June
2023

MID-YEAR OUTLOOK

CROSS ASSET INVESTMENT STRATEGY SPECIAL EDITION

Opportunities lie beyond precarious path to growth

Trust
must be earned

Amundi
ASSET MANAGEMENT

Monica DEFEND
Head of Amundi Institute

"A central bank pause supports the case for bonds. Investors will have to assess the inflation path and the earnings outlook moving into 2024, in the search for opportunities in equities."

Vincent MORTIER
Group Chief Investment Officer

"Amid low visibility on the economic outlook, quality -- both for equity and bonds -- is the compass with which to navigate this uncertain phase."

Matteo GERMANO
Deputy Group Chief Investment Officer

"Emerging markets are key to enhancing diversification and fostering medium-term return potential, with Asia in focus."

June 2023

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Key CIO convictions for H2 2023

Vincent MORTIER
Group Chief Investment Officer

Matteo GERMANO
Deputy Group Chief Investment Officer

1. Narrow and uncertain path to growth, with a bottom in H2 2023

The lagging effects of tightening in the real economy will lead to a further deceleration in growth with divergences: a mild US recession, anaemic growth in Europe and more resilience in emerging markets. With low absolute numbers, both on the positive (Europe) and negative (United States) sides, the path ahead remains very uncertain.

2. Gradual slowdown in inflation

Inflation is trending lower, but the speed of adjustment is slow as core inflation remains sticky and stubborn. Evidence from past episodes of high US inflation suggests it will take about two years to bring core inflation down by half from its peak level. This is also our view this time.

3. Monetary tightening is close to peaking, but do not expect a U-turn

We believe that Fed and ECB rates are close to their cyclical peak and do not expect any cuts for the remainder of 2023, as inflation remains above central banks' targets and the slowdown is pushed back towards year-end.

4. The growth premium of emerging markets remains wide, with Asia in focus

The resilience in emerging market (EM) growth is leading to a wide growth gap vs. developed markets (DM). We expect Asia to continue to attract investment flows and also to benefit from China and India moving towards more sustainable and inclusive long-term growth models.

H1 2023: mid-year in review

	Themes shaping our 2023 scenarios	Financial markets
Expected	▪ **United States -- Fed pivot:** Inflation on a downward trend, but core inflation sticky, leading to central bank tightening, albeit at a slower pace than in 2022. Fed pause in Q1-Q2 2023. ▪ **Europe -- Energy crisis**: weak economic outlook amid energy crisis**.** ▪ **China -- Growth path**: domestic-driven and reopening.	▪ Confirmation that **bonds are back,** particularly govies and quality credit. ▪ Return of **60-40 portfolios.** ▪ **Weak risky assets outlook**, entry points in Q1-Q2 2023. ▪ **US equity favoured** against other markets. ▪ **Downward US dollar** trend.
Surprise	▪ **United States -- Fed pivot:** US regional bank turmoil. ▪ **Europe -- Energy crisis**: Stabilising energy prices at lower levels, supply diversification averting recession. UK also more resilient. ▪ **China -- Growth path**: earlier than expected reopening, with modest recovery amid property sector woes.	▪ **Strong performance of equity markets**, with different narratives across regions: Japanese and European equities, and US tech. Resilience of EM assets excluding Chinese equities**.** ▪ **Widespread stability in credit spreads** despite financial stress. ▪ **Downside in commodities**, except for gold.

Source: Amundi Institute as of 13 June 2023. DM: developed markets. EM: emerging markets. CB: central banks. Economy and politics themes refer to our 2023 investment outlook.

5. US consumer resilience is a key variable to watch

So far, strong demand has allowed companies to pass through higher costs to consumers, but these benign conditions should fade. Savings will dry up and tighter lending conditions are worsening the outlook for consumers. We expect a deterioration in US sales and EPS.

6. The cyclical outlook calls for a cautious start to H2

The uncertain macroeconomic outlook and weak corporate earnings growth call for allocations to remain cautious as upside is uncertain and downside risks persist, while risky assets valuations are expensive. The summer earnings season could shine some light on the resilience of companies. A Fed pause, moderating inflation and a persistent recovery in earnings should spark the move into a late-cycle phase and be more favourable for equity markets towards the year-end.

“Markets are at a critical juncture as central banks are hitting the pause button after the fastest hiking cycle since the ‘80s. Quality is the compass for navigating this phase.”

7. Rates close to peak support bonds, govies and high-quality credit

Bonds are back is the key 2023 investment theme. Moderating inflation, growth slowing down and a Fed pause will support global high-quality credit, while inflation protection also remains in focus. Investors should stay cautious on high yield, and be mindful of liquidity risk and corporate leverage.

8. Equity: focus on quality, look beyond mega caps and seek to add to cyclical markets

Concentration risk is high, as US equity market upside has been driven by just a few names. Opportunities are now in the quality space in the search for earnings resilience and in moving down the capitalisation spectrum to avoid areas of excessive valuation. Later in the year, the move towards a late cycle could favour cyclical markets, such as Europe.

9. Play emerging markets’ growth advantage in equity and bonds

Attractive valuations, an end to Fed tightening and a possible US dollar depreciation bode well for EM assets. Selection remains crucial, as there are areas of fragile economic conditions and the inflation-monetary policy outlook is mixed.

10. Asset allocation resilient to inflation on the spotlight

Inflation remains above normal levels and calls for additional sources of diversification such as private markets (particularly infrastructure) and hedge funds (global macro). Addressing the direction of inflation will be key to tilting sector allocation towards areas more resilient to inflation.

0

Number of interest rate cuts expected by the Fed and the ECB in H2.

Amundi Institute forecast

4.2%

US annual Inflation, 2023 average (CPI, YoY).

Amundi Institute forecast

3.3%

Expected gap between EM and DM real GDP growth in 2023.

(+4.2% EM vs +0.9% DM),

Amundi Institute forecast

20%

Probability of a deeper profit recession in H2 2023.

Amundi Institute forecast

Investment themes for H2 2023

Bonds and cash in focus

In a decelerating economic backdrop, with rates at their peak in decades, bonds – with a focus on quality – and cash are favoured.

Search for quality in equities

Ongoing high inflation and deteriorating growth will put corporate profitability under pressure. Quality will be key in the search for resilience.

Emerging markets: from West to East

Investors should embrace a dedicated allocation to Asia, to benefit from its growth advantage (around 70% of global growth is expected to come from Asia this year).

Inflation-proofed dynamic allocation

This cycle comes with high uncertainty on growth, inflation, and valuation mispricing. This backdrop offers opportunities for a dynamic asset allocation approach.

ESG themes in focus

Assessing the Net Zero direction and its impact on investment is becoming a key priority at a time when other themes, such as strategic autonomy and food security, are also gaining traction.

Follow the sequence

<table>
<tr><th></th><th>H1 2023</th><th>We are here
H2 2023</th></tr>
<tr><td>Bonds and cash in focus</td><td>▪ US bond duration favoured over euro given the more advanced tightening cycle in the United States.
▪ Global credit in focus.
▪ We have become increasingly cautious on HY.</td><td>▪ Cash, US government bonds.
▪ Global credit with a focus on quality, cautious on HY.
▪ EM HC bonds and seek entry points in EM LC debt.</td></tr>
<tr><td>Search for quality in equity markets</td><td>▪ Play quality, value and high dividends.
▪ Increasingly cautious on the US, particularly mega caps on concentration and fundamentals at risk.</td><td>▪ Seek quality both at a global level and within each region.</td></tr>
<tr><td>Emerging markets: from West to East</td><td>▪ We started adding to China equity to benefit from China's reopening and consumption led recovery.
▪ Start adding to EM bonds from Q2 offering interesting real yields and with most EM CBs at peak of the hiking cycle.</td><td>▪ Start raising EM exposure as currencies should benefit from Fed pause.
▪ With a medium-term horizon, build dedicated allocation to Asian assets, particularly China and India.</td></tr>
<tr><td>Inflation-proofed dynamic allocation</td><td colspan="2">▪ Play dynamic asset allocation to exploit opportunities from evolving economic backdrop with a tilt towards those assets and sectors more resilient to inflation, namely commodities and risk assets, as inflation moderating but staying above CBs' targets.</td></tr>
<tr><td>ESG themes in focus</td><td colspan="2">▪ Look for ESG improvers, net-zero portfolio construction and, more generally, themes on climate change and socially-oriented strategies.</td></tr>
</table>

Source: Amundi Institute as of 1 June 2023. CB: Central banks.

