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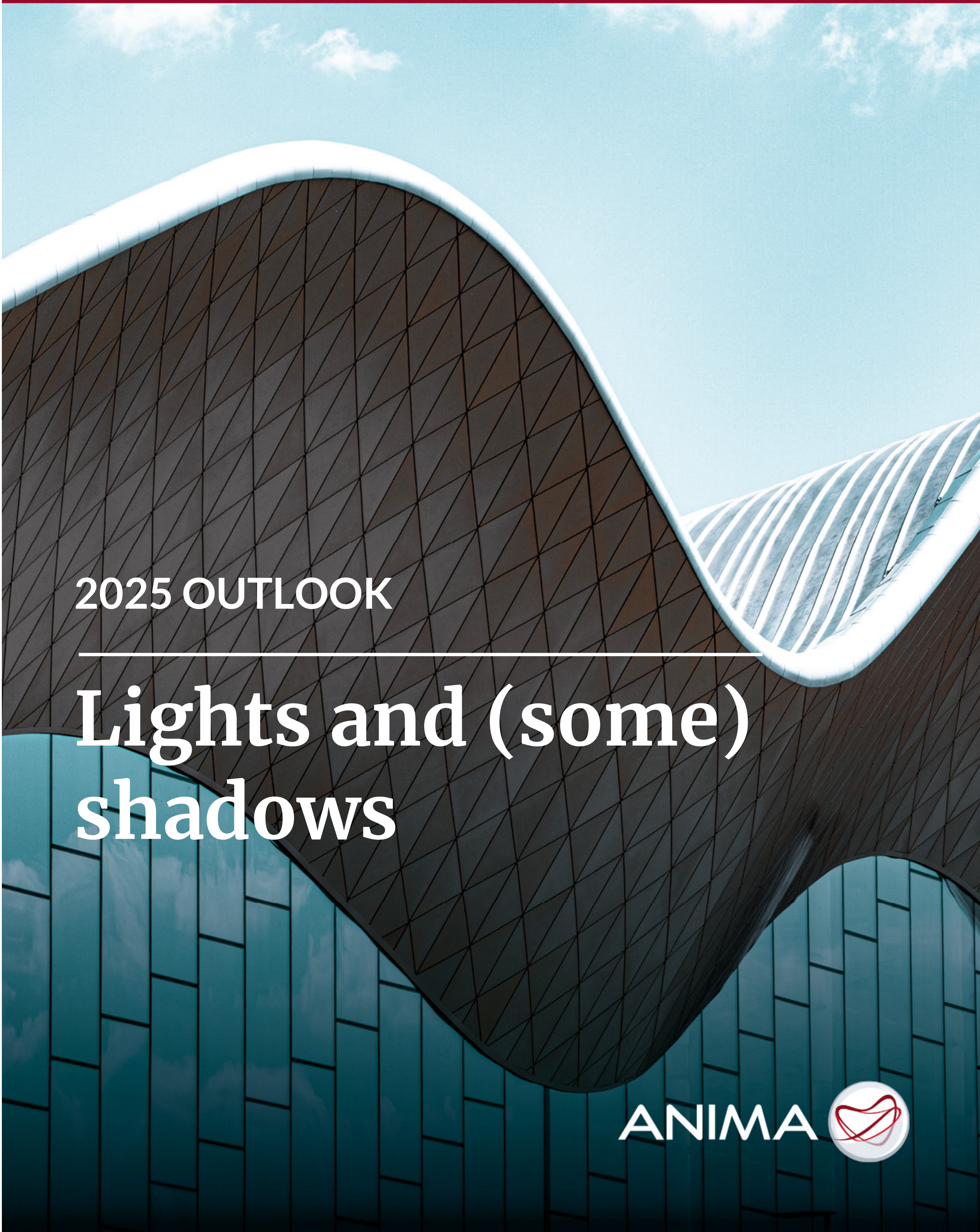

2025 OUTLOOK

Lights and (some) shadows

ANIMA

Lights and (some) shadows

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Overview

Macroeconomic data published during 2024 have further reinforced our sustained optimism about the post-pandemic recovery. The United States remains at the forefront of growth among developed economies, while globally, the labour market is finding its balance: both the unemployment rate and supply-side indicators, such as new job openings and vacancies, have returned to pre-COVID levels. Inflation is steadily decelerating and aligning with the targets of central banks, many of which have begun a gradual normalisation of interest rate.

As per our 2025 forecast, the policies proposed by the newly elected President Trump are unlikely to have a significant impact on the baseline scenario, at least during the first part of the year: the potential onset of a global tariff war would have later repercussions, only becoming a risk towards the end of 2025. We expect global growth to remain steady at a rate similar to 2024, averaging at 2.6%, slightly above consensus expectations. Our outlook on US growth is more positive than the consensus (2.3% for 2025 against 1.9%) and more cautious for the Eurozone (1.0% compared to the consensus of 1.2%), while forecasting intermediate levels of growth rates for the other major economies. In China, growth prospects will largely depend on the extent of support provided by the authorities and the trade policy decisions made by the Trump administration.

Therefore, we do not expect the outcome of the US elections to halt the ongoing economic policy normalisation, and we expect most major central banks will continue to significantly ease their tight monetary stance.

The Federal Reserve, in particular, is pursuing a disinflationary rate-cutting cycle, and we anticipate an overall reduction of 125 basis points by the end of 2025. However, although the direction is clear, the pace is still uncertain: continued upward surprises in real growth data could fuel concerns about a slowdown in the disinflation process, and a pause in December cannot be ruled out.

On the other side of the Atlantic, the European Central Bank is expected to cut rates by 25 basis points at each meeting until June 2025, bringing the deposit rate to 2%; however, risks that in the second half of the year rates could fall below the neutral level cannot be ruled out, especially if growth weakens more than expected and/or core inflation declines more quickly.

In China, the People's Bank of China is expected to ease monetary policy alongside increased fiscal stimulus to maximise support for the economy. A 50 basis point reduction in the reserve requirement ratio (RRR) and a 20 basis point cut in the reverse repo rate are expected by year-end, with another 50 basis points of RRR cuts and 40 basis points of benchmark lending rate cuts anticipated in 2025.

INTRODUCTION – ASSET ALLOCATION

BOND MARKETS – After a disappointing performance in 2024, **we take a slightly more positive view on the bond markets for 2025 and anticipate better returns than this year.** In the United States, in particular, yields at historical high will be the main driver of income, while there is little scope for a significant drop in rates**. In the Eurozone, a moderate recovery and growth still below potential could lead to a decline in yields from current levels,** particularly in the first half of the year. **We forecast a positive performance for BTPs, especially in the first half of the year:** a more dovish European Central Bank may offer support, and we do not expect idiosyncratic risks to rise, preventing a significant widening of the spread.

EQUITY MARKETS – **The outlook for global equity markets in 2025 remains positive**, primarily driven by resilient economic growth. The strength of the economy in the US, backed by strong consumer spending, is likely to drive corporate earnings growth above 10%, leading to positive impact on valuations. Despite valuation levels starting above their historical average, a positive growth outlook and the shift towards more expansionary monetary policies by Central Banks will fuel further optimism. Within this scenario, **we suggest tilting the allocation towards Quality and Growth sectors, with a geographical bias for the United States** due to its stronger macroeconomic resilience.

CURRENCY MARKETS – In 2025, a marginal slowdown in global growth is likely to favour the dollar against all other currencies, especially the euro. In our view, Donald Trump's re-election, marked by the introduction of tariffs first against China and eventually other countries, will primarily result in a strengthening of the dollar against major currencies. Furthermore, the new US presidency could slightly increase the risks of a slowdown in the disinflationary process towards the end of 2025, prompting the Fed to adopt a more cautious approach to rate cuts.

WHAT COULD CHANGE OUR SCENARIO?

Our optimistic stance on the macroeconomic outlook and major asset classes could be undermined by a range of factors, varying from regulatory and/or geopolitical nature.

In terms of regulatory risks, Donald Trump's election alongside the "republican sweep" have increased uncertainty surrounding **global trade policy** frameworks. During his fervent electoral campaign, the Republican candidate floated the idea of a potential 10% blanket tariff on all imports to the US and a 60% tariff on Chinese goods. Should these measures be enacted, trade volumes would decrease, which could adversely affect corporate profitability and lead to inflationary pressures. These consequences could be exacerbated in the event of retaliatory actions.

A further risk associated with the upcoming US presidency's decisions is linked to the adoption of **stricter measures to control and limit immigration**, which would reduce the labour supply and could generate inflationary pressures through higher wages.

Not forgetting decisions regarding **the regulation of American Big Tech and the Green Economy,** considering Trump's past antagonistic comments on Media & Entertainment companies (several of which are already making financial headlines) and the alternative energy sector. The tycoon has always been in favour of traditional energy sources, appointing Chris Wright, an executive from a fossil fuel-related company, to lead the Department of Energy: there is also speculation about the US potentially withdrawing from the Paris Climate Agreement again and restarting drilling in the Arctic. In addition to the environmental impacts, the purely economic repercussions should not be overlooked: **Trump could abolish or reduce the impact of the Inflation Reduction Act (IRA)** approved in August 2022 by Biden, which allocated $433 billion, with $369 billion specifically dedicated to domestic energy production and renewable energy development.

Among geopolitical risks, an **intensification of the conflicts in Ukraine and the Middle East**, along with a flare-up of **tensions between China and Taiwan**, are certainly significant concerns. This latter scenario, in addition to increasing market volatility, would negatively impact semiconductor production, with detrimental consequences for a wide range of industries: from consumer electronics to automobiles, from aviation to healthcare equipment, and of course, Artificial Intelligence (Taiwan accounts for over 60% of global chip production, with 90% for the most advanced models).

Other risks are related to **companies' ability to innovate and continue exceeding** investors' expectations. The biggest threat comes from the world of **Artificial Intelligence** (AI), a sector that has driven the rally in US and global equity markets thanks to optimistic earnings growth projections: if these forecasts fail to materialise, a significant correction could occur. Another market-specific risk is **liquidity**, particularly in the high-yield corporate bond sector: spreads are near historic lows and could widen abruptly if liquidity dries up, negatively affecting the equity asset class as well.

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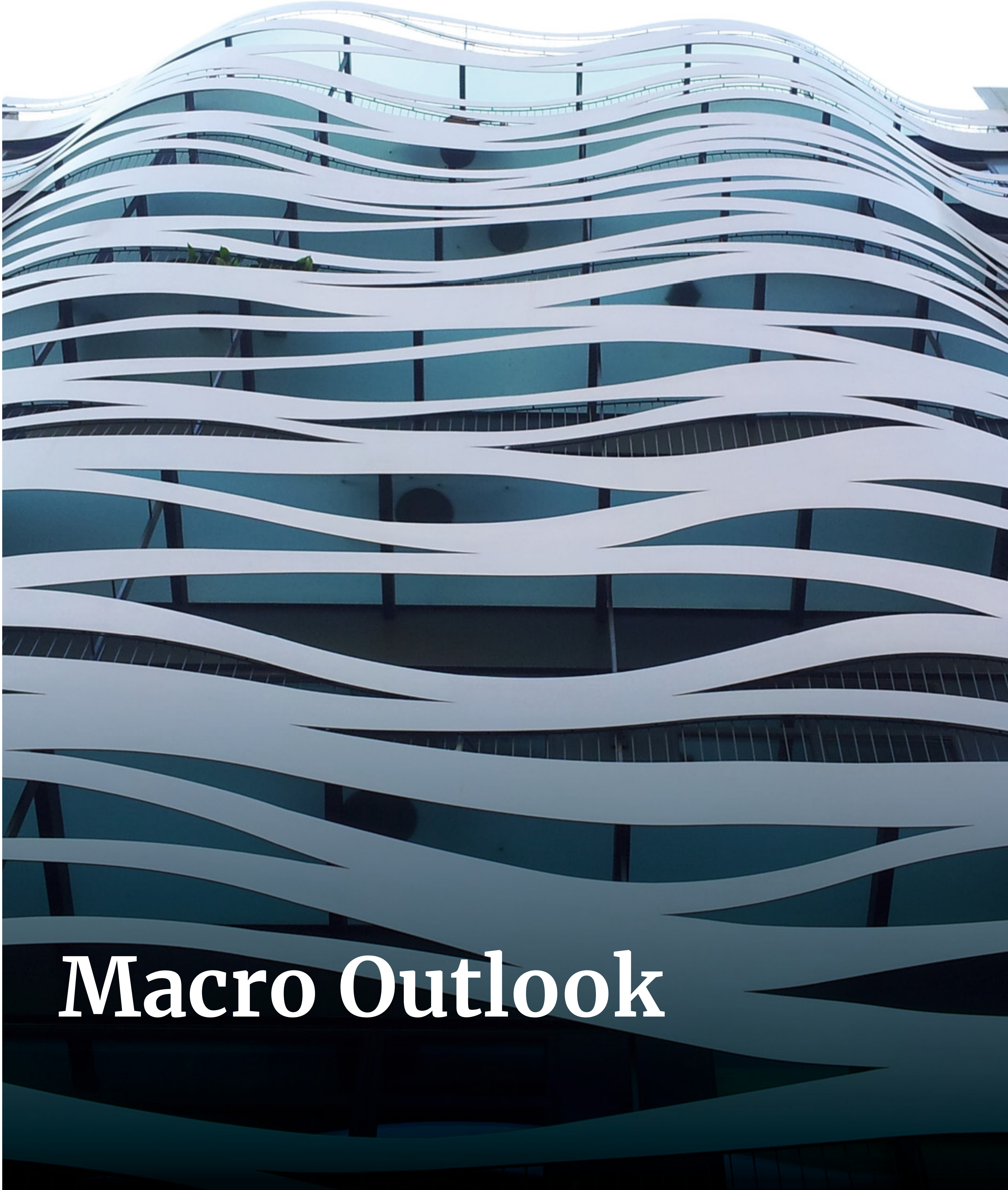


Macro Outlook

GROWTH

TABLE 1 – REAL GDP GROWTH BASELINE

Baseline scenario - Growth in the US, Eurozone and China

	USA	EA	China
	Q/Q %, SAAR	*Q/Q %*	*Y/Y %*
2023	**2.9**	**0.5**	**5.2**
Q1 24	1.6	0.3	5.3
Q2 24	3	0.2	4.7
Q3 24	2.8	0.4	4.6
Q4 24	2.6	0.2	4.4
2024	**2.8**	**0.8**	**4.7**
Q1 25	2.4	0.2	5
Q2 25	1.9	0.2	4.5
Q3 25	1.8	0.2	4.3
Q4 25	1.7	0.2	4.1
2025	**2.3**	**1.0**	**4.6**

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

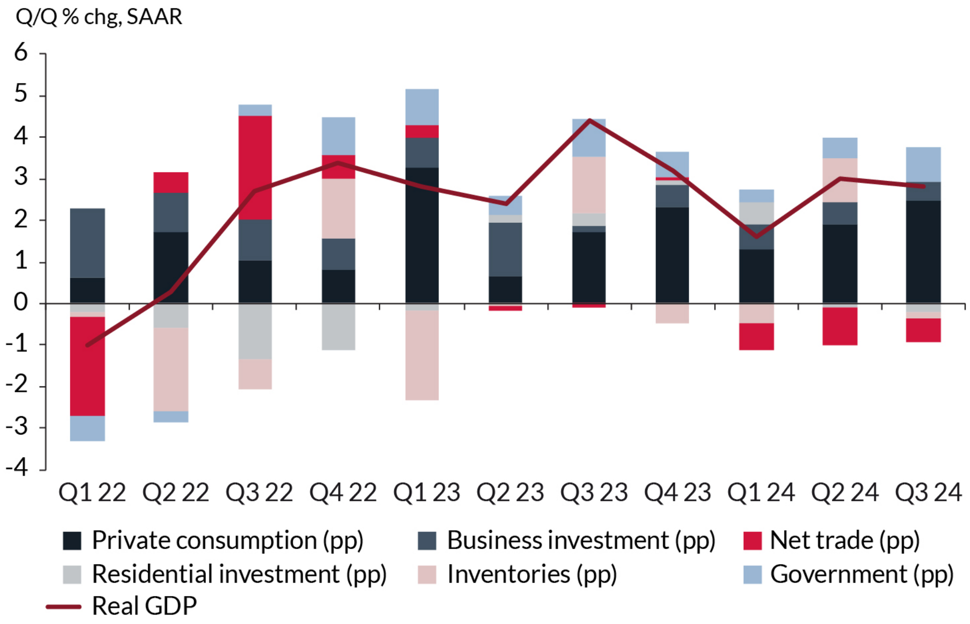
US – From soft to softer

We stick to the view that the US economy remains on a "soft" soft landing path led by consumer spending. Over the forecast horizon (2025) macro policies pledged by President-elect Trump should not have meaningful impact on our above-consensus baseline that remains consistent with a quarterly pace of growth of 2.3%.

