Investment Institute Macroeconomics

Outlook 2024-25

Mid-cycle adjustment, not end-cycle crash

AXA IM Research

November/December 2023

Summary: Outlook 2024 & 2025

Mid-cycle adjustment, not end-cycle crash

- Advanced economies look likely to soften next year, from solid growth in the case of US, Japan and Canada as policy tightening weighs, or to remain lacklustre, as likely in the Eurozone and UK. In most cases we expect recession to be avoided, but this will be close in several economies.
- Emerging markets posted a resilient 2023. For EM overall, we forecast a modest improvement in 2024, despite a weakening in key international economies. However, most regions are likely to see divergent trends for different economies, several larger EMs look likely to soften next year.
- Overall global growth should soften to 2.8% in 2024 – an ex-pandemic low – but accelerate to 3.0% in 2025.
- Inflation has fallen back in headline terms across advanced and emerging economies, in all cases in part thanks to central bank policy tightening, although food and energy price disinflation has dominated and core disinflation has been slower in all regions. This process should continue over the forecast horizon, with most advanced economies only achieving central bank mandates in 2025
- Inflation improvement and a weakening growth outlook should usher in looser monetary policy across many regions, advanced and emerging, with the latter already seeing the start of an easing cycle. However, with growth expected to avoid sharp retracement, central banks are likely to have to leave policy in restrictive territory to ensure core disinflation to mandate consistent levels in 2025.
- Cyclical uncertainty persists with several economies threatening recession. However, we do not consider most economies severely imbalanced and forecast an acceleration in growth if they can withstand the lagged impact of recent central bank tightening.
- Geo-political risks remain elevated with marked uncertainty over whether Israel’s conflict with Hamas will escalate with broader regional implications and ongoing risks of escalation in Russia’s invasion of Ukraine.
- A heavy political year with 2bn people going to the polls will add to geopolitical tensions, none more than the US Presidential election in November 2024.

Investment Strategy: risky assets still in a constructive mood

- Rates: This year, two types of rise in nominal rates have been identified with real rates taking over from inflation expectations by March. While monetary policy appears to be fairly restrictive, fiscal policies are sowing doubts. Moving forward, the bond yields are clearly encouraging carry for next year.
- Equities: The relationship between the discount rate and share prices seems to us to be insufficient, and it is important to take into account the sanctity of companies' balance sheets and their ability to provide visibility on their business. Optimism about earnings growth seems high to us.
- FX: Our outlook of high-for-longer rates should mean the USD rate differential advantage persists. This adds to historic experience to suggest that a Fed peak need not equate to a USD peak, albeit that steady yields should mean a steady, not rising dollar. This applies to the yen too.

Central scenario

Summary – Key messages

Our central scenario: Global economy to slow, several adv economies on brink of recession

We forecast global growth to slow to 2.8% in 2024 and 3.0% in 2025.

Inflation to slow gradually further, most to achieve central bank mandates only in 2025.

Inflation

Headline inflation to resume disinflation in 2024, but slower than 2023. Disinflation likely to be more obvious in core.

Monetary policy

Most central banks now appear at peak. DM rate cuts likely only from mid-2024. But loosening to ease real rate restrictiveness, not add significant stimulus

Growth

Growth slows. We do not forecast recession in the advanced economies – although it is likely to be close in some.

Fiscal policy

US fiscal spending to slow across 2024, European economies to see less loose policy. Some EM's to see subsidies end.

Rates

10-year yields should soften further as central banks begin to ease policy. However, term premia rise to limit overall retracement.

Emerging Markets

Growth to soften in major EM economies, but unchanged across region as a whole. Inflation easing slows, focus more on core.

Equities

The stabilisation of long-term interest rates improves the visibility of the prospects for companies despite higher interest rates. However, we feel that the consensus is too optimistic regarding earnings in 2024.

FX

The eventual softening of US has reversed dollar gains. A soft-landing would suggest reversal is overdone.

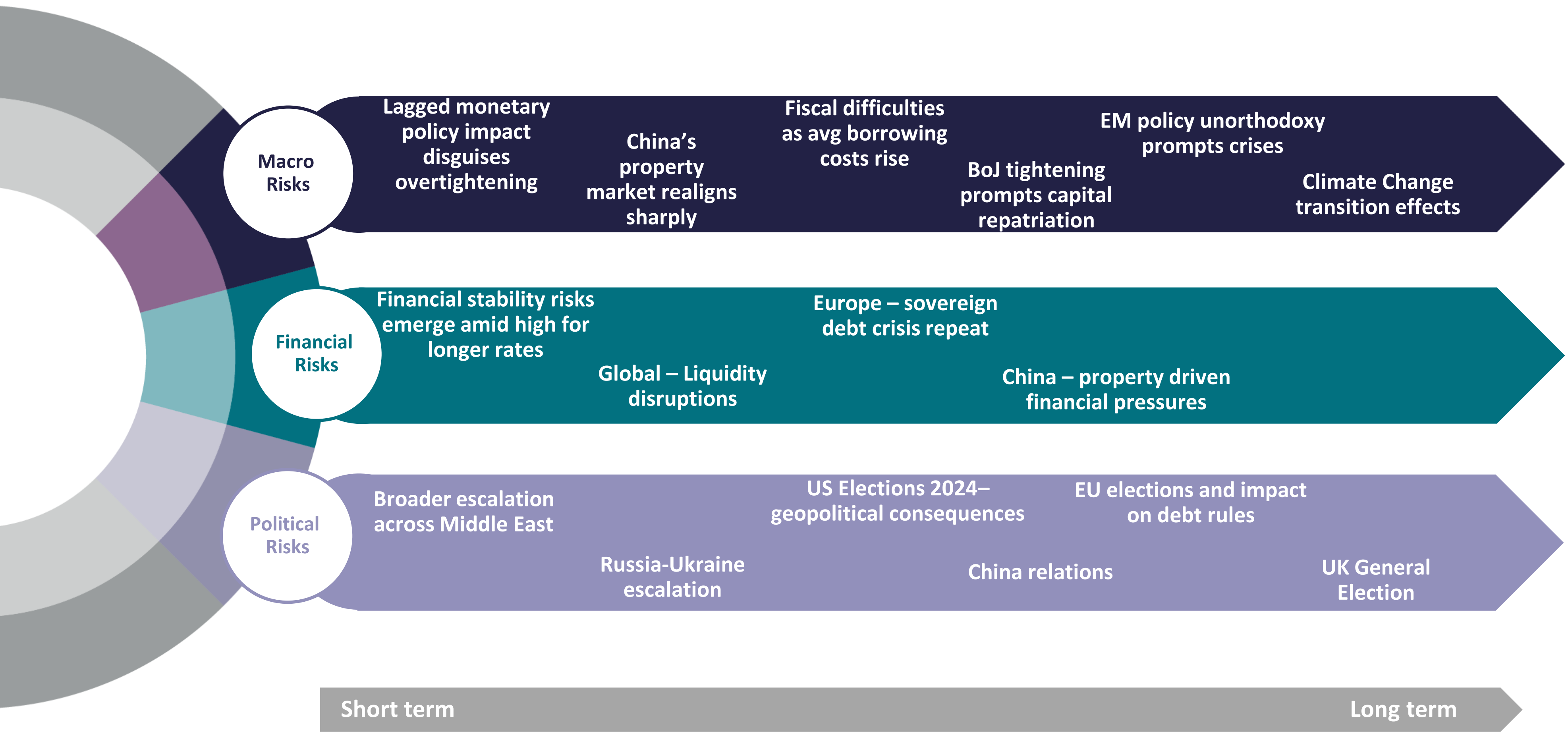
Alternative scenarios

Summary – Key messages

	Recessions Probability 20%		Continued resilience Probability 20%
What could be different?	- Banking turmoil escalates, credit conditions tighten. - Escalation in Ukraine conflict or Middle East tensions - Lags disguise scale of central bank tightening – growing impacts lead to sharper slowdown, suggesting overtightening - COVID outbreaks spreads again: China and/or new mutations		- Geo-political tensions ease, in Ukraine, Middle East and with China. - Consumers spend more excess saving, borrowing offsets income hit. - Investment boost on firmer outlook, AI and climate change. - Productivity boost following investment rebound and structural post-pandemic adjustments
What it means	- Growth weaker, employment starts to fall, labour markets loosen - Inflation falls more quickly, subject to supply disruption re-emerging - Central banks forced into a quicker loosening of monetary policy		- Growth continues to surprise on the upside in most regions - Inflation falls less quickly, in both core and headline terms. Improving productivity may dampen this effect - Monetary policy stays elevated for longer, envisaged cuts delayed
Market implications	- Risk appetite deteriorates / equities sell off / credit widens - Sovereign yields reprice lower, credit spreads widen - Dollar rises on reduced risk appetite - EM struggles with capital outflows		- Risk-on environment, equities make further gains, growth retains lead over value - UST softens, yields rise; EUR strengthens modestly - Spreads grind tighter

RISk Radar

Summary – Key messages



Contents

Theme of the Month

Summary Outlook 2024 and 2025

Global

Global growth to slow to ex-pandemic low

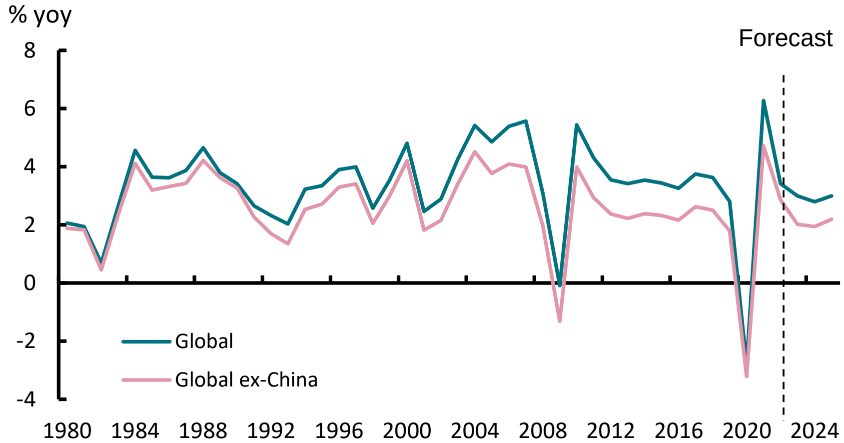
- Amidst significant geo-political risks, we expect deceleration in advanced economies as monetary tightening weighs more obviously, forecasting slowing in the US, Eurozone, Japan and UK. We expect global economic activity to soften, despite forecasting a modest quickening in EM economies to 4.0% from 3.9%. We forecast global GDP slowing to 2.8% in 2024. Excepting the global pandemic, this would be the (joint) weakest growth since 2009. Modest acceleration in 2025 should see growth pick-up to 3.0%, still below the 3.7% average growth rate 2010-19 (although ex-China this would be closer at 2.2% vs 2.5%).

Central banks to lower rates, but policy likely stays restrictive

- Softer growth and gradual taming of inflation should see a loosening in central bank policy in 2024 (continued easing in the case of some EM markets). In most cases, however, policy loosening looks set to be gradual with only a modest adjustment in real rates as central banks likely require still restrictive policy to return core measure of inflation to central bank mandate consistent territory.

