# Market Insights

May 2023

BANQUE CRAMER

# CIO Synopsis

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## Climbing the Wall of Worry

Last month, all eyes were on US politics being able to reach an agreement on the debt ceiling. A deal was reached under the wire, which brought back investors' positive sentiment. Recession fears have been pushed out towards 2024. Even the most bearish economists are now turning less negative on the US and European economies.

Tech replaced safe havens like Consumer Staples and Utilities, as they hold large cash positions and are responsible for most of the performance of the main indices like the S&P 500. Is "AI" a hype or a complete reshaping of the use of technology in many fields of our daily lives?

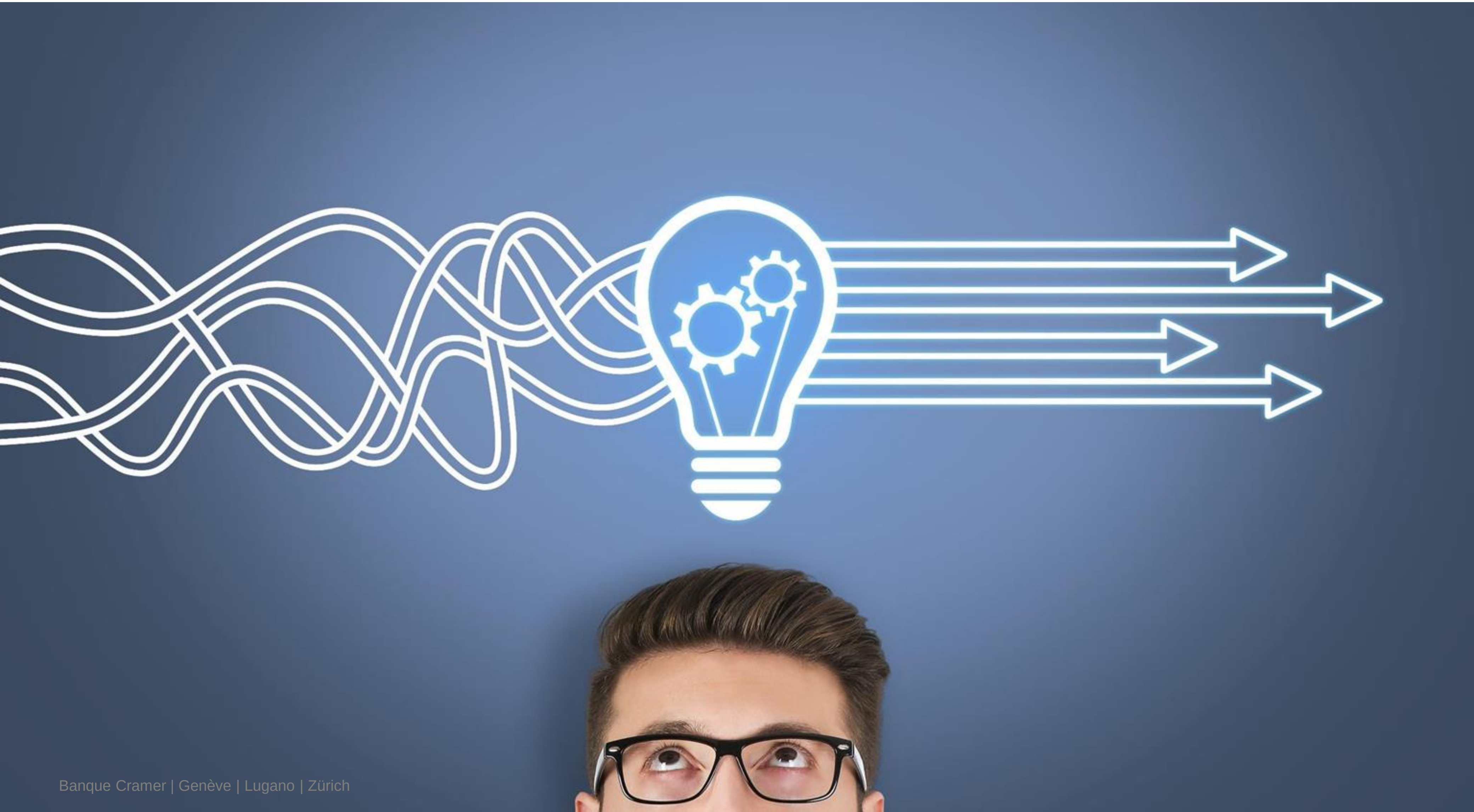
We are now entering summer, which is historically known for storms and stress in the markets, caused by less liquidity and little appetite from investors to enter new positions. The focus will remain on economic numbers and especially on how much positive or negative surprises are already priced in. The US consumer data have shown resilience, is it going to last? Are current valuations sustainable going into H2 of 2023? We are climbing the Wall of Worry …

