INVESTMENT STRATEGY

3RD QUARTER 2024

Editorial
STATE DEBT: NORWAY OR THE UNITED STATES?

The economist's viewpoint
WE HAVE FAITH IN IT...

BCGE

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Editorial

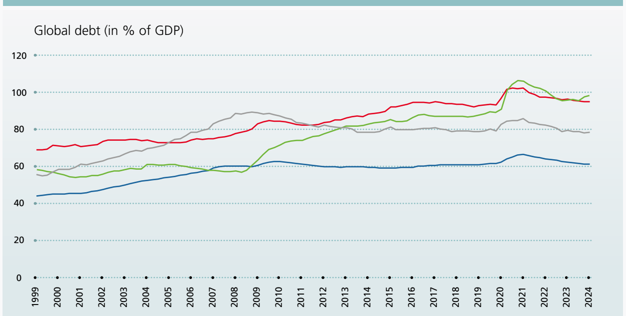
State debt: Norway or the United States?

Colossal, gigantic, abysmal... there is no shortage of superlatives to describe the level of debt of certain governments. Some are (re-)announcing a repeat of the crisis experienced in 2011 against the backdrop of the euro crisis. In a more measured tone, major institutions such as the ECB, the BIS and the IMF are also expressing concern. They point out that any increase in debt through public spending has to be financed by (tax) revenues, otherwise a downward spiral will ensue. What is particularly worrying is the uncontrolled increase in the net interest burden in relation to government revenues.

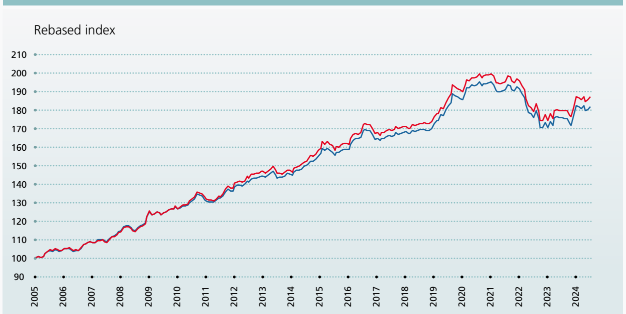
Let's put things into perspective. The figures estimated by the IIF (Institute of International Finance) assume a world GDP of around 93 trillion (93,000 billion!). At the end of May 2024, the combined debts of households, States and financial and non-financial companies amounted to USD 315 trillion, of which around 29% was government debt alone. In other words, three years of global economic output would not be enough to wipe out the debt accumulated by the global economy. What is striking is the particularly sharp rise in government debt (graph 1) since the financial crisis. Around a third of this global debt is securitised and held in institutional portfolios, whether government or private. Government debt is taking the lion's share, with the perverse effect that the more debt a government issues on the market, the greater its weighting in the investment universe as represented by benchmarks and benchmark indices. Passive investors therefore run the risk of being forced to finance the budget deficits of over-represented government issuers.

Alternative benchmarks based on fiscal quality exist. Through a rating system, the latter penalise the weighting of poor performers in favour of "better managed" States. In our example provided by Bloomberg, recent ratings range from 1.75 to 8. Consider the fiscal strength of developed countries, the South or Switzerland... Norway, with the best score, went from a weighting of 0.12% to 0.37%. While the notion of favouring countries according to their ability to finance deficits seems laudable, the results are not spectacular in terms of performance. Graph 2 compares the historical performance of a traditional benchmark with a benchmark based on fiscal quality. In our example, the currency effect has been neutralised to make the indices comparable. Despite the turbulence, over the period in question the gap is in favour of the "tax strength" strategy but has not really widened. The narrowness of the spread suggests that other corrective forces are at work in this highly liquid segment of the bond market.

Be that as it may, government debt will continue to be the subject of debate and will deserve our full attention.



— Households
— Non-financial companies
— States
— Financial companies



— Global Treasury - HEDGED USD
— Global Treasury Fiscal Strength Weighted - HEDGED USD

VALÉRIE LEMAIGRE
Chief Economist

The economist's viewpoint

We have faith in it...

KEY POINTS

1. Productivity as a growth driver for 2025; US at an advantage
2. The key to productivity: investment in intellectual property (i.e. R&D and technology)
3. Synchronised cycles and transitions will limit the impact of risks and fuel long-term opportunities

At a time when economic activity and inflation are still blowing hot and cold, and political and geopolitical risks are on our doorstep, the resilience of the financial markets is proving both surprising and worrying. The US stock market, represented by the S&P 500, saw prices rise by around 15% in the first half of the year, while the European and Swiss markets lagged behind at around 7%. The main factors behind this performance were a change of direction (albeit a timid one) by central banks, along with improved visibility and business prospects for companies. Of particular note is the continued dominance of leading US technology stocks, driven by the advent of artificial intelligence (AI). This has been spearheaded by the surge in Nvidia's share price, which has contributed over 30% to the S&P's performance since the start of the year. So, is this a technology bubble or Industry 4.0?

For the proponents of the technology bubble, the argument is based on Nvidia's market capitalisation, which now exceeds 3 trillion dollars (or nearly 10% of the annual income, i.e. GDP, of the United States) and has increased almost 10-fold in one year. However, this surge needs to be distinguished from the rise in industrial technology stocks such as Microsoft and Apple, which have finally reached the peak of their rise at around 30% since their 2021 highs.

For the proponents of Industry 4.0, the advent of AI is being considered a new form of productivity, a combination between that of machine and human productivity that could be deployed in particular in business (e.g. tax, legal) or personal (e.g. health) services; this is a new era that is being studied by the leading national and international research centres. The conclusions are not yet consistent, but they nevertheless suggest a major potential for accelerating productivity, based on a historically decisive pillar: investment in intellectual property, especially through R&D (e.g. fundamental academic and applied industrial research) and technology (e.g. software and databases).

Among the 2,500 global companies listed in 2022 as major contributors to applied research, US tech is among the top 10 investors worldwide (Microsoft, Apple, Meta, Alphabet, etc.). Nvidia was not yet at the top of this list in 2022 – the year ChatGPT was launched (November 2022). Fifty-two Swiss companies are represented in the list, in which the two Swiss pharma giants (Roche and Novartis) are neck and neck with the American pharma and tech giants. These major companies have clearly not been held back in their investments by the tightening of financing conditions and are already making a decisive contribution to future growth in the face of the economic cycle and structural transitions (i.e. demographic and energy transitions).

It should be noted that the scenario for 2025, described in our second-quarter publication, is based on the return of activity without excess, which will enable us to cope with the transitions recognised throughout the company, at the heart of essential innovations. *"Consequently, adjusting the outlook by an additional 0.5% to 1% of regional growth compared to current potential is not excessive. There will be surprises in growth momentum and phases of euphoria after the crises and depressed sentiment… ".* As far as this more dynamic scenario for 2025, **we have faith in it.**

The United States is once again showing a significant economic lead, fuelled by the productivity generated by investment in intellectual property. The United States' share of value added has continued to increase during periods of crisis and now accounts for a quarter of annual global wealth creation (i.e. GDP) to the detriment of the eurozone, which amounted to less than 14% in 2022. Despite the numerous questions surrounding the Chinese economy, the country has overtaken the eurozone and now stands at around 18%. Though doubts remain, having positioned itself in transition technologies and their essential resources, China is still a key and dominant player in international trade.

Over and above the cyclical factors that are multiplying signals of improvement in international trade and regional activity, attention is increasingly being focused on the responses to the structural challenges of major transitions. Central banks, under the scrutiny of financial markets, are grappling with this cyclical and structural complexity. The ECB and the SNB have begun to cut interest rates by targeting a so-called neutral level (with no impact on activity or inflation); the Fed has not yet ventured to do so. The fact that the interest rate cut did not take place at the same time on both sides of the Atlantic is because of different initial contexts and regional consequences, as well as the dissimilar nature of the systems at hand. The joint increase, on the other hand, was due to the global context at the time and its impact.

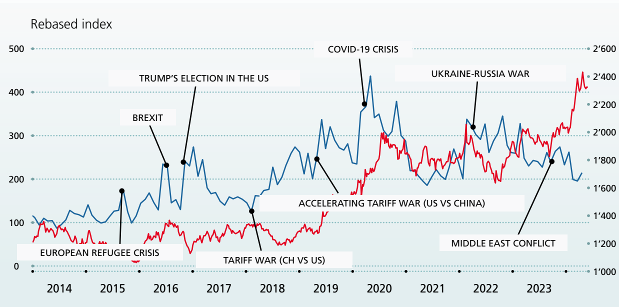
A return to a cost of risk that is lower than the profitability of industrial initiative (with the market swap rate curve straightened out) is part of a healthy rebalancing. For central banks, this means finding the right balance between moderating balance sheet management and easing interest rates. Accompanying the transitions underway and the challenges they create, such as: financing the ageing population, rising metal prices in Industry 4.0 and the energy transition, and increasing geopolitical tensions, requires a return to financing costs (i.e. interest rates) that are lower than the growth generated. This would make it possible to limit the increase in debt servicing, ensure its sustainability and avoid the snowball effect of the 1970s and 1980s when debt servicing automatically fed the increase in the budget deficit and public debt, without any additional expenditure. These factors illustrate the essential need for interaction and cooperation between regional and international authorities, as well as for trial-and-error analysis of the effects of the complex monetary and budgetary policies to be implemented. This is a context that is difficult to assess for voters, who have expressed their dissatisfaction and mistrust of the governments in power through their votes at the European and French ballot boxes. The electoral agenda will continue to sway sentiment for a few months yet as we await the US presidential elections. We're betting the current economic improvement will limit the impact of voters' indecision as long as neither the major currencies (i.e. dollar, euro and Swiss franc) nor the prices of key commodities and their transport, which are essential for both economic and structural growth, suffer a major shock.

