SUNLINE
WEALTH MANAGEMENT

April 2023

March: A convoluted and volatile month

Over the month the world witnessed three US bank failures, led by the collapse of Silicon Valley Bank in less than 48 hours, a quasi-collapse of Credit Suisse - likely originated on rumors on social media, that forced it into a merger with UBS, only to be followed by similar worries over Deutsche bank - emergency action by policy makers and central banks to stabilize the financial sector, more central bank rate hikes and a US presidential indictment. It is thus quite remarkable, for many observers, that equities finished the month in the green.

Large technology companies have been a powerful stabilization force, as their essentially debt-free balance sheets lent them haven-status, along with more classic defensive sectors such as healthcare and utilities. And, contrary to 2022, global fixed income, despite wild swings in interest rates, proved to be once again an asset class that acts as a true multi-asset diversifier and ballast provider to portfolios: the global aggregate index ended the month up over 3%.

Financial markets

As events unfolded, the market, in a matter of a week, went from pricing one extreme to another:

- The markets went from implying two US Fed rate hikes to 5.5%, to two rate cuts to 4.5% by June of this year. The one-year rate went from being priced at 5.4%, to as low as 3.55%: it has since stabilized at around 4%.

- The equity market quickly started to price a recession, with financials and the energy sector the worst performers. Cyclicals and industrials also sold off, as investors switched into defensives and technology mega caps. Just to give an example, over the period, Caterpillar lost 18%, while Meta, the parent company of Facebook, rose 17%. Similarly, in Europe, ArcelorMittal lost 17% in less than two weeks. Such examples abound.

- Gold rose from USD 1,800 to over USD 2,000 an ounce.

- Cryptos continued to rise, and, eventually, Bitcoin hit 30,000 again.

As mentioned in our last strategy update, authorities moved swiftly to contain the banking crisis, which was one of the factors in keeping our exposure unchanged. Over the last ten days, the markets have begun repricing some of the above moves, with US stocks rotating out of technology mega caps, and back into cyclicals. In Europe, due to the dearth of technology stocks, the moves have been mostly out of defensives, such as Nestle or Danone, and healthcare stocks, and back into cyclicals and industrials.

We continue to prefer European equities over US ones.

Year to date, the US market has been pulled upwards exclusively by a rebound in the 6 largest technology stocks. The move brought their valuations, in terms of PE ratio for example, to either historical highs, (Amazon and Nvidia), or above their 5-year average, (Microsoft, Meta, Apple and Alphabet). This just before an earnings season that could be pretty brutal: for the group's earnings are expected to drop 15% in Q1, the biggest drop since 2009. Just 6 months ago earnings for this group were expected to gain 1%. For the S&P as a whole, earnings are expected to drop 7% year on year, the largest decline since Q3 2020. Margins should continue to contract and will likely not be compensated by sales growth. This deteriorating view reflects weaker economic growth, particularly in the US, a saturated market for technology gadgets, PCs, smartphones and electronic components, (as recently confirmed by Samsung).

On top of all this, global advertising is unlikely to have really grown, and we doubt there is a reacceleration in global subscriber services. As these companies represent 20% of the S&P 500, they will inevitably act as a break to any upside in the S&P 500, while lower bond yields will likely act as a support.

To the contrary, in Europe, we should start to see the positive effects of China's, and hence Asia's, reopening.

In Europe also, the index is very different: 20% of the STOXX600 is made up of companies such as Roche, ASML, LVMH, Shell or Nestle, which, contrary to the group dominating the US index, as a group, offer:

- Double-digit earnings growth
- Strong balance sheets
- Sustainable dividends
- Are defensive
- Stable and high margins

As a group, it is estimated these companies will grow revenues by 6% and EPS by 12%. The group is likely to lead European indices higher, while cyclicals should start to feel the positive effects of China's reopening. Also, as we highlighted in the past, on several metrics, Europe cannot be described as expensive, the opposite is true for the US. This should continue to help Europe's outperformance.

