azimut

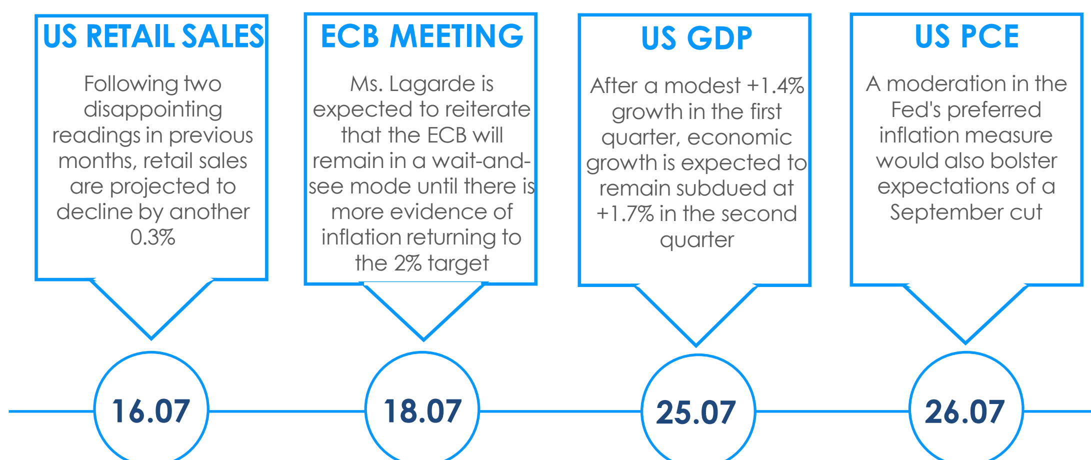
AZIMUT GLOBAL VIEW

15. 07. 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



TOWARDS A SEPTEMBER CUT

- **The latest macroeconomic data confirmed that the US labor market is softening, albeit it still remains quite robust**
- **U.S. inflation data came in below expectation for the second month in a row, bolstering hopes that rates might be cut already in September**
- **Should this scenario materialize, the short ends and the belly of the curves are the segments to be preferred, while caution is still needed on the long ends**

In previous reports, we have argued extensively about how U.S. employment data were showing signs of cooling. The data released last week further confirmed that the labor market might indeed be losing some of its momentum.

June's non-farm payrolls figure shows that 206,000 new jobs were created in the month. However, it's important to note that the data for the previous two months were revised downwards by a significant 111,000 jobs. In addition, job creation in the private sector was only 136,000, which fell short of the expected 160,000. The total number of unemployed workers inched up by 162,000, bringing the unemployment rate to 4.1%, the highest level since November 2021. The Household survey claims that only 116,000 jobs were created in June, indicating a weaker labor market than what the non-farm payrolls data portrays.

On a more positive note, the number of job openings rose to 8.14 million from 7.92 million the previous month, and both initial and continuing jobless claims stabilized.

Among other noteworthy macroeconomic data, it is important to mention the sharp decline in the ISM services PMI. While this figure should be taken with a pinch of salt — since post-pandemic confidence indicators have often been unreliable in predicting business cycle developments and the ISM services PMI index itself has shown significant volatility recently — it still warrants attention.

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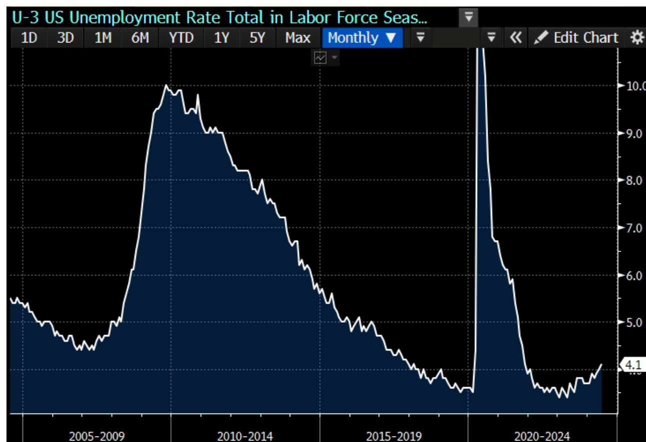


