Market Review May 2023

With the hope of being able to identify which economic cycle the world's economies are in, investors focused on the macro statistics in April. As we have been saying for several months, there is (almost untenable) uncertainty about the evolution of global growth. Following the most violent rate hike cycle in history, which began in the first half of 2022, some players are betting on a sharp economic slowdown that will push developed economies into recession. Others believe that demand remains robust enough to cushion the blow and expect a soft landing. Given that we are at a crossroads and that central banks are slowly but surely coming to the end of their many rounds of tightening, the difficulty at the moment lies in the interpretation of the figures. Indeed, the latter can be totally different from one statistic to another.

1. US and European inflation measured by the CPI index is declining, which is pleasing to investors. On the other hand, the labour market remains tight, which keeps upward pressure on wages in certain occupations, such as the service sector.
2. The recently released first quarter growth figures show that the US and European economies are slowing down but that demand remains robust despite declining purchasing power.
3. Corporate results for the first quarter held up well overall.
4. The luxury sector is breaking records, which is not a sign of future recession.
5. The yield curves have been inverted for several months, which is generally interpreted as a leading indicator of recession.

In short, as you may have understood, with all these diverging signals, the reading of the economic situation is very complicated at the moment.

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Usually investors hate uncertainty and tend to reduce their positions when visibility is not good. Yet, in the current confusing fog, markets performed rather well in April. Helped by the large caps, most stock market indices rose between 1% and 3%, with defensive indices such as the SMI (+2.98%) and the Dow Jones Industrials (+2.48%) outperforming. But these indices are not the best performers since the beginning of the year. The Nasdaq, which finished virtually unchanged in April, has rebounded by more than 20% since the end of the year, while most European indices have gained between 10% and 15% over the same period. The CAC40, which represents the main French companies and which is experiencing historic social movements, has even afford itself the luxury (no pun intended with LVMH...) of exceeding the January 2022 highs to print an all-time high of 7581 points. The German DAX is not far from doing the same. The time when some analysts were burying the European stock markets, which, according to them, would suffer serious consequences from the war in Ukraine, seems to be long gone. However, this enthusiasm must be tempered. Not all components of the indices have contributed to their rise. LVMH, for example, accounted for 21% of the rise in the CAC 40. If we add L'Oréal and Hermès, two companies in the same sector, these three stocks are responsible for 40% of the rise in the French index. The same is true, if not more so, for the S&P500. Apple, Microsoft, Nvidia, Meta (Facebook), Amazon and Alphabet (Google), i.e. six companies, have contributed to 70% of the index's rise since the beginning of the year. In short, the current economic environment is not benefiting all companies equally, which is not a good signal for the sustainability of the rebound initiated in October 2022, as few stocks are participating in the rise.

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For once, interest rates were very quiet. Both the German 10-year yield (2.31%) and its US counterpart (3.42%) ended the month of April close to their March levels. The same can be said for the short end of the curve, which is more volatile at the moment. After peaking at 4.28%, the 2-year dollar yield returned to the 4% level. This status quo keeps the inversion of the curves unchanged. The yield differential between the 10-year and the 2-year US is still around -60 basis points, while the yield differential between the 10-year and the 3-month has reached an all-time low of -166 basis points. After a rise in March linked to the debacles of some US commercial banks and Credit Suisse, credit spreads have tended to stabilise, which seems to confirm that most investors do not fear contagion and consider these bank failures as specific and isolated. However, a third commercial bank had to be rescued last month. First Republic Bank, which was also one of the "Usual Suspects" in March, was bailed out to the tune of $30 billion to keep it going by a consortium of the largest US banks including JP Morgan, Wells Fargo and Bank of America to name a few. If the market thought that this aid would be a salvation, it only allowed the bank to "hold on" for a few more weeks. The final blow came at the end of April, when investors realised that the haemorrhage of capital flight had not been stopped. At the time of its first quarter results, the bank announced that its assets under deposit had fallen by 41% to 104.5 billion dollars over the period. This was too much for the US authorities who orchestrated, through its Federal Deposit Insurance Corporation (FDIC) department, the takeover of the bank by JPM which, like most of its peers, would have had a lot to lose in the event of a failure...a feeling of déjà vu. We remain convinced that the majority of the banking sector has strong balance sheets and that the risk of contagion remains low at this stage, but it is unrealistic to believe that the capitalisation problem of US commercial banks has been resolved. Following the psychosis caused by the collapse of Lehman Brothers in 2008, we can assume that governments and central banks will do whatever is necessary to prevent another disorderly collapse of a bank.

