



Investment letter

Monthly review of global financial
markets



SWISS
CAPITAL^{IB}

FEBRUARY 2023

MACROECONOMICS

The transition from 2022 to 2023 was marked by continued prospects of slower growth in the US while Eurozone's particularly gloomy expectations at the end of last year have markedly improved thanks to collapsing gas prices and Chinese reopening.

In the US, most advanced indicators in January continued to point to a recessionary environment later this year, with the Empire Manufacturing index plummeting to levels not seen since the Great Financial Crisis excluding Covid, and PMIs still well in contraction territory. Hard data are starting to show signs of softening too, with retail sales and industrial production sharply down in December. Meanwhile, the December labour report showed a still tight but gradually slowing job picture, with the monthly pace of jobs creation (223k) at its lowest since December 2020 and wage growth down to 4.6% YoY. Unemployment rate remains sticky around historical lows (3.5%), consistent with the fact that it is the most lagging real economic indicator, which should rise in the latter part of the year.

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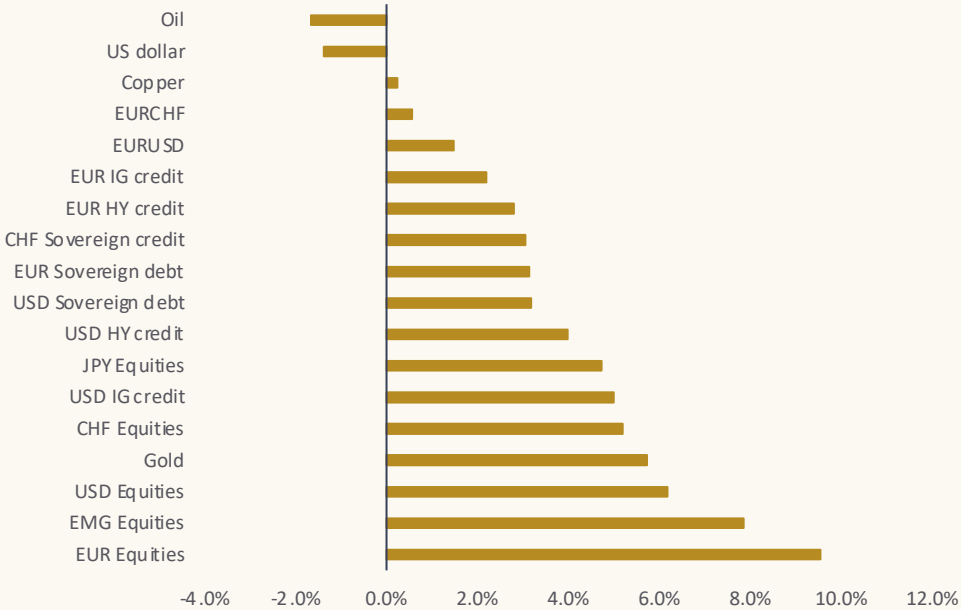
Inflation is now on a well-established downward trend, with the peak confirmed in December. The sticky and lagging shelter component is the last remaining culprit behind positive monthly core inflation prints, and should normalise later this year according to the forward-looking NAHB indicator of housing activity and sentiment in the US.

As a result, the end of the tightening cycle in the US is now well anticipated by the markets, with the suspense shifting to the easing cycle. Markets' pricing of cuts early H2 2023 seems premature, with some repricing likely due, potentially impacting risk assets' momentum when it happens.

January was also marked by the beginning of a new debt ceiling saga, with the government officially reaching its borrowing limit on January 19th. While the ceiling always ends up being raised (10 times since 2011), the tense political configuration this time means that disruption's risks may be higher than usual, with potentially higher uncertainty and tighter fiscal policy, reinforcing our cautious view on the US economy.

