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Investment Policy

Q3 2024 | June 2024

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Key points

Gold's new paradigm

Because it does not generate income, pay a coupon or earn dividends, Gold cannot be assigned a **"fair" value** using tried-and-tested valuation methods. Even so, we all know that its price is historically **correlated negatively to the US dollar** and **real dollar interest rates**. It also functions as a hedge against **major geopolitical risks** (**Chart 1**).

Since the beginning of 2022, in the wake of the US Fed's monetary tightening, real interest rates have risen and the dollar has appreciated. Strange, then, that gold should have gained more than 25% during this time. Granted, the wars in Ukraine (February 2022) and Gaza (October 2023) have underpinned the price move. But what really made the difference has been the **confiscation** of the Russian central bank's **foreign exchange reserves** held at the Fed (and the ECB) as part of the sanctions regime against Moscow. This decision set a legal precedent and led monetary authorities in a number of countries (China naturally but also India and Turkey) to diversify their foreign exchange reserves away from the dollar and into gold. Since then, central bank gold purchases have doubled and currently exceed 1,000 tonnes a year, representing one-quarter of global gold demand. This change is structural – a reflection of policies in some parts of the world to **break free** from the dollar's dominance. This new paradigm is long term and not only gives gold an additional performance driver, but could also lead to a reduction in its volatility.

What's more, the gold price has appreciated despite the absence of the usual **financial investors**, who in Q1 2024 sold 113 tonnes of gold in addition to 244 tonnes last year. When – as we expect – dollar yields fall further and lead the dollar lower, these investors will flock back and provide fresh impetus to the upward price move. Gold's sparkle therefore remains undimmed.

Scenario and conclusions

- **Inflation** is on the right track, despite the odd uptick along the way
- **Central banks** are embarking on monetary easing
- Economic momentum is stagnating in the US...
- ... but recovering in **Europe** and **Switzerland**
- **China** continues with measures to galvanise economy

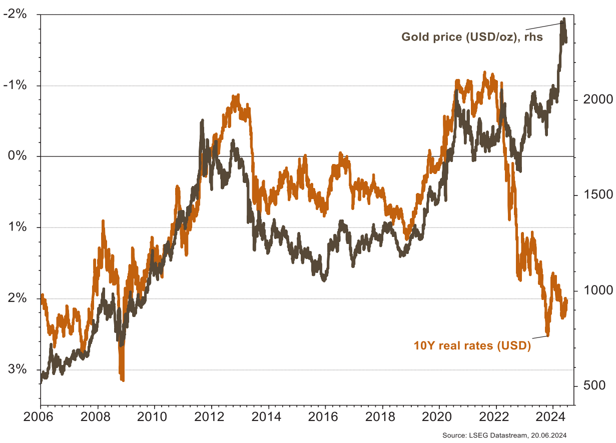
→ **Equities**: neutral, limited regional bets
→ **Bonds**: overweight (IG corporate bonds)
→ **Currencies**: preference for CHF and USD
→ **Cash**: neutral

	UW (-)		N (=)		OW (+)
Asset allocation					
Equities	□	□	■	□	□
Sovereign bonds	□	■	□	□	□
Credit	□	□	□	□	■
Alternative investments	□	□	■	□	□
Cash	□	□	■	□	□
Equities					
US	□	■	□	□	□
Europe	□	□	■	□	□
Switzerland	□	□	□	■	□
Japan	□	□	□	■	□
Emerging markets	□	□	■	□	□
Bonds					
Sovereign	□	■	□	□	□
Corporate investment grade	□	□	□	■	□
High-yield corporate	■	□	□	□	□
Emerging market sovereign (USD)	■	□	□	□	□
Emerging market sovereign (local)	■	□	□	□	□

Economy: *signs of divergence between the US and the rest of the world?*

The US economy had held up surprisingly well until recently but signs of weakness are appearing. Europe and even China are looking more promising, although growth remains lower than in the US.

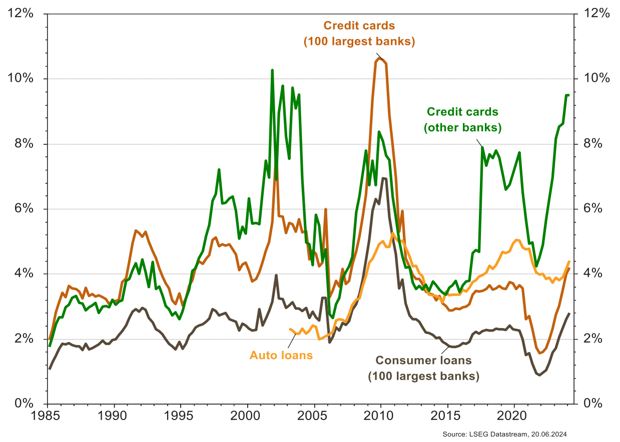
Chart 1 | Gold: correlation between price and real interest rates broken



