CURMI & PARTNERS

October 18th, 2023

Monthly Strategy Update

The quarter in summary:

The recent escalation in the Middle East in the aftermath of the horrible attack in Israel is a key area of concern for investors. First and foremost, the loss of human life is a terrible consequence of war, but we were also reminded of the impact this can have on the global economy, as the US Dollar and Oil inched higher. How this conflict evolves could have severe current and future implications on the global economy.

During the third quarter most asset classes we follow, except for credit, generated negative returns against a backdrop of heightened rates volatility. The year has been a complex one for investors with different data suggesting very different outcomes. Economic data is divergent, and inflation remains high but moderating though corporate earnings have so far remained resilient. The strength of the US economy has surprised markets, despite fears of a sudden slowdown in Q4. During the last two months, we saw a re-pricing in rates leading to a reversal of the interest rate cuts previously expected in 2024, with "higher-for-longer" narrative now being priced-in. This explains the sell-off in yields seen in 3Q23, with the US 10-year paper yielding 4.6% by the end of September or 73bp higher than the yield at the end of June 2023. The risks around policy decisions weighed on the safer US credit buckets, as USD IG lost 3.1% during the quarter as opposed to a small gain for EUR IG (+0.3%) where potentially the headwind from more tightening by the ECB is less relevant.

On the equity side, the combination of rising real yields and growth eluding both China and Europe weighed on the asset class performance in 3Q23. The only exception was the FTSE 100, where its high allocation to the energy sector benefited from the strong rally seen in oil during the quarter. The sell-off was quite broad and indiscriminative. Using two US indices as a gauge to exclude region preference from the equation, the Nasdaq (growth stocks proxy) lost 3.9% in 3Q23 compared to 2.1% loss for the Dow Jones Industrial Average (value stocks proxy). Also of note, is the weakness seen in the German stock market (a China proxy), shedding 4.7% during the period.

Commodities rallied strongly, as the S&P GSCI commodity index gained c.14%, recovering from a c.11% loss in 1H23. Within commodities, we note that Brent Oil had a particularly strong quarter, with prices up c. 30% in the period, following a decline of c.12% in 1H23. Also, the US Dollar strengthened during 3Q23, with the Dollar basket up 3.2% during the period after a 0.6% decline in 1H23.

Sovereign				
Movement in yield	Yield	Sep bp	3Q23 bp	YTD bp
US 10-year yield	4.6%	46	73	70
DE 10-year yield	2.8%	11	45	-18
UK 10-year yield	4.4%	21	5	72
Credit				
LCL Total returns		MoM %	3Q23 %	YTD %
EUR IG		-0.9%	0.3%	2.5%
EUR HY		0.3%	1.9%	6.8%
USD IG		-2.7%	-3.1%	0.0%
USD HY		-1.2%	0.5%	5.9%
GBP IG		0.0%	2.2%	1.2%
GBP HY		1.2%	3.8%	8.3%
Equities				
LCL Total returns		MoM %	3Q23 %	YTD %
Global		-4.3%	-3.4%	11.6%
S&P 500		-4.8%	-3.3%	13.1%
Nasdaq 100		-5.8%	-3.9%	27.1%
STOXX 600		-1.7%	-2.1%	8.5%
DAX		-3.5%	-4.7%	10.5%
CAC		-2.4%	-3.4%	13.4%
FTSE 100		2.4%	2.1%	5.2%
Emerging markets		-2.6%	-0.3%	5.0%
EM ASIA		-2.6%	-2.9%	2.1%
EM LATAM		-2.7%	-3.3%	-0.2%
EM EMEA		-2.3%	-4.7%	12.9%
Currencies				
Total return		MoM %	3Q23 %	YTD %
EURUSD		-2.5%	-3.1%	-1.2%
EURCHF		1.0%	-1.1%	-2.2%
GBPEUR		-1.3%	-0.8%	2.2%
GBPUSD		-3.7%	-3.9%	1.0%
Commodities				
Total return		MoM %	3Q23 %	YTD %
Oil WTI		9.4%	29.9%	15.9%
Oil Brent		6.9%	24.3%	12.3%
Natural Gas		5.8%	5.3%	-34.5%
Gold		-4.7%	-2.8%	1.3%
Copper		-1.8%	-1.2%	-1.2%
Iron Ore		1.2%	11.7%	2.6%
S&P GSCI Index		3.1%	13.9%	-0.1%

Robert Ducker, CFA
+356 23426112

Macro-economic views

The economic data published over the past weeks continued the trend of surprisingly resilient US growth, with some welcome early signs of stabilisation in both China and Europe. Global manufacturing PMI improved for the second consecutive month in September (49.1), led by output and new orders whilst the global services sector slowed down, with growth moderating to an eight-month low (50.8) driven by weaker business and consumer services sectors.

China's economic slowdown in the early summer months was a key concern for markets, especially due to the implications this would have on global growth. However, we note that there have been recent signs that the worst is now behind us. The official NBS composite PMI picked up for a second consecutive month (52.0), as the manufacturing PMI has now risen for four consecutive months and moved to expansionary territory for the first time since March. Yet, the Caixin PMI (which focuses mostly on small and medium sized companies) released a day later surprised to the downside with composite (50.9) and manufacturing (50.6) both easing but still in expansionary territory.

The stabilisation in global growth provided the market with some respite, but the fiscal dynamics in the US are becoming a concern. More specifically, for a country running at full employment and growing at a rate above trend, the fiscal deficit of 5.3% (2022) remains above the average of 3.3% (calculated since 1929). This suggests that the cyclically adjusted budget deficit may be meaningfully higher, and, except for the COVID-19 impacted years, the current budget deficit is at the highest levels since 2012. Treasury supply has been rising sharply over the past years and will probably keep on rising in the future (which results in a higher term premium).

