Market Insights

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Syz PRIVATE BANKING

Key takeaways

- Developed equity markets recorded strong gains in the third quarter, as the S&P 500 advanced by more than 5%. This marks the strongest year-to-date gain through three quarters (+20.8%) for the blue-chip index since 1997. Notably, the third quarter also witnessed changes in leadership within global equities. Thanks to a strong end of the quarter by Chinese stocks, Asia ex-Japan and emerging market equities outperformed developed markets. Global value stocks and small-caps outperformed growth stocks as the "Magnificent 7" lost some of their shine. On a year-to-date basis, Bitcoin and gold remain by far the best-performing assets, while bonds and global commodities continue to lag.
- In the first section of this publication, we review the top 10 stories from the past quarter. We then present the key takeaways from our latest Tactical Asset Allocation Committee meeting. While the macroeconomic environment remains broadly supportive of equity markets, regional variations are emerging. The U.S. economy continues to demonstrate remarkable resilience, while Europe faces slowing growth. The risk of stagnation or a mild recession is increasing in Europe but remains low in the U.S. Meanwhile, inflation is decelerating globally as central banks have now begun their tapering cycle. The market is pricing in strong upside for 2025 earnings. Equity valuations remain expensive, with both the S&P 500 and its equal-weighted counterpart at recent highs. Some risks, such as those related to the Middle East, U.S. election uncertainty, and the unwinding of the yen carry trade, seem underpriced.
- A few weeks ahead of the U.S. Presidential elections, the race remains highly uncertain, with both candidates neck and neck in the polls. The debates, along with recent events such as Joe Biden's health issues and assassination attempts on Donald Trump, have added to the unpredictability of this election, which could significantly impact the U.S. economy and financial markets. Let's explore the key issues at stake and how the election outcome may affect equity and bond investments.
- We then turn to our home country to discuss the "Swiss miracle." Despite challenges posed by a strong currency, Switzerland's economy remains robust, with significant industrial growth driven by specialised sectors. This resilience contrasts with stagnation seen in many neighbouring countries.
- The last section focuses on the rise of stablecoins. In recent years, this specific segment of cryptocurrencies has significantly transformed the landscape of digital finance, with over $170 billion of these digital assets now held globally.

We wish you a great end of the year!

Q3 markets review: 10 charts to remember

Chart #1 The Fed joins the rate cut club

Read more on page 1 - Image iStock

Fed cuts rates as Europe faces recession, China boosts stimulus, and U.S. debt soars

The Fed cuts rates, meanwhile Europe teeters on the brink of recession, China ramps up stimulus, and U.S. debt surges. Developed market equities surge amid global challenges, while fixed income rallies on easing rate expectations.

Each quarter, the Syz investment team takes you through the last 3 months in 10 charts.

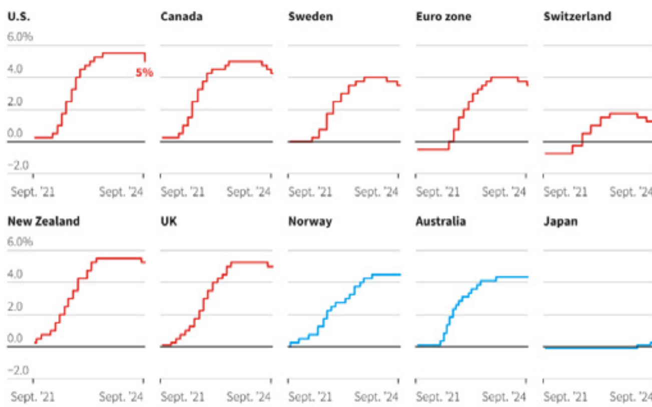
Charles-Henry Monchau
Chief Investment Officer

Chart #1

The Fed joins the rate cut club

The Federal Reserve has finally cut its interest rates for the first time since March 2020, beginning the long-awaited "Fed pivot". With an oversized 50-basis-point rate cut, the Fed appears to be prioritising the labour market, given the rise in unemployment in the U.S. to 4.2%, rather than maintaining its previous focus on controlling inflation. This decision reflects growing concerns about the economic slowdown and suggests the Fed is now aiming to support the broader economy by moving interest rates back to neutral levels.

This global trend toward easing monetary policy is not limited to the U.S., as central banks across Europe are also shifting their stance. The Bank of England initiated its own easing cycle with a 25-basis-point cut in August. The European Central Bank followed suit in September with its second rate cut, lowering rates to 3.5%, while the Swiss National Bank reduced its key rate for the third consecutive time, bringing it down by 0.25% to 1%.



Source: Reuters

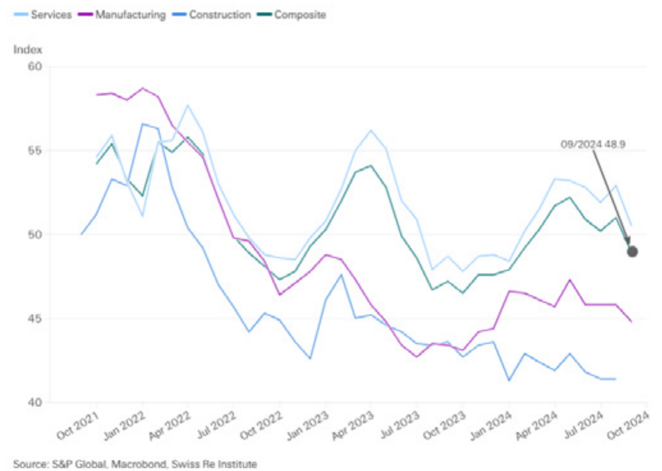
Chart #2

Europe on the brick of recession

Economic growth in the Eurozone began slowing in early summer 2024 and recent data confirms this downward trajectory. While Q2 brought a modest 0.2% q/q GDP growth, largely driven by net exports, the September flash composite PMI fell into contraction territory at 48.9, highlighting the decline in manufacturing activity and its spillover into the services sector.

Germany, once the economic powerhouse of the Eurozone, has become its weakest link. Its industrial sector struggles with declining demand from China, increased competition from cheaper Chinese exports, and energy supply challenges worsened by sanctions on Russia. Economists are now expecting that Germany's economy will stagnate at best for the remainder of 2024.

Meanwhile, in France, the brief economic boost from the "Olympic effect" in August has faded away, leaving the country, along with Germany, facing economic contraction. Italy and Spain have shown resilience, with strong service sector activity helping to offset the broader European slowdown. Still, the overall growth in the Eurozone remains weak and underperforms expectations.

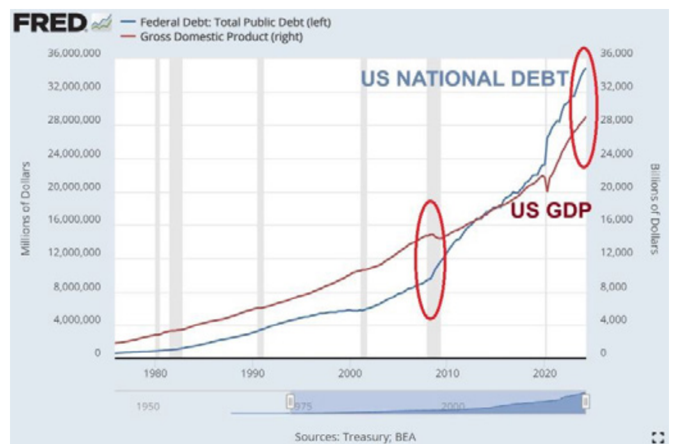


Source: Swiss Re Institute

Chart #3

US Debt explodes

Total U.S. debt explodes again, reaching $35.7 trillion on October 1, up $345 billion from September 27. This figure becomes more alarming when looked at in its relationship to US GDP. In 2008, the U.S. federal debt was $9.4 trillion while the U.S. GDP was $14.7 trillion, resulting in a debt-to-GDP ratio of 64%. Now, with public debt sitting at $35.7 trillion and GDP at $29 trillion, the debt-to-GDP ratio has skyrocketed to 122%, making the U.S. the country with the 6th highest ratio in the world.



Source: Global Markets Investor, FRED

Chart #4

Chinese authorities "go big"

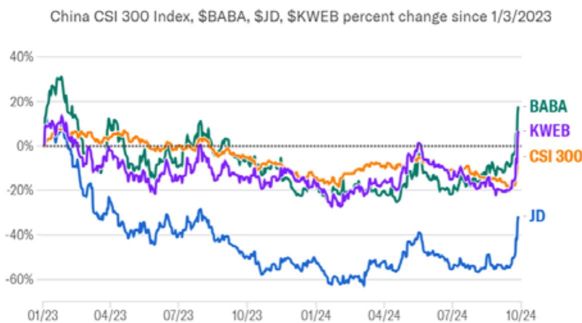
The story of the end of the quarter was the deployment of China's massive stimulus package. After years of stagnation and a slow recovery post-pandemic, Chinese authorities finally decided to "go big" to stabilise the struggling property market and support the country's economy.

A key component of the plan is the People's Bank of China (PBOC) cutting mortgage rates for individual borrowers and lowering the reserve requirement ratio (RRR) for banks by 0.50 percentage points. Additionally, the minimum down payment for second-home purchases has been reduced from 25% to 15%. Further cuts to the RRR, potentially between 0.25 to 0.5 percentage points, are being considered for later this year, though these adjustments will not apply to smaller banks. Lastly, the government has proposed a $113 billion market stabilisation fund, representing less than 1% of China's total stock market capitalisation, to bolster the financial sector.

These measures triggered an immediate 4.3% surge in the CSI 300 index after the stimulus package announce and Asia ex-Japan was the top performing major region, returning 10.6% over the quarter.

CHINA'S STIMULUS MEASURES ARE CONVINCING INVESTORS THAT THIS TIME IS DIFFERENT

China CSI 300 Index, $BABA, $JD, $KWEB percent change since 1/3/2023



SOURCE: YAHOO FINANCE • AS OF SEPTEMBER 27, 2024

Source: Yahoo!finance

Chart #5

Developed market equities surge despite global challenges

During the third quarter of the year, developed market equities delivered a strong 6.5% return. Geopolitical tensions in the Middle East and Europe, along with a revision in U.S. employment data and concerns about the "Yen Carry Trade" posed challenges during the quarter. Nonetheless, the S&P 500 maintained its upward momentum, adding 5.9% over the quarter. Small-cap stocks led the way with a notable 9.5% increase, while global REITs delivered a remarkable 16.2% gain.

European markets, however, showed more muted growth. The UK posted a modest 2.3% increase, while the broader European market, excluding the UK, edged up by 1.6%. The Eurozone's economic recovery continues to struggle, with Germany's manufacturing sector facing headwinds from weak Chinese demand and increased competition from lower-cost Chinese exports.

In Asia, Japanese stocks dropped 4.9%, hit by the Bank of Japan's July rate hike and Governor Ueda's signals of more hikes to come. A weak U.S. labour market report and narrowing U.S.-Japan interest rate differentials led to a sharp yen appreciation and the unwinding of carry trades.

