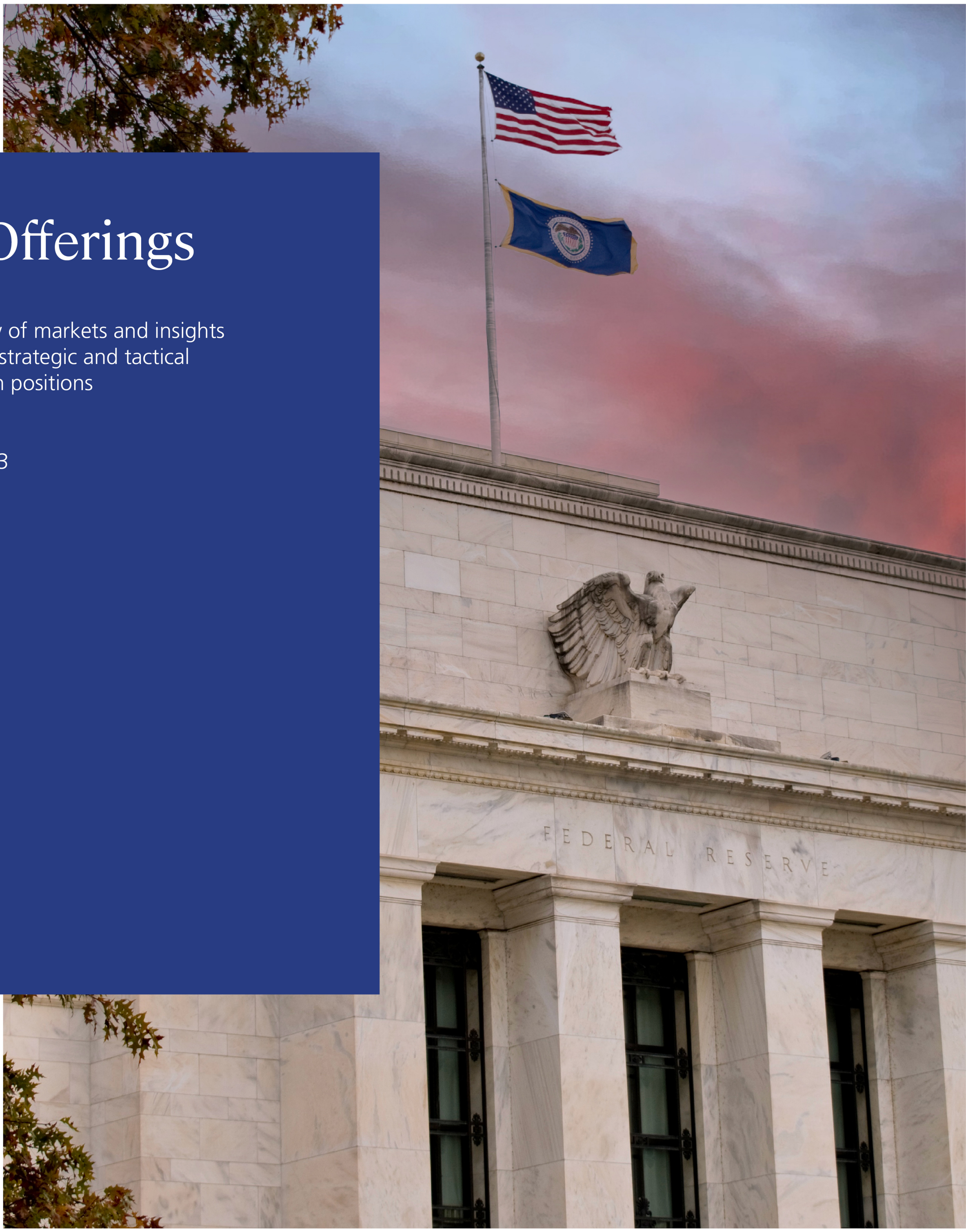
Central bank outlook

Skip, hike or pause as cuts delayed to 2024?



Core Offerings

Our latest view of markets and insights into our latest strategic and tactical asset allocation positions

June / July 2023

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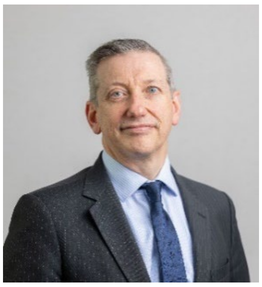
Skip, hike or pause as cuts delayed to 2024?

AN UPDATE FROM LGT CRESTONE'S CHIEF INVESTMENT OFFICER



Scott Haslem
Chief Investment Officer

The contours of the global outlook have been changing as the European and UK economies avoid recessions for now, and debate about a more delayed downturn in the US intensifies. Growth is proving more resilient than many expected. And while the data support further slowing in H2, that will likely still render 2023 at the milder end of global recessions.

Yet, the corollary of more resilient growth and still tight jobs markets is that inflation, while falling, remains stickier for services prices. While we believe central banks are at or near their peak for policy rates, there's insufficient evidence for them to commit to a pause. Any 'skip' in tightening during June and July could give way to further hikes should inflation not move lower over the next few months. At the very least, hopes for a typically quick easing of policy in the months ahead now almost certainly appear likely to be disappointed.

In this month's *Core Offerings*, we highlight the outlook for central bank policy, as markets now delay hoped-for rate cuts until early 2024. Persistently higher rates will continue to support fixed income returns (where we have tactically added to investment grade credit), while limiting the extent that equities can break higher. Staying underweight equities as rates and inflation peak is not without angst. Yet, adopting a more 'risk-on' stance is difficult until inflation falls more clearly and a base in the US growth cycle is within view.

The contours of the global outlook have been changing as the European and UK economies avoid recessions for now, and debate about a more delayed downturn in the US intensifies.

Economies and consumers proving resilient, but credit may yet wield some pain

The contours of the global growth slowdown have shifted as we have moved through H1 2023. The near-consensus recession forecasts for the **UK and Europe** have now given way to flat growth profiles that have softened the global slowdown to date (though clearly risks remain). Easing supply chain shortages and falling energy costs have underpinned stronger industrial activity, including better trends for exports and business capex.

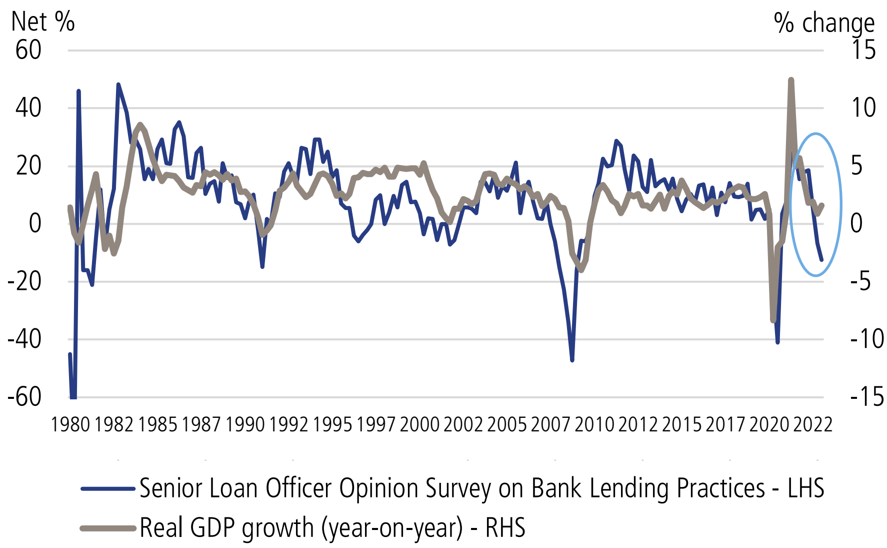
For the **US**, the anticipated H1 weakness in growth looks more distant, now expected to be revealed more convincingly in H2 2023. A tight jobs market has kept consumer spending resilient, led by strong demand. With manufacturing activity (in the US and globally) now showing some softening, the lagged impact of credit tightening (see the chart below) will be key. This is a feature that is also likely to weigh in the UK, Europe, and Australia.

For **Australia**, the mid-year mortgage reset, record low consumer sentiment, and tentative signs of a softening jobs market suggest, like the US, growth should be more clearly on a slower trend through H2 2023. Interestingly, this could see both countries on a much weaker profile than other key economies in H2 2023, some of which (e.g., China and Asia) may be entering modest recoveries. Still, few forecasters see Australia entering a recession, given the uplift in migration, a tight jobs market, and China's pick-up.

Yet, the corollary of more resilient economic growth and still tight jobs markets is that inflation, while falling, remains 'sticky' at a core level.

These shifting contours – together with the 'as yet' quite uncertain magnitude of the credit and liquidity tightening in H2 – suggest there's further slowing ahead in global growth. The data to date still support our long-held view that, while the journey is not yet over, this will be on the milder end of global growth downturns. Yet, this view is not unanimous.

Tightening US lending standards point to a significant slowing in US growth



Source: US Federal Reserve, BLS, UBS.

While UBS has recently lifted its global growth forecasts for 2023 from 2.0% to 2.6% ahead of a pick-up to 2.8% in 2024, Société Générale (SG) sees the US entering a recession in 2024 that drags global growth lower than in 2023. Such a result would be a significant headwind to equity earnings and corporate margins over the coming year.

The IMF suggests inflation is unlikely to return to target until 2025. Of course, proximity to target may be clearer by early 2024, giving central banks scope to contemplate cutting from then.

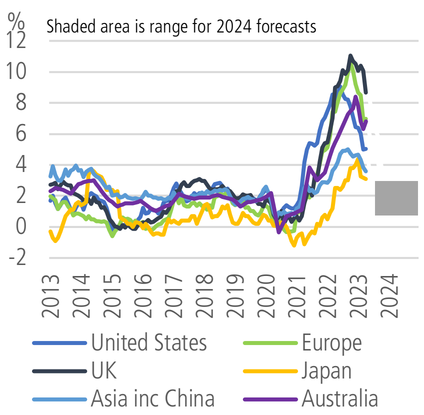
Inflation passed its peak…but services prices keep core inflation elevated

Over recent months, inflation has continued to fall at a fairly healthy clip (see left-hand chart below). In the US, it has dropped from 9.1% last year to 4.9% in April, while in Europe, it has fallen from 10.6% to 7.0%, and in Australia, from 8.4% to 6.3%. However, much of these falls reflect the impact of retracement in rapidly rising food and energy prices in 2022, significantly due to the outbreak of the Russia-Ukraine war.

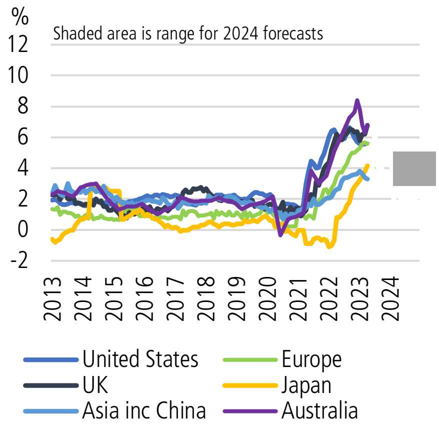
But the corollary of more resilient economic growth and still tight jobs markets (as noted above) is that inflation, while falling, remains 'sticky' at a core level. It is also well above central bank targets and above the level where they likely feel comfortable to start an easing cycle. Core inflation in the US fell to 5.7% late last year but remains at 5.5% four months later. As shown below, core inflation is not falling sharply – largely due to persistent services prices inflation (reflecting resilient consumer demand) – and in the case of Europe, it is still rising.

In its April *World Economic Outlook*, The International Monetary Fund (IMF) suggests inflation is unlikely to return to target until 2025. Of course, proximity to target may be clearer by early 2024, giving central banks scope to contemplate cutting from then.

Headline inflation turns down…



…but core remains elevated



Source: UBS, ABS, LGT Crestone.

The errors of the 1970s are mostly to do with easing too soon, and these appear to be errors central banks are focused on avoiding.

