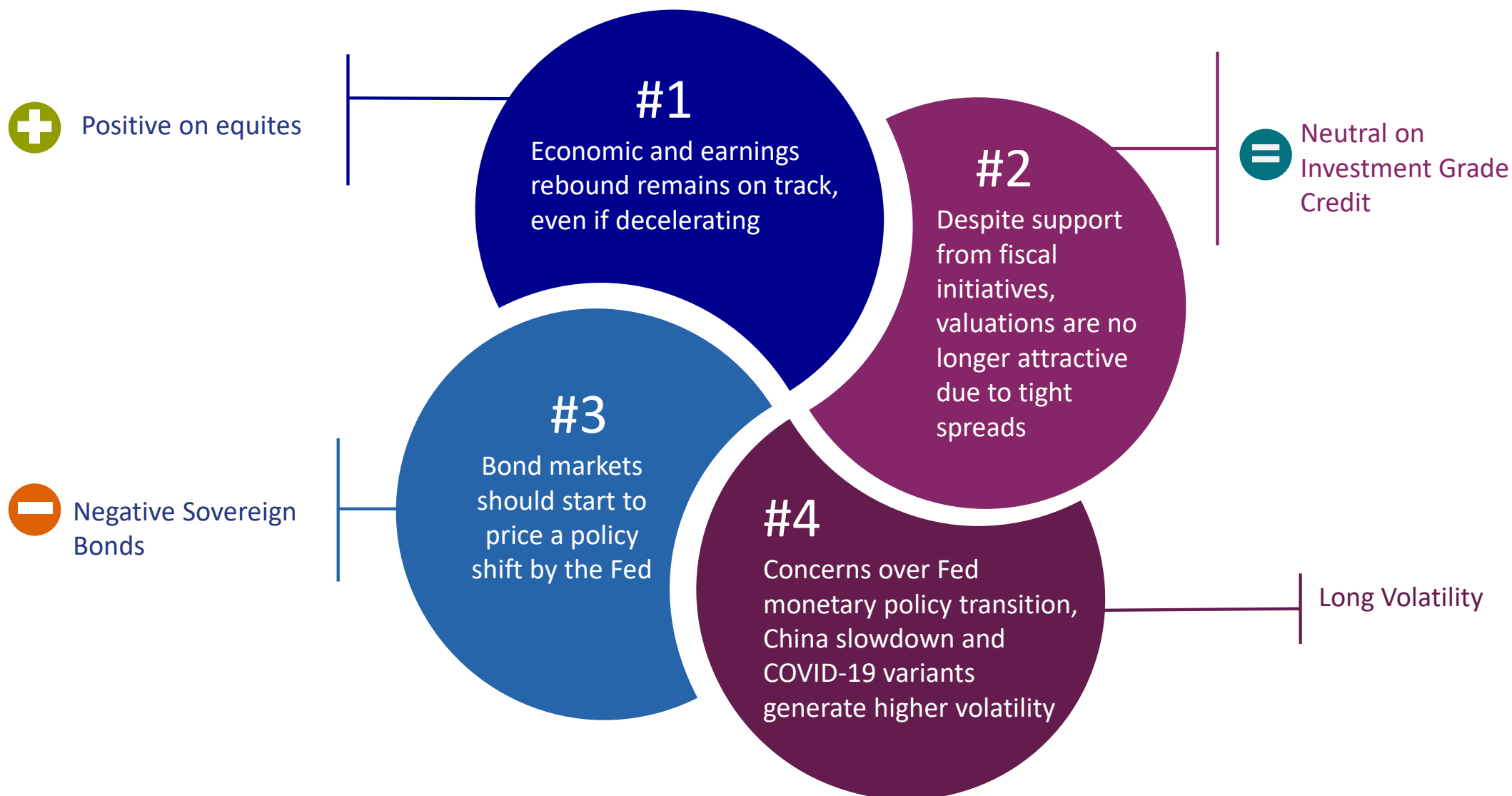


# Multi Asset Allocation Views

October 2021

# Multi-Asset Investment views

## Our key messages and convictions



Source: AXA IM as at 22/09/2021

# Asset allocation stance

## Positioning across and within asset classes

Asset Allocation			
<b>Key asset classes</b>			
Equities			Positive
Bonds	Negative		
Commodities	▼		
Cash			▲

