Outlook

MIDYEAR ISSUE JUNE 2023

Long-term perspective on markets and economies

The new reality for investors

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As we reach the midpoint of 2023, it's clear we are facing tremendous uncertainty and change. We are moving through a period of transition in the global economy, the financial markets and individual sectors. What had been a binary market — a market that was either/or — is now more balanced.

Previously, you could focus on a handful of large internet-related companies and disregard everything else. You could borrow at nearly zero percent and not worry about the consequences of free money, the threat of inflation, or the possibility that central banks might raise interest rates. Times have changed.

From an investor's point of view, that's good news. The market is no longer going in just one direction and that presents a more compelling, target-rich environment. The opportunity set has grown to include U.S. companies and international companies, growth stocks and value stocks, the technology sector and health care, industrials and energy, short-term and long-term bonds, Treasuries and corporates. We're living in a world where there are both cyclical and secular opportunities for investors willing to do their homework.

It's important to note, we are also searching for opportunities where the baby has been thrown out with the bathwater — that is, companies left humbled by the selloff of 2022, but still worth our attention because business models remain intact, earnings are holding up and the potential for stock price appreciation remains strong. So far this year we've seen companies in the tech and consumer sectors demonstrate the ability to bounce back impressively.

The risks have also grown. Not just market and economic, but policy risks. Where does the U.S. stand in relation to China? Will the war in Ukraine escalate? How will regulators respond to a crisis of confidence in the banking sector? These are all issues to be considered as we evaluate potential investments. And we must be willing to embrace short-term discomfort for long-term benefit.

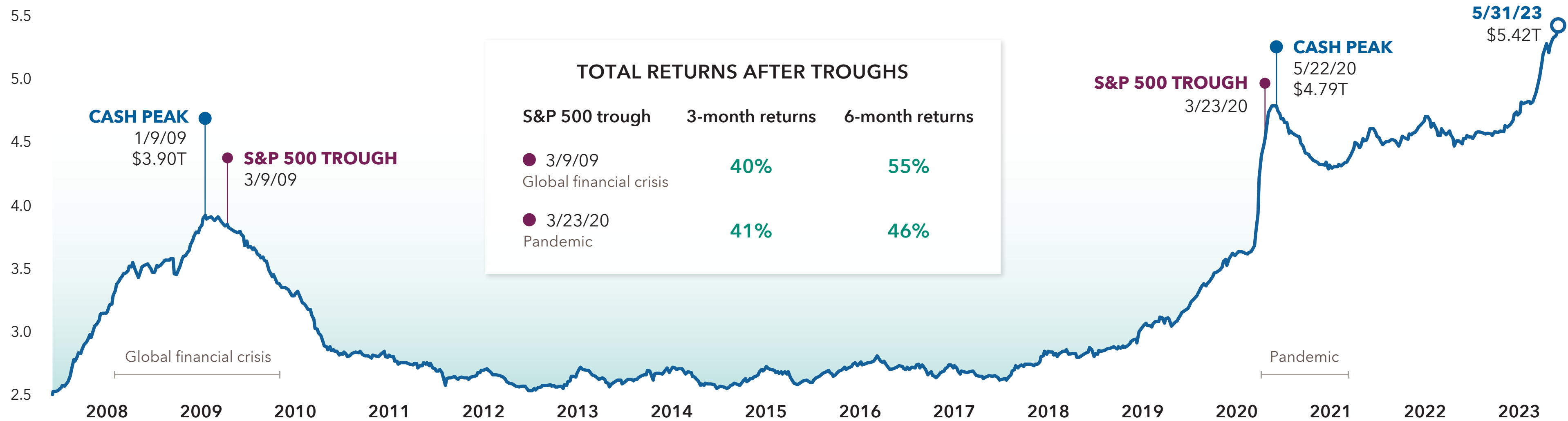
The reality is, it's a great time to be an active investor. It's more important than ever to look for opportunities on a global scale, but also to keep an eye on growing risks in the markets, the economy and the world. Given the uncertainty, there's a lot of cash on the sidelines these days. Now may be the time to consider putting it to work.

Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.

A mountain of cash on the sidelines can be a bullish signal

Investors’ flight to cash has surpassed that of the pandemic and financial crisis

ICI Money Market Fund Assets (USD trillions)



TOTAL RETURNS AFTER TROUGHS

S&P 500 trough	3-month returns	6-month returns
3/9/09 Global financial crisis	40%	55%
3/23/20 Pandemic	41%	46%

Investors have anointed cash as king, shifting assets out of stock and bond investments and driving money market totals to a record $5.4 trillion as of May 31, 2023.

This flight to cash and cash alternatives (such as money market funds and short-term Treasuries) is understandable following last year’s tandem decline of stocks and bonds in the face of rising interest rates, inflation and slowing economic growth. Many investors moved deposits from banks to money markets amid ongoing volatility and relatively high yields on cash instruments.

But conditions have shifted thus far in 2023, and long-term investors may want to rethink their approach. Levels of cash alternatives peaked near two recent market troughs. During the global financial crisis, for example, money market fund assets peaked two months before the S&P 500 Index reached a bottom on March 9, 2009. The stock market recorded a 40% return over the subsequent three months and a 55% return over the following six months. Similarly, during the pandemic, money market fund levels reached a high weeks after the S&P 500 reached its trough in March 2020.

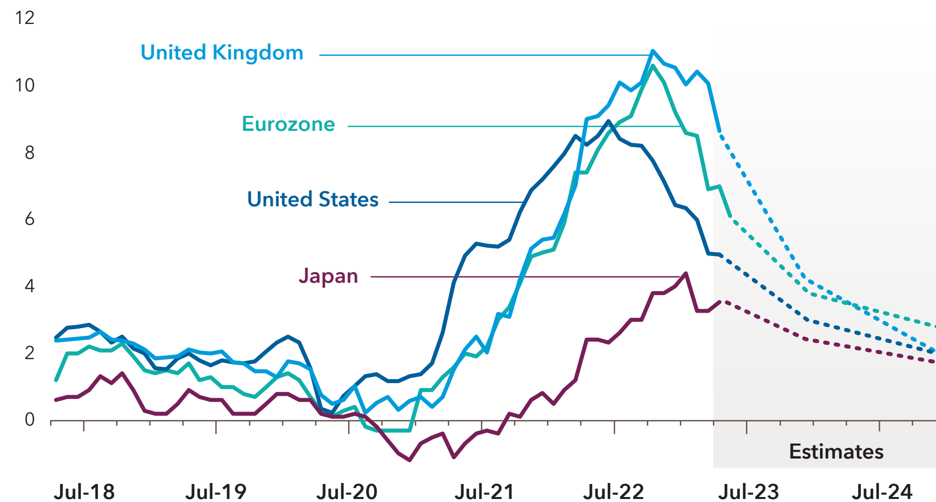
After the painful losses of 2022, more risk averse investors might consider allocating some cash to dividend-paying stocks, which provide income and capital appreciation potential, and select short- and intermediate-term bonds, which have been offering higher yields than in 2022.

SOURCES: Capital Group, Bloomberg Index Services Ltd., Investment Company Institute (ICI), Standard & Poor’s. As of May 31, 2023. In the chart, “cash peak” refers to peak money market fund assets. Unlike cash, which may be insured or guaranteed by the Federal Deposit Insurance Corporation, dividend-paying stocks, short- and intermediate-term bonds are not guaranteed and are subject to loss. Past results are not predictive of results in future periods.