China will also play a central role in the second act of 2023. Everyone is waiting for the great recovery that is playing hard to get, and that will be the main driver for commodity prices such as copper, steel and oil. The Middle Kingdom needs a stimulus package in order to return back to growth and achieve the growth target set by its government.

Credit Spreads still seem too low, as the refinancing of debt has become much more expensive, and usually the effects of higher financing costs are lagging. Watch out for High Yield with low quality.

Hans Itburrun

# What keeps me up at night



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Chief Investment Officer (CIO)

## The Magnificent Seven!

America's Magnificent Seven stocks are up 70% YTD (equal-weighted), the other 493 stocks in S&P 500 up only 0.1%!! The only other times when the tech sector surged over 4% while overall stocks declined were at the onset and in the middle of the Tech Bust - April 2000 and March 2001. Seen another way, the performance of the S&P 500 equal weighted index vs the market cap weighted index is rather poor this year. We can see why, as year-to-date performance has been strongly concentrated in a handful of these very large stocks, many of the same have very high weightings in the S&P 500, and even more so in the NASDAQ 100.
Another record breaking event was the **LARGEST SINGLE DAY MARKET CAP GAINS IN US STOCK MARKET HISTORY !**

Apple Nov 2022 $191B, Amazon Feb 2022 $184B, **Nvidia May 2023 $179B,**Microsoft Mar 2020 $144B, Tesla Jan 2022 .

When we think of technological development, we often imagine a smooth exponential line upwards. In reality, technological development is mostly a series of overlapping step-changes. Certain technological breakthroughs occur, cause a multi-decade technological boom, and then run into a hard ceiling and stagnate, until the next breakthrough emerges.
***Artificial intelligence (AI)*** has been with us for a while. For over two decades, chess programs have been able to beat the best human chess champions. AI has the capacity to disrupt all sorts of legacy-white collar businesses. Administrative overhead within organizations can be greatly streamlined, for example. ***Unless or until AI helps us solve some materials constraint of the globe, it will likely to be slower to affect the physical world than the digital world***. What it means is that the ***production and distribution of energy and materials remains a key limitation***. Economy is just about access to easy and cheap Energy and its transformations – never forget that! Artificial Intelligence has all sorts of capacities to change how we interact with digital systems, but is unlikely to change energy and materials markets much, other than giving us small or moderate efficiencies around the margins.
Robots are complex, energy-intensive, materials-intensive, and maintenance-intensive. People have historically overestimated the speed of hardware development (supersonic planes, flying cars, robot assistants) and underestimated the speed of software development. I can only endorse current AI excitement only if it brings some major physics breakthrough.
This AI mania has worsened market breadth - worst than the Dot Com bubble. Poor market breadth often leads to a leg down and as Bob Farrell's will put it:
***Markets are strongest when they are broad and weakest when they narrow to a handful of blue-chip names. This is why breadth and volume are so important. Broad momentum is hard to stop, Farrell observes. Watch for when momentum channels into a small number of stocks.***

# Market review

# Macro Outlook

The economic forecasts continue to assume that the effects of the expected further tightening in bank credit conditions, amid already tight financial conditions, would lead to a mild recession starting later this year, followed by a moderately paced recovery. Real GDP is expected to decelerate over the next two quarters before declining modestly in both the fourth quarter of this year and the first quarter of next year. Real GDP for 2023 is expected to grow at 1.10% and 0.79% in 2024. The unemployment rate is forecasted to increase this year, to peak next year, and then to start declining gradually in 2025. Core Inflation continues to trend lower, but at a slower pace.

In the European Union, the expectations are that a recession will be avoided, and that growth will be 0.6% followed by 1.0% in 2024. Inflation however is still high and predicted to stay at elevated 5.60% for 2023. The expectations are however that the peak was reached in April. The ECB indicated that they would continue to raise interest rates in the coming months to achieve lower inflation in 2024. The forecasts now predict a 2.5% in Core CPI in 2024. Unemployment rate for the Euro Area is expected to remain unchanged at 6.8%.

