April 2024

Market overview and positioning

Equity markets were in the spotlight in the first quarter. Headwinds picked up a little towards the end. But despite some evidence of weakening, the economic data coming from the US has remained encouraging in recent weeks. Here in Europe, a process of normalisation is apparent. We therefore expect the growth environment to remain constructive with declining rates of inflation.

US economy loses some of its momentum

In the US, the key growth indicators weakened slightly in March following a largely stable period of development. The latest data suggests that the US economy is enjoying less momentum as it moves into the second quarter. From a sectoral perspective, we discern ongoing weakness in the services sector and a negative trend in manufacturing. Inflation is having an impact on both sectors: industrial companies are feeling the effects of higher commodity prices, while service providers are confronted by higher wage costs, among other things.

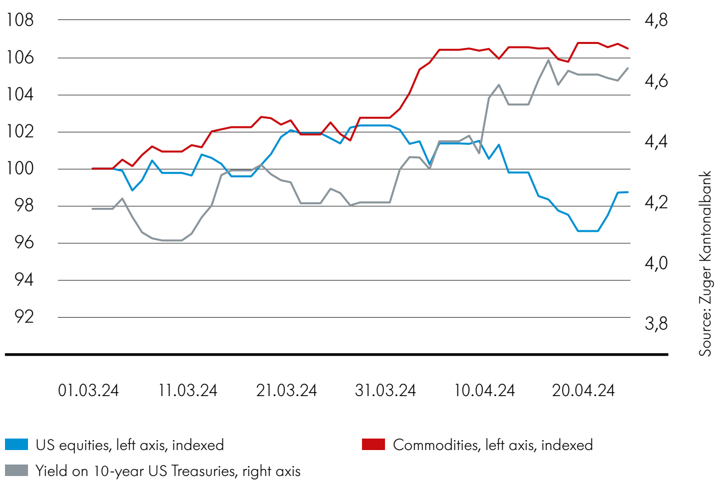
Soft landing likely

The current growth rate of gross domestic product (GDP) confirms the weaker trend: the US economy recorded nominal GDP growth of 1.6% in the first quarter. However, real growth data continues to point to a “soft landing” scenario. Both government and private spending are supporting economic development. Consumers remain happy to open their wallets. The labour market continues to be stable. The high number of immigrants has boosted the size of the working population and brought equilibrium to wage growth.

Inflation proving stubborn

The combination of higher commodity prices and rising interest rates triggered price falls in equity markets (see chart). These were the result of a negative surprise in inflationary developments in recent weeks, with a renewed surge evident. In our view, the latest data is exaggerating the true inflation trend, among other things due to effects in the area of rental price development. We are therefore expecting the uptrend in inflation to weaken somewhat over the next few quarters. Thus we expect declining rates of inflation, a robust but less tight labour market and rising real incomes to support the performance of high-risk investments.

Development of US equities, US interest rates, and commodities



Fewer interest rate steps than originally expected

The eyes of the financial markets have been firmly set on central banks, particularly the Fed. The assessments of members of the Federal Open Markets Committee (FOMC) point to a fall in interest rates in 2024. While these remain factored into market expectations, the number of expected key rate cuts has been scaled back markedly in recent months: At the start of the year no less than seven cuts were anticipated, whereas now the market is expecting two at most.

Market overview and positioning

Lower key interest rates on the horizon
Declining rates of inflation and gradually weakening economic indicators support our prediction that US interest rates have peaked. We are expecting rate cuts across the board over the course of 2024. Where the Eurozone is concerned, the latest developments on the inflation front point to the European Central Bank (ECB) cutting rates before the Fed.

Hope for Europe's economy
Europe's economy is growing at a below-average rate, but an upward trend is now evident. Following five successive quarters in which virtually no growth has been apparent, the silver lining on the horizon is becoming ever clearer. The leading economic indicators have now risen above the growth threshold for the first time since October 2023. Thanks to sharply declining rates of inflation, the ECB can be expected to cut interest rates in the summer. This should provide another boost to the economy.

Germany livens
Evidence of the stabilisation of the economy is apparent in many European countries. The picture in Germany is more nuanced. The key ifo Business Climate Index, which evaluates the sentiment of German companies, improved for the third month in a row in April. Companies are doing brisker business and forecasts are becoming more bullish. This raises hopes of slightly stronger overall growth, driven primarily by consumer spending. German households have yet to work through all of the surplus savings built up during the coronavirus pandemic. By contrast, the construction sector remains beset by difficulties, and this is keenly felt due to its importance to the overall economy.

