UBS House View

Monthly Extended April 2024

Chief Investment Office GWM
Investment Research

This report was prepared by UBS AG London Branch, UBS Switzerland AG, UBS AG Hong Kong Branch, UBS AG Singapore Branch and UBS Financial Services Inc.

To see our most recent forecasts, please refer to our publication called "Global forecasts "

Please see the important disclaimer at the end of the document.

This document is a snapshot view. For all other forecasts and information, we advise you to check the Investment Views section in your E-Banking or in Quotes.

Published: 21 March 2024

Section 1

Investment views

UBS

Section 1.1

Asset class outlook

Asset class outlook

Global asset allocation

In our global strategy, we keep our preference for bonds over equities.

Within equities, we retain our preference for quality. Our most preferred region is emerging markets (EM).

Within bonds, we prefer high grade and investment grade over high yield and emerging market credit.

Within commodities, we hold a preference for oil.

Within foreign exchange, we have the CHF as least preferred and the AUD as most preferred. We stay neutral on the remaining major currencies.

Equities

Global equities extended their gains in February and March, buoyed by solid macroeconomic data. Led by AI-related stocks, earnings continue to recover, although consensus estimates appear quite optimistic, in our view.

We still expect economic growth to slow from current levels. Inflation risks appear two-sided in the near term but remain skewed lower over the medium term. Hence, lower yields should follow and support equity valuations.

We remain neutral on global equities and expect low-single-digit returns for the remainder of 2024.

Regionally, we prefer emerging markets over the UK.

Bonds

We have a most preferred stance on the higher-quality segments of fixed income given the all-in yields on offer and as central banks transition from rate-hiking to rate-cutting cycles. Specifically, we maintain a preference for high grade (government) and investment grade bonds, and are neutral on high yield and emerging market credit.

Although inflation has printed higher in recent months, we continue to see it on a downward path as the drivers of lower inflation on the goods, rent, and labor market sides remain encouraging. Additionally, financial conditions have eased since the beginning of the year. However, lending standards remain restrictive and hence will continue to transmit into the real economy and apply downward pressure on growth and inflation, and by derivation nominal interest rates. This is a positive driver for the performance of high-quality bonds.

Foreign exchange

Surprisingly solid US economic data and reduced expectations for Federal Reserve rate cuts are supporting the US dollar, which has strengthened marginally within well-established ranges. Our most preferred G10 currency with upside potential against the USD remains the Australian dollar.

A positive backdrop for high-yielding currencies has unfolded over recent weeks. Our favorite is the Brazilian real. In frontier markets, exposure to the Egyptian pound looks attractive for investors with a high risk tolerance.

We view the Swiss franc as least preferred. Swiss interest rates are very low, inflation has reached the Swiss National Bank's target range, and the need for CHF appreciation to defend against imported inflation has faded.

Commodities

Our benchmark UBS CMCI total return index is up by around 4% this year, supported by strong contribution from all sectors in March.

We retain a positive outlook for commodities, supported by interest rate cuts, a recovery in global industrial activity, and commodity-specific supply-side factors that should combine to push commodities higher.

We target total returns of around 10% over the next 6–12 months, with all sectors contributing to the performance.

We keep holding a preference for oil.
We also continue to recommend actively managing commodity exposure.

Section 1.2

Risk scenarios

Key scenarios – June 2024

	Upside: Goldilocks	Base case: Soft landing	Downside: Hard landing	*Things to watch*
Probability	20%	60%	20%	
Market path	**Bonds slightly up, equities up** Equity markets and other risk assets rally as bonds remain supported by lower policy rates.	**Bonds up, equities slightly up** Equity markets remain volatile but continue to grind higher amid slow but stable growth, falling inflation, and normalizing financial conditions.	**Bonds up, equities sharply down** Global equities post double-digit losses and credit spreads widen. Safe-haven assets such as high-quality bonds, gold, the Swiss franc, and the Japanese yen appreciate.	
Economic growth	The US continues to grow above the trend rate of about 2% as labor markets, household balance sheets, and corporate earnings prove resilient. China opts for large-scale fiscal stimulus. European growth improves.	The US economy slows to roughly trend growth over the next 12 months. Other Western economies continue to decelerate and experience sub-trend or negative growth. China announces targeted measures to support economic activity.	Growth falls sharply on a global scale toward mid-2024 owing to the delayed impact of monetary tightening. Sticky US inflation pushes bond yields higher in the near term, but yields later move sharply lower as the economy enters recession. China continues to decelerate amid underwhelming fiscal support.	*US, China: PMI data* *US, Europe: Industrial production* *Global: Consumer spending* *US: Housing starts* *US: Savings rates, depletion* *US, Europe: Delinquency ratios* *Europe: Gas prices*
Inflation	Reaches central bank targets earlier than expected.	Continues to slow in the US and in Europe, normalizing by 2H24.	Falls quickly as demand for goods and services collapses.	*Global: Oil price* *US: CPI and PCE inflation* *US: ISM prices-paid subindex* *US: Average hourly earnings* *US: Change in nonfarm payrolls* *US: JOLTS openings and hires* *Eurozone: HICP inflation*
Central banks	Cut policy rates more than current market expectations. The Fed cuts at least 100bps.	Start cutting policy rates by mid-2024 as inflation normalizes. The Fed cuts rates by 75bps.	Cut interest rates after seeing evidence of a deep recession. The Fed cuts rates down to 1–1.25%.	
Financial conditions	Ease as a better growth-inflation mix is priced in.	Ease gradually amid building expectations of upcoming monetary easing.	Tighten dramatically, causing stress in the financial system and increasing the risk of systemic events.	*Global financial conditions* *Bank lending surveys*
Geopolitics	The Middle East crisis de-escalates. The war in Ukraine also de-escalates, e.g., via a cease-fire agreement. Progress is made in bilateral relations between the US and China.	The US election season may have an impact at a sector level but unlikely on broader markets. The Middle East crisis results in a contained regional confrontation. The war in Ukraine drags on as cease-fire negotiations remain elusive.	The Israel-Hamas war turns into a regional conflict with potential for greater disruption to oil supply. The war in Ukraine escalates, and US-China tensions intensify.	*Middle East crisis and oil supply* *Territorial moves by Russia* *Weapons shipments to Ukraine* *US sanctions on Chinese companies* *US election season*

Asset class targets - December 2024

Key targets for December 2024	spot*	Upside	Base case	Downside
MSCI AC World	940	995 (+6%)	940 (+0%)	700 (–26%)
S&P 500	5,225	5,500 (+5%)	5,200 (-0%)	3,700 (–29%)
EuroStoxx 50	5,000	5,400 (+8%)	4,900 (-2%)	3,800 (–24%)
SMI	11,619	12,300 (+6%)	11,640 (+0%)	9,800 (–16%)
MSCI EM	1,032	1,200 (+16%)	1,100 (+7%)	820 (–21%)
Fed funds rate (upper bound, %)	5.50	4.00	4.75	1.25
US 10-year Treasury yield (%)	4.27	4.00	3.50	2.50
US high yield spread**	314bps	300bps	400bps	800bps
Euro high yield spread**	339bps	325bps	400bps	800bps
US IG spread**	81bps	70bps	100bps	200bps
Euro IG spread**	114bps	100bps	140bps	200bps
EURUSD	1.09	1.15 (+5%)	1.12 (+3%)	1.03 (–6%)
Commodities (CMCI Composite)	1,812	2,000 (+10%)	1,860 (+3%)	1,470 (–19%)
Gold***	USD 2,161/oz	USD 2,000/oz (–7%)	USD 2,250/oz (+4%)	USD 2,500/oz (+16%)

* Spot prices as of market close of 20 Mar 2024. Developed market constituents of the MSCI All Country (AC) World index display in the local currency. The MSCI EM index displays in US dollar. Values in brackets are expected percentage changes from the quoted spot levels. Dividends, share buybacks and other sources of carry are not included.

** During periods of market stress, credit bid-offer spreads tend to widen and result in larger ranges.

*** Gold is a safe-haven asset whose price tends to rise when risk assets, such as equities, fall, and vice versa.

Note: Asset class targets above refer to the respective macro scenarios. Individual asset prices can be influenced by factors not reflected in the macro scenarios.

Analysts: Dirk Effenberger, Daniil Bargman

Section 1.3

Asset class preferences and themes

Global asset class preferences

	Least preferred		Most preferred
Liquidity		=	
Equities		=	
United States		=	
Eurozone		=	
Switzerland		=	
Emerging markets			+
Japan		=	
United Kingdom	−		
Bonds			+
High grade			+
Investment grade			+
High yield		=	
Emerging markets		=	

	Least preferred		Most preferred
Commodities		=	
Oil			+
Gold		=	
Foreign exchange			
USD		=	
EUR		=	
JPY		=	
GBP		=	
CHF	−		
AUD			+

Note: The global asset class preferences reflect the high-level UBS House View. The tactical asset allocation (TAA) positioning of our different investment strategies may differ from this view because our strategies seek specific investment objectives and can frequently adjust portfolio allocation to achieve them. Also, these preferences may vary in different regions for various reasons such as currency considerations.

Least preferred
We expect this asset class to deliver the least attractive risk-adjusted returns over the next 12 months within our asset class universe.

Most preferred
We expect this asset class to deliver the most attractive risk-adjusted returns over the next 12 months within our asset class universe.

Asia ex-Japan asset class preferences

	Least preferred		Most preferred
Equities			
Asia ex-Japan		=	
China		=	
Hong Kong			+
India		= ←	⊕
Indonesia			+
South Korea		=	
Malaysia	−		
Philippines		=	
Singapore	⊖ →	=	
Taiwan		=	
Thailand	−		
Bonds			
Asian investment grade bonds		=	
Asian high yield bonds		=	
Chinese government bonds		=	

Note: The Asia ex-Japan asset class preferences reflect the high-level UBS House View. The TAA positioning of our different investment strategies may differ from this view because our strategies seek specific investment objectives and can frequently adjust portfolio allocation to achieve them.

Least preferred
We expect this asset class to deliver the least attractive risk-adjusted returns over the next 12 months within our asset class universe.

Most preferred
We expect this asset class to deliver the most attractive risk-adjusted returns over the next 12 months within our asset class universe.

US asset class preferences

	Least preferred		Most preferred
Cash		=	
Fixed Income			+
US Gov't FI		=	
US Gov't Short		=	
US Gov't Intermediate		=	
US Gov't Long		=	
TIPS			+
US Agency MBS			+
US Municipal		=	
US IG Corp FI			+
US HY Corp FI		=	
Senior Loans		=	
Preferreds		=	
CMBS			+
EM Hard Currency FI		=	
EM Local Currency FI		=	

	Least preferred		Most preferred
Equity		=	
US Equity		=	
US Large Cap	–		
US Growth Equity		=	
US Value Equity		=	
US Mid Cap		=	
US Small Cap			+
Int'l Developed Markets		=	
UK	–		
Eurozone		=	
Japan		=	
Australia		=	
Emerging Markets			+
Other			
Commodities		=	
Gold		=	
Oil			+
MLPs		=	
US REITs		=	

Note: The US asset class preferences reflect the high-level UBS House View. The TAA positioning of our different investment strategies may differ from this view because our strategies seek specific investment objectives and can frequently adjust portfolio allocation to achieve them.

Least preferred: We expect this asset class to deliver the least attractive risk-adjusted returns over the next 12 months within our asset class universe.

Most preferred: We expect this asset class to deliver the most attractive risk-adjusted returns over the next 12 months within our asset class universe.

Global and regional sector preferences

Sectors	LP	US	MP	LP	Eurozone	MP
Communication services		=		–		
Consumer discretionary		=				+
Consumer staples		=				+
Energy		=			=	
Financials		=			=	
Healthcare			+	–		
Industrials			+		=	
Information technology			+		=	
Materials		=				+
Real estate	–				=	
Utilities	–				=	

Least preferred (LP)
We expect this sector to deliver the least attractive risk-adjusted returns over the next 12 months within our sector universe.

Most preferred (MP)
We expect this sector to deliver the most attractive risk-adjusted returns over the next 12 months within our sector universe.

Messages in Focus

Optimize tech exposure

The AI revolution is here. Investors can't afford to be underinvested, and optimizing exposure to technology is key. We think this involves a diverse strategic exposure to the sector, balancing a focus between the beneficiaries of tech disruption and sector leaders including "Asia's Super 8." The current environment of high interest rates and low volatility also presents an opportunity to use structured solutions to position for further upside while protecting against downside.

- *Global technology stocks*
- *Technology disruption*
- *"Asia's Super 8"*
- *Capital preservation strategies on technology stocks*

Source of funds
- Cash and money markets
- Address equity portfolio biases
- Excess US technology exposure
- Excess individual tech stock exposure

Opportunities beyond technology

While we hold a constructive view on technology, investors need to be mindful of concentration risks and overexposure. For those diversifying beyond technology, we see opportunities in quality companies (including regional champions in Europe and Asia); the energy transition, healthcare disruption, and water scarcity; and small- and mid-cap stocks. Exposure to these ideas can also be built up through structured investments.

