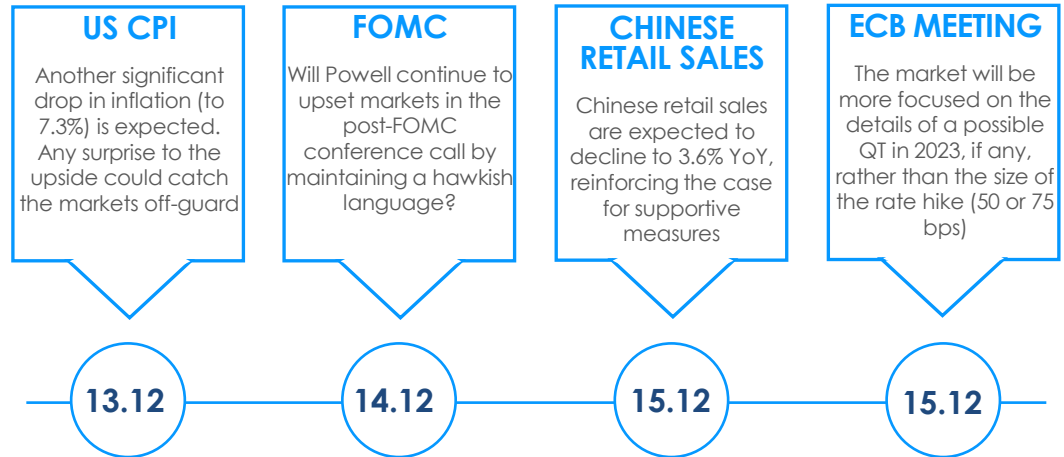


## Main Events

### Azimut Global Network

- \* Milan
- \* Abu Dhabi
- \* Austin
- \* Cairo
- \* Dubai
- \* Dublin
- \* Hong Kong
- \* Estoril
- \* Istanbul
- \* Lugano
- \* Luxembourg
- \* Mexico City
- \* Miami
- \* Monaco
- \* New York
- \* Santiago
- \* São Paulo
- \* Shanghai
- \* Singapore
- \* St Louis
- \* Sydney
- \* Taipei

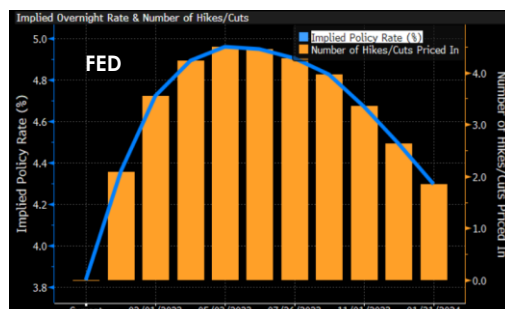


## READING THE SIGNS (AND CURVES)

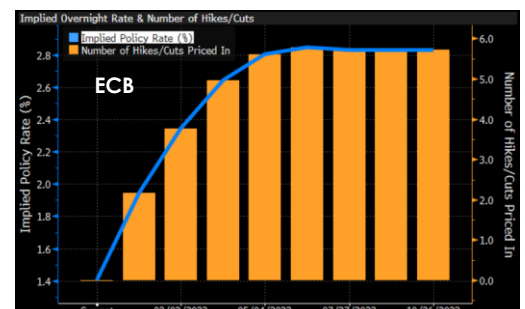
- **Although central banks continue to signal higher rates for longer, markets are still expecting them to come down shortly**
- **Short- and long-term rates have never been at lower levels than official rates when central banks ended their rate-hiking cycle**
- **Despite the fact that the rate hike cycle is still ongoing, short- and long-term rates in the US and Europe are currently lower than official rates, exposing government bonds to renewed downside risks**

As long as central banks implemented monetary policies that favored asset class price increases, the market motto was "don't fight the Fed (or the central banks)". The opposite has been true ever since central banks started implementing tight monetary policies to combat inflation.

