Tactical Asset Allocation

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ADCB بنك أبوظبي التجاري

Staying risk-on in a world of term-premia

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- **Macro backdrop supports a measured risk-on stance, with resilient PMIs, improving earnings visibility, and a shift from hard-landing fears to a slow-grind soft-landing narrative.**
- **Our equity rotation turns more balanced: closing UW Europe as cyclical stabilization emerges and closing OW Asia Pac ex-Japan as semiconductor concentration risks rise.**
- **In fixed income, we favor credit over duration, with an upgrade to EM USD Sovereign IG within TAA and the addition of Core Infrastructure IG for high-quality carry and inflation-linked cash-flow resilience to our focus list.**

Growth

We see global growth staying resilient. Any soft patch is likely to be just that, and not a recession.

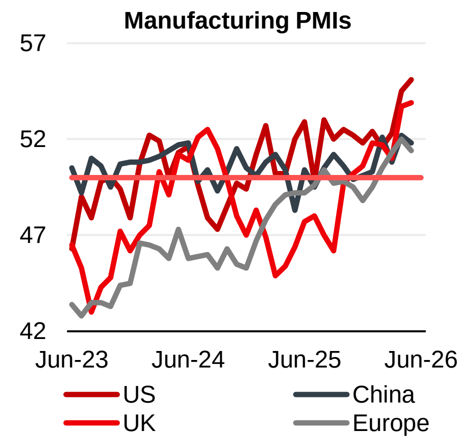
Global growth remains resilient, and in our view, is in a matured early cycle, with recent PMI prints and data surprises highlighting a fragile expansion. S&P Global's latest manufacturing PMI shows global factory output at a near five-year high in May, driven partly by precautionary demand amid commodity and supply concerns, yet the broader flash PMIs for major developed economies point to growth grinding to a halt as the Middle East conflict weighs on confidence and costs. Given this dynamic, a strong divergence between manufacturing and services PMIs has become noticeable. In the US, flash PMIs signal moderating growth, and emerging job cuts, suggesting that the earlier resilience of domestic demand is fading as higher input prices and tighter financial conditions bite. Although, the official jobs data for May in the US surprised significantly on the upside. The eurozone flash PMI indicates a deepening downturn, with output contracting and price pressures reintensifying, consistent with a region facing both external energy shocks and internal structural headwinds. By contrast, emerging markets with strong commodity exposure continue to show relative resilience, supported by terms-of-trade gains and proactive policy frameworks. Overall, the global growth narrative has shifted from a clean disinflationary soft landing to a more complex stagflation-risk environment, where upside surprises in activity are increasingly driven by precautionary behaviour rather than genuine demand strength. Yet we see no signs of an impending recession.

Inflation

The global disinflation trend has stalled rather than reversed, as the Middle East conflict reintroduces a stagflationary impulse via higher energy and transport costs. Rising fuel prices are feeding through to transport, food and fertilizer, while shipping and insurance premia have increased as trade routes are disrupted – broadening the shock beyond crude oil. In the US, headline inflation continues to moderate from its peak, but renewed cost pressures and still elevated services inflation keep the Federal Reserve cautious about declaring victory. The eurozone faces a more uncomfortable mix: weaker real income growth and renewed price pressures, particularly in energy sensitive sectors, as PMIs show output contracting while input prices rise. In sub-Saharan Africa and other fuel importing emerging markets, higher fuel costs are driving a reacceleration of inflation, underscoring the vulnerability of lower income economies to external price shocks. Overall, the inflation narrative has shifted from a straightforward glide path back to target to a stop start process, where geopolitical risks and fiscal dynamics keep medium term inflation expectations and term premia under upward pressure.

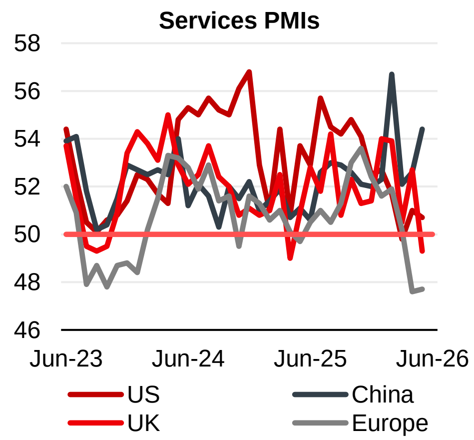
Inflationary risks have risen but we still see a path by which the recent inflationary bump would fade.

