LOOMIS | SAYLES

INVESTMENT OUTLOOK

APRIL 2021

WE BELIEVE RISK ASSETS HAVE FURTHER TO RUN AS THE CREDIT CYCLE CONTINUES TO MOVE FORWARD INTO EXPANSION.

Economic and earnings growth may exceed consensus expectations if the global economy continues to accelerate. Though we anticipate higher US Treasury yields, we doubt a modest rise in rates could meaningfully derail credit and equity market performance in the months ahead.

MACRO & MARKET COMMENTARY

MACRO DRIVERS

Policy support remains in place while the global vaccination effort continues.

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CREDIT

With company fundamentals set to improve, an upgrade cycle may lie ahead.

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GOVERNMENT DEBT & POLICY

Treasury yields should drift rather than spike higher.

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CURRENCIES

Idiosyncratic factors will likely drive foreign currency performance.

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EQUITIES

The global bull market is still young.

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POTENTIAL RISKS

It's too soon to remove accommodative policies.

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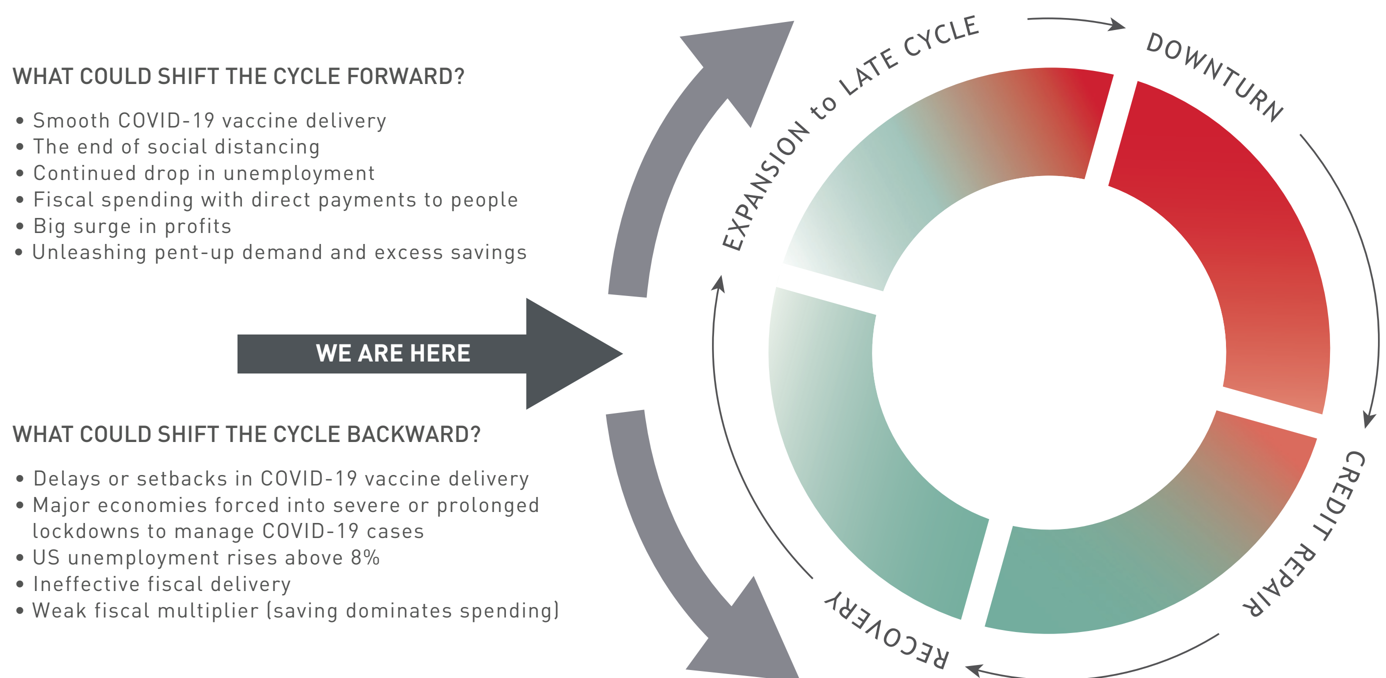
MACRO DRIVERS

We expect the US and China to lead the global economy into expansion.

