MENTENOVA

HOUSEVIEW TACTICAL ASSET ALLOCATION

21 July 2022

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We have decided to keep our tactical asset allocation unchanged for August, with SA cash being the balancing figure.

Figure 1: Houseview Tactical Asset Allocation

Asset class	--	-	Neutral	+	++
SA cash				■	
SA bonds				■	
SA inflation-linked bonds		■			
SA-listed property		■			
SA equity			■		
Foreign cash				■	
Foreign bonds			■		
Foreign equity			■		
Foreign property		■			

Synopsis

We have reiterated our prior positions across all asset classes. We have chosen to remain moderately overweight in SA nominal bonds, based on attractive valuations, improving fiscal conditions and better compensation for inflation than that offered by SA inflation-linked bonds. We have kept our moderately underweight position in SA inflation-linked bonds as the breakeven inflations implied by the inflation-linked bonds suggest that this asset class is expensive over the medium- to long-term maturities, despite the upside risk to inflation in the short term. With the SARB front-loading its rate hiking cycle, increasing the repo rate by 75bps in July, we do expect central bank actions to curb the runaway inflation. In growth-dominated regimes, equities and bonds typically tend to have been associated with negative correlations. Given the weakening growth momentum, we have therefore chosen to remain neutral in offshore equities and offshore bonds so that the portfolio is balanced to growth and inflation. Owing to the leverage inherent in listed property, making this asset class more sensitive to rate hikes than the broader equities, we have therefore remained moderately underweight in local and offshore listed properties.

TAA Overview

Market overview	After another difficult quarter for markets, local and offshore equities had a slight reprieve into July. Regionally, the ALSI and Capped SWIX indices were up 2.4% and 2.3% respectively for the month to date, as at 19 July 2022. The S&P 500, STOXX 600 and Nikkei 225 gained 4.1%, 4.1% and 2.2% respectively over the same period. Developed market equities outperformed those of emerging markets, with the MSIC World returning 3.3% vs MSCI Emerging Markets extending the losing streak and returning -1.7%. Growth stocks saw a stronger rebound into July, up 5.3% vs 1.3% from the value stocks, but the former still significantly lagged the latter for the year to date. Bonds have been hit hard so far this year, failing to provide investors with diversification and protection, as markets have priced in significant further increases in interest rates on top of those already announced. We do, however, expect the correlation between equities and bonds to continue to come off in the near future as recession fears loom in the face of central banks continuing to pursue an aggressive course of monetary tightening. Local and offshore property sectors followed the direction of the broader equity market, recovering some lost ground into July. Commodities were largely in the red for the month to date, as the dampened growth outlook hurt industrial metals and the strong greenback hurt commodities in general. Local fixed income returned -2.1% for the month to date, as at 19 July 2022, while the WGBI Index return in ZAR was

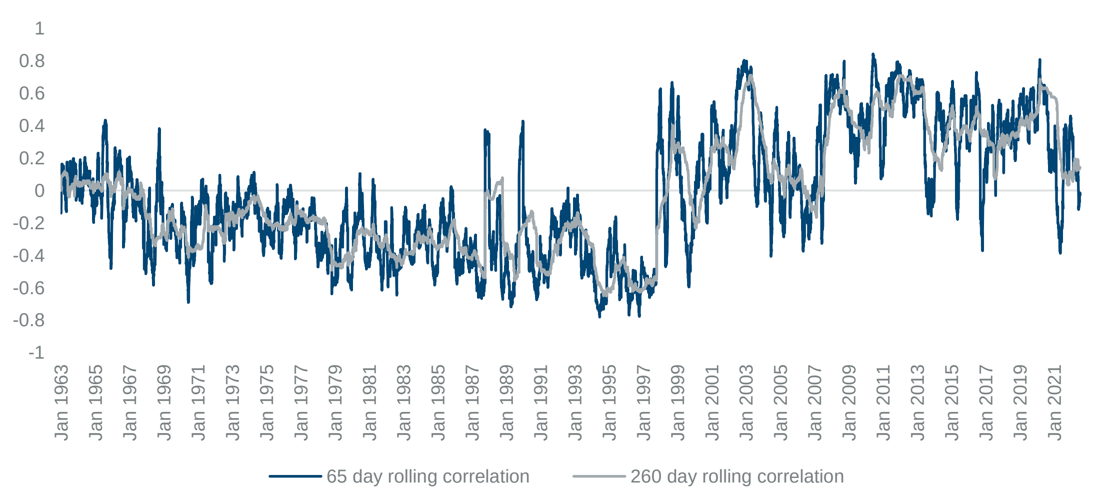
amplified by the 5.0% rand depreciation against the US dollar. The dollar strengthened by 1.9% against other major currencies for the month to date.

Figure 2: Major indices and asset class returns in local currency

30 June 2022 (Local Currency)	1M	3M	YTD	1 Year	3 Year (annualised)	5 Year (annualised)	10 Year (annualised)	MTD 19 July 2022
FTSE/JSE ALSI Total Return	-8.0%	-11.7%	-8.3%	4.7%	8.2%	8.7%	10.5%	2.4%
FTSE/JSE Capped SWIX Total Return	-7.5%	-10.6%	-4.6%	6.9%	6.8%	5.9%	9.1%	2.3%
S&P 500 Total Return	-8.3%	-16.1%	-20.0%	-10.6%	10.6%	11.3%	13.0%	4.1%
STOXX 600 Total Return	-8.0%	-9.5%	-15.0%	-7.8%	4.3%	4.0%	7.8%	4.1%
Nikkei 225 Total Return	-3.1%	-4.9%	-7.3%	-6.5%	9.5%	7.7%	13.5%	2.2%
MSCI World Total Return	-8.6%	-16.1%	-20.3%	-13.9%	7.5%	8.2%	10.1%	3.3%
MSCI ACWI Total Return	-8.4%	-15.5%	-20.0%	-15.4%	6.7%	7.5%	9.3%	2.7%
MSCI EM Total Return	-6.6%	-11.3%	-17.5%	-25.0%	0.9%	2.5%	3.4%	-1.7%
MSCI World Value Index	-8.8%	-11.4%	-11.8%	-5.9%	5.4%	5.5%	8.5%	1.3%
MSCI World Growth Index	-8.5%	-21.1%	-28.7%	-22.2%	8.7%	10.3%	11.4%	5.3%
MSCI World Small Cap Index	-9.9%	-17.1%	-22.4%	-21.6%	4.6%	5.2%	9.3%	3.8%
FTSE UK Series FTSE All Share TR	-6.0%	-5.0%	-4.6%	1.6%	2.4%	3.3%	6.9%	2.1%
MSCI AC Asia Ex. Japan Index	-4.5%	-9.0%	-16.3%	-24.9%	2.4%	3.4%	5.8%	-2.2%
MSCI Europe Excluding United Kingdom Index	-8.1%	-9.9%	-16.9%	-10.0%	5.0%	4.7%	9.2%	4.4%
STEFI	0.4%	1.2%	2.2%	4.2%	5.0%	5.9%	6.1%	0.3%
ALBI	-3.1%	-3.7%	-1.9%	1.3%	5.8%	7.8%	7.2%	-2.1%
IGOV	-1.0%	3.0%	3.2%	10.8%	7.2%	5.4%	6.3%	-1.5%
WGBI	-3.1%	-8.9%	-14.8%	-16.8%	-4.3%	-1.2%	-0.7%	-0.8%
Bloomberg Global Inflation-Linked Total Return Index	-5.3%	-14.0%	-17.8%	-15.0%	-1.1%	0.7%	1.2%	-1.1%
Bloomberg US Agg Total Return	-1.6%	-4.7%	-10.3%	-10.3%	-0.9%	0.9%	1.5%	0.2%
Bloomberg EuroAgg Total Return Index	-2.3%	-7.1%	-12.1%	-12.6%	-3.7%	-0.9%	1.9%	1.0%
Bloomberg Global Agg Corporate Total Return Index	-3.6%	-8.7%	-15.5%	-16.5%	-2.3%	0.2%	1.7%	0.2%
Bloomberg US Corporate High Yield Total Return Index	-6.7%	-9.8%	-14.2%	-12.8%	0.2%	2.1%	4.5%	2.7%
Bloomberg Pan-European High Yield Total Return Index	-6.8%	-10.7%	-14.3%	-13.8%	-1.8%	0.1%	4.4%	1.9%
J.P. Morgan EMBI Global Core Hedged EUR	-7.0%	-12.9%	-21.8%	-23.0%	-7.0%	-3.4%	0.6%	-1.8%
SAPY Total Return	-10.3%	-11.6%	-12.7%	0.2%	-9.0%	-7.3%	2.7%	5.4%
MSCI US REIT Total Return	-7.4%	-16.9%	-20.3%	-6.4%	4.0%	5.3%	7.3%	2.6%
S&P Global Property Total Return	-8.1%	-16.5%	-19.3%	-13.1%	-0.6%	2.5%	5.5%	1.4%
STOXX 600 Real Estate Total Return	-16.5%	-25.3%	-30.0%	-24.1%	-4.1%	-2.0%	4.7%	5.9%
FTSE EPRA Nareit Global REITs TR Index	-8.3%	-17.0%	-20.0%	-10.1%	0.6%	3.3%	5.8%	2.3%
Crude Oil	-6.5%	6.4%	47.6%	52.8%	19.9%	19.1%	1.6%	-6.5%
Aluminium	-12.3%	-29.9%	-12.9%	-3.1%	10.8%	5.0%	2.5%	-2.3%
Copper	-12.6%	-20.4%	-15.0%	-11.9%	11.3%	6.8%	0.7%	-11.9%
Gold	-1.6%	-6.7%	-1.2%	2.1%	8.6%	7.8%	1.2%	-5.3%
Platinum	-7.4%	-9.1%	-7.4%	-16.6%	2.4%	-0.6%	-4.7%	-2.1%
Nickel	-20.1%	-29.5%	8.5%	24.4%	21.5%	19.3%	3.1%	0.0%
Palladium	-3.1%	-14.5%	1.9%	-30.3%	8.1%	18.1%	12.8%	-3.1%
Iron Ore	-13.4%	-18.9%	1.3%	-45.3%	0.8%	13.4%	-1.6%	-20.4%
Bloomberg Commodity Index Total Return	-10.8%	-5.7%	18.4%	24.3%	14.3%	8.4%	-0.8%	-0.8%
USDZAR	4.1%	11.4%	2.1%	13.9%	4.9%	4.5%	7.1%	5.0%
GBPZAR	0.5%	3.3%	-8.1%	0.4%	3.5%	3.1%	4.5%	3.5%
EURZAR	1.7%	5.5%	-5.9%	0.7%	2.1%	2.7%	5.1%	2.5%
JPYZAR	-1.2%	-0.1%	-13.4%	-6.6%	-2.8%	0.6%	1.6%	3.1%
Dollar Index Spot	2.9%	6.5%	9.4%	13.3%	2.9%	1.8%	2.5%	1.9%

