AXA Investment Managers

Investment Institute Macroeconomics

The times they are a-changin'

Monthly Investment Strategy

AXA IM Research

June 2024

Summary: June 2024

Theme of the month: The times they are a-changin'

- We described 2024 as the great election year and at the mid-way point it has not disappointed.
- In recent Emerging Market elections, India re-elected Modi for a third term, but in a surprise, with a smaller majority than expected, relying now on junior coalition partners. This threatens necessary fiscal reforms and a more populist approach, something that echoes more broadly across EMs.
- Mexican and South African elections also sparked market reaction. The former a drop in the currency as the expected new president Sheinbaum achieved a super-majority in the lower house. In South Africa, the ANC's loss of overall majority and subsequent coalition negotiations have been taken positively.
- European parliamentary elections were broadly as expected, with gains for the far right, but the centre right likely retaining a viable majority. But these precipitated early elections scheduled in France (30 June and 7 July), where Macron's centralist rule is likely to be overturned by the far right's RN and the left's Nouveau Front Populaire. Similar tensions will hang over Germany for local elections later this year.
- The UK election on 4 July looks set to deliver a change of government: Labour on track for a comfortable majority. Fiscal constraints are likely to require any new government to tighten fiscal policy. The UK's strong backing of political centralism suggests post-peak populism for now.
- The US election – the most globally significant – will hang over the rest of this year, with increasing focus after the 27 June TV debate. Polls suggest a slender lead for former President Trump for now.

Macro update: Sticky inflation, more cautious policy easing and elections

- Cautious central banks are emerging as a common theme despite the ECB and BoC easing policy. This comes as growth has started the year more positive and inflation has typically been stickier. For many economies dollar strength is an additional headwind to easier policy.
- In the US there are tentative signs of softening (not weakening), with Q1 GDP at 1.3% (saar) and consumer spending slowing from a fast pace in H2 2023. Inflation appears to be softening after a services-led spike in Q1. The Fed looks likely to cut twice this year from September, despite its own cautiousness.
- Europe has seen a tightening in financial conditions following election uncertainty. Inflation edged higher in May, but we expect a more decisive decline in services inflation in the autumn. The ECB cut rates but fell short of communicating a future path. We continue to forecast another two cuts this year.
- GDP softened in April after a solid Q1 in UK but should post at least 0.3% in Q2. A softening labour market should ease services inflation further, even as headline inflation has reached 2%. The BoE looks set to ease in August, with some of June's no changers suggesting the decision was "finely balanced".
- Japan's activity has been subdued, albeit exaggerated by one-off effects. We expect consumption to recover with real disposable income. The BoJ is likely to raise policy in Q3, we think in September after adjusting bond purchases in July. We think it will take a long time to reach the BoJ's 1% neutral rate
- Chinese activity remains challenged. Short-term we have seen a modest lift in retail activity and more generally industrial output has been supported by government-led investment. Longer-term, a more challenging external environment adds weight to the need for domestic rebalancing.
- In broader emerging markets, central bank cautiousness is also echoing inflation stickiness and fx softness against a strong dollar. Expectations for monetary loosening are being delayed. In several jurisdictions there is a risk that fiscal discipline is also fading.

Central scenario

Summary – Key messages

Our central scenario: Global economy softens, disinflation slows.

Global growth expected to slow to 3.2% in 2024 and 3.1% in 2025.

Disinflation slower this year, spreading to core. Creates space for monetary policy easing, Fed doubts have global spillover.

Inflation

Headline close to targets in many economies. Core disinflation to broaden this year but stickiness in services; target rates more likely next year.

Monetary policy

Central banks tip into easing restrictive policy, but slower delivery with Fed caution impacting others. Balance sheet policy from ECB and BoJ to come to the fore around mid-year.

Fiscal policy

European rules require fiscal consolidation, elections sharpen focus. EU budget submissions in Sept/Oct. US longer term outlook still in doubt.

Emerging Markets

Inflation easing slowly across EM. Central bank easing cycle becomes more cautious as strong dollar weighs.

FX

Dollar rebounds on overseas political uncertainty. Euro weakens, but impact on several EMs. Yen increasing issue for Japan authorities.

Rates

Delayed delivery of easier policy lifts term rates higher. Actual cuts should see yields lower. Re-weighting of slowdown probabilities could lower rate outlook into summer.

Growth

Growth started 2024 on firmer footing in most economies, but likely to settle into softer pace for rest of year. Consumers supported by real disposable income growth.

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Alternative scenarios

Summary – Key messages

	Entrenched supply shock Probability 15%	A global boost Probability 20%
What could be different?	- Banking turmoil, political escalates, credit conditions tighten. - Geopolitical tensions escalate: Ukraine, Middle East and Indo-Pacific - Inflation expectations rise, affecting wages and persistence	- Labour market participation recovers/migration strong, strong income growth and easing inflation pressures - Productivity boost following investment rebound and structural post-pandemic adjustments, AI impact becomes visible
What it means	- Growth weaker, employment falls back, but inflation remains elevated - Monetary policy ill-equipped to deal with supply shocks and financial instability, deteriorating inflation credibility forces still tighter policy in DMs	- Growth surprises on the upside in most regions - Inflation fades more quickly towards and below central bank targets - Monetary policy softens quicker than signalled
Market implications	- Risk appetite deteriorates / equities sell off / credit widens - Sovereign yields reprice higher - Dollar remains elevated - EM debt to come under pressure	- Risk-on environment, equities make further gains, growth retains lead over value - UST softens, EUR strengthens - Spreads grind tighter

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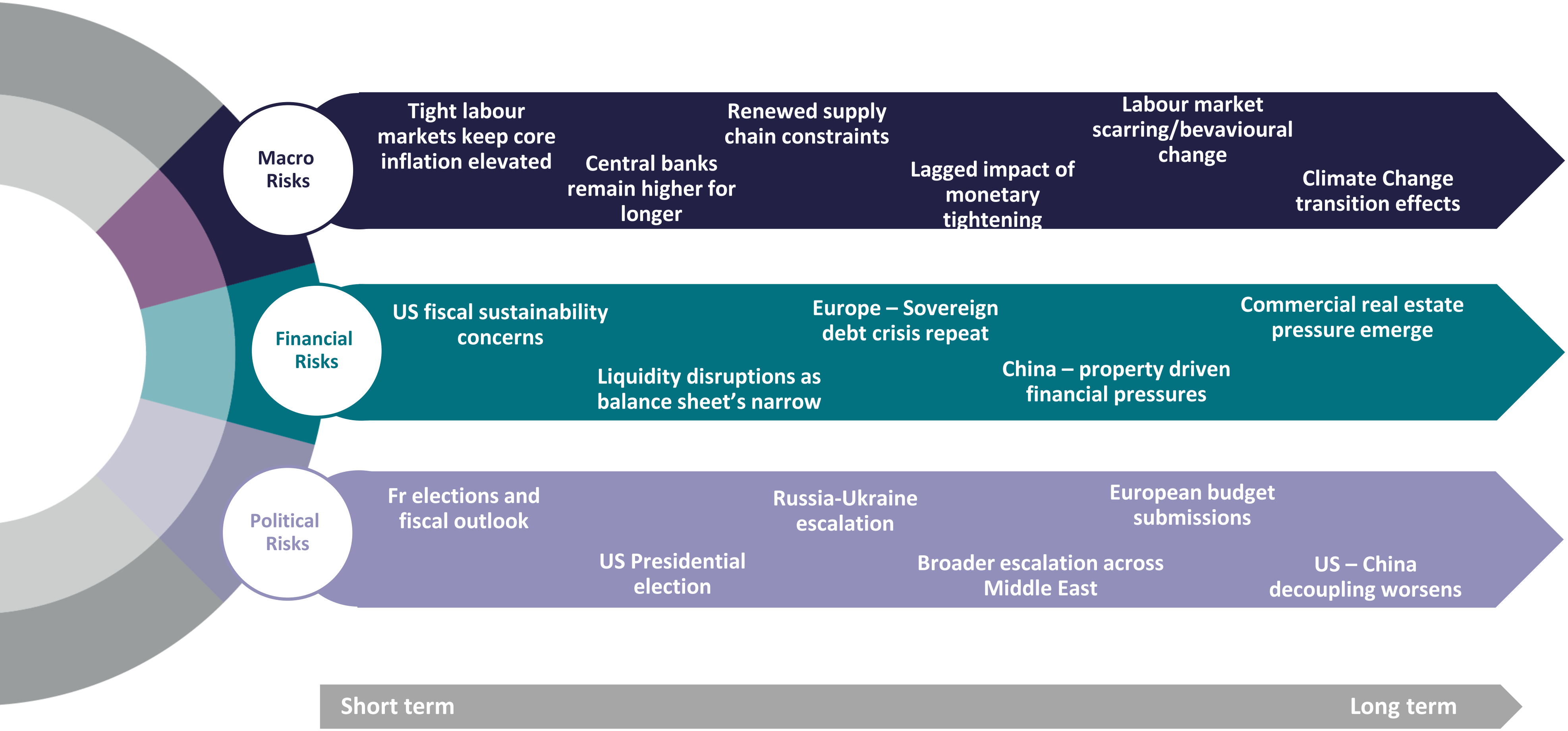
RISk Radar

Summary – Key messages



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Theme of the Month

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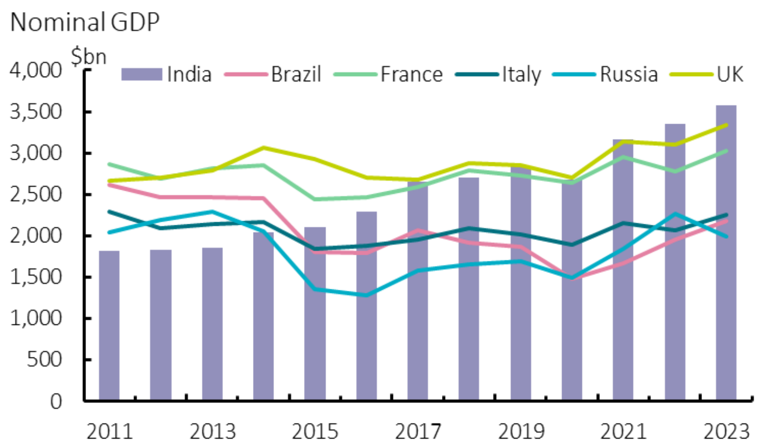
The times they are a-changin’

India returns Modi, but less of a strongman

Pro-investment policy continuity, but still a challenging environment

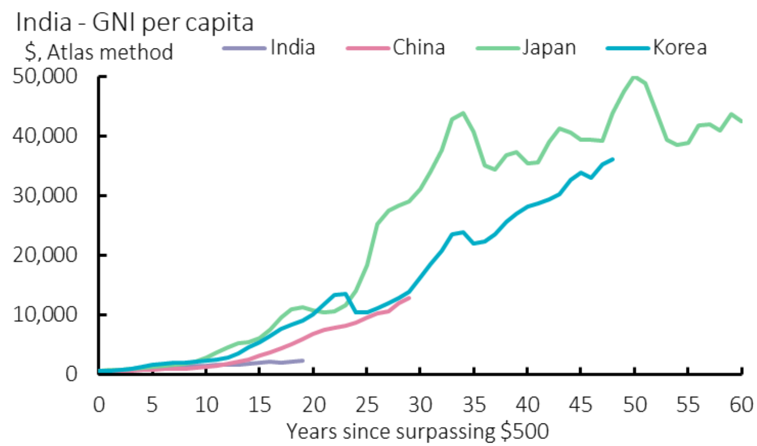
- Narendra Modi has secured another five years in office following the parliamentary elections completed in early June. However, his Bharatiya Janata Party (BJP) lost the absolute majority it enjoyed during the previous two parliamentary terms. Widening income inequality, rising youth unemployment, and stubbornly high food price inflation contributed to the reduced support for Modi in the election, along with broader social tensions, including a rejection of his polarising Hindu nationalism rhetoric and growing authoritarian tendencies. His majority now stands on a more fragile coalition with junior partners.
- The initial negative market reaction to Modi's failure to secure an absolute majority proved short-lived, as India’s fundamental position is expected to remain stable. Moreover, India's economic expansion should continue to outpace most other major emerging markets, such that at the end of this coming five-year term, India will likely be the third largest economy in the world.
- India continues to present investors with a compelling growth story, but the new political environment under Modi 3.0 could make it even more difficult to enact challenging, but necessary reforms to enable India to capitalise on its 'demographic dividend'. Much still needs to be done to improve the overall business environment to lift investment, create jobs and drive-up per capita income.

