AURIS
WEALTH MANAGEMENT

Market Insight

Spring 2022

Economic context

At this stage, the world economy is showing resilience in the Western countries despite inflation and war on Europe's doorstep.

However, a more detailed analysis suggests a slowdown ahead as central bank rate hikes have barely begun. Although they have begun to fall, delivery times remain historically long **#1**, limiting business output.

Some commodity prices are beginning to stabilise, but food inflation is creating severe strains in emerging countries, leading Sri Lanka to default.

Against a backdrop of economic slowdown, fears of recession and the risk of the FED overreacting to inflation, it seems difficult to find good news, except for the cautious positioning of investors and a bond market that has integrated the rate hikes.

Economic outlook

The earnings season is shaping up to be a crucial one as the "relief rally" fades.

In the United States, the economy is currently in the mid-cycle phase. However, the leading indicators point to a continued slowdown, especially as the first effects of rate hikes will be felt primarily in the real estate sector. This is happening at the same time as consumer and business confidence is waning under the impact of continuing high inflation, which maynevertheless have reached its peak **#2**.

In Europe, leading indicators are also pointing to a future slowdown and confidence in the economic outlook is deteriorating, ***not least because of the strength of inflation, which, unlike in the US, is mainly driven by energy inflation*** **#3**. Consumers will therefore have to dip into their savings to cope.

In China, a significant slowdown is confirmed with PMIs falling below 50 due to the severity of the current Covid confinements, despite the rise in protests. ***The central bank will seek to ease monetary conditions to stabilise the economy, capital markets and a troubled property sector***. The effectiveness of such support is clearly questionable as long as the country remains confined.

The slowdown of the economy is not to the displeasure of the central banks, which have made it a clear objective to calm inflationary pressures. FED members are hinting here and there that it will already be necessary to do more than what was announced in mid-March, which the market is also taking into account. The details, finally announced, of the reduction of its balance sheet suggest a fairly rapid pace, which could even accelerate. Will the ECB take the opportunity to exit its negative interest rate policy?

Financial markets

The general rise in interest rates continued across the entire US yield curve, causing even the worst start to the year in terms of performance for the asset class. This has had the merit of correcting some of the aberrations of the bond world. How far can this go? We believe that US real 10-year yields need to move back into positive territory, which is the norm outside the crisis period. The topic of the moment will have been the brief inversion of the US yield curve, a leading indicator of recession (even if not systematically verified) that indicates on average the occurrence of a recession within 18 months of the inversion.

That said, ***yield curve inversions are not necessarily bad for equity market performance***, even if sectoral performance is very disparate.

In the market context we describe, the indices have therefore entered a downward phase, causing valuations to deflate. This being said, the latter do not reflect the drop in future EPS as companies have only just begun to revise their guidance downwards.

We are not convinced that the market is "pricing in" all the bad news at this stage, even though investor positioning is already very cautious #4.

Investment policy

In a context where the FED is hinting that it will do even more to fight inflation, we expect the US market to retreat under the effect of rate hikes and ***we are taking a negative view of the*** US ***equity segment for a while.***

For European equities, with a relatively more accommodating ECB, the slowdown could be less, while the most cyclical stocks have incorporated a fairly sharp decline in growth.

Although positive on Chinese technology, we are avoiding exposure to the country's growth at this stage. ***However, we remain positive on Latin America***, which is back in favour with international investors.

