Monthly CIO Letter

16 September 2024

With the latest US labour market data, concerns about economic growth have increased. Hopes of further interest rate cuts in the near future are keeping the markets at current valuation levels for the time being; the asymmetry between opportunities and risks has not improved as a result. We are leaving the equity allocation underweighted and maintaining the broad diversification of the portfolios.

Christoph Boner
Chief Investment Officer

Highlights

- A weakening US labour market has rekindled concerns about economic growth.
- Current valuation levels, on the other hand, call for sufficient growth – or sufficient interest rate cuts.
- Whether interest rate cuts or growth: risks are to be found on both sides.

Asset Allocation

Asset Classes	Change	- -	-	=	+	+ +
Liquidity	➡					●
Bonds	➡		●			
Reference Currency	➡		●			
World / Topics	➡		●			
Emerging Markets	➡			●		
Convertible Bonds	➡				●	
High Yield	➡		●			
Equities	➡		●			
Switzerland	➡			●		
Europe	➡			●		
USA	➡			●		
Pacific	➡			●		
Emerging Markets	➡			●		
Themes	➡	●				
Alternative Assets						
Gold	➡			●		
Crypto	➡				●	
Other	➡	●				
Currencies						
CHF	➡		●			
EUR	➡				●	
USD	➡				●	

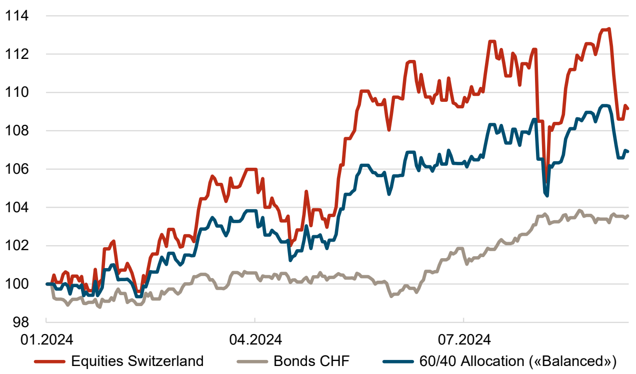
Change: compared to previous month, **positioning:** - - strongly underweighted | - underweighted | = neutral | + overweighted | + + strongly overweighted

Asset allocation

Following the first major setbacks on the stock markets in August, the first half of September also saw increased volatility on the stock markets. On the one hand, ambitious valuation levels such as the current one are more susceptible to setbacks; above all, however, growth concerns have increased significantly in recent weeks.

In response, the bond markets are showing clear gains: expectations of more and faster interest rate cuts are leading to significantly lower yields, which is causing prices on fixed-interest investments to rise accordingly.

Market Development 2024: Equities and Bonds



As if the indicators of a slowdown in growth – above all developments on the labour markets but also a deterioration in the outlook for the manufacturing sector – were not enough to worry the investment community, the US yield curve has normalised for the first time in two and a half years: Longer maturities are once again yielding more interest income than their shorter-dated counterparts. The timing of this normalisation is often interpreted as a harbinger of an impending slowdown in growth or even a recession.

Against this backdrop, we are leaving the equity allocation for the time being at an underweight of currently 42% for a "balanced" profile. The risk of growth being too low for current valuation levels, as outlined in the last CIO Letter, remains. The sensitivity of the equity markets to (supposed) signs of such a slowdown in growth makes a cautious positioning appear appropriate.

The expectations of further interest rate cuts associated with growth concerns have given the bond markets a significant tailwind in recent weeks. In view of the current high expectations of central banks and the potential for disappointment, we are leaving the bond allocation at 40% for a balanced profile. The above-market credit quality of the portfolios remains unchanged, as does the short duration.

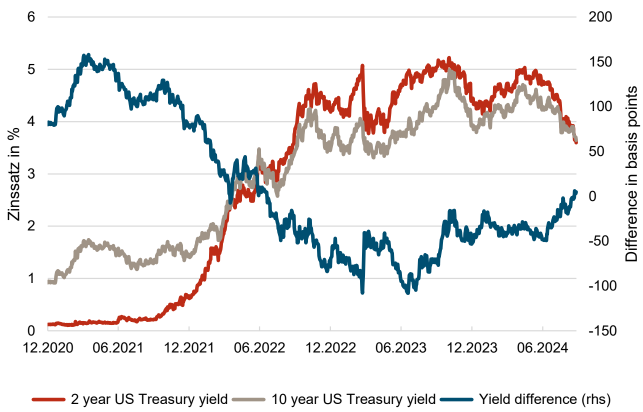
We are continuing our diversifying investments in gold and cryptocurrencies. For additional diversification, particularly with regard to existing geopolitical risks, we also remain invested in Brent oil via a structure.

Bonds

With the emergence of growth concerns, hopes of interest rate cuts have increased. Between four and five interest rate cuts are now expected for the US in the final months of this year alone and between two and three moves for the eurozone. In fact, a slowdown in growth would open up scope for interest rate cuts, as inflationary pressure naturally eases in such an environment.

