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Bad news is good news

January 2020

- Recession fears disappeared
- Investors act boldly but not yet overconfident
- More defensive alignment of our portfolio structures
- Equities downgraded to neutral

Repo-Crisis leads to Fed balance sheet expansion

The flood of liquidity caused by central banks starting last October caused equities, bonds and precious metals to rise in parallel. Hence, markets have once again become strongly dependent on central bank actions. At the beginning of last year, fears of a recession prompted the FED to change its interest rate policy, while fear of the so-called repo crisis (liquidity shortage within the US banking system) has caused the FED to massively inflate the US central banks' balance sheet since October. In this context, many prominent market participants are talking about a relaunch of the "Quantitative Easing" program, which the FED has denied with rather technical arguments. Either way, both alleged bad news had positive effects on financial markets. In the course of this development, markets have become even more disconnected from their fundamentals. As a consequence, the absolute and relative valuation of equities has increased. In the case of fixed-income securities, the "uplift" is reflected by the fact that the yields on government bonds and risk premiums on high-yield corporate bonds have fallen in lockstep. It comes as no surprise that investors' risk appetite has also continued to rise at the same time. With the exception of derivatives (the "put/call ratio" dropped to historical lows), investors have so far acted boldly but not yet euphorically. Our risk index, a countercyclical indicator, has dropped into negative territory, however, without reaching an extreme value.

Sound Capital Investment Navigator

Valuation Bonds: --

	low		Yields		high
	- -	-	0	+	+ +
New	X				
Old	X				

	low		Spreads		high
	- -	-	0	+	+ +
New	X				
Old		X			

Valuation Equities: 0

	expensive		Shiller PE		cheap
	- -	-	0	+	+ +
New	X				
Old	X				

	low		Risk Premium		high
	- -	-	0	+	+ +
New					X
Old					X

	Contraction		Leading Indicators		Expansion
	- -	-	0	+	+ +
New				X	
Old				X	

	Euphoria		Risk-Index		Panic
	- -	-	0	+	+ +
New		X			
Old			X		

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In a nutshell, this leads to a less positive overall assessment in our navigator, which has the following impact on asset classes and asset categories:

Asset categories

Liquidity is upgraded to overweight from neutral, while bonds are reduced to heavily underweight. Equities are down-graded to neutral from slightly overweight, while alternative investments are upgraded to overweight from slightly overweight.

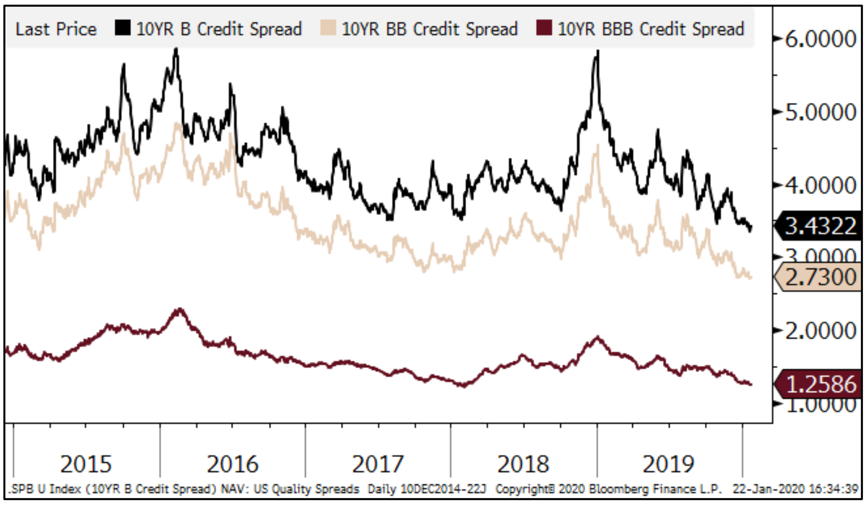
Asset classes:

Regional equity exposures are rebalanced to neutral, except emerging market equities which stay over-weight. High yield corporate bonds will be reduced to heavily underweight from neutral. Government bonds will be revalued to neutral. Investment grade corporate bonds & emerging market bonds are up-graded to positive from neutral.

