swisspartners
The art of finance.

PORTFOLIO UPDATE

JUNE 2021

MONTHLY REVIEW

After the euphoria that swept through the equity markets in March and April, sentiment turned a little more sober in May. It was a month that ended with volatility rather than any clear sense of direction and probably led some investors to make decisions that they now regret. As soon as a particular event is over, the market tends to shift its focus to the next one: in this case, from company results to economic data, which held plenty of suspense and surprise in store for market observers.

The steady rise in US yields since the beginning of the year prompted many investors to take a closer look at inflation numbers, which ultimately were either in line with expectations or surprised to the downside last month. Some investors saw their fears confirmed as the US consumer price index unexpectedly surged to more than 4%, triggering a sell-off on the equity markets. Nonetheless, the indices quickly headed back upwards, albeit supported by relatively few stocks. The dollar took another tumble in response to the numbers. This was beneficial for inflation-proof assets, especially gold, which saw stratospheric growth in prices.

The shift away from producers of consumer discretionary goods to consumer staples firms continued last month. IT stocks also had a hard job holding on to their gains. Unsurprisingly, European indices largely outperformed their Asian and US counterparts in this setting. Oft-neglected companies from the battered energy sector also made a positive contribution to the portfolio's return last month as the oil price stabilised at a higher level.

While bonds avoided further losses for the most part, last month's movements did little more than stabilise the downtrend we have seen this year. The impact of the inflation data on yield levels was fairly limited, although bond prices were pushed down by widening credit spreads, especially in the US market.

Financial markets 2021 total return

Equities	May	2021
S&P 500 (US)	0.7%	12.6%
Dow Jones Industrial Average (US)	2.2%	13.8%
EURO STOXX 600 (EU)	3.1%	14.0%
DAX (DE)	2.5%	13.1%
SMI (CH)	3.9%	9.7%
MSCI Emerging Markets (EM) in USD	1.2%	6.0%
Fixed Income	**May**	**2021**
US Corporate Bonds Inv. Grade	0.8%	-2.9%
US Corporate Bonds High Yield	0.3%	2.2%
Pan-Europe Corporate Bonds Inv. Grade	0.1%	-0.6%
Pan-Europe Corporate Bonds High Yield	0.3%	2.9%
Alternative Investments	**May**	**2021**
Gold	7.6%	0.5%
Oil (brent)	2.9%	33.7%

Sources: swisspartners, Bloomberg

MANDATE RETURNS GROSS

	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%	2.9%	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%
2019	9.2%	15.7%	21.6%	8.3%	14.8%	19.6%	11.5%	17.5%	22.0%	9.4%	15.3%	19.8%
2020	3.2%	5.3%	8.6%	2.6%	5.5%	9.0%	6.7%	9.7%	13.6%	4.6%	6.5%	10.3%
Jan 21	0.2%	0.3%	0.8%	0.2%	0.2%	0.8%	0.0%	0.1%	0.5%	0.0%	0.0%	0.3%
Feb 21	0.3%	1.3%	2.1%	0.7%	1.8%	2.6%	0.3%	1.3%	2.1%	-0.1%	0.6%	1.4%
Mar 21	0.9%	2.1%	2.8%	1.1%	2.4%	3.1%	0.2%	1.1%	1.6%	0.4%	1.5%	2.2%
Apr 21	1.4%	2.2%	3.0%	1.2%	2.0%	2.7%	2.0%	3.1%	4.0%	1.9%	2.9%	3.9%
May 21	0.5%	0.6%	0.6%	0.5%	0.6%	0.6%	0.9%	1.2%	1.2%	0.3%	0.3%	0.2%
2021	3.3%	6.6%	9.6%	3.7%	7.1%	10.2%	3.5%	7.0%	9.7%	2.6%	5.4%	8.2%

Actual portfolio returns may differ from the values shown above owing to the level of implementation, costs and restrictions on implementation.

TRANSACTIONS IN MAY

For a detailed overview of the transactions for each strategy, please do not hesitate to contact us.

