Global Asset Allocation: The View From the UK

September 2024

1 Market Perspective

- Trends in recent data are more decisively pointing to slowing growth alongside easing inflation pressures, with a soft landing still within grasp as central banks pivot to easing.
- In the US, economic data are showing signs of cooling, particularly in the labour market. European growth remains modest and bolstered by services, whilst manufacturing lags. Japanese growth rebounds from contraction earlier in the year are supported by exports. Chinese growth remains stagnant, with policymakers remaining measured with stimulus support.
- A US Federal Reserve (Fed) cut this September is highly anticipated as focus shifts from inflation to the labour market. The European Central Bank (ECB) looks to advance easing as inflation data provide support. The Bank of Japan (BoJ) signals commitment to its divergent path of rates hikes, with a cautious eye on currency impacts. The Bank of England (BoE) is likely to cut at a quarterly pace, but probably less than priced into the market.
- Key risks to global markets include a steeper decline in growth, central bank policy missteps, election calendars, geopolitical tensions and the trajectory of Chinese growth.

2 Portfolio Positioning

As of 31 August 2024

- Whilst valuations are broadly extended, we remain modestly overweight equities that should benefit from easing monetary policy and still resilient, albeit slowing, economic growth.
- We maintain an overweight to cash relative to bonds. Cash yields should remain at attractive levels even as the BoE embarks on easing as we expect a gradual path.
- Within equities, we remain overweight value based on more attractive relative valuations, whereas narrowly led growth equities are extended and susceptible to weakness on earnings disappointments. Supportive global central bank easing should provide a backdrop for broader market participation.
- Within fixed income, we continue to favour higher-yielding sectors, including high yield and emerging markets (EM) bonds as fundamentals remain broadly supportive.

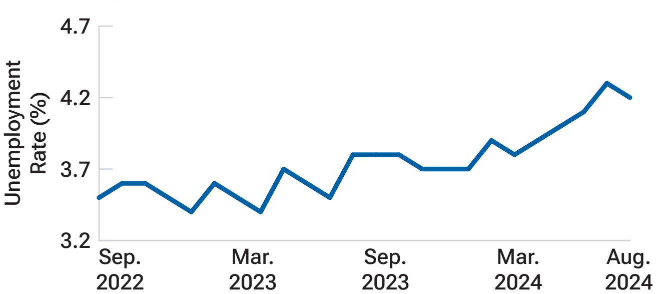
3 Market Themes

What Lies Beneath?

US consumer confidence rebounded in August on optimism about the resilience of the economy and easing inflation pressures. And whilst markets cheered the rosier outlook of the all-important US consumer, a deeper dive into the survey data suggests there are growing concerns, particularly about declining labour market conditions. Employment data have turned decisively cooler recently, with the unemployment rate climbing and jobs becoming less abundant. With the survey data also showing consumers remaining very concerned about their personal finances, any further deterioration in jobs could lead to a quickening pullback in spending. This is particularly weighing on lower-income consumers facing higher prices and now turning more to credit cards as excess savings accumulated during the pandemic have been depleted. And whilst higher-income consumers have been buffered by rising 401(k) balances and elevated home prices, their propensity to consume could turn quickly as well if layoffs broaden. Let's hope that rate cuts have been well timed to allow for a cooling of the labour market rather than too late and already facing the risk of a sinking US consumer.

US Unemployment Rate Has Been Ticking Up[1]

As of 31 August 2024

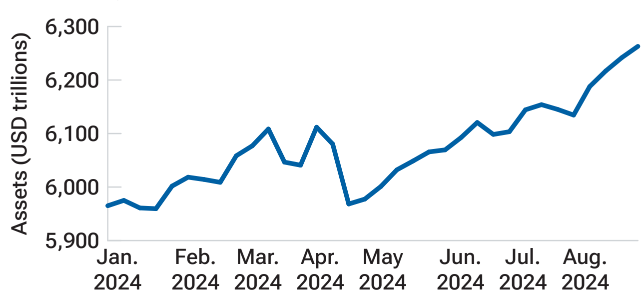


Sidelined

Despite market expectations for an unwinding of the huge pile of money market assets to provide a tailwind as they flow back to risk assets, the category has continued to garner flows, hitting an all-time high of USD 6.6 trillion in August. Whether it's extended equity valuations, concerns over bond market volatility or simply still attractive 5% yields keeping investors on the sidelines, they have seemed wary to jump back into risk assets. Unfortunately, those investors parked in money markets awaiting an opportunity have missed out on a huge equity rally, with the S&P 500 returning more than 20% over the past year. And for those more conservative investors who may have considered inching out into longer-maturity bonds, they too have missed out more recently on a major rally in yields. Perhaps the start of rate cuts on the horizon could entice some investors to come off the sideline, but with a gradual path priced in, it is unlikely to have a huge impact. And for those who remember earning 0% in money markets not too long ago, still getting over 4% could remain compelling for a while longer.