Source: Bloomberg

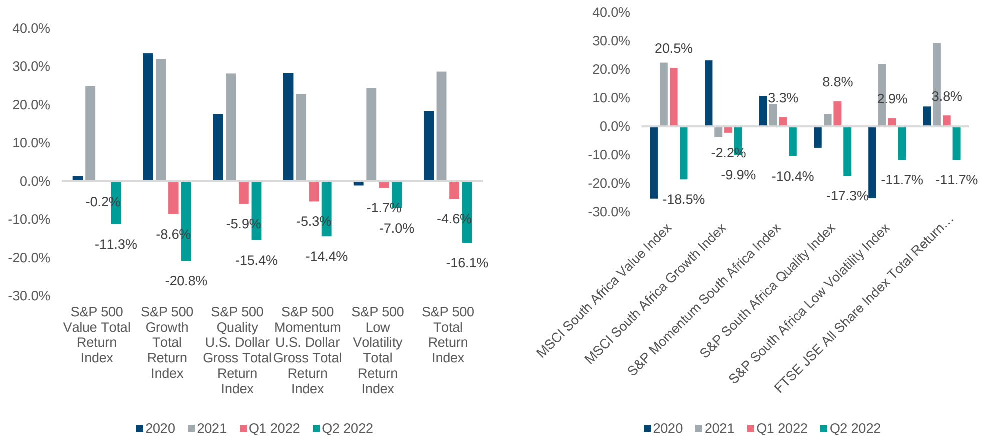
Figure 3: Correlation between S&P 500 and US 10-year Treasury



Source: Bloomberg

From a style perspective, the low volatility and value indices meaningfully outperformed the S&P 500 Index for the second quarter. For SA equities, growth and momentum were the two best-performing indices which marginally outperformed the ALSI.

Figure 4: US and SA style indices performance in local currency



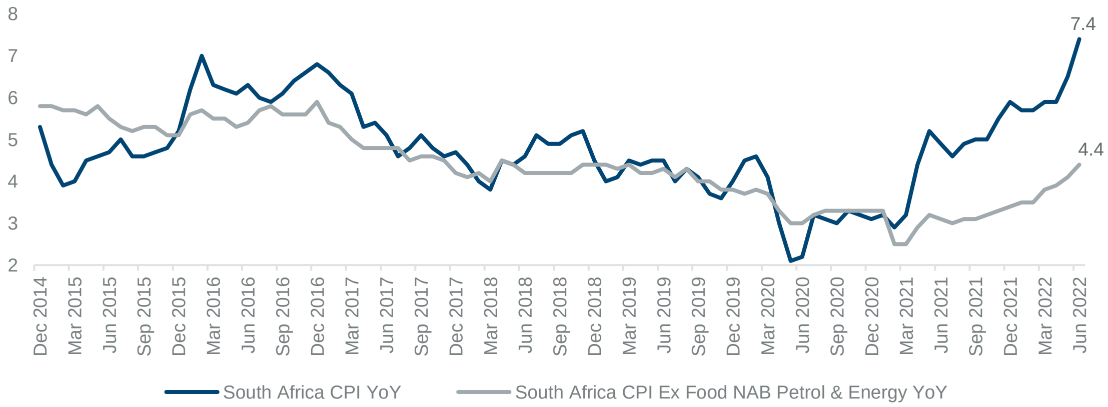
Source: Bloomberg

SA equities

Economic updates for South Africa were mixed, with improving business confidence and a strong trade figure, but weaker consumer confidence and anaemic retail sales data. The South Africa Consumer Confidence Index weakened from -12 in March to -25 in June, while the BEAR South Africa Composite Business Confidence Index jumped from -4 to 42 over the same period. The trade surplus increased from R15.5bn in April to R28.3bn in May, exceeding the market expectation of R26.3bn. However, the manufacturing PMI declined from 54.8 in May to 52.2 in June, with yearly and monthly growth in manufacturing production being negative in May, as the country experienced probably one of the worst years of loadshedding ever. According to the loadshedding app, EskomSePush, which calculates the loadshedding days based on cumulative time spent in rotational power cuts, Eskom had implemented 46 days of loadshedding by 11 July 2022. If we count any day during which loadshedding was in effect, it would be 73 days, as of 11 July 2022, according to Eskom Systems Operator general manager, Isabel Fick.

Retails sales were flat in May, and we expect SA consumers to remain under significant pressure as elevated fuel and food inflation and rising interest rates erode disposable income.

Figure 5: SA inflation



Source: Bloomberg

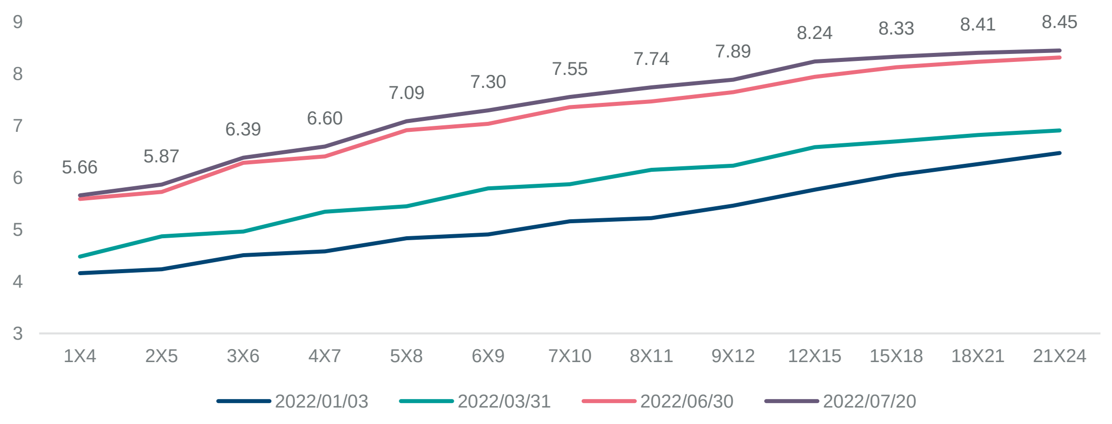
Figure 6: SA inflation rates per category