- *Quality stocks (including global and regional champions)*
- *Energy transition, healthcare disruption, water scarcity*
- *Small- and mid-caps (including US small-caps, European small- and mid-caps, ESG engagement)*
- *Defensive structured investments (yield-generating and capital preservation)*

Source of funds
- Cash and money markets
- Excess US technology exposure

Manage liquidity*

We expect interest rates to fall in 2024. This means cash will progressively deliver lower returns, creating a risk for investors who do not proactively manage cash holdings. We believe investors should build a liquidity strategy beyond cash and money market funds, in favor of a combination of fixed-term deposits, bond ladders, and structured investment strategies to cover expected portfolio withdrawals over the next five years.

- *Fixed term deposits*
- *Bond ladders*
- *Structured investment strategies with capital preservation features*

Source of funds
- Cash and money markets
- Maturing investments

Buy quality bonds

We keep a preference for quality bonds. Robust economic growth and elevated inflation have kept bond yields high in recent months. But we expect yields to fall over the balance of the year as growth and inflation moderate. That makes now an attractive time to lock in yields, benefit from potential capital gains if yields fall, and diversify portfolios against risks. Beyond individual bonds, active and diversified bond exposure can provide investors with a convenient way to realize the full return potential of the asset class while managing credit and concentration risks.

- *Quality bonds (HG and IG)*
- *Sustainable bonds, including MDB bonds*
- *Active and diversified bond exposure*

Source of funds
- Cash and money markets

*Time frames may vary. Strategies are subject to individual client goals, objectives and suitability. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved.

Analysts: Kiran Ganesh, Sagar Khandelwal, Wayne Gordon, Jason Draho, Michael Gourd

Messages in Focus

Generate income with currencies and commodities

We believe that major currency pairings are likely to continue to trade in established ranges as most major central banks are set to cut interest rates in tandem. This presents an opportunity for investors to generate added portfolio income by trading the range in currencies, as well as in select commodities.

- *Generate income from USD, EUR, GBP, and CNY*
- *Upside for AUD and JPY*
- *Structured solutions on oil and gold*

Source of funds
- Cash
- Maturing investments
- Available collateral (for OTC range-trading strategies)

Get in balance

Investors today are grappling with a complex financial environment. Some worry that the stock market has reached its peak, leading them to hold too much cash. Others may be overly focused on specific sectors, risking too much concentration in their portfolios. Against this backdrop, getting in balance is a key principle. We believe that only by diversifying across asset classes, regions, and sectors can investors effectively manage the tension between navigating short-term market dynamics and growing long-term wealth.

- *Balanced portfolios*

Source of funds
- Cash
- Maturing investments

Diversify with alternatives

Alternative assets should be a key component of long-term portfolios, in our view. They can help diversify return sources and smooth portfolio returns. We currently see opportunities in strategies that offer unique return sources (credit hedge funds), provide access to fast-growing companies (private equity), and align with powerful long-term trends like digitalization and decarbonization (private infrastructure and thematic private equity funds).

- *Infrastructure*
- *Hedge funds (specialist credit, equity long-short, macro, and multistrategy)*
- *Private equity (secondaries, buyout, and thematic growth) and credit*

Source of funds
- Cash
- Maturing investments

Key investment ideas by asset class

	We like	Source of funds
Equities	• Global technology stocks • Technology disruption • "Asia's Super 8" • Quality stocks • Energy, healthcare disruption, water scarcity • Small- and mid-caps (including US small-caps, European small- and mid-caps, ESG engagement)	CIO least preferred equities, excess cash
Bonds	• Quality bonds (investment grade and high grade) • Sustainable bonds including MDB bonds • Fixed term deposits • Bond ladders • Active and diversified bond exposure	Excess cash, excess EM/HY bonds
Foreign exchange	• Upside for AUD and JPY • Generate income from USD, EUR, GBP, and CNY	CHF
Commodities	• Active commodity exposure • Oil	Excess cash
Hedge funds, private markets	• Infrastructure • Hedge funds (specialist credit, equity long-short, macro and multistrategy) • Private equity (secondaries, buyout, and thematic growth) and credit	Excess bonds and equities, excess cash

Section 2

Macro economic outlook

Global economy – Moving slowly toward cuts

Base case (60%)

Growth

A soft economic landing remains the most likely economic scenario at this point. Unemployment remains low, although workers are less inclined to move between jobs. There has been some increase in the number of people taking more than one job, reflecting a mix of structural change in labor markets and economic necessity after a period of weak real wage growth. Broad measures of consumer spending continue suggest that growth will not slip too far below trend, although there is some evidence that consumers are increasingly unwilling to accept price increases.

Inflation

Market forces continue to push inflation lower across the major economies. Inflation inequality and peculiarities in calculation mean that some consumers face notably lower inflation rates than the headlines suggest—meaning their spending power is correspondingly stronger.

Positive case (20%)

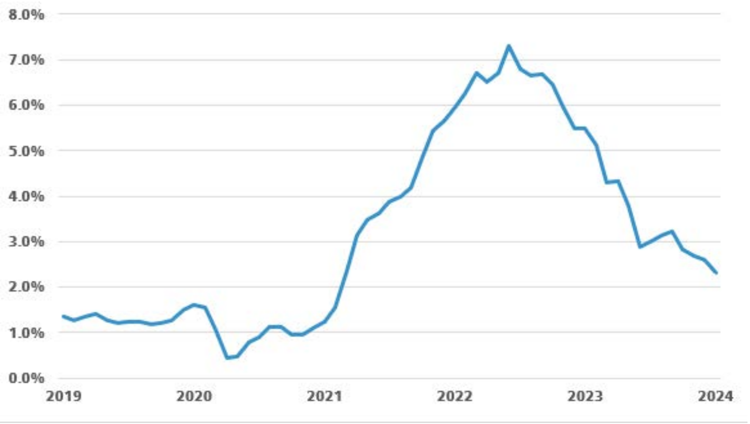
The positive scenario is an enhanced version of existing trends. Real wage growth is supported by a sharper slowdown in inflation. Low unemployment gives consumers in advanced economies confidence to accelerate spending. Investment increases more rapidly in new technologies and areas of labor shortage. Fiscal policy remains a drag on growth in developed economies, but China implements a more effective fiscal boost.

Negative case (20%)

A more rapid tightening of credit standards and higher costs of borrowing for existing debtors lead to a sharper slowdown in consumer demand as spending power is eroded. Concerns about the cost of credit slows borrowing for middle-income consumers as well as lower-income groups. Fear of unemployment starts to increase, resulting in higher precautionary savings. This compounds the risks to growth.

Market forces remain disinflationary

US market-based personal consumer expenditure deflator, in % y/y



Source: Haver, UBS, as of 17 March 2024

Spending on fun remains resilient

UK level of real spending on "fun" versus goods, 2019 av = 100

Source: Haver, UBS, as of 17 March 2024

US economy – On a path toward a soft landing

Base case (60%)

Growth

Growth has remained above-trend since 3Q22, including a strong 3.2% in 4Q23, led by consumer spending. Recent data has been mixed, with strong payroll growth in February but retail sales coming in weaker than expected. More households have used up the excess savings built during the pandemic, while credit card balances have risen rapidly despite high interest rates. We expect consumer spending to moderate, but rising real disposable income should continue to provide support. Our base case remains a soft landing, with the Fed starting to trim rates in June as the growth data turns softer.

Inflation

Monthly inflation prints showed bigger increases in January and February, breaking a string of more favorable data. Inflation is being driven by service prices, which are more sensitive to the still-strong pace of wage growth. Businesses report that consumers are pushing back against further price increases, and we still expect inflation to trend toward the Fed's 2% target in the months ahead.

Positive case (20%)

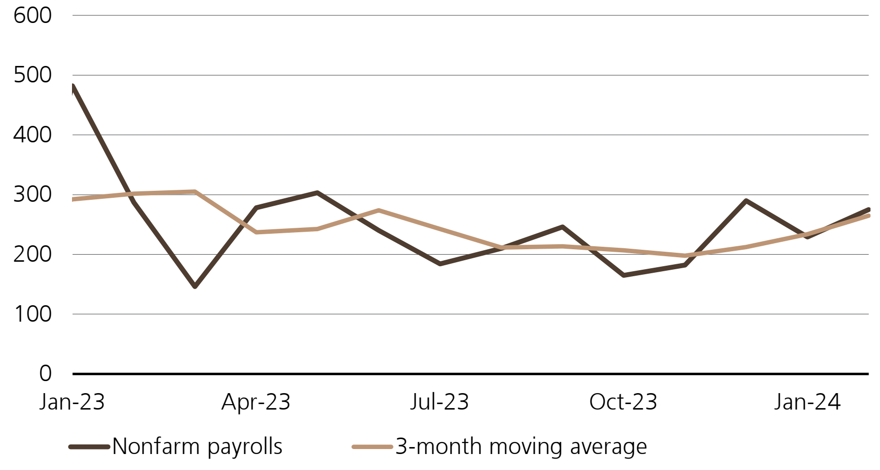
Better labor supply allows businesses to fill their open job positions. Wage growth slows to a more moderate pace, helping bring inflation down while growth remains robust. New industrial policies continue to promote business investment. The Fed sees enough progress toward its mandates to start cutting rates even as the economy continues to expand and the unemployment rate stays low.

Negative case (20%)

Household spending finally takes a breather after an extended period of strong growth, and the savings rate moves higher. Seeing weakening consumer demand, businesses increase the pace of layoffs and reduce hiring, reinforcing the consumption slowdown. A spike in energy prices could lead to stagflation, but otherwise inflation should fall quickly, allowing the Fed to cut rates aggressively and helping to prevent a severe downtown.

Payroll growth still strong

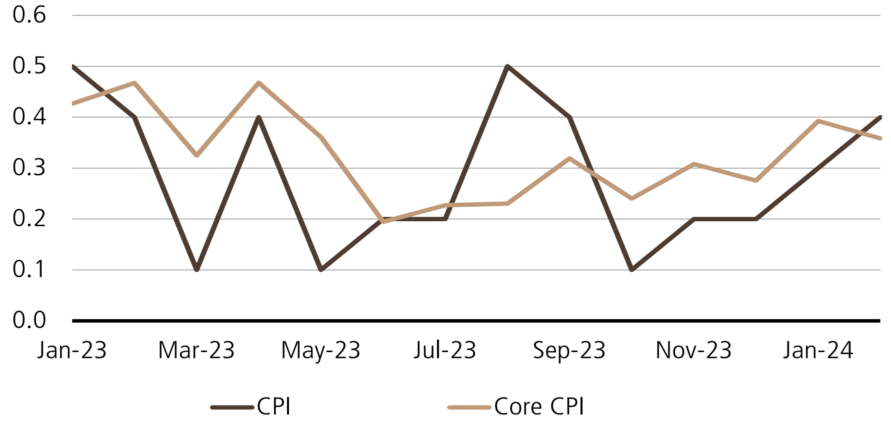
Nonfarm payrolls, month-over-month change, in thousands



Source: Bloomberg, UBS, as of 18 March 2024

Stronger inflation prints so far in 2024

CPI and core CPI, month-over-month change, in %



Source: Bloomberg, UBS, as of 18 March 2024

Eurozone economy – Still waiting for improvement

Base case (60%)

Growth

Sentiment surveys are stabilizing, with some signs of mild improvement, but they remain at low levels. Likewise, hard data remain weak. In our view, the economy is set to remain on its current sideways trend in the coming months, then start to show a modest pickup later in the year as real incomes improve and the drag from tight monetary policy eases.

Inflation

We expect inflation to fall back to target over the coming quarters, faster than the European Central Bank (ECB) projects. Some modest volatility in inflation could persist early in the year as governments phase out remaining fiscal support measures and the disinflationary impulse from energy base effects fades. Still, coupled with a moderation in wage growth, the ECB should gain the confidence to start lowering interest rates, most likely starting June. In total, we expect 100bps of cuts from the ECB this year.

Positive case (20%)

Economic activity normalizes sooner, supported by a sharp fall in inflation, a pickup in consumer sentiment, earlier-than-expected monetary policy easing, and ongoing labor market strength.

Economic growth in Asia and the US accelerates, with the latter avoiding a recession, boosting demand for Eurozone exports.

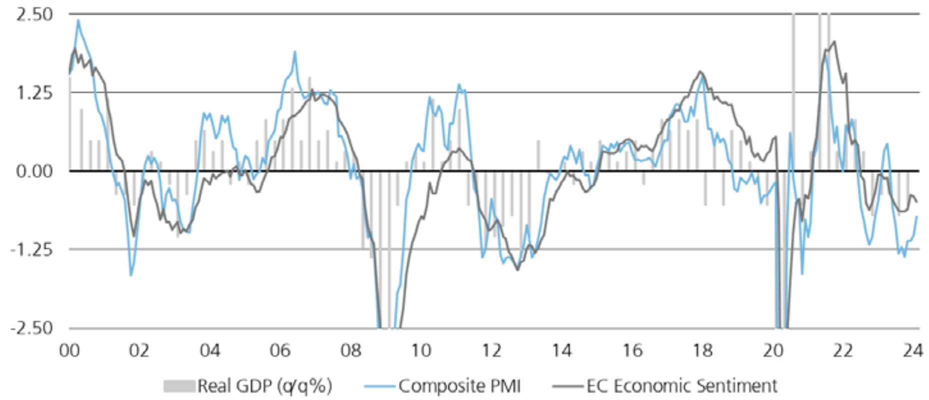
Negative case (20%)

The ECB overtightens monetary policy by placing too much weight on near-term inflation. Tighter financial conditions see demand for credit collapse further, hurting consumption and investment.

