Market review

So was that it? Have we finally reached the end of the long-awaited cycle of interest rate hikes? At present, the market is not expecting any further interest rate hikes – neither in the USA, in Europe nor in Switzerland. Looking at the final stages of past tightening cycles in the US market, equity returns are found to be largely positive within twelve months of the last rate hike. Where this was not the case, the reason for it was that the USA had slipped into recession. Given that a hard landing is currently rather unlikely, there is a good chance, then, that equity valuations will be higher by the end of the year. However, this depends on companies being able, with their outlook for the coming months, to confirm their high earnings estimates of over +9% for 2024.

The reopening of the window for IPOs and spin-offs in September, after a two-year hiatus, is another indication that the environment for risky assets is improving. It shows that investors are receptive to companies with high earnings growth, although astronomical valuations such as the US IPO of Klaviyo (price-to-sales ratio of 14) are rather the exception.

Despite higher interest rates, stress in the credit market has not yet reached a level that could be considered worrying, but even so insolvencies are slowly on the increase. Historically speaking, companies are well capitalized and have little immediate need for refinancing. All the same, it is important to be mindful of the many risks as setbacks can occur at any time.
A broadly based portfolio with tactical cash holdings is certainly not a miss in the current environment.

Author
Jana Schenker

Market data
per 30.09.2023

Equity Markets		**since 31.12.2022**
SMI CHF	10'963.50	2.18 %
S&P 500 USD	4'288.05	11.68 %
EURO STOXX 50 EUR	4'174.66	10.04 %
FTSE 100 GBP	7'608.08	2.10 %
MSCI Emerging Markets USD	494.90	1.82 %
NIKKEI 225 JPY	31'857.62	22.09 %
MSCI All Country World Local	347.16	11.18 %

Bond Markets		**since 31.12.2022**
Eidgenossen (10y)	1.06 %	-51.3 Bps
US-Treasury (10y)	4.57 %	69.6 Bps
Bund (10y)	2.84 %	26.7 Bps
SBI AAA-BBB 3-5 TR	122.66	2.13 %

3 Month Key Rates		**since 31.12.2022**
CHF (SARON)	1.71 %	77.3 Bps
USD (SOFR)	5.31 %	101.0 Bps
EUR (ESTR)	3.88 %	199.0 Bps

Exchange Rates		**since 31.12.2022**
EUR/CHF	0.968	-2.22 %
USD/CHF	0.915	-1.00 %
EUR/USD	1.057	-1.23 %

Alternative Investments		**since 31.12.2022**
Real Estate (UNGL)	1'888.74	-7.23 %
Gold (USD/Ounce)	1'848.63	1.35 %
US Crude Oil (USD/Barrel)	90.79	13.12 %
Hedge Funds (HFRXGL)	1'387.68	1.45 %
Bitcoin (XBT)	27'072.54	63.68 %

Macroeconomic environment

Global economic growth is estimated this year at +2.7%. While Europe and China have recently seen slight downward revisions to GDP, the US economy is proving comparatively robust: the tight labour market is losing some momentum (unemployment rate: +3.8%) and workers' wage growth is slowing. Households' disposable income is increasing as inflation declines. This has seen private consumer spending increase slightly recently. What's more, savings that were built up during the pandemic are still available and supporting the all-important consumption component. Weak growth well below the trend rate of just under 2% (a soft landing) seems realistic and is also reflected in US monetary policy. The US Fed is pushing the first rate cuts further out into the future. This could strengthen the economic recovery from the middle of 2024, since manufacturing should bottom out towards the end of 2023.

In Europe, many companies are holding back from making investments. Manufacturing companies continue to suffer from high cost pressure, staff shortages and destocking. The mood is gloomy and leading indicators suggest economic output in the eurozone could decline in Q4. However, the dip in growth seems to have bottomed out. China is attempting to mitigate its structural problems through the use of stimulus measures. Even if China's economic growth were to remain weak next year, Chinese demand alongside rising US orders could boost European exports from spring 2024.

Inflationary pressure is gradually easing, which is an encouraging sign. Core inflation, however, is likely to remain elevated and pose a challenge for central banks at their next meetings.

