Looking back, looking forward
2024-25
Looking back, looking forward

1. **2024 a crowded political year** with households and firms likely to adopt a wait-and-see approach and postpone key economic decisions from large purchases to major investments.

2. **Soft landing in the US and muddling through in the Eurozone** with increasing risks of prolonged technical recession for the latter in H1 2024.

3. **Disinflation is gaining traction** and central banks should pivot earlier than expected (summer 24) but later than market expectations as it takes time to cool down a ‘hot’ labor market.

4. **Fiscal safety nets unwinding in Europe**, Germany not to the rescue amid budget woes, US fiscal consolidation underwhelming.

5. **Global trade is set to rebound modestly after 2 consecutive years of below-average global GDP growth**. The rebound will be led by Europe emerging from trade recessions and Asian countries (ex-China) still benefiting from the reshuffle in global value chains.

6. **The Chinese consumer didn’t save the day** but China increases its influence abroad through investment while increasing its policy support to fight a distressed property market and muted consumer confidence.

7. **Emerging markets**: re-emerging on lower rates, weaker dollar, lower twin deficits and friend-shoring. Selectivity key as some countries still struggle (Egypt, Argentina or Ghana).

8. ** Corporates digesting higher yield environment** with risks concentrated on real estate, retail, utilities

9. **Capital markets: rates struggle between policy pivot and supply** amid large deficits and central bank quantitative tightening, volatility to decrease as rate pivot approaches. The recovery of risky assets will be put to the test as the AI frenzy cools and some of the anticipated cuts do not materialize (esp. Eurozone)

10. **Financial cracks under the surface and liquidity squeeze to continue adding pressure on corporate spreads**. But risks will not materialize systemically as central bank policy becomes accommodative
Global Macro & Corporate Outlook
2024-2025
Upcoming super election year increases political volatility and uncertainty

<table>
<thead>
<tr>
<th></th>
<th>Q1 2024</th>
<th>Q2 2024</th>
<th>Q3 2024</th>
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<td>United Kingdom, parliamentary (Oct)</td>
<td>US presidential &amp; parliamentary (Nov)</td>
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<td></td>
<td>• Portugal, parliamentary (Mar)</td>
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</table>
**Global Outlook**

Soft landing is still our baseline for 2024

We expect most developed markets to grow below trend in 2024

Output gaps suggest there is no spare capacity left in China and the Eurozone (HP output gap, %)

Sources: LSEG Datastream, Allianz Research
Sidestepping the recession

## Global real GDP growth (%)

<table>
<thead>
<tr>
<th>Growth (yearly %)</th>
<th>2021</th>
<th>2022</th>
<th>2023f</th>
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</table>

## Subdued growth ahead

Quarterly real growth rates (q/q %)

*Dotted lines are AZ Research forecasts

Sources: LSEG Datastream, Allianz Research
Timid rebound in global trade in 2024

Europe & APAC to lead the rebound in 2024

Forecasted export gains in 2024, by country

Sources: UNCTADstat, Allianz Research
Ongoing disinflation

<table>
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<tr>
<th>Inflation (yearly %)</th>
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</tbody>
</table>

Approaching central bank targets in 2024
Quarterly inflation rates, y/y%

Sources: LSEG Datastream, Allianz Research
Oil price weighed down by demand, but electricity prices elevated in Europe

Global Outlook

- Oil to remain expensive
  - Brent prices, USD/bbl

- Electricity prices should not decrease much in 2024 in Europe
  - Wholesale prices, USD/MWh

Sources: LSEG Datastream, Allianz Research

Sources: IEA, Allianz Research
From goods deflation to services disinflation

Producer price deflation, notably in China and Germany

Producer price index, y/y %

Services inflation will take time to slow

Core services inflation, y/y %

Sources: LSEG Datastream, Allianz Research
Labor market rebalancing starting to feed through to lower wage growth

Labor market imbalances moderate but remain above pre-pandemic levels

((Job openings + Employment) / Labour force) - 1

- Nominal wage growth shows signs of turning around

Indeed wage tracker on newly hired employees, % y/y

Sources: LSEG Datastream, national sources, Allianz Research

Sources: Indeed, Allianz Research

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Businesses and consumers’ price expectations normalizing

