Global Research Unlocked

Our Outlook for 2024: Breadth in Rate Cuts and Markets

Key takeaways

- BofA Global Research analysts join the podcast to discuss emerging risks, opportunities, and growth themes in global markets.
- Claudio Irigoyen expects a number of central banks to cut in '24; Mark Cabana expects the Treasury curve to steepen.
- Savita Subramanian and Michael Hartnett expect broader strength in the markets but Michael sees downside risk first.

Investors face a much different backdrop in 2024

Our Economics and Strategy teams expect central banks in developed economies to start cutting rates in '24, inflation to slow further and the dollar to weaken. But questions persist, ranging from which emerging economies may perform best amidst the weakening dollar backdrop, whether 10Y Treasury rates will follow Fed Funds rates lower, and if the markets might be too complacent about inflation and growth. Members of our Economics and Strategy teams join the podcast to answer these questions and provide their outlook for 2024. In case you're interested in a particular speaker, you can skip to a particular time: Claudio Irigoyen (0:58), Michael Hartnett (9:46), Mark Cabana (22:00), and Savita Subramanian (29:38). *Global Research Unlocked can now be found on public podcast platforms, including Spotify, Apple Podcasts, Google Podcasts, and Amazon Music. These podcasts are first released to clients and then to the platforms.*

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Refer to important disclosures on page 11 to 12.
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Full Podcast Transcript

T.J. Thornton, Head of Product Marketing: Hello, and welcome to Global Research Unlocked, where we discuss what's rising from growth industries to rising risks and opportunities in global markets. I'm T.J. Thornton, Head of Product Marketing at BofA Global Research, and we're recording this episode on Tuesday, December 5, 2023. BofA Global Research's Macro and Strategy teams released their year ahead notes just before the US Thanksgiving holiday. These notes offer views on economies, rates, index targets, and hundreds of pages of thoughtful text and charts. Days later, we released a note with the 10 key themes from those notes, a version of which is available on business.bofa.com. And with this podcast, we've taken four Q&A sessions on some of the biggest topics, the global economy, global markets, rates and US markets, and combined them into a single year ahead podcast. We hope you find it insightful. Let's start with Claudio Irigoyen, Head of Global Economics Research. Claudio, you recently released your year ahead piece, and you're expecting a soft landing for the US economy, slower growth ahead, but you don't think that we'll see a recession. Consumer savings have fallen. The US unemployment rate is 50 basis points off the lows, some of the biggest boosts from fiscal stimulus are already behind us, why are you so convinced that it will be a soft rather than a hard landing for the US?

Claudio Irigoyen, Head of Global Economics: This is a very important question, and it's a question that we receive almost in a daily basis. All the evidence we have on consumption dynamics indicates that a soft landing is way more likely than a hard landing, basically because we haven't had built enough imbalances to drive into a hard landing. That doesn't mean that we cannot have a hard landing down the road, but that could be more a story for end of '24, beginning of '25. Ironically, in order to have a hard landing in end of '24, beginning of '25, you might need a buildup of imbalances, which means stronger consumption and investment before having the hard landing, and therefore, the Fed being forced to either continue hiking interest rates or holding interest rates high for longer. You pointed out very good reasons why we should expect a slowdown in economic activity. Excess savings have been depleted probably about 60%; remember that the recent revisions of GDP imply that excess savings are now bigger than what we thought. The consumption dynamics is slowing down, but the labor market remains pretty tight, and therefore, disposable income is growing still at a reasonable pace. Households and corporates have hedged their interest rate exposure when interest rates collapsed, especially houses through mortgage refinancing and large corporates through refinancing in the bond market, so the balance sheets are pretty healthy for this stage of the cycle, and that's the reason why consumption has been so strong, and the recession that everybody has been calling and the hard landing that everybody has been calling didn't happen yet. Definitely hard landing is one of the risks scenarios to our baseline, but also we need to highlight a couple of things. First of all, a soft landing doesn't mean no landing. Soft landing means a decent deceleration relative to trend growth, relative to potential output, which is roughly 2% for the US. And the worst of the slowdown will be in the first half of next year.

