Global Investment Strategy

Third Quarter 2024

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Overview

World economy and capital markets

- Economic growth is positive in the major global regions, despite some soft segments (e.g. European industry, US property market).

- After a stronger than expected first half of the year, economic momentum is likely to slow slightly in the second half of the year, particularly in the US, without this questioning the economic expansion. Europe's economy is characterized by restraint among consumers and businesses, though fundamentals would suggest upside potential.

- According to the polls, the French elections will see a shift in power, which now appears priced in.

- Monetary policy will continue to be guided by economic data, though interest rates will eventually fall. The backdrop for bonds thus remains positive, notably for medium maturities.

- The overall news flow regarding the economy and inflation has remained just about supportive for the stock markets. A slight economic slowdown in the US implies a certain susceptibility to corrections, which would correspond to the normal pattern in the summer months. An end to the economic and stock market cycle nevertheless does not seem likely.

Agenda

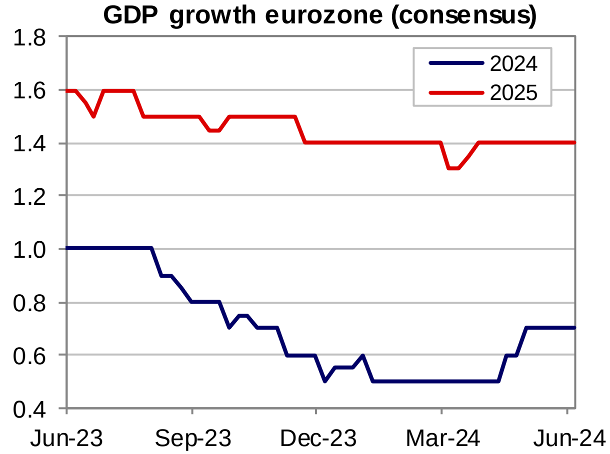
Consensus estimates: Positive overall

The consensus estimates are calculated as the mean value of the forecasts by leading forecasters.

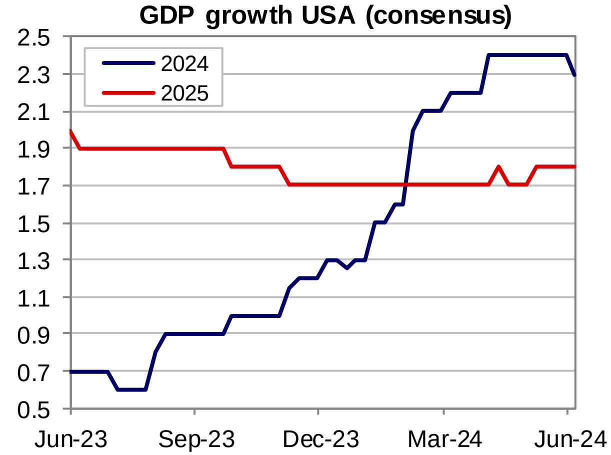
GDP growth expectations for the US for this year have risen significantly in recent months. Also the 2024 inflation forecast is now a bit higher than at the beginning of the year.

Following positive GDP growth in the first quarter, the 2024 growth forecast for the euro area has been raised somewhat. The inflation forecast has remained unchanged.

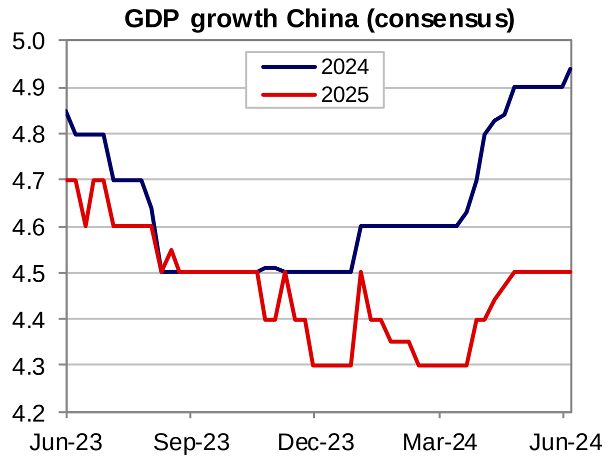
In China, economic growth forecasts for 2025 are at a realistic level of around 4.5%, with revision trends for both this and next year positive in recent months.