We also believe that, as the banking crisis subsides, markets will be driven again by fundamentals: the economy.

Global Economics

As highlighted in our last document, the banking crisis is a tightening event: lending will become more expensive and less available, while, at the same time, banks will have to adjust deposit rates: this is particularly true in the US, as banks suffer immense competition for deposits from money market funds. As such, the effect should be more pronounced in the US than in Europe. How much conditions will tighten as a result, on both sides of the Atlantic, is one of the main topics of discussion in estimating how much economies have been slowed down by this.

In the US, senior loan officers' surveys will be particularly followed: while we have a 2 months' delay, conditions were already tightening in January. Couple that with already high rates at close to 5%, and especially with money supply (M2) being drained from the system at the fastest pace we could see in our charts, then US financial conditions are likely to be much tighter than what traditional indicators might suggest. In Europe, the banking system is different:

- It is not balkanized, unlike the US, (mostly the result of the Glass-Steagall act of 1933).
- The oversight has not been lessened post the GFC, (for the US, see our last monthly paper).
- There is no evidence of money leaving the balance sheet of the banks.
- There is also no evidence of money switching countries, or looking for refuge at the ECB, as this would show up in the bank's Target 2 system.

Also considering that:

- US inflation, whilst sticky, is coming under control: services' inflation, (including rents), is slowly becoming disinflationary.
- Recent US data points to weakness, not only in the manufacturing sector but also in services.
- The US job market appears to be cooling faster than expected, despite an unemployment headline rate of 3.5%: temporary workers are falling, firings are increasing, the number of people filing for unemployment is increasing, job openings are falling, and a recent survey of small businesses, (which are responsible for 2/3rds of US job creation), shows a reluctance to hire new workers in future plans not observed since 2017. Also, as highlighted in the past, we believe consumers are not in very good financial health anymore.
- In Europe, while services continue to be solid, recent data points to growth in manufacturing, with positive figures for both new factory orders and industrial production in Spain, France, and Germany - maybe the first side-effects of China's reopening.

- In Europe, the issue with inflation is that core is rising faster than the headline figures, (dragged down sharply by energy, as the base effect from Ukraine fades away), whilst food inflation stays stubbornly high, at around 15%. Food inflation cannot be addressed by interest rates: governments instead are looking at subsidies and or radical cuts in the VAT of essential food items, such as bread, pasta, or oil.

- Post Zero Covid policy, the government only recently withdrew mask restrictions on public transport and in offices. At first, the Chinese seemed to be hesitant to consume, and that was shown in sluggish data: recent high frequency data point to a surge in the services sector as consumers spend, amongst other things, on travel and restaurants. The government is also now trying all methods to revive its beleaguered property sector and is trying to reactivate its private sector, such as its embattled technology one.

Summing up the above we believe that:

- The US Federal Reserve is likely to increase its benchmark rate by another 25 basis points, and then stay put for several months: we thus believe, as written in the past, that the market is overly optimistic that the central bank will lower rates by almost 1.5% over 12 months, starting in July this year.

- We believe that the US is likely to enter, (or has already entered), a shallow recession in Summer. Obviously, should the recession be deeper, then the central bank is likely to react by deeply cutting its rates again. It is not, however, our central scenario.
- The ECB is likely to increase rates to a terminal rate of around 3.75%, (this is the market consensus also).

- The European economy should reaccelerate, albeit not dramatically, to achieve 1% growth for 2023, helped by Asia reopening and Asian tourism. Also, the full effect of the fiscal spending from the European recovery Fund is being felt now.

The above implies that equities will respond more favorably to the brightening outlook, enabling them to better cope with higher interest rates, particularly in Europe.