Central banks skipping, pausing, but unlikely to be cutting in 2023

While falling headline inflation eases central banks' concern on inflation expectations and gives them hope they have done enough on lifting rates, the stickiness in core inflation is giving them little room to reverse that tightening, even as unemployment rates start to rise (which is usual). The errors of the 1970s are mostly to do with easing too soon, and these appear to be errors central banks are focused on avoiding. As BCA Research notes, "repeated attempts to conquer inflation during the 1970s and 1980s led to abrupt policy pivots. Given this experience, the Fed may attempt to avoid prematurely easing policy by staying on hold for longer this time around".

As discussed below, the market has moved to begin pricing in further rate hikes over coming months from central banks in the US, Europe, and the UK.

US Federal Reserve (Fed)–Policy is currently at 5.00-5.25% (see table below). Fed Chair Powell has backed a 'skip' in June, but comments from Fed officials suggest further hikes are still being debated. Futures markets, having at one stage priced 1.00% of cuts by end-2023, now have a partial *further hike* priced this year, with the first full cut delayed to mid-December, ahead of further cuts in early 2024. While CBA sees no Fed cuts this year, UBS is the outlier, with 1.0% of cuts still slated for this year from September.

Reserve Bank of Australia (RBA)–The RBA increased the policy rate to 3.85% in May. After 'skipping' in April, and likely again in June, RBA Governor Lowe warned against generous wage gains, stressing he had "no tolerance for high inflation lasting a long time". Markets, having at one stage priced 0.50% of cuts by end-2023, now have a partial *further hike* for this year, with no cuts in 2023 and only 0.50% of cuts priced by mid-2024. CBA expects 0.50% of cuts this year, but UBS sees another hike, delaying forecast cuts until 2024.

European Central Bank (ECB)–The ECB raised the key policy rate to 3.25% in May, but officials say they debated a 0.5% hike. According to SG, "they also say that they are not done yet with rate hikes, are not committing to cutting rates at any time, and can hike rates even if the Fed pauses." The key concern for the ECB remains sticky core inflation, which remains elevated and above 5%. The futures market is priced for two more hikes this year, while neither CBA nor UBS expect cuts until 2024.

Bank of England (BoE)–The BoE raised the policy rate to 4.5% in May, its twelfth consecutive hike. Despite little change to their forward guidance, UBS believes the BoE's tone "was, on balance, somewhat hawkish", given comments around the moderation in inflation being slower than expected. UBS expects one further 0.25% hike to 4.75%, while CBA has recently added two further hikes, taking the cash rate to 5.0% by August. However, market pricing is for a further 1.0% of hikes to 5.5% by end-2023.

Bank of Japan (BoJ)–The BoJ has retained an aggressively easy policy stance, with rates unchanged over the past year at -0.1%. Notwithstanding a surprise hawkish decision last December to widen the band on its 0% 10-year bond yield target from +/- 0.25% to +/- 0.50%, there has been no further change. According to UBS, the case to unwind the yield curve control "continues to build", given solid growth, rising inflation and rising wage growth. Markets do not anticipate an exit from negative rates until 2024.

Emerging markets–Central banks in Asia, in contrast to elsewhere, are seen to be in a better position to cut policy in H2 2023, given inflation has begun to surprise significantly weaker. This has been led by falling food and energy prices, with potentially 'sticky' services prices a smaller weight in the inflation metrics. However, the extent of any easing will be impacted by currencies and may be more limited if the Fed remains on hold.

Central bank policy outlook – rate cuts concentrated in 2024, not 2023

	End-2021	End-2022	Current	Market	End-2023 UBS	End-2023 CBA	End-2024 UBS	End-2024 CBA
Australia	0.10	3.10	3.85	4.00	4.10	3.85	3.10	na
US (mid-point)	0.13	4.13	5.13	4.90	4.13	5.13	1.13	2.50
Europe	-0.50	2.00	3.25	3.56	3.75	4.00	2.75	2.00
UK	0.25	3.50	4.50	5.40	4.75	4.50	2.75	2.50
Japan	-0.10	-0.10	-0.10	-0.01	-0.10	0.00	0.10	0.00
Korea	0.75	3.25	3.50	3.35	2.00	na	1.25	na
India	4.00	6.25	6.50	6.50	6.25	na	6.00	na

Source: Bloomberg, UBS, CBA, LGT Crestone.

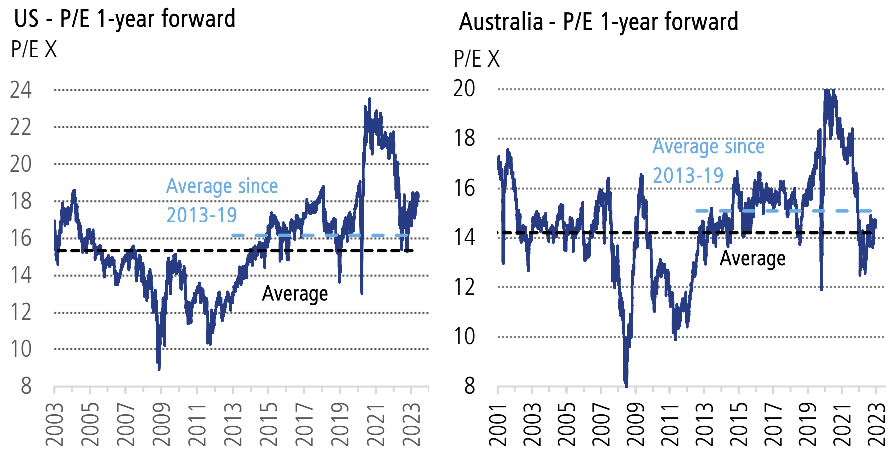
While being modestly underweight equities is not without angst, given peak inflation and peak policy, we continue to favour fixed income returns over equity returns for now.

Implications for tactical positioning

We remain constructive on the investment outlook. And while being modestly underweight equities is not without angst, given peak inflation and peak policy, we continue to favour fixed income returns over equity returns for now:

- Equities–Our modest underweight to equities is concentrated in the US (where valuations are challenging and the growth slowdown risks are deepest for H2) and Europe (where the ECB has more work to do than elsewhere to contain sticky inflation). We continue to look for an opportunity to adopt a more 'risk-on' view for equities, which is likely to reflect a balance of core inflation moving lower more quickly and a softer growth landing that reduces the hurdle for an earnings correction. We remain overweight domestic equities and emerging markets (mostly Asia).
- Fixed income–Global yields have reversed higher over the past couple of months, led by the US 10-year Treasury, which has increased from 3.30% in early April to 3.80% at end-May. While this has hurt our tactical positioning, we believe the continued moderation in inflation through H2 2023 and near-term pricing of central bank rate cuts for 2024 will underpin a broad-based rally in yields across the curve (and a re-steepening of the curve from the short end). Easing risks of over-tightening and deeper recession have led us to tactically add to investment grade credit.
- Aussie dollar–The direction of the Australian dollar in H2 2023 is likely to be largely conditioned by the relative hawkishness of the RBA and Fed, as well as the robustness of China's recovery. While UBS expects the currency to rally to USD 0.75 on the back of aggressive Fed cuts, CBA expects the currency to remain around USD 0.65 on further Fed tightening (before rising to USD 0.74 by end-2024). Given the currency is at the bottom of this range, a degree of hedging offshore risk assets is likely to provide a benefit over the coming year.

World price/earnings (P/E) ratios are at the upper end of 'fair' (US appears expensive)



Source: UBS, FactSet, LGT Crestone.

For now, equities seem to be pricing in a path of both lower inflation and resilient growth. Should this be maintained, it is possible that equity markets will remain rangebound through mid-year, as they have been since May 2021.

Navigating equities through mid-year

Although there has been a slight near-term recalibration in interest rates higher over the past month in Australia and the US, equity markets have generally proven resilient in the face of this. Additionally, as noted, 10-year bond yields have moved higher, by 40-50 basis points (bps). With inflation expectations falling, this has meant that real interest rates have actually pushed higher. Typically, as we saw in 2022, such a move in interest rates would have been a headwind for equity performance, especially the longer-duration segments of the market, such as Technology. However, more recently, equity markets have been able to absorb these headwinds, perhaps focusing on the more resilient near-term growth outlook.

The near-term challenge through mid-year is that, firstly, stronger growth may further inhibit a slowdown in core inflation. This would lead to a more extended period of elevated interest rates than the market is expecting. Secondly, while the path to a "softish" landing is perhaps somewhat more plausible than appeared previously, the impact of credit tightening globally has yet to be fully judged. The tightening in lending standards, already in motion before the collapse of several US regional banks, will limit credit availability and may impinge growth over H2 2023 into early 2024 (especially in the US).

However, we believe absolute upside remains challenged by 1) absolute equity market valuations that, in the main, remain expensive; 2) a more resilient growth outlook that also implies stickier inflation and more time may be needed to accept inflation; and 3) returns in competing assets, where the earnings yield from equities is not far removed from yields on government bonds or investment grade credit.

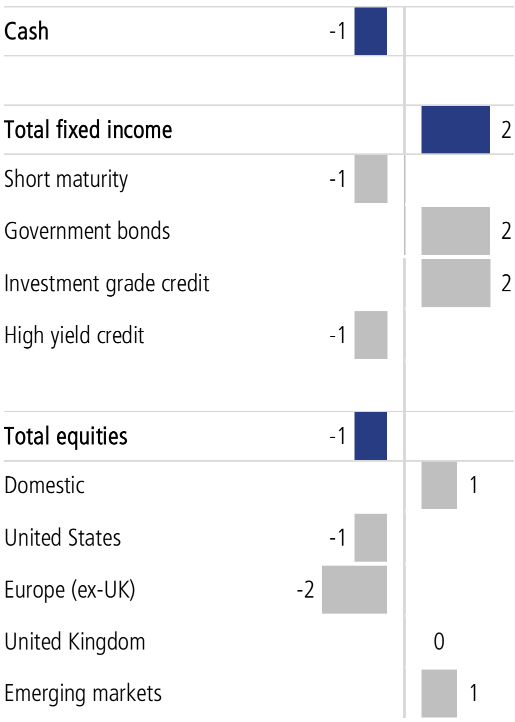
For now, equities seem to be pricing in a path of both lower inflation and resilient growth. Should this be maintained, it is possible that equity markets will remain rangebound through mid-year, as they have been since May 2021. However, we believe absolute upside remains challenged by 1) absolute equity market valuations that, in the main, remain expensive outside of the post-COVID 2020-2021 bubble period; 2) the fact that a more resilient growth outlook also implies stickier inflation and more time may be needed to accept that inflation can approach acceptable levels without further central bank tightening; and 3) returns in competing assets, where the earnings yield from equities is not far removed from yields on risk-free government bonds or investment grade credit.

Regionally, this leaves us with a value skew towards Australia and emerging markets. The 12-month forward P/E ratio for the S&P/ASX 200 index is just 14.3x, 1.2 standard deviations below its 10-year average. Against stellar year-to-date performance of US and European markets, the 'flattish' emerging market result is painfully weak. But there are several reasons why this year could be a year of emerging market outperformance. Firstly, emerging market earnings per share (EPS) growth is forecast to outperform developed market EPS over 2023 and 2024. Secondly, emerging market valuations are now 2 standard deviations cheaper than their average discount to the MSCI World index. Thirdly, emerging market economic growth is expected to exceed developed economy growth by over 3%, an extent to which in the past has led to emerging market equity outperformance.

The US equity market remains challenged by extremely rich valuations and a banking sector dealing with deposit flight and a significant tightening in lending standards. European equities are now back to average valuations, with the lagged impact of tighter monetary policy still to be felt. Importantly, the European Citi Surprise Index has now turned negative (data is coming in worse than expected) and there is a reasonable relationship between the relative performance of the US versus Europe, depending on the direction of the economic data. Despite peaking growth momentum, the ECB is likely to stay hawkish due to persistent inflation. This implies that the outlook from here is more challenging.

