EDMOND DE ROTHSCHILD

LETTER FROM THE CIO AM

MARKET ANALYSIS AND PRINCIPAL INVESTMENT THEMES

NOVEMBER 2022

BONDS RATHER THAN SHARES

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► As the end of 2022 approaches, various encouraging elements have disrupted the prevailing gloomy outlook: China has started easing its zero-Covid policy, the global economy may be decelerating but is less depressed than expected, gas prices everywhere have fallen sharply and inventories look high enough to get us through winter. Above all, there are incipient indications that US inflation is turning lower.

We could also point out that the idea of peace talks has been mooted in the Kremlin following the Russian army's retreat from Kherson. Press reports even suggest the West and Ukraine itself might be on the same wavelength albeit more discreetly. We should avoid rushing to conclusions but there is an air of change about. Equity and bond markets have reacted by rallying sharply since October.

SLOWING US INFLATION IS REASSURING

There is no doubt that the decisive issue is whether US inflation turns lower. The surge in inflation started in the US and has had the biggest impact on markets this year. It goes without saying that a small drop does not constitute a trend but it is reassuring that the slowdown in inflation has been seen in goods and services generally and not just in isolated components. As commodity and freight prices have been returning to normal and production lines are back in action, it is only logical to see a slowdown in goods inflation. And with falling property prices and the sharp drop in new rents, we can also expect the rent index to slow over the second half of this year. Despite all this, inflation will struggle to move below 4% if wages continue to rise by around 5%. The labour market is still very tight. The Fed will be forced to keep a very close eye on employment data but it would be a whole new game if inflation were to fall back to more reasonable levels. That is not yet a done deal but it would mark the end of persistent upward revisions in the Fed Funds rate, reduce bond market volatility from extreme levels and therefore volatility on all markets.

KEY FIGURE

> 2.75%

expectations for ECB rates.

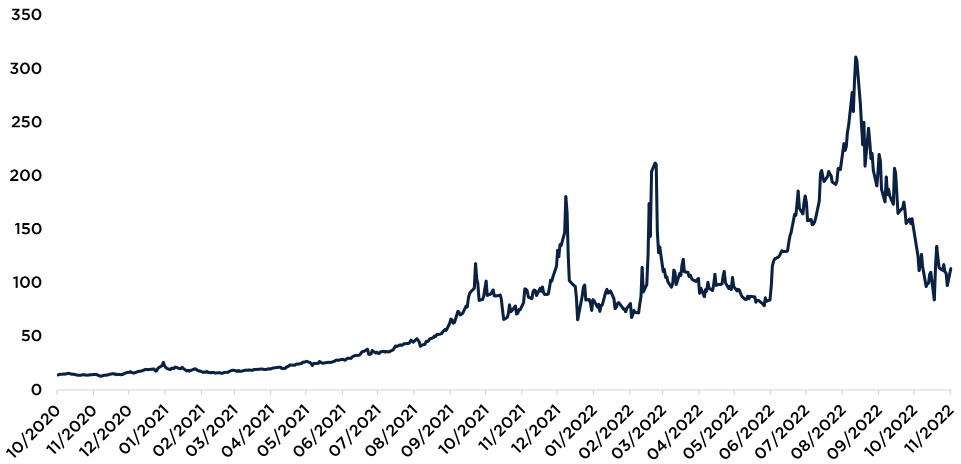
RECESSION IS STILL A POSSIBILITY

At the end of September, we were still cautious on equities, saving ammunition for more tactical moves. We have since gradually raised equity exposure towards neutral. Faced with today's situation, we are sticking to this stance for a little longer while staying tactical.

Equity markets have already enjoyed a strong rally but a recession is still possible. The global economy is still slowing and company margins continue to contract. This leaves us with poor visibility on equity markets but they could still continue to rise up to the end of year, especially if we have more signs of disinflation.

If US inflation has already peaked, the dollar should stabilise as the interest rate differential between the US and elsewhere would logically narrow. We now think it is time to raise exposure to emerging country debt, a segment that would benefit if the Fed pivots, the dollar stabilises and China's zero-Covid policy eases. We are also raising portfolio duration with US Treasuries and investment grade corporate debt while staying somewhat cautious on European duration. Markets are already expecting the ECB to raise rates a little above 2.75%, but high inflation in Europe and poor visibility on the ECB's policy suggest we should tread more carefully.

EUROPEAN GAS PRICES HAVE FALLEN BACK SHARPLY



Source: Bloomberg, Edmond de Rothschild Asset Management. Data as of 14/11/2022.
Past performance is not indicative of future performance. They are not constant over time.

	Our convictions*	Changes compared to the previous month
ASSET CLASSES		
Equities	= ☆	↑
Fixed Income	+	↑
Cash	-	↓
EQUITIES		
US	=	→
Europe (ex-UK)	-	↓
UK	=	→
Japan	=	↑
China	+	→
Global Emerging	+	↑
Convertibles	=	→
SOVEREIGN BONDS		
US	+	↑
Euro Zone	-	→
Emerging Markets	+	↑
CORPORATE BONDS		
US Investment Grade	+	↑
Euro Investment Grade	=	↑
US High Yield	=	↑
Euro High Yield	=	↑

☆ Tactical score

*Range of investment committee ratings on the asset class/geographical zone (from -/- to +/+). Source: Edmond de Rothschild Asset Management (France). Ratings at 14/11/2022.

KEY POINTS

We are raising exposure to emerging country debt

We are increasing portfolio duration with US Treasuries and investment grade corporate debt

We remain somewhat cautious on European duration

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