CITĒ GESTION
PRIVATE BANK

Newsletter: At the top of hiking / January 2024

1. Macro and Rates
2. Fixed Income
3. Equity
4. FX and Commodities

Key Take-Aways

- Despite experiencing four rate hikes in 2023 (+100bps), resilience in economic data and decent earnings seasons have fueled a favorable financial year, leading to central banks hitting pause.
- Financial markets have embraced the idea of a soft landing combined with moderating inflation and slowing but positive GDP growth.
- Markets currently price a 75% chance of a first rate-cut by the Fed in March and a 100% chance of a first cut by May. For the whole of 2024, investors bet on more than 6 cuts as of writing which would bring the Fed rate down to 3.875% by December 2024.
- 2023 was a good year for bond total returns, but most of the performance was generated in the last two months of the year.
- With continuing inflation reduction and the scenario of falling interest rates materializing, flows should continue to move from money market funds to riskier assets like bonds and stocks.
- Geopolitical tensions remain, with oil potentially experiencing volatility. In addition to ongoing armed conflicts, the second half of the year could be tumultuous with a U.S. presidential election that looks as disputed as it is uncertain.
- The US dollar appears poised to start 2024 with increasing signs of decline. It posted its worst yearly performance since 2020, reflecting a 5.50% drop in the dollar index (DXY) from its October peak at 107.34.
- The EUR has started the year above the psychological resistance at 1.10 against the USD, while the YPY currently trades around 142 after reaching a 32-year high of 151.9 in October. The Swiss Franc is expected to remain strong against the USD and the EUR toward 2024.
- After a strong comeback in 2023, gold stands to benefit further in 2024 due to potential rate cuts and worsening global geopolitical conditions, increasing safe-haven demand.

Review

December's Overview

2023 was a volatile year for equities, with the Russo-Ukrainian war continuing, China's economic recovery failing to materialise, bank failures in the USA and the purchase of Credit Suisse by its competitor, UBS. Or the outbreak of conflict between Israel and Palestine. The bond market was not exactly calm either, with the US yield curve rising by more than 111 basis points on the intermediate to long end, before finally returning to its starting point.
All this was largely offset by the fact that rates in the US and Europe reached their peak, with the hope that they would soon come down, by the advent of AI or simply by the resilience of the US economy.

In terms of equity indexes, the S&P500 rose by 4.53% in December and ended 2023 up 26.26%, while the Nasdaq Composite gained 5.62% to end 2023 up 44.70%. The Dow Jones ended the year up 16.88%, thanks to a strong 12.23% rise in December. The EuroStoxx50 ended the month up 3.22%, the CAC 40 and DAX 3.31%, with annual performances of 23.21%, 20.10% and 20.31% respectively. Only the FTSE 100 and the SMI ended the year up by less than 10%, with the former up by 7.68% and the latter by 7.06%.

In Asia, the Nikkei ended the month flat at 0.04% and the CSI 300 at -1.76%, ending the year in mixed fashion with Japan up 30.90% and China down 9.14%.

In fixed income, the global indices ended the year up, with the Bloomberg Global Aggregate index up +5.72%, the EMBI index up +10.45% and the BBG Global High Yield up +14.04%. In Europe, the BBG Euro Aggregate index ended up 7.19%.

The DXY index eased by -2.09% in December, to end the year at 101.333 (-2.11% YTD).

The US 10-years yield ended the month down 45bps, ending the year exactly where it ended 2022.

The Swiss 10-years contracted by 17bps, the Bund by 42bps and the UK Gilt by 64bps. All saw their yields contract in 2023.

The Bloomberg Commodity index contracted by 3.10%, to end the year at -12.55%.

The VIX lost 0.49 points to close 2023 at 12.5, close to its annual lows.

