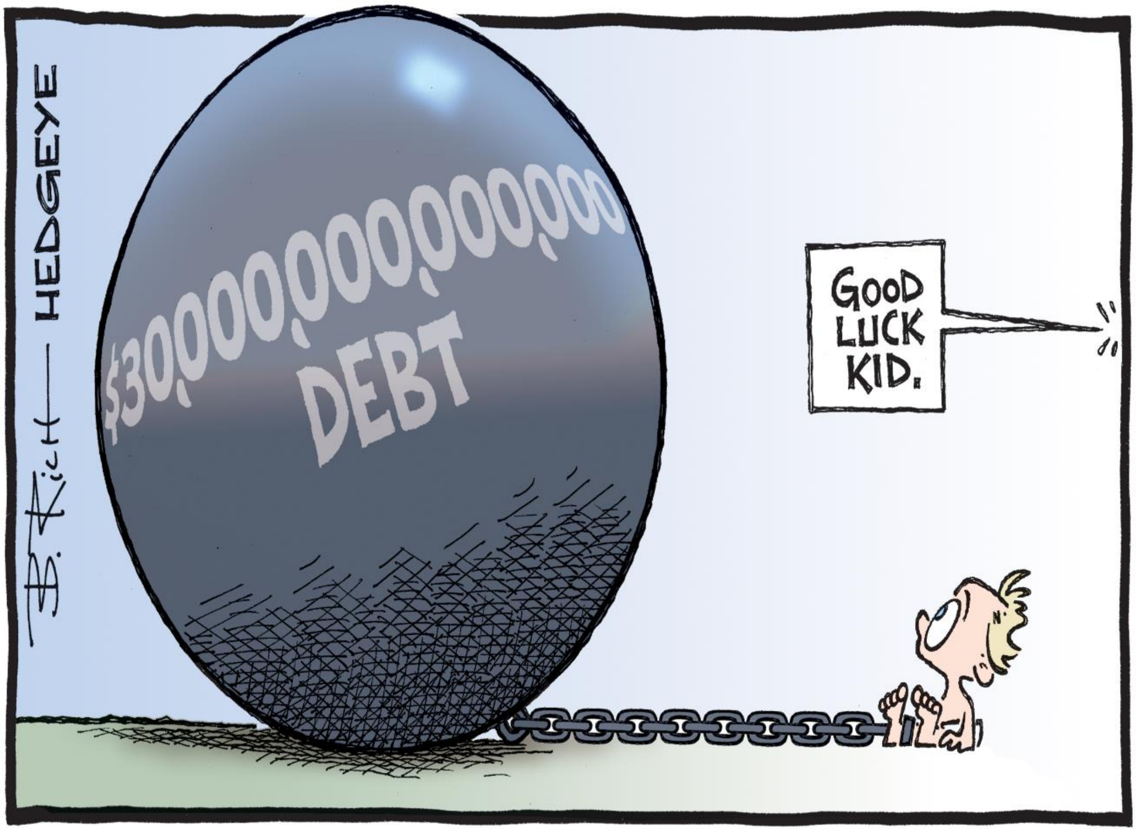
Market Review February 2023



In contrast to 2022, 2023 has started off with a bang! In an environment of hope for a "soft landing", the stock markets experienced a massive "short covering" in January. Even digital assets (the pests of 2022) had their best January in 10 years. The most optimistic are already pointing to a statistic that shows that when January's performance is positive, the performance of the whole year will be positive. This has happened more than two-thirds of the time over the last 95 years and has been confirmed in 2022, as after a difficult January on the stock markets, the indices ended the year in the red. Interestingly, the sectors and segments that suffered the biggest losses last year were among the big winners in January. Indeed, even though the MSCI World gained 7% for the month, growth stocks strongly outperformed defensive stocks. Take semiconductor companies as an example. After experiencing shortages in 2021, they have seen their stocks swell, sending the sector's stocks down more than 35% over the past year. January was a much happier month as the sector, represented by the SOXX ETF, soared 16%. Goldman Sachs lists in an index the US listed companies that do not generate profits. This index, which gave up more than 60% in 2022, has rebounded by 22% since the beginning of the year. Conversely, it is the health care and consumer staples sectors that have performed the worst over the month. The same is true in Europe, where the banking (+14.04%), automotive (+11.35%) and consumer discretionary (+17.18%) sectors have performed strongly.

