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Trends and Developments in the Global Fixed Income markets in 2023

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What are some of the trends we are likely to see in the fixed-income markets in 2023?

If we look at 2023, we're going to see some of the trends that we saw last year continue into this new year. The big one is inflation and the path of inflation. So we have seen it peak over the last few months and we will need to see how that develops over the course of this year. It's interesting to see the decomposition of inflation, be it energy prices, as these have started to tail off. If you look at the price of goods, those have also started to tail off, which is great, but we're still seeing some inflation on the services side. I think that's going to be one of the influences in terms of the markets over the course of this year.

Another aspect to look at is growth and what happens there. We've had very active central banks over the last few months and the impact of them raising rates takes a while to filter through in the economy, call it 12 to 18 months, and that's going to hit us in the middle of this year. So it'll be very interesting to see if central banks are able to engineer a soft landing over the course of this year. I think these are going to be two of the big influences in the market over the course of 2023.

How do you expect Central Banks to change interest rates?

So central banks have got their work cut out this year. If you look at last year, they were behind the curve. They've now caught up and we're going to have to see if they get ahead of the curve over the course of this year. Our expectation is that if you look at the Fed and the European Central Bank and even the Bank of England, we are getting to the tail end of their hiking cycle. If you look at what they've just done, the Fed is probably maybe another 25 basis points for the next meeting, another 25 in May. Then we're expecting to see more of a plateau in terms of rates.

If you look at the European Central Bank, there, are probably another two hikes, but slightly higher given where they are here, maybe 50 basis

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points each. It'll be interesting to see what the Bank of England must do. They've got a much tougher job than the European Central Bank and the Fed at the moment, given the sort of relative growth prospects for the UK. So, it is very much heading towards what we think is going to be the tail end of the hiking cycle over the course of this year.

What other influences will we see on the fixed-income markets in the year ahead?

One of the big changes this year is that we have come out of years of financial repression. We now have yield in the fixed-income markets and yield in some of the more defensive areas of the fixed-income market. And that's a big change and as a result, we are starting to see a bit of a change in terms of investment behaviour. You don't need to be a hero at this point. There are opportunities opening up in markets that have been tougher from a yield perspective in recent years. Just to give you an example, if you go back some 18 months ago, yields on investment-grade European assets were 12 basis points. Now, these are close to 4%. That's a big difference.

So we're starting to see investors that have been a bit more not as invested in the fixed income space, looking at that asset class again, which is great. And we think that a lot of opportunity is opening up there and we've got a yield cushion now on that asset class that we haven't had in recent years. That gives a bit of protection to what is likely still to be quite an exciting year in terms of events.

Where will we find the best value and opportunities?

So, as I mentioned, opportunities have opened up in some of the higher-quality areas of the market in fixed income and we think that this is very interesting. A few examples here that really reflect some of our views, be it in terms of the path of inflation, the path of growth over the course of this year, but global investment grade, looking at 5% or so in that asset class. Interesting asset class to look at. Interesting yields to look at there. We talked about the European investment grade. Again, that's an interesting one, particularly if you look at it hedged in dollars, which adds a little bit of yield, you can get to five, five and a half percent in dollar terms. So again, something interesting to look at.

And I think reflective of the fact that we are expecting a more difficult environment, or at least a slowdown from a growth perspective in other areas that are of interest, the short-dated high yield on the sort of higher end, you can look at yields of 7 or 8% in dollar terms. Again, areas where we can look for income without taking on too much risk at this point. So, we feel that these are interesting areas to look at again when building our portfolios for 2023. ■