2023 special: an **unexpectedly great year** for investments

- **All asset classes delivered very positive returns in 2023, against most predictions**
- **A large majority of 2023 portfolio returns was generated in the last two months of the year**
- **We will issue our full 2024 Global Investment Outlook later in January, as always.**

2023 has been a spectacular year for investments in many ways. First, all asset classes did very well: from +3% for hedge funds, +4% for government bonds, +5% for cash to +13% for gold, +14% for high yield and almost +24% for stocks from developed markets.

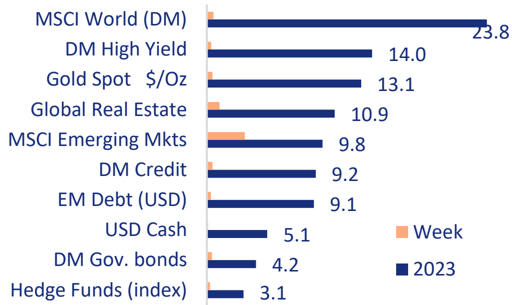
In addition, volatility was material, with several full swings in terms of scenario, especially on inflation and central banks, that shaped risk appetite and aversion. Finally, it was a difficult year for forecasters. Both growth and market returns were much better than what pretty much everybody had predicted a year ago. This was a driver for the year-end rally, which wasn't about the economy or a sudden burst of euphoria. It was the painful capitulation of overly pessimistic investors, caught short by unexpected good news, spiralling into the fear of missing out and panic buying.

We had started 2023 with humility, calling it the year of unpredictability. We prioritized core portfolio construction, with a reshuffled strategic asset allocation, over low confidence tactical bets. It worked. Our profiles returned respectively +9%, +13% and +15% (rounded), outperforming our global peers.

The questions of 2023 are still here as we start 2024, but this time, they will be answered: from growth, inflation and central banks to major political and geopolitical developments, markets will be volatile, in a constant adjustment between implicit expectations and reality.

We will release our 2024 Global Outlook later this month – we always wait for the actual end of year, to report accurately, including on our own performance. It's not over until it's over, which was particularly the case in 2023. We wish you a peaceful, healthy, joyful and prosperous new year.

ASSET CLASSES USD % TOT.RETURN, YTD 2023 & LAST WEEK



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Cross-asset Update

In this "2023 Special" we will have a quick look-back at what was clearly a remarkable year for global markets. It may be useful to remember that it followed a genuinely devastating 2022. The return of inflation, as a consequence of the post-Covid rebound, turbocharged by an unprecedented level of global monetary and fiscal support, had created a "correlation shock" on markets where every single asset class was negatively hit, with the only exception of cash.

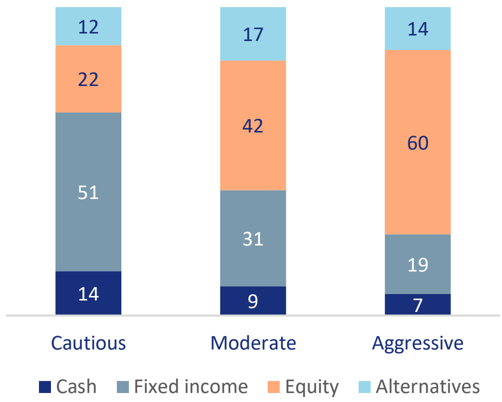
2023 started on a positive note, as a kind of normalization after the terrible 2022. This happened despite very gloomy predictions from many experts, including a few Wall Street superstars who expected a recession, falling stock markets and a range of financial troubles. At the end of a relatively positive Q1, financial troubles indeed started to hit, with balance-sheet tensions In US regional banks, turbulences in the UK pension system, and finally, a hurricane in Zurich which led to the emergency take-over of Credit Suisse by UBS. Volatility spiked, markets fell, but this was paradoxically the beginning of another positive episode: central banks provided clear and effective support to the financial system, including massive liquidity provision, which gave comfort to market participants. Appetite for risk came back.

