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SoundInsight N°14

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02 Interest rates jump significantly

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04 Unchanged asset allocation

Interest rate cuts under review

In recent months, market participants have been gaining confidence in upcoming interest rate cuts. However, macroeconomic data forces central banks to maintain a continued stance of restrictive monetary policy.

It has been nearly two years since the Federal Reserve adopted a restrictive monetary policy course due to a significant rise in inflation. The era of zero interest rates ended. Over the past 24 months, interest rates have been increased at a historically unprecedented pace and lifted to a target range of 5.25% to 5.50%. While the battle against inflation has been a challenging one, it has been successful so far thanks to the drastic measures taken.

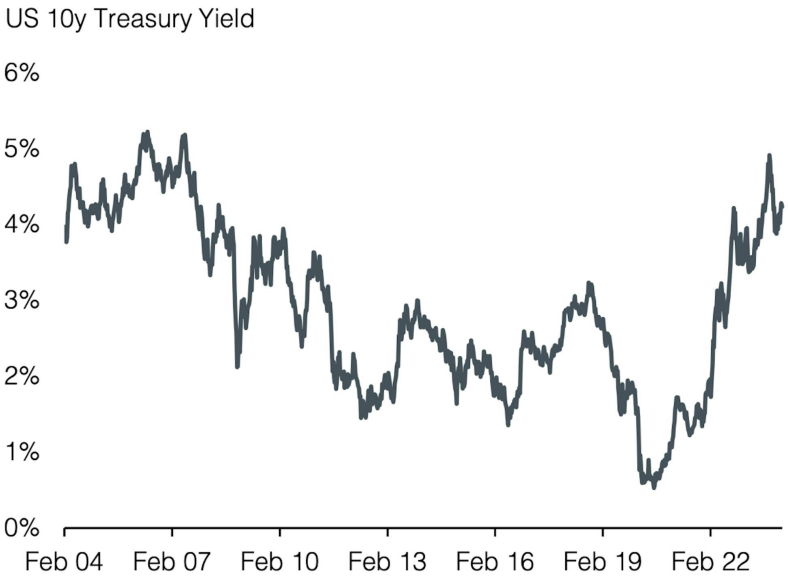
With growing confidence that inflation is receding, market participants have begun to anticipate the timing of a shift in monetary policy. Investors are confident that easing will start soon and are looking for lower interest rates going forward. In our outlook for 2024, we have already pointed out that the market expects significantly more interest rate cuts this year than central banks have been communicating. Accordingly, recently released positive economic data out of the US served as a reality check regarding the future course of monetary policy.

Despite carrying the burden of high interest rates for some time now, the US economy continues to show resilience. In addition to a robust labor market and a surprisingly stable residential property market, both the manufacturing and services sectors have seen positive developments in purchasing manager sentiment. In addition, consumer prices rose much more than expected in January, while core inflation also exceeded forecasts. Given this set of data, interest rate cuts by the central banks appear unlikely in the near future. As a result, significant shifts have occurred in the bond market since the beginning of the year. At the start of 2024, the market expected both the Fed and the ECB to cut interest rates six times totaling 1.5%. Initially, the first rate cut was anticipated for March. However, strong economic reality has pushed back these expectations to June, with only four interest rate cuts left for the current year. Concerns about continuous inflationary growth persist, and Chairman Powell emphasized that he would like to see more signs of sustainably lower inflation before considering rate cuts.

Thus, expectations of rate cuts have been put under review, leading to a jump in interest rates for both the Euro and the US Dollar across all maturities. For fixed-income investments, this led to losses since the beginning of 2024. However, the last quarter of 2023 clearly showed how quickly the window of opportunity to lock in higher interest rates can close. Therefore, we consider the current interest rate levels, especially for USD denominated investments, as attractive and recommend investors to opt for longer maturities.

The stock market experienced an incredibly positive start to 2024, with a similar dynamic as in the prevailing year. Once again, the 'magnificent seven,' whose performance was driven by very solid corporate results, were the main driver of equity returns. Upcoming developments around artificial intelligence remain one of the reasons for the robust performance of technology stocks, which propelled the global market to a new all-time high in February.