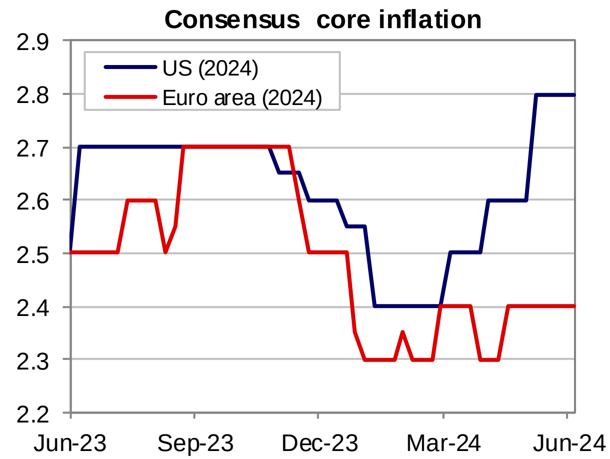
Source: Bloomberg indices



Source: Bloomberg indices



Source: Bloomberg indices



Source: Bloomberg indices

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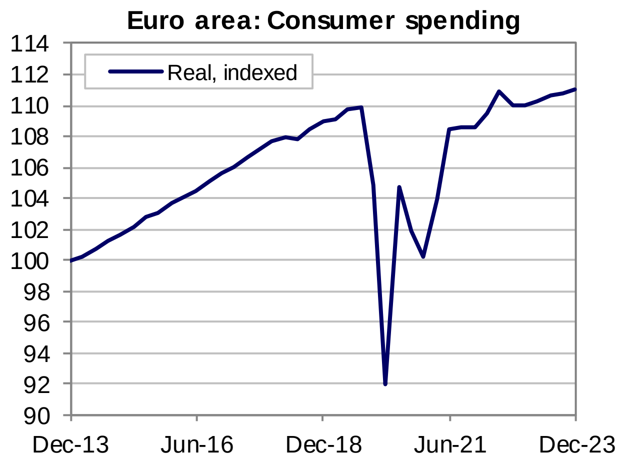
Europe: Reluctant consumers

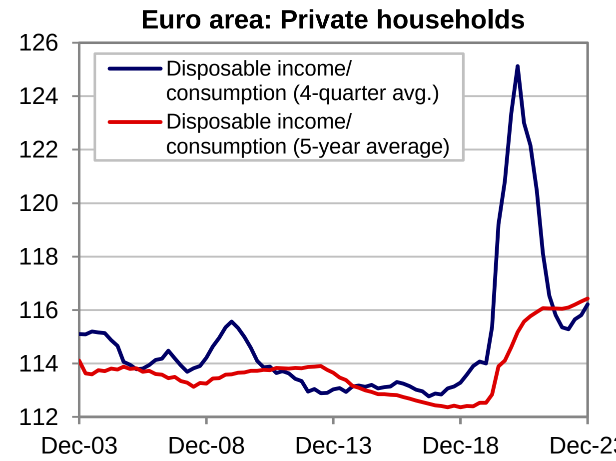
Private consumption is currently well below the pre-pandemic trend. Indeed, euro area consumers in the euro area are more reluctant to spend than the fundamental data would suggest.

The unemployment rate in the euro area is at its lowest level since measurements began, and real disposable incomes are currently rising significantly due to wage growth exceeding inflation. In addition, a high proportion of fixed-rate mortgages limits the impact of the increase in interest rates on the cash flows available for consumption.

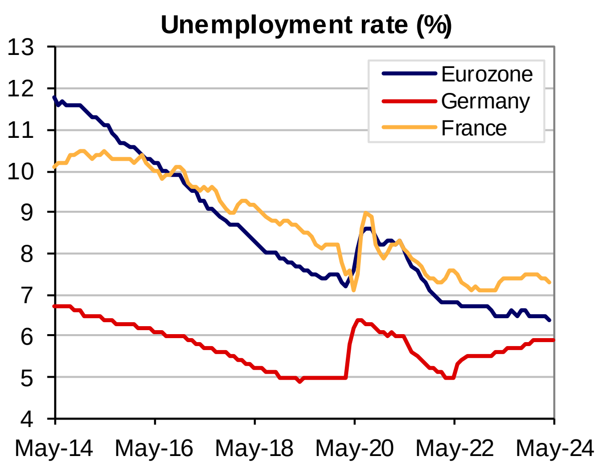
Overall, the fundamental constellation suggests that there is potential for a recovery in private consumption in Western Europe.