Financial markets throughout 2023 have wanted to see a pivot much sooner than when that pivot has come (or will come), and most importantly, markets have always been willing to believe that it was the rise in interest rates that was transitory (rather than inflation, as central banks erroneously claimed a year ago). The market already expects that official rates will not even reach the level that central banks have repeatedly heralded. Despite Powell's repeated claims that interest rates will remain higher for longer, the market also expects the U.S. interest rate to start falling as soon as the cycle of rate hikes ends.



Source: Bloomberg



Source: Bloomberg

(continued)



Source: Bloomberg



Source: Bloomberg

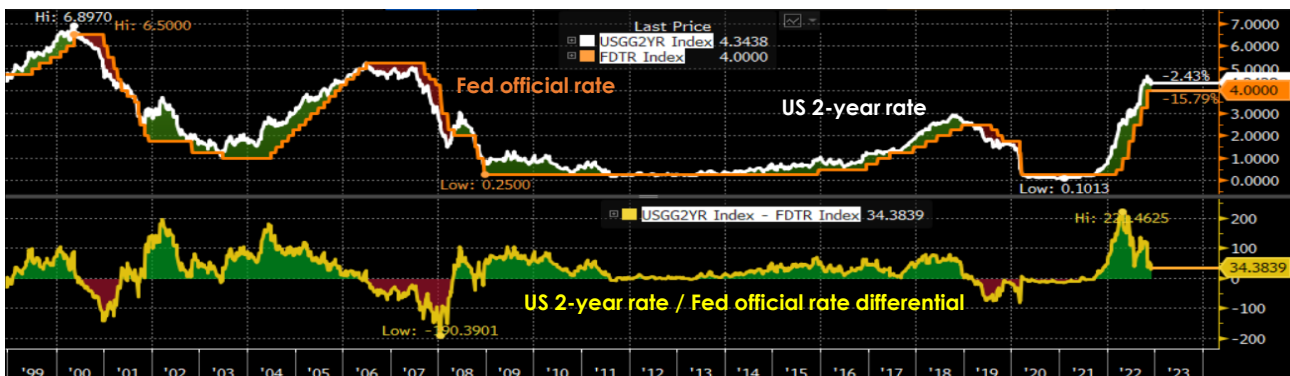
Interest rates in both the United States and Europe have retraced violently, since talk of a pivot began in mid-October, especially in the long end. The U.S. 10-year fell 85 bps from the highs, returning to levels first touched in June, at the time of the first of the four 75 bps hikes, and before the Jackson Hole meeting, when Powell made it clear that interest rates would have risen more than the market expected, and would have remained at that higher level for a fairly long time so as not to repeat the mistakes of the 1970s and 1980s when the Fed started cutting rates prematurely.

In Europe, although inflation has risen from 8.1% in May (last announced figure in mid-June) to 10.0% today, the 30-year German yield has fallen by nearly 90 bps, returning to levels lower than the highs reached in June, when official rates were still at -50 bps.

The short ends, which are more sensitive to official rates, dropped less. Nevertheless, in both Europe and America, market rates have returned to the levels touched immediately after the Jackson Hole meeting despite the fact that the FED and ECB have both raised rates by 150 bps since then, and are continuing to say they will raise them more than expected, but evidently the market does not want to believe it.