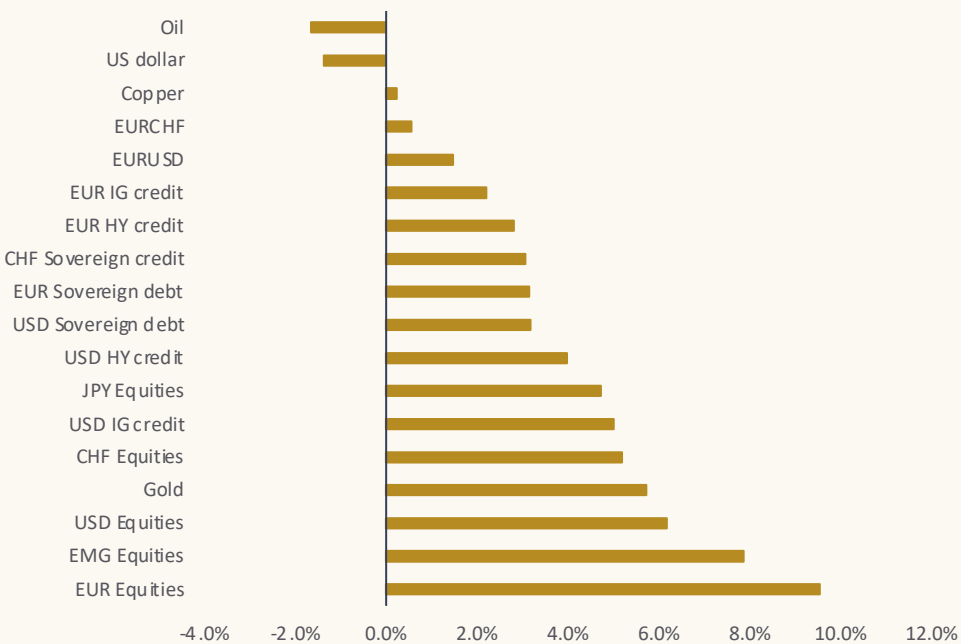
OVERVIEW

MAIN ASSET CLASSES MONTHLY PERFORMANCE



Source: Bloomberg, 31/01/2023

MAIN ASSET CLASSES PERFORMANCE YEAR-TO-DATE



Source: Bloomberg, 31/01/2023
Past performance is not indicative of future performance

MACROECONOMICS (continued)

In the Eurozone, macroeconomic risks linked to energy have all but disappeared as warm and windy weather, lower weather-adjusted consumption and a big increase in LNG imports led to a swift replenishing of inventories and collapsing prices.

In addition, Chinese reopening will provide a big boost to European exporters, Germany in particular, lifting yet another cloud on the region's outlook. As a result, the major tail risk now comes from an ECB potentially overly hawkish stance. Indeed, given no evidence of wage-price spiral at this stage, going well above 3% on the key depo rate may bring a deeper-than-necessary slowdown to tame mostly supply-driven inflation.

Finally, after three difficult years, China is set for a large cyclical bounce from a low base as zero-Covid policy, regulatory tightening and property deleveraging are all on track to fade simultaneously in 2023. Question marks remain around consumer confidence's ability to rebound with the true death toll difficult to track from abroad. If this happens, significant excess savings can be tapped and contribute to 2023 growth.

EQUITY MARKETS

"We would remain positioned on long duration stocks with cheap valuations, composed by the renewable segment"

Global equities rallied strongly in January on improving odds of a soft landing in the US and better growth prospects in the EU and China. Markets were clearly risk-on as equities had the second-best January in more than three decades.

