

» *Fisch View*

*March's topic:
„Global liquidity is stabilising“*



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Global liquidity is stabilising

- Global liquidity has been slightly increasing again since January following a decline in the fourth quarter of last year. Previous warning signals for the financial markets are therefore diminishing.
- Although this is providing a tailwind for equities and corporate bonds, it is also leading to global inflationary pressure. In conjunction with growth concerns as a result of the erratic US trade policy, this is creating opposing forces for long-term government bond yields.
- We therefore remain neutral to slightly overweight in terms of equity and credit risk exposure and neutral in terms of duration.

Overall economic situation

Although economic momentum in the US is slowing somewhat, growth remains robust. However, economic expansion is being driven one-sidedly by high government spending and the resulting consumption. This is not sustainable in the longer term and is leading to persistent inflationary pressure, which is causing a degree of uncertainty. Growth in Europe remains anaemic. However, we see positive impetus as the year progresses.

Recent developments: Liquidity drives equities and inflation

- Surprisingly, the decline in global liquidity observed in the fourth quarter of last year – measured by an index based on the global M2 money supply – has reversed, with the result that the index is currently rising again slightly. Global liquidity is the main driver of equity and credit markets. It stimulates the economy, but also increases inflation, thus ensuring further gains in the price of gold.
- The reason for the rebound in global liquidity is a combination of an unexpectedly weaker US dollar, global key interest rate cuts, the increased issuance of T-bills in the US rather than long-dated government bonds, and increased lending in the US, Europe and China. However, the Chinese central bank is still increasing liquidity too little at the moment to have a global impact. This expansion of liquidity is dampened by the quantitative tightening (QT) of the Fed and ECB, but not fully negated.
- Due to the very regular long-term liquidity cycles historically, liquidity is not expected to fall again until the fourth quarter of this year at the earliest.

Overview & outlook: Risky assets on an upward trend

» Persistent inflation is expected

- Although the current resurgence in global liquidity is positive for risky assets and the economy, it is also putting upward pressure on inflation and commodity prices and therefore structurally also on long-term government bond yields. Various indicators for inflation expectations in the US (both market-based and survey-based) have recently risen to over 3%. This is not yet alarming, but should be monitored closely. There is a risk that inflation expectations, which were still in the region of 2% before the pandemic, will be 'de-anchored'. This would be a strong reason for central banks to stop easing monetary policy or even tighten it again.
- The current sharp rise in the price of gold is likely to be driven by rising inflation expectations in addition to continued central bank purchases. And there are good reasons for continued upward pressure on prices. In particular, the rising M2 money supply remains an important driver. However, the robust US economy, rising real wages, increasing economic momentum in the eurozone, and price increase plans by many smaller companies in the services sector are also having an inflationary effect.
- Strong dampening base effects on annual inflation will remain in the US at least until April. In addition, the calming of the situation in Ukraine and Gaza may lead to an easing of oil and gas prices. The US government's cost-cutting efforts are also likely to have a dampening effect on inflation, and on interest rates in particular. In addition, there are global growth concerns as a result of the US government's erratic trade policy, which has led to a flattening of the yield curve in the last month.
- Overall, the environment for equity and credit markets remains favourable and inflation and long-term interest rates are still just under control, at least for the time being.

Chart: Rising US inflation expectations



Sources: Bloomberg, Fisch Asset Management

Positioning: Risk exposure neutral to slightly overweight

» Opposing forces act on government bonds

- As the global supply of liquidity has been rising again slightly for a good month, the environment for risky assets (equities and credit spreads) remains positive. The warning signals towards the end of last year due to the declining liquidity momentum at that time have diminished. We therefore remain neutral to slightly overweight in equity and credit risk exposure in all our strategies. Risk will only be reduced if warning signals increase again.
- The previous upward trends remain intact for the time being. However, various potentially worrying developments need to be monitored closely. These include the relatively poor equity market technicals ('distribution selling' by large investors in the US and weak market breadth). In addition, problems in the form of rising interest rates and inflation could also arise at any time from the economic upturn, which is being financed largely by high government spending. We therefore recommend allocating to equities via convertible bonds (rather than direct equity investments). Convertible bonds currently offer very interesting opportunities and an optimised risk/reward profile.
- We are currently keeping the duration of government bond yields in a neutral range due to opposing forces (rising inflation expectations coupled with global growth concerns). At the same time, the renewed rise in liquidity and upward wage pressure are leading to stubborn inflation. In addition, persistently high government spending, particularly in the US, could lead to upward pressure on interest rates for long-dated government bonds at any time. This also applies in Europe (France, Italy and the UK), while in Germany rising government spending and a reform of the debt brake can also be expected in the foreseeable future.
- However, the starting position for Swiss franc government bonds is much more favourable. Here, low inflation and a strong currency have a dampening effect on interest rates.

