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ANALYSIS

Pivotal Moment

VANTAGE POINT

Q2 2024

ANALYSIS

BNY MELLON

INTRODUCTION

Welcome to another edition of Vantage Point, the quarterly global economic and market outlook from the Global Economics and Investment Analysis (GEIA) team at BNY Mellon Advisors.

We have reached a point where the key fear gripping markets in the past couple of years – inflation – has receded, but not disappeared. Instead, markets are looking forward to a year of reasonable global growth, with falling inflation and lower interest rates. Add to that excitement about the potential of Artificial Intelligence (AI) and you get three months in which equities have done very well, even though interest rates remain high. This narrative has been particularly influential in the US, but there is growing evidence that the worst of the European and UK downturns is behind us, while China stimulus appears to be limiting much further downside risk in that economy. In addition, Japan looks to have a reasonable chance of escaping the deflationary mindset that has held it back for more than 25 years, while emerging markets have benefited from looser global financial conditions and, in some cases, a degree of 'friend-shoring'.

So far, so good then and it increasingly looks like some of last year's fears were overdone. Remember, we along with many others, assumed that the post-COVID inflation shock was deeply embedded and that central banks, having been late to recognize this, would have to create a lot of economic slack to get inflation back down to target sustainably. The equity market's progress has largely been founded on the view that this analysis was wrong: that most of the inflation spike was driven by supply disruption and that it would trend back towards target naturally as these supply shocks dissipate, allowing interest rates to fall rapidly. That view was particularly prevalent during the 'everything rally' of late Q4/early Q1 and has been wound back a little since then, but the optimism remains intact in most risk markets.

Were we wrong then, to be pessimistic about central banks' ability to bring inflation back to target without triggering a recession? Well, not in Europe and the UK, where that seems to be exactly what happened – both economies stagnating during the second half of 2023. But that's not what happened in the US, and what happens to the US matters most to global markets.

With the benefit of hindsight, we can identify three factors that enabled the US to outperform. First, US consumers behaved much more like their textbook counterparts than Europeans: faced with a shock to real incomes they 'smoothed' their consumption by dipping into 'excess' savings built up during the pandemic. Second, the international terms of trade behaved very differently in the US, compared with Europe. The latter is a large energy importer, whereas the US is a

net exporter, so a large rise in energy prices had very different and opposing effects on the economy. Third, fiscal policy was loosened dramatically in the US in 2023, whereas it tightened modestly in Europe.

We believe these three factors account for much of the divergence between US and European economic performance in 2023. But they are unlikely to be repeated in 2024, so we may well see a period of gentle European revival just as the US economy slows. If China delivers reasonable growth of around or even a bit less than 5%, then the world economy may well experience the modest but solid growth markets appear to be pricing in. And if aggregate demand grows modestly, alongside manufacturing-led stimulus in China, then it may well be that economic slack opens a bit more and sufficiently to elicit further goods price disinflation and bring core inflation down. And if that happens, then we should see the 3-4 interest rate cuts the markets appear to be expecting now. And all of that would validate market expectations as they currently are, meaning a degree of progress for equities even as fixed income continues to deliver a reasonable income return. That also describes well our single-most-likely economic scenario: **Muddle Through**, to which we assign a **50%** probability.

Risks abound however, to the upside and the downside. We have an optimistic scenario (**New Economy, 30%**) – in which AI starts to deliver on its macroeconomic promise sooner than expected. By boosting productivity and aggregate supply, in this world growth is higher in the major economies, notably the US, and inflation is lower, allowing interest rates to come down more quickly than current pricing. Moreover, as productivity growth starts to spread wider than the tech sector itself, equity market performance widens beyond the big tech companies too, with early AI adopters in key services looking set to benefit first. Ultimately, we think the fruits of AI will largely accrue to consumers in the form of lower prices and new products, but there may well be an interim period in which early-adopting firms benefit first.

That said, the inflation genie has not quite been pushed back into the bottle yet, and our final scenario (**Second Wave, 20%**) counts the cost of declaring victory too early. In this setup, inflation continues to fall in H1, prompting central banks to cut rates, but it turns out that financial conditions were already too loose and not enough economic slack has been created to bring inflation back to 2% sustainably. As a result, inflation starts to pick up again in H2 and central banks must slam on the brakes again. In this world, it is possible that rates start to go up again – possibly the single most underpriced risk in the markets today. The huge monetary policy surprise this represents, causes both equities and fixed income to sell off sharply, replaying some of the nastiness of 2022 and triggering a significant economic downturn late this year and into 2025.

Of course, there are many tail risks, not least the possibility of escalation in one of the major geopolitical conflicts currently at play, or from a surprise election result in one of the many taking place worldwide this year. However, for the moment we are treating the nastiest of these as outcomes that fall outside the 80% probability range of our fan charts. Those charts suggest a lot of things about markets in 2024/25. First, the outlook for equities is modestly positive, justifying a cautiously risk-on approach. Cautious because the downside risks, though lower probability, are relatively large in magnitude. Second, fixed income continues to play an important role in multi-asset portfolios, both because it continues to offer a decent income return, even if nominal short rates fall. But also, because, at higher yields, it can play the hedging role in a multi asset portfolio it is supposed to. Internationally, we still prefer US equity markets, though at some point, probably when the reality of rate cuts bites, the relative cheapness of European markets comes into play, while Japanese markets are still favored to outperform despite Bank of Japan (BoJ) policy normalization, which we think won't be unduly restrictive. After a couple of strong years, the dollar is likely to be rangebound during 2024, thanks to growth and interest rate convergence.

This is the 26th edition of Vantage Point and, to date, it has played a useful role communicating the macro team's investment thoughts to fund managers and clients alike. However, with the establishment of BNY Mellon Advisors, it takes on a new role, closer to direct investment decisions. It becomes a critical macroeconomic and markets input into the new Global Macro Advisory Council (GMAC), which consists of experts from around the businesses (including the investment firms), whose asset allocation advice informs the shape all portfolios handled by Advisors.

SHAMIK DHAR
CHIEF ECONOMIST

VANTAGE POINT SUMMARY

We summarize the outlook in the graphics below. These show: 1) our 12-month forecasts of GDP growth, inflation, and monetary policy relative to their long-term trend; 2) how our fan chart forecasts differ from market expectations– in terms of expected returns and expected uncertainty.; and 3) our investment conclusions, based on the largest discrepancies between our own views and what the market is pricing in. Our conviction around our tactical investment views is higher when the level of uncertainty around our forecast is lower.

Table 1: Summary of our 12m outlook

How to read the heatmap. **Green** indicates above trend growth, below target inflation, policy accommodation and lower-than-average levels of uncertainty. Grey indicates economic growth in line with trend, inflation in line with target, a neutral policy stance, and average levels of uncertainty. **Red** indicates below trend growth, above target inflation, a tight policy stance, and higher-than-average levels of uncertainty.

		Growth	Inflation	Policy	Takeaway
Summary of VP outlook	**Average expectations**				Global growth is seen as positive but falling below trend in 12m; inflation is around target and policy is a little restrictive but still above neutral.
	Uncertainty				Uncertainty around growth is broadly in line with history, but higher for inflation and for future interest rates.

Table 2: Own forecast vs the market

How to read the heatmap. **Green** indicates that we expect growth to be higher than the market believes, inflation to be lower and policy accommodation to be greater. Green also indicates that uncertainty around our macro expectations is lower than the market is pricing. Grey indicates that expectations (or uncertainty around expectations) for economic growth, inflation and policy are broadly in line with the market. **Red** indicates worse than expected growth, greater than expected inflation and a tighter than expected policy stance. Red also indicates that uncertainty around our macro expectations is higher than what signaled by the market.

		Growth	Inflation	Policy	Takeaway
Vantage Point vs market pricing	**Average expectations**				Our inflation view is broadly in line with the market, but we see a higher likelihood of a positive growth surprise, and policy remaining tighter vs expectations.
	Uncertainty				Our fan charts imply greater uncertainty in the outcomes for growth, and monetary policy, but lower uncertainty for inflation compared to what is priced in option markets.

Table 3: Summary of 12 Month Investment Conclusions

How to read the heatmap. **Green** indicates overweight. Grey indicates neutral. **Red** indicates underweight. Polarized possible outcomes for the economy mean this is an environment to tighten risk budgets and not make bold directional bets.

