CHECK-UP

January 2024
Client information
Reichmuth & Co Private Bankers

Our Scenarios
Page 3

Investment opportunities for 2024
Page 4

Real investments in infrastructure
Page 7

Editorial

As the new year begins, we wish you, our readers, a healthy and happy 2024. We would like to thank you for the trust you have placed in us over the past year.

In 2023, the rise in interest rates caused some turbulence in the banking and real estate sectors – as well as in industry. The risks associated with refinancing are still quite high, as rising interest rates are slowly eroding the less liquid markets. Stock market prices always react first, followed only at a later point by asset values, which have lower valuations based on models and higher discount rates. Now, the cycle of interest rate hikes appears to have come to an end, at least for short-term rates.

In this Check-Up, you will find our assessment of the outlook for 2024 and why we believe the new year will get off to a rather good start for investors.



Remy Reichmuth
General Partner



Under the Red Sky

“Under the Red Sky”, often the harbinger of approaching storm clouds from the west, serves as a metaphor for current global economic trends. It is becoming more and more clear that the Western-dominated world order is under pressure. Traditional economic powers and structures are being challenged to an increasing extent.

Everyone against the West

The BRICS countries (Brazil, Russia, India, China and South Africa) are showing growing determination to free themselves from the Western-dominated world order. This is evident in their joint meetings emphasising closer cooperation, but also in their reaction to the sanctions imposed by the USA. Geopolitical tensions are intensifying and creating a climate of mistrust, even though the growing markets in these countries can still offer opportunities for investment and trade. For the time being, Europe will not be able to assume an independent political role on a world stage. The US elections in 2024 will be closely watched. All the signs are still pointing

to Joe Biden facing Donald Trump once again; so, enthusiasm among voters is accordingly limited. Hopes are high for younger, less divisive figures to enter the race. Whoever is in charge of the Western world is not only decisive for those of us in Europe. Will the world find its way back to peace and prosperity or, will its fragmentation intensify even further with economic and military conflicts?

Europe's location disadvantages: Energy and regulation
Europe is also facing home-made challenges, particularly in the area of energy and excessive regulation. These factors are creating an unfavourable economic environment and in turn affecting investment and growth in the region. Companies must adapt to these unfavourable conditions and increasingly seek more attractive locations for new investments. Multinational companies have an advantage in this regard, as their flexibility allows them to relocate their activities depending on a location's attractiveness.

Skilled labour shortage despite recession
The last 30 years of globalisation have integrated more and more countries into the world economy. In the past there were hardly any labour shortages, but those days are over. Nearshoring is the buzzword of the hour. Coupled with demographic factors, a phenomenon is emerging in the West: despite a weak economy, companies continue to suffer from a shortage of skilled labour. Innovations in automation and digitalisation can only partially offset this trend, but, more critically, upward pressure on wages will continue.

End of deficit spending?
The US is booming, yet the country still has a high deficit of 6%. Europe is flirting with recession, which will also lead to higher deficits. However, today's reality means that these can no longer be financed with "free debt". Rising interest rates are placing an increasing burden on national budgets. In the future, countries will no longer be able to live beyond their means to the same extent as they did in the era of cheap money, which will lead to social unrest and fiercer fights for redistribution. Investors need to keep an eye on how governments react to this new situation. Will fiscal policy become more disciplined and taxes raised, or will they continue to rely on unlimited debt? If it is the latter, who will finance it and at what interest rates?

Central banks seek to reduce excess liquidity
Over the past 15 years, government debt has largely been financed by central banks, with both the US Fed and the ECB now holding enormous quantities of such bonds. Since raising key interest rates to combat inflation, they have had to pay interest on the large money overhang on their balance sheets. They want to reduce this excess liquidity, but can only do so by selling or letting bonds expire. This means that they will no longer buy government bonds, unless there are new crises. The Swiss National Bank also wants to reduce its huge pile of liquidity. But instead of having Swiss government bonds on its balance sheet, it has EUR and USD. How quickly these holdings can be reduced will depend on exchange rates, and as a result, the CHF will continue gaining value for some time.

