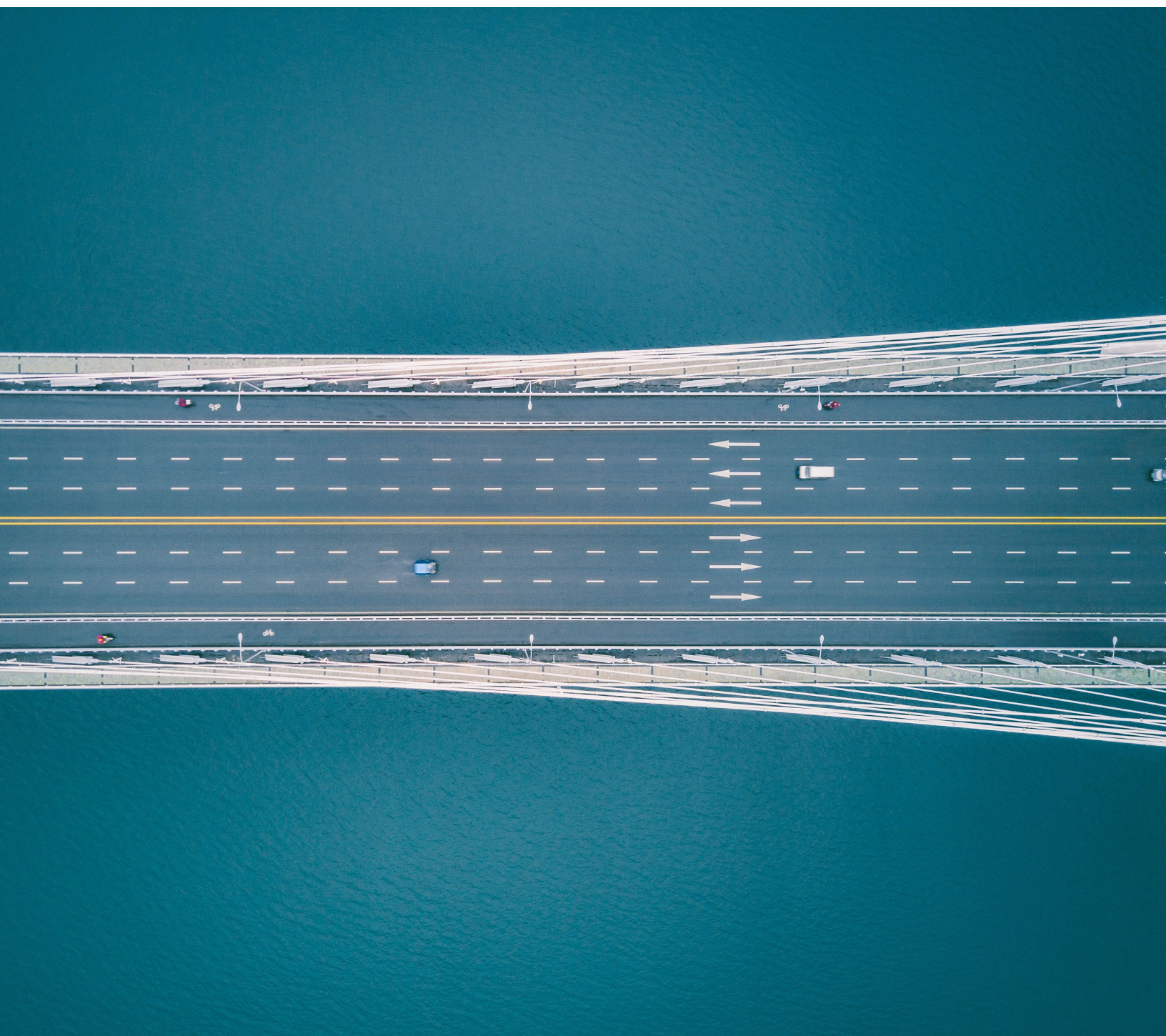


Perspectives

Quarterly economic views and asset class outlook

Fall 2024





We remain broadly constructive on the outlook for the global economy.



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Welcome to the 2024 fall edition of *Perspectives*

Our core economic views are little changed since [the summer edition of *Perspectives*](#). We remain broadly constructive on the outlook for the global economy. The US economy continues to set the pace amongst the major economies and consumer spending sustained domestic economic activity above trend. A benign slowing in US growth remains likely in coming quarters, and a relatively soft landing appears in reach for the US Federal Reserve. Inflation in the US, and elsewhere, continues to moderate and looks to be a weaker constraint on central bank policy decisions than it was at the beginning of 2024. With most major central banks now cutting interest rates, fiscal policy becoming more supportive of economic activity, and investment spending likely to become a tailwind we continue to expect a gradual recovery in global gross domestic product (GDP) growth.

We also expect constructive economic conditions to foster a (cautiously) positive environment for risk-taking and investment performance over the next 12 months. Fundamental factors such as economic growth and inflation, interest rates, corporate profitability and technological innovation are the key drivers of longer-term investment performance. Within this outlook, we think equities and bonds can both make a positive contribution to investment performance. We currently see little reason to favour one asset class over the other relative to strategic allocation weights.

Also consistent with last quarter's edition, political risk remains the key challenge to this cautiously constructive outlook. Geopolitical risks increased over the last three months and November's [US presidential election](#) is now top-of-mind for investors. Both are contributing factors to more volatility in markets—consistent with history. In particular, rising uncertainty associated with possible election-driven policy changes often encourages investors to try and time market participation. Frequently, this has proven to be the wrong decision. Staying invested in a well-diversified portfolio through short-term volatility—regardless of the source—has typically paid off.

