I DROVE ALL NIGHT Roy Orbison, 1992

The last few weeks have seen central banks continue to ease their policy stances in response to tepid global growth and the absence of inflationary pressures. The ECB cut its deposit rate by 0.10% and relaunched their asset purchase programme for "as long as necessary," while the Fed cut its target rate by 0.25% and indicated that another cut could follow by the end of the year if necessary. The actions were largely in line with investor expectations and the market reaction was relatively muted. With these two key events in the rear-view mirror, can we dream of a long, straight road ahead? Or will investors catch a fever, burning up inside?

WHAT'S NEXT?

Macro: Central Bank Support Continues

We have communicated for some time our concerns about the Eurozone, with both peripheral countries such as Italy and core countries like Germany approaching recessionary levels. With inflation pressures low, the ECB needed to deliver an aggressive stimulus package in order to kick-start the economy. In some key ways, it did deliver: in addition to the 10bps cut to the deposit rate and a resumption of quantitative easing, its extension of LTRO maturities and the introduction of a two-tier system for reserves should ensure that credit conditions in Europe remain easy.

The ECB's forward guidance to help the economy "as long as necessary" is a strong commitment from the central bank that monetary policy will remain supportive for some time. This will be important as credit showed signs of tightening broadly according to the Q2 2019 ECB Bank Lending survey (BLS), primarily driven by concerns around the economic outlook and banks' increased risk aversion. At the same time, the BLS survey pointed to increased demand for credit, from both businesses and households (home purchases as well as consumer credit). The pickup in credit demand was mainly due to the low level of interest rates and spending (on fixed investment for businesses and on durable goods for consumers). This improved credit demand picture needs to be sustained if the ECB wants to avoid 'pushing on a string' with its monetary policies.

The Fed faces a different set of challenges: the US economy continues to grow at a decent rate, though at a slower pace than it did in early 2019. However, the uncertainty introduced by trade tensions and the broader global growth slowdown have skewed the risks to the downside. Continuing its policy stance of a mid-cycle adjustment, the Fed cut their target rate by 25bps and their median projection calls for one more cut this year, though that will surely depend on how the economy evolves over the next few months.

Importantly, the inflation forecasts were unchanged while growth was revised higher for 2019 (2.2% from 2.1%) and 2021 (1.9% from 1.8%). Clearly, the Fed acknowledges that growth momentum persists, leading to wide dispersion on the need for further cuts according to the so-called "dot plot." At this point, the Fed would likely need to see a significant worsening of the US economy to cut rates further. Indeed, both for the Fed and the ECB, there is less consensus among their members, which effectively raises the bar for further easing going forward.

Sentiment: Investors Seem to Continue Their Defensive Stance

Despite a decent macro picture – global growth remains around potential, inflation is nowhere to be seen, and central banks are providing support – investors still appear to be maintaining a fairly cautious view on risky assets. Although no one indicator would be enough on its own, the confluence of multiple perspectives on a cross-asset basis points to the market's defensive stance:

- Government bonds remain the most expensive risk premia based on their historical and cross-sectional carry, despite very low or even negative yields;
- Safe-haven currencies, like the Japanese yen and Swiss franc, remain overvalued;
- Positioning in gold, whether in ETFs or futures contracts, remains elevated on a historical basis and has not been meaningfully reduced despite the run up in the gold price;
- The implied equity beta of macro hedge funds and CTAs has moved from strongly positive two months ago to now negative, suggesting these investors have moved net short equities; and
- The short-term downside skew for equity options remains elevated, with the S&P 500 index seeing levels at around the 80th percentile historically and the Euro Stoxx 50 index at the 90th percentile.

In our view, such defensive positioning would be reasonable today if recession risk was high or there was a significant escalation in the trade war. The former seems unlikely, at least at the global level. And while the latter is a risk that will likely be with us for some time, recent developments have been neutral. This motivates our view that the risks from sentiment are tilted to the upside for growth assets, as investor defensiveness seems overdone. Indeed, we communicated in early September that hedging assets, such as bonds, looked overbought on the back of considerable optimism about central bank easing. The first half of this month has seen that optimism wane. We believe the pain trade remains to the upside for growth assets.

Valuation: Few Opportunities But Clear Risks

Based on carry, most assets are expensive from a historical perspective. However, corporate credit (both investment grade and high yield) stands out as inexpensive from a cross-sectional basis, partly motivating our overweight in credit. And despite rising yields on government bonds, they still remain expensive and a clear valuation risk. Interestingly, equities are roughly neutral, both from a cross-asset carry perspective and traditional equity-specific valuation metrics such as price-to-earnings or price-to-book, especially in emerging markets. Thus, valuations are reinforcing our pro-growth assessment.

