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NPB CIO Office Update

Quarterly Asset Allocation Views – Q4 2023

Executive Summary

- Financial markets during the summer period were under the usual seasonal influence of slowly but steadily increasing volatility, culminating in a bond melt-down towards the end of September, which also left its mark in other asset classes
- We continue to overweight money market investments given their still attractive pay-offs. However, we keep an eye on roll-over risk.
- In fixed income we slowly start extending duration risk after having been at the very short-end for several quarters now. We also increase credit quality of our exposure.
- In equities, we move to a cautious underweight, given the fragility of the current environment and an expected pick up in credit spreads.
- We like equity exposure to specific parts of Asia (India, Japan), but also continue to shun others (China)
- It is still too early to move exposure to precious metals up, but we are getting closer

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NPB Investment Committee

André Huwiler
Chief Investment Officer

Dr. Markus Hofmann, CFA
CEO, Partner
Global Head of Asset Management,
Trading & Advisory

Tom Govaerts
Managing Director, Partner
Head of Private Banking International,

Tim Pfister
Deputy Head of Asset Management

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CIO Office Global Scenarios

Geopolitical and macroeconomic assessment

	Base Case	Best Case	Worst Case
Russian War	Gridlock; neither side makes notable progress, war goes on	Ceasefire; peace talks	The US, to reduce its growing debt pile, ceases any financial support to Ukraine/NATO, leaving Russia space for a larger offensive
Energy	Global energy crisis is adverted; but structurally higher prices are a drag on global economic activity	Better infrastructure and faster than expected adoption of alternative sources keep fossil fuel prices low	Rising geopolitical tensions and chronic underinvestment in traditional energy sources cause prices to rise dramatically
(De)Globalisation	Rising protectionism leads to reshuffling of global supply-chain map (re-shoring, friend-shoring)	Globalisation continues unabated	Over-protectionism, trade-tariffs, etc. lead to a clear dampening of global growth prospects
Geopolitics	Sino-US relations remain tense, but the status quo prevails	US and Chinese diplomats find agreements on main friction points; newly found peace in Middle East leads to new era of global prosperity	Sino-US tensions escalate, with China invading Taiwan.
Economy	A recessions seems less avoidable now; global slowdown is orderly though, setting stage for the next growth cycle	Slowdown but no recession; inflation falls back to CBs long-term target level (~2%)	Hard landing, with unemployment quickly rising, forcing CBs to cut rates leading inflation spiralling out of control
Probability	*High*	*Highly unlikely*	*Tail risk; low probability*

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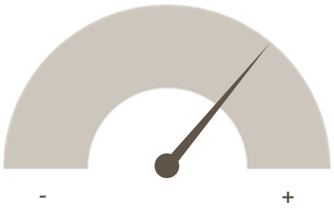
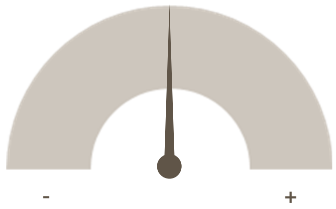
NPB Global asset allocation views (6-12m outlook)



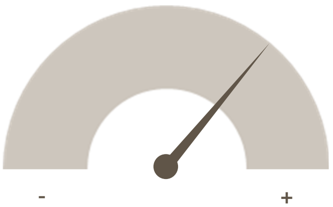
Cash & Money Market Instruments

We remain overweight money market instruments given the attractive risk-return dynamics, but are aware of the roll-over risk



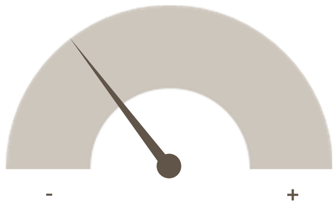
Precious Metals

High real rates are pressuring precious metals, but especially gold continues to deserve its allocation within a portfolio as an ultimate store of value



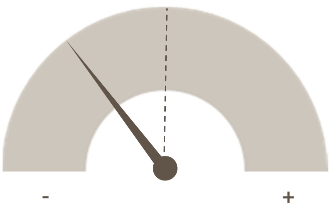
Fixed Income

We remain overweight fixed income, however, start shifting part of the allocation to the longer end of the curve. Simultaneously, we increase credit quality of the allocation meaningfully



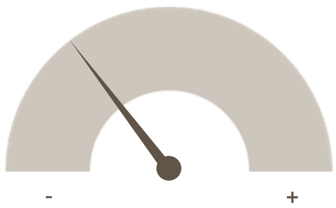
Commodities

Under our (downward) revised base case, it is still a bit too early for broader commodity exposure. However, longer-term risk remain to the upside (inflation, geopolitical turmoil, deglobalisation)



Equities

We move our equity exposure to somewhat underweight; we do not expect an outright "crash", but a too fragile situation combined with an unattractive Equity Risk Premium ("ERP") justifies a lighter exposure



Alternatives & Real Assets

Given illiquidity and probably still elevated valuations, we see no reason to expose ourselves to private markets for now. However, other alternative pockets, such as distressed debt, could be interesting over the months to come.

