SUPPLEMENT TO THE US MACRO MONITOR

The Chart Pack features our latest investment calls and probability forecasts on the US stock market and its key sectors, US sovereign and corporate bonds and overall asset allocation.

June 2021

Summary and highlights:

- **Stocks**: Stock returns accelerated this past month, even as the Fed moved forward their projected timeline for rate hikes. Most gains stemmed from tech-heavy sectors, which benefited from falling long-term yields as breakeven inflation normalized. We remain bullish on US stocks, given strong growth and earnings prospects.

- **Sectors**: While falling long-term yields have caused tech stocks to outperform since May, reopening sectors and late cyclicals should regain the upper hand over the coming year. Similarly, above-target inflation and strong GDP growth should favour 'value' investments over 'growth' stocks during this period.

- **Bonds**: 10Y bond yields are down 25 bps since reaching 1.75% in March. Stronger demand for long-dated bonds has pushed prices above their 'fair' value, weakening their appeal in a context of rising growth and inflation. We expect bonds to underperform, and recommend favouring gold and TIPS in balanced investment portfolios.

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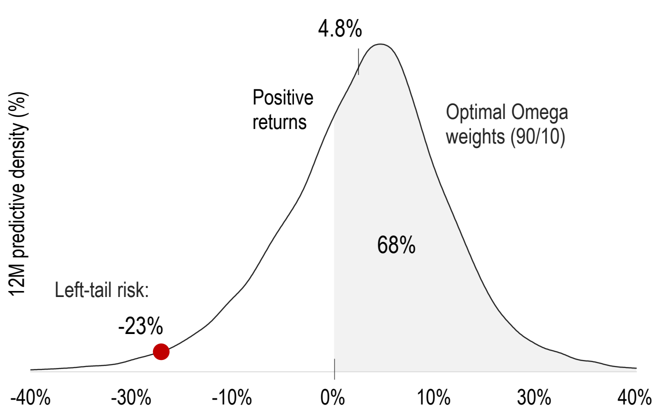
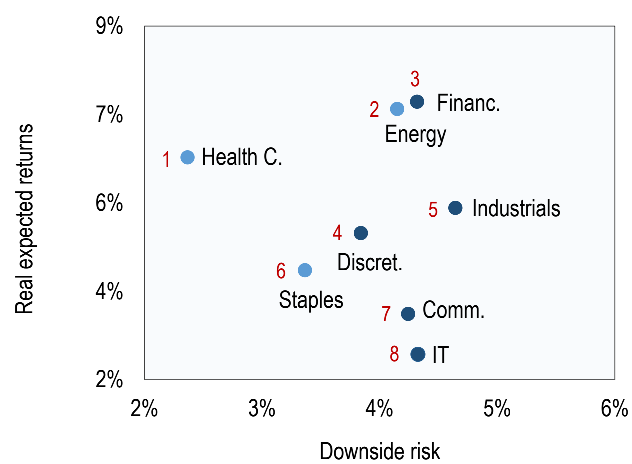
Optimal Omega portfolio - 12M



Note: Probability forecast for a portfolio comprised of US stocks and bonds, with weights chosen to maximize the portfolio's Omega ratio over a 12M holding period. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive returns. Source: Numera Analytics.

F2: Risk-reward comparison
US equities - 12M ahead



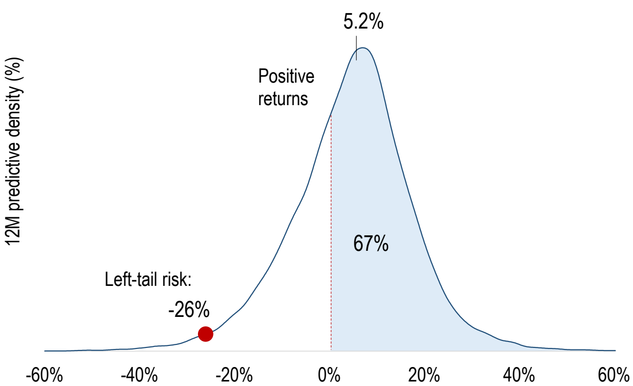
Note: Real USD total expected returns versus downside risk for 12M holdings in major US equity sectors. Numbers rank assets by their Omega ratio. Source Numera Analytics.

1) US Stock Market:

- **Absolute** – *Overweight* (●). A high vaccine coverage and ample stimulus should push GDP back to pre-COVID levels by Q3. High growth improves the risk-reward balance for US stocks, even as rising inflation creates uncertainty over Fed policy. Given still weak employment levels, we expect a single rate hike over the next 12M. While the policy shift would weigh on valuations, higher yields should be more than offset by strong earnings.

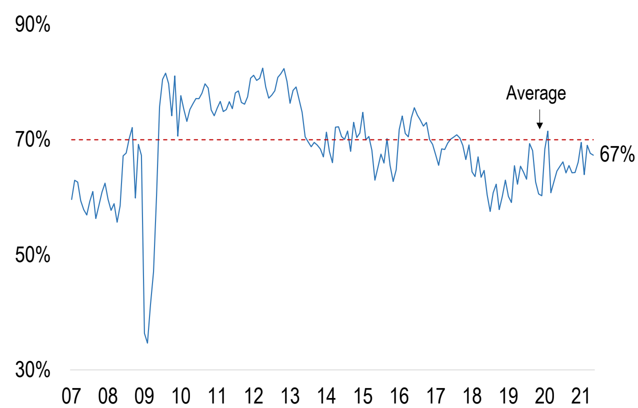
- **Relative** – *Overweight* (●). From an asset allocation perspective, a 90% equity weighting maximizes risk-adjusted returns for a US-only stock/bond portfolio (F6). As we show in our May US Macro Monitor, however, replacing nominal bonds by inflation hedges like TIPS or gold materially improve the portfolio's projected performance.

F3: Real returns - US stocks[1]
12M probability forecast



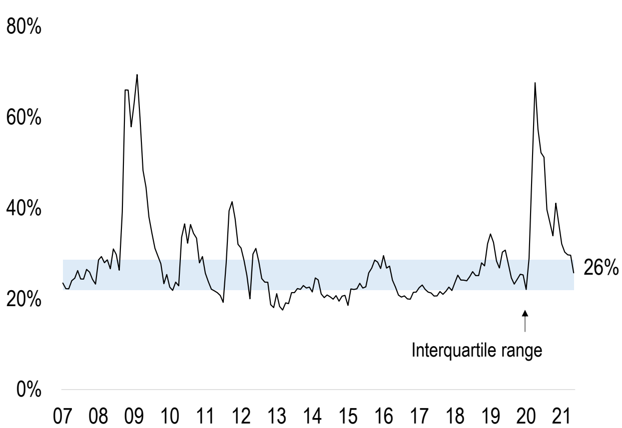
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F4: Positive real returns - US stocks
Likelihood, 12M ahead (%)



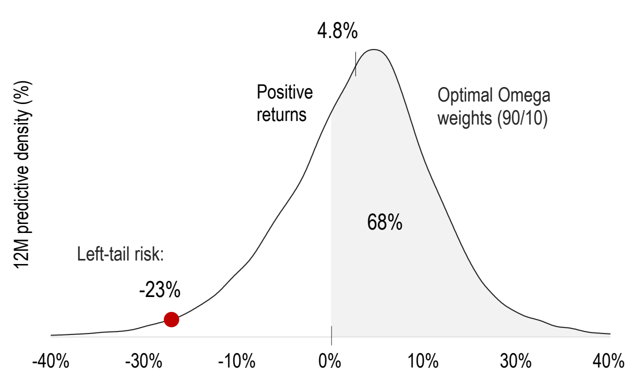
Note: Chart tracks probability of positive real returns on US equities (S&P 500 TR) over a 12M holding period. Last value corresponds to shaded area in F3. Red line is the historical average. Source: Numera Analytics.

