MARKETING DOCUMENT | JUNE 2024

UBP House View

Union Bancaire Privée

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Converging growth

European countries are finally rebounding from a period of stagnation. The recovery momentum is expected to gather pace in the coming months, driven by swifter easing of monetary policies by European central banks. Household confidence is on the rise, and consumption is picking up as purchasing power improves. Meanwhile, US growth projections are likely to normalise, leading to a convergence of developed market economies in the second half of the year.

The marked decline of inflation in Europe relative to the US implies that, after the surprise rate cut from the Swiss National Bank (SNB), the European Central Bank (ECB) and the Bank of England (BoE) are set to decouple their monetary policies from the Federal Reserve's inclination towards a "higher-for-longer" stance. The ECB should begin its easing cycle in June, followed by the BoE in August after the general election in July. However, with growth expected to stabilise in 2025, terminal rates could remain at relatively high levels, reflecting a persistently challenging landscape.

The rebalancing of growth is reflected in the solid performances by European markets. Since the beginning of the year, market rallies regionally broadened, underpinning our convictions in the United Kingdom (UK) and Switzerland raised in April.

In the coming months, we will closely monitor the progress of the US presidential race. During non-recession periods, US election years have demonstrated positive investment returns for equity and credit investors.

Key Takeaways

1 MACROECONOMY

Europe rebounds and improves growth prospects for developed countries.

2 MONETARY POLICY

European central banks are more accommodating than the Federal Reserve.

3 EQUITIES

In May, global equities recovered from weakness in April, with the MSCI World index rebounding +4.5% and the S&P 500 reaching an all-time high.

4 FIXED INCOME

Considering elevated risks in long-duration bonds ahead of the US presidential election, we maintain our short-duration positioning of 3.2 years for a USD balanced portfolio, while maximising yields.

The opinions expressed in this document are as at 3 June 2024 and are subject to change without notice.

Macroeconomic environment

EUROPEAN GROWTH REBOUNDS

As anticipated in our scenario, global growth has strengthened to 3.2% in 2024, driven by a rebound in Europe and China's measures to contain the property crisis.

Europe picks up, the US slows down

The outlook for European growth has been revised upwards following the positive surprises in first-quarter growth figures. European countries are showing better indicators than the United States, where they have disappointed, except for confidence in the services and manufacturing sectors. Growth in developed countries is therefore expected to approach 1.6% in 2024.

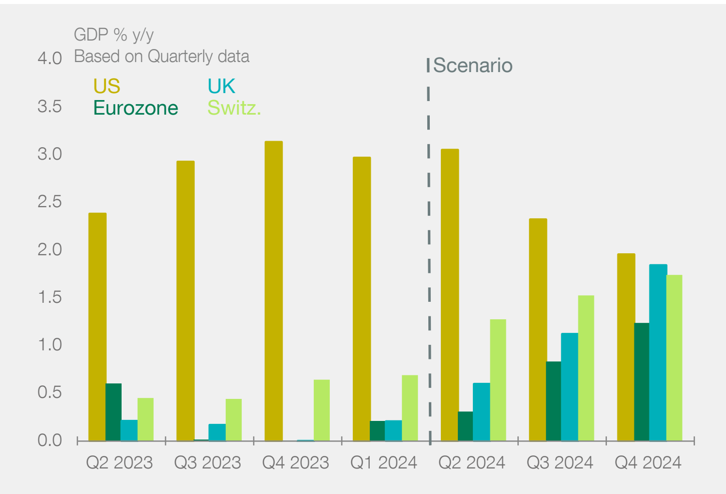
The Chinese authorities have unveiled new measures to stabilise the property sector by reducing financing costs and rebalancing the market. These decisions provide a floor for the sector, but further measures should underpin a long-term boost to consumption.

EUROPE EMERGING FROM STAGNATION

European countries are finally emerging from a long period of recession and stagnation. GDP growth in the first quarter was stronger than expected in both Germany and the United Kingdom (UK). As a result, growth forecasts for 2024 have been revised upwards from 0.3% to 0.8% for the UK and from 0.5% to 0.7% for the eurozone.

The rebound in the first quarter is set to continue, and the recovery in growth is expected to gain momentum in the second half of 2024. Household confidence is recovering in all countries and consumption is picking up as purchasing power improves. Public spending remains strong and continues to support economic activity. In Germany, consumption is slowly recovering but is still fragile, while exports to China are depressed. German growth is expected to be around 0.2%, up from -0.3% in 2023.