Equities			
<b>Developed</b>			
Euro area			Positive
UK			Positive
Switzerland		Neutral	
US		▼	
Japan		Neutral	
<b>Emerging &amp; Equity Sectors</b>			
Emerging Markets		Neutral	
Europe Cyclical/Value		▼	
Euro Opening basket			Positive
Euro Financials			Positive
US Financials		Neutral	
US Russell 2000		▼	

Fixed Income			
<b>Govies</b>			
Euro core	Negative		
Euro peripheral		Neutral	
UK		Neutral	
US	Negative		
<b>Inflation Break-even</b>			
US		Neutral	
Euro		Neutral	
<b>Credit</b>			
Euro IG		Neutral	
US IG		Neutral	
Euro HY		Neutral	
US HY		Neutral	
<b>EM Debt</b>			
EM Bonds HC		Neutral	

Legend

Negative

Neutral

Positive

Change

▲ Upgrade

▼ Downgrade

Source: AXA IM as at 22/09/2021



# Central & alternative scenarios

## Persistent recession

↑ 20%\*

## Central scenario

↓ 60%\*

## Fast recovery

20%\*

- Coronavirus mutations reduce vaccine effectiveness
- Labour market dislocation and business disruption headwinds to demand recovery
- Fiscal policy fades amidst elevated debt and political opposition
- Geo-political tensions mount post-Covid
- Growth/inflation expectations weaken further, corporates' earnings under more pressure
- Further monetary policy where space permits (including China). Governments continue with fiscal stimulus and divide between monetary financing blurs further.

- 2021 rebound as virus controlled, but recovery needs policy support. Global growth forecast to rise by 5.7% in 2021 and 4.4% in 2022.
- Economic rebound on vaccine and stimulus, must overcome labour market and indebtedness headwinds
- Monetary and fiscal policy will remain key policy support. Fed tone turned more hawkish but all central banks will be wary of withdrawing support too quickly.
- US spending in flux, expecting large package in Q4. In Europe and UK fiscal support rolled out more slowly.

- Vaccine rolls out more quickly than expected, governments allow virus to run unchecked achieving collective immunity
- Labour market recovers, economies benefit from post-virus euphoria and faster consumption of 'excess saving'
- Virus-shock reshapes business practice, boosting productivity
- Global/US/EMU growth surprises to the upside in a stronger and more persistent rebound from 2020
- Monetary policy fights expectations for swift tightening through forward-guidance

- **Equities:** Risk appetite deteriorates / equities sell off
- Safe haven **government bonds** rally resumes
- **Credit** spreads to widen
- EM debt to come under pressure

- **Equities:** Corporate earnings 2021 rebound on track. Value/Growth rotation still at play. Equity risk premium has compressed.
- **Government bonds:** Rates stable as technical offset growth and inflation outlook for now. Macro argues for higher rates- technical to persist over the summer
- **Credit:** Tight spreads belie higher corporate debt levels.

- **Equities:** Risk-on environment with equities making further gains amidst broader rotation
- **Government Bonds:** US and EUR break-even rates rise
- **Credit:** Spreads grind tighter

\*Probability for each scenario according to AXA IM as of 22/09/2021. Those expectations are provided for illustration purposes only. They are hypothesis based on data made public by official providers of economic and market statistics. AXA Investment Managers Paris disclaims any and all liability relating to a decision based on or for reliance on this document

