Market Commentary
1st Quarter 2023

Volatile First Quarter

Business Activity and Global Economy

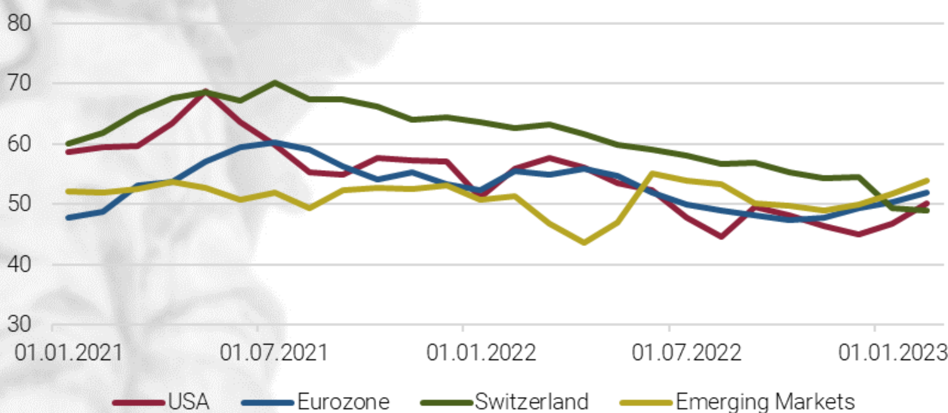
After a challenging 2022, investors took fresh courage in the first days of the new year which sparked an enthusiastic rally. After the initial advances however, renewed interest rate worries soon put an end to the good mood, and stock prices even tended to weaken again, before starting a rapid recovery towards the end of the quarter.

The interest rate hikes introduced by central banks to combat inflation claimed their first victims in March 2023, particularly in the financial sector. Regional banks in the USA in particular came under pressure, and it was not long before fears of a systemic crisis in the banking sector spread. Many felt reminded of the beginnings of the great financial crisis of around 15 years ago and tried to put their money in a safe place. Since in today's age of mobile and online banking, a few clicks are all it takes to transfer money from one institution to another, the media-effective queues in front of ATMs and bank branches were largely absent, but the shifts and flows of money within a short period of time were presumably greater than at any time since the financial crisis of 2008.

Against this backdrop, various governments and central banks have rushed to the rescue, seeing financial stability at risk. Central banks face a difficult trade-off. They consider further interest rate hikes to be necessary to curb inflation, but these could put additional banks in trouble. With the (rescue) operations carried out in March, the central banks ensured that they could implement their previously announced interest rate hikes without triggering a dangerous downward spiral.

Otherwise, some economic data surprised positively. For example, the purchasing managers' indices continued to recover and in March even exceeded the 50-point growth threshold in some cases. After inflation remained stubbornly above expectations in January, the situation eased to some extent in the course of the quarter, which was noted with pleasure by the stock markets.

Figure 1: Purchasing Managers Indices (Composite)



Source: Refinitiv, Datastream

Key Takeaways

- We anticipate a challenging economic environment this year.
- In our base scenario, we currently expect a moderate weakening of the economy.
- The interest rate hikes by the national banks have exposed weaknesses in the global financial system.
- We believe that central banks will primarily implement the interest rate hikes announced so far.

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Monetary Policy

To this day, central banks continue to fight inflation and put the announced interest rate hikes into practice.

The rise in interest rates observed since 2022 has also brought interest rates back to considerable levels in a longer-term view. Savers are receiving (at least nominally) attractive interest rates again for the first time in years, and bonds have almost been rediscovered as an asset class.

