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# Investors' Outlook

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May 2024

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# Traversing risky terrains

—
**Dan Scott**
Head of Vontobel Multi Asset,
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Dear readers,

April served as a reminder that geopolitical tensions could swiftly disrupt portfolios. Investors have woken up to geopolitical risks and the fact that while many ponder the job market, interest rates, and inflation, the dreaded proverbial Black Swan could come from outside the macroeconomic context.

Iran's first-ever attack on Israel marked further escalation in the Middle East, with investors apprehensive over the prospect of a broader conflict in the region that could draw in the US. All the while, the war in Ukraine grinds on, with Russia planning a late spring or summer offensive[1], and investors have had growing concerns over tensions between China and Taiwan. It's also a historical election year that is likely to be a divisive one in the US.

The CBOE[2] Volatility Index, known as VIX, has been inching higher this year reflecting a rather slow awakening to the abnormally high geopolitical tensions and fragmentation, oil prices creeping higher, as well as reemerging inflation fears. These worries carried over into a sell-off in global equities.

At the same time, the traditional 60/40 portfolio—long revered as a cornerstone of diversified investment strategies with its blend of 60 percent equities and 40 percent bonds—stands at a crossroads. The classic portfolio strategy took a historic hit in 2022, and it's worth asking what its future looks like and whether structural shifts in the markets mean that harvesting long-term growth while seeking protection from short-term volatility will require a rethink. How can we best shield ourselves from the drawdowns markets will likely face in the future? Are traditional fixed income allocations in need of review? For instance, might there be a good reason why spreads of investment-grade credit and high-yield bonds aren't wider? Perhaps they reflect not only the healthy state of companies' balance sheets but also the G-7 nations' bloated debt levels. We may well see 60/40 portfolios reducing government debt allocation as investors seek better sources of risk mitigation.

Considering we're in a period of record-high prices for everything, from cocoa to crypto and gold, seeking alternative assets to stay well-protected may seem like a challenge. Adding liquid alternative asset classes to portfolios, like catastrophe bonds, can serve as solid diversification and a buffer for various outcomes in geopolitical events or turbulent markets. Even commodities, which most would regard as highly cyclical and volatile, can deliver a good degree of inflation protection and provide a source of return without exposing investors to outsized risks. Since the beginning of 2022, the maximum drawdown in the Bloomberg Commodity Index of about 30 percent isn't far off that of 10-Year US Treasuries, which most people still see as a risk-free asset. What's clear is that the simple bonds and equities-only portfolio of our parents' generation won't be fit for the purpose of our children's generation.

In this Investors' Outlook, we dedicate extra space to an early analysis of the upcoming US presidential election, provide a closer look at what the escalation in the Middle East means for commodities, and detail our asset allocation.

**⟶ Webcast**
To view our webcast on recent market developments, click **here.**

[1] Source: Institute for the Study of War. understandingwar.org/backgrounder/russian-offensive-campaign-assessment-april-26-2024
[2] The CBOE Volatility Index (VIX) reflects the implied volatility of the S&P 500 Index. The VIX is calculated and published in real time by the Chicago Board Options Exchange.

—
**Frank Häusler**
Chief Investment Strategist,
Vontobel

# April showers

**Growing geopolitical tensions in the Middle East were among the most alarming "showers" of April, with investors closely monitoring the possibility of an escalation and its potential effects on the market. In the meantime, central banks and the timing of interest-rate cuts also remain primary considerations.**

Amid strong consumer spending and a resilient labor market, US economic data has continued to surprise to the upside. This translates into stickier-than-expected inflation, which is likely to make the latter stages of the US Federal Reserve's (Fed) inflation fight more difficult. It also means that the first interest-rate reductions will probably occur later than originally anticipated, as Fed Chair Jerome Powell indicated last month, saying that policymakers can keep rates steady for "as long as needed" should price pressures continue.

Nevertheless, investors are still eagerly awaiting the month of June. The Eurozone economy is showing signs of improvement, according to leading indicators: the bloc's manufacturing and services industries appear to be growing, inflation has slowed sharply, and industrial production in the region's biggest economy, Germany, rose more than expected. The European Central Bank (ECB) is now planting the seeds for a first interest-rate cut. ECB President Christine Lagarde said in a CNBC interview in mid-April that the central bank is "heading towards a moment" where it must moderate its restrictive monetary policy, barring any "major shock." Other ECB members echoed that tone.

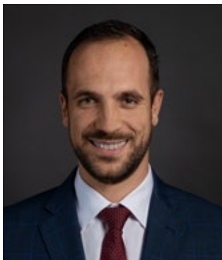
The Vontobel Investment Committee decided to downgrade fixed income to underweight from neutral and, in turn, upgrade commodities to neutral from underweight, in part due to potential tailwinds from geopolitical risks that may materialize. We continue to favor equities with an overall overweight stance. Find the details of our asset allocation on page 5.

| | UNDERWEIGHT significantly | UNDERWEIGHT slightly | NEUTRAL | OVERWEIGHT slightly | OVERWEIGHT significantly | |
|---|---|---|---|---|---|---|
| **1 Liquidity** | | → | | | | We stay underweight on cash; we believe that for a nine- to 12-month investment horizon, returns from asset classes should outpace those from cash. |
| **2 Bonds** | | ↘ | | | | We trim our exposure to investment-grade corporate bonds to underweight from neutral. This moves our view on the entire fixed income asset class to slightly underweight from neutral. Our improved macro-economic scenario of slightly higher growth tends to favor cyclical asset classes like equities and commodities at the expense of fixed income. In terms of sub-asset classes, we believe investment-grade corporate bonds' valuations are not particularly attractive and prefer getting rate exposure via government bonds, where we remain overweight, along with emerging-market debt in hard currencies. |
| **3 Equities** | | | | → | | We stick to our equity overweight. We think the Fed will cut rates later than originally expected, but by more than the markets are currently pricing in. We also believe that leading global economic indicators, such as purchasing managers' indices, could show further improvement in the coming months. At the same time, despite stronger-than-expected monthly inflation data, we don't see a big risk of a second wave of inflation. This should continue to support equities. On a sub-asset class level, we retain our overweight on US equities. We upgrade Eurozone equities to neutral from underweight at the expense of Swiss equities, which we downgrade to neutral from overweight. We think Eurozone equities offer more cyclical exposure in the current cycle than Swiss ones. We also believe the ECB has more room to ease monetary policy than the Swiss National Bank (SNB). We stay neutral on Japanese and emerging-market stocks. |
| **4 Gold** | | | | → | | We retain our slightly positive view on gold, one of the top-performing asset classes since the beginning of the year, with an almost 13 percent return in US dollar terms. Despite rising US real yields, continued US dollar strength, and hawkish Fed rhetoric, the yellow metal continues to chase one record high after another, partly due to its "safe haven" profile. There is solid demand from key markets, heightened geopolitical risks, like an escalation in the Middle East, and strong central bank demand, especially from emerging markets. |
| **5 Commodities** | | | ↗ | | | We lift commodities to neutral from underweight. Our decision is based on three convictions: first, we believe that a re-acceleration of the global economy could provide a little extra boost to this cyclical asset class. Second, we believe that markets underestimate the potential for Chinese stimulus. Third, we think the asset class might benefit from the tailwind from heightened geopolitical risks, considering a possible escalation in the Middle East conflict. |
| **6 Alternative strategies** | | | → | | | We maintain our neutral take on alternative funds and real estate. Within alternative funds, we like insurance-linked securities as they tend to have a low correlation with traditional financial markets considering their performance is linked to specific insurance events and can therefore help to reduce overall portfolio risk. |

