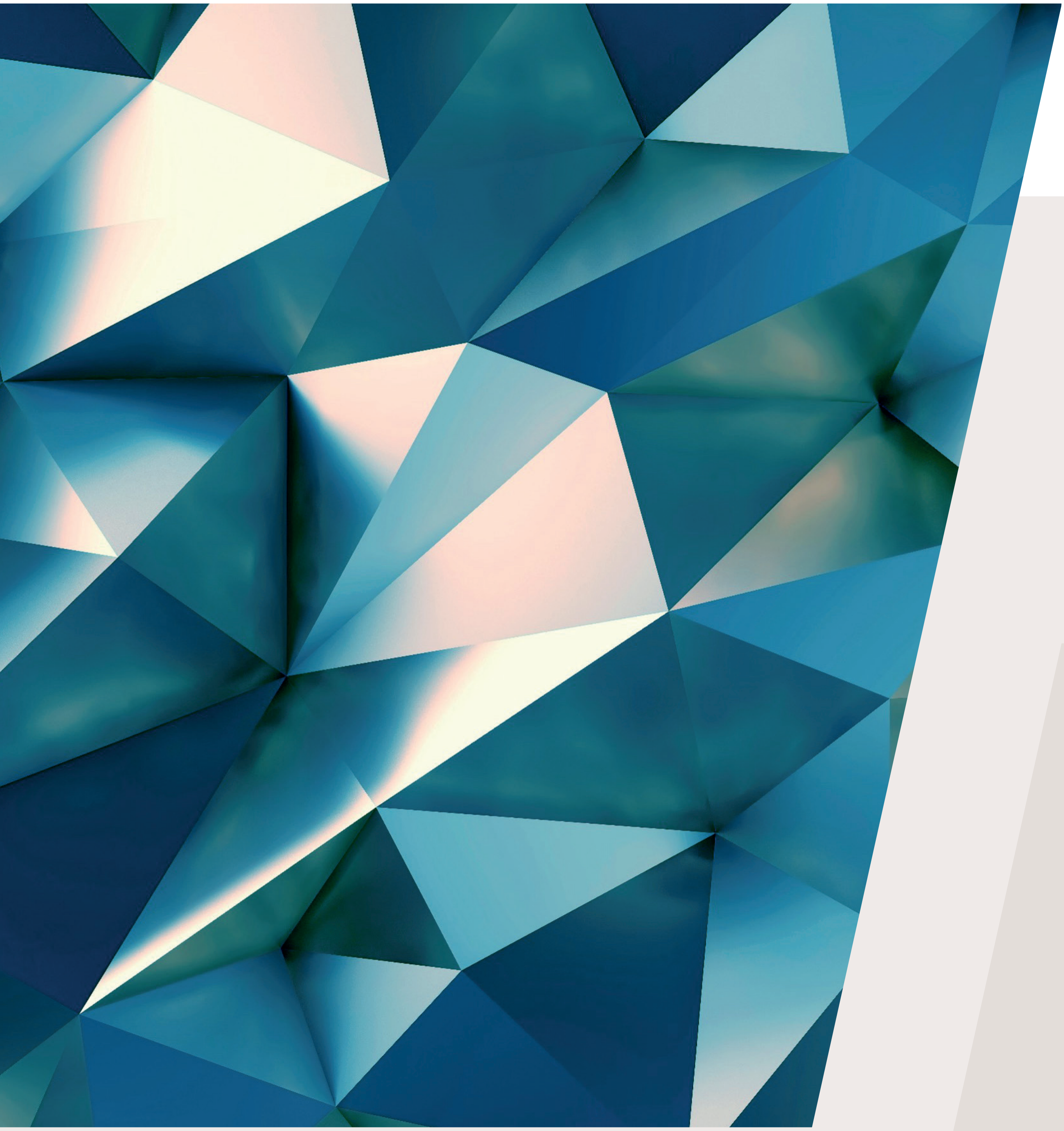
Rothschild & Co
Wealth Management



NOVEMBER 2024

Mosaique Asset Allocation

Our current view

Dr. Carlos Mejia
Chief Investment Officer

Kevin Gardiner
Global Investment Strategist

KEY POINTS

- The further reductions in US interest rates priced into money markets look plausible
- Falling rates globally continue to coincide with healthy corporate profitability
- We see little reason to change our positioning, particularly with the US election so close