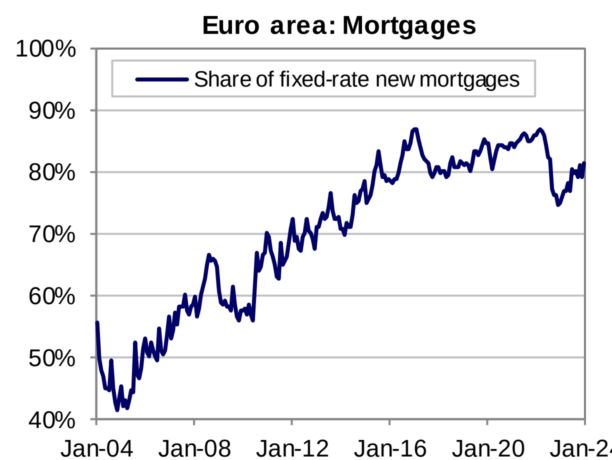
Source: Eurostat



Source: European Central Bank, Eurostat



Source: Eurostat, Deutsche Bundesbank



Source: European Central Bank

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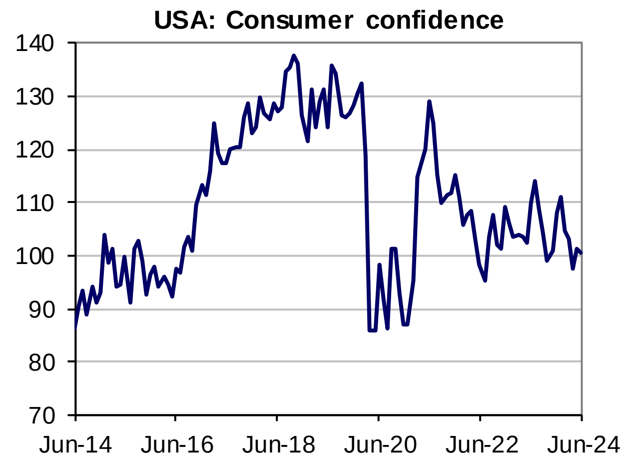
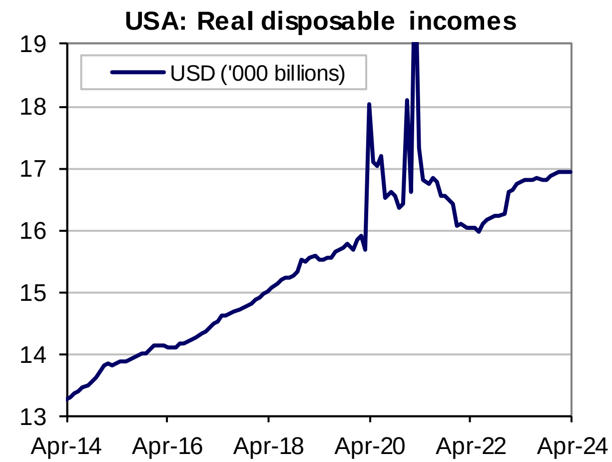
USA: Forces driving consumer spending

The pandemic continues to reverberate in US private consumer spending (there are still excess savings available, and a lot of households refinanced their fixed-rate mortgages at record-low rates during the lockdowns).

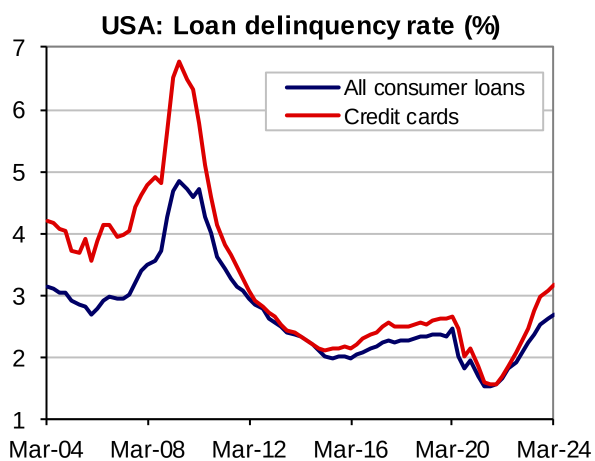
In contrast, real disposable income is currently below the pre-pandemic trend and growth is soft.



