PostFinance investment compass March 2022

PostFinance

Editorial

A less secure world

The war in Ukraine is a reminder that barely conceivable events can actually occur. But part of life is preparing for the future, despite all the uncertainty.

Daniel Mewes
Chief Investment Officer

I can still vividly recall seeing a black swan for the first time in my life when I was at a nature park. It was a surreal sight. The combination of colour and animal is so remarkable that you can barely believe your eyes.

Sometimes momentous events also seem surreal. The images of the Ukraine war are leaving people shocked and pensive. Few of us would have anticipated that 2022 would begin with a war in Europe.

"Black swans" represent improbable events

"Black swans" symbolize events that are extremely unlikely or unexpected. It would be foolish to dispute the existence of "black swans". No, events occur that are barely imaginable in this world. Including negative ones: the Ukraine conflict and the tremendous suffering being caused is a current example of that. By definition, such events don't happen when everyone is expecting them to – and even if they do, definitely not in the way that might be expected.

The past two decades in Western Europe have been marked by an enormous degree of planning certainty, thanks to a high level of institutional, economic and political stability. But it's important to remember that the world is still an unpredictable place, where future developments can be predicted only to a certain extent. The coronavirus crisis gave us a reminder of that, and now the Ukraine war is, too. Living means navigating your way through this environment and standing up for social values with conviction.

Dealing with "black swans"

Investment is quite rightly of secondary importance in light of the suffering in Ukraine. But this still raises the question of how investors can deal with "black swans"?

"Black swans" have an impact on the economy and financial markets, often producing a shock. That's also true of the war in Ukraine. The financial markets have been causing concern recently, and not without reason. The sanctions imposed, further energy price rises, the uncertainty over how the conflict will unfold and potential escalation scenarios are creating uncertainty in many different ways.

> "It's almost impossible to focus on the ups and downs of everyday life."

It's almost impossible to focus on the ups and downs of everyday life. But in the portfolios entrusted to us, we've increased protection with a slightly lower equity allocation and by purchasing additional gold. Long-term investors can be sure that "black swans" will repeatedly cause turbulent conditions, but the world goes on, and you're ideally positioned with a well-diversified portfolio.

Positioning

Gold for additional protection

Geopolitical tensions, growing inflationary pressure and signs of an economic slowdown are increasing the downturn risks. We're reducing risk in our portfolio by lowering the equity allocation and purchasing additional gold.

Against a backdrop of the Russian invasion and economic sanctions by the West, energy prices in particular have soared. A barrel of North Sea Brent crude oil was briefly trading at a 14-year high of almost 140 US dollars. This is ramping up the pressure on inflation rates, as energy prices account for a significant share of the average shopping basket. In the USA, housing costs and wage growth are also creating inflationary pressure. As a result, US inflation climbed again slightly to 7.9 percent in February, even before the outbreak of the Ukraine conflict.

But Europe hasn't been spared from rising inflation rates, either. The European Central Bank is now showing concern over high inflation. It announced plans to accelerate the withdrawal from its bond-buying programme and is set to end the purchases in the third quarter.

High inflation rates are a growing cause of concern for the economy. This leaves central banks facing a dilemma. While they actually need to tackle high inflation rates, this is proving difficult in a weaker economic environment. The situation is increasing the risk of not only an inflation spiral, but also an economic slowdown. Due to the increased risks, we're positioning our portfolios more defensively. Rising inflation means interest rates are unlikely to fall. In light of this, we are maintaining our underweighted position in global bonds.

"The situation is not expected to settle down in the near future – neither geopolitically nor in relation to inflation."