Changes month-on-month: same → higher ↗ lower ↘

# US presidential election—what a second Trump term could mean for investors

**The US presidential election may still be a while away; the world's largest economy won't head to the polls until November 5, 2024. But a glance at the major financial news outlets and social media channels quickly reveals that the election campaign is already in full swing.**



—
**Stefan Eppenberger**
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—
**Michaela Huber**
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Incumbent Joe Biden and Donald Trump have recently engaged in verbal blows over which of them was better suited to the presidency. Trump, 77, has called Biden "grossly incompetent"[1], while Biden, 81, when asked about his advanced age, replied, "One candidate is too old and mentally unfit to be president… the other guy is me[2]."

Robert F. Kennedy Jr., son of assassinated Attorney General Robert Kennedy and scion of one of the most prominent political dynasties in the US, has not yet given up hope for one of the most influential jobs in the world.

Attempting to make a call on who will end up moving into the White House is about as helpful as flipping a coin, in our opinion. We don't think it makes a lot of sense to try to predict the election outcome by using probability calculations. However, thought experiments and asking "what if" questions can be helpful to investors.

In this article, we focus on Trump as opposed to Biden. This is not due to any political tendencies on our side or any conviction that Trump has better chances at winning. Rather, it reflects our belief that a second Trump term would have greater market implications than the re-election of Biden. A Biden re-election would, in our view, be more likely to result in a continuation of the status quo.

**Why we believe a second Trump term should seriously be taken into consideration**
Trump's first term in office (2017–2021) was eventful: from a trade war with China to the withdrawals from the Iran nuclear deal and the Paris climate agreement and threats to pull out of alliances such as the North Atlantic Treaty Organization (NATO) or the World Trade Organization (WTO), his presidency was also marked by numerous personnel changes, entry bans for certain population groups, the construction of the US-Mexico border wall, impeachment proceedings, stolen secret papers, election fraud allegations, and an armed storming of the Capitol. So, one might think that the hurdles for a second term

would be high. However, polls currently indicate a tight race. And the situation doesn't look too bad in the fiercely contested swing states either[3]. Moreover, Trump ended up doing better than polls suggested in the past[4].

**What speaks in favor of Trump?**
In our opinion, his lingering popularity has a lot to do with social developments and Trump's status as the "enfant terrible" of the establishment. Take, for example, the increasingly frustrated US middle class[5], which has felt left behind as globalization has lifted many formerly low-income people into the middle class and benefited developing countries like China in recent decades. In the 1990s, the middle class owned around 37 percent of private household wealth in the US. At the turn of the millennium, this figure fell to around 30 percent. Today, it's just under 26 percent, according to Fed data.

At the same time, trust in state institutions has been declining for years. According to a Gallup poll[6], trust in the Supreme Court was just under 60 percent in the 1980s. In 2023, it was only 27 percent. Only trust in newspapers (2023: 18 percent) or Congress (2023: 8 percent) looks worse.

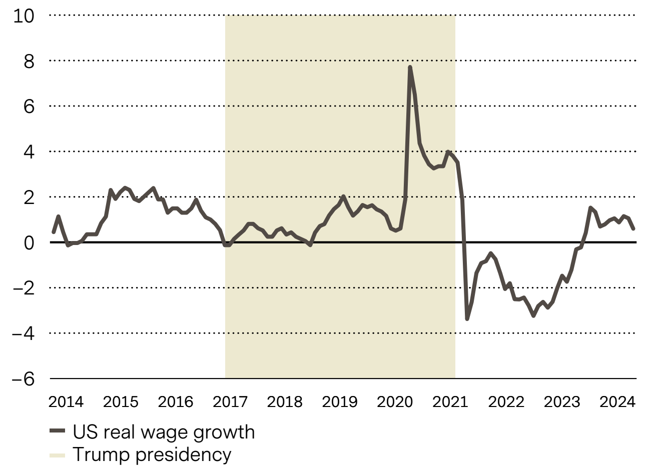
These long-simmering developments have worsened since Trump's departure. One important reason is likely to be the inflation shock, which pushed the real (i.e., inflation-adjusted) wage growth of many Americans into negative territory at the start of 2021 (see chart 1).

What also plays into Trump's hands is Biden's unpopularity. A president's approval rating is normally a good predictor of his chances of re-election. In the past, the public's opinion of the president depended primarily on their assessment of the economy. Recently, however, this relationship has been turned upside down: The US economy is strong, the unemployment rate remains at a historic low, and even inflation (the groundwork of which was laid before Biden took office) has declined significantly. And yet, Biden's approval rating has plummeted. While his approval rating stood at 53 percent at the beginning of 2021, it's now at around 40 percent, according to ABC News-owned website FiveThirtyEight[7]. This makes him even less popular than Trump was during his first term.

Many Americans don't trust Biden to tackle issues that are important to them, according to an Ipsos survey[8]. This applies in particular to social issues such as crime or immigration. The latter has increased significantly since 2022 (partly due to easing pandemic restrictions) and has intensified since. In December alone, federal agents encountered 10,000 people a day crossing the southern border of the US, according to Bloomberg News[9]. That's poised to be a breeding ground for populist slogans.

**Chart 1: Since Trump left, the average American can afford less**

Year-on-year percentage change




Source: LSEG, Vontobel; data as of April 16, 2024.

In addition, one of the Democrats' most reliable voting blocs appears to have shifted its opinion. According to an April New York Times / Siena poll[10], Trump's support among black voters has climbed to 16 percent. Hispanic voters are also warming to Trump. One possible explanation could be that these groups are disillusioned with Biden and are particularly affected by negative real incomes.

**What speaks in favor of Biden?**
The statistics are on Biden's side. Historically, the incumbent US president is re-elected 67 percent of the time. If the incumbent president manages to avoid a recession, that probability increases to 80 percent. However, if the economy slips into a recession, the president is penalized, and the rate drops to 44 percent (see chart 2, page 9). In view of the strong labor market, both in the US in general but also in swing states, it currently looks as if a recession could be avoided before the election.