	Latest Weight	July 2021 YoY	August 2021 YoY	September 2021 YoY	October 2021 YoY	November 2021 YoY	December 2021 YoY	January YoY	February YoY	March YoY	April YoY	May YoY	June YoY
Reported		4.6%	4.9%	5.0%	5.0%	5.5%	5.9%	5.7%	5.7%	5.9%	5.9%	6.5%	7.4%
Calculated		4.7%	5.0%	5.0%	5.1%	5.5%	5.9%	5.7%	5.7%	6.1%	5.9%	6.6%	7.5%
Housing & Utilities	22.6%	3.8%	3.8%	4.0%	4.0%	3.9%	4.3%	4.3%	4.4%	4.8%	4.8%	4.9%	5.1%
Food & Non Alcoholic Beverages	19.2%	6.7%	6.9%	6.6%	6.1%	5.5%	5.5%	5.7%	6.4%	6.2%	6.0%	7.6%	8.6%
Miscellaneous Goods & Services	14.8%	4.2%	4.2%	4.3%	4.3%	4.2%	4.3%	4.6%	3.2%	3.2%	3.8%	3.9%	4.0%
Transport	14.7%	8.0%	9.9%	10.1%	10.9%	15.0%	16.7%	14.5%	14.3%	15.7%	14.7%	15.7%	20.0%
Alcoholic Beverages & Tobacco	5.9%	5.2%	5.0%	4.2%	4.0%	4.8%	4.8%	4.7%	4.8%	5.9%	6.3%	6.6%	6.7%
Recreation & Culture	4.9%	1.7%	1.9%	1.6%	1.4%	1.3%	1.4%	1.9%	2.0%	1.7%	1.5%	1.9%	2.1%
Household Contents & Services	4.3%	1.3%	1.3%	1.8%	1.8%	1.9%	2.1%	2.2%	2.6%	3.0%	3.3%	4.3%	4.7%
Clothing & Footwear	4.0%	1.8%	2.0%	1.9%	1.9%	1.8%	1.7%	1.5%	1.6%	1.6%	1.7%	1.7%	2.0%
Restaurants & Hotels	3.4%	2.3%	2.7%	3.2%	4.1%	3.7%	4.2%	5.0%	6.1%	6.7%	5.6%	6.2%	6.2%
Communication	2.6%	-0.5%	-0.5%	-0.6%	-0.6%	-0.6%	-0.6%	-0.9%	-0.9%	-0.9%	-0.9%	-0.6%	-0.2%
Education	2.3%	4.1%	4.1%	4.1%	4.1%	4.1%	4.1%	4.1%	4.1%	4.4%	4.4%	4.4%	4.4%
Health	1.3%	3.6%	3.5%	3.6%	3.8%	3.8%	3.7%	3.4%	4.9%	4.9%	4.7%	4.9%	5.1%

Source: Bloomberg

The FRA rates suggest that the market is pricing in a policy rate of 6.6% by the end of this year, with the Bloomberg Survey of Economists indicating that the median forecast was for the SARB to raise rates from 4.75% to 5.25% in the afternoon of our monthly TAA meeting. Subsequent to our meeting, the SARB hiked the rate by 75bps, taking it to 5.50% (exceeding market expectations), to rein in resurgent inflation. Three members of the MPC voted for a 75bps hike, one for a 100bps hike and one for a 50bps hike. Tighter financial conditions are not conducive to growth, but the credible central bank and the hawkish stance adopted to stabilise prices will support the local currency. Local consumers will certainly feel the squeeze from the rising cost of living and higher cost of servicing debt. Overall, markets lacked a clear catalyst for a change in sentiment or economic outlook. As a result, we continue to prefer to stay neutral in SA equities on the back of slowing global growth, high inflationary pressures, tighter monetary policies and other idiosyncratic issues constraining domestic growth.

Figure 7: SA FRA rates



Source: Bloomberg

SA bonds

Despite SA bonds continuing to be attractive from an implied-yield and a hedged-yield perspective, while offering good value on a real-yield basis compared to other emerging-market nominal bonds as well as local inflation-linked bonds and cash, we have not seen a significant return of investors' appetite for our local nominal bonds over the past few months. Non-residents' holdings of SA government bonds declined further from 28.4% in May to 27.4% in June 2022. Foreign investors net sold $10.3n of SA bonds as at 14 July. While SA government debt fared well from a governance perspective, the visibility of the rate path and external factors seemed to dominate investors' appetite for our bonds. We chose to maintain our moderately overweight position in SA nominal bonds on the relatively attractive valuation of our nominal bonds, together with the attractiveness of our nominal bonds over inflation-linked bonds as compensation for inflation.

Figure 8: SA 10-year nominal bond yield vs implied 10-year yield

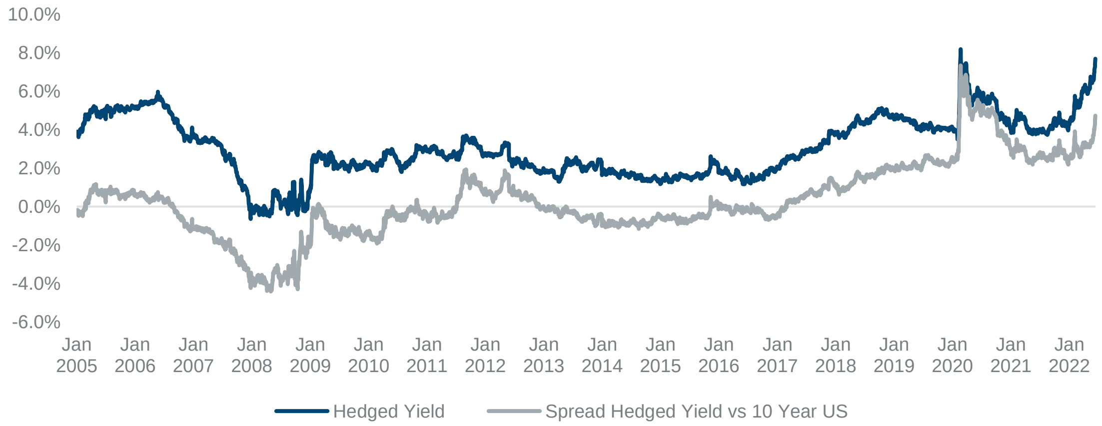
Source: Bloomberg

Figure 9: SA 10-year nominal bond real yields vs other EM peers

	South Africa	India	Indonesia	Russia	Mexico	Brazil	Turkey
10 Year Yield	**11.54%**	**7.44%**	**7.46%**	**15.99%**	**9.16%**	**13.75%**	**18.81%**
Inflation	7.4%	7.0%	4.35%	15.90%	8.0%	11.9%	78.6%
Inflation Expectation	6.21%	5.40%	3.80%	15.20%	7.33%	10.00%	70.00%
10 Year Real Yield	**4.14%**	**0.43%**	**3.11%**	**0.08%**	**1.17%**	**1.86%**	**-59.81%**
10 Year Real Yield based on inflation expectation	5.33%	2.04%	3.66%	0.79%	1.83%	3.75%	-51.19%
Currency Risk Premium	**4.93%**	**2.66%**	**2.76%**	**12.96%**	**4.11%**	**7.40%**	**6.81%**
Sovereign Risk Premium	**3.78%**	**1.75%**	**1.68%**		**2.02%**	**3.33%**	**8.98%**
US 10 Year Yield	2.82%	3.02%	3.02%	3.02%	3.02%	3.02%	3.02%
S&P Rating - Foreign Currency	**BB-**	**BBB-u**	**BBB**	**NR**	**BBB**	**BB-**	**B+u**
Moody's Rating - Foreign Currency	**Ba2**	**Baa3**	**Baa2**	**NR**	**Baa2**	**Ba2**	**B2**

