

CROSS ASSET Investment Strategy

#05

May
2020

Monthly



CIO VIEWS

The aftershocks
of the Covid-19 earthquake

THIS MONTH'S TOPIC

Contraction > recovery > late cycle:
a cycle round trip in three years

#05 - May 2020

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CIO VIEWS



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The aftershocks of the Covid-19 earthquake

After closing one of the worst quarters ever for equity markets, Q2 started on a high note, with indices (S&P 500 and Euro Stoxx 600) recovering markedly from the bottom hit during the previous month. There is clearly a **battle between bull and bear forces** taking place. On the bull side, extraordinary policy actions continue to propel market sentiment (signals of virus-peeking in Europe and hopes of sooner-than-expected re-opening). On the bear side, deteriorating fundamentals from the earnings season and the sustainability of the mounting debt pile will be key risks. The tug of war **between sentiment and fundamentals** is just the first in a long list of battles in course. The most important will be the duel **between liquidity and solvency** in which the focal point that could shift power from one side to the other is the pandemic's evolution. How long it will last is the key variable that will determine the shape of recovery, which now appears likely to be U-shaped, with a long bottom phase and the slow recovery.

From an investment perspective, the aforementioned battles point to some **key actions**:

- **Remain cautious in short term.** Markets have priced in some light at the end of the tunnel in the next six months. This is overly optimistic as economies will not be switched back-on overnight and as there is uncertainty on the temporary vs. permanent nature of losses in potential output and employment.
- **Be ready to play the sequence of rebound at asset class and regional level.** The crisis is inducing a partial de-synchronisation in the economic cycle that is strictly linked with the epidemic in each country and/or region. In China, where the outbreak originated, the economic outlook is slowly improving, while it is deteriorating in Europe and the US. We believe earnings will be the first to suffer, while defaults will come later. A prolonged lockdown could eventually affect risk premia in real estate.
- **Manage liquidity dynamically,** by keeping appropriate liquidity buffers to be able to exploit entry points and not be caught in a liquidity trap if the economic outlook worsens. This translates into building a barbell risk exposure, with big cash buffers on one side and exposure to the rebound on the opposite.
- **Differentiate risk opportunities.** Credit is favoured vs. equity, because the latter seems to be pricing in a too-positive outcome. Second, because fiscal and monetary measures will favour bondholders vs. shareholders. In equities, risk exposure should focus on cyclicals with quality that could best exploit a way out of the crisis. Investors should assess the long-term implications of the current crisis at a sector and company level. Sectors with high fixed costs are most exposed, while companies or sectors that are more flexible in adapting their models to the new pandemic world will fare better. In credit, debt sustainability, liquidity and eligibility for Central Banks' purchasing programmes is key. In Emerging Markets, fiscal vulnerability, external vulnerability to USD strength and oil dependency must be monitored.

The Covid-19 crisis is reinforcing the **need to be active and selective**, as it will transform the world and the aftershocks have just started. The path to reach a (new) equilibrium will oscillate and propagate through waves. In this process, a rising component of external intervention is altering capital markets structures. Hence, price discovery is becoming chaotic and full of traps. This means that a first wave could benefit some asset classes that are distorted by these interventions. For example, some part of HY could benefit from the Fed and the ECB's actions during the first wave of interventions, but could come under pressure in a second wave of normalisation. Similarly, in equities, some overreaction could create compelling long-term opportunities. We are seeing this in sectors such as airlines, where all companies have been almost indiscriminately affected, but where those with strong balance sheets will be able to navigate these stormy waters. The way the system readjusts will also have significant implications on a new battle that is opening up, the one of **inflationary vs. disinflationary forces**. While in the short term the collapse in global demand is favouring the disinflationary front, the economic cure for the crisis (debt creation with monetisation of debt, regionalisation vs. globalisation in trade dynamics) could prove to be inflationary. The new equilibrium that is reached at the end of this sequence will be very different from the one we had been getting used to in the last decade of low inflation and low rates. But it will take time to reach and for now **the focus should be to stay in cash, stay in some risk assets and stay active**.

Overall risk sentiment



Dynamic liquidity management is critical; overall stay defensive on risk assets.

Changes vs. previous month

- Some opportunities in US credit to exploit market dislocation, without increasing the overall risk exposure

Overall risk sentiment is a qualitative view of the overall risk assessment of the most recent global investment committee.

MACRO

China: a bumpy road to recovery



MONICA DEFEND
Global Head of Research



CLAIRE HUANG
Macro-Strategist, EM

The impact of the Covid-19 outbreak on the Chinese economy was uneven – catering services and the hotel industry registered the biggest fall, whereas financial and ICT services were bright spots

With much of the world under lockdown, China's economic activities are slowly returning to normal, demonstrating what a recovery post the Covid-19 hit could look like. We believe the path to recovery will be uneven and bumpy. In light of the dim global demand, Chinese leadership has turned more decisively towards easing.

The Covid-19 outbreak has impacted the economy unevenly. Activities that rely heavily on physical interactions were particularly hard hit. Catering services and the hotel industry registered the biggest fall in GDP in Q1 (-35.3%, yoy), followed by domestic trade (-17.8%), construction (-17.5%) and transportation (-14%). On a positive note, information and communications technology (ICT) and financial services were bright spots, with GDP growth remaining positive and only slowing slightly. The economic damage was highly correlated with the severity of activity controls. In Hubei province, where the outbreak was most severe and where almost all outdoor activities were restricted since late January, GDP slumped by 39.2% in Q1, compared with a decline of 6.8% nationwide.

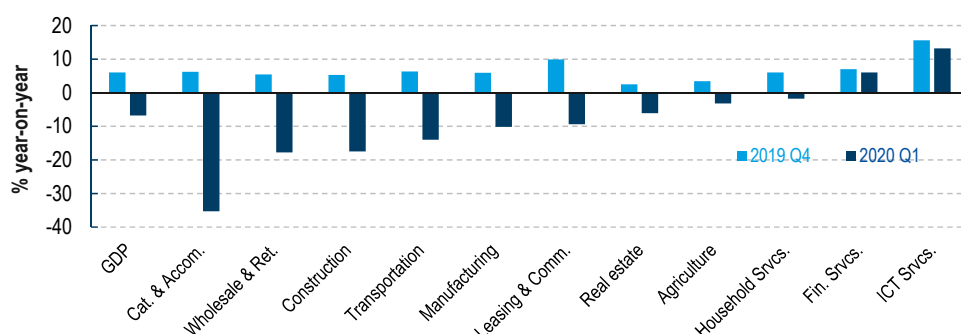
Production could rebound rather quickly, not so for demand. Following the removal of restrictions, industrial production bounced back strongly in March, reflecting a back-to-normal jump from the suspension in February. April data, including the air quality index and the concrete batchers' utilisation rate suggest, construction is also warming up.

The recovery in consumer demand varies across segments. While staples outperformed during the entire outbreak, discretionary consumption goods only managed to partially narrow contractions in March. But further improvement is well on track: auto sales growth picked up to -7% in the first three weeks of April from -40% in March. The services sector is lagging behind. High-frequency data shows national passenger

flows are still way below their normal levels in April, while catering and accommodation services are picking up slowly. **Continuous epidemic prevention could weigh further on the services recovery.** As the government remains alert to imported cases and to the risks of a second wave, most entertainment venues across the country remain closed at the time of writing.

A step-up in policy support is expected to unleash domestic demand. Progress aside, persistent pressures in the labour market and mounting external risks have driven the country's leadership to step up supportive policies to stimulate the domestic economy. Infrastructure spending remains the top-picked growth stabiliser. **We expect the fiscal deficit to expand meaningfully by around 4 percentage points of GDP from 2019,** after including special national and local government bonds. The latest policy indicate that boosting property market is not a preferred option. **Monetary easing will continue and the People's Bank of China (PBoC) is likely to reduce the reserve requirement ratio (RRR) and interest rates in the near term.** A deposit rate cut is still on the table, but may have to wait until food inflation eases further. Credit growth is expected to firm up throughout the year, with a notable amount of funding likely to be directed into the infrastructure sector. However, the above-mentioned stimulus cannot fully offset the economic damage throughout the year. The deterioration of external demand points to increasing downward pressures on the manufacturing sector and the labour market. **The outlook for services consumption remains challenging, with most of the losses likely to be permanent.** We expect a soft recovery ahead and forecast China's economy to grow by low single digits in 2020.

Real GDP growth by sectors



Source: Amundi Research - Data as of 23/04/2020 Chart categories from left to right = GDP, Catering & Accommodation, Wholesale & retail sales, Construction, Transportation, Manufacturing, Leasing & Commercial services, Real Estate, Agriculture, Household services & others, Financial Services, ICT Services. All % changes are year on year (yoy).

MULTI-ASSET

Focus on fundamentals instead of emotions



MATTEO GERMANO
Head of Multi-Asset

We remain cautious and wait for possible entry points, keeping a strong focus on fundamentals

The Covid-19 outbreak has spread globally over the past month, delaying the peak of the contagion to April/May. The exogenous shock, which was initially mainly affecting Chinese growth and trade dynamics is now negatively affecting global demand, with many regions experiencing lockdowns. As a result, despite massive support from economic policy, growth forecasts deteriorated sharply for DMs and EMs. From an investor's perspective, credit crunch and **concerns over rising corporate defaults** have magnified financial market turbulence. However, we believe active monetary and fiscal policies will support growth stabilisation in the last quarter of the year, although time horizons will differ for each country and will depend on the evolution of the outbreak and pre-existing fragilities. In this environment, **we remain defensive and continue to monitor fresh data to better assess the impact.**

High conviction ideas

The recent rally was a result of an emotional response as the growth in the number of new cases slowed in many countries, as well as an unwinding of investor positions. Stronger fundamentals are needed for any sustained upward movement in stock prices. As a result, **we remain cautious on European and US equities.** Stock valuations are not attractive as consensus expectations for margin growth seem too optimistic. In the UK, the contagion is likely to raise the uncertainty in a situation already complicated by the geopolitics of Brexit. Elsewhere in EMs, we maintain a neutral stance owing to the high volatility and downside risks. Nonetheless, we continue to look for potential opportunities (Asia, Russia) in case of positive developments.

In duration, we have a broadly neutral view as the ultra-loose monetary policies of central banks are likely to keep yields range-bound. Therefore, the attractiveness of opening new directional positions is low for now. In the US, where the Fed's monetary response eased liquidity constraints in the second half of March, UST levels are now closer to their fair values. We maintain our preference for US 5y vs. Germany 5y as the former may benefit from safe-haven demand – although to a lower

extent now – and from the Fed's aggressive asset purchases (in short- to medium-term segments). **We are now cautious on Japanese 10y breakeven inflation** due to deteriorating GDP growth prospects and the correction in oil prices (disinflationary effects).

The Italian curve continues to offer attractive yields, leading us to keep our preference for Italy 30y vs. Germany 30y. The ECB has been flexible with respect to its capital key rules, and as a result its actions are allowing a ceiling on Italian yields. **We remain positive on credit** (support from central banks) and focus on high quality and liquid names. Here, we prefer IG to HY due to concerns over high default rates and slowing top-line growth. Within HY, we favour EUR over US as the latter is more vulnerable because of its relatively high exposure to commodities and the energy sector.

In **EM FI**, market volatility will remain high and emerging bond spreads are likely to remain under pressure for several months.

We confirm our neutral stance on EM spreads for three key reasons: (1) concerns of significant macroeconomic deterioration; (2) the reduction in the growth gap between DM and EM in 2021; and (3) the low oil price, which will be a headwind for many countries in the EMBI index. Having said that, we acknowledge that overall fundamentals point to tighter spreads, but EM FI will be driven more by technical factors in near term.

On **DMFX**, we remain positive on NOK vs. EUR as NOK has already corrected significantly and is also a way to gain exposure to a more optimistic scenario. Our constructive stance on EUR vs. CHF is maintained due to expensive CHF valuations.

Risks and hedging

Investors should maintain appropriate hedges, such as yen, derivative instruments and gold, as these can serve as a good tool to limit the impact of market uncertainty and to protect portfolios

USD = US Dollar, UST = US Treasury, DM = Developed markets, EM/GEM = Emerging markets, FX = Foreign exchange, FI = Fixed Income, IG = Investment grade, HY = High yield, CHF = Swiss franc, NOK = Norwegian Krone, EUR = Euro, EMBI = EM bond index,

Amundi Cross Asset Convictions

	1 month change	---	--	-	0	+	++	+++
Equities				■				
Credit						■		
Duration						■		
Oil					■			
Gold						■		

Source: Amundi Research. The table represents cross asset assessment on a 3-6 month horizon, based on views expressed at the most recent global investment committee. The outlook, changes in outlook and opinions on the asset class assessment reflect the expected direction (+/-) and the strength of the conviction (+/+/+/+). This assessment is subject to change.

FIXED INCOME

Normalisation is not yet here: focus on liquidity



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Head of Fixed Income



YERLAN SYZDYKOV
Global Head of Emerging Markets



KENNETH J. TAUBES
CIO of US Investment
Management

We have seen a gradual improvement in market conditions after the massive price and liquidity dislocation in March, but we are not back to normal yet. Liquidity remains choppy, the short end of the credit curve has not normalised yet and there is discrimination between what is eligible for central banks' programmes and what is not. We are **cautious and selectively play relative value opportunities** and exploit the premium for **good quality issuance**. Liquidity focus is critical and convictions that have the potential to rebound, despite weak short-term performance, should be maintained. In addition, investors should aim to avoid permanent loss by staying clear of sectors exposed to recession.

DM bonds

With a global fixed income perspective, we have a **neutral view** on duration, with a constructive stance on the US. But we have **tactically reviewed our stance** - neutral on core Euro (more positive than before), negative in Japan, although to a lesser extent than previously. Elsewhere, we are more confident on US inflation bonds due to expectations of a rebound in inflation. We believe rates markets are now highly administered and have lowered our conviction on curve-flattening strategies in Europe and the US. **Euro peripheral countries** offer attractive yields, although we are now more cautious, in particular on Italy. **In credit**, we see less dislocation of liquidity, but there is still a lack of securities to purchase. We remain constructive on IG (particularly financials) on expectations of normalisation, liquidity backstop from CBs and hopes of fall in migration and default risks. We favour EUR IG (low leverage) and are more positive on US than before. There are opportunities in US IG primary markets in higher yields. In HY, we still favour EUR over the US (high default risk). From the **US FI perspective**, Covid-19-

induced market dislocation is an opportunity for **active management** in favour of assets with strong upside potential, but a focus on selection is essential, as fundamentals are challenged by the deep recession. For most non-government sectors of the US bond market, yield premiums over UST are attractive across all rating categories (long maturity IG corporate bonds, HY corporates, well secured RMBS). We like 30y IG corporate bonds (cautious on 10y) and some HY names available at deep discounts. **Liquidity remains a priority** and we favour assets such TIPS owing to our inflation expectations relative to breakeven rates already priced in. We are cautious on UST and agency mortgage bonds. **Investors should utilise upward movements to reduce idiosyncratic risks** - OPEC+ deal and a pick-up in demand for mortgage credit risk provide a chance to pare back risk in energy.

