

B E R G O S



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Bergos AG is an internationally operating, independent Swiss Private Bank with headquarters in Zurich and a branch in Geneva. We have been active in the Swiss financial centre for over 30 years and can trace our history to the founding of Joh. Berenberg, Gossler & Co. KG in 1590. Our international team is dedicated to all aspects of wealth management and advisory, with a special focus on private individuals, family entrepreneurs, next generation and shipping clients. With a business model focused on pure private banking, we advise our clients on all liquid and non-liquid asset classes and alternative investments.



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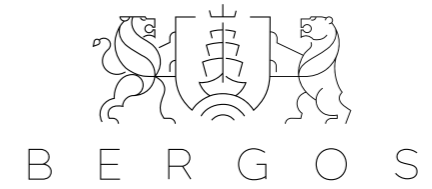
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# E X E C U T I V E S U M M A R Y

Dear Readers,

Investors continued to suffer major price fluctuations on the capital markets in the 3rd quarter. At first, market participants were able to enjoy a dynamically positive stock market development beginning in the middle of the year. However, this quickly turned out to be another bear market rally. In the month of September, the counter movement was cashed in on the fly and the stock markets slid to new lows. Jerome Powell's unequivocal rhetoric leaves little room for interpretation. Inflation, which is

far too high, is being fought by all means and a recession is being accepted. An environment which means a very tough headwind for equities. For the bond markets, however, it is a disaster that also led to substantial losses in the third quarter.

In addition to the restrictive money market policy in most industrialized countries, the very strong U.S. dollar acts as a further global liquidity brake. U.S. dollar debt and commodities, which mostly have to be paid

for with a weak local currency, are becoming an increasing global drag. However, the strong US dollar is not disadvantageous for the United States, where the greenback has a deflationary effect due to cheaper imports.

However, the U.S. labor market and the associated wage trend remain central for the Fed. Managing this is a balancing act. This is because monetary policy has a time-delayed effect. To what extent and with what time lag it will reach the real economy remains a high factor of uncertainty. Furthermore, the labor market also reacts very late in the economic cycle. According to the latest US labor market report from September, a sufficient slowdown is not yet in sight. Nevertheless, it remains to be said that, in light of the multi-layered risks, the stock markets and, in particular, the bond markets have undergone a substantial valuation correction.

This has affected market segments and resilient companies that are worth taking a closer look at. This is also what we are looking at in more depth in this issue of Reflexions.

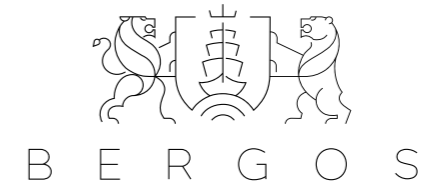
At this point, I would like to introduce our new chief strategist for the bond markets, Christoph Jung, with his analysis on central banks and the bond markets.

Enjoy reading and stay confident!

With best regards,  
Maximilian Hefe

Head of Asset Management

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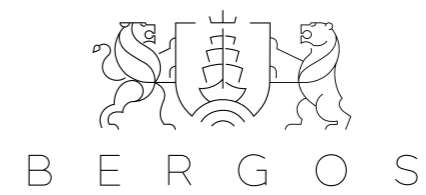
## EDITOR



MAXIMILIAN HEFELE CFA  
HEAD OF ASSET MANAGEMENT

Maximilian Hefe is Head of Asset Management at Bergos since 2003. He is responsible for all discretionary investments solutions offered by the bank. He is Managing Director, Deputy Chief Investment Officer and member of the Bank's Investment Committee.

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# INVESTMENTS OUR EXPERT



**TILL CHRISTIAN BUDELMANN**  
CHIEF INVESTMENT OFFICER

As Bergos' Chief Investment Officer, Till Christian Budelmann regularly comments on events in the international capital markets and examines them in the context of economic and political trends. In close coordination with the responsible asset class heads, he and the CIO Office define the base case scenario, which provides the foundation for the work within the asset class teams. Budelmann is member of the bank's executive board and heads the investment committee.

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# COMPASS

## BASE CASE SCENARIO

BY TILL C. BUDELMANN, CHIEF INVESTMENT OFFICER

The continuing rise in energy and food prices is eroding consumers' real purchasing power and, combined with the global supply chain issues, provides a significant drag on the global economic outlook. We expect a recession for the developed world over the next six to twelve months, but this should be largely anticipated by capital markets.

The persistent inflationary pressure is forcing central banks to take a more hawkish stance. As expected, the US Federal Reserve raised its key interest rate by a further 75 basis points in September. The Fed also believes that further interest rate hikes are appropriate in the future. In addition, the Fed is continuing to reduce its balance sheet and emphasizes that it is determined to bring inflation back to the target level of 2%. For the last two meetings of the year, the futures markets are pricing in up to five more hikes of 25 basis points each. The European Central Bank has also responded, raising key interest rates by a historic 75 basis points at its September meeting. A significant tightening is also expected for the euro zone by the end of the year - an interest rate level of up to 2.25% is likely.

Geopolitically, we are currently obviously concerned about the ongoing Russian war against Ukraine. For the time being, our basic assumption remains that Russia will shy away from directly attacking a NATO member state and thus triggering the alliance case. At the same time, the tensions between China and Taiwan need to be closely monitored. In the US, we currently expect mixed results for the midterm elections: While we favor the Republicans to win back the House of Representatives, the Democrats currently seem to have slightly above average chances of defending their narrow Senate majority.

The economic burdens caused by Covid measures are hardly noticeable in Europe and the United States. However, the risk of renewed restrictions is still present, especially in Germany and the euro zone (less so in Switzerland and the United Kingdom and probably not to the United States). China's "zero-covid policy" and the resulting consequences must continue to be included in all considerations.

## GDP ESTIMATES

### EUROZONE

2021: +5.2%  
 2022: +2.5%  
 2023: -1.0%  
 (2024: +1.5 - 2.5%)  
 Slowdown in  
 4Q 2022 - 1Q 2023

### GERMANY

2021: +2.6%  
 2022: +0.8%  
 2023: -1.5%  
 (2024: +1.5 - 2.5%)

### SWITZERLAND

2021: +3.7%  
 2022: +1.5%  
 2023: -0.5%  
 (2024: +0.5 - 1.5%)

### GREAT BRITAIN

2021: +7.4%  
 2022: +2.8%  
 2023: -1.0%  
 (2024: +1 - 2%)

### UNITED STATES

2021: +5.7%  
 2022: +1.5%  
 2023: -0.3%  
 (2024: +0.5 - 1.5%)  
 Slowdown in  
 2Q 2023 - 3Q 2023

### CHINA

2021: +8.8%  
 2022: +3.0%  
 2023: +4.0%  
 (2024: +3 - 4%)

### JAPAN

2021: +1.7%  
 2022: +1.7%  
 2023: +0.5%  
 (2024: +0.5 - 1.5%)

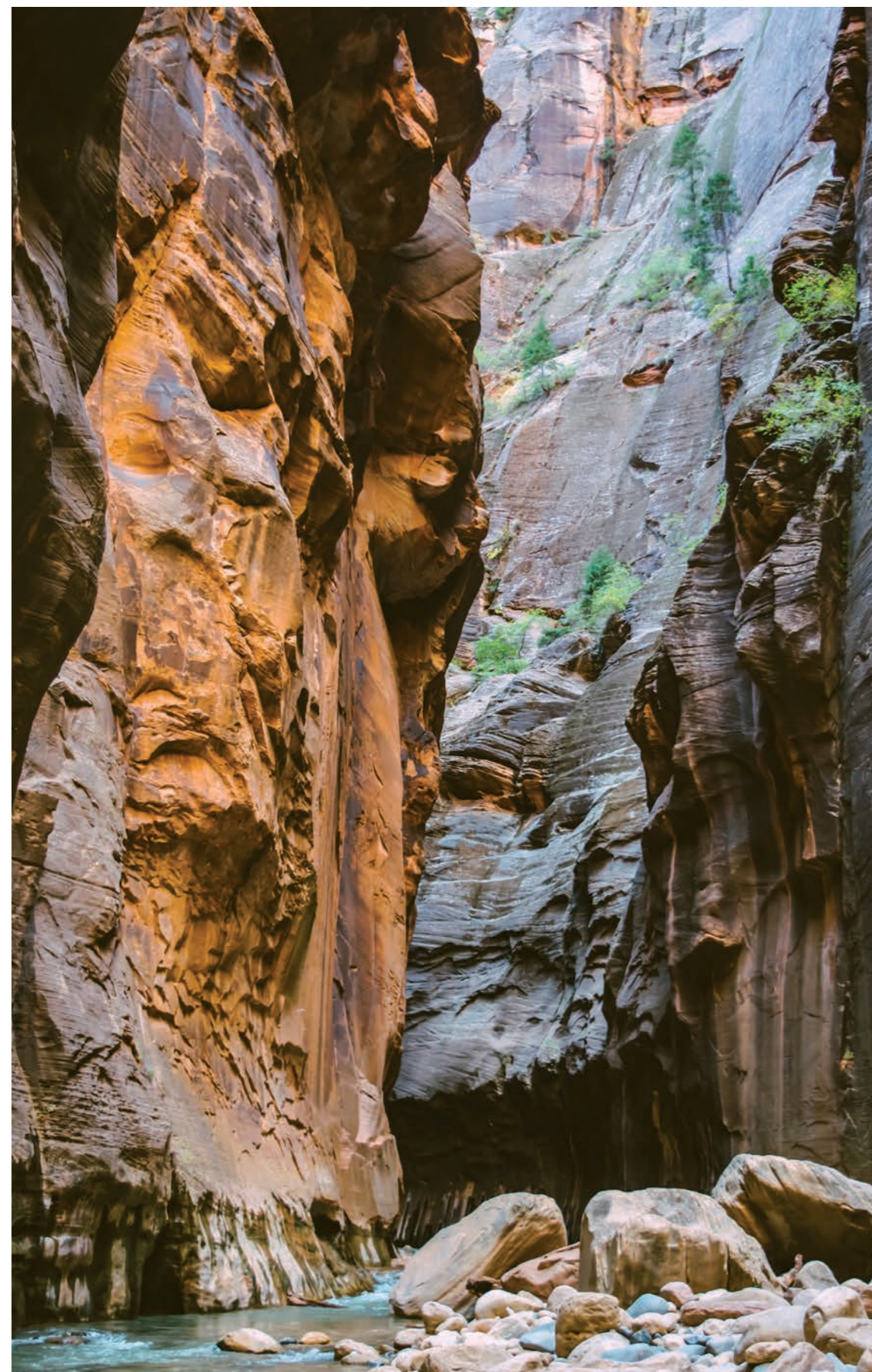
## CPI ESTIMATES

### EUROZONE

2021: 2.6%  
 2022: 8 - 9%  
 2023: 5.5 - 6.5%  
 (2024: lower than  
 2023)