T.J. Thornton: Okay, so Claudio that was mostly focused on the US. Curious to get your thoughts about emerging markets in 2024. China disappointed in '23, but then Mexico put up some record numbers on the investment front, thanks to nearshoring. Do fortunes flip in '24, as things revert and China continues to stimulate, is there anything else interesting to highlight on the emerging market front?

Claudio Irigoyen: Yes, this is a very important question. We think that the countries that did very well in 2023, will be slowing down in 2024. In the case of Mexico, it's not surprising. Mexico surprised to the upside in 2023, because it's an economy that is pretty much linked to the US. As we expect a soft landing in the US, we should expect also a soft landing in Mexico too. The case of Brazil, the other outperformer of Latin America, is a little bit different, but we also expect a slowdown in economic activity, though less so than consensus. Countries that will do better in 2024, relative to 2023.

Probably in EMEA, we need to highlight Türkiye and we need to highlight Poland. In Asia, as you mentioned, given that there will be some sequential stabilization in growth in China due to the incremental policy easing of the government, we should expect ASEAN to perform well. And the bigger outperformer of 2023 will be, again, the bigger outperformer of 2024, and that will be India. India is doing pretty well. There is still investment coming into the country. The manufacturing sector is doing well. Consumption is very strong, labor market resilience, so we expect India to continue doing very well. Obviously, the US is slowing down and therefore interest rates are peaking here, and China is at least sequentially stabilizing in terms of growth. And usually emerging markets do well when China leads global growth rather than the US because that means a weaker dollar rather than a stronger dollar. The concern we have is how much or for how long we're going to be able to see that stabilization in sequential growth in China, because we have sequential growth in China to peak around third quarter of next year and then gradually moving lower. That's why we have average growth slowing down to 4.8% in 2024 relative to 5.3% in 2023, and then continue slowing down to 4.6% in 2025.

T.J. Thornton: Okay. Claudio, continued disinflation is key to the more sanguine economic view, and you think that across the globe we will see disinflation, really everywhere, even though you've got different growth outlooks in different places. But so much progress has already been made, especially in the US, on the disinflation front, so why are you so convinced that it will continue to happen, and what would you say are the upside risks to watch when it comes to inflation?

Claudio Irigoyen: What I would say is the following: this inflation that we have observed so far has been mostly driven by goods disinflation and that started when energy prices stabilize after the spike in oil prices due to the Russia/Ukraine War. Service inflation has been way stickier, but it's still coming down. And as economies slowdown and monetary policy, as I said, is starting to have an effect on consumption and investment, we're going to continue seeing service inflation moving lower to the target. What can go wrong? Okay, I think that depends a lot on the type of countries we are talking about. In the case of the US, if consumption and investment remains strong, and we have those imbalances that I was talking about before continue building over time, we are going to have a lot of pressure in the labor market because, so far, increasing the demand for labor has been met by an increase in labor for participation and also an increase in migration. Next year, migration will not be probably much higher, or at least the rate of growth will be limited because it's an electoral year in the US and labor for participation is reaching a plateau. If the demand for labor continues moving higher, we should see a nonlinear acceleration in nominal wages that can feed into inflation again, so that's probably the biggest risk for the US. In the case of the rest of the world, I think we need to pay attention to energy and food prices. Obviously an escalation in Middle East that can put oil prices above 100 for a while or 130 or 150 represent an important risk. It’s not so much a risk for the US, given that the share of energy is much smaller in the US compared to other CPI baskets, and also US is shielded because of energy independence. Food prices are always a risk. This is especially particularly relevant for EM (emerging market) countries. And the food prices, we should expect some volatility in food prices because of the volatility that we are seeing every day in weather conditions, and in particular, El Niño could spoil the disinflationary dynamics that we are seeing across the board, both in developed markets and in emerging economies. Energy prices and food prices, obviously, if there is a spike in those, that’d represent actually a change in relative prices, the relative price of goods relative to services will go up. But technically it's going to show up as inflation. And if inflation expectations are being altered by those relative price shocks, central banks will have to act accordingly, so that's probably the main threat outside the US for inflation dynamics.

T.J. Thornton: Okay, Claudio thank you very much for joining us.

Claudio Irigoyen: Thank you.

T.J. Thornton: And now to Michael Hartnett, Head of Global Investment Strategy. Michael, thank you for joining us today.