India's economy to continue its ascent...



Source: International Monetary Fund and AXA IM Research, June 2024

... but a long way to go to rival successes of East Asian peers



Source: World Bank and AXA IM Research, June 2024

The times they are a-changin'

Mexico and South Africa surprise in different ways

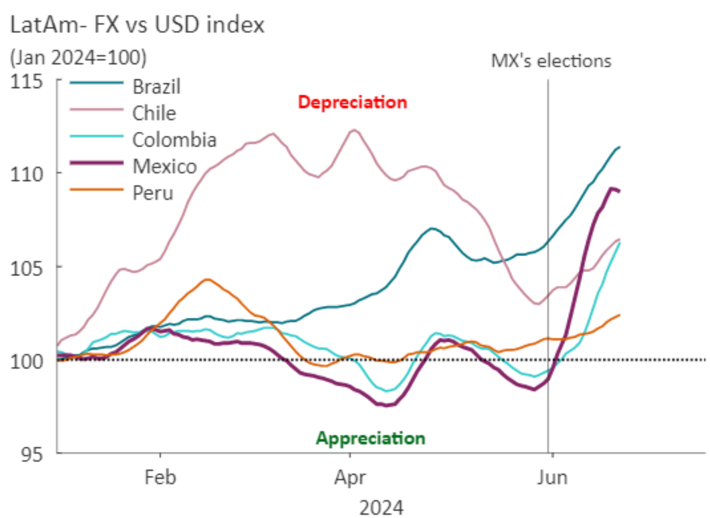
Big win for Morena, institutional uncertainty ahead

- Claudia Sheinbaum secured a historic victory, winning the presidency by a record margin and becoming Mexico's first female president. Morena and its allies now hold a supermajority in the House and are 2 seats short of one in the Senate. Investor sentiment, has been negatively impacted by the results with concerns over the potential approval of contentious constitutional reforms proposed by the outgoing administration as they are perceived as threats to institutional checks and balances.

From a negative to a positive surprise in South Africa

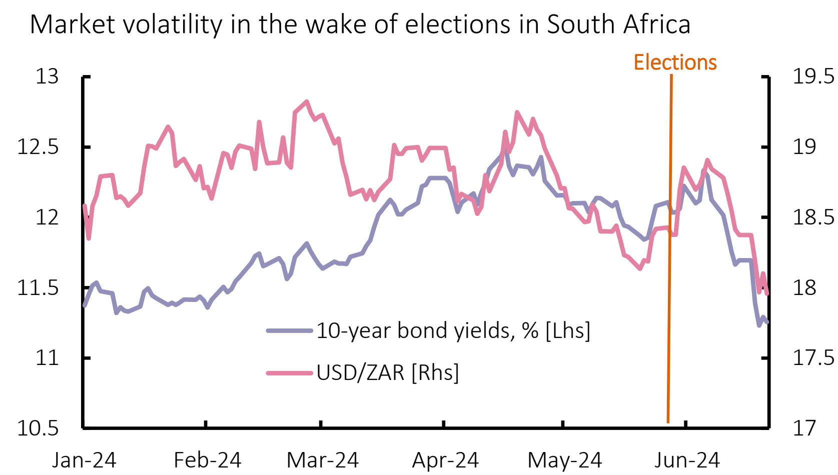
- Although the loss of ANC's majority was more pronounced than expected (to 40% of votes), with the Zuma-led radical-left MK party gaining 15%, the outcome for the economy could prove positive. President Ramaphosa has been re-elected by Parliament and the ANC has formed a coalition with centrist parties DA and IFP. That bodes well for structural reforms, including in the energy and transportation sectors, fiscal adjustment, and overall, for improved policy implementation. Key to monitor however will be the stability of such a 'national unity government' that excludes both far-left MK and EFF parties.

The Mexican peso depreciated sharply after the elections



Source: LSEG Datastream and AXA IM Research, 21/06/2024

Market volatility in the wake of elections in South Africa



Source: Macrobond and AXA IM Research, 21 June 2024

The times they are a-changin'

European elections: large pro-EU coalition likely to be renewed

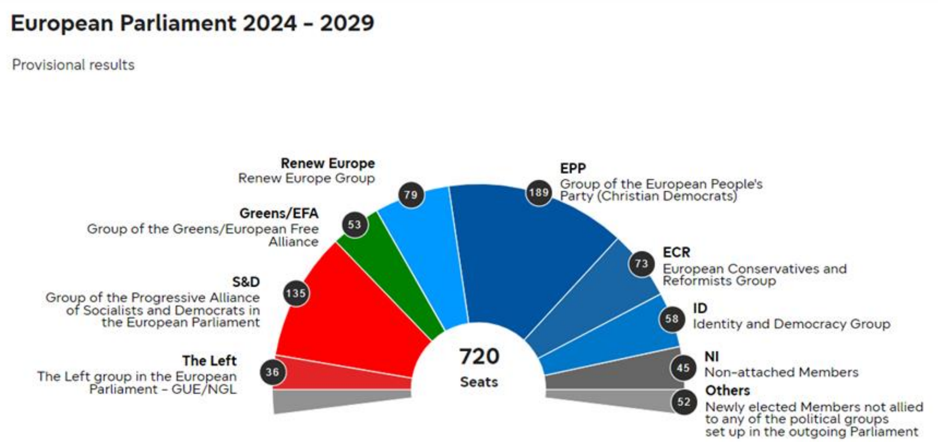
Large pro-EU coalition likely to be renewed

- After the European Parliament election results, we keep our baseline scenario: the EPP should renew its coalition with "Renew Europe" and the Social & Democrats (400 seats in total, 56% from 59%). No alternative coalition looks viable. This will be formed by mid-July, when they will elect a President. Later, the EU council (head of states) proposes a president of the European Commission (endorsed by Parliamentary majority). Despite some disagreements within the EPP, Von der Leyen is likely to be reappointed.
- Nevertheless, parties on the right made significant gains this time and will have an increasing influence on the agenda.

Political agenda

- The fight against climate change has not gone down well on the campaign and has helped reinforce the far right in opposition to it. We don't expect any regression, but focus on implementation
- NGEU: the EC & Parliament are likely to delay the deadline for spending NGEU money beyond 2026.
- Recently, banking union and capital market came back in the discussion topics, but it is unlikely to go any further without a stronger coalition that support those reforms in Germany

Far right parties made gains, but large pro EU coalition still holds around 56% of votes



Source: European Commission Research, May 2024

The times they are a-changin’

France prepares for early election (30 June & 7 July)

Most likely outcome increases uncertainties

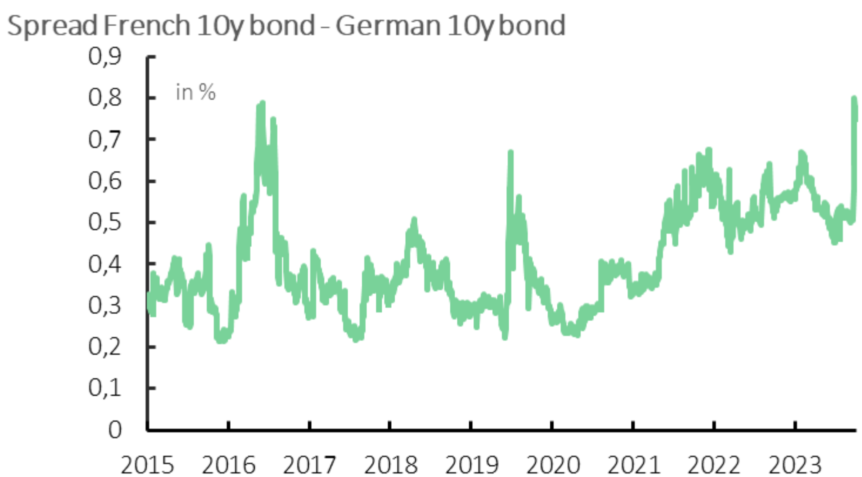
“Hung parliament”: Without absolute majority, a government would be unable to enact laws without using Article 49.3. In return, a prime minister would rely on the responsibility of the government and runs the risk of being overthrown. This would likely persist until the 2027 elections (unless the president resigns and/or dissolves parliament again - but only after one year). This would lead to difficult 2025 budget negotiations, most likely without any fiscal consolidation, despite the Commission’s recent Excess Deficit Procedure.

Or an RN majority: but two possible manifestations depending on how the RN decides to approach the 2027 presidential elections

- “Meloni style”: prudent economic management and a focus on social issues to satisfy the electoral base. Truss’s episode in the UK reminds the RN of fiscal risks. The alliance with some former centre-right members should also provide some budget guarantees.

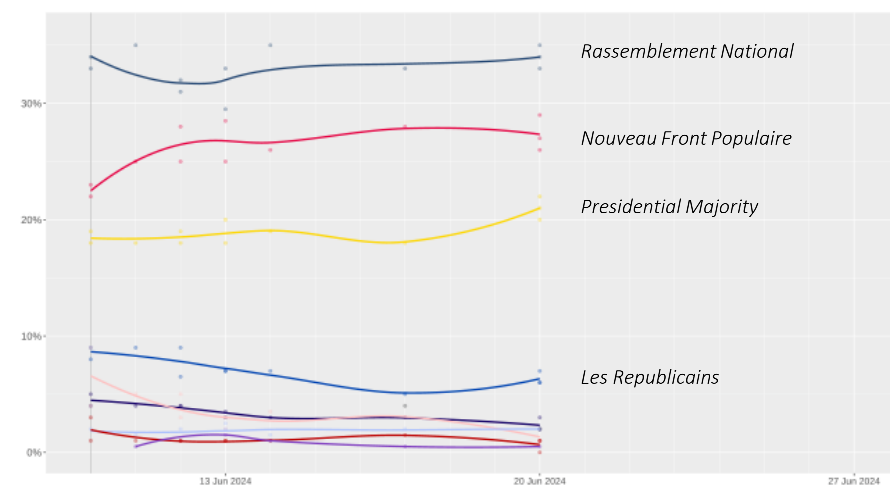
- RN delivers on its economic agenda. Bardella just released a new manifesto, but figures are too rare to make an assessment. 2022 manifesto was estimated to cost ~€100bn per year. This could see severe market stress and long-lasting credibility damage.

