
C.I.A. NETWORK

Asset Strategy in Brief

September 2024



BNP PARIBAS
WEALTH MANAGEMENT

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Macro, Market Views

	Macro		<ul style="list-style-type: none"> - US economic data came out broadly better-than-expected especially on consumer sentiment. The manufacturing sector remains the weak point. Initial jobless claims suggest slower hiring, not layoffs. Corporate bond market indicators also suggest limited recession risks. - In the eurozone, consumer confidence remains on an upward trend despite the small fall last month. The main worry is the manufacturing sector. The service sector is holding up somewhat better. China and global trade could bring positive surprises.
	Rates	=	<ul style="list-style-type: none"> - We revise our 12-month target for the US 10-year yield to 4% from 4.25%. We move tactically to Neutral from Positive on US government bonds as we expect rates to move higher in the short term. We stay Neutral on German government bonds. We also like EM bonds (both in hard and local currency).
	Credit	+	<ul style="list-style-type: none"> - We keep a positive stance on US and eurozone corporate bonds of high quality ("Investment Grade"). - For higher yield (at higher risk), consider the US fallen angels strategy and Euro subordinated financial bonds.
	Equities	+	<ul style="list-style-type: none"> - The key risks are that the market starts to reprice growth fears with central banks being perceived as "behind the curve". Increasing policy uncertainty around tariffs could weigh on sentiment too. - Favour eurozone, UK, Japan. Within Asia prefer China, Singapore, South Korea, Indonesia. In Latin America, we downgrade Mexico and keep a positive stance on Brazil. - We like EU Small Caps. Positive on Health care, Industrials and Materials like Metals. We also like EU financials, tech and REITs. - We downgrade EU Travel & Leisure to Underweight and upgrade EU Telcos to Neutral. - We prefer investment themes like clean water, copper miners, electricity infrastructure, circular economy, deep value markets.
	Real Estate	=	<ul style="list-style-type: none"> - Lagged impact from higher interest rates to fade gradually. We see European real estate prices slowly stabilising, with rental yields now more attractive post reset in prices.
	Commodities	+	<ul style="list-style-type: none"> - We are now Neutral on oil as Chinese demand remains weak, US recession fears linger and the OPEC+ wants to taper its voluntary production cut from October. We expect Brent to trade in the USD 75-85 range. - Gold fundamentals remain strong, but would take some profits above the top of our expected near-term USD 2350-2550 trading range
	FX		<ul style="list-style-type: none"> - EUR/USD: We change our 3-month target to 1.10 and our 12-month target to 1.12 (value of one euro). - USD/JPY: We change our 3-month target to 145 and keep our 12-month target at 140 (value of one US dollar).

Key macro & markets forecasts

	GDP Growth %		Inflation %		Central Bank Rates %			Key market forecasts			
	2024e	2025e	2024e	2025e		Now	3M	12M		Now	12M
US	2.5	1.9	2.9	2.3	US Fed Funds Rate	5.50	5.00	4.50	US 10Y yield %	3.83	4.00
Eurozone	0.9	1.6	2.3	2.0	ECB Deposit Rate	3.75	3.25	2.75	Euro 10Y yield %	2.27	2.25
Japan	-0.4	0.7	2.7	2.6	Bank of Japan Policy Rate	0.25	0.50	1.00	UK 10Y Yield %	3.97	3.65
UK	1.0	1.3	2.6	2.2	Bank of England Base Rate	5.00	4.50	3.75	S&P 500	5604	n/a
China	5.2	4.3	-0.1	1.2	China MLF 1Y Interest Rate	2.30	1.60	1.30	Euro STOXX 50	4938	n/a
									Oil Brent USD/bbl	74	75-85
									Gold USD/oz	2479	2600

Source: BNP Paribas WM. As at 2 September 2024

Asset Allocation

Allocation changes this month:

- ❑ **Equities:** Downgrade Mexico to Neutral/ downgrade EU Travel & Leisure to Underweight/upgrade EU Telcos to Neutral.
- ❑ **Bonds:** We move tactically to Neutral from Positive on US government bonds. We remain constructive on US Treasuries strategically.
- ❑ **FX:** No major changes
- ❑ **Commodities:** We turn Neutral on Oil.

