Market review

The year has started well – at least as far as investors are concerned – though the very positive sentiment seen in January has since cooled somewhat. The economic significance of the ongoing war in Ukraine is declining after a mild winter averted the expected energy crisis in Europe. COVID-19 is similarly no longer a fear factor driving markets following the end of China's zero-COVID policy. These positive developments, together with continued high employment, are making consumers feel confident about the future.

On the downside, however, inflation remains high and persistent in virtually all the major economic regions. High core inflation is forcing central banks to raise interest rates further, even though cyclical weakness in the economies is becoming ever more evident. The bankruptcy of a major US regional bank can be seen as an indirect consequence of this development, as can, in a broader sense, the historic watershed in the Swiss banking universe with UBS's takeover of Credit Suisse. The tightening cycle is well advanced after the most recent interest rate hikes, but rate cuts are unlikely before 2024.

Geopolitical risks are increasingly taking centre stage. As previously discussed, the formation of blocs – with Western democracies (USA, Europe, etc.) on one side and authoritarian regimes (China, Russia, etc.) on the other – must be particularly closely monitored against the backdrop of the Taiwan conflict. Although optimism is more subdued given the size of the challenges, there are grounds for confidence in the future.

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Market data
per 31.03.2023

Equity Markets		**since 31.12.2022**
SMI CHF	11'106.24	3.51 %
S&P 500 USD	4'109.31	7.03 %
EURO STOXX 50 EUR	4'315.05	13.74 %
FTSE 100 GBP	7'631.74	2.42 %
MSCI Emerging Markets USD	505.29	3.96 %
NIKKEI 225 JPY	28'041.48	7.46 %
MSCI All Country World Local	334.16	7.03 %

Bond Markets		**since 31.12.2022**
Eidgenossen (10y)	1.20 %	-37.2 Bps
US-Treasury (10y)	3.47 %	-40.7 Bps
Bund (10y)	2.29 %	-27.9 Bps
SBI AAA-BBB 3-5 TR	120.37	0.2 %

3 Month Key Rates		**since 31.12.2022**
CHF (SARON)	1.42 %	47.6 Bps
USD (SOFR)	5.19 %	42.5 Bps
EUR (ESTR)	3.04 %	90.6 Bps

Exchange Rates		**since 31.12.2022**
EUR/CHF	0.992	0.26 %
USD/CHF	0.915	-1.00 %
EUR/USD	1.084	1.25 %

Alternative Investments		**since 31.12.2022**
Real Estate (UNGL)	2'035.03	-0.04 %
Gold (USD/Ounce)	1'969.28	7.96 %
US-Crude Oil (USD/Barrel)	75.67	-5.72 %
Hedge Funds (HFRXGL)	1'367.78	0.04 %
Bitcoin (XBT)	28'395.30	71.68 %

Macroeconomic environment

Expectations of global economic growth at 3.4% for 2022 and 2.9% for 2023 have been revised slightly upwards in recent months (+2.7% 2023E at end-2022). In other words, the growth of the global economy is not slowing as drastically as was feared only a few months ago. With expected growth of +0.5% in both the USA and the eurozone, no, or only a very mild, recession is still factored in for the most important economic regions.

The exports business is benefiting from better functioning supply chains, lower commodity costs and the opening of the Chinese economy. US consumers are continuing to spend and are still drawing on excess savings accumulated during the pandemic years. Together with very high employment, they feel confident about the future despite higher costs.

While a declining inflation trend is emerging in the USA and Europe, core inflation (i.e. excluding energy and food) remains elevated. Experts see the profit-price spiral – where companies use the higher price level to get price increases through so as to maintain or even widen their margins – as being behind the stubbornly high inflation.

Fighting inflation remains a top priority for central banks, even at the cost of negative economic growth or problems in the banking sector. If banks become more cautious and hence more restrictive in their lending in the next few months, such a credit crunch could make it even more difficult for companies to access liquidity – and to a greater extent than anticipated by central banks. The latter will need to act with appropriate caution over the months to come.

