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Optimal Income Strategies

Markets Pause After a Strong Ten-Month Rally

- Fed policy shifts and AI valuation risks drive market Moves
- Hopes for peace in Ukraine crept higher as the US backed a peace framework
- Diversification matters as concentrated single-theme bets face rising risks

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What's happening?

Looking for Normalisation, there are emerging signs that the White House is moving away from policy radicalism. Recent concessions to China aimed at maintaining the trade truce, along with new tariff exemptions on basic goods such as coffee, indicate that the U.S. administration acknowledges the negative impact of the trade war on consumer purchasing power—though this shift remains tentative.

In the U.S., job creation rebounded above expectations in September, but downward revisions to previous months reveal a slowdown following April's tariff announcements. The unemployment rate climbed to 4.4%, its highest level since October 2021, while dovish comments from the Federal Reserve offered some market relief, leaving a December rate cut uncertain.

In the Eurozone, GDP growth accelerated to 0.2% quarter-on-quarter in Q3, with underlying data painting a more optimistic picture. Persistent services inflation and reduced downside risks have closed the door on near-term ECB cuts, though we still anticipate one final reduction in March 2026 as headline inflation bottoms out and downside risks re-emerge.

Meanwhile, China's growth momentum weakened in October, with fixed asset investment posting its sharpest decline since the pandemic—down 11.4% year-on-year—amid continued weakness in manufacturing and infrastructure. Although fiscal support announced in late October has yet to materialize in the data, we expect improvement in the coming months.

Looking ahead, central banks are likely to adjust policy gradually: the Fed is expected to deliver a series of insurance cuts, lowering rates to 3.0% by Q3 2026; the ECB may cut once more to 1.75% in March 2026; the Bank of England's rate could fall to 3.5% by year-end 2026; and the Bank of Japan is projected to hike to 0.75% in January, supported by a positive domestic outlook.



Portfolio positioning and performance

| | GLOBAL OPTIMAL STRATEGY | | | OPTIMAL STRATEGY | | | DEFENSIVE OPTIMAL STRATEGY | | |
|--------------------------------|-------------------------|---------------|---------------|------------------|---------------|---------------|----------------------------|--------------|--------------|
| | Dec-24 | Oct-25 | Nov-25 | Dec-24 | Oct-25 | Nov-25 | Dec-24 | Oct-25 | Nov-25 |
| Net Equity | 87,9% | 97,9% | 99,7% | 76,3% | 82,4% | 89,3% | 34,6% | 44,5% | 43,7% |
| Equities | 79,7% | 71,4% | 73,2% | 72,9% | 66,8% | 66,3% | 37,0% | 36,5% | 36,4% |
| Equities derivatives | 13,9% | 30,2% | 27,9% | 5,2% | 18,9% | 23,2% | -2,4% | 8,0% | 7,3% |
| Risk Mitigation Strategies | -5,7% | -3,7% | -1,4% | -1,8% | -3,3% | -0,2% | 0,0% | 0,0% | 0,0% |
| Fixed Income | 5,0% | 13,0% | 13,2% | 23,6% | 25,1% | 25,6% | 62,9% | 57,4% | 53,6% |
| Govies | 0,0% | 0,0% | 0,0% | 0,0% | 0,0% | 0,0% | 0,2% | 0,3% | 0,3% |
| Bond Derivatives | 45,0% | 12,4% | 10,8% | 27,4% | 8,9% | 8,8% | 10,4% | 3,0% | 1,7% |
| High Yield Credit | 1,0% | 2,3% | 2,0% | 5,6% | 4,6% | 4,8% | 16,3% | 21,0% | 18,5% |
| Investment Grade | 3,9% | 10,3% | 10,9% | 17,6% | 20,4% | 20,7% | 46,0% | 34,8% | 33,6% |
| Emerging Debt | 0,1% | 0,4% | 0,3% | 0,3% | 0,2% | 0,2% | 0,5% | 1,3% | 1,2% |
| Diversification | 11,6% | 6,4% | 8,3% | 2,2% | 2,6% | 2,2% | 5,9% | 4,0% | 6,4% |
| Cash & Money Market | -4,4% | -17,2% | -21,2% | -1,9% | -10,1% | -17,1% | -3,4% | -6,0% | -3,7% |

Global equities remain firmly overweight, with positioning looking beyond recent volatility. Stress from credit markets—driven by fraudulent behaviour and poor oversight—was previously assessed as insufficient to alter our positive outlook for risk, and that view remains unchanged. The end of the U.S. government shutdown adds support by reducing near-term uncertainty and improving liquidity conditions.