Also, the situation is being made worse by the political dynamics in the US, where the temporary funding bill negotiated at the end of September will keep the government operating through November 17, at which point a new agreement will have to be reached. The probability of a similar resolution is unlikely, given that House Speaker McCarthy was removed from office. The removal of the Speaker not only puts the House agenda on hold until a new speaker is appointed, but with the Republicans having a slim majority in the House, appointing a new speaker will not be a straightforward task. McCarthy himself only managed to become speaker after making a series of concessions to the most conservative members, and similar factors will again be in play. In our opinion, this raises the probability of a shutdown in November which could weigh on US growth in Q4.

Exhibit 1 – Consensus real GDP growth and inflation expectations

Global economic growth expectations for FY23 revised slightly higher driven by the strength seen in the US and Japan economy

	Consensus, YoY%			IMF, YoY%		
Real GDP, YoY%	*FY23F*	*FY24F*	*FY25F*	*FY23F*	*FY24F*	*FY25F*
United States	2.1	1.0	1.9	2.1	1.5	1.8
Japan	1.8	1.0	1.1	2.0	1.0	0.7
Germany	-0.4	0.6	1.4	-0.5	0.9	2.0
France	0.8	0.8	1.4	1.0	1.3	1.8
Italy	0.7	0.6	1.2	0.7	0.7	1.0
Spain	2.2	1.5	2.0	2.5	1.7	2.1
Eurozone	0.5	0.8	1.5	0.7	1.2	1.8
UK	0.4	0.4	1.4	0.5	0.6	2.0
Developed Economies	1.5	1.1	1.8	1.5	1.4	1.8
China	5.0	4.5	4.5	5.0	4.2	4.1
Emerging Economies	3.8	4.0	4.2	4.0	4.0	4.1
Global	2.8	2.6	3.0	3.0	2.9	3.2

	Consensus, YoY%			IMF, YoY%		
Consumer Prices, YoY%	*FY23F*	*FY24F*	*FY25F*	*FY23F*	*FY24F*	*FY25F*
United States	4.1	2.7	2.3	3.0	2.6	2.3
Japan	3.1	1.9	1.4	2.7	2.6	1.8
Germany	6.1	3.0	2.1	4.1	2.8	2.4
France	5.7	2.7	2.0	4.0	1.9	2.5
Italy	6.3	2.3	2.1	1.1	3.0	2.2
Spain	3.5	2.9	1.9	4.0	3.4	1.5
Eurozone	6.3	3.0	2.2	3.3	2.7	2.2
UK	7.4	3.1	2.2	5.2	2.4	2.0
Developed Economies	5.6	3.6	2.6	3.3	2.6	2.2
China	0.6	1.9	2.0	0.9	1.9	2.2
Emerging Economies	5.9	5.9	4.1	8.5	6.8	6.0
Global	6.0	4.3	3.5	6.4	5.1	4.5

Source: Bloomberg Consensus Forecasts as at 10/10 and IMF October 2023 forecasts

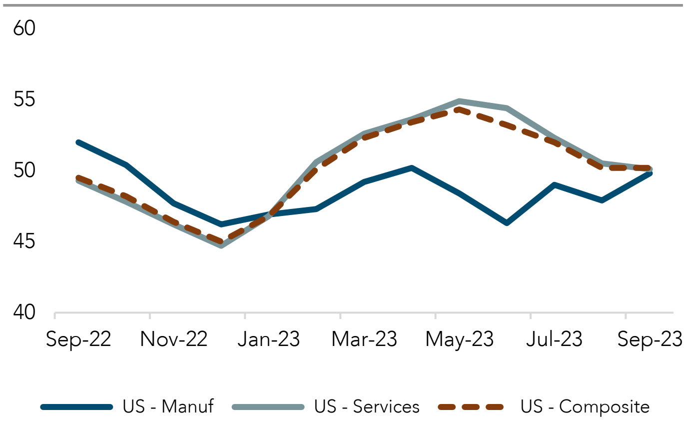
United States

The above-trend economic growth in the US probably persisted during 3Q despite expectations that growth would moderate in 2H23. Bloomberg consensus was expecting growth of c.0.3% in 3Q at the start of the year, which has been revised up to 2.1%. The expected slowdown never materialised as consumer spending, financed primarily from household savings, boosted growth. Forward-looking indicators do not point to any meaningful weakness in September. The S&P Composite PMI remained unchanged at 50.2, as the 0.4pp softening in services, led by the second consecutive drop in new orders, was offset by the 1.9pp improvement in manufacturing to 49.8 (Exhibit 2). Currently, the Atlanta FED's GDP tracker points to 5.1% QoQ saar growth in 3Q23 (Exhibit 3), with consumption expenditures expected to contribute to 48.9% of GDP growth during the period. Yet, growth in 4Q is likely to slow due to: (1) end of student loan mortarium; (2) tighter financial conditions; (3) replenishing of savings by households; (4) UAW strike; (5) higher commodity prices and (6) Government shutdown.

The September inflation release came in above expectations as Core CPI index rose 0.3% MoM, a 2bp increase from last month's print. On a YoY basis, Core CPI rose 4.1% in September, c. 20bp decrease from August (Exhibit 4). Furthermore, the recent uptick in job openings led to a re-opening in the job-workers gap which could suggest more pressure on prices going forward.

