MONTHLY HOUSE VIEW

November 2023

Should we fear soaring oil prices?

Architects of Wealth

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POLARISATION

Delphine
DI PIZIO TIGER
Global Head
of Asset Management

Dear Reader,

Against the backdrop of the ongoing war in Ukraine, the attacks in Israel by Hamas on 7 October – 50 years after the start of the Yom Kippur War – came as a surprise to the Israeli government. In an increasingly divided world, this new war was the final nail in the coffin of the Oslo Accords, signed 30 years ago with the aim of ushering in a new era of peace between Israel and Palestine.

This attack also occurred on President Vladimir Putin's birthday, who will likely want to use this conflict to exert influence in the geopolitical arena. In fact, by strengthening the western front, this war is accelerating polarisation and putting the international community's focus on Ukraine on the back burner.

This new conflict potentially puts the Abraham Accords[1] in jeopardy, just as Israel and Saudi Arabia were nearing a peace treaty signalling a new configuration of the Middle East. Furthermore, the Americans have always had trouble managing several external conflicts simultaneously. With next year's presidential election ramping up in the United States, the situation in Congress has been complicated by the historic removal of Kevin McCarthy, the Republican speaker of the House of Representatives. Although a shutdown[2] has been averted in the short term, aid for Ukraine has technically been suspended. In addition to the 43.9 billion dollars in US aid since the start of the conflict in Ukraine (i.e. 4% of the defence budget), the White House says 60 billion dollars is still needed to support the country.

The most recent survey available shows the extent to which Americans are increasingly divided on aid to Ukraine. This reluctance is particularly salient among Republican voters, with more than 60% questioning the expenditures already made since the start of the conflict. In this context, Israel can now be expected to take priority.

What will be the impact on the market?

Historically, in times of geopolitical tension, investors tend to turn to safe havens such as gold, the yen, the Swiss franc and the highest-rated government bonds. Indeed, this trend became evident soon after the attack, most prominently with gold. Conflicts in the Middle East generally cause volatility and put pressure on energy prices because the region is not only a significant exporter of energy but also the site of strategic sea passages, including the Strait of Hormuz. The market is expected to stay focused on energy risk. Oil and gas prices could remain under pressure and show volatility as we enter the winter months. Risks to global growth could materialise if Israel enters into direct conflict with Iran, bringing the price of a barrel of oil to well above 100 dollars. Such an extension of the war is not our scenario.

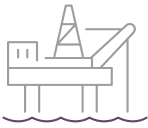
To learn more about our analyses, I encourage you to read this issue which looks specifically at the impacts of this crisis on oil prices and at our economy's reduced dependence on black gold.

1 - Abraham Accords: signed starting in 2020, these are US-brokered agreements to normalise relations between Israel and the United Arab Emirates, Bahrain, Sudan, and Morocco.
2 - Shutdown: this is what happens when the US government ceases to operate because Congress has failed to pass funding bills. When there is a shutdown, the debt ceiling is no longer raised, which forces the government to start shutting down what it views as non-essential services (museums and national parks, for example) that it can no longer fund.

SHOULD WE FEAR SOARING OIL PRICES?

Nicolas MOUGEOT
Head of Investment Strategy
& Sustainability

Geopolitical events that could affect energy prices have been front and centre in recent months. Russia invaded Ukraine in 2022, and in 2023 the Nagorno-Karabakh conflict flared up again between Armenia and Azerbaijan, an exporter of oil and gas. In recent weeks, Hamas's attack on Israel has increased fears of a Middle East conflict that could drive oil prices higher. So what would the economic cost be?



Negative IMPACT OF THE FIRST OIL SHOCK on the economy in 1973

THE ECONOMY IS LESS OIL DEPENDENT THAN IN THE 1970s

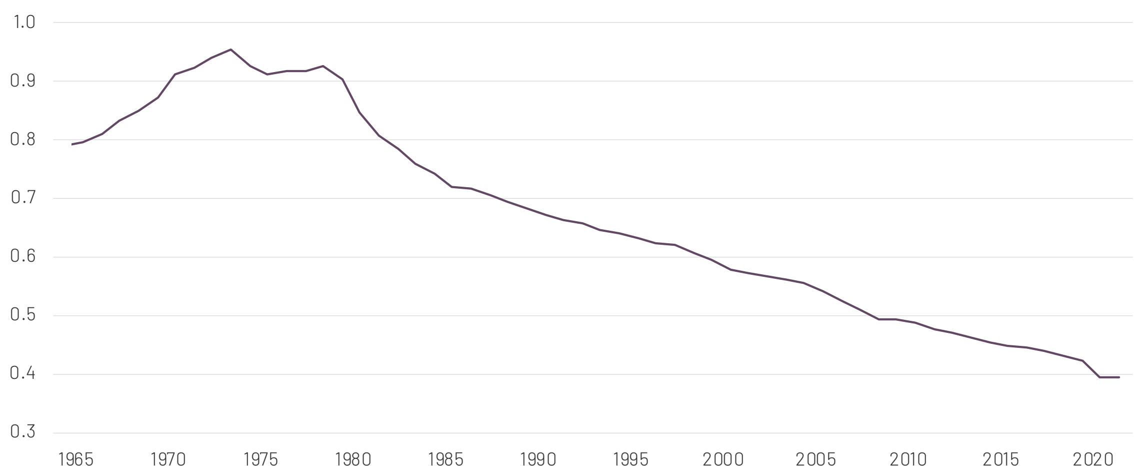
The 1973 oil shocks that started with the Yom Kippur War are now top of mind. After the war began, Arab OPEC member countries decided to raise oil prices and reduce their production. The impact was quickly felt on the economy, with inflation and unemployment both moving higher. The unemployment rate in the United States, for example, nearly doubled in less than two years, increasing from 4.6% in October 1973 to 9% in May 1975. But the impact of an escalation of the situation in the Middle East could be more limited today.

First, if the situation in the Middle East were to deteriorate significantly, oil prices would rise but probably not to the same extent as in the first oil shock.

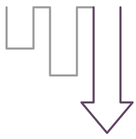
Oil prices actually quadrupled, rising from USD 2.5 in 1973 to more than USD 11 in early 1974 before hitting more than USD 30 in 1980 after the second oil shock in 1979. However, oil prices were artificially low before the first oil shock, as they were largely controlled by the major US and UK energy companies that were operating oil wells in the Middle East. The situation today is fundamentally different, as oil prices are much higher, close to USD 90, nowhere near 1973 prices even accounting for 50 years of inflation.

Second, oil is starting to play a smaller role in the global economy. Oil consumption did of course double between 1972 and 2022, with only occasional annual declines (mainly the 1973 and 1979 oil shocks, the 2008 financial crisis, and the 2020 COVID-19 crisis).

CHART 1: OIL INTENSITY, BARREL OF OIL TO PRODUCE USD 1'000 OF GLOBAL GDP



Source: Center on Global Energy Policy (Columbia), Bloomberg, Indosuez Wealth Management.



