

PROBUS  PLEION

Monthly newsletter

September 2023

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Contents

- 2 Editorial
- 3 Assessment of the economic situation
- 4 Financial markets over the month
- 5 Comments on investment decisions
- 6 Performance summary
- 7 Contacts & disclaimer

EDITORIAL

Recession or stagflation ?

Economic growth

It takes two consecutive quarters of GDP decline for the NBER (National Bureau of Economic Research) to report that the USA is in recession. (see chart below) Although growth has been close to zero since the economy's flash crash in March 2020 (COVID), it has since returned and should remain so in 2024. In Europe, industrial activity figures are contracting, while services have remained positive until recently.

Emerging markets and energy

The economic slowdown in China is particularly penalizing Germany, which mainly exports to the country. On the other hand, Latin American countries and the USA are benefiting from the adaptation of their means of production and raw materials exports. Although India currently benefits from an access to cheaper oil energy, it is nonetheless confronted with inflation on certain basic goods, such as tomatoes. Today's world is totally inter-connected, and we realize that

we are not in an orderly crisis, but in a sprawling, diffuse one, where inflation is favorable to certain geographical areas or economic sectors.

Stagflation

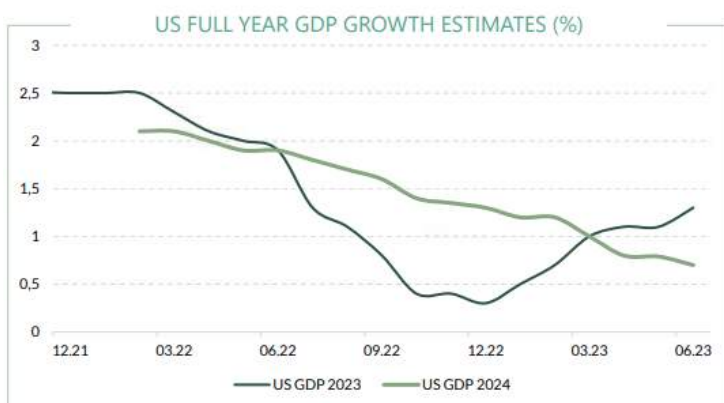
A country's economic situation characterized by stagnating activity and production, and rising prices. Consumers are obviously worried about it. The job market is shrinking, while all costs - housing, food, leisure, etc. - are rising.

Where are we now?

Inflation in the USA has fallen sharply from its peak in 2022. In Switzerland, it is at 2020 levels. In Europe, inflation has also fallen from its peaks, but still appears to be at high levels, with energy imports and other factors still weighing on prices. With the US unemployment rate at 3.5%, the job market remains strong.

What consequences can we expect on the markets?

Take advantage of the inversion of the curve to put cash at work. Quality government and corporate bonds pay well and mitigate the impact of inflation.



Benoît Derwael

Head of Investment Solutions



Assessment of the economic situation

The financial health of listed companies in the second quarter is better than expected. In the absence of any major news during the summer period, tourism is running at full speed, boosted by high oil prices.

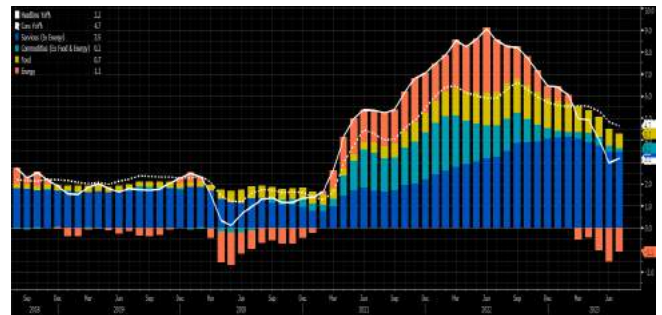
The crisis in China continues

We are always talking about the USA, and rightly so: it is the most open economy and its currency accounts for 70% of world trade. However, when China has a cold, the rest of the world can suffer too. After the various sanctions imposed on its major new-economy leaders, the Communist Party did not expect to have to carry the real estate sector for so long. The reopening of Evergrande's listing after 18 months at -80% shows just how far the problem has gone. Everyday, China announces "small measures" to improve its economic situation. A massive plan would certainly be more welcome. But do they still have the means?



