PIMCO

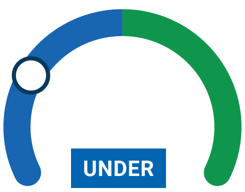
Whether Pause or Pivot, Look to Bonds

With the U.S. likely to enter a recession, investors are asking, are there better opportunities for allocation in global markets? We are selective in our approach.

In light of our macro and market forecasts, we favor bonds as a portfolio allocation due to their diversification, capital preservation, and upside opportunities. Starting yields appear competitive, and we favor high quality duration as well as select credit and securitized assets. In equities, however, we remain cautious as earnings expectations appear too high, and valuations too rich.

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

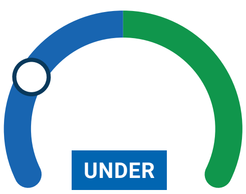
OVERALL RISK

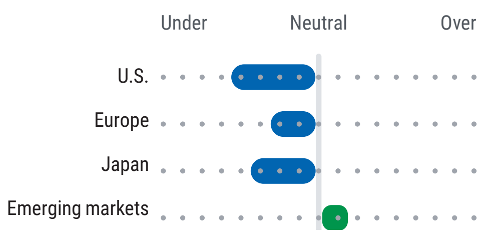


Despite a robust start to the year, the outlook is clouded by restrictive monetary policy, bank failures and still-elevated inflation. These factors appear likely to constrain bank lending and exert a material drag on activity. For this reason, we are underweight risk as the probability of an earlier, deeper recession has risen. Moreover, should a recession occur, policy responses are likely to be lagged and less aggressive compared to past cycles.

POSITIONING / OPPORTUNITIES

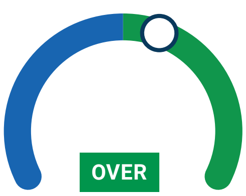
EQUITIES

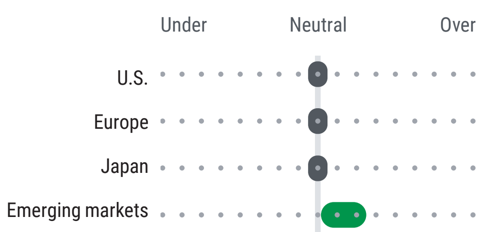




We are cautious on equities amidst an increasingly fragile growth outlook and overly optimistic valuations. These concerns are most prevalent in the U.S., which represents our largest underweight, but also lead us to be cautious on European and Japanese equities. Conversely, we believe the Chinese reopening is in its early stages so we are constructive on emerging markets but sizing is modest as idiosyncratic geopolitical issues remain a risk.

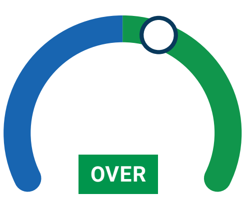
RATES

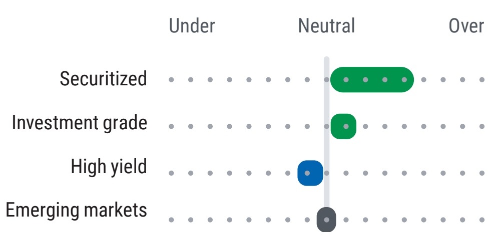




We are constructive on duration given slowing growth and the view that policy rates are close to peaking. Duration tilts within the developed world remain modest so we are neutral, remaining diversified across regions and tactically adjusting exposures as yields shift within their expected ranges. We find select, high quality emerging market duration offers a diversified, attractive source of return for investors.

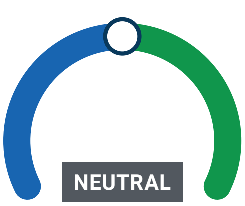
CREDIT

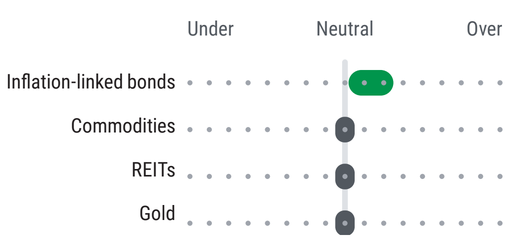




We are modestly overweight credit, emphasizing higher quality issues. Non-agency MBS stands out given its strong fundamentals and attractive valuations. High all-in yields and wider spreads in investment grade corporate credit should provide greater downside cushion in a recession. However, we are cautious on lower quality issues as tight financial conditions are expected to weigh on fundamentals, though we believe defaults should remain in-line with historical averages.

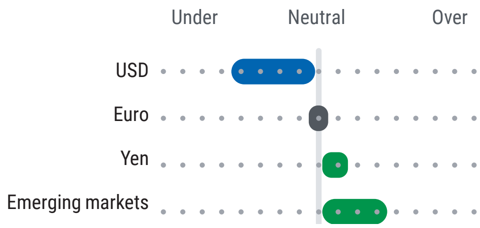
REAL ASSETS





We believe markets are fairly reflecting the path of inflation so we are neutral on real assets but recognize inflationary risks skew to the upside. We find inflation-linked bonds attractive as they should provide protection in a recession, an upside inflation surprise, or both. Despite commodities' inflation hedging potential, most may struggle over the cyclical horizon given their dependence on growth so we are neutral. We are monitoring relative value opportunities in the asset class.

CURRENCIES



We are cautious on the U.S. Dollar due to a likely peaking U.S. policy rate, an anticipated US relative growth deficit, and overvaluation concerns. Instead, we favor emerging markets' currencies, which should be supported by stronger growth as well as valuation tailwinds, and to a lesser extent, the Japanese Yen, which should benefit if Japanese rates move higher. We are neutral on the Euro as we expect higher policy rates in the region to be offset by slowing growth.

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