Oil RESERVES have NOSEDIVED

But the global economy needs less and less oil: as a Columbia[3] University study shows, oil intensity, i.e. the number of barrels needed to produce USD 1'000 of GDP (inflation adjusted), has been halved since the 1970s.

While it used to take nearly one barrel of oil to generate USD 1'000 of GDP, it now takes less than 0.4 (Chart 1, page 4). This can be attributed to several factors. First, productivity gains have reduced oil dependence. Another factor is the gradual shift from an industrial economy to a service economy, which requires less energy. Economists therefore agree that movements in oil prices have less of an impact on employment and inflation today than they did in the 1970s (see Blanchard and Riggi[4], for example).

THE POTENTIAL MARKET IMPACT SHOULD NOT BE IGNORED

While the effect of a significant increase in oil prices on the global economy could be smaller than in 1973 or 1979, this increase will likely have a considerable impact on the markets. As we described in a recent CIO Perspectives, most of the geopolitical events of the last 50 years had a positive impact on oil and a negative impact on the equity markets, although the effect was sometimes short-lived.

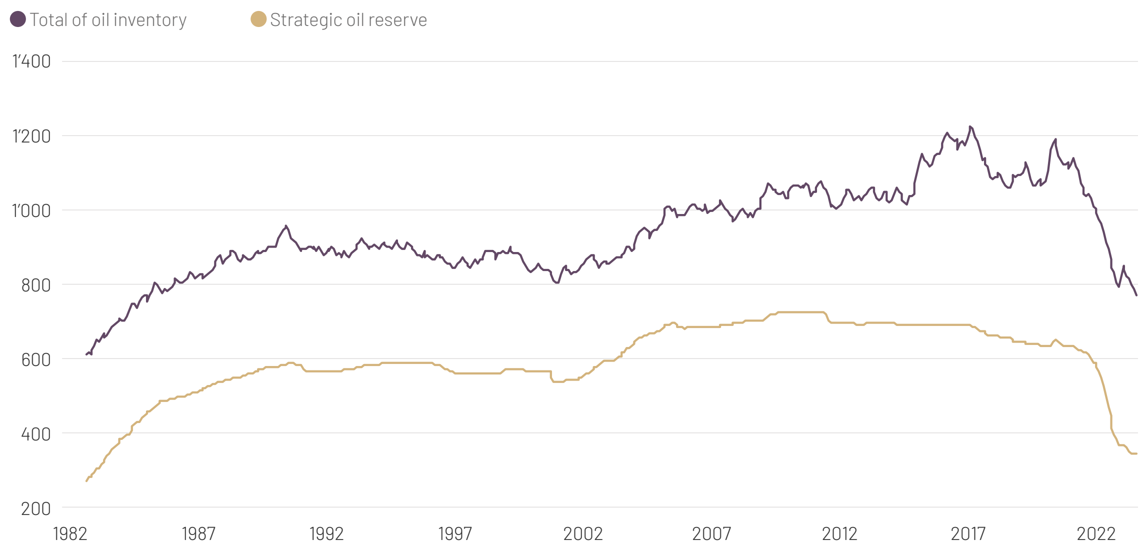
Furthermore, as seen in Chart 2, current oil reserves are at an all-time low, particularly in the United States, which had to tap its strategic reserves after imposing an embargo on Russian oil following Russia's invasion of Ukraine. While the strategic reserves did what they were engineered for and made up for Russian oil, they are now depleted by more than 40%. Their usefulness as a buffer would therefore be limited if the situation in the Middle East were to result in a decline in production in that region.

ENERGY INDEPENDENCE, A KEY FACTOR

The latest series of geopolitical events – invasion of Ukraine, Nagorno-Karabakh conflict, attacks on Israel – has provided an unfortunate ongoing reminder that energy independence is a major challenge for governments, and for European governments in particular. While fossil fuels are now less important for the functioning of the global economy, they nonetheless remain critical for certain sectors, such as transport and chemicals, and access to oil is still a major national defence issue.

Non oil-producing countries are thus expected to continue to support the development of renewable energies, given how necessary they are to reducing dependence on fossil fuels and to ensuring long-term energy independence.

CHART 2: US OIL INVENTORY, MILLIONS OF BARRELS



Source: Bloomberg, Indosuez Wealth Management.

3 - See "*Oil Intensity: The curiously steady decline of oil in GDP*", September 2021, Columbia Center on Global Energy Policy.
4 - See "*Why are the 2000s so different from the 1970s? A structural interpretation of changes in the macroeconomic effects of oil prices*", Blanchard and Riggi, Journal of the European Economic Association, 2013.

A SOFT LANDING

Lucas MERIC
Investment Strategist

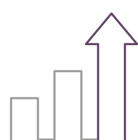
For several months, we have been highlighting the resilience of the US economy despite one of the fastest monetary tightenings since the 1980s. Notwithstanding the numerous headwinds that could slow growth in the coming quarters, we now believe a soft landing of the US economy is highly likely based on recent consumption trends, households' strong financial health, and the robustness of the labour market.

THE RESILIENCE OF THE US CONSUMER

The market began 2023 waiting for one of the most anticipated recessions in history. And yet, nearly 18 months after the start of the Federal Reserve's (Fed) 525 basis points (bps) rate hike cycle, here we are at the end of the third quarter with a nearly 4% increase in consumer spending on an annualised basis. In a country where the consumption component represents more than two-thirds of gross domestic product (GDP), consumers play a decisive role in achieving a soft landing. And, for now, they have not faltered.

DRIVEN BY POST-PANDEMIC DYNAMICS

Consumption has been resilient for several quarters now due to post-pandemic phenomena that enabled consumers to maintain high levels of spending. During the pandemic, households were able to accumulate significant excess savings, reaching as much as 2.1 trillion dollars in 2021. Estimates of this excess vary depending on which pre-COVID savings trend we look at, but one thing is certain: while last month we had estimated excess savings at 1 trillion dollars at the end of the second quarter, the early October revision to savings data for the last 10 years by the Bureau of Economic Analysis (which publishes US GDP, among others) indicates a lower pre-COVID savings trend than before. This means that excess savings would actually be almost 600 billion dollars higher.



BEA revision:
USD 600 BN ADDITIONAL EXCESS SAVINGS

This represents an additional layer of protection for US households, which also have healthy financial balance sheets due to the significant wealth effects they have benefited from since the pandemic, whether through higher equity markets or higher real estate prices. US household net worth assets have increased by more than 30 trillion dollars since end-2019, and these same households now find themselves in a situation where savings are earning high returns, although these phenomena do vary by income level.

At the same time, US consumers have also benefited from significant wage growth (the Atlanta Fed currently estimates annual growth in the average hourly wage at 5.2%), as the labour market was very out of balance coming out of the pandemic: at the end of 2022, the number of job openings was still twice as high as the number of unemployed. Since then, the labour market has continued to rebalance, through a decline in job openings and not through job cuts, with the unemployment rate still at a record low of 3.8%. At the same time, the disinflation process underway in the United States should continue to support households' purchasing power, even though this phenomenon appears to be less significant than in Europe and disinflation is expected to be bumpy due to technical effects.