Inflation has eased as rate-hiking cycle nears an end

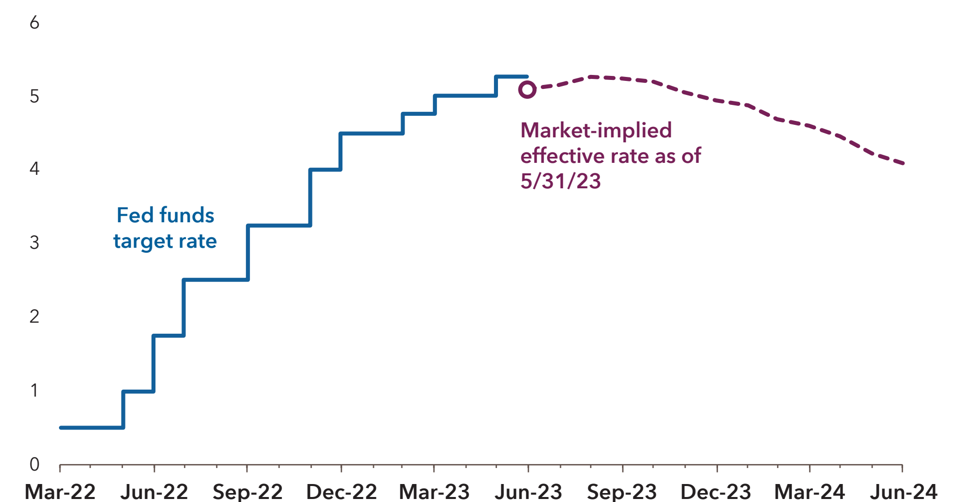
Inflation, still elevated, is less fierce

Annual consumer price index (%)



Markets expect a decline in rates over the next year

Federal funds rate – Actual and market implied (%)



It may not feel like it at the grocery store, but inflation is on a downward trajectory in the U.S., Europe and many other markets. That's largely due to lower energy prices, fewer supply chain disruptions and a steady series of interest rate hikes by central banks.

Interest rate-sensitive industries such as housing are already feeling the effects, with home prices falling in some formerly hot markets. Inflation still remains well above the U.S. Federal Reserve's 2% target, but monetary policy often works with long lags, so the full impact of rate hikes should spread through the rest of the economy over time.

The recent U.S. banking turmoil could also help slow economic growth as some banks may become more cautious and reduce their lending activities. Taken together, these factors have significantly changed the interest rate outlook.

"We knew there would be consequences to one of the most aggressive tightening campaigns in history," says fixed income portfolio manager Pramod Atluri. "The dislocations we are seeing in the financial markets signal a painful new phase for the Fed. It has clearly exposed some vulnerabilities and, as a result, I believe we are nearing the end of this rate-hiking cycle."

SOURCES FOR LEFT CHART: Capital Group, FactSet, Bureau of Labor Statistics, Eurostat, UK Office for National Statistics, Japanese Statistics Bureau & Statistics Center, International Monetary Fund. Data as of June 5, 2023. Consumer price indexes for each region provide a measure of the average change over time in the prices paid for a basket of consumer goods and services. SOURCES FOR RIGHT CHART: Capital Group, Bloomberg Index Services Ltd., Refinitiv Datastream, U.S. Federal Reserve. Fed funds target rate reflects the upper bound of the Federal Open Markets Committee's (FOMC) target range for overnight lending among U.S. banks. As of May 31, 2023.

Recession is likely, but the recovery could be stronger than expected

This may be the most widely anticipated recession in history. The question is: What comes after?

"When an insight is widely held, such as the likelihood of recession before the end of the year, it may already be priced into the market," U.S. economist Jared Franz says. "Investors may be better served by preparing for what I expect will be a stronger than usual recovery."

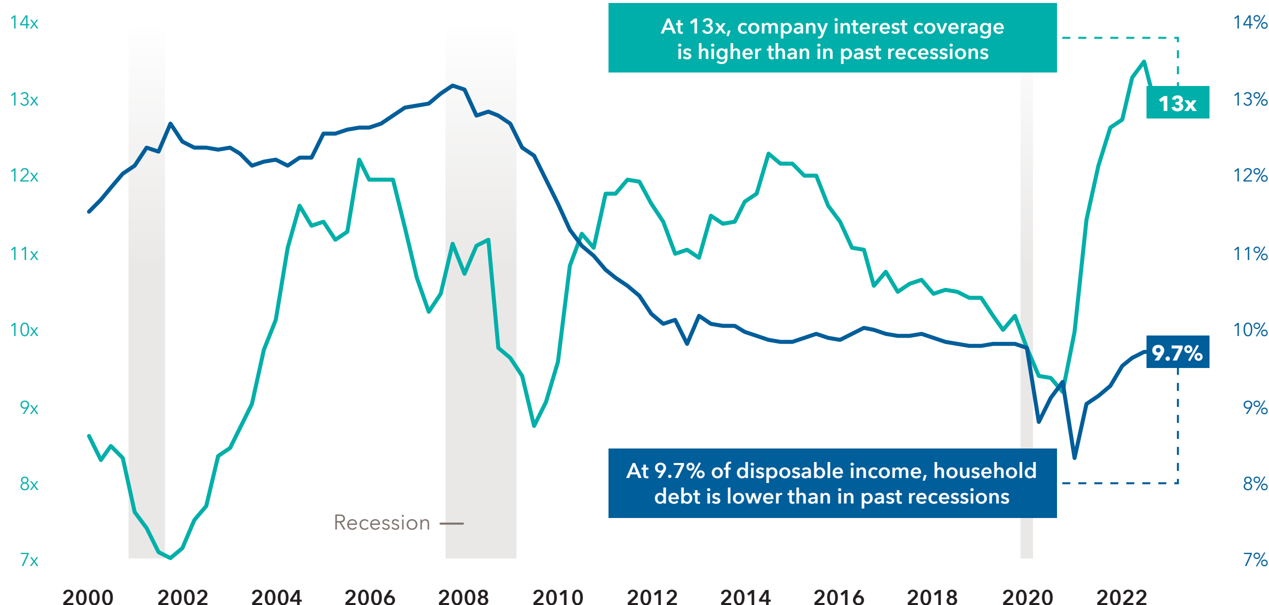
Franz cites three reasons the next recovery could be more robust than prior cycles. First, companies are expecting economic weakness and taking action, cleaning up inventories and balance sheets.

Second, the U.S. consumer is in relatively good shape. Consumer debt is low relative to levels during the global financial crisis and other more typical recessions.

Third, Franz expects moderating inflation to support consumer strength. "While it will take some time for the Federal Reserve to get inflation down to its 2.0% target, I believe it will be contained near 3.0%, which can feel like a real wage boost," Franz says.

Strong consumer spending could boost a range of industries, including travel and leisure. What's more, some signs suggest the housing market, which has already been in recession, may be recovering, providing a tailwind for spending on construction and durable goods such as household appliances.

Consumers put their houses in order as companies cleaned up balance sheets



SOURCES: Capital Group, Federal Reserve Bank of St. Louis, Morgan Stanley, National Bureau of Economic Research. Interest coverage reflects the ratio between earnings before interest and taxes (EBIT) and interest expense. Shaded bars represent U.S. recessions as defined by the National Bureau of Economic Research. Data as of December 31, 2022.

Now may be the time to move out of cash

Market volatility hastened a flight to cash for many investors. While understandable, this response effectively placed investment objectives on hold and relinquished long-term return potential.

"I believe many investors have become disbelievers in balanced strategies at the wrong time. I am confident that, going forward, balanced portfolios – whether they are a 60/40 split or 65/35 – may continue to be a successful approach," says portfolio manager Hilda Applbaum.