Geopolitical tensions force energy prices materially higher, leading to renewed supply-push inflation that induces a real income loss and a tighter monetary stance.

Growth is likely to remain anemic, as sentiment measures stabilize at a low level

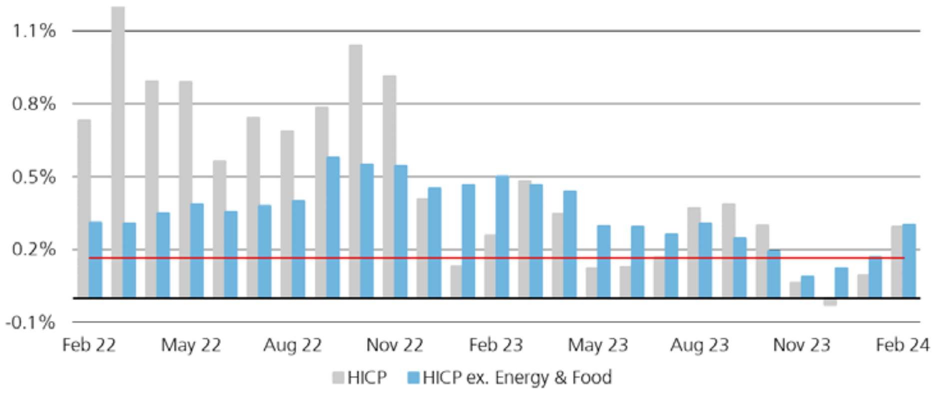
Output measures for the Eurozone (z-scores)



Source: Haver Analytics, UBS, as of 18 March 2024

Month-over-month inflation picked up recently, likely due to start-of-year seasonality rather than renewed inflationary pressures

HICP inflation m/m, SWDA (3-month avg.)



Source: Haver Analytics, UBS, as of 18 March 2024

Swiss economy – Growth to stay below trend

Base case (70%)

Growth

Swiss GDP grew 0.8% in 2023 and we expect it to grow a still-below-average 1.3% in 2024. A gloomy economic outlook for the Eurozone is weighing on industrial sentiment. External demand improved recently, but our export barometer is still in negative territory, pointing to below-trend growth in the months ahead. Domestic demand looks more solid on the back of robust employment growth and declining inflation.

Inflation

At 1.2% year-over-year, Swiss inflation fell slightly in February compared to January and remained well within the SNB's comfort zone. With rents expected to rise in May, short-term upside risks to the inflation outlook persist. We expect the Swiss National Bank to cut the policy rate three times this year to 1%.

Positive case (15%)

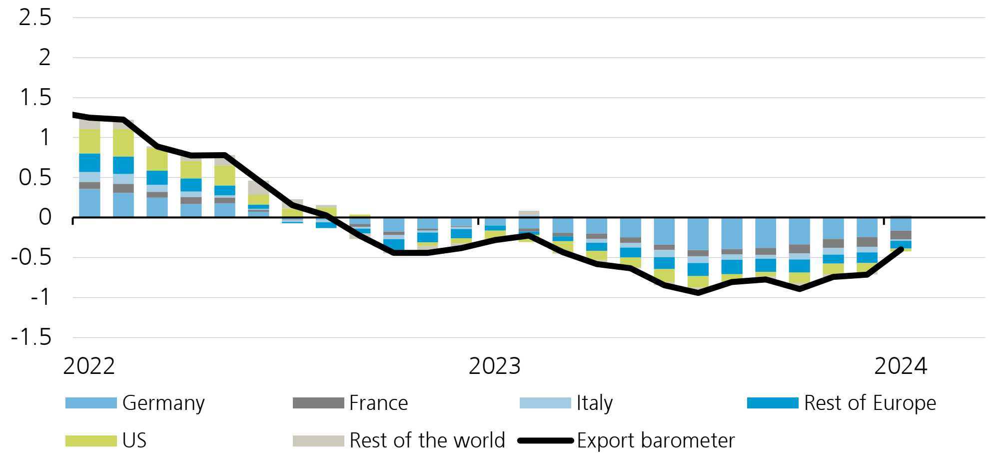
Better global growth momentum: Growth in the US remains strong. Lower-than-expected inflation allows global central banks to cut rates earlier. Switzerland benefits from the stronger global backdrop and a weakening of the safe-haven Swiss franc.

Negative case (15%)

US downturn pushes Switzerland into a recession: If the global economy fell into a recession, Switzerland would suffer strongly from the slump in global export demand and from a strong appreciation of the Swiss franc.

External demand improved but still in negative territory

Export barometer from the manufacturing PMIs of Swiss trading partners, standardized



Source: Macrobond, UBS, as of 13 March 2024

Swiss economic data

In %, including UBS forecasts (*)

Source: Macrobond, UBS, as of 13 March 2024

Analysts: Alessandro Bee, Florian Germanier, Maxime Botteron

Chinese economy – Incremental policy support to ensure steady growth

Base case (70%)

Growth

Data for the first two months of the year were generally better than feared. Retail sales growth eased to 5.5% with resilient holiday spending. Fixed asset investment growth rebounded to 4.2%, led by manufacturing (9.4%) and infrastructure (6.3%). Credit growth eased to 9% due to a high base of comparison but could rise to 9.5% by year-end with stronger government bond issuance.

Beijing rolled out policy support including 50bps of cuts to banks' required reserve ratio; a stock market bailout by "National Team" entities; over 6,000 property projects "whitelisted" for bank loans; and easier limits to Tier 1 city home purchases. We expect incremental policy support to ensure GDP growth does not stray far from the 5% target.

Inflation

Consumer price inflation bounced to 0.7% year-over-year in February due to holiday spending but could ease in the coming months to reach a full-year average of about 0.8%. Producer prices stayed in deflation (–2.7%) and may only turn mildly positive by 3Q24.

Positive case (15%)

More policy measures are announced to revive confidence in the economy's medium-term outlook.

Geopolitical risks ease with improved communications between China and the US post Xi-Biden talk at the APEC summit.

The US economy achieves a soft landing.

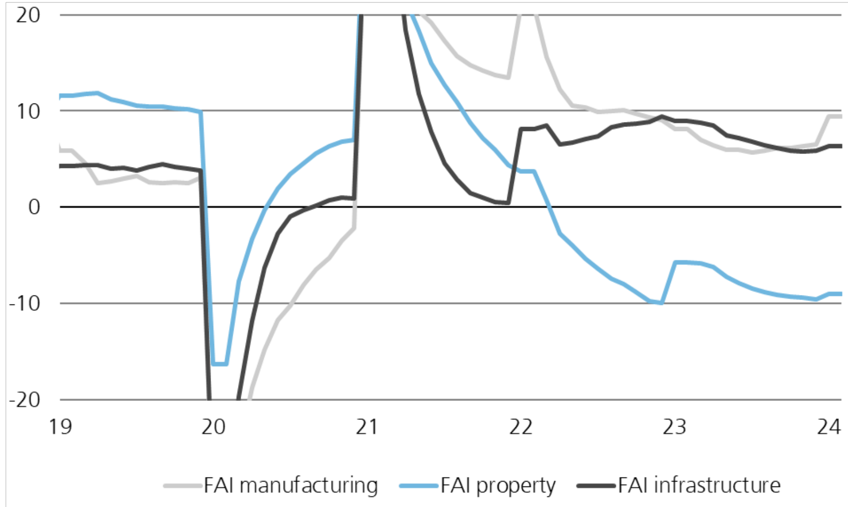
Negative case (15%)

Property activity continues to deteriorate despite supportive policies.

The US falls into a deep recession due to the lagged effect of high rates.

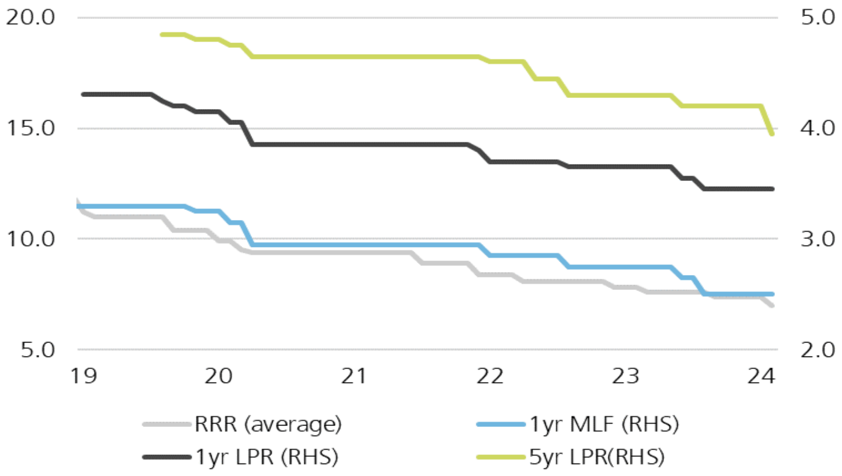
The US imposes much stricter restrictions on China's tech sectors.

Investment supported by manufacturing and infrastructure



Source: CEIC, UBS, as of 18 March 2024

Further rate cuts likely delayed to 2Q



Source: CEIC, UBS, as of 18 March 2024

Section 3

Asset class views

Section 3.1

Summary of major asset classes

Equities

Central scenario

MSCI AC World December 2024 target: 940

We maintain a neutral view on global equities. Global equities extended their rally in February and March and currently trade at record levels. Late last year, the rally was propelled by lower yields, which resulted from hopes of a central bank pivot. This year, the rally has been mainly driven by robust results from high-quality companies and encouraging macroeconomic data. The outlook has undoubtedly improved, but optimism is already high, limiting our appetite to chase the rally from here. We maintain our neutral stance in our asset strategy and expect the asset class to deliver low-single-digit returns by the end of 2024.

The earnings outlook continues to improve. The latest economic data support our base case that a soft landing is the most likely outcome. A Goldilocks scenario where central banks cut interest rates with still-resilient economic growth is also being entertained. Against this backdrop, earnings likely troughed in 2023, and we expect them to reaccelerate in 2024. Tech sectors should lead the growth as they harvest the fruits of their cost-cutting measures from 2023, and they benefit from rapid developments in the AI space. More favorable base effects (i.e., a lower drag from the commodities and healthcare sectors) are also playing a role. That said, we find the current consensus for 2024 earnings per share (EPS) growth to be quite aggressive (around 9% for MSCI ACWI), which suggests that a high dose of market optimism is already priced in.

Rising interest rates remain a risk. For most of 2023, equities and interest rates have been negatively correlated. The latest rally, which started in November, was initially triggered by a sharp drop in yields as inflation slowed and central banks seemed to pivot to a more dovish stance. So far this year, inflation fears somewhat fell in the background, and equities focused essentially on the improved growth outlook and tolerated higher yields. However, the latest US inflation data added some volatility, and further signs of stickiness would question the ability of central banks to deliver the expected cuts. We are wary that equity markets may be underappreciating this risk, even if our base case remains for yields to grind lower from here.

Valuations start looking expensive. MSCI ACWI's 12-month forward price-to-earnings ratio currently trades at 17.5x, roughly 1 standard deviation above its 10-year average. While not extreme in a historical context, it remains on the high side and could reduce the potential for rerating that may come from lower yields. In other words, lower rates would still likely support equities, but not as much as last year. Looking at other metrics, the equity risk premium remains low in a historical context, especially against fixed income markets.

Mixed tactical indicators, stretched positioning. Global equities are trading comfortably above their key moving averages, highlighting a solid price momentum picture. However, short-term indicators such as the 30-day relative-strength index for example appears stretched and point to some consolidation in the coming weeks. Positioning in equities has continued to rise and increasingly looks one-sided.

Emerging market equities most preferred: While we no longer expect China to lead, we still expect emerging markets to outperform in our tactical time frame. The region trades at very attractive valuation, in our view; has fast-growing earnings; and should be a key beneficiary of lower US yields. The start of the Fed cutting cycle may help unlock emerging markets' value.

UK equities least preferred. We expect UK equities to rise less than their regional peers in our tactical horizon. Earnings contracted significantly in 2023, dragged by commodity sectors, and should show one of the weakest recoveries in 2024 among major equity markets.

Equities

.

Upside scenario

MSCI ACWI December 2024 target: 995

Inflation cools quickly and the US and European economies grow above trend: Inflationary pressures quickly dissipate, but growth turns out stronger than expected.

Geopolitical de-escalation: Cease-fires end the wars in Ukraine and between Israel and Hamas, and reduce the risk of further sanctions against Russian or Iranian commodities.

Economic growth reaccelerates: Solid economic growth in the US and emerging markets drives a sharper improvement in corporate profits.

Downside scenario

MSCI ACWI December 2024 target: 700

Inflation runs hot: Inflation surprises again on the upside and central banks are forced to hike again.

Geopolitical escalation: Increased escalation between Russia and Ukraine or between Israel and Hamas leads to a further disruption of Russia's or Iran's energy supplies. Oil and natural gas prices rise sharply and remain elevated.

Economic growth shrinks sharply as a result of the lagged impact of tighter monetary policy, driving earnings growth and valuation multiples lower.

