

## Human Actions Dominating Investment Trends

Many asset managers remain perplexed. Contrary to widespread forecasts for, first, transitory inflation and, then, recession, both have yet to fully materialize.

It should now be clear that the current environment is markedly different. It is rocked by global disruption, geopolitical fragmentation and intensive propaganda. Nonetheless, asset managers must respond. They need to shift and tack.

But, in which direction?

The dilemma is that there are no historical frameworks — cyclical or secular — to rely upon, as there are now epochal behavioural shifts from both policymakers and individual investors. What's more, humans often change their minds frequently and suddenly. Diffidence and flippancy are both part of the human neural wiring.

That means markets are often pulled in different directions by “human actions”. The challenge is that these changes can be capricious and sudden or take place over several decades.

Our investment team therefore monitors these human-driven trends because these are the primordial source of financial and economic impetus. What are today's most important “human action” examples?

**Global Fragmentation:** The pro-globalization consensus of the 2000s is now being replaced with a more critical version. China's efforts to supersede America and to set-up alternate world systems is now fully in play. Importantly, China is now the only major economy that can deviate directionally from the US's domestic growth path. As China re-opens, growth trends between the West and Asia Pacific are set to diverge: the former will slow, while the latter will accelerate.

**Global Demographic Shift:** The global millennial generation, now entering their prime working years, is now the world's largest generation — some 1.8 billion strong and nearly a quarter of the world population. Nearly nine in every ten millennials live outside developed markets. And, especially in Emerging Asia, they are experiencing rapid income growth. As the lead consumer cohort, they are set to shape the direction of the global economy in the coming years.

**Global Warming Fears:** Whether readers agree with climate change theories or not, it is clear that fossil fuels will be steadily replaced by renewable electricity as the world's dominant energy. 91% of global governments are committed. The point is this: decarbonization will be enormously capital intensive, comparable to the post-WWII reconstruction boom, as infrastructure, transportation networks and technologies require vast amounts of fixed investment.

The above “Super Trends”, all of which are driven by human actions (and are global in scope), will dominate world affairs and portfolio return vectors for the coming decade at least. This explains why consensus forecasts have been wide off the mark

over the last year: many have not yet included macro-minded analysis, but now, more than ever, will need to include these frameworks into their portfolio analysis.

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## CASH AND CURRENCIES

### Deploying excess cash

- Cash balances were raised sharply last quarter to cushion against volatility emanating from regional bank failures in the US.
- Institutional investor positioning followed suit, with survey data showing some of the most extreme defensive positioning in recent history.
- Such extreme readings are a reliable contrarian indicator. Cash and equivalents have been decreased but remain modestly overweight in client portfolios.

### Emerging markets (EM) carry trade

- Inflation in emerging markets varies across countries but is broadly trending lower.
- Many EM central banks were more proactive than their developed market peers, aggressively raising policy rates once signs of inflationary pressure first emerged.
- With an unusually wide real yield advantage vs. developed markets, EM currencies offer an attractive carry opportunity. We remain overweight EM currency exposure in client portfolios.

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## GLOBAL EQUITIES

### Increasing equity overweight

- When a recession occurs in a disinflationary environment, equity markets tend to bottom only once it becomes evident that the economy has bottomed.
- But in an inflationary environment (as is the case today), stocks generally rally once central banks begin to ease monetary policy.
- With policy pauses and pivots drawing near in many economies worldwide, we opted to increase equity allocations this quarter.

## US bank stocks in focus

- The failure of multiple regional banks in the US has shaken investor confidence in the financial sector.
  - However, bank solvency remains strong, regulators have acted expeditiously to shore up liquidity and protect depositors, and credit risk from commercial real estate exposure is manageable.
  - We have switched from a broad market-cap weighted US financial sector overweight to a more targeted equally-weighted US bank exposure in client portfolios.
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## GLOBAL FIXED INCOME

### Remaining underweight fixed income

- Despite much higher nominal yields compared against recent history, real yields in most markets remain deeply negative.
- With our expectation of “sticky” inflation for longer than the consensus currently expects, bonds continue to be relatively unattractive vs. equities.
- We remain underweight fixed income exposure this quarter.

### Moving from floating to fixed

- Staying short duration, particularly for North American exposure, remains a key tenet of our fixed income strategy, as inverted yield curves do not compensate for the risk at the long end of the curve.
  - However, with central banks at or near the end of their tightening cycles, a rotation from floating rate (whose interest rates reset lower with central bank rate cuts) to fixed rate (where prices would rise as yields fall) is warranted.
  - Overweight floating rate exposure in Canada and the US has been replaced with short-term corporate bond exposure in client portfolios.
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## OPPORTUNITY INVESTMENT HIGHLIGHTS

### Sticking with industrial metals

- Industrial metals prices have been weak of late, as developed market demand concerns persist, while the economic recovery in China has been somewhat disappointing thus far.
- Regardless, metals remain attractive over a medium-to-longer term time horizon due to under-investment over the past decade and a forthcoming surge in demand from decarbonization initiatives.
- Industrial metals-sensitive exposures including Chilean, Brazilian and global metals and mining industry equities have been maintained in balanced and growth-oriented strategies.

### Selling hard currency EM debt

- We maintain a favourable view on EM debt, as we expect EM inflation to continue to roll-over, policy rates to ebb and growth to outpace developed markets.
- However, our preference is for local currency debt rather than hard currency (primarily US dollar-denominated) as the latter is exposed to a weakening greenback and tends to take cues from the US high yield bond market which we believe is vulnerable to widening spreads.
- EM hard currency bond exposure has been reduced in income-oriented strategies this quarter.

INVESTMENT STANCE	Versus Benchmark			Changes from previous quarter
	Under	Neutral	Over	
<b>NET GLOBAL ASSET MIX</b>				
Cash			⬇️	⬇️ Decreased
Total Equity			⬇️	⬆️ Increased
Total Fixed Income	⬇️			⬆️ Increased
Opportunity		⬇️		➡️ Unchanged
<b>CANADA INVESTMENTS</b>				
Bonds	⬇️			⬆️ Increased
Stocks		⬇️		⬆️ Increased
<b>U.S. INVESTMENTS</b>				
Bonds		⬇️		⬆️ Increased
Stocks	⬇️			⬇️ Decreased
<b>INTERNATIONAL INVESTMENTS</b>				
Bonds	⬇️			➡️ Unchanged
Stocks			⬇️	⬆️ Increased