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Financial markets remain very volatile as the outlook stays clouded. While the market seems to be less concerned about the war in Ukraine itself, inflation risks, more hawkish central banks, supply-chain disruptions, as well as a sluggish and Covid-plagued Chinese economy are creating strong headwinds for the global economy, and for global bond and equity markets.

The US Fed hiked rates in March and will continue to do so in the coming months. The ECB has found itself between a rock and a hard place since inflation has risen to 7.5% and, at the same time, the European economy has been particularly hard hit by the effects of the war.

As a result, we have taken a slightly more cautious stance and reduced European equities, corporate bonds and inflation-linked bonds to an underweight position.

Trauth

Thomas Trauth
CEO – IMT Asset Management AG

THE OUTLOOK IS CLOUDED

Financial markets

In March equity markets remained highly volatile. Global equity markets moved inconsistently. The Japanese Nikkei 225, the US S&P500, and the Brazilian Bovespa performed strongly, rising 4.9%, 3.6%, and 6.1%, respectively. In contrast, the Chinese CSI 300 and the MSCI EMU lost 7.8%, and 0.8%, respectively. Dividend stocks in general, as well as energy stocks, US Utilities, and US Industrials performed very well in March.

Rates continued to rise in March, driven by hawkish central banks and rising inflation. Also, US real yields rose sharply, by 27 basis points. Inflation expectations, as measured by 10-year break-even rates, rose sharply in the month. High-yield and emerging markets credit spreads tightened somewhat as credit markets rebounded. Together with heightened uncertainties, fixed-income volatility remained very high.

Energy prices continued to rally in March. The Bloomberg Energy index rose 16.1%. The gold rally slowed with the price of gold rising only 1.5%. REITS rebounded strongly in March. The global REITS index gained 5.1%. Crypto assets recovered part of their January losses. Bitcoin climbed 10% and Ethereum 17%. The market environment was beneficial for global macro hedge funds, which on average gained 2.3% in March.

The USD remained on the strong side as US short-term interest rates rose strongly and widened the yield differential to other currencies. Especially the JPY weakened significantly, as the Bank of Japan kept firmly to its accommodative monetary policy path. Safe-haven and commodity currencies rallied. The USD appreciated 4% against the EUR and the EUR-CHF exchange rate fell to parity temporarily. At the same time commodity currencies, like the AUD and the NOK strengthened. The Chinese CNY stayed on the strong side and strengthened further against the USD.

Macroeconomics

All major manufacturing PMI indices remained clearly above 50, which is the threshold for positive growth. The only exception was the Chinese PMI, which fell to 48.1 after 50.4. Inflation continued to rise, with US inflation further accelerating as commodity prices surged. US inflation reached 8.5% and EMU inflation 7.5%. US non-farm payrolls rose by 431,000 in March, clearly below the 750,000 new jobs registered in February and below expectations. The unemployment rate dropped to 3.6% from 3.8% and average hourly earnings rose 5.6% year-on-year.

In France the second round of presidential elections will be held on Sunday. In the pre-election TV debate Macron seemed to have come out slightly ahead of the far-right candidate Marine Le Pen. Macron especially criticized her for being too close to and allegedly even dependent on Russia. Current opinion polls suggest that Macron will narrowly win the elections.

A win of the populist Le Pen, however, would in all likelihood unnerve markets. In this case, we would expect European equity markets to sell off and sovereign risk to come back to the forefront, which in turn would push French sovereign bond yields higher. Furthermore, it would make a much needed unified European foreign and security policy very difficult to achieve.

Central banks

The US Fed has the difficult task of fighting inflation, which is at a 40-year high, without risking a hard landing for the economy. The US Fed raised interest rates by 25 basis points on March 16. This was the first rate hike since 2018. The market digested this broadly anticipated move without major movements. It is expected that the Fed will add another 50 basis points hike in May and will start to reduce its balance sheet aggressively.

