of 05.12.2022



Quelle: Refinitiv Datastream

Emerging Corporates in Hard Currency

Performance hedged in EUR, as of 05.12.2022



Quelle: Refinitiv Datastream

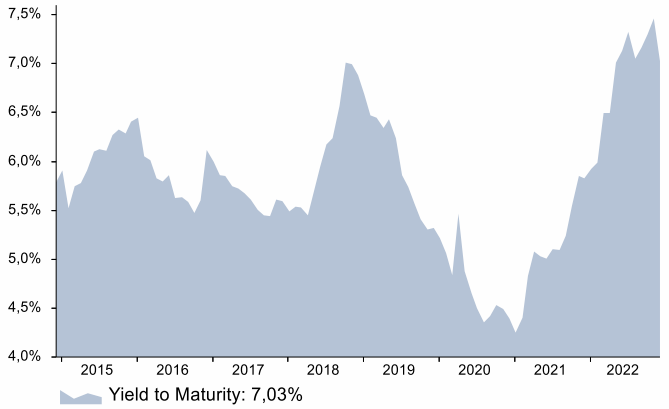
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Emerging Market Bonds in Local Currency

Global and Central Europe

Emerging Market Bonds in Local Currency

Yield to Maturity, as of 05.12.2022



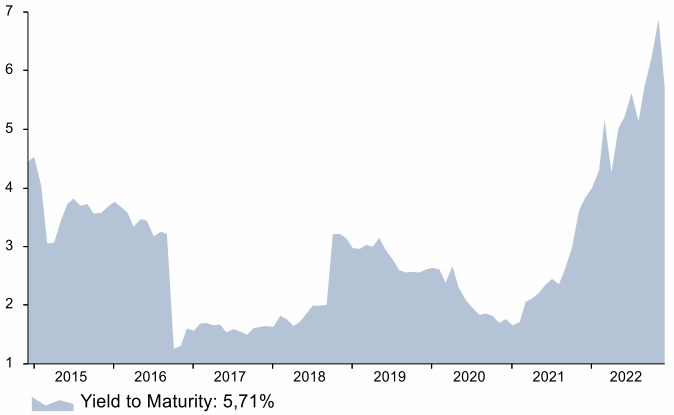
Quelle: Refinitiv Datastream

Numerous central banks have raised key interest rates since the beginning of 2021 due to increasing inflation risks (in aggregate: from 3% to 4.75%). The aim was to contain a pass-through from high inflation rates to inflation expectations and to stabilize the currency. For this reason, yields on local currency bonds trended upward between early 2021 and mid-October 2022 (high: around 7.5%). In the meantime, there are signs that the cycle of interest rate hikes is coming to an end. Already since the beginning of the second half of the year, the bond class has shown price gains (in local currency). Negative: The EM currency basket has shown a weakening trend against the US dollar since the beginning of 2011. The weakening of the USD vs. EM currencies has not helped because the EUR vs. USD has also strengthened.