What's driving our views

Tactical asset allocations (% weights)



Source: LGT Crestone Wealth Management. Units refer to the percentage point deviation from strategic asset allocations. Investment grade credit includes Australian listed hybrid securities.

More banking jitters, lower inflation, and debt ceilings

Equity markets continued to grind higher in May, helped by solid earnings and margins, despite slowing growth and jobs markets in Australia and the US. After pausing in April, the RBA raised rates to 3.85% and the Fed hiked to 5.25%. Both central banks are likely now near the end of their respective rate-hiking cycles. Reflecting our cautious view of markets, we have increased our fixed income overweight. In the short term, we expect fixed income to outperform equities under various scenarios.

Inflation volatility is likely to persist—Inflation continues to fall, though services inflation remains sticky. However, fading impacts of globalisation, structurally tight labour markets, and geo-political impacts on supply chains suggest less deflation and more inflation.

A return to 'normal' interest rates—Peaking inflation is likely to foster a near-term peak in central bank hikes. But stickier inflation than over the past two decades is likely to limit a return to near-zero interest rates.

Geo-political volatility likely to be enduring—Russia's invasion of Ukraine has ended a long period of benign globalisation. Ongoing decoupling of leading-edge technology, political and trade alignment, as well as military and energy security, are all key potential drivers of growth and profits.

Diversification matters —In a world of heightened volatility and fewer long-cycle trends, it is important to maintain portfolio diversification, avoiding over-exposure to individual markets, sectors and other specific return drivers. Unlisted investments are likely to grow in favour.

Structural thematics

The energy transition—As the world faces a trade-off between net-zero commitments, cost, and energy security, this is setting the scene for both old and new forms of energy to play a role.

Sustainable investing—As the world becomes more connected, it is also becoming more socially aware. The intersection of finance and sustainability will govern a reallocation of capital.

The search for income—The exit of 'zero-bound interest rates' has resulted in a resetting of income expectations across all asset classes, including equities, fixed income, and income-generating unlisted assets.

Deglobalisation—Brexit, trade wars, COVID-19, and Russia's invasion of Ukraine have up-ended a relatively harmonious world order, with impacts spanning geo-politics, military spend, supply chains and demographics.

	What we like	What we don't like
Equities	▪ Energy companies now focused on shareholder returns with an 'OPEC put' in place ▪ Later-cycle defensive exposures in the consumer staples, telco and healthcare sectors ▪ Emerging markets due to China re-opening, improving earnings and better valuation metrics	▪ Companies with shorter-term debt maturities at risk of re-pricing into a higher rate environment ▪ S&P 500 companies, where valuations are now back above pre-COVID average valuations ▪ Continental Europe, where inflationary pressures suggest significant earnings headwinds
Fixed income	▪ Green bonds and ESG-oriented strategies ▪ Fixed rate three to five-year senior unsecured banks ▪ Fixed-rate Australian bank subordinated tier II	▪ Short maturity bonds with a preference for more duration in portfolios
Alternatives	▪ Multi-strategy, credit-oriented and discretionary macro hedge funds ▪ Domestic private debt and asset-backed securities (excluding real estate) ▪ Core/core-plus infrastructure assets with inflation linkages ▪ Private market and real assets exposed to the global energy transition	▪ Passive private market and/or real asset strategies ▪ Lower grade / buy-and-hold real estate assets ▪ Pre-IPO strategies ▪ Construction and/or junior real estate lending ▪ Carbon-intensive assets with no transition plan

Economic and asset class outlook

Economic outlook

Global economy

The contours of the global outlook have been changing over recent months. The European and UK economies appear to have avoided recessions for now and debate has intensified over whether a delayed downturn in the US will eventuate. Still, while growth is proving more resilient than many had expected, leading indicators—from credit tightening to consumer spending patterns—strongly suggest there will be a further slowing in activity in H2. The relatively mild global recession we have been anticipating is likely to give way to a modest 'rocky recovery' in 2024, according to the IMF.

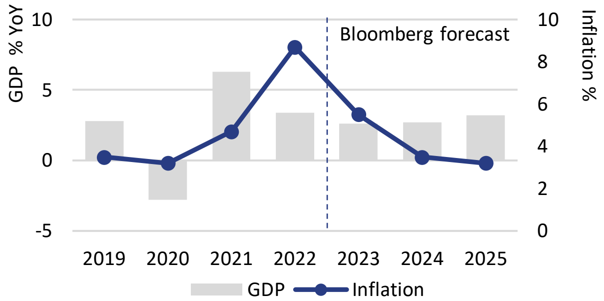
For Q1, growth in the world economy bounced strongly, up by around 0.9% (after just 0.2% in Q4 last year), lifting the annual pace of growth from 1.9% to 2.3%. China's growth surprised positively amid a stabilising property sector and further stimulus. Growth in the UK, Europe and the US was tepid but positive (albeit the US consumer remained resilient), and slower than Japan in Q1.

Yet, the corollary of more resilient growth in the near term and still tight jobs markets in many regions (including the US, Europe, the UK, and Australia) is that inflation is falling slowly, largely due to sticky services prices. While central banks are near their peak for policy rates, hopes for a typically quick easing over coming months will almost certainly be disappointed. Cuts are unlikely to take place until H1 2024.

Near-term growth resilience, slower disinflation, and the risk of further financial pressures are likely to see interest rates held high for longer to ensure inflation risks are removed over time. There are already signs that Q2 global growth will be slower, led by China and the US consumer. The US debt ceiling debate has also likely lifted interest rates, added to volatility, and dented sentiment, albeit temporarily.

Forecasts for the 2023 outlook have recently been lifted. UBS raised its forecast to 2.6% (from around 2%) and, similar to the IMF, expects a pick-up in growth to 2.8% in 2024. SG has added around 0.5% to its latest 2023 outlook for the US, Europe, UK, and China under the banner of "recession must wait", but expects a global recession in 2024, led by a recession in the US from early 2024.

Global GDP growth and inflation



Source: Bloomberg as at May 2023.

Australia

Recent data suggest the economy slowed noticeably in late 2022, with data pointing to relatively flat activity for Q1 2023. With consumer spending now slowing, ahead of rising housing interest costs in Q2, growth is expected to shift below trend into mid-2023. Still, China's moderate growth pick-up (even if less commodity intensive), the recent budget stimulus, and strong rebound in immigration have added to confidence that Australia can avoid recession and moderately outperform growth in other developed economies in 2023.

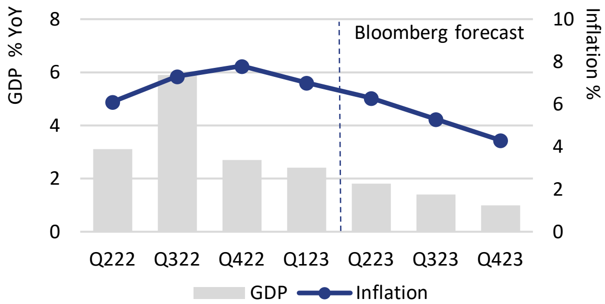
Growth in Q4 eased to 0.5% from 0.7%, its slowest in a year, with the annual pace braking from Q3's 5.9% to 2.7%, a near-trend rate of growth. Q1 data, due imminently, are consistent with further slowing, led by the consumer. In April, retail sales were flat (after 04%), with the annual pace slowing for the seventh consecutive month to 5.4%. While there are some signs of stabilisation in housing prices, new building approvals have corrected lower. April jobs data revealed the first clear evidence of a weakening, with unemployment rising from 3.5% to 3.7%. Consumer sentiment fell 10% in May.

The 2022-23 Federal budget delivered a $4.2 billion surplus (0.2% of output), the first since 2007-08, on the back of lower unemployment and higher commodity prices. Still, with modest new stimulus (about 0.5% of output) and spending pressures, the budget quickly returns to deficits of around 1% in the out-years, an improvement from last year's deficit trend near 2%.

Inflation slowed to 1.4% in Q1 (from Q4's 1.9% pace), seeing annual inflation moderate from a likely peak of 7.8% to a still high 7.0%. However, April monthly inflation lifted from 6.3% to 6.8%, suggesting the pace of inflation moderation may be slower than expected. After remaining on hold in April, the RBA tightened by 0.25% in May to 3.85%, with a rebound in house prices and strong jobs data likely catalysts. The RBA retained a tightening bias. UBS expects a further final hike to 4.10% in July, while CBA sees 3.85% as the peak of the cycle.

After 3.7% growth in 2022, UBS expects Australia to avoid a recession in 2023, with growth slowing to 1.3%, while CBA has lifted its forecast from 1.1% to 1.5%. UBS expects growth to recover modestly to a 1.6% pace in 2024.

Australian GDP growth and inflation



Source: Bloomberg as at May 2023.

Economic outlook

United States

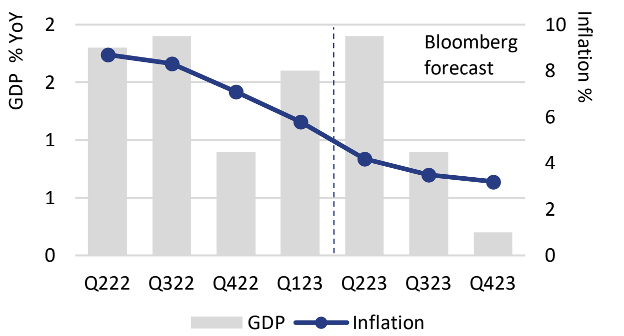
Recent strains in the US regional banking system remain contained, though May saw another ‘takeover’, this time by JPMorgan of The First Republic Bank (easing concerns of a collapse). Greater focus remains on the likely impact of the inevitable tightening of financial conditions, above that already delivered via higher rates. House Republicans and White House negotiators appeared to reach an agreement in late May to raise the nation’s debt ceiling until after the next Presidential election. While leading indicators signal an imminent, though likely mild, recession ahead, recent data continue to validate support by some for a softer landing.

Growth missed expectations in Q1, rising just 0.3% (1.3% annualised) after Q4’s 0.6% (2.6%), albeit consumer spending proved robust (at 3.8% annualised). While the composite purchasing managers index (PMI) rose further to 54.5 in May, its fastest since April 2022, the key manufacturing ISM is lower at 47.1, near its weakest since 2020. Retail sales rose modestly in April, by 0.4% after two 0.7% monthly declines. While the jobs market remains tight (with unemployment falling to 3.4% in April), jobless claims are now trending higher. As SG notes, April’s Senior Loan Officers Survey revealed that additional credit tightening by banks in Q1 was not as bad as many had feared. “Yet tightening there was, and this recessionary signal is compounded by a massive negative US credit impulse”.

Price pressures continues to ease gradually, with inflation at 4.9% in April (well below its mid-2022 peak of 9.1%). There were further signs of easing in the key rent component, raising hopes for a renewed downward trend in core inflation. The Fed lifted rates 0.25% in May to 5.25%, as expected. Less hawkish comments suggest the Fed is ready to pause, but not yet willing to commit to that pause, while also keeping the door open for further hikes should they be deemed needed. UBS and CBA believe the Fed has now finished its tightening.

After 2.1% in 2022, UBS expects growth to slow sharply to 0.8% in 2023 (and to 0.4% in 2024). SG forecasts stronger growth in 2023 of 1.7% before a clearer slowing into recession in 2024, with growth of just 0.1%.

US GDP growth and inflation



Source: Bloomberg as at May 2023.

