Politics to drive geo-politics in 2024

Navigating a historic election year

Core Offerings

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

February 2024

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Navigating a historic election year

AN UPDATE FROM LGT CRESTONE'S CHIEF INVESTMENT OFFICER

Scott Haslem
Chief Investment Officer

Markets have quickly embraced our call to look beyond 'higher for longer' and focus on a path to lower rates in 2024. This has led to an aggressive fall in global bond yields in late 2023. With rising risks of a soft landing for growth, equities have also had a positive start to the year. Yet, as we discuss in this month's *Core offerings*, despite this more positive macro backdrop, investors will likely need to navigate an alternative powerful force in 2024, namely politics. With more than half the world's population going to the polls in 2024—including in the US, UK and India—politics could well be the factor that drives geo-political volatility. This month, we are closing our modest overweight in emerging market equities and our modest underweight in US equities, while trimming our bond overweight.

The worlds' central banks may well be still focused on holding their policy rates 'higher for longer' to ensure they walk the last mile of the inflation journey…

…but financial markets have quickly moved to factor in the next phase of the cycle, which almost certainly embodies lower interest rates.

Markets look beyond 'higher for longer' and embrace a lower rate outlook

The worlds' central banks may well still be focused on holding their policy rates 'higher for longer'—maybe into H2 2024—to ensure they walk the last mile of the inflation journey and safeguard an inflation outlook consistent with their inflation targets. In and of itself, securing a future where inflation is relatively low (even if not as low as during 'the great moderation') and avoiding turning dovish too soon should be viewed as an important driver of a positive market backdrop for investors over the next few years.

However, since early December 2023, when we penned our 2024 outlook, *The path ahead points to lower rates*, markets have embraced our challenge to look beyond the 'higher-for-longer' theme. They have moved quickly over the past couple of months to factor in the next phase of the cycle, which almost certainly embodies lower interest rates. Arguably, bond markets moved too far too fast as 2023 came to end, underpinning one of the most aggressive falls in 10-year bond yields in history. US Treasuries fell from a peak of 5.02% in late October to 3.78% in mid-December (see chart below). Credit spreads also tightened.

Given this reflected a significant share of our forecasted fall in bond yields for all of 2024, we trimmed our overweight to government bonds in late December, ensuring we captured some of this tactical outperformance. Fixed income, nonetheless, had a strong finish to 2023, with benchmarks alone delivering about 6% in November and December.

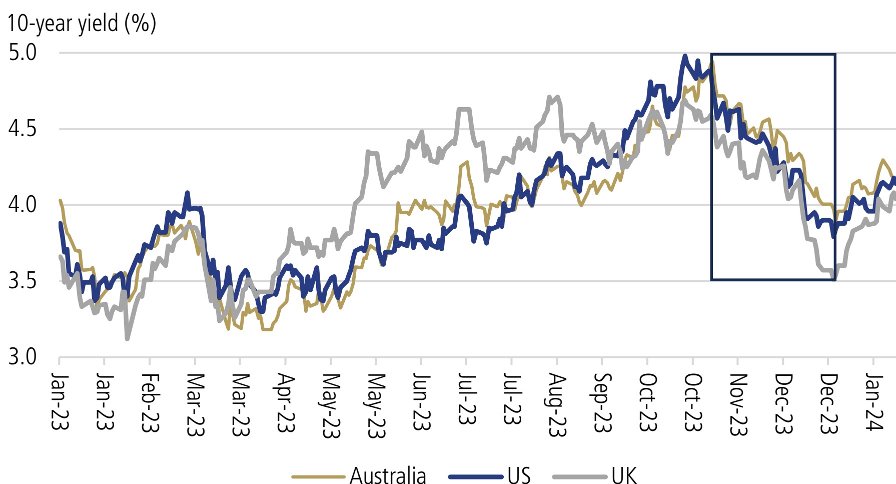
In their defense, markets were responding to a number of data developments in late November and December that accelerated confidence in our 'path to lower rates' thesis for 2024. Most importantly, core inflation is falling further, annualising in the three months to December at 2.0% in the US (from 4.2% mid-year), at -0.8% in Europe (from 5.5% mid-year), and 3.2% in the UK from (6.9% mid-year. In Australia, the monthly inflation indicator fell to 4.3% in November from 5.4% for Q3 (see chart on following page).

In December, "the Fed validated market expectations of non-recessionary monetary policy easing by forecasting three 0.25% rate cuts in 2024, the first of which may come as early as March based on previous comments from Governor Christopher Waller".

BCA Research
December 2023

Furthermore, the tone of central banks also shifted in late 2023 to more clearly flag that policy rates had peaked, signalling rate cuts were likely in H2 2024. But, for policymakers, the aggressive market pricing that emerged – six rate cuts in the US from March this year – has led to more 'moderate' messaging re-emerging from central banks, and US Treasuries have partially reversed course in early 2024 to around 4.05%.

Bond yields rallied sharply in November and December as rate cuts came into view



Source: Macrobond, LGT Crestone.

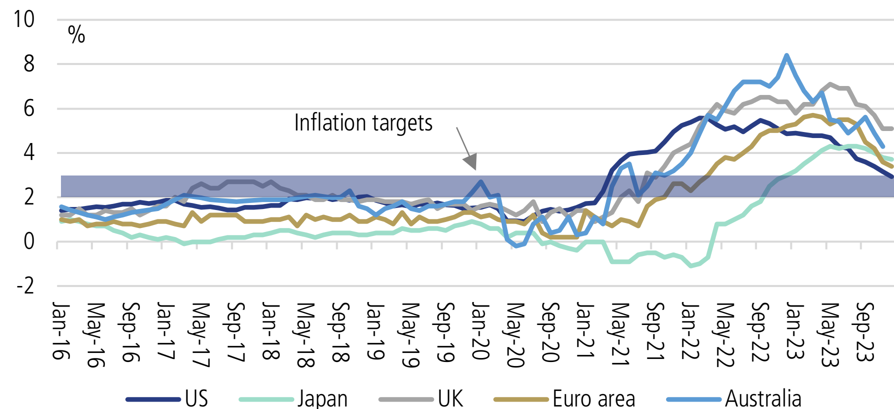
"The risk of a US soft landing is growing."

CBA
January 2024

For equities, they may well have also been pre-emptively harvesting some of our expected positive returns that we flagged for H2 2024. The combination of falling inflation and still surprisingly resilient growth (at least in the US and Australia but less so in the UK, Europe and China where activity has disappointed), has led markets to lower the probability of a hard economic landing in 2024. Together with rising hopes of lower interest rates ahead—easing one of the valuation headwinds—this has driven a positive backdrop for equities (despite early-year wobbles as market interest rates reversed some of their late 2023 rally).

Despite their early-year wobbles, equity markets may also be pre-emptively harvesting some of our expected positive returns that we flagged for H2 2024. Falling inflation and the prospect of lower rates (easing one of the valuation headwinds) have driven a positive backdrop for equities to date in 2024.

Inflation has continued to fall quickly toward central bank targets



Source: Macrobond, LGT Crestone (Australia headline, US core PCE, others core).

Our core views for 2024 remain unchanged—we make some modest TAA changes

As 2024 gets underway, our core views remain unchanged. The global economy is slowing, and inflation is moving gradually lower. Reflecting this, we continue to expect H1 2024 to favour fixed income returns over equity returns. If major central banks start signalling the next move in rates is down, as we expect in H1 2024, government bonds and investment grade credit should deliver strong returns. Moreover, with only a moderate easing cycle ahead, this should still present the opportunity to add defensive yield to portfolios.

We expect central banks to trim rates by 0.5-1.0% during H2 2024, a relatively modest move in a historic context, given inflation is likely to settle higher than in the recent past.

For equities, we continue to believe the opportunity to turn more bullish equities may emerge in H2 2024. Slowing growth through H1 has the potential to challenge currently bullish corporate earnings expectations, which at 11% for the US, appear on the optimistic side (in tandem with current bullish rate cut expectations). Reflecting this, as we transition H1, for now we remain neutral equities, noting an increasingly constructive backdrop.

Nonetheless, this month we have made some adjustments to our tactical positioning 'within' asset classes. This reflects the more reflationary environment that is emerging.

We maintain our preference for fixed income returns (overweight) relative to equity returns (neutral)…

…However, we have closed our US equity underweight and added to high-yield credit, reflecting less chance of an economic hard-landing ahead.

- **We have neutralised our underweight to US equities**, funded from closing our overweight to emerging market equities. This reflects growing evidence that the US economy remains resilient, as well as recognising the significant cyclical and structural challenges facing emerging markets, in particular China. A rising risk of geo-political volatility is also likely to favour the US over emerging markets.
- While we maintain our strong conviction overweight to fixed income as a whole, **we have tilted our allocation toward high yield credit**, funded by reducing our overweight government bond position. This also partially reflects the resilience of the US economy, taking advantage of still attractive all-in yields in the asset class and on the margin reduces exposure to government term premia.

We believe these two changes better set our tactical positioning in an environment where US economic growth might remain more resilient than expected amid easing financial conditions and as political considerations ramp up in the lead-up to the US Presidential elections. Indeed, were the global economy to face growth or geo-political challenges in the year ahead, the US equity market may prove defensive in a risk-off environment.

Politics to drive geo-politics in 2024

Yet, despite the arguably positive backdrop unfolding in 2024 from a macro perspective, markets will also likely have to navigate an alternative powerful force, namely politics. In 2024, politics takes centre stage, and not just in the US with the Presidential election. 2024, according to UBS, is the "biggest election year in human history", with more than half the world's population going to the polls in more than 70 elections globally. This includes India, the UK, Indonesia, and the European Parliament.

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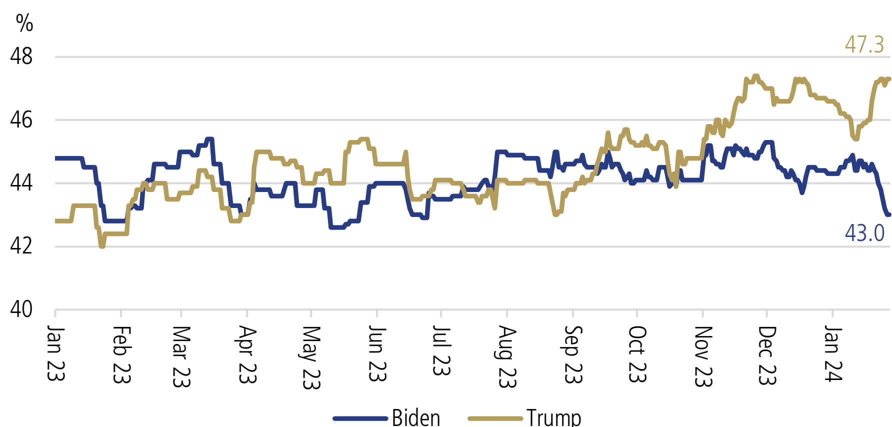
…according to UBS, 2024 is the "biggest election year in human history", with more than half the world's population going to the polls in more than 70 elections globally.