In China, the economic recovery is moving slower than expected. The GDP Growth expectations for 2023 have been revised lower by most analysts, with consensus now below 5% and below the PBOC expectations of 5.60%. Especially net exports are dragging numbers down, while domestic consumption is expected to gradually accelerate. The consensus is that more stimulus is needed to achieve growth targets for this and next years.

| Zone | Item | 2022a | 2023e | 2024e |
|---|---|---|---|---|
| US | Real GDP (YoY%) | 2.10 | 1.10 | 0.79 |
| | Industrial Production (YoY%) | 3.41 | -0.50 | 0.30 |
| | CPI (YoY%) | 8.02 | 4.11 | 2.57 |
| | Unemployment (%) | 3.64 | 3.78 | 4.60 |
| | Current Account (% of GDP) | -3.71 | -3.10 | -3.10 |
| | Fiscal Bal. (Budget, % of GDP) | -5.43 | -5.58 | -5.70 |
| China | Real GDP (YoY%) | 3.00 | 5.60 | 5.96 |
| | Industrial Production (YoY%) | 4.00 | 5.38 | 5.00 |
| | CPI (YoY%) | 1.96 | 1.75 | 2.30 |
| | Unemployment (%) | 3.96 | 5.00 | 5.00 |
| | Current Account (% of GDP) | 2.23 | 1.50 | 1.14 |
| | Fiscal Bal. (Budget, % of GDP) | -4.70 | -4.90 | -4.60 |
| EU | Real GDP (YoY%) | 3.50 | 0.60 | 1.00 |
| | CPI (YoY%) | 8.36 | 5.60 | 2.50 |
| | Unemployment (%) | 6.73 | 6.80 | 6.90 |
| | Current Account (% of GDP) | -0.73 | 1.50 | 1.80 |
| | Fiscal Bal. (Budget, % of GDP) | -3.60 | -3.50 | -3.00 |

Source: Bloomberg (a = actual, e = consensus forecasts), as of 31/05/2023

# Equities

The US equity market traded in a narrow range but managed to hit a new eight-months-high towards the end of the months. Volatility dropped to the lowest levels as recession fears have been pushed out into the future. The focus rapidly shifted from the banks deposit crisis to the debt limit discussion in Washington. The worries of the US Treasury not being able to pay interest rates in June created some volatility in the first week of May. Negotiations finally succeeded and an agreement was found before the X-day on June 1st. It needs to be mentioned that almost all of the year-to-date performance of the S&P 500 is concentrated in the big seven stocks, namely Apple, Alphabet, Microsoft, Meta, Nvidia, Amazon and Tesla. Technology was the stand-out sector, rising 9.29%. An increased demand for "Artificial Intelligence" related equipment and applications forced investors to increase their exposure. Nvidia's market cap has been pushed above one trillion USD for the first time. This explains the outstanding rally of the Nasdaq 100 index, climbing 7.6% in May and over 30% year-to-date. The worst performing sectors were Energy (-10.61%) and Materials (-7.11%). A weak demand from China and fears of a slowing economic growth in the 2nd half of this year were the main drivers for the sell-off.

In Europe, both main indices the Stoxx 600 and the Euro Stoxx 50 lost 3.2%. The Energy, Materials and Financials heavy weighted indices mainly lagged due to their composition, having little exposure to Technology. Despite a negative quarterly GDP growth and high inflation, the German DAX managed to hit a new all-time high. The year-to-date performances of the main European indices are still higher than in the US, showing a historically rare picture.