Traditional Investments

Currencies
The CHF appreciated by a further 0.9% against the EUR in Q3. Even though the ECB has hiked interest rates one time more than the SNB since the end of June, the economic situation in Switzerland is definitely more solid. We do not expect a strong recovery of the EUR/CHF exchange rate by year's end. By contrast, the USD has strengthened broadly on the back of expectations of US rate cuts being pushed further out into the future. We are sticking to our scenario of a weaker USD over a one-year horizon. Currency hedges for CHF investors remain expensive due to the interest rate differentials, about 3.6% p.a. for USD hedges and 2% p.a. for EUR hedges.

Bonds
Headline inflation in the developed markets has been falling compared to the previous year. The bond market, however, is reacting to uncertainty about the future course of inflation. Yields on 10-year government bonds have increased over the past three months in most countries. The USD and EUR yield curves remain inverted – even in CHF, short-term bonds are yielding more than bonds at the long end of the curve. Corporate credit risk premia are stable, even slightly lower, compared to Q2. It is to be assumed that a large measure of confidence is priced into the market. There has been a further widening of the interest rate spread between US and German bonds, which has been attributed to Fitch Ratings' downgrade of the ratings of the USA and can be interpreted as a vote of no confidence by the market.

The first interest rate cuts are not expected before the summer of 2024. Despite talk of the interest rate tightening cycle coming to an end for the time being, leading central bankers are keeping all their options open. As long as this is the case, we will remain underweight in this asset class.

Equities
Global equity markets had a strong first half, but then fell back in Q3, losing 1.7%. Good news on the corporate reporting season and on economic activity as well as a stabilization of the geopolitical situation were positively received by investors in July. This was followed by profit-taking from August. These price setbacks on the equity markets were primarily driven by hikes in key rates by the Fed and the ECB at the end of July, which sent yields on European and US government bonds surging in the ensuing weeks. Equity valuations fell accordingly. Q3 saw growth stocks in particular lose more ground than value stocks.

Regionally, UK, Italian and Spanish equities were among the better performers in Q3. Chinese equities put in a middling performance, with news from the real estate sector tending to depress investor sentiment and recent economic data helping to uplift it. In the USA, the Nasdaq technology index has suffered most from rate cuts being pushed further out. European equities have performed comparatively weakly. High inflation and a weak order intake (especially in Germany) made European equities even cheaper, which is why investments need to be made very selectively here.

Towards the end of Q3, the mood among investors was less euphoric. However, the response to recent IPOs suggests that good companies will continue to command high valuations – as the examples of ARM Holdings, a British chip designer, and Klaviyo, a US marketing automation specialist, show. And hence the spinning-off of the generics division Sandoz from its parent company Novartis is eagerly anticipated at the beginning of October.

Alternative Investments

Commodities: The prospect of a soft landing in the USA together with USD strength have kept the gold price in check as a result of higher nominal (and real) yields. We expect the gold price to continue to be supported by demand from central banks. The price of Brent crude, by contrast, has risen by more than USD 20 since the end of June to over USD 94 a barrel. This reflects the fact that, on the one hand, the global economic situation has improved and the demand for oil has increased, and, on the other hand, oil production has been cut, limiting the supply.

Real Estate: Premiums on residential real estate funds and discounts on commercial real estate in Switzerland have fallen further. Real estate funds have become more attractive in Q3 as a result and, with interest rates having peaked, met with interest from investors.

Private Markets

Private Equity: Since the beginning of the year, low buyout deal volumes and higher base rates have led to lower private equity valuations. The secondary market currently provides good opportunities to invest in quality companies at an attractive discount. Global megatrends such as digitalization, automation, new living, decarbonization and artificial intelligence offer good investment opportunities even in a difficult environment. There are also likely to be more exits over the next 12 to 24 months.

Private Debt: Limited availability of financing (syndicated loans in the USA down 40% in 2022 over 2021) has increased both volumes and margins in the private debt market, providing greater returns for investors despite lower corporate debt.

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Valterna AG
Neuhofstrasse 32
6340 Baar, Schweiz
+41 41 768 83 83
info@valterna.ch
valterna.ch