Forecast: somewhat positive

CEE Government Bonds in Local Currency

Yield to Maturity,as of 05.12.2022



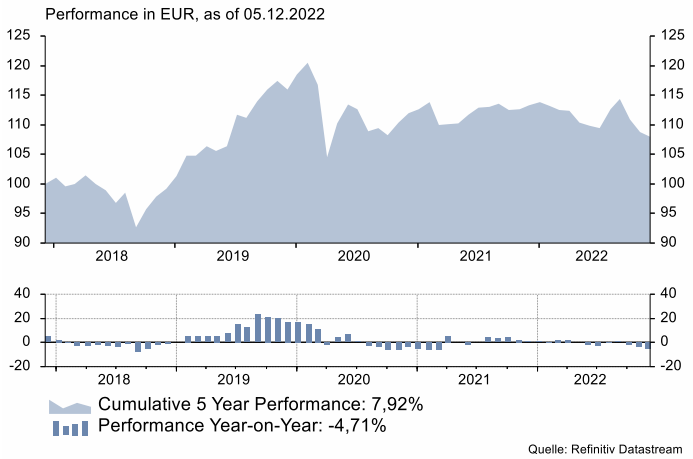
Quelle: Refinitiv Datastream

Several spheres of influence dampen economic activity. 1) High inflation rates and high energy prices. 2) Strong increases in key interest rates. 3) Increased yields have tightened the financial environment. Working assumption: "Downturn" scenario. However, in case of supply disruptions for energy, risks for recession would increase. Central banks were / are under pressure for key rate hikes (Czech Republic: 7%, Hungary: 13%, Poland: 6.75%, Romania, 6.25%). In the meantime, there are signs that the rate hike cycle is coming to an end. Yield curves in Poland, the Czech Republic and Hungary are already pricing in key rate cuts. Some currencies are exposed to weakening pressure (RON & HUF, also due to high current account deficits).

Forecast: neutral

EM Government Bonds in Local Currency

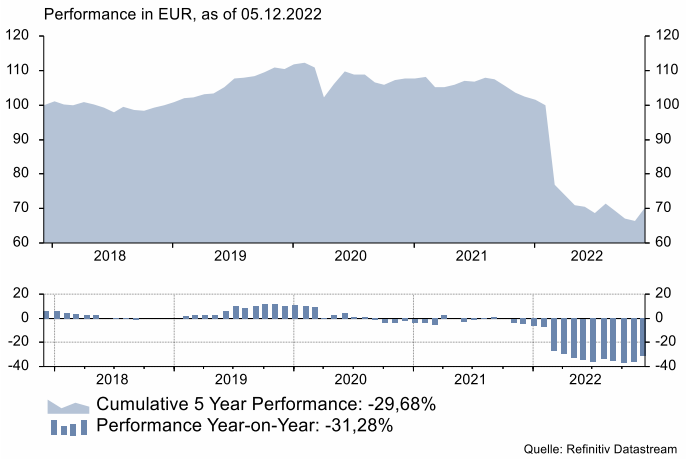
Performance in EUR, as of 05.12.2022



Quelle: Refinitiv Datastream

CEE Government Bonds in Local Currency

Performance in EUR, as of 05.12.2022



Quelle: Refinitiv Datastream

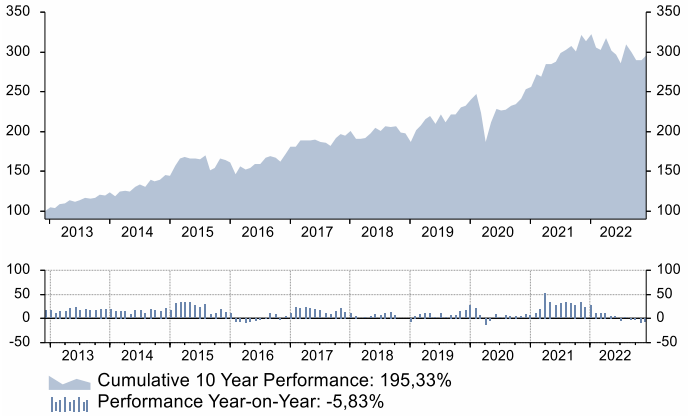
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Equities Developed Markets

Overview

Developed Markets

Performance in EUR, as of 05.12.2022



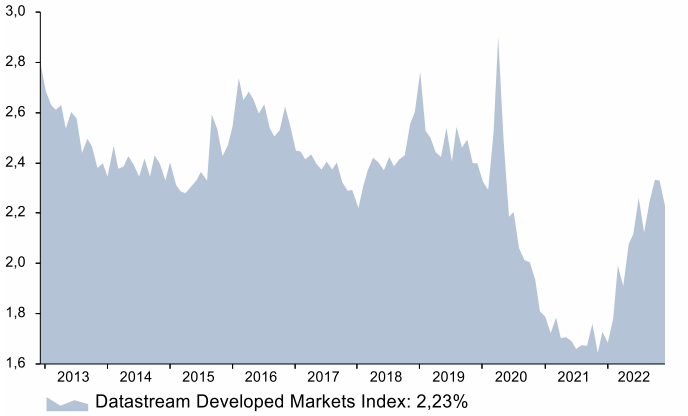
Quelle: Refinitiv Datastream

The falling dollar index and volatility favored the recovery of the global equity market index in November. It subsequently rose by +2.4% in EUR terms. Forecasts for sales and earnings growth of the companies in the global equity index improved slightly in November for 2023. Sales should increase +2.0% (y/y) in 2023 and profits should remain stable (2023e: +0.5% y/y). The expected operating margin should be 17% next year and remain at the 2022 level. With an expected 2023e P/E ratio of 15.1x, the valuation of the global equity market appears reasonable. We expect the global equity market index to rise slightly in December.