**Don't lose sight of third-party candidates**
Trump and Biden currently dominate the headlines. However, investors should also keep in mind that potential third-party candidates could have an impact on the election. A poll conducted by Quinnipiac University[11] in March found that 20 percent of voters would choose a candidate other than Trump or Biden if they had a choice between

[1] Source: The Hill article, published September 14, 2023 thehill.com/homenews/campaign/4203873-trump-biden-not-too-old-to-be-president/
[2] Source: Reuters article, published March 17, 2024 www.reuters.com/world/us/biden-michigan-governor-whitmer-utahs-cox-joke-washingtons-gridiron-dinner-2024-03-16/
[3] "Swing states" are US states in which there is no clear preference for a candidate before the election. Populous swing states have often influenced the outcome of elections in the past. In 2024, Arizona, Nevada, Georgia, Michigan, Pennsylvania, and Wisconsin are considered swing states.
[4] Source: Pew Research Center article, published November 9, 2016. www.pewresearch.org/short-read/2016/11/09/why-2016-election-polls-missed-their-mark/
[5] We define "middle class" as all households between then 20th and 80th income percentile.
[6] Source: Gallup poll. news.gallup.com/poll/1597/confidence-institutions.aspx
[7] Source: FiveThirtyEight, as of April 29, 2024. projects.fivethirtyeight.com/biden-approval-rating/
[8] Source: ABC News article, published March 10, 2024. abcnews.go.com/Politics/biden-trump-americans-trust-president-poll/story?id=107938351
[9] Source: Bloomberg News article, published April 2, 2024 www.bloomberg.com/features/2024-election-texas-border-migration/
[10] Source: The New York Times, published April 13, 2024. www.nytimes.com/interactive/2024/04/14/us/elections/times-siena-poll-registered-voter-crosstabs.html
[11] Poll published March 27, 2024. poll.qu.edu/poll-release?releaseid=3894

five candidates instead of two. The independent candidate, Robert F. Kennedy Jr., accounted for 13 percent. However, the Green Party candidate, Jill Stein, was also able to win 4 percent.

The Greens have already thrown a spanner in the works for the Democrats in the past. Just think of 2000, when activist Ralph Nader prevented Al Gore from entering the White House, or 2016, when Jill Stein stole votes from Hillary Clinton.

**Who will win Congress?**
Another important question is who will win Congress. In our view, two scenarios have the highest probability: either a "red wave" (significant gains for the Republicans) or a stalemate. We think a "blue wave" (significant gains for the Democrats) is less likely.

Why? Congress is divided into the Senate and the House of Representatives. In the Senate, 28 Democratic seats are up for re-election this year; 23 Democratic seats are not up for election and are therefore considered to be "safe". The situation is different for the Republicans: only 11 seats are up for re-election, and 38 are considered to be "safe". According to political website 270toWin's polls[12], the Republicans are currently ahead. It is therefore quite possible that the Republicans will gain seats and increase their influence in the Senate. Who will be in charge in the House of Representatives will probably depend on the outcome of the election.

In our view, Trump would be less restricted than Biden in the event of an election victory. While Biden would (probably) face a blockade in the event of a victory, Trump could (probably) work with a majority in Congress.

**What is unlikely to change under either president**
Regardless of who moves into the White House, in our view, protectionism, anti-China policies, rearmament, and high national debt are likely to continue.

**1. Protectionism**
Anyone hoping for a little less "America first" and a little more trade openness from Joe Biden has been proven wrong in recent years. Biden is said to be pursuing a policy of "polite protectionism": he posts fewer angry tweets than his predecessor, but still has America's interests firmly in mind. Many of Trump's national security tariffs or voluntary restrictions that were negotiated with other countries remained intact under Biden. Biden appears to share Trump's view that protecting the US steel industry is a matter of national security. Other measures can also be seen as protectionist. One example is the Chips and Science Act promoted by Biden, which provides billions in investment in semiconductor manufacturing, research, and development and is intended to create more domestic jobs in the manufacturing industry.

**2. Anti-China policy**
The attitude towards the world's second-largest economy is also unlikely to change much. Both Republicans and Democrats have learned over the years that an anti-China policy increases voter favorability.

While Trump is openly hostile to China (like his various punitive tariffs imposed by Trump or Trump's statement that Covid-19 is a "Chinese virus"[13]), Biden's approach is more subtle but no less determined.

This becomes clear, for example, if we take a look at the Chinese companies that have been placed on the "entity list" by the US in recent years (see chart 3, page 9)[14].

**3. Rearmament**
Another point is the trend towards military rearmament. Trump has repeatedly called for higher military spending[15] and has also demanded this from other NATO member states[16]. In February, he even announced that he would not stand by NATO allies in an emergency.

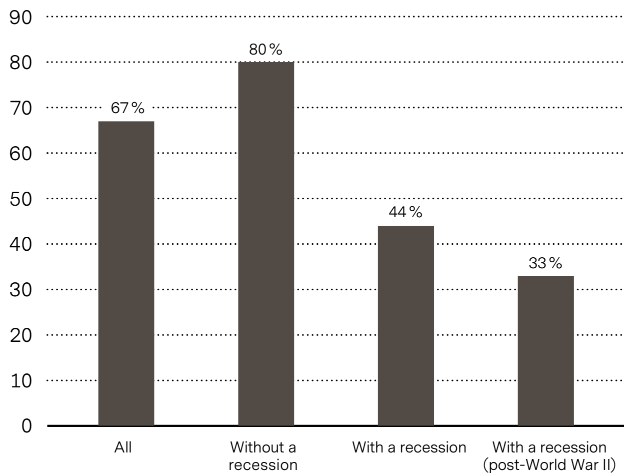
Biden also advocates for increased spending—he submitted a budget proposal in March 2024 for fiscal year 2025 that includes a request for USD 850 billion in discretionary funding for the Department of Defense (+4.1 percent over fiscal year 2023).

**4. Debt issue**
The debt issue (and associated questions around the "sustainability" of debt) is also likely to persist. At first glance, ever-increasing government debt is nothing new. Government debt, measured as a percentage of gross domestic product (GDP), has only been heading in one direction for years: upwards. In the 1980s, the national debt was still around 30 percent; now it is over 120 percent. What could soon become a problem, however, is the higher cost of servicing the debt (due to higher interest rates). These are higher than they have been for 40 years.