In our view, these factors as a whole indicate that consumption and growth will no longer contract in the third quarter of 2023 and first quarter of 2024. Our core scenario is therefore for a soft landing of the US economy, even though the latter is still expected to slow in the coming months.

A SLOWDOWN RATHER THAN A CONTRACTION

The resilience of the US consumer is real, but the US economy will have to deal with a number of headwinds at the end of the year. For example, the end of the student loan moratorium is expected to weigh on consumption, although the latter remained strong over the summer despite a significant increase in payments to the US Department of Education for early repayment of student debt. At the same time, rising oil prices and tighter financial conditions due to higher US long-term rates since the summer are also expected to dampen growth *momentum*.

Lastly, the threat of a US government shutdown continues to loom, as the deadline for reaching a budget agreement has been pushed back to mid-November, while the US auto workers union is continuing the strike it began in early September, which is affecting more than 30'000 workers. Year-end growth would be constrained if these risks drag on, even though their impact would be only temporary and their resolution would translate into an immediate reverse positive impact on growth *momentum*.

AN UPWARD REVISION OF GROWTH AND INFLATION OUTLOOKS

The increased likelihood of a soft landing of the US economy and the resilience of consumption during the summer require a significant upward revision to our growth outlooks for the United States, which are now 2.2% (+40 bps) in 2023 and 1.2% (+70 bps) in 2024 (Table 1). We expect average inflation of 2.7% (+10 bps) in 2024 due to recent oil price developments, which should bring total inflation to around 2.4% by the end of next year. This level is still higher than the Fed's target inflation rate.

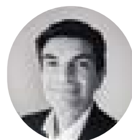
TABLE 1: MACROECONOMIC FORECAST 2023 - 2024, %

● Revised down since last month ● Revised up

	GDP		INFLATION	
	2023	2024	2023	2024
United States	2.2%	1.2%	4.2%	2.7%
Euro Area	0.5%	0.8%	5.6%	2.9%
China	5.1%	4.5%	0.4%	1.8%
Japan	1.9%	1.1%	3.2%	2.0%
India	6.5%	6.0%	6.2%	5.9%
Brazil	2.6%	1.3%	4.8%	4.0%
World	3.0%	2.7%	-	-

Source: Indosuez Wealth Management.

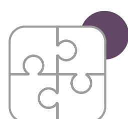
NEVER GIVE UP



Thomas GIQUEL
Head of Fixed Income

With the contribution
of the Fixed Income Team

Factors external to the financial markets have once again found their way into forecasts and valuations. Renewed volatility is affecting all the markets, and bonds are no exception. Higher yields are creating new opportunities for medium- and long-term investors.



FUNDING NEEDS of large European companies estimated to DECLINE BY 25% in 2024

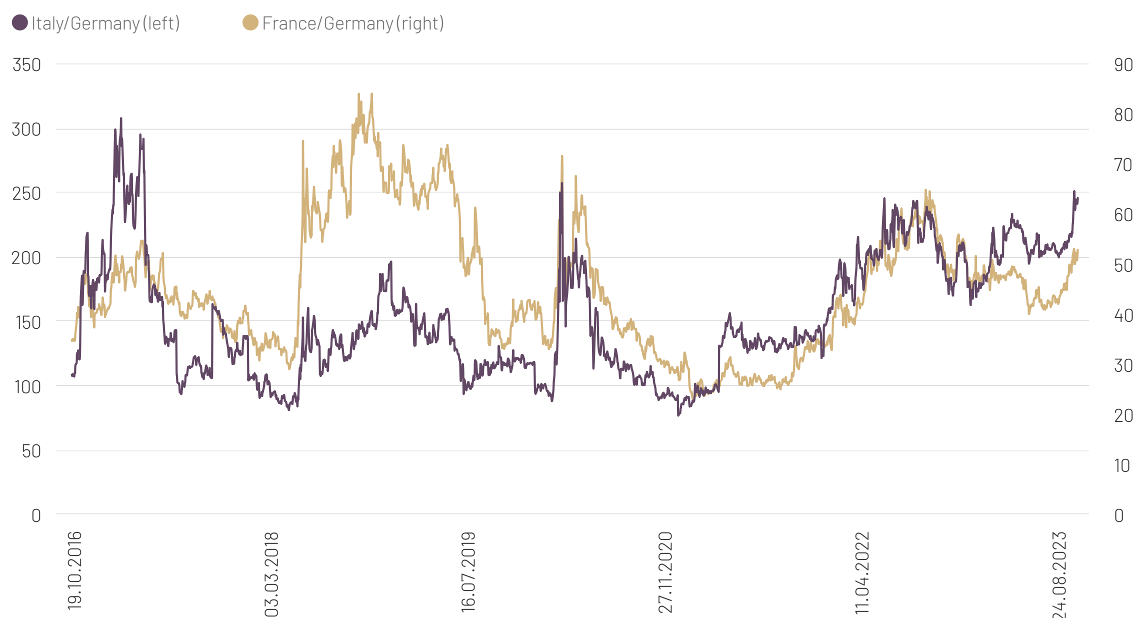
The rise in bond rates has been halted by the tragic events in the Middle East. Bonds temporarily played their role as safe haven, while risky assets fell without giving way to panic. Diplomatic efforts very quickly stopped the rise in oil prices and gave new hope to the equity markets, and fundamentals on the bond markets regained the upper hand. Since the summer, the US Treasury's decision to fund the federal deficit with long-term issues has weighed on long-term rates. The return of the term premium, an expression that has fallen out of use in recent years, has cancelled out the Fed's interventions since the COVID-19 pandemic. Quantitative tightening resumed in early September, and the withdrawal of liquidity is starting to affect all assets. The real estate markets in different geographic regions are clearly adjusting to the new financing conditions and the scarcity of credit, in both volume and price terms.

CENTRAL BANKS

Short-term rates are now anchored in both the United States and the Euro Area. In our view, the markets are still optimistic in their forecasts of key rate cuts in 2024. In contrast, rates continue to adjust to the high-for-long scenario, which explains the curve steepening underway. At nearly 5% on a nominal basis, the US 10-year rate includes a real rate of 2.5%, that is, an excess return above anticipated inflation of 2.5%. This compensation exceeds the Fed's 2% target, as well as "natural rate" estimates.

Short-term rates have also hit their high for this cycle in the Euro Area. Anecdotally, the European Central Bank's (ECB) deposit rate, at 4%, is at its highest level since the creation of the single currency.

CHART 3: INTER-COUNTRY SPREAD (10-YEAR RATE), FRANCE AND ITALY VERSUS GERMANY, BPS



Source: Bloomberg, Indosuez Wealth Management.

The next step is to gradually decrease the central bank's balance sheet, a key step that is still in the works. In this phase, the risk premium of the most heavily indebted European countries could widen significantly relative to the German benchmark. With the market always quick to identify the weakest elements, spreads on French and Italian spreads have already started to widen (Chart 3, page 8).