	Outlook Synthesis				
	Very underweight	Underweight	Neutral	Overweight	Very Overweight
Equities				+	
Government Bonds			=		
Corporate Credit				+	
Real Estate			=		
Alternatives				+	
Cash		-			

02

Bonds



Fixed Income at a glance

Recession concerns in the US peaked after the release of the July jobs report. While those concerns have diminished, markets keep pricing a deep rate-cutting cycle, which seems overdone to us. We expect US bond yields to increase in the short term. We thus tactically move to Neutral from Positive on US government bonds. We intend to re-enter the asset class with a better starting yield in a few months as we remain constructive on US Treasuries strategically.

We favour high quality assets (IG corporate bonds) and see value in EM bonds.

Central Banks

We add one rate cut to our sequence on the back of the deteriorating labour market in the US. We now assume two 25bp rate cuts in 2024, four in 2025 and two in 2026.

We maintain our assumption for the ECB with two 25bp cuts this year, and three next year.

Corporate Investment Grade (IG) Bonds

⊕ Carry is attractive and credit spreads could tighten further as economic growth and investors' demand persist. **We prefer short maturities in the US and up to 10 years in the eurozone.**

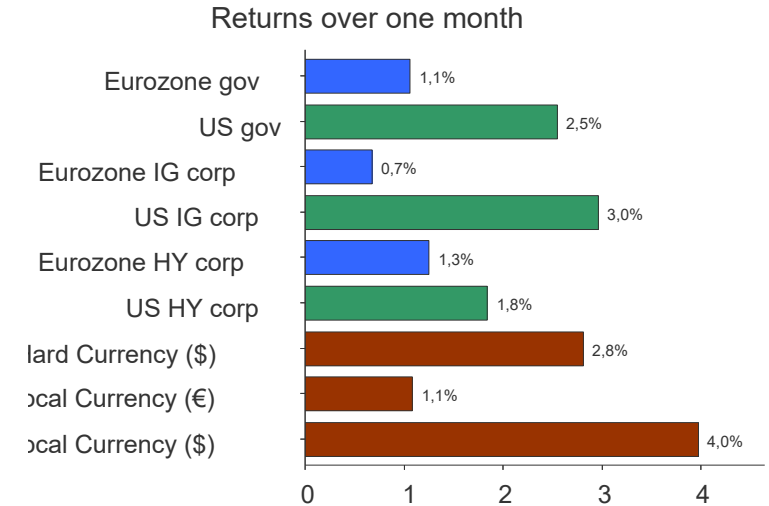
10-year yields	02/09/2024	12-month targets
US	3.83	4.00
Germany	2.28	2.25
UK	4.00	3.65

Government Bonds

⊖ We revise our 12-month target for the US 10-year yield to 4% from 4.25%. **We move tactically to Neutral from Positive on US government bonds** as we expect rates to move higher in the short term. We stay Neutral on German government bonds.

Corporate High Yield (HY) Bonds

⊖ Credit spreads have retraced very quickly after the early August sell off, and currently imply very low default rates. Spreads could widen if the Fed fails to deliver rate cuts as fast as the market expects.



Source: LSEG Datastream, Bloomberg and JPM indices, 27/08/2024

Peripheral bonds

⊖ We are Neutral on peripheral debt. The potential for further spread tightening is limited in our view. Valuations are somewhat tight. However, yields are elevated. We benefit from the carry.

Emerging Market (EM) Bonds

⊕ EM bonds have lagged the US HY rally. We see potential for rates to decline further and EM currencies should appreciate. We stay Positive on both hard and local emerging bonds.