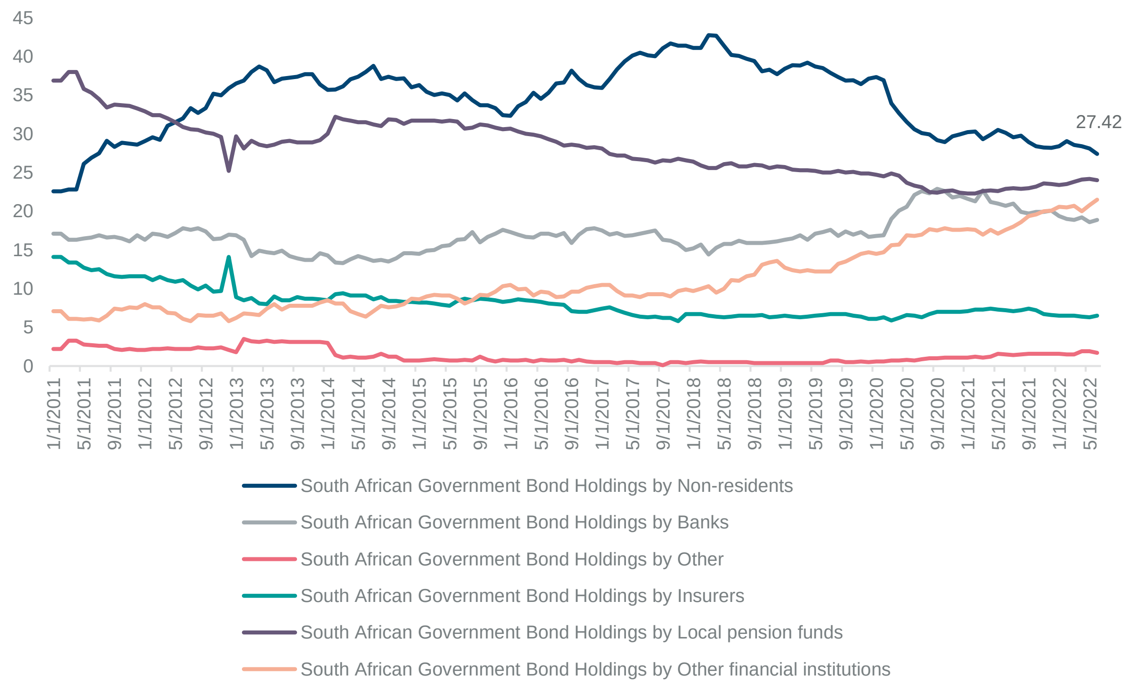
Source: Bloomberg

Figure 10: SA 10-year hedged yield and spread



Source: Bloomberg

Figure 11: SA government bond holdings by non-residents

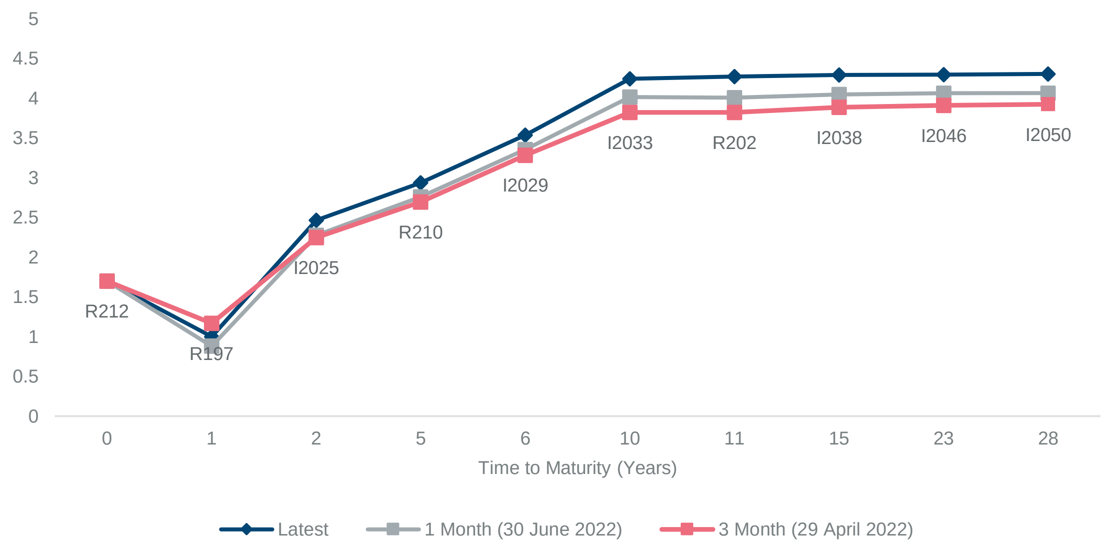


Source: Bloomberg

SA inflation-linked bonds

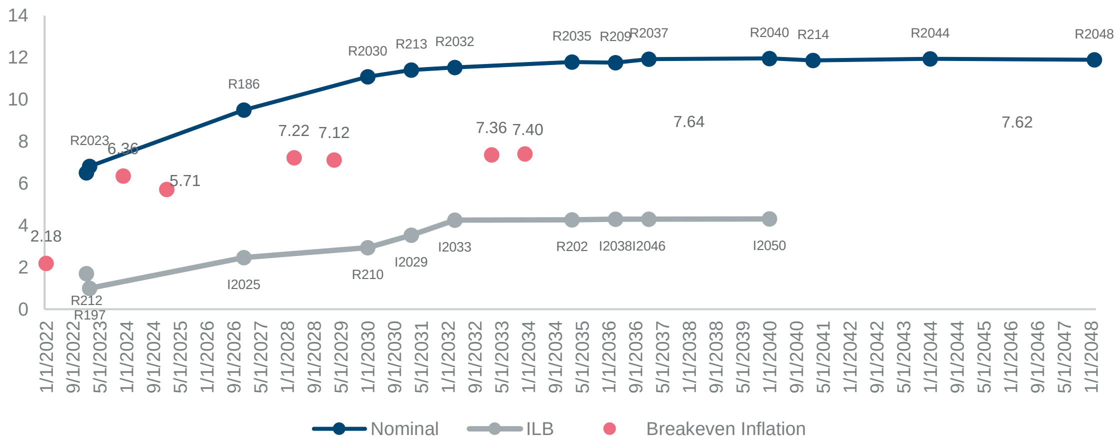
The resurgent level of core inflation indicates that underlying inflationary pressure remains. The real yield curve has steepened slightly over the past few months. However, the level of breakeven inflation suggests that inflation-linked bonds remain on the expensive side, despite the upside risk to inflation in the short term. The real yield of the 10-year inflation-linked bond remained below that of the implied yield, again suggesting the high cost of SA inflation-linked bonds. We chose to maintain our position of moderately underweight in SA inflation-linked bonds as we prefer SA nominal bonds which provide better compensation for inflation.

