

# Optimal Income Strategies

## Resilient Growth: U.S. Cools as EU and Asia Improve, Recession Risk Fades.

- Positive on global equities favouring developed markets.
- Staying constructive despite strong YTD performance.
- Started to progressively increase duration through short maturities.

### What's happening?

Global economic growth is expected to slow, prompting Central Banks to proceed with interest rate cuts mid-year.

US growth is expected to slow due to softer consumer spending. Consumer confidence and services surveys are also on a softening trend. Latest inflation in both headline and core surprised to the upside. While we expect disinflation to resume, service inflation may remain quite sticky. We edge our GDP growth forecast higher to +2.1% for 2024, then slowing to +1.5% in 2025.

Eurozone economic growth remains weak, particularly industrial, but there are some signs of services recovery, underpinned by recovering real wages. Disinflation has slowed. Headline inflation has come down, albeit not at the same pace across the board, while services inflation has proven stickier even if expected to gradually converge to the downside. We anticipate growth to remain anaemic at +0.3% in 2024 improving to +0.8% in 2025.

China exports and industrial activity improved at the start of 2024, but consumer spending remains subdued, weakened by continued property sector weakness. The PBoC left rates unchanged this month, although hinted at future RRR cuts. Altogether, we maintain a deceleration in GDP to +4.6% in 2024 and +4.2% in 2025.

Emerging markets exhibit heterogeneous trends. EM Asia has shown impressive growth, with inflation slowly coming off. Some central banks in EM Latam have accelerated their monetary policy easing recently. CEE weak growth led to some easing across the region already.

Market expectations for Central Banks are increasingly aligned with ours. US Fed expected to cut rates in June and has indicated 3 cuts this year. ECB is also likely to begin easing in June and looking for 3 cuts in total this year. BoE is also likely to cut rates in June. BoJ hiked rates for the first time in 17 years, ending 8 years of negative rates.

**Positioning & Performance:**

	GLOBAL OPTIMAL STRATEGY			OPTIMAL STRATEGY			DEFENSIVE OPTIMAL STRATEGY		
	Dec-23	Feb-24	Mar-24	Dec-23	Feb-24	Mar-24	Dec-23	Feb-24	Mar-24
<b>Net Equity</b>	<b>65,5%</b>	<b>75,9%</b>	<b>82,4%</b>	<b>54,1%</b>	<b>65,9%</b>	<b>70,7%</b>	<b>34,4%</b>	<b>35,0%</b>	<b>32,2%</b>
Equities	63,0%	74,2%	80,4%	60,0%	71,0%	72,5%	33,7%	39,0%	40,0%
Equities derivatives	8,6%	8,9%	8,4%	-0,8%	-1,4%	0,0%	0,7%	-4,0%	-7,8%
Risk Mitigation Strategies	-6,1%	-7,2%	-6,4%	-5,1%	-3,7%	-1,8%	0,0%	0,0%	0,0%
<b>Fixed Income</b>	<b>21,3%</b>	<b>17,6%</b>	<b>10,7%</b>	<b>33,5%</b>	<b>23,7%</b>	<b>21,1%</b>	<b>28,5%</b>	<b>29,0%</b>	<b>39,2%</b>
Govies	1,0%	0,5%	0,1%	1,0%	0,4%	0,0%	0,0%	0,0%	0,0%
Bond Derivatives	8,1%	27,8%	20,3%	9,4%	21,8%	19,5%	17,5%	21,9%	26,1%
High Yield Credit	1,2%	1,2%	1,2%	3,4%	3,2%	3,5%	10,5%	10,5%	14,6%
Investment Grade	17,3%	14,7%	9,0%	26,5%	18,9%	17,4%	17,9%	18,4%	24,6%
Emerging Debt	1,8%	1,2%	0,3%	2,6%	1,2%	0,2%	0,0%	0,0%	0,0%
<b>Diversification</b>	<b>3,4%</b>	<b>3,5%</b>	<b>3,4%</b>	<b>1,5%</b>	<b>1,0%</b>	<b>0,9%</b>	<b>5,6%</b>	<b>3,1%</b>	<b>2,3%</b>
<b>Cash &amp; Money Market</b>	<b>9,8%</b>	<b>3,0%</b>	<b>3,5%</b>	<b>10,7%</b>	<b>9,4%</b>	<b>7,3%</b>	<b>31,6%</b>	<b>33,0%</b>	<b>26,2%</b>