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Bonds benefited from the drop in long-term rates. The U.S. 10-year yield fell from 3.87% to 3.50%, while its German counterpart also fell by nearly 30 basis points to below 2.30%. Against the backdrop of an economic slowdown, the inversion of the yield curve has become even more pronounced, reaching record levels in the US. Gold was also a big winner this month. The yellow metal posted its third consecutive monthly increase, which cumulatively represents an appreciation of over 16%. We have repeatedly mentioned our dismay over the past year that gold was not benefiting from the current economic and geopolitical uncertainty... it seems that this time, the movement is on!

Market evolution at the end of January 2023

	Equities in Local Currencies							
End of January	MSCI World	S&P 500	EuroStoxx	CAC	Spain	Switzerland	MSCI EM	CSI 300
Perf 1 Month	7.00%	6.18%	9.75%	9.40%	9.78%	5.19%	7.85%	7.37%
Perf 3 Month	9.31%	5.28%	15.09%	13.02%	13.54%	4.23%	21.62%	18.47%
Perf YTD	7.00%	6.18%	9.75%	9.40%	9.78%	5.19%	7.85%	7.37%

	Commodities				Currencies vs EUR			
End of January	WTI Oil	Brent Oil	Gold	Copper	USD	JPY	GBP	CHF
Perf 1 Month	-1.73%	-1.65%	5.72%	10.16%	-1.46%	-0.64%	0.43%	-0.56%
Perf 3 Month	-8.85%	-10.90%	18.05%	23.79%	-9.04%	4.00%	-2.22%	-0.53%
Perf YTD	-1.73%	-1.65%	5.72%	10.16%	-1.46%	-0.64%	0.43%	-0.56%

	Bloomberg Indices Bonds Total returns							
End of January	Global Aggregate	US Aggregate	Euro Aggregate	US 10 Year Treasury	German 10 Year Bund	Global Credit	Global High Yield	Emerging Sovereign $
Perf 1 Month	3.28%	3.08%	2.21%	3.17%	4.73%	3.75%	4.18%	3.20%
Perf 3 Month	8.73%	6.39%	0.87%	5.70%	0.21%	9.55%	10.12%	10.98%
Perf YTD	3.28%	3.08%	2.21%	3.17%	4.73%	3.75%	4.18%	3.20%

Source: Bloomberg 31/01/23.

<u>What debt?</u>

At the end of last year, the colossal amount of the American public debt and the approach of a new limit ("debt ceiling") loomed as a threat on the markets. Indeed, because of an ever-increasing budget deficit approaching 1,500 billion dollars, a new debt ceiling should be reached soon. According to U.S. Treasury Secretary, Janet Yellen, this should happen by June. Currently, the limit is set at 31,400 billion dollars. As a reminder, it is the Congress (and the Congress alone) that sets the maximum amount that the US government can borrow. This limit does not represent a limit on new spending, but simply the amount of money the government can borrow. If this limit is reached (and not increased), it means that the US government can no longer pay the bills that it intended to pay. This would be tantamount to a default of payment. Fortunately, this risk is relatively low because members of the Congress (in principle) always find common ground to increase this limit. But in the current political context, where neither Democrats nor Republicans have a clear majority, this situation is worrying. For the famous brokerage firm Goldman Sachs, this even represents the main "black swan" for 2023.