Exhibit 2 – US S&P Manufacturing, Services and Composite PMI

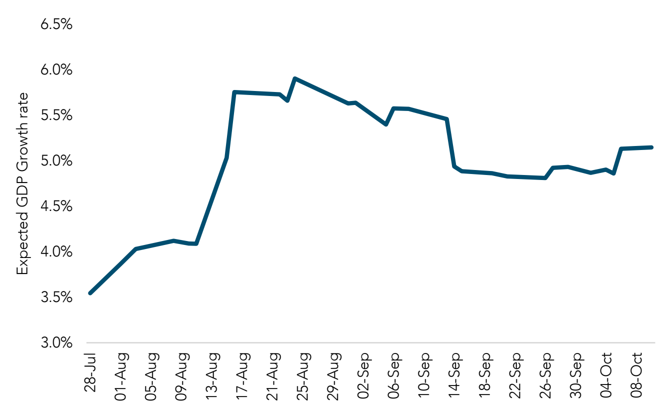
The composite PMI was unchanged during September as the recovery in manufacturing was offset by some softness in services



Source: Bloomberg

Exhibit 3 – Atlanta FED GDP estimate

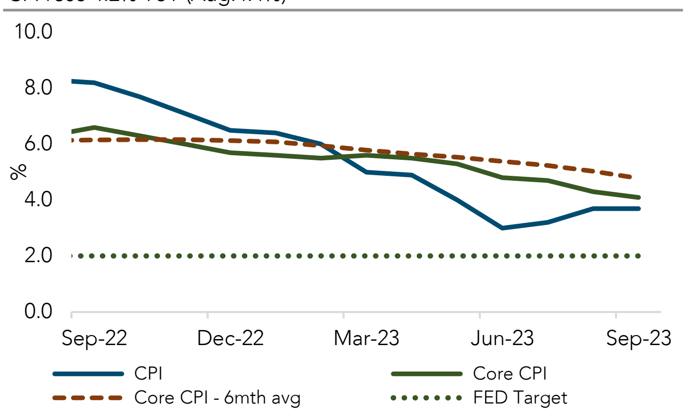
The latest Atlanta Fed forecast points (10/10) to 3Q QoQ saar GDP growth of 5.1%, following a peak reached in August of 5.9% (24/08)



Source: Atlanta FED

Exhibit 4 – US Inflation rate

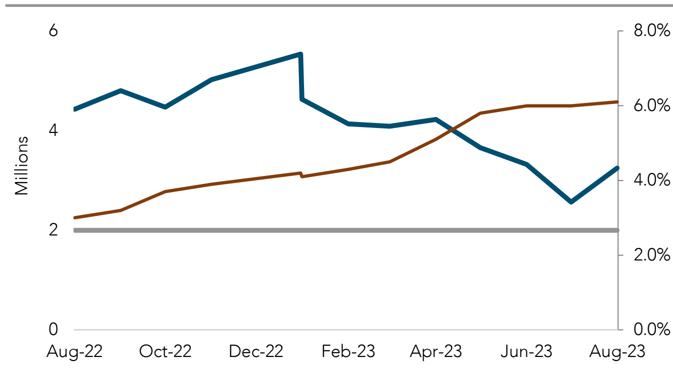
Headline CPI rose 3.7% YoY in September (Aug:3.7%) whilst Core CPI rose 4.2% YoY (Aug:4.4%)



Source: Bloomberg

Exhibit 5 – Job-workers gap (LHS) and Atlanta FED wage tracker (RHS)

The job-workers gap re-opened during August, with job openings rising to 9.6 million



Source: FRED, Atlanta FED

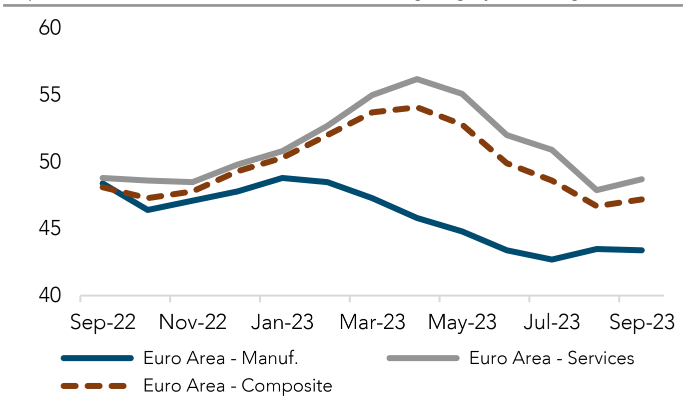
Europe

The economic situation in Europe has worsened throughout 2023, after a promising start to the year when the composite PMI improved to 54.1 by April, from 49.3 in December 2022. Yet, economic activity slowed down significantly since then as the composite PMI fell in contraction territory and has been there for the past four consecutive months. However, we note an uptick in activity during September to 47.2 (from 46.7), driven by the services sector (48.7) with manufacturing still under pressure as new orders continue to shrink (Exhibit 6). The Euro-area now-cast tracks real GDP growth of -0.5% QoQ in 3Q (Exhibit 7), whilst the Bank of Italy Eurocoin tracker estimates growth at -0.2% QoQ. This is not surprising given that retail sales in the region contracted 1.2% in September after reporting no growth in the previous two months.

Core inflation in Europe moderated to 5.3% in August with inflation on a downtrend since its peak in March 2023 (Exhibit 9). We expect this downward trend to continued over the coming months given the extent of the economic deterioration. Demand in the region could also be further impacted by the tightening of financial conditions. Bank lending rates data shows that the new loans have re-priced over the past months. Looking at data since December 2021, it appears that new corporate and mortgage loans have re-priced significantly higher. As of August, c.81% and 56% of the 425bp increase in policy rates have been passed-through corporate loans and mortgage loans respectively (Exhibit 8).

