IHAG PRIVATBANK

Monthly CIO Letter

24 February 2023

As hopes of a possible soft landing for the economy gain traction, sentiment on the investment markets is becoming more positive and relaxed. The macroeconomic situation and the current state of the market appear to be much better synchronised at present. We are maintaining our neutral stance on equities; bonds remain underweighted.

Christoph Boner
Chief Investment Officer

Highlights

– As inflationary pressures ease and second-round effects remain absent, the investment community hopes to have seen the back of aggressive monetary policies.

– For the first time for more than a year, the growth outlook has been revised upwards.

– The macroeconomic situation and current market levels are much more in synch with each other; a decisive positioning – in either one direction or the other – is not advisable at present.

Asset Allocation

Asset Classes	Change	– –	–	=	+	+ +
Liquidity	➡			●		
Bonds	➡		●			
Reference Currency	➡	●				
World	➡	●				
Emerging Markets	➡					●
Convertible Bonds	➡				●	
Equities	➡			●		
Switzerland	➡			●		
Europe	➡			●		
US	➡			●		
Pacific	➡			●		
Emerging Markets	➡			●		
Alternative Assets						
Gold	➡				●	
Crypto Assets	➡				●	
Currencies						
CHF	➡			●		
EUR	➡			●		
USD	➡			●		

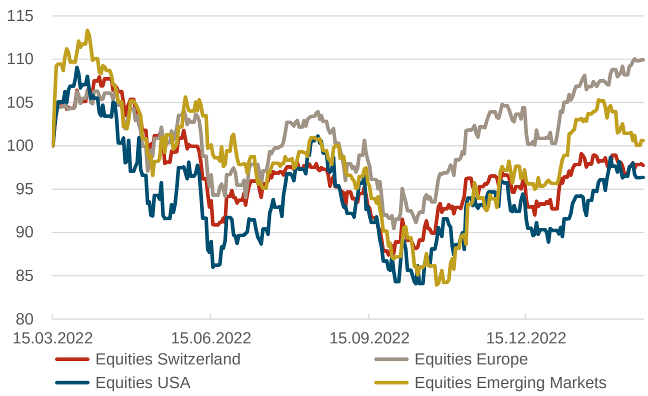
Change: compared to previous month, **Positioning**: -- strongly underweighted | - underweighted | = neutral | + overweighted | ++ strongly overweighted

Asset Allocation

This week marks the first anniversary of the escalation of hostilities in the Russia-Ukraine conflict. Following supply problems due to the various Covid measures of recent years and a sudden sharp surge in demand after the economy reopened, the outbreak of war sparked an abrupt spike in inflationary pressures via rising energy and food prices. This forced central banks to implement immediate and aggressive interest rate hikes in a bid to counter these very price rises. Since then, interest rates have been hiked with unprecedented speed and ferocity. The resulting deterioration in the economic outlook – coupled with heightened risk aversion – sent both bonds and share prices tumbling.

Almost a year after the Fed's first rate move, some equity markets are already trading above their levels back then, while the interest markets continue to trade deep within red territory.

Equities: performance since the Fed's first rate move (15 March 2022)



The background to the easing of market tensions in evidence since October is the hope that the economy will have a softer landing after all – despite unprecedentedly aggressive intervention on the part of the various central banks.

A more positive view on inflation, based mainly on lower energy prices and the absence of second-round effects, even led to a revision of the global economic growth figures in January. For the first time for more than a year, this year's global GDP growth expectations were revised upwards to 2.9%.

This more balanced picture – higher share prices accompanied by a simultaneous improvement in the outlook for growth – is leading us to maintain our neutral positioning for the moment. The equity allocation for a balanced mandate is 50%; while we do not currently have a strong regional preference, we are continuing to overweight our quota of Chinese equities at the expense of other emerging markets.

We are also leaving the allocation to interest-bearing securities underweighted for the time being. Having increased the quota at the shorter end in January to avoid opportunity costs, we are biding our time before going for any further increase as interest rates at the longer end are currently too low. The bond allocation for a balanced mandate stands at 38% and we are also deliberately continuing to add emerging market bonds denominated in hard currency (USD).

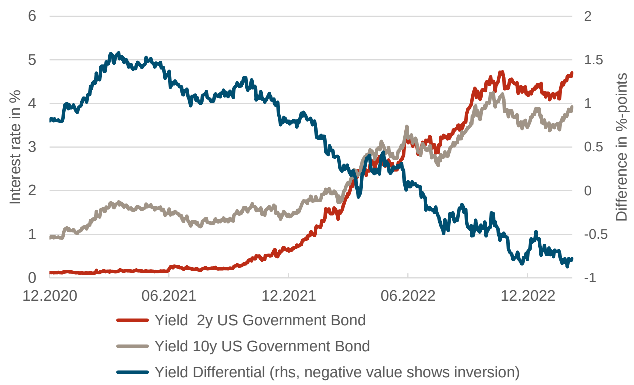
We believe the use of diversifying asset classes should also be an additional element in the asset allocation process, and are therefore continuing to hold gold in particular in the portfolios. We have also included some crypto investments, which started the current year with extremely strong price trends after a poor 2022.

Bonds

With inflation figures receding and no second-round effects in evidence for the time being, the situation on the interest markets has eased considerably for now. Hopes of less aggressive central bank action have boosted bond prices. For example, the yield on 10-year Swiss Confs fell well below 1% in January. At the same time, some risk premiums retreated significantly, giving something of a boost to bonds. Various interest markets have made gains since the beginning of the year, with some advancing by more than 2%. However, after the latest US labour market figures, interest rates rose again across the board.

Investors are concerned about the current strongly inverted yield curves. For example, the interest rate on ten-year US Treasuries is 0.80 percentage points lower than that on 2-year Treasuries. Such an inversion is generally seen as an indicator of a coming recession.