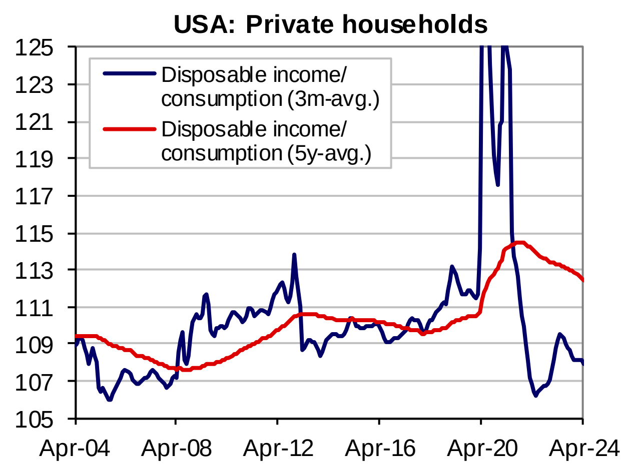
Source: Conference Board



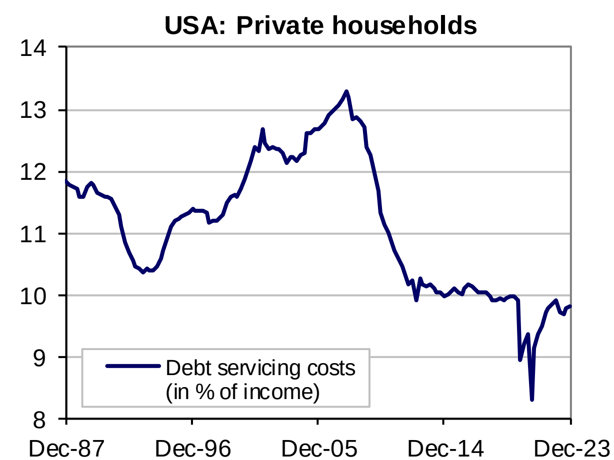
Source: Bureau of Economic Analysis



Source: Federal Reserve



Source: Bureau of Economic Analysis



Source: Federal Reserve

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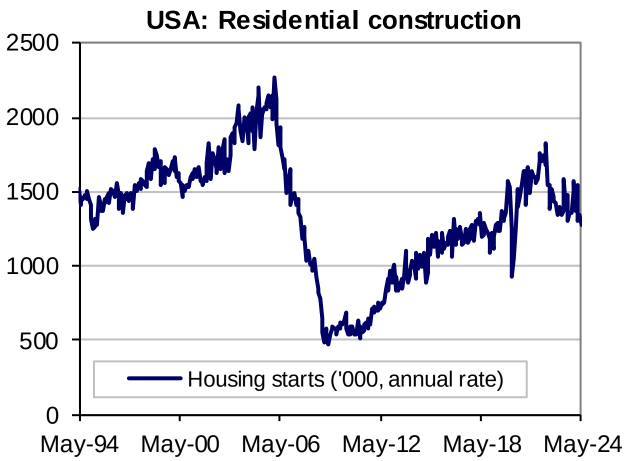
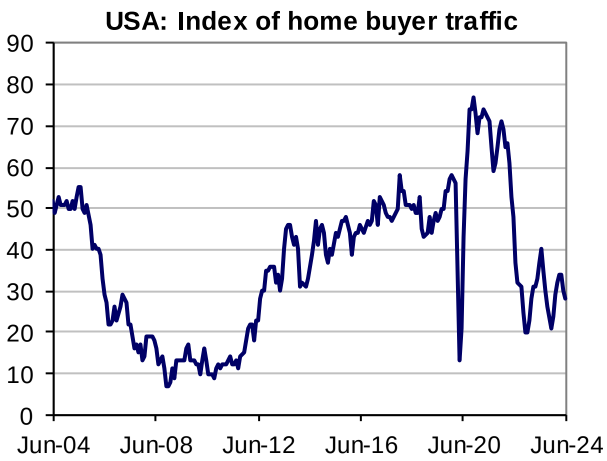
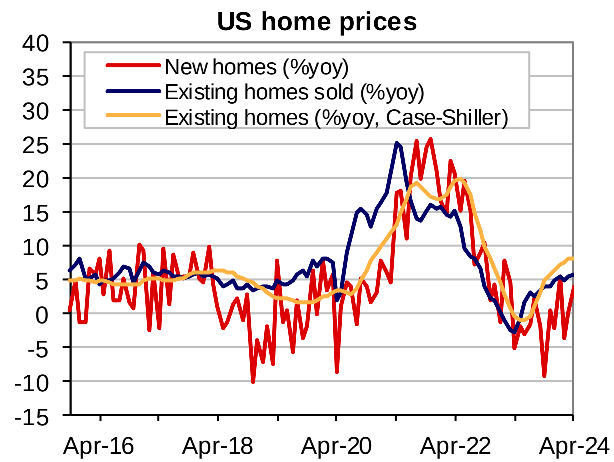
USA: Real estate trends modest, but not weak