EM bonds

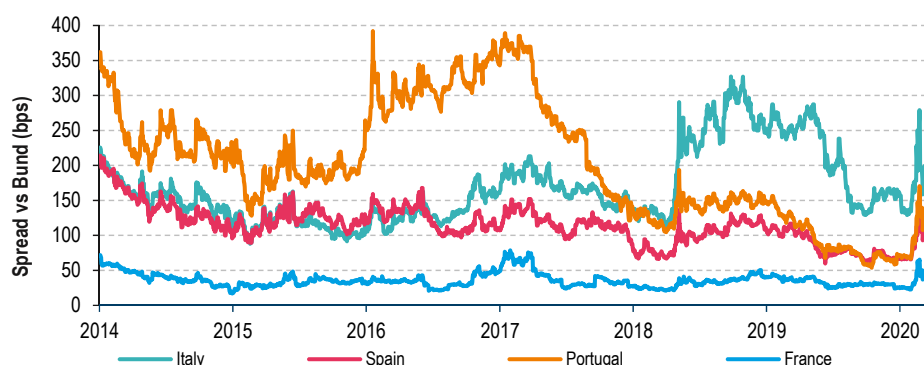
We remain cautious on EM debt, although sentiment has started to improve in terms of asset prices and fund flows. We see value in EM external debt, particularly HY, where spreads have already widened to GFC levels. Quasi-sovereign debt in Latin America offers attractive risk/reward scenarios across Brazil, Mexico and Peru. Within local currencies, we prefer EM rates, where we see value in Russia in FX and rates. In Mexico and South Africa, we see value in rates, but not in FX. Overall, how the lockdown is lifted and a possibility of second wave of virus spread are the key risks.

FX

We remain positive on USD/EUR because of the extraordinary slowdown caused by the pandemic, making US assets attractive in such a crisis. In EM, we remain bearish, especially on growth-sensitive currencies such as China

Areas of strain remain in fixed income, but there are some opportunities opening up from market dislocation

10y euro-bond spread vs Bund



Source: Amundi, Bloomberg - Data as of 22/04/2020

EQUITY

Balance sheet strength matters now more than ever



KASPER ELMGREEN
Head of Equities



YERLAN SYZDYKOV
Global Head of Emerging Markets



KENNETH J. TAUBES
CIO of US Investment Management

Overall assessments

Equities have recovered over the past weeks amid an environment where some countries are thinking of an exit strategy and ways to support a demand recovery. We expect governments' debt burdens and their role in the economy to increase. On the other hand, private sector has also spurred into action as European companies culled dividend. From investors' viewpoint, the crisis offers attractive stock selection prospects but is producing higher than usual uncertainty and volatility, leading to significant dislocations in some parts of the market, without any fundamental rebasing. As a result, **we search on more opportunistic grounds for some of those cases (quality/growth) and also look for long-term investment ideas.**

DM equities

In Europe, earnings will have to come down significantly from current market expectations and this will be a painful process. Caution is warranted near term, while we look for selective opportunities exposed to a demand recovery. We take a **barbell approach on having quality stocks with resilient business models** in sectors such as health care, utilities and consumer staples at the one end and then some high quality cyclical stocks with exposure to the demand recovery in sectors such as consumer discretionary and industrials. On both ends of the barbell, the **strength of balance the sheet** and strong competitive position remain critical to us. At a more granular level, quality banks and insurers trading at attractive valuations and supported by backstop measures of CBs fall into that category. We are constructive on the luxury sector in China and on the leading sports goods manufacturers that

have attractive valuations. However, we expect automotive names to report sharp declines in 2020 earnings.

In the US, **we maintain a cautious stance** and wait for evidence related to earnings performances, coupled with corporate guidance for the quarters ahead, although there is not yet much clarity on this. Earnings estimates have come down, particularly in cyclicals, as earnings expectations have collapsed; there is less room for error given the relative valuations in growth and low volatility/defensive stocks. Value is still historically attractive relative to growth, but we remain cautious because of issues such as further industry consolidation and permanent changes resulting from the pandemic. At a sector level, we like high quality names in financials, industrials, healthcare equipment and communication services but are cautious on semiconductors and bond proxies such as consumer staples.

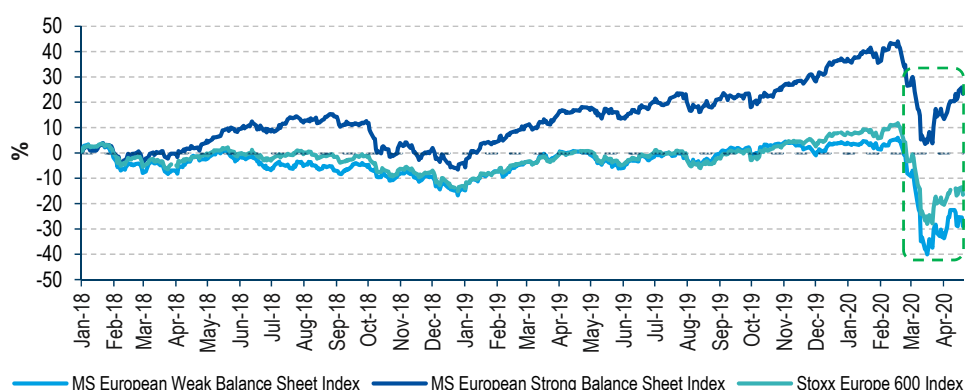
In general, we believe that companies that can seize the opportunities in the next phase will emerge in better shape. To conclude, investors should realise that it is difficult to call a market bottom, but **dislocations may offer long-term opportunities to enter the market gradually.**

EM equities

We remain relatively defensive but are witnessing encouraging signs in countries that look to be at a later stage of the coronavirus cycle. Countries with fiscal buffers and strong domestic bases (such as China, Korea and Taiwan) present a strong investment case as they are close to being autonomous regarding internal demand and are less dependent on global supply chains and trade. However, we are extremely defensive on names dependent on export, commodities and tourism.

When the range of outcomes is wide and there is ambiguity on the recovery path, it is all about exploring resilient business models and finding relative value opportunities

Weak vs strong balance sheets



Source: Amundi, Bloomberg, as of 21 April 2020. Stoxx Europe 600 data for some holidays is not available

THEMATIC



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Head of Global Views



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Fiscal multipliers are likely to be larger when economic activity is very depressed

As part of Global Research, the main mission of the newly established Global Views team is to strengthen Amundi's thought on key cross-cutting thematic

Don't underestimate the multiplier effect

Over the last few weeks, significant stabilisation plans have been announced across advanced economies and in addition true stimulus plans are now under consideration. Recent empirical studies show that fiscal multipliers could be much larger in the current depressed context than during normal times. We believe this could boost the recovery path of corporate dividends going forward, in Europe in particular.

There is near consensus among economists on the need to stimulate growth once the epidemic is under control. Numerous hysteresis effects will hamper the recovery (affected sectors, lack of confidence, and increase in household savings during the lockdowns). Stabilisation plans will therefore gradually have to give way to growth stimulation plans, if only to anchor expectations of a recovery. Moreover, the conclusions of the empirical literature on the scale of the multiplier effects have changed considerably since the early 2000s. Prior to the GFC, most estimates gave multipliers of the order of 0.5x. Many empirical studies have shown since then that **fiscal multipliers** are likely to be **larger when economic activity is very depressed**.

Assessing fiscal multipliers

The rationale is quite straightforward. When economic activity is depressed and unemployment is high, household consumption depends more on current income than on future income, while business investment depends more on current profits than on future profits. Therefore, the multipliers are higher than in normal times and, in this case, are likely to be much higher than 1x. **This is especially the case when banks restrict credit and when households seek to reduce their debts quickly** (Eggertsson and Krugman, 2012). In addition, **multipliers are found to be significantly greater than when policy rates are at their zero lower bound** – see Michael Woodford (2011), Christiano, Eichenbaum and Rebelo (2011). Authors have shown, using a dynamic stochastic general equilibrium model (DSGE), that under such conditions, **budget multipliers can exceed 3x**. Using US data, Auerbach and Gorodnichenko (2012) found that **fiscal multipliers for government spending range from zero in normal times to about 2.5 during recessions**.

If the fiscal multipliers are larger than in normal times while growth projections implicitly assume they are the same, then economists, and investors with them, might underestimate the strength of the recovery in 2021-22. Although the shape of the recovery is more likely to be a U with a long base than a V, the subsequent growth trend might be stronger than expected due to the leveraged effect of multipliers on budgetary measures.

Corporate dividends recovery pace

This could have implications for corporate earnings in two or three years, and on the recovery path of stock dividends. Among identified **market dislocations**¹, forward dividends have actually been the most affected by the recent sell-off, particularly in Europe. **Dividends have been under significant pressure** since the outbreak of Covid-19 for fundamental and technical reasons. The most obvious factor is the massive revision of corporate earnings, which has led to dividend cuts or cancellations. Yet, historically, DPS are far less volatile than EPS, and tend to fall by about half during recessions. In Europe, however, banks have been asked by the regulator to cut their 2020 dividends (based on 2019 profits) in order to increase their capital base. Moreover, companies that have benefited from state guarantee schemes as well as those in directly exposed sectors have also cancelled their dividends. Market implied dividends have been hurt by selling flows from investment banks on forwards during the more acute phase of the equity crash.

Consequently, **expectations for European stock dividends look like an L-shape scenario** that is far darker than Amundi's downside scenario on earnings. If multiplier effects lead to a stronger scenario, chances are that corporations will resume their dividends earlier than expected. We believe that **income strategies** that are actively focusing on **dividend recovery** will provide an interesting risk/reward profile over the next two to three years.

Finalised on 24/04/2020

Eurostoxx50 Index	24 April 2020	20 February 2020	Change
2020 EPS consensus est.	202,6	259,6	-22%
Dividend Fwd	70,1	123,2	-43%
2021 EPS consensus est.	242,8	282,6	-14%
Dividend Fwd	67,8	123,2	-45%
2022 EPS consensus est.	272,3	303,8	-10%
Dividend Fwd	77,9	119,5	-35%
Index in points	2809	3822	-27%

¹ We define dislocation as a temporary disruption in the co-movement of assets versus historical norm or traditional regime

THEMATIC



ALESSIA BERARDI
Head of Emerging Markets
Macro & Strategy Research

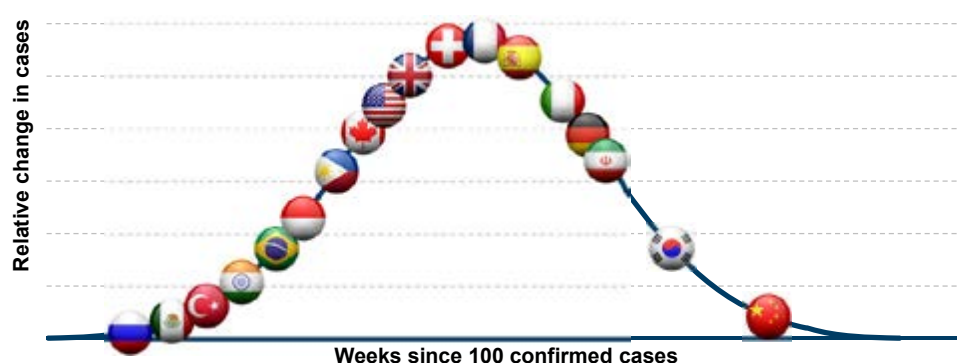
Emerging markets, navigating among several shocks

When we analyse emerging markets in the context of the Covid-19 pandemic, we need to assess not only the impact on growth and the policy mix in place to drive its recovery, but also the vulnerabilities that the same policy mix is breeding, through capital outflows and currency depreciation. The following analysis will help to navigate the different situations in a number of emerging markets, and will offer a more granular country view.

In order to assess where we are with the Covid-19 pandemic and its economic impact on the emerging markets universe, we should firstly **highlight the sequence of outbreaks across the world**. The first outbreak episode in mainland China in January 2020 was followed by a second outbreak in South Korea and in Western countries (Europe and the US) in the second half of February. Finally, over recent weeks, we have been seeing a sort of third wave that has increasingly impacted the emerging markets and frontier countries. Among the emerging markets, in terms of the infection curve, Turkey, Brazil and Russia seem to be the most affected

countries so far, with India and Peru following some way behind (source: Worldometer's Covid-19 data). However, at this point it is fair to highlight that the death toll is still small in comparison with the situation in Western countries. With regard to this third outbreak, the good news is that emerging markets and frontier countries can heed the early warnings and benefit from the best practices implemented in countries that experienced the pandemic earlier. On the flip side, the bad news is that the healthcare systems in most emerging markets are ill-equipped to handle the kind of severe outbreak seen in the hardest hit countries in the West.

1/ Covid-19 conceptual schematic cycle



Source: Amundi Research, Worldometer, WHO, Data as of 17 April 2020

In terms of economic impact, no country will be spared

The stimulus is still primarily being driven by monetary policy rather than fiscal authorities

In terms of economic impact, no country will be spared. The combination of a domestic outbreak and the related lockdown measures implemented to contain it (the cure of the disease), together with the external shocks materialising due to weaker demand from abroad and lower tourist flows, will not spare anyone. As we speak, emerging markets are falling into recession, the depth and the length of which will mainly depend on the infection curve, the length of lockdowns and how soon global treatments (accessible to the poorer countries as well) for the virus and/or a vaccine become available. The struggle in terms of domestic demand will be much more widespread in the most open economies, the ones that are well integrated into the global supply chain or are commodity exporters, as well as in smaller economies that are highly dependent on tourism.

Compared to the consensus, **Amundi's emerging market growth forecasts appear**

slightly less negative for 2020, but weak economic performance is expected to continue for longer, resulting in a U-shape rather than a V-shape recovery with less robust growth levels until 2021. Barring the impact of base effects on next year's economic growth forecasts, we do expect that economic activity will continue to recover in China and the authorities' efforts will be focused on putting the country back on track towards the economic moderation envisaged before the crisis.

Overall, emerging market authorities have adopted a much bolder easing mode. At this point in time, **the stimulus is still primarily being driven by monetary policy rather than fiscal authorities**, with very few exceptions implying a more balanced mix. The role of monetary policy as the leading force in the policy accommodation mix is reflected by the actions of many central banks at unscheduled meetings, as was the case very recently in South Africa, India and

THEMATIC

We do have to consider some side effects related to policy easing where there is little policy room and high levels of vulnerability

Mexico, to name just a few examples. This is even more revealing in the case of Mexico, where the Banxico still has a reputation of being a very orthodox central bank. Among the few exceptions to policy mix being driven by monetary policy, the Bank of Indonesia and the Ministry of Finance recently announced a more coordinated effort to adopt a three-year fiscal plan, which goes well beyond the fiscal deficit's legal limit of 3% (at 5.1%) in 2020 and is not expected to drop back below the limit before 2023. In our interpretation of the events, at the latest monetary policy meeting, the Bank of Indonesia held steady, favouring macro prudential measures to monetary policy easing as a sign of coordination with a more proactive fiscal authority. A controversial aspect to monitor going forward is the incremental number of emerging market central banks that are adopting quantitative easing and getting ready to buy bonds on the primary market (in some cases amending their constitutions to do so).