Exhibit 4: World stock market returns

2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	Q3 '24
Japan TOPIX 54.4%	US S&P 500 13.7%	Japan TOPIX 12.1%	UK FTSE All-Share 16.8%	MSCI Asia ex-Japan 42.1%	US S&P 500 -4.4%	US S&P 500 31.5%	MSCI Asia ex-Japan 25.4%	US S&P 500 28.7%	UK FTSE All-Share 0.3%	Japan TOPIX 28.3%	US S&P 500 22.1%	MSCI Asia ex-Japan 10.6%
US S&P 500 32.4%	Japan TOPIX 10.3%	MSCI Europe ex-UK 9.1%	US S&P 500 12.0%	MSCI EM 37.8%	UK FTSE All-Share -9.5%	MSCI Europe ex-UK 27.5%	MSCI EM 18.7%	MSCI Europe ex-UK 24.4%	Japan TOPIX -2.5%	US S&P 500 26.3%	MSCI Asia ex-Japan 21.5%	MSCI EM 8.9%
MSCI Europe ex-UK 24.2%	MSCI Europe ex-UK 7.4%	US S&P 500 1.4%	MSCI EM 11.6%	Japan TOPIX 22.2%	MSCI Europe ex-UK -10.6%	UK FTSE All-Share 19.2%	US S&P 500 18.4%	UK FTSE All-Share 18.3%	MSCI Europe ex-UK -12.2%	MSCI Europe ex-UK 17.3%	MSCI EM 17.2%	US S&P 500 5.9%
UK FTSE All-Share 20.8%	MSCI Asia ex-Japan 5.1%	UK FTSE All-Share 1.0%	MSCI Asia ex-Japan 5.8%	US S&P 500 21.8%	MSCI Asia ex-Japan -14.1%	MSCI EM 18.9%	Japan TOPIX 7.4%	Japan TOPIX 12.7%	US S&P 500 -18.1%	MSCI EM 10.3%	Japan TOPIX 14.2%	UK FTSE All-Share 2.3%
MSCI Asia ex-Japan 3.3%	UK FTSE All-Share 1.2%	MSCI Asia ex-Japan -8.9%	MSCI Europe ex-UK 3.2%	MSCI Europe ex-UK 14.5%	MSCI EM -14.2%	MSCI Asia ex-Japan 18.5%	MSCI Europe ex-UK 2.1%	MSCI EM -2.2%	MSCI Asia ex-Japan -19.4%	UK FTSE All-Share 7.9%	MSCI Europe ex-UK 12.1%	MSCI Europe ex-UK 1.6%
MSCI EM -2.3%	MSCI EM -1.8%	MSCI EM -14.6%	Japan TOPIX 0.3%	UK FTSE All-Share 13.1%	Japan TOPIX -16.0%	Japan TOPIX 18.1%	UK FTSE All-Share -9.8%	MSCI Asia ex-Japan -4.5%	MSCI EM -19.7%	MSCI Asia ex-Japan 6.3%	UK FTSE All-Share 9.9%	Japan TOPIX -4.9%

Source: FTSE, LSEG Datastream, MSCI, S&P Global, TOPIX, J.P. Morgan Asset Management. All indices are total return in local currency, except for MSCI Asia ex-Japan and MSCI EM, which are in US dollars. Past performance is not a reliable indicator of current and future results. Data as of 30 September 2024.

Source: J.P.Morgan

Chart #6

Investors All-in

Sentiment in the equity market has continued to pick up throughout Q3 and is now through the roof. U.S. equity futures positioning by investors (excl. market-makers) just hit a net long of approx. $290 billion, the most on record. This net long positioning by investors has more than doubled since the beginning of the year, and currently sits at a level over twice as high as those seen during previous peaks in early 2018 and 2020. This sentiment is further highlighted by the Fear & Greed Index reaching levels of "extreme greed" for the first time since March. With U.S. household stock allocation also hitting new highs, investors appear to be all-in on stocks.

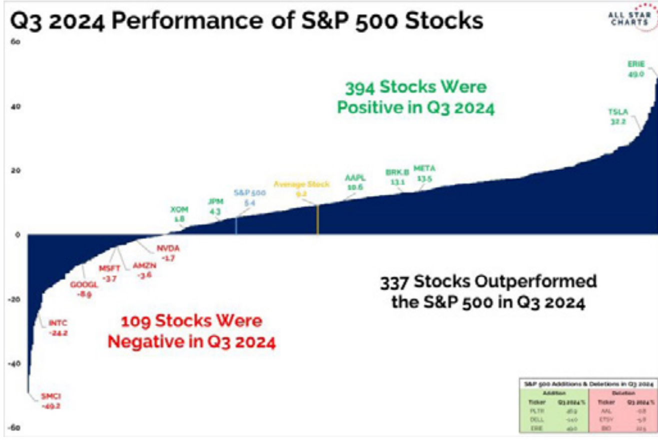
Source: Goldman Sachs FICC & Equities Division Futures Strats Group as of 24-Sep-2024
Past performance is not indicative of future results

Source: The Kobeissi Letter

Chart #7

Bulls continue charging ahead

Bulls are thriving as Q3 has been favourable to equity markets. The quarter ended on a high note, with the S&P500 posting a green September for the first time in 5 years. The bull market also appears to continue broadening (a prediction we made for 2024), with 337 stocks outperforming the S&P500 in Q3. Overall, 394 stocks were positive in Q3, with the index closing at 5.3% for the quarter. With tech stocks struggling, it was value stocks that took the lead in the third quarter. US value stocks managed to outperform growth by 7% points, with small caps rallying in anticipation of lower rates to come.



Source. All Star Charts

Chart #8

Fixed income rally on easing rate expectations

Fixed income markets performed strongly in Q3 2024, largely driven by the anticipation of lower interest rates, and increasing confidence of a soft landing for the economy. The changing outlook on interest rates boosted government bonds, with U.S. Treasuries returning 4.7%, while European sovereign bonds gained 4.0% during the quarter.

Investment-grade (IG) credit spreads narrowed slightly by the end of the quarter, resulting in a 6.3% quarterly return. High-yield bonds followed a similar trend, leading to gains of 5.3% in the U.S. and 3.5% in Europe. Emerging market debt saw a strong rally, gaining 6.1% and ranking near the top of fixed income sector performances year-to-date.

Exhibit 3: Fixed income sector returns

2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	Q3 '24
Euro Gov. 1.6%	US HY 17.5%	EM Debt 9.3%	Euro Gov. 1.0%	EM Debt 14.4%	Global IL 12.7%	US HY 5.3%	US HY -11.2%	US HY 13.5%	US HY 8.1%	Global IG 6.3%
EM Debt 1.2%	EM Debt 10.2%	Global IG 9.1%	US Treas. 0.9%	US HY 14.4%	Global IG 10.4%	Euro HY 3.4%	Euro HY -11.7%	Euro HY 11.9%	EM Debt 8.0%	EM Debt 6.1%
US Treas. 0.8%	Euro HY 10.1%	Global IL 8.7%	US HY -2.3%	Global IG 11.5%	US Treas. 8.0%	Global IL 2.7%	US Treas. -12.5%	EM Debt 10.5%	Euro HY 6.7%	Global IL 6.0%
Euro HY 0.5%	Global IG 4.3%	US HY 7.5%	Global IG -3.6%	Euro HY 10.7%	US HY 6.1%	EM Debt -1.5%	EM Debt -16.5%	Global IG 9.6%	Global IG 5.3%	US HY 5.3%
Global IG -3.6%	Global IL 3.9%	Euro HY 6.1%	Euro HY -3.6%	Global IL 8.0%	EM Debt 5.9%	US Treas. -2.3%	Global IG -16.7%	Euro Gov. 7.1%	US Treas. 3.8%	US Treas. 4.7%
US HY -4.6%	Euro Gov. 3.2%	US Treas. 2.3%	Global IL -4.1%	US Treas. 6.9%	Euro Gov. 5.0%	Global IG -2.9%	Euro Gov. -18.5%	Global IL 5.8%	Global IL 3.2%	Euro Gov. 4.0%
Global IL -5.0%	US Treas. 1.0%	Euro Gov. 0.2%	EM Debt -4.6%	Euro Gov. 6.8%	Euro HY 2.7%	Euro Gov. -3.5%	Global IL -22.9%	US Treas. 4.1%	Euro Gov. 2.0%	Euro HY 3.5%

Source: Bloomberg, BofA/Merrill Lynch, J.P. Morgan Economic Research, LSEG Datastream, J.P. Morgan Asset Management. Global IL: Bloomberg Global Inflation-Linked; Euro Gov.: Bloomberg Euro Aggregate - Government; US Treas: Bloomberg US Aggregate Government - Treasury; Global IG: Bloomberg Global Aggregate - Corporate; US HY: BofA/Merrill Lynch US HY Constrained; Euro HY: BofA/Merrill Lynch Euro Non-Financial HY Constrained; EM Debt: J.P. Morgan EMBIG. All indices are total return in local currency, except for EM and global indices, which are in US dollars. Past performance is not a reliable indicator of current and future results. Data as of 30 September 2024.

Source: J.P.Morgan

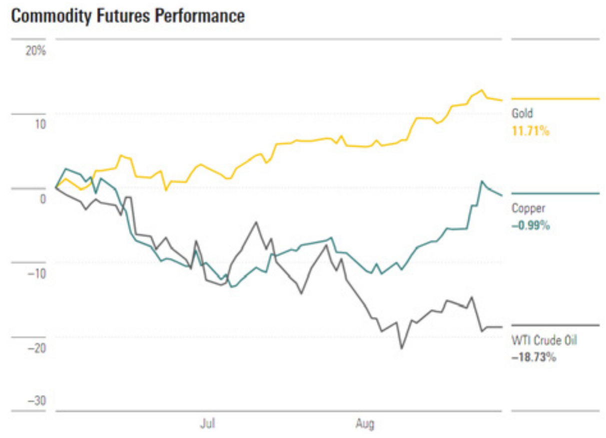
Chart #9

Energy slumps, precious metals shine

In the third quarter of 2024, commodity markets experienced relatively muted performance overall, returning just 0.7%. Amid ongoing concerns about the global economy, energy markets took a hit: Brent Crude oil prices fell by 17% largely driven by weakening demand in China, compounded by OPEC+ easing production cuts later in the year.

Meanwhile, the precious metals market performed well. Gold's new all-time highs rally continues, soaring over 11% over the quarter. This rally is now supported by the U.S. Federal Reserve's rate-cutting cycle, which historically has led to strong gains in the following months. Similarly, silver rose more than 6%.

Copper saw only a marginal increase of approximately 1% in Q3 2024, following a mid-year surge driven by rising demand from the energy transition and power needs for AI-related data centers. As a metal widely used in various industrial processes and products, copper prices faced pressure from concerns about declining demand for industrial materials in China.



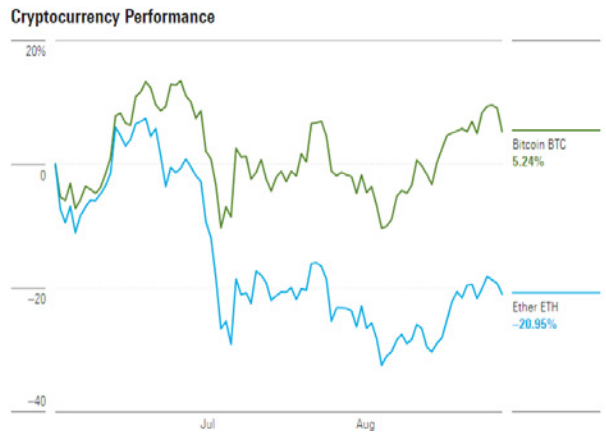
Source: Morningstar

Chart #10

A more cautious crypto market

After posting spectacular gains at the start of the year following the approval of its first spot ETFs, bitcoin performed rather modestly in the third quarter, returning 5.24%. This relative stagnation can be explained by a slowdown in investor enthusiasm after the initial euphoria linked to the approval of ETFs.

Meanwhile, ether suffered losses of over 20%. Interest in ether also waned after the launch of Ethereum ETFs, which failed to generate the hoped-for enthusiasm, and investors preferred to turn to safer havens in the face of market uncertainty.



Source : Morningstar

Unbreakable?

Key takeaways

- Overall, the overall macro and liquidity conditions are rather positive for risk assets. Still, equity market valuations are rich, especially in developed markets and some risks are under-priced. Consequently, while we keep our preference for equities over bonds, we refrain to increase exposure at this stage. We keep our neutral stance on equities.
- Our view on Eurozone equities is downgraded from neutral to negative, mainly due to weakening economic trend, while we upgrade our view on emerging markets from negative to neutral (China stimulus, improving earnings dynamic, room for easier monetary policy).
- Within rates, we continue to favour the 1-10 years segment over long-dated bonds.
- We keep our gold and hedge funds exposure for diversification purposes. Our stance on currency (neutral dollar against major pairs) is unchanged.