[12] 270toWin polls, as of April 17, 2024. www.270towin.com/2024-senate-election/
[13] Source: University of California San Francisco article, published March 18, 2021. www.ucsf.edu/news/2021/03/420081/trumps-chinese-virus-tweet-linked-rise-anti-asian-hashtags-twitter
[14] The "entity list" is a list compiled by the US government of foreign individuals, companies, and organizations that are classified as a national security risk and are subject to export restrictions and licensing requirements for the export of certain technologies and goods.
[15] Source: New York Times article, published February 27, 2017. www.nytimes.com/2017/02/27/us/politics/trump-budget-military.html
[16] Source: Reuters article, published July 11, 2018. www.reuters.com/article/idUSKBN1K12BW/

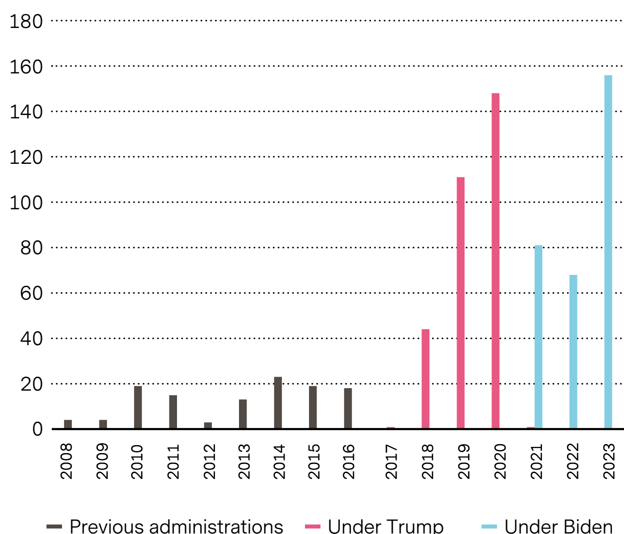
**Trump's campaign promises**
Summarizing all of Trump's campaign promises is quite ambitious. We will therefore limit ourselves to the five most important areas: Fiscal policy, monetary policy, trade policy, immigration policy, foreign policy.

**Chart 2: History shows election odds favor the incumbent president when there is no recession**
Incumbent president win rate in US elections in %




Source: BCA Research, NBER, Dave Leip's Atlas, Vontobel; data as of April 16, 2024.

**Chart 3: Democrats and Republicans agree on a hawkish China policy, primarily by inhibiting innovation**
Number of Chinese entities added to entity list under past US administrations




Source: Department of Commerce, Bloomberg, Vontobel; data as of April 16, 2024.

**1. Fiscal policy**
Trump's fiscal policy agenda is primarily aimed at lowering taxes. During his first term in office, he had already attempted to reduce corporate tax from 35 percent to 15 percent. In the end, it was at 21 percent. Trump and his advisers have discussed further cuts to corporate tax rates, potentially as low as 15 percent, according to a September article by the Washington Post[17]. Private individuals could also hope for lower taxes under Trump. In the past, lower taxes have weakened budgetary discipline in the US. It can be assumed that the already high budget deficit will continue to grow.

Trump wants to make savings elsewhere and, among other things, discontinue state funding for public broadcasting. Foreign aid, climate subsidies, and investments in sustainable technologies are also to be cut back (Trump sees the expansion of electric cars, for example, as paving the way for mass redundancies in the US car industry)[18].

**2. Monetary policy**
Trump has primarily zeroed in on Fed Chair Jerome Powell. Trump and Powell share a turbulent history. Trump appointed Powell (who is also a Republican) as Fed Chair in 2017 and praised him at the time as "wise" and experienced. But when Powell raised interest rates in 2018, he fell out of favor. Trump described Powell and the Fed as "clueless"[19] and called for Powell's dismissal. In 2019, Trump even tweeted the question of "who is our bigger enemy" Powell or China's President Xi Jinping[20]. In 2024, Trump hinted that Powell would lower interest rates to help the Democrats and secure Biden's second term in office[21].

In our view, Powell's dismissal is likely to be difficult. Legally speaking, the President can only remove a Fed Board member (including Powell) for "cause". Dissatisfaction with the Fed's monetary policy is unlikely to be a valid point.

However, Trump has already announced that if he were to be elected President, he wouldn't give Powell a second term in office (Powell's four-year term expires in 2026). After that, he could try to appoint a Fed chair he prefers, though Congress would have to give its approval.

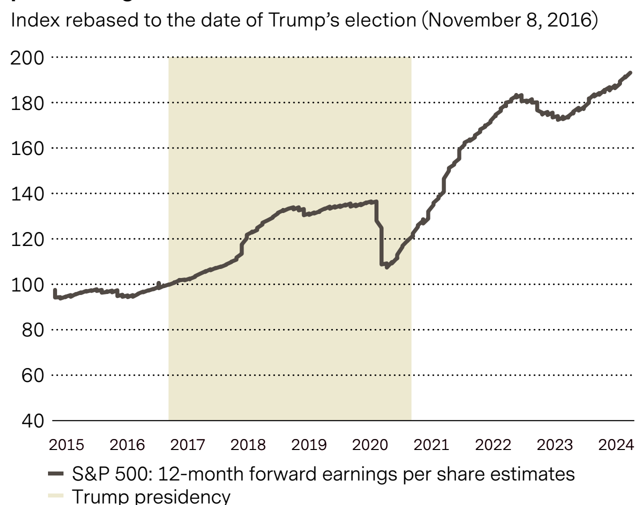
**3. Trade policy**
Trump continues to strive for an "America first" policy. In the event of a second Trump term in office, greater trade policy uncertainty can therefore be expected.

He has already announced that he would impose import tariffs of 60 percent on goods from China and 10 percent on goods from other countries if he wins the election. The current average tariff rate is 3 percent, or 19 percent in the case of China, according to the South China Morning

[17] Source: Washington Post article , published September 13, 2023. www.washingtonpost.com/business/2023/09/11/trump-tax-cuts-2024/
[18] Source: Time article, published September 28, 2024. time.com/6318298/why-trump-talking-about-electric-vehicles/
[19] Source: CNBC article, published August 14, 2019. www.cnbc.com/2019/08/14/trump-hammers-clueless-jay-powell-rails-against-crazy-inverted-yield-curve.html
[20] Source: CNBC article, published August 23, 2019. www.cnbc.com/2019/08/23/trump-tweets-who-is-our-bigger-enemy-fed-chairman-powell-or-chinese-president-xi.html
[21] Source: Fortune article, published February 2, 2024. fortune.com/2024/02/02/donald-trump-says-political-jerome-powell-will-help-democrats-lower-interest-rates/

**Chart 4: Another tax cut would likely boost earnings per share growth**

Index rebased to the date of Trump's election (November 8, 2016)




Source: LSEG, Vontobel; data as of April 16, 2024.

Post[22]. If Trump were to push this through, the European Union—as the US's second-largest trading partner—would be particularly affected, alongside China.

Restricting Chinese ownership of US infrastructure (e.g., in the areas of energy, technology, telecommunications, and natural resources) is also under discussion. Trump is also considering a ban on investments by US companies in China and a rethink of the US's role in important organizations such as the WTO.

**4. Immigration policy**

Trump's plans for immigration sound similarly determined. At a recent fundraiser, Trump complained that no people from "nice" countries (Trump's definition: Denmark, Switzerland, and Norway)[23] were immigrating to the US. Instead, he said, we have to contend with people from other countries. But legal immigration and the right to citizenship for babies born in America should also be put to the test.

Although stricter immigration policy would be welcomed by populist voters, it could have negative consequences for the labor market.

Strong immigration under Biden has had a relaxing effect on the tight labor market. The latter has been struggling for some time with too high a demand for labor and too low a supply of labor. Lower immigration would exacerbate the shortage of labor and further fuel wage pressure (and thus inflation).