### UNITED STATES

2021: 4.7%  
 2022: 7.5 - 8.5%  
 2023: 3 - 4%  
 (2024: expected to  
 be lower than 2023)



# MACRO ECONOMY

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IN A DOWNTURN

BY DR. HOLGER SCHMIEDING

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The economic outlook has deteriorated further in recent months. High energy and food prices are hitting the European economy hard. In the US, the aggressive interest rate policy of the US Fed is slowly making itself felt. The interest rate-sensitive real estate market is weakening. China's economy is wobbling. The big lockdowns there are over for the time being. But in view of high debts, China's private sector is hardly responding to the previous stimuli. The strong US dollar and higher interest rates are also weighing heavily on some emerging markets.

### **Europe: Recession until spring 2023**

After recovering strongly in the first half of 2022 as the Omicron wave subsided,

economic output in the eurozone appeared to have slipped into recession in the autumn. Sharp increases in energy bills are leaving consumers with less money to buy other goods and services.

Further trouble looms in the months ahead in terms of price inflation. Unlike oil, the high gas prices have not yet fully reached households, as electricity and gas suppliers are only gradually adjusting their sales prices to the market situation. After Russia suspended its gas supplies through the Nord Stream 1 pipeline for an indefinite period at the end of August, price pressure has increased once again. Even if governments cushion this with interventions and aid packages, consumers will have to bear even higher costs.

After two Corona years, a buoyant travel season did manage to keep the eurozone economy from collapsing in the summer. After that, however, hard-pressed consumers are likely to curb their spending considerably. We now expect euro GDP to contract by more than 2% up to and including Q1 2023, but as storage has filled up well, the risk of having to ration gas in winter in Germany and other major European countries has diminished. Otherwise, the recession would be even more severe.

In the downturn, private consumption of goods, private investment and foreign trade goods in particular are likely to decline. By contrast, governments will continue to expand their investment. In view of the currently very high demand for labor, unemployment is likely to rise only slightly in the recession in the euro zone. This limits the downside risks.

Over time, declining demand may help significantly to largely resolve the current supply chain problems. Raw material prices and transport costs are also likely to fall again somewhat in the course of the coming year. This will help both to dampen inflation and to strengthen upward forces again.

#### **New upswing in summer 2023**

Once the winter is over and the gas market has eased somewhat, the euro economy could pick up again in summer 2023. From then on, the rise in incomes could also be above the rate of inflation again, so that consumers will have a little more money in their pockets in real terms after a severe setback. As soon as the presumably mild US recession also comes to an end in fall 2023, exports could also pick up again. After a decline in euro economic output of around

1.5% on average in 2023, we expect growth of 2.4% in 2024. For the UK, we expect a similar trend to that for the euro zone.

#### **Transatlantic difference**

Consumers in the USA are also suffering from high prices. But unlike Europe, the USA is not dependent on Russian natural gas. By contrast, the United States is suffering from home-grown inflationary pressure. With its late but more forceful turnaround on interest rates, the US Fed is likely to dampen demand in such a way that the US economy stagnates at the beginning of 2023 and then falls into a mild recession until the fall of 2023, with declining consumption of goods in particular and less investment, especially in housing construction. By contrast, government spending, including public investment, is likely to support the economy.

#### **The highest inflation in 40 years**

In the US, price pressure has apparently already passed its peak. While wage increases will remain high for the time being, somewhat lower prices for gasoline and used cars are providing relief for consumers. As the labor market slowly loses momentum, wage pressure could also ease in a few months.

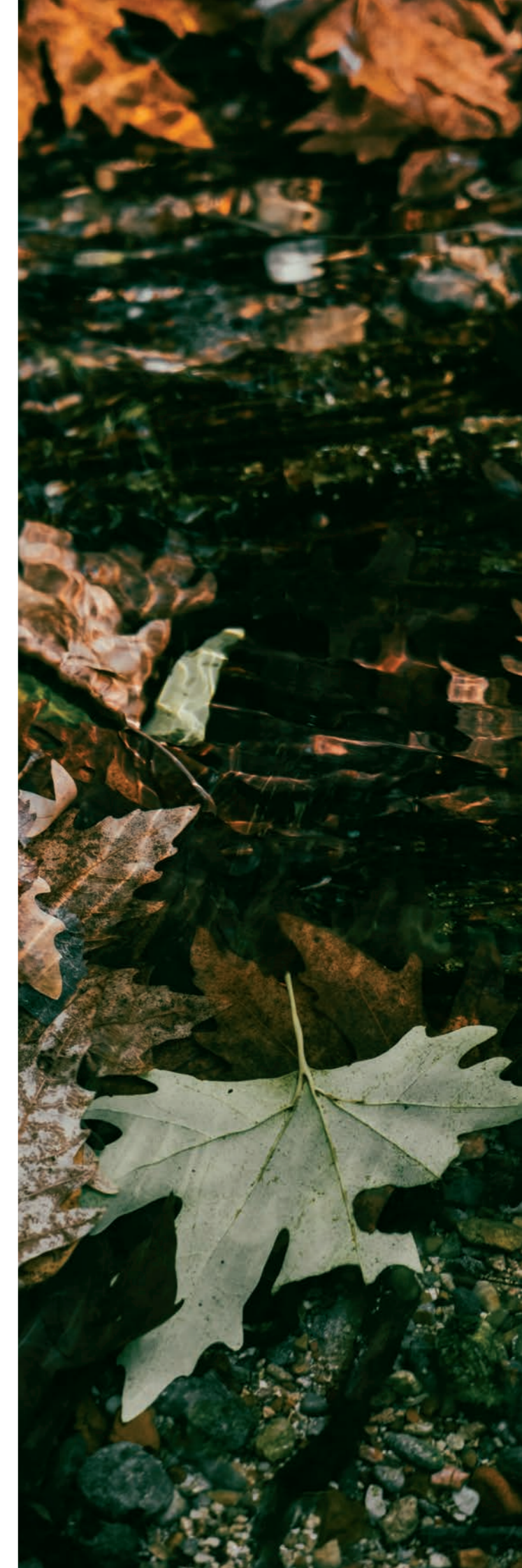
Unlike in the United States, consumers in Europe will have to adjust to noticeably higher electricity and gas prices for the time being. This is because the further increase in prices for natural gas imports and electricity has not yet fully reached consumers. In Europe, the inflation rate could even slightly exceed 10% in the fall before falling back in 2023. The exact inflation profile will also depend on the extent to which governments absorb the energy price shock, shifting

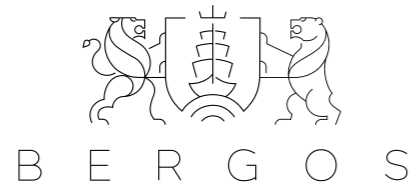
some of the costs from today's consumers to future taxpayers.

In the course of the coming year, inflation rates on both sides of the Atlantic are likely to fall noticeably. At that point, 2022 energy price increases will gradually drop out of year-on-year comparisons. The extent to which inflation then approaches the central bank target of 2% will also depend on the extent to which employees can push through higher wages, which in turn would intensify cost pressure for companies. Presumably, given a structural shortage of labor and the resulting wage pressure, inflation rates will probably settle at somewhat above 2% in the long term.

#### **Central banks shift course - Fed more energetic than ECB**

To prevent high inflation from becoming entrenched, the US Fed and - somewhat more hesitantly - the ECB are also putting the brakes on interest rates. In the US, the key interest rate could even reach 4.75% at the beginning of 2023. As soon as the Fed sees sufficient signs that the recession has sufficiently dampened inflationary pressure, it will then lower interest rates again somewhat, probably starting in the summer of 2023. However, the Fed will not hold this in prospect for the time being. The ECB is following the Fed's lead. However, so far it has no home-grown inflationary pressure to combat in the euro zone. Moreover, the eurozone is probably already in recession. Therefore, we do not expect the ECB to go beyond 3%. It could raise its main refinancing rate to around 2.75% by early 2023 and thereafter maintain this roughly neutral level for the foreseeable future due to the recession.





# M A C R O O U R E X P E R T



**DR. HOLGER SCHMIEDING**  
CHIEF ECONOMIST, BERENBERG

Since 2010 Chief Economist of Berenberg Hamburg and one of the best-known German bank economists. He has received several awards for his forecasts and analyses. In 2016, for example, he was named forecaster of the year by the Süddeutsche Zeitung and in 2015 he was voted best banking economist for Europe for the third time in a row by more than 16,000 international financial experts in the renowned Exel Surveys. He has worked at the Kiel Institute for the World Economy and the International Monetary Fund, among others, and served as Chief Economist Europe for Bank of America Merrill Lynch.





# E Q U I T I E S

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DEFENSIVE POSITIONING OF MARKET PARTICIPANTS LIMITS FURTHER DOWNSIDE POTENTIAL

BY FREDERIK CARSTENSEN

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Global equity markets remain volatile. After markets were betting on a quick pivot by the US Federal Reserve and partly rallied at the beginning of the summer, there was a counter-movement from mid-August. Stubbornly high inflation figures, restrictive tones from central bankers and increasing fears of a recession led to a correction. Over the entire third quarter, the global equity market as measured by the MSCI World Index was unchanged (+0.1% in EUR). From a regional perspective, US equities especially showed relative strength alongside Japanese equities. European equities barely gained any ground as the energy crisis worsened and emerging market equities suffered significantly in some cases from the strong US dollar.

