

Institute

#07-08  
July-August  
2022

# CROSS ASSET Investment Strategy

CIO VIEWS

Play the desynchronization of the cycle

AMUNDI INSTITUTE

The emerging markets hurdles

Confidence  
must be earned

**Amundi**  
ASSET MANAGEMENT

## #07/08 - July-August 2022

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The ECB is determined to tighten its monetary policy in the face of record high inflation levels. However, it is addressing that risk by cooling inflation down or pushing the economy into recession or triggering a spike in peripheral debt borrowing costs, as in 2012. The markets are already sounding the alarm about what may lie ahead. Italian government bond yields jumped past 4% this month for the first time since 2014 as investors are concerned about the ECB's first step in normalising its monetary policy.

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CIO VIEWS

Play the desynchronization of the cycle



Vincent MORTIER,  
Group Chief Investment Officer



Matteo GERMANO,  
Deputy Group Chief Investment Office

Dramatic price action has taken place over the past weeks in equities and bonds, following hot inflation prints, central bank (CB) actions and rising concerns over economic growth. **These events are a reminder of the regime shift, in which we are witnessing the resurgence of stagflationary risks and central banks trying to assert their credibility.** Going forward, growth, inflation and central banks' policies will continue to drive markets:

**(1) Growth:** We were already expecting a deceleration of growth at the start of the year, but we are now moving to a marked slowdown, particularly in the euro area, with the risk of a technical recession. This is mainly due to weak private consumption and investment in Europe (which is most impacted by inflation). In contrast, in the US stronger private consumption and investment should continue to support growth. But we expect a marked slowdown and rising recession risks for 2023. The market is going to focus on the growth path and, in particular, on any signal of deterioration in the US outlook.

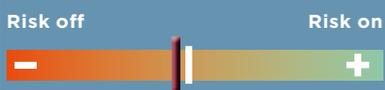
**(2) Inflation – not yet at the peak, with different drivers in the US and Europe:** The expected peak in inflation has been postponed, while the peak level has moved higher than initially thought. The inflation drivers are different in the US and Europe, with inflation more demand-driven in the US, while in Europe, the primary reason for inflation has been supply constraints, with the energy shock from the war further exacerbating the outlook. In an environment of slowing growth, inflation should also slow.

**(3) Central banks have the difficult task of restoring their credibility:** In general, monetary tightening is more effective when inflation is driven by strong internal demand. However, when inflation is caused by external factors (supply constraints), then CB tightening is not very successful in taming inflation. Thus, there is more scope for tightening in the US, while the ECB is in a worse position as it also has to address EU fragmentation, as signalled by the announcement of a dedicated anti-fragmentation tool by the ECB. Overall, we believe that when inflation peaks and attention turns to growth trending lower, central banks will likely pause and deliver less than initially stated.

**Against this still highly volatile backdrop, investors should stay diversified** and avoid adding risk as the market repricing, although advanced, is not over yet. This is the time to move towards high-quality areas and resilient business models that can preserve margins. In particular:

- **The recent bond sell-off makes this asset class selectively more attractive**, as CBs' hawkishness is now priced in and at a certain point, they could be forced to do less to avoid a recession or further fragmentation. The current levels are also becoming more attractive for investors such as insurers and pension funds and that could cap the potential further upside in yields. **We are more positive than before and close to neutrality on duration in the US and core Europe**, but keep an agile approach overall. In euro peripheral debt, we remain neutral and are closely monitoring the fragmentation risks.
- **Credit – we recommend moving towards higher quality credit** and being more selective in general across the credit spectrum (IG and HY), given some concerns over earnings. However, our regional preference for US IG remains in place in light of the strong consumption and labour markets in the country. This should help deliver better economic growth.
- **Equities** – we keep an overall vigilant stance and given that in Europe further earnings downgrades are not fully priced in, we are cautious due to the headwinds from high inflation, which could dampen consumer demand. The US, on the other hand, should fare relatively well and we maintain a preference for the US. In terms of style, investors should opt for the less cyclical areas in equities in value, quality and dividend oriented stocks. Companies with strong balance sheets and pricing power, as well as the ability to pass rising costs on to consumers and preserve margins, should do well.
- **We are becoming slightly more positive on Chinese A shares** as these appear more insulated from the developed world, where stagflationary risks are surging. We also expect this asset class to benefit from the reopening of the Chinese economy and the stimulus in place.
- **For diversification purposes, investors should consider commodities and strategies with low correlation to equities and bonds.** On currencies, we keep our preference for the USD versus the Euro and, to a lesser extent, for the Yen.

Overall risk sentiment



In a stagflationary environment, do not increase risk; instead, stay diversified and move towards more quality, less cyclical areas in equities, credit.

Changes vs. previous month

- ▶ Earnings recession risks make us cautious on Europe in the near term.
- ▶ Positive on China amid reopening and policy support.
- ▶ Less optimistic on yen, as CB sticks to easing.

Overall risk sentiment is a qualitative view of the overall risk assessment of the most recent global investment committee.

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**Big picture in short**



**Pascal BLANQUÉ,**  
Chairman, Amundi Institute

*The greater the gap between what central bankers say and what people believe, the higher the cost of bringing inflation under control may be*

**Central banks in search of credibility**

Western monetary policy has executed an impressive U-turn in the space of a few weeks. The Federal Reserve announced the biggest interest rate increase since 1994 and the European Central Bank is gearing up to hike soon. There was market turmoil, investors questioned the credibility of central banks and the probability of recession began to rise. The greater the gap between what central bankers say and what people believe, the higher may be the cost of bringing inflation under control since significant monetary policy tightening will be needed to rein in expectations about how fast prices will rise.

Most people today have never before been confronted with sustained periods of high inflation. The current collective memory has instead been shaped by an environment where central banks were more concerned about undershooting their inflation targets and were free to act to support growth. However, the decades of low inflation had less to do with monetary policy and more to do with other factors (coincidences), such as China's entry onto the world economic stage, which depressed international labour costs. Now that inflation expectations are becoming unanchored, a new approach is needed. I see three main scenarios:

- 1. 'Credible disinflation':** The recent collective memory of low inflation prevails, and central banks' credibility is restored. In this scenario, an economic soft landing could be engineered. Financial markets would return to the pre-crisis situation that was characterised by relatively low rates and slim risk premia. This is more or less what is priced in today, although there have been setbacks in certain overvalued asset classes and market segments. This scenario does not appear likely, unless inflation retreats on its own, a development that would represent good luck on par with the series of coincidences that delivered the low inflation of recent decades.
- 2. 'Incredible disinflation':** Central banks started out too far behind the curve, and are racing to prevent long-dormant inflation memories from resurfacing and becoming entrenched. Monetary policy actions would be painful for markets and economic activity, but necessary to curb inflation. In this scenario, investors should take shelter and wait out the storm. There would be a recession and asset price bubbles would burst, but then there would be a return to normal. This is a viable option but policymakers probably lack the resolve to fight this long and hard battle.
- 3. 'Incredible inflation':** Central banks have not fallen behind the curve by chance or by mistake, but are undergoing a profound change. They will tolerate higher inflation to foster nominal growth. This implies a structural change in the public's psychology as well, and higher inflation expectations would become the norm. In this case, equities would do better than feared and real rates would remain low for some time, postponing - but not eliminating - the recession risks. In this scenario, investors should look to tackle inflation through real assets. This is a credible alternative to the current consensus view.