At [CIBC Asset Management](#), we're committed to providing market insights and investment research. We hope our quarterly market and economic outlook are helpful as you find the right investment strategies that align with your portfolio goals. If you have questions or would like to discuss our insights and commentary, please contact your advisor or CIBC representative anytime.

Global markets strategy

Global policy relief tailwind, but political and geopolitical risks remain

In the [last edition of Perspectives](#), we highlighted that while a benign investment environment would be supportive of markets, we could face periods of volatility. The conclusion was that both equities and bonds would likely do moderately well—with a small expected outperformance of equities. However, given the expected outperformance was small considering the potential risks, we preferred to maintain a neutral tactical strategy positioning in equities versus bonds.

Over the last few months we've seen a materialization of some of those risks. On the political front, the US elections were sent back to the starting line after Joe Biden dropped out of the race and Kamala Harris became the Democratic presidential candidate. At this point it remains a very close race and uncertainty prevails with respect to what the policy environment will look like over the next four years. The race in the Senate is also close and the results will determine whether the winning President will face a majority or a divided Congress. Meanwhile, the war in the Middle East continues to be a source of instability, as the conflict broadened beyond Gaza and brought Israel into more direct confrontations with Iran. Among other things, an attack hampering the production or the flow of oil could have a significant impact on energy prices—and in turn on inflation.

Although politics and wars have attracted a lot of headlines, a more consequential event for financial markets has been the policy shift from the Bank of Japan (BoJ)—which adopted a more hawkish rhetoric. For many years, investors were able to borrow at 0% in the Japanese yen (JPY) and invest in higher yielding securities in the US or other markets. The so-called yen carry trade made sense as long as the Japanese currency was expected to continue depreciating. This was the case when the US Federal Reserve (Fed) was hiking rates and the BoJ was keeping rates at 0%. However, when the BoJ communicated a desire to move out of its zero interest rate policy, the yen appreciated sharply—creating a shockwave across global financial markets.

The [Fed started to cut rates in September](#) in response to improving inflation data. Inflation's deceleration has been partly driven by a rebalancing of supply and demand in the labour market. This is good news, but markets have been concerned that the slowdown in employment driving inflation lower is also a symptom of an economy that's more fragile than expected. Recent economic data has assuaged these concerns and suggest US growth remains robust.

In the US, markets expect the Fed will cut rates by 1.5% over the next 12 months. If the Fed delivers these cuts, the stance of monetary policy will be close to what is generally considered as neutral, neither encouraging further deceleration or a reacceleration in inflation. Based on our outlook for growth, we think the Fed will be less aggressive in easing policy than market pricing. Meanwhile, 10-year bond yields were trading below our long-term fair value of 4.1% as of September 30, 2024. Over the next 12 months, 10-year bond yields will most likely fluctuate in a range of 3.25% to 4.75%. The 10-2-year yield curve slope is positive for the first time since 2022 and will likely continue to gradually steepen.

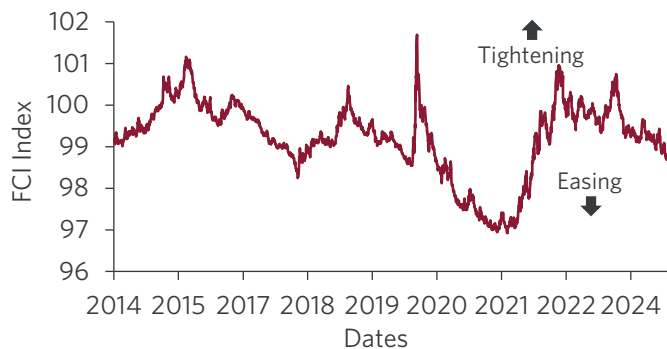
Finally, but not least, China announced a series of measures that will target monetary policy, housing and the equity market. Although a more detailed plan is not yet known, there is a clear signal that the government will act decisively to support the economy. The combination of the two biggest economies (the US and China) easing policy should provide solid support to the global economy and could put a floor under inflation.

Similar to earlier this year, the equity and bond markets appear at odds; the equity market reflects optimistic expectations and the bond market less so. This divergence is not sustainable and will correct itself either through a sharper economic slowdown that pushes equities lower, or a continued expansion that pushes bond yields a little higher. Our bias is the latter. Given the balance of risk, we remain cautiously optimistic on equities.

And relative to fixed income, equities look marginally more attractive. However, the escalation of the conflict in the Middle East dictates prudence. As such, we remain neutral in equities versus fixed income in tactical asset allocation and instead remain focused on relative strategies within both asset classes.

Easing financial conditions

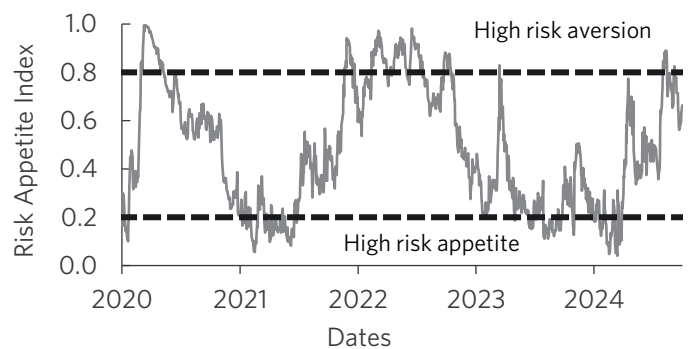
Goldman Sachs US Financial Conditions Index



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at September 30, 2024.

A short lived spike in risk following the BoJ hike

CAM Risk Indicator



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at September 30, 2024.