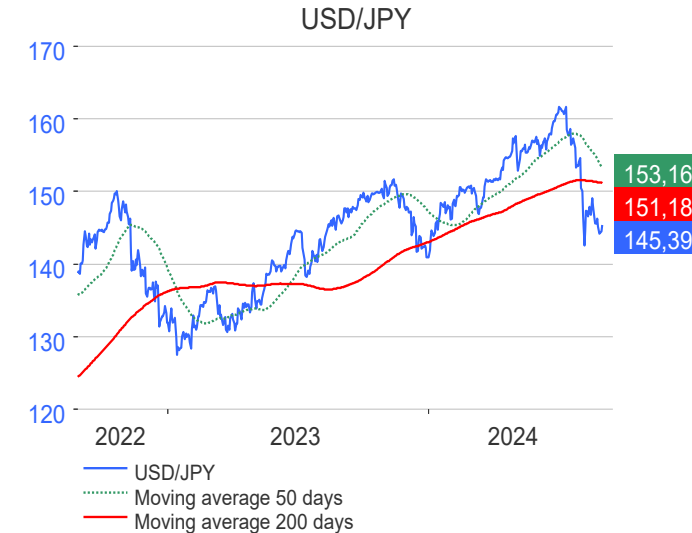
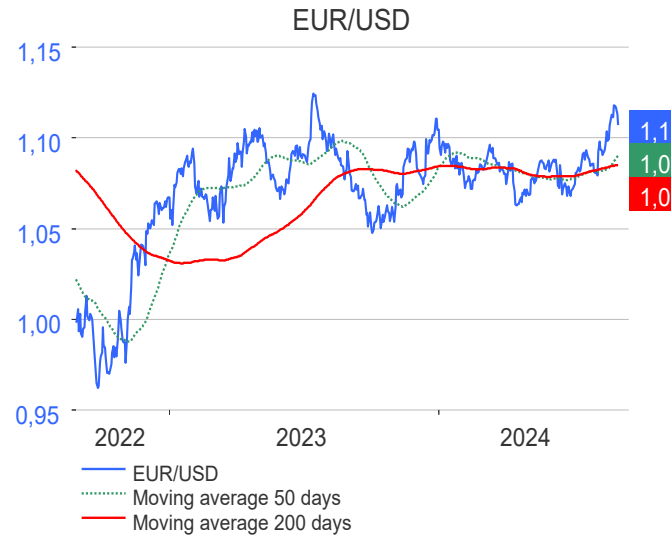
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Currencies



Currencies

- EUR/USD:** The sharp move towards bigger and faster rate cuts by the Fed have pushed the dollar lower. The move is somewhat exaggerated in the short term. **We change our 3-month target at 1.10 and our 12-month target at 1.12 (value of one euro).**
- USD/JPY:** the BoJ surprised the markets by hiking rates at the end of July. We think that the BoJ will hike rates relatively quickly until the nominal rate reaches about 1%, and slow down the hiking pace thereafter. The Yen rose sharply after the announcement (see chart). **We change our USD/JPY 3-month target to 145 and keep our 12-month target at 140 (value of one US dollar) suggesting an appreciation of the Yen.**



>> TARGET 12M EUR/USD: 1.12

Our long-term outlook suggests more rate cuts in the US over 2025-26 than the ECB. This points to a stabilisation of the USD against the euro at around 1.12 over the coming year. In the short term the dollar could rebound as the repricing has been somewhat extreme. We change our 3-month target to 1.10.

>> TARGET 12M EUR/GBP: 0.86

The BoE cut rates in August. We expect one more rate cut this year, and 4 next year. The Pound has overshoot a bit over recent months and we look for a normalisation. **We maintain our 3- and 12-month targets at 0.86.**

>> TARGET 12M USD/JPY: 140

The BoJ surprised the markets by hiking rates at the end of July. We think that the BoJ will hike rates relatively quickly until the nominal rate reaches about 1%, and slow down the hiking pace thereafter). **We change our USD/JPY 3-month target to 145 and keep our 12-month target at 140 (value of one US dollar).**

>> TARGET 12M EUR/CHF : 0.98

On 20 June, the SNB made its second rate cut with a policy rate now at 1.25%. Inflation remains below the 2% target at 1.3% in July. Looking forward the rate differential is not expected to move much. **We expect stability and maintain our EUR/CHF 3- and 12-month targets at 0.98.**

>> TARGET 12M USD/CNY: 7.2

The CNY also benefitted from the rate repricing in the US. The USD/CNY fell marginally below 7.10. We expect more stimulus to reach this year's 5% GDP growth target. The divergence in monetary policy trajectories between China and the United States should, however, limit the appreciation potential of the CNY. **We maintain our 3- and 12-month targets at 7.2.**