CREDIT MARKETS

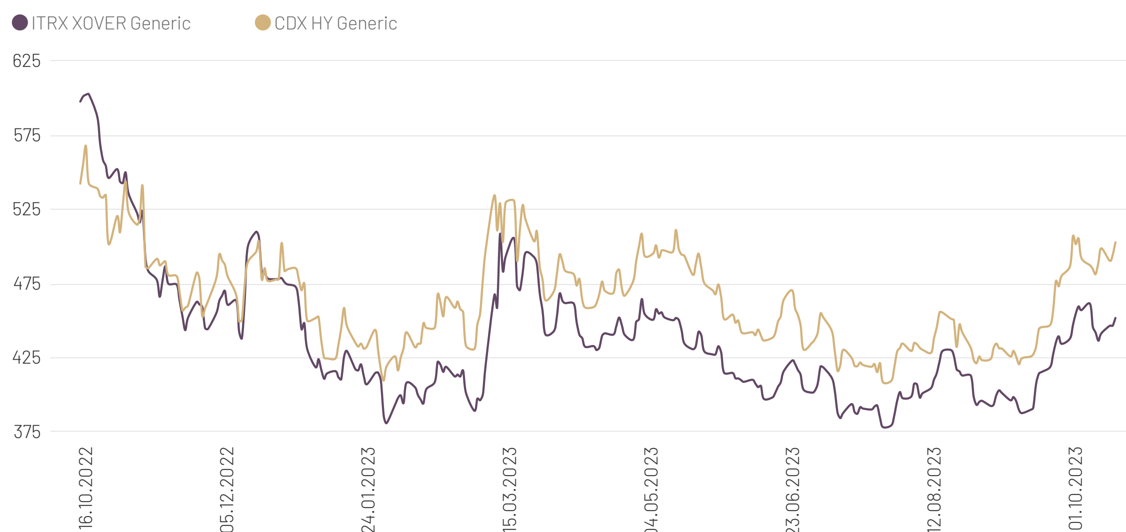
Specific risk remains contained in developed countries. However, systemic risk has materialised since mid-September through a significant widening of the iTraxx credit derivative indices in the United States and the Euro Area (Chart 4).

High yield has underperformed equities since mid-September. Some opportunistic companies have made their investors an offer in which they would recall their debt maturing at end-2023 or 2024 and then reissue it for 2028, for example. This type of liabilities management can be used to maintain access to the market, with many participants anticipating a relatively illiquid year end. The primary market issues were active in September, a sign that issuing companies and investors were evenly matched. However, renewed volatility since 9 October has all but shut down the primary market.

The tightening of the credit conditions granted by banks is affecting the leveraged loans[5] market, where default rates are increasing more quickly in the United States than in Europe. The year-to-date performance in the region tops that of the US market. The lowest-rated debt on the credit market is affected through contagion.

Our analysts conducted a review of the banking sector. The European Banking Authority (EBA) published a consolidated report on the sector and confirmed its good health: the level of capital has reached a high, past due loans are stable, and cost of risk has remained stable at 45 bps. The rise in rates has made it possible to strengthen the sector's profitability, but the outlook is darkening and asset quality is likely to decline. However, reserves are largely sufficient to absorb the headwinds. In the United States, the sector is once again under pressure due to the rise in rates, which is causing potential (but unrealised) losses on asset portfolios invested in government bonds. Rising rates also caused deposits to move into money-market funds, and this shift in capital is now complete. Assets, mainly in real estate, have also deteriorated slightly, but without posing any systemic risk. Lastly, the regulator is imposing new and more stringent capital rules, which benefits bondholders. We continue to focus our investments on the largest banks, which are sound and geographically diversified.

CHART 4: CREDIT DERIVATIVE INDICES, CREDIT DEFAULT SWAP (CDS), HIGH YIELD



Source: Bloomberg, Markit iTraxx, Indosuez Wealth Management.

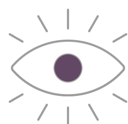
5 - Leveraged loans: type of debt used by companies that are already in debt to fund merger/acquisition transactions, for example. This debt is riskier for investors, with high returns in exchange.

A MUCH ANTICIPATED EARNINGS SEASON

Laura CORRIERAS
Equity Portfolio Manager

With the contribution
of the Equity Team

The equity markets are under pressure due to rising long-term rates (the US 10-year is at its highest levels since 2007!) and investor attention appears to be focused on companies' ability to navigate this new environment. The US economy remains resilient, but the next round of releases will provide confirmation at the micro-economic level of the impact movements in rates are having on companies.



THE ENERGY SECTOR in the lead, LUXURY SUFFERS from profit-taking

EUROPE

Seasonality once again affected the post-summer period and contributed to European equity market weakness. Driven by rising oil prices, the energy sector continued to lead the pack in terms of performance, while luxury goods were again subject to profit-taking. These shifts within sectors translated into a strong outperformance by Value style equities over Growth style equities, which are more sensitive to interest rate moves.

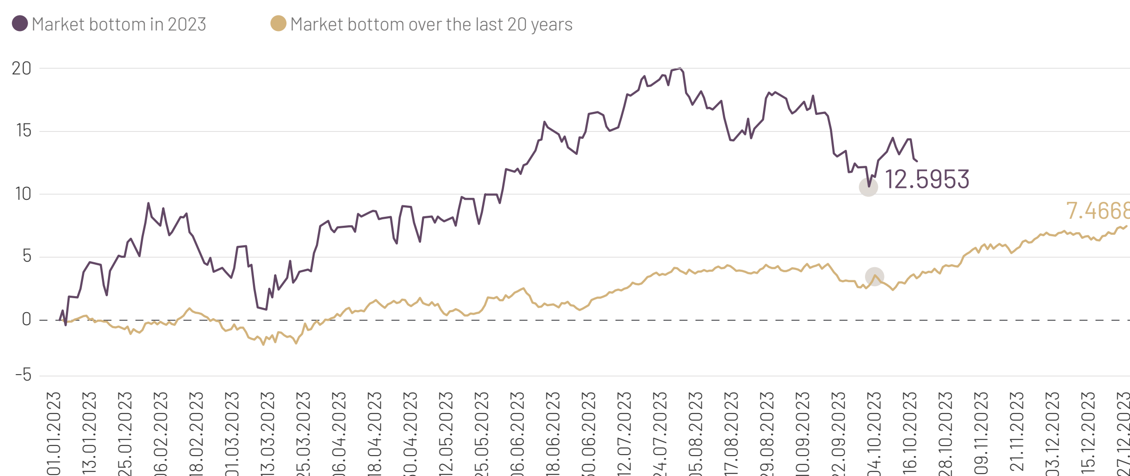
European equity valuations remain very attractive and are currently well below their historical median. Furthermore, earnings revisions proved resilient last month and are trending positively for 2023 and 2024.

Investor attention is now expected to turn to the third-quarter earnings season and to management outlooks for 2024, in particular with respect to demand and the ability to maintain margins.