Global growth to soften, but avoid recession

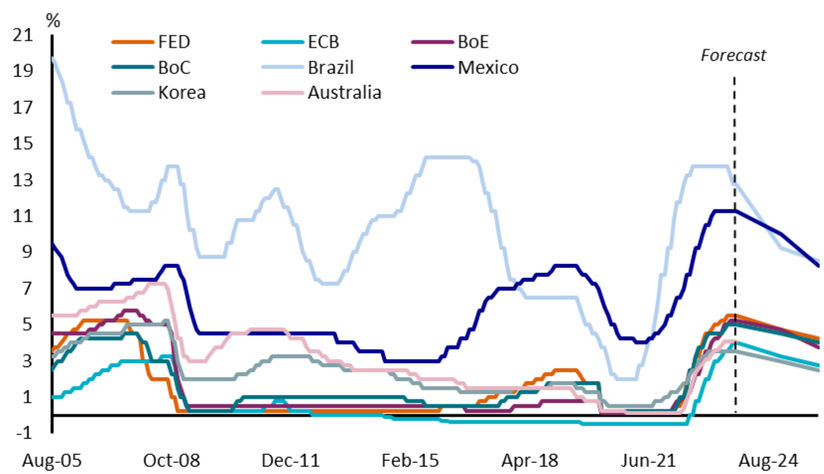
Global GDP (inc and ex China)



Source: IMF, AXA IM Research, Nov 2023

Central banks set to loosen policy, but maintain restrictiveness

Central Bank Policy Rates



Source: AXA IM Research, Nov 2023

Summary Outlook 2024 and 2025

US

Expect slowdown, avoid recession

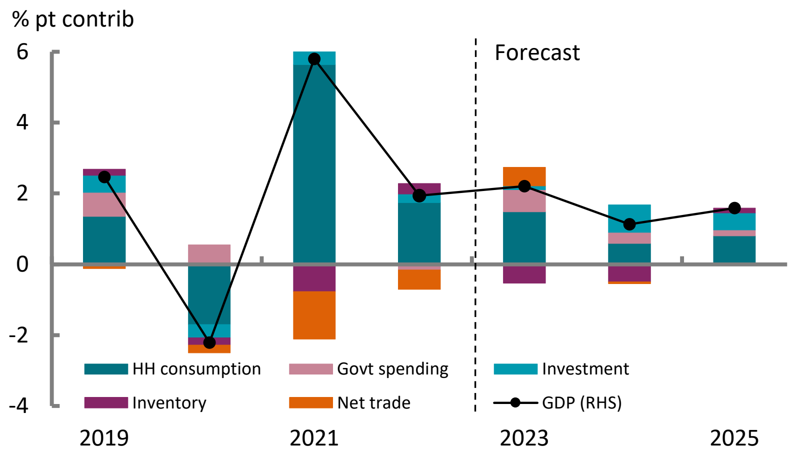
- We expect the final stage of economic deceleration in the household sector – resilient through 2023. This slowdown, having been deferred through a combination of solid real income growth and excess savings, should materialise as other sectors of the economy now look on firmer ground. The US has slowed by instalments. This should avoid outright recession, although we expect below trend growth over the coming quarters to see GDP slow to 1.1% in 2024 and 1.6% in 2025 from an expected 2.3% in 2023.

Inflation to hit Fed target in 2025, but little room for manoeuvre

- We forecast disinflation to continue at a slower pace in headline terms, but driven proportionally more by core disinflation. We forecast CPI inflation to average 3.2% in 2024 and 2.7% in 2025 (from an expected 4.2% in 2023). PCE inflation is likely to be lower than CPI over the coming years and we forecast this falling to the Fed's target in 2025. However, we forecast PCE inflation to close 2025 marginally above target, suggesting the Fed will need to be cautious in how far it reverses restrictive policy.

Household sector to slow, weighing on overall activity

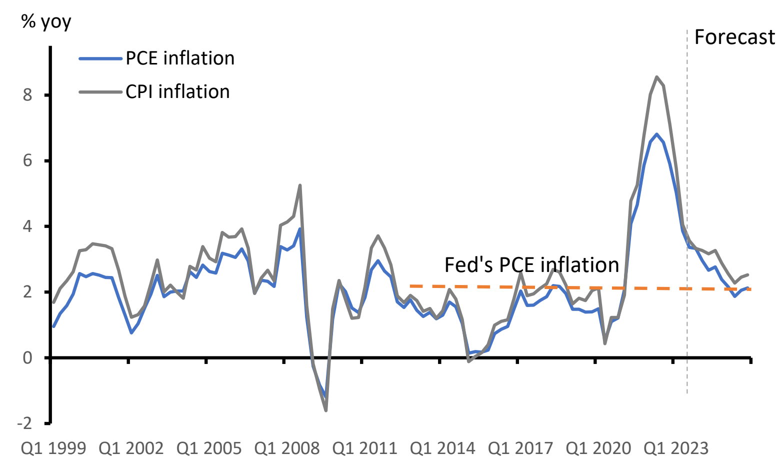
US contributions to growth



Source: BEA, AXA IM Research, Oct 2023

Inflation forecast to return to target in 2025

Headline PCE and CPI inflation measures



Source: BLS, BEA, AXA IM Research, Nov 2023

Summary Outlook 2024 and 2025

Euro area

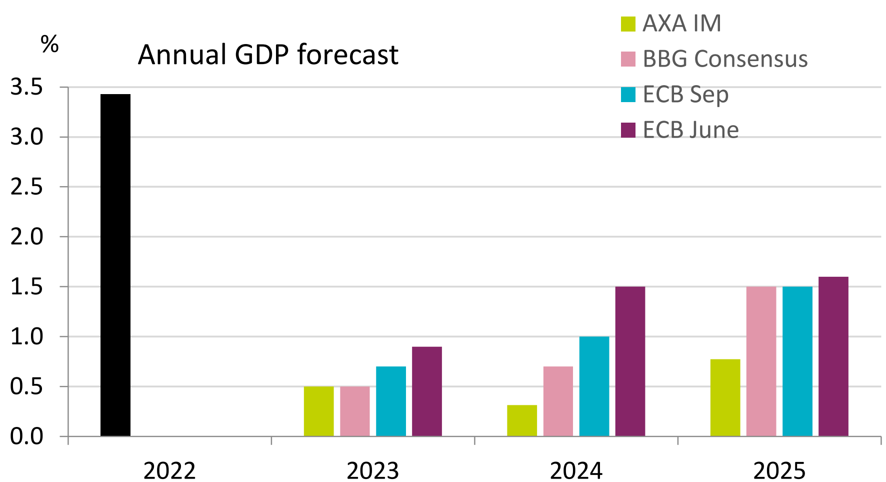
Weak growth, inflation to land at 2% in mid 2025

- We maintain our below consensus growth outlook, projecting eurozone GDP to grow by 0.3% and 0.8% in 2024 and 2025 after 0.5% in 2023, essentially driven by household consumption supported by increasing real incomes.
- Euro area headline inflation should come down to 2.7% and 2.2% in 2024 and 2025 from 5.5% this year. Core disinflation is likely to be more limited, edging to 3% in 2024 from 5% this year. We project it to remain above 2% throughout 2025, averaging 2.3%.

Rate cuts: no earlier than summer 2024

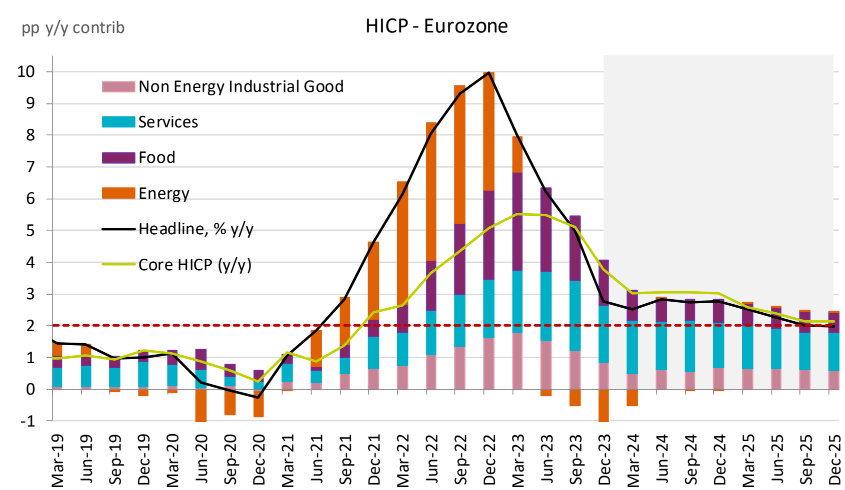
- The ECB's balance sheet is likely to be the main focus over the next six months with a PEPP reinvestment policy and operational framework review. On PEPP, we see a decision this winter starting with partial roll-off in H2 24, market conditions dependent.
- We foresee ECB rates cuts likely to come during the summer, later than current market pricing. Our below consensus ECB growth forecast makes June our preferred option. Though mindful of what the Fed decides, September is also very likely.

We maintain our below-consensus view on growth



Source: ECB, Datastream, Bloomberg, AXA IM Research, November 2023

Core inflation to remain above 2% until end-2025



Source: Eurostat, AXA IM Research, November 2023

Summary Outlook 2024 and 2025

China

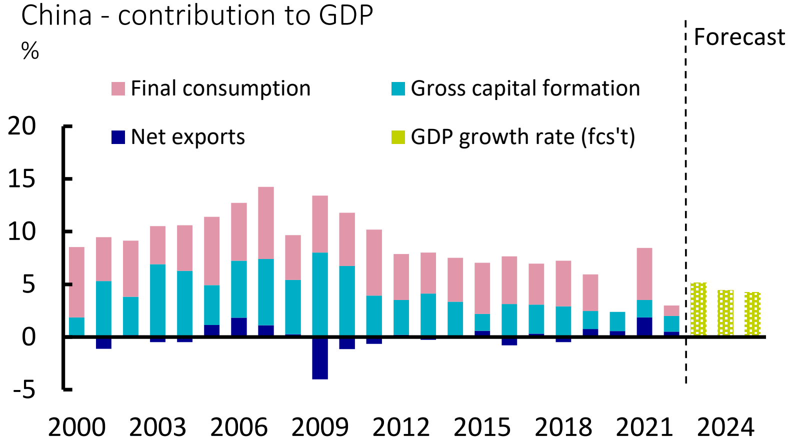
First year free of COVID-19 restrictions, but marked by scars

- 2023 endured a sluggish mid-year due to wavering confidence and delayed policy boosts. Stimulus helped quicken the pace in Q3.
- Next year is expected to grow at a faster quarterly pace, backed by supportive measures and eventually firmer external demand.
- But the economic upswing from announced stimuli looks set to fade into 2025 and could lead to future imbalances, requiring a potentially prolonged adjustment period.

The conventional remedial policy response returns

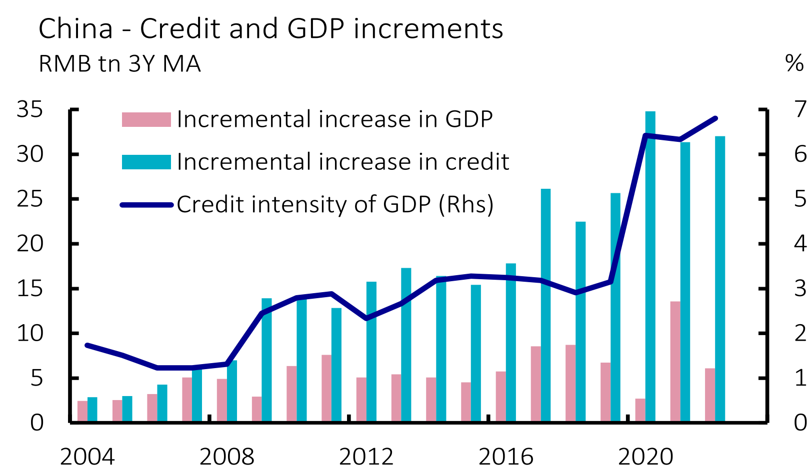
- Recent announcements from Beijing have indicated that stimulus-backed investment will be the way of boosting the economy, evident from the surprising mid-year budget revision and early issuance of local government special bonds.
- However, this method is becoming less efficient and adds to long-term challenges.