Equity % Change	Price	1 day	5 days	MTD	QTD	YTD	EST P/E
S&P 500	4,770	-0.28	0.34	4.53	11.68	26.26	20
Nasdaq	15,011	-0.55	0.17	5.62	13.84	44.70	29
Russell 2000	2,027	-1.52	-0.26	12.23	14.02	16.88	21
Euro Stoxx 50	4,521	0.16	-0.00	3.22	8.64	23.21	12
Stoxx 600 EUR	479	0.19	0.30	3.85	6.77	16.63	13
FTSE 100	7,733	0.14	0.47	3.85	2.31	7.68	10
SMI	11,138	0.73	-0.14	2.61	1.59	7.06	17
NIKKEI 225	33,464	-0.22	1.00	0.04	5.16	30.90	21
CSI 300 China	3,431	0.49	2.82	-1.76	-6.81	-9.14	10
MSCI EM Index	1,024	0.09	3.18	3.88	7.85	10.12	12

Equity % Change	Price	1 day	5 days	MTD	QTD	YTD	EST P/E
S&P 500	4,770	-0.28	0.34	4.53	11.68	26.26	20
UTILITIES	322	-0.09	1.21	1.91	8.56	-7.08	16
ENERGY	640	-0.24	-1.37	-0.08	-6.99	-1.42	11
TELECOM	246	-0.50	-0.40	4.81	10.95	55.80	18
CONS STAPLES	762	0.16	1.11	2.67	5.54	0.52	19
REAL ESTATE	252	-1.09	0.84	8.70	18.83	12.27	19
CONS DISCRET	1,418	-0.63	-0.43	6.10	12.42	42.30	25
MATERIALS	540	-0.35	-0.07	4.56	9.69	12.55	19
HEALTH CARE	1,590	0.04	0.97	4.30	6.41	2.06	19
INFO TECH	3,397	-0.28	0.27	3.83	17.17	57.84	27
FINANCIALS	626	-0.27	0.74	5.36	13.98	12.10	15
INDUSTRIALS	965	-0.20	0.74	6.96	13.00	18.08	20

Currency % Change	Price	1 day	5 days	MTD	QTD	YTD
DXY	101.333	0.10	-0.36	-2.09	-4.56	-2.11
EUR-USD	1.1039	-0.20	0.23	1.39	4.41	3.12
USD-JPY	141.04	-0.26	-0.96	-4.83	-5.58	7.57
USD-CHF	0.8414	-0.40	-1.66	-3.86	-8.07	-8.99
EUR-CHF	0.9289	-0.61	-1.43	-2.52	-4.01	-6.13
GBP-USD	1.2731	-0.02	0.24	0.85	4.36	5.36
EUR-GBP	0.8669	-0.21	-0.01	0.51	0.03	-2.08
JP EM FX Index	48.14	0.13	0.39	0.49	2.35	-3.53

10 yr Yield Bps Change	Price	1 day	5 days	MTD	QTD	YTD
US	3.88	3	-2	-45	0	0
Germany	2.02	8	4	-42	-55	-55
UK	3.54	4	3	-64	-14	-14
SWITZERLAND	0.70	3	-0	-17	-92	-92
Japan	0.61	2	-1	-6	19	19
US IG Spread	105	1	-2	-4	-38	-38
US High Yield spread	371	6	-7	-38	-138	-138
EUR High Yield spread	392	-5	-2	-25	-109	-109

Commodity % Change	Price	1 day	5 days	MTD	QTD	YTD
BBG Commo Index	98.6	-0.92	-0.71	-3.10	-5.91	-12.55
Gold Spot $/OZ	2063.0	-0.13	0.48	1.30	11.60	13.10
Crude Oil WTI	71.7	-0.17	-2.20	-5.67	-21.08	-10.73

Volatility	Price	1 day	5 days	MTD	QTD	YTD
VIX	12.5	-0.02	-0.58	-0.47	-28.94	-9.22

Source: Bloomberg 12/30/2023

Macro & Rates
Growth Amidst Inflation

Despite experiencing four rate hikes in 2023 (+100bps), resilience in economic data and decent earnings seasons have fueled a favorable financial year.

2023 has been spectacular for investors, with all asset classes performing positively. Following the declines seen in September and October, November and December witnessed a remarkable performance, contributing to 80% of the year's returns. Due to high volatility and brutal shifts in terms of scenario and market reaction, 2023 has been a terrible year for economists and forecasters as both the economy and financial markets outperformed most of the predictions that were made a year ago, with the S&P 500 up by approximately 24% over the year.