F5: Downside risk - US equities
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in the S&P 500. Shaded band is the interquartile range. Source: Numera Analytics.

F6: Real portfolio returns - US assets[3]
Optimal Omega portfolio - 12M



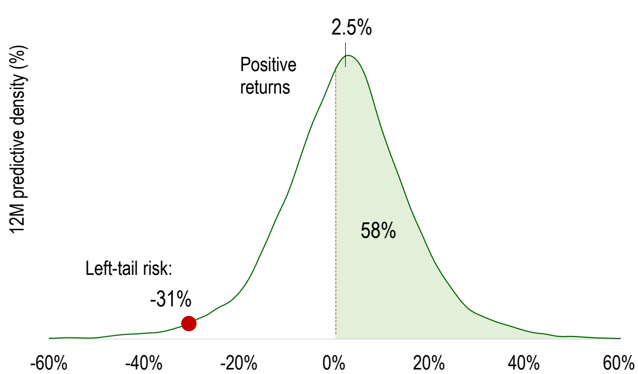
Note: Probability forecast for a portfolio comprised of US stocks and bonds, with weights chosen to maximize the portfolio's Omega ratio over a 12M holding period. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive returns. Source: Numera Analytics.

2) Information Technology:

- **Absolute** – *Neutral* (●). IT stocks are up 6% this past month, as falling long-term yields offset the drag of improving mobility on demand for consumer electronics. In addition, bullish earnings projections boosted IT stock purchases, with 72% of IT firms reporting a positive Q2 EPS guidance (the highest share among S&P 500 sectors). Returns should weaken over the next 12M, weighed down by a normalization in expenditure patterns.

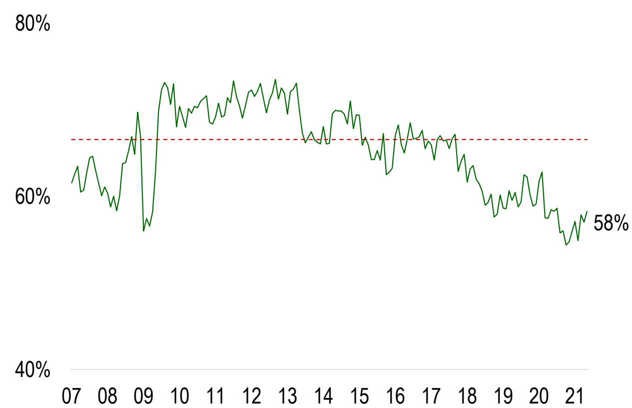
- **Relative** – *Underweight* (●). IT stocks continue to trade at a premium, which in a reflationary environment weakens their relative appeal against other sectors. IT investments have only a 48% chance of outperforming the S&P over the next 12M (F10), and remain exposed to deeper losses (although tail risk has diminished considerably).

F7: Real returns - IT stocks[1]
12M probability forecast



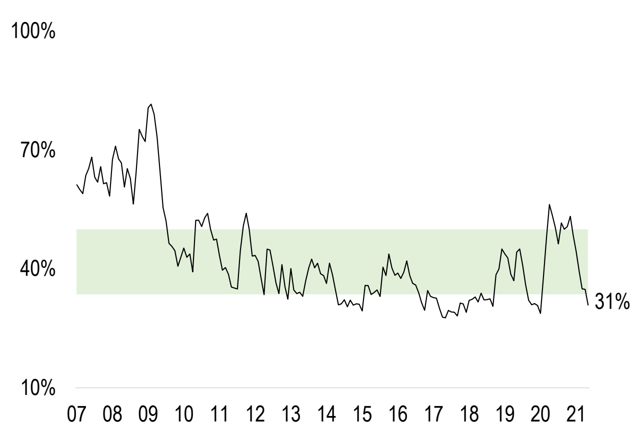
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F8: Positive real returns - IT
Likelihood, 12M ahead (%)



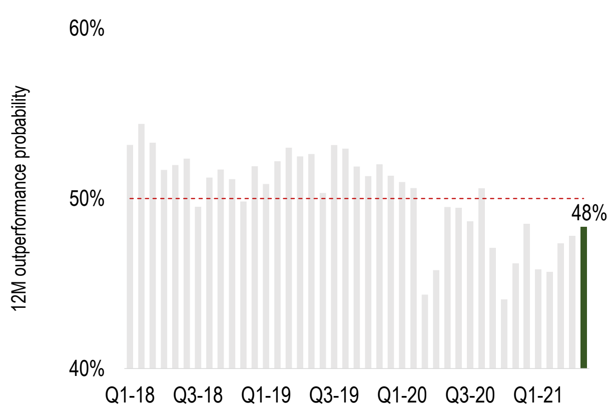
Note: Chart tracks probability of positive real returns on S&P IT stocks over a 12M holding period. Last value corresponds to shaded area in F7. Red line is the historical average. Source: Numera Analytics.

F9: Downside risk - IT
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in S&P 500 IT stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F10: Excess returns - IT
Outperformance[4] probability (vs. S&P)



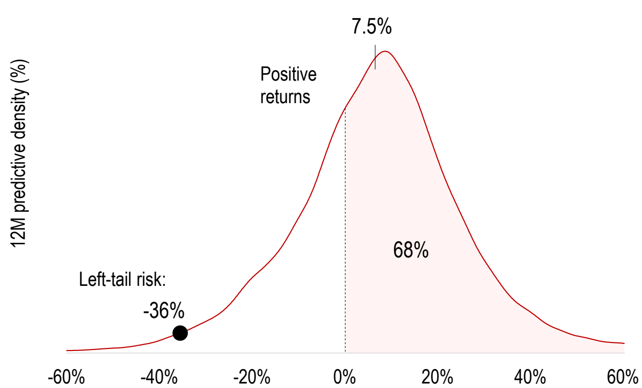
Note: Chart plots likelihood of IT stocks outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

3) Financials:

- **Absolute** – *Overweight* (●). Financials are down 6% since peaking in early June, weighed down by a narrower term spread. We believe this weakness should prove temporary, with financials delivering above-trend returns over the next 12M (F11). Banking stocks should continue to benefit from strong growth, high inflation and relatively low valuations, while low financial stress limits the probability of extreme losses (F13).

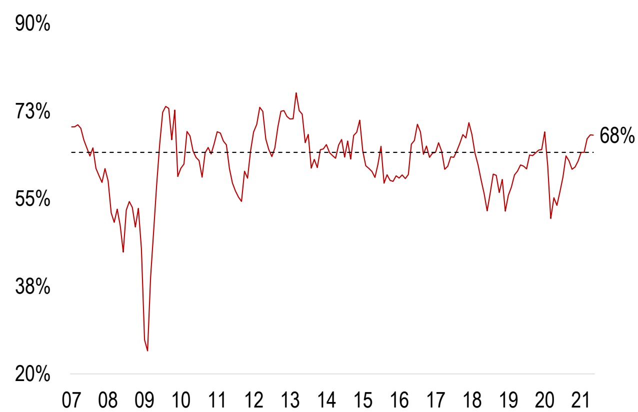
- **Relative** – *Overweight* (●). There is currently a 62% chance that financials will outperform over the next 12M, a high probability by historical standards (F14). The high likelihood reflects a higher sensitivity to GDP growth than the overall market, and a much more limited impact of higher long-term yields on equity returns.

