FORECASTS 2023

2023 – a challenging investment year

Without a look at the past year, the coming months remain emotionally difficult to digest. 2022 brought the abrupt end to the long-term low interest rate policy. Abruptly, because the military escalation in southeastern Europe and the uncompromising corona regime in China caused damaged supply chains worldwide and rampant inflation. Central banks responded with the toughest and fastest rate hikes since 1913. No asset class was spared of losses. The start into the new year will be accordingly bumpy. The macroeconomic facts are known so far, so the market thrives on emotions and surprises. We consider the amount of negative surprises to be manageable and largely priced into the market. The higher potential for positive surprises can trigger the long-awaited turnaround of the financial markets.

Stock markets are influenced in the short term by three factors: The focus on corporate profits as the number 1 market risk. A looming earnings recession, i.e., a decline or weak growth in corporate profits, would be poison for stock markets. The slightest disappointment of a profit expectation is currently punished with high price discounts. The second point we see is the influence of central banks on the markets. Despite the prophecies of doom, the very rapid interest rate hikes have not yet led to a recession. The daily statements of the various regional Fed members give the impression that any quick stock market recovery is unwelcome. The fear of recession has calmed an overheated economy and reduced inflation rates somewhat. The interest rate hikes show the desired effect. But anyone who speculates today on the end of interest rate hikes or even expects interest rate cuts this year is probably wrong. The Fed will adjust interest rates moderately due to the good effect in order to force the inflation rate in small steps into normal levels. Thirdly, fear of recession will bother investors permanently in 2023. Although we do not believe in a global economic crisis, but recessionary phases are possible in certain regions.

Due to the good effect, central banks will raise interest rates only moderately. The goal of reducing inflation without causing a recession may seem like squaring the circle, but it will be possible for the first time in economic history. Let’s still be careful, the topic of recession is far from being off the table and will also shape the new year and trigger severe volatility in the market.

Inflation has damaged consumers' purchasing power where it hurts most: in basic needs. Housing, food, energy, mobility. The basic costs for imported goods have declined today and have partly reached the level of 2021. This advantage has not yet reached the consumer, but as a windfall profit in the companies.

Economic data paint a mixed, moderately positive picture: inflation is slowly receding. An astonishing 2.9% inflation shows robust stability of the Swiss economy. At 7.9%, the annual average of German inflation is significantly higher than that of the USA at just under 7%. The annual average in France is lower at 5.4%, probably due to government intervention in favour of moderate energy prices.

Economic growth in our core regions is showing moderate growth. We are in stagflation, i.e., stagnant growth combined with high inflation. The USA achieved an acceptable result in 2022 with a plus of 3.2%, Germany with just under 2% achieved an increase similar to Switzerland with 2.1%. France's economy grew by 2.6% in 2022. The outlook for 2023 in these regions assumes weaker global growth to the edge of a recession. In 2023, the buzzword 'slowcession' could make history: slow growth. Significantly stronger increases are not expected until 2024. The classic leading industrial indicators support these figures: The global purchasing managers' index PMI for industry is currently oscillating below 50 points, a sign of zero growth in industry. This figure can be corrected by the damaged supply chains from China and the icy storms in the US at the end of last year. The effect was a regional standstill in the US. As a classic growth indicator of the global economy, China will pick up speed after the end of the corona measures. We expect a rapid normalization of supply chains from this global workplace. This PMI is much more positive for the service sector. In a modern society, this sector accounts for three-quarters of economic output.

The State Street Investors Confidence Index (Global) fell to a low 75 points at the year, well below a neutral 100. This confirms an extraordinary distrust of investors, fear of loss and consequently a partly undervaluation of the stock markets. Current data show that consumer confidence is steadily improving. As a driver of the global economy, the disposable income of US citizens has risen sharply. On the positive side, the private level of debt for US citizen fell to a historic low. The trade deficit of the US economy has declined significantly. In the Western countries, the order books are full, industrial growth is only possible thanks to qualified staff. In December, around 200,000 new jobs have been achieved in the US, which was commented by the US Federal Reserve as inadequate.

The market development in the new year will be no less volatile than before. The controversial chart technique gives hope to some optimism. Even a critical interpretation of the Shiller Cape suggests a better year. It is important that as a long-term investor you do not let yourself be seduced by the wild volatility in stock markets into day-trading. A long-term view of qualitative successful companies should not be clouded by short-lived emotions. Equities will continue to outperform bonds this year. Bonds also offered no protection against losses last year. It is often forgotten that equity dividends are not inferior to the interest rates of bonds, and can offer better returns. A global survey shows that 70% of professional investors are expecting a moderately positive investment year. Almost 30% express latent insecurity. In the mood environment at the turn of the year, the opinions of the financial institutions are astonishing: of 20 global major banks, 19 see 2023 as positive, while one bank sees it moderately negative. It is striking that finance houses in Asia are decidedly more optimistic. The return of China is likely to contribute significantly to this.

Apart from political systems, a modern society is built on three economic pillars: affordable housing, affordable food and affordable mobility. Investments in these areas promise long-term stability. Demographics and health, communication and security remain driving topics in stock markets. Private equity thrives on cheap debt capital. The new interest rate landscape could badly slow down this business segment in the near future.

Anyone who wants to grasp the importance of the US Federal Reserve should remember that around 65% of the world's financial activities are settled in US dollars. Consequently, American decisions also have global implications. Recently the various members of the Fed Committee have come forward almost daily with opinions on the course of the economy. Instead of behind closed doors, discussions and disputes are carried into the media. Investors follow these sometimes violently different statements with eagle eyes and not only react abruptly, but neglect to look at the essentials: the companies and their balance sheet and profit quality. Many market participants overlook the fact that a central bank does not have to serve the stock markets, but must ensure a stable economy and currency. Comparisons to 1929, the late 60s or 2008, like all statistics, are of little help for the future. The coming years will be different.

With a portfolio of high-quality values anyone that sees asset management as a long-term task, can look down the street in a relaxing mind in any environment, even in difficult years.

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