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North America edition

Global investment strategy

Stronger USD and preference for equities over bonds

page 10

Editorial

Michael Strobaek
Global Chief Investment Officer

Giles Keating
Head of Research and Deputy Global CIO

August has been somewhat of a wake-up call for investors, in particular in fixed income. Ten-year yields are below 1% in Germany, 0.5% in Switzerland, and 2.7% in Italy, and also fell in the USA. What is going on? This was not supposed to happen in a world where most investors expect nominal growth to accelerate in H2. We believe the main driver has been soft Eurozone economic data combined with a sense that the Fed may use the benign US inflation outlook to go slow on rate hikes even if growth strengthens somewhat. On top of this, geopolitical tensions in Russia, Iraq, and Gaza intensified into early August. So now what? We believe that long rates are near their range-bottom and will tend to edge up, helped by a modest rebound in global growth. However, the rises may be smaller than previously anticipated. For example, the US 10-year yield may not reach 3% this year. Meanwhile, we believe that nothing much has changed fundamentally for the medium-term equities outlook, which we still see as positive. Yet, we do not consider the recent correction in equities to be sufficient for us to buy more. For that, we would want better entry levels. Meanwhile, bond markets are, in our view, underestimating the strength of the economic expansion. As our growth forecasts materialize, bonds should come under pressure. For our asset allocation, that also means that we continue to dislike bonds and prefer equities. It really is that simple. A final note as we look to the second half of this year. We have updated and refreshed our "Top investment ideas," adding "Techs in focus" and "Sustainability." We encourage you to consult the pages in this Investment Monthly for more details, which should help you find added sources of return in markets that seem increasingly challenging.

In this issue

Editorial deadline: 27 August 2014

North America investment strategy

Don't give up on the yield enhancers

- Equities have been overlooked as an asset class to generate income.
- We look at three yield-enhancing strategies: covered calls, preferred REITs, and MLPs.

Barbara M Reinhard
CIO – Americas

Dave El Helou

A question we often hear from market participants is: "Where are the opportunities to find yield in an income-starved world?" While it is easy to turn to the classic fixed income investments for yield – high yield bonds, senior loans, and corporate bonds – we think these have already received the lion's share of attention this year, as over USD 113 billion in assets have flowed into fixed income, substantially more than the just-under USD 72 billion that have flowed into global equities. It appears that equities, this year, have been overlooked. We find some compelling opportunities to boost yield through covered call strategies, preferred REITs, and Master Limited Partnerships (MLPs).

Covered calls

A covered call strategy involves taking a long equity position, while writing short-dated calls on the underlying exposure to generate additional income. This strategy provides a way to gain equity market exposure, while increasing income and managing downside risk.

To analyze a potential covered call strategy, we looked at the CBOE S&P 500 BuyWrite (BXM) Index, a proxy for a hypothetical covered call strategy. This index is calculated by buying the S&P 500 Index and writing slightly out-of-the-money near-term call options in tandem. The premium collected is added to the value of the index. While, historically, this strategy has had marginally lower returns than a long-only approach to the S&P 500 Index, it has had higher risk-adjusted returns, with almost 30% less volatility than the S&P 500 Index. This strategy may also be of interest to investors concerned about downside risk as, over the last 20 years, the BXM Index has on average only captured 54% of the downside of the S&P 500 Index.

Preferred REITs

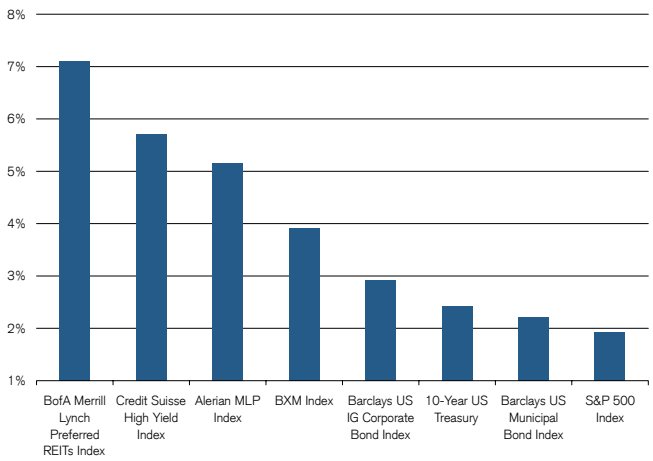
Real Estate Investment Trusts (REITs) are big issuers of preferred stocks. Most preferred REITs have fixed coupons that are either cumulative, meaning the dividend accrues if they have been suspended, or non-cumulative, which means they do not accrue dividends. Currently, the dividend yield on preferred REITs is 7% on average, and the securities have been trading at par value. What we have found to be impressive is the price discipline that has been exhibited this year, as the relatively high yield has not become overpriced and chased by market participants. We view preferred REITs as good quality collateral at reasonable value.

MLPs

MLPs are publicly traded limited partnerships, which generate most of their cash flows through the ownership of pipelines, storage tanks, and energy infrastructure assets. They have been the darlings of the US equity markets, gaining 18% year-to-date, with a yield of 5.2%. While that performance has been impressive, we think MLPs are still in the early stages of the long-term trend toward developing energy infrastructure across North America. We see more growth opportunities for the sector, with the American Gas Association estimating there will be approximately USD 30 billion per year of incremental energy infrastructure expenditure over the next 22 years. In our view, this should provide ample opportunity for continued distribution growth. Please see this month's "North America deep dive" for an in-depth look into MLPs.

(22/08/2014)

Current yields across US asset classes (as of 22/08/2014)



Source: Bloomberg, BofA Merrill Lynch, Barclays, Credit Suisse. BXM Index yield estimated based on average gross monthly premiums collected by BXM Index.

Latin America investment strategy

Changes in Brazilian elections attract investors' attention

- Brazilian equities rise despite bleak fundamentals as investors are hopeful about a potential new president; we maintain our underperform view on Brazilian equities.
- Mexican hard-currency bonds and peso show upside potential as reforms will likely translate into economic growth.

Philipp E Lisibach

Barbara M Reinhard
CIO – Americas

The Datafolha poll released on 18 August, which shows voters' intentions in the upcoming Brazilian Presidential election on 5 October, is the first one to reflect the new situation since the Socialist Party's candidate Eduardo Campos tragically died in a plane crash early in August. While we prefer not to read too much into one single poll, it shows that the situation for President Dilma Rousseff has taken a dramatic turn, despite a recent recovery in her approval ratings. At the time of writing, Marina Silva has not yet been officially confirmed as a candidate, yet the poll has included her as she seems likely to replace Eduardo Campos as the PSB candidate. The survey finds that Dilma Rousseff will not have the required votes to avoid a second round in the election process, but that she should have a comfortable lead in the first round compared to the other candidates, Aecio Neves and Marina Silva, who are expected to attract about equal votes. However, the picture changes in the second round, if President Rousseff faces off against Marina Silva. The poll favors Marin Silva, but it is too close to come to a conclusion, so the race remains completely open.

Investors embrace the idea of new leadership…

The initial reaction to the poll results has been positive from investors as the poll shows an increased likelihood of a new president, and many investors tend to blame President Rousseff for the slow economic growth and disapprove of her left-leaning policies. Continuing the positive trend that started this spring, the Brazilian equity index, Bovespa, has gained approximately 5% month-to-date through 19 August. What remains unclear is whether Marina Silva will become the next Brazilian President, and whether she has enough political capital to push through necessary reforms, as she has a relatively small political alliance compared to her popularity. As we are entering the final period of a close and emotional race, we expect to see some elevated levels of equity market volatility, since investors tend to draw direct conclusions from the polls and anticipate the election outcome.

Table 1: Latin America equity strategy (3-6 months)

Region/Country	Index	View*
Latin America	MSCI Latin America	Underperform
Brazil	MSCI Brazil	Underperform
Chile	MSCI Chile	Neutral
Colombia	MSCI Colombia	Neutral
Mexico	MSCI Mexico	Neutral
Peru	MSCI Peru	Neutral

*vs. MSCI Emerging Market

Source: Credit Suisse

Figure 1: Brazilian earnings growth continues to decline amid macro headwinds

Source: Datastream, Credit Suisse / IDC

… but weak Brazilian fundamentals persist

While many investors in Brazil have been driven by the expectation of a new president, the fundamental picture remains bleak. We maintain our underperform view on the Brazilian equity market compared to global emerging markets, see Table 1, as the business cycle is slowing. This can be seen in the latest readings of the industrial production or the manufacturing Purchasing Manager Index (PMI). Our estimate for 2014 real GDP growth stands at 0.8%, with only marginal acceleration to 1.4% in 2015. Furthermore, second-quarter corporate results, including the unfavorable calendar effects of the FIFA World Cup, have been weak, with earnings 11% below estimates and cash flows 3% lower than estimates. While equity

markets have been driven by a general improvement in investor sentiment, we believe that earnings revisions will likely stay negative and act as a headwind, see Figure 1.

