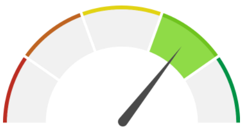
Fideuram Asset Management's View

Edition 06.2024

Macroeconomic Scenario

Uncertainty surrounding the inflation outlook is prompting the major central banks of advanced economies to adopt a cautious approach. As widely expected, the ECB cut rates at the beginning of June, despite raising its inflation forecasts, but gave no indication of the next steps. The Fed was also very cautious, reducing the expected cuts in the projections of FOMC members from three to only one by the end of the year, despite the significant surprise downward inflation trend in May. Our scenario has not changed: we expect a Fed cut in September, followed by another in December, while in the ECB case we expect two more cuts following the one decided in June (again in the September and December meetings). Finally, the return of political risk in Europe should be noted with the early elections in France being called by surprise by President Macron after the voting results for the European Parliament.

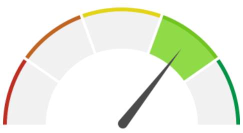
Equity Markets



We maintain an equity overweight of an average size in our portfolios, linked to the upward revision of earnings and the prospect of a broadening in the coming quarters to those sectors and countries that have so far underperformed technology and the United States in terms of earnings growth.
At the sectoral level, we are addressing this evolution gradually and are continuing to maintain a substantial weight in technology, introducing, for example, a small exposure to companies active in the management of electricity networks and grid infrastructures benefiting from strong capex spending in technology, data management, renewable energy and security.
At the geographical level, the equity overweight mainly concerns the US and Europe. The latter, according to the results from the first quarter, gave signs of a recovery of the economic cycle and profits, although the decision to hold early elections in France reintroduced a premium for political risk in European (and mainly French) assets and could create volatility at least until the results of the consultation.
We hold a neutral view on Japan and emerging countries.

Europe	United States	Japan	Emerging Markets
Slightly positive	Slightly positive	Neutral	Neutral

Bond Markets



The portfolios maintain a slight overweight in terms of duration that is concentrated in the government component, with a preference for the European market, and an overall credit risk underweight, mainly for the most speculative high-yield segments.
The ECB started the interest rate reduction phase in June and the Fed indicated the possibility of a single cut in 2024 but did not reduce the overall size of the cuts for the foreseeable future (end 2025). This reduces any potential room for rate increases, even in a context of uncertainty around the monetary policy path and strict data dependency. The reintroduction of political risk in France has also led to a widening of peripheral spreads, which for now falls within a range of normal volatility (return to start-of-year levels) and is partly offset by the fall in the German base rate. Within the credit segment, we prefer the quality segment and banking subordination. Portfolios maintain cyclical risk-taking through equity exposure and we are underweight in terms of high-yield corporate credit and neutral in terms of emerging debt.

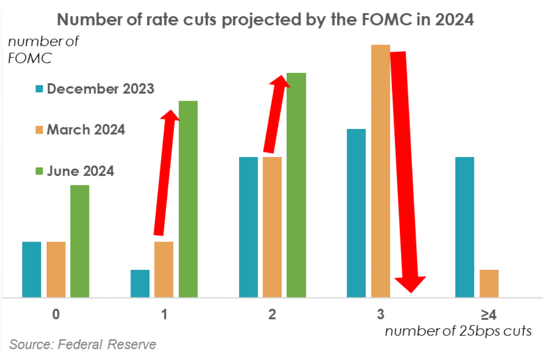
Government	Corporate	High Yield	Emerging Markets
Slightly positive	Neutral	Slightly negative	Neutral

Content updated as of June 18th, 2024

USA: May inflation easing (but not yet for the Fed)

After being very high in the first four months of the year (and definitely above expectations in January and March), **core price growth slowed down considerably in May** (+0.16% mom), thanks to the significant weakening in the price of services net of rents, the most sensitive component to labour market conditions (and, consequently, closely monitored by the Fed). Despite the surprise in May's inflation, the Fed meeting that ended on 12 June (the same day that the inflation data were published) **sent out a signal of considerable caution.** In particular, the new FOMC members' rate projections now incorporate only one rate cut by the end of the year against three expected in March (and a consensus forecast of two cuts). **However, we have maintained our expectation of a first cut in September** and another in December.