Money Market Assets Reaching New Highs[2]

As of 31 August 2024



Past performance is not a reliable indicator of future performance.

[1] U-3 US Unemployment Rate total in labour force is seasonally adjusted.
[2] Assets are sourced from ICI Money Market Funds Assets.
Source: Bloomberg Finance L.P.

REGIONAL BACKDROP

		Positives	Negatives
United Kingdom	N	– The BoE has begun cutting rates – Inflation has been steadily declining – Economic growth outlook has stabilised	– Fiscal consolidation may need to be accelerated – Tight labour market could keep wage inflation stubbornly high
Europe	U	– Monetary policy expected to ease further – Inflation has been steadily declining	– Economic growth remains weak – Geopolitical uncertainty remains heightened – Earnings growth remains weak, with minimal tailwinds from innovative technologies
United States	O	– Monetary policy expectations are improving – Resilient corporate earnings – Wage growth is moderating to sustainable levels – Recent inflation reports have been favourable	– Stock valuations have become challenging – Economic data have been surprising to the downside – Consumption trends are weakening – Political uncertainty is heightened
Japan	O	– Economic indicators are pointing to a reflationary environment – Corporate governance improvements are resulting in stronger company fundamentals – Stock valuations are attractive	– Heightened volatility may reduce investor appetite – The BoJ may maintain a hawkish bias due to inflation – The unwind of the carry trade positions highlights the risk of the extreme positioning in the yen
Asia Pacific ex-Japan	N	– China macro data are showing resilience, especially export sectors – Monetary easing in China is part of an incremental loosening approach – In Australia, government support to the economy continues to be a net positive	– Prolonged China deflation remains a concern whilst property market issues challenge growth – Consumer spending in China tier 1 cities is depressed, and earnings forecasts are unattractive – Australia market pricing appears to be too optimistic about future rate cuts
Emerging Markets	N	– Monetary policy is loosening in many emerging markets – A weaker US dollar favours emerging markets	– Chinese property deleveraging continues to weigh on activity – Meaningful fiscal stimulus measures appear unlikely – Export demand from developed markets has slowed

U Underweight N Neutral O Overweight

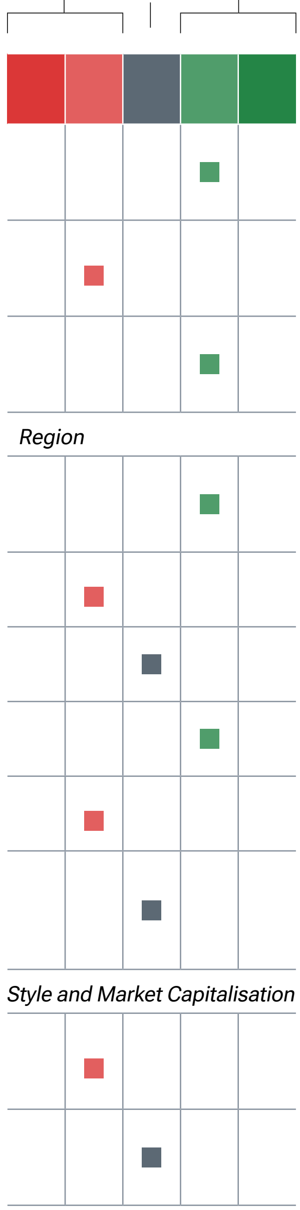
Views are informed by the Asset Allocation Committee and regional investment committees (United Kingdom, Europe, Australia, Japan and Asia) and reflect the equity market.

UK INVESTMENT COMMITTEE POSITIONING

As of 31 August 2024

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.

ASSET CLASSES

Equities	Potential for multiple expansion on anticipated Fed cuts; however, already elevated valuations may limit upside. Concerns about peaking artificial intelligence (AI) spending and economic uncertainty could remain headwinds.
Fixed Income	Markets have priced in weaker growth and moderating inflation, driving dovish central bank expectations. Credit fundamentals remain supportive; however, spreads remain tight.
Cash	Despite a recent shift downward on the back of expectations for BoE cuts, cash still provides attractive yields as the yield curve remains inverted and offers liquidity should market opportunities arise.