Mexico's signals are mixed, but improving; peso offers upside

The Mexican economy has been sending mixed signals about whether a rebound in growth is underway. On the positive side, economic leading indicators have been hovering in low, but positive territory, suggesting that the economy is expanding and industrial production is gaining some momentum. On the other hand, consumption remains slow and inflation has been ticking up slightly. The government's commitment to reform may put growth on a more solid path, and Mexican President Nieto has signed the important secondary legislation, guiding the opening of Mexico's energy industry to private investments. As a consequence, we continue to expect the Mexican peso to appreciate, with a 12-month target of 12.40 per US dollar, which is an upside of approximately 6%.

Table 2: Latin America fixed income strategy (3-6 months)

	Sovereign bonds*	
Country	**Hard currency**	**Local currency**
Argentina	Negative	N/A
Brazil	Negative	Negative
Chile	Neutral	Neutral
Colombia	Neutral	Negative
Mexico	Positive	Neutral
Peru	Positive	Positive
Venezuela	Neutral	N/A

*views reflect total return estimates

Source: Credit Suisse

Valuation supports Mexican hard-currency bonds

Mexican hard-currency bonds seem attractively valued from a fundamental perspective, see Table 2. Even if the fiscal performance of the country may be questioned in an environment of cyclical slowdown, we believe hard-currency bond valuations are supportive enough to offset this risk. In local-currency bonds, we are of the view that technical factors, such as a heavy positioning in Mbonos, increase the vulnerability of the market to significant swings in the US rate or potentially negative inflation surprises. More specifically, we note that the recent market pricing suggests an excessively positive view of inflation in the near term. As a consequence, our neutral stance primarily reflects a balanced risk-reward picture.

We maintain our negative view on Argentine bonds, as the situation remains unclear and recent developments and announced potential changes to the country's laws do not suggest an imminent solution for the restructured bond investors, which also makes it difficult for Argentina to return to the global bond market in the short or medium term.

(26/08/2014)

North America asset allocation overview

Maintaining our equity overweight

- US data continues to improve, but geopolitics weigh on our portfolios.
- We prefer equities over fixed income.

Dave El Helou

We continue to see economic data improving in the USA. In particular, job openings in June reached the highest level since February 2001 and the hiring rate improved. In July, we changed our view on the USA to neutral, with a focus on large cap growth due to improving economic data and better earnings. We continue to believe US small caps will lag the overall equity market. Our overweight positions in Europe and Japan have been maintained. Geopolitics and weak local economic data have weighed on European equities – Germany in particular – over the last few weeks. However, we reiterate our positive view due to the ever-supportive monetary policy. Our Japanese overweight position, which lagged earlier in the year, has performed solidly, with Japanese equities up over 8% in the last three months.

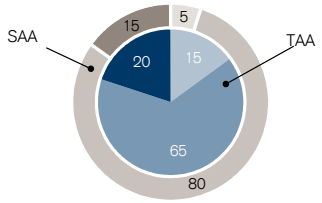
Within fixed income, we continue to maintain our underweight position, with expectations that we will see the first Fed rate hikes in the middle of next year. While benchmark yields have declined this year, partly as a result geopolitical uncertainty, we believe that they are at the low end of their trading range. Our cash position and short duration positions have hurt us this year, but we continue to maintain the view that the reacceleration of economic growth we are seeing in the second half of the year will put upward pressure on yields.

Our position in alternative investments remains unchanged, with a preference for hedge funds. (25/08/2014)

Current versus neutral allocation

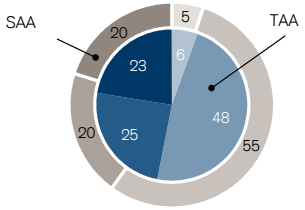
Indicative capital allocation that may change over time; implementation may deviate slightly, depending on benchmarks, currency positions and other implementation considerations. TAA=Tactical asset allocation; SAA=Strategic asset allocation.

Fixed Income



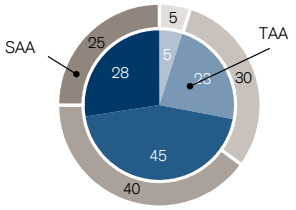
	SAA	TAA
Cash	5%	15%
Fixed Income	80%	65%
Tax Exempt	64%	53%
Credits	16%	13%
Equity	0%	0%
US	0%	0%
Non-US	0%	0%
Alternative	15%	20%

Income



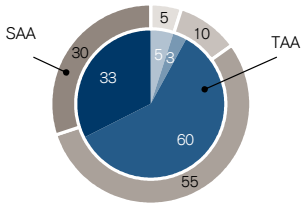
	SAA	TAA
Cash	5%	6%
Fixed Income	55%	48%
Tax Exempt	44%	41%
Credits	11%	7%
Equity	20%	25%
US	10%	10%
Non-US	10%	15%
Alternative	20%	23%

Balanced



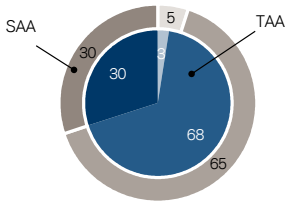
	SAA	TAA
Cash	5%	5%
Fixed Income	30%	23%
Tax Exempt	24%	19%
Credits	6%	4%
Equity	40%	45%
US	20%	20%
Non-US	20%	25%
Alternative	25%	28%

Capital Gain



	SAA	TAA
Cash	5%	5%
Fixed Income	10%	3%
Tax Exempt	8%	3%
Credits	2%	0%
Equity	55%	60%
US	28%	28%
Non-US	28%	32%
Alternative	30%	33%

Equities



	SAA	TAA
Cash	5%	3%
Fixed Income	0%	0%
Tax Exempt	0%	0%
Credits	0%	0%
Equity	65%	68%
US	33%	33%
Non-US	33%	35%
Alternative	30%	30%

Source: Credit Suisse

The proposed Strategic and Tactical Asset Allocations for each of the risk tolerance referenced above are created by the Private Banking Americas Asset Allocation & Investment Strategy group. The Strategic Asset Allocation (SAA), for a 3-7 year time horizon, is the neutral position reflecting the predefined risk tolerance and meets investment objectives over a full market cycle. The Tactical Asset Allocation (TAA), for a 3-6 month time horizon, expresses views resulting in temporary deviations from the SAA to generate expected excess returns or reduce risk. Alternative investments are typically high-risk investment vehicles which are available only to qualified individuals or entities that are willing to assume above average risk and sustain limited liquidity with a portion of their net worth.

North America deep dive

Master Limited Partnerships – still in the early innings

- Master Limited Partnerships still have material value to be unlocked.
- Energy independence and infrastructure build-out are fundamentally supportive.

Barbara M Reinhard
CIO – Americas

Nicolo Sebastiano Foscari

What are Master Limited Partnerships?

Master limited partnerships (MLPs) are partnerships that are listed on public exchanges. MLPs operate physical assets such as pipelines and other equipment for oil and natural gas, as well as refined products processing and services such as fractionation, transportation and storage. MLPs were created as a result of the Tax Reform Act of 1986 and Revenue Act of 1987, which created publicly traded partnerships and required these partnerships to generate at least 90% of their income from qualified resources such as real estate or natural resources.

MLPs trade in the form of units and unit holders receive quarterly cash distributions. Structured as pass-through entities, MLPs pay no entity-level tax; instead, taxes are paid by unit holders on distributions, based on the unit holder's specific tax rate, with a portion of the taxes paid on a deferred basis.

Growth of a sector

Few sectors have witnessed the rapid growth that MLPs have enjoyed. According to MLP index provider, Alerian, there were fewer than 20 listed MLPs in 1995, with a total market capitalization of USD 7 billion. As of June 2014, there were 117 listed energy MLPs, with an aggregate market capitalization of over USD 500 billion. What is behind this extraordinary growth rate for the sector? MLPs were originally created as a way of encouraging individuals to invest in domestic energy infrastructure. To attract investors, MLPs were structured to allow favorable tax treatment for individual investors – as opposed to double taxation, as is the case with corporate dividends – and MLPs were organized to have a relatively high level of income distribution. The shortcoming for the sector is the administrative burden of filing K–1 forms on MLP holdings. However, another factor contributing to the rapid growth is the unconventional hydrocarbon production revolution, commonly known as fracking, which allows producers to drill horizontal wells in shale formations to extract natural gas and oil.

Average annual MLP returns vs. S&P 500 and commodities-related strategies

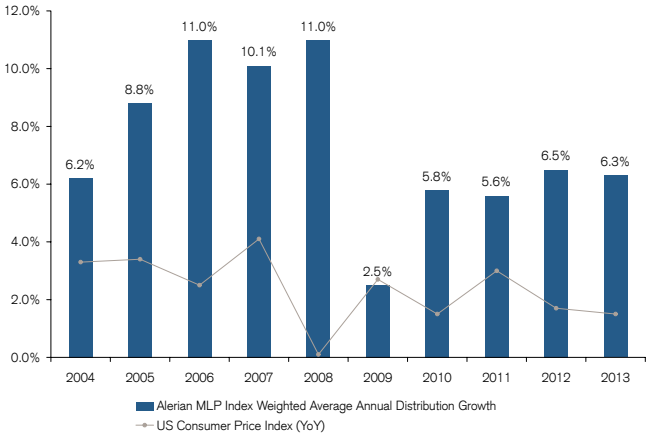
	MLPs	S&P 500	MSCI Energy	MSCI Utilities	UBS Commodities
Return	16.95	9.37	11.62	4.28	5.31
Risk	15.35	15.59	19.35	15.84	16.20
Return per Unit of Risk	1.10	0.60	0.60	0.27	0.33

Source: Credit Suisse, Datastream, December 1995 to June 2014, UBS Commodity Index Rebranded as Bloomberg Commodity index in June 2014

Fundamental outlook

All of this has not been lost on the sector. Since 1996, the Alerian MLP Index has compounded at 16.95%, far outpacing the S&P 500 Index and other comparable sectors (see table). The reasonable question becomes: what is the outlook for the sector going forward? We expect positive long-term performance to continue, albeit at a less robust pace. Valuations are still compelling as MLPs currently yield over 150 basis points over BBB-rated corporate bonds, versus a long-term average of 97 basis points. We see three fundamental dynamics for the sector that support this view: yield, infrastructure spending, and democratization of the sector.