Exhibit 6 – EU S&P Composite, Manufacturing and Services PMI

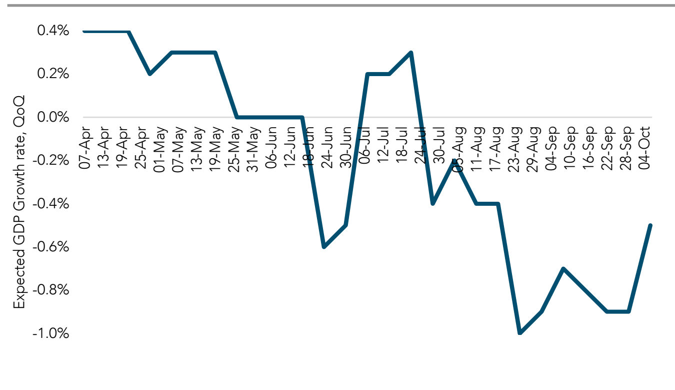
The Composite PMI improved to 47.2 in September, driven by improvement in Services with manufacturing largely unchanged



Source: Bloomberg

Exhibit 7 – EU Q3 GDP Growth Tracker (as at 6th October)

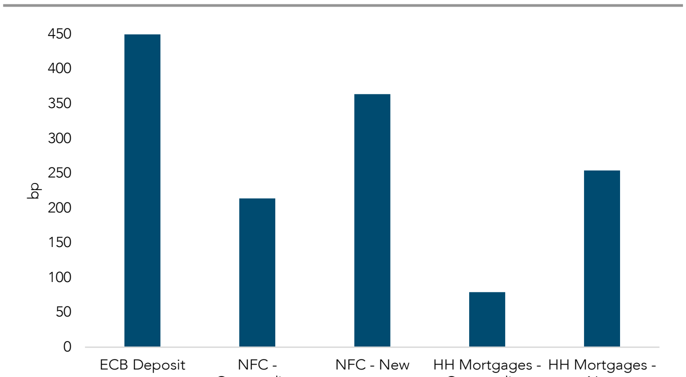
Euro-area's GDP is expected to turn negative in Q3 after surprising at -0.5% QoQ annualised



Source: Giannone, Garcia et al – International Journal of Forecasting

Exhibit 8 – Policy rate impact on lending rates up to August 2023

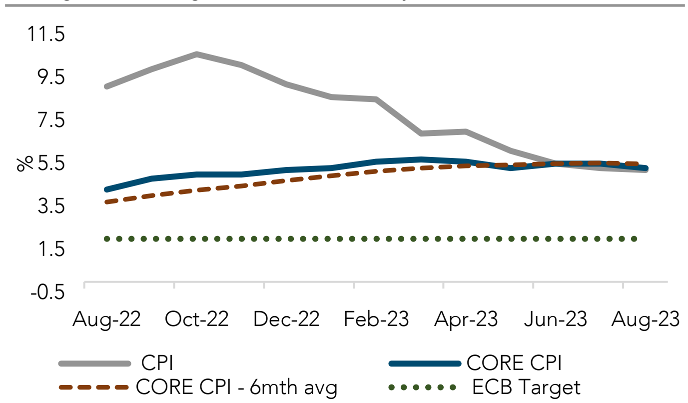
Cumulative increase in lending rates since December 2021 to August 2023



Source: ECB

Exhibit 9 – HICP headline and core inflation

Core HICP inflation moderated further in August with the 6-month average moderating for the first time this year

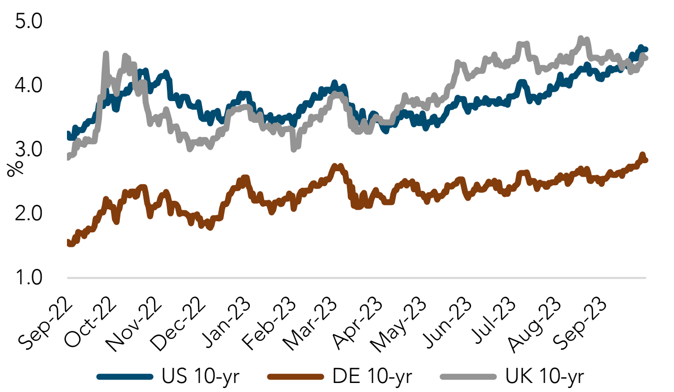


Source: Bloomberg

Rates

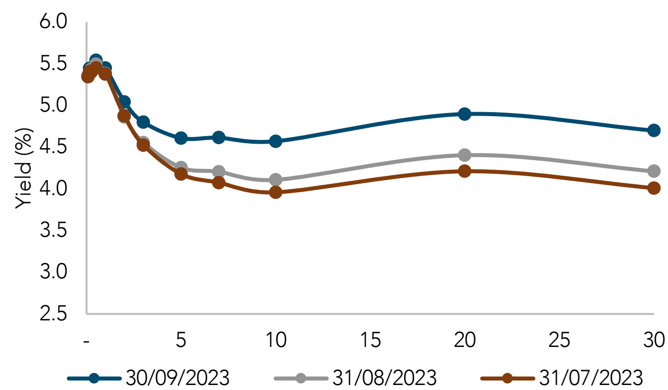
The sell-off in yields during September was severe as investors started to price-in the "higher-for-longer" message that has been a mainstay in central bank language for some time. Furthermore, uncertainty about inflation, mainly coming from the continued resilience shown by the US economy, as well as the stabilization in China and the rally seen in oil prices, as well as concerns around the fiscal deficit in the US, Italy and France also weighed on rates during September. In terms of central bank policy action, nine out of the ten central banks with the most heavily traded currencies held meetings last month, but only three (Sweden, Norway and European Central Bank) hiked rates by 25bp each. The US FED, Bank of England, Australia, Canada, Switzerland and Japan opted for a pause. The New Zealand central bank did not meet last month.

