



Global Asset Allocation: The View From the UK

March 2023

1 Market Perspective



- Global growth is proving resilient in the face of tighter monetary policies; however, impacts of central banks' tightening are still expected to weigh on the economic growth and earnings outlook in the back half of the year.
- Despite declining goods inflation, services inflation remains sticky on the back of higher wages, keeping the US Federal Reserve and other central banks hawkish.
- While uncertainty remains, optimism surrounding China's reopening and resilient growth in Europe, supported by declining energy costs, could help buoy the global economy.
- Key risks to global markets include central bank missteps, resilient inflation, steeper growth decline resulting in a hard landing and geopolitical tensions.

2 Portfolio Positioning

As of 28 February 2023



- We remain underweight equities and bonds in favour of cash. Equity valuations remain extended in the face of tightening liquidity and slowing growth. Bond yields are likely to remain volatile amid mixed economic data and central bank policy shifts, while cash offers attractive yields and stability.
- Within equities, we are overweight areas with more attractive valuation support such small-/mid-caps, Japan and emerging markets (EM). We also maintain a broad balance between value and growth—with a modest overweight to value—to reduce exposure to extreme interest rate sensitivity and cyclicalities.
- Within fixed income, we remain overweight emerging market bonds, where yields still offer reasonable compensation for risks despite persistent market volatility.

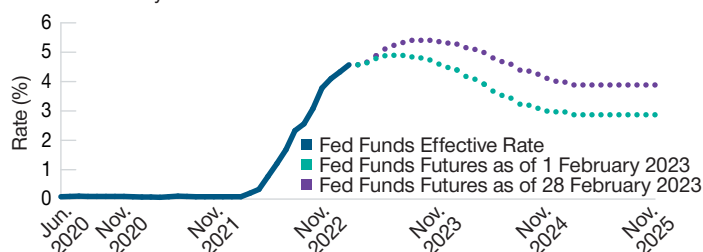
3 Market Themes

Too Hot to Handle

Recent good news on consumer spending, sentiment and employment has been bad news for the US Fed as they are not seeing evidence that aggressive rate hikes are having the intended impacts in slowing growth and reining in inflation. Markets had started the year positively on signs of peaking central bank tightening; however, the positive sentiment quickly faded as expectations for the path of future rate hikes jumped in response to the hotter data. Over the course of February, the futures market went from projecting the fed funds rate to peak at 4.90% in June to a projected peak of 5.41% in October. Having already raised rates by 450 basis points over the past year, the Fed is hopeful that the lagged effects will help them reach their inflation target of close to 2%, but if the economic data keep coming in strong, the Fed may find it too hot to handle and need to step up the tightening. The months ahead are likely to be volatile as every bit of data will be scrutinised by investors hoping for just enough bad economic data to please Fed officials, yet not bad enough to signal that a hard landing is imminent.

Fed Funds Rate Expectations Have Adjusted Higher

As of 28 February 2023



Past performance and hypothetical performance are not reliable indicators of future performance. Actual performance will vary, perhaps materially, from the performance shown. The performance of the hypothetical portfolio does not include fees or costs. If these fees were deducted from the returns shown, the returns would be lower.

Figures shown in USD.

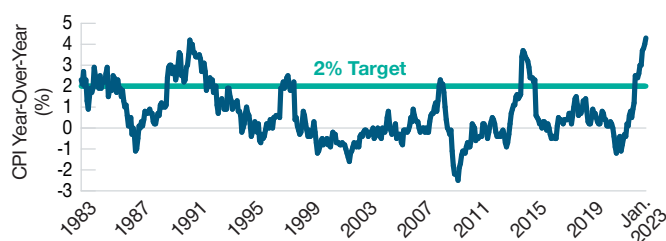
Source: Bloomberg Finance L.P.

Last One Standing

Bank of Japan (BoJ) Governor Haruhiko Kuroda is set to step down in early April after a decade in office, with markets speculating that ultra-easy monetary policies he oversaw may be ending. The bank had already surprised markets when it eased yield curve controls at the end of last year, allowing rates to rise more. With inflation running near 4.3%, a 40-year high, the BoJ has been the last major central bank standing firm with ultra-easy policy, while almost all others pivoted to aggressive rate hikes to fend off high inflation. With his expected replacement, Kazuo Ueda, coming into office amid high inflation, it is likely Mr Ueda will begin to take further steps to unwind ultra-easy policy. While stocks and bonds have broadly declined in the face of higher inflation and rates, Japanese markets may benefit as assets are repatriated back home, where they are now able to earn higher yields. For investors outside of Japan, a stronger yen supported by higher yields could provide a further boost to Japanese market returns. Although inflation has not been a friend to investors elsewhere, the Japanese market may be one area where investors welcome it.