The upward trend on the stock markets that began last November, which has so far been fuelled almost exclusively by technological innovations and intellectual property from the AI sector, has not yet reached its peak. The caution surrounding the Nvidia hype should not obscure the fact that other major American investors or companies that want to increase their productivity and thus their profitability have considerable potential. For the smallest companies (i.e. SMEs) – those that account for almost 70% of employment and 50% of value added – a monetary stimulus is needed to loosen the reins on financing. Switzerland and Europe have not yet benefited from the rate cuts initiated by their respective central banks. The need for more time, the political stakes involved and the controversial anniversary of the quarter-century bilateral agreements between Europe and Switzerland are all reasons for investors on the continent to be more cautious, reminding us that Europe is one of Switzerland's key industrial partners, with which it shares decisive economic stakes.

Beyond this political noise, which most observers see as a risk, the fundamentals of financial assets are solidifying, starting with corporate activity and profitability. This is in addition to the potential for acceleration that stems from the extension of productivity gains in most sectors. Confident that these markers of growth will be expressed in 2025, the volatility generated by the political agenda may provide an opportunity to increase portfolio exposure to sources of cyclical and structural growth. US companies in general, not just in the technology sector, are maintaining their competitive edge; the concentration of gains has been spreading to other sectors and types of companies. These positions will be strengthened over the coming months as opportunities arise among companies focused on innovation and its integration into processes to ensure their business' long-term future.

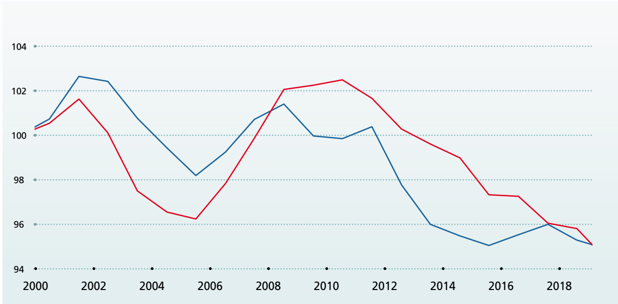
The financial markets have yet to decide between the technology bubble and Industry 4.0 even though they have not ruled out the possibility that some highly concentrated targets on the US market may be overvalued. This must be taken into account in risk management, even though the stock market cycle is far from complete and has not yet reached its peak. We have faith in it…

GLOBAL INDICATOR OF POLITICAL UNCERTAINTY



— Political uncertainties
— Gold, USD/ounce

UNITED STATES: LEVEL OF REAL GDP/CAPITA



— Eurozone
— Switzerland (RH scale)

Macro overview: Trend and scenario

Recent developments

Economic growth in the first quarter of the year came as something of a surprise to most Western economies. It was positive – with the exception of the Netherlands – and reached levels close to or above potential, with the exception of the United States, where the quarter saw a slowdown in activity, particularly in private consumption. As previously discussed, the beginning of the year was characterised by a normalisation of inventories, and as in 2023, companies and private households proved to be resilient, supported by budgetary policy.

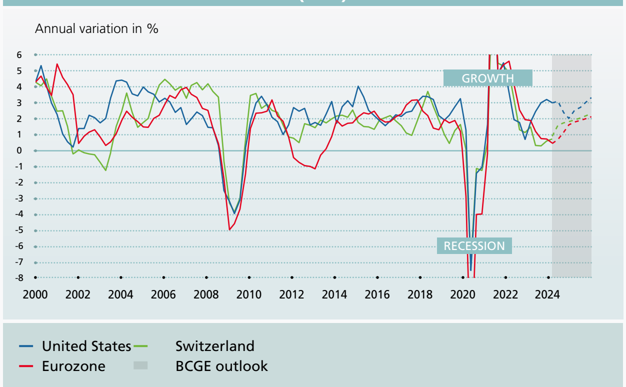
Following a sharp drop in inflation last year, price growth is no longer falling significantly. On the contrary, it has stabilised and is around 3% in the USA and 2.5% in the eurozone, with some countries at significantly higher levels (Belgium 4.9%, Spain and Portugal 3.8%, Austria 3.3%). Switzerland is the exception, with inflation stabilising at around 1.4%. In Europe, the ECB and SNB have both cut their key interest rates by 25 basis points in response to the economy's return to target. This all-clear signal, however, is one that the Fed has not yet given.

The economic outlook for 2024-2025

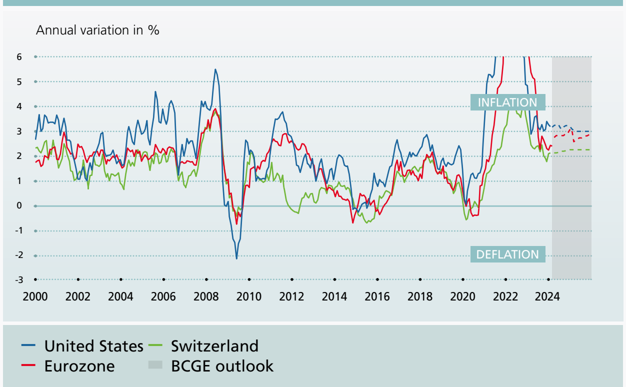
The first signs of cyclical recovery can be seen in international trade and the demand for resources that are essential for investment. Following the normalisation of activity in 2024, the road to recovery should solidify in 2025, gaining strength from past investment in innovation and associated productivity gains. The current boom in artificial intelligence, which can be integrated into a number of sectors, particularly services, means that optimising the combination of production factors (i.e. capital and labour) should enhance potential growth. In this respect, the United States increasingly stands out for the dynamism of its intellectual property investments, particularly those by the major technology companies, which, combined with massive public investment, serve to encourage private initiative. As a result of this industrial dynamism, the US has a solid labour market that feeds regular salaried income, the main source of private consumption. The United States' contribution to global wealth creation continues to increase, mainly at the eurozone's expense.

Inflation is sticky around current levels for a variety of structural reasons including limits on available production resources including labour and commodities. Depending on **monetary policies**, this is likely to remain the case in 2025. The search for an equilibrium rate should guide monetary policy throughout 2024 and 2025; it is the subject of debate among the major research institutes.

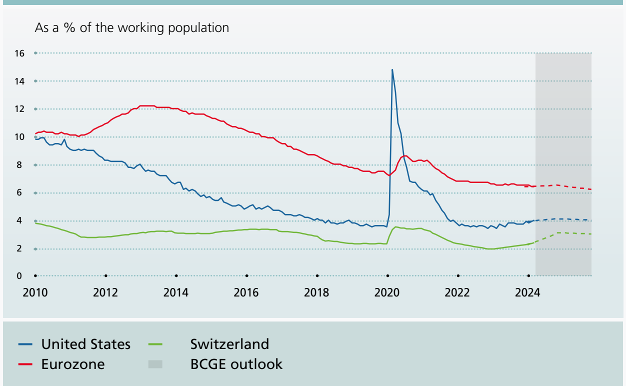
GROWTH IN NATIONAL WEALTH (GDP)



CONSUMER PRICE INFLATION



UNEMPLOYMENT RATE



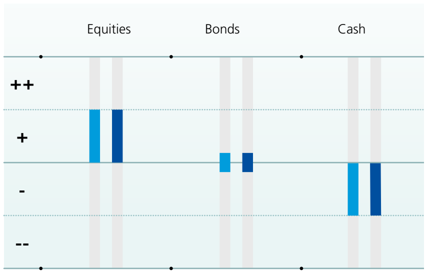
Market summary

Previous
Recent

ASSET ALLOCATION

- Asset allocation is based on companies. The increasingly broad participation of sectors and regions in the recovery is supporting the growth phase of equities. We are strengthening the allocation to equities through cash.
- Holding bonds has regained its virtues, and the debt of quality companies secures capital, with maximum preservation over its lifetime.
- Selection and conviction will enable us to capture the gains associated with improving productivity. Active management, which is less concentrated than passive management, makes a lot of sense when the profitability dynamic is expanding.

