Tactical asset allocation views

A one- to three-year view of markets

As of 31 October 2020

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Please read the investment risks on p3.

Here are the Henley Multi Asset team's fundamental tactical asset allocation views over a 1-3 year investment horizon. Powered by their proprietary VOTES asset allocation framework – which ranks markets on Valuation, Other (e.g. Policy) Technical, Earnings/ Economics and Selection (e.g. alpha) drivers – these fundamental preferences are reflected in the team's long-only portfolios.

To find out more about the Henley Multi Asset team's Summit Growth range of funds, visit **www.invesco.co.uk/summit**

		Overweight		Neutral	Underweight	
		A	B	C	D	E
Equities	**Overall**		●			
	UK equities		●			
	US equities		●			
	Europe ex UK equities			●		
	Japan equities		● ←	●*		
	Pacific ex Japan equities[1]			●		
	Emerging markets equities			●		
Fixed Income	**Overall**				●	
	Government bonds				●	
	Investment grade credit		*● →	●		
	High yield bonds		●			
	Emerging market debt		●			
	Absolute return bonds			●		
Alternatives	**Overall**			●		
	Real estate (REITS)			● ←	●*	
	Global macro strategies			●		
	Absolute return strategies		●			
Cash	**Overall**				●	

Source: Invesco, as at 31 October 2020. [1] Developed Asia. * Indicates an upgrade or downgrade.

Equities

Overall — B: Overweight ●

Absolute valuations are not cheap on a standalone basis, but in this investment climate we think relative valuations are more important. Equity valuations remain attractive relative to fixed interest and cash given the risk-free rate is likely to stay close to zero for some time. As we have mentioned before, the likelihood of a disrupted economic recovery means that we would not be surprised to see bouts of equity market volatility in the short-term. Policy support will be very important in sustaining the recovery and supportive of equity markets on a three-year view.

UK equities — B: Overweight ●

Valuations versus history and other major equity markets remain attractive, though the sector mix has been unhelpful in terms of driving outperformance. The domestic political landscape is stable, but post-Brexit trade deal issues remain a concern. A combination of attractive valuations, aggressive policy measures, and the potential for foreign investor flows (once a Brexit deal has been finalised) could be supportive of UK equities in the medium-term.

US equities — B: Overweight ●

US equities have continued to outperform their developed market counterparts and look expensive, both in terms of absolute valuations and relative to other equity markets. Market leadership, though narrow, has started to broaden a little as investors start to anticipate a less disrupted economy. The outcome of the Presidential election could create some short-term uncertainty, but given the stated policies of both candidates, a decisive outcome (either way) may be less significant for the overall market than it is for potential rotation between sectors within the market, over our tactical timeframe.

Europe ex UK equities — C: Neutral ●

Valuations look neutral at best overall suggesting sustained outperformance relative to the broader global equity market will remain difficult. The earnings picture is relatively weak in the context of some other equity markets, and dividends in the region remain at risk. Co-ordinated policy support is modestly helpful, but its potential to meaningfully support European equity markets is arguably limited.

Equities (cont.)

Japan equities — B: Overweight
upgrade from C

Foreign (net) flows have turned positive in recent weeks, after more than 5 years of net outflows. There is once again stability in the political sphere with new PM Suga committing to Abenomics. Corporate action and shareholder activism on governance provides a helpful backdrop. Equity market valuations are attractive in a global context and the policy framework remains helpful with the Bank of Japan being an active buyer and owner of Japanese equities. Japanese balance sheets are strong which should provide support for dividends. Upgrade from Neutral (C) to Overweight (B).

Pacific ex Japan equities (Developed Asia) — C: Neutral

Valuations are not notably cheap, and the earnings recovery has seemingly lagged some other developed markets thus far. However, the coherent and seemingly effective response to the coronavirus pandemic bodes well for a less disruptive economic recovery going forward.