Equity allocation continues to be diversified, with conviction in AI-driven momentum within the S&P 500 intact. Utilities benefit from grid modernization and easing rates, while Oil & Gas majors face persistent headwinds from weak supply-demand dynamics. We maintain exposure to defensive names alongside selective healthcare positions, which delivered a notable rebound this month. In Europe, EU banks present compelling value, while in China, technology stands to gain from renewed domestic stimulus aligned with strategic innovation priorities.

Short-dated German bonds are held as a hedge against credit stress and systemic risk. Sovereign curves have flattened as investors seek safety, and the ECB's hawkish stance appears increasingly misaligned with soft exports, strong currency, and subdued energy prices. The Eurozone also faces risks from U.S.-China tensions, with weaker exports and deflationary imports redirected from China.

Exposure to copper and uranium stocks is maintained, reflecting a constructive view on industrial metals. Sustained demand from electrification, infrastructure development, and AI-linked data centres provides strategic access to long-term structural growth trends.

Outlook

Global investor attention has shifted from idiosyncratic issues in credit markets—despite persistent concerns around private credit highlighted in the financial press—to the outlook for Federal Reserve policy following the end of the U.S. government shutdown. The conclusion of 40 days of uncertainty is broadly positive for policy and market sentiment, albeit with one caveat: limited fresh labour market data ahead of the December Fed meeting. Several Board members have signalled the need for pragmatism and additional time before voting on another Fed Funds rate cut. Available data remains reassuring, showing a softening labour market trend without significant deterioration during the shutdown. If a December cut is delayed, January appears likely, as the Fed prioritizes credibility and stability in the U.S. dollar and Treasury markets. Importantly, investors should not interpret this as a reversal of the Fed's commitment to the three near-term insurance cuts outlined in September.

The backdrop remains supportive for risk assets. Earnings season delivered strong results across the U.S. and Europe, while policy accommodation from the Fed appears only delayed, not derailed. Limited macro data, complemented by alternative sources, shows no signs of slowing activity, with the Atlanta Fed's GDP Nowcast hovering near 4% annualized. In Europe, survey data has held firm despite lingering deflationary risks in core economies.

Investor positioning adds further support. Discretionary allocations remain below long-term equity norms, while systematic positioning—previously stretched—has begun to normalize, which should prove constructive over time. Near-term, cross-market volatility needs to subside, but structurally, our machine-learning Bull/Bear model continues to signal a bull market, intact since the U.S. policy pivot in late April.

Crypto market turbulence may have amplified recent risk aversion. Bitcoin's sharp correction (-33% from early October to late November) and weakness across other digital assets likely reduced retail buying power in equities. While institutional exposure remains minimal (0.4% of cash per BoA's November survey), U.S. retail investors are more heavily involved, and flow data confirms their seasonal absence. Encouragingly, retail-favoured momentum stocks appear to have bottomed at depressed levels, consistent with prior recovery patterns this year.

Credit markets remain resilient, reinforcing a neutral stance. Despite recent equity volatility and last month's focus on issuer-specific challenges, investment-grade CDS spreads have resisted widening. Issuance from AI corporates seeking infrastructure funding has surged, but cash-rich balance sheets suggest these firms are not driving stress or risk aversion. In summary, the combination of easier monetary policy, steady economic growth, enthusiasm for AI-driven infrastructure and productivity gains, ongoing fiscal stimulus in Germany, Japan, and China, and robust corporate earnings—even amid negative reactions to strong results from names like Nvidia—continues to underpin a constructive outlook for risk assets into 2026.

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