Chinese equities experienced heavy losses in particular. In the coming weeks, the market should continue to focus primarily on inflation figures and the corresponding reactions of central banks.

### **Macroeconomic data as a burdening factor**

Of our four dimensions (macroeconomics, microeconomics, technical picture and sentiment), the macroeconomic data represents a significant stress factor for equity markets. According to the “Global Fund Manager Survey”, the biggest tail risks include topics such as persistently high inflation, hawkish central banks, fears of recession, and geopolitics (including the war in

Ukraine as well as tensions between China and Taiwan). The broad US equity market, as measured by the S&P 500, has lost more than 20% from its all-time high in early January and is thus officially in a bear market. However, this means that the equity market has probably already anticipated many of the issues mentioned above.

### European gas supply and US midterms in focus over the short term

As outlined in the economic section, economic data is likely to deteriorate further for the time being. In all probability, Europe will already be in a recession at this point. The contraction of the economy over the winter is also likely to be more pronounced than on the other side of the Atlantic. The

war in Ukraine and the energy crisis are global issues, but they weigh particularly heavily on Europe. Concerns about gas supplies are hitting the German economy especially hard. Gas prices in Europe are already a multiple of those in the United States. However, investors should not fear a recession too much. It may be unpleasant, but it is part of the economic cycle and can have a cleansing effect.

In addition to the extremely tense geopolitical situation, the US midterms on November 8 must also be taken into consideration. In the US, Biden's approval rating remains low, but we currently expect a mixed picture in the midterm elections: While we favour the Republicans to win back the House of Representatives, the Democrats currently

seem to have slightly above average chances of defending their narrow Senate majority. A divided government is likely to be beneficial for markets.

### Negative earnings revisions

Negative revisions to earnings estimates have also weighed on global equity markets recently. High input costs, which are becoming increasingly difficult to pass on to the end consumer, and weaker demand have created headwinds. While the analyst consensus at the beginning of the year still expected double-digit percentage US earnings growth for 2022, the latest revisions now point to only a mid to high single-digit percentage range. Over the course of the Q3 reporting season, estimates are likely to be adjusted further downward. This would also be in line with the typical seasonality of earnings revisions. Nevertheless, we do not expect aggregate corporate earnings to collapse by 10-20% as seen in past recessions.

In terms of valuations, equities (when measured against themselves) are more attractive than at the beginning of the year. Compared to Europe, the US equity market remains expensively valued with a price earnings ratio of around 17. The reason for this, apart from the concentrated index structure (expensive growth companies with high index weights), is the geopolitical component. Europe is regionally closer to the war in Ukraine and, as a large net energy importer, suffers more from the energy crisis. At the same time, the export dependency on China is significantly higher.

### Sentiment and positioning as a ray of hope

Supportive for equity markets, and one of the reasons why we are currently refraining from underweighting equities, is the

extremely pessimistic investor sentiment and positioning. This has proven to be a reliable contrarian indicator in the past. Whenever the number of bears, as measured by a survey of the American Association of Individual Investors, has been above 60% (as is currently the case), equities have been able to post mostly positive returns in the following months. At the very least, the current positioning, together with the low equity ratios of systematic investment strategies, should limit the further downside potential for equities.

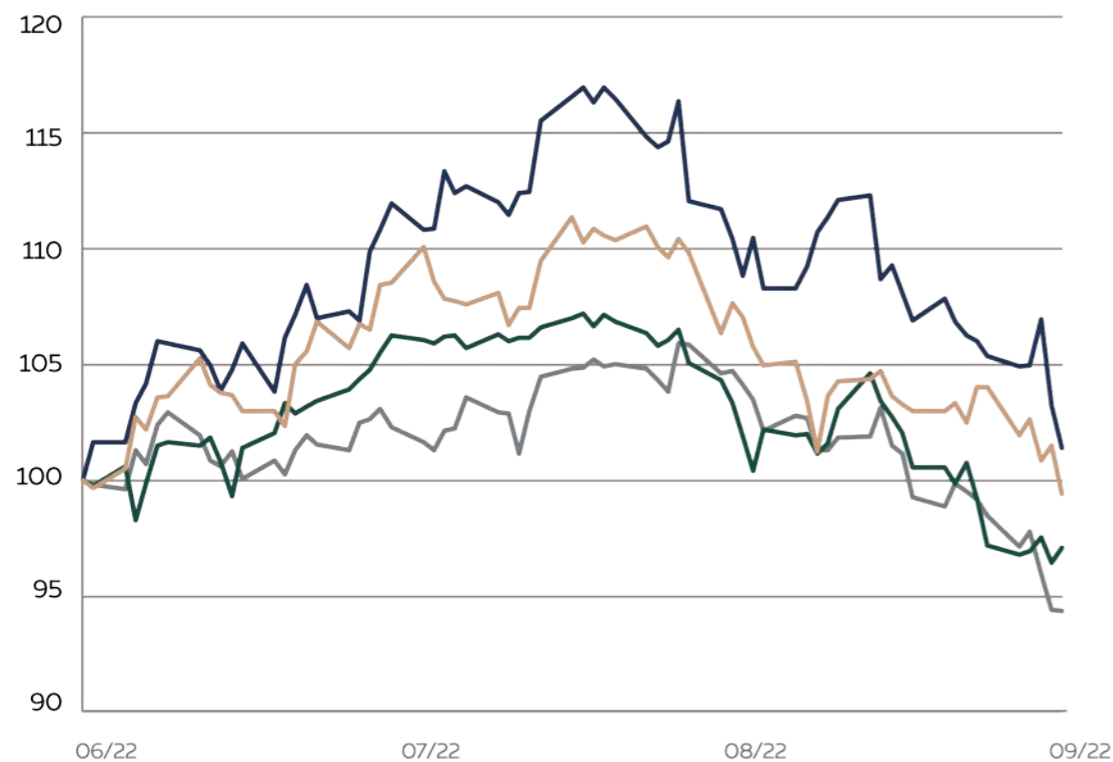
### Balanced positioning, US and Japanese equities preferred

We maintain our view that current opportunities and risks balance each other out. Against this backdrop, we are positioning ourselves with a neutral overall equity allocation into the fourth quarter, with a broad and global diversification. By the end of the year, the economy should have weakened sufficiently and fading demand should favour a more pronounced decline in inflation. With less hawkish central banks and a possible recovery from a recession in 2023, investors should then become more optimistic about equities and stock markets should rally – after all, they usually price in expected developments six to twelve months in advance. Investors with a defensive positioning should consider whether it is time for a more balanced positioning.

In terms of regions, we continue to see the greatest upside potential in the US. Not only do we consider the overall economy to have an advantage over Europe, but Europe's energy dependence on Russia also represents a particular factor of uncertainty for Europe's economic outlook. We remain less constructive on emerging markets. In China,

FIGURE 1: DEVELOPMENT OF INTERNATIONAL EQUITY MARKETS IN Q3 2022

— S&P 500 net in EUR — Stoxx 50 net in EUR — MSCI Emerging Markets net in EUR — TOPIX net in EUR



INDEXED TO 100

SOURCE: BLOOMBERG, BERGOS, DATA AS OF 09/30/2022

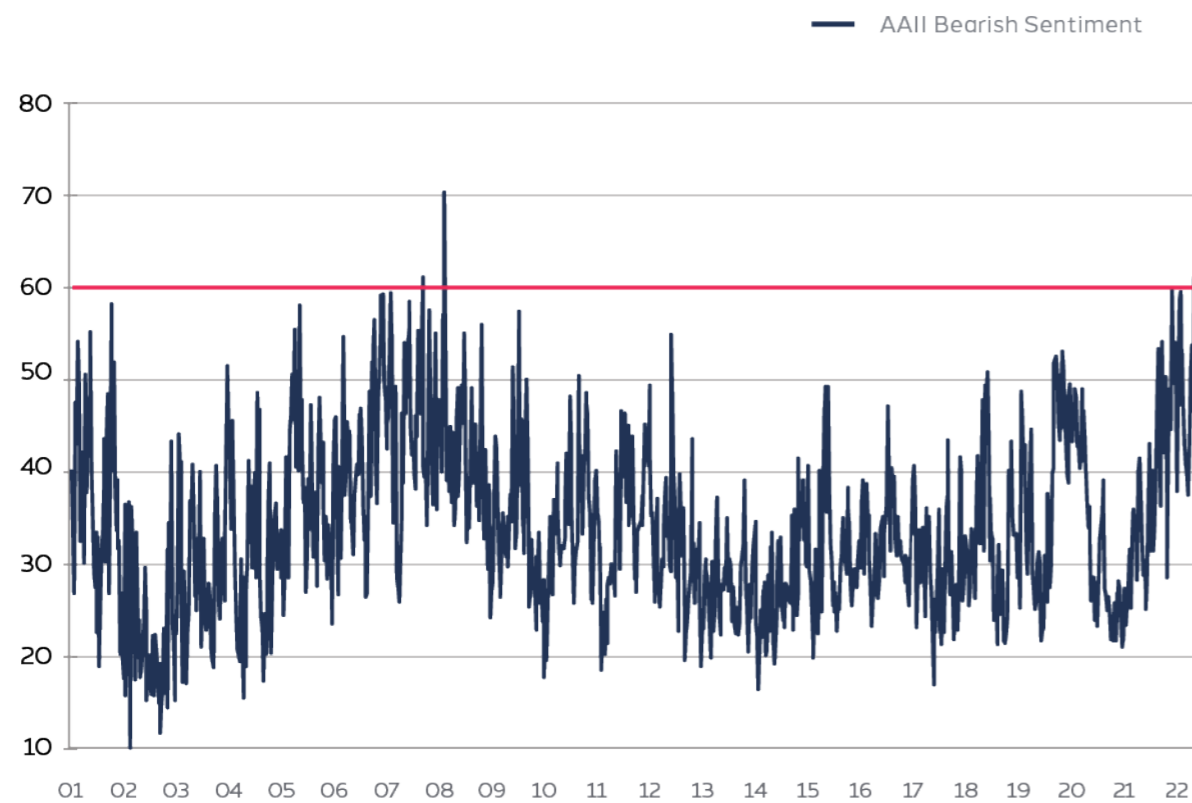
there are increasing signs of an economic downturn and their “zero-covid policy” and the resulting consequences must continue to be included in all considerations. Japan suffers indirectly from China, but compared to the rest of the major industrialized countries, we see relatively little inflation here so far and monetary policy therefore remains expansive. As a result, we continue to overweight Japan.