The second quarter and the first part of the summer were buoyant, in what we had called a "Goldilocks Interlude": global growth was resilient, especially impressive in the US, while inflation did not seem to re-accelerate – the hikes from the Fed were not a surprise anymore, and the idea that the end was near supported markets, which, helped by a new tech paradigm around artificial intelligence, printed a year high in late July.

The following three months were much more difficult: a downgrade in the US sovereign credit rating preceded a not-so-friendly tone in Jackson Hole central bank symposium. Then, the September Fed meeting was a trauma: the institution drastically changed their projections in a hawkish way, crushing bond markets and risk appetite, especially as geopolitical tensions in the Middle East erupted in early October.

At this point in time, the YTD returns of our three profiles fell to low single digit (positive). But then, a marginally better than expected US CPI report triggered a powerful "rally of everything", as market participants were certainly not ready for good news. This only accelerated when the Fed adopted a much more friendly tone, in various speeches and finally in the press conference of their December meeting. The year ended with all asset classes in the green, and our three profiles delivered very positive returns of 9.6%, 12.8% and 15.3%, exceeding both our own expectations and most of our competitors' returns. This happened despite a constant, although modest, overweight of cash and safe bonds throughout 2023, which was not overly detrimental as we remained close to neutrality on equity, with a switch from emerging to developed markets in the second part of the year.

TACTICAL ASSET ALLOCATION: SIMPLIFIED POSITIONING

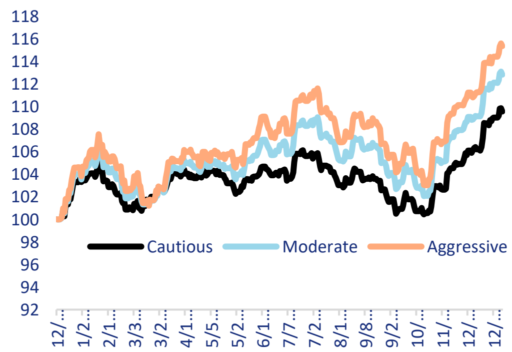


TAA – RELATIVE POSITIONING – MODERATE PROFILE

UW/N/OW: Underweight/Neutral/Overweight

	UW	N	OW
Cash			>>>>
DM Gov.			>>>
DM Credit			>
DM H. Yield	<<		
EM Debt	<<<		
DM Equity		=	
EM Equity		=	
Gold		=	
Hedge Funds	<<		
Real Estate	<		

TAA – 2023 INDICATIVE PERFORMANCE



Source: Bloomberg. CIO Office calculation based on TAA applied to market indices, net total return in USD.

Fixed Income Update

Last year was supposed to be the year of Fixed Income after the horrible 2022. In a sense, absolute return-wise, it wasn't bad, with US Treasuries returning +4.1% while High Yield bagged the top spot with a +14% return. But compared to other asset classes, it wasn't anything out of the ordinary. The CIO Office theme for the year was unpredictability, and the year justified the theme. The Treasury volatility index MOVE was continuously above 100 except for very short periods. The US 10-year treasury yield started the year at 3.9% and dropped to 3.3% before jumping to 5% in October, ending the year at around the same level where it had begun.

The US Treasury index was down -5.2% by the end of the year, and the return came only with the rally in treasuries in the last two months. There were three primary rationales behind the rally. Firstly, the US Treasury announced a lower-than-anticipated auction size on 31st October, triggering the upside. Secondly, momentum traders were caught on the wrong foot at the start of November and started unwinding positions, leading to further gains in the treasuries. Lastly, the weakening macro data, including lower inflation numbers and softening NFP figures combined with dovish FED speak, led to the soft landing scenario gaining traction as investors started to take into account the Fed pivot in 2024 after the 525 bps of rate hike cycle that ended in July 2023. From pricing in 2 rate cuts at the end of 31st October to pricing in 6 rate cuts, with the first cut starting in March 2024, the narrative has completely turned on its head. These expectations look a little stretched now.

