

Opportunity In Uncertainty: Building Resilient Portfolios With Income

Webinar for the Hong Kong Retirement Schemes Association (HKRSA)

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Agenda

- Are Interest Rates High Enough?
- The Outlook on U.S Growth, Inflation and the Rest of the World
- Are There Buyers of Bonds?
- The Long-Term Allocation to Fixed Income

Are Interest Rates High Enough?

It's Always a Soft Landing... Until It's Not

In the U.S., soft landing hopes overtake hard landing fears, but it's complicated, and risks to growth are elevated.

The Economy Is Facing Stiff Headwinds (Hard Landing Risk):

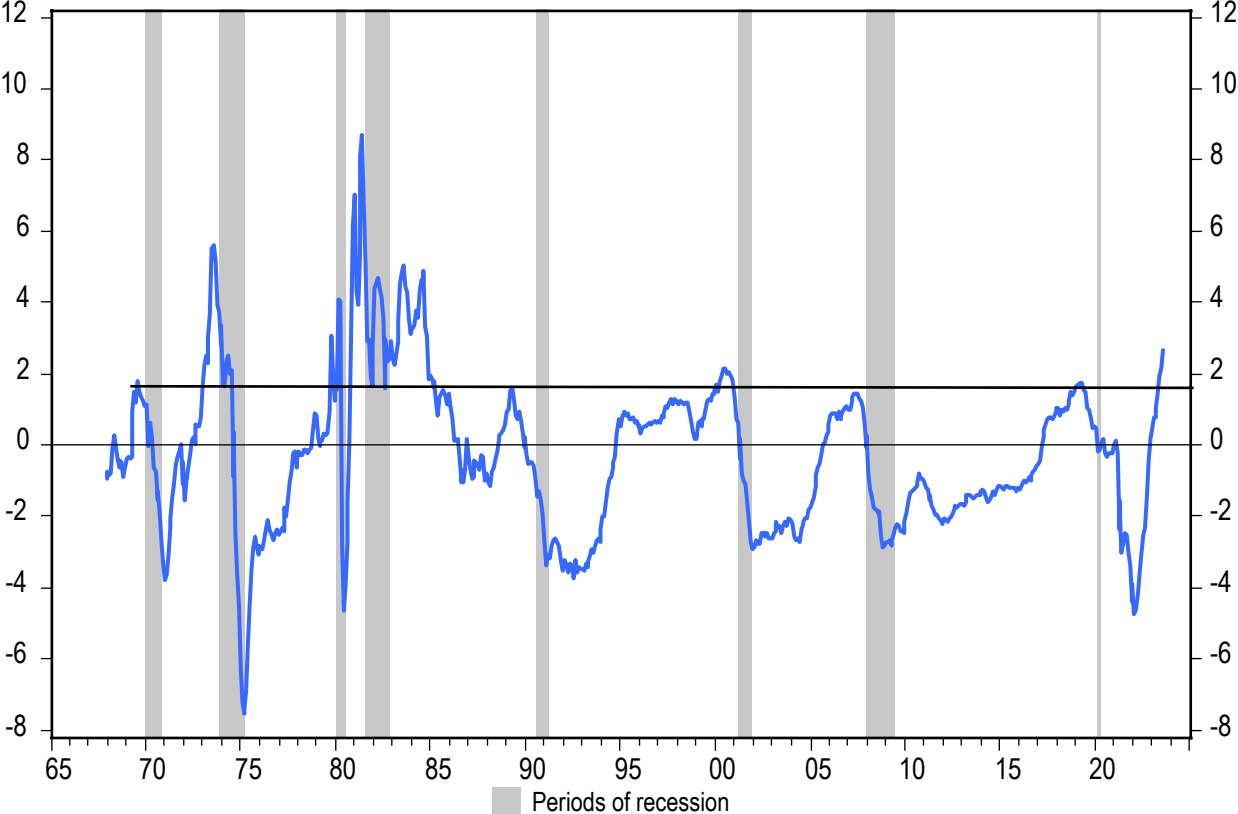
- Leading Economic Indicators Continue Flashing Warning Signs
- Consumer Headwinds Mount
- Housing Market Frozen
- Student Loan Payments Restart
- Oil Prices Up
- Tight Credit Conditions
- Labor Markets Are Rebalancing Rapidly
- Excess Savings Being Depleted
- Manufacturing Malaise
- Quantitative Tightening Behind the Scenes

...But There Are Tailwinds, as Well (Soft Landing Potential):

- Consumer Balance Sheets at Strong Starting Point
- Fiscal Spend
- AI Fueled Productivity Gains
- Structural Support for Labor
- Inflation - Mission Accomplished or Next Wave?

US Policy Rates Are In Restrictive Territory

Real Fed Funds - 10Y Moving Average Using Core CPI



Source: Haver Analytics, 10/05/23

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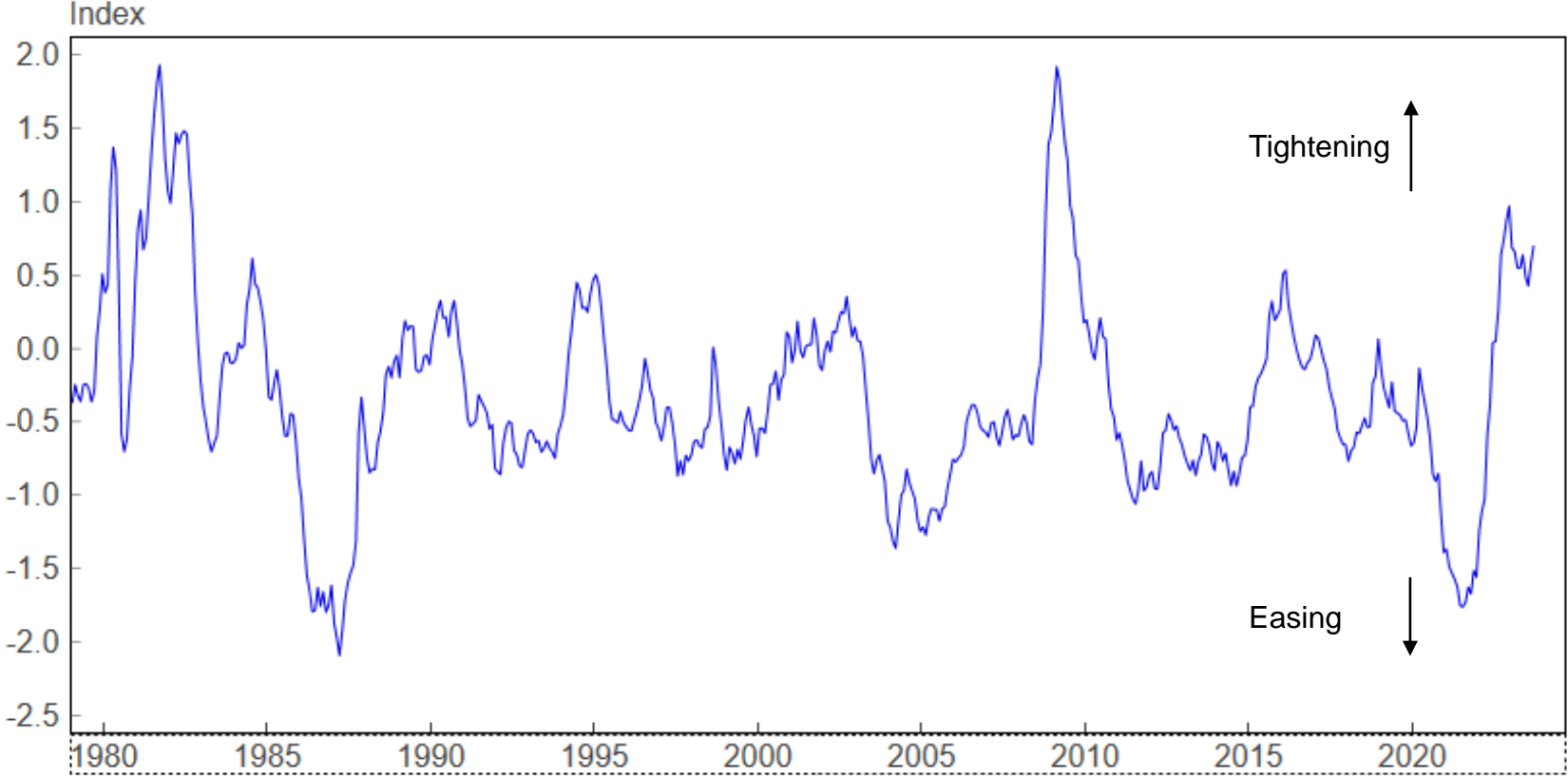
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Units in Percentage.