UNITED STATES

The S&P 500 is down overall since end-July, but this correction looks healthy. The index tested its February highs and its 200-day average, without calling into question the S&P 500's long-term bullish trend. In addition, the summer period is historically weaker in terms of volume and performance and, over the last 20 years, this weakness has on average ended just before the start of the corporate earnings season in mid-October (Chart 5). Earnings revisions for US companies are also trending positively and could spark a year-end rally. Lastly, even though long-term rates have hit particularly high levels, many US companies within the very large cap segment have not necessarily been affected, thanks to their healthy balance sheets and large amounts of cash.

CHART 5: S&P 500 SEASONALITY (AVERAGE PRICE OVER 20 YEARS) AND PERFORMANCE IN 2023



Source: Bloomberg, Indosuez Wealth Management.
Note: Historically, the market has hit bottom on 9 October, which corresponds to the S&P 500 bottom in 2023.

ASIA

Asian stock markets are still struggling to find a direction in the context of high volatility, uncertainty and widespread pessimism, particularly on China. The reopening of the Chinese economy disappointed, despite a robust but short-lived post-COVID recovery. This raised questions about the effectiveness of the measures implemented by the Beijing government. Despite the stimulus efforts, capital inflows are scarce due to the ingrained pessimism about China: the private sector's lack of confidence, weak domestic demand, tension with the United States and ongoing fears in the real estate sector are fuelling concerns among foreign investors.

It could take some time to see the positive impacts of the acceleration in monetary easing and the steps recently taken by the Chinese government to support the real estate sector, while market expectations are focused on the possibility of a strong fiscal stimulus as well as additional stimulus for infrastructure spending. The main events we are keeping an eye on are the third plenum of the 20th Central Committee and the Central Economic Work Conference.

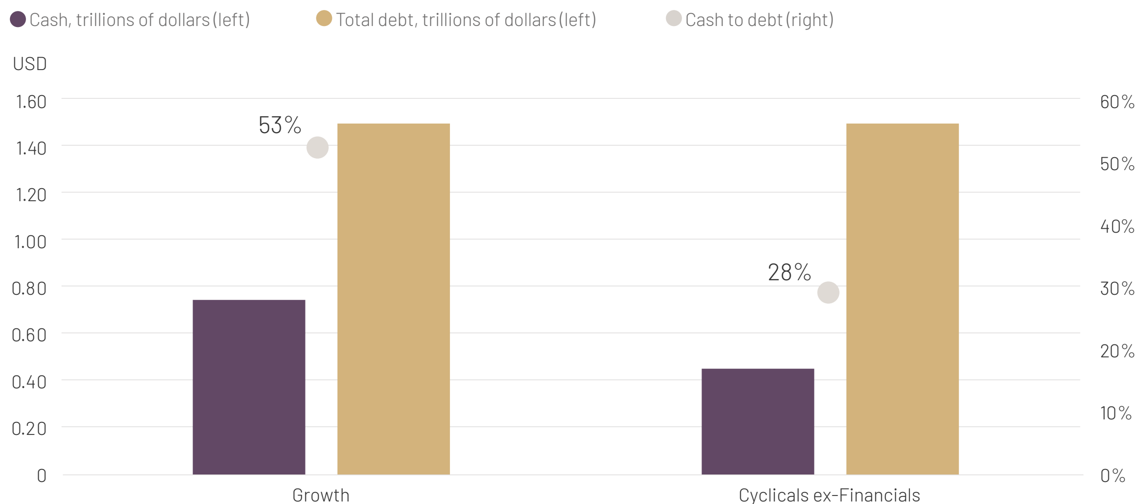
INVESTING STYLES

The rebound in long-term interest rates continued last month, pushing the relative performance of the Value style higher and putting pressure on Growth stocks, particularly in Europe. The less expensive Value sectors (banking, energy, mining, etc.) tended to outperform.

However, Growth/Quality stocks held up quite well in the market downturn, in particular in the United States, thanks to their strong income generation, combined with very low debt/cash levels (Chart 6) which allowed them to benefit from high money-market returns with no need for funding.

Also, while pressures on rates are easing or remaining stable, the next earnings season could highlight top-quality companies with resilient margins, strong cash generation and pricing power.

CHART 6: CASH AND TOTAL DEBT FOR THE S&P 500



Source: Citi Group, Indosuez Wealth Management.
Note: Growth stocks had a cash-to-debt ratio of 53% versus 28% for Cyclicals (ex-Financials).

BETWEEN GEOPOLITICS AND FUNDAMENTALS

Maxime GARCIA
Investment Strategist

Developments on the international stage have somewhat altered the forex landscape. The Swiss franc and gold have regained their lustre thanks to their safe haven status, but sentiment remains neutral on these assets due to persistent headwinds, particularly on the fundamentals side.

EUR

Risks persist

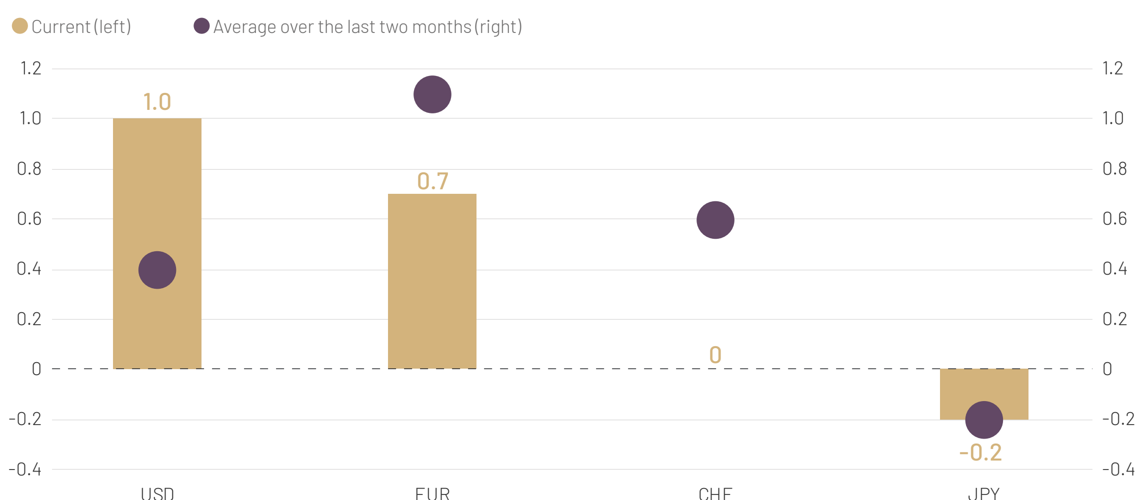
Macroeconomic divergences between the United States and the Euro Area and the increase in the transatlantic spread have hurt the EUR/USD, which fell 1.5% over one month. Furthermore, support from flows that benefited the euro and resulted from the improvement in the trade balance has started to taper off, given the slowdown in global trade and the rebound in energy prices. Foreign investors seem to have lost their taste for assets in euros (Chart 7). That said, expectations are now low and we see the recent stabilisation of the EUR/USD real rate differential as a positive for the single currency. Equally important, in the longer term the first rate cuts are expected to come from the Fed, which could provide fundamental support to the currency pair in the future. Accordingly, we believe the EUR/USD outlook remains balanced if we assume that geopolitical tensions will not escalate (expecting trading range: 1.045 to 1.085). Close attention needs to be paid, however, to the BTP-Bund spread, which could weigh on the euro, and we should be aware that the low end of the range could be reached in the event of a supply shock on energy.