Market developments to the end of April 2023

	Equities in Local Currencies							
End of April	MSCI World	S&P 500	EuroStoxx	CAC	Spain	Switzerland	MSCI EM	CSI 300
Perf 1 Month	1.59%	1.46%	1.03%	2.31%	0.09%	2.98%	-1.34%	-0.54%
Perf 3 Month	1.83%	2.28%	4.70%	5.78%	2.29%	1.34%	-5.28%	-3.07%
Perf YTD	8.96%	8.59%	14.91%	15.72%	12.30%	6.60%	2.16%	4.07%

	Commodities				Currencies vs EUR			
End of April	WTI Oil	Brent Oil	Gold	Copper	USD	JPY	GBP	CHF
Perf 1 Month	1.47%	-0.29%	1.05%	-4.42%	-1.64%	-3.98%	0.26%	0.69%
Perf 3 Month	-2.65%	-5.86%	3.20%	-6.80%	-1.41%	-5.83%	0.53%	0.98%
Perf YTD	-4.34%	-7.41%	9.10%	2.67%	-2.85%	-6.44%	0.97%	0.42%

	Bloomberg Indices Bonds Total returns							
End of April	Global Aggregate	US Aggregate	Euro Aggregate	US 10 Year Treasury	German 10 Year Bund	Global Credit	Global High Yield	Emerging Sovereign $
Perf 1 Month	0.44%	0.61%	0.13%	0.85%	-0.44%	1.18%	0.64%	0.39%
Perf 3 Month	0.17%	0.49%	0.00%	1.19%	-1.37%	0.77%	-0.36%	-0.63%
Perf YTD	3.46%	3.59%	2.22%	4.39%	3.29%	4.55%	3.80%	2.55%

Source: Bloomberg 30/04/23.

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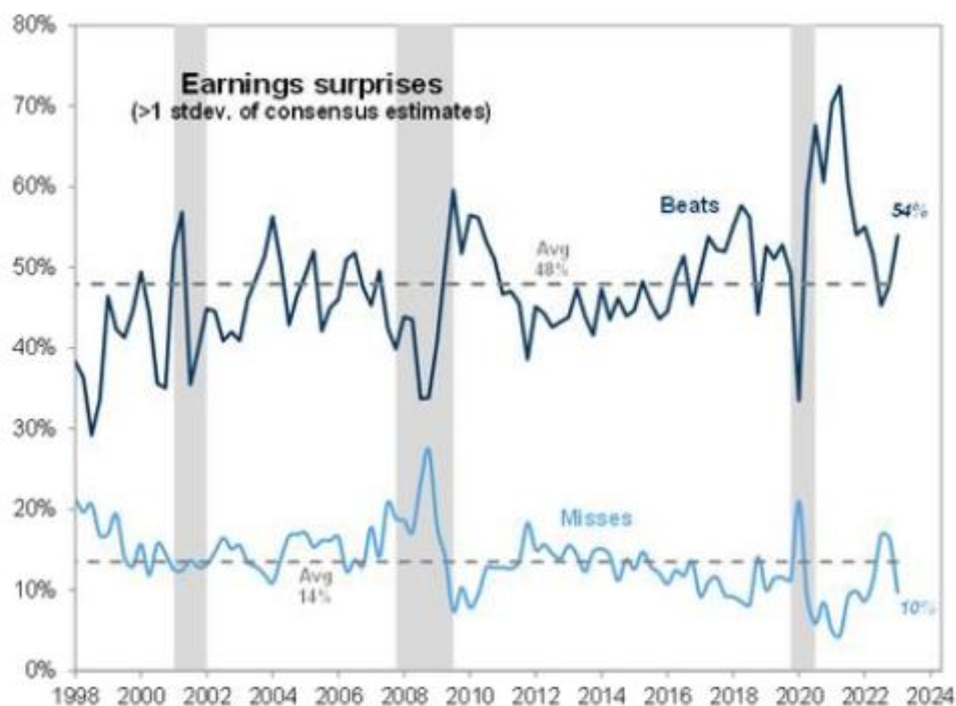
As mentioned above, the first quarter results published so far are generally good. Even though in many industries, both sales and profits are down, the damage is not as severe as expected by the consensus. This has reassured investors. Earnings growth should even return to positive territory as early as the third quarter, or at least that is what the consensus expects. Even if global demand is likely to weaken, company executives are rather optimistic about the future course of business and note that the bottleneck problems experienced in the past are gradually fading.
Well capitalised and financially sound banks had a strong quarter. These banks, which charge interest on cash and pay virtually no interest on their customers' current accounts, have made huge profits. Trading has also generated significant income since the beginning of the year. The latter are therefore back to "normal" conditions to be able to do their job. On the other hand, the credit market is struggling and many SMEs are complaining about this. Because of the rise in interest rates and the drying up of liquidity, banks are less inclined to play their role in financing projects, which complicates the lives of companies and individuals. This is also an argument used by analysts at JP Morgan and Bank of America to justify a future decline in the equity markets. Nevertheless, the sector should not rest on its laurels. Unexpected competition could emerge and take market share like Apple, which, with the help of Goldman Sachs, is now proposing to pay its customers 4.15% for their cash under certain conditions. Most US banks do not pay more than 0.45% interest per year on cash. Apple has reportedly already taken in more than $900 million in deposits in just a few days.