>> TARGET 12M USD/MXN: 18

We now expect the Mexican policy rate to reach 9.75% late 2024. The recent weakness of the MXN is linked to the post election uncertainty and the risks of lower foreign investments. That reduces the upside for the MXN. **We change our USD/MXN 3-month target to 19 and our 12-month target to 18.**

Forex at a glance

FX FORECASTS EUR

	Country		Spot 9/1/2024	Trend	Target 3 months (vs. EUR)	Trend	Target 12 months (vs. EUR)
	United States	EUR / USD	1.11	Neutral	1.10	Neutral	1.12
	United Kingdom	EUR / GBP	0.84	Neutral	0.84	Negative	0.86
	Japan	EUR / JPY	160.95	Neutral	160	Positive	157
	Switzerland	EUR / CHF	0.94	Negative	0.98	Negative	0.98
	Australia	EUR / AUD	1.63	Neutral	1.62	Neutral	1.60
	New-Zealand	EUR / NZD	1.77	Negative	1.83	Neutral	1.78
	Canada	EUR / CAD	1.49	Positive	1.45	Positive	1.46
	Sweden	EUR / SEK	11.34	Positive	11.00	Positive	11.00
	Norway	EUR / NOK	11.64	Positive	11.30	Positive	10.80
	Asia	China	EUR / CNY	7.87	Neutral	7.92	Negative
India		EUR / INR	92.85	Positive	90.20	Neutral	91.84
Latam	Brazil	EUR / BRL	6.24	Positive	5.50	Positive	5.60
	Mexico	EUR / MXN	21.99	Positive	19.80	Positive	19.60

Sources: BNP Paribas, Eikon/Datastream

FX FORECASTS USD

	Country		Spot 9/1/2024	Trend	Target 3 months (vs. USD)	Trend	Target 12 months (vs. USD)
	Eurozone	EUR / USD	1.11	Neutral	1.10	Neutral	1.12
	United Kingdom	GBP / USD	1.32	Neutral	1.31	Neutral	1.30
	Japan	USD / JPY	145.39	Neutral	145.00	Positive	140.00
	Switzerland	USD / CHF	0.85	Negative	0.89	Negative	0.88
	Australia	AUD / USD	0.68	Neutral	0.68	Positive	0.70
	New-Zealand	NZD / USD	0.63	Negative	0.60	Neutral	0.63
	Canada	USD / CAD	1.35	Positive	1.32	Positive	1.30
	Asia	China	USD / CNY	7.11	Neutral	7.20	Neutral
India		USD / INR	83.87	Positive	82.00	Positive	82.00
Latam	Brazil	USD / BRL	5.64	Positive	5.00	Positive	5.00
	Mexico	USD / MXN	19.87	Positive	19.00	Positive	18.00
EMEA	South Africa	USD / ZAR	17.75	Neutral	18.00	Neutral	17.50
	USD Index	DXY	101.34	Neutral	101.75	Neutral	100.01

Sources: BNP Paribas, Eikon/Datastream

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Equities



A foggy morning leads to a sunny day

Key Points

- **Earnings Season recap** – The Q2 reporting season saw earnings reports generally better than expected, where EPS growth came in better than initially expected. Encouragingly, the US saw a broadening in earnings delivery beyond the Mag7. While earnings delivery in the US continues to be stronger than in Europe, the spread between the region’s EPS growth has narrowed further.
- **The crash that didn’t happen** – The markets were quick to recover from the yen-related flash crash. Interestingly, the Mag7 failed to reach new highs during the rebound. History tells us that future long-term performance, after such incidents, is usually above average.
- **The next few miles might still get choppy though** – Markets tend to double dip after huge spikes in the VIX. This coincides with seasonal headwinds as the second half of September is the weakest period of the year and election years often experience a correction in October.
- **The long-term picture still supports equities** – While the short-term outlook may look bumpy, the long-term backdrop of falling rates in a non-recessionary environment still looks encouraging for equities. We would see any short-term weakness as a buying opportunity, especially in our favoured markets such as the EU + UK Equities, Japan and Small Caps.