Uncertain growth path calls for allocation to remain defensive

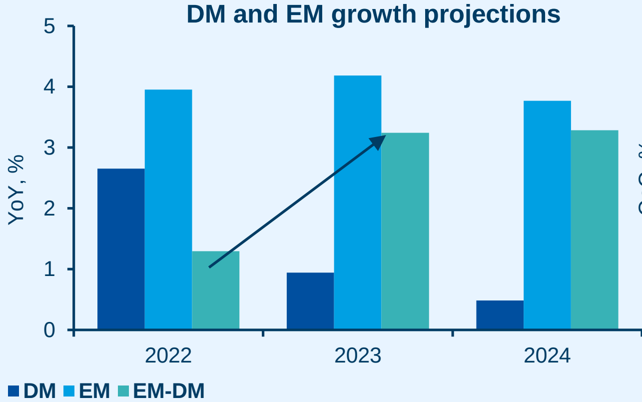
Monica DEFEND
Head of Amundi Institute

"It is time to rein in a defensive stance and look beyond the cyclical slowdown to seek opportunities ahead."

Economic resilience and a smoother adjustment of supply chains and sources (**transformative globalisation)** both in developed (DM) and emerging markets (EM) have led us to upgrade our near-term growth projections **despite the weak global backdrop.** We expect global GDP growth at 2.9% in 2023. DM should slow to 0.9% from 2.7% in 2022, decelerating less than previously anticipated, while EM growth should reach 4.2%, widening the EM-DM growth gap. Despite this, high inflation within a restrictive macro policy setting and a deteriorating geopolitical environment lead us to expect **low overall global growth for 2023.** The growth outlook is even more mixed across regions and countries, especially where upgrades reflect better near-term momentum rather than expected future tailwinds. Monetary tightening is close to a peak, even if its lagged effects are still underway, but we expect a restrictive monetary policy stance to be maintained for an extended period. As such, liquidity should be monitored. Central banks are engaging on two fronts: rate rises to fight inflation and ample balance sheets to preserve the economic cycle and financial stability. **We expect anaemic growth in Europe, while the UK may also avoid recession, amid strong employment and better tax revenue.** High inflation and tight credit conditions should cap household and business spending. Despite below-potential growth, inflation should remain above target up to mid-2024. **Despite some resilience, we expect a mild US recession from Q4 2023** amid tighter credit conditions stemming from ongoing stress in the regional banking sector and the progressive transmission of monetary policy tightening to the real economy. US inflation should remain above target throughout the year.

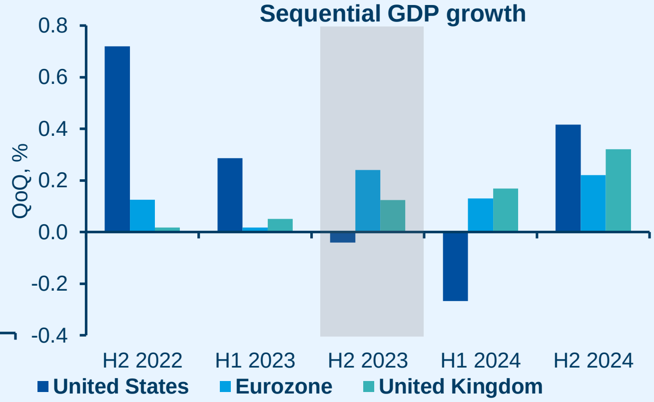
In **EM,** the overall macroeconomic momentum is fragile but resilient, mostly where policy support is stronger. Fiscal support is overshadowing monetary policy support, as most measures to shield consumers from high living costs have not been phased out yet. H2 2023 should see stable, or easier, monetary policy across EM. In **China**, we see 2023 real **GDP growth at 5.7%,** with signs of weakness materialising in housing during May. Overall, EM economic conditions remain fragile, with most economic strength having been front-loaded in Q1 2023.

DM and EM growth projections

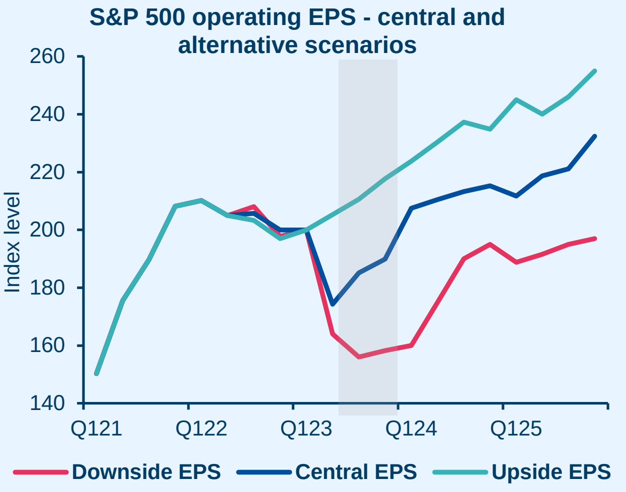


Source: Amundi Institute. Data and forecasts are as of 13 June 2023.

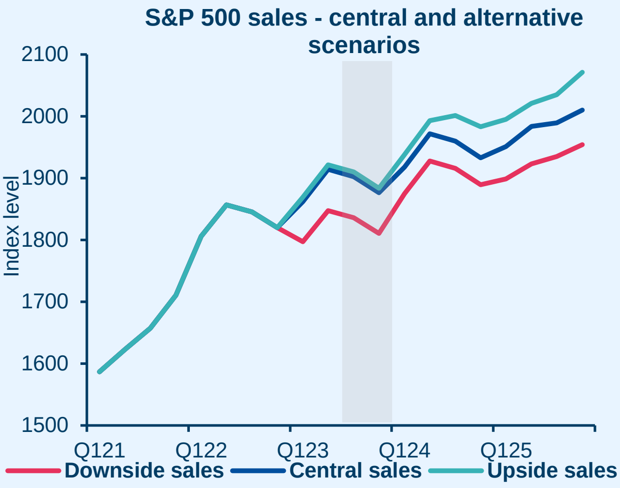
Sequential GDP growth



Source: Amundi Institute, Datastream, Bloomberg. Data is as of 13 June 2023. Forecasts are by Amundi Institute and are as of 13 June 2023. Data is average QoQ growth, not annualised.



Source: Amundi Institute, Bloomberg for the history. Data is as of 31 May 2023. All forecasts are from Amundi Institute.



Source: Amundi Institute, Bloomberg for the history. Data is as of 31 May 2023. Downside and central forecasts are from Amundi Institute, Upside is the official consensus from S&P Capital IQ.

Defensive allocation is preferred during a correction phase

The expected economic backdrop should facilitate a continuation of the current **Correction phase** – according to **Amundi Institute's Advanced Investment Phazer** (see the next page) – in financial markets until year-end, with even stronger conviction given to deteriorating US economic conditions and a profit recession that has not yet hit its trough. Markets have stayed buoyant on Q1 earnings. Amid strong demand, companies were successful in passing through higher costs to consumers, but **these benign conditions should fade for Q2-Q3 earnings**, reflecting a worsening outlook for consumers. We expect a deterioration in US sales and EPS, as we see a mild recession materialising. The next two quarters of the reporting season could lead to a market correction from current levels that could create entry points for equity markets. When it comes to inflation regimes, according to **Amundi Institute's Inflation Phazer**, H1 2023 saw a shift from the **Hyperinflation regime** (featuring a YoY price change in the US >10%) that prevailed in 2022 to a more benign **Inflationary** one (featuring a YoY price change at 3-6%). For **H2 2023**, the combination of monetary policy tightening, lower commodity prices, and weakening demand should favour **further price moderation**, particularly in reference to headline inflation. However, the return to a **Normal inflation regime** – featuring YoY inflation changes at 2-3% – **remains uncertain**, as core inflation remains sticky and is expected to remain above central bank targets.