THE MACRO PICTURE

After the US Federal Reserve cut interest rates by a bumper 50bp in September, money markets again became overly optimistic on the scale of future US rate cuts, as they had been for much of the previous year. However, more recent data has seen these expectations reined-in to (we think) more plausible levels. Barring a dramatic surge in US growth and/or inflation, we think the resultant sell-off in US Treasuries may now have run its course.

Meanwhile, the more subdued growth prospects in Europe have allowed the ECB to continue trimming its policy rates without such a sell-off in longer-dated bonds. In Switzerland, the absence of much on an inflation problem to begin with effectively gives the SNB carte blanche to cut rates as and when it thinks best. China's growth and inflation have also been muted by local standards, and the authorities there continue to focus on supporting the troubled real estate sector in particular.

Only in the UK has there been a sell-off in government bonds on a par with that seen in the US, but this likely reflects uncertainty surrounding the imminent first budget from its new government – a budget which we doubt will be expansionary, and which we think will leave the Bank of England with room to resume cutting policy rates.

This leaves global markets still facing a relatively favourable backdrop of subdued inflation alongside ongoing moderate growth, a continuing recipe for gently declining interest rates and healthy profitability. This is a constructive mix for portfolios, favouring stocks ahead of bonds, and both ahead of cash.

With this market-friendly mix still in place, our asset allocation committee again decided to leave its positions unaltered in October. The latest gains in stock markets, which have hit new highs in recent weeks, have pushed valuations higher; meanwhile, there are signs of some overconfidence amongst investors, both in market positioning and in the tone of commentary around the likely impact of Artificial Intelligence on wider productivity growth, which can seem naïve. But neither of these developments yet seemed to our asset allocation committee to be sufficient yet to warrant a reduction in risk assets, or a refocusing on more cyclical sources of growth.

As a result we again stay one notch overweight in stocks, which can benefit from both healthy profitability and falling rates, funded by an ongoing underweight position in liquidity. We stay neutral on bonds, which benefit only from falling rates. Those gains are only reliable at the short-dated end of the market, but as noted, we think the rise in longer-dated yields may now have largely run its course, and we remain patient in our preference for longer duration bonds, which we expect to rally within our tactical one-year investment horizon.

INVESTMENT CONCLUSION

We have again left asset allocation unchanged. Within the two big asset classes, regional, sectoral, duration and credit positions are also unaltered. There was some discussion of marginal changes to sector positions, but with several of those likely exposed to the likely binary risks associated with what seems to be a coin-toss US election result, there was little appetite for changes there either.

Asset allocation overview

Equities. Valuations are almost as extended as they were in 2021, and it is hard to see the macro climate becoming much more positive than it already is. That said, further rate cuts are very likely on both sides of the Atlantic in what remains of 2024 and in 2025, and expectations for those now look more realistic than they did.

Within the equity market, we favour cyclical and secular growth sectors, with ongoing overweight positions in industrials, technology and communications. These positions are sustained by ongoing underweights in utilities (another defensive sector) and real estate (which needs bigger reductions in policy rates and bond yields than are currently in prospect to perform more strongly), and by a more recent underweight in the consumer discretionary sector.