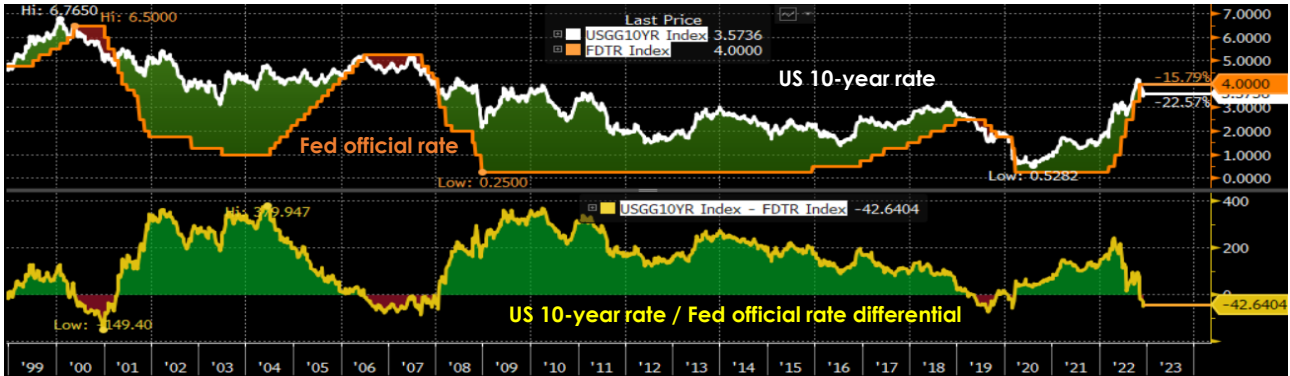
Looking at past evidence, it is quite likely that the euphoria of recent weeks is ill-placed. Comparing the official rates with the 2-year rate, we see that the latter has been at the same level (2006) or at a higher level (2000, 2018) than the official rates each time the rate hike cycle has ended (this evidence is also verified in earlier occasions). Given that the Fed is anticipated to increase rates by at least 50 basis points (if not 75 basis points) in ten days, the 2-year rate is currently lower than what official rates will be following the December Fed meeting, leaving the assumption that 2-year rates must be higher than official rates when the rate hike cycle ends untested.

The move of the 2-year back below 4.2% (from a high of 4.8% in early November) exposes the short-ends of the US curve to further downside in the event that the Fed raises rates above 5% as it has indicated it will. Obviously less severe than those experienced in 2022, but nonetheless of some significance.



Source: Bloomberg

(continued)