Japan Seeing Decades-High Inflation

40 Years Ended 31 January 2023





REGIONAL BACKDROP

Positives

Negatives

Europe

U

- Unusually warm winter has driven energy costs lower
- Fiscal spending is rising
- Equity valuations remain attractive, despite recent rally

- Inflation remains elevated, particularly core inflation
- Monetary policy remains restrictive
- Heightened geopolitical uncertainty due to the war in Ukraine

United Kingdom

N

- Energy cap benefitting household finances
- Inflation expectations have reverted to normal
- The UK labour market remains resilient

- The Bank of England may be forced to hike more than expected
- Fiscal consolidation may weigh further on demand in 2023
- A recession and house price declines in 2023 appear likely

United States

U

- Corporate and consumer balance sheets remain strong
- The labour market has been extremely resilient
- Services sector remains remarkably strong

- Recession risk remains elevated
- Inflation has proven more persistent than expected
- Labour supply remains scarce

Japan

O

- Equity valuations remain very attractive
- Gradual monetary policy normalisation
- Lower commodity prices and a stronger yen are lowering the inflation impulse

- Expectations in earnings are prone for disappointment
- Accelerating wage growth is making gradual monetary policy normalisation difficult
- A stronger yen may weigh on the export sector

Asia Pacific ex-Japan

N

- China's reopening proved faster than anticipated
- Equity valuations are undemanding, relative to the US
- In Australia, China's reopening has boosted earnings expectations; the economy remains broadly resilient

- Given the strength of the reopening thus far, Chinese policy may become less supportive
- Geopolitical risks remain elevated
- Australia consumer spending is at risk with mortgage rates being reset. The Reserve Bank of Australia remains hawkish

Emerging Markets

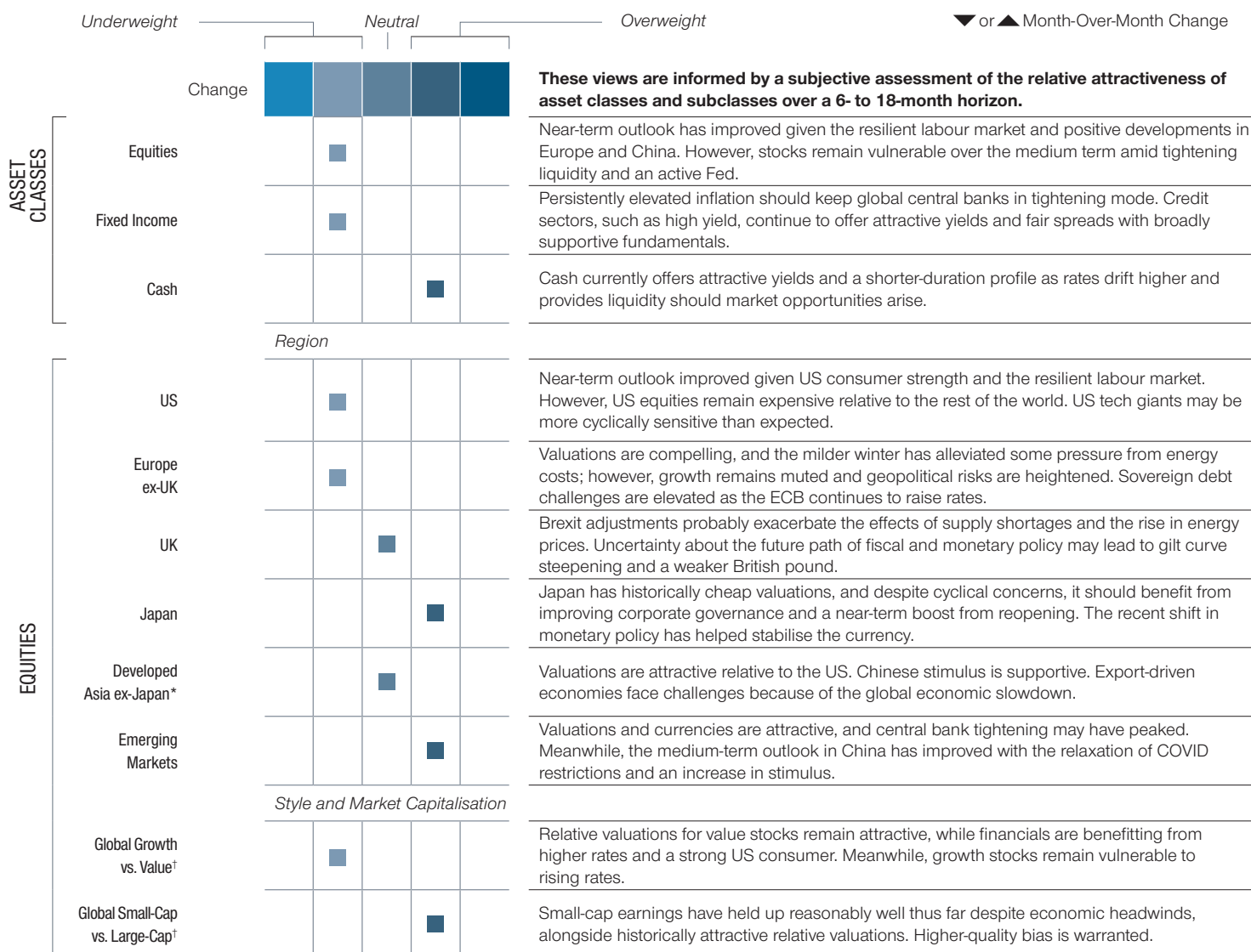
O

- China's reopening should provide a strong boost to growth in emerging markets
- Equity valuations are attractive relative to the US
- Central banks tightening is likely to have peaked

- Exports to developed markets are weakening as global growth is slowing
- Chinese housing concerns remain a structural headwind
- Geopolitical uncertainty remains elevated

U Underweight **N** Neutral **O** Overweight

Past performance is not a reliable indicator of future performance.



