

## Liquid Real Assets – Recap & Outlook

### Third Quarter 2021

#### IN A NUTSHELL

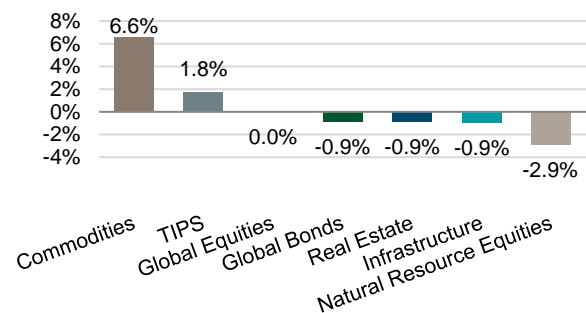
- At the beginning of 2021, we expected a reflationary environment to be beneficial and higher nominal interest rates to be driven by both rising inflation and strong economic growth.
- Heading into the fourth quarter of 2021, a Quad 2 scenario is most probable (i.e. accelerating YoY growth and inflation). In this environment, shorter-duration, growth-oriented segments remain our preferred exposures while the re-opening continues to offer tactical opportunities in certain sectors.
- Overall, we believe stable real asset classes and companies with quality fundamentals and earnings resilience will provide the best risk-adjusted returns.

### Summary

Broader equity markets ended the third quarter flat after retreating sharply in September. For most of the period, optimism over the global economic recovery and vaccination progress was balanced by concerns over increasingly restrictive Chinese regulations, inflationary pressures, and Delta variant worries as case counts (and associated death counts) in the U.S. ramped up. Markets continued rising steadily through August, supported by strong corporate earnings, renewed recovery optimism, and dovish Fed signals, before giving back all quarter-to-date gains during the month of September on signs of distress across China's real estate market and as the U.S. Federal Reserve took a decidedly hawkish tone, driving up bond yields and prompting a broad market sell-off. Against this backdrop, Commodities were the standouts for the second quarter running as gains across the Energy sector lifted overall asset class returns into positive territory. Natural Resources slipped on weakness across Metals & Mining, but were similarly supported by strength from Oil & Gas producers. Meanwhile, Global Real Estate and Infrastructure securities lagged, succumbing to broader market pressures with losses led by the European and U.S. regions amidst a surge in government bond yields. Within Infrastructure, energy segments were largely spared while communications names slipped.

Looking ahead, we contend that the timing and size of the U.S. Federal Reserve's tapering agenda has already been fully discounted by global market participants. We remain focused on the high probability of a Quad 2 economic regime, characterized by both GDP and CPI growth accelerating, for 4Q21. In this environment, we expect shorter-duration, growth-oriented sectors will be in favor.

#### 3Q 2021 INDEX PERFORMANCE RECAP



Source: DWS Group, Bloomberg. As of 9/30/21.

**Commodities** = Bloomberg Commodity Index; **TIPS** = Barclays U.S. TIPS Index; **Global Equities** = MSCI World Index; **Global Bonds** = Bloomberg Barclays Global Aggregate Index; **Real Estate** = FTSE EPRA/NAREIT Developed Index; **Infrastructure** = Dow Jones Brookfield Global Infrastructure Index; **Natural Resources Equities** = S&P Global Natural Resources Index.

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# Global Infrastructure

We are positive on improving fundamentals for transports and energy, supported by longer term re-opening trends and favorable energy supply/demand dynamics

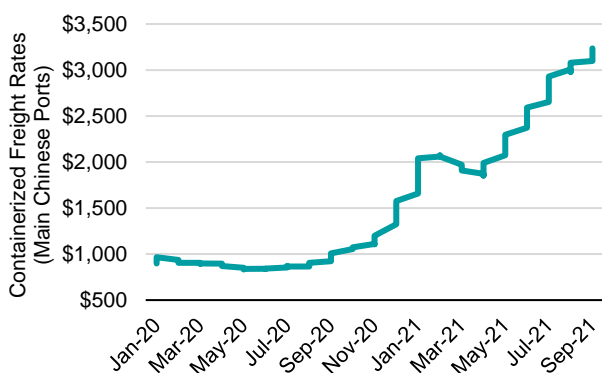
Global infrastructure securities posted a -0.9%<sup>[1]</sup> return in 3Q. Across the U.S., the Rail segment led losses while Communications names were also amongst the weakest performers as broader market pressure was felt acutely amongst technology-oriented sectors. Additionally, Utilities were generally out of favor as bond market activity signaled a risk-on shift towards quarter-end. Conversely, Waste and Transports were well-bid against an improving travel/mobility backdrop. In addition, Midstream Energy producers were supported given a strong, positive energy demand backdrop as supply concerns abound.