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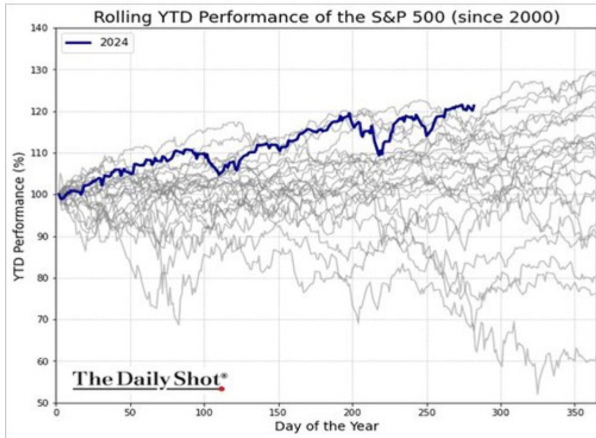
THE BIG PICTURE

At the time of our writing, the S&P 500 is about to hit $50 trillion in market cap for the first time in history. It's now up +40% since October 2023's low and +22% in 2024, making it the best year-to-date performance of the decade for this time of the year.



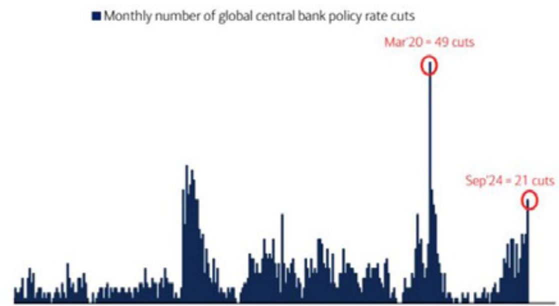
This euphoria is taking place despite the Russia-Ukraine war still going on, very high tensions in the Middle East and a very uncertain US elections outcome. Meanwhile, equity valuations remain highly demanding especially for the US large-caps, and bullish sentiment is through the roof: US equity futures positioning by investors excluding market-makers just hit a net long of ~$290 billion, the most on record.

Since the beginning of the year, net long positioning has more than doubled. This is also twice as high as during the previous peaks seen in early 2018 and 2020. Meanwhile, US households' stock allocation as a percentage of financial assets hit a new record of 41.8% in Q2 2024. Investors are all-in on stocks.

Are we in bubble territory for stocks?

Not necessarily. There are indeed some fundamental reasons to justify the current market advance.First, we are currently facing an almost synchronised global monetary cycle. The two largest economies in the world – the US and China – are injecting fiscal and monetary policy stimulus at the same time. September 2024 has been the biggest month of monetary easing since April 2020. Last month, central banks around the world cut interest rates 21 times, the most since the COVID crisis. This was also the 3rd highest number of cuts since the Great Financial Crisis.

Chart Sep'24 is biggest month of monetary easing since Apr'20
Monthly global central bank policy rate cuts



Source: BofA Global Investment Strategy, Bloomberg. Large sample of 100+ central banks

Secondly, recent economic data shows that the hard landing scenario seems less and less plausible. Some economies – e.g. Germany – might already be in recession. But in the US, Citigroup economic surprises index is at its highest since April, having flipped positive recently.

The recent stimulus package announced in China – while unlikely to trigger a major reacceleration of the Chinese economy - could be a boon for global economic growth especially in emerging markets. With oil prices way off the highs, a weaker dollar than at the start of the year and stable bond yields, non-US equity markets are currently enjoying some much welcome tailwinds.

On the earnings front, the usual negative revision is taking place ahead of the third quarter earnings season. However, earnings momentum remains positive and global equity indices should see their underlying companies grow earnings by high single to low double-digits in 2025. Profits have kept pace with nominal GDP and margins are at record high. Core companies are monsters with high share buy backs, sky high ROEs, and huge free-cash-flow generation.

Stocks are indeed expensive vs. bonds but given new risks with bonds (e.g. massive supply due to fiscal indiscipline in most G7 countries), a lower Equity Risk Premium might be warranted.

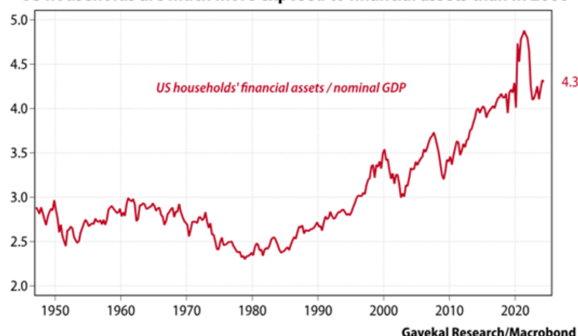
So, is this market unbreakable?

Not so fast.

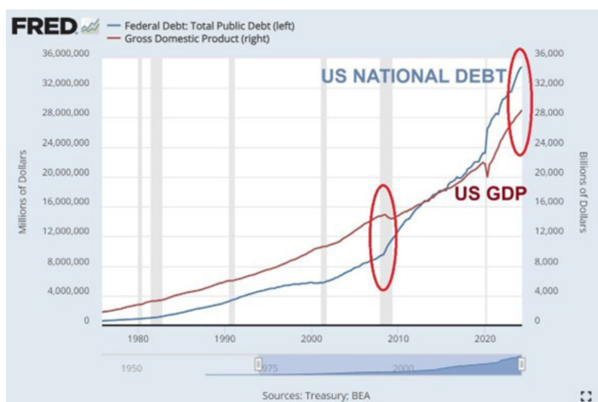
First, we need to consider the "tail risks" adjacent to our core scenario which is a soft landing of the global economy. While the odds of a hard landing of the global economy have been decreasing recently, we need to keep in mind that historically, most hard landing have started with a soft landing. For example, there is a "J-curve" effect once the economy starts to slow down, with an acceleration of the downside once the job market starts to get impacted.

Second, markets might have been getting ahead of themselves when it comes to the number of rate cuts that the Fed might be willing to implement. Another "tail scenario" is a no-landing, which could force the Federal Reserve to put on hold monetary easing. This could trigger another rise in bond yields, putting pressure on equity market valuations. In the case of a "no-landing" scenario, premature monetary easing could trigger a secondary wave of inflation with unpleasant consequences for equity markets.

Third, in 2000, US households were less exposed to financial assets than they are today. Back then, the value of US households' financial holdings was roughly 3.5 times US GDP. Today, that multiple is 4.3 times—almost 25% higher. As the US consumer contributes to roughly 80% of the US economy, any severe equity market pullback could have severe consequences on their morale and spending habits, hence affecting economic growth. In this context, it is not so much the US economy impacting the stock market but rather the other way round.



Fourth, the risk of a "fiscal blowout" in the US or in Europe remains. In the US, a budget deficit of 6% at full employment is unprecedented. We live an era of fiscal dominance which means that profits would be lower without the fiscal excesses. Debt stock over 100% of GDP is the largest in peace time. If interest rates stay high, debt sustainability is in question and could at some point incentivise investors to require much higher yields on government bonds issued by the most indebted G7 countries. Previous recessions like in 2008 or 2011 have come from the private sector borrowing too much.



Finally, geopolitical uncertainties remain elevated. The new US President and Congress might not necessarily please the financial markets. Meanwhile, any escalation in the Middle East could trigger a rise in oil prices and increase the odds of a stagflation scenario.

What does it mean in terms of asset allocation?

Going forward, we expect the Fed rate cut cycle to proceed gradually. Barring a financial crisis or a sharp and unexpected change in the path of inflation or unemployment, the current rate-cutting cycle is not going to be dramatic; we expect the Fed to make incremental, 25 bps cuts to its policy rate. Moreover, the Fed is going to stay highly data dependent and will calibrate accordingly.

Overall, this is a rather positive scenario for risk assets. Still, equity market valuations are rich, especially in developed markets, while some risks seem to be underpriced due to Middle East tensions and US election uncertainties. Consequently, while we keep our preference for equities over bonds, we refrain to increase exposure at this stage. We keep our neutral stance on equities. Our view on Eurozone equities is downgraded from neutral to negative, mainly due to weakening economic trend, while we upgrade our view on emerging markets from negative to neutral (China stimulus, improving earnings dynamic, room for easier monetary policy).

Within rates, we continue to favour the 1-10 years segment over long-dated bonds.

We keep our gold and hedge funds exposure for diversification purposes. Our stance on currency (neutral dollar against major pairs) is unchanged.

A MACRO & MONETARY POLICY UPDATE

GLOBAL GROWTH

Diverging dynamics are at play in the global economy. The United States remain surprisingly resilient and continues to grow strongly, while Europe extends its worrying downward trend, dragged down by Germany. In the meantime, after a summer slowdown, China's short-term prospects have suddenly improved thanks to the economic package recently announced. At a sectoral level, global manufacturing activity remains under pressure while services are holding up well in most regions.

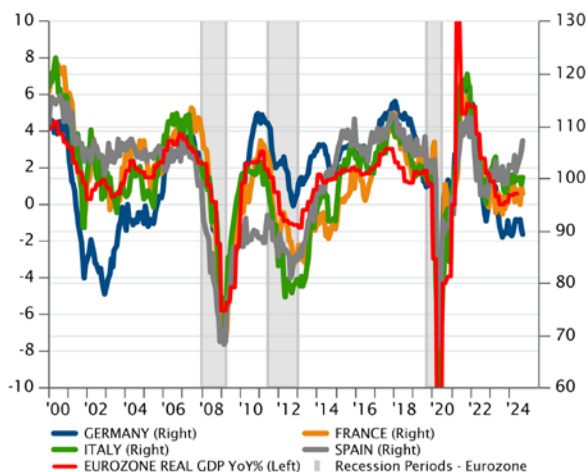
Economic surprises are positive again in the US, but still negative in Europe. In China, the dynamic should improve soon.

This desynchronisation of growth dynamics, coupled with the coming US elections, raises the level of uncertainty surrounding the outlook. However, this should not detract

from the fact that the world's two largest economies will benefit from an easing of monetary policy and from fiscal support over the coming months, which should be enough to keep global growth on a positive trend.

More specifically, in the United States, domestic consumption remains firm and supports the "soft landing" scenario, as low unemployment and softer inflation keep fuelling households' spending. While some indicators point to downside risks for the labour market, recent employment data has defied expectations, and the ongoing easing in financing conditions will likely prevent an unwarranted deterioration in economic conditions in the months ahead.

Europe faces a much less favourable economic backdrop as the prolonged slump in manufacturing activity weighs heavily on the German economy. Growth had already started to slowdown since the beginning of the summer, and the recent data has confirmed this negative trend. Activity in Germany is depressed and continues to decline, to the point where GDP is now expected to stagnate at best for the entire year 2024. In France, the "OlympicEffect" has quickly faded away. In the meantime, in stark contrast with last decade's dynamics, peripheral economies now exhibit better growth momentum, especially Spain that is led by tourism and strong service sector activity. However, overall growth momentum is weak for the monetary union and keeps undershooting expectations. This situation weighs on the Swiss economy as subdued demand in its main export market combined with the strength of the CHF are a drag for exporting sectors.



As for China, the economic measures announced at the end of September are unambiguously positive. During the summer, further signs of growth slowdown had raised the risk of the economy slowing below stall speed. Chinese authorities therefore decided to "go big" on providing support to their ailing economy, and the package appears sufficiently large and broad based to act as a positive shock. However, if this will likely reverse the negative trend and spur economic growth in the months ahead, medium and long-term challenges remain for China. Unfavourable demographic dynamics, depressed business and households' sentiment, and rising trade barriers in the US and in Europe will remain headwind for China's growth going forward.

