INVIEW

GLOBAL HOUSE VIEW & INVESTMENT PERSPECTIVES

AUGUST 2021

DISCIPLINED BY NATURE. FLEXIBLE BY DESIGN.
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 flexiblility 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 August edition of *Inview: 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

Equity markets have continued to rally in the summer months, supported by various factors. While the rise in US inflation was unexpectedly strong in the spring, investors are increasingly wondering whether it is now peaking. Several things point in this direction. In particular, PCE inflation has been broadly constant and PCE core inflation fell in the second quarter of the year. And commodity prices have recently weakened. Oil prices are about 10 percent off their recent peak and agricultural commodity prices have also fallen. Furthermore, what matters for inflation is the rate of change, typically on an annual basis, and this will most likely moderate in the remainder of 2021 and in early 2022.

It is also true that the very low inflation rates recorded in the spring of 2020 have now dropped out of the 12 month inflation calculation. These base effects are expected to put downward pressure on inflation for several months, although the path towards lower inflation will be volatile.

Market sentiment has also been supported by evidence of ongoing recovery in economic activity. GDP growth exceeded expectations in the second quarter of 2021 and survey data point to a continued solid expansion also in the current quarter. Markets cheered at the positive news, although strong data also carries the risk of an earlier withdrawal of policy support.

The debate about tapering the Fed's monthly asset purchases is a case in point. The good news, from an investor's perspective, is that policymakers, from both the monetary and the fiscal side, have made it clear that any policy normalisation will be gradual and data dependent. With respect to US monetary policy, the forthcoming Jackson Hole symposium will likely give Chairman Powell the opportunity the clarify the timeline of policy normalisation.

In Europe, the ECB is in no hurry to reduce support for the economy. Rather, the conclusions of the strategy review presented in July seem to allow for even greater patience before considering a reversal in the current accommodative stance. The new ECB monetary policy strategy clarifies that it will aim for 2% percent inflation instead of the previous target of "below, but close to, 2%", that in setting policy it will give equal importance to deviations of inflation from the target both on the upside and the downside, and that it will tolerate inflation above the target if needed to recover from protracted economic weakness.

Very accommodative fiscal and monetary policy supports the momentum in global equities. In our view, a moderate overweight to equities is thus warranted within a diversified portfolio, with a preference for US and Asian markets. In contrast, the low level of government and corporate bond yields is unappealing; within fixed income assets, convertible bonds and hybrids are more attractive. Industrial metals and gold have recently corrected and look attractive on a fundamental basis but may be constrained by the rise of the US dollar consistent with expected tapering of asset purchases by the Fed.

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Global Asset Allocation: Summary

Equities

- European equities got off to a weak start to the third quarter although have performed better more recently. While there has been some debate on increasing allocation, for now we remain neutral.
- US growth stocks continued to outperform value, while the S&P 500 keeps hitting new highs. Company earnings have largely been upbeat and we remain overweight to the US.
- We continue to look closely at the consumer discretionary sector as it has not yet shown signs of momentum. Both energy and materials have lost their uptrend, confirming our previous cautious view on these sectors.
- There has been some discussion on reducing our Japan overweight but we believe that the low sentiment going into the Olympics could improve on any positive spill over from the games.
- The recent crackdown on large Chinese tech stocks has caused some market unease. However, we stand by our China overweight stance as the overall investment thesis remains broadly unchanged – it is one of the cheapest markets at the moment, supported by a fast recovery in earnings.

Fixed Income

- Despite fears of rising inflation, bond markets rallied and yields declined in July. Within sovereign bonds we would caution against overly long duration positions at least until yields are higher and the yield curve has steepened.
- Investment grade corporate bonds were previously downgraded to reflect the greater sensitivity to rates. A further downgrade has been considered but for now we maintain a neutral position on a risk management basis.
- Recent bank earnings have shown that loan losses so far are not as high as expected and regulators are limiting dividends and buy-backs. With this, we are tactically and strategically overweight preferred and hybrid debt.

Alternative Investments

- The EU recovery fund and a bipartisan infrastructure bill in the US are positives for the asset class so this is an area we are overweight within our alternatives positioning.
- Market volatility may bring opportunities for skillful portfolio managers to enhance performance and alpha streams in their portfolios. This view can be exploited in the directional mandates and alternative LO models.