Businesses’ selling prices at or close to pre-pandemic level
(Composite PMI output prices, index)

Consumers’ short-term inflation expectations are off their highs (Germany/France = balance of opinion)

Sources: LSEG Datastream, Allianz Research
Consumers get some relief from positive real wage growth, but precautionary savings remain high.
Bank interest rates seem to have peaked in the US

Mortgage interest rates started to fall in the US, %

Bank rates to business don’t show signs of cooling, %

Sources: LSEG Datastream, Allianz Research
High rates constraint loan growth, mainly for firms

The US leads the cycle of consumer credit with delinquencies rising to their highest level since 2020, y/y, %

Credit growth to firms has taken a toll since the start of 2023, y/y, %

Sources: LSEG Datastream, Allianz Research
Monetary policy transmission: more delayed in Europe compared to the US

The transmission of monetary policy to bank rates has been higher in the US than in Europe, bp

Impact of monetary policy, pp of gross disposable income

- Up to date monetary policy transmission
- Remaining transmission
- y/y increase as of Q2 2023
- 2019 average increase

Sources: LSEG Datastream, Allianz Research
**Global Outlook**

*Timid pivots in policy rates to start mid-2024*

Central banks will start cutting rates in summer 2024 amid weak growth and ongoing disinflation

Quantitative tightening will continue in the Eurozone whereas the Fed is expected to stop in mid-2024

---

**Graphs:**

1. Fed Funds rate, high (%)
2. ECB deposit rate (%)
3. BoE policy rate (%)

*Numbers refer to end of 2023, 2024 and 2025 forecasts*

---

Sources: LSEG Datastream, Bloomberg, Allianz Research

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Fiscal policy turning mildly restrictive

German budget dispute turns fiscal spending more restrictive
(budget and structural balance as % of GDP)

Fiscal policy adjustments will be only gradual
(cyclically adjusted primary balance, % of GDP)

Sources: German Government, LSEG Datastream, Allianz Research Notes: The adjusted forecast counts in the ruling of the German constitutional court in November 2023, which led to a budget dispute for the 2024 household and will lead to a return to the debt brake starting from 2024.

Sources: LSEG Datastream, IMF, EC AMECO, Allianz Research
Corporates are burning cash

Revenue growth for industrial companies, y/y

- Spain
- Germany
- France
- Italy
- US

Cash deposits of non-financial corporates, y/y

- UK
- Germany
- France
- Italy
- Spain

Sources: LSEG Datastream, Allianz Research
Business insolvencies: Normalizing at a high speed

North America and Europe are leading the global rebound, selected countries

Strongly increasing (+30% and more)
- Brazil
- Estonia
- Italy
- Japan
- Ireland
- US
- Poland
- South Korea

Noticeably increasing (+15% to +30%)
- Chile
- Turkey
- Lithuania
- Australia
- France
- Germany
- Luxembourg
- New Zealand
- Norway
- Portugal
- Canada
- Finland
- Hungary
- UK
- Sweden

Increasing (0% to +15%)
- India
- Latvia
- Colombia
- Czechia
- Slovakia
- Austria
- Belgium
- Bulgaria
- Switzerland
- Romania
- Denmark
- Morocco
- Spain

Decreasing
- China
- Russia
- Singapore
- South Africa
- Taiwan
- Hong Kong

Still higher levels to expect in most countries and regions in 2024, index 100 = 2019

Sources: national sources, Allianz Research

GLOBAL OUTLOOK
Financial institutions are better prepared to absorb shocks, but watch out for unrealized losses

Banks are better capitalized compared to 2015 and able to absorb shocks...

Tier 1 ratio (%)

US    EZ    UK

...but bond owners lost 12 trillion USD in book value since 2021 (realized or unrealized)

Bloomberg Global Aggregate Bond Index (trillion USD)

Sources: LSEG Refinitiv, Allianz Research. Note: The figures refer to G-SIBs: global, systemically important banks.
GLOBAL OUTLOOK

Beware of hidden financial risks as maturity wall looms and higher interest rates start to bite

Bond redemptions in the next couple of years complicate the landscape
share* of IG corp. debt maturing in the next 3 years

Higher interest rates start to bite NFCs balance sheets – disproportionally affecting more the smaller ones
Interest coverage ratios*, by market cap

Sources: LSEG Datastream, Allianz Research. Calculated based on bond index values, where the average maturity of USD corporate bonds (11Y) is 5 years larger than for EUR (6Y).

