

# Our View in June

11. June 2024



# Our View in June

**The euphoria regarding artificial intelligence (AI) knows no bounds. The situation is different when looking at the global political stage, where concerns and uncertainties dominate. We take both topics seriously.**

The biggest, but not the only, beneficiary of the AI boom is Nvidia. It has become difficult to compare the meteoric rise of the stock. Only Microsoft is sporting a larger market capitalisation by now, but Nvidia is not trailing far.

Recently, the shares of the semiconductor manufacturer were split. Instead of approximately 1'200 US dollars a share, they now trade at about 120 dollars. Theoretically, a split does not change anything, but practically, it does. The stock appears more affordable, a purely psychological phenomenon.

In general, there are a lot of things in financial markets that have to do with psychology. As fabulous as the Nvidia success story is. It can also trigger stress for investors.

Specifically, if you have missed out on the fantastic run.

This may tempt investors to ignore the risks and buy the name just to be part of the success story. But it may also be paralyzing, because you keep looking for all sorts of reasons why this will end badly. We will only know at some point in the future.

But if in doubt, why not decide on the middle way? This is also true when assessing the current geopolitical conflicts. Investors cannot avoid them. And it is not advisable, on the other hand, to assume that everything will always turn out well.

The good news is that uncertainties and psychological pitfalls can be avoided. The easiest way is to invest in a diversified manner. That's why we hold gold in the portfolio and have increased the weighting of this position to neutral. You will soon find more such tips in our investment magazine Telescope (to be published mid-June).

Dr. Felix Brill, **Chief Investment Officer**

# Our View on the Portfolio



- Attractive yields for **money market investments**
- High-yield bonds with **short maturity**
- **Chinese equities** still with potential



- **Inflation concerns** could increase again
- Demanding **equity valuations**
- Low **volatility** can be deceptive

- ● ● ● ● strong overweight
- ● ● ○ ○ neutral
- ○ ○ ○ ○ strong underweight

(Base: Mandate CHF balanced)

## Money Market



## Bonds



- Government Bonds
- Corporate Bonds
- USD Bonds
- Emerging Market Bonds



## Equities



- Equities Switzerland
- Equities Europe
- Equities USA
- Equities Japan
- Equities Emerging Markets
- Equities World and Themes



## Alternative Investments



- Hedge Funds
- Insurance-linked Securities
- Convertible Bonds
- Gold



# Our View on Monetary Policy



- Inflation in the eurozone continues to fall, giving the ECB further **room to cut interest rates**
- If the **rise in rents** in the US flattens out and, as a result, the inflation rate is falling, the Fed may cut interest rates at the end of the year



- Unexpected significant **second-round effects** could rekindle inflation and stand in the way of interest rate cuts
- Continued **solid growth in the US** could delay monetary policy easing by the Fed

## ECB on course to cut interest rates more

The European Central Bank (ECB) has done it: after raising interest rates at record speed, the monetary authorities decided to cut interest rates for the first time in June. Despite better early indicators, the eurozone economy is still weakening, while the inflation rate is close to the ECB's target of 2%. The traffic light was therefore green in June for the first monetary easing since 2019. Further interest rate cuts will follow. However, it is quite possible that the ECB will take a less pronounced approach than previously assumed. It is also conceivable, judging by the statements during the last press conference, that monetary easing will be based on the ECB projections. These are available in September and December, which would imply only two further interest rate cuts over the course of this year.

# Our View on the Economy



- Signals for **better economic development** in the eurozone
- Sentiment in **manufacturing stabilises**, albeit at low levels



- **Disinflation process** in the US is stalling, meaning that interest rates will remain higher for longer
- Despite the improved outlook, the **global economic situation** remains fragile - also due to geopolitics

## USA: Cracks in the economic picture

Despite record interest rate hikes, the US economy proved to be extremely robust. In 2023, US gross domestic product grew by 2.5 % and, in the first quarter, at an annualised rate of 3 % compared to the previous quarter, was still growing rapidly. In the current second quarter, the growth rate could be even higher. This contrasts with a series of economic data in recent weeks, which were significantly weaker than expected. In particular, the ISM purchasing managers' indices for the industry and the service sector, important leading indicators for the economy, fell significantly. The companies surveyed stated that they were reducing their employment figures. It is therefore possible that a deterioration in the labour market will also lead to weaker consumption in the coming quarters. So there are cracks in the economic picture.

# Our View on Government Bonds



- Fed recently stuck to the wording that **interest rates will fall in 2024**
- **We see record high forward sales** of US government bonds as a contraindicator, i.e. in favour of falling yields



- Easing **Economic concerns** could cause yields at the long end of the yield curve to rise
- The Fed **could hike interest rates** further, if inflationary pressure increases

## Foreseeable path of US yields

The path of US government bond yields is currently easy to understand: Poor economic data leads to a fall in yields and vice versa. As some US economic indicators were negative in May and yields initially fell again, they rose again somewhat after the surprisingly strong labour market report for May. If the economic data continues to be favourable, the potential for a significant rise in yields still seems low to us. The longer interest rates remain high in the US, the stronger the economic downturn is likely to be at a later date, which would result in significant interest rate cuts. This thinking is shared widely on financial markets. Even an unlikely interest rate hike by the Fed would not push yields significantly higher.