Change of the month: Upgrade ↑ Downgrade ↓

# Setting the scene: our global economic outlook

## Signs of decelerating growth amidst supply bottlenecks, Central Bank evoke shift in monetary policy

- **In the US, we lowered our growth outlook for the 3<sup>rd</sup> quarter as consumption slows.** The uptick in Covid cases may have impacted the expected goods for services rotation. The recent surge in inflation should have peaked but its persistence will depend on how quickly the supply shocks are absorbed. **We revised our 2021 GDP growth forecast to 5.7%, from 6.2% previously, but expect 2022 to rise by 4.3%.**
- **In the Euro area, 70% of the population is fully vaccinated. Economic activity benefited from a solid momentum in the 3<sup>rd</sup> quarter after a strong 2<sup>nd</sup> quarter.** Both Services and Manufacturing sectors contributed to stronger economic activity despite negative drag from the auto sector. **We upgraded our GDP growth to 4.7% in 2021 and 3.9% in 2022.**
- **In China, the mobility restrictions resulted in weaker growth as consumer spending dropped.** A rebound in consumption and services was expected but a new Covid cluster clouds the outlook. Industrial output has held up so far but expect weaker exports. **There's downside risk to our 8.5% forecast for 2021 but maintain 5.5% in 2022.**
- **EM economic recovery was off to a positive start but the Delta variant proved to be a hurdle for Asian recovery in the 2<sup>nd</sup> quarter.** EM domestic demand may be affected by tighter monetary policies whilst exports normalise.
- **Most major central banks continue with their accommodative policy whilst preparing markets for a shift towards tapering.** The US Fed\* more hawkish although reiterating that tapering is dependent on "substantial further progress" despite signalling hikes in 2023. ECB\*\* maintains QE whilst adjusting its PEPP purchases. The BoE\*\*\* reduced its asset purchases. The BoJ\*\*\*\* maintains its monetary policy.

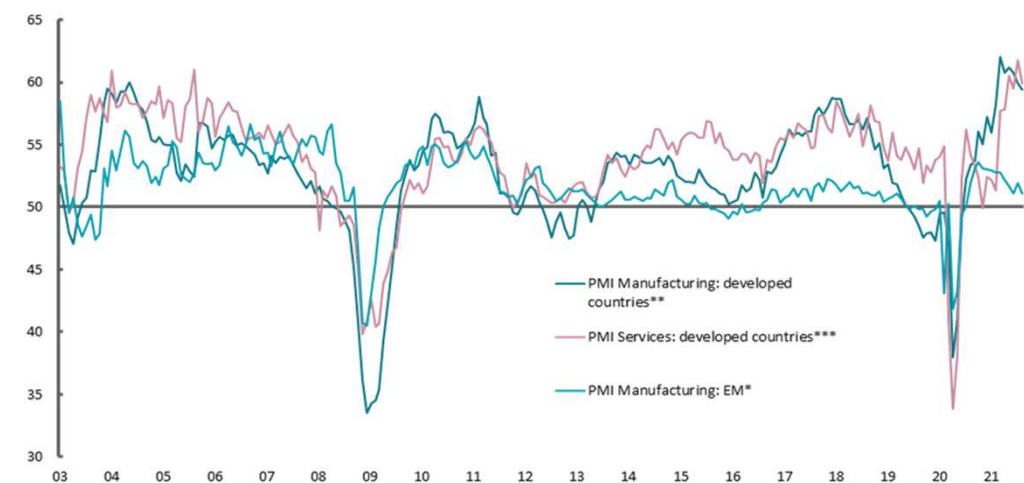
Source: AXA IM, Consensus Economics, IMF and Datastream as at 22/09/2021

\*Federal Reserve \*\* European Central Bank, \*\*\*Bank of England, \*\*\*\*Bank of Japan

## AXA IM Research & Investment Strategy economic forecasts\*

Real GDP growth (%)	2019	2020	2021*	2022*
<b>World</b>	2.9	-3.6	5.7	4.4
<b>Advanced economies</b>	1.7	-5.3	5.1	4.2
US	2.3	-3.4	5.7	4.5
Euro area	1.3	-6.8	4.7	3.9
UK	1.4	-10	6.7	5.7
Switzerland	0.9	-3	3.6	3.3
Japan	0.7	-4.9	2.6	3.3
<b>Emerging economies</b>	3.6	-2.5	6.1	4.6
China	6.1	2.3	8.5	5.5

Global PMI indices  
(national PMI surveys weighted by PPP-adjusted nominal GDP)



\* Poland, Mexico, Chile, South Africa, Russia, China, India, Brazil, Turkey, Hungary, Czech