Sources: LSEG Refinitiv, Allianz Research
*ICR is calculated as EBIT divided by net interest expenses, the higher the better

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Systemic stress is easing but more leveraged sectors in the spotlight amid higher interest rates

Systemic financial stress eases

Highly indebted Real Estate & Renewable Energy sectors at risk of investment slowdown amid rising interest rates

Note: summarizes 15 individual financial stress indicators (banking ratios, volatility measures etc.) from different market segments (FX, bonds, equity, money markets etc.), see ECB working paper for details.

Source: LSEG Datastream; Allianz Research

Size of bubble indicates % of debt maturing in 1Y
Sources: Bloomberg, Allianz Research
Markets are discriminating against real estate and renewable energy

Real estate companies in trouble
Additional spread from real estate IG companies (vs. corp. credit IG benchmarks)

Valuations in alternative energy sector have also adjusted severely in the last year
Price returns rebased on 31/12/2019

Sources: LSEG datastream, Allianz Research.

Wind and solar companies in the US and Europe have the largest share in the index.

Sources: LSEG datastream, Allianz Research.
Real estate: office segment in midst of the storm

US Commercial Real Estate Funding Gap
(5Y loans originated in 2018-2020, USD bn)

Office property value
(% change Q3 2023 – Q2 2022)

Sources: CBRE, Allianz Research

Sources: GreenStreet, Allianz Research
China is not a growth engine

Further rate cuts are warranted in Q1 2024 as CNY prospects improve but credit efficiency is low, % y/y

- Credit efficiency (ratio of yearly change in nominal GDP to yearly change in credit outstanding)
- Average

Infrastructure spending will remain the main fiscal tool

Local government special bonds issuance, bn RMB

Sources: Official Sources, Allianz Research
Global decoupling from China

The world dependency on China is hard to shake off but there are some growing alternatives

- Change in share exports to the US, relative to total US imports, pp
- Change in share of imports from China, relative to total imports, pp

Sources: UNCTADstat, Allianz Research

Sources: LSEG Refinitiv, Allianz Research
But China is increasing influence in external markets

China is a net investor abroad, mainly in the Asean and Latam countries, USDbn

China’s is contributing to US and EU improvements in trade balance, USDbn

Sources: national, Refinitiv, Allianz Research
Limited contagion from China to emerging markets, risks of balance of payment crisis moderated

Domestic issues have increased risk aversion in China, net portfolio flows (USD bn)

Current account improvements to remain in 2024; Asia and Middle East in most favorable positions (% of GDP, 4-quarter rolling average)

Sources: IMF, national statistics, Refinitiv, Allianz Research

* Q2 2023 for Colombia, India, Israel, Philippines, Saudi Arabia, South Africa and UAE
Markets in South-East-Asia and Africa re-emerging

Real GDP growth contributions, 2024, pp

Sources: National statistics, EIU, Refinitiv Datastream, Allianz Research

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Rising employment and wages are driving consumer spending in most emerging markets

Except for CEE, employment (index, Q4 2014 = 100, 4-q MA) has grown to record levels in EM regions

Wage growth (% y/y, 12-m MA) is particularly strong in CEE and Latin America
Tough decisions ahead in emerging markets due to costlier refinancing and politics

Cyclically-adjusted fiscal balance (% of GDP) and annual changes (pp of GDP)

Upcoming sovereign debt maturity (bars, lhs) over total outstanding debt vs. avg. coupons (dots, rhs)

Sources: IMF, Allianz Research

Calculated using among outstanding and current exchange rates. Only marketable debt, excludes loans and for (*) other type of arrangements. For POL, HUN, CZE & ROU the average coupon for hard currency issuances the EUR is taken as reference, otherwise the USD.