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FED's Financial Conditions Impulse on Growth

United States, Leading Indicators, Federal Reserve, Financial Conditions Impulse on Growth, FCI-G Index (Three-Years Lookback), Index



Brandywine Global, Macrobond, Fed. As of 9/2023.
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The Outlook on U.S Growth, Inflation and the Rest of the World

U.S. – Consumer Squeeze

Cost of Living Crisis

The Average...	2023 (in USD)	2020 (in USD)	Change
New Home Mortgage Payment	\$2,900/month	\$1,600/month	+81%
New Car Payment	\$750/month	\$550/month	+36%
Used Car Payment	\$550/month	\$400/month	+38%
Gallon of Gas	\$3.75	\$2.25	+67%
Student Loan Payment	\$500/month	\$300/month	+67%
Credit Card Balance (per household)	\$10,000	\$6,600	+52%
MEDIAN HOUSEHOLD INCOME	\$92,750 ('22)	\$84,350	+10%

*** **Excess Savings** has been exhausted for all but the top 20% (by income) of Americans.

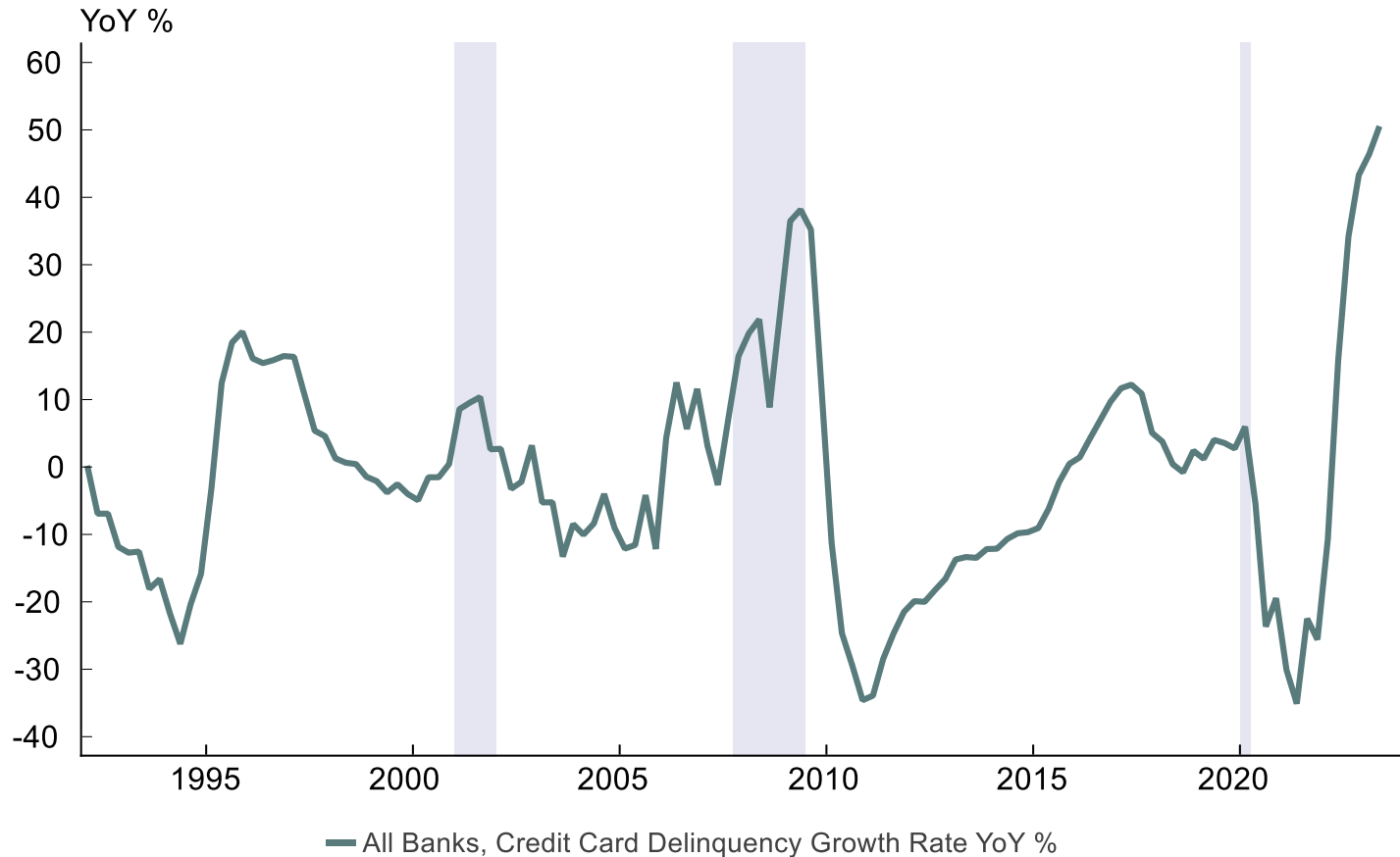
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U.S. – Rapid Rise in Credit Card Delinquencies

Overall delinquency growth surges, while small banks have delinquency rates at record levels.

Credit Cards Delinquency Growth Rate



Brandywine Global, Macrobond, Fed

As of October 2023

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Gray areas denote periods of recession.

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U.S. – Housing Market Is Frozen

Housing affordability today is worse than the peak of the last housing bubble.

U.S. Pending Home Sales



Brandywine Global, Macrobond, NAR
As of October 2023

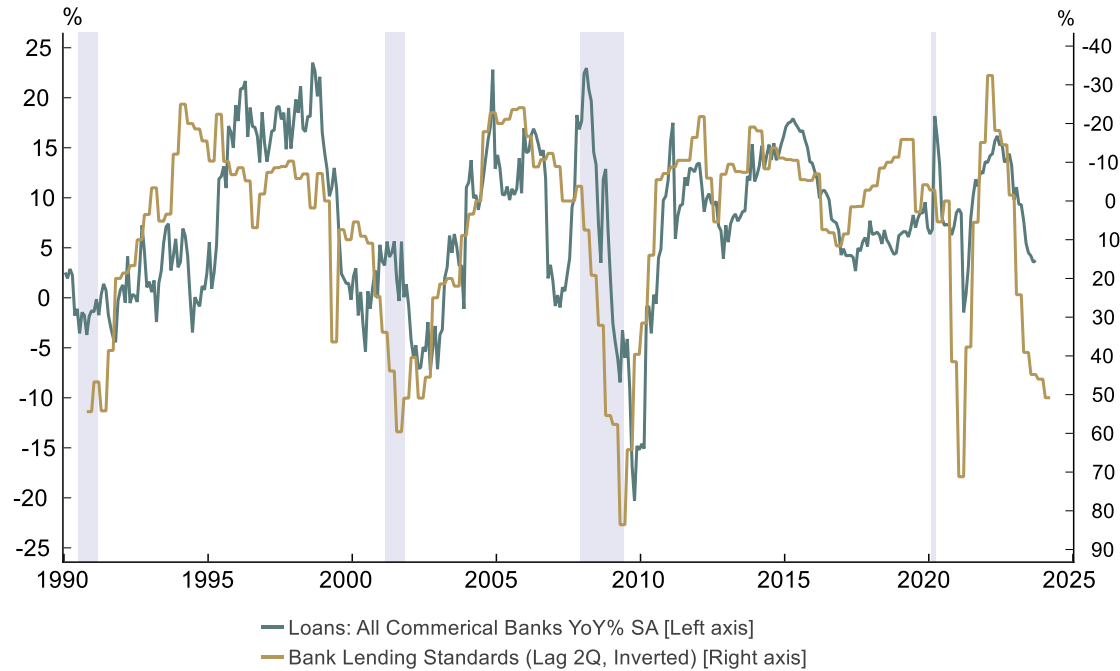
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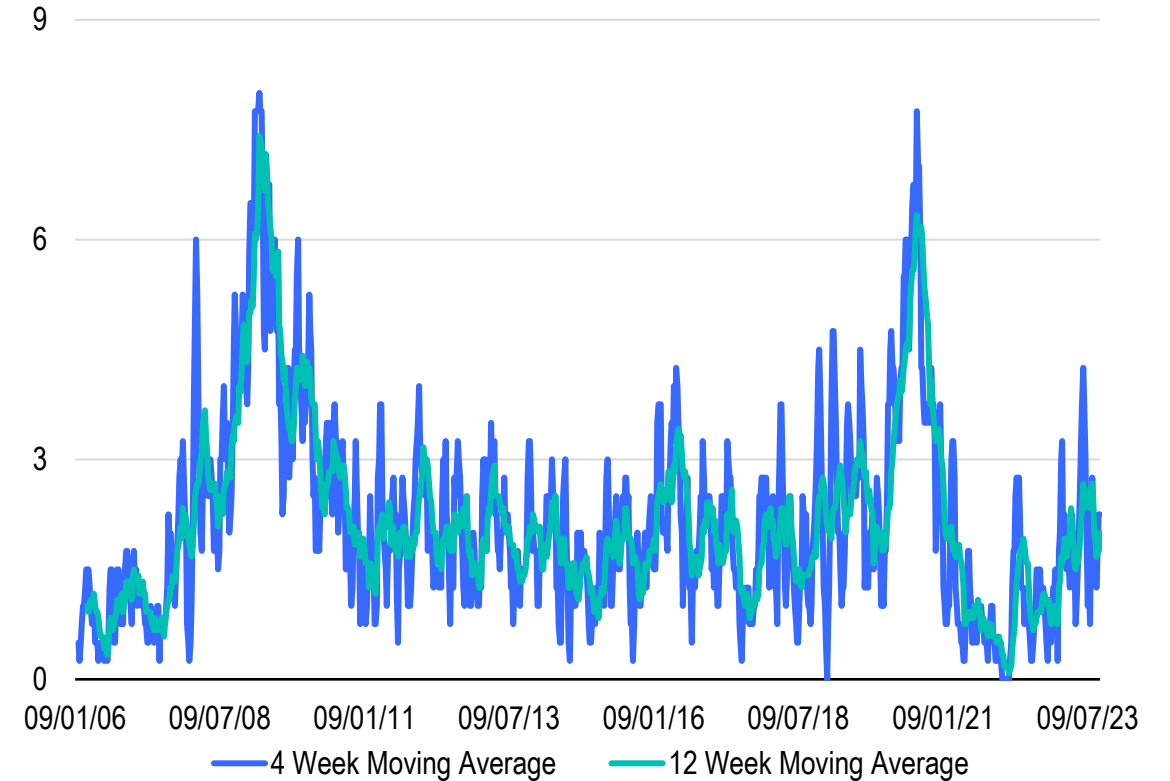
U.S. – Tightening of Lending Standards Continues, Bankruptcy Filings Increasing

The number of banks tightening lending standards is reaching multi-decade highs.

