

Asset Allocation

FED'S REACTION FUNCTION TO BENEFIT BOTH STOCKS AND BONDS

Andrea Cicione

MULTI ASSET We expect the Fed to prioritize full employment over price stability and to ease at the first sign of labour market weakness in 2024. This should help the US avoid recession next year.

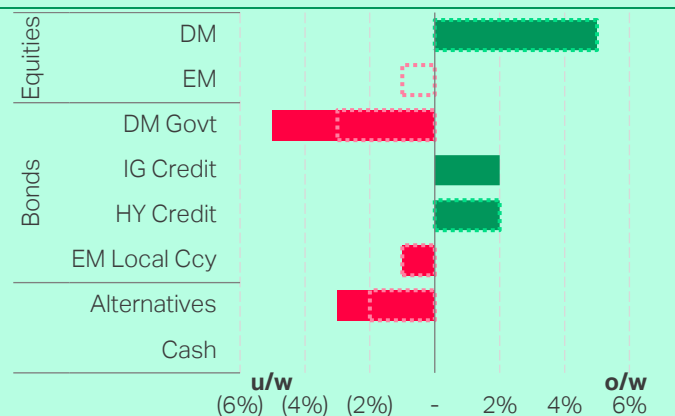
A more dovish Fed (and earnings that appear to have bottomed) should boost equities, but bonds stand to benefit too. This makes duration more appealing, but the sweet spot is in IG credit rather than govies.

The shift in the Fed reaction function means that headwinds for EMs this year are likely to weaken. This, coupled with the encouraging outlook for profits, warrants a more constructive view on EM equities.

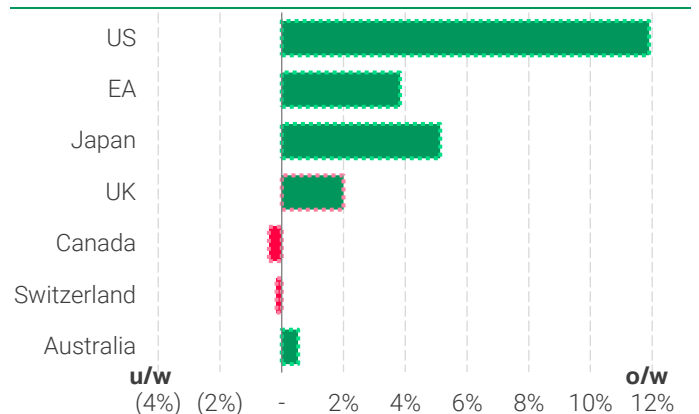
ASSET ALLOCATION We increase our pro-risk asset allocation stance further this month, adding to EM Equities at the expense of Energy Commodities. In Fixed Income, we rotate from Government Bonds to IG Corporate Bonds. **Our portfolio beta increases somewhat to 1.05 from 1.03.**

MACRO OUTLOOK High-frequency data continue to point to a world economy that is holding up but short of impetus. Disinflation in 2024 will reflect weak growth rather than being the "immaculate" variety. While the US may be headed for a soft landing, in Europe, downside economic surprises continue to dominate.

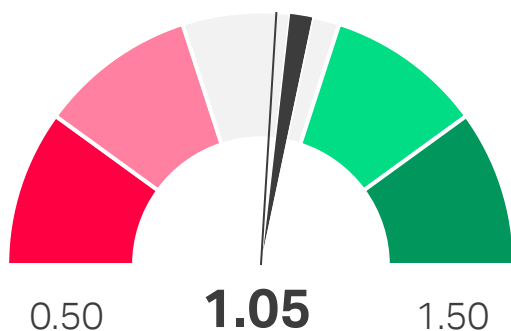
Global asset allocation*



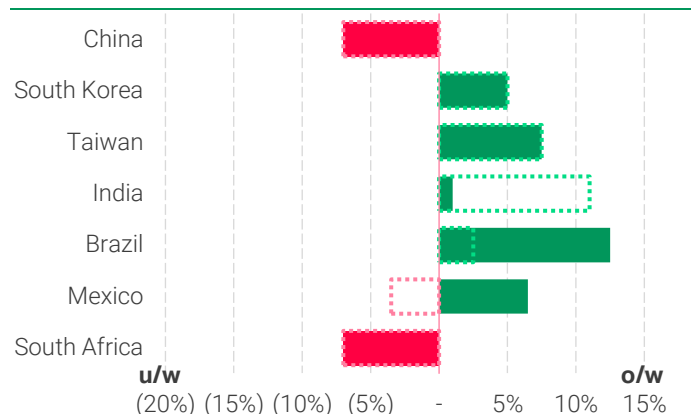
DM Equities asset allocation*



Model portfolio beta vs benchmark



EM Equities asset allocation*



Thin line represents last month's beta

(*) Dotted lines represent last month's allocation

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ASSET ALLOCATION

3 to 6-month view. Previous ratings in brackets. Monetary policy outlook changes in bold. Rationale on next page.

	Equities	Govt Bonds	FX vs. USD	Monetary policy
Developed Markets				
North America				
US	+1	0		Quicker to cut, unlikely to hike
Canada	0	0	+1	Cuts in 2024
Developed Europe				
UK	0	+1	0	Rates on hold, active QT
Switzerland	0		-1	Long pause
Euro Area				
Germany	0	+1		
France	0	+1		
Italy	0	0		
Spain	0	0		
Asia Pacific				
Japan	+1	-1	-1 (0)	Policy normalization under Ueda
Australia	0	0	+1	Higher for longer
Emerging Markets				
Asia				
China	0	0	0	10bps cut to rate corridor
India	0 (+1)	0	0	On hold at least until Feb-24
Korea	+1	0	0 (-1)	Unchanged
Taiwan	+1	0	0	Unchanged
Latin America				
Brazil	+1 (0)	+1 (0)	+1 (0)	50bp cut in Dec, 11.75% end-2023
Mexico	+1 (-1)	0 (-1)	0	Easing to start in Q2 2024
Europe & Africa				
South Africa	-1	-1	-1	On hold

Alternative Assets	
Real Estate	-1
Energy Commodities	0 (+1)
Industrial Metals	0
Precious Metals	-1 (0)

Corporate Bonds		IG	HY
US		+1	+1
UK		+1	
Euro Area		+1	+1

Key to recommendations				
+2 = strongly positive	+1 = positive	0 = neutral	-1 = negative	-2 = strongly negative
Recommendations based on expectations of normalized local-currency total returns . FX returns include carry .				
Model portfolio on p. 11.				

Summary of key recommendation changes

	From	To	Rationale
India Equities	+1	0	Markets lack new impetus amid lagging private-sector revival, weak consumer sentiment and food price risks. However, India remains a safe haven among EM economies as it has comparatively little exposure to the US economy. Cheaper oil is another positive.
Brazil Equities	0	+1	The tax reform bill was approved in the Senate earlier this month, bringing it closer to being signed into law. The reform is far from ideal but will nonetheless simplify the current byzantine system and should still have a positive impact on GDP and productivity.
Mexico Equities	-1	+1	Nearshoring momentum and the prospect of lower interest rates next year will drive markets supported by a relatively robust US economy.
Brazil Government Bonds	0	+1	MoPo easing from a high policy rate provides sizeable carry and capital appreciation; the inflation outlook is favourable.
Mexico Government Bonds	-1	0	Interest rates will remain high into 2024, but monetary easing will begin in the second quarter.
Energy Commodities	+1	0	Crude failed to react meaningfully to risks in the Middle East, and NatGas prices are likely to be capped owing to large stockpiles and a mild start to the winter.
Precious Metals	0	-1	Lower yields are a plus for Precious Metals, but a large gap remains between real yields and gold price. As central bank purchases slow, there could be significant downside.
JPY vs USD	0	-1	Yields are the fundamental driver of the yen and very slow moving BoJ normalization will not save the currency.
KRW vs USD	-1	0	The semiconductor cycle is beginning to turn more positive, providing a tailwind for exports; rate differentials will improve as the BoK maintains hawkishness.
BRL vs USD	0	+1	Tax reform has a positive impact on GDP and productivity; high interest rates provide further support.

Summary of model portfolio changes

	1-month chg	O/W (U/W)	Comments
EM Equities	+1%	-	We add 1% each to Brazil and Mexico and cut India by 1%.
Government Bonds	-2%	(5%)	We reduce US and Canada bonds by 1% each.
IG Corporate Bonds	+2%	2%	We add 2% to US IG Credit and go overweight.
Alternative Assets	-1%	(3%)	We cut Energy by 1% to a small underweight.

Full model portfolio composition and performance from [p. 11](#).

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MULTI ASSET

Andrea Cicione

- The global economy will decelerate further, but the US should avoid recession in 2024
- US earnings have bottomed; this, together with easier policy, should support equities
- It is too early for overweight duration, but IG looks appealing again while HY remains so

Go to Asset Allocation and portfolio changes

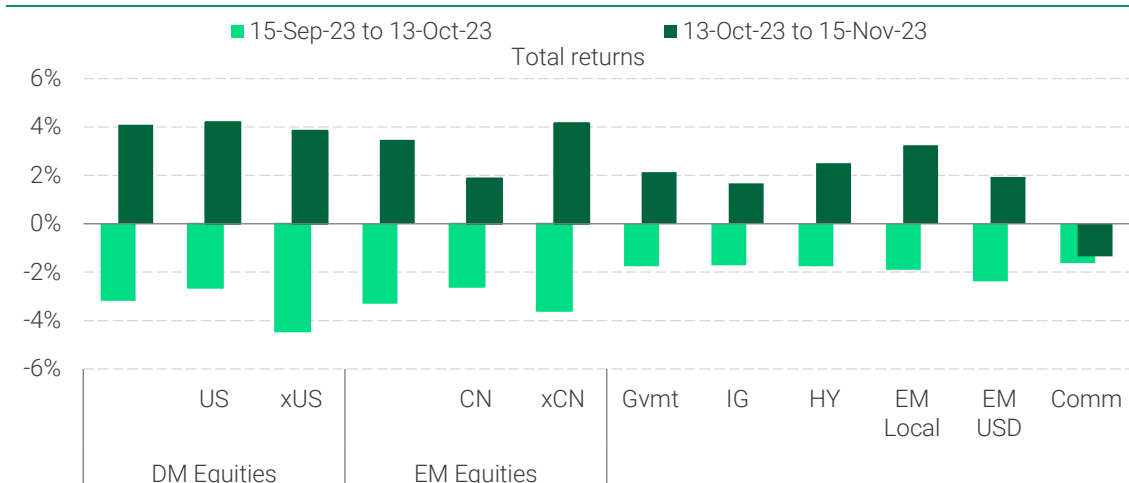
Chances of a US recession are getting slimmer. Inflation continues to surprise to the downside, even in the US, where growth remains more resilient than elsewhere. The global economy continues to decelerate, but we think that the US should avoid recession in 2024. We see GDP bottoming out in H2 at positive levels and unemployment peaking at the same time at around 4.5%. As long as inflation remains below 4.5%, the Fed will prioritize full employment over price stability and will ease at the first sign of labour market weakness.

US earnings have bottomed and the EM ex-China trend is positive, too. Corporate earnings appear to have bottomed in the US. This, coupled with what is likely to be easier monetary policy, should support equities. The trend for profits is a lot less clear in other DMs, and we retain a US bias in stocks. The outlook for EM earnings is more positive, especially beyond China.

IG Credit is the best way to add duration. We argued last month that UST 10y yields in the 4.50-5.00% range are close to fair value as they are consistent with the Fed’s dot-plot median expectations. We continue to think that risk for yields is skewed to the downside, which warrants a more positive view on duration. However, with the growth outlook improving too, we believe the best way to get duration exposure is via IG Credit.

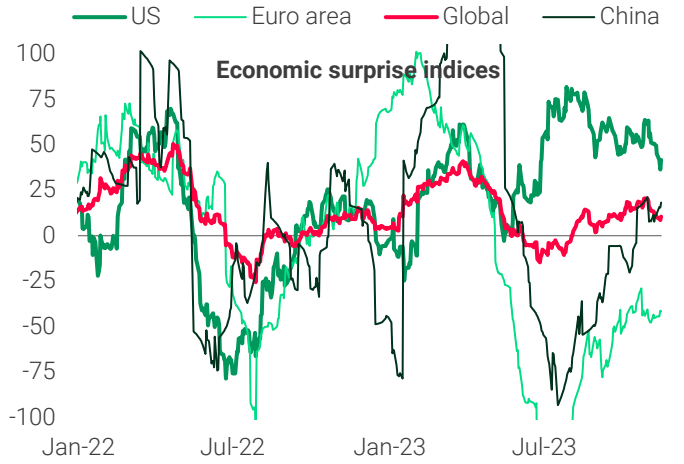
We add EM Equities and IG Credit. We rotate from DM Government Bonds to IG Corporate Bonds and we add to EM Equities at the expense of Energy commodities. **Our portfolio beta climbs to 1.05 from 1.03.**

All asset classes – except Commodities – posted positive returns in the past month



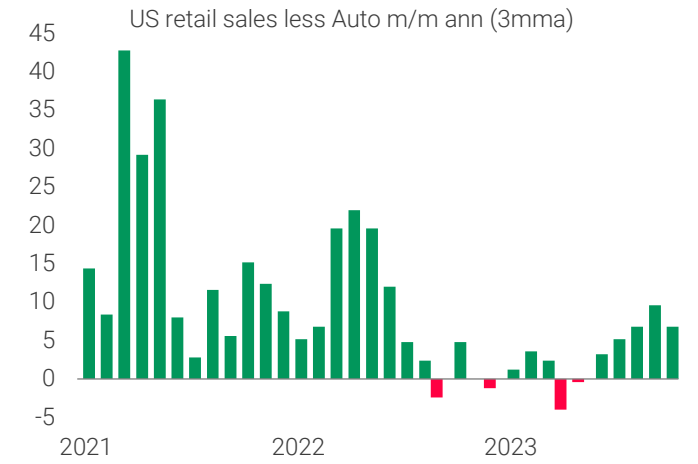
Sources: Bloomberg, GlobalData TS Lombard.

Chinese surprises are back to positive



Sources: Citi, Bloomberg.

US consumer demand remains solid



Sources: Bloomberg, GlobalData TS Lombard.

US soft landing in H1 2024 likely

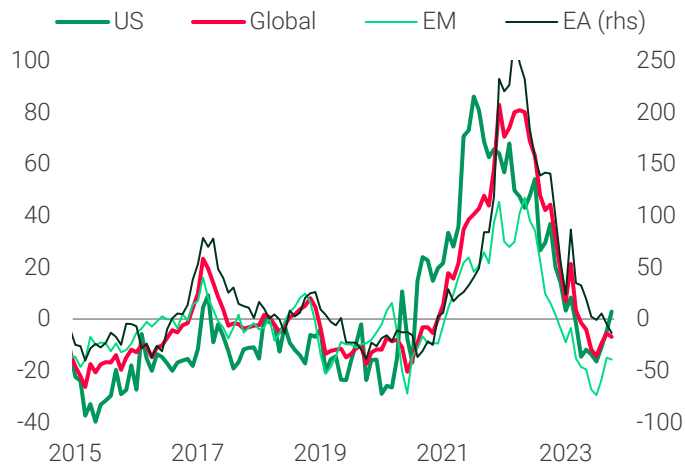
No US recession in 2024. A US recession in 2024 is becoming increasingly unlikely. While there is still a recessionary process in place – the result of the cumulative tightening of the past two years – recent communications by Fed officials suggest that their bias is shifting from fighting inflation come what may to making sure a recession does not happen.

Fed will try to be invisible. Since 2024 is an election year, we believe the Fed will want to do whatever it takes to avoid shouldering the blame for a possible recession caused by policy overtightening. As long as inflation stays below 4.5%, the FOMC will cut rates at the first sign of economic weakness, acting pre-emptively to try to keep people in jobs.

US GDP to bottom in Q1 or Q2 2024. While this is no guarantee that a recession will be avoided, a soft landing is our central case. We see US growth bottoming out at about 0.5% q/q annualized in Q1 or Q2 2024 and unemployment peaking at about 4.5% at the same time.

