Global Asset Allocation: The View From the UK

November 2024

1 Market Perspective

- Economic data continue to show signs of resilience, and inflation remains on a moderating path, providing room for further easing.
- US data are holding up, confirming a soft landing as inflation nears the target. European growth remains modest and bolstered by services, while manufacturing lags. Japanese growth is modestly slowing as manufacturing output has softened. Chinese stimulus is expected to continue to bolster growth, though impacts so far have been modest. UK growth has slowed, but surveys indicate re-acceleration.
- The path of Fed cutting is largely dependent on incoming data, while the European Central Bank (ECB) looks to advance easing as inflation data provide support. The Bank of Japan (BoJ) signals commitment to their divergent path of rate hikes. The Bank of England (BoE) is likely to continue to cut its policy rate.
- Key risks to global markets include elevated geopolitical tensions, central bank policy missteps and the path of Chinese growth.

2 Portfolio Positioning

As of 31 October 2024

- We remain modestly overweight to equities on a favourable outlook centred around easing monetary policy, Chinese stimulus measures and potential for broadening earnings growth.
- Within equities, we remain overweight large-cap value based on more attractive valuations and potential for broader market participation, and modestly overweight to large-cap growth as it should continue to see durable earnings growth from several high-quality companies.
- Also, within equities, we remain neutral in emerging markets following the recent rally in China. Although Chinese stimulus should continue to provide a tailwind, potential policy shifts create uncertainty.
- We neutralised the overweight to cash relative to bonds. While cash yields remain attractive even as the BoE embarks on easing, we used cash to reduce the underweight to gilts to take profits and add resilience should economic growth slow more than expected.
- Within fixed income, we neutralised the overweights to global high yield bonds and emerging markets bonds because spreads are tight and we used to proceeds to neutralise the underweight to US Treasuries.

3 Market Themes

Checks and balances

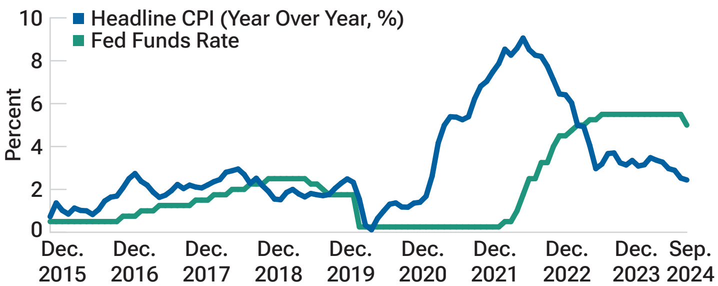
The markets' immediate reaction to President Donald Trump's victory has, for the most part, played out as if his new term will take off where his last ended. A lot, however, has changed in the past four years, and executing on many of his campaign promises—including higher tariffs and deregulation—could bring about inflationary pressures. When the president first took office in 2016, inflation was low and central banks had policy rates anchored at near zero levels in an effort to increase inflation. That's not so today, as inflation is just finally nearing central bank targets, policy rates and bond yields are at much higher levels and deficit spending has only grown. Because it is now looking increasingly possible that Republicans may also sweep both houses of Congress, market reaction is reflecting the increasing likelihood that Republicans will be able to quickly act on their agenda. While there will undoubtedly be significant changes in policy coming, it may be the forces of higher inflation and rates that prove to be the checks and balances that keeps some discipline in policy.

Earning their share

While the S&P 500 Index has continued to deliver strong earnings, it has been primarily driven by the performance of the 'Magnificent 7', which has reflected that versus the broader market. And with their earnings now starting to slow from extreme levels on moderating spending in artificial intelligence (AI), investors are beginning to look at the 'other 493', which are seeing encouraging signs of earnings growth. This broadening began in the second quarter and has continued into the third quarter on the back of better economic growth and easing monetary policy. And while the direction is encouraging, their earnings are only moving up to low single digits from negative levels, while the Magnificent 7 are still expected to deliver growth near 20% levels. Despite the earnings backdrop still favouring the Magnificent 7, still resilient economic growth, easing monetary policy and now potential changes in fiscal and regulatory policies could provide tailwinds to companies beyond the Magnificent 7—giving them a better shot at earning their share.

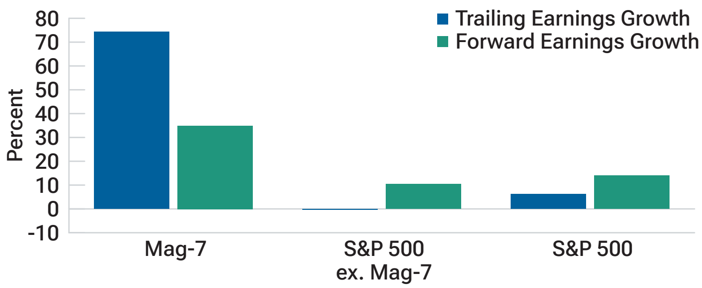
Facing higher inflation and rates today

As of 30 September 2024



Earnings growth differentials beginning to compress

As of 31 October 2024



Past performance is not a reliable indicator of future performance.
Source: Bloomberg Finance L.P.

