2024 Global Market Outlook
Midyear Update

How central bank policy could impact your portfolio

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2024 Global Market **Outlook**

Midyear Update

Nikolaj Schmidt
Chief Global Economist

Ken Orchard
Head of International Fixed Income

Peter Bates, CFA
Portfolio Manager, Global Equities

Tim Murray, CFA
Capital Markets Strategist, Multi-Asset Division

All eyes on central banks

We are pleased to share our outlook for global economies and markets for the second half of 2024.

In the six months since we published our 2024 Global Market Outlook, the market environment has changed in many ways. Consensus expectations for central bank policy, in particular, are markedly different. Prices of interest rate futures reflect expectations for far fewer interest rate cuts from global central banks than seemed likely in December 2023. Equity and fixed income markets are readjusting accordingly.

The European Central Bank (ECB) kicked off the cycle of lowering rates by the major developed market central banks at its June policy meeting. But the path and magnitude of easing by the world's rate setters for the rest of the year is far from certain. This outlook details the factors shaping that path for the Federal Reserve (Fed) and other key central banks.

For the global economy, we anticipate broadening growth. While the U.S. remains strong, leading indicators elsewhere suggest that the narrative of U.S. economic exceptionalism may abate.

What does this backdrop mean for markets and asset classes? We expect a broadening in U.S. equity market performance and see attractive value in some international stock markets. Investors seeking to move out of cash may find attractive opportunities in shorter-term bonds, as well as equities.

Most importantly, we believe the ongoing transition from the low rates that prevailed after the 2008–2009 financial crisis to an environment characterized by structurally higher interest rates will present favorable conditions for active managers to outperform.

Broadening global growth, resurgent inflation define outlook

Six months ago, the consensus outlook for the global economy in late 2024 featured steadily falling inflation amid a slide toward recession that would trigger aggressive central bank rate cuts. The best outcome would be a "soft landing" slowdown that dodged a recession thanks to central bank action. Investor hopes for this scenario led to simultaneous rallies in equities, high-quality government bonds, and bonds with credit risk.

What a difference a few months make: Consensus now expects continued expansion, resurgent inflation pressures, and limited easing from central banks. We're not quite as sanguine on growth as this "no landing" scenario, but it looks like recession is off the table for at least the next six months.

Broadening of global growth

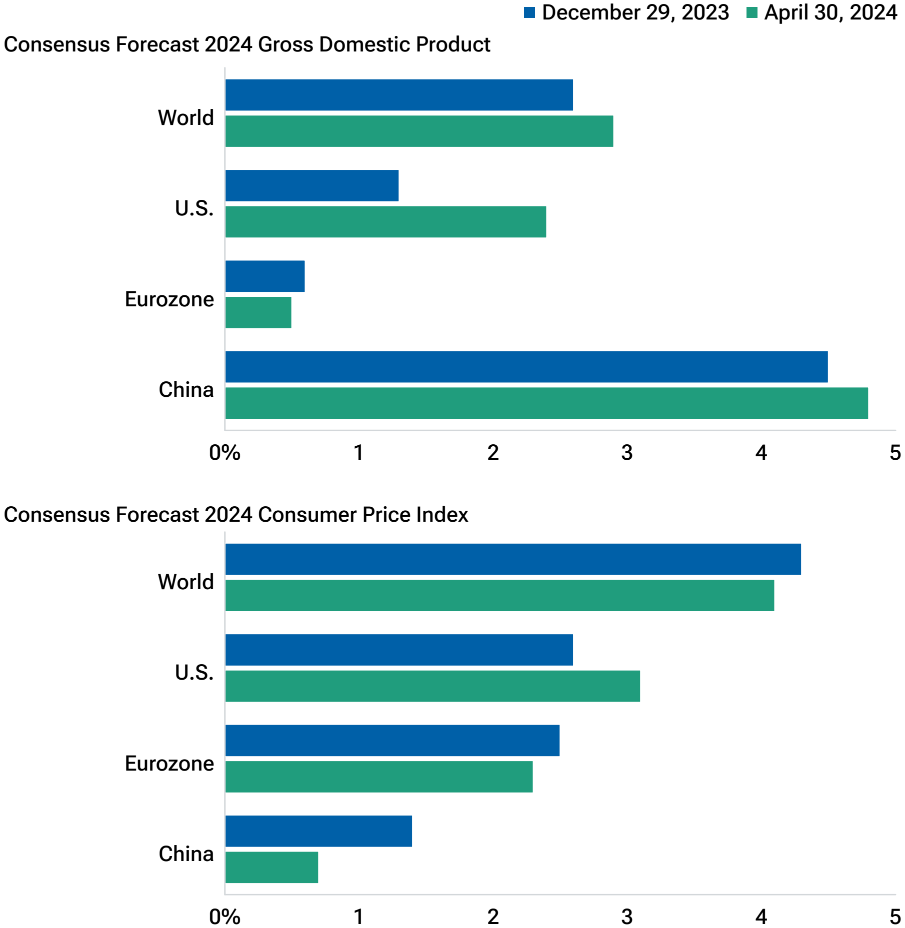
The consensus also still involves U.S. exceptionalism, with U.S. expansion easily outpacing anemic growth in other developed markets. But U.S. first-quarter growth disappointed. With leading indicators in the eurozone moving smartly higher, we could easily see an overall broadening of global growth, undercutting the U.S. exceptionalism narrative.

"...recession is off the table for at least the next six months."

Nikolaj Schmidt
Chief Global Economist

More growth, more U.S. inflation

(Fig. 1) How consensus forecasts have shifted since the end of last year



As of April 30, 2024.
Source: Bloomberg Finance L.P.
There is no guarantee that any forecasts made will come to pass.
The consensus forecasts are for full-year 2024 GDP and CPI figures, taken at the end of December and the end of April, respectively.

The European Central Bank at its June meeting became the first major developed market central bank to cut interest rates. The Bank of England (BoE) looks poised to be the next to ease ahead of the UK general election on July 4, followed by the Federal Reserve. Because of the weaker starting point for the eurozone economy, we think the ECB will cut the most in 2024, with sticky inflation keeping the Fed to only one or possibly two rate reductions of 25 basis points each.