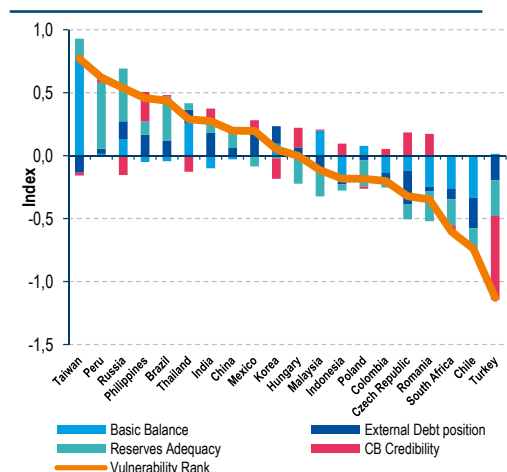
In order to reach a more balanced policy mix, we do think that more stimulus should come from the fiscal side.

Having said that, within the EM universe, beyond the direct assessment of the stimulus as being enough to put the different countries back on track, **we do have to consider some side effects related to policy easing where there is little policy room and high levels of vulnerability. The combination of recessionary growth rates, a strong USD**

(or weaker local currencies) and very low oil prices can trigger rating downgrades (which have increased sharply in recent weeks), currency/balance of payments crises and defaults in the worst cases.

In order to assess the risks emerging markets are experiencing, we need to evaluate their fiscal fragility and their external vulnerability. As a simple matter of fact, fiscal metrics in 2020 are going to deteriorate due to recessionary growth levels and expansionary fiscal measures implemented to combat the COVID-19 crisis, while at the same time a strong USD or weak local currencies are increasing external vulnerabilities. Combining all these factors, we came up with a stress rank that puts countries like **South Africa, Colombia, Hungary and Malaysia as the countries that are more exposed on both sides.** Adding the many contingent liabilities to the Central Government's fiscal position would worsen the ranks of countries such as Mexico and others. The framework presented is going to evolve according to factors that are not easily predictable. In the middle of the crisis we need to monitor the changes to lockdown measures, whether they become stricter or more relaxed, and the subsequent impact on the growth. On the other side, we need to assess the incremental fiscal supportive measures implemented and the resulting deterioration of fiscal metrics. Finally, the advent of a treatment or vaccine could quicken the return to a pre-crisis lifestyle and speed up the economic recovery.

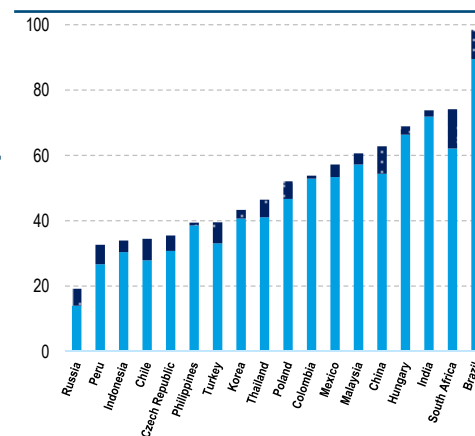
2/ External vulnerability index and central bank credibility



Source: Amundi Research, CEIC, BBG, Data as of 22 April 2020

The third risk factor under scrutiny is the exceptionally low oil prices we have seen recently. In an already depressing environment of significant oversupply, a technical incident based mainly on positioning at the time contracts were rolled over from April to May triggered negative oil prices for the first time in history. In our opinion, **the latest price movement has**

3/ 2020 Debt



Source: Amundi Research, CEIC, IMF, Data as of 20 April 2020

less to do with fundamentals and more with technical factors and positioning. Therefore, we expect oil prices to gradually recover to a positive and moderated market fair value with oversupply and falling demand continuing to drive market conditions for some time.

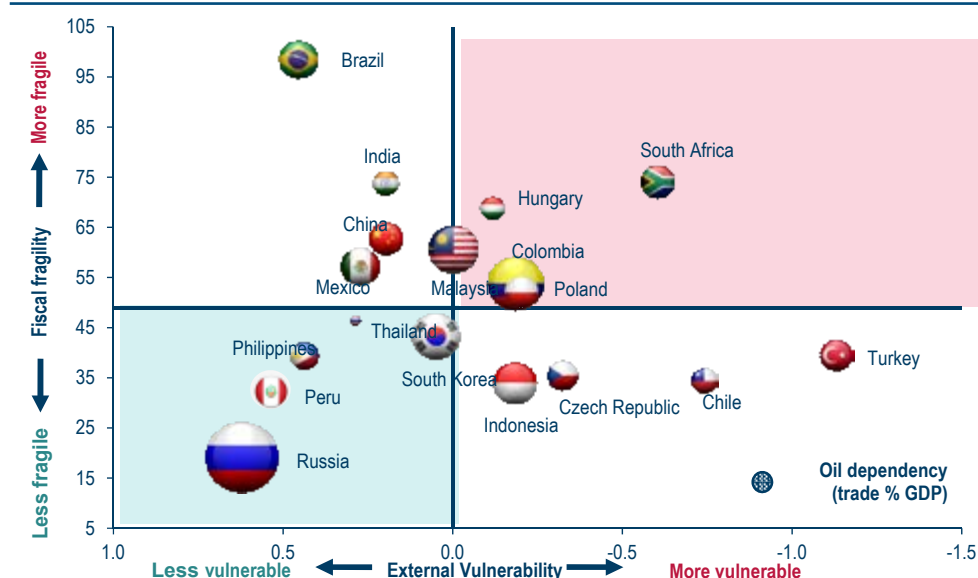
As far as the emerging markets are concerned, we need to firstly discriminate

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between **oil exporters and oil importers**. The current environment will continue to favour the second group of countries such as India/Turkey or even China, improving their external positions and decreasing the oil related fiscal costs. However, it will negatively impact Russia, Colombia, Mexico and the Gulf countries.

Having said that, among the oil producers and exporters, there are countries that will suffer more than others if we look at different oil price levels as a **fiscal breakeven in the budget or the different costs of production**. When we consider this, Russia comes out as better positioned in comparison with most of the Gulf countries.

4/ Assessing the emerging markets three dimensions risk



On a more positive note, we have seen international institutions like the IMF and the World Bank stepping in

On a more positive note, we have seen international institutions like the IMF and the World Bank stepping in. In recent weeks, the Fund has received several (around one hundred) requests for disbursement or debt relief and has been quickly processing them. In the last couple of weeks, many of them have been approved: on Monday, 13 April, twenty five countries received debt service relief for an initial six months under the Catastrophe Containment and Relief Trust (CCRT), among them DR Congo, Gambia, Mozambique, Nepal and Afghanistan, to name a few.

Regarding the tools used, the IMF has many different options in its portfolio. There are two emergency financing facilities with less stringent conditions than a proper IMF programme: the Rapid Credit Facility (RCF) and the Rapid Financing Instrument (RFI), which are both accessible by the poorest countries. These two facilities can be used on top of a pre-existing IMF programme, as was the case with the disbursement under the RCF approved for Niger.

Moreover, the IMF has different credit lines, such as the Flexible Credit Line (FCL) for pre-approved countries with minimal vulnerabilities and strong institutions (recently extended for Colombia) or the Precautionary Liquidity Line (PLL) for countries with moderate vulnerability.

In the current environment, the point is less to do with the availability of instruments

and more the increase in lending capacity. What the IMF is trying to do is revamping its instruments to increase the resources it can allocate. It is thanks to the recent support from the UK and Japan that the Catastrophe Containment and Relief Trust (CCRT) was able to provide US\$ 500 million in debt service relief to the 25 of the IMF's member countries. The IMF has asked its members for more resources to provide additional debt service relief under the CCRT for a full two years. Instruments such as Special Drawing Rights are sizable in the context of frontier countries like the small countries of Sub-Saharan Africa, which are in need of reserve buffers, but they become less adequate in size if we consider emerging markets and frontier countries as one universe. More resources are necessary.

One last point to take into consideration when we assess the impact of debt relief/cancellation for the lower income countries is the role of China. In recent years, China has become an increasingly relevant creditor for small (resources rich) economies around the world. When we talk about debt relief, we must not underestimate the importance of this non-institutional creditor and the commercial nature of its loans. **China's massive presence can act as a limit to the effectiveness of the IMF initiatives and curb the US' ability to obtain more resources.**

Finalised on 23/04/2020

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DELPHINE GEORGES
Fixed Income Strategist

The Fed has purchased \$1.42tn since 16 March to restore a smooth functioning of treasury markets

Fed's QE: the next phase

The Federal Reserve has bought US Treasuries at an unprecedented pace since it started its QE programme on 16 March. As volatility and liquidity on Treasury markets continue to improve, the Fed is expected to slowly taper its purchases that were aimed at maintaining proper market functioning. However, uncertainty around the extent of the recession the Covid-19 has caused and strong Treasury issuance to fund the fiscal stimulus could discourage the Fed from slowing the pace of purchases too rapidly. In particular, if the supply shock in the Treasury market triggers liquidity tensions, the Fed will increase its pace of purchases. On top of this, the Fed is likely to fine-tune its management of financial conditions with yield curve control (YCC).

Restoring liquidity and smooth bond market functioning with quantitative easing

The Fed launched QE, in its words, to support the smooth functioning of markets for Treasury securities and agency mortgage-backed securities that are central to the flow of credit to households and businesses.

At the peak in late March, the Fed was buying \$75bn in Treasuries every day when liquidity deteriorated strongly on the Treasury markets. It has since gradually decreased its purchases of Treasuries, buying only \$10bn per day this week. For comparison, the earlier pace of quantitative easing (QE) was \$35bn per month during QE1 (Q4 2008 - Q2 2010), then \$75bn per month for QE2 (Q4 2010 - Q2 2011), and \$45bn per month for QE3 (Q3 2012 - Q4 2014).

Indeed, this unprecedented pace of Treasury purchases has helped stabilise treasury markets. Yields are starting to settle into a range; realised volatility has calmed down; the bid-offer spread has started normalising although it remains wider than before the crisis; and real yields have retreated after their spike, as seen on the graphs below.

It is worth noting that, despite the fact that Fed has been buying Treasuries across the curve, **it has focused the largest part of its purchases on the short end of the curve.** This highlights that the underlying goal was

essentially to address the Treasury market's liquidity problems. As seen on the graph below, 55% of Treasury purchases planned recently were in the 0-4.5Y maturity range and only 13% in the 20-30Y maturity range.

By purchasing Treasuries at the front end of the curve, the Fed has been supporting the markets' need to raise cash ahead of the coming recession. In a deleveraging context linked to a rise in risk aversion, investors sold short-term Treasuries to fund their cash needs. The large asset purchases also helped free dealer balance sheets from USTs and MBSs, allowing them to pursue more funding intermediation, thereby improving liquidity on the markets. Taking into account the purchases of Treasuries (\$1.42tn) and MBS (\$268bn), the Fed's balance sheet has expanded by \$1.68tn since 16 March.

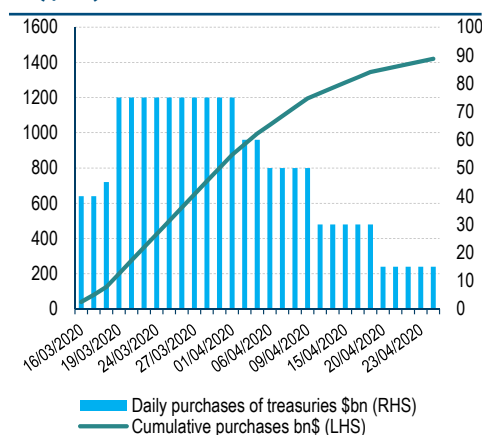
So, what's next?

As liquidity improves, the Fed is expected to move towards a more classic version of QE, consisting of a much lower and regular pace of buying, focused on longer-term maturities to stimulate the economy.

QE will aim at easing financial conditions to support growth and inflation working through two main channels:

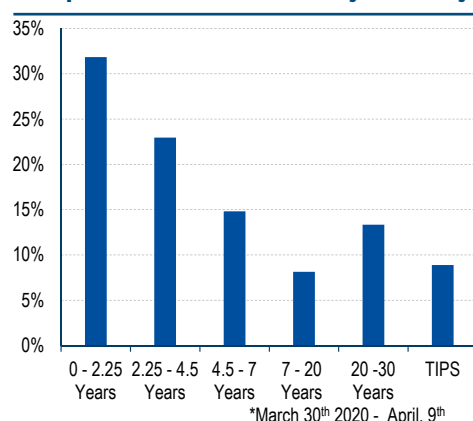
- Portfolio balance channel: this works by removing duration risk from the Treasury market, pushing investors to bid up the

1/ Daily purchases of Treasuries (\$bn)



Source: NY Federal Reserve, Amundi Research - Data as of 24/04/2020

2/ Planned Treasury Operations* Breakdown by maturity



Source: FRBNY, Amundi Research - Data as of 9/04/2020

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QE is expected to be maintained until the recovery is on track and might have to be supplemented by Yield Curve Control

value of both remaining longer-term Treasuries and close substitutes such as mortgages and corporate bonds.

- Signalling channel: by signalling policy makers' intention to keep short rates low for an extended period of time.

Sizeable purchases on longer-term Treasuries are, therefore, to be expected

According to Janet Yellen, the former chair of the Fed, overcoming the effects of the zero lower bound during a severe recession, as the current one will most probably be, would require about \$4 trillion in asset purchases. On top of this, it will also require a pledge to keep rates low for even longer than before.¹

QE should be maintained until the recovery is on track

The future pace of QE is dependent on how fast the economy recovers. The exogenous nature of the coronavirus shock blurs the outlook on the depth and the duration of the recession. The Fed could gradually decrease the pace of purchases to \$150bn per month. In that case, the QE purchases over the year would total \$2.6tn. If the recovery is strong enough, the Fed might slow further to a pace of \$100bn per month; in that case the total amount of Treasury purchases could be close to \$2tn over the year.

QE should absorb a large part of the deficit. On the back of the government actions to counter the economic recession, the massive fiscal response is going to trigger a deluge of Treasury issuance in the coming months, on the front end of the curve in particular. The deficit is expected to exceed \$3.5tn for 2020 with a net increase of \$1.6tn coming from the Coronavirus Aid, Relief, and Economic Security Act (CARES). This is a massive supply shock that is in the making.

¹ Janet L. Yellen: The Federal Reserve's monetary policy toolkit – past, present, and future Speech August 2016.

² The New Tools of Monetary Policy, American Economic Association, Presidential Address, Ben S. Bernanke. January 4, 2020.

Half of the deficit should be funded by Treasury bills. If this supply shock triggers problems on the bond market, the Fed is likely to increase the pace of QE once again.