Asset class	Q1 '24	Q2 '24	Rationale
Cash			Cash is attractive given low volatility, income returns, and rates that are expected to fall slowly.
Fixed Income			Benefits from high yields but low expected price returns seen as providing little uplift compared to cash, with greater risk.
Equities			A lot of optimism is priced in by the market over the near term, but expected returns are broadly in line with long term averages as recession risk recedes.
Credit			Elevated yields are attractive, but spreads are very compressed, and expected to rise providing a drag to total returns.
Alternatives			With a more constructive views of growth and expectations that inflation will be broadly in line with consensus, we remain neutral.

Source: BNY Mellon Investment Management, as of March 11, 2024.

EXECUTIVE SUMMARY

Our New Scenarios in Brief

PROBABILITY

50%

SCENARIO 1

Muddle Through

- The US economy slows throughout 2024 but avoids recession.
- Europe begins to grow slowly from near-recessionary levels.
- With no new shocks, global nominal demand moderates but remains steady.
- Global aggregate supply, unshackled from global pandemic concerns, stays balanced with demand.
- Inflation uncertainty persists, constraining central banks from aggressive policy rate cuts. Wage inflation remains high and stubborn, despite labor supply growth and high US immigration. Core services inflation in the US remains uncomfortably high.
- Credit concerns linger in the banking system due to maturity walls, misplaced duration bets, commercial real estate exposure fears and minimal regional bank profit spreads.
- China endures a “long muddle through”, missing optimistic Gross Domestic Product (GDP) growth targets generated by the government. Chinese property concerns linger. China exports a moderate disinflationary impulse to the rest of the world.
- AI frenzy moderates as productivity gains remain promising but elusive. Expenditures on AI and machine learning keeps tech spending at high levels, but with little immediate reward.
- Elevated market valuations come under pressure. Corporate profit margins face pressure but don’t collapse, keeping earnings to a mix of upside and downside surprises. Markets continue to look forward to easier monetary policy.
- Despite partisan friction, electorates contain policy extremism across numerous global elections.
- Peak globalization and geopolitical risk dampen speculative fever and animal spirits.

In our most likely scenario, present conditions persist into the future. Higher rates pressure the US economy to slow, but it avoids an outright recession, even while risks of a future recession linger. No new shocks affect either global demand or supply, so global supply chains continue to normalize and adjust to the absence of pandemic effects. However, considerable uncertainty about the path of inflation prevents central banks from cutting policy rates aggressively. Central banks limit policy easing to a small set of rate cuts (overall, less than 1%). Markets clamor for more rate cuts but central banks remain wary of reigniting a second wave of inflationary pressures. Markets also worry over credit concerns in the banking system due mostly to commercial real estate (CRE) or balance sheet issues. Globally, China misses its growth targets due to a meagre expansionary fiscal policy response, thus exporting deflation to the rest of the world. However, new sources of demand arise from other emerging market countries like India, Brazil, and Mexico. The frenzy around AI moderates to some degree as hoped-for productivity leaps remain elusive. Thus, AI tech expenditures mostly reduce healthy corporate profit margins. The plethora of democratic elections around the globe create partisan friction, but electorates sideline most extreme policy proposals. Sizeable geopolitical and global trade concerns hover in the background.

PROBABILITY

30%

SCENARIO 2

New Economy

- Generative AI technologies become ubiquitous, rapidly making meaningful contributions to total factor productivity as a general-purpose technology (GPT).
- Other technological innovations start to bear fruit, such as advancements in robotics, autonomous vehicles, labor augmentations, medical care, longevity, energy efficiency and green investment, among others.
- Growth surprises to the upside based on accelerated productivity from new technologies, allowing inflation to fall faster than markets anticipate.
- Developed markets productivity improves, wage growth remains robust, but critically, unit labor costs stay consistent with the inflation target. Productivity gains are largely cyclical to start with.
- Inflation expectations remain anchored. Wages, shelter, services, and core inflation fall more quickly than current market expectations.
- Central Banks begin to cut in the back half of 2024 at a pace faster than markets expect.
- Technology-led markets persist. Margins and fundamental multiples remain at high levels. Earnings surprise to the upside relative to forecasts.
- Equities are supported by easing policy and buoyant central bank liquidity.
- Other emerging markets pick up demand to compensate for lackluster Chinese growth.
- Optimism around technology improvements and growing economies contain partisan friction and policy extremism.
- Geopolitical risks lurk in the shadows but are kept mostly at bay.

In the "New Economy", current strong productivity growth in the US, largely cyclical in nature, remains in place in 2024, and AI starts providing a structural lift to productivity in 2025, ahead of what we envision (see here). AI technologies begin permeating all aspects of consumer and commercial life. Many industries are affected by new technological innovations, but these advancements work mostly to augment human labor rather than supplant it (i.e., net job losses are minimal, at least within our 3-year forecast horizon). On the heels of these productivity gains, wage growth and economic output remain robust. Cyclical fears of recession diminish entirely. Inflation also continues to stay on a path to meet central bank targets more quickly than many expect, opening the door to rate cuts. Thus, central banks exceed market expectations for easier policy and risk markets respond positively. Corporate profit margins bolster earnings by maintaining historically high levels. Optimism about the sustainability of those earnings also keeps intact relatively high (historically) price-to-fundamentals multiples and may push them higher as risk appetite firms. Effects of the spread of technological advancements spread globally and most regions perform well. The growth picture ameliorates strained internal and external political tensions. While serious geopolitical fractures still exist, they stay mostly in the background.

PROBABILITY

20%

SCENARIO 3

Second Wave

- US economy remains robust in the first half of 2024 while Europe, UK and China also gain forward momentum.
- Consumers continue to propel economies forward as households make up for lost consumption during the pandemic period.
- US inflation initially moves lower but then reaccelerates mid-year to over 4% due to tight US labor markets, loose US financial conditions and expansionary fiscal policy.
- Central banks abandon rate cuts and consider hikes in a major monetary policy surprise. The tightening in policy, relative to what is priced in by the market, is substantial. US real policy rates initially decline before hikes are enacted. Longer-rates begin to follow policy rates higher.
- In Europe, labor hoarding, high real wage resistance, low labor productivity with high and rising unit labor costs feed rising inflation in the second half of 2024.
- China adds large consumption stimulus to monetary easing, mitigating the effect of softer real estate and capital markets. Chinese housing markets rebound. A domestic deflationary spiral is averted. Globally, disinflationary goods price pressures reverse.
- Fear of trade wars and higher tariffs constrain global aggregate supply, exacerbating price pressures.
- Higher rates and monetary tightening affect real estate. Cracks from commercial real estate spreads to other credit sectors. High yield and even investment grade credits struggle with refinancings and rising debt service costs.
- US and EU slow sharply by year-end. Recession fears emerge for 2025.
- AI enthusiasm is overshadowed by the inflation and the hawkish monetary policy surprise.

In the "Second Wave", inflation follows a common historical pattern and rises again without coming near central bank targeted levels. Tight labor conditions keep wage inflation high, housing supply constraints keep shelter costs high, and energy markets stay too elevated to ease price pressures. Central banks, to the market's dismay, retreat from policy rate cuts and likely begin planning for additional tightening measures to stem the rising tide of inflation. Higher rates impair CRE and credit markets. Recessionary cyclical concerns form as a response to tightening monetary policy. Credit spreads begin to widen from very low levels. Growth stocks and the AI theme come under valuation pressure from higher long-term interest rates. China steps up with meaningful policy response to offset real estate and labor concerns, averting a deflationary spiral but adding to global inflation pressure. Inflation causes tension in domestic political circles as minimal real wage gains put pressure on consumers. In this scenario, the US dollar, reacting to likely policy rate hikes, proves stronger than many competing global currencies. Inflation hedges perform well, at least initially, as investors look for safe havens from the inflationary impulse. Many global economies as well as global risk assets face pressure.

