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CIO Office Viewpoint

Ten Investment Convictions for 2024

Investment Solutions

5 December 2023

In 2024, investors must balance the lingering effects of high interest rates leading to slower growth, against welcome disinflation, and the risks around geopolitical tensions.

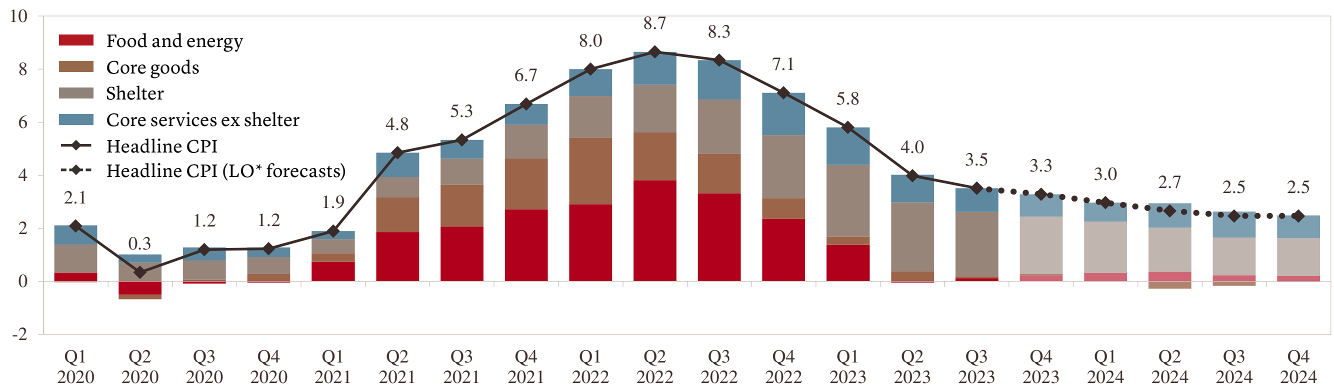
Despite recent progress, the path to a soft economic landing remains challenging. The historical evidence argues against ruling out a recession, but we do not expect to see a severe US downturn this time. After a dramatic 2022, bonds have remained volatile in 2023. Peaking yields and slowing growth would be positive for high quality fixed income in 2024. It would also lend some support to investor risk appetite, and equity markets, but we expect material volatility in the first half of 2024.

High interest rates should remain in place at least through the first half of 2024. The European Central Bank may be the first to cut interest rates mid-year, with the Federal Reserve (Fed) following suit in September 2024. The global economy should then start to benefit from lower borrowing costs. If inflation proves sticky, or strong growth persists, that scenario would be at risk and put bond and equity valuations under pressure. Meanwhile, restrictive financial conditions and slowing growth will continue to add pressure to indebted corporate borrowers, including some governments. We think bonds represent one of the strongest risk-adjusted opportunities in what we expect to be a volatile 2024.

Equities' performance in 2023 was strong, but also exceptionally narrow, as a few names accounted for almost all of the S&P 500's gains. Granted, corporate earnings were under pressure, and experienced a mild recession. We think there is room for some recovery as results stabilise, making US stocks a core portfolio holding for next year. Valuations are now above long-term averages and markets expect an earnings expansion of around 12%, plus as many as five US interest rate cuts in 2024. We see fewer rate cuts and lower earnings growth of around 6%, along with some improvement in profit margins and broadly unchanged valuations. Positive equity returns are a typical feature of late-stage economic cycles, but this is often accompanied by higher volatility.

Successful disinflation should allow central banks to adjust policy

Contribution to headline US consumer price index (CPI), key segments, in % year-on-year



Sources: Bloomberg, * Lombard Odier calculations/forecasts

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Monetary policy and economic growth will remain key drivers of financial markets in 2024. However, we do not underestimate the risks from geopolitics, energy, strategic competition between the US and China, and a high-stakes, highly-polarised US presidential election.

Our investment strategy continues to manage these various challenges, actively taking advantage of the investment opportunities as they arise.

Michael Strobaek
Chief Investment Officer

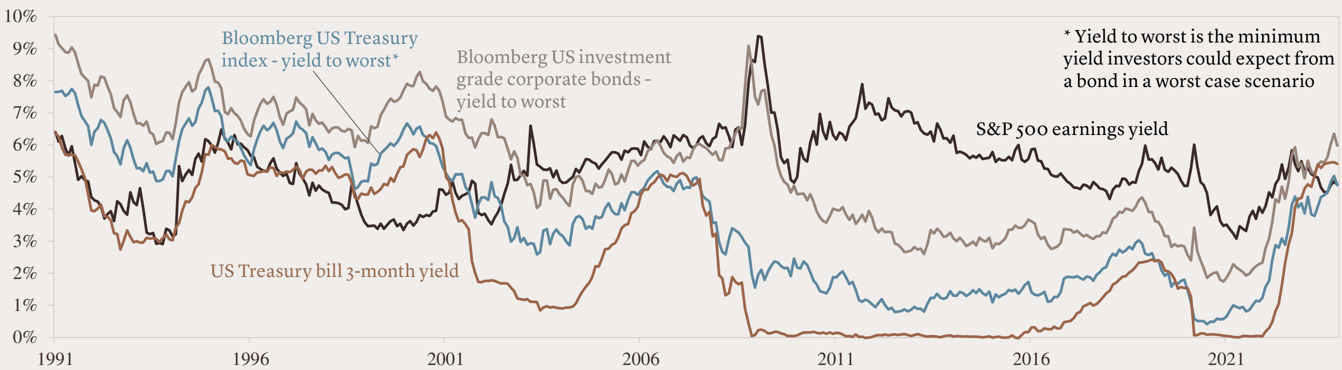
Christian Abuide
Head of Asset Allocation