While some will argue such events rarely impact markets in a sustainable way, there is potentially a greater risk that this year's elections will reach beyond just domestic politics, instead impacting the geo-political landscape. Sure, the US election in late 2024 may be expected to impact outcomes more particularly during 2025. But while the potential for former President Trump to receive the Republican nomination may be seen as a positive for supporters of president Joe Biden, the prospect of former President Trump being re-elected is increasingly likely to be priced to varying degrees in markets through 2024.

In addition to risks around fiscal stimulus, US Federal Reserve (Fed) policy, and bond yields, any increase in the probability of a shift in the US' electoral status quo could have meaningful impacts on geo-politics events, such as global trade wars (rising protectionism), the US' ongoing support for Ukraine's military efforts, as well as tensions with China and the South China Sea. The carry-through to supply chains and inflation could start to meaningfully impact markets. Elections elsewhere could also have the potential to impact returns in different regions.

Former President Trump leading in 'general election polling'



Source: RealClearPolitics, Macrobond, LGT Crestone.

"[A Trump] victory in the 2024 US presidential election would put the fate of liberal democracy in the hands of a demagogue who undermines its most basic principles."

Chris Patten
Former British Governor of Hong Kong and a former EU Commissioner
January 2024

US elections: Former President Trump increasingly looks likely to receive the Republican nomination, while President Biden is the presumptive Democratic nominee. Markets are thus likely to soon start focusing on a 2020 rematch and any implications for US domestic and foreign policy. A Biden victory is arguably a known status quo, though the extent of any victory (and a likely split Congress) may impact his ability to pursue his priorities.

In contrast, there is much less visibility over what a Trump victory could look like, though greater clarity may emerge in coming months. Investor concerns have highlighted issues, such as a potential US withdrawal from Ukraine or the North Atlantic Treaty Organization (NATO), as well as whether Trump would follow through with plans to put a 10% tariff on all imports to the US (to fund tax cuts) and spark global retaliation. On the other hand, some commentators have posited that a second Trump Administration could still take on traditional Republican characteristics, emphasising tax cuts and deregulation. Similar to a Biden victory, the outcome of Congressional elections may constrain his policy options.

In an increasingly divisive political environment, some have claimed that 'establishment' concerns over a Trump presidency could prompt the Fed to take a more proactive role in supporting the economy in 2024. Similarly, Chris Patten, the last Governor of Hong Kong, recently claimed a new Trump presidency would put "the fate of liberal democracy in the hands of a demagogue who undermines its most basic principles."

"From Beijing's perspective, the result of Taiwan's election is acceptable."

The Observatory Group
January 2024

Taiwan elections: In January, the year of elections kicked off in Taiwan. The ruling pro-independence (from China) Democratic Progressive Party (DPP) was re-elected. According to the Observatory Group, "from Beijing's perspective, the result of Taiwan's election is acceptable". No party won a majority, and DPP won with a much narrower margin than in 2020. There is also now scope for the pro-China parties to control the legislative agenda. This was a positive development for regional calm, and increases the likelihood that "the geo-political tensions across the Taiwan Strait will likely be kept under control"…for now.

Indian elections: Current Indian prime minister Narendra Modi is widely expected to secure a third term in the 2024 elections. Supporters of Modi claim he has lifted India to a global power, while others question his aggregation of power in the now second most populous country in the world, including India's strategic alignment with less democratic nations.

The Ukrainian army is bogged down in a war of attrition with a far larger enemy, and the US and Europe are losing interest.

Russia-Ukraine: The Ukrainian army is bogged down in a war of attrition with a far larger enemy, and the US and Europe are losing interest. Earlier expectations by some that a re-equipped Ukrainian army could repel Russia, trigger a coup in the Kremlin, and deliver a swift end to the war have not eventuated. Instead, the war is ongoing, and the US and Europe are losing interest, with the risk of a shift to a more insular US leadership potentially impacting meaningful developments through 2024 and 2025.

Israel's war in Gaza: Israel's efforts in the Gaza strip to destroy Hamas continue, and a shift in US leadership could impact the 'moderating' influence the US has been imparting, and increase the risk of escalation, most likely with Iran (and Hezbollah). This obviously bleeds over into another geo-political event, namely the aggression of the Houthis in the Red Sea, where the US has been willing to make efforts to free the significant trade route. Risks centre around Israel taking unilateral action against Iran, while the latter's ability to control the Houthis could also escalate developments.

For now, and according to geo-political analysts at the Observatory Group, "while every theatre in the Middle East is ripe for escalation, several factors argue against Iran wanting to escalate the conflict with the US and Israel further than it already has". On one front, the 'public' does not share the regime's ideological goals. On another (equally but separately worrying front), Iran's significant progress to produce weapons grade uranium means Iran would not want to risk US or Israel strikes on its nuclear infrastructure. Adding to the political angle, discussions are ongoing in terms of succession for 84-year-old Supreme Leader of Iran, Ali Khamenei, with little unity among the elites in regard to who should take over.

Increasingly regular attacks across December and January by Houthis militants in the Red Sea – where 30% of world's container ships pass (including oil and gas) – have raised concerns of a sharp slowing in global growth or an inflation shock that delays interest rate cuts.

Red sea and shipping lanes: Increasingly regular attacks across December and January by Houthis militants in the Red Sea – where 30% of world container ships pass, including oil and gas – have raised concerns of a sharp slowing in global growth or an inflation shock that delays interest rate cuts. A US-led naval force is, for now, committed to secure the safety of super-tankers. However, as reported by Bloomberg, most vessels are now travelling around Africa, adding two weeks to logistic costs.

While the risk of recession is reduced, the risk of inflation has risen. For now, estimates from UBS suggest that while some shipping costs have risen over 100%, the impact on inflation is "very small". Still, resolution significantly rests on de-escalation and the ongoing willingness of the US to play a role in the region.

Investment implications for 2024

Each investment cycle almost always has something unique to bring that challenges investors. At its extreme, it's always "different this time". The current investment environment has seen the uniqueness of "excess cash savings", as well as supply-chain driven "disinflation". Growth is slowing, but proving resilient, at the same time that inflation is falling fast enough to discourage central banks from overtightening. That's a relatively constructive market backdrop for both fixed income (where we are overweight) and equities (where we are neutral).

"Our central scenario of mediocre, but positive, returns should mean investors don't chase rallies too hard and be prepared to buy the dip."

MST Marquee
January 2024

It may be a year to buy the dips, but not chase the equity rallies. Equity markets have been quick to price positive macro developments. After a mild correction in early 2024, equities have arguably been focused on the prospect of lower rates and resilient growth. However, with equities having defied expectations in 2023 with double-digit returns, it makes a repeat performance in 2024 a relatively high hurdle. According to MST Marquee, this could be a year of "mediocre, but positive, returns" for equities.

Staying the course in fixed income may be key. The shift in tone from central banks has already led to a sharp rally in yields into early 2024. As with equities, significant capital gains may be hard to harvest, unless the "hard landing" scenario for the global economy comes back into frame. Yet, ignoring the defensive characteristics that fixed income can provide portfolios could be a mistake in 2024. Similarly, with "a higher resting pulse for inflation" (in the tomes of KKR) limiting the prospect of zero-policy rates returning, the ongoing yield from fixed income is likely to remain the opportunity.

As the turning point to a new phase emerges, we expect market disruption and volatility to persist. This suggests a focus on quality and tactical opportunism may prove more rewarding than traditional asset class positioning.

Tactical positioning within asset classes may outperform. Volatility is a companion we may just need to befriend. As we wrote in our 2024 Outlook, "as the turning point to a new phase evolves, we expect market disruption and volatility to persist". This suggests that a focus on quality and tactical opportunism may prove more rewarding than traditional asset class positioning. Within fixed income, this might look like subordinated tier 2 major bank paper. Within equities, it might look like under-owned sectors or small caps. Within alternatives, it might look like distressed real estate or hedge funds that can capture dispersion across assets and regions.

What's driving our views

Tactical asset allocations (% weights)

Cash	-2
Total fixed income	2
Short maturity	-2
Government bonds	1
Investment grade credit	2
High yield credit	1
Total equities	0
Domestic	1
United States	0
Europe (ex-UK)	-1
United Kingdom	0
Emerging markets	0

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

Adjusting our tactical tilts to reflect a shifting environment

December and January provided investors with further evidence of moderating (but still resilient) US economic activity and disinflation. Easing financial conditions have raised further hope that the US economy might avoid a hard landing.

We continue to believe that we have reached peak interest rates, though any potential rate cuts will likely occur later than markets are currently pricing. To reflect this shifting outlook and better position portfolios for the year ahead, we have adjusted our tilts within fixed income towards high yield credit and neutralised our US equity underweight.

Can policymakers stick the landing—After a fast and steep tightening cycle, central bankers now need to calibrate policy to continue lowering inflation without triggering a recession. While consumer sentiment is still healthy, there remain political and geo-political pressures, financial markets are hyperactive, and the secular inflation outlook is more volatile.

Politics takes centre stage in 2024—After the geo-political shocks of the past two years, politics will be a key market driver this year. More than 64 elections will take place in 2024, headlined by the US in November.

Diverging cycles—The US economy is resilient, while Europe flirts with technical recession, and China faces key cyclical and structural challenges. How these macro dynamics play out will be a key driver for markets.

Fortune favours the flexible—With ongoing volatility and uncertainty, we believe it will pay to be diversified, nimble, and flexible over the year ahead. Investors will benefit from prudently managing liquidity, investing with high quality active managers, and flexibly managing portfolios.

Structural thematics

Positioning for multi-polarity—As the world order continues to transition towards multi-polarity, we expect more volatility and more geo-political shocks, but also more growth and opportunities for astute investors.

A challenging energy transition—Amid rising political and geo-political tensions, the world faces an increasingly challenging trade-off between net-zero commitments, cost, and energy security.

Innovative upside—Artificial intelligence presents a key challenge and opportunity, while advances in pharmaceuticals show that human ingenuity remains potent and is a key constructive force for the long term.