**5. Foreign policy**

Apart from China policy, relations with Russia are also likely to be one to watch. Trump appears to have a good relationship with Russian President Vladimir Putin. While Trump's statement that he would settle the Ukraine war within 24 hours[24] may be a bit ambitious, one way he could influence the war would be by cutting off financial aid to Ukraine, which is what Hungarian Prime Minister Viktor Orban claims Trump told him in a meeting in March[25]. That would, however, require convincing a Russia-sceptic Congress.

A "forced" settlement of the war would not necessarily be market-relevant in our view: while oil prices rose significantly after Russia's invasion, they have fallen since the end of 2022, i.e., the "geopolitical risk premium" of the Russia-Ukraine war is no longer really present. Instead, other conflicts (Israel-Hamas) are driving the oil price.

Trump's Iran policy could have more of an impact on the oil price. For Trump, sanctions seem to be the only way to prevent Iran from enriching uranium (and thus from making a nuclear bomb) in the future. Iran is one of the largest oil producers in the world and ranked 7th in 2016 with a production of 4.4 million barrels per day. After Trump's surprising withdrawal from the Joint Comprehensive Plan of Action (JCPOA) nuclear deal in May 2018, the price of oil rose by 60 percent within a short period of time. According to estimates, 2 to 4 million barrels of oil disappeared (at least temporarily) from the world market.

In the rest of the Middle East, Trump impressed with his diplomatic skills. The Abraham Accords (2020), brokered by his administration, normalized diplomatic relations between Israel and some Arab states. The signatories—the United Arab Emirates (UAE), Bahrain, and Israel—reaffirmed their desire to strengthen peace in the Middle East. The UAE and Israel also concluded a peace agreement. Trump also maintains good relations with Saudi Arabia and the important gas exporter Qatar.

[22] Source: South China Morning Post article, published January 17, 2024. www.scmp.com/news/china/diplomacy/article/3248691/us-tariffs-chinese-imports-might-increase-2024-analysts-say
[23] Source: The Guardian article, published April 8, 2024. www.theguardian.com/us-news/2024/apr/08/trump-immigration-north-europe
[24] Source: Wall Street Journal video, courtesy of CNN, published May 11, 2023. www.wsj.com/video/watch-trump-says-as-president-hed-settle-ukraine-war-within-24-hours/0B-CA9F18-D3BF-43DA-9220-C13587EAEDF2
[25] Source: Reuters article, published March 11, 2024. www.reuters.com/world/europe/trump-wont-give-money-ukraine-if-elected-says-hungarys-orban-2024-03-11/

**What Trump 2.0 could mean for the economy**
It is not easy to say how a second Trump term would affect key macroeconomic variables.

Firstly, it is not clear whether Trump can win a majority in Congress. Secondly, it is not certain whether the Republicans will go along with all his proposals. This will influence whether (and how) his campaign promises are implemented. Thirdly, the current situation is different: many of Trump's campaign promises would be met with a much tighter labor market today. In other words, the upside risks for inflation are higher than they were during Trump's first term in office. But we believe the following might be a possible scenario:

**1. Growth**
A second Trump term might be broadly positive for economic growth. The tax cuts planned by Trump should lead to a higher fiscal deficit. This would result in a positive fiscal stimulus. Trump's deregulation plans could also lead to higher productivity. As long as Congress goes along with Trump, this should support the US economy.

In the longer term, however, there would also be negative implications for growth. Lower immigration would probably lead to weaker population growth. Due to increased trade uncertainty, there is also a risk that companies will invest less. Higher tariffs and the associated higher prices could also lead to lower consumption.

**2. Inflation**
A second Trump term is likely to be largely reflationary, i.e., the price level in the US is more likely to rebound amid a stronger economy and private consumption. This is partly due to the presumably higher fiscal deficit and the associated positive demand stimulus, and partly due to lower immigration and the associated risk of an additional shortage on the labor market (higher wage pressure due to lower labor supply). Last but not least, higher tariffs are also likely to be reflected in higher inflation.

A small disinflationary effect could come from lower immigration (fewer immigrants, less demand for housing, and thus less pressure on house and rent inflation).

**3. Interest rates**
Between 2017 and 2018 (i.e., during Trump's first term in office, when he had full control of Congress), interest rates (in this case, bond yields) rose. Even if Trump wins another election, interest rates are likely to rise due to higher economic growth, higher inflation, and the prospect of a Republican-controlled Congress. However, trade uncertainty and foreign policy geared towards maximum pressure could somewhat limit the upside potential.

**4. US dollar**
In our view, the combination of stronger economic growth, higher inflation, and trade uncertainty harbors upside risks for the US dollar. However, the Fed's reaction function is crucial here. The prerequisite for a stronger dollar is that the central bank takes decisive action against higher inflation (i.e., raises interest rates). If it does not do this and stands idly by and watches inflation rise, this is more likely to weigh on the dollar.

**What Trump 2.0 would mean for financial markets**
It's important to remember that asset classes are also influenced by other factors, such as the global economic cycle, which in turn is influenced by far more than just the outcome of the election.

**1. Equities**
If history is any guide, equity markets often trend sideways in the run-up to elections. This is hardly surprising: election campaigns are typically accompanied by uncertainty about the future political course, and stock investors don't like uncertainty. Once a winner was determined, the markets usually went up—even if the incumbent president was not re-elected.

A further tax cut would probably have a positive impact on earnings per share (see chart 4, page 10). At the same time, investors should be prepared for higher equity market volatility (similar to 2019), due to the more unpredictable policy.

Within the asset class, developed-market equities are poised to benefit the most. There could be headwinds for some emerging-market stocks due to the trade war.

**2. Bonds**
Bonds are likely to struggle more in the event of a second Trump term. While the asset class would benefit from a stronger US dollar, the combination of higher growth, higher inflation, and higher interest rates would have a negative impact.

A stronger economy makes equities look more attractive than bonds from an investor's perspective. Higher inflation reduces the purchasing power of a bond's future cash flows. Rising interest rates cause existing bonds to lose value.

**3. Alternative investments**
If our assumption of a reflationary second Trump term is confirmed, commodities could also benefit. Higher economic growth should also benefit the cyclical asset class. While gold could benefit temporarily from increased geopolitical uncertainty, higher interest rates and a stronger US dollar are likely to weigh on the precious metal (real interest rates and the US dollar generally move in the opposite direction to gold).

Please see disclaimer for this article on page 18.

