



## 2024 – let us think about possible scenarios

Let us start to think on the year past. The year has been marked by expectations of recession in the developed world and positive consequences from the reopening of China - both of which turned out to be the wrong horse to bet on in 2023. This disappointing situation is largely due to investor positioning, the rapid interventions of central banks in March and the poorly understood consequences of inflation in terms of corporate earnings. The markets are now quoting a relatively "goldilocks" scenario, and although we'd like to adhere to it unconditionally, we feel it's essential to consider the macro forces at play. Inflation has declined, but remains sufficiently high for central banks to pivot tomorrow rather than today, while the "landing" process in the US and Eurozone continues. 2024 should therefore be a landing year, and with it, ultimately, a pivot year for central banks. Given this scenario, which asset classes offer the most attractive potential in this context of a soft landing with disinflation? And what would happen in two alternative scenarios: a hard landing with a rapid pivot, or a continuation of the current "no-landing" situation? Our thoughts.

It's always tricky to establish a link between economic scenarios and market performance. The safest approach is probably to break down asset returns into a cash component and an excess cash return. Then, by calculating the average "excess returns" per plan, we can relate them to the plans. Expected returns are then deducted from the sum of our projections in terms of short rates and excess returns per regime, here in the context of a portfolio denominated in US dollars.

The regimes we consider relevant in the case of 2024 are listed in below:

|                                 | Base case    | Alternative scenario 1 | Alternative scenario 2 |
|---------------------------------|--------------|------------------------|------------------------|
| Growth                          | Soft landing | Hard landing           | No landing             |
| Inflation                       | Disinflation | Deflation              | Inflationary           |
| Monetary policy                 | Pivot        | Dovish                 | Hawkish                |
| Average corresponding cash (US) | 5.00%        | 3.00%                  | 6.00%                  |

A base scenario (1) involving a soft landing, with continued disinflation and a central bank pivot in the second half of the year, as inflation returns to levels compatible with central bank mandates.

Scenario (2) is a harder landing, involving a full-blown recession, deflation and explicitly dovish monetary policy - not simply a pivot, but central banks forcefully reorienting policy once confronted with rising unemployment beyond their expectations.



Finally, the blind spot of these first two scenarios is that of a "non-landing", i.e. a total absence of growth contraction and omnipresent inflationary pressures, accompanied by a hawkish monetary policy, with four further rate hikes in the USA.

Using our nowcasting indicators for growth, inflation and monetary policy as a means of dating each type of regime, we derived average excess returns for each of these periods. The final expected returns combine our projections in terms of short rates and excess returns for each regime. Which asset class should be favored for each of these scenarios?

Emerging markets or bonds? Probably a bit of both

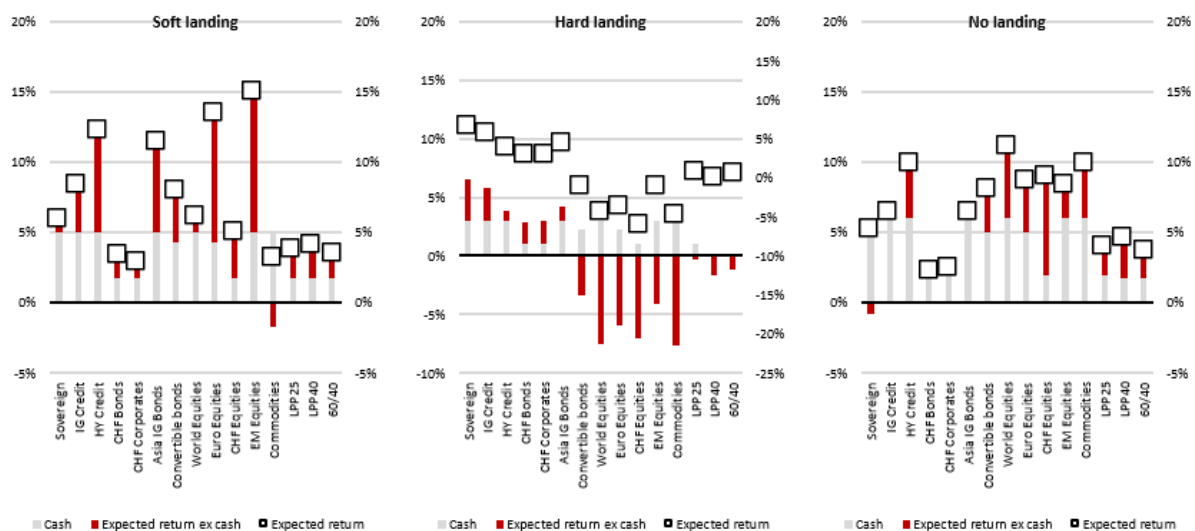


Figure 2 shows the expected returns derived from our calculations for these three scenarios. Bearing in mind that past performance does not necessarily predict future market developments, the key points to be drawn from our calculations are as follows:

**Soft landing:** with inflation moderating and short-term interest rates falling, risky assets could see a new wave of gains. With declining short-term rates and a falling dollar, credit and emerging equities, as well as European equities, could outperform.

**Hard landing:** as short rates fall and earnings prospects wane, equities would be hardest hit, leaving government and Swiss bonds to play their ultimate role as diversifiers. Here too, emerging assets should suffer less, their valuations already discounting a pessimistic outlook.

**No landing:** rising interest rates would increase expected returns somewhat, while earnings growth would benefit from persistently high inflation. Under these conditions, most equities would post roughly the same positive performance, while



bonds would struggle to outperform money market yields, as has been the case this year.

Three asset classes therefore stand out from the crowd: emerging assets in the event of a soft landing, government and CHF bonds in the event of a hard landing, and finally high-yield bonds and global equities in the event of no landing at all. It should also be noted that convertible bonds could offer their traditional convexity in this type of environment. The well-informed, diversified investor will compose his portfolio by assembling different investment vehicles - but far be it from us to judge investors who favor a single portfolio scenario. The main thing is to recognize that a soft landing and a pivot could make 2024 a year with interesting prospects after two complicated years. The greatest danger would be a hard landing by surprise: this is 2024's Achilles heel.

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