



Market Compass

March 2024

MARKET OUTLOOK

- Overly ambitious rate cuts expectations by the turn of the year have deflated to now far more reasonable levels. We are starting to warm up to bonds; any further investor capitulation will be an opportunity to extend duration.
- Equity markets have proven remarkably resilient to the central bank repricing. The bifurcation between high yield and resilient equity owes much to the 'AI miracle' and rising optimism about the economy.
- We see a bit of complacency considering the still fragile point of the cycle, and with (geo)political risk lurking, bullish investor sentiment and positioning, as well as depressed risk asset volatility.
- Our underweights (UW) in Equities and High Yield (HY) credit are small, but we prefer safer Investment Grade (IG) buckets in Fixed Income and retain a tactical cash overweight.

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

- + Q1 growth projected to exceed 2%
- ! January core inflation proved stickier than expected
- + Labour market keeps cooling
- ! The Fed will cut by 75bps, maybe less

UK

- UK fell into recession in Q4
- + The composite PMI returned to growth on strong services
- + Wage growth receded...
- ...but core inflation moved sideways of late

EUROZONE

- + Mixed sentiment data suggest that activity only sluggishly improves
- Disinflation slower than expected
- + ECB dented hopes of a swift rate cut
- + We deem a June cut most likely but see risk now towards later cuts

CHINA

- China's manufacturing PMIs continued to point in different directions
- + The central bank cut 5y Prime Loan Rate to help the real estate sector
- + There is talk about more support for private consumption
- + The annual NPC meeting starts on March 5th

EMERGING MARKETS (EM)

- + Easing of EM financing with heavy bond issuance
- + Renewed appetite for EM fixed income as spreads tightened
- ! Resilience of EM growth and inflation decline

- + Positive
- Negative
- ! Topics to watch

DIRECTION OF TRAVEL

- We further trimmed our UW in the riskiest parts of our portfolio (equities, HY).
- We continue to favour IG credit and spreads can tighten further.
- We trimmed our overweight (OW) on Treasuries but if 10 years yield reach 4.4 - 4.5% we are ready to OW and extend duration.
- We keep our OW in cash.

Equity

- Markets are discounting better macro data.
- Short term, the positive trend may continue, but equities look increasingly risky. Positioning has visibly increased and a bottoming **VIX index** is a short-term headwind for an overbought S&P500.
- After the recent rally, our 12-month TR targets are reduced. We stay slightly UW.

Bonds

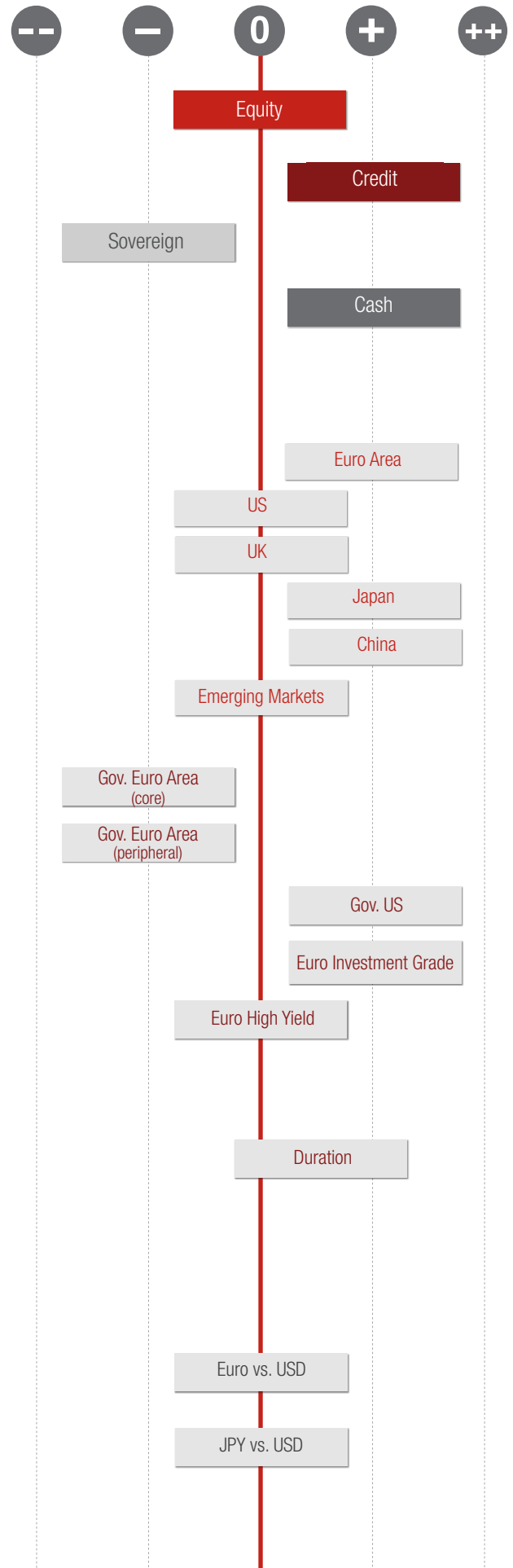
- With mispricing regarding future monetary policy eliminated, there is leeway for US and EA core yields to fall slightly amid lower inflation and looming key rate cuts in Q2.
- Carry-friendly environment to keep EA non-core bond spreads on a rather low level. Modest spread widening in H2.

Duration

- Moderately long duration.

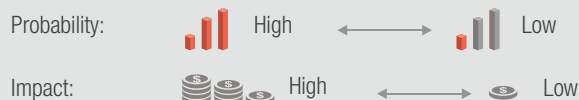
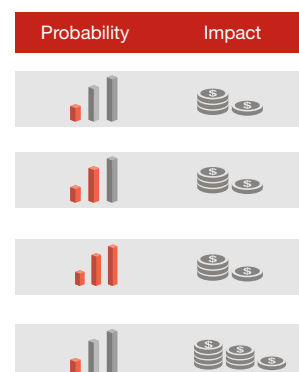
Currencies

- It is still premature to position for USD weakness near term. Solid US growth and slowing disinflation may delay rate cuts.
- Further out, the USD's fortune may turn on the back of narrowing yield differentials and lower rates uncertainties, with the JPY to benefit from the BoJ's removal of policy accommodation.



TOPICS TO WATCH

- Tighter financial conditions affecting financial stability (banking, housing, CRE defaults, non-bank liquidity, etc.).
- Risk of higher inflation (more persistent services inflation, supply chain disruptions).
- Trade decoupling intensifying, notably China/US around elections (Nov 5, 2024).
- Sharp changes in geopolitical stress up (Ukraine, Middle East, Taiwan...), or down (de-escalation relief more muted but regionally significant).



GLOSSARY

VIX INDEX

The CBOE Volatility Index (VIX) is a real-time index that represents the market's expectations for the relative strength of near-term price changes (or volatility) of the S&P 500 Index (SPX). The index is more commonly known by its ticker symbol and is often referred to simply as "the VIX." It is an important index in the world of trading and investment because it provides a quantifiable measure of market risk and investor' sentiments.



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