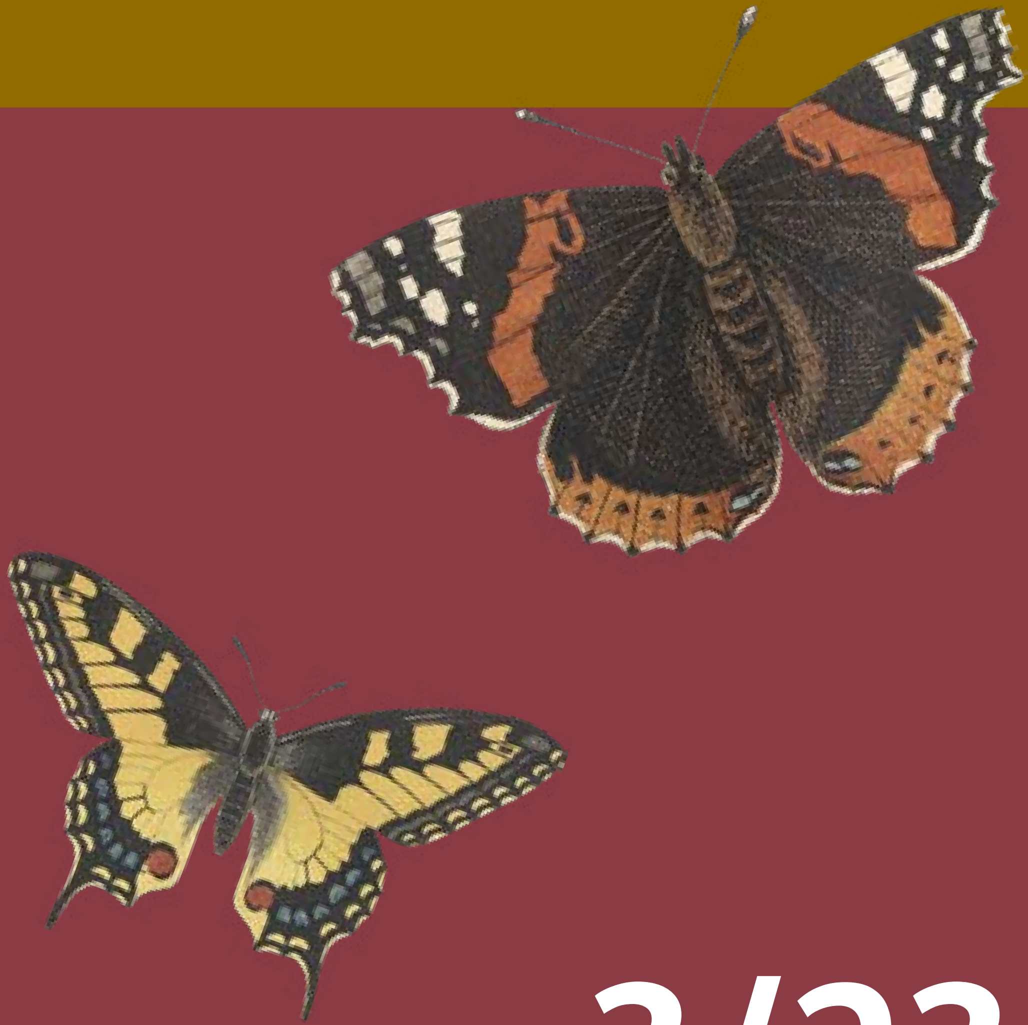
Investmenttrends 3rd quarter 2023



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Market outlook from ONE Asset Management AG

Investmenttrends 3rd quarter 2023

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ONE® Asset Management

01/ Equities

The last quarter was consistently „green“ on the stock markets. However, performance in the regions has varied widely. Central banks obviously had a major influence on price performance: the more muted their restrictive stance became, the better the stock markets in the countries performed (with the exception of China and Hong Kong, where this influence was overshadowed). Accordingly, among the largest indices, Japan posted the strongest performance, up 18%, followed by the U.S. indices, where the broad S&P 500 gained around 7%. Europe, on the other hand, lagged behind under the impression of a restrictive ECB. The Euro Stoxx 50 gained just some 2%.