Higher rates increase investors' options—The resetting of interest rates at a higher level increases forward-looking returns across all asset classes, and gives investors more options to construct robust, diversified portfolios.

	What we like	What we don't like
Equities	▪ Broader S&P 500 exposure over mega-cap (long equally weighted S&P 500 over market cap-weighted S&P 500). ▪ Value and quality-tilted active strategies. ▪ Actively managed small and mid-cap equities.	▪ Companies with shorter-term debt maturities at risk of re-pricing into a higher rate environment. ▪ Stocks trading at historically tight dividend yields to the risk-free rate.
Fixed income	▪ Actively managed funds investing in higher quality credit. ▪ Fixed rate three- to five-year senior and tier 2 bank credit. ▪ Shorter maturity high quality bonds (two to five years). ▪ Higher quality issuers and actively managed funds within high yield credit.	▪ Longer-maturity bonds, which are vulnerable to rising inflation and term premia risk. ▪ Lower quality credit vulnerable to higher cost of funds.
Alternatives	▪ Credit-oriented and macro hedge fund strategies. ▪ Senior private debt (strategies excluding real estate). ▪ Real assets with inflation linkages and/or exposure to secular themes (e.g., multi-polarity and energy transition).	▪ Lower grade real estate assets (particularly office). ▪ Assets that have not adjusted to a higher rate environment. ▪ Assets and industries with no transition plan.

Economic and asset class outlook

Economic outlook

Global economy

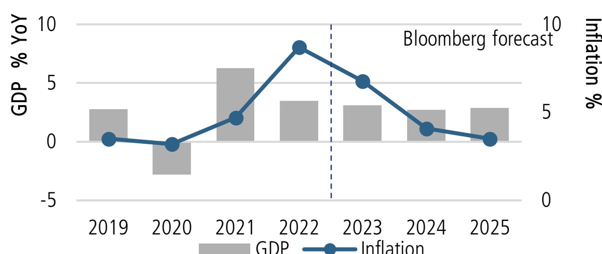
After early signs that monetary policy may be starting to weigh more heavily on global activity in early Q4 2023, latest data into year-end has tended to add weight to the notion of a relatively 'softish' landing for the world economy in 2024. While manufacturing remains below trend, economic activity in the services sector is proving robust. Elevated net wealth, high levels of saving, and cyclical support from solid jobs markets (where unemployment has only risen moderately) continue to offset higher interest rates and tighter credit conditions when it comes to consumer spending, which has surprised positively.

We believe that we are entering a new phase for the global economy, where interest rates have peaked, but are unlikely to fall to extremely low pre-pandemic levels. Recent signs that core inflation rates are annualising nearer central bank targets have led several central banks, including the US and Europe, to become open to the possibility of rate cuts before mid-year. However, we expect the bulk of the policy easing to occur in H2 2024, in part due to the resilience of the growth backdrop. This has created a more positive backdrop for financial markets and eased residual concerns of a hard economic landing globally. However, some still expect a US recession to eventuate.

Politics (as well as geo-politics) are also likely to take centre stage in 2024. Indeed, politics has the potential to drive geo-politics, with elections in 2024 impacting more than half of the world's population. During this year, polls will be held in the US, India, Indonesia, the UK, and Europe (Parliament). Focus will likely be on the US, where success in the recent Iowa and New Hampshire caucuses suggests former President Trump will secure the Republican nomination soon. During the year, markets may turn their attention to the implication of a possible Trump victory on US-China relations, US support for Ukraine (and treaties, like NATO), US tax and fiscal policy and the implications for the Red Sea traffic and inflation.

Consensus expects global growth to ease in 2024 to a pace a little below long-term averages, but above that aligned with a sharp slowdown. The International Monetary Fund (IMF) recently upgraded their 2024 outlook (lifting growth from 2.9% to 3.1%) noting that a 'soft landing' was in sight. UBS and Société Générale (SG) still anticipate a mild US recession in 2024, together with weak growth in Europe and the UK.

Global GDP growth and inflation



Source: Bloomberg as of 31 January 2024.

Australia

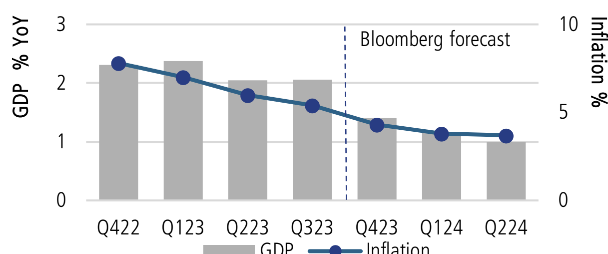
Australia's economy appears to have been expanding, albeit at a sub-trend pace during H2 2023. However, much of this growth is sourced from strong population growth and elevated inflation. Consumer sentiment and housing activity have been weaker, and may slow further in early 2024 following the monetary policy hike in November. However, like elsewhere, the recently better inflation performance and resilient jobs market suggest the peak headwind from policy tightening is approaching. While growth is likely to be slower ahead, recession appears an unlikely outlook for 2024. This is due to a stabilising China (where more stimulus is being delivered) and a strong fiscal backdrop that is likely to be supportive, ahead of already planned personal tax cuts from mid-2024.

Growth slowed further to just 0.2% in Q3 after 0.4% in Q2, although this saw the annual pace edge slightly higher to 2.1% from 2.0% (still below the current population growth rate). Consumer spending and income were weak, with growth supported largely by government and business capex. Data for Q4 suggest a similarly modest pace of growth, reflecting a slowing consumer but strong capex (infrastructure) backdrop. While retail sales collapsed 2.7% in December, signalling weakening demand, the jobs market slowing is relatively glacially (with unemployment still just below 4%). In contrast, housing activity has begun to weaken more clearly, with Q3 dwelling starts falling to their lowest level in a decade.

Inflation eased to 4.1% in Q4 from 5.4% in Q3, below the Reserve Bank of Australia's (RBA) 4.5% year-end forecast. Core inflation slowed slightly less to 4.2% from 5.2%. Importantly, the quarterly pace of core inflation slowed to 0.8% from its unexpected acceleration to 1.2% in Q3. Following the hike to 4.35% in November (on the back of Q3's stronger inflation data), the RBA signalled a weaker tightening bias at its latest meetings. Leading indicators point to further easing of price pressures, with the Q3 wages broadly in line with RBA forecasts. UBS expects an initial rate cut in August 2024 (was November), while CBA sees the first cut in September 2024.

After likely growth of 2.0% in 2023, UBS expects Australia to avoid a recession, with growth of 1.5% in 2024, ahead of a recovery to 2.1% in 2025. CBA sees slightly slower growth of 1.2% for 2024, with stronger growth of 2.5% in 2025.

Australian GDP growth and inflation



Source: Bloomberg as of 31 January 2024.

Economic outlook

United States

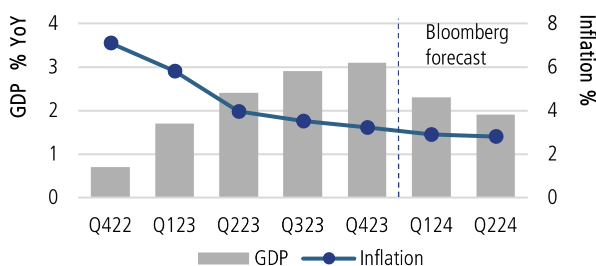
Growth in the US economy remains solid, but has continued to trend slower in late 2023. Nonetheless, early 2024 data has retained a relatively resilient tone across consumer spending and the jobs market, while housing activity appears to be stabilising as borrowing rates fall. This has, again, increased the focus on the US economy achieving only a mild downturn in 2024. Further signs of moderating growth, with continued falls in inflation, should increase confidence that policy tightening has peaked. But the resilient growth backdrop suggests little urgency for a pivot toward rate cuts before mid-year unless growth slows sharply. Elsewhere, with a US government shutdown averted once again, focus on the US Presidential election is increasing after former President Trump's victory in the early Republican caucuses.

Growth in Q4 rose a stronger-than-expected 0.8% (3.3% annualised), slowing moderately from Q3's sharp acceleration to 1.2% (4.9%). Recent data has proved more resilient than during early Q4. The composite Purchasing Managers Index (PMI) jumped to 52.3 (from 50.9) in January, its strongest level since mid-2023. In December, retail sales surprised positively, rising 0.6%, while non-farm payrolls lifted to 216,000 from 173,000 and unemployment claims remained very low. Housing starts have trended higher through Q4, up almost 8%, and mortgage applications have also risen.

Inflation has continued to moderate through Q4, albeit at a slower pace. While headline inflation edged higher to 3.4% in December (from 3.1%), core moderated to 3.9%. In Q4, the Fed's preferred inflation measure annualised below its inflation target of 2%. At its December meeting, the Fed did little to dampen aggressive rate cut expectations, removing the previous final rate hike 'dot' and signalling (arguably more modest) rate cuts by end-2024. The subsequent sharp rally in market rates has been somewhat reversed on stronger data and Fed minutes that signalled data dependence and determination to restore price stability. Both UBS and SG expect Fed cuts to start before mid-year.

After a 2.5% pace in 2023, UBS expects a mid-year recession and growth of 1.5% in 2024, before edging higher to 1.6% in 2025. SG is forecasting a sharper slowdown to 0.9% in 2024, but a sharper recovery in 2025 to 2.7%.

US GDP growth and inflation



Source: Bloomberg as of 31 January 2024.

Europe

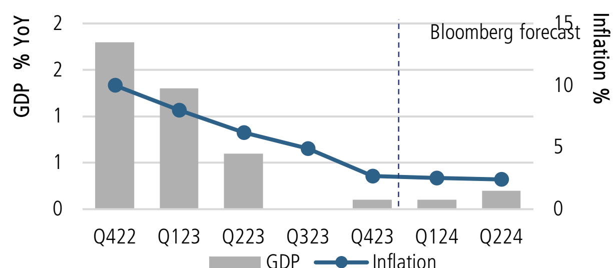
European activity has remained weak in early 2024, particularly in Germany, with recent data suggesting recessionary conditions in H2 2023. The growth outlook for 2024 remains under pressure, according to Longview Economics. This is due to ongoing tight monetary policy, high inventory levels on the back of globally weak goods orders, some signs of labour market softness, and the demise of households' spare cash. Twin wars in the region, Red Sea supply impacts, and tighter German fiscal policy have added to the negative European growth outlook. Still, the recent faster-than-expected fall in inflation (and weaker-than-anticipated growth) are raising the prospect of earlier-than-forecast rate cuts. This is fostering an improvement in business and consumer confidence.

