# Investment Strategy Insights

Monthly Views From Our Diverse Global Investment Teams

PineBridge® INVESTMENTS

June 2024

# A Rare Window of Growth Convergence Between the US and the Rest

**Hani Redha, CAIA,** Global Multi-Asset Portfolio Manager

Over the entire post-Covid period the US has experienced strong nominal growth, driven by an exceptional fiscal thrust and rapid immigration, while most other regions have struggled with weaker economic performance. This is nothing new; US growth has diverged from and outperformed other developed economies for decades, driven by a flexible and innovative economic foundation. US assets have outperformed even the nation's own economic outperformance, as a result of its unique sectoral composition and the quality of its equity market leaders. Yet on a cyclical basis, at least, this divergence is starting to narrow as the US economy moderates and other global economies gain momentum. This convergence has significant implications for investment strategies as the world adjusts to a more balanced phase of growth.

Outside of China, Asia's economy is thriving, primarily on the back of a robust recovery in exports fueled by increased demand from developed markets, particularly in the technology sector. Investment and domestic consumption are also recovering robustly, supported by a solid labor market. While inflation in most Asian economies has fallen within central banks' target ranges, the hawkish stance of the Fed is causing Asian economies to hold off on rate moves until the Fed acts. Nevertheless, we believe Asia's trade recovery has more room to grow, providing a buffer against the effects of tight monetary policy.

In China, after a pronounced period of weak growth, we are seeing a nascent cyclical recovery spurred by the conclusion of the global manufacturing recession for consumer goods and bolstered by China's fiscal measures. The potential property rescue plan appears to beat expectations, yet given the vast scale of China's property market, it remains insufficient to fully resolve the issue. We expect follow-up plans, along with a mini-dose of quantitative easing, to be announced at the significant July meeting, the third plenum. However, we do not envision this will be a monetary bazooka, as maintaining a reasonably firm yuan is still a policy objective. In the second half of the year, growth is likely to be driven by exports and increased fiscal spending, with full-year GDP growth close to 5%.

Similarly, as we have been expecting, Europe is displaying signs of a cyclical recovery, with the manufacturing purchasing managers' index (PMI) improving by 5 points since its trough and the service PMI remaining comfortably above 50. Real wages are also improving as inflation comes down, which should support consumption once households rebuild their balance sheets to a more comfortable level. Easing of monetary policy is expected to begin in June, yet fiscal tightening in response to EU requirements could be a modest drag. Nonetheless, improving industrial demand and a potential pickup in China's economy will support European growth for the rest of the year.

In contrast, we are (finally) seeing signs of a slowdown in the US. Consumers are becoming more cautious, focusing on essentials and services while reducing discretionary spending – a trend reflected in weaker retail sales and declining consumer confidence. Low-income consumers, in particular, are struggling with dwindling savings and high prices. The US labor market is softening, as evidenced by lower payroll numbers, weaker wage growth, and a slight increase in unemployment rates.

In sum, we see a moderate convergence of economic conditions globally. The US is normalizing from exceptionally strong growth drivers like excess savings and robust fiscal and labor conditions, while other regions are gradually improving. It is unlikely that US growth will fall off a cliff, or that the rest of the world will experience an explosion in growth. Instead, we are witnessing a moderate normalization in both directions. This should not be mistaken for a structural shift – we firmly believe in continued US exceptionalism over the medium term – yet this rare window of growth convergence offers a welcome opportunity to diversify investment portfolios without sacrificing return potential.

### About This Report

PineBridge believes that not only do differences of opinion make markets, but they also foreshadow substantial moves ahead as these differences are resolved. Once a month, investment leaders from our global multi-asset, equities, and fixed income teams meet to share their diverse viewpoints. This report reflects those discussions and debates by providing insight on the topic of the month along with snapshots of our asset class views and convictions across the firm.

# Conviction Score (CS) and Investment Views

The Conviction Scores shown below reflect the investment team's views on how portfolios should be positioned for the next six to nine months. 1=bullish, 5=bearish, and the change from the prior month is indicated in parentheses.