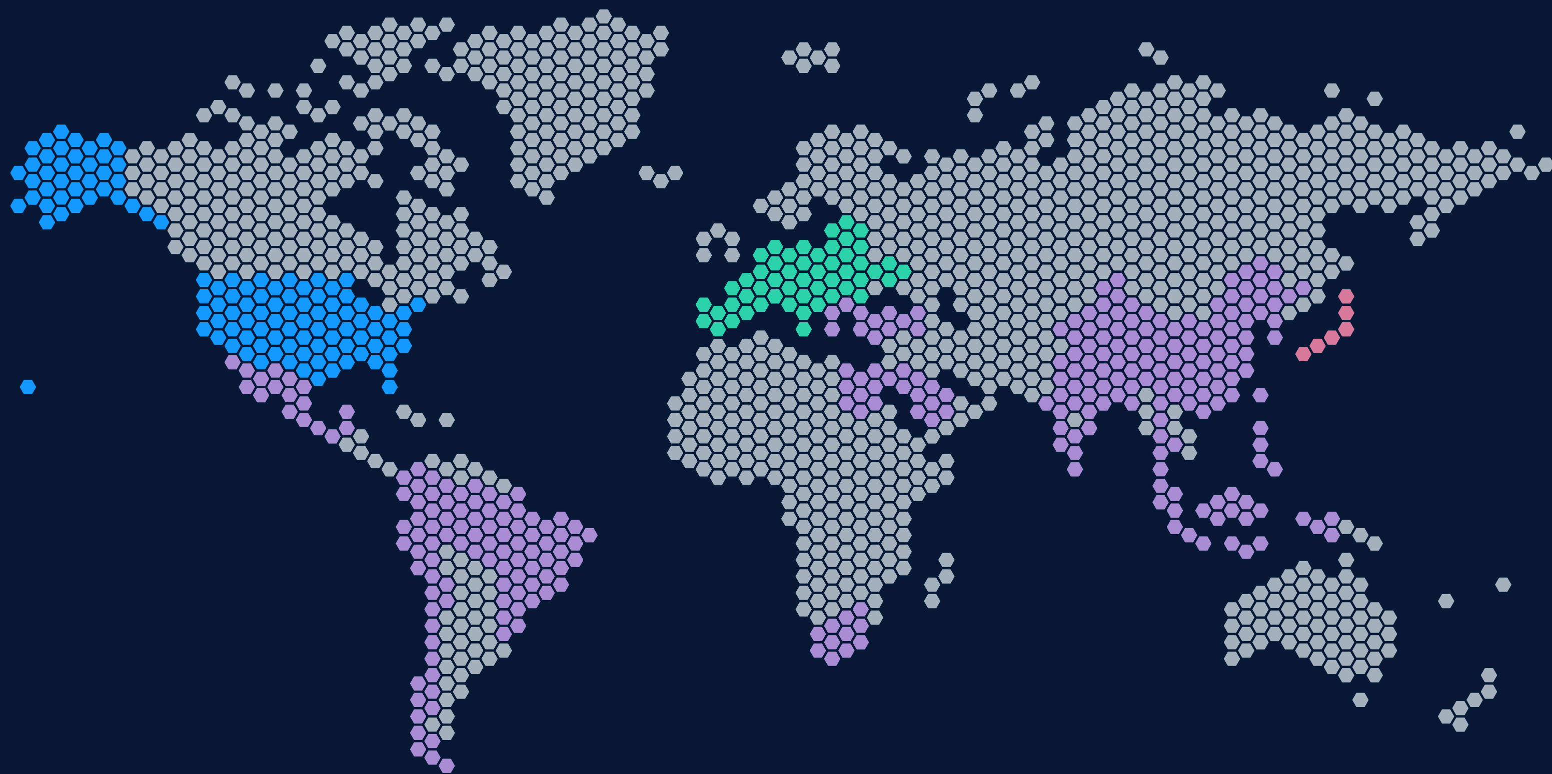
Which way for monetary policy in 2025?

The overarching question is: Where will this bring monetary policy in 2025? Even modest rate cuts this year could easily lead to reaccelerating growth—and inflation that would force the Fed to raise rates next year, with other major central banks following close behind. This could mean that central banks will be tightening policy as the labor market weakens going into the next recession.

In this unusual scenario, we would expect more divergence in returns as investors sort through the implications for sectors and individual securities. Active portfolio management, with a focus on fundamental analysis and relative value, would be vital in this environment.

Global macro and monetary policy guide 2024

As of May 31, 2024.



	U.S.	Eurozone	Emerging Markets	China	Japan
Growth	Outperformance of the U.S. economy versus developed markets to taper.	Economy faces medium-term challenges from tighter fiscal impulse.	Improving global picture is expected to support emerging markets (EM) economic growth.	Policy is modestly supportive, constrained by subdued credit impulse.	Growth expected to pick up, driven by increases in real (inflation-adjusted) incomes.
Inflation	Inflation unlikely to fall to target, with services proving sticky.	Inflation should gradually come down to target, with the risk being services.	After a rapid fall, the disinflation trend is starting to meet some resistance in EM.	Difficult to see much upward inflationary pressure without a credit cycle.	Core inflation expected to remain well below target, with yen posing upside risks.
Monetary policy	Maximum two cuts this year; resilient data to keep rates higher for longer.	ECB became first major developed market central bank to start cutting rates in June.	EM central banks to slow cuts due to currency weakness concerns.	Incremental easing to continue through balance sheet instead of rate cutting.	Window to deliver further hikes is narrowing amid weakening inflation momentum.

For illustrative purposes only. Actual future occurrences may differ, perhaps significantly, from expectations.

Murky environment to challenge Fed policymakers

Investors have steadily ratcheted back their expectations for Federal Reserve rate cuts in 2024. In most previous economic cycles, the Fed has been the first to ease, but the ECB was the first mover this time. We still see a slight possibility of a Fed cut this summer followed by the central bank cutting 25 basis points at its December policy meeting, after the November elections are out of the way.

Fed policymakers seem eager to implement an "insurance cut" or two in 2024 to preempt a slowdown—assuming that inflation moderates. The Fed believes that monetary policy is tight, so it would only take modest softening in the labor market to convince the central bank to cut.

The Fed wants to avoid any sign that it is influenced or motivated by politics, so will not act at the September or November Federal Open Market Committee (FOMC) meetings. In fact, a July rate reduction might be earlier than the Fed would act if it were not an election year.