The resulting **asset allocation** suggests a **defensive approach, with gold and duration among the favoured asset classes**, while we keep a cautious stance on risky assets. Looking to 2024, a gradual recovery in H1 is more likely. However, it is too soon to call for a generalised risk-on move, given limited visibility on the extent of the cumulated impact of the financial tightening induced by the Fed rate hikes. A **scenario of moderating inflationary pressures should make current valuations more sustainable**. Upside risks could come from a less-painful-than-expected macroeconomic scenario, with a positive impact on corporate revenues, which are the main driver of any profit recession. Margins should benefit from a producer-price and labour-cost normalisation, alongside a weaker dollar. Downside risks relate to a credit event and its spill-over to corporates and the whole economy.

Francesco SANDRINI
Head of Multi-Asset Strategies

"Low growth and high inflation suggest a cautious asset allocation. Gold and government bonds are favoured over risky assets in H2. Moving into 2024, an improving outlook for earnings could open up opportunities to add risk assets."

John O'TOOLE
Head of Multi-Asset Investment Solutions

Dynamic asset allocation calls for a cautious start before adding equity

Lorenzo PORTELLI
Head of Cross Asset Strategy, Amundi Institute

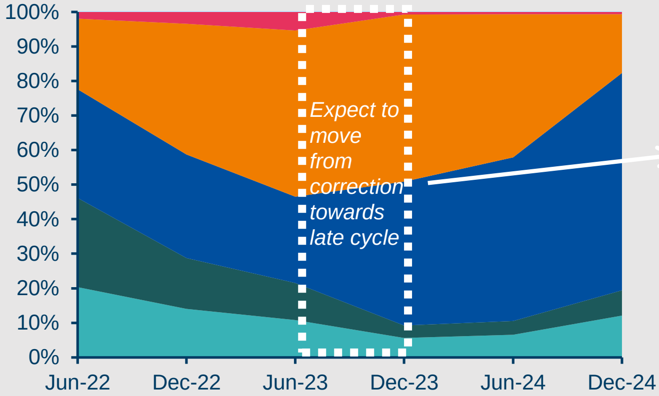
Amundi Institute's Dynamic Asset Allocation (DAA) seeks to determine the medium-term (6 months to 3 years) optimal allocation, which is determined by assessing:

- **Economic backdrop:** what asset classes can deliver historically according to the expected financial and inflation regime*.
- **Top-down valuation**: what markets are pricing in and not pricing in. This is key to fine-tuning the allocation denoted by the economic backdrop.

According to Amundi Institute's models for assessing the economic backdrop (Advanced Investment Phazer and Inflation Phazer), in H2 2023 we will gradually move from a likely *correction* phase (featured by a profit recession and tighter financial conditions) towards a *late cycle* scenario (featured by a stabilisation in EPS, GDP growth improving, but financial conditions still tightening), while inflationary pressures are likely to persist, albeit at a more moderate pace than in H1 2023. The certainty of uncertainty driven by close probabilities of more vs less constructive market phases, calls for a cautious allocation stance to start with, especially for equity markets where overall valuations are not supportive either. Once markets have corrected part of this overvaluation, or should the economic backdrop move into a late cycle more quickly, this will open opportunities to rebuild the exposure towards risky assets.

Economic backdrop assessment

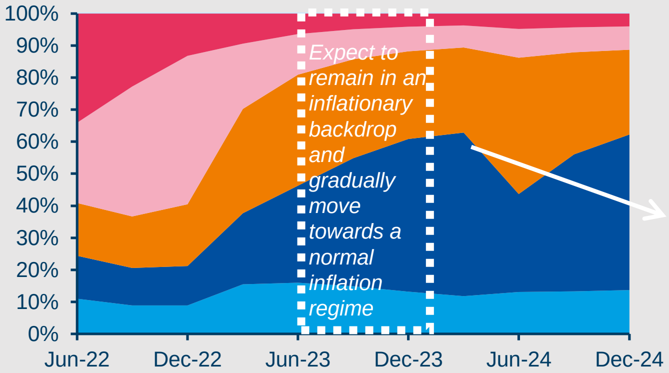
Advanced Investment Phazer (probability of financial regimes): The model defines five phases based on macro-financial variables and the associated probabilities of their occurrence. For each phase, the model defines the favoured asset classes and their optimal allocation.



Phases, markets, and allocation implications

Contraction	▪ Risky assets unattractive. ▪ **Favour:** Govies, gold, cash.
Correction	▪ Global equities down and volatility up. ▪ **Favour:** Govies, Gold, Credit IG.
Late cycle	▪ Focus on high-quality risky assets. ▪ **Favour:** DM equity, quality credit.
Recovery	▪ Risky assets are most attractive. ▪ **Favour:** GEM assets, cyclical DM.
Asset reflation	▪ Low volatility, asset classes up (ex cash). ▪ **Favour:** Global equities and credit.

Inflation Phazer (probability of inflation regimes): The model defines five phases based on key inflation metrics and determines the probabilities of the occurrence of each phase. A high probability of inflationary phases will call for an asset allocation tilt towards those asset classes and sectors more resilient to inflation.



Inflation regimes, CPI YoY, core PCE YoY ranges

Hyperinflationary recession	CPI >10% - Core PCE >8%
Hyperinflationary recovery	6%< CPI <10% - 6% < Core PCE < 8%
Inflationary	3%< CPI <6% - 3% < Core PCE < 6%
Normal	2%< CPI <3% - 2% < Core PCE < 3%
Deflationary	CPI <2% - Core PCE < 2%

Source: Amundi Institute, Bloomberg. Data is as of 1 June 2023. **For Illustrative purposes only**.* Discover more on Advanced Investment Phazer: a guide to dynamic asset allocation

Central and alternative scenarios

	DOWNSIDE SCENARIO Financial crisis triggers global recession 20%	CENTRAL SCENARIO Persistent stagflationary pressure 70%	UPSIDE SCENARIO Economic resilience 10%
Geopolitics 	▪ Worsening Ukraine war impairs commodity trade. ▪ More protectionism and increased retaliation to protectionist measures.	▪ Ukraine war. Risk of escalation in the short run. De-escalation is likely in late 2023 / early 2024. ▪ China-US tensions. ▪ More protectionism (IRA and its 'siblings'). ▪ OPEC+ imposing a floor on oil prices.	▪ De-escalation / ceasefire in Ukraine. ▪ Lower energy or food prices.
Inflation and policy mix 	▪ Sticky core inflation leads to tighter financial conditions. ▪ CB hike more than expected. ▪ Financial stress. ▪ **Two sub-scenarios** with different paths for key rates: **modest recession:** inflation risks may still prevail; and **strong recession**: large rate cuts as soon as H2 2023.	▪ Inflation: gradual slowdown. Sticky core inflation should get closer to target by end-2024. ▪ DM CB close to the peak, no rate cuts in 2023. ▪ Fed funds rate back to 3% by end-2024 (-225bp). ECB: no rate cut before end Q1 2024. ▪ Monetary policy is more mixed across EM: many EM have hit peak rates. ▪ EU fiscal policies to tighten. US fiscal impulse to stay negative due to spending caps over the next two years as a result of the debt ceiling deal. EM fiscal space constrained amid prudent stance.	▪ CB status quo, key rates higher for longer.
Growth path 	▪ More widely spread recessionary outlook (global growth below 2%).	▪ Subdued global GDP growth (below 3%), with divergences: anaemic growth in Europe, mild US recession, reopening rebound in China. ▪ Tightening credit conditions will impact DM economic activity in H2 2023. ▪ Sub-par growth expected in 2024 in most DM. ▪ Growth gap still favours EM in 2024, but with no further widening.	▪ In case of pronounced cyclical disinflation, we could see a faster-than-expected return to potential growth in 2024. ▪ IMF- or ECB-type scenario.
Climate change 	▪ Climate transition measures postponed, with more climate events hitting supply chains.	▪ Climate transition measures postponed with more climate events impacting supply chain and food security. Disorderly policy response.	▪ Climate change policy and energy transition are top priorities and coordinated across regions.