Forecast: neutral

Dividend Yield

as of 05.12.2022

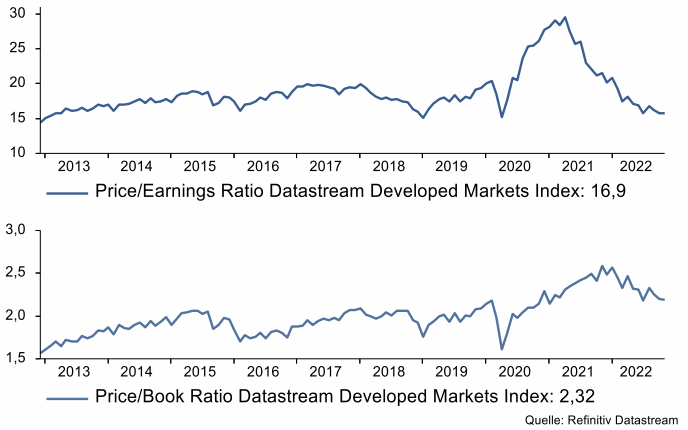


Quelle: Refinitiv Datastream

In the 3Q reporting season, 73% of US companies reported positive earnings surprises. Earnings growth was +2.2% (y/y) in 3Q. It was below the long-term average. For 4Q, profits are expected to decline by -2.2% (y/y). Positive profit growth rates should only be achieved again from 1Q. For 2023 as a whole, the consensus expectation is a +3.1% (y/y) increase in sales and a +3.8% (y/y) rise in profits. In Europe, 60% of companies reported positive earnings surprises for 3Q. This was most common in the financials, materials, and technology sectors. Earnings growth for European firms was +35.0% (y/y) in 3Q. From 4Q, earnings growth rates will slow down. For 2023, the consensus forecasts a -5.9% (y/y) decline in profits for European companies.

Key Indicators

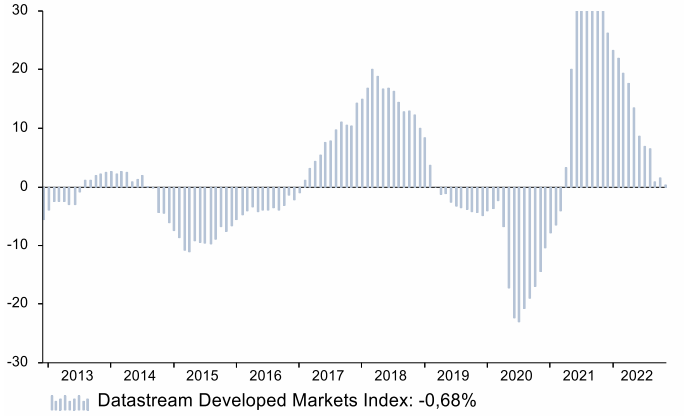
as of 05.12.2022



Quelle: Refinitiv Datastream

Earnings Growth

Earnings Expectation per Share: Year-on-Year Change, as of 05.12.2022



Quelle: Refinitiv Datastream

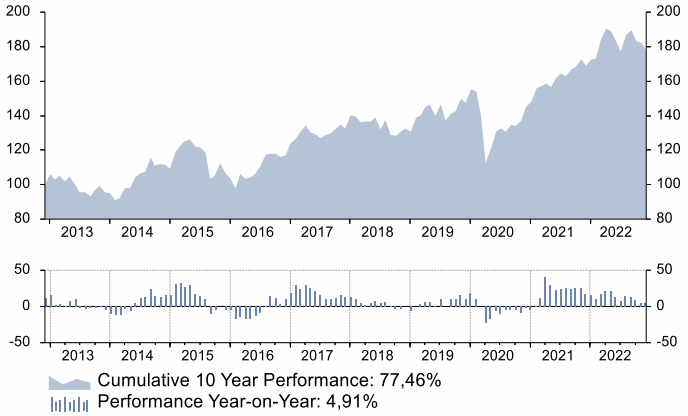
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Equities Emerging Markets