Performance of asset classes

Asset class		1M in CHF	YTD [1] in CHF	1M in LCY [2]	YTD [1] in LCY [2]
Currencies	EUR	–3.3%	–1.5%	–3.3%	–1.5%
	USD	0.5%	1.9%	0.5%	1.9%
	JPY	0.4%	1.1%	0.4%	1.1%
Equities	Switzerland	–6.9%	–11.9%	–6.9%	–11.9%
	World	–6.2%	–9.1%	–6.9%	–10.9%
	USA	–5.2%	–9.5%	–5.7%	–11.1%
	Eurozone	–15.9%	–16.5%	–13.0%	–15.2%
	United Kingdom	–8.7%	–2.8%	–5.9%	–1.5%
	Japan	–6.7%	–7.9%	–7.1%	–8.9%
	Emerging markets	–11.3%	–8.6%	–11.7%	–10.3%
Fixed Income	Switzerland	–1.5%	–4.5%	–1.5%	–4.5%
	World	–1.5%	–3.2%	–2.0%	–5.0%
	Emerging markets	–7.4%	–9.8%	–7.9%	–11.5%
Alternative Investments	Swiss real estate	–0.3%	–1.9%	–0.3%	–1.9%
	Gold	9.3%	12.6%	8.8%	10.6%

[1] Year-to-date: Since year start
[2] Local currency

Data as of 10.03.2022
Source: Web Financial Group, MSCI, SIX, Bloomberg Barclays, J.P.Morgan

Reducing risks

This uncertainty is impacting the financial markets. The equity markets have lost significant ground. European equities recorded particularly sharp losses of around 10 percent, while US equity markets have been less severely hit. A similar picture emerged for corporate bonds. The credit spreads on European corporate bonds widened significantly. This shows that the geopolitical and economic tensions have had a clear impact. The situation is not expected to settle down in the near future – neither geopolitically nor in relation to inflation. As a result, the financial markets will remain under pressure. Risk reduction is advisable in this environment, and we have confirmed the reduction in the weighting of European equities that was recently introduced.

Gold for additional protection

Commodities were prominent once again. Energy prices rose, but so too did those of agricultural commodities, such as wheat. The Ukraine conflict and economic sanctions have led to supply chains breaking down and wheat harvests falling victim to the war. A rise in prices is the logical consequence of increasing supply shortages. But this is creating further potential for inflation. Gold is benefiting from this uncertain environment. The precious metal is one of the few asset classes to achieve a positive return since year-opening. It is also currently playing a key role in portfolio diversification. Gold provides protection against inflation and crises. In light of greater risks of economic downturn and inflation, we're providing additional protection by adopting an overweighted position in gold in the portfolios entrusted to us.

Positioning relative to long term strategy: Swiss focus

Asset class		TAA[1] old	TAA[1] new	underweighted[3] ––	–	neutral[3]	+	overweighted[3] ++
Liquidity	**Total**	**9.0%**	**9.0%**					
	CHF	9.0%	9.0%					
Equities	**Total**	**50.0%**	**48.0%**					
	Switzerland	23.0%	23.0%					
	USA	8.0%	8.0%					
	Eurozone	5.0%	3.0%					
	United Kingdom	2.0%	2.0%					
	Japan	4.0%	4.0%					
	Emerging markets	8.0%	8.0%					
Fixed Income	**Total**	**29.0%**	**29.0%**					
	Switzerland	17.0%	17.0%					
	World[2]	6.0%	6.0%					
	Emerging markets[2]	6.0%	6.0%					
Alternative Investments	**Total**	**12.0%**	**14.0%**					
	Swiss real estate	7.0%	7.0%					
	Gold[2]	5.0%	7.0%					

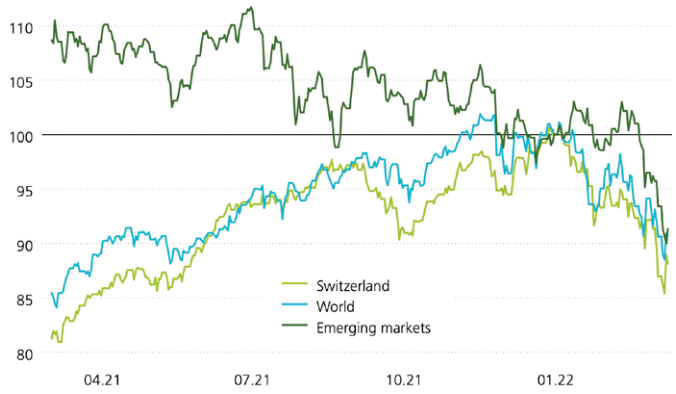
[1] Tactical Asset Allocation: short to mid-term orientation
[2] Currency hedge to CHF
[3] Positioning relative to our long-term asset allocation

— Adjustment compared to last month

Market overview
Equities

The equity markets suffered significant losses last month. Europe was particularly affected by this. By contrast, the energy sector is benefiting from rising energy prices.

