INVIEW

MONTHLY GLOBAL HOUSE VIEW & INVESTMENT PERSPECTIVES

DECEMBER 2023

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The icons alongside represent our investment process. Through a disciplined provision of investment policy and security selection at the global level, regional portfolio management teams have the flexibility to construct portfolios to meet the specific requirements of our clients.

HIGHLIGHTED IN THIS PUBLICATION:

GLOBAL STRATEGIC ASSET ALLOCATION

GLOBAL SECURITY SELECTION

REGIONAL ASSET ALLOCATION

REGIONAL PORTFOLIO CONSTRUCTION

Editorial

Welcome to the December edition of *Inview: Monthly Global House View*. In this publication we consider significant developments in the world's markets, and discuss our key convictions and themes for the coming months.

Moz Afzal
Chief Investment Officer

After three negative months, market sentiment turned overwhelmingly positive in November with the MSCI World index rallying by 9.2%, one of the best monthly performances in history. The index is now close to the highs of the year seen at the end of July. Government bonds also posted gains of more than 3% for the month as yields fell sharply. Performance since the beginning of the year therefore remains firmly in positive territory for shares and has also become positive again for bonds.

There are two main reasons behind the recent market rise. First, the fear of an escalation of tensions in the Middle East has gradually receded, something that has helped encourage the decline in oil and natural gas prices. The second reason is that inflation has fallen by more than expected across several countries and it appears likely that this trend will continue, not least because of lower energy prices. If so, inflation could return to central banks' objectives as early as next year.

As a result, monetary policy expectations for 2024 have been drastically revised, as evidenced by interest rate futures that are now pricing in rate cuts as early as the second quarter of next year. Long-term government bond yields have declined in response and are now back to September levels. At the same time, a more dovish central bank outlook has been a catalyst for the recovery in share prices.

The asset allocation of a diversified portfolio should favour a slight overweight on both equities and bonds. Conventional and inflation protected sovereign bonds remain attractive at current yield levels, as do investment grade corporate bonds. Equities will likely benefit from favourable seasonality in the next few weeks, although the gains will be more moderate than in November. Equity market valuations are generally supportive, particularly for European markets, where an overweight exposure seems warranted in our view.

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Global Allocation

Based on a balanced mandate, the matrix below shows our 6-12 month view on investment strategy

Given the strong market performance of markets in November, portfolio drift has been significant. As a result, we are rebalancing our exposures, increasing slightly fixed income to keep a slight overweight and also taking profits marginally within equities to maintain the level of overweight and capture some of the strong momentum in markets expected into the end of the year. January is historically a positive month for equities so we expect a rally in early 2024 and would wait until then before scaling back our overweight equity positioning. An equity market sell-off could be triggered in late Q1/Q2 if the Federal Reserve doesn't turn as dovish as markets expect. For reference, US interest rate futures are currently pricing the first rate cut as early as March 2024 with five rate cuts expected by the end of next year. Futures markets expect the ECB to behave similarly to the US Federal Reserve next year in terms of both the timing and the number of cuts. The US yield curve is expected to steepen through the year as longer end yields remain supported by the large US fiscal deficit while the shorter end rallies in sympathy with lower policy rates.

	Allocation versus the benchmark	Weighting change from last month*
FIXED INCOME	+	↓
EQUITIES	+	↑
ALTERNATIVES	–	↓
CASH & MONEY MARKET	–	↔
FX	●	↔

– Underweight + Overweight ● Neutral

↔ No change ↑ Increase ↓ Decrease

*Note that arrows reflect any adjustment to allocation weighting and is not necessarily a full upgrade or downgrade.

Fixed Income

No changes are being made to the sub-sectors in fixed income this month. We continue to favour sovereign bonds, with duration maintained at around 6.5 years. There is a preference for the middle part of the curve, while the normalization of the yield curve and pressure from investors keeps us more cautious on the long end. Exposure to indexed-linked bonds should be considered given higher real yields for USD and GBP portfolios. We maintain a positive view on investment grade bonds and convertibles, while we remain cautious on high yield credit despite the good performance of the asset class this year.