Exhibit 10 - 10-year nominal bond yield for the US, Germany and UK
Sovereign bond yields rose sharply last month in all regions with the UST 10-year at levels not seen since 2007



Source: Bloomberg

Exhibit 11 – US Yield Curve
The yield curve steepened during September as the long-end of the curve sold-off whilst the short-end was largely unchanged



Source: Bloomberg

United States

Financial conditions have tightened significantly throughout September as yields rose 46bp to 4.6%, levels not seen since 2007. The sell-off was mainly concentrated at the long-end of the curve, leading to a steeping of the yield curve as the 2s10s spread tightened 28bp during the month. The steeping in the US yield curve reflects greater confidence by investors in the strength of the US economy, with growth reported so far more than exceeding consensus expectations. However, there is reason to believe that growth in the US may slow down in Q4, and this should become more apparent in future data releases. Following the sharp sell-off in yields, we expect some of this to reverse if economic data weakens over the coming weeks.

There is still some uncertainty about what the FED will do at its next meeting in November, though the message from the central bank has always been that high policy rates will be maintained for a considerable amount of time. The divide within the FOMC became clear during recent speeches. Cleveland Fed President Mester, Minneapolis Fed President Kashkari and Governor Bowman signalled that they are likely to support more tightening, whilst New York Fed President Williams, Atlanta Fed President Bostic and San Francisco Fed President Daly expressed their preference to hold rates unchanged.

Following the release of the US labour market data on 06/10 the market was pricing in a c.30% probability of a rate hike in November. This has gone down to 9% by 17/10, which implies that the view has changed over the weekend. The release of the September FOMC minutes will allow for a better understanding of the participants' view on the disinflation progress achieved.

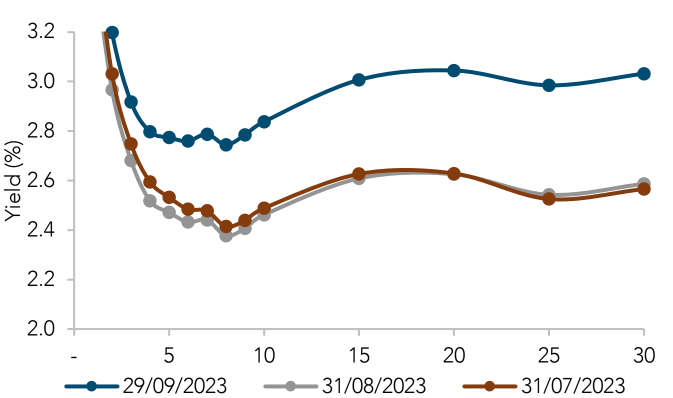
Europe

During September, the yield on the 10-year German bond rose 37bp to 2.8%, levels not seen since 2011 driven by the US led sell-off in yields. The economic conditions in Europe have worsened significantly over the past months, nevertheless the September PMI showed some improvement albeit from a depressed level. This could suggest that the worst in terms of economic weakening could be behind us. Economic growth is expected to pick-up slightly in the coming quarters, but in the near-term we expect movement in European yields to be dictated by US news-flow, inflation data, with energy a key consideration (the Middle East conflict could have implications on energy prices), fiscal news coming out of France and Italy and QT related news-flow.

On this latter point, there has been some concern that the latest budgetary announcements from Italy and France are too optimistic on growth. Italy raised its deficit target (deficit/GDP) to 5.3% of GDP in 2023 (from 4.5%) and 4.3% in 2024. This assumes GDP growth of 0.8% in 2023 (vs consensus estimate of 0.7%) and 1.2% in 2024 (cons: 0.8%). Italy is planning virtually no debt reduction through 2026 and the deficit is not expected to return below the 3% Maastricht threshold until 2026. As for France, the budget deficit targets have been left unchanged at 4.9% and 4.4% of GDP respectively, though the deficit is not expected to return below the 3% Maastricht threshold until 2027. Real GDP growth is still expected at 1.0% in 2023 (consensus at 0.8%) with the 2024 forecast lowered to 1.4% (consensus at 0.8%). The 2024 real GDP growth forecasts for both Italy and France are well ahead of consensus, raising the probability of future downgrades by both countries unless growth picks up. Despite this, spreads have held up relatively well, with the French 10-year widening just 3bp since the end of July and the Italian BTP widening 33bp, and below levels seen at the start of the year (-19bp).

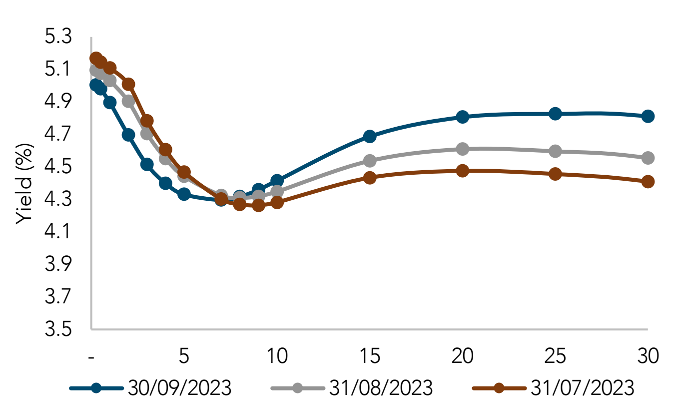
The yield on the UK 10-year paper rose just 8bp to 4.4%, primarily driven by the downside surprise in inflation and more encouraging news on the labour market front. This has led to a re-pricing lower of the terminal rate, limiting the spillover effect from the US. During its September meeting the BoE announced its intention to unwind Gilt holdings at a faster rate from this October, moving from £80 billion to £100 billion over 12 months, £50 billion of which will be through active sales. Also, over the past weeks MPC members spoke about the UK economy. BOE Deputy Governor Broadbent warned there are now "clear signs" that the economy is weakening, which was taken as dovish whilst MPC member Mann suggests more aggressive policy is required.