**High-quality stocks should form the core of any portfolio**

We currently consider active selection to be even more important than the regional focus. The days of index investments are over. However, we warn against excessive

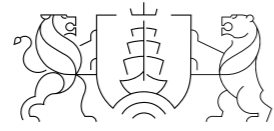
bargain-hunting because investors could quickly find themselves saddled with junk. Instead we recommend carefully selected quality companies with pricing power that are able to pass on increased costs to customers. They should have low debt, stable business models, strong competitive positions, solid balance sheets, and high levels of cash. Such companies reported significant, year-over-year profit growth in the second-quarter reporting season. Despite solid profits, the prices of such quality stocks are extremely volatile. Equity investors should be willing and able to withstand that.

FIGURE 2: AAIL BEARISH SENTIMENT



SOURCE: AAIL, BERGOS, DATA AS OF 09/30/2022





B E R G O S

E Q U I T I E S  
O U R E X P E R T



F R E D E R I K C A R S T E N S E N  
E Q U I T Y S T R A T E G I S T

Frederik Carstensen joined Bergos in 2015 as a portfolio manager and has since been responsible for various equity funds and mandates. As a member of the Investment Committee, he leads the top-down equity strategy and regularly comments on events in the international equity markets.





# B O N D S

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BY CHRISTOPH JUNG

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We look back on a turbulent third quarter: A new era in European and U.S. central bank policy has begun. Disillusioned by a new reality, they carried out an remarkable change of course in monetary policy. On the other hand, the bond markets climbed to new yield levels with high volatility, which we have not seen for a long time.

### **The new era of «whatever it takes 2.0»**

Rising inflation figures, which reached 8.6% in the euro zone in July, prompted the ECB to raise interest rates sharply and accelerate

the pace of monetary tightening. Thus, it surprised at this time that the ECB raised the key rate in July by 50 basis points instead of 25. This was an important first step to ensure that inflation returns to its target of 2% in the medium term, as they emphasized. In doing so, it completed the first rate hike in the euro area since 2011 and also ended the era of negative interest rates with this increase. In addition, the ECB approved a Transmission Protection Instrument (TPI). The TPI is designed to ensure that the desired effects of the monetary policy stance reach all euro area

countries as smoothly as possible and can be activated at any time to counter unwarranted, disorderly market dynamics. In other words, in doing so, you want to prevent an excessive widening of the risk premia of countries such as Italy, which, given its high debt level of over 150% of GDP, could be concerned by the new interest burden. In this context, the size of purchases under the TPI depends on the severity of the risks to monetary policy transmission and is not limited in advance. Thus, unlike the U.S., the ECB is still not reducing its balance sheet because they invested maturing bonds from the asset or pandemic emergency purchase program at an unchanged pace. Unfortunately, this plan to avoid fragmentation has not yet manifested itself in the market and the spreads of the peripheral countries continue to widen. The outcome of the elections in Italy has not helped to increase confidence in the market. However, we believe in the ECB's forcefulness and consider yields to be attractive relative to the core countries.

The pressure on the monetary authorities did not abate during the summer break and increased continuously, as the general price trend could not be tamed. Inflation is rising at a rate not seen in 40 years. The meeting in Jackson Hole and the following message from Jerome Powell and the other FOMC members was clear. "Our responsibility to deliver price stability is unconditional". This means, the demand must be contained and inflation seriously curbed. The message to the market was unambiguous that a significantly restrictive level of interest rates is needed, and will be for a while. The Fed, as well as other national banks, seemed ready to do "whatever it takes" to bring inflation under control. For the first time in many years, at least it seems, the fight against inflation is really determining national bank

policy, not that of a mounting recession. They no longer seem to shy away from cyclical braking effects - inflation seems to be galloping too strongly across the board.

The Governing Council of the ECB decided to take the biggest interest rate step since the introduction of the euro by raising key rates by 75 basis points in September to 1.25%. The Fed also followed suit in the same month with another 75bps increase to a target range of 3% to 3.25% - and more are to follow.

### The bond market - like a phoenix rising from the ashes

The past quarter was characterized by extremely high volatility in the bond markets. Surprisingly, yields at the longer end of the yield curves fell rapidly and significantly in July. For example, yields on 10-year Bunds almost collapsed from their contemporaneous high of around 1.75% by almost 1% to 0.82%. In the case of 10-year Treasuries, the decline, which was surprising in its extent and speed, was also initially large. From the beginning of August, the bond markets made a remarkable comeback. The 10-year U.S. Treasury climbed back above the 4% mark for the first time in around 12 years, while the yield on the two-year bond soared to almost 4.5% as can be seen on figure 1. This continued the pronounced yield differential between short- and longer-term bonds, which widened to around 50 basis points during the quarter. This negative differential is known to be a strong recession signal. Yields in Europe also shot up - the 10-year government bond posted a sharp rise above the 2.2% mark. The list of government bonds now showing yields not seen years ago continues to grow. This remarkable interest rate movement can also be observed in the ICE BofAML MOVE

index, which is reflected in the figure 2. The Move Index is now recognized as a measure of U.S. Treasury bond interest rate volatility and is used to interpret the changing risk sentiment in U.S. Treasury bond markets. The index briefly climbed to 158.9 points at the end of September, a level last seen during the Corona pandemic or the financial crisis.

In such a market environment, fiscal incentives have to be set in a well-considered way, as the British government had to learn. The uncovered tax plans of the new British government sent the markets into turmoil. Prices of British government bonds (Gilts) came under heavy pressure, leading to further near-panic selling by British pension funds, which has run into liquidity difficulties due to margin calls and had to sell Gilts on a large scale. Ten-year Gilts rose from 3.5% to 4.6% within three days. As a

result, the Bank of England (BoE) even had to step in as an emergency buyer at short notice and purchase government bonds to support prices. By doing so, the BoE acted against its actual plan to reduce its balance sheet and temporarily start buying long-dated bonds to calm the market chaos triggered by the new government's so-called mini-budget.

### High yields = high financing costs

Due to the higher interest rates, financial conditions are tightened as financing costs increase and consequently also have a negative impact on the profitability and earnings of companies. On the other hand, consumers are also affected by the higher borrowing costs in their financed purchases. The negative impact can be seen in the accumulation of rating downgrades, but also in the newly anticipated increased risks

FIGURE 1: YIELD DEVELOPMENT OF 2- AND 10-YEAR TREASURIES SINCE 2005



SOURCE: BLOOMBERG; DEPICTION BY BERGOS AG

shown in credit spreads in figure 3. Market participants believe that the first signs of a recession, however, have not yet been fully priced into credit spreads. Credit spreads for investment grade corporates as measured by Bloomberg aggregated indices are hovering around 150bps in the US and already around 220bps in Europe. In light of the ongoing uncertainties, continued high volatility and possibly further increases in yield spreads can also be expected in the future. In previous periods of slowing growth and stress in credit markets, spreads have typically risen above 200bps. In our view, investors would do well to remain cautious on corporate credit, but on the other hand it offers attractive yields by historical standards - a selective approach remains essential and financial companies currently appear to be priced slightly more attractively in the market.

### Demand and supply in decline

With regard to the primary market, we also observed the strong uncertainty, particularly in the high-yield segment. New issuance business is very sluggish and the volume of issued US high yield corporates bonds fell by a staggering 78% year to date. The volume of new corporate bonds issued in September, when new issuance normally picks up due to the summer break, was one of the worst since 2014. Companies appear to be waiting for better terms and increased demand in the market. In the last week of September alone, investors pulled \$10.3 billion out of investment grade bonds - the third largest measured «outflow on record» according to Refinitiv Lipper.