USD

Limited appreciation potential

The dollar hit another one-year high at the beginning of the month, driven by macroeconomic dynamics that continue to surprise to the upside and could persist, and could thus be accompanied by renewed interest in the greenback. The events in the Middle East also supported demand for safe assets (and thus for the dollar) in the second half of the month (Chart 8, page 13). A widespread conflict could further strengthen the US currency. So, as we noted last month, we are less negative on the dollar but still think it has limited appreciation potential.

CHART 7: CURRENCY POSITIONING INDEX



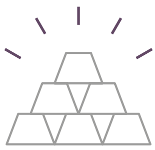
Source: CACIB, Indosuez Wealth Management.

The dollar did lose several points of performance after a few members of the Fed made some seemingly accommodative comments, stressing that the recent tightening of financial conditions in the United States could reduce the need for further key rate hikes. In addition, the USD is now the G10 currency with the largest long positioning, which limits the likelihood of inflows.

CHF

Between safe haven and fundamentals

The Swiss franc has remained the best-performing G10 currency since the beginning of the year. The Swiss currency initially took a hit in early October after the last meeting of the Swiss National Bank's (SNB) committee, at which it decided not to raise its key rates. But later on, the CHF was supported by its safe haven status and rose 1.6% against the euro over the month. We maintain our neutral position and expect a trading range of 0.90-0.94 for the USD/CHF and 0.95-0.98 for the EUR/CHF. On the one hand, the Swiss currency could continue to rise if geopolitical tensions intensify, and could also benefit from the SNB's readiness to intervene on the forex market if necessary. On the other hand, headwinds persist, including the CHF's carry disadvantage.



GOLD
HAS CLIMBED
above
USD 1'900
due to the escalation
of the conflict
in the Middle East

JPY

No change, no appreciation

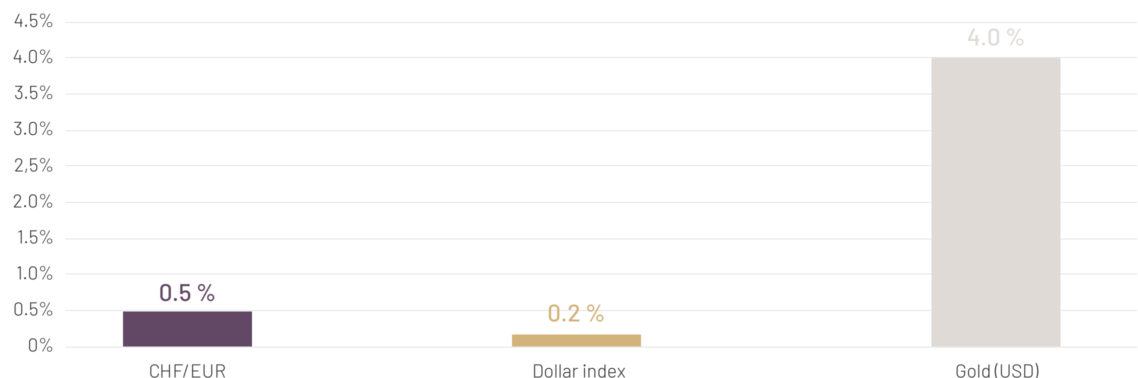
The USD/JPY was trading close to the 150 threshold in early October before falling sharply in just a few minutes, suggesting that the Japanese monetary authorities had intervened. If true, their intervention was not very effective as the USD/JPY is once again trading near 150, an uncomfortable level for Japanese policymarkets. The yen continues to be penalised by its rate differential relative to other major economies, but weak wage growth and the global economic slowdown could keep the Bank of Japan from changing its monetary policy in 2023. As we said last month, only a Fed pause or a policy normalisation by the Bank of Japan would allow for long-term JPY appreciation, which could push the USD/JPY pair between 138 and 140.

GOLD

Real yields or geopolitics?

The (negative) correlation that was re-established between real interest rates and gold remained a drag, pushing the ounce to an annual low of around USD 1'800. The fall was short-lived, however, as the geopolitical situation helped gold climb back to the USD 1'900 level. Short-term sentiment remains neutral as the Fed's restrictive stance is holding back a surge in gold prices. In the longer term, geopolitical uncertainty, currency reserve diversification, and the prospect of a less restrictive US monetary policy in 2024 are supports for gold. We expect it to trade in the USD 1'850 to USD 1'950 range.

CHART 8: PERFORMANCE OF SAFE HAVENS SINCE THE START OF THE TENSIONS, FROM 09.10 TO 18.10.2023, %

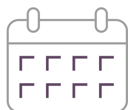


Source: Datastream, Indosuez Wealth Management.

INVESTMENT SCENARIO AND ALLOCATION CONVICTIONS

Grégory STEINER
Global Head of Multi Asset

Adrien ROURE
Portfolio Manager



PREFERENCE
for a positioning on
MATURITIES
OF UP
TO FIVE YEARS

INVESTMENT SCENARIO

- **Growth:** we have revised upward our growth scenario in the United States, with economic activity now expected to expand slightly for the next two quarters due to the stronger resilience of the US consumer. Economic activity in Europe will remain modest next year but with major differences between countries in the region. More generally, emerging countries will be the main engine of global growth in 2024.
- **Inflation:** we maintain our scenario of a non-linear disinflation process in developed economies. The balance of risks is to the upside due to the robustness of the US economy and the possible impacts on energy prices of the emerging geopolitical tensions in the Middle East.
- **Central banks:** the rise in long-term rates in the markets is partially replacing the work of central banks in tightening financial conditions. In conjunction with the slowdown in inflation, we believe the Fed and the ECB have come to the end of their rate hike cycles. We now expect a plateau of high interest rates until the beginning of the second half of 2024.
- **Corporate earnings:** we are generally comfortable with the market's earnings expectations for 2024 but continue to closely monitor the divergence in earnings revisions: upward for the United States and Japan, downward for Europe and China.
- **Risk environment:** geopolitical risk has taken centre stage again and prompted us to include more hedges in our portfolios. At the same time, after the latest rise in long-term rates we can no longer rule out the emergence of idiosyncratic risks in the financial world.

ASSET ALLOCATION CONVICTIONS

Equities

- We maintain a constructive position on risky assets in the short term given the more favourable economic environment (particularly in the United States) and companies' continued strong financial health.
- We continue to favour US equities for the reasons outlined above, while positive earnings revisions in the region offer further support. We maintain a neutral stance on European equities, as there are no clear signs of an improvement in economic activity at this stage and the earnings revision trend is not as positive as in the United States.
- In sector terms, our preference for Growth stocks remains intact, as they continue to benefit from investor interest in the artificial intelligence theme. We maintain our conviction on the listed real estate sector for the coming quarters. This segment has already factored in a large part of the rate hikes and the expected decline in physical real estate prices.
- Despite the Chinese government's recent announcements of economic support measures and the impacts they are already having on economic activity, at this stage we have not yet seen any concrete reaction on the equity markets. While we do expect a rebound by the end of the year, we nonetheless take a less favourable strategic stance on Chinese equities. However, we maintain our constructive stance on emerging market assets, which will benefit from a positive growth differential versus advanced economies and could be viewed as a diversification region if geopolitical tensions intensify.