Risks to central scenario

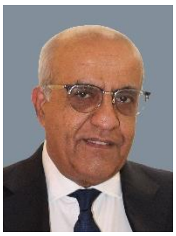
HIGH — PROBABILITY — LOW

	25%	20%	20%	20%	10%
	Geopolitical risk and war escalation	**Global economic slowdown and deep profit recession**	**Persistent stagflationary pressure (US / Europe)**	**Macro financial risks triggered by tighter credit and liquidity conditions**	**US government shutdown****
Market impact +	**Positive** for DM govies, cash, gold, USD, volatility, defensive assets and oil.	**Positive** for cash, JPY, gold, quality vs. growth, and defensives vs. cyclicals.	**Positive** for TIPS, gold, commodity FX and real assets.	**Positive** for US Treasuries, cash and gold.	**Positive** for EUR, JPY, CHF and Bund.
Market impact −	**Negative** for credit, equities and EM.	**Negative** for risky assets and commodity exporters.	**Negative** for bonds, equities, DM FX and EM assets.	**Negative** for credit.	**Negative** for US Treasuries, US equities, and risky assets.

Source: Amundi Institute as of 16 June 2023. DM: developed markets. EM: emerging markets. CB: central banks. USD: US dollar. EUR: Euro. CHF: Swiss franc. JPY: Japanese yen. TIPS: Treasury inflation-protected securities. FX: foreign exchange markets. **Despite the debt ceiling agreement, Congress still has to adopt a budget for FY2024, which starts on 1st October. Budget negotiations should be tense and the possibility of a shutdown at a later date cannot be ruled out. Otherwise, fiscal policy can become more restrictive than expected.

GLOBAL THEMES

Central banks remain credible regarding inflation



Mahmood PRADHAN
Head of Global Macroeconomics - Amundi Institute

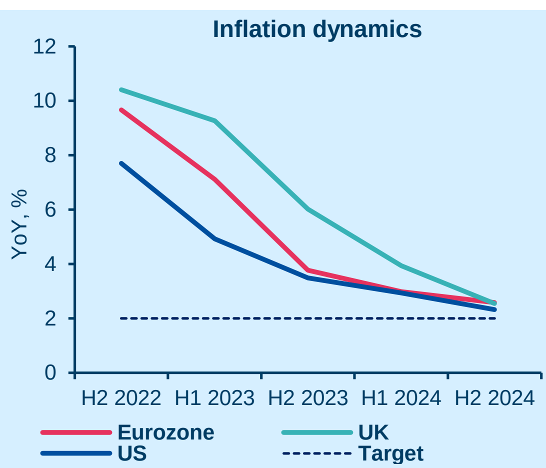
Annalisa USARDI, CFA
Senior Economist – Amundi Institute

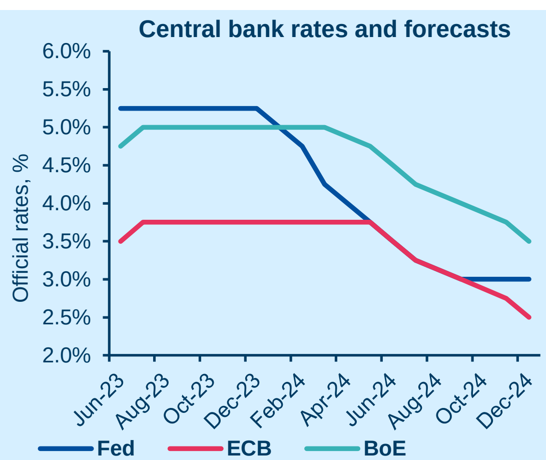
Central banks face a dilemma. Substantial monetary tightening has reduced headline inflation, but core measures are proving sticky, both in Europe and the United States. Even though inflation is still well above central bank targets, markets expect policy rates to be near their peaks. As central banks retain credibility, **most measures of inflation expectations remain anchored**.

The risks of inflation reaccelerating appear limited, especially as we expect central banks to maintain a restrictive monetary stance for an extended period. Past experience with advanced economies indicates that **wage-price spirals do not materialise when monetary policy remains focused on meeting the inflation target**. We also expect wage growth to moderate as growth slows and labour market pressures gradually ease, as currently underway in the United States. In the Eurozone – where wage growth picked up later than in the United States and with significant dispersion across countries – it may take longer for wages to moderate, but here, too, the weakening economic environment should contain any significant rise in real wages. Our reading of market-based expectations is consistent with this.

Consumer and business expectations have been more volatile, with consumer inflation expectations ticking up recently. After aggressively repricing their short-term expectations higher last year, business expectations have retraced progressively lower, although remain above their pre-Covid average levels.

Evidence from past episodes of high inflation in the United States suggests **it takes about two years to bring core inflation down by half from its peak level**. Our forecasts for the current episode are consistent with this. In Europe, favourable energy base effects and lower food prices will reduce headline inflation faster than core inflation. The impending economic slowdown will reduce the pricing power of corporates and, together with the normalisation of supply chains, help both core and headline measures to converge by the end of 2024.





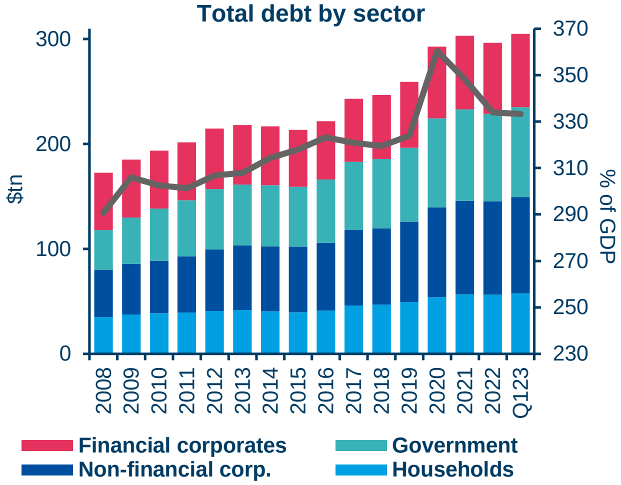
Source: Amundi Institute, Bloomberg. Data is as of 16 June 2023. Forecasts are by Amundi Institute and are as of 15 June 2023.

Macro fragilities

A world flooded by debt

Global debt hit a record of $300tn in Q1 2023, or 333% of GDP. High debt could limit fiscal support in the case of a strong economic downturn, making the economic outlook more fragile.

Total debt by sector

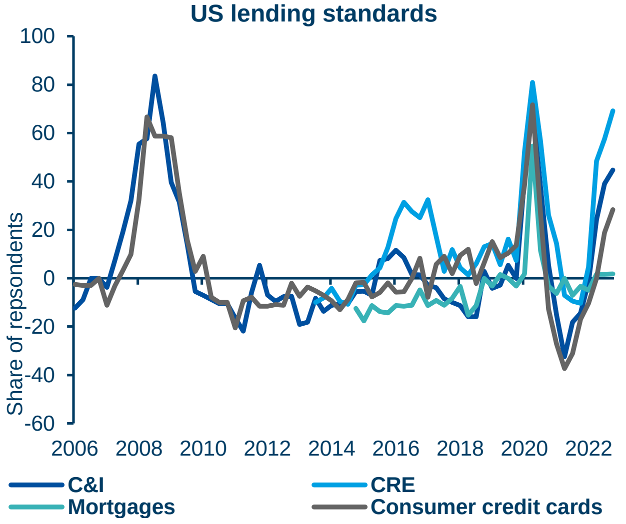


Source: Amundi Institute on IIF data as of end Q1 2023. Note: total debt is the sum of government debt, household debt, financial sector debt and non-financial corporate debt.

Tighter lending standards

Lending conditions are tight, as borrowing costs for corporates and households have risen a lot, increasing the risk of an economic downturn.

US lending standards



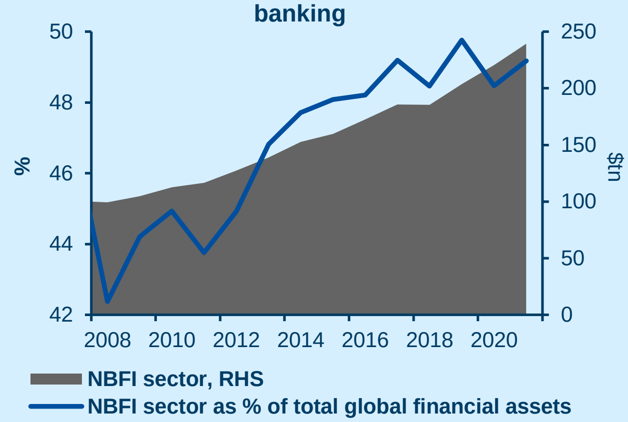
Source: Amundi Institute, Bloomberg. Data is as of 29 May 2023. C&I: Commercial and industrial loans; CRE: Commercial real estate. Indices are based on surveys, and % refers to net domestic respondents of tightening standards. It is calculated by taking the difference between share of respondents giving favourable and unfavourable responses.