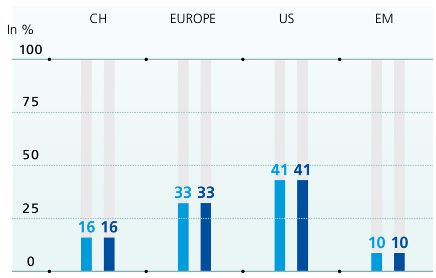
—• Increase the overweight position in equities.
—• Keep the weighting of bonds close to benchmarks.
—• Invest cash.



EQUITIES

- The earnings outlook for 2024-25 continues to improve, with normalisation allowing a return to fundamentals.
- Exposure should take account of cyclical and structural economic forces where the US has the edge; investment in intellectual property and innovation has been redoubled in recent years, particularly in the technology and pharmaceuticals sectors. Switzerland is holding its own; Europe is losing ground.
- China may disappoint with its cyclical and dogmatic stance, but it remains a key player.

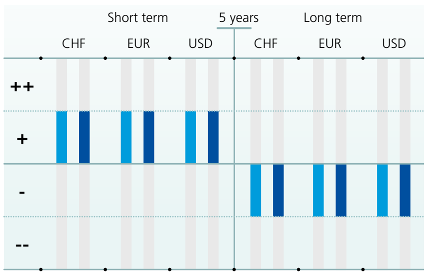
—• Increase US exposure to reflect its advance in technology while limiting the risk of concentration.
—• Maintain exposure to megatrends (e.g. IT, pharmaceuticals, industrials) and diversify further.



BONDS

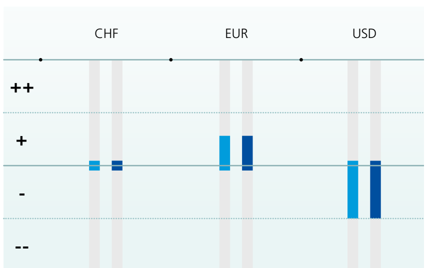
- The entire bond environment is now in normalised interest rate territory. Bond allocation will once again protect the capital of high-quality borrowers and restore long-term value to the portfolio.
- With inflation on a rigid downward trend, and growth and employment resilient, the yield curve will rise, mainly as a result of monetary policy. More than two years down the road, rates will remain closer to high levels.
- The price of credit risk is stable and historically low, reflecting solid fundamentals; this does not prevent us from maintaining rigorous selectivity to avoid any mishaps in the bond portfolio.

—• Maintain the less sensitive 5-year maturity benchmark.
—• Maintain high-quality bonds and limit corporate credit and liquidity risk.



CURRENCIES

- Apart from the fluctuations associated with electoral factors, the main currencies have not varied significantly from one another.
- The Swiss franc has been swinging back and forth relative to 2023 but remains highly sensitive to the SNB's monetary management (i.e. interest rates and liquidity).
- The systematic appreciation pattern of the Swiss franc against the euro could well change, despite the solidity of Switzerland's currency. Let us therefore remain cautious about a potential appreciation of the Swiss franc.

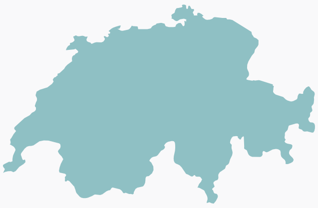


Outlook

ECONOMY		CURRENT		OUTLOOK	
		2023	MOST RECENT DATA* ANNUALISED VARIABLE	2024	2025
% GDP	SWITZERLAND	0.7	1.8	1.4	2.0
	EUROZONE	0.6	1.2	0.9	1.9
	UNITED STATES	2.5	1.4	2.5	2.8
	DYNAMIC GROWTH REGIONS	4.0	N/A	4.2	4.2
% INFLATION	SWITZERLAND	2.1	1.4	1.4	1.6
	EUROZONE	5.4	2.4	2.7	2.7
	UNITED STATES	4.1	3.4	3.4	3.1
	DYNAMIC GROWTH REGIONS	9.8	N/A	8.3	6.2

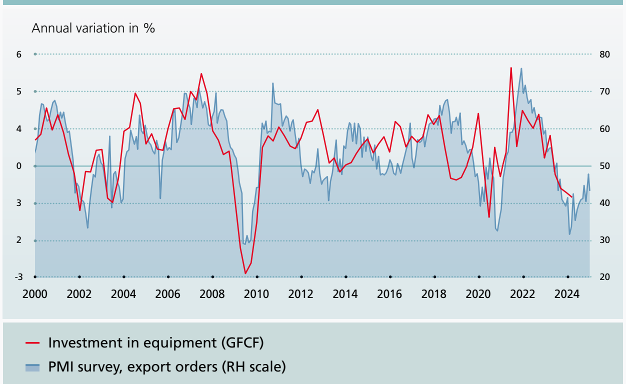
MARKETS		31/12/2023		31/06/2024		3 MONTHS	12 MONTHS
		VALUE	2023 %*	VALUE	% YTD		
% KEY INTEREST RATE	SWITZERLAND	1.75	0.75	1.25	-0.50	1.00	1.00
	EUROZONE	4.50	2.00	4.25	-0.25	4.00	3.00
	UNITED STATES	5.50	1.00	5.50	0.00	5.25	4.50
% 10-YEAR INTEREST RATE	SWITZERLAND	0.7	-0.9	0.6	-0.1	0.8	1.2
	EUROZONE	2.0	-0.4	2.5	0.5	2.5	2.5
	UNITED STATES	3.9	0.1	4.4	0.5	4.4	4.5
EXCHANGE RATES	USD/CHF	0.84	-8.8	0.90	6.8	0.90	0.89
	EUR/CHF	0.93	-5.6	0.96	3.6	0.97	1.00
	EUR/USD	1.11	3.8	1.07	-3.1	1.08	1.12
STOCK INDICES	SMI	11138	2.6	11994	7.7	11350	12700
	STOXX 600	479	11.3	511	6.8	490	535
	S&P 500	4770	23.9	5460	14.5	5000	5700
	MSCI EM	1024	6.9	1086	6.1	1000	1150
COMMODITIES	CRUDE OIL	78	-5.7	86	11.2	95	105
	GOLD	2065	14.0	2326	12.6	2350	2450

*For interest rates, values are expressed as a differential over the period.

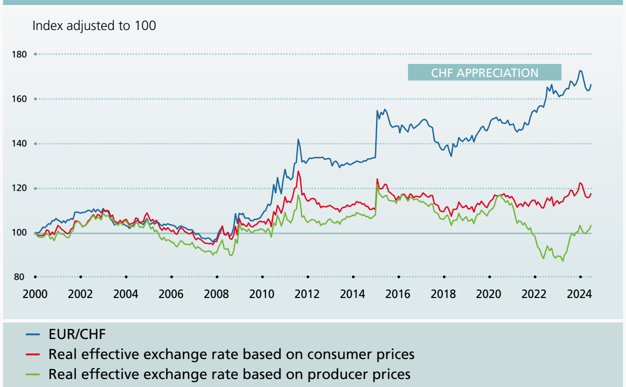


Switzerland
Macroeconomic trend

SWITZERLAND: ROLE OF EXPORTS IN INVESTMENTS



SWITZERLAND: VALUE OF THE SWISS FRANC



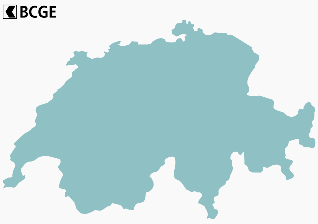
The role of bilateral agreements

At the start of 2024, Swiss economic activity grew at its historical average quarterly rate despite a decline in net exports, the traditional driving force. Domestic demand has been supported by private consumption, a sign of the resilience of households, which have been supported by buoyant wage income and savings that are once again yielding interest. Moreover, following the adjustments made in 2023 to meet the rising order backlog that started last summer (especially in the pharmaceutical sector), company inventories can now be replenished. Growth normalisation is taking hold.

The outlook for businesses is gradually brightening and visibility is improving, allowing capital spending to pick up again this year, despite the fact that construction is still suffering from the slowdown in mortgage lending following the tightening of financing conditions. The resumption of international trade and the reopening of bilateral negotiations with Europe are key factors for future economic growth. In the midst of a demographic, technological and energy transition that extends far beyond our borders, it would be dangerous to stray from the industrial guidelines of our largest market. Bilateral trade in the chemicals and pharmaceuticals sector, which accounts for over 30% of Swiss exports, must be able to rely on commercial, academic, research and development exchanges, which are already severely limited by the expiry of bilateral agreements in place since 2004 and the lack of a satisfactory alternative. Europe is an indispensable partner for Switzerland in terms of trade, the exchange of labour, and access to joint research programmes including Horizon and Iter and in quantum physics. The resumption of discussions is therefore essential to prepare for future economic growth in Switzerland, whose productivity advantage depends on R&D and the optimisation of its industrial model.