Exhibit 12 – German 10-year yield curve
The US-led re-pricing higher in G10 yields continued in September with the spread 2s10s spread tightening 15bp



Source: Bloomberg

Exhibit 13 – UK 10-year yield curve
The move in the 10-year Gilt was more contained, though a similar level of tightening in the 2s10s (32bp) was observed



Source: Bloomberg

Credit

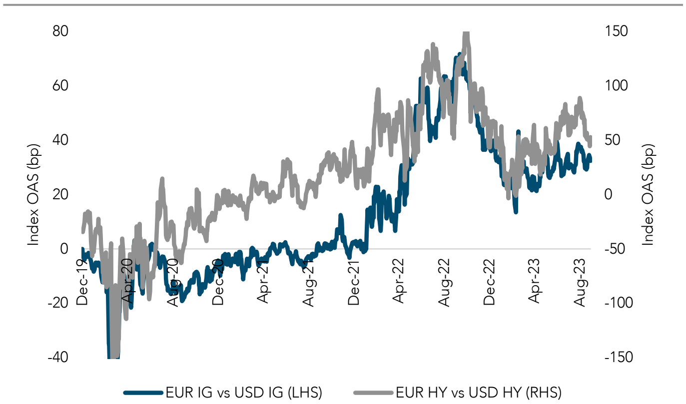
The broad sell-off across rates that started around May and intensified in mid-July has brought back painful memories of 2022. On balance we think that the moves in cash spreads have been largely contained, especially when considering the outsized move in rates. Over September, the yield on the US 10-year climbed 46bp compared to a 3bp widening in USD IG spreads and 23bp widening in USD HY spreads. The move in Europe was quite similar, with a relatively large move in the German Bund's 10-year yield (37bp) compared to 2bp tightening in EUR IG and 9bp tightening in EUR HY.

The move in rates was much more pronounced in US sovereign paper over the past month, and therefore the underperformance of USD credit should not come as a big surprise. USD IG fell 2.7% last month whilst USD HY fell 1.2%. In contrast, EUR IG fell 0.9% whilst EUR HY benefited from the tightening in spreads, gaining 0.3% during the month. The spread differential between EUR IG and USD IG seems to have peaked in October 2022 at c. 75bp, before moderating to 13bp by March 2023 (Exhibit 14). Since then, spreads have widened by around 18bp, reversing most of the Q1 EUR IG outperformance. A similar trend can be observed when looking at EUR HY and USD HY. Given that the current base case is for the US economy to cool down, we expect convergence between EUR IG and USD IG spread differential over the coming months. This supports our preference for EUR denominated credit as opposed to USD.

Economic data released in Europe over the month of September has continued to show evidence of the slowdown in the region, though there are early signs of stabilisation. Although recent news-flow around China could be a positive catalyst for the European economy, we believe that headwinds remain. Global manufacturing, an important sector for Europe, remains subdued and the recent rally in oil prices could have implications for headline inflation. Notwithstanding this continued deterioration in Europe's economic fundamentals, EUR HY spreads remain c.27bp tighter than the average calculated since 2003. By contrast, EUR IG spreads are currently 25bp wider. Generally, the risk of default rises during periods of economic slowdown, which makes the IG space preferable to investors. Yet, this has not been the case. In isolation, the current yield available in the HY space (c.8.6%) is attractive relative to history, ranking in the 88th percentile when looking at data since 2010. Yet, we caution that the current spread of 474bp ranks in the 66th percentile, which implies limited protection in the event of continued deterioration in Europe's economic fundamentals (Exhibit 15). On this basis, we continue to prefer EUR IG to EUR HY.

Exhibit 14 – EUR IG vs USD IG & EUR HY vs USD HY OAS

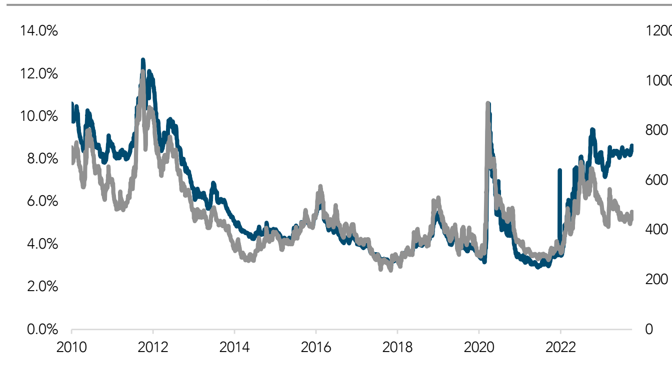
EUR-IG and EUR-HY have underperformed USD-IG and USD-HY since March as a result of the US economic outperformance



Source: Bloomberg

Exhibit 15 – Euro-Area HY OAS compared to YTW

Although YTW for HY bonds appears to be attractive relative to history, the cushion from spread is limited