Policy supported 2024, impacts to fade in 2025



Source: CEIC, AXA IM Research, Nov 2023

Credit less efficient in producing GDP in recent years



Source: CEIC, AXA IM Research, Nov 2023

Summary Outlook 2024 and 2025

Emerging Markets

Tight international financial conditions not supportive for EMs…

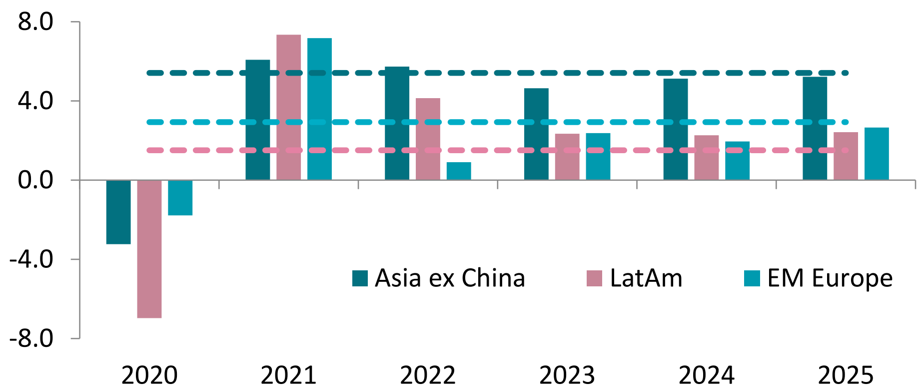
- Central banks may be more limited in terms of monetary policy easing. Disinflation, faster than initially thought, will allow an easing stance in 2024 in many EM economies. We remain wary of the Frontier market (FM) space, which has partially lost access to financial markets while debt service costs have has risen.

… but growth should still show resilience overall, despite inter- and intra- regional dispersion

- China's expected improved sequential growth should support improvement in external demand for many EMs, particularly in Asia. Meanwhile, disinflation will allow a better consumer backdrop, particularly in Central Europe where real wages growth is likely to turn positive after a tough 2023. We see significant dispersion in different countries' growth profiles in Latin America.
- EM ex-China growth should pick up from 3.3% in 2023 to respectively 3.7% and 4.0% in 2024/25, but much of this acceleration comes Asia and the smaller countries of various EM regions. GDP growth in 2025 is nonetheless still expected to remain below its post-GFC - pre-Covid averages in both Asia and EM Europe.

Growth to remain below last decade's averages by 2025

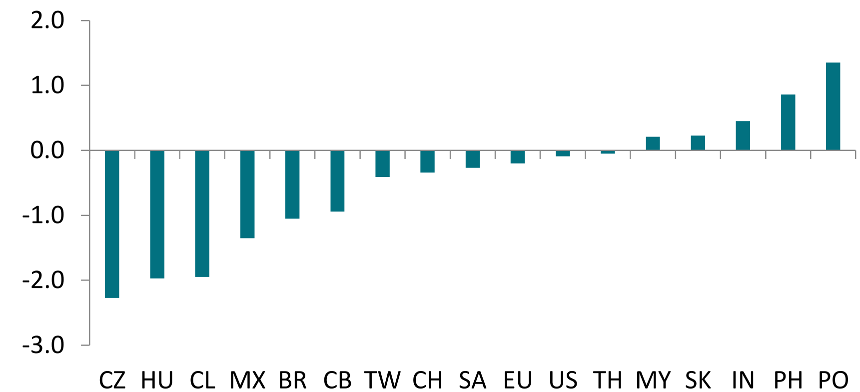
Annual real GDP growth in %
(2011-19 average in dotted lines)



Source: IMF, AXA IM Research, November 2023

Monetary policy stance expected to ease in many EMs

Ex-ante real policy rate change YE2024 vs YE2023 (%)
Market implied policy rates, consensus YE inflation rates



Source: Bloomberg, AXA IM Research, November 2023

Macro outlook

Slowdown by instalment

US

Consumer slowdown the final and most difficult stage of economic softening

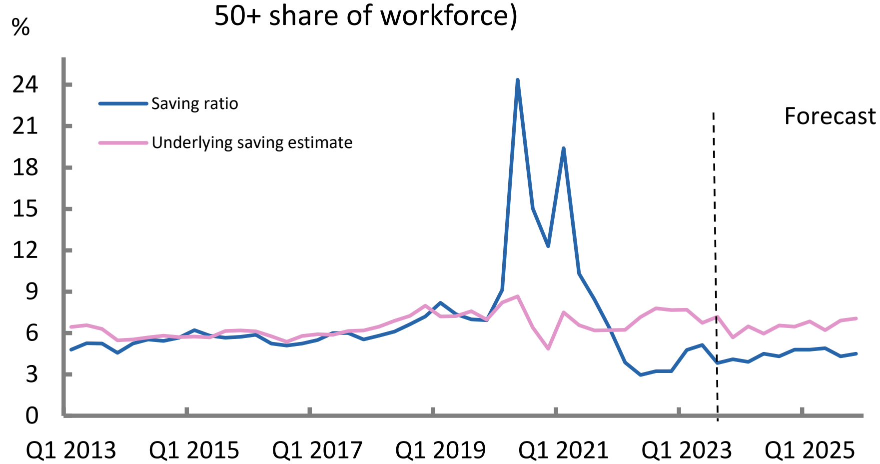
- We forecast a material slowdown in consumer spending as real income growth slows and most households have exhausted excess savings. These have provided a buffer and it is uncertain for how long they will continue to underpin higher-income household spending. This and borrowing provide ongoing upside consumer spending risks to our forecasts. We expect investment spending to continue at a solid pace, but should provide less of a boost than in 2023.

Inflation outlook increasingly dependent on labour market

- Our expectation for disinflation across 2024 and 2025 to be more concentrated in core items also reflects our outlook for the labour market. We expect unemployment to rise gently (peaking around 4.5%) and wage growth to slow to 3.5% by end-2025. However, over the forecast horizon, a softening in productivity growth could keep unit labour costs somewhat elevated, a challenge to reducing CPI back to target.

Excess savings have been a buffer, but should fade and could reverse

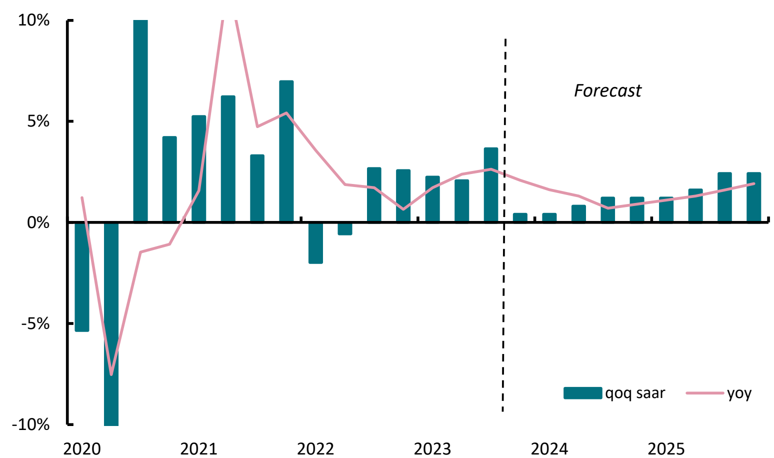
Household saving rate and model (net worth, inflation, 50+ share of workforce)



Source: BEA, AXA IM Research, Nov 2023

Growth forecast to slow, while avoiding contraction

US GDP growth



Source: BEA, AXA IM Research, Nov 2023

Fed to ease amidst election uncertainty

US

Federal Reserve to manage policy restrictiveness

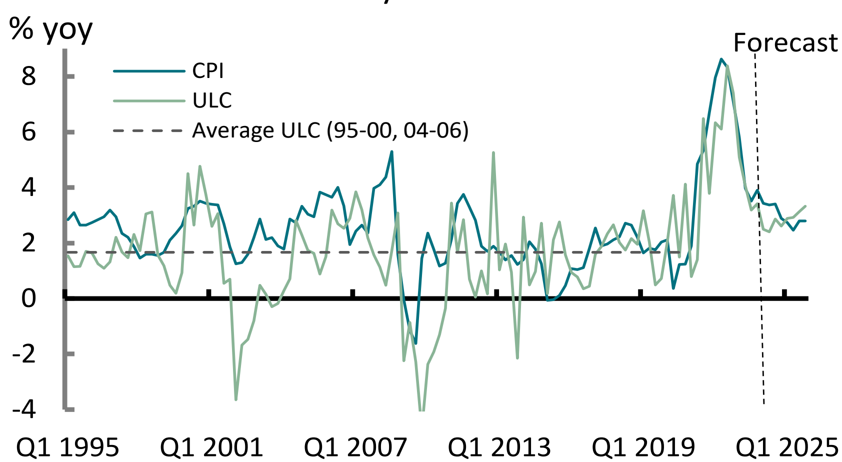
- We believe the Fed has peaked at 5.25-50%. With inflation expected to return to target over the coming years, the real FFR would become more restrictive if left unchanged. We expect the Fed to manage this restrictiveness over coming years, reducing the rate by 75bps from June 20024 to end-year and a further 50bps to 4.25% in 2025. This would still leave policy in restrictive territory by end-2025. We also expect QT to continue until the end of 2025, when we expect the Fed to announce an end in early 2026.

November Elections pose significant risks

- The Presidential Election next year will be consequential. A re-run of the Biden v Trump 2020 contest looks most likely, but this match-up is not certain. Polls have wavered recently that President Biden would win such re-match, but polls only tell so much this far out. The Senate election looks unfavourable to Democrats, suggesting a second Biden term would struggle to pass legislation. A second Trump term would likely focus on reversing TCJA tax cut expiries; we would see broader geopolitical risks in this outcome.

Unit labour costs to keep inflation somewhat elevated

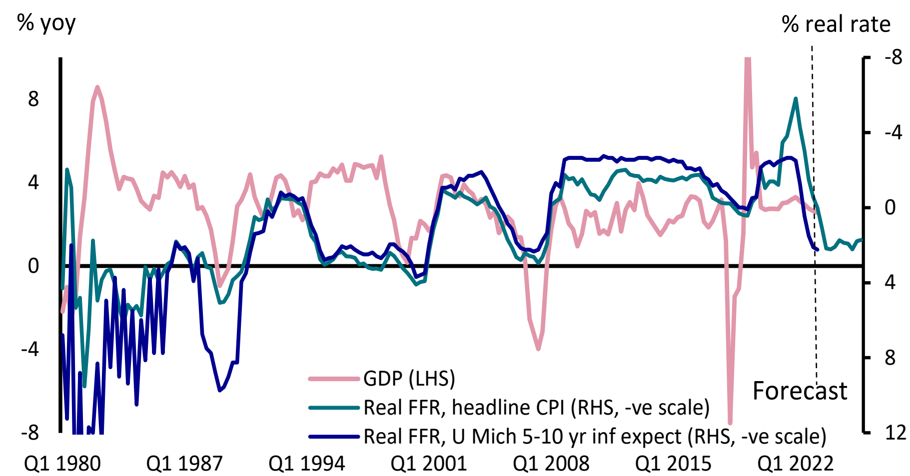
Inflation outlook driven by unit labour costs