Private consumption: the gift that keeps on giving. Growth came in on the strong side in Q3 (2.8%), only slightly below Q2 (3.0%). The expenditure breakdown reports also broadly the same drivers, with households being the growth stronghold led by a rebound in goods spending and stable services consumption (**Figure 1**).

FIGURE 1

Real GDP growth proved more than resilient



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

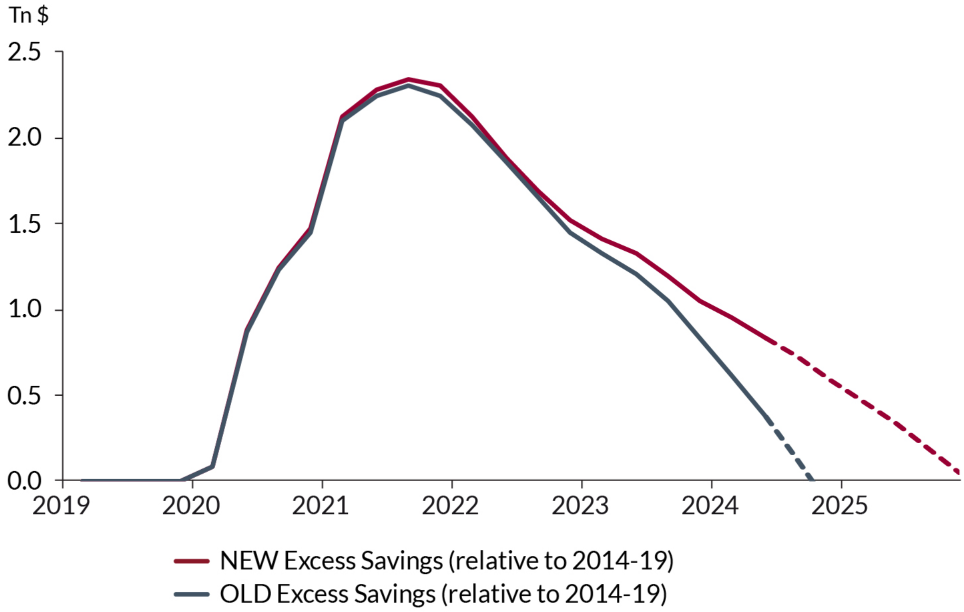
Consumers are better off than anticipated. The latest BEA revision to national accounts data indicates that the US economy has been growing quicker and generating more income than earlier estimates suggested. Applying our estimation methodology to the adjusted trajectory of household savings through Q2 we now estimate that excess savings accumulated since the beginning of the pandemic will reach nearly $840 billion by Q2 2024 (**Figure 2**). This level is adequate to allow for a drawdown of $100 billion per quarter until Q4-25 as opposed to our earlier assumption of Q4-24.

Against this backdrop, we have adjusted our medium-term outlook for the US economy. On the one hand, the latest data strengthens our conviction that the US will avoid a recession next year. On the other hand, we now expect a "softer" soft landing than we had thought. With increased savings and stronger nominal and real disposable income (**Figure 3**), it appears that US consumer momentum may persist longer than we had earlier estimated.

In the United States, the robustness of macroeconomic data flow and revisions by the Statistics Office indicate a slower and less significant weakening of consumption trends

FIGURE 2

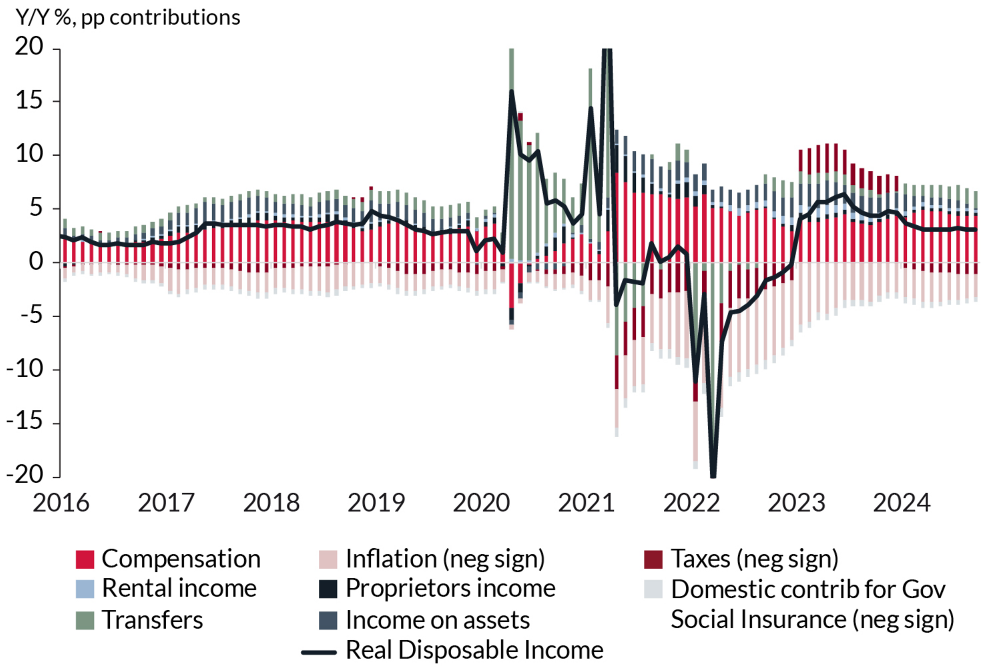
Consumers still have a large stock of excess savings



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

FIGURE 3

Real disposable income offers some more support



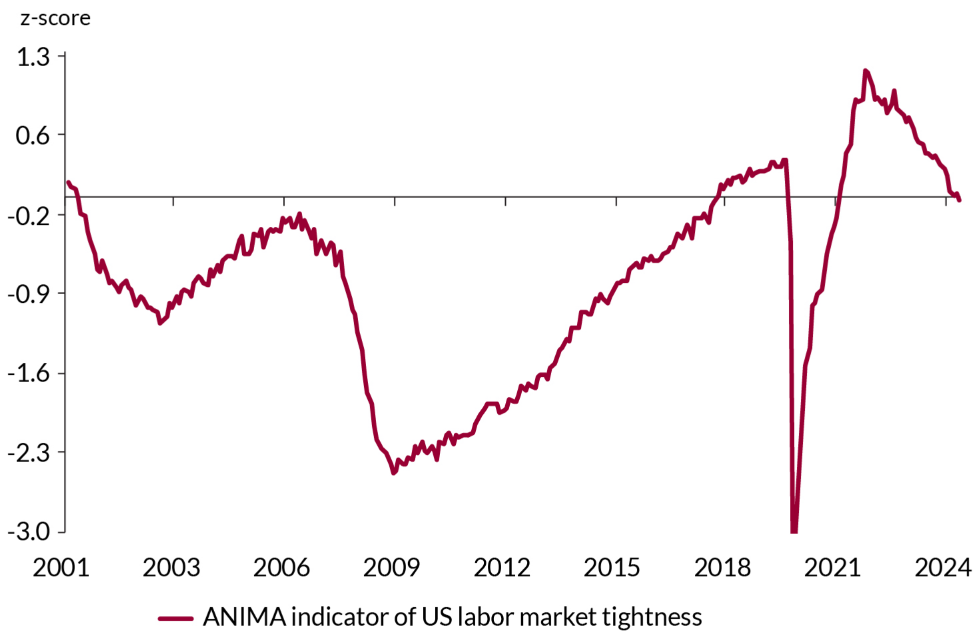
Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

We expect the US economy to grow by 2.3% next year, well above consensus forecasts (1.9%). Given the robust consumer balance sheets highlighted by the latest BEA data, we believe that household spending momentum will taper off more gradually. On a quarterly basis, our updated outlook suggests that the US economy may dip below potential in Q3 next year, although the risks point to a later downturn. Our growth forecast is consistent with our baseline projection that underlying inflationary pressures will keep easing. While we have found that the level of excess savings is nearing what was observed at the end of Q3-23, we believe that current labor market conditions are less reassuring for households than they were previously (**Figure 4**).

In 2025, we foresee only a slight weakening in momentum: our projected growth is above the consensus estimate

FIGURE 4

The labour market is gradually rebalancing



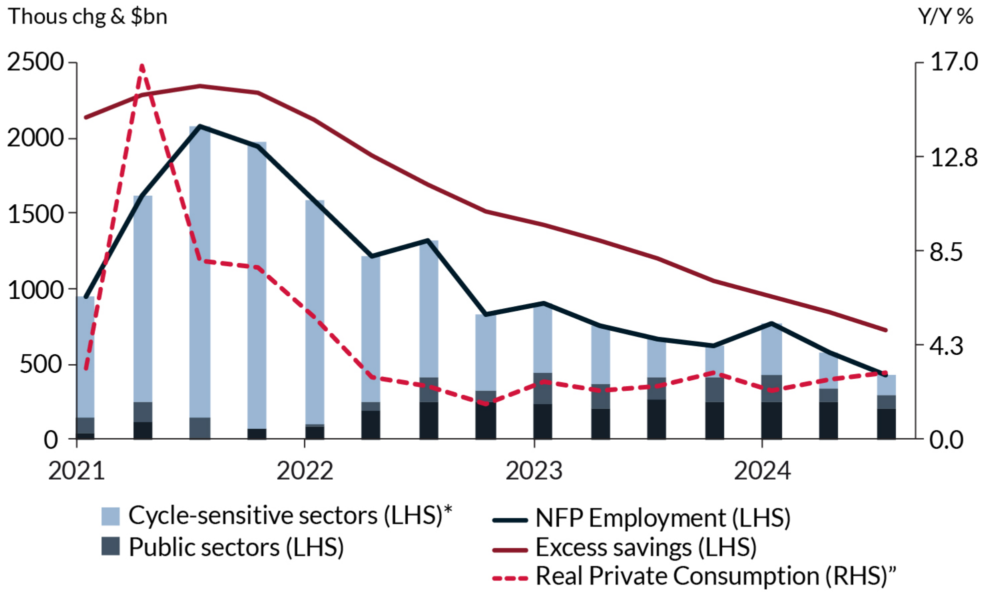
Average of z-scores for Quits rate, Unemp rate, Openings/Unem ratio, Prime-age emp/pop ratio. Difference from pre COVID levels are shown.

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

Re-acceleration risks? Unlikely. Despite stronger household fundamentals, we do not expect the US economy to regain momentum. While excess savings are reported to be higher than previously understood and will likely be depleted more slowly than we had assumed, the backing provided by the labor market is now weaker than it was before. With hiring slowing and labor demand undergoing considerable rebalancing, consumers are anticipated to moderate their excess savings drawdown in the coming period (**Figure 5**).

FIGURE 5

A slowing labour market is unlikely to stimulate an increase in spending



**Note: Cycle-sensitive sectors = leisure/hospitality svs, prof/business svs, manufacturing, financial activities, retail trade, transportation and construction.*

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

ANIMA baseline. Against this macro backdrop and given that the policy mix proposed by the re-elected Trump is unlikely to boost growth notably over the forecast horizon, we maintain our baseline largely unchanged. We project growth at 2.6% q/q SAAR for Q4-24 (vs 2.5% prior) – consistent with an annual growth rate of 2.8% (vs 2.7% prior). For 2025, we continue to expect growth at 2.3%. In sequential terms, we forecast growth at 2.4% in Q1-25 (vs 2.3% prior), 1.9% in Q2-25 (vs 1.8% prior), 1.8% in Q3-25 (vs 1.7% prior) and 1.7% in Q4-25 (vs 1.6% prior).

EA – Strained path

In the EA, incoming data shows that the near-term growth outlook has deteriorated further. We anticipate growth to underperform its potential in Q4-24, reaching 0.2% q/q (0.7% 2024 annual average). We continue to expect a pick-up in growth in 2025, but at a slower pace than the previous baseline. We expect growth to remain slightly below potential at 0.9% in 2025 (vs 1.3% previously expected).

There's less substance beneath the surface. The preliminary release of EA GDP growth came in slightly stronger-than-expected, accelerating 0.4% q/q, up from 0.2% in Q2.

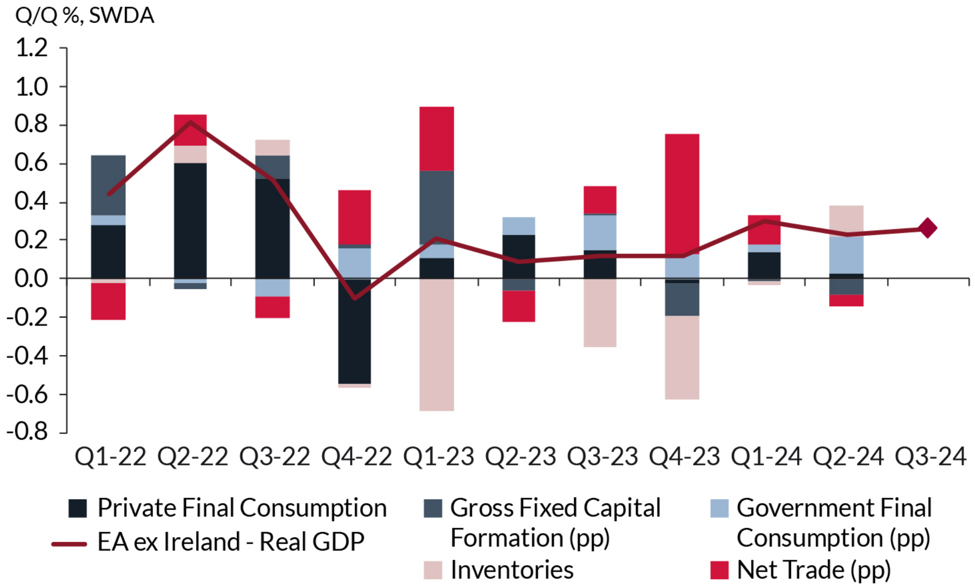
However, preliminary indications suggest that the data was biased to the upside by idiosyncratic and one-off factors.

1. Firstly, excluding notoriously volatile Irish numbers, GDP growth was 0.3% q/q in Q3, marking a modest acceleration from the 0.2% seen in Q2 (Figure 6).

In the third quarter, GDP growth in the Eurozone exceeded expectations, but this was due to idiosyncratic factors and one-off events

FIGURE 6

Real GDP Growth: Under Pressure



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

2. Secondly, the uptick in domestic demand was likely driven by Spain – where government spending saw one of the highest sequential gains since 2004 – and by France – where the Olympics boosted household consumption.
3. Moreover, deceleration in fixed investments and net trade was noticeable and widespread across various countries.

As neither of those forces is likely to sustain momentum, we expect the EA growth to return to a modestly below-potential rate (0.2%) from Q4 onwards, with this pace likely to continue on average throughout the next year.