Currencies

- Following the European Central Bank's policy review we expect it to remain dovish for longer. Both fundamental and technical indicators suggest that we should no longer maintain our tactical overweight of the euro, leading us to downgrade the currency to neutral.
- The US dollar has strengthened against most developed currencies following recent market activity and concerns over Covid-19 variants. Tactically we remain underweight.
- The UK pound, Australian dollar and Chinese renminbi are amongst our most favoured currencies, supported by signs of economic recovery.

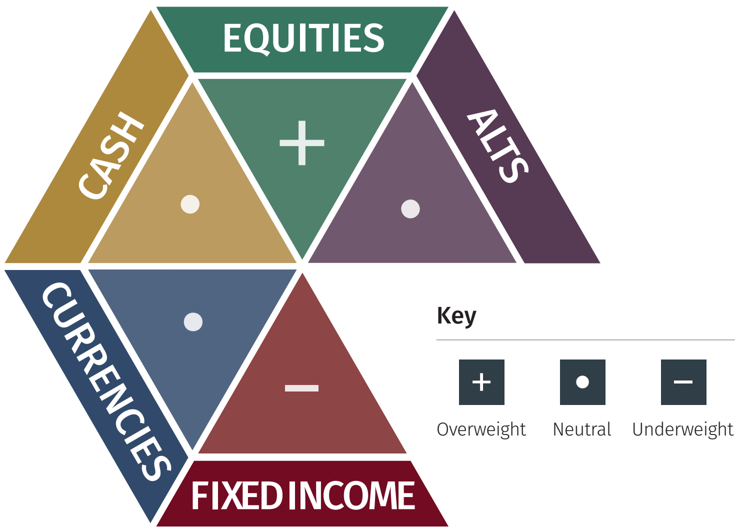
Sector allocation (✚ overweight, ▬ underweight, ● neutral)

Sector	Jul. 2021 Weight	Change	Aug. 2021 Weight
Consumer Discretionary	✚	↔	✚
Consumer Staples	●	↔	●
Energy	▬	↔	▬
Financials	●	↔	●
Healthcare	✚	↔	✚
Industrials	●	↔	●
Information Technology	✚	↔	✚
Materials	●	↔	●
Real Estate	▬	↔	▬
Telecoms	●	↔	●
Utilities	▬	↔	▬

Global Asset Allocation: 12-Month Strategic Outlook

Based on a balanced mandate, the matrix below shows our long-term house view on investment strategy.

Overall Asset Allocation Views



Asset Class Breakdown

	EQUITIES	FIXED INCOME	ALTS	CURRENCIES	CASH
+ Overweight	North America Japan Asia Pacific ex-Japan	Convertible Preferred & Hybrid	Hedge Funds Equity-Linked Hedge Funds Macro Infrastructure		
• Neutral	Europe Europe ex-UK ex-Switzerland United Kingdom Switzerland	Investment Grade Corporate High Yield Emerging Markets Other	Hedge Funds Relative Value Commodities / Mining Equity Property / REITS Insurance-linked Securites Other Volatility	USD EUR GBP AUD Asia CHF	
– Underweight	E. Europe, ME & Africa Latin America	Sovereign			Money Market Cash

Global Asset Allocation: 3-Month Tactical Outlook

Based on a balanced mandate, the matrix below shows our short-term house view on investment strategy.

Asset Class Breakdown

Note: The highlighted boxes indicate a difference from our 12-month strategic outlook.

	EQUITIES	FIXED INCOME	ALTS	CURRENCIES	CASH
+ Overweight	North America United Kingdom Japan Asia Pacific ex-Japan	Convertible Preferred & Hybrid	Hedge Funds Macro Commodities / Mining Equity Infrastructure	AUD Asia GBP	
• Neutral	Europe Europe ex-UK ex-Switzerland Switzerland	Investment Grade Corporate High Yield Emerging Markets	Hedge Funds Equity-Linked Property / REITS Insurance-linked Securites Other Volatility	EUR	
− Underweight	E. Europe, ME & Africa Latin America	Sovereign Other	Hedge Funds Relative Value	USD CHF	Money Market Cash

Equity Allocation Grid

Based on a balanced mandate, the table below provides our long-term (strategic) and short-term (tactical) house view on investment strategy.