# Shifting economic currents and the elusive ‘year of the bond’

—
**Christopher Koslowski**
Senior Fixed Income & FX Strategist, Vontobel

**Investors initially expected 2024 to be a year marked by slumping growth, decreasing inflation, and early, significant rate cuts. It’s evolving, however, into a year characterized by seemingly steady growth, persistent inflationary pressure, and a more gradual approach to policy normalization that will begin later than anticipated. Thus far, the "year of the bond" appears to remain elusive … at least for now,**

Large parts of the US economy continue to show signs of stability, even amid aggressive monetary policy tightening. The absence of an immediate recession has led the market to anticipate stickier inflation. We were skeptical that inflation would decrease as quickly as the market had anticipated not too long ago, maintaining that the last mile would be the hardest. A lot depends on the data from the coming months, including when the first rate cut will occur and how many cuts will be made this year. Most Fed officials anticipate two or three rate cuts this year. However, a prolonged delay in inflation improvement, inflation expectations spiraling out of control, or an unexpected decline in the labor market could significantly alter the situation.

The big change in market pricing is the magnitude of rate cuts. In early 2024, the market priced in a 10 percent probability of a federal funds rate of 2 percent or less by year-end. Since then, the market has reduced those odds. The market seems to be pricing in benign economic outcomes. Currently, options are pricing a 30 percent likelihood that the year-end federal funds rate will be between 4 percent and 5 percent, with a greater likelihood that it will exceed 5 percent (see chart 1).

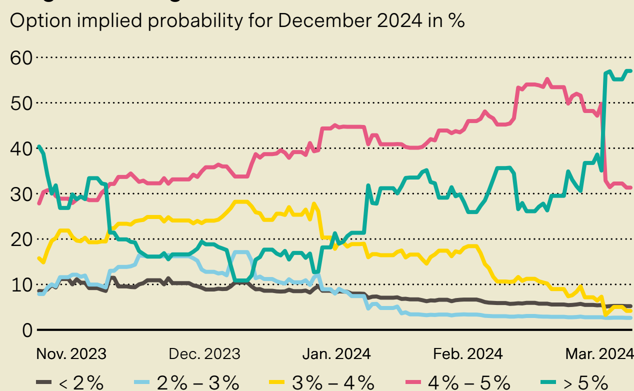
**Credit caution**

Option-adjusted spreads to US Treasuries, which reflect the difference in yield between sovereign and corporate bonds, are a common gauge of default risk. The sharp tightening in investment-grade credit spreads has considerably reduced the margin for safety in credit. Spreads now represent less than 20 percent of the total yield of the Bloomberg US Corporate Bond Index (see chart 2).

This “price to perfection” encourages us to be more vigilant in this segment. High-yield risk premia ticked up to 329 basis points after dropping below 300 basis points over the past month, the tightest level in about three years. High-yield bonds could come under pressure in this very uncertain environment. Expectations of higher default rates, paired with fairly restrictive monetary policy, are expected to weigh on this segment, prompting us to be mindful of the asymmetric risk-reward relationship. The current valuation of US high-yield spreads implies only very modest default rates and the absence of a near-term slowdown.

**Chart 1: Markets assign an increased probability to “higher for longer” Fed funds**

Option implied probability for December 2024 in %




Source: Bloomberg, Vontobel; data as of April 16, 2024.

**Chart 2: Sharp tightening in investment grade credit spreads**

In %

Source: Bloomberg, Vontobel; data as of April 16, 2024.

# Can earnings keep stocks rolling?

—
**Mario Montagnani**
Senior Investment Strategist,
Vontobel

**After almost five consecutive months of stellar performance, equity markets have been in a broad-based consolidation phase since the end of March. Stock investors are beleaguered with questions. Can the current earnings season keep stocks rolling? Can economic growth withstand higher yields and defy the Fed's extending its "higher for longer, no urgency to cut rates" mantra as it's still dissatisfied with the progress made in taming inflation?**

Since October, valuation re-rating has been the biggest driver behind stock markets' performance, reflecting an anticipation for good news, ranging from less restrictive monetary policy to the prospect of a soft landing.

The result? In the US, the S&P 500 Index closed above its 50-day moving average (the average closing price over the last 50 trading days) for more than 160 consecutive days, the longest streak since the global financial crisis. This phenomenon occurred only on rare occasions since 1945. But three consecutive hotter-than-expected monthly prints for US consumer price inflation, stronger-than-anticipated US consumer spending data, and rising tensions in Eastern Europe and the Middle East, which caused energy prices to spike, were enough to rekindle inflation fears.

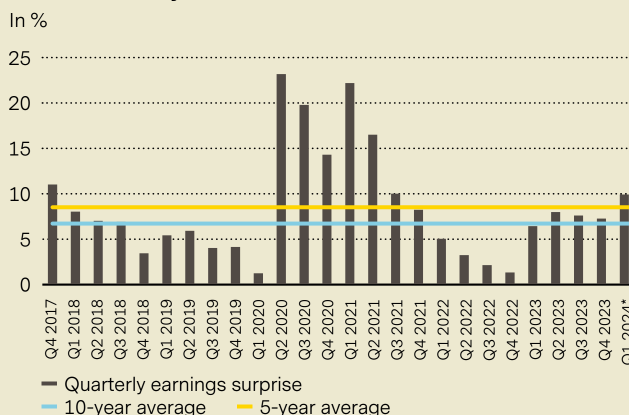
The Fed's "higher for longer" narrative and hawkish stance drove up yields and recalibrated market expectations that rate cuts were just around the corner. Markets were pricing in up to seven rate cuts this year at the start of the year, beginning as early as March. At the time of this writing, expectations have shifted to less than two, starting in the third quarter at the earliest.

Are we back to the same central-bank plot as last summer, and is this the beginning of a stronger correction? We don't think so. First, given the backdrop of higher inflation and the pushback on a pivot, coupled with extremely bullish investor sentiment at the end of March, a consolidation is certainly not surprising. Statistically, we have observed three to four pullbacks, on average, of about 5 percent or more per year since 1920. Second, for central banks, the major difference from last year is that the heavy lifting has been done as economic growth is recovering globally. This suggests we are nearing the beginning of a new economic cycle. If so, the reporting season that recently kicked off could show a continuation of earnings surprises seen in the last quarters (see chart 1), which in turn would be supportive of equities.

Backing up this view is that global earnings revisions, albeit in negative territory, seem to have bottomed and are trending up (see chart 2). This prompts us to retain an overweight stance on equities. More on this on page 5.

**Chart 1: Quarterly earnings surprises for the S&P 500 over the last 8 years**

In %




*Reporting season in progress. An earnings surprise is a difference between the reported earnings and the expected earnings of a company.

Source: Bloomberg, Vontobel; data as of April 19, 2024.

**Chart 2: Global earnings revisions remain in negative territory, though they seem to have bottomed out**

Earnings revisions* in %

* Values above 1 represent the majority of companies in the MSCI AWCI that had upward earnings revisions; values below 1 represent downward revisions.

Source: LSEG, Vontobel; data as of April 19, 2024.