Bank Loans (Left) vs. Lending Standards (Right)



United States: Bankruptcy Filings



Brandywine Global, Macrobond, Fed
 As of October 2023

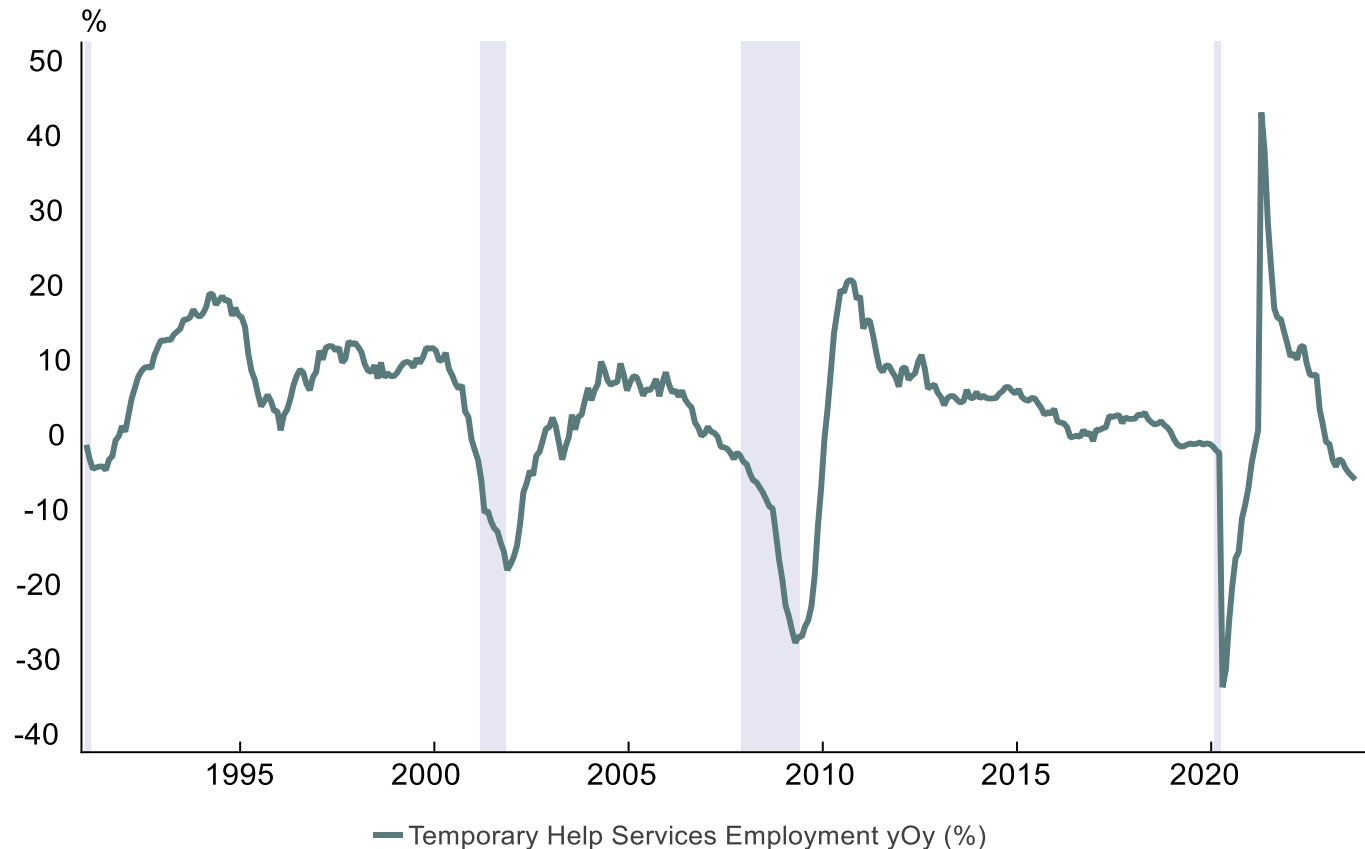
Underlying data consists of US companies with US\$50M or more in liabilities
 As of September 2023

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U.S. – Temporary Workers Are Losing Their Jobs

Leading indicator for labor market flashing warning signs.

Temporary Help Services Employment



Brandywine Global, Macrobond, BLS

As of October 2023

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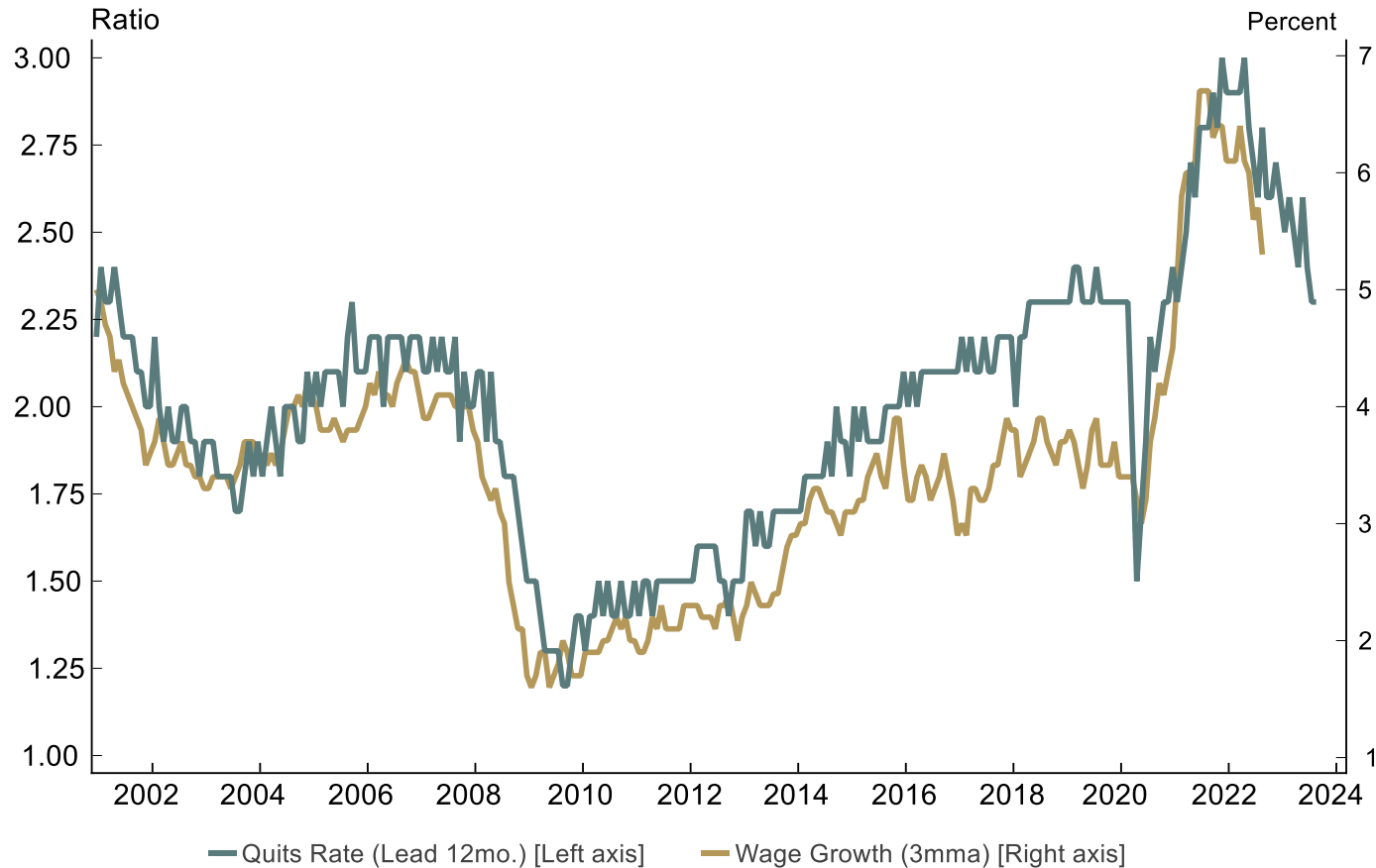
Gray areas denote periods of recession.

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U.S. – Wage Growth is Softening

Americans are quitting their jobs at a significantly slower pace.

