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

09.05 — CHINA NEW LOANS
Will Chinese lending data (new loans and aggregate financing) continue to support the nascent recovery of the domestic economy?

10.05 — US INFLATION EXPECTATIONS
University of Michigan data are expected to confirm that inflation expectations remain anchored

15.05 — US CPI
For the stability of financial markets, it is essential that inflation does not surpass expectations for the fourth consecutive month

16.05 — JAPAN GDP
After narrowly escaping a technical recession, defined as two consecutive quarters of negative growth, Japan's GDP is anticipated to experience a sharp decline once more

STICKING TO THE DOVISH STANCE

- **The Federal Reserve proved less hawkish than expected, and willing to scrap the tail scenarios about the trajectory of rates**
- **Quantitative tightening (QT) will be reduced as early as June, and by an amount ($35 billion) that is larger than anticipated, thereby diminishing the liquidity withdrawn from financial markets**
- **The Fed also appears committed to maintaining the easing bias it has held since December. However, the first rate cut, if it occurs, will not happen before September 2024 at the earliest**

After the streak of stronger-than-expected macroeconomic data in recent months, which showed a notable resilience of both inflation and economic growth, the financial community was anxiously awaiting the Fed meeting, fearing that it might have to abandon hopes of a rate cut in 2024 altogether. Some had even begun to speculate that the Fed's next move might be a hike and not a cut.

The post-FOMC press conference allowed everyone to breathe a sigh of relief.

Indeed, the first important takeaway from the conference call is that Powell and the Fed seemed willing to dismantle the “tail risks” that the market had been pricing in recent months (in some cases induced by the Fed itself...): earlier in the year, an aggressive series of rate cuts, and more recently, even the possibility of further hikes.

To dispel those risks he said that "it's unlikely that the next policy rate move will be a hike" and "our policy focus is really [...] how long to keep policy restrictive. "This means that the most the Fed will do is keep rates at the current level, possibly extending the duration for which rates will remain at this level. However, a rate hike is still out of the question despite the stronger data on inflation and growth. On the other hand, the FOMC statement included the phrase “in recent months, there has been a lack of further progress toward the Committee's 2 percent inflation objective.”

(continued)

The addition of this sentence, which acknowledges the stickiness of inflation, will de facto prevent the Fed from cutting rates at least until September: it would be extremely complicated for the Fed to do an about-face before then, barring a dramatic deterioration in the macroeconomic situation that currently does not seem plausible.

In short, the Fed has ruled out the tail scenarios (a substantial drop in rates as well as the possibility of further hikes), thereby greatly reducing uncertainty about the trajectory of rates. For the market, which does not like uncertainty, this is definitely a positive development.

The second takeaway is that the Fed has announced a more significant tapering of QT than anticipated: starting in June, QT will be reduced from $90 billion per month to $55 billion, achieved by lowering the monthly redemption ceiling for Treasury securities from $60 billion to $25 billion. We remember that back in December, the Fed surprised the market by floating the possibility of reducing the QT, an option almost no one expected at the time. Today, history seems to be repeating itself: although the tapering of QT was expected to be announced either at this meeting or the next one in June, the Fed has once again surprised with a dovish stance. This surprise comes both in the unexpectedly large size of the tapering and its immediate implementation, without a gradual phase-down. This development, like the previous one, is also favorable to markets, as a more gradual reduction of excess liquidity benefits all asset classes, especially the riskier ones

The third takeaway is that the Fed appears committed to the dovish stance it adopted in December, when it unexpectedly signaled the possibility of three rate cuts in 2024 along with a tapering of QT—countering the market's acceptance of a 'higher for longer' narrative. Since December, there has been a widespread expectation that the first rate cut would occur in June. However, recent data on inflation and growth have ruled out this possibility. The larger-than-anticipated reduction in QT, set to take effect in June, can be interpreted as the Fed's method of initiating a stealthy monetary easing at the time it had originally indicated a willingness to do so.

Similarly, despite data indicating a clear re-acceleration of inflation well above the 2 percent target, a further rate hike has been ruled out. Additionally, Powell mentioned in the conference call that even if inflation proves more resilient than expected, rate cuts could still be possible should the labor market show signs of weakening.