As is widely known, emerging markets generally experienced a strong recovery in

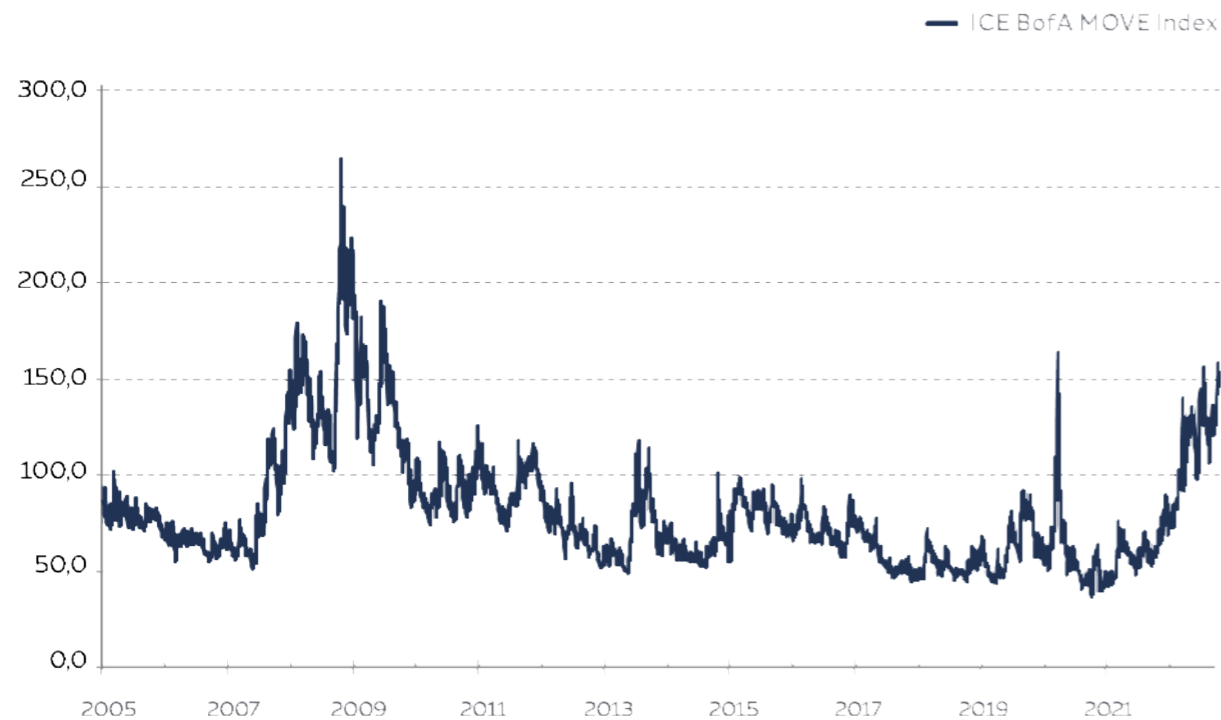
2021, accompanied by a remarkable improvement in fiscal balances and a decline in debt-to-GDP ratios. In 2022, however, the tide turned. The strong US dollar and rising external financing costs have led to financing problems in several vulnerable emerging markets. As a result, concerns about emerging market insolvency have increased, as can be seen from the International Monetary Fund's latest calculations that 60 percent of low-income countries are in debt distress or at risk in this regard. As always, there are winners and losers, as some countries are more affected by the current external environment than others due to differences in food and energy prices and the associated social impacts. Underlying economic momentum and the robustness of economic growth remain central. We still rate bonds as attractive after the sharp correction in risk premiums. But more caution than ever

is needed. Commodity-exporting countries seem to be at an advantage.

### On the safe side with shorter duration

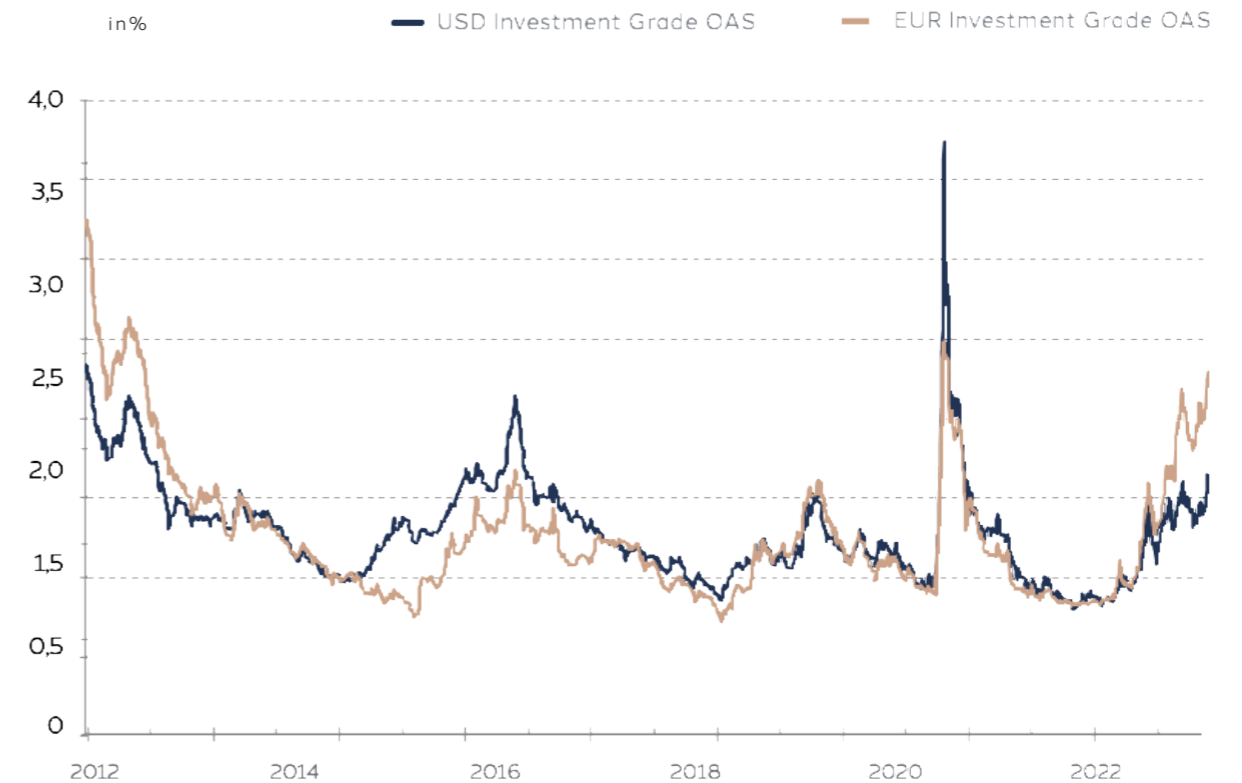
In view of this development, we believe that shorter duration bonds, with their now higher initial yields, also have the potential to sustain the current market volatility better. Not least because they are less price-sensitive to changes in interest rate and credit risk premiums than bonds with longer maturities. Short-maturity portfolios can again offer some resilience in times of heightened uncertainty: Therefore, we have consistently used and continue to use an investment strategy with a relatively short duration in a portfolio context. Tactically, however, we have slightly increased the duration in the EUR portfolio due to the rapid rise in interest rates mentioned at the

FIGURE 2: THE DEVELOPMENT OF INTEREST RATE VOLATILITY BASED ON THE MOVE INDEX



SOURCE: BLOOMBERG; DEPICTION BY BERGOS AG

FIGURE 3: THE DEVELOPMENT OF CREDIT SPREADS FOR INVESTMENT GRADE CORPORATES IN USD AND EUR



SOURCE: BLOOMBERG; DEPICTION BY BERGOS AG

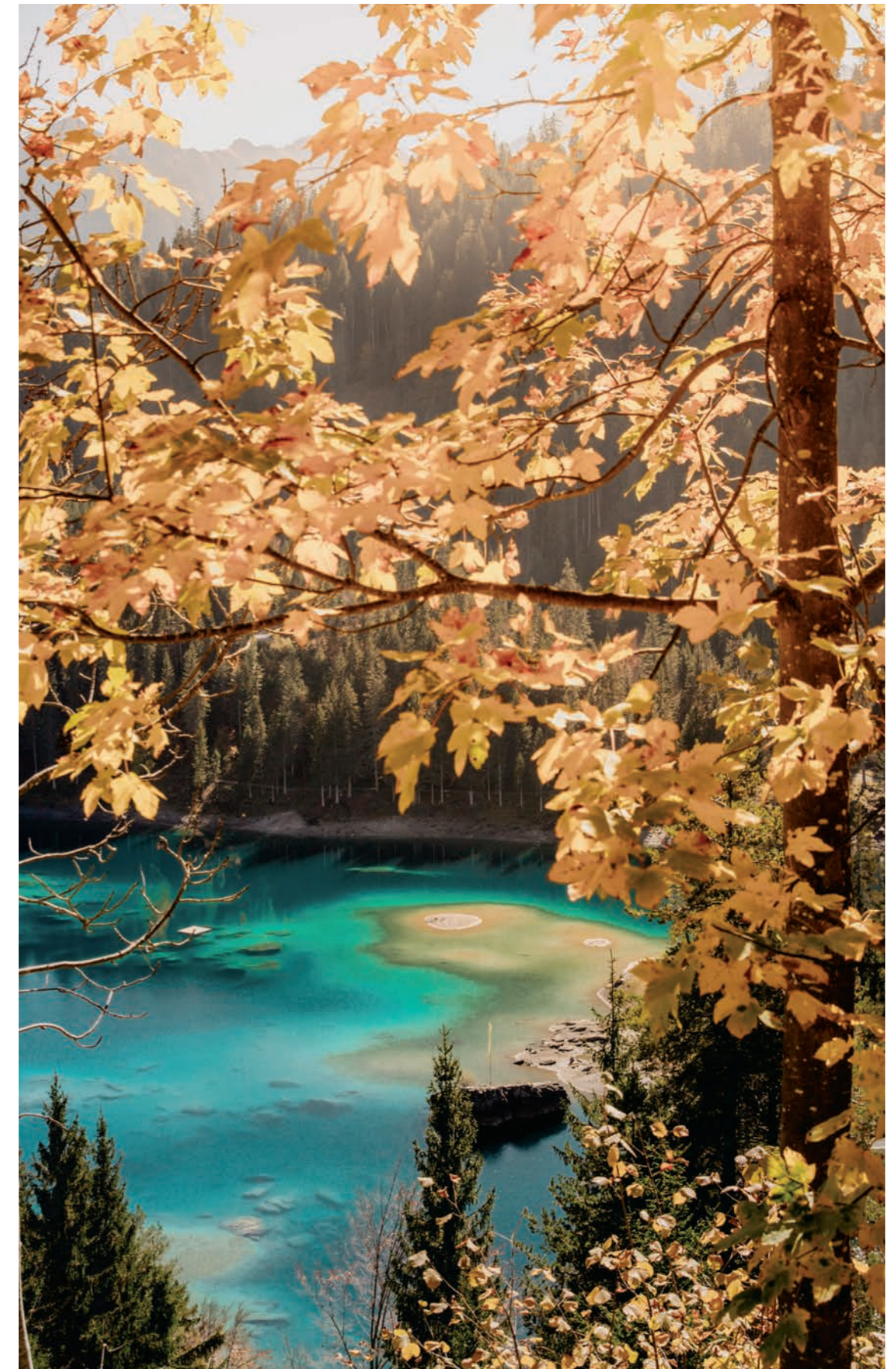
beginning - but we still like to be short in this context.