Market vulnerabilities

The rise of shadow banking

A significant risk to watch out for is the rise of shadow banking, which could threaten the financial system's stability as the former is less regulated and can represent a hidden risk.

Total global financial assets - shadow banking

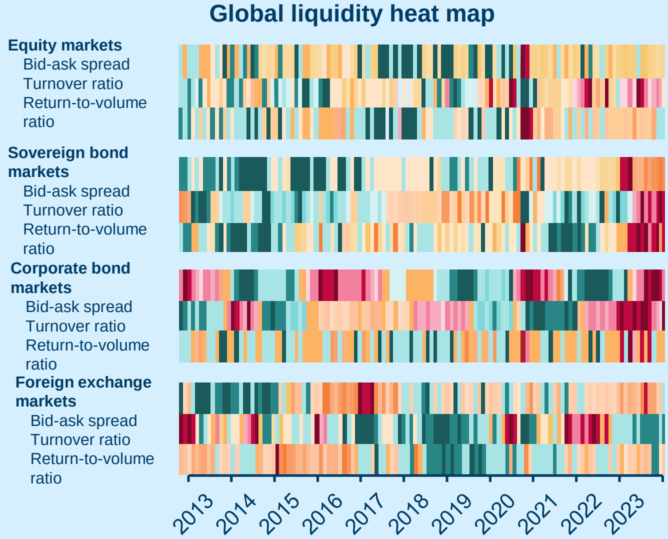


Source: Amundi Institute on Jurisdictions' 2022 submissions (national sector balance sheet and other data) and 2021 submission for Russia; FSB calculations. Data is as of 29 May 2023.NBFI: non-bank financial institutions.

Deteriorating liquidity in some market segments

Given the rapid pace of monetary tightening, some key financial markets are suffering a clear deterioration of liquidity conditions.

Global liquidity heat map



Source: Amundi Institute on IMF sources which are Bloomberg Finance L.P., JPMorgan Big Data, and AI Strategies, JPMorgan Chase & Co., Market Axess, Refinitiv Datastream, and IMF staff calculations. Red (green) cells represent the lowest (highest) liquidity levels. Data is as of 31 May 2023.

Asia to attract foreign flows

Alessia BERARDI
Head of Emerging Macro and Strategy Research - Amundi Institute

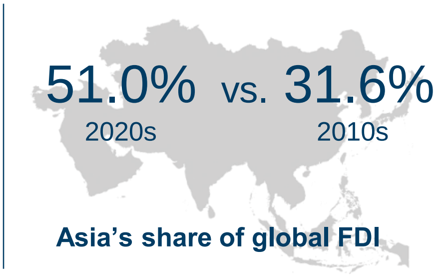
"In the long term, we expect a structural, steady, and controlled downward evolution of the China-US relationship, rising regional integration, and China and India moving towards more sustainable growth models to make Asia an attractive region for foreign investors."

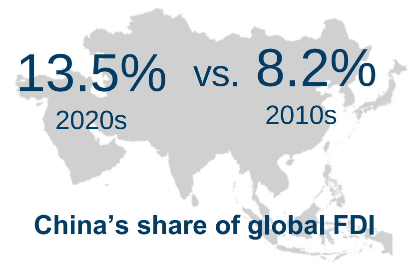
Despite intensifying geopolitical tensions, Foreign Direct Investments (FDI) in China and Asia have been rising steadily in recent years, continuing a trend that started over two decades ago. **As of 2021, Asia hit 43.6% of global FDI, with China alone accounting for 11.4% of global FDI**. **The region is attractive to foreign investors** due to its market size, labour costs and business environment, supported by effective government policies such as tax incentives, streamlined business regulations and infrastructure development. While the trend is based broadly across the region, with India, Indonesia, Vietnam and Malaysia attracting significant amounts of FDI, China remains the largest recipient of FDI in Asia.

In the long term, the rising role of digital technologies and the increasing integration of regional economies through initiatives such as the Belt and Road scheme – which is increasingly focused on China's neighbours, both South and West – and the Regional Comprehensive Economic Partnership (RCEP) should support the FDI trend. However, the region remains mixed in terms of economic development, regulatory frameworks and infrastructure, making the journey towards deeper economic integration challenging.

In the short term, early Q2 signals out of China, stemming from uncertain consumer confidence and the housing market, have raised concerns about its growth trajectory ahead. Our growth outlook (GDP growth is forecast at 5.7% in 2023) includes some modest recovery and is subject to the evolution of home sales in smaller cities, construction demand, youth unemployment and consumption. At this point, the authorities are unlikely to respond with a sizeable fiscal stimulus. However, the PBoC has definitely shifted to a more accommodative stance vis à vis its policy rates. The economy should remain on a moderate growth trend and – only in a worst-case scenario – 2023 real GDP could print at the 5.0% growth target. Yet, we should look at this short-term pattern as part of needed structural changes to engineer a more sustainable growth model.

India's growth should also moderate in the short term, at around potential for FY2024 (5.5% YoY), after extremely robust post-pandemic growth rates while, longer term, the country's growth model should become more sustainable thanks to renewed investment focused on newer sectors, such as semiconductors, electric vehicles and renewable energy.





Source: Amundi Institute on Unctad FDI World data. Annual data is as of end-2021. 2020s is the 2020 and 2021 data average. 2010s is the average of annual data from 2010 to 2019.

GLOBAL THEMES

US-China relations and Russia-Ukraine war to dominate H2

Anna Rosenberg
Head of Geopolitics - Amundi Institute

"China has ended its strategy of 'hide your strength and bide your time' to emerge as a more assertive geopolitical player."

In H2, the geopolitical outlook should be dominated by US-China tensions and the Russia-Ukraine war. The current geopolitical realignment will evolve with third countries emerging as more important players. Looming risks include the threat of a surprise Israeli attack on Iranian nuclear infrastructure and the upcoming Taiwan election in January. On the **Russia-Ukraine war**, focus will turn to Ukraine's counter-offensive, which will play out over the summer and into early autumn. Depending on battlefield developments and ongoing talks, **a window for negotiations** could open in the autumn. On **US-China tensions**, something has changed meaningfully. China has ended its strategy of 'hide your strength and bide your time' to enter the world stage as a more assertive player. This shift, coupled with US political dynamics, means that **US-China relations should remain on a downward trajectory for the next several years**. The steady and controlled decline does not exclude temporary improvements in the relationship. Indeed, the remainder of 2023 is likely to be relatively calm as there will be various high-level meetings between the two sides. While the United States will step up pressure on G7 countries to align with its policy towards China, many parts of the 'Global South' should remain non-aligned, leveraging their position to extract benefits from the US, EU, China and Russia simultaneously. **On the upside**, H2 2023 is likely to see further **improvement in EU-UK** relations, as well as progress in economic diversification with a Mercosur trade deal between the EU and parts of Latin America making inroads. Other events to watch are Spain's election in July and the EU Parliament election in May 2024, which should drive the reform agenda moving forward.

GLOBAL THEMES

Fiscal policy will weigh on GDP growth in the EU

Didier BOROWSKI
Head of Macro Policy Research - Amundi Institute

"EU countries face a new dilemma: how to increase green investments while respecting the new rules."

The EU Commission presented its legislative proposals. The goal of the new fiscal governance is to strengthen public debt sustainability and promote sustainable and inclusive growth through reforms and investments. The reference values of 3% of GDP (deficit) and 60% of GDP (debt) are unchanged, but **the new governance** takes into account the fact that Member States (MS) **face different fiscal challenges** (no one size does not fit all). Moreover, the rules are simplified: the only operational indicator for the budgetary adjustment path will be the volume of expenditure over several years.

The Commission made important concessions to Germany: a minimum fiscal adjustment of 0.5% of GDP per year will have to be implemented as long as the deficit exceeds 3% of GDP and green investments will not be treated separately.

