# Investment letter

Monthly review of global financial markets

SWISS CAPITAL IB

December 2023

# MACROECONOMICS

The month of November started with an FOMC meeting where the Fed kept its key policy rates on hold at 5.25%-5.5% for the second meeting in a row, in a unanimous decision. At the time of the meeting, they kept the optionality to raise rates again if necessary, but the tone was dovish, with risks of doing too much rather than too little becoming more balanced.

**Since then, most data and Fed speaks have reinforced the idea that the Fed is done with its hiking cycle.**

**October CPI surprised on the downside** with yearly growth rates at 3.2% and 4.0% for the headline and core respectively, versus 3.3% and 4.1% expected. Going forward, it is becoming increasingly clear that goods' inflation is not an issue anymore, housing prices will continue to fall with the usual lags (linked to asking rents taking time to filter through) and core services ex-housing, the "supercore", will keep decreasing as the labour market continues to soften. This good news on the disinflation front was confirmed by **the October core PCE, the Fed's preferred inflation gauge, falling to 3.5% y/y.**

One element worth noting and watching on the inflation front, though, is that the November University of Michigan survey showed that **long-term inflation expectations are at a 12-year high** of 3.2%, while 1-yr expectations are at an elevated 4.5%. This should remind the Fed that risks of unanchored inflation expectations are never too far given where we come from.

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MOST DATA AND FED SPEAKS IN NOVEMBER HAVE REINFORCED THE IDEA THAT THE FED IS DONE WITH ITS HIKING CYCLE

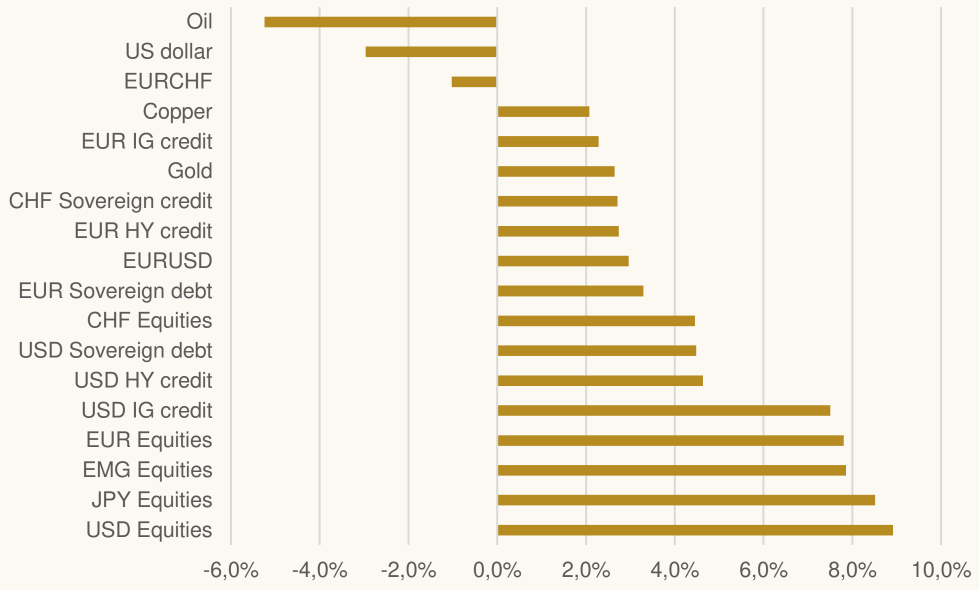
Meanwhile, November brought more evidence that growth has been very strong in the US up to the end of September, with the second release of 3rd quarter GDP revised even higher to a stellar 5.2% annualized quarterly growth.

However, **other indicators signal that the third quarter's strength may not be repeated in Q4.** The Conference Board Consumer Confidence survey increased to 102 in November, but from a downwardly revised 99.1. Moreover, the sub-80 reading on the expectations index is consistent with a recession next year, and the present situation index fell to a 31-month low. We also note that while the services component of November PMIs surprised on the upside at a still fairly resilient 50.8, the manufacturing side came out below expectation at a contractionary 49.4.

As for the highly scrutinized labour market's figures, **weekly initial jobless claims remain low so far in this cycle, but continuing claims are starting to pick up more meaningfully**, with data for the week ending November 18th surprising quite significantly on the upside at 1.93mn versus 1.87mn expected. We would not read too much into one single data point, but this might be worth monitoring in the next few weeks.