Japan's Nikkei climbed above the important level of 30'000, after two failed attempts this year. The unchanged low interest rate policy of the new BOJ President and good corporate earnings have pushed the index to levels not seen since 1990. The Hang Seng Index continued to underperform losing 8% in May, erasing all positive momentum about the Chinese post-pandemic excitement.

| | **As of 31/05/2023** | **1-month perf.** | **Year-to-date perf.** |
|---|---|---|---|
| S&P 500 | 4 179.83 | 0.2% | 8.9% |
| Nasdaq 100 | 14 254.09 | 7.6% | 30.3% |
| Euro STOXX 50 | 4 218.04 | -3.2% | 11.2% |
| STOXX Europe 600 | 451.76 | -3.2% | 6.3% |
| SMI | 11 217.89 | -1.9% | 4.6% |
| DAXK | 6 207.70 | -3.8% | 9.1% |
| CAC 40 | 7 098.70 | -5.2% | 9.7% |
| FTSE MIB | 26 051.33 | -3.8% | 9.9% |
| IBEX 35 | 9 050.20 | -2.1% | 10.0% |
| Nikkei 225 | 30 887.88 | 7.0% | 18.4% |
| MSCI EM | 958.53 | -1.9% | 0.2% |
| HSCEI | 6 163.34 | -8.0% | -8.1% |
| IBOVESPA | 108 335.07 | 3.7% | -1.3% |

Source: Bloomberg

# Rates & Credit

The US fixed income market was dominated by the newsflow around the Debt-Limit discussions. Especially the very short-term interest rates were subject to unusually high volatility. The yield for the US T-Bill expiring on June 8th spiked to almost 6% before normalizing after the announcement of a debt limit extension. The US 1-year CDS in EUR dropped from high 175 to below 50 after the news.
The rest of the US yield curve shifted higher in May after another strong job market report and inflation data showing little changes compared to April's decline. Although the consensus that the Fed will pause after a last 25bps hike in June or July is high, bond markets do not agree on Fed Funds Forwards, already pricing in three FED cuts until the end of the year.

Global corporate bond markets seem to share this view and took the opportunity to refinance some of their debt at lower conditions. Credit Spreads however were mainly unchanged in May.

Analysts are starting to flag higher default rates in High Yield if rates continue to move higher and economic activity would continue to contract.

In Europe spreads within the European Union did not change materially, as the message from the ECB to continue raise rates is unilateral and the political situation within the EU can be described as calm.

| | **As of 31/05/2023** | **1-month perf.** | **Year-to-date perf.** |
|---|---|---|---|
| Euribor 3M | 3.46 | +20 bp | +133 bp |
| SOFR RATE | 5.06 | +25 bp | +76 bp |
| Germany 2yr yield | 2.71 | +3 bp | -3 bp |
| Germany 10yr yield | 2.28 | -3 bp | -29 bp |
| US 2yr yield | 4.40 | +40 bp | -2 bp |
| US 10yr yield | 3.64 | +22 bp | -23 bp |
| France 10yr spread vs. Germany | +57 bp | -1 bp | +2 bp |
| Portugal 10yr spread vs. Germany | +74 bp | -8 bp | -27 bp |
| Spain 10yr spread vs. Germany | +105 bp | n.a. | -4 bp |
| Italy 10yr spread vs. Germany | +180 bp | -7 bp | -34 bp |
| iTraxx Main 5yr | +82 bp | -1 bp | -9 bp |
| iTraxx Crossover 5yr | +434 bp | -1 bp | -40 bp |
| iTraxx Financials Senior 5yr | +93 bp | -5 bp | -6 bp |
| CDX IG 5yr | +76 bp | n.a. | -6 bp |
| CDX HY 5yr | +475 bp | +9 bp | -9 bp |



Source: Bloomberg

# Commodities

May was a rough month for commodities.
Most of them significantly declined, partially driven by a softening inflation. Only Cocoa prices rose by +2.38% on concerns that an El Niño, which is predicted to develop in the coming months, could trigger extreme weather and affect crops.

Oil prices tumbled again, with Brent losing -8.65% in May and the WTI -11.32%. Even though some OPEC+ members announced a 1mio barrels/day cut in the production, investors have turned bearish due to the weakening US economy, ongoing fragility within its banking sector, and the unfavorable manufacturing data from China, leading to a decline in refining margins.

Gold traded above the $2000 during the first half of May, before reverting toward $1962 on a strengthening USD. The same goes for Silver which tested the $26 level for the first time since March 2022, before dropping back towards $23.

Copper fell below $360 for the first time this year. Inventory have almost doubled since mid-April as China’s weak recovery has hit the demand for the red metal.

