MFM
MIRANTE FUND MANAGEMENT

Market Overview

JULY 2023

We believe in active management based on a structured investment process to ensure optimal diversification in terms of asset classes, types of financial instruments and geographic sectors. Risk management is an investment tool fully integrated into the portfolio construction process.

The benefits of this approach are numerous: the reduction of risk against significant market declines, as well as the potential to create increased value over the long term.

Frank Crittin, Chief Investment Officer

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STUBBORN MARKETS

Stubborn is undoubtedly one of the words that best characterize the financial markets since the beginning of the year. Indeed, despite rising inflation and the first shocks associated with the spectacular rise in interest rates, the main asset classes have experienced strong positive performances. The Nasdaq even posted a stunning return of more than 30%. This was the best start to the year since 1983. The technology giants and the enthusiasm generated by artificial intelligence were the main drivers of this performance. The last month of the semester was just as promising as the beginning of the year. Despite colossal macroeconomic uncertainty, investors demonstrated their optimism, pushing all asset classes in the right direction.

At the equity level, all regions observed positive performance. China, which has been disappointing investors since the beginning of the year, took advantage of rumors of impending economic stimulus to recover a little. However, Chinese consumers continue to remain underwhelmingly low spenders. Indeed, the number of trips during the last national holiday increased significantly, but spending remained below expectations. This, combined with a persistently moribund real estate market, is generating sluggish growth. Conversely, Japan continued its march forward. The return of inflation combined with an ultra-accommodating monetary policy continues to push investors to buy. At the sector level, those considered defensive continue to be shunned by investors. They posted positive performances, but far behind growth sectors.

In fixed-income, convertible bonds benefited from investors' risk appetite and their sensitivity to the equity premium to post a robust performance. This very attraction to risk enabled high-yield bonds and those of emerging countries to generate favorable returns.

MACROECONOMIC OUTLOOK AND INVESTMENT STRATEGIES

At the start of the second part of the year, the remarkable performances of the major asset classes come up against a particularly uncertain economic context. The biggest uncertainty relates to overall growth. US growth is slowing, but for the moment, its economy can withstand this parabolic rise in interest rates without generating a recession in the short term. Europe is technically already in recession, yet its central bank has announced that it will continue to raise rates. Chinese growth is less strong than expected and could be stimulated more intensely.

Consequently, overall growth should remain positive in the short term, but what about the medium term? Once again, the time horizon profoundly changes the outlook. In the medium term, for equities to continue to offer positive performance, it is necessary that company profits increase. Earnings estimates have stopped falling recently and are now even being revised upwards. However, if inflation increases revenue in the short term, it can impact margins in the medium term. For now, a relatively small number of companies have observed this, however, if inflation sets in, this fear will return to investors.

Regarding interest rates, it is highly likely that they will remain high. The Fed and the European Central Bank continue to raise rates but are approaching the end of their hike cycles. In terms of inflation, again, the time horizon is crucial. In the short term, it will continue to decline to anchor itself at its equilibrium level. If this anchor point is higher than the «magic» 2% targeted by central bankers, two scenarios are possible.

1) Either the central banks remain inflexible and continue to raise rates in order to force the economy

to slow down and consequently bring down inflation. The risk is clearly a severe recession.

(2) Or the central banks decide to let inflation settle at a higher level in order to avoid generating a recession to bring it down. This scenario, offering higher inflation until the end of the cycle, would have significant consequences for the construction of portfolios and for the expected returns of the various asset classes.

At the allocation level, our «World Equity Risk Premium» indicator continued to decline during the month, driven by the increase in interest rates combined with the strength of equity markets. This indicator justifies an allocation to bonds versus equities. It should be noted that in the first half of the year, investment grade bonds once again provided a shield during weaker periods in the equity markets. This is positive news for all of our multi-asset strategies.

The spectacular year-to-date performance of equities has been driven primarily by rising valuations. Corporate profits will have to grow in the second part of the year to confirm this performance. It's clear that the impact of artificial intelligence on business productivity and profits is real but will take quite some time to materialize. Therefore, a cautious approach seems rational because of the risks linked to global growth and the potential pressure on companies' margins. At the regional level, while it is clear that China is slowing down (or rather growing more slowly), attention is now focused on the responses provided by the Chinese government and its central bank. They have already announced measures to support household consumption and increase infrastructure spending.