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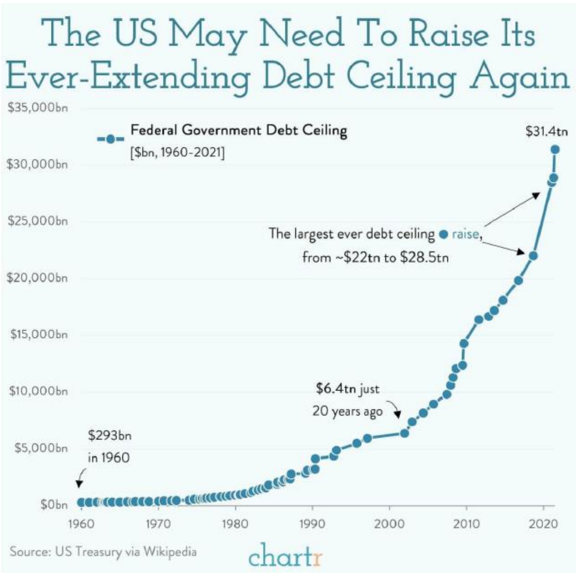
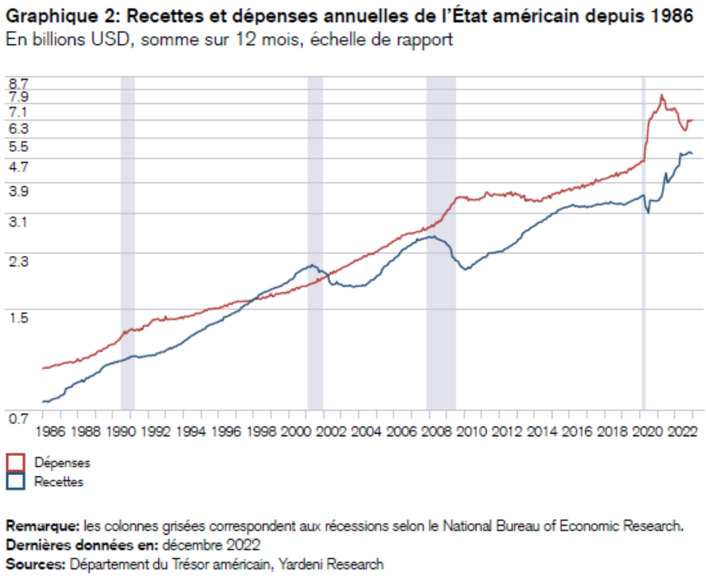
Let's remember that Congress has already had to raise the limit nearly a hundred times since World War 2. Needless to say, the Congress is well versed in this exercise. Often, these increases have come about almost naturally. But sometimes, as in 2011, it takes several rounds of voting for an increase to be validated. At that time, it was precisely the prevarication over raising the debt ceiling that cost the US government its AAA rating. During the difficult negotiations, some bills were suspended, some public servants were no longer paid and others were put on short-time work. To sum up, the country is running in slow motion.





Source: Credit Suisse

Investors will need to take into consideration this risk into their scenarios for 2023. If the cap is raised (most likely), this should be seen as good news. But is it really? Wouldn't it be better for the US to get serious about the budget deficit once and for all? This issue was swept under the rug during the period when interest rates were close to zero because it did not unduly affect government spending. But with rates at 4.75%, the cost of servicing the country's debt is skyrocketing. At current rate levels, the United States is expected to spend more than $800 billion on interest this year. This amount could increase by 50% if rates were to rise by 1% from current levels! Not to mention a possible downgrading by the rating agencies which would add a risk premium and thus raise the country's refinancing rate. The one-year US CDS has risen from 15 to 70 basis points since the beginning of the year... something to think about.

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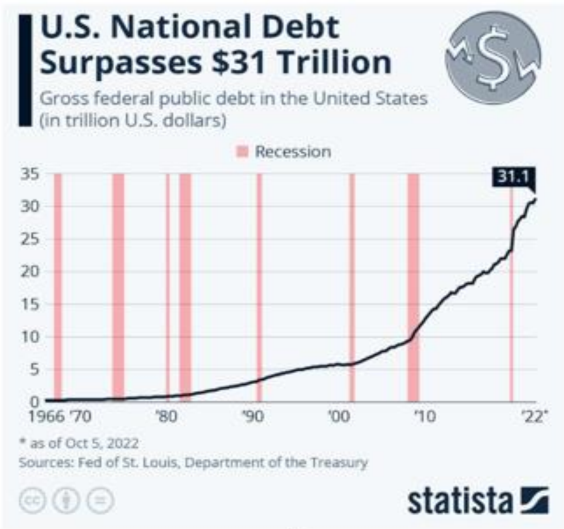