Michael Hartnett, Head of Global Investment Strategy: Pleasure, T.J. Pleasure.

T.J. Thornton: You believe that a buying opportunity in markets is coming, but not before investors get a lot more concerned about the economy and corporate profits get hit. Essentially you see a growth scare ahead. What's in the data that tells you that there's a sharper slowdown coming and how soon will this be clear to the market?

Michael Hartnett: I think we love to buy markets. We love to go all in. We love to be maximum bullish when positioning is extremely bearish and it's extremely bearish 'cause people are completely worried about recession and that recession provokes a policy panic: the three Ps of positioning, profits and policy that we always use to say, now's the time to go all in, or now's the time to go all out. My concern going into 2024 is that soft landing is a pretty consensus view right now. I think if you look at things like oil, the oil price, which is a pretty good global demand indicator, it's interesting that despite OPEC (Organization of Petroleum Exporting Countries) cuts and despite wars in the Middle East that is not getting a bid right now. In fact, oil has been flirting with a bear market ever since. Is that something to do with global demand? It could be. I'm concerned that the ISM indicator, well that wonderful, beautiful sort of coincident indicator of the US economy, the US corporate sector, US profits, again, another thing that was starting to improve in the summer, which drew in a lot of people to say, now's the time to go back into equities that's rolled over. I think that worries me a little bit. And then I do see a labor market that is weakening. I think you can see that in the payroll data. I think you can see it in the JOLTS (Job Opening and Labor Turnover Survey) data. And historically markets, they tend to rally in anticipation of the Fed cutting rates. But actually when the Fed starts cutting rates, if it's because of a recession or a hard landing or a growth scare, as you call it, that's when you get a pullback in markets, and that's the pullback that I'd like to buy.

T.J. Thornton: Okay. One of the trades that you favor is 'diamonds in the rough', at least once we get that pullback and the low. Could you explain what you mean by 'diamonds in the rough' and have valuations for some of these diamonds gotten really attractive? Because I know that outside of the Magnificent Seven, there are some very cheap stocks out there.

Michael Hartnett: I think they are already very cheap, and not just in the US, but also in international markets as well. But let's leave aside equities to begin with. I think bonds will do better, government bonds will do better next year. We're coming off the third consecutive year of loss in US Treasuries – it's never happened before in the history, 250 year plus history of the US Republic. I think if you get a landing, the Fed cut rates, bonds are going to do better. If bonds do better, the dollar's going to do worse. That's why we like gold bullion. So, I think that there are already trades that you can do. The equity trade that we talk about with 'diamonds in the rough'. If you think about 2023, what worked in equities was themes. AI, tech, lack of homes, homebuilders, end of Japanese deflation, the Nikkei, reshoring, industrials. If you like, T.J., it was like bubbles for the few and bear markets for the many. No one wanted banks, no one wanted REITs, no one wanted utilities, no one wanted small caps, no one wanted China, etc., etc. Why? One word - leverage. No one wanted to own leverage. And the 'diamonds in the rough' theme is, look, if next year bond deals are going down, if next year the dollar's going down, then surely the pressure on that leverage is going to be relieved. A lot of people will say, like me, I don't think yields are going back to 0% or 1% or 2%. I think over the next couple of years they're going to remain high-ish, because I don't think inflation's coming all the way back down again. But surely in a year in which yields are coming down and the dollar is coming down, you've got to find some diamonds in those sectors that have been incredibly depressed and punished because rates have gone up and no one's wanted to own leverage, so you want to look for the best two or three regional banks, the best two or three companies that you like that are exposed to China, the best two or three companies in the REITs market, the diamonds in the areas of the equity market that have been really roughed up in 2023.

T.J. Thornton: Okay. And Michael, in the past you've written about favoring real assets, but with rates and inflation falling next year, has that view changed at all? And how do you see those performing?

