
INVESTMENT OUTLOOK

Q4 2023

Testing the Economy's Limits

How resilient is the U.S. economy?



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*Chief Investment Officer
American Century Investments*

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INTRODUCTION

Is the Soft Landing a Fairy Tale?



VICTOR ZHANG

Chief Investment Officer
American Century Investments

From the outset of the Federal Reserve's (Fed's) rate-hike regime in March 2022, pundits didn't like the central bank's chances of taming inflation without crashing the economy. Skepticism about the potential for a Goldilocks-style soft landing grew as inflation climbed to 40-year highs and proved stickier than many expected. Recession worries reached a fever pitch as 2022 closed with sharp losses for stocks and bonds.

But something happened on the road to perdition. Some 18 months after the Fed's first hike, economic growth remains positive, inflation is cooling, the labor market is strong and consumers continue to spend. Corporate earnings are weakening, but the market is behaving like the worst is behind us, and stocks across the globe are on pace for a solid year as of early September.

Is this the soft landing?

Not So Fast, Goldilocks

Even though the economy and the market have turned out to be resilient, we're not out of the woods yet. Rates rose at an unprecedented pace, but Fed governors caution that there's a "long and variable lag" for a rate hike's full effect to hit the real economy.

Indeed, we estimate that only about 60% of the hikes have taken hold, with the effects of the entire campaign playing out into 2024. Considering this delayed impact, along with the inverted yield curve, weakening housing market and declining manufacturing activity, we still think a recession is the most likely economic outcome.

Investing with a Recession in Mind

In this issue of Investment Outlook, our chief investment officers discuss the risks and opportunities that come with an uncertain economic backdrop.

- Inflation may be receding, but we don't expect it to fall to the Fed's target level any time soon. Therefore, we're not counting on a quick policy pivot, and we're still emphasizing quality and extending duration in our bond portfolios.
- Security selection is paramount. Businesses aren't equally prepared to handle a recession, so our teams are looking for companies that can fund their operations and sustain their profit growth through a downturn.
- Artificial intelligence is grabbing headlines, but growth opportunities lie elsewhere. Other notable themes include the strong rebound in travel and mobility and the onshoring and nearshoring trends.
- Inflation hasn't been as stubborn in emerging economies as developed markets. Emerging markets central banks may have room to ease monetary policy to fuel economic growth heading into next year.

Though the economy and the markets have been resilient in 2023, we urge our clients to proceed cautiously. Given the uncertain outlook, we think the watchwords remain balance, diversification and risk management.

Thank you for entrusting us with your capital.

KEY TAKEAWAYS

We still think a modest recession is likely given the inverted yield curve, weakening housing market, declining manufacturing activity and the delayed impact of aggressive interest rate hikes.

Catastrophic losses have pressured large insurers, but regulatory relief to raise prices may allow well-capitalized insurance companies to rebound.

KEY TAKEAWAYS

Expect rates to remain higher for longer. The fastest series of rate hikes in 40 years will likely slow down the economy, but we don't think policymakers will quickly pivot to easing unless something in the economy breaks.


Emerging markets inflation has been less sticky than in developed markets. EM central banks have room to begin easing monetary policy, potentially propelling EM economic growth into 2024.

Uncertainty keeps the emphasis on bond quality. We remain selective and focused on higher-quality securities, and we believe extending duration remains a prudent strategy.

Artificial intelligence is a big thing, but not the only thing. Selective opportunities can be found in other corners of the market, including businesses tied to such themes as the strong rebound in travel and mobility and the onshoring and nearshoring trends.

The upward trend in the semiconductor cycle could have staying power. Forecasts project annual demand growth for chips and chipmaking equipment in the high single-digit range through 2030, which should bode well for Asian markets.

GLOBAL MACROECONOMIC OUTLOOK

A satellite view of Earth at night, showing the illuminated continents of North and South America. The city lights are visible as a dense pattern of yellow and white dots. The Earth's blue atmosphere is visible at the top and right edges of the frame. The background is a dark, starry space.

GLOBAL MACROECONOMIC OUTLOOK

GLOBAL ECONOMY

Recession remains on the radar.

Growth Slowdown Is in Store

Despite tighter financial conditions, gross domestic product and corporate earnings have exceeded expectations, the labor market has remained strong, and consumers have continued to spend. However, cracks are emerging. Certain key indicators, including housing and manufacturing, have been struggling, suggesting a slowdown may be imminent. It can take nine to 24 months for the economy to feel the full effects of each Fed rate hike. Accordingly, we believe a recession is still forthcoming and likely will be evident by early 2024.

European, U.K. Economies Remain Fragile

Weakness in the European Union's export-centric countries continues to threaten economic activity in the eurozone. The manufacturing and services sectors have contracted, amplifying recession risk. Rising interest rates and still-high inflation are also stifling growth. A similar situation is unfolding in the U.K., where inflation remains elevated and interest rates recently hit a 15-year high. Economic growth has been modest for several quarters, and hiring has slowed amid a labor shortage. We believe this dynamic exacerbates the risk of stagflation.

China's Recovery Is Losing Steam

China's economy has been disappointing, with mounting concerns the government will fail to reach its 2023 growth target. All the piecemeal monetary and fiscal stimuli have failed to overcome the headwinds from structural issues. Recently, youth unemployment soared to a record 23%, consumer and producer prices declined, and the nation's imports and exports contracted. An anticipated domestic spending rebound following the lifting of COVID-19 lockdowns never fully materialized, due to decreasing income, waning confidence and a sinking property market. Real estate sales have plunged, while the financial woes of China's property developers are at risk of spreading.

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It can take nine to 24 months for the economy to feel the full effects of each Fed rate hike.

GLOBAL MACROECONOMIC OUTLOOK

INFLATION

Prices ease, but not enough.

Fed's Inflation Target Remains Elusive

While inflation has slowed considerably from last year's multidecade highs, it remains well above the Fed's target. Persistent wage pressures suggest services inflation may remain resilient. Shelter prices, which are lagging indicators, should slowly ease to historical levels. We believe goods prices will continue to fuel inflation but moderate over time. In this environment, we still favor short-maturity inflation-linked securities, given still-strong pricing momentum in services components and risks from the energy sector.