Elevated potential for Fed surprises

The potential for surprises from the Fed is much greater than in a typical late-business-cycle environment. There's an increasing chance that a lack of progress on getting annual core inflation to 2% will prompt the Fed to keep rates steady for an extended period. Stepping back for a broader view, we are more likely to see the Fed surprise with fewer cuts than with more. Preempting the question on whether it is possible that resurgent inflation could prompt the Fed to raise rates later this year, we place less than 20% odds on that outcome.

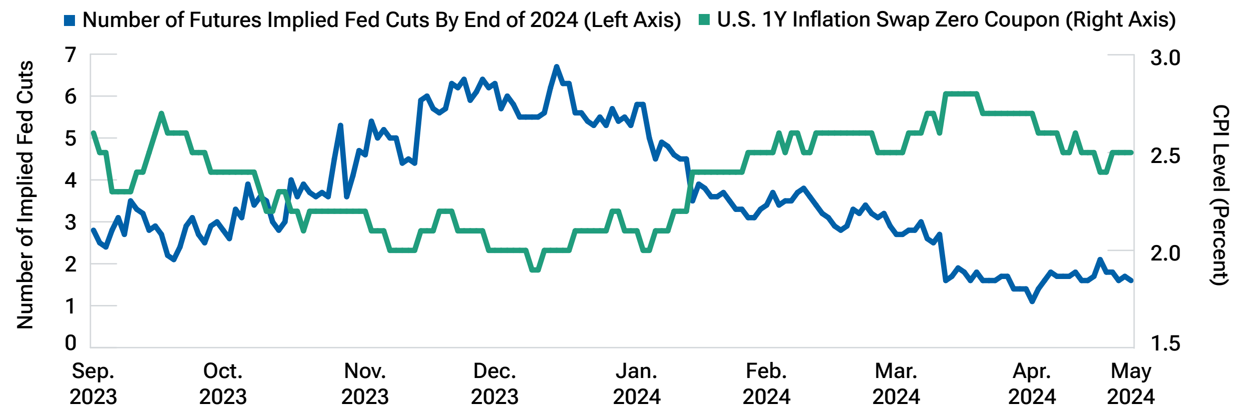
The outlook for Fed easing in 2025 is even murkier. Two to three cuts in 2025 are priced in now, which appears too dovish. One or two rate reductions next year seems more realistic. And there is a risk that "insurance cuts" by the Fed could allow inflation to fester and raise the chances of the Fed moving back to a hiking bias in 2025.

Key takeaway

The Fed is more likely to surprise with fewer cuts than with more.

Rate cut expectations have fallen steadily in 2024

(Fig. 2) Rising inflation concerns have dampened anticipation of significant easing



As of May 22, 2024.
Source: Bloomberg Finance L.P.
Actual outcomes may differ materially from any expectations made.

ECB and BoE to cut as BoJ remains an outlier

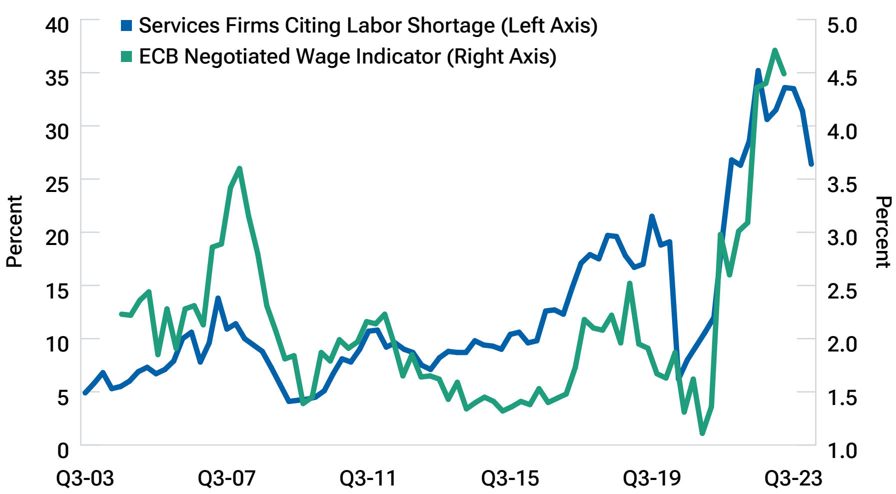
For all developed market central banks (excluding the Bank of Japan (BoJ), which is an outlier), monetary policy is quite tight. They will want to avoid tipping their economies into recession. Consequently, these central banks can cut while preserving a tight monetary policy stance. In fact, they will probably ease proactively if inflation allows—if they wait until economic activity craters before cutting, they will be far behind the curve because it will be a long way back to neutral.[1]

[1] The neutral rate neither stimulates nor restrains economic growth.

Persistent wage growth will make ECB cautious over easing

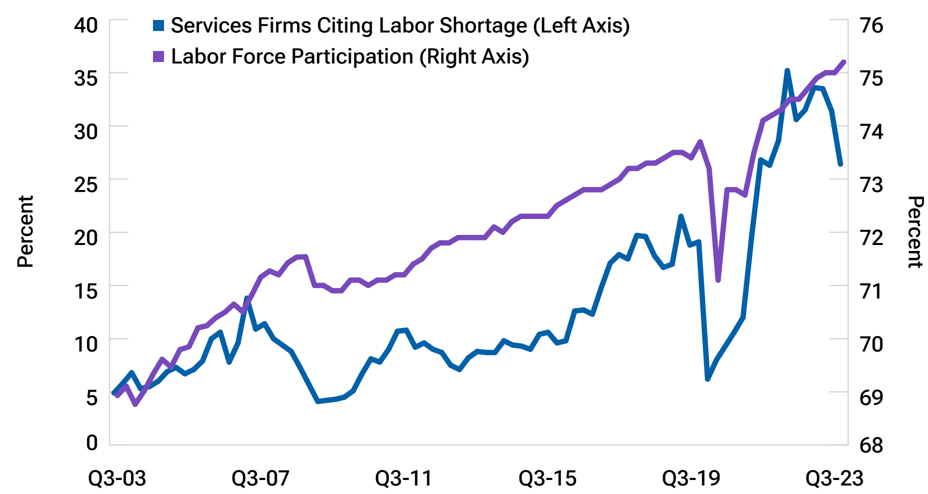
(Fig. 3) The eurozone economy could be susceptible to an abrupt labor market slowdown

Labor Shortage vs. Eurozone Wages



As of May 24, 2024.
Sources: ECB, European Commission.

Eurozone Labor Demand vs. Labor Supply



As of May 24, 2024.
Sources: European Commission, Eurostat.

