

# GOAL: Flash-update

Portfolio Strategy Research

## Upgrading equities

### What's changed

We upgrade equities to overweight over 3 months, in line with our 12-month view. We have rolled our index targets forward to higher levels for all regions except Japan and, following the dovish ECB decisions yesterday, we now see the risk to equities from higher bond yields as less imminent. We maintain a high conviction that yields will rise from here, but since our last GOAL, risks have clearly shifted in the direction of a slower path. Today we re-iterated our yield forecast for the US, UK and Japan and lowered our year-end Bund forecast from 1.60% to 1.30%

### Our recommended asset allocation

**Equities:** We are overweight over both 3 and 12 months. We expect earnings growth, dividends, and high risk premia to support returns.

**Commodities:** We are neutral over both 3 and 12 months but expect significant dispersion below the index level. We like nickel, palladium, zinc and aluminium, but see downside for copper and gold. Roll carry is likely to contribute significantly to returns, especially for oil, copper and aluminium.

**Corporate credit:** We remain underweight over both 3 and 12 months. We expect spreads to narrow, but given already tight levels, rising government bond yields are likely to dominate the returns, especially for US IG credit. The exception is US HY, and within credit we would recommend an overweight in HY relative to IG.

**Government bonds:** We remain underweight. We expect yields to rise due to sustained high US growth and accelerating inflation, a decline in deflation concerns in Europe, and support to inflation expectations from ECB policy action.

### Expected returns and recommended asset allocation

New Recommendation					
3-Month Horizon			12-Month Horizon		
Asset Class	Return*	Weight	Asset Class	Return*	Weight
Equities	3.3 %	OW	Equities	12.0 %	OW
Cash	0.0	N	Cash	0.5	N
Commodities	2.5	N	Commodities	1.5	N
5 yr. Corporate Bonds	-1.1	UW	5 yr. Corporate Bonds	-0.9	UW
10 yr. Gov. Bonds	-3.5	UW	10 yr. Gov. Bonds	-5.4	UW

\* Return forecasts assume full currency hedging

Source: Goldman Sachs Global Investment Research.

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## What's new?

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### In Summary

**This week, we have rolled forward our equity targets for the US, Europe and Asia ex-Japan to higher levels. We have also lowered our forecast for German Bunds from 1.60% to 1.30% by year-end. We upgrade equities to overweight over 3 months and, within corporate credit, we emphasize an overweight in high yield relative to investment grade from a total return perspective. We balance the upgrade of equities with a downgrade of cash to neutral over 3 months.**

### Our view on bonds

Yesterday's ECB decisions were more dovish than expected. On the back of this new information, our bond strategists have today lowered their year-end forecast for German bunds to 1.30% while re-iterating their existing year-end forecasts for the US, the UK and Japan. We maintain a high conviction that yields will rise from here, but since our last GOAL, risks have clearly shifted in the direction of a slower path.

### Still UW credit

In our last GOAL, we downgraded equities to neutral over 3 months and corporate credit to underweight over both 3 and 12 months. In the case of equities, we were concerned about the risk from a rise in bond yields and, to a lesser extent, geopolitical risks that had to be held up against our longer-term very constructive outlook. In corporate credit, we were still constructive on spreads, but this constructive view had to be held up against the losses we expect on the government bond component of the total return. Even with bond risks somewhat lower they still dominate the spread return for IG credit, and we remain underweight corporate credit. For high yield on the other hand, the spread return has the potential to offset any loss on the bond component of the total return. Therefore, on a total return basis, we have a clear preference for HY over IG.

### Upgrading equities

For equities, our longer-term view is very positive. We expect solid returns for all the major regions, driven mainly by earnings growth and dividends. Reflecting this longer-term view and the passage of time, this week we rolled our equity targets to higher numbers in both the US, Europe and Asia ex-Japan. Given this and the somewhat lower risk we see from bonds, we upgrade equities to overweight over 3 months, in line with our 12-month allocation. The ECB policy action reflects a weaker growth and inflation outlook for the Euro area, which is also a drag on equities. However, we think much of this is already reflected in the data and, on balance, we think the net effect of the policy action from here will be positive for equity markets.

### Regional changes

Over 12 months, we maintain our current regional allocations within equities: overweight Europe and Japan; neutral Asia ex-Japan; and underweight the US. We have less conviction in our regional allocations over 3 months but, on balance, we downgrade Japan to underweight after a strong run in recent months and given current macro headwinds. Longer term, for Japan, we still believe in the ability of reforms to drive profit and performance and that, together with an attractive valuation, is reflected in our overweight stance over 12 months. We upgrade Asia ex-Japan to overweight over 3 months and expect support from the Shanghai-Hong Kong stock connect theme as well as our generally more positive view on EM assets (for details see *China Strategy report: SH-HK Connect: New regime, unprecedented opportunity*, September 1 and *Emerging Markets Weekly (14/28): Tactically positive EM risk*, September 4). We upgrade the US to neutral reflecting the current robust US growth environment. Finally, we maintain our overweight in Europe.

### GOAL flash update

The GOAL Flash-update is a new addition to our GOAL product. We intend to use this very shortened version of the GOAL to comment on events and adjust our allocations with a faster turnaround time. We will follow up this piece with our regular GOAL update next week, providing more in-depth commentary on our new allocations.

