N° 175

2nd quarter 2023

Perspectives

Financial markets analysis

- Turbulence in the banking sector has increased the risk of recession.
- Services inflation, still stubborn, will slow down during the year as the situation on the labour markets deteriorates.
- The central banks' monetary tightening is coming to an end.

- The outperformance of the US market seems to be behind us, unless one thinks that the large technology stocks will maintain their leadership.
- The structural trend towards a better allocation of corporate capital remains the main argument in favour of the Japanese market.
- Gold prices are approaching their 2020 highs.

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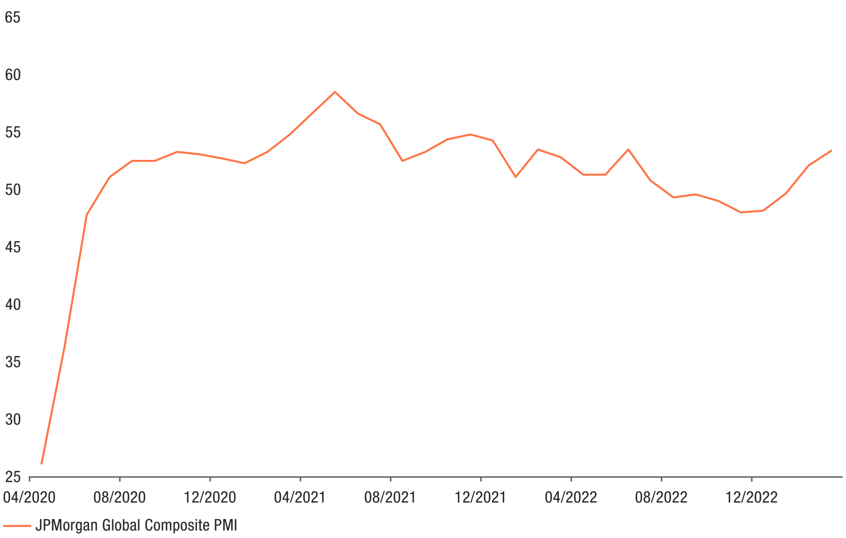
Macroeconomic environment

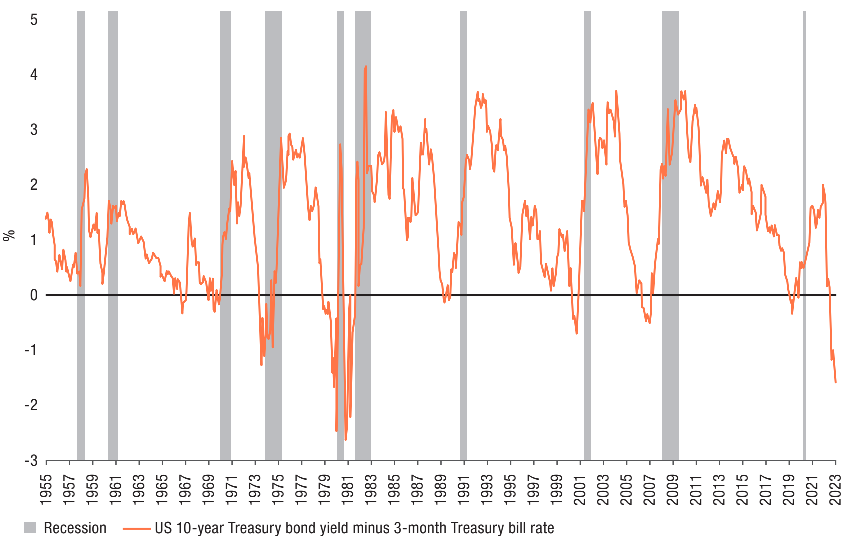
GLOBAL COMPOSITE ACTIVITY INDEX



Source: S&P Global, Bloomberg

The global economy continued to show remarkable resilience in the first quarter, despite intense geopolitical tensions and the central banks' aggressive monetary tightening. The resilient nature of activity is largely due to stable labour markets, with most countries remaining at full employment. Since the end of containment measures, services activities have enjoyed a level of demand that shows no signs of waning, as the deprivation of leisure activities and travel during the pandemic has triggered a seemingly relentless need to make up for lost time. In addition, because of the lower cyclicality of services activities compared to manufacturing, economic activity has become structurally more resilient in the face of all types of obstacles. However, despite being more stable, the economic situation is expected to decline in the second quarter. The current signs of deterioration such as weakness in the real estate sector, slowing manufacturing orders, and lower corporate earnings are generally followed by a deterioration in the labour market marking the beginning of the entry into recession.

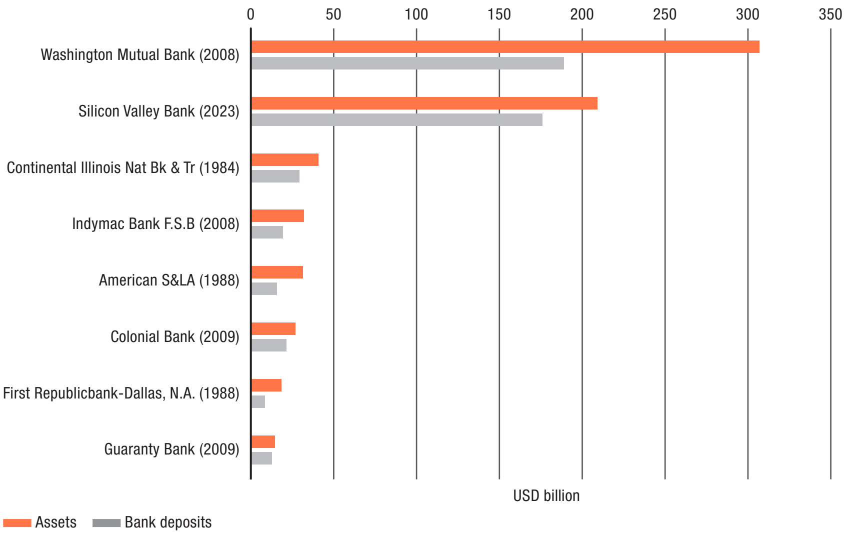
US YIELD CURVE



Source: Federal Reserve, US Treasury, Jefferies

The US authorities seem to have committed economic activity to a 'boom and bust' cycle. After record growth in 2021 following the unprecedented fiscal and monetary support measures, the Federal Reserve's aggressive monetary tightening since March 2022 and the end of the government support programmes have set the stage for a major economic slowdown this year. Since the yield curve has historically been by far the best leading indicator, its current degree of inversion points decisively to the onset of a recession. In the past, every time that the difference between the 10-year and 3-month yield has been negative for more than three months, the economy has subsequently contracted. An exception in the current cycle would be all the more surprising given that the inversion of the yield curve exceeded 150 basis points at the beginning of April, a level only reached in the early 1980s during the Federal Reserve's record monetary tightening under its illustrious chair, Paul Volcker. Because of the usual 12 to 18 month lag between the start of tightening on the one hand and the start of recession on the other, the interest rate hike campaign that began in March 2022 is expected to result in the first decline in GDP in the third or, if not, the fourth quarter at the latest.