Central banks are pausing for sure, backed by a slowdown in inflation trends and encouraging macroeconomic data.

The latest dot plot indicates that FED economists expect rate cuts over the coming three years to bring the overnight borrowing rate back down near the long-run range of 2%. During its final meeting of 2023, the FED held its key interest rate steady for the third straight time, citing "clear progress" made against inflation. Nevertheless, the Federal Reserve also noted a small upside miss from expectations, with headline inflation at 3.1% for the 12 months ending November, as well as uneven progress across various sectors. While growth rates of energy and core goods prices slowed, core services continued to rise. FED officials reiterated the necessity of maintaining a restrictive monetary policy stance until inflation shows a sustained downward trend in line with the Committee's objectives. This process may take longer than what the market originally anticipated, as core inflation over the last 12 months is at 3.9% in December, remaining relatively stable around 4% for several months now. The January CPI release highlighted the continued presence of inflation, with headline inflation at 3.4% for the 12 months ending December, up from 30 bps compared to November.

The latest GDPNow projection has adjusted the Q4 2023 economic growth rate to an annualized 2.5%, up from the initial 2% prediction, reflecting robust consumer spending and increased investment. This update follows a deceleration from Q3 2023's 5.2% growth rate. Overall, the economy is expected to have expanded by 2.4% throughout 2023. The December US PMI Manufacturing Index dropped to 47.9, suggesting a contraction in manufacturing, while the US PMI Services Index rose to 51.4, indicating a slight acceleration of growth in the services economy in December. According to the latest Job Openings and Labor Turnover Survey, November's job market cooled, with the lowest monthly demand for workers in over 2.5 years and a slight reduction in openings and hires, which may ease wage pressures and contribute to the moderation of inflation. Despite this cooling, December saw the creation of 216,000 jobs, holding the unemployment rate steady at 3.7%. The 0.4% drop in average hourly earnings from the previous month, coupled with the recent Job Openings and Labor Turnover Survey, suggests a potential easing of inflationary pressures.

For now, financial markets have embraced the idea of a soft landing combined with moderating inflation and slowing but still positive GDP growth.

This scenario seems today consensual, and we do not intend to contradict it. However, it is essential to emphasize that this optimistic scenario will likely face challenges throughout the year, given that it is already fully reflected and generously priced into most asset classes. The Fed has pre-committed to three rate cuts for 2024 (-75bps) but uncertainty surrounds their timing. In the meantime, the market is currently predicting that Powell may implement more than twice rate cuts (-160bps). At some point, financial markets will confront painful adjustments.

Regardless of a critical 2023 financial year for China, several indicators suggest a cautiously optimistic outlook for 2024.

China's exit from zero-COVID has not been without its challenges. The journey toward recovery included comparative analyses with Japan's post-1990s economic trajectory, debt risks, and new reforms in the housing sector. Despite a less robust post-COVID consumption rebound and a 42% decline from its 2021 peak in the CSI 300 Index, factors such as attractive valuations, low investor positioning, accelerating policy support, and improving earnings momentum offer optimism for China's equity market for 2024.

Fixed Income

A historic December for Bonds

In terms of yield, the US 10-year Treasury ended the year exactly where it began it: 3.87%. The movement over the year, however, was huge. Firstly, yields rose rapidly to reach 5% in October only to rally back down towards year-end. The first chart on the right hand shows the 10-year Treasury yield (log-scale) over a longer time period. The recent rally in yields is clearly small in comparison to both, the previous multi-decade fall in yields and the sharp rise since 2020.

While 2023 was finally a good year for bond total returns, most of the performance was generated in the last two months of the year. The Bloomberg Global Aggregate Treasury Total Return Index for example would have ended the year in negative territory without the performance contribution of December. Looking at rolling 3-year total returns of longer bonds, the last two years are still among the worst ever for US bonds (-26.46% as of 2022 and -17.52% as of 2023).

In spite of softening US macro data, most economists still don't expect a recession within 12 months: according to a Bloomberg survey at the beginning of December 2023, 49% expect a soft landing, 19% a hard landing without a recession and only 32% a recession. In a Bank of America survey of fund managers in December 2023, 66% expected a soft landing for 2024.

