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Multi-Asset Solutions Strategy Report

Global markets and multi-asset portfolios

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In brief

- Macroeconomics are constructive globally; as inflationary pressures ease, central banks are showing flexibility in adjusting their policies.
- The cycle looks set to extend in the U.S. amid a strong labor market and sufficient household savings that also supports consumption growth.
- The euro area's growth momentum is faltering, however, supporting our relative underweight euros vs. the U.S. dollar.
- In China, a shift toward aggressive monetary easing and further expected fiscal measures should continue supporting growth—as previous stimulus likely produced September's slightly better than expected activity data.
- Our portfolio positioning favors U.S. large cap equities, particularly in AI sectors; emerging market equities, especially in Asia because of tech goods demand and China's stimulus; and euro-area fixed income, specifically Italian government bonds.

Our outlook for the global economy remains constructive despite regional and sectoral imbalances. Several recent developments in the U.S. and China suggest the global expansion is likely to stay on solid footing.

The U.S.: An extension of the economic cycle

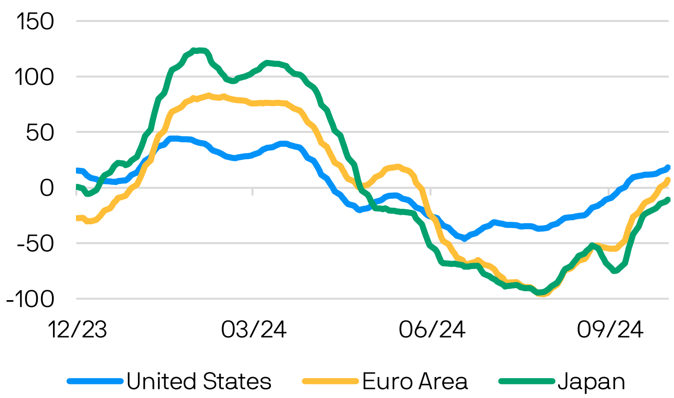
Our base case expects U.S. growth to gradually slow to a trend-like pace of around 2%, providing scope for the cycle to extend. Stronger than expected data in recent weeks—indicating a healthier labor market and a higher savings buffer than seemed to be the case before—has prompted us to reduce our view of the probability of a U.S. recession in the next 12 months. We lower it to 15%, from 20%.

The sharp slowdown in U.S. labor demand around mid-2024 presented a key risk to U.S. economic expansion. Although we did not observe clear signs that a negative feedback loop had begun between job losses and reduced spending, the risks to the U.S. labor market were skewed to the downside. Since then, however, a solid September payrolls report, and upward revisions to previous months' labor data, indicate a reversal in the downward trend in U.S. labor demand. The three-month moving average of nonfarm payrolls improved to 186,000 (from 140,000) in September, and real payroll earnings are growing at about 2.5% year-over-year (y/y). We see sufficient momentum in labor demand to sustain solid consumption growth.

U.S. income and the personal savings rate data have also been revised upward recently—a sign that household savings, a buffer against a consumer spending squeeze, appears higher than previous estimates. Our estimates now suggest that the households have built up excess savings equal to 5% of GDP. While that is below the pre-pandemic average of around 6%, households have strong balance sheets: The ratio of net worth to disposable income remains elevated. In short, a variety of positive U.S. data releases have outstripped those in other regions (**Exhibit 1**).

On a relative basis, recent U.S. data have consistently outperformed other regions

Exhibit 1: Data surprises, U.S. vs. Europe and Japan



Source: Citi, Bloomberg, J.P. Morgan Asset Management; data as of October 29, 2024.

China: A clear shift to aggressive monetary easing

In late September, China clearly and decisively shifted from modest, reactive easing to a more aggressive and coordinated approach to policy easing. On September 24, the People's Bank of China rolled out a set of monetary easing measures. Two days later a Politburo meeting, a gathering not usually reserved for economic discussions, sent a very clear dovish signal, calling for proactively stepping up counter-cyclical monetary and fiscal policy easing, to achieve the 5% annual economic growth target.

A coordinated policy has been building over the past few weeks. Further easing measures have been announced—monetary, fiscal and in the property markets. The measures have prompted us to revise up our annual GDP growth forecast for China, to 4.9% y/y in 2024, from 4.7% previously. However, the size of the stimulus measures announced so far is broadly in line with market expectations. The measures seem intended to put a floor under growth and to reduce downside risks for the Chinese economy, especially when it comes to property and local government finances.

September's set of major activity indicators for China came in slightly better than expected, in part reflecting the impact of previous easing measures. (The newest measures' impact may not be felt for some time.) Other areas of the economy without policy support (household consumption outside of appliances, for example) continued to show sluggish growth momentum. Most property-related indicators remained in double-digit y/y contraction, suggesting the limited effectiveness of previous rounds of property sector easing.

We believe more fiscal easing is needed to support growth amid subdued private sector sentiment. We are waiting for more details on the fiscal measures – likely to be announced in early November during the National People's Congress Standing Committee meeting – before we more fully assess their impact on growth. Should the central government support the property sector in more meaningful ways, that would be an upside risk to our base-case growth forecast. A significant external shock, such as a major increase in U.S. tariffs on Chinese goods, would also likely lead to additional policy support.

Europe: The weak link

Meanwhile, the euro area remains a weak link in the global economy. After a strong start to the year, growth momentum faltered in the second quarter. The October flash PMI readings point to lackluster growth momentum, aligned with sub-1% annual GDP growth for the region. We expect a gradual recovery in consumer spending, driven by rising real incomes, although households are likely to remain relatively cautious. The euro area also faces external headwinds—both from stronger competition with

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Chinese exports and weaker Chinese import demand that will likely weigh, in turn, on business investment.