Inflation Stays High in Europe

Alongside weakening growth, stubbornly high inflation has challenged economies and central banks in the eurozone and the U.K. Year-over-year inflation rates have eased faster in the eurozone than in the U.K. but remain far from central bank targets. Inflation rates in the U.K. and the eurozone have been notably higher than in the U.S. Elevated food, rent and services prices have been key culprits, while falling energy prices have helped slow headline inflation. Additionally, wage growth has pressured a broad range of prices, suggesting inflation may be entrenched, particularly in the U.K. economy.

China Inflation Rate Sinks

As Western nations struggle with persistent above-target inflation, consumer prices in China have fallen. The nation's consumer price index recently logged its first year-over-year decline since February 2021. Food prices, the index's largest component, plunged almost 2%, while housing, the second-largest component, was nearly flat. Officials insist the decline will be temporary and inflation should pick up slowly as the effects of a high base in 2022 fade. Inflation in other emerging markets (EM) generally has eased further, allowing some central banks to start cutting rates. We expect inflation in most markets to move toward central bank targets absent of energy or food shocks.

GLOBAL MACROECONOMIC OUTLOOK

MONETARY POLICY

Central banks are still in play.

Fed Is on the Fence

In the fastest series of rate hikes in four decades, the Fed has pushed interest rates to a 22-year high. Yet the central bank hasn't yet officially ended its rate-hike campaign. Inflation still exceeds the Fed's comfort zone, and the economy has remained surprisingly resilient. Some Fed officials worry about the economic fallout of tightening further. Others believe additional rate hikes are needed to keep combating above-target inflation. In our view, the significant tightening to date should slow the economy and eventually trigger a recession. But it's unlikely policymakers will quickly pivot to easing, leaving rates higher for longer.

Europe, U.K. Policymakers Face Tough Choices

Amid its fastest tightening pace in history, the European Central Bank (ECB) committed to keeping rates restrictive until inflation slows to 2%. But policymakers recently acknowledged the marked slowing of growth. The Bank of England remained hawkish after announcing its 14th consecutive rate hike in August. Growth in the eurozone and the U.K. has slowed considerably, bordering on recession, while inflation remains well above central bank targets. Against this backdrop, a recent larger-than-expected decline in eurozone business activity may keep the ECB on the sidelines. In the U.K., wages have soared, fueling expectations for more tightening.

China Seeks Economic Turnaround

To boost China's weakening economy, the People's Bank of China recently cut key lending rates. Policymakers have indicated they seek to boost liquidity, lower financing costs and support the currency amid slowing business activity, deflationary worries and weak trade. They also reiterated the urgency of meeting China's economic goals. Elsewhere, many EM central banks that were aggressive in hiking rates to combat inflation have ended or are close to ending their tightening campaigns. EM central banks must balance the need to support growth amid lower inflation against pressures on currency and financing.

GLOBAL MACROECONOMIC OUTLOOK

INTEREST RATES

Yields reach multiyear highs.

Rate Outlook Highlights Duration

Fed policy, high inflation and better-than-expected economic data have driven U.S. bond yields to multiyear highs. Additionally, the Treasury Department's much larger-than-expected borrowing needs have pushed longer-maturity yields even higher. But we believe the Fed is likely finished tightening, which should help stabilize shorter-maturity Treasury yields. As growth ultimately slows, yields across the curve likely will decline, highlighting the potential advantages of extending portfolio duration. We also believe reinvestment risk is rising for investors with large cash balances, underscoring the potential benefits of shifting into intermediate-maturity bonds before yields head lower.

Yield Curve Opportunities Emerge in Europe, U.K.

Elevated inflation and additional central bank tightening should continue to pressure shorter maturity European and U.K. government bond yields, even as recession risk escalates. Longer-maturity bonds should begin to stabilize and may continue to outperform U.S. Treasuries as investors factor in a likely recession and an eventual pause in central bank policy. Yields in semicore countries, such as Finland and Ireland, have been attractive versus core countries, while peripheral countries may underperform as quantitative tightening support fades. We expect eurozone and U.K. rates to peak in 2023's second half as growth slows and rate-hike campaigns conclude.

EM Yield Advantages Remain but Challenges Surface

We continue to see a much better environment for local currency EM bonds. EM inflation has trended in the right direction, allowing for more policy easing. EM yield advantages and peak repricing of global risk-free rates have provided further tailwinds. We expect countries with high real yields, steep yield curves and low betas to outperform China, where we expect further fiscal stimulus. Rate cuts, weaker Chinese data and the risk of a major slowdown in developed markets, together with higher volatility and low liquidity, will challenge EM currencies.

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***Emerging markets
inflation has
trended in the
right direction,
allowing for more
policy easing.***

U.S. EQUITY



U.S. EQUITY



KEITH LEE, CFA
Co-Chief Investment Officer
Global Growth Equity

MARKET DIRECTION HINGES ON CORPORATE EARNINGS

We believe the key driver for market direction will be future earnings growth. As of late August, expectations are for earnings-per-share (EPS) growth of 10% for the S&P 500® Index for 2024. EPS estimates are even higher for the Russell 1000® Growth Index at 14%. We think these numbers are high given the level of interest rates, the shape of the yield curve and the pace of economic growth.

If the forecasts turn out to be correct, then the market is fairly valued or only slightly expensive. The implication is that valuations aren't bad but assumes companies hit those aggressive earnings expectations. It also implies that a recession isn't priced in. As a result, any obvious slowdown in growth or further rate hikes would likely create market volatility.

Assessing Financial Strength as Borrowing Costs Rise

We recognize that the cost of capital is going up, and the Federal Reserve (Fed) is committed to keeping rates higher for longer. Because rates are high and a recession is possible, we believe corporate balance sheet strength and interest expense are key. That's why we're looking for companies with the financial strength to navigate an extended period of economic weakness.

We're keenly focused on whether the companies we own have balance sheet strength. We look for cash on the balance sheet and a company's ability to fund its growth. We want to know whether they generate enough cash or have enough cash to fund operations if there's a recession.

Bottom-Up Strategies for Identifying Innovative Companies

When talking about macroeconomic conditions, there's a temptation to think in terms of top-down positioning. Top-down investing would lead investors to own the most durable business models with the least earnings volatility, highest visibility and lowest expectations and, therefore lowest valuations.