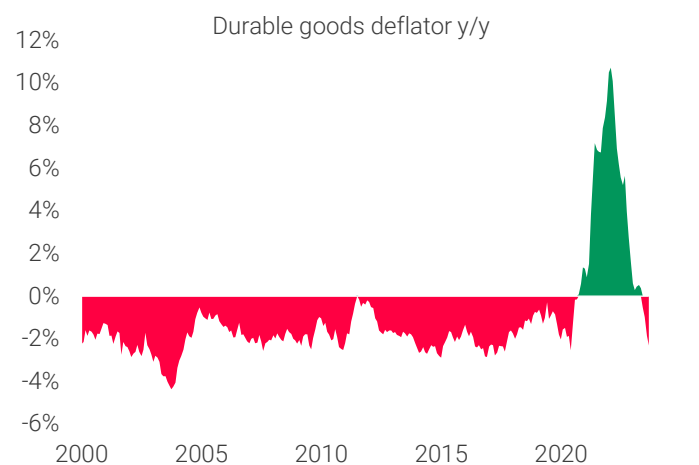
Inflation surprises are gravitating towards zero. Consensus is adjusting to a benign inflation surprise, but the disinflationary trend remains well entrenched. With the global economy likely to decelerate through H1 2024, this is unlikely to change for now.

Inflation surprise gravitating back towards zero



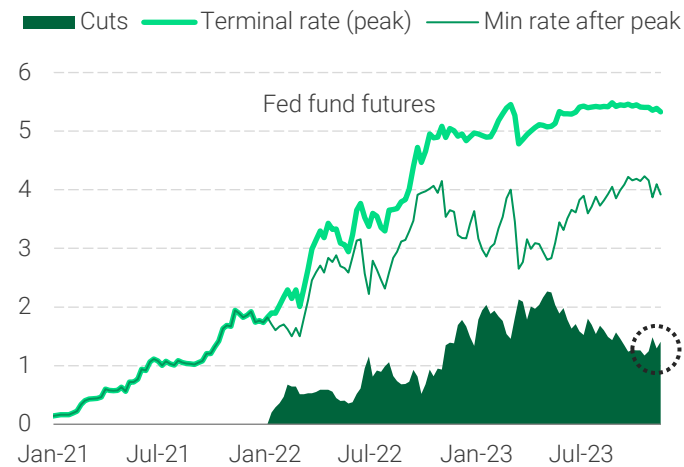
Source: Bloomberg.

Durable goods inflation spike is over



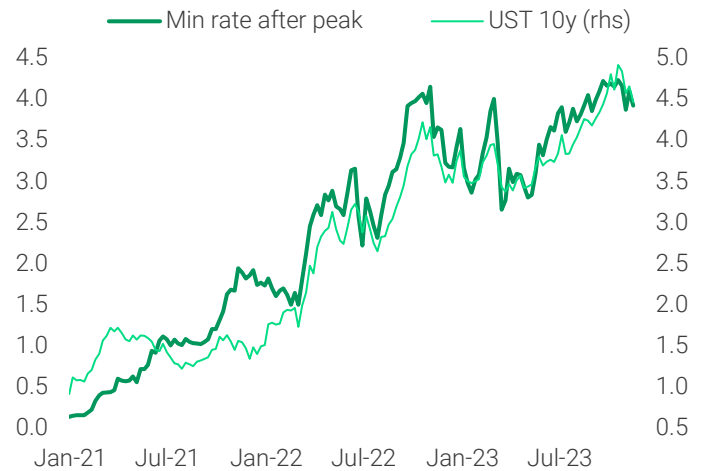
Source: Bloomberg.

Market is pricing in more than four cuts in 2024



Sources: OECD, Bloomberg, GlobalData TS Lombard.

UST 10y keeps tracking Fed policy expectations



Sources: Bloomberg, GlobalData TS Lombard.

UST yields slightly below fair value

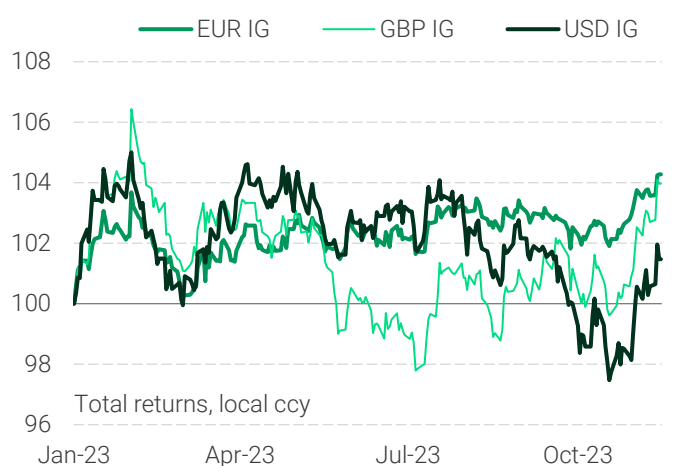
Fair value for UST 10y in the 4.50-5.00% range. We argued last month that a fair value estimate for UST 10y yields based on the Fed dot-plot median estimates is around 4.75%. As FOMC forecasts for the policy path have not changed since then, that estimate remains valid.

However, we continue to think that risk is skewed to the downside for yields – for two reasons. First, the Fed communication has since turned more dovish. Second, our fair value incorporates a generous dose of term premium (about two percentage points). Although this is consistent with the pre-2015 norm, it clashes with recent evidence of a term premium close to zero.

This warrants a more positive view on duration. However, with yields below the bottom end of our fair value range and with rate markets already pricing in more than four Fed cuts by January 2025, we do not feel the time is right to go overweight just now. For this reason, we keep our Fixed Income allocation unchanged – at a small underweight.

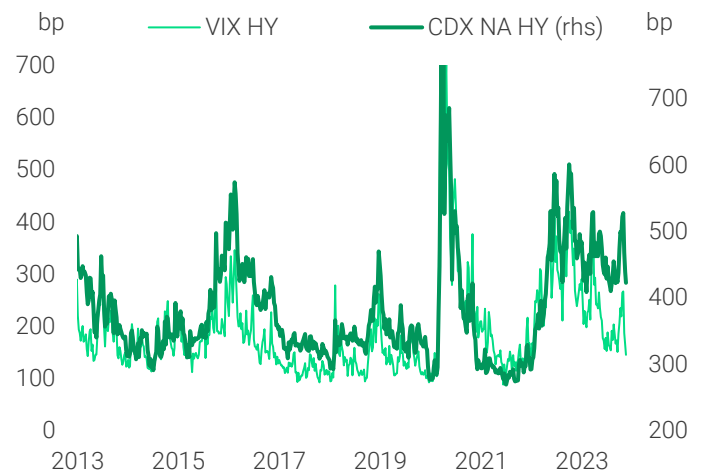
IG Credit is the best way to add duration risk. Since the most likely sustained move for yields remains to the downside and given the more benign outlook for the US economy, we believe the best way to add duration exposure is via IG credit. Risk compensation also remains generous in HY: we go back overweight IG and stay overweight HY.

IG ytd total returns back to positive, even in US



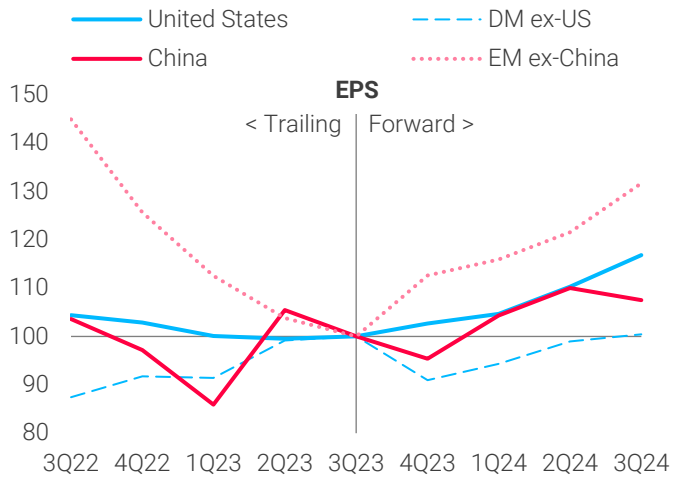
Sources: GlobalData TS Lombard, Bloomberg.

HY spreads wide for level of market volatility



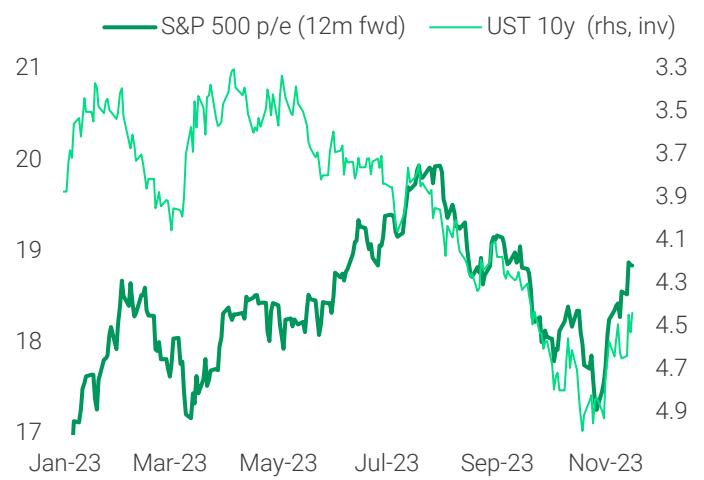
Sources: GlobalData TS Lombard, Bloomberg.

Earnings have bottomed in US and EM ex-China



Source: Bloomberg.

Yields (hence Fed) are main p/e driver



Sources: Bloomberg, GlobalData TS Lombard.

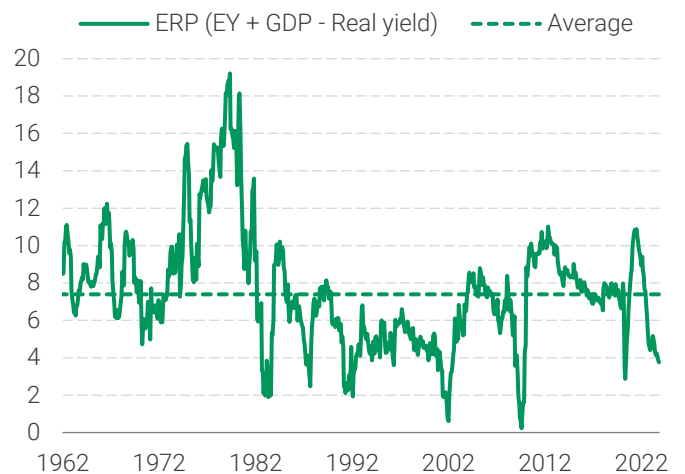
US earnings recession over, EM outlook positive, too

US earnings are expected to start climbing again. US earnings have stagnated for the past two years. With profits flat, the main performance driver for US equities has been rates and yields, which has affected valuations. The good news is that earnings are finally projected to start climbing in Q4 2023 and beyond, as profit margins appear to be stabilizing at healthy levels.

But there is poor risk compensation in US equities. With the earnings outlook turning positive and rates likely to remain supportive rather than be a hinderance, we stay positive on US Equities. However, valuations remain significantly above the historical average, both in absolute terms and compared with bonds (chart below left). Because of the poor risk compensation, we keep our US model portfolio overweight unchanged.

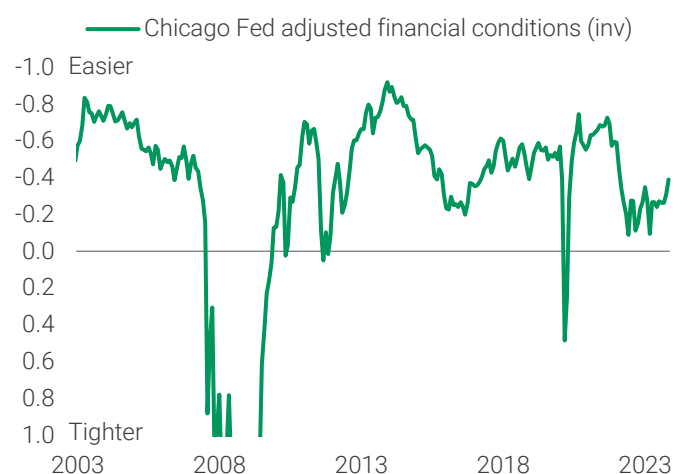
We rotate from EM leaders to laggards. In other DMs, the earnings outlook is still stagnation, in line with economic growth. But in EM the expected profit trajectory is more appealing. This, coupled with easier financial conditions and a softer dollar, should allow EM assets to continue to recover. We rotate from leader India to laggards Brazil and Mexico and go to benchmark weight overall. We keep a small underweight in China.

ERP continues to wither



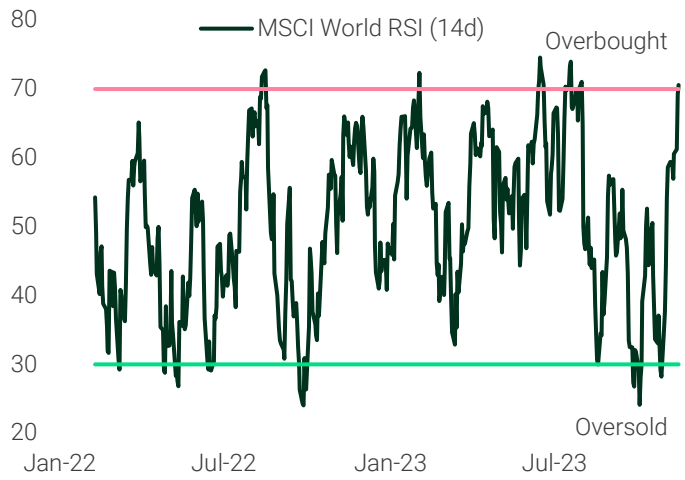
Sources: Bloomberg, GlobalData TS Lombard.

Financial conditions easing



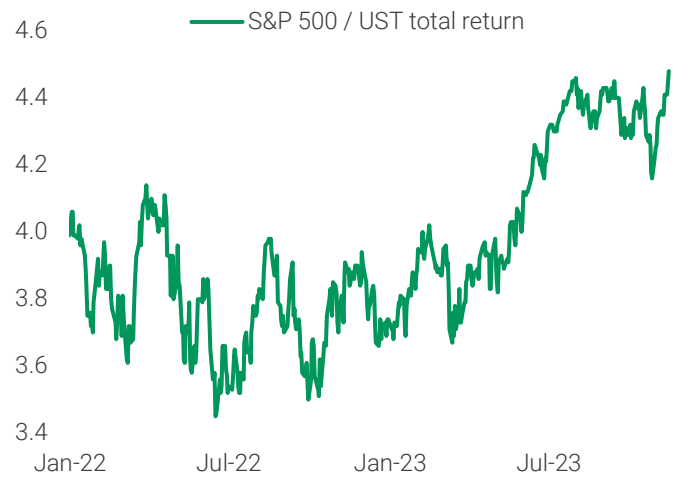
Sources: Bloomberg, GlobalData TS Lombard.

Equities are overbought



Sources: Bloomberg, GlobalData TS Lombard.

Equities outperformance of bonds resumes



Sources: Bloomberg, GlobalData TS Lombard.

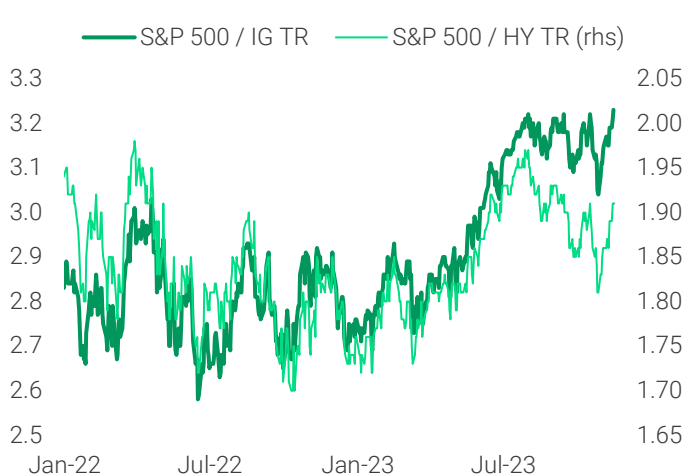
Asset allocation and portfolio changes

We go benchmark-weight EM Equities. With the likelihood of a US recession further decreasing, we retain a relatively pro-risk asset allocation this month. However, since the global economy looks set to continue slowing for another two to three quarters, four Fed cuts are already priced in and stocks are overbought, we add only marginally to equities and go benchmark-weight in EM.