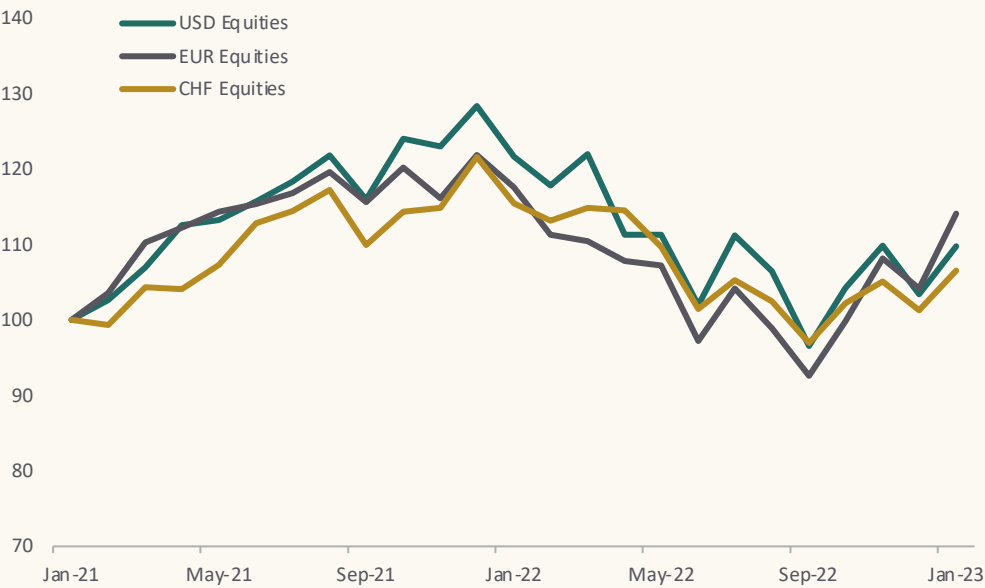
Europe outperformed among developed markets countries, with all core EU markets performing strongly on the back of the drop in natural gas prices and tailwinds from rising Chinese growth expectations. Defensive indices like the FTSE 100 and SMI lagged.

Growth outperformed other factors and had its best month since July 2022. With inflation starting to trend down, central bank hikes have likely reached their final stages, reducing duration risk and benefiting growth assets.

While we acknowledge the European tail risk of gas prices and China re-opening have been reduced, we think the market has gone too far too fast, courtesy of the short covering in European futures.