Key

+	•	—	▲	—	▼
Overweight	Neutral	Underweight	Upgrade	No Change	Downgrade

Sub-Asset Class	Strategic 12-month		Tactical 3-month		Sub-Asset Class Additional Guidance
	View	Change	View	Change	
North America	+	—	+	—	The last few months have continued to see investor rotation, without really having an impact on the S&P 500, in fact the S&P 500 is up almost 3% over the last two months, with Value underperforming Growth in July by close to 3%. This rotation has caused angst among the professional investing community. With US bond yields peaking at 1.7% in June and with Q2 earnings results we feel that Growth stocks' expectations are quite low, relative to higher expectations for Value stocks. That said, longer term we suggest a more balanced profile given the expected strength of the economy over the course of this year and next.
Europe	•	—	•	—	European equities underperformed in the last month, although they remain up by over 11% on a year-to-date basis. The start of the third quarter has been weak in comparison to previous months as questions loom over the pace of the economic recovery. The question is whether investors will buy into the rally in the second half of year? We think they will, as Europe kicks off pandemic recovery programmes and earnings confidence continues. We will wait for a pull-back or consolidation to become more confident, especially following recent outperformance. We still have a bias towards quality growth companies as they will continue to be the long term winners. But this has been painful in the short-term as European banks continue to drive forward. Although we have re-balanced this was probably not enough.
Europe ex- UK ex- Switz.	•	—	•	—	European equities underperformed in the last month, although they remain up by over 11% on a year-to-date basis. The start of the third quarter has been weak in comparison to previous months as questions loom over the pace of the economic recovery. The question is whether investors will buy into the rally in the second half of year? We think they will, as Europe kicks off pandemic recovery programmes and earnings confidence continues. We will wait for a pull-back or consolidation to become more confident, especially following recent outperformance. We still have a bias towards quality growth companies as they will continue to be the long term winners. But this has been painful in the short-term as European banks continue to drive forward. Although we have re-balanced this was probably not enough.
United Kingdom	•	—	+	—	UK stocks fell last month as fears over the spread of the Delta variant impacted markets. We maintain our tactical overweight as we anticipate the successful vaccine roll-out, cheap valuation and a GBP that has pulled back could drive the UK markets higher. The UK economy has had a lot of challenges over the last few years principally due to Brexit and a highly exposed UK economy to the services sector during a pandemic. With the successful roll-out and clearly relief from the population with excessive savings, we do expect a strong economic response. We would have a bias to the smaller companies that are sensitive to improving conditions.

Equity Allocation Grid

Based on a balanced mandate, the table below provides our long-term (strategic) and short-term (tactical) house view on investment strategy.

Key

+	●	−	▲	—	▼
Overweight	Neutral	Underweight	Upgrade	No Change	Downgrade

Sub-Asset Class	Strategic 12-month		Tactical 3-month		Sub-Asset Class Additional Guidance
	View	Change	View	Change	
Switzerland	●	—	●	—	Swiss equities have a growth bias relative to European equities due to their defensive characteristics i.e. large index weights in consumer staples and pharma. We would proactively re-balance into mid-caps right now as we expect continued economic improvement in 2021 and also due to the stretched valuation in the larger companies.
Japan	+	—	+	—	We upgraded Japanese equities last year as the "global value" rally continued and the sensitivity of Japan to global economic conditions is very high. Stock selection in Japan has been quite critical with growth names leading last year, but there has been a clear leadership flip more recently to value companies. We would not necessarily chase this move, but it does warrant a more balanced profile going forward. We believe sentiment around Japanese assets remained low ahead of the Olympic games and any positive outcome could spill over into positive sentiment for the stock market.
Asia Pacific ex-Japan	+	—	+	—	Asia was the epicentre of the Covid-19 outbreak and was also one of the first regions to get it under control. That said, the experience has not been uniform and the markets of ASEAN and India have had to digest a steep rise in Covid-19 cases. We continue to see upward earnings revisions in China as stimulus measures are applied. The recent crackdown on the large technology companies in China does suggest a pivot towards the cyclical parts of the country. Stock valuations reflect China is currently one of the cheapest markets at the moment, consistent with recent underperformance and a fast recovery in earnings. The rest of the ASEAN markets remain underweight for us.
Eastern Europe, Middle East and Africa	−	—	−	—	Given the large drop last year and subsequent political volatility, it is difficult to see how the EMEA markets can outperform sustainably despite their relative valuations. We see these markets more as later cycle performers. Of course, quicker vaccine dissemination will lead to quicker recoveries.
Latin America	−	—	−	—	Latin American countries remain vulnerable to indifferent policy and anaemic growth trends as a result of the on-going Covid-19 pandemic. So it is hard to see how Latin America can recover quickly from the recession that the virus has created. Despite these pandemic tensions, interest rates are close to all time lows and the economic reform agenda continues to make progress. Nonetheless, relative caution is warranted in the region.