Main recommendations

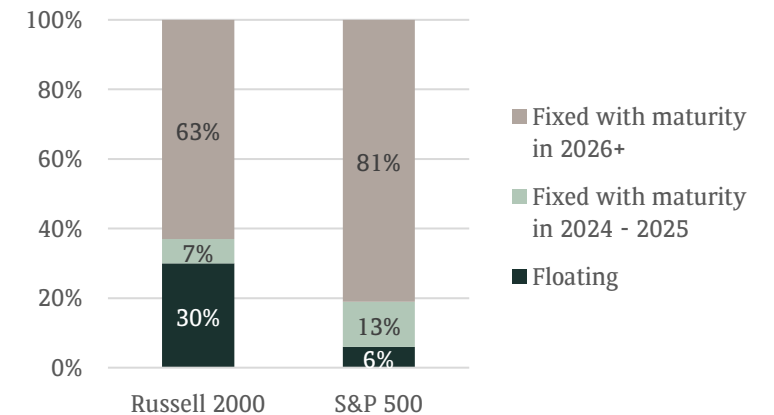
- ➔ **Look for Japanese small caps** as a way to diversify away from FX sensitive exposure while harvesting the potential of domestic economic reacceleration. High levels of cash allow for a growing shareholder return.
- ➔ **We downgrade Mexico to Neutral** following the Judicial reform proposal the Executive sent to Congress. We believe replacing the judicial system should increase risk, Mexico’s risk premia and limit Capex. That is a problem as nearshoring is reaching key bottlenecks.
- ➔ **EU Telecoms UPGRADE to Neutral:** one of the most defensive sectors when policy risks and trade tariffs increase. We expect EPS cuts to come to an end as previous investments in fibre are now generating free cash flow and EBITDA.
- ➔ **EU Travel & Leisure DOWNGRADE to underweight:** The YOLO (You Only Live Once) effect is fading as the services demand catch-up effect comes to an end due to the rising cost of living. Earnings estimates continue to face downgrades. Sell into strength.
- ⚠ **The key risks** are that the markets start to reprice growth fears with central banks being perceived as “behind the curve”. Increasing policy uncertainty around tariffs could weigh on sentiment, too.

EARNINGS SEASON IN A NUTSHELL

	S&P500	StoxxE 600	Topix
% Cos. reported	89%	85%	95%
% Cos. beating EPS	79%	59%	61%
EPS %y/y	8%	1%	11%
% Cos. beating Sales	48%	51%	58%
Sales % y/y	5%	2%	7%

Source: BNP Paribas, Bloomberg

US SMALL CAPS INSTANTLY BENEFIT FROM FALLING RATES DUE TO MATURITY PROFILE



Source: BNP Paribas, Bloomberg

05

Commodities



Commodities at a glance

Brent prices reached a low of USD 76 in August as fears of a sharp economic slowdown have resurfaced, while OPEC+ production cut tapering should start from October. Brent prices rebounded at the end of the month as Libyan production (1 mb/day) was interrupted.

Most base metal prices declined sharply in July as manufacturing PMI were much weaker than forecast but started to recover from mid-August as recession

fears abated. YTD, tin is still 31% higher, zinc +11%, copper +10%, aluminum +7%, lead and nickel +3%. Iron ore (-10%) is substantially lower (as at 28/08).

Gold continued to rally to reach a high of USD 2530/oz on 20 August.

BASE METALS



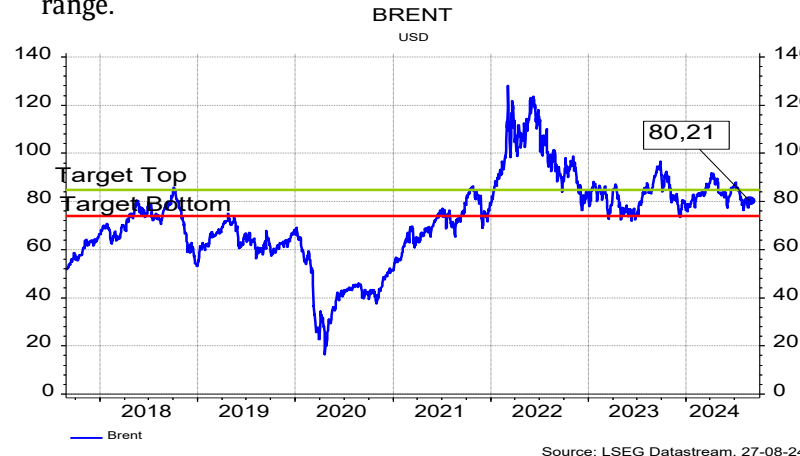
A rebound in manufacturing PMI is needed for base metals to fully recover but nevertheless we remain Positive as inventories outside China are low and the medium-term outlook remains bright.