Overview

Emerging Markets

Performance in EUR, as of 05.12.2022



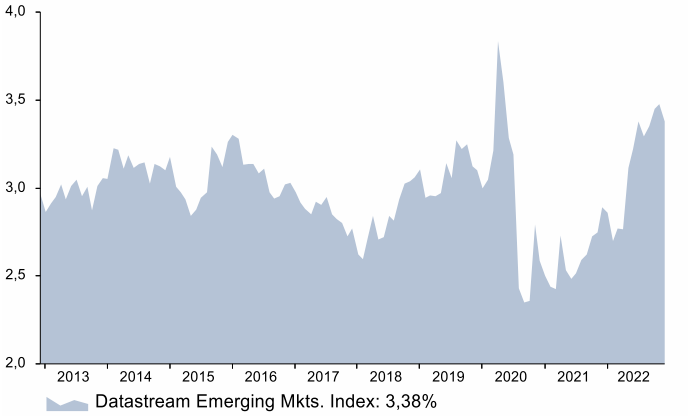
Quelle: Refinitiv Datastream

The global Emerging markets index rose by +9.9% in EUR terms in November. The performances of the individual country indices varied widely. The Chinese stock market gained +7.5% in EUR after a slight easing of the strict Covid-19 measures. The Indian equity market also posted a positive performance (in EUR: +1.5%). In contrast, the Brazilian equity market declined by -8.5% in EUR terms. For the companies of the global Emerging market index, earnings are expected to increase by +1.0% (y/y) in 2022. Next year, a profit growth rate of +6.4% (y/y) should be achieved. Accordingly, the medium-term outlook is positive. We expect the Emerging Market Index to rise slightly in December.