Fixed Income Allocation Grid

Based on a balanced mandate, the table below provides our long-term (strategic) and short-term (tactical) house view on investment strategy.

Key

+	●	–	▲	–	▼
Overweight	Neutral	Underweight	Upgrade	No Change	Downgrade

Sub-Asset Class	Strategic 12-month		Tactical 3-month		Sub-Asset Class Additional Guidance
	View	Change	View	Change	
Sovereign	–	–	–	–	Fixed income markets are now delicately poised as the Covid vaccine roll-out continues and confidence takes hold in the economic recovery. We have seen Gilts and European Govt's sell off and US Treasuries in a range. We are not concerned by inflation worries, noting that much of the increase in commodity prices will be transitory (i.e. base effects). We would caution overly long duration positions at least until yields are higher and the yield curve has steepened to cycle highs. A quicker move in yields will be countered by central banks who are closely monitoring inflation data.
Investment Grade Corporate	●	–	●	–	Spreads have come in dramatically over the last year encouraged by widespread central bank support. However, given that spreads have tightened substantially in the AA to A space any change in interest rates will have a greater impact. As a result we previously downgraded IG to neutral to reflect the greater sensitivity to rates. We have considered a further downgrade but we maintain a neutral position on a risk management basis.
Convertible	+	–	+	–	We stay overweight in Convertibles. The Converts space has generally performed well on a relative basis in the current environment, given the continued undervaluation of implied volatility and as investors look for equity sensitivity with a floor. We expect a decent risk / reward trade off for Converts in the current environment.
High Yield	●	–	●	–	We have been possibly too cautious on high yield debt over the last 6-months given very tight spreads and yields at all time lows. Coupon clipping is the name of the game in this environment and has kept us neutral given the zero to negative central bank rate environment we are in. There are a number of issues to consider in HY: BB+ now has greater rate sensitivity, zombie companies may have been formed due to the rate environment and finally when the economy opens we will start to see the skeletons in the closet. Over the next 3-6 months good alpha opportunities might be created, so selectivity will be key.
Preferred & Hybrid	+	–	+	–	Preferred and Hybrid debt is higher beta. However as much of it is related to the financial sector and bank debt - AT1 and Cocos for example - we feel that the asset class is more attractive than high yield. Recent bank earnings have shown that loan losses so far are not as high as expected and regulators are limiting dividend and buy-backs. So we are overweight the sector.
Emerging Markets	●	–	●	–	Similar comments to high yield, in that coupons are attractive both in hard and local currency bonds relative to zero rates. We have strong bias for China RMB bonds as yields are higher with a strengthening currency. Overall, however, selectivity is warranted given the balance of macro conditions, left wing political bias, Covid and tight spreads.

Alternatives Allocation Grid

Based on a balanced mandate, the table below provides our long-term (strategic) and short-term (tactical) house view on investment strategy.