BIGGEST BANK FAILURES IN US HISTORY



Source: Federal Deposit Insurance Company, Wall Street Journal

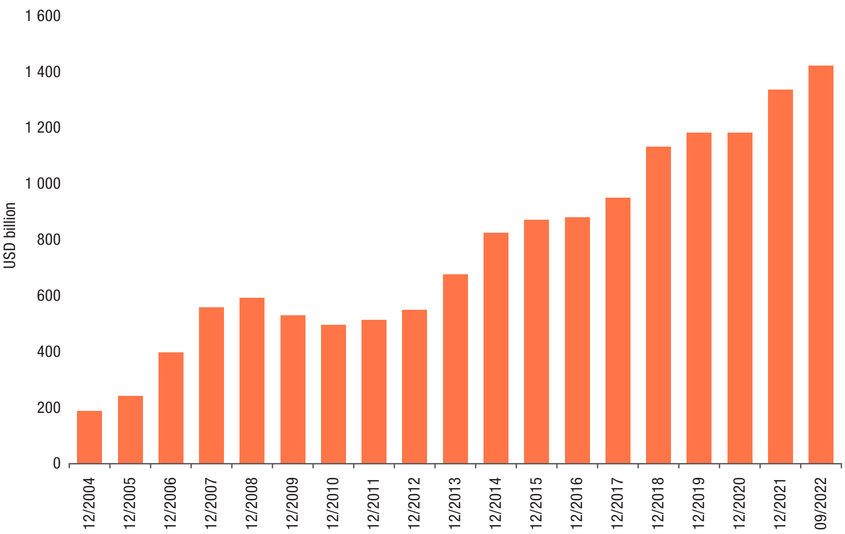
Turbulence in the banking sector since the collapse of Silicon Valley Bank (SVB) has increased the likelihood of a recession during the year. The collapse of the Californian bank was the result of the Federal Reserve's monetary tightening combined with deficient asset-liability management of its balance sheet. Having accumulated a large volume of deposits during the tech boom in the pandemic, SVB had invested the funds in government bonds, at that time offering very low yields. Since SVB had not hedged its securities portfolio against a possible rise in interest rates, it was forced to realise significant capital losses when its clients – who were affected by the slowdown in the technology sector – began to withdraw some of their deposits. The announcement of a capital raise quickly triggered a flight of funds that was fatal to the bank, making this the second largest bank collapse in US history. Panic spread like wildfire, triggering a massive transfer of deposits from medium-sized banks to the major players considered to be systemic, and hence theoretically too big to fail.

BANK DEPOSITS AND MONEY MARKET FUND ASSETS IN THE US

Source: Federal Reserve, Investment Company Institute, Bloomberg, Jefferies

In order to stop the haemorrhaging of mid-sized banks, the US government extended the deposit guarantee for the failing Silicon Valley Bank beyond the USD 250,000 limit covered by the Federal Deposit Insurance Company (FDIC). The Federal Reserve has also established an additional line of credit to provide banks with access to liquidity in the event that customers withdraw deposits on a large scale. While these measures appear to have curbed the transfer of funds from smaller to larger players within the banking sector, they will do little to reverse the trend of households replacing their deposits with money market funds offering higher rates of return. The deposit flight may force banks to offer higher rates of return, thereby lowering their interest margins, and to limit the volume of new lending in order to avoid a balance sheet imbalance between outstanding loan assets and deposit liabilities. This development will inevitably end up slowing down the level of cyclical growth due to a significant reduction in the financing possibilities for all economic agents.

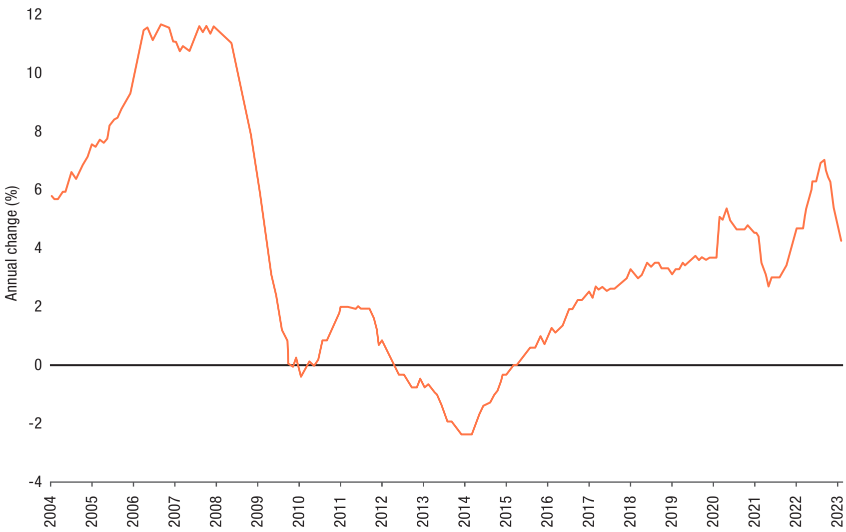
US LEVERAGED LOANS OUTSTANDING



Source: Federal Reserve – Financial Stability Report, S&P Global, Jefferies

Apart from the financial risks in the banking sector, the strong growth of private equity funds is a potential additional source of crisis in the wake of the Federal Reserve's aggressive monetary tightening. This is because leveraged loans, which are loans made to companies that are already highly indebted, are the primary source of private equity financing. This industry has the potential to cause a major incident at any time due to a much less stringent regulatory framework than that applied to traditional commercial banks. In addition, most leveraged loans are issued at variable rates and are therefore very sensitive to changes in monetary policy. Finally, all players involved in the private equity industry have an interest in delaying price discovery as long as possible, whether they are the capital lender, the fund manager or the end investor. Monetary tightening will therefore have a delayed impact in a context of ongoing favourable financing conditions while the underlying business fundamentals have already deteriorated considerably.