MLP distribution growth has outpaced inflation



Source: Bloomberg, Alerian, Credit Suisse

Yield, infrastructure, and democratization

In terms of yield, the MLP sector has benefited from the decline in yields from many income-generating financial assets, such as bonds. Over the past ten years, the average growth of distributions for MLPs has averaged 7.4%. Estimates are that income distribution should grow, on average, 6%–9% over the next several years. What's more, the growth in income distribu-

tion has outpaced the US Consumer Price Index every year except one since 2004 (see chart). This characteristic makes MLPs a natural inflation hedge.

In terms of infrastructure, the North American energy sector is currently in the middle of a long-term trend toward greater energy production. Energy supplies that historically have not been available have become easier and cheaper to access, and are expected to see significant growth, particularly in shale, natural gas, and natural gas liquids. The continued demand for these resources will provide new organic growth opportunities for MLPs, since new mid-stream infrastructure build-out will be required to support the increased production. As of today, oil produced is still greater than what can be transported or stored and, with increasing discussion around reviving US oil exports, there appear to be significant new opportunities for MLPs. According to the American Gas Association, there will be approximately USD 30 billion in incremental annual energy infrastructure spending in the next 22 years. This increased infrastructure is needed to meet new demand and should help fuel future distribution growth.

There is the potential for the democratization of the sector to continue, as market participants become acquainted with this sector. We have found that MLPs add diversification to an equity portfolio in an overall asset allocation context. MLPs have a positive modest correlation to S&P 500 Index that has averaged approximately 0.38. Correlation to commodities is also low, with an average level of 0.28. When markets are under stress and volatility spikes upward (VIX index >25%), correlation levels increase to 0.50 and 0.44, respectively, thus decreasing the potential diversification benefits. Nevertheless, even after this increase, MLPs still add diversification to a balanced portfolio.

Risks

MLPs are dependent on capital markets for external funding, and the ability of energy MLPs to continue to access debt from capital markets and retain strong credit ratings is crucial for continued growth. MLPs exhibit a higher sensitivity to yield movements than the broad equity markets, as many investors hold MLP stocks for the distribution component of total returns. US government Treasury yields are relevant because, if rates increase, investors should expect distribution yields on MLPs to increase as well. As more non-traditional assets attempt to adopt the MLP structure, selectivity and active management of a portfolio of MLPs will be key.

(25/08/2014)

Economics

Limited growth momentum calls for continued monetary support

- While US and UK growth are robust, a number of headwinds are holding back the Eurozone and, to a lesser extent, Japan, China and other emerging markets.
- With economic growth subdued globally and oil markets well supplied, inflation should remain very low. Monetary policy can thus generally stay easy, with only gradual Fed tightening.

Oliver Adler
Head of Economic Research

While the US economy has emerged from its winter dip and UK growth is beating forecasts, activity in the Eurozone and, to a lesser extent, in Japan, has been disappointing. Looking ahead, we expect US GDP growth to remain in the 3% range, but growth in the Eurozone to come in below 1% this year and only slightly above in 2015. The number for Japan should be similar. Meanwhile, the Chinese economy is likely to decelerate somewhat into 2015 due to the overhang in the housing market, while the outlook for other emerging markets remains mixed.

US expansion now self-sustaining, Eurozone facing old and new headwinds

After the decline in the first quarter, the US economy has returned to what we believe is a self-sustaining expansion. Employment is growing steadily, and wages are rising, albeit quite gradually, while US companies should boost equipment spending in response to improving demand. The housing recovery also seems back on track after some "wobbles." The picture in the Eurozone is much less encouraging. The tax burden remains very high in many economies, even though some governments have recently lowered taxes very marginally. While government bond yields have fallen substantially, consumer loans and loans to small and medium sized enterprises remain too costly in the "periphery," and bank credit remains anemic. The European Central Bank's (ECB) new Targeted Long Term Refinancing Operations program should provide a slight boost to credit creation, and the upcoming asset quality review (see special topic) should be helpful, but whether it will result in a thorough "clean-up" of balance sheets and puts the banking system on a truly sound footing remains to be seen. Finally, the Eurozone's growth engine, Germany, has recently been held back by slowing demand in Italy, France as well as China. The Ukraine crisis and the associated risk of declining exports to Russia and other Eastern European economies could reinforce the slowdown. That said, absent a further deterioration of geopolitical stresses, momentum should improve somewhat toward year-end.

Low inflation suggests continued monetary ease

The renewed sluggishness has brought the Eurozone to the brink of deflation. As a result, the ECB will need to maintain its expansionary stance; if growth and inflation decelerate further, policy may even shift to quantitative easing in 2015. In Japan, euphoria over Abenomics has given way to realism: while the moderate expansion should continue, growth will remain subdued into 2015 due to structural reasons (mainly demographics) and in response to a further tax hike. Meanwhile, the Bank of Japan will likely miss its 2% inflation target and will thus probably extend its policy of aggressive balance sheet expansion beyond 2015. Growth deceleration and low inflation in China are allowing the People's Bank to relax policy as well, though measures will remain limited due to ongoing worries over excess credit creation. While inflation in some emerging markets, including Brazil, India and Turkey, is still above target, monetary tightening has ended there, too. This leaves the Federal Reserve (Fed) and the Bank of England as the only major central banks slated to begin a tightening process in 2015. Given the global growth and inflation backdrop, they are likely to proceed quite cautiously. (25/08/2014)

Global investment strategy

Stronger USD and preference for equities over bonds

- We continue to prefer equities over bonds, and recommend alternative investments for diversification.
- USD strength is supported both by fundamentals and the balance of geopolitical risks.

Nannette Hechler-Fayd'herbe
Head of Investment Strategy

Geopolitical risks have made a comeback in the past few years, with a surge in recent months. The reaction of various asset classes and markets has been quite differentiated, however. The Ukraine/Russia conflict has, for instance, had a measurable impact on the German DAX, but this has not prevented US stocks from making new highs. Core government bond yields are down, but gold has remained in its broad trading range, as has oil. The general conclusion is that geopolitical events add to uncertainty, but only rarely constitute "game-changers" for investors (see special topic article on geopolitical risks). They may temporarily reduce returns for various riskier assets, which may call for a temporary "de-risking" of portfolios, but not for a fundamental change in asset allocation.

Equities still our preferred asset class

Financial markets remain awash with liquidity despite a gradual shift toward Fed policy tightening. Given our view that growth fundamentals are essentially intact and supportive of corporate earnings, we expect volatility in equity markets to remain low; even in periods of deteriorating sentiment, market setbacks should be limited in time and in size. We also note that investors are not overly exposed in equities, and while valuations are in most cases not cheap, they are not extended either. Conversely, bond yields are at or close to historical lows. For all these reasons, we continue to regard equities as more attractive than bonds.

Improved compensation for risks in high yield but value has not turned positive yet

Spreads on speculative corporate bonds have widened in recent weeks, improving the compensation for risk. But we believe credit spreads do not yet offer value for the asset class more broadly. We therefore stick to our neutral view. We have also turned more neutral on financial bonds. While redemptions by European financials are now higher than new issuance (which supports these assets), the "technicals" indicate a loss of momentum. Meanwhile, the decline in core government bond yields to (or close to) historical lows, seems at odds with economic indicators, which continue to paint a picture of economic expansion. We therefore expect yields to edge up from current levels.

Alternative investments diversify portfolios

Correlations are at very low levels across many assets. This increases the gains from diversification. Commodities have acted as a good diversifier this year. We hold a neutral view on the overall asset class. Our relative preference for energy commodities over industrial metals has not paid off so far, but we believe that energy supplies may be tighter than the market currently assumes, while declining construction activity in China should, in turn, generate downside pressure on industrial metals prices. Hedge funds and real estate continue to constitute valuable alternative sources of investment returns.

Further USD gains; EUR and GBP (temporarily) soft; CHF capped by SNB

Our forecast of a USD appreciation has finally materialized. We continue to believe that economic fundamentals and the balance of geopolitical risks favor the USD. Ahead of the Scottish independence referendum, the GBP is likely to remain soft, but in the – more likely – event of a no-vote, this trend should reverse. The CHF has appreciated somewhat against the EUR, but we continue to believe that the Swiss National Bank's EUR/CHF 1.20 floor remains credible. If necessary it would be reinforced by currency interventions.

