

» *Fisch View*

*April's topic:
„Goldilocks: how much longer?“*



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“Goldilocks”: How much longer will it last?

- The economy is cooling in the US and Europe, while inflation remains stubbornly high. We therefore expect a temporary stagflationary trend.
- However, financial markets continue to price in a "Goldilocks" environment. While a recession is not expected, declining inflation and falling interest rates with moderate economic growth are nevertheless anticipated. Disappointments are therefore becoming more likely.
- We remain neutrally positioned for the time being, as our indicators are not yet giving any sell signals.

Overall economic situation

While the European economy continues to stagnate, the booming US economy is cooling down. However, the ongoing supply of liquidity from the overnight reverse repo facility is still supporting the economy and stock markets for the time being. Overall, however, the previously supportive factors in the US are weakening and inflation remains stubbornly high. This creates a potentially challenging environment for monetary policy and makes it more difficult to ease it quickly.

Recent developments: US labour market is weakening

- The unemployment rate in the US rose to 3.9% in March, well above last April's low of 3.4%. Consumer spending and retail sales, which had previously provided strong support for the economy, are also falling. This shows that most of the enormous surplus savings from the pandemic period have been used up. What is also striking is the increasing weakness of the NFIB Small Business Optimism Index and, in particular, a decline in the planned hiring of new employees. Small businesses employ around half of the US labour force and account for over 40% of economic activity.
- At the same time, the weaker US labour market is being met with a persistently restrictive monetary policy, as inflation remains stubbornly high.
- Similar trends can also be found in Europe. The economy is stagnating, while inflation persists at an elevated level. The latter is due to strong wage pressure and thus inflationary second-round effects.

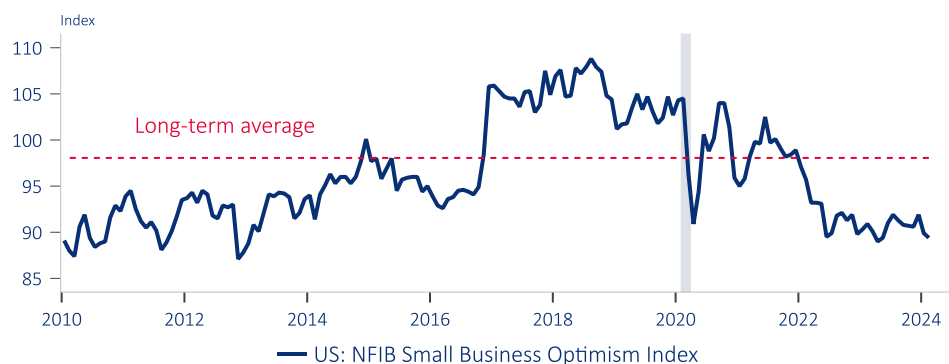
➡ **On the radar:** Gold has reached an all-time high (page 6)

Overview & outlook: Residual monetary energy is declining

- US banks continue to hold around USD 450 billion in excess reserves (ON RRP) at the Fed. This balance has been steadily reduced over the past 12 months from a peak of 2,300 billion and shifted into US government bonds. As a result, these funds flowed back into financial markets and made a significant contribution to the stock market rally and the stabilisation of the US economy. This also led to a considerable easing of the monetary environment and compensated for the Fed's restrictive monetary policy and quantitative tightening (QT). However, the loose monetary environment is also fuelling inflationary tendencies. These may even increase until the aforementioned excess reserves have flowed back into the financial system in full.
- After that, this important support factor will disappear. At the same time, the Fed is continuing to withdraw around USD 90 billion per month from the system for the time being as part of the QT, and the Japanese central bank is ending its previously very loose monetary policy, which will also have consequences for the global supply of liquidity.
- In addition to the US labour market, various other economic indicators (new orders, consumer sentiment, credit card defaults) are also weakening, while services inflation is stubbornly persistent and the base effects of goods price inflation are disappearing. The rising gold price points to certain dangers here (see "Topic on the radar").
- Overall, the coming months could therefore see a combination of declining liquidity, cooling economic momentum and yet persistent inflation. As a result, the previous "Goldilocks" environment could shift towards a stagflationary trend. However, this will only be temporary, as we expect the central banks to ease monetary policy very quickly if the economic slowdown becomes too severe. In this case, inflation is also likely to become a rapidly diminishing problem.

» Liquidity is currently still high, but a decline is becoming more likely.

Chart: The NFIB Small Business index is weakening



Sources: NFIB, Macrobond, Fisch Asset Management

Positioning: Risks and opportunities remain balanced

» We remain neutrally positioned and are waiting for sell signals.