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Across all sectors, companies that were able to raise prices and thus cushion the negative effects of inflation fared best. In the food sector, Nestlé and Danone reported an excellent performance for the first three months of the year. The Swiss company achieved an indecent organic growth of 9.8% thanks to price increases that did not impact volumes too negatively. Both values are up 6.8% and 21% year-to-date.
Some companies have tended to "abuse" this pricing power to raise their prices more than necessary and thus increase their profits. This has been called "greedflation". Even if retail companies are mostly operating in free markets, the ethics of this practice leave a bitter taste with the public and some politicians. Indeed, in a difficult economic period for the middle class, which is suffering from a drop in purchasing power due to soaring inflation, this approach may be questionable. While many civil servants and low-income professionals are protesting in the streets for an adjustment of their salaries, large groups are taking advantage of the fact that they are increasing their prices by more than the increase in their charges. There is no need to question capitalism. However, some governments with more socialist ideologies could tackle this phenomenon if it continues.

Q1 2023 Growth

	Price	Volume
CocaCola	9.0%	3.0%
Colgate-Palmolive	12.0%	-3.5%
Conagra	15.1%	-9.0%
Hershey	8.9%	3.3%
Mondelez	16.2%	3.2%
P&G	10.0%	-3.0%
PepsiCo	16.0%	-2.0%
Unilever	10.7%	-0.2%

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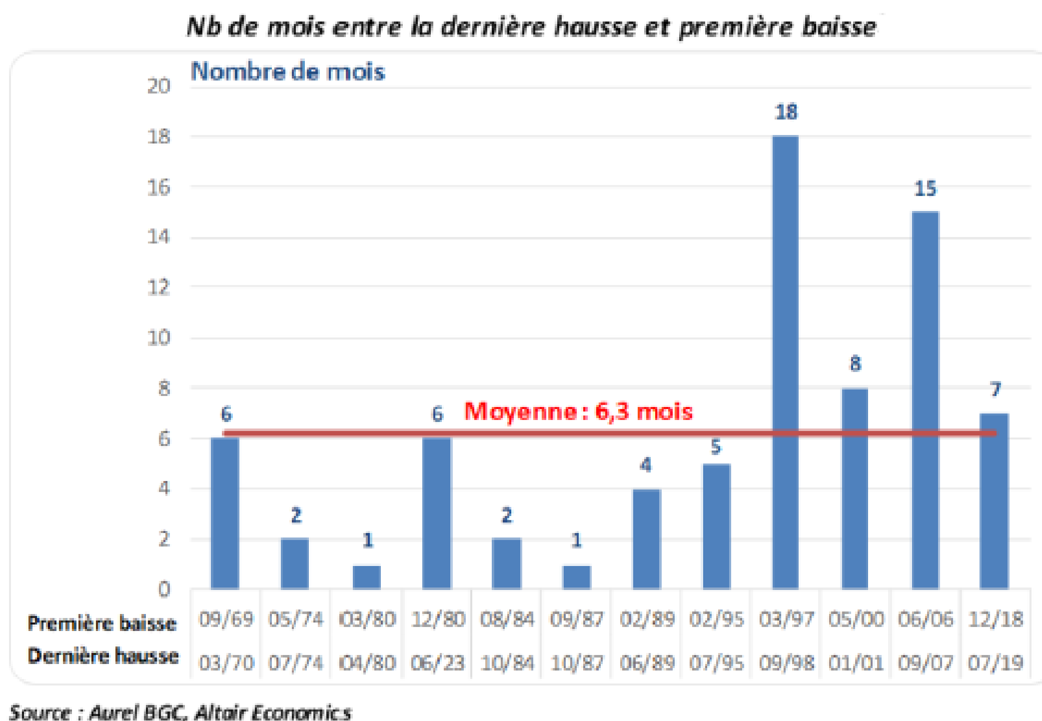
Given the importance of the impact of monetary policies on the stock markets at the moment, we have exceptionally waited for the meetings of the European Central Bank and the FED to finalize our monthly letter and give you our reactions on the spot to this week's announcements. And in the end, these long awaited meetings "gave birth to a mouse". The two main central banks of the world delivered exactly what the consensus expected, i.e. a 25 basis point increase in their key rates to bring them respectively to 5.25% for the FED and 3.75% for the ECB. The press conferences did not give much indication of their future actions. At most, the FED hinted that this could be the last hike and that a pause in the hike cycle could occur, but that no rate cuts were to be expected in the near future. The ECB, which initiated its first rate hike 4 months after the FED and which is struggling with slower inflation in the Eurozone, is expected to continue to adopt a restrictive policy in the months to come. The consensus is for a further 25bp hike at the June meeting. Even if inflation is falling, the fight against it does not seem to be over and central banks do not seem to want to lower their guard. The reaction to these announcements was therefore rather negative as investors were expecting a faster easing. Will the US commercial bank debacles muddy the waters? It should not be long before we find an answer to this question.