Fed members' rate projections moved more cautiously than expected at June's meeting

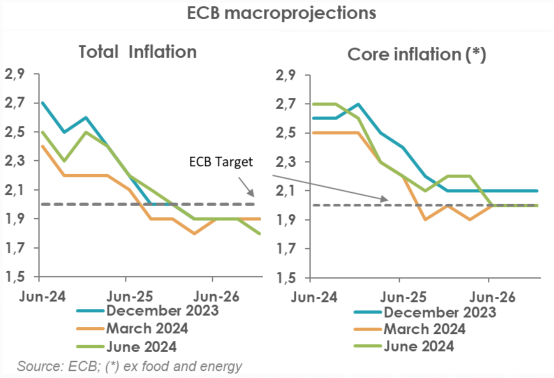


Source: Federal Reserve

Euro Area: Political and trade tensions

At the meeting on 6 June, the ECB cut rates by 25 bps, in line with expectations: despite the rise in inflation in May and the upward revision of its inflation and growth forecasts, the ECB remained convinced that it was still appropriate to start reducing the monetary tightening. **However, it did not commit in any way as to its future moves:** our expectations and those of the market are for a second cut in September, if inflation slows down during the summer. **Political uncertainty has greatly increased** with the outcome of the European elections (which were overall in line with expectations): **in France, President Macron dissolved Parliament and called new elections** with the first round to be held on 30 June, which could bring Le Pen's far-right party to power for the first time. In turn, the European Commission **has raised tariffs on imports of electric cars** from three Chinese manufacturers, exacerbating trade tensions with China.

The ECB has revised its short-term inflation forecast upwards, but not for long

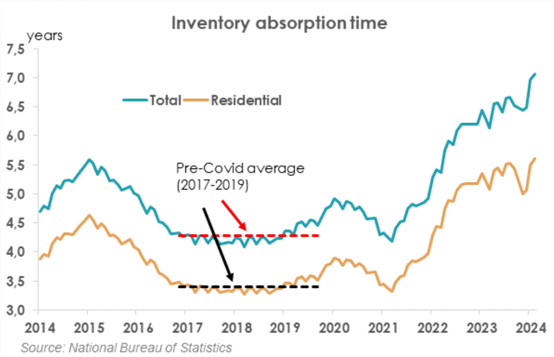


Source: ECB; (*) ex food and energy

China: more can be done

May's figures also provided a mixed picture on the performance of economic activity: exports and retail sales were higher than expected, while investments and industrial production were disappointing. We confirm our expectations of a slowdown in GDP growth from 6.6% to 4.1% annualised in the current quarter. **May's figures also highlighted the continuation of the real estate sector crisis:** sales remained weak and prices continued to decline. The policies in support of the sector announced in mid-May will take a few months to manifest their effects. In the coming months, the authorities could decide on a new interest rate cut or expand the funds earmarked for the management of the stock of unsold residential properties.

The absorption rate of the stock of unsold residential properties is at its lowest since 2014



Source: National Bureau of Statistics

Fideuram Asset Management Economic Forecast

	GDP			Inflation			Monetary Policy Rate		
	2023	2024*	2025*	2023	2024*	2025*	2023	2024*	2025*
US	2,5	2,3	1,8	4,1	3,2	2,3	5,38	4,88	4,13
Eurozone	0,5	0,7	1,2	5,5	2,3	2,1	4,50	3,75	3,00
Japan	1,8	0,5	1,2	3,2	2,8	2,3	-0,10	0,25	0,50
China	5,2	5,2	4,6	0,2	0,7	1,5	2,50	2,40	2,40

Annual average growth, monetary policy rates are end of period. Refi rate for ECB.

** Fideuram Asset Management Forecasts*

INVESTMENT VIEW

Equity Markets

Europe

SLIGHTLY POSITIVE

The overweight is based on relatively low and discounted valuations compared to those in the US, and on the improvement of cyclical and income conditions. We believe that the gap with the US in terms of earnings dynamics could narrow over the coming quarters. The British and especially French elections may produce some volatility in the short term, however the market has already introduced a certain political risk premium.

United States

SLIGHTLY POSITIVE

We maintain the US overweight on the strength of profits, which have so far exceeded expectations and are expected to remain robust even in the coming quarters. We believe that the technology sector will continue to have good growth levels, however in the second half of the year other segments are expected to show an accelerating growth. Alongside the technological exposure, which we maintain in the portfolios, we have started a process of gradual increase in sectoral and style diversification in favour of those components that have accumulated a performance and evaluation gap compared to the mega cap growth.

Japan

NEUTRAL

We are neutral on Japan after the strong hikes of the past months because we think that in the short term the fundamental progress is partly reflected in the valuations and in the market positioning that is already relatively favourable to Japanese equities. From a longer-term perspective, we continue to see the Japanese market being characterised by a positive approach, thanks to rising inflation expectations, the path of balance sheet restructuring and increased investment spending.

Emerging Markets

NEUTRAL

We maintain an overall neutral position on emerging markets, however we begin to highlight some elements of greater positivity for the area or at least for some countries, namely improving cyclical conditions, inflation close to the targets of the respective central banks, attractive valuations, and Chinese measures on the right track albeit not yet sufficient. On the other hand, there remains greater volatility linked also to the impact of exchange rates (primarily the dollar) and a little volatility also linked in this context to electoral outcomes.