In contrast, the ECB takes a more balanced approach, as the European economy is hit much harder by the economic consequences of the war in Ukraine. European inflation climbed as high as 7.5% in March. We are curious to see what the ECB will decide at its June meeting regarding a reduced asset purchase program, and also whether it will start hiking rates in the second half of this year. As a result of dovish ECB rhetoric the EUR weakened against the USD.

Covid-19

While globally the numbers of new Covid cases are declining, the Chinese authorities maintained their strict lockdown measures in the region centered around Shanghai. Many countries have relaxed or are on the way to relaxing Covid measures, which will allow more people to return to normal lifestyles.

Outlook

Global economic growth continues to be very strong but will weaken because of the high commodity prices and rising interest rates. We do not expect that this will lead to a recession in the next five to six quarters.

Nevertheless, we currently see two particular, big risks for the global economy and the financial markets. One is that Europe could cease to have access to Russian gas, either because Russia stops delivering it or Europe imposes an embargo. The other is that the central banks could too aggressively tighten monetary policy.

In this environment we remain cautiously positive regarding the equity markets, and we assume that bonds will continue to be under selling pressure. We reduced our allocation of European equities a little and are currently slightly underweight in equities. Furthermore, we lowered our exposure to corporate and inflation-linked bonds to reduce interest risks.

Although the US dollar value seems to be very high at present, the interest-rate differential and the comparatively strong US economic growth suggest that the currency will remain strong in the coming months.