(25/08/2014)

Forecast summary

More information on the forecasts and estimates is available on request. Past performance is not an indicator of future performance. Performance can be affected by commissions, fees or other charges as well as exchange rate fluctuations.

(27/08/2014)

Short interest rates 3M Libor / 10-year government bonds

	3M Libor			10Y		
in %	Spot	3M	12M	Spot	3M	12M
CHF	0.02	0.0-0.2	0.0-0.2	0.49	0.6-0.8	0.9-1.1
EUR *	0.17	0.1-0.3	0.1-0.3	0.94	1.1-1.3	1.4-1.6
USD	0.24	0.2-0.4	0.5-0.7	2.40	2.7-2.9	3.1-3.3
GBP	0.56	0.5-0.7	1.1-1.3	2.45	2.6-2.8	3.1-3.3
AUD **	2.63	2.5-2.7	2.8-3.0	3.35	3.6-3.8	4.0-4.2
JPY	0.13	0.1-0.3	0.1-0.3	0.50	0.5-0.7	0.7-0.9

Spot rates are closing prices as of 26/08/2014. Forecast date: 25/08/2014. * 3M Euribor, ** 3M Bank Bill rates.

Source: Bloomberg, Credit Suisse

Equities

Index	Spot	P/E	Div. y. (%)	3M*	12M*
MSCI AC World**	194	14.4	2.8	200	212
US S&P 500	2,000	15.6	2.3	2,020	2,120
Eurostoxx 50	3,198	12.6	4.5	3,250	3,500
UK FTSE 100	6,823	13.5	3.9	6,850	7,100
Japan Topix	1,285	13.7	1.8	1,330	1,420
Australia S&P/ASX 200	5,638	15.0	4.2	5,750	6,000
Canada S&P/TSX comp	15,619	15.3	2.7	16,000	17,000
Switzerland SMI	8,673	15.4	3.1	8,650	9,000
MSCI Emerging markets**	454	11.2	2.7	460	495

Prices as of 26/08/2014; *forecast; **net returns (incl. dividends).

Source: Datastream, Credit Suisse

Commodities

	Spot	3M*	12M*
Gold (USD/oz)	1281	1300	1200
Silver (USD/oz)	19.37	19	17
Platinum (USD/oz)	1417	1550	1600
Palladium (USD/oz)	886.7	900	900
Copper (USD/ton)	7054	6500	6200
WTI Crude Oil (USD/bbl)	93.9	98	101
Credit Suisse Commodity Benchmark	5852	5900	5900

Spot prices: New York close 26/08/2014; *forecast.

Source: Bloomberg, Credit Suisse

Credit: Selected Indices

	Yield (%)	Spread (bp)	Duration (years)	3M forecast	12M forecast
BC IG Corporate EUR	1.3	94	4.6	0.2%	1.0%
BC IG Corporate USD	2.9	101	7.2	0.1%	0.8%
BC IG Financials USD	2.6	98	5.7	0.4%	1.2%
CS LSI ex govt CHF	0.6	36	5.3	-0.1%	-0.2%
BC High Yield Corp USD	5.2	361	4.1	0.9%	3.6%
BC High Yield Pan EUR	4.5	332	4.0	0.7%	3.5%
JPM EM hard curr USD	5.4	301	7.8	0.5%	3.0%
JPM EM local curr hedg. USD	6.5	n.a.	4.7	0.7%	3.1%

BC = Barclays Capital, IG= Investment Grade, CS = Credit Suisse, JPM = JP Morgan (EMBI+ and GBI Gl. Div). Index data as of 26/08/2014.

Source: Bloomberg, Credit Suisse

Foreign exchange

	Spot	3M	12M
EUR/USD	1.32	1.29-1.33	1.26-1.30
USD/CHF	0.92	0.91-0.95	0.93-0.97
EUR/CHF	1.21	1.20-1.24	1.20-1.24
USD/JPY	104	104-108	108-112
EUR/JPY	137	137-141	139-143
EUR/GBP	0.80	0.76-0.80	0.75-0.79
GBP/USD	1.66	1.65-1.69	1.65-1.69
AUD/USD	0.93	0.90-0.94	0.90-0.94
USD/CAD	1.10	1.07-1.11	1.07-1.11
EUR/SEK	9.16	9.18-9.22	8.98-9.02
EUR/NOK	8.14	8.08-8.12	7.93-7.97
EUR/PLN	4.19	4.18-4.22	4.18-4.22
USD/CNY	6.15	6.13-6.17	6.06-6.10
USD/SGD	1.25	1.23-1.27	1.23-1.27
USD/KRW	1017	1020-1040	1020-1040
USD/INR	60.4	60-62	60-62
USD/BRL	2.26	2.30-2.40	2.40-2.50
USD/MXN	13.1	12.7-12.9	12.3-12.5

Spot rates: London close 26/08/2014.

Source: Bloomberg, Credit Suisse

Real GDP growth and inflation

	GDP growth			Inflation		
in %	2013	2014E	2015E	2013	2014E	2015E
CH	2.0	2.0	1.8	-0.2	0.1	0.5
EMU	-0.4	0.8	1.3	1.3	0.6	0.8
USA	2.2	2.1	3.0	1.5	2.0	2.0
UK	1.7	3.2	2.7	2.6	1.8	1.9
Australia	2.4	2.7	2.8	2.4	2.5	2.4
Japan	1.5	1.0	1.1	0.4	2.7	1.8
China	7.7	7.4	6.9	2.6	2.3	3.0

Forecast date: 21/08/2014.

Source: Credit Suisse

Top investment ideas

Top investment ideas

- In equities, we continue to see value in European companies. In fixed income, financials still offer opportunities, but selection is key.
- China's short-term equity outlook is improving, and a bigger move is possible if structural reforms accelerate.

Markus Stierli
Head of Fundamental Micro Themes Research

European value

In our view, European companies still offer value through attractive products and strong brands. After a long period of corporate restructuring, even a small up-tick in demand can have a significant impact on profitability. In addition, should the decline in the euro continue, European exporters' competitiveness would likely improve.

Fixed income: The search for yield

We still see opportunities in selected financials. However, the Investment Committee's recent decision to move financials to neutral from outperform highlights the need for careful selection.

Emerging market reformers, cyclicals & dividends

Implementation of structural reforms will hold the key to China's longer-term outlook. China was upgraded to outperform from neutral on a tactical basis to reflect improved technicals, stabilizing macro and earnings momentum, attractive valuations and positive reform progress. (23/08/2014)

Top investment ideas 2014 – overview

Top idea	Status	Comment
European value	■	Benefit from investing in different stages of the recovery (consumer, industrial) or sector restructuring (telecoms) and a weakening EUR post ECB monetary easing (e.g. German manufacturers) and a selection of small/mid cap stocks exposed to the recovery.
Seeking equity alpha	■	Low correlations within equity markets help outperformance via style, sector and bottom-up selection. We recommend stocks from our preferred sectors, European small/mid-caps for long only investors and pair trading strategy and hedge funds for long-short investors.
Techs in focus	■	In a generally attractive IT sector, we favor technology stocks that benefit from the expansion of automation and the evolution of the Internet of Everything. Our focus is on Internet platform firms, enablers of the Internet of Things (IoT), as well as IT and capital goods companies which use the IoT for factory and process automation.
Emerging market reformers, cyclicals & dividends	■	Focus on selected opportunities based on structural reforms, as recently seen in India and currently in progress in China, as well as beneficiaries of favorable cyclical effects and strong dividend stocks such as the tech sector in Taiwan.
Cash-rich companies	■	High corporate cash levels and inexpensive financing give rise to M&A opportunities and scope for raising dividends/share buybacks.
Sustainability	■	As construction activity accelerates and energy costs are high, we include resource efficiency and adaptability to a changing business environment.
Fixed Income: The search for yield	■	Searching for yield in a bond universe that looks richly valued, but the exact emphasis evolves over time, currently favoring European financial sub debt, CoCos and corporate hybrids.

Key to status symbols: green = attractive investment opportunities – continue to invest in theme; yellow = keep holdings but do not add to existing positions; red = reduce /exit existing positions.

Source: Credit Suisse

Special topic

Geopolitics and its market impact

■ In a large majority of major geopolitical events that we examine, the most profitable strategy has been the contrarian one of buying into the resulting equity price falls.

■ A profound market impact only arises if these events lead to widespread and prolonged conflict or serious cuts in energy supplies; historically this is very rare.