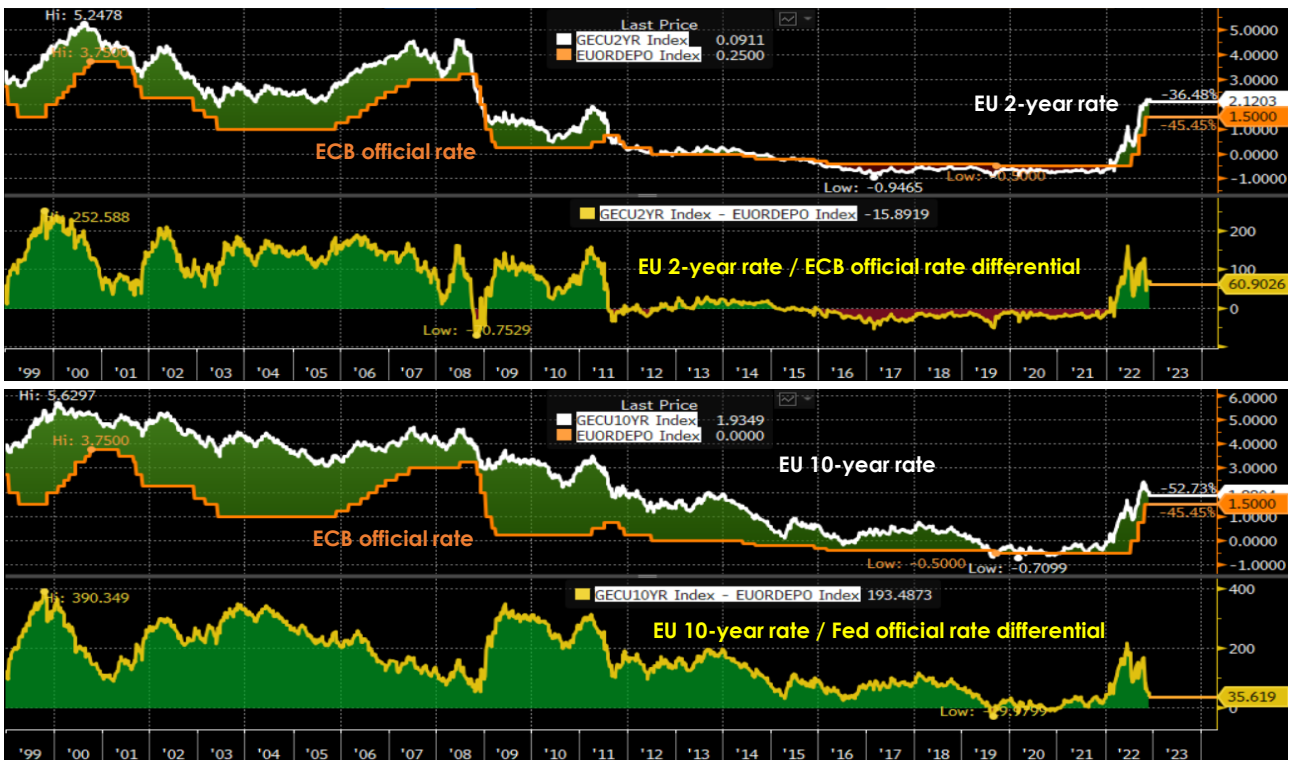


Source: Bloomberg

If we compare the official rates with the 10-year rate, we observe that by the time the tightening cycle ends, the 10-year is already at the same level (2000, 2006) or just higher (2018) than the official rates. Soon after, the difference between the two falls into negative territory, signaling that the rate hike was strong enough to cause an economic slowdown, which often turns into a difficult-to-stop recession (interest rates begin to rapidly decline, the stock market experiences significant corrections).

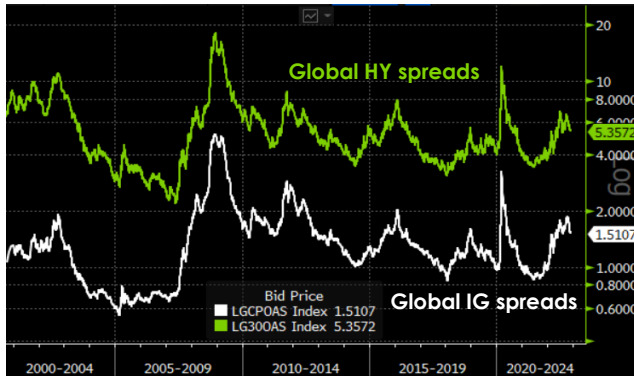
Again, 10-year interest never fell below the official rate before the rate hikes ended. The 10-year (currently at 3.57%) is already lower than the official rate (4.00%) even before rates are increased once more in December. If official rates were raised to at least 5% and history were to repeat itself, long-term interest rates would have a fairly large downside again, having to rise over 5%, and, considering their duration, the potential downside for 10-year bonds would become significant again.

In Europe, whenever the rate hike cycle has ended, the 2-year and 10-year rates have always been at higher levels than the official rates, in a range of +60 to +150 bps. Today, the 2-year yield is above the official rate by only 60 bps, while the 10-year is only 35 bps higher. It is not yet clear whether the ECB will raise rates by 50 or 75 bps at its December meeting. If the hike were only 50 bps, the spread with the 2-year would be barely positive, but already negative with the 10-year. In the case of a 75 bps hike, both differentials would be negative. Also here, market rates seems too low.



Source: Bloomberg

(continued)



