Quarterly Pulse – Monday, 3rd April 2023

Economic Outlook

Q1 2023 was busy on the news with two rate hikes and a banking crisis following the collapse of several US lenders and the takeover of Credit Suisse Group by UBS. While some of the analysts remain bearish and wait until the yield curve shows some positivity, others see the recent banking stress as the beginning of the end of the bear market.

Tactical Asset Allocation

Liquidity	Neutral
Rates	Overweight
Credit	Neutral
Equities	Neutral
Alternative Investments	Neutral

Macroeconomics

Despite all the reasons to be negative, Nasdaq has its best quarter since its second quarter of 2020, entering a bull market. It could be due to the rotation and cash outflow from the financial sector but also cooler than expected inflation data reported on March 31st. The US consumer spending data stabilized, the core PCE showed the smallest increase since October 2021, services finally fell for the first time in over a year, and the saving households' rate is up, the highest in over a year. Europe, in the meantime, is months or quarters behind the US in its inflation fight.

Nevertheless, it is still too early to estimate the full impact of the recent banking turmoil on the economies overall since coming tighter credit conditions and massive layoffs will have direct implications on economic activity and hence GDP growth.

In contrast, Chinese equity funds, along with Japan's, saw some strong cash inflows due to China's continuing reopening and raised growth forecast.

During a low economic growth environment, utilities, staples and healthcare are usually seen as defensive sectors. "Big Tech" stocks might continue their rally due to low debt and shift their focus towards profitability and lifting up productivity, especially after we have seen a large number of layoffs. Well, of course, small tech companies and Startups will probably suffer and face troubles in closing their funding rounds in current market conditions.

Fixed Income

Q1 can be divided into two parts. First, there was a repricing of interest rates expectations but later the banking crisis called everything into question again. After a good start into the new year, FI markets reversed gains as mounting signs of persistent inflation forced investors to make a reality check about their view on the future path of interest rate hikes. The kick-off was a strong US labour market report in February, followed by better-than-expected economic data and higher CPI. Especially the lingering labour shortage in selected industries is delaying the economic downturn.

Futures markets, which had previously predicted that the FED is going to pause soon, had to readjust their expectations. The market got ahead of itself in terms of pricing in FED cuts, hoping this cycle would end soon. After this reassessment, the new credo is "higher for longer". 10-year yields climbed from 3.35% to 4% by early March. The closely-watched spread between 2- and 10-year yields showed a discount larger than 100 bps for the first time since 1981.

That was the time we decided to introduce our "overweight rates" trade. We invested half of our target allocation to a 10-year US Treasury bond. For the second half we wait , as we like to have some dry powder for a potential average down of the position.

The second part of Q1 was totally different as renewed turmoil in the banking sector led to save-haven flows with the 10-year trading down again to 3.35%. The collapse of the Silicon Valley Bank and the shotgun wedding of Credit Suisse and UBS have forced a drastic repricing of how much further the FED will need to act to pursue its policy goals.

The recent banking crisis has sparked fears about tougher lending conditions, with financial institutions expected to increasingly pull back credit lines to protect their own balance sheets. Especially the commercial real estate sector is one of the critical areas, as it is primarily driven by regional banks in the US. Although the FED may be under less pressure to continue its battle against inflation, we do not believe that they are going to cut rates this year. Once the sentiment in the financial sector is improving, we are going back to focus on inflation and economic data. We think the peak in rates is near but first we need to have evidence from the data front.

Credit markets showed relatively good resilience in the current market environment. HY spreads widened by about 100 bps in March. The financial sector was the main underperformer (see AT1 article). For HY, we remain cautious as a potential recession is not off the table yet. This might

bring back volatility and higher default rates. 2023 will be a challenging fundamental landscape for corporates.

We prefer IG credits with intermediate maturities. Absolut yield levels of 4-5% for solid names still offer good value. For rates we remain overweight as odds of a recession are rising.

Additional Tier 1 capital (AT1s or Cocos)

One of the biggest shock for bond investors was the wipeout of USD 17 bn of Credit Suisse AT1-bonds (Cocos). The decision to write them down to zero as part of the bank's takeover by UBS came as a big surprise for markets.