Exhibit 01: Manufacturing sector sees improved activity thanks to front-loaded demand



Sources: S&P Global, LSEG Workspace, and ADCB Asset Management

Exhibit 02: Services sector is experiencing softness in certain regions



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Monetary policy

Monetary policy is now characterised by divergence rather than synchronised easing, as central banks balance incomplete disinflation against any softness in growth. Markets have, in recent years, moved from a “lower for longer” view to a regime where long end yields are at multi decade highs, reflecting repricing of inflation, fiscal and policy risks. In the US, the Federal Reserve has effectively adopted a cautious stance: rate cuts are delayed as inflation progress slows and term premia rise, even as growth indicators cool. We do not see rate hikes from the US Fed. The European Central Bank is likely to tighten in the near-term but only to reverse course quickly later. The Bank of England is likely to stay on hold in the near-term while Bank of Japan is likely to deliver a hike before going on hold. In emerging markets, renewed commodity driven inflation and global yield

Distinct feature of the monetary policy outlook is the emerging divergence across key central banks.

repricing limit the pace of accommodation. Overall, policy paths are increasingly idiosyncratic, reinforcing the importance of regional differentiation in tactical asset allocation.

Fiscal policy

Fiscal dynamics are now a primary driver of term structure and risk premia, not a background variable.

Fiscal policy remains a central macro driver, with fragile expansion in major economies contributing to higher term premia and complicating monetary policy. Elevated fiscal deficits in the US and Europe are exerting upward pressure on long term yields, as investors demand greater compensation for duration risk. In the US, expansive fiscal programmes and mid-term policy proposals are reinforcing a narrative of "stabilization at scale", where the neutral rate is being recalibrated higher by markets rather than central banks alone. The eurozone continues to balance fiscal support with debt sustainability concerns. Some emerging markets have improved fiscal frameworks and benefitted from commodity revenues, supporting resilience in hard currency debt despite global yield pressures. However, the combination of higher funding costs and geopolitical uncertainty keeps fiscal space constrained, particularly for lower income sovereigns. All in all, fiscal dynamics are now a primary driver of term structure and risk premia, not a background variable – requiring closer integration of sovereign risk analysis into portfolio construction.

Financial conditions

The cost of capital is higher, and term premia have risen in recent months, reinforcing a regime where quality, cashflow durability and balance sheet strength are key differentiators. However, risk appetite in equities remains surprisingly resilient.

Global financial conditions have stayed easy, as risk appetite in equities remains surprisingly resilient. Long-end bond yields across advanced economies have reached levels not seen in nearly 20 years, reflecting repricing of inflation, fiscal and central bank risks. In the US, the S&P 500 has pushed to new highs despite higher yields, indicating that equity markets are "climbing a wall of worry" and focusing on earnings quality and balance sheet strength. Further, equity markets in the US, Taiwan, and South Korea have benefited from their AI-orientation. The eurozone faces tighter conditions via higher real yields and weaker credit demand, consistent with PMI indicated softness in activity and renewed price pressures. For emerging markets, hard currency debt has shown notable resilience, particularly in countries with robust commodity export profiles and credible fiscal reforms, though funding costs remain above the 2010-2020 average. Overall, the cost of capital is higher, and term premia have risen in recent months, reinforcing a regime where quality, cashflow durability and balance sheet strength are key differentiators. For tactical asset allocation, this environment favours selective risk-taking, disciplined duration management, and a clear preference for assets that can sustain returns without reliance on ultra-low rates.

Tactical Asset Allocation: Risk-on stance with an overweight to equities

The global macro backdrop continues to justify a measured risk-on stance, supported by resilient activity data, improving forward-looking indicators, and still-contained recession probabilities. Recent global PMI releases show manufacturing stabilising above the 50 threshold in several key economies, while services remain expansionary, pointing to a broadening – albeit uneven – growth pulse. Corporate earnings momentum remains constructive, with upward revisions concentrated in technology, industrial automation, and energy-linked sectors. Against this backdrop, equities continue to offer superior risk-adjusted return potential relative to bonds, particularly in an environment where real yields remain elevated but stable. The balance of risks has shifted away from hard landing fears toward a more benign soft landing or "slow-grind" scenario, allowing risk assets to absorb higher rates. This combination of resilient macro data, improving earnings visibility, and supportive liquidity dynamics argues for maintaining an overweight in equities within a diversified multi-asset allocation.