Bond Markets

Government

SLIGHTLY POSITIVE

We maintain an overweight for the government component with a preference for the European component, where the ECB has already started the benchmark rate reduction; although it has not given clear indications on the next monetary policy path, the downward direction limits the potential of a rate hike. The reintroduction of political risk in France has also led to a widening of peripheral spreads, which for now falls within a range of normal volatility (return to start-of-year levels) and is partly offset by the fall in the German base rate.
The Fed has reduced the number of cuts for the current year but not the overall size of the cuts, so there remains greater data dependency.

Corporate

NEUTRAL

Despite the relatively low spreads, total return is attractive, and investment grade remains our preferred segment along with financial subordination. However, we maintain a neutral positioning because the most attractive yield component is offered by the base rate and, in general, we prefer to take equity risk over credit risk at this stage.

High Yield

SLIGHTLY NEGATIVE

The default rates, despite the impact on lower-quality loans of an increase in the cost of capital, are still relatively limited. We prefer to avoid the associated risks for the most fragile segments of a prolonged period of high rates and favour cyclical risk-taking through the equity component as long as earnings are solid and prove capable of beating estimates.

Emerging Markets

NEUTRAL

In general, we are cautious about the more volatile and lower quality components of the bond segment, which are more exposed to macroeconomic data and rate movements. The position on emerging markets is overall neutral since the carry offered is relatively generous in absolute terms and the cyclical context and the evolution of US monetary policy are evolving in a more favourable direction for emerging assets.

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EQUITY MARKETS

UPWARD EARNINGS REVISION IS DRIVING EQUITY MARKETS

The structure of the equity exposure is not subject to changes, maintaining an overall overweight, to an extent that can be defined as of average size. In geographical terms, **overexposure is always concentrated in the US and Europe,** with a neutral position towards Japan and emerging countries.

The overweight in equities is based on the idea that **the earnings cycle will continue to be quite robust,** characterised by a gradual improvement in quarterly earnings growth and the ability of companies to continue to exceed consensus estimates.

Looking at the US equity exposure, it is noted that it **has relatively richer valuations** compared to the rest of the world. For the time being, however, we do not believe that valuations are the main element supporting equity markets, but rather earnings growth dynamics, which is why we place a great deal of emphasis on companies' income performance. The US equity markets, despite the high valuations, **remain moderately overweight in our portfolios,** precisely because of the support that comes from the good fundamentals and the strength of profits, which have so far been above expectations and are prospectively looking solid also in the coming quarters. In the US we have recently witnessed a further market rally that continues to be driven by technology stocks and in particular by the semiconductor sector linked to the development of artificial intelligence infrastructure.

The overweight in Europe stems from the mix of rising profits, cyclical performance and favourable valuations. Looking ahead, the path of sequential profit growth **sees Europe gradually accelerating** and approaching the expected profit growth rates for the US S&P 500 index at year-end. Finally, compared to the US market, **Europe can also count on low relative valuations and discounts compared to the US.**

Moreover, we believe that there is progressively room for the rest of the market **to increasingly contribute to the growth of earnings.**

From the sectoral and thematic point of view, we believe that the technology sector will continue to have good profit growth levels, however in the second half of the year also other segments are expected to show an accelerating sequential growth. This broadening of leadership in favour of the more cyclical and value components is, however, being tackled gradually and whilst still maintaining a substantial weight in technology.

BOND MARKETS

THE ECB GETS THE RATE CUT PROCESS UNDERWAY

As widely expected, **the ECB's monetary tightening activity has finally begun,** despite the simultaneous upward revision of growth and inflation expectations.

As we also had pointed out earlier, **we believe that it is more important** for central banks to start cutting interest rates than the overall size of the cuts. This is because the start of the cuts decisively **removes even marginal scenarios from market pricing** in terms of the likelihood of further tightening, and helps to define a slightly more predictable behaviour of the trend in government rates.

The uncertainty for the Fed at this stage **is greater** since it is linked not only to the intensity and pace of the expansionary cycle but also to the timing of its start. However, the CPI figure for May is positive despite being surprisingly well below expectations, since it goes in the direction of confirming the disinflation process.

As also emerged at the ECB conference, we are not at the beginning of a multi-year path of rapid and linear interest rate reduction. Rather, **it is the start of a phase of greater stabilisation** (although we expect elements of short-term volatility linked to macro data flow) of the ten-year rates that also makes the context in which the risky asset classes are moving prospectively less challenging.

We maintain the marginal overweight towards the government component with a preference for the European component, on the basis of less uncertainty for the monetary policy path. The current Bund level remains within our fair value range of 2.3%-2.5%. In the US, inflation data pushed the 10-year Treasury slightly below the 4.3%-4.5% range, which we consider to be a fair value area.

We maintain a cautious position on credit risk. The components we favour in this area are always those with the highest credit rating, investment grade and financial subordination securities. The latter has a better performance and lower duration against good issuer quality. **We are more cautious on emerging markets and, above all, on the high yield segment.** This approach is partly dependent on the relatively compressed level of spreads, but above all on the preference we have for equities, at least as long as we can see corporate profits improve and companies are able to beat estimates.

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