AquilaFlash

Review of 2023 – Outlook for 2024

Focus: In 2023, industrialized country central banks raised interest rates repeatedly while numerous geopolitical tensions came to the fore. The conflict in Ukraine will soon have lasted two years. In addition, tensions in the Middle East have recently been exacerbated by the war between Israel and Hamas. So far, an escalation of this conflict to neighboring Arab countries has, by and large, been avoided. Geopolitical tensions will likely remain an important factor in the coming year. However, in the past the impact of such tensions on markets has often been short-lived. Economic weakness is evident in two of the heavyweights in global trade, China and Germany. Not surprisingly both are key trade partners for Switzerland. Global trade flows are slack.

Global economy

Falling inflation, but still above the central banks' 2% target in many countries

Central banks in the US and Europe (including Switzerland) have continuously tightened monetary policy to combat inflation and have repeatedly disappointed market hopes of an imminent end to the cycle of interest rate hikes. Those interest rate hikes have reduced imbalances in the goods and labor markets and have helped to lower price pressures. A favorable base effect, particularly in energy costs, has contributed to a significant reduction in broad measures of inflation in recent months. Central banks are scarred by their experience of the early 1980s, when they cut rates prematurely and had to reverse course drastically as inflation spiked again. They will be cautious when it comes to initiating a series of interest cuts. We don’t expect these before the second half of 2024.

A resilient US economy

The US economy has been surprisingly robust in the face of unusually high inflation and the sharp rise in interest rates. Annualized growth as high as 5.2% is now estimated for the third quarter. Consumption has been fueled by savings built up during the pandemic and government stimulus packages. A shortage of skilled labor and record-low unemployment supported job security and consumer sentiment - although higher wages also contributed to inflation. Some weakening of demand, also in the labor market, suggests the tightening cycle may be at an end. Given the extent to which interest rates have already risen and the Fed’s decision to hold rates steady in December, markets now view interest rates as having peaked.

The German economy is weak

Germany has slipped into recession. Relatively high inflation, which has sapped purchasing power, higher interest rates and consequently higher financing costs are having a major impact on the economy and, above all, the property sector. Leading indicators suggest little growth momentum And Budget constraints indicate little or no scope for stimulus from the government sector. As Germany is the largest economy in the single-currency area, weakness there has an impact on the entire Eurozone as well as on Switzerland. Estimates for Eurozone growth in 2023 are around just 0.5% with only a slight recovery expected in 2024.

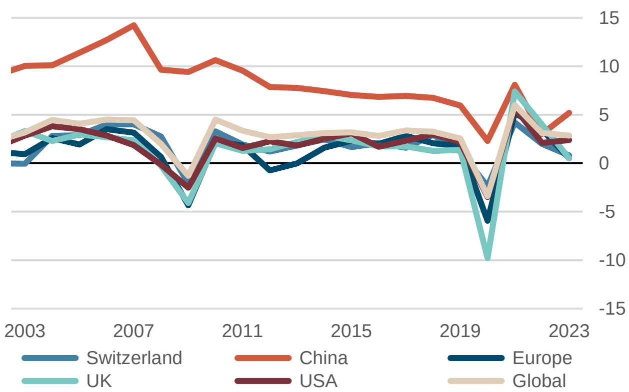
Switzerland

With two of Switzerland's major trading partners, China and Germany, weak there is a lack of stimulus from foreign trade and leading indicators from industry and services point to a continuing slowdown. Thanks to favorable developments in the labor market private consumption remains supportive for the economy. However, sharply rising health insurance premiums and another round of rent increases are weighing on purchasing power and, hence, on the outlook. Despite this, indicators suggest a slight acceleration in growth in Switzerland during 2024.

China is struggling with several problems simultaneously

Record-high youth unemployment, the collapse of a chronically overheated property market, a rapidly ageing population and the disappointing reopening of the economy after the pandemic have combined to dash hopes of a strong economic upturn and have also held back global growth. Substantial measures of stimulus are expected from the China's government and her central bank in 2024.

Annual growth in gross domestic product



Source: Bloomberg Finance L. P.

Equity and commodity markets

Marked variation in stock market performance

After a very poor 2022, there were already hopes last winter for a bounce in 2023. And indeed, most equity markets are about to end the year with a positive performance, albeit with significant variation by country, region and sector. Large-cap growth stocks were favored, while defensive, "value" stocks went out of focus. Stock prices fell in the third quarter as hopes of a "pivot" in interest rates faded. Thereafter, favorable inflation data and signs of an end to the US rate-tightening cycle triggered a rally in the closing weeks of the year. Few expect a strong economy in the near term and investors are weighing the implications of this for earnings growth, the outlook for interest rates and whether near-term prospects justify current valuations. We recommend keeping the equity allocation close to the strategic quota and favor defensive stocks, including the attractively valued Swiss market.