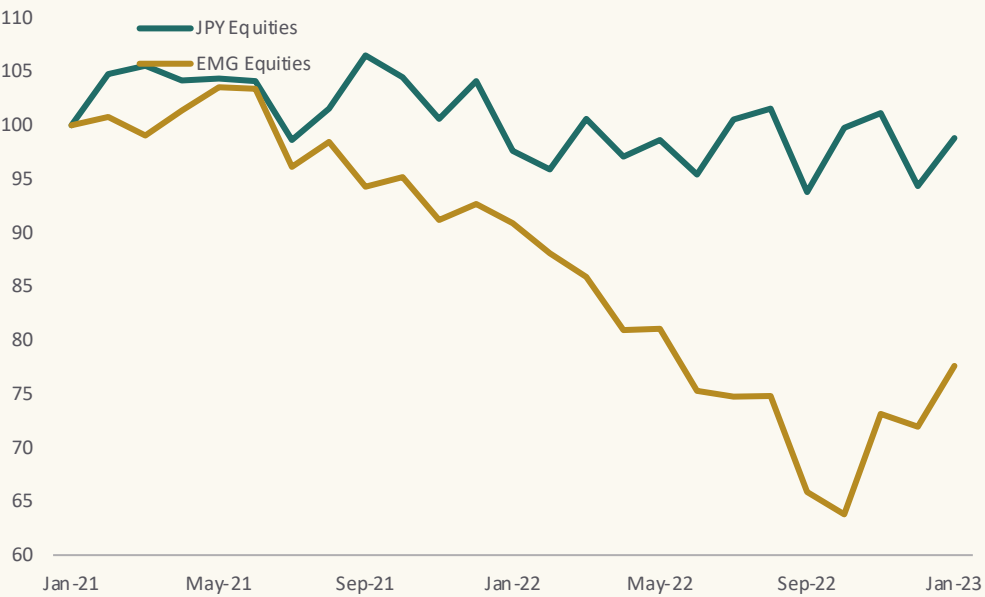
EQUITY MARKETS

EQUITY MARKETS EUR USD CHF
PERFORMANCE OVER 2 YEARS



Source: Bloomberg, 31/01/2023

EQUITY MARKETS JAPAN – EMERGING MARKETS
PERFORMANCE OVER 2 YEARS



Source: Bloomberg, 31/01/2023
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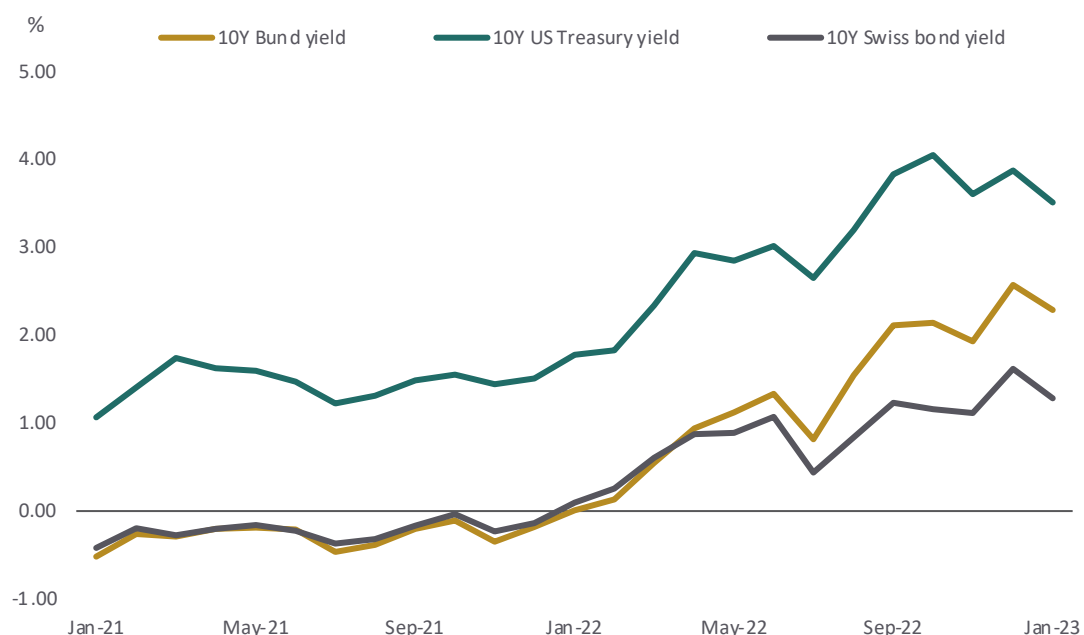
BOND MARKETS

Government bond yields fell materially with US Treasuries outperforming, as the disinflation trend accelerates, the Fed slows the pace of rate hikes and edges closer to a pause. The recent and steep fall in gas prices also helps reduce inflation tail risk in the euro area. With policy rates set to reach very restrictive levels in Q1 and as the inflation outlook improves, interest rate implied volatility has fallen steadily, softening a material headwind for corporate credit.

Primary markets were extremely active, with January record issuance levels set for European banks as they prepare for the upcoming remaining roll-off of TLTRO. Earnings risk is seen as particularly low for European banks in this cycle. Financials outperformed non-financials as demand for the banking sector outweighed the heavy supply. ATIs logically outperformed with various denominated new issues coming at attractive levels and trading well on the break.

“Credit spreads continued on their tightening trend ”

10Y SOVEREIGN BOND YIELDS EVOLUTION OVER 2 YEARS



Source: Bloomberg, 31/01/2023
Past performance is not indicative of future performance

CURRENCIES

The USD continued to weaken in January as the Fed is on track to conclude its **tightening cycle** in the next few months while global growth concerns have abated with a still resilient US economy, Chinese reopening and the very likely avoidance of a European energy crisis.