Regional/Country preferences

Most preferred: Emerging markets

Least preferred: UK

Analysts: Crystal Zhao, Fabian Deriaz, Adrian Zuercher, Ivan Peric

Bonds

Preference: Most preferred

Developed market bond yields traded in a 20–30bps range over the last month as pricing on the timing and magnitude of rate cuts fluctuated. Another month of relatively sticky inflation prints was offset by evidence of labor market easing and central bank speeches indicating that rate cuts remained appropriate this year. As of writing, the market is priced for around three Fed cuts this year. This is similar to expectations on the ECB and BOE with the timing of the first cuts centered around middle of the year. This has been recalibrated from the beginning of the year when pricing was far more aggressive in anticipating six cuts. Now we have market outlooks close to central bank and market economist consensus expectations.

Our constructive view on the high quality segments of fixed income is based on the fact that once central banks begin rate-cutting cycles, a momentum is often established as the bond market looks to price the end point. Additionally, as the lagged effects of previous hikes continue to pass through to the real economy, there is always the risk of a recession and need to cut rates more aggressively, which would boost high quality bond returns. The starting yield on high quality bonds provides an ample buffer against ongoing volatility. Additionally, following the pandemic, governments have been left with significant debt loads and large deficits. The size of deficits at present is unprecedented outside of a recession. By virtue of these fiscal dynamics and the fact that central banks are reducing their stock of government bonds, there is significant bond supply coming to the market and required to be absorbed by the private sector. In October last year, we observed a pickup in term premium as the market began to focus on this supply backdrop. Historically, a widening of fiscal deficits has coincided with a deteriorating economic backdrop and hence a pickup in demand for high-quality bonds. With rate cuts coming back onto the agenda, this has trumped these technicals for now. Our preferred approach is to take exposure in the 1- to 10-year part of the curve, which has a stronger link to growth, inflation, and policy, rather than the ultra-long end of the curve, which is more sensitive to these technical elements. We have gained some comfort with Fed speakers beginning to discuss the conditions necessary to slow the pace of balance sheet runoff (quantitative tightening, or QT). This would alleviate some of the need for the private sector to absorb the net additional supply and a sharp run down of excess reserves, which could generate instability in the banking system.

Within the fixed income asset class, we are maintaining an up-in-quality bias expressed through high grade (HG) and investment grade (IG) bonds. There are select opportunities in the more growth-sensitive areas of high yield (HY) and emerging market (EM) credit. The prospects of rate cuts has been priced into market expectations and hence resulted in some easing of financial conditions already. This should offset downside risks to growth to some extent. However, higher-beta credit segments are trading tight and not offering much spread compensation in the event of a worsening growth backdrop, while also being vulnerable to a further repricing of Fed rate cut expectations. Furthermore, current spreads also appear to be discounting a below-average credit risk premium. As a result, we see HY and EM spreads as being more vulnerable to spread widening relative to IG and HG.

High grade bonds: We keep HG bonds as most preferred. Inflationary pressures are abating and, as a result, major central banks are now in discussions on when rate cuts may be appropriate. This is a favorable backdrop for duration risk. To see structurally higher interest rates across the curve from here, we believe we would need to see economic growth accelerate meaningfully. As excess savings have been run down and fiscal policy is already loose, we see growth more likely to slow than accelerate going forward. High grade bonds are rated AA- or better, and therefore have minimal default risk. Given that the outright level of rates is high due to high policy rates, we see an attractive asymmetric absolute return profile in light of the inflation and growth mix.

Investment grade bonds: Like HG bonds, we keep IG bonds as most preferred. Looking ahead, we see returns in the high-single-digit range over the coming 12 months supported by both elevated yields and price upside on prospects for falling interest rates. Within EUR IG, the average yield is around 4%. On US IG, yields for all maturity and intermediate profiles are around 5.3%. Credit fundamentals on the US IG corporate side remain solid, and we expect limited credit quality deterioration in our base case. Any widening of spreads should be more than offset by falling interest rates as the focus turns toward rate cuts.

High yield bonds: We are neutral on the asset class as, relative to the higher-quality segments, we see more pronounced risks of spread widening and decompression given risks around continued credit quality deterioration and corporate defaults among the more leveraged, lower-rated companies. Spread levels appear to discount a very low expected default level of 1–2% and a below-average credit risk premium. That said, the fundamental backdrop in HY is arguably not too bad. There has only been a limited amount of time since the last downturn, so we have not had the classic buildup of financial excess or leverage seen in previous cycles. In fact, the average credit quality in HY has improved. Additionally, the outright level of yields in US HY and EU HY is around 8% and 6.5%, respectively, which has attracted capital flows and supported performance, hence our neutral stance.

Bonds

Emerging market bonds: We maintain a neutral stance on the asset class. We think EM bonds can deliver high-single-digit returns in 2024, not least thanks to the elevated yield level. Current yields are around 8% and 7% for sovereign and corporate bonds, respectively. High nominal yields and prospects for a weaker US dollar and US policy rate cuts should support the asset class. But following the strong compression in spreads, the room for error is small with spreads at the tight end of their historical range, leaving the asset class vulnerable to temporary setbacks. These could occur due to various reasons, including the risks arising from negative growth and inflation shocks, escalating geopolitical tensions, or rising defaults.

CIO themes

Resilient credits

Resilient credits offer a decent income following a sharp rise in interest rates and credit spreads. Our selection of tenors around five to seven years offers additional potential outperformance over riskier bonds (and stocks) in case of a recession, where interest rates would likely decline materially, while risk premiums of resilient credits would only rise moderately. Investors concerned about recession risk should consider this positioning over shorter-dated bonds with higher credit risk.

FX

Price action and economic conditions suggest EURUSD is likely to stay in a 1.05 to 1.10 range for the time being. We believe the pairing may test the lower edge of that trading band in the coming weeks, as surprisingly solid US data pave the way for the dollar to appreciate. Still, we see limits to dollar strength. Markets are expecting most G10 central banks to cut interest rates by 150 to 200 basis points over the next two years. This should provide very solid support for risk-on currencies like the EUR, the GBP, and the commodity bloc (AUD, CAD, and NZD). In light of that long-term expectation, most investors are likely to shy away from buying US dollars below EURUSD 1.05.

Still, the upside for the euro and other risk-on currencies is also limited for the time being, in our view. A necessary condition for a sharp and large appreciation of the euro would be a strong rebound in both Eurozone and global growth. Over the next couple of months, we see some support for the common currency given that the European Central Bank (ECB) is usually slow to react to changing trends, and does not seem to be in any hurry to cut interest rates. This implies higher real interest rates that would support the euro around current levels and even more strongly around 1.05.

The pound is also steady against the EUR. The UK and the Eurozone are at a very similar stage in the economic and monetary policy cycle. Just like the euro, the GBP would likely need a stronger global growth backdrop and a more stable geopolitical outlook to rally sustainably. A rebound of GPBUSD to 1.30 cannot be ruled out in light of easing global monetary conditions and improving risk sentiment.

The Swiss franc is on a weakening trend in response to Swiss inflation dropping into the Swiss National Bank's (SNB) target band, reducing the need to shield Switzerland from imported inflation. This backdrop suggests to us the CHF should decline further from here, and we keep our least preferred view on the franc. We think the currency is well suited to finance carry trades in the coming months. In contrast to this short-term least preferred view, we continue to see long-term value in CHF positions. The last two years have demonstrated that the Swiss franc has strong appreciation potential when the global economy is hit by high inflation or rising geopolitical concerns.

USDJPY, meanwhile, is likely to remain in a 145–152 trading range in the coming months, in our view. The Bank of Japan (BoJ) judged that reaching 2% inflation is in sight, and hence announced an end to its negative interest rate policy (NIRP) and yield-curve control (YCC) regimes at its March meeting. However, the yen did not benefit from the decision, implying that markets remain comfortable using the yen as a funding currency amid elevated US yields. Nevertheless, USDJPY's rise above 150 attracted renewed pushback from both the Finance Ministry and BoJ Governor Ueda. In this context, we continue to see limits to USDJPY upside, and favor selling USDJPY upside risks for yield pickup.

For the CAD, NOK, AUD, and NZD, we anticipate only benign changes in the crosses. To be sure, we think the AUD is likely to profit the most as the Reserve Bank of Australia will likely join the rate-cut cycle only in 4Q in view of its stronger domestic economy. The pullback in oil prices should be transitory and any rebound may support the CAD and NOK. We expect EURCAD to move lower and the NOK to outperform the SEK again.

After the strong repricing of global central banks' policy rate outlooks at the start of the year, emerging market currencies benefited from solid-enough economic data, general pro-risk sentiment in markets, and their own rather elevated interest rate carry (some more than others). Even a second US inflation release coming in hotter than expected left the asset class rather unscathed. We expect the carry-supportive backdrop to extend in the coming months. With the Federal Reserve expected to start cutting its policy rate by the middle of the year, high-yielding emerging market currencies that saw initial policy rate cuts should still fare well. Our preference is for the Brazilian real, which should benefit from its strong external balance as well. And for investors with a high risk-tolerance, we recommend exposure to the Egyptian pound, whose total return outlook has much improved after the investment deal struck between Egypt and the UAE, the recent devaluation, and the rekindled IMF program. Emerging market currencies remain exposed to more hawkish-than-expected Fed policy, which could lead to a global growth slump, geopolitical flashpoints, broad risk-off sentiment, as well as idiosyncratic risks for individual currencies stemming from local monetary policy, fiscal policy, and politics.

For China, we expect limited upside potential for the yuan, because of weakening Chinese growth momentum, which speaks for further easing measures. Our end-2024 forecast of 7.15 shows a sideways profile for USDCNY, which reflects our view that the yuan is unlikely to benefit materially from medium-term dollar weakness. In this context, we reiterate our recommendation that investors should continue to hedge their CNY long exposure.

The biggest risk to our short-term USD view is a rapid fall in US growth, which would put investor focus on structural USD negatives and the greenback's elevated valuation. The speed at which the US economy slows matters. If the economy doesn't slow because consumer demand or fiscal spending comes in strong ahead of the presidential elections, current market expectations for lower US rates could still be revised higher.

Analysts: Thomas Flury, Teck Leng Tan, Tilmann Kolb

FX

Conversely, a hard landing with risk assets under downward pressure could support the USD beyond the ranges that we currently promote. The USD tends to perform positively in a risk-off environment, while risk-on currencies (the EUR, GBP, commodity dollars, and emerging market currencies) tend to depreciate. Still, a hard landing would likely lead to a strong reaction from the Fed. Therefore, we think any major USD rally could be sharp initially, but would be watered down eventually by expansive central bank action.

Lastly, we are also watching the US bond market at the long end of the yield curve. The US fiscal deficit seems to be too high without the market commanding a higher term premium. A further rise in the 10-year US Treasury yield north of 5% could keep the USD on a path of further strength. That being said, there would also be a point where higher rates would provide little support for the currency as investors begin to worry about the economic knockdown effect at a later stage. However, we have yet to see any signs of this scenario for the US economy and the USD.

Commodities

We hold a neutral view on commodities overall and gold, but remain most preferred on crude oil.

OPEC+ extends voluntary production cuts. Oil demand growth figures have surprised positively in recent months. At the same time, with OPEC+ retaining a cautious stance and extending their voluntary production cuts until the end of June, we expect the oil market to stay undersupplied, and oil prices supported.

Silver linings emerge in base metals. We see further supply disappointments and structurally low exchange inventories providing the conditions for higher prices this year. While prices will likely remain volatile in the near term on global growth concerns, structural demand drivers for the sector are still in place, which should drive a recovery over the coming quarters.

Gold is a hedge with benefits. Gold prices surged to a new record intraday high as technical factors likely spurred money market participants to buy gold futures. With our base case of solid central bank demand for the metal and the Fed starting to cut rates by midyear, we think a revival in gold ETF demand is the next catalyst. Our year-end target remains USD 2,250/oz.

Agriculture: Despite the steady decline in grain prices over recent months, the prices of some soft commodities including cocoa and cotton have continued to surge. Cocoa has closed at new all-time highs above USD 8400/mt as participants try to find a price point at which demand destruction begins to balance the market. The ICCO released its 2023-24 numbers, and the deficit now exceeds 370,000 metric tons (mt) with 74,000 mt last season. This is the third annual deficit in a row and the largest since ICCO records began in 1960 and could see global stockpiles drop by around 21% from a year earlier. Market participants are also turning their attention towards the US Department of Agriculture's (USDA) March US Prospective Plantings report—we expect acreage projections for corn and soybeans to beat previous forecasts. Markets remain pressured by cheap wheat from Russia and a seasonal pick-up in exports of soybeans from South American suppliers. According to the NOAA, the chances of a La Nina by Christmas is above 70%. Historically, these events have raised the risks of drought in parts of the US, Brazil, and Argentina. We remain least preferred on grains and most preferred on soft commodities in our active strategy.

Where to invest

Opportunities in longer-dated oil contracts. Longer-dated oil contracts are trading cheaper than spot prices. While commodity markets tend to price in the "now," futures curves, as a rule, don't hold much predictive power. So, vanishing available spare capacity should support longer-dated contracts, in our view.

Gold still a good hedge. We continue to recommend investors use gold as a hedge despite being neutral in the global asset allocation—within a balanced USD portfolio our analysis shows around a mid-single-digit percentage is most optimal.

Volatility-selling strategies. On an individual commodity level, we see opportunities to engage in selling downside in crude oil, copper, gold, and platinum.

Analysts: Dominic Schnider, Giovanni Staunovo, Wayne Gordon

Section 3.2

Details per asset class

UBS

Eurozone equities

Central scenario

DJ Euro Stoxx 50 December 2024 target: 4,900

We maintain our neutral stance on Eurozone equities. Relative valuations remain attractive, in our view, but subdued economic growth points to a relatively slow earnings recovery.