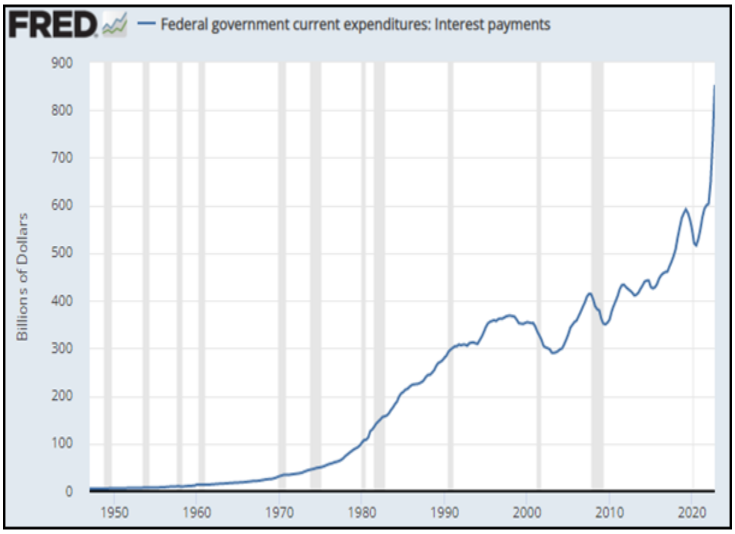

The Middle Kingdom

We talked about it in December, China decided to suddenly lift the sanitary measures in the country. This is what we call "China's reopening". Investors welcomed this announcement with strong interest in Chinese assets. The Shanghai Shenzhen CSI300 index of onshore Chinese companies and the Hang Seng index of Hong Kong-listed stocks rose by 7.37 and 10.7% respectively in January. Large Chinese companies such as Tencent and Alibaba gained nearly 20%. The latter had suffered heavy losses on the stock market last year. The lifting of health restrictions came at the right time, just before the Chinese New Year festivities. This allowed most citizens to travel to celebrate the Year of the Rabbit with their families. Although this decision caused a significant increase in Covid infections, it seems that the authorities are now advocating general immunity and are no longer concerned about the number of potential deaths that this decision may cause. The fact that the Chinese are back to work and moving about normally is good for the country's economy and for the rest of the world. On the other hand, if the country gets back to normal in the near future, this will put pressure on the demand for raw materials, which could be reflected in future inflation figures. The "second wave effects" of this reopening will therefore have to be closely monitored. For now, investors seem to see the glass as half full. This announcement has even allowed IMF economists to revise their global growth forecasts upwards for 2023. According to them, with China "firing on all cylinders", a global recession should be avoided.