For several months now, monetary authorities have been satisfied with **price inflation**, which is anchored within the fluctuation range of 1-2%. The rate cut initiated in March and confirmed in June left the SNB's benchmark rate at 1.25% and was bolstered by the appreciation of the franc in June, which took place against the backdrop of the European elections; this proved an opportunity to take profits on holdings of foreign assets and a source of the franc's temporary appreciation against the dollar and the euro. Lastly, we should not forget that falling import prices are not independent of agreements with Europe; customs duties or electricity prices could upset the SNB's benchmarks.

MACROECONOMIC DATA: SWITZERLAND		2024	2025
% GDP		1.4	2.0
% INFLATION		1.4	1.6
% UNEMPLOYMENT RATE		3.1	3.0
% KEY INTEREST RATE		1.00	1.00
% 10-YEAR INTEREST RATE		1.20	1.30
USD/CHF		0.89	0.86
EUR/CHF		1.00	0.96
SMI	INDEX	12000	13500
	EPS	10%	19%
	P/E	17.3	18.1

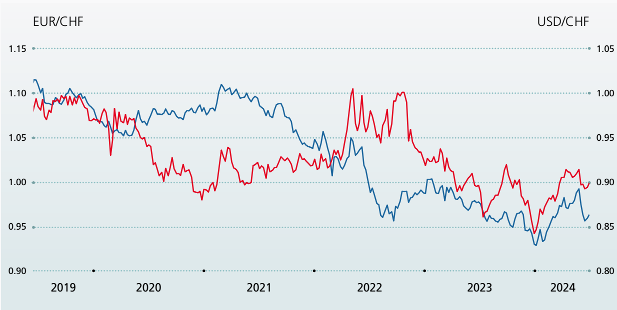


Switzerland
Interest rates and exchange rates

SWITZERLAND: INTEREST RATES

— 10-year Swiss government
— SARON

SWITZERLAND: EXCHANGE RATES



— EUR/CHF
— USD/CHF (RH scale)

Short-term rates: the SNB in action

In June, the SNB cut rates by a further 25 basis points, taking the benchmark rate to 1.25%. The SARON adjusted, ending the first half of the year at 1.21%. The 2-year rate continued to anticipate further key interest rate cuts, ending the quarter at 0.82%. Despite the SNB's search for an equilibrium or neutral rate above 1%, it would appear that the markets are considering a return to a key interest rate close to or below 1%. This is also our target.

Long yields: below the lows

During the second quarter, medium- and long-term Swiss government yields fluctuated within a range of 30 to 40 basis points, returning at the end of June – after the SNB cut – to the lows reached last December. This final half-year drop in Swiss government risk-free rates also set the trend for swap rates. However, this normalisation has not hurt risk premiums on corporate debt, with the risk premium on Investment Grade (IG) remaining close to record lows (80 basis points between top quality AAA and bottom quality BBB). There is no doubt that this time the cut in key interest rates is not triggering a risk of lost business and hence of credit risk.

More than a reaction to economic data on activity, inflation or monetary policy, the drop in rates observed reflects investment preferences, particularly among large institutional investors, who have not hesitated to rebuild bond holdings in their portfolios after benefiting from attractive short-term money market yields.

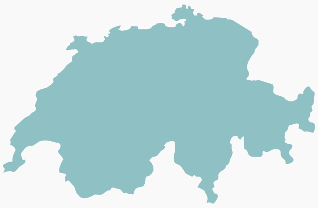
Franc: predefined fluctuations?

The franc's continued depreciation at the start of the second quarter finally came to a halt at the end of May, giving way to a rapid appreciation until 19 June, the day before the SNB cut interest rates. By the end of June, the franc had depreciated by 7% against the dollar, compared with 3.7% against the euro since the start of the year.

The franc has maintained an appreciation of around 4% against the euro since its most volatile peaks of 2022; nevertheless, adjusted for price differentials, the franc has been remarkably stable or hovered within a limited margin of fluctuation against its partners for almost a year. Back-to-back elections in Europe have helped keep the franc strong but haven't triggered any clear new trends. June's celebration of a quarter of a century of access to the European market reminds us of the importance and interdependence between Swiss and European companies, starting with the pharmaceuticals and chemicals sector, which dominates international trade and the creation of value added in the Swiss manufacturing industry.

The resumption of bilateral negotiations could have a positive impact on a number of crucial economic issues, not to mention R&D and innovation programmes, university and academic collaboration, and the reservoir of European labour needed to maintain Swiss activity against a backdrop of a shrinking workforce.

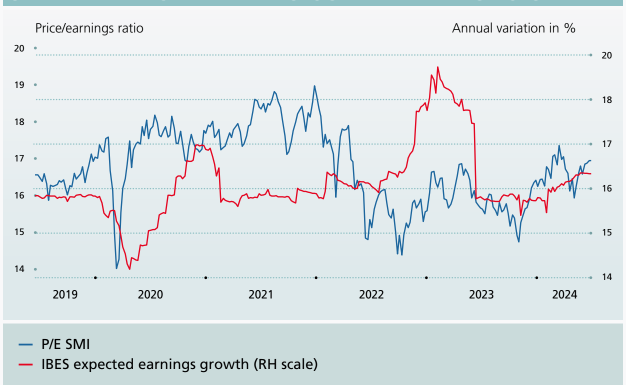
Monetary policy is the key to stabilising the franc's exchange value against its economic partners. Structural economic issues with Europe must be addressed because the franc's status as a safe haven is not guaranteed.



Switzerland
Stock market

SWITZERLAND: STOCK MARKET INDICES

SWITZERLAND: FUNDAMENTAL STOCK MARKET INDICATORS



Expected recovery in the second half of the year

2024 got off to a timid start for Swiss companies, with volumes under pressure and less power to raise prices after an intense period. The second quarter should see a sequential improvement. Companies are nonetheless more optimistic about this second half of the year, thanks to full order books and normalised inventory levels. This is particularly true of the semiconductor industry, which will be bolstered by major investments in memory production capacity.

Construction is still suffering from the weakness of the residential sector but remains buoyed by infrastructure and certain niches, such as data centres. The automotive sector, which is under pressure, is seeing little improvement, with no hope for the rest of the year.

Valuations are above their historical averages: 17.7x for the SMI and 20.7x for the S&M Caps. The S&M Caps' valuation premium is now 17.1%, below its historical average of 21.3%. At this stage, valuation no longer seems to be providing support for equity performance; earnings will have to pick up the slack.
The consensus has revised its growth expectations for 2024 upwards from +10% three months ago to +12%. The consensus is very heterogeneous by sector; it seems to us to be particularly optimistic for financials and overly cautious for industrials and healthcare.

With volume recovery likely to take shape in this second half of the year, we will be looking to gradually increase our exposure to small and mid caps, which are more sensitive to the cycle and to improved financing conditions.

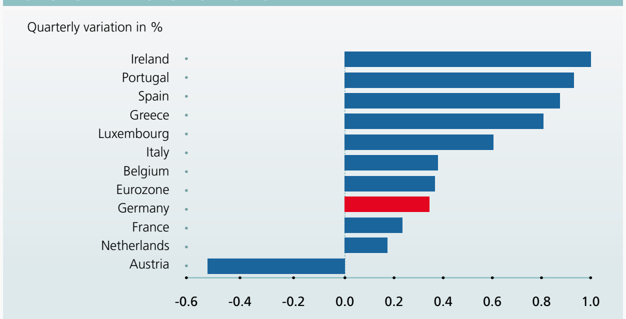
KEY TAKEAWAYS

- The resilience of the Swiss economy is showing itself and its outlook brightening, driven by exporting companies. After the current normalisation, growth should be sustained and productivity gains from investment in innovation and research should be maintained in 2025.
- Inflation is under control. The SNB confirmed this fact with a second key interest rate cut in June. A return to around 1% of the reference rate has become a near-term objective.
- Asset allocation should continue to focus on value creation by quality companies and long-term themes.
- The outlook for Swiss earnings in 2024 and 2025 is improving, supported by productive investment efforts; S&Ms are well positioned to take advantage of it.
- Bond investments can once again generate income and value over the long term.
- The franc is under pressure from the SNB's balance sheet management but should remain a strong currency in 2024-25.

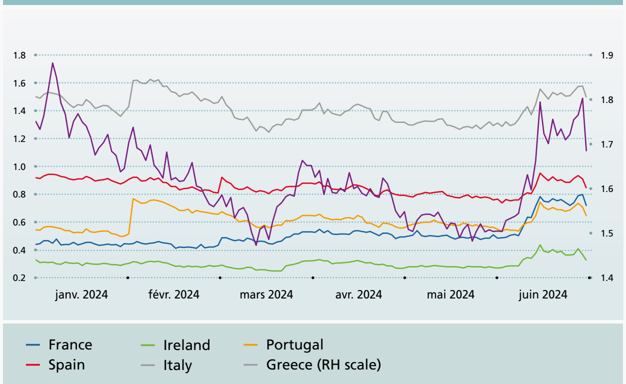
BCGE

Eurozone
Macroeconomic trend

EUROZONE: EVOLUTION OF GDP



10-YEAR BOND YIELDS: GAP WITH GERMANY



Behind the political tree lies...

