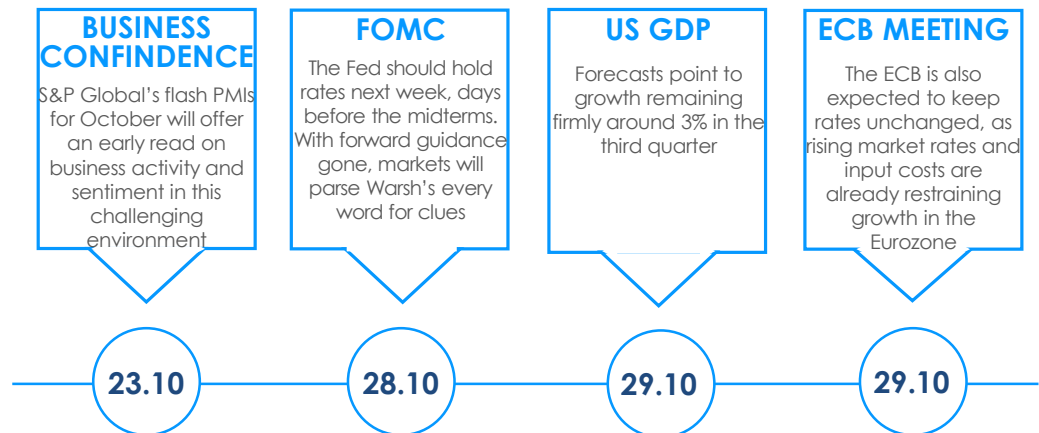


Main Events

Azimut Global Network

- * Milan
- * Abu Dhabi
- * Austin
- * Cairo
- * Chicago
- * Dubai
- * Dublin
- * Hong Kong
- * Estoril
- * Istanbul
- * Lugano
- * Luxembourg
- * Mexico City
- * Miami
- * Monaco
- * New York
- * Santiago
- * São Paulo
- * Shanghai
- * Singapore
- * St Louis
- * Sydney
- * Taipei



THE BOND MARKET TAKES A BREATH

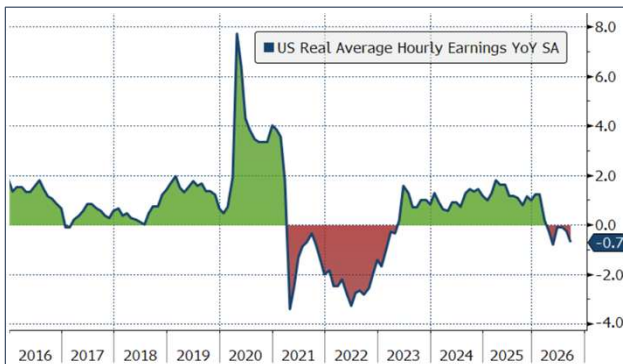
- **A softer tone from Fed governors alongside weak readings in real disposable income and retail sales halted the bond route, reversing most of late-quarter yield spikes**
- **The rally remains vulnerable to underlying inflationary pressures, as consumer and producer price indices rose more than expected**
- **However, investors should exploit ongoing volatility to gradually increase exposure to bonds, as risk-free rates around 5% offer compelling carry and could again act as a hedge for the portfolio, though tight credit spreads still warrant caution in riskier debt**

Over the past two weeks, selling pressure on bonds has eased due to a combination of factors, from macroeconomics to positioning.

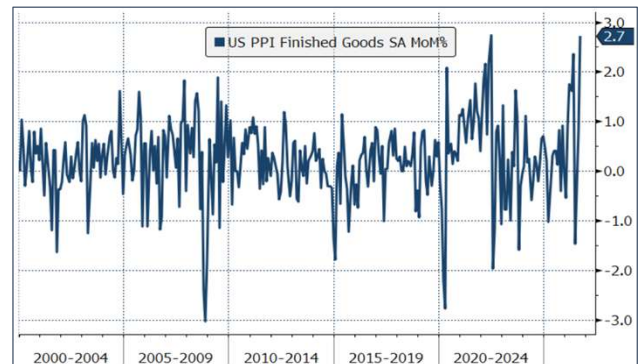
First and foremost, remarks by some Fed governors—such as Christopher Waller and Michelle Bowman—helped soothe investors' nerves, as they stated that rate increases "do not need to come at consecutive meetings." The rise in market rates has indeed already led to a tightening of monetary conditions equivalent to at least one Fed rate hike, thereby reducing the need for the Fed itself to act. John Williams, President of the powerful Federal Reserve Bank of New York, went further by stating that "it may be appropriate to have one more rate hike" this year to ensure inflation returns toward target, while explicitly indicating that he sees no current justification for additional rate hikes extending into 2027. Such a scenario is much more favorable for the markets than the three rate hikes currently still priced in by Fed Funds futures.

