FIDEURAM INTESA SANPAOLO PRIVATE BANKING Asset Management

Fideuram Asset Management's View

Edition 10.2024

Macroeconomic Scenario

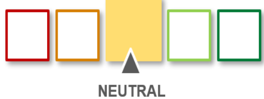
In recent weeks, there has been a shift towards more accommodative monetary policy in the advanced economies. This was evidenced by the 50 basis point rate cut by the Federal Reserve at its September meeting and the decision by the European Central Bank (ECB) to cut interest rates further in October, after having cut rates just five weeks earlier in September. Meanwhile, in China, recent policy announcements have been much more expansionary than expected, although the overall size of these measures, particularly the fiscal ones, remains uncertain. In the United States, recent data have significantly eased concerns over labour market weakness, which initially prompted the Fed to take such an aggressive stance in September. It is also worth noting that the outcome of the upcoming US elections could have important economic implications, both domestically and globally.

Equity Markets

The rapid recovery to levels close to all-time highs following the August correction leads us to maintain a neutral equity exposure. Macroeconomic data and the initial boost from Chinese stimulus support the view that cyclical momentum remains intact and that earnings growth will continue.

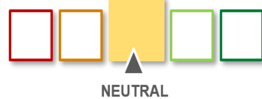
However, current valuations have largely priced in earnings growth into 2025, and the upcoming US elections, which have rarely been a game changer in the past, add an additional layer of uncertainty in the near term. Geographically, we remain close to neutral on the major regions, with a preference for UK equities within Europe. At the moment, we believe that the recovery in the Chinese market is the result of investor repositioning, which may continue in the short term, although it does not yet represent a structural change in the overall landscape. Even from a sectoral and thematic perspective, we currently maintain a relatively diversified position with limited active risks. However, we anticipate the possibility of shifting this approach towards more value and cyclical components, in the presence of a macroeconomic scenario that demonstrate stability.

Europe



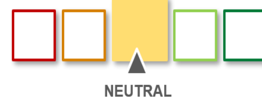
NEUTRAL

United States



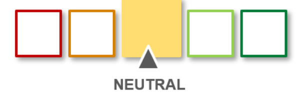
NEUTRAL

Japan



NEUTRAL

Emerging Markets



NEUTRAL

Bond Markets

The portfolios are structured with a duration slightly longer than the benchmarks and a preference for high quality credit risk (investment-grade corporates and subordinated financial debt). The weighting of the government bond component remains between neutral and slightly overweight, as recent data showing cyclical resilience has reduced the size of expected central bank rate cuts and pushed core yields back towards the upper end of their fair value range. At current levels (above 4.1% for the US 10 -year and around 2.3% for the German Bund), core government bonds have regained their ability to act as a hedge against equity risk should the macroeconomic outlook deteriorate. We remain overweight in investment-grade corporate bonds and subordinated financial debt. However, overall, exposure to credit risk is mitigated by our greater caution with the high yield segment and substantial neutrality on emerging markets. We prefer a tactical approach to equity risk over high yield, while emerging markets remain vulnerable to the outcome of the US elections and potential changes in tariff policy.

Government

NEUTRAL

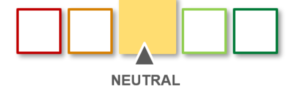
Corporate

SLIGHTLY POSITIVE

High Yield

SLIGHTLY NEGATIVE

Emerging Markets



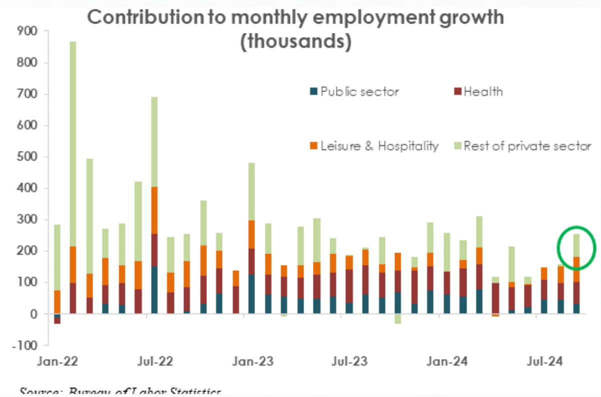
NEUTRAL

MACROECONOMIC SCENARIO

US: All eyes on the elections

With the creation of 254 thousand jobs and a sharp drop in the unemployment rate, the September labour market data has **significantly reduced the signs of weakness that had emerged in July and August** and which had prompted the Fed to aggressively cut interest rates at its September meeting. The renewed strength in labour market conditions has now eliminated the likelihood of another 50 basis point cut at the Fed's upcoming meeting on 7 November, with **the most likely outcome being a more moderate 25 basis point cut** (with a similar decision expected at the mid-December meeting). The outcome of the elections on 5 November, which remains highly uncertain, could also have a significant impact on the economic outlook for the coming years.

