SAF & CO

Independent Wealth Management

Monthly Review:

All-time highs…What’s next?

Geneva | February 2024

Overview

SAF&CO's monthly global outlook and portfolio allocation

Outlook

- In February, all major indexes in the USA surged to record highs, maintaining their bullish trajectory propelled by good earnings reports, especially by the 'Magnificent Seven'. Concurrently, fixed income spreads continued to narrow, now approaching historic lows.

Allocation

- During the month of February, we maintained our target allocation of 40% Equity and 40% Fixed income while slightly increasing our exposure to the S&P500 in the US.

Bonds

- In light of the spread compression the market is experiencing recently, we keep being more exposed to Investment Grades and are optimizing our portfolio to start lowering our spread risk

Equities

- Our equity portfolio remains underweighted in the overall allocation. We keep being optimistic on the US economy and maintain our overweight to the US over Europe.

Alternatives

- Our alternatives exposure did not change, the portfolio keeps giving us a good diversification in light of equities being at all time highs.

Monthly Review

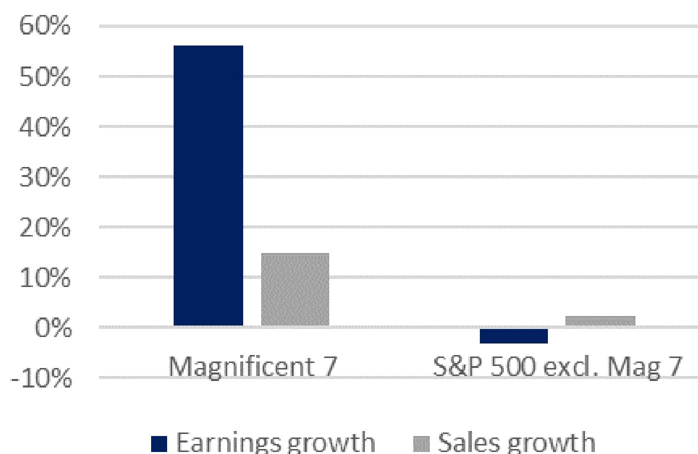
February 2024 - Overview

In February, the upward trajectory observed since November persisted, culminating in **record-high prices for both the S&P 500 and NASDAQ**, which gained 5.2% and 6.1% respectively, concluding a 4-months winning streak with the S&P 500 closing for the first time above 5’000 points. **Conversely, long-term treasury yields rebounded to 4.26%** as the market adjusted its rate cut expectations in response to January's unexpectedly high CPI figures.

The US Equities experienced notable momentum **driven primarily by the positive Earnings Reports** of the Magnificent Seven (See figure 1). Notably, close to half of the monthly performance happened on Feb 21st, when Nvidia's impressive performance bolstered investors’ confidence, surpassing the high expectations of the market. This marked a turning point in the month and drove both indexes even higher. The company demonstrated remarkable growth, with revenue nearly tripling and earnings increasing eightfold over the past year. **Despite the market's concentration**, with only 10 companies contributing to over 60% of the performance on that day, the broader equity landscape remained buoyant, with **70% of stocks delivering positive returns in February**.

Macroeconomic indicators presented a mixed picture. **US consumer confidence**, which had seen three consecutive months of gains, **retreated to 106.7** from January's 110.9, falling below the anticipated 114. Households expressed growing concerns regarding the labor market and the domestic political landscape. **Additionally, the manufacturing Purchasing Managers' Index (PMI) declined to 47.8** from January's 49.1, failing to meet expectations. New orders reverted to contraction territory, while both new exports and imports experienced increases. Inflation keeps being the major concerns of consumers and, following the **January’s hotter than expected CPI (3.1% against 2.9%) the market continued its bond’s repricing and cuts expectations.**

Figure 1: Magnificent Seven YoY Earning and Revenue growth Q4 2023



Source: : SAF&CO, Bloomberg, Syz Group

Currently, these are expected to be postponed to the summer and are getting **closer to the 75bp cuts in 2024 that the fed plotted, compared to the 150+ basis points cut that were priced at the beginning of the year.** The month closed on a positive indicator, reassuring investors we are still in the disinflation trajectory after the **Core PCE (the main indicator that the Fed follows) was 2.8% as expected.**