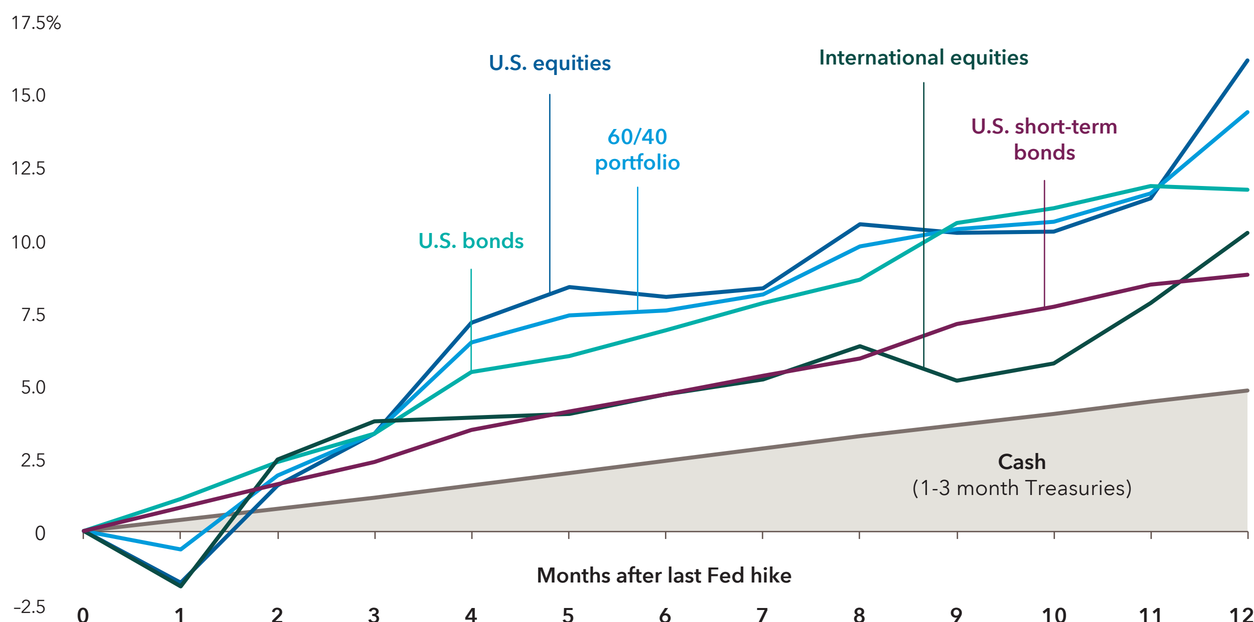
The 60% equities and 40% fixed income portfolio aims to generate attractive returns while reducing risk. Investors were hit hard in 2022 as the Federal Reserve started raising interest rates and both stocks and bonds posted losses.

With inflation inching toward normal and the Fed pausing interest rate hikes, now is an opportune time for investors to consider moving back into a balanced strategy. Valuations across a range of stocks are more attractive, and bonds are now offering more income and higher return potential.

Over the last four hiking cycles since 1995, investing after the last Fed rate increase has generated strong returns for both stocks and bonds. What's more, the best returns occurred in the first 12 months after the last rate hike.

Stocks and bonds have outpaced cash after a Fed hiking cycle

Average returns following the last Fed hike – Prior four hiking cycles



SOURCES: Capital Group, Bloomberg Index Services Ltd., MSCI, Refinitiv Datastream, Standard & Poor's. Returns reflect the average cumulative return over each of the first 12 months immediately following the last increase in the target U.S. federal funds rate ("last Fed hike") over the prior four hiking cycles. The specific start months for the periods included in the average calculations are: February 1995, May 2000, June 2006, and December 2018. U.S. bonds are represented by the total return of the Bloomberg U.S. Aggregate Index; U.S. equities are represented by the total return for the S&P 500 Index; the 60/40 portfolio is represented as the weighted average return using 60% of the total return for the S&P 500 Index and 40% of the total return in U.S. dollars for the Bloomberg U.S. Aggregate Index, with no rebalancing for the first 12 months. International equities are represented by the total return in U.S. dollars for the MSCI EAFE Index; U.S. short-term bonds are represented by the total return for the Bloomberg 1–3 Year U.S. Government/Credit Index; cash is represented by change in the Bloomberg U.S. Treasury Bill 1–3 Months Index. As of May 31, 2023. Past results are not predictive of results in future periods.

A stronger long-range investment outlook across asset classes

After a tumultuous 2022, the future appears brighter across a range of asset classes. So, investors who fled to cash may now want to revisit their asset allocation.

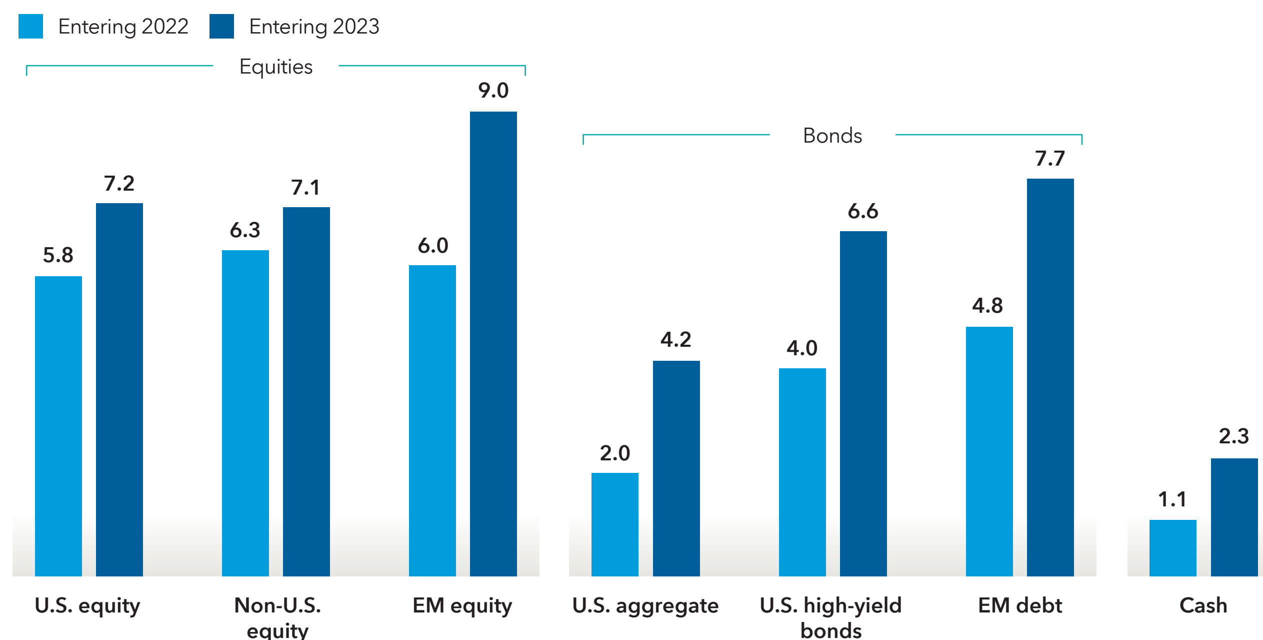
"Entering 2023, our long-term capital markets return assumptions show a more appealing investment environment," says solutions portfolio manager Michelle Black. "We see better corporate fundamentals and a currency tailwind more than offsetting potentially slower global economic growth, most notably in China."

Following the sharp decline in U.S. equities, valuations are more reasonable. "We are also optimistic on non-U.S. equities, which should be propelled by a combination of higher dividend yields, multiple expansion and a weaker dollar," notes Black.

U.S. fixed income returns should improve in large part from a higher starting point in yields, but also may benefit from price appreciation and declining yields. From a total return perspective, the solutions team finds emerging markets debt to be attractive. Yields are higher than in other areas of fixed income, and the U.S. dollar could be a tailwind for local currency debt returns.

Many asset classes offer better long-term potential than cash

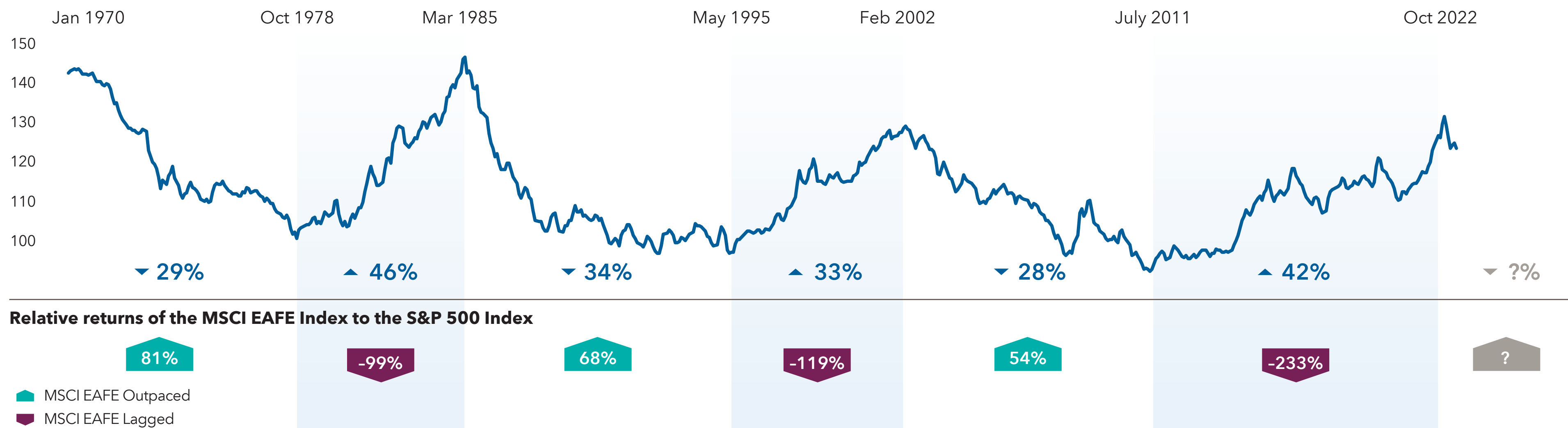
Capital Group's capital market assumptions – Forward 20-year annualized expected returns across asset classes (%)