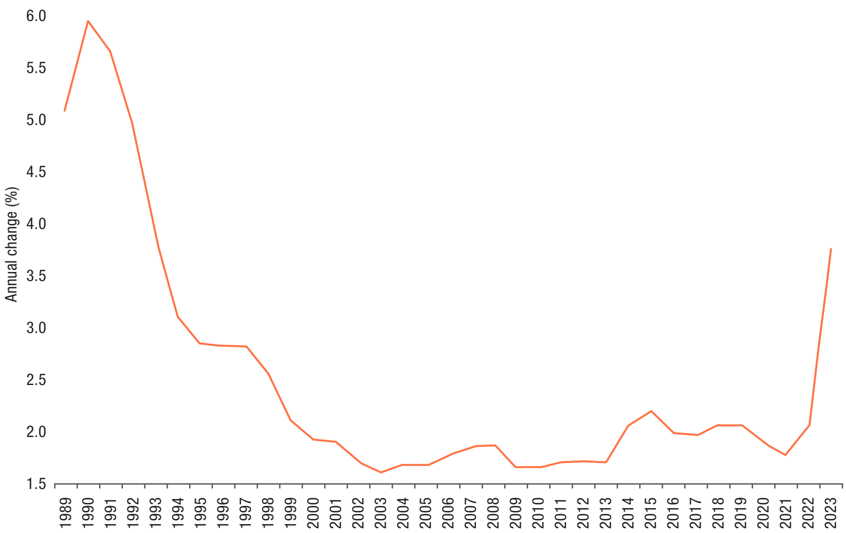
EUROZONE LOAN GROWTH TO THE PRIVATE SECTOR



Source: ECB, Jefferies

The economic situation in the eurozone is comparable to that in the US. The current resilience of the economy is mainly due to the favourable behaviour of the labour market, which is not yet showing signs of deterioration. Consumption of services remains high, and retail sales continue to grow in nominal terms although they have started a downward trend in real terms. In contrast to the US, industrial production has even rebounded slightly due to falling gas prices after a milder than expected winter. Despite the current resilience, cyclical deceleration is expected to intensify in the coming months. Real estate activity is beginning to slow considerably in most countries, although the relatively high proportion of fixed-rate loans should prevent a crisis similar to that of 2008, when variable-rate loans were largely predominant. Turbulence in the banking sector also reached Europe, as the Swiss authorities were forced to orchestrate the urgent merger of an imperilled Credit Suisse with its rival UBS in order to prevent its liquidation. This instability will reinforce the banks' reluctance to incur additional risk, and accentuate the moderation in private sector loan growth already in evidence since Q4 2022.

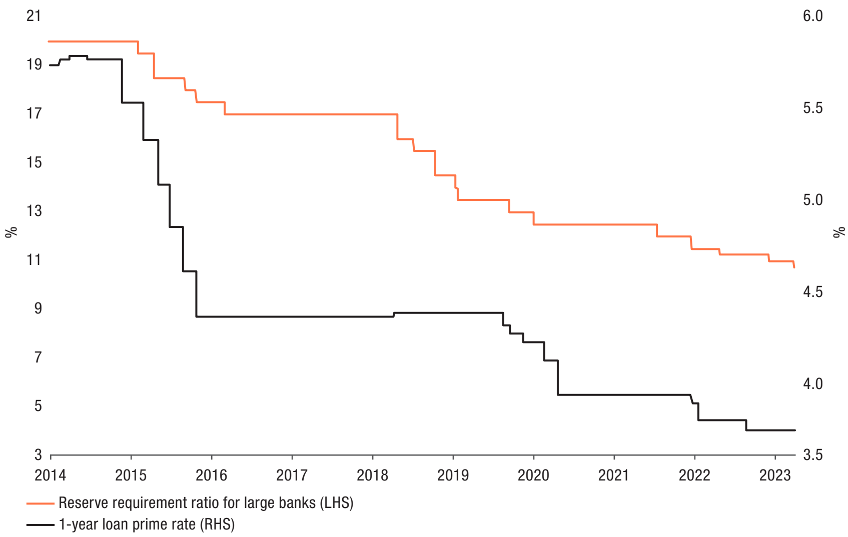
AVERAGE WAGE INCREASE IN JAPAN'S SPRING WAGE NEGOTIATIONS



Source: Japanese Trade Union Confederation (Rengo), Jefferies

After taking the reins at the Bank of Japan in early April, the new governor Kazuo Ueda made no mention of any desire to change his predecessor's ultra-accommodative monetary policy. Nevertheless, Japan's highest monetary authority is faced with a dilemma that could become more acute. On the one hand, the 2% inflation target could be jeopardised by the annual spring wage negotiations, which have resulted in preliminary average increases of 3.8%, the highest increase in three decades, including a 2.25% increase in the base wage. On the other hand, Japan's inflation rate is nowhere near the high levels recorded in both the US and Europe, and has recently begun to trend downwards. At the same time, despite the low level of long-term interest rates, the majority of Japanese real estate loans are at variable rates and therefore highly sensitive to the slightest monetary tightening. Finally, abandoning yield curve management would expose the Japanese banking sector to an asset-liability management risk similar to that of US and European banks, a risk that Japan might be tempted to avoid after the Silicon Valley Bank and Credit Suisse calamities. The new Governor Ueda is expected to provide more clarity on the country's future monetary strategy at the Bank of Japan's next meeting in late April.

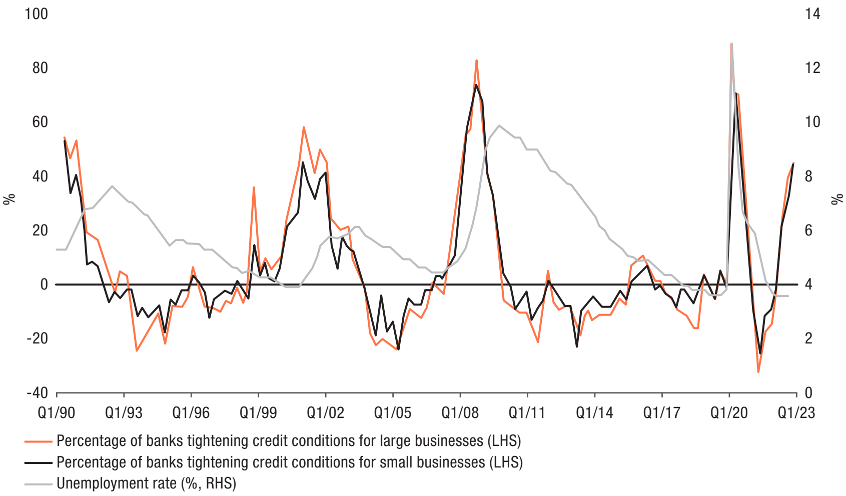
MONETARY POLICY IN CHINA



Source: PBOC, CEIC Data, Jefferies

Visibility regarding the extent of China's post-pandemic recovery is relatively low. Following the reopening of the economy after a prolonged period of lockdowns, domestic services activities are rebounding in line with expectations. However, the industrial sector is struggling to recover as it is affected by the slowdown in foreign demand. In the real estate sector, the situation is stabilising, as sales of existing homes have returned to pre-pandemic levels. Land purchases by real estate developers, a key factor for recovery in the construction sector, still seem premature, generally lagging the recovery of the secondary market by nine months. Although inflation and hence interest rates remain low in China, unlike in the West, the Chinese government is being careful to avoid excessive credit growth, preferring moderate support measures, such as the recent 25 basis point reduction in the banks' required reserve ratio. Boosting activity without unduly increasing the financial risks seems to be the Beijing government's plan of action.

