Multi-Asset Strategy

Monthly Asset Class Convictions and Risk Positioning

May
2019

Green Shoots With Deep Roots

The trajectory of fundamentals continues to surprise on the upside. Unlike others, we have been calling for global growth to reaccelerate after wobbling into the spring as a result of China's economic problems, the Fed's uncertain direction, and President Trump's trade policies. Those restraints are indeed reversing, so we maintain our constructive Risk Dial Score (RDS) of 2.3.

Against a backdrop of improving global fundamentals and accommodative financial conditions, President Trump has reintroduced uncertainty by threatening a re-escalation of trade frictions, reportedly in response to China's extensive redactions to the initial markup of a trade deal. While productivity-driven disinflation is prolonging the cycle, sustaining it will require an investment uptick, which awaits a calmer environment on the trade front. We continue to believe that a path will be found toward de-escalation.

Consensus is still focused on a slowdown to a "2% trend" in the US, predicated on the idea that 2018 saw a fiscally driven "sugar high" that elevated growth almost 1% above trend. Since only the spent portion of a tax cut actually elevates GDP, the three-quarters of the stimulus that was not spent went to improve corporate balance sheets or bolster individual savings. In our view, since there was no sugar high, there will be no letdown. Others presuming a slowdown to the 2% trend define the trend as 1% labor force growth plus 1% productivity growth. Yet the behavior of each of those components defies the naysayers. Productivity has been rising for three years with the latest read at 2.4%, while payroll growth has been 1.7% for a decade and in the last 12 months continued that pace at 1.8%.

Two data points stand out this month: the impressive 2.4% gain in productivity and a spike in new household formations. Both had been depressed well below prior norms during the post-crisis period. Like private sector deleveraging and fiscal austerity, which had acted as economic wet blankets before reversing, the turnaround in these latest economic indicators points the way to an economy whose outlook is less slow and more durable.

Over our Capital Market Line horizon, another factor that might continue to frustrate proponents of secular stagnation is demographics. In a new study, Morgan Stanley points out that after two decades of decelerating labor force growth due to retiring baby boomers, members of Gen Y and Gen Z are now flooding into the workforce. Even allowing for their more muted consumption patterns, trend consumption is set to accelerate. Personal consumption growth peaked in the late 1990s at 4%, fell to 1.7% at present, and, according to this demographic study, will now rise to 2.5% in five years. The US stands alone in this respect, with most other nations still facing shrinking workforces.

Finally, China's slowdown is already showing green shoots, with growth set to cyclically inflect higher for the remainder of 2019. Growth in 2020 and beyond depends on China's success in rejuvenating its private sector, which is less leveraged and more productive than its state-owned enterprises. Thus, it could surprise in its sustainability.

About This Report

Each month, we meet to evaluate our overall risk positioning and asset class convictions over a nine- to 18-month horizon. In this report, we take a broad look at the markets and our risk posture. Then, we drill down to discuss the latest developments affecting our positioning within asset classes and provide a snapshot of our convictions across regions and markets.

Our Risk Dial Score (RDS)

The RDS is based on the Capital Market Line's slope and asset-class dispersion in conjunction with the direction of fundamentals over nine to 18 months.

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Market Developments

Here, we summarize the trends and developments that could have an impact on our positioning.

Equities

Brazilian chances for pension reform are evolving in a positive manner. While its recovery is weak by historical standards, Brazil remains one of the very few countries in an early growth stage, which would be fortified with this reform. We think it is an attractive candidate for adding exposure, as are US cyclical stocks, which have participated in the year-to-date rally but whose valuations continue to reflect disbelief regarding growth prospects into 2020.

Fixed Income

The recent rally in US Treasuries takes them deeper into unattractive territory. We maintain our stance for very short duration, expecting yields to rise on further signs of growth recovery in the global manufacturing sector and a de-escalation of trade issues.