- COVID-19 vaccine distribution within the United States has improved substantially since the early phases of the rollout. Certain restrictions and crowd limits are likely to remain in place for some time, but we believe an end to social distancing could be in sight by mid-summer 2021.
- Wealthier nations have made more progress in vaccinating their populations, creating uneven vaccination rates around the world. We anticipate a more widespread global ramp-up, though progress will likely remain uneven.
- Global economic activity appears set to accelerate, but vaccine distribution (or lack thereof), has contributed to diverging individual country growth expectations.
- We believe the need for emergency fiscal policies and stimulus remains in most economies, though it should fade as the global economy reopens.
- Monetary policy will likely remain highly accommodative in countries where inflation pressure remains low. We believe central banks like the Federal Reserve and European Central Bank should have the flexibility to remain focused on restoring labor market health.
- We expect year-over-year inflation measures to spike over the next few months, due largely to base effects. We believe these sharp changes will be transitory in developed economies.



Views as of 1 April 2021. The chart presented above is shown for illustrative purposes only. Any opinions or forecasts contained herein reflect the subjective judgments and assumptions of the authors only and do not necessarily reflect the views of Loomis, Sayles & Company, L.P. Views and opinions are subject to change at any time.

CREDIT

With spreads near pre-pandemic levels, we believe security selection will be critical.

- Investment grade credit spreads in the US and Europe may not tighten much further. However, we anticipate positive excess return potential over US Treasurys in a robust economic environment.
- US and European high yield credit spreads could compress a bit if corporate earnings growth surges and economic activity accelerates meaningfully. Relatively low duration and higher carry could help drive high yield return potential versus investment grade credit.
- The US leveraged loan market could offer potential high yield investment opportunities in sectors that were hit hard by the pandemic, but now feature improving outlooks as the economy reopens.
- Emerging market investment grade and high yield corporate credit spreads have been near pre-pandemic levels. However, we believe the scope for moderately tighter spreads and decent returns is probable if the global economy accelerates.
- In our view, securitized credit remains attractive even though spreads are currently tight. We believe weakness in high-quality consumer asset-backed securities should be viewed opportunistically.
- Financial sector spreads appear stable and do not currently show indications of surging to levels that may spark broader risk asset volatility.

GLOBAL HIGH YIELD FINANCIAL SECTOR SPREADS

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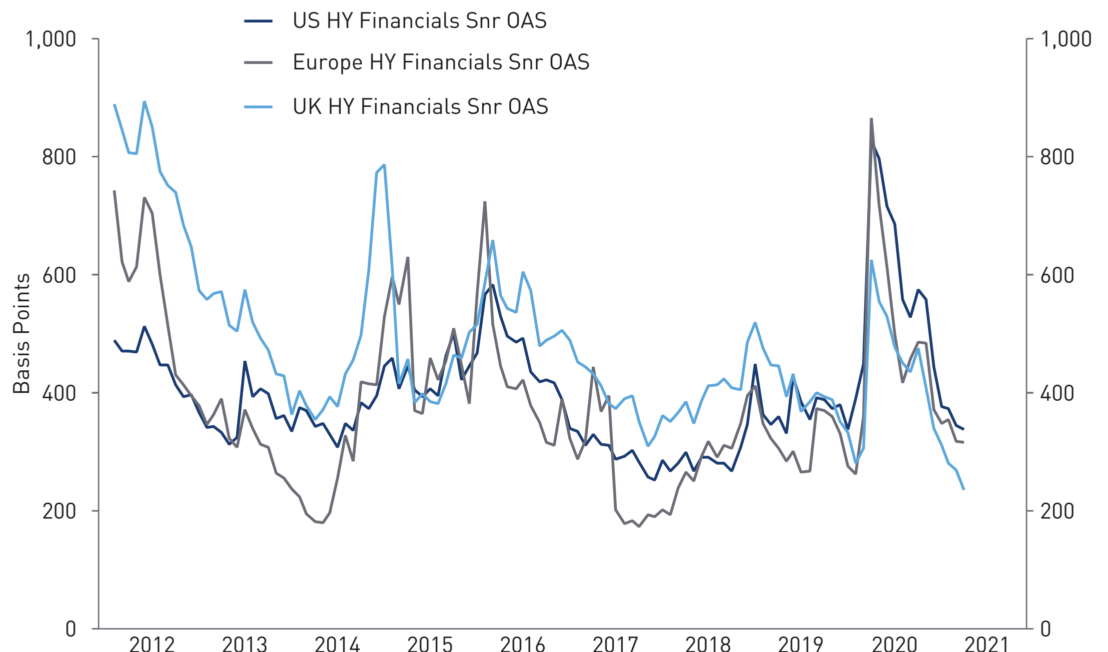