European growth may have passed its inflection point at the start of 2024, rising at an annual rate of 1.2% in the first quarter. Germany is back on the growth track and the countries in Southern Europe are making rapid progress. Ireland dominates the rankings, with an incredibly high level of activity reflecting the uninterrupted digital and pharmaceutical dynamic.

Recent export indicators are picking up, and by giving companies a brighter outlook, they could stimulate much-needed European productive investment to close the gap with the giant on the other side of the Atlantic. The race for R&D investment is important for all regions but particularly for Europe, which is largely exposed to international trade dominated by the main sectors that initiate applied research: information and communications technology (ICT), pharmaceuticals, and automobiles. Europe participates in the ranking mainly through the automotive sector and through leading German companies, while the United States has gained a significant lead in the ICT and pharmaceuticals sectors. These strategic choices have continued to affect Europe's share of global wealth creation, to the benefit of the United States. Given that growth potential is heavily dependent on innovation and productive investment, it could remain constrained and the gap widened even further. The German automotive sector has probably not lost the battle for good against leading electric vehicle retailers Tesla and Byd, thanks to Volkswagen, the leading R&D investor.

Following the normalisation of inventories this year, growth in 2025 will rely on the value added by industrial companies; private consumption should continue to rise moderately thanks to wage increases and rising interest on high savings.

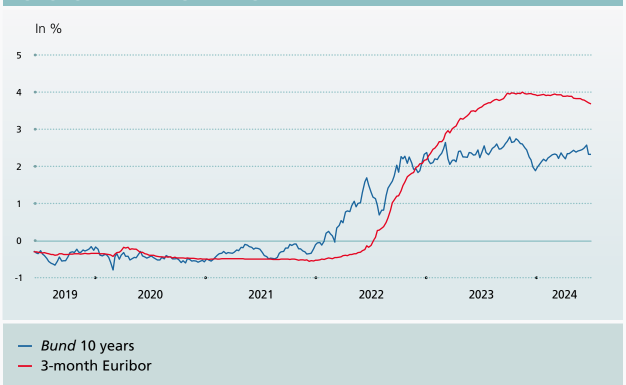
ECB: easing begins

With inflation closer to target at 2.55%, the ECB began its monetary easing by cutting key interest rates by 25 basis points, signalling some easing in the face of wage growth. This does not mean that the ECB will not continue to monitor the situation closely. However, the question of how to best adapt financing conditions for SMEs is crucial in an environment where cyclical and structural issues are converging toward a common investment and innovation solution.

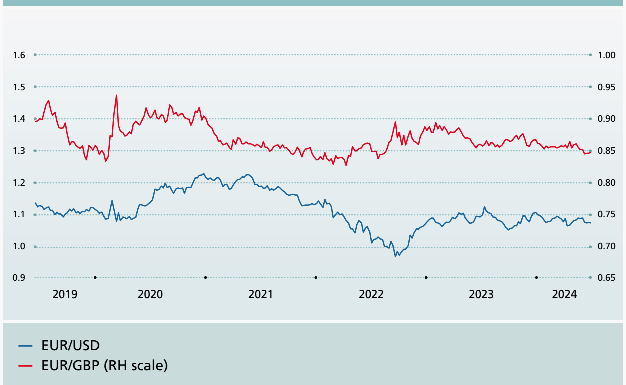
MACROECONOMIC DATA: EUROZONE		2024	2025
% GDP		0.9	1.9
% INFLATION		2.7	2.7
% UNEMPLOYMENT RATE		6.5	6.2
% KEY INTEREST RATE		3.00	2.75
% 10-YEAR INTEREST RATE		2.50	2.80
EUR/USD		1.08	1.12
STOXX 600	INDEX	515	570
	EPS	6%	13%
	P/E	13.5	14.0

Eurozone
Interest rates and exchange rates

EUROZONE: INTEREST RATES



EUROZONE: EXCHANGE RATES



Short-term rates: no surprise here

In the second quarter, short-term rates changed very little, hovering around 3% for 2-year rates as the markets awaited a cut in ECB rates. Monetary easing is likely to continue and the reference interest rates should ultimately tend to hover around 3%; the interest rate corridor is currently still in the region of 4% in the case of the ECB refinancing and deposit rate. When setting the equilibrium interest rate (with no impact on economic activity or inflation), the ECB analyses the transmission of its monetary policy in advance. However, the efficiency of the transmission channels has decreased over the last ten years, particularly due to the deleveraging of companies and private individuals, the tight labour market situation and low interest rates. All of these indicators could tempt the ECB to raise its estimate of the equilibrium interest rate.

Long rates: electoral impact

The ECB's interest rate cut, which was widely anticipated by bond traders, did not disrupt the medium- and long-term yield curve. Quarterly fluctuations in German 5-, 10- and 30-year yields were limited to around twenty basis points. Volatility was more pronounced on the government debt of the most indebted countries. Indeed, the European elections on 9 June enshrined the rise of far-right parties in Parliament (reaching almost 30% of the vote), setting off tensions, particularly in France where the National Assembly was dissolved by Emmanuel Macron. Most of the region's high-debt countries saw their risk premiums rise by around 20 to 25 basis points. During election periods, the currency is generally the receptacle of worried sentiment. The existence of a common currency shifts risk onto the cost of regional debt. The easing seen at the end of the quarter confirms our 10-year interest rate targets, which we expect to hover around current levels over our investment horizon.

Euro: unaffected by election results

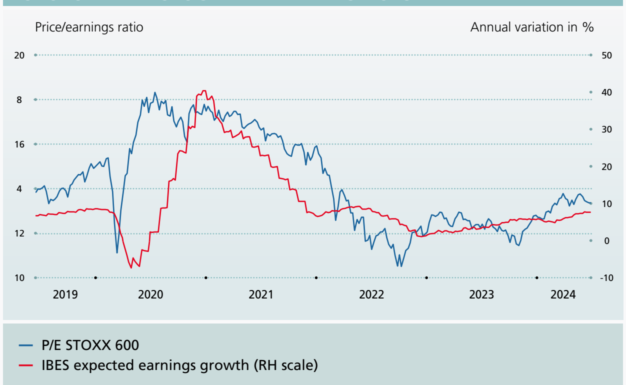
In the second quarter, the euro moved little against its main reference currency, the dollar, proving far removed from the electoral news on both sides of the Atlantic. Since the start of the year, the euro has lost 1.5% against the dollar and appreciated against Scandinavian currencies. It is stable against its partners, with no comparative advantages. It has to be said that the common currency has weathered the electoral headwinds remarkably well.

Economic and financial flows are once again proving to be quite favourable for the eurozone in view of the fact that it can once again report a current account surplus (thanks to lower gas prices), as well as the fact that interest rates are low and European integration has hardly been disrupted by the election results. Fluctuations in the euro are therefore essentially linked to price differentials with its partners. More than the weakness of the euro, it is the strength of the dollar that has had to be questioned since 2015, while the depreciation of the euro against the Swiss franc reflects an adjustment to the price differential between the eurozone and Switzerland in the case of consumer prices.

Eurozone
Stock market

EUROZONE: STOCK MARKET INDICES

EUROZONE: KEY STOCK MARKET INDICATORS



On hold

The second quarter ended with an anaemic European market. Overall, the results of European companies in the first quarter were rather mediocre; 37% of companies surprised in terms of earnings, 59% in terms of profits. A few firms exposed to automotive suppliers issued profit warnings. Absorption of excess inventory in this sector should ease in this second half of the year. Some companies have reported that geographically, business is in a "wait and see" mode, particularly in the United States, while China is being described as very weak. Europe may have reached its inflection point.

Targeting opportunities

The seeding sector should show an inflection point from the second half of 2024, driven by a recovery in memory and utilisation rates. For 2025 and beyond, hyperscalers, intelligent networks and 2nm nodes remain powerful levers. In life sciences, order books are pointing to a recovery after a long period of destocking.

Ambitious consumer expectations

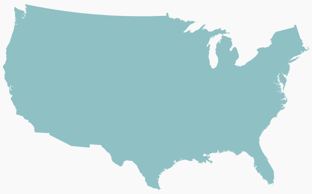
The consensus expectation for 2024, which had decreased to 4%, is now at 5%, driven by financials, healthcare and materials. The 2025 consensus of 10% looks ambitious, particularly for consumer discretionary and durable goods.

Timid rebound for small caps

In contrast to the first quarter of 2024, the valuation of small caps rose during the second quarter, while that of their large-cap counterparts fell.

