Market Commentary
4th Quarter 2023

Christmas Gifts from the Fed

Market and Economic Developments

The start of the fourth quarter of 2023 was marked by negativity. The attack by Hamas on Israel unsettled global markets and fueled an already high inflation rate in the short term due to elevated oil prices. This uncertain climate was also mirrored in the purchasing managers' surveys published in October for both Europe and Switzerland.

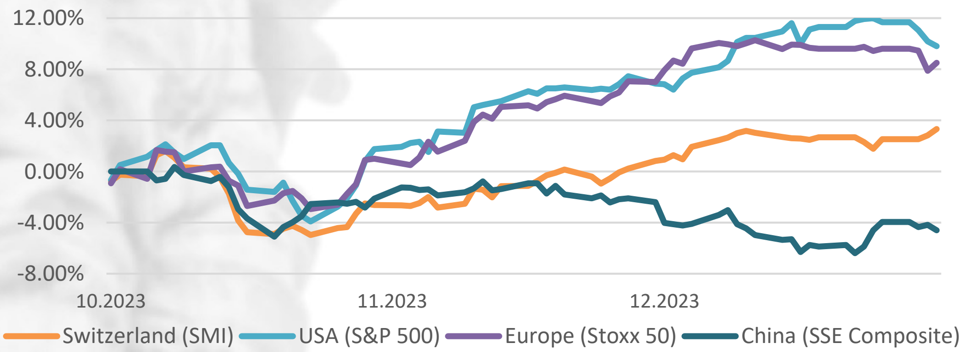
In contrast, the Purchasing Managers' Index (PMI) in the USA indicated marginally positive signals, which were substantiated by robust GDP figures released at the end of October. Europe, however, presented a mixed picture: While the economies of Germany and Italy experienced a downturn, France and Spain reported modest economic growth.

In response to the weakening global economy, the US Federal Reserve (Fed) and the Bank of England refrained from adjusting interest rates in November. Newly released US labor market and inflation figures likely played a pivotal role in their decision. While US unemployment rose in October, inflation steadily declined to 3.2% in November following the recent oil price shock. However, core inflation in Europe and the US continues to be high and the inflation still exceeds the 2% target.

By the end of November, bolstered by sharp declines in inflation in Western countries such as Germany and France, the markets began to factor in interest rate cuts. The rhetoric of individual Fed members, in particular, ignited the stock market rally. Neither the uncertainty surrounding the German budget nor the cautionary remarks from ECB Chief Christine Lagarde could dampen the upswing. Consequently, the low EU inflation in November (2.4%) and statements by Fed Chairman Powell that the Fed had initiated discussions on interest rate cuts acted as a catalyst for the stock markets.

The outcome was a year-end rally that was particularly pronounced in the Eurozone and the USA. Switzerland was positioned in the middle, while China, grappling with deflationary tendencies, lagged behind. This was in stark contrast to other emerging markets, which reaped substantial benefits in the fourth quarter.

Figure 1: World Indices in Local Currency



Source: Refinitiv, Datastream as of 10.01.2024

Key Takeaways

- The Middle East conflict dominated the markets at the start of the fourth quarter of 2023
- Statements by the US Federal Reserve spread hope that interest rates would be cut soon
- As a result of lower expected interest rates, all observed asset classes were able to gain towards the end of the year
- Nevertheless, questions regarding the sustainability of the recent price advances remain
- The global economy is weakening without any clear signs of a downward or upward trend

Monetary Policy

In the final quarter of 2023, the US Federal Reserve (Fed), the European Central Bank (ECB), and the Swiss National Bank (SNB) maintained a steady stance on interest rates. Australia was among the few Western nations to implement an interest rate hike in the fourth quarter.