GOVERNMENT DEBT & POLICY

Cyclical uptick in economic activity shouldn't spook the Fed.

- We believe quantitative easing, most notably the purchase of $80 billion of US Treasurys per month, is likely to continue through the latter half of 2021.
- The Fed vowed to look through anticipated above-trend year-over-year economic data during the second quarter, which will be compared to levels at the depths of the downturn.
- When the Fed is ready to move away from ultra-accommodative policy, we think one of its first moves will be tapering asset purchases. Embarking on a new rate-hiking cycle is a separate policy decision that may not materialize until mid-2023 or later.
- We believe the front end of the US yield curve is likely to remain anchored for the foreseeable future, but 5- to 30-year yields are likely headed higher. We view rising rates as a positive sign of cyclical improvement within the domestic economy.
- With the recent move off pre-pandemic lows behind us, we believe US rates will trend higher at a much slower pace. Rates in developed Europe may trend higher too, but likely at a pace that is commensurate with less-robust growth in that region.
- Rising US Treasury yields tend to represent a headwind for sovereign and local-currency emerging market bonds. However, we expect the asset class to remain resilient as the global economy recovers.

G-3 CENTRAL BANK MONETARY POLICY

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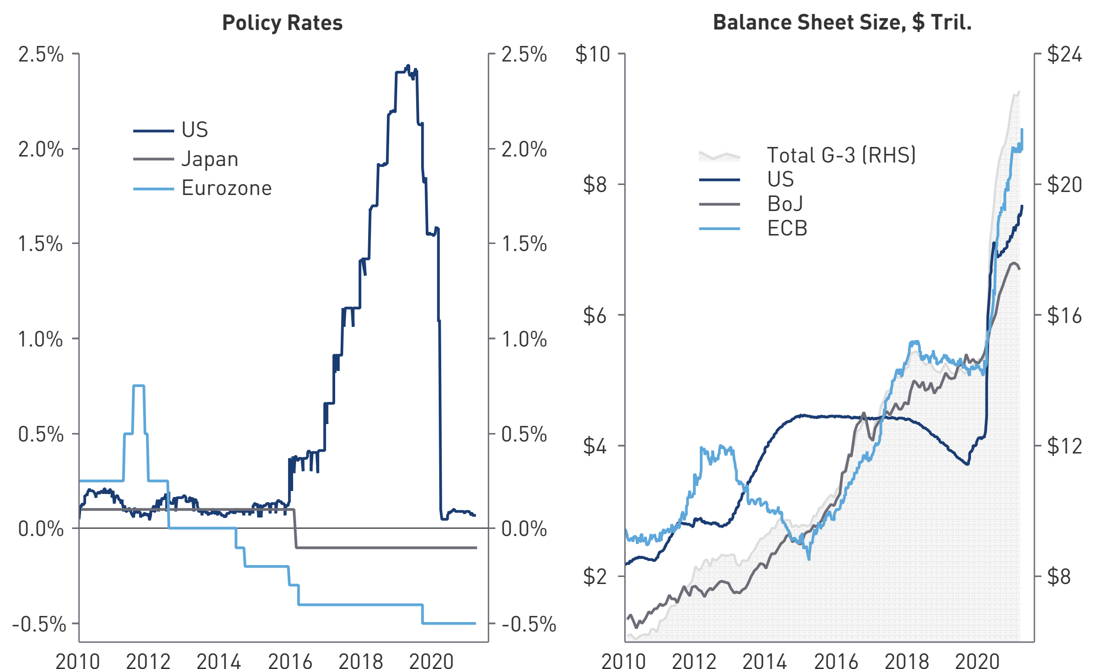