* Includes Australia.

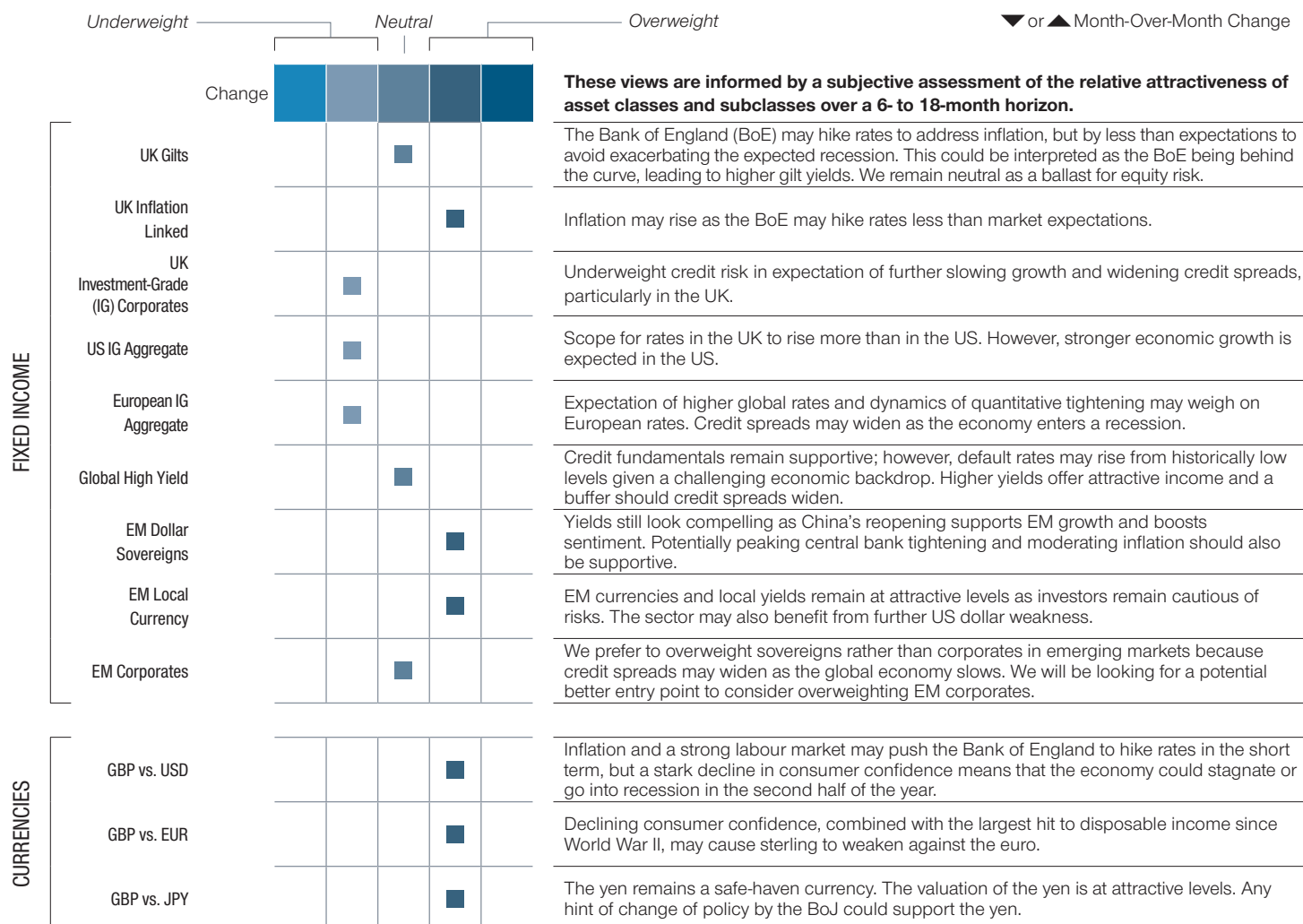
† For pairwise decisions in style and market capitalisation, positioning within boxes represents positioning in the first-mentioned asset class relative to the second asset class.

The asset classes across the equity and fixed income markets shown are represented in our multi-asset portfolios. Certain style and market capitalisation asset classes are represented as pairwise decisions as part of our tactical asset allocation framework.



UK INVESTMENT COMMITTEE POSITIONING

As of 28 February 2023



The specific securities identified and described are for informational purposes only and do not represent recommendations.



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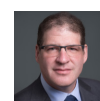
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