U.S. EQUITY

We think every recession is different and individual companies will respond differently. Today, the labor market is strong, wages are rising and inflation remains elevated. That's characteristic of a stagflationary environment and not a traditional deflationary recession.

Consider another megatrend: demographic change characterized by graying populations all over the developed world. This raises the challenge of fewer workers to support growing entitlement expenses.

We think society will solve stagflation and the shrinking labor force through technology-driven productivity gains. Indeed, we're finding opportunities in companies developing new products and technologies transforming entire sectors and industries. We don't view these as top-down solutions. Instead, we rely on bottom-up, fundamental research to identify individual companies innovating and reimagining their competitive landscapes.

GLOBAL EQUITY



GLOBAL VALUE EQUITY



KEVIN TONEY, CFA
Chief Investment Officer
Global Value Equity

CATASTROPHIC LOSSES RESHAPE OPPORTUNITIES FOR INSURERS

California's slow wildfire season this year felt like a reprieve of sorts for a state often afflicted by natural disasters.

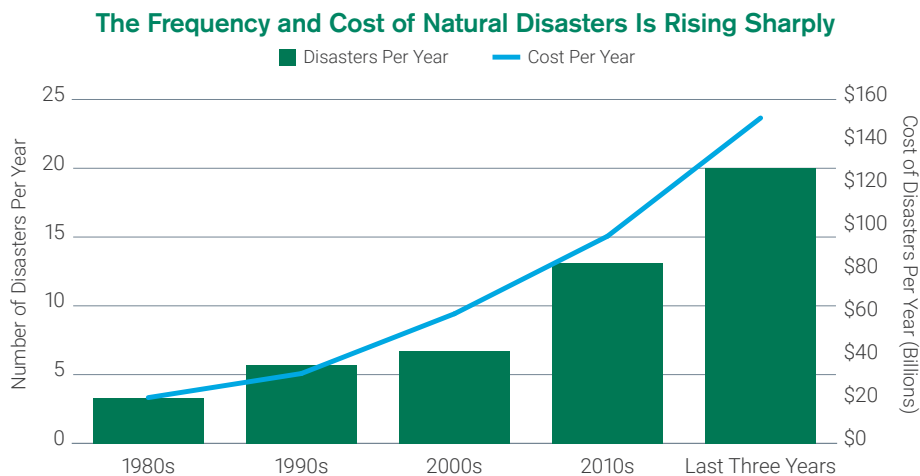
Then came a tropical storm in August. Tropical Storm Hilary, the first of its type to hit Southern California since 1939, flooded the region.

The immediate and most obvious effect of these catastrophes falls on those who have to recoup what they've lost. That pain makes its way upward to insurance companies, some of which doubt how much they want to keep doing business in the state.

The Golden State Highlights Challenges for Insurance Companies

California is a microcosm of the broader near-term troubles confronting U.S. insurance companies.

As the chart below shows, an increasing number of severe catastrophes has brought on more claims by insureds.



Source: NOAA National Centers for Environmental Information. Data as of 9/11/2023.

GLOBAL VALUE EQUITY

Inflation and supply chain issues during the last two years have made the replacement cost of insuring damaged property much more expensive, whether or not the loss is tied to a natural disaster.

Higher prices for construction materials have made it more expensive for insurance companies to pay to rebuild homes. Rising automobile costs have made it more costly to replace damaged cars.

In these circumstances, insurers ask state regulators to increase premiums to offset the losses. Some state regulators — again, California is a prime example — have been largely reluctant to raise them.

The ill effects on insurance companies show up on their earnings reports.

State Farm in February reported a 130% combined loss ratio in automobile insurance. That means State Farm lost 30 cents for each dollar of automobile premiums it wrote in 2022.

Allstate reported a net loss of \$1.4 billion in the second quarter of 2023 because of severe weather.

Insurers Are Leaving California

Allstate's share price tumbled 17% year to date. That seems troublesome, but as value investors, we see opportunities in well-capitalized insurance companies that can withstand the industry's challenges.

For one thing, State Farm announced in May that it would stop selling new home insurance policies in California. In a statement, it said historic increases in construction costs and rapidly growing exposure to catastrophes drove its decision to curtail its business in the disaster-prone state.

California's insurance commissioner started approving rate increases toward the end of 2022 after holding rates largely steady after the onset of the pandemic. Kemper Insurance, a property and casualty insurer, won a 30% rate increase from California regulators.

GLOBAL VALUE EQUITY

What's Next for the Insurance Industry?

We think State Farm fleeing California will cause regulators to approve more rate increases, which will give remaining insurance companies better pricing power in the future.

If these dynamics play out in California and elsewhere, we think well-capitalized insurance companies may have an opportunity to recoup their losses from recent quarters. If inflation continues to cool, insurance companies may receive an additional boost to profitability in future quarters if claims cost less to settle.

Insurance companies face real challenges. Managing and accounting for risk in an increasingly unpredictable world is no easy task. But we think patient and selective investors may see future opportunities in this sector.

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GLOBAL GROWTH EQUITY



PATRICIA RIBEIRO

Co-Chief Investment Officer
Global Growth Equity

ECONOMIC GROWTH, INFLATION AND INTEREST RATES **REMAIN IN FOCUS**

Global investors will remain focused on three closely linked macroeconomic indicators: the pace of economic growth, level of inflation and direction of interest rates. A U.S. economy that appears more resilient than we expected has somewhat altered our views on these factors.

U.S. inflation has moderated considerably, thanks to the Federal Reserve's (Fed's) interest rate increases. Yet amid the rate-hike campaign, the U.S. economy has continued expanding at a stronger rate than many expected. The degree to which consumer spending levels remain intact will guide growth prospects.

The economy's resilience provided the backdrop for Chair Jerome Powell's speech at the Fed's annual conference in Jackson Hole, Wyo. Powell declared the Fed would remain vigilant on inflation "until the job is done," indicating it would consider additional rate hikes if economic data warrants them.

High Interest Rates May Linger

Though the U.S. economy has been resilient, slowing growth remains likely, particularly with the possibility that higher interest rates will remain elevated for an extended period.