In Q4, Europe's growth was 'flat', narrowly missing a technical recession after Q3's -0.1% print. The annual pace remained unchanged, also 'flat' and down from 0.6% in mid-2023. Risks of a further contraction in early 2024 have risen with recent data on retail sales and industrial production during Q4 weak. More positively, despite the PMI relapsing below the key 50-mark during Q4, January's print edged higher to 47.9 from 47.6. The unemployment rate edged down to a new record low of 6.4% (signalling a still tight jobs market) and consumer sentiment improved to a 10-month high.

Inflation has moderated sharply in recent months. While December rebounded to 2.9% (from 2.4%), still around half its mid-2023 pace, core inflation improved to 3.4% from 3.6%, its lowest since March 2022. As such, prior commentary from the European Central Bank (ECB) that it is premature to expect rate cuts has given way to signals from President Lagarde that cuts may begin in the summer (though not as early as the markets' March pricing). This message was echoed in the latest December minutes, according to CBA. UBS and CBA expect a rate cutting cycle to start mid-year, while SG has recently brought forward its expected start for rate cuts from December to October.

After relatively weak growth of 0.5% in 2023, UBS expects a modest recovery in H2 2024. It expects year-average growth of 0.6% for 2024 (albeit with some downside risks), and 1.2% in 2025. SG expects slightly stronger growth of 0.8% in 2024, while CBA sees Europe in ongoing recession, with growth averaging just 0.2% in 2024.

European GDP growth and inflation



Source: Bloomberg as of 31 January 2024.

Economic outlook

United Kingdom

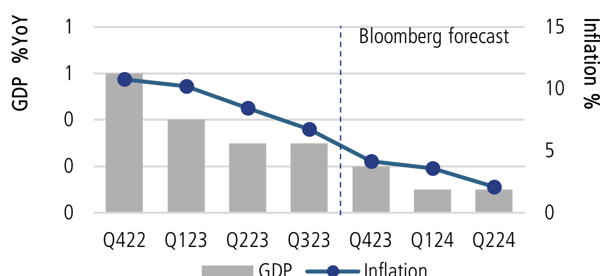
The UK appears to have defied expectations for a sharp contraction in growth in 2023, helped by a resilient consumer, solid capex, and a relatively tight jobs market. However, the risk of a shallow recession in H2 2023 persists, ahead of ongoing 'flat' growth in early 2024, reflecting "headwinds from tighter financial conditions, in particular higher mortgage payments, and external sector weakness", according to UBS. Yet, with inflation continuing to moderate, and households further supported by likely H2 rate cuts, a tepid recovery is expected through the second half of 2024.

Growth in Q3 was revised from an initial 0.0% to a fall of 0.1%, while Q2 was cut from 0.2% to flat. Reflecting this, the annual pace of growth was just 0.3% in Q3, compared with 2.1% a year earlier. Monthly data, despite rising in November, point to another flat quarter for Q4 2023, ahead of soft but potentially positive growth in early 2024. Similarly, the PMI lifted in January to 52.5 from 52.1 (its strongest level since mid-last year). Retail sales fell sharply in December, with a 3.2% fall reversing all the 1.4% gain in November. The jobs market remains tight, with unemployment little changed at a relatively low 4.2% (since June). However, positively for the inflation outlook, wages growth continued to slow in November to 6.5% (from 8.5% mid-year).

After a problematic first half of the year, inflation in the UK has trended significantly lower during H2 2023. While December inflation proved a little above expected (on stronger services inflation), the slight increase to 4.0% compares to its peak of 10.4% in February. Core inflation was unchanged at 5.1%, down from 7.1% in May. The Bank of England (BoE) kept policy unchanged at 5.25% at its mid-December meeting, noting "it was too early to conclude that services price inflation and pay growth were on a firmly downward path". While UBS views the BoE as pushing back on market pricing for near-term rate cuts, it expects the first cut in May, similar to SG, while CBA sees a later start in September.

After likely growth of 0.6% for 2023, UBS forecasts similar growth for 2024, ahead of a modest recovery to 1.5% in 2025. CBA expects a recession in 2024, with activity growth of just -0.2%, recovering to 0.7% in 2025.

UK GDP growth and inflation



Source: Bloomberg as of 31 January 2024.

Japan

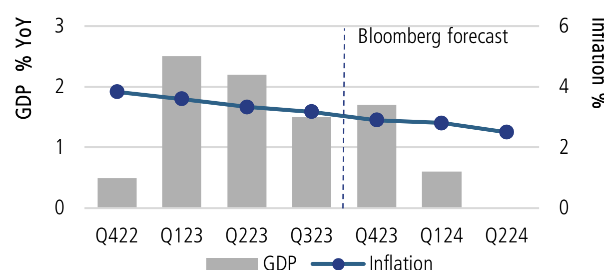
Japan's economy expanded more strongly than expected in H1 2023. However, recent data have been consistent with some 'payback' in H2, leaving Japan on a likely modest expansion path through 2024. Business conditions appear relatively robust, albeit consumer trends are weaker, as wage growth fails to keep pace with price increases. This presents some downside risks to early 2024 growth. Recent natural disasters may also impact tourism in Japan. Inflation, while steady, appears likely to slow over coming months, and should support activity, while minimising urgency for higher policy rates.

Q3 growth contracted by 0.7% (from +0.9% in Q2), easing the annual pace of growth to 1.5% in Q3 (from 2.2%). This was a larger retracement from Q2's solid result than markets were expecting. Weakness was noted in private domestic demand and investment. Japan's composite PMI edged higher to 51.1 in January, from 50.0 in December, still only modestly above the break-even rate. Positively, Q4 business sentiment rose to its highest in six years, led by large manufacturers. Retail sales also rebounded 1.0% in November, after two monthly falls. The jobs market remains tight, with unemployment ticking back down to 2.5% in November.

After having been remarkably stable at around 3.3% for much of 2023, inflation has eased across November and December to 2.6%, its lowest since mid-2022. Average cash earnings growth has also slowed sharply in recent months to just 0.2% in November (likely pressuring consumption ahead). After making another tweak to its yield curve control policy in October to now treat its 1% upper limit for the 10-year yield as a reference rather than a hard constraint, the Bank of Japan (BoJ) left policy little changed at its December and January meetings. CBA expects the BoJ to maintain a negative cash rate this year, while UBS expects gradual policy normalisation, including an end to yield curve control and a positive 0.25% cash rate by the end of 2024. Wages growth is likely to be the key determinant, where UBS expects acceleration in March.

After strong growth of around 2.0% in 2023, UBS expects growth to retrace to just 0.6% in 2024, before steadying at around a 1.0% pace in 2025. SG forecasts a similar 0.7% pace for 2024, but strong growth of 1.4% for 2025.

Japanese GDP growth and inflation



Source: Bloomberg as of 31 January 2024.

Economic outlook

China

Confidence surrounding a sustainable recovery in China's economy has remained somewhat elusive in early 2024. After recovering solidly early in H2 2023, sequential momentum slowed into year-end, albeit the official 5% growth target for 2023 was achieved. Activity outside the property sector appears to be strengthening in early January. Yet, property activities continue to weaken and challenge the outlook. As UBS recently noted, China's key growth drivers over recent decades, namely property, infrastructure, and exports, are all facing headwinds. New structural growth engines (which include consumption, upgrading manufacturing and data and AI) "will take some time" to support growth.

China's annual output rose to 5.2% in Q4, from 4.9%, in line with expectations and slightly above the 5.0% government growth target. Despite this, sequential growth disappointed, slowing in Q4 to about 4% from Q3's 6%. As Longview Economics notes, "the economy remains under significant cyclical (and structural) pressure, with the housing downturn weighing upon growth." December month data suggest that property activities are yet to bottom, with sales and starts declining further from the November level. Retail sales also decelerated. More positively, both manufacturing and infrastructure capex growth picked up, as did export volumes.

China concluded its much-awaited annual Central Economic Work Conference (CEWC) in mid-December. As usual, key growth and policy targets were not announced at CEWC but are set to be released at the National People's Congress meeting next March. However, as SG notes, "given weak data recently…policymakers vowed to be more pro-growth at the CEWC". In late January, the government announced a further 0.5% cut to the reserve requirement, as well as other measures to support the property and equity market.

After 5.2% in 2023, UBS expects China's 2024 and 2025 growth to slow to 4.6% (revised up from 4.4%). SG expects a similar slowdown to 4.5% in 2024, while CBA expects stronger growth of 4.9% for 2024 and 5.1% in 2025.

Emerging markets

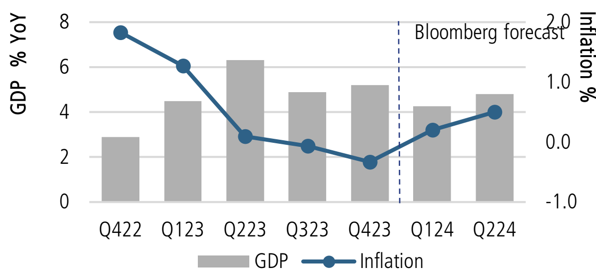
Emerging market growth is now expected to decelerate by about 0.5% (including and excluding China) through 2024, albeit mostly through H1 2024. In contrast, H2 2024 should embody modest recoveries in Latin American and emerging European growth. Asia is expected to strengthen into mid-year, helped by ongoing disinflation that paves the way for some renewed central bank easing in H1 2024. However, China's mixed growth outlook and potential US dollar strength on geo-political and political concern could weigh on the emerging market export and currency outlook.

According to UBS, growth in Southeast Asia will strengthen moderately in 2024, from 4.2% to 4.6%, albeit growth is seen below trend for all economies except Thailand. This recovery will be supported by a likely recovery in the tech export cycle that supports activity in Malaysia, Singapore, and Vietnam. North Asian economies, namely Korea and Taiwan, which are more linked to the tech export cycle, should benefit more in 2024. India appears to have lost some growth momentum during Q4 2023, that could linger into early 2024. While high frequency data remain strong in Q4 (two-wheeler sales, car sales and services such as airfares), recent weakness has reflected weaker activity in industrial activity (steel and cement). India goes to the polls during Q2 and the upcoming budget in February is expected to remain on a fiscal consolidation path. A stabilising consumer in 2024 (helped by rate cuts mid-year), together with stronger capex, should see India remain one of the fastest growing economies.

For Latin America, growth is expected to slow in 2024. For Brazil, UBS sees growth halving from around 3% to 1.4%. Monthly data steadied in November after a weak October, with a further modest gain in December expected, albeit overall activity remains relatively sluggish.