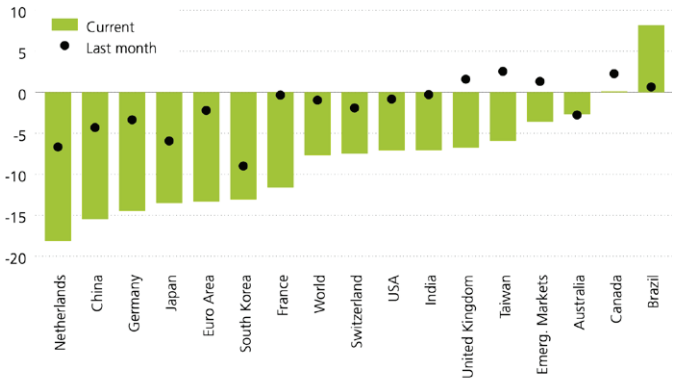
Indexed stock market performance in Swiss francs
100 = 01.01.2022



Prices plummeted on the European stock exchanges after the outbreak of the Ukraine crisis. Losses exceeded 10 percent within a few days. While the Swiss equity market was also hit by this sell-off, it fell much less sharply at 6 percent. The two commodities countries Brazil and Australia were the exception to this negative picture. The energy sector also benefited in other regions. Equity markets are currently much more volatile due to greater uncertainty. In Russia, the central bank temporarily suspended trading in equities.

Source: SIX, MSCI

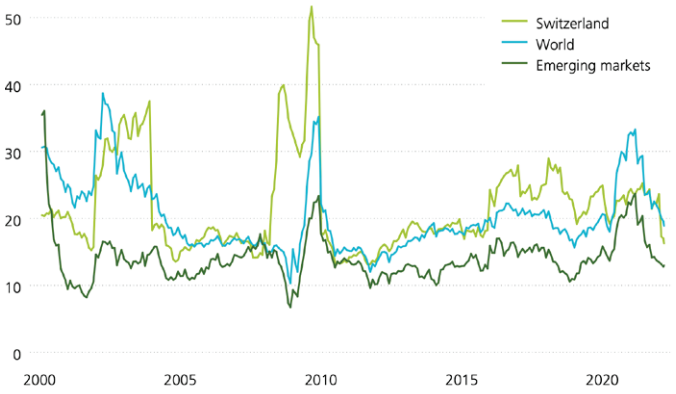
Momentum of individual markets
In percent



The geopolitical risks accelerated the downward trend on the stock exchanges. This was most clearly evident in the European countries, particularly the Netherlands, Germany and France. Brazil was a positive outlier. The Brazilian central bank has further boosted confidence in its currency by pursuing an aggressive interest rate policy. This created a mood of optimism, especially amongst foreign investors.

Source: MSCI

Price/earnings ratio
P/E ratio



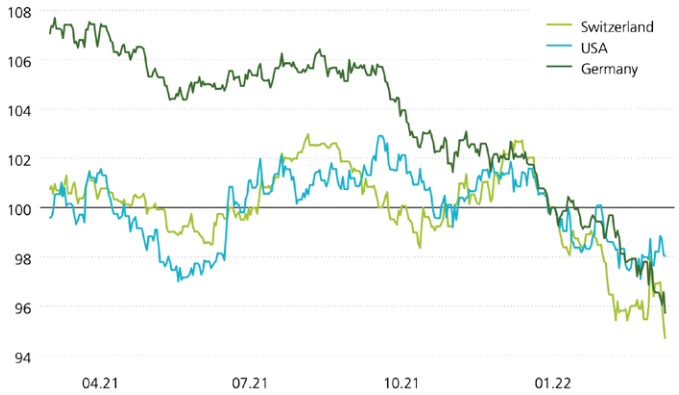
Companies worldwide enjoyed enormous profit growth last year. In the case of France and Brazil, profit levels even doubled. The rise in profits was comparatively low in the final quarter of the year. Measured by the ratio of equity prices to corporate profits, the Swiss and US equity markets are amongst the most expensive in the world, but India is now at the top.