Interest rate expectations and financing government debt
Short-term interest rates have peaked for the time being. The more important question is what to expect for longer-term interest rates. These depend on supply and demand and can be influenced by the government and central bank only through extraordinary interventions. Based on current geopolitics, it is unlikely that export-oriented countries will want to continue financing Western debt. As mentioned, central banks are also out of the picture. This leaves it to investors, but they are price sensitive and will continually reassess the situation and act accordingly. Given that capital requirements are high, whether it is for the military, new production facilities as part of nearshoring, the conversion of energy infrastructure, or for other government programmes, we expect interest rates on government debt in the West to be higher in future compared with the last 15 years.

Looking ahead to 2024: adjustments and global events
As we can see, the challenges facing the world and the economy are considerable. However, the prospects for 2024 look positive for investors. Interest is being paid again. When it comes to interest-bearing investments: Cash is king! Returns on the money market are higher than on medium and longer-term bonds. The price risks for investors there seem too high, in our opinion. There is also cause for optimism about the stock markets, as expectations have adjusted to both, the new interest rate environment and the very subdued economic growth.

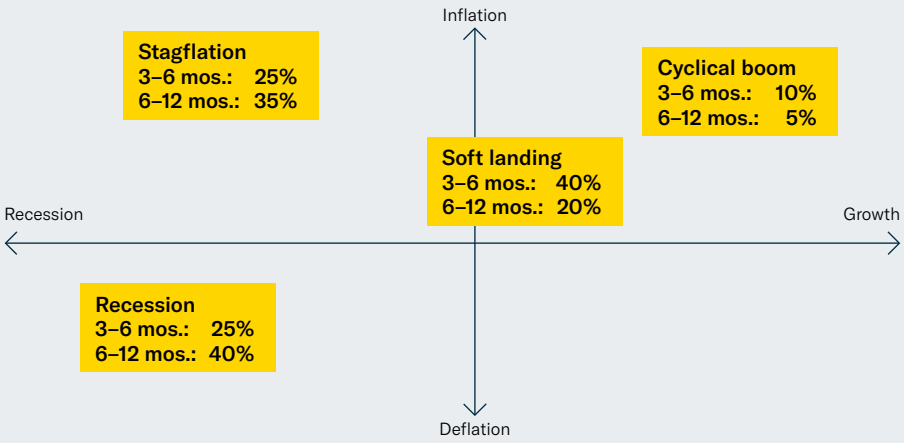
As always, it is wisest to use scenarios to prepare for upcoming events in 2024, such as an escalation or de-escalation of the conflicts in Ukraine and the Middle East, and the outcome of the US elections. An integrated asset overview helps to deal with surprises and is the only way to ensure that you are in a position to make well-founded decisions.



Christof Reichmuth
General Partner

Our Scenarios

Will recession risks end the inflation phase?



Scenarios – estimated probability of occurrence over time

Current assessment

- Core inflation remains above the 2% target of central banks
- Refinancing of outstanding debt remains expensive for companies
- The probability of a "soft landing" decreases over the course of the year

Despite restrictive monetary policy and various geopolitical flashpoints, the global economy is developing relatively well. Many indicators point to a soft landing in the short term. But it is almost impossible to predict the time lag and how much the various hikes of key interest rates will affect the economy. A defensive approach and a flexible response are required if the scenarios end up shifting more significantly. Investors need to remain committed to certain promising growth trends for the time being.

Future scenario: Stagflationary environment

Following the sharp rise in interest rates over the last few quarters, financing conditions remain restrictive. Consequently, credit growth in the private sector is weak. But government fiscal policy continues to be expansive, with budget deficits remaining on an elevated level. The labour market has dried up in many places, and core inflation remains stubbornly above the 2% target. In nominal terms, growth continues to look good, but consumers are growing more dissatisfied because increasing numbers of them are suffering from higher costs. Real value investments such as equities are preferable to nominal value investments.