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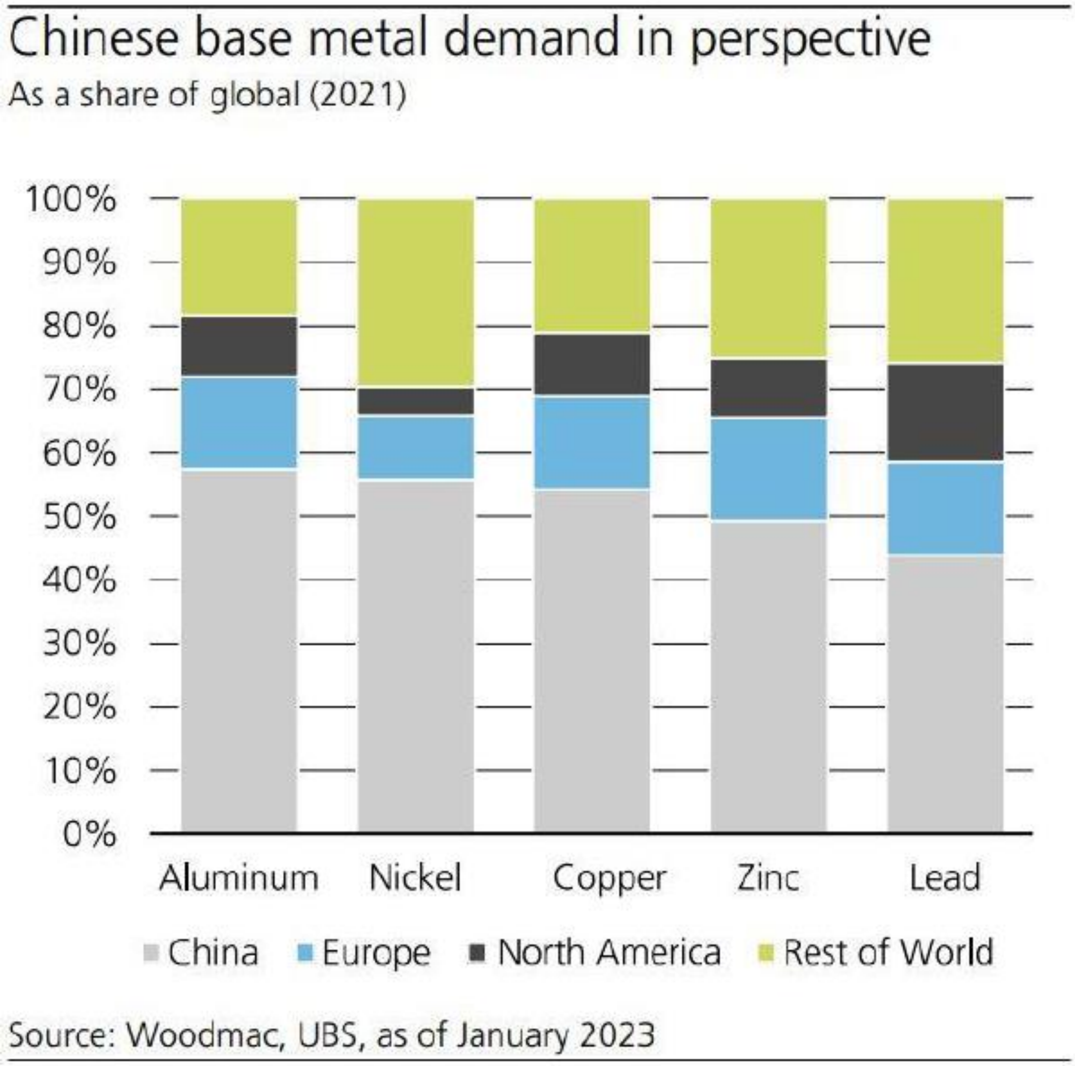
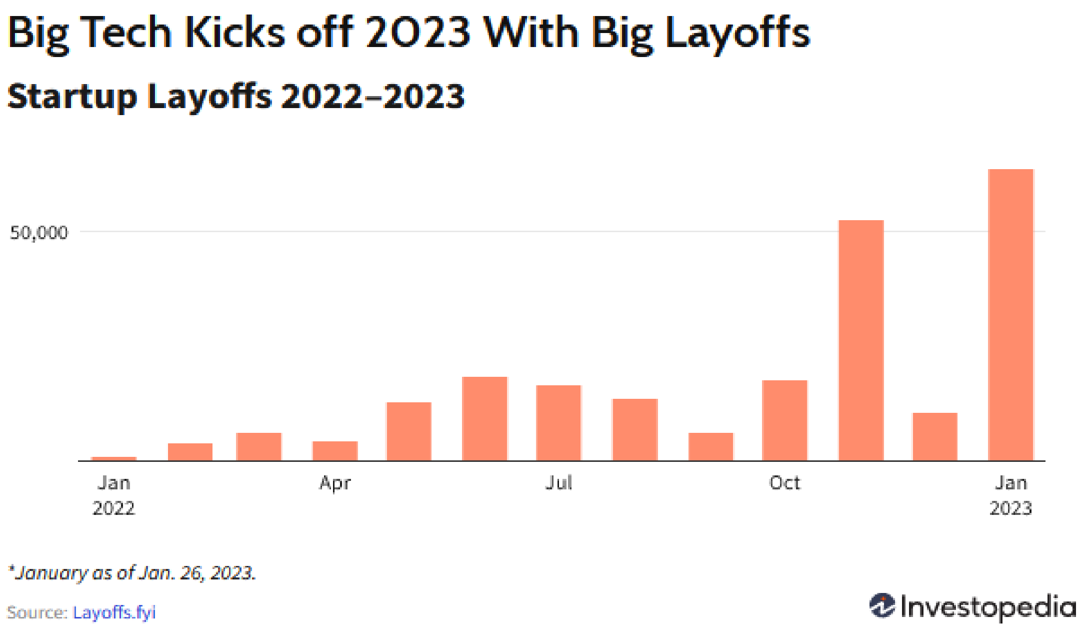
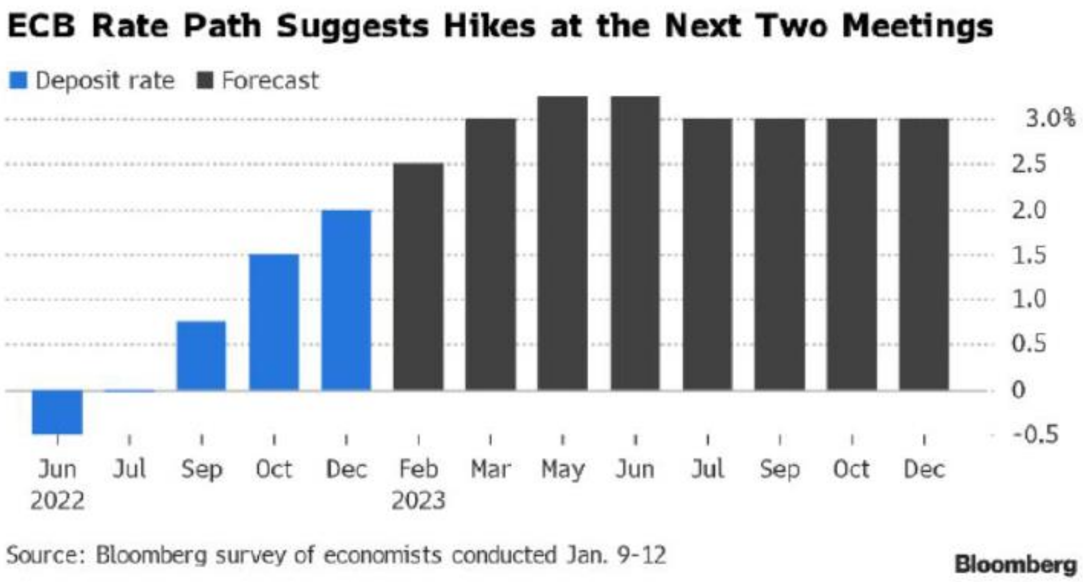