	US	Europe	Japan	Asia ex-Japan	LatAm	CEEMEA	Key:
Return drivers							
Equities	o	+ ↑	o	+ ↑	o	o	++ Strong positive market
Gov. Bonds	o	o	- ↓				+ Positive market
Credit IG (Spreads)	o	o		-	o	o	o Neutral
Credit HY (Spreads)	o	o		o	+	o	- Negative market
Total return							-- Strong negative market
Convertibles	o ↓	+	- ↓	+			
Credit IG	+	+		o	+	+	
Credit HY	+	+		+	+	+	
	PrecMet	InduMet	Energy				
Commodities	+	+ ↑	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) – Healthcare – CBs with high convexity – Bond-like CBs with quality credits and attractive yields – Balanced deep investment grade Chinese tech with high convexity 	<ul style="list-style-type: none"> – Utilities – Consumer discretionary – Unprofitable, early stage, expensively valued IT and biotech – Weak credit quality and/or liquidity – Cryptocurrency-related names
Global IG Corporates	<ul style="list-style-type: none"> – Financials, healthcare, leisure – EUR- and CHF-denominated issues – BBB-rated bonds 	<ul style="list-style-type: none"> – Transportation, utilities, capital goods – GDP- and CAD-denominated issues – AA-rated bonds
Global Corporates	<ul style="list-style-type: none"> – Healthcare, financials – BBB & BB-rated bonds – Developed markets & emerging markets investment grade 	<ul style="list-style-type: none"> – Transportation, utilities, chemicals – AA-rated bonds – Emerging markets high yield
Global High Yield	<ul style="list-style-type: none"> – Capital goods – Basic industry – Telecommunications 	<ul style="list-style-type: none"> – Transportation – Financial services – Technology & electronics
Emerging Markets - Defensive	<ul style="list-style-type: none"> – LatAm (Chile, Peru, Mexico), Eastern Europe – Utilities, metals & mining, oil & gas – Maturities 7-10 years 	<ul style="list-style-type: none"> – Asia, Middle East – China, Israel, Kuwait
Emerging Markets - Dynamic / Opportunistic	<ul style="list-style-type: none"> – LatAm (Brazil, Colombia, Mexico) – High yield energy – Short-dated high-yield bonds 	<ul style="list-style-type: none"> – Asia, Middle East – 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: US Treasury manipulates yield curve

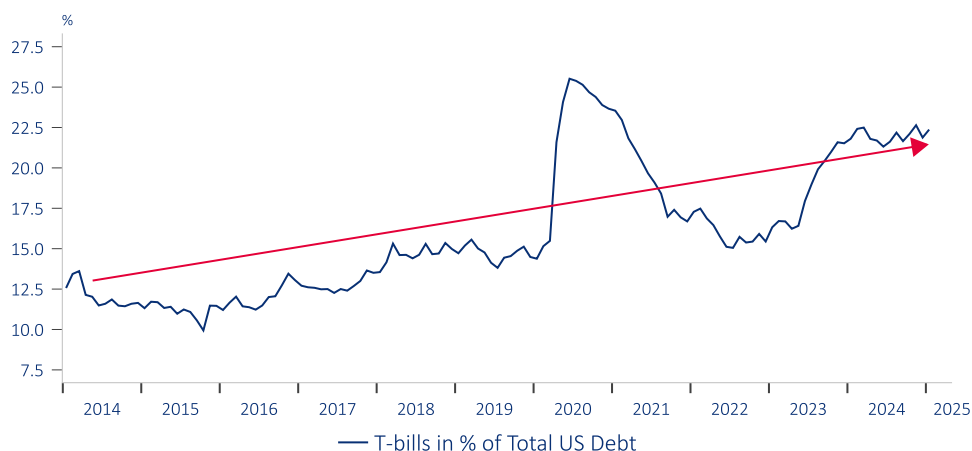
The new US Treasury Secretary, Scott Bessent, is currently acting as a kind of 'shadow Fed chief' and is specifically trying to prevent a rise in yields on long-term US government bonds - especially 10-year T-notes - or even achieve lower rates. He emphasised this in an interview at the beginning of February. This would be important as the rapidly rising national debt is continuously increasing the interest burden and now even exceeds military spending.

» The US Treasury spares the long end of the yield curve

In order to achieve this goal, the US Treasury under Bessent plans to finance new debt in the coming months primarily by issuing short-term T-bills, thereby reducing the supply of 10-year US government bonds. Bessent is thus continuing a successful strategy already adopted by his predecessor Janet Yellen. According to estimates, the increased issuance of T-bills instead of longer-dated government bonds has 'spared' the long end of the yield curve and pushed it down by around 100 basis points. This strategy is in fact indirect interference by the US Treasury in the Fed's monetary policy. It is remarkable that Bessent repeatedly criticised his predecessor for precisely this, and described the excessive debt financing via T-bills as unsustainable and even a 'time bomb'. Short-term T-bills must be refinanced annually.

However, the fact that Bessent is now continuing this risky financing strategy unchanged is a serious warning signal for long-term government bonds. He apparently fears that issuing too many 10-year US government bonds could lead to price losses or a sharp rise in yields - exactly the opposite of his objective. Bessent emphasises that lower interest rates are to be achieved through a combination of falling energy prices and a leaner government. However, this is unlikely to succeed without the help of the Fed (with QE instead of QT). An additional burden for Bessent at the moment is the Fed's balance sheet reduction (sales of government bonds or 'quantitative tightening').

Chart: The share of T-bills in US government debt is rising



Sources: U.S. Treasury, Fisch Asset Management

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