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Rotation within equities: closing UW in Europe and OW in Asia Pacific ex Japan

We close the underweight in Europe as the region shows early signs of cyclical stabilisation. Economic surprises in Europe have bottomed out but remain in the negative territory. Earnings revisions have turned less negative, with cyclicals showing tentative improvement as global trade volumes recover. Although structural headwinds remain – particularly in Germany's industrial sector – the near-term macro flow is less negative, and valuations remain attractive relative to the US. With sentiment already discounting the weakening outlook and potential ECB rate hikes, the risk-reward profile has improved sufficiently to justify closing the underweight.

We close the overweight in Asia Pacific ex-Japan as the region's earlier macro tailwinds are now moderating. Recent performance trends across Asia point to the outperformance from semiconductor-related themes. We think it is time to rebalance the exposures to the semiconductor sectors which have seen disproportionate gains in recent months. With the earlier valuation advantage now less pronounced and concentration risks building in the semiconductors sector, we neutralise the overweight to reflect a more balanced risk-reward profile.

Fixed income: prefer credit risk to duration risk; upgrade EM USD Sovereign IG

We maintain a preference for credit risk over duration risk, consistent with the current macro rate environment. Long-term yields remain structurally higher, reflecting persistent term premia linked to fiscal dynamics, supply-demand imbalances in sovereign issuance, and central banks' slower path toward easing. In the post-pandemic cycle, Global rate structure has shifted into a "higher for longer" equilibrium, with neutral rates likely above pre-pandemic levels. In this environment, duration exposure offers limited convexity benefits unless recession risks rise materially. Conversely, corporate fundamentals remain robust: leverage ratios are stable, interest coverage remains healthy, and default rates are contained. Investment grade and higher quality-high yield spreads remain well-anchored, supported by strong demand from institutional investors and constrained net issuance. This backdrop favours credit carry over duration, particularly in a world where inflation volatility keeps long-end yields sensitive to macro surprises.

We upgrade EM USD sovereign IG to overweight, supported by improving macro fundamentals, attractive carry, and resilient external balances. Many EM sovereigns – particularly in the IG cohort – have strengthened fiscal frameworks, rebuilt FX reserves, and benefitted from favourable terms of trade. EM IG sovereigns have experienced positive rating momentum, with several countries on upgrade watch due to fiscal consolidation and structural reforms. Hard currency EM spreads remain compelling relative to developed market credit, offering attractive compensation for fundamentally improving credit profiles. Moreover, EM external financing conditions can improve as global risk appetite stabilises and commodity prices remain supportive. With default risks concentrated in the lower-rated frontier segment, the IG portion of the EM sovereign universe offers a favourable blend of carry, quality, and diversification. This justifies raising the allocation from neutral to overweight within the fixed income sleeve.

Exhibit 03: We stay risk-on in our TAA (3-6M view) but rotate within equities

	View				
Asset Class	**SUW**	**UW**	**N**	**OW**	**SOW**
Equities				●	
North America				●	
Europe		● →	●		
Japan				●	
APac ex Japan			●	← ●	
EM ex Asia			●		
Fixed Income		●			
DM Treasuries IG		●			
DM Corporate IG			●		
EM USD Sovereigns IG			● →	●	
EM LCY IG			●		
EM Corporate IG			●		
Global HY				●	
Cash		●			

Sources: ADCB Asset Management

Cross-asset focus list

We make the following changes to our cross-asset focus list (see exhibit 04):

- We closed our Nasdaq-100 position after it hit its target of 20% on May 15, 2026.
- We reiterate our conviction on gold and adjust the target and stop loss to reflect the recent volatility in the precious metals space.
- We launch a new fixed income trade idea of long Core Infrastructure IG with a target return of 5% and a stop loss at -3%. Core infrastructure IG bonds are backed by regulated or contracted revenue models, which provide high visibility of cash flows and often include inflation pass-through mechanisms. More than two-thirds of core infrastructure assets have explicit CPI indexation or regulatory frameworks that adjust tariffs with inflation. This makes Core Infra IG one of the few fixed-income segments that naturally hedges inflation volatility without requiring long-duration exposure. Infrastructure IG issuers consistently exhibit lower leverage, stronger interest-coverage ratios, and lower default rates than the broader corporate IG universe. Despite their defensive nature, Core Infra IG bonds continue to trade at a spread premium to similarly rated corporates.

