LimmatWealth

Investment Strategy – June 2022

Data & Forecasts

Developed Markets	Growth (%)		Inflation (%)		Equities			Bonds (10 Years)			Currencies (vs CHF)		
	GDP 21	GDP 22	CPI 21	CPI 22	Actual	3 Mths	12 Mths	Actual	3 Mths	12 Mths	Actual	3 Mths	12 Mths
Switzerland	3.6	2.5	0.6	2.2	1’792	→	↗	1.05	0.90	1.10	-	-	-
Germany	2.8	2.0	3.2	6.9	14’541	→	↗	1.31	1.05	1.10	-	-	-
Eurozone	5.2	2.6	2.6	6.8	3’811	→	↗	-	-	-	1.04	1.04	1.06
United Kingdom	7.2	3.7	2.6	7.8	7’592	→	↗	2.24	1.85	1.90	1.23	1.24	1.27
United States	5.7	2.6	4.7	7.2	4’161	→	↗	3.00	3.10	3.20	0.98	0.96	0.95
Japan	1.7	1.8	-0.2	1.8	28’234	→	↗	0.25	0.20	0.20	137	133	130

Emerging Markets	Growth (%)		Inflation (%)		Equities			Bonds (10 Years)			Currencies (vs USD)		
	GDP 21	GDP 22	CPI 21	CPI 22	Actual	3 Mths	12 Mths	Actual	3 Mths	12 Mths	Actual	3 Mths	12 Mths
Asia ex Japan	7.0	4.9	1.2	2.6	681	→	↑	-	-	-	-	-	-
China	8.1	4.5	0.9	2.2	72	→	↑	2.81	2.80	2.80	6.68	6.65	6.65

Review – Markets stabilize in May

After a weak month in April, global markets attempted to stabilize in May and ended the month on a neutral trend. In the United States, inflation rates remain high, but are currently declining. US bond markets are therefore pricing in a peak in inflation dynamics and the associated peak in Fed hawkishness. Finally, the aggregate US macro data points to an economy that, while continuing to grow, is clearly past its peak. Consequently, in this combination, US interest rates were stable to slightly falling in May. European interest rates, on the other hand, have continued to rise. Inflation rates in the Eurozone rose to new highs in May. As a reaction to the inflation problem, the European Central Bank ECB is signaling more and more timely interest rate hikes. On the commodities side, as in the previous months, oil prices rose again significantly, which once again gave energy stocks a boost. After long discussions, the European Union decided on a partial embargo on Russian crude oil. This policy tightens the oil supply and consequently increases crude oil prices. On the other hand, industrial metals lost significantly in the past month. These are weighed down by the weak macro data from China, which continues to be economically slowed down by the tough lockdowns. Since the number of new infections in China has decreased significantly, the restrictive Corona policy is likely to be relaxed in the short- to medium-term, thereby relieving the economy in the future.

Equity markets around the world ended May with positive returns. Markets in China (+4.6%), Germany (+2.1%), and Japan (+1.6%) performed best, while the one in Switzerland (-4.4%) fell significantly.

Global 10-year government bond yields continued to rise in most countries over the past month. They rose the most in the United Kingdom (+0.20% to 2.10%) and Germany (+0.19% to 1.12%). In Switzerland, interest rates only rose slightly (+0.01% to 0.89%).

Currency markets moved little in May. The Swiss Franc strengthened against the US Dollar (+1.5% to CHF 0.96) and the British Pound (+1.2% to CHF 1.21) but remained unchanged against the Euro (CHF 1.03). The US dollar weakened slightly against the Euro (-1.8% to USD 1.07).

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Alternative investments finished the past month with mixed results. Gold (-3.1% to USD 1,837 per troy ounce) and hedge funds (-0.6%) ended the month with negative returns, while oil prices (WTI, +9.5% to USD 114.67 per barrel) continued to rise.

Outlook – Inflation remains in focus

The fundamental outlook is becoming increasingly difficult. The Ukraine war and China's economic weakness are having a negative impact on the global economy. At the same time, both factors have an inflationary effect. The Ukraine war is having an inflationary effect via the commodity channel, while the tough lockdowns in China are having an inflationary effect by disrupting global supply chains. As a result, the general pressure to increase interest rates – especially in the Eurozone – remains intact. In addition, there will be overriding normalization effects in 2022, which stem from a slowdown in fiscal stimulus and tighter monetary policy. In particular, the swift throttling of liquidity by the global central banks and the resulting exit from the strongest monetary expansion phase of modern times should ensure regular withdrawal symptoms on the financial markets. At the same time, the inflationary pressure will continue and will require a very tight monetary policy in the medium-term. In 2022, it can also be expected that workers will take inflationary pressure into account in their wage demands and that part of the inflationary pressure will therefore be permanently cemented. These inflationary factors and rising wage spending will put pressure on historically high corporate profit margins. As such, earnings disappointments are likely to increase in 2022 compared to 2021, leading to regular bouts of fragility. Finally, China remains an important market driver. Beijing is increasingly focusing on stimulating countermeasures, both at the level of monetary and fiscal policy. However, the fundamental structural problems in China are so pronounced that the stimulus is hardly reflected in the macro data. China is therefore likely to increase the pace of stimulus again over the course of the year in order to ensure fragile stabilization in the second half of the year.

Based on the above statements, we expect the equity markets to continue trending sideways in the short-term before they pick up again. We continue to expect positive global economic and earnings growth, but it will be lower than expected at the beginning of the year due to rising interest rates and geopolitical events. This is likely to lead to more volatility in the markets as the year progresses. The corrections in certain markets last year and at the beginning of this year offer entry opportunities in selected areas/sectors. We continue to favor Switzerland and the United States over Europe, while continuing to focus on good quality companies that are spared the long-term effects of the pandemic and benefit from long-term trends. We remain positive about Asia and China in particular: there is significant catch-up potential and – as mentioned above – stimulus from the Chinese central bank can be expected.

Market participants expect the US Federal Reserve to raise interest rates eight times over the course of the year. The situation looks extreme in Europe now, where markets are pricing in 13 rate hikes by the ECB until the end of the year. The Swiss National Bank SNB is likely to follow suit with a slight delay as soon as the ECB raises interest rates.

Trade policy disputes and geopolitical developments will continue to lead to strong movements from time to time in the currency markets. The Swiss Franc will serve as a safe haven during these periods.

Hedge funds continue to benefit from a normalization of correlations, volatilities, and dispersion. They typically thrive when dispersion is high and correlations are low, because then they can take full advantage of their trading techniques.

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Limmat Wealth Ltd.