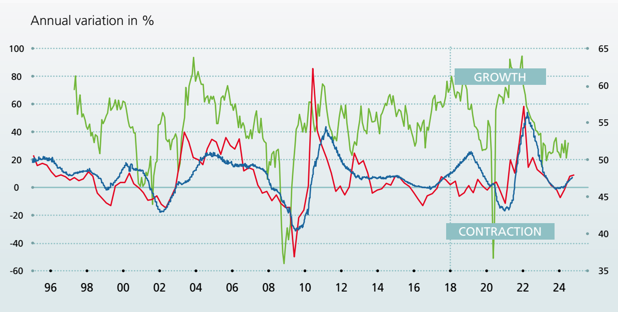
KEY TAKEAWAYS

- In 2024 and 2025, growth will be on a road to recovery. It should gain strength, driven by investment and associated productivity gains. Employment is resilient and structural transitions should support activity, especially with the easing of financial conditions.
- Consumer price inflation is stable at around 2.5%, allowing the monetary easing cycle to begin. The path toward monetary neutrality in relation to activity should continue into 2025.
- The normalisation of interest rates speaks for a comeback of bonds in portfolios. While awaiting growth to be confirmed, limit duration and credit risk through quality.
- The moderate allocation in favour of value creation based on innovation by quality companies is to be maintained. Its extension to other sectors should enable broader diversification over the course of 2024-25.
- The euro is fluctuating within a range of fundamental fluctuations linked to price differentials. The euro does not have enough strength to warrant the appreciation that its external surplus could have justified.



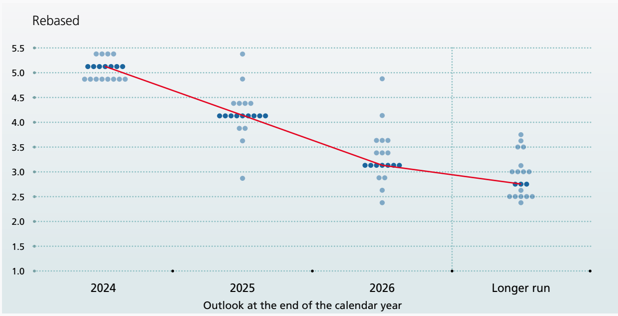
United States
Macroeconomic trend

UNITED STATES: CORPORATE PROFITS AND BUSINESS SENTIMENT



— S&P 500 earnings per share
— Profits of all companies in the economy
— ISM survey of business sentiment (RH scale)

UNITED STATES: FOMC MONETARY POLICY OUTLOOK



• June 2024
— Median

A loss of momentum

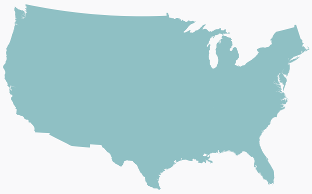
The slowdown in activity figures for the first quarter of 2024 conceals mixed domestic fluctuations. Consumer spending has slowed, mainly as a result of restrictions on durable spending linked to housing and access to it (i.e. cars), but other consumer spending is holding up well. The company is continuing to invest at a pace that favours technology and software, with annual growth approaching 10%. On the other hand, on the basis of short-term indicators, there may be some loss of momentum this summer if we are to believe domestic survey indicators which point to a levelling-off after the recent momentum.

In 2024, with inventories returning to normal and the momentum generated by investment in innovation and technology, growth should be taken up by all sectors and by smaller companies. An analysis of the United States' position in the 2022 R&D investment rankings reveals the dominance of companies in the information and communications technologies sector and in the pharmaceuticals sector. In the space of ten years, investment in these strategic sectors has more than doubled. Alphabet, Meta, Microsoft and Apple are at the top of the list, with pharmaceuticals giant Pfizer also contributing. This concentration of companies on an economic and stock market scale should not, however, overshadow the contribution of smaller companies. The integration of the innovations produced and developed by the giants should fuel an increase in growth potential which, in our view, could already be boosting business momentum by 2025. A helping hand from the monetary authorities to ease financing conditions by cutting interest rates would be most welcome for this category of business, which is more dependent on bank credit.

Inflation: back at 3%

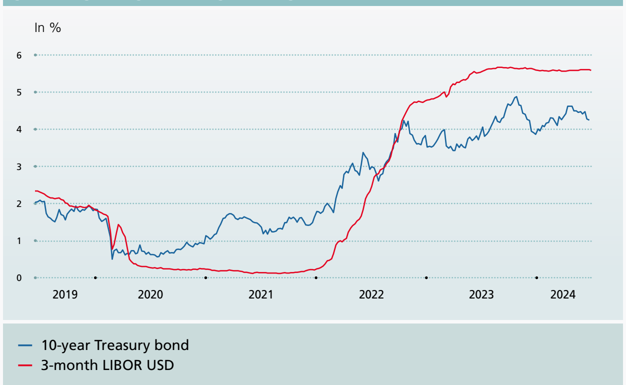
Since a year ago when US inflation fell below the 3% threshold, it has been hovering around these levels. All service prices are rising at this rate, with resilient pressures gradually easing. The Fed, hitherto cautious about easing key interest rates, should be reassured. The economic symposium in Jackson Hole at the end of August will give us an indication of the next monetary policy decisions, which should bring benchmark rates closer to 4% by the end of 2025, the level of an equilibrium rate that will allow the cost of financing to fall below the profitability levels of the smallest companies, SMEs.

MACROECONOMIC DATA: UNITED STATES		2024	2025
% GDP		2.5	2.8
% INFLATION		3.4	3.1
% UNEMPLOYMENT RATE		4.1	4.0
% KEY INTEREST RATE		4.50	4.25
% 10-YEAR INTEREST RATE		4.50	5.00
EUR/USD		1.08	1.12
S&P 500	INDEX	5400	6200
	EPS	10%	20%
	P/E	21.6	22.9

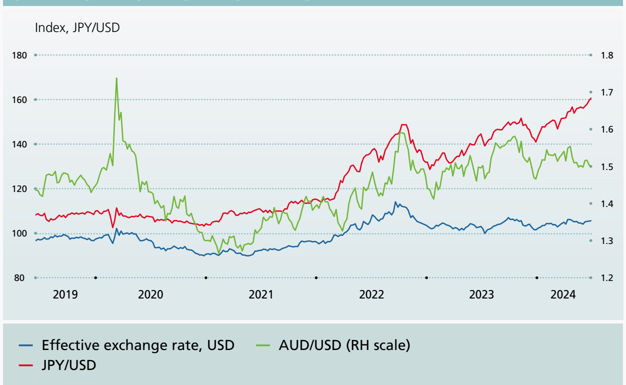


United States
Interest rates and exchange rates

UNITED STATES: INTEREST RATES



UNITED STATES: EXCHANGE RATES



Short-term rates: a slackening of expectations

With the exception of 3-month Treasury rates, which remained stable over the second quarter, short and long maturities fluctuated within a range limited to 40-50 basis points. After disappointing investors for many months, the bond markets were busy waiting for the Fed to signal its first rate cut. Once initiated, short maturities will move toward the equilibrium rate, estimated at around 4% for 2025, in line with sticky inflation assumptions of around 3%.

Long-term interest rates: similar fluctuations

There will be no major fluctuations on long Treasury maturities since inflation expectations remain anchored. The diversification of foreign exchange reserves by certain Asian central banks over the last few months and the issue of US budget debt, which has arisen as a result of the elections, have rekindled the debate about the abundance of US debt on the secondary bond market. No trend has emerged from these questions. The slope of the yield curve (the difference in yield between 2- and 10-year maturities), which is still inverted, has remained stable, a source of uncertainty for smaller companies looking to invest productively in the future. Short rates will have to come down to normalise the curve.

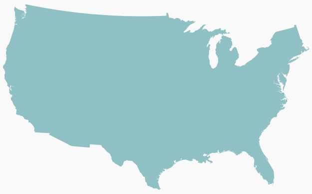
On the corporate debt side, risk premiums remain at their lowest for the highest quality segments. For their part, lower-quality debt (i.e. High Yield) recorded fluctuations limited to 20 basis points, proof that the economic context remains solid.

Dollar: normalisation

The dollar's ups and downs over the second quarter show once again that the normalisation of 2024, which began with the economy, is gradually affecting all financial assets. Back on its 2022 highs, the dollar is stabilising against its trading partners, taking account of inflation differentials between regions. Since the start of the year, it has appreciated 1.5% against the euro, and the depreciation of the Swiss franc has pushed the dollar 6.5% higher.

The return of inflation differentials to a normalised range (1 to 2%) between the major economies has not led to significant fluctuations in bilateral rates, resulting in a stabilising of the dollar index.

Beyond these fluctuations driven by investor expectations, the twin US deficits (fiscal and external) remain massive and the strength of the dollar a handicap. The depreciation of the dollar can only be prevented by compensatory capital inflows. The financial attractiveness of US assets is essential to maintaining the dollar's strength, which may be limited by the forthcoming fall in interest rates and the concentration of stock market investments. The return of the dollar's fundamental cyclicality should rekindle fluctuations in favour of some depreciation, which could take it to EUR/USD 1.12 without triggering a new trend. The dollar's dominance in international trade and finance, although regularly questioned, should keep it above its fundamental value.