Source: SIX, MSCI

Market overview
Fixed income

The escalation in the Ukraine conflict overshadowed the strong economic situation and inflation concerns last month. Bonds made gains as a result.

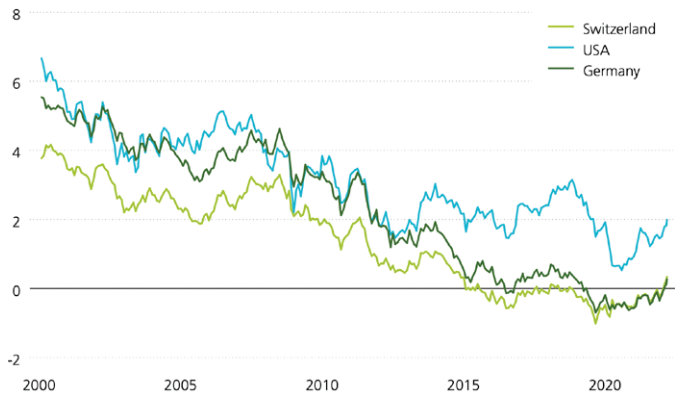
Indexed performance of government bonds in Swiss francs
100 = 01.01.2022



The Ukraine crisis also triggered turbulent conditions on the financial markets. After the Russian invasion, there was strong demand for government bonds, particularly in Europe. But the abrupt increase in value didn't last long. Concerns over inflation grew again due to the price shock on the oil markets that was triggered by the crisis. A barrel of oil briefly rose to over 130 US dollars, which equates to more than 60 percent higher than at the end of 2021. As there is no immediate end in sight to the high price trend, the value of government bonds is not expected to rise to any great degree in the near future.

Source: SIX, Bloomberg Barclays

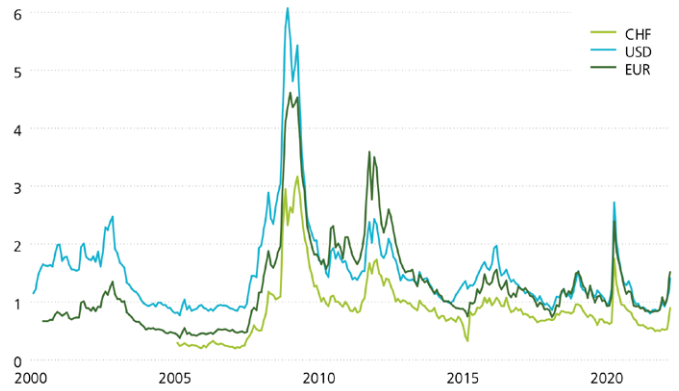
Trend in 10-year yields to maturity
In percent



The recovery from the coronavirus crisis has been marked by rising interest rates. During this period, the yield to maturity on 10-year US government bonds rose from just over 0.5 percent to 2 percent, while their Swiss counterparts re-entered positive territory, reaching their highest level for seven years, at 0.3 percent. This trend was interrupted at the end of February by the Russian invasion of Ukraine. Inflation rates have also risen again, especially in the industrial countries. This leaves the major central banks with the difficult choice of deciding between tackling inflation or supporting the economy.

Source: SIX, Bloomberg Barclays

Credit spreads on corporate bonds
In percentage points



Corporate bonds entail higher risk than their government counterparts. This is factored in accordingly by the spreads. After the coronavirus-related economic slump, the spreads have returned to their pre-crisis levels, or even exceeded them. In other words: the risks were factored in at less than 1 percent spread. The greater geopolitical and economic risks have interrupted this downward trend and have caused the spreads of US and European corporate bonds to widen significantly again.

Source: Bloomberg Barclays

Market overview

Swiss real estate investments

The price of Swiss real estate funds fell in response to the escalation of the Ukraine conflict.

Indexed performance of Swiss real estate funds
100 = 01.01.2022

Swiss real estate funds posted losses once again last month. While January's decline was mainly explained by interest rate hikes, greater anxiety on the market over the Ukraine conflict is currently causing larger fluctuations. Swiss real estate funds were down 6 percent for a time, before making a rapid recovery.

