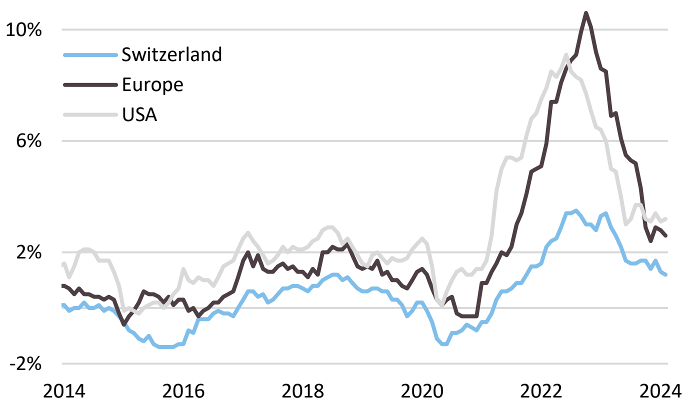
Financial Markets 2024: Pleasing Start

Inflation falls – will interest rates follow?

In the first few months of 2024, overall inflation in the world's largest economies continued to normalise. However, the rate of decline has slowed in many countries and it is therefore questionable – with the exception of Switzerland – whether inflation will reach the central banks' target of 2% in the current year. The fact that inflation in Switzerland is currently well below the 2% mark mentioned above enabled the Swiss National Bank to cut its key interest rate by 0.25% to 1.50% in March. To what extent the US Federal Reserve and the European Central Bank will follow suit is uncertain, in view of the more persistent inflation there.

Graph 1: Inflation in Switzerland, Europe and the USA*



*Source: Bloomberg, Belvalor; *Consumer Price Index (CPI); Europe: Eurozone*

The different inflation trends and corresponding interest rate expectations have led to most foreign currencies – including the US dollar and the euro – appreciating against the Swiss franc. In view of the structural attractiveness of the Swiss franc, however, we assume that the effect will be temporary.

Despite the uncertain decline in inflation, the equity markets of most major economies are on the rise, with numerous indices reaching new record levels in recent weeks. The US equity markets are being sustained by the hype surrounding artificial intelligence, even if the price advances are more broadly based. There is room for improvement in the Swiss Performance Index (SPI). The index is still trading around 10% below its peak reached at the beginning of 2022 owing, not least, to its defensive nature.

In the face of tempered expectations for interest rate cuts, gold also performed extremely well, benefiting from purchases by numerous central banks, rising global government debt and geopolitical tensions.

Conclusion and positioning

While market participants have so far focused on the surprisingly strong US economic growth, economic activity in Europe is also beginning to recover, albeit from a low recessionary level. A slight acceleration in growth during the forthcoming months can therefore not be ruled out, but is also dependent on any interest rate cuts that take place. In order to prevent inflation from flaring up again, central banks will proceed with caution when it comes to cutting interest rates. Monetary policy will therefore remain restrictive for the time being. At the same time, equity markets are already anticipating an economic recovery to some extent and valuations have risen in many places in recent months.

European activity indicators point to a stabilisation of the industrial sector.

We are maintaining our constructive investment outlook from December 2023, but are exercising a certain degree of caution owing to unresolved inflation and interest rate risks, uncertain economic developments and existing geopolitical risks, and are therefore not fully utilising the equity quota. In the event of corrections, this enables us to invest in quality companies with good returns on invested capital. Our long-term investment strategy focusing on real assets with inflation protection, particularly equities, will therefore not change. Corporate bonds of good borrowers are suitable for supplementing and replacing liquidity in the portfolio. Alternative investments, especially gold, also contribute to diversification.