Quarterly letter

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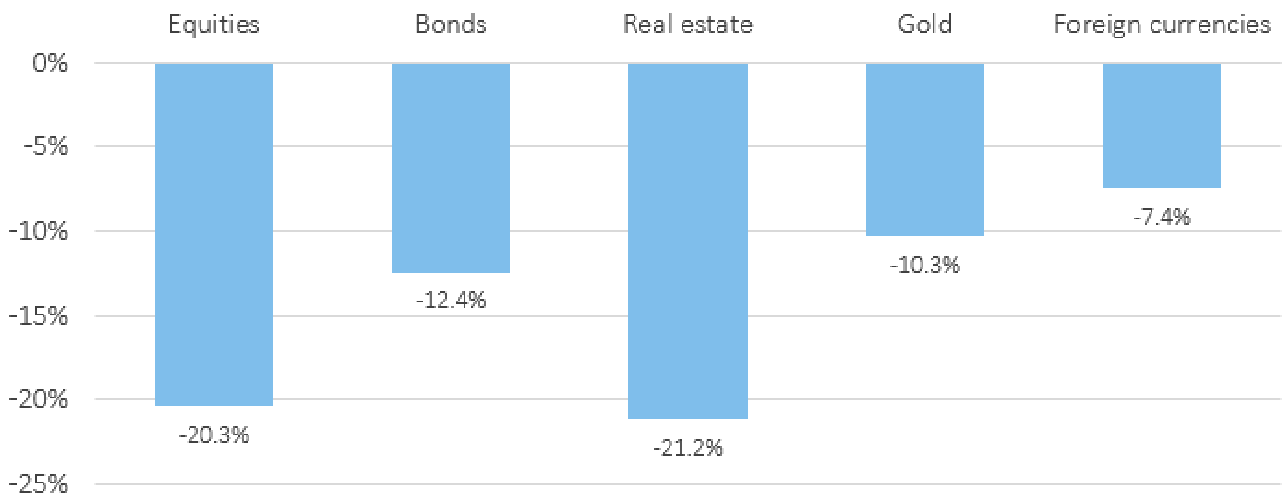
Interest rates undermine diversification strategy temporarily

An unpleasant third quarter for investors followed on seamlessly from the difficult first half of 2022. The conflict between inflation and economic growth, described in our semester letter, has further intensified. The central banks intend are raising interest rates even faster in order to curb the persistent inflationary pressure - even though the economy is increasingly stuttering. Rising interest rates and a further escalation in the Ukraine war have been the main drivers of falling asset prices, affecting all asset classes.

Performance of asset classes in CHF since the beginning of 2022



Source: Bloomberg, Belvalor AG; data as of 28.09.2022; Equities: SPI; Bonds: SBI Swiss Bond Index (AAA-BBB); Real estate: SXI Swiss Real Estate Funds Index; Gold: ZKB Gold ETF (hedged); Foreign currencies: Average of USD, EUR, GBP, NOK, SEK, JPY, AUD, CAD vs CHF

Price correction of all assets

Bond prices have fallen as interest rates were moving higher. The price losses are unpleasant, but the higher yield levels offer investment opportunities. We consider bonds with short maturities as attractive. **Equities** have entered a bear market (phase with falling share prices), which is usually accompanied by a recession. Solid companies will emerge stronger from this difficult phase, although even the prices of these first-class companies have suffered significant losses. In **real estate**, demand is falling as a result of higher mortgage rates, inflation and recession concerns that are holding back consumption. Even **precious metals** have not been spared from the correction.

Challenging combat of inflation

After pursuing an expansionary monetary policy for far too long, the central banks are now raising interest rates sharply. Although inflation was not ignited solely by the overly loose monetary policy, it is to be pushed down at all costs by means of interest rate hikes. The associated economic risks, i.e. a longer and/or deeper recession, are being accepted. It cannot be ruled out that the central banks are exaggerating their interest rate hikes. There are signs that inflation has passed its zenith. Aspects such as lower commodity prices, lower freight prices and a generally weaker economy support this thesis. For the first time this century, we find ourselves in an environment of sharply and rapidly rising interest rates. This has caused asset valuations to correct massively and prices in all, not just individual, asset classes to fall. The diversification strategy that has proven itself over the long term, but which in our view still makes sense, has temporarily failed to have an effect. We assume that the central banks will be forced to adjust to a more generous monetary policy sooner rather than later.

We stay true to our investment style / Corrections also offer opportunities

In such times, it is difficult to keep a cool head and not to lose focus on the longer term. It is important not to let oneself get carried away and not to be guided by emotions. Equities and other real assets, including gold, offer the best opportunity to maintain purchasing power in the long term. The Swiss franc remains particularly attractive. Crises are stress tests; however, corrections that accompany them always offer opportunities for long-term oriented investors.

Depending on risk capacity and willingness, we have started to buy first equities of quality companies. In addition, we invest in bonds with shorter maturities from debtors with good credit ratings. Although our assessment of the market situation is that a great deal of negative news has been factored into current stock market prices, the investment environment will remain challenging for the time being. However, prices usually bottom out before the end of the recession. We expect this to be the case this time as well. In addition, unexpected positive news can favour a recovery within a very short time.