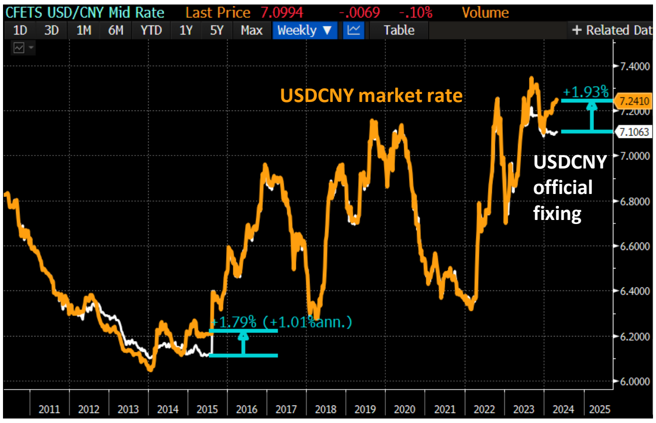
It is not possible to know what is the real reason behind this persistent easing bias of the Fed. One possible reason was offered by former Dallas Fed Governor Kaplan in a recent interview: the root cause behind the resilience of inflation is the excessively loose fiscal policy of the U.S. government, which continues to run high-single-digit deficits, forcing the Fed to be more restrictive than it should be. Another possible explanation is that the Fed is concerned about some weak spots, such as the drop in existing home sales, the strain on the commercial real estate sector, or the rising delinquency rates in some segments of the consumer credit. Additionally, the Federal Reserve may be concerned about the trajectory of interest expenditure on U.S. debt, which has now far exceeded one trillion dollars on an annualized basis - a figure higher than the budget allocated for military spending.

Perhaps the most concrete, or at least the most apparent reason is that keeping high interest rates in the U.S. – a consequence of its stronger economy (even if "doped" by fiscal stimulus) is causing excessive strain outside the United States, particularly in Asia and emerging markets. The growing gap between growth and inflation in the United States relative to the rest of the world has cemented the expectation that U.S. monetary policy will remain much tighter than what might be necessary in other countries. As a result, the rate differential has widened in favor of the United States, putting many of the world's currencies under pressure.

In this regard, much attention has been given to the weakness of the yen, which has touched the 160 mark against the dollar, losing 1/3 of its value in the past three years and halving in just over a decade. But, in recent weeks, many emerging currencies have also begun to suffer against the dollar. Among them, the Chinese yuan is the one that deserves the most attention, although the financial community seems not to be paying much attention to it.

(continued)

Source: Bloomberg



Source: Bloomberg

Recall that for years the renminbi exchange rate has been allowed to fluctuate within a band of +/-2% from the official fixing set by the central bank. In case of deviations beyond these thresholds, the central bank is supposed to intervene to keep the market exchange rate within this band. Under normal conditions, the market cross rate and the Chinese central bank fixing coincide. Since the beginning of the year, however, the market has brought the renminbi exchange rate closer and closer to the +2% threshold (thus to the maximum level of weakness allowed by the band). Let us also recall that such a situation previously occurred only between 2014 and 2015, just before China unexpectedly devalued the renminbi in August 2015, triggering major disruptions in financial markets. At that time, the renminbi had been slowly and steadily appreciating against the dollar for years, and it also offered a higher interest rate than the dollar. This scenario led to substantial leveraged long renminbi and short dollar positions by hedge funds, capitalizing on what was one of the most lucrative and least volatile carry trades of the period.

The losses incurred on those carry trade positions after the sudden devaluation is what then created the disruption in the financial markets. Today the situation is completely different, since there are no longer any significant carry trade positions on the renminbi. Nevertheless, a sudden devaluation of the Chinese yuan could cause in turn some volatility in the markets, since it could lead to chain reactions from other emerging countries.

In summary, it is expected that for various reasons (domestic and international) the Federal Reserve will be incentivized to cut rates as soon as it is put in a position to do so, either because of a decline in inflation or in reaction to a possible slowdown in the business cycle. However, this will probably not happen before the end of the summer.

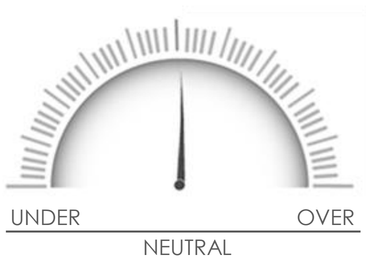
Asset Allocation View

	−	=	+
Equity			
Developed Markets		Upgrade	
Emerging Markets			Upgrade
Fixed Income			
Developed Markets Sovereign			■
Developed Markets Corporate			■
Emerging Markets		■	
Commodities			■
Currencies		*Commentary below*	

− UNDER = NEUTRAL + OVER

Equity

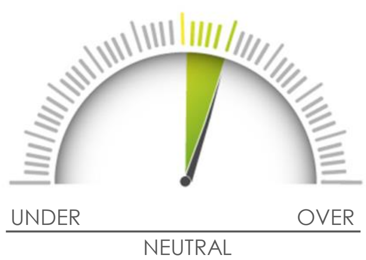
Developed Markets



We increased our recommendation on Developed Market Equities back to **Neutral**. The correction that began in mid-April was significant enough to resolve the overbought condition. Moreover, Powell's more dovish stance, the weaker-than-expected payroll numbers, and a strong earnings season suggest that the downside at these levels is limited. However, the competition from still high nominal and real interest rates may continue to limit the upside potential of the main stock indices.