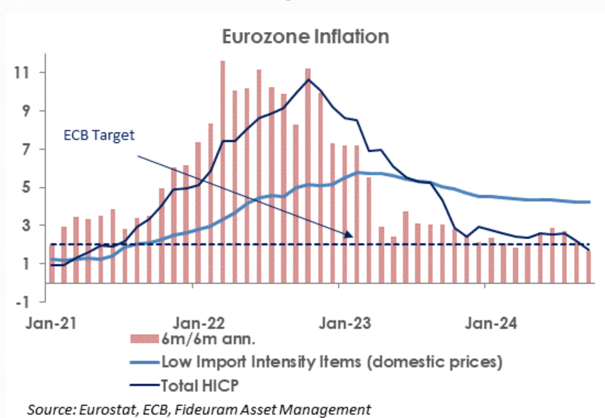
Employment growth surges again in September



Euro Area: ECB speeds up rate cuts

Two major surprises in the macroeconomic landscape last month convinced the ECB to ease monetary policy more quickly than expected: first, the **further weakening of business confidence** in September, including in the services sector; **and second, a sharp drop in inflation**, with the rate falling to 1.7% in September from 2.2% in August (against expectations of 1.9%-2%). Moreover, following the expansionary measures taken during the pandemic, fiscal policy will have to become more restrictive from 2025 onwards, in line with the requirements of the new Stability Pact. As a result, **the ECB cut rates by a further 25 basis points at its October meeting**, just five weeks after the previous cut in September. We expect the ECB to continue to cut rates at every meeting until at least next spring.

Inflation Surprises to the downside in September, falling below 2%

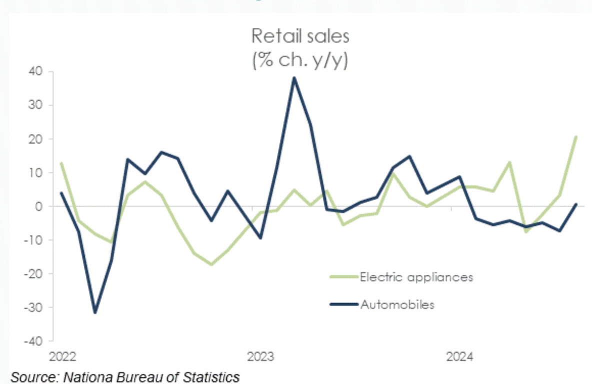


Source: Eurostat, ECB, Fideuram Asset Management

China: Growth likely past its trough

In the third quarter, GDP growth accelerated from 2.0% to 3.6% annualised, with most September data beating expectations, although the property sector remains weak. Since the end of September, a series of announcements from both the monetary and fiscal authorities have surprised markets to the upside, highlighting greater coordination among policymakers and a stronger commitment to achieving the growth target for the current year. As a result, **we now forecast growth of 4.8% this year**, with a sharp acceleration in the fourth quarter (6.5% annualised) **and 4.7% in 2025** (up from 4.7% and 4.5% respectively).

Appliance and auto sales surge in September thanks to government incentives



Source: Nationa Bureau of Statistics

Fideuram Asset Management Economic Forecast

	PIL			Inflazione			Tasso di riferimento politica monetaria		
	2023	2024*	2025*	2023	2024*	2025*	2023	2024*	2025*
USA	2,9	2,6	2,0	4,1	3,0	2,3	5,38	4,63	3,63
Area Euro	0,5	0,7	0,8	5,5	2,3	2,0	4,00	3,00	1,75
Giappone	1,7	-0,1	1,0	3,2	2,5	2,0	-0,10	0,25	0,50
Cina	5,2	4,8	4,7	0,2	0,4	1,5	2,50	1,90	1,70

Crescita media annua per PIL e inflazione; livello di fine anno per i tassi. Tasso depo per BCE. ** Previsioni Fideuram Asset Management*

