FIDEURAM INTESA SANPAOLO PRIVATE BANKING Asset Management

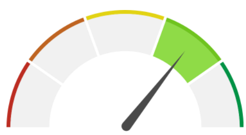
Fideuram Asset Management's View

Edition 03.2024

Macroeconomic Scenario

We have not made any significant changes to our global growth and inflation scenario this past month. We therefore continue to expect both the Fed and the ECB to start cutting rates at their June meetings. The risk to this baseline scenario remains a more delayed start (and fewer cuts over the forecast horizon), especially for the Fed, because a significant easing of core inflation in the US after the upside surprises earlier in the year is necessary for the Fed to be confident enough to start cutting rates. Upside risks to inflation appear more limited in the Eurozone, where the growth profile is also still significantly weaker than in the US.

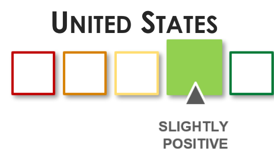
Equity Markets



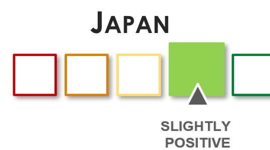
The equity overweight of the portfolios has been further increased following confirmation of the good health of the US economy which is reinforcing the expectation that corporate earnings will continue to grow in the coming quarters. Valuations are generally not cheap, but remain supported by the perception of a longer and more diversified earnings cycle across sectors and geographies. Buying has focused on those sectors/geographies that have accumulated a performance and relative valuation gap with technology. For those segments, including European equities, which we are upgrading to overweight, we expect more favourable earnings growth in the second half of the year. We have reduced the weighting of technology and the US only marginally (and which remain overweight), as short-term earnings momentum remains robust. In terms of themes, we have reduced the weighting of cyber security because, although the sector has strong long-term growth, we are less positive on the near-term competitive environment.

Europe

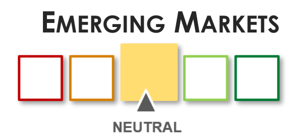
United States



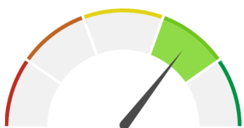
Japan



Emerging Markets



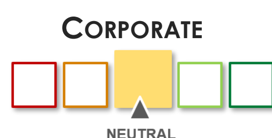
Bond Markets



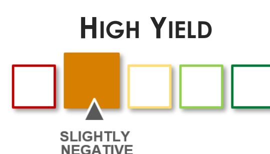
We are maintaining our current bond allocation, keeping portfolios slightly overweight in duration and favouring government bonds. The yield curves have unwound the excessive expectations of Fed and ECB rate cuts that were priced in at the beginning of the year, despite recent less favourable inflation data. However, we have not yet increased our exposure because financial conditions have not tightened and the rise in growth expectations may lead central banks to wait longer before embarking on a cycle of interest rate cuts to ensure that they do not lead to a subsequent rise in inflation. We are taking a more cautious approach to credit risk and continue to favour higher quality bonds, such as investment grade and financial subordinated bonds, over high yield and emerging markets. Overall, we prefer equity exposure to credit as long as we see earnings growth and companies capable of beating estimates.

Government

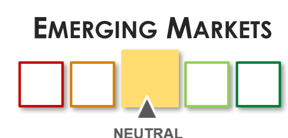
Corporate



High Yield



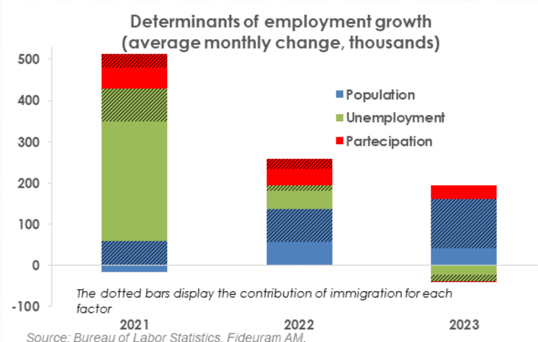
Emerging Markets



USA: All eyes are on inflation

Initial data on employment and inflation have been stronger than expected, especially in January, but they may be somewhat inflated by statistical distortions that are expected to diminish in the coming months. **We continue to expect growth to decelerate** from the rapid pace seen in the second half of last year, with price pressures gradually easing from the March data onwards. As a result, we continue to expect **the Federal Reserve to make its first rate cut (of 25 basis points) at its meeting in mid-June**, followed by three more cuts of 25 basis points each later in the year. However, recent inflation surprises point to a significant risk that the Fed will delay the start of rate cuts well beyond June.