US	=	**Europe**	=	**Japan**	=

Emerging Markets

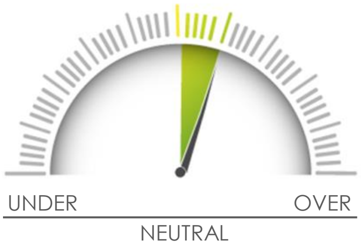


Similarly, we upgraded our recommendation on Emerging Markets Equities to **Slightly Overweight**. The reasons for the upgrade are the same as those previously mentioned for Developed Countries. As for China, following the major rally from the January lows, a physiological correction is possible. If this occurs, it should be viewed as a buying opportunity. Market valuations still remain at a steep discount compared to developed countries, and investors may continue to rotate their portfolios towards markets and sectors with the lowest valuations, as has been the trend since the beginning of the year.

Asia ex-Japan	=	**EEMEA**	−	**LATAM**	=

Fixed Income

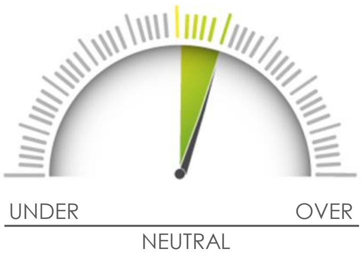
Developed Markets Sovereign



We confirmed our **Slightly Overweight** recommendation for Developed Markets Sovereign Bonds. As discussed in the prologue, Powell's conference was primarily focused on mitigating tail risks on interest rates. Therefore, it is reasonable to anticipate that rates will stabilize around current levels. The committee continues to prefer the short and medium segments of the yield curves. Conversely, we remain cautious about the long end, considering the possibility that the ongoing bull steepening could extend further.

EU Core	=	EU Periphery	=	US Treasury	=	Japanese JGB	=

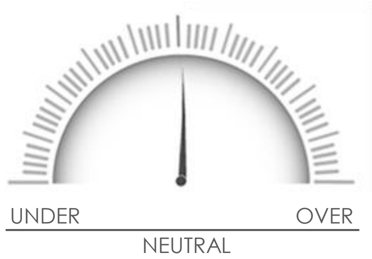
Developed Markets Corporate



We kept our **Slightly Overweight** recommendation on Developed Markets Corporates. We maintain our preference for investment-grade corporate bonds due to the persistently narrow spreads. Given the current low volatility environment, the carry trade strategy remains paramount.

IG Europe	+	IG US	+	HY Europe	−	HY US	−

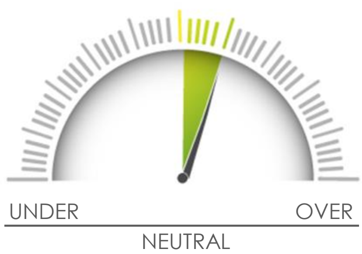
Emerging Markets



We also maintained our **Neutral** recommendation for Emerging Market bonds. The strength of the dollar coupled with rising interest rates in Western countries, and escalating geopolitical tensions, is worsening the outlook for emerging markets debt. Consequently, we offer a relatively more cautious recommendation compared to other bond strategies.

Local Currency	=	Hard Currency IG	−	Hard Currency HY	−

Commodities



We confirmed our **Slightly Overweight** recommendation on Commodities. Precious metals remain our preferred commodities, serving as a portfolio hedge amid unexpected geopolitical tensions and sustained inflationary pressures. Additionally, precious metals are gaining from substantial purchases by central banks, especially the Bank of China. While still positive, our outlook on other commodities is more cautious. Energy commodities could see a boost from increased demand for electricity necessary for artificial intelligence, and industrial commodities may benefit from rising demand in China.

Precious	+	Energy	+	Industrial	+	Agricultural	=

Currencies

The Committee kept the **Neutral** stance on the US Dollar. After weakening slightly in the past few days due to Powell's more dovish than expected press conference, the dollar is now considered fairly priced.

The view on the Euro is **Neutral** as well. The fact that the ECB is expected to cut rates before the Fed is counterbalanced by the slightly better-than-expected macroeconomic data coming out in Europe, particularly confidence data.

The view on the **Chinese Renminbi** is downgraded to **Negative**. For several weeks, the Renminbi has been trading near the upper boundary of the permitted fluctuation band with respect to the central bank's fixing. In the past, when such a situation persisted for a while, it was followed by a devaluation of the Chinese currency. Another reason that could lead China to let the renminbi weaken is the depreciation of the yen, which reduces China's competitiveness.

The outlook for other **emerging market currencies** is **Neutral**. Among emerging currencies, the committee is now preferring the Turkish Lira.

Euro	=	**USD**	=	**CNY**	=	**Other EM**	=