Both equities and bonds are set to benefit from easier Fed stance. Equities are not the only asset class likely to benefit from a more dovish Fed; bonds should do so as well. A historically low equity risk premium suggests risk compensation is more generous in bonds than stocks. But since we expect the US to avoid recession in 2024, we think the best way to add duration is in IG Credit, where spreads compensate investors nicely for market and recession risks.

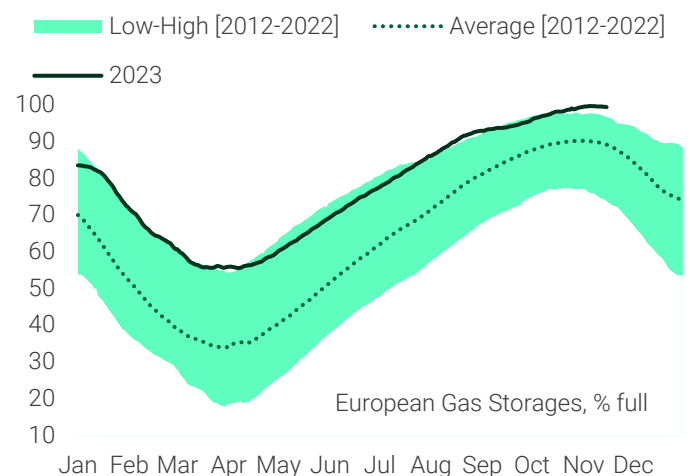
We cut Energy Commodities to 0 and go slightly underweight. To make room for more EM equities in our portfolio, we cut Energy Commodities to a small underweight. Crude failed to react meaningfully to risks in the Middle East, and NatGas prices are likely to be capped owing to large stockpiles and a mild start to the winter.

HY is still faring better than IG relative to equities



Sources: Bloomberg, GlobalData TS Lombard.

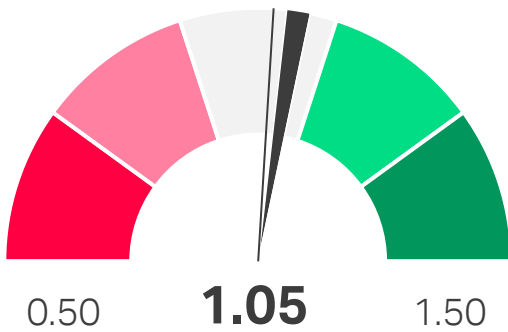
Natural gas storage is at its fullest in a decade



Sources: Bloomberg, GlobalData TS Lombard.

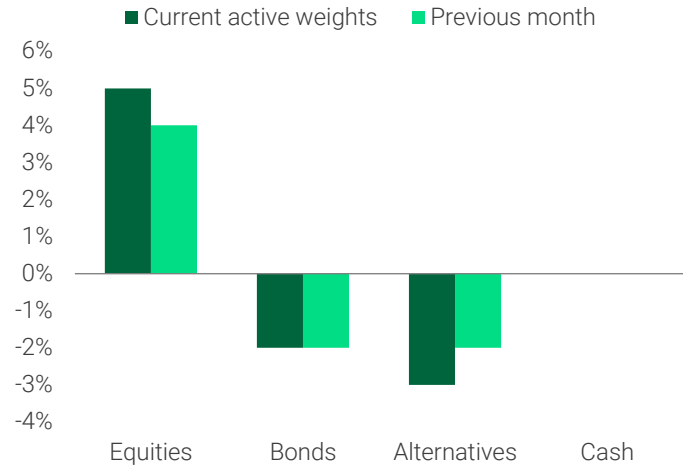
Our model portfolio beta increases slightly to 1.05 from 1.03 last month.

Model portfolio beta to benchmark



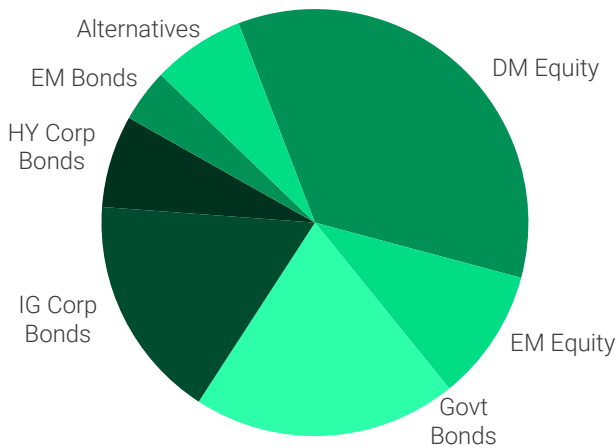
Source: GlobalData TS Lombard. Thin line = last month

Model portfolio changes



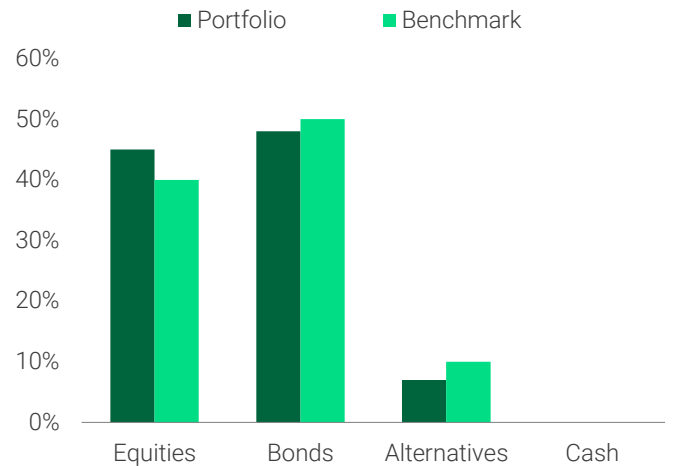
Source: GlobalData TS Lombard.

Model portfolio composition



Source: GlobalData TS Lombard.

Model portfolio vs benchmark



Source: GlobalData TS Lombard.

Multi Asset dashboard

	Total Return LC			Volatility			Sharpe Ratio			1Y Correlation			3Y Beta		
	1y	3y	5y	1y	3y	5y	1y	3y	5y	LI	Infl.	Rates	LI	Infl.	Rates
DM Equities	12.8	8.6	10.3	11.7	14.4	17.7	0.7	0.5	0.5	33.3	3.3	-39.7	5.9	0.5	-5.5
EM Equities	5.5	-1.3	4.4	11.5	14.2	15.0	0.0	-0.2	0.2	34.3	26.5	-45.3	5.3	3.9	-5.8
DM Govt Bonds	0.7	-6.6	-1.1	6.8	6.1	5.6	-0.6	-1.4	-0.5	29.7	0.0	-76.9	2.5	0.0	-5.5
DM Corp Bonds	2.4	-5.8	1.6	9.5	8.8	8.7	-0.3	-0.9	0.0	22.6	-9.0	-71.6	2.4	-0.9	-6.5
EM Bonds	10.4	-2.6	1.9	6.2	6.6	6.8	0.9	-0.7	0.0	21.8	-1.9	-55.2	2.1	-0.2	-4.6
Energy	-6.5	39.6	5.3	30.2	34.5	42.4	-0.4	1.1	0.1	15.9	15.2	2.5	5.3	4.8	0.7
Industrial Metals	-8.1	5.8	4.6	17.6	20.8	18.3	-0.7	0.2	0.2	34.2	6.1	-26.7	7.7	1.3	-4.9
Precious Metals	10.0	0.4	8.8	14.1	15.5	16.6	0.4	-0.1	0.4	13.6	14.8	-41.2	2.2	2.4	-5.7
DM Currencies	4.8	-9.2	-5.4	7.1	7.1	6.5	0.0	-1.6	-1.1	21.0	3.3	-58.0	1.8	0.3	-3.9
EM Currencies	-51.7	-54.0	-52.7	54.8	31.8	24.8	-1.0	-1.8	-2.2	27.8	16.2	14.8	1.4	5.6	4.4

All figures % except 3Y Beta.

MODEL PORTFOLIO

Andrea Cicione

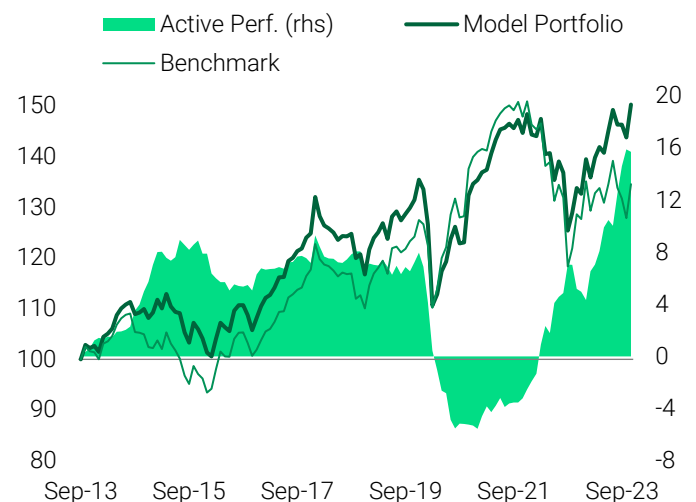
- We increase our Equity exposure at the expense of Commodities, adding to EM
- In Fixed Income, we rotate from Government Bonds to IG Corporate Bonds
- Our portfolio beta nudges up to 1.05 from 1.03
- **We add to EM equities.** We increase our overall Equity overweight by adding to EM Equities. We do so by reducing India by 1%, while raising Brazil's and Mexico's portfolio weight by 1% each.
- **We rotate from Government to Corporate Bonds.** We reduce DM Government Bonds by 2% to a 5% underweight by cutting US and Canada Bonds by 1% each. We move the weight to US IG Corporate Bonds, thereby returning to overweight. We are now 2% overweight IG and remain 2% overweight HY.
- **We cut Alternatives further.** This month we go further underweight Alternative Assets by cutting Energy Commodities by 1% to a small underweight. We are now underweight both Real Estate and Commodities.
- **We hedge half our JPY exposure.** We add a 3% hedge to JPY – half of our 6% portfolio exposure. As a result, we are 4% underweight JPY vs the benchmark.
- **Our model portfolio beta increases to 1.05 from 1.03.**

Model portfolio statistics

	Model Portfolio	Benchmark
Returns (since Sep-13)	50.3%	34.6%
YTD	13.3%	5.4%
2022	-10.6%	-15.4%
2021	10.2%	7.8%
Annualized return	4.1%	3.0%
Volatility	9.2%	9.6%
Sharpe Ratio	0.38	0.25
Sortino Ratio	0.69	0.49
Beta	0.92	
Alpha	1.4%	
Tracking error vol	2.6%	
Information ratio	0.44	

Sources: Bloomberg, GlobalData TS Lombard.

Model portfolio performance



Sources: Bloomberg, GlobalData TS Lombard.

	Portfolio	Benchmark	O/W (U/W)	1m change
DM Equities	35%	30%	5%	-
US	21%	17.4%	3.6%	-
Canada	1%	1.1%	(0.1%)	-
UK	3%	2.4%	0.6%	-
Switzerland	1%	1.1%	(0.1%)	-
Germany	1%	1.1%	(0.1%)	-
France	1%	1.1%	(0.1%)	-
Italy	1%	0.3%	0.7%	-
Spain	1%	0.4%	0.6%	-
Japan	4%	2.5%	1.5%	-
Australia	1%	0.8%	0.2%	-
Others	-	1.8%	(1.8%)	-
EM Equities	10%	10%	-	+1%
China	2%	2.7%	(0.7%)	-
South Korea	2%	1.5%	0.5%	-
Taiwan	2%	1.3%	0.8%	-
India	1%	0.9%	0.1%	-1%
Brazil	2%	0.8%	1.3%	+1%
Mexico	1%	0.4%	0.7%	+1%
South Africa	-	0.7%	(0.7%)	-
Others	-	1.9%	(1.9%)	-
Government Bonds	20%	25%	(5%)	-2%
USTs	8%	10.0%	(2.0%)	-1%
Canada	-	0.4%	(0.4%)	-1%
Bunds	2%	1.7%	0.4%	-
Gilts	3%	2.1%	1.0%	-
JGBs	2%	4.4%	(2.4%)	-
OATs	2%	1.9%	0.1%	-
BTPs	2%	1.9%	0.1%	-
BONOs	1%	1.0%	0.0%	-
Australia	-	0.4%	(0.4%)	-
Others	-	1.4%	(1.4%)	-
IG Corporate Bonds	17%	15%	2%	+2%
US	11%	8.6%	2.5%	+2%
EA	4%	3.0%	1.0%	-
UK	2%	1.1%	1.0%	-
Others	-	2.4%	(2.4%)	-
HY Corporate Bonds	7%	5%	2%	-
US	4%	2.8%	1.3%	-
EA	3%	0.9%	2.1%	-
Others	-	1.3%	(1.3%)	-
EM Bonds	4%	5%	(1%)	-
China	1%	1.0%	-	-
Brazil	1%	0.5%	0.5%	-
Mexico	-	0.5%	(0.5%)	-
India	1%	0.5%	0.5%	-
Taiwan	-	0.5%	(0.5%)	-
South Africa	1%	0.5%	0.6%	-
South Korea	-	0.5%	(0.5%)	-
Others	-	1.1%	(1.1%)	-
Alternative assets	7%	10%	(3%)	-1%
Real Estate	4%	5.0%	(1.0%)	-
Energy Commodities	3%	3.5%	(0.5%)	-1%
Industrial Metals	-	0.3%	(0.3%)	-
Precious Metals	-	0.2%	(0.2%)	-
Other commodities	-	1.0%	(1.0%)	-
Currency Hedging	(8%)	-	(8%)	-3%
JPY	(3%)	-	(3.0%)	-3%
GBP	-	-	-	-
EUR	(5%)	-	(5.0%)	-
AUD	-	-	-	-
Cash	-	-	-	-

EQUITIES

Andrea Cicione

- Declining US recession risk and a cautious Fed boost the outlook for equities
- Earnings have bottomed in the US and several other markets
- We add to EM as lower UST yields and a softer dollar boost sentiment

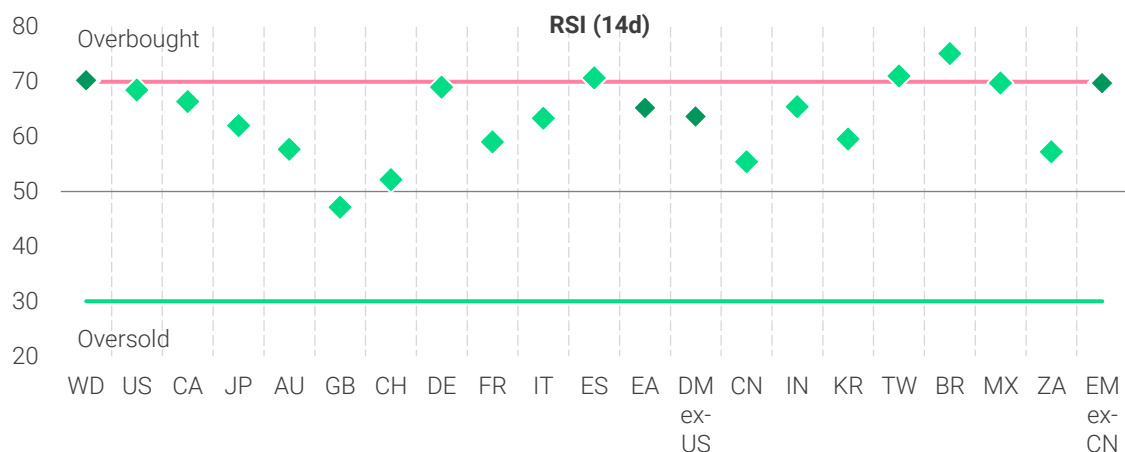
US is likely to avoid recession in 2024. With inflation on a path towards normalization and the global economy continuing to slow down, we think the Fed has shifted from a hawkish to a dovish bias. Since there is a presidential election in the US next year, it is likely that the Fed will choose to err on the side of caution and prioritize full employment over price stability. And given that the FOMC will cut at the first sign of weakness, a US recession in 2024 should be avoided.