		Allocation versus the benchmark	Weighting change from last month
	Rates	+	↔
USD	Investment Grade	+	↔
USD	Sovereign	+	↔
EUR	Investment Grade	+	↔
EUR	Sovereign	+	↔
GBP	Investment Grade	–	↔
GBP	Sovereign	+	↔
CHF	Investment Grade	+	↔
CHF	Sovereign	+	↔
	Credit	–	↔
USD	High Yield	–	↔
EUR	High Yield	–	↔
	Hybrids	–	↔
	Asset-backed Securities	–	↔
	Convertibles	+	↔
	EM Local Currency	●	↔
	EM Hard Currency	–	↔

– Underweight + Overweight ● Neutral

↔ No change ↑ Increase ↓ Decrease

Equities

We remain positive on European equities, noting an improvement in technical factors. In Japan, valuations have become more stretched in comparison to other markets, but we continue to hold a slight overweight. The developments in the Japanese yen will be an important component for this market going into 2024. According to the EFGAM model, US stocks are currently at around fair value given strong recent market performance, while earnings revisions in the US, particularly communication services and consumer discretionary remain strong. The environment in Switzerland has deteriorated, with a more negative macro picture, neutral valuations and negative technical factors. This was reflected in our views last month, following the decision to reduce our allocation to Swiss equities.

	Allocation versus the benchmark	Weighting change from last month
North America	●	↔
Europe	+	↔
UK	●	↔
Switzerland	–	↔
Asia ex-Japan	–	↔
China & Hong Kong	●	↔
India	↔	↓
Indonesia	+	↔
Korea	↔	↑
Malaysia	–	↔
Philippines	–	↔
Taiwan	–	↓
Thailand	–	↔
Other	+	↔
Japan	+	↔
Latin America	+	↔
EMEA	●	↔
Thematic/Global	●	↔

– Underweight + Overweight ● Neutral

↔ No change ↑ Increase ↓ Decrease

Equity Sector Views

UK

Industrials is the largest sector overweight within our UK exposure, taking advantage of the de-rating seen across the sector to pick up quality companies. We favour more internationally exposed companies in the sector over those more reliant on domestic UK business.

Global oil demand is back above pre-Covid levels and at the same time OPEC has continued to control supply via production cuts. The UK energy majors trade at much more attractive valuation levels than their international peers and so we overweight the energy sector.

The consumer staples sector has demonstrated resilient earnings through this period of high inflation as it has been able to price ahead of rising costs in raw materials and labour while also keeping volumes stable. However, recent earnings have shown a shift in price elasticities, with several companies reporting weaker volumes and offering more cautious guidance for the future. With this in mind, we remain underweight in UK consumer staples.

Equity Sector Views *(cont.)*

US

We are overweight in specific technology and consumer discretionary stocks and encouraged by recent signs of public cloud spending bottoming. After a year of IT budget optimisation, public cloud spending (and digital adoption in general) is poised to reaccelerate again later this year. We are also enthused by the prospects of artificial intelligence. We are also more positive on life science tools within healthcare. Headwinds related to pharma/biotech spending rationalisation and inventory destock, post-Covid normalisation and China macro weakness, which have played out over the last 9-12 months have stabilised. Overall, we have a barbell positioning with longer duration high quality growth barrelled with more defensive names. We have underweights in the more cyclical sectors like energy and materials.

Europe

Within sectors, we have reduced our financials exposure, where we are underweight with a focus on banks and insurance. We see limited scope for further earnings upgrades on net interest income/investment yields as terminal rate expectations in Europe have declined. Provisions and liquidity risks, primarily related to real estate, cannot be overlooked. We previously increased exposure to communication services, consumer staples, healthcare and technology sectors, having an overweight position in all of these sectors, focusing capital on the highest quality, most defensive parts of the European market.

Asia ex-Japan

We see the IT cycle turning, with restocking in smartphones and PCs. We remain neutral around China and Hong Kong, with consumer activity remaining weak but further property support. Within India, property and industrial trends remain stronger than the consumer, with the rural consumer a particular weak spot.

Alternatives

No changes were made to our alternatives exposure this month, following a previous upgrade of insurance linked securities to neutral and a downgrade to commodities. We maintain an underweight to commodities, with gold the only current area of interest, while copper or palladium may become more attractive in our view in the new year. We continue to be overweight to hedge funds relative to the neutral allocation.

	Allocation versus the benchmark	Weighting change from last month
Hedge Fund	+	↔
Private Markets	●	↔
Real Assets	●	↔
Commodity	–	↔
Insurance	●	↔

– Underweight + Overweight ● Neutral

↔ No change ↑ Increase ↓ Decrease

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