Amplia Monthly Investor Letter

Strong finish on first quarter

Equity investors could embark on Easter holidays with relaxed feelings thanks to the strong first quarter performance of most global stock indices. The Nikkei 225 dominated the scene with its staggering 20.63% total return, followed by the Italian FTSE MIB (+14.49%). The remaining indices all posted mid- to high single-digit or low double-digit total returns, with the Hang Seng being the only exception with its -2.97% respectively.

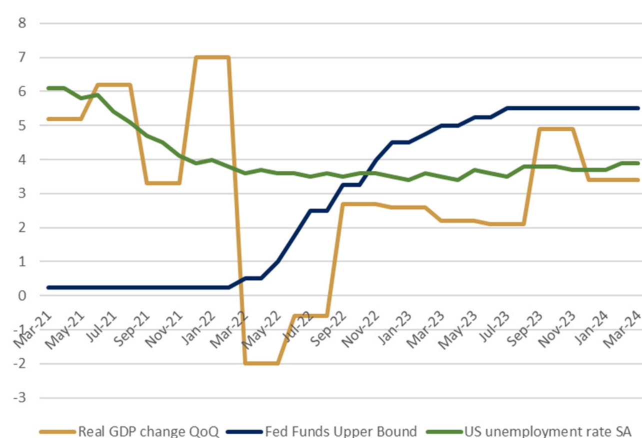
On the currency markets a long tranquil period came to an end, as the Swiss National Bank opened the rate lowering cycle. As a result, the Swiss franc weakened significantly against the currencies of the main trading partners of the Swiss, with the SNB guiding for more cuts towards the end of the year. We think the second quarter will be exceptionally interesting for currency and macro trading, as most of the G10 central banks must communicate whether they will follow the SNB on a policy rate cutting path or not.

US keeps diverging from China and Europe

Aside of the AI stock hype that has lifted the American equity markets and left the European ones stranded due to the little tech weight of the latter, the macroeconomic divergence of the large trading blocs remains significant.

The US unemployment rate has remained below 4% since January 2022, with the consensus expecting a 3.8% tally for the March release due on 5th April. The US GDP growth in turn has come from the COVID-stimulus fueled 5.4% in the fourth quarter of 2021 to the present 3.1% two years later.

In the meanwhile, the Fed has raised its policy rate, the Federal Funds Target Rate's upper bound, from 0.25% to 5.50%. In other words, the historically steep rate hike cycle has had no meaningful impact on the key metrics of the American real economy. It has however almost met its main objective, the suppression of the galloping inflation, with the Core PCE quoting at 2.8% p.a.



Policy rate of the Federal Reserve, the US real GDP change quarter-on-quarter and the country's unemployment seasonally adjusted since March 2021. Source: Bloomberg, Amplia.

This robustness of the American economy has silenced even the most stubborn recession-mongers for now but has also raised questions should the Fed bother lowering the rates at all. We agree and think the market may overestimate the chance of the Fed rate cut: the interest rate futures price in currently a 56% chance of a rate cut in the Fed's June meeting.

Meanwhile, the Eurozone countries continue struggling to find the recipe for growth. Since the beginning of 2022, the highest quarterly real GDP growth print has been 0.8%, and for the fourth quarter the print was a flat zero. Basically, the entire continent has been flirting with a recession the past two years.

In such an environment, companies that derive their revenues from domestic operations instead of exports will struggle to grow. The cost cutting recipe did perhaps work in the first year of the nil-growth era but not anymore.

Neither can European-domiciled companies expect their share of the GDP to grow - it Is rather shrinking in several countries as a result of wage hikes and union strikes. Accordingly, buying companies focused solely on Europe and calling it a value trade is like buying an annuity with constantly dwindling annual payouts and no final value. In other words, the European equity universe may look large but it shrinks massively if one applies even a few basic filtering criteria.

At the same time, the Chinese government is exploring new ways to get back to the growth trajectory with a limited fiscal headroom. The Chinese capital stock in the industrial sector has grown substantially and the government may well try to substitute industry for the ailing real estate sector. We would however tread cautiously there as the trade policies both in Europe and the US are becoming increasingly hawkish again, and the prospect of a new Trump administration may exacerbate that.

Our current asset allocation

In light of this divergence of the trade blocs, we continue to favor US shares over Europe. In Asia, we keep our growth-at-a-reasonable-price approach across countries. In Europe, we focus on exporters, which are mostly industrials and consumer discretionary such as carmakers or sports garment and luxury goods manufacturers.

The share prices valuations are becoming gradually challenging, however pockets of value can be found for instance in those US sectors that are lagging the broader market.

The Swiss market is again trailing the broader European stock markets, however we would expect this to reverse thanks to the high export share of the Swiss large caps and the weaker franc.

We keep bonds in overweight, favouring investment grade issues over high yield. Seeking US exposure also in bonds is advisable due to the differing macroeconomic development in Europe and the US, which may result in higher-for-longer rates in the US and consequently a stronger dollar.

On 2nd April 2024

Yours sincerely

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