Within the Midstream Energy sector, volumes remain strong, and through 2021 we expect an accelerating backdrop for their fundamentals. Despite some deceleration expected in 2022, future growth is expected to be positive with excess cash flows being returned to shareholders, and we expect relative valuations and fundamentals to offer tactical opportunities, whereas quality and ESG factors should facilitate longer-term stable growth. We continue to favor stocks with quality assets and are seeking signs of a sustainable recovery to provide greater conviction in certain names. We expect Transports to benefit from a resurgence in fundamental growth drivers, though the pace of recovery is uneven. Select airports appear attractively valued, but the Omicron virus, and more specifically government response

functions, could create some near-term uncertainty on traffic recovery. Toll roads with high-quality assets should remain well bid, and we specifically favor companies with congestion-based pricing. U.S. Regulated Utility fundamentals are stable, but diverse business profiles require selective exposure. In Europe, we are concerned near-term from mixed utility valuations and uncertain policy measures, and we favor the electric grid companies over the gas companies. Across the globe, we expect select utilities stand to benefit from favorable policy that supports enhancing transmission and electric distribution grids and where policy is in place to increase spending on renewable energy projects and electric vehicle charging stations.

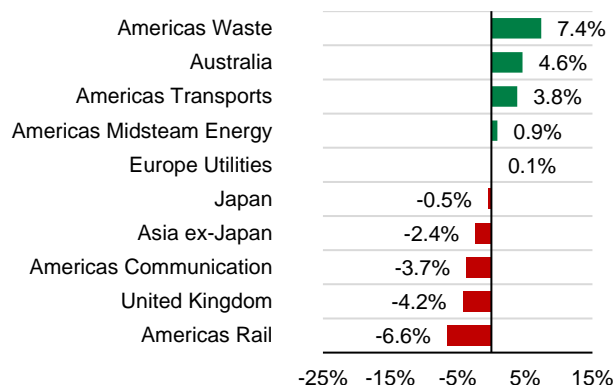
Looking ahead, we expect performance dispersion to continue across companies, regions, and sectors as the global economy regains its footing. As we enter the fourth quarter, we expect accelerating growth and inflation to provide incremental support for more cyclical, growth-oriented names. We remain positive longer-term on improving fundamentals for sectors such as Transports and Energy, which are further supported by re-normalization of growth and favorable energy supply/demand dynamics. Additionally, broader market volatility may offer tactical opportunities for stable names at attractive valuations.

## FREIGHT RATES – SHANGHAI SHIPPING EXCHANGE



Sources: Bloomberg, DWS Group. As of 9/30/21.

## 3Q 2021 TOP & BOTTOM PERFORMING SECTORS



Sources: Bloomberg, DWS Group. As of 9/30/21.

<sup>[1]</sup> Index = Dow Jones Brookfield Infrastructure Index. As of September 30, 2021

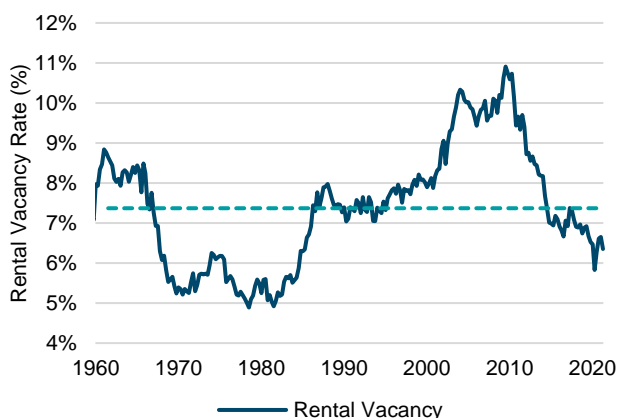
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# Global Real Estate