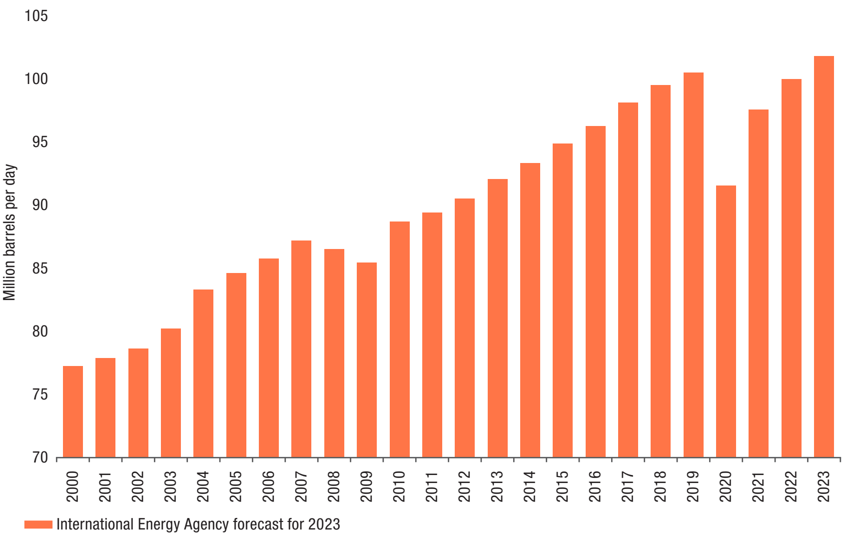
TIGHTENING CREDIT CONDITIONS AND UNEMPLOYMENT RATE IN THE US



Source: Senior Loan Officer Onion Survey, Bureau of Labor Statistics, Morgan Stanley Research

After a strong price surge in 2022, inflation rates are now in a slowing phase. The moderation in inflationary pressures is primarily affecting energy, food and many consumer goods, while services inflation remains stubborn for the time being. US headline inflation fell from 9.1% in June last year to 5.0% in March, while core inflation (i.e. excluding energy and food components) dominated by services only fell from 5.9% to 5.6%. By the end of the year, however, the situation is likely to change for two main reasons. First, the heavy shelter component should begin a phase of moderation as rents gradually ease. Second, the current tightening of credit conditions in the banking sector is generally followed by an increase in the unemployment rate, leading to a slowdown in wage growth, which is highly correlated with core inflation. If the labour market deteriorates as expected, services inflation, which has been tenacious so far, will start to slow.

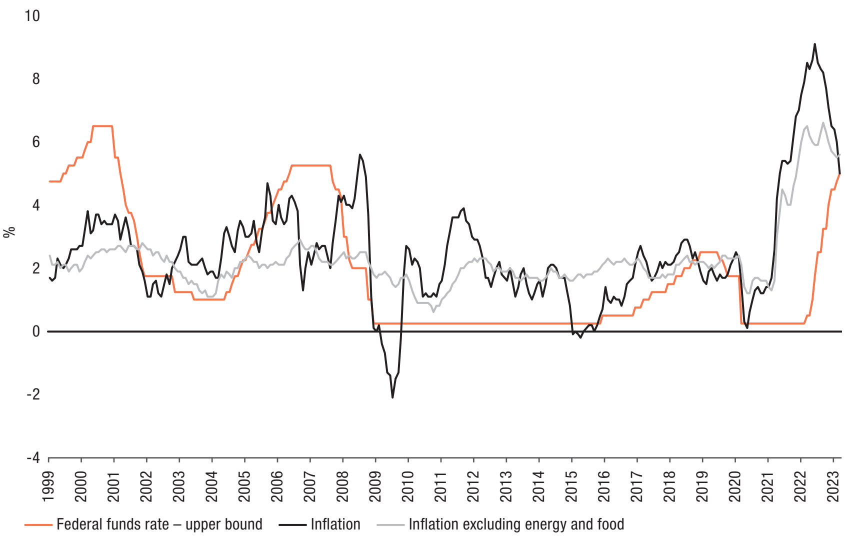
GLOBAL OIL DEMAND



Source: International Energy Agency (IEA), Jefferies

The recent decision by OPEC+ to cut oil production by 1.16 million barrels per day reflects unprecedented discipline by the oil exporting countries and their allies. This reduction follows a 2 million barrel per day cut in October 2022 and is aimed at avoiding a price collapse in anticipation of a global recession. These actions illustrate the US's gradual loss of influence over Saudi Arabia, which, along with the other members of the Gulf Cooperation Council, is moving closer and closer to China, whose energy needs are growing sharply. The development of contracts to pay for Saudi crude in renminbi, as well as the spectacular rapprochement between Saudi Arabia and Iran negotiated by China, also testify to the evolution of alliances on the geopolitical level. OPEC+'s decision to cut oil production could therefore doubly affect Western countries by thwarting the disinflationary actions of their central banks, while at the same time accentuating the weakness of the global economy just when it is about to enter recession.

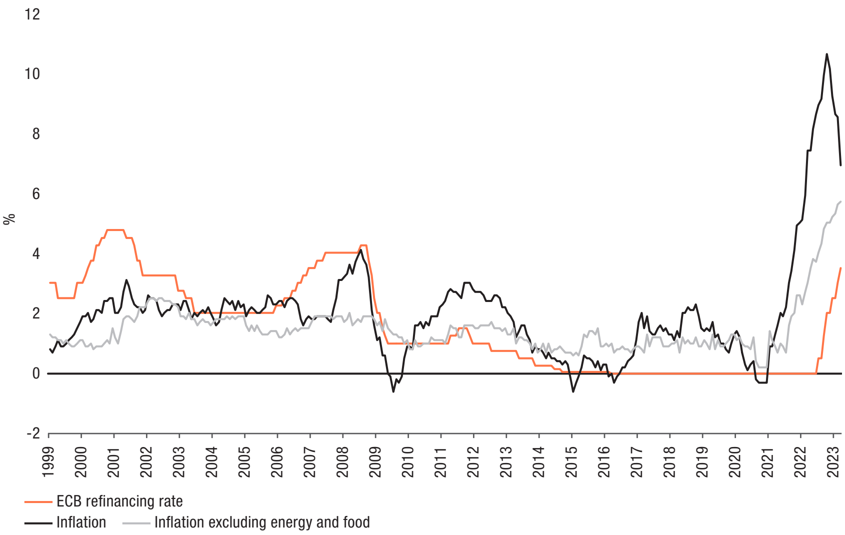
US MONETARY POLICY



Source: Bloomberg, Federal Reserve, Bureau of Labor Statistics

At each of its two meetings in Q1 2023, the US Federal Reserve raised the target range for the federal funds rate by 25 basis points, taking it to 4.75%–5.00%. Since the start of monetary tightening in March 2022, the target range has now been raised by 475 basis points, an order of magnitude that has historically always triggered a financial crisis. In the coming months, US monetary policymakers will therefore have to find a balance between meeting inflation targets on the one hand and the stability of the banking sector on the other. The tenacity of services inflation argues for continued monetary tightening to completely dispel the anchoring of rising inflationary expectations. On the other hand, the flight of bank deposits triggered by Silicon Valley Bank's collapse and accentuated by higher money market rates argues for a rapid cessation of interest rate rises. The pragmatic solution that the Federal Reserve seems to be moving towards is, assuming no new events, to raise the fed funds rate target range by 25 basis points one last time in May, before pausing to observe the impact of monetary tightening on economic activity in general, and the financial sphere in particular.