But two other macroeconomic indicators also contributed to the recent decline in interest rates, both of which fueled concerns about the resilience of the US Consumer. The first was the data on real wages, which fell 0.7% year-over-year, as inflation outpaced nominal wage growth, particularly in recent months. The real wages data was released at the same time as the CPI data, which showed inflation jumping 0.6% month-over-month in September (0.65% unrounded), lifting the headline annual rate to 3.7%. The reading exceeded Wall Street forecasts of 3.6% and marked a noticeable reacceleration from the 3.4% annual pace seen in both July and August.

(continued)



Source: Bloomberg



Source: Bloomberg

Excluding the volatile food and energy sectors, the core CPI rose 0.3% month-on-month (0.33% unrounded), defying expectations of a slowdown to 0.2%, with core inflation edging up to 2.6% on a yearly basis.

The market's reaction to these two macroeconomic data was quite telling: immediately after the release, the focus was on the inflation figure—objectively worse than expected—with the US two-year rate soaring from 4.77% to 4.95% in a matter of minutes. But after this initial emotional reaction, market rates declined steadily for the rest of the day, with the two-year yield closing at 4.80%, as investors focused more on the possible impacts on economic growth. With purchasing power eroding, households are more likely to cut back on discretionary spending, particularly those without assets who struggle the most to make ends meet.

These concerns intensified the following day, with the release of retail sales data: overall retail sales jumped 0.8% month-over-month, comfortably topping consensus forecasts of 0.6%. Yet beneath that impressive figure lies a starkly different reality. The rise in retail sales, which are calculated in nominal terms, was driven by a 6.4% monthly surge in receipts at gas stations, caused by a sharp 9.1% spike in pump prices. Once gasoline and automotive purchases are excluded, retail spending rose a meager 0.2%. The control group sales figure—which excludes the most volatile categories and mostly correlates with GDP's calculation—crawled ahead by just 0.1%, falling short of Wall Street's expectations of +0.3% and representing a sharp slowdown compared with the downwardly revised +1.2% (nominal) increase recorded in August.

The dovish statements by Fed governors, combined with the rapid succession of data releases suggesting some strain on consumers, triggered a quite meaningful drop in rates, fueled by extreme market positioning and oversold conditions. Indeed, over the previous weeks and months, investors—particularly CTAs—had built up enormous short positions betting that government bond yields in Western countries would continue to rise amid the threat of persistent inflation and massive bond issuance. Since CTAs were at max short in bonds, any significant drop in rates could have triggered a self-sustaining wave of short-covering. As a result, interest rates—both at the short- and long-end of the yield curves—have returned to levels similar to those prevailing a month ago, thereby almost completely reversing the sharp rise that occurred around the end of the quarter.

Even though many of the extremes have been eliminated, we are not necessarily out of the woods yet. Inflationary pressures continue to mount. More than the consumer price index, it is the producer price data that are causing concern. The “final demand” index—which has been adopted in recent years as the new benchmark for producer prices—rose by 1.3% in September alone, bringing the annual rate to +6.3%. In the version that excludes the volatile food and energy components, the increases were +0.7% and +5.0%, respectively. In the version that has been used as a benchmark for decades—the “PPI finished goods,” which is more volatile than the “final demand” version—the monthly increase was +2.7%, matching the highest reading during the inflationary spike of 2021–2022.