BNY MELLON

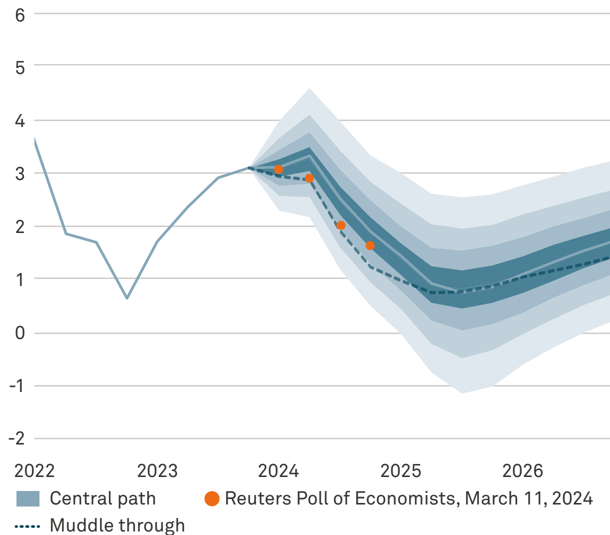
01 WHAT WE THINK

01 WHAT WE THINK: FORECAST SUMMARY

The US economy has proved remarkably resilient in the face of one of the most rapid tightenings of monetary policy since the Second World War. Growth surprised repeatedly to the upside through last year, while other measures of economic activity, such as the non-farm payrolls measure of employment, also turned out stronger than expected. Europe too has fared better than many feared. Although both the euro area and the UK saw two consecutive quarters of falling output in the second half of last year, these falls were modest, there were no signs of an increase in unemployment in either location, and business surveys point to a return to more normal rates of economic expansion through the first quarter of this year. At the same time, inflation has proved a little stickier than many had hoped in most major economies. Wage inflation is no longer clearly on a downward trend in the US, while in Europe, and particularly in the UK, it remains far above levels consistent with meeting the 2% inflation target. It is against this uncertain backdrop that we present our latest forecast.

Our assessment of the range of possible outcomes for US economic activity is shown in the first fan chart. Risks to our single most likely scenario, which is close to the consensus among other economists and sees US growth drop below trend this year as the policy tightening starts to bite, lie mainly to the upside. In the short-term this reflects primarily the sustained period of above-trend growth that occurs in ‘Second Wave’. Further out upside risks to growth reflect the possibility that the supply side of US economy is already stronger than most forecasters, including the US Federal

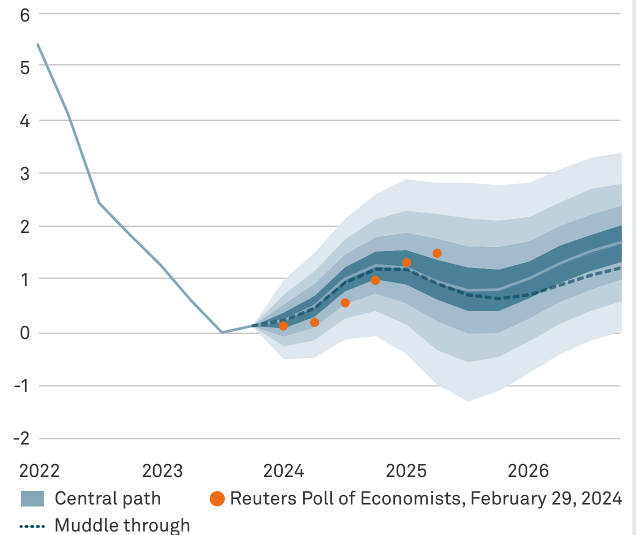
CHART 1: US GDP
FOUR-QUARTER PERCENTAGE CHANGES



Source: Refinitiv Datastream/Fathom Consulting.

Key Takeaway: We expect US growth to slow, more or less in line with consensus expectations, but most likely avoiding a recession with growth troughing near a 1% annualized rate.

CHART 2: EURO AREA GDP
FOUR-QUARTER PERCENTAGE CHANGES



Source: Refinitiv Datastream/Fathom Consulting.

Key takeaway: Euro area growth has likely already troughed and we expect will rise gradually in the coming quarters, albeit the pick up may be short lived.

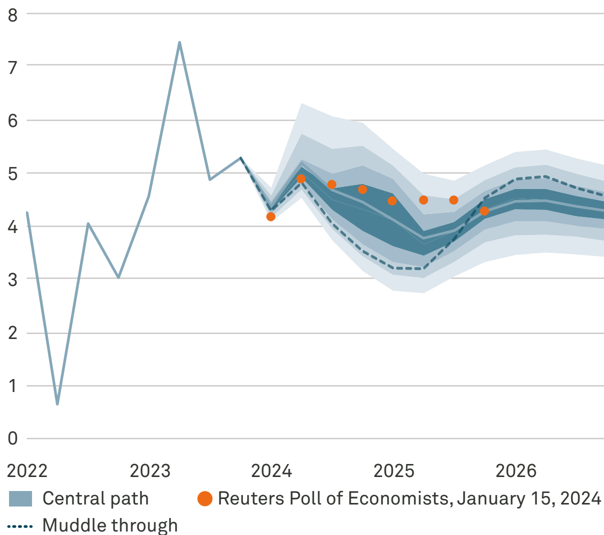
Forecasts begin in Q4 2024 and were calculated as of March 10, 2024. Source: BNY Mellon Investment Management and Fathom Consulting. The “central path” (i.e., blue bands) represents the central 20% of outcomes based on a mean or probability-weighted average forecast across all three scenarios. The light gray bands show progressively less likely outcomes covering a combined 60% of the forecast distribution. The width of the fan chart shows the level of uncertainty and when the bands below the central path are wider than those above, this shows the balance of risks lies to the downside.

Charts are provided for illustrative purposes and are not indicative of the past or future performance of any BNY Mellon product.

Reserve (Fed), believe it to be, and that sustainable rate of economic growth improve further from here. That the chances of a severe contraction in US economic activity are fading becomes apparent when one considers the relatively small portion of the distribution of outcomes that now lies below the horizontal axis in our chart. Three months ago, we saw a four-quarter contraction in GDP as most likely to occur in the first half of next year, with odds close to 1-in-2. Now those same odds peak at around 1-in-4 and are concentrated in the second half of next year.

We see a good chance that growth in Europe has already troughed, and we are a little more optimistic than the consensus about near-term prospects for that region. While the possibility of a severe contraction remains, we now see it as more of a risk for next year, driven by a prolonged period of higher interest rates in 'Second Wave', than this year. In our judgement the near-term prospects for China's economy are particularly uncertain, reflected in the width of our fan charts for Chinese economic growth through this year. In 'Second Wave', policy stimulus proves successful, and growth recovers, removing the threat of a domestic deflationary spiral. By contrast, in our single most likely scenario, 'Muddle Through', growth slows further from here, and Chinese output prices continue to fall. Weighting the three scenarios together, our mean path for Chinese growth is generally weaker than the consensus among other forecasters, particularly through next year.

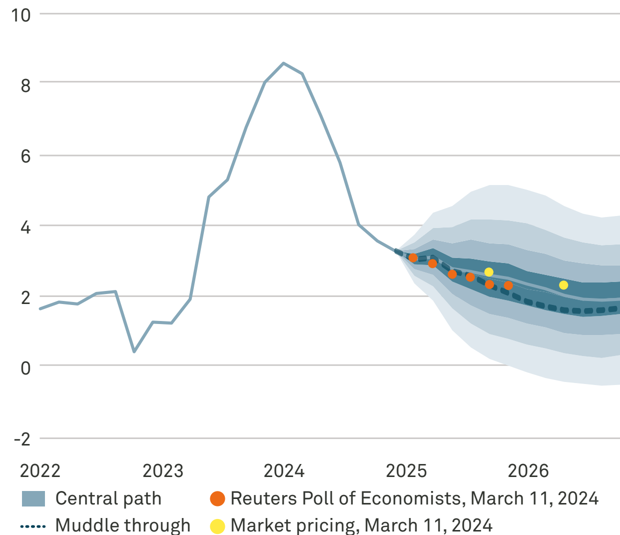
CHART 3: CHINA GDP
FOUR-QUARTER PERCENTAGE CHANGES



Source: Fathom Consulting.

Key Takeaway: We see China growth weaker than consensus in the coming quarters, particularly in our 'muddle through' scenario.

CHART 4: US CPI
FOUR-QUARTER PERCENTAGE CHANGES



Source: LSEG Datastream/Fathom Consulting.

Key Takeaway: We expect the disinflation trend to continue, broadly in line with consensus, however, we see larger upside risk stemming from our odds-against scenario 'second wave'.

Forecasts begin in Q4 2024 and were calculated as of March 10, 2024. Source: BNY Mellon Investment Management and Fathom Consulting. The "central path" (i.e., blue bands) represents the central 20% of outcomes based on a mean or probability-weighted average forecast across all three scenarios. The light gray bands show progressively less likely outcomes covering a combined 60% of the forecast distribution. The width of the fan chart shows the level of uncertainty and when the bands below the central path are wider than those above, this shows the balance of risks lies to the downside.

