Global Asset Allocation Views

Insights and implications from the Multi-Asset Solutions Strategy Summit

4Q 2021

AUTHOR

John Bilton, CFA
Managing Director
Head of Global Multi-Asset Strategy
Multi-Asset Solutions

IN BRIEF

- Over recent months, we have seen a slowing of growth momentum and a renewed focus from some investors on potential tail risks. Despite a moderating pace of growth, we see a positive direction for the global economy and further upside for corporate earnings.
- Central banks are past the point of maximum monetary policy accommodation, but even so, financial conditions remain extremely easy, with negative real rates set to persist for some time, providing a supportive backdrop for risk assets.
- We favor a pro-risk tilt with an overweight (OW) to stocks spread across the U.S., Europe and Japan, and with a modest cyclical tilt. Stock-bond correlation has returned to negative territory, so while we take a mild underweight to duration, we acknowledge its role as a portfolio diversifier.
- Credit stays at a small OW but with returns driven largely by carry; although valuations are undemanding, we remain neutral on emerging market equity and debt, as the growth and earnings outlooks continue to lag developed markets.

ASSET CLASS VIEWS (PAGE 3)

Underweight ● Neutral ● Overweight ●

Asset class		Opportunity set	UW	N	OW	Change	Conviction
MAIN ASSET CLASSES		Equities	○	○	●		High
		Duration	●	○	○		Low
		Credit	○	○	●		Low
		Cash	●	○	○		Moderate
PREFERENCE BY ASSET CLASS	EQUITIES	U.S.	○	○	●		Moderate
		Europe	○	○	●		Moderate
		UK	○	●	○		
		Japan	○	○	●		Moderate
		Emerging markets	○	●	○		
	FIXED INCOME	U.S. Treasuries	●	○	○		Low
		G4 ex-U.S. sovereigns	○	●	○		
		EMD hard currency	○	●	○		
		EMD local FX	○	●	○		
		Corporate investment grade	○	●	○		
		Corporate high yield	○	○	●		Low
	CURRENCY	USD	○	●	○		
		EUR	○	○	●		Low
		JPY	●	○	○		Moderate
		EM FX	○	●	○	▼	

BETWEEN MEMORIAL DAY IN MAY AND LABOR DAY IN SEPTEMBER – THE TRADITIONAL U.S. SUMMER SEASON – THE S&P 500 MADE A RECORD 28 ALL-TIME HIGHS IN 69 DAYS OF TRADING, DELIVERING A PRICE RETURN OF 7.9%. The upward grind of stocks in this most unusual of summers ran counter to the "Sell in May and go away" maxim: On average over the last 50 years, the S&P returned 1.7% between May and September, and 7.3% from September to the following May. A summer rally does have precedent, but the record number of new highs – against the backdrop of monetary policy uncertainties, Chinese regulatory change and the ebb and flow of coronavirus statistics – certainly bears scrutiny.

We continue to expect above-trend growth through the end of 2022 and see further upside for equity earnings as economies around the globe reopen fully and pent-up demand materializes. But without doubt, the momentum of growth is diminishing, and over the summer we saw economic surprise indices drop from elevated levels.

While moderating growth presents a headwind for stocks, not least by denting sentiment, a supportive backdrop remains in place: ample liquidity, strong household balance sheets and a powerful capex cycle. Crucially, too, not all of the rebound in equity earnings is yet reflected in analysts' forecasts – providing a basis for further upside.

To be sure, there are some confusing signals across markets — not least from the bond market, which continues to appear detached from fundamental growth and inflation dynamics. But we would argue that this situation could persist for some time, given the ongoing central bank demand for duration, as well as other, less price-sensitive demand for bonds, such as by pension portfolios de-risking. Even accounting for a tapering of Federal Reserve (Fed) purchases starting later this year, we expect real yields to remain profoundly negative throughout 2022.