At the bond level, the duration risk (i.e. sensitivity to interest rates) is lower than in the past, but remains harmful as long as the central bankers have not stopped their rate hike cycle. This is why we are keeping durations low in all of our investment strategies. Moreover, as the higher rates allowed this asset class to regain its defensive character during market corrections, it does not seem wise to increase our exposure to long maturities. For credit risk, we maintain an approach focusing on quality by diversifying our exposures in terms of business sectors and regions.

In a very uncertain environment, well-controlled diversification, in terms of asset classes and investment premiums, makes it possible to build resilient approaches while optimizing the risk-return trade-off. In addition, these strategies ensure that the portfolios withstand a wide range of possible scenarios, both at the macroeconomic level and in terms of performance of the main asset classes.

HARRY MARKOWITZ, ECONOMIST, 1927-2023

- **Harry Markowitz, who received the Nobel Prize in Economics in 1990 for his work on portfolio theory, died at the age of 95 on June 22.**
- **Markowitz will remain the father of modern portfolio theory, which revolutionized portfolio management. Through his research, he demonstrated why investors should diversify their investments by using combinations of assets rather than focusing on individual securities. He explained that the risk of a portfolio depends less on the degree of risk of the shares (and other assets) that make it up than on how they are linked to each other.**

MAIN DRIVERS SUMMARY

GLOBAL GROWTH

- Developed economies will slow down; the central question remains how deep these downturns will be.
- In the United States, the unemployment rate remains at an extremely low level, consumers continue to spend and the housing market begins to stabilize, for the moment a deep recession is not on the agenda
- Europe is technically in recession and the central bank promises to keep raising rates…
- Chinese growth is not as strong as expected at the end of the Covid. The government is likely to stimulate its economy in order to achieve the 5% growth target.

PROFIT GROWTH

- The spectacular performance of equities since the beginning of the year has come mainly from the increase in valuations. Corporate earnings will need to rise in the second half of the year to confirm this performance.
- In 2024, a large proportion of companies will have to refinance at significantly higher costs.

INFLATION

- Overall, rising service prices are now driving inflation in most countries around the world.
- Some forces driving inflation higher could strengthen, including optimizing supply chains, decarbonization and defense.
- In the longer term, the forces pushing inflation down remain demographic and productivity gains.
- Could central bankers accept interest rates permanently above 2% to avoid destabilizing the economy?

INTEREST RATE

- A slowdown in the economy should mechanically dampen inflation... and thus reduce the pressure on interest rates.
- Probably"higher for longer", the Fed and the European Central Bank continue to raise rates but are nearing the end of their hike cycles.
- QT (quantitative tightening) is likely to create only moderate pressure on long-term rates.

SOURCE: MFM, July 2023

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MONTHLY PERFORMANCE, 30TH JUNE

Equities Market (Local currency)

Japan	7.69
United States	6.63
World (all countries)	5.69
Europe	4.79
China	4.40
Emerging Markets	3.45
Asia (ex-Japan)	2.91
United Kingdom	1.25
Switzerland	0.41

Equities Sector (Local currency)