GLOBAL INFLATION

Inflation is slowing down across the board and now tends to surprise to the downside in developed and emerging economies. Labour market normalisation and slower wage growth support the disinflationary dynamic. Inflation rates are now back around central banks' targets in the US and in the Eurozone, China is flirting with deflation and deflationary pressures are increasing in Switzerland. The recent rise in energy prices might exert short term upward pressures on inflation but, unlike in 2021/22, it appears unlikely to reignite a true inflationary dynamic given a more subdued global demand and normalised labour markets.

MONETARY POLICY

The expected global rate cut cycle has started in Europe and will start in the US, with room to cut if inflation actually normalises. Central banks will cut rates in developed and emerging economies and will likely proceed gradually as long as economic growth remains positive, but they could cut significantly in 2025 if inflationary pressures truly dissipate. The potential for rate cuts might be even larger in some EM economies once the Fed starts cutting rates.

For the US Federal Reserve, the time has come for policy to adjust. The direction of travel is clear, and the timing and pace of rate cuts will depend on incoming data. Inflation is slowing and close to target and the labour market has normalised. The Fed will start cutting rate in September and will continue, possibly at each meeting, into 2025.

For the ECB, as wage growth slows, the path for more rate cuts is cleared. Upward wage pressures were the lingering source of concerns for some ECB officials, and the latest data proved to be quite reassuring on that front. Inflation is close to target and wage pressures are easing in the Eurozone, clearing the way for ECB rate cuts. Soft economic growth and waning upward pressures on wages and prices no longer warrant the current level of restrictiveness of the ECB policy. The ECB will cut rate gradually (25bp in September, 25bp or 50bp in Q4 & possibly 100bp in 2025).

In Switzerland, the CHF cash rate is now close to neutral, and the SNB has already done most of the job. One or two rate cuts might be warranted, in 2024 (or 2025).

When it comes to global liquidity, conditions are rather neutral, and broad Financial Conditions remain quite accommodative. Quantitative Tightening is still ongoing in the US and Europe, but "cleaner" measures of liquidity have broadly stabilised. Broad Financial Conditions remain accommodative as market credit spreads are tight and equity markets close to ATH.

THE WEIGHT OF THE EVIDENCE

Our asset allocation preferences are based on 5 indicators, including 4 macro and fundamental indicators (leading) and 1 market dynamics (coincident). The weight of the evidence suggests a neutral allocation to equities. Below we review the positive and negative factors for each of them.

Indicators review summary - our five pillars

The Macro Cycle remains positive for equity markets. China will benefit from economic stimulus and the US economy is holding up remarkably. Inflation is slowing down across the board and central banks have now embarked on their rate cutting cycle.

Liquidity remains neutral as the effects of ongoing quantitative tightening are balancing the impact of central banks' rate cuts.

We remain neutral on earnings growth. Bottom-up, the consensus is expecting an acceleration/broadening but a deceleration in China and Japan. However, revisions for 2025 are only positive in these two latter countries.

However, our equity valuations indicators remain in negative territory, as seen in the equity section. Valuations in China and in Europe are in line with historical averages, but prospects are now more attractive in China.

Market factors are still very positive. Despite the slight correction at the beginning of the month, the trend indicators remain positive. In parallel, technical indicators are neutral as markets have not reached yet the "overbought" territory. Market sentiment remains neutral, but one component (the put call ratio) is showing complacency. Finally, market breadth and volume are back to positive as the participation is strong in the USA but less so in Europe. Consequently, the overall signal is very positive.

Overall, the weight of the evidence is slightly positive for equities.

	(+)	(-)	WEIGHT OF THE EVIDENCE
MACRO CYCLE	The Macro Cycle remains positive for equity markets. The US economy is holding up remarkably and supports a "soft landing" (or even "no landing"?) scenario. China will benefit from the recent stimulus. Inflation is slowing down across the board and central banks have now embarked on their cutting cycle.	Uncertainty around the outcome of US elections makes the outlook uncertain, while Europe is clearly slowing down, with risks of stagnation or mild recession rising. China's structural challenges remain.	POSITIVE
LIQUIDITY	Financial conditions remain on the "easy side". Central banks will continue to cut rates in the coming months to avoid maintaining unnecessarily restrictive financing conditions as inflation gradually slows down. The pace of US Quantitative Tightening is slowing down, easing pressures on USD liquidity.	Central banks, especially the Fed as long as the US economiy remains strong, might be cautious in adjusting their policy stance toward neutral. Quantitative Tighening is still ongoing in the US and Europe.	NEUTRAL
EARNINGS GROWTH	The focus is now turning on 2025 earnings, and the bottom-up consensus calls for an acceleration in earnings growth: a broad-based acceleration in earnings growth in the US and a normalization of growth in Europe thanks to high employment and lower interest rates.	While not unusual, revisions remain negative across the board.	NEUTRAL
VALUATIONS	Valuations are reasonable in regions such as Europe and Asia.	We are cautious on valuation particularly for US equities. Uncertainties about the economic outlook in 2025 remain elevated (impact of US elections, weak economic momentum in Europe). The tensions in the middle east remain a potential black swan.	NEGATIVE
MARKET FACTORS	Despite the slight correction at the beginning of the month, the trend indicators remain positive (both are positive). In parallel, technical indicators are neutral as markets have not reached yet the "overbought" territory. Finally, market breadth and volume are back to positive as the participation is strong in the USA but less so in Europe.	Market sentiment remains neutral but one component (the put call ratio) is showing complacency.	POSITIVE

ASSET ALLOCATION VIEWS

EQUITIES

Regions, sectors, and styles

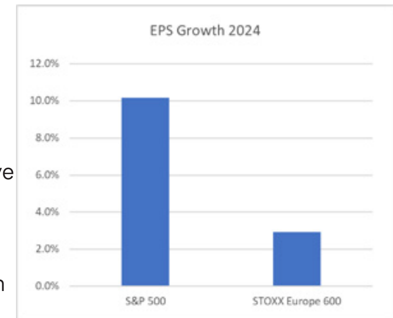
We continue to be neutral (slightly overweight due to market effects) on equities on the backdrop of a slowing global growth environment and elevated valuations partially offset by many central banks across the world that are cutting interest rates.

From a regional perspective, we are neutral on US equities as the soft-landing scenario continues to be well alive with resilient economic data and an ongoing easing cycle by the Fed, but valuations are stretched. Conversely, we are exercising caution regarding Europe due to a weakening economic trend. Germany, in particular, is facing challenges with sluggish manufacturing activity and a struggling automobile sector—one of Europe's largest employers—impacted by weak demand and fierce competition from Chinese brands.

Regarding emerging markets and China, we are now neutral as the measures announced by the Chinese government are limiting the risks of further slowdown in the economy and deflationary pressure. On the other hand, the central government is not yet willing to push for a large stimulus package while some underlying negative trends such as the demography remain negative.

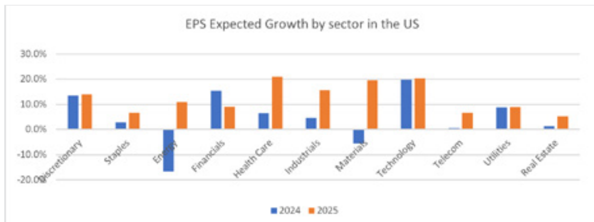
Earnings

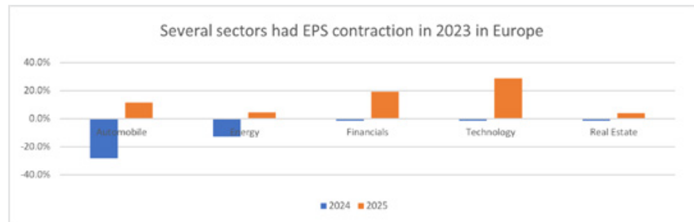
We are at the beginning of the third quarter earnings season and investors should expect a relatively positive message going into year-end in the US at least. Effectively, government spendings remain high in the US supporting consumption, and only a few companies have announced profit warnings in recent weeks. On the other hand, Europe is on the weak side as most large auto makers have issued profit warnings and the luxury sector won't be supportive yet as China will remain soft in the near-term. Therefore, revisions remain negative for Europe for this year earnings. The key topics investors will watch is the resilience of the consumer particularly in the US, the pace of investment in the AI field, and if manufacturing shows any sign of pick-up. We believe these trends will continue while employment remains high in the US, and large technology companies will continue to invest as their profits remain high.



However, attention will soon shift to 2025 earnings, where the debate intensifies. The bottom-up consensus calls for a broad-based acceleration in earnings growth, particularly in the US, where a wider range of sectors is expected to report higher earnings. Many investors anticipated this broadening to occur in 2024, but cyclical sectors such as industrials, materials and smaller market capitalisations have yet to experience the effects of a broader economic recovery.

In Europe, as earnings growth is muted this year, the consensus expects a "normalisation" of the growth rate next year as five sectors had earnings contraction this year, and lower interest rates by the ECB are expected to be supportive.





Overall, for 2025, the consensus is clearly positive as bottom-up estimates are expecting a broad-based acceleration in earnings growth in the US and a normalisation of growth in Europe thanks to high employment and lower interest rates. However, while not unusual, revisions remain negative the board.

Let's look now at the "Magnificent 7": Microsoft, Apple, Nvidia, Alphabet, Tesla, Amazon, Meta. These were the major contributors of earnings growth both last year and this year in the US. Looking at the consensus, while decelerating, still exhibit resilient growth, and are expected as a group to outgrow the broad market in earnings growth next year. Thus, investors should not overlook them.

Valuations

We are cautious on valuation particularly for US equities. We acknowledge lower interest rates are a positive for valuation as an acceleration in earnings growth into next year. However, there are uncertainties about the economic pick-up as the US economy may slow further and the situation in Europe is far from robust. Finally, the tensions in the Middle East remains unsettling for the markets. Given this context, we believe valuation is expensive in the US while more reasonable in some other regions such as Europe and Asia.

FIXED INCOME

Overview

We maintain a neutral position on fixed income within our portfolios, guided by a mix of encouraging inflation data, a cooling job market, and the onset of the Federal Reserve's rate cut cycle. While these positive indicators provide some optimism, several factors urge caution. Ongoing supply pressures driven by the need to finance the large fiscal deficit, a flat yield curve, and persistent interest rate volatility suggest it is premature to adopt a more bullish stance. Additionally, while our base case remains a soft landing, the potential for significant long-term interest rate declines is limited. In this context, we continue to favour the short and intermediate segments of the yield curve over long-duration bonds. We remain cautious on high yield and hold a neutral position on investment grade credit. Valuations in the high yield space are particularly stretched—especially compared to investment grade credit—given where we are in the economic cycle. Furthermore, with potential volatility expected in the second half of 2024, we are also cautious on USD-denominated emerging market debt. However, EM local debt could present opportunities if the US dollar continues to weaken.

