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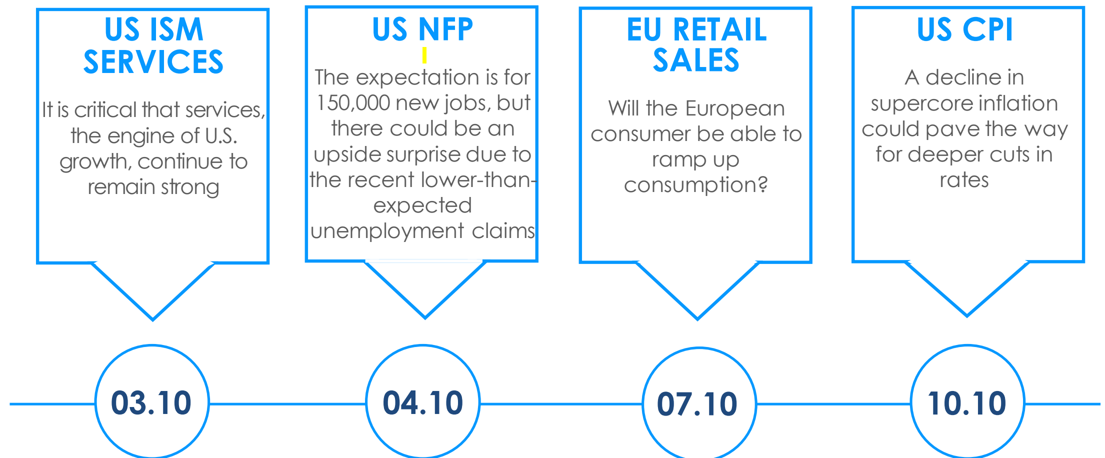
AZIMUT GLOBAL VIEW

30.09.24

Main Events



Azimut Global Network

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

FED OVERDO, PBOC OVERDUE

- **The Fed began its rate cut cycle with a 50 bps reduction, more than the market expected, and slashed projections of where rates might be at the end of 2024 and 2025.**
- **Given the trajectory of inflation and the weakening labor market, the Fed is likely to deliver the cuts projected by the dots, with the possibility of doing more if needed.**
- **After years of market-hostile policies, China has finally pulled out the monetary and fiscal bazooka. The rebound that started last week still has legs.**

The Federal Open Market Committee (FOMC) concluded one of its most closely watched meetings with a decision to cut interest rates by 50 basis points, bringing the federal funds rate at a range of 4.75 per cent to 5 per cent, with only one dissenter. A cut of this size came as a surprise to most. Nearly four-fifths of economists surveyed by Bloomberg predicted a 25 basis point cut, while the market was pricing in a 70 percent probability of a 50 basis point cut immediately ahead of the meeting, but was around 50 percent just days before.

This "jumbo" cut is consistent with Powell's statement at Jackson Hole that it was time for the Fed to adjust its monetary policy, and signals a significant change in the Federal Reserve's monetary stance for months to come. But more than the size of the first cut, what matters to markets is the speed and cumulative amount of rate cuts to be expected over the entire cutting cycle that has just begun.

In this regard, Powell was keen to caution that such a large cut will not be the norm going forward, that the Fed's actions were not on a "preset path" and future adjustments would depend on incoming data. Also, in the dot plot, the median projection for the federal funds rate pointed to 4.4% for 2024, implying that the central bank could make two more 25-basis-point cuts this year, fewer than the market expected ahead of the meeting. The median projection for the federal funds rate pointed to 3.4% by the end of 2025, implying four 25 basis point cuts, and 2.9% by the end of 2026.

(continued)

Source: Bloomberg

China's Announced/Reported Stimulus Measures

Sector	Measure	Status
Monetary	Seven-day reverse repurchase rate cuts	Delivered on Sept. 27
	Medium-term lending facility rate cuts	Delivered on Sept. 25
	Loan prime rate cuts	To be guided lower
	RRR cuts	Delivered on Sept. 27, more could come
Property	Outstanding mortgage rate cuts	Delivered on Sept. 29
	Cuts on minimum down-payment ratio on second-home purchases	Delivered on Sept. 29
	Expansion of PBOC re-lending program	Delivered on Sept. 29
	Megacities to relax curbs for non-local buyers	Delivered by Guangzhou on Sept. 29
	Scrapping of distinctions between first- and second-home purchases	Delivered by Guangzhou on Sept. 29
Stocks	Swap facility to tap PBOC money to purchase equities	Still to come
	Re-lending facility to buy back shares and raise holdings	Still to come
	A possible stabilization fund	Still to come
	New measures to encourage mergers and acquisitions	Delivered on Sept. 24
Finance	Addition of core tier 1 capital to six major commercial banks	Still to come
Fiscal	Potential issuance of special sovereign bonds	Still to come