Europe

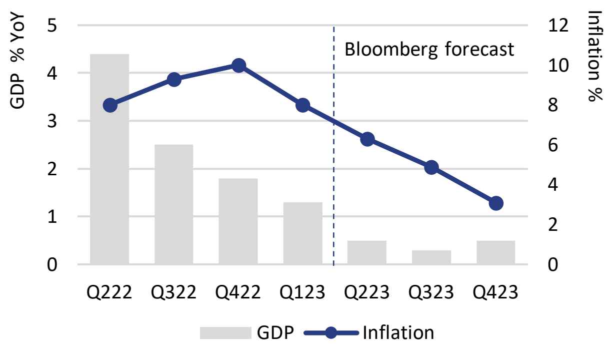
Europe’s warmer-than-expected winter has lifted the likelihood the region can avoid recession in 2023. However, growth is likely to remain soft until early 2024, and some countries, like Germany, are already in recession. Stronger momentum in industrial activity is expected to be challenged by tighter credit conditions due to recent rate hikes and banking system stability issues. With core inflation elevated, rates will likely be hiked into mid-year, adding to the credit tightening increasingly evident in the lending surveys. Recently announced budget plans, according to SG, point to “euro area governments planning to tighten fiscal policy by close to 1% of GDP – mostly thanks to spending cuts”, a significant tightening of fiscal policy in 2024 that will weigh on any recovery.

Europe’s Q1 growth was positive, though a little weaker than expected, rising by just 0.1%, and slowing the annual pace further from 1.8% to 1.3%. Data for Q2 is mixed. May’s PMI data eased to a three-month low of 53.3 (from 54.1). Industrial activity slumped 4.1% in April, more than retracing prior months’ gains. Retail sales remain volatile, falling 1.2% in March and trending 4% below year-ago levels. In contrast, the jobs market remains surprisingly tight, with unemployment easing to 6.5% in March, below the 6.7% rate during 2022.

After a sharp fall in March from 8.5% to 6.9%, inflation edged higher to 7.0% in April, while core inflation edged only slightly lower to 5.6% (its first decline this cycle). The ECB, while slowing the pace of hikes, raised the policy rate again in May to 3.25%, reiterating its ‘data-dependent’ outlook. The ECB’s Chief Economist, Philip Lane, noted there “is still a lot of momentum in inflation, but later this year, a lot of this inflation is supposed to reverse”. This is a view shared by Longview Economics, which expects “a rapid fall in Eurozone inflation this year”. CBA expects one further hike, UBS two, and SG three, with rates at 4.0% by September.

After growth of 3.5% in 2022, UBS expects a sharp slowing to 0.8% in 2023 (with a softer Q1 result dissipating upside risks). SG expects higher growth of 1.2% in 2023, while CBA lifted its growth outlook from -0.5% to +0.5% (and 1.0% in 2024).

European GDP growth and inflation



Source: Bloomberg as at May 2023.

Economic outlook

United Kingdom

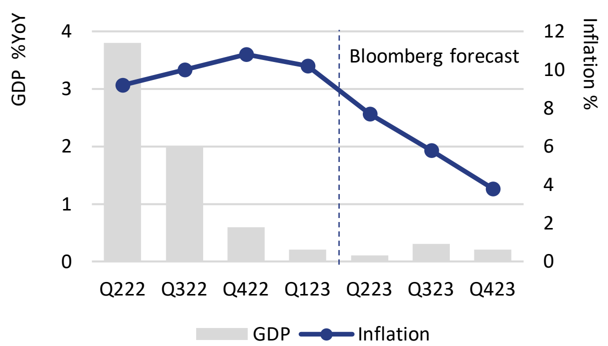
Growth in the UK economy remains weak, albeit recent data suggest a recession is being narrowly avoided. Recent quarters have seen the economy eek out marginally positive growth, as consumers and businesses prove more resilient than expected to high energy prices and elevated inflation. Nonetheless, the growth outlook remains challenged by expiring government energy support and tightening financial conditions, while rising mortgage payments will increasingly weigh on consumer spending. Together, these headwinds are expected to render growth similarly tepid, near flat, over coming quarters, ahead of modestly stronger growth through 2024.

Output grew by just 0.1% in Q1, the same pace as in the prior quarter, slowing annual growth to just 0.2% (from 0.6%). Consumption edged up by 0.1%, while public and private capex rose a solid 1.3%, as industrial output and construction activity strengthened. However, weak exports and government spending left growth virtually flat. Early Q2 data have been mixed, but resilient. The UK's PMI stayed high in May, easing to 53.9 from 54.9. The labour market remains tight, with earnings growing at an annualised rate of 7.6%, albeit the unemployment rate rose to 3.9% in March (from 3.7% in January), and payroll numbers have started to decline.

While lower energy prices saw a significant fall in inflation to 8.7% in April (from 10.1%), this was less than expected, with core inflation accelerating to 6.8% from 6.2%. In May, the BoE raised the policy rate by 0.25% to 4.5%. But despite little change to its forward guidance, UBS believes the BoE's tone "was on balance somewhat hawkish", given comments around better-than-expected growth, a still tight jobs market, and a moderation in inflation that was likely to be slower than expected. UBS expects a further hike, to 4.75% in June, with rate cuts delayed until early 2024, while CBA has added two additional hikes, taking the rate to a peak of 5.0% by August.

After growth of 4.0% in 2022, UBS has revised up its forecast for 2023 from -0.6% to +0.2%, while CBA now expects flat growth in 2023. For 2024, growth is expected to strengthen modestly, with CBA forecasting 0.4% and UBS 0.6%.

UK GDP growth and inflation



Source: Bloomberg as at May 2023.

Japan

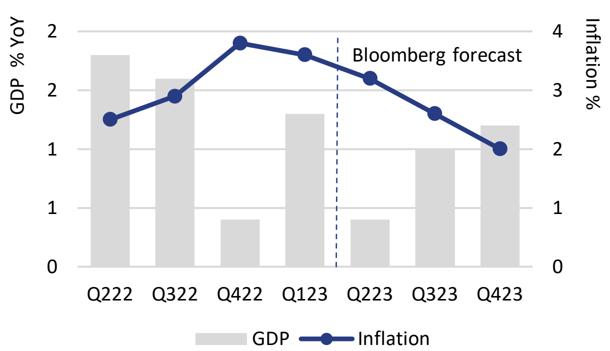
Japan appears on track to deliver steady, if not somewhat modest, growth over the next couple of years. A key focus is on the expected impact of slowing global growth on exports, and the extent to which it is more than offset by stronger activity domestically, as the economy continues to open post-pandemic. As UBS notes, a "key feature of the economy is the divergence between weakening in goods (mainly overseas) and recovery in services (mainly at home)". A key focus will be on the impact of strengthening domestic growth and wages and the pressure this may apply to encourage policy makers to step away from the current zero interest rate setting.

Growth rose by a stronger-than-expected 0.4% in Q1 (1.6% annualised), leading to an acceleration in annual growth from 0.4%to 1.3%. Stronger consumer spending (led by services), along with business and government capex, led the rebound. Exports fell more than expected (led by weaker goods demand out of China). Early Q2 data point to ongoing growth. Japan's PMI jumped to 54.9 in May (from 52.9), while retail sales rose 0.6% in March. Japan's Tankan sentiment index for manufacturers jumped to 6 in May 2023 from -3 in April, turning positive for the first time this year. In contrast, unemployment continued its recent rise, lifting to 2.8% in March, its highest since early 2022.

Inflation retraced higher to 3.5% in April from 3.2% in March (but below January's 4.3% peak), while core inflation is 3.4%. According to UBS, the case to unwind the yield curve control (YCC) "continues to build with a continued flow of strong growth prints. Price prints are still surprising to the upside and strong Shunto wage settlements should start to materialize in the April wage data. This should make its June meeting live." The BoJ left policy unchanged in May, with consensus for near-term policy tightening (widening the YCC bands from +/-0.5% to +/-1.0%) drifting out to the July meeting, given dovish comments by BoJ Governor Ueda.

After growth of 1.0% in 2022, UBS expects a similar annual pace to unfold for 2023-2025. SG forecasts 1.3% in 2023, but slowing again to 0.9% in 2024.

Japanese GDP growth and inflation



Source: Bloomberg as at May 2023.

Economic outlook

China

China's economy recovered significantly through Q1, as it jettisoned its COVID-zero policies and continued its moderate policy stimulus. More recently, some questions have emerged over the durability of China's pick-up, with some key activity data revealing a loss of momentum during April. The less commodity-intensive nature of China's pick-up has recently been garnering more attention, and as SG notes, "the service-led nature of the recovery is also why China's spillover effects on global demand and inflation have been less visible this time". Notwithstanding April's moderation, growth is expected to continue picking up through the year.

China's output rose by more than expected in Q1, up by 4.5%, its fastest pace of growth in a year. However, most April data have weakened sequentially. As UBS highlights, "while retail sales growth jumped to 18.4%y/y, we estimate real retail sales slowed to 0.3%m/m. Property sales improved to 5.5%y/y, but its absolute level declined by 20%m/m from March. Both infrastructure and manufacturing capex growth moderated, while export growth (8.5%y/y) slowed".

April credit growth stayed strong at 10%, though this partly reflects a low base a year ago. UBS expects recent Politburo messaging around a "prudent" (and supportive) monetary policy stance with "accurate and effective" measures may limit the upside of credit growth for the rest of 2023. However, MST Marquee believes "infrastructure spending [is] benefiting the most and [it] expect[s] the stimulus will continue and broaden out to other parts of the economy". Inflation was weaker again in April, collapsing to just 0.1% from 0.7% in March. Falling food and non-food prices contributed. Core inflation was low and unchanged at 0.7%. UBS "expects price increases to gather momentum in 2H23".

China's growth dropped from 8.4% to 3.0% in 2022. But in contrast to most other economies, growth is expected to strengthen in 2023 and 2024. UBS recently upgraded its 2023 growth outlook from 5.4% to 5.7%, before a 5.2% pace is seen for 2024. SG has raised its 2023 forecast from 4.8% to 5.8%, with 2024 also expected to slow modestly to 4.8%.

Emerging markets

After a H2 2022 rebound in activity led by Asia, the emerging market region is expected to recover moderately during 2023. Trade-orientated economies are expected to slow into mid-year before Asian growth stabilises and emerging Europe rebounds in the second half of the year. China's accelerated re-opening provides further support, with SG viewing this as a "game changer" for Asia. Inflation is now moderating more clearly, and most central banks have paused tightening, and some easing of interest rates is expected during H2 2023.

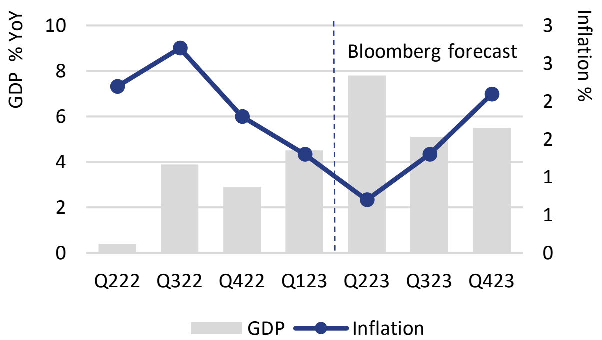
Inflation has begun to surprise significantly weaker across Southeast Asia, led by falling food and energy prices. This has been particularly the case for Indonesia (5.0% to 4.3%) the Philippines (7.6% to 6.6%), and Vietnam (3.4% to 2.8%). India's inflation fell below 6% in March, and then to 4.7% in April. UBS expects Korea, India, Malaysia, Indonesia, and Singapore central banks to remain on hold, with potential rate cuts coming from India, Indonesia, and the Philippines, particularly if the Fed signals lower rates later in the year.

Growth in India rose 0.7% in Q4, with the annual pace slowing from 6.3% to 4.4%. Tight monetary policy is weighing on purchasing power as pandemic savings are depleted. According to SG, "India's economic rebound led by pent-up demand appears to have run its course and the economy is likely to grow by 6.0% in 2023, the lowest in three years. Yet, that will still make India the fastest-growing G-20 economy". UBS sees 2023 growth slowing to 5.5% from 7.0%.