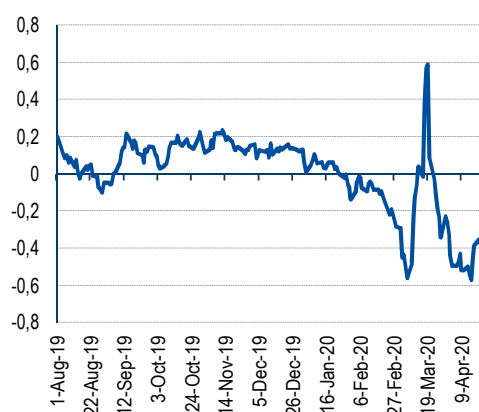
Forward guidance + QE + Yield Curve Control for a fine-tuning of financial conditions

With inflation and inflation expectations at low levels and unemployment surging, the Fed will ensure that financial conditions remain exceptionally accommodative. A state-contingent forward guidance could be supplemented by front-end yield curve control, while the traditional QE would still be used for the long end of the curve. Yield curve control extends the maturity of interest rates that the central bank directly targets. With yield curve control, the Fed can limit yield increases by purchasing as many bonds as necessary when yields rise over a certain rate to bring them back down to its target.

The Fed has maintained a constructive view of the possibility of front-end yield curve control

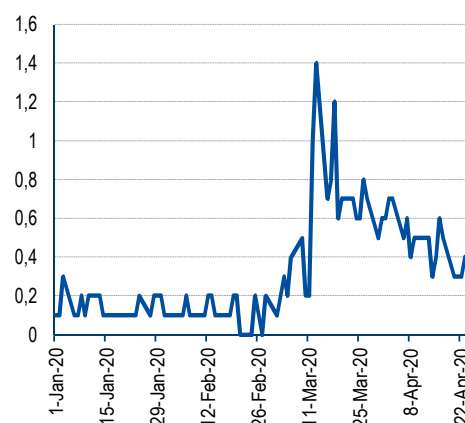
In January 2020 Ben Bernanke, the former Chair of the Fed, recommended including YCC in the list of new monetary policy tools: *"The Fed has not used new tools other than QE and forward guidance, but, within the bounds of its legal authorities, it should not rule out other options. The Fed's use of yield curve control could be substantially different from the BoJ's as it will most likely focus on controlling the short end (below the 2-year horizon) of the curve to augment the Fed's forward guidance. This has been explicitly suggested recently by Fed Governor Lael Brainard in a speech in February".*²

3/ US 10Y Real Rates



Source: Bloomberg, Amundi Research - Data as of 24/04/2020

4/ Bid-Ask Spread on US 30Y BY



Source: Bloomberg, Amundi Research - Data as of 24/04/2020

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Yield curve control could be a useful tool with the prospect of surging government debt issuance at the front end of the curve. YCC could help ensure that front-end rates remain low and stable. Fed Governor Lael Brainard refined its potential use in a advocating for yield curve control as a tool for strengthening the credibility of the forward guidance and as the way to reinforce the Fed's commitment to maintaining exceptionally accommodative financial conditions. She was considering the possibility of capping interest rates on the short-to-medium segment of the yield curve.³

In this environment, **the US Treasury yield curve is expected to be under continuous flattening pressure with short-term rates near the effective lower bound** and an increase demand for duration from the Fed. This environment should be **supportive for longer-term investment grade corporate bonds.**

Finalised on 28/04/2020

³ Lael Brainard: Monetary policy strategies and tools when inflation and interest rates are low, February 2020

The Fed's response to the Covid crisis is much larger than its QE. The Fed is deploying its tools and weapons around two intermediary objectives. The first one is to ensure **smooth functioning of the Treasury market**, which is key for the US economy and financial markets overall, and to provide **exceptionally accommodative financial conditions**, both through QE. The second objective is to combat the disruption of the credit channel caused by the Covid crisis. The Fed has shown its commitment to supporting households, employers of all sizes, state & local governments through programmes and facilities of unprecedented scale and scope.

The table below summarises the programmes and facilities deployed by the Fed in response to the Covid crisis:

Treasuries and MBS - QE	
Treasuries	Purchases of Treasury securities through Open Market Operations
Agency MBS & CMBS	Purchases of Agency securities and MBS through Open Market Operations
Funding/ Money Markets Facilities	
Repos	Overnight and term repo operations for primary dealers
PDCF - Primary Dealer Credit Facility	Term funding against eligible collateral for primary dealers
PPPLF - Paycheck Protection Program Lending Facility	Term financing backed by PPP loans for depository institutions
Central bank liquidity swap lines	Foreign central banks access USD liquidity from the Fed
FIMA Repo Facility	Repo facility for Foreign and International Monetary Authorities
MMLF - Money Market Mutual Fund Liquidity Facility	Dealer purchases eligible assets from MMFs, using Fed loans
Credit Facilities	
CPFF - Commercial Paper Funding Facility	The Fed purchases 3m CP directly from issuers
PMCCF - Primary Market Corporate Credit Facility	The SPV* purchases corporate bonds on the primary Market
SMCCF - Secondary Market Corporate Credit Facility	The SPV* purchases corporate bonds in the secondary Market
TALF -Term Asset Backed Securities Loan Facility	Fed issues loans to holders of eligible ABS, collateralized by ABS
MSLF - Main Street Lending Facility	US banks institutions make loans to SMEs. The SPV* purchases these loans
MLF - Municipal Liquidity Facility	SPV* purchases securities from US states, cities & counties
* SPV = Special Purpose Vehicle. The Fed and the Treasury (via the Exchange Stabilisation Fund) set up investment an investment vehicle	

Source: Amundi Research

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Contraction→ recovery→ late cycle: a cycle round trip in three years



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The pandemic outbreak altered the cycle of financial regimes we had in mind at the end of 2019

The pandemic outbreak altered the cycle of financial regimes we had in mind at the end of 2019, with consequences extending over the medium term: after a sharp contraction in 2020, 2021 will see a “recovery” in the growth and profit cycle with a rebound in risky assets while in 2022, we expect a normalization towards a late cycle.

Macroeconomic backdrop

The geographical impact of the pandemic has extended globally over time, quickly evolving from an external shock to trade dynamics sourced in China to an endogenous shock of collapsing demand in most countries experiencing forced shutdowns.

While different timelines of the outbreak and related containment measures suggest a jerky recovery, with the risk of possible setbacks should a second wave of epidemic/lockdown occur, single economies are facing double shocks, both domestic and external.

Real GDP growth is expected to fall Q1/Q2/ Q3 2020 hit by the pandemic and global economic lockdowns.

On the inflation front, the mix of lower oil prices and weaker prospects of global growth suggest a shallower path for inflation across the globe in the near term, with widening output gaps slowing the pace of core inflation, and lower oil and commodity prices providing a drag on headline inflation.

Because the peculiarities of the economic fallout, targeted fiscal, monetary, and financial market measures are being deployed to support affected households and businesses domestically.

Monetary policy across the globe has swiftly responded to the emergency, tackling the situation with new tools and instruments, acting to provide liquidity to markets and the financial system. The Federal Reserve has cut its main policy rate back to zero, using all its firepower on rates, cutting by a cumulative 150 bp, while providing coverage of huge fiscal needs through unlimited QE. The ECB took several steps and ultimately delivering a strong package. It acted on preannounced targets, providing ample liquidity to the financial system, and delivering a huge increase in QE2 and de facto ceiling intra-EMU spreads, and providing support to governments' higher funding needs.

The fiscal response has been sizable in most advanced economies, and many emerging markets economies have also begun announcing significant fiscal support for sectors that have been hit. Measures aim at reducing the impact on the hardest-hit households and businesses,

while preserving economic relationships and activities as the pandemic outbreak forces lockdowns. The size of tools depends on the fiscal room available at the national level, although in the Eurozone a more coordinated effort is gradually shaping up.

Investment Phazer medium-term implications: a contraction followed by a recovery supported by massive policy coordination and eventually a late cycle, or potentially asset reflation, should central banks continue to expand their balance sheets. The first phase is characterized by a preference for cash, Govies, IG under the central banks' and gold.

The next step will be to move to EM equity (first-in, first-out), base metals and HY, as soon as the profit cycle bounces back, while the latter stage will be broadly repositioning in DM equities and the full credit spectrum.

The pandemic outbreak altered the cycle of financial regimes we had in mind at the end of 2019...

Given our macroeconomic assessment, we expected a financial regime of “contraction”, but the pandemic's consequences will persist over the medium term (three years), changing the financial cycle until 2022. In 2021 we shall see a “recovery” phase in growth and a profits cycle supported by relief in economic activity (changing our previous expectations of an economic slowdown and a profit recession to take place in 2021). In 2022, we expect a normalization towards a late cycle. Should central banks persist in their accommodative stance (primarily through balance sheet expansion), we could even move into an asset reflation regime (similar to 2013-17).

... while current risky assets prices, multiples and valuations are not pricing in the profits recession we now expect for 2020. The forthcoming reporting season will be highly uncertain but crucial in sizing the Covid-19 damages to the real economy. We expect a free fall in 1H20, followed by a partial recovery in 2H20, driven by a gradual global lockdown easing.

The final outcome should be a deep profits' recession. In our central case, we expect S&P 500 EPS to fall by -25% in 2020 (the duration of lockdowns will be key), followed by a rebound of the same size in the following 12 months. The exceptional nature of the

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recession, the biggest and fastest since the Great Depression, should help bring about a faster recovery than has usually happened in the past.

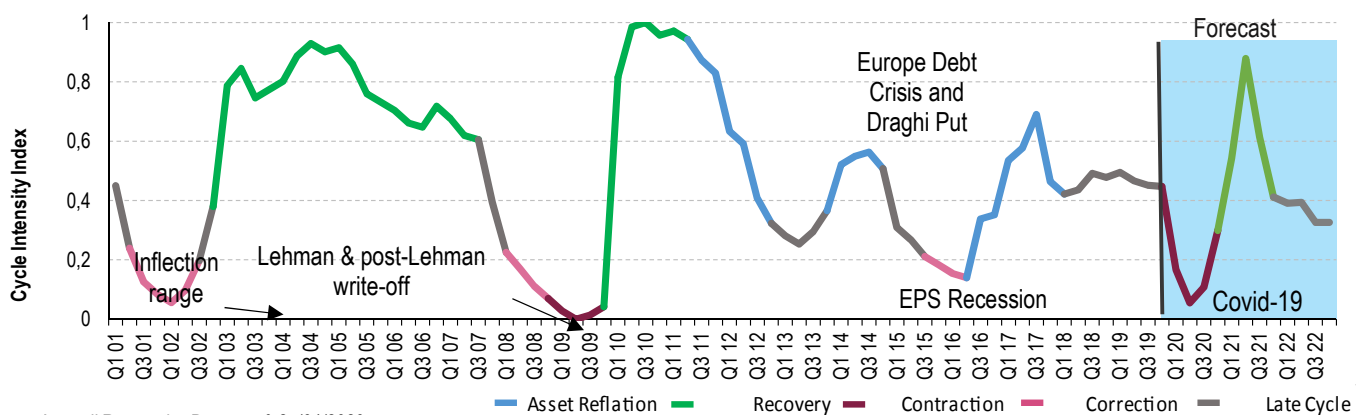
The resilience of earnings and markets sentiment would help equities making new highs in 2021-22 without stretching valuations.

2021 operating EPS are expected to be resilient and higher than before the global economic lockdown. We expect the S&P 500 to recover in 2021 by around 25% in line with the rebound in profits. We believe the index

could drift higher in 2022 as well, although at a more normalized rate (close to +8%). Therefore the risk is skewed to the upside, and the average returns (post the 1Q20 correction) on a three-year horizon should be close to double digits. This scenario with a combination of EPS rebound and S&P 500 making new highs is consistent with past bounce-backs after equity corrections, and the expected PE will move to the median of historical realized PE. Markets will not be expensive in relative value terms either, as interest rates should remain low helping credit to deliver good risk-adjusted returns.

1/ Medium term view: advanced investment phazer

A contraction followed by a recovery supported by massive policy coordination and eventually a late cycle, or potential asset reflation, should central banks continue to expand their balance sheets.



Source: Amundi Research - Data as of 25/04/2020

Financial regime mapping according to the investment phazer

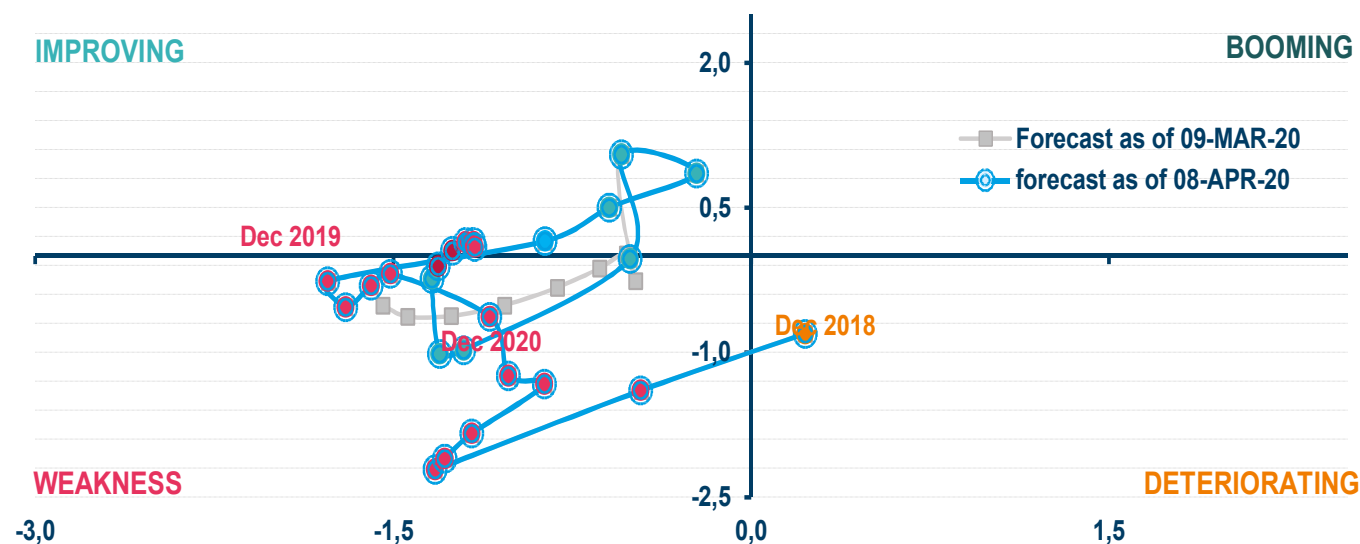
Financial regimes	Macroeconomic parameters behaviour				Investment implications	
	Growth	Inflation	Monetary Policy	Financial Conditions	Cross Asset Evidence	Cross Asset Preference
Slowdown	<ul style="list-style-type: none"> Growth below trend level Below trend EPS growth 	<ul style="list-style-type: none"> CPI, PPI below trend Falling ULC YoY growth 	<ul style="list-style-type: none"> Easy conventional MP CBs balance sheet growth at trend levels 	<ul style="list-style-type: none"> Financial conditions start to be tighter 	<ul style="list-style-type: none"> Global equity suffer IG preferred to HY in credit Gold good hedge Volatility increases 	<ul style="list-style-type: none"> Govies Gold Investment Grade
Contraction	<ul style="list-style-type: none"> Growth far below trend level Falling EPS 	<ul style="list-style-type: none"> Inflation far below trend 	<ul style="list-style-type: none"> CBs very accommodative Excessive CBs balance sheet growth 	<ul style="list-style-type: none"> Tight financial conditions 	<ul style="list-style-type: none"> Credit and global Equity unattractive Safe to quality Lack of trust High volatility 	<ul style="list-style-type: none"> Cash Gold Govies
Asset Reflation	<ul style="list-style-type: none"> Growth at trend level Above trend EPS growth 	<ul style="list-style-type: none"> Inflation below trend 	<ul style="list-style-type: none"> CBs very accommodative Excessive CBs balance sheet growth 	<ul style="list-style-type: none"> Easy financial conditions 	<ul style="list-style-type: none"> Global Equity rises Bond yields fall Most assets do well Volatility stays low 	<ul style="list-style-type: none"> Global Equity High Yield Commodities
Recovery	<ul style="list-style-type: none"> Growth expanding far above trend level Strong EPS growth 	<ul style="list-style-type: none"> CPI, PPI above trend levels Above trend ULC YoY growth 	<ul style="list-style-type: none"> Tight conventional MP CBs balance sheet growth below trend level 	<ul style="list-style-type: none"> Easy financial conditions 	<ul style="list-style-type: none"> Risky assets the most attractive Commodities and EM Equity rally High volatility 	<ul style="list-style-type: none"> High yield Base Metals EM Equity
Late Cycle	<ul style="list-style-type: none"> Growth expanding slightly above trend level EPS consolidation 	<ul style="list-style-type: none"> Inflation rises towards targets 	<ul style="list-style-type: none"> CBs correction (less easing) 	<ul style="list-style-type: none"> Easy financial conditions 	<ul style="list-style-type: none"> Bond yields rise Global equity consolidates HY rotation into Equity Volatility Increases 	<ul style="list-style-type: none"> DM Equity Investment Grade High Yield