Forecast: neutral

Dividend Yield

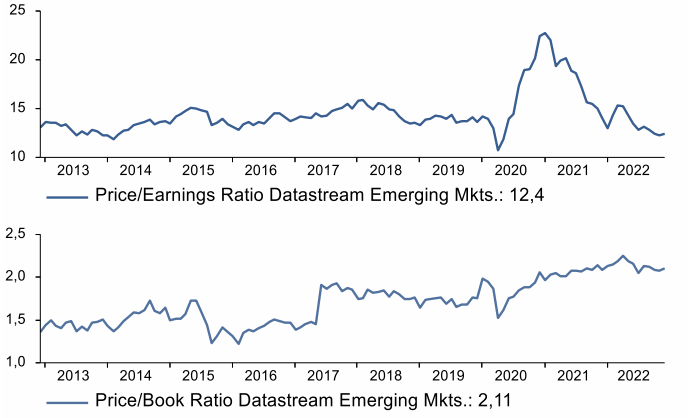
as of 05.12.2022



Quelle: Refinitiv Datastream

Key Indicators

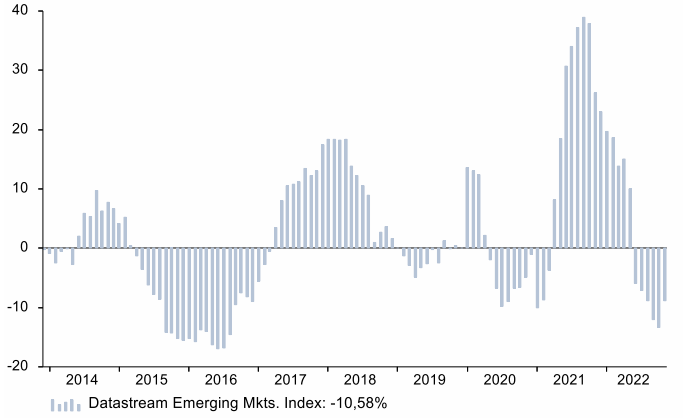
as of 05.12.2022



Quelle: Refinitiv Datastream

Earnings Growth

Earnings Expectation per Share: Year-on-Year Change, as of 05.12.2022



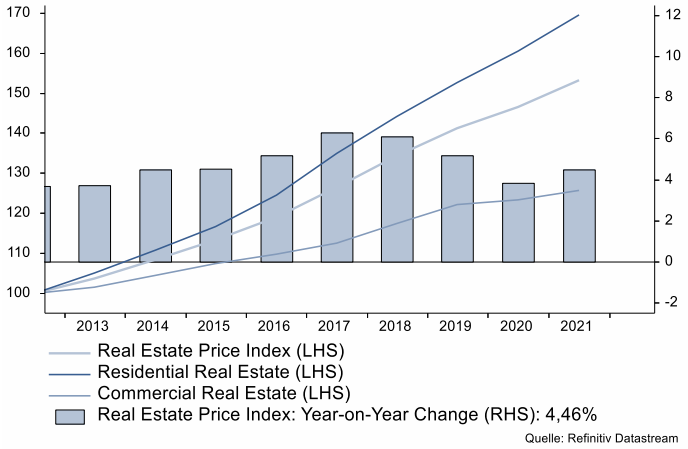
Quelle: Refinitiv Datastream

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

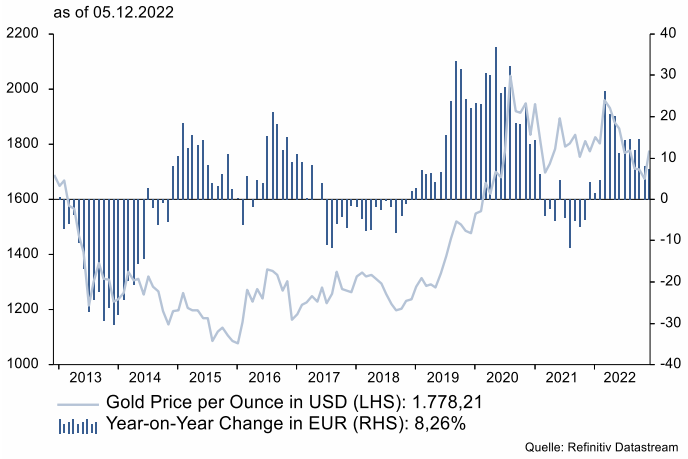


Quelle: Refinitiv Datastream

The transaction volume in the German residential real estate sector fell significantly in the third quarter of 2022. Higher financing costs make it harder to close. At the same time, falling real wages and rising construction costs are having a negative impact on new construction activity and the demand for new living space. Overall, the environment is causing a significant dampening, but probably not a slump, since the population development is likely to ensure increasing demand in the medium and long term. Another trend that will lead to price differentiation could lie in the energy efficiency of properties: the more efficient, the higher prices will probably be enforceable.

Forecast: neutral

Gold

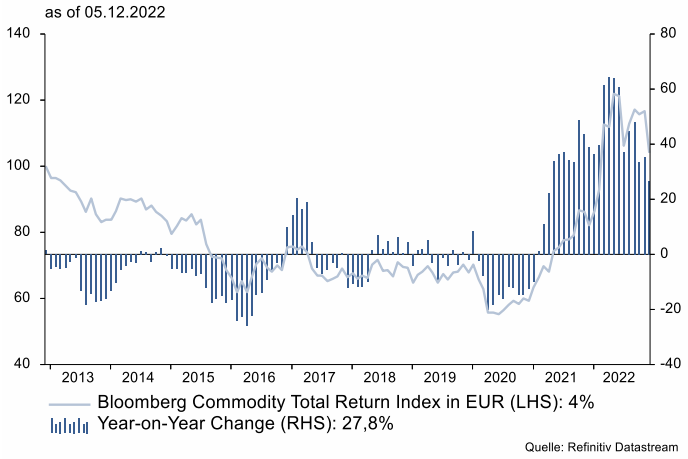


Quelle: Refinitiv Datastream

The gold price increased by +3.8% in EUR in November. The performance since the beginning of the year in EUR amounts to +6.7%. Gold has thus outperformed the asset classes bonds and equities this year. To fight inflation, the Fed will still raise interest rates this year. Nevertheless, real U.S. yields remain in negative territory. This is a factor that supports a positive gold price trend. However, real yields in the U.S. are now less negative than in previous months. Little should change in this situation for the time being. We expect the gold price to move sideways in December.