UBS expects growth in Latin America to slow from 3.7% in 2022 to 1.5% in 2023 on the back of weak external demand for exports. In Brazil, falling inflation is cementing peak central bank rates, with policy held steady in May for the first time since the cycle began in early 2021. For emerging Europe, weak consumer spending is a key driver of weaker growth.

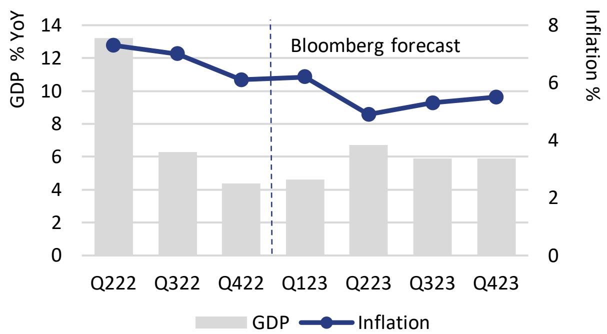
After 4.0% in 2022, UBS expects a marginally stronger pace of 4.1% for 2023, accelerating to 4.3% in 2024. Growth in emerging Europe is expected to collapse to 0.9% in 2023 after 3.2% in 2022, before a rebound to 2.4% in 2024.

Chinese GDP growth and inflation



Source: Bloomberg as at May 2023.

India GDP growth and inflation



Source: Bloomberg as at May 2023.

Asset class outlook

Short maturity and government bonds

Position: Underweight short maturity, overweight government bonds

Key points

- Central banks are likely to pause hiking rates as the crisis in the financial sector weighs on lending and activity.
- Global bond yields increased as debt ceiling concerns led to increased volatility in bond markets.
- We expect rate volatility to remain elevated in Q2 2023, reflecting the risk of inflation data and a slowdown in economic growth.

Short maturity—Debt ceiling concerns continue to hang over US markets, causing increased volatility in bond markets. This whipsaw shift in sentiment will likely continue, but as time passes and the risk of further contagion in US regional banks subsides, central banks will maintain their focus on inflation and whether the recent turmoil is likely to slow growth considerably. While the Fed increased rates by 25bps at its May meeting, it is likely the terminal peak in rates is near. The RBA also raised rates unexpectedly to 3.85%, but we believe it will now hold at this level for longer and be guided by future inflation and growth data. The economic outlook is uncertain, but our base case is inflation is slowing and the RBA will remain on hold before potentially cutting in late 2023 or early 2024.

We are underweight short maturity debt, which helps protect against rising interest rates. While the market will likely remain volatile at the front end of the curve, it is our six to 12-month view that global overnight fund rates will fall. We, therefore, recommend adding duration. The recent market turmoil is likely to tighten lending liquidity and slow economic growth, and as inflation is already showing signs of falling, we expect central banks will ease later in Q4 2023.

Government bonds—We continue to maintain an overweight position in high grade and investment grade bonds. Our base case is that the recent moderation in inflation will continue, growth will decelerate, and bond yields will fall below the current trading range on the 10-year Treasury, which is 3.75-3.35%). While central banks are close to the end of their tightening cycle, labour markets remain tight, wage growth robust, and core services inflation is high. There is an element of doubt in the market regarding the assumption that central banks are reaching the end of their rate-hiking cycles, and this is creating some volatility in markets. We can expect periodic spikes in bond yields as it remains too early to declare victory on the inflation fight. We see these spikes as an opportunity to add duration. The recent financial instability in the banking sector and post the debt ceiling crisis should put further downward pressure on nominal growth and interest rates.

The risk-return profile for defensive, higher-quality segments of the fixed income market remains appealing, given the all-in yields on offer and the expected transition from inflation risks to growth risks. Within this context, we prefer high grade and investment grade bonds.

Investment grade and high yield credit

Position: Overweight investment grade and underweight high yield credit

Key points

- Domestic subordinated Tier II debt is our most preferred segment within investment grade credit.
- Investment grade credit spreads have been stable as higher outright yields attract demand.
- We prefer investment grade credit over high yield, as the latter is vulnerable to an increase in default risk.

Investment grade credit— Investment grade credit spreads have been remarkably stable, given recent financial conditions in the banking sector. Investment returns were flat in May, given the move in outright interest rates. We believe corporate credit spreads are sitting at fair value, and fundamentals for US and Australian corporates are robust. The sensitivity of lower rated asset classes to an economic slowdown is likely to increase default risk. As such, we recommend staying in the high-quality investment and high-grade sectors. In the US and Europe, there has been a stream of new issuance, which has kept investor confidence high. In May, markets saw $61 billion of new issuance in one week. Pharmaceutical giant Pfizer issued $31 billion in eight tranches—this was the largest trade of the year and fourth largest of all time. With demand peaking at over $85 billion, Pfizer was able to tighten pricing by 20bps and land with roughly 20bps of concessions.

In Australia, spreads on additional tier 1 hybrids have widened, but not to the extent they did in Europe following the collapse and subsequent sale of Credit Suisse. Australian hybrids have widened from around BBSW +275bps to BBSW +300bps. An attractive running yield of 6.90% allowed CBA to issue $1.55 billion of new money through the CommBank PERLS XV Capital Notes at a spread of BBSW +300bps. The issue was met with strong demand and 1.65x over-subscribed. Retail investors continue to retain their long position as the asset class is still regarded as a safe haven. Earlier in the month, ANZ raised $1.15 billion via a 10 non-call 5 tier 2 subordinated note transaction at BBSW +235bps. On a risk-adjusted basis, we prefer subordinated tier II over additional tier 1 hybrids.

High yield credit—High yield spreads have stabilised as outright yields have settled around 8.5%. However, we remain cautious about the high yield market and expect further widening of spreads in coming months. This is consistent with less supportive liquidity conditions, an increase in defaults to a more normalised level, and high yield spreads coming under further pressure from a likely further tightening of financial conditions.

Yields for US and European high yield debt of around 8.50% provide a level of protection against falling prices. With a large part of the investment universe now trading at a discount to par, there are select opportunities available for investors. Our preference is to be higher up the credit quality curve in investment grade credit.

Asset class outlook

Domestic equities

Position: Overweight

Key points

- Domestic equities fell 3.0% in May, underperforming global equities in Australian dollar terms.
- The IT sector had a very strong month, rising 11.6% as sector heavyweights Xero (+17.8%), WiseTech (+9.2%), and Technology One (+8.5%) rose strongly.
- The cyclical parts of the market were noticeable laggards, with materials, consumer discretionary and financials all underperforming the broader market.

The RBA surprised with a 25bps hike to 3.85% in May and RBA Governor Lowe's subsequent speech suggests the bank has renewed concern about the stickiness of services inflation (and the upcoming minimum wage decision). So far in 2023, investors have been prepared to play a peak inflation narrative through growth versus value bias, which was turbo-charged by the collapse of Silicon Valley Bank.

The change in rhetoric and re-pricing of possible outcomes to a slightly higher (and maybe longer) peak have significant ramifications for sector rotation in Australia. The banks are already seeing performance wane (albeit book value share prices for Westpac and ANZ are cushioning the blow). The outlook for housing and housing-related stocks has become cloudier. Many investors had been positioning for a pause in rate hikes, and house prices had seemingly bottomed, with record migration expected to support the sector. It has also become more challenging to form a view on domestic rate-sensitive cyclicals and real estate investment trusts. The flip side is that defensive stocks and insurance stocks are set to benefit in this environment.

May saw a range of companies provide trading updates and/or deliver quarterly results. Consensus estimates have been generally underwhelmed by the news, with downgrades to forward earnings estimates outnumbering upgrades by a ratio of 3:2. The magnitude of this disappointment has, however, only been small in aggregate, taking (on average) just 0.1% off earnings for both financial years 2023 and 2024. Although bank results have set new profit records, all the major banks have suggested that the peak in net interest margins was last year and that competition (both for deposits and mortgage market share), as well as future credit quality (currently benign), would likely inhibit performance.

Valuation remains supportive in Australia. The 12-month forward P/E ratio for the S&P/ASX 200 index is currently just 14.3x. This is one standard deviation from its 10-year average and is cheap versus the MSCI World, where it is trading at a 12% discount. The largest discount over the past decade has been 18%. Nonetheless, the current reading is 1.2 standard deviations from the 10-year average. Australia's dividend yield of 4.3% also offers some support versus the rest of the world, although it is still below its 10-year average of 4.5%.

International equities

Position: Underweight Europe and the US, neutral UK and overweight emerging markets

Key points

- In May, global equity markets rose 1.3% in Australian dollar terms. The NASDAQ was a notable outperformer, while the UK and Europe traded around 4% lower.
- The strongest performing sector was IT, led by strong gains in semi-conductor chip designer, NVIDIA.
- Interestingly, IT and telco stocks traded higher over the month, while all other sectors were at least 1% lower, with cyclicals particularly hard hit.

There are several crosscurrents currently impacting global equities. Although the MSCI World index was unchanged in May, market leadership was very narrow. The technology and telecoms sectors have risen 32% and 26% respectively year-to-date, accounting for most of the market's performance. This is partly because we are at, or close to, the peak in the interest rate hiking cycle. However, at the beginning of May, the market was priced for a peak in the Fed funds rate of 5%. At the time of writing, that peak had been revised to 5.3% (not far from the cycle peak of 5.6% in February). Furthermore, US 10-year bond yields rose 50bps to late May and real interest rates at 1.56% are not far removed from the cycle high of 1.75%.

So, why has the market been able to sustain such strong performance in the face of rates pressure? It largely comes down to the technology sector, where the seven largest companies have been responsible for more than 110% of the total return of the S&P 500 index year-to-date. For the technology sector, earnings have surprised positively, with estimates moving 3-4% higher. However, this relatively small earnings revision does not explain the strong share price performance. The surprising component of the move, especially viewed in the context of interest rates, has been the valuation re-rate. The 12-month forward P/E for the MSCI World Technology index has risen from 22.5x prior to the collapse of Silicon Valley Bank to 25x as at the time of writing. Although this is a long way from the 30x it sustained over 2020-2021, it is still 7% higher than the pre-COVID peak and almost 60% higher than the pre-COVID average. It is possible that the market is "hiding" in companies where relative revenue (recurring, software) and earnings (cost-out) trends are more insulated, and balance sheets for mega-cap stocks are largely net cash.

The European equity market has recovered from its March downturn and is now trading at levels similar to one year ago. Beneath the surface, however, this recovery has been driven more by defensive than cyclical stocks. Additionally, over the past three months to end-May, low beta sectors have, overall, outperformed high beta sectors, despite the market rising slightly.

Asset class outlook

Currencies

Key points

- Increased risk aversion and persistent inflation concerns remain the focus for currency markets.
- A peak in Fed policy may eventually pave the way for broader US dollar weakness. The question remains how long the Fed will keep rates restrictive.

The USD index had been on a steady decline since reaching a peak of 114 in Q4 2022. However, in May we saw a slight rebound as the market weighed if Fed policy had truly reached a peak, or if additional hikes would be required to control inflation. The focus has now shifted to how long the Fed will need to keep rates at an elevated and restrictive level, which has been providing support for the dollar. Additionally, the recent collapse of Silicon Valley Bank and the ensuing stress in the US banking system have caused near-term market volatility. This, along with elevated global recessionary fears, have seen safe-haven flows into the US dollar. In the near term, given the counter-cyclical nature of the US dollar, further downside may be somewhat limited. Sentiment should change in a more meaningful way once the Fed transitions to an easing cycle. Fed Chair Powell noted that officials do not expect any rate cuts in 2023, whereas the market has currently priced the start of a cutting cycle in December.

Through May, the Australian dollar moved in a trading range between USD 0.65 and 0.68 as perceptions of global risks continued to deteriorate, commodity prices fell on a weaker demand outlook, and the RBA retained a relatively dovish stance. Even though the bank delivered a surprise 25bps hike at its May meeting, its relatively less-hawkish stance stands in contrast to the more hawkish Fed outlook. Rate differentials between Australia and the US have since become even more of a headwind, especially as the Fed has indicated another rate hike is possible - or at least that rates will remain higher for longer, with no cutting cycle expected until 2024. CBA continues to expect the Australian dollar to weaken near term, falling to a low of USD 0.62 in September, before recovering slightly to USD 0.65 at year-end. UBS expects it to lift to USD 0.75 by year-end on a relatively weaker US dollar outlook.