Fears of labor market cracks lead ECB to act

Eurozone inflation has fallen to the extent that the ECB was able to cut rates in June. ECB policymakers think that eurozone employers have been hoarding labor over the past 12 months. This makes the region's economy susceptible to an abrupt labor market downturn if corporate profit margins come under pressure amid softer final demand.

The big questions are: When will the ECB ease after June, and how large will the cuts be? The number of expected cuts has been steadily dropping, but we believe the ECB will likely cut twice before the end of 2024—however, it could be as few as once or as many as three times.

BoE likely to follow in the third quarter

There have been hopes that the BoE would follow fast on the heels of the ECB by cutting rates later in June, but we believe it may be a little later than that. With tentative signs that the UK economy is recovering, the BoE may not feel it needs to rush in cutting rates and is likely to wait until the autumn before doing so.

Gradual tightening from the BoJ

Japan has also struggled with inflation—but the lack of it rather than prices rising too quickly. After finally moving away from its subzero rates policy earlier in 2024, we expect the BoJ to continue gradually tightening while sounding dovish enough that the market doesn't undo its work in boosting inflation. By tightening policy, the BoJ would also support the yen, which has plumbed multi-decade lows against other major currencies in 2024.

"The BoE may not feel it needs to rush in cutting rates...."

Ken Orchard
Head of International Fixed Income

Central bank decisions to watch

June 6
ECB became the first major developed market central bank to cut rates

June 12
Fed likely to stay put at FOMC meeting

June 14
BoJ could continue to tighten policy

July 31
Fed could make its first rate cut

September 18
With the U.S. presidential election on the horizon, Fed policymakers likely hesitant to cut

September 19
Possible first cut from the BoE

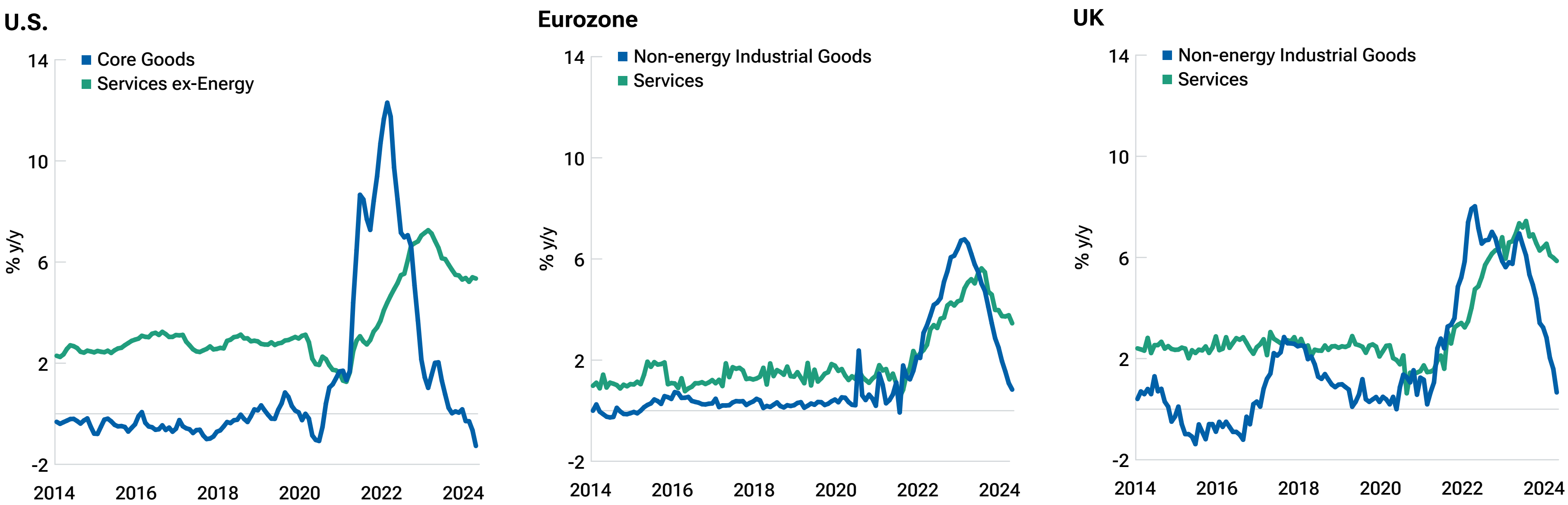
November 7
Two days after presidential election, Fed likely to hold rates steady

December 18
Look for the Fed to lower rates

Reaccelerating inflation to make central banks walk tightrope

Developed market services inflation is proving sticky

(Fig. 4) Goods inflation is falling much faster



As of April 30, 2024.
y/y=year-over-year.
Source: U.S. Bureau of Labor Statistics, EU Statistical Office of European Communities, UK Office for National Statistics/Haver Analytics.

Inflation is notoriously difficult to predict, and it has continued to baffle most forecasters since the onset of the pandemic in 2020. However, it's becoming clear that inflation isn't going away, and we see a meaningful risk that it will reaccelerate as U.S. exceptionalism moderates and global growth broadens.

Several factors drive risk of reaccelerating inflation

The big decrease in global inflation from 2022 to 2023 was due to goods disinflation, which is the easy part of taming inflation. Now services inflation, which is sticky, needs to fall. But for this to happen, the labor market must have space to adjust—wage pressures drive services inflation, and higher unemployment is required to control wage pressures. Artificial intelligence (AI) is one countervailing force that could help tame services sector wage growth, but AI will take time (and expense) to implement, making it a longer-term factor.

Fiscal spending in an election year will also put upward pressure on inflation, and energy prices—which have been a headline inflation tailwind since surging in 2022 following Russia's invasion of Ukraine—are a wild card that could easily spike again if conflict in the Middle East escalates or other geopolitical hot spots erupt.

These factors would, of course, make central banks' difficult balancing act between supporting growth and restraining inflation that much harder.

Because we see renewed upward pressure on inflation, investors may benefit from exposure to real assets such as commodities—including gold and silver—and real estate or to inflation protected government bonds. Real assets tend to hold up well in inflationary environments, while inflation-protected government debt has principal and interest payments that adjust based on inflation data.

Key takeaway

The big decrease in global inflation from 2022 to 2023 was due to goods disinflation, which is the easy part of taming inflation. Now services inflation, which is sticky, needs to fall.