SOURCE: Capital Group. All asset classes reflect asset class proxy benchmarks used in Capital Market Assumptions (CMAs). All assumptions are for market asset classes only and are reviewed at least annually. These figures represent the views of a small group of investment professionals based on their individual research and are approved by the Capital Market Assumptions Oversight Committee. They should not be interpreted as the view of Capital Group as a whole. As Capital Group employs The Capital System™, the views of other individual analysts and portfolio managers may differ from those presented here. They are provided for informational purposes only and are not intended to provide any assurance or promise of actual returns. They reflect long-term projections of asset class returns and are based on the respective benchmark indices, or other proxies, and therefore do not include any outperformance gain or loss that may result from active portfolio management. Note that the actual results will be affected by any adjustments to the mix of asset classes. All market forecasts are subject to a wide margin of error. EM = emerging markets. EM debt is a blend of 50% emerging markets debt denominated in U.S. dollars and 50% emerging markets debt denominated in domestic currency. For a full list of benchmarks used, please see the disclosures page.

A declining dollar may boost international stocks

Dollar down cycle could be needed catalyst for investing abroad



U.S. dollar dominance appears to be on the ropes after an 11-year bull run. While that has implications for U.S. assets, a continuing downward trend would be welcome news for investors in international stocks and bonds, where returns have been eroded in recent years by currency translation effects.

Markets outside the U.S. are already showing signs of a currency tailwind. European stocks, as represented by the MSCI Europe Index, have generated strong returns as the dollar has lost ground against the euro, the yen and most other currencies. Since reaching a peak last October, the dollar has declined about 6%, as measured by the J.P. Morgan USD Real Effective Exchange Rate Index.

"The dollar tends to move in big cycles," explains Andrew Cormack, a portfolio manager with Capital World Bond Fund®, "and the strong dollar cycle we saw over the past decade was a bit long in the tooth."

While the dollar may yet see intermittent periods of strength due to its perceived status as a safe-haven asset, Cormack believes the long-term trajectory is lower. That's due to several factors, including a soft U.S. economy, a weak housing market and indications that the Fed may be nearing the end of its rate-hiking cycle.

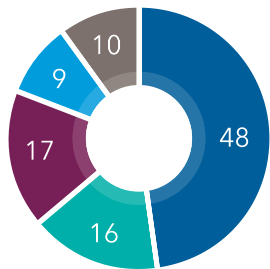
SOURCES: Capital Group, J.P. Morgan, MSCI, Refinitiv Datastream, Standard & Poor's. Relative returns and change in the USD index are measured on a cumulative total returns basis in USD. The U.S. dollar index reflects J.P. Morgan's USD Real Broad Effective Exchange Rate Index, which is re-based to 100 as of 2010. As of May 31, 2023. Past results are not predictive of results in future periods.

Global champions in Europe are navigating the new reality

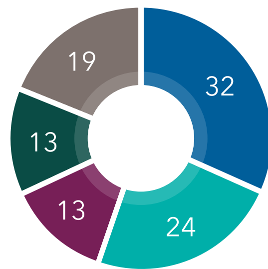
Leading European companies are operating in markets around the world

Revenue by region across top MSCI Europe Index constituents (%)

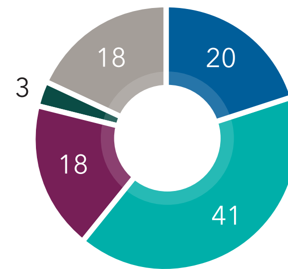
United States · Europe · Asia Pacific · Latin America · Africa & Middle East · Others



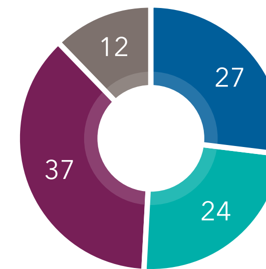
Novo Nordisk
(Denmark)



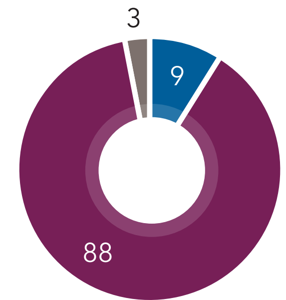
Nestlé S.A.
(Switzerland)



Airbus
(France)



LVMH
(France)



ASML
(Netherlands)

Europe's economy has proved resilient despite the war in Ukraine, high inflation and rising interest rates. Consumers have continued to spend, travel and tourism have picked up, and European companies are benefiting from a combination of modest domestic growth and international opportunities, including the reopening of China's economy.

In fact, some of Europe's most successful multinational companies have been highly adept at tapping into external revenue streams from Asia to Latin America to the United States.

For example, Novo Nordisk's weight-loss drug Wegovy has seen enormous worldwide demand, prompting the Denmark-based company to nearly double its sales guidance compared to 2019.

"In Europe, select companies can thrive even in a tough economic environment," says equity portfolio manager Lara Pellini, stressing the importance of bottom-up, fundamental research.

In the luxury goods industry, many of the world's elite brands are based in Europe, but their customers live all over the world. French luxury giant LVMH reported record-high revenue of $86 billion for 2022, driven largely by strong demand from the U.S. and Japan.

"One reason these companies have the potential to outpace domestic peers is because they are subject to global competitive forces, which can spur innovation," Pellini adds. "The expertise they develop is difficult to replicate."

SOURCES: Capital Group, FactSet. Companies above are among the top 25 largest constituents within the MSCI Europe Index by market cap across a range of industries. Revenue by region is estimated by FactSet based on most recently reported figures. Data as of May 31, 2023.

New growth opportunities emerge

Big Tech is back. Many of the names that led the last bull market are leading a nascent recovery, including Amazon, Apple, Microsoft, Meta and Nvidia – the top five contributors to the rise of the S&P 500 Index this year, as of May 31.

Whether this advance will continue remains an open question, but so far this year the tech-heavy Nasdaq Composite Index has gained about double the return of the S&P.

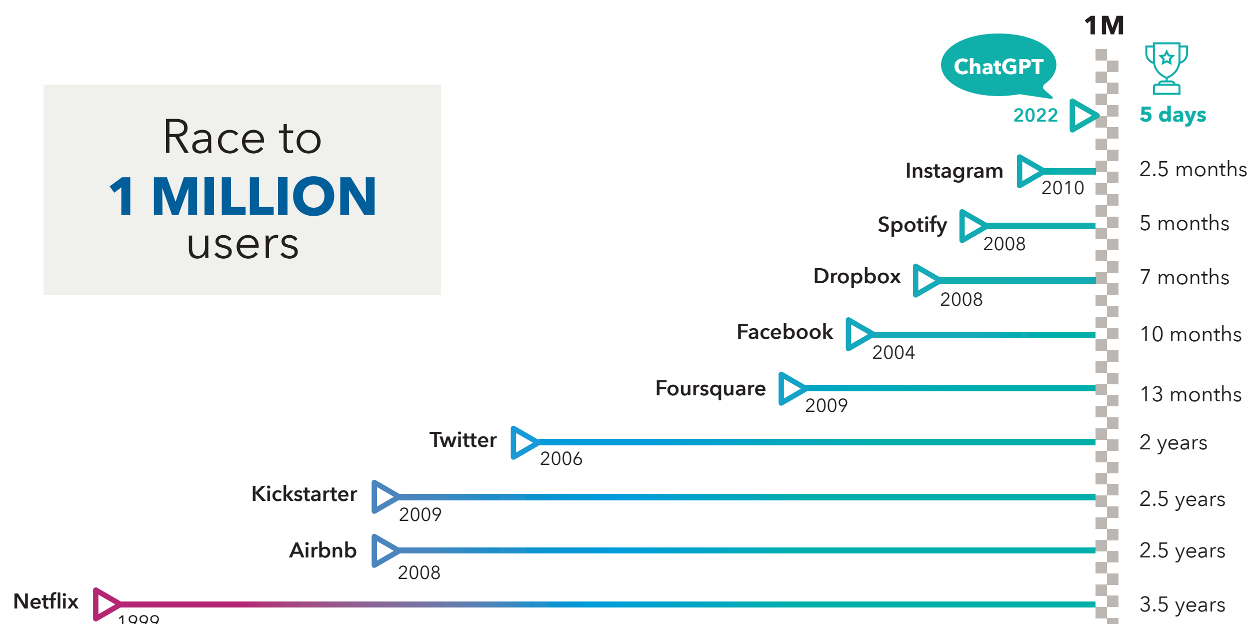
The rise of artificial intelligence (AI) systems, such as ChatGPT, is one of the factors driving enthusiasm for the tech sector. Earlier this year, ChatGPT, co-owned by Microsoft and OpenAI, became the fastest growing consumer app in history.