In the **US**, some delayed effects connected with earlier interest-rate hikes are surfacing. In particular, **consumer** default rates on credit card balances at the 100 leading banks have hit their highest level in over a decade (4.2%). At the other institutions, this is 9.5% – a level not seen in 20 years (**Chart 2**). This latest indicator is a further sign that the cost of credit has become prohibitive for some consumers (APR on credit cards is 21.5%) and the excess savings accumulated by households during the pandemic are running dry. The impact on one of the **spending components** – retail sales – is already visible. Even as things stand, retail sales have been flat in real terms for the past three years. Spending on services is underpinning growth in consumer spending as a whole (+2.1% y/y in Q1 2024) for the time being, even though the pace of growth is decelerating compared with the previous quarter, when it was still 2.9% y/y. On the positive side, as long as the **labour market** – now the main source of personal income – can withstand the pressure, the risk of recession remains low. The US economy still managed to add 272,000 jobs in May, following just 165,000 in April and 310,000 in March, despite the unemployment rate edging up to 4%.

In addition, the **property** market is not showing any tangible signs of recovery. The commercial segment has been hit by higher borrowing rates. Offices have fallen victim to the teleworking trend while online sales have dragged down shopping centres. All in all, commercial segment prices have fallen by 12% since the summer of 2022. The trend remains negative just as major refinancing operations are looming on the horizon over the next two years. The regional banks are most exposed and are replenishing their reserves...

Chart 2 | US: increase in consumer credit default rate



Economic trends may have experienced some wobbles but we believe that **inflation** is reassuringly on track. Despite some monthly fluctuations previously, inflation excluding volatile items (food and energy) and home prices was 2.1% y/y in April, barely a whisker away from the Fed's target. Because of its weight within the broad

Financial markets

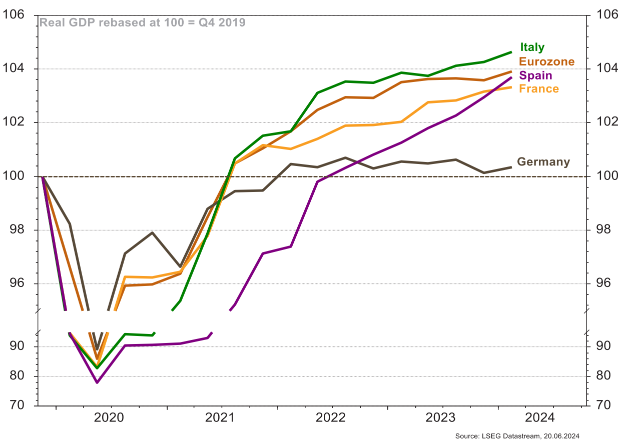
***) To 19.06.2024**	Performance			Valuation			Earnings growth			
Equity markets	Price (local currency)	Quarter Q2*)	Since 31 Dec 2023	12-month P/EPS	Dividend yield	Price/ net assets	12-month EPS	2024 EPS	2025 EPS	2026 EPS
United States	5 215.37	4.14%	14.60%	21.22	1.6%	4.8	13%	11%	15%	12%
Europe	514.13	0.28%	7.33%	13.40	3.2%	2.0	8%	5%	11%	9%
Japan	2 728.64	-1.40%	15.00%	14.80	2.1%	1.4	8%	8%	10%	9%
Switzerland	12 060.24	2.80%	8.30%	16.99	3.0%	3.8	12%	12%	13%	10%
United Kingdom	4 473.37	3.10%	5.70%	11.20	3.9%	1.8	5%	1%	8%	8%
Emerging Markets (USD)	1 095.28	4.99%	6.99%	12.12	2.8%	1.6	19%	22%	16%	11%
World (USD)	3 523.66	2.50%	11.20%	18.56	2.1%	3.3	11%	8%	13%	11%

Source: Datastream, IBES consensus

index (~35%), home prices (+5.5% y/y in April) are still the component driving inflation, at +3.4% y/y, which is still too high for the Fed's liking. Yet it's worth bearing in mind that growth in the New Tenant Rent Index, a one-year leading indicator for the home price component, slowed sharply to just 0.4% y/y in April. The **Fed** thereby has grounds to ease monetary policy in the months ahead.

Unlike the US, latest statistics in the **Eurozone** have sprung some pleasant surprises, resulting in **upward revisions** in the current-year GDP growth forecast (from +0.5% at the start of the year to +0.7%). Even in the first quarter, the Eurozone recorded forecast-beating growth (+1.3% q/q annualised) fairly evenly spread between Germany (+0.9%), France (+0.6%) and Italy (+1.4%) (**Chart 3**). Most importantly, the marked upswing in purchasing manager confidence (PMI) suggests that the trend will continue. Some might point at the manufacturing PMI, which at 47.3 was still in contraction territory (<50) in May. But this is forgetting that it is at a much higher level than last June (42.7), and the latest reading for the services PMI was 53.2, in expansion territory and by far

Chart 3 | Eurozone (real GDP): economic recovery



exceeding the reading of 47.8 in October 2023. In addition, despite inflation (+2.6% y/y) hovering above the 2% target, the monetary easing initiated in June by the **ECB** will help the recovery.

