MIRANTE FUND MANAGEMENT

Market Overview

DECEMBER 2023

Lac d'Emosson, Switzerland

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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INVESTORS NO LONGER BELIEVE CENTRAL BANKERS

Although central bankers insist they are reluctant to consider rate cuts, investors think they are on the wrong track. Investors seem convinced that the US Federal Reserve (Fed) and the European Central Bank will be forced to cut rates in the coming year. In anticipation, long rates therefore fell sharply during the month. This has contributed to the increased risk appetite in financial markets in recent weeks. This optimism has been exacerbated recently by the confirmation of the overall slowdown in inflation and economic growth. In November, global financial markets experienced a remarkable rebound.

Bonds (as measured by major global indices) have had one of the best monthly performances in decades. They weren't the only ones invited to the party. Global stocks also thrived, with benchmark indices posting impressive gains of over 8% for the month. This euphoric behavior underlines the short-term importance of investors' expectations on the performance of financial assets.

At the equity level, Europe achieved the best regional performance, thanks to a significant drop in inflation and a notable reduction in the risks of a new energy crisis. China lagged behind, but still recorded a positive performance for the month. Its economy is slowly recovering, but stimulus measures are not enough to generate investor enthusiasm. The growth sectors were the best performers. The robust results of these companies and the reduction in interest rates have led to a mechanical increase in their valuation. In addition, the listed property market was strong, also benefiting from the impact of falling interest rates. The only sector remaining in negative territory was energy, negatively impacted by the drop in oil prices, despite the crisis in the Middle East. Weakening Chinese demand could explain why oil prices remain unaffected by these geopolitical events. Duration (which measures sensitivity to interest rates) was the main driver of bond performance, with all long-duration assets performing strongly. Furthermore, raw materials suffered a decline during the month, largely attributable to weak oil prices.

LONG-TERM OUTLOOK: PARADIGM SHIFT FOR ALLOCATION STRATEGIES

The end of the Covid-19 crisis also marked the end of a long period of extremely low interest rates. Massive economic stimulus from governments has had a considerable impact on economies and consumption. This influx of liquidity, combined with the energy crisis caused by the war in Ukraine, led to an explosion in inflation and, in turn, interest rates across the planet. At the investment level, this had a significant impact on the performance of bonds and stocks, but it also affected their expected return. Now it seems we have come to the end of this cycle. It indeed seems unlikely that interest rates could rise much higher. The financial market consensus is betting more on rate cuts for the coming year.

Rising interest rates are starting to weigh on consumption and corporate profits due to rising financing costs. A decline in profits leads to a reduction in expected returns on stocks. This phenomenon is, however, offset by a significant increase in expected returns on bond assets. These two factors combined mean that our "MFM World Equity Premium" indicator remains at historically low levels. Indeed, the strong rebound in stocks in November was initiated, and therefore offset, by a general drop in interest rates. This premium measures the expected excess return that investors require for holding stocks rather than bonds which are considered less risky. It therefore confirms that it is essential to have exposure to bond investment premiums such as duration (sensitivity to interest rates) and credit (sensitivity to bankruptcy risk). This also results in an increase in the expected return on diversified approaches combining bonds and stocks, while making these strategies less risky. Although most market events frequently seem like incomprehensible noise, this paradigm shift in investing is significant for the majority of strategies.

SHORT - TERM OUTLOOK AND CRYSTAL BALLS

The Christmas baubles that hang on the trees are, for the most part, no longer made of crystal. They are therefore not particularly useful for predicting the future. However, this forward period is the preferred time chosen by most analysts to make their predictions. These forecasts cover the trajectory of the global economy, geopolitical events and the future performance of different financial assets.

Before jumping into predictions for the coming year, it doesn't hurt to look back. In 2023, despite extreme and continued increases in interest rates in the United States and Europe, and China bordering on a major crisis, global growth remained robust and inflation declined continuously. Financial markets remained surprisingly struggling to price in a unique mix of growth, moderate inflation and rising interest rates.