\*\* US, Euro area, Japan, UK, Australia, Canada, Sweden, Switzerland

\*\*\* US, Euro area, UK, Australia, Sweden

# Overview of asset allocation stance

## Our views:

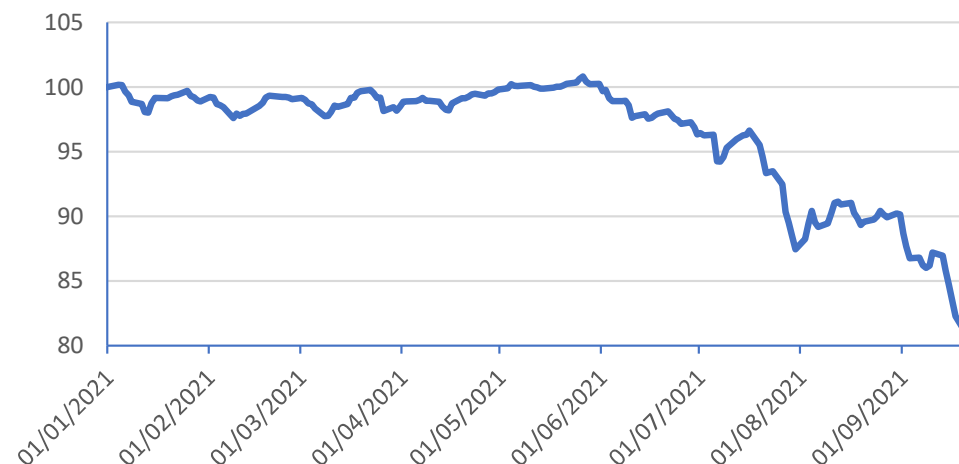
- **Markets are concerned by a wide set of risks**, in particular the crisis in the Chinese real estate sector, decelerating US growth, reduced policy support and COVID variants and waning vaccine efficacy.
- **On China, our baseline remains that any potential default or restructuring of the property developer Evergrande would be carefully managed** by the government with limited contagion effect in both financial and property markets.
- Despite disappointing data in the US, **growth is likely to stay above trend well into 2022**. Pent up demand, very high excess saving, improving labour markets and healthy consumer balance sheets should continue to support demand. However, supply-chain issues could take longer to improve, suggesting a period of weaker activity but followed by more robust growth once supply constraints ease, businesses rebuild depleting inventories and ramp-up in capex
- Policy support will turn less stimulative, but **central bank policies should remain growth-oriented and US households could partially offset the fiscal tightening by spending part of their excess savings**

## Our key convictions:

- **Positive on equities** - Growth should remain significantly above trend in 2021 and 2022, supporting earnings; vaccine roll-out should continue to support market sentiment. Financing conditions should remain highly accommodative
- **Negative government bonds** – The Treasury market is prone to outsized bouts of volatility as investors question the growth and inflation scenarios. Above trend economic activity, rising inflations expectations and less favourable technical factors should push bond yields higher

## China real estate credit has been under strong pressure

**Markit iBoxx USD China Real Estate High Yield cumulative return**



### Key asset classes

Equities			
Bonds			
Commodities			
Cash			

Change

▲ Upgrade

▼ Downgrade

# Equity markets outlook and convictions

## Our views:

- **We remain constructive** – However economic activity whilst robust, is clearly peaking and is now also grappling with the supply chain challenges – be it semiconductor shortage or capacity closures in SE Asia due to numerous local lock downs i.e. ports or factories. These disruptions are being felt across a wide range of sectors and add to inflationary pressures. The question is whether this lost production will be met by demand later.
- **Valuations** look high on an absolute basis. That said, multiples are contracting as earnings grow sharply. The Equity Risk Premium has room to decrease, and Equities look attractive relative to bonds. What is interesting is that cheap stocks continue to derate. Note earnings revisions are slowing.
- **Sentiment** indicators have come off very high levels and the mood is now rather defensive.

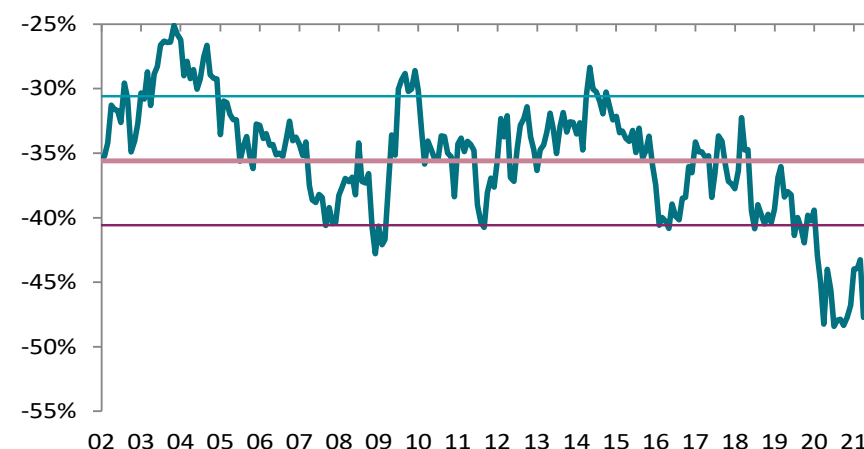
## Our key convictions:

- Positive **banking** sector in the Eurozone which should benefit when yields rise again as is our scenario and valuations are reasonable.
- **Neutralise exposure to European Energy & Materials** despite robust economic activity as momentum peaks
- **Positive on UK domestic stocks** : GDP bounce-back is likely to be very strong while the vaccine rollout continues apace, so far the Delta variant has not had a big impact on activity. UK domestic stocks remain cheap
- Positive **reopening stocks in continental Europe** focusing on travel, retail, beverages and airlines despite some new restrictions
- Neutral **emerging markets** – Vaccine roll out slower, China credit impulse is negative and the global recovery is more services than trade led. Many Local Covid spikes in SE Asia are playing havoc with activity.

Source: AXA IM, Datastream as at 22/09/2021

## Cheap gets cheaper – quid the catalyst ?

Stoxx 600: PE spread - cheapest quintile vs. median



### Developed

Eurozone			
UK			
Switzerland			
Sweden			
US			
Japan			

### Emerging & sector diversification

European cyclicals			
EU Financials			
EU reopening basket			
UK domestic stocks			
US cyclicals/value			
US Financials			
US Russell 2000			

Change

▲ Upgrade

▼ Downgrade

# Government and inflation-linked bonds outlook and convictions

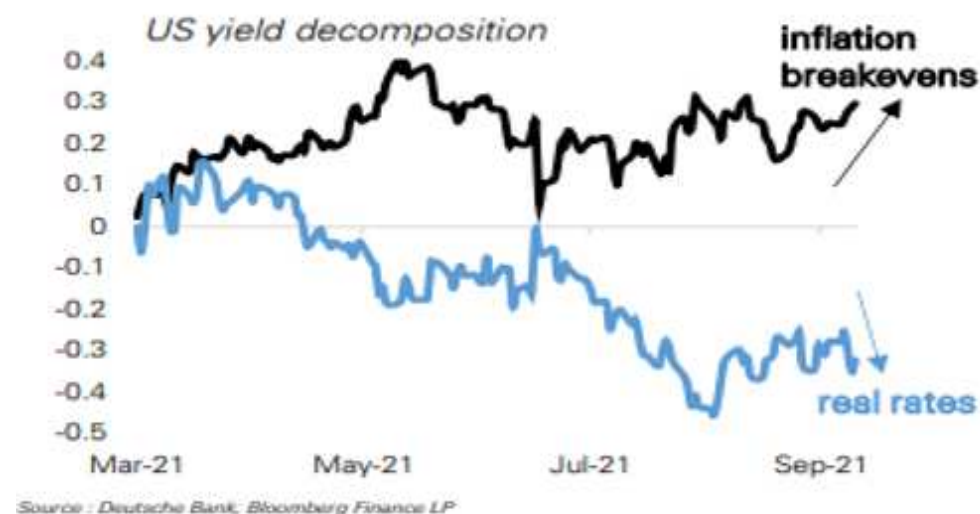
## Our views:

- **Global nominal bond yields** have begun to move gently higher after the early summer move lower on Covid concerns, weakening macro momentum and investors closing out short Treasury positions that were losing money.
- **Inflation break-even pricing** remains well supported with a noticeable catch up in Euro Zone inflation pricing relative to that of the US whilst the UK has outperformed further as the current supply side economic shock is having a more pronounced impact on the post-Brexit economy.
- **Macro (negative)** - weaker momentum should cap expectations for significantly higher bond yields
- **Valuation (very negative)** - marginally improved but remains extremely expensive
- **Sentiment (positive)** - inflows remain strong across fixed income
- **Technicals (negative)** - Central Banks will be shortly reducing monetary accommodation and thus supply/demand relationship changes should favour higher yields although private demand has proved to be very resilient thus far