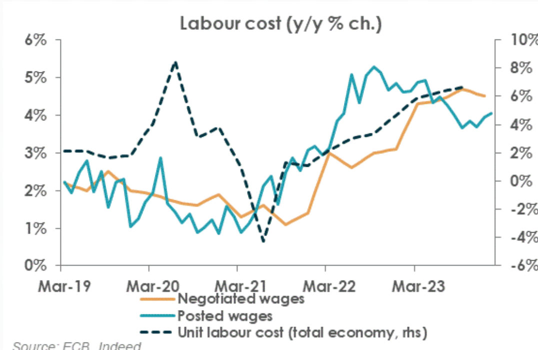
Increased immigration has boosted employment significantly over the past year



Euro Area: The ECB is looking ahead to June

There are signs of cyclical improvement: in February, the PMI index (a measure of business confidence) posted its strongest rise in four months, driven by a rebound in the services sector. The manufacturing sector remains weak due to Germany's struggles with structural industrial reconfiguration issues. However, the **sharp decline in natural gas prices** (even in long-term contracts) should allow for a gradual recovery in production and the competitiveness lost during the energy crisis. **Inflation continues to fall, albeit at a slower pace:** in February headline inflation fell to 2.6% (from 2.9%) and core inflation by only one decimal point to 3.1%. At its March meeting, the ECB hinted that **rate cuts might not start until the June meeting.** Market expectations for a rate cut in April are below 15%.

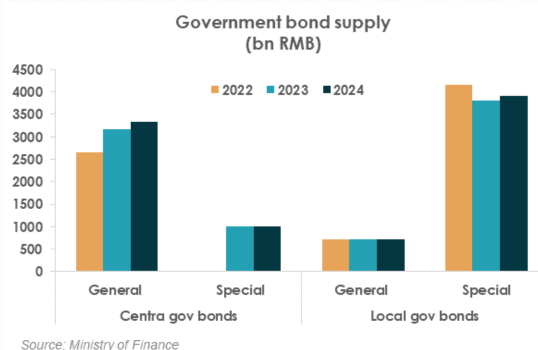
The ECB wants to see more data on wage dynamics before initiating rate cuts



China: unambitious fiscal package

As stated in the final document of the National People's Congress, **the growth target for the current year has been set at "around 5%"**. However, unlike 2023, **this is seen as an ambitious target for 2024,** as it lacks the benefit of a favourable base effect and more significant economic policy measures. **The 3% deficit/ GDP ratio was disappointing**, following the revision of the 2023 figure 3.8% in October last year. Moreover, the government seems unconcerned about deflation, favouring **supply-side policies** over demand-side measures (especially consumption). The accommodative monetary policy stance remains unchanged, with further interest rate cuts and reductions in the reserve requirement ratio expected in the coming months.

Chinese authorities have decided to issue one trillion yuan of long-term bonds to finance key projects



Fideuram Asset Management Economic Forecast

	GDP			Inflation			Monetary Policy Rate		
	2023	2024*	2025*	2023	2024*	2025*	2023	2024*	2025*
US	2,5	2,2	1,7	4,1	2,9	2,3	5,38	4,38	3,38
Eurozone	0,5	0,5	1,2	5,5	2,4	2,1	4,50	3,25	2,50
Japan	1,9	0,8	1,2	3,2	2,4	1,9	-0,10	0,00	0,00
China	5,2	4,9	4,6	0,2	0,8	1,5	2,50	2,30	2,30