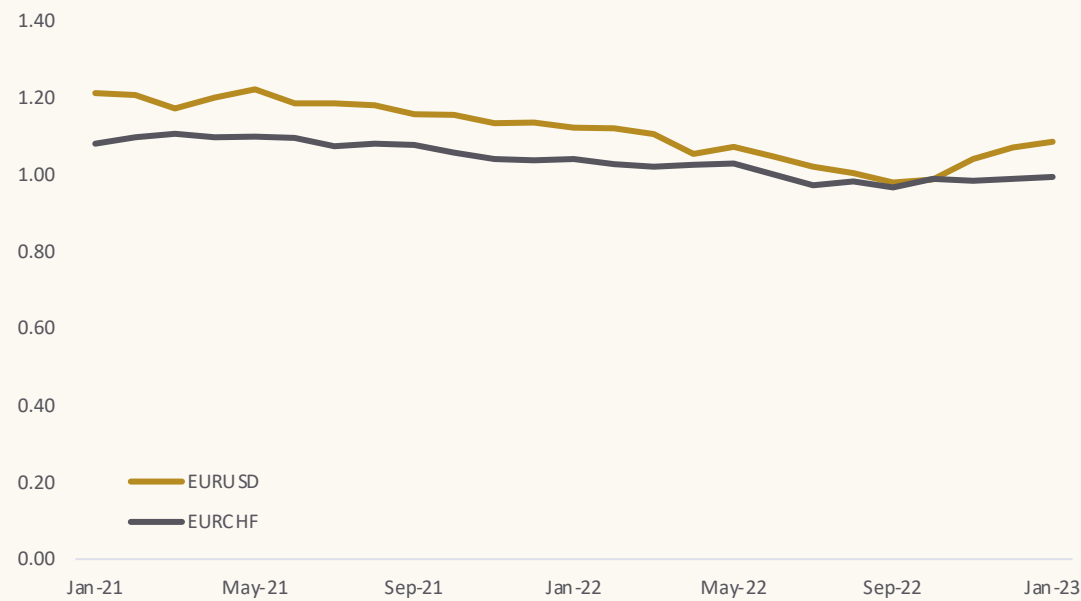
Whilst the USD peak is likely behind, the downtrend may slow somewhat as growth concerns take over later this year.

With the **EUR-USD** fair value likely around 1.15, there is still some upside, with monetary policy and growth differentials probably still playing more in favour of the EUR in 2023.

Similarly, the **EUR-CHF** pair should benefit from monetary policy differential. The ECB is still battling high inflation, while the Swiss National Bank has less reason to hike aggressively given low inflation.

There is also likely more upside to the **JPY-USD** pair despite a very significant retracement of the pair already. The driver of the yen's decline in 2022 has been exclusively monetary policy divergence between Japan and the US, which will continue to fade. The yen would also benefit from any further tweaks to the Bank of Japan's policy settings, and it tends to outperform during global slowdowns.

USD & CHF
EVOLUTION OVER 2 YEARS AGAINST THE EUR



Source: Bloomberg, 31/01/2023
Past performance is not indicative of future performance

COMMODITIES

OIL

Whilst the oil market remains stuck between competing forces of constrained supply and slower global growth, the swift reopening of China and weaker USD brought a material change to the near-term picture, and provided a support to crude prices, which may continue to play out in 2023.