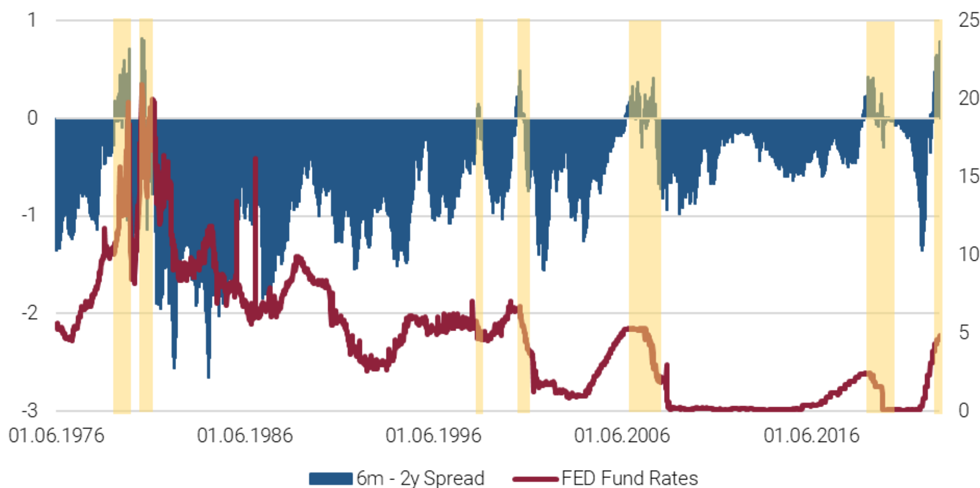
Recently however, a slight decline in yields to maturity was observed in the wake of emerging fears of a banking crisis. Yet, this is in stark contrast to the announcements made by the central banks, which are aggressively pushing for higher rates at the moment. On the contrary, further interest rate hikes this year have been announced or at least discussed. However, the market seems to have increasing doubts towards this sharp rhetoric, and certain market observers even expect interest rate cuts towards the end of this year.

In March, both the European Central Bank and the Fed in the USA and the Swiss National Bank raised their interest rates once again. As a result, the main refinancing rate in the euro zone is now 3.5%, in the U.S. it is (up to) 5%, and in Switzerland the key interest rate has recently also been increased to 1.5%.

Although the monetary policy makers continue to be cautious about an end to the cycle of interest rate hikes, the momentum in interest rate expectations has slowed noticeably. However, as long as inflation remains so markedly above the national banks' target, no rapid easing is to be expected. At the end of the day, the top priority for central banks must be to maintain price stability and thus ensure confidence in the monetary system.

As already explained in the last quarterly report, we expect central banks to primarily implement the interest rate steps currently priced in. The economic situation is too fragile to withstand further major interest rate hikes, but on the other hand, inflation has not yet been tamed either. That the current cycle of interest rate hikes is coming to an end could be concluded from Figure 2, because in the past a positive interest rate differential between the 6-month and the 2-year US Treasury was a fairly reliable indicator of this. In fact, this picture has become even more accentuated in the first quarter of the current year, signaling a soon but not imminent end to the tightening course.

Figure 2: US Treasury Spread and Fed Fund Rates



Source: Refinitiv, Datastream

Market Data

Equity Market Perf.	2023
SPI	5.91%
DAX	12.25%
Euro Stoxx 50	14.31%
S&P 500	7.50%
Nasdaq 100	20.77%

Yield to Maturity Government Bonds	in %
10Y Swiss Federal Bond	1.22%
10Y German Federal Bond	2.30%
10Y US Treasury	3.48%

Gold oz. Perf.	2023
in CHF	7.49%
in EUR	6.94%
in USD	8.86%

Commodities Perf.	2023
Oil Brent	-7.27%

In local currency, as of 31.03.2023
Source: Refinitiv, Datastream

Financial and Capital Markets

The start to the investment year 2023 was very good and, in particular, stocks that had fallen sharply in value last year, recovered significantly in the first trading days of this year. However, this phase of strong price gains was short-lived. Nevertheless, many stocks were able to stabilize at higher levels. As a result, the stock markets as a whole became more expensive, measured in terms of common valuation ratios, which then also curbed investors' enthusiasm to buy more.