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2/ Short term view: Global composite economic momentum

Economic momentum : Swinging around the Investment Phazer

On a shorter term perspective, the pandemic triggered a sequence of “pain”: our Composite Economic Momentum Index (CEMI) dropped into the “weakening” quadrant on soft data collapse in Asia and moved even deeper as the pandemic outbreak in Europe. The negative EPS revisions touching historical lows leave little hope of improvement, in 2020. This is consistent with the contractionary financial regime flagged by the Investment Phazer.

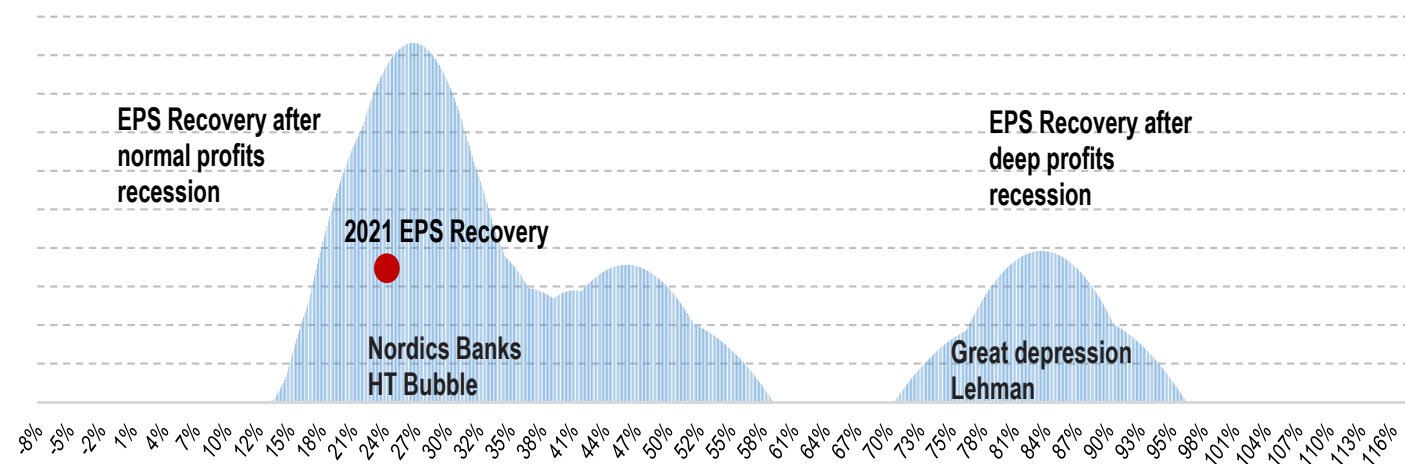


Source: Amundi Research - Data as of 10/04/2020

The Global Economic Momentum index is an Amundi proprietary indicator based on four regional baskets (US, Eurozone, Japan and EM) and on the following variables: earnings revisions, 10Y interest rates, leading indicators, CPI YoY, PMI surveys, the Economic Surprise Index and the Inflation Surprise Index. We consider the level and the momentum (variation) of the index in order to define four economic cycles: **Booming**: uptrend level and positive momentum; **Deteriorating**: uptrend level and negative momentum; **Weakness**: downtrend level and negative momentum; **Improving**: downtrend level and positive momentum.

3/ The magnitude of profits recovery in 2021 will depend on 2020 pain

From an empirical perspective, EPS recoveries are bimodal and anchored to two pivots linked to the magnitude of the preceding recessions. In the US, a profit recession in the -25% range is followed by a rebound of a similar amount. We expect to confirm this pattern in 2020/21. Besides, larger losses (below - 50%) had historically been followed by rebound of around 85%.

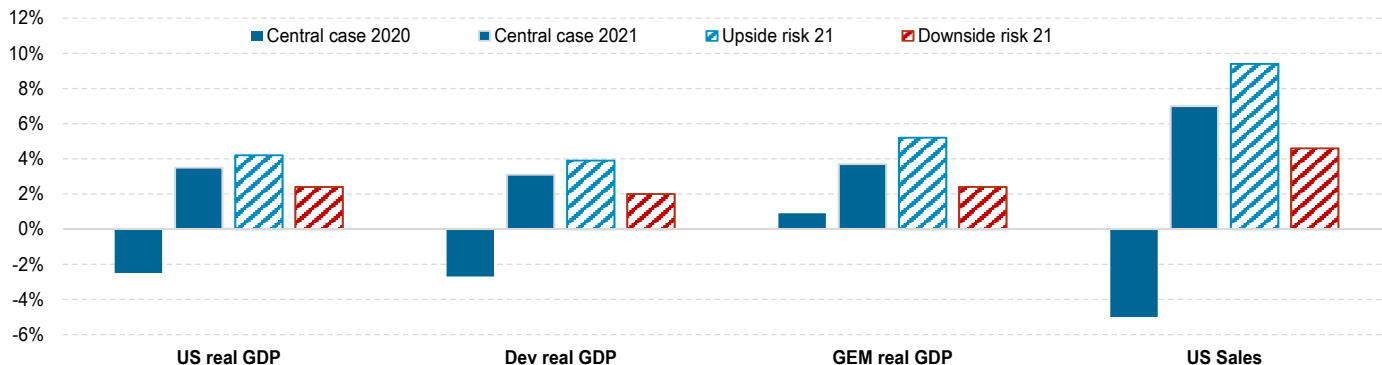


Source: Amundi Research - Data as of 24/04/2020

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4/ Growth under central and alternative scenarios

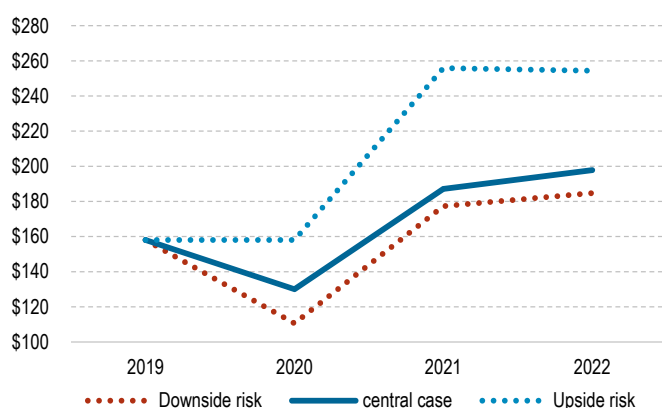
Growth is expected to recover in 2021 to potential in the US and Developed Economies but still below potential in Emerging Economies. While guidelines remain uncertain, we expect the top line to improve eventually.



Source: Amundi Research - Data as of 24/04/2020

5/ S&P 500 aggregate earnings simulation

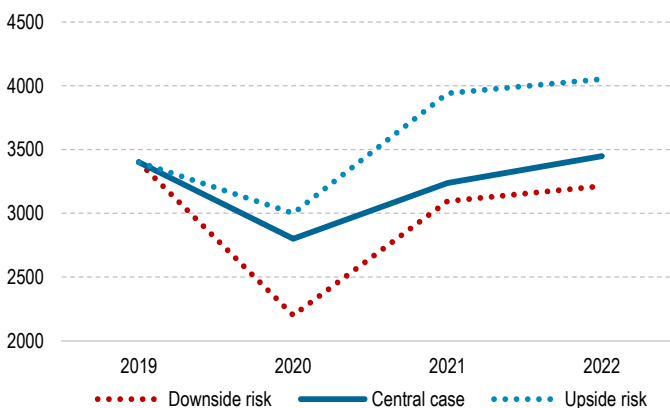
S&P 500 2021 EPS are expected to be resilient and to move higher than before global economic lockdown.



Source: Amundi Research - Data as of 24/04/2020

6/ S&P 500 levels simulation

We expect the S&P 500 to recover in 2021 by 25% in line with the rebound of profits and to drift even higher in 2022, albeit on a more normalized pace (+8%). The risk is skewed to the upside.

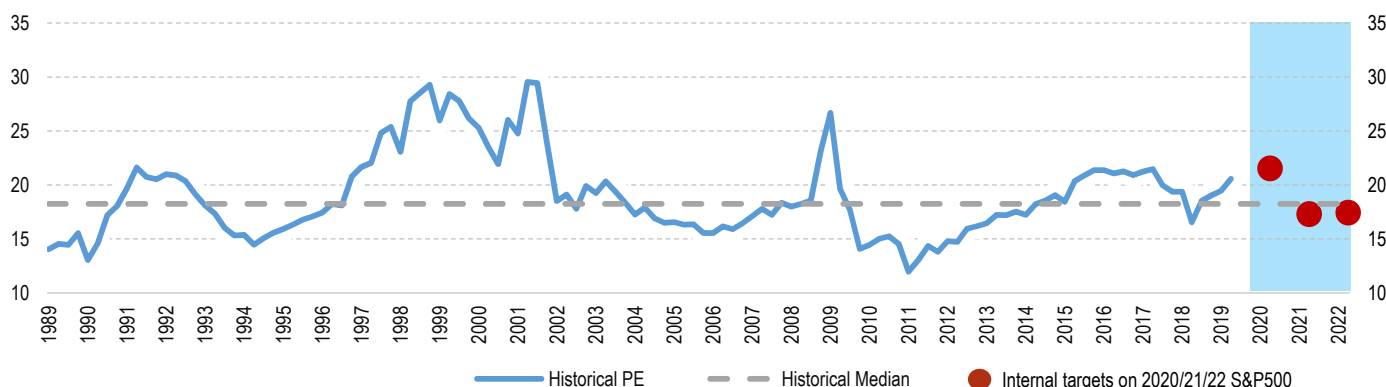


Source: Amundi Research - Data as of 24/04/2020

Methodological note: LTM EPS simulation is the outcome of patterns generation based on the sequence of identified phases by Amundi's Research proprietary tool AIP. The downside and upside are calculated according to the simulated distribution centered on the central case scenario.

7/ S&P 500 price earnings (historical and targets)

Combining our expectations on EPS and S&P500 levels, we expect PEs to move back to the historical realized median. Consistently with past dynamic, a spike is likely on the bounce back once equity market corrects.



Source: Amundi Research - Data as of 24/04/2020

Operating S&P500 PE (Actual) is defined as the ratio S&P500 level / Realized Operating LTM EPS
Historical median: Historical median of Operating S&P 500 PE (Actual), sample: 1989-2019

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Implication for the labour market: key to assess the shock size on the demand side

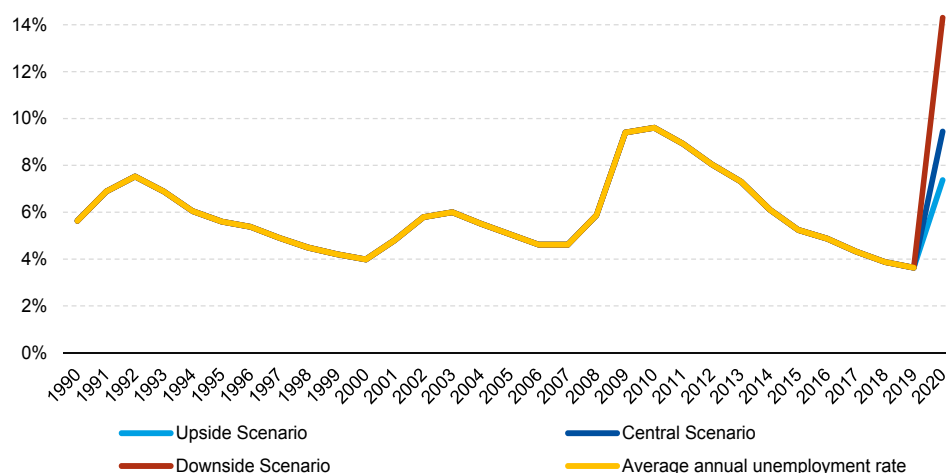
While different timelines of the outbreak and related containment measures point to a jerky recovery, with the risk of possible setbacks should a second epidemic/lockdown wave occur, single economies are facing double shocks, both domestic and external. On the domestic front, major concerns are related to the vulnerability of the labour market, with implications on disposable income, spending and saving patterns in both the short and longer term. In addition, the path for capex remains highly uncertain while disruptions to local and international production chains will affect imports/export dynamics and global trade overall.

Of particular concern is the impact of the lock-down measures on the employment front. Indeed, many workers employed in temporary jobs and in so-called "proximity" activities are at risk of seeing their jobs eliminated or their hours reduced. In the US, the surge in jobless claims since the first lockdown measures has been unprecedented, and in few weeks wiped out all jobs created in a decade of economic expansion. For the US economy, this should translate into an increase in unemployment, which could spike temporarily to a range 14% to 20% and then revert to more moderate rates as the economy reopens. We expect the US unemployment rate to average approximately 10% in 2020, and then gradually revert towards the NAIRU. However, to see a reversal in the unemployment trend, we will need to see a rebound of the corporates' profits first.