CURRENCIES

We see limited broad dollar weakness ahead.

- Conditions that typically lead to substantial US dollar weakness seem unlikely to prevail. We expect key dollar drivers such as growth and interest rate differentials to remain in favor of the dollar near term.
- Progress on vaccinations and reopening could contribute to US economic outperformance in 2021, but we anticipate a solid rebound outside the US if the credit cycle progresses.
- We believe the case for investing in foreign currencies more broadly will likely grow stronger as expectations for non-US growth improve and if interest rate differentials begin to reverse course.
- For now, we remain focused on specific foreign exchange opportunities. We tend to favor currencies with moderate return potential and carry, which currently include Brazil, Colombia and Mexico.
- With monetary policy at or below the zero lower bound in many developed markets, we are broadly neutral on developed market foreign exchange. However, we currently prefer markets like Norway and Australia, which can perform well if commodity prices rise in a global recovery.

US DOLLAR INDEX LEVELS

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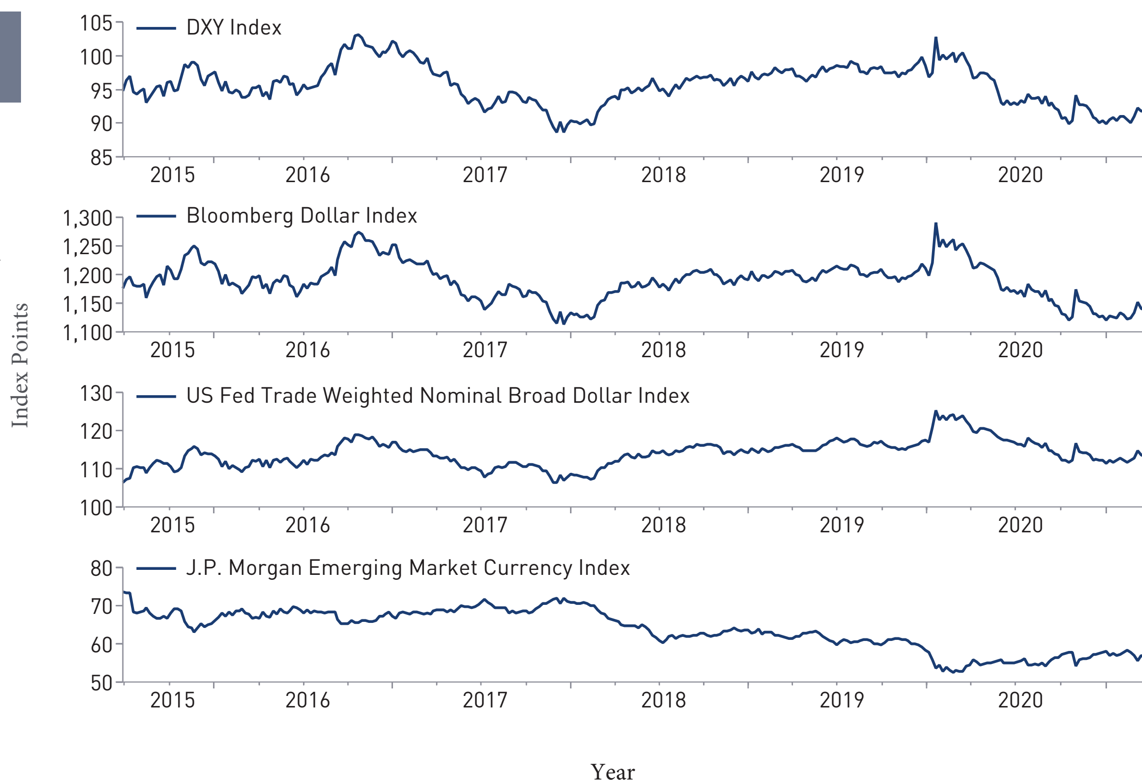