From mid-January to the end of February, for example, the Swiss stock market trended more or less sideways, before prices came under pressure at the beginning of March. In the wake of decisive intervention by governments and central banks, especially in the USA and Switzerland, in connection with an emerging banking crisis, investors regained their courage and the major indices rose sharply again at the end of the quarter.

Bond prices have also had a volatile quarter, with a sharp rise in line with equity markets at the start of the year, a setback in February against a backdrop of stubbornly high core inflation rates, and a renewed decline caused by investors seeking a safe haven in the context of the recent banking turmoil.

After a weak February, gold was able to advance close to all-time highs and is up 8.86% in USD terms since the beginning of the year.

Although we have had a very eventful first quarter, the returns since the beginning of the year have been encouraging. Bonds as well as equities and gold have gained in value.

Asset Allocation

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

- In bonds, we continue to buy selectively but still maintain an underweight.
- In equities, we positioned ourselves at the end of last year and made only a few changes in the first quarter of 2023.
- In general, the market reality was largely in line with our expectations, which is why only few portfolio adjustments were necessary.

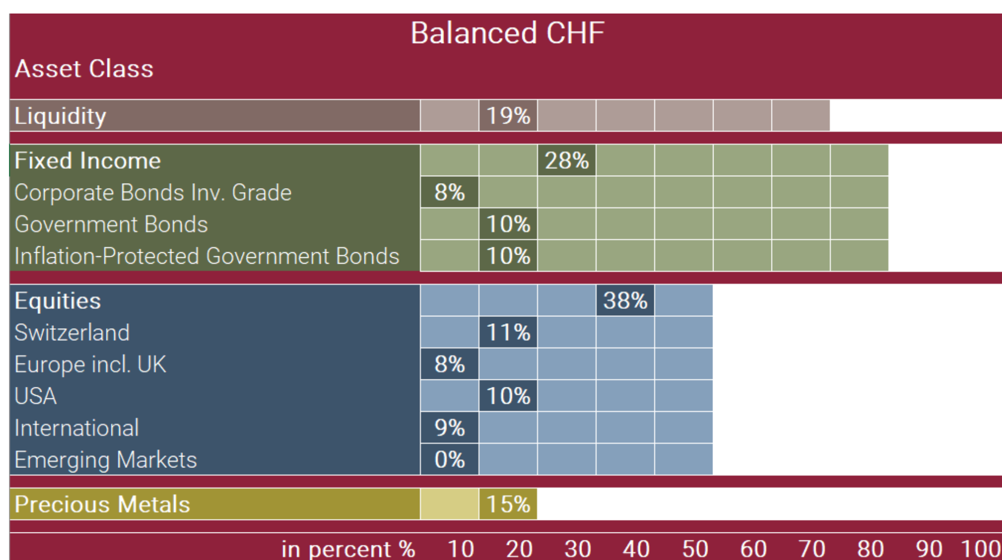
Figure 3: Performance of S&P 500 and 10-Year US Government Bonds

Source: Refinitiv, Datastream

Current Asset Allocation

In our asset management strategies, we continue to be defensively positioned. After increasing our bond allocation once more in the last quarter of 2022 and repositioning ourselves in equities, we carried out only few transactions in the new year, as the first quarter of 2023 was in line with our expectations in many respects. Currently, we are still slightly underweight in equities and hold a more substantial underweight in bonds. However, a substantial part of the bond underweight is invested in gold. This diversification has paid off in the first three months of this year.

Since the beginning of the year, our strategies are comfortably up in all three main currencies. We feel well positioned with the current alignment of our portfolios. However, we are constantly reviewing a further increase in the bond quota, and our underweight there has also become significantly smaller in the meantime, also depending on the base currency. In our CHF mandates, the underweight is still most pronounced, as the expected returns after trading costs only partly compensate for the risks taken. However, if interest rates and credit spreads rise, further purchases are planned. In equities, too, the goal is to increase the allocation to neutral, but we currently feel very well positioned with the slight underweight and, above all, the quality-focused implementation of our equity allocation.



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