GDP GROWTH IN SELECTED DEVELOPED COUNTRIES



Sources: National statistics, UBP
Past performance is not a guide to current or future results. Any forecast, projection or target, where provided, is indicative only and is not guaranteed in any way.

US GROWTH EXPECTED TO NORMALISE

In the US, domestic demand continued to grow strongly in the first quarter (2.8%), while exports and falling inventories reduced GDP growth to a mere 1.3%. Our scenario favours a moderate slowdown in domestic demand and GDP growth of around 2% or slightly below in the second half of the year.

Consumption continues to be driven by job creation and purchasing power. The labour market is expected to rebalance, with fewer new jobs being created. As a result, consumption, which is already more focused on services than on the purchase of goods, is likely to be less buoyant in the coming quarters.

European central banks begin a rate-cutting cycle

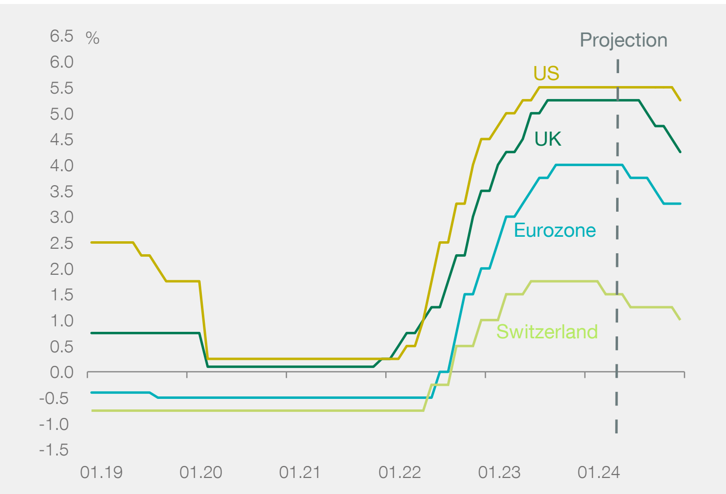
The recent rebound in confidence in industry is positive for the recovery of all components of investment, in addition to those linked to R&D and artificial intelligence.

This normalisation of growth does, however, present some uncertainties, with the risk of a sharper downturn in employment and activity or, in contrast, a reacceleration in services and industry.

EUROPEAN CENTRAL BANKS DISCONNECT FROM THE FED

Over the next few months European central banks are likely to cut rates before the Fed does. Disinflation is more advanced in Europe, giving the region's banks more room to manoeuvre.

MONETARY POLICY PROJECTION OF MAJOR KEY RATES



Sources: BloombergFinancial L.P., central banks, UBP
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The ECB is expected to make its first rate cut in June, followed by regular cuts in the second half of the year, bringing the deposit rate down to 3.25% by the end of the year. The Bank of England is expected to make its first cut in August and then reduce its base rate to around 4.25%, depending on wage moderation and services.

Last, the Fed is showing doubts about the restrictive bias of its policy and its effectiveness. Based on our inflation projection, the Fed might not cut rates before December unless there is a negative shock to employment or growth.

Strategy

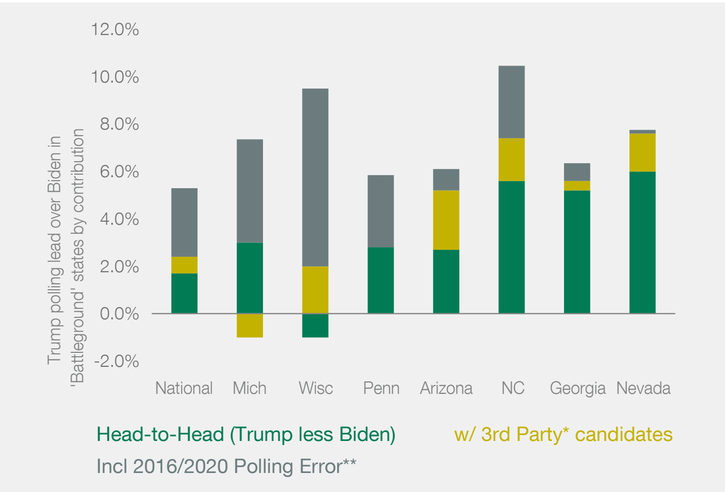
THE 2024 US ELECTIONS COME INTO VIEW

Investment returns during US presidential election years have been favourable for equity and credit investors outside recession years. This is consistent with our optimism on both asset classes amidst the current economic expansion.

