GENERALI INVESTMENTS

Market Compass

July 2024

MARKET OUTLOOK

- The economic story of moderate growth and disinflation conflicts with political gridlocks. A Trump victory would fan international trade tensions, while political troubles in Europe are not limited to just France.
- The global recovery appears slightly more entrenched. We are confident that inflation normalization is proceeding again, making rate cuts more likely.
- Political developments often support our long-standing preference for Investment Grade (IG) Credit over Govies. But we try to avoid falling into the excessive influence of political crises, often the cause of temporary spikes. The French election may be a buying opportunity for French government bonds (OATs), unless a fully split parliament causes stalemate and makes fiscal consolidation impossible.
- Until the political fog lifts, we keep our equity overweight (OW) minimal, and High Yield and Financial Credit neutral. We stay long non-financial IG credit. We like to play the range in rates, still with a long duration bias. EMs offer good diversification benefit (both in Equities and HY Credit), despite near-term dollar strength.

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 growth remains solid on the back of strong consumption
- (+) Gradual disinflation continues
- (+) Labour market cooling contains wage growth but unemployment remains low
- (!) The Fed will start cutting in rates in September

UK

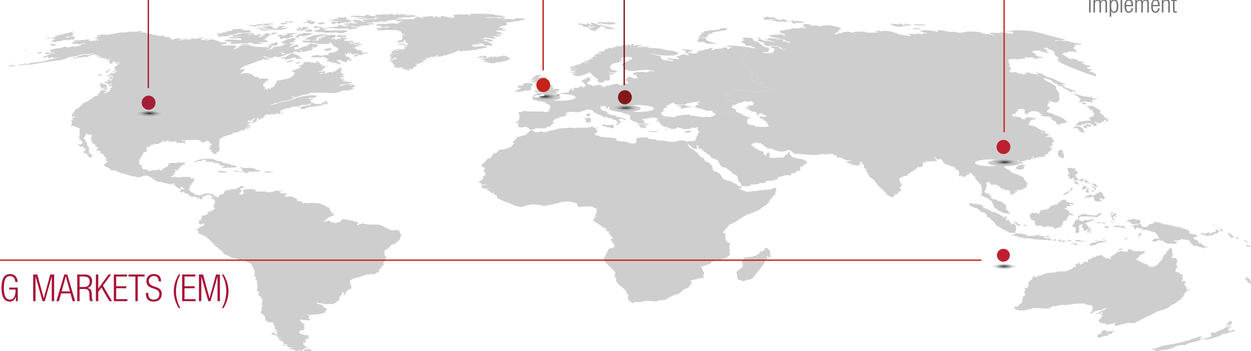
- (+) Manufacturing PMI remains positive in June
- (−) Despite falling inflation rate, services prices keep rising at a fast pace…
- (−) …forcing the BoE to remain cautious on rate cuts
- (!) Labour set to win big in the election, but cautious fiscal stance should remain

EUROZONE

- (−) Call of French snap election lifted uncertainty
- (−) Key sentiment indicators weakened
- (+) Inflation to trend down while remaining volatile
- (+) ECB fueled expectation of quarterly 25 bps cuts

CHINA

- (+) Exports continue to outperform, supporting manufacturing…
- (−) …but this does not fully offset weak domestic demand
- (−) Housing activity keeps contracting
- (!) PBoC likely to tolerate moderate currency weakness, but this may be difficult to implement



EMERGING MARKETS (EM)

- (+) Growth resilient
- (−) But disinflation slows down
- (+) EM credit spread to tighten further
- (−) EM FX carry trades on a backfoot

(+) Positive
(−) Negative
(!) Topics to watch

DIRECTION OF TRAVEL

- We raise our Equity exposure to a marginal overweight position with a preference for the US.
- On Credit we stay neutral in EA HY and reduce EA IG Financials to benchmark level in favour of IG Non-Financials.
- We underweight Government Bonds overall. We turn slightly positive on the USD given the higher EMU political risks and the ECB leading the easing cycle.
- Preferring the long over the short maturity buckets, we keep a moderately long duration stance.

Equity

- Equities are to benefit (slight OW) from resilient margins, improving ex-US confidence indicators and earnings growth of 5-7% in 2024-25.
- That said, we see short-term risks from French elections, S&P500 high valuations and higher positioning.
- We see positive total returns (TR) in the next 12 months: ex-US +7.5%, 4.5% for the SPX.