Michael Hartnett: Commodities have had a tougher time of it. For example, in 2023, REITs, real estate arguably has also had a tougher time of it in 2023. And I'll take slight issue with what you say in I think inflation's already fallen. I think that disinflation story played itself out. And of course it's been at a great disadvantage to real assets: the commodities, the real estate. There's a little chicken and egg thing there. But nonetheless, generally when you get a great decline in inflation, real assets don't do well. If, like me, you believe that Washington, D.C. and its fiscal excess or the geopolitics of the world today, which are very different from the last 20 years in which you're seeing war not peace and trade agreements being broken rather than launch. If like me, you believe that labor in the early part of the 2020s, this will be the last great chance with very low unemployment. And with AI in its nascent phase, rather than develop, this is the last great opportunity to extract health benefits and pension benefits and wage gains from corporations. I think that inflation will go up again. I don't think it's coming down and staying down. And so in many ways, 2024, I think offers you a last great entry point into real assets. And I think that real assets will do well over the medium term. And just generally from an asset allocation perspective, it's not to say bonds and equities can't do well. We'll see bonds do well in '24. We saw some equities do very well in '23. But my point would be is you still got to have commodities, real estate, real assets, cash. These are still areas of your portfolio that you don't want to take down back to the levels that you had them in the first 20 years of this century.

T.J. Thornton: Okay, and agreed on disinflation, sorry if that was not clear, but right, we're expecting continued disinflation next year. I would point out too that my family bought chickens and absolutely top ticked the price of eggs, so once, we bought that flock of six, we were sure to see disinflation ahead, which we did.

Michael Hartnett: Right, right. Okay, tell me when you start buying pigs or something.

T.J. Thornton: We bought them more, more to keep everybody happy.

Michael Hartnett: Yeah, yeah. I hope the chickens are happy. That's the thing most important to me.

T.J. Thornton: They're all still alive.

Michael Hartnett: Good.

T.J. Thornton: Okay, so I want to ask about the Fund Manager Survey (FMS). It suggests that consensus is more that there will be a soft landing that we'll see continued disinflation and we'll see rate cuts even without a sharper slowdown in economies, sort of a Goldilocks view. That's what the FMS says. But do you think that's already priced in and obviously you have somewhat more bearish view on growth, what's the upside if that soft landing view does come to fruition?

Michael Hartnett: I think it's a great question. If it's a soft landing, yields will go from, as they've just done in the past month, 5% to 4%, and equities will do well. You could certainly romance earnings of 240, 250 and a multiple that is close to 20 and you can do the math on that one. I think however if it's a hard landing and yields are going from 5% to 3% that's less fun for equities because that's much less fun for earnings. And particularly as you point out the point about disinflation, let's remember a year ago everyone was predicting EPS (earnings per share) recession and some things we got right this year, some things we got wrong this year, but one of the things we got right this year was saying, how can you get an EPS recession if prices are going up 5%, 6%, 7%? You really need volumes to collapse to see nominal earnings decline. Didn't happen!

But now, next year, everyone's like, "well, there's no inflation." Well, you're not going to get the price increases to give you those earnings. So, it could well be that in a hard landing, you're more like 220 of earnings and or 225 and maybe the multiple can stay closer to 20 times, but probably it would drop to somewhere like 17, 18 times. Again, you can do the math on that one. Clearly there's going to be surprise, it's an election year, there's so much going on geopolitically. The biggest surprise next year would be there's no surprises given what we've just lived through for the past three years. But I think that if you want to simplify 2024 soft landing, you find hard landing, you're going to have trouble.

T.J. Thornton: Okay. And I did want to finish this section with the question about upside and downside risks. Obviously one of the downside risks to the market, a harder landing, but right geopolitics, anything else you want to add on the upside of the downside that people should be thinking about?