Source: Government statements, media reports

Source: Bloomberg

Instead, the so-called terminal rate rose to 2.9% from 2.8%. That's a small change, but 2,9% is significantly up from 2,5% in December 2023, a level where it had been virtually unchanged for years. Moreover, the terminal rate will be reached already in 2026, compared to 2027 as it was in the June dot projections.

The new dot plot, while indicating a more moderate pace of rate cuts than the market expected (which notoriously tends to err on the side of over-optimism), shows a much more rapid and pronounced path of rate cuts than was predicted in June, aligning with the need for a change of stance in monetary policy communicated in Jackson Hole.

Federal Reserve Chair Jerome Powell's remarks following the decision were aimed at reassuring markets that the U.S. economy is still "in a good place." He described the rate cut as part of a "recalibration" of the Fed's policy stance to avoid unnecessarily harming the economy or the labor market, while at the same continuing to achieve further progresses on inflation.

Powell also sought to alleviate concerns about falling behind the curve, stating, "We do not think we are behind [in cutting rates]," underscoring the Fed's commitment to remain responsive and ready to act, even forcefully, if warranted.

In short, the Fed's decision was interpreted by most as a hawkish cut. Instead, the committee's view is that the Fed is rushing to exit its now overly restrictive monetary policy, considering the marked progress in inflation (although supercore inflation still remains elevated) and the weaker-than-expected labor market, particularly in light of the huge downward revision (-800k) in the number of jobs created in the year ending March 2024, released just before the Jackson Hole meeting.

Therefore, the path laid out by the dot plot seems to be the bare minimum, with the possibility for the Fed to cut more aggressively if the economy, and particularly the labor market, were to show signs of further deceleration. In this regard, it is worth mentioning that Powell has repeatedly stated in recent weeks that any further weakening of the labor market is unwelcome to the Fed.

Adding fuel to the fire, China finally pulled out the bazooka.

In stark contrast to previous piecemeal and ineffective measures, the set of actions outlined by the Chinese authorities is substantial and comprehensive. This shift in stance should enable the Chinese economy to achieve its 5 percent GDP growth target for 2024, revitalize an ailing real estate market, and revive a stock market that since 2021 has undergone its biggest underperformance in decades.

The information reported in this document has been extrapolated from Bloomberg and external research sources, and subsequently re-elaborated by Azimut Investments S.A. Please read the disclaimer at the end of this document

(continued)

Source: TO BE INSERTED

Source: Bloomberg

Among the major steps:

- The Medium-Term Lending Facility rate was cut by 0.3%, the biggest-ever decrease
- The seven-day reverse repurchase rate was lowered to 1.5% from 1.7%.
- The required reserve ratio (RRR) was cut by 0.5%, injecting 1 trillion yuan ($145 billion) in liquidity. Another cut, between 0.25 and 0.5 bps, is expected in the next three months.
- Minimum down-payment ratios were slashed to 15% for second-home buyers, down from 25%.
- Loan prime rates and deposit rates are set to decline by 0.2 to 0.25 percentage points.
- The PBOC will fully cover local government loans for purchasing unsold homes with cheaper funding, up from the previous 60%.

Additionally, China's homeowners were granted the option to renegotiate their mortgage terms, starting November 1. This will allow borrowers to switch to lower rates, providing relief to millions of households. The PBoC announced 500 billion yuan ($71 billion) equity market swap facility to allow non-bank financial institutions (insurers, funds, and securities companies) to borrow from the PBoC to purchase Chinese equities; this facility could be expanded up to 1.5 trillion yuan. Additionally, a separate specialized relending facilities will also be set up for listed corporates to support buybacks, totaling 300 billion yuan ($42 billion); this facility could be expanded up to 900 billion yuan. PBoC also confirmed that a National Stabilization fund is under consideration. Finally, the Politburo pledged further fiscal stimuli by the end of the year, worth about 2 trillion yuan ($290 billion), funded through the issuance of long term special sovereign bonds.

