Investment Institute *Asset Class Views*

The view from the Core CIO Office

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KEY INVESTMENT THEMES		
Markets withstand August's volatility	Federal Reserve likely to **cut rates soon**	Growth equities and high yield bonds **show solid potential**

CIO Office: Opinions

Chris Iggo, CIO AXA IM Core

August bounce may augur well for rest of 2024

Whatever triggered early August's volatility spike has not proved serious enough to derail markets' robust year-to-date performance. Equity and credit markets rebounded quickly while risk indicators – such as the VIX – swiftly reverted to their more benign lower levels. However, the early August moves highlighted that markets are priced to perfection and therefore, vulnerable to adverse fundamental news, even if the volatility was exaggerated by seasonally thin markets. Additional bouts cannot be ruled out in the months ahead given market sensitivity to US labour market data, Japanese monetary policy, and technology company earnings. At the same time, the rapid reversal in the risk sell-off can be seen as good news.

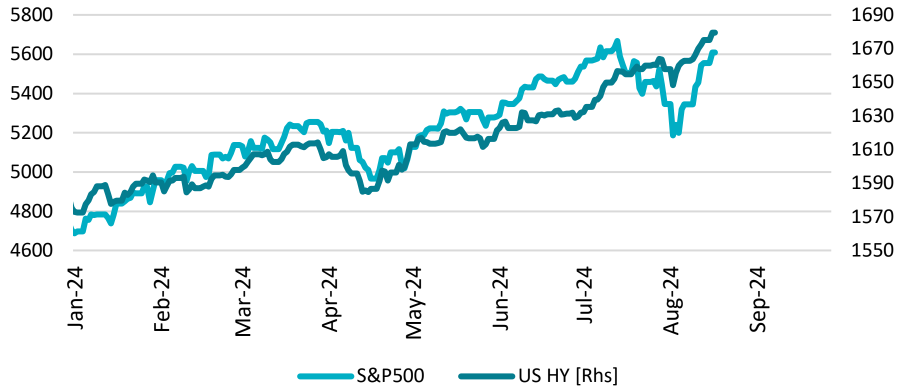
Fundamentals remain supportive. The Federal Reserve should start its interest rate cutting cycle soon - following the moves from other central banks. Elsewhere refinancing problems remain absent in public credit markets while second quarter corporate earnings largely met growth expectations. There has arguably been a moderation in political risk. Strong returns from risk assets might be sustained into the end of 2024, with growth equities and higher beta credit leading the way as they have for the whole of the year. High yield and other short-duration fixed income credit strategies most likely offer the lowest risk path to sustaining positive returns in the final semester of the year.

Alessandro Tentori, CIO Europe

High yield's optionality opportunity

High-yield bonds are often seen as one of the riskier inhabitants of a portfolio. However, recent stock market volatility tells a different story. The chart compares the Bank of America US High Yield Index with the S&P 500; it shows the market has dropped around 8.5% from 16 July to 5 August, while the US high yield universe actually lost less than 1%. Furthermore, high yield bonds have fully recovered, even reaching new highs for 2024. There are technical reasons for high yield's resilience but the point we are making here is related to the 'defensive option' embedded in high yield bonds. Just like any corporate bond, they can be decomposed in a risk-free yield and a risky credit spread. This latter component widened roughly 80-85 basis points but the total return effect was somewhat softened by the simultaneous sharp decline in US Treasury yields. Of course, we can compute a break-even between these two components but their inverse correlation is already a beneficial property for bond owners. The other obvious benefit results from high yield's rather contained duration, which is especially valuable during periods of relatively high absolute yield. The trade-off here is between credit risk and time value - investors enjoy an attractive carry profile, while at the same time avoid excessive sensitivity to spread widening. Once the US economy avoids recession – and we're not forecasting one in the near future – investors should potentially reap the benefits.