U.S. stocks face a broadening, not a rotation

In recent years, the U.S. stock market has been dominated by the "Magnificent Seven" technology stocks, but there are signs this once-monolithic group of large-cap growth firms is beginning to fragment. The outperformance of the Magnificent Seven propelled the S&P 500 to new highs earlier this year and resulted in the index becoming concentrated to an unprecedented degree.

Performance within the group is now diverging, however— as of late May, NVIDIA, Meta, Microsoft, and Amazon have continued to outpace the market, while Apple, Alphabet, and Tesla have begun to lag. As the benefits of AI technology are unlikely to be evenly spread among the members of the Magnificent Seven, further dispersion within the group can be expected.

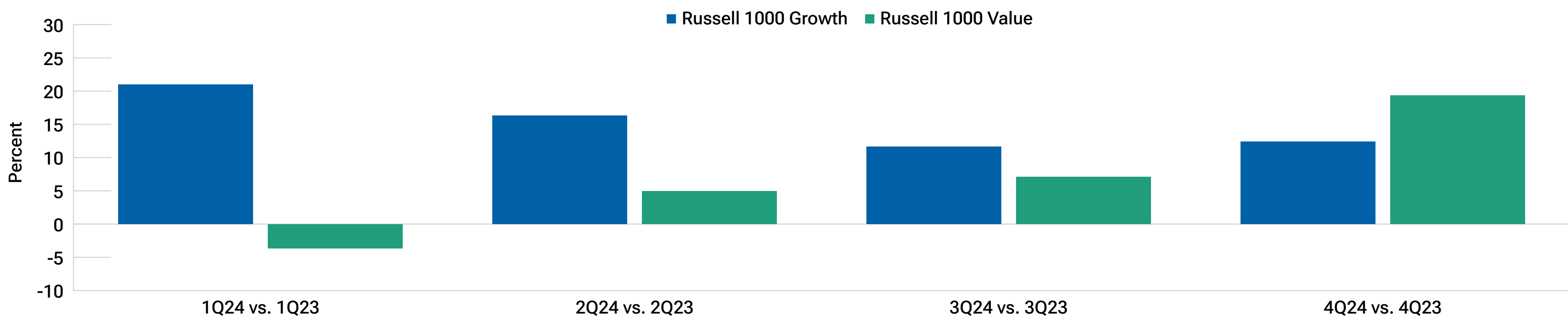
Fewer cuts should favor value stocks

Meanwhile, value stocks could be primed for a comeback as investors seek to diversify their exposure beyond the Magnificent Seven, particularly given growing expectations that the higher rate environment will persist. If the Fed only makes a few cuts or does not cut at all, value companies should benefit as they have tended to be more rate-sensitive and have typically fared better in a world where interest rates

Past performance is not a reliable indicator of future performance and is subject to change.

Value stocks look poised for earnings resurgence

(Fig. 5) Estimated earnings per share of value stocks set to outstrip growth stocks later this year



As of May 13, 2024.
Source: FTSE Russell (see Additional Disclosures).
Actual outcomes may differ materially from estimates.
Each time period shows the estimated year-over-year change in quarterly earnings for growth and value stocks for each quarter this year.

remained higher for longer. And while value stocks have begun to perform better in recent months, they continue to trade at a significant discount to growth stocks. If conditions continue to favor value stocks—as we believe they will—the dominance of growth stocks may start to fade.

Small-cap stocks are trading at a major discount to larger companies after struggling for several years against high inflation and a steep rise in borrowing costs. While the persistence of a higher rate environment could limit the upside of small-cap stocks, the earnings of smaller firms should improve if rates come down.

A widening opportunity set

Although we believe that value—and possibly small-cap—stocks may begin to challenge the dominance of large-cap growth stocks, it is important to stress the difference between a broadening of the market's opportunity set and a rotation between market styles, sectors, or capitalization. We are not predicting the imminent demise of the Magnificent Seven—rather, we anticipate a continued broadening of opportunities to include more companies and sectors across the market that may have lagged in recent years.

> **"...we anticipate a continued broadening of opportunities to include more companies and sectors across the market that may have lagged in recent years."**

Peter Bates, CFA
Portfolio Manager,
Global Equities

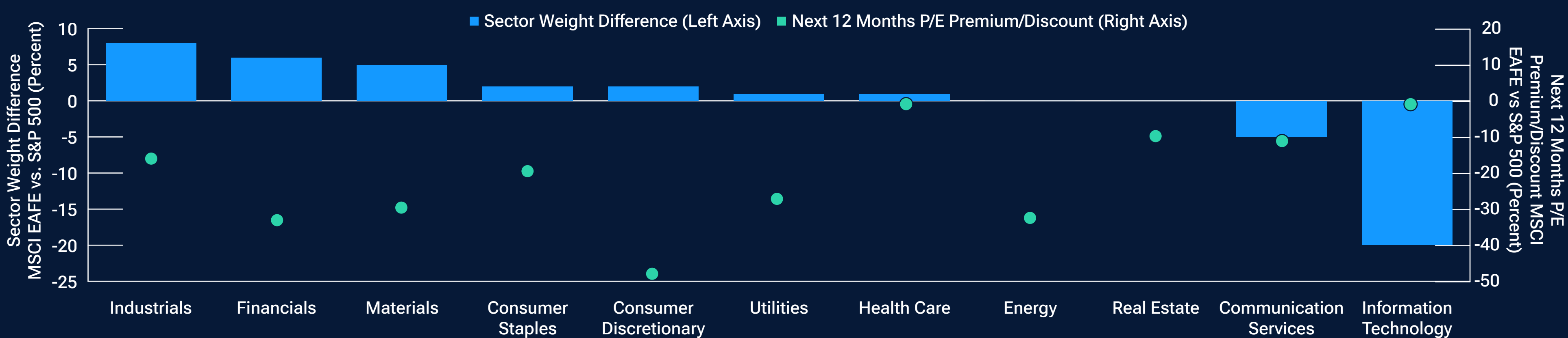
International stocks still appear to be good value

Fueled by the outperformance of growth technology stocks, U.S. equities reached all-time highs earlier this year, pushing their premium versus international (i.e., non-U.S.) stocks to 20-year wide levels. International stocks remain favorably valued but are fundamentally more attractive in the post-COVID environment, as demonstrated by improved earnings growth in recent years. This is because, in contrast to the U.S. market's heavy exposure to growth stocks, the international market is more exposed to value-oriented sectors such as financials, materials, industrials, and energy, where we see secular support in the years ahead. The S&P 500 Index, for example, has a very different sector composition from the MSCI EAFE Index.