Figure 12: SA real yield curve as at 20 July 2022



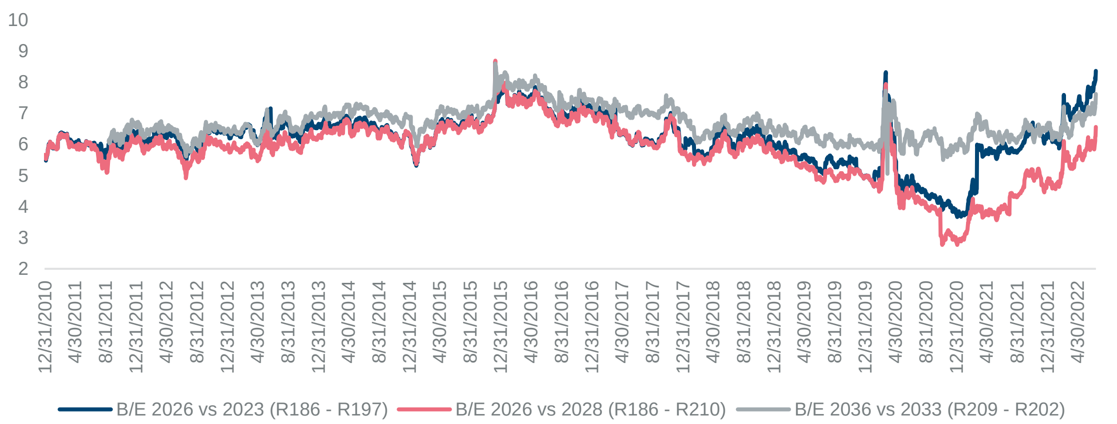
Source: Bloomberg

Figure 13: SA breakeven inflation as at 20 July 2022



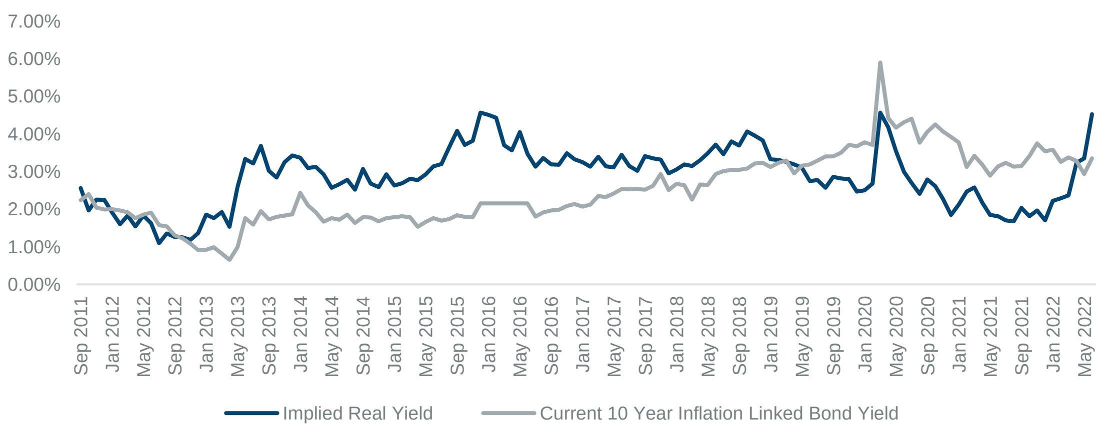
Source: Bloomberg

Figure 14: SA breakeven inflation rates over time



Source: Bloomberg

Figure 15: SA inflation-linked bonds yield and implied yield



Source: Bloomberg

SA-listed property

The yield spreads between the SAPY and the ALSI and the SAPY and the 10-year bond yield suggest a neutral position in this sector from a valuation perspective. If growth concerns are becoming a dominating factor in driving investor sentiment, that is not good for listed properties. Negative rental reversions pressure remains as lease agreements approach their expiry dates. Our investment case for the local property market was largely unchanged. Tapering and rate hikes, which would see tightening financial conditions, and rising discount rates would be negative for real estate due to the leverage inherent in this asset class – thus making it more sensitive to rate hikes than the broad equity class. We therefore chose to remain moderately underweight in listed property.

Figure 16: SAPY yield spread vs ALSI

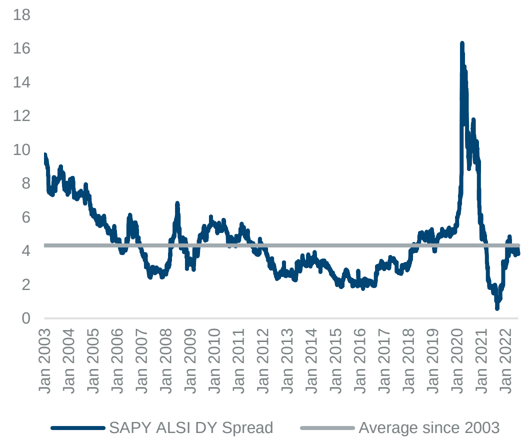
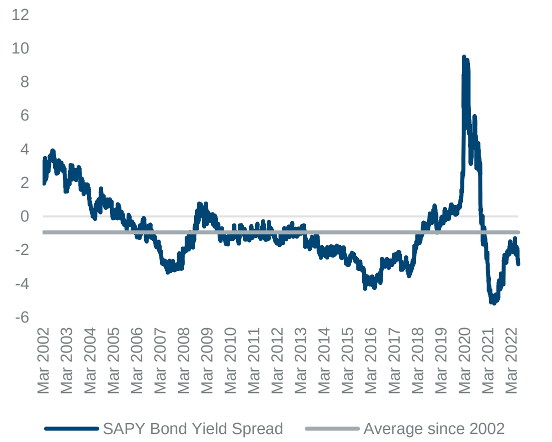


Figure 17: SAPY yield spread vs 10-year bonds



Source: Bloomberg

Offshore equities

Global inflation rates remained red hot and global manufacturing PMIs have continued to cool for most regions. China manufacturing and non-manufacturing PMIs improved from 49.6 and 47.8 in May to 50.2 and 54.7 respectively in June as the country continued to recover from recent months of lockdowns. Yearly import growth in China was weaker than market expectations, but export growth was strong. Furthermore, Chinese retail sales showed a stronger recovery than market expectations in June, up 3.1% year on year vs the market consensus of 0.3%. The impact of China's zero-COVID policy was also reflected in the weaker-than-expected Q2 GDP growth rate.

Figure 18: Global inflation rates

	Dec 2020	Jan 2021	Feb 2021	Mar 2021	Apr 2021	May 2021	Jun 2021	Jul 2021	Aug 2021	Sep 2021	Oct 2021	Nov 2021	Dec 2021	Jan 2022	Feb 2022	Mar 2022	Apr 2022	May 2022	Jun 2022
Global	2.1	2.1	2.2	2.6	3.1	3.6	4.1	4.2	4.2	4.3	4.6	5.2	5.7	6.0	6.4	7.0	8.0	8.8	9.1
Citi Inflation Surprise Index - Global	0.0	5.3	17.7	15.7	21.6	34.8	38.5	40.5	42.8	47.7	43.9	58.1	82.9	70.5	74.0	80.0	80.8	80.1	68.9
Citi Inflation Surprise Index - Major Economies	6.4	10.6	26.6	19.7	25.3	43.4	48.3	55.3	57.5	62.3	58.8	71.9	107.8	97.6	104.7	113.5	107.4	102.2	89.4
Citi Inflation Surprise Index - Emerging Markets	-9.5	-2.6	4.3	9.6	16.1	21.9	23.9	18.2	20.7	25.8	21.6	37.3	45.4	29.9	27.9	29.9	40.8	46.9	38.1
France	0.0	0.6	0.6	1.1	1.2	1.4	1.5	1.2	1.9	2.2	2.6	2.8	2.8	2.9	3.6	4.5	4.8	5.2	5.8
Germany	-0.3	1.0	1.3	1.7	2.0	2.5	2.3	3.8	3.9	4.1	4.5	5.2	5.3	4.9	5.1	7.3	7.4	7.9	7.6
Greece	-2.3	-2.0	-1.3	-1.6	-0.3	0.1	1.0	1.4	1.9	2.2	3.4	4.8	5.1	6.3	7.2	8.9	10.2	11.3	12.1
Ireland	-1.0	-0.2	-0.4	0.0	1.1	1.7	1.6	2.2	2.8	3.7	5.1	5.3	5.5	5.0	5.6	6.7	7.0	7.8	9.1
Italy	-0.2	0.4	0.6	0.8	1.1	1.3	1.3	1.9	2.0	2.5	3.0	3.7	3.9	4.8	5.7	6.5	6.0	6.8	8.0
Spain	-0.5	0.5	0.0	1.3	2.2	2.7	2.7	2.9	3.3	4.0	5.4	5.5	6.5	6.1	7.6	9.8	8.3	8.7	10.2
Sweden	0.5	1.6	1.4	1.7	2.2	1.8	1.3	1.4	2.1	2.5	2.8	3.3	3.9	3.7	4.3	6.0	6.4	7.3	8.7
Switzerland	-0.8	-0.5	-0.5	-0.2	0.3	0.6	0.6	0.7	0.9	0.9	1.2	1.5	1.5	1.6	2.2	2.4	2.5	2.9	3.4
United Kingdom	0.6	0.7	0.4	0.7	1.5	2.1	2.5	2.0	3.2	3.1	4.2	5.1	5.4	5.5	6.2	7.0	9.0	9.1	9.1
United States	1.4	1.4	1.7	2.6	4.2	5.0	5.4	5.4	5.3	5.4	6.2	6.8	7.0	7.5	7.9	8.5	8.3	8.6	9.1
Australia	0.9	0.9	0.9	1.1	1.1	1.1	3.8	3.8	3.8	3.0	3.0	3.0	3.5	3.5	3.5	5.1	5.1	5.1	5.1
Japan	-1.2	-0.7	-0.5	-0.4	-1.1	-0.8	-0.5	-0.3	-0.4	0.2	0.1	0.6	0.8	0.5	0.9	1.2	2.5	2.5	2.5
Brazil	4.5	4.6	5.2	6.1	6.8	8.1	8.4	9.0	9.7	10.3	10.7	10.7	10.1	10.4	10.5	11.3	12.1	11.7	11.9
China	0.2	-0.3	-0.2	0.4	0.9	1.3	1.1	1.0	0.8	0.7	1.5	2.3	1.5	0.9	0.9	1.5	2.1	2.1	2.5
India	4.6	4.1	5.0	5.5	4.2	6.3	6.3	5.6	5.3	4.4	4.5	4.9	5.7	6.0	6.1	7.0	7.8	7.0	7.0
Indonesia	1.7	1.6	1.4	1.4	1.4	1.7	1.3	1.5	1.6	1.6	1.7	1.8	1.9	2.2	2.1	2.6	3.5	3.6	4.4
Mexico	3.2	3.5	3.8	4.7	6.1	5.9	5.9	5.8	5.6	6.0	6.2	7.4	7.4	7.1	7.3	7.5	7.7	7.7	8.0
Russia	4.9	5.2	5.7	5.8	5.5	6.0	6.5	6.5	6.7	7.4	8.1	8.4	8.4	8.7	9.2	16.7	17.8	17.1	15.9
South Africa	3.1	3.2	2.9	3.2	4.4	5.2	4.9	4.6	4.9	5.0	5.0	5.5	5.9	5.7	5.7	5.9	5.9	6.5	6.5
South Korea	0.6	0.9	1.4	1.9	2.5	2.6	2.4	2.6	2.6	2.4	3.2	3.8	3.7	3.6	3.7	4.1	4.8	5.4	6.0
Taiwan	0.1	-0.2	1.4	1.2	2.1	2.5	1.8	1.9	2.3	2.6	2.6	2.9	2.6	2.8	2.3	3.3	3.4	3.4	3.6

