Market Commentary
2nd Quarter 2023

Positive Stock Markets

Market and Economic Developments

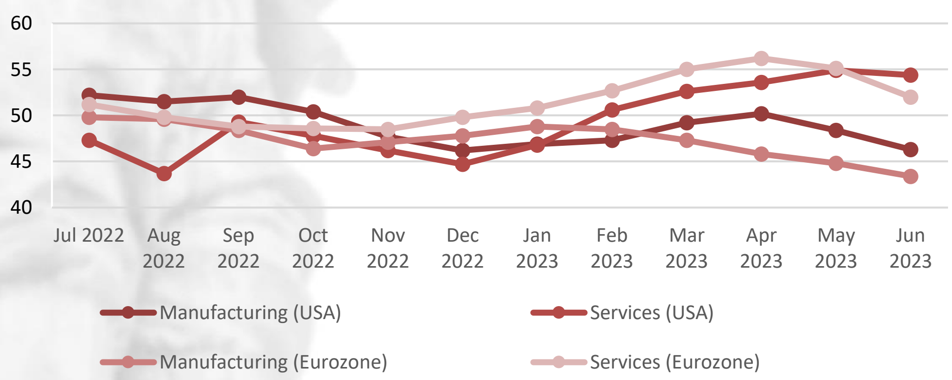
The stock market has enjoyed a remarkable first half of the year, despite some ominous clouds that have loomed over investors' horizons for a while. The Nasdaq 100, the US tech index, posted its best first half-year performance since its inception. The leading performers were especially the firms that capitalized on the hype around artificial intelligence (AI). On this side of the Atlantic, European stock markets also delivered solid half-year results.

Besides the rally in tech stocks, inflation also grabbed the headlines. It has decreased in most Western industrialized nations compared to the previous quarter, but still remains clearly above the 2 percent target. Consequently, central banks are hiking key interest rates. In the second quarter, the ECB and the Fed increased interest rates again sharply. It can also be observed that a significant portion of the decrease in inflation is due to declining energy prices. The intriguing question will be how they evolve in the upcoming winter. The latest labor market data from the US also presents a mixed picture. Fewer new jobs have been created than expected, yet workers managed to secure wage increases, which could fuel inflation further.

A look at China reveals a contrasting picture with Europe. China's economic engine is faltering, which is also reflected in the low inflation figures. Therefore, interest rate cuts are within the realm of possibility. An economic downturn in China would have far-reaching implications for Asia and the global economy. China is not only an exporting nation, but also the world's second-largest importer of goods.

A glance at the purchasing managers' indices shows that a positive sentiment persists in the service sector. This is not surprising, as price increases have largely been passed on to consumers so far. In the manufacturing sector, however, the mood is more subdued and the index lies below the 50 mark.

Figure 1: Purchasing Managers Indices (PMI)



Source: Refinitiv, Datastream as of 30.06.2023

Key Takeaways

- Tech stocks had a very successful first half of the year.
- Inflation is on the decline, although it remains above target.
- Central banks have announced further interest rate hikes to bring inflation under control.
- In our base scenario, we expect inflation to come back only slowly. In addition, we currently expect a technical recession of 1-2 quarters.
- China's economic problems could lead to distortions beyond the country's borders.

Monetary Policy

As discussed in the previous quarterly report, the battle against inflation is not over yet and will continue to challenge us in the upcoming quarters. By hiking key interest rates, central banks are attempting to cool down the economy and curb the price surge. The interest rate increases observed so far have already had some impact on inflation and have reduced it in most countries. However, the figures in both Europe and the U.S. are still well above the target range.

The market has factored in further interest rate increases until the end of the year so far. However, new information can quickly disrupt this consensus. For instance, labor market data from the U.S. still indicates an expanding economy with rising wages. Such developments can be perilous for central banks, as firms often pass on wage costs to consumers in the form of price increases, which fuels the current inflation dynamic and ultimately forces central banks to raise interest rates. Debt is also becoming increasingly costly again. Whereas a few years ago countries with a sound fiscal budget were still able to refinance themselves cheaply, in the current environment larger sums have to be allocated for interest rate payments. This affects not only governments, but also firms. They now have less capital available for new investments. Without these investments, the economic engine will eventually start to falter. The challenge for the central bankers will be not to bring the economy to a complete halt. Since the high interest rates can also be the downfall of firms whose growth ambitions were too high and who borrowed too heavily in the low-interest environment. Such firms now face the risk of going bankrupt. Therefore, careful due diligence during stock selection is more crucial than ever.