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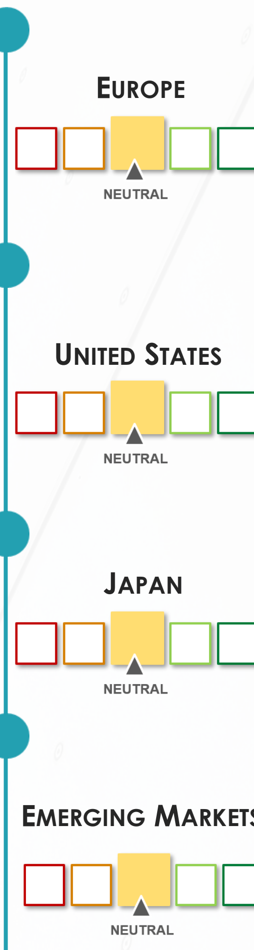
INVESTMENT VIEW

EQUITY MARKETS



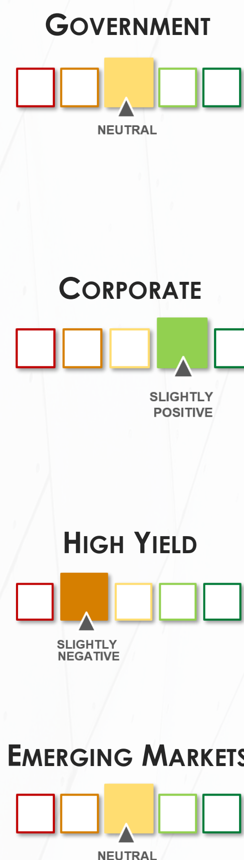
Valuations in Europe remain attractive relative to the US, although cyclical momentum has been weaker than expected. Nonetheless, we expect corporate earnings to strengthen over the coming quarters, supported by more accommodative monetary policy. We continue to favour the UK market, where the institutional and political backdrop is perceived to be improving and valuations still reflect a significant discount. From a sector perspective, banks stand out with growing earnings, despite a lower expected contribution from net interest margins. They are also trading at attractive valuations.

We remain neutral on US equities as current valuations already price in favourable earnings growth, even for much of next year. While we continue to believe that a soft landing for the economy and continued earnings growth is the most likely scenario, macroeconomic uncertainty has increased, especially as we get closer to the election. For the time being, we are limiting active exposure to themes, although our macro view supports the potential for further market diversification, particularly towards sectors that have lagged behind the growth of the mega-caps in terms of performance and valuation.

We are neutral on Japanese equities, as fundamental progress appears to be priced in, both in terms of market valuations and positioning. In addition, the possibility of currency appreciation adds further near-term uncertainty. Looking further ahead, however, we see room for valuation expansion and earnings growth for Japanese equities, driven by higher inflation expectations, corporate balance sheet restructuring and rising capital expenditure.

China's recent strong rebound comes on the heels of more vigorous government stimulus, although the fiscal component remains undefined in terms of content and size. For the time being, the rally in Chinese markets appears to be driven by investor repositioning rather than a structural change in the outlook. In emerging markets in general, the macroeconomic backdrop is favourable, supported by interest rates, Chinese stimulus and a soft landing, but political uncertainty remains, particularly if there is a wider reintroduction of tariffs on international trade after the US elections.

BOND MARKETS



We maintain a neutral to slightly overweight position in government bonds, based on the view that the yield curve structure has shifted lower compared to recent months. This shift is driven by falling inflation, central bank rate cuts and mixed macroeconomic signals. The recent rise in yields has pushed government bonds to the upper end of our fair value range, making the asset class more attractive in the short term. In Europe, and in particular in core rates, we see a lower risk than in the US for the steepening of the longer maturity part of the curve. Peripheral spreads, although at a slightly lower level than that suggested by the fundamentals, are still an attractive source of carry.

The total return offered by the high-quality corporate bond sector is still attractive thanks to the base rate, which gives a certain degree of defensiveness for the asset class even under more uncertain macroeconomic conditions, and the contribution of spreads that, although relatively narrow and net of short-term movements, offer an extra return compared to government bonds. Supporting factors include the resilience of the economic cycle and central bank rate cuts, which have lowered the interest rate structure compared with some time ago.

The default rates, despite the impact on lower-quality loans of an increase in the cost of capital, are still relatively limited. However, even with attractive expected returns on a historical basis, we remain underweight as we prefer equities among the risky assets, at least until companies continue to show capacity for growth and an upward revision of earnings, and to limit the credit risk that may be generated due to central banks maintaining high rates. maintaining high rates.