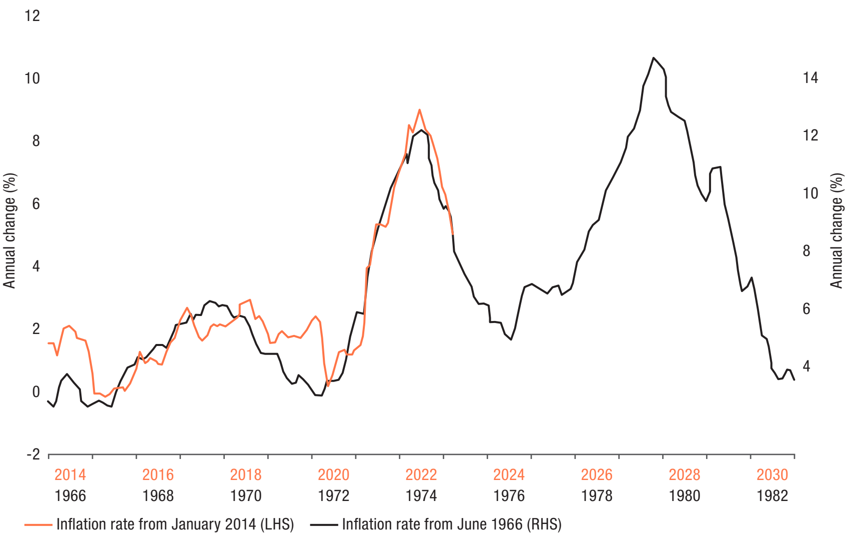
EUROZONE MONETARY POLICY



Source: Bloomberg, ECB, Eurostat

With the European cycle lagging the US cycle by a few months, inflation excluding energy and food in the eurozone is still in an ascending phase, suggesting an even longer period of tightening on the European side. However, since the emergency rescue of Credit Suisse, European Central Bank officials have been more reserved in their guidance to the markets. At the last meeting of the Governing Council, at which the ECB's refinancing rate was raised by 50 basis points to 3.5%, ECB president Christine Lagarde gave no guidance whatsoever to the markets, preferring to wait for the publication of the next inflation statistics and to monitor the evolution of the situation in the banking sector before making a more precise statement. Provided nothing untoward intervenes, the ECB's key rates are expected to continue to rise, but more likely in 25 basis point increments, as opposed to the 50 so far. Nevertheless, although the monetary authorities never tire of emphasising the current strength of the banks compared with the situation prior to the euro crisis in 2012, they are well aware that the probability of financial turbulence remains high. As a result, even on the European side, a potential rate hike in May could eventually prove to be the last in the current tightening cycle.

US INFLATION

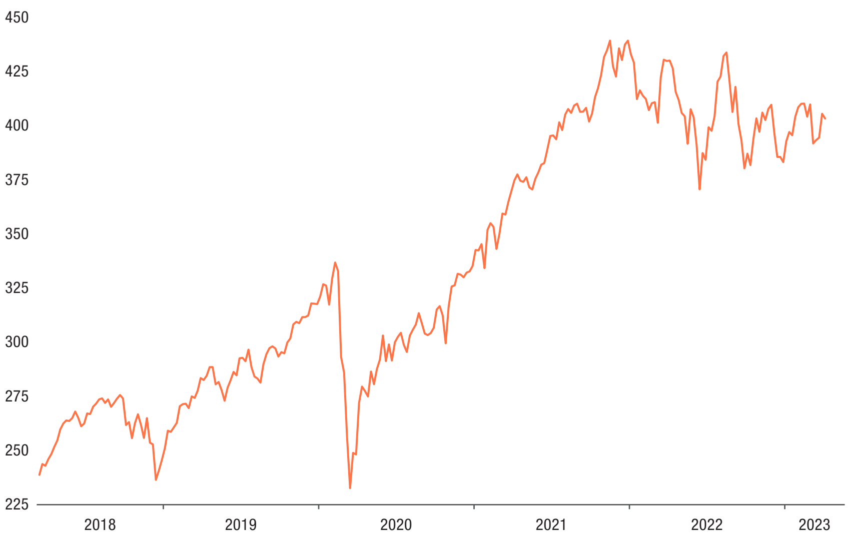


Source: BCA Research 2023

Although inflation will slow this year, it could prove to be both more volatile and higher on average over the coming decade. Of the four deflationary trends of the past 20 years, only digitisation seems to persist. The other three trends – globalisation, restrictive fiscal policies, and surplus labour and raw material resources – are gradually being squeezed out by geopolitical tensions, expansionary fiscal policies, and a deficit in human and natural resources. The world economy seems to be going through a structural transition phase corresponding to a regime change that occurs every half century. The current period is reminiscent of the 1970s, when the United States ended the convertibility of the dollar to gold and negotiated with Arab countries to introduce the petrodollar, thereby changing the monetary system that had been in place since the Bretton Woods Agreement after World War II. Recent developments suggest that the current monetary system based on the dollar as the ultra-dominant reserve currency is gradually coming to an end. Such transition phases are usually characterised by high volatility at all levels – inflation, interest rates and financial asset values – and they therefore harbour many risks, but also numerous opportunities.