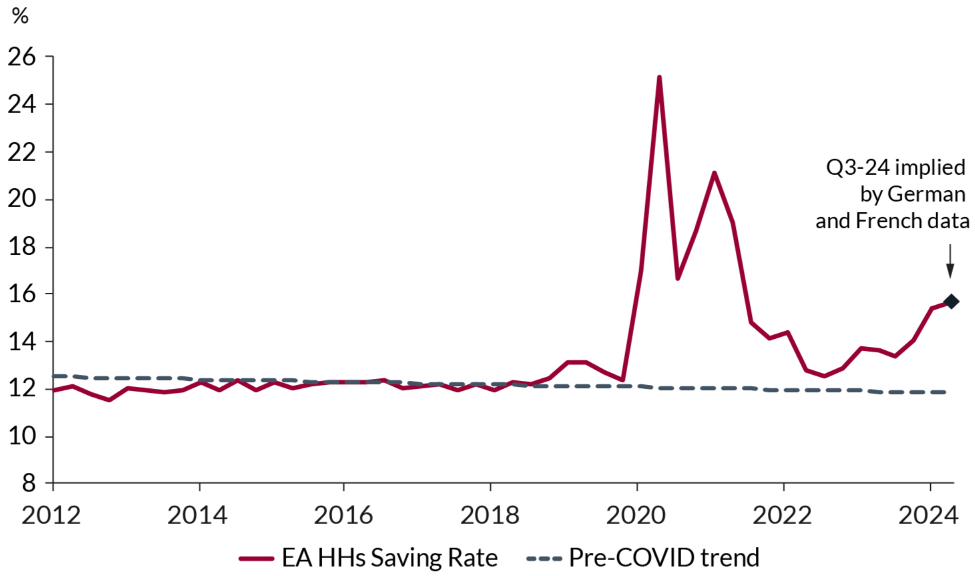
We expect the recovery to remain weak and below potential through 2025

Nowhere to be found. Consequently, we continue to expect a pick-up in growth in 2025, but at a slower pace than the previous baseline. We now expect growth to remain slightly below potential at 1.0% in 2025 (vs 1.3% previously expected). In sequential terms, we forecast GDP at 0.2% q/q from Q1 to Q3-25 and 0.3% in Q4-25. Our forecast is below the consensus and ECB staff projection for September (both at 1.3% for 2025).

European consumers continue to behave cautiously, much like ants. The household saving rate continued to rise in Q3, remaining well above the pre-COVID levels (**Figure 7**).

FIGURE 7

Consumer caution continues to prevail

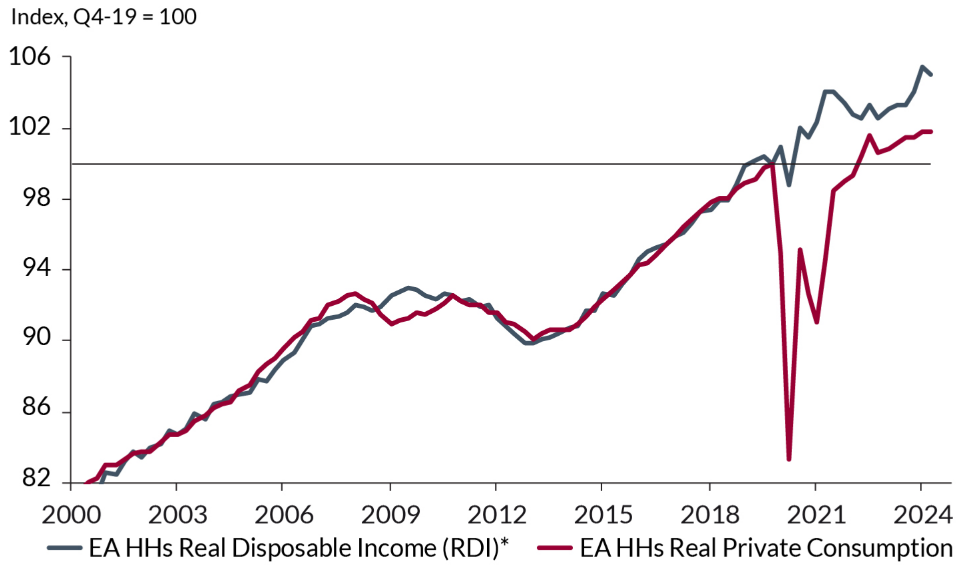


Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

As a result, consumption has not improved despite strong gains in real disposable income (Figures 8 and 9).

FIGURE 8

The gap between real incomes and consumption remains wide

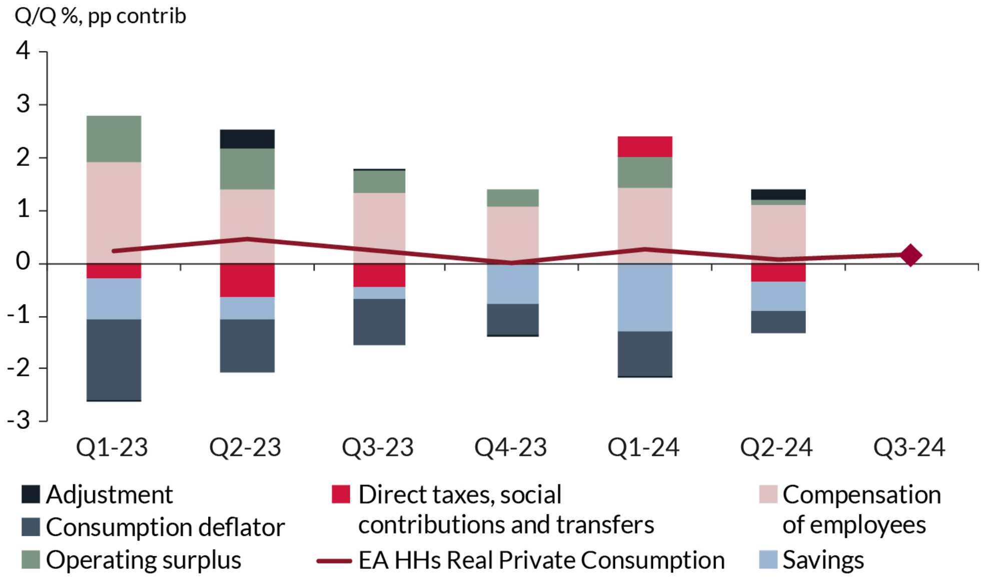


** Deflated by GDP Private Consumption*

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

FIGURE 9

Private consumption continues to be restrained



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

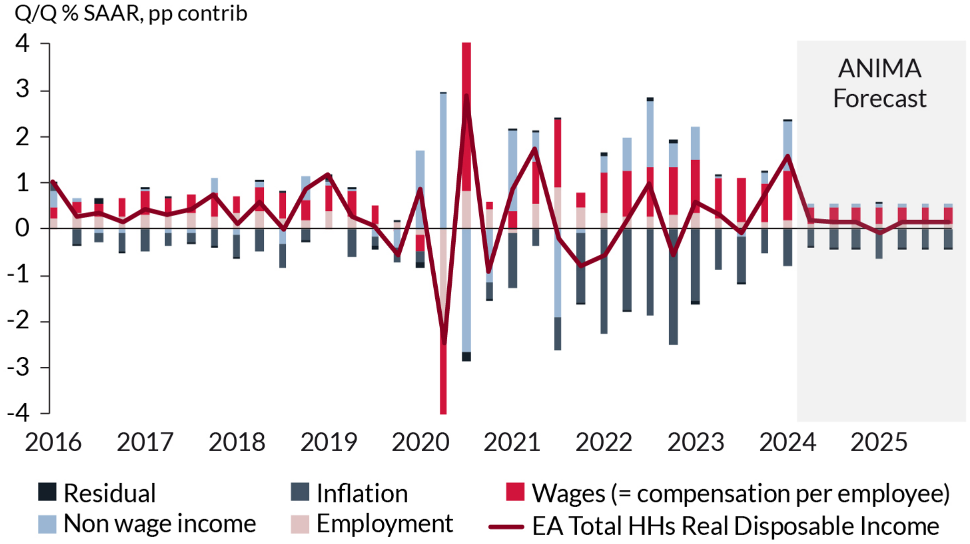
We believe that private consumption growth will remain modest. The reason for this is that real disposable income has likely peaked, the labor market outlook is showing slight signs of deterioration, and although we do not expect the saving rate to increase much further, it is likely to normalize towards pre-COVID levels at a slower rate.

End of the road for real income gains. Real gross disposable income (GDI) in H2-24 grew by more than 1.2pp compared to its pre-COVID trend. However, it has now peaked, and we expect it to decelerate towards trend in 2025 for the following reasons:

1. About 80% of the real GDI was generated by the compensation-per-employee contribution (i.e. income) – (**Figure 10**). Since we expect wage growth to decelerate moving forward, due to the catch-up process with past inflation being largely exhausted (**Figure 11**), it should no longer act as a driving force for GDI growth.
2. Employment growth has reverted to trend levels, and soft data suggest a stabilization, if not a slight slowdown.

FIGURE 10

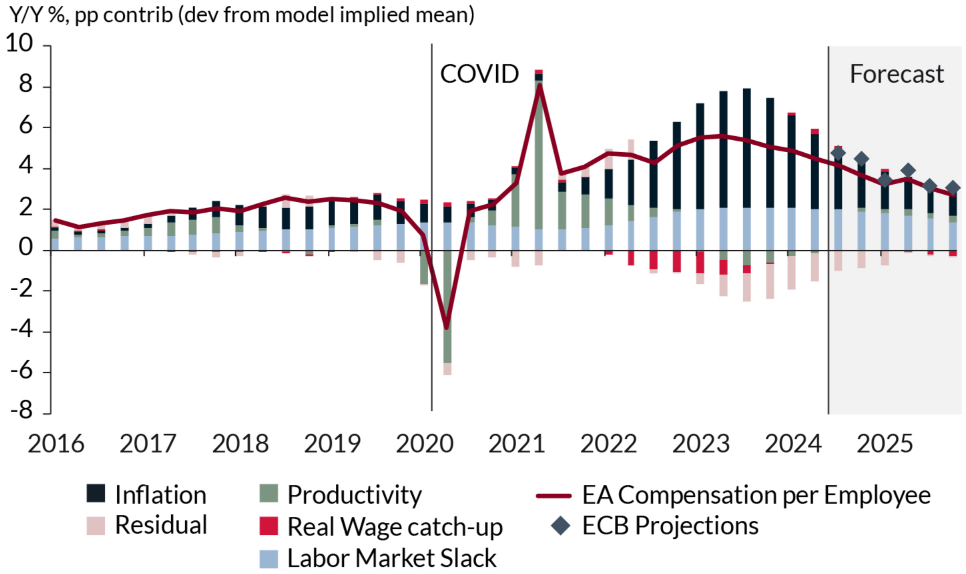
Real disposable income growth has likely peaked...



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

FIGURE 11

... largely driven by a deceleration in wage growth



Model based on an augmented Phillips curve that relate sequential growth in compensation per employee to measures of labor market slack, inflation catch-up and other factors (including lagged wage growth, trend labor productivity per person employed). Real wage catch-up (gap to trend) measures the wage level that is justified by labor productivity.

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

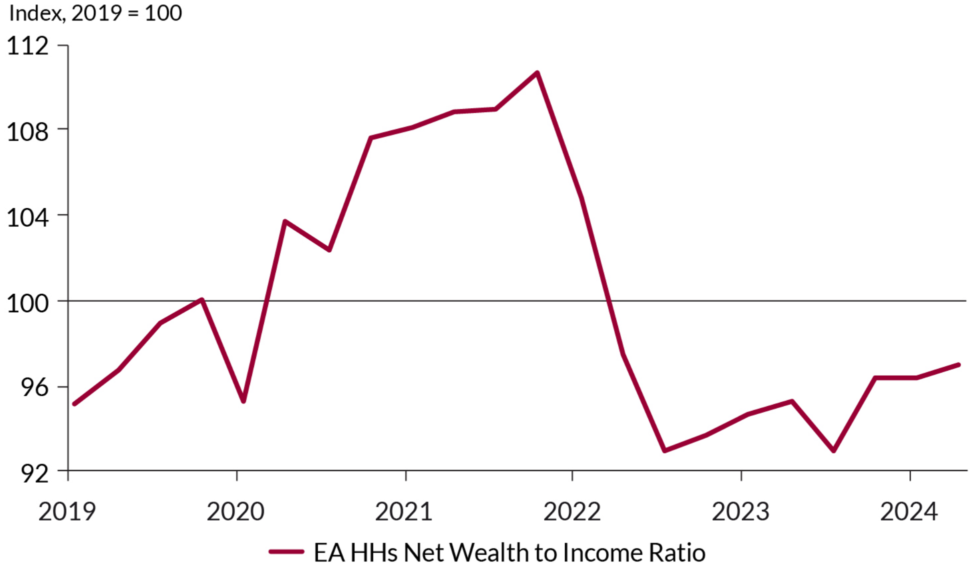
Against this backdrop, we expect real disposable income to normalize next year.

Slower normalization of savings behavior. The recent increase in the saving rate, despite the strong recovery of the real GDI, has prevented the recovery of private consumption.

We believe that the recent increase in the saving rate is mainly attributable to higher interest rates compared to pre-COVID which have influenced the propensity to save; and the need for households to rebuild their real net financial wealth, which as of today is still below 2019 levels (**Figure 12**).

FIGURE 12

Households still need to rebuild their net wealth



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

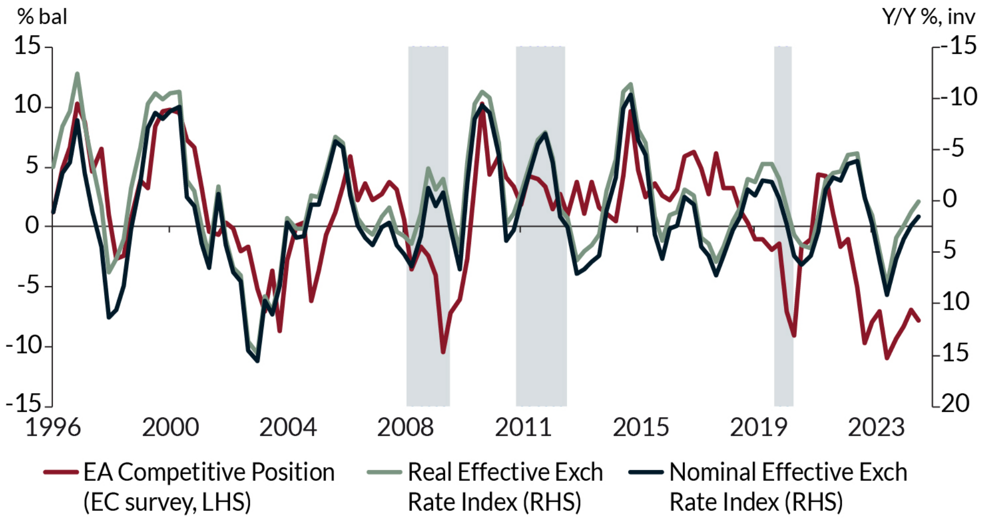
Against this backdrop, we have downgraded private consumption growth (on average) by 0.1pp in 2024 and 2025 compared to the previous baseline.

Fixed investment lagging. The manufacturing industry continues to remain weak. We highlight that the depression is attributed to both idiosyncratic factors, such as the energy crisis in Germany and external factors, including sluggish global demand.

The prospects are not good. While we expect fixed investments to benefit from easing financial conditions (Figure 16), we believe they are unlikely to return to a sustained growth trajectory. This is due to several reasons: 1) Even with a lower cost of capital, narrower credit spreads, and rising equity prices, investment intentions are still subdued, and the rate of new business creation remains flat. 2) Competitiveness prospects continue to remain weak (**Figure 13**); 3) Global political uncertainty remains elevated. 4) Our non-financial corporate vulnerability monitor suggests that fundamentals are weakening. Profit margin compression, limited credit origination, and persistently high debt financing costs are contributing to this trend (**Figure 14**).