However, the fact that the market is being dominated by just a few stocks while trading near record levels has historically been a sign of some complacency to macroeconomic data. The S&P 500 is trading more than 1.5 standard deviations above the long-term average forward price-earnings ratio, indicating that many of the expected positive developments are already priced in.

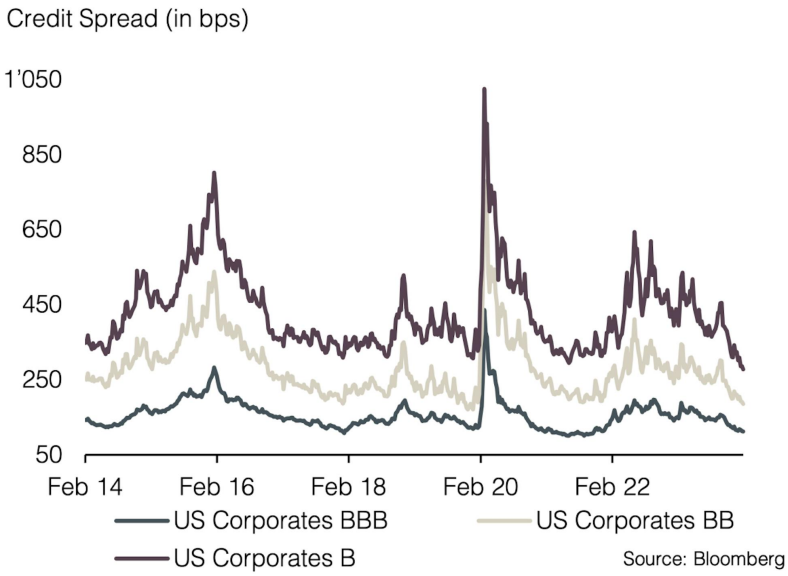


Yields

Strong economic data out of the US led to a significant increase in long-term bond yields. After 10-year US Treasury yields rose to 5% last October, they fell below 3.8% by the end of the year, only to be trading above 4.3% now. High volatility in the bond market illustrates that expectations regarding the future trajectory of the economy fluctuate between a soft landing and robust growth (with continuously high interest rates). From our perspective, interest rate levels remain attractive.



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Spreads

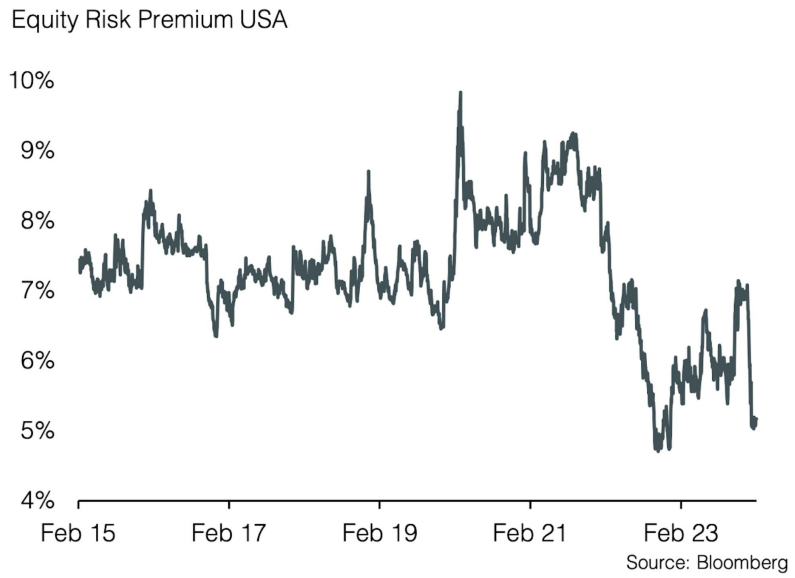
For several months, we have been writing about exceptionally low credit spreads, which have

continued to decline in the last month. In the current market environment, we continue to recommend focusing on top-tier borrowers thus seeking yield opportunities in longer maturities rather than credit risks.



