T. Rowe Price

Global Asset Allocation: The View From Europe

December 2023

1 Market Perspective

- Given asynchronous trends in growth and inflation policy, divergence is expected in 2024.
- European economic growth and inflation are trending lower, giving the European Central Bank flexibility. The Bank of Japan is expected to tighten policy in the first half of the new year. Despite increasing evidence of softening inflation, US Federal Reserve Chair Jerome Powell reiterates the pledge to hold rates higher. Chinese growth is incrementally improving, aided by stimulus support.
- Key risks to global markets include central bank missteps, a deeper retrenchment in growth, sticky inflation, a trajectory of Chinese growth and geopolitical tensions.

2 Portfolio Positioning

As of 30 November 2023

- We have a balanced view on equities supported by positive earnings trends and more attractive valuations beyond narrow leadership, against a backdrop of softening growth and still high interest rates. We remain overweight areas of the market with supportive valuations, such as small-caps, Japanese equities, global high yield bonds and emerging market debt.
- Within equities, we remain overweight US large-cap growth due to the continued strength of technology and artificial intelligence, US small-caps because of attractive valuations, and Japan due to the reflationary story and governance improvements. Europe ex UK remains an underweight due to slowing growth and restrictive monetary policy.
- Within fixed income, we remain modestly overweight cash relative to bonds. Cash continues to provide attractive yields and liquidity to take advantage of potential market dislocations.
- Within fixed income, we remain overweight high yield and emerging market bonds on still attractive absolute yield levels and reasonably supportive fundamentals.

3 Market Themes

A November to Remember

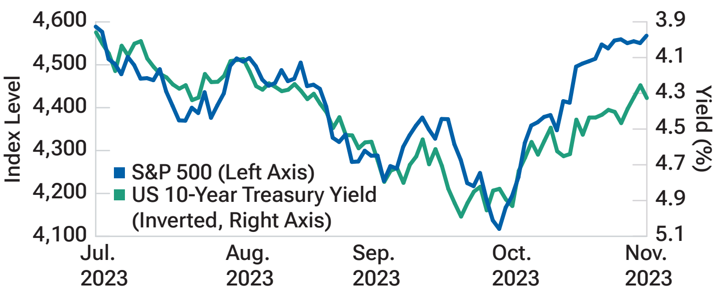
November was a banner month for stocks and bonds, with the S&P 500 Index up close to 9%—its seventh best month over the last 30 years—and US 10-year Treasury yields rallying over 50 bps, as the market interpreted cooling inflation data as an indication that the Fed could begin easing policy earlier than anticipated. Further evidence of lower consumer spending, a softening labour market and a continued downshift in PMIs further supported the narrative that tighter financial conditions are finally taking hold. Despite the market's euphoria over November's bad news possibly pulling forward rate cuts, Fed Chair Powell ended the month reiterating that the Fed is committed to holding rates higher and is not ready to declare victory on inflation just yet. The year 2024 is setting up to be a critical year for the Fed, not wanting to make a similar policy mistake as it did over the coronavirus pandemic by not getting ahead of 'transitory' inflation. While Powell may keep policy tight to ensure he stamps out inflation, it could be at the expense of not acting soon enough and allowing the lagged effects of monetary policy to push the economy into a recession. This tough decision may be made more complicated with the upcoming election.

Home for the Holidays!

For want-to-be homeowners who had hoped to be in a new home for the holidays, September's new record in home prices was not welcomed news. A lack of supply due to existing homeowners' unwillingness to leave their current low rate mortgage for much higher rates has been the main reason for the shortage. And while mortgage rates are off their October highs, a 30-year fixed mortgage is still near 7.5%, well above the average current outstanding rate of 3.7%. The modest decline in rates, however, has been met with an increase in new listings which can help ease tight supply. Should the Fed start to lower rates next year as the market is expecting, that could be a welcomed sign for the housing market in enticing existing homeowners to sell and helping on the affordability front for buyers. The outstanding question is where will home prices be by the holidays next year—as lower rates typically mean higher prices? Hopefully this holiday brings homebuyers a surge in supply; otherwise, they may be still wishing for a new home next year too.