Financial markets

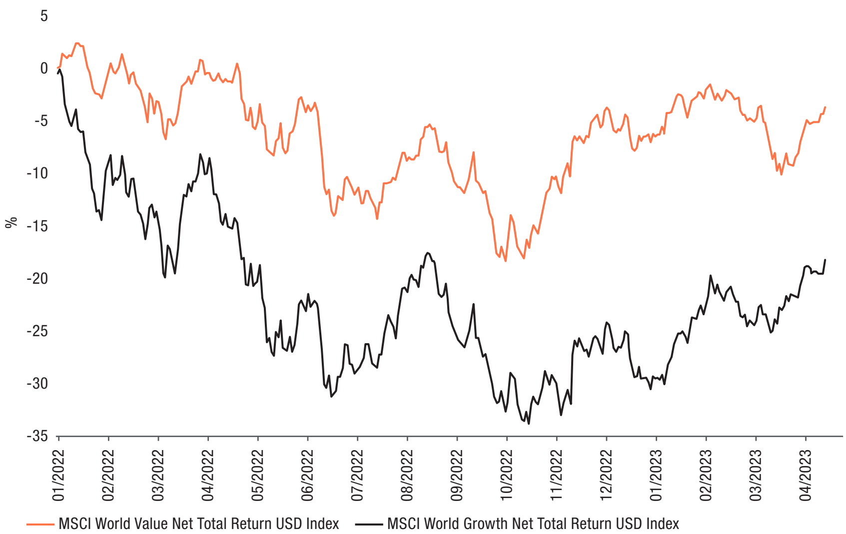
MSCI WORLD INDEX IN EURO



Source: Bloomberg

After their decline in 2022, financial markets rebounded in the first quarter. The month of January in particular was very favourable. Falling inflation suggested that central bank monetary tightening would soon end, while signs of resilience in economic activity fuelled expectations of a soft landing for the global economy. February was less buoyant, due to less encouraging inflation figures, reflecting in particular the tenacity of core inflation (excluding energy and food). March was then marked by tensions in the banking sector. While these tensions weighed heavily on the banking sector and led to a slight decline in the European market, they did not prevent the global equity index from rising, helped by the decline in bond yields. For the first quarter as a whole, European markets were the best performers, while Asian markets lagged somewhat.

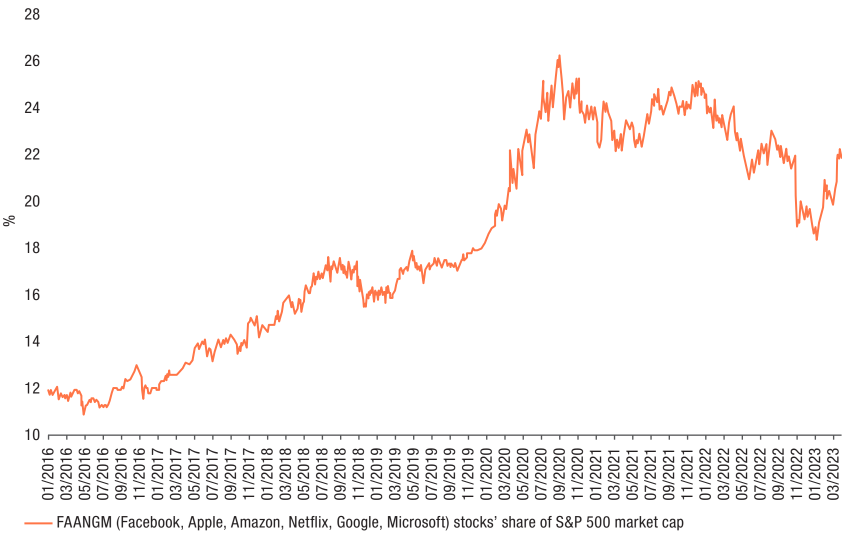
MSCI WORLD GROWTH AND VALUE INDICES IN DOLLARS



Source: Bloomberg

Within the stock markets, the decrease in risk aversion and the decline in bond yields particularly benefited growth stocks, especially technology stocks. In the United States, three stocks – Apple, Nvidia and Microsoft – accounted for more than half of the increase in the S&P 500 index over the quarter. Their performance was mainly due to an increase in their valuation. At the other end of the spectrum, sectors generally associated with the value style were neglected. The fall in oil prices weighed on the energy sector, the collapse of Silicon Valley Bank in the US and the takeover of Credit Suisse in Europe on financials, and growing concerns about US growth on the industrial materials. As a result, the MSCI World Growth Index outperformed the MSCI World Value Index by 13% in the first quarter, after underperforming by nearly 25% last year.

SHARE OF THE TOP 6 TECHNOLOGY STOCKS IN THE S&P 500



Source: Bloomberg, Jefferies

The rise of the tech sector has caused the share of the 'big 6' tech stocks (Apple, Meta, Alphabet, Amazon, Netflix and Microsoft) in the S&P 500 to rise again, from 18% in early January to 22% at the end of March. It had reached a high of 26% in September 2020. As is usually the case, investors seem to be looking in the rear-view mirror and assuming that the winners of the recent past will also be the winners of the future. Technology stocks have indeed been the big winners in the years following the financial crisis. Their ability to show strong earnings growth and visibility in an environment of moderate economic growth meant that they were, and still are, considered high-duration stocks. As such, they benefited from an upward adjustment of their valuation multiples in an environment of historically low interest rates, and therefore from a double effect: higher earnings and higher multiples that investors were willing to pay for those earnings. In addition, the trend towards passive management meant that as the prices of these stocks and their weighting in the S&P 500 increased, they attracted more capital.

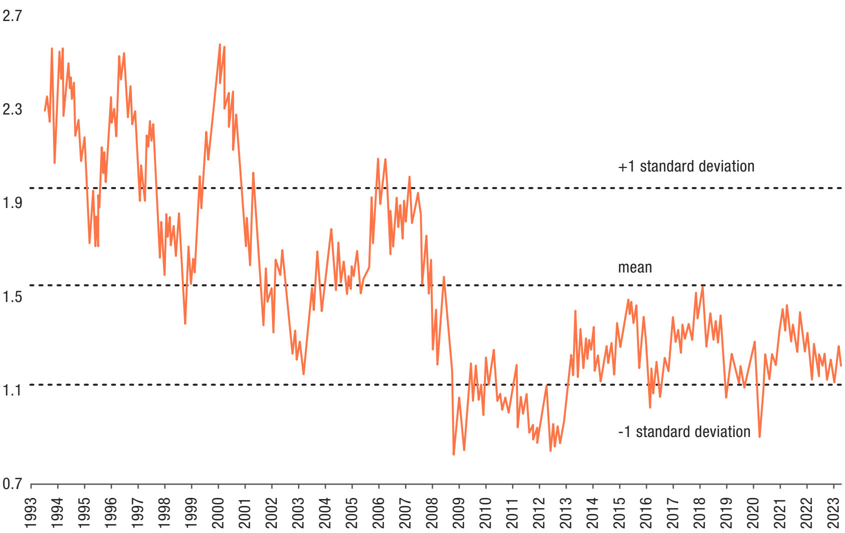
EARNINGS PER SHARE AND PRICE/EARNINGS RATIO OF ALPHABET, APPLE AND MICROSOFT

	Earnings per share		Price/earnings ratio	
	2012	2022	2012	2022
Apple	1.58	6.11	15	23
Microsoft	2.69	9.16	11	28
Alphabet	0.87	4.56	20	20

Source: Bloomberg

Unless we believe that the environment in the coming years will be identical to that of the last few years, it does not seem realistic to expect a new period of sustained outperformance by technology stocks. While it is too early to talk about a paradigm shift and a further decline in bond yields is still possible in the event of a pronounced economic slowdown, it is clear that the days of an environment marked by permanently low and stable inflation and historically low interest rates seem to be over. However, the main argument against the return of a sustainable leadership of the few large technology stocks is based on common sense and lies in the base effect: the earnings of these companies and their valuation multiples are now significantly higher than in 2009. Without such an outperformance of technology stocks, it is difficult to see the US market continuing to do much better than other markets.