In the Eurozone, to prevent a surge in unemployment, national governments have made some extraordinary schemes available to a broader than usual group of companies, which agree to avoid laying off any of their employees but instead reducing the working hours of all or most of them, with the government making up some of the employees' lost income. This is particularly important in Eurozone where the labour market ability to adjust to the down cycle and to recover afterwards may be slower. The German Kurzarbeit plan is the ideal reference, and the more effective that national plans are in replicating this model, the less likely unemployment will jump well beyond the levels seen after the GFC and sovereign debt crisis. In a case of only partial effectiveness and deep contraction in activity, in line with our central case, we could see unemployment rise to between 8.5% and 25%, depending on the countries, as pre-crisis starting points were different. Most vulnerable labour markets, such as Spain and Italy, may pay the higher costs of ineffective implementation of such workers protection schemes.

US unemployment projections under various scenarios

In the US, the surge in jobless claims since the first lockdown measures has been unprecedented and in few weeks wiped out all jobs created in a decade of economic expansion.



Source: Amundi Research - Data as of 24/04/2020

The shock on the demand side, in regions where labour is less flexible as employees are on average more protected, such as in the Eurozone, might materialize later, delaying the recovery. This is why we welcome the SURE plan approved by the EU commission to temporary support and mitigate unemployment risks.

Finalised on 24/04/2020

CENTRAL & ALTERNATIVE SCENARIOS

Monthly update

We maintain the overall pandemic narrative confirming the probabilities, assigned to the base and alternative scenarios.

DOWNSIDE SCENARIO

L shaped

20%

- **Pandemic extended up to mid-2021**, with slow medical advances and a second round of outbreaks late 2020
- **National lockdowns measure are extended** as fatalities increase
- **Deep and long global recession leads to a depression.** Demand and economic activity collapse, even beyond the direct impact of the public health emergency
- **Full debt monetisation** worldwide with ballooning public debts and rising CB balance sheets
- **Loss of potential output** on collapsing businesses
- Long period of **financial repression** (through regulation and zero-interest-rate policies)
- **Massive bankruptcies and mounting costs of collapsing businesses** undermine confidence in the banking sector and lead to financial instability
- **Secular stagnation** comes back to the fore and **de-globalisation is the new norm**

CENTRAL SCENARIO

Base shaped

50%

- Temporary but prolonged shock:
 - **the pandemic is not over end 2Q20** (falling death rate, but the disease doesn't disappear)
 - thanks to national **lockdowns limited in time** (3-months max), the epidemic is finally under control in late Q3
 - health and economic crises in vulnerable emerging markets (Africa and South Asia)
- **Global deep recession in Q1, Q2 and Q3 2020**
- **Slow recovery beginning in 4Q20** (hysteresis effects and sluggish growth), followed by a **rebound in 2021** (mostly driven by the base effect and stimulus packages)
- Governments and CBs "**Bazooka**" policies fail to calm animal spirits (fear factor) in the short run (Q2) but **preserve incomes and businesses**
- **Corporate defaults surge in 2020** with tighter financing conditions and declining profits, coupled with the oil-price fall. Deep fragmentation of credit markets and solvency issues
- The **reversal in the manufacturing sector lags the reversal in services**
- **The Chinese recovery** is curbed by weaker demand from the RoW
- Some stagflationary forces materialise (**de-globalisation**)

UPSIDE SCENARIO

U shaped

30%

- **Time-limited shock, the pandemic** is under control in 2Q20
- **Deep but short-lived recession** mainly in 1H2020
- Global central banks and fiscal **coordinated actions** support the restart of the economy which heads back to its pre-crisis level
- **Reversal** of the manufacturing sector and services
- **Limited number of corporate defaults** thanks for government supports and central bank liquidity measures
- Pent-up demand materialises
- **Above potential growth in 2021**, and possibly in some countries as early as 2H2020

Where do we stand on Covid-19







The potential easing of lockdown measures bring some light at the end of the tunnel. This is particularly the case in Europe where several countries are opening back shops, manufacturing capabilities or services. **Data show that the worse is probably over** in Italy and France for instance, but in the US, many states such as New York remain in an acute phase of the outbreak. Moreover, **emerging countries are still at the beginning of the pandemic**. Although it is too early to draw a conclusion, the low level of death toll registered so far in Africa gives hope for a more benign impact than feared. On one hand, these countries' infrastructures will make the disease more difficult to fight but on the other hand, EM demographics are more favourable. Going forward, the lack of tests make the **statistics less and less reliable**.

The total number of deaths directly linked to the virus are significantly underestimated according to recent studies. Therefore, we still ignore the magnitude of the outbreak at the global level. The situation seems to be **stable in China** where feared of a second wave remain. As constraints measures starts to unfold, many questions remain unanswered: Is the **collective immunity** sufficient to avoid a sharp pick up in cases once we reduce confinement measures? Are we going to see a second wave? If so, will it be smaller or bigger than the first? **It is reasonable to assume that Covid-19 will not disappear anytime soon**, and will remain a source of risk until a medical treatment appears.

TOP RISKS

Monthly update

Risks are clustered to ease the detection of hedging strategies but they are obviously linked. While we confirm the overall narrative on the outlook, pandemic exacerbated existing fragilities and vulnerabilities while more risks materialized in our radar: financial and geopolitical risks' probabilities are set to creep higher.

ECONOMIC RISK	FINANCIAL RISK	(GEO)POLITICAL RISK
10% Probability	15% Probability	15% Probability
Depression	Financial instability	Covid-19 exacerbates political tensions
<ul style="list-style-type: none"> – The pandemic continues with a second outbreak and rising fatalities – A deep, long global recession: demand and economic activity collapse and national lockdowns remain for more than six months – Loss of potential output as businesses collapse – Debt burden exacerbated by emergency fiscal policies and liquidity injection to overcome the coronavirus drawdown – Rising default risk on small countries single commodity exporters (i.e. oil) and strongly dependent on touristic flows 	<ul style="list-style-type: none"> – Mounting corporate vulnerability, solvency issues, and increase of default risks (>15 or even 20%) – Spill over into the banking sector and financial risk exacerbation with a large number of defaults due to global recession and financial instability – Credit illiquidity and risk misallocation – USD liquidity drought – Central bank policies inefficacy: UST long-term bond yields to rise despite the Fed QE with low pick-up in the primary markets (the same may occur in Europe) – Rating downgrades, Balance of Payment crisis and at the worst credit default as a result of excessive policy easing on existing fiscal and external vulnerabilities 	<ul style="list-style-type: none"> – US elections: Trump poorly handling the pandemic national emergency might revert the course of presidential election while no electoral campaign will take place – Economic and national security interests (and objectives) arising from a revival in the coronavirus, lead to a new wave of trade conflicts – Failure of Eurogroup's deal, anti-establishment parties take the lead (mainly a European risk) – The UK is moving to hard Brexit – US-China fissures are opening up in many areas of crisis response, from debt relief plans to WHO funding – Open oil war – North Korea and KJU health risk: unintended escalation on bumpy power transition
<div> Cash, linkers, USD, Defensives vs. Cyclical</div> <div> Oil, risky assets, FX commodity, EM local CCY exporters</div>	<div> CHF/AUD, YEN (AUD, NZD, CAD), CDS, optionality, Min Vol</div> <div> Oil, risky assets, frontier markets and capital outflows</div>	<div> DM Govies, cash, gold, linkers, USD, volatility, quality</div> <div> Oil, risky assets, EMBI</div>

Methodology

– Scenarios

The probabilities reflect the likelihood of financial regimes (central, downside and upside scenario) which are conditioned and defined by our macro-financial forecasts. We use the k-means clustering algorithm to our enlarged macroeconomic dataset, splitting the observations into the K cluster, where K represents most of the variability in the dataset. Observations belong to one cluster or another based on their similarities. The grouping of the observations into the k clusters is obtained by minimizing the sum of squared Euclidean distances between observations and clusters centroids i.e. the reference values for each cluster. The greater the distance, the lower the probability to belong to a given regime. The GIC qualitative overlay is finally applied.

– Risks

The probabilities of risks are the outcome of an internal survey. Risks to monitor are clustered in three categories: Economic, Financial and (Geo)politics. While the three categories are interconnected, they have specific epicentres related to their three drivers. The weights (percentages) are the composition of highest impact scenarios derived by the quarterly survey run on the investment floor.

CROSS ASSET DISPATCH: Detecting markets turning points

How to the read turning point assessment

- Not reached yet too early to call it
 ● Approaching to the turnaround
 ● Turnaround happened

ECONOMIC BACKDROP

- Global growth contraction in Q1-Q3 2020 followed by a bounce-back sequence in 2021.
- Economic momentum based on soft-data indicators pencil in the same "Weakening" flash with some differences: US/EZ/China nit distance from the bottom, Row in transition phase.
- Covid-19 outbreak has stretched global financial conditions. Despite central banks' efforts, investors' "perceived" liquidity is under stress but far higher than the lows seen during the Global Financial Crisis.

FUNDAMENTALS & VALUATION

- We expect earnings to drop in Q2, Q3 this year and to bounce back in 2021.
- Despite recurrent downward revisions, we believe consensus EPS expectations remain far too high.
- Valuation: PEs are far from flagging potential entry points (S&P500's PE @ 15 and Euro Stoxx 600 PE @ 13 2020).



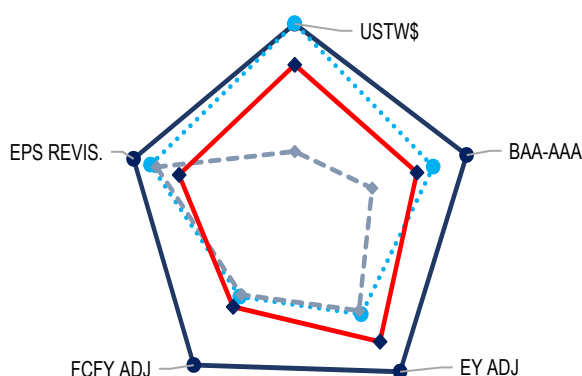
TECHNICALS

- Price Momentum signals turned mildly constructive on building back some risk exposure during the first week of April. However, this has not been followed by a broader Risky Assets improvement on a more medium-term perspective.
- Dislocation strategies remain profitable (since end of March). However, there are some selected pockets of dislocation that continue to underperform (oil in particular).

SENTIMENT

- Despite markets retracing, our overall assessment on risk sentiment remains negative. Financial conditions improved only at the margin with unclear direction. The credit risk premium remains high despite the spread tightening in response to the Fed's umbrella on Fallen Angels. EPS revisions are negative and the USD strength vis a vis the broader FX spectrum acts as a headwind.
- Flow-based sentiment metrics, tracking institutional investors' risk appetite, show some attempts to reposition in search for a potential bottom in the defensive spectrum, "barbell" risk in a relative positioning.

Cross Asset Sentinels Thresholds (CAST) touching the top



Source: Amundi Research - Data as of 24/04/20

CAST flags extremely high risk perception.

Sentinels wave above the top on persistent stress in the low-quality credit names as flashed by the Moody's spread (AAA↓↓, Baa↓). EPS revisions continue to run downwards touching all-time lows.

Methodology We consider five inputs which we call "Sentinels": USTW\$, Moody's Baa-Aaa, EPS revisions, Earning Yield risk adjusted and Cash Flow yield risk adjusted. These sentinels are used to reposition our tactical asset allocation. Once sound thresholds are detected, the five variables are aggregated as an indicator that anticipates the market's stress conditions, with a certain level of conviction. The pentagon visualises the five sentinels where the red line represents the alert threshold. The greater the distance above the red line, the higher the risk perception, and eventually the need to move closer to a defensive asset allocation.

GLOBAL RESEARCH CLIPS

- 1** **The big picture:** The pandemic outbreak has altered the financial regime cycle we had in mind at the end of 2019. We now expect a **contraction** (central bank and government support, a recession, and rising unemployment), followed by a **recovery** later in 2021 (economic activity retracing back but below 2019 levels, rising labour costs, and cooling down of monetary and government actions), which would eventually land in a **late cycle** in 2022 (or potentially an asset reflation regime, should central banks remain ultra-supportive). The first phase is characterized by a preference for cash, govies, IG under the CB umbrellas, and gold. The following step will be to move to EM equity (*first-in, first-out*), base metals and HY as soon as the profit cycle bounces back while the last stage will be a broad repositioning in DM equities and the full credit spectrum.
- 2** **Economic backdrop:** a global recession with sequencing drawdown and diverging recovery path. The length of the weakness and the extent of permanent output loss and demand destruction will depend on how long the lockdowns last, only partially compensated by central bank and government actions. The recovery will lead to de-synchronized paths in three blocks: China/South Asia, US/Europe and developing countries, each producing specific investment opportunities.
 - **Labour** markets will be key to assessing the final shock to domestic demand. Unemployment is expected to rise to levels not seen in the past 50 years, if policies and schemes to support reduced hours workers fail to produce their intended effects. Most vulnerable are Italy and Spain, whose labour markets are more exposed to temp workers, sectors at risk (tourism-related), and those that still have not fully recovered from 2012 crisis. Among EMs, the larger the informal sector, the more pronounced the shock.
 - **China first-in-first-out.** Policy has tilted towards further easing to cope with downside (exacerbated by weakening global demand).
 - Covid-19 is exacerbating **EM fragilities** on rising debt, increasing external vulnerability and oil dependency. Fiscal and reserves buffers are favouring Russia, South Korea, the Philippines and Peru.
- 3** **Global liquidity** started to increase in Q2 2019, with the Fed back on a rate-cut course and eventually entered cross-border banking circuits. However, **liquidity as perceived by market participants remains tepid**. In fact, global financial conditions, while far from GFC levels, have bottomed out in 2020 and corrected only marginally, notwithstanding the massive monetary policy efforts.
- 4** **Italy:** Covid-19 and lockdowns will be a drag on GDP that we expect to revert back to pre-crisis levels in 2022 in our base case. The debt/GDP path will depend on growth, the average cost of debt and the primary balance. **PEPP** (flexibility on capital key and no issuer limit) will **support short-term financing needs**. The ECB has around €100-120bn of firepower for buying BTPs and will absorb the €55bn of new net issuance for 2020 very easily (including €25bn of new fiscal measures). In the **medium term, Italy will take more than 10 years to revert back** to its 2019 debt/GDP level. Rating agency actions will depend on the policy response.

Stimulus packages - Update

The **large fiscal packages** announced by governments to counter the virus crisis aim, so far, at stabilizing more than stimulate economies. In addition to **funding emergency response** to the virus situation itself, these packages intend to prevent a worsening of the crisis through the financial and household income channels. Only part of the amounts recently announced by governments are budget easing measures under a strict definition. On these, there is a larger push in the US and Japan than in Europe so far. Other amounts are advances meant to be reimbursed, or (for the largest amounts) government guarantees to corporate debt.