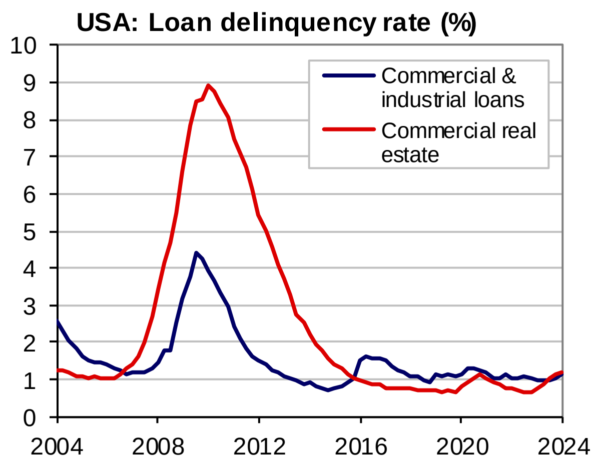
Source: US Census Bureau



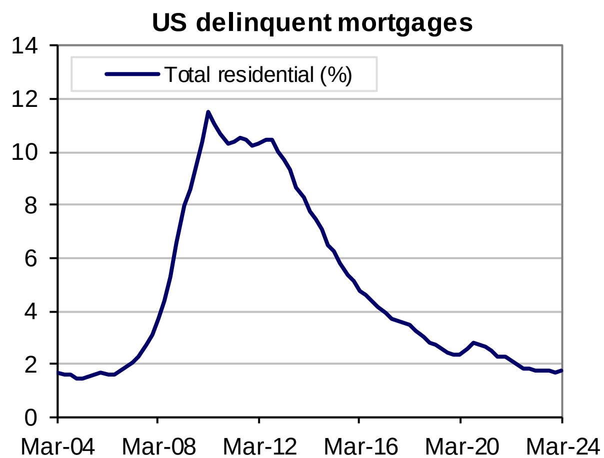
Source: National Association of Home Builders



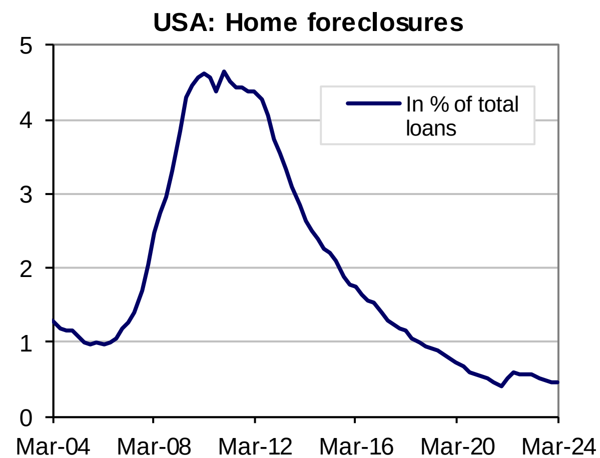
Source: US Census Bureau, Ass. of Realtors, Case-Shiller



Source: Federal Reserve



Source: Federal Reserve



Source: Mortgage Bankers Association

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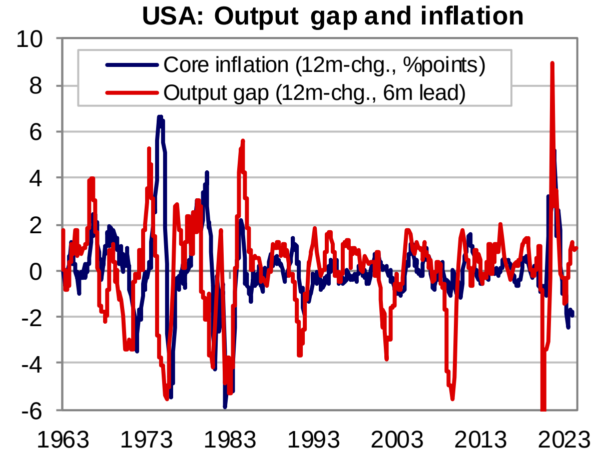
Inflation: Capacity constraints are the key factor

The chart "Output gap and inflation" shows the year-on-year change in inflation (in percentage points) and, as a measure of capacity constraints, the output gap (the 12-month change, 6 months ahead). A rising output gap means that there are more capacity constraints, and firms are more likely to raise prices than when demand softens. The chart shows that changes in the output gap determine inflation with a lag of about 6 to 18 months, with a very short lag during the pandemic, likely due to extreme bottlenecks surfacing very quickly.