We believe the earnings backdrop remains broadly supportive. The recent full-year results season showed signs of an earnings trough in real terms, with profit margins surpassing consensus expectations for a fourth consecutive quarter. This should be supportive for equities, but we expect the earnings recovery to be relatively slow as we think European economic growth will remain below trend and lower inflation should weigh on growth rates in nominal terms. We forecast 3% earnings growth this year (consensus 2%) and 4% in 2025 (consensus 10%).

Falling inflation, easing financial conditions, bottoming manufacturing activity, light investor positioning, and reasonable equity valuations (13.3x forward P/E, versus average since 1988 of 13.4x) present a relatively favorable backdrop for equities. But after the strong run, we see only modest further gains from here in the absence of a faster economic recovery or bigger interest rate cuts.

We favor beneficiaries of disinflation, interest rate cuts, and bottoming manufacturing activity, where valuations are attractive, in our view. We expect consumer sentiment to improve as real incomes turn positive and rate hikes end, boosting consumer sectors. Eurozone small- and mid-caps should benefit from easing credit conditions and a trough in activity, with relative valuations at 20-year lows. The materials sector also offers attractive relative value with upside from bottoming manufacturing activity and the end of destocking.

CIO themes

Eurozone small- and mid-caps

We see attractive value in small and midsize companies, and believe that supportive inflections are starting to emerge in the macroeconomic backdrop.

Consumer recovery

We like European consumer stocks that are poised to benefit from an improving consumer outlook as real household income growth turns positive, inflation pressures ease, and central banks stop hiking.

Greentech goes global

This theme recommends companies that will likely play a key role in the global energy transition.

Sector Preferences:

Most preferred: Consumer discretionary, consumer staples, and materials

Least preferred: Communication services and healthcare

Eurozone equities

Upside scenario

DJ Euro Stoxx 50 December 2024 target: 5,400

Inflation falls quickly, allowing central banks to ease policy at a faster pace, supporting valuations.

Faster economic recovery. In this scenario, earnings could surprise to the upside if US and European economic growth is better than expected or China's economic outlook brightens.

Companies keep pricing power. If companies can maintain pricing power, margins could expand more than we expect and revenues could stay resilient, leading to upside risks to our earnings forecasts.

Lower European gas prices could support the outlook for households and manufacturers in the region.

Downside scenario

DJ Euro Stoxx 50 December 2024 target: 3,800

Growth disappoints, triggering weaker earnings growth and lower valuation multiples in anticipation of it.

Inflation starts to turn back up, which could mean rates stay at high levels, weighing on valuations and raising the risk of a deeper growth downturn in the future.

Political risks or fiscal tightening emerge at a fragile time given high government debt levels.

Loss of European competitiveness due to structurally higher energy prices, more innovation from the US and China, and the rise of new industrial competitors.

US equities

Central scenario

S&P 500 December 2024 target: 5,200

Over the last several months, US equities have been buoyed by: 1) better-than-expected economic growth, 2) improving inflation, 3) the end of Fed rate hikes and a likely pivot to rate cuts, and 4) surging investment in AI infrastructure and applications. Despite some recent economic data that suggests a slowdown in growth and hotter-than-expected inflation, we continue to believe that these four key equity market drivers remain largely in place.

Crucially, consumer spending should continue to be supported by healthy labor market dynamics. Initial claims for unemployment insurance remain low, jobs continue to be added in the most cyclical segments of the labor market (e.g., construction), there are 1.4 open jobs for every unemployed worker, and real wages are rising. In addition, access to capital is improving with high yield markets open and the banks backing away from their tightening bias.

While inflation readings for January and February were a bit hotter than expected, we think the disinflation trends remain in place. Pricing power for corporate America continues to fall, commodity prices—although off their lows—are still muted, and consumer inflation expectations remain well contained. This should enable the Fed to start cutting interest rates later this year. We expect three rate cuts in 2024 with the first one in June. With the Fed now in a position to cut rates in case growth falters, this should limit the scope of potential downside risks for stocks.

It's been over a year since ChatGPT first burst on the scene, which has unleashed an AI arms race that shows no signs of letting up. Key semiconductor manufacturing companies expect AI chips to be supply constrained into next year. At the same time, software companies are racing to deploy applications to take advantage of the new capabilities, with many starting to gain some early traction. While expectations in this segment are elevated, we think the underlying demand will remain robust in the near term.

So even though US equities have performed very well in recent months, we think the key market drivers will remain supportive. Our 2024 and 2025 S&P 500 EPS estimates are USD 245 (+9% y/y) and USD 260 (+6% y/y), respectively.

Our year-end S&P 500 price target suggests modest upside through the end of the year, and we retain a neutral allocation to US equities in our tactical asset allocation. With some sentiment and positioning indicators looking elevated, we would not be surprised to see a modest pullback in the coming months. That could offer investors a better opportunity to add to equity positions.

Sector preferences

Most preferred

Healthcare: This is our preferred defensive sector due to faster earnings growth relative to the other defensives and the potential for certain segments—managed care and life sciences tools—to benefit from a pickup in earnings growth as the year progresses.

Industrials: The sector should benefit from resilient economic growth, an improvement in manufacturing business sentiment, a bottoming in cyclical areas such as transports, secular growth in infrastructure, re-industrialization of the US economy, and aerospace demand.

Information technology: The sector should benefit from a bottoming in PC and smartphone end-markets. AI investment spending remains robust and key components will likely remain supply constrained into next year. Investors will likely continue to gravitate to high-quality companies that have good secular growth. That all being said, the sector has performed well recently and pullbacks are possible.

US equities

Upside scenario

S&P 500 December 2024 target: 5,500

Artificial intelligence is a game-changer: The impact of artificial intelligence on productivity and earnings growth is larger and comes sooner than investor expectations.

Stronger-than-expected economic growth: High wages attract even more workers into the labor force, and demand for labor stays strong. Real incomes continue to grow, and household cash cushions remain.

Inflation cools quickly: Inflationary pressures dissipate faster than expected, and the Fed cuts rates even more than we expect. This lifts expectations for economic growth and corporate earnings.

Downside scenario

S&P 500 December 2024 target: 3,700

Recession: The US slips into a full-blown recession in the next 6–12 months, primarily driven by the lagged effects of Fed rate hikes and as household cash cushions dwindle.

Inflation stays hot: Inflation pressures reaccelerate. Central banks are forced to raise interest rates even more or keep them at lofty levels for longer than expected. Stagflation risks increase as wage-price spirals start to form.

Geopolitical turmoil: Geopolitical flashpoints spiral further out of control, potentially disrupting energy supplies or dragging more countries into hostilities.

Sector preferences

Least preferred

Real estate: The sector looks slightly expensive relative to real interest rates, which are a key driver of sector valuations. Estimates are still high in some areas that over-earned during the pandemic. Growth in adjusted funds from operations will likely lag S&P 500 profit growth.

Utilities: Increased regulatory risks and resilient economic data may lead to underperformance. We prefer to have defensive exposure through healthcare which offers better earnings growth.

UK equities

Preference: Least preferred

Central scenario

FTSE 100 December 2024 target: 7,780

We expect easing monetary policy in 2024 as inflation cools, which in combination with reasonable valuations and earnings that should be close to bottoming out should support UK equities around current levels. We rate UK equities as least preferred in our global asset class preferences as we see more upside in other markets that are expected to deliver significantly faster earnings growth than the 2% we anticipate for the FTSE 100 this year. Looking ahead to 2025, the picture should brighten, and we forecast 6–7% earnings growth driven by fading headwinds to energy and banks' profits, alongside an improving economy.

The FTSE 100 trades at 10.9x forward P/E with a 4.2% dividend yield. Valuations are attractive relative to a long-run average forward P/E for the FTSE 100 of 12.8x since 1987. However, much of that value is in the energy (7.5x P/E) and financials (7.5x P/E) sectors, reflecting market concerns about the sustainability of their profits given current oil prices and expectations for rate cuts. Excluding these sectors, we estimate the UK market trades around 14.2x forward P/E.

We believe quality stocks with strong returns on invested capital, resilient operating margins, and relatively low debt on their balance sheets are best positioned to continue generating profits amid sub-trend global growth. We also expect household disposable income growth to improve in 2024 as inflation pressures fade and interest rates come down, supporting our preference for consumer stocks across Europe.

Upside scenario

FTSE 100 December 2024 target: 8,400

Valuations rerate: A reduction of the UK's discount versus global equities offers upside risk to valuations.

Higher commodity prices: Higher commodity prices, especially oil, could provide additional upside to FTSE 100 earnings, especially relative to other regions.

Better global growth: If global economic growth is better than expected, this could support higher earnings than we currently anticipate and boost equity valuations.

CIO themes

Consumer recovery

We like European consumer stocks that are poised to benefit from an improving consumer outlook as real household income growth turns positive, inflation pressures ease, and central banks stop hiking.

Downside scenario

FTSE 100 December 2024 target: 6,000

Lower oil prices: If oil prices fall, earnings growth could be hurt as the energy sector contributes around 25% of FTSE 100 earnings.

Weaker economic growth: Should global economic growth slow more than anticipated, this would be negative for earnings and equity valuations.

Sticky inflation: Persistently high inflation could keep Bank of England rates higher for longer and put downward pressure on equity valuations and the economic growth outlook.

Stronger sterling: Sterling strength would be a drag on the FTSE 100, which generates close to 75% of its revenues outside the UK, although stronger sterling likely comes alongside a better economic growth backdrop.

Swiss equities

Central scenario

SMI December 2024 target: 11,640

After a strong 2021, we estimate corporate profits to have dropped 11% over the 2021–23 period due to the global economic slowdown and significant currency losses. This year, we expect 7.5% earnings growth, supported by robust organic sales growth; margin improvements, particularly in the healthcare, consumer staples, and financials sectors; cost-cutting measures; and no major currency losses. Although we are working on the basis of a significant economic slowdown, the greatest risk to our 2024 earnings expectations lies in an even weaker global economy than currently forecast. This would probably cause the Swiss franc to appreciate as well.

From June 2022 to June 2023, the Swiss National Bank (SNB) hiked its prime interest rate five times to mitigate inflation pressures. Higher interest rates supported the Swiss franc, which indeed was strong last year. On 21 March, the SNB cut its rate as a result of domestic inflation rates moderating significantly. This move should soften the Swiss franc. As a result, this will not support Swiss corporate profits, of which 90% of are generated in foreign currencies. We expect negative currency effects to moderate significantly from 2Q24. Moreover, we forecast further SNB rate cuts later this year.

Swiss equity valuation multiples trade at around a 10% premium to their 25-year average, which we think caps further upside potential for now. Dividend yields remain attractive, in our view, despite the now higher bond yields. At 3.3%, the expected yield is above the 25-year average of 2.4%. We think the key drivers for Swiss stock prices from here will be companies showing robust profit improvement and, to a lesser degree, multiple expansion. Hence, stock selection is important.

With European and global economic growth prospects still weakening, the defensive characteristics of the Swiss market look favorable compared to other equity markets. With regard to investment strategy, we recommend focusing on quality firms and service companies, and selectively on cyclicals and mid-caps. Companies with attractive and sustainable dividend and free cash flow yields are particularly appealing to us.

Key risks include protectionism, international trade disputes, a significant economic downturn, currency losses, and Swiss-EU negotiations.

Swiss equities

Upside scenario

SMI December 2024 target: 12,300

Robust Swiss profits: If there is only a modest global economic downturn ahead, corporate profits could expand by low teens in 2024.

Sustainable dividends: Swiss dividends have generally grown every year since 2009. In 2021, however, total SMI dividends fell by 3%. In 2022 and 2023, they recovered by 6% each. In our upside scenario, we would expect mid-single-digit percentage rises this year (i.e., for the business year 2023) and in 2025.

Manageable currency impact: In 2020, currency effects were clearly negative, while those in 2021 were insignificant. They then increased a bit in 2022 and significantly in 2023. In 2024, we expect currency losses to moderate significantly.

Downside scenario

SMI December 2024 target: 9,800

Economic and political risks: Significant global economic risks, negative currency trends, and international political disputes are headwinds for a small country with above-average international exposure.

Valuations: While dividend yields are attractive, corporate profits may be flat in 2024, leaving the SMI trading at an unjustified premium to its 25-year forward P/E average.

Sector composition: The SMI has a high exposure to defensive industries and quality companies that tend to underperform when bond yields increase strongly or economic growth expands.

Emerging market equities

Preference: Most preferred

Central scenario

MSCI EM December 2024 target: 1,100

We view emerging market (EM) equities as most preferred. The macroeconomic picture in emerging markets remains healthy. Economic activity continues to expand, with aggregate manufacturing PMIs remaining strong and economic surprises posting positive signals, while inflation continues to normalize. In our view, emerging market companies look set to deliver solid mid-teens earnings growth in 2024.

Valuations for the MSCI EM index are largely in line with their 10-year average, yet stand at an above-average discount to US and developed market stocks. In our view, this gap does not factor in the better earnings growth prospects we see for emerging markets relative to global peers.

A strong US dollar, sharply higher US rates, an uptick in geopolitical tensions, a pronounced US recession, and policy and growth disappointments in China are risks to the outlook for EM equities.