Source: Bloomberg

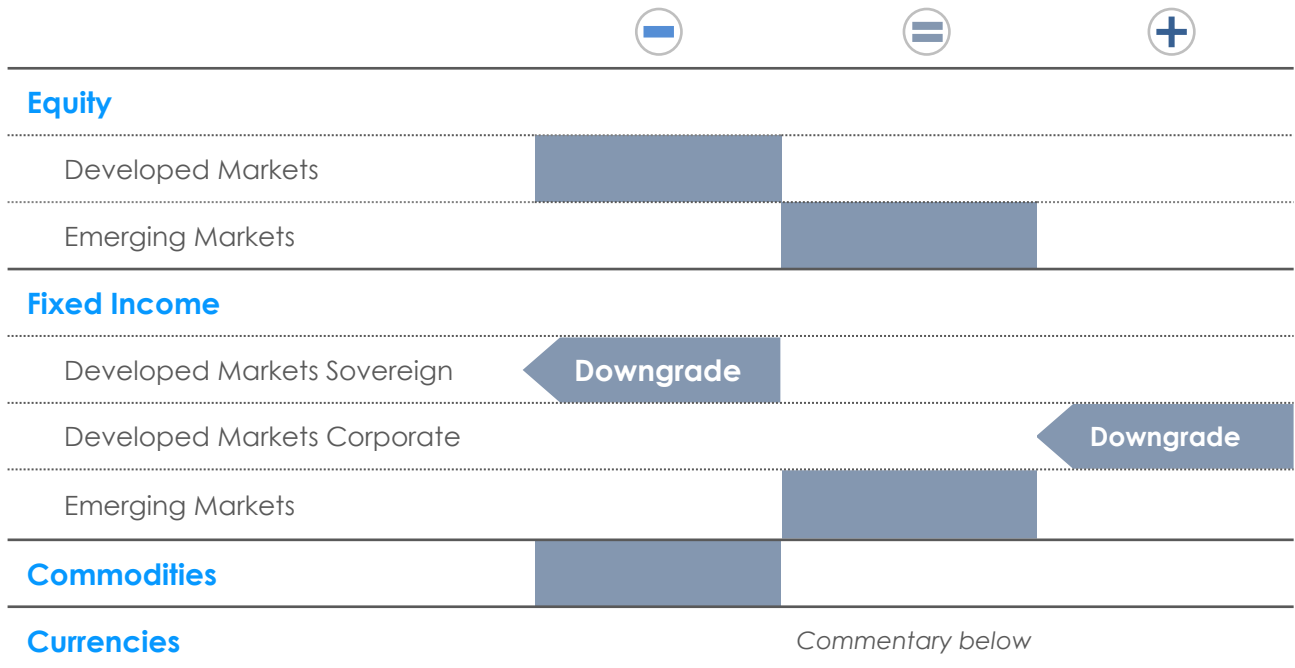


Source: Bloomberg

Since October, corporate bond spreads have also compressed significantly. Investment-grade spreads narrowed by about 35 bps, and high yields have shrunk by 120 bps. These levels of spreads are still attractive, although less so than a couple of months ago, given that for the time being the economic cycle seems to remain very resilient. If, on the other hand, fears arise of a possible pronounced economic slowdown or outright recession, spreads could easily return to the levels preceding this compression.

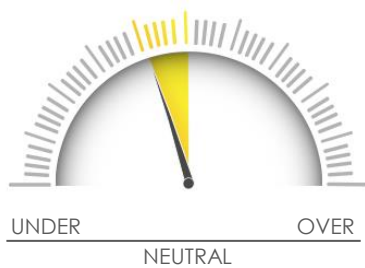
Finally, it remains to be seen how the central banks will react to such movements when they meet next week for their last meeting of 2022. Financial conditions in the United States seem to be the most closely monitored variable by the Federal Reserve so far: whenever these became significantly more accommodative, Fed members have always reacted by sending messages that are decidedly hawkish. The strongest easing of financial conditions in all of 2022 has occurred since mid-October. The possibility that the market could be caught off guard is not negligible.

# Asset Allocation View



## Equity

### Developed Markets



We maintained our **Slightly Underweight** recommendation on Developed Markets Equities. Equity markets' upside potential has been significantly reduced by the recent rebound, and there is still a chance of at least a brief retracement, especially if interest rates begin to rise once more as predicted in the prologue. We reiterate our view that the "Santa Claus rally" may have already occurred in November and that a more cautious approach until the end of the year may be warranted.

US



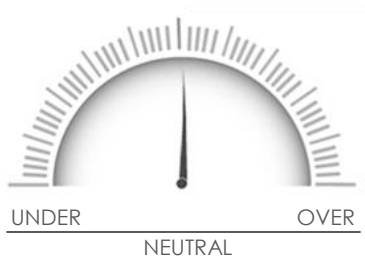
Europe



Japan



### Emerging Markets



We maintained our recommendation on Emerging Markets Equities as **Neutral**. Despite the substantial rebound achieved by emerging countries over the past month, growing evidence that China is effectively abandoning its zero-covid policies and enacting measures to support the real estate sector may allow emerging markets to continue to outperform.