Michael Hartnett: The other downside risk that we haven't mentioned is China. It is the second largest economy in the world. It's one of the great trading nations in the world, and it's in a completely different galaxy right now from everything else. This has been a good year for stock markets broadly. It's been extraordinarily narrow, fine, but China's ending the year with the stock market of China back at the COVID lows. What is going on? Is it the lack of stimulus? Is it the lack of a full reopening? Is it that there truly is a banking crisis and it's happening right now in China? It is an enigma. No one's really quite sure, but I think that's something that needs to be watched very closely. And the upside risk, I think geopolitics. I think geopolitics, the oil price falling, I said, mentioned earlier, it hasn't done as well as you would think off the back of geopolitics in 2023. Is that because there are so many elections next year in Europe, the UK and of course the US, and politicians in a democracy are realizing that voters don't like geopolitics that cause inflation and cause prices to go up and that foreign policy is not a vote winner. And actually the markets, what they're saying is, we've got to discount a year where the West tries to cool the geopolitics of Asia, the geopolitics in the Middle East, the geopolitics of Europe, Russia, and actually that leads to much lower oil prices, which together with a lower dollar, it gives you a nice boost in terms of financial conditions. The other political point, and of course I'm sure you've mentioned this before, T.J., next year 80% of the world's stock markets goes to the polls, 60% of the world's GDP goes to the polls and 40% of the world's population goes to the polls, so it's a huge election year. Most times elections don't matter, but clearly in the case of the US, they did in 2016, they did in 2020, both of those elections mark great big inflection points for the market, so that is going to be something that people think about next year. And again, as an upside risk, there are more than one or two very smart investors that say, look, at the end of the day the politics is a positive in 2024 because the politics of democracies right now is that they will need to do everything they can to prevent a recession in an election year. And that just means more monetary stimulus, it means more fiscal stimulus, and it means less geopolitical tension than would otherwise be the case, were it not an election year.

T.J. Thornton: Okay, great. Michael, thanks very much for joining us.

Michael Hartnett: Pleasure. Thanks for having me.

T.J. Thornton: And now for Mark Cabana, Head of US Rate Strategy. Mark, we just heard from Claudio, the Global Economist, also discussed the US view, where we expect disinflation to continue next year, the US economy to slow and for the Fed to start cutting rates. Why don't you expect a bigger decline in the 10-year, especially given the slowdown and given the Fed cuts that we expect?

Mark Cabana, Head of US Rate Strategy: Thanks, T.J. Great question! Our rate forecasts have the 10-year ending 2024 at 4.25%. I'd note that our forecasts are above consensus, which is around 3.6%, at least according to Bloomberg. And the reason that we don't have rates falling as much as consensus is likely because we anticipate that the economy will remain reasonably resilient. It'll moderate, but it won't fall off cliff. And we also think that the market will continue to overweight two other factors. Those include a potential, higher neutral in the economy, given the fact that we might have some type of residual upside inflation risk and will also have probably learned that some of the investment and broader economic activity that we have seen in 2023 will hold in the future, that means a higher nominal neutral rate. Along with concerns about the supply demand backdrop, and that key question of who's going to buy the bonds? The Treasury has to issue an awful lot of debt in 2024. We think that they'll be issuing about $2 to $2.5 trillion of net new supply, and we continue to get questions about where the demand for those bonds will come from. We're cautiously optimistic that more demand will emerge as inflation moderates, and we see signs that the economy is cooling. But nevertheless, we do think that Treasuries are going to remain reasonably cheap to SOFR (Secured Overnight Financing Rate) swaps or to the expected path of policy, simply because there is so much Treasury duration risk that the market will need to absorb.

T.J. Thornton: Okay, Mark, there's a lot of cash on the sidelines. Investors have piled into short-term instruments because of the compelling yields that they can get, there in the 5% range now, but with the Fed cutting in the middle of next year, do you think that money will pivot into 10-years? And will that matter for the supply demand picture? Also, if it's not coming from this cash forward, where is the demand for the 10-year going to come from?

Mark Cabana: Yeah, another great question. We do expect that the supply demand backdrop in the Treasury market will modestly improve next year. We do expect that investors will extend out the curve, as they see clearer signs that the Fed is going to be moving towards rate cuts. Investors will be extending out the curve to try and lock in higher rates while they still exist - and we've already seen some signs of that. We have recently seen money market mutual funds increase their weighted average maturities, notably as they've grown more confident that the Fed has delivered at the last hike of the cycle and the next move will be rate cuts. We have seen banks, bank portfolios start to increase their Treasury holdings modestly. Again, banks hold an awful lot of cash at the Fed and overnight they earn IORB or the Interest Rate on Reserve Balance with the Fed. But as the Fed cut rates or as the Fed cuts rates, the return that they get on their cash will decrease. They've been extending out the curve modestly. Now, we think that demand will probably be most concentrated in intermediate tenors or the belly of the rates curve, think 3-5 year tenor. We are less confident in how the demand picture will improve for Treasury securities that are further out, think 10-year, 30-year, simply because we think that investors will still be uncertain about the macro backdrop. We think that there's a clearer argument for demand to move out the curve to really be concentrated in intermediate tenors as opposed to very short dated tenors. And we do think that investors will question the value proposition of going all the way out into 10 or 30 years. And that's one of the reasons again, why we only have the 10-year falling to 4.25% in our forecasts, and it is also one of the reasons why we expect that the Treasury curve will be steepening over the course of 2024. For what it's worth, we think that the twos tens yield curve will dis invert, right now it's about 50 basis points inverted. We think it'll realize at the end of next year at about 25 basis points steep, and we think that other parts of the rates curve, such as the five year or 30 year spread, which is currently at about 15 basis points, we think that that will end up realizing closer to 60 basis points by the end of 2024.