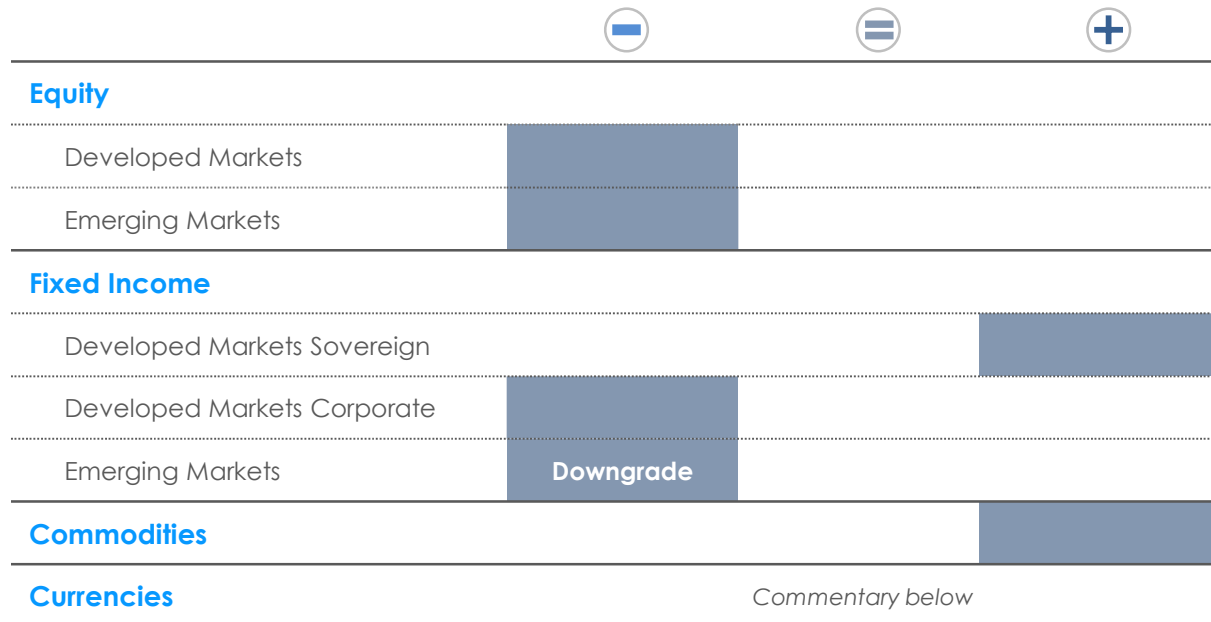
Since producer prices are gradually passed on to consumer prices, the path toward lower inflation may take longer than the market and central banks had anticipated, with volatility in the bond market likely to persist for some time yet. We therefore recommend continuing to take advantage of this volatility to gradually increase exposure to bonds in a portfolio.

(continued)

Indeed, at current yield levels, bonds offer significant carry. Moreover, since equities must deliver higher returns than the risk-free rate to compensate for their greater volatility (the so-called equity risk premium), risk-free rates around 5% are increasingly competitive with the expected long-term returns on equities. Finally, if risk appetite deteriorates significantly, government bonds could resume their role as a portfolio hedge from these levels, exactly as they did during the market turbulence that began in early October.

Within fixed income, however, caution is still warranted in the riskier segments of the credit market, where spreads, despite the recent widening, still do not adequately compensate for the risks.

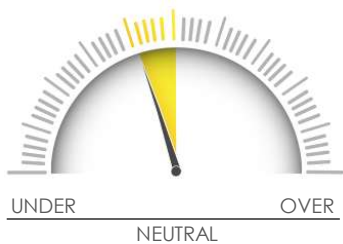
Asset Allocation View



⊖ UNDER
= NEUTRAL
⊕ OVER

Equity

Developed Markets



We have maintained our **Slightly Underweight** recommendation on Developed Market equities. The cracks appearing in the fixed-income market, the recent steep rise in nominal and real interest rates and geopolitical tensions are creating a tougher environment for equities. While we recognize that internal rotations among themes and sectors continue to support equity indices, we recommend keeping a more cautious approach. On the bright side, the most challenging period in terms of seasonality is slowly coming to an end, and the upcoming earnings season looks promising once again. Therefore, we continue to believe that any significant correction should be viewed as a buying opportunity, provided that economic and earnings growth remain solid.