- There are still opposing forces at work: on the one hand, the economy, labour markets and consumption are cooling, which is also dampening inflation and interest rates. On the other hand, the still high supply of liquidity from the private banking system is providing a strong positive counterbalance with support for the economy, but also increased inflationary pressure.
- The positive and negative forces acting on equity and corporate bond markets therefore balance each other out. In fact, the positive impetus provided by high liquidity and continued strong inflows of funds into the corporate bond markets (investment grade and high yield) could even continue to drive prices higher for some time. However, equity and corporate bond valuations are now ambitious. In addition, market expectations are currently very high. Even a slight deterioration in the environment could quickly lead to disappointment. We are therefore positioning ourselves neutrally in terms of risk exposure and are waiting for monetary or technical market warning signals before taking out risk.
- Positive and negative forces are also acting simultaneously affecting government bond markets, particularly at the long end of the yield curve. Stubborn inflation and slightly rising inflation expectations, together with persistently high government spending (particularly in the US), are putting upward pressure on interest rates. On top of this, the change in monetary policy in Japan, which should not be underestimated, is likely to lead to less demand for government bonds in the US and Europe in the medium term. The Fed and the ECB are also continuing to sell government bonds on a large scale (QT), which is an additional negative factor. Conversely, the declining economic momentum is having a dampening effect on interest rates. Overall, we are therefore taking a neutral stance on duration.

	US	Europe	Japan	Asia ex-Japan	LatAm	CEEMEA	
Return drivers							Key:
Equities	o ↓	o	+	o	o	o	++ Strongly positive
Gov. Bonds	o	o	o ↑				+ Positive
Credit IG (Spreads)	o	o		- ↓	o	o	o Neutral
Credit HY (Spreads)	o	o		o	+ ↑	o	- Negative
							-- Strongly negative
Total return							
Convertibles	o ↓	o	+	o			
Credit IG	o	o		o	o	o	
Credit HY	+	+		+	+	+	
	PrecMet	InduMet	Energy				
Commodities	+ ↑	o ↑	o				

Notes regarding the table: The table summarises the model results for the total return of convertible bonds and credit investment grade and high yield, which are a function of the listed return drivers. Changes from prior month are indicated with ↓ or ↑, i.e. "O ↓" means that the output has weakened from a prior value of + or ++. The methodology for calculating model outputs, and how the various pieces fit together to form the big picture, is explained [here](#). Within government bonds, we take German Bunds into account for Europe.

Cross asset class preferences

This table combines top-down views with bottom-up analysis at the portfolio level.

	Most preferred	Least preferred
Convertible Bonds	<ul style="list-style-type: none"> – Software (Cybersecurity) – Semiconductor (AI-related) – CBs with high convexity – Bond-like CBs with quality credits and attractive yields 	<ul style="list-style-type: none"> – Utilities, REITS – Unprofitable, early stage, expensively valued IT and biotech – Weak credit quality and/or liquidity
Global IG Corporates	<ul style="list-style-type: none"> – Energy, healthcare, financials – 5-10 year maturities 	<ul style="list-style-type: none"> – Technology & base metal – Maturities >10 years
Global Corporates	<ul style="list-style-type: none"> – Energy, healthcare, financials – Investment grade – Developed markets 	<ul style="list-style-type: none"> – Technology & base metal – High yield – Emerging markets
Global High Yield	<ul style="list-style-type: none"> – Capital goods, energy – Basic industry – Leisure 	<ul style="list-style-type: none"> – Financial Services – Technology
Emerging Markets - Defensive	<ul style="list-style-type: none"> – South Korea, Mexico – A-rated bonds – Maturities < 5 years 	<ul style="list-style-type: none"> – China, Hong Kong, Israel – BBB-rated bonds – Maturities >7 years
Emerging Markets - Dynamic / Opportunistic	<ul style="list-style-type: none"> – LatAm (esp. Brazil and Mexico) – High yield energy – Short-dated high-yield bonds 	<ul style="list-style-type: none"> – Maturities >10 years – A-rated bonds

Note: Preferred sectors/regions may differ between asset classes owing to respective performance drivers. In particular, equity exposure is the key performance driver for convertible bonds and is not relevant for corporate bonds.

On the radar: Gold prices at an all-time high

The price of gold is soaring. This may have something to do with the demand from various central banks in the emerging markets that want to break away from the US dollar currency regime. However, the recent acceleration in prices is also likely to be based on a fundamental change in longer-term inflation expectations and confidence in monetary stability.

The reason for this potential loss of confidence is likely to be the current combination of high financial market liquidity, stubborn inflation, unsustainable and exploding government spending and an increasing likelihood of interest rate cuts by central banks.

» Historically, the gold price has always been a reliable indicator of inflationary risks.

Historically, the gold price has always been a very reliable indicator of inflationary risks and has maintained its real value for more than 2000 years. The anchoring of higher inflation expectations associated with rising gold prices could then also lead to a self-fulfilling prophecy and fuel not only expectations but also inflation itself.

However, inflation still appears to be under control – and the rising gold price is merely a warning signal, not yet a symptom. However, further developments must be monitored closely. An increasing correlation between rising gold prices and rising yields on long-term government bonds is also becoming more likely, especially if the central banks loosen too quickly at the short end.

Chart: The price of gold has reached a new all-time high



Sources: Macrobond, Fisch Asset Management

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