CIBC AM risk indicator**Multi-asset outlook**

Asset class	Current 30-Sept-24	Most likely range for the next 12 months	
		Minimum	Maximum
Canada 3 Month T-Bills rate	4.25%	2.25%	4.25%
Canada 2 Year government bond yield	2.91%	2.00%	3.00%
Canada 10 Year government bond yield	2.96%	2.75%	3.60%
US 10 Year government bond yield	3.78%	3.25%	4.75%
Germany 10 Year government bond yield	2.12%	1.50%	3.00%
Japan 10 Year government bond yield	0.85%	0.65%	1.50%
Canada Investment Grade corporate spreads	1.21%	0.90%	1.30%
US High Yield corporate spreads	3.04%	2.65%	3.75%
EM Sovereign (USD dominated) bond spreads	323	250	500
S&P/TSX price index	24,000	22,750	27,500
S&P 500 price index	5,762	5,300	6,350
Euro Stoxx 50 price index	5,000	4,825	5,775
Japan Topix price index	2,646	2,600	3,150
MSCI Emerging Markets	71,281	69,000	84,000
USD/CAD	1.3525	1.310	1.420
EUR/USD	1.1135	1.02	1.140
USD/JPY	143.63	135.00	155.00
USD/CNH	7.01	6.80	7.40
Gold	2,635	2,400	2,900
Oil price, WTI	68.17	60.00	92.00

Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party provider: Bloomberg. Data as at 29 June 2024.

Global equities: Moderate returns driven by earnings growth

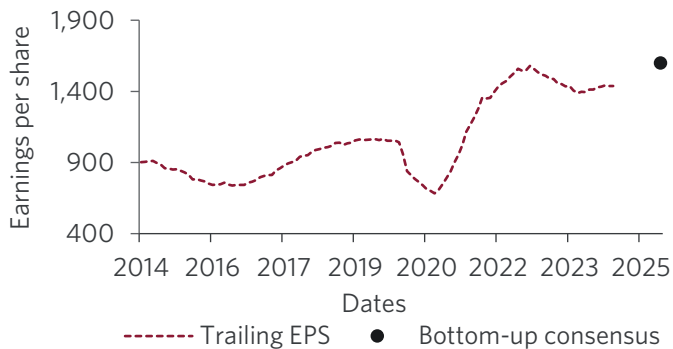
The last three months have been highly volatile in equity markets. Japanese equities corrected lower by 25% following the BoJ policy shift, before recovering about two third of those losses. The S&P500 and the TSX Composite indexes corrected by 8.5% and 5%, respectively, but rebounded rapidly and are currently trading at all time highs as of September 30, 2024. The [Magnificent 7 investing theme](#) receded and a broader group of companies participated in the rally. The Chinese equity market was down 15% from its peak in May and rebounded an astonishing 23% in just 5 days following the stimulus announcements.

The strong equity returns this year were driven by a combination of earnings growth and higher valuation multiples. Given our outlook of trend-like economic activity, we expect earnings to continue to grow at a moderate pace. Valuation is close to neutral in many markets. Continued easing in monetary policy will maintain price to earnings (P/E) ratios above fair value. As such, our baseline scenario would see high single digit equity returns.

After two years of underperformance, Canadian equities have become one of the best performing markets in recent months. The Bank of Canada (BoC) moved ahead of the Fed and indicated it is [likely to continue cutting rates](#). We expect the economy will continue to recover and outperform consensus expectations. Valuation increased but there are no signs of excesses being priced in for Canadian equities.

Canadian earnings are recovering

TSX Earnings



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at September 30, 2024.

Canada equity valuation rising, but not expensive yet

TSX Forward PE



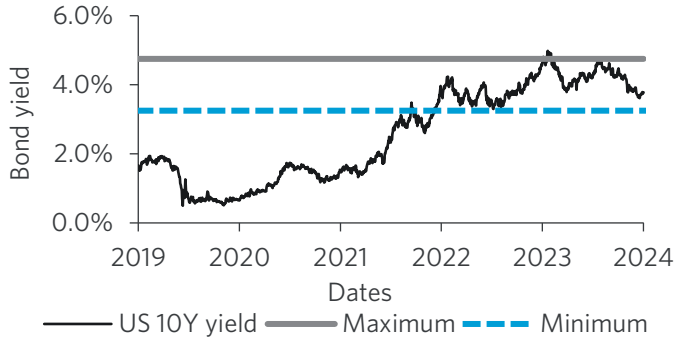
Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at September 30, 2024.

Global fixed income: Markets are pricing too many rate cuts

Global bond markets performance was very positive in the third quarter of 2024. The WGBI index (Canadian dollar hedged) gained 3.84% during the period. 10-year US Treasury yields were pushed lower throughout the quarter, decreasing by 62 basis points (bps). Credit spreads in global high yield bonds and EM US dollar (USD) bonds continue to be tight. Bond markets performance across countries has become very synchronized as of late, leaving limited opportunities to add value through relative value trades.

Our global bonds portfolios are underweight in duration and maintain a balance of high beta/high carry bonds such as Brazil and Chile mixed with lower risk/lower carry bonds such as Japan. We're underweight in those developed countries, notably Canada and the US, where too many rate cuts are priced in. A repricing higher would lead to negative returns for these markets. In terms of EM local bonds exposure, our strategy remains selectively pro-cyclical. Since many EM countries are already engaged in rate cutting cycles, positive returns should be expected if cuts continue. EM bonds could also outperform as Chinese authorities look to stimulate their economy. Policy stimulus usually leads to positive demand spillovers in related EM economies—which in turn leads to increased foreign inflows. We have low appetite for US dollar bonds issued by emerging countries because valuations appear rich considering the under-priced risks of a global slowdown.