Asset class implications

We continue to favor euro area fixed income, driven by strong evidence of disinflation and the absence of a broad-based recovery in growth, particularly in Germany. Services inflation, while a risk, remains soft and wages are coming down slowly. The latest European Central Bank (ECB) meeting showed a willingness to be flexible and policymakers have now moved to data dependent, meeting-by-meeting rate cuts. We see this dovish shift as supportive of our preference for European duration.

We are positioning for these macro conditions through a positive view on Italian bonds, BTPs,[1] rather than using German Bunds to collect carry. Expectations of further ECB policy easing, strong investor demand and low political volatility are supportive factors for BTPs. Political instability in France is a risk factor but this is offset, in our view, by a proactive ECB supporting fixed income through rate cuts. Italy's credit ratings are expected to remain stable with a positive outlook, according to recent major rating agency reviews. Strong demand for BTPs from institutional and retail investors should support prices especially as issuance drops off at year-end. We do not foresee significant spread tightening in BTP vs. Bund spreads, but find the BTPs' carry to be attractive given the macro backdrop.

On a relative basis, U.S. growth has consistently outperformed the euro area this year and recent data releases point to further divergence. To us, this implies more rate cuts from the ECB than the Federal Reserve. Taken together, rate and growth differentials support a weaker euro vs. the U.S. dollar. This—added to the event risk around the U.S. elections—lends further support to our underweighting the euro.

We also expect to see the euro weakening vs. the Japanese yen, based on our view that the Bank of Japan (BoJ) will continue raising the policy rate, in the context of a relatively resilient Japanese economy. While there are reasons BoJ policy normalization may be prolonged, we still see rates rising in Japan, while they are expected to fall in the euro area. Japan is also at the early stages of a virtuous cycle of rising inflation expectations and rising wages. On the other hand, the euro area economy has already passed this reflation and is now facing multiple cyclical and structural headwinds to growth. We are therefore more positive on the yen and prefer positioning for JGB yields to rise relative to European government bonds.

Our increased confidence in business cycle extension and lower recession risks keeps us overweight equities. Growth and policy divergences across regions provide us with relative-value opportunities. We favor regions with strong potential for earnings, particularly those aligned with long-term secular themes including artificial intelligence. U.S. large cap equities remain our most preferred market, supported by the leading AI companies' strong cash generation capabilities. Even though valuations are expensive vs. other markets, these stocks have a superior fundamental outlook.

We also like emerging market equities, which should benefit from easing financial conditions globally. Emerging Asian markets in particular are well positioned to benefit from tech goods demand. The demand for AI capital expenditure should benefit corporations in Taiwan and Korea; India continues to be supported by a robust domestic macroeconomy. China's recent policy announcements have helped mitigate downside risks in Chinese equities. Further such policy support in China, and prompt implementation, could boost emerging markets.

On the other hand, Europe continues to face domestic and external challenges. Weak growth, subdued consumer demand and lower inflation indicate increasing margin pressures on European companies and thus a lackluster earnings outlook. Index valuations are slightly above historical norms and we see limited potential for expansion in the current environment, leaving us cautious on European equities.

[1]Italian treasury bonds, Buoni del Tesoro Poliannuali.

Exhibit 2: MAS Asset Class Views

Asset Class		Opportunity Set	UW	N	OW	Change	Conviction
Main asset classes		Equities	○	○	●		Low
		Duration		●	○		
		Credit	○	○	●		Moderate
Main asset classes	Equity	U.S. large cap	○	○	●		Moderate
		U.S. small cap	○	●	○		
		Europe	●	○			Low
		Japan	○	●	○	▼	
		UK	○	●			
		Australia	●	○	○		Moderate
		Canada	○	●	○		
		Hong Kong		●	○	▲	
		EM	○		●		Low
	Fixed income	U.S. treasuries	●	○	○	▼	Low
		German Bunds	○	●	○		
		JGB	●	○	○		Low
		UK Gilts	○	○	●		Low
		Australia bonds	○		●		Low
		Canada bonds	●		○		Moderate
		BTPs	○	○	●		Moderate
		Corporate Inv. Grade	○	●		▼	
		Corporate High Yield	○	○	●		Moderate
		EMD Sov	○	●	○		
	Currency	USD	○	○	●		Low
		EUR	●		○		Low
		JPY	○	●	○	▼	
		CHF	●	○	○		Moderate

The tick chart and views expressed in this note reflect the information and data available up to October 2024.

Multi-asset solutions

J.P. Morgan Multi-Asset Solutions manages over USD 269 billion in assets and draws upon the unparalleled breadth and depth of expertise and investment capabilities of the organization.
Our asset allocation research and insights are the foundation of our investment process, which is supported by a global research team of 20-plus dedicated research professionals with decades of combined experience in a diverse range of disciplines.

Multi-Asset Solutions' asset allocation views are the product of a rigorous and disciplined process that integrates:

- Qualitative insights that encompass macro-thematic insights, business-cycle views and systematic and irregular market opportunities
- Quantitative analysis that considers market inefficiencies, intra-and cross-asset class models, relative value and market directional strategies
- Strategy Summits and ongoing dialogue in which research and investor teams debate, challenge and develop the firm's asset allocation views

As of June 30, 2024.

Next steps

For more information, contact your J.P. Morgan representative.

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