Investment views going into 2024

Portfolio Risk Maintain a neutral stance	**1. We maintain a neutral overall risk stance in portfolios** We balance disinflation and mixed economic data against tight credit conditions and risk-asset valuations consistent with a soft landing. A mild recession is possible in 2024, but should not be too detrimental for risk assets over this time horizon. We want to position for a range of economic and market scenarios, and by doing so, privilege portfolio diversification and quality assets.
Cash and fixed income Prefer high quality bonds	**2. Cash and long-dated bonds offer yield and diversification** We favour fixed income in multi-asset portfolios. Peaking interest rates and a slowing economy should favour high quality fixed income, which should also offer some diversification benefits to portfolios, particularly in a downturn. We like longer-dated government bonds, where we have gradually built exposure, and prefer US Treasuries.
	3. Prefer investment grade credit in developed markets The potential for a longer cycle of high rates, limited corporate issuance and demand for all-in-yields has kept spreads (or the credit risk premium paid) tight, although dispersion and defaults should rise modestly. We favour the attractive yields and resilience offered by investment grade credit, which is competitive with equities for the first time in many years.
	4. In riskier bonds, prefer high yield and emerging local debt over hard currency bonds High yield income is attractive, and demand will remain. But refinancing risks are rising and so are defaults, while the risk premium is average, so we retain a preference for the top layer of credit quality. In emerging market local debt, select opportunities offer return and diversification potential to benefit from attractive yields and potential price gains from rate cuts – here we favour Brazil. In contrast, we remain negative on Chinese government debt, where yield differentials are not attractive, and there is room for the yuan's weakness to persist.

Equities face competition in the short term

For total return investors

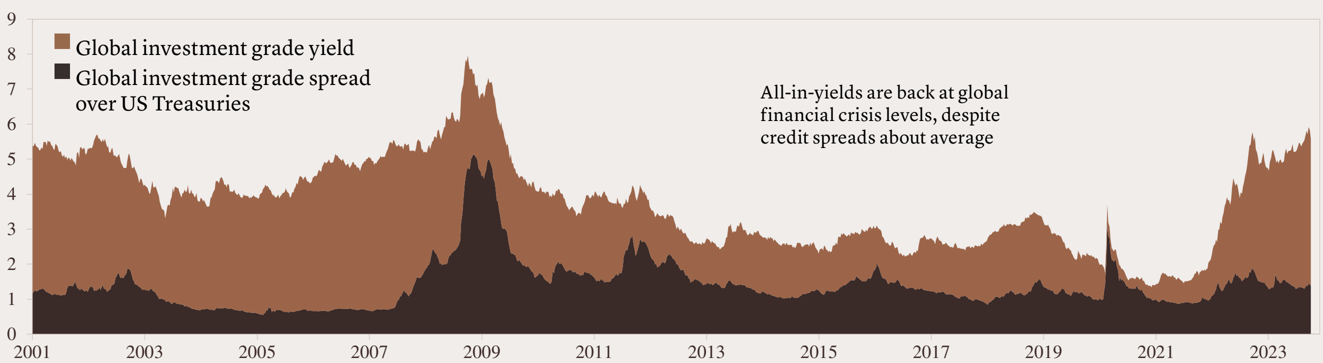


Source: Bloomberg

Equities Remain overall neutral	**5. Equities can offer upside; take advantage of corrections** We are neutral in equities, but see potential opportunities from differentiation. Equities are likely to be supported by mid-single-digit earnings growth and rate cuts in the second half of 2024, but growth is slowing and valuations appear, on aggregate, demanding versus other asset classes. Equity markets can deliver positive – although very volatile - returns in the late stages of an economic cycle. Such a scenario would be consistent with a gradual rise in equity indices, but also with a quality bias given lingering uncertainty over the macroeconomic backdrop.
	6. Prefer US over China and Europe regionally, and quality stocks generally We favour companies that combine quality and growth characteristics. Quality stocks have historically outperformed other factors in late-cycle markets. Within defensive stocks we prefer consumer staples and telecoms. The US, where we see a 6% rise in earnings per share in 2024, remains a core portfolio holding given earnings outperformance and the market's exposure to quality growth sectors. We remain neutral on emerging market and European equities, despite their attractive valuations, as growth there could be more challenged.
Currencies USD to be supported over H1	**7. The US dollar is likely to see a recovery heading into 2024** A US soft landing amid sluggish growth elsewhere should see the US dollar (USD) maintain both yield and growth advantages versus peers. However, a harder US landing would likely trigger safe-haven demand, at least until the Fed responds with significant policy easing. Any USD weakness could come from an improvement in global growth, likely led by China, although not before the second half of 2024.
Commodities Short-term gold prices at risk	**8. Commodities present opportunities in a broad portfolio context** Short term, we see gold prices challenged by markets reducing their expectations of aggressive US interest rate cuts, and a normalising geopolitical risk premium. By mid-2024, we expect a gradual price rise to USD 2,100/oz. Copper should see some medium-term support from still tight supplies. Brent crude oil should trade in a USD 80-90 per barrel range, with down-side risks.
Alternatives Macro and trend following strategies diversify, private assets can strengthen portfolios	**9. Alternative strategies for income and diversification** Macro and trend-following hedge fund strategies look positioned to benefit from return dispersion. For eligible clients, alternative investment strategies can offer risk-controlled opportunities to participate in markets and/or hedge positions, taking advantage of current low equity and currency market volatility.
	10. Private assets to strengthen long-term portfolios For investors with an appropriate time horizon and risk tolerance, private assets can help diversify portfolios further and offer an additional return and liquidity premium.

Investment grade credit remains attractive

Yields on offer and spread over US Treasuries, in %



Source: Bloomberg

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