The massive set of measures are expected to be pivot for equities. After years marked by market-hostile monetary and fiscal policies and unprecedented geopolitical tensions with Western countries, international and domestic investor sentiment toward Chinese stocks was extremely negative. This led to a flight from Chinese stocks, which reached record-high valuations. Because of this extreme underweighting, the measures announced caused massive short covering. Chinese stock markets rose 25 percent in 5 days, the biggest jump ever.

Although this is an extraordinary surge, there is no reason to worry. Valuations are still extremely attractive and at a discount compared to where they might have been had years of market-hostile policies not occurred. Chinese markets still have ample room to continue their ascent.

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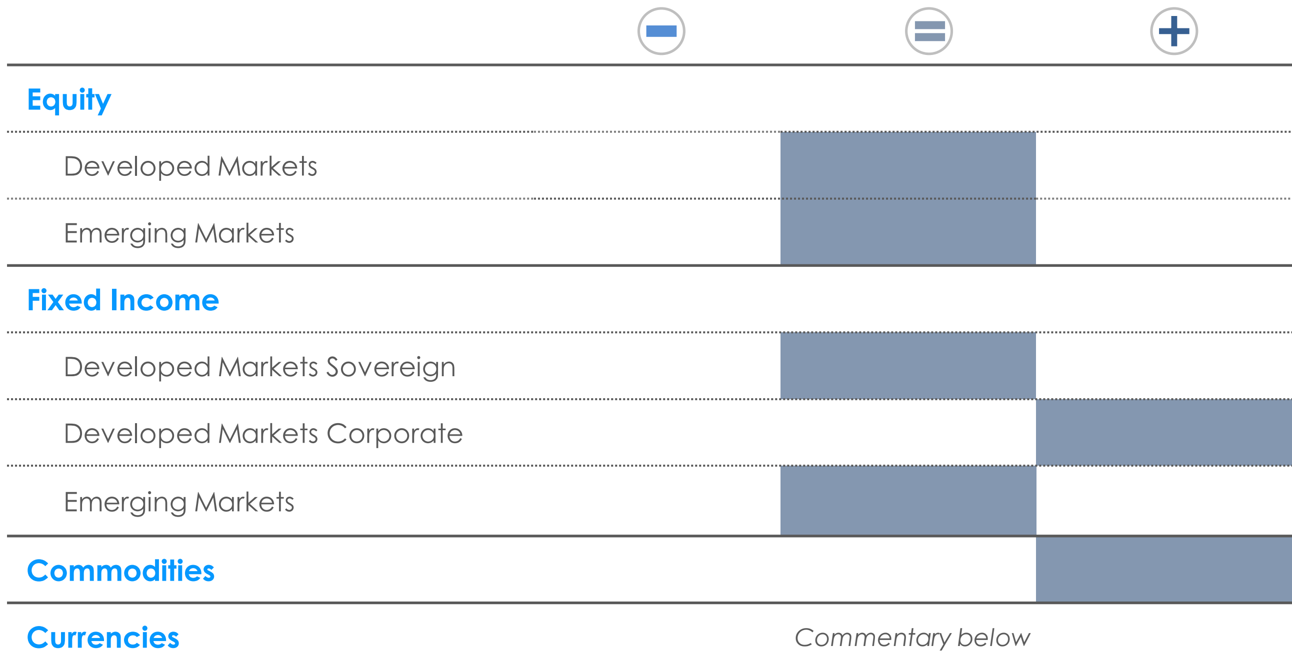
Asset Allocation View

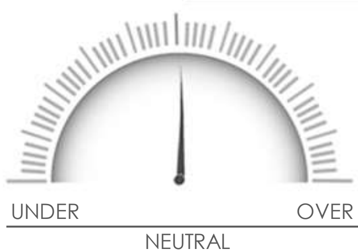


	Under (−)	Neutral (=)	Over (+)
Equity			
Developed Markets		■	
Emerging Markets		■	
Fixed Income			
Developed Markets Sovereign		■	
Developed Markets Corporate			■
Emerging Markets		■	
Commodities			■
Currencies		*Commentary below*	

UNDER NEUTRAL OVER

Equity

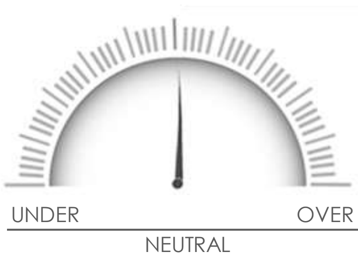
Developed Markets



We have kept our **Neutral** recommendation on Developed Market Equities. We expect markets to remain range-bound around current levels for the near term. The potential for further easing by central banks, ample liquidity, and consistently strong economic data are counterbalanced by elevated valuations. Among developed markets, we are more cautious on Japan due to its higher volatility and the strength of the yen.