Discover our new **Global Investment Outlook for H2 2022**  
"Life above zero: investors' journey at a time of rising rates"



			<b>Most likely</b>
<b>Scenario</b>	<b>Credible disinflation</b>	<b>Incredible disinflation</b>	<b>Incredible inflation</b>
<b>Probability</b>	 <b>LOW</b>	 <b>MEDIUM</b>	 <b>HIGH</b>
<b>Outcomes</b>	Inflation retreats on its own and an economic soft landing can be engineered.	Tough monetary policy action brings inflation under control but also results in recession.	Central banks tolerate higher inflation to foster growth. This produces a lasting shift in inflation expectations.
<b>Implications</b>	<b>POSITIVE</b> Markets return to pre-crisis levels, with low rates and slim risk premia.	<b>VERY NEGATIVE</b> Asset prices bubble burst and a period of sharp adjustment in financial markets.	<b>POSITIVE FOR EQUITIES</b> Real rates stay low for a while and stock markets perform better than anticipated.

Source: Amundi Institute as of 27 June 2022.

MULTI-ASSET

## Stay cautious with preference for China and US



**Francesco SANDRINI,**  
Head of Multi-Asset Strategies



**John O'TOOLE,**  
Head of Multi-Asset Investment Solutions

*While markets have already seen repricing in equities and yields, we do not think this is over yet. Instead of adding risk, investors should try to benefit from the diverging economic outlooks globally*

The repercussions of the Russia-Ukraine war, energy demand/supply dynamics and CB rate hikes are creating a double whammy for markets. Even as we see pressures on growth, upward pressures on inflation have been building for quite some time (financial repression), and collectively this will affect corporate earnings, particularly in Europe. Policy manoeuvres add another layer of complexity that will tighten financial conditions. **We think investors should explore relative value and play the divergences: stay cautious in European equities, and selectively benefit from the resilience of the US and the economic opening in China.** On duration, neutrality and agility are the way forward. In addition, the positive correlation between equities and bonds underscores a need to diversify via non-traditional avenues such as commodities (e.g., oil, gold).

### High conviction ideas

**While we are marginally cautious on equities,** primarily due to our stance on Europe, we stick with our regional preference for the US. Europe is more affected by the Ukraine crisis and the resulting impact on inflation and demand and weakness in corporate earnings. In EM, as we look for relative value opportunities, we are turning positive on China (vs. India, owing to the inflationary impact of commodities) due to its desynchronization with the global economy and accommodative policies.

**In fixed income, as core yields in the US and Europe have risen substantially and economic growth concerns have emerged, we have been reducing our cautious stance on duration (US, core Europe) and moving towards neutrality.** However, amid the uncertainties over the inflation path and CBs' terminal rates, we remain flexible. In the UK, we no longer believe in the steepening of the 2-10Y curve. The flattening of global yield curves, as a result of significant increases in short-term yields due to hawkish CBs, could put upwards pressure on short-term UK yields. We recommend investors stay

active across curves and geographies to take advantage of any future opportunities.

**On euro peripheral debt, we are less constructive than before on 10Y Italian BTPs.** A hawkish ECB and the general move towards higher core yields has caused some volatility. We are closely watching the ECB's efforts and communication to avoid fragmentation in the Eurozone. **Elsewhere, we think the Fed's resolve to tighten policy could affect EM bonds, where we are now neutral, but the situation is dynamic and we remain watchful.** In credit, we continue to think US IG offers opportunities amid the earnings resilience, strong consumption and corporate fundamentals in the country. However, we are wary of taking directional calls in the HY segment due to the risks of spread widening and a further increase in defaults. There are opportunities to gain from the spike in volatility, but we remain selective.

**Not surprisingly, policy decisions by CBs are affecting FX markets.** We are less constructive on JPY (vs. the EUR) now after the Japanese central bank decided to stick to its easing stance, which should weigh on the yen. But we maintain our positive view on CHF/EUR and our cautious stance on EUR/USD amid the wide interest rate differential in favour of the US. The dollar should continue to do well against the CAD. In EM, although we stay cautious on FX in general, we remain positive on the BRL vs. PLN and HUF. The real should benefit from higher commodity prices whereas Poland and Hungary are commodity importers and physically close to the Ukraine crisis.

### Risks and hedging

**Hedging costs have been rising because of a significant increase in volatility.** We recommend investors evaluate the cost-efficiency of hedges and maintain protection on credit, FX and equities. Investors should build protection keeping in mind the potential risks of the upcoming earnings seasons and recession (limited for now).

### Amundi Cross Asset Convictions

	1 month change	---	--	-	0	+	++	+++
Equities				■				
Credit & EM bonds	↘					■		
Duration	↗				■			
Oil	↘				■			
Gold					■			

Source: Amundi. The table represents a cross-asset assessment on a three- to six-month horizon based on views expressed at the most recent global investment committee. The outlook, changes in outlook and opinions on the asset class assessment reflect the expected direction (+/-) and the strength of the conviction (+/+\*\*/+\*\*\*). This assessment is subject to change.

CGB = Chinese government bonds, EM = emerging markets, PBoC = People's Bank of China, FX = foreign exchange, IG = investment grade, HY = high yield, CBs = central banks, BTP = Italian government bonds, EMBI = EM Bonds Index, QT = quantitative tightening.



FIXED INCOME

Govies and investment grade credit in focus



**Amaury D'ORSAY,**  
Head of Fixed Income



**Yerlan SYZDYKOV,**  
Global Head of Emerging Markets



**Kenneth J. TAUBES,**  
CIO of US Investment Management

While volatility may persist amid the uncertain growth/inflation outlook, the current level of yields make the government bond space more attractive than before

Inflationary pressures, persistent bottlenecks and tightening financial conditions might lead some DM into recession. CBs are acting aggressively to control inflation, and as a result short-term rates are likely to go above the neutral rate. The main questions for markets are how much monetary tightening is essential and what the effect will be on consumer demand and corporate earnings.

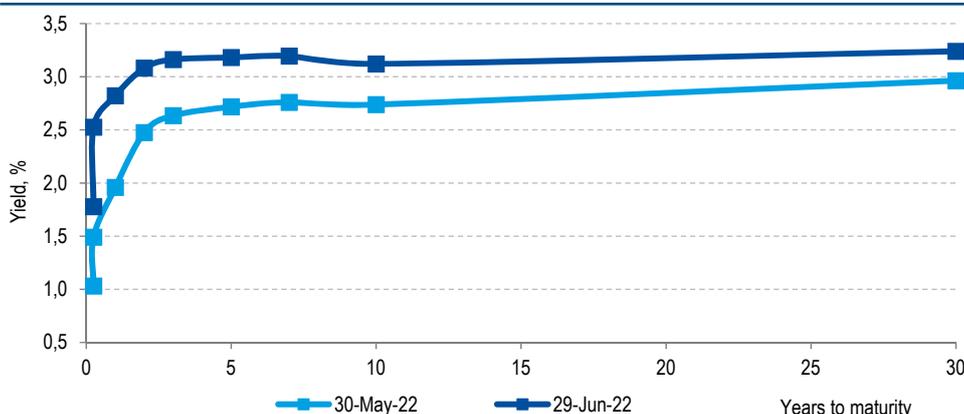
**On yields, we may see some further volatility, but current levels are more attractive considering the direction of growth is down and inflation is reaching its peak. On credit, there is a need to consider more quality assets in the portfolio, and stay clear of high-risk, leveraged areas.**

**Global and European fixed income**

We remain close to neutrality on duration in general but keep a flexible stance across geographies and curves due to the ambiguity on terminal rates, inflation and economic growth fears. For instance, **in Europe and the UK, we are slightly cautious to neutral, but remain defensive in the US.** In breakevens, we believe the aggressive Fed stance could cause upward movements in real rates, and hence we are no longer positive there. In peripheral debt though, we stay neutral as we monitor the evolution of ECB policy and how the central bank addresses the issue of EMU fragmentation through its yet-to-be-clarified anti-fragmentation tool.