## Global Macro

**Ilke Pienaar**
Head of Sovereign Research, Global Emerging Markets Fixed Income

CS 2.75 (unchanged)

Contrary to expectations, the US economy lost momentum in the first quarter. Government expenditures and export growth slowed significantly, while retail sales growth trended lower and manufacturing remained in contractionary territory. Slower momentum in credit growth coupled with the savings rate sitting below its long-term average — amid no expectations of a reacceleration of growth in government spending — underlie the view that the economy will continue its gradual slowing. While the economy's pace is still far from recessionary and immigration has provided a lift, the fall in productivity growth suggests a below-potential pace.

Upward surprises in inflation are expected to fade as increases in insurance premiums normalize and home prices start aligning with rental surveys. Durable goods prices are deflating at the fastest pace in 20 years, showing that underlying pricing power is weak outside of services. Against this backdrop, the Consumer Price Index should reach close to 2% in the first quarter of 2025.

Due to the slower growth, equities markets are again pricing in two cuts for the year (up from one cut last month), with the likely start date sometime between September and November, which is now later than previously anticipated since sufficient evidence of lower inflation would be available only after the Federal Reserve's July meeting. With all big central banks save for the Bank of Japan set to ease this year, and helped by sideways to more stimulatory fiscal policy, global growth has generally come in stronger than expected. In fact, the global purchasing managers' index (PMI) is in expansionary territory for the first time since mid-2022. European growth, except for Germany, also has bottomed and has commenced an upward trajectory, however mild.

## Rates

**Gunter Seeger**
Portfolio Manager, Developed Markets Investment Grade

CS 3.25 (+0.25)

While the Federal Reserve attempts to balance a rapidly slowing economy with stubbornly persistent inflation, market participants are recognizing that inflation may continue to be problematic. This new backdrop of higher rates for longer will ultimately change the calculus for risk assets. We recognize the problem and believe that government spending without commensurate tax hikes will be detrimental for risk assets in the future. But that future is not now. This is an election year, and the current administration is doing everything in its power to lower prices and relieve the financial stresses that consumers face.

## Credit

**Steven Oh, CFA**
Global Head of Credit and Fixed Income

CS 3.50 (+0.25)

After a surprising rise at the start the year, the most recent inflation data was closer to expectations as economic data and sentiment turned bearish. The net impact was a rally in base rates and some marginal compression in already tight spreads. Yields declined for fixed rate credit, largely driven by rates, as the five-year part of the curve rallied by nearly 30 basis points (bps). Investment grade (IG) spreads are approaching +80 levels once again while high yield (HY) spreads have dipped below +300. The BB-BBB differential is below +70, representing a highly bullish credit market outlook. While floating-rate credit superficially looks much cheaper, with a majority of issues offered above par, negative convexity and repricing activity is in full swing. While strong technical demand and starting point fundamentals should keep spreads from widening meaningfully anytime soon, the tight valuations have led us to downgrade our CS to an incrementally more cautious bias.

## Currency (USD Perspective)

**Anders Faegermann**
Senior Sovereign Portfolio Manager, Emerging Markets Fixed Income

CS 3.00 (unchanged)

An environment of higher US rates for longer, which markets now anticipate, typically means lower risk appetites and investors demanding US dollars as a safe haven. Fed Chair Powell has taken the sting out of that outlook by saying the Fed is unlikely to raise interest rates one more time in this cycle, refocusing the market on the potential for one or two cuts in 2024 and further cuts next year as the Fed's expectations of inflation falling toward its 2% target are met. In addition, the slow improvement seen in recent US economic data suggests that the factors driving the US dollar higher in the first quarter could be fading. Perceived policy divergence, terms of trade, and ongoing US exceptionalism have been strong factors in support of a stronger US dollar versus the euro, yet the euro/US dollar ratio, which has stayed shy of testing the 1.05 level, would be considered appropriate in a "higher for longer" scenario. Long-term valuations and market positioning also have weighed on the US dollar, affirming our decision to move our conviction score to neutral last month. Should the euro/US dollar ratio be cemented in its 1.05-1.10 range, foreign exchange (FX) volatility could dampen further. We believe the European Central Bank (ECB) now has a clearer path to cut interest rates three or four times over the next 12 months, starting in June. Inflation is moderating, and while parts of the eurozone see signs of recovery, Germany and France are lagging.