Valuations are supported, earning will improve. The end of the monetary-policy tightening cycle and the prospect of easing should continue to support equity valuations. But earnings are expected to improve, too. In the US, profits appear to have bottomed and are forecast to grow over the next few quarters, albeit rather gradually at first. With margins seemingly having stabilized at healthy levels, these expectations seem reasonable.

Earnings cycle is favourable for EM ex-China. It is likely that earnings have also reached a cyclical low in other markets. As the charts on the next page illustrate, there is still significant dispersion across both DM and EM equities. EMs appear to be in a better overall position as far as the earnings cycle goes, although the outlook for China is pretty flat.

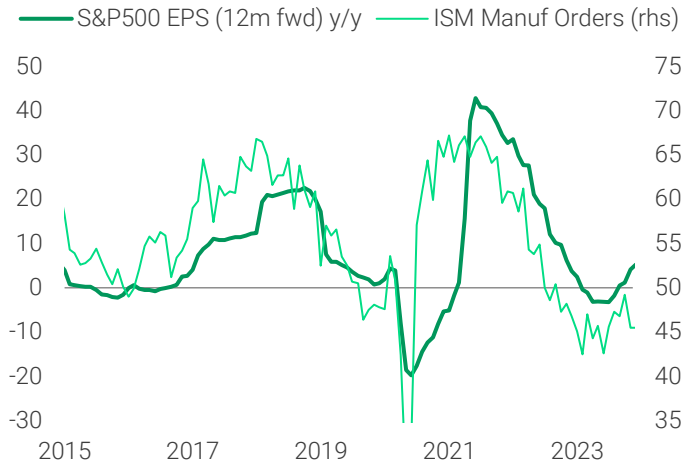
Equities are overbought in the near term. Despite the improving prospects for stocks, there are reasons for not getting overexcited. First, the global economy is still expected to slow down for another two to three quarters. Even if a US recession is averted, the ride to the bottom may be bumpy. Second, the US is the only major economy faring relatively well, making it our main pick. However, valuations are rich, limiting the re-rating potential even on a more dovish Fed outlook. Finally, a lot of the good news is already in the price and several markets look overbought.

Equity markets are in overbought territory



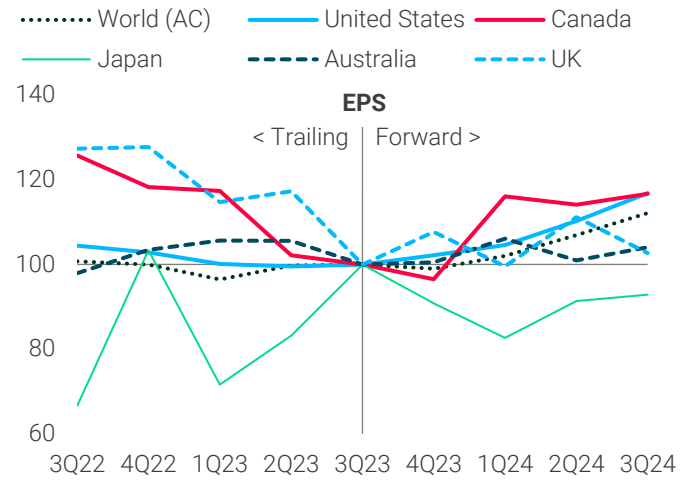
Source: Bloomberg.

Manufacturing recovery needed for EPS growth



Source: Bloomberg.

US EPS seems to have bottomed around Q3



Source: Bloomberg.

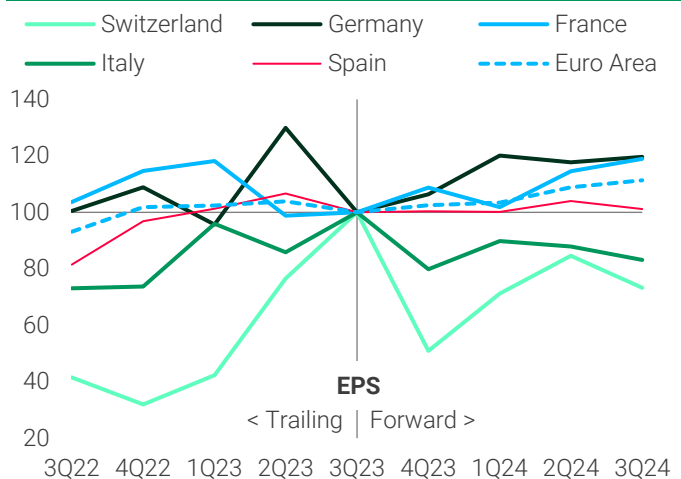
ISM Manufacturing setback. The nascent recovery in US earnings has closely the formation of a bottom in manufacturing activity. Against this background the October ISM print was a significant setback for the profit outlook, with both the headline index and new orders falling back further below 50. One disappointing data point is not enough to challenge what remains a seemingly recovery in industrial activity. However, given the predictive power of ISM over EPS, we will continue to watch this indicator very carefully.

DM ex-US valuations are close to a record discount to the US. The US has been our favourite equity market since the summer and it remains so, mainly owing to the exceptional resilience of the economy. At the same time, we have been cautious on China because of the cyclical and secular slowdown. As the top-left chart on the next page shows, however, the valuation gap between the US and other DMs remains close to all-time highs. For this reason, we keep an overweight in DM ex-US equities, despite their less compelling economic and EPS growth outlook.

Recommendation and portfolio changes

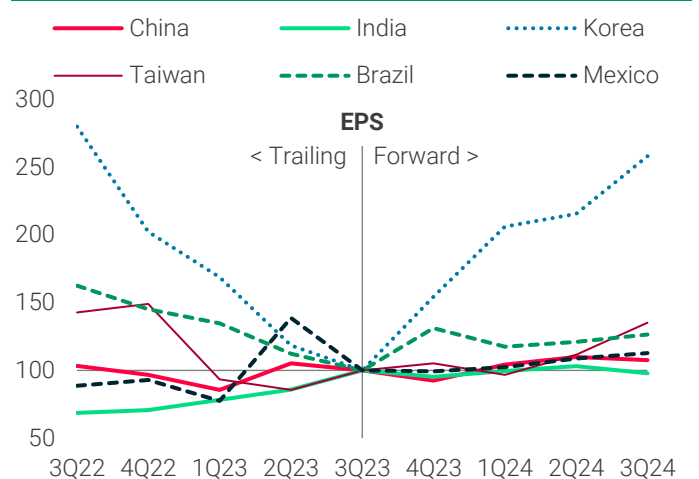
UST yields & USD headwinds are fading for EMs. The shift in the Fed reaction function means that the two main headwinds for EMs this year – rising yields and a stronger dollar – are likely to weaken. This, coupled with the encouraging outlook for profits, warrants a more constructive

EPS dispersion is high in Europe



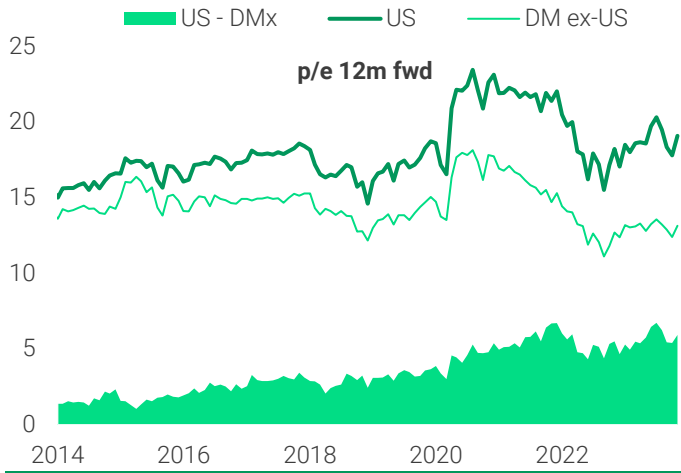
Sources: Bloomberg, GlobalData TS Lombard.

Most EMs should experience positive EPS growth



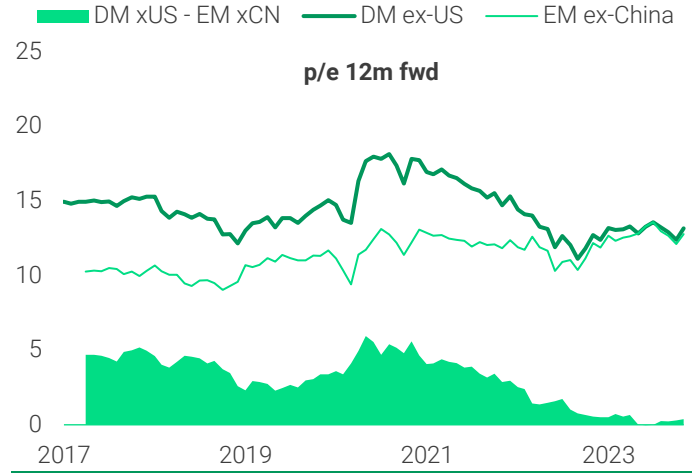
Sources: Bloomberg, GlobalData TS Lombard.

DMx valuations close to record discount to US



Sources: Bloomberg, GlobalData TS Lombard.

Ex China and US, no meaningful EM discount to DM



Sources: Bloomberg, GlobalData TS Lombard.

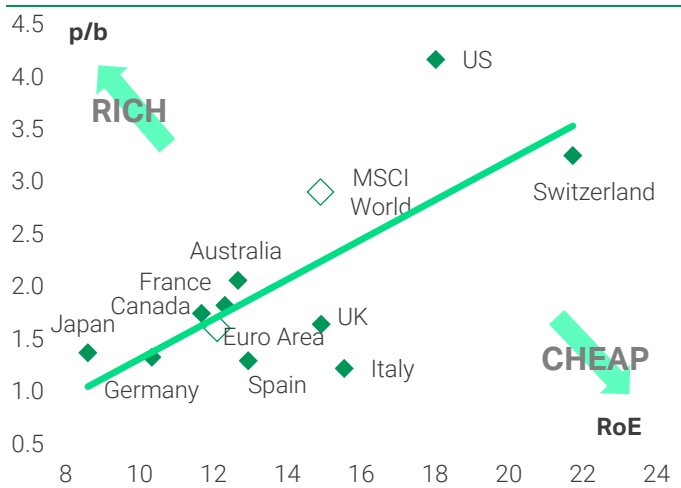
view on EM equities. We increase the weight in our model portfolio from underweight to benchmark weight, while at the same time rotating from relative winners (India) to relative laggards (Brazil and Mexico). Although we are mindful that LatAm equities look overbought in the near term, we think that their recovery has more legs.

India cut to 0 from +1. Markets lack new impetus amid lagging private sector revival, weak consumer sentiment and food price risks. However, India remains a safe haven among EM economies with comparatively little exposure to the US economy. Cheaper oil is also a positive.

Brazil upgraded to +1 from 0. The tax reform bill was approved in the Senate earlier this month, bringing it closer to being signed into law. The reform is far from ideal but will nonetheless simplify the current byzantine system and should still have a positive impact on GDP and productivity.

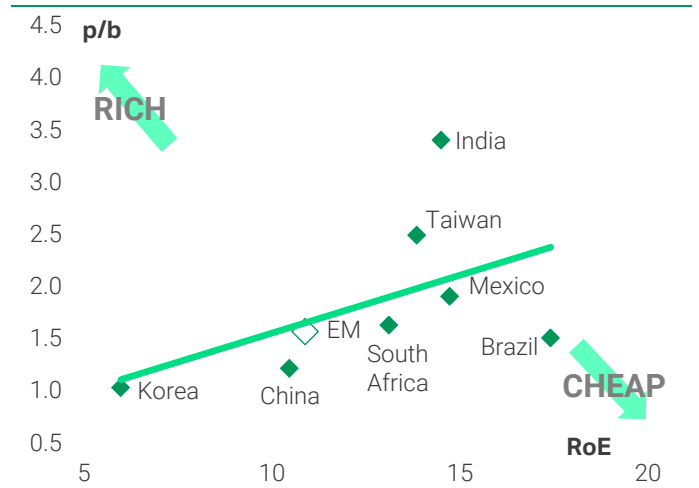
Mexico raised to +1 from -1. Nearshoring momentum and the prospect of lower interest rates next year will drive markets supported by a relatively robust US economy. We expect interest rates to remain high well into next year, but Banxico has taken a lead from the Fed with less hawkish comments earlier this month. Economic growth was solid in Q3 2023, but we expect momentum to slow heading into next year.

DM price-to-book ratio vs RoE



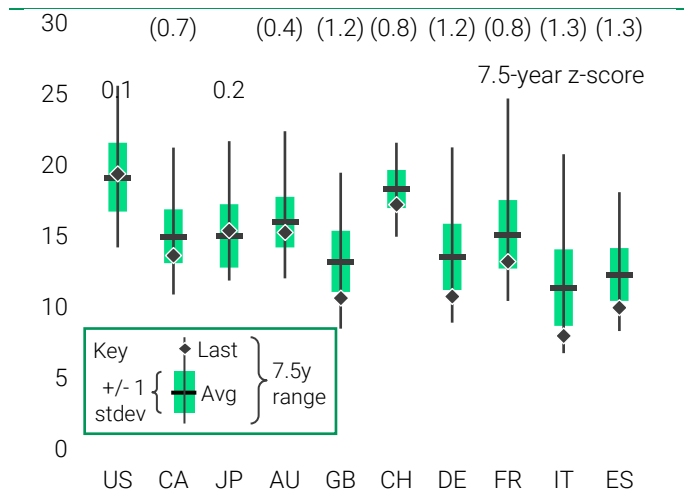
Source: Bloomberg

EM price-to-book ratio vs RoE



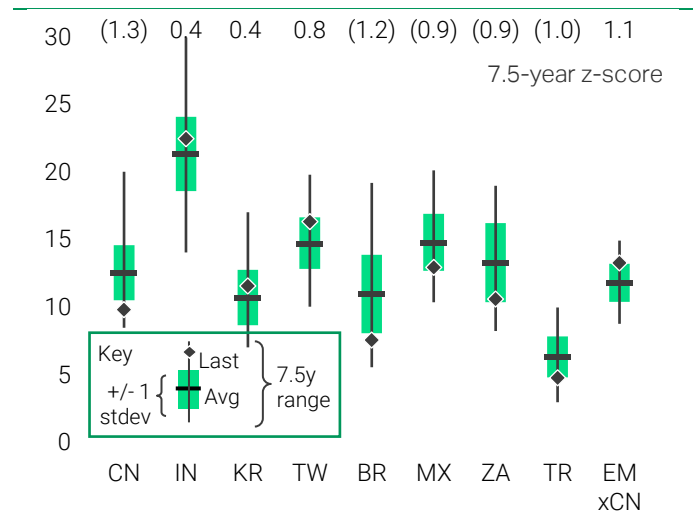
Source: Bloomberg.

DM price-to-earnings ratio vs cycle



Sources: Bloomberg, GlobalData TS Lombard.

EM price-to-earnings ratio vs cycle



Sources: Bloomberg, GlobalData TS Lombard.