In the short term, the withdrawal of the support measures introduced in 2022 will weigh on growth. Going forward, it is difficult to gauge the impact of this new discipline on fiscal tightening. The dilemma is: either MS will prioritise investment – and current spending will be cut – or taxes will be raised, which would be unpopular. Or they will sacrifice green investments to fiscal discipline, which would be counterproductive.

Time is running out with the European elections taking place in May 2024. These key technical points are still under discussion. An agreement by the EU Council is possible before the end of the year, but it is still far from being a done deal.

INVESTMENT CONVICTIONS

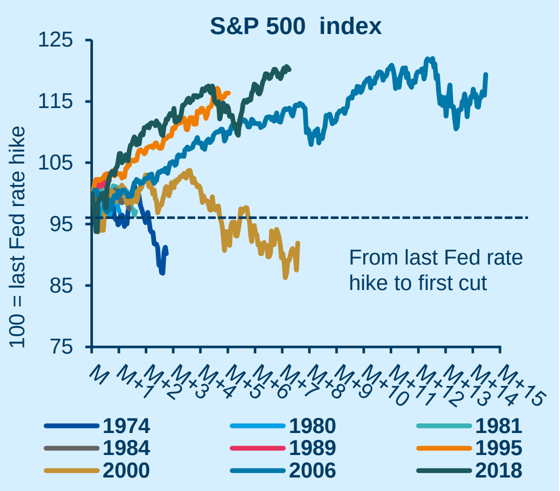
Amundi asset class views

	Asset class	Stance as of June 2023	Direction of views for H2 2023	
EQUITY PLATFORM	United States	-	=	Bottom out
	US value	+	+	Stable
	US growth	--	-	Bottom out
	Europe	-/=	=	Bottom out
	Japan	=	=	Stable
	China	+	+	Stable
	Emerging markets ex-China	=	=/+	Improving
FIXED INCOME PLATFORM	US govies	=/+	=/+	Stable
	US IG corporate	=/+	=/+	Stable
	US HY corporate	-	--	Deteriorating
	European govies (core)	-/=	=	Improving
	European govies (peripherals)	-/=	=	Improving
	Euro IG corporate	=/+	=/+	Improving
	Euro HY corporate	-	--	Deteriorating
	China govies	=	=	Stable
	EM bonds HC	=/+	=/+	Stable
	EM bonds LC	+	+	Stable
OTHER	Commodities	=/+	=	Deteriorating
	Currencies (USD vs. G10)	-	-	Stable

-- - = + ++
Negative Neutral Positive

Source: Amundi as of 12 June 2023. Direction of views for H2 2023 refers to the possible evolution of stance on each asset class during the period. 'Bottom out' means that we see a deterioration first, followed by a recovery.

DM equity: focus on quality, entry points in the case of correction



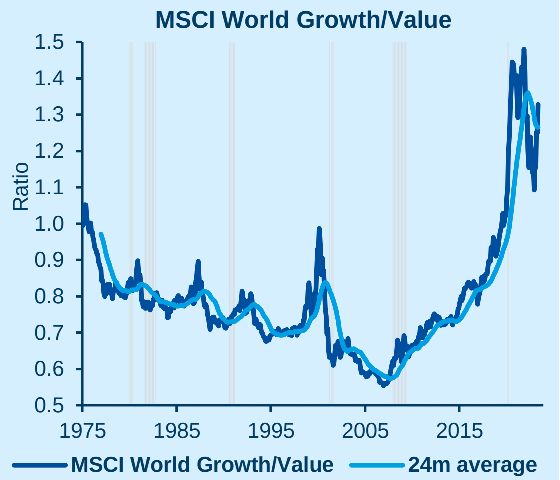
Source: Amundi Institute, Bloomberg. Data is as of 31 May 2023.

US recession to outweigh the benefit of a Fed pause

Caution in equities is still required while Fed rates plateau. Market performance between when the Fed stops raising rates and the first cut could be positive or negative, depending on economic conditions.

This was positive when there was no recession (1984,1995 and 2018) or when a bubble was building (2006). In our scenario, we see a risk of recession in H2, triggered by a weak earnings seasons in Q2-Q3. As such, we remain on the cautious side for H2.

We consider the current risk-reward for entering a US recession as unattractive for equities. **However, when inflation drops from high levels, equities tend to react positively earlier when the Fed relaxes monetary policy,** as was the case in 1953, 1974 and 1980. As of today, we expect this phase to only happen next year.



Source: Amundi Institute, Refinitiv. Data is as of 26 May 2023.

Quality first, across the board

In March 2003, the correction of the Growth vs. Value overvaluation found another impulse in favour of Value as the market bottomed out.

Repetition is a strong possibility. In the meantime, we favour quality (low leverage, earnings recurrence and protected dividends). However, **at a regional level, the United States -- usually a quality play -- is too expensive and deserves to be underweight entering H2 2023**. Europe needs a breather and will not be immune to a US recession but looks a bit better due to its exposure to China's recovery and is really cheap. **Japan is an interesting diversifier** due to its unhedged currency (domestic recovery, China exposure and improving corporate governance).

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CIO of US Investment Management

DM fixed income: stay with quality credit and core govies

Treasury yield curve

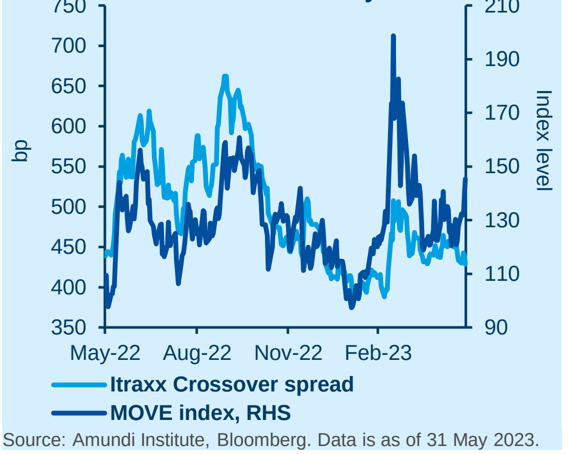
Source: Amundi Institute, Bloomberg. Data is as of 5 June 2023.

Core govies: good value and diversification qualities

DM fixed income investors remain focused on sticky inflation and the need for CB to do more. **We expect the Fed to push the US economy into recession** to bring inflation closer to 2%. **The ECB remains focused on inflation** despite disappointing economic data and Germany's slide into recession. In the Eurozone, growth should remain subdued and inflation sticky.

On fixed income markets, **in the United States** this translates into a slightly positive stance on duration. We see curve steepening opportunities (5-30y). In the **Eurozone**, investors should stay slightly underweight on duration and move gradually towards neutrality. Inflation protection strategies remain in focus for H2 2023. Overall, **core government bonds** retain good value and investors can consider **bonds as risk diversifiers** in the current market environment. At this stage, most of the expected tightening is already reflected in current yields, especially for US rates.

HY valuations do not incorporate rise in rates volatility



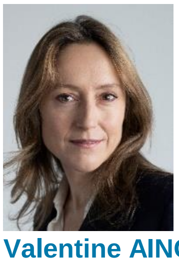
Source: Amundi Institute, Bloomberg. Data is as of 31 May 2023.

Investment Grade favoured in an economic slowdown

The upcoming economic slowdown is not priced by credit markets. **We maintain a quality focus, with a preference for Investment Grade credit over High Yield.**

The impact of monetary tightening on corporate fundamentals has been limited so far, because of the huge liquidity accumulated during the Covid-19 crisis and low short-term refinancing needs.