Inflation / Central Banks

Central banks delivered the message that investors wanted to hear. The FED was the first to act. As expected, the FED raised its benchmark rate by 25 basis points to 4.75% and confirmed that further rate hikes were on the way. It also hinted that the "disinflation" process was in place. The implication is that the first rate hikes are beginning to bear fruit and that inflation is in a cycle of returning to the target. So, there should be no nasty surprises in the future and the terminal rate between 5 and 5.25% that the market is expecting seems realistic. These announcements were welcomed by investors who rushed into stocks and long bonds. As for the dollar, it fell back to the 1.10 zone against the euro, a level not seen since April 2022. Mr. Powell has repeatedly said that the labor market is key to ensuring that inflation is under control. What if the latter were to resolve itself? Following the recent layoff announcements in most sectors, the imbalance could indeed normalize. The thousands of Americans who will be out of work in the next few months should put pressure on wages and thus further fuel the disinflation process. Will the battle finally be won?



Mrs. Lagarde also merely confirmed what the consensus was expecting. She raised ECB rates by 50 basis points to 3.00%, as expected, and announced that a further 50 basis point increase was expected at the next meeting in March. The latter reaffirmed that the institution will consider future economic data to make its decisions ("data dependency"). Prior to this meeting, the European statistics gave a rather ambivalent message. First of all, we learned that inflation was back on the rise in France and Spain. Second, even though Olaf Scholz himself announced in December that his country would avoid a recession, Germany surprised everyone by reporting negative GDP growth for the 4th quarter (-0.2%) mainly due to weaker than expected household consumption while the consensus was for zero growth. But this did not seem to sow doubt in the minds of investors who continued to rush into risk assets.