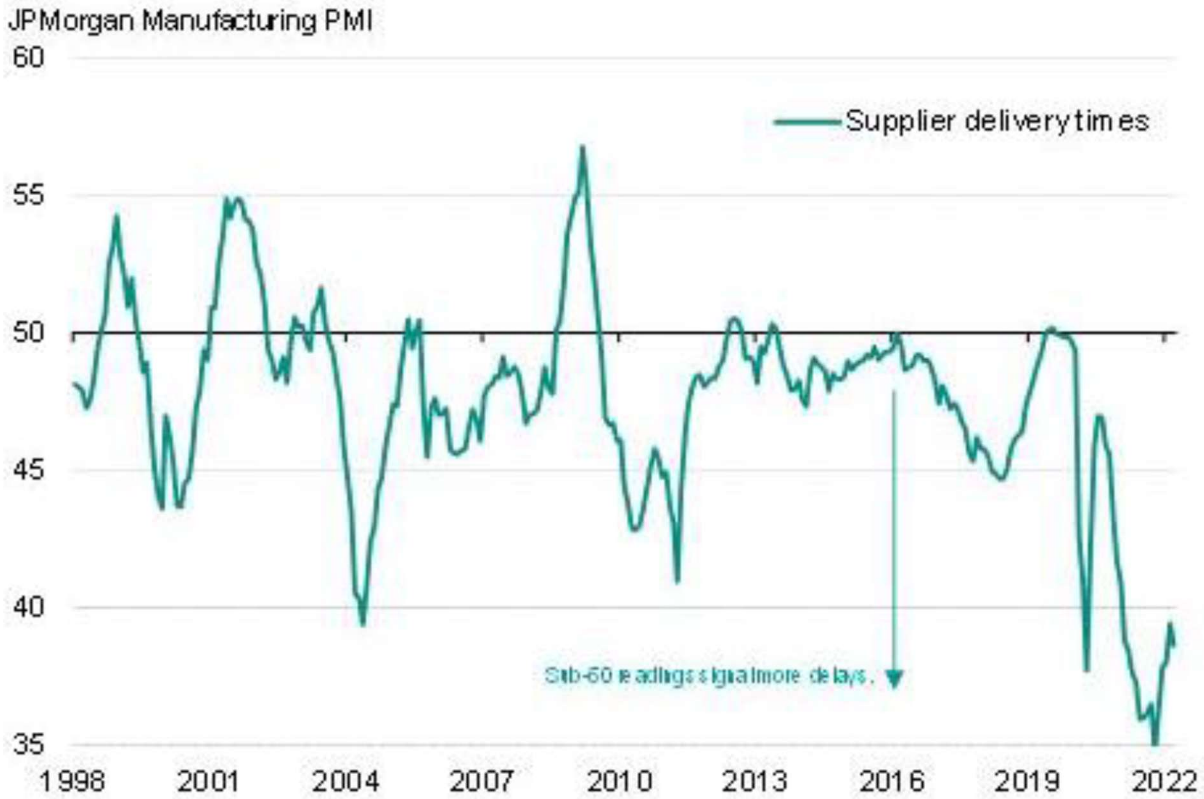
With US real rates expected to move back into positive territory, we expect nominal rates to stabilise above 2.85%.

For European peripheral bonds, the reduction in monetary support is not favourable, but we expect the ECB not to let their rates deviate significantly.

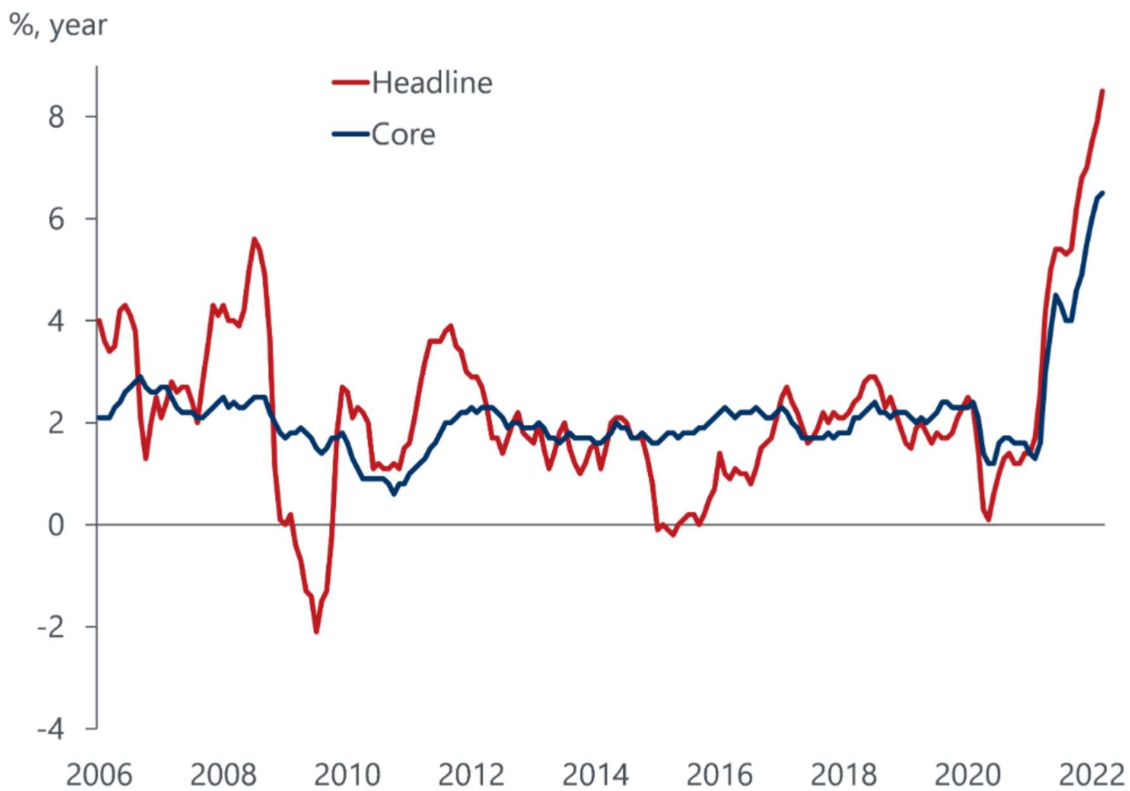
As far as corporate bonds are concerned, we believe that a revival of interest is possible following the spread, and this selectively on the high yield or investment grade segment. We also believe that financial subordinates have taken on board the consequences of the war and offer new opportunities, especially for bonds with a higher beta (long call and/or low coupon).