**Chinese bonds continue to offer diversification opportunities.** In credit, there are selective opportunities to benefit from new issue premiums. In general, **we prefer US IG over EU** and believe fundamentals are robust, but we could see some weakening as growth and liquidity concerns percolate through to risky segments. Thus, investors should maintain sufficient buffers and move away from risky names towards quality A-rated, more liquid securities.

**US yield curve further repriced in June**



Source: Amundi Institute, Bloomberg, data as on 29 June 2022.

GFI = global fixed income, GEMs/EM FX = global emerging markets foreign exchange, HY = high yield, IG = investment grade, EUR = euro, UST = US Treasuries, RMBS = residential mortgage-backed securities, ABS = asset-backed securities, HC = hard currency, LC = local currency, MBS = mortgage-backed securities, CRE = commercial real estate, QT = quantitative tightening



EQUITY

A moment of truth for earnings



Kasper ELMGREEN,  
Head of Equities



Yerlan SYZDYKOV,  
Global Head of Emerging Markets



Kenneth J. TAUBES,  
CIO of US Investment  
Management

Pricing power is key and this is not the time to compromise on balance sheet strength because it is only a matter of time before earnings come under pressure

Overall assessment

We have been highlighting for some time now that valuations are not completely justified given the economic growth risks on the horizon, but this has only dawned on markets recently. **Collectively, growth fears, aggressive tightening by CBs and high inflation led to the recent sell-off.** Looking ahead, we think earnings growth may be impacted by the fall in disposable incomes, rising financing costs and higher input costs (earnings revisions may come down). However, this effect will not be felt equally in all sectors, regions and businesses. Companies that have pricing power and display product differentiation should fare better. **Security selection is the key to long-term returns, while we also play regional divergences – preference for the US and China in the near term.**

European equities

In a challenging environment for Europe, we believe rising input prices and rates will weigh on corporate earnings and valuations. We also note that valuation dispersion is high across sectors and think investors should maintain a barbell exposure, with defensive stocks (healthcare, staples) on the one end and value, cyclical names (materials, industrials) on the other. **However, it is important to stay balanced, maintain a quality tilt across portfolios and focus on companies' pricing power and balance sheet strength.** This is because businesses that are able to pass on rising input costs to consumers are likely to preserve margins. Thus, we maintain selection as our primary driver of risk. We remain cautious on IT and utilities, particularly in areas with expensive valuations and where we believe the risk return trade-off is not attractive.

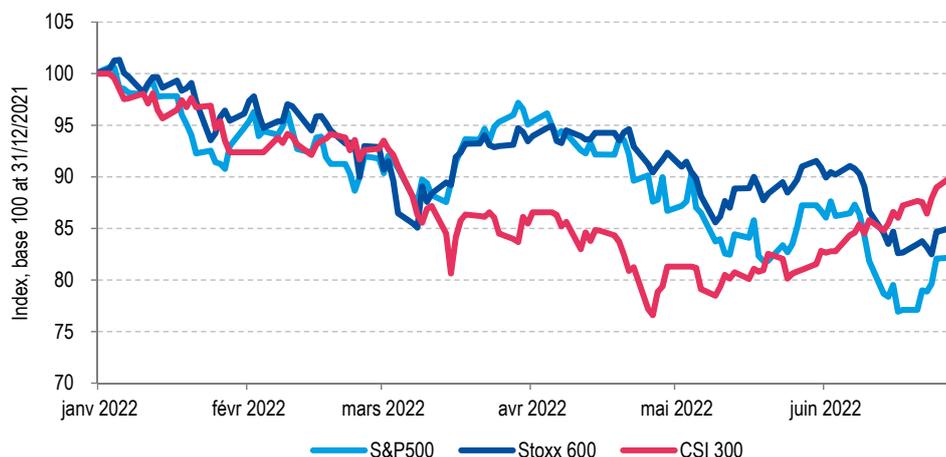
US equities

The 'wealth effect' (loss of asset value that discourages discretionary spending), coupled with high inflation, may cause growth to slow but a recession is not our base case. The recent correction has reduced valuations, but multiples are not cheap and companies are still exposed to the risk of an earnings correction as margins are high at the moment. On the other hand, high inflation and slower growth are the consensus now, though are not completely understood by the markets. **We stick to our conviction on companies that reward shareholders through buybacks/dividends and maintain operational efficiencies in an environment of higher input prices.** We see such companies in the quality, value segments of the markets that are reasonably priced. In addition, we are exploring profitable names in certain growth areas as they have become attractive following the correction, but selection remains crucial. However, we are cautious on unprofitable growth names and look for stable returns on equity. Value names and US banks demonstrate this characteristic, along with select names in energy, materials and healthcare. But we focus on the less cyclical and more quality oriented areas of the market.

EM equities

We maintain a prudent stance as global uncertainties remain. **Attractive valuations, coupled with strong divergences, persist at country level, allowing us to be very selective** and favour commodity exporters (Brazil, UAE). In China, sentiment has turned favourable, especially on the discretionary side due to an expected rebound in demand. Overall, we maintain our preference for value over growth.

Regional divergences in equity market performances set to continue



Source: Amundi Institute, Bloomberg, as of 27 June 2022.

THEMATIC  
GLOBAL VIEWS

Didier BOROWSKI,  
Head of Global Views

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*The freezing of the Russian central bank's assets following the invasion of Ukraine was a reminder to all sovereign investors that their allocation choices have a strategic dimension*

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## Renminbi's rise will not challenge dollar dominance

A sharp economic slowdown seems to be looming in both Europe and the US, which would make bond markets attractive again, especially in the US. Conversely, the Chinese economy is expected to reaccelerate. International monetary system set to become multipolar as geopolitical factors are likely to prevail.

Inflation's return will impact the strategic allocation of all long-term investors, especially central banks and sovereign funds. The Federal Reserve is normalising monetary policy swiftly, which has caused a rapid rise in long-term interest rates in the US and, to a lesser extent, Europe. This has helped strengthen the dollar.

At the same time, **a sharp economic slowdown (or even recession) seems to be on the cards in both Europe and, possibly, the US.** This would give many investors the opportunity to reposition themselves in US Treasuries. At current levels, US bond yields are becoming more attractive compared to Chinese bond markets. **When inflation slows, which we expect to happen in 2023, US bond yields will become even more attractive.**

**Does this mean that the dollar will continue to dominate the international monetary system?** This old question resurfaces from time to time. Despite major structural changes in the monetary system over the past 60 years, the dollar remains the dominant international reserve currency. Yet the dollar's share of global reserves has fallen to 59% from 71% in 1999, when the euro launched. This shows that central banks were gradually moving away from the dollar before Russia's war in Ukraine. Some expect this trend to continue or even accelerate as central banks in emerging economies seek to further diversify their reserve mix.

**The freezing of the Russian central bank's assets following the invasion of Ukraine was a reminder to all sovereign investors that their allocation choices have a strategic dimension.** The US administration - through Treasury Secretary Janet Yellen - is now promoting the concept of 'friend-shoring', whereby countries commit to working with others that adhere to a set of norms and values about how to operate in the global economy and how to manage the global economic system. Western countries, seeking to increase their resilience and strategic independence, will naturally take this argument into account. Recall that, **historically, military strength and monetary dominance are intertwined.** Countries around China will, for this very reason, seek to increase their exposure to the renminbi, at the expense of the dollar. The launch of the digital yuan will certainly help them to do so.

