PIMCO

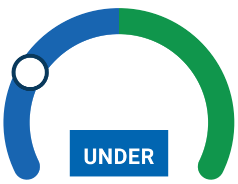
Risk-Off, Yield-On

PIMCO believes an extreme shift in macroeconomic conditions over the course of 2022 and the corresponding impact on financial markets have significantly altered the relative attractiveness of asset classes. Markets are moving away from a “TINA” world (where “there is no alternative” to equities) to one in which fixed income is increasingly appealing.

Yet, as we navigate a period of elevated inflation and an economic slowdown, our starting point is one of caution. PIMCO’s business cycle models forecast a U.S. recession in the next year, and the U.S. Federal Reserve is pressing ahead with policy tightening despite increasing strain in financial markets.

Here is a summary of how we are positioning multi-asset portfolios in light of our global economic outlook.

OVERALL RISK

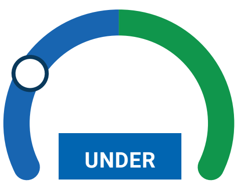


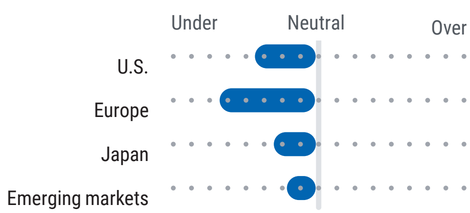
Our view is that the global economy will enter a significant slowdown, with some countries tipping into recession. We are therefore underweight risk. We believe most asset classes are not yet fully discounting the impact of sticky inflation, persistent interest rate hikes, and lower growth.

POSITIONING

OPPORTUNITIES

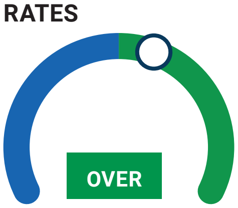
EQUITIES

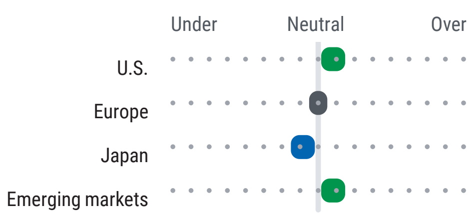




We maintain a negative outlook for equities given elevated recessionary risk. Valuations are still far above levels consistent with our macro outlook, and Bloomberg’s consensus estimates for 2023 earnings growth remain too optimistic. Among developed markets (DMs), neither the U.S. nor Europe is attractive. Synchronized policy tightening also makes emerging market (EM) equities unattractive. Among sectors, we prefer defensive areas, such as healthcare, versus cyclicals such as industrials.

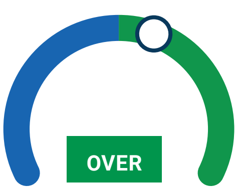
RATES

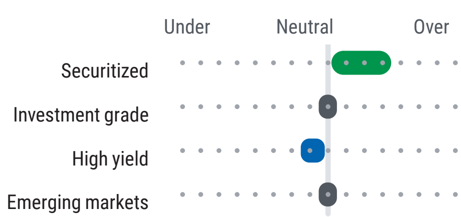




Duration has historically been a valuable hedge in uncertain times, but sticky inflation keeps us close to neutral. Duration should become increasingly attractive; however, with the first opportunities in the most rate-sensitive DMs and certain EMs that hiked early. Duration should also become attractive in the U.S. as the Fed brings the hiking cycle to a close and as economic fundamentals deteriorate further.

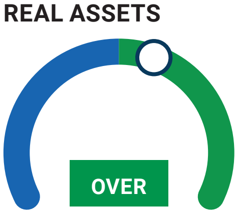
CREDIT

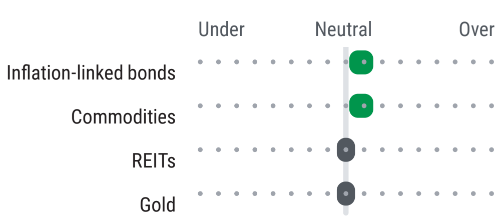




We believe credit will become attractive again after yields stabilize – likely at higher levels than we’ve seen in the last decade. In corporate credit, we think higher-quality issuers are best positioned to navigate cyclical pressures, and lower-quality and cyclically sensitive issuers will suffer. U.S. agency mortgage-backed securities (MBS) with high coupons could provide attractive returns, as they are of higher average quality and tend to provide good liquidity at an attractive spread.

REAL ASSETS





We currently favor select assets within commodities markets, which should provide an inflation hedge. However, as we progress through 2023, inflation is likely to moderate and economic growth will turn negative – a challenging scenario for commodities historically. Our view on real estate investment trusts (REITs) is neutral, with a focus on relative value opportunities. Lastly, we maintain a balanced allocation to inflation-linked bonds as we expect inflation to be sticky in the near term.

CURRENCIES

We believe the U.S. dollar can continue to outperform in the short term. However, overvaluation concerns should begin to prevail when peak rates are reached. The euro faces structural challenges, particularly in peripheral economies, which may discourage investors even as rates rise, while a resolution to the war in Ukraine (not our base case) would present an upside risk. We find select EM currencies attractive relative to DM, but overall we maintain modest overweights given prevailing macro conditions.