The euro had been on a steady comeback since falling to a 20-year low in 2022, though the rally faded in May, with the euro falling back around USD 1.08. US dollar strength has been the currency's main headwind. Interest rate differentials will continue to be an important consideration, given that the ECB's hiking cycle has lagged other major central banks. Although the ECB tapered its hikes to 25bps at its latest meeting, it retained a combative tone on inflation, with the bank likely to keep the policy rate higher until late 2024. This should eventually lead to some compression in Europe/US interest rate differentials once the Fed begins to cut. UBS expects that the euro will continue to strengthen towards USD 1.15 for end-2023, while CBA targets USD 1.08.

Commodities

Key points

- Concerns about weakening economic growth in major economies saw commodities come under further downward pressure during May.
- The near-term demand outlook for commodities remains uncertain, as the market considers the prospect of slowing global growth and increased supply in some areas.

Brent oil prices fell to a 17-month low in May, falling towards USD 70 per barrel (bbl). The outlook for the oil market has darkened in recent weeks, driven by concerns that China's commodity-intensive economy might be slowing faster than expected, casting doubts over the global oil demand outlook. That said, the International Energy Agency recently lifted its forecast for oil markets and pointed to a stronger rebound in China's oil demand following the re-opening of the Chinese economy. An increase in China's oil consumption in 2023 is expected to account for around 59% of global oil demand growth this year. On the supply side, OPEC+ recently announced it would cut production by 1.1 million barrels per day (1.1% of global supply) in May and June, which has also been supportive of prices. Both UBS and CBA recently trimmed their forecasts, now expecting end-2023 prices to reach USD 88 bbl and USD 87 bbl respectively.

After surging more than 70% since November, iron ore prices have since weakened, continuing to fall sharply in May to below USD 100 per tonne (p/t). China remains the key driver, where its recent economic growth target of 'around 5%' disappointed expectations for a stronger, infrastructure-led economic rebound. Additionally, concerns that policymakers in China will intervene in iron ore markets have added downward pressure to prices after the National Development and Reform Commission issued warnings on price gauging and hoarding. China's plan to reportedly reduce steel output again this year also looms as another downside risk to iron ore prices. Note that China's steel output fell approximately 3% in 2021 and 2% in 2022. The plan to reduce China's steel output in 2023 is linked to reducing carbon emissions from China's steel sector and is expected to limit price upside. UBS forecasts USD 111 p/t for end-2023 and USD 91 p/t for end-2024, with long-term prices settling around USD 65 p/t.

Base metal demand is expected to increase notably by 2030 as the world shifts away from fossil fuels to cleaner energy sources, which has been supportive of prices. Optimism that the Fed is nearing the end of its rate-hiking cycle and a weaker US dollar have also been supportive factors. As these decarbonisation trends play out, nickel, copper, aluminium, and lithium graphite all face significant under-supply, which should support prices over the longer term.

Asset allocation views

Strategic asset allocation views

Why do we believe in strategic asset allocation?

We believe that the central component of successful long-term performance is a well-constructed strategic asset allocation. Empirical evidence suggests that a disciplined strategic asset allocation (SAA) is responsible for around 80% of overall investment performance over the long term[1]. Diversification plays a critical role within SAA. By diversifying your portfolio among assets that have dissimilar return behaviour, lower overall portfolio risk can be achieved, and your portfolio can be better insulated during major market downswings.

Why do we advocate SAAs to our clients?

We believe that SAAs encourage a disciplined approach to investment decision-making and help to remove emotion from these decisions. A thoughtfully designed SAA provides a long-term policy anchor for clients. Over the long term, we believe clients are best served by identifying the risk they can bear, then adjusting their return expectations accordingly. Return expectations may be anchored unrealistically. However, risk tolerance tends to remain more consistent throughout the cycle.

Why strategic asset allocation?

Strategic asset allocation is an important part of portfolio construction as it structures your portfolio at the asset class level to match your specific objectives and risk tolerance.

Furthermore, history has shown that a disciplined strategic asset allocation is responsible for around 80% of overall investment performance over the long term.

Strategic asset allocations in models

	Yield (%)	Balanced (%)	Growth (%)	Endowment (%)
Cash	3	3	3	3
Fixed income	53	35	17	14
Short maturity	8	6	3	3
Government bonds	32	15	7	5
Investment grade credit	11	11	4	4
High yield credit	2	3	3	2
Equities	24	42	60	38
Domestic	12	19	28	11
United States	6	11	16	13
Europe (ex-UK)	3	4	5	4
United Kingdom	2	3	4	3
Emerging markets	1	5	7	7
Alternatives	20	20	20	45
Hedge funds	6	6	5	14
Private markets	7	7	9	17
Real assets	7	7	6	14

Source: LGT Crestone Wealth Management. Investment grade credit includes Australian listed hybrid securities.

[1] Ibbotson, Roger G., and Paul D. Kaplan. 2000. Does Asset Allocation Policy Explain 40, 90, or 100 Percent of Performance? Financial Analysts Journal, vol. 56, no. 1 (January/February).

Active portfolio weights and tactical asset allocation views

Our current tactical asset allocation views

It is beginning to look like central banks are now closer to the end of their policy rate-hiking programs. However, with respect to interest rates and core inflation pressures, Europe and the UK are still a little behind other developed markets, with more adjustment ahead.

In Australia, recent data suggest activity was relatively flat in early 2023. That said, it is expected that Australia can avoid a recession and will outperform other developed economies, helped by a pick-up in growth in China, increased immigration, and the recent (moderate) budget stimulus. Offshore, inflation and rates are easing in most developed markets, except in the UK where inflation remains stubborn. It is also possible that Europe and the UK will avoid a recession and post positive, albeit low, growth.

Our cautious view is reflected in our positioning. Shorter term, we expect fixed income to outperform equities under various scenarios, though we continue to look for an opportunity to add equity risk.

Why tactical asset allocation?

Tactical asset allocations have a six to 12-month investment horizon and are reviewed monthly. They can be considered an interim strategy where the aim is to provide a smoother investment journey without altering the end goal.

Cash

We have moved slightly underweight cash to fund an increase in investment grade credit.

Fixed income

We have increased our overweight to fixed income by adding to our position in investment grade credit. We are cautious about risk assets, as they continue to grind higher despite mixed fundamentals and economic data, as well as the potential for tighter credit conditions. If market volatility rises, we believe that fixed income, particularly government bonds and investment grade credit, will hold up relatively well, particularly if the growth outlook deteriorates from here.

Alternatives

We favour increasing allocations to hedge funds and unlisted infrastructure, while deployed private equity is our least preferred sub-asset class within alternatives.

Equities

We are underweight equities and continue to prefer non-US markets. Although equities continue to surprise with respect to earnings and margins, sentiment is mixed. We are overweight domestic equities and emerging markets due to attractive valuations (on a relative basis), as well as the potential for tailwinds associated with China's re-opening and stronger activity.

Active portfolio weights and active tactical asset allocation tilts

	Active tilt		Yield (%)	Balanced (%)	Growth (%)	Endowment (%)
Cash	-1	V	2	2	2	2
Fixed income	2	Λ	55	37	19	16
Short maturity	-1		7	5	2	2
Government bonds	2		34	17	9	7
Investment grade credit	2	Λ	13	13	6	6
High yield credit	-1		1	2	2	1
Equities	-1		23	41	59	37
Domestic	1		13	20	29	12
United States	-1		5	10	15	12
Europe (ex-UK)	-2		1	2	3	2
United Kingdom	0		2	3	4	3
Emerging markets	1		2	6	8	8
Alternatives	--		20	20	20	45

V Decreased weight this month   Λ Increased weight this month

Source: LGT Crestone Wealth Management. Investment grade credit includes Australian listed hybrid securities.

Our view on fixed income

Short maturity

We are underweight short maturity. We favour a more balanced position in duration-related bonds and credit securities, as aggressive monetary policies from central banks have sufficiently repriced bond yields. Our base case is that central banks will be required to ease monetary policy in late 2023 or early 2024, making a duration play in fixed rate outperform floating rate over time.

Government bonds

We are overweight government bonds. With expectations of modest further central bank rate hikes over coming months now priced into markets (both domestically and offshore) and yields elevated, we remain overweight government bonds. Although it is difficult to forecast the absolute peak in yields, government bonds have largely absorbed rising rates (which we expect will reach a peak in Q3 2023).

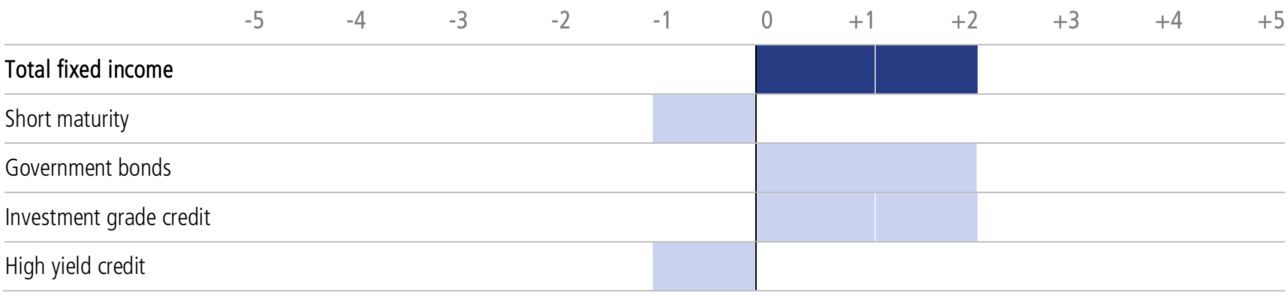
Investment grade credit

We are overweight investment grade credit where we believe spreads are fair value. This month, we increased our overweight to investment grade credit. We believe that higher outright yields, helped by a wider swap curve cushion, will limit any widening in investment grade credit spreads.

High yield credit

We are underweight high yield credit. With central banks unlikely to ease near term, and unemployment yet to rise, high yield credit spreads are vulnerable to some widening. We believe spreads have not widened sufficiently to compensate for higher funding costs and a higher liquidity premium. They are also vulnerable to a potential acceleration in defaults as interest rates rise more than initially anticipated and as the global economy slows.

Active fixed income weights (%)—We are overweight fixed income



Fixed income market summary

Fixed income indices	Current	One month ago
Australian iTraxx	80.94	90.00
Australian 3-year yield	3.43%	2.95%
Australian 10-year yield	3.68%	3.30%
Australian 3/10-year spread	24.0 bps	34.5 bps
Australian/US 10-year spread	-1.0 bps	-14.8 bps
US 10-year Bond	3.69%	3.45%
German 10-year Bund	2.34%	2.40%
UK 10-year Gilt	4.25%	3.73%
Markit CDX North America Investment-Grade Index	74.4 bps	79.0 bps
Markit iTraxx Europe Main Index	80.5	86.0
Markit iTraxx Europe Crossover Index	427.2	453.2
SPX Volatility Index (VIX)	17.5	18.8

Source: LGT Crestone Wealth Management, Bloomberg as at 30 May 2023. Pricing based on UBS Global Research. Active fixed income weights sourced from LGT Crestone Wealth Management. Units refer to the percentage point deviation from strategic asset allocation.

Our view on equities

Domestic equities

We are overweight domestic equities. The 12-month forward P/E for the S&P/ASX 200 is 14.5x, which features in the bottom quartile of valuations over the past decade. With its leverage to a re-opening in China, a likely near-term pause in policy tightening, and a dividend yield almost twice that of the MSCI World index, Australia remains an overweight.