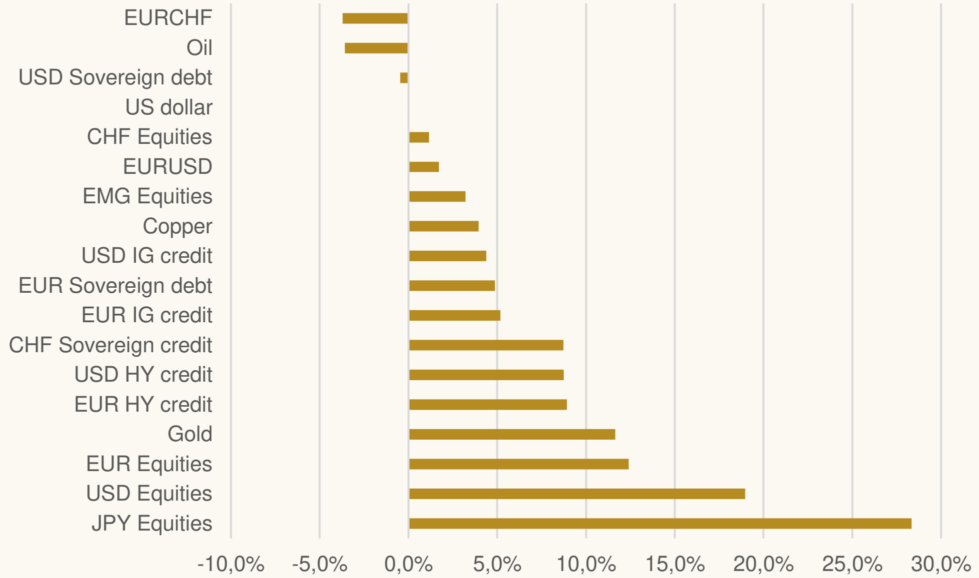
# OVERVIEW

**MAIN ASSET CLASSES**
MONTHLY PERFORMANCE




*Source: Bloomberg, 30/11/2023*

**MAIN ASSET CLASSES**
PERFORMANCE YEAR-TO-DATE




*Source: Bloomberg, 30/11/2023*
*Past performance is not indicative of future performance*

# MACROECONOMICS (CONTINUED)

Turning to the Eurozone, if one was really needed, **the sharp fall in November inflation from 2.9% to 2.4% for the headline and 4.2% to 3.6% for the core**, is a testament that **monetary policy is being channeled to the economy**, as the contracting money supply has been signaling for months. This was confirmed by the second reading of 3rd quarter GDP in the Eurozone at **0.1% quarterly contraction**.

Thus, going forward, as the tone of the last ECB meeting indicated, the focus will turn to support growth rather than fight inflation. On that front, markets' pricing of a first cut in Q2 2024 seems fair.

If the ECB's reaction function is dovish enough, economic activity may be close to troughing with a recovery on the cards later in 2024. Indeed, **the November forward-looking ZEW index provided hopes that a recovery could materialise later in 2024** with expectations for the Euro Area rebounding sharply to a 9-month high.

A hawkish reaction function on the other hand, with belated rate cuts, would precipitate a deeper recession. **Although Eurozone PMIs improved in a welcome sign that the economy may be close to bottoming, they remain all in contraction and at depressed levels**, with the manufacturing index at 43.8 and the services component at 48.2, leaving the door open to another contraction in GDP during the 4th quarter of 2023.