French bond spreads highest since 2017 presidential election



Source: Refinitiv, AXA IM MAcro Research, as of 20 June 2024

RN poll wins overlook complexity of the second round



Source: Wikipedia, June 2024

Investment Managers

The times they are a-changin'

UK to deliver a change of government

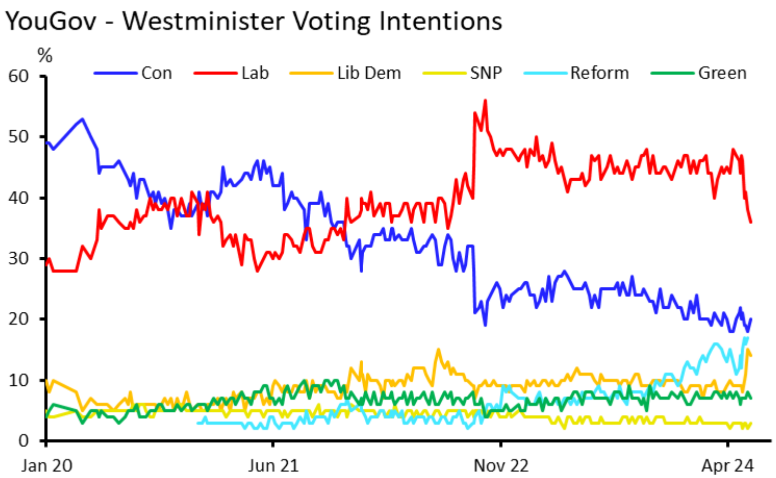
A comfortable Labour majority is our base case

- Labour have maintained around a 20-point lead in the polls since the election was called on 22 May. Note the gap between parties usually narrows in the run up to election day. But what really matters is how this translates into seats. Estimates vary, but BritainElects puts Labour on track to win 485 seats, more than in the 1997 election when Blair won 418 seats.

Additional fiscal tightening likely necessary

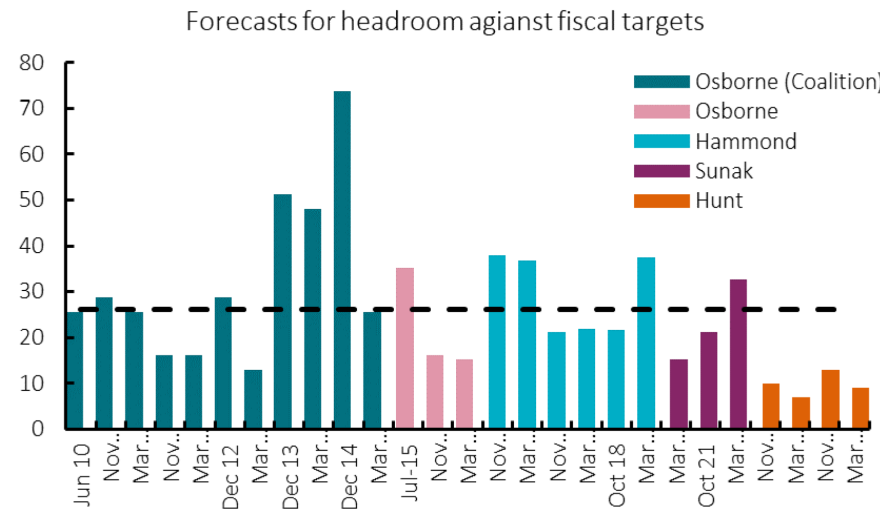
- Any incoming government's policies will be limited by high debt, sluggish growth and high interest rates. Both major parties have committed to getting debt as a share of GDP falling in five years' time, leaving both with just £8.9bn of headroom, according to the OBR in March. The Spending Review – where coffers are usually topped up by around £10bn-£20bn – and forecast changes mean this headroom has probably already been wiped out. In addition, chunky spending cuts are already pencilled in under the current government, which any government will struggle to implement. Additional fiscal tightening, therefore, looks inevitable; we expect Labour to push ahead with tax increases early in the parliament, which they should reverse by the next election.

Labour's lead in the polls has remained solid



Source: YouGov, AXA IM Research, June 2024

The headroom against current fiscal rules was wafer thin in March



Source: The OBR, AXA IM Research, June 2024

The times they are a-changin'

And the US election still looms large

Current polling remains tight

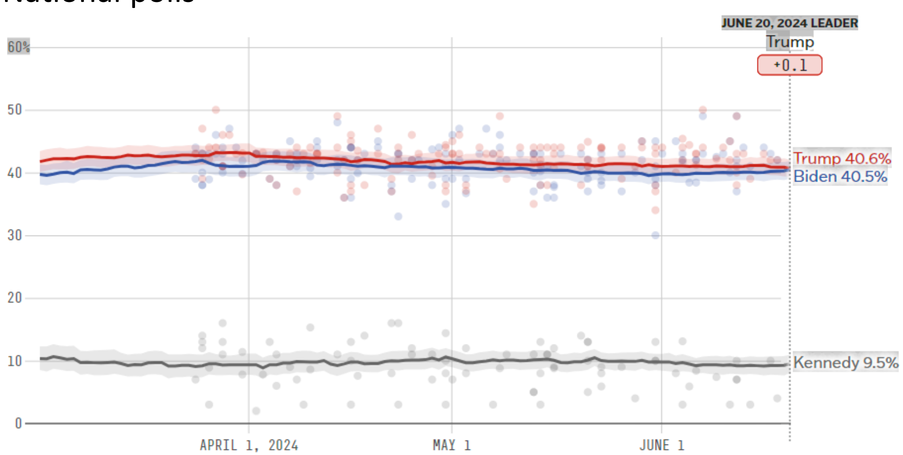
- Current polling in the US remains very tight. At a national level, former President Trump leads President Biden by 0.1ppt. In that context, independent challenger Robert Kennedy jnr's 9.5% vote share is significant. Trump has a stronger lead in marginal seats, but even here few leads exceed the error margins of the polls.

TV debate to spark renewed focus

- The coming month is likely to see markets place more focus on November's elections. The first TV debate between Biden and Trump will be held on 27 June. Both candidates are 'known' so this may not shift the dial much, but Biden's performance – particularly with ongoing speculation around his health and acuity will be critical – and impressions may linger with the next debate not until September. Thereafter, Trump is set to reveal his choice for Vice President at the Republican National Convention in July. The Democrat convention is held in mid-August.

Investment usually an accelerator of underlying activity

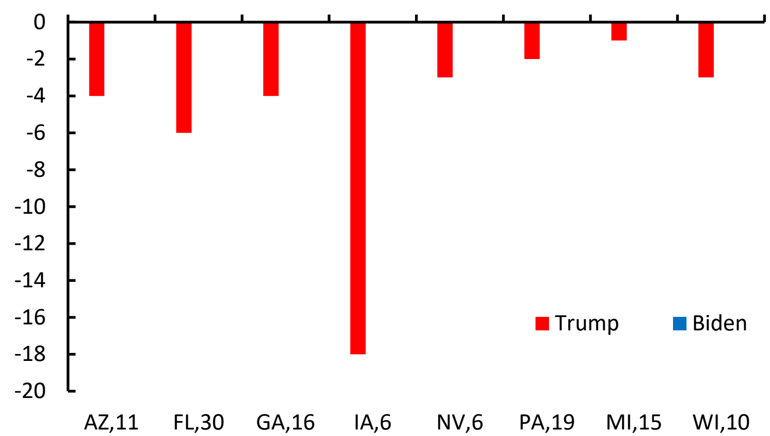
National polls



Source: 538, June 2024

Investment spending and the interest rate cycle

Marginal states election wins



Source: 538, June 2024

Macro outlook

Investment Managers

An unexpected weakening in the labour market

US

Labour market heading towards better balance

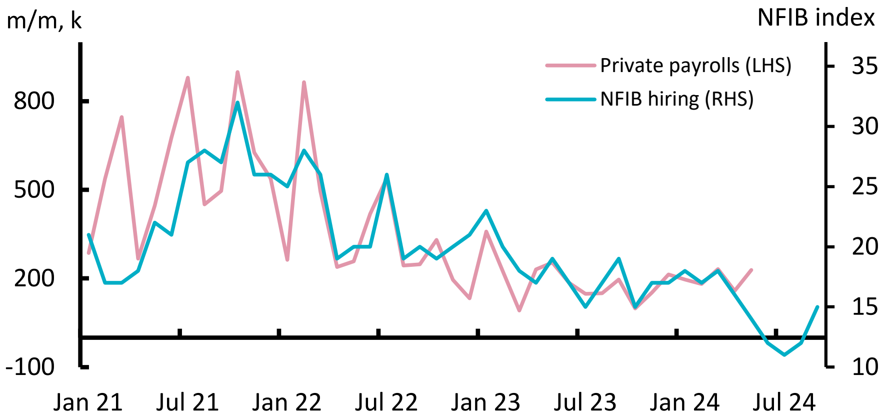
- May's payrolls defied weaker expectations, surging 272k and leaving the 3m trend around its 2024 average of 250k. Earnings also accelerated to 4.1% (3m yoy) up from 3.0% last month and above the Fed's comfort zone, probably closer to 3.5%. However, the household survey employment measure fell 408k, unemployment rose to a 3-year high of 4.0% and separately vacancies fell sharply again to 8.1m, with the vacancy/unemployment ratio, the Fed's preferred measure of slack, now close to pre-pandemic levels

May's inflation report "good"

- Inflation fell below expectation. The headline was flattered by falling oil prices, flat on the month, but the core increase of 0.163% was the slowest in over 3 years, with services inflation depressed by ex-shelter prices +0.02%, albeit that shelter remained at 0.4%. We continue to expect shelter inflation to soften in H2. Last year's base effects for H2 will make it difficult for the annual rate to fall this year, but a stable rate means slower momentum. We forecast inflation to average 3.3% in 2024 and 2.6% in 2025.

Payrolls defy weaker survey in May, but for how long?