Giles Keating
Head of Research and Deputy Global CIO

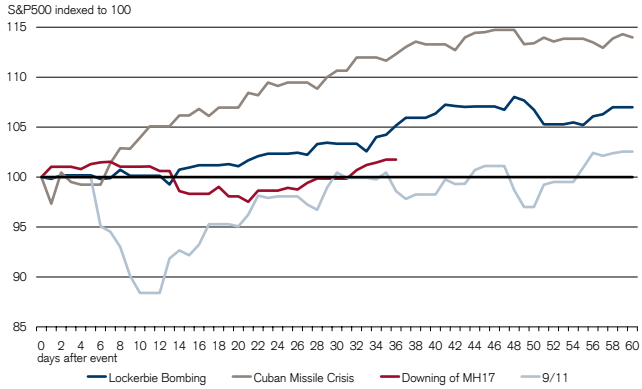
Jonathan Horlacher
Fundamental Macro Research

Geopolitical events receive considerable attention from investors – especially during flare-ups, as have recently occurred. But, how much impact do they actually have on markets? Our review suggests that the large majority of individual major events – ranging from the assassination of Archduke Ferdinand 100 years ago through to 9/11 and events this year in Iraq and Ukraine – impact major stock markets by around 10% or less, with the effect typically being fully reversed within a month or so. This suggests that the most profitable strategy has usually been the contrarian one of buying into price falls caused by such incidents. We have identified only a handful of events in the last hundred years that break this rule, and even these saw a recovery within two to three years. For strategic investors, it has been far more important to identify the larger geopolitical shifts that build up gradually in the background, such as the collapse of the Austro-Hungarian empire, the rise of the United States as global "hegemon" between the two world wars, and potentially the current reversal of that rise. The first of these trends culminated in an 87% collapse in the dollar value of the Vienna stock market over a four-year period of hyperinflation, the second saw the US stock market outperform the outgoing power, the UK, by a multiple of 1.5 over the 25 years to the end of the Second World War. Headline-grabbing individual events are often symptomatic of these deeper realignments, but should usually be used by investors – alongside a long accumulation of other evidence – to motivate a long-term portfolio realignment over years, rather than as major market breakpoints in their own right.

Very few individual geopolitical events have a sustained global impact

The Cuban Missile Crisis, which briefly threatened a global atomic war, saw only a few days of sideways markets, followed by a major rally. Looking at 9/11, once US equity markets reopened after a 7-day hiatus, they briefly fell by just over 10% and then recovered those losses within a bit over a month. Falls associated with the Japanese attack on Pearl Harbor were similar, and a series of other tragic geopolitical events, ranging from the sinking of the Lusitania to the Lockerbie plane bombing and the tragedy of flight MH17, only caused limited market impact (Figure 1).

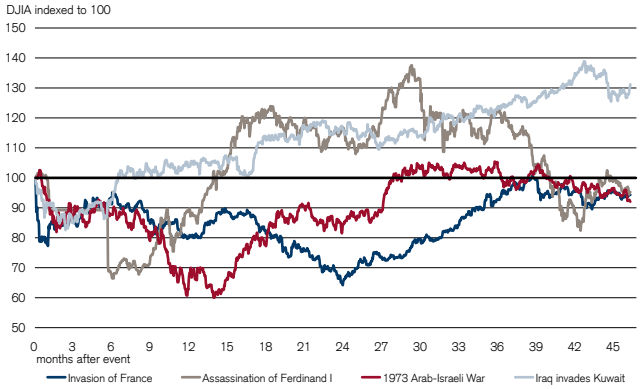
Figure 1: Geopolitical events with minor market impact



Source: Bloomberg, Credit Suisse / IDC

The only three individual geopolitical events we have identified over the last 100 years that had a major and persistent impact are the German invasion of France in 1940, the start of the First World War, and the Yom Kippur War and subsequent oil crisis, which saw respectively 20%, 30% and 40% declines in US stocks. But even in these cases, the decline was fully reversed within 1 to 3 years (Figure 2).

Figure 2: Major market movements due to geopolitics

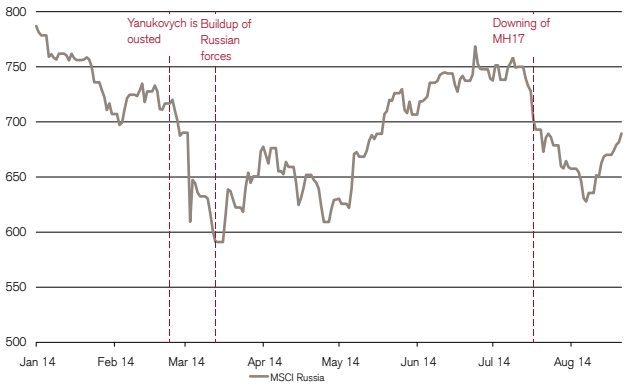


Source: Bloomberg, Credit Suisse / IDC

Why are large, sustained market impacts so unusual? The reason seems to be that stock returns reflect corporate earnings, and most companies' revenues and earnings are not greatly affected by a single terrorist attack or a war in a far-away country. Moreover, central banks might counterbalance the impact with monetary easing. These events can cause tragic loss of life and major disruptions to economic and social life locally, but tend to be far less significant in the global perspective. Ukraine is facing a disastrous loss of a quarter of its annual GDP due to the internal turmoil this year, but this equals roughly one hour of global GDP.

The exception is when a single event changes the world totally, including all previous assumptions about future corporate income streams. The invasion of France in 1940 signaled a conflict whose limits simply could not be assessed, while the Yom Kippur War led to a total realignment of control over global oil supply and a tripling of its price. An interesting contrast is to look at the muted market reaction to the Cuban Missile Crisis: since an atomic war would certainly have radically affected global corporate earnings, investors probably felt this outcome was so extreme that it could almost be ruled out.

Figure 3: MSCI Russia during the events in Ukraine



Source: Bloomberg, Credit Suisse / IDC

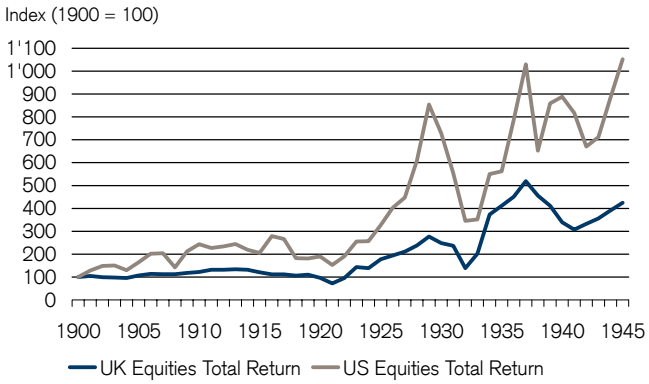
While the effect of most geopolitical events on global markets may be limited, there can be substantial effects on specific local markets, but even these may be rapidly reversed. Russian equities fell about 20% on two occasions this year, but each time have recovered at least partially within a couple of months (Figure 3). This suggests that investors should start from the baseline assumption that the impact on major markets of any given geopolitical panic will be rapidly reversed, and they should set a very high bar when trying to identify events that might break this pattern.

Longer-term geopolitical shifts: Historical evidence

With the USA being the only superpower with a stock market in the post Second World War era, academic studies of that period have struggled to find a clear relation between seismic geopolitical shifts and stock markets. However, we can look at earlier periods using data from the Credit Suisse Research Institute's Global Investment Returns Yearbook (see Figure 4). From 1900 onward, there were major geopolitical shifts, with the rise of the USA, the relative decline of the UK, the weakening of Germany and the collapse of the Austro-Hungarian empire.

In real terms and measured in US dollars, an investor in US stocks enjoyed a 10-fold rise from 1900 until the end of the Second World War in 1945, almost two-and-a-half times as much as the quadrupling in UK equities, with the effect particularly marked after 1920 when the transfer of power to the USA accelerated. For Germany and Austria-Hungary, the contrast is even starker, with stock market investments losing all but a tiny fraction of their pre-war dollar value after the hyperinflation of 1922.

Figure 4: Equity returns UK and USA 1900–1945



Source: Credit Suisse Research Institute

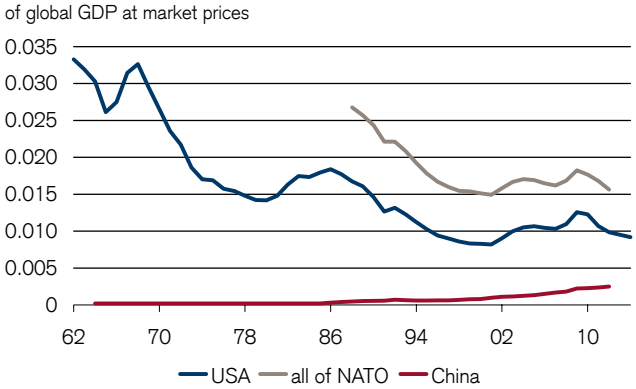
Longer-term geopolitical shifts: Where do we go?

Possibly the biggest long-term geopolitical shift now underway is the progressive relative decline of the USA, albeit from a position of dominance. This is illustrated by Figure 5, which shows how US military spending has declined as a percentage of global GDP (and the same is true if all of NATO is included). This is almost inevitable, as successful economic development around the world, and especially in Asia, is substantially reducing the share of US GDP, and hence its military spend,

in the global total. The USA could avoid this only by increasing, year after year, the share of its output devoted to military spending, which is clearly not practical.

While this trend has been underway for decades, what has changed over the last decade or so is that China, and to a lesser extent, other countries, have started to raise their own military spending substantially. While the scale makes it difficult to see on the chart, China's spending, which was negligible two decades ago, is now about one-quarter of that in the USA and is rising rapidly. Smaller, but still important to understanding the global situation, Russia has moved from the decline in military spending seen after the collapse of the USSR into an expansion phase, and rises are also visible elsewhere, including in Saudi Arabia.