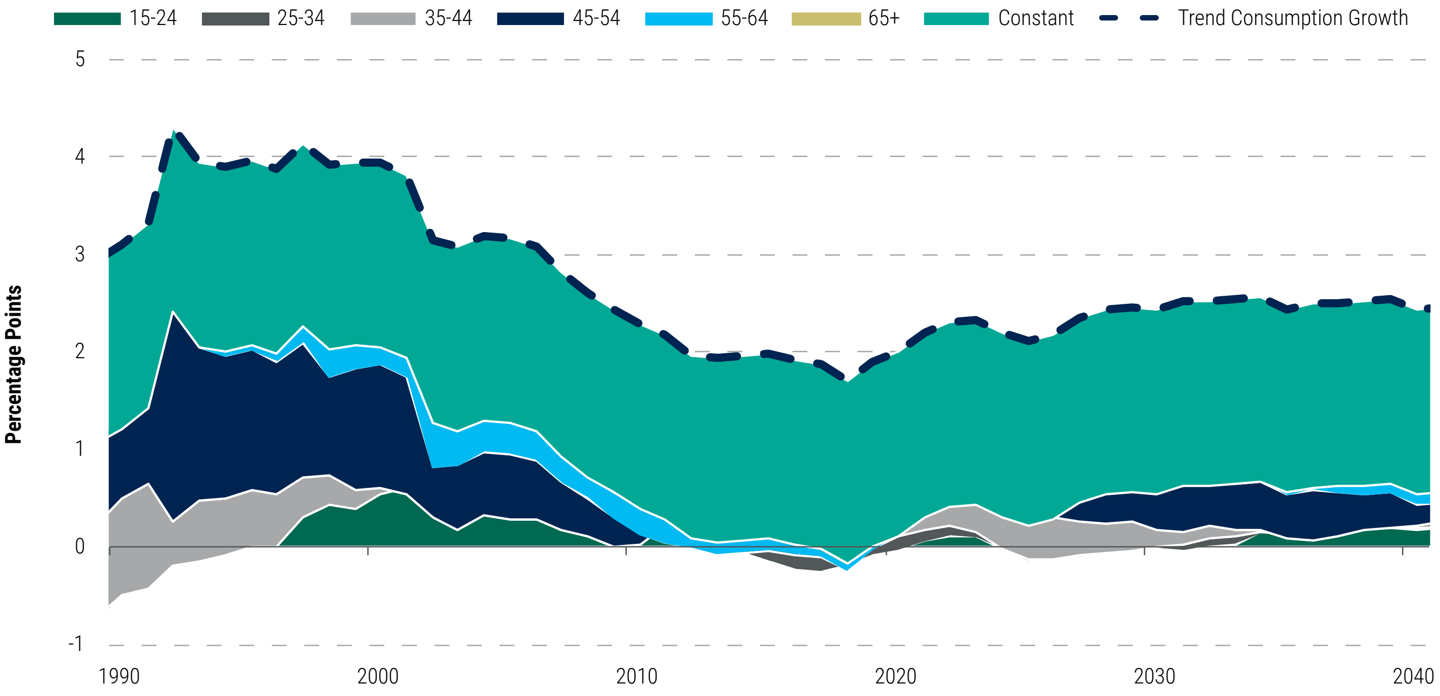
Within credit, we find it puzzling that despite the rally in high yield spreads, investment-grade credit curves have remained fairly steep. This may provide an opportunity.

Alternatives

The US midstream energy sector has been through a dramatic transformation over the last few years, as markets have disciplined it into reducing leverage and controlling capital expenditures. Yet the sector continues to trade at an attractive yield, despite an expected jump in EBITDA over the next few quarters as new pipelines finally come on-stream. This could set up this sector for a re-rating alongside the healthy return from carry.

US Demographic Contributions to Consumption Growth

We expect demographics to be a tailwind to US growth as millennials reach their peak consumption age.



Sources: Morgan Stanley, Census Bureau, as of 30 April 2019.

Asset Class Convictions and Capital Market Line (CML)

Here, we provide our intermediate-term convictions across major asset classes, along with select opportunities in regions where we have particular conviction in fundamentals.