The correlation has been strikingly stable over the last six decades. It is worth noting that the output gap and inflation recorded greater swings in the period from 1960 to the mid-1980s than after 1990, which would explain the lower inflation since the 1990s without having to resort to moderating factors such as globalisation.

The economic cycle is therefore a good indicator of inflation. In particular, an inflationary overheating of the economy is not always the result of an excessively loose monetary policy. It can also be caused by government stimulus measures (as in the US during the pandemic).



Source: BLS, Congressional Budget Office

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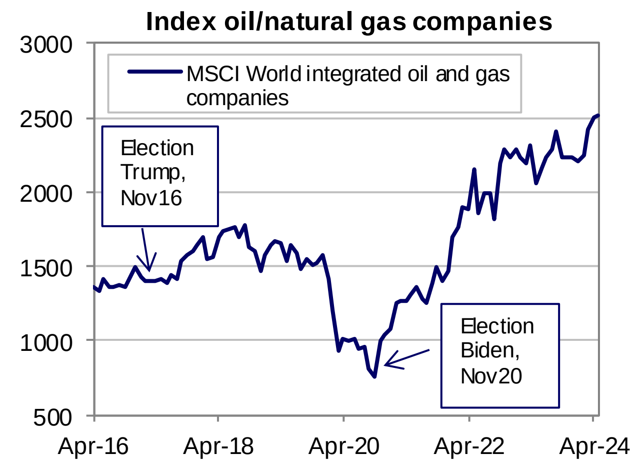
Energy: Fossil fuels vs. renewables

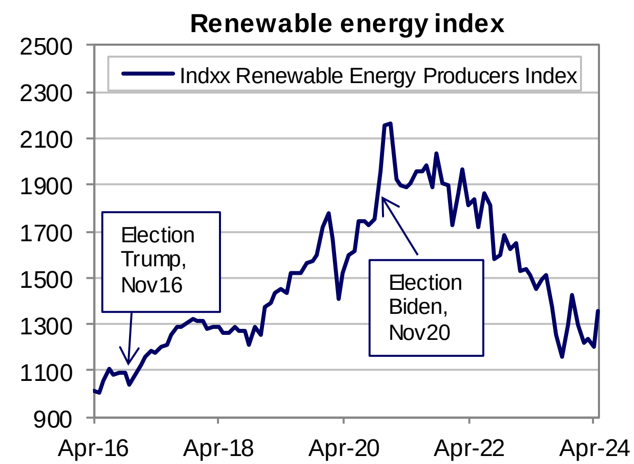
Under Donald Trump, who was elected president in November 2016, the fossil fuel industry experienced an improvement in its competitive position thanks to political support and deregulation. Although the broad MSCI World Integrated Oil and Gas Index rose slightly thereafter, the increase was more pronounced during Joe Biden's term in office (also corrected for the slump during the pandemic).

Renewable energies, as measured by the Indxx Renewable Energy Producers Index, achieved significant price gains during Trump's presidency despite a lack of political support. After a brief rise immediately after the election of Joe Biden – a clear supporter of the expansion of renewables – the index experienced a brief spike, but then delivered a negative performance in an overall positive market environment.

It can generally be concluded that a focus on US politics for a global equity sector outlook rarely delivers results that are easy to implement and decisive for performance.



Source: MSCI



Source: Soloactive

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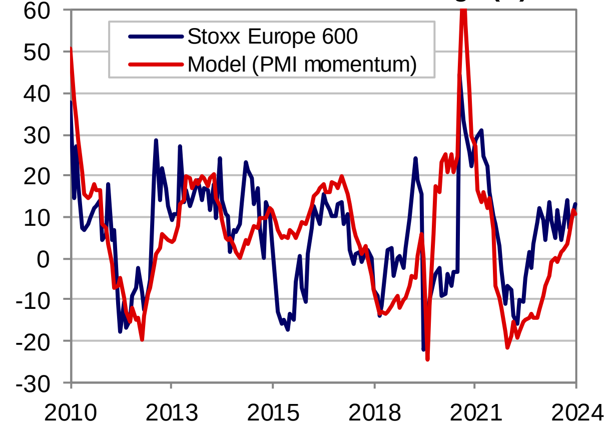
Chapter 7: Equity markets – Economic momentum key factor

In the wake of the improved economy (see the charts), stock markets have performed well for nearly two years, especially in comparison to bonds.