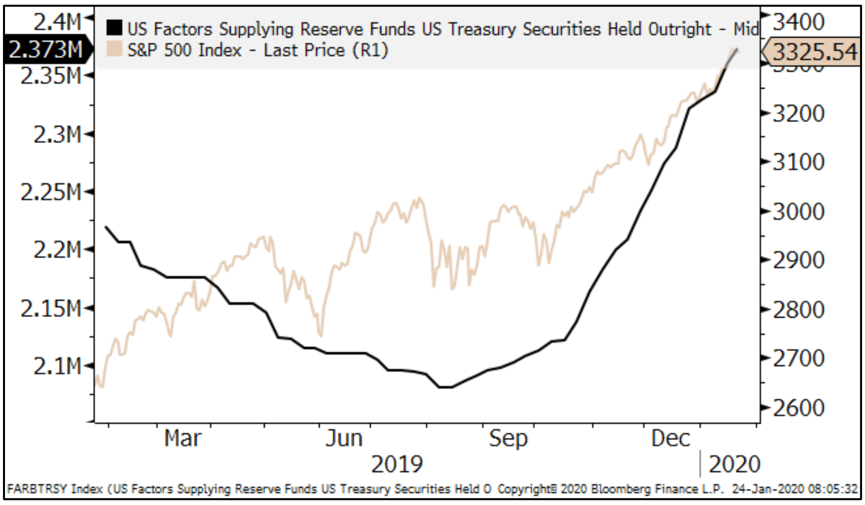
Interest rate level (indicator --) / Spreads (indicator --)

assessment unchanged / assessment decreased to -- from -

Since our last report, the interest rate on 10-year government bonds as well as spreads of high-yield corporate bonds have fallen simultaneously. Credit spreads are now close to historical lows.



Risk assets went up sharply since October in the wake of the Fed's balance sheet expansion.



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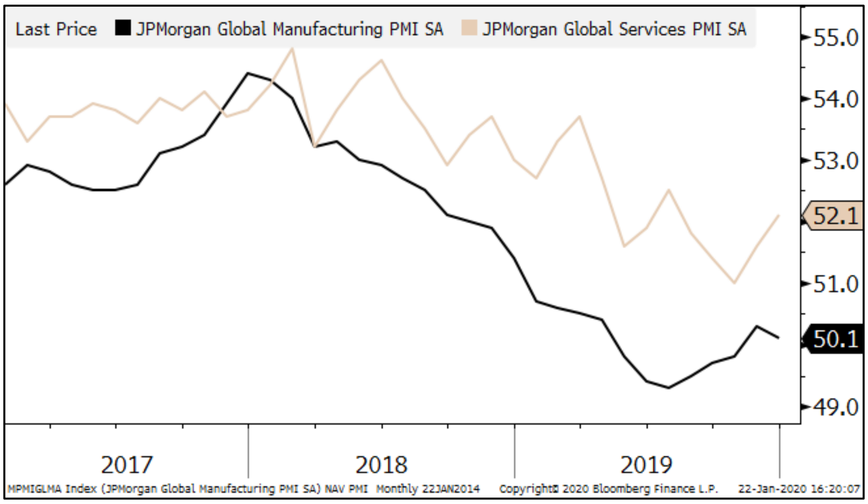
Shiller P/E ratio (indicator --) / Risk premium (indicator ++)
assessment unchanged / assessment unchanged

The absolute as well as the relative valuation of equities have increased further. On the other hand, the equity risk premium is still attractive.

Macro leading indicators (assessment of indicator +)
assessment unchanged

The global industrial and services sectors are both back in expansionary territory.



Risik index (indicator -)

Assessment reduced to – from 0

With the exception of derivatives (so-called put/call ratio already at historical lows), investors have so far been bold but not euphoric. Accordingly, our risk index, a countercyclical indicator, has dropped into negative territory, however, without reaching an extreme value.