Currently, markets price a 75% chance of a first rate-cut by the Fed in March and a 100% chance of a first cut by May. For the whole of 2024, investors bet on more than 6 cuts as of writing which would bring the Fed rate down to 3.875% by December 2024.

There are good reasons to believe in this scenario. US CPI has come down and is approaching the Fed's 2% target. Moreover, money supply is falling and easing supply bottlenecks – still in normalization after the pandemic – are also disinflationary. On the other hand, there are multiple risks which might currently be underpriced by the market.

Firstly, an inverted yield curve has historically been followed by recession on average 257 days after its initial inversion. Now, the US yield curve is inverted for 394 days. Secondly, it is not clear whether inflation has really bottomed, or at least whether it won't rise again on the back of a still strong labor market and rising geo-political tension weighing on global supply-chains. Thirdly, if «the Fed has hiked too much» over a short period of time, something else «has broken» many times in the past... leading to recessions.

If anything, the price-action since the beginning of the year has indicated a somewhat more cautious stance of investors and a certain «return to the mean». We still believe that 2024 will be a good year for bonds, but it may well be a bumpy road with various obstacles rather than an easy ride!

US 10-year Treasury yield, log-scale

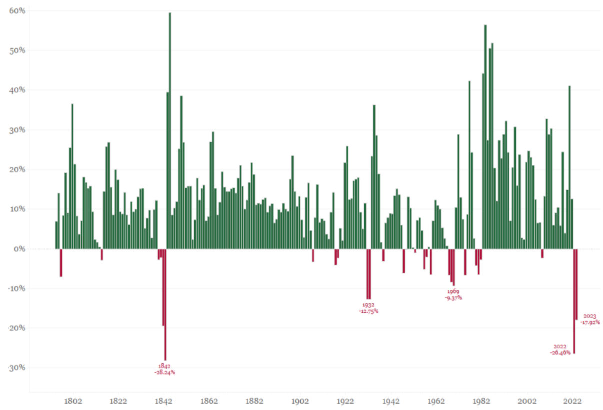
Source: Bianco Research LLC

Fixed Income Total Returns as of 29.12.2023

Index Name	Ticker	MTD Rtn	YTD Rtn
EM USD Aggregate	EMUSTRUU	4.20%	9.09%
Euro-Aggregate	LBEATREU	3.33%	7.19%
Global Aggregate	LEGATRUU	4.16%	5.72%
Global High Yield	LG30TRUU	4.03%	14.04%
Global Inflation-Linked	LF94TRUU	4.44%	5.77%
Pan-Euro Aggregate	LP06TREU	3.56%	7.49%
Pan-European High Yield	LP01TREU	2.85%	12.78%
Treasuries	LGTRTRUU	4.30%	4.18%
US Aggregate	LBUSTRUU	3.83%	5.53%
US Corporate High Yield	LF98TRUU	3.73%	13.44%
US Treasury	LUATTRUU	3.36%	4.05%

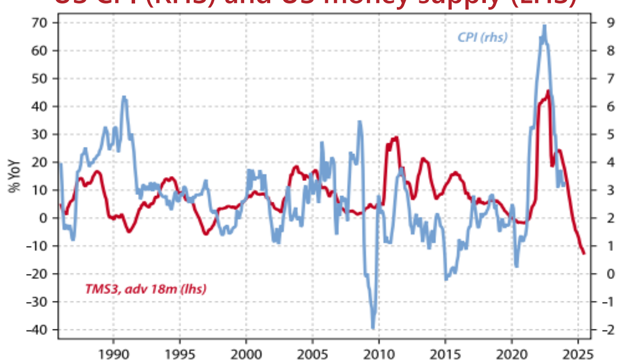
Source: Bloomberg

Rolling 3yr US LT Nominal Bond tot. returns



Source: Bianco Research LLC

US CPI (RHS) and US money supply (LHS)



Source: Gavekal

Equity

"What a year!" (1/2)

Equity markets ended December at their highest point of the year on almost every continent. 2023 was an excellent vintage, despite initial fears about the economy. All eyes now turn to 2024.