Leading Indicators for Wage Growth



Brandywine Global, Macrobond, BLS, Federal Reserve Bank of Atlanta

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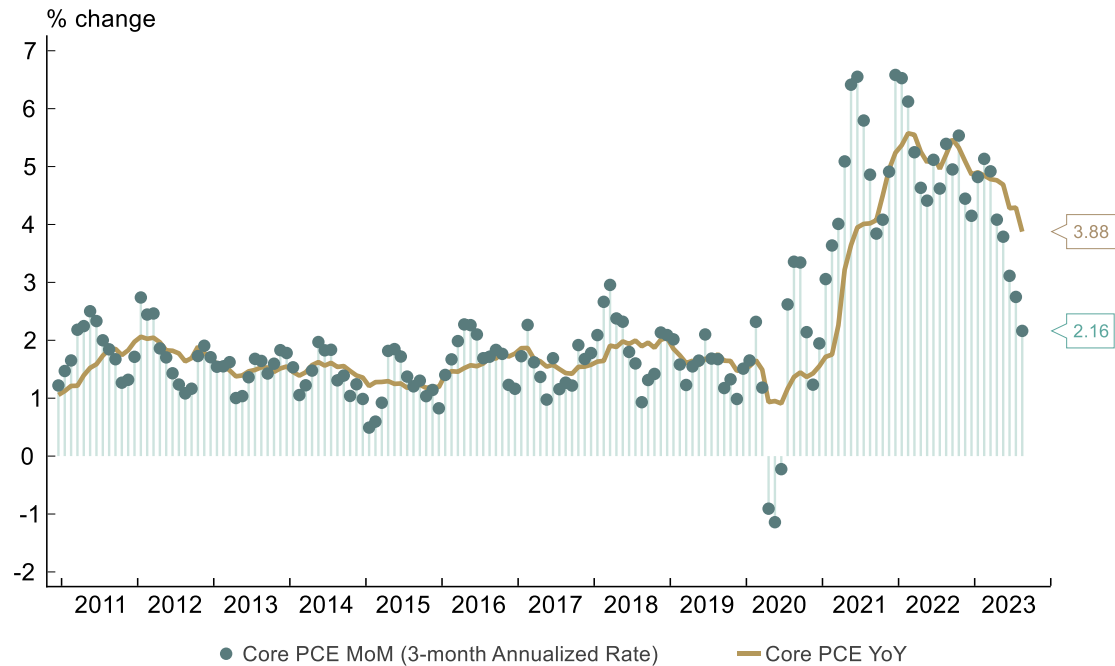
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Inflation: Mission Accomplished?

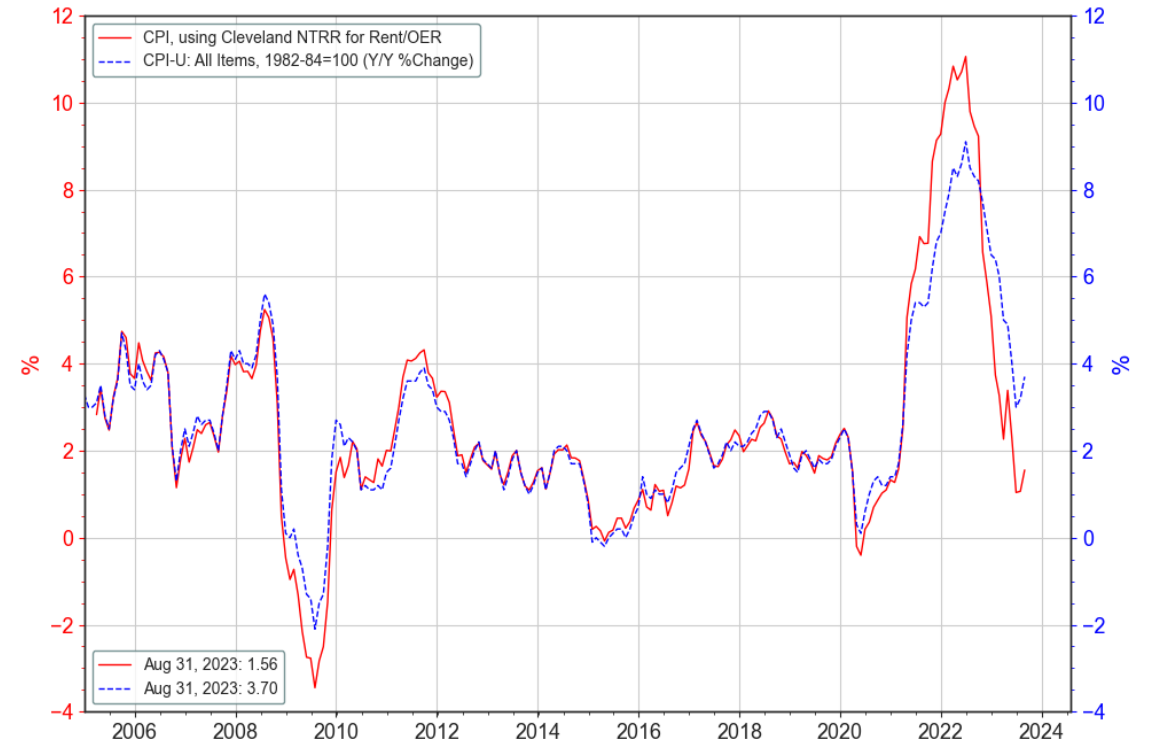
Annualized inflation rate (last 3 months) is now at the Fed's target.

Note the trajectory – declining quickly!

United States: Core PCE



CPI Using Market Rents



Brandywine Global, Macrobond, BEA
As of October 2023

Source: H/Bloomberg/Brandywine Global/BLS. Data as of 10/08/2023

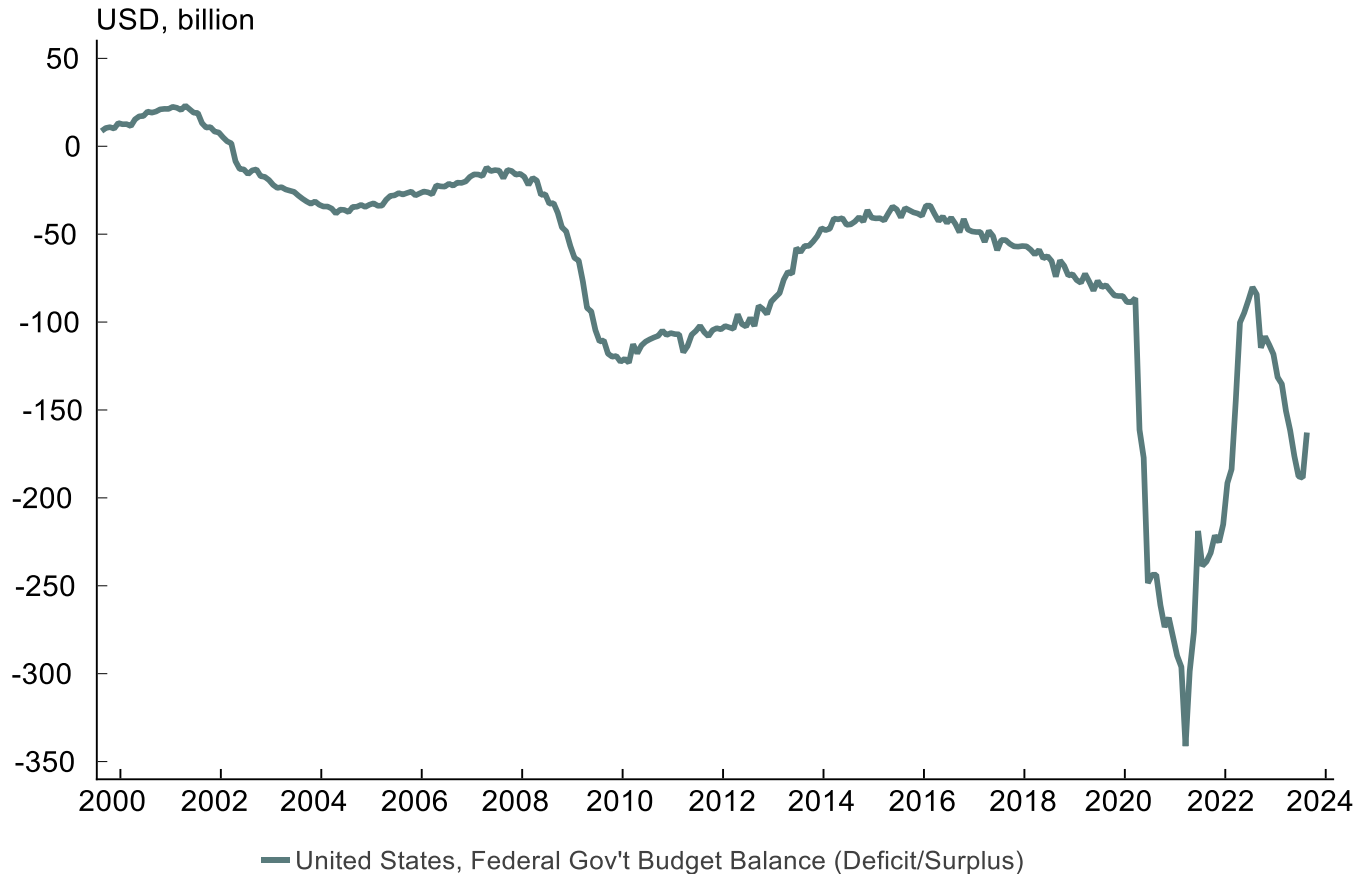
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U.S. – Fiscal at Odds With Monetary

Federal outlays are still US\$1 trillion above pre-Covid trend, and nearly 24% of GDP.