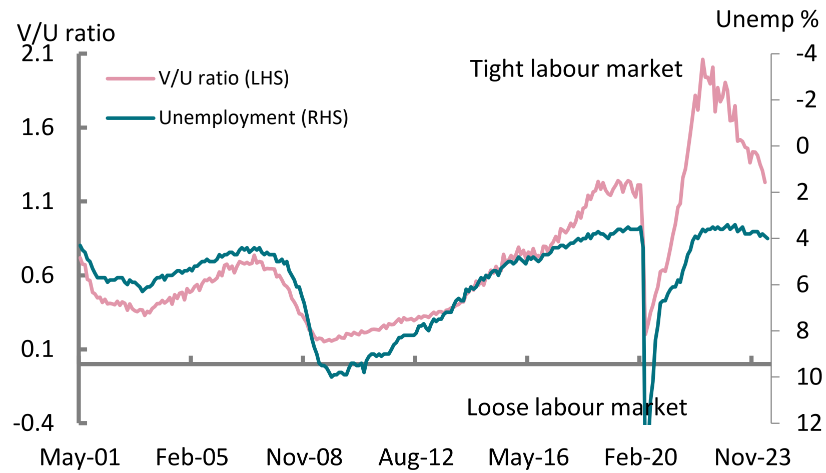
Private payrolls and NFIB hiring intentions



NB Chart adjusts NFIB index lead from 2 to 4 mths Sep 22
Source: BLS, NFIB, AXA IM Research, June 2024

Labour market in better balance

Measures of labour market slack



Source: BLS, AXA IM Research, June 2024

FOMC treading water

US

Softening, but not weakness in broader growth

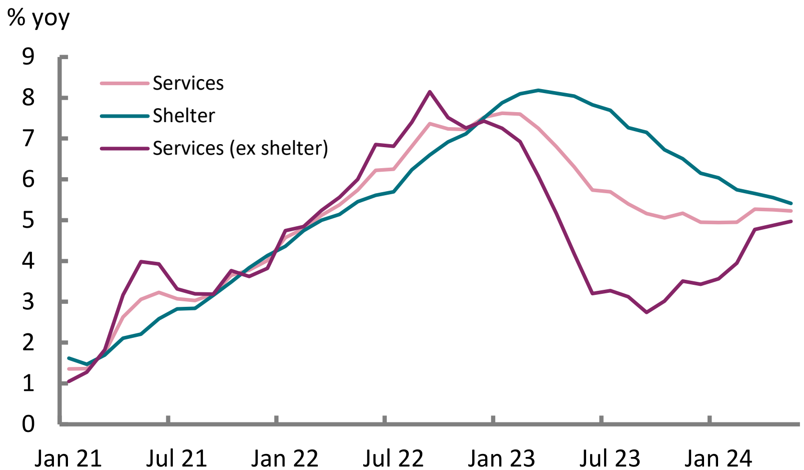
- With mixed messages in the labour market, broader indicators have softened. GDP growth rose by just 1.3% in Q1 and we expect 2.0% in Q2 (current Atlanta Fed GDP now-tracker at 3.0%). This is likely to be driven by weaker consumer activity, confidence has softened this year and real retail sales growth has been also weaken with a sharp drop in April and modest rebound in May. We expect this trend to persist through H2 and into 2025, forecasting growth averaging 2.4% in 2024 and 1.6% in 2025.

Fed median forecast one cut for 2024

- The Fed left policy unchanged in June as was widely expected. The Summary Economic Projections saw little adjustment, inflation nudged up 0.2ppt this year, 0.1ppt next and unchanged at 2.0% in 2026. But the Fed's rate forecasts shifted higher. The median rose to just one cut this year, but reflected 4 votes for no change, 7 for 1 cut and 8 for 2. We left our forecasts unchanged expecting the Fed to cut twice this year starting in September, and four times in December.

Services inflation momentum softens

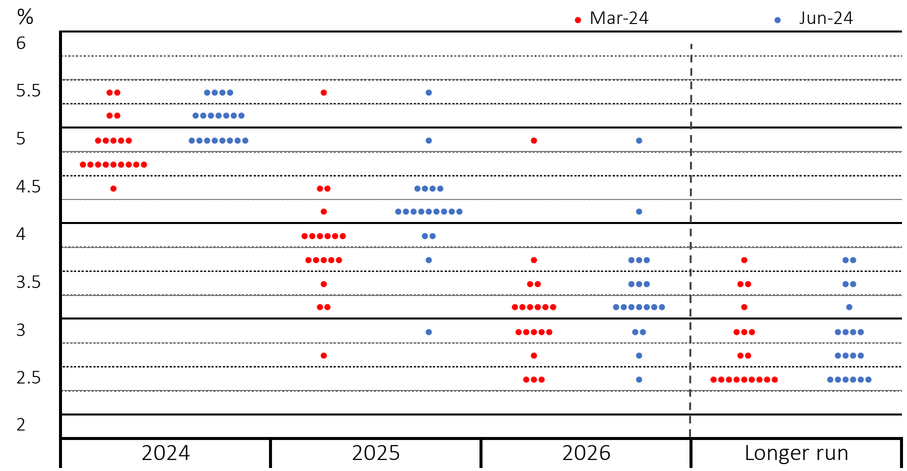
Services inflation



Source: BLS, AXA IM Research, June 2024

Fed median view shifts to one cut, by finely balanced

Fed participants end-year rate projections (the "dot plot")



Source: FRB, Jun 2024

French political turmoil and limited contagion

Eurozone

The surprise French dissolution caused some market turmoil

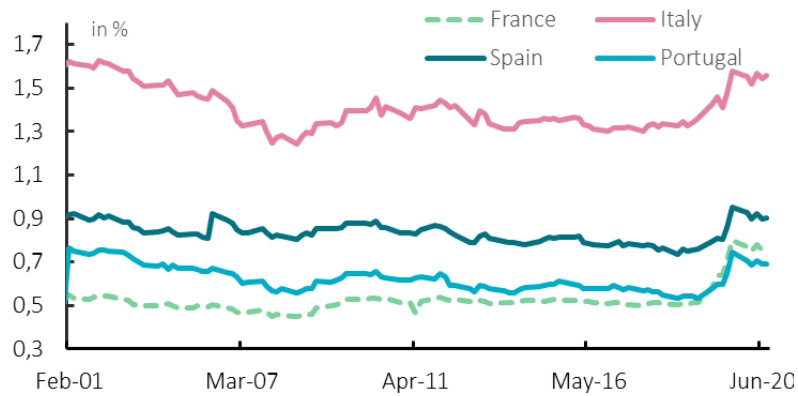
- Financial markets reacted negatively to the surprise French election announcement with a sudden and large fall in domestic equities, particularly for companies more exposed to domestic markets. It also impacted French sovereign spreads (versus German Bunds), which widened to 80bps - not seen since the second round of 2017's presidential election, with a risk of a far left and right win, with neither party ruling out leaving the EU. The situation has stabilized (but not improved) and uncertainties remain. Despite the idiosyncratic French nature of the shock, other countries have seen spreads widen but contagion has been limited so far.

France already hit by business surveys, business goes on elsewhere

- In June, euro area consumer confidence continued to rise on the back of real wage gains. Confidence remains below the 2010-2019 average (0.7 standard deviation) but is still consistent with a gradual improvement in private consumption. Flash PMIs were weaker in June. The manufacturing sector fell to 45.6 (from 47.3 – below 50 signifies contraction), impacted by lower output in France and Germany. Services sector is well anchored in expansion territory at 52.6 but fell below 50 in France for the second month in a row

A higher premia for France

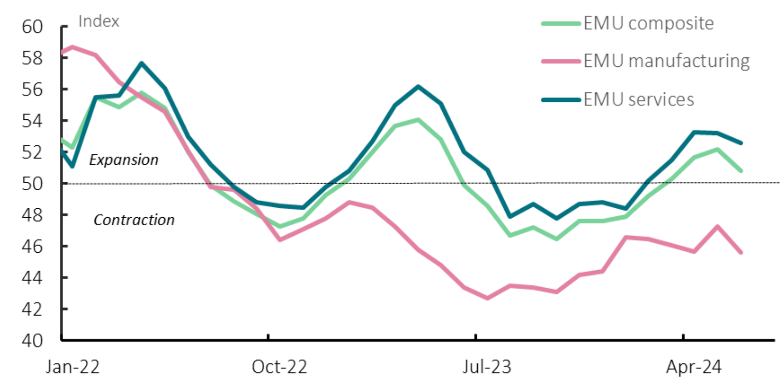
Spreads versus German 10Y



Source: Refinitiv, AXA IM Macro Research, as of June 21

An aborted recovery ?

EMU Purchasing Managers indices



Source: Bloomberg, AXA IM Research, June 2024

ECB: Direction is clear but next steps are not

Eurozone

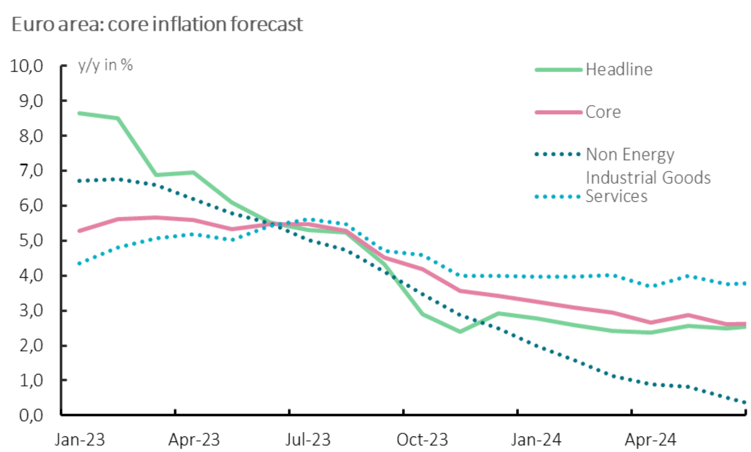
Bumpy inflation road

- Headline inflation reached 2.6% year-on-year in May and core ticked up to 2.9%, driven by services inflation rising to 4.1%. Prices in recreation, leisure, tourism items continue to boost services prices while other services have started to normalize. We continue to anticipate a more marked slowdown of services inflation from Sept/Oct 2024.

The ECB needs more

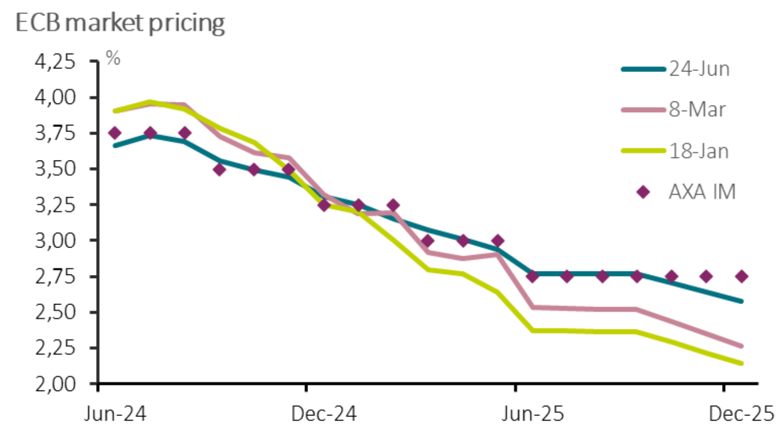
- The ECB gave mixed signals in June, confident it was the right moment to deliver the first cut, but not sufficiently so as to reiterate a dovish signal for coming quarters. Instead, the ECB insisted it will make its decision based on incoming data. We believe the caution was not driven so much by domestic fundamentals as by the uncertainties in the US. If US inflation and the labour market evolve as we expect over the coming months with the Federal Reserve easing later this year, our scenario of further ECB rate cuts in September and December should be confirmed despite questions over longer-term inflation.

Core inflation deceleration hides two different underlying dynamics



Source: Eurostat, AXA IM Macro Research, as of June 2024

Our long standing calls on rate cuts are now market baseline



Source: Bloomberg and AXA IM Research, June 2024

Recovery should continue this year

UK

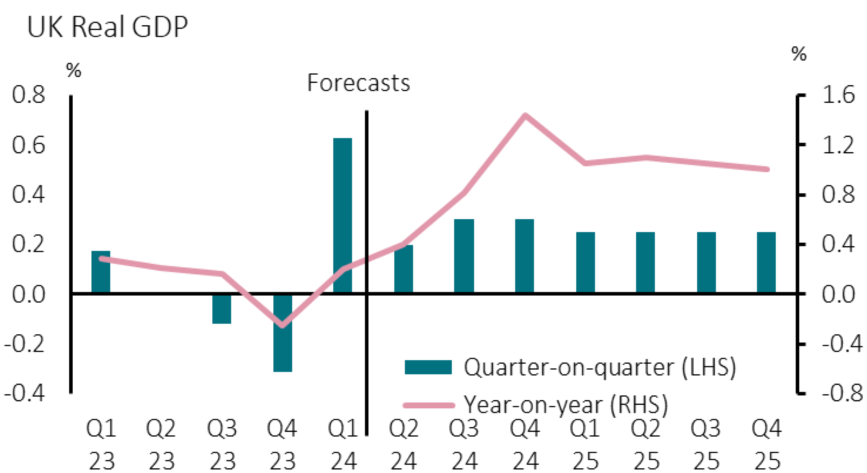
Recovery faltered in April, but momentum should resume

- Monthly GDP showed that growth stall in April, with output remaining unchanged on the month, but activity was still up 0.7% on a three-month-on-three-month basis, so even if GDP remains unchanged in May and June, we will still see a quarter-on-quarter rise in output of around 0.3%. We remain comfortable with our outlook for 0.7% growth in 2024.