United States
Stock market

UNITED STATES: STOCK MARKET INDICES

UNITED STATES: KEY STOCK MARKET FACTORS

All-in on artificial intelligence

The US market hit an all-time high, still buoyed by a handful of technology stocks linked to artificial intelligence. Over the quarter, the market gained 4.05%. Nvidia, the company enabling the development of new AI models, contributed 44.6% of this performance.

From euphoria to maturity

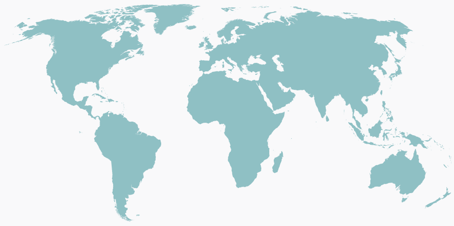
The history of financial markets shows that investors' optimism of innovation is often correct but lacks temperance. The internet bubble of the 2000s is an example of this. Fortunately, the monetisation of AI should be quicker, but the question of who the winners will be will persist until the whole market benefits. Stock selection will have to avoid the herd effect in order to position the portfolio properly and avoid any incongruous volatility.

Active asset management benefits

Under these particular conditions, funds that replicate indices are exposed to the risk of high concentration in a few stocks. To benefit from the maturity phase of AI, the winners will be companies integrating applications to boost productivity (e.g.financial, industrial, consumer) or those to improve their products or services (e.g. pharma, medtech). These conditions offer opportunities to diversify portfolios by reducing the risk of concentration. Moreover, by 2025, earnings growth is expected to be more uniform across all sectors (14.5%) and across an index of equal weighting (15.9%). There is valuation potential.

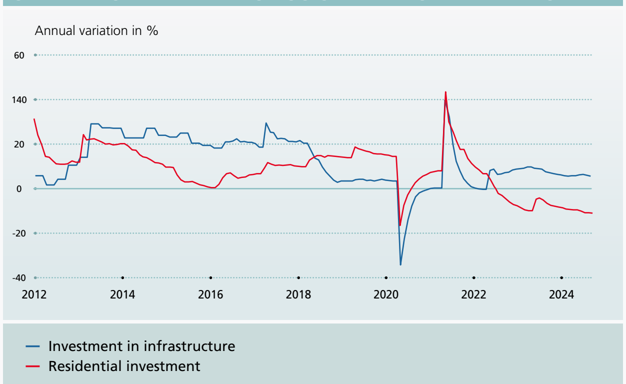
KEY TAKEAWAYS

- The current downturn does not reflect any major weaknesses but rather necessary breathing space for companies as they normalise inventory management. In 2025, the benefits of the easing of financing conditions and the productivity of past massive investment should expand growth across the board.
- With inflation back close to 3%, sticky inflation should not prevent the anchoring of expectations. The Fed should be able to start easing official interest rates toward equilibrium levels close to 4%.
- As long as there are no curve balls, bond assets should once again demonstrate their fortes of capital protection and standardised yield. They are building longer-term portfolio value.
- The earnings outlook for 2024-25 remains attractive and the US market's lead due to increased investment in R&D over the past ten years is now clearly evident. Opportunities arising from quality technologies exposed to transitions should spread to other sectors, allowing broader diversification to maintain an even more moderate bull market.
- Fundamentals and the financial context are fuelling limited swings in the dollar, which continues to dominate international commercial and financial transactions.

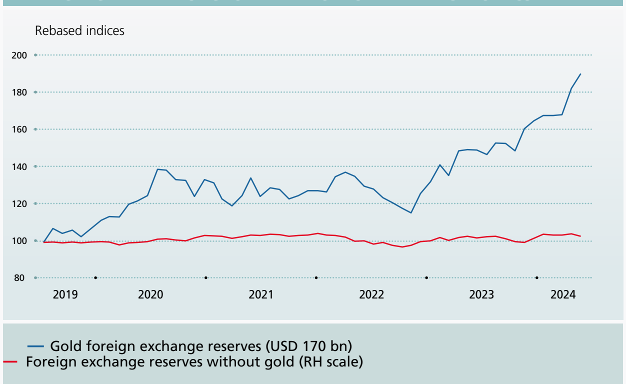


Dynamic growth regions
Macroeconomic trend

CHINA: INVESTMENT IN INFRASTRUCTURE AND RESIDENTIAL INVESTMENT



EMERGING MARKETS: GLOBAL EXPORTS AND ELECTRONICS



Battling the headwinds

China, a key player, remains at the centre of attention because of its economic position. The recovery in retail sales growth and fixed capital investment in manufacturing are encouraging signs. Export growth accelerated sharply thanks to the global technology cycle and resilient foreign demand. Nevertheless, real estate activity remained in sharp contraction, pushing up housing prices. The government's contribution to infrastructure and local financing, weakened by real estate, remains China's Achilles heel, with implications for private players.

The issue of rising tariff barriers in the United States is at the heart of the concerns of Chinese and Asian manufacturers. With a tariff of 60%, the direct costs could reach as high as 2.5% of GDP according to some estimates. On the other hand, as in recent years, expansion into other markets and the relocation of production chains through foreign direct investment are underway, particularly benefiting Mexico.

According to the latest UNCTAD study on international trade, which includes an observation of the first quarter of world trade, trade is picking up, with certain regional and sectoral disparities. The regions and sectors most exposed to energy transitions (e.g. batteries, solar panels, electric vehicles) and AI (e.g. high-end semi-conductors) are benefiting. Other indicators are recovering, notably those concerning freight transport. World trade dynamics are being reshaped by responses to the production chain and geopolitical tensions, raising tariff risks. While China is being targeted, other regions, including Latin America and certain countries in Europe and East Asia, may see opportunities to take their place in the supply chain of prized and concentrated sectors. The fragmentation of international trade is reshuffling the trade cards but has not reduced its volume, which is again up by 3% year-on-year.

In an economic environment marked by industrial recovery, where the driving force is companies investing in the major transitions underway, the continuation of international trade is crucial, even if the introduction of heavy tariffs will encourage companies to bypass restrictive markets.

MACROECONOMIC DATA DYNAMIC GROWTH REGIONS		2024	2025
% GDP		4.2	4.2
% GLOBAL TRADE		3.0	3.3
% INFLATION		5.8	4.4
MONETARY POLICY		EASING	STABILISATION
MSCI EM	INDEX	1050	1250
	EPS	17%	28%
	P/E	12.5	13.2

Dynamic growth regions
Bond debt

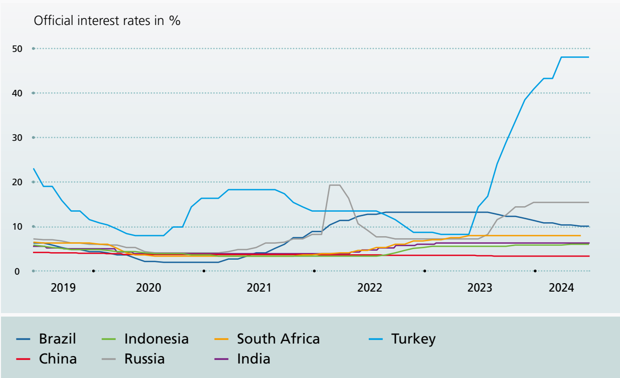
China & co.

Price inflation has stabilised, monetary policy interest rates are flat despite continued easing in LATAM (particularly in Brazil and Chile), and China is on hold... It would seem that the Fed's rate cut is essential to providing fresh monetary impetus in developing regions. Russia continues to be the exception, affected by the war and its consequences for economic activity and price inflation.

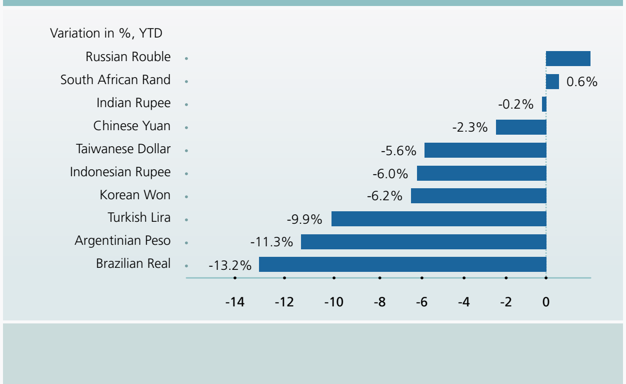
On the currency front, fluctuations since the start of the year have been linked to their respective economic situations. The main countries with external deficits and in need of USD and foreign financing are still experiencing depreciation, which continues at a rapid pace. This is the case for Argentina, Turkey and Brazil. The depreciation of 10% and more against the dollar has resulted in local currency and dollar debts performing very differently, opening the door to certain opportunities, particularly for local currency debt. Public debt levels in most dynamic growth regions, with the exception of China, may be the envy of developed markets, where government debt is a growing concern.