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Equity Risk Premium

Despite witnessing sustained strong economic momentum in the US, the stock market's recent gains have already priced in most of the positive outlook. Expected earnings growth has not kept pace with stock price appreciation, making the stock market more expensive and thus less attractive.



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Leading Indicators

There have been encouraging developments in leading indicators. The increasing momentum in manufacturing is likely to lead to a positive assessment, assuming the current trend continues. However, the indicator remains at a neutral rating for now.



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Manufacturing PMI

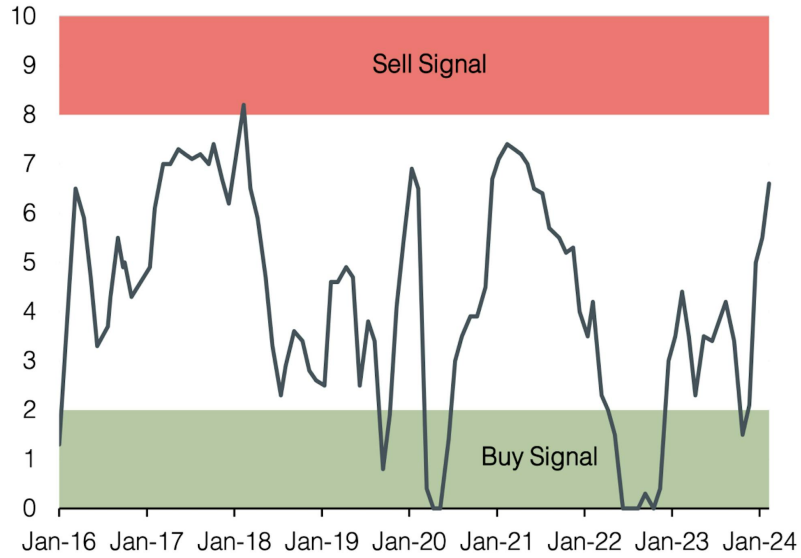
	May 22	Jun 22	Jul 22	Aug 22	Sep 22	Oct 22	Nov 22	Dec 22	Jan 23	Feb 23	Mar 23	Apr 23	May 23	Jun 23	Jul 23	Aug 23	Sep 23	Oct 23	Nov 23	Dec 23	Jan 24	Feb 24
Global	52.3	52.2	51.1	50.3	49.8	49.4	48.8	48.7	49.1	49.9	49.6	49.6	49.5	48.7	48.6	49.0	49.2	48.8	49.3	49.0	50.0	
USA ISM	56.1	53.4	52.8	52.8	50.8	50.0	48.9	48.1	47.4	47.7	46.5	47.0	46.6	46.4	46.5	47.6	48.6	46.9	46.6	47.1	49.1	
Europe	54.6	52.1	49.8	49.6	48.4	46.4	47.1	47.8	48.8	48.5	47.3	45.8	44.8	43.4	42.7	43.5	43.4	43.1	44.2	44.4	46.6	46.1
United Kingdom	54.6	52.8	52.1	47.3	48.4	46.2	46.5	45.3	47.0	49.3	47.9	47.8	47.1	46.5	45.3	43.0	44.3	44.8	47.2	46.2	47.0	47.1
Switzerland	59.8	59.1	58.0	56.7	56.8	55.4	54.4	54.5	49.3	48.9	47.0	45.3	43.2	44.9	38.5	39.9	44.9	40.6	42.1	43.0	43.1	
China Local	49.6	50.2	49.0	49.4	50.1	49.2	48.0	47.0	50.1	52.6	51.9	49.2	48.8	49.0	49.3	49.7	50.2	49.5	49.4	49.0	49.2	
Japan	53.3	52.7	52.1	51.5	50.8	50.7	49.0	48.9	48.9	47.7	49.2	49.5	50.6	49.8	49.6	49.6	48.5	48.7	48.3	47.9	48.0	47.2