Source: BLS, AXA IM Research, Nov 2023

Fed to ease policy to manage restrictiveness of real rates

Measures of real Fed Fund Rate and GDP growth



Source: Refinitiv, AXA IM Research, Nov 2023

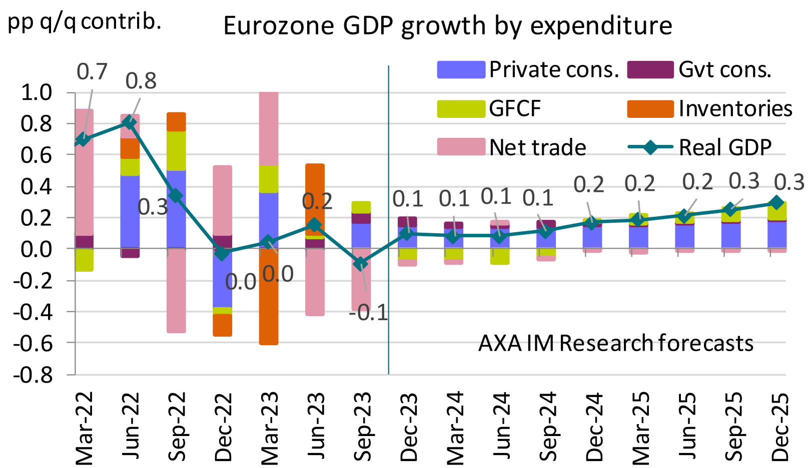
Meagre growth to continue

Euro area

Avoiding recession thanks to consumers

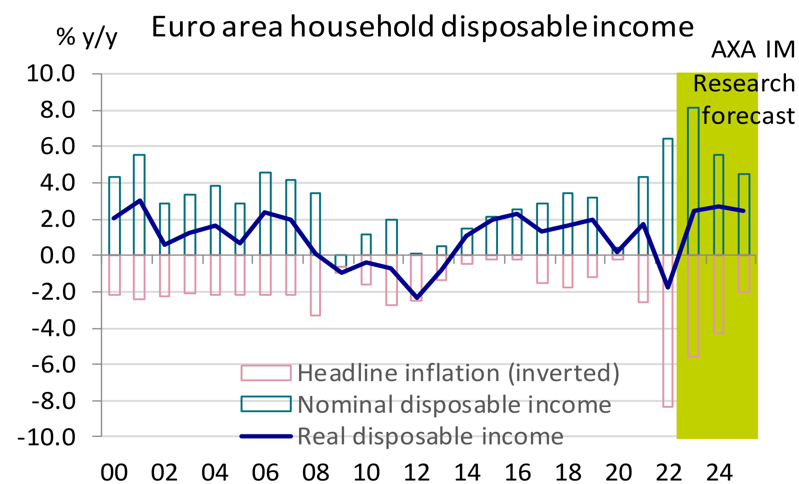
- Although it cannot be entirely ruled out, we think euro area should avoid a technical recession in H2 23. We look for meagre 0.1% q/q Q4 GDP growth after -0.1% q/q in Q3. All in, we project 0.3% and 0.8% eurozone GDP growth in 2024 and 2025, after +0.5% in 2023. Supply issues to fade, though unlikely to disappear.
- We forecast negotiated wage growth to slow gradually from 4.5% in 2023, to 4.0% in 2024, and 2.8% in 2025, but to remain higher than inflation 2024-2025 forecasts at 2.7% and 2.2% (after 5.5% in 2023).
- Private consumption recovery should more than offset an expected mild investment contraction, coming from both residential construction and business investment. We think investment is likely to stand more resilient than historical relationship suggest.

Well below potential growth driven by private consumption



Source: Eurostat, AXA IM Research, November 2023

Falling inflation to support resilient nominal disposable come



Source: Eurostat, AXA IM Research, November 2023

ECB: A challenging policy sequence

Euro area

ECB's balance sheet next in focus

- We expect the ECB to proceed carefully on Pandemic Emergency Purchase Programme (PEPP), mimicking its approach for the Asset Purchase Programme (APP). We expect a decision this winter, looking to initiate partial PEPP roll-off from H2 24. March (or possibly April) would be the most appropriate timing, encompassing the planned comprehensive operational framework review.

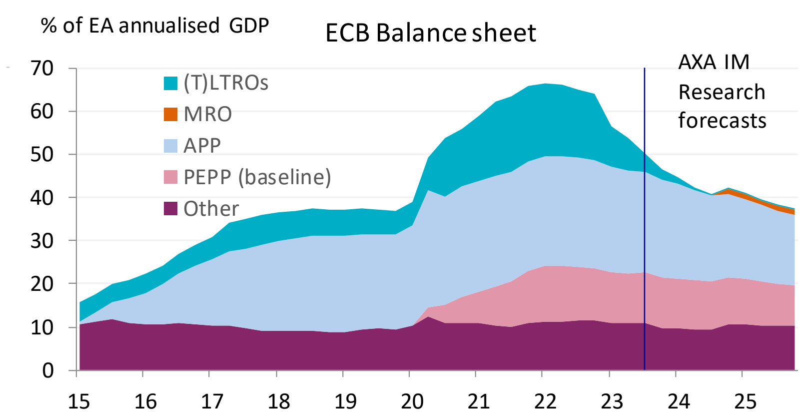
Rate cuts: no earlier than summer 2024

- Reflecting our below consensus/ECB view on growth, we have pencilled June for the first cut (25bps a quarter until June 25 to 2.75%). This will also depend on what the Fed does (our baseline is also for a June easing), as well as the pace of underlying price pressures cooling. A possible later start to easing in September is also very likely.

Italy: Beware of market discipline (again)

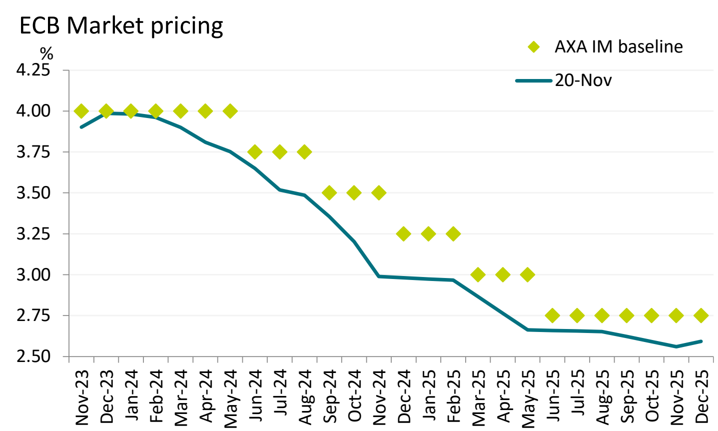
- Despite relative political stability, we do not think 2024-25 is likely to be plain sailing for Italy's bond market. We find Italy's government growth forecast too optimistic (1.2%/1.4%; AXA IM: 0.0%/0.5% for 2024/25) paving the way for fiscal slippage. Meanwhile, net issuance is c.€50bn higher than in 2023 and we are unsure that Italian households will save the day (again).

ECB's balance sheet normalisation to continue at gradual pace



Source: ECB, AXA IM Research, November 2023

ECB rate cuts: Market is on the aggressive side



Source: Bloomberg, AXA IM Research, as of 20 November 2023

Economic outlook weakens

UK

BoE's tightening to continue to weigh

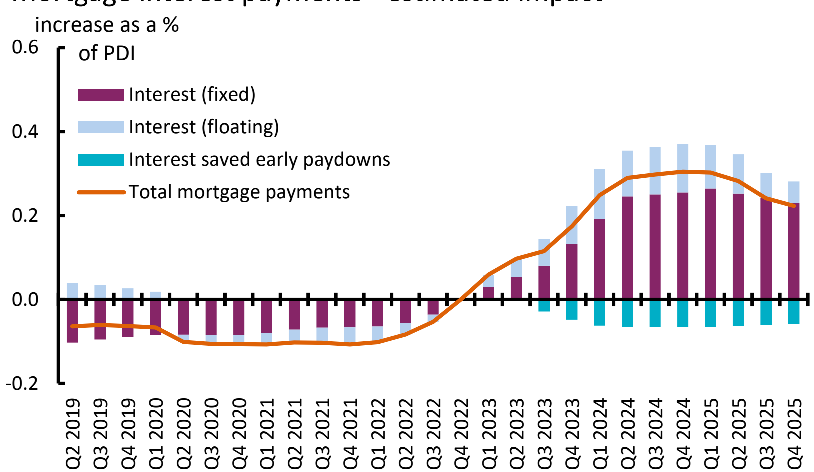
- Continued weakness is expected in household spending as the lagged impact of Bank Rate tightening impacts mortgage payments and rents. Investment spending is also likely to be subdued, particularly in the face of recent government U-turns over large infrastructure projects. The combination should see growth on the cusp of recession (but narrowly avoiding). We forecast GDP growth at 0.5% in 2023, 0.0% in 2024 and 0.5% in 2025. This would be below potential throughout the forecast horizon.

Rising excess supply to continue disinflation

- Our weak growth outlook is consistent with a quicker emergence of labour market slack – unemployment rising quicker in our forecast than BoE expectations. This should contribute to a deceleration in wage growth, which in turn should soften domestically generated inflation pressures, particularly in the services sector. We forecast inflation to average 3.1% in 2024 and 1.8% in 2025 (from an expected 7.5% this year). We fear inflation could fall further below target beyond 2025.

Mortgage market transmits lagged tightening

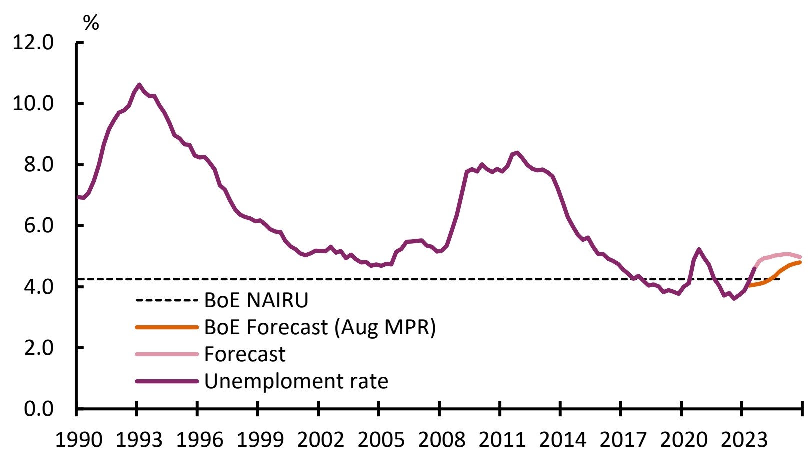
Mortgage interest payments - estimated impact



Source: ONS, AXA IM Research, November 2023

Labour market to ease more quickly

Unemployment rate forecast



Source: ONS, AXA IM Research, November 2023

Investment Managers

BoE to loosen monetary policy; election looms

UK

Monetary policy lags could add volatility

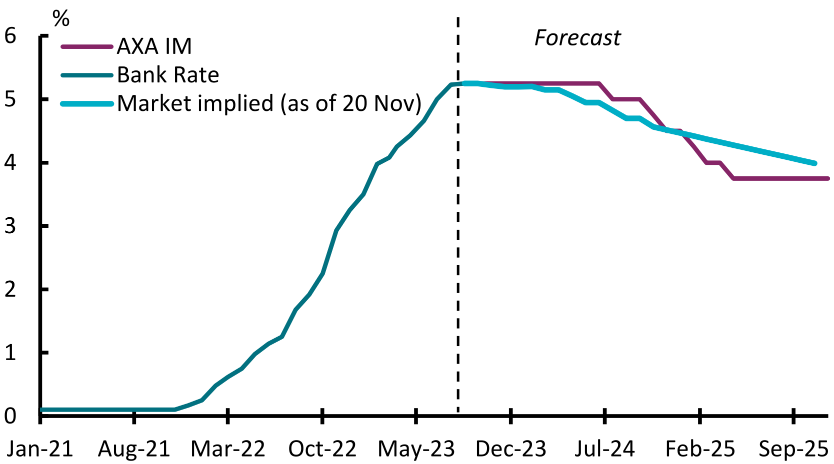
- A quicker loosening of the labour market should be consistent with the BoE loosening monetary policy as it projects inflation falling below target and excess supply rising. We suspect the BoE will want to see evidence of wages slowing in next Spring's wage round. We forecast the BoE loosening from August 2024 (risks of earlier). We then see the BoE easing quicker than markets currently expect, looking for Bank rate at 4.50% by end-2024 and 3.75% end-2025. We expect QT to continue through 2025.

2024 election likely; polls suggest change of government

- The UK will hold a General Election between now and 28 Jan 2025. The most likely date is October 2024. The recent Autumn Statement provided some fiscal loosening ahead of this election; we expect a little more in the March Budget. Current polling and recent by-elections suggest an outright Labour victory. But much can change over a year and the current government has a large majority. Any new government is likely to tighten fiscal policy sharply in the first few years of the new parliament.