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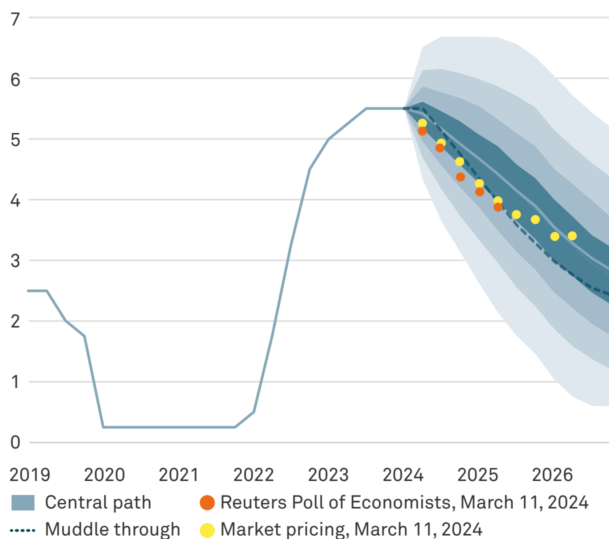
Looking across the range of possible outcomes, we expect inflation to continue to fall towards the 2% target in both the US and the euro area, though much less rapidly than took place through much of last year. We see close to a 40% chance that inflation is either at or below 2% in the US by the end of this year, and around a 20% chance that it has moved back above 4%. The corresponding probabilities for euro area inflation are very similar.

Our fan chart for the US Federal Funds rate shows that, in our judgement, the single most likely path for the US policy rate of interest is very close to what is priced in through this year. The risks, however, lie to the upside in the short-term as further tightening becomes a possibility in 'Second Wave', and further out, as an improving outlook for productivity growth puts upward pressure on the neutral rate of interest, or r* ('R-Star'), in 'New Economy'. Ten-year US government yields are also likely to fall from here, although less rapidly than is priced in. Our mean path for yields lies above market pricing throughout our forecast horizon.

Although we expect to see higher short- and long-term interest rates than other forecasters, and notably those participating in financial markets, we expect to see higher equity prices too. That is because our beliefs about both are shaped by the weight we attach to our 'New Economy' scenario, which sees productivity growth rise above its post-Global Financial Crisis (GFC) norms globally, led by

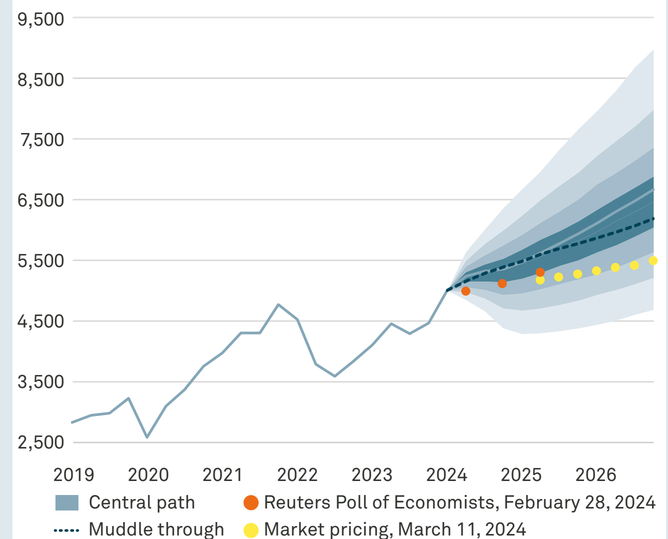
CHART 5: US FEDERAL FUNDS RATE
PER CENT



Source: LSEG Datastream/Fathom Consulting.

Key takeaway: We continue to expect the Fed's easing cycle to kick off mid-year and progress broadly in line with current market pricing (~3 cuts in '24). Note that market pricing previously expected many more cuts, but has moderated and moved in line with our view in recent months.

CHART 6: US S&P 500
INDEX



Source: LSEG Datastream/Fathom Consulting.

Key takeaway: Receeding recession risk and the start of the easing cycle supports risk asset progress, albeit headwinds persist (i.e., valuations). Ongoing AI enthusiasm and corporate adoption, which our research corroborates, pushes our S&P 500 forecast modestly above consensus.

Forecasts begin in Q4 2024 and were calculated as of March 10, 2024. Source: BNY Mellon Investment Management and Fathom Consulting. The "central path" (i.e., blue bands) represents the central 20% of outcomes based on a mean or probability-weighted average forecast across all three scenarios. The light gray bands show progressively less likely outcomes covering a combined 60% of the forecast distribution. The width of the fan chart shows the level of uncertainty and when the bands below the central path are wider than those above, this shows the balance of risks lies to the downside.

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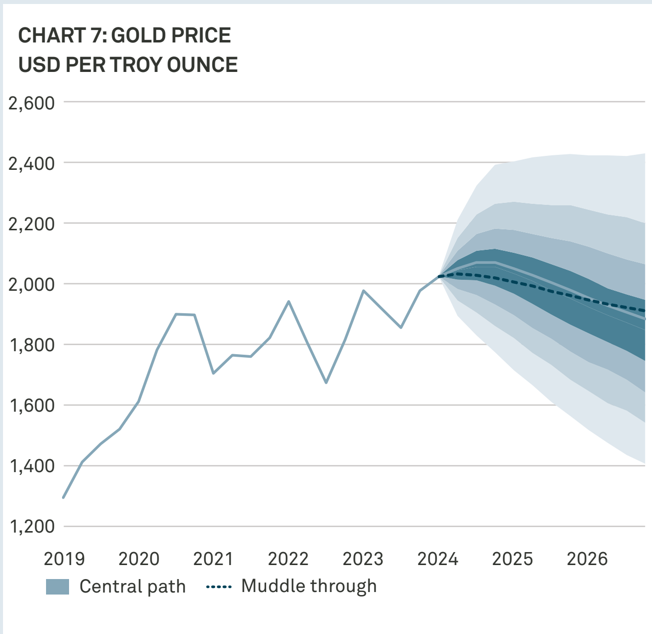
the US. This is a scenario in which equities do very well, with stronger earnings growth more than offsetting the higher discount rate necessary to contain aggregate demand in an environment where households perceive a marked improvement in their lifetime resources. Risks to the single most likely path for the S&P 500 lie clearly to the upside, particularly towards the end of our forecast.

The real price of gold has more than trebled since the turn of the century as real rates of interest have fallen. While our fan chart for the price of gold is wide, reflecting in part its historic volatility, we nevertheless expect gold prices to fall from here in cash terms, with larger falls after adjusting for inflation. The decline occurs because, in scenarios with a combined weight of 80%, the recent period of high and volatile inflation is largely behind us. It also reflects the 30% weight we attach to 'New Economy', a world in which discount rates rise.

CHART 7: GOLD PRICE
USD PER TROY OUNCE



Source: Fathom Consulting.

Key Takeaway: We expect gold prices to decline due to the fact in scenarios with a combined 80% weight, the recent years of very high and volatile inflation are now behind us. Moreover, with recession risk declining, the safe haven benefits of gold are fading.

Forecasts begin in Q4 2024 and were calculated as of March 10, 2024. Source: BNY Mellon Investment Management and Fathom Consulting. The "central path" (i.e., blue bands) represents the central 20% of outcomes based on a mean or probability-weighted average forecast across all three scenarios. The light gray bands show progressively less likely outcomes covering a combined 60% of the forecast distribution. The width of the fan chart shows the level of uncertainty and when the bands below the central path are wider than those above, this shows the balance of risks lies to the downside.

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BNY MELLON

02

WHAT THE MARKET THINKS

02A WHAT'S PRICED IN

Summary: The strong positive performance of risky assets this year, even as rate cut expectations unwound and bond yields rose, signal expectations of robust growth ahead. Presently, market expectations are consistent with strong aggregate cyclical conditions, and a slow return of monetary policy to non-contractionary (i.e., neutral) levels. Not only has 'soft landing' likely already occurred in the markets' view, but the landing is seen to have taken place on the runway of a much better cycle – one characterized by stronger growth and higher interest rates. US, euro area and UK monetary policy are seen as loosening gradually from mid-summer, and gradually adjusting to neutral levels approximately by the end of 2025. Very little in the way of market pricing suggests the market remains concerned about recession. Cross asset risk premia are compressed, particularly on US assets. In fact, the compensation offered to investors to go overweight US risky assets such as equities or credit is at the lowest since the global financial crisis. That said, we think the AI story has further room to run and would not be surprised if US equities became even more expensive going forward (see here). Some divergence in DM growth remains reflected in market prices, but less so than at the end of last year. The risk that inflation remains away from target is still elevated compared to history, and high inflation is still seen as a greater risk than low inflation in the coming years.