FIGURE 13

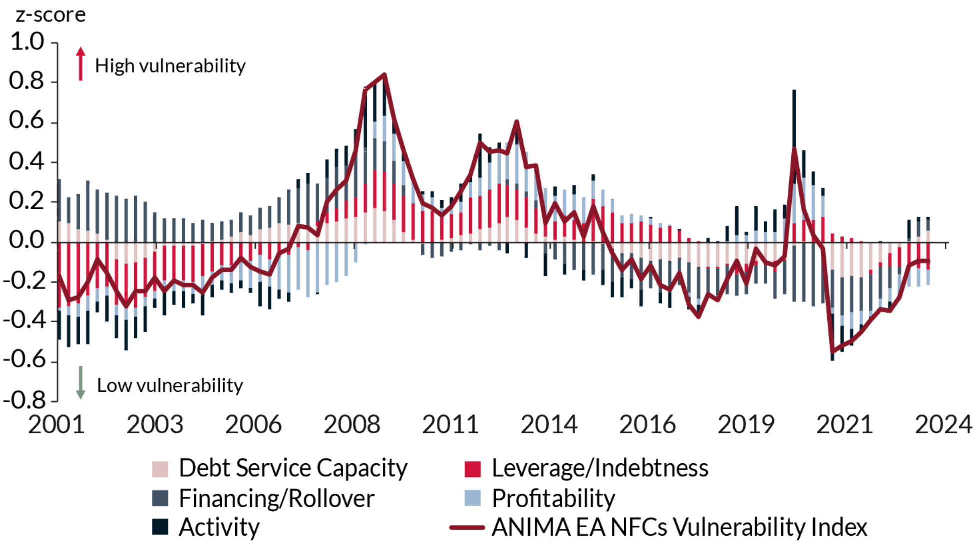
Competitiveness prospects are poor



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

FIGURE 14

The corporate balance sheets are starting to creak



Note: The composite measure is based on a broad set of indicators along five dimensions: debt service capacity (measured by the interest coverage ratio, corporate savings and revenue generation), leverage/indebtedness (debt-to-equity, net debt-to-EBIT and gross debt-to-income ratios), financing/rollover ((short-term debt-to-long-term debt ratio, quick ratio (defined as current financial assets/current liabilities), overall cost of debt financing and credit impulse (defined as the change in new credit issued as a percentage of GDP)), profitability (return on assets, profit margin and market-to-book value ratio) and activity (sales growth, trade creditors ratio and change in accounts receivable turnover). Except for the overall cost of debt financing and GDP, all indicators are based on data from the ECB's quarterly sector accounts. The overall cost of debt financing indicator is calculated as a weighted average of the costs of bank borrowing and market-based debt, based on their respective amounts outstanding.
Based on ECB methodology presented in "Assessing corporate vulnerabilities in the euro area".
See here: https://www.ecb.europa.eu/press/economic-bulletin/articles/2022/html/ecb.ebart202202_02~7a61e442be.en.html

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

Given this context, we have downgraded fixed investment growth (on average) by 0.1pp in 2024 and 2025 compared to the previous baseline.

ANIMA baseline. We expect growth to underperform its potential in Q4-24, reaching 0.2% q/q. This results in a growth rate of 0.7% for 2024. For 2025, we expect growth to remain slightly below potential at 1.0% in 2025 (vs 1.3% previously expected).

China – Push and pull

Going into 2025, growth prospects will be a function of authorities' support on the one hand and Trump's administration policies on the other. Net, we downgraded our growth forecast: we now expect 2025 growth at 4.4%.

Momentum remains weak. Following a weaker-than-expected Q3 GDP, economic activity challenges have intensified in Q4. Despite ongoing support from exports, October soft data suggest a stall in domestic demand.

Going into 2025, growth prospects will be a function of authorities' support on the one hand and Trump's administration policies on the other. We expect supportive measures for the property sector to be announced in December, during the CEWC conference, at the earliest. This is very important as the real estate sector backdrop has barely changed lately. House prices remain in free fall amid weak consumer confidence and wide supply/demand imbalance. At the same time, though, we expect Trump Administration to move fast on bilateral tariffs that we expect to become effective by Q2 next year.

China's economic outlook is very weak; 2025 trends will hinge on how domestic government stimulus efforts interact with US trade policies

Net, we downgraded our growth forecast to 4.4%. Given: 1) the fact that real estate support, while appropriate in principle, might take time to work out and 2) tariffs will quickly hit the only growth engine now at work in China, we believe that the overall net impact on Chinese growth for next year will be negative.

Tariffs – Artificial barriers to the free movement of goods or factors between countries. They often take the form of indirect taxes applied to imported or exported goods.

ANIMA Baseline. We stick to our 2024 annual growth profile, and we continue to expect GDP to grow by 4.8% y/y. As per 2025, following the outcome of the US presidential race, we trim to the downside our GDP growth baseline to 4.4% from 4.7% y/y as the event significantly increased exogenous risks faced by the Chinese economy, with US tariffs likely to be announced in Q1-25 and being effective from Q2-25.

INFLATION

TAB. 2 - INFLATION BASELINE

	CPI Core US	PCE Core US	HICP Core EA	CPI Headline China
	Y/Y %	Y/Y %	Y/Y %	Y/Y %
2023	**4.8**	**4.1**	**4.9**	**0.2**
T1 24	3.8	2.9	3.1	0.0
T2 24	3.4	2.7	2.8	0.3
T3 24	3.2	2.6	2.8	0.6
T4 24	3.2	2.7	2.7	0.4
2024	**3.4**	**2.7**	**2.8**	**0.4**
T1 25	3.0	2.4	2.4	0.5
T2 25	2.8	2.3	2.3	0.5
T3 25	2.8	2.3	2.2	0.5
T4 25	2.6	2.2	2.2	1.3
2025	**2.8**	**2.3**	**2.3**	**0.7**

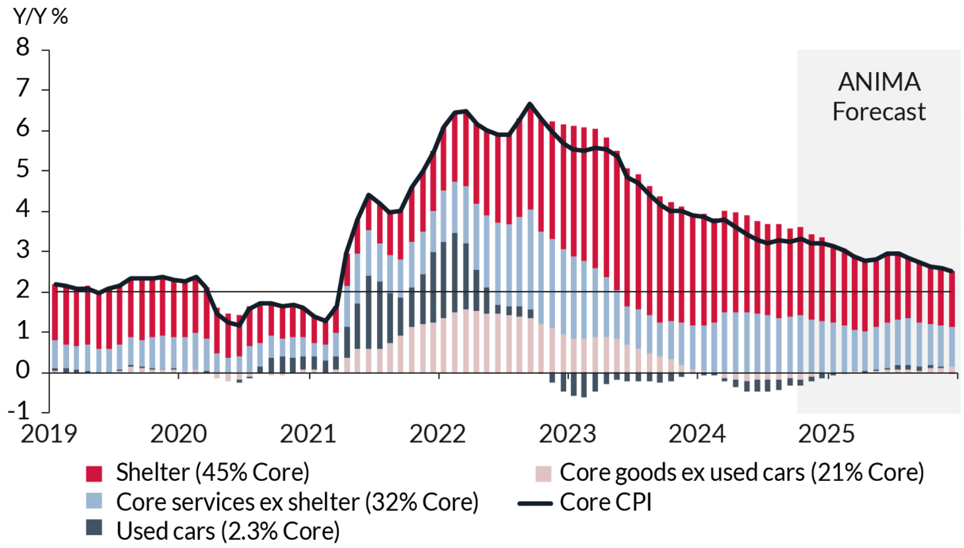
Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

US – Disinflation intact

*We expect US inflation to keep heading towards its target over the forecast horizon. We project core CPI inflation to average at 2.8% in 2025, down from 3.4% in 2024 (**Figure 15**). We believe that with a renewed Trump presidency and a unified Congress there may be upside risks as the threats associated with a global trade war would be greater this time. However, we also believe that the implementation of tariffs will have a material impact outside our forecast horizon and will be an issue from 2026 onwards.*

In the US, disinflation is likely to stabilise over the next few quarters, but political developments could lead to upside risks beginning in 2026

FIGURE 15
US - Inflation baseline



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

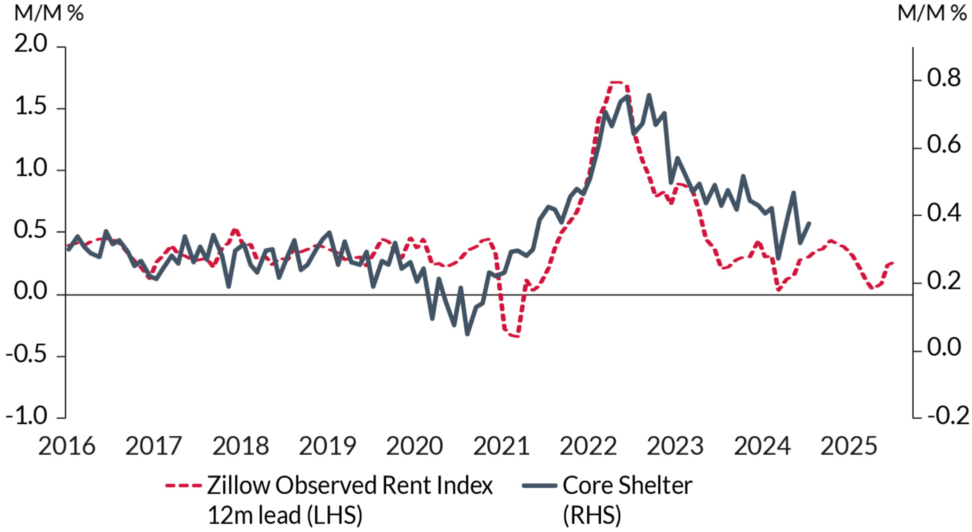
Par for the course. The headline CPI inflation rate slowed to 2.6% on a year-ago basis in T3-24, the slowest annual pace of inflation since early 2021. Excluding the volatile energy and food prices, the unwinding of pandemic-era price distortions has proven to be more "up like a rocket and down like a feather." Indeed, the core CPI inflation rate plunged to 3.2% y/y in T3-24 after peaking at 6.3% in T3-22.

Core goods: well-behaving. The benefits of smoother supply chains and cooler demand still have yet to run their course. After a temporary pickup in core goods prices in September, goods deflation should resume in the final months of this year. Looking ahead to 2025, we expect core goods inflation to continue in line with its pre-COVID trend.

Core services: gradual progress. At 4.8% year-over-year in September, services categories remain the laggard in terms of core inflation settling back down, but service providers should continue to benefit from more stable prices for goods inputs moving forward. Meantime, the ongoing softening in the labor market and pickup in productivity growth are reducing inflationary forces from labor inputs—dynamics that will help limit goods and services inflation alike. Milder shelter inflation seems only to be a matter of time. In this regard, we continue to anticipate disinflation in the core shelter space (i.e. rent of primary residence + OER), creeping toward their pre-pandemic trend of about 0.25% m/m in 2025, consistent with private data on observed rents that have been trending lower amid an increase in supply of multifamily units (**Figure 16**). Beyond shelter prices, we believe that in the core-services ex-housing sector the deceleration process will proceed rather smoothly. Many of the items that we define as macro-reopening sensitive (MV insurance, recreation services, food services etc.) have already normalized to the pre-COVID trend.

FIGURE 16

Leading indicators for core shelter continue to point south



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

The Sheriff is back in town. With the renewed Trump presidency and a unified Congress upside risks are posed to our inflation baseline as the threats associated with a global trade war would be greater this time. While they are unlikely to materialize in 2025 owing to implementation issues, they have the potential to push up US inflation from 2026 onwards. That said, quantifying the magnitude at this stage is very difficult. The introduction of a universal baseline tariff is a serious threat, though institutional constraints, lack of public and political support and strategic considerations may dampen the sanguine approach of the administration.

Information to date is scarce but what we can do is to analyze how US inflation behaved during the first wave of tariffs in the previous Trump presidency.

1. **There are lessons to be learned**. The 2018 trade war seemed to avoid the worst-case outcome critics had feared. The impact on core CPI inflation stemming from higher tariffs, including on goods and services excl. housing, was muted. According to our calculation, only 15% of the core goods basket experienced a temporary rise in inflation from -0.5% in January 2018 to 1.3% y/y in January 2019. This was offset by slight disinflation in the remainder of the basket, resulting in core goods CPI inflation hovering around zero in 2018- 2020 (**Figures 17 and 18**).

FIGURE 17

Impact of 2018-19 tariffs on Core Goods CPI (Index)

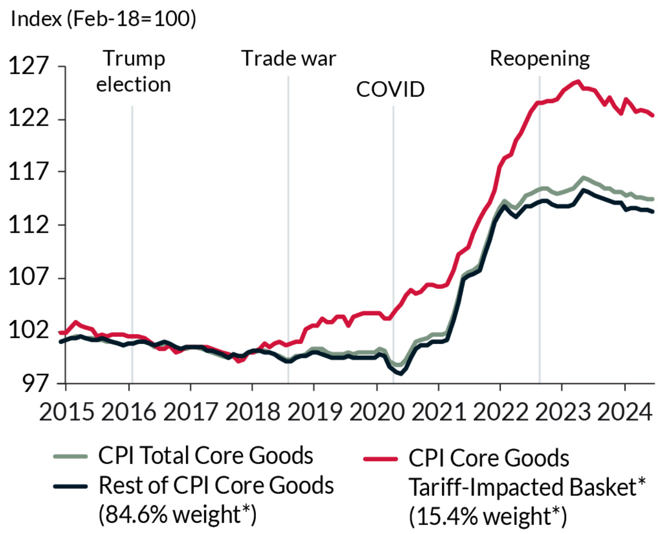
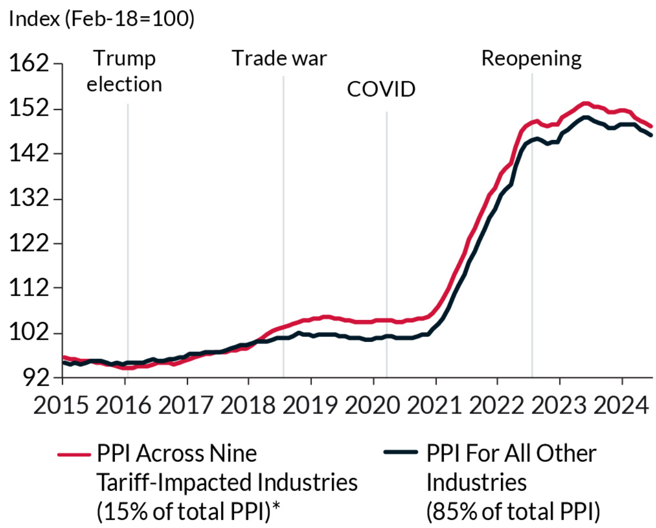


FIGURE 18

Impact of 2018-19 tariffs on Core Goods PPI (Index)



* *Basket constructed with the following CPI items: Laundry Equipment; Other Appliances; Furniture and Bedding; Floor Coverings; MV parts and equipment; Sport Vehicles including Bicycles; Housekeeping Supplies; Sewing Machines, Fabric and Supplies - weighted by their relative importance weights. Same as for PPI.*

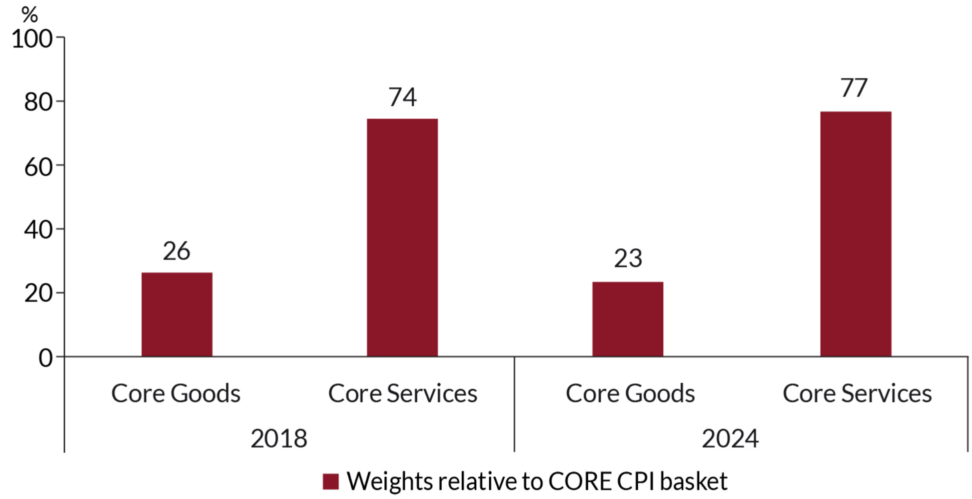
Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

2. **Although the latest proposed tariff increase on Chinese imports is 3x larger than that announced in 2016, offsetting factors should still allow for a benign impact on US core CPI inflation**. The overall weight of core goods prices within the CPI basket is 23% - 3pp below that of 2018 (**Figure 19**), while imports from China, especially those related to goods affected by the first wave of tariffs (tariffable goods) are 37% below 2017 levels (on average; **Figure 20**). Unless President Trump widens the scope of its action to those goods deemed non-tariffable in 2017, the overall impact on Chinese tariffable goods inflation should not be dissimilar to that generated by the 2018 tariff war.