Figure 5: Military spending as % of global GDP



Source: SIPRI Military Expenditure Database 2012

This declining relative spending is only a proxy for power, especially in a world of cyber warfare and proxy wars, but even so, it probably signals a reduced ability for the USA and NATO to engage in many areas at once. So, events in Ukraine, the Middle East and Asia-Pacific may form part of a pattern, in which China, Russia, organizations such as ISIS and others, become more willing to exercise their own military strength since they see the USA less likely to respond.

So, investors may face more of such events in coming years. Does this mean greater uncertainty and thus higher risk premia on assets (i.e. lower price-earnings multiples for stocks)? Based on the analysis above, a greater number of headline-grabbing events need not mean greater uncertainty, except in the very short term, since they usually have only a limited impact. General uncertainty would rise only if these events lead to widespread conflict or serious interruption to energy supplies, and as we saw, such seismic changes have historically been very rare.

Our preferred interpretation is that events both in Ukraine and in the South China Sea and Pacific Ocean are symptoms of the dominant power of the USA and NATO giving way to greater relative power, within those areas, of Russia and China respectively, potentially a new geopolitical equilibrium which can offer long-term opportunities in those two countries' currently low-valued equity markets. In contrast, in the Middle East, with no single such power, the potential for a truly disruptive event, although very low, cannot be ruled out completely.

(25/08/2014)

Special topic

Asset Quality Review: Boosting trust, promoting securitization

- We expect a fairly tough outcome of the AQR and stress tests, which should improve confidence in the banking sector.
- The re-opening of the securitization market would mark a further critical milestone, both for the ECB and investors.

Christine Schmid
Banking Research

The results of the Eurozone bank asset quality review (AQR) conducted by the ECB will be published by mid-October, though some information may "leak" out beforehand. The AQR will be aligned with the so-called stress tests conducted by the European Banking Association (EBA), which simulate the behavior of bank balance sheets for various economic scenarios. Banks for which the ECB detects a capital shortage will be given two weeks to come up with a plan for how to fill the gap. The ECB will approve or reject the proposals by 4 November. In case of approval, banks will be given six months to fill the gaps identified under the AQR for the stress test's base scenario and nine months for gaps under the adverse scenario.

Further increase in recognition of non-performing loans in Q2

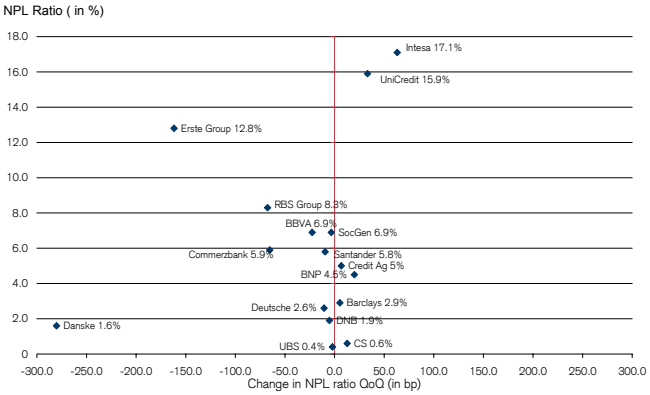
Expectations regarding the outcome of the stress tests and AQR will continue to drive the performance of bank stocks in the coming weeks. While banks know the macroeconomic assumptions used by the ECB, the classification of loans by the ECB and EBA into non-performing, impaired, restructured and performing might differ by bank and country. As problem loans may be handled quite strictly, capital shortfalls could result. Greek and Italian banks further increased the volume of non-performing loans in Q2 2014 in preparation for the ECB results (see Figure 1), but capital shortfalls may nevertheless result.

Transparency achieved by AQR could boost securitization

The stress tests and AQR will be an important milestone in the ECB's efforts to foster trust in the banks' balance sheet quality. Moreover, an important side effect of officially assessing bank asset quality could be a pick-up in their securitization. The European securitization market has lost over 75% of its 2008 volume, with new issuance below EUR 200 bn in 2013, only about 14% of US issuance. Enhanced securitization would not only boost the provision of credit to the economy, but could also offer interesting investment opportunities in a low yield environment (also for the ECB, if it launches QE). Banking stocks could also react positively to an improving securitization market, although investors would worry if banks shed too many lower risk mortgages. Our rating for the banking sector remains neutral, given still significant regulatory and litigation uncertainty. (25/08/2014)

Figure 1: Non-performing loan ratio of selected European banks

Italian banks with high level of non-performing loans



Source: Company data

Fixed income

Bonds expensive, but upside for yields seems limited

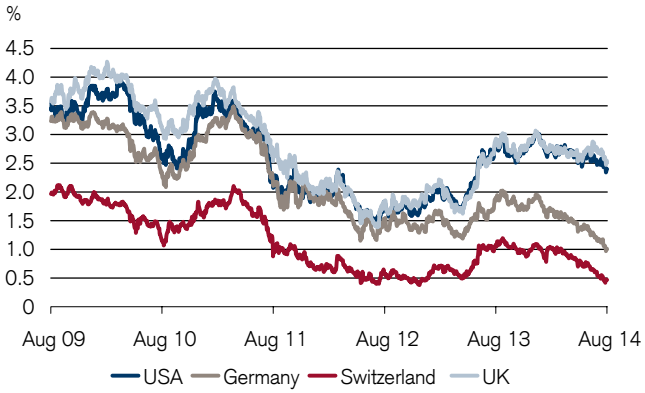
- Increasing risk of a prolonged period of low global bond yields, but valuations remain unattractive.
- Bank bonds: Weak price momentum balanced by low supply; we have a neutral outlook.

Sylvie Golay Markovich
Head Fixed Income Analysis

Monetary divergence driving relative bond performance

Core government bond yields declined further on increased geopolitical tensions and renewed concerns about the Eurozone economy. Moreover, market reaction to news has remained asymmetric, with negative headlines leading to larger yield movements than positive ones. However, as this performance pattern is not uniform across markets, strategy should focus on relative performance. In this regard, US Treasuries are likely to continue to underperform German Bunds and, even more so, European peripheral sovereign bonds. This view remains supported by the strong monetary policy divergence between the US Fed and the ECB as well as indications of stronger US economic growth. Although movements in Swiss government bonds yields remain closely linked to the EUR market, their absolute level offers very little value.

Major government bond markets: 10-year yield
Long-dated bond yields have remained on a downtrend YTD



Source: Datastream, Credit Suisse / IDC

Favor European peripheral bonds, neutral on financials

Our preference for European peripherals and, in particular, Italian sovereign (and covered) bonds, is to a large extent based on support measures by the ECB, including the potential for outright purchases of sovereign bonds (quantitative easing) should the economic and inflation backdrop deteriorate further. Among corporate bonds, the chart technicals for financials have recently deteriorated. Still, we view the ECB's Targeted Long Term Refinancing Operations as positive for European financials, not least because they are likely to further limit senior bank bond issuance. We now have a neutral outlook on the sector.

In the rest of the credit space, valuations have generally improved, especially for high yield bonds. Still, high yield spreads do not offer enough compensation yet for us to turn more positive, especially for bonds rated single B and below. In emerging markets, the situation in Ukraine remains a risk, especially for Eastern European issuers. Still, in light of Russia's strong financial fundamentals and attractive valuations, we keep our positive view on Russian sovereign hard currency bonds. In contrast, we have changed our view on RUB bonds to neutral, mainly due to the deteriorating inflation outlook. In CEEMEA, we now have only a tactically constructive view on TRY bonds. Finally, we now see more downside risk for Argentina, including local law bonds, given the deteriorating fiscal outlook and risks linked to the country's offer to swap foreign into local law bonds. (22/08/2014)

Equities

Micro data finally turning positive

- The correction in equities was short-lived. Global equities have almost recovered.
- The earnings season has been good overall, with earnings growth backed by strong US revenues.

Gérald Moser
Head of Equity Analysis

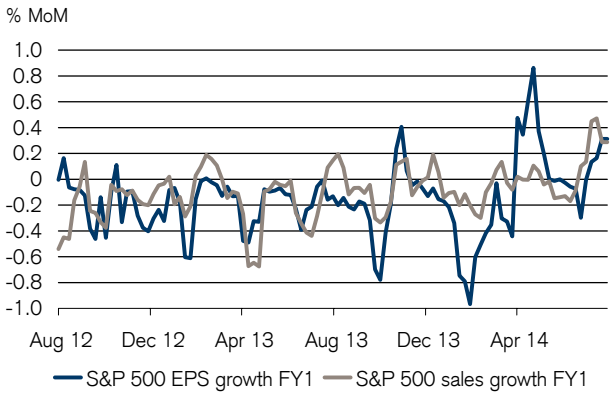
A correction in the equity bull trend

Weakness in equity markets in late July/early August was mostly triggered by a shift in investor sentiment due to heightened geopolitical risk. In most regions, the macro data continued to be solid. Europe suffered relative to other regions, with negative data surprises and proximity to the Russia/Ukraine crisis impacting the region. But with fundamentals globally still supportive in our view, we view this phase of weakness as a buying opportunity, rather than a start of a more sustained period of equity underperformance.