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

** Fideuram Asset Management Forecasts*

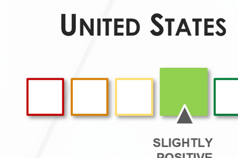
FIDEURAM INTESA SANPAOLO PRIVATE BANKING Asset Management

EQUITY MARKETS

EUROPE

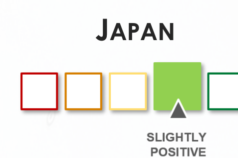
Valuations are modest and trade at a significant discount to the US. Current macroeconomic momentum is less robust and earnings are weaker, partly due to differences in sector composition and the lower influence of the technology sector. Nevertheless, we anticipate a potentially more favourable period for European equities in the coming quarters, driven by improvements in the macroeconomic outlook and earnings momentum in the second half of the year. As a result, we have started to gradually increase our investment in the European market, resulting in a slight overweight position.

UNITED STATES



From a fundamentals perspective, we continue to favour the US market due to the superior quality of companies and strong earnings growth. Valuations are at the higher end of the spectrum, but we expect them to remain stable, at least in the short term. While the portfolios remain heavily exposed to the technology sector, we have started to gradually diversify across sectors and styles, favouring names that have underperformed and are undervalued relative to large caps. We expect other sectors to show improved sequential earnings growth in the second half of the year, supported by favourable economic conditions.

JAPAN



After the recent significant increase, we are reducing exposure slightly but maintaining an overweight position based on a mix of still attractive valuations and earnings growth expectations. Profit growth is influenced by both cyclical factors, such as rising inflation expectations and improved profitability in the financial sector due to the Bank of Japan's easing of yield curve control, and structural factors, such as balance sheet restructuring and increased investment.

EMERGING MARKETS

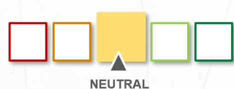
We remain neutral on emerging equity markets.
Valuations are attractive and there are expectations of a period of greater stability and additional stimulus from the Chinese authorities, even if the measures taken thus far have not fully met investors' expectations.

BOND MARKETS

GOVERNMENT

We remain overweight in government bonds. We see a fair valuation of between 4.3% and 4.5% for 10-year Treasuries and between 2.3% and 2.5% for 10-year Bunds. Any potential rate hike above these levels is seen as an opportunity to increase exposure. While peripheral spreads are at the lower end of the fair valuation range, the current macroeconomic situation doesn't seem compatible with a sudden widening, at least in the short term.

CORPORATE



The investment grade sector offers a favourable combination of yields and spreads, keeping returns stable at attractive levels. It remains our preferred segment within corporate credit risk, including financials. However, spreads are relatively tight, and therefore we prefer government bonds at this stage for their better ability to hedge equity risk.

HIGH YIELD

The robustness of the US economy is limiting the rise in defaults, even if lending standards deteriorate and higher capital costs affect lower-quality loans. Despite historically attractive expected returns, we remain underweight as we favour equities over riskier assets, particularly as long as companies continue to deliver growth and upward earnings revisions. This strategy also helps manage the credit risk associated with central banks keeping interest rates high.

EMERGING MARKETS

We remain neutral on emerging markets, with a slight bias towards local currency debt over hard currency debt. While spreads are relatively tight and offer limited potential for further narrowing, local yield curves appear less vulnerable, despite significant rate cuts already being priced in.

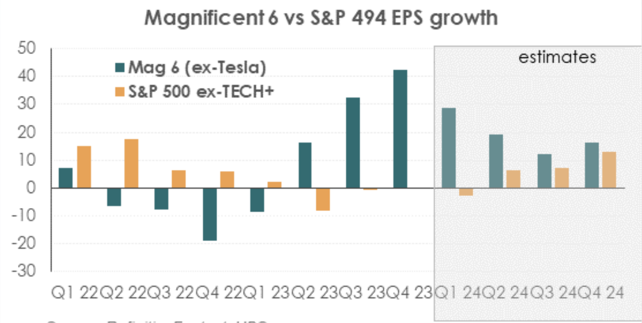
EQUITY MARKETS

THE OVERWEIGHT POSITION IN EQUITIES IS INCREASING IN ANTICIPATION OF A BROADENING MARKET LEADERSHIP.

