AZIMUT
DEFINING INVESTMENT DIRECTION

AZIMUT GLOBAL VIEW

28.
04.
23

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

FOMC
The Federal Reserve may announce the last hike of the tightening cycle that began just over a year ago

ECB MEETING
European inflation data to be released May 2 could be the determining factor in the ECB's decision to raise 25 or 50 bps

US GDP
For the first time since 2020, the U.S. economy may have created fewer than 200k new jobs

US CPI
U.S. headline inflation is expected to remain unchanged, but core inflation may fall by 0.2% to 5.4%

COMING TO A STANDSTILL

- **At its next meeting, the Federal Reserve may finally announce the end of the tightening cycle after a last increase of 25 bps**
- **The best scenario for financial markets would be for the Fed to reiterate that it does not intend to cut rates in the near future**
- **However, there is still a risk that the Fed will not rule out further rate hikes**
- **The ECB is expected to raise rates by 25 basis points, but in Europe, it is still too early to think that the tightening cycle is already nearing an end**

The coming week is marked by the Fed and ECB meetings. What these two central banks say may could determine the direction of markets in the coming months.

The Federal Reserve will meet on May 3, and for the first time in more than a year, market expectations could prove correct: Wednesday's hike may be the last in what has been the steepest and quickest hiking cycle in more than 40 years.

If the Fed raises rates by 25 basis points one more time, interest rates will peak around 50 basis points lower than projected before the banking crisis. As Powell and other Federal Reserve officials have repeatedly stated, the continuous credit contraction caused by the recent bankruptcies will have the same impact as monetary tightening, allowing the Fed to halt earlier.

In addition, the condition that has always caused the Federal Reserve to pause during previous rounds of monetary tightening occurred this month, namely when headline inflation, falling, reached the level of official rates. In the most recent survey, inflation fell to 5 percent, the same level as Fed Fund Rates.

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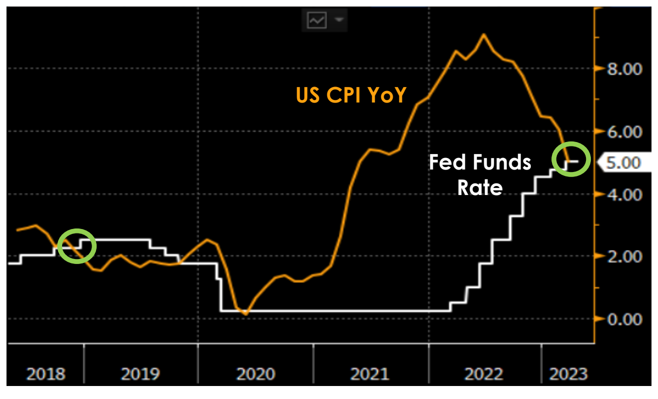

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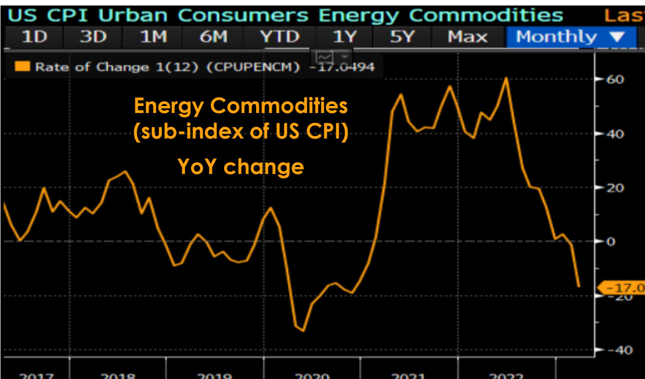


Source: Bloomberg

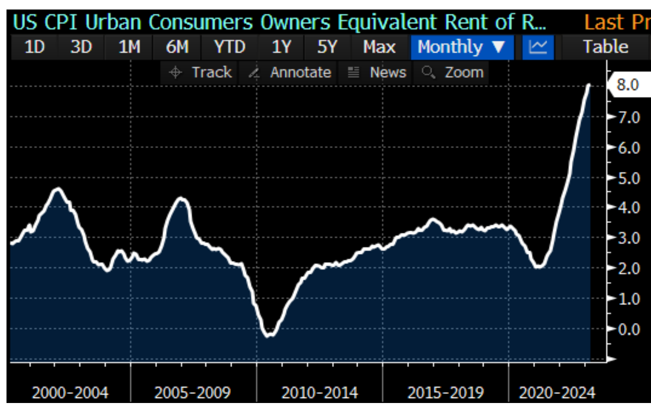
In the ideal scenario for financial markets, the Federal Reserve should say that it is standing still and waiting to see the effects of the rate hikes made so far on the economy, without conveying any message of possible cuts in the months to come. This would be a reassuring message to markets, as it is equally well known that the Federal Reserve cuts rates when there is a concrete risk of recession on the horizon, or some systemic problem. Refraining from hinting at any cuts would therefore be the best scenario.