AT1s were introduced as part of the post-global financial crisis regulatory reforms that pushed banks to increase their capital levels. Regulators require banks to hold certain levels of Tier 1 and Tier 2 capital as reserves, in order to ensure that they can absorb large losses without threatening the stability of the institution. If a bank's capital ratio falls below a predefined threshold, Coco investors can lose their principal or have their investment converted into equities. AT1s are a class of debt designed to take losses when institutions run into trouble but are generally believed to rank ahead of equity on the balance sheet.

However, in this case , shareholders were not fully wiped out, which some investors described as "an obvious breach of the hierarchy of claims". But the bond prospectus states that the Finma (Swiss regulator), "may not be required to follow any order of priority".

The specifics of the treatment of CS's AT1 bonds will now be legally challenged as several investors and analysts have argued that the contractual conditions for writing down the bonds were not met.

AT1s have grown into a USD 260 bn market since they were introduced in the aftermath of the global financial crisis. Especially in Asia, these instruments are popular with wealthy individuals. Investors also worried that issuance of new AT1 debt might dry up following the CS case. If banks know that they can't issue more AT1s anytime soon, they may stop calling them and this has significant issues for valuations. The extension-risk for the asset class is clearly growing.

The European Central Bank and other EU regulators pointed out that the Swiss rules are not applicable for European Banks and they also stressed the strategic importance of this market: "AT1 is and will remain an important component of the capital structure of European banks". Although the wipe-out of USD 17 bn can be seen as an isolated Swiss-case, and very unlikely to be repeated elsewhere, the impact to investors sentiment is considerable. Current pricing is very much liquidity driven, as bottom-fishers can't absorb selling pressure from Asian accounts.

For the moment we expect that the uncertainty in the asset class will continue and volatility will persist. The repricing will take time as trading flows are still skewed to selling. But we are not panicking as the asset class is too important for the banking system. For investors, who can take risk we see the current situation rather as a buying opportunity.

Equities

The month of March was packed with events: Silicon Valley Bank, Signature Bank as well as Silvergate are history; Credit Suisse went into a tailspin and was taken over by UBS; as well as the 180 degrees turn of the FED. And all this happened in less than two weeks!

Many investors will have had uncomfortable flashbacks of the Global Financial Crisis. The rush of policymakers and financial institutions to provide stability in such an unprecedented manner and speed brought back unpleasant memories. However, we would describe the current period of financial turmoil as a period of banking sector stress, not a crisis. There are important differences between what is happening in 2023 versus 2007/2008. While analysts view a systemic crisis as highly unlikely, there are negative growth effects that will result from the current banking stress. Credit is the lifeblood of the economy and recent developments will reduce its supply and increase its cost on an aggregate level. And one less helpful difference from 2008 is the problem of high inflation, which will prevent central banks from easing as quickly as they might have in response to this slower growth. At this point, it is difficult to gauge just how much credit standards will tighten and how much they will affect the economy. The range of macroeconomic outcomes has widened and shifted in a negative direction. On the other hand, a sooner pause in FED tightening is likely, which should provide some cushion for financial markets and the economy. Given still strong household and corporate balance sheets, we don't think the U.S. economy is heading for an imminent recession, but it is something to watch for in H2.

Equity Indicators

Valuation	Neutral
Momentum	Neutral
Seasonality	Positive
Macro-Economics	Negative

What's next as central banks' priority remains fighting inflation? Inflation risks have not been averted, and recent

developments have increased concerns about the stability of the financial system and the economy. Market expectations of central banks have therefore taken a dramatic turn this month. Three weeks ago, the FED was expected to possibly raise the key interest rate by 50 basis points in March and subsequently to up to 5.5% to 5.75%. Admittedly, the assessment of the further course of monetary policy is much more difficult than it some weeks ago. The financial markets expect from the FED for just one more interest rate increase and are already expecting interest rate cuts in summer. For most analysts, the fight against inflation remains the top priority for the central banks, which is why the markets tend to price in another hike in May by 25 basis points. However, our view is slightly different, and we expect the FED to be on hold which would catapult risky assets. The "higher for longer" is history in our view. If you look at the BoC's monetary policy and compare it to the FED, they are similar in their interest rate policies. Since fall 2019, their interest rate decisions have not differed by more than 25 basis points. Since the BoC did not raise its key rate in March and the FED did by 25 basis points, we expect a pause in May from the Americans.