Bonds: Inversion of the US yield curve



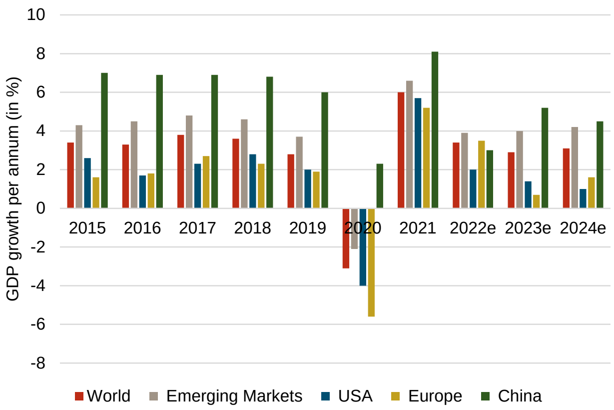
We assume that this risk is significantly overestimated and that for once the bond market reflects too negative a view. The marked inversion is probably also due in no small part to a persistent and pronounced distortion of the yield curves at the long end due to continuing central bank interventions. Considering the ongoing but extremely slow contraction of central-bank balance sheets, the risk of rising interest rates on the longer side of the yield curves becomes evident. Cautious positioning therefore remains essential.

Equities

Some stock markets are currently trading at the same levels as this time last year – against a backdrop of significantly higher interest rates and expectations of slower growth. The key reason for this (currently) positive bottom line lies in the earnings trend. Despite increases in the cost of energy, other input products and labour, companies are largely succeeding in maintaining their margins – and hence also their earnings – thanks to higher sales prices.

Thus, the discrepancy between the macroeconomic assessments of market strategists and the microeconomic assessments of analysts – mentioned on a number of occasions in the CIO Letter – is starting to be resolved. Indeed, this process recently culminated in a (positive) revision of the growth outlook. For example, the global economy is currently expected to grow by 2.9% in 2023 – compared to predictions of a growth rate of 2.7% in autumn 2022.

Economy: GDP growth forecasts as of January 2023 (Source: IMF)



Given this more balanced situation and the ultimately more coherent picture, a neutral equity positioning is the logical consequence.

On the negative side, there is currently a marked easing of tensions in some areas of the markets and this is reflected in various risk indicators. There is also a certain negative asymmetry regarding future developments: this is due to the risk of a further slowdown in growth triggered by the (delayed) effects of interest rate hikes, the end of catch-up effects following the lifting of Covid measures – particularly in China – and the cost savings that companies may yet ultimately need to make. At present, though, these factors do not justify a fundamentally more cautious positioning in equities.

Alternative Assets

Alternative investments serve to provide additional diversification in a portfolio context and in doing so help improve the risk/return ratio. Due to risk considerations we are continuing to hold investments in both gold and cryptocurrencies. While the gold price remains subject to the conflicting forces of higher interest rates and portfolio diversification benefits, we expect crypto assets to continue their recovery over the next few months.

Currencies

The USD should continue to trend towards relative weakness as it is at a more advanced stage in the interest rate cycle. We expect the EUR/CHF exchange rate to continue moving sideways.

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Annex

Economy and Markets

GDP (E: Consensus)

	2022	2023E
USA	2.1%	0.6%
EU	5.4%	0.4%
Switzerland	4.3%	0.6%

Inflation (E: Consensus)

	2022	2023E
USA	8.0%	3.8%
EU	8.4%	8.4%
Switzerland	2.9%	2.1%

Central Bank Rates (higher)

	21.02.2023	Consensus
USA FED	4.8%	5.25%
EUR ECB	2.5%	3.50%
CHF SNB	1.0%	

Government Bonds (10 Years)

	21.02.2023	Outlook
USA	4.0%	3.75% – 4.10%
Germany	2.5%	2.35% – 2.60%
Switzerland	1.5%	1.30% – 1.60%

Foreign Exchanges

	21.02.2023	Outlook
EUR/CHF	0.988	0.95 – 1.00
USD/CHF	0.928	0.90 – 0.94
EUR/USD	1.065	1.06 – 1.09

Raw Materials and Alternatives

	21.02.2023	Outlook
Gold (USD/Ounce)	1'835	1'800 – 1'900
Oil (USD/Brent)	83.1	78 – 92
Bitcoin USD	24'200	22'000 – 25'000

Equity Markets

	P/E ø 5J.	P/E 2024	Div. Yield	Outlook
World	18.7x	15.4x	2.2%	sideways
USA	20.2x	16.5x	1.7%	sideways
Europe	16.0x	13.2x	3.2%	sideways
Switzerland	19.4x	16.6x	2.8%	sideways
Emerging Markets	12.6x	11.8x	3.1%	sideways

Markets in Local Currencies

Equity Markets

	QTD	YTD
World	5.5%	5.5%
USA	4.4%	4.4%
Europe	9.3%	9.3%
Switzerland	5.6%	5.6%
Emerging Markets	4.1%	4.1%

Government Bond Yield (10 Years)

	21.02.2023	30.12.2022
USA	3.95%	3.87%
Germany	2.53%	-0.18%
Switzerland	1.49%	1.62%

Raw Materials and Alternatives

	QTD	YTD
Gold (USD/Ounce)	0.6%	0.6%
Oil (USD/Brent)	-4.4%	-4.4%
Bitcoin USD	46.0%	46.0%

Foreign Exchanges

	QTD	YTD
EUR/CHF	-0.2%	-0.2%
USD/CHF	0.4%	0.4%
EUR/USD	-0.5%	-0.5%

Data as of 21 February 2023, QTD: Performance since Beginning of Quarter, YTD: Performance since Beginning of Year