Equities dashboard

	MktCap		Total return LC			P/E (x)			P/B (x)			RoE			EPS growth		Dividend yield		
	Memb.	(US\$)	1m	ytd	2022	Trail.	Fwd	ZScr	Trail.	Fwd	ZScr	Trail.	Fwd	ZScr	Fwd	3m	Trail.	Yr	ZScr
World (AC)	2947	63,398	3.3	15.3	-17.9	18.3	16.5	-0.2	2.7	2.5	0.8	13.6	14.5	1.0	-2.0	0.5	2.1	2.3	-0.5
United States	626	39,811	3.2	19.5	-19.5	22.2	19.5	0.1	4.3	3.9	0.8	17.5	18.4	1.0	-1.5	1.9	1.5	1.6	-1.0
Canada	88	1,774	2.7	7.8	-5.8	14.9	13.7	-0.7	1.9	1.7	-0.8	11.5	12.1	0.2	-1.5	2.2	3.3	3.6	1.0
Japan	236	3,481	4.6	29.7	-4.1	16.6	15.5	0.2	1.4	1.3	0.6	8.7	8.5	0.1	0.4	2.0	2.2	2.4	0.2
Australia	58	1,089	1.3	7.6	3.6	15.2	15.3	-0.4	2.1	2.0	0.3	13.0	13.1	0.4	-4.4	-3.4	4.5	4.3	-0.3
UK	83	2,247	-2.7	2.8	7.0	10.8	10.7	-1.2	1.7	1.6	-1.1	15.9	13.9	0.9	-9.1	0.0	4.1	4.6	0.8
Switzerland	45	1,476	-1.8	2.1	-16.5	18.7	17.3	-0.8	3.7	3.2	1.1	22.5	16.8	1.9	-23.1	0.2	3.2	3.4	0.9
Germany	59	1,291	3.6	13.2	-16.5	13.3	10.8	-1.2	1.3	1.2	-1.6	8.3	9.8	-0.4	3.3	0.9	3.8	3.8	1.1
France	63	1,834	2.3	12.1	-7.0	14.1	13.3	-0.8	1.8	1.8	0.9	10.8	12.5	1.2	-2.8	-0.3	3.1	3.3	0.0
Italy	23	408	3.1	28.2	-7.7	6.6	8.1	-1.3	1.1	1.2	0.8	13.9	15.4	1.8	-7.6	3.7	4.7	6.4	2.0
Spain	19	409	4.4	23.8	0.6	10.3	10.0	-1.3	0.9	1.2	0.0	9.0	11.9	1.5	-1.9	3.0	4.3	5.3	1.3
Euro Area	229	5,060	3.4	13.6	-11.7	12.9	12.1	-1.1	1.5	1.5	-0.2	10.3	11.9	1.0	-1.1	1.4	3.4	3.8	1.0
DM ex-US	884	16,859	3.3	10.0	-13.7	14.0	13.5	-0.8	1.7	1.6	0.1	11.2	11.6	0.9	-4.1	-1.0	3.3	3.6	1.0
China	765	1,961	1.6	-7.1	-21.7	12.4	9.9	-1.3	1.2	1.2	-1.4	9.5	11.4	-0.8	6.8	-4.9	2.5	2.6	0.7
India	122	1,039	1.2	10.6	3.0	25.7	22.5	0.4	3.3	3.5	0.8	12.7	15.7	0.6	10.5	1.2	1.3	1.4	-0.5
Korea	104	844	3.1	16.7	-24.7	18.3	11.6	0.4	1.0	1.0	-0.2	5.2	8.4	-0.6	-0.9	-3.7	2.0	2.5	0.5
Taiwan	90	1,040	3.8	25.2	-21.5	19.1	16.4	0.8	2.3	2.4	1.0	12.5	14.5	0.3	2.9	4.3	3.4	3.2	-1.5
Brazil	47	385	5.8	13.6	8.6	8.1	7.6	-1.2	1.6	1.3	-1.3	19.5	16.5	0.1	-3.3	9.2	5	8	1.3
Mexico	23	171	6.9	11.9	-6.3	15.3	13.0	-0.9	1.9	1.8	-0.7	14.8	14.2	0.4	4.0	-8.8	3.4	5.0	1.6
South Africa	34	203	1.1	4.3	3.4	15.3	10.7	-0.9	1.7	1.6	-1.4	12.9	14.3	-0.4	-3.8	-3.9	4.3	4.4	0.7
EM ex-China	672	4,768	4.8	11.4	-18.9	15.9	13.3	1.1	1.8	1.7	0.9	11.3	12.7	0.0	1.4	1.2	3.0	3.4	-0.1

ZScr is the number of standard deviations from the 7.5-year avg (numbers below -1 and above 1 highlighted). All figures % unless stated otherwise. P/e, p/b, RoE and DY ZScr are over 7.5y on 12m forward measures. EPS growth is forward / trailing. EPS 3m growth is on forward earnings.

MSCI sector weights

	%	US	Canada	Japan	Australia	UK	Switzerland	Germany	France	Italy	Spain	Euro Area	Brazil	China	Taiwan	India	Mexico	South Africa	Korea	DM	EM
Industrials		8.8	12.7	23.3	5.5	11.8	9.5	18.9	23.7	5.1	8.9	16.6	7.6	9.9	3.1	7.6	14.7	2.5	10.7	11.0	8.4
Energy		4.1	17.9	0.8	5.4	13.4			8.1	11.7	4.4	4.8	19.5	2.4	0.3	9.0		1.8	1.1	4.6	6.0
C. Discr.		10.6	3.9	19.0	5.9	5.8	4.8	14.5	18.9	23.1	18.0	15.4	2.3	19.5	2.1	10.2		13.2	7.9	10.7	11.8
Healthcare		12.5		8.0	9.5	12.4	34.8	9.2	10.0	2.7	1.1	7.5	3.3	7.5	0.3	4.4		1.6	4.7	12.2	5.1
Financials		12.3	33.3	11.9	32.4	18.6	17.5	18.6	10.8	35.1	33.2	18.1	32.3	17.7	13.8	33.1	16.5	40.7	8.2	14.8	22.4
Real Estate		2.4		3.1	5.8	1.0						1.0		2.2	0.2			3.3		2.4	1.6
Utilities		2.3	3.2	1.2	1.5	4.4	0.2	4.2	2.7	19.1	25.0	6.1	7.9	2.3		3.8			0.5	2.7	2.4
Tech		29.5	9.0	14.0	1.5	1.0	1.3	16.6	5.0	1.2		12.4	0.9	11.8	71.5	10.7			50.4	23.2	18.9
Communications		8.7	4.5	7.8	3.5	2.8	1.0	6.5	2.9	1.8	9.4	4.3	1.8	10.4	2.6	2.5	14.5	5.6	6.3	7.5	7.1
Materials		2.4	10.0	5.0	24.4	10.7	8.3	6.5	6.1			5.6	16.7	7.5	4.7	8.3	19.5	22.2	8.2	4.0	8.7
C. Staples		6.1	4.6	5.9	4.6	18.4	22.2	2.9	10.8	1.5		8.0	7.7	8.9	1.4	9.8	31.9	9.1	2.0	7.0	7.2

Largest three sectors for each market highlighted

Sector price-to-earnings ratio (12-month trailing)

	US	Canada	Japan	Australia	UK	Switzerland	Germany	France	Italy	Spain	Euro Area	Brazil	China	Taiwan	India	Mexico	South Africa	Korea
Market	22.3	15.0	14.8	15.3	10.1	15.5	11.7	14.8	7.4	9.4	12.4	7.9	10.6	17.1	24.3	12.4	11.3	11.9
Industrials	21.9	21.6	13.0	29.6	22.2	20.2	11.9	18.3	8.1	19.8	15.8	34.4	7.0	11.3	45.1	13.3	15.1	14.0
Energy	8.8	15.0	8.7	9.0	5.6			8.3	8.9	4.4	8.6	4.2	5.7	75.0	18.1		6.1	14.4
C. Discr.	28.5	17.6	13.5	25.2	17.8	16.4	5.9	18.6	6.2	25.4	10.6	15.4	23.5	24.2	46.2		11.4	4.9
Healthcare	27.4		31.1	35.9	19.4	22.9	24.8	16.5		117.9	19.9	34.2	19.0	273.1	41.0		15.0	56.8
Financials	13.4	10.9	11.1	13.5	7.0	6.1	9.5	7.1	6.4	5.7	7.0	8.9	4.3	16.3	18.2	8.7	10.0	4.6
Real Estate	34.8	37.6	14.8	24.4	7.4	31.9	341.0	59.6			68.9		6.4	14.9	83.4	4.5	9.1	
Utilities	18.3	12.8	3.9	25.7	9.8	9.3	15.6	22.6	9.4	12.1	11.2	14.7	8.5		17.6			5988
Tech	37.0	75.2	25.5	174.8	38.0	38.3	34.3	16.4		35.0	29.1	37.0	15.6	16.8	25.3			15.9
Comms	21.5	25.8	17.9	30.2	4.5	15.6	11.6	15.7	36.9	19.7	15.5	18.9	15.1	24.1	42.1	12.9	8.7	29.3
Materials	18.4	18.7	12.7	11.8	10.9	21.0	12.6	17.4			14.9	6.4	10.9	62.4	20.2	12.2	12.6	25.9
C. Staples	23.3	17.2	23.3	23.5	12.2	27.1	27.3	26.2			20.9	16.1	23.9	15.0	54.7	17.9	26.6	16.9

Sector 12-month total returns (local currency)

	%	US	Canada	Japan	Australia	UK	Switzerland	Germany	France	Italy	Spain	Euro Area	Brazil	China	Taiwan	India	Mexico	South Africa	Korea
Market		16.3	5.5	24.1	6.4	4.5	0.1	10.6	10.6	26.2	27.7	11.9	28.3	1.5	19.9	8.9	19.0	3.6	7.9
Industrials		10.3	4.0	24.6	6.4	22.1	13.9	12.5	17.7	-19.6	32.2	14.7	13.0	-9.4	7.1	9.7	6.6	34.5	-2.2
Energy		-7.6	0.7	37.0	0.7	9.0			13.5	10.3	3.2	8.5	87.6	27.5	1.8	7.2	0.0	-2.5	-12.5
C. Discr.		21.1	12.8	30.2	14.6	11.8	-1.5	5.7	5.2	42.8	40.9	10.7	-10.3	-2.6	14.1	31.1		21.2	15.6
Healthcare		-1.5		-1.8	-8.0	-1.2	-6.1	-12.5	1.4		30.5	-0.9	-3.8	-8.3		22.0		16.7	-4.7
Financials		2.2	0.6	50.3	3.8	13.2	12.3	18.8	6.7	40.2	52.5	19.3	36.7	8.0	14.9	6.2	34.4	11.9	18.2
Real Estate			14.2	13.4	11.5	2.8	6.8	3.3	3.4					-21.9	-22.4	52.1	50.8	0.7	
Utilities		-4.7	1.4	50.7	3.0	11.2	0.0	13.1	17.8	25.0	8.9	12.4	25.6	-6.9		-19.6			-9.7
Tech		39.7	60.2	25.4	5.8	9.2	0.0	24.1	9.3			14.6	29.7	-4.3	24.5	3.8		0.0	16.1
Comms		42.5	-0.2	11.7	12.1	-2.5	6.9	15.8	14.3	16.5	6.5	13.3	56.2	20.5	14.4	12.5	-12.7	-24.1	-8.7
Materials		3.2	-1.9	32.9	16.6	-7.7	7.0	3.6	20.7	0.0	0.0	8.0	7.0	-12.2	-4.3	6.5	25.0	-16.1	-1.7
C. Staples		-1.5	12.7	11.1	-2.0	-6.9	-7.1	7.9	13.4			7.9	6.1	-9.3	12.3	15.4	30.6	15.5	-12.6

FIXED INCOME

Skylar Montgomery Koning

- Bond yields are “fair value” to the Fed dot plot; it’s too early to go overweight, especially as downside risks persist
- But with the upside for yields limited, IG credit looks appealing again while HY remains so

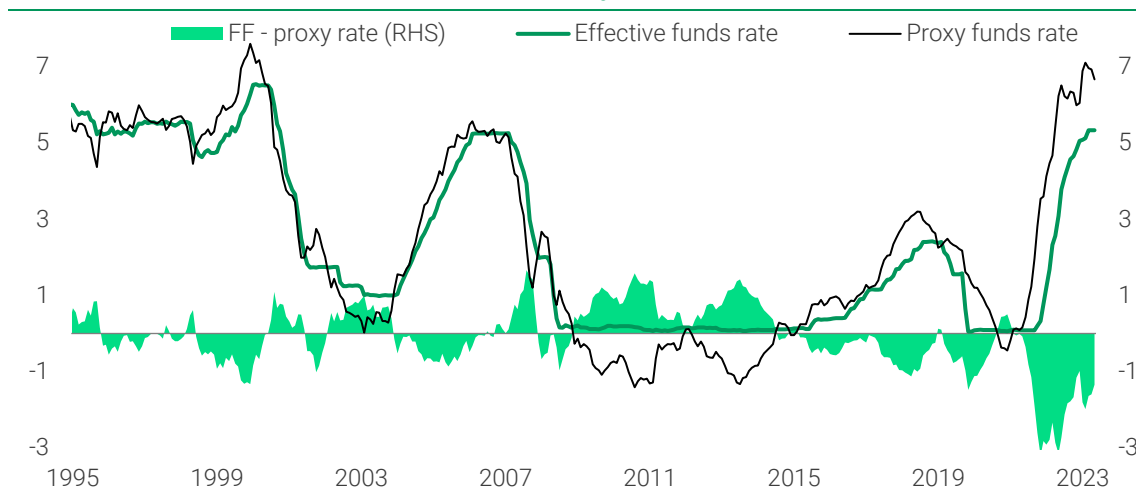
Tactically adding duration

Financial conditions have loosened.... Since our last allocation, yields have whipsawed, with the 10y falling from 5% to below 4.5%. There is no consistent way to measure financial conditions, but the market move we have seen certainly points to loosening. To put this in context, though, it seems fair to use one of the regional Fed’s metrics. The San Francisco Fed’s Proxy Funds rate uses 12 financial variables to estimate the stance of monetary policy; essentially, it can be used to estimate whether financial conditions are tighter or looser than the Fed funds rate.

...but policy is still tight.... On this measure, financial conditions peaked in July. But the key is that the proxy funds rate has been above Fed funds throughout 2022-23 (and while the measure has declined, it still sits at 6.7% –i.e., financial conditions tighter than indicated by FF). The Fed cares about the level of tightness and how long conditions stay there. Given the forward-looking nature of markets, the proxy funds rate has tended to lead Fed funds, so the recent turnover could be a leading signal for a turn in the policy rate. However, we did get a false signal at the end of 2022.

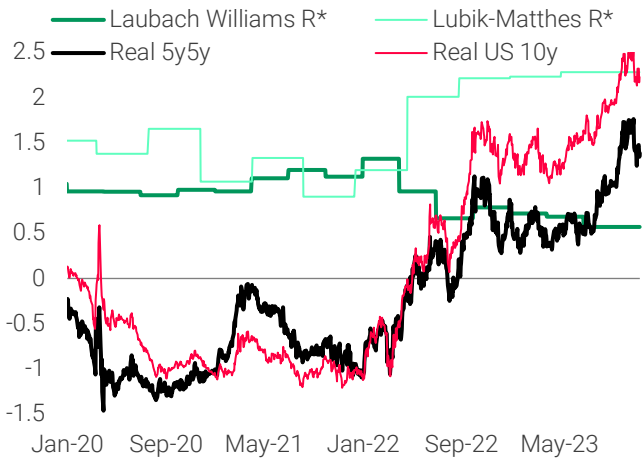
...squeezing the economy. Still-elevated financial conditions point to pressure on the economy, as does our Macro Strategy, which showed real rates across the curve are higher than any estimate of neutral (including the markets). This means that policy is restrictive; and indeed, we are seeing evidence of policy curbing demand through both stock and flow effects. Thanks to a 3Q number that was well above trend, real 4Q growth will still be positive, but there will be slowing into 2024 and an economic soft patch.

Financial conditions have loosened, but policy is still tight



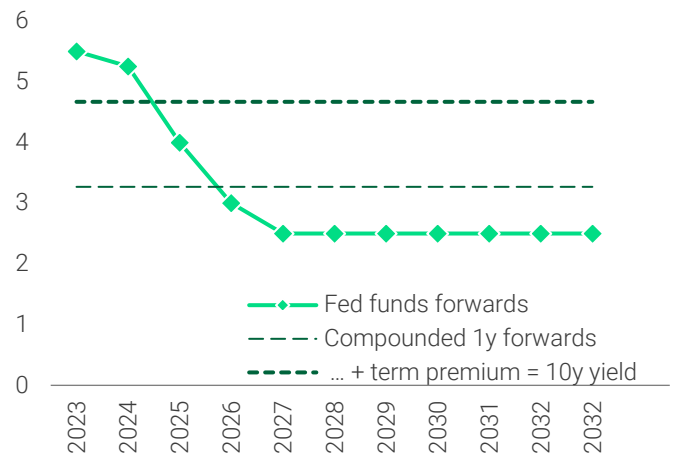
Sources: GlobalData TS Lombard, Bloomberg.

Neutral has shifted, but policy is restrictive



Sources: GlobalData TS Lombard, Bloomberg.

