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>>>> ABSTRACTS <<<<

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NEWSLETTER & WEBSITE TITLE [max 170 characters]

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Clear for landing: Coming in steep, adjusting monetary and fiscal thrusters



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IN A NUTSHELL

- Disinflation and slower hiring open reentry window: Adjust policy mix to land softly
- 2024 is an election year amidst Fed pivoting: The election will be consequential
- Slow global growth ahead: What if the US sneezes or catches a cold?
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Disinflation and slower hiring open reentry window: Adjust policy mix to land softly

We still expect an economic soft landing for the US with slowing growth through mid-2025 and then moderate re-acceleration to trend in late 2025. With the right balance of monetary and fiscal adjustments over the coming quarters, we see high chances for an extended healthy economic expansion of several more years. But now is the time for the pilots and flight control to carefully configure the use and sequence of their maneuvering thrusters.

The first maneuver will be rolling monetary policy. Our economists expect the first U.S. Federal Reserve (Fed) rate cut later this month to be 25 basis points (bp), followed by further cuts over the coming 12-months to lower the top-end of the range Fed Funds rate to 4.0%. The second maneuver should be pitching to slower fiscal policy to prevent overheating upon reentry as the Fed aims to normalize rates. In our view, substituting Harris for Biden improved Democrat's chances this election and hence raises the chances of fiscal tightening after the election primarily in the form of tax hikes. Optimizing the balance between monetary loosening and fiscal tightening, particularly not overdoing either, is crucial to maximizing the chances for a healthy long-lasting expansion.

2024 is an election year amidst Fed pivoting: The election will be consequential

Vice President Harris is campaigning on the back of many Biden policies, including tax hikes; albeit more moderate tax hikes than previously proposed by Biden, yet he never aggressively pursued. Biden's fiscal policy was basically borrow to spend and Trump's was borrow to cut taxes; of course both saw their borrowing as investments for growth. The fiscal situation today and trajectory, call for a slower pace of borrowing and addressing the spending vs. tax tradeoff. Both US politics and difficult to control secular trends suggest that counting on spending cuts is mere long-shot optimism, especially for the bond market and monetary policy setters. Thus, it might be that a proper soft landing of monetary policy with no recession near-term and also with inflation returning to and being well anchored at 2% requires some tax hikes. We don't see this as the best possible path, but it might be the safer path ahead, bringing slow growth with benign inflation and benign interest rates. Harris proposes a 28% US corporate tax rate from 21%, which would likely hit S&P earnings per share (EPS) by about 7%. She also calls for an increase in the top capital gains rates to 28% from 20% and an increase in the Affordable Care Act's tax on investment income from 3.8% to 5%. When Trump personal tax rates sunset, Harris is expected to push for a more progressive structure.

Slow global growth ahead: What if the US sneezes or catches a cold?

Beyond the US, economic activity is muted but not falling off the cliff. Unlike the past 20 years, China is no longer the locomotive for the global economy; quite the opposite: hit by its housing downturn and weak domestic demand. China is exporting its manufacturing overcapacities into Europe and worldwide. Weak China construction, coupled with soft global manufacturing and goods demand, suggests that commodities and goods will not be major inflation risks barring no further geopolitical shocks. Services remain the lingering inflation risk for the developed world and especially the US. Key service spending categories like healthcare, insurance, education/childcare, etc. Also, ongoing utilities and local tax hikes make cost of shelter an issue beyond monthly rent or home price/mortgages payments. Investors remain optimistic about profitable and productivity driving Artificial Intelligence (AI) to help.

DWS CIO Day strategic 12-month targets: S&P 500 to 5800, 10-year Treasury Yield to 4%

We raise our S&P 500 target to 5800 from 5600 primarily on lower nominal and real interest rate expectations across the curve, while still expecting soft landing scenarios to prevail. We lowered our 10-year Treasury yield target to 4.05% from 4.25% and thus lowered our S&P real cost of equity to 5.4% from 5.5%. We did not change our S&P EPS forecasts: \$245 in 2024, \$270 in 2025, \$300 in 2026. However, our S&P targets do not ignore the potential for tax hikes hitting our EPS estimates or affecting our interest rate outlook which is uncertain.

Cautious on stocks into election, afterward moderate gains and better breadth

Our preferences remain for large caps and balanced style exposure. While we expect better breadth beyond the magnificent seven, we do not see either an economic acceleration or commodity or banking outlook that would justify a rotation to cyclical value. Our preferences remain Health Care, big Banks and Insurance, Utilities and select Capital Goods. We're still under-weight Tech, but mostly at Semiconductors. We are broadly more cautious on Consumer Discretionary upon slower growth, jobs and likely tax hikes ahead.

Glossary

Artificial intelligence is the theory and development of computer systems able to perform tasks normally requiring human intelligence

One **basis point** equals 1/100 of a percentage point.

Cost of equity (CoE) is the return (often expressed as a rate of return) a firm theoretically pays to its equity investors, to compensate for the risk they undertake by investing their capital.

describes a slowing of the pace of price inflation.

Earnings per share (EPS) is calculated as a company's net income minus dividends of preferred stock, all divided by the total number of shares outstanding.

The term **federal funds rate** refers to the target interest rate range set by the Federal Open Market Committee (FOMC). This target is the rate at which commercial banks borrow and lend their excess reserves to each other overnight.

Fiscal policy describes government spending policies that influence macroeconomic conditions. Through fiscal policy, the government attempts to improve unemployment rates, control inflation, stabilize business cycles and influence interest rates in an effort to control the economy.

Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.

Large cap firms generally have a market capitalization of more than 10 billion dollars.

Monetary policy focuses on controlling the supply of money with the ulterior motive of price stability, reducing unemployment, boosting growth, etc. (depending on the central bank's mandate).

Productivity measures how much economic output is produced for a given level of inputs (such as capital and labor).

The **S&P 500** is an index that includes 500 leading U.S. companies capturing approximately 80% coverage of available U.S. market capitalization.

A **soft landing** is when an economy's rate of growth slows in a controlled fashion without major disruptive effects on employment, external balances etc.

The **U.S. Federal Reserve**, often referred to as "**the Fed**," is the central bank of the United States.

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