**The long-term impact the war in Ukraine will have on the international monetary system is uncertain.** It depends on how countries react, as geopolitical factors will increasingly be taken into account. In a fragmented and multipolar world there can no longer be one dominant currency. There is no doubt that **the yuan will become more international, but this may be limited to a few countries.** While the renminbi will play an increasingly important role, it will not supplant the dollar.

*Finalised on 24 June 2022*

## THIS MONTH'S TOPIC

## The emerging markets hurdles



**Alessia BERARDI**,  
Head of Emerging Macro and  
Strategy Research



**Debora DELBO'**,  
Senior EM Macro Strategist

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*Current geopolitical and macro environment increase the probability of idiosyncratic crisis with low probability to become systemic*

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*The policy mix has been incrementally less supportive in particular on the Monetary Policy side*

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While not envisaging any systemic risk propagating across emerging markets, the macro financial outlook remains challenging amid growth concerns, still-high inflation and tighter global financial conditions. The current geopolitical environment, with its impact on macro and financial conditions, is making an idiosyncratic crisis more likely.

**While not envisaging any systemic risk propagating across emerging markets, the macro financial outlook remains challenging amid growth concerns driven by softening domestic demand and decelerating global demand, uncomfortably high inflation triggering yet more monetary policy tightening, and shifting global financial conditions from extremely accommodative to tighter ones.**

Although, by nature, it should not result into systemic destabilisation, **the current geopolitical environment**, which is not expected to improve anytime soon, **with its repercussions on macro and financial conditions, is increasing the probability of idiosyncratic crisis across the EM** as well as raising the necessity of intervention by international institutions such as the IMF. In the case of Turkey, its high energy bill and ongoing important stimulus to the economy are deteriorating its external accounts further and increasing the risk of a balance-of-payments crisis once relief from summer tourism receipts has gone. Low-income countries' debt-servicing capacities have diminished sharply, magnified by high energy and food import prices and by the need to keep expensive subsidies in place. Amidst ad hoc measures (such as Pakistan's super tax hike) and more structural reforms under discussion, more countries are trying to negotiate new, or re-establish existing, IMF programs, while the Common Framework is advancing only slowly in offering comprehensive debt restructuring.

As far as growth is concerned, on the domestic demand side, several governments are trying to limit the erosion of household purchasing power from the spiking cost of living, by extending measures introduced during the pandemic or enacting new ones, such as price caps, higher subsidies, lower excise taxes and several other non-monetary measures. Generally, this is softening domestic demand at only a slow pace. Having said that, for commodity importers the impact is even more negative and not negligible on the fiscal accounts, in absence of any mitigation from higher revenues, dividends and royalties as it happens for commodity exports. Since the beginning of the year, budget balance targets for 2022 have been on a deteriorating path for many Ems, with the exception of Gulf countries, several Latam America countries, South Africa and few countries in Asia, such as Malaysia and Indonesia, where we do expect more stable economic conditions rather than a proper improvement. The complexity and heterogeneity of the universe appears even more striking when we look at countries

that should actually benefit from the current environment but do not. In Nigeria, the obsolete production system as well as the amount of oil disappearing from the official accounts is making it hard to benefit from relatively high oil prices while, on the contrary, its fiscal position is suffering from the high costs of fuel subsidies.

**The withdrawal of policy stimulus put into place after the pandemic outbreak on the fiscal side as well as the normalisation of monetary policy that began in early 2021** (even earlier in China, in the second half of 2020) **is going to weigh incrementally on economic activity and domestic demand.** Significantly high inflation has allowed real policy rates to stay supportive for long even in the middle of the current monetary policy tightening cycle. Only few EM countries are closer to positive real rates (China, Brazil, and Mexico, to name some). **The inflation uptrend has been stronger than expected and mostly driven by volatile global factors, such as energy and food; moreover, the absence of demand pressure, due to longer mobility restrictions together with effective subsidies policy, has differentiated the inflation picture in Asia in comparison with Latam and CEEMEA.** Looking at the next six months, on the back of a more benign trend in oil and commodities prices (in comparison with the peaks seen in the first half of the year), as well as a wider supply bottlenecks adjustment (already visible in declining freight costs on some routes), inflation dynamics should stabilise and then moderate. In our expectations, **the first and boldest hikers will get there earlier than other EMs. Brazil has already reached this turning point between April and May.**

Contrary to what normally happens, emerging markets embarked on the transition of monetary policy away from their extraordinary dovish conditions much earlier than developed markets. **The wave of monetary policy normalisation has continued unabated until today and is still not done. In particular, regarding the external drivers of EM monetary policy, while the Federal Reserve had turned more hawkish relatively late, since then, the hawkish bias has increased in tone and actions that have been undertaken.** With that to consider, EMs have more than domestic drivers to look at and increasingly tight global financial conditions have made EM monetary policy authorities more prudent. Some CBs have abandoned a premature narrative of neutral or easier MP stance while others have finally started to hike, absent any Inflation pressure so far.



THIS MONTH'S TOPIC

*Chinese economy expected to get traction after the transitory recession*

However, considering our EM inflation outlook, as well as the house outlook vis-à-vis Fed hiking (with a terminal rate of around 3.75% by early 2023), US yields and the USD, the EM monetary policy turning point, starting from few countries, has been only slightly pushed forward from the end of 2022 to early 2023.

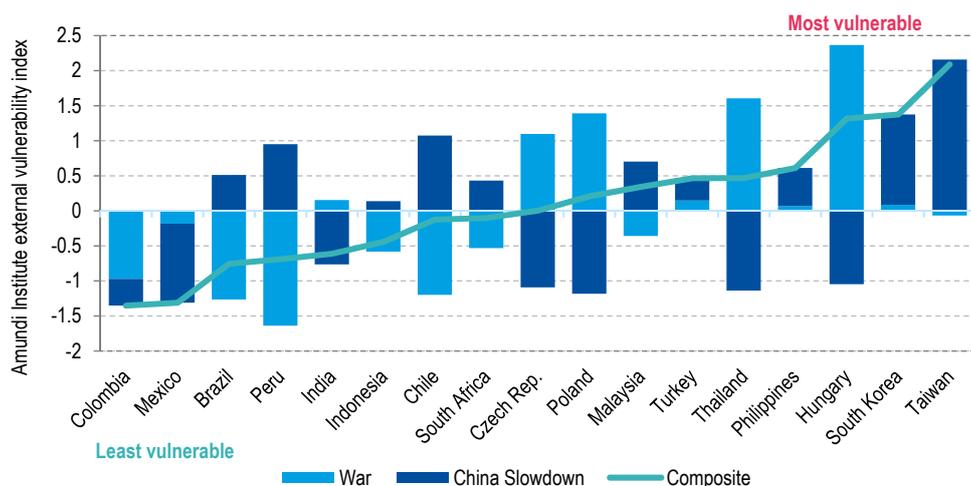
Coming back to the growth dynamics from an external angle, it's worth highlighting that, in the aftermath of the conflict in Ukraine, global growth expectations have been revised down sharply and, almost simultaneously, we have seen a resurgence of local lockdowns in China. All of a sudden, global demand has become an orphan of its most important contributors – European growth will flirt with zero/negative rates; US GDP has been significantly revised down; and China is expected to perform less robustly than the official growth target set in late 2021 (around 3.5% YoY vs 5.5% YoY). Across the EM, some partial relief will come from the commodity boom for the commodity exporters, alleviating/offsetting the demand deceleration. Indeed, recent trade balance figures are highlighting clear positive dynamics

between commodity exporters while negative for the commodity importers; only across Asia the different Trade Balance trends between Indonesia and Philippines highlight that. Unfortunately, more protectionist measures aiming at directing raw material production to the domestic market instead of exporting it are partly limiting the benefit of commodity high prices.