Source: Bloomberg

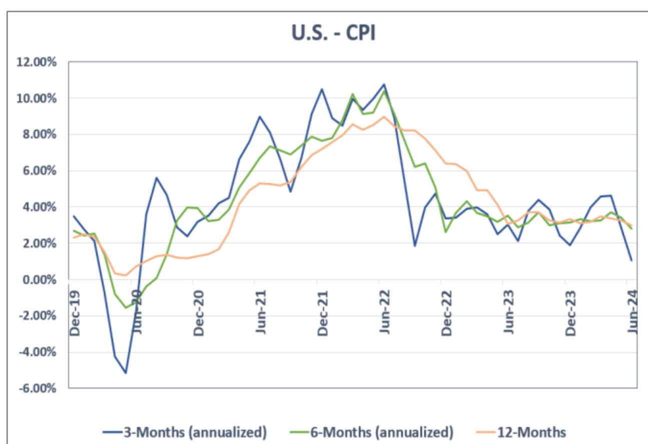
Source: Bloomberg

This is because the services sector has been the primary driver of economic expansion in recent years. Moreover, the level reached (48.8) is the lowest since May 2020, and the 6- and 12-month averages show a clear downward trend. The sub-indices on employment and new orders, which are more closely linked with future growth, stand at 46.1 and 47.3, respectively.

However, the most relevant figure for monetary policy implications was inflation. For the first time since the pandemic, the CPI recorded a monthly decline, falling 0.1% against expectations for a 0.1% increase, bringing the annual figure down from 3.3% to 3.0%. The core index was also lower than expected, rising 0.1% on the month, while the annual figure fell from 3.4% to 3.3%.

More than the absolute value, what matters most is the trend. Data released in the first part of the year had fueled concerns about a renewed pickup in inflation, with all readings above expectations. In recent months, the trend first stabilized and then reversed. CPI numbers were in line in May and below expectations in the last two months. The 3- and 6-month annualized rate of inflation has started to decline again toward the levels expected by the Federal Reserve for both the headline and core CPI.

Shelter costs, which account for more than a third of the core CPI, were a notable factor in the slowdown in inflation. They rose by just 0.2% on the month, the smallest increase since 2001. Shelter costs are still up 5.2% year-on-year but are expected to fall significantly over the coming months, looking at real-time data (shelter inflation usually lags real-time data by several months), contributing to keeping inflation in check. The "core services less housing" (or "supercore") inflation, which strips out housing costs, fell slightly for the second month in a row. The annual reading retreated to 4.7%, the lowest since February.



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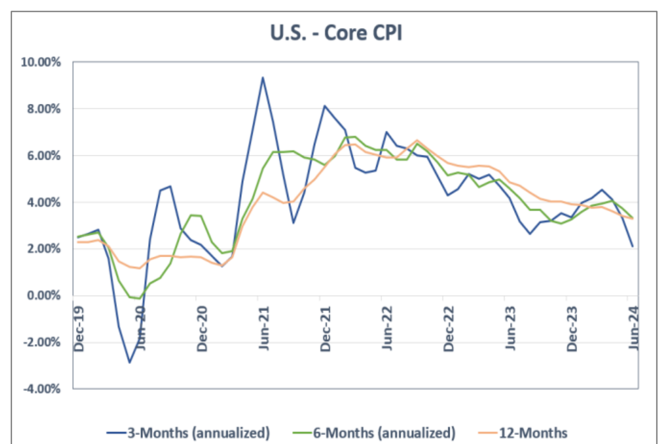

Source: Bloomberg

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The macroeconomic macroeconomic picture that is emerging is therefore the ideal one for the Federal Reserve to begin cutting rates, considering its dual mandate of pursuing the economic goals of maximum employment and price stability.

On the one hand, the labor market is still healthy, although softening; keeping monetary policy tight for too long would risk causing a more pronounced economic slowdown, with negative consequences for employment. On the other hand, recent inflation data are encouraging enough to give the Fed the confidence it needs that inflation is coming back under control.