In the dog days of summer, we were certainly reminded that risks beyond COVID-19 continue. Regulatory tightening in China and, most recently, issues in China's property sector have weighed on the wider emerging market (EM) complex. But even when they did, the U.S. and other developed equity markets remained reasonably poised. While some would argue a correction might be overdue, even in the event of a drawdown we would expect buyers to emerge quickly — noting, as we do, that the underlying combination of growth drivers and easy policy probably still outweigh the potential tail risk issues.

In our multi-asset portfolios, we reflect our economic optimism with continued overweights (OW) in equities and credit and continued underweights (UW) in duration and cash. Within equities, we maintain a preference for developed markets over emerging markets, with reasonable balance across the U.S., Europe and Japan — the U.S. providing a quality angle to our exposure and Europe and Japan offering a welcome cyclical tilt. In credit, we favor high yield, but at this mid-cycle stage in the economic expansion, we note that credit is largely a carry, rather than a capital growth, asset.

On the face of it, very little has changed in our preferred asset allocation from our last Strategy Summit, in June. However, below the surface, we continue to make subtle but important changes within portfolios. Notably, our attitude to duration has shifted. At the start of the year, we expected a rapid rise in yields and could take a pro-growth stance through an underweight in bonds. For a time, stock-bond correlations drifted into positive territory, in turn presenting a challenge to portfolio construction. As the sum of investors' fears has shifted from inflation to growth, negative stock-bond correlation has reasserted itself, and despite low prevailing yields, bonds once again play a valuable role in portfolios, offsetting pro-risk positions taken in stocks.

While we continue to expect yields to rise from here and note that our quant models remain strongly negative on duration, we expect both the scale and the pace of yield increases to be modest. For investors with a significant pro-risk stance in equities, the portfolio benefits of holding duration may now outweigh the mildly negative outlook that we have on bonds in isolation.

In sum, our portfolio maintains a pro-risk tilt, mainly through stocks. While we see the momentum of equity returns moderating, we do not expect a change in the direction over the coming months. The greatest risk to our portfolio stance today is a disappointment on growth — not an overshoot in inflation. But at the same time, we note that policymakers around the globe remain committed to supporting nominal growth, and this, in our view, provides a supportive backdrop for risk assets.

Multi-Asset Solutions Key Insights & "Big Ideas"

The Key Insights and "Big Ideas" are discussed in depth at our Strategy Summit and collectively reflect the core views of the portfolio managers and research teams within Multi-Asset Solutions. They represent the common perspectives we come back to and regularly retest in all our asset allocation discussions. We use these "Big Ideas" as a way of sense-checking our portfolio tilts and ensuring they are reflected in all of our portfolios.

- Global growth above trend; U.S. mid-cycle, rest of world a little earlier
- Inflation elevated for now but set to return toward target in 2022
- Fiscal and monetary policy accommodative but focus is on tapering
- Yields drift up slowly; negative stock-bond correlation back in play
- Dollar supported near-term by rates, but long-run trend still lower
- Further EPS upside supports stocks while multiples decline further
- OW equities balanced across DM regions; still too soon for emerging markets
- Prefer a blend of quality, value and cyclical sectors in equities
- Key risks: supply chain issues, new virus strains, growth disappoints

Active allocation views

These asset class views apply to a 12- to 18-month horizon. Up/down arrows indicate a positive (▲) or negative (▼) change in view since the prior quarterly Strategy Summit. These views should not be construed as a recommended portfolio. This summary of our individual asset class views indicates strength of conviction and relative preferences across a broad-based range of assets but is independent of portfolio construction considerations.