The banking crisis in the US, which had caused a brief but sharp setback in March, quickly dissipated at the beginning of April. A positive trigger were interest rates, whose buoyancy ultimately came to a halt. The Dax also took advantage of the tailwind from the technical and fundamental side and set new records - as described in our last Quarterly Outlook. At the same time, however, a number of issues remained unresolved, with the result that the German market was unable to sustain its upward momentum. At the end of the quarter, it finished at the level of early April.

This constellation could remain until new facts are established. There are also no harbingers of violent movements in chart terms. The Dax index fluctuated 800 points in the second quarter. At the extreme points of the trading range, the bulls but also the bears were regularly trapped. That is, a new record was regularly sold off. Optimists who still wanted to jump on got a bloody nose.

Technically speaking there is only a clear fresh buy signal when the German benchmark index Dax can overcome its old record high with significance in temporal or point terms. At the same time, however, a clear new low is missing, which could be interpreted as a sell signal. In this phase, we trust in stock selection and swim with the overall market if the factual situation changes sustainably.

Though the momentum in the German stock market has weakened. Even as the index record was pushed up a little further in the course, as we expected. After Germany found itself in a technical recession in the winter, and also in view of the inflammatory material in energy policy, among other things, this is quite remarkable. However, new highs were sold off in each case, but in the end no sustainable pressure wanted to emerge either. The same time, the „fear barometer“ VDax remains at a very low level, so that bargain hunters repeatedly used the setbacks as good buying opportunities.

Also, the geopolitical situation has recently come to a head once again. The implied mutiny of the „Wagner“ troops, who set off for Moscow, ended just as quickly as it had begun. Nevertheless, the action is likely to leave its mark. Putin appears weaker than ever before. Uncertainty is rising. Hardliners may gain further influence in the future which would elevate the risks. But there is also a chance of moderation and an approaching end to the ongoing war in Europe to muten things.

In parallel with the mock coup, representatives from many countries gathered for an informal peace summit in Denmark to discuss the future of Ukraine. Also, at the table were previously ambiguously positioned countries such as South Africa, Brazil and India. Whether the situation will deteriorate further in the new quarter or whether the first steps towards peace will actually be taken is completely up in the air. The markets initially reacted in a correspondingly balanced manner.