PRICE/BOOK RATIO OF THE TOPIX INDEX



Source: Bloomberg

The structural trend towards better capital allocation remains the main argument in favour of the Japanese market. While for a long time Japan was the mirror image of the US in terms of shareholder treatment, things started to change in the first decade of this century. The profitability of Japanese companies is continuously improving and they are willing to pass on the benefits to their shareholders through dividend increases and share buybacks. The recent decision of the Japanese Stock Exchange to encourage reforms in companies that are trading below book value is a further step in the same direction. This has not yet been honoured by investors and the Japanese market is trading at attractive valuations in absolute and relative terms (compared to bonds and other equity markets). Added to this is the fact that for many experts, the yen is highly undervalued. The Japanese market thus offers the rare combination of stock price and currency appreciation potential.

YEN TO DOLLAR EXCHANGE RATE

Source: Bloomberg

It will be interesting to see if the Bank of Japan's monetary policy will change with the arrival of Kazuo Ueda as the new governor. A continuation of the current monetary policy would be difficult to justify in an environment where the main stated objectives of that policy, rising inflation and wage growth, seem to have been achieved. A possible normalization of the yield curve would also prompt local institutional investors to reallocate their assets. Currently, the equity allocation of pension funds and life insurance companies is estimated at 8% and 6% respectively, despite the broad outperformance of equities against bonds since the introduction of a set of policies known as Abenomics in late 2012 and the fact that the dividend yield on equities exceeds that on government bonds. Such a normalization of the yield curve would in principle be accompanied by an appreciation of the yen and thus limit the appetite of Japanese investors for foreign assets.

MSCI CHINA INDEX IN DOLLARS

Source: Bloomberg

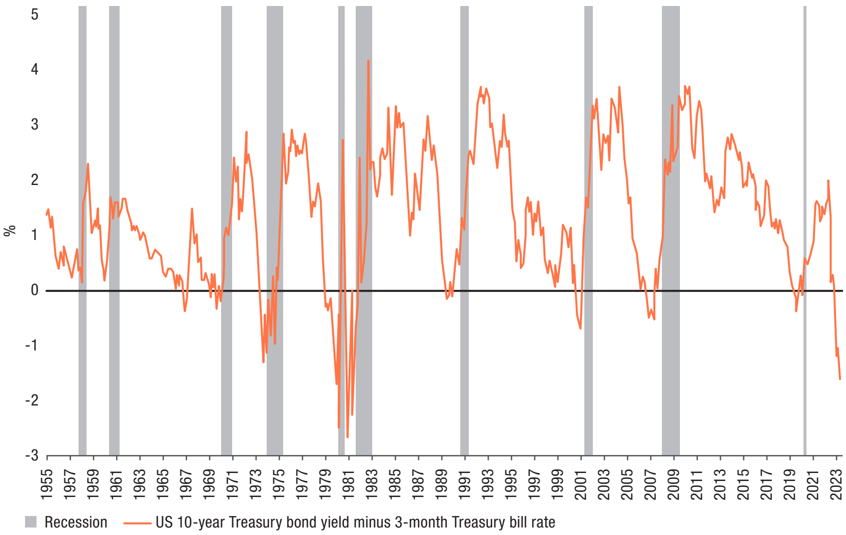
The abandonment of the 'zero-covid' health strategy and the reopening of the economy had led to a strong rebound in the Chinese market between early November and early February. Since then, the market has again given up some of the gains. Many investors remain wary of the Chinese market given the measures taken by the Chinese authorities against certain sectors and the worsening tensions between China and the United States. They remain largely absent from this market despite the fact that China represents one third of the emerging market index. The Chinese authorities have been trying for some time to convince investors of their willingness to pursue market-friendly policies and their intention to guarantee property rights. The decision to split Alibaba into six entities was thus welcomed by the markets. However, one has to be aware that the Chinese market is governed by different rules than the US market. The objectives of the Communist Party take precedence over the rights and interests of shareholders, which results in a higher risk premium demanded by investors and therefore a lower valuation.

US 10-YEAR GOVERNMENT BOND YIELD

Source: Bloomberg

After their historic decline in 2022, bond markets recovered in the first quarter. The decline in inflation, the economic slowdown, expectations of a rapid end to central bank tightening and the tensions in the banking sector that emerged in March were behind this recovery, which had in fact already begun in October of last year. After reaching a high of 4.25% at the end of October 2022, the yield on the US 10-year government bond ended the year at 3.87%. It continued to decline during the first quarter, reaching 3.47% at the end of March. The situation is different in the euro zone, where German and French 10-year rates are still practically at the same level as in October. Between the Federal Reserve's continued increase in key rates and the decrease in long-term bond yields, the inversion of the US yield curve has intensified. The spread between the 10-year rate and the 3-month rate has gone from positive 200 basis points to negative 140 basis points since April 2022. Such a negative spread had not been recorded since the early 1980s.

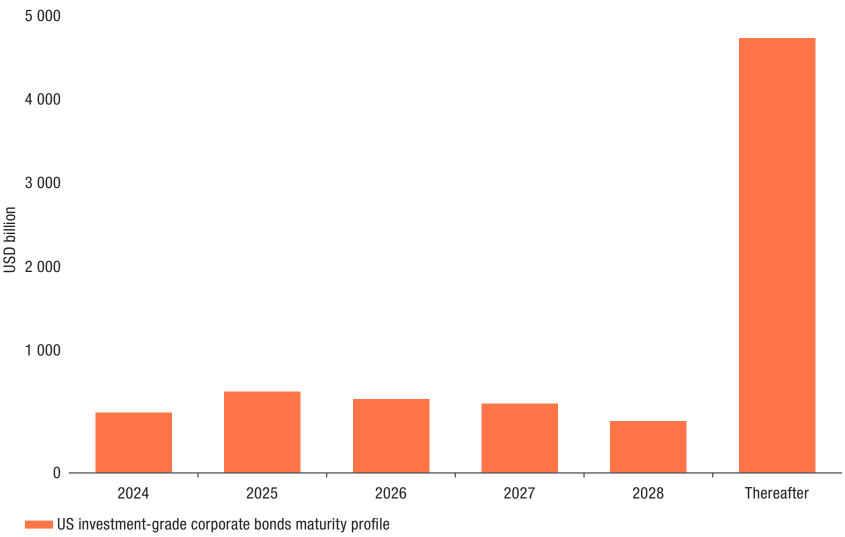
US INTEREST RATE CURVE



Source: US Treasury, Jefferies

The continued economic slowdown should continue to support government bond prices in 2023. In an environment where demographic trends, environmental constraints, military spending and social demands are leading to ever-increasing government financing needs and where inflation is likely to be structurally higher, the longer-term outlook for this asset class appears to be much less favourable. To prevent a sharp rise in bond yields from causing the cost of government debt to explode, central banks could abandon their objective of reducing the size of their balance sheets and resume buying bonds, even though they already hold between 20% (Federal Reserve) and 50% (Bank of Japan) of their respective countries' government bonds. In such a scenario, the real, inflation-adjusted yields offered by these bonds would become largely negative. Government bonds would then again make no sense for rational investors.

