A Prudential plc company

September 2023

Monthly Views

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Summary

Macro overview

Growth: Global economic activity is holding up better than expected despite a high interest rate environment and heightened geopolitical uncertainty, supported by the global consumer. The market has shifted towards a higher probability of a soft landing, but the upturn remains relatively weak. Financial conditions have eased, global supply chains have recovered, and direct concerns about the health of the banking sector have receded. However, with a slower-than-anticipated economic recovery in China and extreme weather events in North Asia, the balance of risks to growth remains to the downside.

Inflation: The recent August 2023 US job market report showed wage increases (i.e., average hourly earnings) slowing down, potentially suggesting that US inflation pressures are easing. A weakening labour market will eventually weaken consumer spending and weigh further on aggregate demand. As such, disinflationary trends remain intact.

Monetary Policy: Weaker growth, softer aggregate demand and disinflationary trends in goods prices will likely lead to less hawkish outcomes in monetary policy. The Fed seemingly has a balancing act between curbing inflation (at the potential cost of high unemployment) or preventing much higher unemployment (at the potential cost of inflation running higher). Futures markets are currently pricing in little possibility of rate hikes from the Federal Open Market Committee following a cooler US labour market in August.

Key risks

Inflation: While core inflation in developed market countries is cooling, crude production cuts amidst dwindling inventories and higher food prices due to weather conditions could reignite inflationary fears.

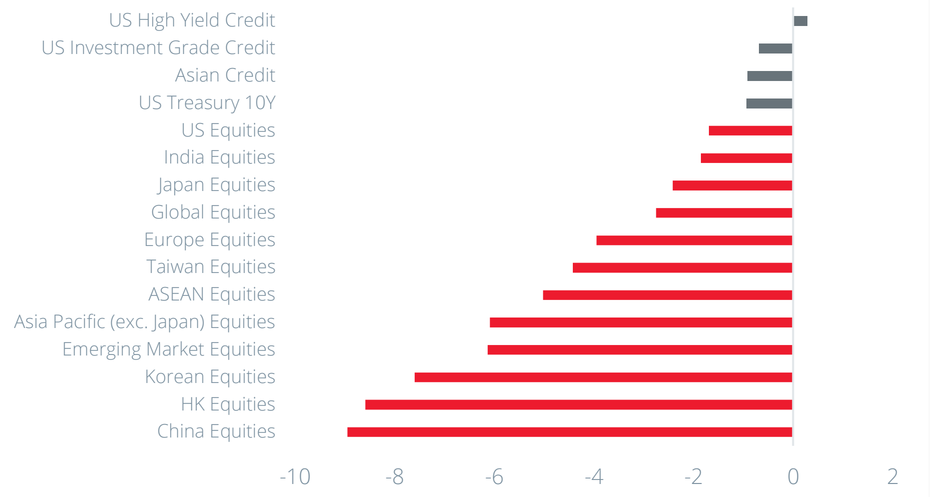
Geopolitics: Investor sentiment continue to be affected by rising political risks and social instability (e.g., tensions between China and the US, China and Taiwan).

US Growth: US consumers' propensity to spend remains relatively high, owing to previous fiscal support, a 3.5% household savings rate, and positive real income growth. This upside growth risk may challenge Eastspring's Multi Asset Portfolio Solution Team's 12-month outlook.

China Growth Slowdown: Despite positive signals from Chinese leaders/regulators since late 4Q22, there has been limited timely follow-through and implementation, which still warrants concerns for China macro risk. Further, China debt in real terms has effectively increased amid disinflationary backdrop.

Market update

% monthly total returns (in USD unless otherwise stated)*



Equities: Global equities declined in August as the Asian countries underperformed their developed markets. Declines were led by Hong Kong equities and Korean equities, whilst the US market was a relative outperformer although still in negative territory in absolute terms. Weak Chinese macro data, combined with renewed stress in the country's property market, weighed heavily on risk sentiment over the month. US equity sentiment has pulled back meaningfully, becoming less stretched.

Fixed Income: Investors digested the news that Fitch had downgraded the US government's credit rating to AA+. Although the Fitch announcement had a muted impact on 10-year US Treasury yields, they rose by 12 bps to end the month at 4.09%, as the month progressed on strong US economic data. The prospect of a default by Country Garden further weighed on sentiment during the month along with the news that China's Evergrande had filed for chapter 15 bankruptcy protection in New York.

*Refinitiv Datastream. As of 31 August 2023.

Asset class views

	3-month view			12-month view			Rationale
	Underweight	Neutral	Overweight	Underweight	Neutral	Overweight	
Equities			●	●			There is still scope for upside in near-term if positive trends persist: positive earnings beat and earnings revision, US equity sentiment becoming less stretched, etc. Fading fiscal impulse and weakening labor market to drive slowing growth and economic recession which in turn will likely drive equities lower over the medium-term.
10Y Government Bonds			●			●	As the US economy slows, markets will price in more rate cuts, driving a bull steepening of the US yield curve.
Corporate bonds			●	●			In line with the outlook for equities, corporate bonds still have scope to head higher in the near-term.
Cash		●				●	Positioning for risk-off assets over a 12-month time horizon keeps us overweight cash over the medium-term.
Equities							
US			●	●			Underweight US equities over the medium-term, driven by decelerating growth and as the impact of tighter monetary policy kicks in.
Europe			●	●			Weak Euro Area data (e.g., manufacturing) and restrictive ECB policy weigh on economic conditions; European equities are likely to drive lower over the next year, in line with recessionary trends.
Emerging Markets	●				●		Though partly driven by China macro data, EM equities (and their idiosyncratic profile) remain the bright spot over the medium-term as the global recession is driven by developed markets.
Asia Pacific ex-Japan	●				●		Asian equities may trade range-bound over the medium-term as global headwinds are offset by improving fundamentals in China.
Government Bonds							
US			●			●	As the US economy slows, markets will price in more rate cuts, driving a bull steepening of the US yield curve.
Europe			●		●		Europe growth remains at very low level and diverging from US, but not getting worse. Markets starting to price in ECB pause for the rest of the year, and rate cuts next year.
Singapore			●			●	With a narrowing growth forecast and easing inflation outlook, MAS does not seem likely to adjust its NEER policy. Current yield levels look attractive for investors to enter
Corporate Bonds							
US High Yield			●	●			The rating migration continues to be supportive in the short-term. However, despite relatively lower default rates, corporate refinancing risk may be underpriced as the maturity wall swells in the next few years.
US Investment Grade	●				●		Investment Grade credit may trade sideways as higher spreads are offset by lower base rates.
Emerging Markets			●		●		EM central banks have remained relatively dovish, which should help support overall EMBI spreads.
Asian Credit			●		●		As growth slows in the region (though not as much as in DM economies), corporate bond yields in Asia may remain better behaved relative to DM counterparts.
FX							
USD			●			●	The recessionary environment will generally drive investors to flock into safe-haven currencies, like the USD.
EUR	●			●			The persistence of weaker Eurozone data will likely weigh on the EUR/USD.
SGD		●			●		No discernible trend as Singapore's economic data looks mixed and SGD looks to be fairly valued at the moment.

Source: Asset class views are as of 4 September 2023, and should not be taken as a recommendation. The information provided herein is subject to change at the discretion of the Investment Manager without prior notice. Eastspring Multi Asset Portfolio Solutions Team.

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