POSITIONING

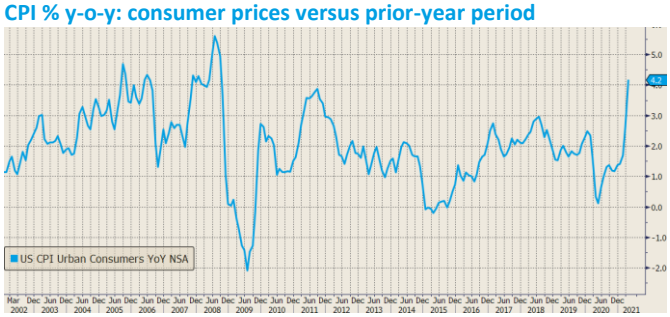
Liquidity (neutral)		Outside of the US dollar investment universe, there are few opportunities to avoid the negative interest rates applied by the central banks. If necessary, we are parking excess liquidity in cash and accepting a negative return, which is partially passed on to customers, especially as there are no other risk-free alternatives. Short-dated bond and trustee investments offer opportunities in US dollars.
Conservative	3.0%	
Balanced	5.5%	
Dynamic	5.5%	
Bonds (underweight)		In light of increasing debt levels in the public and private sectors, we favour bond issuers with solid balance sheets, a healthy business model and correspondingly good credit ratings. At the same time, however, the only way of achieving a positive yield to maturity is to take positions outside of the AAA/AA rating segment. Within the asset class, we utilise various bond types and market segments to maintain a cautious approach, including in the lower rating categories. As scope for further rate cuts is limited, we are keeping the duration (interest rate risk) low in the portfolio, which affords greater protection against sudden rises in interest rates. Given the recent rise in bond yields, opting for a low duration has worked out well. The current level now offers potential leeway to generate better returns on the fixed income front.
Conservative	48.0%	
Balanced	25.0%	
Dynamic	6.0%	
Equities (overweight)		The Covid-19 pandemic maintains a firm grip on the global economy and the stock markets. While vaccines are being administered worldwide, producing the required volumes remains a challenge for the manufacturers. Nonetheless, progress is being made in the level of vaccination coverage. This will allow a gradual return to normality, the prospect of which continues to be positively received on the financial markets. Other reasons for maintaining an overweight position in equities include ultra-loose monetary policy, the vast fiscal policy support programmes implemented by governments, the dearth of alternative investment options on the financial markets and better-than-forecast company results. If these supports are removed, the situation will have to be reassessed.
Conservative	27.5%	
Balanced	50.5%	
Dynamic	74.5%	
Alt. investments (overweight)		A broadly diversified portfolio of gold, cat bond funds, market-neutral equity and credit strategies, global macro, commodities and option-based arbitrage/volatility hedging strategies. In contrast to traditional asset classes, these instruments exhibit low levels of correlation and offer a degree of protection from geopolitical risks. In normal market conditions, the aim is to achieve a positive market yield while minimising volatility. A high level of liquidity is a fundamental requirement.
Conservative	21.5%	
Balanced	19.0%	
Dynamic	14.0%	
Currencies (strategy-related)		Foreign currency allocations differ depending on the risk strategy. Hedging foreign currency positions for US dollar strategies remains advisable in view of the current interest rate environment. This is because these strategies continue to benefit from a positive roll yield due to the interest rate differential versus the EU/Switzerland. Nevertheless, this approach is becoming less appealing due to the high level of net new debt and the shrinking interest rate advantage, not least as a result of the waning global dependence on the US dollar. In this environment, we have relative overweights in the euro and the Swiss franc.

OUTLOOK

Inflation? Interest rates? Beneficiaries?

There have not been any far-reaching consequences as yet, with the inflation surprise triggering more debate than action so far. However, this comes as no surprise given the way in which these numbers have emerged. Indeed, it makes absolute sense. Rather than taking action for the sake of it, it is a good idea to conduct a critical examination of these figures and analyse where they have come from.

CPI % y-o-y: consumer prices versus prior-year period



Sources: swisspartners, Bloomberg

There are various reasons for the marked surge in consumer prices shown in this chart. One of the drivers to be expected on the back of the Covid-19 crisis is a supply shock impacting goods that are in demand. First, prices of input goods such as building wood, iron, wheat and coffee climbed sharply. Second, there was also a pronounced rise in the price of used cars on account of supply bottlenecks in microchips for the new car market. This type of shock may be one-off in nature, but this is not necessarily the case. It would be an isolated phenomenon if the supply side were able to rapidly meet the elevated demand, or if the heightened level of demand proved to be a one-off (due to replenishing inventories, for example) before falling back to the previous level. A large part of the price rise in the basket of goods used to measure consumer prices stems from precisely these bottlenecks, which have emerged as a result of the lockdown situation. Alongside the issue of pent-up demand, the current debate revolves around

whether these bottlenecks are one-offs or will morph into a trend.

In theory, these factors should converge in relation to (expected) inflation and, as a consequence, the interest rates demanded on the capital market. These aspects should be considered when it comes to investments in bonds in particular because at present – depending on the assumptions made – there are reasons to raise the maturity of bond portfolios. Following the rise in March, nominal rates have largely trended sideways. Owing to the increase in inflation expectations, this means that real interest rates have fallen back to levels close to their lows.

Interest rate environment: (real) interest rates versus inflation expectations

Sources: swisspartners, Bloomberg

Inflation expectations are especially worthy of note, with 1-year and 10-year expectations shown above. The striking discrepancy, which also applies between 1-year and 5-year expectations, suggests that on the whole the market is currently anticipating – or pricing in – a short-lived surge in inflation. As a result, a high probability is being assigned to the scenario of a one-off effect, which would not imply an earlier, unavoidable rate move. This means that nominal interest rates would be more likely to decouple from this trend and remain stable.

Gold: the precious metal and commodities

Sources: swisspartners, Bloomberg

At the mention of the words "inflation" and "falling real interest rates", it is almost inevitable that attention focuses on one particular asset: gold. Thanks in part to the continued decline in real interest rates, having formed a double bottom the precious metal, which offers no inherent yield, met our expectations by breaking out to the upside from its flag-shaped consolidation phase. While this trend is likely to persist over the longer term, a reversal in short-term inflation expectations could possibly put an end to this dynamic.

If the current drivers of inflation expectations remained in place, investments in commodities and gold would offer attractive opportunities. Equally, inflation-linked bonds would be a better option than their fixed-rate counterparts. This is because a residual risk remains even if market rates do not move up (falling real interest rates), which could prompt the market to price in this risk at a later date.

Editorial deadline: 3pm CET, 3 June 2021

The publication was written by:

Dino Lüssi
Investment Management & Solutions (CH)