Switzerland still strong
In Switzerland, inflation surprised on the positive side – in February it stood at 1.2%. This was well within the target bandwidth (0 to 2.0%) of the Swiss National Bank (SNB), which was therefore able to reduce its key interest rate by 0.25 percentage points to 1.5% in March. The strong franc has mitigated any inflation imported through higher commodity prices. The leading indicators are already pointing to a trend reversal, with the Leading Indicator of the Swiss Institute for Business Cycle Research (KOF) at ETH Zurich having stabilised at around its long-term average.

Franc weakens
The recent rate cut by the SNB has removed some of the upward pressure on the Swiss franc. The US dollar has bounced back, supported by higher capital market interest rates in the US. The euro too has gained a little ground. This is a positive development for export-oriented Swiss companies, as is the Eurozone's improved economic trend. The sales and earnings forecasts of companies have improved accordingly.

"The US looks to be headed for a soft landing. In Europe, the signs of economic stabilisation are very clear. The focus remains on higher-risk investments."

Alex Müller, Chief Investment Officer

The potency of geopolitical developments
The world's major conflicts seem to have almost passed the financial markets by. In view of the US having just approved a USD $61 billion package of armaments deliveries to Ukraine, investors appear to be unruffled by the risk of further Russian advances. In the Middle East, Iran's retaliatory attack on Israel proved ineffective against the efficient defences. Although this attack had been pre-announced, the defensive strength of the Israeli armed forces and its allies was nonetheless impressive.

That said, the situation remains critical. Escalation would not be in the interests of the US, Israel, Iran or the countries of the Arab world, yet the threat of "wildfire contagion" has not gone away. The indirect effects of a possible escalation – above all in the form of higher commodity prices – remain under scrutiny.

What does this mean for investors?

US remains attractive

We have slightly increased our overweighting of US equities. The US stock market is likely to remain popular with investors, even though it doesn't look cheap. Earnings expectations are ambitious in the technology sector in particular. The upcoming reporting season is likely to be another key litmus test. Tech companies will have to impress analysts with their sales and earnings figures over the next few quarters too. Some have already done just that. In our view, the strength of the US economy and the boom surrounding AI justify the valuation premium for the time being. For this reason, we increased our exposure to US equities further in March.

Positive momentum

Given expectations of a soft landing for the US economy, both equities and high-yield bonds have appeal. The latter allow investors to benefit from high current yields and stable credit spreads. As things stand, we are less keen on international government bonds, specifically those of the US government. We have reduced our positions here further, but remain convinced of their utility as an instrument of diversification.

Weak stimulus from domestic market

Despite its positive performance over the year to date, the Swiss equity market has lagged behind its European and American counterparts. This is first and foremost attributable to the defensive heavyweights such as Nestlé and Roche, which have failed to impress with their recent figures and outlooks. Nevertheless, the backdrop looks solid for Swiss equities in the second half of 2024. The leading economic indicators have improved steadily in recent months. Also on the rise are the sales and earnings forecasts of Swiss companies. This is in keeping with the positive outlooks of many companies for the second half of 2024 as well as the 2025 financial year. As an additional factor, the Swiss equity market looks to be modestly valued, which bodes well for the next few months.

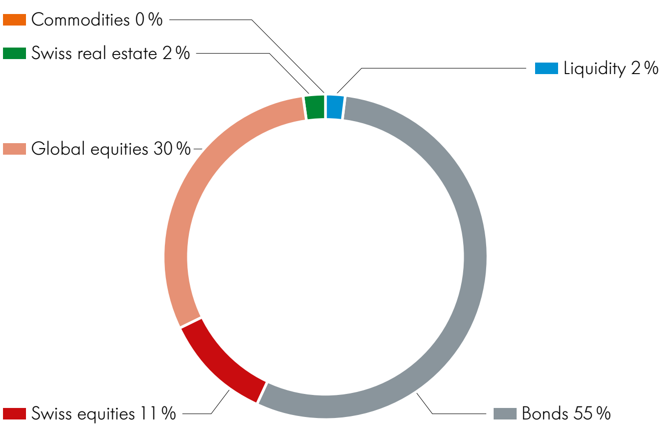
Europe picks up

We are now recommending a neutral weighting of European equities. The economic headwinds faced by the Eurozone have abated further. While growth has stagnated here for the last five quarters, the leading indicators point to brighter days ahead: industrial activity is picking up again, and both the closely-watched ZEW Indicator and the ifo Index have risen. Meanwhile, consumer confidence and real wages are rising. Inflation rates are receding and the savings ratio is likely to decline.

Less exposure to real estate

Swiss real estate funds have appreciated in value against a backdrop of declining capital market interest rates. Given the current level of interest rates, their valuations are fair to slightly elevated. We have therefore reduced our exposure by taking profits, and are now neutrally weighted. European equities look to us to have greater return potential.