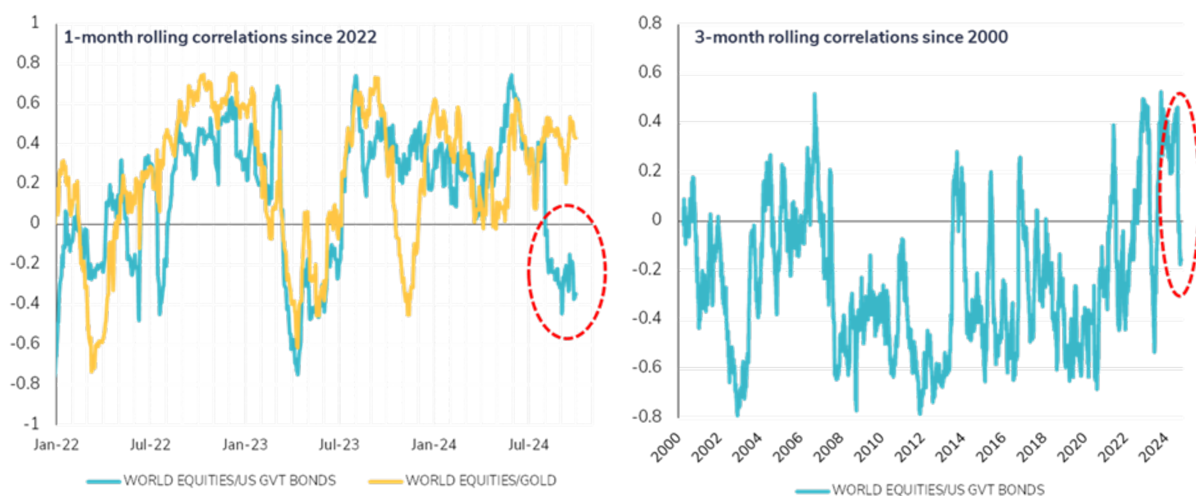
Government Bonds

Our outlook for government bonds with maturities under 10 years remains positive, as we anticipate favourable conditions for yield improvements by year-end. This view is supported by several key factors:

- Reassuring inflation data and economic stability: The US economy shows signs of normalisation, with a cooling job market and gradually declining inflation rates, despite occasional volatility.
- Monetary policies: Federal Reserve Chair Powell has initiated the rate cut cycle, which is expected to continue. In addition, easing quantitative tightening and improving liquidity in the Treasury bond market through a buyback program are expected to further stimulate demand.
- Bonds as a diversifier: Bonds are once again proving their worth as effective diversifiers in balanced portfolios, with their correlation to equities turning negative.

However, we remain cautious on longer-term bonds due to the flat yield curve, negative term premiums, ongoing rate volatility, and the pace of interest rate declines. Other concerns include the growing US fiscal deficit and increased Treasury issuance.

Bond-equity correlation turns negative in August for the first time in a year!



Source: Syz CIO office, Bloomberg

In Europe, we maintain a neutral stance as the European Central Bank initiates monetary policy normalisation, beginning with its first rate cut in June and in September. We anticipate additional rate cuts in October and December, which could support a bull steepening of European rates. The market has largely priced in the French election outcomes as a contained, idiosyncratic risk, with the yield spread between 10-year Italian and German bonds returning to pre-election levels of 130bps. However, the bond market still perceives some risk, as the 10-year French real yield is near its highest level this cycle. While European wages remain a concern, the latest wage report shows promising progress, and ECB members are confident of further normalisation soon. Our outlook on UK government bonds is also neutral but close to turning positive. The political shift following Labour's victory has not significantly impacted the gilt market, with memories of the 2022 crisis under Liz Truss fostering caution towards expansive fiscal policies.

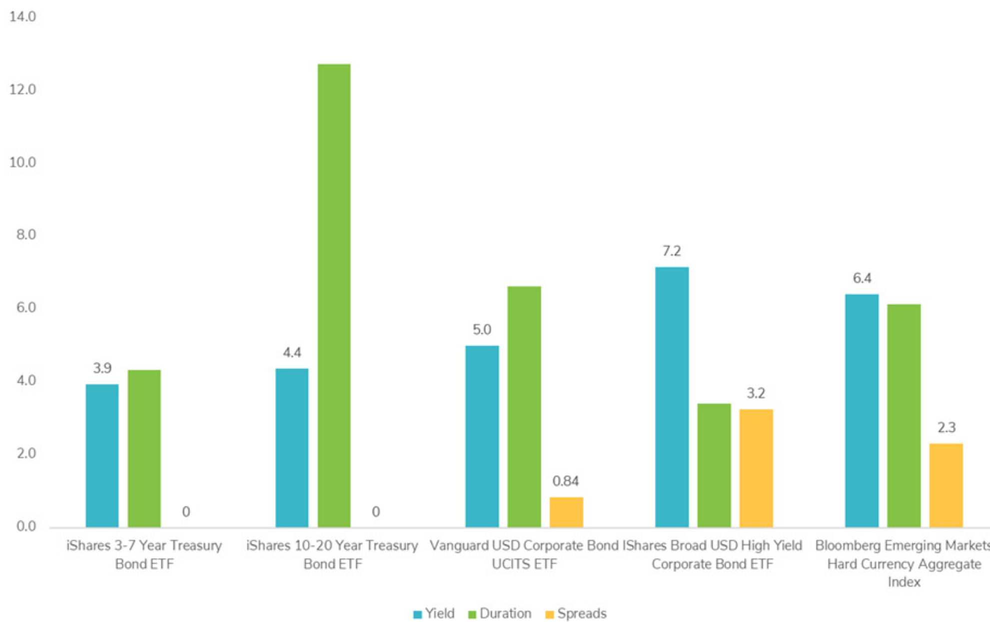
Market perception of French election risks

Source: Syz CIO Office, Bloomberg.

Corporate Bonds

Our stance on investment-grade bonds remains neutral. Credit spreads have tightened significantly to their lowest levels since 2021, reducing the safety margin to just 15% of the total yield. Current market conditions are "priced to perfection," necessitating close monitoring. For the first time since 2022, there are more BBB-rated bonds with a negative outlook than those with a positive outlook. Despite these factors, the solid macroeconomic backdrop and concerns over US Treasury sustainability suggest that it might be premature to reduce credit exposure. In the high-yield sector, we see selective opportunities in short-term corporate high-yield bonds due to their favourable risk/reward profile, though we acknowledge that overall valuations in high yield are stretched, especially if volatility increases in the second half of 2024.

Yield composition across fixed income segments



Source: Syz CIO Office, Bloomberg.

Emerging Markets

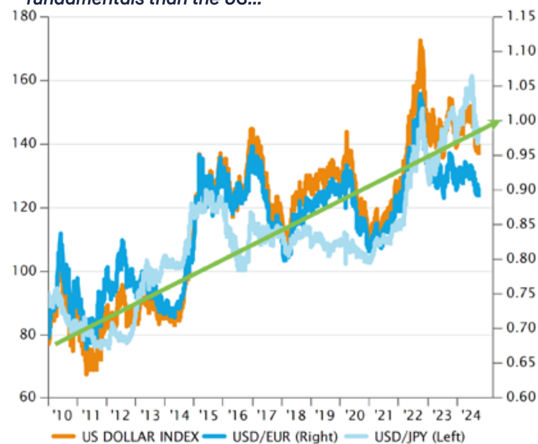
Our stance on hard-currency EM debt remains cautiously negative, though we identify some attractive opportunities in bonds with maturities up to four years. Market sentiment toward EM debt remains subdued, as evidenced by ongoing negative capital flows and rising short interest in USD-denominated EM debt. Valuations appear stretched, with EM corporate spreads at their narrowest since 2007. However, the recent weakening of the US dollar and declining US real interest rates have provided some relief to EM local debt, making it an attractive consideration if the trend continues.

FOREX (view against USD)

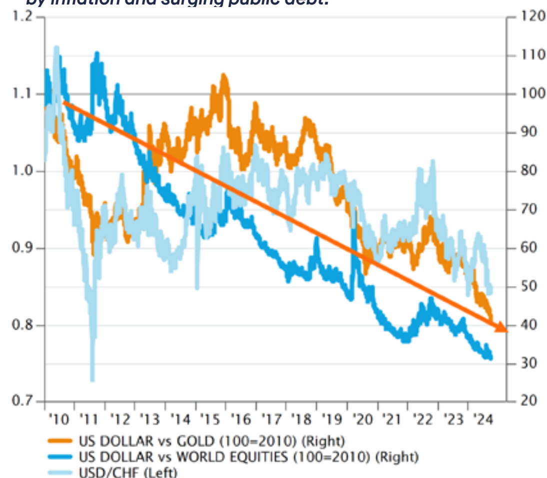
Following recent economic development and the continuation of the global rate cut cycle, we now expect the US dollar to remain broadly stable against most major currencies. With the Fed now having joined the global rate cut movement, interest rate differentials will no longer be as much of a support for the greenback, and the upside potential for the USD appears limited.

We bear in mind that the outlook for the US dollar is relative: one can only have a view on it against something else. Our current neutral view on the greenback is set against other major currencies, around the current strong level where it has been driven by higher rates and relatively favourable (or least unfavourable) economic fundamentals.

The US dollar has been strengthening against currencies with worser fundamentals than the US...



... but its value vs real assets or sound currencies has been eroded by inflation and surging public debt.



ALTERNATIVES

We remain positive on gold, which continues to exhibit low volatility with other asset classes, and should be a beneficiary of any tail risk event. We note that a significant gap remains between gold and real yields. Why? Because: 1) With debt sustainability having become an ever-increasing issue, the market anticipates that real interest rates cannot stay at this level for too long; 2) Investors buy gold as insurance against adverse circumstances, such as inflation, recession, etc. 3) There is heavy demand stemming from central banks, especially in emerging markets.

We are keeping a positive stance on commodities as a portfolio diversifier and protection against inflation upside, which is not our core scenario. Commodity prices are moving higher, driven by resilient US growth, geopolitical uncertainty, segmentation of global trade and AI demand for energy.

We maintain a neutral view on hedge funds. We like well-established global macro funds that have a multi-portfolio managers approach. We cautiously like relative value funds but are wary of liquidity conditions. We like having a core position in a diversified systematic strategy with a long-term commitment. We prefer staying away from equity long/short and directional funds as their beta is too high. We do not like event-driven funds, as we believe the merger and arbitrage landscape will be very challenging in 2024.

INVESTMENT CONCLUSIONS

- Overall, the overall macro and liquidity conditions are rather positive for risk assets. Still, equity market valuations are rich, especially in developed markets, while some risks seem to be underpriced due to Middle East tensions and US election uncertainties. Consequently, while we keep our preference for equities over bonds, we refrain to increase exposure at this stage. We keep our neutral stance on equities.
- Our view on Eurozone equities is downgraded from neutral to negative (mainly due to weakening economic trend) while we upgrade our view on emerging markets from negative to neutral (China stimulus, improving earnings dynamic, room for easier monetary policy).
- Within rates, we continue to favour the 1-10 years segment to long-dated bonds.
- We keep our gold and hedge funds exposure for diversification purposes. Our stance on currency (neutral dollar against major pairs) is unchanged.

TACTICAL ASSET ALLOCATION (TAA) DECISIONS

TAA Balanced moves

We started the year with an allocation to equities which was close to our Strategic Asset Allocation (SAA). Due to market effects, the allocation has been rising progressively to overweight throughout the first half of the year and we didn't sell into strength. However, during our July Tactical Asset Allocation Committee, we decided to rebalance portfolios towards a neutral allocation to equities, which means that we effectively reduced our exposure to equities to neutral. Since then, positive markets have been driving our exposure to a slight overweight.

As mentioned earlier, we favour equities over fixed income but refrain on adding more risks at this stage. The true exposure to equities within client portfolios is thus slightly overweight versus our Strategic Asset Allocation.

Within equities, we decided to downgrade European equities from neutral to negative and to upgrade Emerging markets from negative to neutral. See below matrix of preference moves.

ASSET ALLOCATION GRID

TACTICAL ASSET ALLOCATION (TAA) 4.10.2024

	--	-	NEUTRAL	+	++
Portfolio Risk		Cash	Fixed Income Equity Alternatives		
Fixed Income		HY (local or global hdg) EM Debt	Govies 10+ (local) Corporate IG (local)	Govies 1 - 10 (local)	
Equities		Euro Zone ←	United States United Kingdom Switzerland Japan → Emerging Markets		
Alternative Investments			Hedge Funds		
Commodities				Gold Commodities	
Forex (vs USD)			EUR CHF GBP JPY EM currencies		

Change from last month: More attractive → Less attractive ← *Source: Investment strategy group - 4 October 2024*

US Elections 2024

Image source: iStock/MicroStockHub

As we approach the US Presidential election, the race remains highly uncertain, with both candidates neck and neck in the polls. The upcoming debates, along with recent events like Joe Biden's health issues and an assassination attempt on Donald Trump, have added to the unpredictability of this election, which could significantly impact the US economy and financial markets. Let's explore the key issues at stake and how the election outcome may affect equity and bond investments.