If the Fed instead leaves the door open for more rate hikes, the market may become jittery. This possibility cannot be fully ruled out at the moment, given that headline inflation has declined relatively rapidly, but this is mostly owing to the deflationary impact of the CPI's energy component.

If we look at the energy sub-index, the year-on-year change is currently at -17%. This is due to the fact that compared to a year ago, commodities have dropped significantly from the peaks immediately following Russia's invasion of Ukraine. This disinflationary push could accelerate further in the next three months as the energy sub-index peaked in June 2022.

Just as it was predicted a year ago that inflation would fall significantly in 2023 due to the base effect (energy prices would fall after the spike in the first half of 2022), the same logic should now apply in reverse: in the second half of 2023, the volatile energy component will stop contributing to keeping inflation down, and the more stable, "core" components will drive the CPI.

The core components of inflation continue to show much stronger year-over-year increases than those indicated by overall inflation. Housing prices, as measured by owner-equivalent rents, are up 8 percent and continue to rise, showing no signs of moderation. In contrast, wages, another component closely monitored by the Fed, appear to have already begun a stabilization phase, but at +6.4 percent they remain much below the 2 percent target. The Fed is fully aware of these dynamics, which is why there is still a small risk that further hikes cannot be categorically ruled out.



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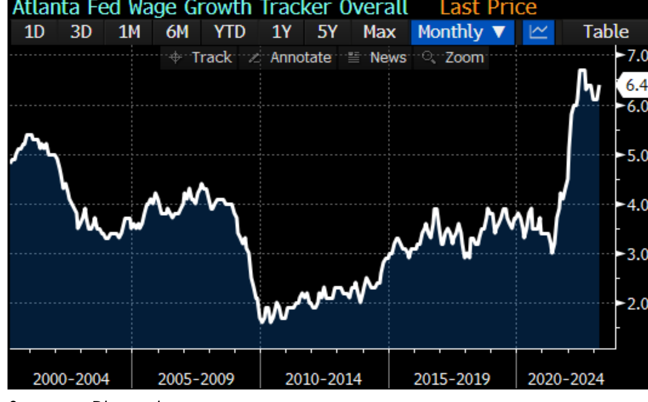

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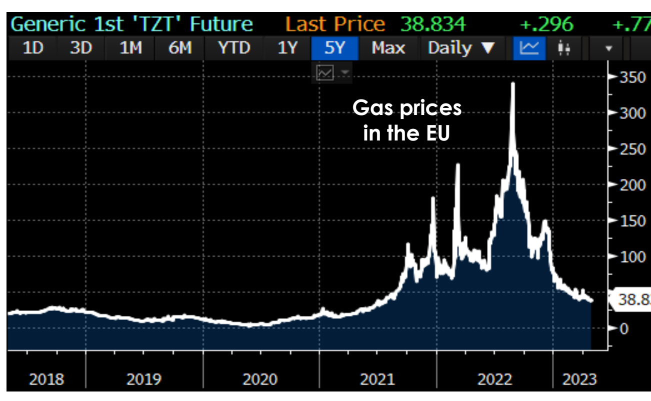

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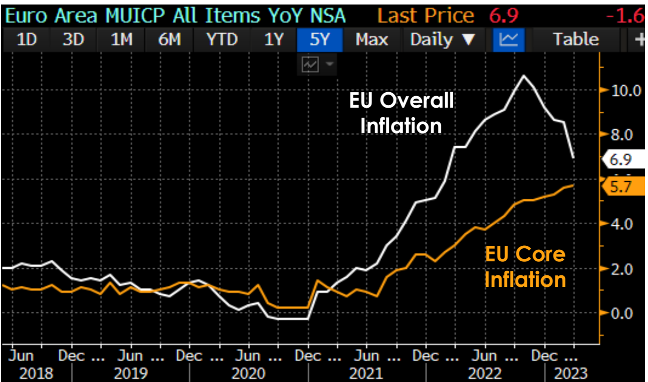


Source: Bloomberg

In Europe, there is more uncertainty about the decisions that will be implemented, partly because of the greater divisions within the ECB. Governors from northern countries have always been stricter and are pushing for hikes of 50 basis points, while those from Mediterranean countries are more cautious and would like to slow the pace of hikes given the greater macroeconomic uncertainties, not least the ongoing banking crisis.