Another market that is especially affected by interest rate hikes is the construction and housing market. In particular, countries in which owners have financed their properties with low interest rates could face pressure. An example of this is the UK housing market, where the majority of the population owns their own homes. This can create a dangerous situation in which the central bank has to raise interest rates to control inflation, but at the same time the population starts to resist for fear of losing their homes due to the burden of ever higher mortgage rates.

If we look at the yield curve of various Western industrialized nations, we observe that long-term bonds (10 years) have a lower interest rate than short-term bonds (3 months). Therefore, the yield curve is inverted. Such an inverted yield curve is historically regarded as a reliable predictor for a recession. If we compare the performance of the S&P 500 with the US Treasury spread, we see that a negative spread has often been followed by a negative performance of the S&P 500.

Market Data

Equity Markets Perf.	2023
SPI	8.19%
DAX	15.97%
Euro Stoxx 50	12.53%
S&P 500	15.91%
Nasdaq 100	38.75%

Yield to Maturity of Government Bonds	in %
10Y Swiss Federal Bond	0.93%
10Y German Federal Bond	2.39%
10Y US Treasury	3.81%

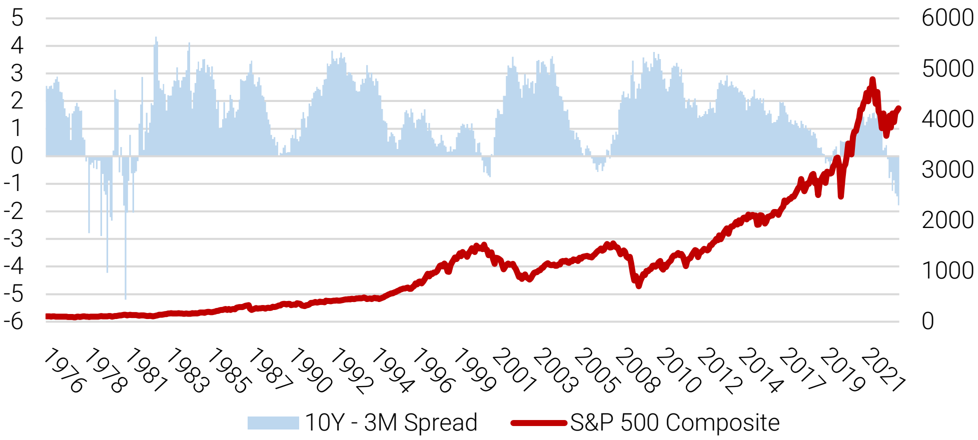
Gold (oz.) Perf.	2023
in CHF	1.90%
in EUR	3.21%
in USD	5.21%

Commodities Perf.	2023
Oil Brent	-10.71%

Year-to-Date (YTD) performance
in local currency, as of 30.06.2023

Source: Refinitiv, Datastream

Figure 2: US Treasury Spread and S&P 500 Performance



Source: Refinitiv, Datastream as of 30.06.2023

Financial and Capital Markets

As we mentioned at the beginning, tech stocks have performed particularly well this year. Especially the large firms in the Nasdaq led the rally, which lasted the entire first half of the year. Notably, for example, Nvidia, which reached a market capitalization of over one trillion. European technology stocks such as SAP also gained considerably.