Supply chain diversification, infrastructure rebuild, defense spending, and the likelihood of higher energy prices should favor traditional value sectors as capital spending accelerates. As these sectors are currently cheaper and, in some cases, have a lower earnings bar than their U.S. counterparts, investors seeking diversification from large-cap tech growth stocks may seek to increase their exposure to select international markets.

The MSCI EAFE Index is not an ex-U.S. S&P 500 Index

(Fig. 6) Sector weightings and valuations contrast sharply between the two indices



As of April 30, 2024.
Source: T. Rowe Price analysis using data from FactSet Research Systems Inc. All rights reserved. Please see Additional Disclosures page for more information about this Standard & Poor's information.
These statistics are not a projection of future results. Actual results may vary.
P/E= price-to-earnings.

Improving corporate governance is driving Japanese stock performance

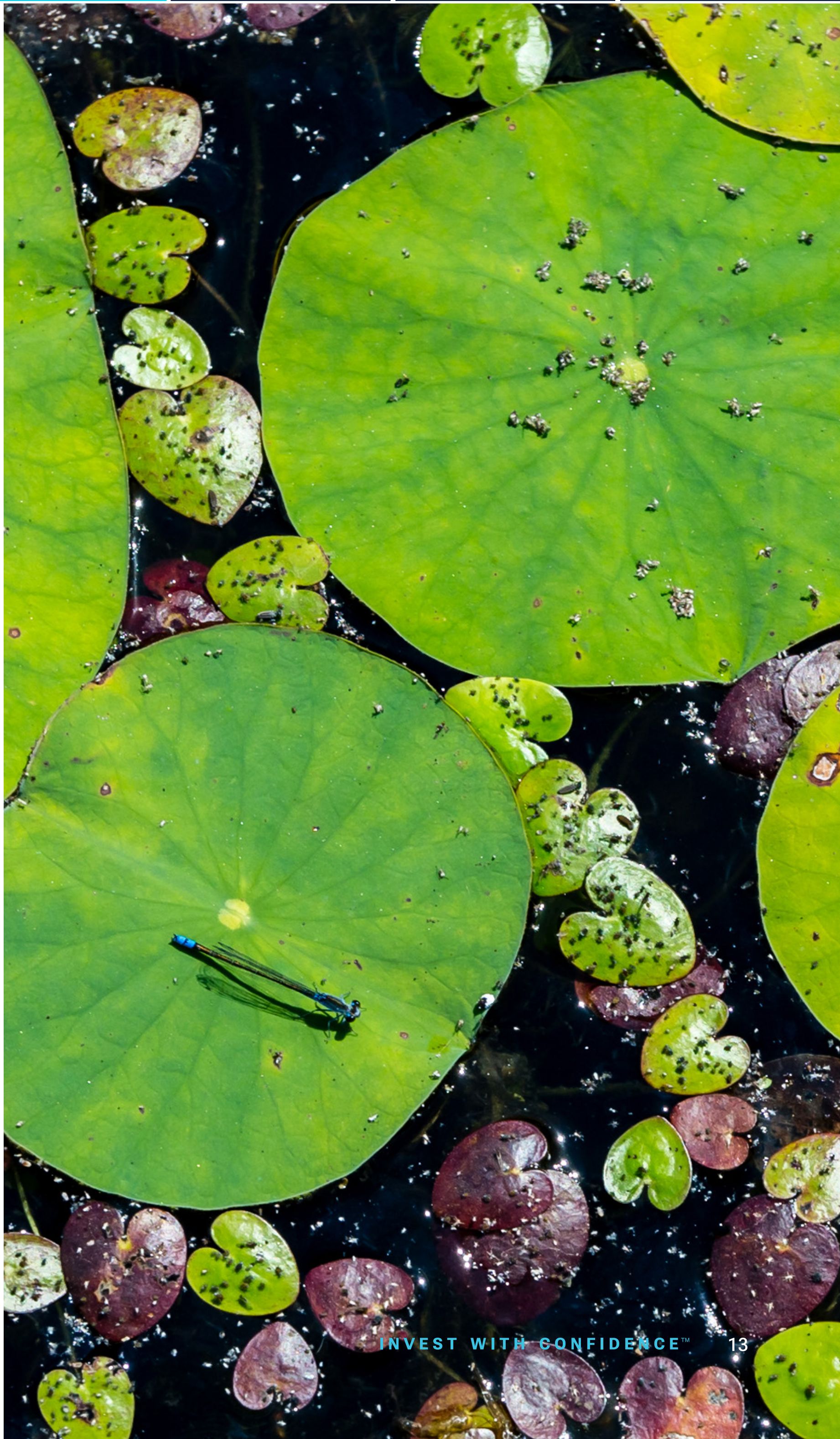
Of the international markets, we continue to favor Japan. Improved corporate governance standards continue to have a tangible—and considerable—impact on company performance. Shareholders are now a much higher priority in Japan than they were in the past. While the BoJ recently ended its negative interest rate policy, it is not expected to embark on a hiking cycle that brings Japanese rates in line with those of other developed markets. This should keep the yen relatively weak and Japanese exports competitive. Valuations are reasonably attractive, too—although the Nikkei 225 has climbed to within reach of its record high, Japanese stocks continue to trade at a low price-to-book value. However, investors outside of Japan will need to consider how yen weakness relative to other currencies will impact the value of their returns.

South Korea and Vietnam the pick of emerging economies

South Korea has sought to emulate Japan's success in boosting stock valuations with a corporate governance drive. Tax incentives have been offered to businesses that prioritize shareholder returns, while the new "Korea Value-up Index" will list firms that have improved capital efficiency. Vietnamese stocks also appear cheap despite a cyclical recovery, an expanding consumer economy, and a looming upgrade to emerging market status. With corporations seeking to diversify their supply chains beyond China, Vietnam appears well placed to attract manufacturing capacity.

Key takeaway

Of the international equity markets, we continue to favor Japan, South Korea, and Vietnam.