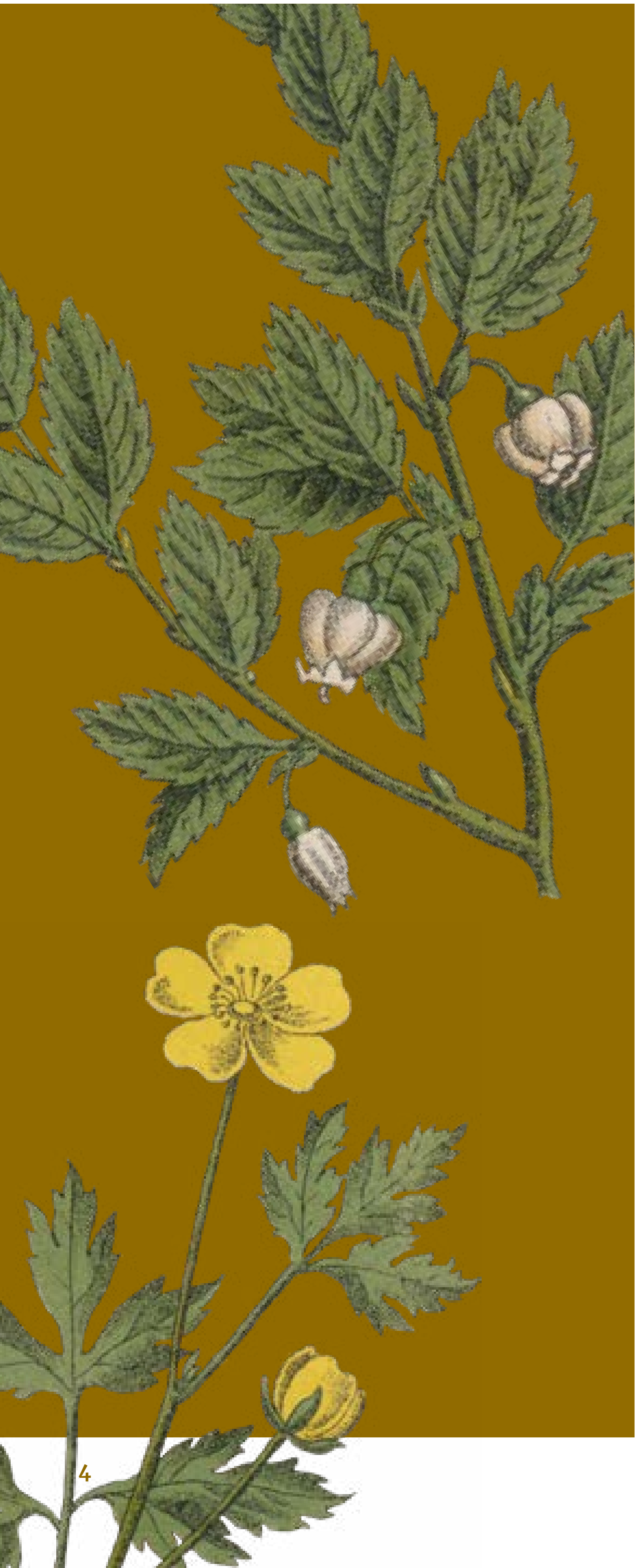
In the meantime, the negative harbingers for the European economy are accumulating. The purchasing managers‘ indices have recently disappointed. This time, even the service sector, which had previously shown resilience, has stumbled. In Germany, a disappointing ifo index is another warning signal. Its slump was caused in particular by a decline in Business expectations and the current conditions also deteriorated. Prospects for a recovery in the second half of the year, out of the technical recession in winter, seem at least less certain for Germany with these data.

On the market, the card “economy” is repeatedly played negatively. One reason is the tepid Chinese economy, which has fallen well short of expectations on its return from the long pandemic break. The government of this huge country will now counter this again with additional fiscal stimulus. But deep-seated problems are also becoming apparent. For example, deflation risks are being discussed, which could further cripple China. Pessimism about the growth outlook is high. From the relatively lower level, however, there may be positive surprise potential again in the coming months.

Inflation remains a hot topic. In general, price developments are losing momentum. This is partly due to high base effects, but also to the weak economic outlook. For example, the world‘s leading central bank, the Federal Reserve in the US, paused its rate hike series in the summer. Nevertheless, the overall expectation of monetary policy in the Western countries has become more hawkish once again. Still the market is unperturbed in its expectation of a near peak in interest rates.

Whether the interest rate peak will be 0.25% higher or lower seems to be perceived as less relevant. Meanwhile, initial interest rate cuts discussed for the U.S. at the end of March before the end of this year have been priced out again. We expect a near interest rate peak, but with a long plateau phase.

01/ Equities



Looking ahead to the domestic reporting season, a number of companies, particularly from the cyclically sensitive chemicals sector, have already jumped ahead with bad news. They have somewhat curbed the high market expectations. Morgan Stanley also deduces dangers for the large European capital goods providers, which often follow the chemical sector. Siemens Energy, for example, promptly came to the market with a warning - but one that was home-grown due to quality deficiencies in its wind power business.

Analysts now also expect further negative news in cyclical sectors such as chemicals. In general, however, the market is expecting significantly more positive quarterly reports. Warburg, for example, sees almost three times as many companies with positive surprise potential in its universe of stocks than with negative ones. This is more of a potential risk for the stock markets. However, the indices are proving resilient, despite the enormous fluctuation in individual stocks. This results in a sideways phase, which should continue.

02/ Bonds

The Federal Reserve has taken a pause in its cycle of interest rate hikes for the time being. Nevertheless, the central bankers have once again become more cautious. The dot plots, which reflect the expectations of the FOMC members for their most important parameters, are once again more negative and suggest that two more hikes are likely before the interest rate peak. Fed Chairman Jerome Powell nevertheless did not allow himself to be pinned down to a new rate hike in July. Visibility remains extremely low for the monetary authorities. Fed & Co are driving on sight.