The difference today is that tech stocks are no longer the only game in town. Over the past year, market opportunities have broadened to include energy, health care and industrials, as well as traditional value-oriented and dividend-paying stocks.

"There are many long-term secular themes in sectors beyond technology," says Jody Jonsson, a portfolio manager with New Perspective Fund®. "For instance, we are witnessing an incredible age of discovery in health care. It's perhaps the most fertile environment I've seen in my career. In the energy sector, I'm excited about the transition to cleaner, more efficient energy systems. It's just an amazing time to be an active investor."

The adoption rate of new technologies is accelerating

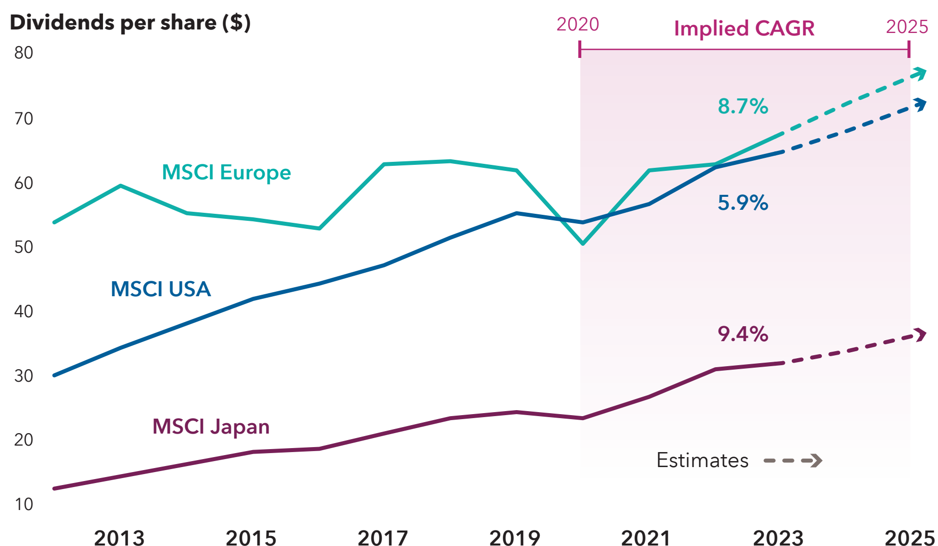
Time for selected online services to reach one million users



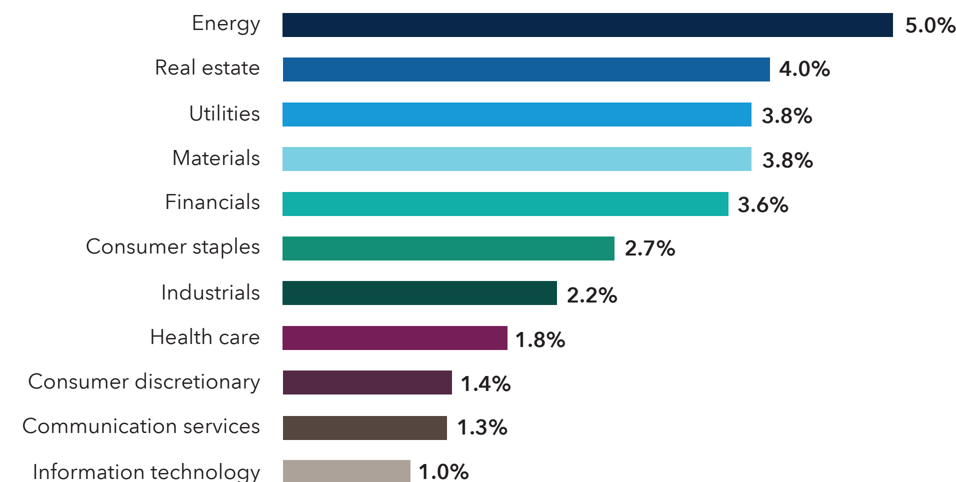
SOURCE: Statista. As of May 31, 2023. Kickstarter refers to number of backers. Airbnb refers to number of nights booked. Foursquare and Instagram refer to number of downloads.

Dividends have reached new heights

Dividends projected to grow through 2025



Attractive yields can be found across a range of sectors



When growth slows and market volatility rises, the role of dividends takes on greater prominence in investment portfolios.

Since the start of 2022, dividend contributions to total returns have increased, as have total payments to investors. Global companies distributed more than $2.0 trillion in dividend payments for the 12 months ended May 31, 2023, an 12.3% increase from the previous 12 months.

"I expect dividends will be of greater significance to investors this year and beyond," equity portfolio manager Caroline Randall says. "But in a period of relative instability and rising debt costs, it is essential to focus on the quality of dividend payers."

For Randall, that means closely scrutinizing company balance sheets, credit ratings and interest costs. This has guided her to select companies across pharmaceutical and medical device firms, utilities, energy producers and some industrials.

"It is critical to track what management says about dividends and equally critical to follow what they do," notes Randall. "If you are going to rely more on dividends, you must be confident the companies will pay them. That's where we can add value as active managers."

For example, Abbott Laboratories has increased its dividend payout for 50 consecutive years. European beverage maker Diageo has done so for 20 straight years.

SOURCE FOR LEFT CHART: FactSet. Data for 2023-2025 is based on consensus estimates as of May 31, 2023. CAGR = compound annualized growth rate. SOURCES FOR RIGHT CHART: Capital Group, MSCI, RIMES. Data as of May 31, 2023. Past results are not predictive of results in future periods.

Wage growth is finally coming to Japan amid higher inflation

There's no question Japan has been a tough place to invest over the past decade, as an aging population, sluggish economic growth and stagnant wages have plagued the world's third-largest economy. Things could be changing, however, as a post-pandemic inflation surge has forced Japanese companies to act.

