



## Market Compass

September 2024

### MARKET OUTLOOK

- Central banks are getting more confident about moving closer to victory over inflation. With risks to growth from tight policies rising, markets have boosted hopes of fast rate cuts into autumn.
- This may be prone to a partial reversal. After too much inflation pessimism in H1, markets now risk rushing into oversized hopes of fast policy easing amid high disinflation optimism and cyclical worries.
- While continued disinflation and prospective rate cuts keep yields geared to the downside medium term, we cut our recommendation for long duration exposure for now.
- Global growth has become bumpier, but we deem the moderate expansion trend still intact and US recession risks low. This is conducive to a prudent overweight in risk assets.

Edited by  
**MACRO & MARKET RESEARCH TEAM**

A team of 13 analysts based in Paris, Cologne, Milan and Prague runs qualitative and quantitative analysis on macroeconomic and financial issues.

The team translates macro and quant views into investment ideas that feed into the investment process.

#### US

- + Q2 GDP revised up on solid consumption
- + Core PCE inflation nearing target
- ! Unemployment rate up, but mostly due to higher supply. Lay-offs still historical minimum
- + Fed to cut by 75bps by year end. Easing in 2025 dependent on election outcome

#### UK

- + Manufacturing PMI remains positive in July/Aug
- + BoE started its easing cycle in August ...
- ...but higher inflation in coming month warrants cautious easing
- Poor public finances might warrant a tougher 2025 budget

#### EUROZONE

- + Again solid growth (0.3% qoq) in Q2
- Indicators suggest weaker Q3 activity
- + Inflation down to 2.2% in August
- + ECB confirmed expectation of further cuts

#### CHINA

- Economic activity remains subdued
- Real estate sector still weak
- + Surprising monetary easing and new calibrated measures
- + CNY appreciated, PBoC to dampen bond yield decline

#### EMERGING MARKETS (EM)

- + Expected lower US rates and disinflation provide room for easing
- + EM assets resilient to the summer sell-off
- + EM spreads to tighten but EM FX high-yielders on a backfoot

- + Positive
- Negative
- ! Topics to watch

## DIRECTION OF TRAVEL

- We just confirm our moderate overweight (OW) positions in Equities and Euro Area High Yield.
- We keep our OW in Euro Area IG non-financials as our largest active position while staying neutral in Euro Area IG financials.
- We keep the underweight (UW) government bonds overall.
- We stick to our preference for long-dated over short-dated bonds, but we trim our moderately long active duration stance.

### Equity

- Market bounced back after overreaction to recession fears.
- While there are still headwinds coming from negative global macro surprises, above average positioning, and political issues, monetary policy has become more market friendly, with bottoming financial conditions and credit cycle.
- We are slight OW and expect positive total returns in 1 year: ex-US +7.5%, 4% for the S&P 500.

### Bonds

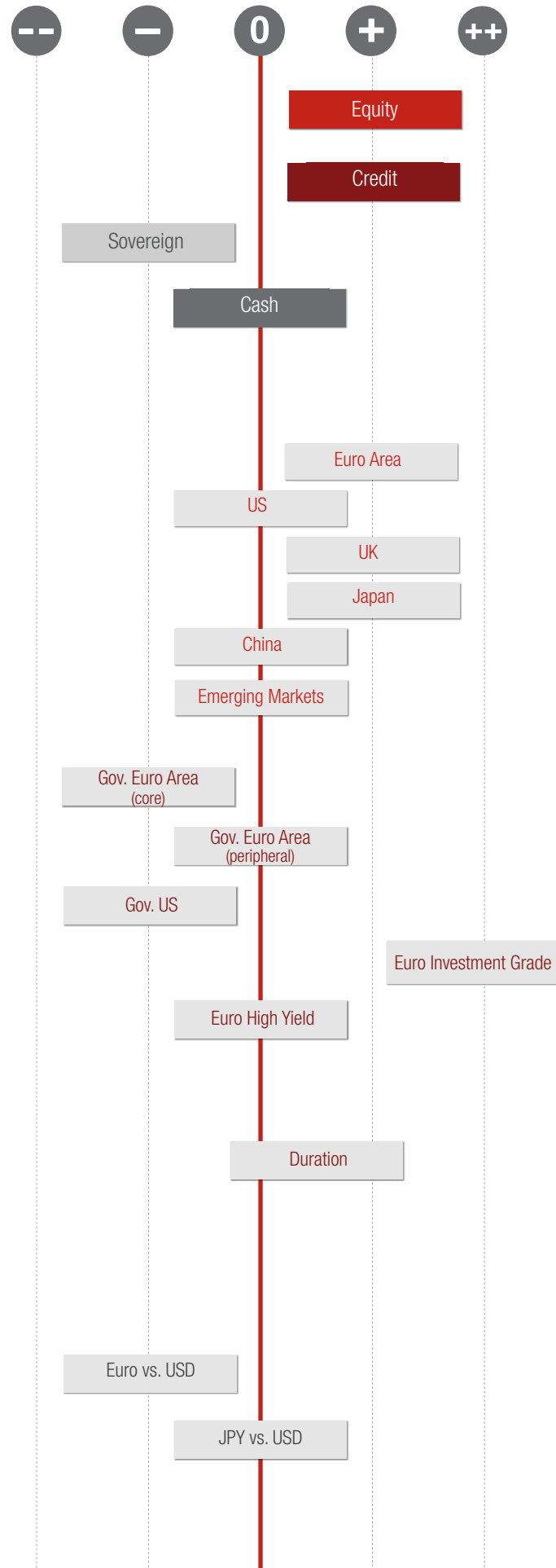
- Strong rally in government bonds overdone. Economic pessimism, inflation optimism and priced key rate cuts appear overdone, particularly in the US.
- Difficult government formation and adoption of 2025 budget in France to take centre stage for Euro Area non-core bond markets. Spreads skewed to the upside.

### Duration

- Marginally positive duration tilt.

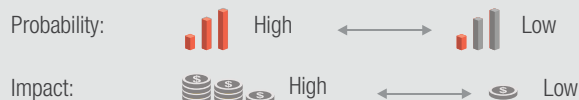
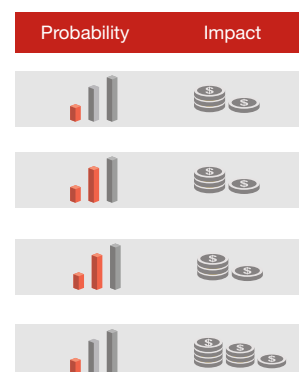
### Currencies

- The yen's sharp rise is set to flatten out near term, but we see more downside for USD/JPY further out on closing valuation gaps and opposed monetary policies.
- Recent USD weakness may have gone too far as markets have started to price in too fast and deep rate cuts by the Fed.



## TOPICS TO WATCH

- Fast deterioration of the business cycle, forcing a steeper path of rate cuts.
- Political gridlock in France weighs on sovereign rating and add to woes on EU integration, delaying pro-growth policies.
- High odds of Trump victory and the risk of protectionist policies accelerate global fracturing.
- Tighter credit eventually feeds through the economy worsening financial conditions.



## GLOSSARY

### PROTECTIONIST POLICIES

These are measures taken by a government to restrict or limit international trade with the objective of boosting domestic industries. They can take the form of tariffs, quotas, and subsidies. Proponents argue that this approach can shield domestic producers from the competitive effects of globalization while critics say it distorts market forces and harms overall consumer welfare.



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