T.J. Thornton: Okay. And Mark, you are the US Rate Strategist, but I did want to discuss our global views as well, especially as they do matter for US rates - anything to highlight from other parts of the world? I see that in Europe, we are actually looking for the 10-year rates to fall more substantially than in the US. Does that matter when it comes to demand for Treasuries, as European investors may be looking for more yield?

Mark Cabana: Yes, it absolutely matters. If we do see the rest of the world slow down more materially than we see in the US that should increase investor demand for fixed income broadly. And if investor demand is increasing outside the US, we do expect that the Treasury market will be a beneficiary of that increased demand for duration. T.J. you're right, our European rates team, they're long. They're unabashedly bullish on the European fixed income market, primarily because they worry about an economy that just has insufficient demand and a policy mix that is too tight from both a monetary and fiscal perspective. As a result, they do think that European rates will be falling as we see signs that inflation is subsiding in Europe. We also think that, in other parts of the world, rates will be moving lower as well. In Australia and Canada, we think that those central banks will be taking a more dovish stance overall. We think they'll be more sensitive to higher rates in their economy. In particular, the housing market there is not nearly as long in terms of the lockup period that home buyers can enjoy. They tend to reset on a much shorter frequency than in the US, so higher rates will be felt more clearly in those parts of the world. They will slow. We do think that those markets will benefit by seeing rates fall and fixed income prices appreciate there.

T.J. Thornton: Okay. Well, Mark, thank you very much for sharing your views and joining us today.

Mark Cabana: Thanks for having me.

T.J. Thornton: And finally, to Savita Subramanian, Head of US Equity and Quant Strategy. Savita, you offered five reasons to be bullish on equities into 2024. The first of those was lukewarm sentiment, but in just a few weeks since publishing your year ahead note, the market's rallied a lot as the yield top seems to be in and you published a note very recently on sell side sentiment and how it's rising. Where do you think sentiment is now and is it still as supportive?

Savita Subramanian, Head of US Equity and Quantitative Strategy: Yeah, sentiment has warmed up a little bit towards equities, but I would say it's still relatively bearish even based on our Sell Side Indicator, which we updated, as of the beginning of December, so the sell side has gotten a little bit warmer on equities. They've nudged up their equity allocations by about 1%, but they're still quite bearish relative to history. Where we are today, the average Wall Street strategist is recommending that you put a little bit over half of your portfolio into stocks versus the rest, mostly into bonds and then a little bit of cash. A 50%ish allocation to stocks is still quite low. And if you recall at the beginning of 2022, one of the reasons we were more worried and nervous about equities was that allocations had approached 60%, the highest levels we'd seen in a decade. We think despite what feels like a big jump in sentiment, data still points to relatively convictionless bears, except for bullishness on Mega-cap tech and AI plays. Across the board, if you look at pension funds, if you look at asset allocators, if you look at analysts' expected growth for next year; they're all close to the lows that we've seen in at least a decade. For pension funds, equity weights are close to 25-year lows. I would argue that we're still far from euphoria, which is typically what ends a bull market.

T.J. Thornton: Okay, thanks Savita. And we, meaning the Econ team and the market, are expecting rate cuts next year from the Fed. That's of course a big change from the hikes that we saw in '23 and '22. But what's interesting is that these cuts aren't really a driver of your bullish view, so what have rate cuts tended to mean for the S&P and have rate cuts favored certain styles like growth or value?