**As far as China is concerned, the enforced lockdown is likely to have sent China into a transitory recession in Q2. However, since April, new Covid cases have fallen and activities have been recovering steadily, and a realistic assumption would be for reopening continuing to get traction moving forward.** Our H2 China growth outlook is far more constructive on these assumptions. Together with the reopening, China has been pursuing economic policies on its own: it is on an easier monetary policy path and supportive fiscal policy path that has sped up since May. The improvement in the outlook in China is an important pillar for the EM growth story to hold up relatively well moving forward.

*The gloomy macro backdrop appears priced by the markets*

1/ War and China slowdown heighten fragmentation across EM



Source: Amundi Institute on ComTrade, IMF, CEIC, Bloomberg. Data is as 15 June 2022.

*Positive catalysts for the Chinese Equity markets*

In recent months, it looks as if the **emerging asset classes have already discounted most of the aforementioned negative environment.**

Yields have been spiking in both hard and local currencies debt, while the EM currencies have depreciated significantly vs USD, with the only exception being the Russian rouble and a few Latam currencies. Meanwhile, equity markets have underperformed more acutely in the EMEA region, penalised by the conflict proximity and increasing uncertainties on growth and inflation expectations.

Over the next few months, we expect markets to remain on high alert, with a focus on growth slowdown and inflation dynamics (stagflation risk) and a possible shift in geopolitical risks.

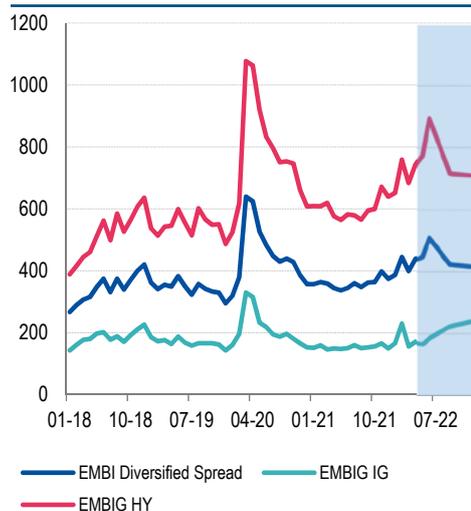
Having said that, it's fair to add some **possible positive catalysts.** High frequency indicators are confirming the story that China has bottomed out and that the worst

is behind us. In 2021, Chinese equity markets suffered a prolonged sell-off, starting with the implementation of a new regulatory framework whose impact has affected mainly the tech and property sectors, amplified by policy tightening and the lack of clarity on the delisting issue. Although these elements are taking time to fade away and are contributing to a very volatile environment, they should already be priced into Chinese equity market valuations. **The deceleration in the regulatory effort as well as more supportive policy signals, together with the ongoing lifting of restrictions should help the recovery in the H shares market,** which has been neglected by investors in recent months. At the same time, domestic A shares should benefit from the current domestic policies, aimed to boost domestic demand and domestic production, showing attractive entry points at this stage.



**THIS MONTH'S TOPIC**

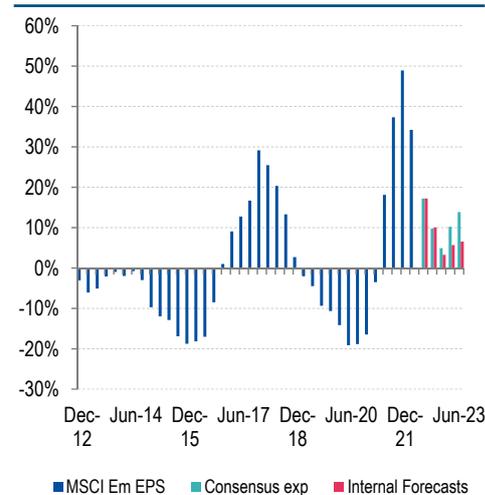
**2/ HY EMBI Diversified spread expected to tighten**



Source: Bloomberg & Factset, Amundi Institute - Data as of June 2022

Moving into the second half of the year and early 2023, the macro drivers resulting in a wider growth premium in favour of EMs should set a floor on certain emerging asset classes that have so far underperformed significantly. Commodity exporters in the emerging space are benefitting from the substitution effect (vs Russian oil and gas) and from improving terms of trade. Inflation is stabilising/peaking, with some decline expected over the next few months, albeit remaining at higher levels than pre-pandemic. With a strong USD, we recommend high selectivity and tactical positioning on the EM FX markets (commodity exporters, a brighter growth outlook and a sound MP environment). **In the fixed-income space, we continue to prefer the hard**

**3/ MSCI EM - EPS forecast - USD**



Source: Bloomberg & Factset, Amundi Institute - Data as of June 2022

**currency segment, high yield over IG, and taking advantage of a strong US dollar and a still sustained oil price.** For the time being, we see less support for local debt even though stable (or not spiking) US 10y yields, together with stabilising, if not turning, local monetary policies could soon offer some attractive entry points. The first hikers, like some Latin America countries, are seeing, or will see soon, inflation peaking and the end of the monetary policy tightening cycle. Eastern European countries offering attractive carry will be late on the same path. An increase in geopolitical uncertainty and the consequent increase of stagflationary risk represent the main risk for emerging markets debt.

*Finalised on 28 June 2022*

## THEMATIC



**Valentine AINOUZ,**  
Deputy Head of Developed  
Markets Research

*Skyrocketing inflation  
remains the ECB's top  
priority*

*Tighter monetary policy  
is increasing financial  
fragmentation across the  
Eurozone*

*The ECB's ability to raise  
rates will depend on  
the strength of its anti-  
fragmentation tool*

## The ECB's ability to raise rates will depend on the strength of the anti-fragmentation tool

The ECB is determined to tighten its monetary policy in the face of record high inflation levels. However, it is addressing that risk by cooling inflation down or pushing the economy into recession or triggering a spike in peripheral debt borrowing costs, as in 2012. The markets are already sounding the alarm about what may lie ahead. Italian government bond yields jumped past 4% this month for the first time since 2014 as investors are concerned about the ECB's first step in normalising its monetary policy.

### High inflation remains a major challenge

- In May, Eurozone headline inflation reached another record of 8.1%. Inflationary pressures have been exacerbated by the war in Ukraine and ongoing lockdown measures in China. Global supply chains remain under pressure. Energy prices stand 39% above their levels of one year ago.
- We do not expect headline inflation to peak before October. In addition, underlying inflation has been rising further and could continue to surprise on the upside in the second half of the year. On the one hand, more and more companies should continue to raise their prices to compensate for the record jump in production costs. On the other hand, demand in the Eurozone could be supported by targeted government support or rising wages.

### The European Central Bank remains determined to fight against inflation.

- The ECB remains much more focused on the risk of inflation expectations becoming unanchored than on the downside risks weighing on growth. "The longer inflation numbers are at the high level where they are, the more likely it is that wages negotiations, entry-level salaries, and renegotiations of existing agreements will actually take place." (Christine Lagarde).
- Central banks are afraid of losing their credibility. "Inflation is undesirably high and is expected to remain above our target for some time." "The Governing Council will make sure that inflation returns to our two per cent target over the medium term." (Christine Lagarde).
- We are therefore maintaining our forecast of a 25bp hike in July, followed by 50bp hikes in September and October.