The transition towards higher funding costs will be more painful and faster for low HY-rated corporates, which have less ability to generate cash flow and higher short-term refinancing needs. Current valuations do not reflect this risk**.** As such, we favour quality credit, **for which fundamentals remain good and valuations fair or even very cheap for European investment grade.**



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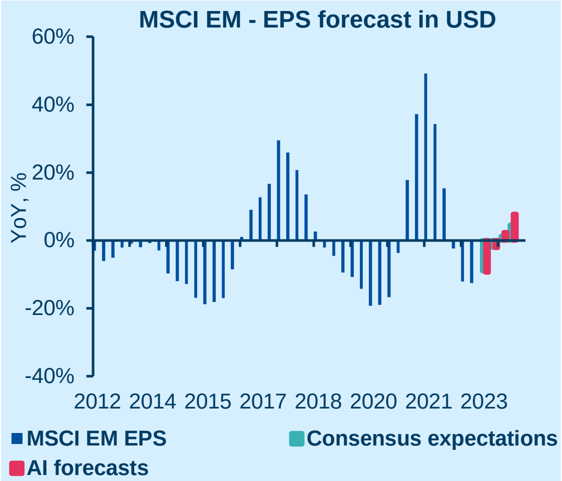
EM assets favoured due to tamer inflation and earnings recovery

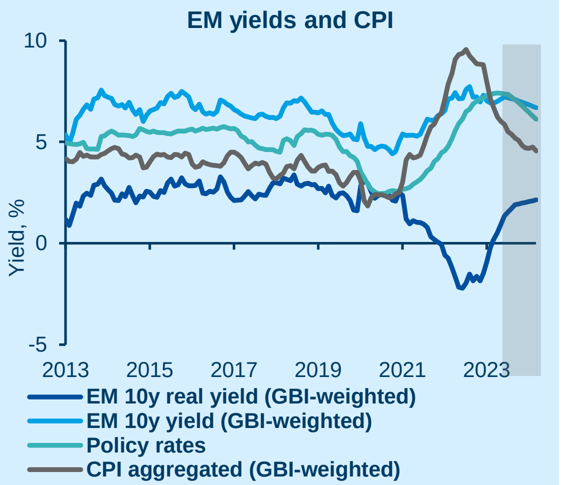


Source: Amundi Institute, Factset. Data is as of 26 May 2023. Forecasts are by Amundi Institute.

EM equity: earnings growth is back in EMEA and Asia

After a challenging first half of the year for EM equity, harmed by negative sentiment towards China, **we expect a better environment in H2 2023**. EM equity could benefit from: 1) **attractive valuations,** particularly in LatAm and EMEA; 2) the approach of an **end to the Fed tightening** cycle (possibly transmitted into EM CB easing); 3) the expected **dollar depreciation**.

We expect earnings to return to positive YoY growth after two negative quarters -- especially in EMEA and EM Asia -- as EM economics should prove relatively more resilient in terms of growth trends compared to developed economies. **Margins started to recover in Q1 2023. This trend should continue in H2.** In China, we see the risk-reward ratio as being more favourable for A-shares (onshore) than for H-shares (offshore) markets amid high geopolitical risk. We maintain a positive outlook for Brazil, but we are closely monitoring the progress of fiscal reforms.



Source: Amundi Institute, Bloomberg. Data is as of 26 May 2023. Forecasts are by Amundi Institute.

EM fixed income: attractive yields and spreads

While EM bond yields have dropped in H1 2023, **the asset class still offers an appealing entry point in terms of spread and carry, supported by a weakening dollar**. **We maintain an upbeat outlook, particularly for LatAm**, where the hiking cycle has ended and should reverse in H2 2023 over decelerating inflation. Hard-currency bonds are expected to yield high-single-digit returns on a six-month horizon and volatility remains limited. **We favour HY**, which offers more appealing valuations. **Conditions in the EM corporate bond space are improving**, with corporate net leverage levels well below those in the United States. Additionally, **EM HY corporate defaults have peaked and should moderate in 2023 in LatAm and EMEA.** However, China's real estate sector still poses risks.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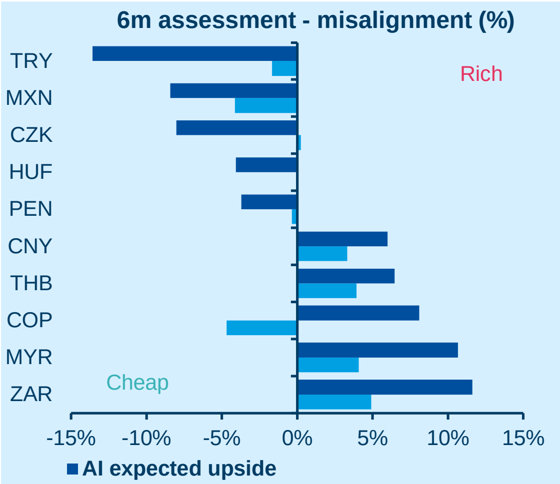
Global Head of Emerging Markets



Source: Amundi Institute's calculation on Bloomberg data. Data is as of 5 June 2023. Chart shows top and bottom five EM currencies based on their expected upside according to AI's expected upside.

EM currencies: recovery is on track

As the US economy loses its exceptionalism in economic growth and interest rates, investors should look elsewhere for higher returns, leading to a **shift away from the dollar**. With the Fed tightening cycle ending, EM CB should turn towards an easing cycle, thanks to peaking inflation rates which should be on a declining trend in H2 2023. While undervaluation and light positioning on EM currencies could contribute to an asset class recovery, **we recommend a selective approach**. We are focusing on commodity-exporter currencies, thanks to a resilient commodity cycle – driven more by supply than demand – as well as high-carry currencies such as those in LatAm. Meanwhile, EMEA currencies may be harmed by their high vulnerability and persistent inflation.

"The approaching end to the US tightening cycle, prospects of a weaker US dollar, stabilising or falling inflation, and an earnings recovery could make EM assets shine in H2. Country-specific assessments should lead to investment opportunities, which we particularly see in Asia and LatAm, both for equities and fixed income."

EM CONVICTIONS

	$ DEBT	LC DEBT	EM EQUITIES	EM FX
Overall stance	= + Slightly positive on HC debt with preference for HY over IG given current spread levels.	+ Positive on LC debt with focus on areas of attractive real yields. We like local-currency EM corporate debt.	+ Positive on EM equities, with focus on areas with attractive valuations. We favour value over growth.	= + Positive on EM FX, with preference for high-carry currencies.
Regional preferences	▪ LatAm (Brazil, Mexico, Argentina); ▪ Indonesia; ▪ South Africa; ▪ EM corporate debt: attractive valuations, especially within the HY space: Brazilian corporates, Mexican energy, and Indonesian, Kazakhstani, and GCC quasi-sovereign.	▪ LatAm: supported by quality of carry, Brazil, Mexico; ▪ Indonesia; ▪ South Africa; ▪ Romania; ▪ India.	▪ LatAm, especially Brazil; ▪ China, preference for onshore vs offshore market amid geopolitical risks; ▪ Hong Kong; ▪ Indonesia; ▪ Vietnam (largest member in the MSCI Frontier Index).	▪ Brazilian real; ▪ Mexican peso; ▪ Indonesian rupee; ▪ Indian rupee; ▪ South African rand.

Source: Amundi Institute as of 6 June 2023. EM: emerging markets. HC: hard currency, LC: local currency.

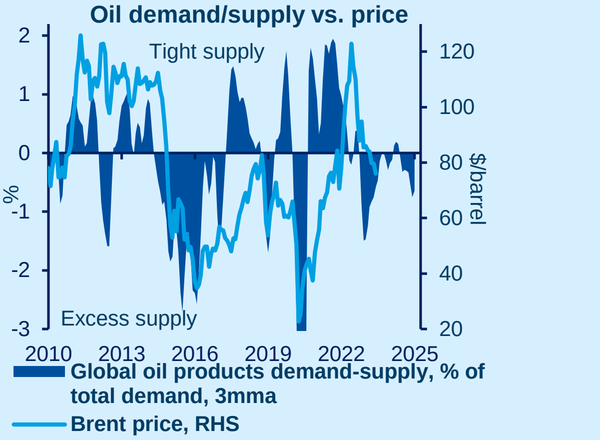
INVESTMENT CONVICTIONS

Oil to firm on evidence of tightness

Jean-Baptiste BERTHON
Senior Cross Asset Strategist - Amundi Institute

Francesco SANDRINI
Head of Multi-Asset Strategies

Oil demand and prices are cyclical, sensitive to the economy and to consumer reactions to high prices. Yet, oil has disconnected from macro forces several times in the past. This has occurred when supply could be adjusted quickly, when macro deterioration was manageable or in times of an oil supply shock. We expect oil demand to stay resilient, supported by China's decoupling and amid a manageable contraction of the global economy. OPEC+ also has the upper hand – without heavy competition from US producers, with declining Western leverage and thanks to DM's chronic under-investment – allowing the cartel to act on supply more decisively. Following a period of range trading, we see prices gaining traction later in H2 upon evidence of market tightness. We then expect Brent to reach $90/barel.