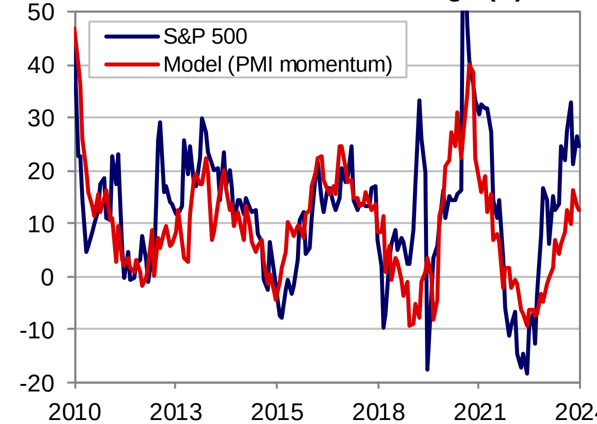
In a mature bull market, there is always a certain susceptibility to corrections, notably in the often comparatively weak summer months. The news flow regarding the economy and inflation, however, has remained modestly supportive in June.

Stoxx 600: 12-month change (%)



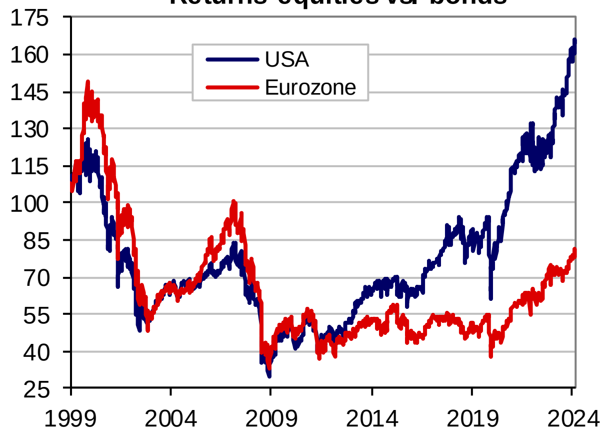
Source: S&P Global, Stoxx, own calculations

S&P 500: 12-month change (%)



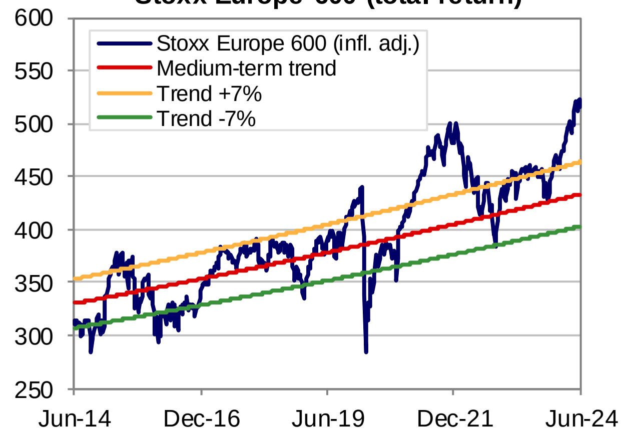
Source: ISM, S&P Global, own calculations

Returns equities vs. bonds



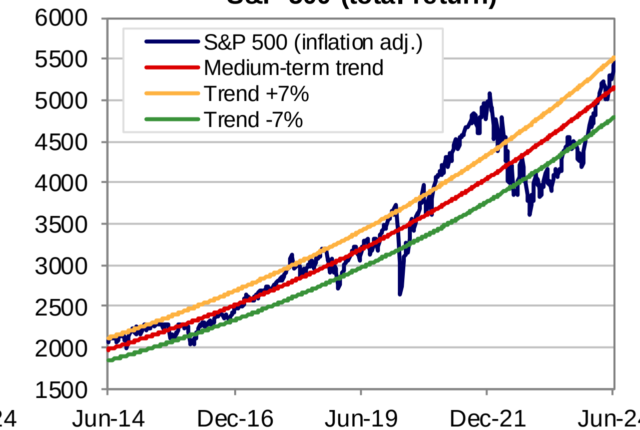
Source: S&P, STOXX, Bloomberg, own calculations

Stoxx Europe 600 (total return)



Source: Stoxx, Eurostat, own calculations

S&P 500 (total return)