Best investment ideas:

- Attractive domestic market thanks to price stability
- Equities from defensive sectors
- Focus on quality stocks and dividend payers
- Active credit strategies (after price corrections)
- Gold

Current: Soft landing

Victory will be declared in the fight against inflation, giving the Fed the opportunity to quickly cut key interest rates again. A renewed expansionary monetary policy will stimulate corporate investments and shore up stock market valuations. With interest rates having reached their cyclical peak, high levels of investment in artificial intelligence will lead to a surge in economic growth and productivity, from which an increasing number of companies will start to benefit. Both, real value and nominal value investments offer good yield potential.

Best investment ideas:

- Growth stocks, especially relating to artificial intelligence or biotech
- Cyclical small caps
- Emerging market equities
- Medium-term corporate bonds

Cajetan Bilgischer und Silvan Betschart

Investment opportunities for 2024

Less growth, but more investment alternatives

The growth prospects for the global economy in 2024 are weak. The boom in the USA, which until a few months ago appeared broadly resistant to higher interest rates, is weakening. Furthermore, hardly any political impetus for the economy can be expected in the run-up to the elections due to be held in the US in 2024.Europe has been in a state of stagnation for some time now. China may well be stimulating the economy in certain areas, yet this is not enough to fuel growth in the global economy.

The situation remains problematic for Western central banks. Key interest rates are in restrictive territory, and growth as well as inflation figures are falling. However, because core inflation rates are still above target and labour markets remain tight, interest rate cuts could hardly be justified in the coming months without subsequently stoking inflation once again.

Soft landing?

The latest market forecasts expect inflation to continue to fall while the Federal Reserve being able to lower its key interest rate (a key rate reduction of 1.5% is currently expected for 2024) in order to prevent the economy from slowing down too much. This is based on expected earnings growth of 10% for the US equity market. Even though many leading indicators would support this scenario, from a historical perspective, soft landings are rare. That means there are two risk scenarios for 2024 that should not be completely ignored:

1. If growth weakens more than expected in 2024, interest rates are likely to be cut faster and more sharply than today's market is anticipating. However, this would make earnings estimates high and require downward revisions, which would likely put pressure on the stock markets.

2. The high level of new debt in Western countries is a particularly volatile factor in the current environment. If Trump ends up winning the US presidential elections, budget deficits threaten to increase further and more government bonds will have to be issued to finance them. Whether this growing supply of government bonds can be absorbed by the market depends on the invest-

Investment ideas for 2024 by region and asset class






	Switzerland	Europe	USA	Asia
Attractive asset categories	– Short-dated bonds – Equities	– Equities – Infrastructure	– Money market – Active credit – Selected stocks	– Equities
Investment themes	– Cyclically resistant dividend stocks – Small caps with catch-up potential	– Defensive sectors (consumption, healthcare) – Industrials with focus on clean energy	– Artificial Intelligence – Catch-up potential for interest-sensitive biotech and clean energy	– Vietnam – Japan
Select implementation ideas	Roche, Nestlé, Zurich, Holcim, Tecan, Bossard	Sanofi, Schneider Electric, Siemens, L'Oréal, Anheuser, Unilever	Microsoft, Alphabet, Honeywell, Linde, active funds in the area of biotech and clean energy	Active funds or ETFs
Currencies	–	EUR negative	USD negative	JPY positive

ment alternatives. If demand lags behind supply, 10-year interest rates could rise further and increase valuation pressure on the markets. In the past, major distortions often appeared on financial markets following sharp rises in long-term interest rates.