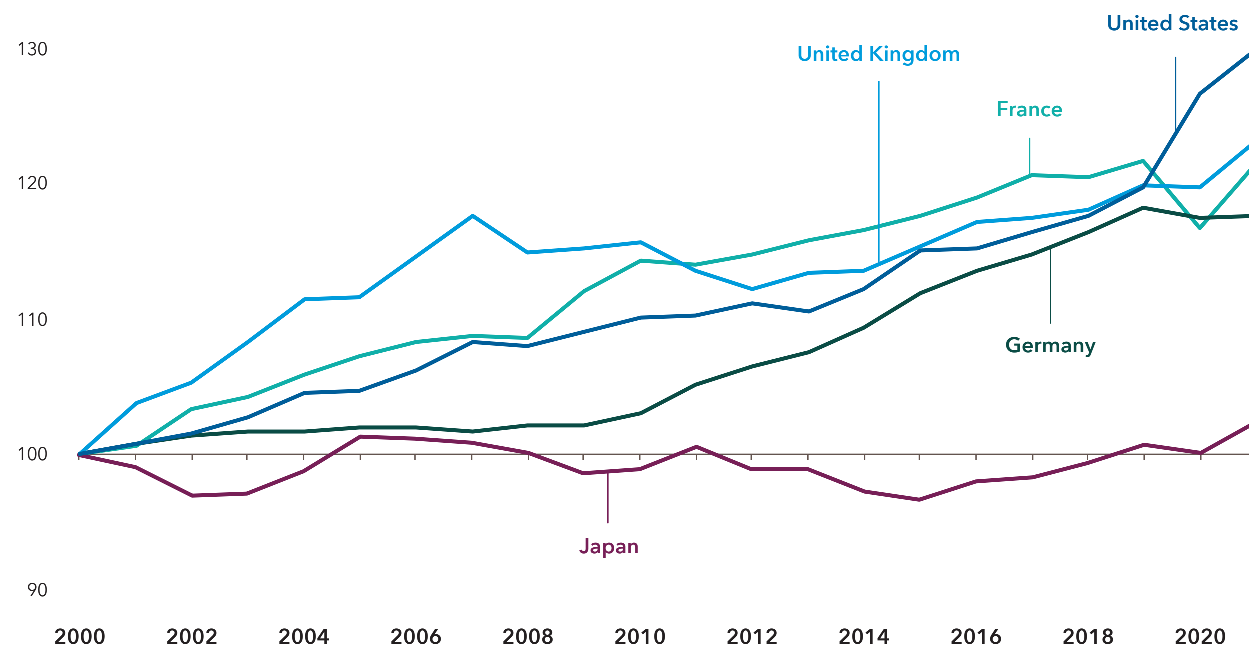
In a nation where pay hikes are rare, nearly 30% of Japan's industry leading companies have announced increases this year. For example: Nintendo and Honda announced increases of 10% and 5%, respectively. Toyota agreed to boost employee bonuses by the equivalent of more than six months' salary.

"Hefty pay increases will be a headwind for corporate profits," says Capital Group economist Anne Vandenabeele, "but profit margins are at multi-decade highs, and Japanese stocks are rallying this year, so many companies can afford to share the wealth."

Japan's government officials and labor unions agree. They've been pushing for across-the-board pay increases of around 3.8% this year, roughly matching core inflation, which has risen to a 41-year high.

Companies' willingness to grant wage hikes is well correlated with their expectations for demand growth three years out, Vandenabeele says. "This trend could bode well for consumer spending in the future."

Japan is looking to catch up with global peers in wage growth



SOURCES: Capital Group, Organisation for Economic Co-operation and Development (OECD). Average wage growth reflects constant prices at 2021 U.S. dollar purchasing power parity (PPP), indexed to 100 as of 2000. Figures through 2021 reflect most recently available data as of May 31, 2023.

As China reopens, equity valuations are attractive but caution is warranted

No doubt when it comes to investing in China, there are clear challenges. Geopolitical tensions are elevated, medium- to long-term growth will likely moderate from the rate of prior decades and the property sector is mired in debt. That said, China has not relinquished its title as the world's second-largest economy, providing opportunities to selectively invest despite the risks.

"There are great entrepreneurs in China, and the large addressable markets have not disappeared despite geopolitical worries and the crackdown on private sector," says portfolio manager Chris Thomsen.

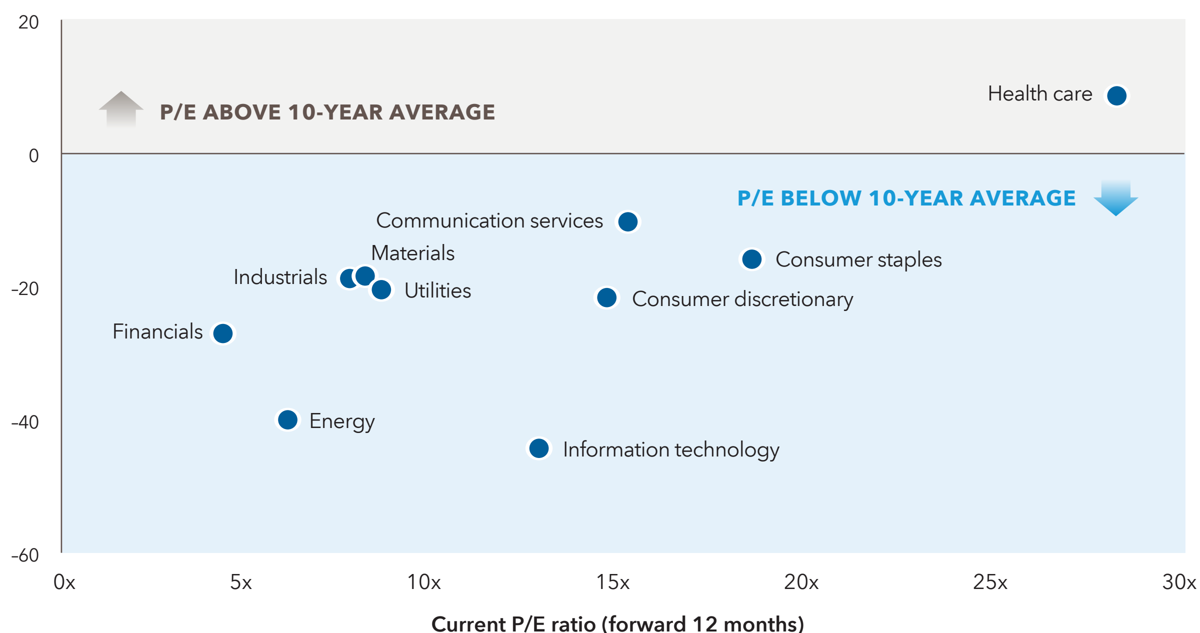
China's economy looks to be improving after the government lifted COVID restrictions in late 2022 and reprioritized growth. Airports are busy. Movie theaters and restaurants are packed. And Chinese tourists are flocking to their favorite Asian destinations.

Thomsen says both multinationals and domestic firms stand to benefit from the country's reopening. Luxury goods giant LVMH has seen demand in China surge. Starbucks and McDonald's are planning to open additional stores. Meanwhile, domestic consumer goods makers, hotels and Macau casino operators may potentially thrive as the economy recovers.

But caution is warranted. While valuations for Chinese equities remain depressed against their long-term averages, "it becomes a question of the risk premium you apply to stocks, which impacts the multiple you are willing to pay for them," Thomsen adds.

Valuations across several sectors are below historic averages

MSCI China Index – Price-to-earnings ratios vs. 10-year average (%)

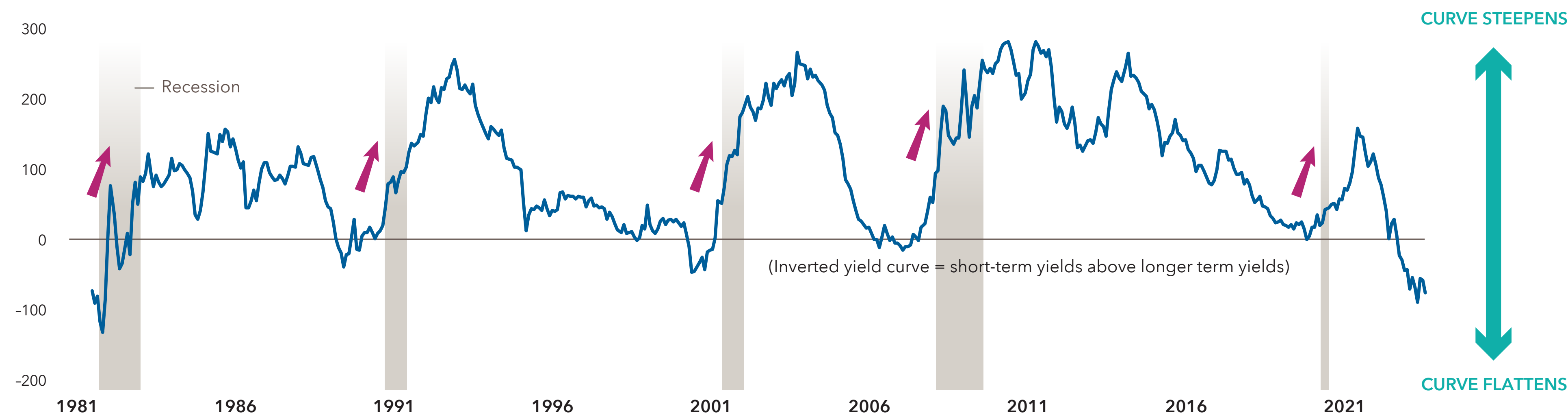


SOURCES: Capital Group, MSCI, RIMES. Forward price-to-earnings ratios reflect the current share price relative to the consensus estimate for earnings per share on a forward 12-month basis. Data as of May 31, 2023.