US equities

We are underweight US equities. With valuations on the S&P 500 now back to 18.5x (and 25x for the NASDAQ), US equities appear vulnerable to any earnings disappointments that may emerge (with Q2 reporting season ahead). The recently agreed US debt ceiling increase needs to be passed, while credit spreads on a US default are now the highest on record.

European (ex-UK) equities

We are underweight European (ex-UK) equities. European equities have been able to trade on a raft of 'less negative' issues. However, with the index within 5% of all-time highs, further momentum from here may be more difficult. High inflation is also proving more problematic than elsewhere, raising the risk that sentiment and earnings growth may be impacted by ongoing central bank policy tightening.

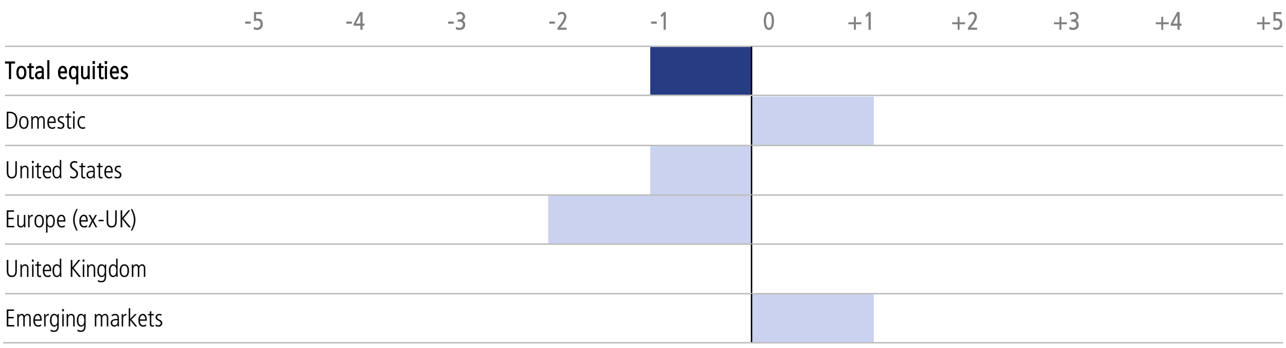
United Kingdom equities

We are neutral UK equities. The UK is a deep-value market with a defensive bias. It has the highest correlation to 'value as a style' among all the major regions. Like Australia, its China-related exposure (mining and energy) and its large healthcare exposure (which provides defensive qualities) should offer a degree of comfort in an uncertain market.

Emerging market equities

We are overweight emerging market equities. We believe the recent pull-back is a correction that should be bought. China remains a key focus for investors and appears to be in the midst of a 'savings boom', with excess consumer savings at a record 10% of GDP. While relatively moderate by historic standards, we expect China to still recover solidly over the coming year, supporting broader emerging market earnings.

Active equity weights (%)—We are underweight equities



Equity market summary

Region	Index	Latest price	Consensus 1 yr Target	Consensus 1 yr Upside	Next year P/E [1]	Next year D/Y [2]
Australia	S&P ASX 200	7209.3	7725.8	7.2%	14.5	4.31%
New Zealand	S&P NZ 50	11878.7	12867.5	8.3%	23.5	3.44%
United States	S&P 500	4205.5	4740.5	12.7%	17.4	1.66%
Europe	Euro Stoxx	451.7	537.7	19.0%	11.7	3.55%
United Kingdom	FTSE 100	7522.1	9114.6	21.2%	10.2	4.27%
China	CSI 300	3224.2	4004.3	24.2%	9.8	3.12%
Japan	Nikkei 225	31328.2	32799.1	4.7%	17.7	1.94%
India	Sensex	62969.1	70694.3	12.3%	20.7	1.44%

Source: Bloomberg. Data as at 30 May 2023; 1 P/E = Price to earnings ratio; 2 D/Y = Dividend yield. Active equity weights sourced from LGT Crestone Wealth Management. Units refer to the percentage point deviation from strategic asset allocation.

Our view on alternatives

Hedge funds

Low beta hedge fund strategies are preferred, but credit remains attractive. Market volatility continues to provide a ripe hunting ground for hedge funds, where mis-pricing has created opportunities across asset classes for skilled managers. Heightened macro-economic and geo-political uncertainty is also presenting attractive opportunities for discretionary macro strategies, while idiosyncratic credit strategies should provide increasingly attractive risk-adjusted return opportunities in 2023. We are, therefore, focusing on satellite exposures in those areas, alongside diversified multi-strategy solutions that can take advantage of the wider investment universe.

Private markets

The normalisation of valuations should present an attractive deployment opportunity for private equity and venture in 2023. While private equity is least preferred on a relative risk-adjusted basis when compared to other alternative assets, we believe 2023 will be an attractive year to deploy new capital. 2022 served as a re-calibration with regards to private market valuations, particularly within the venture and growth sectors. As such, entry valuations are readjusting meaningfully, while secondary (fund) market activity is beginning to pick up. We recommend maintaining exposures to private equity and venture capital, albeit investors should have a preference for new primary and secondary fund commitment structures.

Private debt looks increasingly attractive as yields reset higher on the back of interest rate increases. If investors do not compromise on credit quality and cater for increased debt servicing costs, private debt should be attractive due to wider spreads, credit protections relative to public market equivalents, and their typically floating rate structures. We prefer direct lending and sponsor-backed transactions versus broadly syndicated strategies, as loan terms can be negotiated directly, offering greater protection to the end investor. We also prefer corporate transactions relative to real estate lending strategies that are often heavily focussed on construction, a sector more exposed to supply-chain disruption, contractor risk and rising rates.

Real assets

Real estate allocations should prioritise core-plus, high-quality assets. We have a neutral view on real estate, given ongoing weakness across certain sectors. We see a meaningful dichotomy across different assets, sectors, and investment approaches, and a particular bifurcation between prime office and lower grades worldwide. To that effect, we prefer high-grade commercial assets where there is some ability to add value through up-leasing, repositioning, or marking rents to market, for example. These initiatives can help to partially offset ongoing valuation declines, arising from interest rate increases. We also like high-quality, overseas, multi-family accommodation. This can benefit during periods of higher inflation, as shorter lease terms allow rents to mark to market more often. In addition, firms that have prudently put in place longer-term debt facilities at attractive rates, and those with conservative long-term discount rate assumptions, are likely to provide a superior experience for investors.

Infrastructure is our most favoured sub-asset class. Infrastructure can provide more defensively positioned core assets on long-term, typically inflation-linked contracts. This can provide both a defensive ballast and inflation protection, both of which are in high demand currently. With most COVID-19 related travel restrictions likely behind us, volume-based transport-related assets, such as airports, and contracted assets should play a key role in diversified portfolios. Further, we see attractive investment opportunities focussed on energy transition.

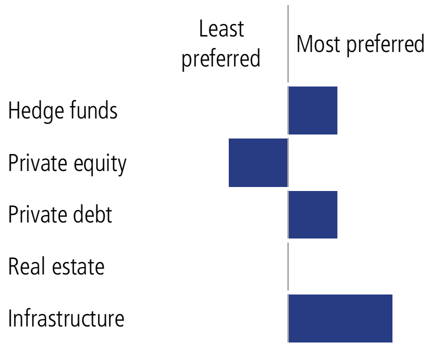
Our most preferred and least preferred exposures—We continue to favour infrastructure, private debt, and low-beta hedge fund exposures while maintaining private equity and real estate exposures

What we like

- Multi-strategy, credit-oriented and discretionary macro hedge funds
- Domestic private debt and asset-backed securities (excluding real estate)
- Core and core-plus infrastructure assets with inflation linkages
- Private market and real assets exposed to the global energy transition

What we don't like

- Passive private market and/or real asset strategies
- Lower grade and/or buy-and-hold real estate assets
- Pre-IPO strategies
- Construction and/or junior lending within real estate
- Carbon-intensive assets and industries with no transition plan



Direct equity

Recommendations: Domestic equities—Best sector ideas

Objective of this list

The objective is to identify the best business models or best in breed by GICs Industry Group for longer-term investors. While we also overlay valuation, companies are included based on anticipated three to five-year performance. When analysing companies to add to the list, some metrics we consider are:

- **Profitability measures**—Return on net operating assets, return on invested capital, free cashflow and return on equity
- **Liquidity and leverage**—Net debt to equity, Altman Z-score, net debt to earnings before interest, tax, depreciation and amortisation (EBITDA)
- **Efficiency**—Capital expenditure to sales
- **Valuation**—Price/earnings ratio, price/book ratio, enterprise value to sales and EBITDA, private equity screens

Code	Company	Sector	Market price	Consensus upside	P/E 1yr fwd (x)	Dividend yield	ROIC	ROE	1yr EPS growth	MSCI ESG rating
REA	REA Group	Com. Services	$137.29	-2%	48.8	1.1%	29%	27%	22.5%	AA
ALL	Aristocrat Leisure	Cons Discret	$37.66	19%	19.1	1.7%	22%	20%	7.6%	AA
TLC	Lottery Corp	Cons Discret	$4.95	7%	30.6	3.1%	22%	125%	12.3%	AA
MTS	Metcash	Cons Staples	$3.65	12%	11.7	6.1%	21%	27%	-4.2%	--
ALD	Ampol	Energy	$31.86	16%	11.6	5.9%	16%	18%	-2.3%	AA
MQG	Macquarie Group	Financials	$175.10	10%	15.4	3.9%	na	13%	6.7%	AA
IAG	Insurance Australia Group	Financials	$5.21	4%	23.3	3.1%	na	10%	66.1%	AA
RMD	ResMed	Health Care	$33.22	14%	33.3	0.5%	28%	25%	13.8%	A
CSL	CSL	Health Care	$308.24	12%	37.3	0.8%	15%	17%	28.7%	A
MND	Monadelphous Group	Industrials	$12.44	4%	23.0	3.9%	13%	13%	21.8%	--
ALU	Altium	IT	$38.79	6%	50.7	1.2%	34%	23%	25.3%	--
XRO	Xero	IT	$109.91	0%	113.3	0.0%	10%	13%	56.1%	AA
IGO	IGO	Materials	$14.58	8%	7.3	2.5%	37%	36%	-13.4%	AA
JHX	James Hardie Industries	Materials	$38.14	5%	20.2	0.0%	41%	30%	13.4%	AA
GMG	Goodman Group	Real Estate	$20.05	12%	21.3	1.5%	10%	10%	10.5%	AA
ORG	Origin Energy	Utilities	$8.37	4%	26.1	4.4%	9%	5%	62.0%	A

Source: UBS Global Research, Bloomberg Analyst consensus and MSCI Research. Data as at 30 May 2023. ESG is environmental, social and corporate governance.

Trade opportunities

Please note the following opportunities may not fully satisfy metrics for the above table.

IGO Group (IGO)—Buy. IGO's 20% pull-back from its peak provides an attractive entry opportunity. Chile's recent moves to effectively nationalise its vast lithium industry should refocus investors' attention on the strategic importance of lithium and the attractive jurisdiction in which IGO operates.

Xero Limited (XRO)—Buy. XRO's software should be viewed largely as non-discretionary, and its Software as a Service (SaaS) delivery mode gives the company the ability to pass on price increases at regular intervals, with little to no churn. A 15% reduction in workforce (700 - 800) roles has been announced, which will aid profitability and free cash flow.

REA Group (REA)—Buy. REA is one of the highest quality companies globally. Although housing finance is already experiencing its biggest contraction since the GFC, history suggests that this should trough some two to three months after the end of the tightening cycle. The tightening cycle leads house prices by two to three months.