United States, Federal Gov't Budget Balance (Deficit/Surplus)



Brandywine Global, Macrobond, U.S. Department of Treasury

As of October 2023

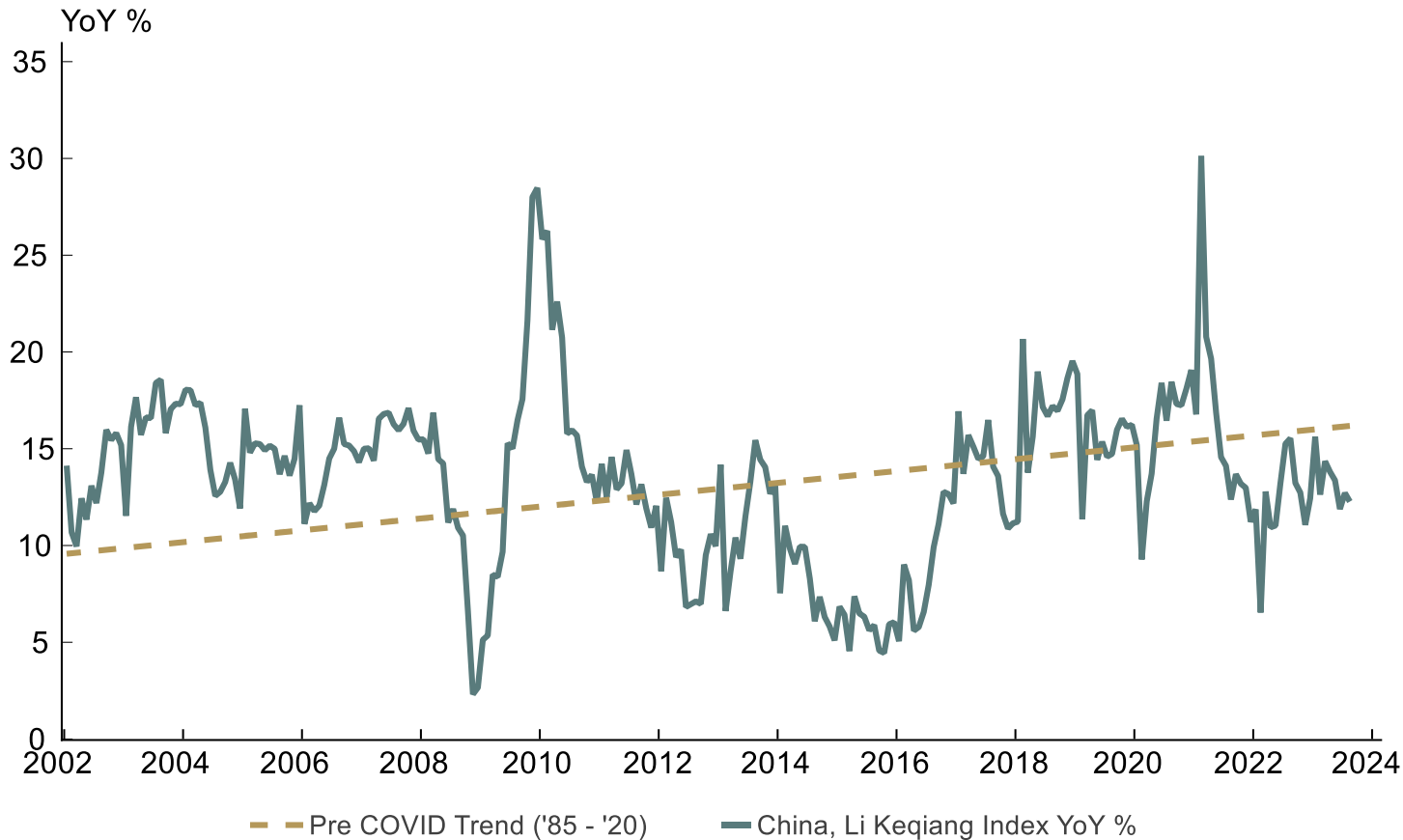
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China – Lackluster Growth Continues

Weak Chinese growth will provide an additional disinflationary impulse to the global economy.

China – Li Keqiang Index



Brandywine Global, Macrobond, Macrobond

As of October 2023

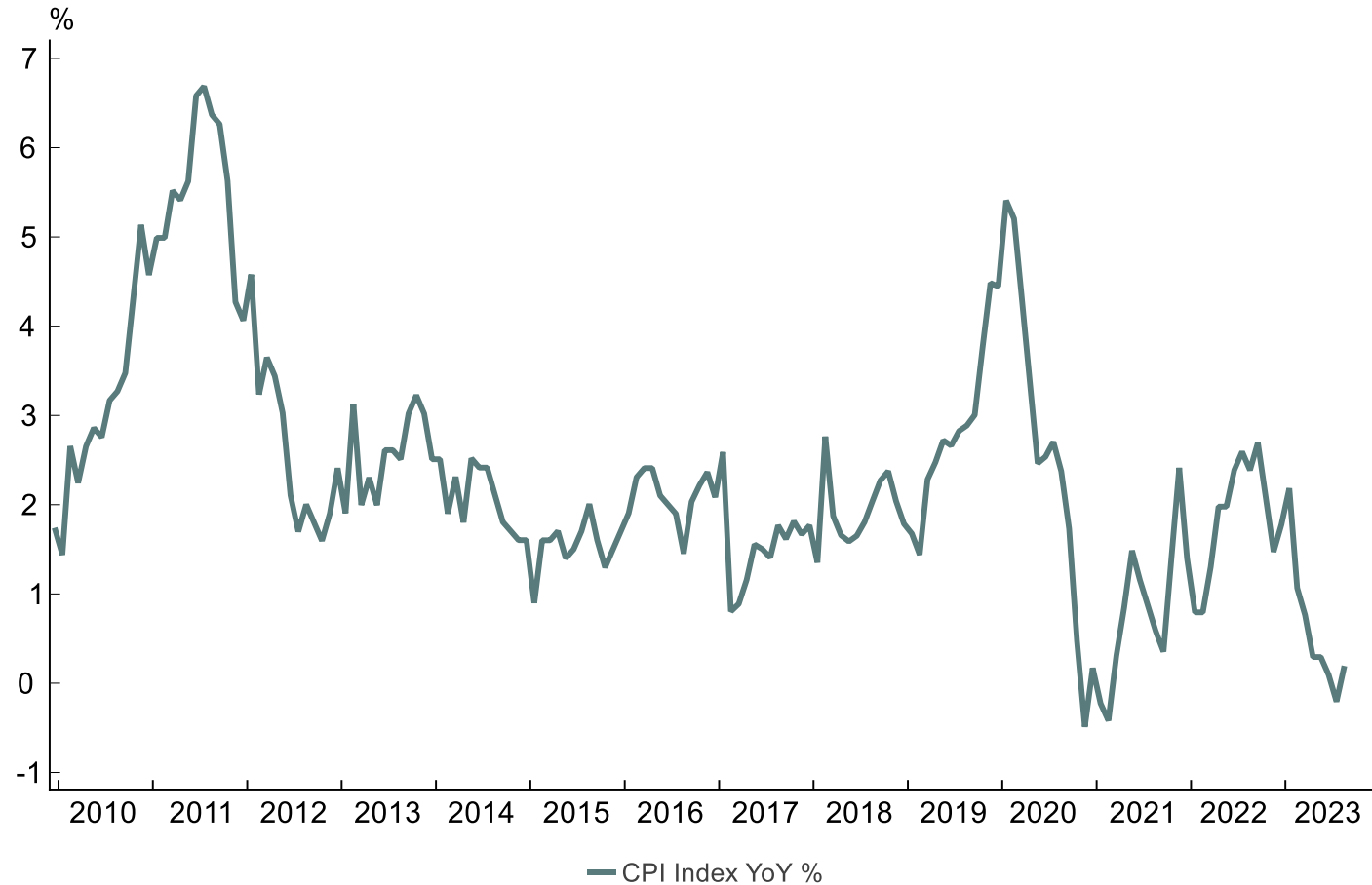
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China – Inflation Non-Existent

Reflective of soft domestic demand.

China – Consumer Price Index



Brandywine Global, Macrobond, NBS

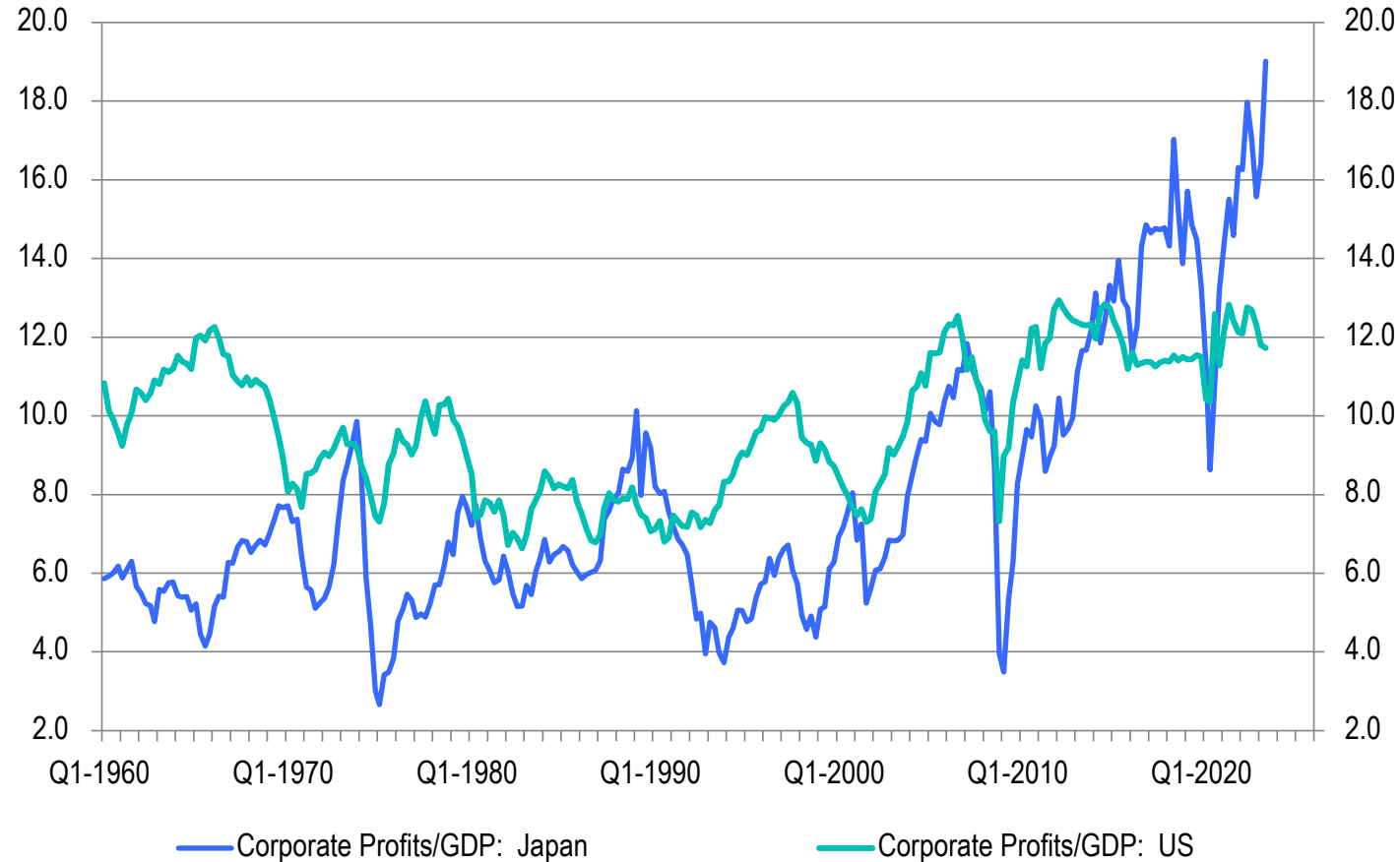
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Japan – Record Corporate Profitability Sustaining Expansion

Corporate Profits (%GDP): Japan vs US



Data as of September 2023.