Source: S&P Global, BEA, own calculations

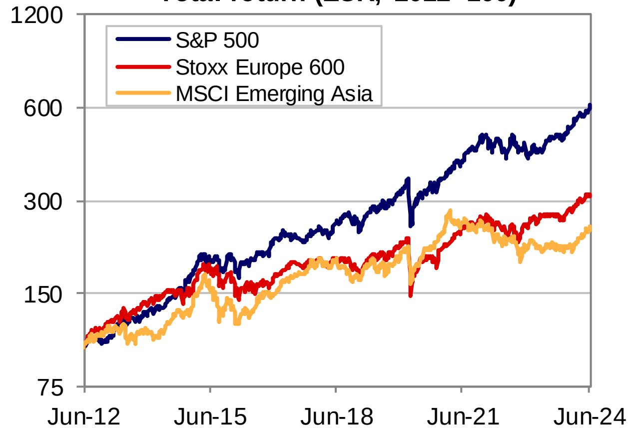
Regional trends: Technology weighting is key

The US stock market (S&P 500) outperforms Europe and the Asian emerging markets in terms of corporate earnings and returns over the long term. The US market is more defensive than Europe (e.g. a lower weighting of financial companies). When technology stocks and technology-related sectors outperform, the US market has a clear advantage (weighting of around 40%, compared to less than 10% in Europe).

The conditions for outperformance in Europe, where value stocks are over-represented, include a good global economy, high bond yields (positive for financials) and rising commodity prices.

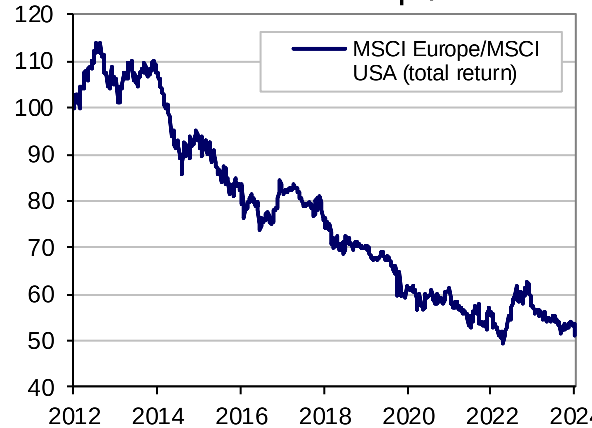
Based on free cash flows, Europe has been valued more favourably than the US since 2022. However, a favourable valuation alone is unlikely to be enough for outperformance.

Total return (EUR, 2012=100)



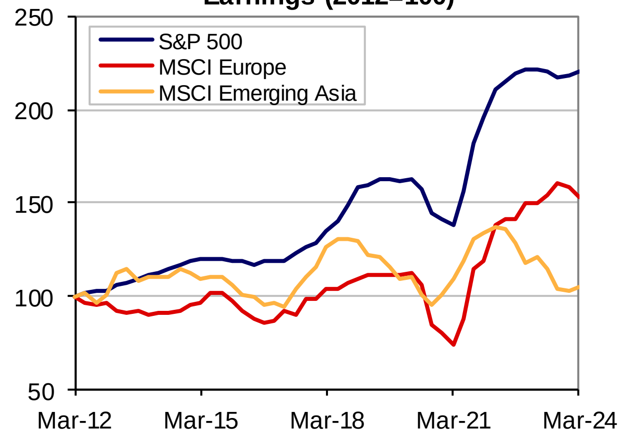
Source: S&P, STOXX, MSCI

Performance: Europe/USA



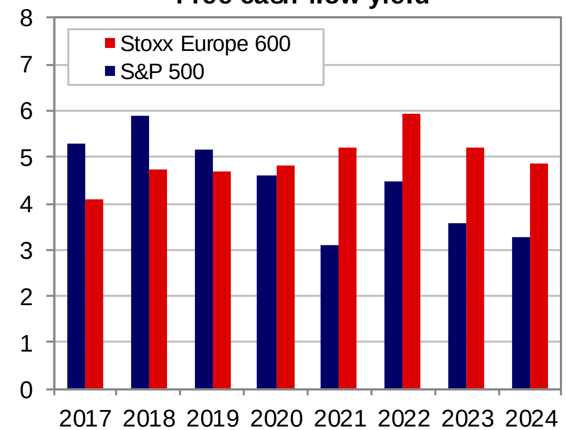
Source: MSCI

Earnings (2012=100)



Source: S&P, MSCI

Free cash flow yield*



*Key sectors. Source: Own calculations

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Data sources in charts or tables that are not specifically mentioned are either companies or index provider.

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