| Relative Value: US High Yield vs Equity



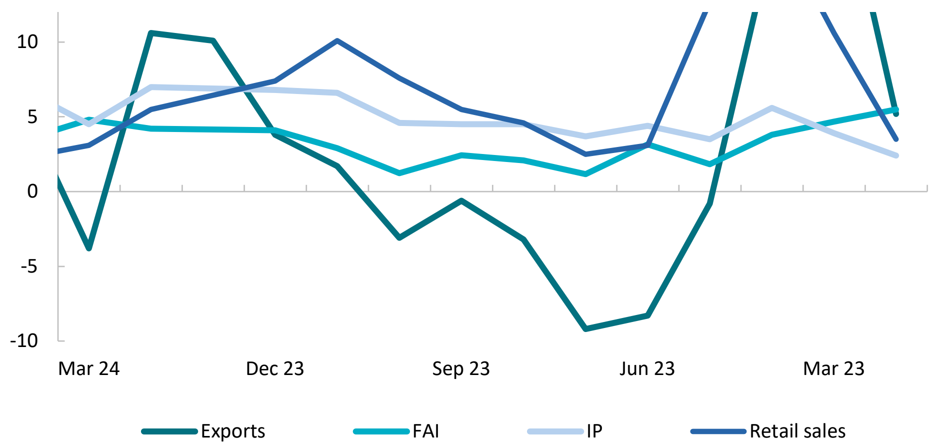
Source: Bloomberg

Ecaterina Bigos, CIO Asia ex-Japan

China's uphill journey of rebalancing its economy

China's current economic armoury - infrastructure and manufacturing sector investment – appears to be helpful in defending its real GDP growth. However, it comes with a cost of entrenching deflationary pressures and rising concerns of overcapacity. The downward pressure on the Producer Price Index also affects export prices, which is contributing to the fears of exporting deflation. While this is being tolerated for now, as many countries grapple with high inflation, it could become problematic when inflation rates fall within target ranges. An exit from deflation, helped by global trade, looks increasingly challenging. The rather notable sequential slowing in July's exports, with broad-based easing across major developed and emerging markets, is sending tentative signals the export engine may soften. As the export sector has been an important growth driver for China's economy in recent quarters, amid ongoing weakness in the housing sector and sluggish consumption growth, potential slowing would imply growing uncertainty on the industrial sector's growth outlook going into the second half of 2024. This comes on the back of cautious signals from the external front of slowing demand. Further out, trade tensions concerns are a major uncertainty. The current stimulus plan, if fully implemented, without changes, may exacerbate the issue of overcapacity, add to disinflationary pressures, and increase the future debt burden.

| Growth rate of exports, IP, FAI and retail sales %, year on year



Note: Exports in RMB; IP: industrial production; FAI: fixed asset investment. Source: CEIC and AXA IM Research, August 2024

AXA Investment Managers

Asset Class Summary Views

Views expressed reflect CIO team expectations on asset class returns and risks. Traffic lights indicate expected return over a three-to-six-month period relative to long-term observed trends.

Positive	Neutral	Negative

CIO team opinions draw on AXA IM Macro Research and AXA IM investment team views and are not intended as asset allocation advice.

Rates		Developed economy data points to interest rate cuts from September - path from there is less certain
US Treasuries		Fed likely to ease in September. Volatility remains a risk on new economic data and path from the first cut
Euro – Core Govt.		Further ECB rate cuts expected; political uncertainty remains a risk
Euro – Peripherals		Presents opportunities and higher real yields than Bunds
UK Gilts		Interest rate cuts fully discounted; markets await fiscal plans
JGBs		Uncertainty over Bank of Japan policy normalisation path. Yen remains volatile
Inflation		Stable expectations, with gradually lower inflation for the rest of 2024

Credit		Favourable pricing is increasing the asset class's contribution to excess returns
USD Investment Grade		Without significant growth deterioration, credit to remain resilient
Euro Investment Grade		Resilient growth and lower interest rates support credit's income appeal
GBP Investment Grade		Returns supported by better growth and expectations of rate cuts
USD High Yield		Narrative of growth without inflation is supportive. Fundamentals and funding remain strong
Euro High Yield		Strong fundamentals, technical factors and ECB cuts support total returns
EM Hard Currency		Higher quality universe, well-placed with US interest rate cuts commencing

Equities		Lower inflation will impact earnings cycle. Unmet return expectations from AI spending is a risk
US		Growth and quality to continue to dominate - but need to watch company earnings momentum
Europe		Attractive valuations, along with positive economic and earnings surprises
UK		Relatively more attractive valuations and positive economic momentum
Japan		Benefitting from semiconductor growth. Reforms and monetary policy in focus for broader performance
China		Growth remains unbalanced. Accelerating industrial output masks a weak consumer
Investment Themes*		Secular spending on technology and automation to support relative outperformance

*AXA Investment Managers has identified six themes, supported by megatrends, that companies are tapping into which we believe are best placed to navigate the evolving global economy: Technology & Automation, Connected Consumer, Ageing & Lifestyle, Social Prosperity, Energy Transition, Biodiversity.

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