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BoJ Too Easy With Highest Inflation Rate in 30 Years

Bank of Japan – Real Policy Rate



Source: BoJ/Brandywine Global, data as of 10/08/2023.

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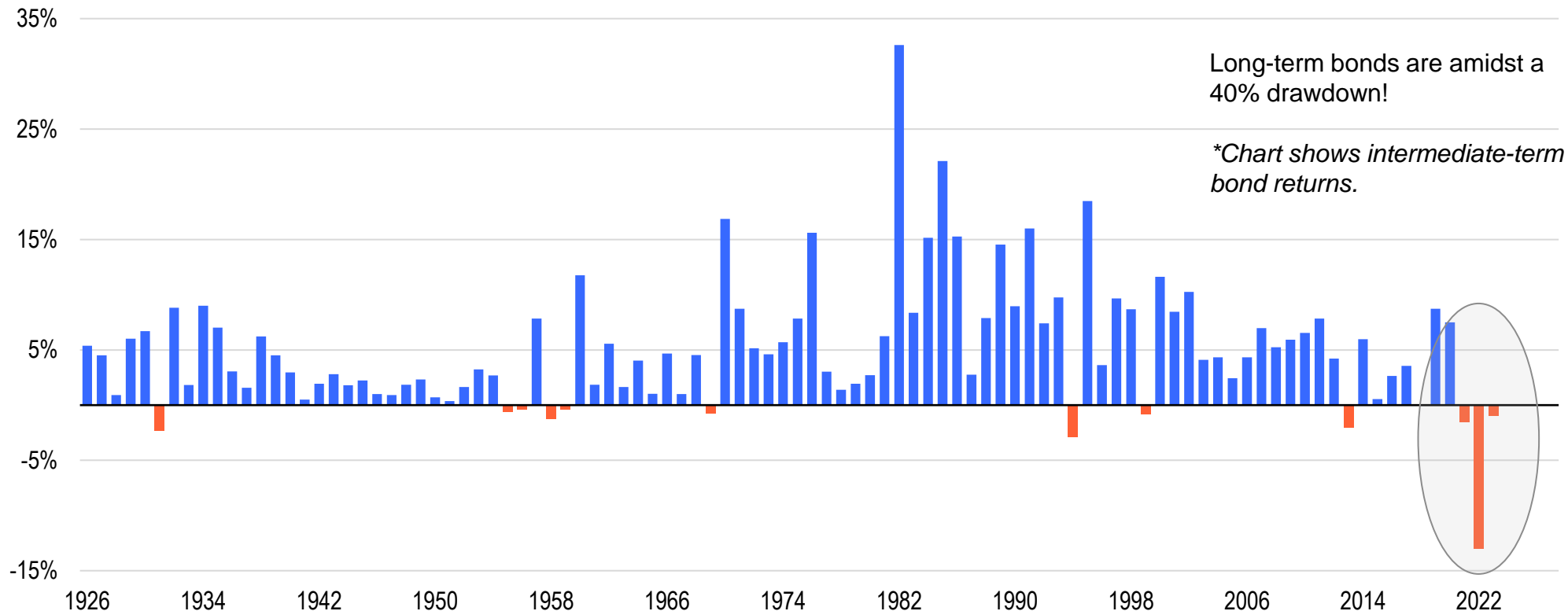
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Are there Buyers of Bonds?

The Great Bond Market Massacre

One for the record books? There has never been back-to-back-to-back calendar year losses for US bonds.

Calendar Year Returns for US Bonds

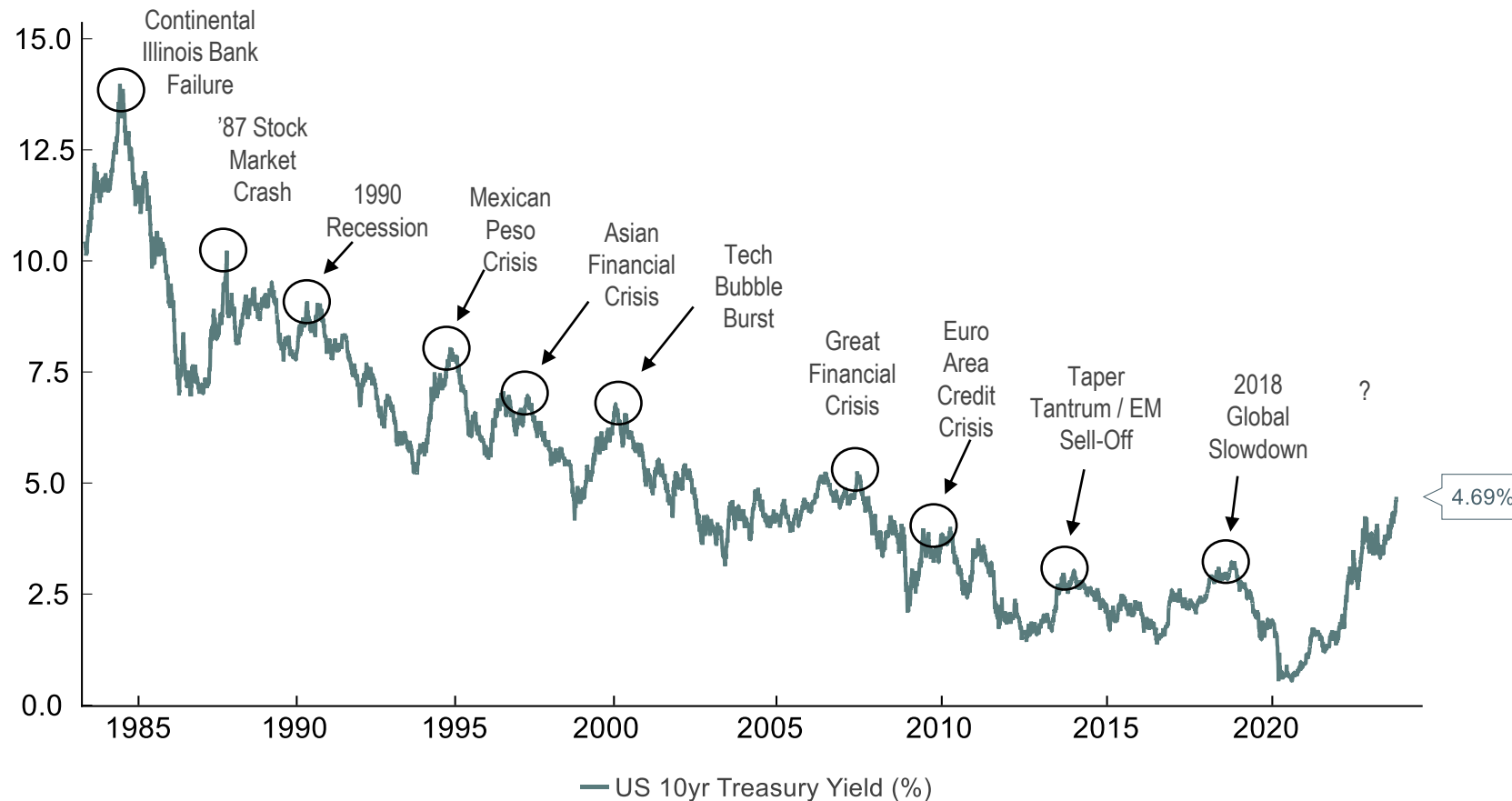


Index used is a blend. Blend is sourced from research by Ibbotson and Sinquefeld using the Intermediate-Term US Government Index from 1926-1975, then the Bloomberg US Agg from 1976 onwards.

Wrecking Ball

Surging bond yields often lead to financial accidents.