Expect slower start, then quicker easing

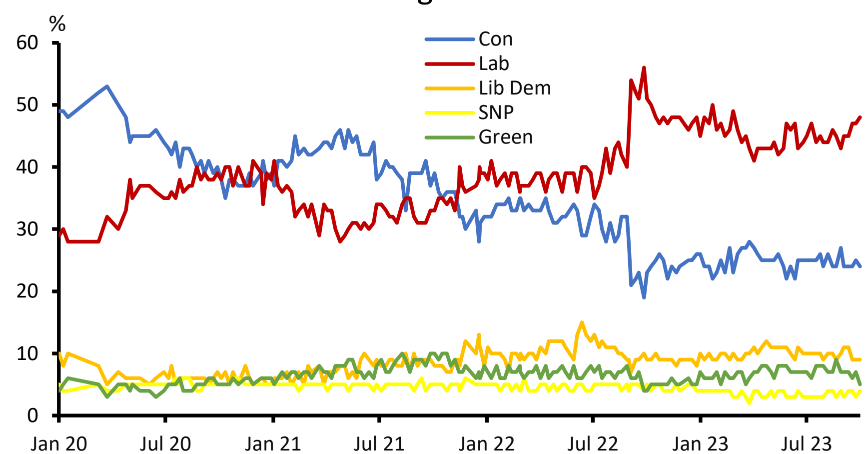
BoE Bank Rate outlook



Source: ONS, AXA IM Research, November 2023

Current polls point to a Labour government

YouGov - Westminister Voting Intentions



Source: YouGov, November 2023

Traditional investment stimulus revived 2023 growth prospects

China

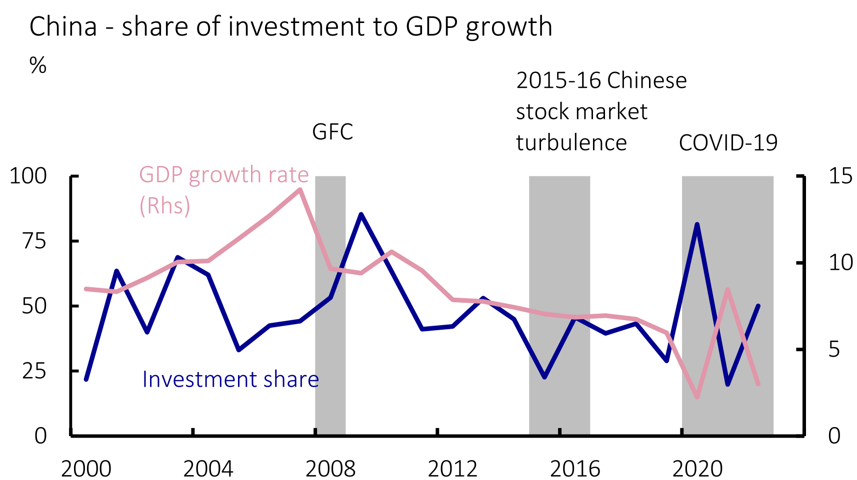
Weaker-than-expect rebound after lift of COVID-restriction

- Three years of rollercoaster pandemic restrictions and real estate turmoil have eroded public confidence and resulted in a material weakening in growth around mid-year.

Investment the transmission of stimulus, once again

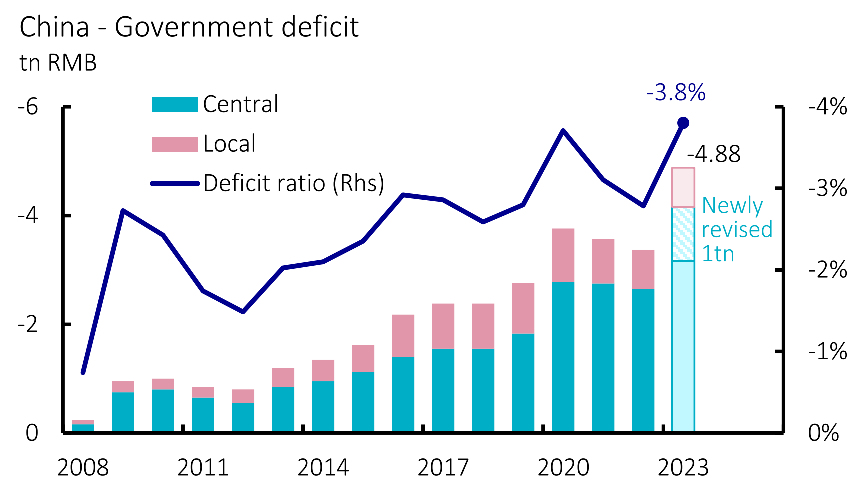
- Beijing has followed the conventional economic doctrine – using stimulus-backed investment as the marginal policy tool. The impact of this stimulus could be gradual, as the bulk of it inevitably funnels into infrastructure projects.
- The unexpected mid-year budget deficit revision confirmed the theme of future stimulus, but also indicated the new willingness of central government to assume more debt on behalf of local governments.
- This risks perpetuating a cycle of 'more debt, more investment, low returns', exacerbating resource misallocation.

Investment used to rescue GDP growth



Source: CEIC, AXA IM Research, Nov 2023

Central government willing to take on more debt



Source: CEIC, AXA IM Research, Nov 2023

Structural reforms needed, but (when) will it happen?

China

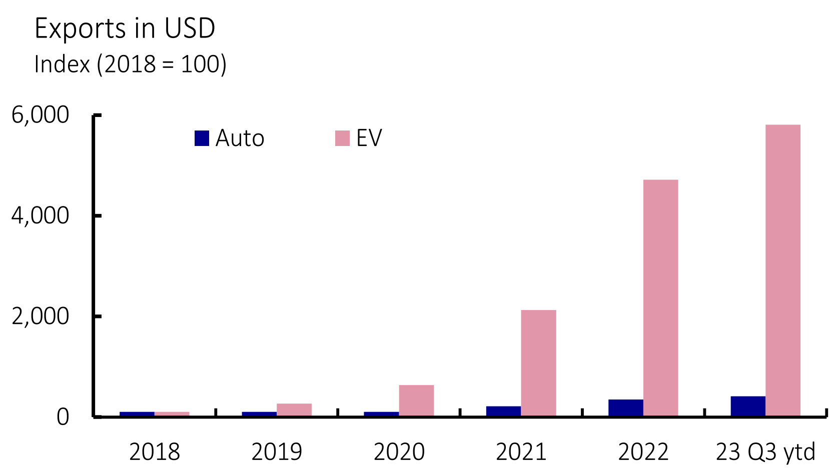
Consumption is counting on the property market, rising starts in exports

- Given high home ownership and housing being the main investment vehicle for households, more intervention and support are likely needed to stabilise the property sector, which in turn would underpin public confidence and lift consumption.
- Exports are expected to improve later next year following a recovery in global demand. Yet geopolitical risks could worsen.

Long-term structural reform is as needed as short-term stimulus

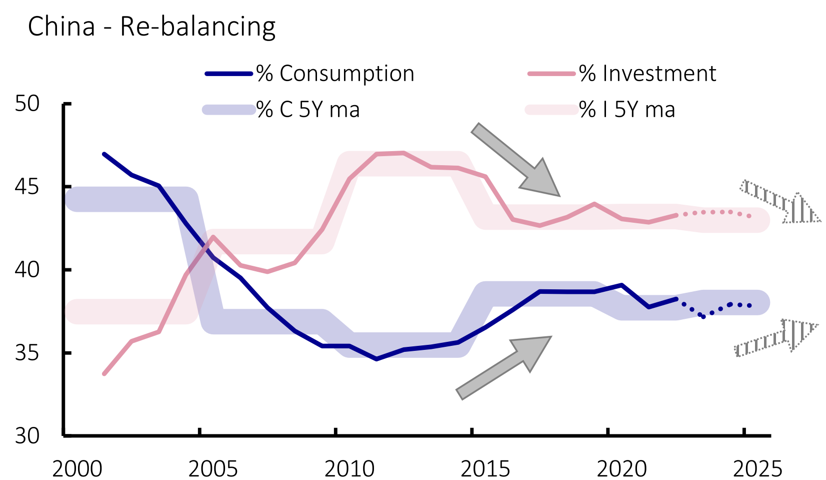
- The investment-driven growth model has served China these past four decades, but it is running out of steam.
- Structural reform and economic rebalancing are necessary for continued long-term economic growth prospects.
- But such reforms entail a loosening of Beijing's grip on the economy. Based on President Xi's recent behaviour, there are questions about whether this will be acceptable.

Electric vehicle exports have grown exponentially



Source: CEIC, AXA IM Research, Nov 2023

When will economic rebalancing be back on the agenda?



Source: CEIC, AXA IM Research, Nov 2023

The end of Japan's deflation story

Japan

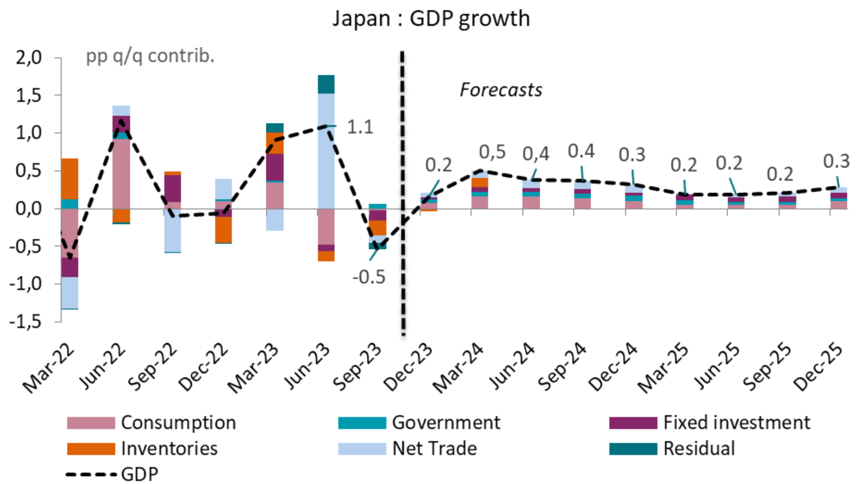
Generous government spending to sustain growth

- The household outlook is better oriented with fading inflation and better wage growth prospects. The government intends to support purchasing power with a further stimulus package, including lower tax brackets. Private and public investment should also benefit from the plan. We believe the ¥37.4tn package (of which ¥14.3tn is a supplementary budget) should boost GDP by 0.8 percentage points and forecast GDP growth of 1.2% and 1.0% in 2024 and 2025 respectively.

Japan's inflation at a turning point

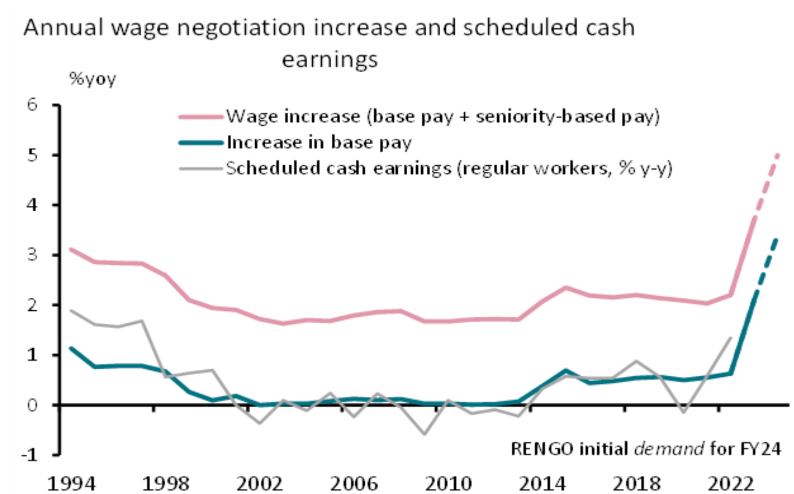
- Helped by the global inflation shock brought on by rising energy costs and a weak yen, pricing dynamics are improving. However, while we think it is unlikely that trend inflation will rise to 2% yet, increasing inflation expectations should help shift an economy that has battled with deflation for decades. Wages have long been central to the weak domestic inflationary pressures and are showing sustained signs of rising. We forecast inflation to average 3.2% in 2023, 2.2% in 2024 and 1.6% in 2025

Slow but resilient growth



Source: Refinitiv, AXA IM Research, November 2023

2024 wages negotiation point to a large increase



Source: Rengo, Refinitiv , AXA IM Research, November 2023

Stars nearly aligned for the Bank of Japan to begin normalisation

Japan

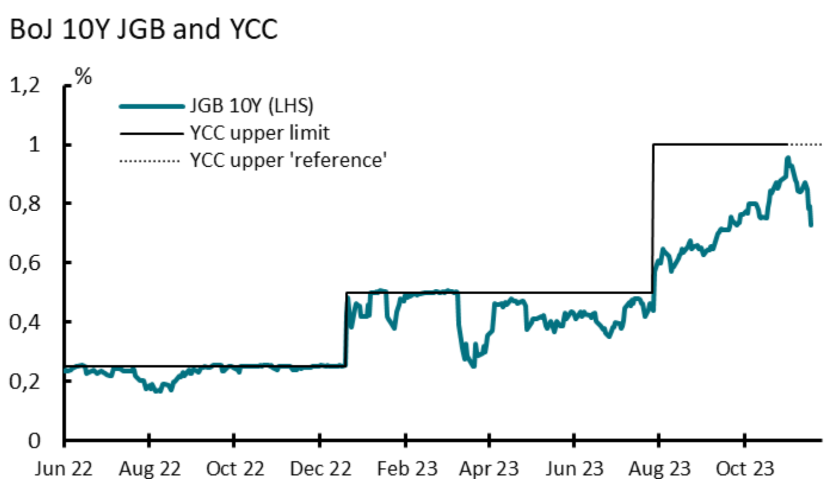
Loosening control on 10-year JGBs just the beginning

- The yield curve control policy's 1% cap on 10-year yield is now a soft reference. We expect the YCC's formal end to be accompanied by an initial step towards rate policy normalisation with the short-term rate likely to be increased by 10 basis points to 0.0%. We believe that this will happen around April 2024, once the BoJ has better sight of 2024's wages outcome.