Regarding **guarantees**, the European push is, at this stage, much larger than the US one. Within the specific architecture of the Euro area, **European institutions have also played a major part**, by lifting restrictions so that member states can deploy their national program. A European-level mutualized response is also under way, with a number of programs already decided and larger ones currently being negotiated.

The combined effect of the recession and the whole array of above-mentioned measures on deficits and debt could be, very roughly for large advanced economies given the many unknowns, a **7% to 15% of GDP deficit increase and a 15% to 25% of GDP public debt increase in 2020**. However, the public debt sustainability of large advanced economies may not be that damaged by the crisis, due to the large QE programs announced by central banks that will monetize the additional debt. Yet, the recently announced stabilization-aiming fiscal measures are not the end of the fiscal easing chapter opened by the crisis. Indeed, they will probably give way to further measures, this time stimulus-oriented, once the confinement measures are gradually lifted. It is also very probable that some of the crisis-fighting fiscal measures, currently presented as temporary will become more or less permanent due to demands of a stronger government role in the economy, and stronger social safety nets. If not matched by offsetting revenue-raising measures, they **may lead to permanently higher structural primary deficits**.

* See forthcoming Thematic Paper by Tristan Perrier

AMUNDI ASSET CLASS VIEWS

	Asset Class	View	1M change	Rationale
EQUITY PLATFORM	US	-/=		The current rebound was warranted after the quick sell-off between Feb and 23 March. But there are concerns as we enter the earnings season because companies are not giving guidance for the rest of the year as visibility on the extent of the economic lockdown impact of the virus is extremely low. We maintain a cautious stance as we expect earnings to come down further.
	Europe	-/=		Earnings visibility is low and the range of outcomes is wide. As a result, we do not feel confident of the recent recovery. The crisis offers attractive stock selection prospects but is producing higher than usual uncertainty and volatility, leading to dislocations in some parts of the market. We prefer companies with strong balance sheets.
	Japan	=		Japanese balance sheets remain underleveraged and valuations are also attractive. But companies' earnings are likely to be affected by the global economic slowdown. As a result, we stay neutral.
	Emerging markets	=		We maintain our relatively defensive stance but we are observing positive signs in countries that are in the later stage of the coronavirus cycle. In particular, we like countries with strong fiscal buffers, domestic bases and lower external vulnerabilities. However, we avoid names dependent on export, commodities and tourism.
FIXED INCOME PLATFORM	US govies	=/+		Demand for safe haven assets is supportive for US govies. The ultra-loose monetary policies of central banks are likely to keep core bond yields range-bound. UST yields appear close to fair value and the Fed's monetary response eased liquidity constraints in the second half of March.
	US IG Corporate	=/+		The IG market has been a beneficiary of the Fed's stimulus and we have seen high level of new issues. Importantly, the Covid 19-induced market dislocation has presented long term opportunities across all rating categories, in particular in long maturity IG corporate bonds, which initially underperformed their own equity returns. We remain selective.
	US HY Corporate	-		High leverage, falling oil prices and economic lockdowns due to Covid-19 increase the risk of default in the HY markets, and as a result, we are very cautious. Certain segments of HY corporates offer unique value but require a strong focus on selection.
	European govies	-/=		We are slightly more positive than before on core EU but remain cautious overall. Euro peripheral countries offer attractive yields, although we are now more cautious, in particular on Italy.
	Euro IG Corporate	++		We maintain our constructive view on EUR IG, as it will benefit from the ECB's liquidity backstop and fiscal package, which will reduce migration and default risk. The sector remains relatively less leveraged than US peers. We believe investors should continue to adjust sector allocations to reduce risk from sectors more exposed to a recession.
	Euro HY Corporate	-/=		We favour EUR HY to US where we believe the default rate risk is high. However, we are still very selective overall and looking at industrials sectors such as telecom, media and non-cyclical consumer. Liquidity conditions are stabilising but remain poor in the current market environment.
	EM Bonds HC	=/+		We remain cautious but believe sentiment is improving in terms of asset prices, as well as fund flows. There is some value in HC, particularly in high yield, where spreads have already widened to GFC levels, and there is ample value in Bahrain and Indonesia. Quasi-sovereign debt in Latin America offers attractive risk/reward in Brazil, Mexico and Peru.
	EM Bonds LC	=		Our preference is for EM rates, where we see value in Russian assets in both FX and rates. In Mexico and South Africa, we see value in rates, but not in FX. Overall, countries with strong fiscal buffers will be better able to weather this downturn.
OTHER	Commodities			Cyclical commodities such as oil are not finding any support from the economic backdrop, due to the current global lockdown. While oil prices may benefit from a restoration in economic activities, markets at the moment are discounting a huge structural oversupply and a no recovery scenario. Gold remains the great winner in this framework as it benefits simultaneously from economic uncertainty, increasing government deficits and CB QE purchase programmes.
	Currencies			Despite ongoing concerns on the economic impact that lock/down measures have so far created, CB and government interventions have helped to contain credit risk, and marginally ease financial conditions thus stabilising stock market sentiment. Despite the fact the Fed's strong intervention (conventional and unconventional) should suggest a weaker USD, the greenback remained resilient/strong in the month, with cyclical commodities-related currencies losing the most. As growth differential remains in favour of the US and uncertainty is expected to stay high in the short-term, we think it's worth maintaining USD long for the time being and maybe try to play some reflation trades (anticipating then 2021 outcomes) where dislocations are huge.
LEGEND				
<div> <div>---</div> <div>--</div> <div>-</div> <div>=</div> <div>+</div> <div>++</div> <div>+++</div> <div>▼</div> <div>▲</div> </div> <div> <div>Negative</div> <div>Neutral</div> <div>Positive</div> <div>Downgrade vs previous month</div> <div>Upgraded vs previous month</div> </div>				

Source: Amundi, as of 28 April 2020, views relative to a EUR-based investor. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This information should not be relied upon by the reader as research, investment advice or a recommendation regarding any fund or any security in particular. This information is strictly for illustrative and educational purposes and is subject to change. This information does not represent the actual current, past or future asset allocation or portfolio of any Amundi product.

IG = Investment grade corporate bonds, HY = High Yield Corporate; EM Bonds HC / LC = EM bonds hard currency / local currency. WTI= West Texas Intermediate. QE=quantitative easing.

DEVELOPED COUNTRIES

Macroeconomic outlook

Data as of 7/05/2020						
Annual averages (%)	Real GDP growth %			Inflation (CPI, yoy, %)		
	2019	2020 range	2021	2019	2020	2021
World	3.1	-3.9/-2.4	3.8/5.1	3.0	2.4	2.4
Developed countries	1.7	-7.6/-5.7	3.0/4.7	1.5	0.7	1.0
US	2.3	-6.5/-4.5	2.5/4.5	1.8	1.0	1.0
Japan	1.2	-4.8/-4.3	2.3/2.8	0.7	0.3	0.6
UK	1.4	-8/-6	3.0/5.0	1.8	1.2	1.4
Eurozone	1.2	-10.2/-7.5	3.6/5.6	1.2	0.6	1.1
Germany	0.6	-9.5/-7.5	3.4/5.4	1.5	0.7	1.2
France	1.2	-10.6/-7.0	4.3/6.0	1.3	0.6	1.1
Italy	0.3	-10.7/-7.8	2.9/4.9	0.7	0.2	1.0
Spain	2.0	-10.4/-7.9	3.5/5.5	0.7	0.5	1.0

Source: Amundi Research

- **United States:** Heading towards a sharp contraction in H1; the H2 recovery is being shaped by the duration of the crisis and the effectiveness of the unprecedented policy response, once the post-containment normalization phase starts. Since the start of April, both hard and soft data have begun to show the impact on the economy. In one month, the crisis has erased almost the number of jobs added since the GFC, and unemployment moved up sharply to 4.4% from 3.5% one month earlier. Sentiment plunged across business lines, especially in service and consumer sectors. Retail sales fell the most since 1992. Inflation moderated in March.
- **Eurozone:** The Eurozone economy is entering a recession, as almost all European countries have implemented increasingly strict Covid-19 containment measures, with a significant impact on growth. As hard data releases lag behind, soft data provide an up-to-date indication of a sharp downturn, with manufacturing PMIs remaining in contraction territory and service PMI falling sharply. Preliminary data on March retail sales, in particular car sales, are appalling (car sales declined 56.4% on a monthly basis). Economic data releases over the next few weeks will provide a preliminary assessment of the impact of confinement measures.
- **Japan:** The Japanese economy is expected to sink into a deep recession, as most economies go through a double shock of collapses in both internal and external demand. The soft lockdown imposed by the government in April will weigh further on domestic consumption, after the March contraction likely exceeded the one that came after the 2011 earthquake. Proposed cash handouts will help, but are only expected to be approved by lawmakers in late May or June. As much of the global economy remains under lockdown, we continue to expect a soft trade and business investment outlook.
- **United Kingdom:** The UK economy is set to face a recession expected to significantly drag down H1 economic growth. The shock will play out via domestic and external demand. We forecast a significant contraction in household consumption, in particular in discretionary spending and investments. Business surveys are moving deeper into contraction territory both in manufacturing and services, and the construction industry is also showing significant weakness.

Nota Bene: The uncertainty around our macroeconomic forecasts is very high, and it triggers frequent reassessments any time fresh high frequency data are available. Our forecasts at this point include a higher qualitative component, reducing the statistical accuracy and increasing the uncertainty through wider ranges around them.

Key interest rate outlook

	29-04 2020	Amundi +6m.	Consensus Q3 2020	Amundi +12m.	Consensus Q1 2021
US	0.13	0/0.25	0.15	0/0.25	0.16
Eurozone	-0.50	-0.50	-0.58	-0.50	-0.58
Japan	-0.05	-0.2	-0.11	-0.2	-0.12
UK	0.10	0.00	0.09	0.00	0.14

Source: Amundi Research

- **Fed:** In order to stabilize financial conditions, the Fed moved rapidly into action, making full use of its conventional and unconventional tools:
 - 1) cutting rates by a cumulative 150bp and moving to ZIRP
 - 2) introducing supporting facilities for the CP market and primary dealers' liquidity
 - 3) providing liquidity to the system through massive repos, and acting on banks reserves requirements and capital buffers
 - 4) moving to open QE and to support corporates and ABS through dedicated facilities
 - 5) providing foreign central banks with both dollar swap lines and repos, and
 - 6) extending its support to fallen angels and municipalities
 Liquidity and coverage of extraordinary fiscal financing needs on the fiscal side are the Fed's main objectives.
- **ECB:** The ECB acted in several steps and finally delivered a strong package
 - An overall amount of QE of EUR 1,050tn to be spent just over the next nine months (a triple-digit average monthly path).
 - Lifting of issuer and maturity limits on the public sector QE, increasing flexibility and QE firepower to better cover extra fiscal spending
- **BoJ:** The BoJ joined other central banks in easing, by expanding asset purchase amounts significantly, in order to alleviate financial stress. The BoJ can now purchase JGBs without limit. It also raised purchase constraint for corporate bonds and commercial papers from JPY 1tn to JPY 7.5tn each with a relaxation of the single-issuer share limits. Following this decisive move, we expect the central bank to remain on hold for a while and to refrain from policy rate cuts. A rate cut is seen running counter to the government's epidemic control efforts.
- **BoE:** Like the Federal Reserve, the BoE decided to first deliver an emergency, intra-meeting 50bp rate cut, within a synchronized global easier policy scenario: the rate cut was combined with a later announcement of easier fiscal policy. Following the first decisions, the BoE also announced some days later the launch of a new GBP200bn QE targeting treasury bonds, and cut rates by further 15bp, therefore moving to ZIRP, too.

Monetary policy agenda

Central banks	Next meeting
Federal Reserve FOMC	June 10
ECB Governing Council	June 4
Bank of Japan MPM	June 16
Bank of England MPC	May 7

Source: Amundi Research

EMERGING COUNTRIES

Macroeconomic outlook

Annual averages (%)	Data as of 7/05/2020					
	Real GDP growth %			Inflation (CPI, yoy, %)		
	2019	2020 range	2021	2019	2020	2021
World	3.1	-3.9/-2.4	3.8/5.1	3.0	2.4	2.4
Emerging countries	4.1	-1.4/-0.2	4.4/5.3	4.0	3.6	3.3
Brazil	1.1	-4.5/-3.1	0/1.0	3.7	3.3	3.8
Mexico	-0.1	-4.9/-3.9	-1.2/-0.2	3.6	2.7	2.7
Russia	1.3	-6/-4	2.5/5.0	4.5	3.3	3.9
India	5.3	0.2/1.6	3.4/4.7	3.7	5.3	4.1
Indonesia	5.0	0.6/1.6	3.6/4.6	2.8	2.6	3.2
China	6.2	1.4/2.4	7.6/8.2	2.9	2.7	2.0
South Africa	0.2	-7/-5.8	1.0/2.0	4.1	4.0	5.0
Turkey	0.8	-7/-6	2.8/4.8	15.5	9.8	10.1

Source: Amundi Research

- **China:** The March data reports show that economic activity rebounded from the widespread suspension in February, with manufacturing production recovering at a faster pace than the services sector. We expect the economy to grow 2.3%-3.3% in 2020, as the policy stance has turned more accommodative. Credit growth is expected to firm up along with public spending, with a focus on boosting infrastructure builds. There is more room for monetary policy easing, although a deposit rate cut must wait until the CPI eases back more. The slump in global demand remains the major downside risk.
- **India:** The recovery in economic performance in Jan/Feb has been wiped out by the pandemic and subsequent lockdown. In March, economic data deteriorated sharply across the sectors (electricity generation, vehicle sales, freight traffic and exports). Thanks to substantial moderation in food prices, headline inflation finally dropped back below the target's upper band (5.9% yoy vs. 6.0%) and is expected to fall further. The policy mix is still driven by the RBI, which recently introduced new liquidity measures. The fiscal strategy is not clear yet, though it is very likely that the fiscal targets will be missed due to the ongoing recession.
- **South Africa:** The SARB cut rates by 100bp to 4.25% at a surprise committee meeting. This is the third drop since the start of the year, totalling 225bp. The SARB justified this decision with new forecasts of sharply deteriorated growth (6% recession in 2020) and lower inflation (3.6% in 2020) due to the pandemic. South Africa, which has also been under lockdown measures for a few weeks, is now facing a substantial domestic demand shock. Given that its room for manoeuvre is extremely limited on the fiscal level, the only tool to support activity remains monetary policy.
- **Argentina:** The government finally disclosed its debt restructuring proposal, but the offer has not been accepted by the bondholders. The old debt is to be replaced by new amortising bonds of five different maturities ranging between 2030 and 2047, with a grace period of three years and with significantly lower coupons. This implies an average haircut of 60-70% on coupons and 5% on the principal. Depending on the exit yield used and the bond, the offer translates into recovery values of 25-50% of principal. If a compromise is not reached with the bondholders in the next few weeks, Argentina could default on its debt at the end May following the 30-day grace period on NY law coupon payments due on 22 April.