An encouraging earnings season globally

The Q2 earnings season has come to an end, and the conclusions are positive. In the USA, results were impressive for both the bottom and top line, while European companies also managed to beat bottom-line expectations, albeit by a smaller margin. We had been expecting European companies to lag their US counterparts in the earnings cycle, as it is typically the case. We highlighted at the end of the last earnings season that revenues needed improve for earnings to continue to grow. It is therefore encouraging to note that revenue growth surprises were the most positive in years in the USA. We would expect a similar trend to develop in the next couple of earnings seasons in Europe. Margins expanded to a new historical high in the USA, reaching 9.1%, but a few companies highlighted in their comments that inflationary pressure is starting to build up in some areas. Margins in Europe are still below historical highs, so we believe the prospects for a further increase in earnings is higher in the long term in Europe than in the USA.

Revenue estimates revised up during earnings season
S&P 500 EPS and sales growth, FY1 1-month change



Source: Datastream, I/B/E/S, Credit Suisse / IDC

We keep our regional and sector allocation unchanged

Although Europe has been underperforming recently, we think that most of the bad news has been priced in. Our economists expect economic momentum to turn positive in Q3. It is likely to be a small improvement and from a low base, but European equities would benefit from a turn in macro momentum. We also remain positive on Japan. Valuations are attractive and fundamentals are still supportive. On the sector side, we still favor a barbell strategy, which blends defensive and cyclical sectors to balance the risks. Our preferred sectors are healthcare and IT. (26/08/2014)

Alternative investments

Mixed prospects for alternative investments

- Risk of higher yields weighs on commodities, real estate outlook.
- Market conditions for hedge funds continue to improve.

Tobias Merath
Head of Cross Asset and AI analysis

Selected opportunities

The current environment of slow economic recovery, low inflation and low interest rates is not uniformly positive for alternative investments. The risk of rising bond yields is negative for real estate and gold, while the level of growth is still not high enough to support a positive view on commodities. We think hedge funds are best positioned, given low cross-asset correlations and low volatility.

Hedge fund market conditions are improving

Hedge funds saw a minor pullback in July. The Credit Suisse Hedge Fund Index lost 0.31%, bringing year-to-date performance to 2.52%. Looking ahead, while performance has been below average year-to-date, we would note that market conditions are improving, suggesting scope for better returns during the remainder of the year. Our Hedge Fund Barometer, which measures risk factors such as volatility, liquidity, business cycle and systemic risks, continues to improve. Given low inter-stock correlations and our positive outlook on equities, long-short equity is a promising hedge fund style. We also hold a positive view on the global macro style, as elevated geopolitical risks should provide managers with a wide opportunity set.

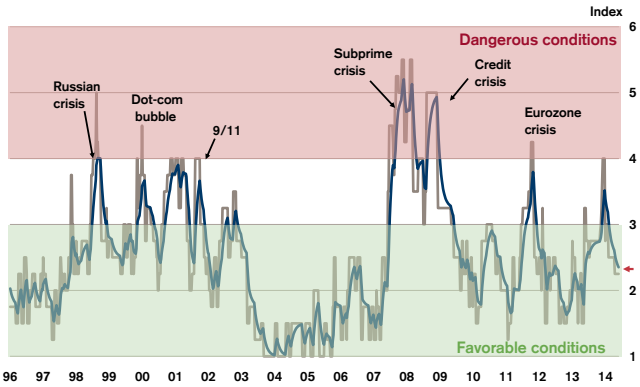
Neutral outlook for commodities

In July and August, the Credit Suisse Commodity Benchmark gave back most of the gains achieved earlier this year. The individual commodity sectors have very different fundamentals. Thus, commodity performance is diverging. This is bad news for commodity indices, as gains in one sector are diversified away by losses in another. As a result, we have a neutral outlook for the asset class. Within commodities, we think oil prices could recover from their recent dip, as inventories remain below average and as geopolitical risks remain high. Gold remains torn between the risk of higher bond yields and cheap valuation. We expect gold prices to move sideways for now.

Risk of higher yields limits outlook for REITs

Global REITs and other real estate securities continued to perform well amid improving direct real estate markets and the recent drop in bond yields. However, this performance is unlikely to last, as recovering growth should push up interest rates eventually. As a result, our outlook for REITs is just neutral. Regionally, we prefer US, UK and Japanese REITs, which benefit from dynamic underlying real estate markets. Contrary to this, emerging market real estate securities are likely to underperform, especially as China's real estate market is losing momentum. (22/08/2014)

Hedge Fund Barometer moving further into positive territory



Source: Bloomberg, Datastream, Credit Suisse / IDC

Foreign exchange

Scottish referendum temporarily clouds GBP outlook

- Continue to favor USD exposure. EUR to depreciate further on falling interest rates. GBP faces political headwinds.
- Prefer MXN over BRL, and hold to CNY positive view. Risks for RUB and PLN have increased.

Luca Bindelli
Head of Foreign Exchange Analysis

USD stronger, EUR more vulnerable

The USD uptrend has continued over the past month, in part due to higher investor risk aversion. We expect this trend to persist, as US economic data should remain strong. This will keep the threat of a higher-than-expected path of Fed rate hikes in place. In contrast, the Eurozone economy continues to surprise to the downside, prompting a decline in interest rates and a weaker EUR. We continue to expect the EUR to depreciate against the USD and the GBP, as the ECB "anchors" interest rates at low levels. This will also continue to prevent the EUR from making gains against the CHF. We expect EUR/CHF to remain close to the Swiss National Bank's floor of EUR/CHF 1.20. Our view on USD/JPY remains positive, as rate spreads and investment flows should weigh on the JPY.

GBP facing political risks

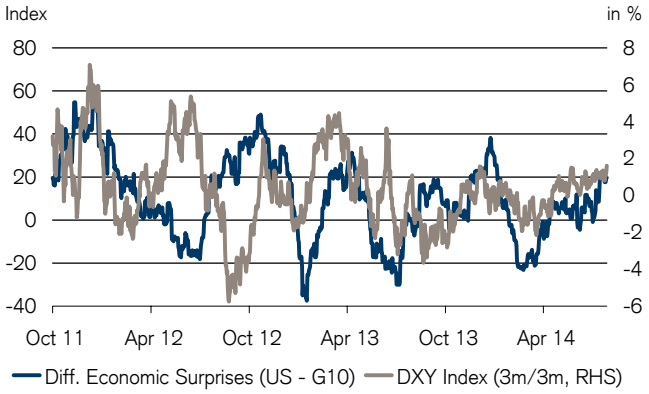
The Scottish independence referendum will likely generate some volatility and weigh on the GBP in the near term. Assuming that the vote for independence is rejected, as polls currently suggest, GBP weakness should reverse. This is what happened with the CAD during the Québec independence referendums in Canada in 1980 and 1995. A vote in favor of independence could have a more lasting impact and require a reassessment of our view. From a cyclical standpoint, the GBP lost ground as rate hike expectations were lowered in response to dovish statements from the Bank of England and a decline in inflation. That said, the economy is still doing well and the interest rate "carry" remains quite attractive relative to other markets. We remain neutral on GBP/USD.

Emerging market currencies struggle

Ongoing geopolitical tensions in Ukraine and the Middle East slightly boosted the volatility of EM currencies. We now see the RUB weakening further as risks to growth increase, capital outflows resume and the central bank reduces its support for the RUB as it moves toward inflation targeting. Risks for the PLN have increased due to a disinflation trend, softer growth and Poland's exposure to Russia/Ukraine. We continue to hold a positive long-term view on the CNY. We prefer the MXN over the BRL, as Mexico's energy reform should boost foreign investment and growth in the medium term. In contrast, political uncertainty has increased in Brazil after the death of Eduardo Campos, a contender in the presidential election race, while the growth-inflation mix remains negative.

(22/08/2014)

Economic surprises (US-G10) vs. DXY Index
Spread in data surprises supports a higher USD scenario



Source: Datastream, Credit Suisse / IDC

Glossary

Risk warnings

Market risk	Financial markets rise and fall based on economic conditions, inflationary pressures, world news and business-specific reports. While trends may be detected over time, it can be difficult to predict the direction of the market and individual stocks. This variability puts stock investments at risk of losing value.
Bond risks	Investors are exposed to interest rates, currency, liquidity, credit market and issuer fluctuations, which may affect the price of bonds.
Emerging markets	Emerging markets are located in countries that possess one or more of the following characteristics: a certain degree of political instability, relatively unpredictable financial markets and economic growth patterns, a financial market that is still at the development stage or a weak economy. Emerging market investments usually result in higher risks as a result of political, economic, credit, exchange rate, market liquidity, legal, settlement, market, shareholder and creditor risks.
Hedge funds	Regardless of structure, hedge funds are not limited to any particular investment discipline or trading strategy, and seek to profit in all kinds of markets by using leverage, derivative instruments and speculative investment strategies that may increase the risk of investment loss.
Commodity investments	Commodity transactions carry a high degree of risk and may not be suitable for many private investors. The extent of loss due to market movements can be substantial or even result in a total loss.
Real estate	Investors in real estate are exposed to liquidity, foreign currency and other risks, including cyclical risk, rental and local market risk as well as environmental risk, and changes to the legal situation.
Currency risks	Investments in foreign currencies involve the additional risk that the foreign currency might lose value against the investor's reference currency.