The difficult situation of the central banks is illustrated by the latest interest rate decision by the Bank of England, which is playing a pioneering role in the current interest rate cycle. It had to increase the pace of interest rate hikes again after a surprisingly hot inflation figure. Other central banks, such as in Australia and Canada, also had to quickly end their interest rate pauses again due to persistently high inflationary pressure. Uncertainty about the price trend remains correspondingly high. After the initial misjudgment of inflation as a temporary phenomenon, there is still a need to catch up. However, the tight monetary policy will increasingly put pressure on the economy in the future and thus also affect the labor markets. This will make the job of central bankers even harder.

In order for the ECB to also take a break in September like the Fed did, core inflation would have to fall every month of this quarter, Council member Pierre Wunsch currently drew in new guard rails. Otherwise, the European monetary guardians would have to stay on their interest rate hike path. Martin Kazaks of the Latvian central bank signaled that interest rate cuts would only be possible again when the inflation rate falls below 2%. Overall, the ECB's communication thus remains hawkish, which also remains remarkable in view of the numerous doves on the Governing Council. They are keeping a very low profile. None has spoken out against a rate hike in July. However, dovish members like Chief Economist Philip Lane do not want to commit to September yet.

In Europe inflation numbers calmed down all-in-all and prices seem to be leveling off. The issue could then lose some of its steam if this trend continues. But core inflation still stays (too) high. A look at slumping retail sales shows that inflation is not being absorbed by wage increases. Consumers will therefore have to save more. Accordingly, companies can no longer raise prices slightly without weighing heavily on demand. This should keep inflation in check for the time being.

The Federal Reserve has paused its series of 10 rate hikes since March 2022. Its tone was somewhat more hawkish then expected, though. The likely magnitude of pending rate hikes, as indicated by dot plots, is larger than thought. This reinforces our assumption that the Fed remains committed to fighting inflation and does not intend to start cutting rates anytime soon. Given the continued tight labor market in the US, we maintain our expectation of a prolonged interest rate plateau.

In the UK, inflation remains hot and pressure from the Bank of England is accordingly not abating. The Flash PMI declined in June, but continues to point to solid growth. Consumer confidence and retail sales rose, underpinning a strong economic outlook. But there are also ambiguities in the data. The KPMG/REC survey has fallen below 50, pointing to declining employment. If negative signals manifest on the labor market and inflation remains high, the BoE will have a problem.

03/ Currencies

Inflation still remains a main driver. In Europe core inflation was 5.4% in June, more than 3% above the European Central Bank‘s inflation target. The ECB will therefore not back away from further interest rate hikes for the time being. On the contrary, it could raise key rates at each of its meetings until further notice. In the US, this pressure appears to be less at present. Inflation is lower, but interest rates are higher than in the euro area. In addition, fiscal policy support in the wake of the pandemic in the USA was stronger, earlier and more concentrated. Now, however, pressure from the price side is also easing faster than in Europe. The monetary policy stance of the central banks is drifting somewhat apart. In contrast to the USA, it is virtually certain that the ECB will continue to raise interest rates. This has been in favor of the euro against the dollar again for some time.

Looking at the global economy, the stock markets with their near-record levels reflect more optimistic expectations than the bond markets. If the message of Nasdaq indices in the US is to be believed, a recession is likely to be averted. Driven in particular by a number of heavyweights, it recorded its best first half-year since 1983. A certain lack of concern is suggested by the market‘s expectation that, in case of doubt, the Fed will take action against more pronounced weakness by cutting interest rates. This is diametrically opposed to the communication from the Fed and also to the signals from the bond markets, which show a persistently inverse interest rate structure.