Emerging markets equities — C: Neutral

Performance in emerging equity markets has been divergent, with Latin American and emerging European markets deep into negative territory for the year. Conversely, emerging Asian markets have been stronger with new-economy China (in particular) relatively resilient throughout the equity market volatility this year and many economies in the region ahead of the Covid curve aiding the earnings and equity markets across the region. Within emerging markets we continue to see some areas as higher risk – such as India and parts of Latin America – which we think are more likely to experience a more disruptive recovery and potential political instability.

Fixed Income

Overall — D: Underweight

Fixed income remains unattractive at the asset class level with a significant proportion of the fixed income market offering limited value given ultra-low rates. However, spreads on high yield corporate bonds offer good relative value, despite a potential pick-up in the likely corporate default rate in the coming years.

Government bonds — D: Underweight

Unless yields move through zero and decisively negative, value in government bonds is currently very limited. We believe policy makers will keep yields anchored at low levels with quantitative easing measures for some time to come while economies endure a difficult recovery. Yield curves have flattened, which means limited roll-down opportunities, but the risk is a steepening (and hence capital losses) as economies start to slowly normalise. While government bonds are an important defensive asset in a multi-asset portfolio, they are potentially less so than they traditionally have been, at current yields.

Investment grade credit — (C: Neutral)
downgrade from B

At current levels, investment grade spreads offer reasonable risk/reward opportunities given that the quantitative easing policy framework ('buy at any price') provides strong structural support for the asset class. However, we feel that the market is somewhat complacent now as increased debt issuance and tighter spreads mean the total return outlook is limited. Downgrade from Overweight (B) to Neutral (C).

High yield bonds — B: Overweight

Absolute yields remain high offering attractive rewards for those prepared to take risk. While opportunities exist in both the US and Europe, we prefer the US high yield market because US corporates are potentially better placed to benefit from the likely recovery in profits that is now starting to emerge. The US policy framework is also more supportive in that it includes potentially unlimited central bank purchases of US high yield ETFs, albeit this has yet to be undertaken in a meaningful way.

Emerging market debt — B: Overweight

Yields are high in a global context (and hence attractive) and we think there are rewards for those prepared to take risk. We are mindful that leverage continues to rise at the country level in emerging markets, that the political backdrop is generally less stable, and that supply is elevated. However, aggressive central bank rate cuts and QE has provided a supportive environment for domestic and international investors.

Absolute return bonds — C: Neutral

With a significant proportion of the fixed income markets offering low or even negative value, the opportunity set for absolute bond strategies is currently smaller. However, such strategies can take advantage of opportunities in those select areas of the market that offer better value.

Alternatives

Overall — C: Neutral

Depending on the nature of the strategy, alternatives can help to dampen volatility and provide less correlated sources of return. We have a neutral view on the broad asset class. Our concerns over the outlook for real estate are tempering with valuations becoming more supportive and we have a positive view of absolute return strategies given traditional market valuations.

Real estate — C: Neutral

upgrade from D

The global real estate market continues be unloved, with property rents under pressure and the outlook for the sector uncertain as corporates look to move away from 'bricks and mortar' business models. Policy support that is generally supportive for other asset classes remains less so for the real estate sector. However, valuations now appear more supportive, with significant discounts to net asset values to be found. Upgrade from Underweight (D) to Neutral (C).

Global macro strategies — C: Neutral

Economic uncertainty and valuation disparity between asset classes and markets are positives for global macro strategies. However, such strategies are varied in approach and less full valuations in some parts of the more traditional markets dampens relative attractiveness.

Absolute return strategies — B: Overweight

In periods of increased market volatility, absolute return strategies can exploit valuation dislocations and provide potentially defensive properties for portfolios. In a potentially low return environment for government bonds and cash, these strategies provide a return potential that is lowly correlated to traditional asset classes.

Cash

Cash — D: Underweight

Cash rates are close to zero and in some cases negative. While cash offers the ultimate capital protection in another economic downturn, we prefer to obtain defensive exposure elsewhere.

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