US



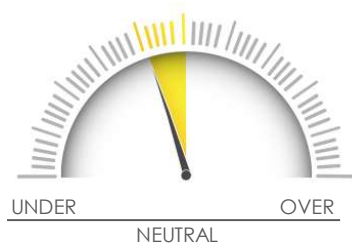
Europe



Japan



Emerging Markets



We have kept our **Slightly Underweight** recommendation on Emerging Market equities. The same factors—both positive and negative—mentioned above also apply here. Other reasons for caution stems from the hawkish stances of many central banks and the strengthening US dollar—all factors that typically weighs on emerging markets. On the positive side, emerging markets continue to trade at a significant discount relative to developed markets and remain the primary beneficiaries of hyperscalers' capex, owing to the heavy weighting of tech and semis in emerging market indices.

Asia ex-Japan



EEMEA

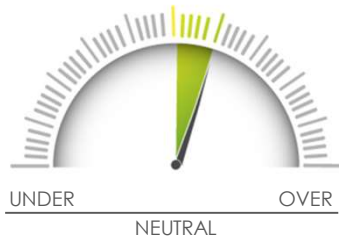


LATAM



Fixed Income

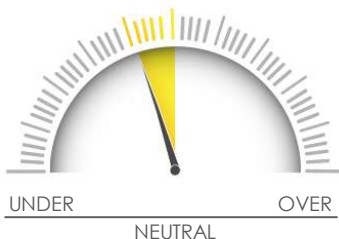
Developed Markets Sovereign



We kept our **Slightly Overweight** recommendation on Developed Market sovereign bonds. The recent decline in interest rates should be viewed as a natural retracement after the sharp jump of the previous weeks. Geopolitics, inflationary pressures, and hawkish stances by central banks suggest that rates could continue to rise. However, in a portfolio allocation, where one must consider the expected return of asset classes, the rise in rates cannot be ignored, and it is appropriate to gradually increase exposure. Not only to increase the portfolio's carry, but also because it is possible that duration can act as a portfolio hedge in case of troubles. We emphasize "gradually over time" precisely because we cannot rule out the possibility that the rise will continue for a while longer, particularly in light of recent CPI and PPI data in the US. We still prefer the short- and medium-term segments, which are subject to less volatility.

EU Core ☒ EU Periphery ☒ US Treasury ☒ Japanese JGB ☒

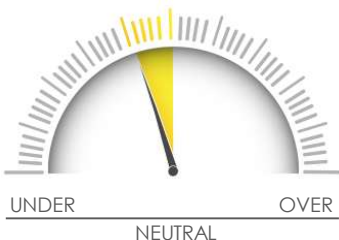
Developed Markets Corporate



We have maintained our **Slightly Underweight** recommendation on Developed Market corporate bonds. Although spreads on distressed securities have widened since mid-September, they are not yet considered attractive in either the investment-grade or high-yield segments. Within credit, we continue to prefer investment-grade bonds over high-yield.

IG Europe ☒ IG US ☒ HY Europe ☒ HY US ☒

Emerging Markets



We have lowered our recommendation on Emerging Markets Debt to **Slightly Underweight**. The ongoing turbulence in developed-market bonds is starting to weigh on investor appetite for emerging-market debt as well. Although emerging-market bonds still offer higher yields than developed-market bonds with the same credit rating, we prefer to remain cautious here too.

Local Currency ☒ Hard Currency IG ☒ Hard Currency HY ☒

Commodities



We have maintained our **Slightly Overweight** recommendation for commodities. We remain tactically cautious on precious metals given the risk that global rates may still move higher, but the long-term bull case remains intact. We are positive on industrial metals and rare earths, as supply shortages are set to worsen in the coming years due to their increasing adoption across various strategic sectors, including artificial intelligence, the space race, military applications, and energy production.

Precious ☒ Energy ☒ Industrial ☒ Agricultural ☒

Currencies

We have maintained our **Neutral** recommendation on the **US Dollar**. The greenback is currently seen as fair valued considering the interest rate differential.

We have maintained our **Neutral** recommendation on the **Euro** as well. Recent concerns about Europe seem to be slightly subsiding, suggesting that a consolidation might take place in the near future.

The recommendation on the **Chinese Renminbi** remains **Neutral**.

Likewise, the outlook for other **emerging market currencies** has been maintained at **Neutral**.

Euro	=	USD	=	CNY	=	Other EM	=
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