Current view   Previous view (if different)

NPB Global tactical views (6-12m outlook)

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Equities	View	Commentary
United States		While we move overall equity exposure to underweight, we think many parts of the US markets have corrected enough now to bring valuations in-line with the longer-term mean and move the allocation within the asset class back to neutral.
Europe		Europe may have recently beaten the US in golf, but in terms of stock market performance, our American friends keep the overhand. Europe's valuations are outright cheap, which raises the question: Cheap for a reason?
Switzerland		Given the defensive (healthcare, consumer staples) construction of the Swiss stock market, we move Switzerland to overweight, expecting more resilience during a downturn.
UK		The FTSE-100 has recently failed to move lower on negative news flow and has even started to outperform its global peers. Probably too much bad news has bombed out investors' sentiment, and the risk lies now for further (relative) outperformance.
Japan		Even though Japanese stocks are closing in on their all-time highs of 1989, it seems to us that global investors remain under-allocated to this market. Valuations remain attractive, warranting a continued overweight.
Emerging Markets		The US Dollar continues to be EM's Damocles Sword, however, given the currency's recent strength, we are encouraged by the resilience of emerging markets. Keep entire complex neutral but continue to make regional differentiation (see below).
China		Given structural problems (youth unemployment, real estate woes) in the Chinese economy, we recommend to leave this equity market as an underweight. Extremely negative sentiment, decent valuations and possible state-induced stimulus keep us from downgrading further.
India		Prospects for the country's economy remain bright, currently further strengthened by friend-shoring (e.g., Apple moving production from China to India). It continues to be a pricey stock market; however, investors seem willing to pay that premium.
Asia Ex-Japan		Year-to-date performance across the Asian plain is very mixed this year, but we continue to believe in the long-term prospects of the greater region. Newcomers to global financial markets, such as Indonesia, carry an execution risk, but also port great opportunities.
GCC Countries		The GCC area continues to be one of the growth "hot spots" globally, attracting foreign capital at a breathtaking pace. We continue to be overweight.

Underweight | Neutral | Overweight | ● Previous view (if different)

NPB Global tactical views (6-12m outlook)

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Fixed Income	View	Commentary
Government		We keep an overweight to government bonds and start actively increasing duration risk within this segment, given a) the recent jump in yields and b) our base-case recession view. However, we simultaneously keep a close eye on deteriorating government fiscal discipline.
Investment Grade		We keep an overweight and start increasing duration here too, but with a clear focus on the highest end of the quality spectrum.
High Yield		Given our economic base case view, we expect credit spreads to start rising meaningfully from here. As we are moving closer to the zone where previous, low-interest environment debt has to be rolled over at the new, higher rates, the risks increase for a further downgrade.
Emerging Markets		We keep EM debt at a neutral weighing for now, as many EM central banks were ahead of their DM peers during the inflationary cycle. However, we keep a close eye on local currency EM debt as the US Dollar continues to strengthen.
Duration		While we believe that global interest rates are in a secular uptrend, we think this cycle is coming to an end, which warrants a duration increase over the months to come.

Currencies	View	Commentary
Swiss Franc		Opposing forces are at work in the Swiss Franc. On one side, it seems the SNB may already be done with their hiking cycle, which could be a drag on the currency if other economies continue to hike. On the other hand, the CHF has a "safe haven" status during economic upheaval, which could remain a tailwind for the period we are entering. Keep overweight for now.
Euro		We keep a neutral weight on the Euro, but just about. A drop below 1.04 versus the US Dollar would likely trigger a technical "underweight" signal.
US Dollar		The logical explanation for recent US Dollar strength is the market's expectation of an increasing interest rate differential, as the Fed will keep a "higher for longer" policy, whilst other major economies, including the Eurozone, may be on the verge of cutting rates. We are slightly worried that something "darker" may lay behind the USD accumulation observed recently.
British Pound		Our GBP underweight has worked well over the past quarter, as the Pound gave back approx. 8% versus the US Dollar. From here, the path remains a bit less clear, though the technical pictures allows to keep an underweight for now.

Underweight | Neutral | Overweight | ● Previous view (if different)

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