Bond yields are 'fair value'



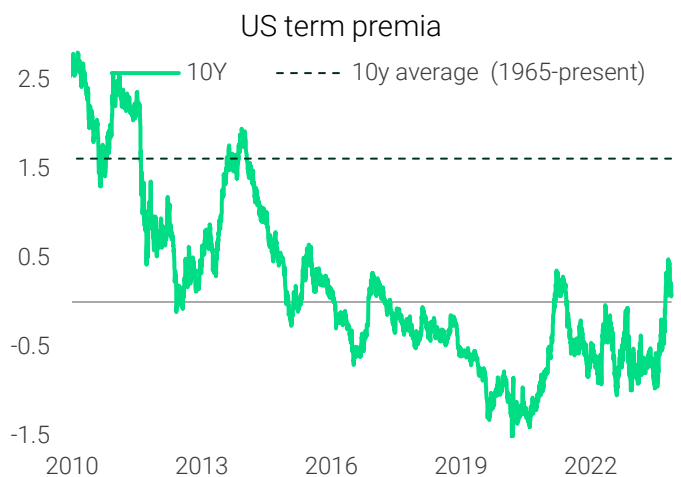
Sources: GlobalData TS Lombard, Bloomberg.

We maintain a bullish US FI bias... As the disinflation mirage continues, the next move from the Fed will be cuts, with any signs of weakness bringing them on quickly. This means the longer-term bias for fixed income is bullish; and it is certainly the case that current yield levels are attractive. But there are still questions about timing; and as we argued last month, 10y yields of 4.5-5% look about right, under the Fed's central case. So, if anything, yields are a bit low right now.

...amid continued downside risks: the term premia are below "normal" levels, having fallen back to zero in the recent rally (auctions like last week's 30y are a reminder of the term premia risk). Our structural view is that in the post-Covid economy, investors will want to be compensated for no longer being at the zero-lower bound, the associated risk of capital loss, the higher volatility and the greater uncertainty. While it is unlikely that we can get to our long-term view of structurally higher term premia in one go, higher term premia is certainly a risk for the bullish view.

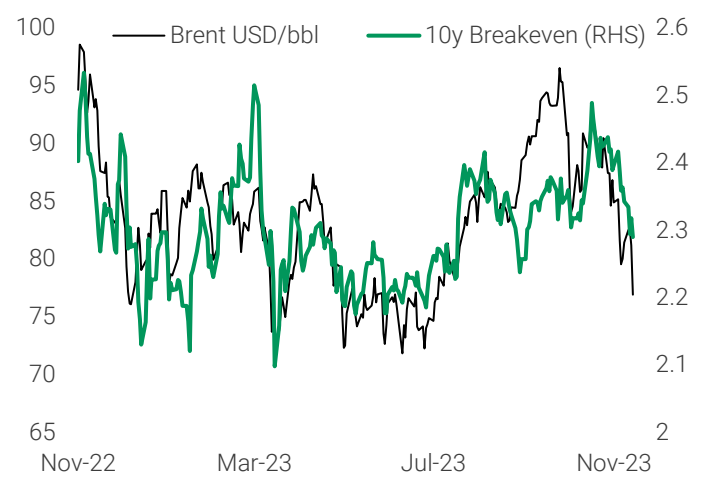
Oil prices currently point to downside for breakevens, but geopolitics pose a consistent supply-shock threat that could force yields higher. Furthermore, while we do not expect the Fed to hike, our expectation that the US economy will remain resilient means an upside surprise to growth could still put upward pressure on yields, especially if it means cuts are once again priced out of 2024 – there are currently 100bp of cuts priced in.

Term premia are well below 'normal' levels



Sources: GlobalData, TS Lombard, Bloomberg.

Energy shocks remain a risk to FI



Sources: GlobalData, TS Lombard, Bloomberg.

The US govvie rally may be self-defeating in the near term. The Fed attributed the November policy pause in part to tight financial conditions being a substitute for further hikes. The flipside of this is that while conditions are still restrictive, the loosening that we have seen post-meeting should feed into hawkishness. And that means there is a limit to the FI rally we can get until either the Fed is convinced that inflation is beaten or unemployment rises towards 4.5%. We thus stay neutral US govvies this month, preferring to express our bullish FI view in other markets that will benefit more from the robust risk outlook or where the economic outlook is less rosy (last month we added duration in Europe and we have been +1 Gilts since July).

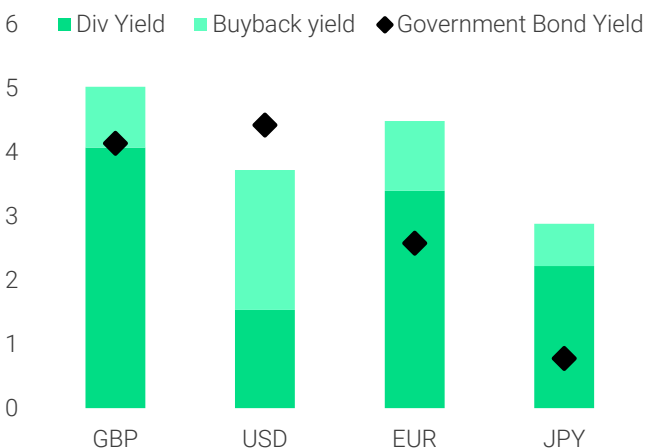
Risk-reward remains compelling in credit. What the market is seeing right now is an environment that is just right: growth is slowing but there is no recession, and disinflation will allow the Fed to cut in 2024. As central banks remain patient, allowing the tightening they have already done to feed into the economy, we would expect volatility to come down and thereby support risk appetite and thus credit. We have been positive on IG & HY credit for most of the past year, as compensation for risk has been more generous in credit than in equities.

IG credit is the best way to add duration. The main risk for US IG credit came from rising interest rates, but with yields having found "fair value" and the Fed done with tightening, this risk is now limited. Moreover, as the economy slows but does not enter recession, IG will get the best of both worlds: spreads are likely to compress in the positive risk environment and total returns will benefit from the eventual rally in US govvies. Even in the worst-case scenario of a mild recession, we would expect IG total returns to be positive: IG experiences negative total returns only very rarely, as spread widening is offset by falling rates.

We upgrade Brazil government bonds to +1 from 0. Banco Central will remain cautious into 2024, but the easing cycle is set to continue with the Selic rate reaching 9% in 2024, providing FI investors with both sizeable carry and capital appreciation. Additionally, the downside surprise to the October CPI reinforces our view of a more favourable inflationary outlook.

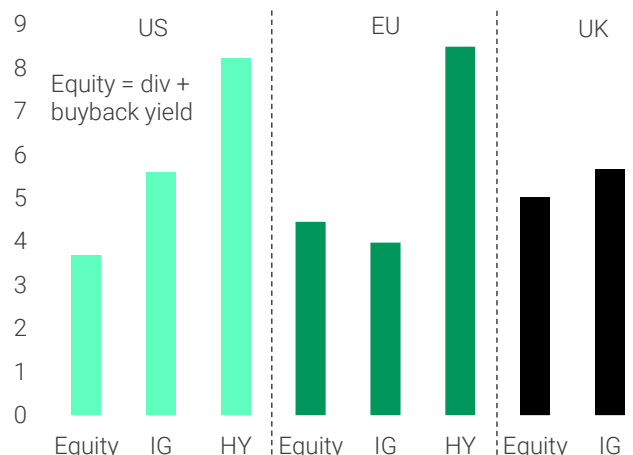
We upgrade Mexico government bonds to 0 from -1. We expect interest rates to remain high well into next year, but Banxico has taken a lead from the Fed with less hawkish comments earlier this month. Headline inflation has fallen but core is sticky. We expect monetary easing to begin in Q2/24.

Govvie yields are compelling...



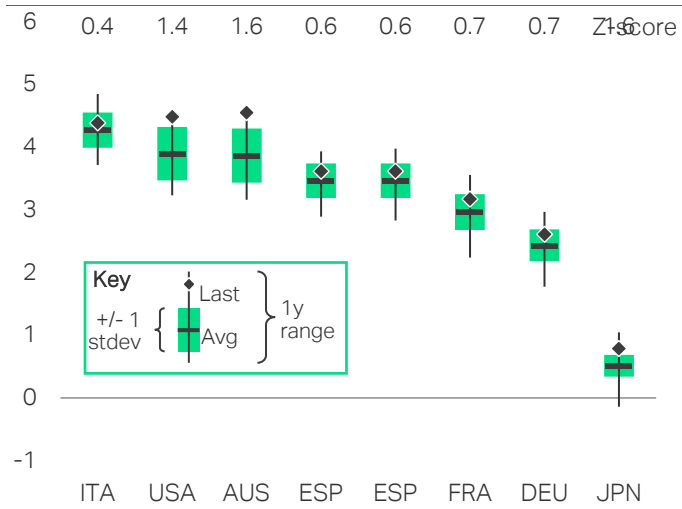
Sources: GlobalData, TS Lombard, Bloomberg.

...as are credit yields, especially in US

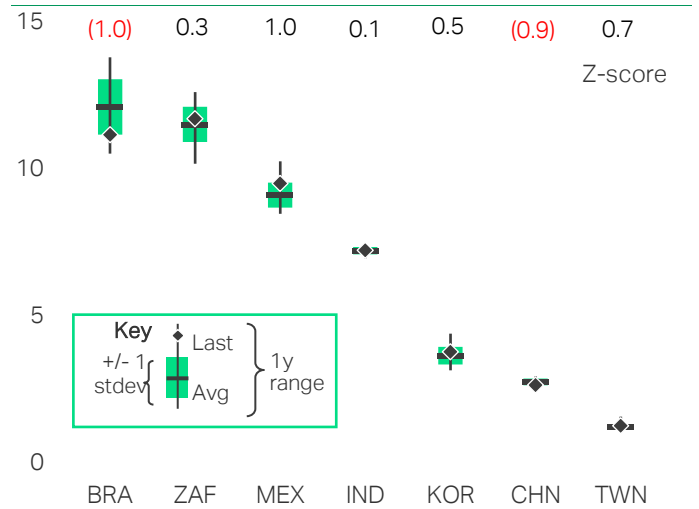


Sources: GlobalData, TS Lombard, Bloomberg.

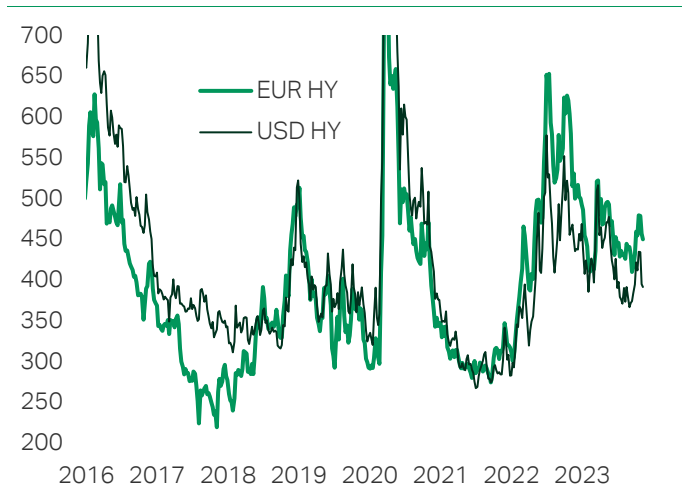
DM yields (%)



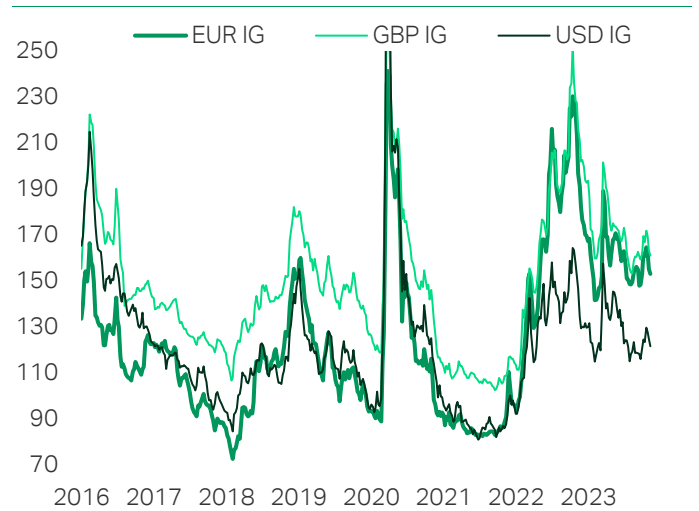
EM bond yields (%)



HY corporate spreads



IG corporate spreads



	Policy rate	Inflation		2y yield		10y yield		7-10y total return			5y CDS (bp)		Money grth		Budg %GDP	Debt %GDP	GDP y-y
		Rate	Target	Last	'score	Last	'score	1m	ytd	2022	Last	StDev	arrow	Broad			
US	5.50	3.7	2.0	4.87	2.0	4.43	2.2	2.9	-1.4	-14.9	48	0.0	22.9	-3.6	-6.1	126	2.9
Canada	5.00	3.8	1.0-3.0	4.45	2.1	3.66	2.1	22.3	17.2	-14.9	48	-0.4	-4.9	5.8	-0.5	72	-0.2
Japan	0.10	3.0	2.0	0.04	1.5	0.76	3.3	-38.5	-41.2	-14.9	28	0.0	9.0	2.4	-4.3	216	1.2
Australia	4.35	5.4	2.0-3.0	4.15	2.1	4.47	2.2	2.2	-0.1	-14.1	15	(-1.3)	-13.6	5.1	-2.7	69	2.1
UK	5.25	4.6	2.0	4.52	2.3	4.08	2.2	34.4	28.7	-14.9	33	1.1	N.A.	-3.9	-2.3	195	0.6
Germany	4.00	2.9	<2.0	2.94	2.4	2.57	2.2	5.6	1.2	-14.9	18	0.9	-9.9	-1.2	-2.5	64	-0.3
France	4.00	2.9	<2.0	3.30	2.5	3.14	2.2	20.4	15.3	-14.9	26	0.0	-9.9	-1.2	-4.8	123	0.7
Italy	4.00	2.9	<2.0	3.56	2.2	4.33	1.8	96.4	88.0	-14.9	95	-0.9	-9.9	-1.2	-8.0	132	0.0
Spain	4.00	2.9	<2.0	3.39	2.4	3.58	2.0	78.0	70.4	-14.9	49	-0.4	-9.9	-1.2	-4.7	141	1.8
Brazil	12.25	4.8	2.5-6.5	10.33	0.5	11.06	0.5	-58.5	-60.2	-14.9	154	(-1.1)	2.8	10.9	-7.6	101	3.4
Mexico	11.25	4.3	2.0-4.0	10.24	1.6	9.42	1.7	-59.1	-60.8	-14.9	99	-0.8	6.4	9.2	-6.2	54	3.3
India	6.50	4.9	4.0	7.19	1.0	7.30	0.7	-58.1	-59.9	-14.9	N.A.	N.A.	6.7	11.0	-6.8	47	7.8
Taiwan	1.88	3.1	5.0	0.00	N.A.	1.29	1.3	-74.9	-76.0	-14.9	N.A.	N.A.	3.1	6.0	0.0	36	2.3
S Africa	8.25	5.4	3.0-6.0	N.A.	N.A.	11.64	2.0	120	110.4	-14.9	241	0.2	15.8	7.7	0.2	53	1.6
Korea	3.50	3.8	2.0	3.73	1.9	3.81	1.9	9.0	1.2	-15.0	34	-0.3	-1.7	2.6	1.7	46	1.4

Zscore is number of standard deviations from the 7.5-year average (numbers <-1, >1 highlighted). All figures % unless stated otherwise.