What can we expect in 2024?

Once again, a lot of volatility, and perhaps even more than in 2023 where, apart from the March crisis over Silicon Valley Bank and Credit Suisse, the markets did not face any major shocks.

With continuing inflation reduction and the scenario of falling interest rates materializing, flows should continue to move from money market funds to riskier assets like bonds and stocks.

Are we safe from geopolitical tensions? Certainly not, and that is why oil could still experience volatility. In addition to ongoing armed conflicts, the second half of the year could be tumultuous with a U.S. presidential election that looks as disputed as it is uncertain. While some say this type of election does not ultimately impact equity markets, apart from potential fiscal stimulus, many have quickly forgotten that only 537 votes separated George W. Bush from Al Gore in a country of 300 million people back in 2000 (the Florida recount). Would Al Gore have initiated the 2nd Gulf War as Commander in chief? The world as we have known it for the past 20 years might have been very different.

While savvy investors can protect their equity portfolios from volatility with low-cost hedging strategies (selling Call options and buying Put), others can accept volatility by picking top performing fund managers who actively manage portfolios, as opposed to index funds (ETFs), so called passive management.

Hedge Funds ? It is also possible to turn to alternative funds at the risk of some disappointments. The 2023 vintage of this asset class have been very uneven despite strong equity markets with many funds failing to return better than money market funds.

Equally Weighted S&P 500 starts outperforming

We wrote last month that the S&P 500 equally weighted and the S&P 500 were neck-and-neck in terms of performance in November. This is no longer true. Since November, the equally weighted index returned 8.52% versus 5.21 % for the S&P 500. It still underperformed significantly in 2023: 12.50% less than the S&P 500.

This is to remind us that Big Tech is a significant component of the US equity index.

Artificial Intelligence, Robotics and Cybersecurity can no longer be ignored

There is one reason to it. This theme is an important growth driver and many companies in this sector are very profitable, far from the hype of the 1999/2000 years and the internet bubble. It is difficult to talk about a bubble on Nvidia, which cost 25 times its 12 months forward PE: The same with Crowdstrike and Datadog, which respectively cost 73 and 71 times their 12 months forward earnings.

These levels are far from what we experienced at the turn of the last century. AI is already a reality in our daily lives. We all speak regularly with chatbots. The same goes for cybersecurity. Daily cyber attacks against infrastructures and the debate around the integrity of our personal data are a regular reminder.

Yes, it is difficult today to build an equity portfolio without exposure to this theme despite its significant underlying volatility.

Real estate is back. Already ?

Real estate should continue to benefit from falling interest rates next year everywhere. Since September, we have regularly (and successfully!) talked here about the potential for Swiss real estate, a country where long-term interest rates have risen little compared to the rest of Europe or the US. Switzerland remains a very specific market where real estate companies are less indebted than elsewhere and therefore less subject to the volatility of interest rates.

Among European real estate companies, Unibail-Rodamco-Westfield should, like others, benefit from the return of dividends even if the stock already rebounded 58% since the low reached late October. The same goes for Vonovia in Germany in the residential area which has recovered 83% since the end of March bottom.

Caution: Some real estate companies will struggle to renew their debts that are coming due. The risk of dilution is significant for equity holder. And in a world where companies reduce office space, some will suffer more than others. Stock picking is key.

Equity
"What a year!" (2/2)

China... too late to sell or too early to buy?

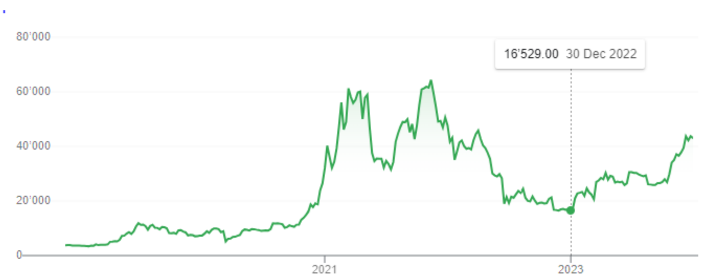
China is like Ali Baba. We keep hearing that the company is undervalued in relation to its American rivals and worth a fraction of Apple, but it continues to fall like a stone into a bottomless pit. How far down it can go? Are we naive enough to think that there's a trampoline at the bottom ? Some will sell and go away, some will stay.