Bonds

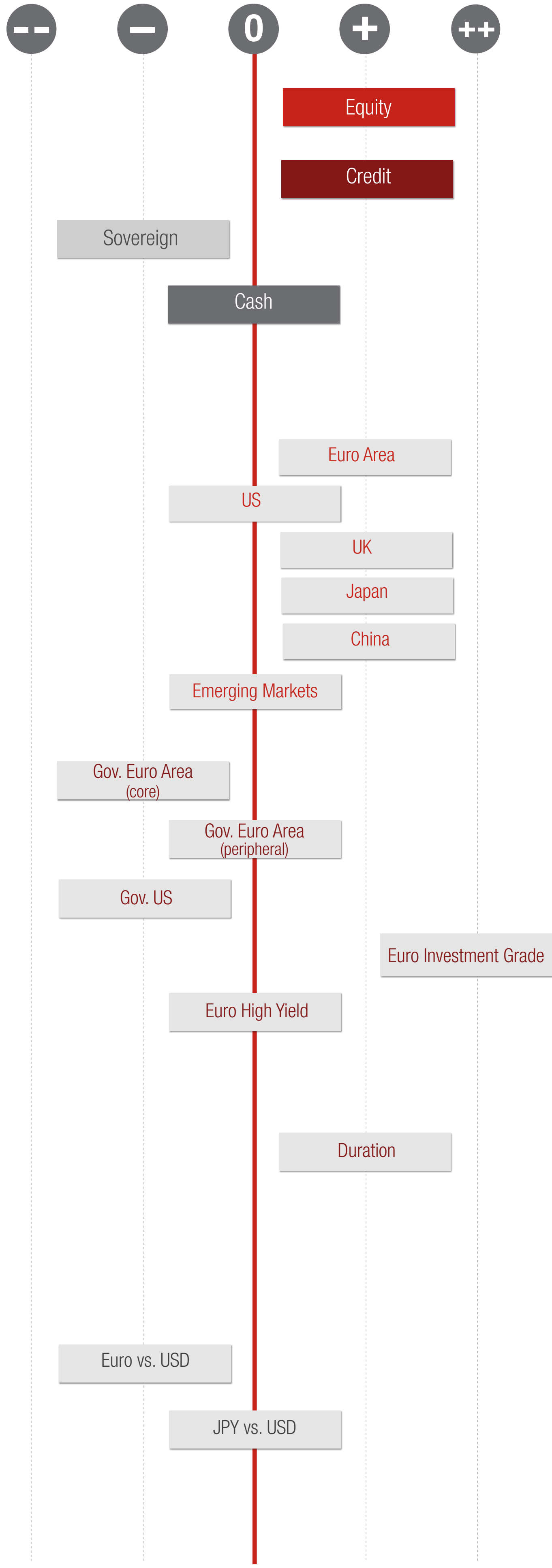
- Declining inflation will enable the ECB and the Fed to cut key rates by 25 bps in Q3. No strong rally, but core yields are skewed to the downside.
- EA non-core bond spreads to remain determined by political news flow for the time being. Countries with sound fundamentals to be preferred.

Duration

- Moderately long duration.

Currencies

- We tactically favour USD exposure amid political uncertainties about France, the ECB's lead in the easing cycle and the odds of a Trump win in the US elections.
- The battered yen bears appreciation potential in the mid- to long-term, but amid a lack of triggers and a low carry we caution against larger exposure for now.



TOPICS TO WATCH

Probability	Impact

- A more stubborn last mile of disinflation (wages, sticky services inflation, energy prices) delaying rate cuts.
- French political impasse (no majority, RN- or FP-led government) undermines French fiscal outlook, ratings and EU integration hopes. This adds to current geopolitical stress.
- Intensified global fracturing (esp. China/US), notably on grown odds of Nov. 5 Trump victory (punitive tariffs).
- Cracks in financial stability as tighter conditions feed through (CRE defaults, banking, housing, non-bank liquidity…).

Probability: High ⟷ Low

Impact: High ⟷ Low

GLOSSARY

OATs

OAT (Obligations Assimilables du Trésor) are French government bonds, equivalent to Italian BTPs and German Bunds.

Find out more:
www.generali-am.com

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