Graphics

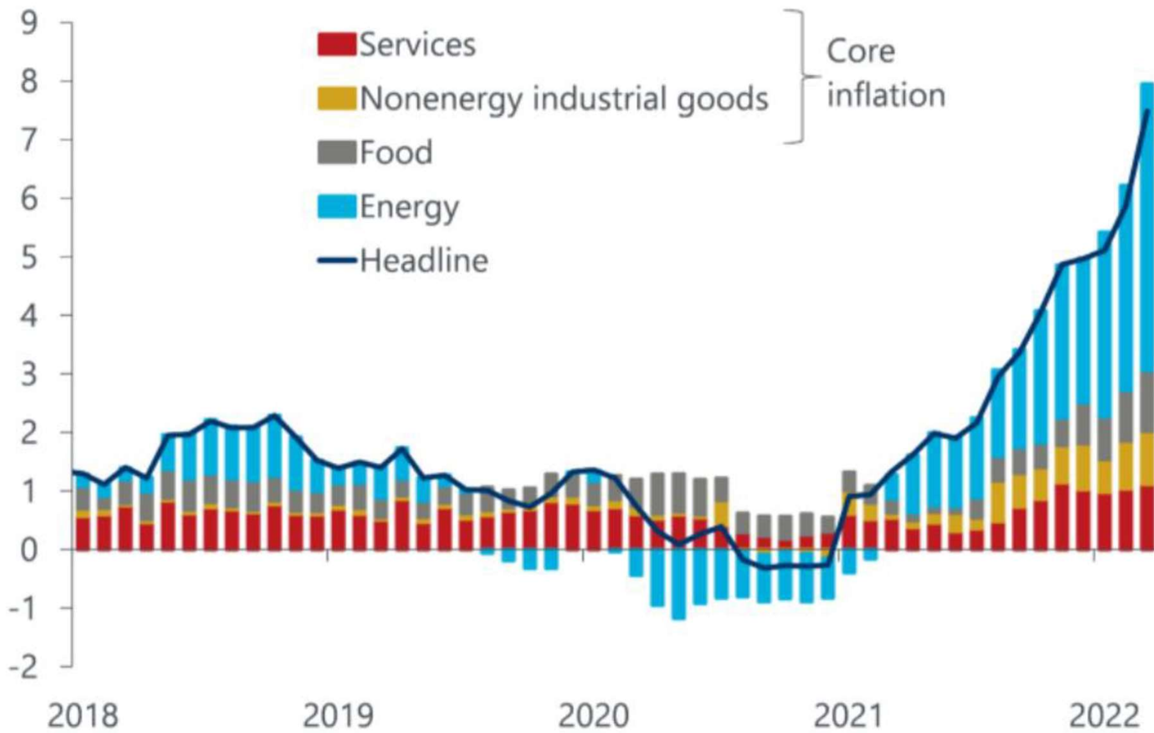
#1 delivery times slightly down, but still negatively impacting production



#2 inflation potentially close to the highs?



#3 preponderance of energy inflation in Europe



#4 percentage of managers who think the economy is improving

www.auriswm.ch
20 bis rue de Lausanne - CH 1201 Geneva

Disclaimer: This document is a marketing publication and is not a financial analysis and as such is not subject to the legal requirements of independent investment research. This document is provided for information purposes only and does not constitute an offer or recommendation to enter into a financial transaction or mandate with Auris Wealth Management SA (hereinafter "AWM"). It reflects the opinion of AWM as of the date of its issue, without guaranteeing the timeliness, accuracy or completeness of such information and analyses. AWM assumes no responsibility for any loss or damage that may result from their use. This document is issued by AWM and is not intended for persons who, by reason of their nationality or place of residence, are not entitled to receive such information under local law.