F11: Real returns - Financial stocks[1]
12M probability forecast



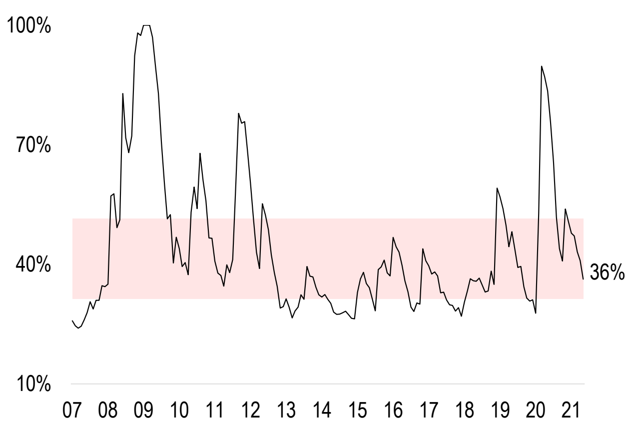
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F12: Positive real returns - Financials
Likelihood, 12M ahead (%)



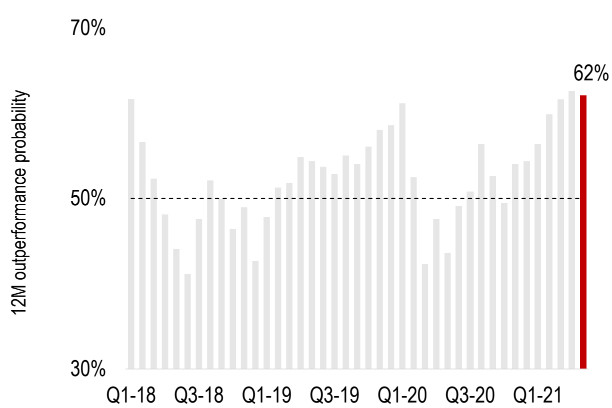
Note: Chart tracks probability of positive real returns on S&P financial stocks over a 12M holding period. Last value corresponds to shaded area in F11. Black line is the historical average. Source: Numera Analytics.

F13: Downside risk - Financials
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in S&P 500 financial stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F14: Excess returns - Financials
Outperformance[4] probability (vs. S&P)



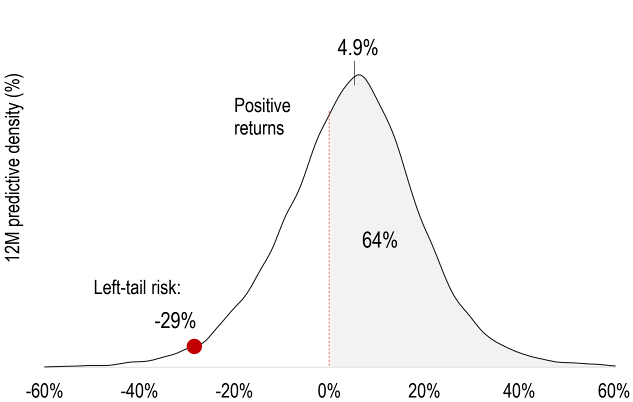
Note: Chart plots likelihood of financial stocks outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

4) Consumer Discretionary:

- **Absolute** – *Overweight* (●). Consumer cyclicals recovered from their May losses, buoyed by strong returns on internet retail stocks. Much like IT, electronic shopping firms are benefiting from a decline in long-term yields, as investors revise downwards their inflation expectations. Rising mobility, strong consumer confidence and high excess savings improve the sector's upside over the next 12M – particularly for consumer services.

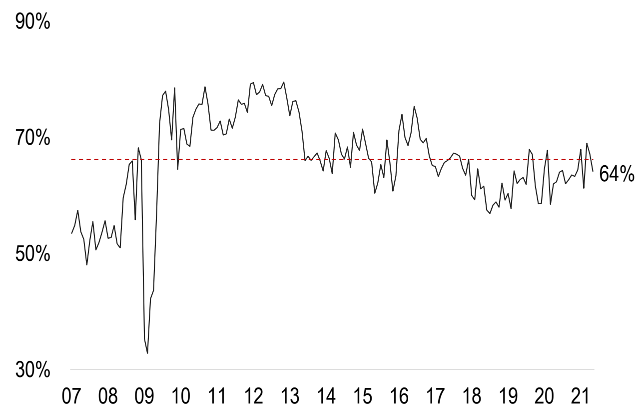
- **Relative** – *Neutral* (●). Discretionary stocks offer a similar risk-reward balance than the overall market. However, the vaccine rollout improves their relative appeal versus other 'growth' sectors like IT (F2). The reason for this is that higher mobility is hugely beneficial to in-store retail and consumer service stocks (40% of market cap).

F15: Real returns - Discretionary stocks[1]
12M probability forecast



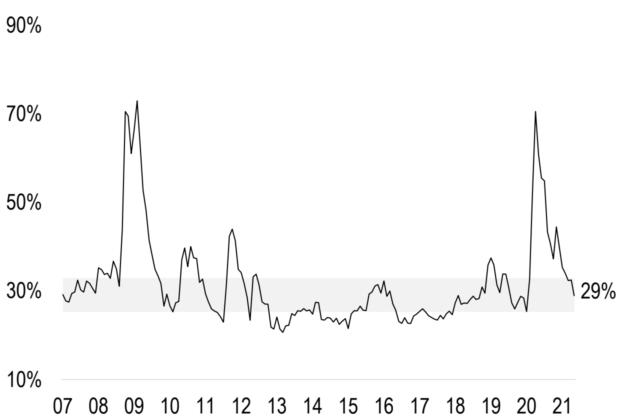
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F16: Positive real returns - Discretionary
Likelihood, 12M ahead (%)



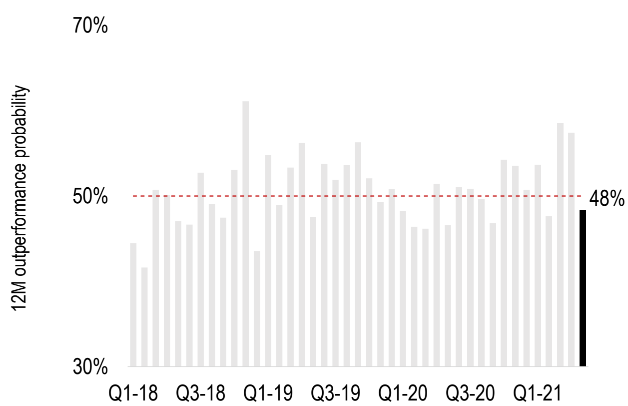
Note: Chart tracks probability of positive real returns on S&P consumer discretionary stocks over a 12M holding period. Last value corresponds to shaded area in F15.Red line is the historical average. Source: Numera Analytics.