Exhibit 04: Our high conviction tactical investment themes – open and closed positions

New/Open positions	Asset class	RV?	Date opened	Current date	Performance	Target	Stop
Gold	Commodities		2-Feb-26	9-Jun-26	-9.0%	25%	-15%
US Small Caps (Russel 2000)	Equities		6-Oct-25	9-Jun-26	15.3%	20%	-10%
Indian equities	Equities		11-Apr-25	9-Jun-26	-4.5%	20%	-10%
Global Core Infrastructure IG	Fixed Income		9-Jun-26	9-Jun-26	0.0%	5%	-3%
Average					**0.4%**		

Closed positions	Asset class	RV?	Date opened	Closed date	Performance	Target	Stop
Silver	Commodities		15-Oct-25	31-Dec-25	35.1%		
Silver	Commodities		22-Sep-25	15-Oct-25	20.4%	20%	-10%
Copper	Commodities		15-Jun-23	15-Oct-25	26.5%		
Silver	Commodities		10-Jun-25	22-Sep-25	20.6%	20%	-10%
Gold	Commodities		14-Nov-22	14-Jun-23	10.4%		
Commodities average					**22.6%**		
US Large cap Innovation Growth	Equities		26-Mar-26	15-May-26	23.5%	20%	-10%
US Homebuilders	Equities		2-Sep-25	12-Mar-26	-11.0%	20%	-10%
US Small Caps (Russel 2000)	Equities		6-Mar-24	6-Oct-25	20.2%	20%	-15%
High dividend yielders index	Equities		6-Mar-24	10-Jun-25	15.1%	15%	-10%
Gold miner equities	Equities		17-Mar-25	2-Jun-25	20.8%	20%	-10%
SPW relative to SPX	Equities	Yes	6-Mar-24	10-Apr-25	-5.7%	15%	-10%
Gold miner equities	Equities		25-Nov-24	17-Mar-25	22.3%	20%	-10%
HK equities	Equities		14-Nov-22	13-Nov-24	13.3%		
Chinese hotels & leisure	Equities		14-Nov-22	13-Nov-24	-18.6%		
Chinese semiconductors	Equities		22-Mar-23	13-Nov-24	9.0%		
Dow Jones World Cons. Goods	Equities		25-Aug-23	6-Mar-24	1.5%		
Indian equities	Equities		22-May-23	6-Mar-24	31.3%		
Cybersecurity	Equities		22-Mar-23	6-Mar-24	26.9%		
Gold miner equities	Equities		14-Nov-22	14-Jun-23	13.1%		
US Div.banks over US Regional	Equities	Yes	13-Mar-23	13-Jun-23	24.8%		
Equities average					**12.4%**		
US Mortgage Backed Securities	Securitised credit		11-Apr-25	5-Sep-25	5.2%	5%	-5%
UK gilts over other DM Sov.	Rates	Yes	14-Nov-24	1-Sep-25	-2.5%	5%	-5%
UST (7Y-10Y) over other DM Sov.	Rates	Yes	5-Jul-22	13-Nov-24	-1.1%		
EU IG Corp over US IG Corp	Credit	Yes	9-Jan-23	13-Nov-24	6.0%		
Asia investment grade credit	Credit		9-Jan-23	14-Jun-23	1.8%		
Fixed Income average					**1.9%**		
USDJPY	FX		6-Mar-24	26-Apr-24	-6.0%		
GBPUSD higher	FX		15-Jun-23	20-Sep-23	-2.8%		
USDJPY lower	FX		9-Jan-23	14-Jun-23	-5.5%		
GBPEUR lower	FX		9-Jan-23	14-Jun-23	-2.9%		
FX average					**-4.3%**		

Sources: Bloomberg, and ADCB Asset Management

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