At these levels, the question is not much about the valuation of the Chinese market but the policy of the government. Just when you thought China was done with annoying Baba, the government attacked Tencent this month and the gaming industry.

None of this will help to bring foreign inflows back into Chinese equities and thus boost cheap valuations. What is more surprising is that local investors aren't rushing into their own market either. Otherwise, given the country's population and market capitalization, equities would shake up. This being said, when the upturn finally come, it could be extreme, like a rubber band, unless... it breaks (Taiwan?).

The Russian stock market was always cheap before closing the final curtain to foreign investors.

Ali Baba stock in HKD



All charts - Source: Google.com

2024: Crypto to the roof ?

We cannot give any advice on crypto but it is unfair not to talk about it since, yes, crypto were the asset that performed the best in 2023. Solana, Cardano, Avalanche, those called the "altcoins", not just Bitcoin and Ether have rebounded strongly after losses of up to 95% in 2022-2023. Despite a massive rebound all are still very far from their all time high of 2021.

We cannot yet see the use of cryptos in our everyday lives, and this is perhaps the difference with the AI theme mentioned earlier. Apart from a few early adopters, most crypto buyers will board the train "because it's going up", and this explains the immense volatility of these unregulated and decried assets.

2024 could prove to be a major turning point, as a decision is expected on January 10: the potential authorization of the first Bitcoin Spot ETF by the SEC. If approval is granted, more than a dozen other ETFs could follow. While it is now very easy to gain exposure to the theme via ETFs or by buying the coins on specialized exchanges, there are no "spot" ETFs, i.e. those that effectively hold crypto as underlying assets and do not just own future contracts to match the performance. Spot ETFs are considered to be a game changer that could fuel inflows from institutional investors,

And this is the problem ! Arthur Hayes, founder of BitMEX recently forecasted that "If TradFi asset managers, such as Blackrock, become too successful with spot Bitcoin ETF, they will completely destroy Bitcoin". Are ETF the keys to a kind of crypto regulation? In a nutshell, the bigger they grow, the more Bitcoins in circulation will be held by ETFs, which runs against the crypto philosophy to separate from the state and finance. This could well end up being the indirect answer to the will of some governments to regulate Bitcoin..

April 2024 will see a new "Bitcoin halving" - the moment when rewards for Bitcoin miners are halved until they disappear completely when the 21 million mark is reached. Not counting those that have been lost forever by their owners.

In short, the first part of the year once again promise to be extremely volatile, both ways as news come out.

We do note that crypto can be played through listed stocks of "crypto mining " companies and exchanges.

Forex And Commodities

Confirming Signs Of Weakness For The Dollar in 2024?

The US dollar appears poised to start 2024 with increasing signs of decline. It posted its worst yearly performance since 2020, reflecting a 5.50% drop in the dollar index (DXY) from its October peak at 107.34. This decline mirrors investors' anticipation of the Federal Reserve cutting interest rates as inflation approaches the central bank's 2% annual target. Analysts predict a marked slowdown in the US economy and cooling inflation in 2024, providing the Fed with the opportunity to trim rates by H2 2024, impacting the USD negatively.