Market-based growth expectations: Global market-implied growth expectations remain elevated but not stretched, and around the average seen since mid-summer 2023. The divergence between the market view of growth and survey indicators – such as the global Purchasing Managers Indexes (PMIs) – is closing, with macro data improving rather than market expectations deteriorating. And while there remains some divergence, leading growth indicators that tend to anticipate changes in the global PMIs, support further progress from here. Asset classes and strategies most sensitive to the economic cycle continued outperforming, in line with what seen since the start of 2023. US markets still appear to be pricing the strongest cyclical conditions, but the gap with other Developed Markets (DM) regions has been narrowing, with growth prospects improving the most in the euro area and Japan. In contrast, Emerging Markets (EM) proxies of growth have improved

The market is expecting strong growth, at target inflation and rate cuts to neutral. Uncertainty around this view is not elevated, particularly with respect to the growth outlook.

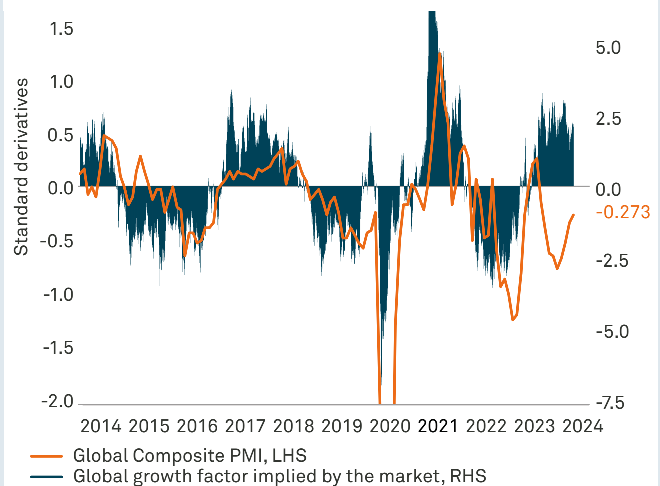
TABLE 1: SUMMARY OF MARKET PRICING

Market pricing	Growth	Inflation	Policy
Expectations – at end Q4	Green	Grey	Green
Expectations – current	Green	Grey	Grey

Green indicates above trend growth, below target inflation and policy accommodation. Grey indicates economic growth in line with trend, inflation in line with target and a neutral policy stance. Red indicates below trend growth, above target inflation and a tight policy stance.

Markets' view of growth is elevated but survey measures of growth are improving.

CHART 8: MARKET GROWTH EXPECTATIONS AND GLOBAL GROWTH LEADING INDICATORS



Source: Macrobond, BNY Mellon Investment Management. Data as of March 11, 2024.

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little and remain very low, in line with pessimistic expectations around the outlook for Chinese growth. Despite what remains a complex macro environment to navigate, measures of downside tail risk derived from equity option markets paint an optimistic picture for growth risks in major economies, with very little probability of a growth scare priced in for the next 12 months.

Market-based Inflation expectations: Markets pricing of inflation remains consistent with a steady return to target across most economies. For the US, the market sees inflation remaining around 3% in the very near term, before easing towards 2-2.5% in the second half of the year. In the euro area, inflation is expected to remain around 2.5% in Q2, dip briefly below 2% around September and then bounce back to 2% by year end. Long term inflation forwards signal stronger inflation in the US than in the euro area. The differential between US and euro area forward inflation had almost closed in 2023, and the recent move in favor of stronger US inflation is more consistent with our view. The UK remains an outlier, with the market pricing in continued stickiness in inflation in the near term, and above target inflation in the distant future. Option markets continue to signal higher than usual uncertainty around the outlook for inflation over the next five years, and the probability of a large upside deviation of inflation from target remains high, despite falling a little since the start of the year.

Market-based monetary policy expectations: Global monetary policy expectations repriced higher over the quarter, after rates had fallen significantly below the policy rate paths signaled by major central banks. The Fed, the European Central Bank (ECB) and the Bank of England (BoE) are now seen as loosening policy from mid-summer. The market expects between 6 and 7 rate cuts for the Fed and the ECB, and 5 to 6 rate cuts from the BoE by the end of 2025. We find it notable that little policy divergence is expected between major central banks over the next few years, despite different growth and inflation backdrops. The pace of cuts is broadly consistent with a continued, somewhat slow, progress towards a return of inflation to the to 2% target – which merits a 'start and stop' approach, to assess the impact of the first round of loosening on the economy – and a higher real neutral rate of interest (r*). Long term forward US real rates are trading at around 1%, above the FOMC's real long run dot (at 0.5%), but not much above model implied estimates of r*. Our research suggests that global r* will rise by the end of the decade, and current market expectations are directionally consistent with our views (see here). Outside of the US and Europe, some greater divergence in monetary policy is expected, with the BoJ seen as normalizing policy back into positive territory by 2025, and the Reserve Bank of Australia (RBA) expected to deliver only one rate cut by the end of the year and less than three rate cuts by end 2025.

The probability of above-target inflation in the US has fallen a little but remains much higher than the pre-Covid average.

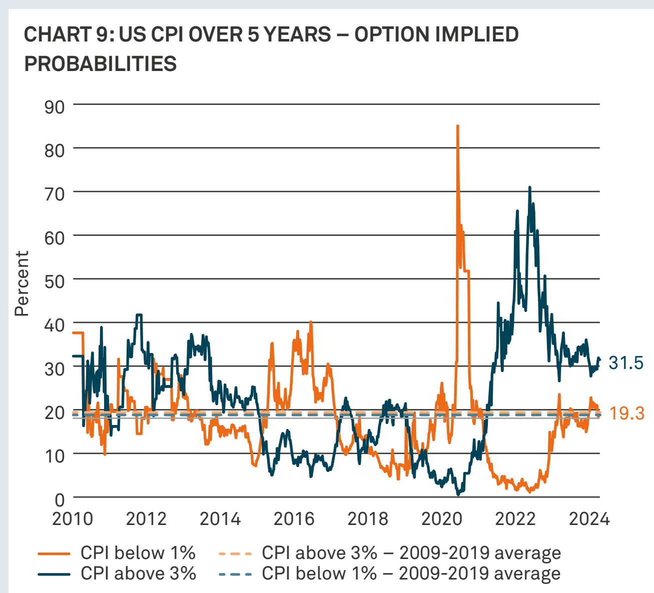

CHART 9: US CPI OVER 5 YEARS – OPTION IMPLIED PROBABILITIES

Source: Macrobond, BNY Mellon Investment Management. Data as of March 13, 2024.

Markets are not pricing much divergence in monetary policy across the G10.

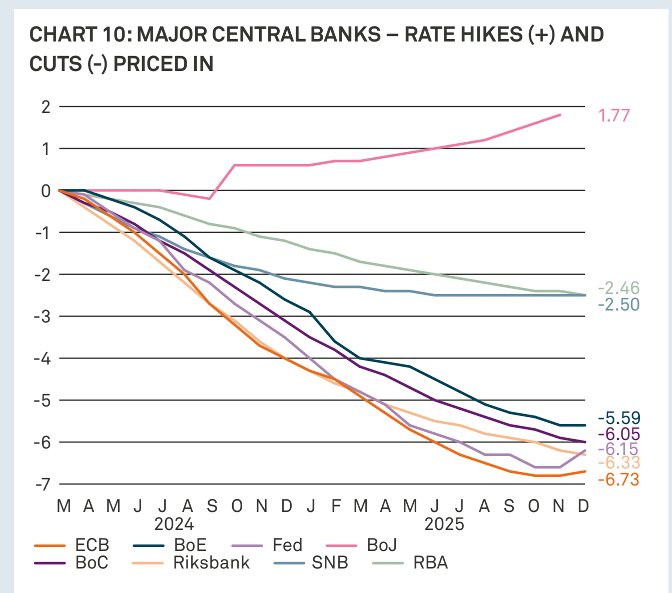

CHART 10: MAJOR CENTRAL BANKS – RATE HIKES (+) AND CUTS (-) PRICED IN

Source: Macrobond, BNY Mellon Investment Management. Data as of March 8, 2024. European Central Bank (ECB), Bank of England (BoE), US Federal Reserve (Fed), Bank of Japan (BoJ), Bank of Canada (BoC), Swiss National Bank (SNB), Reserve Bank of Australia (RBA)