ECONOMICS

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Fig. 1: PMIs

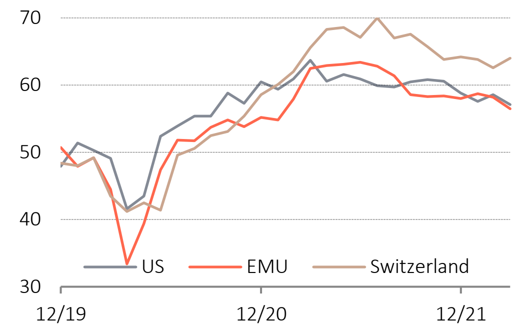


Fig. 2: PMIs

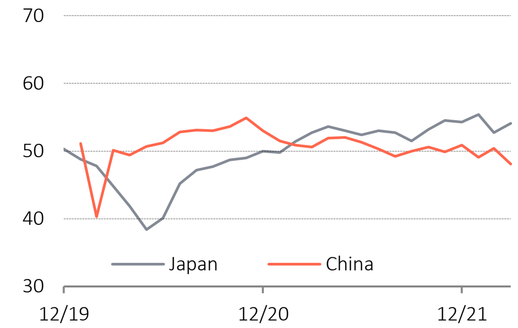


Fig 3: Consumer price inflation, in % YoY

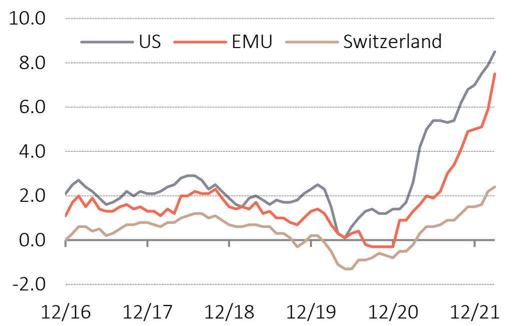


Fig. 4: Consumer price inflation, in % YoY

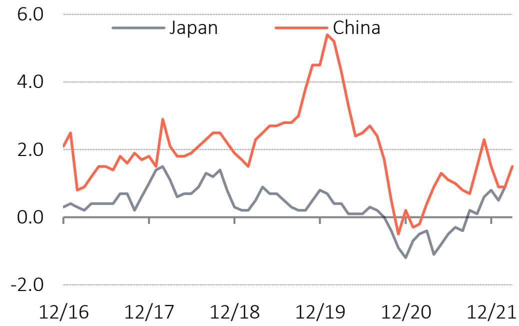


Fig 5: Unemployment rates, in %

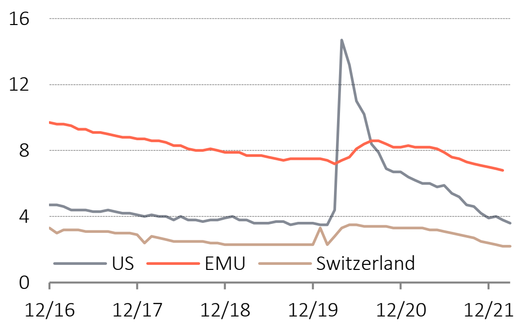
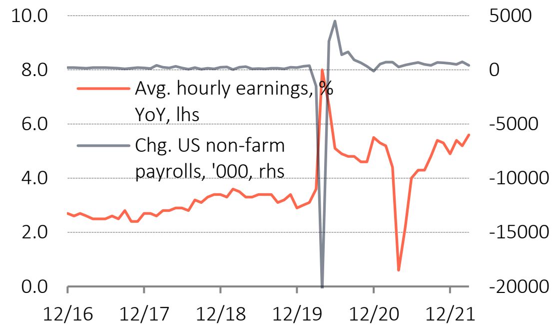


Fig 6: US labor market



FIXED INCOME

In March rates continued to rise, driven by hawkish central banks and rising inflation. Also, US real yields rose sharply, by 27 basis points. Inflation expectations, as measured by 10-year break-even rates, rose sharply in March. High-yield and emerging markets credit spreads tightened somewhat as credit markets rebounded. Together with heightened uncertainties, fixed-income volatility remained very high.

Fig.7: 2Y government bond yields

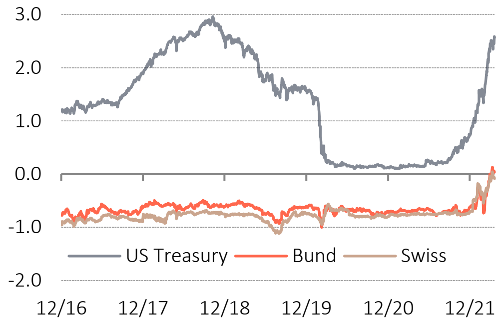


Fig. 8: 10Y government bond yields

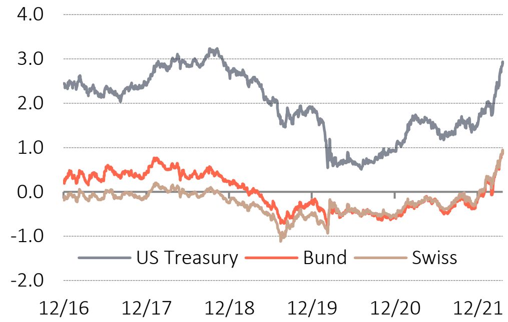


Fig 9: 10Y break-even inflation

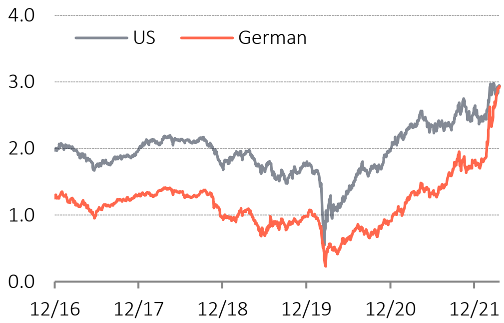


Fig. 10: Credit spreads, 5Y credit default swaps

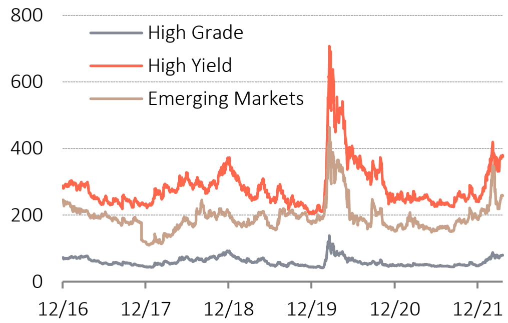


Fig 11: Money market spreads (O/N-2Y)