# EQUITY MARKETS

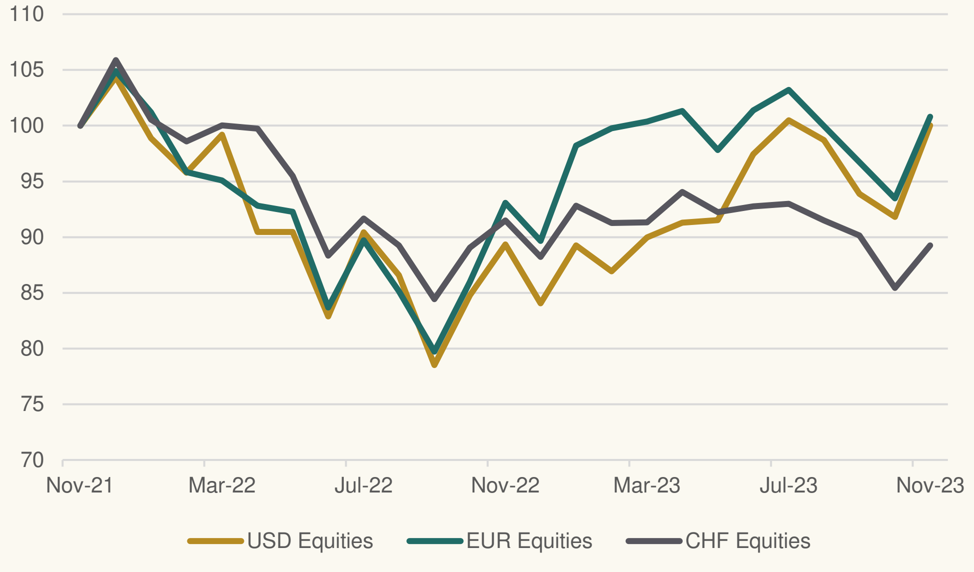
**Rates relief prompted risk on rally in markets in November with global equities and bonds delivering their best returns since Nov'20 and Dec'08 respectively**. Consequently, Global 60:40 portfolio delivered its strongest returns in three years with volatility retracing sharply lower after the spike in October. With inflation continuing to surprise on the downside in the West, **investors piled on to rate cut expectations and pared short positions significantly** in longer duration and unloved rate sensitive parts of the markets like small caps, real estate etc., At the same time with the conflict in the Middle East seemingly contained for now, the geopolitical risk premium also has been partially unwound adding to the bullish sentiment. Dollar, commodities and Oil declined delivering the worst returns among the major asset classes last month.

INVESTORS PILED ON TO RATE CUT EXPECTATIONS AND PARED SHORT POSITIONS SIGNIFICANTLY

**More specifically, stocks rallied back after three months of decline** with DM strongly outperforming EM. **US outperformed Europe with Tech heavy Nasdaq delivering better returns than the S&P 500**, followed by DJIA. Within Europe, returns dispersion was high with Sweden, Germany and Spain outperforming the most given their Cyclical and duration tilt. Meanwhile, the UK significantly underperformed given its under exposure to Tech and commodities tilt. EM equities lagged notably as China underperformance acted as a drag with investors still looking unimpressed with the raft of measures taken by the authorities to boost growth.

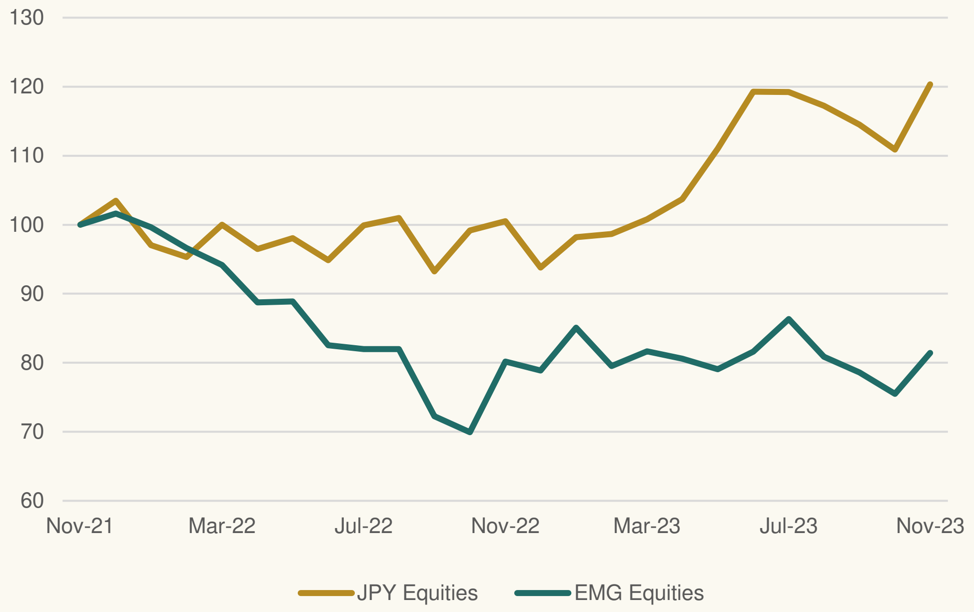
# EQUITY MARKETS

**EQUITY MARKETS EUR USD CHF**
PERFORMANCE OVER 2 YEARS




*Source: Bloomberg, 30/11/2023*

**EQUITY MARKETS JAPAN – EMERGING MARKETS**
PERFORMANCE OVER 2 YEARS




*Source: Bloomberg, 30/11/2023*
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# BOND MARKETS

