

Scenarios Meet Solutions

2024

With inflation at historic highs immediately following the unprecedented Covid period and volatility continually jolting markets, economic uncertainty had been the dominant theme. Though Western Asset's base case expects slowing growth and moderating inflation, we recognize the need to scope out a variety of potential market outcomes. Here we present three distinct scenarios, the likely investment implications and Western Asset's investment solutions that we believe could be most appropriate.



Base Case: Slower Growth, Moderating Inflation

SCENARIO

- Global growth remains resilient with the US slowing but avoiding a recession
- Global inflation continues to recede, in part, on stabilizing commodity prices
- Market expectations for future rate cuts accelerate

INVESTMENT IMPLICATIONS

- In this scenario, we favor high-quality, higher-yielding, diversified strategies for income and total return
- The backdrop here should be particularly favorable for spread products to outperform
- This environment should also be positive for rate compression

SOLUTIONS

- Global Aggregate
- Multi-Asset Credit
- Structured Product
- US Core/Core Plus
- US High Quality High Yield



Optimistic Outlook: A Classic "Goldilocks" Scenario

SCENARIO

- Global growth conditions are buoyed by a China recovery
- US growth achieves a soft landing
- Global inflation surprises to the downside, aided by lower energy prices
- Global financial conditions normalize

INVESTMENT IMPLICATIONS

- This outcome would result in steady economic growth that prevents a recession, but without excessive growth that might fuel too much inflation
- Here we favor corporate bonds and total-return-focused strategies
- Risks to this outlook are more balanced, with the Fed able to guide rates lower to support economic activity
- With the US dollar weakening modestly, we would expect credit spreads to grind tighter

SOLUTIONS

- Emerging Markets Diversified and Local Currency
- Global Credit
- Global Multi-Sector
- US High Yield/Bank Loans
- Macro Opportunities
- Structured Product/US Agency MBS
- US Long Duration/Long Credit



Pessimistic Outlook: Headwinds Intensify

HARD LANDING SCENARIO

- Global growth weakens materially
- Refinancing and default risks rise among various DM corporate and EM sovereign issuers
- The Fed and other central banks bring forward rate cuts to support economic/financial conditions

INVESTMENT IMPLICATIONS

- Here we favor defensive strategies to weather credit-spread widening and increased market volatility

SOLUTIONS

- US Core
- US Government
- US Municipals (High Quality)

STAGFLATION SCENARIO

- Global growth stagnates or decelerates
- Headline and core inflation reaccelerate and remain stickier for longer
- The Fed and other central banks resume hawkish stance and telegraph more rate hikes

INVESTMENT IMPLICATIONS

- In this scenario, we favor cash-based and inflation-protection strategies until inflation momentum shows sustained signs of abating

SOLUTIONS

- Global Inflation-Linked
- US Enhanced Liquidity
- US Liquidity
- US TIPS
- Global & US Short Duration



As of 31 Jan 24.

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