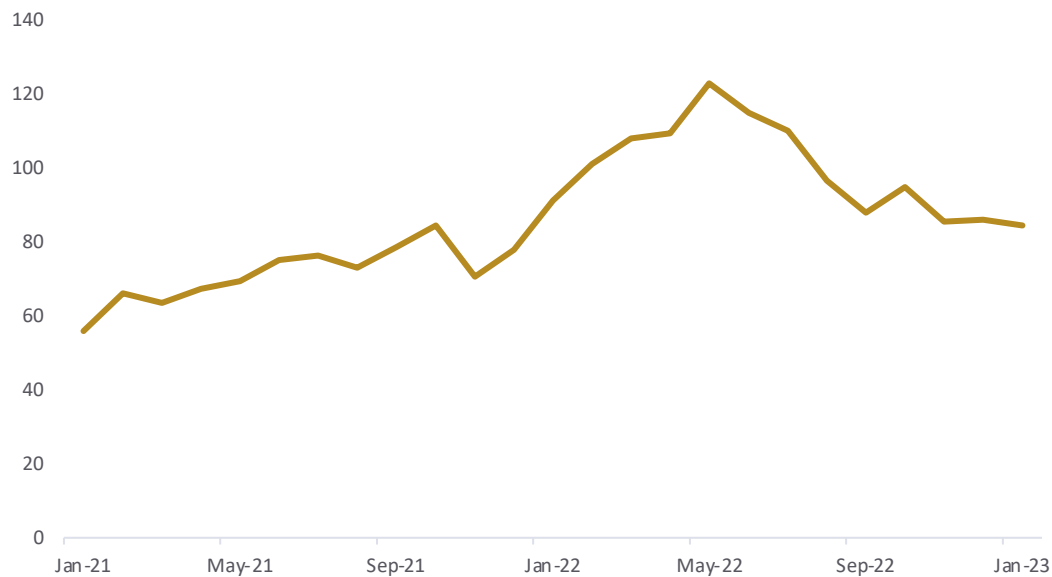
With almost all mobility restrictions lifted in China, the country's demand may bounce significantly from a very low base, with international travel a significant source of additional oil demand. In addition, the upcoming February EU embargo on Russian oil may challenge global supply levels.

This should put a floor under oil prices in the next few months at least. That said, a significant economic slowdown in the latter part of the year may limit the upside potential.



The swift Chinese reopening may continue to support oil prices, but the upside may be ultimately limited by a slowdown later this year

OIL
EVOLUTION OF BRENT PRICES OVER 2 YEARS



Source: Bloomberg, 31/01/2023
Past performance is not indicative of future performance

COMMODITIES

GOLD

Gold’s ascent since its early November’s lows continued relentlessly in January, with the yellow metal now well above 1900 (\$ per ounce).



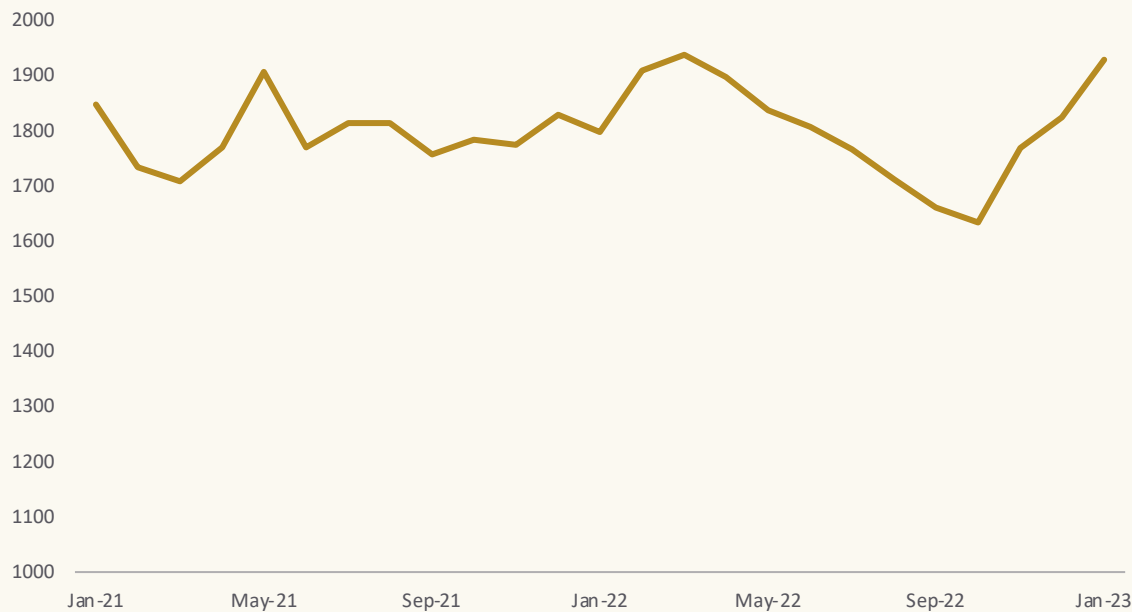
Whilst the move up may be explained by the Fed approaching the end of its tightening cycle, a weaker USD and fears of an upcoming economic slowdown, current prices are not in line with high and positive real rates.