We expect shorter-duration, cyclical-oriented property stocks to be in favor as we navigate an economic regime where interest rates, on average, have historically risen

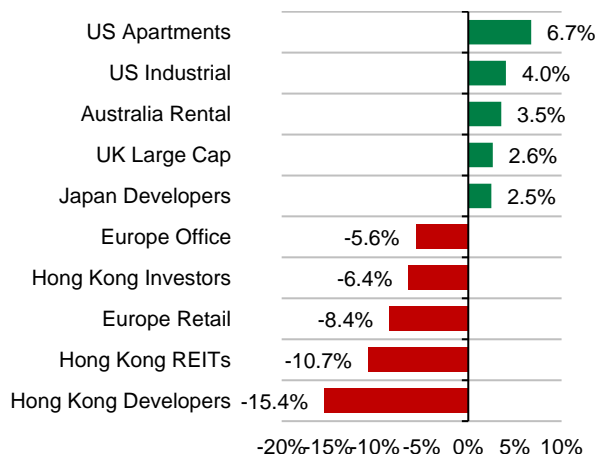
Global real estate securities returned -0.9%<sup>1</sup> in 3Q, tracking broader equities. Across the real estate landscape, we remain optimistic given continued re-opening trends and strong secular growth drivers across select real estate sectors. We continue to focus on valuations and the likelihood of cash flows to recover to pre-Covid-19 levels as a framework to assess potential opportunities.

## TIGHT RENTAL MARKET FOR U.S. APARTMENTS



Sources: U.S. Census Bureau (BOC) and DWS Group. As of 9/30/21.

## 3Q 2021 TOP & BOTTOM PERFORMING SECTORS



Sources: Bloomberg, DWS Group. As of 9/30/21

In the U.S., REITs performance was mixed during the quarter. Growth segments fared best, namely Apartments, Industrial, and Self Storage, while positive re-opening sentiment saw Retail and Regional Malls similarly well-bid. Recently, apartment fundamentals have improved rapidly with low vacancies and rents on the rise while mall traffic and strip center fundamentals have also shown signs of improvement. This was somewhat offset by losses across Healthcare, Hotels, and Net Lease. Healthcare players are being tested in the absence of government support as rising labor costs threaten further strain. The Net Lease sector's defensive, bond-like profile was also out of favor.

European property stocks were also somewhat mixed. The UK property stocks were the standouts during the quarter against a positive re-opening backdrop. The large cap names were particularly well-bid in this environment while niche players also managed gains. Meanwhile, across Continental Europe, losses were broad-based with Retail, Office, and Residential names the weakest performing segments while Nordic and diversified names managed modest gains. The retail environment in Europe remains challenged, while Office also remains under pressure.

Across Asia Pacific, concerns over COVID-19 and geopolitics continue to be balanced by undemanding valuations, post-pandemic recovery prospects, and capital management initiatives (i.e. buybacks and privatizations). In Hong Kong, property stocks were pressured in Q3 as the health of Chinese real estate markets was called into question, but have since begun to stabilize after China suggested it would ease local bond issuance rules. In Japan, balance sheets appear healthy compared to the previous downcycle. Within Australia, we expect ongoing volatility as the re-opening continues to develop.

Longer-term, we believe performance for public (listed) real estate to ultimately be driven by the pricing and fundamentals of their underlying assets. While broader sector-level themes may influence regional property market performance, we maintain that stock selection will likely be the key driver going forward in this market.

