Main Events

Azimut Global Network

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

BoE — 04.08
Will the Bank of England meeting be interpreted as dovish, as the ECB and Fed were?

US PAYROLLS — 05.08
The market would welcome signs of moderation in the US labor market as a sign of easing inflationary pressures

US CPI — 10.08
After the sharp drop in commodities, market expects a significant slowdown in inflation

EU TRADE BALANCE — 16.08
Will the EU's trade balance continue to worsen due to rising energy bills?

ONCE UPON A TIME…

- **The market reacted to the latest Fed and ECB meetings as if the central banks will soon make a dovish pivot**
- **U.S. GDP has already contracted for two consecutive quarters, meeting the definition of "technical recession," and confidence indexes warn that further slowdowns is possible**
- **Should central banks confirm a change in their stance and that the current slowdown can be managed without triggering a recession, then markets may have reached a long-term bottom. Otherwise, the recent rebound will prove to be just another bear market rally**

The long-awaited rebound has finally arrived, driven by central banks or, more likely, by the market's interpretation of what Lagarde and Powell said during the press conference following the central bank meetings.

Let's start with the ECB.

Although Lagarde stated verbally that the ECB's priority is to ensure the decline in inflation, a message that should suggest a more restrictive monetary policy given that inflation is still rising and the ongoing energy crisis in Europe is a harbinger of further increases, the market reacted with a choral downward movement in European rates, affecting both the short and long ends of the curves, the core and peripheral countries. And this despite the fact that European inflation hit a new high in July.

What the market has focused on are the risks of economic slowdown and the fact that the new instrument (TPI, Transmission Protection Mechanism) announced by the ECB to prevent unwanted movements on European government bonds has no size limits.

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If indeed an economic slowdown occurs, it will be more difficult for the ECB to raise rates, and in any case the slowdown itself will lead to a comeback in inflation, so the ECB will need to be as tough as previously announced. As a result, the market now assumes that official rates in Europe will not even reach 1%.

Instead, the reduction of rates across Europe is probably more related to the fact that the market has interpreted the unlimited size of the TPI as if the ECB is willing to implement a yield curve control policy like the Bank of Japan has done in the past months. And since the BoJ has been able to avoid an increase in market rates, there is no reason for rates to rise in Europe as well.

However this seems like a nonsense since, as Lagarde said, the TPI is an instrument that should ensure the transmission of the ECB monetary policy. Currently, the ECB's stated monetary policy is restrictive to ensure a drop of inflation. Unlimited bond purchases are nothing more than an unrestricted QE (thus more powerful than the one just ended, which was limited in size), i.e.: a tool used to loosen the monetary policy (with inflationary consequences). The use of the TPI is conceivable only if, and only after, interest rates in all (or part) of Europe have risen to undesirably high levels. It is utterly unrealistic to imagine using it to cap rates in the current inflationary environment. Despite this, rates in Europe (in both at the short and the long end of the curves) in the past month have retraced roughly half of the increases since the beginning of the year.

The most surprising remark, however, came from Powell during the last press conference following the Fed meeting. The chairman said that with its rate hike to 2.25%-2.5%, the Fed's "monetary policy is now in neutral territory", a level that is no longer accommodative, neither stimulating nor slowing the economy or inflation. Such a statement has been interpreted as the U.S. central bank believing that the current rate hike cycle is nearing an end, or at least that the Fed will slow the pace of the current monetary tightening. In addition to this, Powell reiterated several times that the economy may slow down in the coming months, favoring a decline in inflation, but he also insisted on his belief that the Fed will likely be able to prevent the economy from sliding into recession.

In the days that followed, several economists, including El Erian and Larry Summers, as well as major newspapers like the Wall Street Journal, strongly criticized these statements, particularly the one about the neutral level of interest rates. Quoting the latter, "not to be unkind, but when the fed funds rate was 2%-2.25% in October 2018, Mr. Powell said "we're a long way from neutral" on interest rates. The inflation rate at the time was a mere 2.5%. Times and circumstances change, but the meaning of "neutral" can't possibly have changed that much". Larry Summers made similar comments, stating that the neutral level of rates depends also on the level of inflation, and “If you think it [2.25% -2.50%] is neutral, you are misjudging the posture of policy in a fundamental way". He also added that “it's the same kind of, to be blunt, wishful thinking that got us into the problems we have now, with the use of the term 'transitory'".

Finally, U.S. GDP data released last week showed the first back-to-back quarterly contraction, falling 0.9% annualized. Normally a recession is defined as two consecutive quarters of GDP contraction. However, President Biden and Treasury Secretary Yellen were keen to state it was only a "technical recession".