Bond yields expected to trade in a range



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at September 30, 2024

Yield curve positive, more steepening to come



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at September 30, 2024

Currencies

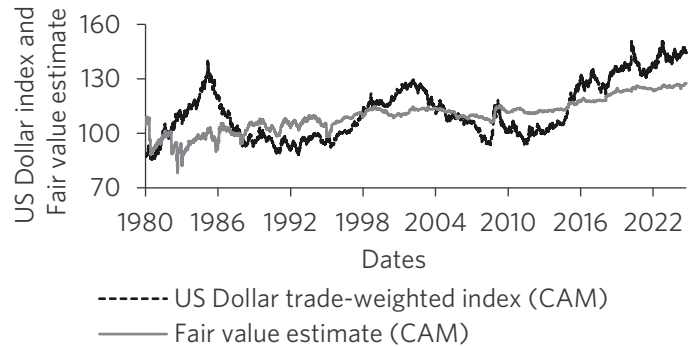
US Dollar

With the Fed delivering a bigger rate cut than widely expected in September, the USD weakened in the third quarter of 2024. This gave back some of the ground gained earlier in the year. While the greenback's weakness was broadly based, more ground was lost against Asian currencies such as the Malaysian ringgit, Thai baht and JPY.

This recent bout of USD weakness doesn't change the bigger picture. The currency still screens as overvalued, just as it has for more than a decade. The start of this period began as US productivity gains started to outpace other countries. This isn't a coincidence: stronger productivity means stronger economic growth, better profitability and financial market outperformance. In short, it comes with a structurally strong currency.

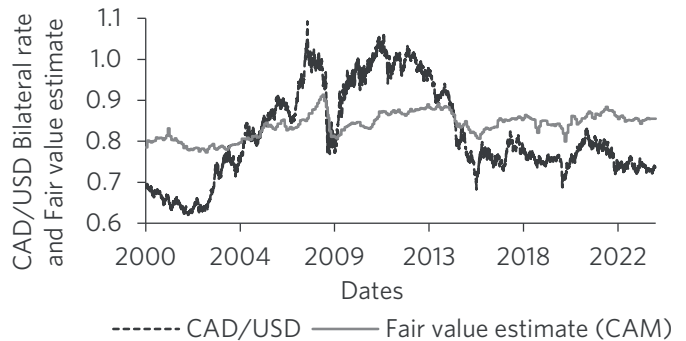
This doesn't mean USD won't experience temporary episodes of weakness. That's exactly what happened over the third quarter. Instead, it means that USD will likely continue to trade in overvalued territory over our 12-month forecast horizon, implying US trade imbalances will persist. With [US elections just around the corner](#), these trade imbalances will likely take center stage again with increased prospects of another trade war. We see no big directional USD move over the forecast horizon but do expect higher foreign exchange volatility.

The almighty US dollar



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 30 September 2024.

Limited upside for the Canadian dollar



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 30 September 2024.

Canadian dollar

Since early July, the price of oil dropped by more than 10%. Surprisingly, this oil price correction had no impact on the value of the Canadian dollar (CAD). To the contrary, the Loonie managed to appreciate a little against USD over the same period. More than a decade ago, one could readily explain more than 90% of the fluctuations in CAD with swings in the price of oil. Back then, a 10% oil price correction would have been expected to be accompanied by a 1.5% CAD depreciation against USD. Those days are long gone.

What has to be taken into account is the fact that since 2022 the US has turned into a net exporter of oil. This makes a big difference, explaining the lower-than-usual CAD/USD volatility observed since then. Instead of being hard hit when the price of oil goes up, USD gains support. Putting it differently, when looking at CAD/USD, relative sensitivities to oil now completely offset each other with oil's net impact turning neutral. This allows other currency determinants like relative productivity to become more important driving forces. From this angle, the downward pressures on CAD/USD are not likely to abate anytime soon. Based on the latest available figures from Statistics Canada and the US Bureau of Labor Statistics, as of September 2024, the Canadian to US productivity yearly growth gap remains particularly wide at -3.4%. CAD/USD is expected to stay weak over the forecast horizon trading in a range of \$0.70 and \$0.76.

Euro: A more volatile range

The European Central Bank (ECB) Governing Council decided to lower its deposit facility rate for a third time in October by another 25 bps. The reduction to 3.5% came as inflation slowed with the ECB facing pressure to bolster the eurozone's ailing economy. Given that the euro (EUR) screens as overvalued on a trade-weighted basis, monetary policy easing implicitly aims at weakening EUR's value. However, with central banks of the eurozone's main trading partners also in easing mode, this is easier said than done. What really moves EUR is expectations about the ECB's policy stance relative to other central banks. At this juncture, markets are already pricing deep ECB rate cuts on high conviction that inflation will converge to target. We're more skeptical. With still-elevated inflation in services, the risk is for inflation in the eurozone to bottom out above target. This will force the ECB to move to the sidelines earlier than generally expected. We're looking for a more volatile EUR/USD exchange rate trading between €1.02 and €1.14 over the 12-month forecast horizon. As of September 30, 2024, the EUR/USD exchange rate was €1.1135.

Japanese yen

For nearly four years, the JPY steadily trended lower against USD. Taking many market participants by surprise, it strongly appreciated in the third quarter gaining more than 10% in less than two months. This sudden reversal took place because of a hawkish turn taken by the BoJ early in the quarter. In late July, the BoJ held its policy setting meeting and concluded that it was appropriate to reduce its purchase amount of Japanese Government Bonds (JGBs) in a predictable manner while raising its policy rate another notch. These policy changes are important because they signal the start of the BoJ's monetary policy stance renormalization. With inflation projected to be at or close to target over coming years, Japanese monetary authorities are now convinced the time has come to take the policy rate closer to neutral as well as to shrink the size of its balance sheet. Putting it differently, this means we're in the early stages of a very important BoJ regime shift that will likely

come with some further strengthening of JPY. Keep in mind that JPY still screens as deeply undervalued both on a bilateral basis against the greenback (~45%) and a multilateral basis (~33%). USD/JPY is projected to trade between ¥135 and ¥155 over the 12-month forecast horizon. As of September 30, 2024, the USD/JPY was trading at ¥142.2.