Recent layoffs in the financial and information technology sectors have helped trigger a slight increase in weekly jobless claims. Meanwhile, rising credit card debt and declining savings suggest consumers largely have spent the cash they accrued during the pandemic.

Outside the U.S., the Bank of Japan's recent pivot from ultra-accommodative monetary policy suggests its interest rates may increase. That may ease the strongest appetite for Japanese equities in decades. Eurozone inflation still exceeds long-term targets. As a result, rates there may remain elevated despite slowing growth that will remain challenged by the war in Ukraine and weakening demand from China.

GLOBAL GROWTH EQUITY

Narrow Equity Market Leadership Requires Selectivity

Global equity market gains in 2023 primarily reflect a group of technology stocks riding the wave of exploding interest in artificial intelligence (AI). In this landscape, selectivity remains paramount.

Nevertheless, opportunities exist outside the realm of AI. Global travel and mobility have rebounded from pandemic limitations. Airline traffic has surged, with a corresponding impact on orders for new jets and related equipment, which has driven solid performance for stocks in companies supplying them.

The desire of North American companies to move supply sources and production closer to home also represents an important theme. This push for improved supply-chain stability has fed the onshoring/nearshoring trend. It's one that should benefit suppliers and manufacturers in the U.S., Canada and Mexico.

GLOBAL GROWTH EQUITY

CHINA ASIDE, THERE'S LIGHT AHEAD FOR EMERGING MARKETS

Amid Rapid Disinflation, Easier Monetary Policy May Be on Deck

Inflation hasn't proven as stubborn to arrest in most emerging economies, with deflation actually now arising as a concern in China. Consequently, central banks have room to begin easing monetary policy, potentially propelling EM economic growth into 2024.

China's economy remains problematic. The recovery from strict pandemic restrictions lifted late last year proved shorter and weaker than expected. That has prompted calls for fiscal stimulus and measures to support a languishing property market. Such action would sustain investment growth. Still, we think China's equity market likely will remain volatile, even amid increased activity in the services sector and a recent uptick in weak consumer confidence.

Latin America, led by Brazil, seems poised to lead the way for emerging markets in the months ahead. Inflation has moderated broadly and will support a reduction in central bank rate cuts throughout the region. Conversely, Turkey finally has raised interest rates to quell inflation as steady growth has continued despite devastating earthquakes earlier this year.

Road to Recovery for Commodities?

Commodities prices and emerging equities markets tend to rise and fall in tandem. Though spot commodity values have lagged the rebound in equity markets that began last year, this gap appears as if it may soon close.

If it does, South Africa's otherwise challenging economic environment could improve. Other emerging markets heavily reliant on commodity production, including many in Latin America, also would receive a boost.

That's certainly the case for rare earth metals such as lithium, nickel and cobalt. These building blocks for electric vehicle batteries should benefit amid the broader

GLOBAL GROWTH EQUITY

global decarbonization trend. Financial incentives targeting climate change in last year's Inflation Reduction Act aid companies participating in this trend.

Semiconductor Cycle Turns Promising

Global demand for semiconductors has declined sharply from a late 2021 peak but finally appears on the verge of rebounding. Rising demand for electronics and other end markets, including autos and data centers, should help shrink bloated inventories. In addition, producers of chips for specialized AI applications face overwhelming orders.

An upward turn in the chip cycle could last; forecasts project annual demand growth in the high single-digit range through 2030. That would bode well for Asian markets focused on chip production, including Taiwan.

More broadly, the push in developed markets to diversify supply sources for semiconductors should aid industrial and manufacturing firms involved in building out that additional production.

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GLOBAL
FIXED INCOME



GLOBAL FIXED INCOME



JOHN LOVITO
Co-Chief Investment Officer
Global Fixed Income



CHARLES TAN
Co-Chief Investment Officer
Global Fixed Income

U.S. RECESSION APPEARS **INEVITABLE**

Many market pundits have abandoned their recession calls, viewing resilient U.S. gross domestic product and labor market data as a soft-landing signal. We don't share that view.

So far, multiyear highs in inflation and interest rates have been unable to halt the nation's economic output. However, the economy's luck may be fading, partly due to the magnitude of the Federal Reserve's (Fed's) tightening campaign. In a 16-month span, policymakers lifted interest rates 5.25 percentage points — the fastest tightening pace since the 1980s.

In addition, while the monthly year-over-year inflation rate has slowed, consumer prices are up nearly 17% on a cumulative basis since January 2021, according to the Bureau of Labor Statistics. Furthermore, slowing manufacturing, consumer, housing and corporate profits data suggest we're in the late stages of the economic cycle.

Also, the U.S. Treasury yield curve — a key recession indicator — has been inverted for more than a year. While the timing between curve inversion and an economic downturn has differed widely, a negatively sloping yield curve has preceded every recession since the 1970s.

Rate Hike Lag Time Is Narrowing

Given our economic outlook, we remain selective and focused on higher-quality bonds. We also believe extending duration remains a prudent strategy in this environment.

GLOBAL FIXED INCOME

In our view, a modest recession appears the most likely outcome. This backdrop should push Treasury yields lower and credit spreads wider. Inflation should continue to moderate, but we don't expect it to fall to the Fed's target level any time soon.

For that reason, we don't expect a quick policy pivot from the Fed. Policymakers likely will hold interest rates steady for an extended period, unless the recession proves more severe than expected or another crisis unfolds.

Outlook Favors Quality, Longer Duration

Given our economic outlook, we remain selective and focused on higher-quality bonds. We also believe extending duration remains a prudent strategy in this environment.

Here's how this approach is driving our sector teams' investment decisions:

U.S. Government

Fed policy, inflation and robust economic data have driven Treasury yields to multiyear highs. But with an economic slowdown likely unfolding in the coming months, these yields should follow suit. In particular, intermediate-maturity Treasury yields appear close to peak levels. Therefore, we see value in extending duration. With inflation likely to remain above target, we also believe short-maturity Treasury inflation-protected securities (TIPS) offer value.