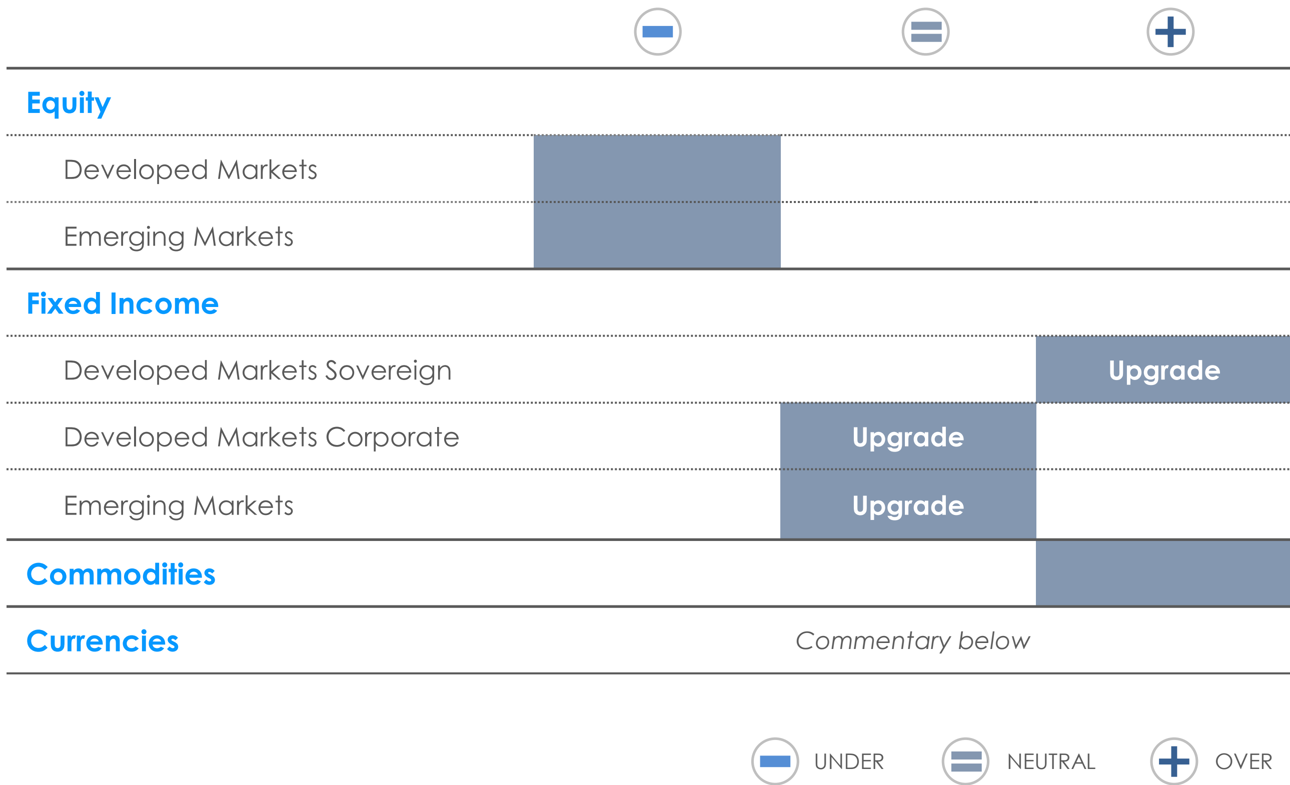
A compromise that could be achieved at the next meeting is a 25 basis point raise (in line with market expectations), connected to a commitment to continue rising as long as required to keep inflation under control while taking time to monitor the macroeconomic situation's evolution.

Crucial to the decision will be the European inflation data for April, which will be released shortly before the ECB meeting. At the time of writing, only those from a few European countries are available. In France, prices rose by 0.2 percent more than expected, and in Germany by 0.2 percent less.

The difference between headline and core inflation will also make monetary policy decisions more complex in Europe. The impact of energy prices has been significantly greater in Europe due to the spike in gas prices in the summer of last year. Between then and now, gas prices in Europe have fallen by nearly 90 percent, and this dynamic explains why overall inflation is falling so rapidly. Nonetheless, core inflation is on a clearly upward trajectory, as so-called second-round effects are now materializing.

However, it is hard to imagine that the ECB might stop raising rates in the summer, should core inflation continue to be way too high relative to interest rates. Therefore, unless inflation surprises to the downside in the coming months, it still seems too early to hope that the ECB's cycle of hikes will end shortly after the Fed's.