As Fed takes a pause, value can be found in rates market

A more balanced view amid risk of recession could present opportunities in yield curve positioning

Spread between two-year and 10-year Treasury yields (bps)



After 10 consecutive interest rate increases totaling 500 basis points, the Fed paused rate hikes in June.

"The Fed is confronting a lot at once: persistent inflation, a resilient labor market and stresses in the banking sector. Pausing gives them time to see how things play out, though I do think the risk of a recession is higher," says Tim Ng, portfolio manager.

Fed hikes have lifted yields across fixed income, with the Bloomberg U.S. Aggregate Index yielding 4.59% on May 31, 2023.

"Exposure to interest rates now may provide portfolios a meaningful return potential," according to portfolio manager Ritchie Tuazon. "It also offers a possible upside – and diversification – should the Fed cut rates to support growth, as bonds would experience price appreciation."

If the economy continues to weaken, short-term Treasury yields may drift lower, particularly if Fed rate cuts are more likely. Meanwhile, longer term Treasury yields could be more anchored or even rise. These movements would cause the yield curve to steepen from being so deeply inverted.

"We favor positioning portfolios that would benefit from a steepening of the Treasury yield curve. The position should work well in a slowing economy or outright recession and is compelling from a valuation perspective," adds Tuazon.

SOURCES: Capital Group, Bloomberg Index Services Ltd., National Bureau of Economic Research, Refinitiv Datastream. As of May 31, 2023.

Corporate bonds can likely weather an economic slowdown

A weaker economy equals weaker credit markets. That's been the traditional wisdom. But this cycle may be a little different.

Corporate bonds have come under some selling pressure in the wake of banking sector turmoil since financials hold a large place in the investment-grade (rated BBB/Baa and above) bond universe. But overall, the sector has held some ground, with yields hovering around 5% and spreads over Treasuries expanding to approximately 130 basis points. Credit markets could decline further if the economy slows materially and corporate profitability decreases.

However, according to portfolio manager Scott Sykes, two factors are helping to counteract this possibility in the current market environment. Corporations with investment-grade ratings generally have strong balance sheets with sufficient cash to fund their operating and expansion needs. Additionally, most corporate bonds are trading at a discount to their issuance price, which provides a valuation cushion as investors are likely to get fully paid when the debt comes due.

Current starting yields look compelling. Historically, when investment-grade bonds yielded in the range of 3.8% or higher, two-year forward returns averaged 6.5% or more.

Sector selection is also important, says portfolio manager Robert Caldwell. In a slowing economy, companies in non-cyclical areas such as pharmaceuticals and telecommunications tend to look more appealing than those in cyclical areas such as autos, metals and mining.

Higher starting yields have led to better returns for investment-grade bonds

SOURCES: Capital Group, Bloomberg Index Services Ltd. As of May 31, 2023. Average forward two-year returns are annualized, based on each quartile of starting yield to worst. Yield to worst is a measure of the lowest possible yield that can be received on a bond that fully operates within the terms of its contract without defaulting. Past results are not predictive of results in future periods.

Patience could reward investors in high-yield bonds

Owning high-yield bonds ahead of a potential recession might make some investors uneasy. But for those with a time horizon beyond one year, investing in bonds with current yields of around 8% has historically offered solid returns.

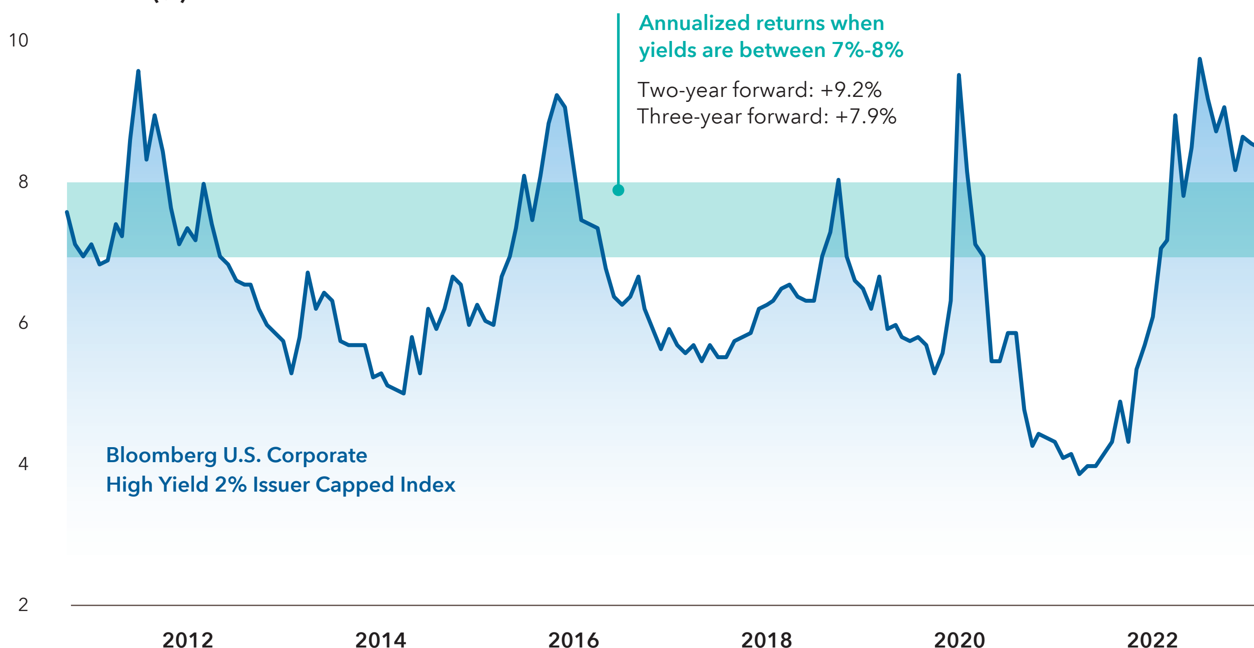
"You can't have financial conditions tighten substantially and not have repercussions in the real economy," says portfolio manager Tara Torrens, who expects a slowdown.

Fundamentals are especially important as corporate profitability comes under pressure in the face of rising costs and higher interest rates. "Fundamental credit analysis helps identify which companies can pay their debts," portfolio manager David Daigle adds. "For example, although oil prices often decline as growth slows, there are energy companies that can comfortably navigate a downturn."

The quality of the high-yield universe has improved, with nearly half the market carrying the highest rating (BB/Ba). One reason is that many companies with riskier financial profiles have opted to raise funds in the private credit and leveraged loan markets.

Taken altogether, defaults will likely increase but remain low relative to prior recessions – current valuations reflect this scenario. And while spreads could widen in a recession, investors waiting for better entry points may not see them given the improved credit profile of high yield.