In **Switzerland**, 12-month inflation was unchanged in May at 1.4%, in line with the SNB's expectations. Swiss franc depreciation year to date has not triggered a rise in imported inflation, which is giving the central bank some wiggle room. Economic growth may be picking up in Switzerland but remains below potential due to weaknesses in the manufacturing sector. Because of that, further monetary loosening is in the pipeline. We expect two more rate cuts between now and the end of the year (to 1% in December).

In **China**, new measures to support the property sector have been announced. Admittedly, the need is huge. The sector's share of GDP has fallen from almost 20% at its peak three years ago to less than 10% today. The aim of these measures is threefold: to stimulate demand, reduce gluts and channel public funds in support of developers. As with previous measures, these are all steps in the right direction, but it's too little to reverse the trend. On the positive side, further **signs of improvement** were seen in May, especially on the foreign trade front. Exports were up 7.6% y/y, driven by tech (+13.7% y/y) and automotive (+16.5% y/y). The increases in US-imposed customs duties affect only 0.5% of exports and will have no impact on economic activity. We believe that, with monetary policy also in easing mode, China will be in a position to achieve its 5% growth target, in tandem with improving PMIs in both services and manufacturing.

10-year sovereign bonds	Level at 19.06.2024	Change Q2*) (bps)	Change since 31 Dec 2023 (bps)
USD yields – United States	4.22%	1	35
EUR yields – Germany	2.38%	10	38
JPY yields – Japan	0.93%	21	31
CHF yields – Switzerland	0.71%	0	0
GBP yields – United Kingdom	4.07%	13	47
Emerging markets (USD)	7.41%	7	9
Emerging markets (local currency)	3.97%	-3	-11
Commodities	Price	Quarter Q2*)	Since 31 Dec 2023
Gold (USD/oz)	2 325.51	5.0%	13.0%
Brent (USD/bl)	86.22	-2.3%	11.0%

FX	Level at 19.06.2024	Change Q2*)	Change since 31 Dec 2023
EUR vs. CHF	0.9505	-2.29%	2.24%
EUR vs. USD	1.0739	-0.58%	-2.79%
EUR vs. JPY	169.7321	3.84%	8.99%
EUR vs. NOK	11.3455	-3.17%	1.13%
GBP vs. EUR	1.1817	1.05%	2.41%
GBP vs. USD	1.2733	0.79%	-0.12%
USD vs. CHF	0.8843	-1.82%	5.07%
USD vs. CAD	1.3703	1.26%	3.92%
AUD vs. USD	0.6675	2.31%	-2.18%

Source: Datastream

Monetary preferences

Rank 1	Rank 2	Rank 3
Appreciation expected	Stabilisation	Depreciation expected
CHF | USD	GOLD | EUR | JPY | NOK	GBP
▪ **CHF**: haven and hedging currency, which compensates for lower yield; no longer overvalued ▪ **USD**: richly valued, but should benefit from higher yields for longer as Fed behind the curve	▪ ↑ **GOLD**: rate cuts and a depreciating dollar will provide support; role in hedging geopolitical risk ▪ **EUR**: attractively valued, but early ECB action and political haze are a hindrance ▪ **JPY**: very attractively valued; monetary tightening would be a powerful catalyst ▪ **NOK:** diversification play, correlated with the price of oil	▪ **GBP**: attractively valued but structural effects of Brexit are hurting growth potential; early parliamentary elections (in July) are adding extra volatility

Investment conclusions

A more favourable global economic momentum, with upward revisions to growth prospects except in the United States, has led us to cancel our slight underweight in equities and to be **neutral** on the asset class. The prevailing **political uncertainty** in France could act as a brake, at least temporarily, on the real potential for equity appreciation on the Old Continent. Our regional bets are therefore **limited** to a slight preference for **Japanese** equities. They should continue to benefit from an upturn as their economy emerges from deflation.

In addition, the second quarter seems to be showing a **turnaround**, or at least some stabilisation in the performance of bonds relative to equities after a period of underperformance. We expect this trend to continue, particularly in the US, where interest rates are highest and opportunities most attractive. Our overexposure to high-grade **corporate bonds** should benefit in particular from the more widespread adoption of looser monetary policies in the coming months.

To offset the low yields available on Swiss bonds, in which we are underweight in **CHF portfolios**, we have added to positions in structured products and uncorrelated hedge funds. We are also keeping the allocation to Swiss residential property unchanged as a further alternative to Swiss bonds.

Finally, the allocation to **gold** has also been raised to neutral, as gold too stands to benefit from the current easing wave and still hedges against all those geopolitical risks that simply won't go away.

Publication date | 10 June 2024

Design ClPa

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