Underweight ● Neutral ● Overweight ●

Asset class	Opportunity set	UW	N	OW	Change	Conviction	
MAIN ASSET CLASSES	Equities	○	○	●		High	Momentum but not direction of earnings recovery moderating; further upside from earnings, not multiples
	Duration	●	○	○		Low	Yields set to grind higher, but demand for bonds still robust, esp. with correlation to stocks again negative
	Credit	○	○	●		Low	Carry is attractive and default risk low at this stage in the cycle; limited scope for capital appreciation
	Cash	●	○	○		Moderate	Cash rates set to remain very negative as policy rates set to remain well below prevailing inflation in 2022
PREFERENCE BY ASSET CLASS – EQUITIES	U.S.	○	○	●		Moderate	Strong earnings delivery and high quality in large caps are attractive; small caps supported by reopening trends
	Europe	○	○	●		Moderate	Meaningful upside potential for earnings as economy reopens, and attractive exposure to cyclicality
	UK	○	●	○			Cheap valuations and decent dividends, but supply chain concerns and political uncertainty are headwinds
	Japan	○	○	●		Moderate	Earnings revisions catching up to other developed equity regions and are very positive relative to history
	Emerging markets	○	●	○			Growth concerns in China a major headwind for EM; strong returns from Korea and Taiwan likely peaking
PREFERENCE BY ASSET CLASS – FIXED INCOME	U.S. Treasuries	●	○	○		Low	Fed set to taper over 1H22, but demand elsewhere remains solid; expect rates to move up but only slowly
	G4 ex-U.S. sovereigns	○	●	○			Ex-U.S. inflation pressure lower, and central banks more vocally committed to lower yields
	EMD hard currency	○	●	○			Attractive valuations are offset, to a degree, by asset class's long duration and questionable fundamentals
	EMD local FX	○	●	○			Valuations attractive on a relative basis, but growth uncertainty across EM a concern and a drag on EM FX
	Corporate investment grade	○	●	○			Tight spreads, but ongoing demand, especially in longer maturities, likely from portfolio de-risking flow
	Corporate high yield	○	○	●		Low	Defaults low, but spreads are tight; new issuance being well absorbed, but now very much a carry asset
PREFERENCE BY ASSET CLASS – CURRENCY	USD	○	●	○			Long-term outlook sees dollar lower, but policy differentials and EM growth concerns lend near-term support
	EUR	○	○	●		Low	Growth improvement supports EUR over medium term, but easy ECB policy likely slows pace of appreciation
	JPY	●	○	○		Moderate	BoJ's ongoing commitment to easy policy could lead to some weakness as safe haven demand fades
	EM FX	○	●	○	▼		Uncertain EM growth outlook creates more nuanced backdrop for EM FX over next couple of quarters

Source: J.P. Morgan Asset Management Multi-Asset Solutions; assessments are made using data and information up to September 2021. For illustrative purposes only.

Diversification does not guarantee investment returns and does not eliminate the risk of loss. Diversification among investment options and asset classes may help to reduce overall volatility.

MULTI-ASSET SOLUTIONS

J.P. Morgan Multi-Asset Solutions manages over USD 303 billion in assets and draws upon the unparalleled breadth and depth of expertise and investment capabilities of the organization. Our asset allocation research and insights are the foundation of our investment process, which is supported by a global research team of 20-plus dedicated research professionals with decades of combined experience in a diverse range of disciplines.

Multi-Asset Solutions' asset allocation views are the product of a rigorous and disciplined process that integrates:

- Qualitative insights that encompass macro-thematic insights, business-cycle views and systematic and irregular market opportunities
- Quantitative analysis that considers market inefficiencies, intra- and cross-asset class models, relative value and market directional strategies
- Strategy Summits and ongoing dialogue in which research and investor teams debate, challenge and develop the firm's asset allocation views

As of June 30, 2021.

NEXT STEPS

For more information, contact your J.P. Morgan representative.

IMPORTANT DISCLAIMER

For the purposes of MiFID II, the JPM Market Insights and Portfolio Insights programs are marketing communications and are not in scope for any MiFID II / MiFIR requirements specifically related to investment research. Furthermore, the J.P. Morgan Asset Management Market Insights and Portfolio Insights programs, as non-independent research, have not been prepared in accordance with legal requirements designed to promote the independence of investment research, nor are they subject to any prohibition on dealing ahead of the dissemination of investment research.