F17: Downside risk - Discretionary
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in S&P 500 consumer discretionary stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F18: Excess returns - Discretionary
Outperformance[4] probability (vs. S&P)



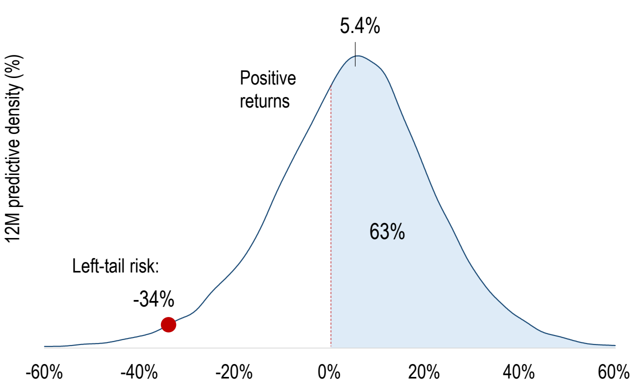
Note: Chart plots likelihood of consumer discretionary stocks outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

5) Industrials:

- **Absolute** – *Overweight* (🟢). Industrials fell 3% this past month, their first monthly decline since January. Most sub-sectors experienced losses, in part owing to a normalization in business investment amid decelerating vaccination rates. We expect the sell-off to prove short-lived, with strong GDP growth and improved mobility boosting profit margins for ‘reopening’ sub-sectors like aerospace and transportation.

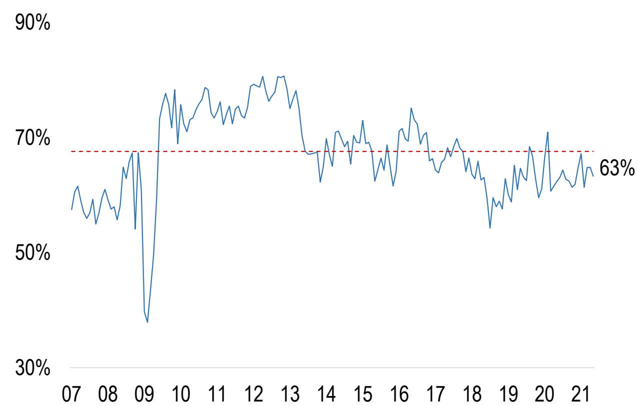
- **Relative** – *Neutral* (🟡). Industrials retain a slightly higher upside than total US stocks. Nevertheless, the uncertain nature of the pandemic exposes capital-intensive sectors to deeper potential losses. For instance, the likelihood of a ‘bear’ market (a 20%+) correction is about 10% on 12M holdings, versus 5% for the S&P.

F19: Real returns - Industrial stocks[1]
12M probability forecast



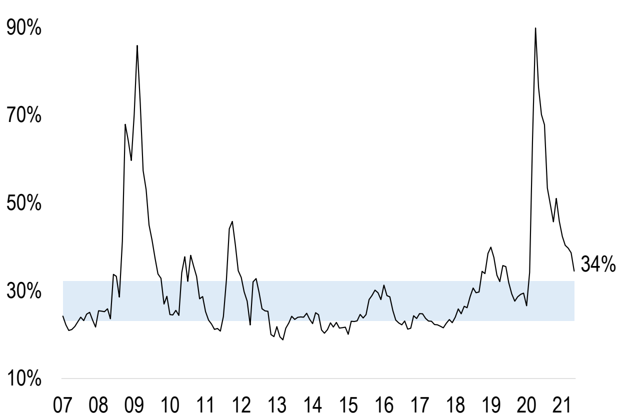
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F20: Positive real returns - Industrials
Likelihood, 12M ahead (%)



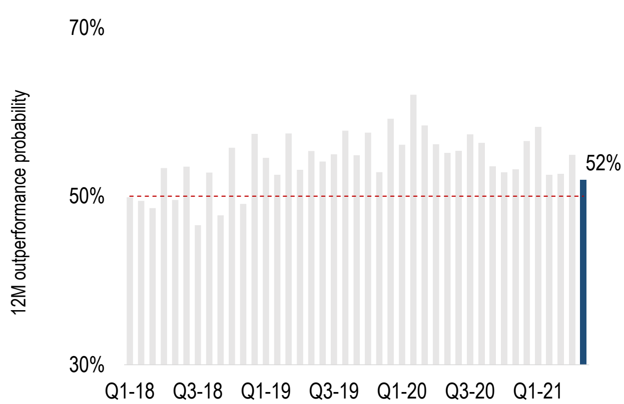
Note: Chart tracks probability of positive real returns on S&P industrial stocks over a 12M holding period. Last value corresponds to shaded area in F19. Red line is the historical average. Source: Numera Analytics.

F21: Downside risk - Industrials
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in S&P industrial stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F22: Excess returns - Industrials
Outperformance[4] probability (vs. S&P)



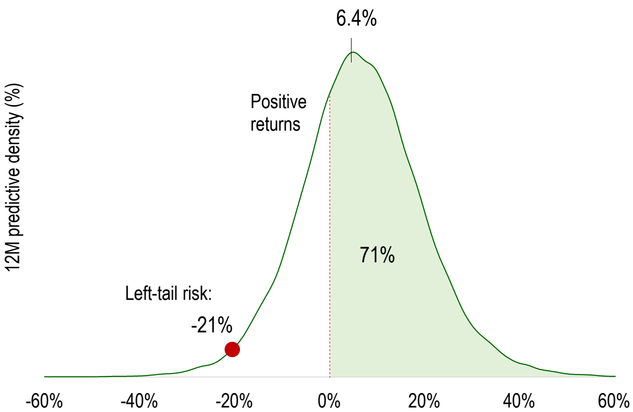
Note: Chart plots likelihood of industrial stocks returns outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

6) Health care:

- **Absolute** – *Neutral* (🟡). Health care continues to trail the S&P, owing to a rotation away from defensives and concerns over pharma stocks given a Democrat-controlled Congress. Despite policy uncertainty, we remain bullish on health care. Low valuations and strong demand for health care should offset any policy concerns 12M out. An ageing population and strong R&D, in turn, vastly improve the sector's appeal as a core long-term holding.

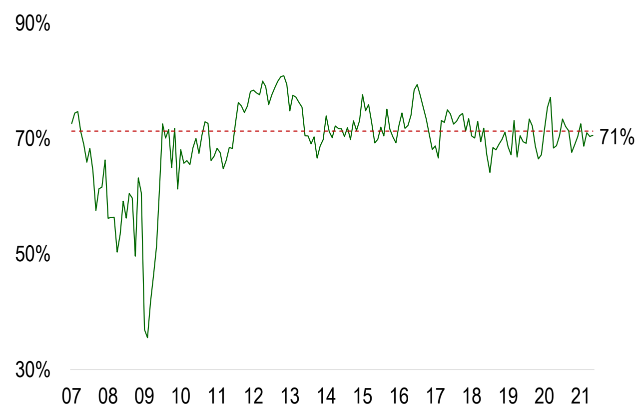
- **Relative** – *Overweight* (🟢). In relative terms, health care stocks offer an attractive risk-reward trade-off versus other sectors (F2). There is currently a 60% chance that health care will deliver excess returns on 12M holdings (F2), whereas downside risk remains considerably lower than for overall US equity investments.