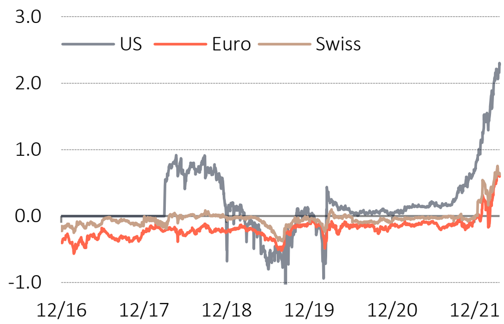
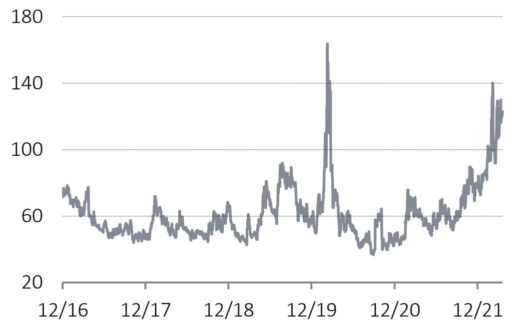


Fig 12: Merrill Lynch volatility index (MOVE)



EQUITIES

In March equity markets remained highly volatile. Global equity markets moved inconsistently. The Japanese Nikkei 225, the US S&P500, and the Brazilian Bovespa performed strongly, rising 4.9%, 3.6%, and 6.1%, respectively. In contrast, the Chinese CSI 300 and the MSCI EMU lost 7.8%, and 0.8%, respectively. Dividend stocks in general, as well as energy stocks, US Utilities, and US Industrials performed very well in March.