OIL



We are now Neutral on oil as Chinese demand remains weak, recessions fears linger in the US and the OPEC+ wants to taper its voluntary production cuts from October. We expect Brent to trade in the USD 75-85 range.



GOLD



Gold fundamentals remain strong, but we are inclined to take some tactical profits above the top of our near-term expected USD 2350-2550 trading range.



06

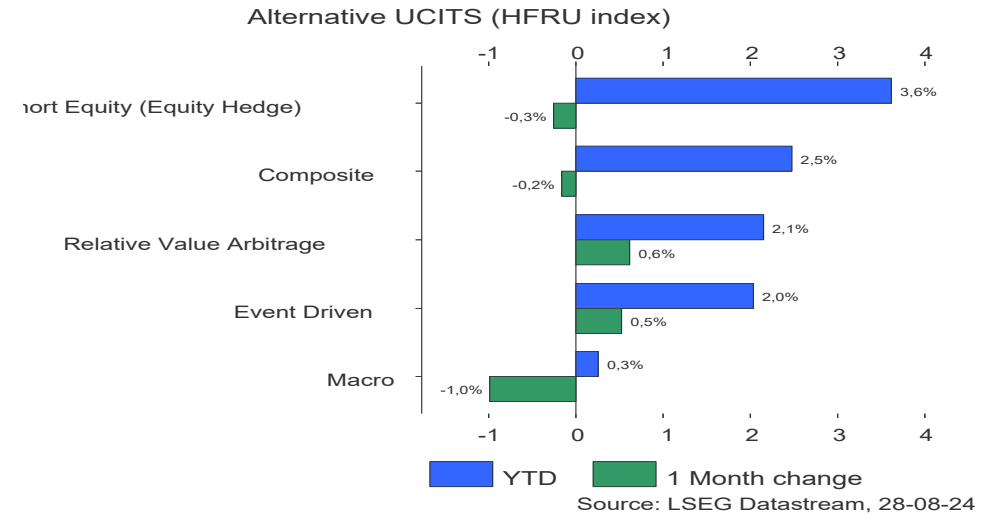
Alternative investments



Alternative Investments at a glance

Performance has been slightly negative over the past month for the main strategies. It remains positive this year. Long-short equities were the best performer year-to-date. Relative value has outperformed over the past month.

Positive opinion on Event Driven, Long-Short equities and Relative Value.



Global Macro



Neutral: Markets are still contending with the pace of monetary easing and a soft vs. hard landing of the economy, but also now with political risk, culminating with the US presidential election. Low visibility regarding future trends. Given potential surprises, directional bets remain more challenging than Relative Value trades.

Event Driven



Positive: After a slow 2023, M&A activity is expected to continue to tick up in 2024 with first half M&A activity increasing 18% to USD 1.5 trillion. Despite current political risk, the combination of increased volume, several large outstanding deals, inflation slowing with rates likely going down, may yield a good end to the year for the strategy as in 2023.

Long/Short Equity



Positive: Intra market equity dispersion is back at historically high levels, with a very wide gap between expensive and cheap stocks, paving the way for better long and short stock-picking opportunities. If equity markets get challenged on bearish sentiment, long/short should provide strong absolute returns with low correlation to equity markets.

Relative Value



Positive : The lagged effect of rising rates and the need to refinance debt before the “maturity wall” should cause dispersion between strong and weak issuers. Managers are currently well “paid to wait” on shorts, as they collect positive interest on the cash proceeds of these shorted bonds. Convertible bond arbitrage is benefiting from increased issuance/refinancing, stabilised rates, and the end of long only investor outflows. Government bond Relative Value arbitrage should benefit from diverging monetary policies & inflation, with less risk than directional macro trades.



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