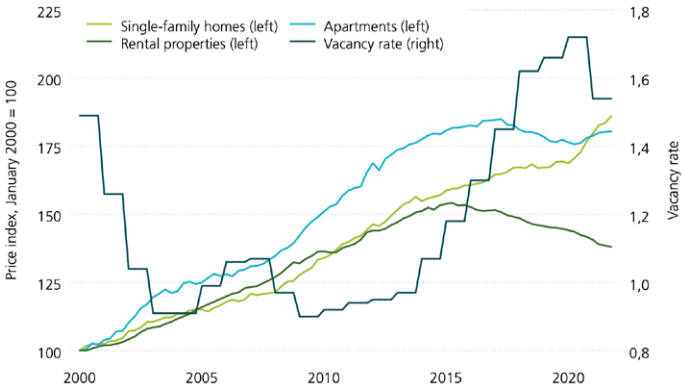
Source: SIX

Premium on Swiss real estate funds and 10-year yields to maturity
In percent

Last month, the premiums on Swiss real estate funds fell slightly from their record-high levels. Firstly, real estate investments have undergone price corrections since year-opening, and secondly, interest rates have climbed significantly during this period. While the yield to maturity on 10-year Swiss government bonds stood at just below zero at the turn of the year, it is now fluctuating at around 0.3 percent. The premiums demanded are now approaching the 40-percent mark again.

Source: SIX

Vacancy rate and real estate prices
100 = January 2000 (left) and in percent (right)



The gap on the real estate market is continuing to widen. While property owners are benefiting from rising prices on the real estate market, buyers are finding it increasingly difficult to enter the market because of the prices being asked. The price of Swiss single-family homes has risen by 6 percent on average in the past year alone. The increase since the turn of the millennium stands at an incredible 80 percent. Despite mortgage rates remaining low by historical comparison, climbing on to the property ladder is proving increasingly difficult. This is reflected by figures such as the higher average age of first-time buyers.

Source: SNB, SFSO

Market overview

Currencies

On the currency markets, a few currencies in particular underwent major fluctuations. While the Russian rouble collapsed under the pressure of sanctions, currencies deemed secure made gains.

Even the currency markets weren't spared by the turbulence on the financial market in the wake of the Ukraine crisis. As intended, the Russian rouble has collapsed under the pressure of economic sanctions. It has lost over 50 percent of its value since the outbreak of the Ukraine crisis. The euro has also suffered heavy losses, with the eurozone still being heavily dependent on Russia for its energy supply. This means that the economic risks are significant. At the beginning of March, the euro–Swiss franc exchange rate even briefly reached parity. The uncertain geopolitical outlook triggered a spike in demand for "secure currencies", including the US dollar, Swiss franc and Japanese yen. The currencies of commodity countries, such as Australia, New Zealand and Brazil, which are geographically far removed from the Ukraine conflict, also made gains.

Currency pair	Price	PPP [1]	Neutral area [2]	Valuation
EUR/CHF	1.02	0.93	0.86–0.99	Euro overvalued
USD/CHF	0.93	0.81	0.71–0.91	USD overvalued
GBP/CHF	1.22	1.34	1.15–1.52	Pound neutral
JPY/CHF	0.80	0.99	0.84–1.15	Yen undervalued
SEK/CHF	9.57	10.27	9.28–11.26	Krona neutral
NOK/CHF	10.38	11.54	10.30–12.77	Krona neutral
EUR/USD	1.10	1.14	0.99–1.28	Euro neutral
USD/JPY	116.14	82.13	66.99–97.28	Yen undervalued
USD/CNY	6.32	6.03	5.79–6.27	Renminbi undervalued

[1] Purchasing power parity. This metric calculates an exchange rate using relative inflation rates.
[2] Range of historically normal fluctuations.

Source: Web Financial Group

Gold

Gold has always been a popular investment in times of crisis. The precious metal once again lived up to this reputation in recent weeks, climbing to over 2,000 US dollars.