This document is a general communication being provided for informational purposes only. It is educational in nature and not designed to be taken as advice or a recommendation for any specific investment product, strategy, plan feature or other purpose in any jurisdiction, nor is it a commitment from J.P. Morgan Asset Management or any of its subsidiaries to participate in any of the transactions mentioned herein. Any examples used are generic, hypothetical and for illustration purposes only. This material does not contain sufficient information to support an investment decision and it should not be relied upon by you in evaluating the merits of investing in any securities or products. In addition, users should make an independent assessment of the legal, regulatory, tax, credit, and accounting implications and determine, together with their own financial professional, if any investment mentioned herein is believed to be appropriate to their personal goals. Investors should ensure that they obtain all available relevant information before making any investment. Any forecasts, figures, opinions or investment techniques and strategies set out are for information purposes only, based on certain assumptions and current market conditions and are subject to change without prior notice. All information presented herein is considered to be accurate at the time of production, but no warranty of accuracy is given and no liability in respect of any error or omission is accepted. It should be noted that investment involves risks, the value of investments and the income from them may fluctuate in accordance with market conditions and taxation agreements and investors may not get back the full amount invested. Both past performance and yields are not reliable indicators of current and future results.
J.P. Morgan Asset Management is the brand for the asset management business of JPMorgan Chase & Co. and its affiliates worldwide.

To the extent permitted by applicable law, we may record telephone calls and monitor electronic communications to comply with our legal and regulatory obligations and internal policies. Personal data will be collected, stored and processed by J.P. Morgan Asset Management in accordance with our privacy policies at https://am.jpmorgan.com/global/privacy.

This communication is issued by the following entities:

In the United States, by J.P. Morgan Investment Management Inc. or J.P. Morgan Alternative Asset Management, Inc., both regulated by the Securities and Exchange Commission; in Latin America, for intended recipients' use only, by local J.P. Morgan entities, as the case may be.; in Canada, for institutional clients' use only, by JPMorgan Asset Management (Canada) Inc., which is a registered Portfolio Manager and Exempt Market Dealer in all Canadian provinces and territories except the Yukon and is also registered as an Investment Fund Manager in British Columbia, Ontario, Quebec and Newfoundland and Labrador. In the United Kingdom, by JPMorgan Asset Management (UK) Limited, which is authorized and regulated by the Financial Conduct Authority; in other European jurisdictions, by JPMorgan Asset Management (Europe) S.à r.l. In Asia Pacific ("APAC"), by the following issuing entities and in the respective jurisdictions in which they are primarily regulated: JPMorgan Asset Management (Asia Pacific) Limited, or JPMorgan Funds (Asia) Limited, or JPMorgan Asset Management Real Assets (Asia) Limited, each of which is regulated by the Securities and Futures Commission of Hong Kong; JPMorgan Asset Management (Singapore) Limited (Co. Reg. No. 197601586K), which this advertisement or publication has not been reviewed by the Monetary Authority of Singapore; JPMorgan Asset Management (Taiwan) Limited; JPMorgan Asset Management (Japan) Limited, which is a member of the Investment Trusts Association, Japan, the Japan Investment Advisers Association, Type II Financial Instruments Firms Association and the Japan Securities Dealers Association and is regulated by the Financial Services Agency (registration number "Kanto Local Finance Bureau (Financial Instruments Firm) No. 330"); in Australia, to wholesale clients only as defined in section 761A and 761G of the Corporations Act 2001 (Commonwealth), by JPMorgan Asset Management (Australia) Limited (ABN 55143832080) (AFSL 376919). For all other markets in APAC, to intended recipients only.

For U.S. only: If you are a person with a disability and need additional support in viewing the material, please call us at 1-800-343-1113 for assistance.

Copyright 2021 JPMorgan Chase & Co. All rights reserved.

PROD-0921-714806-AM-PI-GAAV 4Q21 | 0903c02a81cef736

J.P.Morgan
Asset Management