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EMs are early pivoters as pressure on FX faded

Widespread positive real policy rates (excl. Eastern Europe) as a sign of effective fight against inflation

Policy normalization has started but few will manage to cut as quickly as desired considering weak growth

EM central bank clusters

Sources: Refinitiv, Allianz Research. * Indonesia, Thailand and Philippines proceeded with minor 25bps hikes after June, the rest of countries in cautious pause have hold these rates for at least 5 months. Additional note: Middle-Eastern countries are not included as their monetary policy/currency regime is tied to that of the US.

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Geopolitics increasingly polarized and devoid of trust

- Europe's credibility and unity tested
- RU-UKR war likely turning into frozen conflict
- Middle-east tensions flaming up again
- Indo-Pacific / Taiwan tensions increasing
- Global South more visible and influential
- US-China strategic competition to stay
Uncertainty shocks act like a negative supply shock

Higher economic uncertainty across regions (Index 3-m MAV)

Policy uncertainty lowers output, fixed investment, and private consumption (pp)

Sources: Baker, Bloom and Davis (2016), Allianz Research

Sources: Mumtaz and Ruch (2023), Allianz Research Note: Cumulative impact of a one standard deviation increase in fiscal or monetary policy uncertainty. Results based on a structural panel vector autoregressive model with stochastic volatility for 54 economies including 32 advanced economies and 22 developing economies. Orange whiskers reflect the 16-84th percentile.
Regional outlooks
2023-2025
US growth cycle starting to turn down but private sector buffers limit downside risks

Delinquencies starting to pick up for consumer loans
% of loans delinquent

Household debt servicing remains very contained
Debt service % disposable income

Sources: Refinitiv Datastream, Allianz Research
Eurozone decoupling from US with risks tilted to the downside

Consumption and investment remain depressed in the Eurozone compared to the US (Index 2019=100)

After four quarters of stagnation, leading indicators signal no rebound soon

Sources: Datastream, Ameco, Allianz Research
German budget dispute forces to stay within budget undermining investment catch-up effect

GDP components (index 2015=100)

Government revenue and expenditure (y/y %)

Sources: Refinitiv Datastream, Allianz Research

Sources: Refinitiv Datastream, Allianz Research
France: growth will struggle through mid-2024

Monthly hard data showing broad-based weakness
Index, January 2023 = 100

Business investment braced for a slowdown amid lower credit demand

Sources: Refinitiv Datastream, Allianz Research
Italy: Consumers trying to save the day

Private consumption picked up slightly despite confidence remains at historically low levels...

...and higher interest rates have impacted credit growth (y/y, %)

Sources: Refinitiv Datastream, Allianz Research
Spain: Slowing but resilient

Strong momentum in tourism-related activities and more contact-intensive services has been key to growth...

Labor market resilience and easing price pressures support growth despite high interest rates

Sources: Refinitiv Datastream, Allianz Research
UK: Soft landing, but the runway is long

Wage pressures remain high in a number of sectors
Nominal wage growth, y/y

- LT average
- 2022
- Latest (Aug 2023)

Corporates are starting to revise their selling expectations prices on the downside, net balances

Sources: LSEG Datastream, Allianz Research
**China: Property sector stabilization efforts ongoing**

Chinese consumer confidence remains depressed

Sources: LSEG Datastream, Allianz Research. Y/Y evolution of prices across 91 Chinese cities.

Housing indicators in China point to a stabilization at low levels, % y/y

Sources: Official sources, Allianz Research
APAC: Weak global trade performance will jeopardize regional growth

GDP growth and short-term country risk as of Q4 2023

Sources: Allianz Research.

APAC exports remain in recession
Exports, % y/y

Sources: IMF, Allianz Research.
EM Europe: Growth to recover gradually in 2024-25, supported by rebalancing and monetary easing

GDP growth and short-term country risk as of Q4 2023

Rapid unwinding of current account imbalances (% of GDP, 12-m MA), slower in Romania and Turkey

Sources: Allianz Research

Sources: Datastream, Allianz Research
Crude oil production has decreased by 12 barrels per person in the region affecting overall revenues (Oil revenues, USD per person)
LatAm: Growth convergence; inflation will continue to ease

Outperformance of Brazil and Mexico to reduce

Fiscal consolidation remains Brazil's main challenge; Chile and Colombia more exposed to external shocks