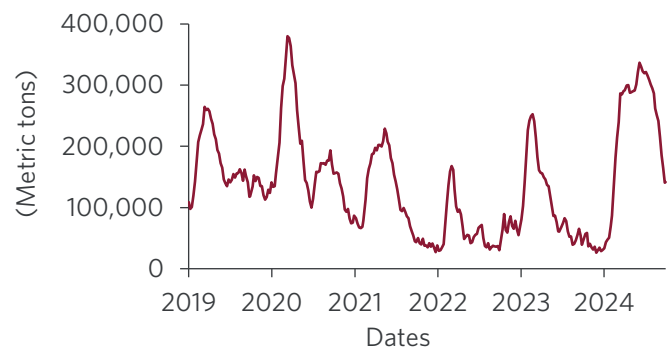
Commodities

Copper

The copper price drifted sideways throughout the summer, trading between US\$4.00 and US\$4.20/lb. as market participants searched for direction. That direction was recently provided by China as stimulus measures announced at the end of September broke the lull and pushed the price back up to US\$4.60/lb.

On the demand side, we're seeing signs that Chinese buyers are more engaged. Copper inventory levels on the Shanghai Futures Exchange are falling from highs and the premium for copper cathode imports into China is increasing. These are two important signals we watch for in this key end-market for the red metal. While concerns around the Chinese property sector are certainly not behind us, the stimulus measures and recent copper demand data provide some near-term support for the price.

Shanghai Futures Exchange Copper inventory



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg. Data as at 30 September 2024.

Over the medium term, we continue to see a compelling case for copper price appreciation. The transition to a lower carbon economy will be copper intensive because of the need to manufacture renewable-energy-producing assets and to install the distribution networks needed to deliver low-carbon electricity to end users. The impact of this transition demand will outweigh slower demand from traditional sources—such as the Chinese property sector. We also expect the supply of copper will be challenged to meet this growing demand. Major new copper discoveries are becoming less common and located deeper underground than the previous generation of assets. Put together, we think growing demand and challenging new supply issues will put upward pressure on the copper price over the medium term.

Silver

Silver is a commodity that perhaps gets a bit less attention than its higher profile cousin gold. That said, since precious metal prices hit a bottom in February of this year, silver has actually outperformed gold by approximately 8% as late September.

The silver price is driven by many of the same factors as gold such as interest rate expectations, the US dollar outlook and geopolitics. However, for silver there are some nuances that also distinguish it from gold. Industrial demand for silver is growing at a much more rapid pace, driving a deficit in the market. Growth in solar power is driving a significant increase in demand for silver. Solar demand for silver was up 63% Year-over-Year (Y/Y) in 2023 and is forecast to continue growing as global solar capacity continues to be developed. With mine supply of silver effectively flat, we expect the silver market to remain in deficit over the near to medium term.

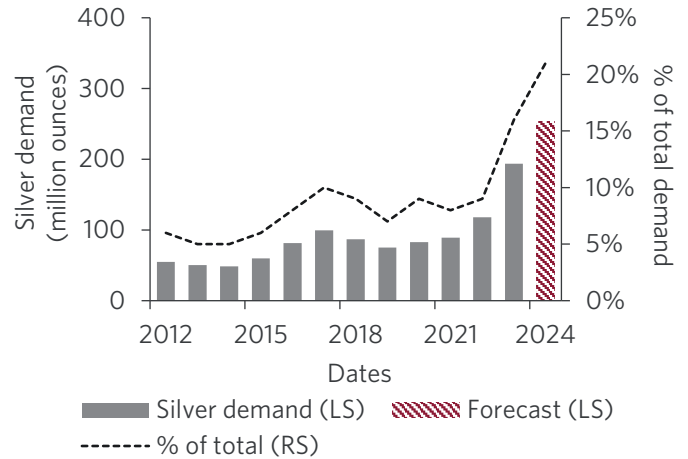
Gold to silver ratio



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg. Data as at 30 September 2024.

Despite the recent outperformance of silver and the growing demand from industrial applications, we note that the gold to silver ratio (the gold price divided by the silver price) currently sits at 84:1—well above the 10-year average of 79:1. If we look back even further, since the US came off the gold standard in 1971, the average gold to silver ratio over this period was 60:1. With growing industrial demand for silver and a market in deficit, we could see the silver price move back towards a more historically consistent gold to silver ratio. If we were to apply the 10-year average ratio of 79:1, that would imply a silver price of US\$33.75/oz, compared to the current spot price of US\$31.15/oz as of September 30, 2024, representing a 7% increase. And given the demand growth story we believe silver should actually trade at a premium to its 10-year average versus gold, implying even more price upside.

Silver demand in Photovoltaics growing rapidly



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 30 September 2024.

We continue to see a case for a strategic portfolio allocation to precious metals like gold and silver. This encompasses heightened geopolitical risk, an expectation of higher financial and economic volatility, lower interest rates and a residual risk of recession. Gold and silver are expected to represent a relatively consistent hedge to a wide range of tail risks.