A "technical recession" is defined as a situation in which GDP contracts for two consecutive quarters due to mere statistical causes but without a generalized decrease in economic activity. Considering that consumption and employment (two of the main metrics that normally contract during a recession) are still strong, there is a chance that we are indeed not in a recession. The final word rests with the National Bureau of Economic Research, but they usually take quite a long time before pronouncing on the matter in order to properly weigh all the indicators. In the meantime, the Biden administration's position prevails that the current slowdown should be dismissed as a technical recession. Tough, the decline in business confidence, as measured by the S&P Global PMI indices, which are approaching or exceeding the 50 level, threshold between expansion and recession, as well as the plunge in consumer confidence to the lowest level on records don't bode well for the future.

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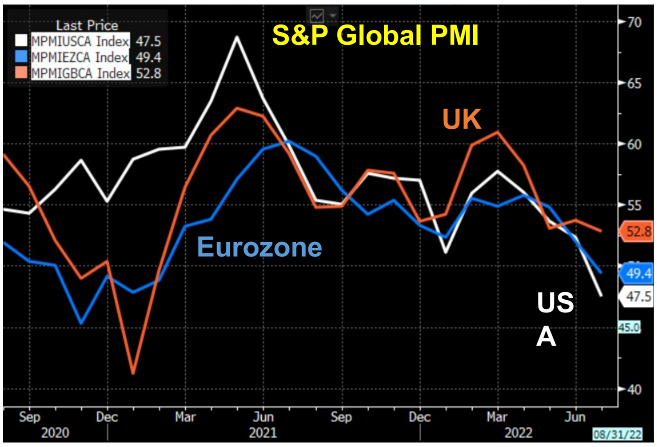
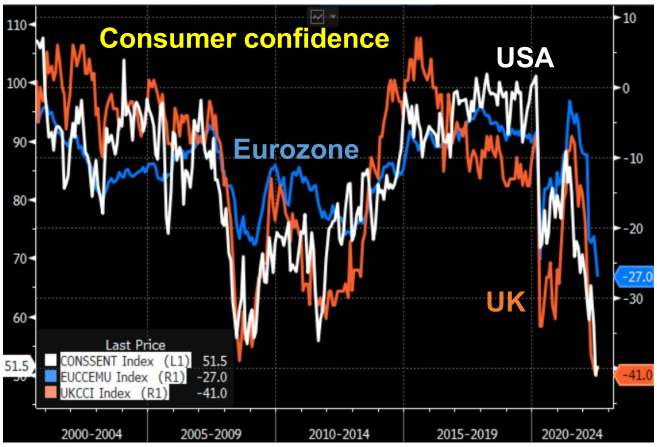


Source: Bloomberg



Source: Bloomberg

In recent days, the market has been willing to believe that central banks have changed their stance becoming less hawkish and closer to the end of their interest rate hike cycle (or even ready to inject liquidity through unlimited bond purchases), that inflation is about to subside thanks to an economic slowdown that will not result in a recession, and that the two quarters of negative growth in the US is a mere technical recession.

If proven correct, there is a possibility that the stock markets have made a medium/long-term bottom in June. If not, then the recent rebound will turn out to be another bear market rally similar to the one that occurred from mid-March to early April, and it should be exploited to reduce equity exposures for those who have been caught overexposed to the stock market.

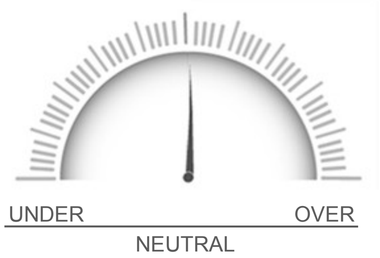
Asset Allocation View

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

− UNDER = NEUTRAL + OVER

Equity

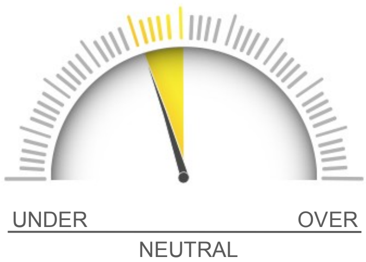
Developed Markets



We maintained our recommendation on Developed Markets Equities to **Neutral** after the upgrade made two weeks ago, on the expectation that the recent rebound may extend. Nevertheless, there is a possibility that this may just a bear market rally as discussed in the prologue, and therefore we advise those who were overexposed to equities to take advantage of the pullback to trim exposure on further strength. In the medium term, we remain cautious because of a possible economic slowdown and the risk that the dovish central bank pivots expected by the market may not materialize.