After years of low interest rates the road to normalization is fraught with risks

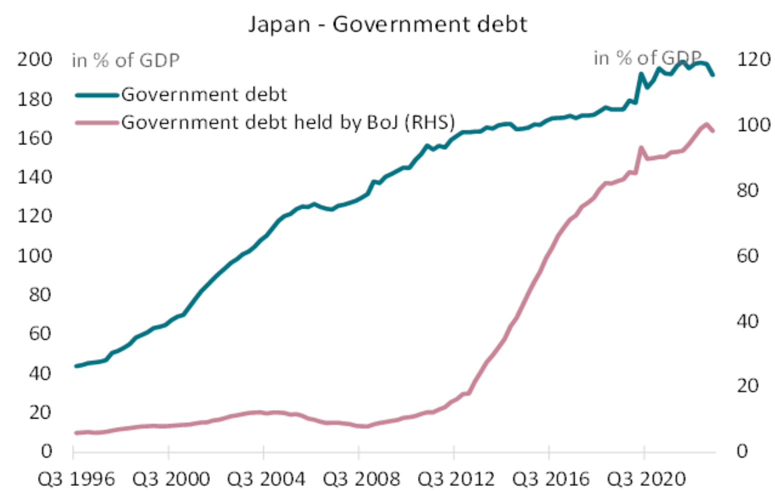
- Japanese mortgages are mostly floating rate (60%), so rising interest rates will negatively impact households' income immediately. The impact on income should be manageable, but sentiment and the impact on the broader housing market is a risk.
- Vulnerable corporates and smaller and medium size firms (including most 'zombie' companies) face similar issues.
- Government debt, which stands at 263% of GDP is also at risk with a rising cost of servicing its debt likely to become more burdensome.

BoJ to refrain from acting forcefully if 10yr yield exceeds 1%.



Source: Refinitiv, AXA IM Research, November 2023

Debt/GDP ratio to stabilise at best in coming years



Source: Refinitiv, BoJ, AXA IM Research, November 2023

Risks of domestic driven recession

Canada

Household sector hobbled by rate hikes

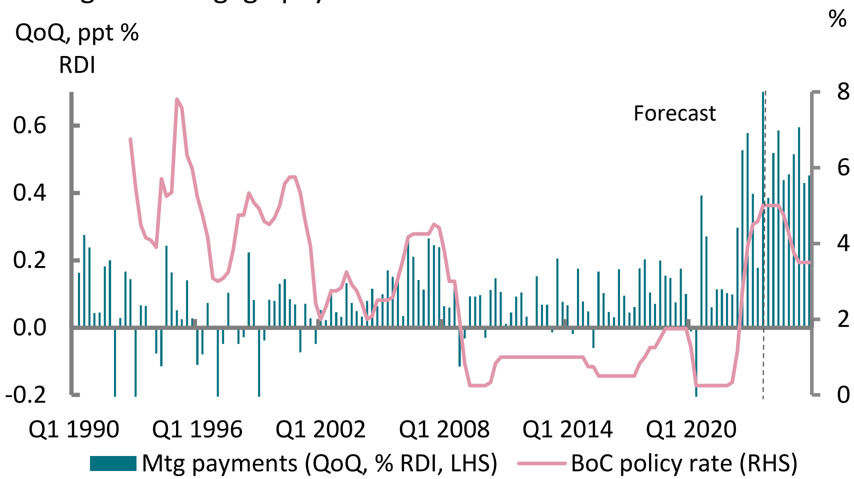
- Consumption stalled in Q2 and we forecast a similar outcome around the turn of the year. While employment and wage deceleration is likely to soften real income growth, even as inflation slows, it is the lagged impact of interest rate hikes on mortgage holders that concerns us. By end-2023 just over 40% of mortgage holders will have reset mortgages to higher rates. This will rise to over 60% by end-next year and over 80% by end-2025. A consumer slowdown is likely to be a big drag on broader GDP.

Household sector to drive weak growth in 2024

- We also envisage a marked softening in investment growth over the coming quarters, despite support from US incentives. Moreover, an expected softening in external growth is likely to slow export growth, despite relative outperformance this year - net trade is likely to turn neutral from a strong support. In total, we forecast growth of 1.1% in 2023, 0.5% in 2024 and 1.7% in 2025. A sharper slowdown in US or Chinese growth could tip the economy into recession. Further US resilience would be supportive.

Lagged impact of tightening to weigh on consumers

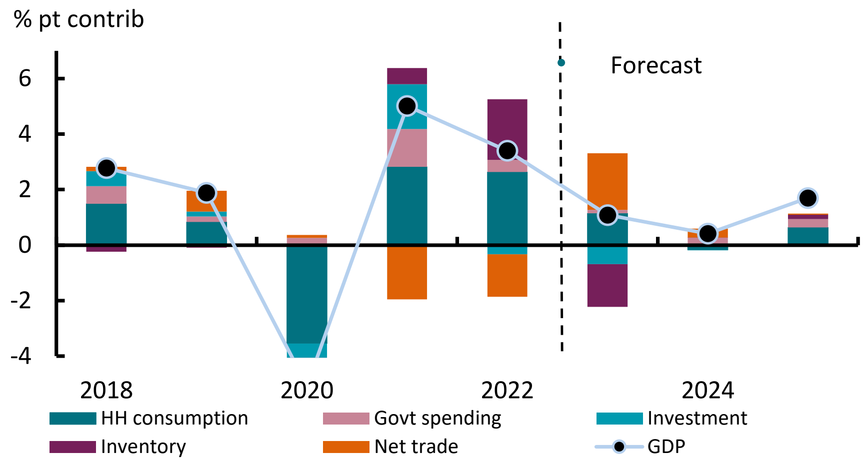
Change in mortgage payments and BoC Rate



Source: CANISM, BoC, AXA IM Research, Nov 2023

Subdued 2024 growth outlook to improve for 2025

Contributions to growth



Source: CANISM, AXA IM Research, Nov 2023

Investment Managers

A structural challenge for inflation

Canada

Structural issues pose challenge for falling inflation

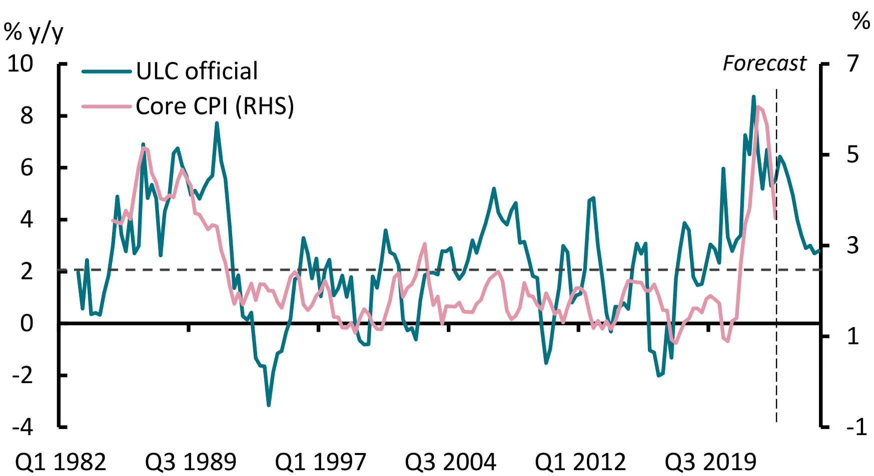
- Inflation has fallen sharply to 3.3% from a peak of 8.1% 16 months ago, but most of this reflects energy disinflation while core measures have remained stickier. Canada's high migration economy, high house price and household indebtedness and low productivity growth (despite high-skilled migration) mix pose challenges for returning inflation to target, as unit labour costs look set to remain elevated. We forecast inflation to average 4.0% in 2023, 3.2% in 2024 and 2.6% in 2025.

BoC should ease policy in 2024, but later than expected

- The BoC remains concerned about sticky core inflation. However, it faces an economy on the brink of recession, which could create financial stability concerns if it exacerbates the housing slowdown. We forecast the BoC to have peaked with its policy rate at 5.00%, although the BoC is still deliberating. We expect it to leave policy unchanged to lower core inflation until July 2024, when we forecast 3 cuts (to 4.25%) by end 2024 and a further 75bp (to 3.50%) in cuts to around mid-2025.

Productivity challenges inflation return to target

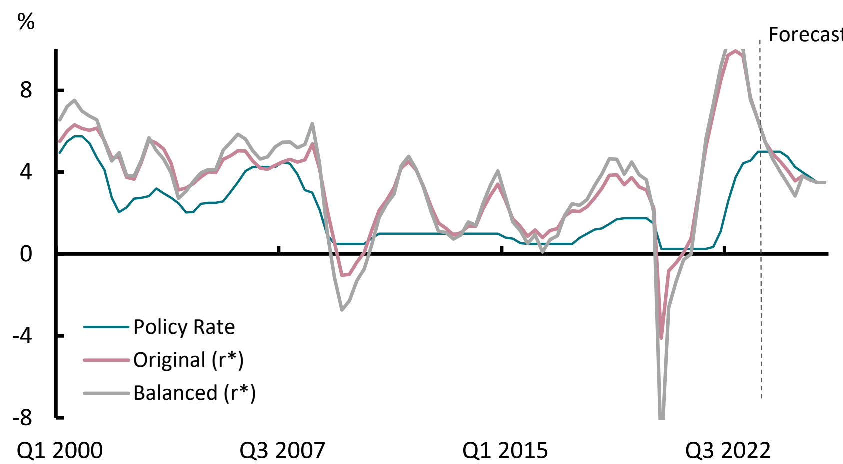
Core CPI inflation and unit labour costs



Source: CANISM, BoC, AXA IM Research, Nov 2023

Inflation to see BoC lagged rate easing

Taylor Rules and BoC policy rate



Source: CANISM, BoC, FRB, AXA IM Research, Nov 2023

Central Europe exiting recession; Turkey's adjustment uncertainties...