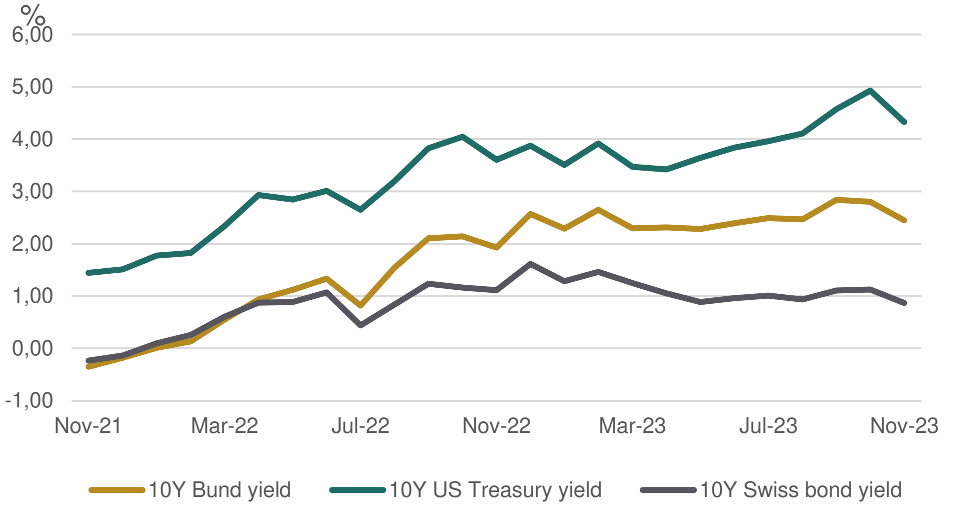
**The markets experienced a spectacular end-of-year rally in November, fueled primarily by the easing of long-term rates in the US and Europe**. Following the peak in 10-year yields at the end of October, investors saw a historic opportunity to increase their bond allocation and lengthen the average duration of their portfolios, as risk became increasingly asymmetrical. As a result, the UST 10-year lost 60bps over November, while 10y Bund yield declined by 35bps.

**The credit market obviously benefited from this movement** across its entire spectrum, even if the most spectacular movements were seen on US IG (the longest in duration), $-denominated emerging debt (historically highly correlated with US investment-grade bonds), and European subordinated financials (the highest carry outside HY).

**November's upward movement finally makes 2023 a good year for bond total returns, with a reservoir of performance intact for 2024** in the wake of the expected global cut in key rates (the battle against inflation is on the way to being won) and the search for defensive assets in view of slowing economies. According to us, gains of between 5% and 10%, depending on the risk chosen, are base-case assumptions for next year.

> NOVEMBER'S UPWARD MOVEMENT FINALLY MAKES 2023 A GOOD YEAR FOR BOND TOTAL RETURNS, WITH A RESERVOIR OF PERFORMANCE INTACT FOR 2024.

**10Y SOVEREIGN BOND YIELDS**
EVOLUTION OVER 2 YEARS




*Source: Bloomberg, 30/11/2023*
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# CURRENCIES

Amid bets that Fed hikes are now in the rearview mirror, the **DXY** dipped below 103, the lowest since last August. This move was driven by the global consensus around the US economy's trajectory shifting from "higher for longer" to "soft landing" and the US 10Y benchmark bond yields ebbing from 5% to below 4.3%. Over the coming weeks, rates' differentials with other key economies might play an important role in the USD trajectory. Whilst the US economy softens and the Fed prepares to cut rates later in 2024, other major blocs, such as the Eurozone, will likely do the same, possibly limiting further downward pressure on the greenback.