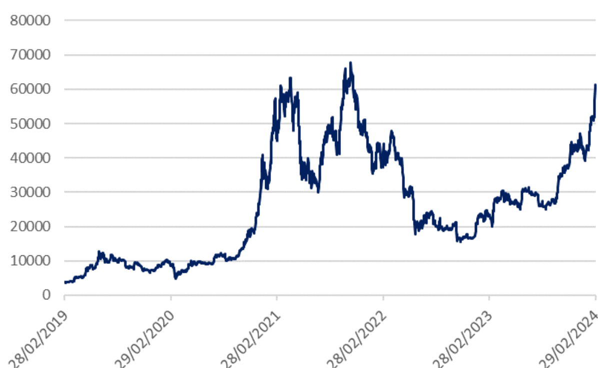
Consequently, yields initially retraced back reaching a high of 4.32% on February 22nd but closed the month at 4.25% seeing a lot of volatility throughout the month between 4.30% and 4.15%. While **High Yield and Emerging markets bonds have benefited from spreads contractions** (See figure 3 and 4) and tend to have a positive performance since the beginning of the year, Investment Grades where spreads had a smaller impact, suffered with the adjustment of the yield.

In Europe, the Euro Stoxx 50 index witnessed a notable **increase of 5.1%.** This growth occurred **despite only half of the companies surpassing expectations,** which were already relatively modest for the region. In fact, this marks the lowest percentage of outperformers since the first quarter of 2020. Both the Consumer Price Index (CPI) and Core CPI remained in line with expectations, standing at 2.8% and 3.3% respectively. Additionally, the yield on the German bund experienced an uptick from 2.16% to 2.41% over the course of the month.

In February**, China emerged as the top-performing major economy**, evidenced by the Hang Seng index closing with a substantial gain of +6.48%, bringing its year-to-date performance close to positive territory. This performance occurred despite the persistent challenges posed by the ongoing property crisis and deflationary pressures. Market sentiment received a boost as **regulators initiated policies aimed at bolstering both the market and the broader economy** such as strong rate cuts on the 5-year term. Regulatory authorities also introduced a series of measures to support the stock market, including restrictions on the short selling.

From a commodity perspective**, Crude oil closed at 78.26$** marking a 3.6% increase bolstered by the OPEC+ alliance's plan to prolong voluntary oil output cuts. Conversely, **gold remained relatively unchanged**, registering a modest 0.22% increase. Meanwhile, **Bitcoin** sustained its upward trajectory, **propelled by robust demand from US exchange-traded funds (ETFs),** which substantially outpaced available supply. Notably, since the initiation of ETF trading on January 11, these funds have amassed a total of 300,000 bitcoins while newly issued supply in the same period was 44,000. As a result, Bitcoin concluded the month at $61,430, reflecting an **impressive 44.7% surge for the month** (see figure 2).

Figure 2: Bitcoin price last 5 years



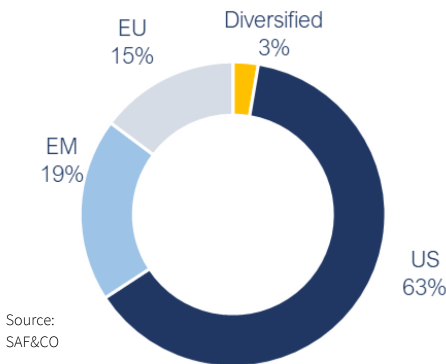
Source: : SAF&CO, Bloomberg

Asset allocation:

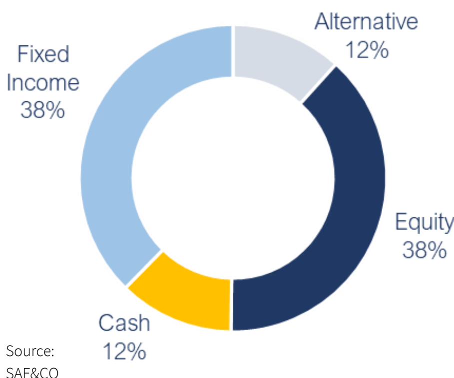
In February, there was a **marginal increase in the allocation towards the S&P500,** which currently stands at 16.5%, Our target allocation to equities remains at 40% as well as fixed income. Alternative investments account for 12%, and we aim to remain with cash allocation at around 8%, reminding that we benefit from a high yield on short term cash management. Geographically, **the portfolio maintains a predominant focus on the US market**, comprising 63% of the allocation, with Emerging Markets and Europe representing 19% and 15%, respectively. A modest proportion of 3% is diversified across other global markets (See Figure 4)