U.S. Securitized

We continue to favor short-maturity, senior securitized credit issues offering strong relative value and risk/reward profiles. While we are mitigating exposure to office and retail subsectors of the commercial mortgage-backed securities (CMBS) market, we continue to see value in multifamily housing and select industrial properties. We're avoiding consumer-driven asset-backed securities (ABS) in favor of aircraft and data infrastructure assets. On a relative basis, agency mortgage-backed securities (MBS) valuations appear compelling, and the sector's defensive nature makes it an increasingly attractive asset class. However, technical factors, such as bank balance sheet activity and the Fed's quantitative tightening, present potential headwinds.

GLOBAL FIXED INCOME

U.S. Corporate

We remain defensively positioned as the credit cycle shifts to lower growth. We don't think the risk of tighter lending conditions is reflected in valuations. We remain neutral toward banking as higher rates pressure margins. We favor high-quality credits in the electric, construction and machinery, food and beverage and consumer products industries. Overall, with spreads likely to widen, we're seeking opportunities offering risk management, low event risk and less cyclical exposure.

Municipal

We expect municipal credit fundamentals to remain durable, supported by reserve fund balances and unspent federal recovery funds. Favorable credit trends generally have moderated, while year-over-year real revenue collections for most states have peaked. In terms of portfolio positioning, we're maintaining a neutral to slightly long duration and may extend interest rate risk as valuations improve. We generally favor higher-quality issuers and sectors and believe security selection remains key to performance, particularly among lower-rated issuers.

Money Markets

We expect to see a resurgence of yield curve inversion, especially as it's clear the Fed's hiking cycle is complete. Ahead of that, we expect to have more appetite for longer-maturity securities, such as 12- to 13-month paper. Historically, the Fed often cuts rates fairly quickly after reaching the terminal rate. If this trend persists, we expect rate cuts in the second or third quarter of 2024. This increases our demand for locking in yields for longer across Treasury bills and credit securities. Meanwhile, we expect to remain close to neutral on overall Treasury and credit positioning, actively and opportunistically seeking pricing dislocations.

Non-U.S. Developed Markets

We believe European inflation is peaking and therefore see value in long-maturity euro-denominated yields in core countries. We expect the European Central Bank to pause its rate hike campaign due to cooling inflation data. Therefore, we recently initiated a moderate duration overweight via German bunds while maintaining our overweight in semicore countries. The region's growth outlook remains weak, and we believe recession is likely. Elsewhere, we have increased our duration overweight in New Zealand, expecting inflation to peak and the central bank to end its hiking campaign.

GLOBAL FIXED INCOME

Emerging Markets (EM)

Given heightened global uncertainties, we're keeping risk exposure at the lower end of our target range. Overall, emerging markets (EM) inflation is easing, which provides further tailwinds for renewed EM allocations. We still expect a better environment for local currency EM bonds versus external bonds. We believe some low-beta countries and those with high real yields may outperform. In our view, they will have higher correlation to U.S. duration and more space to ease once markets price in a U.S. recession. We prefer countries with steep curves and real rate cushions, such as Mexico, Indonesia, Brazil and South Africa. We are underweighting China due to expectations for additional fiscal support.



**MULTI-ASSET
STRATEGIES**

MULTI-ASSET STRATEGIES



RICH WEISS

Chief Investment Officer
Multi-Asset Strategies

IS THE ECONOMY HEADED FOR A **HARD** OR **SOFT** LANDING?

From the beginning of the tightening campaign to tame inflation, market participants have pondered which economic scenario would play out: a hard landing or a soft landing.

The economic hard-landing scenario involves an economy that careens into recession, while stocks and economically sensitive corporate bonds struggle. A soft landing would mean that the economy continues to grow — even if only modestly — while inflation moderates, allowing stocks and bonds to continue to do well.

Soft Landing Case Rests on Backward-Looking Data

The argument for a soft landing rests on several pillars. These include better-than-expected corporate earnings, a strong labor market, continued steady consumer spending and a slowdown in the rate of inflation. The important thing to note about these statistics, however, is that they're all backward looking. They're useful for telling us where we've been, but less good at indicating where we're going.

Indeed, the Federal Reserve's (Fed's) own GDPNow estimate of third-quarter growth based on current economic indicators is 5.6%. Note that it's called a "nowcast" as opposed to a forecast because it relies on already observed variables without factoring in expectations for future figures.

In our view, the fact that it is based on historical data and doesn't include any forward estimates is precisely the disconnect between the hard and soft landing camps. For example, contrast that 5.6% number with the sub-2% forecast of leading economists shown in the Blue Chip Financial Forecasts.

Hard-Landing Argument Is Broad-Based

In contrast, many of the best forward-looking indicators we know are pointing down. The yield curve (a graphic representation of bond yields at different maturities) is pointing down, the housing market faces an affordability crisis and manufacturing activity has declined for nine straight months through July. Any one of these would be a flashing economic warning signal, but all three together make an ominous sign.

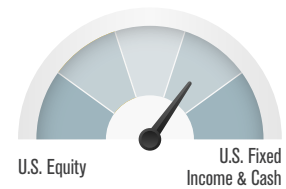
MULTI-ASSET STRATEGIES

But perhaps the single most important argument for a hard landing ahead is the lagged effect of Fed rate hikes. A good rule of thumb is that it takes around 18 months for the Fed's rate changes to show up in the real economy. It turns out that the Fed's first hike in this cycle was in March 2022, or exactly 18 months ago.

If the effect of the Fed's rate increases flows into the economy gradually over 18 months, then fully a third of the Fed's rate hikes are yet to be felt. The long lag between policy changes and economic effect is a key reason why we believe the recession is still ahead of us.

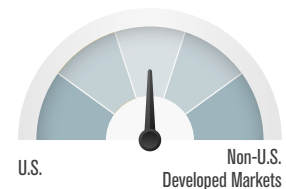
ASSET CLASS

We maintain a strong preference for cash relative to bonds and some stocks. An inverted yield curve necessarily means that cash and shorter-term investments offer attractive yields relative to longer-term bonds. Cash yields also look compelling relative to stock earnings yields. In addition, stock market momentum stalled in August, further reducing equities' appeal. Qualitatively, negative leading economic indicators also cloud the outlook for stocks relative to alternative, safer investments, like cash. Within equities we are emphasizing an underweight to real estate investment trusts (REITs).

