Investment Managers

Investment Institute *Asset Class Views*

The view from the Core CIO Office

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KEY INVESTMENT THEMES

Rate cut hopes **boost bonds**	Europe's **tech imbalance**	**AI powers** Asia-Pacific trade

CIO Office: Opinions

Chris Iggo, CIO AXA IM Core

Fixed income benefiting from lower rate expectations

Lower interest rate expectations – further confirmed by the Federal Reserve's September cut - have helped drive recent strong fixed income performance. Returns for global government and corporate bonds over the third quarter have been among the strongest of the last 10 years. Going forward, bond yields may not be able to fall much further given what is already priced in. For rate expectations to decline further, the narrative would have to be that recessions risks are increasing or that a 'neutral' level for rates is even lower than previously thought. However, this is a low conviction view, given that recession signs are minimal so far. Forecasts of rates below 3% in the US and below 2% in Europe by the end of 2025 look to reflect the most likely macroeconomic outcomes.

As such, we believe the best way to access fixed income remains through yield curve steepening strategies, i.e. focusing on bonds towards the shorter end of the maturity spectrum. These should benefit from lower central bank interest rates. Additionally, corporate bonds remain attractive at current yields. Cash interest rates are set to fall below average yields on high grade corporate bonds, while high yield bonds provide a significant yield premium. Fundamentals in the corporate sector are solid and demand for higher yielding, income-generating assets remains strong. A consolidation of yields is not a negative sign for fixed income returns.

AXA Investment Managers

Alessandro Tentori, CIO Europe

European equities: Improved earnings but still lagging the US

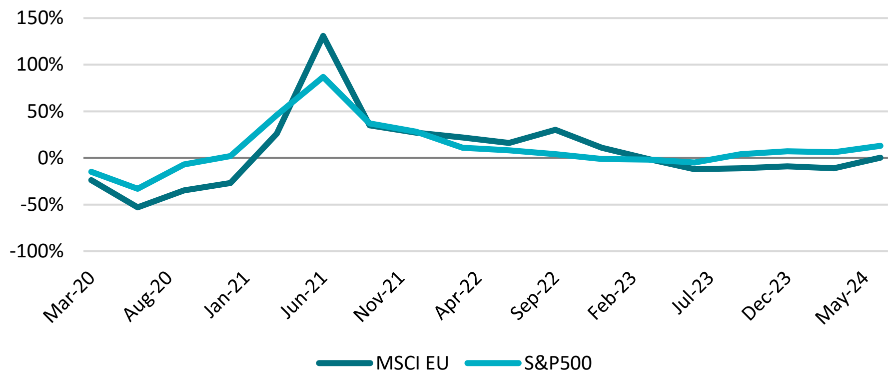
Following five quarters of negative earnings growth, European equities have crawled back into positive territory. And data measures suggest markets are bullish on European equities. However, absolute earnings growth still lags Wall Street by a considerable margin. Two factors could explain the 10 times price-to-earnings valuation gap between the MSCI US and MSCI EU indices.

Firstly, structural factors - relatively low productivity, regional fragmentation and implementation issues on European Union (EU) projects – such as the Banking Union - continue to depress Europe's potential growth rate. The International Monetary Fund expects the US to grow almost twice as fast as Europe in the long run.

Secondly there's sectoral differences. Looking at the historical composition of major indices, Europe seems to lag in industries like information technology. Some 20 years ago, the sector represented 16% of the S&P 500's and 4% of the Stoxx 600's market capitalisation. By the end of 2023, the share had increased to 29% in the US, but only to 7% in Europe. However, industrials and healthcare have gained in importance in the bloc since 2004.

Assuming artificial intelligence-based technology will dominate in the years to come, Europe's specific industrial make-up might be a key factor both in terms of long-term macroeconomics and expected performance - a crucial issue highlighted by former European Central Bank President Mario Draghi's recent report on EU competitiveness.

| Earnings per share growth: US vs EU



Source: Bloomberg, data as of 13 September 2024

Ecaterina Bigos, CIO Asia ex-Japan

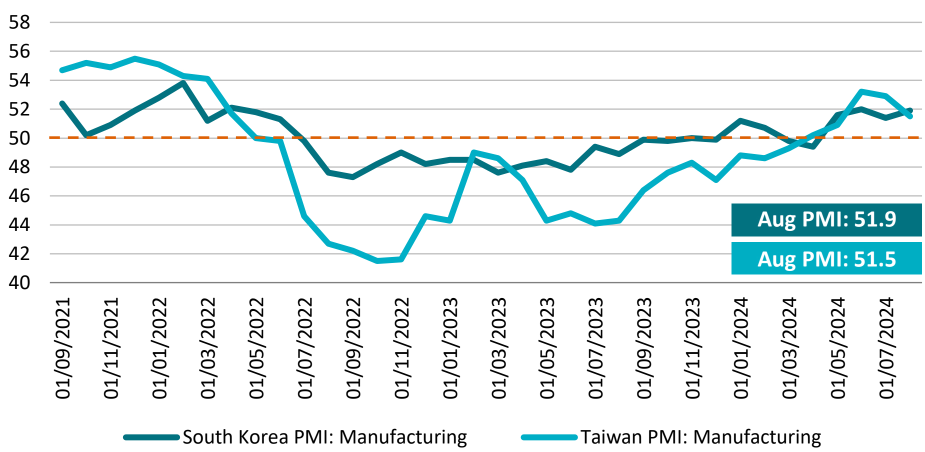
Asia-Pacific manufacturing holding up, powered by AI

Despite worries about artificial intelligence (AI) overhype, US capital goods imports remained robust over the past year, driven by industrial machines, computers, computer accessories and semiconductors - likely due to AI-related investment and spurred on by the 2022 CHIPS act. In contrast, consumer goods imports have largely returned to pre-pandemic levels.

This resilient investment in technology is supporting Asia's tech trade. The initial winners of the investment cycle have been the enablers – infrastructure firms, storage providers and chipmakers. Asia ex-Japan has the highest share among the major regions of enabler companies, primarily in the semiconductor and hardware supply chain. Taiwan, followed by South Korea, are the market leaders and industry bellwethers.

Taiwan recorded sharp growth in chip exports of 89.8% year on year to September 2024, while South Korea's rose by 44% over the same period. This has contributed to both countries' manufacturing Purchasing Managers' Indices staying resilient despite the global growth slowdown. The drivers are undoubtedly narrow and could be derailed if demand falters, but for now, with under-investing in AI perceived by many corporates as a bigger risk than over-investing, the cycle likely has further to run.

| Manufacturing Purchasing Managers' Index: South Korea and Taiwan



Source: Bloomberg, September 2024

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		Easing cycle in full swing but much is already priced in
US Treasuries		Market already priced for significant rate cuts in 2025
Euro – Core Govt.		Little value right now with ECB rate cuts priced in
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		Market pricing not discounting any post-election inflation shock

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		Soft landing to support stocks into year-end
US		Lower rates should sustain confidence in earnings
Europe		Attractive valuations, along with positive economic and earnings surprises
UK		Relatively more attractive valuations and positive economic momentum
Japan		Benefiting from semiconductor growth. Reforms and monetary policy in focus for broader performance
China		Policy announcements may lead to improved growth and market performance
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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