Justification for Home Preference Switzerland

The rather negatively connoted term "home bias" describes the tendency of investors to predominantly invest in local companies they are familiar with and understand. This often results in inadequate geographical diversification. According to modern portfolio theory, investors should diversify their portfolios broadly in order to reduce unsystematic risks (arising from the individual characteristics of a company) and thereby optimize the risk-return ratio. Despite this insight from modern portfolio theory, investors around the world show a strong home bias.
When it comes to our equity investment strategy, we prefer to refer to the concept of "Home Preference Switzerland", whereby we deliberately overweight the Swiss equity market based on the fundamentals.

The Swiss Home Advantage

Switzerland as a small, open economy with few natural resources is rather a special case in international comparison. Stability, innovation, growth and quality are crucial attributes in order to be able to compete internationally. Its liberal politics and attractive framework conditions for companies – well-educated workers, low taxes, state-of-the-art infrastructure, etc. – attract both employers and employees alike to Switzerland.
Consociational democracy and the strong principle of the rule of law form the foundation for political stability and contribute to economic consistency as well as to the high quality of the companies based here. All these aspects come together to make little Switzerland one of the 20 largest economies in the world and also one of its most competitive.
Furthermore, the Swiss financial centre offers excellent conditions, and its regulatory system is exemplary.

Switzerland Seen as a "Safe Haven"

The Swiss franc is considered a strong currency, supported by low inflation, low government debt and a credible, independent monetary policy. Especially in times of crisis, the franc is sought as a safe haven. Further, the majority of companies in the Swiss Market Index (SMI) are from more defensive sectors such as healthcare or consumer staples. Share prices are therefore comparatively less volatile.
An interesting insight from the 2008 financial crisis shows that the Swiss equity market, because of its defensive nature, performs better than international markets in times of crisis. The World Equity Index, for example, lost around 55% of its value during the financial crisis, whereas the Swiss Performance Index (SPI) "only" lost 43%.
The strength of the Swiss franc, coupled with the defensive nature of high-quality domestic companies, is not just a bulwark for times of crisis. Indeed, the Swiss Market Index (incl. dividends) has produced an annualized return of about 4.8% since the turn of the millennium, compared to 4.2% for the World Equity Index. Throughout this period, it has been difficult to earn much of anything on European equities and emerging market stocks have generated significantly lower returns (Fig. 1).

Swiss Equities in the Spotlight

High-quality Swiss companies are among the global leaders, providing stable corporate earnings and attractive dividend yields. Their global orientation enables them to capitalize on international growth opportunities and to spread risks across different markets, which in turn provides some diversification. An example here would be Nestlé, which generates just 1.2% of its sales in Switzerland. These companies bear the costs of hedging against currency and geopolitical risks themselves.

Conclusion

Switzerland offers attractive framework conditions for companies. These compete internationally on the strength of their stability, innovation, growth and quality. The global orientation of Swiss companies and the security provided by the Swiss franc increase the attractiveness of investing in Swiss companies. For Swiss investors, a certain home preference is therefore justified.

Author
Rafael Gonzalez

Fig. 1: Benchmark comparison of Swiss Market Gross Total Return Index (SMIC) since January 1, 2000 (in CHF)

Discover yet more interesting facts in our magazine.

Scan the QR code now

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