The increase in tariffs in 2017 did not cause inflation, and multiple factors should mitigate their impact on this occasion too

FIGURE 19

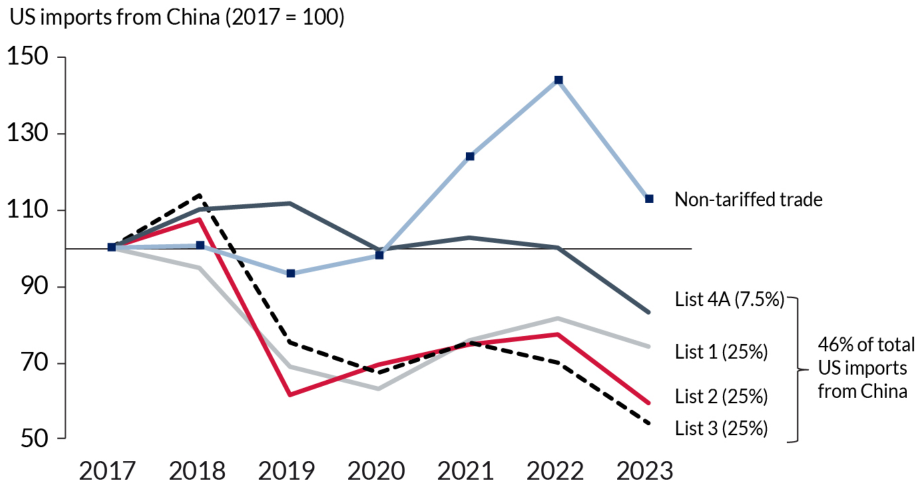
CPI relative weights: Goods vs Services (2018 vs 2024)



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

FIGURE 20

US total imports from China by 2018/19 by tariff category



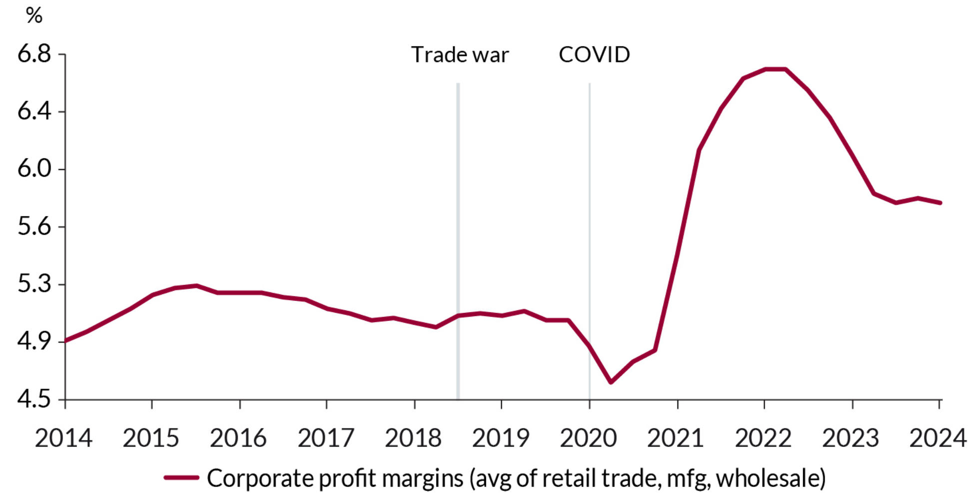
Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

3. **Most of the literature finds that the US bore almost entirely the cost of its own tariffs**. Against the backdrop of an economy experiencing a soft landing and excess savings that have been depleted by low- and middle-income cohorts—likely the largest spender of tariffable goods imported from China—we expect businesses to continue to prefer to take the hit on their margins, rather than risk losing market shares by passing tariff increases onto consumers. We acknowledge that larger tariffs than those announced in 2016 might be more challenging to be absorbed; however,

the profit margin outlook is much brighter now than in 2018. In aggregate, corporate profit margins have grown by about 14% compared to 2017, across industries (**Figure 21**).

FIGURE 21

Aggregate corporate profits margin (national accounts data)



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

EA - 2025: the second half of the disinflation story

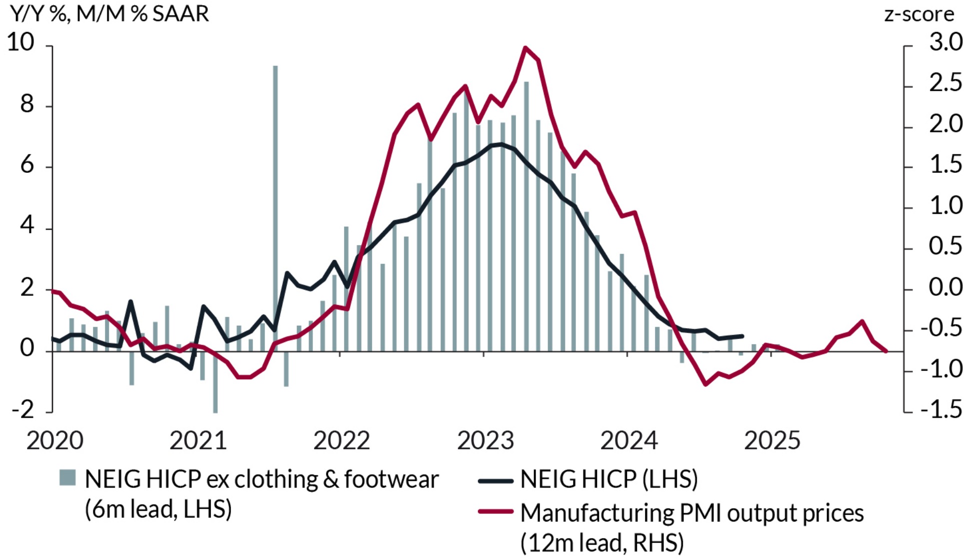
We remain of the view that core inflation will continue to decline next year. We expect services prices to take the lead in the process as core goods items are set to move sideways. Several idiosyncratic factors that kept non-tradable prices elevated this year, including technical adjustments, calendar effects and one-off events will likely payback in 2025.

Disinflation will continue in the Eurozone, driven by service sector prices. The technical and idiosyncratic factors at play in 2024 will dissipate

Continued normalization in core goods. During H1-24 core goods inflation decelerated significantly: in terms of year-on-year inflation rate it stood at 0.5% y/y in Q3-24, in line with the pre-COVID trend. Overall, we believe that core goods prices are now on a path of stabilization. This is in line with the trends observed in leading indicators (PMI manufacturing input/output prices and EC manufacturing prices expectations) (**Figure 22**).

FIGURE 22

Core goods inflation normalized

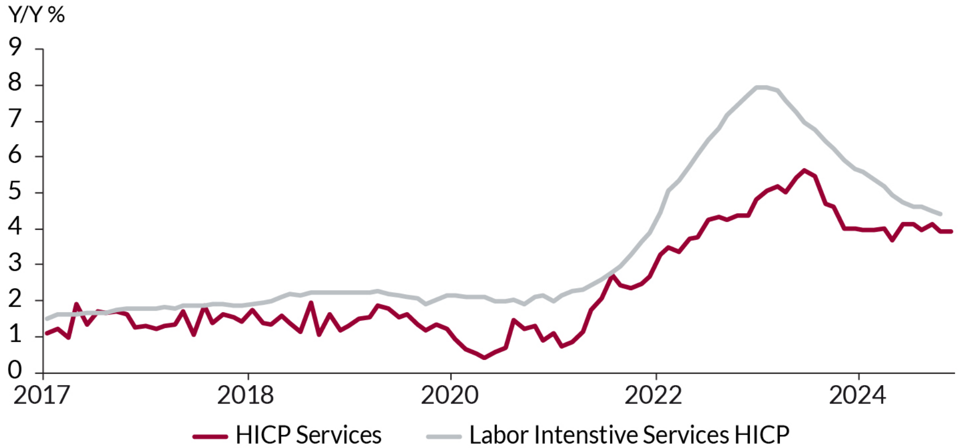


Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

Services strength will continue in 2024. Services inflation remained rather sticky during this year, keeping (on average) unchanged in the 3.9/4.0% range. We believe that service items that are most sensitive to wages will continue to ease very slowly during Q4-24 and will remain above pre-COVID seasonal patterns until H2-25, reflecting a catch-up with past wage pressures in a relatively tight labor market (**Figure 23**).

FIGURE 23

Services inflation more linked to wage pressures remains sticky



'Labour intensive services' (restaurants and cafés, hairdressers, car maintenance). This bucket represents 20% of the services basket and is made of components which are (1) labour-intensive; (2) not regulated; and (3) not influenced by the calendar. This is why you will not find hotels (too calendar-dependent) or health services (too regulated) here.

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

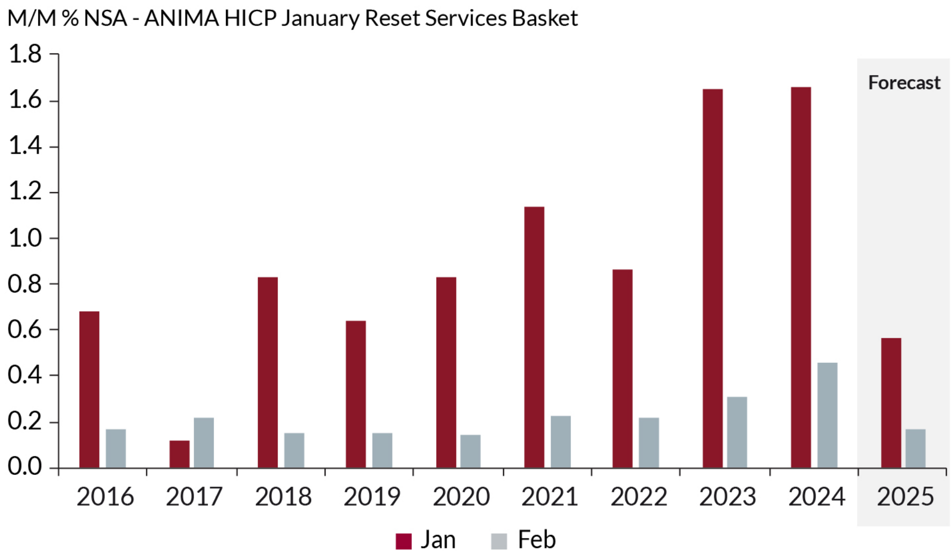
More softening in 2025. We retain our call that from Q1-25 onwards the deceleration of services will take hold in a moderately more pronounced manner than so far. As a result, we expect HICP services to fall from 3.8% in Q4-24 to 3.5% y/y in Q1-25, 3.1% y/y in Q2-25, 2.9% in Q3-25 and 2.7% in Q4-25.

Our assumptions are based on the following backdrop:

1. The timing of Easter is factored into our assumptions. In 2025, Easter will fall on 20 April (later than usual), and we, therefore, expect this to impact seasonal services such as package holidays and airfares, with prices lower in March, higher in April, and lower again in May.
2. We maintain our view that service items most sensitive to price resets will ease significantly, as the Q1-25 reset wave is expected to be smaller than that of 2023-24 (**Figure 24**). We believe that this will be particularly evident in regulated insurance prices (which have been hovering around 8.8% for the last two quarters). In this regard, we have created cost proxies for each of the main insurance price categories (health, transport, dwelling insurance) and find that the catch-up process at the area-wide level is now nearly complete.

FIGURE 24

January reset services basket: m/m % NSA every January



Our January Reset Services Basket groups components for which a high share of total annual price growth happens in January. 20% w in total HICP services.

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

3. We observed further easing in the momentum of other, less volatile services, consistent with the more complete passthrough of past supply shocks and the weakening economic activity.
4. Favorable base effects should support the disinflation process.

ANIMA baseline. For Q4-24 we expect headline/core HICP to be 2.0% and 2.7%, respectively (unchanged from our previous baseline). This keeps our 2024 projections unchanged at an annual average of 2.3% for headline inflation and 2.8% for core. For 2025, we project headline/core HICP at 1.8%/2.4% in Q1-25 (vs 1.9%/2.5% in the previous baseline), 1.8%/2.3% in Q2-25 (unchanged), 1.8%/2.2% in Q3-25 (up from 1.7%/2.2%), and 1.8%/2.2% in Q4-25 (down from 1.9%/2.3%). Our full-year 2025 projection remains at 1.8%/2.3%.

China – Deflationary risks keep intensifying

Headline inflation is set to disappoint in Q4 as China's CPI inflation should slip to 0.3% in Q4 from 0.6% y/y in Q3. Food inflation should be flat in Q4 vis à vis Q3 to 2.9% y/y due to stabilizing fresh vegetable prices. Non-food inflation, on the other hand, should decelerate further during the winter as energy prices are set to ease.

In China, price pressures were very limited in 2024, and will only gradually increase in 2025, after the summer months

PPI inflation in H2 eased as supply remains strong, with downstream sector deflation accounting for nearly 45% of the decline.

Reflation is set to slowly advance next year. Looking ahead, a gradual reflation path is expected, highlighting the need for further demand-side measures to boost confidence and domestic demand.

ANIMA baseline. Against this backdrop, we expect full-year inflation for 2024 to reach 0.3% y/y, same level as in 2023. For 2025 we downgrade our baseline to 0.7% y/y from 0.9% y/y, as downside risks are on the rise. We expect headline inflation to unfold as follows: 0.3% q/q in Q4, 0.3% y/y in Q1-25 and 0.3% in Q2-25.

MONETARY POLICIES

Sailing towards neutrality at different speeds

The faster pace of disinflation in 2024 enabled central banks to initiate expansionary cycles, aiming to make monetary policy less restrictive and ensure continued positive growth.

The Fed and the ECB will continue to cut rates towards the neutral level, but at different speeds, in line with stronger growth expectations in the United States compared to the Eurozone

The ECB initiated rate cuts in June from a 4% deposit rate and ramped up the pace in October, moving from quarterly 25 basis point cuts to cuts at every meeting, mainly due to disappointing growth data.

The Fed opted for an initial 50 basis point cut at the September meeting, followed by a 25 basis point reduction in the November meeting, bringing the Fed funds rate down from a peak of 5.25-5.50% to 4.50-4.75%.

We expect both the Fed and the ECB to continue their rate-cutting cycle in 2025, supported by a further decrease in inflation towards the target levels. Both the Fed and the ECB are likely to move rates towards neutral territory, though at different speeds, reflecting the relatively stronger growth in the United States compared to the Eurozone.

Specifically, in 2025 the Fed will slow its pace, delivering a 25 basis point cut each quarter, bringing the Fed funds rate to 3.25-3.50% by the end of the year, nearing the neutral level.

The ECB, on the other hand, will continue to cut rates by 25 basis points at each meeting during the first half of 2025, bringing the deposit rate to 2% by June 2025 (i.e., at the lower end of the neutral rate estimate range). Due to the sluggish European recovery and the potential acceleration of the downward trend in service inflation, rates could also fall below the neutral level in the second half of the year.

In terms of risks, a divergence can be observed between the two sides of the Atlantic. In the United States, the main risk is that the Fed may ease its tightening more slowly if growth turns out to be stronger than expected and the disinflation process loses momentum. In the Eurozone, the main risk is that an even weaker recovery than expected could lead the ECB to cut rates below the neutral level, especially if service inflation declines at a faster pace than expected.

Federal Reserve – A slowdown in the rate-cutting cycle

The acceleration of the disinflation process in the second quarter of 2024, following a slowdown in the first quarter, and the rebalancing of supply and demand in the labour market has led the Fed to start easing its monetary tightening to facilitate a soft growth landing.

The risk balance, which in the first part of the year favoured the risk of inflation above target, shifted in the second half to being more evenly distributed between the risk of inflation and the risk of higher unemployment.

The Fed will continue to cut rates, but at a slower pace, as the economy remains strong and uncertainty remains high

Against this backdrop, the Fed delivered an initial 50 basis point cut at the September meeting and a second 25 basis point reduction in November, bringing the Fed funds rate to 4.50-4.75%.

However, at the November meeting, Chairman Jerome Powell introduced a note of caution, stating that the future pace of cuts and the final destination are unclear at this time: decisions will be guided by data, particularly those related to the labour market.