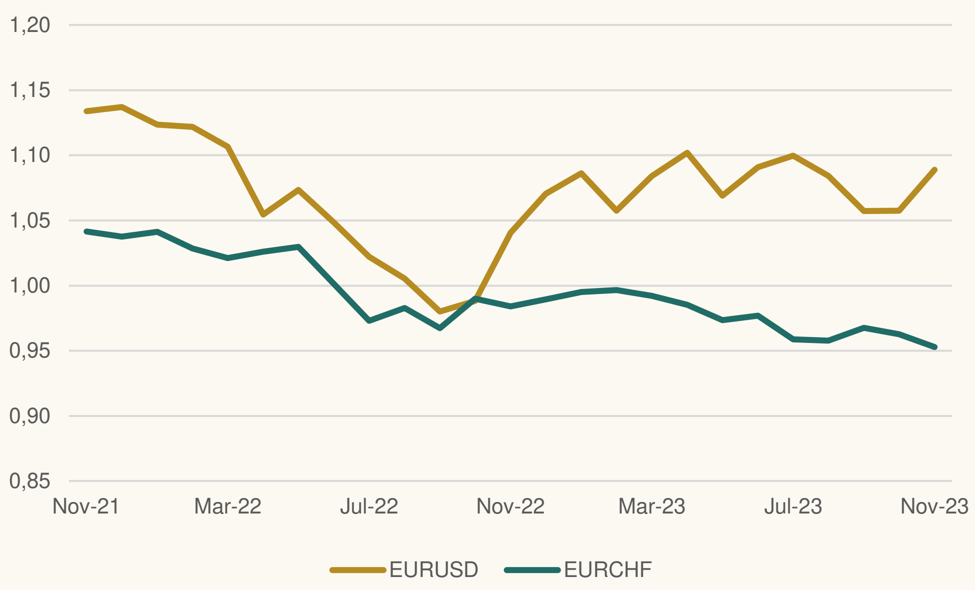
The **EUR** benefited from the relative decline in the **USD** to edge higher in its 1.05-1.11 trading range so far this year. The single currency jumped from 1.05 and ended the month testing the 1.10 level. In addition to a cooling US economy, November's uptick in the pair is no stranger to the ECB's cautious comments arguing that the "last mile" of disinflation may be arduous to cover. Moreover, the Eurozone may have already bottomed, helping the **EUR** to pick up towards levels in line with its 1.15 fundamental value, from a PPP standpoint.

The combination of a hawkish Bank of England (BoE) and resilient PMIs (Composite at 50.1 in November) helped the **GBP** gain traction. The central bank is expected to cut less than its European and American counterparts in 2024, sending the **GBP-USD** above 1.26.

The **CHF** extended gains against the **USD**, with the **CHF-USD** ending November just shy of 1.15 from less than 1.10 at the start of the month. True, there was little need for the SNB to hike rates above 1.75% and easing geopolitical concerns limited demand for the Swiss safe-haven currency. However, the Franc benefitted from a weaker USD and the central bank's continued intent to curb imported inflation by drawing in its foreign exchange reserves.

**USD & CHF**

EVOLUTION OVER 2 YEARS AGAINST THE EUR

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# COMMODITIES

## OIL

**Brent** traded near $80 in the last days of November, way below its September peak above $90.

On the supply side, discrepancies between OPEC producers explain the IEA's reckoning that **global oil markets should be in slight surplus in 1Q24**, despite the potential extension of OPEC+ supply cuts into 2024. In fact, some members of the cartel can't afford cutting back on output in the aftermath of substantial losses in production capacities and revenues in recent years. Overall, oil supply flows have suffered no material impact from the war between Israel and Hamas.

Demand is seen as robust – even higher than expected – with China accounting for 1.8 mb/d of the total 2.4 mb/d increase, lifting demand to 102 mb/d in 2023. However, **Brent's future curve has slid in a lower trading range,** owing to a deteriorating global macroeconomic sentiment.