Source: Credit Suisse

Explanation of indices frequently used in reports

Index	Comment
MSCI World	MSCI World is an index of global equity markets developed and calculated by Morgan Stanley Capital International. Calculations are based on closing prices with dividends reinvested.
US S&P 500	Standard and Poor's 500 is a capitalization-weighted stock index representing all major industries in the USA, which measures the performance of the domestic economy through changes in the aggregate market value.
Eurostoxx 50	Eurostoxx 50 is a market-capitalization-weighted stock index of 50 leading blue-chip companies in the Eurozone.
UK FTSE 100	FTSE 100 is a market-capitalization-weighted stock index that represents 100 of the most highly capitalized companies traded on the London Stock exchange. The equities have an investibility weighting in the index calculation.
Japan Topix	TOPIX, also known as the Tokyo Stock Price Index, tracks all large Japanese companies listed in the stock exchange's "first section." The index calculation excludes temporary issues and preferred stocks.
Australia S&P/ASX 200	S&P/ASX 200 is an Australian market-capitalization-weighted and float-adjusted stock index calculated by Standard and Poor's.
Canada S&P/TSX comp	The S&P/TSX composite index is the Canadian equivalent of the S&P 500 Index in the USA. The index contains the largest stocks traded on the Toronto Stock Exchange.
Switzerland SMI	The Swiss Market Index is made up of 20 of the largest companies listed of the Swiss Performance Index universe. It represents 85% of the free-float capitalization of the Swiss equity market. As a price index, the SMI is not adjusted for dividends.
MSCI Emerging Markets	MSCI Emerging Markets is a free-float-weighted Index designed to measure equity market performance in global emerging markets. The index is developed and calculated by Morgan Stanley Capital International.
BC IG Corporate EUR	The Euro Corporate Index tracks the fixed-rate, investment-grade, euro-denominated corporate bond market. The index includes issues that meet specified maturity, liquidity and quality requirements. The index is calculated by Barclays.
BC IG Corporate USD	The US Corporate Index tracks the fixed-rate, investment-grade, dollar-denominated corporate bond market. The index includes both US and non-US issues that meet specified maturity, liquidity and quality requirements. The index is calculated by Barclays.
BC IG Financials USD	The IG Financials Index tracks the fixed-rate, investment-grade, dollar-denominated financials bond market. The index includes both US and non-US issues that meet specified maturity, liquidity and quality requirements. The index is calculated by Barclays.
CS LSI ex govt CHF	The Liquid Swiss Index ex govt CHF is a market-capitalized bond index representing the most liquid and tradable portion of the Swiss bond market excluding Swiss government bonds. The index is calculated by Credit Suisse.
BC High Yield Corp USD	The US Corporate High Yield Index measures USD-denominated, non-investment grade, fixed-rate and taxable corporate bonds. The index is calculated by Barclays.
BC High Yield Pan EUR	The Pan European High Yield Index measures the market of non-investment grade, fixed-rate corporate bonds denominated in euro, pound sterling, Norwegian krone, Swedish krone and Swiss francs. The index is calculated by Barclays.
JPM EM hard curr. USD	The Emerging Market Bond Index Plus tracks the total return of hard-currency sovereign bonds across the most liquid emerging markets. The index encompasses US-denominated Brady bonds (dollar-denominated bonds issued by Latin American countries), loans and Eurobonds.
JPM EM local curr hedg. USD	The JPMorgan Government Bond Index tracks local currency bonds issued by emerging market governments across the most accessible markets for international investors.
CS Hedge Fund Index	The Credit Suisse Hedge Fund Index is compiled by Credit Suisse Hedge Index LLC. It is an asset-weighted hedge fund index and includes only funds, as opposed to separate accounts. The index reflects performance net of all hedge fund component performance fees and expenses.
DXY	A measure of the value of the US dollar relative to the majority of its most important trading partners. The US Dollar Index is similar to other trade-weighted indices, which also use the exchange rates from the same major currencies.

Source: various index providers, Credit Suisse

Abbreviations frequently used in reports

Abb.	Description	Abb.	Description	Abb.	Description
bp	Basis points	EPS	Earnings per share	P/E	Price-earnings ratio
CAGR	Compound annual growth rate	EV	Enterprise value	PEG	P/E ratio divided by growth in EPS
CFO	Cash from operations	FCF	Free cash flow	r.h.s.	right-hand side (for charts)
CFROI	Cash flow return on investment	FFO	Funds from operations	ROE	Return on equity
DCF	Discounted cash flow	IBD	Interest-bearing debt	ROIC	Return on invested capital
EBITDA	Earnings before interest, taxes, depreciation and amortization	P/B	Price-to-book value	YoY	Year-on-year

Source: Credit Suisse

Currency codes frequently used in reports

Code	Currency	Code	Currency	Code	Currency
ARS	Argentine peso	HKD	Hong Kong dollar	PEN	Peruvian nuevo sol
AUD	Australian dollar	HUF	Hungarian forint	PHP	Philippine peso
BRL	Brazilian real	IDR	Indonesian rupiah	PLN	Polish złoty
CAD	Canadian dollar	ILS	Israeli new shekel	RUB	Russian ruble
CHF	Swiss franc	INR	Indian rupee	SEK	Swedish krona/kronor
CLP	Chilean peso	JPY	Japanese yen	SGD	Singapore dollar
CNY	Chinese yuan	KRW	South Korean won	THB	Thai baht
COP	Colombian peso	MXN	Mexican peso	TRY	Turkish lira
CZK	Czech koruna	MYR	Malaysian ringgit	TWD	New Taiwan dollar
EUR	Euro	NOK	Norwegian krone	USD	United States dollar
GBP	Pound sterling	NZD	New Zealand dollar	ZAR	South African rand

Source: Credit Suisse

Important information on derivatives

Pricing	Option premiums and prices mentioned are indicative only. Option premiums and prices can be subject to very rapid changes: The prices and premiums mentioned are as of the time indicated in the text and might have changed substantially in the meantime.
Risks	Derivatives are complex instruments and are intended for sale only to investors who are capable of understanding and assuming all the risks involved. Investors must be aware that adding option positions to an existing portfolio may change the characteristics and behavior of that portfolio substantially. A portfolio's sensitivity to certain market moves can be heavily impacted by the leverage effect of options.
Buying calls	Investors who buy call options risk the loss of the entire premium paid if the underlying security trades below the strike price at expiration.
Buying puts	Investors who buy put options risk loss of the entire premium paid if the underlying security finishes above the strike price at expiration.
Selling calls	Investors who sell calls commit themselves to sell the underlying for the strike price, even if the market price of the underlying is substantially higher. Investors who sell covered calls (own the underlying security and sell a call) risk limiting their upside to the strike price plus the upfront premium received and may have their security called away if the security price exceeds the strike price of the short call. Additionally, the investor has full downside participation that is only partially offset by the premium received upfront. If investors are forced to sell the underlying they might be subject to taxing. Investors shorting naked calls (i.e. selling calls but without holding the underlying security) risk unlimited losses of security price less strike price.
Selling puts	Put sellers commit to buying the underlying security at the strike price in the event the security falls below the strike price. The maximum loss is the full strike price less the premium received for selling the put.
Buying call spreads	Investors who buy call spreads (buy a call and sell a call with a higher strike) risk the loss of the entire premium paid if the underlying trades below the lower strike price at expiration. The maximum gain from buying call spreads is the difference between the strike prices, less the upfront premium paid.
Selling naked call spreads	Selling naked call spreads (sell a call and buy a farther out-of-the-money call with no underlying security position): Investors risk a maximum loss of the difference between the long call strike and the short call strike, less the upfront premium taken in, if the underlying security finishes above the long call strike at expiration. The maximum gain is the upfront premium taken in, if the security finishes below the short call strike at expiration.
Buying put spreads	Investors who buy put spreads (buy a put and sell a put with a lower strike price) also have a maximum loss of the upfront premium paid. The maximum gain from buying put spreads is the difference between the strike prices, less the upfront premium paid.
Buying strangles	Buying strangles (buy put and buy call): The maximum loss is the entire premium paid for both options, if the underlying trades between the put strike and the call strike at expiration.
Selling strangles or straddles	Investors who are long a security and short a strangle or straddle risk capping their upside in the security to the strike price of the call that is sold plus the upfront premium received. Additionally, if the security trades below the strike price of the short put, investors risk losing the difference between the strike price and the security price (less the value of the premium received) on the short put and will also experience losses in the security position if they owns shares. The maximum potential loss is the full value of the strike price (less the value of the premium received) plus losses on the long security position. Investors who are short naked strangles or straddles have unlimited potential loss since, if the security trades above the call strike price, investors risk losing the difference between the strike price and the security price (less the value of the premium received) on the short call. In addition, they are obligated to buy the security at the put strike price (less upfront premium received) if the security finishes below the put strike price at expiration.

Source: Credit Suisse

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