Key themes and their investment implications for Q2 2023

	Asset Allocation	Equities	Fixed income	Private markets	Real estate
Hard vs. soft landing	▪ Currently, the fallout from SVB has not changed our medium-term outlook. We still expect a hard landing but at a later date. We are defensively positioned, underweight credit and overweight cash. ▪ We think markets are under-pricing the risk of a recession in DM and that credit will be the first to come under pressure. Equities are supported by sentiment and strong labour markets for now. ▪ Within credit, we prefer IG for its higher quality, defensive characteristics.	▪ This quarter could be volatile amid issues in the banking sector alongside ongoing uncertainty over the future path of the global economy and interest rates. ▪ Equity markets are yet to fully reflect the potential hit to earnings from a faltering global economy. ▪ For companies, the near-term pain is evident in our survey's wide range of data points. Our analysts expect a rise in debt defaults over the next 12 months.	▪ The risk of a hard landing is not yet fully priced into HY spreads. Credit conditions are tightening, the weighted average cost of capital is increasing. High yield bonds offer high all-in yields, but spreads still don't provide adequate protection for a hard landing.	▪ Private debt less impacted by dichotomy of hard vs soft landing – both suggest challenges, but even in the hardest landing scenario, the private debt product retains protections at the most senior secured position of the capital structure, while floating rate nature mitigates impact of volatile rates backdrop.	▪ In a soft-landing scenario, the recent repricing in real estate should provide a good foundation for performance driven by a combination of rental growth and attractive yield. ▪ In a hard-landing, higher inflation and or interest rates could cause a further wave of repricing and reduced liquidity and reduced confidence. ▪ Real estate related debt and bond exposure could create a crisis in confidence in the broader sector.
Risks and opportunities	▪ SVB highlights the risks involved with today's fast pace of tightening. The Fed has been amongst the most aggressive – one reason why we favour a relative underweight in US equities. Now, the fallout looks to be contained but we will continue to monitor the situation as it unfolds. ▪ European small caps have lagged the broader recovery in Europe equities, creating the opportunity for a catch up. They are priced for a deep recession while the outlook is for a milder recession.	▪ We believe an earnings correction will occur this year. Corporate profit margins are under pressure, and rising funding costs are also adding risk. ▪ US earnings woes are likely to be extended, driven by multiples compression, with a strong labour market weighing on margins. ▪ China's re-opening is a significant boost for equities within Asia. Regional earnings for 2023 remain encouraging vs global markets.	▪ Refinancing is becoming more expensive for companies and rising interest rates are already having an effect on the residential mortgage market and auto loans. This is normally the time to gain duration exposure: government bonds typically outperform higher-risk assets at this point in the cycle. ▪ The next maturity wall occurs in 2025. However, at the margin there will be companies that do need to refinance and this will be expensive.	▪ The sectors that dominate the European private debt market are predominantly stable – services etc. – with limited exposure to Russia or inflated energy prices. ▪ Europe offers more mature market than U.S. with more experienced borrowers and fewer names from more stressed subsectors.	▪ Limited exposure to energy, banking, and tech sectors. ▪ Structural changes in supply chains continue to create demand for logistics. ▪ Acute shortage of supply and abundance of demand in sustainable buildings. Linked to companies net zero carbon ambitions.
China reopening	▪ We prefer EM equities to DM equities. We also expect EM currencies to be supported. ▪ Other beneficiaries of China's reopening include the Thai baht, the Australian dollar, and Indonesian and Chinese A-Shares equities. ▪ We prefer Asia high yield to that of Europe and the US.	▪ The rapid reopening has resulted in a spike in valuations among Chinese equities. The next stage will be a switch to earnings as the main driver for future gains. ▪ Earnings per share (EPS) still has a long way to go to catch up with the historical average peak increase. ▪ Chinese corporates enjoy favourable tailwinds. Monetary and fiscal policies are both accommodative and inflation remains benign.	▪ The macroeconomic backdrop remains supportive in China, with Covid cases having peaked, easing monetary policy from the People's Bank of China (PBOC), and increasing fiscal support. This will be expensive.	▪ Europe currently enjoying the economic tailwind from China reopening, but this is likely to have postponed any expected recession rather than resolving the risk completely. ▪ Economic buoyancy seen in borrowers' input costs decreasing, but wage pressures persist and this continues to weigh on operating cash flow.	

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