Adrien Pichoud
Chief Economist

Gaël Combes
Head of Equities

Gaël Fichan
Head of Fixed Income – Senior Portfolio Manager

We are now less than two months away from the US Presidential election. The first debate between Kamala Harris and Donald Trump will take place tomorrow, September 10th. A second debate will be organised in October, after the Vice-Presidential candidates have a dedicated debate on October 1st. The outcome of this election is highly uncertain, as the two candidates are currently neck and neck in the polls.

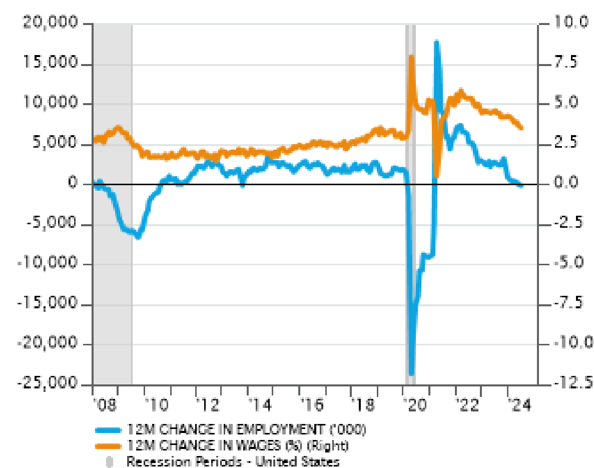
The summer's events, including Joe Biden's health issues, a poor debate by the incumbent president, an assassination attempt on Donald Trump, and Kamala Harris's nomination, have created uncertainty in what was expected to be a 2020 election remake.

Yet, the agenda of the two candidates is radically different, and the upcoming election could alter the course of the US economy for the years to come. Uncertainty will likely fuel volatility on financial markets in the weeks ahead of November 5th. Depending on the outcome and the composition of the Congress, sectorial divergences in performance are to be expected in equity markets. Bonds markets will need to adjust to the impact of new policies amid slowing economic growth, rising public deficits, and the Federal Reserve's rate cuts. Let's look at the main issues at stake in this campaign and the potential impact of the election on equity and bond investments.

An election with slowing economic growth in the background

The US economy has shown surprising resilience over the past two years, enduring the worst inflation in decades and a brutal cycle of interest rate hikes, despite sluggish global economic growth. A very strong labor market associated with savings accumulated during the Covid pandemic have long fueled consumption spendings in the service sector. Those two drivers have sustained solid GDP growth, despite the weakness of some cyclical and interest rate sensitive sectors such as manufacturing and real estate. However, the impact of a very tight monetary policy by the Fed is being felt in 2024, as the employment market gradually cools off and allows for a slowdown in wage growth. The Fed had been waiting to be confident that the inflation was finally contained, which Jerome Powell has signaled by announcing that a rate cut cycle is set to begin.

Employment growth stalls, easing pressures on wages but rising fears of a recession



Recent economic data has raised fears that this growth slowdown could eventually turn into a recession at the crossroads of 2024 and 2025. As always, the economic situation will be crucial in the election, as any downturn could be blamed on Kamala Harris due to her key role in the current administration. In that respect, the evolution of US economic data in the weeks to come will be crucial not only for company earnings and interest rates but also for the election outcome, as the saying goes, "it's the economy, stupid."

Two fundamentally different economic agendas

There's still time before the election, and both candidates are likely to flesh out their programs in the coming weeks to try to tip the balance in their favour. Still, Kamala Harris and Donald Trump have already outlined several economic measures that they will push forward if they reach the White House. Unsurprisingly, the philosophy of their agenda differs fundamentally and could set the US economy on different trajectories depending on the outcome of the Presidential and Congressional elections. Beyond a bipartisan agreement to protect the US industry from Chinese exporters, the anecdotical shared proposal of removing taxes on tips, and a common intention to boost the housing market, the Republicans' and Democrats' economic programs are almost diametrically opposed.

Kamala Harris' economic program is logically in continuity with the policies implemented under Joe Biden's presidency. The Democrats' platform is a set of redistributive policies where fiscal support to families and low-to-middle income households would be financed by higher taxes on corporates and wealthy households. The emblematic economic measures championed by the current Vice-President are tax breaks for households with children, fiscal support to first-time homebuyers, a higher federal minimum wage, various forms of price control in several sectors (i.e. food, rents, prescriptions, bank fees), and an increase in the corporate tax rate from 21% to 28%.

In contrast, Donald Trump is campaigning on a program of reduced federal intervention in the economy, with lower regulation in several areas (energy, banks, utilities, healthcare, housing market), an extension of individual income tax cuts introduced during his first presidency, lower taxes on social security benefits, the reversal of subsidies for green energies introduced under Joe Biden, and a cut in the corporate tax rate to 15%.

The necessity to push back on China's aggressive mercantilism is one of the few bipartisan issues agreed on by Democrats and Republicans. The outgoing Biden's administration, of which Kamala Harris belongs to, has taken significant steps to restrict exports of US

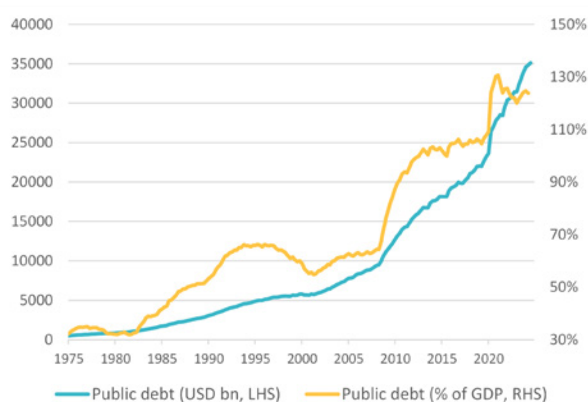
technology to China. It has also recently raised tariffs on imports from China in an array of strategic sectors such as semiconductors, EV, steel, or medical products. If elected, Kamala Harris would maintain the existing tariffs and trade restrictions, as well as possibly introducing additional levies on China.

Donald Trump, while aiming at less state intervention within the US economy, looks for assertive and increased interventionism when it comes to trade exchanges with the rest of the world. He intends to introduce a broad-based 10% tariff (possibly 20%) on all foreign countries' imports, and specific 60% tariffs on all imports from China. The stated goal of this approach is to boost the US industrial sector and to "make America the manufacturing superpower of the world." Donald Trump also appears more defiant toward international and multilateral organisations such as the UN, NATO and the IMF.

Fiscal deficits are here to stay

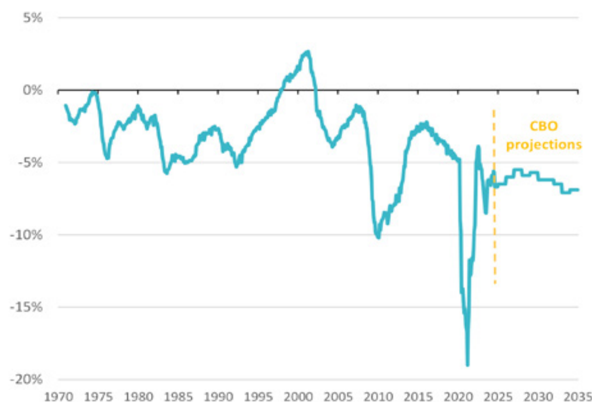
During Donald Trump's first term, the US public deficit steadily deteriorated until 2020. While the COVID-19 pandemic led to unprecedented deficits in 2020 and 2021, the Biden/Harris administration has not improved public finance since then. Instead, the federal deficit has continued to rise, approaching 7% of GDP this year and pushing U.S. public debt above $35 trillion, or 120% of GDP.

US public debt has been rising at an ever-faster pace



In the continuity of this trend, the economic programs of the two candidates are not expected to lead to smaller public deficits or a slowdown in the growth of public debt. Schematically, Kamala Harris intends to finance the support targeted to middle-to-low-income households with the rise in the corporate tax and the income tax on top earners. Donald Trump intends to compensate the loss of fiscal revenues from corporate and individual taxes by tariffs on imports from the rest of the world. Most independent estimates show that both programs will hardly be neutral for public finances and that deficits will remain high in the years ahead. According to the latest report of the Congressional Budget Office, the US public deficit is expected to hover around 6% of GDP for the next ten years. Financial largesse by either candidate is likely to worsen the situation.

12m US government budget balance (% of GDP, rolling 12m)



While the long-term trend for public finances is a real source of concern, in most developed economies like the United States like in most developed economies, it does not mean that a budget crisis is around the corner just yet. Deficits are not a burning issue if nominal economic growth is sufficient. Tellingly, since 2021, the debt-to-deficit ratio has declined in the US despite continuingly large deficits, because nominal GDP growth has been strong (real growth + inflation). If the US economy continues to grow around the current 5-to-6% nominal rate next year, expected deficits should not result in a worrying increase of the debt-to-GDP ratio. The risk lies in an unexpected deterioration of the economic situation, or a recession, which would simultaneously cause a deterioration of the public deficit and an increase in the debt-to-GDP ratio.

The election's impact on fiscal prospects is therefore likely to be broadly similar whoever becomes the next president: deficits are here to stay. In fact, the key element to gauge whether a further deterioration lies ahead or if some form of stabilisation is to be expected will lie in the composition of the US Congress. If the House of Representatives and the Senate are dominated by a majority of the President's party (a Sweep), then the new President will have more latitude to implement some of the most radical measures of the agenda, possibly leading to rising public deficits in the short run. Conversely, if the Congress is divided and the president's party does not have the majority in the two chambers, the ability to push forward ambitious legislations will be constrained, keeping the public deficit trajectory from altering much from the base case scenario.

What to expect for equity markets?

In the table below, we summarise what are the possible policy impacts of each camp by economic sector. Policy changes by the Republican camp are likely to be more pro-cyclical, with the risk of being inflationary over the medium-term.

In a nutshell:

- Republican sweep: positive equities with a pro-cyclical bias such as financials, energy, and industrials.
- Democrat sweep: equities to remain attractive with renewables and infrastructure the main beneficiaries.

	Republican sweep	Democrat sweep
EQUITIES	(+) Republican policies are generally pro-cyclical which is positive for equities. The negative would be too aggressive trade barriers.	(-) Tighter regulation, higher taxes and more spending directed by the government are incrementally negative. However, equities may still be favoured vs other asset classes as a better alternative
Technology	(=) Both parties are likely to continue to pressure big tech on antitrust and data privacy issues. On the other hand, both parties want to stay ahead in terms of digitalisation and AI.	
Financials	(+) Pro-deregulation will favour consolidation/ profitability and a steepening yield curve would benefit banks.	(-) Tighter regulatory environment to prevail.
Health Care	(=) Status quo to prevail as not in favour of more healthcare reforms.	(-) More reform likely with stricter regulation on drug pricing, insurance, etc.
Consumer Discretionary	(-) With more trade tariffs, consumer goods prices will increase offsetting the benefits of lower taxes.	(=) No meaningful increase in trade barriers but no tax benefits.
Communication Services	(=) Deregulation likely offset by higher long-term rates.	(=) Support for digitalisation to be counterbal-anced by regulation (M&A, data privacy).
Industrials	(+) Increase in infrastructure and defense spend-ing will benefit the sector.	(=) Infrastructure spending to increase but tighter regulation emission regulation a headwind.
Consumer Staples	(=) Generally, no meaningful impact for the consumer staples.	
Energy	(+) Supportive of fossil fuel with lower regulation for the sector.	(-) Likely a continuation of the Biden adminis-tration policy that favours renewable energy sources and stricter environmental regula-tions.
Utilities	(-) Higher long-term interest rates are a risk.	(+) Push for green energy project and govern-ment supports.
Materials	(+) Increase in infrastructure spending will act as a positive but heavy industry will face tighter regulation by the democrats.	
Real Estate	(=) Lower tax and regulation may be offset by higher long-term interest rates.	(=) Subsidies for low-income households may not solve the supply issues.