Fig. 13: MSCI equity indices – major regions

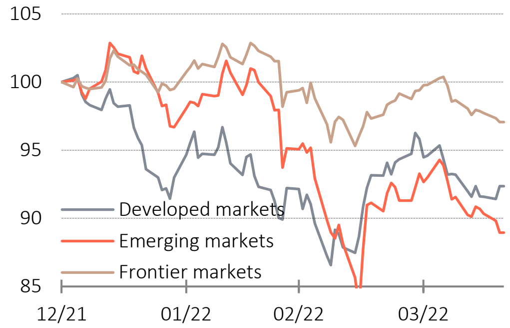


Fig.14: Equity indices – major developed markets

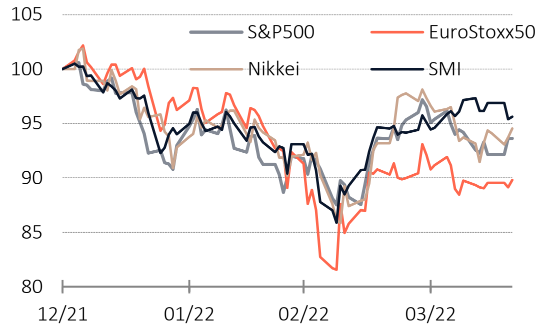


Fig 15: Equity indices – major emerging markets

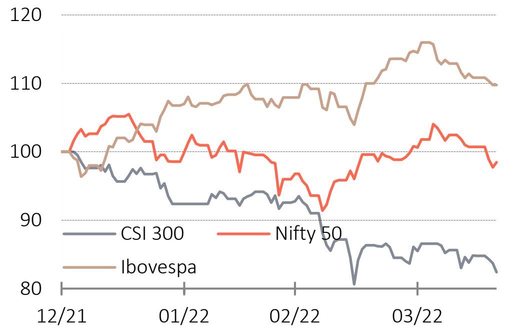


Fig. 16: Sector performance, MSCI Europe, YTD

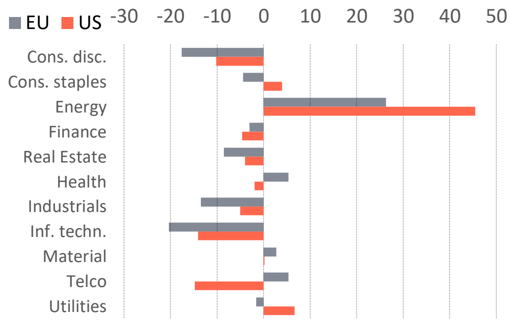


Fig 17: Price-earnings ratios

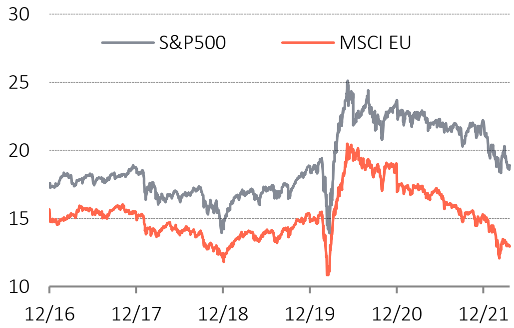
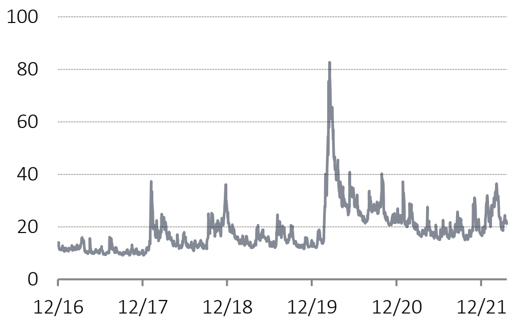


Fig 18: Equity volatility – S&P500 VIX index



ALTERNATIVE INVESTMENTS

Energy prices continued to rally in March. The Bloomberg Energy index rose 16.1%. The gold rally slowed with the price of gold rising only 1.5%. REITS rebounded strongly in March. The global REITS index gained 5.1%. Crypto assets recovered part of their January losses. Bitcoin climbed 10% and Ethereum 17%. The market environment was beneficial for global macro hedge funds, which on average gained 2.3% in March.

Fig. 19: Gold price, USD/oz

Fig.20: Brent oil price, USD/bl

Fig 21: Bloomberg commodity indices

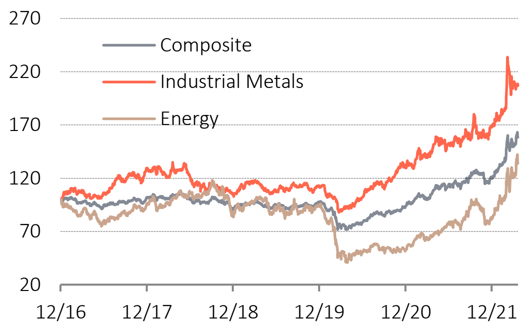


Fig. 22: HFRU hedge fund indices

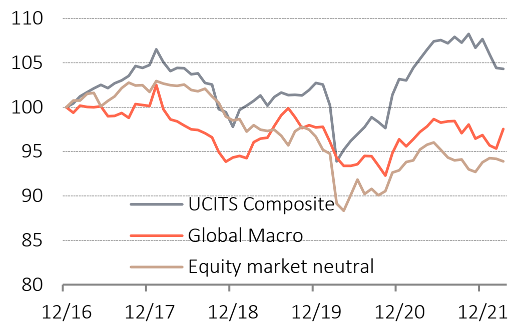
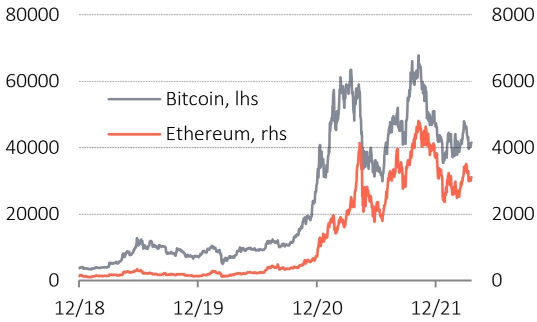


Fig 23: FTSE EPRA/NAREIT global REITS index

Fig 24: Crypto Assets



CURRENCIES

The USD remained on the strong side as US short-term interest rates rose strongly and widened the yield differential to other currencies. Especially the JPY weakened significantly, as the Bank of Japan kept firmly to its accommodative monetary policy path. Safe-haven and commodity currencies rallied. The USD appreciated 4% against the EUR and the EUR-CHF exchange rate fell to parity temporarily. At the same time commodity currencies, like the AUD and the NOK strengthened. The Chinese CNY stayed on the strong side and strengthened further against the USD.