We maintain an overall overweight position in equities, which has been expanded in recent weeks, not only in terms of size, but also in terms of diversification towards sectors/regions that have lagged behind the technology segment in terms of valuations and earnings momentum.

Specifically, the overweight in European equities has been slightly increased, while the overweight in Japanese equities has been reduced.

The earnings gap between large-cap companies and the rest of the market is expected to narrow

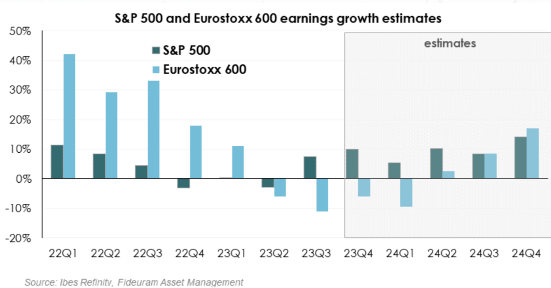


Source: Refinitiv, Factset, UBS

Exposure to US equities remains overweight, but we've increased sector diversification while slightly reducing exposure to mega-caps which, in this early part of 2024, continue to dominate the market. The continued good levels of economic growth that have until now mainly characterised the US economy, if protracted, could reasonably translate into earnings growth in those sectors that have lagged somewhat behind the outperformance of the mega caps.

It's important to note that looking ahead, analysts are forecasting robust earnings growth for the technology sector, particularly for large-cap stocks, outpacing the rest of the market, largely driven by advances in artificial intelligence. However, upcoming quarterly earnings growth forecasts suggest that other market segments will gradually improve their earnings growth, thereby narrowing the gap with large-cap technology companies.

Geographically, the earnings gap between the US and Europe is expected to narrow



Source: Ibes Refinitiv, Fideuram Asset Management

Even from a geographical perspective, given the long-standing valuation discount to the US, the decision to initially overweight the European market is driven by the expectation that the earnings gap will gradually close. As the cyclical outlook improves in Europe, we expect a sequential improvement in quarterly earnings, turning from negative to positive in the second half of the year and improving steadily thereafter.

The increased exposure to the European market is also an indication of increased diversification towards value-oriented investments.

FIDEURAM INTESA SANPAOLO PRIVATE BANKING Asset Management

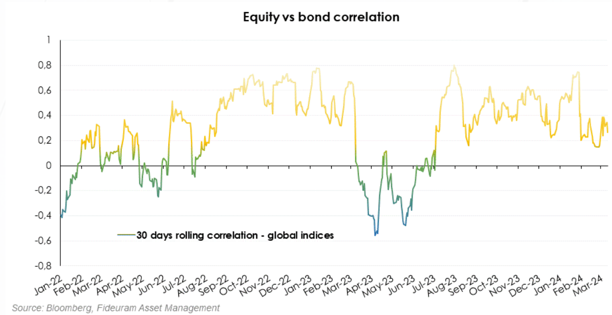
BOND MARKETS

EFFECT OF MONETARY POLICY EXPECTATIONS ON GOVERNMENT YIELDS

Looking to bonds, there is no change in the approach as we maintain a marginal overweight in duration focused on exposure to government bonds, both US and European.

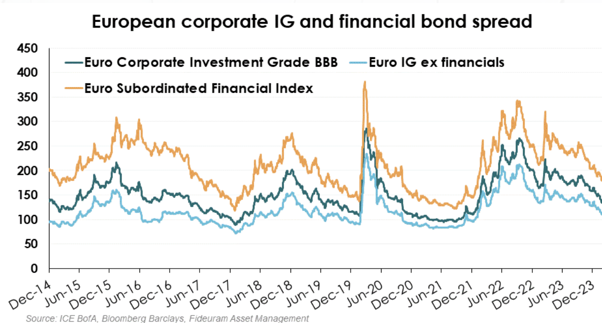
We remain more cautious on credit risk, where we continue to favour higher quality and financials over more speculative segments and emerging markets. In Europe in particular, the financial sector still offers attractive spread levels.