Recommendations: Domestic equities—Sustainable income

Objective of this list

This objective is to generate 'sustainable income' over time. Historically, companies that grow their dividends consistently can offer superior long-term performance. While we also overlay valuation, companies are included based on anticipated three to five-year performance. When analysing companies to add to this list, some metrics we consider are:

- **Profitability measures**—Return on assets, cashflow, return on invested capital and return on equity
- **Liquidity and leverage**—Net debt to equity
- **Efficiency**—Change in revenue, EBITDA and margins
- **Management signalling**—Dividend growth and pay-out ratios

Code	Company	Sector	Market price	Consensus upside	P/E 1yr fwd (x)	P/B 1yr fwd (x)	Franking	Grossed up yield	1yr DPS growth	MSCI ESG rating
IAG	Insurance Australia Group	Financials	$5.21	4.1%	14.0	1.97	30%	3.1%	71.1%	AA
MQG	Macquarie Group Ltd	Financials	$175.10	9.8%	14.4	1.95	40%	3.9%	5.3%	AA
WBC	Westpac Banking Corp	Financials	$21.11	6.2%	10.9	1.02	100%	6.7%	1.5%	A
QBE	QBE Insurance Group Ltd	Financials	$14.85	15.5%	8.7	1.60	10%	3.4%	16.7%	AA
COL	Coles Group Ltd	Cons Staples	$18.21	1.4%	22.0	7.21	100%	3.6%	2.0%	AA
MTS	Metcash Ltd	Cons Staples	$3.65	11.8%	12.2	3.27	100%	6.1%	-4.5%	AAA
SGR	Star Entertainment Grp	Cons Discret	$1.19	22.2%	29.6	0.57	100%	0.0%	na	BBB
TAH	Tabcorp Holdings Ltd	Cons Discret	$1.14	7.9%	29.2	0.97	100%	1.7%	15.8%	AA
TLS	Telstra Corp Ltd	Com. Services	$4.39	5.5%	23.4	3.34	100%	3.9%	6.5%	AA
NEC	Nine Entertainment Co	Com. Services	$1.91	31.4%	11.3	1.70	0%	6.0%	1.8%	AA
RMD	ResMed Inc	Health Care	$33.22	14.4%	29.3	7.85	100%	0.5%	7.3%	A
PME	Pro Medicus Ltd	Health Care	$60.40	-10.6%	87.4	53.95	100%	0.5%	22.8%	BBB
REP	RAM Essential Services	Real Estate	$0.66	39.4%	11.2	1.2	0%	8.8%	1.7%	--
SGP	Stockland	Real Estate	$4.36	-1.9%	13.8	1.0	0%	6.1%	-2.6%	AAA
IRE	IRESS Ltd	IT	$10.23	5.7%	25.3	4.27	0%	4.2%	2.5%	AA
DBI	Dalrymple Bay Infra.	Industrials	$2.60	12.1%	14.6	1.11	0%	8.0%	5.3%	--
ALX	Atlas Arteria Ltd	Industrials	$6.39	2.2%	13.9	0.94	0%	6.3%	1.2%	AA
ORG	Origin Energy Ltd	Utilities	$8.37	3.8%	16.1	1.66	100%	4.4%	-1.6%	A
ALD	Ampol Ltd	Energy	$31.86	16.0%	11.9	2.09	100%	5.9%	-0.9%	AA
BPT	Beach Energy	Energy	$1.43	23.3%	6.5	na	100%	2.9%	69.0%	AA
BHP	BHP Group Ltd	Materials	$43.49	7.6%	10.0	3.4	100%	4.7%	-9.8%	A
AMC	Amcor PLC	Materials	$15.14	4.1%	13.2	na	0%	3.1%	2.5%	AA

Source: UBS Global Research, Bloomberg Analyst consensus and MSCI Research. Data as at 30 May 2023. ESG is environmental, social and corporate governance.

Trade opportunities

Please note the following opportunities may not fully satisfy metrics for the above table.

Metcash Limited (MTS)—Buy. MTS is now trading at a 12-month forward dividend yield of 5.4%, which is not far removed from the 6% yield that marked previous share price lows in 2017 and financial year 2018/19.

Beach Energy (BPT)—Buy. Based on the outlook for gas pricing, peak capex in financial year 2023/24, and production growth that is greater than 20%, Beach Energy is expected to generate around AUD 850 million in free cash flow from financial year 2025. This should lead to a free cash flow yield of almost 30% and a dividend yield of over 8%.

Ampol (ALD)—Buy. ALD is trading at 9.6x 2023 earnings, a 37% discount to its historical average of 15.3x and largely in line with global peers, which are at 9.7x. The business is now structurally better positioned and recent weakness presents a buying opportunity.

Recommendations: International equities—Best sector ideas

Objective of this list

The objective is to provide a list of large-cap international companies across sectors with sustainable business models that generate compounding returns on investment and capital over the longer term. While we also overlay valuation, companies are included based on anticipated three to five-year performance. When analysing companies to add to the list, some metrics we consider are:

- **Profitability measures**—Return on net operating assets, return on invested capital, free cashflow and return on equity
- **Liquidity and leverage**—Net debt to equity, Altman Z-score, net debt to EBITDA
- **Efficiency**—Capital expenditure to sales
- **Valuation**—Price/earnings ratio, price/book ratio, enterprise value to sales and EBITDA, private equity screens

Code	Company	Sector	Base CCY	Market price	Consensus upside (%)	P/E 1yr fwd (x)	Yield (%)	Market cap (USD bn)	MSCI ESG rating
LSEG LN	London Stock Exchange	Financials	GBP	8480.00	12.4	22.0	1.5	58,073	AA
LLOY LN	Lloyds Banking Group	Financials	GBP	45.22	41.1	5.9	6.6	36,545	AA
WFC US	Wells Fargo & Co	Financials	USD	40.98	19.3	8.4	3.7	153,766	BB
2318 HK	Ping An Insurance	Financials	HKD	50.65	40.2	5.1	5.5	121,580	A
939 HK	China Construction Bank	Financials	HKD	5.08	32.6	3.2	8.4	164,654	A
2330 TT	Taiwan Semiconductor	IT	TWD	566.00	9.4	14.5	2.2	479,236	AAA
MA US	Mastercard Inc	IT	USD	367.50	17.8	25.2	0.7	348,254	AA
ASML NA	ASML Holding	IT	EUR	683.10	4.4	30.3	1.1	295,514	AAA
GOOGL US	Alphabet Inc	Comm Services	USD	123.67	5.6	18.0	0.0	1,576,364	BBB
UMG NA	Universal Music Group	Comm Services	EUR	18.71	38.3	20.1	2.9	36,556	AA
DIS US	Walt Disney Co/The	Comm Services	USD	87.82	38.6	16.5	1.0	160,474	A
9988 HK	Alibaba Group Holding	Cons Discret	HKD	78.80	73.9	8.7	0.0	208,215	BBB
NKE US	NIKE Inc	Cons Discret	USD	106.52	26.4	26.6	1.3	163,720	BBB
SBUX US	Starbucks Corp	Cons Discret	USD	97.75	17.8	23.9	2.4	112,061	A
ABNB US	Airbnb Inc	Cons Discret	USD	107.19	20.7	26.0	0.0	68,543	BB
RACE IM	Ferrari NV	Cons Discret	EUR	270.30	4.4	37.7	0.9	52,190	BB
BA US	Boeing Co/The	Industrials	USD	204.69	15.6	35.3	0.8	123,140	BBB
DSV DC	DSV A/S	Industrials	DKK	1343.50	4.6	21.7	0.6	42,396	AA
MSFT US	Microsoft Corp	IT	USD	331.21	2.2	30.1	0.8	2,462,708	AAA
ILMN US	Illumina Inc	Health Care	USD	194.51	22.3	61.9	0.0	30,752	AA
NOVOB DC	Novo Nordisk A/S	Health Care	DKK	1116.00	3.4	27.4	1.7	362,620	AAA
ISRG US	Intuitive Surgical Inc	Health Care	USD	307.07	1.4	49.0	0.0	107,597	A
EL US	Estee Lauder	Cons Staples	USD	191.91	24.7	36.0	1.4	68,591	A
COST US	Costco Wholesale Corp	Cons Staples	USD	508.03	6.6	32.9	0.8	225,170	A
288 HK	WH Group Ltd	Cons Staples	HKD	4.15	62.1	4.9	1.0	6,797	BBB
SHW US	Sherwin-Williams	Materials	USD	228.44	10.8	23.0	1.2	58,912	A
SHELL NA	Shell PLC	Energy	EUR	26.71	24.7	6.0	4.8	194,558	AA
EQIX US	Equinix Inc	Real Estate	USD	734.51	8.0	59.3	2.0	68,694	AA
ORSTED DC	Orsted AS	Utilities	DKK	617.40	17.7	28.8	2.5	37,398	AAA
		Average Yield:					1.9%		

Source: UBS Global Research, Bloomberg Analyst consensus and MSCI Research. Data as at 30 May 2023. ESG is environmental, social and corporate governance.

Recommendations: Thematic investing—Electric vehicles

Objective of this list

Thematic investing is an approach which focuses on predicting long-term trends rather than specific companies or sectors. As it is also often associated with secular forces, this means it can provide investors with exposure to themes that are expected to grow at rates above economic growth over the longer term. Thematic investing is best suited to longer-term investors and those looking for opportunities beyond the comparatively smaller investment universe that exists in Australia. Some key themes that investors are exploring include:

- Climate change
- Cryptocurrency and blockchain
- Demographics
- Electric vehicles
- Healthcare and genomics
- Inflation
- Metaverse
- Security and safety
- Supply chain disruption
- Sustainable investing

Electric vehicles—Select exposures

Global penetration of electric vehicles is accelerating, offering investment opportunities across the value chain – from raw material commodities to auto component manufacturers and infrastructure providers.

Code	Company	Sector	Base CCY	Market price	Consensus upside (%)	P/E 1yr fwd (x)	Yield (%)	Market cap (USD bn)	MSCI ESG rating
NVDA US	NVIDIA Corp	IT	USD	$401.11	9.9	43.2	0.1	990,742	AAA
INTC US	Intel Corp	IT	USD	$29.99	6.6	18.4	2.3	125,088	AA
AMD US	Advanced Micro Devices	IT	USD	$125.27	-17.6	31.1	0.0	201,730	AA
MU US	Micron Technology Inc	IT	USD	$71.69	-2.3	109.6	0.6	78,457	A
NXPI US	NXP Semiconductors NV	IT	USD	$182.07	10.5	12.8	2.3	47,291	AAA
IFX GY	Infineon Technologies	IT	EUR	$35.10	35.2	13.4	1.3	49,182	AA
APTV US	Aptiv PLC	Cons Discret	USD	$91.23	38.4	15.3	0.4	24,678	AA
FR FP	Valeo	Cons Discret	EUR	$19.09	19.5	7.6	4.2	4,988	AAA
FCX US	Freeport-McMoRan Inc	Materials	USD	$34.23	36.2	15.4	1.6	49,061	BBB
IGO AU	IGO Ltd	Materials	AUD	$14.58	7.8	8.4	2.8	7,194	AA
QCOM US	QUALCOMM Inc	IT	USD	$116.00	15.4	11.9	2.8	129,224	A
300750 CH	Contemporary Amperex Technology	Industrials	CNY	$224.99	42.2	16.0	0.9	139,708	A
51910 KS	LG Chem Ltd	Materials	KRW	$702,000	36.8	12.4	1.7	37,538	BBB
AAPL US	Apple Inc	IT	USD	$177.30	2.1	27.1	0.6	2,788,699	BBB
GOOG US	Alphabet Inc	Comm Services	USD	$124.64	5.6	18.2	0.0	1,576,364	BBB
TSLA US	Tesla Inc	Cons Discret	USD	$201.16	-4.8	41.8	0.0	637,577	A
VOW GY	Volkswagen AG	Cons Discret	EUR	$146.35	22.5	4.5	6.6	72,636	B
HON US	Honeywell International	Industrials	USD	$194.55	14.3	19.3	2.3	129,507	AA
		Average Yield:					1.9%		

Source: UBS Global Research, Bloomberg Analyst consensus and MSCI Research. Data as at 30 May 2023. ESG is environmental, social and corporate governance.

Important information

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