In our view, the continued and gradual decline in inflation towards the target will warrant further easing of monetary policy in 2025, but the combination of solid growth, moderately above potential, and the lack of fiscal consolidation will lead to a slowdown in the cutting cycle. This will allow the US central bank to evaluate the impact of its interventions and prevent an excessive easing of financial conditions that could reignite inflationary pressures.

Fiscal consolidation - Economic policy interventions intended to reduce a country's deficit and public debt

In this context, **we expect the Fed to cut rates by 25 basis points at the December meeting** (with the possibility of a pause if economic data exceeds expectations), **before slowing the pace in 2025, cutting by 25 basis points each quarter; with the Fed funds rate nearing neutral level by the end of the year.**

Quantitative Tightening (QT) will be paused in the first part of the year, leaving the stock of Treasury securities on the Fed's balance sheet at a relatively high level.

The main risk to our baseline scenario is that the economic slowdown and the convergence of inflation to the target in 2025 could be slower than expected: in this scenario, the Fed might cut rates at an even slower pace and reconsider the neutral rate level. The fiscal, tariff, and immigration policies implemented by Trump may impact the macroeconomic outlook and monetary policy only from late 2025/early 2026 onwards.

European Central Bank – Moving faster towards neutrality

The ECB is expected to cut rates by 25 basis points at each meeting, reaching the 2% level by June 2025. If the recovery remains weak, monetary easing will continue

The weaker-than-expected recovery in the first half of 2024 and the forecast of inflation reaching the target by 2026 led the ECB to initiate its rate-cutting cycle in June, starting with a 25 basis point reduction. After a second rate cut in September, the ECB adopted a more dovish tone, indicating in the October meeting statement that downside risks to growth could have an impact on the inflation outlook (the only objective of monetary policy in the Eurozone). Against this backdrop, the central bank accelerated the pace of cuts, delivering a third 25 basis point reduction and effectively signalling the possibility of repeating this at every meeting.

We expect that during the December meeting, the growth forecasts will be revised downwards (towards our 2025 estimate of 1% compared to the ECB staff's September estimate of 1.3%) and that the timing for inflation to converge to the target will be brought forward to the first half of 2025. **These revisions will serve as the basis for continuing to cut rates at every meeting: we forecast five 25 basis point reductions between December 2024 and June 2025, bringing the deposit rate to 2%, the lower end of the neutral range in the Eurozone (2-2.5%, according to some ECB members' estimates).**

The risk is that, with growth weaker than expected, this could lead the ECB to cut rates further. The dynamics of service inflation will be crucial, as it remains at high levels for now. We anticipate that the pressure on this component will ease more rapidly in 2025, which could lead the ECB to reduce rates below the neutral level to stop inflation from falling short of the target.

People's Bank of China - We expect further easing next year

PBoC pivoted towards a more forceful easing mode. The PBoC shifted to stronger easing measures, following weak macro data in September. The State Council and PBoC introduced a rate-cutting package to support economic momentum (reduction of the 7-day reverse repo rate, cut of the 1-year MLF rate, cut of the RRR). Mortgage rates were also cut, and policies were adjusted to support housing purchases.

In its Q3 report, the PBOC reiterated its easing stance. The PBOC committed to stronger monetary support and improved policy transmission for the real economy. While reflation remains central to policy, additional fiscal measures to boost consumption may be more impactful.

Further easing ahead. We expect further easing, including a 50bps RRR cut and a 20bps cut to the 7-day reverse repo rate by year-end, as the PBoC aligns with the MOF's fiscal stimulus to drive economic recovery. Furthermore, we expect the CB to enhance competition among financial institutions for smoother rate transmission. For 2025, we expect further easing with two 25bp RRR cuts in Q1/Q3 and two 20bp policy rate cuts in Q2/Q4

AnimaResearch

Bond markets

GOVERNMENT BONDS (DEVELOPED COUNTRIES)

Moderately optimistic

After a very positive fourth quarter of 2023 for bonds from developed countries, the performance in 2024 has been rather disappointing.

The performance of bonds in developed countries in 2024 was quite underwhelming, driven by robust US growth and fears of a deceleration in the disinflation process with Trump in office

Specifically, as of 15 November 2024, Treasury bonds have gained 0.7% year-to-date, Bunds have risen by 0.2%, and BTPs have appreciated by nearly 4.7%.

In the United States, growth remained solid, and inflation only began to decline convincingly in the second quarter, causing concerns among investors and the Fed about the neutral level of interest rates, which might be much higher than in previous periods. The rebalancing of supply and demand in the labour market has nevertheless led the central bank to begin the expansionary cycle in September, with the aim of preserving positive growth, albeit slowing. In this context of economic resilience and accommodative monetary policy, Trump's victory in the elections had a negative impact on Treasury performance.

In the Eurozone, although the recovery has been sluggish, persistent core inflation, particularly in services, coupled with a strong correlation to Treasuries, has hindered Bunds from achieving a solid performance.

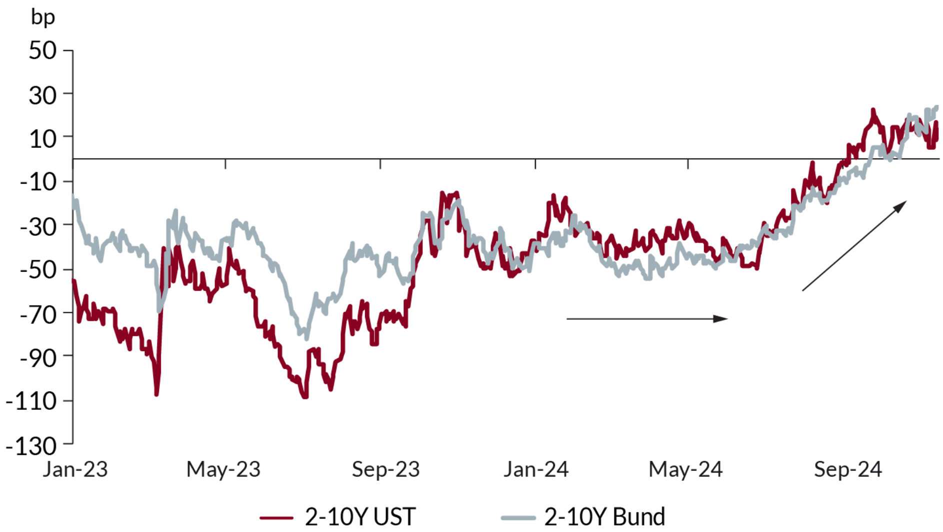
In this context, the main bond market trends in the US and the Eurozone during 2024 have been as follows:

1. Up until April-May, yields increased across all maturities on both sides of the Atlantic, with the curves firmly inverted. Higher-than-expected inflation data in the United States, along with positive economic surprises, contributed to a revision of monetary policy outlooks, putting pressure on government sectors.
2. From the end of May to September, yields began to decline. Short-term maturities outperformed, contributing to a steepening of the curves, with the 2/10-year spreads on both US and German government bonds turning positive again for the first time since the second half of 2022. The movement was driven by a significant downward revision of monetary easing expectations in both regions, following weak economic data and the restart of the disinflation process in the US (**Figure 25**).

Government yield curves in the USA and the Eurozone steepened significantly from May onwards

FIGURE 25

2-10 year spread on the UST and Bund curves



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

3. Since the end of September, the curves have continued to steepen, albeit in a rising interest rate environment. On the one hand, economic surprises have largely been positive, while on the other, markets have started to price in a greater chance of a Trump victory, leading to an increase in the term premium and placing pressure on longer maturities.
4. Nominal yield trends have primarily been driven by the real yield component, reflecting the importance of growth data and expectations around monetary policies in driving government bond performance. The breakeven rates have moved within a narrower range, indicating that inflation expectations stay well aligned with the targets (**Figure 26 and 27**).
5. The Treasury-Bund spread has followed a somewhat erratic path, although the correlation remained very high for most of the year. Until mid-April, Bunds outperformed Treasuries; from mid-April to mid-September, the gap narrowed, while since mid-September, markets have priced in stronger US economic performance and a more dovish ECB stance.

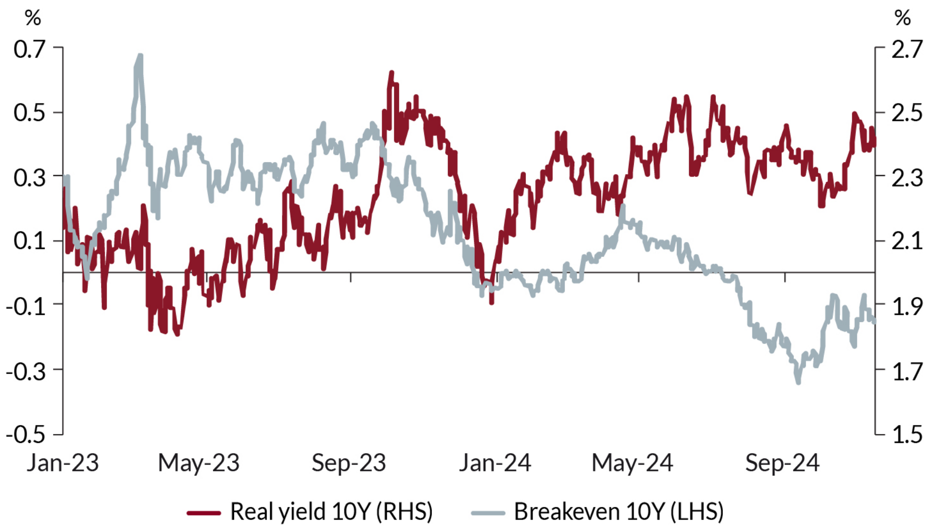
FIGURE 26

Treasury curve: 10-year real yields and breakeven

Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

FIGURE 27

Bund curve: 10-year real yields and breakeven



Data as of 15 November 2024 Source: Haver Analytics, ANIMA Research

Following a year of overall disappointing performance, **the government bond segment is expected to experience more favourable trends in 2025:**

1. According to our baseline projection, US growth is expected to slow moderately, while remaining slightly above potential. As inflation progresses toward the target, it will allow the Fed to ease monetary policy further toward the neutral level. In this context, we do not anticipate a significant decline in yields from current levels, although Treasuries will remain attractive due to an improved risk-return profile compared to the past and appealing income prospects over the medium to long term. **Risks are balanced.** On one hand, investors might price in higher inflation risks due to Trump's policies on tariffs and immigration (as the deficit is unlikely to rise in 2025); on the other hand, the potential for a global tariff war could fuel concerns about global growth.
2. Growth in Europe will moderately pick up, although it will remain below potential, with inflation progressively declining towards the target. The ECB is set to bring interest rates back to the neutral level (2%), but could push them below this threshold if growth disappoints or the disinflationary process accelerates. In this scenario, we expect a decline in Bund yields from current levels, with the largest decline expected in the first half of the year. **Once again, risks are balanced.** While an aggressive tariff policy towards Europe could lead the ECB to take a more accommodative stance, favouring government sectors, the new German government might introduce a large fiscal stimulus, which would negatively affect Bund performance.
3. **We hold a more positive outlook on Bunds compared to Treasuries, particularly during the first half of the year.** This assessment reflects a less optimistic outlook for European growth compared to the US, a monetary policy that, despite rate cuts, remains more restrictive in the Eurozone than in the US (due to the fact that Quantitative Tightening the ECB's quantitative tightening will continue, while the Fed's will end in the first quarter of 2025), and a fiscal policy that, for now, remains relatively more restrictive in the Eurozone.
4. **We expect 2025 to be marked by significant uncertainty regarding macroeconomic policies in both the US and the Eurozone, which will result in high volatility in the government bond sector.**

In 2025, government bonds are expected to deliver positive performance, outperforming their 2024 results. We hold a more positive outlook on Bunds compared to Treasuries during the first half of the year

Quantitative Tightening - A monetary policy instrument designed to systematically and deliberately reduce the money supply (such as by not reinvesting repayments or by selling securities held by the central bank)

In 2024, Italian government bonds delivered a moderately positive performance, thanks to the narrowing of the credit spread compared to other Eurozone government bonds, particularly those of core countries. The reduction in the risk premium was driven by a combination of supporting factors: 1) a decrease in the macro performance differential between peripheral and core countries; 2) the increase in Italy's potential growth due to the PNRR investments; 3) the continued strength of retail investor demand and an acceleration of foreign investor inflows; 4) a fiscal adjustment outlook that remains sustainable and credible for investors; 5) the strong performance of all risky assets.

The ongoing presence of the favourable idiosyncratic factors that emerged in 2024, combined with a dovish ECB, should create a constructive outlook for BTPs

We foresee that in 2025, an accommodative ECB and the ongoing positive idiosyncratic factors from 2024 will continue to support BTPs, leading to another moderately positive performance.

The main risks for the outlined scenario are: 1) a decline in market sentiment towards risky assets; 2) an increase in idiosyncratic risks, for example, due to much lower-than-expected growth that hampers fiscal adjustment; 3) a decline in demand for Italian debt, particularly from foreign investors, due to the continued large-scale issuance program.

GOVERNMENT BONDS (EMERGING MARKETS)

Uncertainty surrounds 2025

By the end of 2024, two major global factors that have significantly influenced the one-sided movement in emerging markets, namely the inflation shock and the coordinated interest rate hikes by central banks, might have been dealt with. In 2025, global growth is expected to decelerate slightly from the 3.2% forecast for 2024 to just under 3%, with emerging markets also slowing down from 4.4% to 4.0%; the inflation rate is projected to halve from 8.2% to around 4%. In relative terms, the Asian region appears to be better positioned than Latin America, where the growth/inflation mix is more unfavourable.

In the first half of the year, trends in the sector will primarily be driven by two factors: the shifting growth/inflation dynamics in the US and Trump's trade policy, which is likely to cause turmoil and support the dollar.

__The macroeconomic outlook and US economic policies will play a pivotal role in shaping the future of emerging markets__

As for the first factor, while we expect a moderation of US growth and inflation in 2025, it is also important to consider that domestic risks to price levels are tilted upwards due to Trump's promised immigration restrictions during his campaign. Regarding the second factor, the real risk for emerging markets is that a widespread increase in tariffs could undermine local growth prospects and force their central banks to take unexpected actions (either to protect the currency or to support growth). Although it is too early to identify clear winners and losers, **it is reasonable to expect that 2025 will be a less homogeneous year for the emerging market sector, with opportunities and risks appearing at different times and in varied ways.**

Among the key downside risks that need to be monitored, we highlight the actual implementation and impact of the tariffs proposed by Trump, the potential escalation of worries about the sustainability of US public debt, and the risk of a recession or an unexpected rise in inflation in the United States.

EURO INVESTMENT GRADE CORPORATE BONDS

Still a favourable environment, but with tight risk premia

2024 was a very positive year for the credit market. From one perspective, macroeconomic and monetary policy dynamics have aligned almost perfectly, with the sluggish recovery of the European economy and the consolidation of the disinflationary process paving the way for a monetary easing. On the other hand, the technical environment has proved extremely favourable: the sector has seen record subscription inflows, with investors keen to lock in historically high yields to maturity, effectively replacing the ECB as a price-insensitive buyer. The tightening of risk premia over government bonds (around 40 basis points for the ICE BofA Euro Corporate Index in terms of Option Adjusted Spread, OAS) was concentrated in the first and fourth quarters. However, volatility remained low throughout the year, with a spread range narrower tnan 50 basis points, less than half the 20-year average. The generally high risk appetite that characterised financial markets for much of the year is clearly reflected in the performance of indices representing various rating categories: the sectors with a greater exposure to credit risk saw the most significant spread tightening and delivered by far the strongest returns, driven by higher carry and shorter duration (compared to the beginning of the year, German government bond yields fell on shorter maturities but rose on medium- and longer-term ones). (Table 3).

Carry - The return provided by a bond assuming no changes in the overall interest rate levels and risk premia

TABLE 3

Year-to-date performance of Euro Corporate Bonds

	Investment Grade	AAA	AA	A	BBB	High Yield	BB	B	CCC & lower
Current spread vs Govt (OAS), bp	**98**	**57**	**66**	**89**	**112**	**318**	**206**	**356**	**1369**
OAS - YTD Change, bp	***-37***	*-13*	*-28*	*-31*	*-46*	***-77***	*-80*	*-95*	*-439*
OAS – 10Y Average, bp	***123***	*66*	*76*	*104*	*149*	***403***	*299*	*526*	*1174*
Yield to maturity (YTM) %	**3.3**	**2.8**	**2.8**	**3.2**	**3.4**	**6.0**	**4.7**	**6.2**	**18.0**
YTM - 10Y Average, %	***1.7***	*1.2*	*1.1*	*1.4*	*2.0*	***4.8***	*3.7*	*6.0*	*12.9*
Performance YTD	**4.3%**	**2.6%**	**3.2%**	**3.8%**	**4.9%**	**7.8%**	**7.5%**	**7.2%**	**10.9%**

Data as of 15 November 2024 Source: ICE BofA ML, Bloomberg, ANIMA Research.