EQUITIES

Region

US	Valuations are elevated, particularly for mega-cap tech stocks. However, monetary policy easing could stimulate broader economic activity and earnings growth. Technology and pharmaceutical innovation remain key differentiators.
Europe ex-UK	Valuations remain relatively attractive, and economic activity has bottomed. However, economic growth remains weak.
UK	Valuations are appealing. A resilient labour market and Brexit adjustments are inflationary. The new Labour government is expected to be fiscally prudent.
Japan	Economic indicators are reaching new highs in this cycle. Corporate governance improvements continue to support Japanese company fundamentals.
Developed Asia ex-Japan[1]	In Australia, government support to the economy continues to be a net positive. However, market pricing appears to be too optimistic about future rate cuts.
Emerging Markets	EM stock and currency valuations are attractive, monetary policy is loosening in many developing markets and a weaker US dollar favours EM. However, Chinese property deleveraging continues to weigh on activity and meaningful fiscal stimulus measures appear unlikely.

Style and Market Capitalisation

Global Growth vs. Value[2]	Easing monetary policy expectations should be supportive of rate-sensitive sectors. Meanwhile, growth stocks face elevated expectations, challenging valuations and growing AI scepticism.
Global Small-Cap vs. Large-Cap[2]	Small-caps offer attractive relative valuations and could continue to benefit from dovish tilt in Fed expectations. However, small-caps could be challenged by a cooling economic growth backdrop.

Past performance is not a reliable indicator of future performance.

[1] Includes Australia.

[2] 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 31 August 2024

▼ or ▲ Month-Over-Month Change

		Change	Underweight		Neutral	Overweight		**These views are informed by a subjective assessment of the relative attractiveness of asset classes and subclasses over a 6- to 18-month horizon.**
FIXED INCOME	UK Gilts			■				Recovering economic activity, persistent services inflation, the BoE cutting less than market expectations, accelerating quantitative tightening, large gilt issuance and US spillovers may keep yields under pressure.
FIXED INCOME	UK Inflation Linked					■		Inflation indicators (services, wages) remain elevated, although the UK labour market has eased a little.
FIXED INCOME	UK Investment-Grade (IG) Corporates				■			Investment grade credit is looking less attractive in terms of valuations, given the tight nature of spreads.
FIXED INCOME	US IG Aggregate			■				Stubborn inflation and a resilient economy could see the Fed cutting rates fewer times than the market expects. Meanwhile, investment grade spreads remain tight.
FIXED INCOME	European IG Aggregate			■				Expectation of higher global rates and dynamics of quantitative tightening may weigh on European rates. Credit spreads could widen if the economy slows down.
FIXED INCOME	Global High Yield					■		Overall yield levels remain attractive, fundamentals are supportive and default expectations are anticipated to remain near long-term averages. However, upside beyond carry from further spread compression is limited.
FIXED INCOME	EM Dollar Sovereigns					■		Yields look modestly attractive; however, higher-quality sovereign spreads look tight. The backdrop is constructive as central banks embark on easing cycles and inflation continues to moderate.
FIXED INCOME	EM Local Currency					■		Central bank easing and lower inflation could be tailwinds, along with increasing prospects of a rate cut.
FIXED INCOME	EM Corporates				■			We currently prefer to overweight emerging market sovereigns rather than corporates as credit spreads may widen as the global economy slows.
CURRENCIES	GBP vs. USD	▼			■			In a benign market environment, the US dollar may soften, particularly from current expensive levels. The Fed is likely to cut less than market expectations.
CURRENCIES	GBP vs. EUR					■		The ECB is likely to cut rates more than the BoE to support economic growth.
CURRENCIES	GBP vs. JPY				■			Interest rate differentials continue to favour the GBP. However, given recent volatility in the yen, we prefer to remain neutral.

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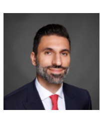
The specific securities identified and described are for informational purposes only and do not represent recommendations.

UK INVESTMENT COMMITTEE



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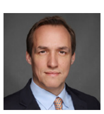

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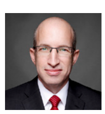

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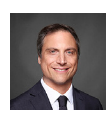

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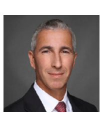

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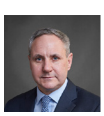

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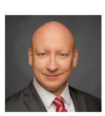

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Additional Disclosures

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