Fig. 25: EUR-USD exchange rate

Fig. 26: GBP-USD exchange rate

Fig 27: USD-JPY exchange rate

Fig. 28: USD-CNY exchange rate

Fig 29: EUR-CHF exchange rate

Fig 30: USD-CHF exchange rate

COVID-19

While globally the numbers of new Covid cases are declining, the Chinese authorities maintained their strict lockdown measures in the region centered around Shanghai. Many countries have relaxed or are on the way to relaxing Covid measures, which will allow more people to return to normal lifestyles.

Fig. 31: Total Covid-19 cases (x 1000)

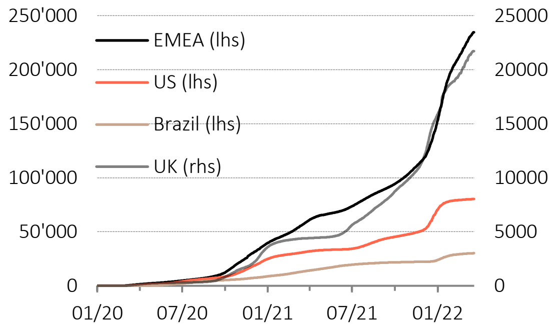


Fig. 32: New cases per day (7-day average)

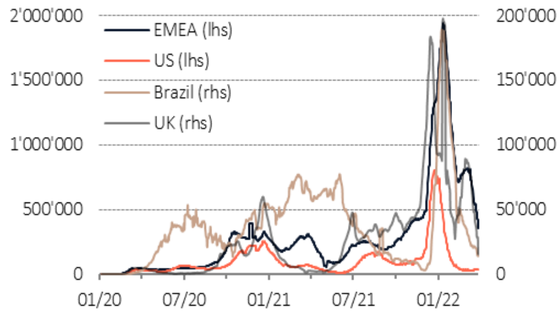


Fig 33: Vaccination rate
(% of the population fully vaccinated)

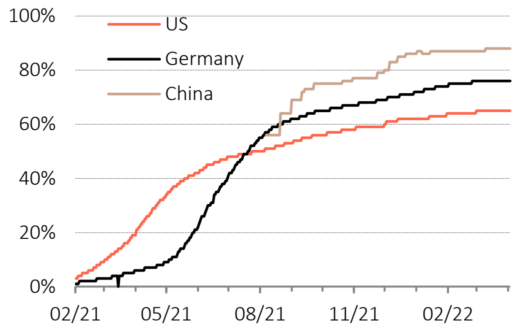


Fig.34: Central bank total assets (indexed)

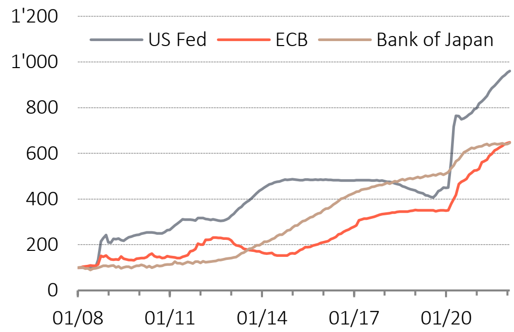
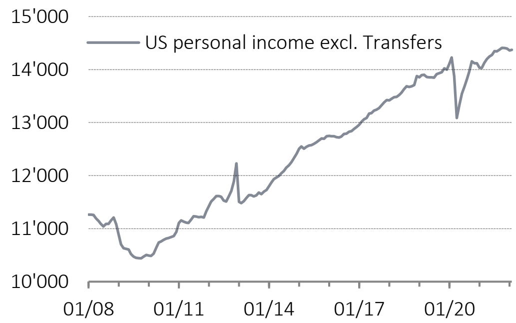