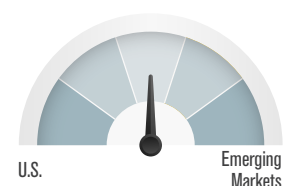


EQUITY REGION

We recently closed out our beneficial overweight to non-U.S. developed market equities relative to U.S. stocks. Our momentum metrics favor the U.S. over European equities, while relative interest rates favor Europe. Real rates in the EU are negative, which supports risk assets. But in the U.S., real rates are flat or positive, depending on which measure of inflation you use. The net effect of these factors is that we're neutral for now.



We have returned to neutral on emerging markets after benefiting from an overweight to U.S. equities in recent months. In our view, macro conditions favor U.S. equity while credit and company fundamentals favor emerging markets at the margin, rendering a neutral reading. China remains a question mark. Growth there is disappointing, but the country's leaders appear to want to strike a balance between doing too little and unleashing another huge wave of stimulus.



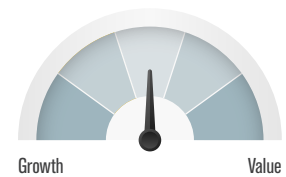
MULTI-ASSET STRATEGIES

U.S. EQUITY SIZE & STYLE

Our small/large model is close to neutral on every dimension we measure, from relative valuations, earnings and sentiment to a range of macroeconomic indicators. From a qualitative point of view, it's hard to favor small-cap stocks when we believe a recession is likely. In such a scenario, large multinationals would be more attractive for their diversified markets and lines of business.

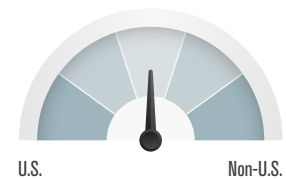


We recently removed our value overweight, which was beneficial in 2022 but detracted in 2023. This environment points up the importance of individual security selection. From a growth point of view, the dominance of the “magnificent seven” have distorted the performance picture for growth stocks more broadly. Value, too, has had performance challenges resulting from a single sector — banks. These conditions create opportunities in less-appreciated businesses across both growth and value.



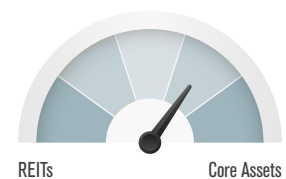
FIXED INCOME

Recession remains the most likely outcome in our view, and we expect this will eventually weigh on corporate bonds. In most scenarios, we see inflation remaining above historical trend levels. As a result, we still see the best value in the short end of the inflation curve. The Fed is likely nearing the end of its tightening cycle. Once hikes are complete we expect an extended pause unless a new crisis emerges. The market likely will factor in rate cuts once it becomes confident the Fed has reached its peak rate.



ALTERNATIVES

Within equities, our highest conviction position is an underweight to real estate investment trusts (REITs). Our global REITs managers continue to find relative value opportunities by region and sector and from security to security. But broadly speaking, economic uncertainty presents fundamental challenges for REITs at a time when cash yields, in particular, are so compelling. Our long-running REITs underweight has been a significant contributor over time.



SUSTAINABLE INVESTING TRENDS



SUSTAINABLE INVESTING TRENDS



SARAH BRATTON HUGHES
Head of Sustainable Investing

CLIMATE ADAPTATION AND INNOVATION **CAN'T WAIT UNTIL 2050**

Climate-focused carbon-emission goals, along with most investors, continue to focus on achieving “Net Zero ” by 2050. In our opinion, based on the current trajectory, the 2050 goal is looking less and less feasible, which has serious economic and societal implications.

Although setting a target 25+ years down the road may seem reasonable given the magnitude of the challenge, it's also misleading. We believe investors should be increasingly focused on climate adaptation and innovation now as globally shifting weather patterns are having a material impact on investor returns today.

Climate Change Costs Are Rising

Whether you attribute weather shifts to climate change, El Niño/La Niña, volcanic ash or something else, the result is the same. The problem is financially material and affects profitability for companies in many sectors as costs increase and consumers adjust their behaviors.

The scale and impact of changing global weather continue to rise. Reinsurance provider Munich Re cited losses in 2020 of around \$270 billion, following losses of \$320 billion the previous year. Its insured losses were roughly \$120 billion in both years. Thus far, 2023 has seen the hottest July on record, devastating hurricanes, floods and drought, as well as raging wildfires in Hawaii, Canada and Europe — resulting in human, economic, and biodiversity loss, and worsening health problems worldwide.

Select Markets Are Nearly Uninsurable

The U.S. real estate market is grappling with insurance premiums that have increased by 20% or more to cover higher weather-related risks, and landlords face a greater likelihood of catastrophic physical property loss because not all damage is covered.

Some insurers are simply abandoning high-risk markets such as Florida and California, and we believe Hawaii will be next. The *Wall Street Journal* recently

SUSTAINABLE INVESTING TRENDS

reported that a growing number of homeowners are gambling with their financial security by leaving their homes uninsured because they can't afford the higher premiums.

American Century Investments' Global Real Estate team continues to assess and monitor how asset integrity risks and physical climate change impact the investable real estate universe. In addition to the cost associated with losses due to climate risk, it's worth noting that the litigious environment in certain states has driven inflated insurance premiums, pointing to the need for tort reform.

Weather-Related Canal Restrictions Affect Supply Chains

Climate-related costs aren't limited to the insurance and real estate sectors. Drought in Panama has produced freshwater shortages, and passage through the Panama Canal has been restricted. Roughly 6% of global maritime trade travels through the canal, and recent experience taught us how blocking a key waterway can impact global supply chains and prices.

According to data from Lloyd's List, when the Suez Canal was blocked for six days in 2021, approximately \$9.7 billion of products were held up each day and global supply chains were affected for months. Panama's economy is suffering, as Bloomberg has noted that roughly \$1 of every \$4 of government revenue comes from the canal. This creates a significant multiplier effect on the country's entire economy.

Extreme Weather Events Threaten Asset Values Today

We believe the world (including all investors) should stop focusing primarily on 2050 targets and start adapting and innovating today. Most of the arguments in support of sustainable investing (including American Century's) focus on financial materiality, and we can say for certain that extreme weather events are threatening the integrity of assets globally and increasing supply chain risks today.

While investors must recognize these risks and costs, we believe there will be opportunities for innovative companies to generate new sources of value while helping to address this great need.