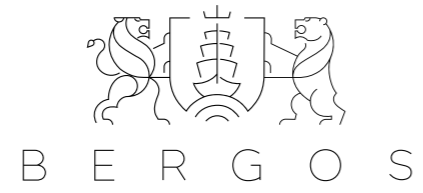
### **Bonds will again function as a buffer**

If the U.S. economy does indeed grow relatively stable in the coming quarters, it can be assumed that key interest rates will initially rise again sharply and only peak at just under 4.75% in the course of 2023 - as stated by the Fed. This would still represent an interest rate increase of 1.5%.

In Europe, market implied policy futures show rates rising to 2.5% by mid-2023. As we believe this rate hike cycle is intact, we remain underweight fixed income overall due to the fragile environment. Bonds are not yet our first choice in our tactical asset allocation. In USD bonds, however, the opportunities have increased significantly and thus we are no longer negative on USD

denominated bonds, but neutral. The fact is that current yields in USD, EUR but also CHF bonds are higher than they have been for a long time, which in our opinion represents a convincing entry point supporting solid forward-looking returns. The potential for capital appreciation is finally back and the days when fixed income prices were kept high and yields low by central banks are over. At long last, the asset class's ability to diversify against riskier assets is starting to be able to work again. In the event of another economic shock or an equity sell-off, we believe the asset class could benefit from the flight to safety and soon resume its «old» function.



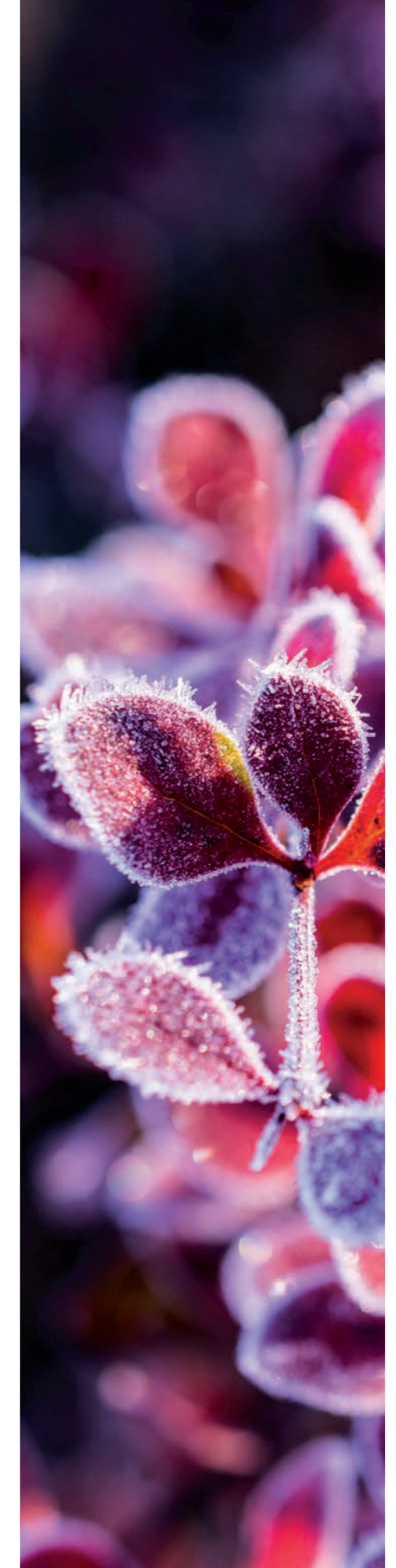


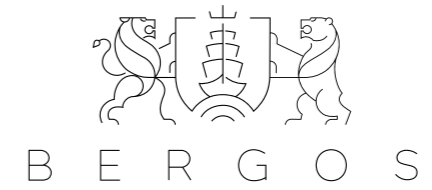
# B O N D S O U R E X P E R T



C H R I S T O P H J U N G C I I A , F R M  
B O N D S T R A T E G I S T

Christoph Jung joined Bergos this year and is responsible for the top-down strategy as well as the bottom-up approach for fixed income investments. As a member of the investment committee, he is particularly responsible for the fixed income strategy.





# ALTERNATIVE INVESTMENTS

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BY SOUMAILA TÉKÉTÉ

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**Some Hedge funds strategies manage to escape the current negative market forces.**

Global macro funds and trend-following strategies are among the few asset classes that have performed positively so far in the course of the calendar year. This is particularly true for those macro strategies that specifically target rising yields and the associated short- and medium-term market trends e.g. short interest rate positions.

In general, we have seen the relative attractiveness of hedge fund strategies increasing significantly this year. Portfolios should always strive for diversification. This is

especially true in market phases like we are currently experiencing this year, where the usual sources of diversification seem to be suspended and all traditional asset classes are suffering in unison from the general rise in interest rates. In this constantly challenging market environment, uncorrelated hedge fund strategies are likely to remain in demand.

**Alternative Credit & Private Debt remains attractive in relative terms.**

One major advantage of alternative credit & private debt remains the variable interest rate component, i.e. the interest rates are

adjusted to the prevailing interest rate level. The asset class is therefore hardly susceptible to the direct effects of the current rise in interest rates.

The indirect negative effects of the current rise on the economy and credit risk, on the other hand, are also felt in this asset class in the form of higher yields, depending on the respective credit risk or rating. However, these higher yields also offer medium and long-term investors potentially attractive entry opportunities - ultimately, they also provide a certain buffer against slightly rising default rates, which are likely to be associated with an impending recession.

In addition, this segment also includes strategies that have been almost entirely spared by the more severe distortions in liquid bonds & debt instruments for the time being. Hence, in this asset class, too, there are strategies that are largely uncorrelated and can therefore contribute a high degree of diversification to a portfolio.

**On the commodity markets, economic fears overshadow possible medium-term bottlenecks.**

In the commodity markets, the impending recession is increasingly making itself felt in prices. Here, too, most indices are well below their highs of the first half of the year (energy ca. -20%, industrial metals ca. -40%, precious metals ca. -20%).

After medium-term supply fears, industrial metals have already been increasingly overshadowed by concerns about economic demand, this now also applies to the majority of the energy markets - even though the

energy crisis is still in full swing, particularly in Europe. While OPEC is likely to step up its efforts further in the future by cutting crude oil production to support prices, the situation remains tense, particularly with regard to gas supplies, due to the geopolitical situation. In Germany, for example, contrary to fears a few months ago, inventories are now almost full again, which has given rise to a little more confidence with regard to the upcoming winter. However, if gas supplies from Russia continue to fail, the issue is likely to become acute again for everyone by winter 2023/2024 at the latest. The burden on Europe therefore remains significantly higher than for most other regions of the world, even for raw materials as an economic input factor.

**Gold not yet in demand despite ongoing recession fears.**

The supposedly “safe haven” gold, cannot benefit from the ongoing risk aversion. Quite the contrary, because here, too, prices were at times more than 20% below their highs from the first half of the year. In particular, the increased opportunity costs in the form of real interest rates have continued to provide a stress test here. However, it remains to be seen whether this rise in real interest rates will continue unabated for the time being or whether declining inflation figures in the foreseeable future will actually give central banks the leeway to abandon their strict monetary policy. Until then, the price of gold is likely to lack sustainable upward momentum, despite ongoing crises.

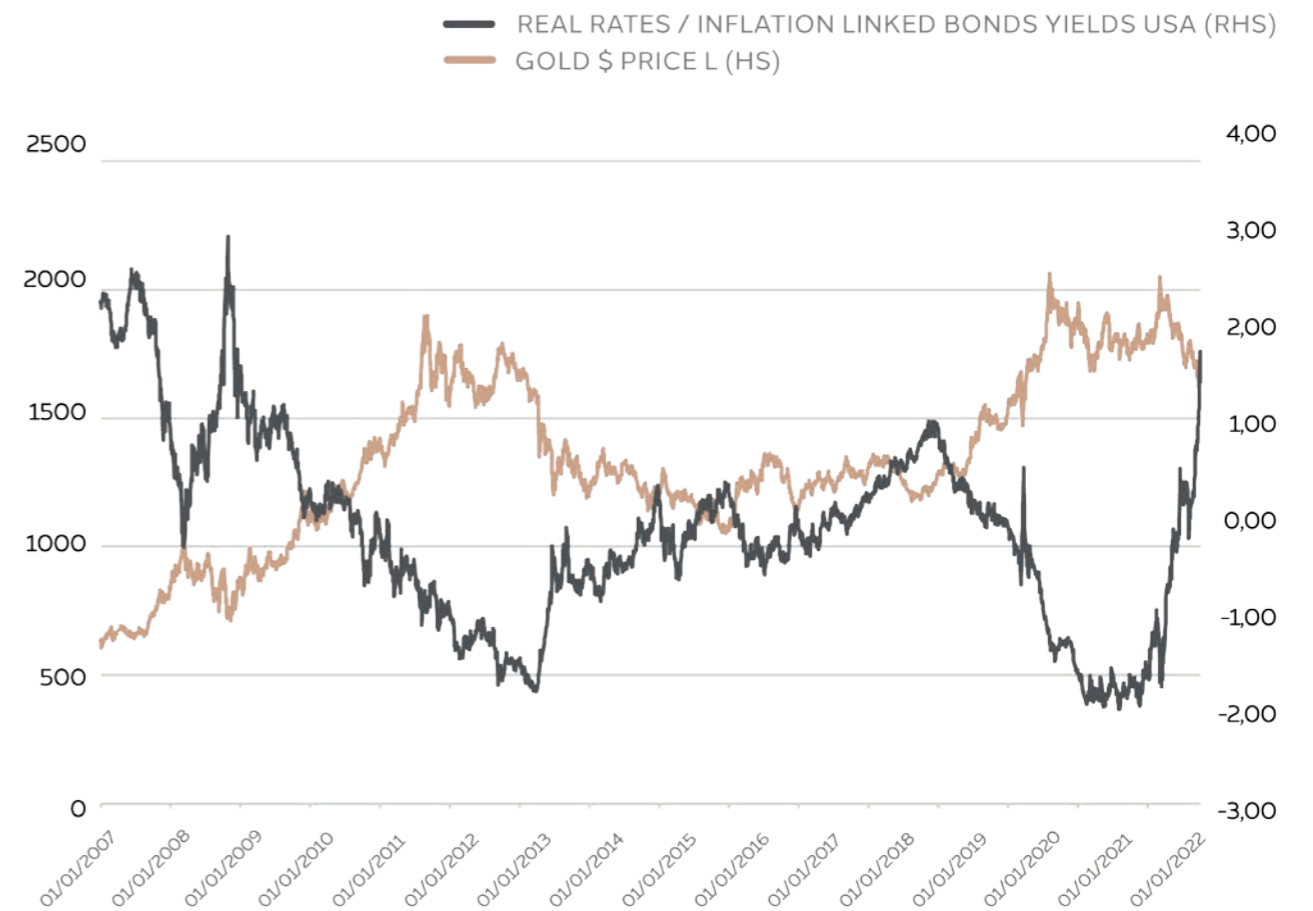
**An end to the crypto winter does not seem to be in sight for now.**

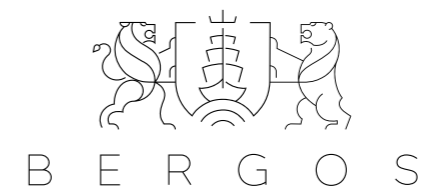
In cryptocurrencies, the downward pressure has reduced in the past quarter, but the markets are still in the middle of a consolidation.