Strategic positioning (based on balanced mandate)

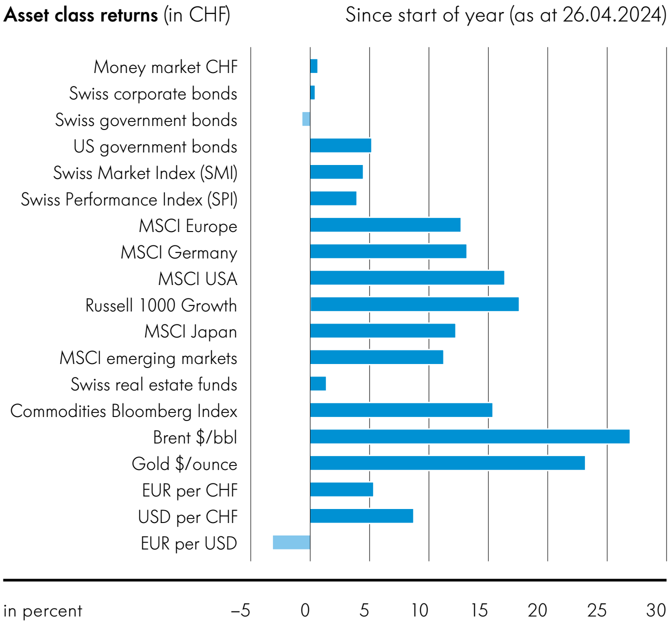


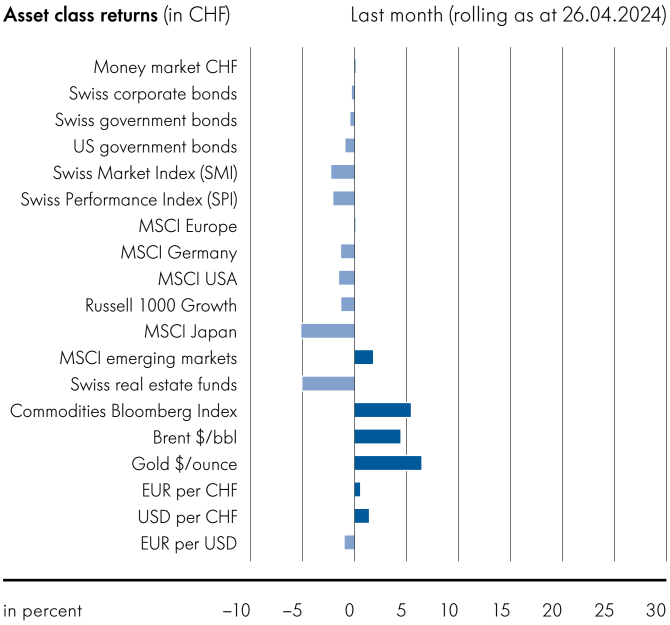
Quelle: Zuger Kantonalbank

Tactical positioning

	−−	−	=	+	++
Liquidity/money market		X			
Bonds			X		
Swiss bonds			X		
Global Bonds		X			
High-yield bonds and emerging markets			X		
Equities				X	
Swiss equities			X		
Global equities ex Switzerland				X	
Emerging markets equities			X		
Swiss real estate			X		
Commodities			X		

Market data (exchanges & markets)





Source: Zuger Kantonalbank, Bloomberg L.P., MSCI, Six Index, Frank Russell Company

Swiss equities SMI (from start of the year to 26.04.2024)

Lonza 49.2% / CHF 527.8	**ABB** 23% / CHF 44.94	**Holcim** 19.8% / CHF 79.1	**Givaudan** 15.6% / CHF 3962	**Richemont** 12.2% / CHF 129.85
Swiss Re 11.7% / CHF 99.5	**Alcon** 9.7% / CHF 72	**Novartis** 9.4% / CHF 89.5	**Zurich** 5.9% / CHF 439.9	**Swiss Life** 5.8% / CHF 617.8
Swisscom 3.9% / CHF 505	**Partners Group** –1.5% / CHF 1195	**Nestlé** –1.8% / CHF 92.7	**Sika** –2.3% / CHF 264.2	**UBS** –4% / CHF 25.06
Geberit –5.7% / CHF 495.5	**Roche** –5.9% / CHF 221	**Sonova** –6.3% / CHF 257	**Logitech** –8.9% / CHF 72.66	**Kühne&Nagel** –16.2% / CHF 242.8

Source: SIX Index, Zuger Kantonalbank

Do you have any questions or thoughts on the current portfolio?

Contact us by email (alex.mueller@zugerkb.ch) or call us on 041 709 11 11.