Barring an unexpected and unlikely re-acceleration of inflation in the coming months, the most likely scenario, therefore, is one in which the Federal Reserve takes note of the positive developments on inflation and the ongoing economic slowdown at its meeting in late July, but without implementing any changes in monetary policy. Then, at the annual gathering of central bankers in Jackson Hole in late August, Powell may anticipate the possibility of an imminent rate cut, which will then be implemented a few weeks later at the September FOMC meeting.

Should this actually materialize, the other major Western central banks will follow suit, as is customary, regardless of their domestic macroeconomic data. All the more so this time, considering that the economic slowdown in other countries is more pronounced than in the United States.

In this scenario, therefore, we can expect the short ends and the belly of the curves (up to 7 years) to benefit the most, as they are the most sensitive to monetary policies. However, we remain cautious about the long ends of the curves due to ongoing concerns about potential slippage in public finances, which could further undermine the sustainability of public debts.

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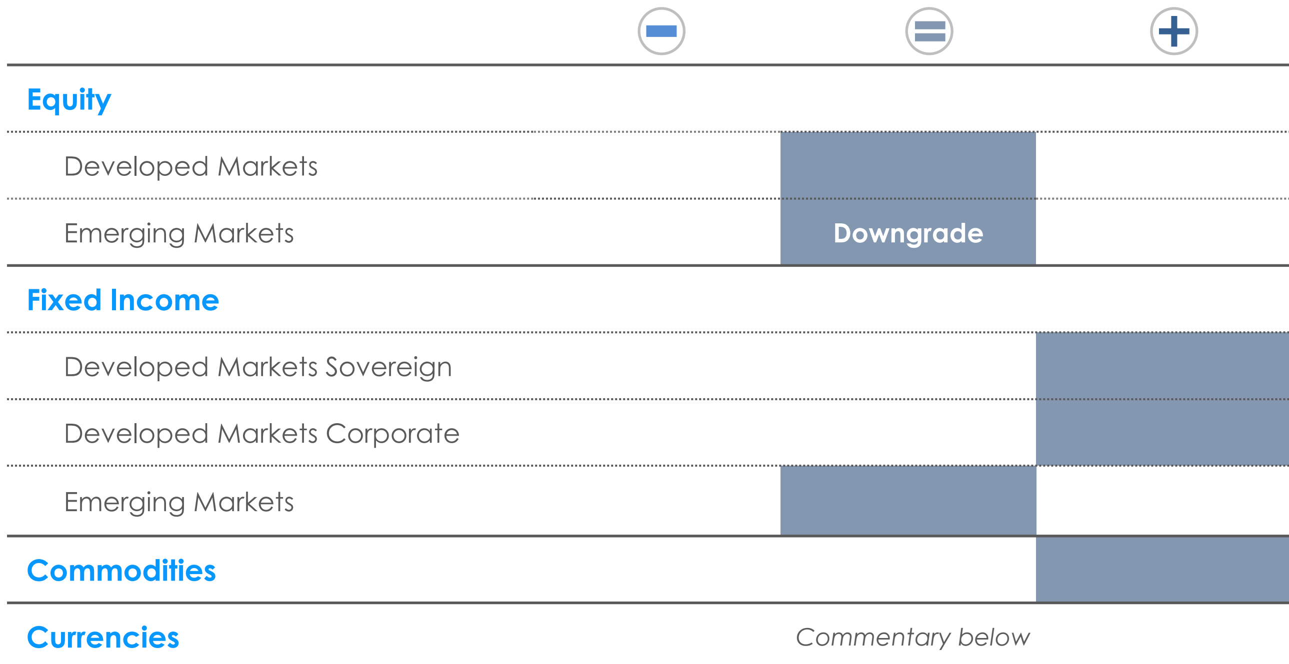
Asset Allocation View

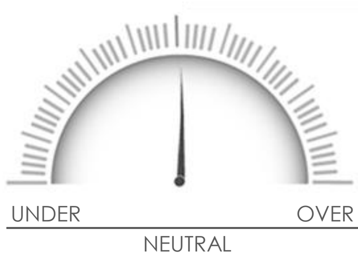


	−	=	+
Equity			
Developed Markets		■	
Emerging Markets		Downgrade	
Fixed Income			
Developed Markets Sovereign			■
Developed Markets Corporate			■
Emerging Markets		■	
Commodities			■
Currencies		*Commentary below*	