Savita Subramanian: Our view is that long rates are probably a more important driver of equities. And here if the 10-year stays at higher for longer levels of maximum tightness in the credit markets, we still think that we're going to be in an environment where cyclical companies, companies that benefit from consumption, companies that benefit from business investment could still outperform. Rate cuts have generally been a sign that we're past the point of peak tightness and credit, but not necessarily out of the woods in terms of economic growth. In our economists' forecast, they're really calling for a soft landing, a sign of the Fed at least being on hold for the foreseeable future, if not cutting interest rates, so our view is that this could actually be a pretty good environment for equities. We're not bullish though because we expect the Fed to cut interest rates, we're bullish because of what the Fed has already accomplished. What I mean by that is that companies have adapted to higher interest rates and to higher inflation. We think we're past the point of wondering how we're going to get off of a zero bound on interest rates where we've seen a lot of that work done by the Fed. Our view is that whether or not the Fed cuts rates next year, we still see equities as a better place to be than other asset classes.

T.J. Thornton: Okay. And Savita, one of the bearish views out there is that the economy will see something closer to a hard landing next year that'll hit earnings, and that will send stocks lower, at least for a period of time before maybe rebounding as the Fed's cutting. Our Economics team does look for a soft landing, but if they're wrong and we do see a hard landing or at least concerns over a hard landing, what does that mean for earnings and for the market?

Savita Subramanian: I think that what we're looking for is really a broader confidence shock. If we see a hard landing, but companies were prepared for it and they continue to spend at a relatively healthy level, if we see a hard landing, but consumers who are actually sitting on relatively healthy balance sheets don't stop spending, if we don't see broad-based job losses that would continue to favor the idea that, whereas investors are expecting, just really a secularly challenged market, things could be okay. But if we do see a hard landing start to drive broad-based layoffs, we think that would be the real driver for consumers to bunker down and not spend as much. What we've seen is that the wealth effect is probably a less of a driver than actually having a job. And if real wage growth right now is positive, that's good for consumption. But if consumers start losing their jobs, that's really the point at which they stop spending. That's the point at which they put their homes for sale, even at distressed prices, so that would be what we're watching. But I think that even a mild recession would be manageable by corporates and consumers because they've already de-levered their balance sheets so aggressively. But if we saw a hard landing that really spooked corporate and consumer confidence, I think that's when we would get more negative on our earnings outlook and our overall market outlook.

T.J. Thornton: Okay. And a quick follow up there, if the recession was mild, you talked about the importance of the 10-year, if the 10-year came down maybe more than expected 'cause right now where the 10-year is essentially in line with where our rate team expects it to be at the end of next year. How bullish is that? Is that actually a particularly bullish environment if we see this slowdown accompanied by much lower rates?

Savita Subramanian: Yeah, I think if the slowdown is accompanied by lower rates and the driver for lower rates is that investors are expecting weaker growth, I don't see that as particularly bullish. If the driver for lower rates is that there's more demand for long duration assets that might be more bullish, but I think if we saw rates surprise meaningfully to the downside, we would be more likely to shift our views towards the continued leadership in growth stocks, in technology, in secular winners rather than the cyclically motivated companies like industrials, materials, financials, manufacturing. I think in that environment of rates dropping on the long end, more than what the market is anticipating, that would actually get us back into the solid leadership of tech companies that we've seen for this year and for most of the last decade. That's not what we're expecting. We're assuming that rates normalize around where we are today, the higher for longer, long rate environment, which gets us more positive on cyclicals and sectors that benefit from a steepening yield curve.

T.J. Thornton: Thank you very much for joining us today.

Savita Subramanian: Thank you.

T.J. Thornton: The Economics team believes the Fed will start cutting in 2024. Among our strategists, there's debate about whether those cuts will come because of a possible hard landing or because continued disinflation allows the Fed to get less restrictive. But Savita and Michael do agree that we should see broad strength, a change from 2023 where performance was fairly narrow. It's just that Michael thinks there's some downside before that positive breath asserts itself. And the rates team expects the short end of the curve to come down more than the long end, resulting in a steeper yield curve that could herald a different investing backdrop in 2024. Indeed, it has tended to favor riskier areas of the market in the past, and that's consistent with many of our strategy views from bullishness on emerging markets to positive views on financials from both Savita and Hartnett, at least once we get that sell-off. Thanks for joining.

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