The election landscape today favours former President Donald Trump, who leads incumbent President Joe Biden in recent polling. More importantly, however, Trump leads Biden in six of seven "battleground" states that either leading candidate will need to secure to win the White House. Recall both the 2016 and 2020 elections were decided by fewer than 100,000 votes in these states out of the over 136 million votes cast.

Taking into account historically significant polling errors in these states leaves open the possibility that these polls favouring President Trump are not only larger, but importantly outside the margin of error of the polls. Fortunately for Biden, since the March State of the Union address, these unfavourable polling gaps have begun to narrow.

FORMER PRESIDENT TRUMP LEADS CURRENT PRESIDENT BIDEN IN 6 OF THE 7 KEY 2024 BATTLEGROUND STATES



Sources: 270towin.com and UBP.
* Including Robert F. Kennedy Jr, Jill Stein, and Cornel West
** Polling error = actual voting result less last poll in 2016 and 2020
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Investors should capitalise on strong returns in the run-up to the US election and then, entering autumn, focus on managing risk via gold

Admittedly, the recent guilty verdicts delivered against Donald Trump by a New York court have the potential to tighten the former president's lead, especially in key Midwestern battleground states, narrowing his own potential paths to victory while opening up avenues for his rival, President Biden, despite his poor presidential approval ratings.

Indeed, President Barack Obama's recovery from low popularity and weak polling in 2011 to hold on to the White House in 2012 provides a potential campaign template for President Biden in the run-up to election day in November 2024. The Biden administration has already begun to deploy fiscal and legislative measures to mimic the Obama strategy. Though unclear whether they will be successful, for investors, these actions should be a tailwind to growth and, looking further afield, potentially to inflationary pressure in 2025.

Being overlooked in the 2024 US presidential campaigns are US fiscal challenges which will constrain the eventual winner of the coming election. The US debt ceiling is set to cap bond issuance once again in January 2025, forcing difficult revenue and spending trade-offs on the new US leader in his first days in office, triggering, we expect, potential interest rate, equity and currency market volatility.

Therefore, with less than six months until the US presidential election, investors should position themselves to capitalise on the tailwinds to returns in equity and credit in the run-up to the election and then, entering autumn, focus on managing risk and pivoting to active sector, stock and currency selection as the prospective winner becomes clear moving into 2025. Gold and inflation-linked bonds should offer attractive protection against potential volatility around the transition into 2025.

Asset allocation

1

Global bonds, hedge funds and gold all contributed positively during the month

2

We initiated a position in European AT1s and slightly increased our exposure to emerging market debt instruments

3

We tactically downgraded our level of conviction on the global technology sector

CONTINUED ADJUSTMENT TO OUR FIXED INCOME EXPOSURE

In May, global equities recovered from the weakness seen in April, with the MSCI World index rebounding +4.5% and the benchmark US index, the S&P 500, reaching an all-time high. The rebound in equities was associated with softer US economic data which led to lower inflation expectations. However, gains continue to be led by a handful of companies, with the S&P 500 outperforming its equal-weight index for the fifth consecutive month (+5.0% vs. +2.8%) and the Magnificent 7 climbing +9.1% (propelled by strong quarterly results and guidance from heavyweight Nvidia). Global bonds, hedge funds, and gold all contributed positively during the month, with performances of +1.2%, +0.5% and +1.8%, respectively.

Overall, we did not change our asset allocation during the month, however, we adjusted our fixed income exposure to better match our macroeconomic expectations. With no recession in sight in the US, merely a slowdown, and considering the elevated risks in long-duration bonds ahead of the US presidential elections, we maintain our short-duration positioning of 3.2 years for a balanced USD portfolio, while maximising yields. Therefore, we initiated a position in European AT1s and slightly increased our exposure to emerging market debt instruments.