Forecast: somewhat positive

Commodities



Quelle: Refinitiv Datastream

Crude oil prices showed an upward trend until mid-June. Since then, prices have fallen somewhat (below $90 per barrel). Energy prices show a similar trend at global level. The reduction in gas supplies from Russia to Europe led to a significant increase in gas prices in Europe until August. Since then, the trend has been downward. In contrast to energy prices, industrial metals prices are below early 2022 levels, which can be explained by weak demand from China and the downward trend in global manufacturing indicators. However, because inventories are low, the vulnerability to significant price increases remains elevated.

Forecast: neutral

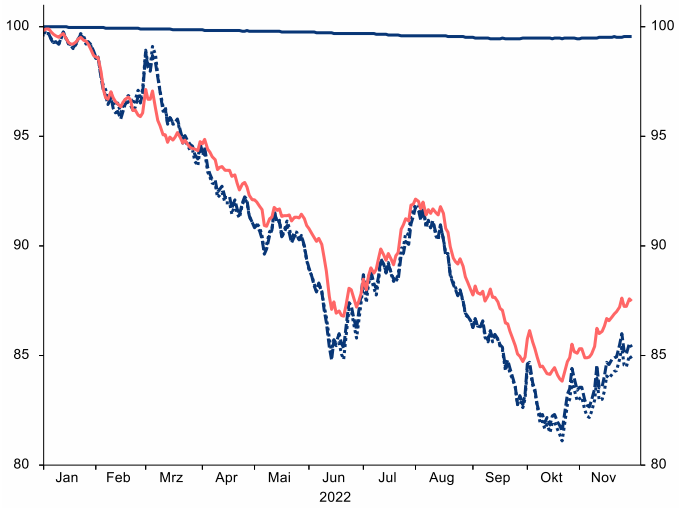
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. Please refer to the annex for the underlying index.

Overview of Key Asset Classes

YTD Performance

Fixed Income Investment Grade

Performance YTD as of 30.11.2022



Euro Money Market: -0,46%
Euro Government Bonds AAA-AA: -15,13%
Euro Government Bonds Investment Grade: -14,61%
Euro Corporates Investment Grade: -12,53%

Quelle: Refinitiv Datastream

Equities

Performance YTD as of 30.11.2022

Equities Europe: -8,37%
Equities North America: -5,41%
Equities Japan: -9,64%
Equities Emerging Markets: 6,79%

Quelle: Refinitiv Datastream

Fixed Income High Yield

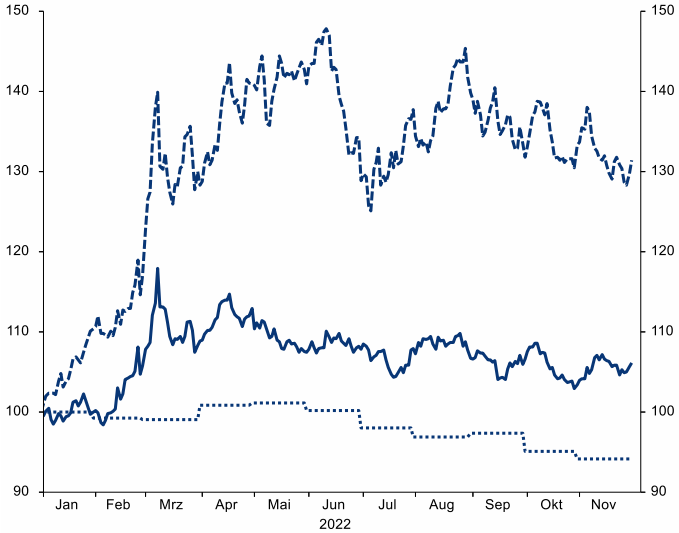
Performance YTD as of 30.11.2022

Euro High Yield: -10,82%
Emerging Market Bonds in Hard Currency: -20,47%
Emerging Market Bonds in Local Currency: -4,06%
CEE Government Bonds in Local Currency: -30,81%