The macroeconomic and monetary policy trends, along with fundamental and technical factors, should continue to support investment-grade corporates, but risk premia are very low

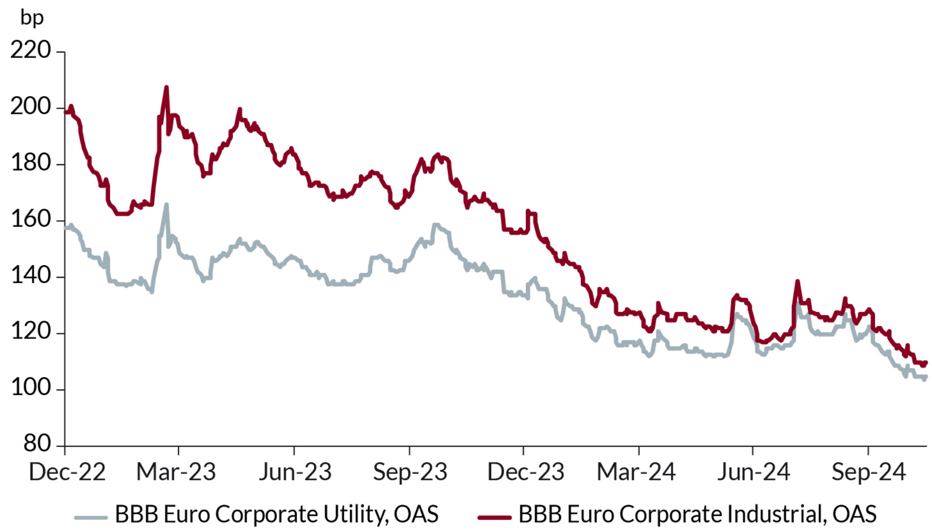
Many of the factors that supported the sector in 2024 will continue to do so into 2025. According to our baseline scenario, growth in the Eurozone will see a modest acceleration, while the US will experience a slight loss of momentum. Price pressures will continue to ease, and rate-cutting cycles will extend, with the European deposit rate expected to reach 2% by June. Corporate fundamentals remain broadly solid: net leverage metrics remain around the 10-year midpoint, despite marked sector disparities, and the balance between positive and negative rating changes show a clear bias towards upgrades. A supportive technical backdrop is likely to persist as well: yields, which remain historically high, will continue to attract investors, and lower short-term rates might prompt a rotation from money markets to bonds. At the same time, net issuance is expected to stay modest, as political and commercial uncertainty may dampen investment and companies' inorganic growth.

However, valuations have reached tight levels: in the Eurozone, the spread over government bonds for the ICE BofA Euro Corporate Index has fallen below 100 basis points, not far from the post-Great Financial Crisis lows, which were recorded around 80 basis points during periods when the ECB was engaged in aggressive bond-buying programmes. The situation is even more extreme in the United States, where the spread of the ICE BofA US Corporate Index over government bonds has recently hit its lowest level since the turn of the century, at 77 basis points. Given these levels, **the potential for further tightening is very limited, and the risks associated with a worsening of the market outlook seem inadequately priced in.** These risks, however, have significantly increased following Donald Trump’s win in the US presidential election: although the most likely scenario is an increase in tariffs against Europe – albeit delayed, gradual, and limited to a small number of goods – it cannot be ruled out that even just the uncertainty or the adoption of a hardline negotiating approach could trigger a deterioration in sentiment, if not in the macroeconomic outlook itself. In 2018, the global trade war and the loss of growth momentum in the Eurozone and China, coupled with monetary tightening, created a very challenging environment for financial markets and led to a significant widening of spreads.

In this environment, **while remaining invested, we pay close attention to downside risks and focus on market segments where valuations appear more attractive or where risk premia are less tight.** Specifically, we **overweight defensive/non-cyclical sectors**, such as utilities, telecoms, and pharmaceuticals. A number of European cyclical sectors are grappling with major structural challenges – such as the automotive industry facing Chinese competition, the threat of US tariffs, hyper-strict environmental regulations, high energy costs, excess production capacity and workforce, margin and profit pressures, and a potential wave of downgrades. Nonetheless, they are scarcely yielding a premium compared to non-cyclical sectors (**Figure 28**).

FIGURE 28

Euro Corporate Bonds, Utilities and Industrial Sectors – Spread vs Government Bonds



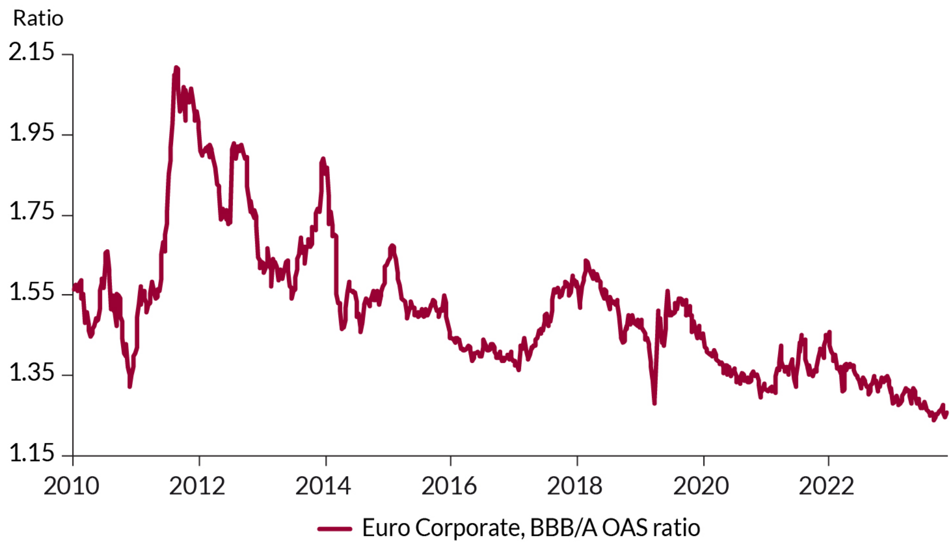
Data as of 15 November 2024 Source: ICE BofA ML, Bloomberg, ANIMA Research.

In addition, with a flat government yield curve and credit spreads largely unchanged across maturities, **we favour the short and intermediate segments (bonds up to 6-7 years)**, which offer greater visibility on earnings dynamics and are less exposed to potential repricing of the term premium, triggered by concerns over the sustainability of fiscal policies. Lastly, **we continue to favour the investment-grade sector over high-yield and generally favour up-in-quality strategies;** speculative segments appear more vulnerable to a widening of risk premia if the macroeconomic or technical outlook deteriorates, and the credit curve is very flat: the spread between BBB and A-rated sectors has reached its lowest level since the Lehman bankruptcy (**Figure 29**).

We favour market segments where risks are better rewarded, such as non-cyclical sectors, short/medium maturities, and high-quality credit

FIGURE 29

Euro Corporate Bonds, BBB and A Sectors - Spread vs Government Bonds Ratio



Data as of 15 November 2024 Source: ICE BofA ML, Bloomberg, ANIMA Research.

EURO HIGH YIELD CORPORATE BONDS

Tactical and selective approach

Euro high-yield credit market is set to close another exceptionally strong year. **Returns have been very strong, both in absolute and relative terms, especially when adjusted for risk**: the outperformance was not limited to government bonds alone, but extended to many continental equity indices, and it was achieved with relatively low volatility, despite significant fluctuations in risk-free rates and the escalation of idiosyncratic risk.

The asset class has been primarily supported by the resilience of the macro/fundamental backdrop, with the sluggish European recovery balanced by the dynamism of the US economy and the strength of corporate balance sheets, although in a context of significant divergence between the higher-credit-rated segments and the more speculative sector: CCC-rated bonds have, on average, experienced a significant deterioration in leverage and financial coverage indicators, alongside five consecutive quarters of net downgrades. The technical outlook also played a key role: a significant increase in supply, compared to the limited volumes of the previous two years, was largely absorbed by very strong demand, largely justified by the attractiveness of the absolute yield levels.

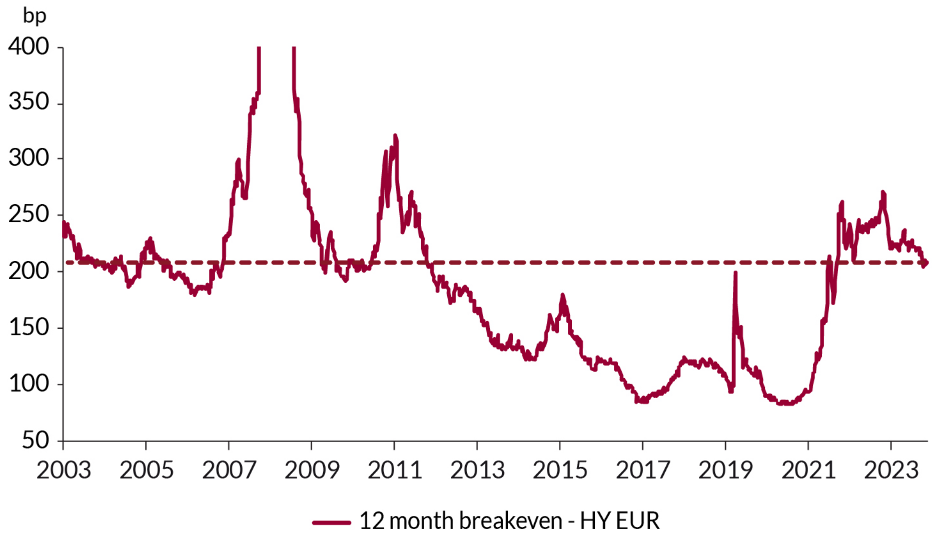
Idiosyncratic risk - (or specific) Risk that pertains solely to a specific financial asset

The long-lasting benefits from these factors may continue into the first part of 2025: despite the decrease in rates and spreads, the yield to maturity, at nearly 6%, is still far above the levels observed for most of the past decade, and it allows for substantial capital losses to be absorbed. With a duration slightly over three years, the 12-month breakeven (the interest rate change that results in a capital loss equal to the carry) stands at 210 basis points, down from the October 2023 highs, but still close to the highest levels recorded outside of systemic crisis periods (**Figure 30**).

High carry and short duration may continue to attract investor interest, but valuations are rich, macroeconomic uncertainty is high, and the technical environment is expected to weaken

FIGURE 30

Euro High Yield – 12-Month Breakeven Rate



Data as of 15 November 2024 Source: ICE BofA ML, Bloomberg, ANIMA Research.

Nevertheless, the massive tightening of credit spreads which has taken place since the fourth quarter of 2022 led to rich valuations: the current level of spreads is lower than long-term averages and has historically been sustainable only for relatively brief periods, with the exceptions of 2017-2018 and 2021. In the US, the spread vs. Govt of the ICE BofA US High Yield Index has even narrowed to just 20 basis points from the historical lows recorded in June 2007, shortly before the early signs of what would later become the Global Financial Crisis (**Figure 31**).

FIGURE 31

Euro and US High Yield – Historical Spread vs. Government Bonds

Data as of 15 November 2024 Source: ICE BofA ML, Bloomberg, ANIMA Research.

Despite significant improvements in the euro high-yield sector in terms of average credit quality and liquidity over the years, and a recent reduction in interest rate risk exposure, **these spread levels are unlikely to be sustained as the year unfolds,** considering the various macro challenges and the deterioration of the technical environment. The net issuance of securities is expected to rise, driven by the need to refinance maturing debt and an increase in capex, M&A activity, and dividend recap activities, following the stagnation triggered by the significant rate hikes of the past two years.

In this context, **2025 is shaping up to be a year where opportunities for value extraction in the sector will be primarily driven by carry accumulation rather than capital appreciation, making it vital to focus on issuer selection** through a strong bottom-up analysis. The current allocation reflects relative preference for the single-B sector, with overweight positions in the financial sector (favouring high-quality names) and real estate, while underweighting automotive and auto components, packaging, and gaming.

Although total return prospects appear encouraging, the high level of uncertainty regarding economic policies, both in the United States and in Europe, and the compression of risk premia, suggests that a **tactical approach and careful monitoring of downside risks** are necessary: key concerns include the potential deterioration of sentiment regarding global growth, driven by the development of a global trade war, as well as possible rising concerns over inflation and interest rate dynamics in the United States, in addition to idiosyncratic risks (according to analysts' estimates, the default rate in the Eurozone will peak in 2025).

The approach is tactical and selective; we carefully monitor risks

AnimaResearch

Equity markets

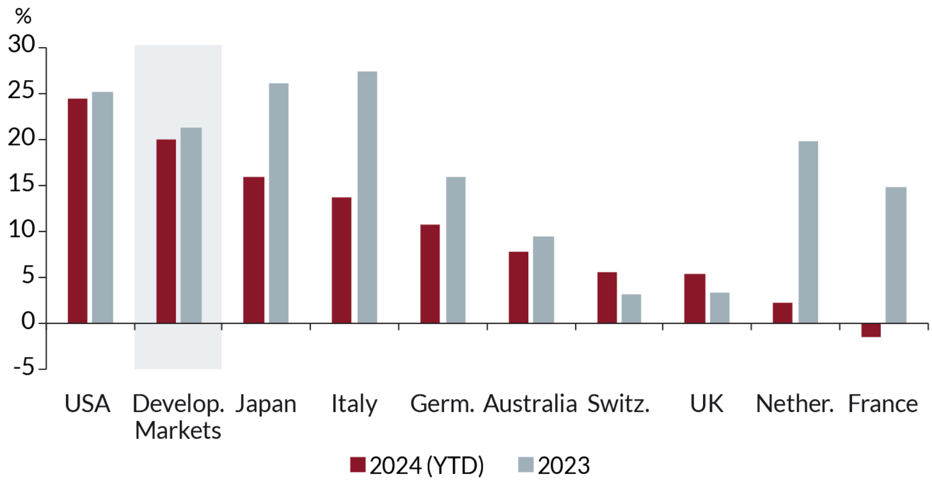
EQUITY DEVELOPED COUNTRIES

Opportunities between resilient growth and supportive policy

Following a strong 2023 for almost all major equity markets, **the indices are continuing to show strength in 2024. In particular, Italy has stood out so far as one of the best-performing markets,** having recorded the highest performance in 2023, even surpassing that of the US index (**Figure 32**).

FIGURE 32

Developed markets performance in 2023 and 2024



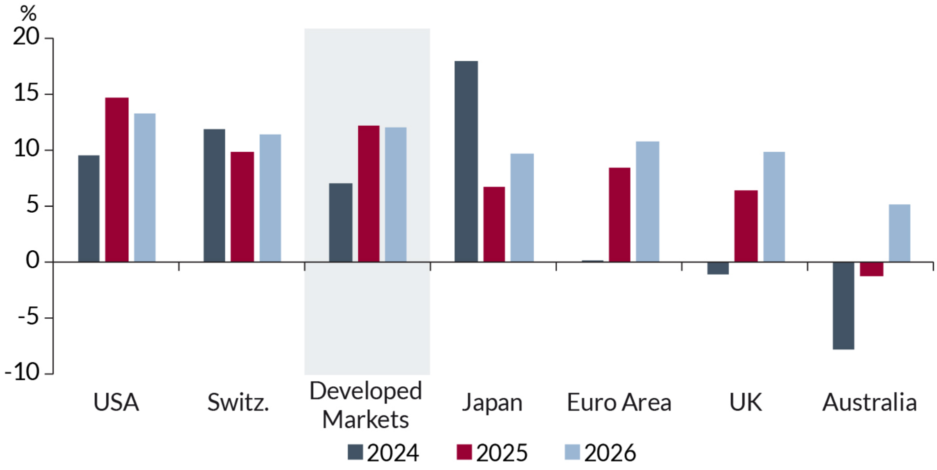
Data as of 15 November 2024. Source: MSCI, ANIMA Research

In 2025, equity markets will be supported by profit growth and a modest increase in multiples

From a forward-looking perspective, **we maintain a positive outlook on the equity markets, which we expect to be supported by both earnings growth and the increase in multiples.** From a macroeconomic perspective, the resilience of the US economy, backed by sustained consumer spending, suggests that the United States may continue to grow and avoid a recession in 2025. At the micro level, this scenario is expected to translate into an aggregate corporate earnings growth of over 10%. Our estimate is broadly in line with analysts' forecasts, who anticipate a 12% earnings growth in developed countries for both 2025 and 2026 (**Figure 33**). Furthermore, Trump's victory is likely to help sustain high growth expectations for the economy and corporate earnings, due to his agenda focused on tax cuts and policies aimed at stimulating investment and boosting domestic demand.