Balancing opportunities and risks
Despite the heightened economic uncertainties, overall we do not expect a sharp drop in corporate earnings. Nevertheless, the balance sheet quality of investments must be considered in 2024. Even if key interest rates fall, there will be an increasing number of indebted companies unable to refinance their upcoming maturities at higher rates. Although this can lead to fluctuations and rotations in individual sectors, it is not a bad starting position for the financial markets in general and, in our view, justifies a neutral equity allocation, provided of course that inflation continues to fall. The rise in key interest rates has also made fixed-income investments more attractive – at least at the short end.

Defensive positioning
For equity portfolios in 2024, we favour a higher weighting in defensive sectors such as healthcare and consumer staples. Many companies in these sectors are reliable dividend payers thanks to stable cash flows. In the past year, these sectors also trailed well behind the market as a whole and, in our view, have the potential to catch up. The Swiss equity market is our preferred market, with a large selection of defensive quality stocks.

Sought-after technology leaders
Certain strong market trends have emerged over the past year – above all in the area of artificial intelligence. These few growth categories will remain in demand, particularly in an environment of under-average growth. In the field of AI, it is difficult to see how the dominant US tech companies could rapidly lose their supremacy without regulatory intervention. The positive momentum, high profitability and good growth prospects continue to favour keeping major technology leaders in the portfolio. However, some other growth segments that have been severely impacted by the rise in interest rates in recent months will also once again offer opportunities in 2024 (see article on page 6).

Attractive emerging markets
From a regional perspective, the comparatively low valuations in some Asian countries, such as China and Vietnam, stand out. China is polarised in geopolitics and thus shunned by many foreign investors. A recovery in China would, however, benefit many European and Japanese companies. Vietnam, on the other hand, is profiting from the relocation of supply chains from China and will provide jobs for a rapidly growing middle class for years to come. High growth, a low valuation and solid prospects for inclusion in the emerging markets index offer good opportunities for returns.

Opportunities in the credit market
Owing to past interest rate hikes, a high proportion of outstanding bonds and loans are trading below par, regardless of quality. Bonds that can be successfully refinanced in the future offer an attractive total yield (price gains & interest). Alternatively, rising default rates also offer entry opportunities for restructuring specialists, with a transfer of value from the shareholder to the creditor.

“The Swiss equity market is our preferred market, with a large selection of defensive quality stocks.”

Alternatives for portfolio diversification
A 10-year Swiss government bond currently yields around 0.6%. This is less than inflation and no longer offers significant price and diversification potential if interest rates fall. In addition, short-term interest rates are considerably more profitable. Interest rates are admittedly higher for foreign government bonds, but in a crisis situation the Swiss franc tends to strengthen, risking currency losses. What is still suitable for portfolio diversification right now?

- **Temporary cash reserve** – offers at least some interest in the home currency. Furthermore, it is available at any time and can be used to respond to new market opportunities.

- **Gold** – inflation expectations have remained firmly rooted. However, risks could ensue if the central banks switch to an expansionary course too early or the geopolitical flashpoints escalate further. Due to the increased risks, there is a good chance that gold will perform well in 2024.



Patrick Erne
Head of Research

New interest rate environment

It is worth taking a differentiated view – what needs to be considered?

Over the last two years, both short-term and long-term interest rates have risen considerably. Long-term interest rates in particular are essential for the valuation of financial assets, as prices are determined by discounting future cash flows by long-term interest rates and adding a risk premium.

A look at the valuations of various asset classes over the last two years shows that the new interest rate environment has not yet made itself felt everywhere. Certain interest rate-sensitive segments have already corrected sharply due to higher interest rates and now offer attractive entry or purchase opportunities for long-term investors:

Opportunities in structural growth areas

Shares in the **"alternative energies"** segment recorded substantial price gains from 2019 to 2021 as a result of political efforts to restructure the energy sector. However, with the sharp rise in interest rates and uncertainties regarding the exact structure of tax credits relating to the "Inflation Reduction Act" in the USA, these shares have lost more than half their value over the past two years. Many projects must be reassessed, adjusted or even cancelled due to current capital costs, leading to write-offs on older projects. With industrial rationalisation and the high competitiveness of wind and solar energy, we anticipate opportunities along the value chain – from scarce raw materials and industrial companies to utilities. Undoubtedly, it seems clear that the expansion of renewable energies will keep progressing rapidly, regardless of interest rates.