Services PMI

	May 22	Jun 22	Jul 22	Aug 22	Sep 22	Oct 22	Nov 22	Dec 22	Jan 23	Feb 23	Mar 23	Apr 23	May 23	Jun 23	Jul 23	Aug 23	Sep 23	Oct 23	Nov 23	Dec 23	Jan 24	Feb 24
Global	52.0	53.7	51.0	49.2	49.9	49.1	48.1	48.0	50.0	52.5	54.3	55.3	55.3	53.8	52.6	51.0	50.7	50.4	50.6	51.6	52.3	
USA ISM	56.9	55.9	56.4	55.9	55.7	54.7	55.2	49.0	54.7	55.0	51.2	52.3	51.0	53.6	52.8	54.1	53.4	51.9	52.5	50.5	53.4	
Eurozone	56.1	53.0	51.2	49.8	48.8	48.6	48.5	49.8	50.8	52.7	55.0	56.2	55.1	52.0	50.9	47.9	48.7	47.8	48.7	48.8	48.4	50.0
United Kingdom	53.4	54.3	52.6	50.9	50.0	48.8	48.8	49.9	48.7	53.5	52.9	55.9	55.2	53.7	51.5	49.5	49.3	49.5	50.9	53.4	54.3	54.3
Switzerland	59.6	58.1	55.6	56.6	52.8	53.8	53.4	49.5	56.7	55.3	54.2	52.2	52.6	49.6	42.7	50.3	52.8	52.2	53.6	56.9	54.6	
China Local	47.1	54.3	52.8	51.9	48.9	47.0	45.1	39.4	54.0	55.6	56.9	55.1	53.8	52.8	51.5	50.5	50.9	50.1	49.3	49.3	50.1	
Japan	52.6	54.0	50.3	49.5	52.2	53.2	50.3	51.1	52.3	54.0	55.0	55.4	55.9	54.0	53.8	54.3	53.8	51.6	50.8	51.5	53.1	52.5

Description: The Purchasing Managers' Index (PMI) is a forward-looking economic indicator based on company surveys. A value above 50 indicates an improving economic environment, whereas a value below 50 indicates a worsening environment.

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Risk-Index

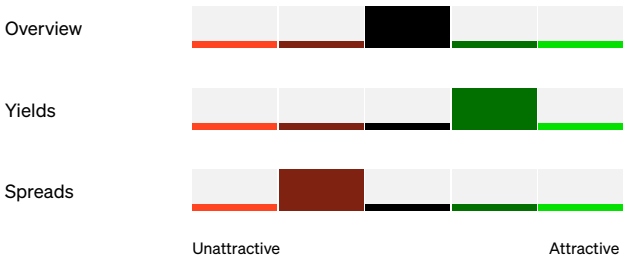
Rising stock prices are currently going hand in hand with an investor sentiment that has reached its highest level since 2021, trending towards euphoria. While no sell signal has emerged yet, our investment committee is closely monitoring the developments, as further increases would likely result in an underweighting of equities as an asset class.



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Bonds



Equities



Appendix

Sound Invest is the central tool for our investment allocation. We use it to systematically and consistently assess the aspects that are relevant to the development of the financial markets. As a result, our clients can rely on a rational and anti-cyclical implementation of our investment decisions.

- **Focusing on the essentials** Interest rate level, risk premium, valuation, economic development, investor sentiment and positioning. These are the decisive factors for success on the financial markets, especially in turbulent times when the temptation to react irrationally to the headlines is particularly strong.
- **Comparability over time and place**
  The factors mentioned above are equally relevant for all markets and at all times. This is the result of a strict «backtesting» process that continues into the future.
- **Cumulating our investment experience**
  Our strength lies in the many years of experience of our partners and principals. It is precisely this experience that we summarize and make it applicable with Sound Invest.
- **Transparency**
  Thanks to our monthly publication, our clients always know where we stand in the investment cycle and how we expect the financial markets to develop.

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