## Emerging Markets Fixed Income

**Chris Perryman**
Corporate Portfolio Manager and Head of Trading, Emerging Markets Fixed Income

**USD EM (Sovereign and Corp.)**
CS 3.00 (unchanged)

**Local Markets (Sovereign)**
CS 2.50 (unchanged)

Recent and pending elections may affect markets in India, Mexico, and South Africa. In India, our base case is that Prime Minister Narendra Modi and his party win a third term, implying policy continuity and growth expectations of 6.5% over the medium term. In Mexico, the election of Claudia Sheinbaum as president gives a slightly more negative feel, with AMLO potentially still having policy influence as he stays on as leader of Morena party. In South Africa, the African National Congress (ANC) received just 40% of the vote and will enter into a coalition government. We place a higher risk than the market on a more extreme coalition being formed.

Regarding US dollar strength, we see the FX channel as the main transmission mechanism of US rate moves to emerging market (EM) sovereigns, requiring EM central banks to be cognizant of dollar strength in their policy decisions. Decoupling requires a weak or stable dollar environment to avoid FX depreciation; otherwise it would create domestic inflationary pressures for EMs, thus undermining any rate cuts. FX pass-through to inflation will vary across countries but remains a key component in central bank reactions. Latin American currencies and rates are most sensitive to significant US rate moves. In Asia, the rising cost of funding and FX risks are negatives for credit fundamentals, but a majority of issuers in our coverage universe will be resilient in withstanding the potential headwinds. In corporates, the story is more mixed in terms of the impact from USD strength. We have maintained our global macro scenario weightings.

## Multi-Asset

**Deanne Nezas**
Portfolio Manager, Global Multi-Asset

CS 2.50 (-0.30)

US inflation was surprisingly strong in the first quarter, pushing up interest rates and stalling the equity rally. Importantly, the reacceleration of inflation appears to be only partly due to demand strength. Supply strength, on the other hand, appears more durable. All told, the uptick in inflation appears to have little to do with domestically generated inflationary pressures, and the contributing factors don't appear to have much staying power. Eras of supply-led growth are disinflationary by nature and good for growth – both of which create a healthy backdrop for financial assets.

Interest rates have been pressured higher by a strong investment appetite as savings dwindle despite higher rates. A widening fiscal deficit has also added to these pressures. Aggressive spending in 2023-2024 as a result of several 10-year appropriations, including the IRA and CHIPS Acts, is largely responsible for the deficit widening as the economy gained steam. Any easing in the pace of Treasury issuance to fund the expanding deficit would be an upside surprise.

Liquidity is fungible and is about to become more generous. While the Fed's policy rate cuts will likely be delayed until year-end, the Fed is moving ahead in tapering the pace of QT, which is one form of easing. Outside the US, the Bank of Japan — while finally ending yield curve control and raising short-term rates — continues its quantitative easing by holding liquidity instead of tightening, which had been expected. The People's Bank of China at long last is beginning a modest dose of QE, and the European Central Bank has become quite clear that it will not wait for the Fed and will begin easing in June. With growth proving resilient, earnings inflecting higher, and liquidity about to become more generous, we became more constructive mid-May and began adding risk to reflect a CS of 2.5.

## Global Equity

**John Song**
Analyst, Global Equities

CS 3.00 (unchanged)

Equity markets have experienced volatility due to the uncertainties around Fed monetary policy as economic datapoints have become mixed. Although the latest Fed meeting suggests a higher-for-longer scenario due to persistent inflation, the possibility of further rate hikes has been dismissed, which has provided some relief to markets. Earnings in the first quarter have been mixed but are trending in a positive direction outside of the software and services sector, which is seeing persistent weakness in IT spending. Industrials and autos remain challenged, but many of these companies are becoming more constructive and are calling for a better second half. In other sectors, first-quarter earnings point toward continuing improvement in end demand, though the recovery appears shallower than expected. AI-exposed hardware remains a standout, exhibiting the strongest trends, with the outlook further upgraded by increased capex guidance from major hyperscale companies. Consumer companies continue to progress steadily, though caution is warranted due to weakening payroll and consumer confidence indicators.