Bank of England remain laser focused on inflation and wage data

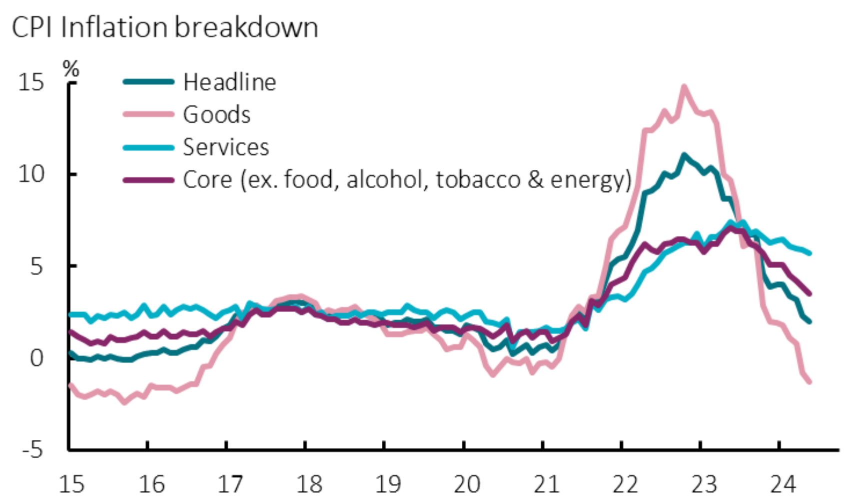
- Headline CPI inflation dropped back to the 2% target in May, from 2.3% in April. This masked sticky services inflation, which ticked down to 5.7%, from 5.9% – the MPC expected 5.4% – but key areas of concern, such as in hospitality, did see inflation ease.
- Average weekly earnings excluding bonuses, meanwhile, were unchanged at 6.0% in April, but the private sector component – a measure more closely watched by the Bank of England (BoE) – dropped to 5.8%, from 5.9%.

Recovery will continue, despite easing momentum



Sources: ONS, AXA IM, June 2024

Services inflation is sticky, but will continue to tick down



Source: National Statistics, AXA IM Research, June 2024

August Bank of England meeting is "live"

UK

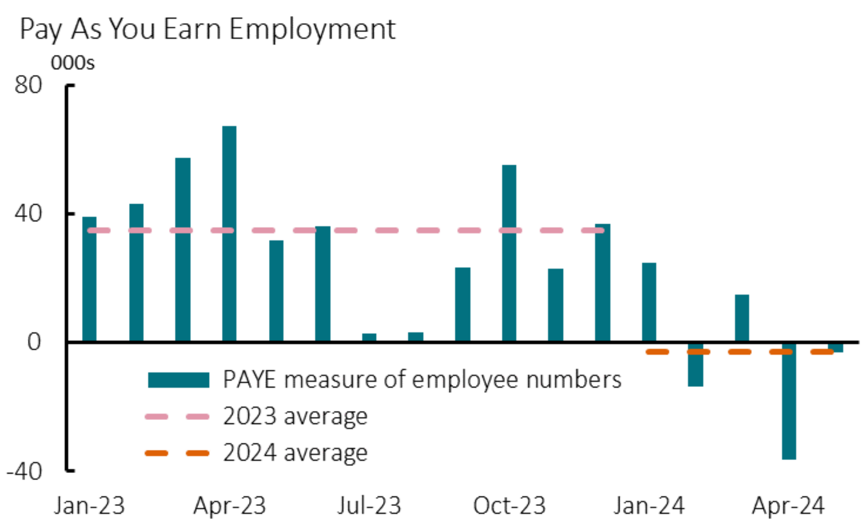
We continue to think the Bank will cut in August, but incoming data remain key

- Growing labour market slack should ease wage pressures going forward. Employment fell by 140K in the three months to April, pushing up the unemployment rate to 4.4%, over a 2½-year high. And PAYE employment has also softened this year, with a monthly decline of 2.7K on average, compared to an average increase of 34.9K across 2023.
- The Bank of England kept the policy rate unchanged at 5.25% in June, with the same 7-2 split as in May. But the MPC is preparing to start the easing cycle; the Bank continued to emphasize "a range of views" on the MPC, stating for some "the policy decision ... was finely balanced." We continue to forecast the first 25bp cut in August and then an additional cut in November.

Labour on track to win election, but tough decisions await

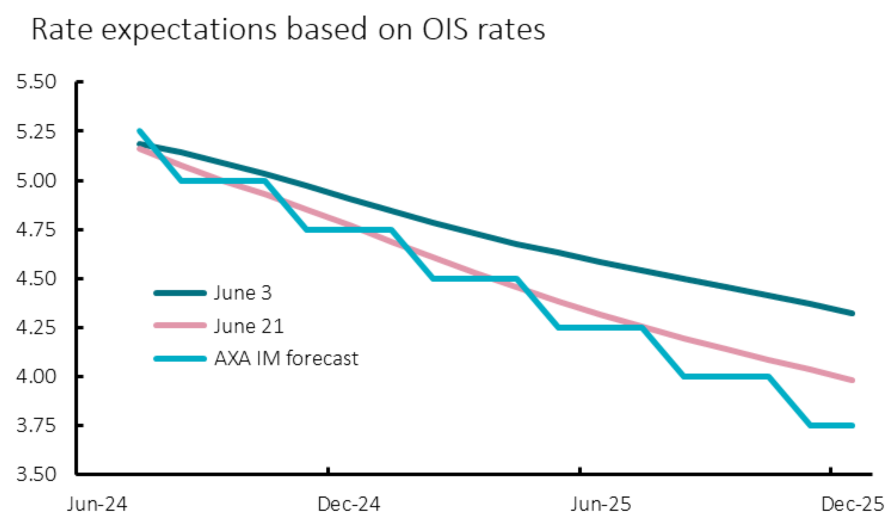
- Labour remains ahead in the polls with a chunky 20-point lead; a comfortable Labour majority remains our base case. The key point though is that whichever party wins, a challenging environment awaits, given the fragile nature of the public finances.

Signs labour demand is easing off



Source: National Sources, AXA IM Research, June 2024

Bank Rate will fall more than markets expect, despite downward shift



Source: Bank of England, AXA IM Research, June 2024

Extra rescue effort on housing has not received a positive response

China

Falling property prices persist despite further policy support

- Despite the central government's announcement of more support in mid-May aimed at stabilising the property market, which has been in decline since early 2022, the market's initial reaction was muted. Property prices have continued to fall. The People's Bank of China's RMB 300 billion re-lending programme has been deemed insufficient in helping local governments acquire housing inventories. As the sector remains under pressure, more substantial support is needed to bring about stabilisation, although only incremental measures are expected in the near term.

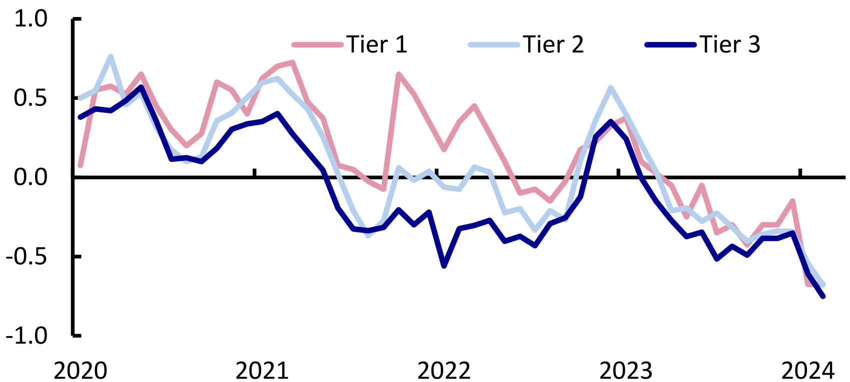
Consumer activity edged up, but sentiments remains fragile

- Despite the latest retail sales report bringing some upside surprises, the overall tone remains subdued, reflecting ongoing property market developments and a weak labour market. Improving labour market conditions would be the most critical factor in reviving consumption, and signs of stabilisation in the property sector would further boost spending. However, neither is currently on the horizon.

Despite further rescue effort property price kept falling

National property price - primary market

mom, %

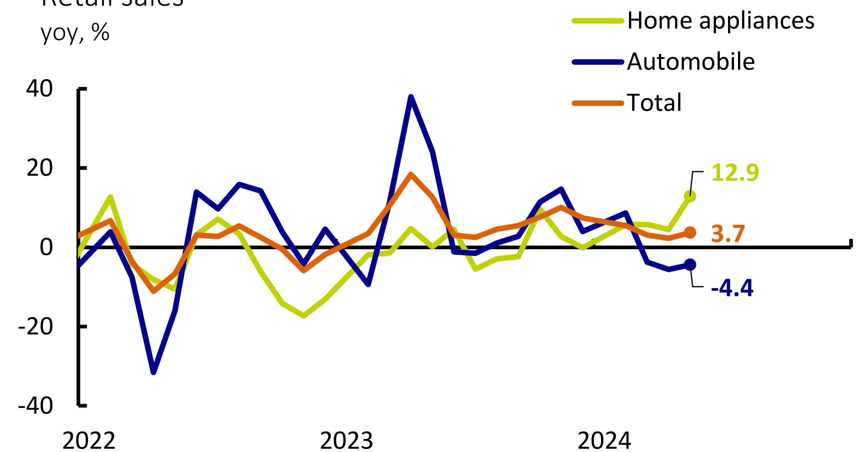


Source: CEIC and AXA IM Research, June 2024

Some upside consumer surprises, but generally subdued

Retail sales

yoy, %



Source: CEIC and AXA IM Research, June 2024

Unbalanced growth is the theme of the year

China

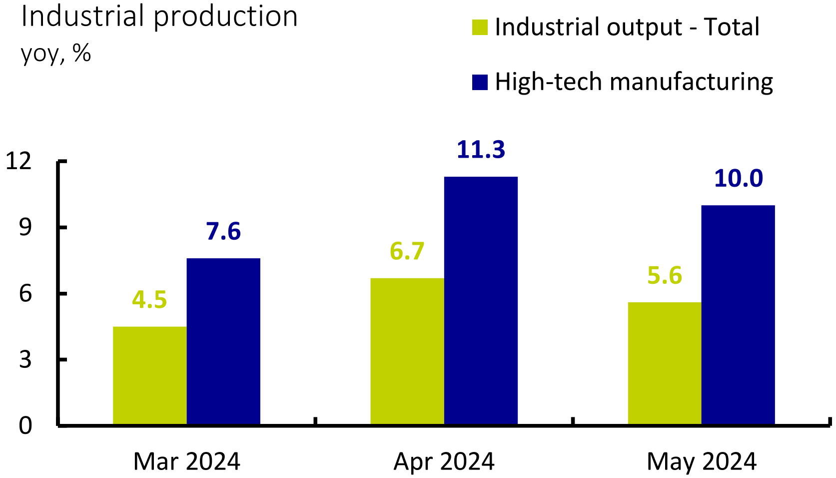
Investment-led growth emerging in resilient industrial production

- China's manufacturing sector has seen significant growth in fixed asset investment this year, materialising in resilient industrial production, particularly in high-tech manufacturing. This aligns with Beijing's strategy for the year. However, the persistent weakness in domestic demand, contrasted with strong momentum in manufacturing, increases reliance on exports for growth.
- Following the US, the European Union announced tariff hikes on Chinese electric vehicles from 10% to up to 38.1% earlier this month. This move highlights rising protectionism in the West and adds hurdles to China's export growth strategy.
- As the external environment becomes more complicated, it becomes increasingly urgent for China to rebalance its economy towards domestic demand—a process that had made some progress until COVID-19 altered the trajectory in 2020. In the near term, Beijing is likely to continue focusing on investment-driven growth to achieve its economic goals. In the longer-term, it remains increasingly unclear whether a consumer rebalancing still aligns with Beijing's long-term interests.