We have identified further opportunities for attractive portfolio additions in the **biotechnology sector.** Following the interest rate hikes, by mid-2022 this segment had lost considerable value from its highest level. We remain constructive for this segment. Pressure on large pharmaceutical companies with weak product pipelines and solid balance sheets (such as Roche) remains high in order to secure access to promising active ingredients by acquiring biotech companies. The primary focus here should be on companies that are actively engaged in later research phases (phase III). Conversely, very young companies still in the early stages are focused on streamlining, as it remains difficult to raise capital.

The price adjustment mechanism for private market investments in particular is somewhat slower, and further price adjustments are possible. It is still worthwhile taking a nuanced and multifaceted approach:

Headwinds expected for private market investments

In contrast to equity investments, which are listed on a stock exchange and whose price is determined daily by supply and demand, the valuations of private market investments are based on either:

- theoretical models with many different assumptions
- the most recent valuation round during which money was raised, or
- the valuation of comparison categories

We are currently seeing private market funds holding off on new external financing rounds and instead raising money from existing investors to defer valuation adjustments, or borrowing at fund level to postpone realisations and still be able to pay out distributions. In addition, the current valuations make portfolio realisations difficult. We expect the price adjustment process for private market investments to likely persist for a few more quarters.

In summary, it is important to take advantage of selective opportunities from undervalued themes in the equity market. In the area of private market investments, we recommend choosing your partners carefully, exercising caution when borrowing, and staggering investments over the cycle, i.e. exploiting any temporary valuation corrections for entry/increase of exposure. In the infrastructure sector in particular, we foresee tremendous opportunities in the future based on the immense need for investment for the energy transition in Europe and new mobility solutions. Please feel free to contact us if you would like to discuss any of these topics.



Silvan Betschart
Research, Head of Investment Policy

Real investments in infrastructure

Mobility sector with attractive yield prospects

We have been making direct infrastructure investments in Switzerland and Europe for over 10 years. In 2012, we laid the foundations for our current infrastructure solutions with real asset investments in railway freight wagons.

The investment in the transport sector made at that time has been gradually expanded and now comprises a fleet of almost 5000 freight wagons, which are leased, mostly on a long-term basis, to around 100 different industrial companies from 15 European countries. In total, we currently manage over CHF 2 billion in direct equity investments in three infrastructure sectors: transport, renewable energy and waste disposal.



Significant infrastructure sector

Modern and efficient transport infrastructure is not only of central importance for the local population, but also represents one of the most vital pillars of successful and future-oriented economies. In Europe, the transport sector employs more than 10 million people and contributes around 5% to the European Union's GDP. The downside, of course, is not only noise, accidents and traffic jams, but also large quantities of greenhouse gas and pollutant emissions, making the transport sector currently responsible for around 25% of total greenhouse gas emissions in the European Union. With its "New Green Deal", Europe has set itself the goal of becoming climate neutral by 2050. This will also require a restructuring of the transport sector in order to reduce transport-related greenhouse gas emissions by around 90% by 2050.

Capital demand offers opportunities

This transformation of the mobility sector requires major investments that state funding alone will be unable to finance. Considerable funds are needed for the maintenance and expansion of the rail network, as well as for refurbishment investments in locomotive and freight wagon fleets. Road transport also requires e-mobility expansion for both private and public transport, while shipping and air transport as well must increase the sustainability of their operations by using renewable fuels. The demand for capital is considerable and offers attractive investment opportunities – including for private investors.