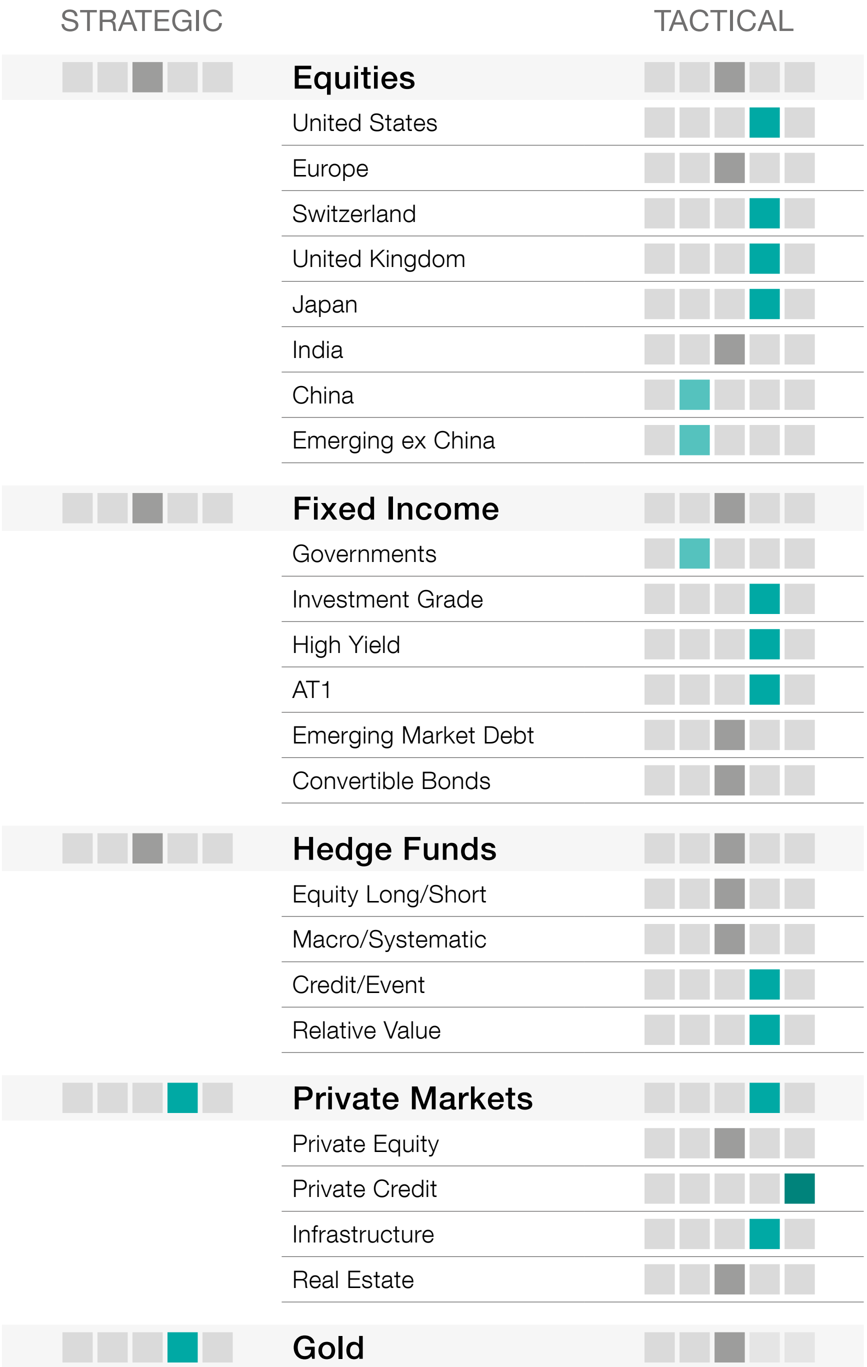
Regarding equities, we tactically downgraded our level of conviction on the global technology sector from 5 to 4 following a slowdown in revenue growth and weaker-than-expected guidance from Q1 earnings reports, notably from software companies such as Salesforce, Workday, and MongoDB. While the S&P 500 Information Technology Index is up +17.0% this year, there is a wide divergence in performance at sub-sector level, with the S&P Semiconductors Index soaring +57.0% so far this year, while the S&P Software & Services Index is up just +2.2%. Overall, earnings growth in large-cap technology names is set to slow from record-high levels (68.0% in Q4 2023) and normalise (to 15.0%) by the end of the year. This underpins our lower short-term level of conviction towards the space.

Directional views

LOW CONVICTION | BASE LINE ALLOCATION | HIGH CONVICTION

PREVIOUS VIEW ● (no dot means no change)

Strategic (long-term view) and tactical (1–6 month) on broad asset classes, June 2024



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Asset classes

EQUITIES

LOWERING OUR LEVEL OF CONVICTION ON US TECHNOLOGY

After having broadened (across both regions and sectors) in previous months, equity market gains in May returned to a concentrated nature with the technology sector driving the majority of the month's return: MSCI World +4.5% vs. MSCI World Technology +8.7%. The latter has been strongly supported by remarkable first-quarter earnings from Nvidia, which exceeded analysts' elevated expectations. Nvidia alone now accounts for a quarter of the US equity market performance so far this year. Emerging markets, Japan, and China underperformed, with gains of 0.6%, 1.2%, and 2.4%, respectively.