F23: Real returns - Health care stocks[1]
12M probability forecast



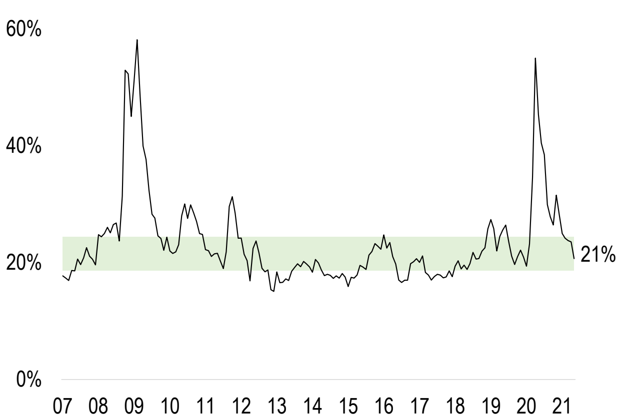
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F24: Positive real returns - Health care
Likelihood, 12M ahead (%)



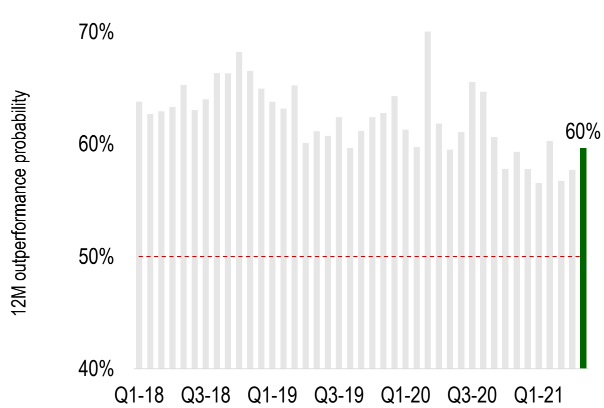
Note: Chart tracks probability of positive real returns on S&P health care stocks a 12M holding period. Last value corresponds to shaded area in F23. Red line is the historical average. Source: Numera Analytics.

F25: Downside risk - Health care
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in S&P 500 health care stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F26: Excess returns - Health care
Outperformance[4] probability (vs. S&P)



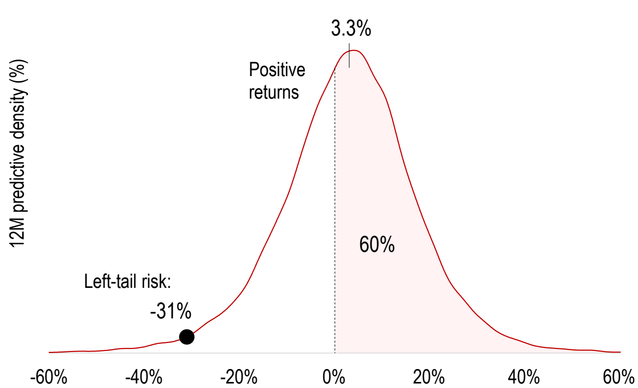
Note: Chart plots likelihood of health care stocks outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

7) Communication Services:

- **Absolute** – *Neutral* (🟡). Communication services are up 3.5% over this past month, benefiting from declining long-term yields despite the Fed's less dovish tone. We expect profit growth for only media stocks to weak this year, as rising mobility will likely weaken the expenditure share allocated to online services. Nevertheless, a bullish growth outlook favour entertainment and telecommunication stocks, justifying a neutral absolute stance.

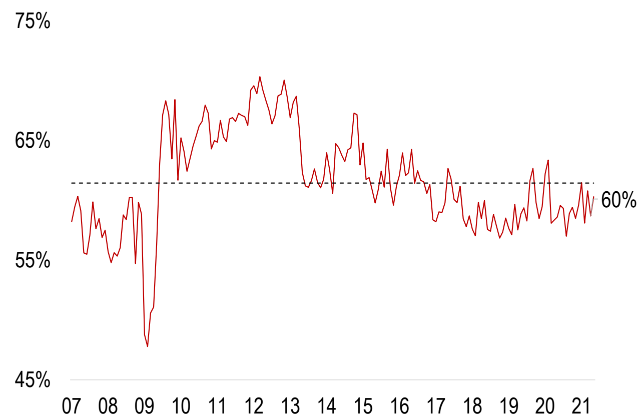
- **Relative** – *Underweight* (🔴). 'Value' rotation makes communication services considerably less attractive than the S&P. There is only a 44% chance that the sector will outperform 12M out (F30), which in combination with higher left-tail risk than US stocks overall justifies a relative underweight position.

F27: Real returns - Comm. Service stocks[1]
12M probability forecast



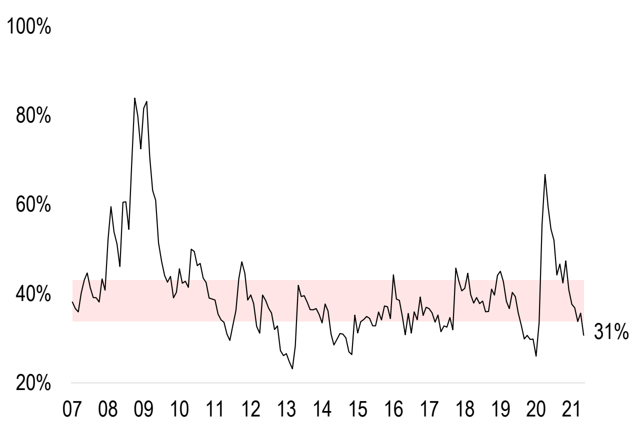
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F28: Positive real returns - Comm. Services
Likelihood, 12M ahead (%)



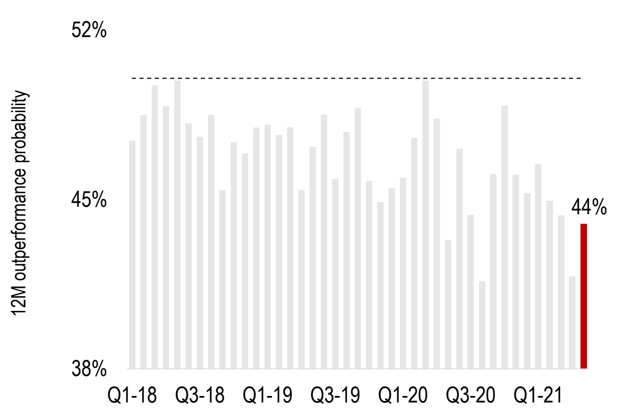
Note: Chart tracks probability of positive real returns on S&P communication services stocksover a 12M holding period. Last value corresponds to shaded area in F26. Black line is the historical average. Source: Numera Analytics.

F29: Downside risk - Comm. Services
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments S&P 500 communication services stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F30: Excess returns - Comm. Services
Outperformance[4] probability (vs. S&P)



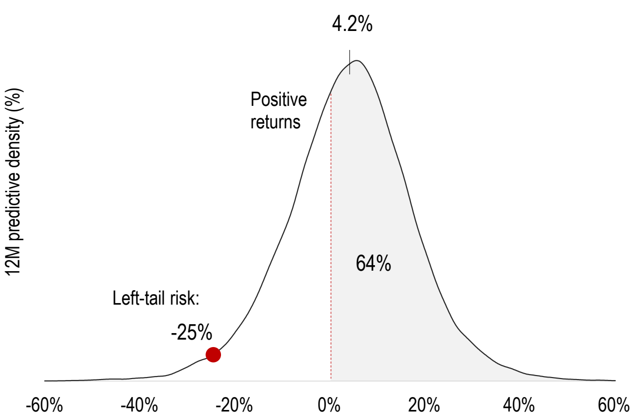
Note: Chart plots likelihood of communication service stocks outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

8) Consumer Staples:

- **Absolute** – *Neutral* (●). Staples fell 0.8% this past month as investors rotated towards 'reopening' stocks and sectors sensitive to falling long-term yields. In a context of improved mobility and reduced economic uncertainty, staples are less attractive investments than in 2020. Still, declining vaccination rates and elevated inflation improve the sector's upside versus earlier this year, so we have upgraded our absolute call from underweight to neutral.