<table>
<thead>
<tr>
<th></th>
<th>Brazil</th>
<th>Colombia</th>
<th>Chile</th>
<th>Mexico</th>
<th>Peru</th>
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<tbody>
<tr>
<td>Fiscal balance/ GDP*</td>
<td>-6.0%</td>
<td>-2.4%</td>
<td>-1.3%</td>
<td>-5.4%</td>
<td>-1.8%</td>
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<tr>
<td>Inflationary risk</td>
<td>CPI*</td>
<td></td>
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<tr>
<td></td>
<td>4.2%</td>
<td>5.8%</td>
<td>4.8%</td>
<td>5.5%</td>
<td>4.2%</td>
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<tr>
<td>Competitiveness</td>
<td>REER (deviation from the average of past 5 years)</td>
<td>4.6%</td>
<td>3.9%</td>
<td>4.1%</td>
<td>17.8%</td>
</tr>
<tr>
<td>Growth</td>
<td>GDP*</td>
<td></td>
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<tr>
<td></td>
<td>1.5%</td>
<td>1.5%</td>
<td>1.6%</td>
<td>2.0%</td>
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<tr>
<td>Domestic Credit Growth</td>
<td></td>
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<tr>
<td></td>
<td>8.8%</td>
<td>6.5%</td>
<td>1.9%</td>
<td>9.2%</td>
<td>7.0%</td>
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<tr>
<td>External Sector Ratios</td>
<td>External Debt/GDP</td>
<td>50.7%</td>
<td>68.4%</td>
<td>77.8%</td>
<td>55.0%</td>
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<tr>
<td></td>
<td>External Debt/ Exports</td>
<td>156.2%</td>
<td>241.1%</td>
<td>209.1%</td>
<td>90.4%</td>
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<tr>
<td></td>
<td>Public Debt/ GDP</td>
<td>90.3%</td>
<td>57.2%</td>
<td>41.2%</td>
<td>57.7%</td>
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<td>FX reserves (USD bn)</td>
<td>344.18</td>
<td>58.11</td>
<td>41.10</td>
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<td></td>
<td>CA/GDP*</td>
<td>-1.8%</td>
<td>-7.9%</td>
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<td>-1.4%</td>
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<td></td>
<td>Import Cover*</td>
<td>11.17</td>
<td>8.33</td>
<td>4.74</td>
<td>3.41</td>
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</tbody>
</table>

Sources: Allianz Research. *Forecast for 2024, otherwise last numbers.
Capital Markets Outlook

2023-2025
Markets to navigate the **policy-heavy environment**

### Capital Markets: Eurozone and US

#### Year-end figures

<table>
<thead>
<tr>
<th>Indicator</th>
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<th>2023f</th>
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<td></td>
<td></td>
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</tr>
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<td>ECB deposit rate</td>
<td>4.00 %</td>
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<td>3.50</td>
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<tr>
<td>10y yield (Bunds)</td>
<td>2.13 %</td>
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<td>2.40</td>
<td>2.30</td>
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<tr>
<td>Eurostoxx (total return p.a.)</td>
<td>20 ytd %</td>
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### Capital Markets: UK, Emerging Markets, FX

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<tr>
<td>BoE rate</td>
<td>5.25 %</td>
<td>3.50</td>
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<td>10y yield sovereign (Gilt)</td>
<td>3.79 %</td>
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<td><strong>Corporate Debt</strong></td>
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<tr>
<td>Investment grade credit spreads</td>
<td>134 bps</td>
<td>192</td>
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<td>130</td>
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<td>High-yield credit spreads</td>
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<td>525</td>
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<td>475</td>
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<tr>
<td>FTSE 100 (total return p.a.)</td>
<td>7 ytd %</td>
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<td>6</td>
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<td><strong>Emerging Markets</strong></td>
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<tr>
<td>Hard currency spread (vs USD)</td>
<td>231 bps</td>
<td>273</td>
<td>235</td>
<td>230</td>
<td>210</td>
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<td>Local currency yield</td>
<td>6.42 %</td>
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<td>MSCI EM (total return p.a. in USD)</td>
<td>7 ytd %</td>
<td>-20</td>
<td>6</td>
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<td><strong>Others</strong></td>
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<tr>
<td>EUR USD</td>
<td>1.10 $ per €</td>
<td>1.07</td>
<td>1.09</td>
<td>1.12</td>
<td>1.14</td>
</tr>
</tbody>
</table>