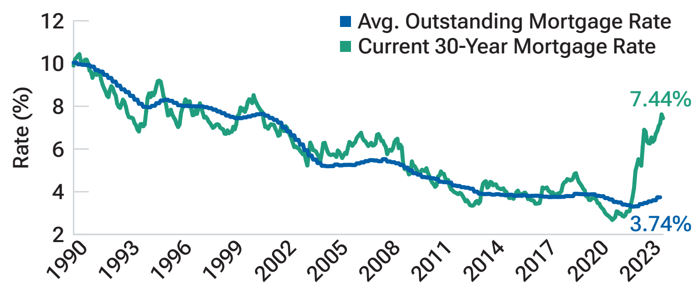
Stocks and Bonds Reversed Course Sharply in November[1]

As of 30 November 2023



Average Outstanding Mortgage Rate Remains Low[2]

As of 30 November 2023



Past performance is not a reliable indicator of future performance.

[1] Sources: Bloomberg L.P. and S&P. Please see Additional Disclosures for more information about this sourcing information.

[2] Source: Haver Analytics.

REGIONAL BACKDROP

		Positives	Negatives
Europe	U	– Inflation is cooling faster than expected – European Central Bank (ECB) may be finished hiking – Labour market has been resilient	– Inflation remains elevated, particularly core inflation – Economic growth is slowing – Monetary policy is restrictive
United Kingdom	N	– Inflation has begun to moderate – Bank of England (BoE) may be finished hiking – Labour market has been resilient	– Fiscal consolidation may need to be accelerated – Tight labour markets could keep wage inflation elevated – BoE may be forced to keep rates higher
United States	O	– Consumer spending remains strong – Labour market has been resilient – Fiscal spending has supported capex – Earnings expectations are increasing	– Monetary policy remains very tight – Banking sector concerns will impact credit availability – Economic data have been surprising to the downside
Japan	O	– Economy is benefitting from uptick in inflation – Corporate governance continues to gradually improve – Equity valuations remain very attractive	– Monetary policy is becoming incrementally tighter – Yen weakness has weighed on equity market returns – Earnings expectations may need to be revised lower
Asia Pacific ex-Japan	N	– Economic activity in China is incrementally improving with supportive policies expected to continue – Sentiment is uniformly bearish towards China, suggesting that contrarian investors could benefit from cheap valuations – In Australia, resilient housing and jobs markets support the wealth effect. The government also has firepower to add fiscal stimulus if needed	– In China, property deleveraging remains an overarching goal, which dampens domestic activity – China consumer and business confidence are fragile, and saving is being prioritised over spending – Higher interest payments in Australia will negatively impact consumer spending with a lag. Corporate earnings forecasts are lower than other regions
Emerging Markets	N	– Monetary tightening in most emerging markets (EM) has peaked – Equity valuations are attractive relative to the US – Chinese stimulus is expected to continue	– Global trade is relatively weak given tighter monetary conditions – Chinese property deleveraging continues to weigh on activity – Chinese consumer and business confidence are fragile

U Underweight N Neutral O Overweight

Views are informed by the Asset Allocation Committee and regional investment committees (United Kingdom, Europe, Australia, Japan and Asia) and reflect the equity market.

EUROPEAN INVESTMENT COMMITTEE POSITIONING

As of 30 November 2023

▼ or ▲ Month-Over-Month Change

These views are informed by a subjective assessment of the relative attractiveness of asset classes and subclasses over a 6- to 18-month horizon.