EQUITIES

Substantial earnings growth could drive global equities higher.

- Equity valuations have been indicating a high degree of optimism regarding the economic rebound and corporate earnings trajectory, but we currently see additional upside potential. We believe global equity indices can continue their broad advance, led by the US.
- A rising rate environment can pressure valuations, but we think it is important to consider that the absolute level of interest rates has remained historically low. Equities typically offer more attractive absolute return potential than fixed income in a rising rate environment.
- While uneven in magnitude, the cyclical upturn across global economies has been supporting most sectors of the equity market. Traditional value-oriented sectors like financials, materials and industrials may continue to perform well on the back of strong earnings growth.
- We believe growth-oriented sectors and industries are likely to keep pace with value in the near term and could potentially outperform over the long term. In our view, the technology sector's secular growth story is unlikely to be derailed.

GLOBAL EQUITY PERFORMANCE SINCE THE MARCH LOW

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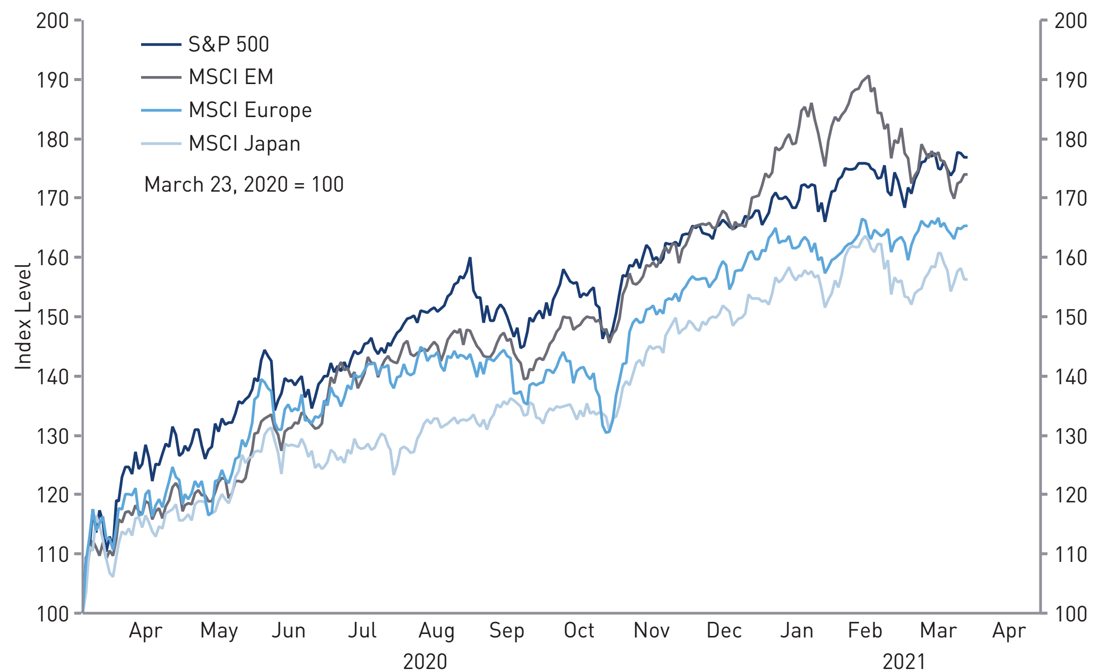


