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Falling inflation will provide support during slump

China's economy is gearing up as the rest of the world slows down into a brief, shallow recession in which corporate earnings will hold up well. The investor community is restrained and cautiously positioned, while the corporate sector is thriving and in good shape. Our main economic scenario foresees a slowdown in 2023 and an acceleration during 2024. We support a neutral allocation at the asset class level, combined with good risk diversification, since volatility is likely to persist.

Inflation has peaked, and we are approaching the first interest rate cut by the US Federal Reserve. Another positive factor worth highlighting is that Chinese economic growth is going against the flow, contributing to our main scenario of a soft landing and a relatively shallow, short-lived recession. Looking at the minus side, a recession can always be more severe than desired, and the impact of record-fast central bank rate hikes arrives only after a time lag.

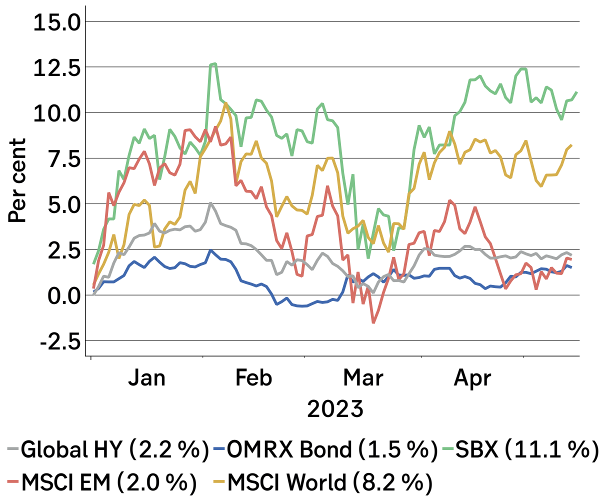
Allocation

Given this situation, we are maintaining the view that it is wise to continue spreading risks across several different asset classes and sub-classes. In Swedish equities, we have reduced our holdings of pure value companies, except in the strategy that focuses specifically on value companies. In global equities we are overweight in large cap growth companies, which serve as a good complement to our Swedish equity portfolio. For the time being, we are also maintaining the partial currency hedging of the US dollar that we initiated last autumn. Unusually, our fixed income portfolios have a fairly neutral structure in terms of interest rate and credit risk. Our alternative investment holdings are living their own lives; as intended, they have a low correlation with our equity and fixed income portfolios. The overall result is unusually broad portfolios, which at the aggregate level have a neutral weight in equities combined with an overweight in fixed income investments at the expense of the proportion of alternative investments. This composition enabled us to earn positive returns last autumn and during the early-2023 rally, as well as to avoid losing ground when such unforeseen events as bank failures affected the market.

Valuations and stock market performance

World stock markets have largely moved sideways over the past twelve months, but with big ups and downs. The corporate sector has delivered surprisingly stable earnings at the aggregate level. Share valuations are at around their historical averages. Waiting around the corner are key interest rate cuts, falling inflation and a cyclical turnaround, but we need either lower valuations or a clearly favourable growth and inflation outlook to become more optimistic about global equities at present. However, we have a cautiously optimistic view of the Nordic stock market for the rest of 2023, since solid earnings growth will outweigh negative factors.

Portfolio performance has been bumpy this year, but with positive signs



Source: Bloomberg

Global equities

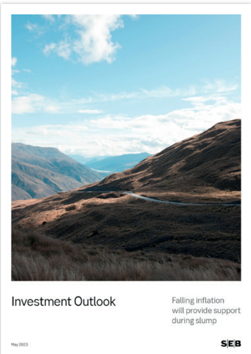
- Key interest rate hikes, anaemic economic growth and banking sector turbulence have not hurt equities
- First quarter 2023 corporate earnings surprised on the upside, but we foresee continued downside risks for earnings this year
- In a short-term perspective we have a negative view of equities, since valuations are not low enough to offset the uncertain economic outlook
- Accelerating economic growth, low valuations and the imminent end to US key rate hikes will favour emerging markets

Fixed income investments

- Central banks are nearing the peak of their rate hiking cycle
- Bond yields are expected to fall during the second half of 2023 in line with central bank rhetoric
- Strong absolute yields in both investment grade (IG) and high yield (HY), but relatively narrow yield spreads
- A continued weakening of the US dollar and lower key interest rates may provide support for emerging market debt

Nordic equities

- Steady corporate earnings growth, with Nordic industrials shining bright
- Energy prices, motor vehicles and China will provide support
- Real estate, forest products, consumer goods and oil are among problem sectors
- Continued focus on weak business and consumer sentiment, central banks and inflation
- Banking sector turmoil provides opportunities for investors and illustrate the delayed impact of higher interest rates



For more details, please read the full report, which also provides you with extra reading in the form of three interesting theme articles:

- New supercycle on the way
- Cracks in the façade, but a solid foundation
- Why are alternative investments appealing?

Our experts Fredrik Öberg and Johan Hagbarth also present our in-depth market view in the form of a video.

You will find all this at seb.se/investmentoutlookreport

Investments
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