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REGIONAL BACKDROP

		Positives	Negatives
United Kingdom	N	– Monetary policy is expected to ease further – Inflation concerns have moderated – Economic growth outlook has stabilised	– Fiscal consolidation may need to be accelerated – While the labour market is slowly becoming less tight, it could keep wage inflation stubbornly high – Domestically generated inflation is too persistent
Europe	U	– Monetary policy is expected to ease further – Unemployment remains low – Equity valuations are attractive	– Economic growth remains weak – Geopolitical uncertainty remains heightened – Earnings growth is structurally weak
United States	O	– The Fed has begun cutting rates – Resilient corporate earnings – Recent inflation reports have been favourable – Earnings have been boosted by AI infrastructure spending	– Stock valuations have become challenging – Consumption trends are weakening
Japan	O	– The reflationary environment continues – Corporate governance continues to improve – Weaker yen is boosting earnings forecasts	– Political instability is impacting foreign investment flows – The BoJ will maintain a hawkish bias due to strong wage growth – Manufacturing indicators are weak due to a drop in global demand
Asia Pacific ex-Japan	N	– A coordinated policy response in China creates a short-term rally opportunity from extreme bearish sentiment and cheap valuations – More fiscal measures are expected by year-end to support Chinese domestic consumption – In Australia, government support to the economy continues to be a net positive	– China's housing sector faces structural challenges that will take time to recover – China's corporate earnings prospects may undermine the rally as policy measures will take time to flow through – Australian market pricing appears too optimistic about future rate cuts; elevated valuations and weak earnings forecasts are not supportive of the domestic market
Emerging Markets	N	– China has enacted coordinated stimulus efforts – Chinese stimulus has positively impacted investor sentiment – Monetary policy is loosening in many emerging markets	– Chinese property deleveraging continues to weigh on activity – Export demand from developed markets remains muted – Geopolitical risks are rising

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 October 2024

▼ 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					■		Despite elevated valuations, we see potential for broadening of earnings growth as developed market central banks cut rates. Questions remain around AI momentum, economic growth and geopolitical tensions.
	Fixed Income			■				Yields have moved higher on resilient growth and potential for increased fiscal spending; however, moderating inflation and further central bank easing could bias yields lower from here. Credit fundamentals remain supportive, but spreads remain tight.
	Cash	▼			■			Despite a recent shift downward on the back of BoE easing, cash still provides attractive yields and offers liquidity should market opportunities arise.
	Region							
EQUITIES	US					■		Monetary policy easing could stimulate broader economic activity and earnings growth. Technology and pharmaceutical innovation remain key differentiators, although valuations remain elevated.
	Europe ex-UK			■				Valuations remain attractive. Services inflation is volatile and might surprise on the upside. Economic activity is likely to stay weak, improving over a medium-term view.
	UK				■			Valuations are appealing. Domestically generated inflation is too persistent, but the labour market is slowly becoming less tight, and core goods inflation could slip into deflation. Surveys indicate a re-acceleration of economic growth.
	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 is positive. Consumer activity has rebounded, thanks to a resilient job market. The Reserve Bank of Australia could pivot to a more hawkish tone.
	Emerging Markets				■			Emerging markets (EM) stock and currency valuations are attractive. China's government policy is supportive. However, geopolitical tensions with the US could rise.
	Style and Market Capitalisation							
	Global Growth vs. Value[2]			■				Easing monetary policy has been supportive of rate-sensitive sectors and could lead to earnings broadening. 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 with support from a dovish tilt in Fed expectations. However, a modest economic growth backdrop could pose a challenge.

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 October 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.

		Change	Underweight		Neutral	Overweight		
FIXED INCOME	UK Gilts			■				Recovering economic activity, persistent services inflation, accelerating quantitative tightening, large gilt issuance and US spillovers may keep yields under pressure.
	UK Inflation Linked					■		Inflation indicators (services, wages) remain elevated, although the UK labour market has eased a little.
	UK Investment-Grade (IG) Corporates				■			Investment grade credit is looking less attractive in terms of valuations, given the tight nature of spreads.
	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.
	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.
	Global High Yield	▼			■			Yield levels are attractive, fundamentals supportive and default expectations should remain near long-term averages. However, upside beyond carry is limited.
	EM Dollar Sovereigns	▼			■			Yields look modestly attractive; however, higher-quality sovereign spreads appear tight. Central banks are easing and inflation continues to moderate.
	EM Local Currency					■		Central bank easing and stronger currencies could provide a tailwind.
	EM Corporates				■			We currently prefer to overweight EM 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.
	GBP vs. EUR					■		The ECB is likely to cut rates more than the BoE to support economic growth.
	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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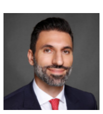
The specific securities identified and described are for informational purposes only and do not represent recommendations.

UK INVESTMENT COMMITTEE



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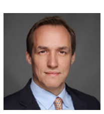

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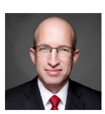

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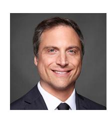

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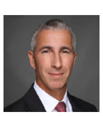

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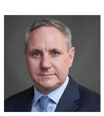

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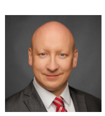

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T. Rowe Price identifies and actively invests in opportunities to help people thrive in an evolving world, bringing our dynamic perspective and meaningful partnership to clients so that they can feel more confident.

Additional Disclosure

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