Corn prices took a hit (-12% in the first half of May) before raising +7% towards the end of the month, as prices are mostly driven by concerns on the expected hot and dry weather. In some US states like North Dakota, up to 500’000 acres of land intended for corn may go unplanted.

| | As of 31/05/2023 | 1-month perf. | Year-to-date perf. |
|---|---|---|---|
| Brent ($/bbl) | 72.66 | -8.65% | -15.42% |
| WTI ($/bbl) | 68.09 | -11.32% | -15.16% |
| Natural Gas ($/MMBtu) | 2.27 | -5.98% | -49.36% |
| Gold ($/toz) | 1 962.73 | -1.37% | 7.60% |
| Silver ($/toz) | 23.49 | -6.26% | -1.96% |
| Platinum ($/toz) | 998.42 | -7.41% | -7.06% |
| Palladium ($/toz) | 1 368.35 | -9.19% | -23.67% |
| Copper ($/MT) | 363.70 | -6.02% | -4.55% |
| Iron Ore Fines62% ($/MT) | 101.23 | -3.42% | -13.59% |
| Corn (c/bu) | 594 | -6.60% | -12.45% |
| Wheat (c/bu) | 594 1/4 | -6.23% | -26.00% |
| Soybean (c/bu) | 1 299 3/4 | -8.42% | -15.23% |
| Coffee (c/lb) | 178.65 | -3.93% | 7.23% |
| Cocoa ($/mt) | 3 007.00 | 2.38% | 15.65% |



Source: Bloomberg

# Currencies

The US dollar strengthened in May (+2.6%) as Democrats and Republicans have finally reached an agreement on the debt-limit on Sunday the 28th, a few days before the X-day.
After two consecutive positive months, the EUR/USD has lost -3.0% in May, and the CHF reached a one-year low early into the month (USD/CHF 0.882) before getting back to 0.91.

Japan’s top currency diplomat said that they are closely watching FX moves and they will respond “appropriately” if required. That statement seemed to have little effect on the JPY, which rose again above 140, as BoJ’s Ueda reiterates that monetary policy will remain accommodative until 2% inflation is reached.

Turkish Lira weakened to a record low (USD/TRY +6.7% over May) after the re-election of Erdogan. With very high inflation and low interest rates, Erdogan’s win was not seen positive by foreign investors.

GBP and CAD remained stable (-1.0% and +0.2%, respectively).

In China, the weak economy recovery weighted on the Renminbi which lost 2.8% against the US Dollar. The FX pair has surged 6.1% from its January low.

The Mexican Peso increased in the first half of the month (USD/MXN -3.15%). It then softened and tested the 18 psychological level without breaking it, fueling its strength.

| | As of 31/05/2023 | 1-month perf. | Year-to-date perf. |
|---|---|---|---|
| EUR/USD | 1.07 | -3.0% | -0.1% |
| USD/JPY | 139.34 | 2.2% | 6.3% |
| EUR/GBP | 0.86 | -2.0% | -3.0% |
| USD/CHF | 0.91 | 1.8% | -1.5% |
| EUR/CHF | 0.97 | -1.2% | -1.6% |
| GBP/USD | 1.24 | -1.0% | 3.0% |
| USD/CAD | 1.36 | 0.2% | 0.1% |
| USD/CNY | 7.11 | 2.8% | 3.0% |
| USD/INR | 82.73 | 1.1% | 0.0% |
| USD/BRL | 5.06 | 1.4% | -4.3% |
| USD/TRY | 20.73 | 6.7% | 11.0% |
| USD/ARS | 239.47 | 7.6% | 35.2% |
| RUB/USD | 0.01 | -1.7% | -8.5% |
| DXY Index | 104.33 | 2.6% | 0.8% |

Source: Bloomberg

# The Month Ahead: Economic Calendar

For June the focus continues to be on how severe the economic slowdown in the US will be. Markets will monitor closely if tighter credit conditions caused by the crisis in the regional banks coupled with the higher interest rates environment will be enough to bring inflation down to neutral levels.

The FED could increase rates either at the next meeting or postpone the 25bps hike into July, depending on the data published in the month of June.

The job market could start to show signs of cooling and if wage growth is starting to slow, this could be another important factor for the FED to stop raising rates.

In Europe a recession seems to be avoided as energy prices have not continued to rise and demand for European goods is stable, despite high inflation.