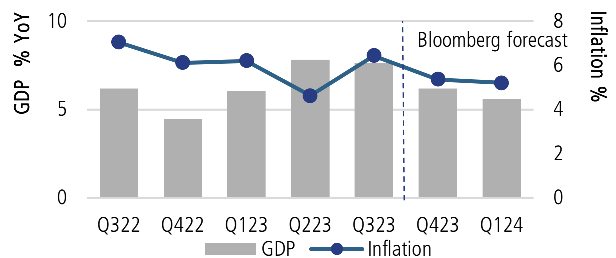
After an expected 4.5% in 2023, UBS expects a moderate slowing to 4.0% in 2024 before a modest pick-up to 4.3% in 2025. SG holds a similar view, with growth slowing to 3.9% for 2024.

Chinese GDP growth and inflation



Source: Bloomberg as of 31 January 2024

India GDP growth and inflation



Source: Bloomberg as of 31 January 2024.

Asset class outlook

Short maturity and government bonds

Position: Underweight short maturity, overweight government bonds

Key points

- We recommend maintaining a diversified portfolio of fixed and floating rate bonds. The sharp fall in the five-year swap rate in the last two months of 2023 (from 4.75% to 3.80%) means the three-month Bank Bill Swap Rate (BBSW) is now 55 basis points (bps) above the swap rate. With floating rate notes pricing off the BBSW, this makes them look more attractive than fixed rate bonds, and should attract interest from investors.
- As central banks provide a clearer outlook on rates, we expect the government bond curve to steepen.

Short maturity— Markets will likely remain very focused on inflation and economic data in 2024 to determine when rate cuts will start. Decade-high interest rates have helped slow inflation, while stronger-than-expected economic data, particularly employment, points to a relatively soft landing. This has created some uncertainty about when the easing cycle will start. The timing and level of easing in 2024 depends on progressive data prints. The higher January non-farm payroll and less dovish tones from the Fed have removed the momentum of the bond market over the past two months and reduced the likelihood of an early rate cut in March. Continued economic resilience, sticky services inflation, and job data will likely keep volatility elevated in the near term.

While our tactical asset allocation to short-term maturity is underweight, we recommend adding fixed-rate bonds to complement existing floating rate positions. Global central banks are likely to start easing from mid to late 2024, so we are recommending adding fixed-rate exposure now. We see value in the five to seven-year part of the curve, as well as the longer end, depending on the portfolio's maturity profile.

Government bonds—Global rates rallied significantly at the end of 2023 as inflation prints came in lower and more rapidly than expected. Dovish statements from Powell post the November Fed meeting added fuel to the positive momentum. Post the November Fed meeting, the 10-year US Treasury rallied 120bps to 3.80% at the end of December. However, it is now back around 4.03%. Markets are pricing an aggressive easing path for the Fed this year, with around 160bps of cuts. However, the latest CPI print, labour data, and Fed speak have cooled rate cut hopes. It is possible the bond market may have over-extended the rally and be over-bought. The degree of further improvement in inflation will subsequently dictate the timing and scale of cuts in 2024 and beyond.

We see clear signs that inflationary pressures are cooling and expect economic growth to moderate in coming quarters, with a relatively soft-landing making a recession unlikely. We believe government bond yields at the front end of the curve will be lower over the next six to 12 months. This is in line with central banks easing at a moderate pace. We remain overweight on an outright yield basis, expecting less capital upside at the longer end as the curve steepens. We have reduced our overweight to this segment of the market.

Investment grade and high yield credit

Position: Overweight investment grade, overweight high yield credit

Key points

- We prefer investment grade bonds as inflation cools and downside risks to growth moderate.
- High yield credit quality has improved and demand for outright yields has risen, driving spreads lower.

Investment grade credit—Investment grade credit spreads are now fully priced for a soft landing, with limited upside from here. Despite the volatility in bond markets, investors have continued to be attracted to the outright yields, driving spreads lower. With good conditions for issuers, January has been a record month for issuance both in the US and Europe. In the first week of the year alone, there was USD 87 billion and EUR 65 billion of issuance respectively. Corporate credit spreads are at historically low levels, but fundamental economic data remains robust. This implies that the economy is likely to experience a soft landing, and spreads should remain tight. As global central banks start to ease later in the year, spreads are likely to widen. But we expect that the total return will remain positive as bond yields fall. An exposure to high-quality bonds should provide a degree of protection to portfolios if the economy slows, as credit spread widening is usually offset by falling government bond yields.

Domestically, issuance has also been high and dominated by financials. Attention has been centred around the ANZ 10NC5 subordinated tier 2, which was issued 10bps tighter than initial price talk at asset swap +195bps. A multi-tranche three and five-year senior unsecured transaction was also issued by Westpac. The Australian banks have now issued more than AUD 20 billion of debt across the US dollar and Australian dollar markets in the first weeks of the year.

High yield credit—Despite global economic risks, high-yield investments continue to attract long-term investors due to the potential for total returns. The end of the rate-hiking cycle, coupled with robust consumer spending and labour market strength, has tightened credit spreads. While concerns exist around the sustainability of high-yield spreads at current levels, there is a common belief that the US economy will have a soft landing. Corporate earnings improved in the latter part of 2023. Irrespective of the sector's sensitivity to interest rates, leverage, and cyclicality, the overall credit quality of the high-yield market has improved, with the average rating for high-yield US issuers now BB. Encouragingly, many high-yield issuers have strengthened their financial positions, maintaining low leverage and manageable interest coverage. With limited near-term maturities and a higher credit quality profile, default rates are expected to remain stable in the near to medium term. While volatility may persist, higher-rated bonds and loans are favoured, given their potentially attractive total returns. Although they have tightened recently, yields on BB-rated bonds and loans still appear compelling. The loan asset class stands out for its higher-than-average coupons, contributing to potentially above-average total returns.

Asset class outlook

Domestic equities

Position: Overweight

Key points

- Domestic equities rose 90bps in January, consolidating the 7.3% gain seen in December.
- The S&P/ASX 200 index is now towards the top of its 6,400–7,600 trading range of the past three years, a level it has failed to breach on five previous occasions.
- Pessimism around the Chinese economic recovery weighed heavily on the materials sector, which fell 5% for the month. Despite this, iron ore prices remained around USD 130 per tonne (p/t), suggesting a robust February reporting season for the iron ore majors.

Barrenjoey strategists have set an S&P/ASX 200 target for 2024 of 7,290 (-5% from current levels), with downside risk if bond yields rise. However, it is worth noting that Barrenjoey's outlook is "not so bearish that we should position completely defensively".

Barrenjoey forecasts 4.5% potential upside to earnings from higher commodity prices and supply chain easing, with offsets from domestic cost pressures and a slowing credit impulse. Notwithstanding its slightly positive earnings view, it thinks that market multiples are somewhat stretched and vulnerable to compression, especially heading into a year when investors need compensation for inflation, political and geo-political risks. MST agrees and views the S&P/ASX 200 as moderately expensive based on simple price/earnings (P/E) ratios. Given the combination of rising stock prices and falling earnings per share (EPS), the index now trades on 16.2x P/E. The long-term average has been 14.5x. While P/E ratios have been good guides to longer-term equity market returns, they have been poor at providing an indication of shorter-term returns like those over the coming 12 months.

We believe there are several factors that may see Australia outperform in 2024. These include RBA rate cuts, proposed stage 3 tax cuts (which should support consumer spending and domestic activity), a relatively strong growth trajectory versus other advanced economies, and a resilient commodities sector, where iron ore prices are around their highest levels since June 2022. The market is now priced for almost two rate cuts by the end of the year versus none two months ago. As we get closer to the timing of the first rate cut (the market is priced for the first cut by September), share prices are likely to start more confidently 'looking through' the cycle. Historically, sectors across the domestic consumer/housing complex have seen share prices bottom and turn upwards approximately three months before the RBA's first rate cut.

Investors are already positioned for an almost 10% deterioration in major bank EPS, suggesting that economic conditions and/or competition would need to weaken materially from here to see sentiment worsen.

International equities

Position: Underweight Europe. Neutral the US, UK and emerging markets

Key points

- The MSCI World ex-Australia Index returned 6% in Australian dollar terms in January. In US dollar terms, the return was more muted, at 2.3%.
- Markets consolidated their end-of-year gains in January after a small pull-back at the beginning of the year. Taiwan Semiconductor's strong quarterly result reinvigorated optimism in the tech sector and saw the NASDAQ climb 7% for the month in Australian dollar terms, and 3% in US dollar terms.
- Hong Kong and Chinese equities were very weak, falling for 13 of the first 15 days before rebounding.

In late January, Hong Kong and Chinese equities were buoyed by several developments. Firstly, there were reports that policymakers were preparing a USD 278 billion package to buy domestic stocks. They are also aiming to raise at least CNY 300 billion of local funds to invest through state-owned China Securities Finance Corp, a unit of China's sovereign fund. Secondly, the *New York Times* reported that both Jack Ma and Joseph Tsai had collectively bought around USD 200 million of Alibaba stock, potentially suggesting that the consistent political and regulatory pressure on the tech sector of the past several years was drawing to a close. On 24 January, China said it will cut the reserve requirement ratio (RRR) for banks within two weeks and hinted at more support measures to come, as further steps were taken to shore up the economy and halt a USD 6 trillion stock market rout. The RRR will be lowered by 0.5 percentage points on 5 February to provide CNY 1 trillion (USD 139 billion) in long-term liquidity to the market, according to Governor of the People's Bank of China, Pan Gongsheng. The 50bps is notable, given historically RRR moves have been in 25bps increments.

Financial conditions have eased much more than most investors anticipated, and the market now expects approximately five rate cuts over the next 12 months, versus the three it expected back in October 2023. An increase in net Fed liquidity, an easing in credit standards, and some better consumer and housing data bolstered equity sentiment. The US stock market continues to command a quality premium over other markets, given its sector composition and cash rich mega-cap stocks. If economic growth momentum continues further into 2024, it is likely that the US will underperform, given the wide valuation gap of the US versus other regions, and its rich investor positioning. However, if the expected 'Goldilocks' environment does not materialise, a risk some believe is under-appreciated, the US will likely outperform in an otherwise disappointing global equity performance in 2024, given its defensive characteristics.

The MSCI World ex-Australia index now trades at around18x 12-month forward P/E, consistent with prior peaks, excluding the 2020-2022 post-COVID period.