Fixed Income

- While high levels of long-term rates offer attractive entry points, we prefer to remain positioned on the shortest ends of the rate curves, with maturities of up to five years. In addition to offering higher carry, these maturities seem to be less correlated to movements in risky assets than longer-term bonds.
- Meanwhile, the volatility that is specific to government bonds with long maturities makes them less attractive. The large issues expected on these tenors in the United States (and the ongoing shrinkage of central banks' balance sheets), combined with the risks of a higher growth/inflation mix, could continue to weigh on this segment.
- Regarding credit, we continue to prefer high-quality corporate debt with short maturities and remain on the sidelines on the high yield segment.
- We have tactically raised our opinion on inflation breakevens, mainly for technical reasons, while the potential widening of geopolitical tensions in the Middle East and the impact on energy prices could benefit this asset class.

Forex

- The macroeconomic environment, which continues to surprise to the upside in the United States, and the continued widening of the transatlantic spread will buoy the dollar in the short term. The latter is benefiting from its safe haven status in the face of mounting geopolitical risk. While these are strong supports for the dollar in the short term, the more accommodative stance taken by some members of the FOMC and investor positioning lead us to believe that its appreciation potential remains limited.
- The Swiss franc is temporarily benefiting from its status as a hedging asset but is expected to remain capped by its unattractive carry relative to other developed country currencies.
- The yen continues to trade at all-time lows and is approaching the Bank of Japan's previous intervention levels. An intervention by the Bank of Japan would support the currency and lead to greater volatility in the short term. However, a more structural change in the monetary environment is needed for long-term appreciation of the yen against the dollar.
- Gold has regained its lustre given the renewed geopolitical risk in recent weeks. Leaving that aside, the price of gold nonetheless seems to be trapped between the support provided by central bank demand on the one hand, and by the rise in real rates on the other.

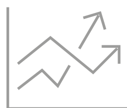
KEY CONVICTIONS

	TACTICAL VIEW (ST)	STRATEGIC VIEW (LT)
FIXED INCOME		
GOVERNMENTS		
EUR 2-Year	=/+	=
EUR 10-Year	=/-	=/-
EUR Periphery	=/-	=/-
US 2-Year	+	+
US 10-Year	=/-	=
EUR Breakevens Inflation	=/+	=/+
US Breakevens Inflation	=/+	=
CREDIT		
Investment grade EUR	=/+	+
High yield EUR	=/-	=
Financials Bonds EUR	=	=
Investment grade USD	=/+	+
High yield USD	-	=
EMERGING DEBT		
Hard Currencies	=	=/+
Local Currencies	=/+	=/+
EQUITIES		
GEOGRAPHIES		
Europe	=	=
United States	=/+	=/+
Japan	=	=
Latin America	=	=
Asia ex-China	=/+	=/+
China	=	=
STYLES		
Growth	=/+	=/+
Value	=	=
Quality	=/+	=
Cyclical	=	=
Defensive	=/-	=/-
FOREX		
United States (USD)	=	=/-
Euro Area (EUR)	=/-	=/+
United Kingdom (GBP)	=/-	=
Switzerland (CHF)	=	=/+
Japan (JPY)	=/+	=/+
China (CNY)	=	=
Gold (XAU)	=/-	=/+

Source: Indosuez Wealth Management.

OVERVIEW OF SELECTED MARKETS

DATA AS OF 20 OCTOBER 2023



GOVERNMENT BONDS	YIELD	4 WEEKS CHANGE (BPS)	YTD CHANGE (BPS)
US Treasury 10-year	4.91%	48.00	103.89
France 10-year	3.51%	22.70	40.60
Germany 10-year	2.89%	15.10	32.30
Spain 10-year	4.00%	18.60	34.90
Switzerland 10-year	1.19%	12.00	-42.80
Japan 10-year	0.84%	9.90	42.20

BONDS	LAST	4 WEEKS CHANGE	YTD CHANGE
Government Bonds Emerging Markets	34.21	-3.38%	-1.44%
Euro Government Bonds	194.52	-0.23%	0.96%
Corporate EUR high yield	203.49	-1.42%	5.15%
Corporate USD high yield	306.04	-2.38%	3.14%
US Government Bonds	294.72	-0.63%	-0.23%
Corporate Emerging Markets	41.44	-2.56%	-3.09%

CURRENCIES	LAST SPOT	4 WEEKS CHANGE	YTD CHANGE
EUR/CHF	0.9450	-2.18%	-4.50%
GBP/USD	1.2164	-0.63%	0.67%
USD/CHF	0.8921	-1.60%	-3.50%
EUR/USD	1.0594	-0.55%	-1.04%
USD/JPY	149.86	1.00%	14.29%

VOLATILITY INDEX	LAST	4 WEEKS CHANGE (POINTS)	YTD CHANGE (POINTS)
VIX	21.71	4.51	0.04

EQUITY INDICES	LAST PRICE	4 WEEKS CHANGE	YTD CHANGE
S&P 500 (United States)	4'224.16	-2.22%	10.02%
FTSE 100 (United Kingdom)	7'402.14	-3.67%	-0.67%
STOXX 600	433.73	-4.31%	2.08%
Topix	2'255.65	-5.08%	19.24%
MSCI World	2'791.24	-3.08%	7.24%
Shanghai SE Composite	3'510.59	-6.11%	-9.33%
MSCI Emerging Markets	925.58	-4.01%	-3.22%
MSCI Latam (Latin America)	2'177.06	-6.93%	2.29%
MSCI EMEA (Europe. Middle East. Africa)	179.94	-3.66%	-6.27%
MSCI Asia Ex Japan	589.23	-3.66%	-4.84%
CAC 40 (France)	6'816.22	-5.13%	5.29%
DAX (Germany)	14'798.47	-4.88%	6.28%
MIB (Italy)	27'357.00	-4.27%	15.40%
IBEX (Spain)	9'029.10	-4.98%	9.72%
SMI (Switzerland)	10'348.60	-6.05%	-3.55%

COMMODITIES	LAST PRICE	4 WEEKS CHANGE	YTD CHANGE
Steel Rebar (CNY/Tonne)	3'590.00	-3.10%	-12.33%
Gold (USD/Oz)	1'981.40	2.92%	8.63%
Crude Oil WTI (USD/Bbl)	88.75	-1.42%	10.58%
Silver (USD/Oz)	23.50	-0.39%	-2.23%
Copper (USD/Tonne)	7'948.50	-3.33%	-5.06%
Natural Gas (USD/MMBtu)	2.90	9.94%	-35.22%

Source: Bloomberg, Indosuez Wealth Management.
Past performance does not guarantee future performance.