CURRENCIES

Skylar Montgomery Koning

- Yields are the fundamental driver of the yen and very slow moving BoJ normalization will not save the currency against UST yields reaching for 5%
- Looking forward, the fate of the yen lies in the hands of the Fed next year; the bad news for JPY is that the US economy continues to surprise to the upside

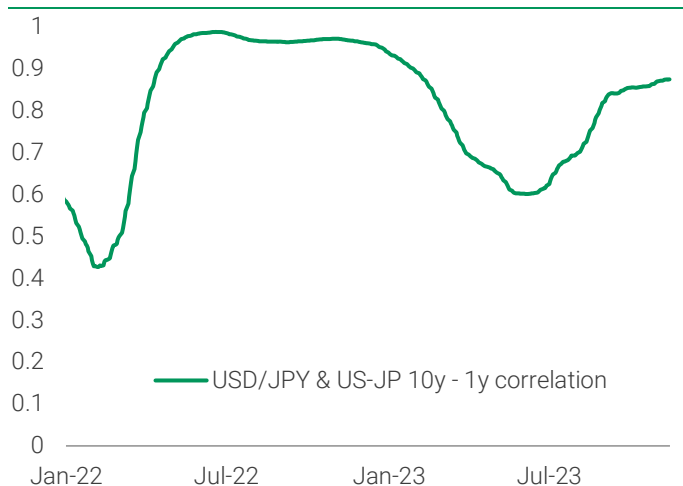
155 is the next stop for USD/JPY

Yields are the fundamental driver of the yen and they are pointing to more downside. Since the start of the DM tightening cycle, JPY has been under pressure as DM yields increased with the correlation between USD/JPY and relative 10y rates rising above 90% when Fed hikes began in March 2022 (see chart below left). The correlation has remained high since then, not pulling back to a still high 60% until Q2 2023 amid the market volatility surrounding the SVB crisis. From here, rate differential momentum clearly points to USD/JPY upside (see chart below right)

Slow-moving BoJ normalization will not save the yen. BoJ policy normalization is slow for two main reasons: the much-discussed need to entrench inflation and, as highlighted in a 2023 St. Louis Fed paper, the large duration mismatch on the governments balance sheet. Japan’s growth has been consistently below the cost of debt, as a result of which it has been unable to achieve debt sustainability through growth. As debt has ballooned to more than twice GDP, it has been funded with short duration low-yielding debt. In parallel, Japan’s government has increased fiscal space by investing in long-duration risky assets.

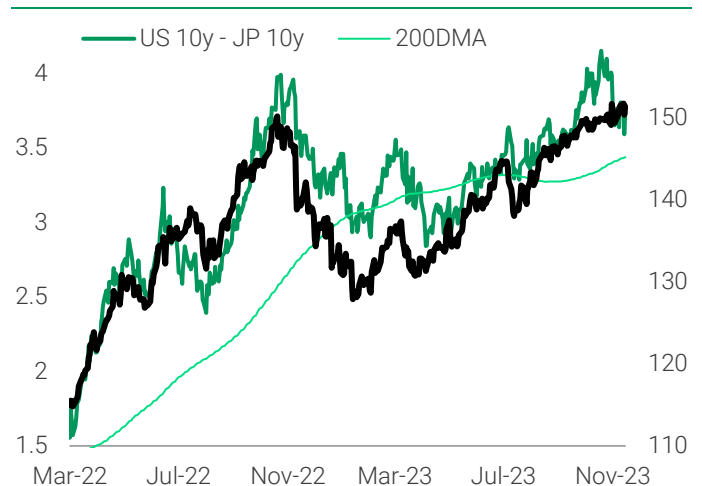
This has created the large duration mismatch, which means that when rates increase, the fiscal capacity deteriorates quickly. This is sustainable right now, but the growing burden of an elderly population means liabilities are only set to increase. Therefore, to ensure debt sustainability – absent increasing risky investment – the cost of debt and thus the policy rate have to be contained. Because of this constraint, Japanese policymakers are unable/unwilling to push yields in the yen’s favour against UST yields reaching for 5%.

Yields are the fundamental driver of the yen...



Sources: GlobalData TS Lombard, Bloomberg.

... and are pointing to more USD/JPY upside



Sources: GlobalData TS Lombard, Bloomberg.

Yen weakness helps Japanese authorities. From a balance sheet perspective, yen strength threatens the large unhedged positions on the governments balance sheet. Moreover, this tightening cycle has been characterized by reverse currency wars, where central banks have fought to appreciate their currency in order to contain inflation. But the BoJ has never played that game: it is focused on sustaining inflation and that is precisely what a depreciating currency does – as well as being positive for exports and the domestic equity market.

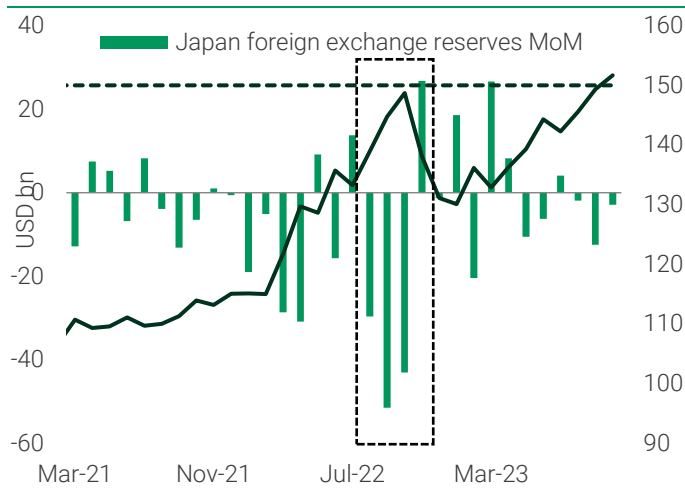
Of course, there are limits to the benefits: a depreciating currency raises input costs for companies and consumers are pinched by the rising price of imports. Moreover, the impact of the 2022 energy shock has not worked its way out of the Japanese current account to the same extent as other importers because of the currency. The BoJ does not want non-linear or one-sided moves in the currency, but at the same time they are not fighting fundamentally driven depreciation altogether.

FX intervention has limits. FX reserves are limited; and, historically, unilateral intervention has failed to trigger a sustained rally. This means the Japanese authorities need to adopt a more tactical approach towards FX intervention. From end-September to 30 October, there was an orderly testing of 150 on USD/JPY with low realized volatility.

The market assumption was that the Japanese authorities were reining in the currency in a similar fashion to last autumn, when reserves fell by a record US\$124bn, in order to hold this key level for the cross. However, they have not intervened in the currency market since 2022. The market was holding the line itself until the realization post-data release that no intervention means 150 is no longer a ceiling for USD/JPY.

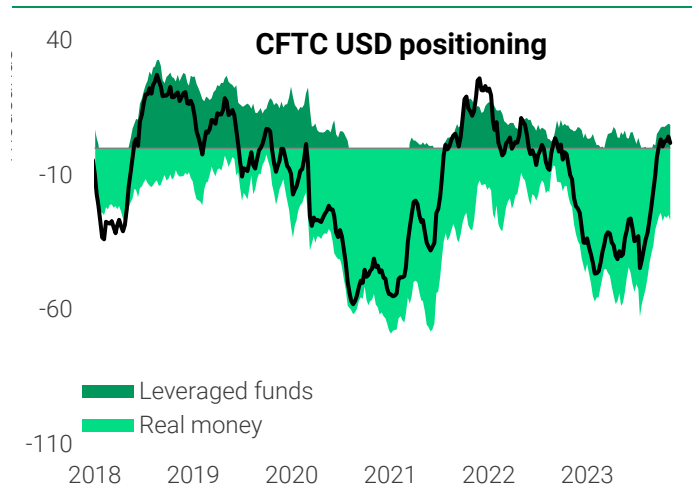
The yen's fate is in the hands of the Fed. Our view has long been that to get sustained USD/JPY downside, we need a turn from the Fed (although the yen is our favoured long when that turn comes). In part, this is because it is what historical experience tells us: it wasn't unilateral FX intervention in 2022 and 1998 that allowed the yen to strengthen; it was a turn from the dollar. A dovish Fed reduces the yen's carry disadvantage and provides an opportunity for the BoJ: waiting until the pressure on DM yields is downwards to tighten policy lowers the risk of a spike higher in yields.

Intervention held 150 last year



Sources: GlobalData TS Lombard, Bloomberg.

Positioning chased the dollar rally



Sources: GlobalData TS Lombard, Bloomberg.

USD strength will re-emerge. Over the past month, the dollar has been under pressure: the first leg down saw USD failing to respond to fundamental drivers, while the second leg down has been triggered by a soft inflation print bringing forward Fed cuts. Certainly, the move can be attributed

in part to sentiment and positioning having rapidly shifted from being bearish USD to chasing the rally. The recent squeeze will likely have cleared out some of that positioning. Additionally, FX intervention is mechanically preventing dollar upside in some crosses. In particular, Beijing had made the 7.32 level a policy priority; however, with USD/CNY at 7.24, strong intervention now seems unlikely. Japan was assumed to be an offender, too (see above).

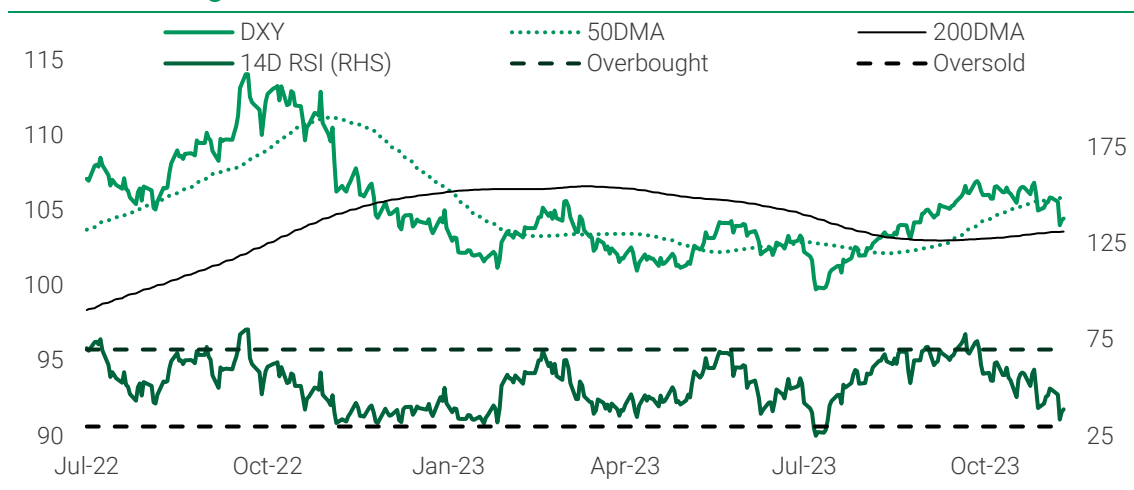
Going forward, we expect fundamentals to reassert themselves in FX markets. US exceptionalism will support the dollar, in part as it contributes to US FI underperformance (see FI section). Yes, disinflation has allowed Fed cuts to be brought forward; but the move has ignored the relative nature of FX. The European and UK economies are stagnating and will see disinflation accelerate into 2024. Thus, our base case is that the ECB and the BOE cut before the Fed. As this backdrop gets priced in, we expect upside pressure on DXY.

Technically, DXY looks to be reaching oversold levels from which it is bouncing, after failing to cross its 200DMA to the downside (see chart below). That means upward pressure on USD/JPY, where 149 is becoming a floor, as the cross remains in its YTD uptrend. The next test is the October 2022 highs of 152 before the cross reaches for 155. **We downgrade JPY to -1 from 0.**

We upgrade KRW to 0 from -1. The semiconductor cycle is beginning to turn positive, providing a tailwind for exports. Rate differentials are likely to improve, too, as the BoK maintains a more hawkish stance than that of the Fed.

We upgrade BRL to +1 from 0. Brazil's tax reform is far from ideal but nonetheless will simplify the current byzantine system and should still have a positive impact on GDP and productivity. High interest rates will support the currency even as Banco Central guides expectations away from rapid monetary easing.

DXY is bouncing from oversold levels



Sources: GlobalData TS Lombard, Bloomberg.

Currencies Scoreboard

(Scoreboard primer)

FX RANK		Momentum		Carry	Surprise Index		Valuation		Positioning		NTM GDP f/c	CA
		direction	accel.	3m chg	level	1m chg	REER level	1y chg	level	1m chg	3m chg	1y chg
1	JPY											
2	GBP											
3	AUD											
4	USD											
5	NOK											
6	CHF											
7	NZD											
8	SEK											
9	EUR											
10	CAD											

As of 16-Nov-23

Currencies dashboard

FX	12m	Spot chg		REER chg			Policy	Inflation		CA %GDP		ToT		Money grth		Budg.	Debt	GDP
spot	fwd	ytd	y-y	ytd	y-y	ZScr	Rate	Rate	Target	Last	ZScr	Last	ZScr	Narrow	Broad	%GDP	%GDP	y-y
USD	104.49	-	0.93 -1.69	1.2 -0.2	2.0	5.50	3.2	2.0	-3.2 -0.9	-13.5 -0.3	22.9 -3.6	-6.1	126	2.9				
EUR	1.084	1.102	1.29 4.31	3.0 3.6	0.6	4.00	2.9	<2.0	0.2 -1.6	-9.5 -0.4	-9.9 -1.2	-3.6	90	0.1				
JPY	151.3	143.1	-13.32 -7.78	-11.0 -7.4	-2.1	0.10	3.0	2.0	2.9 -0.6	-33.4 -0.6	9.0 2.4	-4.3	216	1.2				
GBP	1.239	1.242	2.5 4.0	4.4 4.1	1.5	5.25	4.6	2.0	-1.8 1.0	4.7 -1.2	-	-3.9	195	0.6				
CAD	1.373	1.365	-1.26 -2.90	0.4 -3.2	-0.6	5.00	3.8	1.0-3.0	-1.0 0.8	9.6 0.2	-4.9 5.8	-0.5	72	-0.2				
AUD	0.648	0.652	-4.92 -3.90	0.1 -1.1	-0.2	4.35	5.4	2.0-3.0	1.2 0.6	41.1 0.6	-13.6 5.1	-2.7	69	2.1				
CHF	0.890	0.856	3.89 6.16	2.7 2.7	1.2	1.75	1.7	<2.0	9.8 1.4	-9.6 -0.8	-23.1 -2.7	0.4	21	0.5				
SEK	10.603	10.463	-1.6 -1.15	-0.7 -0.2	-1.7	4.00	6.5	2.0	5.0 0.4	-9.3 -1.3	-7.7 -4.2	1.1	44	-1.0				
NOK	10.862	10.779	-9.74 -7.91	-8.5 -9.6	-1.7	4.25	4.0	2.5	25.8 1.7	95.9 0.8	-1.5 -1.5	16.2	37	-9.2				
SGD	1.350	1.326	-0.74 1.53	4.0 4.6	2.7	N.A.	4.1	-	18.1 0.5	-8.5 -0.7	-3.6 4.1	8.6	153	0.7				
CNY	7.250	7.070	-4.85 -2.10	-5.4 -5.2	-1.5	4.35	-0.2	3.5	1.8 0.5	-26.1 -0.7	10.2 10.3	-4.7	47	4.9				
BRL	4.860	5.054	8.65 10.96	9.5 9.9	-0.3	12.25	4.8	2.5-6.5	-2.7 -0.4	13.1 1.2	2.8 10.9	-7.6	101	3.4				
INR	83.24	84.59	-0.60 -2.32	4.9 0.3	1.4	6.50	-0.5	2.0-6.0	-1.7 -0.6	-43.9 -0.5	6.4 11.0	-6.8	47	4.7				
ZAR	18.34	18.92	-7.10 -5.85	-3.4 -3.2	-0.8	8.25	5.4	3.0-6.0	-1.4 -0.2	20.1 0.4	15.8 7.7	0.2	53	1.6				
MXN	17.29	18.37	12.8 11.8	15.0 13.3	2.2	11.25	4.3	3.5	-1.2 -0.4	11.7 0.4	6.4 9.2	-6.2	54	3.3				
KRW	1297	1271	-2.42 2.20	1.4 3.8	-0.9	3.50	3.8	2.0	0.5 -2.3	-35.1 -0.7	-1.7 2.6	1.7	46	1.4				
TWD	32.01	30.55	-4.03 -2.84	0.7 -0.7	-0.2	1.88	3.1	-	11.9 -0.8	-18.6 -0.8	3.1 6.0	0.0	36	2.3				
HKD	7.802	7.767	-0.01 0.29	3.0 1.3	1.3	5.75	2.0	-	9.3 0.8	0.3 0.3	-19.2 2.3	N.A.	N.A.	N.A.				
PHP	55.78	55.94	-0.08 2.83	6.2 7.3	1.5	6.50	4.9	3.0-5.0	-3.3 -1.0	-16.2 -0.3	17.7 23.7	-2.0	40	5.9				
PLN	4.030	4.060	8.57 12.13	10.0 11.5	2.4	5.75	6.6	1.5-3.5	0.7 0.6	-6.1 -0.1	-8.6 8.3	-3.7	51	0.4				
CZK	22.54	22.53	0.08 3.90	3.6 5.6	1.7	7.00	8.5	1.0-3.0	-4.2 -1.4	-9.0 -0.3	12.3 9.4	-3.2	35	-0.6				
HUF	346.9	357.0	7.61 13.61	11.2 16.2	1.7	12.25	9.9	3.0	-5.1 -1.1	-6.1 -0.3	42.3 -2.5	-6.2	96	-0.4				
TRY	28.670	40.975	-34.7 -35.1	5.4 5.8	-0.8	35.00	61.4	5.0	-5.7 -1.2	-22.4 -0.5	N.A. N.A.	1.5	42	3.1				
IDR	15545	15655	0.15 0.37	3.2 1.3	-0.1	6.00	2.6	3.5-5.5	0.7 1.3	-3.1 0.0	7.0 6.0	-1.8	43	4.9				
THB	35.47	34.39	-2.43 0.63	-1.6 -1.2	-0.6	2.50	-0.3	0.5-3.0	-1.4 -1.1	-22.4 -0.3	4.1 1.8	0.3	50	1.8				
MYR	4.688	4.589	-6.05 -3.04	-4.2 -3.1	-2.2	3.00	1.9	-	3.3 0.3	-4.1 0.4	1.9 2.9	-4.4	62	3.3				
CLP	888.0	902.0	-4.15 2.56	-1.6 0.8	-0.4	9.00	5.0	2.0-4.0	-4.0 0.3	34.9 0.7	-9.1 4.7	-0.3	24	-1.1				
COP	4023	4326	20.63 20.79	28.3 27.7	0.0	13.25	10.5	2.0-4.0	-5.1 -0.5	60.0 0.8	N.A. N.A.	-5.4	90	-0.3				

ZScr is the number of standard deviations from the 7.5-year avg (numbers below/above -1/1 highlighted). All figures % unless stated otherwise.