Source: Bloomberg

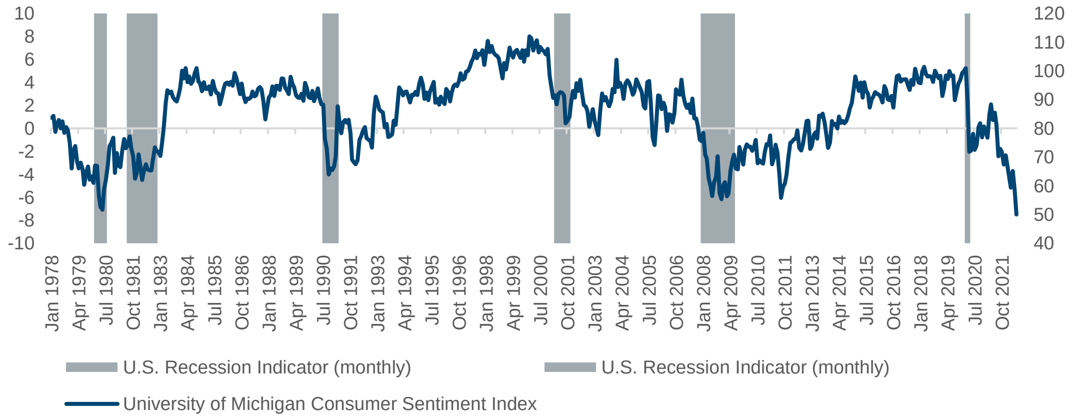
Figure 19: The Global Manufacturing PMI

	Dec 2020	Jan 2021	Feb 2021	Mar 2021	Apr 2021	May 2021	Jun 2021	Jul 2021	Aug 2021	Sep 2021	Oct 2021	Nov 2021	Dec 2021	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22
Global Manufacturing PMI	53.8	53.6	54	55	55.8	56	55.5	55.4	54.1	54.1	54.3	54.2	54.2	53.2	53.6	53	52.2	52.3	52.2
Developed Markets	54.8	55.2	56.5	58.5	59.3	59.8	59.5	59.8	58.3	57.1	56.6	56.9	56.6	56.3	56.6	56.5	56.3	55	52.5
Emerging Markets	52.8	52.1	51.5	51.3	52.2	52	51.2	50.6	49.6	50.8	51.6	51.2	51.7	50	50.9	49.2	48.1	49.5	51.7
Eurozone	55.2	54.8	57.9	62.5	62.9	63.1	63.4	62.8	61.4	58.6	58.3	58.4	58	58.7	58.2	56.5	55.5	54.6	52.1
France	51.1	51.6	56.1	59.3	58.9	59.4	59	58	57.5	55	53.6	55.9	55.6	55.5	57.2	54.7	55.7	54.6	51.4
Germany	58.3	57.1	60.7	66.6	66.2	64.4	65.1	65.9	62.6	58.4	57.8	57.4	57.4	59.8	58.4	56.9	54.6	54.8	52
Italy	52.8	55.1	56.9	59.8	60.7	62.3	62.2	60.3	60.9	59.7	61.1	62.8	62	58.3	58.3	55.8	54.5	51.9	50.9
Spain	51	49.3	52.9	56.9	57.7	59.4	60.4	59	59.5	58.1	57.4	57.1	56.2	56.2	56.9	54.2	53.3	53.8	52.6
Greece	46.9	50	49.4	51.8	54.4	58	58.6	57.4	59.3	58.4	58.9	58.8	59	57.9	57.8	54.6	54.8	53.8	51.1
Ireland	57.2	51.8	52	57.1	60.8	64.1	64	63.3	62.8	60.3	62.1	59.9	58.3	59.4	57.8	59.4	59.1	56.4	53.1
Australia	55.7	57.2	56.9	56.8	59.7	60.4	58.6	56.9	52	56.8	58.2	59.2	57.7	55.1	57	57.7	58.8	55.7	56.2
Sweden	64.8	62.6	61.7	64.1	68.7	66.1	65.4	64.5	60.1	64.6	64.4	63.1	62.1	62.4	58.6	57.3	55	54.9	53.7
Denmark	41.6	42.8	46.1	65.6	66.6	65.5	65.5	69.7	67.3	65.2	71.9	68.1	64.4	60.9	50.7	62.1	63	61.2	71.3
UK	57.5	54.1	55.1	58.9	60.9	65.6	63.9	60.4	60.3	57.1	57.8	58.1	57.9	57.3	58	55.2	55.8	54.6	52.8
US	57.1	59.2	58.6	59.1	60.5	62.1	62.1	63.4	61.1	60.7	58.4	58.3	57.7	55.5	57.3	58.8	59.2	57	52.7
Japan	50	49.8	51.4	52.7	53.6	53	52.4	53	52.7	51.5	53.2	54.5	54.3	55.4	52.7	54.1	53.5	53.3	52.7
China	53	51.5	50.9	50.6	51.9	52	51.3	50.3	49.2	50	50.6	49.9	50.9	49.1	50.4	48.1	46	48.1	51.7
Indonesia	51.3	52.2	50.9	53.2	54.6	55.3	53.5	40.1	43.7	52.2	57.2	53.9	53.5	53.7	51.2	51.3	51.9	50.8	50.2
South Korea	52.9	53.2	55.3	55.3	54.6	53.7	53.9	53	51.2	52.4	50.2	50.9	51.9	52.8	53.8	51.2	52.1	51.8	51.3
Taiwan	59.4	60.2	60.4	60.8	62.4	62	57.6	59.7	58.5	54.7	55.2	54.9	55.5	55.1	54.3	54.1	51.7	50	49.8
India	56.4	57.7	57.5	55.4	55.5	50.8	48.1	55.3	52.3	53.7	55.9	57.6	55.5	54	54.9	54	54.7	54.6	53.9
Brazil	61.5	56.5	58.4	52.8	52.3	53.7	56.4	56.7	53.6	54.4	51.7	49.8	49.8	47.8	49.6	52.3	51.8	54.2	54.1
Mexico	42.4	43	44.2	45.6	48.4	47.6	48.8	49.6	47.1	48.6	49.3	49.4	49.4	46.1	48	49.2	49.3	50.6	52.2
Russia	49.7	50.9	51.5	51.1	50.4	51.9	49.2	47.5	46.5	49.8	51.6	51.7	51.6	51.8	48.6	44.1	48.2	50.8	50.9
South Africa	50.3	50.9	53	57.4	56.2	57.8	57.4	43.5	57.9	56.8	53.6	57.2	54.1	57.1	58.6	60	50.7	54.8	52.2