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

Emerging Markets

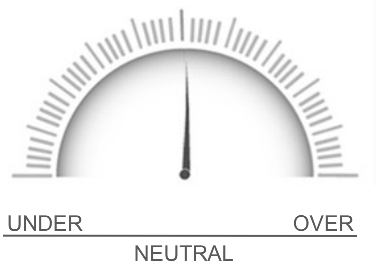


We maintained our **Slightly Underweight** recommendation on Emerging Markets Equities. Emerging markets continued to underperform developed markets, mainly due to weakness in Chinese equities that were weighed down by the ongoing real estate crisis and renewed signs of a slowdown. Emerging markets ex-China have performed significantly better, but failed to outperform developed markets, despite the significant discount in valuations that make them attractive on an absolute and relative basis.

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

Fixed Income

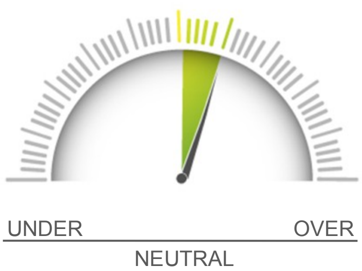
Developed Markets Sovereign



We maintained our recommendation on Developed Markets Sovereign Bonds as **Neutral**. The continued decline in interest rates has pushed the entire yield curve back to unappealing levels, from the short end to the long end. Given the risk of an economic slowdown, an outright short position is not advised, but the possibility that central banks' ostensibly dovish turn will not materialize suggests that long positions are also not advised. The curves' very short segments (up to 6 months of maturity) can be used as a safe haven.

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

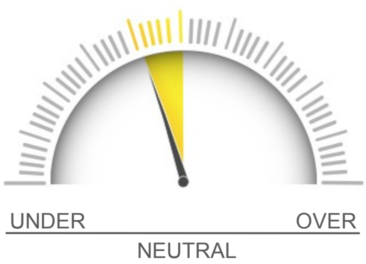
Developed Markets Corporate



We maintained our recommendation on Developed Markets Corporates as **Slightly Overweight.** Among corporate bonds, investment grade and particularly European hybrid bonds continue to offer the best solution, even if an economic slowdown occurs. In contrast, caution is still advised on high yields, which may still have some downside in the event of a global growth slowdown.

IG Europe	=	**IG US**	=	**HY Europe**	-	**HY US**	-

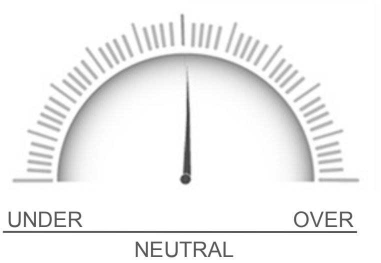
Emerging Markets



We maintained our **Slightly Underweight** recommendation on Emerging Market bonds. Despite spreads reaching high levels, it is reasonable to expect developing market bonds to remain under stress as long as Western central banks continue to raise rates, as well as in the event of a global economic slowdown.

Local Currency	=	**Hard Currency IG**	-	**Hard Currency HY**	-

Commodities



We maintained our **Neutral view** on Commodities. With no ability to generate cash flow, precious metals are facing increasing competition from US government bonds. Energy and industrial metals may suffer if the recent slowdown continues or worsens, while agricultural commodities may face a temporary correction as Ukrainian exports resume.

Precious	=	**Energy**	=	**Industrial**	=	**Agricultural**	=

Currencies

The Committee confirmed its **Neutral View on the US dollar**. After the strong appreciation of recent weeks, the Dollar modestly retraced but there is room for a further weakening. Nevertheless, in the medium term it is still believed that the dollar has further room for appreciation considering that the Federal Reserve is proving to be the most aggressive central bank in tightening monetary policy, and that in case of global economic slowdown or increased risk aversion the Dollar tends to appreciate.

The view on the **Euro is Neutral**. On the one hand energy supply difficulties and the uncertainties surrounding the snap elections in Italy continue to weigh on the currency, on the other hand the strong GDP data could support the common currency.

The view on the **Chinese Renminbi** is confirmed to **Neutral, but with a bearish bias**. The unpredictability of government decisions, the never-ending slump in the real estate sector, and China's dubious stance regarding the conflict in Ukraine are weighing on investors' willingness to invest in Mainland China.

Similarly, on **other emerging market currencies** we maintain a **Neutral** stance, **but with a bearish bias** in view of the heavy correction in commodities and the possibility of an economic slowdown.

Euro	=	USD	=	CNY	=	Other EM	=