High-tech manufacturing kept production high

Industrial production

yoy, %

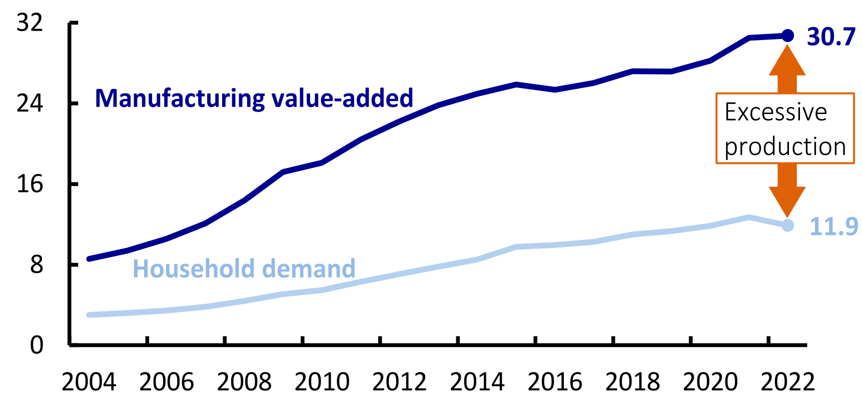


Source: CEIC and AXA IM Research, June 2024

Excessive production means excessive reliant on exports

China's share to the world

%



Source: CEIC and AXA IM Research, June 2024

We are cautious, given the weakness in growth

Japan

GDP still weak in Q1, despite upward revisions

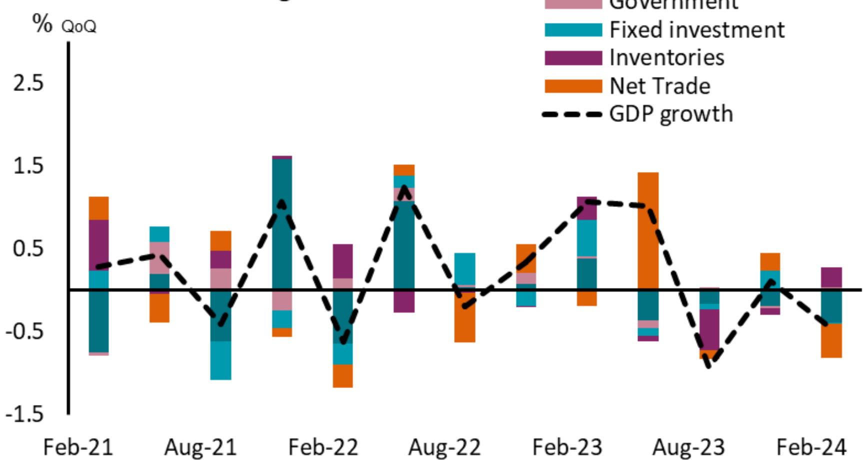
- Q1 GDP was weak, despite the upward revision in the second estimate; activity fell by 1.8% annualised (first estimate -2%). That did reflect several one-off factors, including a temporary shutdown at auto producers. But private consumption and capex were both down a quarterly 0.7% and 0.4%, respectively. A modest rebound over the rest of the year is on the cards, as real incomes start to recover on the back of the Shunto wage negotiations, supporting consumption. But if households choose to increase saving, or if rising prices caused by a weaker yen weigh on spending, the economy may remain in the doldrums.

The outlook is more upbeat, but we doubt the BoJ will hike aggressively

- The BoJ have outlined that they think the neutral rate hovers somewhere around 1%, so further hikes this year look likely. We have two further 10bp hikes to the short-term policy rate pencilled in for Q3 and Q4.

Broad-based weakness in Q1

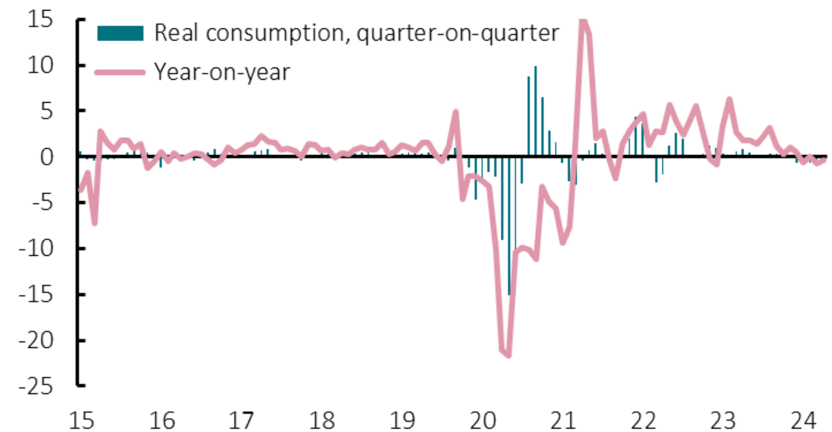
Contributions to QoQ growth



Source: Cabinet Office, AXA IM Macro Research, June 2024

Consumption should rebound in Q2, as real wages start to rise

Consumption Activity Index



Source: Bank of Japan, AXA IM Macro Research, June 2024

Bank of Japan will taper bond purchases

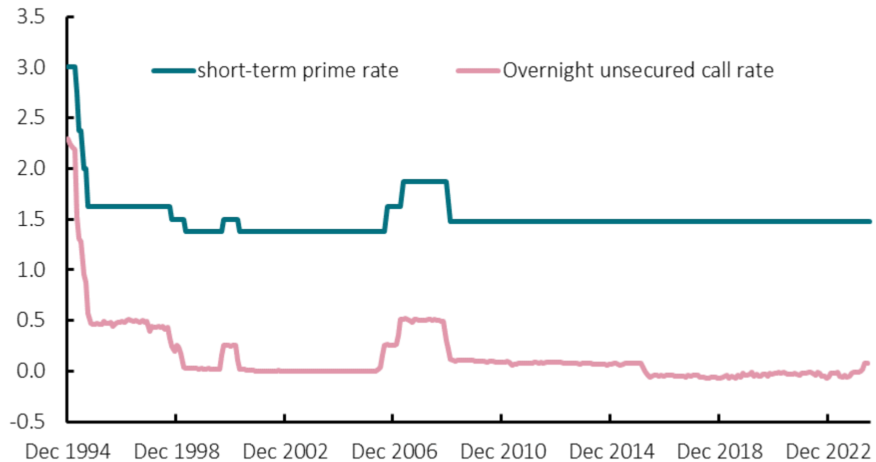
Japan

Policy was unchanged at April's meeting

- The Bank of Japan (BoJ) voted unanimously to keep the uncollateralised call rate between 0% and 0.1% at its meeting in June. The board also voted (8-1) to outline a detailed plan on the future path for JGB purchases over the next one to two years at its July meeting to "ensure that long-term interest rates would be formed more freely in financial markets".
- The BoJ stated that it would maintain monthly purchases of around ¥6tn in the interim, while it gathered views from market participants, including commercial banks and securities firms.
- Market participants had expected guidance on the immediate tapering of bond purchases at its June meeting, so the delay highlights the ongoing caution among Board members.
- The minutes were slightly more hawkish, with one policymaker pushing for a hike in the policy rate "without too much delay".

BoJ voted to keep uncollateralised call rate between 0% and 0.1%

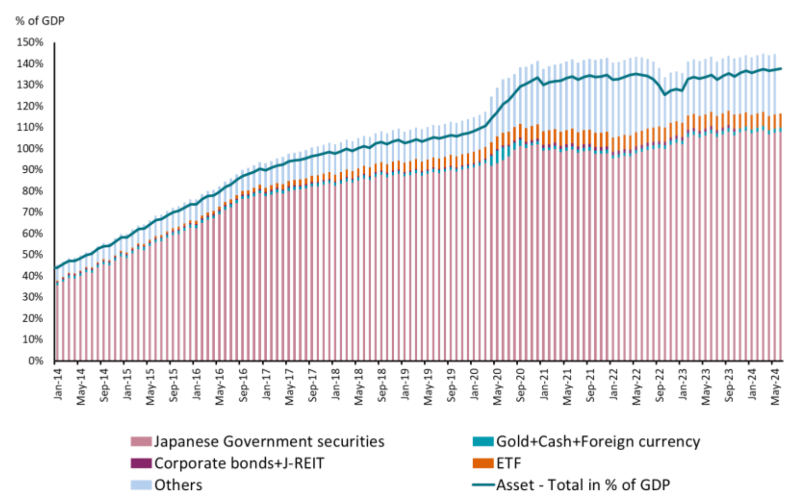
Japan - Prime and overnight rate



Source: Refinitiv, AXA IM Research, June 2024

BoJ plans to taper its massive bond purchase programme

Bank of Japan's Balance sheet- Assets



Source: Bank of Japan, AXA IM, June 2024

Investment Managers

Growth appears on a firmer footing

Canada

Early momentum to persist

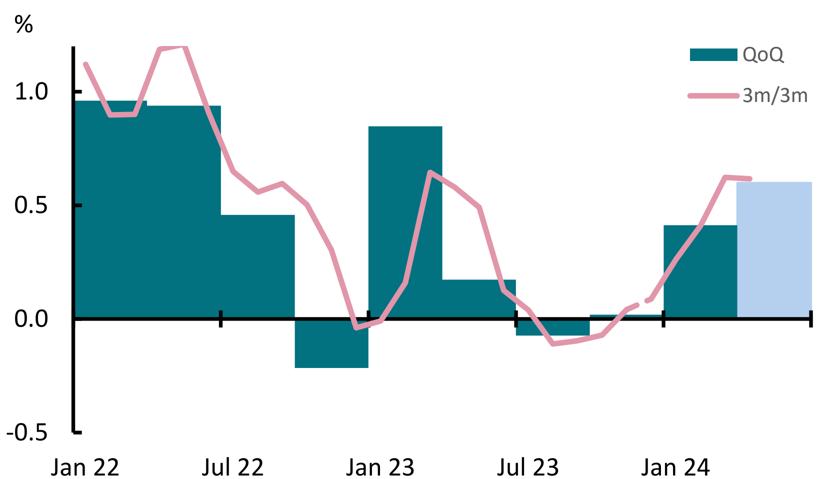
- Q1 GDP rebounded from a weak H2 2023. This was underpinned by a solid quarter for consumer spending, which we expect to persist as real disposable income rises, and ongoing mortgage headwinds soften. We expect investment to gradually recover this year, but the outperformance in exports to fade. We edge our annual forecasts higher to 1.3% this year (from 1.2%) and 1.8% next (from 1.7%). Consensus estimates are 1.0% and 1.8%, with a stronger BoC outlook of 1.5% and 2.2% respectively.