Traditional Investments

Currencies

Turbulence in the financial markets is reinforcing the status of the US dollar and the Swiss franc as safe havens. The high interest rate differential of the Swiss franc to the US dollar and to the euro is resulting in high hedging costs for Swiss franc based investors. When the end of the rate tightening cycle is in sight – and the Fed is ahead of other central banks here – the US dollar can be expected to weaken.

Bonds

Despite concerns about the financial stability of the banking sector, leading central banks have raised their key interest rates further: US Fed from 4.75% to 5%, ECB from 3% to 3.5% and SNB from 1% to1.5%. By doing so, the currency guardians are signaling that inflation is still too high and fighting it remains a top priority.

After the collapse of several small US regional banks and the trouble with Credit Suisse, yields on government bonds initially fell sharply on the flight to safety. The situation has, however, largely eased following the emergency, government-enforced takeover of Credit Suisse by UBS. The picture has been similar for credit risk premia: In the first few weeks of the year hedging premiums for corporate bonds trended down, indicating investors' higher risk appetite; then, in the first weeks of March, they rose sharply. This is a sign of stress in the credit system. Here too, though, the situation has largely normalized.

Despite their much higher nominal yields, we remain negative on bonds. Real yields after inflation are still very much in negative territory. Given inverted yield curves, liquidity can be managed using short-term fiduciary investments.

Equities

Global equity markets were shook in March by turbulence in the banking sector. Bank failures in the USA gave rise to concern about financial market stability, which spread to Europe. The financial system proved to be resilient though, such that the World Equity Index ended the first quarter in positive territory (+7%).

European equities were up almost 14% in the first quarter, having benefited from the fact that investors' worst fears over Ukraine (especially an energy shortage, see "Know-how" from April 2023) did not materialize. The defensive qualities of Swiss blue-chips played less of a role. Swiss equities underperformed at +5.1% (including dividends) by international comparison. The laggard in the SMI was, of course, Credit Suisse with a negative performance of 70.2%!

We assume in our baseline scenario that equity markets will remain volatile and that price potential will be limited due to inflation and interest rate fears and weak growth expectations. How equity markets develop going forward largely depends on what course inflation and monetary policy takes. Should inflation fall faster than expected, the environment for risk assets could similarly improve faster than expected. That said, a hard landing (i.e. a severe recession) or even stagflation (i.e. stagnant economic growth with rising inflation) are within the realm of the possible. We are therefore neutral on equities in a portfolio context.

Alternative Investments

Commodities: The price of gold is benefiting from the dislocations in the (US) banking sector, confirming its value as a diversifier in uncertain times. Recent US dollar strength has weighed on base metal prices, but an improvement in industrial activity should strengthen demand over the coming weeks.

Hedge Funds: The performance of hedge funds varied widely in the first quarter. Trend-following hedge funds (so-called CTAs) were particularly adversely impacted by the generally higher volatility levels.

Real Estate: Real estate fund valuations are much more attractive again in terms of premiums. Given the development of interest rates, however, uncertainties remain.

Alternative Debt Securities: In an environment of rising interest rates, microfinance investments make stable contributions to performance and have low correlations to traditional asset classes. Additional impact returns.

Other Alternative Investments: The first quarter saw prices in the crypto universe rebound sharply, despite the second-round effects of the FTX collapse such as the insolvency of Genesis, the ceasing of operations at crypto bank Silvergate, etc. Further negative domino effects cannot be ruled out. Bitcoin remains a strategic portfolio building block.

Private Markets

Private Equity: Both the profitability and the growth momentum of the underlying investments could be maintained. More difficult financing conditions meant fewer direct participations could be exited. There are opportunities in the secondary market.

Private Debt: Resilient during the interest rate hiking cycle given the very low interest rate risk. Rising base rates with a positive yield effect.

Private market investments provide additional return potential, particularly in macroeconomically challenging times.

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