## Our key convictions:

- **Government Bonds:** Negative US rates with direction of travel higher
- **Inflation Break-evens:** Neutral

## Inflation expectations strong giving yields more upside



### Govies

Euro core	Orange		
Euro periph		Teal	
UK		Teal	
US	Orange		
Japan		Teal	

### Inflation Break-even

US		Teal	
Euro		Teal	

### Emerging

Emerging Markets		Teal	
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Change

▲ Upgrade

▼ Downgrade



# Credit bonds outlook and convictions

## Our views:

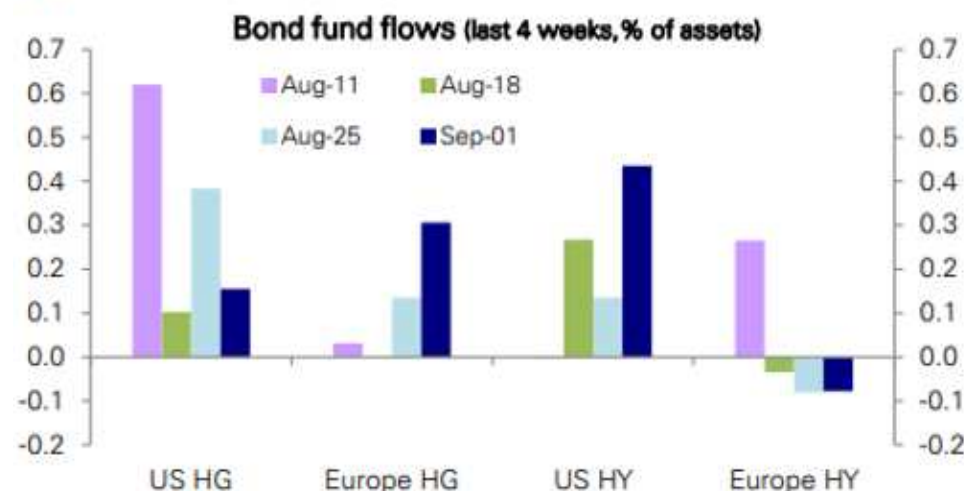
- Credit spreads remain stable as investor flows and a slower summer primary issuance calendar underpin current levels
- Some volatility has been noted in High Yield as average credit quality of new issuers has deteriorated with new names coming to market at a discount to better known issuers
- Higher levels of stress have been noted in Emerging Markets and especially China which has been confined to local names
- **Macro (positive)** - ongoing post lockdown macro recovery with higher profits supports ratings and valuations
- **Valuations (very negative)** – historically tight credit spreads leaves little room for complacency but context skewed by Central Banks
- **Sentiment (positive)** - investor flows reaching for extra yield with risk free yields suppressed
- **Technicals (negative)** – underlying nominal yields should continue to rise gradually as supply/demand dynamics shift

## Our key convictions:

- **Investment Grade:** Neutral
- **High Yield:** Neutral

## Investor flows remain globally positive

Figure 60: Credit fund flows to US and Europe last 4 weeks



Source : Deutsche Bank Asset Allocation, EPFR, Haver Analytics, Data as of 01-Sep-21

### Credit

Euro IG		
US IG		
Euro HY		
US HY		

Change

▲ Upgrade

▼ Downgrade

Source: DB, EPFR, Haver as at 22/09/2021

# Currency market outlook and convictions

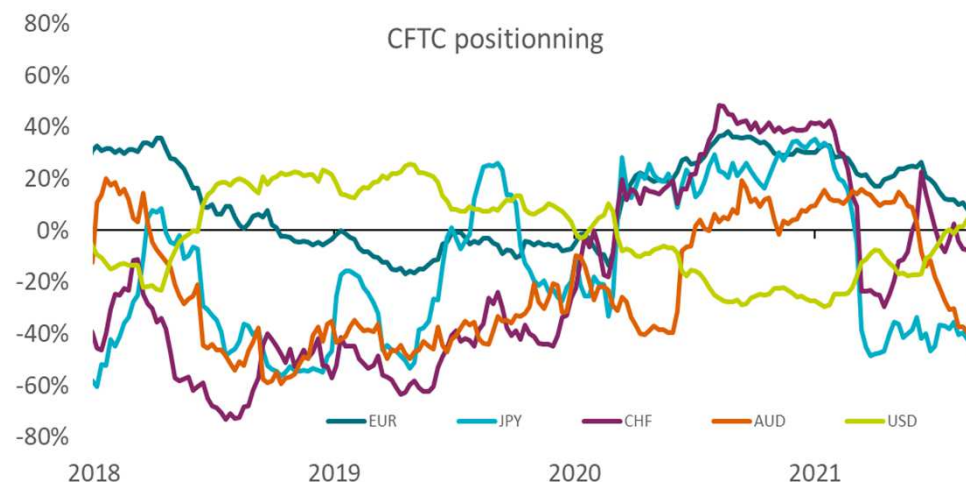
## Our views:

- **USD:** To remain supported versus low yielders. Next FED cycle only timidly priced in. US Congress potentially voting an additional fiscal package. Long term US real rates possibly rebounding as US debt supply recovers in Q4.
- **EUR:** ECB unlikely to follow the FED. German elections probably not resulting in a game changing coalition government for EU fiscal policy.
- **JPY:** Could better resist USD strength. Cheaper than most. Sentiment has been negative for long and could turnaround. Japanese outflows are abated.
- **CHF:** SNB still ready to prevent further EURCHF depreciation not far from current level. Lowest carry and highest valuation.
- **NZD:** RBNZ to raise rates as soon as Q4 : inflation rising, growth rebounding above 2020 level, while house market prices are soaring to 27% YoY.
- **AUD:** RBA to remain dovish as inflation disappoints. Rising doubts on China demand. Prolonged lockdowns with difficulty controlling spread of delta variant.

## Our key convictions:

- We hold a long term **long JPYCHF position**, and a **bullish view on NZDEUR**

USD sentiment leaving negative territory. Market turning bearish AUD. Possible short JPY fatigue ?



## Currencies relative to USD

EUR		▼		CAD		■	
GBP		■		NZD		■	
JPY			▲	NOK		■	
CHF	▼			SEK		■	
AUD		■					

Change

▲ Upgrade

▼ Downgrade

# Commodity market outlook and convictions

## Our views:

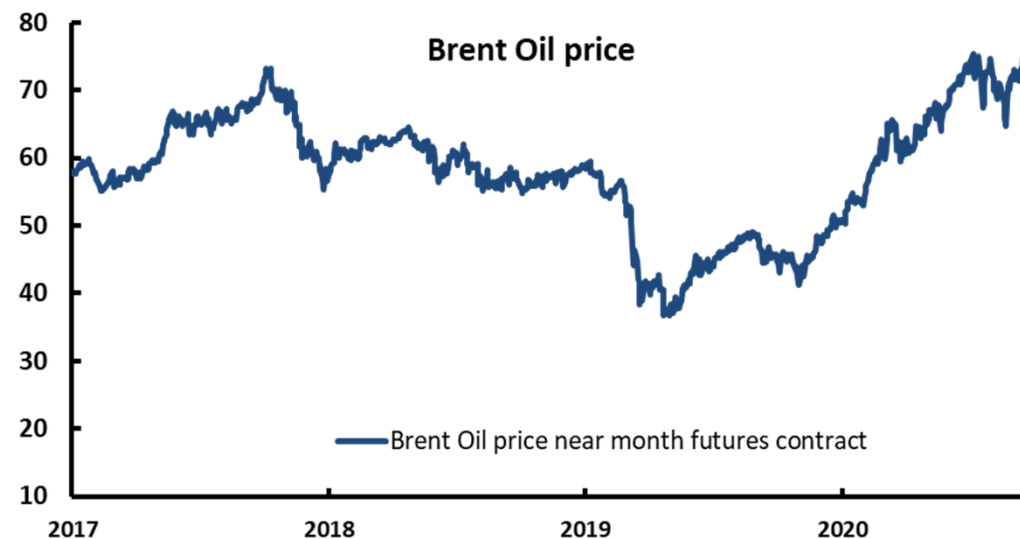
- Demand for cyclical commodities benefited from the recovery in activity **however we expect this momentum to decelerate in line with global economic activity. In parallel, supply is normalising and set to expand further.** Sentiment remains supportive for cyclical commodities whilst technical are close to neutral for most commodities.
- **As the oil price moved back to its previous high, we would adopt a more cautious stance.** We expect demand to recede as we move away from the summer driving season amidst gradually increasing OPEC+ and modestly higher US production.
- **Industrials metals are benefiting from recovering global demand** but we are concerned about weaker demand from China. In parallel, **supply is expected to normalise for some metals (copper)**, in particular from Latin America, leading to a surplus next year. Aluminium's demand and supply dynamics are more balanced but the price at a 13 year high is vulnerable to a correction.
- **The gold price remains anchored by lower real rates and the recovery in jewellery demand.** However, there appetite for Gold as a safe haven is less apparent amidst a headwind from the prospect of higher yields