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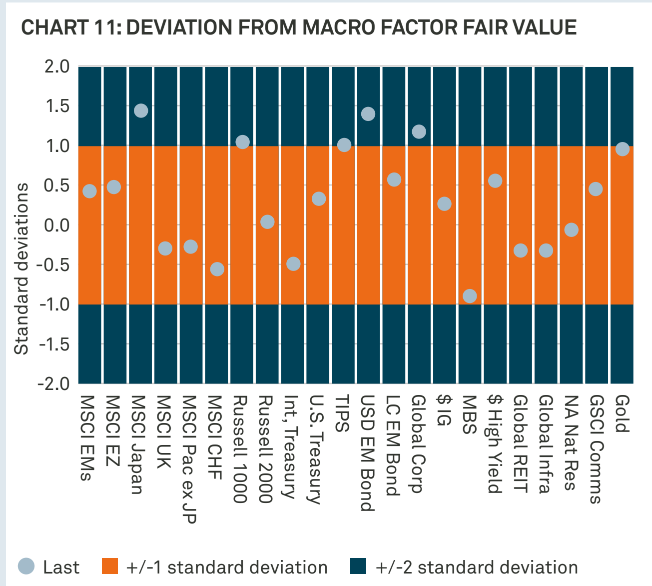
02B MARKET SENTIMENT

Market sentiment and positioning remain bullish and improved further over the quarter but have not reached 'stretched' levels that can provide a useful contrarian buy/sell indicator. Recall, when sentiment and/or positioning reach extremely positive (negative) levels, it may be a tactical selling (buying) opportunity as subsequent performance tends to be negative (positive) in the near-term. Said simply, 'bullishness' can still increase from here. That said, some asset classes – namely Japanese equities, US equities, USD EM bonds and Global IG Corporate bonds – are trading at levels above that consistent with macro drivers and could be vulnerable to a change in sentiment. Indeed, at the time of writing, some signs of exhaustion in the rally could be emerging, for example the Nasdaq and the Nikkei both traded down from their highs recently. The question is whether this may be just a short-lived pause in the upside trend or the start of a more meaningful pull-back.

In equities, concentration is high, as investors continued buying exposure to the areas of the market (e.g., big tech in the US) heavily reliant on the AI story and that have seen strong performance relative to the broader index in recent quarters. In principle, high concentration poses higher risks of a pullback in performance, given greater-than-usual exposure to idiosyncratic, stock-specific, risks. That said, we remain fundamentally positive the AI story, and as we have written about in our recent analysis of the topic, we think the theme has further to run, including thanks to the elevated probability that a stock market bubble may eventually form (see here). The uneasiness of investors with the narrowness of the rally is likely to remain for some time. For now, equity momentum remains positive, particularly in Japanese and US equities. Both markets moved above all-time highs since the start of the year, which in case of Japanese stocks is particularly noticeable given these levels have not been

Japanese equities, US equities, USD EM bonds and Global IG Corporate bonds returns are above what usually explained by macro drivers.

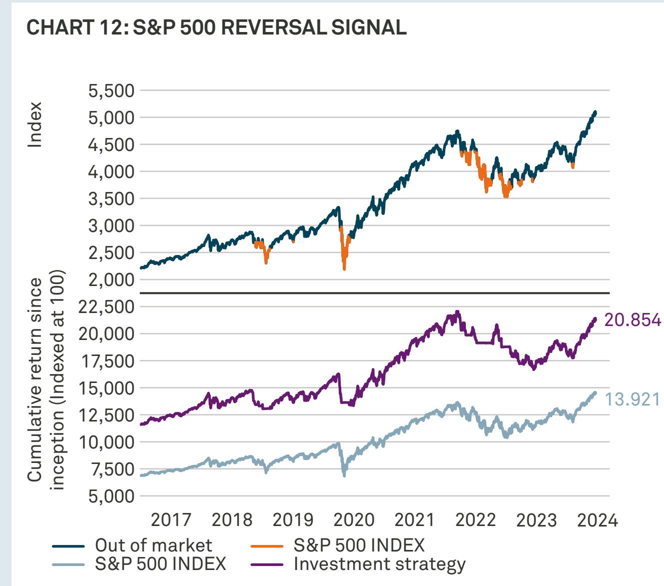
CHART 11: DEVIATION FROM MACRO FACTOR FAIR VALUE



Source: Macrobond, BNY Mellon Investment Management. Data as of March 12, 2024.

Despite the strong rally, technical signals do not suggest turning risk off.

CHART 12: S&P 500 REVERSAL SIGNAL



Source: Macrobond, BNY Mellon Investment Management. Data as of March 11, 2024.

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tested since the end of the 1980s. When an asset class 'breaks up' to the upside of the range it has been trading in for some time, previous 'stop losses' are closed and new technically informed 'take profit'/'stop losses' are set for new trades, which is likely to lead to an extension of the previous directional move. Most short- and medium-term models of risk sentiment for the S&P 500 are mid-range/neutral, also lacking a signal that the market has become 'euphoric' and investors should become more defensive in the near term. Our own 'reversal' signal provides a similar message: it's not yet the time to become more defensive on sentiment grounds.

Turning to fixed income, sovereign bond markets lack momentum at the moment, as performance remains range bound, and investors wait for the start of the loosening cycle by major central banks before becoming more constructive on price returns. Positioning is broadly neutral to slightly negative, as are measures of bond market sentiment. With no indication of stretched sentiment or positioning, and no momentum, we take little signal for a fixed income overweight or underweight decision on technical grounds this quarter.

Trend is positive in equities, credit and alternatives but neutral to slightly negative in sovereign bonds.

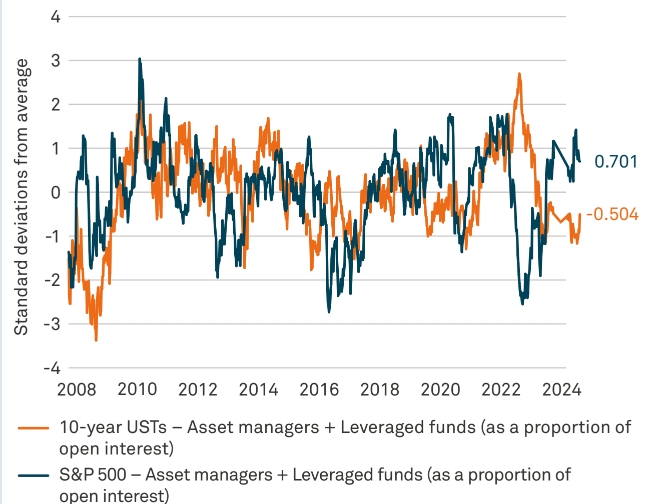
TABLE 2: CROSS ASSET TREND SIGNAL

Cross asset trend signal	
Equities	
S&P 500	
FTSE 100	
Euro Stoxx 50	
Topix (Japan)	
Hang Seng (China/Hong Kong)	
Emerging markets	
Sovereign fixed income	
US 10-year	
Canada 10-year	
Germany 10-year	
UK 10-year	
Credit	
$ Investment grade	
$ High Yield	
Alternatives	
Gold	
Oil	

Source: BNY Mellon Investment management using Bloomberg data. Data as of March 13,2024. The heatmap shows return trends across assets. Green indicates a positive signal (go long/overweight), red indicates a negative signal (go short/underweight), and grey indicates a neutral signal.

Positioning in equities is very positive but not yet stretched, while positioning in bonds in relatively neutral.

CHART 13: POSITIONING IN THE S&P 500 AND 10-YEAR US TREASURIES



Source: Macrobond, BNY Mellon Investment Management. Data as of March 12, 2024.

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03
INVESTMENT CONCLUSIONS

03 INVESTMENT CONCLUSIONS

Summary

With three months in the books, one could be forgiven for thinking we've already racked up a full year of returns and then conclude that we should expect nothing more from 2024. This may seem logical given returns already in line with annual averages, but this is **not** how markets work. Returns are often chunky and highly unpredictable, rather than smooth and steady. So, where does a hot start to the year leave us now?

As always, it's not about where we've been, but where we're heading that matters most to markets. Our scenarios and associated probabilities indicate that we're becoming cautiously more optimistic about the economic destination in the coming months/quarters. This, in turn, makes us more optimistic on the expected performance of risk assets, which is reflected in several upgrades in the following asset class tables. In short, as recession risks recede and easing cycles appear on the horizon, expected returns rise and we project better total portfolio performance.

Our scenarios paint a picture of moderating (but unlikely recessionary) growth, paired with ongoing disinflationary trends, and near-term central bank policy cuts. This backdrop, while not identical across regions, is nevertheless broadly positive for risk assets. Another way to put it: the current cycle appears to be extending with the risk of a "hard landing" fading, which translate into smaller downside risks, particularly for growth sensitive assets like equities. For the first time in at least a year, our proxy portfolios clearly show an odds-on probability of an equity-heavy portfolio outperforming a bond-heavy portfolio over the outlook horizon.