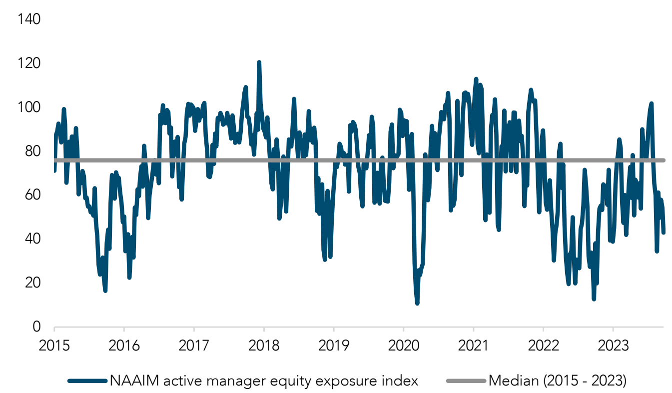


Source: Bloomberg

Equity

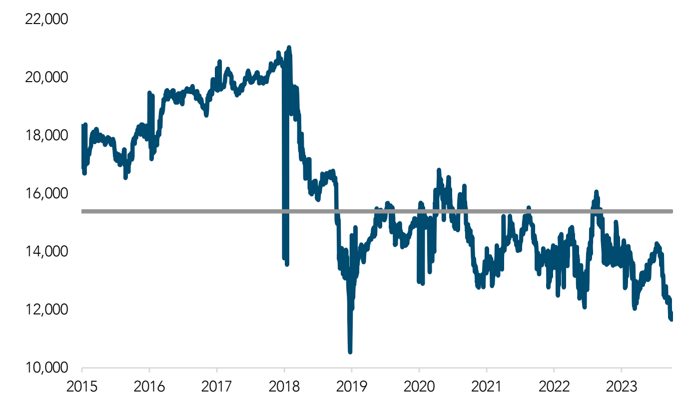
The narrative going into August was of the rising probability of a soft landing which was supported by a resilient but gently slowing US economy, moderating inflation and better than expected earnings growth. Equity market performance in 1H23 was strong (global equities gained 15.4% in local currency terms) but sticky inflation coupled with resilient labour markets led to concerns around policy path over the coming months. The probability of significant rate cuts in 2024 faded and this weighed on certain pockets of the equity market. Additionally, the sectors exposed to Europe's and China's economic strength were also under pressure for most of 3Q as the economic recovery faltered, though there are signs that the situation is starting to change.

Exhibit 16 – NAAIM active manager exposure to equity markets
The NAAIM exposure index suggest that overall, equity investor is below average



Source: National Association of Active Investment Managers

Exhibit 17 – SMART Index
The SMART index has also declined since July to levels not seen since 2018



Source: Bloomberg

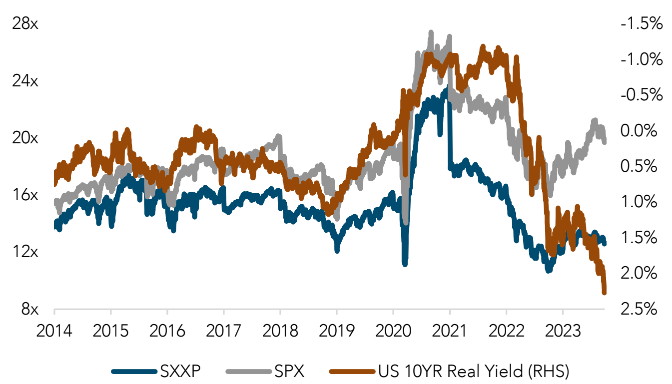
Investors positioned themselves for stagflation during the past two months, buying into commodities (namely Gold and Oil), and US Dollar, whilst increasing their allocation to cash. Active managers have reduced equity exposure sharply since the end of July (Exhibit 16) and is currently below the historical average (since 2015). The current NAAIM exposure index is at its lowest levels since December 2022. Also, the SMART index, which is a proxy for fast money investors, shows that hedge funds have likely reduced their equity exposure over the past months (Exhibit 17).

Global equities were able to climb higher during the four months ending in July despite real yields rising c. 53bp, reaching a peak of 1.8% (07/07), or an increase of 73bp. Equities and real yields are generally negatively correlated, but the upgrades in economic growth and earnings expectations supported the asset class for most of the year. Yet, investors have now finally accepted that rates will remain "higher-for-longer", and the equity/bond correlation has turned positive again, as the most recent surge in real yields (at 2.2% by 30/09, or +118bp since the bottom on 06/04) led to pressure on valuations (Exhibit 18). In Europe, this pressure from rising yields was more evident in long-duration equities, including sectors like Luxury goods (down 15.0% in two months ending in September) and Technology (-10.3%). Also, other interest-rate sensitive sectors like Renewables (-9.6%) underperformed during the period.

In the US, the Nasdaq index performed worst during the two-month period ending in September, following a strong rally in the first seven months of the year. In terms of sector performance, Transportation, Consumer durables and Banks underperformed the most during the period.

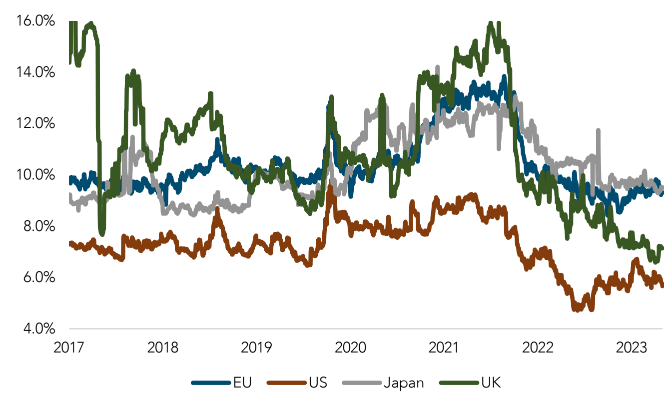
A consequence of the sharp re-pricing in fixed income markets over the past months is the higher yield on offer, making the asset class much more attractive relative to equities. As an illustration, the yield on the US 10-year paper is now at c.4.6%, well ahead of the average dividend yield on offer for the S&P 500 (c. 1.6%). The equity risk premium has been on a downward trend for the past two years (Exhibit 19). The implication here is that if the economic deterioration continues, as is currently being indicated by PMI readings, and earnings growth slows down meaningfully, equities are more likely to underperform bonds. We would expect outflows from equities into bonds, in view of the worse earnings growth outlook and less headwinds from rates.

Exhibit 18 – SPX and SXXP 12-fwd P/E vs UST10-year real yield
P/E's seem to be reconnecting with rising real yields over the past month after the decoupling in 1H23



Source: Bloomberg, FRED

Exhibit 19 - Equity Risk Premium
The Equity Risk Premium has been on a downward spiral since peaking in 2021



Source: Bloomberg

Historically, bond yields have peaked around the last FED hike and moved lower in the following months. This would imply less of a headwind for investors to move away from equities into fixed income not only because of the yield differential available, but also due to the relatively lower risks bond investors are exposed to, particularly in the current backdrop.