Inflation eases in the economic data

While inflation is falling significantly in the aggregates, at household level, the price of bread, gasoline at the pump or soda on a seaside terrace have all skyrocketed. The autumn will be another test for some governments. The recent rise in the Brent crude from USD 68 to USD 86 will not help. Currently, OPEC members are reducing production in line with demand.



Jackson Hole

No surprise there, as the major financial powers repeated their previous speeches. Still intent on slowing, curbing or halting inflation by raising short-term interest rates. Analysts interpreted these messages as opening the door to a further increase between now and the year-end. Probably November. Since the curve is always inverted, a recession is often the solution for a return to normal. It is a good thing that some recessions do not lead to a market crisis, especially one so eagerly awaited.

Region: United States		Instrument: Fed Funds Futures			
Target Rate	5.50	Pricing Date	08/29/2023		
Effective Rate	5.33	Cur. Imp. O/N Rate	5.329		
Meeting	#Hikes/Cuts	%Hike/Cut	Imp. Rate Δ	Implied Rate	A.R.M.
09/20/2023	+0.142	+14.3%	+0.036	5.364	0.250
11/01/2023	+0.487	+34.4%	+0.122	5.450	0.250
12/13/2023	+0.424	-6.3%	+0.106	5.435	0.250
01/31/2024	+0.215	-20.9%	+0.054	5.383	0.250

Source: Gama Asset Management

What about the new wave of COVID?

The US removed Covid-19 from pandemic emergencies in May 2023, reducing the number of accurate statistics. However, hospitalizations for respiratory emergencies rose significantly in mid-August (+24%). The new BA.2.86 variant is also spreading in

Europe. This comes at a bad time for the back-to-school season. On the other hand, it has enabled the "Moderna" and "BioNtech" companies to return to the forefront with substantial rebounds of 10%.



Financial markets over the month

After a positive July, the market consolidated in August. Profit-taking, low volume and the FED's ever-watchful eye on economic data left the door open to a further rate hike(s).

Techno stocks rebound again...

Depending on period observed, performances can be misleading. While the Nasdaq 100 has gained 40% since the beginning of the year, it is still negative since January 1, 2022, just behind the S&P500. In contrast, Nvidia has gained over 65% in the last 20 months. The graphics card manufacturer is now the figurehead of artificial intelligence. It has just reported excellent quarterly results, and this has supported the entire technology sector. The slowdown in its gaming segment was largely offset by the boom in data centers, used for cloud and computational/artificial intelligence models.

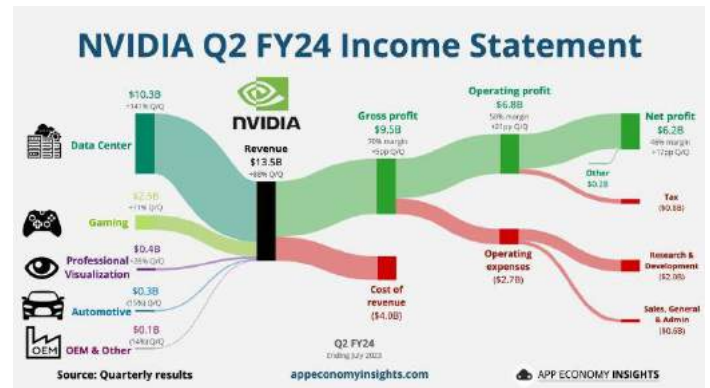
The US 2-year rate briefly dipped back below 5%.