Foreign exchange and commodities

The USD is currently adopting our central scenario described above, and it has been tumbling against most developed currencies, with the EURUSD pair recently crossing the 1.10 mark, a level last seen in March of last year, as the US Federal reserve started its massive tightening campaign. We believe the EUR could at least reach the level of around 1.14-1.15, its pre-war level. As Japan nominated a new Bank of Japan governor, Kazuo Ueda, there was some hope that there could be a new path to normalization in both QE as well as yield curve control: under Ueda's predecessor the yield target in 10-year JGBs was shifted twice to reach 50 bps from zero. Recent comments just dashed that hope, as the new governor repeated plans to continue with monetary easing, and warning that inflation could fall back again below target. The Japanese Yen is thus now expected to move according to short-term rate differentials with the US, rather than being driven by general USD weakness.

Gold reached USD 2,000 an ounce, a level last seen as Russia began its invasion of Ukraine. Beyond being driven by general USD weakness, we also observed central banks, led by China, Turkey and Uzbekistan, after a Covid hiatus, restarting their purchases of the precious metal: Since November 2022, China alone increased its gold reserves by over 40 tons, or 14% of its total.

Crude Oil rose strongly to above USD 80 a barrel, (WTI), after OPEC+ unexpectedly announced it would cut production by about 1.2 million bpd. The cartel commented that they were acting before a global demand slowdown materializes. This was obviously surprising, as China, a large consumer, is reopening its economy, and we are witnessing above normal inventory levels in the US. We believe the reasons are probably linked to geo-politics: the Middle East is changing, The US is notable for its increasing absence. It is welcome that China, Egypt and Turkey are talking, and that relations between rivals Iran and Saudi Arabia are thawing. Maybe it is a stretch, but could we imagine that they cut production to trip-up the United States, who is attacking China on all economic fronts?

Strategy

In view of the above comments, we decided to maintain our positioning: slightly underweight equities, overweight Europe, and Asia, and underweight the US. We own a partial protective put, maturing in September, on European equities and we are long Gold.

Positioning

Overall Exposure
We are Underweight Equities, and Neutral Fixed Income, with a Gold position, partially USD and JPY hedged. Long a partial protection on European equities.

Equity: Underweight
We have a very sizeable Underweight in US equities and a very sizeable Overweight to Continental Europe, Neutral UK, Neutral Japan, Overweight Asia ex Japan.

Thematic Equities
European Family Holdings, Asian Technology, Health Improving Technologies and Services, European Cyclical Champions, the UN's 17 Sustainable Development Goals, Emerging Markets Healthcare.

Fixed Income: Neutral
Underweight Sovereigns, Overweight Investment Grade USD and EUR Bonds.

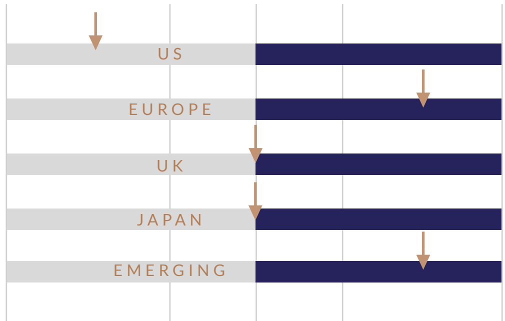
Thematic Fixed Income
Neutral High Yield in USD and EUR, Long US Municipal Infrastructure Bonds, Long Hybrids, long Financial Credit and Long Asian Bonds.

Currencies: Portfolios have a 5% USD exposure.

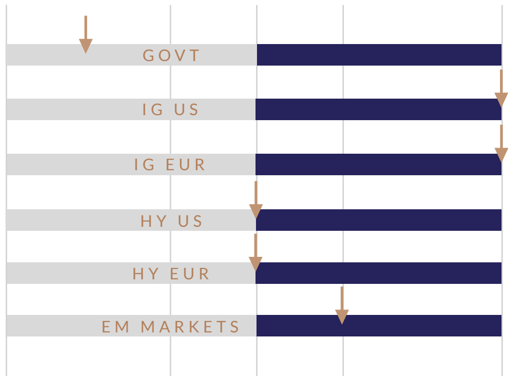
Commodities: Overweight
Long Gold.