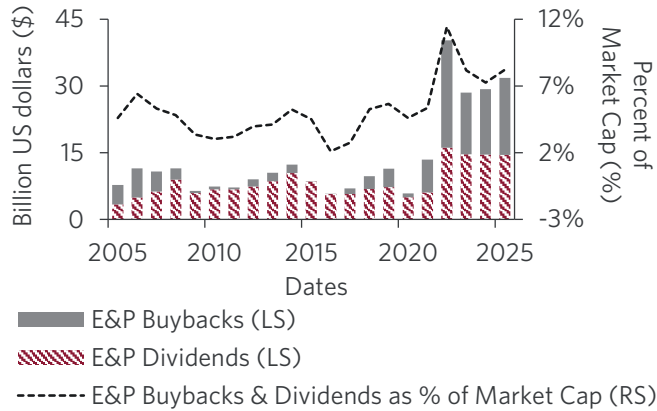
Oil

The oil price traded lower over the summer as uncertainty around both supply and demand weighed on the price. On the demand side, data out of key end user markets like China and India has been underwhelming. On the supply side, there is some uncertainty around OPEC+ compliance with quotas and the timing of the cartel returning idled barrels to the market. Both supply and demand factors moved some investors to the sidelines over the past several months as the market awaits more clarity on [the key drivers of the oil market](#).

In the very near term the market remains highly focused on the conflict in the Middle East and any potential for escalation into a wider regional war. As of now there has been no real impact on oil production as a result of the conflict, but that could change at any time. Recent escalations in the region have put a bit of a bid back into the oil price with the market starting to price in risks that Iran oil production could be disrupted.

While some uncertainty remains around OPEC+, North American producers remain focused on deleveraging and shareholder returns rather than significant production growth. We expect that trend to continue and will be watching for capital plans when budgets for 2025 are published later this year.

Energy sector: Returning cashflow to shareholders



Source: Bloomberg, Peters & Co., and CIBC Asset Management. Data as at September 30, 2024.

Over the medium to longer term, we still expect oil demand to grow in line with global population and GDP growth, consistent with the trend seen over the last 30 years.

Putting all this together, we see support for oil at US\$65/bbl. and continue to think that West Texas Intermediate (a common standard benchmark for oil) will trade between US\$70/bbl-US\$80/bbl during coming quarters with temporary deviations outside this range dictated by the ebb and flow of geopolitical risks and macroeconomic data. This would represent a healthy price for Canadian producers who will likely continue to generate meaningful free cash flow at these levels. Cash flow that can be used to support further deleveraging efforts and capital returns to shareholders.

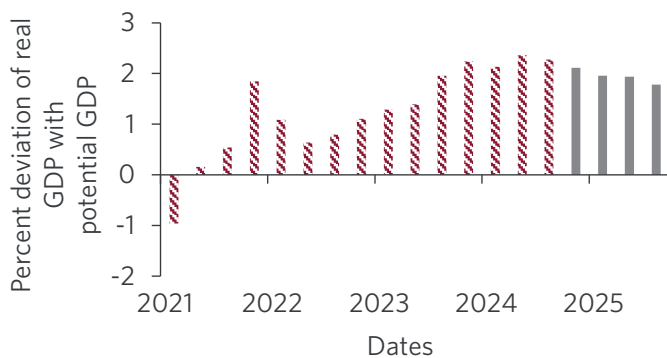
Economic analysis

US: Growth is slowing, not stalling

The US economy has been remarkably resilient in the first half of this year and good times are projected to continue rolling. However, with the economy moving into its fifth year of expansion, a growth slowdown is to be expected. We expect this to be relatively benign. With Y/Y real GDP growth expected to decelerate from 3.0% to 1.9%, there won't be much rebalancing achieved with excess demand conditions prevailing for a second year in a row.

With inflation considerably declining since peaks were reached at more than 5% a year ago, US households and businesses can finally breathe easier. It also means that the Fed now has the necessary leeway to deliver more rate cuts—providing even more breathing room to the real economy. These are welcome developments, justifying our optimism about US economic growth prospects.

A very slow US economic rebalancing



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 30 September 2024.

However, there is an important nuance. In our opinion, the Fed will be cutting less than currently priced by market participants

because inflation is likely to bottom out above its policy target rate of 2%. The current inflation mix is highly unusual, with deflation in core goods but still-elevated inflation in services. Looking forward, taking core inflation all the way down to the target rate will prove to be harder than generally expected.

On politics, while policy divergences between the Democratic and Republican camps are formidable on the surface, we don't see a meaningfully different growth trajectory under either administration. Indeed, both parties are in favour of increasing spending, lowering taxes (or at least making the Tax Cuts and Jobs Act (TCJA) tax cuts permanent) and maintaining a hawkish tariff stance versus China. We also see a second Trump presidency penchant towards deregulation as broadly offsetting his broader tariff plan, some of which is anyway bound to be reined in as the former president builds leverage ahead of making new deals with trading partners.

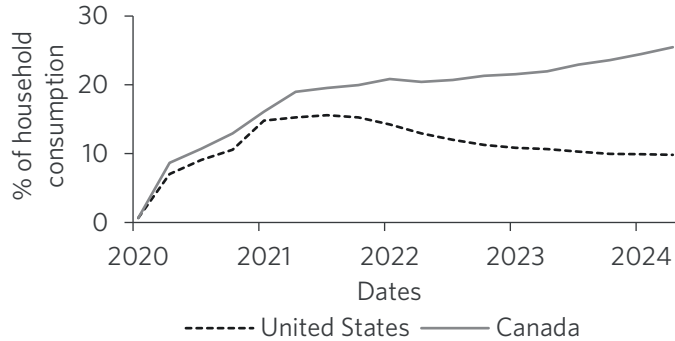
Canada: Solid growth could revive dormant inflationary pressures

Growth in Canada surprised to the upside in the second quarter mainly driven by the government sector and private non-residential investment. While household consumption was tepid, real disposable income growth continued to accelerate from an already fast pace, resulting in a higher household saving ratio. Unlike our US peers, Canadian households haven't deployed any of the accumulated excess household net savings since the pandemic, remaining in a stronger position from a balance sheet standpoint.