We believe that Q3 earnings will be especially important for equities, as positive earnings revisions has been one of the main drivers for the asset class this year. Slower EPS momentum would potentially lead to a re-assessment of the economic growth outlook, which we believe would be more positive for bonds than it is for equities. Also, share buybacks, a major source of demand for equities, have dried up in recent months.

Exhibit 20 – Valuations – Developed markets
Valuations in the US are in the 90th percentile and screen as expensive compared to other international markets

Historical Data	SPX	NDX	SXXP	SX5E	DAX	CAC	FTSE100	FTSE250
Current Forward PE ratio (FPE)	17.5x	22.2x	11.8x	11.4x	10.3x	11.7x	10.5x	10.0x
Forward PE ratio (31/12/2022)	16.8x	21.1x	11.9x	11.3x	10.5x	11.3x	10.0x	11.1x
10 Year data								
Highest	22.1x	30.8x	17.5x	18.0x	15.7x	18.2x	15.4x	17.9x
Highest (date)	31/12/2020	25/01/2021	29/12/2020	29/12/2020	28/12/2020	04/12/2020	02/12/2015	29/12/2020
Lowest	12.2x	15.2x	10.0x	9.0x	8.4x	9.1x	8.4x	8.3x
Lowest (date)	23/03/2020	15/04/2014	18/03/2020	18/03/2020	18/03/2020	18/03/2020	03/10/2022	23/03/2020
Median	16.2x	19.6x	13.7x	12.8x	12.2x	13.3x	12.8x	13.7x
95th percentile	20.4x	28.2x	16.0x	16.3x	14.5x	15.9x	14.9x	15.2x
5th percentile	14.2x	16.7x	11.8x	11.5x	10.9x	11.1x	9.9x	10.3x
Historical rank (since 2006)								
Percentile	85.1%	82.4%	33.9%	38.2%	24.4%	35.9%	29.2%	15.1%
Current FPE, % above/ (below) 10-YR median	7.6%	13.6%	-13.8%	-10.9%	-15.9%	-12.0%	-18.2%	-26.9%
Current FPE, % above/ (below) Dec 22	3.9%	5.6%	-0.4%	1.3%	-2.0%	3.8%	4.7%	-9.8%

Source: Bloomberg

Key – Our view

Positive | Positive /neutral | Neutral | Neutral/ negative | Negative

Key – Allocation

Overweight | Neutral | Underweight

Asset Class	Positioning
Developed Market Sovereign Bonds	We have continued to moderate our view on Developed Market Sovereign bonds given that we are, in our opinion, close to peak terminal rates in most developed economies. Given our view on peak rates we added exposure to the long-end of the curve. The recent sell-off in bonds was driven by the "higher-for-longer" narrative, and we believe this places significant importance on inflation data to be released over the coming months. If inflation moderates further and at a pace that is consistent with consensus views, we would expect less headwind for the rates market.
Investment Grade Corporate Bonds	The IG space has so far delivered positive returns in both Europe and the US despite an additional 200bp and 100bp tightening by the ECB and FED respectively. The recent re-pricing in the rates market to the "higher-for-longer" has weighed on the IG space, though the base case remains of continued moderation in economic growth and inflation going forward. The YTW for EUR-IG is currently at c4.6% which ranks in the 98th percentile since 2010. Additionally, the risk of rising defaults should the economic situation deteriorate further is much lower in IG when compared to HY. Yet, the uncertainty around the economic health of the region is a key risk for IG. On one hand, should inflation persist, it could force the ECB to tighten monetary policy further or keep rates at these levels for longer than currently anticipated. Also, assuming growth does not pick-up, the risk of stagflation will also rise, which could see investors preferring to hold cash or cash-like instruments.
High Yield Corporate Bonds	We maintain our underweight in HY given the current economic outlook and the risk of rising defaults. Although the current yield on offer is high relative to history as the YTW has been lower 88% of the time since 2010. However, the spread differential of 474bp has been lower 66% of the time, which implies that the cushion should the economic situation deteriorate further is much lower today compared to history. We believe that this is particularly important today given the uncertainty around the economic outlook and the deterioration in economic data we have observed over the past months in Europe. The higher-for-longer narrative could have greater implications for HY issuers, especially the lower-rated corporates that will have to refinance bonds (2025/2026 maturities) over the coming months with funding costs significantly higher.
Developed Market Equities	Despite the recent pullback, the base case for equities remains that of a soft landing, with growth in the US slowing to around the long-term growth rate, corporate earnings growth remains positive, and we reach a peak in rates. Yet, recent news-flow suggests that the soft-landing narrative is fragile, with upside risk to inflation and fixed income expected to offer more competition for investor flows. The August/September pullback has led to a moderation in valuation levels, but we believe that equity market performance will be impacted by: (1) The uncertainty around the economic outlook is growing, and any slowdown in earnings growth would raise the probability of stagflation. (2) A strong recovery in China would be helpful for the European equities, but increased demand for oil and an acceleration in economic would likely add to inflationary pressures. (3) Peak rates could potentially make the fixed income market attractive relative to equity markets.
Emerging Market Equities	EM equities have so far underperformed their DM counterparts, not helped by the strengthening in US Dollar and the uncertainty around the global economic backdrop. The Chinese economy has struggled this year, with data released early in the summer showing continued deterioration that has weighed on the country's equity market. However, we note early signs of stabilisation in the August data, with the latest PMI releases suggesting that the worst of the economic downturn could be behind us, a positive catalyst for its stock market.

Disclaimer