Asia ex-Japan



EEMEA

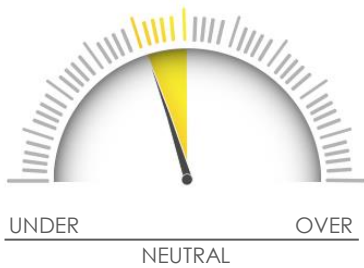


LATAM



## Fixed Income

### Developed Markets Sovereign



We decreased our recommendation on Developed Markets Sovereign Bonds by two notches to **Slightly Underweight**. The substantial reduction in both short-term and long-term interest rates that has occurred in developed countries over the past few weeks has brought rates back to levels that are no longer attractive. The risk, as elaborated in the prologue, is that the curves will rise again, given that interest rates are currently well below the level to which central banks intend to bring the risk-free rate.

EU Core



EU Periphery



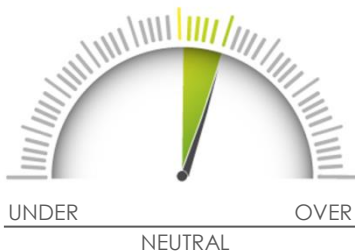
US Treasury



Japanese JGB



### Developed Markets Corporate



We reduced our recommendation on Developed Markets Corporates to **Slightly Overweight**. The significant spread compression that has taken place over the past two months along with the reduction in risk-free rates has led to a not insignificant reduction in the YTM of corporate bonds. Given the strength of the business cycle, spread levels are still considered attractive, at least for the investment-grade bonds. High yield spreads, on the other hand, are still perceived as being too low.

IG Europe



IG US



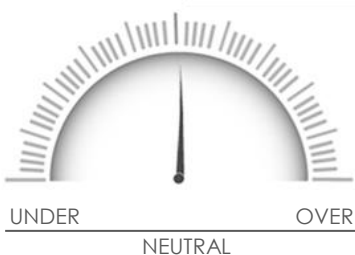
HY Europe



HY US



### Emerging Markets



We maintained our **Neutral** recommendation on Emerging Market bonds. Developing market bonds have recently benefited from the dovish turn of some central banks and the Chinese government's change in stance towards Covid measures and real estate. The latter development could continue to support the asset class, even if rates in developed countries begin to rise again.

Local Currency



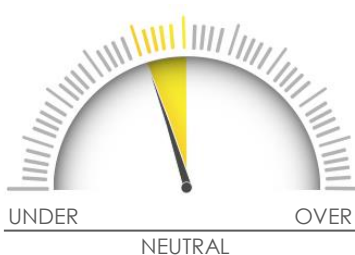
Hard Currency IG



Hard Currency HY



## Commodities



We maintain our **Slightly Underweight** recommendation on Commodities. With no ability to generate cash flow, precious metals face competition from government bonds. Considering the additional steps towards a relaxation of the Covid-containment measures in China and the supportive measures for the Chinese real estate sector, it is possible that Energy and Industrial metals sectors may extend the rebound from the recent lows.

Precious



Energy



Industrial



Agricultural



## Currencies

The Committee confirmed its **Neutral** View on the US Dollar. The decline suffered by the greenback during the past month has been significant. Given the unfavorable momentum, a continuation of the bearish trend cannot be ruled out. Nonetheless, given the strength of US macroeconomic data, a return to strength is possible at any time, particularly if the Fed uses more hawkish tones than expected at its mid-December meeting.

The view on the Euro is also **Neutral**, waiting for more clarity after the ECB December meeting. If Lagarde announces a 75 bps hike and/or the start of a QT, the Euro may have further room to strengthen. If, however, this does not happen, the risk of a retracement after the recent rally is considerable.

The view on the **Chinese Renminbi** has been confirmed as **Neutral**. The relaxation of Covid measures and the approval of supportive measures for the real estate sector will keep the Renminbi strong.

On the **other emerging market currencies**, we maintain a **Neutral** stance considering on the one hand the risk of a possible global slowdown, and on the other hand the decrease in rates in Western countries.

Euro		USD		CNY		Other EM	
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