Treasury volatility was not limited to the US alone. The placid corners of JGBs were comparatively more volatile, as there were talks of BoJ finally doing away with the easy monetary policy. Governor Ueda, however, has been very cautious, walking a fine line between inflation and growth, and he can't be indeed blamed. BoJ had started to move the trading range of the 10-year JGBs up since early 2023, and investors expect sometime in 2024, the central bank will remove yield curve control as well as do away with the negative interest rate regime.

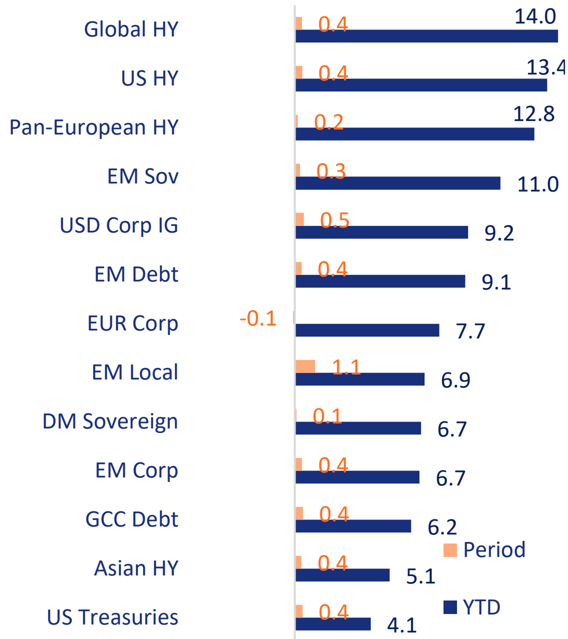
Coming to credit both IG and EM credit were down by 1.5% till October. At the end of October, IG yield was in the top 1% over the last decade and presented ample opportunity for investors to lock in yields. The rally in the Treasury and spread compression drove returns in the credit indices. High yield was the best performer as spreads tightened by more than 110 bps. IG and EM Debt spread compressed by 30 and 45 bps roughly. Overall, credit as an asset class looks rich. Current spreads are below 20-year medians in all the segments.

It was a robust year for GCC primary issuance as the volume at $63.6 Bn in 2023 was almost double that of 2022. The majority of the issuance was from financial institutions, as HY sovereigns from the region mostly stayed out of the market. The holding period return of the bonds issued last year from the region generated an average return of around 4.5% from the issue date. As China issuance gained a backseat, GCC exposure in the EM index increased to around 21% from 16.7% in 2022, cementing its position as the second largest constituent post-Asia.

FIXED INCOME KEY CONVICTIONS (2023)

DEVELOPED MARKETS
OW Quality corporates
OW Government Bonds
UW High Yield
EMERGING MARKETS
Overall UW EM Debt
Favor quality and selectivity
OW Selectively Asia,

FIXED INCOME SUB ASSET CLASS RETURNS (YTD, LAST WEEK)



Source: Bloomberg

Equity Update

The 2023 special: a volatile year ended with global equities up 23%, with big tech leading returns with a focus from investors on the potential use of generative AI and data in Industry. After 3 months of negative returns for global equities, November and December returns were respectively 9% and 5%, with a record nine weeks of positivity. Though many laggards finally performed such as real estate and regional banks, leadership stayed with tech, the US, Japan, India and the Dubai equity indices. The magnificent 7 tech stocks were up 112% in 2023 and the global tech sector up over 50%, but it was not that narrow a rally, as all global regions barring China ended the year up, as did all global sectors. In local currency terms, Japan was the best performing region in 2023, with the Nikkei +31%, and in USD the Dubai Index stood out at +28%. Many indices made new highs, India's Sensex, many tech sub sectors such the SOXX semiconductor Index, and the S&P 500 is almost back to its previous high.