Attractive portfolio component

This is even more true given that infrastructure investments possess various advantageous characteristics for investors and are a solid component in the structure of your portfolio. In concrete terms, these characteristics include:

- Ownership of long-term, recoverable real asset investments with partial inflation protection due to index-linked contracts
- Stable and attractive expected returns and regular distributions thanks to constant usage demand
- Low correlation with other asset classes across different market cycles
- Substantial contribution to sustainability goals, which are being pursued in particular by more and more institutional investors, such as pension funds

We launched our fourth infrastructure fund in October 2023, focusing on the mobility sector and investing in rail, road, waterway and aviation sub-sectors in Switzerland, Europe and the UK.

Interested? We would be happy to talk to you personally – feel free to give us a call.



Marco Mengotti
Client Relations Manager Infrastructure

Fit for the future



Interview with Jürg Staub, General Partner

Mr Staub, as the year begins, you are handing over the "Corporate Clients" division to Sandro Kutschera, who is joining you as the former Head of Credit Suisse Central Switzerland. Does this mean you are retiring?
No, not at all, on the contrary! (laughs) Besides Sandro, we will also have Ivan Blättler, Bruno Della Chiesa, Tamara Egger and Christian Unternährer joining us from that team in February. Facilitating their smooth integration into our existing operations while maintaining client focus is essential for a successful start. I'm delighted that, as an "old hand", I can contribute something towards this. The continued expansion in Germany will also be a challenging task for me.

What are your plans for Germany?
We founded Reichmuth & Co Integrale Vermögensverwaltung AG in Munich in the year 2000, and the sole director since then had been Christoph Schwarz, the company's co-founder and someone who has always exercised very judicious leadership. In light of his age, he has now handed over the operational management to Torsten Steinbrinker, who joined us from Flossbach von Storch in July 2023 and will be working with us to further develop and expand our business in Germany. The next phase we're undertaking is to reinforce the existing team and open a second location in Düsseldorf in January. Christoph Schwarz has now moved to the supervisory board of our German sister company and will remain available as a consultant to clients.

What is the key to successful growth?
Three criteria are central to success. Number one, excellent employees; number two, a strong customer focus; and number three, a flexible range of services and investments offering special features. All three points need to be covered. Welcoming new and younger employees, such as those who are now bolstering our teams in Switzerland and Germany, is akin to cell regeneration. They will certainly bring along their own unique and new ideas, and it's our job to weigh up which innovations will benefit our clients and where we should continue to rely on what's already been proven to work.

How do you go about that?
Ultimately, it's always the clients themselves who decide whether or not there is a tangible benefit for them. This makes it all the more important, in my opinion, that we never recommend anything to our clients that we wouldn't implement for ourselves. In the case of investments, this means that a member of our group of companies or at least one of the three partners with unlimited liability is always personally involved in the investment.

What does your personal investment mix look like right now – similar to that of your fellow shareholders?
Wealth is and will always be something very personal – and it has to be harmonised to fit with me, my family and my goals. We three shareholders definitely hold the same conviction that core investments are primarily income-generating real assets. Nevertheless, our investment allocation differs greatly because our starting positions, goals, families, succession plans, investment preferences and other factors are very different.

What are your longer-term goals?
As a businessperson, it's my intention that when I retire in a few years' time, I will be able to say that Reichmuth & Co is in an even better position than it is today. This is achieved when our clients and their money are in harmony with each other, and they are satisfied with our services. And this in turn requires us to safeguard and grow their assets according to their individual starting positions and goals. I'm more than happy to accept this challenge because I feel "fit" for the future both as a businessperson and investor. Together with our team, I look forward to continuing to provide our clients with the best possible advice and support.

myclimate neutral Drucksache
myclimate.org/01-23-121213

This document is for information and marketing purposes and is therefore deemed to be advertising pursuant to Art. 68 FinSA and Art. 95 FinSO.

Check-Up_EN_0124