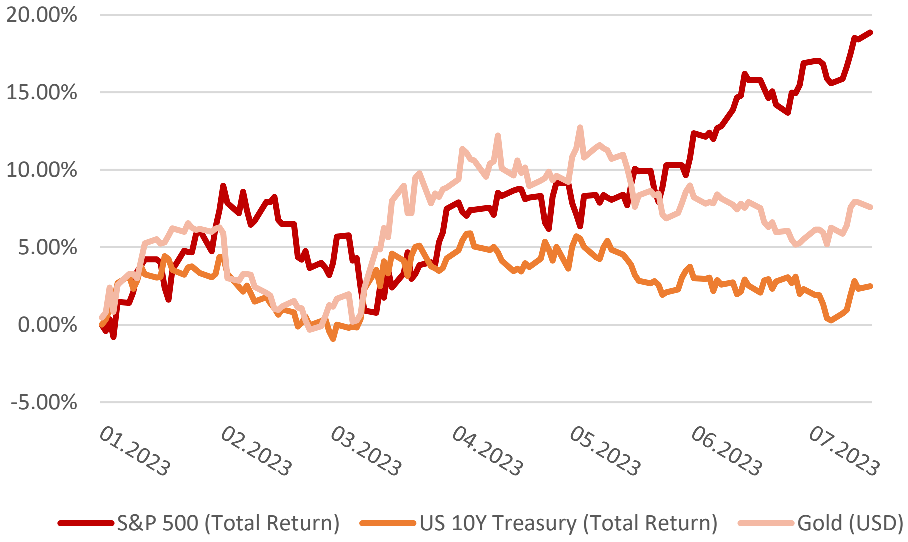
This development is rather counterintuitive, as technology stocks are considered growth stocks. In a rising interest rate environment, the expected future profits of these firms are discounted more heavily, which leads to a lower valuation. So far, no such correction has been observed. Rather, it seems that established technology firms are considered safer compared to conventional industries, even in uncertain times. In addition, developments in the field of artificial intelligence certainly favored the tech industry.

Until the middle of the second quarter, the positive performance of the S&P 500 was also driven by a few large stocks. This trend reversed slightly in June, as all sectors of the S&P 500 were able to achieve a positive performance. It remains to be seen how sustainable this development is.

A look at the currently high interest rates gives investors in short-term bonds more generous returns for their risk. However, if you want to invest your money in single bonds for the long term, the yields are comparatively meager. This is due to the market expecting lower interest rates as a result of lower inflation figures in the long run. However, if interest rates decrease more strongly than expected, for example due to economic turmoil, which triggers measures by central banks, capital gains might also be reaped on long-term bonds.

In the gold sector, the year started extremely well with the temporary high of over 2050 $ per ounce. Since then, the gold performance has been rather disappointing. This is because gold per se does not yield a return. If interest rates on bonds rise, gold becomes less attractive. However, if interest rates decrease and market volatility increases, the end of the year could be positive for the precious metal. Other commodities also lost noticeably in the second quarter. Oil in particular came decreased in value. How the oil price will evolve in the future depends largely on the economic development. Additionally, it is difficult to estimate how strongly the production cutbacks of individual oil producers will affect the price.

Figure 3: Performance of the S&P 500, 10-Year US Government Bonds and Gold



Asset Allocation

Asset Class	Positioning
Cash	Overweight
Fixed Income	Underweight
Equities	Weak Underweight
Gold	Strong Overweight

- We continue to buy bonds selectively, but maintain our underweight.
- Our stock selection remains unchanged. The stocks held to date have made a significant contribution to performance. Return chasing by buying the so far best-performing stocks is not expedient.
- After the stock rally in the first half year, price corrections become more probable.

Source: Refinitiv, Datastream as of 11.07.2023

Current Asset Allocation

Given the current market situation, we adopt a defensive stance. In line with this, we have bought bonds in various currencies again in the last quarter. However, there is still a slight bond underweight in all mandate currencies. This underweight is particularly evident in CHF mandates, as interest rates are not yet high enough in all market sectors to generate an adequate return after transaction costs.

Equities are also slightly underweighted compared to the neutral allocation. Within the asset class, U.S. equities particularly boosted the performance towards the end of the second quarter. However, we had to endure slight losses on our gold positions in the month of June. Nevertheless, we are still up year-to-date in this asset class. Bonds also dragged: As interest rates and interest rate forecasts have risen, bonds are now valued at a lower market price. As a result, this asset class also had a slightly negative impact on performance in the month of June.

Nevertheless, we are clearly up in all mandates year-to-date. The USD mandates in particular have performed well. Overall, we have been able to keep up with our competitors, who strategically hold a much higher equity quota compared to us. After a solid first half, we now eye the second half of the year. We are confident that our current positioning will enable us to navigate well in an uncertain market environment.

Figure 4: Current Asset Allocation

Asset Class	Balanced CHF
Liquidity	19%
Fixed Income	28%
Corporate Bonds Inv. Grade	11%
Government Bonds	9%
Inflation-Protected Government Bonds	10%
Equities	38%
Switzerland	11%
Europe incl. GB	8%
USA	10%
International	9%
Emerging Markets	0%
Precious Metals	15%
in percentages %	10 20 30 40 50 60 70 80 90 100

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