		Change	*Underweight*		*Neutral*	*Overweight*		
ASSET CLASSES	Equities				■			Valuations are broadly neutral with pockets of opportunity amid slow global growth and higher rates. Improving earnings are supportive, but the trajectory of economic growth remains uncertain.
	Fixed Income	▼		■				Despite the recent rate rally, yields are attractive with central banks likely past peak tightening. However, volatility could persist amid increased supply and sticky inflation. Credit fundamentals remain supportive, although spreads are fairly priced.
	Cash	▲				■		Cash continues to offer attractive yields as central banks remain broadly higher for longer and provide liquidity should market opportunities arise.
	Region							
EQUITIES	US					■		Earnings expectations are improving and economic activity remains resilient, with technology innovation a key differentiator. However, valuations are full and higher rates are pressuring companies with high interest expense.
	Europe ex-UK			■				European equity valuations remain relatively attractive, headline inflation has fallen noticeably and the economy is showing signs of slowing, easing pressure to hike rates further. However, with core inflation proving stubbornly elevated, the ECB policy bias remains restrictive.
	UK				■			Equity valuations are appealing relative to history and major peers. Core inflation has fallen, while signs of economic slowdown potentially ease inflationary pressure. However, domestic factors, such as Brexit adjustments and growth in average wages, are inflationary and may keep rates at higher levels for a while longer.
	Japan					■		Japanese stocks are favoured due to the reflationary story and governance improvements. Company valuations and earnings also remain attractive. However, Japanese companies are highly geared to a global economy that is slowing in the near term. Earnings expectations may also disappoint should the yen appreciate.
	Developed Asia ex-Japan*				■			China economic activity is incrementally improving. Policymakers appear focused on the level of growth, implying that supportive policies should continue. However, leading indicators for export sectors continue to be weak, while the overarching goal of deleveraging property is dampening domestic activity.
	Emerging Markets				■			Valuations and currencies are attractive, and central bank tightening may have peaked. The medium-term outlook in China is improving, with incrementally better economic activity. However, business and consumer confidence remain fragile, and saving is being prioritised over spending.
	Style and Market Capitalisation							
	Global Growth vs. Value†					■		A tilt towards higher-quality businesses is warranted given lingering economic concerns and rising rates. Momentum surrounding artificial intelligence and weight loss drugs could provide a structural tailwind to growth, although valuations are extended.
	Global Small-Cap vs. Large-Cap†					■		Small-caps offer attractive relative valuations but face margin concerns due to higher exposure to interest rates and higher input costs. Given heightened economic uncertainty, higher-quality bias is warranted.

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.

EUROPEAN INVESTMENT COMMITTEE POSITIONING

As of 30 November 2023

Underweight — *Neutral* — *Overweight*   ▼ or ▲ Month-Over-Month Change

These views are informed by a subjective assessment of the relative attractiveness of asset classes and subclasses over a 6- to 18-month horizon.

	Change	Underweight		Neutral		Overweight	
FIXED INCOME	Euro Government Bonds		■				The ECB may be done with rate hiking. Bond supply may increase due to energy compensation. High-quality duration can mitigate some risks given the decreasing likelihood of the global economy dodging a recession.
	Euro Inflation Linked			■			Inflation is expected to ease further as the economy slows down. The labour market, however, remains tight, and potential rising energy prices in the winter may become inflationary.
	Euro Investment-Grade (IG) Corporates				■		Euro investment-grade credit offers good value over the short term.
	US IG Aggregate		■				After the recent fall in rates, retracement is expected. Resilient growth, increased bond issuance and Fed policy remaining tight may put upward pressure on rates. However, easing inflation and the US economy losing momentum could see downward rate pressure.
	Global High Yield				■		Attractive yield and reasonable spread levels remain supportive. Default rates are likely to rise to historical long-term averages, although much appears to be priced in.
	EM Dollar Sovereigns				■		Yields are still attractive, with peaking central bank tightening cycles and moderating inflation supportive.
	EM Local Currency				■		EM local bond and currencies attractive. Expectations for central bank easing, lower inflation and a softer dollar could be supportive.
	EM Corporates			■			We prefer to overweight sovereigns rather than corporates in emerging markets because credit spreads may widen as the global economy slows. We will be looking for a better entry point to consider overweighting EM corporates.
CURRENCIES	EUR vs. USD				■		In a benign market environment, we expect the US dollar to soften—in particular, as the U.S. economy shows signs of slowing down, interest rate differentials are expected to remain steady and the dollar is expensive.
	EUR vs. JPY		■				The yen remains a safe-haven currency. The valuation of the yen is at attractive levels. Any further changes of policy by the Bank of Japan could support the yen.

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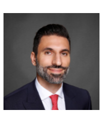
The specific securities identified and described are for informational purposes only and do not represent recommendations.

EUROPEAN INVESTMENT COMMITTEE



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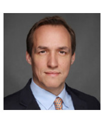

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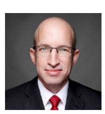

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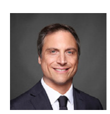

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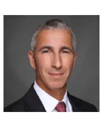

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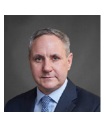

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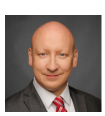

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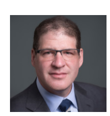

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INVEST WITH CONFIDENCE™

T. Rowe Price identifies and actively invests in opportunities to help people thrive in an evolving world, bringing our dynamic perspective and meaningful partnership to clients so that they can feel more confident.

Additional Disclosures

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