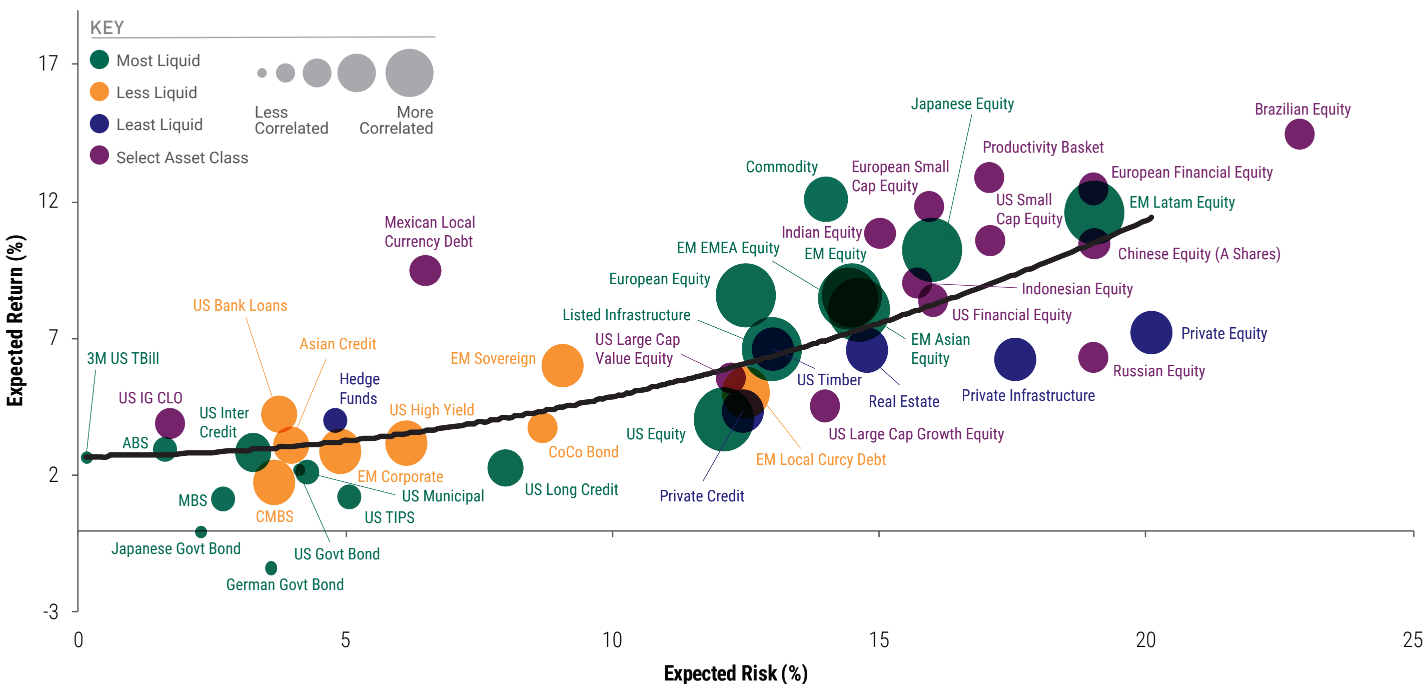
Key: ● Current Conviction ◍ Previous Month's Conviction (If Changed)

		Least Attractive	Unattractive	Neutral	Attractive	Most Attractive
Equities	**US**					
	US Financials				●	
	US Small Cap				●	
	US Small Cap Value				●	
	US Cyclicals				●	
	Japan				●	
	EM EMEA		●			
	European Small Caps				●	
	EM Latin America			●		
	Brazil Equity				●	
	EM Asia				●	
	India				●	
	China A-Shares					●
	South Korea					●
Fixed Income	**US Treasury**	●	◍			
	Intermediate Corporate		●			
	EM Debt: Local Curcy				●	
	High Yield		●			
	Bank Loans				●	
	EM Debt: Corporate			●		
	EM Debt: Sovereign				●	
	Investment-Grade CLO				●	
Alternatives	**Private Equity**		●			
	Hedge Funds		●			
	Real Estate			●		
	Commodities			●		
	Industrial Metals				●	
	Productivity Basket					●

Any views represent the opinion of the investment manager and are subject to change. For illustrative purposes only. We are not soliciting or recommending any action based on this material.

Capital Market Line as of 30 April 2019 (USD View, Local Currency)

Dispersion highlights several pockets of value that are positioned to benefit from the reflationary regime.



As of 30 April 2019. Based on PineBridge Investments' estimates of forward-looking five-year returns and standard deviation. The Capital Market Line ("CML") is not intended to represent the return prospects of any PineBridge products, only the attractiveness of asset class indices, compared across the capital markets. Please see Capital Market Line Endnotes. Note that the CML's shape and positioning were determined based on the larger categories and do not reflect the subset categories of select asset classes, which are shown to relative to other asset classes only.

About PineBridge Investments

PineBridge Investments is a private, global asset manager focused on active, high-conviction investing. We draw on the collective power of our experts in each discipline, market, and region of the world through an open culture of collaboration designed to identify the best ideas. Our mission is to exceed clients' expectations on every level, every day. As of 31 March 2019, the firm managed US$93.4 billion across global asset classes for sophisticated investors around the world.

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Capital Market Line Endnotes

The Capital Market Line (CML) is based on PineBridge Investments' estimates of forward-looking five-year returns and standard deviation. It is not intended to represent the return prospects of any PineBridge products, only the attractiveness of asset class indexes, compared across the capital markets. The CML quantifies several key fundamental judgments made by the Global Multi-Asset Team for each asset class, which, when combined with current pricing, results in our annualized return forecasts for each class over the next five years. The expected return for each asset class, together with our view of the risk for each asset class as defined by volatility, forms our CML. Certain statements contained herein may constitute "projections," "forecasts," and other "forward-looking statements" which do not reflect actual results and are based primarily upon applying retroactively a simulated set of assumptions to certain historical financial information. Any opinions, projections, forecasts, and forward-looking statements presented herein are valid only as of the date of this document and are subject to change. There can be no assurance that the expected returns will be achieved over any particular time horizon. Any views represent the opinion of the investment manager and are subject to change. For illustrative purposes only. We are not soliciting or recommending any action based on this material.

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