## Global Emerging Markets Equity

**Taras Shumelda**
Portfolio Manager,
Global Equities

CS 2.50 (unchanged)

EM equities are up 14.6% since the lows of January amid only minor positive earnings revisions. The index is now at a small premium to its forward price/earnings (P/E) ratios. To generate more upside, investors would need to see further earnings gains or risk-on drivers such as US rate cuts.

In China, the index's 23% rally off the year's lows puts it broadly in line with its own historical forward P/E. Investors are rapidly closing the underweight, but the next leg of outperformance will require earnings-per-share (EPS) upgrades. The government recently announced more details in support of the auto and property industries. Domestic consumption demand remains tepid, but high-frequency data suggest overall stabilization. In India, equity markets have been betting on a return of the ruling party after the elections and for the momentum of infrastructure spending and structural reforms to pick up.

In Latin America, first-quarter earnings in Brazil have been mixed but show improvement over fourth-quarter results. Of note is the strength in healthcare, metals, and consumer but weakness in telecoms and utilities. In Mexico, results have been good, with more beats than misses. In EMEA, reports are just starting to flow in. Results thus far have been stronger than forecast in financials but lagging in food retailers due to competition.

Investors exhibit low conviction in bottom-up fundamentals, which is nonetheless an improvement compared with the heavily top-down and sentiment-driven behavior seen in previous months. Geopolitical and macro factors continue to play a large role, but one that is gradually diminishing. In our investment decisions, we try to look as much as possible past such factors and focus on companies with strong and improving business models, quality management, sound financial structure, and proper adherence to ESG values.

## Quantitative Research

**Haibo Chen, PhD**
Portfolio Manager and
Head of Fixed Income
Quantitative Strategies

Our US Conviction Score improved, driven by credit spread tightening of 3 bps and curve steepening of 4 bps. Global credit forecasts are negative, and our relative model favors EM over DM. In DM, industries the model favors are banking, capital goods, and finance companies; it dislikes utilities and communications. Among EM industries, the model likes infrastructure, oil and gas, and metals and mining; it dislikes real estate, transportation, and diversified companies. Our global rates model forecasts lower yields and a steeper curve globally. The rates view expressed in our G10 model portfolio is overweight global duration, North America, Belgium, Italy, Spain, and Japan. It is underweight France, Germany, and Oceania. Along the curve, it is overweight in the two-year and 20-year and underweight in the five-, 10-, and 30-year.

All market data, spreads, and index returns are sourced from Bloomberg as of 27 May 2024.

## About PineBridge Investments

pinebridge.com

PineBridge Investments is a private, global asset manager focused on active, high-conviction investing. We draw on the collective power of our experts in each discipline, market, and region of the world through an open culture of collaboration designed to identify the best ideas. Our mission is to exceed clients' expectations on every level, every day. As of 31 March 2024, the firm managed US$168.2 billion across global asset classes for sophisticated investors around the world.

**MULTI-ASSET | FIXED INCOME | EQUITIES | ALTERNATIVES**


PineBridge Investments is a group of international companies that provides investment advice and markets asset management products and services to clients around the world. PineBridge Investments is a registered trademark proprietary to PineBridge Investments IP Holding Company Limited.

**Readership:** This document is intended solely for the addressee(s) and may not be redistributed without the prior permission of PineBridge Investments. Its content may be confidential, proprietary, and/or trade secret information. PineBridge Investments and its subsidiaries are not responsible for any unlawful distribution of this document to any third parties, in whole or in part.

**Opinions:** Any opinions expressed in this document represent the views of the manager, are valid only as of the date indicated, and are subject to change without notice. There can be no guarantee that any of the opinions expressed in this document or any underlying position will be maintained at the time of this presentation or thereafter. We are not soliciting or recommending any action based on this material.