Current Gold’s prices are not justified by high and positive real rates

As such, the downside from here is likely more significant than the upside potential.

It might make sense to buy Gold at lower levels, with real rates on track to compress, when recession and the easing cycle approach.

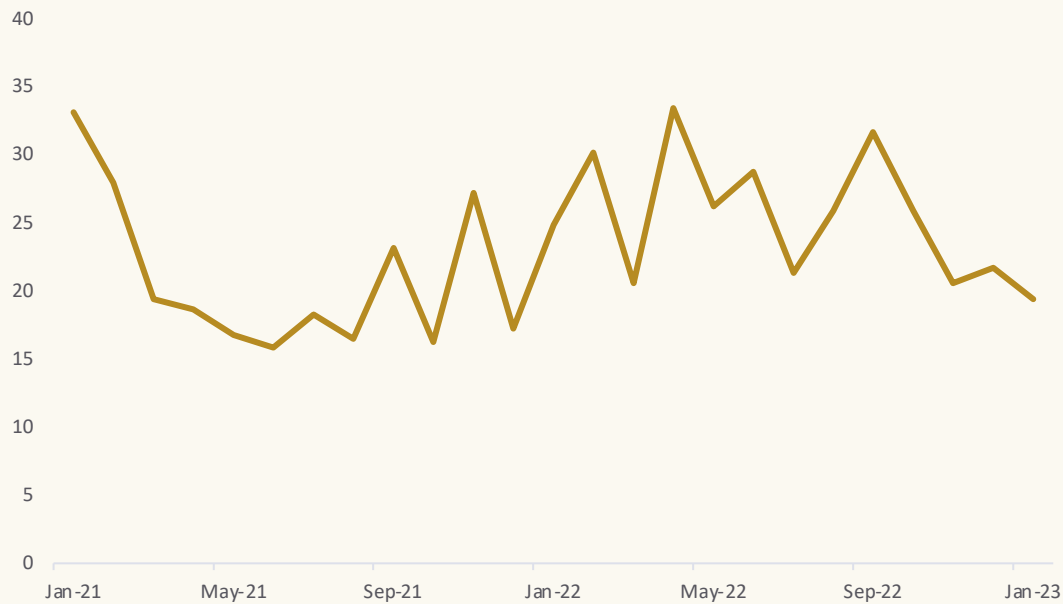
GOLD
EVOLUTION OVER 2 YEARS



Source: Bloomberg, 31/01/2023
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VOLATILITY

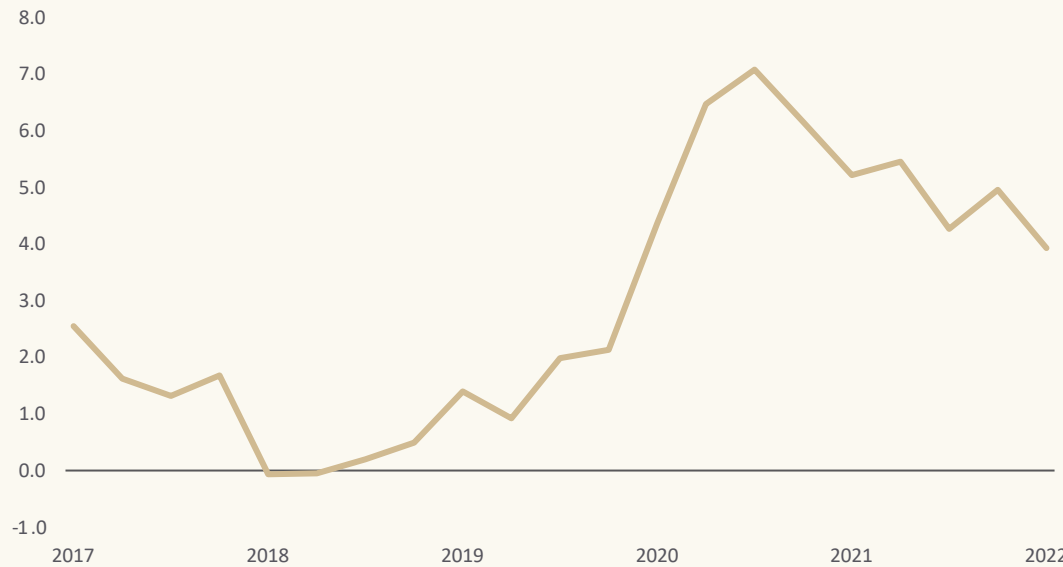
VOLATILITY – VIX INDEX
EVOLUTION OVER 2 YEARS