<sup>1</sup> Index = FTSE EPRA/NAREIT Developed Index. As of September 30, 2021

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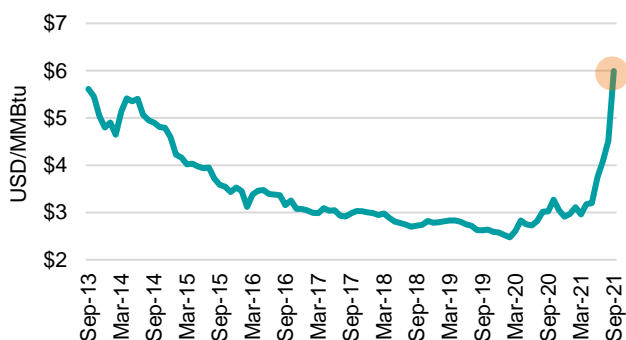
# Commodities

While geo-political risks remain, recovery momentum and prospects for higher and stickier inflation are providing price support across most commodity sectors

Commodities pushed higher during 3Q, returning +6.6%<sup>2</sup> and leading gains across real assets classes. During the quarter, gains were led again by the Energy sector as Natural Gas prices surged on a combination of tight supply and as electricity shortages from higher summer temperatures and unexpected declines in hydroelectric capacity led to a significant rise in demand. China faces further electricity rationing heading into the winter season. Meanwhile, in Europe, concerns abounded as to whether Gazprom would be able to deliver more gas for the winter season as the company continued to step out of auctions for spot and near-term delivery. Elsewhere across the complex, drawdowns in Crude Oil inventories across the U.S. prompted moves higher across oil and oil products.

Fed set the stage for sooner-than-expected rate increases. Silver took the hardest hit while Gold found some support on safe haven buying driven by Evergrande risks. Across the Agricultural complex, performance was mixed. Cotton prices jumped on a potential shortfall of production out of India coupled with booming global consumer demand while the grains complex pulled back as COVID-19 concerns stifled demand. Livestock ended another volatile month down on a similarly weak demand outlook.

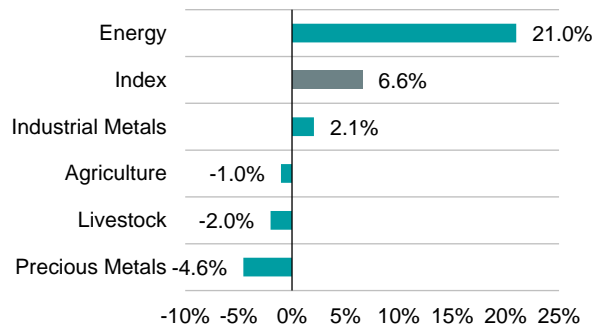
## NATURAL GAS PRICES SOAR ON SUPPLY CONCERNS



Sources: Bloomberg, DWS Group. As of 9/30/21.

Industrial Metals managed modest gains after Aluminum prices spiked following tightened restrictions on energy usage in China. Nonetheless, the complex saw increased pressure during the quarter as investors weighed the impact on Chinese property of the fallout from Evergrande’s financial troubles. Additionally, while electricity rationing also reduces steel supply, it has the opposite effect on Nickel and Zinc, where steel production is considered as demand. Given the expected decline in stainless steel demand from the property sector, Nickel prices declined along with Copper as a strong USD and inflation outlook weighed. The balance of sectors slipped, led down by the Precious Metals complex as a hawkish

## 3Q 2021 SECTOR PERFORMANCE



Sources: Bloomberg, DWS Group. As of 9/30/21.

Looking ahead, within the Energy sector, we expect Crude Oil prices will remain supported on robust recovery driven demand and as OPEC+R remains firmly in control over the path of production increases in the coming months. On Natural Gas, Russia appears willing to send additional volumes and we have already seen prices begin to correct. Base Metals have stabilized and we see supportive conditions for the complex ahead. For Precious Metals, the Fed’s plan to remove monetary support will be a negative headwind for Gold prices, but inflation fears are sustaining some interest. Lastly, while we expect Agriculture prices to remain volatile, we remain constructive on grains given global energy constraints and fertilizer production disruptions. While geopolitical events remain a risk, prospects for higher inflation are providing support. Given that most commodities will have limited growth of supply, we expect supply/demand fundamentals to improve across the Commodities space over the long-term.

<sup>2</sup> Index = Bloomberg Commodity Index. As of September 30, 2021.

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# Natural Resource Equities

Near-term, we believe current macroeconomic conditions favor natural resource equities above other sectors.