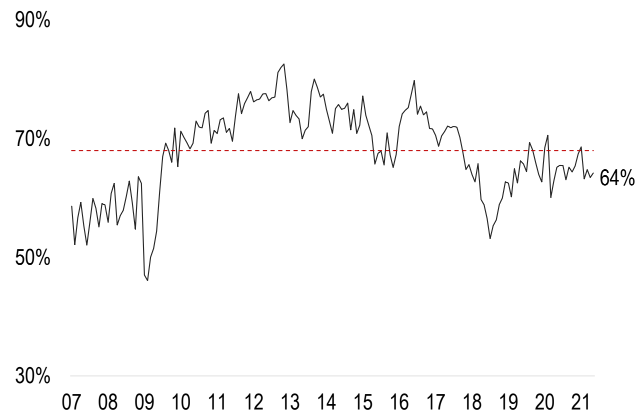
- **Relative** – *Underweight* (●). We have downgraded our relative call to 'underweight'. The bullish growth outlook makes it unlikely for staples to outpace overall US stocks 12M out (F34). In addition, falling uncertainty and low financial stress limit the sector's appeal as a 'macro hedge', narrowing differences in left-tail risk.

F31: Real returns - Cons. Staples stocks[1]
12M probability forecast



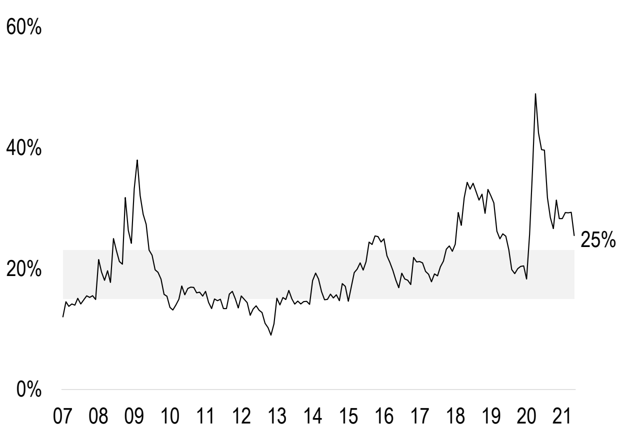
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F32: Positive real returns - Cons. Staples
Likelihood, 12M ahead (%)



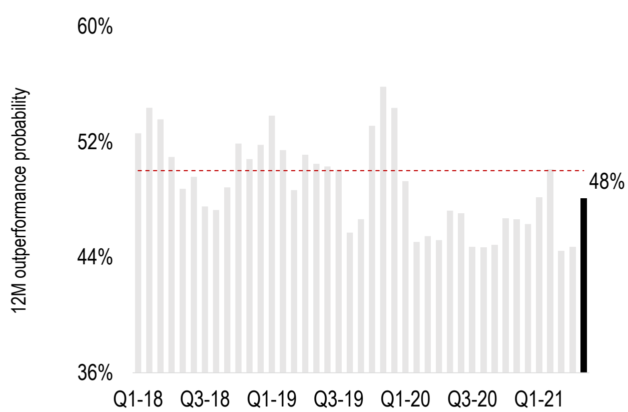
Note: Chart tracks probability of positive real returns on S&P consumer staples stocks over a 12M holding period. Last value corresponds to shaded area in F31. Red line is the historical average. Source: Numera Analytics.

F33: Downside risk - Cons. Staples
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in S&P 500 consumer staples stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F34: Excess returns - Cons. Staples
Outperformance[4] probability (vs. S&P)



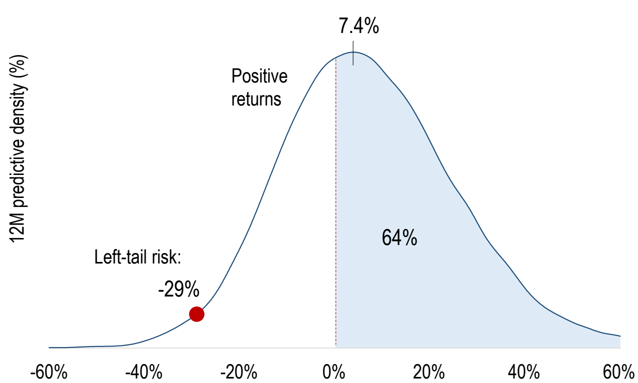
Note: Chart plots likelihood of consumer staple stocks outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

9) Energy Stocks:

- **Absolute** – *Overweight* (●). Energy stocks are up 41% YTD, benefiting from a surge in oil prices and stronger profit margins by oil majors and public E&P firms. The ongoing rally has pushed energy stocks back to 'fair' value, which limits their upside versus earlier in the pandemic (F36). Nevertheless, projected improvements in mobility (and hence transportation demand) still make energy stocks an attractive investment in absolute terms.

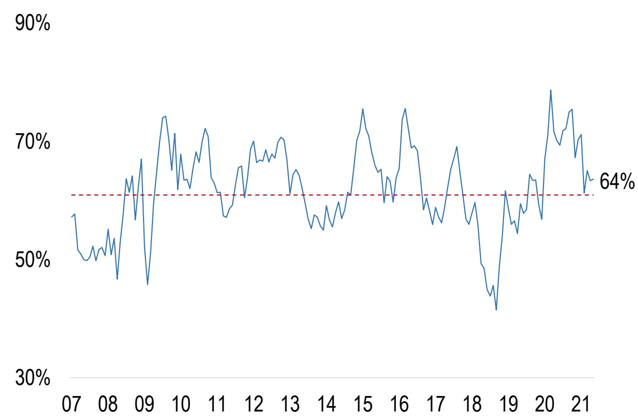
- **Relative** – *Neutral* (●). Compared to other assets, however, expected returns are no longer high enough to justify an overweight relative stance. Specifically, the probability of excess returns on one-year holdings is now 57%, versus 65%+ in Q4/20. As a result, we have downgraded our relative call to 'neutral' for the first time in a year.