The yield curve remains inverted in Europe and in the US. The rebound in short and long rates is due to renewed inflation and buoyant employment. However, the smooth exit from the curve inversion is taking shape, with a slight rise in long yields (10 years) and stabilization in short yields. With US inflation at 3%, above the 2% target, the FED should agree to see benchmark rates cut by at least 1% in 2024, as the market expects. We believe that inflation will find it difficult to fall below 3% in the near future, which is why short rates should remain around 4.5%.

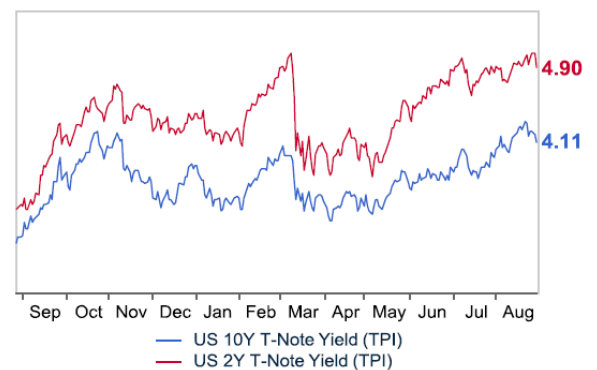
Inflation-linked bonds and gold

Following the rise in US real interest rates since the end of 2021, US TIPS (Treasury Inflation-Protected Securities) have fallen by around 18%. In this inflationary environment, we might have thought that this type of investment would have provided with a better protection. Historically, US TIPS and gold have been correlated. However, this correlation has recently been challenged. Despite this rise in real rates, gold has held up well. This is largely due to purchases of the yellow metal by central banks in order to progressively de-dollarize and maintain reserves in the face of the ongoing war in Ukraine. In a scenario where inflation could stabilize at higher levels, US TIPS offer good protection at these levels.

AI relaunches technology with Nvidia as messenger



US 2 and 10-year yields over 12 months



Recent trends scattered between gold and TIPS (black)





Our convictions

		Current Conviction	Last Outlook	Upgrade/Downgrade	Comment
Equity	US Equity	Neutral	Neutral	→	
	EU Equity	Neutral	Neutral	→	focus on multinationals
	Swiss Equity	Neutral	Neutral	→	
	Japanese Equity	Favorable	Favorable	→	buy the dips
	Chinese Equity	Neutral	Neutral	→	
	Asian EM	Neutral	Favorable	↘	wait for positive trigger
Fixed Income	Cash & Short term debt	Favorable	Favorable	→	
	US Long term debt	Neutral	Neutral	→	
	EU debt	Neutral	Neutral	→	
	DM High Yield	Neutral	Neutral	→	
	EM Debt (Local)	Favorable	Favorable	→	favor LATAM
	EM Debt (Hard)	Unfavorable	Neutral	↘	favor local currencies
	Floater	Neutral	Neutral	→	focus on short maturities
Alternatives	Precious Metals & Miners	Favorable	Neutral	↗	buy the dips
	REITs (EU + CH)	Favorable	Favorable	→	favor residential
	Hedge Funds	Neutral	Neutral	→	

Comments on investment decisions

Investor positioning is around 50% equities. During the second quarter, institutional investors increased their equity weightings, but more recently, have reduced them. The market has been affected by these decisions in low volumes. Our neutral/defensive approach is justified.

Equities

We remain underweight equities, despite a recent buyback of US equity indexes following the mid-August drop in share prices. Valuations remain generous in the US and Switzerland, but are more attractive in Europe, and even more so in Japan and Asia. Despite various « mesurette », China remains the most affected index this month. The recovery from the real estate crisis is taking time. From a technical point of view, while the SMI and Eurostoxx50 are under a strong resistance, the S&P500 is in the middle of its monthly uptrend channel since 2009 and, in the short term (daily), is using its 50-day moving average as support: 4450.

Bonds

In USD and EUR, the sharp inversion of the curves still does not encourage us to take on too much duration, given the particularly attractive yields for short maturities. As for credit spreads, they remain low-yielding, which means we can maintain our positioning on quality companies (IG). In emerging debt, the risk/return profile of local-currency debt remains more attractive than then USD-denominated

debt, as credit spreads have also narrowed.