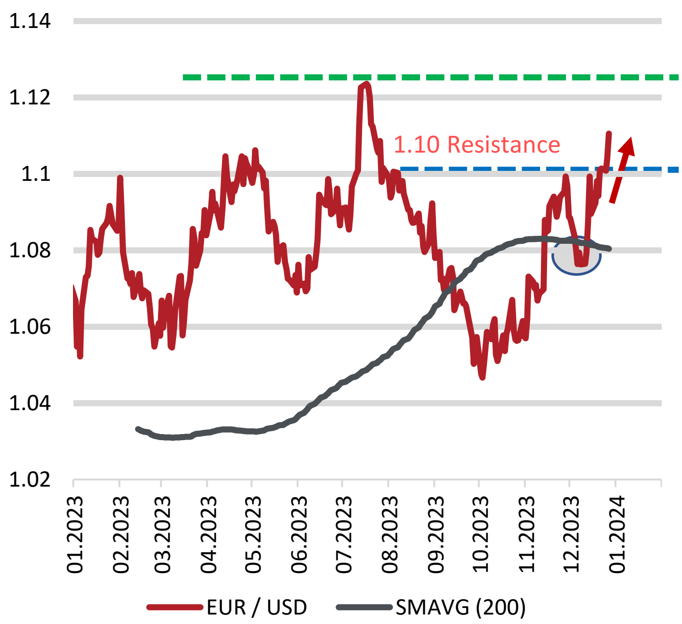
For the EUR, it has started the year above the psychological resistance at 1.10 against the USD. The next hurdle is at 1.127 (2023 peak). If this level is reached and sustained, it could bring new dynamics in 2024 for the EUR/USD pair. The role of the ECB should be monitored, as expectations for an interest rate cut in the Eurozone are uncertain. The USD's new exposure to an interest rate differential in favor of the EUR suggests that the EUR/USD pair may move to higher levels in 2024, with key support at 1.10 and the potential to reach 1.20 and beyond.

After reaching a 32-year high of 151.9 yen in October, the Japanese currency retraced to around 142. The Yen steadied on the belief that the Bank of Japan (BoJ) might end its ultra-easy policy. The 2024 forecast remains therefore positive for the Yen, especially after BoJ Governor Kazuo Ueda hinted at potential policy changes as inflation approaches the 2% target. This prospect could relieve pressure on the yen, bringing it to a more favorable territories at around 120-130 against the Dollar.

The Swiss Franc is expected to remain strong against the USD and the EUR toward 2024, with SNB interventions that should continuing at least till end of Q1. Despite entering oversold territory, the USD/CHF pair might see a slight positive boost in January, aiming to return to the historical range of 0.87–0.92. The EUR/CHF pair, although in a downtrend channel, rebounded from oversold territory at 0.94 in December, currently testing the key resistance at 0.955 (50-day SMA). The medium-term outlook suggests the EUR/CHF pair staying within a range of 0.92–0.96.

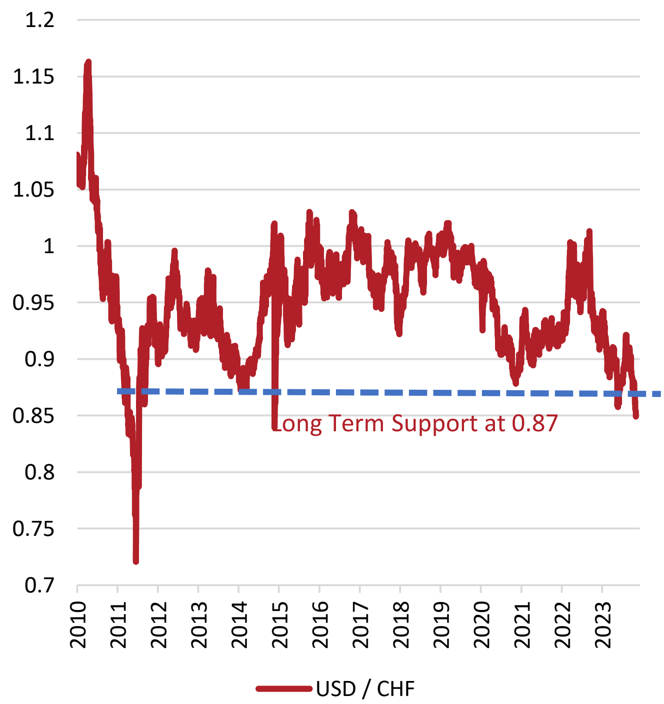
After a strong comeback in 2023, gold stands to benefit further in 2024 due to potential rate cuts and worsening global geopolitical conditions, increasing safe-haven demand. Technically, gold shows positive signals, with a break of the new high around 2100 possibly confirming a momentum pattern with a potential target of around 2400 for 2024.

EUR/USD 1.10 Resistance Broke! Next Target 1.12.



Source : Bloomberg

USD/CHF Broke The Long Term Support, Oversold Territory ?



Source : Bloomberg

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