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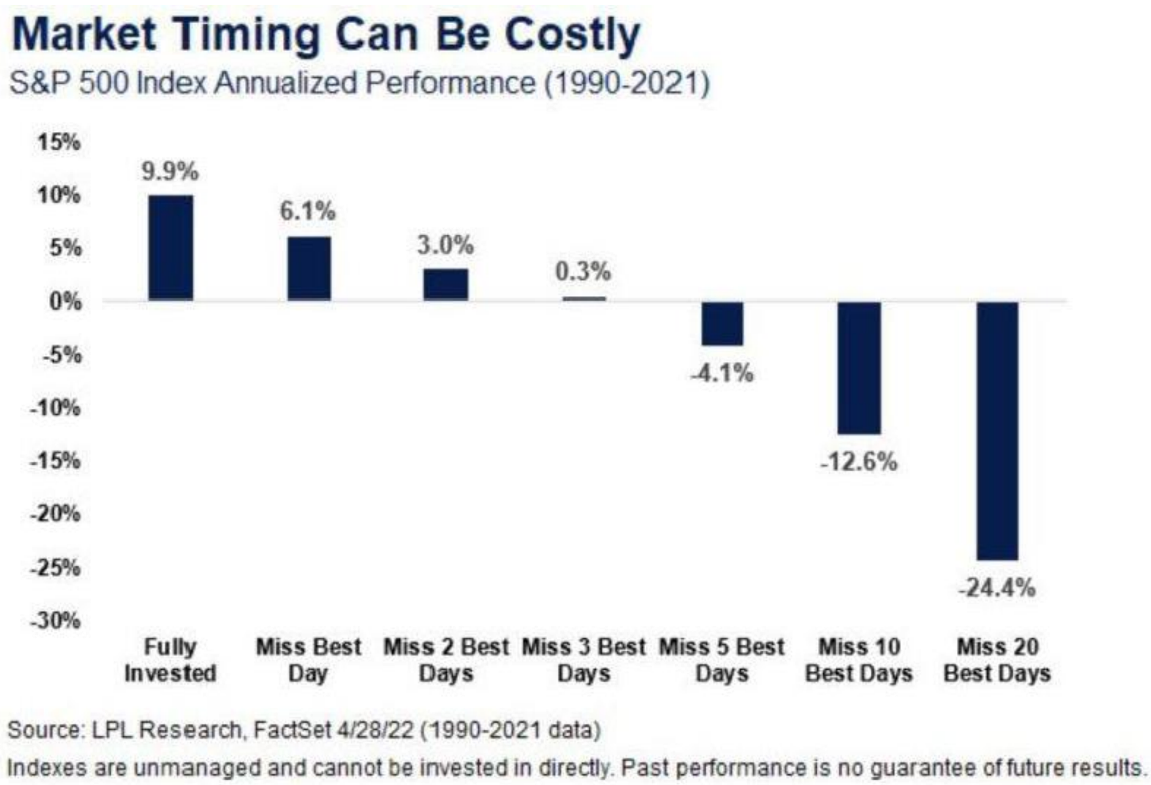
The month of January surprised more than one investor by the strength of the upward movement. Of course, we should not be too quick to claim victory, as 2023 will certainly have its share of good and bad surprises in store for us. That said, concrete confirmation that inflation is in the process of correcting and the resilience of the economy, which could be content with a "soft landing", has put some hope in investors' hearts. Moreover, the results for the 4th quarter are, for the moment, quite good and, above all, the "guidance" for the year 2023 are reassuring. The recent announcements of layoffs in most sectors should allow the job market to relax. But inevitably, this will have a negative impact on future consumption. All of this macroeconomic information proves, as we have discussed several times over the past year, that there was an excess of pessimism in 2022. However, there are risks that could once again put the brakes on it. Starting with the Russian-Ukrainian conflict and the delivery of new weapons to Ukraine, which could raise tensions in the region.

We wish you a good month of February.



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