Indexed performance of gold in Swiss francs
100 = 01.01.2022

Looking for protection in the challenging geopolitical environment and amid greater inflation risks, demand from investors for the precious metal has risen once again. The gold price exceeded 2,000 US dollars per troy ounce for the first time since summer 2020. Measured in Swiss francs, the gold price is up by over 10 percent since year-opening.

Source: Web Financial Group

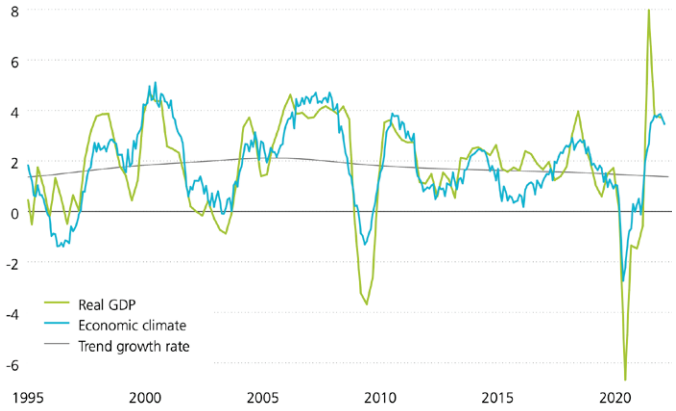
Economy

Ukraine conflict exacerbates inflation problem

The world economy began the year well. But the Ukraine conflict is now causing uncertainty. The main concern is higher energy prices.

Switzerland

Growth, sentiment and trend
In percent

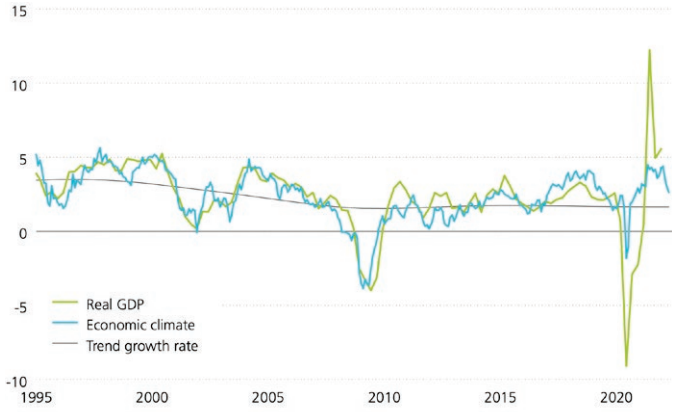


Source: Bloomberg

Switzerland achieved very solid economic growth of 3.7 percent last year. The main pillars of this strong growth were an increase in exports in the pharmaceutical industry (particularly vaccines) and higher revenue in the sales segment, with a record year posted for the retail sector. Unemployment has now returned to the same level as before coronavirus. As a third of industrial companies have indicated in surveys that they intend to increase headcount over the coming weeks, unemployment looks set to fall further. The Ukraine conflict is also causing uncertainty in Switzerland. However, direct trade in goods with Russia is extremely small. While Switzerland also obtains half of its gas supply from Russia, dependence on gas (e.g. for power generation) is low by European standards.

USA

Growth, sentiment and trend
In percent

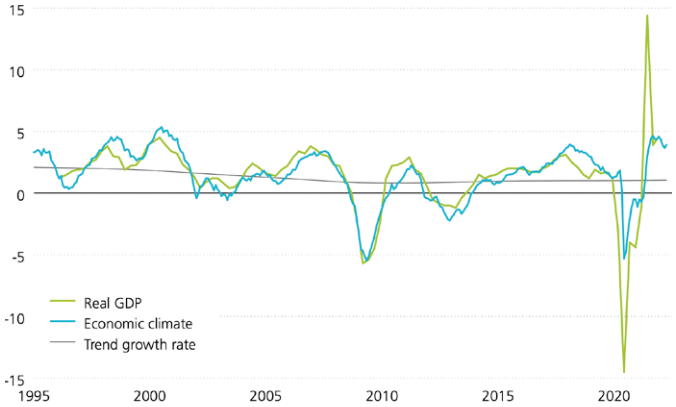


Source: Bloomberg

In the USA, the leading sentiment indicators have fallen sharply over recent months – albeit starting from a very high level. This points to normalization of economic momentum after six quarters of GDP growth. But the outlook remains bright overall. The biggest issue remains high inflation. While the labour market is in great shape – 650,000 new jobs were created in January alone – surveys of US households about consumer behaviour have not been so pessimistic for ten years. Households feared that their personal financial situation would deteriorate owing to high inflation.