GLOSSARY

Agency mortgages. A form of securitized debt that represents ownership in pools of mortgage loans and their payments.

Asset-backed securities (ABS). A form of securitized debt whose underlying assets may include such items as auto loans, home equity loans, student loans, small business loans, and credit card debt.

BB and BBB credit rating. Securities and issuers rated AAA to BBB are considered/perceived “investment-grade”; those rated below BBB are considered/perceived non-investment-grade or more speculative.

Beta. Beta is a standard measurement of potential investment risk and return. It shows how volatile a security’s or an investment portfolio’s returns have been compared with their respective benchmark indices. A benchmark index’s beta always equals 1. A security or portfolio with a beta greater than 1 had returns that fluctuated more, both up and down, than those of its benchmark, while a beta of less than 1 indicates less fluctuation than the benchmark.

Central bank. The entity responsible for oversight of a nation’s monetary system, including policies and interest rates.

Collateralized loan obligations (CLOs). A form of securitized debt (defined below), typically backed by pools of corporate loans and their payments.

Commercial mortgage-backed securities (CMBS). MBS (defined below) that represent ownership in pools of commercial real estate loans used to finance the construction and improvement of income-producing properties like office buildings and apartment complexes.

Commercial paper. Short-term debt issued by corporations to raise cash and cover current expenses in anticipation of future revenues.

Commodity. Raw materials or primary agricultural products that can be bought or sold on an exchange or market. Examples include oil, grains such as corn, foods such as coffee, and metals such as copper.

Consumer Price Index (CPI). Sometimes called headline CPI, this inflation statistic reflects price changes in a market basket of consumer goods and services such as gas, food, clothing and cars. Core CPI excludes food and energy prices.

Corporate securities. Debt instruments issued by corporations, as distinct from those issued by governments, government agencies or municipalities.

Correlation. Measures the relationship between two investments -- the higher the correlation, the more likely they are to move in the same direction for a given set of economic or market events.

Credit quality. The letter ratings indicate the creditworthiness of the underlying bonds in the portfolio and generally range from AAA (highest) to D (lowest).

Credit ratings. Credit ratings are measurements of quality assigned by a Credit Rating Agency (CRA) to issuers of certain types of debt obligations as well as the debt instruments themselves.

Debt security. A debt instrument, including bonds, certificates of deposit or preferred stocks.

Deflation. Deflation is the opposite of inflation (see Inflation); it describes a decline in prices for goods, assets and services, and is considered a highly undesirable economic outcome by economists and policymakers.

Duration. A measure of the price sensitivity of a fixed-income investment to changes in interest rates. The longer the duration, the more a fixed-income investment’s price will change when interest rates change.

Earnings per share (EPS). The portion of a company’s profits allocated to each outstanding share of its common stock. It is an indicator of a company’s profitability.

Eurozone. The eurozone represents member states that participate in the economic and monetary union (EMU) with the European Union (EU).

Federal funds rate. This is an overnight interest rate banks charge each other for loans. More specifically, it’s the interest rate charged by banks with excess reserves at a Federal Reserve district bank to banks needing overnight loans to meet reserve requirements.

Federal Reserve (Fed). The Fed is the U.S. central bank responsible for monetary policies affecting the U.S. financial system and the economy.

Fundamentals. In the context of investment analysis, fundamentals are typically those factors used to determine economic value (growth, interest rates, inflation, employment) and/or financial value (income, expenses, assets, credit quality), as opposed to “technical” based more on market price (into which fundamental factors are considered to have been “priced in”), trend and volume factors (such as supply and demand), and momentum.

GLOSSARY

Gross domestic product (GDP). A measure of the total economic output in goods and services for an economy.

High-yield bonds. High-yield bonds are fixed-income securities with lower credit quality and lower credit ratings. High-yield securities are those rated below BBB- by Standard & Poor's.

Inflation. Inflation reflects rising prices for consumer goods and services, or equivalently, a declining value of money.

Inflation-protected securities. Debt securities that offer returns adjusted for inflation; a feature designed to eliminate the inflation risk.

Investment-grade corporate bond or credit. A debt security with a relatively low risk of default issued and sold by a corporation to investors.

Liquidity. Liquidity describes the degree to which an asset or security can be quickly bought or sold in the market without affecting the asset's price.

Mortgage-backed securities (MBS). A form of securitized debt that represents ownership in pools of mortgage loans and their payments.

Municipal securities and bonds. Debt securities typically issued by or on behalf of U.S. state and local governments, their agencies or authorities to raise money for public purposes. Municipal bonds have maturities of 10 years or longer.

Nominal yield. The interest rate that the bond issuer promises to pay bond purchasers.

Non-agency commercial mortgage-backed securities (CMBS). MBS that represent ownership in pools of commercial real estate loans used to finance the construction and improvement of income-producing properties. Non-agency CMBS are not guaranteed by the U.S. government or a government-sponsored enterprise.

Price-to-earnings ratio (P/E). The price of a stock divided by its annual earnings per share. These earnings can be historical (the most recent 12 months) or forward-looking (an estimate of the next 12 months). A P/E ratio allows analysts to compare stocks based on how much an investor is paying (in terms of price) for a dollar of recent or expected earnings. Higher P/E ratios imply that a stock's earnings are valued more highly, usually based on higher expected earnings growth in the future or higher quality of earnings.

Quality. Nationally recognized statistical rating organizations assign quality ratings to reflect forward-looking opinions on the creditworthiness of loan issuers.

Real Yield. For most bonds and other fixed-income securities, real yield is simply the yield you see listed online or in newspapers (see Yield) minus the premium (extra yield) added to help counteract the effects of inflation (see Inflation). Most "nominal" fixed-income yields (see Nominal yield) include an "inflation premium" that is typically priced into the yields to help offset the effects of inflation. Real yields, such as those for TIPS, don't have the inflation premium. As a result, TIPS yields and other real yields are typically lower than most nominal yields.

REITs. Real estate investment trusts (REITs) are securities that trade like stocks and invest in real estate through properties or mortgages.

Russell 1000® Growth Index. This index measures the performance of those Russell 1000® Index companies (the 1,000 largest publicly traded U.S. companies, based on total market capitalization) with higher price-to-book ratios (market values relative to book values) and higher forecasted growth values.