US	Europe	Japan
Neutral (=)	Neutral (=)	Under (−)

Emerging Markets



We have maintained our **Neutral** recommendation on Emerging Markets Equities. The massive stimulus measures announced by China last week sparked a sharp rally in Chinese stocks. While some consolidation may occur in the short term, the still deeply discounted valuations and the shift in investor sentiment toward China provide significant potential for the rally to extend in the medium term. Looking ahead, the recovery of the Chinese economy could boost commodities, benefiting Latin America, where we maintain a positive outlook, though tempered by political concerns.

Asia ex-Japan	EEMEA	LATAM
Neutral (=)	Under (−)	Neutral (=)

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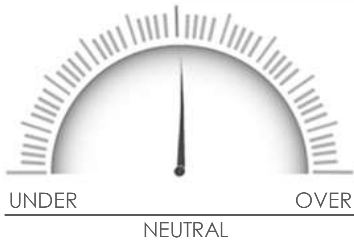
Fixed Income

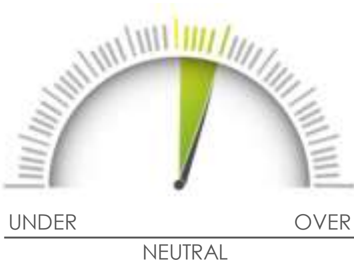
Developed Markets Sovereign



We have maintained our **Neutral** recommendation on Developed Markets Sovereign Bonds. The larger-than-expected rate cut by the Fed, the projected faster decline in rates as indicated by the dot plot, and the potential for more aggressive action if macroeconomic data weakens are all supportive factors for this asset class. However, our recommendation remains neutral as current rates have already priced in more easing than the Fed has suggested.

EU Core	EU Periphery	US Treasury	Japanese JGB

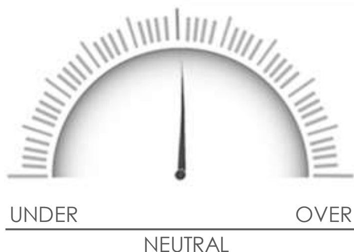
Developed Markets Corporate



We have kept our **Slightly Overweight** recommendation on Developed Markets Corporates. Given that the positive contribution from duration is likely to be limited going forward, as mentioned above, the search for yield within the fixed income market will continue to favor corporate bonds. Among corporates, we maintain our preference for investment-grade bonds over high-yield bonds.

IG Europe	IG US	HY Europe	HY US

Emerging Markets



We have also maintained our **Neutral** recommendation for Emerging Market bonds. China's stimulus measures could increase demand for the asset class; however, spreads are already quite tight, particularly for low-beta bonds.

Local Currency	Hard Currency IG	Hard Currency HY

Commodities

We confirmed our **Slightly Overweight** recommendation on Commodities. Within commodities, we remain positive on precious metals, which tend to outperform in times of monetary policy easing, in addition to serving as a portfolio hedge in the event of unexpected geopolitical tensions and political uncertainties. After the massive Chinese stimuli, we turned bullish on industrial metals as well.

Precious	Energy	Industrial	Agricultural

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Currencies

The Committee kept the **Neutral** stance on the US Dollar, but **with a bearish bias**. Although at current levels the dollar is fairly valued, the possibility that the Fed will continue to surprise on the dovish side, combined with the fact that the dollar is approaching critical support at 1.1250, could lead to further weakening.

The view on the Euro remains **Neutral with a bullish bias**. The reasons for the bullish bias on the euro are the same (in reverse) as those mentioned for the dollar. In addition, the ECB appears to be less responsive than the Fed, with the possibility of the rate differential shifting in favor of the euro.

The view on the **Chinese Renminbi** is maintained **Neutral**. The expected strong inflows due to the repositioning of the financial community in China are likely to be offset by the lower rates following the PBoC cuts.

The outlook for other **emerging market currencies** is **Neutral**. Among emerging currencies, in the current environment the Committee favors Asian currencies.

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