FIGURE 33

Expected earnings growth for 2024, 2025 and 2026



Data as of 15 November 2024 Source: MSCI, IBES, ANIMA Research

The high earnings growth estimates will have a positive impact on equity valuations, thanks in part to the central banks' easing of monetary tightening. Even though the multiples are high compared to historical averages, we believe that the combination of strong growth expectations and falling interest rates will help sustain further, albeit modest, expansion. The global index's price-to-earnings ratio, for example, is trading at 18.7 times the estimated 12-month earnings, and we believe there is room for further, moderate re-rating (Figure 34). In this context, **the outlook for global equity markets remains positive for 2025**; with any corrections viewed as buying opportunities.

FIGURE 34

Price/Earnings Ratio for the Global Index*

** 12-month earnings per share forecast based on consensus estimates*

Data as of 15 November 2024 Source: MSCI, IBES, ANIMA Research.

Considering the positive outlook, we suggest an allocation towards the Quality and Growth sectors, even though the macroeconomic context is somewhat better than anticipated and a greater probability of a Chinese economic recovery. These sectors, in fact, are among the top beneficiaries of an environment characterised by positive growth prospects and lower interest rates.

With regard to investment themes supported by structural trends, **we maintain a significant, albeit selective, exposure to technology, with a specific focus on artificial intelligence**, which is forecasted to experience strong growth in the coming years and positively affect the productivity of a growing number of industries. **On the other hand, we take a more cautious stance on ESG themes, particularly those related to sustainability**, as Donald Trump's second term in office is likely to favour more traditional sectors, particularly within the energy and environmental industries.

Geographically, we continue to favour the United States over other developed countries, owing to its relatively stronger macroeconomic outlook.

The key risks to this scenario include a potential shift in the Fed's stance, which could take a less accommodative approach in response to an acceleration in inflation, and a possible slowdown in U.S. growth, with negative repercussions on the global economy and corporate earnings dynamics. The risk of an escalation in geopolitical tensions persists, although with Trump's victory, this could subside throughout 2025. Furthermore, customs duties and tariffs could harm the profitability of companies, particularly in sectors exposed to international trade. At the sector level, if Big Tech were to fall short of analysts' expectations, this could result in the burst of what is commonly called the "AI bubble," leading to market destabilisation and a downward adjustment of equity valuations in the tech sectors.

We favour the United States over other global markets, with a sector allocation that leans towards Quality and Growth sectors

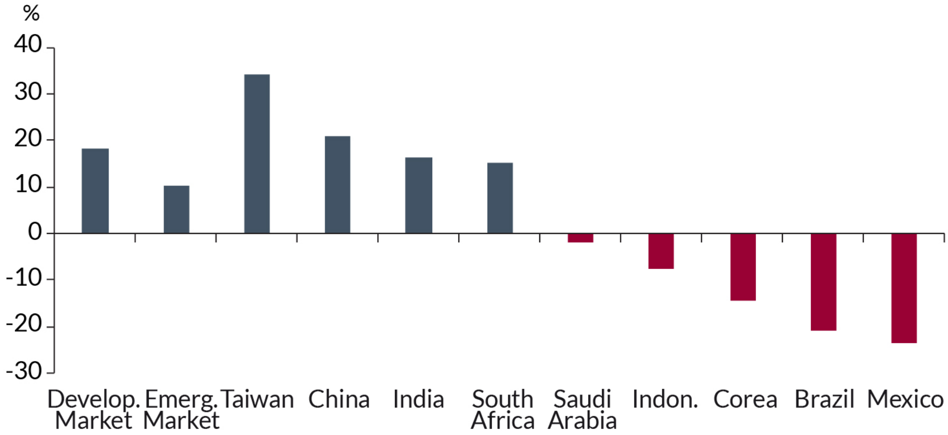
EQUITY (EMERGING MARKETS)

Awaiting further signals from China

In 2024, emerging markets continued to underperform developed countries, continuing a long-standing negative trend that began in 2010. China, which accounts for nearly a third of the emerging market index, weighed down its performance for most of the year, before experiencing a significant rebound from September after the Chinese government unveiled stimulus measures (**Figure 35**).

FIGURE 35

Emerging Markets Performance in 2024



Data as of 15 November 2024 Source: MSCI, ANIMA Research.

For now, we believe it is prudent to wait for further guidance from Chinese government authorities on the size and timing of the stimulus package.

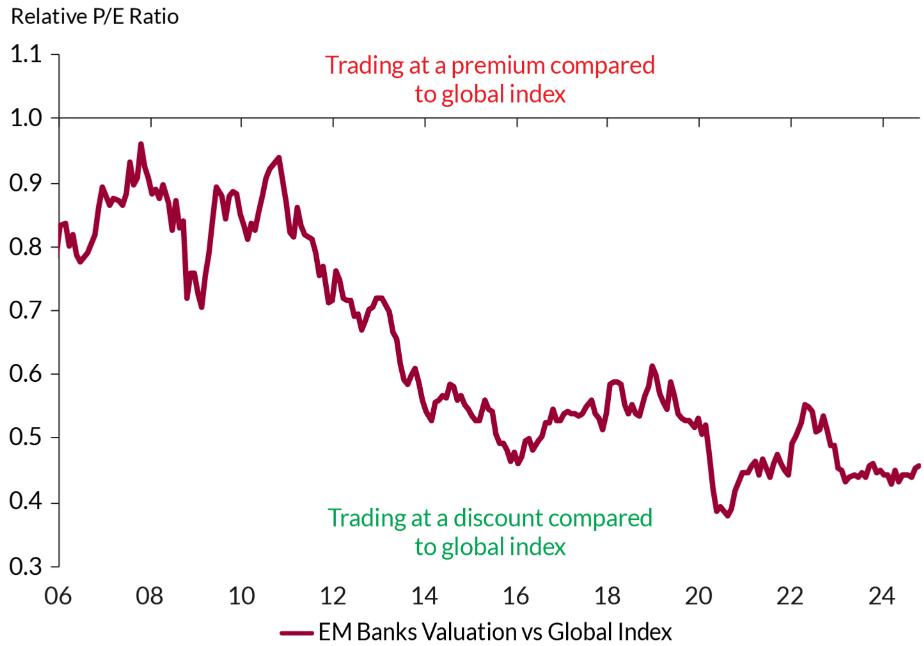
The outlook for emerging markets will depend on the stimulus measures approved by the authorities

In fact, more clarity is needed regarding the further actions that will be taken to stimulate the Chinese economy and to offset the likely appreciation of the dollar resulting from the implementation of Trump's policies.

In terms of sector allocation, we recommend maintaining a balanced approach, progressively increasing exposure to sectors that are likely to benefit directly from the announced measures and that trade at attractive valuations, such as the banking sector (**Figure 36**).

FIGURE 36

Emerging Markets Banking Sector - Relative Valuation compared to Global Index



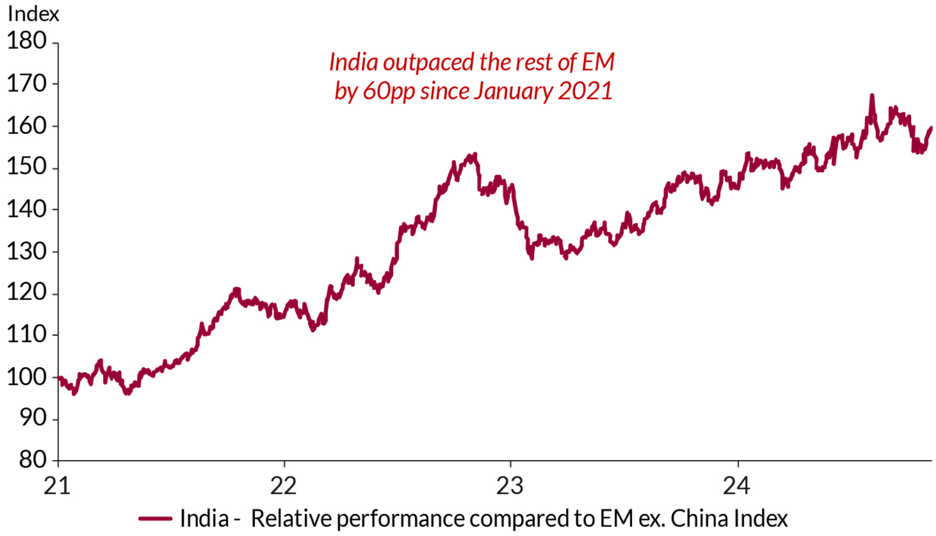
Data as of 15 November 2024 Source: MSCI, ANIMA Research.

Regionally, we favour Asia due to its exposure to the technology sector and the potential rebound of China. Within the Asian region, we are overweight on India, which has evolved from merely being China's rival to a long-term story of structural growth (**Figure 37**). We maintain a negative outlook on Mexico because of the risks associated with political and institutional stability, as well as potential revisions of trade agreements with the United States.

Among the main risks to point out for the sector's outlook, we highlight the effectiveness of the Chinese economic stimulus, which might not be enough to revive the world's second-largest economy, and the potential appreciation of the dollar, should the Fed adopt a more hawkish policy. In addition, the risk posed by the tariffs announced by Trump during his election campaign weighs on China and the emerging markets, potentially hindering China's recovery further. Lastly, geopolitical developments must also be monitored: an escalation of tensions between China and Taiwan could have negative repercussions not only on the emerging markets but also globally.

FIGURE 37

India – Relative Performance compared to EM ex. China Index



Data as of 15 November 2024 Source: MSCI, ANIMA Research.

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Currency markets

Shifts in equilibrium expected for 2025

Dollar – Still strong

In the first half of the year, the dollar will be supported by Trump's policies, but will lose momentum as growth weakens thereafter

Throughout the summer, the dollar declined, coinciding with the Fed's change in policy on 18 September, when the central bank surprised the market by initiating the cycle of cuts with a more aggressive move than expected. However, as the US elections approached, the disparity between macroeconomic data – still strong in the United States and weaker than expected in Europe – led to a reversal in the euro-dollar exchange rate, with the euro starting to lose ground again. **After Donald Trump's electoral victory, which also saw him take control of Congress, the dollar's appreciation trend strengthened and may persist** beyond his swearing-in. Therefore, we maintain a long position on the dollar.

In 2025, the expected slowdown of the US economy should continue to act as a latent drag on the dollar, which we anticipate will end the year at a lower level than at the end of 2024. **Nevertheless, in the first half of the year, the US dollar will be sustained by Trump's aggressive policies and the introduction of tariffs on China and Europe.** In addition, the Euro's weaknesses will be more evident in the first half of the year, both economically (Eurozone inflation could decelerate more than anticipated after winter) and politically, with elections in Germany, an unstable government in France, and the ongoing issue of the war in Ukraine taking centre stage again.

In this context, the target exchange rate for the euro-dollar at the end of 2025 is set at 1.14. The forecast will need to be revised downwards if the US economy proves strong enough to trigger a revision of the Fed's expected monetary loosening.

The Bank of Japan should continue to raise interest rates

The normalisation of Japan's monetary policy may drive an appreciation of the yen, becoming more noticeable from early summer

The yen has fallen by 10% against the dollar since the beginning of the year, weighed down by the Fed's wait-and-see approach and the Bank of Japan's sluggish response. In fact, the Bank of Japan began normalising monetary policy by removing negative interest rates later than expected and at a slower pace, due to insufficient evidence of a domestic inflation uptrend.

Looking forward, we expect this evidence to materialise according to the central bank's projections, Japanese inflation will stabilise at 1.9% in 2025 (matching 2024 levels) and rise to 2.1% in 2026. Consequently, we anticipate that the BoJ will return interest rates to neutral territory over the year, with three 25 basis point hikes, resulting in a benchmark rate of 1.0% by the end of 2025. As a result, the yen should continue its gradual appreciation against the dollar, likely becoming more noticeable from early summer, following a first half of the year where the strength of the dollar will remain a factor.

In this context, the target exchange rate for USD/JPY at the end of 2025 is set at 130. Should the US economy be stronger than anticipated, or if Japanese inflation does not rise enough to stabilise at 2%, this scenario will have to be reassessed.

Pound– A decoupling between the dollar and the pound is on the horizon

The pound has had a rather uneventful year: the exchange rate with the dollar, remains near the levels at the close of 2024, in the 1.27 range. Furthermore, the Bank of England kept interest rates unchanged throughout the first half of the year, initiating a cycle of cuts in July and making a second intervention in November; overall, the tightening was eased by 50 basis points, compared to 75 by the Fed and ECB.

The macroeconomic environment in the UK remains dynamic, with growth revised upwards for this year and expected to slightly accelerate in 2025, while labour market conditions are becoming less tight, although demand-side imbalances remain. Considering the gradual and steady decline in inflation, we believe that **in 2025, the Bank of England will proceed with caution in cutting interest rates**, ensuring room for manoeuvre in a rapidly evolving global context. **This will help support the pound**, both against the dollar and the euro.

As a result, we revise the GBP/USD target upwards to 1.35 in 2025, driven by the macroeconomic divergence between the United States and the UK, along with the Bank of England's more cautious approach to easing monetary tightening. If the US economy remains stronger than expected, hindering a widespread weakening of the dollar, this outlook will have to be reassessed.

Strategic market outlook

EQUITIES (DEVELOPED COUNTRIES)		The outlook for global equity markets in 2025 remains positive, driven by the resilience of economic growth. Specifically, the strength of the US economy, underpinned by strong consumer spending, is expected to drive solid corporate earnings growth, with positive effects on valuations, further supported by monetary easing.
EQUITIES (EMERGING MARKETS)		Regarding emerging markets, we believe waiting for further guidance from Chinese government authorities on the size and timing of the stimulus package is appropriate. Furthermore, a potential appreciation of the dollar driven by Trump's policies could negatively impact emerging markets.
GOVERNMENT BONDS (DEVELOPED CONTRIES)		After an overall disappointing 2024, we are moderately optimistic on bond markets for 2025 and expect positive returns. In the United States, historically high yields will be the main driver of income. In the Eurozone, growth still below potential could lead to a decrease in interest rates from current levels, mainly in the first half of the year.
GOVERNMENT BONDS (EMERGING MARKETS)		The absorption of the inflation shock, along with the end of central banks' tightening cycles are supportive for the asset class in 2025. However, Trump's election and the potential strengthening of the dollar represent two significant sources of uncertainty. We favour a cautious approach.
EURO INVESTMENT GRADE CORPORATE BONDS		Macro and monetary policy trends, the fundamental environment and technical aspects remain positive, however, valuations are rich. Therefore, we favour market segments where risks are better rewarded, such as non-cyclical sectors, short/medium maturities, and high-quality credit.
EURO HIGH YIELD CORPORATE BONDS		Income prospects remain encouraging in absolute terms, but the high level of uncertainty regarding economic policies and the narrowing of risk premia suggest maintaining a tactical and selective approach, along with close monitoring of downside risks.
CURRENCIES	 **Dollar**  **Yen**  **Sterling**	The dollar could take centre stage in 2025: Trump's presidency will trigger new trade wars, which could weaken other currencies. We maintain a positive outlook on the yen for the second part of the year, as the BoJ likely to continue raising rates, while taking a more cautious stance in the first half. Finally, we adopt a moderately positive outlook on the pound in relative terms, given the BoE's cautious stance on cutting rates; we favour EUR/GBP over GBP/USD.

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