Fig 35: US bankruptcy index

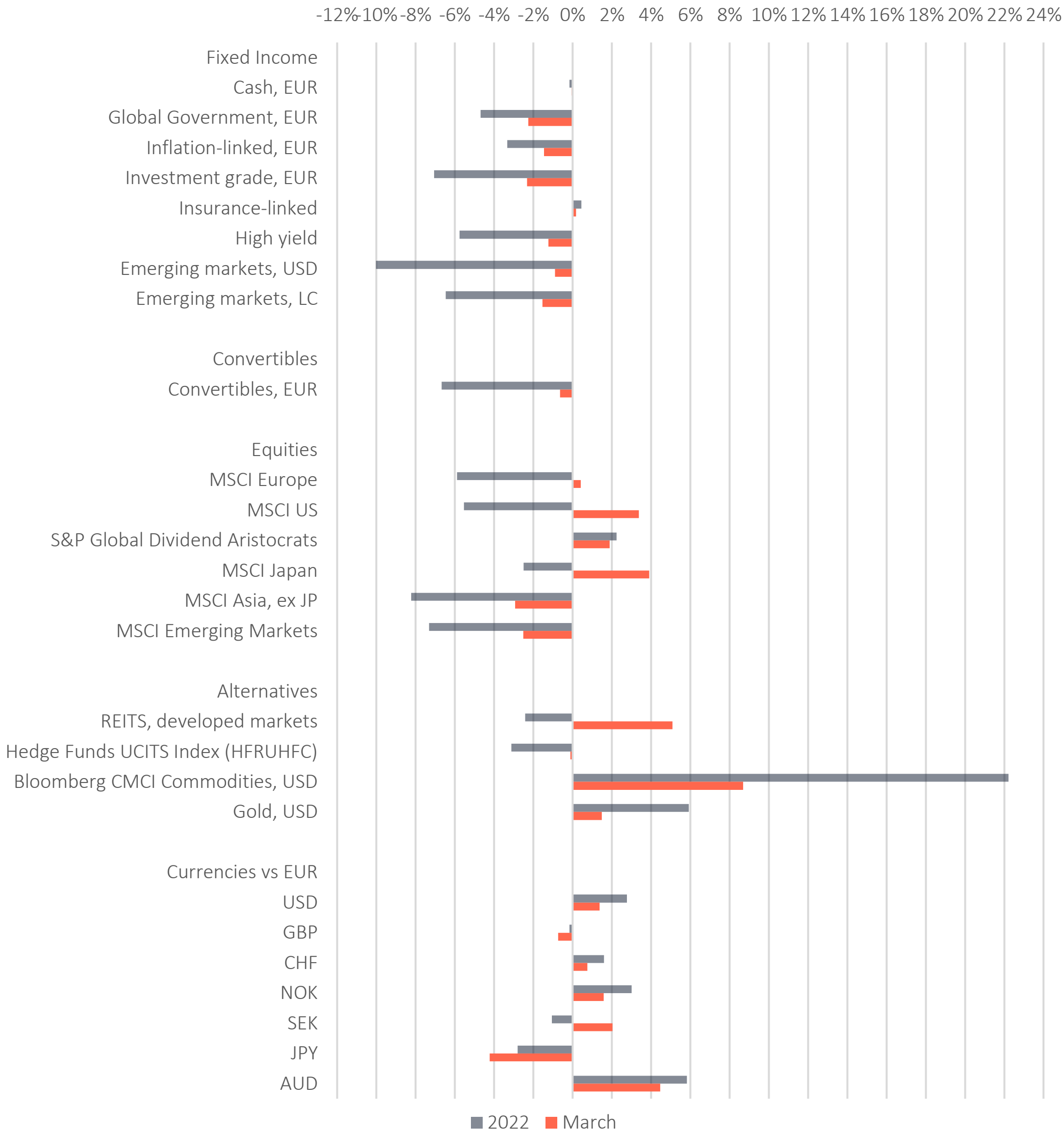
Fig 36: US personal income, excl. transfers
(USD bn, 2012 prices)



ASSET ALLOCATION

March was a difficult market for most asset classes. Almost all fixed income markets sold off in March, with the exception of insurance-linked bonds. Equity market performance was inconsistent. European stocks were about flat, US, Japan, and the Dividend Aristocrats performed well, while especially Chinese and most other Asian stock markets sold off. REITS, Commodities, and Gold continued to rally. The USD and the CHF strengthened.