Asset class outlook

Currencies

Key points

- The US dollar had a volatile two months, with positive risk sentiment and aggressive pricing of Fed rate cuts prompting weakness in December. This reversed as markets pared back these bets in January.
- The Australian dollar was a key outperformer in December, supported by strong iron ore prices and RBA hawkishness. As the US dollar strengthened in January, the Australian dollar gave back some of these gains.

Increasing global risk appetite and aggressive market pricing for Fed rate cuts supported further weakness in the US dollar in December. However, the greenback started finding support in January as markets wound back their dovish bets. Investors are increasingly pricing in a 'soft landing' for the US economy. However, there are significant political risk events this year and markets will likely remain overly priced for rate cuts this year. These factors may provide some support to the US dollar in the near term. As we get closer to the US Presidential elections, political factors are likely to be a key driver for the US dollar this year. Structural factors, including a deteriorating US budget deficit, point to downside pressures longer-term, but these will not be in markets' minds for some time.

The Australian dollar was a key outperformer in December, briefly touching USD 0.68. The currency was supported by risk-on appetite, strong iron ore prices, and expectations for the RBA to lag the global easing cycle. Current levels of USD 0.66 remain in line with or at the low end of longer-term fair value estimates. The stubbornness of inflation (and potential RBA hikes) could provide some support, despite a challenging macro outlook. A significant Chinese stimulus program is a key upside risk for the Australian dollar. CBA sees the currency strengthening to USD 0.74 at the end of 2024.

The euro has lagged both the US dollar and Australian dollar since November, weighed down by moribund macro conditions. We expect the Eurozone will face macro risks going forward, which are likely to weigh on the currency. However, a possible supply shock-driven re-acceleration in inflation may force the ECB to also lag a Fed cutting cycle.

The Japanese yen finally participated in the global US dollar depreciation in December, touching JPY 141 versus the US dollar. However, it gave most of this back over the course of January and is now trading at JPY 147 versus the US dollar. There is potential upside support for the Japanese yen as Japan's domestic inflation and macro dynamics are likely to lead the BoJ to begin normalising policy this year. CBA sees the Japanese yen strengthening to JPY 137 versus the US dollar by the end of 2024.

Commodities

Key points

- Global commodities fell modestly over December and January, weighed lower by China growth concerns. Gold is trading around USD 2,000 per ounce.
- Iron ore prices were modestly weaker over the course of January but remained broadly resilient in the face of Chinese economic weakness.

Concerns over slowing global growth (particularly in China) saw broad commodity prices weaken modestly over the past two months. WTI crude oil prices are trading at around USD 74 per barrel, with weakness in December offset somewhat by rising geo-political risk premia as Houthi rebels attacked shipping in the Red Sea. Gold prices reached just under USD 2,100 per ounce in late December on US dollar weakness and declining real yields. Since then, they have retraced to just over USD 2,000 per ounce as markets pared back rate cut bets and the US dollar strengthened.

Industrial metals prices generally followed the inverse path of the US dollar, strengthening in December and weakening in January, with softer Chinese economic activity adding further pressure at the start of the year. However, the recent announcement of further monetary policy stimulus by the People's Bank of China in late January (together with policies to support the property sector) sparked a rebound in prices.

The evolution of the Chinese economy will continue to play a key role in the near-term outlook for commodities. We expect that authorities will continue to emphasise targeted and limited stimulus packages to support, but not ignite, China's growth pulse. This approach reflects China's multi-year efforts to rebalance its economy towards more sustainable consumer- and services-led growth, while addressing structural issues in its property market and debt dynamics.

Recent data suggests that the Chinese economy continues to face significant cyclical and structural challenges, which presents fundamental headwinds to commodity prices. Conversely, this may also force authorities to pursue more aggressive stimulus, which could support a cyclical rebound in commodity prices in the absence of a broader global slowdown. This backdrop is likely to lead to ongoing elevated volatility in commodity prices.

Looking beyond the cyclical horizon, longer-term themes, including climate change and geo-politics, are likely to support the commodity complex on a secular basis. It is difficult to determine how these competing cyclical and secular forces might evolve over the year ahead, and we are particularly cognisant of the risk that a cyclical downturn could outweigh the secular tailwinds in the near 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

We expect that growth and inflation will continue to slow in most developed economies this year, and we have a stronger conviction that cash rates have peaked this cycle. Central banks have signalled varying intentions to ease policy gradually over 2024, with risks to the outlook broadly balanced.

In Australia, inflation is moderating in line with peers, while consumption (boosted by population growth) has remained resilient, and the US economy continues to hold strong. We retain the view that if there is a recession it is likely to be relatively shallow /soft, and easing financial conditions are likely to support activity in the near term. To reflect the shifting macro and market outlook, we have made two changes to our positioning. Overall, we believe that fixed income will perform well relative to equities under several scenarios in the short term.

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

Our underweight cash position remains at -2, reflecting our view that rates have likely peaked, favouring fixed income over cash.

Fixed income

At an asset class level, fixed income remains our highest conviction position at +2. At a sub-asset class level, we've tilted our conviction towards high yield credit, funded by reducing our overweight position to government bonds. This tilt takes advantage of still attractive all-in yields and reflects a slight risk-on bias. We continue to hold a strong overweight to investment grade credit. If markets experience volatility, we expect fixed income (particularly government bonds and investment grade credit) to prove relatively defensive—particularly if the growth outlook deteriorates.

Alternatives

We favour infrastructure, private debt, and low-beta hedge fund exposures, while maintaining private equity exposures. We are taking a cautious approach to real estate globally.

Equities

We are neutral equities but have neutralised our US underweight and emerging market overweight. This reflects growing evidence of US economic resilience and recognises the significant cyclical and structural challenges facing emerging markets, especially China. We are overweight domestic equities due to attractive relative valuations and potential tailwinds from economic outperformance. We are underweight Europe due to its weaker macro and earnings outlook.

Active portfolio weights and active tactical asset allocation tilts

		Active tilt	Yield (%)	Balanced (%)	Growth (%)	Endowment (%)
Cash		-2	1	1	1	1
Fixed income		2	55	37	19	16
Short maturity		-2	6	4	1	1
Government bonds	V	1	33	16	8	6
Investment grade credit		2	13	13	6	6
High yield credit	Λ	1	3	4	4	3
Equities		0	24	42	60	38
Domestic		1	13	20	29	12
United States	Λ	0	6	11	16	13
Europe (ex-UK)		-1	2	3	4	3
United Kingdom		0	2	3	4	3
Emerging markets	V	0	1	5	7	7
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 for now. Our base case is that central banks will be required to ease monetary policy moderately from mid-2024. This will contribute to the positive total returns from adding duration with fixed rate relative to floating rate over time.

Government bonds

We are overweight government bonds. With expectations that central banks are at the end of their rate-hiking cycles, we remain tactically overweight government bonds. However, we have continued to trim this overweight as yields have rallied. Markets are now pricing significant rate cuts through 2024. Yields should nonetheless continue to move moderately lower as rate cuts come through and inflation falls further.

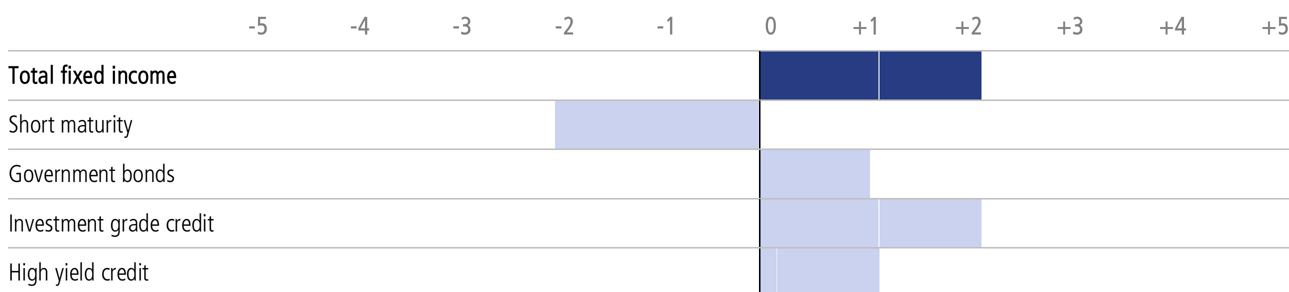
Investment grade credit

We are overweight investment grade credit. While all-in yields are at historically elevated levels, we believe investors should continue deploying into investment grade credit. Staying in high-quality bonds should protect portfolios in a growth slowdown, as credit spread widening is usually offset by falling government bond yields. Easing risks of an economic hard landing should also support returns through 2024.

High yield credit

We have moved overweight high yield credit. Although high yield credit spreads are near historically low levels, the credit quality of high-yield issuers has improved. The average rating of high-yield US issuers is now BB. Many issuers have strengthened their financial positions and are maintaining low leverage and manageable interest coverage. We believe that high interest rates make all-in yields attractive.

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



Fixed income market summary

Fixed income indices	Current	One month ago.
Australian iTraxx	68.49	69.97
Australian 3-year yield	3.70%	3.61%
Australian 10-year yield	4.11%	4.87%
Australian 3/10-year spread	40.5 bp	53.6 bp
Australian/US 10-year spread	7.8 bp	0.0 bp
US 10-year Bond	4.03%	4.89%
German 10-year Bund	2.27%	2.82%
UK 10-year Gilt	3.90%	4.56%
Markit CDX North America Investment-Grade Index	54.3 bp	81.2 bp
Markit iTraxx Europe Main Index	58.3	88.5
Markit iTraxx Europe Crossover Index	318.1	464.9
SPX Volatility Index (VIX)	13.3	19.8

Source: LGT Crestone Wealth Management, Bloomberg as of 31 January 2024. 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 S&P/ASX 200 index has traded towards the upper level of its three-year trading range. With tentative signs of 'panic' among Chinese policymakers, domestic equities could outperform this year, driven by resilient iron ore prices, as well as banks rebasing their expectations. The rising probability of rate cuts could also see share prices more confidently 'look through' the cycle.

US equities

We have neutralised our underweight to US equities. Despite concerns over headline valuations for the market-cap weighted S&P 500, P/E multiples for the equally weighted S&P 500, as well as the broader market (excluding the 'Magnificent 7') are more reasonable. Uncertainty over global growth in Q2/Q3 – or any escalation in geo-political volatility – could see the US prove more resilient than other global markets.

European (ex-UK) equities

We are underweight European (ex-UK) equities. Although the STOXX 50 has traded to 2001 highs, it is now at a significant level of long-term resistance. Furthermore, 2024 sales and EPS estimates have been downgraded by 0.3% and 1.6% respectively. 2024 EPS revisions are negative at -20% and earnings before interest and tax (EBIT) margins are forecast to be lower year-on-year. The composite PMI has fallen back into contractionary territory (47), with both the manufacturing and services components falling.