With the BoC cutting its policy rate, accumulated savings could be re-directed towards the purchase of interest-rate-sensitive durable goods and investments in housing. This is both good and bad news. While providing a welcomed boost to GDP growth, it could trigger renewed inflationary pressures if demand strengthens too significantly.

Canadian households are in a stronger position than US peers

Accumulated excess household net saving as percentage of household consumption



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 30 September 2024.

Inflation decelerated in the second and third quarters mainly driven by prices paid for goods. However, as in the US, service inflation is proving to be a lot stickier and will likely remain so given underlying forces. This makes the inflation deceleration path more uncertain with risk tilted to the upside. In turn, this raises doubts about the BoC’s ability to deliver as many cuts as markets are currently pricing.

Canada is experiencing a supply-driven rebalancing of its labour market owing to an unprecedented surge in its population. With the labour force headcount increasing faster than employment, the unemployment rate is trending higher. However, the disinflationary impact of this rebalancing remains muted because unemployment mainly concerns newcomers and because of the drag on productivity linked to [Canada’s recent population shock](#).

Inflation also remains a big concern because of population growth on housing market conditions. Excess demand conditions have led to a sharp rise in rental inflation—which is now running at its fastest pace since 1983. Strong upward pressures on rental prices are keeping shelter inflation at elevated levels despite the deceleration in mortgages interest cost inflation. Ultimately, a lot more housing supply will be needed to [restore balance in the Canadian housing market](#). However, this can only be achieved over the longer term. In the meantime, rental price inflation is not likely to decelerate much.

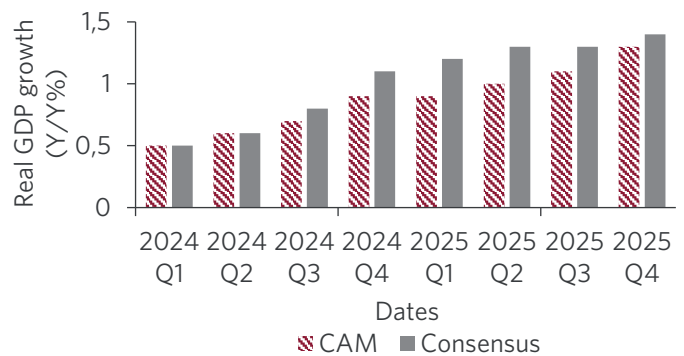
Against this backdrop, the Canadian economy is expected to strengthen with real GDP averaging 1.8% over the 12-month forecast horizon. The main risk is that the faster the Canadian economy expands, the higher the odds are that renewed inflationary pressures will limit the BoC’s ability to ease its monetary policy stance.

Eurozone: Economic green shoots

The eurozone economy has been mired in the mud for two consecutive years, trailing far behind the US in terms of growth. This has been a significant disappointment for European policymakers. After all, back in early 2023 hopes were running high that the eurozone economy would swiftly bounce after flirting with recession. In reality, 2023 real GDP only grew at 0.4% Y/Y against consensus and policymaker expectations of 2.1%. So far, 2024 hasn’t been much better with real GDP growth averaging 0.5% Y/Y, only half of what was expected by private sector forecasters, the ECB late last year.

Looking ahead, growth perspectives are more promising with real GDP growth expected to average 1.0% Y/Y over our 12-month forecast horizon. Economic activity is expected to be supported by rising real incomes, strengthening foreign demand and a fade of the dampening effects from previous monetary tightening. Having said that, eurozone growth isn’t expected to exceed its trend rate, and excess supply conditions are projected to still prevail by late 2025.

Eurozone economy to pick up pace



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 30 September 2024.

Under these conditions, eurozone inflation is projected to decelerate further. However, it will likely bottom out above the ECB’s 2% target. As in other Developed countries, the eurozone’s current inflation mix is highly unusual with still-elevated inflation in core services and particularly low inflation in core goods. We expect both core Harmonized Index of Consumer Prices (HICP) sub-segments to gradually reconverge, with some deceleration in core services and some increase in core goods inflation. If our projections for real economic activity and inflation materialize, the ECB will be well positioned to deliver more rate cuts, bringing its policy stance closer to neutral.

ECB policy easing is a key reason why we’re calling for improving economic growth prospects. Having said that, the eurozone economy’s recent underperformance is more than just a cyclical story. Europe is facing structural problems and needs to boost its competitiveness to avoid falling further

behind the rest of the world. After the second world war, the eurozone experienced strong catch-up growth driven by rising productivity and a growing population. However, both drivers of growth are now slowing. Growth in the working age population is starting to decline, mainly owing to declining birth rates without a big enough offset from net inward migration. Meanwhile, eurozone labour productivity is trailing the US, falling back below 70% of the US level.

As emphasized in [Mario Draghi's recently released competitiveness report](#), "Europe needs faster productivity growth to maintain sustainable growth rates in the face of adverse demographics". Mr. Draghi was the man hailed as saving the eurozone during the sovereign debt crisis when he was president of the ECB. He is now making it crystal clear that the eurozone needs to invest an enormous amount in a relatively short period. Whether Draghi's plan to jumpstart Europe's moribund economy will unfold remains to be seen. Will measures be put in place? If so, at what speed and will they be big enough to make a difference? There are still a lot of unknowns. However, it certainly justifies taking a more constructive view about Europe's longer term growth prospects.