Key

+	●	−	▲	—	▼
Overweight	Neutral	Underweight	Upgrade	No Change	Downgrade

Sub-Asset Class	Strategic 12-month		Tactical 3-month		Sub-Asset Class Additional Guidance
	View	Change	View	Change	
Hedge: Equity-linked	+	—	●	—	We favour directional equity over low net exposure strategies. In market rallies, capture ratios will be higher in directional strategies with short exposure dragging on performance. Market volatility may bring portfolio management skill opportunities to enhance performance and alpha streams in our managers' portfolios. This view can be exploited in the Directional Mandate and Alternative LO Model.
Hedge: Relative Value	●	—	−	—	True credit arbitrage is still a difficult strategy to play for hedge funds managers. However, funds active in the stressed or distressed space as well as in "deep value" sectors of the credit markets have an interesting window of opportunity especially for those having the capacity to select the appropriate names to be engaged with. Convertible arbitrage also remains an area of focus for many credit managers. With the strategy's relative value focus and ability to add value through event driven and credit situations, this current environment should present attractive opportunities to support returns in 2021. Anchored low interest rates coupled with relatively flat yield curves is not conducive for pure fixed income arbitrageurs. Finally, we do not expect Volatility arbitrage to be a major consistent performance contributor in 2021.
Hedge: Macro	+	—	+	—	We have a preference for select Macro and shorter-term focused Systematic Trading strategies as counterbalances to pro-cyclical strategies and expect them to provide portfolio diversification benefits during any pockets of market volatility in 2021. We also keep our preference for longer-term trend-following strategies, although note that in the short term, the diversification benefits are diminished by their current broadly risk-on positioning. Trend-following strategies may therefore come into their own as diversifiers later in the year if and when market trends reverse meaningfully.
Commodities / Mining Equity	●	—	+	—	We are still strategically neutral on commodities but tactically overweight. Gold price has stabilized above 1750 but we expect it could find further support if uncertainty over Covid-19 variants remain. We are overweight in industrial commodities which is our preferred play on improving cyclicality. We remain cautious on the energy complex and see recent spikes as overvaluation relative to fundamentals.
Property / REITS	●	—	●	—	We keep a neutral stance on property. We are underweight on commercial and retail real estate but positive on logistics and residential, supported by record low rates and limited supply during the virus induced downturn and the fact that "nesting" habits will likely continue to grow.
Insurance-linked Securities	●	—	●	—	Cat yield spreads and the asset class generally has been unloved for many years and we are becoming more interested in the asset class, given its diversification properties.
Other (Volatility)	●	—	●	—	Implied volatilities should trend towards normalised levels. At this point we are only interested in selling volatility whenever it spikes. Hedging strategies look interesting once the VIX is in the low 10s or preferably below.
Infrastructure	+	—	+	—	We moved to overweight in infrastructure a couple of months ago as both Europe and the US start to develop long term infrastructure policies. The EU Recovery Fund and the Biden infrastructure plans are positive for the asset class.

Currency and Cash Allocation Grids

Based on a balanced mandate, the table below provides our long-term (strategic) and short-term (tactical) house view on investment strategy.

Key

Overweight | Neutral | Underweight | Upgrade | No Change | Downgrade

Sub-Asset Class	Strategic 12-month		Tactical 3-month		Sub-Asset Class Additional Guidance
	View	Change	View	Change	
USD	Neutral	No Change	Underweight	No Change	The US dollar has been exhibiting strength even with long term bond yields lower, however the curve has flattened which has re-enforced the dollar strength. We are carefully reviewing our shorter term view on the dollar given the dovish ECB, risk abatement and more recently Delta developments.
EUR	Neutral	No Change	Neutral	Downgrade	We have downgraded the EUR to Neutral on a tactical basis. Following the recent policy review we believe the ECB will remain dovish for longer. Additionally, our previous overweight stance was based on the EUR reaching 1.25 and currently both fundamental and technical indicators point that we should not maintain the overweight.
GBP	Neutral	No Change	Overweight	No Change	The GBP has continued to rally following the settlement around Brexit and the UK was one of the fastest developed economies to roll-out vaccines. This inevitably leads to confidence that the UK economy will be out quickly from the pandemic. We hit close to our target of 1.45 back in Feb and has now trended higher- in May we upgraded to target 1.50 as a level.
AUD	Neutral	No Change	Overweight	No Change	Following the steep sell off last year, the AUD has made a robust recovery. After the consolidation the AUD trend continues to be more positive. We previously upgraded the AUD and commodity sensitive currencies, reflecting the improvement in commodity prices and technicals.
Asia	Neutral	No Change	Overweight	No Change	We are encouraged that the JPY has not strengthened much more that it has done, given that we have seen the VIX pretty high. The JPY's status as a fear currency has diminished. We expect fundamentals to re-assert and we look for a weakening of the JPY to our target range of 110. The RMB is one of our favourite currencies, given the improving Chinese economy, a high carry on local rates and more than likely the Chinese will be the first to tighten policy.
CHF	Neutral	No Change	Underweight	No Change	The CHF is benefiting from overall correlation to volatility of financial markets, however with stimulus policy announcements and with any potential abatement of volatility we could see the CHF weaken further. We are now cautiously underweight.

Sub-Asset Class	Strategic 12-month		Tactical 3-month		Sub-Asset Class Additional Guidance
	View	Change	View	Change	
Money market	Underweight	No Change	Underweight	No Change	We have minimal cash levels for now.
Cash	Underweight	No Change	Underweight	No Change	We have minimal cash levels for now.

Important Information

The value of investments and the income derived from them can fall as well as rise, and past performance is no indicator of future performance. Investment products may be subject to investment risks involving, but not limited to, possible loss of all or part of the principal invested.