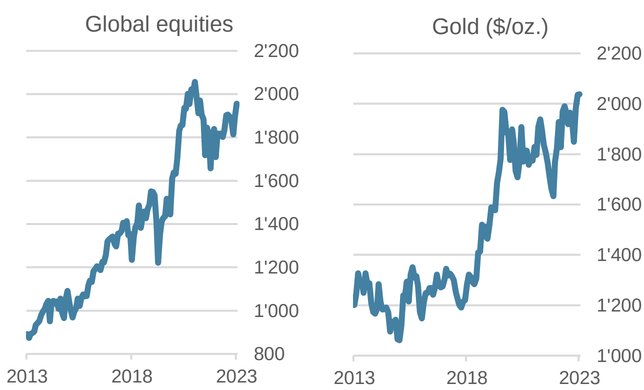
Commodities in a rollercoaster of economic fluctuations and geopolitical tensions

In the second half of 2022, following Russia's invasion of Ukraine, fears of a winter energy crisis were intense and prices spiked. As these fears dissipated, energy prices, especially European gas prices, normalized. Today, war in the Middle East threatens to destabilize the world's energy supply again while OPEC+ (Organization of the Petroleum Exporting Countries plus, in particular, Russia) wants to expand its influence by inviting new producer countries such as Brazil.

Despite higher real interest rates, gold was able to cushion price losses in the context of ongoing international tensions. Finally, a price recovery set in during the fourth quarter, supported by speculation of an end to the rate-tightening cycle, and this recovery took the precious metal back to previous highs.

We expect energy prices to remain stable or to rise slightly in 2024. We expect gold to reach new highs as key interest rates fall.

Performance of equity and commodity markets



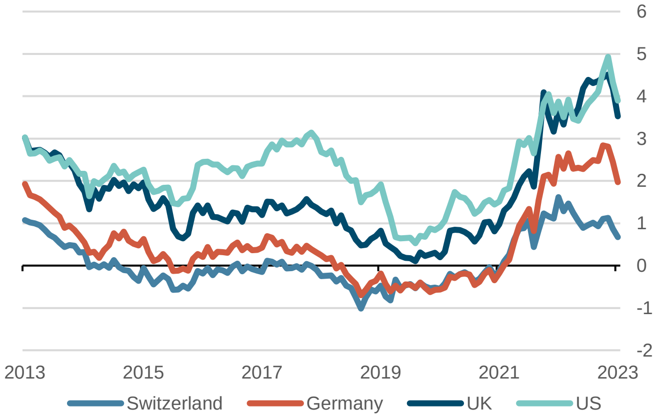
Source: Bloomberg Finance L. P.

Foreign exchange and interest rate markets

Monetary policy is being eased

With policy rates thought to be at their peak, bonds have once again become a viable asset class - even if the recent fall in long-term yields undermines the attraction of long-term issues. The yield on corporate bonds, for example, is around 1.3%. The situation is quite different for US dollar bonds, where yields of over 5% can be achieved. For Swiss investors, however, we advise against taking any foreign currency risks with bonds and favor corporate bonds with medium maturities and government bonds with longer maturities.

10-year government bond yield



Source: Bloomberg Finance L. P.

The attraction of safety

The Swiss franc remains the crisis currency par excellence. This feature is particularly evident in the EUR/CHF exchange rate. While the franc is sought in connection with geopolitical uncertainties, the euro is weakening due to challenging economic conditions in the Eurozone. Meanwhile, the US dollar has recently depreciated significantly. The Swiss franc is has risen to the top. We expect it to stay strong.

Investment Strategy 1st Quarter 2024

Meeting of the investment advisory commitee 27.12.2023

	Asset class	Income	+/-	Balanced	+/-	Growth	+/-	Capital gain	+/-
		Investment Strategy							
Defensive	Liquidity	8%	0%	7%	0%	7%	0%	7%	0%
Defensive	Fixed Income incl. Bond Funds	60%	0%	35%	0%	15%	0%	0%	0%
Offensive	Stocks incl. Stock Funds and ETF	25%	0%	50%	0%	65%	0%	80%	0%
Offensive	Others Real Estates, Commodities, Gold, Structured Products, Alternatives	7%	0%	8%	0%	13%	0%	13%	0%
		100%		100%		100%		100%	

Additional parameters

Reference currency CHF

Currency allocation

CHF	min.	50 %
EUR	max.	20 %
USD	max.	20 %
GBP	max.	15 %
Other	max.	20 %
	(max 10 % per currency)	

Variations +/- 5 % are possible for the various investment categories.

The fourth quarter of 2023 was characterized by the conflict between Israel and Hamas. Once again, the geopolitical risks have increased. This also had a noticeable impact on the performance of the stock markets. They temporarily lost more than 6% of their value in the course of 10 days. The ongoing war between Ukraine and Russia put further pressure on the situation.

In general, however, 2023 was a positive year for the stock markets. Falling interest rates had a positive impact on share prices, but also on bond quotations. The key stock markets recorded double-digit percentage growth (USA S&P 500: 24.2%, Euro Stoxx 50: 19.2%, Nikkei 225: 28.2%). The only exceptions were the SMI and the FTSE 100, both of which increased by 3.8%.

The Swiss franc once again asserted itself as a crisis currency. The uncertainties worldwide and the challenging conditions have led to a flight into the CHF.

In the current year, the challenge remains to lower inflation to the desired level and to prevent a recession as much as possible. We are expecting further interest-rate cuts by the central banks in the second half of the year.

We wish you a Healthy and Successful 2024.