From a geographic standpoint, we rate Indonesia and Hong Kong as most preferred. We continue to expect positive macroeconomic and corporate dynamics to take the driver's seat in Indonesia, with US real yields likely having peaked, and as local election-related uncertainty diminished. In addition, Hong Kong equities will likely be driven by recovering property volumes after a relaxation on property-related, falling US rates down the road, and attractive valuations.

We recently downgraded China from most preferred to neutral. Policy details from the National People's Congress were lacking, and macroeconomic challenges persist. In the absence of solid catalysts to reverse the current negative earnings revisions trend, we struggle to see room for a meaningful rerating of Chinese equities in the near term. After a strong rally since February, we recommend trimming overexposure to the broader Chinese equities space and switching into more defensive segments with higher dividend yields and better earnings visibility.

We are also downgrading India to neutral. Though India's growth and earnings outlook remains robust, we have started to see risks of somewhat weaker consumption and over-heating bank credit. While we continue to like India structurally, we think India will perform in line with other EM peers in the near term.

At a sector level, we see opportunities in the EM tech space. More than 50% of the segment is made up of semiconductor-related companies, which should continue to perform well backed by a combination of strong revenue growth and accelerating AI-related demand. The memory price cycle should continue to trend upwards throughout the year, and only peak in early- to mid-2025, in our view. On the technology hardware side, we see signs of early recovery on end demand. The sector's valuations are fair relative to history, and attractive compared to global peers. A Fed pivot this year should bring tailwinds to the growth-oriented technology companies in the region. In this context, we favor key players in Taiwan and Korea, which account for more than 80% of the EM IT index.

From a thematic angle, we like environmental, social, and governance (ESG) leaders in emerging markets. We think these stocks can help mitigate downside risks and they present attractive valuations. For investors with a multiyear time horizon, we recommend exposure to three thematic opportunities: frontier markets, emerging market infrastructure, and emerging market healthcare.

CIO themes

ESG matters in emerging markets

This theme offers investors an opportunity to add value to their portfolios by incorporating ESG considerations into their investment decisions. The wide disparity in ESG performance among emerging market companies tells us investors should focus on those with strong management to reduce the risk of tail-risk events, particularly in relation to governance (e.g., accounting and audit issues) as well as severe environmental accidents.

Emerging market equities

Preference: Most preferred

Upside scenario

MSCI EM December 2024 target: 1,200

Sizable GDP growth recovery: A continued economic recovery would benefit corporate earnings and lift valuation multiples.

Global monetary policy: A less hawkish policy stance would bring about a more benign external environment.

China policy support: Stronger-than-expected policy easing and faster demand recovery in China would support emerging market stocks.

Downside scenario

MSCI EM December 2024 target: 820

Global GDP growth fears: Persistently high inflation could force central banks to tighten more aggressively, sending economies into a deep recession.

US dollar strength: Emerging market stocks typically suffer in a strong US dollar environment.

Geopolitics: A further deterioration in US-China relations and the war in Ukraine would hurt emerging market assets.

Market preferences

Most preferred

Indonesia, Hong Kong, Information Technology (New)

Least preferred

Malaysia, Thailand

Japanese equities

Central scenario

TOPIX December 2024 target: 2,770

We are neutral on Japanese equities in our global strategy. The TOPIX climbed higher last month after a small correction, supported by improved sentiment in the US market and JPY depreciation against USD. Large-caps dominated the rise, with the top 20 stocks contributing 50% to the YTD rally.

After the recent Bank of Japan meeting, our outlook for Japanese equities remains unchanged: We expect stronger corporate governance and robust corporate earnings growth of 12% in FY2023 (end-March 2024) and 5% in FY2024. While valuations are no longer cheap—TOPIX at 15.5x forward P/E, above the historical average of 13.7x—they look fair versus the MSCI ACWI (17.7x), with the former's P/E discount to the latter still below the long-term average.

We see near-term catalysts for Japanese equities. The labor union wage proposal in March came at the highest request since 1994 (preliminary announcement at 5.2% y/y vs. 3.6% in 2023), providing confidence to global investors in wage growth, and inflation is on a more sustainable path. The BoJ's decision to remove its negative interest rate policy and yield-curve control—and a likely absence of a rate hike in the near term—should also support risk assets. We don't expect a major drag from the ending of the BoJ's purchases of exchange-traded funds (ETFs), which was being used only sparingly for the last two years. Crucially, we could see more governance reforms disclosed during the full-year results season and medium-term plan announcements, which should support return on equity, corporate value, share buybacks, and the unwinding of cross-shareholdings.

We recommend focusing on fundamentals and quality, as we expect the JPY to appreciate alongside Fed signals of policy cuts. We prefer large-cap banks and real estate names, both of which should benefit from Japan's inflation and wage growth dynamics after 30 years of deflation. We also see opportunities in laggard cyclical stocks and like high dividend yield stocks.

Upside scenario

TOPIX December 2024 target: 2,900

Higher ROE: Greater increases in unwinding of cross-shareholdings and share buybacks, business portfolio restructuring, or increased investments to raise return on equity (an aim of the Tokyo Stock Exchange) and profit margins prompt Japanese equities to rerate in the longer term.

Global economic growth remains resilient: A strong Chinese economic recovery and a resilient US economy lead to stronger topline growth for Japanese corporate earnings.

Sustainable inflation and wage growth: Solid 2024 Shunto wage negotiations results provide confidence to investors that Japan's moderate wage growth and inflation could be sustained in 2024, and that there could be structural changes in the economy.

Downside scenario

TOPIX December 2024 target: 2,000

Recession: The US slips into a recession, and increased tensions between the US and China put downward pressure on Japan's economic and earnings growth outlook.

Sharp yen strengthening: Earnings growth would decline, especially for exporters in the tech and auto sectors, if the yen strengthens sharply..

Earlier- and higher-than-expected BoJ rate hike: While we expect policymakers to proceed with caution and keep policy rates at 0–0.1% through 2024, more aggressive hiking without sustainable wage and inflation is a downside risk.

Asian ex-Japan equities

Central scenario

MSCI Asia ex-Japan December 2024 target: 685

Inflation in the region should fall to near 2% this year, opening the door for Asia's central banks to follow the Federal Reserve and cut policy rates, starting in 2Q24. We expect Indonesia, the Philippines, and South Korea to be the first rate-cut movers in Asia. We think Asia's new orders growth returning to trend favors north Asia for now. Meanwhile, PMIs are still mixed, with no decisive trend yet. Consequently, we believe it's still too early to observe a directional trend in the Asia ex-Japan equity market. We remain focused on relative opportunities.

We downgrade India from most preferred to neutral after a rally of more than 20%; Singapore is upgraded from least preferred to neutral. India's corporate earnings trend continues to be strong, but regulators' increasing concerns lately about small- and mid-cap, option speculation, and a rapid rise in retail credit may continue and temper some of the tailwinds, despite the consensus expectation for policy continuity after the general election (19 April to 4 June). India's PMI is still strong, but risks—of a rollover toward weaker consumption and over-heating bank credit—are emerging. Meanwhile, Singapore's economic headwinds might ease due to the recovery in global orders. This, and the stabilization of its earnings trend, lead us to prefer a more neutral stance for the Singapore market.

Indonesia remains as most preferred. Prabowo has been formally confirmed as Indonesia's next president, which largely removes political overhangs for the market. The country's earnings trend remains strong, with valuations reasonable at below the five-year average level, in our view. PMI has also been consistently above 50, creating a supportive macroeconomic backdrop. High policy rates should benefit the financial sector, which has a 60% equity market weighting. Moderating inflation and heathy FX reserves also offer room for Indonesia to be one of the first rate-cut movers in the region after the Fed.

Malaysia also remains as least preferred. Malaysia's macro situation remains weak, with PMI below the sub-50 territory. Manufacturing exports are declining, and the room for rate cuts is limited due to the narrow gap between the policy rate, CPI at just 1.5%, and recent regulations encouraging exporters to retain earnings onshore. Thus, we see no near-term upside catalysts for the market.

Hong Kong has been kept as most preferred, and Thailand as least preferred. Hong Kong has robust investment in the macroeconomy, with mainland tourism arrivals recovering to around 80% of 2019's level. The recent easing of property sector policies should also help to stabilize sales volumes. The market's current dividend yield is attractive at a historical high of 4.4%, and any Fed rate cut could support a market rerating, in our view, with P/E close to –2 standard deviations below the five-year average. But for Thailand, PMI has edged down further to 45.3 in February alongside stagnant business sentiment. The country's earnings trend is muted, and valuations aren't particularly cheap, in our view, with P/E at around –0.8 standard deviations below the five-year average. The upside risks for Thailand include the launch of the digital wallet, and a policy rate cut ahead of the Fed, but we believe these upside risks might not happen in the very near term.

Finally, we keep a neutral view on China after our downgrade of China equities from most preferred to neutral following the NPC in March. The recovery of China's economy remains uneven. The manufacturing PMI was below 50 for the fifth month in a row in February. The country's CPI just had its first positive reading after five consecutive deflationary months. Also, outstanding total social financing (TSF) growth edged lower to 9%, versus 9.5% last month. Moreover, China's earnings revision breadth remains negative. Given the low valuation of the market, with P/E 1.5 standard deviations below the five-year average, we believe the downside is limited, but near-term upside catalysts are still lacking. Thus, we think investors should maintain exposure to China in their portfolios at a level similar to the long-term strategic allocation of their risk profiles.

Asian ex-Japan equities

Upside scenario

MSCI Asia ex-Japan December 2024 target: 741

Fed starts rate cuts earlier than expected

Asian equities are likely to rebound strongly if the Fed starts to cut rates or stops quantitative tightening, especially if the US economic slowdown is less severe than feared and inflation drops faster than expected.

Strong Chinese housing demand recovery

A meaningful recovery in property investment in China is likely to push Asian equity markets higher given the subdued expectations on this front.

Strong demand recovery in tech

If we see a faster-than-expected final demand pickup in this space, it could lift the Asian market as a whole as tech is a key component of MSCI Asia ex-Japan.

Downside scenario

MSCI Asia ex-Japan December 2024 target: 493

Sharp slowdown in DM growth

If US/Europe growth turns out to be much worse than our mild recession assumptions, Asian equities could be impacted.

Re-escalation in Sino-US tensions

Risk sentiment would weaken if the US adds secondary sanctions on Chinese firms or financial institutions.

Stronger US dollar

Asia ex-Japan regional equities usually suffer in a strong US dollar environment.

Market preferences

Most preferred: Hong Kong, Indonesia

Least preferred: Thailand, Malaysia

High grade

Preference: Most preferred

Central scenario

10-year US Treasury yield December 2024 target: 3.50%

With indications that inflationary pressures continue to abate, major central banks ended their rate hikes last year and are assessing when it may be appropriate to ease policy. Against this backdrop, we continue to like high grade bonds. Our rationale is that central banks have succeeded in ensuring inflation expectations remain stable and although volatility is being generated as the market looks to price the timing and magnitude of near term rate cuts, there is often downward momentum on term rates once central banks start rate cutting and the market looks to price the end point. Additionally, although there are high expectations that the US can avoid a recession given recent economic strength, the lagged transmission of all the policy rate tightening over the last two years continues to present downside risks to growth and financial stability. Interest rate volatility is likely to remain elevated, particularly in the long end of the curve, as government bond supply is large given existing deficits and maturity profiles. Accordingly, our preferred approach is to take rate risk in the 1–10-year part of the curve where the link to growth, inflation, and policy is stronger, as opposed to the ultra-long end of the curve, which has sensitivity to technical dynamics.

Upside scenario

10-year US Treasury yield December 2024 target: 2.50%

In the upside scenario for high grade bonds, growth falls sharply on a global scale toward mid-2024, owing to the delayed impact of monetary tightening or additional tightening efforts to tame persistent core inflation. Once demand for goods and services weakens, inflation drops quickly with energy prices falling and the labor market losing momentum. As recession kicks in, major central banks cut rates aggressively. Balance sheet runoff ends and QE restarts.

Downside scenario

10-year US Treasury yield December 2024 target: 4.00%

In the downside scenario for high grade bonds, US activity grows above its trend rate of 2% as labor markets and household balance sheets prove resilient to monetary policy tightening. Inflation continues to fall toward price targets, paving the way for central banks to trim policy rates down from currently restrictive levels.

Investment grade

Preference: Most preferred

Central scenario

December 2024 spread targets: 100bps (USD IG) / 140bps (EUR IG)

Investment grade credit spreads have edged lower over the past month with continued indications of strong investor demand for high-quality credit that offers historically attractive yields. While supply has strongly ramped up as per the typical trend of higher issuance levels at the start of the year, this has so far has been very well absorbed with investors demonstrating strong appetite to meet the increased bond supply. While the share of M&A-related bond issuance has increased this year, so far it is being led by higher-rated issuers with relatively low leverage, with relatively limited active releveraging thus far within the lower-rated BBB issuers.

With yields remaining elevated and major central banks in developed markets likely having ended their hiking cycles, we think total return prospects in higher-quality fixed income remain appealing over the coming quarters. US investment grade (IG) yields are at 5.3% and EUR IG yields are at 3.8% (local currency). While these levels are off their October peaks, they remain historically elevated. The elevated outright yields and the fact that spreads are a much smaller proportion of all-in yields than in the recent past are positives for forward-looking returns.