Eurozone

Growth, sentiment and trend
In percent

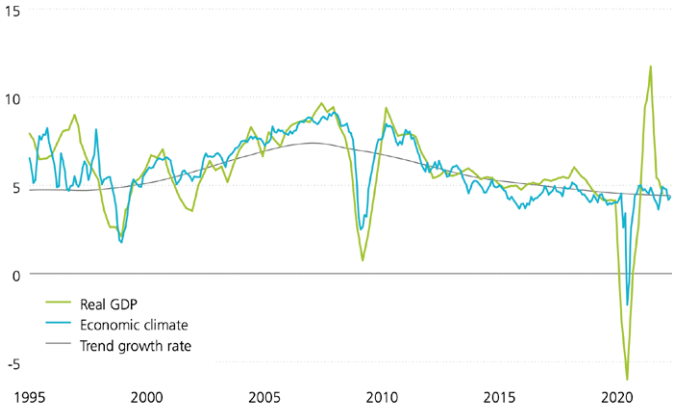


Source: Bloomberg

The sentiment indicators in the eurozone improved in February. Greater optimism is found in the services sector in particular, where there is a great deal of upturn potential after the end of the pandemic. But these surveys were carried out before the start of the Russian invasion of Ukraine. It is currently difficult to predict how much the war will dampen the optimism of households and companies.
Inflation rates are also causing grave concern in the eurozone. Inflation currently stands at 5.8 percent. Energy price rises triggered by the conflict may cause inflation to climb even higher over the coming months. In response, the European Central Bank has announced plans to accelerate withdrawal from its extremely expansive monetary policy. It looks likely to end its bond-buying scheme in the third quarter and then consider the option of interest rate hikes.

Emerging markets

Growth, sentiment and trend
In percent



Source: Bloomberg

Russia faces a challenging economic period after the outbreak of war. The value of the Russian rouble has almost halved since the conflict began. Even before the war, inflation was already high, at 9.2 percent. The collapse of the rouble may see inflation soar even higher. The Russian central bank actually has large currency reserves in euros, which could have been used to halt the collapse of the rouble. But the central bank, like other Russian banks, has been barred from the SWIFT payment system and had its assets abroad frozen, which probably came as a surprise to the Russians. This means that the central bank can no longer draw on its foreign currency reserves. Conversely, various international institutions are providing the Ukrainian state with aid loans.

Global economic data

Indicator	Switzerland	USA	Eurozone	UK	Japan	India	Brazil	China
GDP Y/Y [1] 2021Q2	3.8%	4.9%	4.0%	7.0%	1.2%	8.5%	4.0%	4.9%
GDP Y/Y [1] 2021Q3	3.7%	5.6%	4.6%	6.5%	0.7%	5.4%	1.6%	4.0%
Economic climate [2]	→	↘	↘	↘	↗	→	↘	↗
Trend growth [3]	1.4%	1.6%	0.8%	1.7%	1.0%	5.1%	1.2%	4.1%
Inflation	2.2%	7.9%	5.8%	5.5%	0.5%	6.1%	10.5%	0.9%
Key rates	–0.75%	0.08%	0.00%	0.50%	–0.10%	4.00%	10.75%	4.35%