− UNDER = NEUTRAL + OVER

Equity

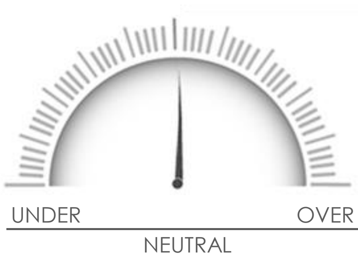
Developed Markets



We maintained our recommendation on Developed Market Equities as **Neutral**. Markets continue to be buoyed by positive momentum, despite a growing number of macroeconomic data signaling a possible slowdown on a global scale. If the slowdown becomes more pronounced and/or companies provide more conservative guidance for the coming quarter, increased caution will be necessary.

US	Europe	Japan
=	=	=

Emerging Markets



We lowered our recommendation on Emerging Markets Equities to **Neutral**. Although valuations remain favorable and at a significant discount to developed markets, the risk of a global slowdown may cause investors to adopt a more cautious attitude toward emerging markets. Additionally, the Chinese government's unwillingness to approve concrete fiscal stimulus continues to dampen the positive momentum of previous months.

Asia ex-Japan	EEMEA	LATAM
=	−	=

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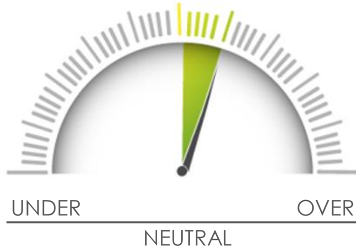
Fixed Income

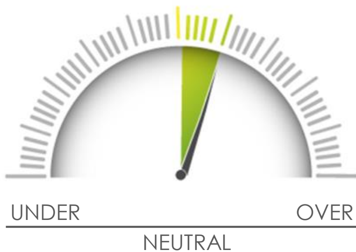
Developed Markets Sovereign



We have maintained our **Slightly Overweight** recommendation for Developed Markets Sovereign Bonds. Growing signs of a slowdown, coupled with moderating inflation, should allow the Fed to begin cutting rates in September. As usual, other major Western central banks are expected to follow suit. Therefore, the committee is increasingly positive on the short-end and the belly of the curves (up to 7 years), which are more sensitive to monetary policy decisions. More caution remains on the long ends of the curves, which may stay under pressure due to concerns about further loosening of fiscal discipline.

EU Core		EU Periphery		US Treasury		Japanese JGB	

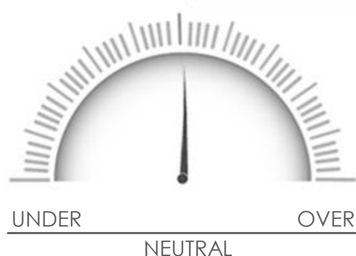
Developed Markets Corporate



We maintained our **Slightly Overweight** recommendation on Developed Markets Corporates. We maintain our preference for investment grade corporate bonds due to their persistently narrow spreads.

IG Europe		IG US		HY Europe		HY US	

Emerging Markets



We also maintained our **Neutral** recommendation for Emerging Market bonds.

Local Currency		Hard Currency IG		Hard Currency HY	

Commodities

We confirmed our **Slightly Overweight** recommendation on Commodities. Within commodities, we are growing increasingly 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. In contrast, we are more cautious on cyclical commodities, which could come under pressure if economic growth slows further.

Precious		Energy		Industrial		Agricultural	

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Currencies

The Committee kept the **Neutral** stance on the US Dollar. We continue to believe that the greenback is fairly valued, considering the weaker-than-expected data from the United States and the rate differential with other countries

The view on the Euro is **Neutral** as well.

The view on the **Chinese Renminbi** is confirmed to **Negative**. China is gradually letting the Renminbi weaken, although market rates continue to remain close to the upper limit of the allowed fluctuation band against the central bank's fixing. This means there is still ample selling pressure and downside risk for the currency.

The outlook for other **emerging market currencies** is **Neutral**, with a **bearish bias**. Among emerging currencies, the Committee still favors the Turkish Lira.

Euro	=	USD	=	CNY	=	Other EM	=

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