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Portfolio Update
July 2019

- **Central banks lift the financial markets**
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- **The final ten percent**

Review

Central banks come to the rescue

Investors seem to be increasingly concerned in their economic forecasts as data reports continue to disappoint. Weaker business surveys have prompted analysts to significantly lower their earnings expectations, which they had previously revised upwards. However, both equities and bonds have posted impressive gains despite the rise in economic worries. So what is driving the current carefree sentiment?

Equity indices 2019 (Total return)

Americas	June	2019
Dow Jones Industrial Average (US)	7.3%	15.4%
S&P 500 (US)	7.0%	18.5%
NASDAQ Composite (US)	7.5%	21.3%
Brazil Ibovespa (BR)	4.1%	14.9%
Europe	**June**	**2019**
EURO STOXX 600 (EU)	4.5%	16.5%
FTSE 100 (GB)	3.9%	13.1%
CAC 40 (FR)	6.8%	20.4%
DAX (DE)	5.7%	17.4%
SMI (CH)	3.9%	21.2%
Asia/Pacific & Emerging Markets	**June**	**2019**
Nikkei 225 (JP)	3.4%	7.5%
Hang Seng (HK)	6.7%	12.7%
MSCI Emerging Markets (EM) in USD	6.3%	10.7%

Sources: Bloomberg, swisspartners

The fact that investors appeared to be shrugging off fears of recession and the various trade disputes in June was probably largely thanks to the supportive comments from central bank presidents. While there was talk of another two rate hikes in the US at the beginning of the year, the financial markets are now pricing in two rate cuts for 2019. The European monetary watchdogs have also signalled their willingness to extend their accommodative measures if necessary.

The shift in rhetoric has pushed what were already ultra-low bond yields further downwards, in some cases well into negative territory. According to an analysis by Bloomberg, 25% of all outstanding bonds already have a negative yield to maturity. In this setting, it is no great surprise that the equity markets have trended upwards. Given the growing shortage of alternative investment options and negative interest rates on cash investments, investors increasingly feel compelled to seek out this riskier asset class for positive returns. At the same time, valuations are still reasonable relative to bonds, with the DAX, for example, offering an expected price/earnings ratio of 13.6 at a dividend yield of 3.2%.

The G20 summit in the Japanese port city of Osaka was a highly anticipated event at the end of the month. For once, subjects such as climate or migration policy played a subordinate role for observers, who were more interested in the subsequent meeting scheduled to take place between US President Trump and the Chinese leader Jinping. While expectations of a ceasefire without any additional far-reaching agreements being made in the trade conflict formed the baseline scenario for observers, the decision to lift the ban on trading with technology group Huawei was a surprising development. However, for the time being it remains unclear just how willing the negotiating parties are to make the necessary concessions when the trade talks resume.

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Mandate returns gross & positioning

	Euro			Swiss Franc			US Dollar			British Pound		
	CONS	BAL	DYN	CONS	BAL	DYN	CONS	BAL	DYN	CONS	BAL	DYN
2012	**6.6%**	**7.4%**	**10.5%**	**4.3%**	**6.5%**	**10.9%**	**5.9%**	**8.4%**	**11.8%**			
2013	**1.5%**	**6.5%**	**13.5%**	**1.9%**	**8.3%**	**16.7%**	**2.8%**	**9.4%**	**18.5%**			
2014	**6.1%**	**8.0%**	**10.2%**	**4.9%**	**6.5%**	**9.2%**	**1.6%**	**2.2%**	**3.1%**			
2015	**2.7%**	**6.3%**	**9.9%**	**-0.8%**	**0.0%**	**1.8%**	**-0.3%**	**0.0%**	**1.0%**			
2016	**2.3%**	**5.3%**	**7.1%**	**1.3%**	**3.9%**	**5.7%**	**2.8%**	**6.2%**	**7.2%**	**4.6%**	**9.5%**	**12.1%**
2017	**3.5%**	**7.3%**	**10.8%**	**4.3%**	**8.9%**	**15.0%**	**7.1%**	**12.7%**	**18.1%**	**4.7%**	**8.7%**	**14.2%**
2018	**-4.3%**	**-9.0%**	**-10.5%**	**-5.6%**	**-10.1%**	**-12.1%**	**-2.5%**	**-7.9%**	**-9.8%**	**-3.3%**	**-8.6%**	**-10.4%**
Jan 19	2.4%	4.4%	6.0%	2.6%	4.7%	6.3%	2.6%	4.8%	6.1%	2.1%	4.0%	5.4%
Feb 19	1.4%	2.5%	3.3%	1.4%	2.4%	3.1%	1.4%	2.6%	3.0%	1.2%	2.3%	2.8%
Mar 19	0.7%	1.3%	1.9%	0.6%	1.1%	1.5%	0.8%	1.1%	1.5%	0.9%	1.3%	1.9%
Apr 19	1.1%	2.2%	3.2%	1.5%	2.6%	3.8%	1.2%	2.5%	3.3%	1.2%	2.3%	3.2%
May 19	-1.3%	-3.0%	-4.7%	-1.7%	-3.3%	-5.1%	-1.1%	-3.0%	-4.6%	-0.8%	-2.4%	-4.0%
Jun 19	1.4%	2.7%	4.0%	1.3%	2.5%	3.8%	1.9%	3.4%	4.7%	1.7%	3.3%	4.6%
2019	**5.8%**	**10.6%**	**14.2%**	**5.6%**	**10.3%**	**13.6%**	**7.1%**	**11.7%**	**14.5%**	**6.4%**	**11.1%**	**14.4%**