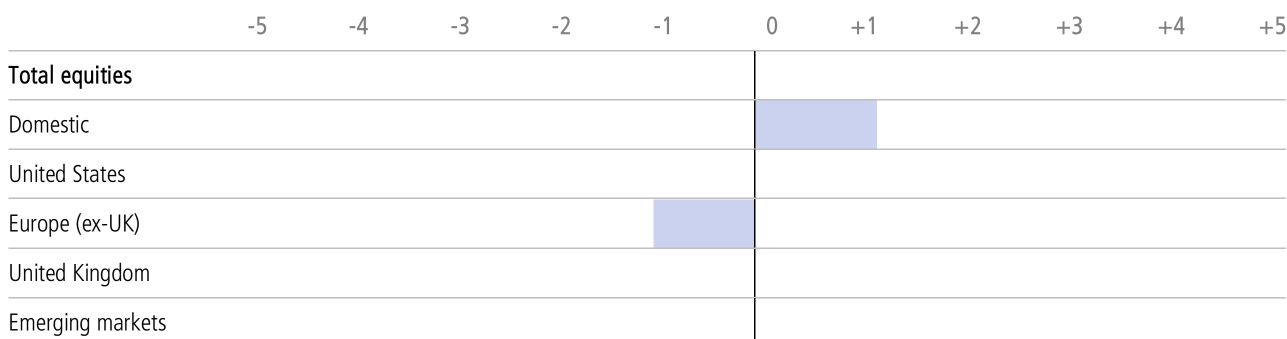
United Kingdom equities

We are neutral UK equities. We are relatively more optimistic on UK equities, given significant valuation support, favourable sector compositions and the long-standing preference for FTSE 100 (global) over the FTSE 250 (domestic) stocks. Notwithstanding this, the region lacks a catalyst to crystallise this valuation support, which is why we maintain a neutral stance.

Emerging market equities

We have reduced our exposure to emerging market equities. Although the Asian earnings cycle has likely bottomed out, this may not be followed by a V-shaped recovery, as in past cycles. Earnings growth forecasts in China are still being revised down, and the earnings revision breadth remains extremely weak, with estimates for almost three-quarters of companies still being revised down. A China policy pivot, both fiscal and monetary, remains a key swing factor.

Active equity weights (%)—We are neutral 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	7,600.2	7,683.2	1.1%	16.1	4.3%
New Zealand	S&P NZ 50	11,914.4	12,323.7	3.4%	24.5	3.3%
United States	S&P 500	4,925.0	5,271.3	7.0%	20.5	1.4%
Europe	Euro Stoxx	483.6	543.7	12.4%	12.8	3.3%
United Kingdom	FTSE 100	7,666.3	8,941.8	16.6%	11.1	4.0%
China	CSI 300	2,830.5	3,630.1	28.2%	9.6	3.4%
Japan	Nikkei 225	36,065.9	37,621.8	4.3%	20.8	1.8%
India	Sensex	71,139.9	79,502.5	11.8%	20.4	1.5%

Source: Bloomberg. Data as of 31st January 2024; 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

Higher rates and greater asset price dispersion should support the case for hedge funds. A decade of quantitative easing has suppressed volatility and dispersion across underlying securities. The rapid increase in interest rates in 2023 and the increasingly uncertain economic outlook should improve the opportunity set for hedge fund managers. In fact, historical data suggests that hedge funds perform better in environments where risk-free rates are in excess of 2%, rather than below 2%. However, investors should note that hedge fund manager dispersion continues to rise, so manager selection remains key. Across the hedge fund universe, we continue to favour credit-orientated strategies, where outright yield increases further support the investment case, and we maintain a preference for lower beta strategies.

Private markets

Private equity remains core, with secondaries looking likely to drive strong returns. With entry valuations having re-adjusted meaningfully, we recommend maintaining exposures to private equity and venture capital and building positions where underweight. We maintain a preference for new primary and secondary fund commitment structures, with venture secondaries looking particularly attractive, given the ongoing market dislocations that remain in play since 2022. However, investors should maintain discipline and partner with a portfolio company or fund manager that has sufficient data and qualitative insights to source and assess high quality opportunities.

Private debt is our favoured alternative asset class. Higher base rates and increased spreads on private debt offshore mean that risk-adjusted returns look highly attractive relative to other asset classes. Lenders can now attract senior deals with strong covenants and an equity cushion of more than 60% at unlevered double-digit yields. We prefer direct, sponsor-backed transactions versus broadly syndicated strategies, as loan terms can be negotiated directly, offering greater protection to the end investor. Investors can also further diversify through private, asset-backed securities, albeit we remain cautious on construction and land-focussed real estate lending. We anticipate significant product proliferation across global direct lending exposures in 2024. As such, we are taking a prudent approach to research, given existing offshore exposures typically have both significantly higher fees (management and performance) and leverage.

Real assets

Real estate is our least preferred alternative asset class, yet 2024 may present an attractive long-term entry point. There remains a meaningful dichotomy across different assets, sectors, geography and investment approaches, and a particular bifurcation between prime office and lower grade assets 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. Offshore industrial assets and multi-family accommodation are favoured alongside alternative sectors, such as self-storage, student accommodation, and manufactured housing. While Australia appears to be lagging due to a lack of transactions, we anticipate that global valuations may settle in 2024 and present an attractive long-term entry point for those that can look past the noise.

We favour growing infrastructure exposures in portfolios. 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. We see attractive investment opportunities focussed on energy transition, but where scale investors are able to build on established platforms and be prudent on entry valuations.

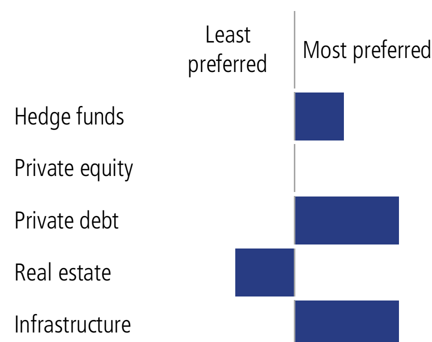
Our most preferred and least preferred exposures—We favour infrastructure, private debt, and low-beta hedge fund exposures while maintaining private equity exposures. We are taking a cautious approach to real estate globally.

What we like

- Credit-oriented strategies; low-beta exposure more generally.
- Senior private debt (strategies 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

- Long-bias equity hedge fund strategies.
- Lower grade and/or buy-and-hold real estate assets (particularly office).
- 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 GIC's 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 Target Price	P/E 1yr fwd (x)	Dividend yield	ROIC	ROE	1yr EPS growth	MSCI ESG rating
REA	REA Group Ltd	Comm. Serv.	$186.62	$167.09	53.3	1.1%	34.9%	29%	19%	AA
ALL	Aristocrat Leisure Ltd	Cons. Disc.	$44.06	$47.15	20.4	1.7%	22.8%	20%	9%	AA
TLC	Lottery Corp Ltd	Cons. Disc.	$4.99	$5.32	29.9	3.3%	21.7%	132%	10%	AA
MTS	Metcash Ltd	Cons. Staples	$3.59	$3.87	12.6	5.7%	19.6%	25%	0%	AAA
ALD	Ampol Ltd	Energy	$36.29	$37.53	11.5	7.1%	17.0%	20%	-7%	AA
MQG	Macquarie Group Ltd	Financials	$188.01	$185.68	19.6	3.4%	na	11%	20%	AA
IAG	Insurance Aust. Group	Financials	$5.91	$6.17	16.6	4.4%	na	13%	13%	AA
RMD	ResMed Inc	Health Care	$28.95	$32.62	25.7	0.7%	23.9%	25%	11%	A
CSL	CSL Ltd	Health Care	$296.74	$319.71	32.4	0.9%	13.5%	17%	17%	AA
MND	Monadelphous Group	Industrials	$13.47	$14.72	20.6	4.2%	17.1%	14%	17%	AAA
BXB	Brambles Ltd	Industrials	$14.47	$15.52	18.1	2.0%	19.2%	24%	10%	AAA
ALU	Altium Ltd	Info. Tech.	$49.35	$48.30	51.7	1.1%	38.5%	26%	25%	AA
XRO	Xero Ltd	Info. Tech.	$110.98	$119.25	119.5	0.0%	9.8%	13%	61%	AA
IGO	IGO Ltd	Materials	$7.73	$9.41	9.4	3.5%	9.2%	17%	-43%	AA
JHX	James Hardie Industries	Materials	$57.66	$55.99	23.6	0.0%	52.9%	39%	9%	AA
GMG	Goodman Group	Real Estate	$25.28	$25.64	24.0	1.2%	10.1%	11%	10%	AA
APA	APA Group	Utilities	$8.36	$8.99	39.2	6.7%	7.0%	13%	11%	A

Source: Bloomberg Analyst consensus and MSCI Research. This list does not constitute research and is the output of material prepared by our research providers. To obtain a copy of the underlying research, please contact your investment adviser. Data as of 31 January 2024. ESG is environmental, social, and corporate governance.

Trade opportunities

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

ResMed (RMD)—Buy. RMD remains in a bear market. Its share price is lower than levels where its major competitor, Philips, was forced to withdraw its product from the market. Fears over the impact of GLP-1s on sleep apnoea are unlikely to materially alter the near-term earnings trajectory. The three-year forward EPS has actually risen 10% over the past 12 months.

Aristocrat Leisure (ALL)—Trim. Although ALL is a long-term portfolio holding, it has performed strongly recently, and is now approaching 20x P/E. Although a moderation in consumer spending is yet to materialise, it remains a risk.

IGO Group (IGO)—Buy. IGO's 40% share price fall is its largest since 2019, but is in line with its average drawdown since 2015. As the world's lowest cost producer of lithium with a large net cash position, IGO is well positioned to weather the current weakness in lithium prices.

