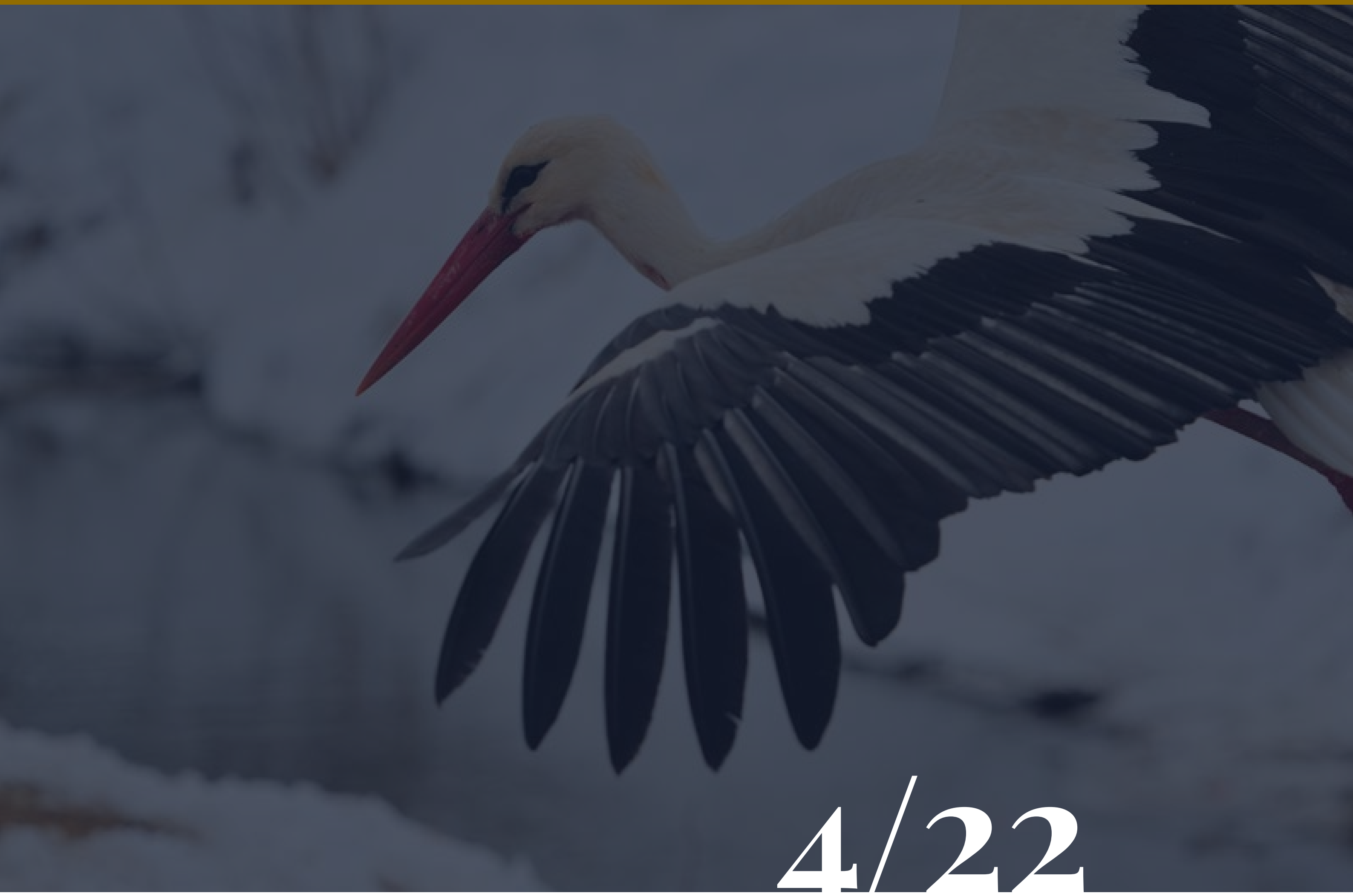
Investmenttrends 4th quarter 2022



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Market outlook from ONE Asset Management AG

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Investmenttrends 4th quarter 2022

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ONE® Asset Management

01/ Equities

The energy crisis and the war of aggression in Ukraine, as well as rampant inflation and the sometimes panicky measures taken by central banks, will continue to keep the global capital markets on tenterhooks in the fourth quarter. Uncertainty remains high. This is basically poison for the stock markets, but bonds have not been able to calm down either.

As a result, the picture on Wall Street in the U.S. and the other stock markets in tow remains critical. For example, analysts at Goldman Sachs recently turned around in the face of an even steeper-than-expected path of interest rate hikes and abandoned their optimistic scenario for the S&P 500. They cut their year-end target for the market-wide US index from 4300 to 3600 points. Growth as well as earnings and valuation expectations would be negatively affected. Many stockbrokers now expected a „hard landing“ of the United States.