Current yields have offered strong two- and three-year returns

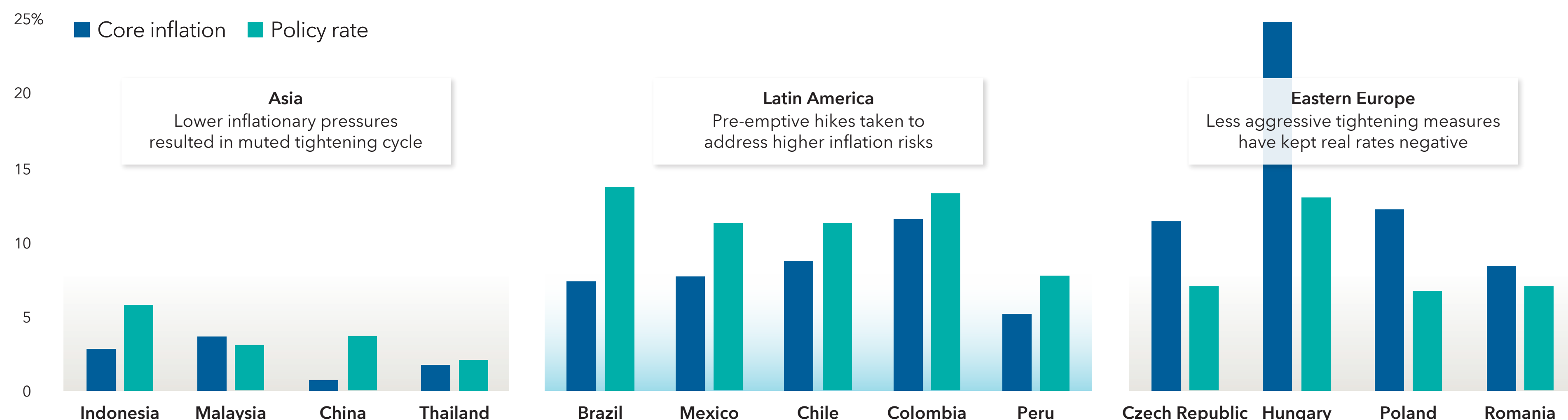


SOURCE: Bloomberg Index Services Ltd. As of May 31, 2023. Yield to worst is a measure of the lowest possible yield that can be received on a bond that fully operates within the terms of its contract without defaulting. The real economy refers to all non-financial elements of an economy. Lower rated bonds are subject to greater fluctuations in value and risk of loss of income and principal than higher rated bonds. Past results are not predictive of results in future periods.

Some emerging markets have benefited from attractive rates, moderating inflation

Countries across Latin America have been more aggressive in tackling inflation

Inflation and interest rates of select emerging market countries



Inflation is trending lower in many emerging markets, providing central banks the room to taper interest rates and provide monetary stimulus. Many developing economies have been ahead of the developed world, raising interest rates earlier and more aggressively to address inflation.

There is some regional divergence, with inflation lower in Asia, moderate in Latin America and high in Central and Eastern Europe.

Decent overall fundamentals, coupled with attractive nominal rates and positive real rates across many developing economies, indicate a reasonably constructive view of emerging market debt overall, according to portfolio manager Kirstie Spence.

That said, selectivity will be key given the divergence in policy and inflation dynamics across countries, as well as varying relative and absolute valuations across issuers. On balance, Spence favors a modest tilt toward local currency issuers compared to hard currency credits.

Spence sees potential value in Latin American local currency bonds given the combination of attractive nominal and positive real rates, moderate inflation, proactive behavior on the part of central banks and a reasonable growth outlook. "Central and Eastern Europe are still struggling to curb inflation – and real rates remain negative – but at some point I believe that region will potentially become more attractive," Spence says.

SOURCES: Capital Group, Bloomberg Index Services Ltd. Core inflation is represented by the year-over-year change in consumer price index (CPI) excluding food and energy across countries. Inflation rate as of May 2023 for Peru and April 2023 for all other regions. Policy rates as of June 5, 2023. Real interest rates reflect the true cost of funds to a borrower. Nominal interest rates equal the real interest rate plus the rate of inflation.

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There are risks associated with investing, including possible loss of principal.

Bond ratings, which typically range from AAA/Aaa (highest) to D (lowest), are assigned by credit rating agencies such as Standard & Poor's, Moody's and/or Fitch, as an indication of an issuer's creditworthiness. If agency ratings differ, the security will be considered to have received the highest of those ratings, consistent with the fund's investment policies.

The market indexes are unmanaged and, therefore, have no expenses. Investors cannot invest directly in an index.

Capital Market Assumptions (CMAs) benchmarks: U.S. equity = MSCI USA; non-U.S. equity = MSCI World ex USA; EM equity = MSCI Emerging Markets; U.S. aggregate = Bloomberg U.S. Aggregate Index; U.S. high-yield bonds = Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index; EM debt = 50% J.P. Morgan Emerging Markets Bond Index (EMBI) Global Diversified / 50% J.P. Morgan Government Bond Index – Emerging Markets Global Diversified; cash = FTSE 3-Month U.S. T-Bill Index Series.

Bloomberg U.S. Aggregate Index represents the U.S. investment-grade fixed-rate bond market. **Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index** covers the universe of fixed-rate, non-investment-grade debt. The index limits the maximum exposure of any one issuer to 2%. **Bloomberg U.S. Investment Grade Corporate Index** represents the universe of investment-grade, publicly issued U.S. corporate and specified foreign debentures and secured notes that meet the specific maturity, liquidity and quality requirements. **Bloomberg 1–3 Year U.S. Government/Credit Index** is a broad-based benchmark that measures the non-securitized component of the U.S. Aggregate Index, including investment grade, U.S. dollar-denominated, fixed-rate Treasuries, government-related and corporate securities, with maturities of one to three years. **Bloomberg U.S. Treasury Bill 1–3 Month Index** is designed to measure the performance of public obligations of the U.S. Treasury that have a remaining maturity of greater than or equal to one month and less than three months.

FTSE 3-Month U.S. T-Bill Index Series is intended to track the daily performance of three-month U.S. Treasury bills.

The J.P. Morgan Emerging Markets Bond Index (EMBI) Global Diversified is a uniquely weighted emerging market debt benchmark that tracks total returns for USD-denominated bonds issued by emerging market sovereign and quasi-sovereign entities. Emerging markets debt local: **The J.P. Morgan Government Bond Index – Emerging Markets Global Diversified** covers the universe of regularly traded, liquid fixed-rate, domestic-currency emerging market government bonds to which international investors can gain exposure. **J.P. Morgan's USD Real Broad Effective Exchange Rate Index** is designed to measure the exchange rate of the U.S. dollar against a trade-weighted average of currencies in more than 50 countries, adjusted for inflation.

MSCI All Country World Index (ACWI) is a free float-adjusted, market capitalization-weighted index designed to measure equity market results in the global developed and emerging markets, consisting of more than 40 developed and emerging market country indexes. **MSCI China Index** captures large- and mid-cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g., ADRs). **MSCI EAFE (Europe, Australasia, Far East) Index** is a free float-adjusted, market capitalization-weighted index designed to measure developed equity market results, excluding the United States and Canada. **MSCI Emerging Markets Index** is a free float-adjusted, market-capitalization index that measures equity market performance of emerging markets. **MSCI Europe Index** is designed to measure developed equity market results across 15 developed countries in Europe. **MSCI Japan Index** is a free float-adjusted, market capitalization-weighted index that is designed to measure the equity market results of Japan. **MSCI USA Index** is a free float-adjusted, market capitalization-weighted index that measures the U.S. portion of the world market. **MSCI World ex USA Index** is a free float-adjusted, market capitalization-weighted index that measures equity market results in global developed markets, consisting of 22 of 23 developed market country indexes, excluding the United States.

NASDAQ Composite Index tracks the performance of more than 3,000 stocks listed on the NASDAQ and is often viewed as an indicator for the newer sectors of the economy.

S&P 500 Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks.

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2023 Midyear Outlook

Investment implications and strategies to consider

	Dividend opportunities	International equity opportunities	Core bond opportunities	Credit opportunities
Themes	**When markets are unsettled, focus on quality dividend payers**	**Global champions are navigating a new reality**	**Bonds can provide strength as the economy weakens**	**Income is back in fixed income**
Investment implications	Look for dividends to play a greater role in portfolios. But with unsettled markets and higher debt costs, it's essential to focus on quality dividend payers.	As Europe's economy shows surprising resilience and China reopens, leading global companies are tapping into growth opportunities around the world.	Bonds typically offer strong income opportunities and a measure of protection from equity market swings.	Higher yields set the stage for more income and may provide a buffer against bond market volatility.

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2019 2020 2021

*SOURCE: Fund Intelligence, February 20, 2020. FUSE Research survey of nearly 600 advisors identifying the "most-read thought leaders." Marketing Support: The Advisor View, June 2020. FUSE Research survey of more than 700 advisors identifying the "most-read thought leaders." Marketing Support: The Advisor View, July 2021. FUSE Research survey of 720 financial advisors identifying the "most-read asset manager thought leaders."

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