Conviction thermometer

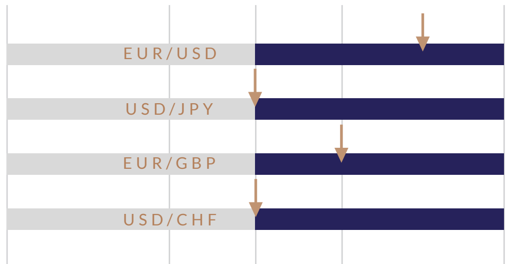
Equities



Bonds



Currencies



Commodities

Market overview as of 31st march 2023

Equities (local ccies)	Level	5D	MTD	YTD	2022
MSCI WORLD	2 791,44	3,78%	3,16%	7,88%	-17,71%
GERMANY DAX	15 628,84	4,49%	1,72%	12,25%	-12,35%
FRANCE CAC40	7 322,39	4,38%	0,86%	13,39%	-6,71%
UK FTSE100	7 631,74	3,14%	-2,48%	3,55%	4,57%
BELGIUM BEL20	3 793,19	4,60%	-2,79%	2,60%	-11,47%
SWISS MARKET INDEX	11 106,24	4,72%	1,59%	5,09%	-14,29%
EUROPE EURO STOXX 50	4 315,05	4,46%	2,01%	14,32%	-8,55%
US S&P500	4 109,31	3,50%	3,67%	7,48%	-18,13%
NASDAQ 100	13 181,35	3,25%	9,54%	20,77%	-32,38%
RUSSELL 2000	1 802,48	3,96%	-4,78%	2,73%	-20,46%
JAPAN TOPIX	2 003,50	3,54%	1,58%	7,07%	-2,48%
MSCI EMERGING	990,28	1,93%	3,04%	3,97%	-19,81%
BRAZIL IBOVESPA	101 882,20	3,09%	-2,91%	-7,16%	4,69%
MEXICO MEXBOL	53 904,00	2,15%	2,21%	11,43%	-5,77%
HS TECH	4 303,71	1,87%	9,67%	4,26%	-26,66%
CHINA CSI 300	4 563,77	0,60%	-0,45%	4,67%	-19,83%
INDIA SENSEX	58 991,52	2,55%	0,05%	-2,87%	5,77%
KOREA KOSPI	2 663,34	2,57%	2,66%	10,76%	-23,21%
HONG KONG HANG SENG	20 400,11	2,43%	3,49%	3,51%	-12,56%
AUSTRALIA ALL-SHARE	4 157,88	3,00%	-2,84%	3,08%	0,23%
SAUDI ARABIA TADAWUL	10 590,10	1,60%	5,70%	1,99%	-4,96%

US: Sectors	Level	5D	MTD	YTD	2022
COMMUNICATION SVCS	191,53	1,46%	10,39%	20,50%	-39,89%
CONSUMER DISCRETIONARY	1 163,98	5,58%	3,12%	16,05%	-37,03%
CONSUMER STAPLES	780,38	2,53%	4,23%	0,83%	-0,62%
ENERGY	634,90	6,22%	-0,21%	-4,71%	65,43%
FINANCIALS	535,28	3,78%	-9,55%	-5,56%	-10,57%
HEALTH CARE	1 510,73	1,77%	2,22%	-4,31%	-1,95%
INDUSTRIALS	856,59	4,43%	0,66%	3,47%	-5,51%
INFORMATION TECHNOLOGY	2 638,98	3,41%	10,93%	21,82%	-28,19%
MATERIALS	507,92	5,01%	-1,04%	4,29%	-12,28%
REAL ESTATE	234,78	5,31%	-1,40%	1,88%	-26,21%
UTILITIES	344,01	3,08%	4,92%	-3,24%	1,56%