Looking ahead in June, we believe investor's attention is set to turn to the most significant political event of the year: the US presidential election. The first debate between President Biden and Republican presidential candidate Donald Trump is scheduled for the end of the month and is likely to overshadow recent investor concerns about inflation and interest rates. We believe the election outcome will likely have substantial implications for various regions, sectors, and investment styles, potentially leading to increased market volatility in the near term. However, any pick-up in volatility ahead of the US elections should be seen as an opportunity to add risk to portfolios.

In May, we maintained our existing portfolio convictions (tactical bets on UK and Swiss equities, core positions in US and Japanese equities). After a strong year-to-date outperformance, we are taking the opportunity to slightly downgrade our conviction level on the global technology sector from 5/5 to 4/5. This adjustment reflects an anticipated slowdown in earnings growth for large-cap technology companies and the recent disappointing figures/guidance from software firms on the back of longer sales cycles, weaker demand from smaller businesses, and increased AI investments impacting margins.

FIXED INCOME

NARRATIVE SHIFTS FROM CAPITAL GAINS TO CARRY

Given persistent inflation and a robust macroeconomic environment, we have shifted our expectations on fixed income returns primarily towards carry. Accordingly, we are repositioning portfolios to favour a shorter duration (3.2 years). The rate-cutting cycle should act as a catalyst to restore a positive slope to the yield curve. To maximise carry, we maintain a relatively low exposure to sovereign bonds, favouring investment-grade bonds and flexible funds. We have also recently added exposure to AT1s of major European banks and increased exposure to emerging market debt with a focus on sovereign bonds.

CONVERTIBLES

PRIMARY MARKET ACCELERATING

The convertible bond market resumed its upwards march in May as the various performance engines contributed positively. However, the main highlight of the month is the number of primary deals: more than USD 18 billion were issued globally, with a large majority coming from the US. The last time we had such a volume of deals in a month was in March 2021, well into the buoyant 2020/2021 cycle. The most publicised deal came from Alibaba (bond convertible into US ADR) with USD 5 billion issued in a single tranche. This is the largest plain vanilla convertible bond issued since 2003 and the largest ever convertible bond from an Asian issuer. This amount of new paper has not significantly weighed on the existing market's valuation, proving the current level of overall demand for the product.

CURRENCIES

THE GOLDILOCKS DOLLAR

Coming into June, the USD has weakened very slightly. US data have been mixed, resulting in a "not too hot, not too cold" reaction from markets to the USD. This Goldilocks scenario is conducive to the outperformance of high-beta currencies such as the AUD, NOK, and even the GBP.

Funding currencies have continued to weaken, in line with carry trade outperformance, presenting upside risks to both the EUR/CHF and the USD/CHF in June.

HEDGE FUNDS

ATTRACTIVE RISK-ADJUSTED PERFORMANCE

After some volatility in April, both equity and credit markets rebounded strongly in May and the most directional hedge funds were able to perform in line with their beta or better. Global macro funds experienced mixed results as several key markets in fixed income, currencies and commodities took a pause or even reversed course. So far, this risk-adjusted performance remains very attractive for hedge funds.

As the range of outcomes on US rates has widened, global macro managers have generally reduced strategic trades for more tactical and short-term ones, with lower risk at portfolio level. In addition to rising markets, managers in both credit and equities continue to benefit from dispersion triggered by disappointing earnings or refinancing issues. Overall positioning has not materially changed among quantitative macro managers, with a high level of directionality on several markets, and we remain cautious on this strategy in the short term. Indeed, with such a positioning, the potential protection they generally provide in a correction could be challenged. Overall, we continue to favour managers with low net exposures and balanced portfolios who are well placed to benefit from dispersion and idiosyncratic opportunities in a wide range of markets.