Nota Bene: The uncertainty around our macroeconomic forecasts is very high, and it triggers frequent reassessments any time fresh high frequency data are available. Our forecasts at this point include a higher qualitative component, reducing the statistical accuracy and increasing the uncertainty through wider ranges around them.

Key interest rate outlook

	27-04 2020	Amundi + 6m.	Consensus Q3 2020	Amundi + 12m.	Consensus Q1 2021
China	3.85	3.65	3.65	3.65	3.85
India	4.4	3.9	3.95	3.9	3.95
Brazil	3.75	3	3	3	3.1
Russia	5.5	4.5	5.15	4.5	5.1

Source: Amundi Research

- **PBoC (China):** In light of the challenging global demand outlook and the risks of a second outbreak, the latest Politburo meeting on 17 April explicitly spelled out that RRR and interest rates should be cut further. We expect the PBoC to "catch down" with interbank market rates in the coming months, cutting OMO and 1-year LPR by a similar amount, although the pace will be controlled and measured. A benchmark deposit rate cut is still on the table, but has to wait until headline inflation eases more as policymakers link it to social welfare issues.
- **RBI (India):** On 17 April, on the back of the economic assessment, the RBI announced a series of extraordinary measures aiming at improving liquidity management (TLTRO2, refinancing facilities and a further reduction of the Fixed Rate Reverse Repo Rate by 25bps to 3.75%). Regulatory measures have also been introduced to reclassify non-performing assets, to extend the resolution timeline, to stop bank dividend payouts until further notice, and to temporarily reduce the liquidity coverage ratio.
- **BCB (Brazil):** The latest Focus Survey published by the BCB (on 17 April) is reporting a faster deterioration in the growth outlook and lower headline inflation. According to the same survey, the SELIC rate target by the end of the year is now 25bps lower than the previous one at 3.0% (currently at 3.75%). On 15 April, the Senate approved a constitutional amendment that, among other things, allows the BCB to buy and sell public and private securities on the secondary markets (QE).
- **CBR (Russia):** On 24 April, the Central Bank of Russia cut its policy rate by 50bps to 5.5% and announced that it had switched to an accommodative monetary policy. It remains open to further rate cuts. The disinflationary pressures from weak demand outweigh temporary pro-inflationary factors such as the weakening rouble. Annual inflation is expected to reach 3.8-4.8% by year-end, and then fall to 4%, which is the target of the CBR. The CBR also revised its macro forecasts for 2020-21. Given the expected deceleration in economic activity, we expect the CBR to cut rates by 100bps by year-end.

Monetary policy agenda

Central banks	Next communication
PBoC	May 20
RBI	June 5
BCB Brazil	May 6
CBR	June 19

Source: Amundi Research

MACRO AND MARKET FORECASTS

Macroeconomic forecasts

(7 May 2020)

Annual averages (%)	Real GDP growth %			Inflation (CPI, yoy, %)		
	2019	2020 range	2021	2019	2020	2021
US	2.3	-6.5/-4.5	2.5/4.5	1.8	1.0	1.0
Japan	1.2	-4.8/-4.3	2.3/2.8	0.7	0.3	0.6
Eurozone	1.2	-10.2/-7.5	3.6/5.6	1.2	0.6	1.1
Germany	0.6	-9.5/-7.5	3.4/5.4	1.5	0.7	1.2
France	1.2	-10.6/-7.0	4.3/6.0	1.3	0.6	1.1
Italy	0.3	-10.7/-7.8	2.9/4.9	0.7	0.2	1.0
Spain	2.0	-10.4/-7.9	3.5/5.5	0.7	0.5	1.0
UK	1.4	-8/-6	3.0/5.0	1.8	1.2	1.4
Brazil	1.1	-4.5/-3.1	0/1.0	3.7	3.3	3.8
Mexico	-0.1	-4.9/-3.9	-1.2/-0.2	3.6	2.7	2.7
Russia	1.3	-6/-4	2.5/5.0	4.5	3.3	3.9
India	5.3	0.2/1.6	3.4/4.7	3.7	5.3	4.1
Indonesia	5.0	0.6/1.6	3.6/4.6	2.8	2.6	3.2
China	6.2	1.4/2.4	7.6/8.2	2.9	2.7	2.0
South Africa	0.2	-7/-5.8	1.0/2.0	4.1	4.0	5.0
Turkey	0.8	-7/-6	2.8/4.8	15.5	9.8	10.1
Developed countries	1.7	-7.6/-5.7	3.0/4.7	1.5	0.7	1.0
Emerging countries	4.1	-1.4/-0.2	4.4/5.3	4.0	3.6	3.3
World	3.1	-3.9/-2.4	3.8/5.1	3.0	2.4	2.4

Key interest rate outlook

Developed countries

	29/04/2020	Amundi + 6m.	Consensus Q3 2020	Amundi + 12m.	Consensus Q1 2021
US	0.13	0/0.25	0.15	0/0.25	0.16
Eurozone	-0.50	-0.50	-0.58	-0.50	-0.58
Japan	-0.05	-0.2	-0.11	-0.2	-0.12
UK	0.10	0.00	0.09	0.00	0.14

Emerging countries

	27/04/2020	Amundi + 6m.	Consensus Q3 2020	Amundi + 12m.	Consensus Q1 2021
China	3.85	3.65	3.65	3.65	3.85
India	4.4	3.9	3.95	3.9	3.95
Brazil	3.75	3	3	3	3.1
Russia	5.5	4.5	5.15	4.5	5.1

Long rate outlook

2Y. Bond yield

	29/04/2020	Amundi + 6m.	Forward + 6m.	Amundi + 12m.	Forward + 12m.
US	0.21	0.25/0.5	0.27	0.25/0.5	0.32
Germany	-0.694	-0.70/-0.50	-0.73	-0.70/-0.50	-0.75
Japan	-0.172	-0.30/-0.20	-0.19	-0.30/-0.20	-0.18
UK	0.054	0/0.25	0.04	0/0.25	0.08

10Y. Bond yield

	29/04/2020	Amundi + 6m.	Forward + 6m.	Amundi + 12m.	Forward + 12m.
US	0.61	0.5/0.7	0.70	0.8/1	0.77
Germany	-0.47	-0.8/-0.5	-0.43	-0.50/-0.30	-0.40
Japan	-0.04	-0.10/0.10	0.00	0/0.2	0.05
UK	0.29	0.20/0.4	0.31	0.4/0.6	0.38

Currency outlook

	24/04/2020	Amundi + 6m.	Consensus Q3 2020	Amundi + 12m.	Consensus Q1 2021
EUR/USD	1.082	1.07	1.10	1.14	1.14
USD/JPY	108	106	107	105	108
EUR/GBP	0.88	0.92	0.88	0.85	0.87
EUR/CHF	1.05	1.05	1.06	1.10	1.08
EUR/NOK	11.50	11.71	11.20	11.01	10.80

	24/04/2020	Amundi + 6m.	Consensus Q3 2020	Amundi + 12m.	Consensus Q1 2021
EUR/SEK	10.87	11.35	10.80	10.27	10.60
USD/CAD	1.41	1.46	1.40	1.31	1.35
AUD/USD	0.64	0.62	0.62	0.75	0.65
NZD/USD	0.60	0.57	0.60	0.69	0.63
USD/CNY	7.08	7.15	7.02	6.95	6.98

Source: Amundi Research

DISCLAIMER TO OUR FORECASTS

The uncertainty around the macro forecasts is very high, and it triggers frequent reassessments any time fresh high frequency data are available. Our macroeconomic forecasts at this point include a higher qualitative component, reducing the statistical accuracy and increasing the uncertainty through wider ranges around them.

A global recession is our base case today

1. How deep?

- The deepness depends on the virus longevity in the countries affected and the consequent gradual to complete lockdown in most of them. Downturn is evident in domestic demand (across its components at different degree) and in trade dynamics. We assume the largest downturn in the lockdown quarter and a milder downturn to follow. We monitor outbreak developments and lockdown/resumption of the economic activity.

2. How long?

- The timeline depends on the deepness of the economic disruption together with the credit conditions and the rise of corporate default, magnifying the financial markets turbulence and therefore the impact on the economy.
- The timeline of the shock has extended, and overall a peak is expected by May to June 2020. The global economy was showing signs of growth stabilization during the 4Q2020.
- The timeline is also a function of the specific developments of the outbreak together with pre-existent fragilities.

3. The fiscal impact

- The impacts of micro and macro fiscal measures are not included in our forecasts but it's fair to assume a normalization in the financial and liquidity conditions driven by Monetary Policy authorities

Financial targets

- Financial targets are reviewed on the same line and include policy actions implemented on a daily basis.

PUBLICATIONS HIGHLIGHTS

INVESTMENT TALKS



Coronavirus crisis: impacts and implications for emerging markets (2020.04.17)

Yerlan SYZDYKOV, Global Head of Emerging Markets, Alessia BERARDI Head of Emerging Markets Macro & Strategy Research, Abbas AMELI-RENANI, Portfolio Manager, Emerging Markets Debt

- Covid-19 will have very significant negative effects on the economic outlooks for EM, mostly leading to recessions. The IMF is trying to revamp its instruments to increase the resources it can allocate
- In order to assess the risks that EM are experiencing, we need to evaluate their fiscal fragility and their external vulnerabilities
- Investor's sentiment has already started to improve in emerging markets, in terms of asset prices as well as fund flows
- We see value in EM external debt, particularly in high yield, where spreads have already widened to global financial crisis levels. Regarding equity, we have been relatively defensive: we prefer countries with fiscal buffers

Playing the possible sequence of market normalization gradually and selectively (2020.04.10)

Pascal BLANQUÉ, Group Chief Investment Officer, Vincent MORTIER Deputy Group Chief Investment Officer

- As the Covid-19 virus spreads, investors can assess the potential sequence of market opportunities that will emerge from the crisis
- A new market theme of Covid-19 de-synchronisation is emerging
- The deviation in equity returns and in credit spreads has disappeared yet the selloff hasn't priced in a permanent loss of potential growth and shock to earnings expansion
- Trying to time the bottom of the market is unrealistic. Investors should consider adding gradually, and with discipline, opportunities to rebalance their long-term strategic allocation, whilst keeping a firm hand on liquidity and quality of assets

A lot of bad news already priced in US assets: a gradual approach to exploit market dislocations (2020.04.08)

Kenneth J. TAUBES CIO of US Investment, Marco PIRONDINI Head of Equities, US

- The US economy has entered a recession, induced by the social distancing and quarantining measures introduced to tackle the pandemic crisis
- To monitor how deep the recession will be, we use both traditional macroeconomic data and big data. Both sets of variables suggest an unprecedented collapse in domestic demand
- Given continued economic uncertainty and the market focus of recently enacted policy measures, we favour high-quality assets within each fixed income sector
- In equities market dislocations may offer opportunities to long-term investors to enter the market gradually

Euro Investment Grade credit reacts to the ECB's bazooka: selective opportunities (2020.04.01)

Eric BRARD Head of Fixed Income, Monica DEFEND Global Head of Research

- The Eurozone economy is facing a severe disruption due to the Covid-19 crisis
- Beyond the political debate, it is unlikely we will see the issuance of corona bonds in the short term as even in case of political agreement, the devil will be in the technicalities of the implementation
- The measures implemented so far have managed to partially calm markets. We spot considerable appetite for investments in the euro fixed income market
- In Credit, we aim at identifying companies that can withstand the crisis and exploit markets fragmentations. We keep a particular focus on liquidity

INSIGHT BLUE PAPER



Covid-19 will redesign sector opportunities amid gradual normalisation and focus on earnings (2020.04.28)

Kasper Elmgreen Head of Equities, Eric Mijot Head of DM Strategy Research, Ibra WANE Senior Equity Strategist, Luc Mouzon Head of European Equity Research

- The spread of coronavirus in Europe and the United States triggered a worldwide stock market crash in March, followed by a partial rebound. We outline three scenarios to analyse the situation
- We compare the current situation with the 2008 GFC and the 1987 crash. In both the above crises, stock markets converged to around 20% below their pre-crash levels one year after the start of the crash
- The fall in European EPS could be equivalent to or much worse than that recorded in the 2008 crisis, given the unprecedented confinement measures
- As the crisis evolves, there is a potential for fiscal stimulus to be targeted at the 'green deal', especially in Europe where ESG remains an integral part of stock selection

PUBLICATIONS HIGHLIGHTS

INSIGHT BLUE PAPER



Revisiting the global high yield outlook in the wake of the Covid-19 pandemic (2020.04.21)

Kenneth J. MONAGHAN Co-Director of High Yield, Andrew FELTUS Co-Director of High Yield, Matt SHULKIN

- Global HY markets sold off aggressively between February and March
- An analysis of past peak-and-trough episodes in the US HY market shows that on most occasions investors have enjoyed positive market returns just one year after the peak
- For the first time ever, the Fed has launched a purchasing programme for recently downgraded HY bonds. These measures should help cushion the HY default spiral
- Investment views:
 - US HY, selectivity will be of paramount relevance, with a focus on industries and companies that are relatively insulated from the effects of the virus
 - EU HY, we favour BB names in defensive sectors due to the current low visibility on the economic outlook
 - EM HY, we believe that this asset class is oversold

DISCUSSION PAPERS



ESG Investing and Fixed Income: it's Time to Cross the Rubicon (2020-01)

Mohamed BEN SLIMANE — Quantitative Research, Eric BRARD — Head of Fixed Income, Théo LE GUENEDAL, Thierry RONCALLI, Takaya SEKINE — Quantitative Research

FX wars, currency wars & money wars

Part 2: Fiat Money vs. Cryptocurrencies Private vs. Public digital currencies... (2020-01)

Philippe ITHURBIDE — Senior Economic Advisor — Amundi

FX wars, currency wars & money wars

Part 1: FX wars vs. currency wars USD vs. EUR vs. RMB vs. ... (2020-01)

Philippe ITHURBIDE — Senior Economic Advisor — Amundi

WORKING PAPERS



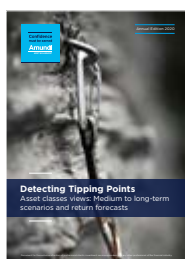
A Note on Portfolio Optimization with Quadratic Transaction Costs (2019-12)

Pierre CHEN, Edmond LEZMI, Thierry RONCALLI, Jiali XU — Quantitative Research

Machine Learning Optimization Algorithms & Portfolio Allocation (2019-10)

Sarah PERRIN — Ecole Polytechnique, Thierry RONCALLI — Quantitative Research

THEMATIC PAPERS



Detecting Tipping Points: Asset classes views: Medium to long-term scenarios and return forecasts (2020-02)

Monica DEFEND, Global Head of Research, Viviana GISIMUNDO, Deputy Head of Institutional Advisory

U.S. inflation... what's up (2020-01)

Annalisa USARDI — Senior Economist — Amundi

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