Source : Aurel BGC, Altair Economics

It is difficult to anticipate when the horizon will brighten, but it is clear that investors are not overly concerned at the moment. Are they blinded by seeing the glass as half full? Only time will tell.

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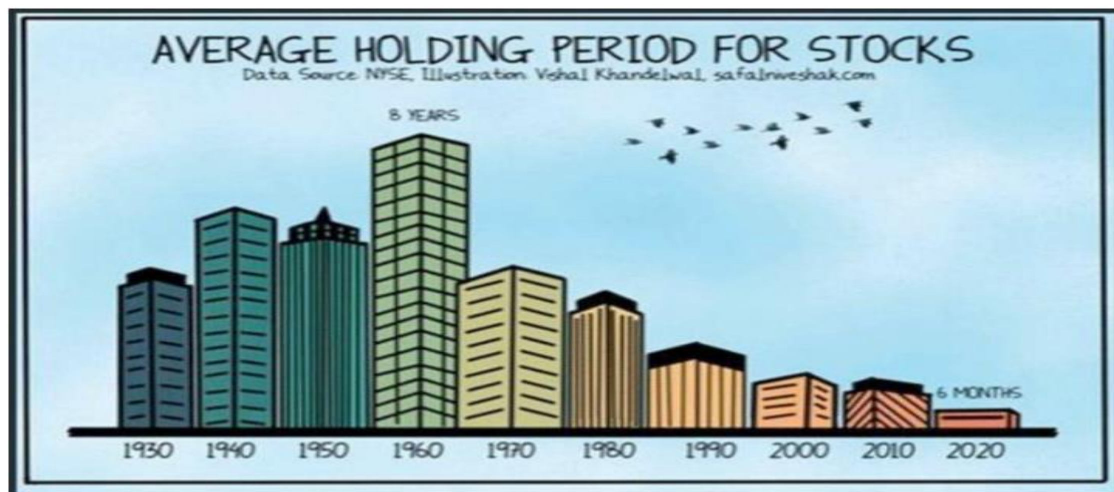
Among other things, thanks to a mild winter, we are happy to see that the worst-case scenario of electricity shortages and all the dramatic consequences that some people predicted did not materialize. However, we should not be lulled into complacency. Some areas of market stress remain very active. First of all, the debt ceiling. Mrs Yellen recently announced that a US default could occur at the beginning of June 2023. In the past, Congress has always found a solution, but sometimes it has been painful and the markets have suffered the consequences. France has been on fire since the pension reform was imposed by forceps. Moreover, the rating agency Fitch took the opportunity to downgrade its rating from AA to AA-. Some will say that this represents a cosmetic revision, but the message is not reassuring. The de-dollarization of the global economy is also a cause for concern. Not because the US dollar is losing its luster, but because a bloc of countries with increasingly strong economies and sometimes questionable ideologies are joining forces. We have seen an intensification of diplomatic relations between China, Russia, India, Brazil (the 'BRICS' of the time) but also countries like Saudi Arabia, which are setting up an alliance to reduce their dependence on the US dollar in their trade transactions. We cannot imagine that this will not increase geopolitical tensions in the long run, given that these are not at their best at the moment.

In conclusion, we reiterate our belief that investment diversification is essential to cope with all market phases. The use of decorrelated investments also makes a positive contribution to the risk/return ratio of portfolios. In this respect, we have recently identified alternative strategies that are worth investigating. The entire Weisshorn team would be happy to discuss these in more detail.

We wish you a wonderful month of May.



Source: Compounding Quality

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