**Risk Warning:** All investments involve risk, including possible loss of principal. If applicable, the offering document should be read for further details including the risk factors. Our investment management services relate to a variety of investments, each of which can fluctuate in value. The investment risks vary between different types of instruments. In making an investment decision, prospective investors must rely on their own examination of the merits and risks involved.

**Performance Notes:** Past performance is not indicative of future results. There can be no assurance that any investment objective will be met. No investment strategy or risk management technique can guarantee returns or eliminate risk in any market environment. PineBridge Investments often uses benchmarks for the purpose of comparison of results. Benchmarks are used for illustrative purposes only, and any such references should not be understood to mean there would necessarily be a correlation between investment returns of any investment and any benchmark. Any referenced benchmark does not reflect fees and expenses associated with the active management of an investment. PineBridge Investments may, from time to time, show the efficacy of its strategies or communicate general industry views via modeling. Such methods are intended to show only an expected range of possible investment outcomes, and should not be viewed as a guide to future performance. There is no assurance that any returns can be achieved, that the strategy will be successful or profitable for any investor, or that any industry views will come to pass. Actual investors may experience different results.

Information is unaudited unless otherwise indicated, and any information from third-party sources is believed to be reliable, but PineBridge Investments cannot guarantee its accuracy or completeness. All information is sourced from PineBridge Investments unless otherwise noted.

This document and the information contained herein does not constitute and is not intended to constitute an offer of securities or provision of financial advice and accordingly should not be construed as such.

The securities and any other products or services referenced in this document may not be licensed in all jurisdictions, and unless otherwise indicated, no regulator or government authority has reviewed this document or the merits of the products and services referenced herein. This document and the information contained herein has been made available in accordance with the restrictions and/or limitations implemented by any applicable laws and regulations. This document is directed at and intended for institutional and qualified investors (as such term is defined in each jurisdiction in which the security is marketed). Before acting on any information in this document, prospective investors should inform themselves of and observe all applicable laws, rules and regulations of any relevant jurisdictions and obtain independent advice if required.

Where applicable, the Manager may determine to terminate any arrangements made for marketing the Shares in one or more jurisdictions in accordance with the AIFM Directive and UCITS Directive respectively, as may be amended from time to time. Investors and potential investors can obtain a summary of investor rights and information on access to collective redress mechanisms at www.pinebridge.com/investorrights.

**Certain Geographic Disclosures:**

**Australia:** PineBridge Investments LLC is exempt from the requirement to hold an Australian financial services license under the Corporations Act 2001 (Cth) in respect of the financial services it provides to wholesale clients, and is not licensed to provide financial services to individual investors or retail clients. Nothing herein constitutes an offer or solicitation to anyone in or outside Australia where such offer or solicitation is not authorised or to whom it is unlawful. This information is not directed to any person to whom its publication or availability is restricted.

**Bermuda:** PineBridge Investments Asia Limited is registered as a Class A Registered Person with the Bermuda Monetary Authority pursuant to the Investment Business Act 2003 (as amended).

**Hong Kong:** The issuer of this document is PineBridge Investments Asia Limited, a company incorporated in Bermuda with limited liability, licensed and regulated by the Securities and Futures Commission (SFC). This document has not been reviewed by the SFC.

**Malaysia:** PineBridge Investments Malaysia Sdn Bhd is licensed and regulated by Securities Commission of Malaysia (SC). This material is not reviewed or endorsed by the SC.

**Singapore:** PineBridge Investments Singapore Limited is licensed and regulated by the Monetary Authority of Singapore (MAS). In Singapore, this material may not be suitable to a retail investor. This advertisement or publication has not been reviewed by the MAS.

**Taiwan:** PineBridge Investments Management Taiwan Ltd. Is licensed and regulated by Securities and Futures Bureau of Taiwan (SFB). In Taiwan, this material may not be suitable to investors and is not reviewed or endorsed by the SFB.

Last updated 7 February 2024. For additional legal and regulatory disclosures including other cross border information, please refer to https://www.pinebridge.com/en/regulatory-disclosure.