EUROPE: Sectors	Level	5D	MTD	YTD	2022
BASIC MATERIALS	2 899,27	4,16%	-1,82%	-0,25%	-2,41%
CONSUMER GOODS	4 326,11	1,41%	2,87%	4,72%	-7,73%
CONSUMER SERVICES	1 525,51	4,23%	4,14%	19,80%	-15,22%
FINANCIALS	786,31	4,88%	-8,87%	4,90%	-1,93%
HEALTH CARE	3 421,08	3,31%	4,47%	4,80%	-3,72%
INDUSTRIALS	3 335,45	5,03%	0,98%	13,50%	-18,88%
OIL & GAS	1 426,95	5,08%	-6,69%	-0,70%	30,59%
TECHNOLOGY	1 563,85	4,44%	6,64%	22,23%	-25,49%
TELECOMS	574,17	3,53%	1,97%	14,50%	-13,24%
UTILITIES	2 026,20	4,99%	4,20%	8,51%	-6,99%

WORLD: Styles	Level	5D	MTD	YTD	2022
QUALITY	3 489,30	3,01%	6,84%	10,54%	-22,21%
MOMENTUM	3 173,76	3,49%	0,88%	-1,33%	-17,79%
VALUE	11 156,76	4,04%	-0,68%	0,92%	-6,52%
GROWTH	7 898,36	3,51%	6,93%	15,10%	-29,21%
VOLATILITY	8 116,46	3,32%	3,68%	6,07%	-15,74%
SIZE	7 607,39	4,04%	1,32%	6,12%	-15,74%
DIVIDEND	4 584,19	3,64%	3,34%	5,31%	-9,62%

Fixed Income	Level	5D	MTD	YTD	2022
Pan-Euro 3-5 yrs IG	195,61	-0,62%	1,29%	1,51%	-11,37%
Euro Aggregate	226,19	-0,92%	2,00%	2,09%	-17,18%
Pan-Euro HY Hedged Eur	382,78	0,76%	-0,39%	2,75%	-10,72%
Global Inflation hedged EUR	240,04	0,22%	3,10%	2,98%	-18,94%
US Corp High Yield	2 264,90	1,74%	1,07%	3,57%	-11,19%
EM USD Aggregate TR	1 260,87	0,48%	1,24%	2,15%	-15,26%
EM Aggregate TR Local Ccy	141,12	0,34%	2,81%	3,11%	-8,44%
EUR Banks CoCo Tier 1	124,86	6,01%	-11,36%	-8,79%	-12,63%
EU GOVT HEDGED EUR	204,48	-1,20%	2,49%	2,34%	-20,38%
Global Aggregate	2 554,99	-0,37%	3,16%	3,01%	-16,25%

Commodities	Level	5D	MTD	YTD	2022
GOLD	1 969,28	-0,45%	7,79%	7,96%	-3,64%
COPPER	409,45	-0,17%	-0,07%	7,45%	26,84%
OIL WTI	75,67	9,25%	-1,79%	-5,72%	55,01%
OIL BRENT	79,77	6,37%	-4,91%	-7,15%	50,15%

Currencies	Rate	5D	MTD	YTD	2022
EURUSD	1,0839	0,73%	2,49%	1,25%	-6,93%
GBPUSD	1,2337	0,85%	2,62%	2,10%	-1,01%
USDJPY	132,86	1,63%	-2,43%	1,33%	11,46%
USDCHF	0,9153	-0,49%	-2,86%	-1,00%	3,13%
AUDUSD	0,6685	0,60%	-0,65%	-1,88%	-5,60%
EURCHF	0,9841	0,23%	-0,44%	0,26%	-11,08%
USDCNY	6,8736	0,09%	-0,89%	-0,36%	5,28%
USDKRW	1 318,40	0,61%	-1,60%	N.A.	4,22%
USDINR	81,43	-0,36%	-0,59%	-0,67%	9,15%
USDIDR	14 995	-1,06%	-1,67%	-3,68%	7,42%
USDBRL	5,0631	-3,50%	-3,31%	N.A.	7,26%
USDTRY	19,1803	0,57%	1,57%	2,51%	78,81%
BITCOIN	28 395	2,81%	22,67%	71,27%	-64,30%

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