The SNB's decision in September to hold interest rates steady was particularly noteworthy. This decision limits the flexibility of the SNB's head, Thomas Jordan, to implement future interest rate reductions, particularly considering the monetary policy challenges anticipated in 2024. On one hand, the increase in Value Added Tax (VAT) has been effective since January, while on the other hand, healthcare costs in Switzerland have once again experienced a significant surge. Projections also anticipate further increases in rent, as these are tied to the reference interest rate in Switzerland, which only mirrors the interest rate environment with a delay. Ultimately, these increases will exert upward pressure on inflation figures. The SNB also expresses concern over the current strength of the Swiss Franc, which is particularly impacting the export-oriented industry sector. The challenge for the SNB in 2024 will be to strike the right balance between fighting inflation and maintaining economic stability. It remains to be seen where the SNB's priorities will lie.

In the United States, the rhetoric of individual members of the Fed committee sparked a rally in stocks towards year's end. However, the monetary authorities promptly sought to dampen the optimism with pessimistic statements. Nevertheless, the new interest rate expectations have taken hold in the markets. Figure 2 illustrates the interest rates on US Treasuries for various maturities, measured at different points in time. As can be observed, the markets initially underestimated the consistency with which the Fed would implement interest rate hikes at the start of 2023. By mid-year, the belief had solidified that interest rate reductions would not materialize until well into 2024. However, the new reality (bright line) now reflects the expectation that interest rates will decrease more rapidly than previously assumed.

In conclusion, it can be said that the central banks have presented investors with a Christmas gift by signaling interest rate cuts. However, the question remains as to the true magnitude of this gift, as it will not be unveiled until 2024.

Market Data

Equity Markets Perf.	2023
SPI	6.09%
DAX	20.31%
Euro Stoxx 50	23.19%
S&P 500	26.29%
Nasdaq Composite	43.42%

Yield to Maturity of Government Bonds	in %
10Y Swiss Federal Bond	0.70%
10Y German Federal Bond	2.03%
10Y US Treasury	3.87%

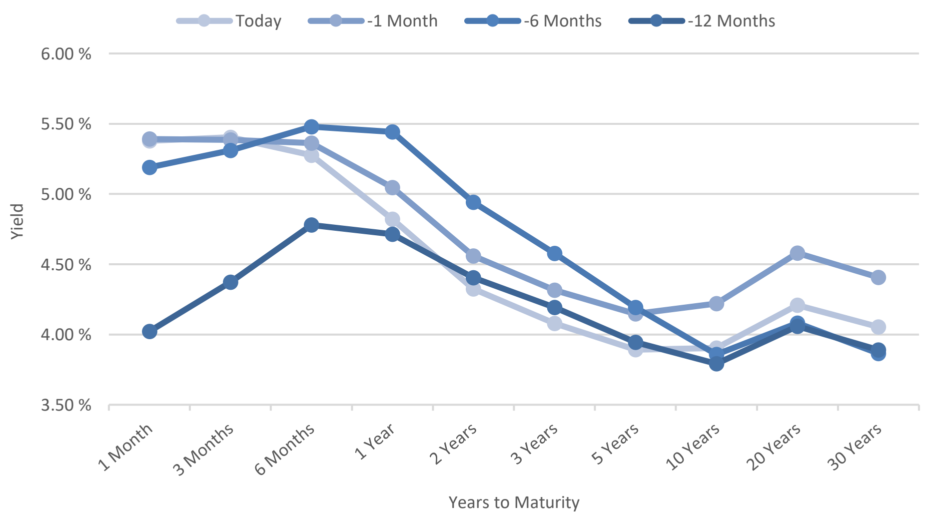
Gold (oz.) Perf.	2023
in CHF	3.49%
in EUR	9.91%
in USD	13.76%

Commodities Perf.	2023
Oil Brent	-3.13%

Year-to-Date (YTD) performance in local currency, as of 31.12.2023

Source: Refinitiv, Datastream

Figure 2: US Treasury Yield Curves



Source: Refinitiv, Datastream as of 10.01.2024

Financial and Capital Markets

At the onset of the fourth quarter of 2023, stock markets experienced a downturn due to uncertainties in the Middle East. However, beginning in November, the markets were driven by expectations of interest rate cuts, propelling some share indices close to or beyond their annual peak. Concurrently with the equity rally, yields to maturity on fixed income investments declined, resulting in price gains in this asset class. Gold also underwent a highly volatile quarter. It remained below the USD 1920 mark in October before geopolitical uncertainties and falling current yields propelled it to a new all-time high, transforming a negative annual performance at the quarter's start into a substantial profit.