Russell 1000® Value Index. This index measures the performance of those Russell 1000® Index companies (the 1,000 largest publicly traded U.S. companies, based on total market capitalization) with lower price-to-book ratios (market values relative to book values) and lower forecasted growth values.

S&P 500® Growth Index. The S&P 500 Growth Index is a style-concentrated index designed to track the performance of stocks that exhibit the strongest growth characteristics by using a style-attractiveness weighting scheme.

S&P 500® Index. The S&P 500 Index is composed of 500 selected common stocks most of which are listed on the New York Stock Exchange. It is not an investment product available for purchase.

S&P 500® Value Index. The S&P 500 Value Index is a style-concentrated index that measures stocks in the S&P 500 using three factors: the ratios of book value, earnings and sales to price. It is not an investment product available for purchase.

Securitized debt. Securitized debt results from aggregating debt instruments into a pool of similar debts, then issuing new securities backed by the pool.

GLOSSARY

Senior-secured securities. A security that has a higher priority compared to another in the event of liquidation.

Sovereign debt. Debt issued by the national government in a foreign currency. Also referred to as government debt.

Spreads, credit spreads. Measured differences between two interest rates or yields compared with each other. Spreads typically are measured between fixed-income securities of the same credit quality, but different maturities (“maturity spreads”), or of the same maturity, but different credit quality (“credit spreads”).

Spread sectors. These are typically non-Treasury securities that usually trade in fixed-income markets at higher yields than same-maturity U.S. Treasury securities. The yield difference between Treasuries and non-Treasuries is the “spread,” hence the name “spread sectors” for non-Treasuries.

Subordinated security. An unsecured loan or bond that ranks below more senior loans in terms of claims on assets or earnings.

Stagflation. An economic cycle marked by slowing economic growth and high inflation.

Treasury inflation-protected securities (TIPS). TIPS are a special type of U.S. Treasury security designed to address a fundamental, long-standing fixed-income market issue—that the fixed interest payments and principal values at maturity of most fixed-income securities don’t adjust for inflation. TIPS interest payments and principal values do. The adjustments include upward or downward changes to both principal and coupon interest based on inflation.

Treasury note. A treasury note is a debt security issued by the U.S. government with a fixed interest rate and maturity ranging from one to 10 years.

Treasury yield. The yield of a Treasury security (most often refers to U.S. Treasury securities issued by the U.S. government).

Valuation. A quantitative estimate of a company or asset’s value.

Yield. The rate of return on bonds and other fixed-income securities.

Yield curve. A line graph showing the yields of fixed-income securities from a single sector from a range of different maturities at a single point in time.

DISCLOSURES

ESG Disclosures

Many of American Century's investment strategies incorporate the consideration of environmental, social, and/or governance (ESG) factors into their investment processes in addition to traditional financial analysis. However, when doing so, the portfolio managers may not consider ESG factors with respect to every investment decision and, even when such factors are considered, they may conclude that other attributes of an investment outweigh ESG considerations when making decisions for the portfolio. The consideration of ESG factors may limit the investment opportunities available to a portfolio, and the portfolio may perform differently than those that do not incorporate ESG considerations. ESG data used by the portfolio managers often lacks standardization, consistency, and transparency, and for certain companies such data may not be available, complete, or accurate.

ESG Definition

ESG Integrated: An investment strategy that integrates Environmental, Social and Governance ("ESG") factors aims to make investment decisions through the analysis of ESG factors alongside other financial variables in an effort to deliver superior, long-term, risk-adjusted returns. The degree to which ESG integration impacts a portfolio's holdings may vary based on the portfolio manager's materiality assessment. Therefore, ESG factors may limit the investment opportunities available, and the portfolio may perform differently than those that do not incorporate ESG factors. Portfolio managers have ultimate discretion in how ESG issues may impact a portfolio's holdings, and depending on their analysis, investment decisions may not be affected by ESG factors.

ESG Focused: An investment strategy that focuses on Environmental, Social and Governance factors ("ESG") seeks to invest, under normal market conditions, in securities that meet certain ESG criteria or standards in an effort to promote sustainable characteristics, in addition to seeking superior, long-term, risk-adjusted returns. This investment focus may limit the investment opportunities available to a portfolio. Therefore, the portfolio may underperform or perform differently than other portfolios that do not have an ESG investment focus. ESG-focused investment strategies include but are not limited to impact, best-in-class, positive screening, exclusionary, and thematic approaches.

Sustainability focuses on meeting the needs of the present without compromising the ability of future generations to meet their needs. There are many different approaches to Sustainability, with motives varying from positive societal impact, to wanting to achieve competitive financial results, or both. Methods of sustainable investing include active share ownership, integration of ESG factors, thematic investing, impact investing and exclusion among others.

The opinions expressed are those of American Century Investments (or the fund manager) and are no guarantee of the future performance of any American Century Investments fund. This information is for educational purposes only and is not intended as investment advice.

Opinions and estimates offered constitute our judgment and, along with other portfolio data, are subject to change without notice.

Investment return and principal value of security investments will fluctuate. The value at the time of redemption may be more or less than the original cost. Past performance is no guarantee of future results.

International investing involves special risks, such as political instability and currency fluctuations. Investing in emerging markets may accentuate these risks.

Historically, small-and mid-cap stocks have been more volatile than the stocks of larger, more established companies.

Diversification does not assure a profit, nor does it protect against loss of principal.

Generally, as interest rates rise, bond values will decline. The opposite is true when interest rates decline.

American Century Investments®

4500 Main Street
Kansas City, MO 64111
1-866-628-8826

330 Madison Avenue
New York, NY 10017
1-866-628-8826

70 Main Street
New Canaan, CT 06840
1-866-628-8826

360 East 2nd Street, 5th Floor
Los Angeles, CA 90012
1-866-628-8826

2 Ice House Street
Central, Hong Kong
+852 3405 2600

12 Henrietta Street
London, WC2E 8LH
+44 20 7024 7080

1 Farrer Place
Sydney, NSW, 2000
+61 2 8667 3025

Suite 4-101, Taunusanlage 8
60329 Frankfurt, Germany
+49 69 8088 5501



americancentury.com