China: Stimulus is finally coming. Now what?

An important policy pivot is underway. For more than two years, Chinese policymakers remained reluctant to launch a more significant stimulus. Recently, important pro-growth measures were announced and signaled a stimulus large enough to stabilize Chinese growth, reduce downside risks and positively contribute to a constructive global growth outlook.

With pain thresholds being reached, Chinese policy makers decided it was time to take action. Despite previously announced stimulus, the housing sector continues its alarming implosion. Home prices continue falling across China, further hurting the rest of the economy—including labour markets. The youth unemployment rate has risen above 20%, higher than the peak seen during the pandemic lockdowns. Without more policy support, China is at risk of facing an important vicious cycle between low inflation, excessive indebtedness, declining confidence, home price deflation and rising unemployment.

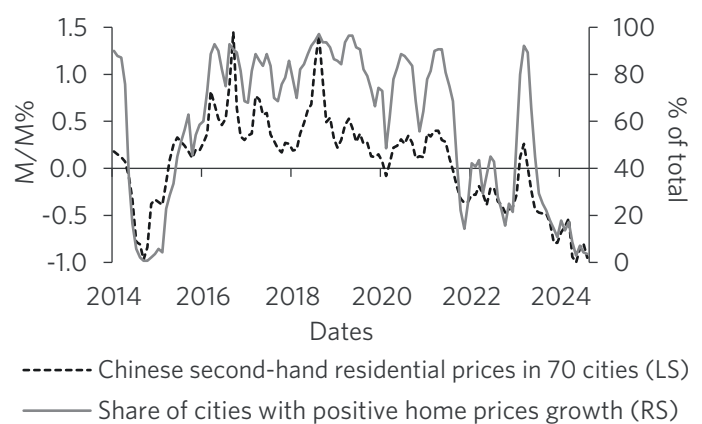
In terms of further policy support, several key announcements are still missing. Overall, we have kept our stimulus outlook broadly unchanged, and look for an increase of government bonds issuance in excess of 3% of GDP and financial support close to 2% of GDP intended to stabilize housing. Policymakers could announce bigger numbers in the eventuality of a Trump re-election or further housing sector weakening.

While the projected increase in bond issuance is substantial, it will likely have a low economic multiplier. Two-thirds of the issuance is expected to be used to finance transfers and debt swaps for distressed local governments who aren't in a position to boost spending owing to the collapse of land sales, a key source of revenue. The remaining third is expected to be used to finance subsidies for consumption trade-ins and equipment upgrades. The economic impact of consumption subsidies has been modest in the past. Tailwinds from equipment upgrade measures should be limited given excess capacity.

The most important development is the political willingness to stabilize housing. Details are still missing but achieving housing stabilization requires two complementary policies. First, financial support for the completion of stalled housing projects under construction. We estimate that the stalled construction stock accounts for at least 5% of GDP. Second, housing upgrade policies are needed to incentivize households to move from low-quality self-built homes to newly finished units. Given that self-built homes still represent 15%-20% of the total housing stock, converting low-quality properties into state-subsidized housing could advance President Xi Jinping's vision of "common prosperity" and foster a more equitable society—while absorbing housing supply.

While the stimulus is not a panacea, it's still good news for the global economy. Although it's not large enough to stop China from exporting deflation, it can stabilize the Chinese economy while considerably reducing downside risks. Chinese GDP growth is forecasted to average 4.5% over the next 12 months.

Imploding housing, pain threshold reached for policymakers



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Alternative economic scenarios

Global policy relief (50%)

This is our baseline scenario. US economic rebalancing and decelerating inflation allows for the Fed to cut rates to 3.5%. This policy relief will allow the US economy to experience a fifth year of economic expansion with real GDP averaging 1.9%. The US output gap will stay positive for a second year in a row, meaning excess demand will prevail. This will eventually limit the Fed's leeway to deliver as many rate cuts as priced by the market consensus. Global growth is projected to average 2.8% Y/Y over the next 12 months. Bond yields are expected to move gradually toward fair value slightly above 4% and the yield curve to steepen. Equity markets will likely perform well, driven by moderate earnings growth and little change in P/E ratios.

Global growth slowdown (25%)

Underestimating the impact of past monetary policy tightening represents one of the main risks to our baseline view. Under this alternative scenario Fed policy easing comes too late with the US economy downshifting into lower gear. Real GDP growth averages 0.5% Y/Y over the 12-month forecast horizon. Inflation would decelerate below the Fed's target of 2.0%. With the output gap turning negative and lower inflation, the Fed would be able to deliver bigger rate cuts taking the policy

rate below its neutral level. Bond markets would rally further, with yields falling. The yield curve would steepen a lot more than in the baseline scenario. Earnings would likely disappoint consensus expectations and investors would mark down the P/E multiples, leading to negative equity returns.

Inflation upturn (25%)

Under this scenario the Fed overestimates the impact of past tightening. The policy easing likely to occur in coming months would likely keep the US economy stuck in high gear with real GDP growth averaging 2.8% Y/Y over the 12-month forecast horizon. Excess demand conditions would continue to prevail, and the labour market would remain tight. As a result, inflation would trough over the first half of the forecast horizon and subsequently drift higher to reach 2.8% at the end of the period. The Fed would move to the sideline earlier than generally expected. The pullback in bond markets would be more pronounced than in our baseline scenario with 10-year Treasury yields moving above our central target level of 4%. The yield curve would steepen more modestly. This scenario would initially likely be positive for equities because of stronger GDP growth. However, as evidence becomes clearer that inflation is moving back up, the rally would be cut short and equities would be expected to roll over.

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