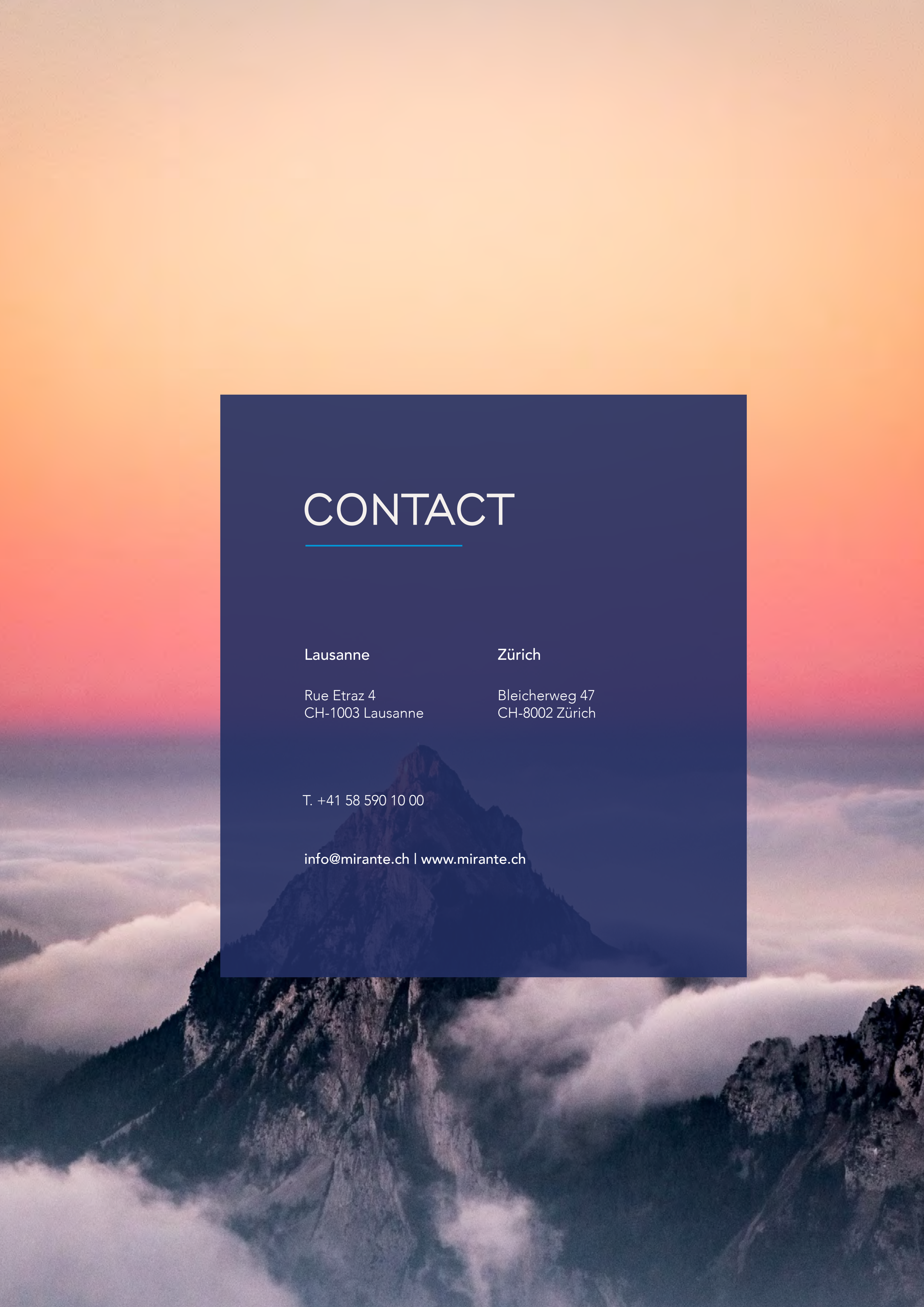
Consumer Discretionary	10.28
Industrials	8.73
Materials	7.07
Information Technologies	6.14
Financials	5.87
Energy	5.50
Real Estate	3.90
Health Care	2.77
Telecommunication Services	2.70
Consumer Staples	2.58
Utilities	1.78

Fixed-Income (USD Hedged)

Global Convertibles	3.79
Global High-Yield	2.12
Emerging Market Hard Currency Aggregate	1.29
Global Aggregate Long Duration	0.78
Global Corporate Credit	0.13
US Treasury Long Duration	-0.02
Swiss Bond Index AAA-BBB (CHF)	-0.03
Global Aggregate	-0.06
Global Treasury	-0.07
Global Aggregate 1-3 Year	-0.14
Global Inflation-Linked Bonds	-0.35
Global Aggregate 5-7 Year	-0.48

Others (USD)

Commo Global (ThomsonReuters)	2.30
Hedge Funds	0.44
Commo Industrials (CBR)	0.04



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