In the DAX, a fresh sell signal was given, half of the steep rise from the Corona low to the record high 2021 has been corrected. This level at 12273 points is of great importance from a technical point of view. If it is sustainably undercut, 11325 points come into view according to the Fibonacci theory. Here, only 38.2% of the rise would be left as the next correction level. The chart picture for the standard stocks would only become sustainably positive again at 14000 points.

A premature grip in the falling knife is therefore not advisable in the width. The recovery movements appear too fragile so far. Even if it will come, as usual in the bear market, again and again to fast and violent reactions. Liquidity remains low in the uncertain environment, which increases volatility. Investments should therefore be made very consciously and selectively. The right „stock picking“ is of particular importance in a tense market.

Meanwhile, some investors are betting on a possible ceasefire in Ukraine in the coming months. This would remove a major factor of uncertainty from the markets. If peace can be restored, the capital markets should at any rate celebrate this with a significant recovery for the time being. However, the fact that the crisis has left behind broken pieces that have not been swept up could be irritating at second glance. If, on the other hand, the crisis worsens, the downward slide would be open.

Even Chancellor Scholz calls Putin‘s partial mobilization an „act of desperation“. The move should at least be seen as a rebellion and could herald a final phase. In addition, there will hopefully be empty threats to use nuclear weapons. How Putin‘s support at home will develop further will also be an exciting question for the coming months.

In addition to the uncertainty caused by the war, however, its far-reaching effects are also weighing on equities. The energy crisis in particular, but also the pressure on production costs and the availability of input factors in general, are even threatening the existence of some companies. The clearest example is the state bailout of Uniper, which had completely lost its footing.

Added to this is the central bank policy with its ultimately abrupt switch to a restrictive monetary policy after so many years of seemingly endless capital glut. Now, monetary guardians around the world are trying to recapture the out-of-control price increases. The Riksbank, for example, has raised the bar again with a 1% increase in the key interest rate. For the Swedes, this was the highest rate of increase since the central bank used an inflation target in 1995. The Federal Reserve, the pace-setter, has not yet taken this extreme step. It currently stuck to 75 basis point increments, as did the Swiss SNB and other central banks recently.

Accordingly, the fourth quarter will remain turbulent. The negative factors are not new, but they remain massive. The Corona pandemic, which had already shaken up the capital markets and left the economy battered, seems to have been almost forgotten. The stock markets were helped by the renewed flood of liquidity to heal the wounds. This time, however, it failed to materialize because of the almost galloping inflation, and that makes the market‘s prospects for the upside more difficult.

Although the bear market is fully intact, it is already extended in terms of time compared to historical levels. The extremely negative sentiment has already led to significant valuation discounts on many selected stocks that appear worth holding for longer-term investments in order not to miss a surprising recovery. How fast and strong this can start, could be seen in the interim recovery in the S&P 500 in the second quarter, which was completely sold off again also due to the again significantly tightened monetary policy.

02/ Bonds

The pace of the central banks‘ interest rate hike race remains high. In view of sustained inflation, there is now apparently a lot of excitement among monetary guardians after years of careless liquidity glut. Unlimited operation of the printing press triggers inflation. Truly, this should not have come as a surprise. In any case, in the wake of the Federal Reserve, interest rate hike mania and inflation panic are sweeping the globe. Central banks are responding in textbook fashion by turning the interest rate screw sharply - with the exception of Japan.

In the USA, the interest rate trend remains correspondingly clear. 10-year interest rates are higher than at any time since April 2010. But the rise at the short end is even more violent. Two-year notes are yielding 4.2%, the highest since 15 years ago. The yield curve thus remains inverted. This is often seen as a harbinger of recession. But the U.S. monetary authorities do not seem to fear a cooling of the economy at all. On the contrary, they are uncompromisingly putting the fight against inflation above everything else. The Fed may still be hoping to achieve a soft landing for the economy, but it would obviously not regard a recession as a serious blow.

It almost seems as if a recession is seen as the last resort in the fight against inflation. The Fed, and with it the markets, are watching price developments like a rabbit in front of the snake. Thus, the inflation data from the U.S. with the labor market figures remain the sticking point. The jobs report is also in the eye because of the particularly tight labor market. Whether a turning point in the data has already been reached or can be reached in the short term remains doubtful so far. Leading indicators also point to a mildly recessionary U.S. economy in early 2023, with the strongest negative impact coming from the housing market, which raises eyebrows after previous crises.

The Fed has announced at least another 0.75% rate hike by the end of the year, more likely 100 to 125 basis points. Overall, the hawks at the Fed are keeping a secure grip on the rudder and gaining even more strength. Stubbornly high inflation and a very tight labor market are their restrictive argument. However, the extent to which monetary policy can combat inflation driven by disruptions in international supply chains remains an open question.