REAL ESTATE

Andrew Lawrence

- Global real-estate total returns fell 5.6% in 3Q23, dragged down by higher long-term bond yields
- At the regional level, North America (-7.2%) underperformed both Asia (-4.2%) and Europe (+1.3%)
- On a global basis, no real estate sector produced a positive total return in 3Q23, but with rates now peaking 4Q23 should see better real estate returns

The FTSE EPRA/NAREIT Global Developed Total Return Index fell 5.6% in 3Q23, having started the quarter on the hope of an economic soft landing. Higher long-term bond yields and the realization that rates may remain higher for longer caused a sector sell-off into the end of the quarter. Property stocks underperformed global bonds (Bloomberg Global Index), which were down 3.6% in the quarter, and global equities (MSCI World), which ended the quarter 3.4% lower. Year-to-date global property total returns (as of end 3Q23) were down 4.1%.

North America was the worst-performing region in 3Q23, with stocks falling 7.2%. US real estate stocks were down 7.2%, while those in Canada were 8.7% lower. Over the quarter, relatively better economic growth than in other regions translated into a rise in real rates and a steepening of the yield curve, which was reflected in a fall in interest rate-sensitive real estate stocks. In the North American market, office was the only sector to provide positive returns, while the weakest performance was from storage and apartments. Following a 24.8% decline in 2022, North America property stocks are now down 2.3% year to date.

The FTSE EPRA/NAREIT Developed Europe index was up 1.3% in 3Q23. Continental Europe was up 3.4% on the quarter, while the UK Index fell 2.7%. Within Continental Europe, weak economic data were seen as positive for interest rate-sensitive stocks, paving the way for more easing in monetary policy. Leveraged German residential stocks staged a recovery after their earlier sell-off. In the UK, self-storage stocks were the worst-performing sector on the back of negative operating data, rising mortgage rates and concerns about a material housing-market downturn. Europe, the worst-performing region in 2022 (-40.4%), is now down 4.2% year to date.

Total returns for Asia fell 4.2% over 3Q23. Hong Kong was again the worst-performing market globally in 3Q23 with total returns of -12.5%, dragged down by slower economic growth and the impact of the US dollar peg. Singapore (-4.7%) and Australia (-9.0%) recorded negative total returns, too, the latter being impacted by significant negative currency movements. Japan managed to produce a small positive return (+1.9%), lifted by a continued rally in the large-cap developers. While the APAC region was the most resilient regional performer in 2022 (-11%), returns so far this year are down 8.7%, making it the worst-performing region year to date.

On a global basis, every real estate sector produced negative total returns in 3Q23. The largest falls were in self-storage (-12.6%), net lease (-11.7%) and life sciences (-10.7%). The best-performing sectors were office (-0.2%), diversified (-1.6%) and homebuilders (-1.9%). The best-

performing sectors year to date have been data centres (+16.4%), on optimism that AI will lead to better earnings and single-family homes (+9.6%) on the back of strong leasing trends and homebuilders (+3.6%). The worst performers year to date are the life sciences (-18.4%) and the net lease (-14.3%) sectors.

As inflation rates fall and central banks put interest rates on pause, real estate stocks should benefit from a year-end rally. Many private real-estate funds are still seeing their marked-to-market valuations catching up with the falls in market prices, but the pace of re-pricing is slowing. Looking forward investors are likely to focus on the pace of any rate cutting and the potential for softening in occupier demand as the lagged effect of monetary tightening starts to kick in for real.

Chart 1: FTSE EPRA Nareit – Global TR



Source: Bloomberg

Chart 2: FTSE EPRA Nareit – Europe TR



Source: Bloomberg

Chart 3: FTSE EPRA Nareit – Asia Pacific TR



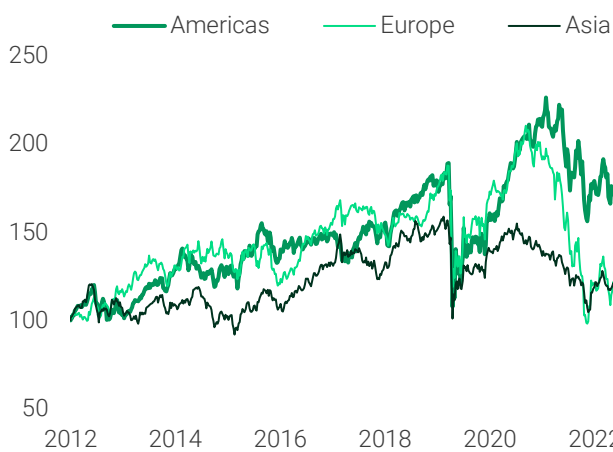
Source: Bloomberg

Chart 4: FTSE EPRA Nareit – Americas TR



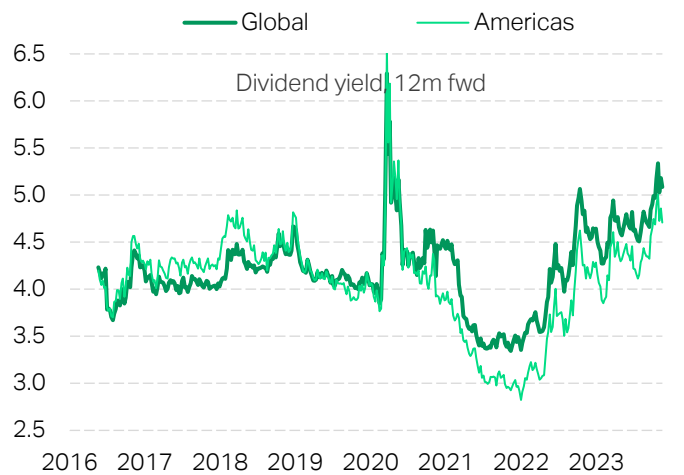
Source: Bloomberg

Chart 5: FTSE EPRA Nareit – Rebased TR



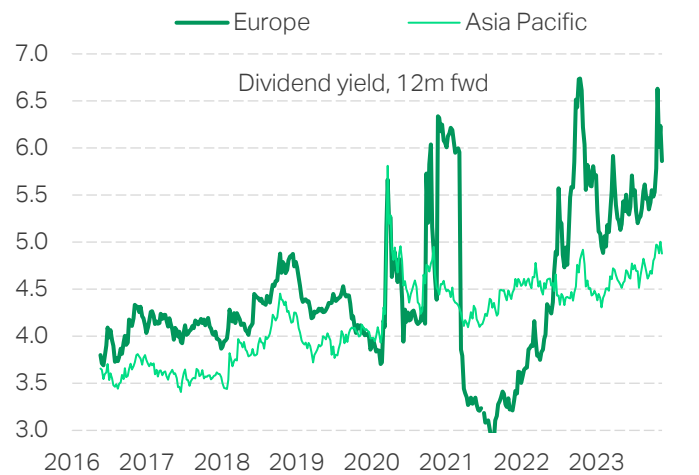
Source: Bloomberg

Dividend yield: Global and Americas



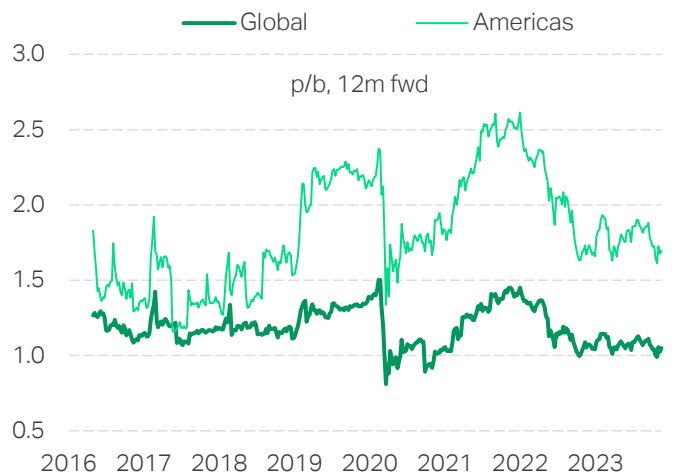
Sources: FTSE EPRA/NAREIT, Bloomberg

Dividend yield: Europe and Asia Pacific



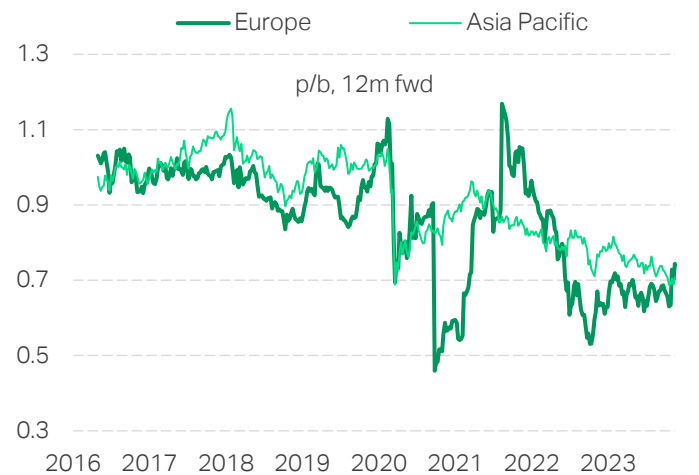
Sources: FTSE EPRA/NAREIT, Bloomberg

Price-to-book: Global and Americas



Sources: FTSE EPRA/NAREIT, Bloomberg

Price-to-book: Europe and Asia Pacific



Sources: FTSE EPRA/NAREIT, Bloomberg

Real Estate Dashboard

	MktCap		Total return (US\$)			P/E (x)			P/B (x)			RoE			EPS growth		Dividend yield		
	Mem.	(US\$)	1m	ytd	2022	Trail.	Fwd	ZScr	Trail.	Fwd	ZScr	Trail.	Fwd	ZScr	Fwd	3m	Trail.	Fwd	ZScr
Global	496	1,994	3.3	-1.7	-23.6	29.1	20.4	-0.4	1.1	1.1	-0.4	1.6	2.9	-1.3	-39.3	-3.0	4.4	4.8	1.7
America	151	1,020	1.7	0.6	-24.4	37.4	30.8	-0.9	1.7	1.7	-0.1	5.3	5.5	0.6	-55.6	0.4	4.4	4.6	0.9
Europe	115	268	11.4	5.3	-40.2	19.7	14.9	-1.1	0.7	0.7	-0.6	-8.9	-4.9	-2.0	N.A.	2.1	4.0	4.7	0.0
Asia Pacific	195	650	3.4	-9.6	-12.4	21.5	14.6	1.2	0.7	0.7	-1.8	2.6	4.4	-2.5	3.9	-16.8	4.6	4.8	1.7

ZScr is the number of standard deviations from the 7.5-year avg (numbers below -1 and above 1 highlighted). All figures % unless stated otherwise. P/e, p/b, RoE and DY StDev from 7.5y average are on 12m forward measures. EPS growth is forward / trailing. EPS 3m growth is on forward earnings.

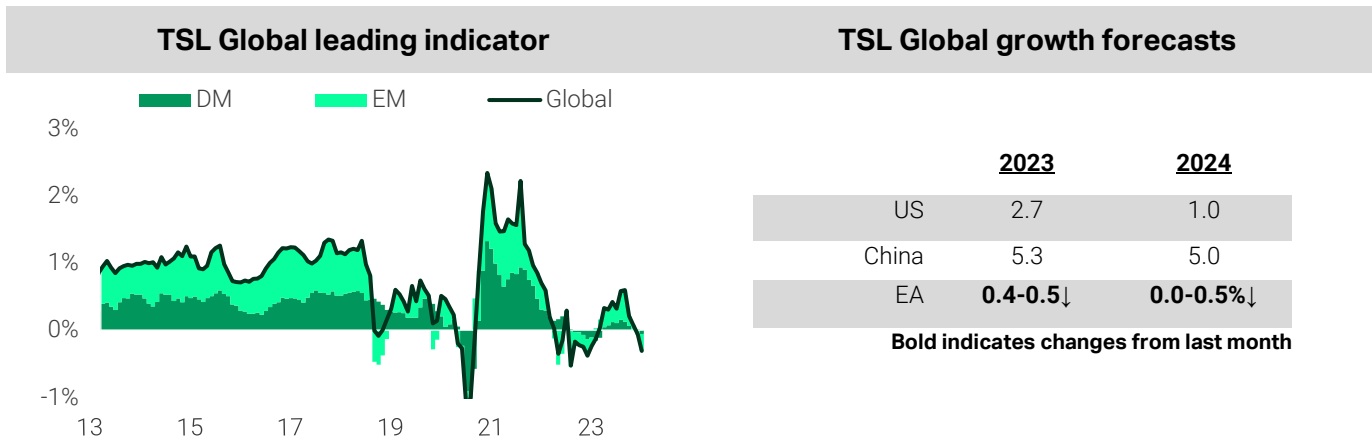
MACRO OUTLOOK

Global Team

- The high-frequency data continue to point to a world economy that is holding up but is short of impetus – a message consistent with the price action in commodities.
- Disinflation in 2024 will reflect weak growth rather than being the immaculate variety that benefitted equity markets in 2023 H1.
- The big question for investors is whether global earnings will prove strong enough to lift equities to new highs even as the threat from rising interest rates is set to subside – ultimately a question about whether the US economy can achieve a “soft landing.”

[Read more in the latest Global Macro Monthly](#)

Global macro at-a-glance



- ### US in the driver's seat

 - For the US, the question is whether the 2023 Q4 slowdown devolves into recession or the economy's resilience requires another round of Fed hikes to ensure a downturn and 2% inflation.
 - In Europe, downside surprises in both the hard data and leading indicators continue to dominate.
 - Beijing continues to ramp up its stimulus measures, adding conviction to our call for an "L-shaped" recovery beginning this quarter..

Major risks

 - Sustained simultaneous strength in bond yields, USD and oil persists, raising the chances that "something breaks" and precipitates a deeper economic slowdown.
 - Central banks continue to be whipsawed into aggressive monetary tightening, amplifying the volatility of this fake cycle and raising the risk of a global recession.
 - Financial market dislocation and/or sharp deterioration of labour market conditions trigger an abrupt policy U-turn.



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