# Our forecasts

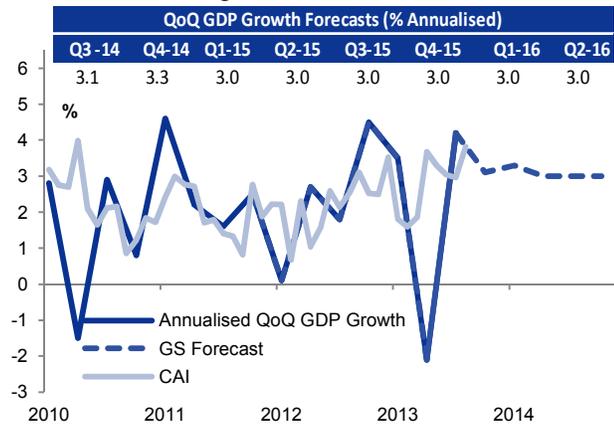
## Exhibit 1: Our forecasts across asset classes

	Return in % over last			Current Level	Forecasts			Unit
	12 m	3 m	1 m		3 m	6 m	12 m	
<b>Equities</b>								
S&P 500 (\$)	23.4	4.1	3.3	1998	2050	2075	2150	Index
Stoxx Europe 600 (€)	19.2	2.1	5.6	349	365	375	390	Index
MSCI Asia-Pacific Ex-Japan (\$)	20.2	7.0	2.3	515	530	540	555	Index
Topix (¥)	14.3	5.3	1.6	1296	1250	1300	1450	Index
<b>10 Year Government Bond Yields</b>								
US	6.5	1.6	0.3	2.40	3.00	3.13	3.38	%
Germany	10.4	3.8	1.4	0.94	1.30	1.40	1.65	%
UK	5.3	2.6	1.3	2.45	3.00	3.06	3.19	%
Japan	3.4	0.9	0.2	0.54	0.75	0.82	0.94	%
<b>5 year credit spreads*</b>								
iBoxx USD	9.0	1.6	0.6	81	73	71	70	Bp
BAML HY Master Index II	10.3	0.7	1.7	385	332	325	320	Bp
iBoxx EUR	8.6	2.5	1.2	103	99	97	95	Bp
<b>Commodities</b>								
WTI	-7.3	-6.0	-3.1	94	96.00	95.00	90.00	\$/bbl
Brent	-5.4	-4.7	-3.9	102	105.00	105.00	100.00	\$/bbl
Nymex Nat. Gas	-5.4	-15.5	-1.3	3.82	4.25	4.25	4.25	\$/mmBtu
Copper	-1.9	2.3	-2.7	6930	6600	6600	6200	\$/mt
Aluminium	9.0	13.4	3.5	2105	2000	2050	2100	\$/mt
Gold	-9.1	1.7	-1.7	1267	1195	1135	1050	\$/troy oz
Wheat	-23.5	-18.0	-5.8	530	560	575	575	Cent/bu
Soybeans	-6.9	-18.1	-7.1	1003	1050	1050	1050	Cent/bu
Corn	-26.2	-21.0	-5.6	336	400	400	400	Cent/bu
<b>FX</b>								
EUR/USD	-2.2	-5.1	-3.6	1.31	1.29	1.25	1.20	
USD/JPY	5.6	2.5	2.7	105	103	107	110	

\* We show performance for credit in total return terms, but current level and forecasts are for spreads

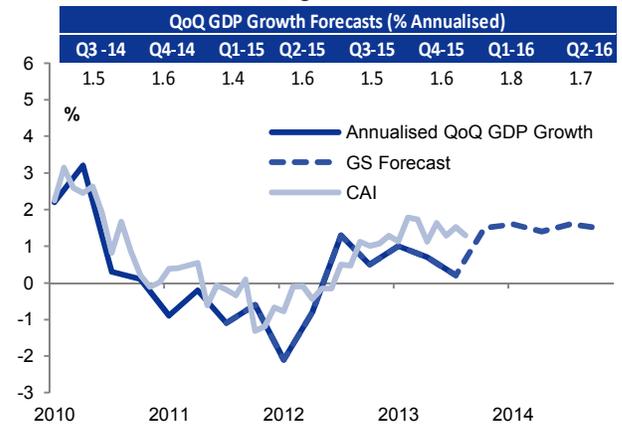
Source: Goldman Sachs Global Investment Research.

## Exhibit 2: US GDP growth vs. our CAI



Source: Goldman Sachs Global Investment Research.

## Exhibit 3: Euro area GDP growth vs. our CAI



Source: Goldman Sachs Global Investment Research.

## Exhibit 4: Our forecasts for economic growth vs. consensus

% yoy	2012	2013	2014E		2015E		2016E		2017E	
			GS	Consensus*	GS	GS	GS	GS		
USA	2.3	2.2	2.1	2.1	3.1	3.0	3.0	3.0	3.0	3.0
Japan	1.5	1.5	1.1	1.5	1.2	1.5	1.5	1.5	1.5	1.5
Euro Area	-0.6	-0.4	0.8	1.0	1.4	1.7	1.7	1.7	1.6	1.6
China	7.7	7.7	7.3	7.4	7.6	7.6	7.6	7.6	7.4	7.4
BRICs	5.9	5.9	5.4	5.5	6.1	6.7	6.7	6.7	6.7	6.7
Advanced Economies	1.2	1.4	1.9	1.9	2.5	2.5	2.5	2.5	2.5	2.5
World	3.0	3.0	3.1	3.1	3.7	4.1	4.1	4.1	4.1	4.1

\* Consensus Economics September 2014

Source: Consensus Economics, Goldman Sachs Global Investment Research.

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