EM Europe

Central Europe (CE) to recover despite main trading partner woes

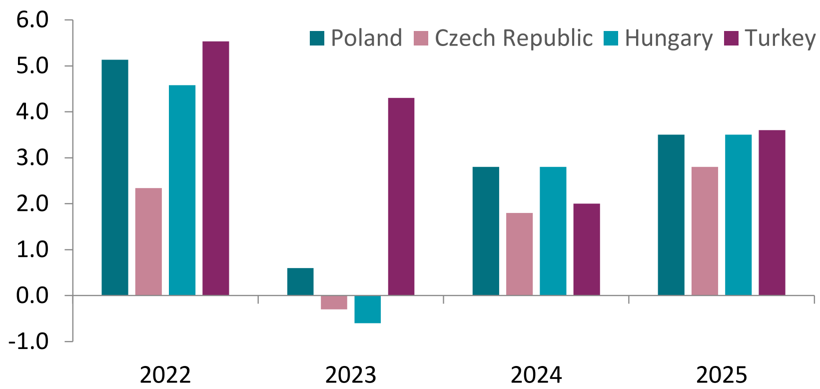
- Despite weak external demand, particularly from Germany, new production lines coming online in 2024 should support output and exports, while improved consumers' purchasing power on the back of strong disinflation will support consumption. Expectations of some EU funds flowing into Poland and Hungary help the 2025 investment profile. We see scope for fiscal consolidation, but monetary policy should ease as inflation comes in closer to targets

Quo vadis Turkey after March 2024 local elections?

- The shift to more orthodox policy since elections in Turkey favours a gradual, not decisive rebalancing, likely to continue beyond the next local elections. TRY should continue to weaken, and Turkey will remain exposed to oil price volatility and foreign investor appetite when it comes to its external financing needs. Inflation should peak by mid-2024 but the pace of disinflation will depend on the central bank's willingness and ability to proceed with care. GDP growth should halve next year from above 4% in 2023.

Intra-regional growth dispersion in 2024, stronger in 2025

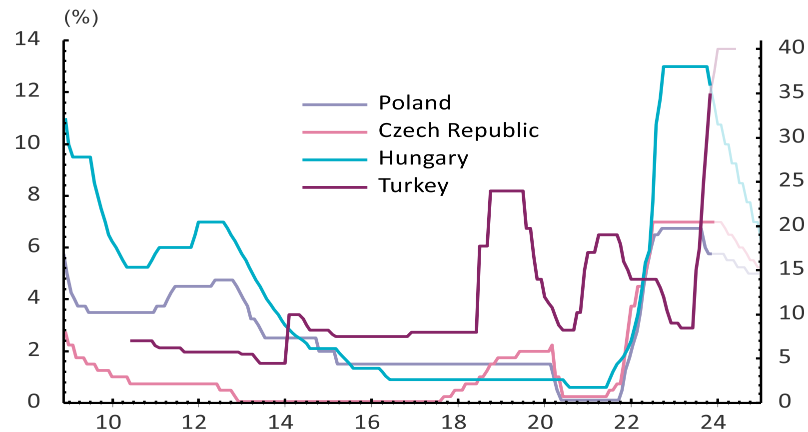
EM Europe: GDP growth (%) forecasts



Source: AXA IM Forecasts, Nov. 2023

Monetary policy at different junctures

Policy rates, history and forecasts (%)



Source: LSEG Datastream and AXA IM Research Nov 23

Growth to bottom in 2024, return to low potential growth in 2025

LatAm

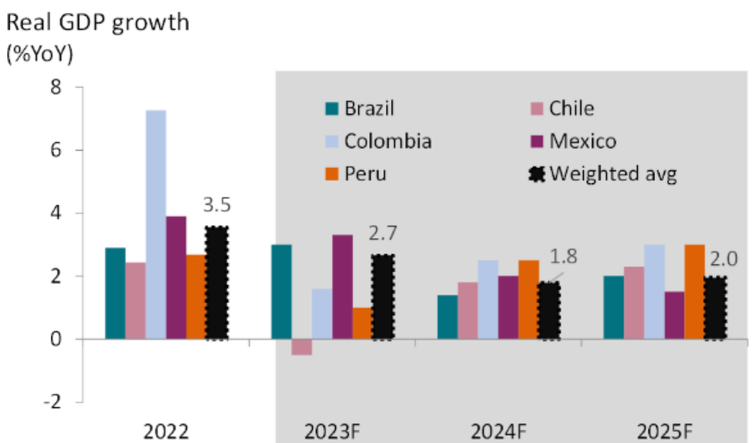
Weaker external environment to drive 2024 slowdown

- Despite expectations of a challenging year for Latin America in 2023, growth in the region has shown remarkable resilience. Brazil and Mexico were the key drivers in this stronger-than-expected performance, while Chile and Peru faced significant challenges. However, the region should slow in 2024, mainly due to weaker projected US and China growth. In the absence of shocks and with normalized monetary policy, economic activity in Latin America should accelerate back to its (low) potential growth in 2025.

Lower inflation should allow for further easing

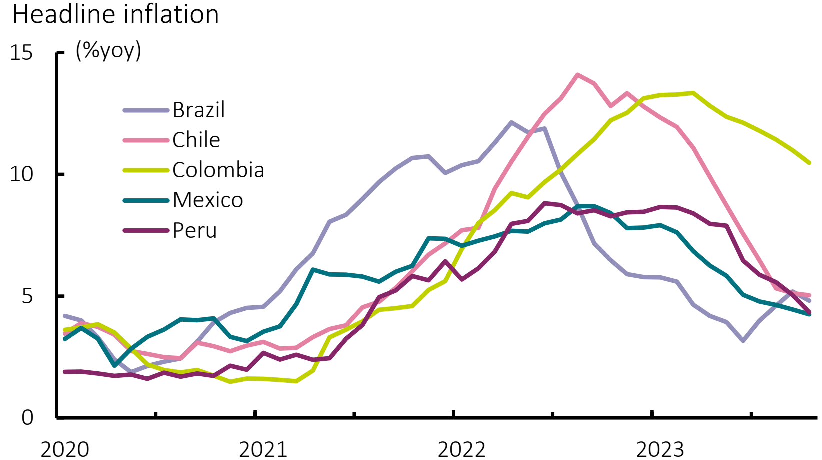
- Disinflation has also been a positive development this year, thanks to the proactive stance of the region's central banks, which began hiking rates earlier than in other regions. Inflation in Latin America is now at 5.5%, a significant drop from the 7.9% at the end of last year. With this improved situation, monetary policy is expected to continue its easing trajectory into 2024. Both Brazil and Chile have already embarked on easing cycles and Mexico should follow suit next year.

Brazil and Mexico to drive the regional slowdown in 2024



Source: LSEG Datastream and AXA IM Research, October 2023

Inflation on a firm downward trend across the region



Source: LSEG Datastream and AXA IM Research estimates, November 2023

Investment Strategy

Investment Managers

Investment strategy

Rates outlook

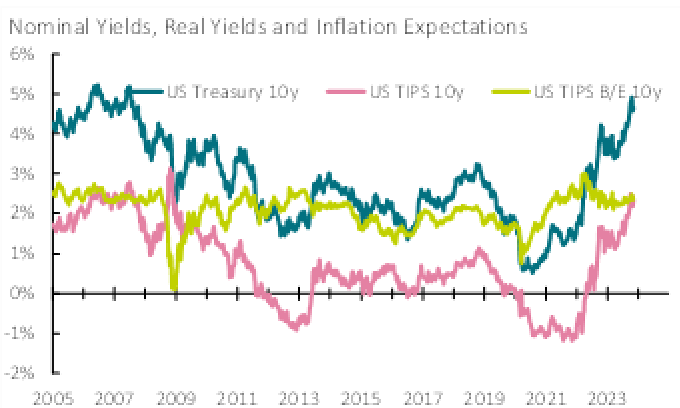
Real rates in the driving seat

- Real rates started to edge higher in March 2022, after nominal rates had already picked up by 180bp compared to pandemic-era lows. The reflation trade has been characterised by two distinct legs - inflation expectations moving from 1% to 3%, and real rates moving from -1% to +2.4%. Monetary policy might be restrictive enough, but there are doubts about the general stance of economic policy, including fiscal policy.

2024: The year of bonds redux?

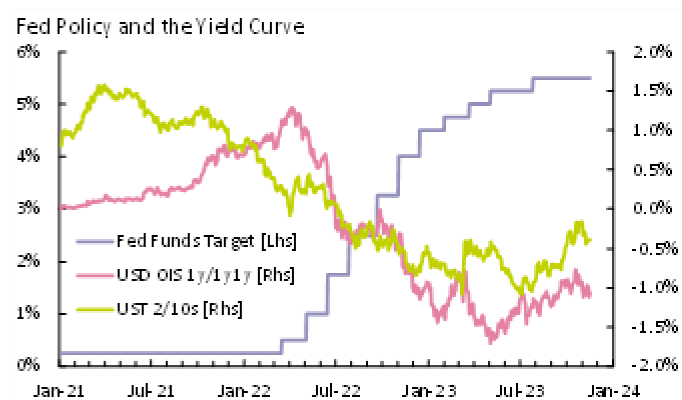
- Expect investors to focus on carry in 2024, even more than they might have done – albeit with mixed results – this year. Carry has the beneficial property of reducing the cost of being on the wrong side of a trade, thus increasing investors' confidence in entering and holding to a position. Risks will mainly result from the macro side and the associated monetary policy paths. Furthermore, Demand conditions need to be monitored carefully in an environment where major central banks reduce their large economic footprint and governments keep running public deficits.

Higher real rates in 2022 and 2023



Source: Bloomberg and AXA IM Research, 16 November 2023

Pricing in rate cuts since July 2022



Source: Bloomber and AXA IM Reserach, 16 November 2023

Investment strategy

Equity outlook

A structural change

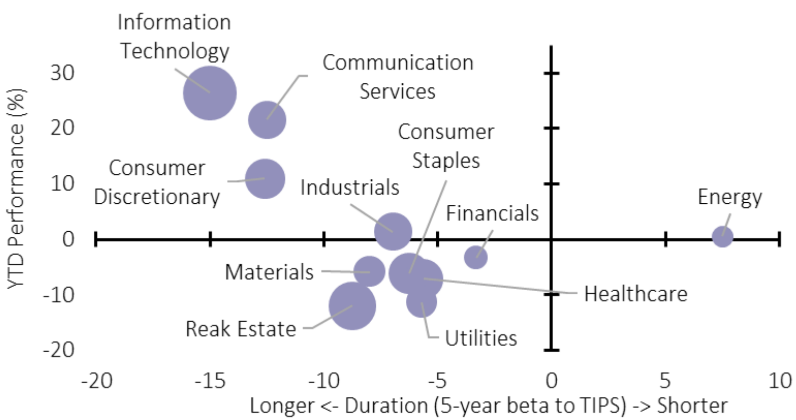
- The convergence of views around the higher level of long-term rates should reduce the interest rate risk for equities going forwards. Although higher rates creates a higher hurdle rate for companies, this rising rates cycle has shown us that quality is just as important as duration. Accordingly, expensive long-duration stocks have led the market's performance this year. For 2024, we believe the market will continue to favour sound balance sheet stocks. This is why a barbell allocation to information technology (benefiting from lower rate volatility) and financials (benefiting from structurally higher rates) looks reasonable.

Sluggish growth outlook

- GDP and earnings growth are diverging. The earnings consensus is for relatively good margin resilience, which we are having difficulty reconciling with our macroeconomic scenario. With pressure from slowing inflation (lower pricing), tight financial conditions and still increasing wage growth, the profit margin could evolve at a below trend pace next year. Yet disparities across different economies could create relative opportunities and we consider favouring the US relative to the rest of the world.