F35: Real returns - Energy stocks[1]
12M probability forecast



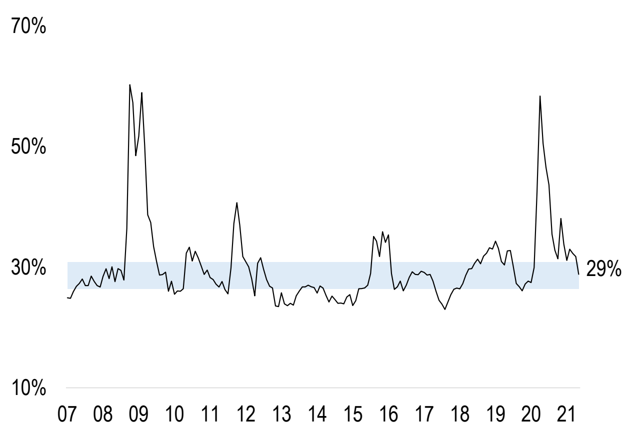
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F36: Positive real returns - Energy
Likelihood, 12M ahead (%)



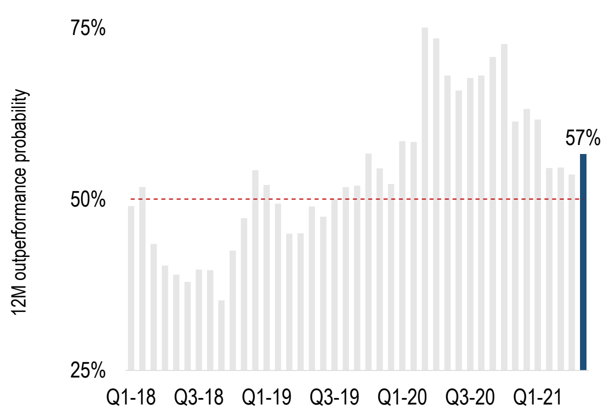
Note: Chart tracks probability of positive real returns on S&P energy stocks over a 12M holding period. Last value corresponds to shaded area in F35. Red line is the historical average. Source: Numera Analytics.

F37: Downside risk - Energy
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in S&P 500 energy stocks. Shaded band is the interquartile range. Source: Numera Analytics.

F38: Excess returns - Energy
Outperformance[4] probability (vs. S&P)



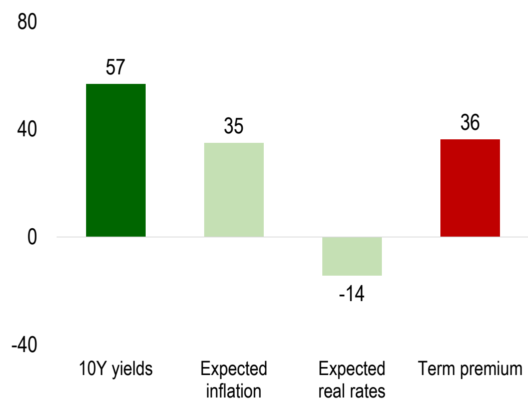
Note: Chart plots likelihood of energy stocks outperforming the S&P 500 over a 12M holding period. Probabilities above 50% indicate most likely outcome. Source: Numera Analytics.

10) Sovereign bonds:

- **Absolute** – *Neutral* (🟡). 10Y yields are down 25 bps since nearing 1.75% in late March. Given strong growth, the drop in yields reflects higher demand for long-dated bonds and more recently a normalization in investor inflation expectations. Forward guidance should prevent yields from rising above 200 bps over the next 12M, but a strong growth outlook and above-target inflation limits their appeal as a macro hedge by increasing left-tail risk (F42).

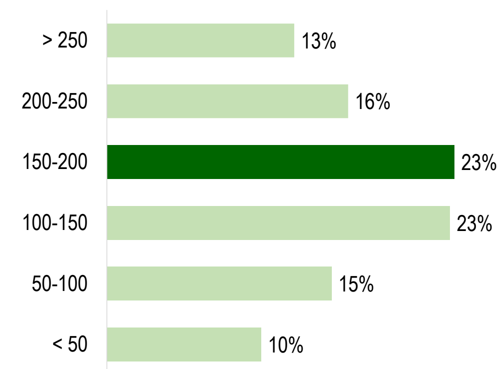
- **Relative** – *Underweight* (🔴). High inflation and a bullish growth outlook affect the projected performance of stock/ bond portfolios. While higher yields depress bond returns, strong earnings should compensate for the impact of higher discount rates on stock valuations. We recommend underweighting bonds versus stocks 12M out.

F39: Term premium decomposition
Change in 10Y yields (bps) - 6M 2021



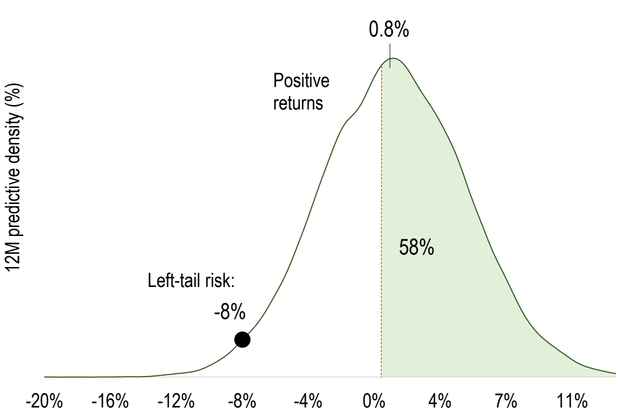
Note: Chart decomposes the change in 10-year Treasury yields YTD into its estimated expectations (inflation + real rates) and term premium components. Source: Numera Analytics

F40: 10Y Treasury yield outlook
12M probability forecasts (bps)



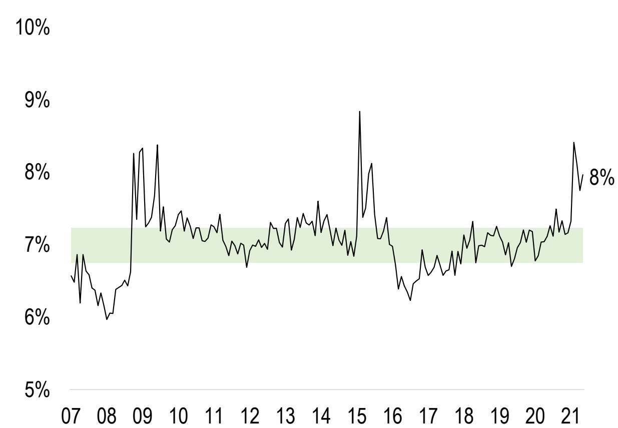
Note: Chart shows the probability of 10-year Treasury yields falling within a given range (in bps) one-year out. Source: Numera Analytics.

F41: Real returns - Sovereign bonds[1]
12M probability forecast



Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F42: Downside risk - Sovereign bonds
Left-tail risk[2] (5%) - 12M ahead



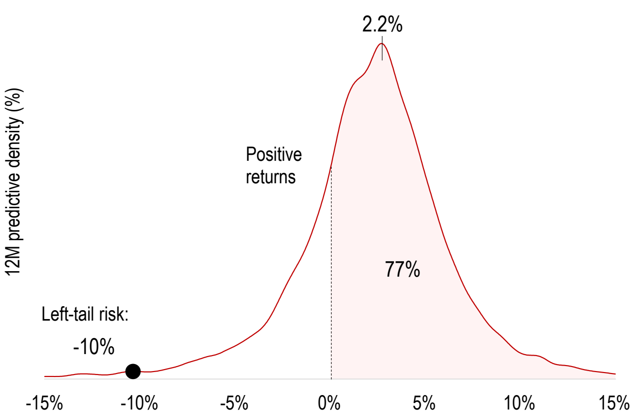
Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in US sovereign bonds. Shaded band is the interquartile range. Source: Numera Analytics.