MATURITY OF US INVESTMENT GRADE CORPORATE DEBT



Source: Bloomberg, Jefferies

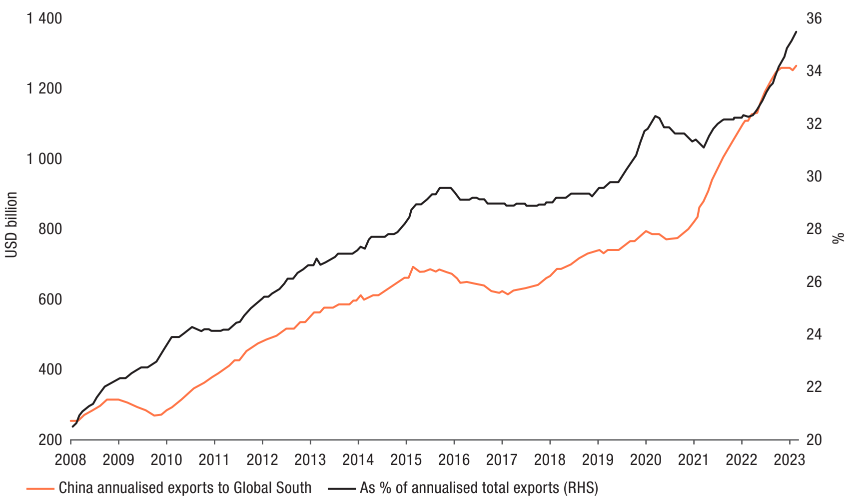
Private sector debt has so far held up well in the face of rising interest rates and a slowing economy. After rising in the first half of last year, the interest rate differential with government bonds has narrowed again and remains low. It is true that many companies have taken advantage of the particularly low interest rates of recent years to take on longer-term debt. As a result, relatively few loans will mature in 2023 and 2024 and the financing requirements are therefore relatively low. Nevertheless, the longer interest rates remain at their current level, or even rise further, the greater the risk that players will suffer financial problems. In addition, many loans originated in the shadow banking system, especially in the private equity sector. Since this system is much less regulated and supervised than the traditional banking system, it is difficult to get an idea of the extent of the risks.

EUR/USD EXCHANGE RATE

Source: Bloomberg

After continuing its appreciation that started at the end of 2020 over the first 3 quarters of last year, the US dollar has since lost over 10% against the single currency. The factors behind the greenback's appreciation are disappearing. The Federal Reserve, which started its monetary tightening before the other major central banks, is also expected to complete it before the others. If this is the case, the short-term interest rate differential between the dollar and other currencies will narrow. As for the interest rate differential on long rates, it has already narrowed considerably. The problems in the banking sector have also led the Federal Reserve to inject liquidity into the system again. Furthermore, the US current account balance will deteriorate if the depletion of shale gas deposits is confirmed. Finally, the reopening of the Chinese economy has allowed Chinese dollar savings to be injected back into the system.

PERCENTAGE OF CHINESE EXPORTS GOING TO THE GLOBAL SOUTH



Source: CEIC, Jefferies

A current buzzword is de-dollarization. This word describes the idea that the dollar will increasingly be replaced by other currencies in trade transactions between countries (especially those related to commodities) and central bank foreign exchange reserves. It is obvious that as a result of the increasing fragmentation of the world economy and the decision of the United States to use the dollar more and more as a geopolitical weapon, many countries are now interested in reducing their dependence on the dollar. China is trying to expand its relations and sphere of influence in the Middle East at a time when relations between Saudi Arabia and the United States have deteriorated significantly. In particular, it aims to pay for its raw material imports in renminbi. Latin American countries are trying to emancipate themselves from the United States and the war in Ukraine is helping to divide the world. The dollar network is therefore beginning to contract and this trend is expected to accelerate. Even if no currency is yet able to replace the dollar as the world's reserve currency and even if the dollar system has been consolidated and strengthened by each of the recent crises, an alternative commodity-based and producer-controlled monetary system is beginning to emerge in some parts of the world.

GOLD PRICES

Source: Bloomberg

In early April, the gold price approached its August 2020 high. The yellow metal benefited from a weak dollar, falling bond yields and rising risk aversion. Although corrections are still possible, the uptrend now seems well established. The main argument in favour of gold is that the need to finance large deficits will lead to a continued increase in the supply of fiat currencies. The monetary tightening currently underway in the G7 countries is thus likely to end before inflationary pressures are sustainably addressed. The value of the currencies of these countries in relation to a hard currency such as gold will therefore fall, especially as the future supply of the yellow metal will be limited by the lack of investment in recent years.

VANECK GOLD COMPANY INDEX

Source: Bloomberg

Gold companies offer leverage to further appreciation in the gold price. The gold mining index has risen by some 60% since the end of September, but remains 45% below its high in August 2011. Gold companies are currently still paying for their past mistakes. They tended to act in a pro-cyclical way by increasing their investments or making acquisitions when the gold price was high. These investments and acquisitions often proved to be unprofitable once the price of the metal fell again. However, companies in the industry seem to have learned from these mistakes and are now more disciplined in their capital allocation. However, it is important to be very selective in this sector.

Summary

In summary, the impact of the monetary tightening started by central banks in March of last year is becoming increasingly visible. The economic slowdown should therefore continue and an entry into recession seems possible in the second half of the year or in early 2024. If this were the case, the stock markets would be at risk of a second downward movement linked to the contraction of earnings, whereas last year's was linked to the contraction of multiples.

Unless one believes that the large technology stocks will regain their leadership in the stock market, the outperformance of the US market is behind us. Such a return to leadership would require a return to the environment that characterized the years 2009 to 2021, marked by moderate growth, stable inflation and increasingly low interest rates. The possibility of a new structural environment emerging, with higher inflation leading to higher nominal growth, will have positive implications for other markets, particularly Asian markets.

Government bonds should continue to benefit from slowing economic activity and lower inflation in 2023, even though long-term rates are already partly anticipating the deterioration of economic activity and the end of central bank monetary tightening. The long-term outlook for bonds, however, does not look good, given government financing needs and the risk of persistently higher inflation.

Gold continues to have a place in a diversified portfolio, especially given the possibility that central banks may abandon their monetary tightening prematurely. However, an investment in the yellow metal should be seen as insurance and not as a short-term trade.

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