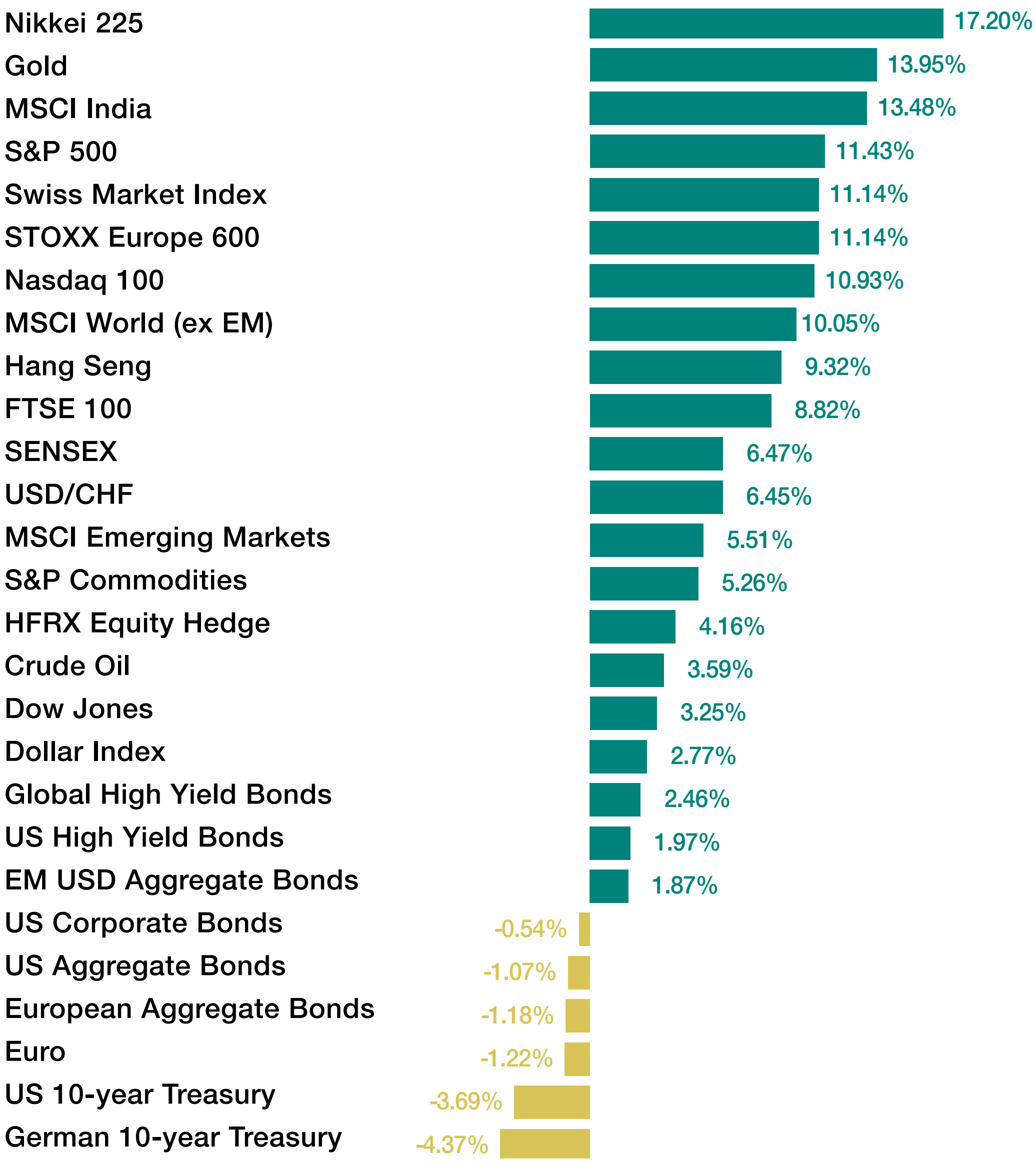
PRIVATE MARKETS

PRIVATE MARKETS: SOME TURBULENCE IN THE AIR

Private equity and private credit came under the spotlight recently after some negative news hit the wires. A large private equity shop had to write off a recent take-private, as the company was unable to service its debt, despite it having been issued at lower rates than today. It was also reported that after NAV loans, another engineering bid came to light in the form of synthetic payment in kind (PIK), allowing lenders to work around their limits on the amount of PIK they can have. Last, in real estate, the bifurcation between grade-A quality assets and lower-quality assets continues to dominate, with tenants focusing mostly on grade-A assets. The anchoring of higher rates will continue to create dispersion within private markets, advocating for thorough manager selection and robust portfolio construction. Medium-to-long-term investors continue to find the environment compelling as a means of building exposure to this asset class.

Market performances

2024 YEAR-TO-DATE RETURNS (%), DATA AS AT 3 JUNE 2024



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