### In tackling the path of inflation, the ECB faces two dilemmas:

- A central bank has few "tools" to fight cost-driven inflation without hurting growth. Indeed, inflation in the Eurozone is being driven primarily by exogenous factors, including high-energy costs and supply chain disruptions. The ECB wants to tighten its monetary policy to limit the spread of price rises across sectors.
- Tighter monetary policy is increasing financial fragmentation across the Eurozone. When it comes to financial fragmentation, we need to watch peripheral government bond yields and not just spreads. The cost of debt cannot be higher than nominal growth, over a long period, for heavily indebted countries. They are wary of high level of debt in Europe, in particular in Italy.

### The ECB's ability to raise rates will depend on the strength of the anti-fragmentation tool.

- The markets are already sounding the alarm. Italian government bond yields jumped past 4% this month for the first time since 2014, as investors are concerned about the ECB's first step in normalising its monetary policy.
- ECB sovereign debt purchases should be targeted. Inflation levels no longer allow the ECB to implement large-scale asset purchase programs to keep peripheral sovereign bond yields at low levels. The ECB wants to limit upward pressure on spreads using: (1) flexibility in PEPP reinvestment and (2) an "anti-fragmentation tool". We expect the details of the new backstop to be announced in July.
- At the Forum of Central Banks in Sintra, the ECB President, Christine Lagarde, explained that "the new instrument must be effective while being proportionate and including sufficient guarantee mechanisms to preserve the momentum of the Member States towards a sound budgetary policy". The challenge for the ECB is to tread the fine line between the remit of the governments and that of the central bank.
- The ECB's ability to raise rates will depend on the strength of the anti-fragmentation tool
- Developments on the euro rate market will strongly depend on developments in the energy sector, political choices (fiscal support) and monetary choices (arbitrage between inflation and growth, anti-fragmentation tool).

Finalised on 29 June 2022

## CENTRAL & ALTERNATIVE SCENARIOS (12 TO 18 MONTHS HORIZON)

### Monthly update

We keep the probabilities of our central and alternative scenarios unchanged vs. last month. The new wave of Covid-19 and stagnation in the Eurozone are adding growth uncertainty over the short-term.

DOWNSIDE SCENARIO 30%	CENTRAL SCENARIO 60%	UPSIDE SCENARIO 10%
<b>Renewed slump toward stagflation</b>	<b>The great divergence</b>	<b>Inclusive and sustainable growth</b>
<b>Analysis</b>	<b>Analysis</b>	<b>Analysis</b>
<ul style="list-style-type: none"> <li> <b>Long-lasting war in Ukraine</b> is hurting confidence and activity, and pushes commodities and energy price higher for longer and disrupting supply.</li> <li> Russia cuts gas supplies to Germany, which enters a recession in 2023.</li> <li> <b>Covid-19</b> resurgence leads to global renewed mobility restrictions and bottlenecks disrupting supply chains.</li> <li> Both triggers lead to an <b>economic downturn</b> while <b>inflation</b> remains elevated and uncontrolled.</li> <li> <b>Several EM</b> default and public debt sustainability concerns in DM.</li> <li> <b>Renewed monetary and fiscal accommodation</b> to support the economy, possibly a further step in financial repression.</li> <li> Inflation amid slower growth, forces some <b>Central Banks</b> and the ECB in particular, to <b>deviate</b> from their guidance and potentially lose credibility.</li> <li> Policies and investments designed to fight <b>climate change</b> are postponed and/or countries policies are disorderly implemented.</li> </ul>	<ul style="list-style-type: none"> <li> The <b>war in Ukraine</b> is hitting confidence and maintains elevated commodities and energy prices.</li> <li> <b>Covid-19 is an endemic disease</b>, with random contagion waves (China); global activity holds up, but supply-chain bottlenecks to persist.</li> <li> <b>Rising growth divergence:</b> <ul style="list-style-type: none"> <li>• Global growth progressively abate to trend in 2022, opening 2023's to downside risks.</li> <li>• Rebound expected in China in H2, after the GDP contraction in Q2</li> <li>• Stagnation or technical/short-lived recession in EZ and the UK</li> <li>• The US economy is resilient, but expected to slow down towards subpar growth in 2023 (rising recession risk).</li> </ul> </li> <li> <b>Headline inflation is peaking</b>, but will remain elevated. High commodity prices, supply-side bottlenecks and rising wage pressures will push core inflation up in some regions (e.g. the EZ).</li> <li> <b>CBs follow different paths:</b> <ul style="list-style-type: none"> <li>• Fed to continue to hike rates aggressively (short run); but to adopt a more dovish stance in H2</li> <li>• BoE in a soft hiking cycle</li> <li>• ECB to hike rates 3x in H2, but no room for a real tightening cycle (recession risk)</li> <li>• PBoC to keep an easing bias</li> <li>• Bond yields to move higher but to stay low for longer</li> </ul> </li> <li> <b>Fiscal policy:</b> to smooth the short-term impact of energy prices (through targeted measures, notably in Europe).</li> <li> <b>Climate change</b> disrupts the commodity cycle and adds to stagflationary trends.</li> </ul>	<ul style="list-style-type: none"> <li> <b>End of the Ukraine war</b> and sanctions are gradually withdrawn. Lower energy and commodity prices and inflation falls back quickly.</li> <li> <b>Endemic recedes</b> faster than anticipated, despite variants.</li> <li> Extra savings and wage rises fuel <b>consumption</b> with low erosion of corporate margins.</li> <li> <b>Productivity gains</b> thanks to digital and energy transitions and structural reforms</li> <li> <b>Inflation</b> remains under control and CBs are gradually normalising.</li> <li> <b>Higher nominal and real interest rates</b>, due to stronger investment and less savings.</li> <li> <b>Debt is sustainable</b> thanks to strong growth and a gradual shift towards fiscal discipline.</li> <li> <b>Inclusive growth</b> and effective fight against inequality.</li> <li> <b>Climate change</b> policies and energy transitions become first priority.</li> </ul>
<b>Market implications</b>	<b>Market implications</b>	<b>Market implications</b>
<ul style="list-style-type: none"> <li>– Favour cash, USD and US Treasuries</li> <li>– Play minimum-volatility strategies</li> <li>– Gold</li> <li>– Commodities and energy</li> </ul>	<ul style="list-style-type: none"> <li>– Lower risk-adjusted real returns expected</li> <li>– Contained steepening of US Treasuries yield curve as well as EZ and EM</li> <li>– Inflation hedge via gold, linkers and equities</li> <li>– EM: Short-term caution, long-term real income and growth story intact</li> </ul>	<ul style="list-style-type: none"> <li>– US Treasuries curves bear steepen</li> <li>– Favour risky assets with cyclical and value exposure</li> <li>– Favour linkers and equities as an inflation hedge</li> </ul>

 Geopolitic  Covid-19 related topics  
 Growth and inflation expectations  
 Monetary and fiscal policy

 Recovery plans or financial conditions  
 Solvency of private and public issuers

 Economic or financial regime  
 Social or climate related topics

**TOP RISKS**

**Monthly update**

We maintain the probabilities of economic, financial and (geo)political risks to 30%. We consider Covid-19-related risks (including lockdowns in China) to be part of the economic risks. Risks are clustered to ease the detection of hedging strategies, but they are obviously linked.