Global stock markets were shaken by turbulence in the banking sector. Bank failures in the USA gave rise to concerns about financial market stability which spread to Europe. However, the financial system proved resilient, the world equity index even closed the month the month in positive territory. Within the index, however, there were significant differences. On a sectoral level, financial services were among the main losers. And commodity-related cyclicals in particular suffered from the worsening economic outlook. The high weighting of the aforementioned sectors resulted in underperformance in Canada, Australia and the UK. The US market, on the other hand, benefited for the first time in a long time from its high weighting in technology and communications, which were by far the main winners of the of the month. Both benefited from their high liquidity which made them safe havens. We already highlighted in January that the most beaten down sectors such as Tech should do well in Q1. Looking forward we are convinced that this sector will continue to outperform other sectors in Q2, i.e. should the FED stop hiking rates in May.

We are aware, that the risk-reward proposition for global equities at an index level is not particularly attractive. Stocks remain expensive, and we believe earnings estimates are biased lower from here, especially as credit conditions could tighten. Importantly, US stocks still account for nearly 60% of global equities and are particularly richly valued. However, and we highlighted this a few times in the past, we still favor U.S. equities over European ones for several reasons. The soon ending tightening cycle in the U.S. will be beneficial for Growth stocks, i.e. Tech. This circumstance, combined with positive seasonality in April, should lift equity markets. We may see liquidity coming back and a positive market sentiment which could surprise many investors to the upside. On this path, some important economic data will be published, which should be important for the central banks and for the further sentiment. Overall speaking, we are very comfortable with our neutral stance in Equities and favor U.S. high beta names and the Tech sector.

Alternative Investments

Gold has been profiting from the banking woes as expectations for further rate hikes were reduced. Gold started the year with USD 1'820 per ounce and closed the quarter at USD 1'970. Despite of the current environment of uncertainty, we expect Gold to be expensive and would further reduce exposure to it. Real yields and a softer US Dollar could be supportive whereas increased price will significantly reduce demand. Not only is the path of Gold depending on the central banks' interest rate path but also on central banks being buyers of Gold – last year by 1'136 tonnes with Turkey and China leading.

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Market Overview as of Monday, 3rd April 2023

Fixed Income

	Rate	Δ 1m	Δ 3m	Δ ytd
USD Overnight	4.80	0.25	0.48	0.48
USD 1y Swap	5.02	-0.54	-0.10	-0.10
USD 3y Swap	3.93	-0.85	-0.32	-0.41
USD 5y Swap	3.57	-0.76	-0.32	-0.45
USD 10y Swap	3.41	-0.57	-0.27	-0.43
EUR Overnight	-0.51	-0.02	-0.01	-0.01
EUR 1y Swap	3.57	-0.25	0.32	0.29
EUR 3y Swap	3.22	-0.43	0.05	-0.09
EUR 5y Swap	3.00	-0.44	-0.04	-0.24
EUR 10y Swap	2.91	-0.37	-0.08	-0.30
CDX Xover 5y	4.63%	0.30%	-0.15%	-0.21%
iTraxx Xover 5y	4.37%	0.40%	-0.25%	-0.37%

	Δ 1m	Δ 3m	Δ 6m	Δ ytd
USD Deposit 1m	0.2%	0.5%	0.9%	0.9%
USD Aggregate 1-3y	1.5%	1.5%	2.2%	1.5%
USD Aggregate 3-5y	2.5%	2.1%	3.3%	2.2%
USD Aggregate 5-7y	2.9%	2.5%	4.0%	2.8%
USD Aggregate 7-10y	2.7%	2.4%	4.1%	2.9%
EUR Overnight	0.2%	0.6%	0.9%	0.6%
EUR Aggregate 1-3y	1.0%	0.7%	0.1%	0.8%
EUR Aggregate 3-5y	1.8%	0.9%	0.0%	1.4%
EUR Aggregate 5-7y	2.5%	1.2%	0.2%	2.1%
EUR Aggregate 7-10y	3.2%	1.6%	0.0%	3.0%
US Corp. HY	0.8%	3.0%	7.3%	3.6%
EUR HY	0.3%	2.6%	8.0%	3.0%