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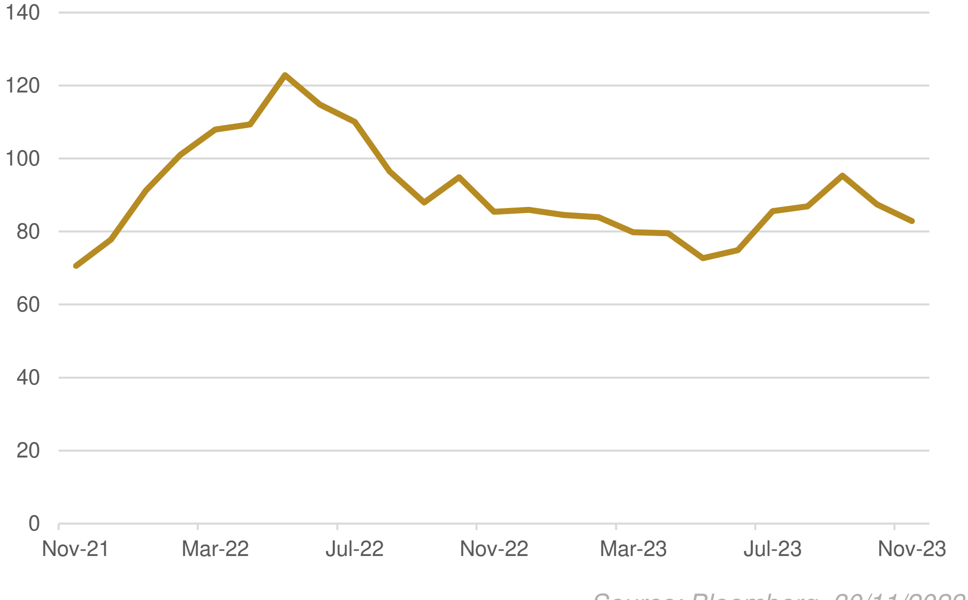
**OIL**

EVOLUTION OF BRENT PRICES OVER 2 YEARS

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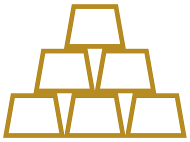
# COMMODITIES

## GOLD



After soaring when the Israel-Hamas war started in October, Gold retreated in the first half of November. But the non-yielding asset rebounded strongly on the back of hopes that the Fed could cut rates earlier than initially expected, resulting in lower Treasury yields and a weaker dollar.

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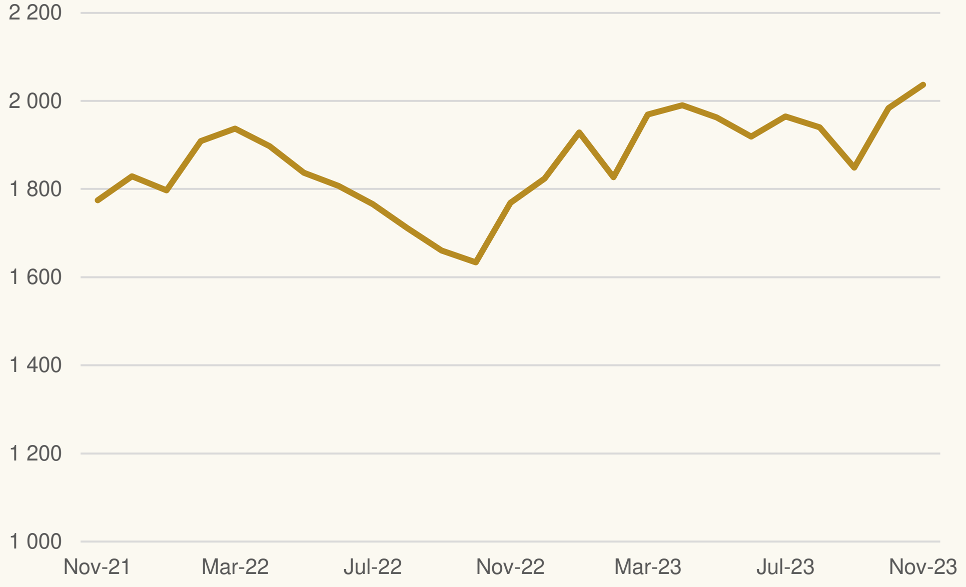
**GOLD**
EVOLUTION OVER 2 YEARS