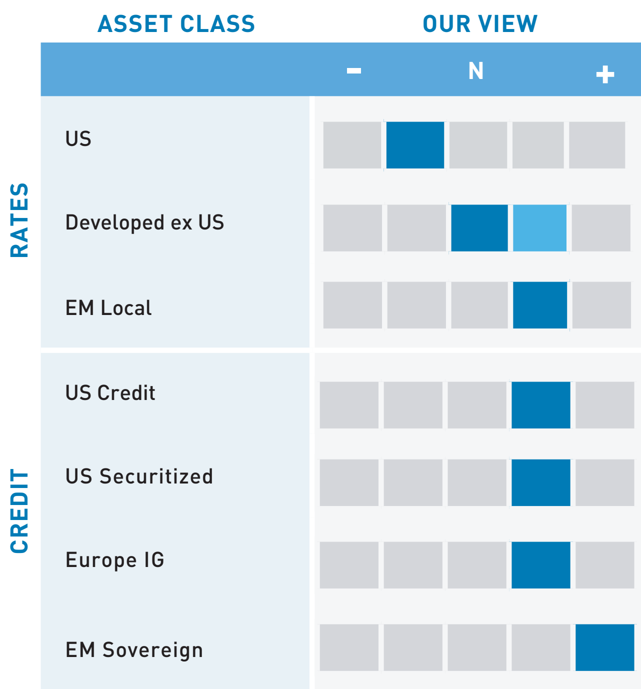
POTENTIAL RISKS

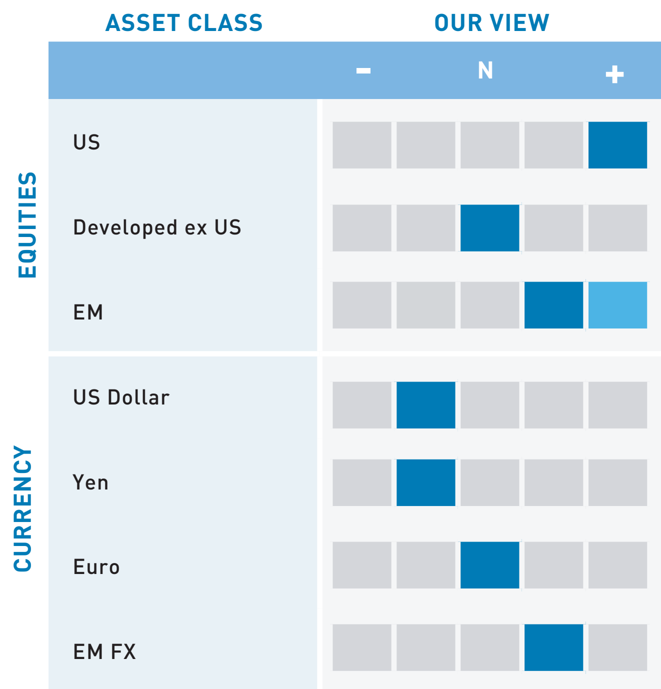
Positive outlook leaves little room for setbacks or policy missteps.

- While we have a high degree of conviction that the credit cycle is heading in a positive direction, that view largely depends on continued vaccination progress, particularly in non-US economies.
- The global reopening process has been a major factor driving our expectations for a sizable economic rebound. Any setbacks to the recovery would be disruptive to our outlook.
- The global economy may not be able to handle missteps by policy makers. We believe withdrawal of monetary accommodation or pivoting toward fiscal austerity could be problematic if engaged too soon.
- Near-term base effects aside, a lack of inflation pressurv across many of the world's largest economies has permitted considerable debt issuance and policy rates at or below the zero lower bound.
- If higher-than-anticipated levels of inflation begin to stick, central banks might shift key policy supports before the labor market has fully recovered, which could prolong the economic recovery.

ASSET CLASS OUTLOOK

Current View   Previous View





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