Equity

	Price	P/E	D. Yield	FCF yield
MSCI World	8'603	16.8	2.2%	4.7%
S&P 500	4'117	18.8	1.7%	4.0%
NASDAQ	13'135	25.5	0.9%	2.9%
Euro Stoxx 50	4'311	12.7	3.5%	6.3%
SMI	11'080	17.2	3.2%	5.6%
FTSE 100	7'686	10.6	4.2%	10.5%
DAX	15'592	12.0	3.4%	6.3%
MSCI Asia Pacific	162	13.7	2.9%	4.8%
FTSE China A50	13'215	11.3	3.0%	7.5%
MSCI Emerging Market	990	12.4	3.1%	6.3%
PH Semiconductor	3'198	24.7	1.4%	2.9%

	Δ 1m	Δ 3m	Δ 6m	Δ ytd
MSCI World	1.4%	7.8%	15.8%	7.7%
S&P 500	1.8%	7.7%	11.9%	7.2%
NASDAQ	6.9%	20.9%	17.0%	20.1%
Euro Stoxx 50	0.4%	11.0%	29.0%	13.6%
SMI	-1.0%	0.9%	7.7%	3.3%
FTSE 100	-3.3%	1.7%	11.2%	3.1%
DAX	0.1%	9.9%	27.7%	12.0%
MSCI Asia Pacific	0.6%	3.4%	16.8%	4.1%
FTSE China A50	-2.6%	1.6%	2.4%	1.6%
MSCI Emerging Market	0.2%	2.9%	13.0%	3.5%
PH Semiconductor	5.6%	27.9%	33.6%	26.3%

Commodity

	Price	FCST 21	FCST 22	Δ Future
Gold	1'984	1798	1806.9	0.2%
Silver	24.19	25.1	21.75	0.8%
Platinum	997	1091	962.36	1.0%
Palladium	1'497	2410	2120.77	2.3%
Crude Oil	80.69	68.12	96	0.8%
Brent Oil	85.09	70.95	100	-1.1%

	Δ 1m	Δ 3m	Δ 6m	Δ ytd
Gold	7.0%	7.5%	17.2%	8.6%
Silver	13.9%	-0.9%	16.1%	-0.1%
Platinum	1.2%	-9.1%	10.2%	-8.2%
Palladium	3.3%	-12.1%	-33.2%	-17.1%
Crude Oil	1.1%	4.3%	5.4%	0.3%
Brent Oil	-0.2%	4.2%	5.4%	0.4%

Foreign Exchange

	Price	FCST 21	FCST 22	Δ Spot
EUR/USD	1.0912	1.14	1	-8.7%
GBP/USD	1.2419	1.35	1.15	-7.7%
USD/CHF	0.9117	0.93	0.97	6.2%
USD/JPY	132.30	114	144	8.5%
EUR/CHF	0.9949	1.06	0.98	-1.5%
USD/RUB	118.69	71.19	62.5	-64.1%
EUR/RUB	85.66	80.7	62	-32.3%

	Δ 1m	Δ 3m	Δ 6m	Δ ytd
EUR/USD	2.6%	3.5%	11.1%	1.9%
GBP/USD	3.2%	3.8%	9.7%	2.8%
USD/CHF	2.7%	2.7%	8.8%	1.4%
USD/JPY	2.7%	-1.0%	9.3%	-0.9%
EUR/CHF	0.1%	-0.8%	-2.0%	-0.5%
EUR/RUB	-6.1%	-10.5%	-31.8%	-7.4%

Source: Clarus Capital Group, Bloomberg

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SWITZERLAND TOP50 INDEPENDENT ASSET MANAGERS 2022

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