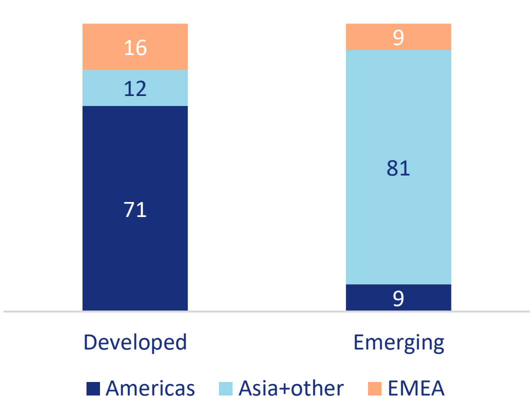
What worked for us in 2023 is the almost year long US overweight within DM and an on and off Japan overweight. What worked in EM, is the India tactical and strategic overweight, the UAE overweight, till October when we went neutral when the Israel Hamas conflict started. We have stuck to a neutral positioning for China and were not tempted by the low valuations. Thematically we had advocated investing in tech, healthcare with a focus on AI (including at the beginning of this year in platforms, networks and applications). The AI focus worked but broader healthcare, except obesity drug manufacturers took a backseat.

As expected, the DM Central bank pivot worked in favor of developed market performance +24% in 2023, with EM posting lower returns, +10%. Globally inflation is lower and while DM rate cuts are still some time away, with no further hikes expected from the Fed, ECB and BOE; sovereign yields ticking down have been positive for sentiment. However, a conundrum with the US 10 year Treasury yield still at a high level, though lower by 20% from its peak of 5%; all about growth in 2023.

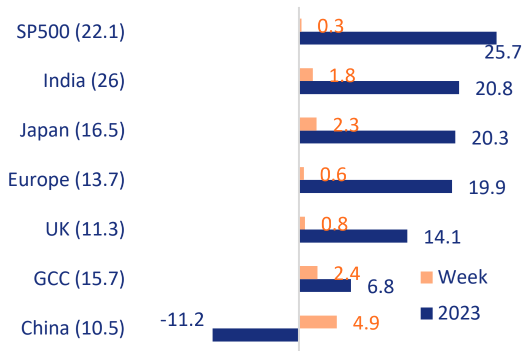
Equity indices in most major regions up over 15% in 2023, and within DM equities the US leading but Europe and Japan also posting strong returns. The S&P 500 ended 2023 +26% and the Nasdaq +45%. With SME's/small caps facing higher interest costs, the Russell 2000, while rallying, is still lagging large cap US indices. In EM, most regions posted strong returns and India +20% for the MSCI India (USD) and the UAE saw a strong performance from Dubai but not the Abu Dhabi Index which has already more than doubled in the past three years. China equities ended down for 2023, with insufficient stimulus, real estate woes and consumer activity not growing.

Our next weekly will give our positioning for 2024, as we look to DM Central banks cutting rates, already lower sovereign yields and a weaker USD, however relatively high DM and India valuations. We would watch earnings and corporate guidance for direction.

EQUITY RECOMMENDED REGIONAL POSITIONING

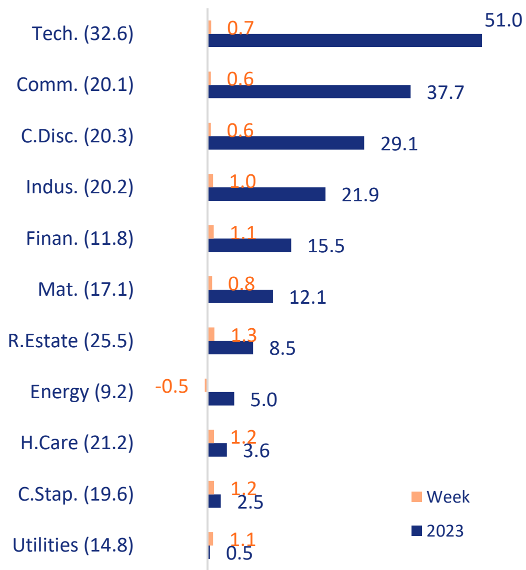


MAJOR INDICES PERFORMANCE (TR, US$) AND 2023PE



Source: Bloomberg consensus. MSCI Indices unless specified.

GLOBAL SECTOR PERFORMANCE (TR, US$) AND 2023PE



Source: Bloomberg consensus. MSCI All Country World sectors US$.

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