We'd previously noted that returns may be constrained by elevated real rates, lingering recession fears, and what's priced in (i.e., too many rate cuts). On the latter, the market has priced out the overly dovish easing cycle and come more in line with both the Fed's and our expectations. As noted in previous sections, market pricing also suggests very little fear of recession. While we similarly expect recession risk is now lower, we do envisage a possible world where a recession develops, but it transpires on the back of a 'Second Wave' of inflation and so does not arrive until 2025 (albeit risk assets would likely sell-off earlier if the Fed unexpectedly hints at re-starting the hiking cycle). Finally, elevated real rates are also still a near-term constraint, however, we see rates falling back in the second half of the year as cutting cycles commence and inflation moderates, which points to a diminishing headwind on valuations.

As these constraints loosen, we see other reasons to turn more favorable. First, history suggests that the macro landscape described in our mean scenario (one of positive growth and nascent cutting cycles due to policy normalization, rather than recession) is fertile ground for supporting the ongoing rally. Moreover, our research into past cycles, and sentiment analysis in the previous section, do not indicate stretched levels. In fact, the US bull run since October 2022 appears quite average compared to all bull runs since 1950.

Second, we remain optimistic on AI's equity impact, especially on US equity (see here). Our research suggests it is still early days of pricing in AI's equity impact and although the impact is highly uncertain, we think there is a high probability that AI will transform many businesses across sectors, ultimately leading to greater profit potential. While markets have quickly moved to price in the benefits for a handful of big tech names, we see the theme as much broader. We capture this view most acutely in the 'New Economy' scenario where multiples push higher while earnings beat on better-than-expected growth fueled by labor productivity gains. Critically, we do not think these benefits are yet priced into the market.

The table shows the potential paths for the S&P 500 using estimates of P/E and EPS (price/earnings and earnings per share, respectively).

Muddle Through	Year End Values		
	2024	2025	2026
EPS Estimate	245	275	297
Earnings Growth	10%	12%	8%
Price/Earnings	22	21	21
Approximate Level	5,397	5,769	6,231
Annual Return Estimate	13%	7%	8%

New Economy	Year End Values		
	2024	2025	2026
EPS Estimate	250	282	310
Earnings Growth	12%	13%	10%
Price/Earnings	23	24	24
Approximate Level	5,744	6,773	7,451
Annual Return Estimate	20%	18%	10%

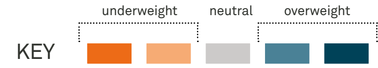
Second Wave	Year End Values		
	2024	2025	2026
EPS Estimate	239	258	278
Earnings Growth	7%	8%	8%
Price/Earnings	19	19	20
Approximate Level	4,534	4,896	5,566
Annual Return Estimate	-5%	8%	14%

Forecasts were calculated as of March 10, 2024. BNY Mellon Investment Management GEIA.

On a tactical basis, the outlook for risk assets appears more balanced (i.e., less downside skew) with expected returns closer to long-run averages, which led us to upgrade our overall equity and US equity views to neutral. Lower recession risk translates to lower probability of aggressive central bank policy cuts, which moderates our view on fixed income. Income returns remain attractive, but a more likely gradual pace of rate cuts will limit a vigorous rates rally. Cash, meanwhile, remains favorable for the time being given still-high short-end rates and low volatility. Reinvestment risk has moved lower in line with a smaller probability of deep recession-induced cuts. Our fan charts show rate cuts coming modestly slower than the consensus, pulled higher by the 'Second Wave' scenario, a risk we see as underpriced by the market.

Based on our probability weighted scenarios, we derive risk-adjusted return estimates across assets, and in the tables that follow, we lay out our tactical (2024 and early 2025) and strategic (multi-year) views. Our fan charts project equity gains and a preference for US and Japanese equities over Europe and UK. On the fixed income side, we favor exposure to developed market sovereign debt with a preference for international sovereigns over US Treasuries.

ASSET CLASS VIEWS



Major asset class	Tactical view	Strategic view	Comments
Equities			Receding recession risks, ongoing disinflation, and the start of policy easing cycles provide a more supportive backdrop to equities. Although inflation uncertainty and by extensions monetary policy uncertainty remain key risks, we assign a significant probability to an ongoing disinflationary trend and gradual policy normalization. A positive, albeit moderating, growth backdrop should provide sufficient support for earnings to deliver on growth expectations. We upgrade to Neutral on a tactical basis with selective regional preferences detailed below.
Fixed Income			Fading recession risk translates into a lower probability of aggressive central bank policy cuts, which led us to moderate our overall fixed income view to Neutral. While income returns remain very attractive, it is likely the pace of rate cuts will be more gradual, which limits the possibility of a vigorous rates rally. We continue to advocate for gradually extending duration of fixed income portfolios to 1) lock in attractive multi-year rates and 2) hedge against unexpected severe growth slowdowns. Given tighter than average credit spreads, we continue to lean in favor of sovereign debt and higher quality credit exposure.
Alts/Real Assets			Alternatives are historically less sensitive to growth and as such may provide additional portfolio stability in an unexpected growth slowdown. We're tactically neutral on alternatives and real assets.
Cash			Cash remains favorable for the time being given still-high short-end rates and low volatility of the asset class. Reinvestment risk has moved lower in line with a smaller probability of deep recession-induced rate cuts. Nevertheless, we expect cash rates to trend lower, especially from H2 onward, so the favorable tactical view is unlikely to persist.

Equity	Tactical view	Strategic view	Comments
Developed Markets Equity			Receding recession risks, ongoing disinflation, and the start of policy easing cycles provide a more supportive backdrop to equities. DM central banks look to embark on cutting cycles that we expect will gradually reduce equity headwinds and shore up risk appetite as lingering concerns about a hawkish surprise are pushed firmly out of mind. Yet, risks remain as victory over inflation is not yet guaranteed and a bumpy patch of inflation data could spook markets into a pullback. Overall, the outlook appears more balanced (i.e., less downside skew) with expected returns closer to long-run averages, which led us to upgrade our tactical view to neutral.
US Equity			Fading recession probability, leaving a favourable macro backdrop (positive growth, disinflation, and nascent policy cuts), combined with ongoing AI enthusiasm led us to upgrade our tactical view to Neutral. Our research into AI's potential equity impact increased our estimation of possible upside returns (i.e., multiples may expand much further from current levels). Of course, the AI tailwind may fizzle out or simply take much longer to deliver on promised labor productivity gains, but we think there is a strong argument that the market will price in AI's impact across sectors sooner-than-skeptics believe. The strong start to the year on increasing multiples maintains a vulnerability that any temporary back up in rates may cause an excessive de-rating in multiples and limit near-term returns, but overall, the macro winds (as captured in our fan charts) suggest the path for US equity trends upward near long-run averages, which is a notable upgrade to previous forecast rounds.
UK Equity			Cheap valuations on both a relative and historical average basis remain attractive and imply that minimal less bad news could spur on markets to re-rate. But the sectoral composition of the index is unhelpful (e.g., UK vs. US equity performance is strongly correlated with Value vs. Growth). The gradual closing of the Brexit premium ahead of the UK general election is supporting the British Pound (GBP), which is a headwind for UK large caps that have a large share of non-sterling earnings. We are more positive UK small caps. Overall, we remain tactically underweight, but more positive on a strategic basis.
Europe ex UK			We upgrade European equities on the back of expected positive earnings revisions and an improvement in multiples over the next 12 months. The asset class is strongly cyclical, and our view is that the global and regional growth outlook has improved. Despite expecting positive returns, we expect allocations elsewhere (e.g., US, Japan) to provide greater returns over the full horizon.

Equity	Tactical view	Strategic view	Comments
Japan Equity			Despite a recent weak growth patch, Japan is reflating --underpinned by rising wages, strengthening corporate sector reforms and more entrenched inflation expectations. We think BoJ policy will not be unduly restrictive despite recent normalization efforts. Corporate earnings to remain buoyed by overseas streams of income, and unlikely to be undermined by any firming in FX settings. Valuation metrics remain attractive. We turn Overweight tactically and remain so strategically.
EM Equity			We stay neutral EM equity both tactically as well as strategically. The drag from China persists. However, it is lessening as China's weight in indices slips. More fundamentally, many EMs are also gradually adapting to a prolonged China slowdown. But subdued commodity prices and odds of, at best, only a modest weakening of the US dollar (USD) index limit much upside.
EM ex China Equity			EM equity excluding China looks increasingly attractive as the drag from China is technically and fundamentally curtailed. Underlying price trends also reflect a variety of secular growth themes: AI-driven semiconductor-led gains in Taiwan and Korea; domestic-demand driven strength in India; and 'friend-shoring' in places like Mexico and Central Europe. Even without a USD tailwind, modest rate cuts from an increasing number of EM central banks will also help. Valuations remain balanced with P/Es in the mid-teens. We stay Neutral tactically, but remain Overweight strategically.
China Equity			Chinese equities have cheapened, dragged lower by weaker real and nominal GDP growth. This reflects a long-term downturn in property, excess capacity, too little stimulus. All of this has resulted in persistent economy-wide deflation. The National People's Congress (NPC) meeting disappointed with a reticent fiscal strategy. We do not see the necessary catalysts to expect a sustained re-bound anytime soon. We remain Underweight on a tactical as well as on a strategic basis.