Quelle: Refinitiv Datastream

Alternative Investments

Performance YTD as of 30.11.2022



Gold in EUR: 6,18%
Hedge Fund Index: -5,81%
Commodity Index: 31,44%

Quelle: Refinitiv Datastream

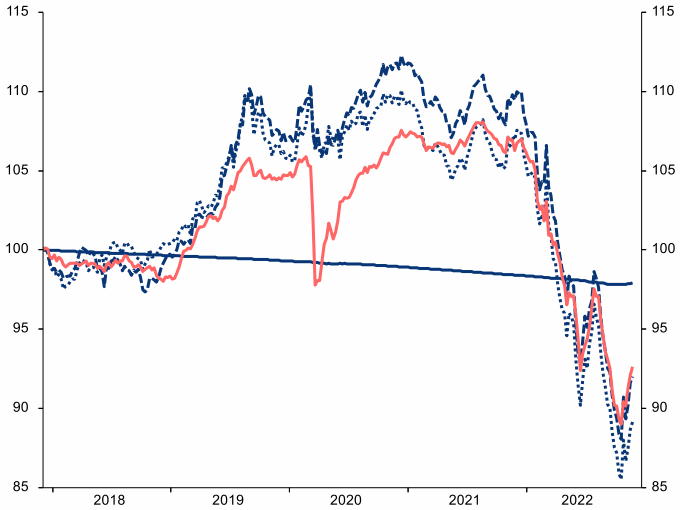
With reference to the performance graphs: past performance is not a reliable indicator of future peformance. This performance representation has little validity due to its short duration. Please refer to the annex for the underlying index.

Overview of Key Asset Classes

5 Year Performance

Fixed Income Investment Grade

5 Year Performance as of 30.11.2022



Euro Money Market: -2,08%
Euro Government Bonds AAA-AA: -10,52%
Euro Government Bonds Investment Grade: -7,77%
Euro Corporates Investment Grade: -7,13%

Quelle: Refinitiv Datastream

Equities

5 Year Performance as of 30.11.2022

Equities Europe: 32,47%
Equities North America: 85,40%
Equities Japan: 12,95%
Equities Emerging Markets: 38,79%

Quelle: Refinitiv Datastream

Fixed Income High Yield

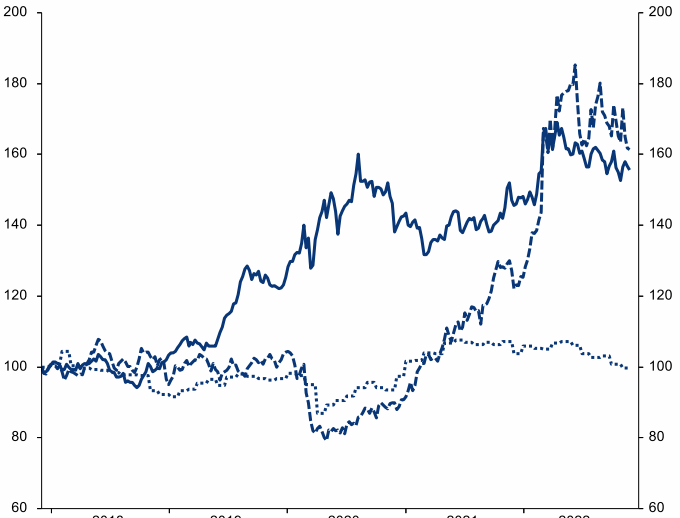
5 Year Performance as of 30.11.2022

Euro High Yield: 1,48%
Emerging Market Bonds in Hard Currency: -18,64%
Emerging Market Bonds in Local Currency: 10,05%
CEE Government Bonds in Local Currency: -29,79%

Quelle: Refinitiv Datastream

Alternative Investments

5 Year Performance as of 30.11.2022



Gold in EUR: 57,37%
Hedge Fund Index: -0,20%
Commodity Index: 64,74%

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.

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As of December 2022

Imprint

Editorial office
Erste Bank der oesterreichischen Sparkassen AG
Business Support S&B
Am Belvedere 1, 1100 Wien