Without going back to emerging market debt as an alternative to Western debt in the event of a return to the sovereign debt crisis experienced in 2011, the comparison of debt levels for bond risk management purposes is understandable.
This context is currently prompting bond investors to limit the emerging market risk premium in USD to its minimums while risk premiums on local currency debt have halted their decline and are recovering moderately. This risk-associated segment is certainly attracting increasing attention.

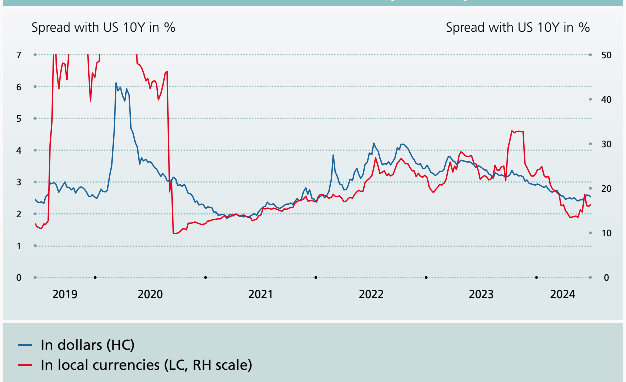
DYNAMIC GROWTH REGIONS: MONETARY POLICY

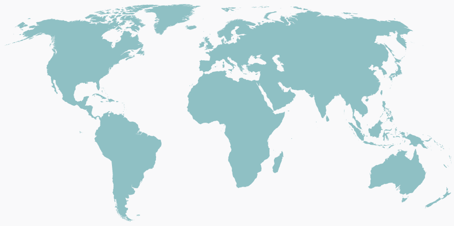


DYNAMIC GROWTH REGIONS: CURRENCY AGAINST THE DOLLAR



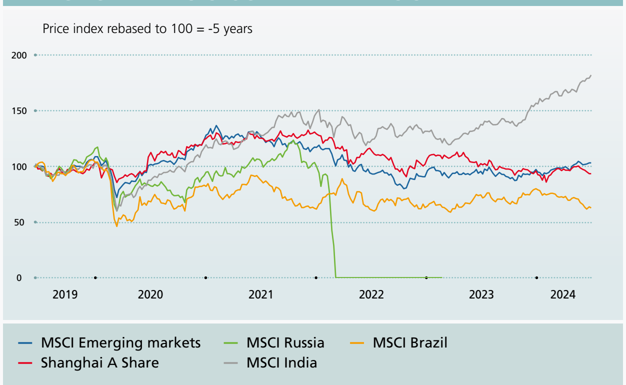
DYNAMIC GROWTH REGIONS: BOND DEBT (LC & HC)



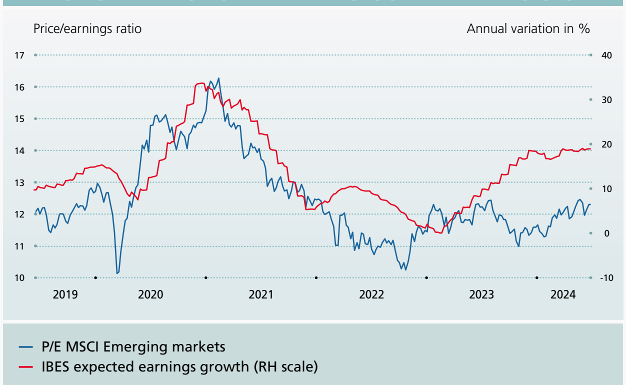


Dynamic growth regions
Stock market

EMERGING MARKETS: STOCK MARKET INDICES



EMERGING MARKETS: FUNDAMENTAL STOCK MARKET FACTORS



Spread out

The MSCI Emerging Market Index ended the second quarter with a positive performance. Emerging Europe was the most dynamic region, followed by China- and Taiwan-led Asia.

Earnings growth for 2025 has been estimated at +15%, driven by technology, materials and healthcare. In terms of sectors, earnings over the twelve months were strongest in utilities, technology and healthcare, which benefited from healthy margin growth. On the other hand, materials, consumer staples and telecoms suffered from lower margins. Sales growth was strongest in energy, consumer cyclicals and healthcare. Other sectors were in decline.

As for the BRICS, profits rose in the second quarter in India and China but fell in Brazil. For 2025, growth estimates for India and China, which remain the two major players in the region, could reach nearly +15%.

2024 should continue to be a volatile year, influenced by geopolitical tensions between China and Western countries. The Chinese real estate market continues to weigh on the economy. There are, however, encouraging signs that consumers are coming back, but the return to growth in China needs to be confirmed.

India should continue to stand out from other regions thanks to its dynamic growth. We remain cautious about Latin America, which is still unable to solidify its fundamentals.

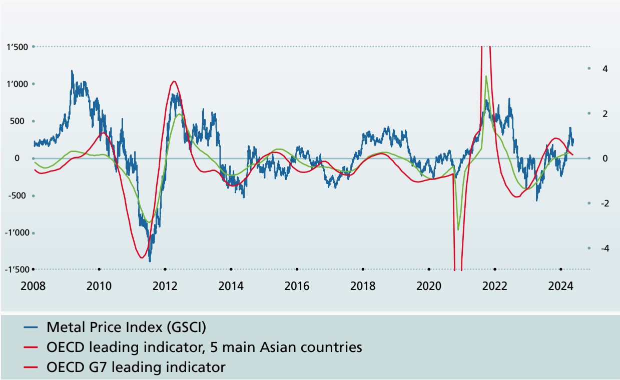
KEY TAKEAWAYS

- Growth in the fast-growing economies is suffering from the difficulties in China, weakened by the property crisis, depressed consumer sentiment and deteriorating relations with Western countries. The outlook for India and ASEAN is more optimistic.
- Geopolitical risk is of particular concern for dynamic growth regions. The volatility it generates should limit exposure to equities and bonds in the riskiest regions.
- The equity diversification these markets offer through exposure to commodities, in particular to metals needed for transitions and technological developments, is worthwhile, as long as it is based on careful stock selection.
- The currencies of the dynamic growth regions are particularly sensitive to geopolitical problems, especially where the respective country has high dollar-denominated external debt, exacerbated by the current crisis.

Commodities

PRICE OF MAIN PRECIOUS METALS

INDUSTRIAL METAL PRICES AND ECONOMIC CYCLE



Oil prices

In the last week of June, Brent crude exceeded 86 USD/bbl, buoyed by the arrival of the summer season in the northern hemisphere and marked by a significant fall in crude inventories. This rise was underpinned by geopolitical tensions and the summer season. As for WTI, it exceeded 80 USD/bbl.

OPEC+ met on 2 June 2024, attracting particular attention as the geopolitical and economic developments of recent months had caused oil prices to fall by more than 8% since mid-April. Against this backdrop of economic fragility and currency uncertainties, OPEC+ decided to extend voluntary production cuts by 2.2mbd until the end of September 2024. Starting this October, these cuts will be progressively reduced until the end of September 2025. This agreement reflects the determination of OPEC+ to maintain support for crude oil prices, while gradually easing production constraints, in response to criticism from certain members such as the United Arab Emirates.

Industrial metals

After hitting a high in May, the prices of industrial metals have eased. The price of **copper** fell throughout June against a backdrop of consolidation of gains following the rally seen between February and May when prices climbed by around 36% to peak at $11,100 per tonne from February's low of $8,100 per tonne. Many analysts explain this price fall as being out of step with the fundamentals of a well supplied market. According to the International Copper Study Group (ICSG), the market will have a surplus of 300,000 tonnes in the first quarter of 2024, despite strong growth in demand (+4.2% annual growth between January and April, mainly observed in China +6.5%). Like for copper, the price of nickel has wiped out much of the rally seen in this year's second quarter. The authorisation of new mining permits in Indonesia is stabilising prices. In the Philippines, the search for American and Western investors to develop the country's nickel industry is in full swing in order to provide a supply chain decoupled from China (largely assured by Indonesian production). Zinc and aluminium, along with their individual production histories, have been subject to the same fluctuations in price.

Precious metals

The price trend in precious metals during the second quarter confirms the acceleration that began at the start of the year, with **gold** up 17% and **silver** up by almost 30%. The main reason for this surge was the diversification by Asian central banks of their dollar-denominated foreign exchange reserves in the face of growing uncertainty about the sustainability of their debts and in the wake of the election results on both sides of the Atlantic. It should be noted, however, that individual and institutional investors have not rushed to buy precious-metals-linked financial products on a massive scale, as ESG considerations may act as a brake on any new enthusiasm. On the other hand, the fall in real interest rates is making the cost of storage more affordable, which is a partial source of demand – a fundamental trend that may continue, supporting precious metals prices.

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Tel + 41 58 211 21 00
Coordination: Grégory Jaquet (gregory.jaquet@bcge.ch)
Graphic design: Level Studio Sàrl
Printer: ATAR Roto Presse SA
Copies: 1,500 copies

Photography, illustrations and graphics:
Greg Dufeil, Refinitiv Datastream, BCGE Asset Management

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