The correction on the financial markets was initially limited to the month of May, which must have been a huge relief to investors. The markets moved into positive territory just in time for the beginning of June. While the previous month's losses are not yet fully digested, returns in June were highly respectable. As previously mentioned, equities were not the only ones to rise, as bonds also climbed sharply. However, equities generated higher-than-average gains versus other asset classes once more, fuelled by hopes of a trade truce and fresh support from the central banks. This is also reflected by the excess return in dynamic profiles.

Overall, therefore, we can look back on an extremely satisfying result for the first half-year. Given the focus on a longer-term target, we did not make any hasty portfolio shifts in the heat of the moment, as reflected by the returns. In the balanced and dynamic profiles, we have achieved a substantial excess return relative to our peers, while we are only marginally lagging behind in our most conservative profiles. However, with regard to the latter we believe we are meeting the needs of our clients who prefer a lower level of volatility in this type of mandate.

We continued to reduce risk in the portfolios in June due to the solid performance data and ongoing uncertainties. Although the markets are expected to be positive, the reduction in risk means that we would be less vulnerable in the event of a sharp rise in volatility. The liquidity allocation has been raised for the time being, but this will offer potential to participate in investment opportunities at short notice.

Equities (neutral)	In light of declining economic prospects and the Trump administration's irregular measures in pursuing other political goals via trade policy (Mexico), the equity allocation was reduced to the neutral level in the course of the month. While we do not anticipate negative economic growth, we feel we have adopted the right positioning with a neutral allocation given the heightened volatility stemming from external effects.
Bonds (underweight)	Focus on global flexible strategies in combination with high-yield bonds, senior loans and floating-rate investment products with low interest rate sensitivity, while underweighting direct investments in government and European corporate bonds that offer too little compensation for risk.
Alternative Investments (overweight)	Combination of insurance securitizations, market-neutral or option-based volatility strategies, which exhibit low correlations, unlike traditional asset classes.
Liquidity (overweight)	Outside of the US dollar investment universe, there are few opportunities to avoid the negative interest rates applied by the central banks. If necessary, we are parking excess liquidity in cash and accepting a negative return, which is partially passed on to customers, especially as there are no other risk-free alternatives. Trustee investments offer opportunities in US dollars.
Foreign currencies (underweight)	The foreign currency allocation is reduced in the portfolio by deploying foreign exchange futures transactions. A higher share in the reference currency is favoured at present on the basis of risk considerations.

OUTLOOK

The final ten percent

According to comments from US finance minister Steve Mnuchin, an agreement between the US and China is just around the corner. Apparently, 90% of a possible deal has been negotiated, with aspects still to be clarified for the remaining 10%. What this tells us is very little, while the areas in which both parties are failing to reach an agreement remain unclear. Moreover, remarks such as these have regularly circulated in the media in the past, without anything specific being finalised thus far. In the words of a Bloomberg analyst alluding to Trump's Twitter account, the next tariffs are never more than 280 characters away. With this in mind, the most observers could hope for at this year's G20 summit was a ceasefire as expectations were correspondingly low. As it turns out, they were low enough for Donald Trump to bolster the equity markets once again.

While the focus is now shifting to the Fed's July meeting, uncertainty amongst entrepreneurs is likely to remain intact. Whatever the 10% means, planning reliability and appetite for investment remain subdued for the time being. This is reflected by numerous surveys, which are still trending weaker despite the highs on the equity markets (see chart). Thus, the prevailing question is whether the rate cuts that financial players are calling for will actually change anything. The outlook is doubtful for Europe and Japan.

The approaching US election is considered a possible game changer. It is logical for market observers to assume that successful political actions will lead to a promising election campaign for Trump. However, to prove his success, even President Trump will be unable to avoid softening his hard-line approach and making an effort towards rapprochement with his opponents. There was an unexpected indication of such a move at the end of last month when the US president briefly entered North Korean territory. Further steps in this direction followed by corresponding agreements could see much-needed confidence in the president being restored.

JPMorgan: Global purchasing managers' index (manufacturing)

Sources: Bloomberg, swisspartners

Interesting developments have also been playing out on the bond market. Austria has secured record-low interest rates going into the next century by issuing a bond with a maturity of 100 years. Investor subscriptions for the issue exceeded supply by four times. What was particularly noticeable was that the yield was only 1.2%.

Record-low risk premiums on bonds such as these, combined with acute uncertainties on the global trade front have prompted us to scale back risk in the portfolios. In the current environment, we are holding more liquidity and underweighting bonds, while keeping the equity allocation in neutral territory. Incoming economic data will reveal whether the latest trade talks are taking effect.

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