We think the total return outlook for US IG remains supported by elevated yield levels, expected lower government bond yields over the coming quarters and our outlook of relatively resilient spreads in our base case of a soft landing. We expect lower government bond yields as inflation and growth continue to moderate, and markets look to price both the upcoming rate-cutting cycle and the expected longer-term neutral policy rate in the coming quarters.

In addition, high-quality bonds tend to be resilient in a growth slowdown, as credit spread widening is usually offset to a good degree by falling interest rates. This was the case in March last year, when deteriorating risk sentiment related to concerns about the banking sector on both sides of the Atlantic caused IG spreads to widen. However, total returns were resilient as falling government bond yields more than offset the widening in credit spreads.

US IG fundamentals remain relatively solid. Median net leverage (excluding financials and utilities) edged lower to 1.9x in 4Q (compared to 2.2x in 4Q19, just prior to the pandemic) on improving earnings. Furthermore, while the median interest coverage ratio has declined from the highs reached in 2022 given rising interest expenses; as of 4Q, it was still at a solid level of 10.5x, compared to 10.4x in 4Q19. In our base case of a soft landing, the pace of nominal growth is likely to moderate yet remain overall relatively resilient this year, and we expect decent earnings growth, which is supportive of fundamentals. So, while ratings migrations have become less supportive over time, they are not expected to turn significantly negative in our base case scenario. We also note that debt growth for the median issuer has remained very muted as companies have continued to exhibit a relatively conservative balance sheet management approach overall. We view the near-term risk of rising downgrades and upward pressure on spreads as limited outside a deep recession. We continue to believe IG bonds stand to deliver attractive risk-adjusted returns, given all-in yields, resilient fundamentals and upside from falling interest rates.

Key risks to our view include a recession (though in our view spread widening would be to a good extent offset by falling interest rates in this scenario), sustained evidence of stalling progress on inflation, which could put further upward pressure on both yields and spreads as the market further reprices expectations of Fed cuts this year, as well as a material rise in creditor-unfriendly actions such as debt-funded M&A and share buybacks that would lead to rising net supply and a deterioration in credit quality over time.

Analysts: Frederick Mellors, Carolina Corvalan, Antoine Geiller

Investment grade

Preference: Most preferred

Upside scenario

Bloomberg Barclays US Int. Corp. December 2024 target: 70bps/ Bloomberg Barclays Euro-Agg. Corp. December 2024 target: 100bps

Goldilocks

Growth remains robust, inflation declines more rapidly than expected, and the Fed cuts interest rates by at least 100bps this year.

Downside scenario

Bloomberg Barclays US Int. Corp. December 2024 target: 200bps/ Bloomberg Barclays Euro-Agg. Corp. December 2024 target: 200bps

Hard landing

Growth falls sharply on a global scale, owing to the delayed impact of monetary tightening.

High yield

Central scenario

December 2024 spread targets: 400bps (USD HY) / 400bps (EUR HY)

Valuations significantly compressed starting late last year amid prospects for Federal Reserve easing and a resilient growth environment. A significant upward repricing of the near-term path of interest rates this year given upward surprises to inflation and labor market activity has done little to dent sentiment thus far. Credit availability has improved, with a broadening of high yield (HY) primary issuance to lower-rated issuers and a continued focus on refinancing.

At current valuations, US HY appears to be discounting a below-average default rate in the year ahead of 1–2%. While less tight than in the prior quarter, lending standards remain somewhat restrictive, pointing to some downside risks to growth and upside risks to defaults over the coming 12 months, though considerably less than before, while we note that financial conditions have considerably eased since late October. Our updated estimate is for defaults to reach around 4% (on an issuer-weighted basis) this year, which would equate to around 3% on a par-weighted basis. While this is relatively low, it still appears slightly above what credit spreads appear to be implying.

We still view the risk of a sharp rise in defaults as low. We have not seen the classic buildup of financial excess and leverage since the last default cycle in 2020 related to the COVID-19 pandemic, which gives some comfort. Leverage remains below the long-term average, although it has been trending higher as earnings growth has declined. The energy sector in the US, which has historically been a source of defaults in downturns, is in a relatively healthy state having deleveraged since the last default cycle.

Many companies were fortunate to lock in lower funding costs prior to the sharp moves higher in rates. Over time, this benefit diminishes as maturities approach and refinancing needs increase. Lower-rated, highly leveraged issuers are at particular risk if rates remain high for longer, given the large associated step-up in interest expenses. Such issuers could struggle to meet their refinancing needs. However, easing financial conditions recently, to a great extent on the back of expectations of Fed easing, have enabled lower-rated borrowers to access primary markets to a greater degree this year, while we also note the role of private credit in providing financing to lower-rated borrowers.

Furthermore, current spreads also appear to be discounting a below-average credit risk premium. This is the compensation credit investors require over and above expected credit losses. One explanation for this could lie in technical factors. The market has shrunk from USD 1.5tr in 2021 to USD 1.3tr today. This is due in large part to net rising stars (issuers upgraded to investment grade and therefore leaving the high yield universe). Looking ahead, the scope for further net rising stars has diminished, and net supply has been trending higher, though use of proceeds overall remain heavily skewed to refinancing.

The latest CPI reports show the disinflation process may not proceed as rapidly as expected and while further rate hikes seem unlikely, the risk of a further repricing of Fed rate cut expectations remains. While HY has thus far weathered the recent repricing in Fed cut expectations well, a further repricing may be more problematic and could lead to widening spreads, an overall tightening of financial conditions, and ultimately weigh on the growth outlook if sustained. At the same time, we note that central banks have shown a willingness to actively use their balance sheets temporarily when market conditions turn dysfunctional, and we also note that discussions at the Fed about reducing the pace of quantitative tightening are likely to increasingly come into focus.

We remain neutral on HY bonds. Although we forecast scope for moderately wider spreads in HY in the coming quarters, the current level of outright yields in US HY remains historically elevated at around 8% at an index level. This is important as the high yield market generates significant carry with every passing day. The higher level of rates provides a sizable buffer against mark-to-market losses that could occur from potential widening in credit spreads.

High yield

Upside scenario

ICE BofA US high yield spread December 2024 target: 300bps / ICE BofA Euro high yield spread December 2024 target: 325bps

Goldilocks

Growth remains robust, inflation declines more rapidly than expected, and the Fed cuts interest rates at least 100bps this year.

Downside scenario

ICE BofA US high yield spread December 2024 target: 800bps / ICE BofA Euro high yield spread December 2024 target: 800bps

Hard landing

A slowdown in growth, possibly resulting from the cumulative effect of interest rate hikes so far, results in a recession.

Emerging market bonds

Central scenario

December 2024 spread targets: 400bps (EM sovereign bonds) /325bps (EM corporate bonds)

After widening in January, yields on emerging market (EM) bonds tightened in February by 30bps to 7.9% for sovereign bonds and by 13bps to 7% for corporate bonds (JPMorgan EMBIG Diversified and CEMBI Diversified indexes, respectively). With this move, both indexes returned to the levels at the start of the year. The asset class this year has been driven to a large extent by volatility in US Treasury rates. While the core services CPI (+5.2% y/y in February) likely remains too high for the Fed to start cutting rates before June, we think a softer labor market, slower economic growth, and further moderation in shelter inflation will help overall CPI to trend lower in the coming months. Our base case remains that inflation will fall enough to allow the Fed to embark on an easing cycle at the June meeting, with a total of 75 basis points of cuts (three cuts) in 2024. We expect yields to finish the year lower; our December 10-year US Treasury forecast is 3.5%.

Primary market activity has been robust year-to-date, with EM sovereign pricing about USD 80bn of paper and EM corporates issuing around USD 94bn. Encouragingly, EM high yield (HY) sovereign issuers have also staged a comeback to the market, accounting for over 40% of EM sovereign issuance in February. Given the spread tightening for various HY sovereign issuers driven by positive idiosyncratic developments, we wouldn't rule out further issuance from this space and capital market access to broaden over time.

We maintain a neutral stance on EM USD-denominated bonds. At current levels, we view EM bond spreads of 357bps for sovereigns and 271bps for corporates as moderately expensive. This leaves the asset class vulnerable to temporary setbacks, in our view. These could occur due to various reasons, including negative growth and inflation shocks, or escalating geopolitical tensions. However, in our base case, we think EM bonds will deliver mid- to high-single-digit total returns until year-end, supported by high nominal yields and prospects for US policy rate cuts and a weaker US dollar.

Analysts: Michael Bolliger, Alejo Czerwonko, Frederick Mellors, Carolina Corvalan

Emerging market bonds

Upside scenario

EMBIG Diversified / CEMBI Diversified spread December 2024 targets: 340bps / 260bps

Goldilocks: China's economy recovers faster than expected as it opts for large-scale fiscal stimulus measures, coupled with a global economy that exhibits resilience to tight financial conditions. Major central banks start cutting policy rates earlier and to a greater extent than expected as inflation normalizes ahead of expectations, in order to avoid monetary policy becoming too restrictive in real terms.

Commodity price recovery: A further price appreciation in commodities improves the terms of trade for commodity-exposed issuers and strengthens fiscal positions.

Downside scenario

EMBIG Diversified / CEMBI Diversified spread December 2024 targets: 600bps / 550bps

Economic slump: A sharp global economic slowdown leads to weaker EM currencies, deteriorating credit quality due to fiscal vulnerabilities, and wider spreads.

Fed remains on hold: Fed could be forced to stay on hold for longer if labor and inflation data continues to run hot, which could tighten financial conditions and weigh on growth.

Geopolitical tensions escalate: Heightened friction, emanating from either the war in Ukraine, the conflict in the Middle East or US-China relations, hurts risk sentiment, strengthening the US dollar and curbing appetite for EM assets.

Rising populism: Increased conflicts within and between countries could arise as populist policies become more widespread globally.

Asian bonds

Central scenario

JACI composite spread December 2024 target: 250bps

After the February US inflation release, US Treasury yields drifted slightly higher to 4.34% (as of 18 March 2024). While the February CPI data was noisy across segments, we think the US economy remains in good shape and is heading for a soft landing. Our base case expects the Federal Reserve to begin to trim rates at the June meeting, for a total of 75 basis points of cuts (three cuts) in 2024. Against this backdrop, we continue to believe bonds—especially high-quality segments like high grade (HG) bonds and investment grade (IG) bonds—could be attractive in terms of risk-reward this year.

Asia credits delivered positive performance in the past month driven by credit spreads tightening. Among Asia credits, our overall assessment remains largely unchanged. With the uptick in yields, we think that Asia IG bonds continue to present solid risk-reward potential. The current yield level of Asia IG bonds of around 5.6% (as of 18 March 2024) remains at a 16-year high, and looks attractive considering its high credit quality (average rating of A-), supportive technical factors (net issuances still negative), and stable fundamentals for most issuers. Potential rate cuts will also benefit IG bonds which have an average duration of five years. Despite valuations being on the tight end of the spectrum, (132bps as of 18 March 2024), we think that spreads could remain resilient in the absence of a sharp economic slowdown globally or in Asia.

Asia high yield (HY) bonds had a strong start this year, and the positive momentum continued into March. This was driven by broad-based spread tightening across multiple HY markets including mainland China, India, Indonesia and Macau. Indeed, outside of mainland China, we are seeing improving fundamentals for issuers in these regions and we believe that there are still some bond selection opportunities from a bottom-up perspective. We still retain a cautious approach on China HY property after the recent rally. With still very weak sales in January and February, coupled with China Vanke's intention to extend non-standard debt from insurers, this may hurt sentiment across other distressed property bonds.

Asian bonds

Upside scenario

JACI composite spread December 2024target: 220bps

Much faster recovery: If China's recovery is faster and stronger than expected in the coming months, Asian credits would likely see upside.

Sharp property rebound: Policy has been focused on demand-side measures so far, but the housing sales recovery remains uneven and mixed. A rebound in housing sales or more details on supporting developers' liquidity needs would offer fundamental support to the credit metrics of this sector.

More dovish-than-expected central bank action: Spreads would likely compress if the Fed becomes more dovish than expected and less aggressive with quantitative tightening if US inflation comes off faster than expected.

Downside scenario

JACI composite spread December 2024 target: 320bps

Much higher default rates: The HY sector may see a sell-off if default rates far exceed current market pricing.

Increased China-US tensions: Heightened friction emanating from the upcoming US presidential election could hurt risk appetite for EM Asia assets.

Deep US/Europe recession: If the US or Europe falls into a deep recession, growth in Asia and sentiment toward Asian credit would be impacted.

Gold

Central scenario

Gold December 2024 target: USD 2,250/oz

Gold surged to a new record intraday high of USD 2,141.79/oz in recent days (previously USD 2,135.39/oz), with the quarter-to-date average now standing at a new record high above USD 2,030/oz. And while we have been one of the few calling for materially higher gold prices this year based on fundamentals, not everything stacks up over the last day or so. For example, as gold is a non-yield bearing asset, lower interest rates tend make the metal more appealing to investors. But in recent weeks, the reverse actually has been the case—i.e., the chances of a Federal Reserve rate cut in June fell to about 64% from 90% a month ago. Moreover, money market pricing of the quantum of Fed rate cuts this year also declined from 117bps a month ago to 86bps; money markets now imply a 21bps cut for June.