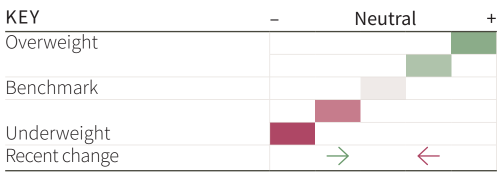
Regionally, we stay overweight the US, and since February have also favoured most of continental Europe too, at the expense of more defensive markets such as the UK and Switzerland. Discussion of whether Europe can share market leadership with the US, has faded as growth indicators have favoured the US and the USD has firmed, but we stay patient. The possibility of a significant increase in protection, and the likely impact it could have on non-US regions, is of course another binary risk posed by the US election.

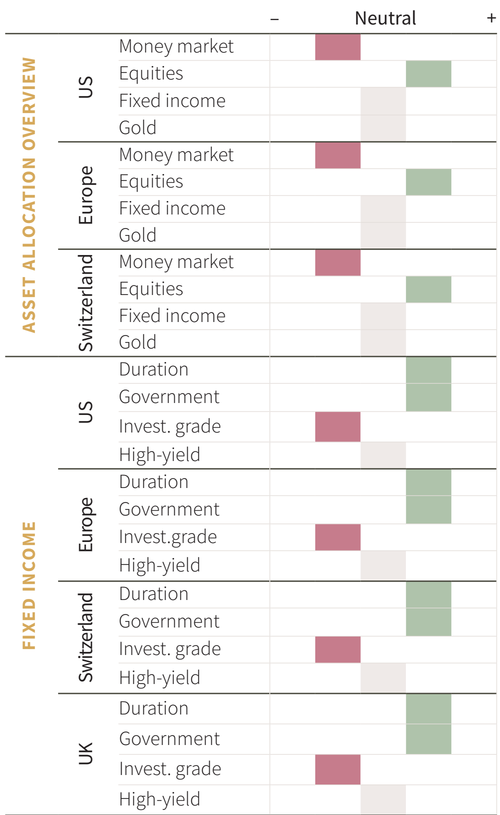
Fixed income. Our preference for longer-duration exposure has hurt in the last month, particularly in USD-based portfolios. However, expectations for terminal interest rates now look more realistic, as noted, and we doubt the longer-term inflation outlook will be damaged by the rate cuts in prospect.

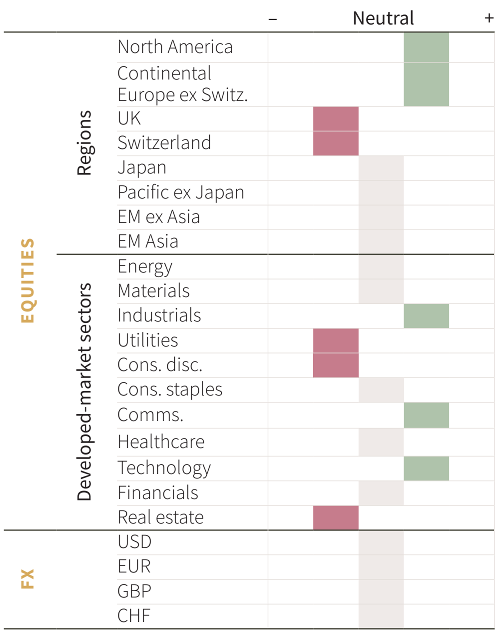
This does not mean that we expect consumer price inflation to stick at or close to targeted rates (2%) any time soon, but we doubt the overshoot will be big enough to trouble markets. Similarly, we continue to favour government bonds over credit – not because we worry about corporate defaults, but on valuation grounds: credit spreads have tightened further as government yields have risen in the last month, and have not been lower in the post-GFC period.

Currencies. The dollar has rebounded somewhat as US growth indicators have remained relatively firm and the scale of expected US rate cuts has faded. Currency volatility remains modest, however, and none of the big bilateral cross rates seems close to breaking out of recent trading ranges.

Asset allocation







Wealth Insights

At the heart of Wealth Insights lies a wide set of timely and insightful publications and podcasts.

For more information please visit our page.

https://www.rothschildandco.com/en/wealth-management/switzerland/insights/