# Our View on Corporate Bonds



- **Solid US labour market**
- **Soft data** significantly worse than reality
- **Credit risk more attractive** than duration risk



- **US elections** promise to be close
- **Budget deficits** are not sustainable in the long term
- **Inflation risks** remain

## Poor sentiment in soft data

Macroeconomic surprises (as measured by Bloomberg Growth Surprise) for the US are currently as bad as they were at the outbreak of the Covid pandemic. By contrast, the surprises in the inflation data were on the positive side. Many expectations are formed from surveys, so-called soft data. It can be deduced that Republicans were significantly more optimistic about the economy than Democrats during Donald Trump's time in office. Now it is the other way round. In any case, the hard data, such as that from the labour market, does not signal any weakness in growth. We feel we are on the safe side with shorter maturities and more credit risk. Bonds with short maturities are less exposed to strong interest rate movements. At the same time, we do not expect a sharp rise in credit defaults. And the yields of just under 8% in US dollars can cushion some of the impact.

# Our View on Equities

● ● ○ ○ ○  
underweight



- **The global economy** provides tailwind
- **Hype surrounding artificial intelligence** drives indices
- **Corporate profits** and **share buybacks** are supporting



- **Market breadth** is slimming
- **Best seasonal market phase** is over
- Relatively **high valuations**
- Stubborn inflation in the US is curbing **interest rate cut fantasy**

## The AI hype

The global stock market has seen a pleasing rise in share prices year to date, although the expected interest rate cuts in the US have been postponed. It is striking that the recent rise in share prices has been driven by just a few stocks. The best example is semiconductor manufacturer Nvidia, a beneficiary of the artificial intelligence trend. The index heavyweight has seen its share price explode this year and this a key driver of the upward trend. This explains the weaker performance of the equal weight indices. A rise in the index driven by fewer and fewer shares is generally a sign of market instability and should be regarded as a warning signal. It is important to stay with the upward trend, but to monitor factors influencing the market very closely. In phases of higher market valuations, the margin of error is small.

# Our View on Equities Europe



neutral



- Early indicators send positive signals
- Prospect of further **ECB easing**
- Comparatively **attractive valuation**



- **Artificial intelligence** underrepresented
- **More cyclical** and therefore more dependent on the economic path

## Leading indicators show upward momentum

When it comes to artificial intelligence, Nvidia is the biggest beneficiary. The US semiconductor manufacturer is the AI flagship company and its shares are driving the US stock markets. Europe is less well positioned when it comes to the sector information technology. The economies and stock markets of the old continent are rather industry-biased. Although the PMIs for manufacturing in continental Europe are still in a contraction phase, they have been pointing upwards for some time. This, together with the prospect of more interest rate cuts by the European Central Bank (ECB) and the significantly more favourable valuation compared to the US creates favourable conditions for European equity markets. This has already paid off in the current quarter, with the broad European index Stoxx 600 outperforming its US counterpart, the S&P 500.

# Our View on Commodities



- **Interest rate cuts and ambitious climate targets** increase demand for metals
- **Protection against resurgent inflation**
- **Long lead times** for the opening of new mines



- China's economy as **the largest consumer of raw materials continues to weaken**
- Markets **still well supplied**
- **Strong price movements** in recent months

## Boom

After a two-year consolidation, some commodities have risen sharply since the beginning of the year. Prices are not only driven by rising energy prices - commodity production is generally considered to be very energy-intensive. In the case of agricultural commodities such as cocoa or wheat, for example, it was weather effects, which triggered strong price movements. Meanwhile, concerns about a medium-term shortage of critical metals for the energy transition remain high. The consumption of minerals such as copper, silver and nickel is likely to increase significantly if governments stick to their ambitious climate targets. Takeover speculation among mine operators is also fuelling the prospect of low supply growth. We do not yet see any acute shortages, but the prospect of interest rate cuts and a recovery in China could fuel demand and thus prices. In addition, commodities also offer protection against the resurgence of inflation.

# Our View on Currencies



- **Dollar** will remain in demand due to economic uncertainty and monetary policy upheaval
- **The Swiss franc** remains well supported, even by the weak economic situation in the eurozone



- The **euro** no longer has any support from the monetary policy side
- **Potential for emerging market currencies** remains limited due to geopolitical risks
- **Yen** is losing ground as a result of Japan's still very expansionary monetary policy

## Focus on the yen

The trading range for the EUR/USD currency pair has been roughly between 1.05 and 1.10 for a year and a half. Trading between the euro and the dollar is therefore not one of the focal points on currency markets. This applies much more to the Japanese yen. It has been depreciating against the dollar for almost four years now and has reached critical levels in the eyes of the Central Bank of Japan and politicians. This has forced the Ministry of Finance to intervene in the foreign exchange market. In Japan, currency interventions are carried out in the name of and on the instructions of the Ministry of Finance. However, the interventions have so far only prevented the yen from depreciating even further. But there has not been any appreciation. As Japan's monetary policy remains very loose, the yen will probably only benefit if the dollar weakens. A weaker dollar, in turn, would presumably require a reduction in interest rates in the US.

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