September 2018

Voya Multi-Asset Perspectives

U.S. Economic Growth Still Drives Global Expansion

U.S. economic growth continues to drive global expansion: recently, second-quarter U.S. GDP was revised up to 4.2% and the Atlanta Federal Reserve raised its third quarter GDPNow forecast to 4.4%. Corporate capital expenditures are growing at a healthy rate, reflecting the ongoing strength in U.S. corporate earnings. The August ISM report showed manufacturing PMI rising to 61.3, up 3.2 points from July (Figure 1). New orders reached 65.1, having run above 60 since May 2017. Although the outlook for trade is still highly uncertain, fears that tariffs will cause U.S. growth to stall have not materialized. Consumers seem unconcerned: confidence is at its highest since 2000; what's more, the NFIB Small Business Optimism index is at an all-time high. Productivity growth is on an upward trend, which helps contain inflation and extend the economic cycle.

The relentless rise of the U.S. dollar gave up some ground in August on renewed hope of a de-escalation in trade tensions. Extended long positioning in U.S. dollars and an interpretation of some modestly dovish language from the Fed helped too.

The Fed is on path to raise interest rates two more times before the end of the year. July's U.S. Personal Consumption Expenditures (PCE) reading, the Fed's preferred measure of inflation, reached its highest level since 2012. Although real wage growth flattened in the period, tight labor markets and rising nominal GDP growth give the Fed reasons to move forward as projected. Nonetheless, the potential for a pause in rate hikes next year appears to be on the horizon. At the annual Jackson Hole meeting, Fed Chairman Jerome Powell said he does not see an elevated risk of overheating that would require the Fed to tighten policy aggressively. Recent communications suggest the Fed remains indifferent about any spillover effects of volatility in emerging markets.

Volatility has been low in the fixed income market, considering trade tensions and U.S. economic strength. Ten-year U.S. Treasurys have moved sideways in a 25-basis-point range since June. This tells us the bond market is expecting tariffs, if implemented, to have only a small impact on U.S. inflation or growth.

Tactical Indicators

Economic Growth (positive):
Strong ISM reading reflects continued U.S. business expansion

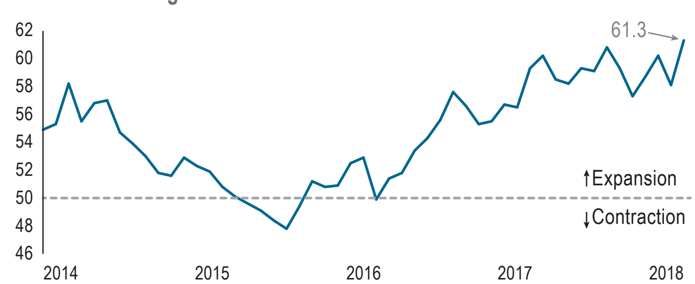
Fundamentals (positive):
Despite rising wage pressures, U.S. profit margins remain resilient

Valuations (neutral):
Strong earnings growth has kept valuations reasonable (Figure 2)

Sentiment (neutral):
While some indicators suggest markets are oversold, the Voya sentiment indicator remains neutral (Figure 3)