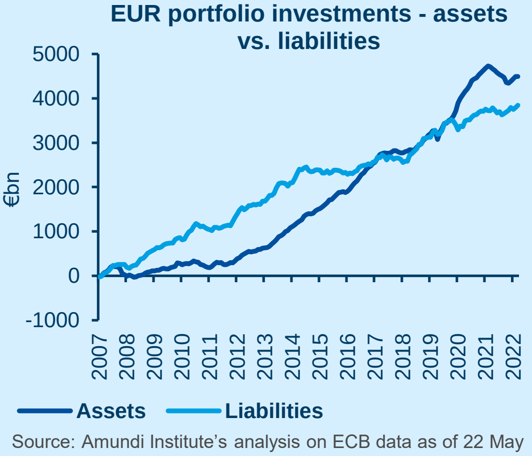


Source: Amundi Institute, Bloomberg, EIA, Macrobond as of 23 May 2023. Estimates are by EIA.

INVESTMENT CONVICTIONS

Another cyclical test for the dollar's hegemony

In the past, the financial industry tended to downplay the USD's dominance in global markets. While reality has invalidated this pattern – USD remains involved in 90% of global transactions – the current cycle has strengthened the argument. USD overvaluation is part of the story, but global capital flows may also be involved this time. **A gradual repricing of the Fed's rate path is the cyclical condition that we expect will reconnect the USD to where it should trade**, based on the regime shift we experienced last year. The amount of out-standing negatively-yielding global debt has plunged, and the interesting asymmetry arising from global portfolio activity – the potential for EUR-based investors to repatriate vast amounts of money into domestic bond markets – suggests a **weaker USD profile moving into year-end.**



Source: Amundi Institute's analysis on ECB data as of 22 May 2023.

Federico CESARINI
Head of DM FX - Amundi Institute

Lauren CROSNIER
Global Head of FX

Alpha makes up for poor market conditions

We are at a complex, macro inflection point, shifting from rate hikes to a growth slowdown. Opposite forces will fuel above-par volatility, opening market-timing windows. CB are nearing peak rates, but sticky inflation will keep some unpredictability in bonds, providing **relative rather than directional trades for macro managers.** Meanwhile, the impact of tightening will deepen the growth slowdown, yet remain orderly thanks to China's growth acceleration. **Alpha** should see asset differentiation with reasonable correlations, prices trading closer to fundamentals and country arbitrages. **Worsening funding access and costs will reveal hidden leverage**. Without a hard landing, dislocations should be limited, providing extra alpha for bottom-up pickers. With markets staying versatile for longer, managers will remain focused on alpha, mitigating milder beta contributions. **Managers' positions remain cautious, but gross exposures suggest no shortage of ideas**. Macro inflections are uncomfortable for **top-down styles**, but the medium-term outlook is promising. Alpha is already supporting bottom-up strategies, waiting for more catalysts and better valuations to deploy fully.

Hedge fund strategies H2 2023 outlook

		-	N	+
L/S equity	Directional		■	
	Market neutral		■	
Event-driven	Merger arbitrage	■		
	Special situations		■	
FI arbitrage	L/S credit		■	
	FI EM arbitrage		■	
	FI macro arbitrage			■
Global macro	Global macro			■
CTAs	CTAs		■	

Source: Amundi Institute as of May 2023.

INVESTMENT CONVICTIONS

Private markets: look for resilient assets

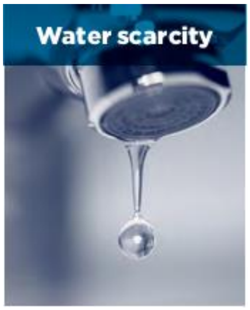
Listed and private markets have not yet repriced for a worsening outlook. Looking ahead, while some areas could be affected by these weaker dynamics, we expect private markets to remain resilient with some differentiation among assets. We particularly **favour infrastructure** thanks to its cash-flow features, stable pricing, and strong growth outlook, which is being boosted by the energy transition. Along with public funding, private capital is required to build renewable energy plants as well as enhance the digitalisation of networks. **We also remain positive on private debt,** as these assets are diversifiers that benefit from strong bargaining power in negotiating lending contracts, as bank financing remains constrained. In the **private equity** space, many non-cyclical businesses (e.g., healthcare) possess pricing power and are profiting from strong structural growth trends. Conversely, cyclical businesses (less represented in this space) may be challenged. Turning to **real estate**, interest rate rises have been difficult for investors, but can create opportunities; inflation should favour rent indexation for ongoing leases. Over a medium-term horizon, current valuations offer an attractive entry point for investors, although a selective approach remains vital.

Private markets outlook for H2 2023

	Infrastruc.	Private equity	Private debt	Real estate
H2 outlook	++	-/=	+	-
Entry opportunities over the next five years	=	+	+	=
Inflation protection	++	=	++	+
Diversification benefit	+++	+	+	++

Source: Amundi Real Assets qualitative assessment as of 10 June 2023. Infrastruc. = Infrastructure. **For illustrative purposes only, on a scale ranging from --- to +++.**

Main themes in Net Zero investing

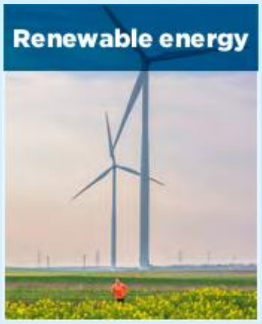


We believe **water scarcity** risk is high and needs to be addressed with technological innovation. By recycling water, manufacturers reduce their dependency on freshwater resources, eliminate the need for extraction and, consequently, conserve natural resources. Treating wastewater can cut its emissions by 33%. We favour both water utilities -- which are a mix of water supply and wastewater treatment operations -- and water quality companies, which provide water treatment equipment and services.

33%

Treating wastewater can cut emissions by 33%.

Source: International Water Association, May 2020.



x3

To reach Net Zero emissions by 2050, global annual clean energy investment will need to more than triple by 2030.

Source: IEA, "Net Zero by 2050", October 2021.

According to the International Energy Agency, **renewable energy** should account for 60% of the world's total electricity production by 2030 and 90% by 2050. Investors can gain exposure to this theme by investing in renewable energy operators/utilities and suppliers of renewable energy equipment for wind, solar, or hydro markets.

Another area of concern are the GHG emissions linked to the **production of uneaten food**. A notable amount is lost in supply chains due to a lack of refrigeration or spoilage during transport. In our view, there are strong tailwinds for innovative companies that can reduce food waste emissions. Investors can play this theme across the value chain, a good example being companies which produce fuel-efficient refrigeration units.

6%

Food waste accounts for 6% of global GHG emissions.

Source: Our World In Data, March 2020.

39%

Buildings contribute 39% of gross annual carbon emissions globally.

Source: UN Environment Program, September 2022.

Real estate impacts energy efficiency, air quality, water and waste management, as well as biodiversity preservation. In this space, investors can look for companies that play a key role in facilitating the transition, such as building insulation businesses. These can play a major role in liaising with their suppliers to reduce carbon emissions across their value chains.

Green bonds issued by governments or supranational entities channel money into green projects, particularly in EM. These projects are focused on areas such as energy efficiency, clean energy and climate change adaptation. Being less volatile than conventional bonds, they are considered an attractive investment vehicle. **Sustainability-linked bonds (SLB)** incentivise issuers' achievement of predefined sustainability / ESG goals through KPIs and sustainability performance targets within a predefined timeline. These tools are another way to finance the energy transition.

>60%

Over 60% of SLB KPIs are linked to GHG emissions.

Source: CMS study of the KPIs used in SLBs, May 2023.

AMUNDI Institute

In an increasingly complex and changing world, investors have expressed a critical need to better understand their environment and the evolution of investment practices in order to define their asset allocation and help construct their portfolios. Situated at the heart of the global investment process, the Amundi Institute's objective is to provide thought leadership, strengthen the advice, training and daily dialogue on these subjects across all assets for all its clients – distributors, institutions and corporates. The Amundi Institute brings together Amundi's research, market strategy, investment insights and asset allocation advisory activities. Its aim is to project the views and investment recommendations of Amundi.

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