US 10 year Treasury Yield



Brandywine Global, Macrobond, Macrobond, U.S. Department of Treasury

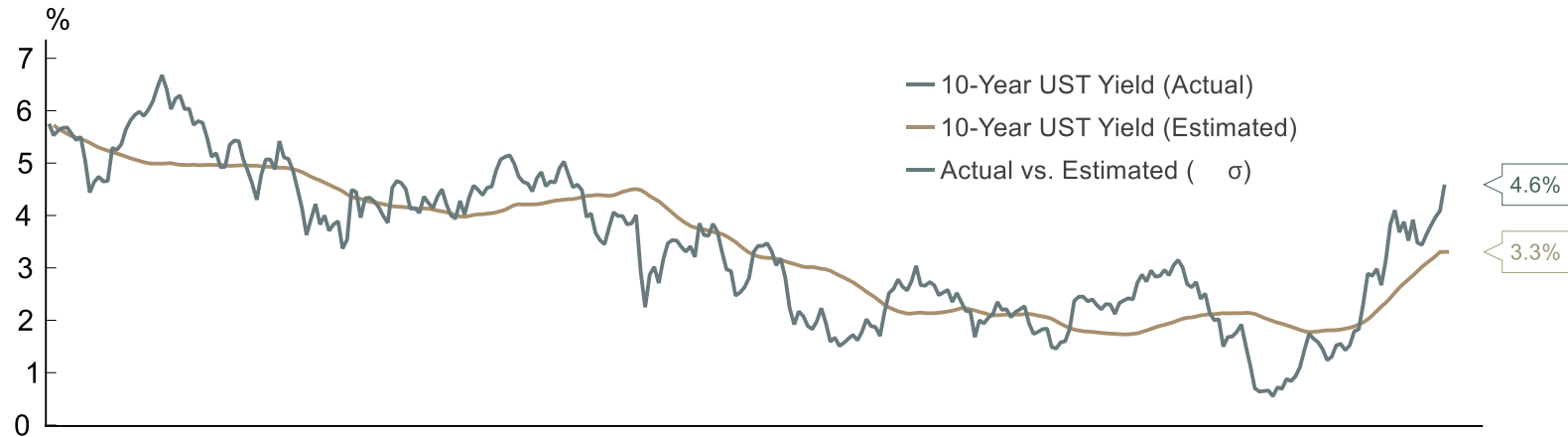
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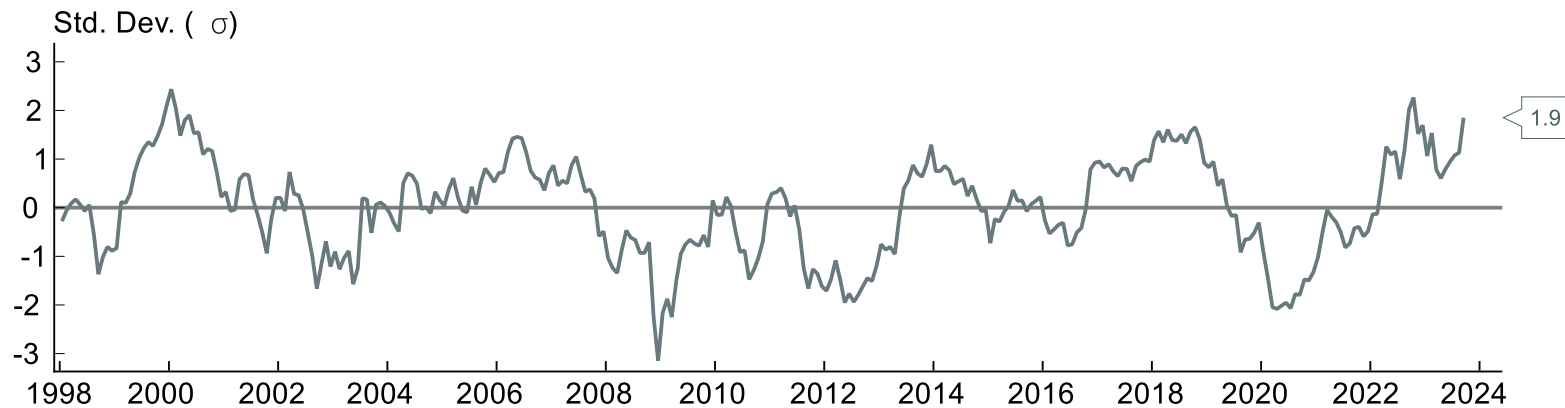
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U.S. Treasuries Look Attractive

10 Year U.S. Treasury Bond Model



Std. Dev. Between Actual and Estimated Yields



Brandywine Global, Macrobond. As of 10/7/2023

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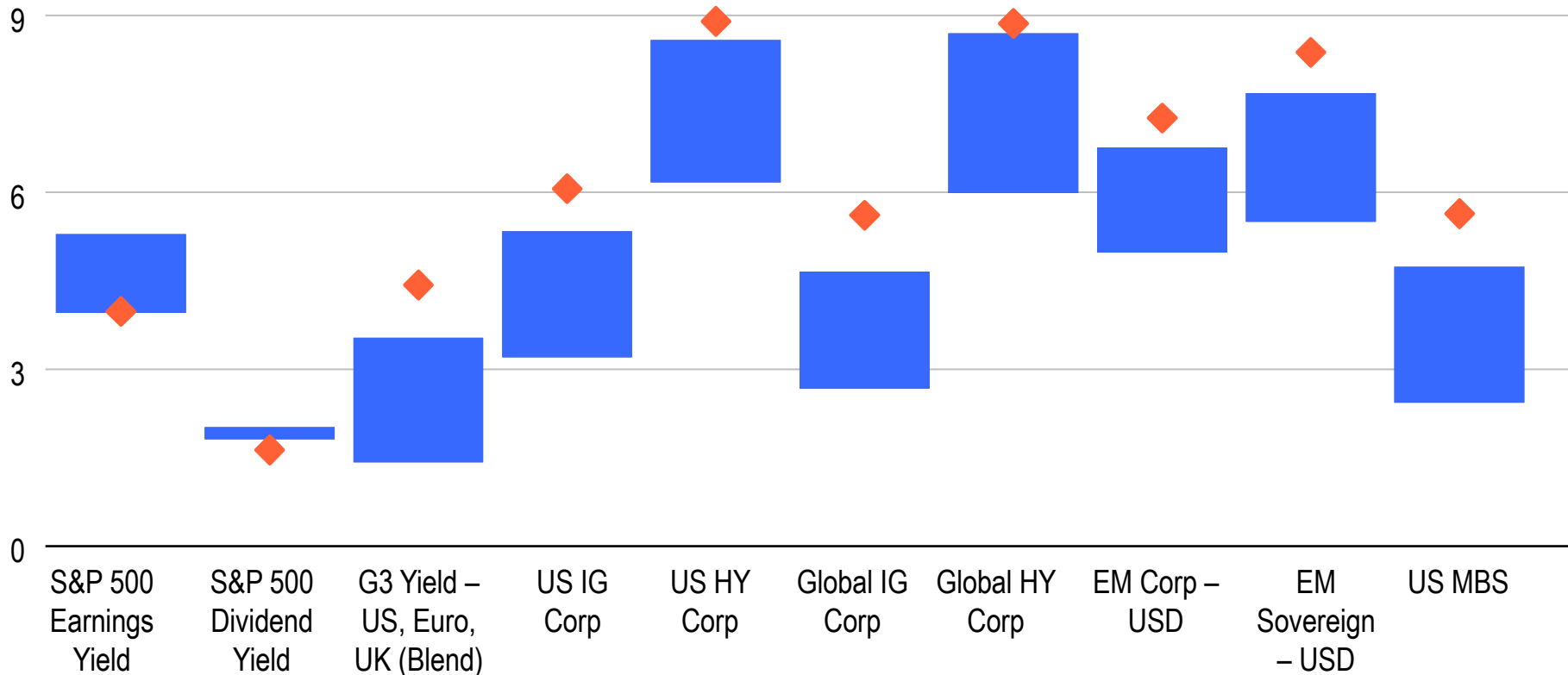
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The Long-term Allocation to Fixed Income

Fixed Income Has Income Again

U.S. investment grade bond yields are above the U.S. equity earnings yield for first time in 20 years.

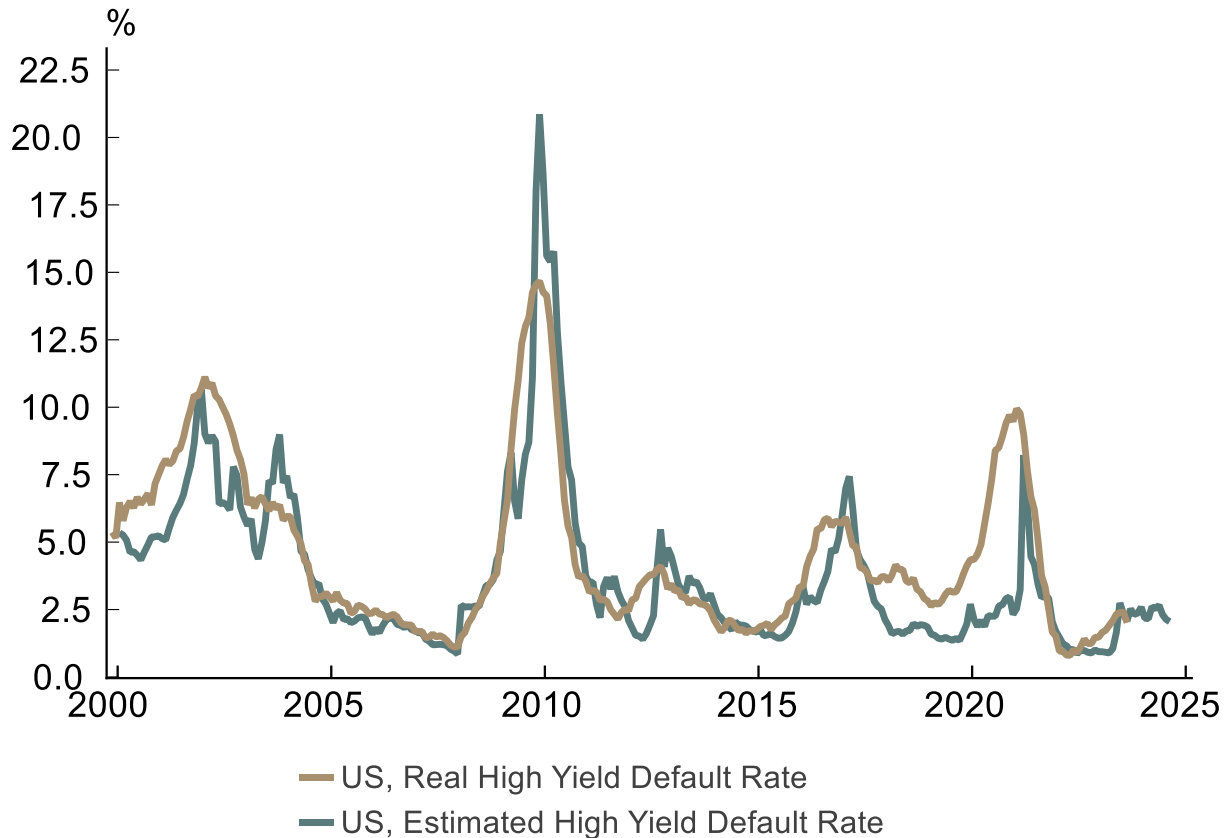
Cross Asset Yield Rankings (Since 12/31/2001)



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As of 30 September 2023.