The positive correlation between bonds and equities declines



More generally, there is a preference for equity risk over credit risk as long as earnings continue to grow and companies are able to beat estimates. This preference, combined with a preference for government bonds, is based on the expectation that the positive correlation between bonds and equities will gradually diminish. In general, the market has gradually moved from a context in which expected monetary tightening led to both a rise in bond yields and a compression in equity multiples (via an increase in the discount factor) to one in which the rate hike is linked to an improvement in growth expectations. The recent rise in interest rates has been well absorbed by equity markets, as this move has not led to a tightening of financial conditions, as the improvement in economic growth expectations has acted as a counterweight. This context is helping to restore the protective mechanism of the negative correlation between bonds and equities in the event of weaker-than-expected growth.

In Europe, the financial sector offers attractive spreads



Despite these developments, we have not increased our exposure to government bonds because the relative strength of the economic cycle could lead central banks to delay a cycle of interest rate cuts to ensure that they do not lead to a subsequent rise in inflation.

FIDEURAM INTESA SANPAOLO PRIVATE BANKING Asset Management

FIDEURAM INTESA SANPAOLO PRIVATE BANKING Asset Management

DISCLAIMER:

*This material has been prepared by Fideuram Intesa Sanpaolo Private Banking Asset Management SGR S.p.A., which is an asset management company enrolled in the register of the asset management companies held by the Bank of Italy no.12 and belonging to the Intesa Sanpaolo banking group ("**Fideuram Asset Management SGR**").*

This material – for internal use only – has been prepared in a limited number of copies and it is for information purposes only.

This material is for distribution to professional clients and authorized intermediaries only and should not be relied upon by any other persons.** Any distribution by whatever means, of this document and related material to persons other than those referred to above is strictly prohibited. **Fideuram Asset Management SGR is not responsible in case of distribution and delivery of this material to third parties.

*This material does not constitute investment research and under no circumstances it should be used or considered as an offer, inducement, invitation, solicitation or recommendation to buy or sell any security or financial instrument or service or to pursue any investment product or strategy or otherwise engage in any investment activity or as an expression of an opinion as to the present or future value or price of any security or financial instrument. The information contained in this material may change as subsequent conditions vary. **The data, unless otherwise specified, do not take into account the applicable tax regime.***

This material has been prepared based on data processed by Fideuram Asset Management SGR (and by other companies of Intesa Sanpaolo banking group) and based on publicly available information or other third-party sources. Fideuram Asset Management SGR does not guarantee the accuracy, completeness and reliability of the data and information contained in this document and declines any responsibility in this regard.

This material has been provided as a general market commentary only and nothing contained in this material is intended to constitute legal, tax, securities or investment advice and it is not predictive of future performance, and should not be construed as an offer to sell or a solicitation to buy any security or make an offer where otherwise unlawful. This material may not be distributed or used for the purpose of offers or solicitations in the United States or in Canada or towards individuals resident in any jurisdiction or in any circumstances in which such offers or solicitations are unlawful or not authorized, or where there would be, by virtue of such distribution, new or additional registration requirements.

PAST PERFORMANCE IS NOT A GUIDE TO FUTURE PERFORMANCE. THE VALUE OF INVESTMENTS CAN FALL AS WELL AS RISE, SO INVESTORS MAY GET BACK LESS THAN ORIGINALLY INVESTED.

*This material has not be filed with Consob pursuant to article 101 of legislative decree 58/98 as amended from time to time **("Italian Consolidated Financial Act").***

The information in this publication should not be relied upon in making investment decisions.

Fideuram Intesa Sanpaolo Private Banking Asset Management SGR S.p.A.

Via Melchiorre Gioia 22, 20124 Milano
Phone +39 02 725071 – Fax 02 72507626
www.fideuramispbsgr.it

Group company of