Figure 1. U.S. Manufacturing Continues to Power Forward

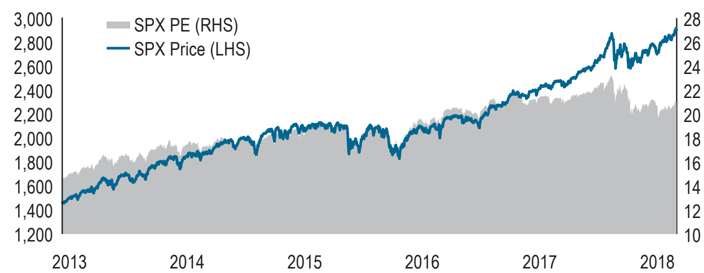
ISM Manufactoring PMI



Source: Bloomberg and Voya Investment Management, as of 8/31/2018

Figure 2. U.S. Stock Valuations Still Look Reasonable

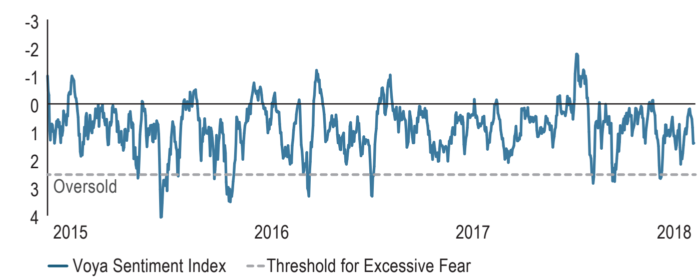
S&P 500 Price vs. P/E Ratio



Source: Bloomberg and Voya Investment Management, as of 8/31/2018

Figure 3. Market Sentiment May Not be so Negative as Certain Indicators Suggest

Voya Sentiment Index



Source: Bloomberg and Voya Investment Management, as of 8/31/2018

Portfolio Positioning

Equities	●	
U.S. Large Cap	○-○-●	Recent contraction in multiples and robust earnings create relative attractiveness versus fixed income
U.S. Mid Cap	○-●-○	Tax reform is fully incorporated into prices from an after-tax profit standpoint
U.S. Small Cap	●-○-○	Large- and small-cap performance divergence appears to be petering out as financial conditions tighten
International Equities	○-○-●	Labor market slack and low inflation, coupled with stabilization in European growth, should support equities
Emerging Market Equities	○-●-○	Less accommodative Fed policy and overseas geopolitical angst is leading to U.S. capital inflows and a resilient U.S. dollar. Although we expect EM volatility to stabilize and markets to move higher, we prefer U.S. assets
REITS	●-○-○	Rising interest rates, full valuations and mature real estate cycle have us underweight
Commodities	○-●-○	Prices are cheaper after large declines in July but trade tensions between the U.S. and China, as well as uncertainty in emerging market growth, have us neutral
Fixed Income	●	
U.S. Core Fixed Income	○-●-○	Tighter Fed policy and stronger economic growth will push yields higher
Non-Investment Grade	●-○-○	Tight spreads offer little value in the face of rising rates. Income potential and floating rate coupon still make senior loans attractive
International Fixed Income	●-○-○	Low absolute and relative yields lead us to favor U.S. bonds

Underweight ● Neutral ● Overweight ●

Investment Outlook: Bears and Bulls

Our Voya recession probability model currently forecasts the likelihood of a U.S. recession over the next 12 months as less than 10%. This provides confidence in our general support for risk assets. The U.S. has continued to exhibit significant strength relative to the rest of the world's equity markets. Earnings strength in the U.S. has been exceptional this year. The three-month earnings revision ratio suggests more upward than downward revisions to estimates. More recently, the index's blistering pace has been decelerating; nonetheless, in terms of visibility, the U.S. retains the lead over other markets.

Our sub-asset class preferences remain directionally the same. However, we have again reduced our near-term outlook for emerging-market equities. Global current activity indicators still point to a flattening of modest improvement in growth outside the U.S. Chinese authorities have begun simulative programs such as tax cuts and reducing reserve requirements. In our view, it may take another three-to-six months for these policy changes to influence any improvement in Chinese data.

From an economic standpoint, Europe seems to be rebounding after a weak first half of 2018. The year-to-date weakness in the euro will likely support growth over the next year. Economic surprise indexes have already turned up, which is consistent with our view that European data are on the mend. We think that if the U.S. dollar can steady, then European equities have a decent chance to play catch-up to U.S. stocks into the end of the year. Having seen the largest outflows of any region over the last six months, Europe appears unloved and undervalued just as the growth news flow is starting to pick up.

From a seasonality perspective, September and October can be especially volatile for equities; this year is unlikely to be an exception to that historical generalization. The comment period on the trade tariffs against China is concluding and the U.S. mid-term elections put some near-term uncertainty into the markets. Notwithstanding these considerations, strong U.S. economic fundamentals and the expected path of interest rates keep us overweight in equities and underweight in fixed income.

Past performance does not guarantee future results.

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