For the quarters to come, it seems clear that global growth will be the main driver of financial markets. Unfortunately, since economists have difficulty predicting the onset and extent of economic downturns, positioning investment strategies based on these forecasts would be clumsy. While developed economies have done better than expected in 2023, they are not out of the woods yet. Persistently high interest rates will have painful consequences for businesses and consumers, even if a recession is avoided. The global economy is therefore expected to remain vulnerable in 2024. Investment premiums for interest rates, credit and equities should theoretically surpass those for cash. This justifies a balanced allocation between these different premiums with an emphasis on portfolio resilience. It does not seem appropriate to take strong directional bets, but we should not hesitate to take advantage of peaks of nervousness to diversify and add quality investments at possibly more advantageous prices.

CITATION OF THE MONTH

I can live with doubt and uncertainty and not knowing. I think it is much more interesting to live not knowing than to have answers that might be wrong.

Richard Feynman (1918-1988), American physicist.

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KEY MARKET DRIVERS

GLOBAL GROWTH

- Growth will likely be the determining factor in the performance of financial assets in the coming quarters.
- Third-quarter US growth was revised to 5.2%. A staggering figure given the rise in rates and inflation. But consumption, inflation and the job market have all cooled.
- In Europe, economic activity is in contraction, as is inflation. Germany has shown encouraging signs in recent weeks.
- Despite some positive signs related to economic stimulus from Beijing, the Chinese economy remains faltering. The real estate sector, still under pressure, still represents more than 20% of the country's GDP.

COMPANY PROFITS

- The current earnings season has shown encouraging signs. Growth companies have clearly benefited from positive surprises from large technology companies.
- Conversely, companies displaying unsatisfactory results were heavily sanctioned.
- In 2024, a large proportion of companies will have to refinance at significantly higher costs. For the moment, some of them are still benefiting from the low rates they contracted a few years ago.

INFLATION

- Inflation data continues to improve across all regions. Most of them even accelerated sharply downwards.
- In the medium term, certain forces pushing inflation upwards could strengthen, notably the optimization of supply chains, decarbonization and defense.
- In the longer term, the forces pushing down inflation remain demographic growth and productivity gains.

INTEREST RATE

- No offense to central bankers, economic data on inflation and employment are the main drivers of interest rates. According to these latest figures, Europe could be the first bank to cut its rates in 2024. Financial markets expect to see the United States cut their rates in the second half of 2024.
- Interest rates remain in absolute terms at levels extremely high. This could have a notable impact on highly indebted countries and companies.
- A slowdown in the economy should continue to mechanically attenuate inflation... And thus reduce pressure on interest rates.

SOURCE: MFM, December 2023

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MONTHLY PERFORMANCE, 30 NOV. 2023

Equities Market (Local currency)	
Europe	9.87
United States	9.37
World (all countries)	8.30
Emerging Markets	6.18
Japan	5.97
Asia (ex-Japan)	5.10
Switzerland	4.36
United Kingdom	2.26
China	1.92

Equities Sector (Local currency)	
Information Technologies	13.30
Real Estate	11.28
Consumer Discretionary	9.80
Financials	9.30
Industrials	8.79
Telecommunication Services	7.47
Materials	6.78
Utilities	5.46
Health Care	4.64
Consumer Staples	2.82
Energy	-0.92

Fixed-Income (USD Hedged)	
US Treasury Long Duration	9.16
Global Aggregate Long Duration	6.97
Emerging Market Hard Currency Aggregate	5.03
Global High-Yield	4.72
Global Corporate Credit	4.67
Global Convertibles	4.46
Global Aggregate	3.44
Global Treasury	3.02
Global Aggregate 5-7 Year	2.88
Swiss Bond Index AAA-BBB (CHF)	1.74
Global Inflation-Linked Bonds	1.70
Global Aggregate 1-3 Year	0.96

Others (USD)	
Industrials (CBR)	-0.18
Global	-2.69

CONTACT

Lausanne

Rue Etraz 4
CH-1003 Lausanne

Zürich

Bleicherweg 47
CH-8002 Zürich

T. +41 58 590 10 00

info@mirante.ch | www.mirante.ch