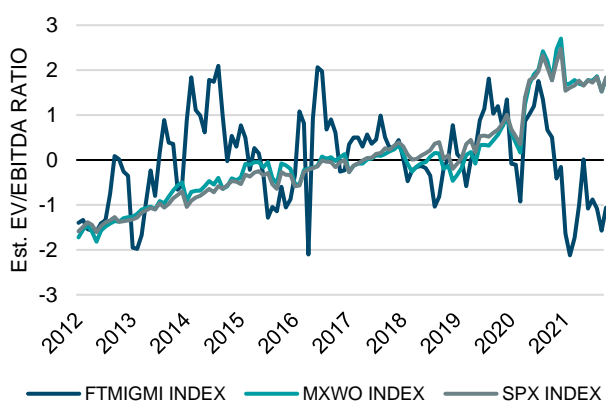
Natural Resource Equities lagged during the second quarter, posting losses of -2.9%<sup>3</sup>. Weakness was most pronounced across Metals & Mining, but this was somewhat mitigated by strength amongst Oil & Gas producers.

Elevated Commodities returns during Q2-Q3 reflected the one-time impact of the economic re-opening. Going forward, the rate of increase is likely to moderate to reflect trend growth by 2022. Equity pricing continues to reflect the market's expectation of the present value of future growth, as well as the immediate demand increase reflected in Commodities prices over the past two quarters. Investment for additional capacity across the complex remains subdued as natural resources companies are being encouraged by investors to pay out positive cashflow via dividends or stock buy-backs rather than invest in growing new capacity. Turning to Metals producers, we expect tightness in thermal coal to keep supply pressure on base metals and support prices. We expect that supply constraints from reduced capital spending will help to support base metals producers. Meanwhile, strong cost control has allowed Precious Metals & Mining companies to take advantage of rising Gold prices to expand margins and reduce leverage. With balance sheets in the best shape in over a decade, Gold miners are positioned to fund growth. Elsewhere across the space, depressed auto demand is keeping a lid on Platinum and

Palladium prices. Also of note, as steel production data in China continues to show a declining trend, we are cautious on steel producers in this environment. Turning to the Energy sector, given current market dynamics amidst an ongoing global energy supply crunch, we expect energy producers to be well-supported heading into the winter quarter and remain on the lookout for tactical opportunities across the space. Finally, within Agriculture, improving export demand coupled with very strong processing margins in nearly every region lead us to be increasingly optimistic on demand. Fertilizer production remains disrupted, with shortages in prime agricultural regions like India and Brazil. We remain constructive on Agricultural Chemicals and Products companies. Meanwhile, across the North American Paper & Forestry sector, strong growth expectations and increased spending from manufacturers and consumers is being balanced by persistent supply chain disruptions.

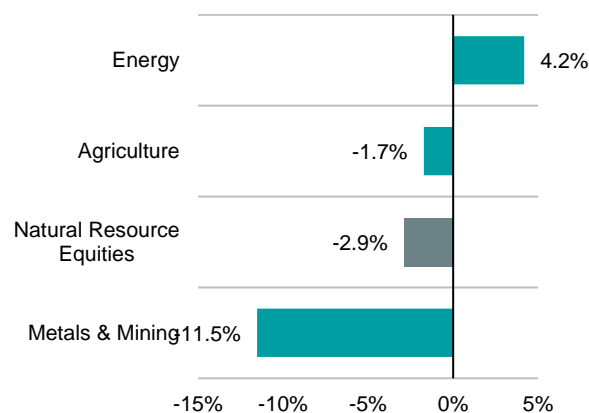
Looking ahead, we continue to expect natural resources companies to focus on delivering yield rather than capex as the primary driver for allocating free cash flow. As we enter the fourth quarter, we continue to emphasize stock selection in this environment. We remain focused on names with visible growth catalysts, as well as shorter-term tactical opportunities across the space.

## COMPELLING RELATIVE VALUE IN GOLD EQUITIES



Sources: Bloomberg, DWS Group. As of 9/30/21.

## 3Q 2021 SECTOR PERFORMANCE



Sources: Bloomberg, DWS Group. As of 6/30/21.

<sup>3</sup> Index = S&P Global Natural Resources Index. As of September 30, 2021.

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