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 Target Price	P/E 1yr fwd (x)	P/B 1yr fwd (x)	Franking	Div. yield	1yr DPS growth	MSCI ESG rating
IAG	Insurance Aust,. Group	Financials	$5.91	$6.17	14.7	2.2	30%	4.4%	16.5%	AA
MQG	Macquarie Group Ltd	Financials	$188.01	$185.68	16.4	2.1	40%	3.4%	9.8%	AA
WBC	Westpac Banking Corp	Financials	$23.82	$22.09	13.0	1.2	100%	6.0%	0.4%	A
QBE	QBE Insurance Group Ltd	Financials	$15.43	$17.89	8.9	1.7	10%	3.0%	30.1%	AAA
COL	Coles Group Ltd	Cons. Staples	$15.70	$16.19	19.3	6.2	100%	4.0%	5.8%	AA
MTS	Metcash Ltd	Cons. Staples	$3.59	$3.87	12.6	3.1	100%	5.7%	0.0%	AAA
TLC	Lottery Corp Ltd	Cons. Disc.	$4.99	$5.32	27.1	41.9	100%	3.3%	9.1%	AA
TAH	Tabcorp Holdings Ltd	Cons. Disc.	$0.76	$1.04	14.6	0.7	100%	1.8%	121.4%	AA
TLS	Telstra Group Ltd	Com. Services	$4.02	$4.48	20.5	3.0	100%	4.5%	5.0%	AA
NEC	Nine Entertainment Co.	Com. Services	$1.98	$2.23	13.5	1.9	0%	4.9%	10.4%	AA
RMD	ResMed Inc	Health Care	$28.95	$32.62	23.2	6.3	100%	0.7%	10.2%	A
PME	Pro Medicus Ltd	Health Care	$101.17	$75.62	101.5	76.1	100%	0.4%	29.1%	BBB
REP	RAM Essential Services	Real Estate	$0.69	$0.84	14.4	1.4	0%	8.1%	-7.1%	--
SGP	Stockland	Real Estate	$4.47	$4.60	13.4	1.0	0%	5.6%	6.7%	AA
IRE	IRESS Ltd	Info. Tech	$8.28	$8.99	26.4	5.8	0%	1.1%	131.8%	AA
DBI	Dalrymple Bay Infra.	Industrials	$2.78	$2.70	15.0	1.2	39%	7.5%	3480.3%	--
ALX	Atlas Arteria Ltd	Industrials	$5.47	$5.84	14.1	1.2	0%	7.3%	-2.0%	AA
APA	APA Group	Utilities	$8.36	$8.99	35.3	5.2	0%	6.7%	1.6%	AAA
ALD	Ampol Ltd	Energy	$36.29	$37.53	12.5	2.6	100%	7.1%	-17.3%	AA
AMC	Beach Energy Ltd	Energy	$1.62	$1.81	5.8	na	100%	2.9%	110.6%	AAA
BHP	BHP Group Ltd	Materials	$47.05	$48.66	11.6	3.5	100%	3.3%	-2.3%	A
AMC	Amcor PLC	Materials	$14.44	$14.91	13.0	na	0%	3.4%	2.5%	AA

Source: Bloomberg Analyst consensus and MSCI Research. This list does not constitute research and is the output of material prepared by our research providers. To obtain a copy of the underlying research, please contact your investment adviser. Data as of 31 January 2024. ESG is environmental, social, and corporate governance.

Trade opportunities

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

The Lottery Corp (TLC)—Buy. On the back of higher yields, TLC's share price has retraced around 12% from its highs. Gearing levels for a defensive cashflow business such as TLC are forecast to fall well below target levels into next year. This should open the possibility for additional capital management opportunities.

RAMS Essential Services Property (REP)—Buy. Having announced a $22 million share buyback in November (4% of issued capital), management is actively executing on this program, and the buyback is 10% complete. With 90% of the buyback remaining and a dividend yield of 7-8%, the stock's total return characteristics for the remainder of 2024 are attractive.

APA Group (APA)—Buy. APA is trading close to nine-year lows, and with easing bond yields valuation pressure has moderated. This makes its decade-low enterprise value/EBITDA of around 11.5x attractive—not to mention a 7% dividend yield for a company whose dividend per share has increased every year for 20 years.

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 Price Tgt.	P/E 1yr fwd (x)	Yield (%)	Market cap (USD bn)	MSCI ESG rating
LSEG LN	LSEG	Financials	GBP	9002.00	10189.94	24.5	1.4	61,869	AA
LLOY LN	Lloyds Banking Group	Financials	GBP	43.02	57.17	6.2	7.2	34,725	AA
WFC US	Wells Fargo & Co	Financials	USD	51.19	55.42	9.6	3.1	184,228	BB
2318 HK	Ping An Insurance Group	Financials	HKD	32.50	63.07	3.9	7.9	91,213	A
939 HK	China Construction Bank	Financials	HKD	4.65	6.03	3.1	8.8	152,102	A
2330 TT	Taiwan Semi. Manuf.	Information Tech.	TWD	642.00	713.24	13.6	2.3	534,630	AAA
MA US	Mastercard Inc	Financials	USD	445.19	470.81	31.4	0.6	417,489	AA
ASML NA	ASML Holding NV	Information Tech.	EUR	801.30	832.82	28.5	1.1	347,211	AAA
GOOGL US	Alphabet Inc	Comm. Services	USD	151.46	159.81	18.3	0.0	1,905,470	BBB
UMG NA	Universal Music Group	Comm. Services	EUR	27.76	28.61	29.0	1.9	54,837	AA
DIS US	Walt Disney Co	Comm. Services	USD	96.94	104.59	18.5	0.8	177,431	A
9988 HK	Alibaba Group Holding	Consumer Disc.	HKD	71.15	110.76	7.7	0.5	185,185	BBB
NKE US	NIKE Inc	Consumer Disc.	USD	104.18	123.39	24.5	1.5	157,845	BBB
SBUX US	Starbucks Corp	Consumer Disc.	USD	94.08	110.09	19.6	2.6	106,517	A
ABNB US	Airbnb Inc	Consumer Disc.	USD	149.44	138.70	32.0	0.0	96,903	BB
RACE IM	Ferrari NV	Consumer Disc.	EUR	322.90	333.69	42.1	0.8	63,132	BB
BA US	Boeing Co/The	Industrials	USD	200.44	261.58	55.4	0.2	121,262	BBB
DSV DC	DSV A/S	Industrials	DKK	1236.00	1435.68	21.4	0.6	39,376	AA
MSFT US	Microsoft Corp	Information Tech.	USD	408.59	433.57	31.3	0.8	3,036,002	AAA
JNJ US	Johnson & Johnson	Health Care	USD	158.77	175.65	14.4	3.2	382,204	AAA
NOVOB DC	Novo Nordisk A/S	Health Care	DKK	748.20	750.69	33.2	1.5	490,862	AAA
ISRG US	Intuitive Surgical Inc	Health Care	USD	377.29	388.37	52.4	0.0	132,833	A
EL US	Estee Lauder Cos Inc	Consumer Staples	USD	134.18	142.31	32.8	2.1	48,016	A
COST US	Costco Wholesale Corp	Consumer Staples	USD	700.74	678.45	40.8	0.6	310,938	A
288 HK	WH Group Ltd	Consumer Staples	HKD	4.64	6.19	6.4	0.8	7,615	BBB
SHW US	Sherwin-Williams Co	Materials	USD	307.63	319.59	24.2	1.0	78,743	A
SHEL LN	Shell PLC	Energy	GBP	2474.00	3031.18	7.7	0.1	204,167	AA
EQIX US	Equinix Inc	Real Estate	USD	841.58	852.86	73.5	2.0	79,010	AA
ORSTED DC	Orsted AS	Utilities	DKK	377.00	433.29	18.1	3.7	23,054	AAA
		Average Yield:					2.0%		

Source: Bloomberg Analyst consensus and MSCI Research. This list does not constitute research and is the output of material prepared by our research providers. To obtain a copy of the underlying research, please contact your investment adviser. Data as of 31 January 2024. ESG is environmental, social, and corporate governance.

Recommendations: Thematic investing—Healthcare and genomics

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
- Energy transition
- Metaverse
- Security and safety
- Supply chain disruption
- Sustainable investing

Healthcare and genomics—Select exposures

Healthcare and genomics sit at the intersection of several other major long-term investment trends – ageing, population growth, finance, and technology. The ageing of societies is one of the easiest predictions to make about the future.

Code	Company	Sector	Base CCY	Market price	Consensus Price Tgt.	P/E 1yr fwd (x)	Yield (%)	Market cap (USD bn)	MSCI ESG rating
NKE US	NIKE Inc	Cons. Disc	USD	110.37	118.72	25.27	1.42	167973.22	BBB
JNJ US	Johnson & Johnson	Health Care	USD	152.11	174.21	14.08	3.22	366171.15	A
UNH US	UnitedHealth Group Inc	Health Care	USD	534.98	590.28	19.19	1.49	494816.53	AA
NOVOB DC	Novo Nordisk A/S	Health Care	DKK	689.40	722.71	30.82	1.62	457644.95	AAA
DHR US	Danaher Corp	Health Care	USD	222.52	232.21	28.24	0.49	164426.06	AA
ISRG US	Intuitive Surgical Inc	Health Care	USD	310.76	316.26	49.50	0.00	109409.77	A
ILMN US	Illumina Inc	Health Care	USD	101.57	138.90	93.10	0.00	16129.32	A
CSL AU	CSL Ltd	Health Care	AUD	261.16	319.02	24.60	1.15	83717.93	AA
RMD AU	ResMed Inc	Health Care	AUD	24.16	31.66	19.70	0.89	23582.62	A
COH AU	Cochlear Ltd	Health Care	AUD	270.88	243.22	42.67	1.64	11774.63	AAA
PME AU	Pro Medicus Ltd	Health Care	AUD	88.62	76.28	89.15	0.55	6142.48	--
A US	Agilent Technologies Inc	Health Care	USD	127.59	130.62	21.11	0.82	37272.00	AA
FRE GY	Fresenius SE & Co KGaA	Health Care	EUR	28.57	37.94	9.16	3.45	17660.63	A
MRK US	Merck & Co Inc	Health Care	USD	101.13	124.56	11.89	3.16	256265.75	A
EXAS US	Exact Sciences Corp	Health Care	USD	65.06	87.36	n/a	0.00	11766.10	A
CRSP US	CRISPR Therapeutics AG	Health Care	USD	69.09	88.17	n/a	0.00	5487.99	--
PFE US	Pfizer Inc	Health Care	USD	30.08	39.71	9.54	5.51	169844.11	A
ROG SW	Roche Holding AG	Health Care	CHF	236.40	302.67	11.74	4.21	220803.59	A
NOVN SW	Novartis AG	Health Care	CHF	84.84	94.75	13.57	4.37	221431.59	AA
AZN LN	AstraZeneca PLC	Health Care	GBP	10032.00	12869.52	15.32	0.03	197500.13	AA

Source: Bloomberg Analyst consensus and MSCI Research. Data as of 31st January 2024. ESG is environmental, social, and corporate governance.

Important information

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