# Crude climbs, gold glitters

—
**Michaela Huber**
Cross-Asset Strategist,
Vontobel

**The Israel-Hamas conflict has dominated the headlines since October 2023. At the time, we outlined three possible scenarios: a scenario in which the conflict remains limited to Israel and Hamas, a scenario in which Hezbollah becomes involved, and a scenario in which the "shadow war" fought between Israel and Iran escalates into a more direct conflict. The third scenario became reality in mid-April, when Iran sent drones and missiles towards Israel in response to an Israeli attack on its consulate in Syria earlier that month (for which Israel has not taken official responsibility).**

The attack marked a new, serious phase in the conflict and temporarily pushed oil above 90 US dollars per barrel (see chart 1). Going forward, a lot depends on how the conflict develops. If there is no further escalation, the focus will sooner or later return to the most important drivers (supply, demand, etc.). However, the potentially higher geopolitical attention of the markets in general could remain. In the event of a further escalation, higher oil prices (even an oil price shock) could be expected. Should a shock occur, the Organization of the Petroleum Exporting Organization of the Petroleum Exporting Countries and its allies (OPEC+) could rush to the rescue, as they have around 5 million barrels per day of spare production capacity.

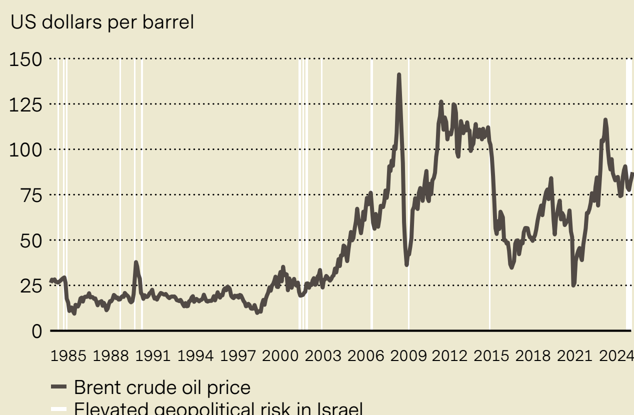
As we go to press, many stakeholders are trying to de-escalate the situation. While US President Joe Biden assured Israel's Prime Minister Benjamin Netanyahu of his support, he also warned against retaliation by Israel. In the event of an Israeli retaliatory strike, the US would more than likely not participate[1]. The Saudi Foreign Ministry also expressed great concern about the military escalation in the region and called on all parties involved to exercise the utmost restraint[2].

Gold's latest surge can't be explained by geopolitics alone. The yellow metal chased one high after the next despite rising US real yields and US dollar strength (usually headwinds for gold). An often-used explanation is strong central bank demand in emerging markets (China and India added gold at a healthy clip).

There may be another, lesser-heard explanation, which is that the market knows something we don't. What do we mean by that? When you look at the recent performance of gold and Bitcoin, you can't help but notice that they are "joined at the hip", i.e., a 1 percent move in gold equates to a roughly 5 percent move in Bitcoin. This is surprising, as both are usually seen as "competitors". One could argue that markets are increasingly concerned about the huge amount of liquidity in the system (see chart 2), and flock to alternative stores of value.

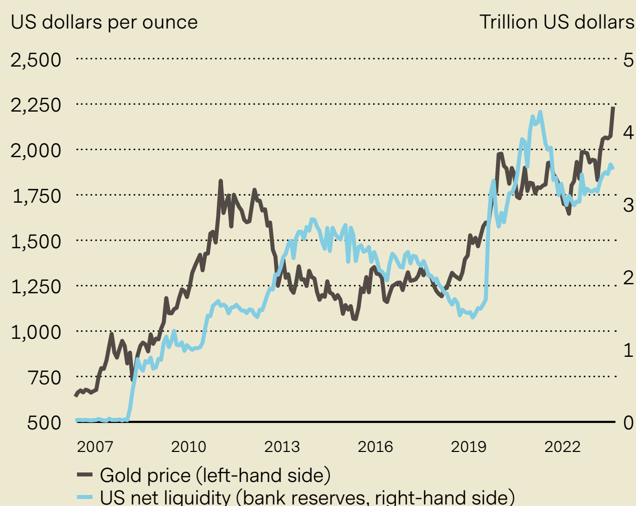
[1] Source: CNN article, published April 14, 2024. edition.cnn.com/2024/04/14/politics/biden-netanyahu-israel-iran-response/index.html
[2] Source: Al Arabiya article, published April 14, 2024. english.alarabiya.net/News/saudi-arabia/2024/04/14/saudi-arabia-expresses-deep-concern-over-military-escalations-in-the-region-

**Chart 1: The situation in the Middle East drives oil prices**




Note: The geopolitical risk index is based on the working paper "Measuring Geopolitical Risk" (Caldara, Dario and Matteo Iacoviello), Board of Governors of the Federal Reserve Board, 2017. White shaded areas mark periods when Israel's geopolitical risk index was greater than one.
Source: LSEG, Vontobel; data as of April 19, 2024.

**Chart 2: Is gold profiting from a (secret) liquidity boost?**




Source: LSEG, Vontobel; data as of April 19, 2024.

# US dollar riding high on rate-cut reversals

—
**Christopher Koslowski**
Senior Fixed Income & FX Strategist,
Vontobel

**US dollar bears have experienced a frustrating start to 2024. So far this year, the US Dollar Index has climbed about 5 percent (see chart 1), buoyed by market expectations that have shifted from anticipating up to seven rate cuts for 2024 by the Fed to fewer than two. A fresh bout of risk aversion is also filtering through markets, compounding the US dollar's advance.**

Given its currently high level, the potential for further gains by the US dollar is likely limited. Should upcoming data and communications suggest that the Fed will only delay its initial rate cut by a few months, yet still implement several rate reductions this year and next dollar bears might soon take the upper hand again.

However, if indications from the Fed suggest that rate cuts may not happen this year, or further tightening is still required, it would likely mean the recent dollar rally will continue. These developments would underscore the dollar's strengthening trend in response to the Fed's monetary policy signals.

**Short-lived geopolitical boost to the Swiss franc**
Although a fresh wave of geopolitical tensions provided some support to the Swiss franc, the underlying fundamentals remain unchanged: the Swiss National Bank (SNB) is confronted with significant dovish risk, indicating potential further downside for the franc.

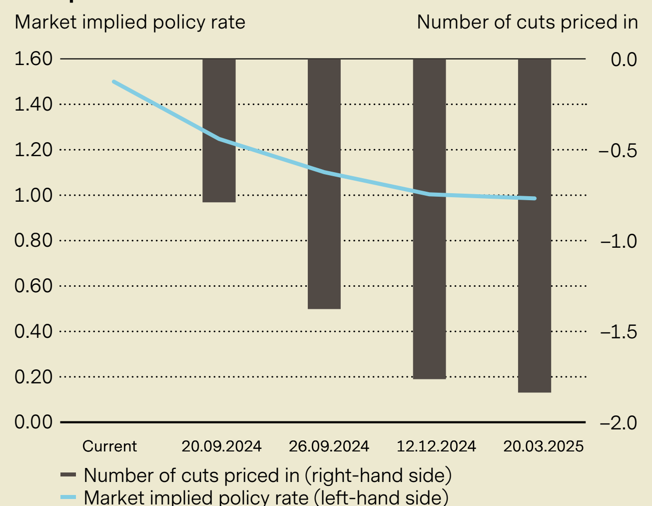
Despite weaker consumer price inflation data in Switzerland, markets continue to anticipate a limited SNB cutting cycle, with only two more cuts fully priced in for this year, ultimately reducing the policy rate to 1 percent (see chart 2). Swiss inflation showed an unexpected slowdown, reinforcing the decision of the SNB to cut interest rates last month. The SNB surprised investors by lowering its key rate last month, a move that was the first of its kind among G-10 central banks since the global inflationary spike.