Labour market in better balance

- Unemployment has gently increased to 6.2% – a 3½ year high – while vacancies have fallen back towards pre-pandemic levels as a % of unemployment. However, much of this has been driven by stronger labour supply, with the average employment gain to date outpacing the average increase of 2022 and 2023. Earnings growth should ease more visibly across H2 2024, which will help the inflation outlook. We forecast inflation to average 2.5% in 2024 and 2.6% in 2025. Still a little above target.

Firmer GDP momentum to persist

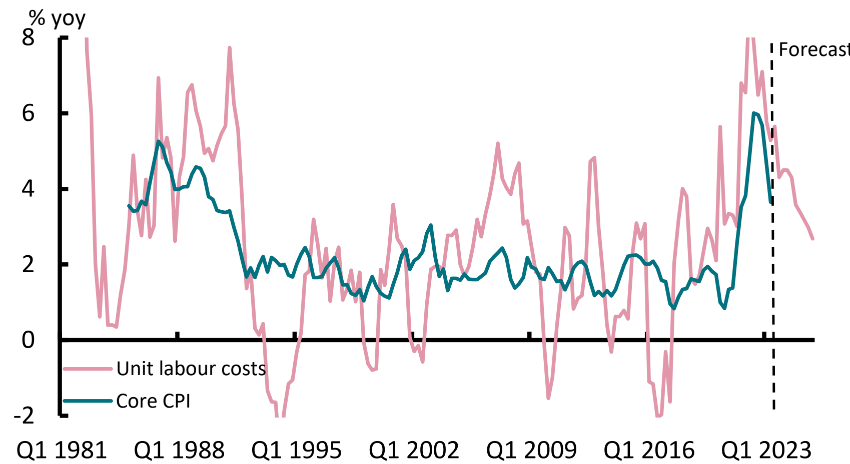
Canadian GDP monthly and quarterly releases



Source: CANISM, AXA IM Research, June 2024

Labour costs point to softer core inflation

Unit labour costs and core CPI



Source: CANISM, AXA IM Research, June 2024

BoC poised but patient

Canada

Spare capacity conundrum

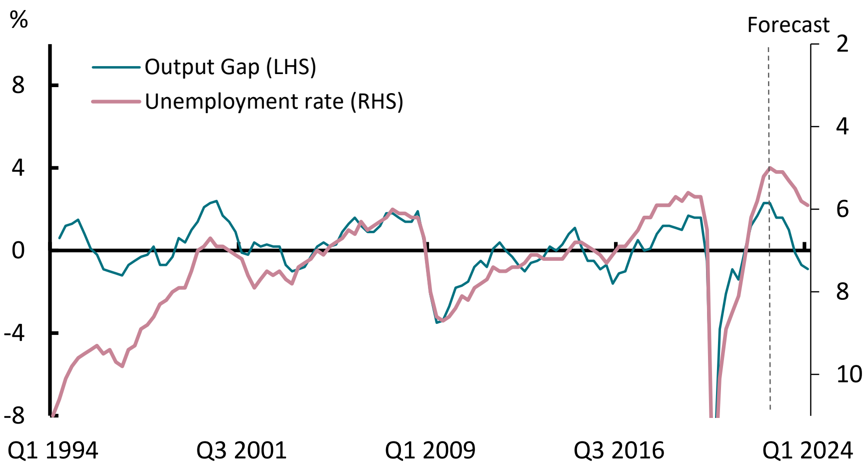
- The BoC estimates the economy in excess supply, consistent with further declines in inflation towards target. BoC output gap estimates certainly suggest modest spare capacity. However, the unemployment rate (and other metrics of labour market capacity) suggest a less tight market, but perhaps not one that is loose. A sharp fall in productivity growth explains most of the divergence in the two measures. The BoC forecasts a decent rebound in productivity; we are less convinced.

BoC embarks on (early) gradual easing path

- The BoC cut rates by 0.25% in June to 4.75%, a little sooner than our forecast July cut. We continue to envisage a further two cuts this year (now July and October), taking the policy rate to 4.25% by year-end. We see a continued quarterly pace of cuts until next summer, leaving the policy rate at 3.50% by end-2025. This would remain in restrictive territory by the BoC estimates (2.25-3.25% estimate of neutral) and is consistent with inflation still a little above target in 2025.

Different gauges of spare capacity

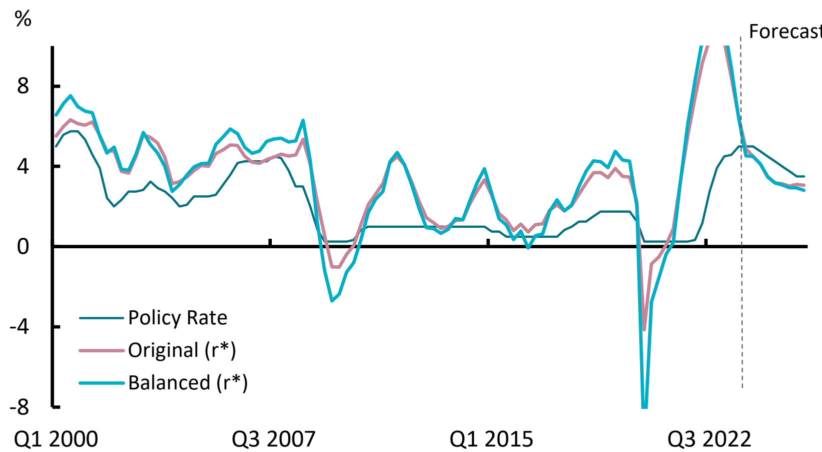
Output gap and unemployment



Source: BoC, CANISM, AXA IM Research, June 2024

BoC embarks on gradual easing

Taylor Rules and BoC policy rate



Source: BoC, Bloomberg, AXA IM Research, June 2024

AXA Investment Managers

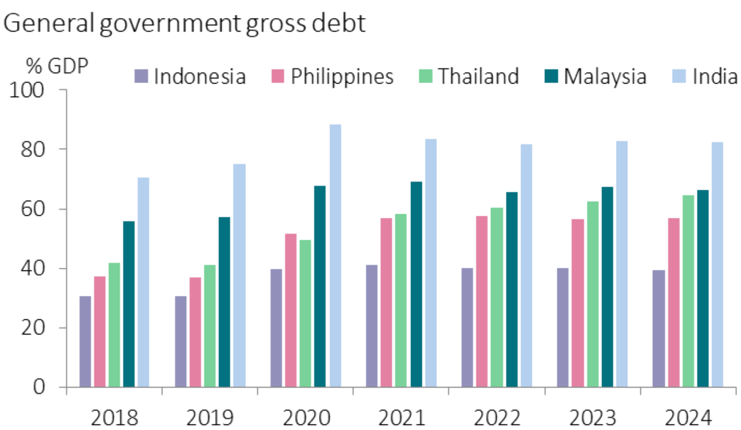
Populism versus prudence, a challenging balancing act

EM Asia ex-China

Risks of fiscal loosening heighten

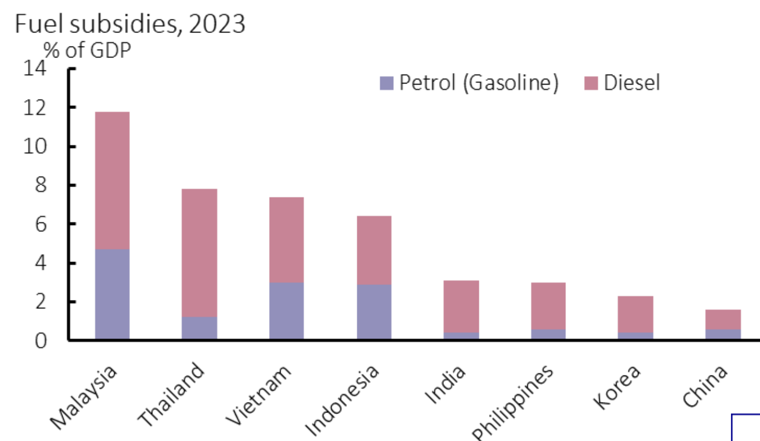
- In recent policy meetings, central bankers have remained cautious, showing no urgency to ease policy until inflation is under control. However, on the fiscal policy side, recent developments have highlighted a risk of prudency giving way to populism.
- In India, Modi's recent failure to maintain a strong parliamentary majority could see a backsliding on previous fiscal consolidation commitments, instead favouring spending and redistribution policies. The final budget for 2024/25 FY will be announced in July.
- Indonesia has a favourable track record on fiscal discipline, adhering to a fiscal rule capping its deficit at 3% of GDP. However, its finances could be stretched in the coming years, as President Elect Subianto is expected to proceed with an election pledge to provide free school meals, costing up to 2% of GDP annually.
- Thailand's prime minister Thavisin proposed an expansionary budget for 2024/25 fiscal year, with a deficit of 4.4% of GDP, and proceeds with plans to deliver his generous flagship "digital wallet" scheme, a digital cash handout equivalent ~3% of GDP.
- Malaysia's government is having to follow a different script, reducing its hefty subsidies program. Highlighting the challenging fiscal policy balancing act, these subsidy cuts are necessary and fiscally prudent, but they have not been popular, and more painful (and unpopular) cuts are planned for petrol (gasoline) subsidies later this year.

India's high debt means it can ill afford major fiscal loosening



Source: International Monetary Fund and AXA IM Research, June 2024

Malaysia has started to reduce its large subsidies bill



Source: International Monetary Fund and AXA IM Research, June 2024

Central banks visibly more cautious

EM Europe

Worried about upside risks to inflation, sticky services inflation, high wage growth…

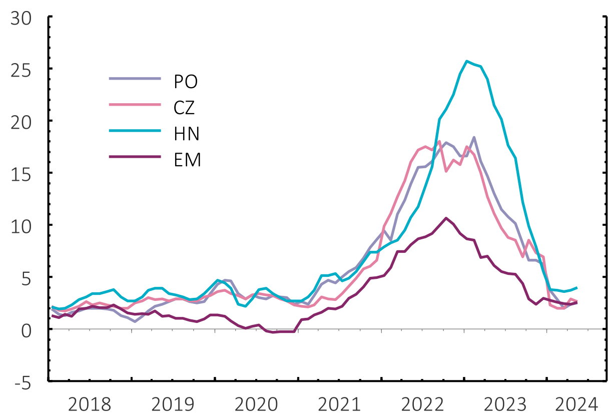
- The mix of worries varies among CEE central banks, but all become more cautious. Monetary easing started last year: Sept 2023 for Poland, Oct 2023 for Hungary and Dec 2023 for the Czech Republic; and has now delivered a cumulative 100bp, 600bp and 175bp cuts respectively taking policy rates to 5.75% for Poland, 7% in Hungary and 5.25% in the Czech Rep. These cuts came along a sharp disinflation process which saw inflation rates come off their peaks – having reached 18.4% in Poland, 25.7% in Hungary, 18% in the Czech Rep. Inflation in May was 2.5% in Poland, 2.6% in Czechia and 4% in Hungary, but will face upward pressures into H2 as base effects reverse and services prices resistance remains. The scope for further cuts appears more limited into H2.