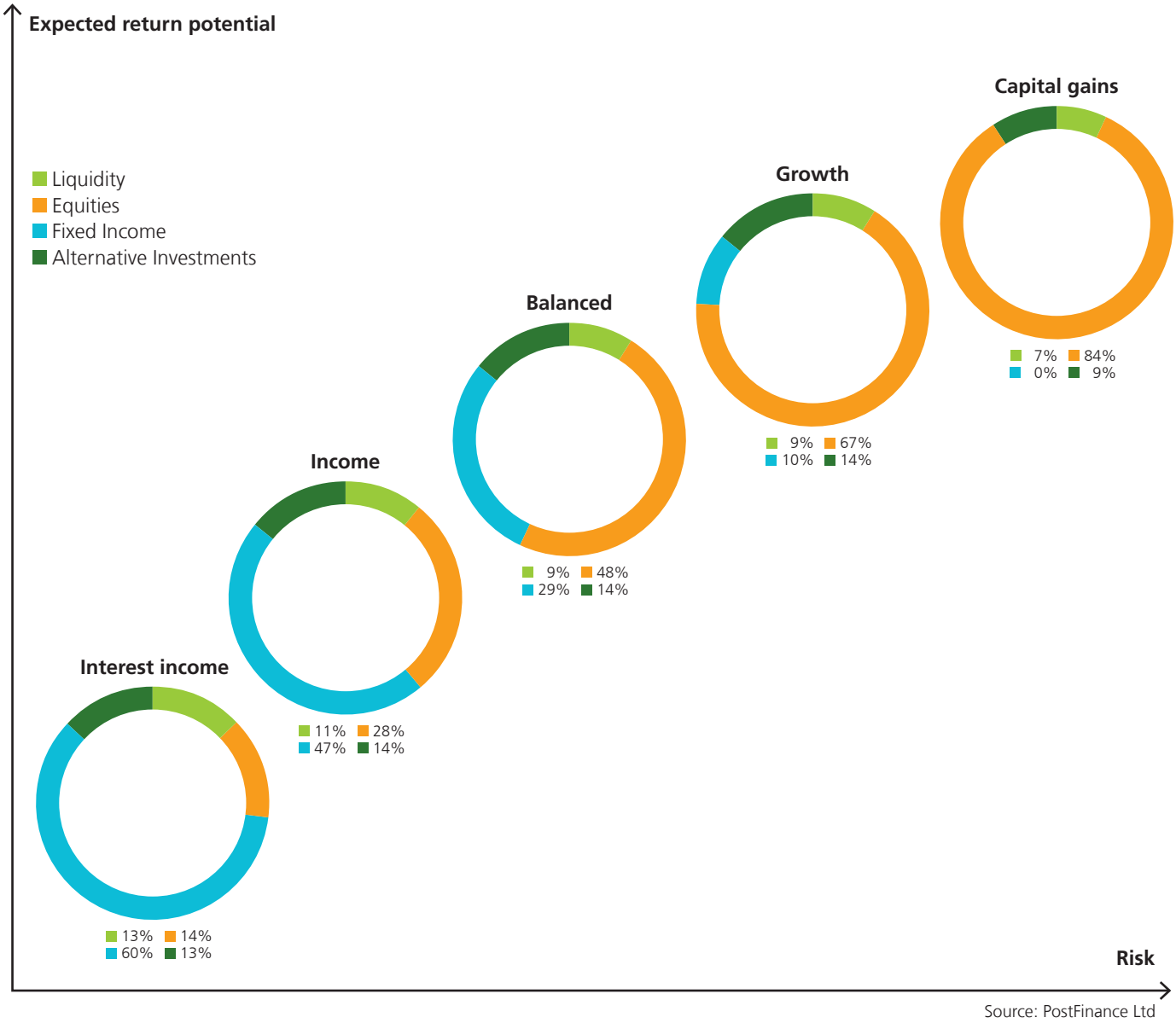
[1] Growth compared to year-ago quarter
[2] Indicator, measuring the overall sentiment and typically leading 1 to 2 quarters in advance of GDP. Plus indicates an increasing economic growth, minus a slowing.
[3] Potential growth. Long-term change in gross domestic product with sustainable capacity utilization.

Source: Bloomberg

Model portfolios Swiss focus

Aligned with increased risks

The geopolitical and economic uncertainties have clearly an impact on the financial markets. The situation is not expected to calm down in the foreseeable future. The high inflation rates will increasingly give rise to concerns about the economy. Central banks are confronted with a challenging situation. In this environment, a reduction of risks is indicated. In addition to the recent reduction in European equities, we are increasing the gold quota. In addition to inflation protection, the precious metal also offers crisis protection. At the same time, rising inflation expectations leave little room for falling interest rates. We are therefore maintaining our underweight in global bonds.



Source: PostFinance Ltd

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