Source: Bloomberg, 31/01/2023

REAL ESTATE

SWISS RESIDENTIAL REAL ESTATE
ANNUAL PRICE CHANGE



Source: Bloomberg, 31/01/2023
Past performance is not indicative of future performance

CALENDAR

Date	Country	Economic Data	Period	Previous
01 February	US	Federal Reserve Interest Rate (%)	Jan-23	4,5
	US	Manufacturing PMI	Feb-23	48,4
	Eurozone	Inflation (YoY)	Feb-23	9,2
	Eurozone	Markit Manufacturing PMI	Feb-23	47,8
	Eurozone	Unemployment Rate (%)	Jan-23	6,5
	UK	Markit Manufacturing PMI	Feb-23	45,3
	Switzerland	Manufacturing PMI	Feb-23	54,1
02 February	Eurozone	ECB Interest Rate (%)	Jan-23	2,0
	UK	Bank of England Interest Rate (%)	Mar-23	3,5
03 February	US	Employment (000s)	Jan-23	223,0
	US	Unemployment Rate (%)	Jan-23	3,5
	US	ISM Non-Manufacturing Index	Jan-23	49,2
	Eurozone	Markit Services PMI	Feb-23	50,7
	UK	Markit Services PMI	Feb-23	48,0
07 February	Germany	Industrial Production (MoM)	Dec-22	0,2
	Switzerland	Unemployment Rate (%)	Jan-23	1,9
10 February	US	Consumer Confidence	Feb-23	64,9
	China	Inflation (YoY)	Jan-23	1,8
	UK	Real GDP (QoQ)	Dec-22	-0,3
13 February	Switzerland	Inflation (YoY)	Jan-23	2,8
14 February	US	Inflation (YoY)	Jan-23	6,5
	Eurozone	Employment (QoQ)	Dec-22	0,3
	Eurozone	Real GDP (QoQ)	Mar-23	0,1
	France	Unemployment Rate (%)	Dec-22	7,3
	UK	Unemployment Rate (%)	Dec-22	3,7
	Japan	Industrial Production (MoM)	Jan-23	-0,1
	Japan	Real GDP (QoQ)	Dec-22	-0,8
	US	Industrial Production (MoM)	Jan-23	-0,7
	Eurozone	Industrial Production (MoM)	Dec-22	1,0
15 February	UK	Inflation (YoY)	Jan-23	10,5
	US	Philadelphia Fed Business Survey	Feb-23	-8,9
	Japan	Nikkei Manufacturing PMI	Feb-23	48,9
22 February	US	Fed minutes	Mar-24	
	Germany	Ifo Business Climate	Feb-23	90,2
23 February	US	Real GDP (QoQ)	Mar-23	2,9
24 February	Germany	Real GDP (QoQ)	Mar-23	-0,2
28 February	France	Real GDP (QoQ)	Mar-23	0,1
	Switzerland	Real GDP (QoQ)	Dec-22	0,2
	Switzerland	KOF Leading Indicator	Feb-23	97,2

LET'S TALK ABOUT IT.

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