Precious metals, listed real estate(REIT)

With the volatility of interest rates, listed real estate has suffered from this uncertainty, but on the whole, we are seeing a certain status quo. New construction of single-family homes in the US continues to sell off, while the overstock of homes is shrinking.

Currencies

The US dollar index (DXY) is back above 103 (200-day moving average), with extreme negative positions on the USD being reduced. We will await the British and European central bank meetings at the end of September to see whether the continental currencies strengthen against the USD in a more structural way. CHF remains sought-after, but more neutral this month against EUR and USD.



Performance summary

Equity performance

Ticker	Equity Indices	Last	1m Return (%)	YTD Return (%)	1y Return (%)
SMI Index	SWISS MARKET INDEX	11126	-1.6	3.7	2.5
SXXP Index	STXE 600 (EUR) Pr	458	-2.8	7.8	10.4
CAC Index	CAC 40 INDEX	7317	-2.4	13.0	19.5
DAX Index	DAX INDEX	15947	-3.0	14.5	24.2
UKX Index	FTSE 100 INDEX	7439	-3.4	-0.2	2.1
SXSE Index	Euro Stoxx 50 Pr	4297	-3.9	11.6	22.2
INDU Index	DOW JONES INDUS. AVG	34722	-2.4	4.8	10.2
SPX Index	S&P 500 INDEX	4508	-1.8	17.4	14.0
CCMP Index	NASDAQ COMPOSITE	14035	-2.2	34.1	18.8
RTY Index	RUSSELL 2000 INDEX	1900	-5.2	7.9	3.0
TPX Index	TOPIX INDEX (TOKYO)	2332	0.4	23.3	18.8
XIN9I Index	FTSE CHINA A50	12602	-5.3	-3.1	-7.2
MXWD Index	MSCI ACWI	686	-3.0	13.3	11.9

Performance of bonds, currencies and commodities

Ticker	Fixed Income Indices	Last	1m Return (%)	YTD Return (%)	1y Return (%)
SBR14T Index	SBI AAA-BBB	128	0.6	4.4	1.8
LBEATREU Index	Euro-Aggregate	228	0.3	2.7	-2.3
LBUSTRUU Index	U.S. Aggregate	2077	-0.6	1.4	-1.2
LEGATRUU Index	Global Aggregate	449	-1.4	0.7	-0.1

Ticker	Currency	Last	1m Change (%)	YTD Return (%)	1y Return (%)
CHF	CHF	0.883	1.3	-4.4	-9.6
EUR	EUR	1.084	-1.4	1.3	7.8
DXE INDEX	DXE	103.62	1.7	0.1	-4.7
GBP	GBP	1.267	-1.3	4.9	9.0
JPY	JPY	145.540	2.3	11.0	4.7
CNY	CNY	7.259	1.6	5.2	5.3
CAD	CAD	1.351	2.4	-0.3	2.9
AUD	AUD	0.648	-3.5	-4.8	-5.2
BRL	BRL	4.955	4.8	-6.2	-4.4
INR	INR	82.785	0.6	0.1	4.2
MXN	MXN	17.038	1.8	-12.6	-15.4
EURCHF	EURCHF	0.958	-0.1	-3.2	-2.5

Ticker	Commodity	Last	1m Change (%)	YTD Return (%)	1y Return (%)
XAU Comdty	Gold	1940	-1.3	6.4	13.4
XAG Comdty	Silver	24.44	-1.2	2.0	35.9
CL1 Comdty	WTI	83.63	2.2	4.2	-6.6
HG1 Comdty	Copper	377.25	-5.9	-1.0	7.2
BCOMIN Index	Industrial Metals	142.74	-5.1	-13.7	-7.0
BCOMAG Index	Agriculture	66.58	-1.9	-3.3	-3.8

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