Investors moving out of cash may favor equities and short duration bonds

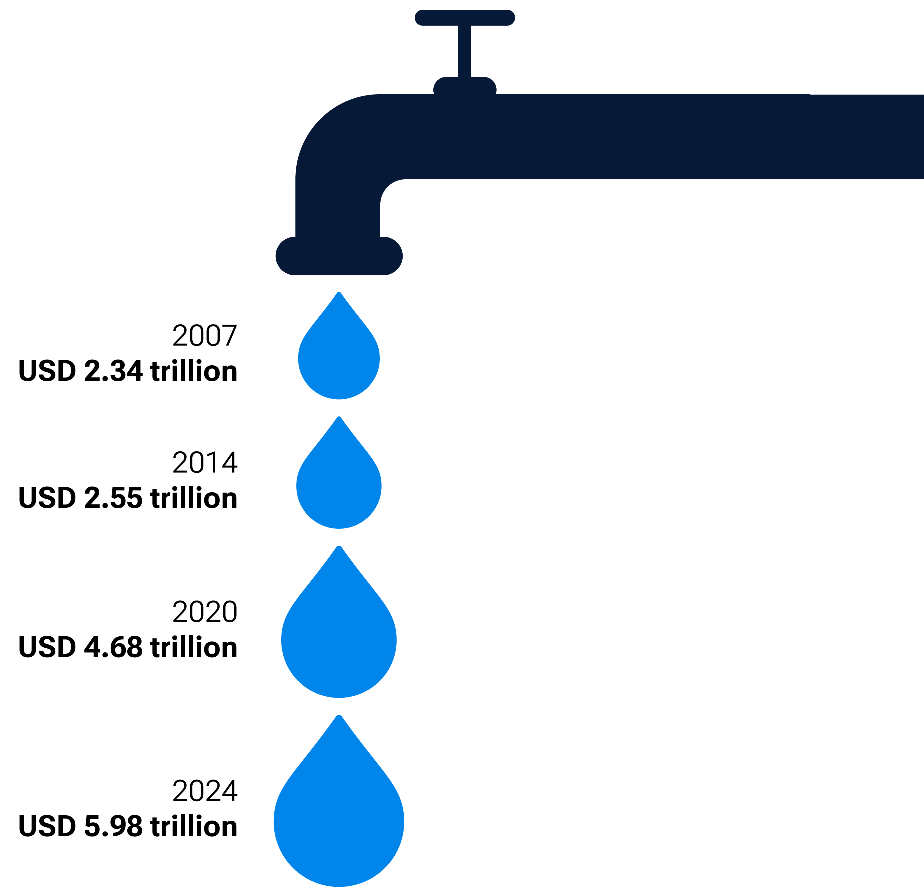
A vast amount of money is hanging over U.S. financial markets in money market funds and other short-term liquid instruments. Evidence from past economic cycles suggests that this strong liquidity preference will ease at some point, especially if the U.S. avoids a deep recession.

As concerns over a hard landing for the U.S. economy have receded, focus has shifted from recession risk to inflation risk. This will impact where investors seek to allocate their money. Historically, bonds—particularly longer-dated bonds—have been an excellent hedge against recession but a poor hedge against inflation. During rare periods when inflation has turned negative due to sharp economic downturns, bonds have outperformed stocks.

"Evidence from past economic cycles suggests that this strong liquidity preference will ease at some point, especially if the U.S. avoids a deep recession."

Tim Murray, CFA
Capital Markets Strategist,
Multi-Asset Division

U.S. investors are flush with liquidity
(Fig. 7) Money market fund assets are highly elevated



As of April 1, 2024.
Source: Investment Company Institute.

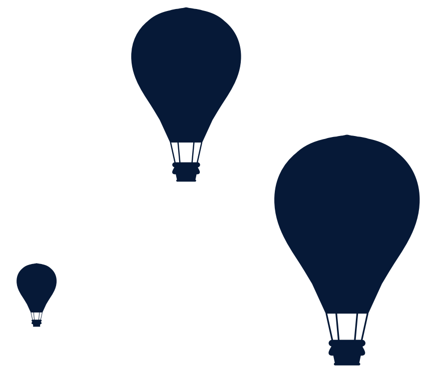
Energy stocks may offer best hedge against inflation

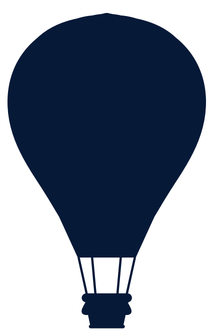
Stocks have tended to perform best during periods of low, moderate, or even slightly elevated inflation. But they have typically dipped sharply during recessions and have also weakened when inflation has moved to very high levels. However, energy sector stocks have historically performed quite well during periods of very high inflation. These patterns suggest that one way to hedge against inflation risk would be to tilt portfolios to stocks, with an emphasis on the energy sector and other commodity-oriented equities.

Investors are also likely to turn to shorter-term bonds given attractive yield levels available and the potential for price appreciation if yields move lower. Short-term bonds are highly valued during uncertain periods—such as the present—as they are less exposed to interest rate changes than longer-dated bonds. They also provide the potential for higher returns than cash while being almost as flexible. This flexibility may be useful given uncertain economic and market conditions.

Key takeaway

Commodity-oriented equities may offer an effective hedge against inflation risk.





Shifting market conditions will favor active management

The investment environment is changing. The post-GFC era of low rates and abundant liquidity is being replaced by one of higher rates, greater divergence of returns, and more volatile markets. We believe this period of transition will continue in the second half of 2024 and underpin conditions for active managers to outperform.

Challenging market conditions will require investors to be more valuation-sensitive than in recent times, when a rising tide lifted all boats. Traditional skills, such as identifying stock drivers and idiosyncratic risk, will continue to be essential, but investors will need to take into account wider macroeconomic, social, and geopolitical factors along with company fundamentals.