What to expect for bond markets?

Key takeaways: the federal Reserve will lead, but fiscal policies will set the tone

The Federal Reserve's monetary policy and the broader economic trajectory will remain the key drivers of bond market performance in the coming years. A Kamala Harris presidency would likely result in strong support for ESG investments, and more stable trade relations which could help contain inflation risks. Conversely, a Donald Trump presidency might drive higher inflation, a stronger dollar, and greater market volatility, particularly for emerging markets and sectors exposed to global trade. In either case, investors will need to closely monitor the Fed's policy and broader economic trends, as these factors will have the largest impact on bond markets in 2025 and beyond.

Government bonds: Fed's role in the yield curve

The 2024 election will have implications for government bonds, but the Fed's rate cut cycle will be the dominant force. The key question remains whether the U.S. economy can avoid recession and achieve a soft landing. However, the election's outcome will shape fiscal policies that could add pressure on long-term rates.

Kamala Harris as president would likely continue the current administration's approach, with increased spending on infrastructure, renewable energy, and social programs. This could result in higher government debt issuance and upward pressure on long-term yields. Should inflation remain moderate, the Fed's expected rate cuts could flatten the short end of the yield curve, but higher debt levels could keep long-term yields elevated. Harris's focus on moderate trade policies could help contain inflationary risks, stabilising bond markets to an extent.

On the other hand, Donald Trump in office would likely set a more aggressive fiscal expansion through significant tax cuts and higher defense spending, accompanied by tariffs. These policies could heighten inflationary risks, limiting the Fed's capacity for aggressive rate cuts. Under this scenario, the yield curve could steepen further, with long-term yields rising more sharply due to higher inflation expectations. Fiscal expansion and potential trade disruptions from tariffs could exacerbate inflation, pushing yields higher as investors demand more compensation for risk.

Regardless of the election outcome, a steepening of the yield curve appears likely. The trajectory of U.S. debt and fiscal deficits will continue to weigh on long-maturity bonds, limiting the potential for significant declines in long-term interest rates. A hard landing for the economy could temporarily push long-term yields lower, but structural pressures from deficits will persist.

The US yield curve is likely to steepen in any case!

Source: Bloomberg

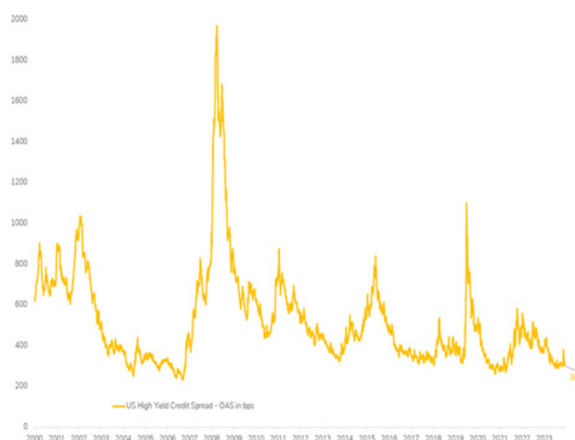
Corporate bonds: fiscal policy and profitability vs. fiscal policy

The corporate bond market is especially sensitive to fiscal and regulatory shifts that will differ significantly depending on the election's outcome. However, the broader economic outlook and the Fed's rate cuts will remain crucial in shaping borrowing costs and credit spreads.

A Harris administration may introduce higher corporate taxes and stricter regulations, particularly in sectors like healthcare, technology, and finance. These measures could weigh on corporate profitability, potentially widening credit spreads as investors seek greater compensation for increased risk. However, Harris's dedicated support for sustainability and green energy initiatives could benefit the ESG bond market, with government incentives likely spurring increased issuance of green bonds and narrowing spreads in sectors aligned with environmental priorities.

In contrast, Trump's administration would likely focus on tax cuts and deregulation, which could enhance profitability in industries such as energy, manufacturing, and defense, tightening credit spreads in those sectors. However, Trump's trade policies, including broad tariffs, could drive up costs for multinational corporations, especially in technology and industrial sectors, potentially widening spreads due to increased costs. Furthermore, inflationary pressures could elevate borrowing costs, creating more volatility in the corporate bond market, particularly for high-yield issuers.

The US high-yield spread - the most at risk?



Source: Bloomberg

Emerging Market Bonds: dollar strength and trade relations

Emerging market bonds are overly sensitive to U.S. monetary policy and the strength of the U.S. dollar, making the Fed's rate cuts and the election's influence on trade policy pivotal.

A Trump-run office, with its focus on aggressive trade tariffs and fiscal expansion, could result in a stronger U.S. dollar, creating challenges for emerging markets. A stronger dollar would raise the cost of servicing dollar-denominated debt for these countries, leading to wider sovereign spreads and weaker currencies, particularly in nations dependent on U.S. trade, such as Mexico. Tariff-related disruptions could also exacerbate bond market volatility in these regions.

On the other hand, Harris is expected to pursue more moderate trade policies, likely leading to a weaker dollar, which would ease debt-servicing costs for emerging markets and mitigate capital outflows. Harris's emphasis on multilateral cooperation and stable trade relations could provide a more favourable environment for EM bonds, reducing the volatility that often hurts these markets during periods of global uncertainty.

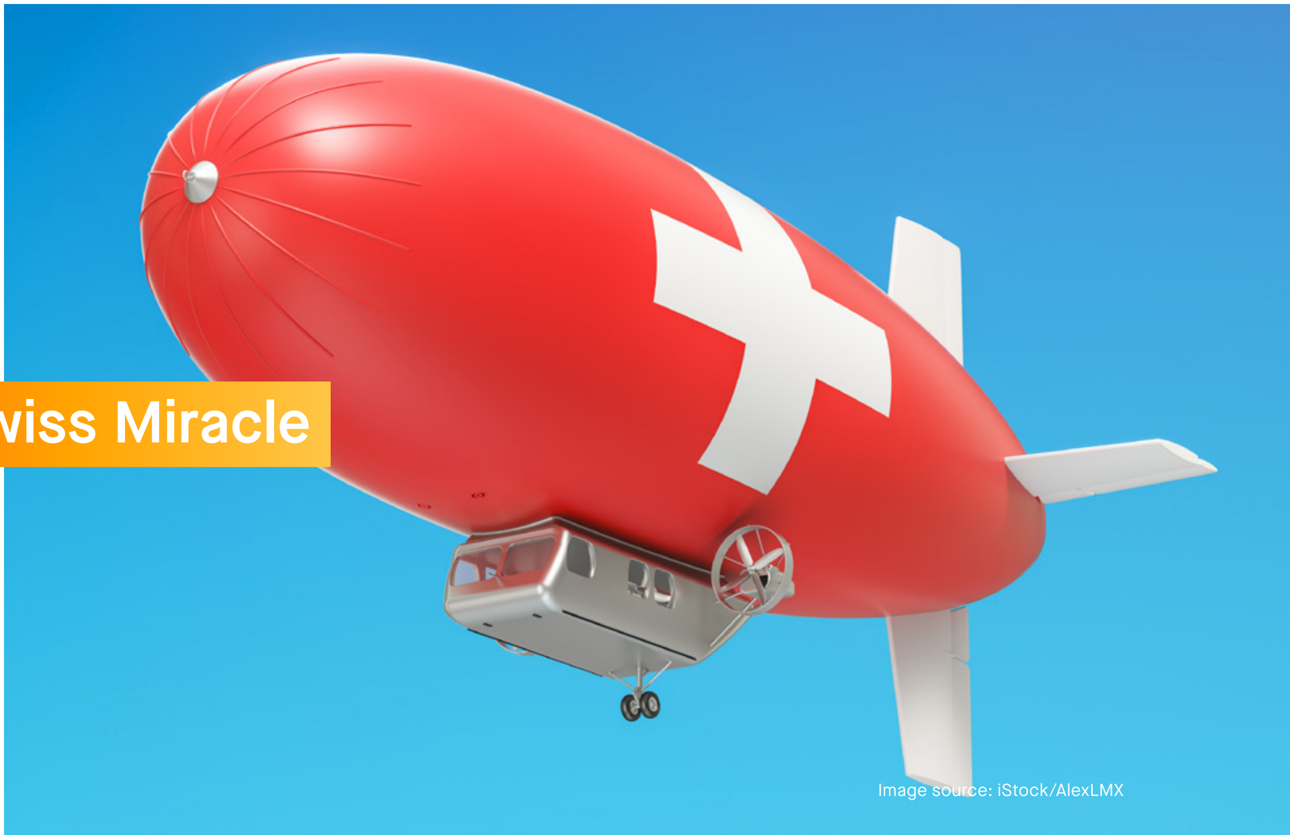


Image source: iStock/AlexLMX

The Swiss Miracle

Despite challenges from a strong currency, Switzerland's economy remains strong, with significant industrial growth driven by specialised sectors. This resilience contrasts with stagnation seen in many neighbouring countries.

Charles-Henry Monchau
Chief Investment Officer

Swiss industry not afraid of the strong franc

In his last appearance before the press as President of the Swiss National Bank, Thomas Jordan warned that the franc is likely to appreciate against the euro, regardless of the SNB's actions. To stay afloat, Swiss exporters will need to continue cutting costs to remain competitive with foreign competitors.

This is hurting the morale of Swiss companies. Over the past few months, Swissmem, the trade association for the machinery, equipment, and metalworking industries, has warned about the negative impact of the CHF's rise on exports. Now, the watchmaking industry is also raising concerns, urging the Swiss National Bank to intervene in its foreign exchange reserves.

Despite this, the figures demonstrate a reality that continues to impress the world: despite globalisation and the franc's continuing appreciation against most currencies, the Swiss economy is holding up. Remember, in the 70s, it took 10 Swiss francs to buy 1 sterling, and 4.5 francs to buy 1 US dollar. In fact, as the graph below shows, Swiss industrial production has grown by almost 40% since 2011, despite the franc's 25% appreciation against the euro. Have our neighbouring countries benefited from the euro's depreciation? Not at all. In fact, industrial production has hardly grown in 15 years. In Germany, it has even declined since 2011. The contrast with Switzerland is striking.

Industrial Production
(Index rebased to 100 on January 1, 2011)

Source: Factset, Banque Syz

What accounts for Switzerland's outperformance of the Eurozone?

In simple terms, this divergence can be explained mainly by the presence in Switzerland of a few important sectors with very high added value, which still stand out from the competition from emerging economies. These include pharmaceuticals, watchmaking, and chemicals.

Despite the 39.6% aggregate increase in Swiss industrial production since 2011, many sectors have seen their output decline over this period, due to the loss of market share to more competitive emerging producers. For example, production fell in the textile (-27%), electrical equipment (-11%), metal products (-12%) and machinery (-16%) sectors.

However, the three aforementioned high-value sectors recorded strong production increases over the period, pulling up the Confederation's industrial output: pharmaceuticals (+189%), watchmaking (+37%) and chemicals (+67%).