Fixed Income	Tactical view	Strategic view	Comments
US Treasuries			We downgrade US Treasuries to Neutral. The outlook for the US economy has improved, and we see less risk of a strong deterioration in growth that would merit sharp rate cuts from the Fed. Instead, our downside scenario for growth is a negative one for US rates as it rests on the view that inflation could reaccelerate prompting further rate hikes. In addition, the fall in inflation seen so far has occurred on the back of strong productivity growth, which suggest that the long-term level of interest rates could be rising, limiting price return expectations in case of cuts. The high level of nominal yields still offers attractive income returns, as does extending duration to lock in multi-year rates.
Intl. Sovereign Debt			We maintain an overweight tactical allocation to a range of other developed market sovereign fixed income, e.g. Germany and UK. With the loosening cycle likely to start soon in the euro area, and risks to growth that remain (e.g. in Germany), we expect favorable risk-adjusted returns over the next 12 months. The potential stickiness of inflation in Europe or the UK prevents us going maximum overweight the asset class, but we have a tactical preference compared to US Treasuries given the weaker economic backdrop despite the somewhat lower income return offered.
Global IG			High grade corporate spreads have become somewhat rich amid a gradual economic slowdown and new issuance needs –all of which are likely to result in modest (~25bps) spread widening in the year ahead. But yield levels are elevated on a historic basis and provide a buffer. We stay Neutral tactically and expect returns to be in line with risk free sovereign returns; we also stay Neutral strategically.
High Yield Debt			Recession avoidance and peak US rates allowed High Yield (HY) to rally much more than we anticipated, in 2023. But rich credit valuations (20-year tights in spreads), coupled with a gradual economic slowdown, slow rate cuts, and elevated re-financing needs weigh on HY's near-term prospects. We remain Underweight tactically, but Overweight strategically on the prospect of higher income returns.

Fixed Income	Tactical view	Strategic view	Comments
EM Local Currency Debt			Peak US rates and better inflation fundamentals have allwoed EM local currency to stage a decent rally in 2023. But EM rate cuts are now also largely priced in and near-term returns are likely to be unexceptional. We suggest tactically neutral. Over a longer horizon, though, high income return potential and further convergence of inflation with DMs keep us strategically overweight.
EM USD Debt			Tighter spreads and weakening activity at G3+China keep us cautious. But these concerns are balanced by historically wide yield levels and improvements in frontier market debt restructuring processes. We stay tactically Neutral. Stabilizing credit fundamentals and greater economic flexibility keep us strategically Neutral as well.

Source: BNY Mellon Investment Mangement GEIA, as of March 10, 2024.

Past performance is no guarantee of future results.

All investments involve risk, including the possible loss of principal. No investment strategy or risk management technique can guarantee returns or eliminate risk in any market environment.

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Equities are subject to market, market sector, market liquidity, issuer, and investment style risks, to varying degrees.

Bonds are subject to interest-rate, credit, liquidity, call and market risks, to varying degrees. Generally, all other factors being equal, bond prices are inversely related to interest-rate changes and rate increases can cause price declines. **Commodities** contain heightened risk, including market, political, regulatory, and natural conditions, and may not be appropriate for all investors. **High yield bonds** involve increased credit and liquidity risk than higher-rated bonds and are considered speculative in terms of the issuer's ability to pay interest and repay principal on a timely basis. Investing in **foreign denominated and/or domiciled securities** involves special risks, including changes in currency exchange rates, political, economic, and social instability, limited company information, differing auditing and legal standards, and less market liquidity. These risks generally are greater with emerging market countries. **Small and midsized company stocks** tend to be more volatile and less liquid than larger company stocks as these companies are less established and have more volatile earnings histories. **Currencies** are can decline in value relative to a local currency, or, in the case of hedged positions, the local currency will decline relative to the currency being hedged. These risks may increase volatility. **Alternative strategies** may involve a high degree of risk and prospective investors are advised that these strategies are appropriate only for persons of adequate financial means who have no need for liquidity with respect to their investment and who can bear the economic risk, including the possible complete loss, of their investment. The strategies may not be subject to the same regulatory requirements as registered investment vehicles. The strategies may be leveraged and may engage in speculative investment practices that may increase the risk of investment loss. Investors should consult their financial professional prior to making an investment decision.

DEFINITIONS

Japan (Nikkei 225): The NIKKEI 225 is an index that tracks the performance of the largest 225 companies traded in the Japanese market. **10Y UK Gilt** – Average yield of a range of UK government bonds all adjusted to the equivalent of a ten-year maturity. **Phillips Curve:** An economic theory that inflation and unemployment have a stable and inverse relationship. US **Consumer Prices (CPI) Index** measure of prices paid by consumers for a market basket of consumer goods and services. The yearly (or monthly) growth rate represents the inflation rate. The **10Y US Treasuries Average Yield** of a range of Treasury securities all adjusted to the equivalent of a ten-year maturity. The **CBOE VIX Index (VIX)** is an indicator of the implied volatility of S&P 500 Index as calculated by the Chicago Board Options Exchange (CBOE). The **Majors Dollar Index (USD)** measures the value of the US dollar relative to a basket of currencies of the most significant trading partners of the US including the euro, Japanese yen, Canadian dollar, British pound, Swedish krona, and Swiss franc. The **MSCI EM Index (Emerging Markets Equities)** tracks the total return performance of emerging market equities. The **S&P 500 Composite Index (S&P 500)** is designed to track the performance of the largest 500 US companies. **Europe STOXX 600** Index represents the performance of 600 large, mid and small capitalization companies across 18 countries in the European Union. **Bloomberg US Corporate High Yield:** covers the universe of fixed-rate, non-investment grade corporate debt in the US. **Bloomberg US Corporate Investment Grade:** designed to measure the performance of the investment grade corporate sector in the US **1-mth. 1-year forward swap:** the avg. interest rate for 1-mth. in 1-year forward. **GDP:** gross domestic product is the total monetary or market value of all the finished goods and services produced within a country's borders over a given time period. **Fed funds Rate:** the target interest rate for overnight lending and borrowing between banks. **Purchasing Managers Index (PMI):** An economic indicator derived from monthly surveys of private sector companies. A level above 50 indicates expansion compared to the prior month and below 50 contraction. Investors cannot invest directly in any index. **Soft landing:** a gradual and controlled economic slowdown, often aimed at preventing a recession or minimizing its impact. **Global Financial Crisis:** The severe economic downturn that began in 2007-2008, characterized by widespread banking failures, a collapse in housing markets, and subsequent global recession.

STATISTICAL TERMS

Skewness in statistics represents an imbalance and an asymmetry from the mean of a data distribution. In a normal data distribution with a symmetrical bell curve, the mean and median are the same. **Kurtosis** is a measure of whether the data are heavy-tailed or light-tailed relative to a normal distribution. That is, data sets with high/low kurtosis tend to have heavy/low tails, or outliers. **Probability-weighted mean** is similar to an ordinary arithmetic mean, except that instead of each of the data points contributing equally to the final average, data points are weighted by the statistical probability for a particular scenario outcome. **Duration** is a measure of a bond's interest-rate sensitivity, expressed in years. The higher the number, the greater the potential for volatility as interest rates change.

OTHER

QE: quantitative easing. **Fed:** US Federal Reserve. **ECB:** European Central Bank. **BOJ:** Bank of Japan. **BOE:** Bank of England.

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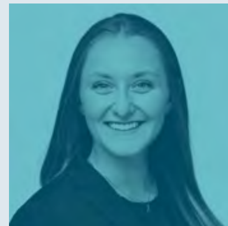

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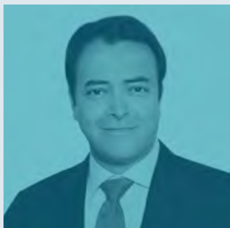

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