China is still the wild card and will continue to send mixed signals. Only an important stimulus package could be supportive for growth rates to start rising again.

| Zone | Item | Date | Survey | Prior |
|---|---|---|---|---|
| US | Unemployment Rate (May) | June 2 | 3.5% | 3.4% |
| US | Change in Nonfarm Payrolls | June 2 | 195k | 253k |
| EU | PPI (YoY) (Apr) | June 5 | - | 5.9% |
| US | Trade Balance (May) | June 7 | -$75.1b | -$64.2b |
| CH | CPI (YoY) (May) | June 9 | 0.2% | 0.1% |
| US | CPI (YoY) (Apr) | June 13 | 4.1% | 4.9% |
| US | FOMC Rate Decision (upper) | June 14 | 5.25% | 5.25% |
| US | PPI Final Demand (MoM) | June 14 | 0.0% | 0.2% |
| US | Industrial Production (MoM) | June 15 | 0.2% | 0.5% |
| CH | Industrial Production (YoY) | June 15 | - | 5.6% |
| US | GDP (QoQ) (1Q T) | June 29 | - | 1.3% |
| CH | Manufacturing PMI (May) | June 30 | - | 48.8 |



Source: Bloomberg

# Invest with our Thematics

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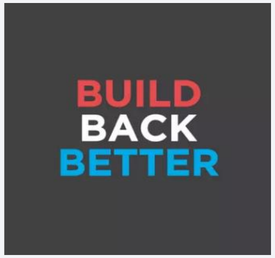
## Strong Balance Sheets

Actively Managed Certificate • Participation • Available in USD

Our proposal is to exploit the well-known Altman Z-Score framework combined with other metrics in order to take refuge in the companies currently exhibiting the most solid balance sheets in Europe and in the US. The latter will resist better in the current environment marked by the credit tightening, geopolitical tension, earnings recession and macro deceleration.




## Global Jobs & Economic Recovery

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The Strategy objective is to benefit from global governmental policies helping people who have lost their job due to COVID-19 to go back to work. US has launched the "Build Back Better" scheme and similar political agendas are prescribed in other part of the world to accelerate job creation. The index invests mainly in Small and Mid-Cap companies which are the biggest employers on a size-adjusted basis which is true globally. Allocation between different regions will be actively managed and run from a Top-Down perspective while the Bottom-Up stock picking will be delegated to active fund managers. The strategy provides exposure to a broad sector allocation. Passive vehicles may be used to add momentum on any major political moves to put people back to work. The short leg of the index aims, first and mainly, to hedge beta exposure whenever the index sponsor deems necessary. On opportunistic and specific cases, short positions may be used to add value. The net exposure will at all-time be net long.

## Macro Long-Biased Asia

Actively Managed Certificate • Participation • Available in USD

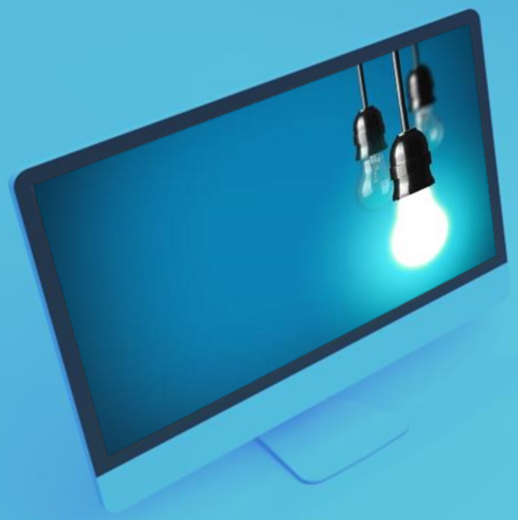
Our Macro Long-Biased Asia strategy follows a long/short approach using the best convictions equities identified by Macquarie's Research department. Macquarie analysts aim at adding value both on their long selection but also on the short leg. Short position on Asian indices can be added as a mean of hedge.  Using a bottom up approach, a committee of experienced analysts individually review and analyze each Asian (ex Japan) stock with a buy and sell recommendation to select only the strongest convictions.

## Energy Security

Actively Managed Certificate • Participation • Available in USD

The war in Ukraine is proving to be a wake-up call for Europeans and the whole world. At the very least, alternatives to natural gas must be found. Nuclear power will be re-examined and carbon sequestration will have to be accelerated, as the exit from coal will be delayed. This crisis has highlighted the importance for states to ensure their energy independence.

The certificate invests mostly in stocks that will benefit from this trend. Direct exposure to commodities is allowed for up to 20% of the portfolio.



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