Long duration did well despite higher interest rates

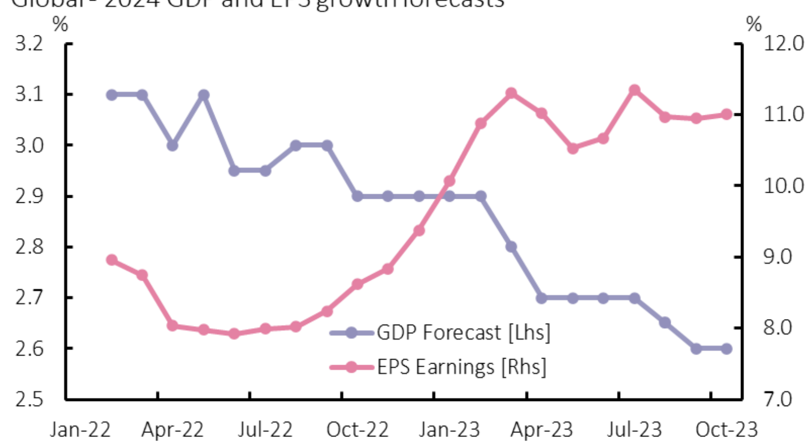
Global - Performance by real rates betas



Source: IBES and AXA IM Research, size of bubble is based on valuations, November 2023

The market and macro at odds

Global - 2024 GDP and EPS growth forecasts



Source: Bloomberg, IBES and AXA IM Research, November 2023

Investment strategy

Currency outlook

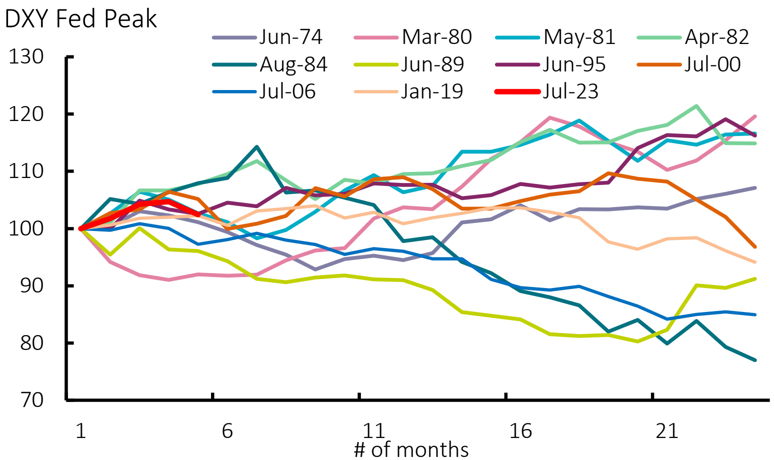
Fed peak, not US dollar peak

There is no clear evidence to suggest that USD should weaken after the Fed peak: particularly looking at the 1970s and early 1980s high inflation periods. We expect the US to continue to show resilience against global monetary policy tightening, deferring the point where USD might be caught up by foreign yields. Admittedly, stability in yield differentials might only mean USD stability, not strength. But the market only expects other central banks to broadly match the Fed's easing pace, not exceed it. In comparison EUR and GBP look rich against our growth differential and monetary policy outlook, and not cheap from a long-term perspective.

Japan's yen: rate differential slow to unwind

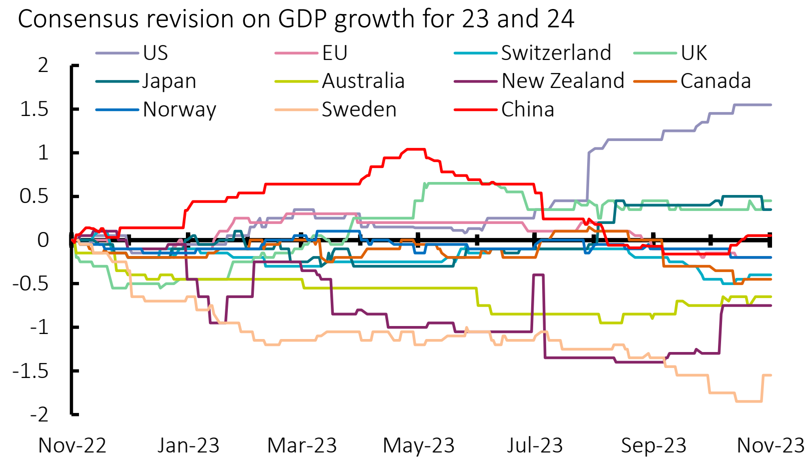
JPY's sharp undervaluation is fully explained by the divergence between Fed and BoJ policy. But we expect only a slow and limited rebound after we eventually pass peak divergence as US rates should remain high for longer. By contrast, the BoJ is likely to remain cautious in terms of reversing policy accommodation: with 6% adverse carry, there is no incentive to position too early against USD.

Fed peak not necessarily leading to USD weakness



Source: Bloomberg and AXA IM Research, 17 November 2023

Unrivalled US exceptionalism



Source: Bloomberg and AXA IM Research, 17 November 2023

Forecasts & Calendar

Macro forecast summary

Forecasts

Real GDP growth (%)	2023*		2024*		2025*	
	AXA IM	*Consensus*	AXA IM	*Consensus*	AXA IM	*Consensus*
World	3.0		2.8		3.0	
Advanced economies	1.5		0.8		1.3	
US	2.2	2.2	1.1	0.9	1.6	1.8
Euro area	0.5	0.5	0.3	0.6	0.8	1.5
Germany	-0.1	-0.4	0.2	0.5	0.7	1.5
France	0.9	0.8	0.6	0.8	0.7	1.3
Italy	0.7	0.7	0.0	0.6	0.5	1.2
Spain	2.4	2.3	0.9	1.3	1.3	1.9
Japan	1.9	1.9	1.2	0.9	1.0	1.0
UK	0.5	0.4	0.0	0.3	0.5	1.2
Switzerland	0.6	0.8	0.8	1.2	1.3	1.5
Canada	1.1	1.1	0.9	0.6	1.7	1.9
Emerging economies	3.9		4.0		4.1	
Asia	4.9		4.8	4.0	4.7	
China	5.2	5.0	4.5	4.4	4.2	4.4
South Korea	1.4	1.2	2.2	2.0	2.3	2.2
Rest of EM Asia	5.0		5.4		5.5	
LatAm	2.3		2.3		2.4	
Brazil	3.0	3.0	1.4	1.6	2.0	2.0
Mexico	3.3	3.1	2.0	1.9	1.5	2.2
EM Europe	2.4		2.0		2.7	
Russia	2.2	1.7	1.1	1.4	1.0	1.1
Poland	0.6	0.2	2.8	2.7	3.5	3.4
Turkey	4.3	3.5	2.0	2.1	3.6	3.2
Other EMs	2.3		3.5		4.0	

Source: Datastream, IMF, Bloomberg and AXA IM Macro Research – As of 27 November 2023
**Forecast*

Investment Managers

Expectations on inflation and central banks

Forecasts

Inflation Forecasts

CPI Inflation (%)	2023*		2024*		2025*	
	AXA IM	*Consensus*	AXA IM	*Consensus*	AXA IM	*Consensus*
Advanced economies	4.7		2.8		1.9	
US	4.2	4.2	3.2	2.6	2.6	2.3
Euro area	5.5	5.6	2.7	2.5	2.1	2.1
China	0.4	0.6	1.1	1.7	2.0	1.9
Japan	3.0	3.2	1.5	2.2	1.6	1.5
UK	7.5	7.4	2.8	3.1	1.8	2.0
Switzerland	2.4	2.2	1.5	1.6	1.3	1.3
Canada	4.1	3.9	3.2	2.6	2.6	2.0

Source: Datastream, IMF, Bloomberg and AXA IM Macro Research – As of 27 November 2023
**Forecast*

Central banks' policy: meeting dates and expected changes

Central bank policy Meeting dates and expected changes (Rates in bp / QE in bn)		Current	Q4-23	Q1-24	Q2-24	Q3-24	Q4-24
United States - Fed	Dates	5.50	13-Dec	31 Jan 20 Mar	1 May 12 Jun	30-31 Jul 17-18 Sep	6-7 Nov 17-18 Dec
	Rates		unch (5.50)	unch (5.50)	-0.25 (5.25)	-0.25 (5.00)	-0.25 (4.75)
Euro area - ECB	Dates	4.00	14-Dec	25 Jan 7 Mar	11 Apr 6 Jun	18 Jul 12 Sep	17 Oct 12 Dec
	Rates		unch (4.00)	unch (4.00)	-0.25 (3.75)	-0.25 (3.50)	-0.25 (3.25)
Japan - BoJ	Dates	-0.10	19-Dec	22-23 Jan 18-19 Mar	25-26 Apr 13-14 Jun	30-31 Jul 19-20 Sep	30-31 Oct 18-19 Dec
	Rates		unch (-0.10)	unch (-0.10)	+0.10 (0.00)	unch (0.00)	unch (0.00)
UK - BoE	Dates	5.25	14-Dec	1 Feb 21 Mar	9 May 20 Jun	1 Aug 19 Sep	7 Nov 19 Dec
	Rates		unch (5.25)	unch (5.25)	unch (5.25)	-0.25 (5.00)	-0.50 (4.75)
Canada - BoC	Dates	5.00	6-Dec	24 Jan 6 Mar	10 Apr 5 Jun	24 Jul 4 Sep	23 Oct 11 Dec
	Rates		unch (5.00)	unch (5.00)	unch (5.00)	-0.25 (4.75)	-0.25 (4.50)

Source: AXA IM Macro Research - As of 27 November 2023

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Calendar of events

2023	Dates	Events	Comments
December	01-Dec	UK Credit rating review (Fitch)	
	06-Dec	BoC meeting	unch (5.00%)
	06-Dec	UK Financial Stability Report	
	10-12 Dec	Egypt Presidential election	
	13-Dec	FOMC meeting	unch (5.50%)
	14-Dec	ECB meeting	unch (4.00%)
	14-Dec	BoE meeting	unch (5.25%)
	19-Dec	BoJ meeting	unch (-0.10%)
2024	**Dates**	**Events**	**Comments**
January		ECB Operational framework review	
		OPEC+ Oil production target cuts	
	01-Jan	UK Post Brexit border regulations on EU goods introduced	
	13-Jan	Taiwan Presidential election	
	19-Jan	Split deadline of end of US continuing resolution	
	22-23 Jan	BoJ meeting	unch (-0.10%)
	24-Jan	BoC meeting	unch (5.00%)
	25-Jan	ECB meeting	unch (4.00%)
	31-Jan	FOMC meeting	unch (5.50%)
February	01-Feb	BoE meeting	unch (5.25%)
	02-Feb	Split deadline of end of US continuing resolution	
	06-Feb	Reserve Bank of Australia (RBA) meeting	
	26-27 Feb	BoE's Agenda for Research conference	
March		UK Chancellor Jeremy Hunt delievers Spring Budget	
	05-Mar	US Super Tuesday	
	06-Mar	BoC meeting	unch (5.00%)
	07-Mar	ECB meeting	unch (4.00%)
	17-Mar	Russia Presidential elections	
	18-19 Mar	BoJ meeting	unch (-0.10%)
	19-Mar	Reserve Bank of Australia (RBA) meeting	
	20-Mar	FOMC meeting	unch (5.50%)
	21-Mar	BoE meeting	unch (5.25%)
	31-Mar	Ukraine Presidential election	
April		BoE Term Funding Scheme repayments begin	
		India General Elections	
	10-Apr	BoC meeting	unch (5.00%)
	11-Apr	ECB meeting	-25bps (3.75%)
	25-26 Apr	BoJ meeting	+10bps (0.00%)
	30-Apr	Post Brexit border full SPS checks on EU goods introduced	
May	01-May	FOMC meeting	-25bps (5.25%)
	07-May	Reserve Bank of Australia (RBA) meeting	
	09-May	BoE meeting	unch (5.25%)
June	02-Jun	Mexico Presidential election	
	05-Jun	BoC meeting	unch (5.00%)
	06-Jun	ECB meeting	-25bps (3.75%)
	6-9 Jun	European Parliament election	
	12-Jun	FOMC meeting	-25bps (5.25%)
	13-14 Jun	BoJ meeting	+10bps (0.00%)
	18-Jun	Reserve Bank of Australia (RBA) meeting	
	20-Jun	BoE meeting	unch (5.25%)
	30-Jun	BoE MPC member & Deputy Governor Ben Broadbent's term ends	

Latest publications

October Global Macro Monthly -Geopolitics and yield add to macro uncertainty

25 October 2023

October OpEd - Bond pressure

25 October 2023

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September Op-Ed - In for the long haul

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Eurozone public debt sustainability: Make hay while the sun shines

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