Source: Bloomberg

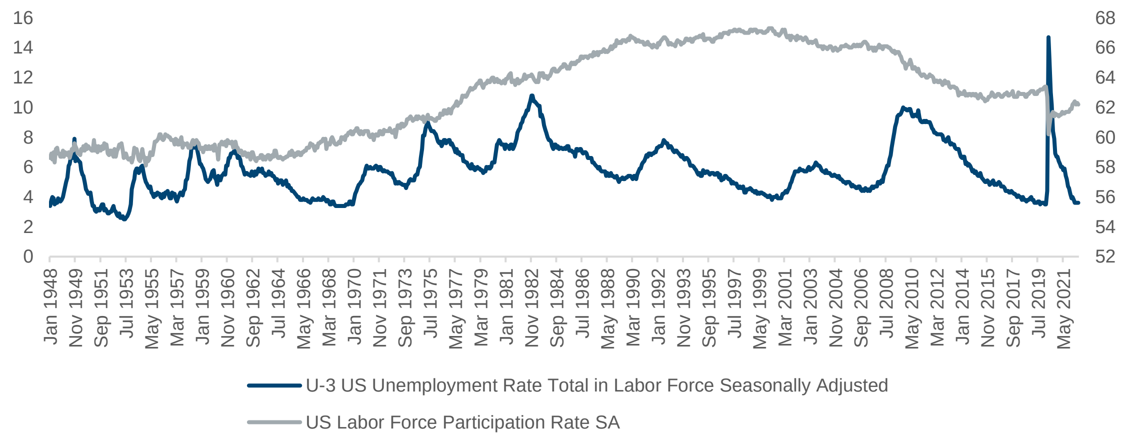
The University of Michigan sentiment remains depressed, plunging from 58.4 in May to 50.2 in June, with a preliminary reading for July of 51.1. The Conference board of consumer confidence displayed a similar trend, weakening from 106.4 in May to 98.7 in June. The labour market remains tight, with the US unemployment rate remaining unchanged at 3.6% while the non-farm payrolls in June also exceeded market expectations. The housing market continued to cool amid rising rates but in an orderly fashion as there is much less supply, more Americans today are on long-term fixed-rate mortgages and there is less sub-prime lending than in 2007. Buying conditions continued to be unfavourable and the US Business Leaders Survey shows that price and wage expectations have stabilised, albeit still elevated. Inflation expectations for the next five years and six to 10 years based on inflation swaps indicate that the levels have fallen significantly from the peak in March. However, they are still significantly above the pre-COVID level.

Figure 20: The University of Michigan Consumer Sentiment Index



Source: Bloomberg

Figure 21: Unemployment rate and participation rate in the US



Source: Bloomberg

Figure 22: University of Michigan Buying Conditions indices

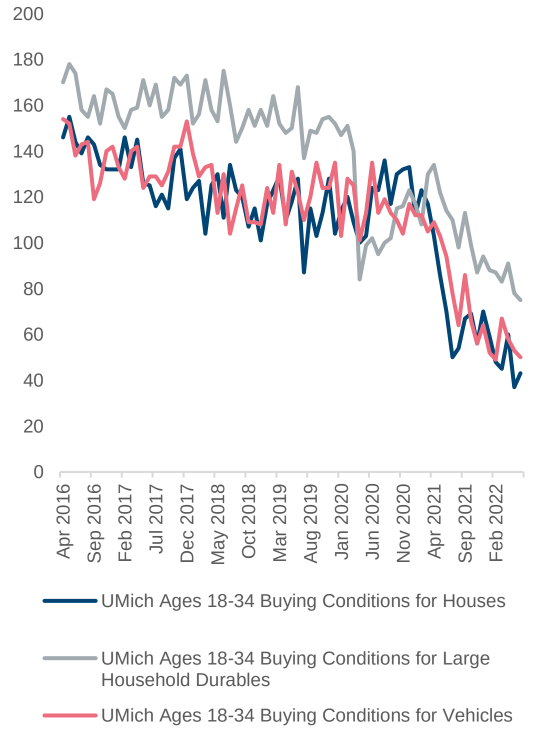
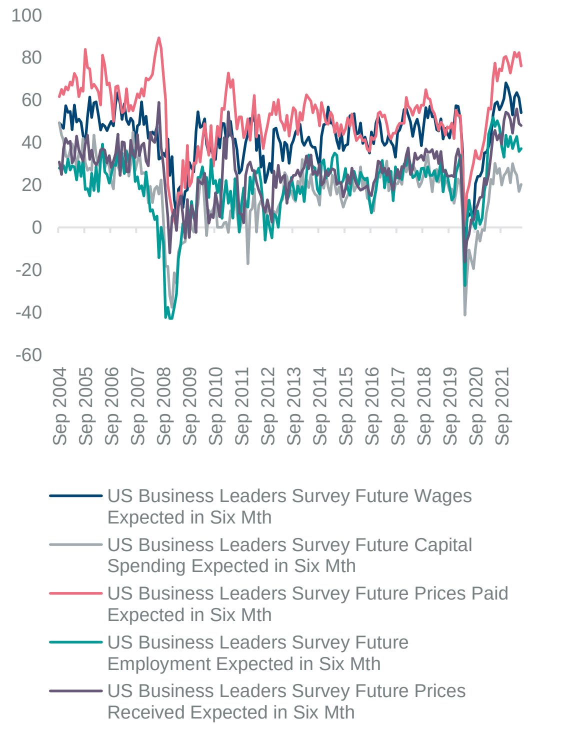


Figure 23: US Business Leaders Survey future conditions



Source: Bloomberg

Most central banks are showing a determination to get inflation under control and markets have priced in more aggressive rate hikes in the short term, as reflected in the FRA rates. We still believe that despite tanking sentiment in the US, the US will nevertheless be in a less vulnerable position, being the largest food exporter globally and having less of an energy burden, while the Eurozone faces no peripheral debt issues on top of the more direct impact of geopolitical tensions.

Figure 24: US FRA rates

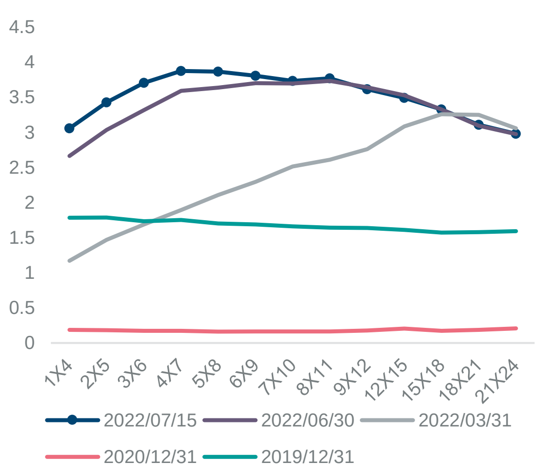
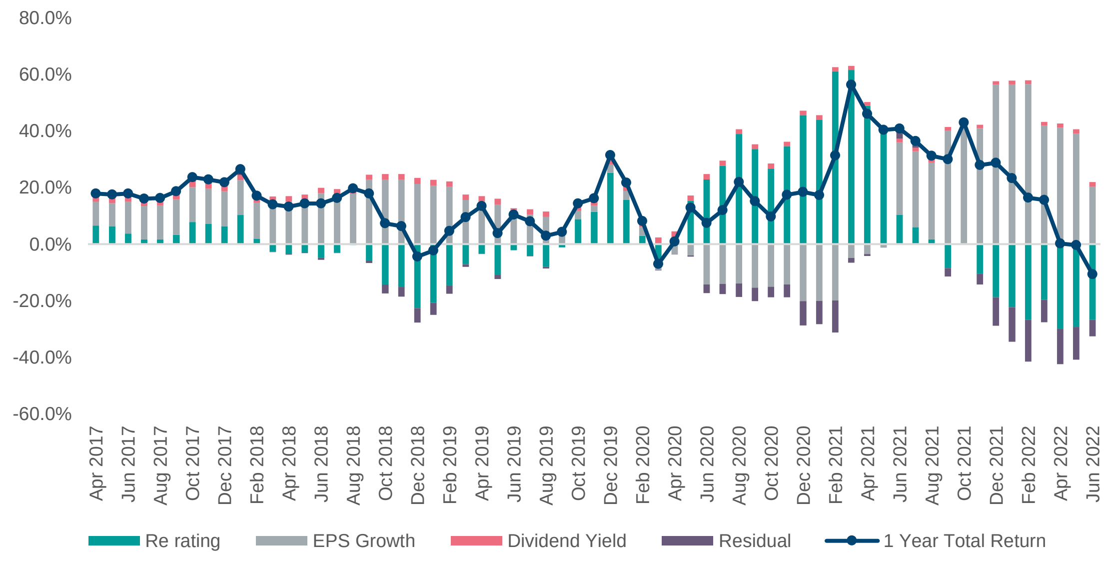