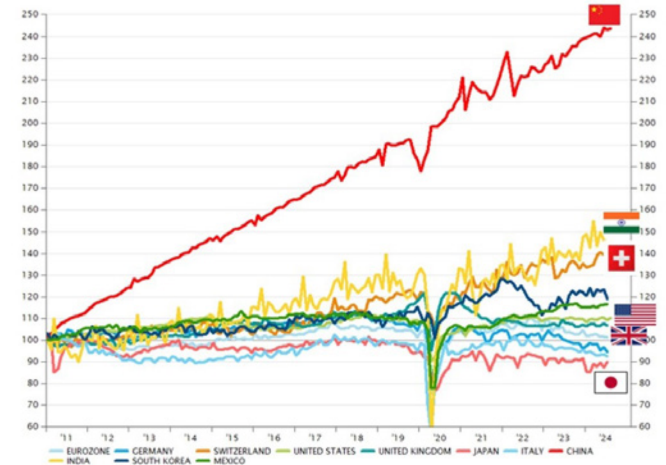
Swiss industry is being driven upwards by these three sectors, whereas industry in the Eurozone has not been able to rely in the same way on less competitive, high-value-added sectors of excellence.

In the Eurozone, particularly in Germany and Italy, the currency union's two main industries, growing competition from emerging producers has caused industrial production to stagnate or even decline since 2011.

Switzerland versus the rest of the world

To broaden the debate and perspective, here's the same chart on industrial production (base 100 on 01.01.2011) including all major economies.

Industrial Production
(Index rebased to 100 on January 1, 2011)



Source: Factset, Banque Syz

It is important to note the following:

- Unsurprisingly, China has experienced the strongest growth in industrial production, although the rate of increase has slowed in recent years.
- The USA and the UK have recently seen industrial production return to pre-Covid-19 levels. However, growth over the last 15 years has been weak, barely better than the downward trend in Europe.
- Some emerging economies have performed well (e.g. India, Mexico), particularly in recent years thanks to the phenomenon of "friendshoring" and "nearshoring". South Korea's performance in recent years has been more mixed.

The de-industrialisation trend in developed economies is clear, especially in Europe and the United States. The efforts to "reindustrialise" (like Trump and even Harris plan in the USA, or the Draghi report in Europe) will require major investments and significant policy changes.

China is no longer "the world's only workshop", even if it remains the largest one, with over 30% of the world's industrial output is produced in China. India, buoyed by its domestic growth and the opening of its economy to trade, and Mexico, which benefits from American reshoring and friendshoring, are experiencing strong growth in their industrial sectors.

Switzerland is a remarkable exception, with its highly specialised, high value-added sectors enabling it to maintain its industrial base despite the decline in the production of lower value-added goods, which are suffering from growing competition from emerging countries.

The rise of stablecoins

Image source: iStock/Funtap

In recent years, the rise of stablecoins has strongly transformed the landscape of digital finance, with over $170 billion of these digital assets now held globally, according to CoinGecko.

Charles-Henry Monchau
Chief Investment Officer

Hashim Almadani
Intern

Unlike traditional cryptocurrencies such as Bitcoin and Ethereum, which are often criticised for their price volatility, stablecoins are designed to keep a steadier value by being pegged to reserve assets such as the US dollar or gold. This stability makes stablecoins increasingly appealing to both everyday investors and large institutions, creating a bridge between traditional finance and the fast-evolving world of digital assets.

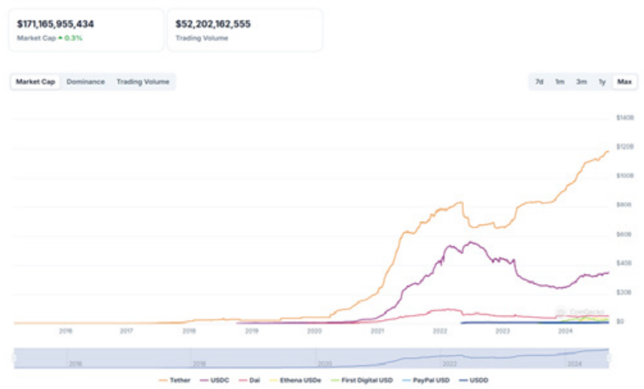
The idea of a stable digital currency echoes the vision expressed by economist Friedrich Hayek in his 1976 work, The Denationalization of Money. Hayek proposed that a competitive market of private currencies, each backed by various assets, could promote a more stable and efficient monetary system than one controlled by governments. While Bitcoin represents a significant move towards Hayek's ideal of a decentralised currency free from central authority, its volatility undermines its utility as a stable medium of exchange.

In contrast, stablecoins aim to realise Hayek's vision by merging the stability of traditional currencies with the cutting-edge capabilities of blockchain technology. By offering a reliable store of value and a practical medium of exchange for everyday transactions, stablecoins address the volatility issues that have been one of the main criticisms of other cryptocurrencies. This intersection of traditional finance and digital technology has not only attracted interest from governments, businesses, and individual users but also set the stage for a new era of financial interaction. As stablecoins continue to evolve and gain traction, they are set to play a pivotal role in reshaping how we think about and engage with money in the digital age.

The evolution of stablecoins

The mechanics behind stablecoins are diverse, reflecting the different approaches to achieving price stability. The most common type is fiat-collateralised stablecoins, which are backed by reserves of fiat currency held in a bank. For example, Tether (USDT), the most widely used stablecoin, is pegged to the US dollar and claims to be backed by a reserve of assets equal in value to the amount of USDT in circulation. Tether's market dominance, with a market share of 69% of the total market capitalisation of all stablecoins according to Forbes, underscores the demand for a stable, dollar-pegged cryptocurrency.

Main stablecoins - Market cap over time



Source: CoinGecko

Another significant player in the stablecoin market is USD Coin (USDC). Issued by the Centre Consortium, which includes companies like Circle and Coinbase, USDC is also pegged to the US dollar and is fully backed by dollar reserves. Unlike Tether, USDC undergoes regular audits by independent accounting firms, providing an additional layer of trust for users. This transparency has made USDC a preferred choice for institutional investors and businesses looking to leverage stablecoins for everyday transactions, cross-border payments and DeFi applications, (as underlined by the increase of USDC market capitalisation growth of around 32% since September of 2023.

The algorithmic stablecoin is another innovative approach within this space. Unlike fiat-collateralised stablecoins, algorithmic stablecoins maintain their peg through algorithms that automatically adjust the supply of the token in response to market demand. TerraUSD (UST), which was one of the most prominent algorithmic stablecoins, maintained its peg by incentivising users to either mint or burn tokens based on the market price. Although TerraUSD ultimately failed in maintaining its peg, leading to its collapse in 2022, the concept of algorithmic stablecoins remains a key area of interest and experimentation within the blockchain community. The failure of TerraUSD also highlighted the risks associated with algorithmic models, particularly in how they respond under stress conditions, prompting more rigorous debate and innovation in the sector.

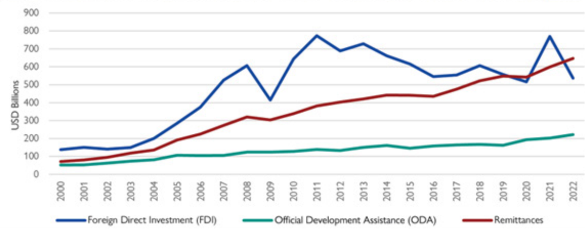
Beyond these examples, the stablecoin landscape continues to evolve, with a range of new models and innovations being introduced. Hybrid stablecoins, which mix elements from both fiat-collateralised and algorithmic approaches, are gaining attention for their potential to balance decentralisation with stability. This exploration of hybrid models is part of a broader trend where multi-collateralised stablecoins, backed by a diverse range of assets instead of just one, are being developed to spread risk and enhance resilience against market fluctuations. By using a variety of assets such as different fiat currencies, commodities, and cryptocurrencies, these stablecoins aim to minimise the impact of volatility in any single asset, providing greater stability and reducing the likelihood of significant value swings. Such innovations address the limitations of previous models by offering improved protection against economic shocks and contributing to overall stability.

These ongoing developments highlight that the stablecoin market is far from static. Developers and financial engineers are continually refining these digital assets to improve their resilience, efficiency, and broader adoption. As stablecoins gain in popularity, their integration into the mainstream financial system is becoming more pronounced, marking their increasing importance in both everyday transactions and complex financial applications. This dynamic evolution underscores the growing sophistication and centrality of stablecoins within the cryptocurrency ecosystem.

Financial inclusion and emerging markets

Financial inclusion, the effort to make financial services affordable and accessible to all, remains a pressing challenge in many emerging economies. According to the World Bank, one of the main obstacles is the high cost of banking services, driven by limited competition and the dominance of a few large institutions. Moreover, changing regulations around cross-border transactions have made it harder for banks to maintain remittance service partnerships. As the Bank for International Settlements (BIS) reports, the number of correspondent banks fell by 25% between 2011 and 2020, further reducing access to the global financial system. This has led to increased costs and frictions in cross-border payments, painting a crucial issue, as remittances often play a more significant role in these economies than development assistance.

Faced with these barriers, many individuals and businesses are seeking alternative and stablecoins offer a promising solution. By providing a more efficient, cost-effective, and stable means of transferring money, stablecoins can help bridge the gap left by traditional banking systems. In doing so, they offer a pathway to greater financial inclusion, broader access to essential services, and the potential for economic growth and stability in emerging markets.



Source: World Migration Report

Center bank digital currency

While private stablecoins have led the charge in the digital currency revolution, central banks around the world are not standing passively by. The rise of stablecoins has caused many central banks to explore the development of Central Bank Digital Currencies (CBDCs), which represent a digital form of a country's sovereign currency. Unlike private stablecoins, which are typically issued by corporations or decentralised organisations, CBDCs would be issued directly by central banks, giving them the full backing and credibility of the government, just as their respective fiat currency. This has important implications for the global financial system, as CBDCs could fundamentally alter the way money is issued, transferred, and managed.

China has been the most proactive in this regard, with its digital yuan, known as the e-CNY, already in advanced stages of development and testing. The People's Bank of China (PBOC) has conducted extensive trials across multiple cities, with millions of yuan in digital currency distributed to citizens and businesses. The digital yuan is designed to work seamlessly with existing financial infrastructure while also enabling direct peer-to-peer transactions without the need for intermediaries. This could significantly reduce transaction costs and increase the efficiency of payments, particularly in a country like China, where mobile payments are already deeply integrated into daily life.

The implications of the digital yuan extend beyond China's borders. If widely adopted, the e-CNY could challenge the dominance of the US dollar in international trade and finance, particularly in regions where China has strong economic ties, such as Africa and Southeast Asia. The digital yuan could also provide a way for countries to bypass the SWIFT system, which is currently dominated by the US, thereby reducing their exposure to US financial sanctions. This geopolitical dimension of CBDCs adds an additional layer of complexity to their development and adoption, as they could become tools of economic influence in the hands of states.

In Europe, the European Central Bank (ECB) is also exploring the issuance of a digital euro. The ECB has launched a two-year investigation phase to assess the feasibility and implications of a digital euro, which would be designed to complement, and not replace existing cash. The digital euro aims to provide a secure and efficient means of payment within the Eurozone, particularly in a digital economy that is increasingly driven by online commerce and mobile payments. The ECB is also considering how the digital euro could enhance financial inclusion, by providing easy access to digital payments for citizens who do not have bank accounts.

The United States, meanwhile, is taking a more cautious approach. The Federal Reserve has published several discussion papers exploring the potential benefits and risks of a digital dollar but has not yet committed to issuing one. The key concerns include the impact on the banking system, as a digital dollar could potentially reduce the demand for bank deposits, which are a primary source of funding for commercial banks. With the election approaching, there are divergent thought between both candidates, with Trump promising to never allow the creation of such currency, whereas ex-candidate President Biden was a strong believer in the benefits of a US-CBDC during his re-election campaign.

However, CBDCs also raise concerns about privacy and surveillance, as governments could theoretically track every transaction made with digital currency. Additionally, the implementation of CBDCs could disrupt traditional banking systems, potentially reducing the demand for commercial bank deposits and altering the way financial institutions operate. This shift could lead to broader economic implications, such as changes in credit availability and interest rates, creating a need for careful consideration of how these digital currencies are integrated into the existing financial landscape.

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