In March, Swiss consumer prices increased by just 1 percent year-over-year, marking the lowest increase in two and a half years, contrary to the 1.3 percent rise economists had forecasted. The drop in inflation was broad based, indicating that inflationary pressures are subsiding more rapidly than anticipated in Switzerland. The departing SNB President Thomas Jordan expressed confidence that there is "very little risk" of inflation climbing beyond the 2 percent upper limit of the central bank's target. The SNB had previously anticipated a modest acceleration in inflation during the second and third quarter, primarily driven by expected increases in rent.

**Chart 1: The US Dollar Index's jump amid shifting Fed expectations**

Source: Bloomberg, Vontobel; data as of March 16, 2024.

**Chart 2: Market implied SNB policy rate and number of cuts priced in**




Source: Bloomberg, Vontobel; data as of March 16, 2024.

# Economy and financial markets 2022 – 2025

The following list shows the actual values, exchange rates and prices from 2022 to 2023 and consensus forecasts for 2024 and 2025 for gross domestic product (GDP), inflation / inflationary expectations, key central bank interest rates, ten-year government bonds, exchange rates, and commodities.

| GDP (IN %) | 2022 | 2023 | CURRENT[1] | 2024 CONSENSUS | 2025 CONSENSUS |
|---|---|---|---|---|---|
| Global (G20) | 2.9 | 3.0 | 3.2 | 2.6 | 2.6 |
| Eurozone | 3.4 | 0.4 | 0.1 | 0.5 | 1.4 |
| USA | 1.9 | 2.5 | 3.1 | 2.4 | 1.7 |
| Japan | 1.0 | 1.9 | 1.2 | 0.7 | 1.1 |
| UK | 4.5 | 0.3 | –0.2 | 0.3 | 1.2 |
| Switzerland | 2.7 | 0.7 | 0.6 | 1.2 | 1.5 |
| Australia | 3.8 | 1.9 | 2.1 | 1.4 | 2.2 |
| China | 3.0 | 5.2 | 5.3 | 4.7 | 4.4 |

| INFLATION | 2022 | 2023 | CURRENT[2] | 2024 CONSENSUS | 2025 CONSENSUS |
|---|---|---|---|---|---|
| Global (G20) | 7.5 | 4.4 | 3.6 | 5.1 | 3.2 |
| Eurozone | 8.4 | 5.5 | 2.4 | 2.3 | 2.1 |
| USA | 8.0 | 4.1 | 3.5 | 3.0 | 2.4 |
| Japan | 2.5 | 3.3 | 2.7 | 2.3 | 1.8 |
| UK | 9.1 | 7.3 | 3.2 | 2.4 | 2.2 |
| Switzerland | 2.8 | 2.2 | 1.0 | 1.3 | 1.2 |
| Australia | 6.6 | 5.7 | 4.1 | 3.3 | 2.8 |
| China | 2.0 | 0.2 | 0.1 | 0.7 | 1.6 |

| KEY INTEREST RATES (IN %) | 2022 | 2023 | CURRENT | CONSENSUS IN 3 MONTHS | CONSENSUS IN 12 MONTHS |
|---|---|---|---|---|---|
| EUR | 2.50 | 4.50 | 4.50 | 3.55 | 2.70 |
| USD | 4.50 | 5.50 | 5.50 | 5.00 | 4.00 |
| JPY | –0.10 | –0.10 | 0.10 | 0.20 | 0.20 |
| GBP | 3.50 | 5.25 | 5.25 | 4.70 | 3.60 |
| CHF | 1.00 | 1.75 | 1.50 | 1.11 | 0.98 |
| AUD | 3.10 | 4.35 | 4.35 | 4.20 | 3.50 |
| CNY | 3.65 | 3.45 | 4.35 | 4.25 | n.a. |

| GOVERNMENT BOND YIELDS, 10 YEARS (IN %) | 2022 | 2023 | CURRENT | CONSENSUS IN 3 MONTHS | CONSENSUS IN 12 MONTHS |
|---|---|---|---|---|---|
| EUR (Germany) | 2.6 | 2.0 | 2.50 | 2.21 | 2.16 |
| USD | 3.9 | 3.9 | 4.60 | 3.96 | 3.76 |
| JPY | 0.4 | 0.6 | 0.85 | 0.91 | 1.06 |
| GBP | 3.7 | 3.5 | 4.26 | 3.68 | 3.46 |
| CHF | 1.6 | 0.7 | 0.77 | 0.70 | 0.80 |
| AUD | 4.1 | 4.0 | 4.26 | 3.95 | 3.78 |

| FOREIGN EXCHANGE RATES | 2022 | 2023 | CURRENT | CONSENSUS IN 3 MONTHS | CONSENSUS IN 12 MONTHS |
|---|---|---|---|---|---|
| CHF per EUR | 0.99 | 0.93 | 0.97 | 0.99 | 1.01 |
| CHF per USD | 0.94 | 0.84 | 0.91 | 0.91 | 0.90 |
| CHF per 100 JPY | 0.72 | 0.60 | 0.59 | 0.63 | 0.67 |
| CHF per GBP | 1.12 | 1.07 | 1.13 | 1.15 | 1.17 |
| USD per EUR | 1.06 | 1.10 | 1.07 | 1.09 | 1.12 |
| JPY per USD | 130.00 | 141.00 | 155.00 | 145.00 | 135.00 |
| USD per AUD | 0.67 | 0.68 | 0.64 | 0.67 | 0.70 |
| GBP per EUR | 0.88 | 0.87 | 0.86 | 0.86 | 0.86 |
| CNY per USD | 6.91 | 7.10 | 7.24 | 7.20 | 7.00 |

| COMMODITIES | 2022 | 2023 | CURRENT | CONSENSUS IN 3 MONTHS | CONSENSUS IN 12 MONTHS |
|---|---|---|---|---|---|
| Brent crude oil, USD per barrel | 86 | 77 | 86 | 84 | 81 |
| Gold, USD per troy ounce | 1,824 | 2,063 | 2,377 | 2,106 | 2,125 |
| Copper, USD per metric ton | 8,372 | 8,559 | 9,735 | 8,914 | 9,275 |

[1] Latest available quarter
[2] Latest available month, G20 data only quarterly
Source: Vontobel, respective statistical offices and central banks; as of Avril 19, 2024

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