Within US equity sectors, CIO remains Most Preferred on industrials and technology, and Least Preferred on real estate and consumer discretionary. (UBS)

Cooling data shifts expectations

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Growth and inflation data have continued to soften. July employment data was weaker than expected, including an annual unemployment rate of 4.3%, up from 3.4% in May 2023.

This rise triggered concerns of further economic weakness ahead and caused markets to price additional rate cuts. At the time of writing, markets are pricing more than 100bps of cuts before year-end, up from 36bps at the start of July.

While recession risk has increased owing to weakness in the labor market, we maintain our expectation for a macro soft landing. We believe recent fears are overdone for a number of reasons:

1. The latest jobs numbers likely had a one-off negative impact owing to Hurricane Beryl.
2. While unemployment has risen, we view this more as a function of too much labor supply, rather than weaker labor demand.
3. Corporate profit margins remain solid, alongside consumer spending and household balance sheets.
4. Recent data has improved the Fed's confidence that inflation is headed sustainably back toward the 2% target, allowing them to focus on supporting the labor market more forcefully.

With our macro outlook for a soft landing, we keep bonds as Most Preferred and stay neutral on equities. We expect 100bps of cuts before year-end, so we advise investors to **position for lower rates**. As rates continue to decline, cash and money market funds will offer lower yields, so investors need to manage their liquidity more actively. We prefer higher-quality fixed income versus riskier credit and see value in IG corps., Agency MBS, CMBS, municipals, and sustainable bonds.

Beyond fixed income, we believe investors should **seek quality growth** throughout their portfolio. Recent earnings growth has been largely driven by firms with competitive advantages and exposure to structural drivers that enable them to grow and reinvest earnings. Within US equity sectors, we remain Most Preferred on industrials and technology, and Least Preferred on real estate and consumer discretionary.

While the US tech sector has grown significantly over the past year, we remain Most Preferred. With AI representing a key driver of growth, we see upside for the sector in both the short and long term. It is critical for investors to **seize the AI opportunity**, as we expect AI to be a key driver of market returns over the coming years.

Looking beyond public markets, we continue to advise investors to **diversify with alternatives**. Our future should see significant investments in realms such as health care, digitalization, and energy efficiency. But already-high government debt levels suggest public spending for innovative solutions will be constrained. Private market managers that can provide debt or equity capital at different company lifecycle stages will have a key role to play. And with the majority of firms in the US now privately held, accessing private markets is essential to achieve enhanced portfolio diversification and improve longer-term risk-adjusted returns.

Lastly, we recommend investors **prepare for US elections**. As we near the election we expect increased volatility across markets. For investors concerned about protecting their portfolio from election-related volatility, we recommend hedging strategies like gold and structured solutions with capital preservation features. We advise against selling risk assets ahead of the election while waiting for the outcome, and suggest investors express their political preferences at the ballot box, not in their portfolios.

Main contributors: Jason Draho, Michael Gourd

Original report - **Yield & Income: Cross asset ideas for yield , 8 August 2024.**