Europe is moving into recession, which probably began in the third quarter. The Eurozone Purchasing Managers‘ Index shows this relentlessly. This is because expensive energy, as well as sharply increased prices for other input costs on the production side, as well as declining consumer spending due to inflation, are strangling the economy. Thus, the data in Europe remains very much in a minor mood.

In addition, political developments in Italy will be exciting. How will the election of Giorgia Meloni as prime minister be digested, even in the overall European context. First of all, this is a major jolt to the right, which could continue to set a precedent in other countries. Economically, the Italian budget is expected to be severely strained. The deficit is likely to be pushed above 6%. Even though this could bring a short-term economic boost and relief, strong pressure on Italian bonds is to be expected overall. This, in turn, will call the ECB into action with its expanded toolbox.

03/ Currencies

Even after falling back to parity with the dollar, the euro was unable to stop its downward trend. After the Fed‘s latest interest rate meeting, the common currency fell to its lowest level in two decades. The European Central Bank also awoke from its slumber with an interest rate hike. It now wants to really step on the gas with its inflation containment efforts. Even the white dove Lagarde has suddenly mutated into a hawk. She was quoted as saying that she would consider raising key interest rates even above their neutral level. The European monetary guardians would have to act much more hawkish and be more decisive to give the euro strength against the trend. The now clear inversion of the U.S. yield curve also plays a role here, because it usually occurs at the end of a cycle and is accompanied by a strong currency.

The Bank of England‘s key interest rate of 2.25% is at a high since 2008. On the other hand, in the current environment, an interest rate hike of „only“ 0.5% can already be considered a dovish signal to the capital markets. After all, compared to the Fed and the ECB, the British have exercised restraint. Overall, it may even have marked an extreme point in its restrictive policy. Declining inflation expectations of households in the medium term and also weak retail data help the monetary guardians.

Due to the ambiguous political and monetary policy measures, visibility for the pound is limited. Technically, the currency is in a clear downtrend against the dollar. A reversal is not to be expected from this perspective, but also in view of the fundamentals. This is also indicated by the current shocks in the pound-currency structure.

The yen has been on a breathtaking slide, heavily impressed by the BoJ‘s „stubborn“ stance. Meanwhile, 10-year U.S. paper yields about 3.3% more than JGBs. A year ago, this premium was less than 1.5%. Accordingly, the yen continues to be sold by large speculators in a bet against the central bank, which is expected to fall at some point. This is a vicious circle for the monetary guardians, because the weakness of their own currency drives up inflation, which in turn should make the ongoing expansionary monetary policy unsustainable. Currently, central banks are trying to calm the situation with interventions in favor of the yen, after the Japanese currency was pushed above 145 yen to the dollar to its weakest level since 1998. Whether the measures will have an effect remains to be seen. Technically and also fundamentally, the yen is likely to remain rather weak in the coming months, in our view.

04/ Commodities

Crude oil prices have made a sharp turnaround in recent months. They look vulnerable for the new quarter, and the likely direction is rather further down. On the one hand, the economic slowdown to the point of recession fears in the major world economies - is weighing on the demand side among the largest oil consumers.

So far, this has not been offset by a production cut by OPEC countries. The cut has so far been rather symbolic, albeit contrary to the increased production levels of previous months. Russia also remains a factor of uncertainty in terms of oil supply. The price cap for Russian crude oil has a negative effect in the short term, but in the longer term it could also prove to be a bullish factor via shifts in supply and demand.

Hovering over everything, however, are recession worries, which are ruining recovery attempts in the current downtrend. Shrinking economies as early as in the new quarter will keep the pressure foreseeably high. This is because demand is more likely to collapse. If one looks at the current situation in a historical context, one is inevitably reminded of 2008. In the financial crisis at that time, investors who had been caught on the wrong foot by the drop in asset prices withdrew their money from commodities to plug the holes. The economic problems, especially in the banking world, spilled over. The economy was crippled, dragging down its fuel, oil.

At that time, too, the most important producing countries had cut their production, but were unable to stop the drop in prices. Due to the recession in the industrialized countries, demand had collapsed more quickly, and the oil in storage was not being called up. The price drop suggests a similar constellation. The chart also points to rather further falling prices in the new quarter.

Gold is also suffering from declining demand and overall reduced interest. The biggest evil for the yellow metal, however, is King Dollar. The increasingly strong U.S. currency is putting pressure on the dollar-denominated precious metal. The strong dollar is effectively devaluing gold. Since the dollar has not yet shown any signs of reversing its trend, the outlook remains gloomy. The supposedly good chances of an upward breakout of the gold price are gone. The downside remains in focus.

Thus, the price prospects for the two commodities but also in the whole complex currently remain limited. In the intact downtrend, no sustainable support can be expected for oil prices so far. The gold price is moving on an important support, which should not be undercut. Overall, the entire commodity complex could rather suffer further in the new quarter under the impression of economic fear and the unbroken strong dollar.

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