**ECONOMIC RISK**  
30%

- **Global recession** driven by an oil and gas shock, and a deteriorating sentiment as the war in Ukraine stalls
- **Economic crisis in Eastern Europe** following a collapse of the Russian economy, elevated energy prices, uncontrolled inflation and a migrant crisis
- **Pandemic 3.0**
  - After Omicron (2.0) a more dangerous and vaccine-resistant variant starts a new wave
  - New lockdowns or mobility restrictions could further undermine the global recovery
- **Supply chain disruptions** carry on (China lockdowns), and input cost pressures lead to corporate earnings recession
- **China zero Covid policy combined with regulatory crackdown and property market collapses**, leading to lower growth prospects
- **Monetary policy mistake**
  - Central banks' miscommunication in the context of a high geopolitical uncertainty
  - Central banks underestimate the strength of supply driven inflation and lose control
- **Climate change-related natural events** hurt growth visibility and social balance.

 Cash, linkers, JPY, Gold, USD, Quality vs. Growth, Defensive vs Cyclical, Oil

 Risky assets, AUD CAD or NZD, EM local CCY

**FINANCIAL RISK**  
30%

- **Sovereign debt crisis**
  - An extended war in Ukraine would hurt DM vulnerable public finance with public debt as a share of GDP already at historically high levels
  - De-anchoring inflation expectations could lead to harsher monetary tightening and a bond market dislocation
  - Most countries are vulnerable to rating downgrades and rising interest rates
  - EM weaknesses could also face a balance-of-payments crisis and increased default risks
- **Corporate solvency risk increases**, amid deteriorating fundamentals, rising uncertainty and corporate margins under pressure (high input cost, double orders lead to profit warnings)
- **Widespread greenwashing and ESG investment bubble** undermine the energy transition funding
- **USD instability** and gradual loss of its reserve currency status lead to unstable currency markets
- **Currency wars**: currency appreciation is a way for CBs to fight inflationary pressures

 CHF, JPY, Gold, CDS, optionality, Min Vol

 Oil, risky assets, frontier markets and EMs

**(GEO)POLITICAL RISK**  
30%

- **War in Ukraine**
  - Short term resolution following Russia military success: markets instability remain as investors are starting to price in Putin crossing new red lines
  - Prolonged military struggle leading to a high intensity conflict and potentially western military confrontation
- **EU political fragmentation** or populist vote bring a disagreement on how to manage the relationship with Russia
- **The US takes a hard line with China** in order to block any tentative to invade Taiwan. Risk of accidental confrontations in the South China Sea or the Taiwan Strait
- **EM political instability driven by** higher food and energy prices, leading to a wave of unrest similar to the Arab Spring
- Iran or North Korea nuclear programs renewed concerns and sanctions
- **US & China lose credibility** on the energy transition and undermine the Paris agreement
- **Global warming** leads to an increased risk of conflicts, driven by water shortages and migratory movements
- **Cyber-attack or data compromise**, disrupting IT systems in security, energy and health services

 DM Govies, Cash, Gold, USD, Volatility, Defensive, Oil

 Credit & equity, EMBI

CROSS ASSET DISPATCH: Detecting markets turning points

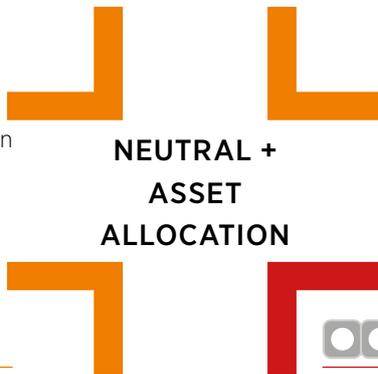
- The turning point has occurred
- Approaching the turning point
- Not reached yet too early to call it

●●● ECONOMIC BACKDROP

- Despite noisy GDP data blurring the reading of underlying trends, economic momentum is slowing progressively amidst higher and not abating inflationary pressures and weakening domestic demand: food and energy inflation hit household purchasing power, operating as a regressive tax, while unabated pipeline pressures on the cost side put margins under stress.
- Directions of revisions on inflation and growth outlooks keep diverging as higher and higher inflation prints remain the key factor dragging down confidence and capping growth. Stagflationary pressures are particularly evident in the Eurozone.
- The prolonged stress on commodities and energy prices, leading to more persistent inflation and tighter monetary policies is exacerbating economic uncertainty, given a much less benign picture for the growth and inflation mix.

●●● FUNDAMENTALS & VALUATION

- Despite some recent tentative rebounds, markets are still not that stretched, although they are not discounting a recessionary environment and not suggesting meaningful entry points.
- QT will address inflation issues, keeping multiples from expanding, while expectations are still very optimistic, at least in Europe, considering the potential shortages of raw materials.



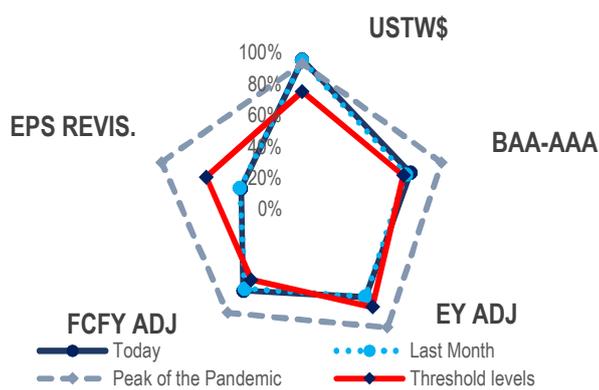
●●● TECHNICALS

- In the first part of June most risky assets touched extremely oversold levels, with RSIs and contrarian indicators (Bull/Bear, Fear&Greed) calling for a mean reversion.
- At the end of the month, a relief rally occurred and contrarian signals moderated lower. The lack of visibility and the poor momentum (risky assets trends remain highly fragmented), keep suggesting an overall neutral exposure from a technical perspective.

●●● SENTIMENT

- Most risky assets kept correcting lower in the first half of June, as the hawkish response from CBs increased the probability of a global slowdown for the next couple of years.
- Risk concentration in the market remains high and the overall risk-off probability keeps suggesting a defensive allocation in the short-term.
- The Moody's Baa-Aaa spread breached alert levels in June, showing a transmission from a weaker economy and a stronger USD. Financial conditions kept tightening globally to respond to more persistent inflation.

Cross Asset Sentinels Thresholds (CAST) still supportive



The CAST risk perception failed to show a structural increase in Q1. EPS revisions have started showing a less benign global outlook, and the USD remains the dimension calling loudly for risk-off. Yet credit risk premiums failed to jump above our alert threshold (i.e., 100 bps) and are partially balancing the overall assessment.

**Methodology:** We consider five inputs, which we call "sentinels": USTW\$, Moody's Baa-Aaa, EPS revisions, Adjusted Earnings Yield Risk and Adjusted Cash Flow Yield Risk. These sentinels are used to reposition our tactical asset allocation. Once sound thresholds are detected, the five variables are aggregated as an indicator that anticipates the market's stress conditions, with a certain level of conviction. The pentagon visualises the five sentinels, where the red line represents the alert threshold. The greater the distance above the red line, the greater the risk perception, and eventually the need to move closer to a defensive asset allocation.

Source: Amundi Institute, Data as of 24 June 2022

## GLOBAL RESEARCH CLIPS

**1 Central Banks determined to fight inflation**

- **The ECB's** policy rate hike will depend on its ability to limit financial fragmentation.
  - EZ fragmentation is the biggest threat the ECB is facing as it raises rates.
  - A remake of 2011 is unlikely as the cost of debt is lower, nominal growth prospects are higher, and anti-fragmentation tools are already there
  - By accelerating the completion of the design of a new anti-fragmentation instrument, the ECB has shown a commitment to prevent the impairment of monetary policy transmission. As a result, a remake of summer 2011 should be avoided.
- **The Federal Reserve** plans to raise rates above neutral by yearend. The FOMC wants to pursue a more aggressive front-loading of rate increases, increasing the probability of a recession in the US.
- **Bank of England** likely to be capped on tightening by a deteriorating economy. We're the most dovish on BoE vs the markets.