Below the market surface, there were also notable changes here. First and foremost, Ethereum, the second largest cryptocurrency by capitalization, successfully transitioned from PoW (Proof-of-Work) to PoS (Proof-

of-Stake). A fundamental technical transition that undoubtedly represents a drastic step forward in terms of required computing power, energy efficiency, speed and scalability. However, even this long-awaited and successful event failed to give crypto markets a new boost in the current environment. This fact once again illustrates that the correlation to conventional asset classes and the dependence on general monetary policy has now become very high here as well.

FIGURE 1: INVERTED RELATIONSHIP - GOLD AND US REAL RATES



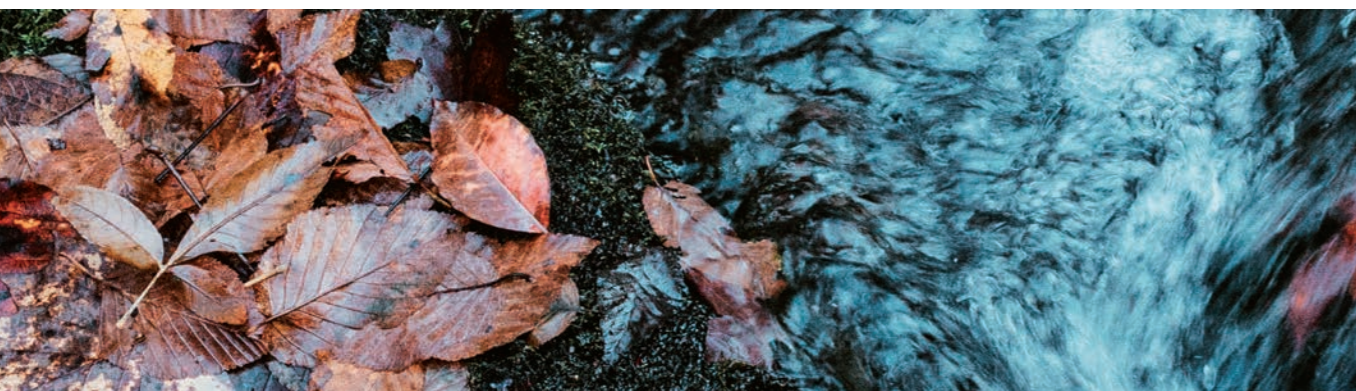


A L T E R N A T I V E  
I N V E S T M E N T S  
O U R E X P E R T



**S O U M A I L A T É K É T É C A I A , C I I A**  
A L T E R N A T I V E I N V E S T M E N T S  
S T R A T E G I S T

Soumaila Tékété joined Bergos in 2016 as a cross-asset strategist and has since been responsible for various investment strategies. As a member of the investment committee, he is also responsible for strategy in the alternative investment area. Previously, he held various portfolio management positions at Union Investment and DZ Privatbank in Frankfurt and Zurich.





# C U R R E N C I E S

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BY DR. JÖRN QUITZAU, BERENBERG GROUP

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## **The euro depreciates significantly**

The mixture of political uncertainty, towering energy prices and a European Central Bank that has been very hesitant for too long further weakened the euro in the past quarter. Against the US dollar, the single currency has really taken a beating and has now fallen to well below parity. At the current level, the euro is undervalued and the US dollar significantly overvalued measured by fundamental criteria. While Europe is starting the autumn with considerable energy supply risks and extremely increased energy prices, the situation in the USA is much more relaxed. The US is not dependent on Russian gas for its energy supply and only has to pay a fraction of the

European prices for energy. The economic consequences of the European energy crisis are not yet foreseeable, so capital is currently tending to flow into the US dollar and other safe investment havens.

After all, the ECB has now clearly positioned itself for the fight against inflation. After the first-rate hike of 50 basis points in July, the ECB made an even bigger move of 75 basis points in September. Aside from these rate hikes, the rhetoric of ECB leadership has also changed. ECB President Christine Lagarde is recognizably concerned with regaining lost trust. Whether this will succeed quickly remains to be seen. In any case, inflation is more likely to be dampened in the short term by political price brakes

than by interest rate hikes – because monetary policy transmission takes time.

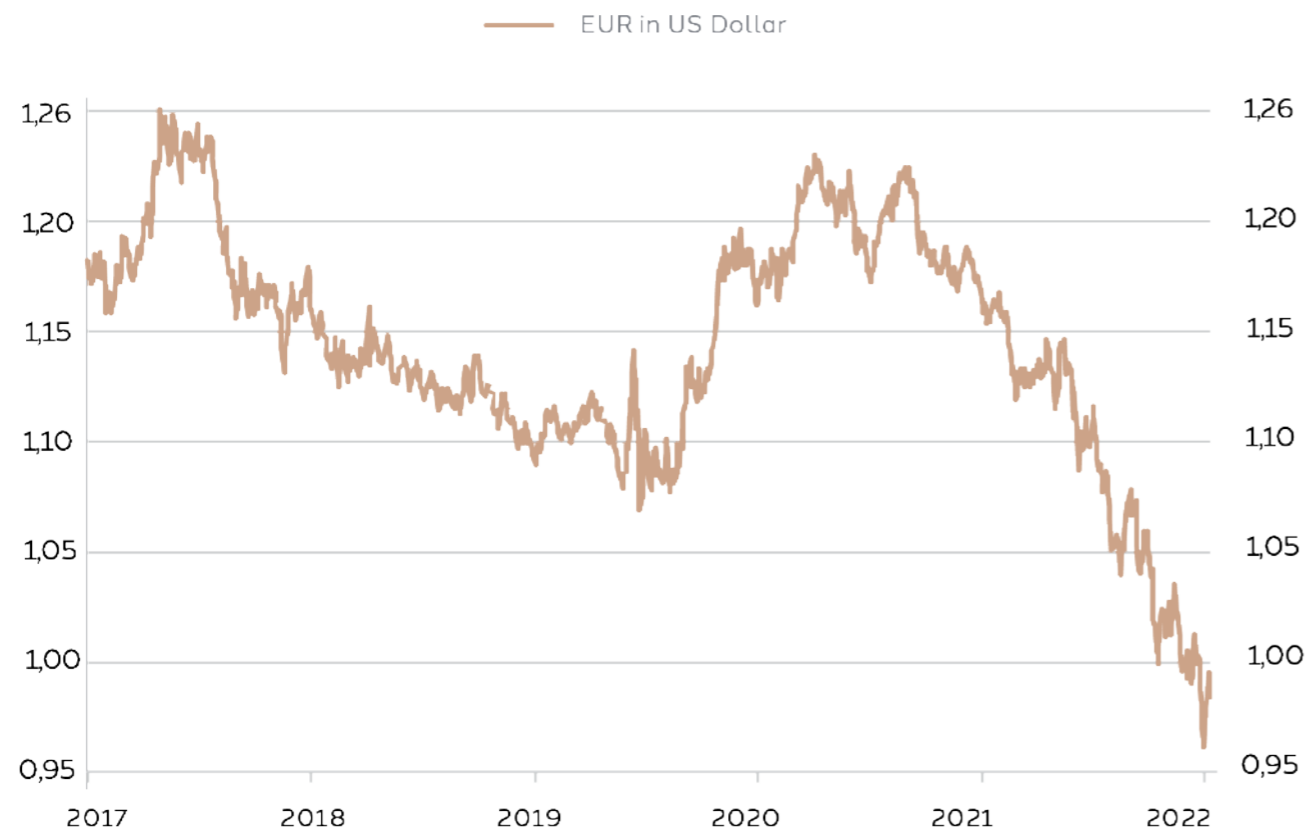
We do not expect any bigger jumps from the euro this year. While the ECB has only just begun its fight against inflation, other central banks such as the Fed are continuing to tighten their monetary policy with major interest rate hikes. However, we would not rule out the euro returning to parity. In the coming year do we see some recovery potential for the single currency.

### British pound experiences turbulence

The British pound experienced a somewhat rapid decline in recent weeks. This decline was particularly pronounced against

the US dollar. However, for a long time it was mainly the dollar's strength that was expressed. Only later was a unique pound weakness added, which was also evident in the EUR/GBP exchange rate pair: the euro rate rose at its peak from around 0.85 to almost 0.90 pounds per euro. However, after a bond market intervention by the Bank of England (BoE), the situation calmed down again somewhat. The intervention contradicted the central bank's original plans. It had actually wanted to withdraw more strongly from the market by selling its bond holdings. This was what the BoE had announced shortly before at its monetary policy meeting in September. But the rapid rise in interest rates has now resulted in exactly the opposite: The BoE

FIGURE 1: EUR/USD EXCHANGE RATE



SOURCE: MACROBOND

is buying up bonds for a limited period of time, thus providing relief in the bond market, where interest rates had risen rapidly.