Asset Allocation: Risk-on, But Looking to Remain Vigilant

For now, hedging assets seem the most vulnerable to the combination of resilience in economic growth, extreme positioning and tense valuations. We have therefore reduced substantially our exposure to these assets and reallocated to growth-oriented ones, especially credit. Gaining downside protection via options is costly given investor defensiveness and we are instead looking for cost-efficient structures with attractive payoff profiles.

Listen to: I Drove All Night

STRATEGY BEHAVIOUR

Our medium-term view is currently more constructive, as we are still overweight growth assets and underweight real assets. We are also complementing our exposures with options to protect the portfolio in the case of equity drawdowns.

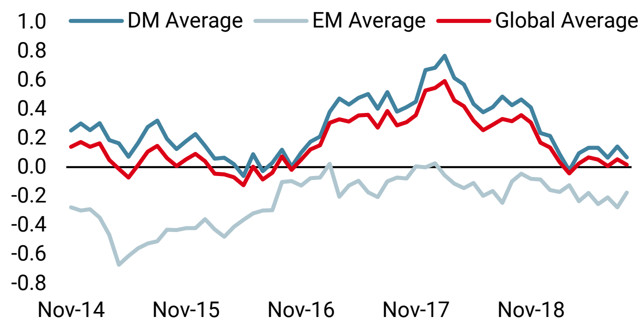
PERFORMANCE REVIEW

Over September to date, the Multi Asset Risk Targeted Strategy is up 1.0% versus 3.0% for the MSCI AC World Index, while the Barclays Global Aggregate (USD hedged) is down 0.9%. Year-to-date, the Multi Asset Risk Targeted Strategy has returned 10.3% versus 17.2% for the MSCI AC World index and 8.3% for the Barclays Global Aggregate (USD hedged) index.

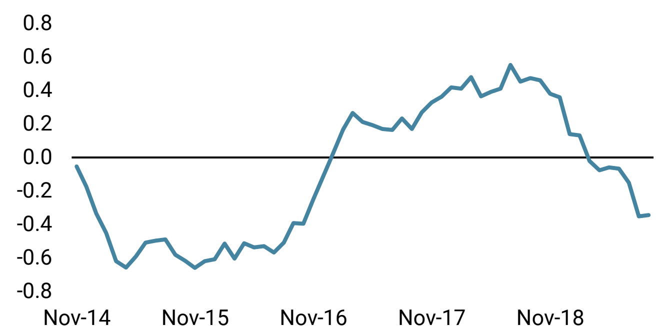
* The Multi Asset Risk Targeted Strategy performance is shown in USD net of fees for the representative account of the Multi Asset Risk Targeted (Medium) USD Composite and reflects the deduction of advisory fees and brokerage commission and the reinvestment of all dividends and earnings. Past performance is not indicative of future performance. This information is presented as supplemental information only and complements the GIPS compliant presentation provided on the following page.

UNIGESTION NOWCASTING

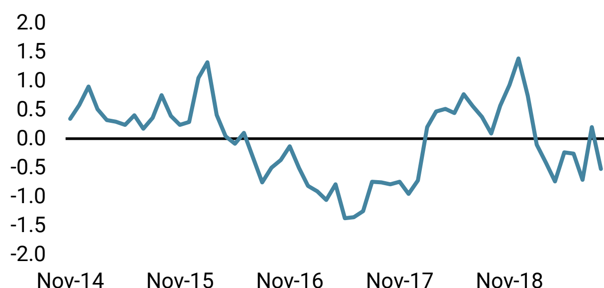
World Growth Nowcaster



World Inflation Nowcaster



Market Stress Nowcaster



Weekly Change

- Our world Growth Nowcaster remains unchanged, pointing to world growth around potential.
- Our world Inflation Nowcaster continued to stabilise last week, after a long period of decline.
- Market stress increased marginally last week as credit spreads widened slightly.

Sources: Unigestion. Bloomberg, as of 23 September 2019.

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Unigestion Multi Asset Risk-Targeted (USD): 31 December 2014 to 30 June 2019

Year	Composite Return Gross of Fees	Composite Net Return	Benchmark Return	Number of Accounts	Internal Dispersion	Composite 3-Yr Std Dev	Benchmark 3-Yr Std Dev	Composite AUM (M)	Firm AUM (M)
2015	-1.61%	-2.80%	–	1	–	–	–	127.24	15,550.31
2016	5.05%	3.79%	–	1	–	–	–	129.66	18,144.46
2017	11.16%	9.82%	–	1	–	–	–	169.51	22,340.80
2018	-2.91%	-4.08%	–	1	–	–	–	286.93	21,403.49
2019[1]	7.45%	6.80%	–	1	–	–	–	364.46	21,692.55

1: This year is incomplete, it stops in June.

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