Another phenomenon has also kept market participants busy these days: for the first time in more than two years – specifically since 1 April 2022 – the US yield curve has normalised again. This means that, for the first time, interest rates on ten-year government bonds are once again above the yield on their two-year counterparts, bringing a prolonged phase of inversion to a (temporary) end. This is the first time in the last fifty years that the curve has been inverted for so long.

Yield Curve: US Treasury Yield 10 versus 2 Years



A normalisation of the yield curve is generally seen as a harbinger of a slowdown in growth: The short end of the curve, which is largely controlled by the central banks, is falling faster in anticipation of interest rate cuts than the longer end, which is probably also falling – but to a lesser extent – due to declining inflationary pressure and a slowdown in growth. A normalisation of the curve with subsequent steepening is the direct consequence.

While a normalised yield curve makes taking duration risks more attractive again, the current slightly exaggerated expectations of interest rate cuts mean that we are not increasing our exposure to fixed-interest bonds. The bond allocation remains cautious. We are leaving the duration in the EUR bond market at 4.4 years, while the duration in CHF and USD is around 3 years. Credit risks also remain underweighted.

Equities

Even with the recent setbacks, the equity markets remain slightly overvalued. As explained in the last CIO Letter, this can easily be supported by sufficient growth and interest rate cuts in the near future and does not necessarily have to lead to further setbacks.

However, the fact is that the potential for setbacks remains elevated, as disappointments with regard to growth in particular may occur. The latest labour market data, with fewer newly created jobs and a slight rise in the unemployment rate, could be an indicator of an imminent slowdown in growth.

It is also apparent that production gains from applications in the field of artificial intelligence (AI) are unlikely to materialise in the short term and will be lower than expected in many places.

It should be noted that the fundamental picture also remains solid at company level and that growth concerns are not yet manifesting themselves across the board.

World Equities: Earnings and Price Performance

Despite this fundamentally appealing picture, we are leaving the equity allocation slightly underweighted. The fall in equities remains high due to the growth and interest rate expectations mentioned above – in addition, geopolitical risks are currently being largely ignored.

Alternative Assets

The diversification of the portfolios will remain ensured through the addition of gold, crypto assets and oil. The diversification contribution of gold and oil is well known; in the case of crypto investments, we are relying on a structural demand overhang thanks to increasing institutionalisation, which should continue to drive prices in the future.

Currencies

Despite continued significant interest rate differentials, we are maintaining our extensive hedging of the USD. The reference currency share for a balanced profile remains at around 75%; the USD share is around 6% and the EUR share below 4%.

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Appendix

Economic and Market Development

GDP (E: Consensus)

	2023	2024E
USA	2.5%	2.5%
EU	0.5%	1.0%
Switzerland	0.8%	1.3%

Inflation (E: Consensus)

	2023	2024E
USA	4.1%	2.9%
EU	5.4%	2.4%
Switzerland	2.1%	1.3%

Central Bank Rates (higher)

	10.09.2024	Consensus
USA FED	5.5%	5.25%
EUR ECB	3.8%	3.50%
CHF SNB	1.3%	

Government Bonds (10 Year)

	10.09.2024	Outlook
USA	3.64%	3.55% – 4.00%
Germany	2.13%	2.05% – 2.35%
Switzerland	0.46%	0.30 – 0.50%

Foreign Exchanges

	10.09.2024	Outlook
EUR/CHF	0.933	0.92 – 0.96
USD/CHF	0.847	0.83 – 0.86
EUR/USD	1.102	1.09 – 1.12

Raw Materials and Alternatives

	10.09.2024	Outlook
Gold (USD/Ounce)	2'517	2'350 – 2'650
Oil (USD/Brent)	69.2	68 – 78
Bitcoin USD	57'575	52'000 – 65'000

Equity Markets

	P/E ø 5J.	P/E 2024	Div. Yield	Outlook
World	19.4x	17.6x	1.8%	slightly down
USA	21.4x	19.8x	1.3%	slightly down
Europe	15.8x	13.1x	3.3%	slightly down
Switzerland	19.9x	17.5x	3.0%	slightly down
Emerging Markets	13.8x	11.0x	2.7%	slightly down

Markets in Local Currencies

Equity Markets

	QTD	YTD
World	4.3%	13.7%
USA	5.2%	16.3%
Europe	1.2%	9.2%
Switzerland	3.0%	9.2%
Emerging Markets	3.6%	6.2%

Government Bond Yield (10 Year)

	10.09.2024	29.12.2023
USA	3.64%	3.88%
Germany	2.13%	-0.18%
Switzerland	0.46%	0.70%

Raw Materials and Alternatives

	QTD	YTD
Gold (USD/Ounce)	12.9%	22.0%
Oil (USD/Brent)	-15.4%	1.0%
Bitcoin USD	-18.7%	37.3%

Foreign Exchanges

	QTD	YTD
EUR/CHF	-4.1%	0.5%
USD/CHF	-6.0%	0.7%
EUR/USD	2.1%	-0.2%

Data as of 10 September 2024, QTD: Performance since Beginning of Quarter, YTD: Performance since Beginning of Year