Economic activity has once again surprised on the upside in the United States, especially for the manufacturing sector thanks to increases in prices, demand, and production. Inflation, even if it remains on a downward trend. A soft-landing scenario accompanied by rate cuts around Q3 remains the baseline scenario, which continues to be a positive support for equity markets. The activity surveys in the euro zone started to improve.

Our portfolios are currently positioned with an overweight allocation to equities. It has been noted that the US market is the preferred option, with additional investments made in Japanese and Eurozone equity markets. Japan's structural story continues to hold promise, with several world-class leaders, particularly in the semiconductor sector, identified as offering attractive valuations. Similarly, Eurozone stocks have demonstrated strong performance and are poised for potential further growth, especially in light of indications of improved economic expansion, given their historically reasonable valuations.

A positive outlook is held for NASDAQ due to its exposure to favored themes such as AI, robotics, cybersecurity, and semiconductors, all of which contribute to its robust earnings potential.

Within other segments of our portfolios, an increase in duration has been initiated by focusing on Eurozone debt, specifically within the 5-year segment of the German yield curve. Additionally, a re-establishment of a steepener position on the US curve is being considered, anticipating a bullish steepening between 2-year and 10-year maturities as the Federal Reserve's rate cut approaches.

Regarding diversification strategies, an overweight position is maintained in USD (against GBP in this instance), and exposure to commodities (excluding agriculture and livestock) is retained. Support for these positions is derived from factors such as supply constraints, geopolitical risks, and increasing positioning.

## Outlook

Markets have continued to perform strongly, and we remain constructive in views of more upside. Sentiment is positive while positioning has risen but not overly, as many markets are flirting with all-time highs, including the US, Japan, India, Italy, Eurostoxx 50, Korea and the DAX. Whereas the initial leaders over the last 12 months were clearly the American Magnificent 7, boosted by the Artificial Intelligence theme, market is now differentiating between these companies, with Nvidia showing a 90% increase and Tesla down over 30%. Market breadth is expanding in the US, but not yet in Europe, where a significant portion of performance is coming from the 'Granolas', the European equivalent of the Mag 7. This is logical given their quality, cash flow generation, and earnings power, however more breadth expansion is needed to maintain confidence.

Some of the recent optimism was provided by Central Banks, especially from the Federal Reserve which decided to maintain rates at their March meeting. However, the median rate outlook continued to see 3 cuts for 2024, most likely starting in June, as for 2025. Growth expectations were raised for 2024 (end year 2.1%) and future growth nudging higher to 2%. Chairman Powell was confident that progress was being made on bringing inflation down, even though it might take a little longer. The economy's current 'soft landing' scenario seems well supported with better growth, stable unemployment and inflation slowly subsiding. On the other hand, the BoJ exited their negative interest rate policy and nudged rates to 0%-0,10% whilst also abandoning their yield curve control policy. The Swiss National Bank cut 25bp to ease pressure on the CHF, hampering the country's terms of trade. Regarding the ECB, we expect it to loosen policy sooner rather than later and perhaps even stealing a march on the Federal Reserve.

Moving back to equity markets, we now have more visibility on Central Bank policy whilst economic growth is relatively resilient, even in the Eurozone. The services sector is clearly doing much better than the manufacturing sector and with Chinese authorities injecting stimulus into their own economy, there is hope for recovery and increased export demand. A better growth/inflation mix and lower rates should continue to be a positive support for equities.

The earnings outlook is also improving and IBES consensus expects between 7-9% for the major developed markets in 2024 and 10-14% in 2025. This, combined with higher pay-out ratios and share buy backs, should support some further equity market gains. Although AI and its expanding eco-system remains a very powerful thematic there are plenty of others including defence, onshoring, GLP-1 (obesity drugs), cyber security and climate related.

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