Fig. 37: Performance of major asset classes, based on our EUR portfolio strategy

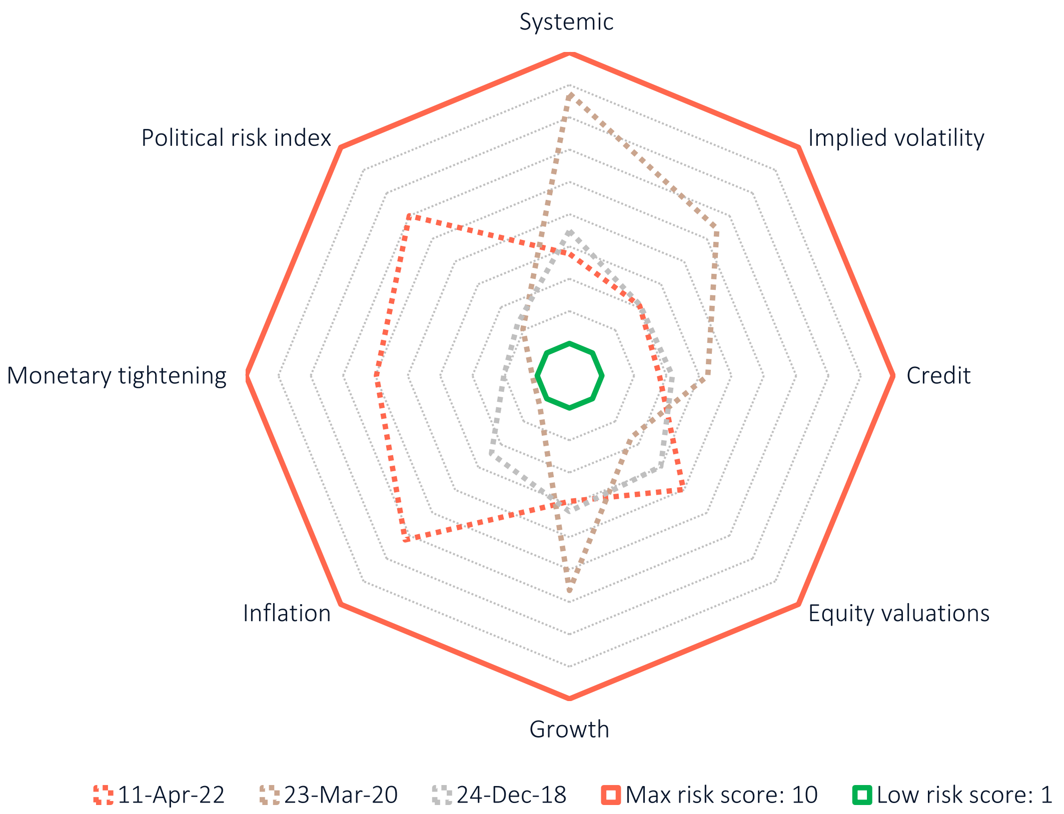


RISK MONITOR

Political, monetary-tightening and inflation risks take center stage. Also, implied volatility (option prices) clearly increased, though less than in other crises. Equity valuations fell slightly. Growth and systemic risks remain muted.

Fig. 38: IMT Risk Monitor

23-Mar-2020: Global pandemic
24-Dec-2018: Growth and monetary tightening fears



DISCLAIMER

Source for all graphs: IMT Asset Management AG, Bloomberg, Real Clear Politics, for Fig 36 Statista (de.statista.com), for Fig. 38, the political risk index: “Measuring Geopolitical Risk” by Dario Caldara and Matteo Iacoviello at https://matteoiacoviello.com/gpr.htm.