In 2023, the financial sector was frequently in the spotlight. In the spring of 2023, following multiple bankruptcies of American regional banks, Credit Suisse was acquired by UBS. Nevertheless, the threat of a global banking crisis did not materialize, largely due to substantial liquidity injections into the system by central banks.

In 2023, the emergence of artificial intelligence as a significant theme on the stock markets propelled technology stocks to new heights. This was mirrored in the robust performance of the Nasdaq, which experienced a surge of over 43%. Microsoft and Nvidia were among the beneficiaries, both achieving new all-time highs in 2023. Even the management turmoil at OpenAI in November, a firm in which Microsoft has made significant investments, could not change the trend. However, the price advances in connection with the AI technology are primarily rooted in the expectation of future profits. If these are not met, share prices may correct downwards.

In 2023, emerging markets, with the exception of China, largely experienced gains. Many emerging markets were bolstered by global companies shifting their supply chains from China to other countries. Some countries, such as Poland and Brazil, have already begun to reduce interest rates. As a result, both stock markets witnessed significant growth in the fourth quarter of 2023. In the case of Brazil, the heightened interest in energy suppliers was particularly advantageous, given that Russia is no longer an oil supplier for Western countries.

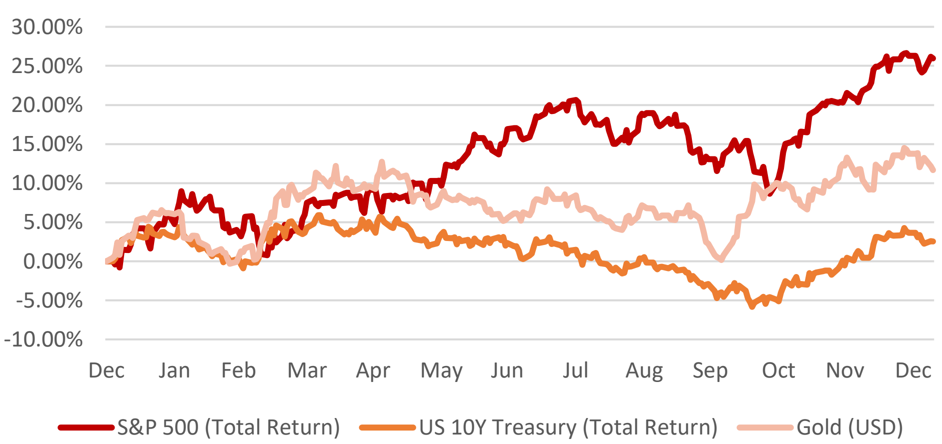
Figure 3 illustrates the performance of the S&P 500, 10-year US Treasuries, and gold for 2023 in USD. The impact of the end-of-year rally across all asset classes, due to the anticipated interest rate cut, can be observed from October onwards.

Asset Allocation

Asset Class	Positioning
Cash	Overweight
Fixed Income	Underweight
Equity	Small Underweight
Gold	Strong Overweight

- Our still high liquidity position, invested in money market funds, gives us flexibility should an opportunity present itself
- Due to the strong gold focus, we were able to benefit noticeably from the rising gold price in the fourth quarter
- The price gains on the markets are driven by expectations of interest rate cuts in the near future. If these fail to materialize, the market could be disappointed and correct, which is why we remain slightly underweight in equities

Figure 3: Performance of the S&P 500, 10Y Treasury and Gold for the year 2023



Quelle: Refinitiv, Datastream as of 10.01.2024

Current Asset Allocation

The Bank's asset management mandates concluded the year on an exceptionally positive note. For the mandates within the balanced risk category, the net performance for the model portfolios with mandate currencies CHF, EUR, and USD were 4%, 8%, and 9.2% respectively.