Triggering the rise in interest rates, was an announcement by the British government to launch a series of measures that would further increase the national debt. This was not well received by markets. Announcing debt-busting tax cuts at a time of high inflation may be wrong. Nevertheless, the UK's fundamentals suggest that the country can still afford the additional borrowing. Despite a sharp rise in government debt over the past 20 years, the UK has the second-lowest debt-to-GDP ratio in the G7 and the longest average remaining bond maturity in the OECD. Nevertheless, the

road to postponing economic and political problems into the future through new government debt is becoming increasingly rocky.

Despite this turbulent phase, we see the pound continuing in the range of 0.85 pounds per euro in the medium term. Against the US dollar, the exchange rate depends in particular on how long the US dollar benefits from its safe-haven status. As long as the geopolitical situation and energy uncertainty in Europe remain elevated, the pound is likely to have little appreciation potential against the US dollar.

FIGURE 2: EUR/GBP EXCHANGE RATE



SOURCE: MACROBOND

### Swiss franc remains remarkably strong

The Swiss National Bank (SNB) has given the already strong franc an even greater tailwind with an unexpected interest rate hike in June. In addition, the SNB now no longer sees a strong franc as a burden on the economy, but as a welcome helper against further rising inflation rates: The stronger the currency, the cheaper goods can be imported from abroad.

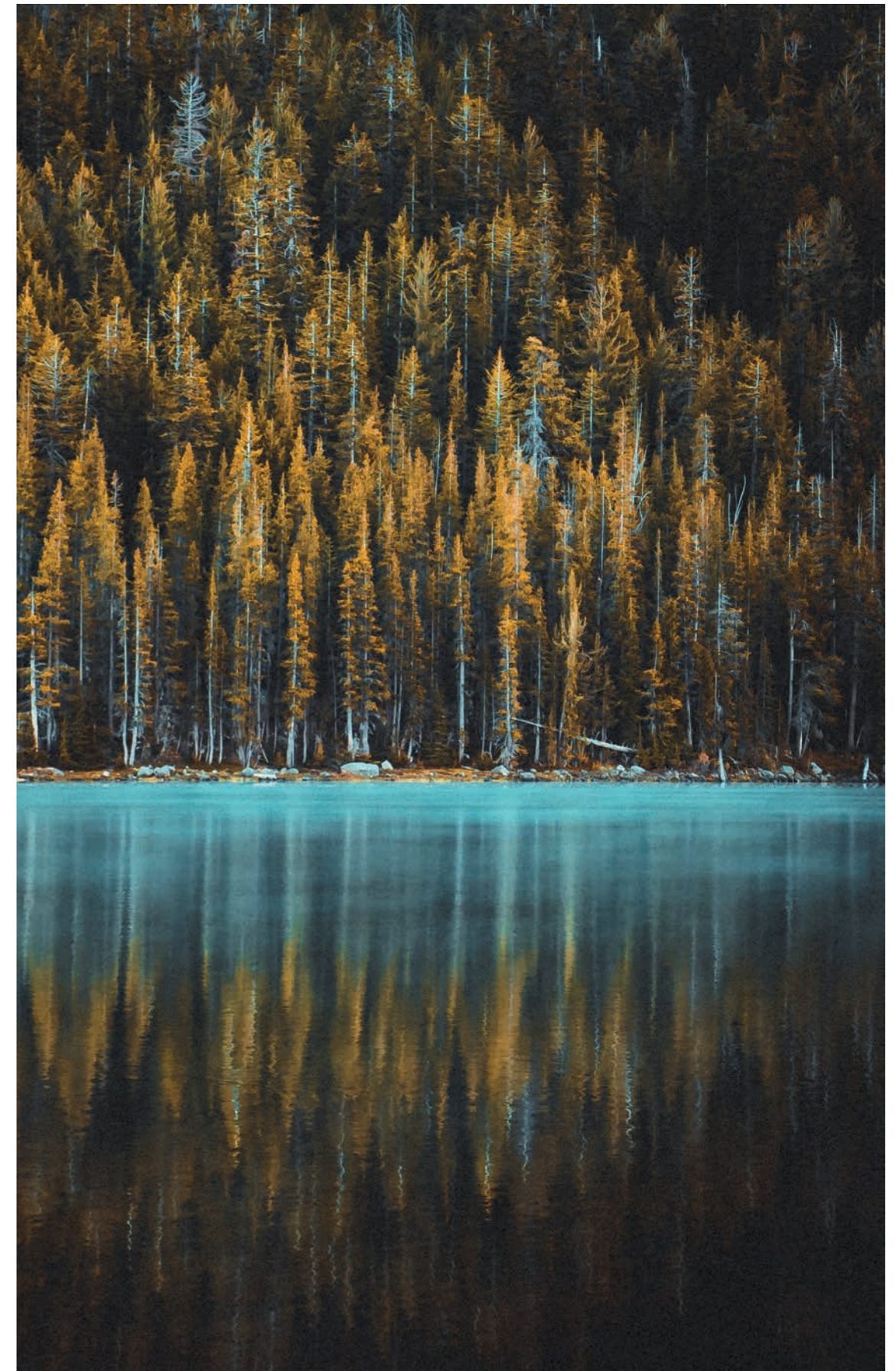
At just under 3.3% in September, the inflation rate is still at a moderate level. However, the share of administered prices in Switzerland is high at 28.7% (euro zone: 12.6%). It could therefore be that the state is artificially depressing the price level through its

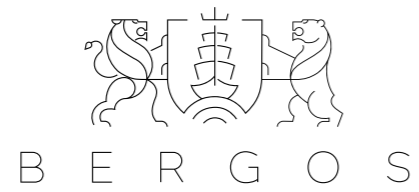
interventions. Regardless, the SNB raised interest rates by 75 basis points in September. The period of negative key interest rates is now over. In addition to monetary policy, the geopolitical situation is strengthening the Swiss franc, which is currently playing to its full potential as a safe haven.

FIGURE 3: EUR/CHF EXCHANGE RATE



SOURCE: MACROBOND





# C U R R E N C I E S O U R E X P E R T



**DR. JÖRN QUITZAU**  
CURRENCY STRATEGIST,  
BERENBERG

Dr. Jörn Quitzau has been with Berenberg since 2007, where he is Head of Economic Trends and responsible for currency analysis. Prior to that, he spent six years at Deutsche Bank Research in Frankfurt. Since 2014, he has been a Non-Resident Fellow at the American Institute for Contemporary Studies (AICGS), Washington D.C.



# BERGOS VIEW MATRIX

## BANK VIEW

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	--	-	0	+	++
<b>EQUITIES</b>	○	○	●	○	○
<b>NORTH AMERICA</b>	○	○	○	●	○
CONSUMER DISCRETIONARY	○	○	●	○	○
CONSUMER STAPLES	○	●	○	○	○
ENERGY	○	○	●	○	○
FINANCIALS	○	○	○	●	○
HEALTH CARE	○	○	○	●	○
INDUSTRIALS	○	○	●	○	○
INFORMATION TECHNOLOGY	○	○	●	○	○
MATERIALS	○	○	●	○	○
REAL ESTATE	○	○	●	○	○
COMMUNICATION SERVICES	○	○	●	○	○
UTILITIES	○	●	○	○	○
<b>EUROPE</b>	○	○	●	○	○
CONSUMER DISCRETIONARY	○	○	○	●	○
CONSUMER STAPLES	○	○	●	○	○
ENERGY	○	○	●	○	○
FINANCIALS	○	○	○	●	○
HEALTH CARE	○	○	●	○	○
INDUSTRIALS	○	○	●	○	○
INFORMATION TECHNOLOGY	○	○	●	○	○
MATERIALS	○	○	○	●	○
REAL ESTATE	○	●	○	○	○
COMMUNICATION SERVICES	○	●	○	○	○
UTILITIES	○	●	○	○	○
<b>JAPAN</b>	○	○	○	●	○
<b>EMERGING MARKETS</b>	○	●	○	○	○

## FIXED INCOME

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	--	-	0	+	++
<b>DENOMINATION U.S.DOLLAR</b>	○	○	●	○	○
DURATION	○	●	○	○	○
SOVEREIGNS	○	○	●	○	○
CORPORATES NON-FINANCIAL	○	○	●	○	○
CORPORATES FINANCIAL	○	○	○	●	○
SENIOR	○	○	●	○	○
SUBORDINATED DEBT	○	○	●	○	○
CORPORATE HIGH YIELD	○	○	●	○	○
<b>DENOMINATION EURO</b>	○	●	○	○	○
DURATION	○	●	○	○	○
SOVEREIGNS	○	●	○	○	○
CORE	○	○	●	○	○
PERIPHERAL	○	○	○	●	○
CORPORATES NON-FINANCIAL	○	○	●	○	○
CORPORATES FINANCIAL	○	○	○	●	○
SENIOR	○	○	●	○	○
SUBORDINATED DEBT	○	○	●	○	○
CORPORATE HIGH YIELD	○	○	●	○	○
<b>EMERGING MARKETS</b>	○	○	○	●	○

## ALTERNATIVE INVESTMENTS

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	--	-	0	+	++
<b>COMMODITIES</b>	○	○	○	●	○
ENERGY	○	○	●	○	○
INDUSTRIAL METALS	○	○	●	○	○
PRECIOUS METALS	○	○	●	○	○
<b>HEDGEFONDS STRATEGIES</b>	○	○	●	○	○
LONG / SHORT	○	○	●	○	○
RELATIVE VALUE	○	○	○	●	○
MACRO	○	○	●	○	○
EVENT DRIVEN	○	○	●	○	○
<b>CONVERTIBLES</b>	○	○	●	○	○
<b>ALTERNATIVE CREDIT AND PRIVATE DEBT</b>	○	○	○	●	○
<b>REAL ESTATE</b>	○	○	●	○	○