11) Corporate bonds:

- **Absolute** – *IG neutral* (●). Further declines in sovereign yields lifted investment-grade (IG) bonds for the third consecutive month in June. IG bonds should continue to recover, as strong growth limits the likelihood of corporate defaults. However, a high probability of above-target inflation over the next 12M increases downside risk versus earlier in the pandemic (F4). As a result, we recommend a neutral absolute stance.

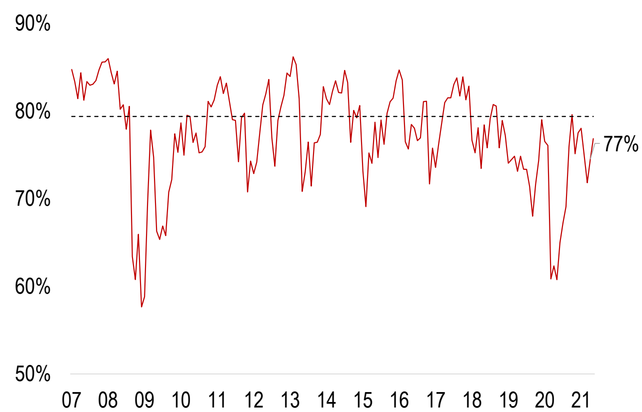
- **Relative** – *IG neutral* (●). For balanced investors, IG bonds offer a similar risk-reward balance than US equities. This is because although their upside is more limited, ample Fed stimulus vastly reduces left-tail risk on new IG investments. High leverage in a context of elevated economic uncertainty makes HY bonds much less attractive.

F43: Real returns - Investment grade[1]
12M probability forecast



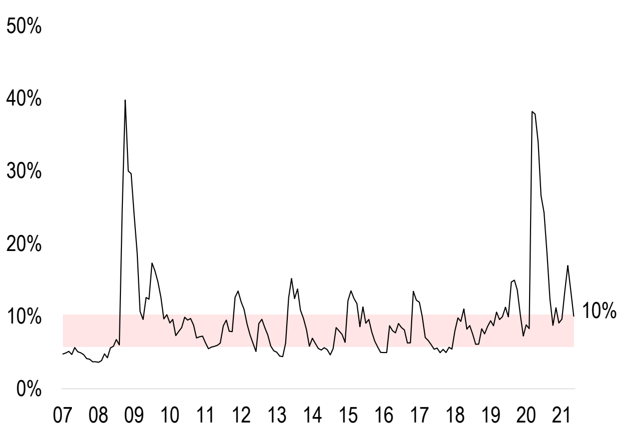
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F44: Positive real returns - Investment grade
Likelihood, 12M ahead (%)



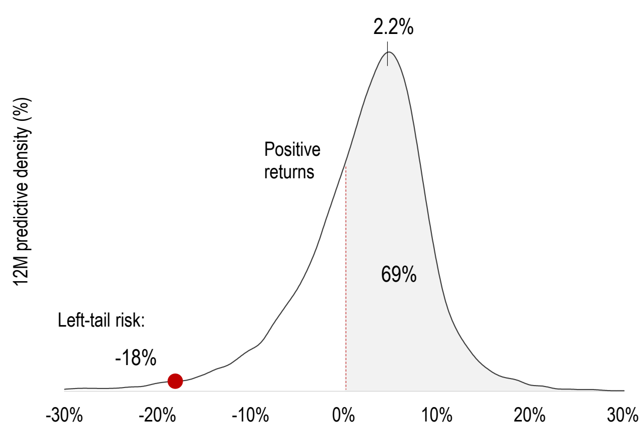
Note: Chart tracks probability of positive real returns on S&P energy stocks over a 12M holding period. Last value corresponds to shaded area in F43. Red line is the historical average. Source: Numera Analytics.

F45: Downside risk - Investment grade
Left-tail risk[2] (5%) - 12M ahead



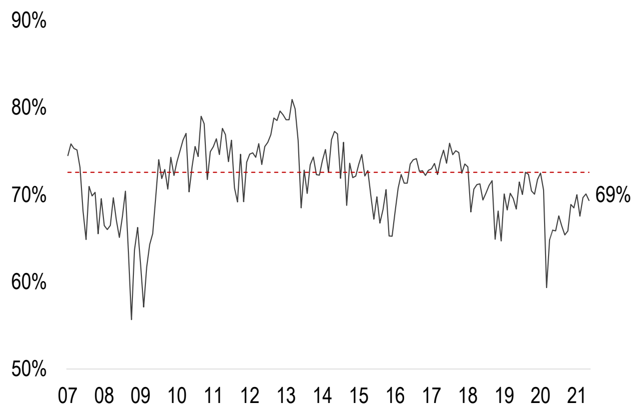
Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in US investment-grade corporate bonds. Shaded band is the interquartile range. Source: Numera Analytics.

F46: Real returns - High yield[1]
12M probability forecast



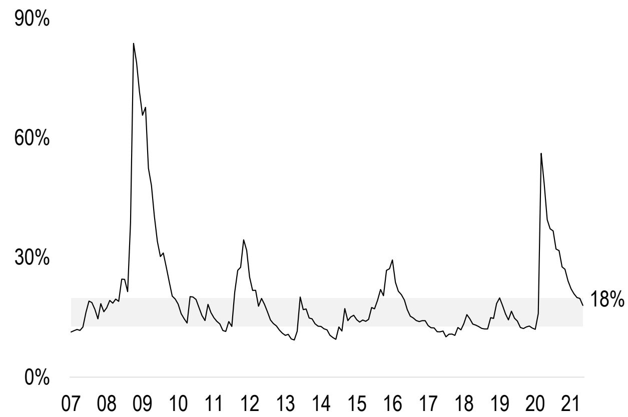
Note: Real expected returns are the mean of the distribution. The red dot is the 5% conditional value-at-risk, expected future losses below the 5% quantile. Shaded area denotes likelihood of positive real returns. Source: Numera Analytics.

F47: Positive real returns - High yield
Likelihood, 12M ahead (%)



Note: Chart tracks probability of positive real returns on S&P energy stocks over a 12M holding period. Last value corresponds to shaded area in F46. Red line is the historical average. Source: Numera Analytics.

F48: Downside risk - High yield
Left-tail risk[2] (5%) - 12M ahead



Note: Chart tracks the (absolute) 5% conditional value-at-risk for 12M investments in US high yield corporate bonds. Shaded band is the interquartile range. Source: Numera Analytics.

Benchmarks and definitions:

1. Benchmarks:

- **Stocks**: Stock market: S&P 500 TR; Information Technology, Financials, Consumer Discretionary, Industrials, Health Care, Communication Services, Consumer Staples, Energy: S&P 500 GICS TR
- **Bonds**: Sovereign bonds: ICE BofAML US Treasury index TR; Investment grade bonds: ICE BofAML US corporate index (all ratings) TR; High yield bonds: ICE BofAML US high yield index (all ratings) TR
- **Deflator**: US consumer price index, all urban consumers (SA)

2. We define left-tail risk as the 5% conditional value-at-risk (cVaR) on 12M investments. The cVaR measures expected future losses below the 5% quantile. It therefore quantifies the *depth* of potential losses when investing in a given asset class.

3. The optimal weights are set to maximize the portfolio's Omega ratio (a measure of investment quality that compares expected returns to downside risk) for 12M holdings. The weights solve a constrained optimization problem via maximum likelihood.

4. The outperformance probability tracks the likelihood of a specific asset class yielding excess returns versus a given benchmark (usually the S&P) over a one-year investment horizon.