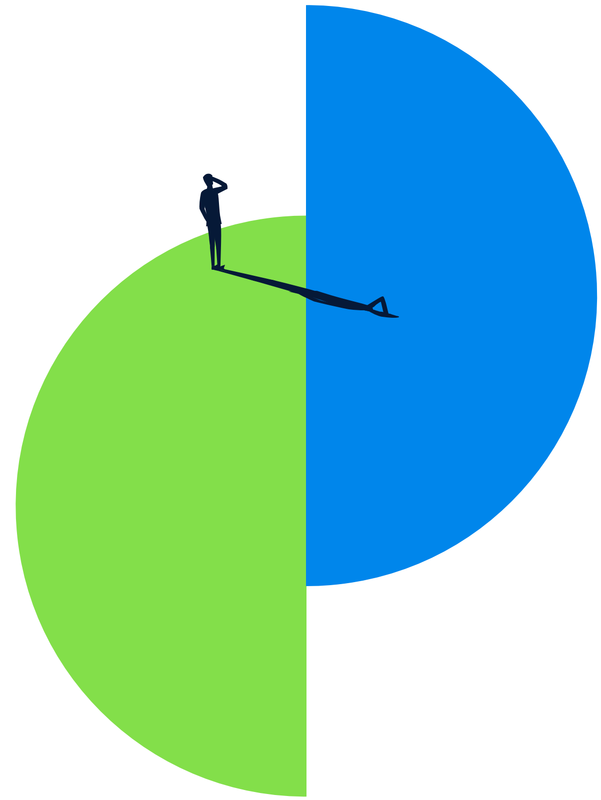
Active managers have performed well following periods of index concentration

Active managers tend to go beyond benchmarks and into factors that can be cyclical, such as small-cap and value stocks—both of which we believe may perform well in the period ahead. Top performing active managers have also historically performed well following periods of heavy index concentration—and markets recently have been concentrated to an unprecedented degree.[2] Although it is difficult to predict when the current period of index concentration will recede meaningfully, there are already signs that the dominance of the Magnificent Seven is beginning to fade.

The end of the period of very low rates will also, we believe, lead to greater dispersion and heightened volatility in bond markets. Active investing can help with duration management, as well as managing country selection, curve positioning, and security selection.

These developments do not mean we expect passive investing to undergo a major retreat. However, we believe that active management will be the better option for the period ahead, as it can offer better outcomes during periods of greater volatility and dispersion.

[2] Based on eVestment U.S. large-cap manager performance and S&P 500 Index concentration analyzed from September 30, 1989 to December 31, 2023. **Past performance is not a reliable indicator of future performance.** As of April 30, 2024, the S&P 500 Index and Russell 1000 Growth Index both registered their highest levels of concentration in 20 years, as measured by the combined weighting of the 10 largest stocks in each index.



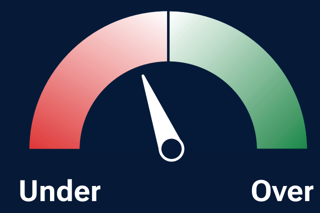
Key takeaway

We believe the likelihood of continued asset price dispersion and heightened volatility will suit active management strategies.

2024 tactical allocation views

As of May 31, 2024.

Weighting Guide



T. Rowe Price multi-asset positioning—asset class

Equities

Earnings continue to strengthen, but face elevated expectations. Potential for broader market participation as economic growth improves, commodity prices increase, and consumer spending remains resilient.

Bonds

Yields remain attractive but volatility could persist due to global divergence in growth, inflation, and central bank expectations. Credit fundamentals remain supportive; however, spreads remain tight.

Cash

Continues to offer attractive yields as the yield curve remains inverted, and continues to offer liquidity should market opportunities arise.

This material is not intended to be investment advice or a recommendation to take any particular investment action.

T. Rowe Price multi-asset positioning—equities

U.S.

Earnings expectations improving. Economic activity resilient. Valuations may limit upside.

Global ex-U.S.

Valuations attractive on a relative basis. European equity outlook improving. Chinese growth appears to have stabilized.

Europe

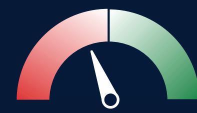
Inflation had been steadily declining but is showing signs of bottoming. Economic growth remains weak.

Japan

Economy welcomes inflation after decades fighting deflation. Corporate governance continues to gradually improve.

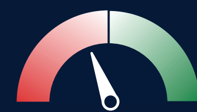
Emerging Markets

Valuations attractive. Monetary policy easing could provide support. Chinese equities finding some footing, but structurally challenged.



U.S. Growth vs. Value[1]

Improving economic outlook and broadening of equity market performance could be supportive for value.

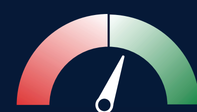


Global ex-U.S. Growth vs. Value[1]

Value stocks cheap and could benefit if recession concerns fade. Growth stocks challenged by consumer weakness in China and Europe.

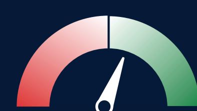
U.S. Small- vs. Large-Cap[1]

Small-caps offer attractive relative valuations but are challenged by higher-for-longer interest rates.



Global ex-U.S. Small- vs. Large-Cap[1]

Small-caps offer very reasonable valuations against a muted global growth profile. Could benefit from improvement in economic growth.



Real Assets Equities

Commodity-related equities are cheap and offer an attractive hedge to stickier inflation.

[1] For pairwise decisions in style & market capitalization, positioning pointed represents positioning in the first mentioned asset class relative to the second asset class.

This material is not intended to be investment advice or a recommendation to take any particular investment action.

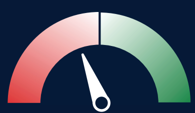
T. Rowe Price multi-asset positioning—bonds

U.S. Investment Grade (IG)

Yields broadly attractive. Credit fundamentals and technical backdrop supportive. But yields have upside risk and credit spreads[1] are tight.

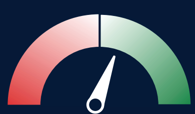
Developed ex-U.S.IG (Hedged)

Global central banks cautiously eyeing rate cuts. Yields look attractive on a USD-hedged basis.



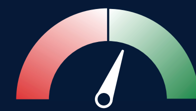
U.S. Treasury Long

Longer term yields biased higher due to increased supply, resilient growth, and stickier inflation.



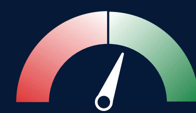
Inflation Linked

Sector offers a hedge should inflation settle at, or move higher, than current levels.



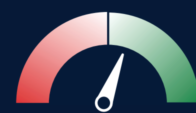
Global High Yield

Attractive absolute yield levels supportive, but tight spreads may reflect a too optimistic backdrop.



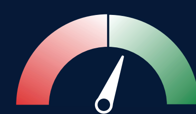
Floating Rate Loans

Yields could remain elevated on less aggressive Fed cut expectations. Spreads attractive, although default rates expected to rise.



EM Dollar Sovereigns

Yields modestly attractive. Central banks easing cycles and moderating inflation may benefit EM bonds.



EM Local Currency

Central bank easing and lower inflation could be tailwinds, but a higher-for-longer Fed could sustain dollar strength.

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[1] Credit spreads measure the additional yield that investors demand for holding a bond with credit risk over a similar-maturity, high-quality government security.

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