Asset Allocation View

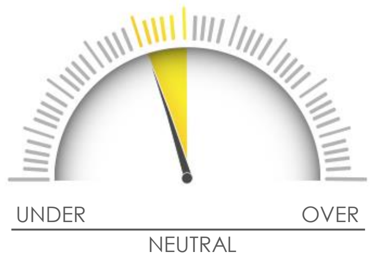


	Under (−)	Neutral (=)	Over (+)
Equity			
Developed Markets	■		
Emerging Markets	■		
Fixed Income			
Developed Markets Sovereign			Upgrade
Developed Markets Corporate		Upgrade	
Emerging Markets		Upgrade	
Commodities			■
Currencies		*Commentary below*	

UNDER NEUTRAL OVER

Equity

Developed Markets



We maintained our **Slightly Underweight** recommendation on Developed Markets Equities. Equity market values remain high, with stock indices trading at the upper end of their forecast trading range for the year. Nonetheless, if the Fed effectively announces the end of the rate hike cycle (without hinting at a cut, which would imply trouble ahead), and given that the reporting season has been fairly strong thus far, the market may have room for another leg up.

US	Neutral	**Europe**	Neutral	**Japan**	Neutral

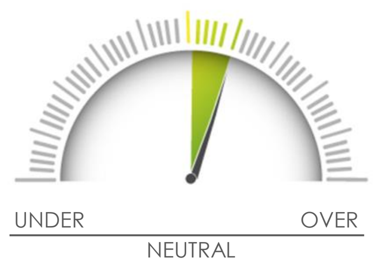
Emerging Markets

We kept our recommendation on Emerging Markets Equities unchanged at **Slightly Underweight**. On the one hand, emerging countries continue to trade at far lower multiples than developed countries, and could benefit from the potential ending of the rate hike cycle by the Fed. On the other hand, the persistent negative news-flow against China and the fear of a global economic slowdown in the months ahead suggest that a cautious stance is still necessary.

Asia ex-Japan	Over	**EEMEA**	Under	**LATAM**	Neutral

Fixed Income

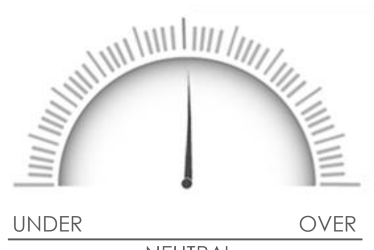
Developed Markets Sovereign



We increased our recommendation on Developed Markets Sovereign Bonds to **Slightly Overweight**. If the Federal Reserve confirms that there will be no future rate hikes, Treasury bonds can be purchased without fear of further downside. Government bonds in the rest of the world should benefit accordingly, on the expectation that once the Fed is done other central banks will also follow suit by stopping raising. Moreover, at the first meeting under the new governor, the BoJ signaled no imminent changes to its monetary policy, so for the time being is off the table the risk of a tightening shift by the BoJ.

EU Core	EU Periphery	US Treasury	Japanese JGB

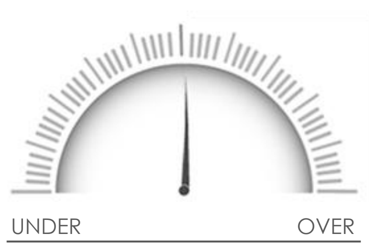
Developed Markets Corporate



We have upgraded our recommendation on Developed Markets Corporates to **Neutral**. The fact that the Federal Reserve may announce the end of the restrictive cycle largely eliminates duration risk. Because duration is an important driver of performance in corporate bonds, particularly investment grade bonds, the recommendation has been raised for corporate bonds as well. We continue to advise against investing in high-yielding securities with tight spreads.

IG Europe	IG US	HY Europe	HY US

Emerging Markets



We increased our recommendation on Emerging Market bonds to **Neutral**. Over the past few weeks, spreads on emerging market bonds have widened significantly. In addition, the asset class tends to outperform when the Federal Reserve stops raising interest rates.

Local Currency	Hard Currency IG	Hard Currency HY

Commodities

We maintained our **Slightly Overweight** recommendation on Commodities. In addition to being a safe haven asset, considering ongoing geopolitical tensions, the banking crisis and the debt ceiling issue, precious metals tend to perform well when the Federal Reserve ends the rate hike cycle.

Precious	Energy	Industrial	Agricultural

Currencies

The Committee confirmed its **Neutral** view on the US Dollar pending the two Central Bank -Federal Reserve and ECB- meetings. The market expectation is that the Fed will implement one last hike, and if this is confirmed, the dollar could remain around current levels or weaken marginally. If, on the other hand, the Fed leaves the door open for a further hike in the months ahead, the dollar could strengthen.

The view on the Euro is also **Neutral**. The ECB is expected to raise rates, but it is not certain whether by 50 bps or only 25 bps. Diverging views among the ECB members may result in a 25 basis point boost. Following the recent rally, it is possible that the euro will not have enough traction to continue the current uptrend in the absence of a hawkish surprise.

The view on the **Chinese Renminbi** is **Neutral** considering that on the one hand geopolitical tensions between China and the rest of the world remain, but on the other hand the attractive valuations of Chinese assets could still attract capital from abroad.

On most of **other emerging market currencies** the view is **Neutral**, but we are more constructive on Latin American currencies.

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