**Investment consequences**

- CB terminal rates: US @ 3.75% (slightly below the markets), ECB @ 1.25% and BoE @ 1.75% (both dovish vs the markets).
- Neutral on peripheral bonds, with flatter curves.

**2 Lower growth and higher inflation is still the name of the game**

- DM: faster deceleration to below trend growth for the US; stagnating growth for the EA with the rising risk of an outright recession.
- EM: We are revising 2022 Chinese growth on the downside, while upgrading commodity countries Brazil and South Africa.
- The war in Ukraine is having a various impact among EM countries, with some clearly benefiting from higher commodities & energy prices. The aggregate growth revision is flat, despite the downgrade to Chinese growth.

**Investment consequences**

- Positioning for stagflationary environment confirmed: equities still UW, OW inflation assets, UW in credit and OW govies & linkers.

**3 Chinese equities: bad news is priced in**

- More supportive policy signals and a gradual lift of the restrictions are leading to a more positive growth outlook
- Several factors behind the fall of Chinese equities since the beginning of 2021:
  - new regulatory reforms, impacting mainly tech and property stocks;
  - geopolitical tensions exacerbated by the conflict in Ukraine, followed by rising inflation and monetary policy tightening by most central banks around the world;
  - delisting headwinds from the U.S. Holding Foreign Companies Accountable Act (requiring the companies listed on US stock exchanges to declare they are not owned or controlled by a government);
  - Zero Covid tolerance.
- More supportive policy signals and a gradual lift of the restrictions in place (positive for growth) should stabilise the equity markets in the near future.
- China can be a good opportunity as a value trade, now that investors are looking to position themselves in an environment of high inflation.
- Fundamentals of MSCI China are calling for a rebound in the index from the correction that has taken place since 2021.

**Investment consequences**

- Long H shares, rates and commodities.

**4 Japanese equities decoupled from the yen**

- In 2021 structural and cyclical forces supported a weaker JPY: Japan's fundamentals weakened the most across DM, and ultra-loose monetary policy made JPY very attractive for funding strategies.
- We see a regime shift for 2022 onwards: fundamentals still justify a weak currency, and we see no imminent risks that the BoJ will change its dovish stance. Yet cyclical forces and competition challenges suggest most of the negative pressure should be behind us.
- Recessionary-like scenarios favour JPY and penalise Japanese equities:
  - JPY has been pushed lower by structural and cyclical forces, but if a recession occurs the currency would be among the main beneficiaries;
  - A recession would instead penalise Japanese equities, it being a cyclical market.

**Investment consequences**

- We see limited depreciation from current levels and expect a reversal of some of the recent losses over the next 12 months.
- USD/JPY targets, 129 in 6M (consensus: 130), 122 in 12M (consensus: 126).

## GLOBAL RESEARCH CLIPS

**5 Concentration risk is elevated by historical standards**

- Volatility on rates is outpacing volatility in equities and FX.
- Historically, when the correlation among risk-sensitive assets rises, systemic risks turn much more acute.
- The ongoing risky assets sell-off has started with a low risk concentration as most of the move was translating into higher stocks volatility. The more the bear market has matured, the more gold and CHF have performed well, adding to the risk concentration.
- The current reading is above our internal alert, but we believe it may be too early for a mean reversion. The JPY has lagged its usual diversification pattern and its comeback may keep supporting a higher concentration.
- Although Amundi's risk concentration index is currently above the alert level, we believe it may be too early for a mean reversion.

**Investment consequences**

- Tactically defensive cross asset allocation: ptf beta <1 and OW cash.

**6 Markets are not yet discounting a recession**

- The correction has closed the overvaluation. Now beware of the challenging environment ahead.
- What is priced in: the ongoing shift towards tighter monetary policy due to the elevated inflation regime.
- What is NOT priced in: the possibility of a profits or economic recession. The current underlying market narrative is not fully discounting the deteriorating margins, or the poisoned mix of liquidity drain, the deterioration in financial conditions, and productivity disruptions that have been starting to materialise.

**Investment consequences**

- Prices would therefore have to correct materially lower in a scenario of slower economic activity, with a subsequent worsening in employment and a downward revision in earnings.
- We reiterate the case for a cautious allocation towards risky assets over the following months, **pending more visibility on profits.**

**Covid-19 situation update**

**Pierre BLANCHET**, *Head of Investment Intelligence*

As the Covid wave that led to a partial closure of the Chinese economy withdraws, a new wave seems to be emerging in Europe and North America. According to WHO data, the number of cases recorded in Europe has increased from around 900k at the end of May to more than 2.5 million at the time of writing. France is most affected at this stage followed by Germany, Spain and Italy. While the rate of serious cases remains limited in relation to the total volume of cases, there is still an increasing number of deaths. In the United States, the increase in the number of proven cases is less brutal but remains just as real. As a result, the West is about to experience a complicated summer as vacationers begin to move.

The new wave affecting Europe is driven by a new and more contagious BA5 variant of the Omicron family. Some experts are worried by the lack of responsiveness of national authorities and call for a return of social distancing and masks. However, these very unpopular measures will be difficult to put back in place in the summer. Statistics are therefore likely to deteriorate further before health measures are potentially reinstated in September. In China, zero-covid politics can quickly lead to new lockdowns as new cases have emerged in the Shanghai region. Therefore, Covid-19 will keep on affecting our daily lives and constraining economic activity.

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### Chief editor

**BLANQUÉ Pascal**, *Chairman of Amundi Institute*

### Editor

**DEFEND Monica**, *Head of Amundi Institute*

### Amundi Institute contributors

**AINOUZ Valentine**, *Deputy Head of Developed Markets Strategy Research, CFA*

**BERARDI Alessia**, *Head of Emerging Macro and Strategy Research*

**BERTONCINI Sergio**, *Senior Fixed Income Research Strategist*

**BLANCHET Pierre**, *Head of Investment Intelligence*

**BOROWSKI Didier**, *Head of Global Views*

**CESARINI Federico**, *Head of DM FX, Cross Asset Research Strategist*

**DELBO'Debora**, *Senior EM Macro Strategist*

### Deputy-Editors

**BLANCHET Pierre**, *Head of Investment Intelligence*

**BOROWSKI Didier**, *Head of Global Views*

**DROZDIK Patryk**, *Senior EM Macro Strategist*

**GEORGES Delphine**, *Senior Fixed Income Research Strategist*

**HUANG Claire**, *Senior EM Macro Strategist*

**PORTELLI Lorenzo**, *Head of Cross Asset Research*

**USARDI Annalisa**, *Cross Asset Research Senior Macro Strategist*

**VARTANESYAN Sosi**, *Senior Sovereign Analyst*

### With Amundi Investment Insights contribution

**BERTINO Claudia**, *Head of Amundi Investment Insights*

**CARULLA Pol**, *Investment Insights Specialist*

**FIOROT Laura**, *Deputy Head of Amundi Investment Insights*

**DHINGRA Ujjwal**, *Investment Insights Specialist*

**PANELLI Francesca**, *Investment Insights Specialist*

### Conception & production

**BERGER Pia**, *Communication Specialist*

**PONCET Benoit**, *Communication Specialist*