We remain neutral on emerging markets overall, as the carry offered is relatively attractive in absolute terms. However, while macroeconomic conditions (interest rates, Chinese stimulus, soft landing) are beginning to favour emerging markets, political and currency uncertainties remain, especially if the US elections lead to increased trade tariffs. We hold a preferential position in relation to Indian bonds.

EQUITY MARKETS

NEUTRAL AFTER RECENT GAINS

We maintain a neutral equity exposure, both overall and across individual geographical regions. After being overweight equities for much of the year, we have moved to a more **balanced stance**, with less active selection from a geographic, sector and thematic perspective. This neutral stance reflects our belief that **the economy is on track for a soft landing** and that, despite heightened macroeconomic uncertainty, **the earnings growth cycle is likely to continue**. The positive earnings momentum limits the potential for a significant market decline, but high valuations - particularly in the US - have already priced in much of the expected **earnings growth over the coming quarters**. Moreover, the exceptionally strong performance of the past two years has taken markets to historically high levels. Therefore, in this scenario of cyclical resilience, **any corrections or periods of weakness could provide opportunities to moderately increase equity exposure.**

In the US, the market has recently benefited from an improvement in the perception of the macroeconomic outlook, as evidenced by a **sector rotation away from defensive stocks towards more cyclical ones.** However, high valuations combined with uncertainty around the upcoming elections suggest a neutral stance.

In Europe, we **remain neutral** with a slight preference for the UK, where **valuations are more attractive.** Earnings revisions remain weak across the region, mainly due to economic challenges in Germany and tighter fiscal policies in some countries.

With regard to Japanese equities, while we continue to see medium-term growth potential, driven by corporate governance reforms and the exit from deflation, our position remains neutral. Much of this potential is already **reflected in valuations**, and **a potential yen appreciation adds to near-term uncertainty.** We remain neutral on emerging markets, while taking a more tactical approach to China. While monetary stimulus is being complemented by fiscal measures, a lack of detail on these initiatives makes it difficult to assess their scale and effectiveness. This suggests that the recent rally in **the Chinese market has been largely driven by investor repositioning** as they wait to see if the forthcoming fiscal measures can have a long-term, structural impact beyond the short-term benefits of a tactical bounce.

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BOND MARKETS

MODERATE DURATION OVERWEIGHT WITH FOCUS ON HIGH QUALITY CREDIT

Our fixed income allocation remains **slightly overweight duration** and **favours high-quality credit risk**, with a focus on investment grade corporates and subordinated financials. This positioning is in line with the broader backdrop of **falling policy rates, easing inflationary pressures and central banks shifting to more pro-growth policies.**

The recent rise in government bond yields, particularly in the US, has tempered some of the market's more extreme expectations of aggressive Fed rate cuts, bringing rates back towards the upper end of what we consider a fair valuation range. At current levels (above 4% for 10-year US Treasuries), US rates could once again act as a diversifier against cyclical risk. However, in the coming weeks, the longer end of the curve could see **increased volatility ahead of the US elections**, especially if a Republican victory creates more uncertainty compared to European rates, which could remain more stable. In Europe, we see further room to **increase government bond exposure**, as current yield levels are not fully justified by the weaker macroeconomic outlook compared to the US and a faster rate cutting cycle by the ECB. Peripheral spreads remain slightly below credit risk levels, but no significant volatility is expected in the short term. In France, 10-year bond spreads reflect the deteriorating fiscal situation, given the lack of convincing budgetary measures.

The preference for **high quality credit and subordinated financial bonds is supported by attractive yields and a correlation between interest rates and credit spreads** that has remained resilient even during periods of heightened volatility in the base rate. In addition, credit quality continues to improve as the economic cycle extends. The high-yield segment has benefited in recent weeks from an **improved macroeconomic outlook**, which led to a tightening of spreads even for ****. Supporting factors include low default rates and the absence of signs of deterioration in credit quality. From a portfolio perspective, we prefer to take moderate cyclical risk through equities and continue to focus on high quality credit risk rather than speculative grade, where we remain underweight.

In emerging market bonds, the US elections and their potential impact on trade policy represent a significant and unpredictable risk. As a result, we maintain a **neutral stance**, although absolute yields remain attractive. Within local debt, we continue to favour Indian bonds for their **higher yields and lower volatility**.

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