MONTHLY INVESTMENT RETURNS, PRICE INDEX

FTSE 100 · Topix · MSCI World · MSCI EMEA · MSCI Emerging Markets
STOXX 600 · S&P 500 · Shanghai SE Composite · MSCI Latam · MSCI Asia Ex Japan

BEST PERFORMING (+)

JULY 2023	AUGUST 2023	SEPTEMBER 2023	4 WEEKS CHANGE	YTD (20.10.2023)
0.41%	6.75%	2.27%	-2.22%	19.24%
-1.77%	5.80%	-0.37%	-3.08%	10.02%
-2.55%	5.68%	-1.74%	-3.66%	7.24%
-2.79%	5.01%	-2.01%	-3.66%	2.29%
-3.38%	4.48%	-2.47%	-3.67%	2.08%
-5.73%	3.29%	-2.81%	-4.01%	-0.67%
-6.21%	3.11%	-2.86%	-4.31%	-3.22%
-6.36%	2.23%	-3.35%	-5.08%	-4.84%
-6.61%	2.04%	-4.45%	-6.11%	-6.27%
-7.90%	1.48%	-4.87%	-6.93%	-9.33%

(−) WORST PERFORMING

Source: Bloomberg, Indosuez Wealth Management.
Past performance does not guarantee future performance.

Basis point (bps): 1 basis point = 0.01%.

Blockchain: A technology for storing and transmitting information. It takes the form of a database which has the particularity of being shared simultaneously with all its users and generally does not depend on any central body.

BLS: Bureau of Labor Statistics.

BNEF: Bloomberg New Energy Finance.

Brent: A type of sweet crude oil, often used as a benchmark for the price of crude oil in Europe.

CPI (Consumer Price Index): The CPI estimates the general price level faced by a typical household based on an average consumption basket of goods and services. The CPI tends to be the most commonly used measure of price inflation.

Cyclicals: Cyclicals refers to companies that are dependent on the changes in the overall economy. These stocks represent the companies whose profit is higher when the economy is prospering.

Defensives: Defensives refers to companies that are more or less immune to the changes in the economic conditions.

Deflation: Deflation is the opposite of inflation. Contrary to inflation, it is characterised by a sustained decrease in general price levels over an extended period.

Duration: Reflects the sensitivity of a bond or bond fund to changes in interest rates. This value is expressed in years. The longer the duration of a bond, the more sensitive its price is to interest rate changes.

EBIT (Earnings Before Interest and Taxes): Refers to earnings generated before any financial interest and taxes are taken into account. It takes earnings and subtracts operating expenses and thus also corresponds to non-operating expenses.

EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortisation): EBITDA takes net income and adds interest, taxes, depreciation and amortisation expenses back to it. It is used to measure a company's operating profitability before non-operating expenses and non-cash charges.

ECB: The European Central Bank, which governs the euro and Euro Area member countries' monetary policy.

Economic Surprises Index: Measures the degree of variation in macro-economic data published versus forecasters' expectations.

Economies of scale: Decrease in a product's unit cost that a company obtains by increasing the quantity of its production.

EPS: Earnings per share.

ESG: Non-financial corporate rating system based on environmental, social and governance criteria. It is used to evaluate the sustainability and ethical impact of an investment in a company.

Fed: The US Federal Reserve, i.e. the central bank of the United States.

FOMC (Federal Open Market Committee): The US Federal Reserve's monetary policy body.

GDP (Gross Domestic Product): GDP measures a country's yearly production of goods and services by operators residing within the national territory.

Growth: Growth style refers to companies expected to grow sales and earnings at a faster rate than the market average. As such, growth stocks are generally characterised by a higher valuation than the market as a whole.

IEA: International Energy Agency.

IMF: The International Monetary Fund.

Inflation breakeven: Level of inflation where nominal bonds have the same return as inflation-linked bonds (of the same maturity and grade). In other words, it is the level of inflation at which it makes no difference if an investor owns a nominal bond or an inflation-linked bond. It therefore represents inflation expectations in a geographic region for a specific maturity.

Inflation swap rate 5-Year, 5-Year: A market measure of what 5-Year inflation expectations will be in five years' time. It provides a window into how inflation expectations may change in the future.

IPPC: The Intergovernmental Panel on Climate Change.

IRENA: International Renewable Energy Agency.

ISM: Institute for Supply Management.

Japanification of the economy: Refers to the stagnation the Japanese economy has faced in the last three decades, and is generally used to refer to economists' fears that other developed countries will follow suit.

Metaverse: A metaverse (portmanteau of meta and universe) is a fictional virtual world. The term is regularly used to describe a future version of the internet where virtual, persistent and shared spaces are accessible via 3D interaction.

OECD: Organisation for Economic Co-operation and Development.

Oligopoly: An oligopoly occurs when there is a small number of producers (supply) with a certain amount of market power and a large number of customers (demand) on a market.

OPEC: Organization of the Petroleum Exporting Countries; 14 members.

OPEC+: OPEC plus 10 additional countries, notably Russia, Mexico, and Kazakhstan.

PMI: Purchasing Managers' Index.

Policy mix: The economic strategy adopted by a state depending on the economic environment and its objectives, mainly consisting of a combination of monetary and fiscal policy.

Pricing power: Refers to the ability of a company or brand to increase its prices without affecting demand for its products.

Quality: Quality stocks refers to companies with higher and more reliable profits, low debt and other measures of stable earnings and strong governance. Common characteristics of Quality stocks are high return to equity, debt to equity and earnings variability.

Quantitative easing (QE): A monetary policy tool by which the central bank acquires assets such as bonds, in order to inject liquidity into the economy.

SEC (Securities and Exchange Commission): The SEC is an independent federal agency with responsibility for the orderly functioning of US securities markets.

Spread (or credit spread): A spread is the difference between two assets, typically between interest rates, such as those of corporate bonds over a government bond.

Secular stagnation: Refers to an extended period of little or no economic growth.

SRI: Sustainable and Responsible Investments.

Stagflation: Stagflation refers to an economy that is experiencing simultaneously an increase in inflation and stagnation of economic output.

TPI : An addition to the Eurosystem's toolkit that can be activated by the ECB to counter unwarranted, disorderly market developments if these pose a serious threat to the smooth transmission of monetary policy across the euro area. The ECB Governing Council approved the instrument on the 21 July 2022.

Uberisation: Term derived from the name of US company Uber which develops and operates digital platforms that connect drivers and riders. It refers to a new business model that leverages new digital technologies and is part of the sharing economy, insofar as it puts customers in direct contact with service providers, at a reduced cost and with lower prices.

Value: Value style refers to companies that appear to trade at a lower price relative to its fundamentals. Common characteristics of value stocks include high dividend yield, low price-to-book ratio, and a low price-to-earnings ratio.

VIX: The index of implied volatility in the S&P 500 Index. It measures market operators' expectations of 30-day volatility, based on index options.

WTI (West Texas Intermediate): Along with Brent crude, the WTI is a benchmark for crude oil prices. WTI crude is produced in America and is a blend of several sweet crude oils.

WTO: World Trade Organization.

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