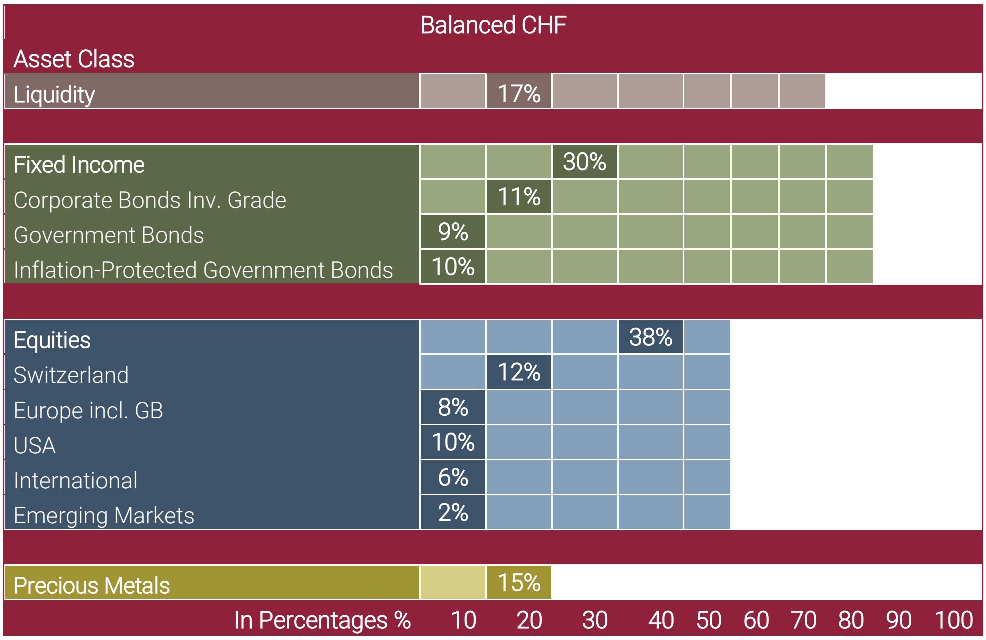
Bank von Roll's equity selection performed extraordinarily well in 2023. Swiss equities, in particular, significantly outperformed the market. The selected individual Swiss equities yielded an equally weighted return of over 20%, compared to the SMI (5.8%), representing an excess return of more than 14%. Due to our superior selection, we were able to offset our small equity underweight and maintain a strong position against our competitors, even during the year-end upswing.

Starting from March, bonds consistently lost value. As the prices declined, the expected return in this asset class rose. During these periods of correction, we strategically made selective purchases. As signs of a reversal in interest rates began to surface in late autumn and the market started to factor them in, the value of the bonds we held appreciated. Bonds with a high duration benefited particularly. However, at the onset of 2024, it became evident that the markets had overestimated the pace of interest rate reductions, resulting in a slight price drop.

Gold experienced substantial gains at the start of 2023, but then steadily depreciated until September. Nevertheless, geopolitical uncertainties and the anticipation of potential interest rate cuts propelled the gold price to new highs in October and December, enabling gold to make a significant contribution to our returns.

We maintain a cautious outlook for the forthcoming year 2024, as the new year presents both known and unforeseen challenges. These include the elections in the USA, Russia, and Taiwan, which could exacerbate geopolitical tensions. In terms of fiscal policy, inflation, which remains above the target range, continues to be a concern, along with the massive debt for countries and enterprises. Unresolved issues pertaining to demographic ageing and climate change will also be a focus in 2024. On the other hand, interest rate reductions, advancing digitalization, and a continued high propensity to consume in large parts of the world continue to be growth drivers for the economy.

Figure 4: Asset Allocation as of 01.01.2024



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