So, gold is clearly being driven by other factors. We believe more technical factors were at play recently, with prices crossing key resistance levels, but the increasing focus on the US presidential election, ongoing buying by central banks, and still relatively modest speculative positioning signal this rally has further to run over the medium term, particularly if ETF buying returns (usually trend following). However, as important US data approaches, we prefer to wait for price setbacks while acknowledging these could be modest and short lived. We also like select gold miners with attractive valuations versus gold.

Crude oil

Central scenario

Brent crude oil December 2024 target: USD 82/bbl

The latest "Commitment of Trader" data shows that non-commercial accounts have slightly reduced week-over-week their netholdings in crude oil futures and options in the week ending on 12 March. Since that date, the price of Brent crude oil has increased by more than 5%. There has been a substantial increase in open interest (the sum of long and short positions) in Brent, reaching the highest level since November 2021. The increase in the US oil benchmark WTI has been more moderate. We think Brent saw an increase in long positions, while the additions of long together with a reduction in short positions in WTI might have limited the increase in open interest.

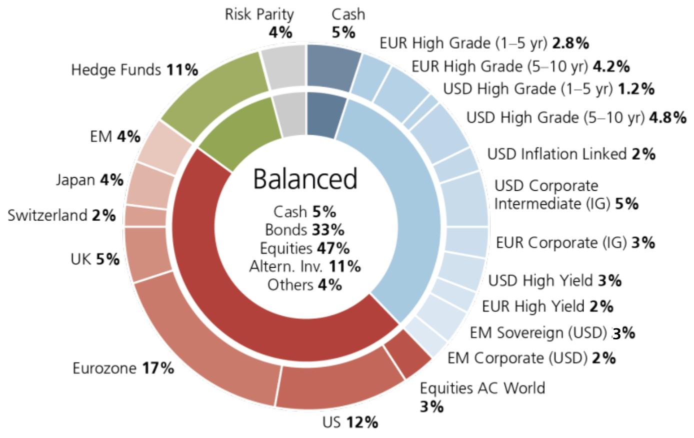
We believe several factors have supported the return of financial investors' interest in crude oil. Oil demand data so far in 2024 has surprised on the positive side. The International Energy Agency increased its 1Q24 demand growth by 270kbpd to 1.7mbpd y/y last week. As a result, oil inventories did not increase as much this year as many market participants had thought, but moved sideways to lower. Also, the extension of the voluntary OPEC+ production cuts for another three months is likely to keep the oil market undersupplied in 2Q24. With Brent expected to trade in a USD 80–90/bbl range this year, we continue to advise investors with a high risktolerance to sell Brent's downside price risks or to add exposure to longer-dated Brent oil contracts.

Section 4

Appendix

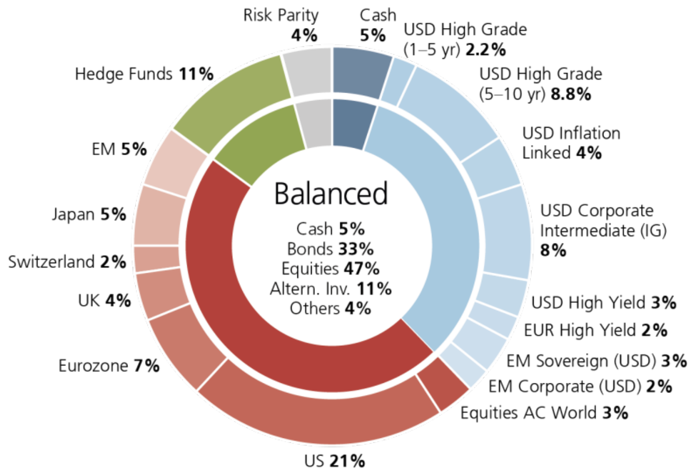
Strategic Asset Allocations (SAAs)

EUR (local portfolio)



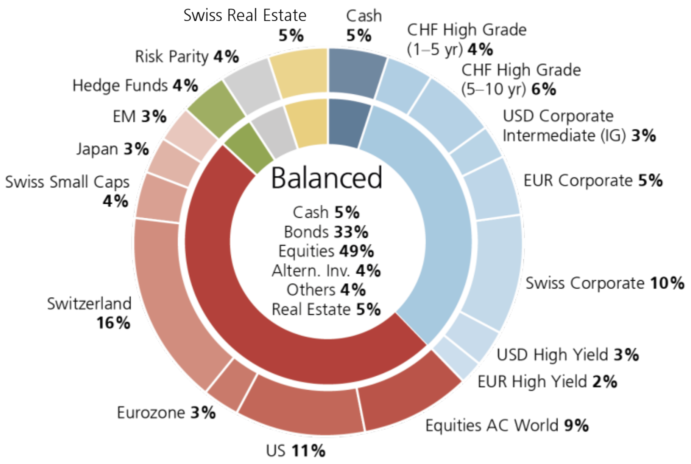
Note: Portfolio weightings are for EUR SAA with a home bias and a balanced risk profile. We expect a balanced EUR SAA to have an average total return of 5.7% p.a. and a volatility of 8.7% p.a. over the next 15 years.

USD



Note: Portfolio weightings are for a USD SAA with a balanced risk profile. We expect a balanced USD SAA to have an average total return of 6.4% p.a. and a volatility of 8.8% p.a. over the next 15 years.

CHF (local portfolio)



Note: Portfolio weightings are for CHF SAA with a home bias and a balanced risk profile. We expect a balanced CHF SAA to have an average total return of 4.9% p.a. and a volatility of 8.6% p.a. over the next 15 years.

Source: SAA as of January 2024

For illustrative purposes only. The above asset classes and allocations are indicative only and can be changed at any time at UBS's discretion without informing the client. All expected returns are p.a. and reflect the arithmetic mean of the estimated return distribution. Risk is measured as annualized volatility of monthly log-returns. Annualized expected risk and return figures are forward-looking and not a reliable indicator of future performance. Forecasts are not a reliable indicator of future performance / results. Please always read in conjunction with the glossary and the risk information at the end of the document.

Contact list

Global Chief Investment Officer GWM

Mark Haefele
mark.haefele@ubs.com

UBS CIO GWM Global Investment Office

Global Asset Allocation
Adrian Zuercher
adrian.zuercher@ubs.com

Global Asset Allocation
Mark Andersen
mark.andersen@ubs.com

UBS CIO GWM Regional Chief Investment Offices

US
Solita Marcelli

APAC
Min Lan Tan
min-lan.tan@ubs.com

EMEA
Themis Themistocleous
themis.themistocleous@ubs.com

Switzerland
Daniel Kalt
daniel.kalt@ubs.com

Risk information

UBS Chief Investment Office's ("CIO") investment views are prepared and published by the Global Wealth Management business of UBS Switzerland AG (regulated by FINMA in Switzerland) or its affiliates ("UBS"), part of UBS Group AG ("UBS Group"). UBS Group includes Credit Suisse AG, its subsidiaries, branches and affiliates. Additional disclaimer relevant to Credit Suisse Wealth Management follows at the end of this section.

The investment views have been prepared in accordance with legal requirements designed to promote the **independence of investment research**.

Generic investment research – Risk information:

This publication is **for your information only** and is not intended as an offer, or a solicitation of an offer, to buy or sell any investment or other specific product. The analysis contained herein does not constitute a personal recommendation or take into account the particular investment objectives, investment strategies, financial situation and needs of any specific recipient. It is based on numerous assumptions. Different assumptions could result in materially different results. Certain services and products are subject to legal restrictions and cannot be offered worldwide on an unrestricted basis and/or may not be eligible for sale to all investors. All information and opinions expressed in this document were obtained from sources believed to be reliable and in good faith, but no representation or warranty, express or implied, is made as to its accuracy or completeness (other than disclosures relating to UBS). All information and opinions as well as any forecasts, estimates and market prices indicated are current as of the date of this report, and are subject to change without notice. Opinions expressed herein may differ or be contrary to those expressed by other business areas or divisions of UBS as a result of using different assumptions and/or criteria.

In no circumstances may this document or any of the information (including any forecast, value, index or other calculated amount ("Values")) be used for any of the following purposes (i) valuation or accounting purposes; (ii) to determine the amounts due or payable, the price or the value of any financial instrument or financial contract; or (iii) to measure the performance of any financial instrument including, without limitation, for the purpose of tracking the return or performance of any Value or of defining the asset allocation of portfolio or of computing performance fees. By receiving this document and the information you will be deemed to represent and warrant to UBS that you will not use this document or otherwise rely on any of the information for any of the above purposes. UBS and any of its directors or employees may be entitled at any time to hold long or short positions in investment instruments referred to herein, carry out transactions involving relevant investment instruments in the capacity of principal or agent, or provide any other services or have officers, who serve as directors, either to/for the issuer, the investment instrument itself or to/for any company commercially or financially affiliated to such issuers. At any time, investment decisions (including whether to buy, sell or hold securities) made by UBS and its employees may differ from or be contrary to the opinions expressed in UBS research publications. Some investments may not be readily realizable since the market in the securities is illiquid and therefore valuing the investment and identifying the risk to which you are exposed may be difficult to quantify. UBS relies on information barriers to control the flow of information contained in one or more areas within UBS, into other areas, units, divisions or affiliates of UBS. Futures and options trading is not suitable for every investor as there is a substantial risk of loss, and losses in excess of an initial investment may occur. Past performance of an investment is no guarantee for its future performance. Additional information will be made available upon request. Some investments may be subject to sudden and large falls in value and on realization you may receive back less than you invested or may be required to pay more. Changes in foreign exchange rates may have an adverse effect on the price, value or income of an investment. The analyst(s) responsible for the preparation of this report may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, synthesizing and interpreting market information.

Different areas, groups, and personnel within UBS Group may produce and distribute separate research products **independently of each other**. For example, research publications from **CIO** are produced by UBS Global Wealth Management. **UBS Global Research** is produced by UBS Investment Bank. **Research methodologies and rating systems of each separate research organization may differ**, for example, in terms of investment recommendations, investment horizon, model assumptions, and valuation methods. As a consequence, except for certain economic forecasts (for which UBS CIO and UBS Global Research may collaborate), investment recommendations, ratings, price targets, and valuations provided by each of the separate research organizations may be different, or inconsistent. You should refer to each relevant research product for the details as to their methodologies and rating system. Not all clients may have access to all products from every organization. Each research product is subject to the policies and procedures of the organization that produces it.

The compensation of the analyst(s) who prepared this report is determined exclusively by research management and senior management (not including investment banking). Analyst compensation is not based on investment banking, sales and trading or principal trading revenues, however, compensation may relate to the revenues of UBS Group as a whole, of which investment banking, sales and trading and principal trading are a part.

Risk information

Tax treatment depends on the individual circumstances and may be subject to change in the future. UBS does not provide legal or tax advice and makes no representations as to the tax treatment of assets or the investment returns thereon both in general or with reference to specific client's circumstances and needs. We are of necessity unable to take into account the particular investment objectives, financial situation and needs of our individual clients and we would recommend that you take financial and/or tax advice as to the implications (including tax) of investing in any of the products mentioned herein.

This material may not be reproduced or copies circulated without prior authority of UBS. Unless otherwise agreed in writing UBS expressly prohibits the distribution and transfer of this material to third parties for any reason. UBS accepts no liability whatsoever for any claims or lawsuits from any third parties arising from the use or distribution of this material. This report is for distribution only under such circumstances as may be permitted by applicable law. For information on the ways in which CIO manages conflicts and maintains independence of its investment views and publication offering, and research and rating methodologies, please visit www.ubs.com/research-methodology. Additional information on the relevant authors of this publication and other CIO publication(s) referenced in this report; and copies of any past reports on this topic; are available upon request from your client advisor.

Important Information About Sustainable Investing Strategies: Sustainable investing strategies aim to consider and incorporate environmental, social and governance (ESG) factors into investment process and portfolio construction. Strategies across geographies approach ESG analysis and incorporate the findings in a variety of ways. Incorporating ESG factors or Sustainable Investing considerations may inhibit UBS's ability to participate in or to advise on certain investment opportunities that otherwise would be consistent with the Client's investment objectives. The returns on a portfolio incorporating ESG factors or Sustainable Investing considerations may be lower or higher than portfolios where ESG factors, exclusions, or other sustainability issues are not considered by UBS, and the investment opportunities available to such portfolios may differ.

External Asset Managers / External Financial Consultants: In case this research or publication is provided to an External Asset Manager or an External Financial Consultant, UBS expressly prohibits that it is redistributed by the External Asset Manager or the External Financial Consultant and is made available to their clients and/or third parties.

USA: This document is not intended for distribution into the US and / or to US persons.

For country information, please visit ubs.com/cio-country-disclaimer-gr or ask your client advisor for the full disclaimer.

Additional Disclaimer relevant to Credit Suisse Wealth Management
You receive this document in your capacity as a client of Credit Suisse Wealth Management. Your personal data will be processed in accordance with the Credit Suisse privacy statement accessible at your domicile through the official Credit Suisse website https://www.credit-suisse.com. In order to provide you with marketing materials concerning our products and services, UBS Group AG and its subsidiaries may process your basic personal data (i.e. contact details such as name, e-mail address) until you notify us that you no longer wish to receive them. You can optout from receiving these materials at any time by informing your Relationship Manager.
Except as otherwise specified herein and/or depending on the local Credit Suisse entity from which you are receiving this report, this report is distributed by Credit Suisse AG, authorised and regulated by the Swiss Financial Market Supervisory Authority (FINMA). Credit Suisse AG is a UBS Group company.

Version A/2024. CIO82652744