**Sources:** LSEG Datastream, Bloomberg, Allianz Research
Long-Term yields ease with monetary policy pivot but supply pressure curbs further drops

Sovereign bond yields to fall slightly on lower policy rates; Bunds look expensive against fair value

Sources: LSEG Datastream, Bloomberg, Allianz Research

Bond supply, QT and limited foreign demand to increase the share of rate sensitive investors

Sources: LSEG Datastream, Bloomberg, Allianz Research
Notes: Estimate before 2003
Volatility in bond markets to fade in 2024 when markets are clearer on future monetary policy path

Rates market volatility remains elevated as inflation uncertainty is replaced by monetary policy

Heightened volatility in the treasury market has only partially translated into corporate spreads volatility

Sources: LSEG Datastream, Allianz Research 
Note: (realized) volatility in US treasuries is computed as 30d standard deviation on observed values; (realized) inflation volatility is computed as 24m standard deviation on observed values.
ECB pivot and solid demand should support spreads going forward

Retail domestic investors have taken over the ECB buying Italian sovereign

Monthly Italian government bond flows (EUR bn)

Eurozone periphery spreads versus Germany to remain stable amid ECB pivot

Sources: LSEG Datastream, Allianz Research

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Japan struggling to exit negative interest rates in 2024 as signs of disinflation emerge

Lower inflation prints in Japan have eased speculation of a more restrictive BoJ policy stance

Policy rate, BoJ balance sheet and foreign investment

Sources: LSEG Datastream, Allianz Research
USD strength to retreat in the medium–run as ‘US exceptionalism’ fades

The USD is very expensive
(REER: deviation from LT average, in standard deviations)

Real transatlantic spread and EUR/USD (inverted)

Sources BIS, Datastream, Allianz Research.

Sources: LSEG Datastream, Allianz Research.
Credit remains tight given current macroeconomic conditions but should still be resilient in the mid-run.

Leverage ratios increasing but under control
(Net Debt to EBITDA; European corporates)

After some volatility in H1 (once uncertainty about cuts slowly fades), we expect spreads to start a gradual compression process.

Sources: Bloomberg, Allianz Research.
Sources: LSEG Datastream, Allianz Research.
Equities to feel the pain H1 as they await the dovish-turn confirmation and the type of landing

Dovish policy rate expectations have driven late-2023 rally but will remain a source of volatility – together with the modest economic growth.

Our scenario suggest low (~3-5%) price returns in 2024, exhibiting a U-trend during the year, which recovery should spill into 2025.
Concentration risk remains high in the US, but that will not impede the US outperforming again. Tech earnings are set to remain strong. Together with the different policy paths it will push US ahead of the EZ.

EPS growth expectations for 2024

Broader support from the rest of the market in H2 after a 2023 where its underperformance was hidden.

Sources: LSEG Datastream, Bloomberg, Allianz Research

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Besides peak Fed fund rates EM resilience was supported by relatively easier financial conditions.

Appetite for high returns and EM macro resilience supported an easing of spreads.

Subdued hard currency issuance also helped, as countries refrain from locking in higher coupons in USD*.

Changes since end-2021 in selected key metrics for HC bonds**

Sources: Bloomberg, LSEG Datastream, Allianz Research. Note: The EMBI HC spreads represent the JPM EMBI Gov Diversified ex-CCC. The EMBI LC yields represent the GBI EM Global Diversified. Financial conditions index by Chicago Fed, lowest since Q1 2022.

Sources: LSEG Datastream, Allianz Research. * For Eastern Europe countries & Morocco EUR indexes have been used. ** Average coupon, maturity and yield based on BofA sovereign debt indexes.
Diversification, a comeback to the post 2000s era or a structural shift?

The simultaneous equity-fixed income underperformance in 2022 will remain engraved in market sentiment...

Declining growth-inflation uncertainty and a comeback of demand-driven dynamics should bring diversification back

Sources: LSEG Datastream, Allianz Research

Sources: LSEG Datastream, AQR, Allianz Research