… and a more complicated external environment

- The geopolitical context has also become less favourable. Increased FX volatility push central banks to focus on an interest rate differential with the Eurozone, but also with the Fed, whose hesitation towards easing appears to have been included in their reaction function. We see scope easing by the Czech CNB while Poland and Hungary may stay on hold until year-end.

Past dis-inflation will encounter resistance into H2

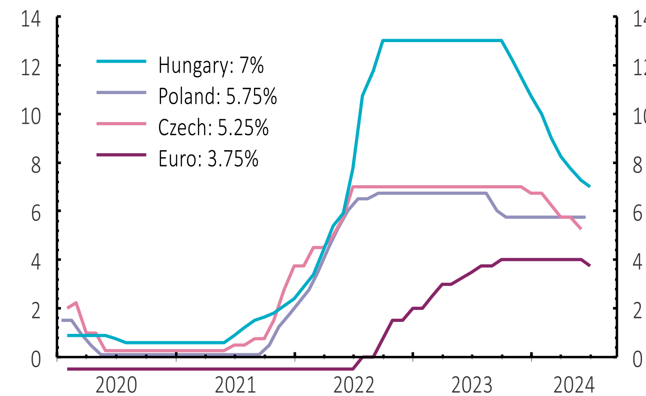
CEE inflation rates vs Eurozone



Source: LSEG Datastream and AXA IM Research May 24

Limiting potential for rate cuts until year-end

CEE CB policy rates (%), Jun 24



Source: LSEG Datastream and AXA IM Research Jun 24

Fiscal issues and hawkish pivots

Latin America

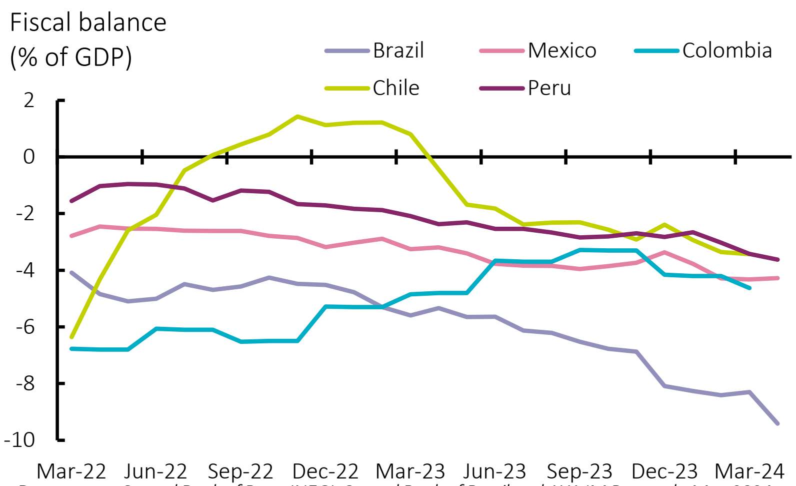
Challenging fiscal targets

- Countries in the region are struggling to manage their finances as fiscal deficits grow, exacerbated by decelerating economic growth, the rescue of state-owned enterprises, and political challenges. Brazil, in particular, faces a rapidly worsening deficit, now at 9.4% of GDP (for the consolidated public sector). Efforts to address this through revenue-enhancing measures have stalled in Congress, with President Lula also resisting calls for spending cuts.

Hawkish pivot

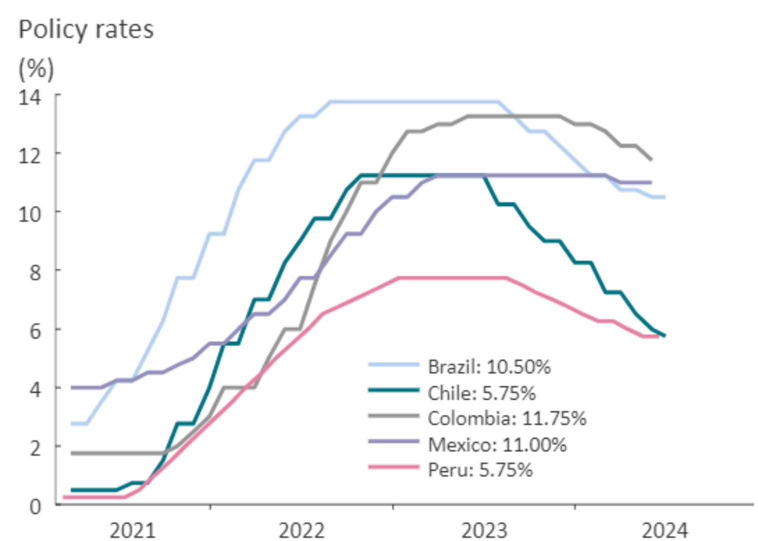
- Central banks are adopting a more cautious stance amidst ongoing uncertainty over the timing of the Fed's easing cycle and mounting fiscal pressures. Brazil stood on hold at 10.5% in a unanimous decision, accompanied by a hawkish policy statement that did not provide explicit forward guidance but indicated an alternative scenario where rates could remain unchanged for the foreseeable future. Meanwhile, Chile cut rates by 25 bps to 5.75%, but its central bank issued a hawkish statement suggesting that the current policy rate level has likely exhausted most planned cuts for the year, signaling an imminent end to Chile's easing cycle.

Deficits have worsened since the beginning of the year



Datastream, Central Bank of Peru, INEGI, Central Bank of Brazil and AXA IM Research, May 2024

Pauses and slower pace across the region



Source: LSEG Datastream and AXA IM Research, Jun 24

Forecasts & Calendar

Macro forecast summary

Forecasts

Real GDP growth (%)	2023	2024*		2025*	
	AXA IM	AXA IM	*Consensus*	AXA IM	*Consensus*
World	3.2	3.2		3.1	
Advanced economies	1.7	1.5		1.4	
US	2.5	2.4	2.4	1.6	1.8
Euro area	0.5	0.6	0.6	1.1	1.5
Germany	0.0	0.1	0.2	0.9	1.5
France	0.9	0.8	0.8	1.0	1.3
Italy	1.0	0.7	0.8	0.7	1.2
Spain	2.5	2.4	2.0	2.1	1.9
Japan	1.9	0.6	0.5	1.1	1.0
UK	0.3	0.7	0.5	1.1	1.2
Switzerland	0.8	1.2	1.2	1.3	1.5
Canada	1.1	1.3	1.1	1.8	1.9
Emerging economies	4.1	4.2		4.2	
China	5.2	5.0	4.9	4.2	4.4
Asia (excluding China)	5.3	5.4		5.3	
India	7.7	6.8	6.8	6.5	6.6
South Korea	1.4	2.5	2.5	2.6	2.2
Indonesia	5.0	5.1	4.9	5.1	5.1
LatAm	2.3	2.0		2.4	
Brazil	2.9	2.2	1.9	1.9	2.0
Mexico	3.2	2.2	2.2	1.4	2.2
EM Europe	3.0	3.0		2.9	
Russia	3.6	3.2	2.6	1.8	1.1
Poland	0.2	2.8	2.9	3.5	3.4
Turkey	4.3	3.0	2.6	3.6	3.2
Other EMs	2.2	2.9		4.2	

Source: Datastream, IMF, Bloomberg and AXA IM Macro Research – As of 25 June 2024
**Forecast*

Expectations on inflation and central banks

Forecasts

Inflation Forecasts

CPI Inflation (%)	2023	2024*		2025*	
	AXA IM	AXA IM	*Consensus*	AXA IM	*Consensus*
Advanced economies	4.7	2.8		2.3	
US	4.1	3.3	3.2	2.5	2.3
Euro area	5.5	2.5	2.3	2.2	2.1
China	0.2	0.6	0.7	1.6	1.9
Japan	3.3	2.5	2.5	1.9	1.5
UK	7.3	2.4	2.5	1.8	2.0
Switzerland	2.1	1.4	1.3	1.4	1.3
Canada	3.9	2.5	2.5	2.6	2.0

Source: Datastream, IMF, Bloomberg and AXA IM Macro Research – As of 25 June 2024
**Forecast*

Central banks' policy: meeting dates and expected changes

Central bank policy Meeting dates and expected changes (Rates in bp / QE in bn)		Current	Q3-24	Q4-24
United States - Fed	Dates	5.50	30-31 Jul 17-18 Sep	6-7 Nov 17-18 Dec
	Rates		-0.25 (5.25)	-0.25 (5.00)
Euro area - ECB	Dates	3.75	18 Jul 12 Sep	17 Oct 12 Dec
	Rates		-0.25 (3.50)	-0.25 (3.25)
Japan - BoJ	Dates	0 - 0.1	30-31 Jul 19-20 Sep	30-31 Oct 18-19 Dec
	Rates		+0.10 (0.1-0.2)	+0.10 (0.2-0.3)
UK - BoE	Dates	5.25	1 Aug 19 Sep	7 Nov 19 Dec
	Rates		-0.25 (5.00)	-0.25 (4.75)
Canada - BoC	Dates	4.75	24 Jul 4 Sep	23 Oct 11 Dec
	Rates		-0.25 (4.50)	-0.25 (4.25)

Source: AXA IM Macro Research - As of 25 June 2024

Calendar of events

2024	Dates	Events	Comments
June	27-Jun	1st US TV debate	
	27-28 Jun	European Council	
	30-Jun	France elections (round 1)	
	30-Jun	BoE MPC member & Deputy Governor Ben Broadbent's term ends	
July	04-Jul	UK General Elections	
	07-Jul	France elections (round 2)	
	15-18 Jul	US: Republican Convention	
	18-Jul	ECB meeting	unch (3.75%)
	24-Jul	BoC meeting	-25bps (4.50%)
	30-31 Jul	BoJ meeting	unch (0-0.1%)
	30-31 Jul	FOMC meeting	unch (5.50%)
August	01-Aug	BoE meeting	-25bps (5.00%)
	19-22 Aug	US: Democrat Convention	
	22-24 Aug	Fed's Jackson Hole symposium	
September	04-Sep	BoC meeting	-25bps (4.75%)
	06-Sep	Italy: Macro assumptions for 2025 draft budget	
	10-Sep	2nd US TV debate	
	12-Sep	ECB meeting	-25bps (3.50%)
	17-18 Sep	FOMC meeting	-25bps (5.25%)
	19-Sep	BoE meeting	unch (5.00%)
	19-20 Sep	BoJ meeting	+10bps (0.1%-0.2%)
	25-Sep	France government to present draft 2025 budget	
October	17-Oct	ECB meeting	unch (3.50%)
	23-Oct	BoC meeting	-25bps (4.25%)
	Before 24 Oct	Austria General Elections	
	30-31 Oct	BoJ meeting	unch (0.1%-0.2%)
November	05-Nov	US Presidential Elections	
	6-7 Nov	FOMC meeting	unch (5.25%)
	07-Nov	BoE meeting	-25bps (4.75%)
December	11-Dec	BoC meeting	unch (4.25%)
	12-Dec	ECB meeting	-25bps (3.25%)
	17-18 Dec	FOMC meeting	-25bps (5.00%)
	18-19 Dec	BoJ meeting	+10 bps (0.2%-0.3%)
	19-Dec	BoE meeting	unch (4.75%)

Latest publications

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21 June 2024

India's economy: A compelling growth and investment story but challenges remain

11 June 2024

Eurozone corporate profits outlook: How they could influence the ECB

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Mexico's General Elections: Continuity likely but headwinds ahead

21 May 2024

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2 May 2024

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26 April 2024

April Op-Ed - Looking outside the West

26 April 2024

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