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AIP

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The current approach remains defensive due to bond volatility and political risks, holding US healthcare, financials, and US 10-year government bonds at yields above 5.25% until lower volatility, AI spending, and earnings signals justify a positive turn on risk.

Staying defensive and diversified

Time to look for defensive stance on risk assets, locking in gains in semiconductor equities, citing elevated bond volatility, narrowing equity market breadth and rising political uncertainty from the approaching US mid-term elections. Over the past week, the US technology sector-heavy Nasdaq 100 index has suffered its biggest weekly decline in three months after a report showed US consumer inflation accelerated in September, briefly lifting bond yields higher.

When to turn more constructive on stocks?

A more constructive turn on equities when several capitulation signals align i.e. when the Nasdaq 100 index approaches a 10% drawdown, the S&P500 volatility index (VIX) rises into the 25–30 range. Greater confidence would also require easing concerns around AI spending, the technology sector's exposure to neocloud revenue, macro risks and narrow earnings breadth across sectors. Until these conditions emerge, volatility may remain elevated, favouring a defensive equity stance. Political uncertainty should ease once the US mid-term elections are over.

Hot US inflation, but not hot enough for an October Fed hike

US core consumer inflation for September beat estimates, with headline at 3.7% y/y (vs. 3.6% expected) and core at 2.6% (vs. 2.5%). This revives the possibility of an October Fed hike. However, expecting a split Fed to weigh it against a soft September jobs report and narrowly hold later this month. A December hike now looks more of a done deal. Probability remains two more hikes by June 2027.

US government bonds offer value as yields spike

The retracement of US government bond yields after an initial spike following the inflation report suggests there is limited upside in yields. The 10-year government bond yield briefly hit 5.32% after the inflation report before closing materially lower as a sharp decline in equities led to an unwind in bearish bond positions. Expecting a 5.00–5.25% near-term range for the 10-year yield and see spikes above 5.25% as good entry point for US 10-year government bonds. Structural pressures (term premium, fiscal supply) keeps it away from turning outright bullish on longer maturities and continue to prefer 3-7-year maturities for broader bond allocations.

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