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# VOLATILITY

**VOLATILITY – VIX INDEX**
EVOLUTION OVER 2 YEARS


*Source: Bloomberg, 30/11/2023*
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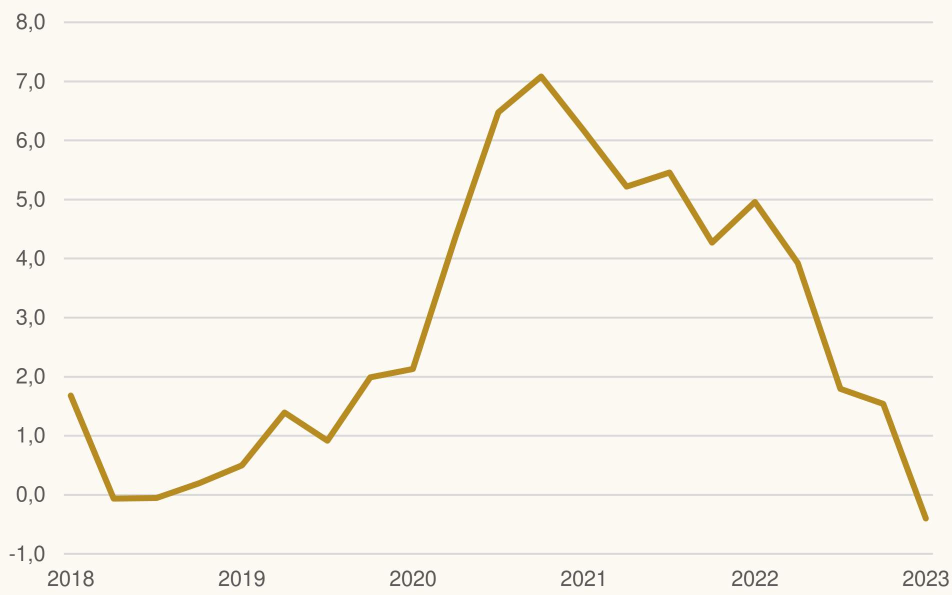
# REAL ESTATE

**SWISS RESIDENTIAL REAL ESTATE**
ANNUAL PRICE CHANGE

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# CALENDAR

| Date | Country | Economic Data | Period | Previous |
|---|---|---|---|---|
| **07 December** | China | Exports (YoY) | Nov-23 | -6,4 |
| | Eurozone | Employment (QoQ) | Dec-23 | 0,3 |
| | Eurozone | Real GDP (QoQ) | Dec-23 | -0,1 |
| | Germany | Industrial Production (MoM) | Oct-23 | -1,4 |
| | Switzerland | Unemployment Rate (%) | Nov-23 | 2,1 |
| **08 December** | US | Consumer Confidence | Dec-23 | 61,3 |
| | US | Employment (000s) | Nov-23 | 150,0 |
| | US | Unemployment Rate (%) | Nov-23 | 3,9 |
| | Japan | Real GDP (QoQ) | Dec-23 | -2,1 |
| **09 December** | China | Inflation (YoY) | Nov-23 | -0,2 |
| **12 December** | US | Inflation (YoY) | Nov-23 | 3,2 |
| **13 December** | US | Federal Reserve Interest Rate (%) | Dec-23 | 5,5 |
| | Eurozone | Industrial Production (MoM) | Oct-23 | -1,1 |
| **14 December** | Eurozone | ECB Interest Rate (%) | Nov-23 | 4,0 |
| | UK | Bank of England Interest Rate (%) | Jan-24 | 5,3 |
| | Japan | Industrial Production (MoM) | Nov-23 | 1,0 |
| **15 December** | US | Industrial Production (MoM) | Nov-23 | -0,6 |
| | China | Retail Sales (YoY) | Nov-23 | 7,6 |
| | China | Industrial production (YoY) | Nov-23 | 4,1 |
| | Eurozone | Markit Manufacturing PMI | Dec-23 | 44,2 |
| | Eurozone | Markit Services PMI | Dec-23 | 48,7 |
| | UK | Markit Manufacturing PMI | Dec-23 | 47,2 |
| | UK | Markit Services PMI | Dec-23 | 50,9 |
| | Japan | Nikkei Manufacturing PMI | Dec-23 | 48,3 |
| **18 December** | Germany | Ifo Business Climate | Dec-23 | 87,3 |
| **19 December** | Japan | Bank of Japan Interest Rate (%) | Nov-23 | -0,1 |
| **20 December** | UK | Inflation (YoY) | Nov-23 | 4,6 |
| **21 December** | US | Philadelphia Fed Business Survey | Dec-23 | -5,9 |
| | US | Real GDP (QoQ) | Dec-23 | 5,2 |
| **22 December** | UK | Real GDP (QoQ) | Dec-23 | 0,0 |
| **29 December** | Switzerland | KOF Leading Indicator | Dec-23 | 96,7 |

# LET'S TALK ABOUT IT.

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This article was finalised on 30th November 2023.

## DISCLAIMER