## Our key convictions:

- Given our expectation of decelerating demand should coincide with increased supply in key commodities (Oil & Copper), we **adopt a negative stance on the commodity complex.**

Source: Bloomberg , AXA IM 22/09/2021

Oil price well above our \$70 target



## Commodities

Oil			
Industrial Metals	▼		
Gold			

Change

▲ Upgrade

▼ Downgrade

# Volatility outlook and convictions

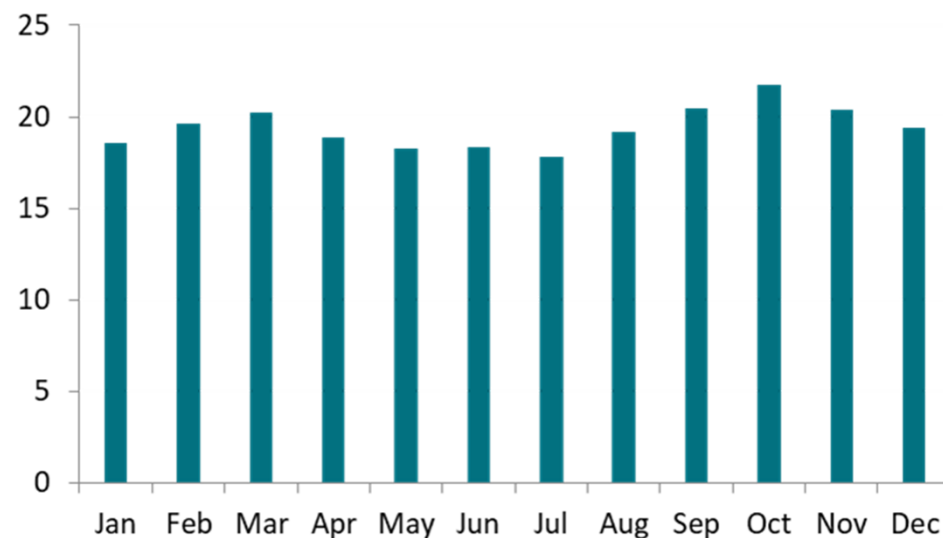
## Our views:

- “**Ghostbuster**”, the flow of news and concerns have fuelled the market since August 21<sup>st</sup> leading to **a progressive increase of the implied volatility in the equity market**. The question of FED Tapering, concern about inflation, the massive leverage of the corporates highlighted by the Evergrande story. As exhibited in the accompanying chart, volatility is usually more pronounced at the start of the 4<sup>th</sup> quarter of the year, coupled with higher inflation, **we believe the current range of the VIX is around 18-22**. Our in-house US Equity volatility model conveys the same message from a macro perspective with a fair value equal to the market level. The FX volatility market remains relatively muted due to pressure from volatility sellers. Lastly, few signs of re-correlation appears on cross-asset implied volatility but still exhibits high dispersion.
- Despite the vol spike on Monday September 20<sup>th</sup>, **the Equity skew for the major markets keeps a high slope**. The term structure has flattened, driven by the front-end curve during the stress but **the term structure still remains steep**, with some dislocations on the 18 Month - 3 Year bucket between the US and EU equity markets. The equity rally has supported **the dynamic "vol up spot up"** pushing the market far away from the vega peak.

## Our key convictions:

- For protection, **benefit from favourable condition in the FX vol market** to complete hedging strategy,
- Maintain **carry equity volatility** strategy and start to re-accumulate around VIX at 28,
- Benefit from the high skew to build **synthetic equity exposure via call** to manage year end performance.

## Monthly Seasonality of the VIX in the last two decades





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