Figure 25: EU FRA rates

Source: Bloomberg

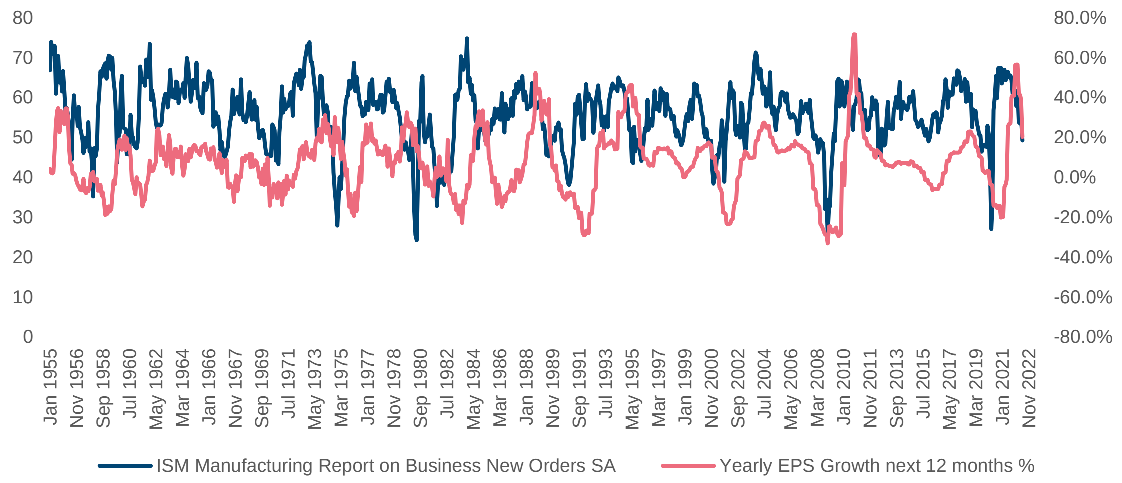
We choose to remain neutral in offshore equities on the balance of improving valuations, the deteriorating global growth outlook and the elevated risk of central banks overtightening their monetary policies to tame inflation. Equities have corrected quite sharply for the year to date, with valuations being more attractive, especially for European and Japanese equities. However, from the return decomposition of the S&P 500 Index, we have observed a slowdown in earnings growth. While re-rating has played a material role in valuations amid rising rates, there is still a potential downside should earnings momentum weaken further. The correlation between the forward 12-month earnings per share growth and the ISM Manufacturing Business New Orders Index is 0.6. Based on where we are for the New Orders Index, a rather bearish picture is painted for US equities for the next 12 months.

Figure 26: S&P 500 return decomposition



Source: Bloomberg

Figure 27: S&P 500 earnings per share vs ISM Manufacturing report on business new orders

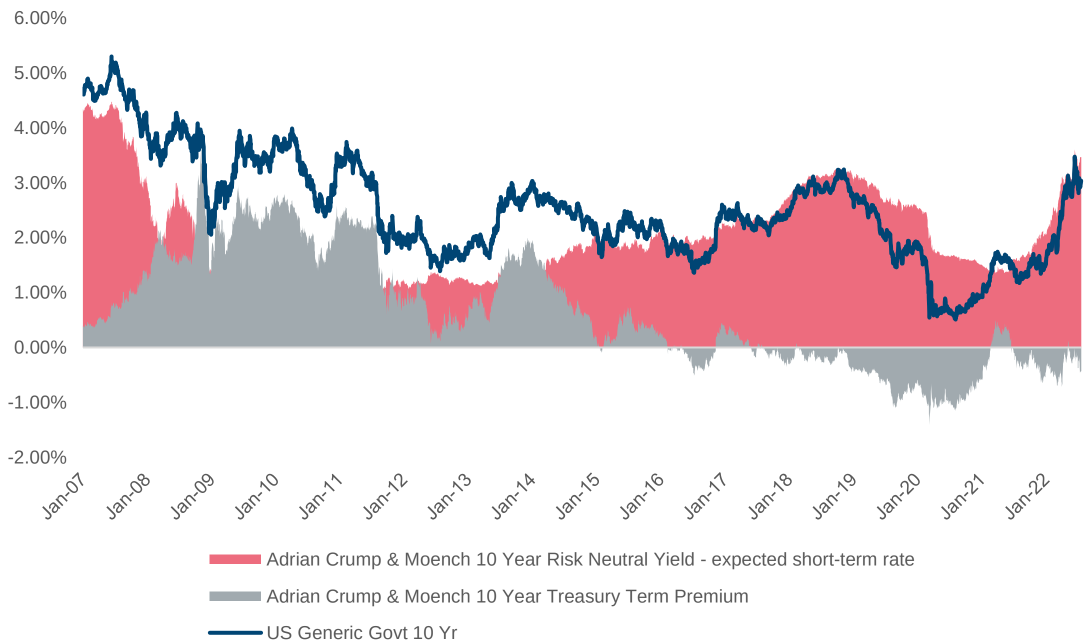


Source: Bloomberg

Offshore bonds

We choose to remain neutral in offshore bonds. The US 10-year bond yield disaggregation indicates that most of the surge in yields was driven by higher-than-expected short-term rates. Meanwhile, yields have surged and may move higher as investors demand a higher-term premium for holding longer maturity bonds. Given the weakening growth outlook, we therefore choose to be neutral in offshore bonds so that the portfolio is balanced to growth and inflation.

Figure 28: US 10-year bond yield disaggregation

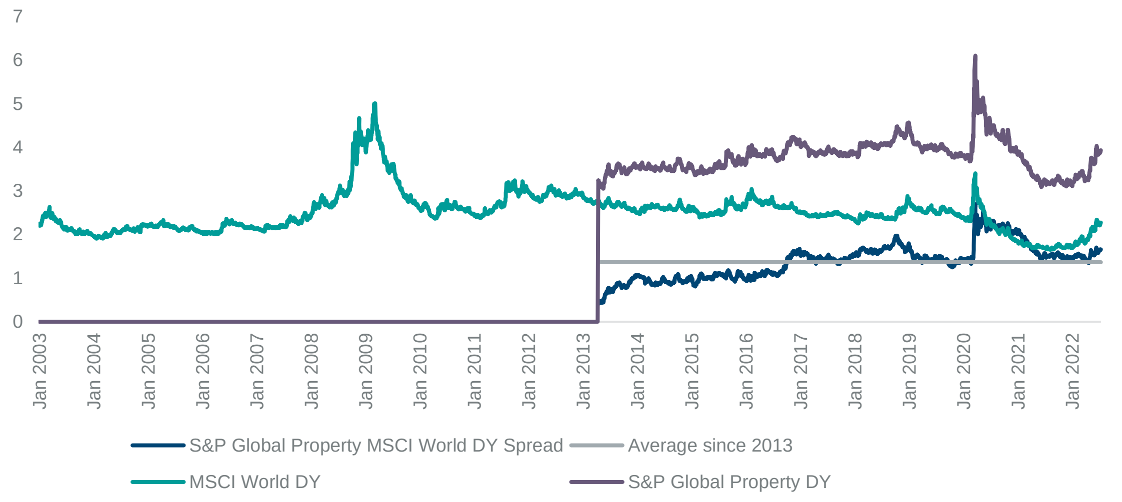


Source: Bloomberg

Offshore property

The valuation of global property remains neutral from a dividend yield spread perspective and expensive vs the 10-year Treasury bonds. This sector remains more sensitive to rate hikes than equities in general, despite the sector's inflation-hedging properties. We therefore choose to remain moderately underweight.

Figure 29: S&P Global Property dividend yield spread relative to the MSCI World dividend yield



Source: Bloomberg

Figure 30: S&P Global Property dividend yield spread relative to the US 10-year treasury yield

Source: Bloomberg

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