High Yield Corporates – Defaults Remain Subdued, Selection Critical

US High Yield Default Rate

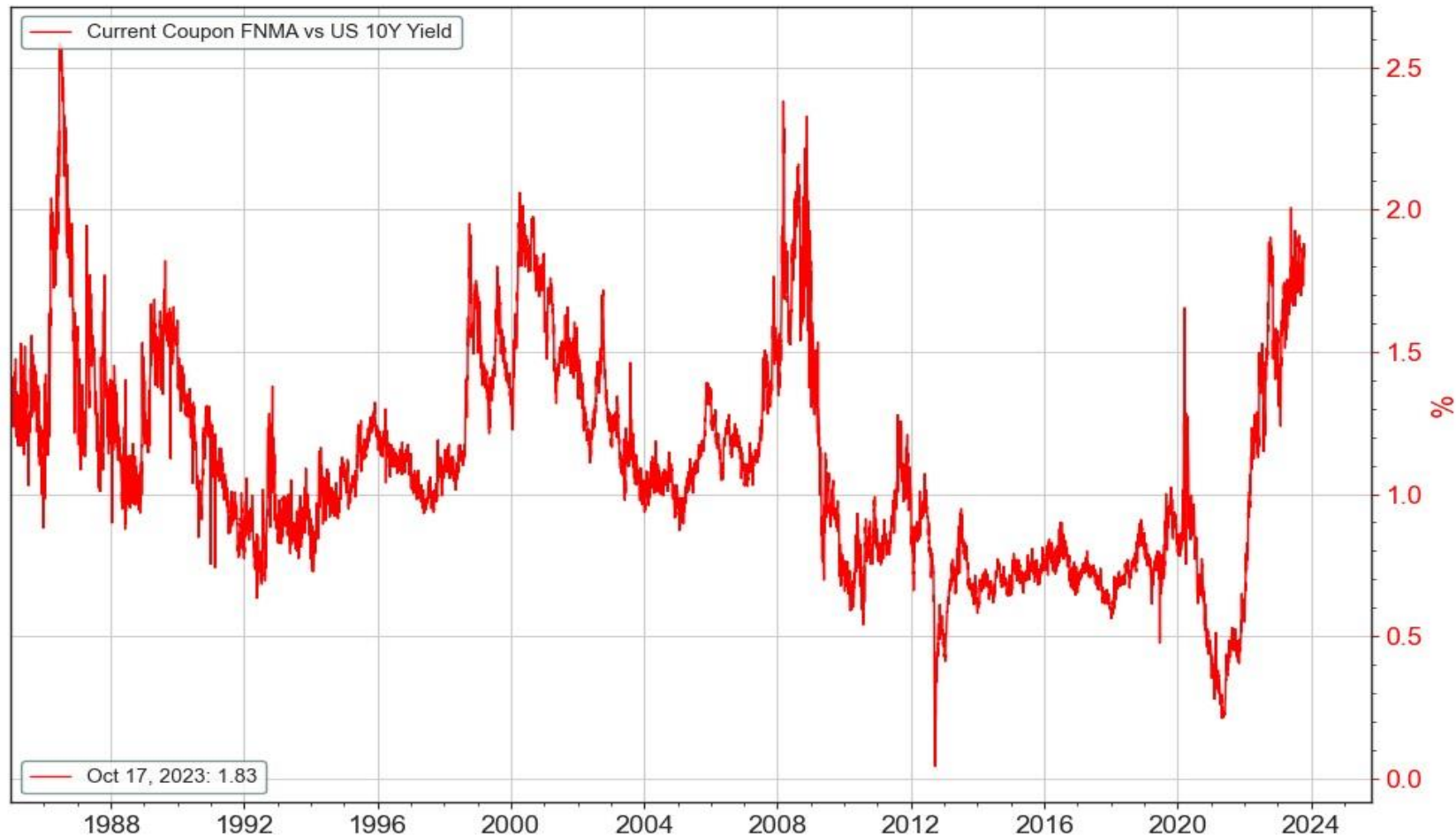


Brandywine Global, Macrobond,
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Agency MBS Exposure is Attractive

Current Coupon FNMA vs US 10Y Yield



Source: Bloomberg/Brandywine Global, data as of 10/17/2023

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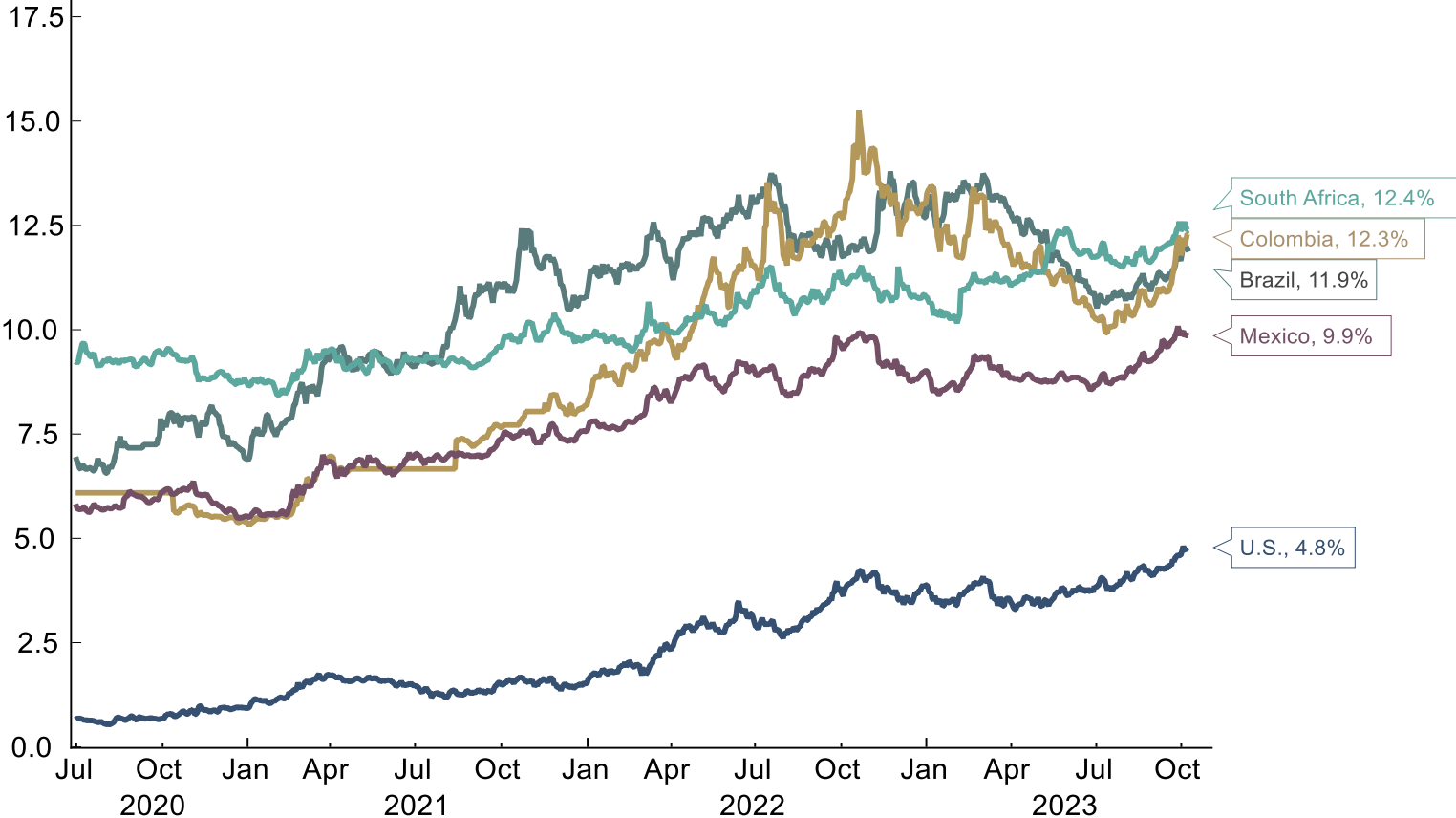
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Emerging Market Local Bonds Still Attractive



Higher-yielding emerging market bonds offer strong carry, wide spreads to Treasuries.

Emerging Market Local Bonds 10yr Gov't Bond Yield Comparison



Brandywine Global, Macrobond, U.S. Department of Treasury
As of October 2023.

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