However, there are stronger concerns in Europe that the economies could be pushed into a deeper, (prolonged) recession by the elevated and rising interest rates. Germany is already moving into a technical recession with two consecutive quarters of sequential negative economic growth. However, according to its projections, the ECB assumes tangible growth and wants to keep interest rates high to curb a wage-price spiral. If, contrary to this assumption, growth weakens more than forecast and price pressure subsides, doubts will arise in the market as to whether the ECB will continue to turn the interest rate screw after the summer. This, in turn, would deprive the euro of its current support.

The Bank of England is having a particularly hard time under the pressure of especially stubborn price increases. At their last meeting, the monetary watchdogs reacted immediately to a hot inflation figure and increased the pace of their interest rate hikes again to 0.5 percent. They had to abandon the attempt to adopt a wait-and-see attitude. A new turnaround in monetary policy is not to be expected for the time being. The pound will thus tend to remain strong in the short term. Especially since interest rate differentials on the currency market are currently used as a valuation argument. This could only change in the longer term, when weak economic forecasts have a negative impact.

The Bank of Japan is staying in its old rut after all. The slow departure from the zero interest rate policy that was played out at the end of last year has not manifested with the change at the top of the central bank. The yen‘s turnaround has been correspondingly dramatic. In its extreme phase of weakness in the last quarter, the Japanese currency depreciated by more than 10% from around 130 yen to around 145 yen per dollar. The fact that the BoJ is apparently ignoring inflation may trigger a spiral in which devaluation and inflation continue to build on each other. However, the high level of government debt also ties the hands of the central bank. The BoJ is therefore likely to continue to shy away from changing its monetary policy course. The yen will remain under pressure accordingly.

The reopening of the Chinese economy has disappointed so far. The recovery movement of the first quarter has already lost considerable momentum again in recent months. For example, industrial production and retail sales were shockingly weak, signaling a lack of support from consumption. Currently, the composite PMI remains around the expansion threshold of 50, with the production component stabilizing. However, things are not running smoothly overall in the huge country. On the other hand, this does not mean that there is any danger of inflation; on the contrary, there are even deflation concerns. This leads us to expect a further expansion of monetary and fiscal policy stimulation. On the currency side, this should keep the pressure on the yuan high.

04/ Commodities

Oil prices are suffering from the disappointing re-opening development in China, which is also disappointing for us. This is fueling concerns about the global economy. Demand expectations for oil remain correspondingly poor. Fears of recession in Europe and a slowdown in economic growth in the USA add to this. In particular, the sluggish Chinese economy is also causing concern. In addition, inventories are also being run down for the time being due to the higher interest rate level. Accordingly, the supply coming onto the market will be absorbed only sluggishly. This negative trend for oil prices is unlikely to change in the coming weeks or months.

Meanwhile, OPEC+ is no longer enforcing mutually agreed quota cuts. When it does, there have been voluntary cuts in production, particularly from Saudi Arabia. Moscow had also announced that it would reduce production in response to EU sanctions and the G7 price cap on Russian crude oil and refined products. Over the long term, however, supply will remain sufficient and prices will not rise again for the time being after their dry spell.

How does the fragile political situation in Russia affect oil prices and supply from Russia? Sustained production disruptions have historically been triggered by major and prolonged unrest among the population or by the destruction of infrastructure through war. This could arise in the future with problems in the Baltic or Black Seas, where major export ports for the Russians are located. Or in Libya, where the „Wagner“ forces have positions at oil installations. However, the rapidly burgeoning unrest seems to be subsiding for the time being. So far, no lasting disturbances are emerging and the sharp market reaction remains absent.

Gold price developments, meanwhile, have again disappointed. With the fake coup attempt in Russia, investors‘ need for security should have blossomed. However, gold was not sought after and, on the contrary, sold off further. After the old record high at $2072 was set in early April, the yellow metal slid further and further. The hawkish central banks with a correspondingly high if stable interest rate level have provided for pressure.

The US dollar also stabilized again initially, so that the tailwind from the currency side was also lost in the end. A falling greenback makes the yellow metal appear more favorable for investors outside the dollar area and can thus boost demand. Recently, however, even the stronger euro did not help the precious metal upward. Also technically, the gold price does not look good with new intermediate lows in the continuing downward trend. Until there is a sustainable stabilization here, caution remains the order of the day for gold investments.

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