Figure 4: SAF&CO's Fund Allocation (as % of total portfolio)

Per Region



Per Asset Class



Equity:

The fund didn't make any major change in its equity allocation apart from some rebalancing, **it continues to be underweighted in equities with the target exposure at 40%.** This was reduced throughout the past year from 50% due to the increased attractiveness of fixed income and in order to take some profits. **We maintain a positive view** especially after the good earning season and the different catalysts that should pressure the markets higher, ie. the American elections and the rate cuts. Hence, The United States continues to present themselves as one of the premier destinations for capital allocation and our biggest exposure, underpinned by its resilient economy. As we near the conclusion of the earnings season (97% of S&P500 companies have disclosed their financial results), the prevailing trend of companies surpassing revenue and earnings growth expectations continues. Remarkably, 73% of S&P500 constituents have reported positive earnings per share (EPS) surprises, reinforcing the confidence in the market's underlying strength and potential. **We remain strongly overweight to the US in comparison to Europe** and we prefer to increase our exposure through indexes in the US instead of specific themes or sectors.

Fixed Income:

Throughout February, **the fixed income asset class experienced minimal changes**. **Spreads continued to narrow**, with investment-grade (IG) spreads in the US and Europe approaching 50 basis points, while those for emerging markets (EM) and European high yield (HY) reached approximately 300 basis points, and US HY nearing 350. **These levels are historically considered tight**, resulting in our fixed income portfolio outperforming our benchmark year-to-date (See figure 3 and 4). However, in light of these developments, it is prudent to consider reallocating, thereby reducing our spread risk exposure. **Currently, we are optimizing our portfolio, reducing exposure to our high yield and Emerging market bonds** where the spreads are very narrow. The portfolio's average rating stands at investment grade BBB, with a duration of 4.8 and a yield to maturity (YTM) of 6.8% and a spread of 272 bps. Compositionally, it consists of 42% investment-grade, 30% high yield, and 28% emerging markets securities.

Alternatives:

In February, the allocation within the alternative asset class remained steady. Year-to-date, all funds, save for our **Long-Short Equity Strategy**, have yielded positive returns. Despite the latter's underperformance, we have ascertained that it falls within the expected volatility and behavior of the strategy. They are still net short in technology and overweight small caps with comparison to large caps, as mentioned in our previous letter, this strategy is negatively correlated to our equity exposure. **Our absolute return strategy fund** delivered a notable return of +3.85% in February. Characterized by a historical volatility rate of 9.2% and exhibiting a negative correlation of -0.35 with the Equity asset class, this strategy effectively mitigates overall portfolio risk. While Equities represent a significant portion of its risk allocation at nearly 40%, it still present a diversified approach, with Fixed Income and Foreign Exchange components collectively accounting for over 40%.

Figure 3: Investment Grade spreads

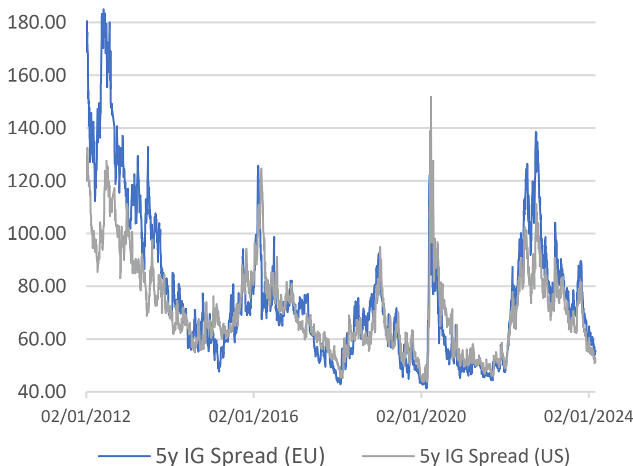
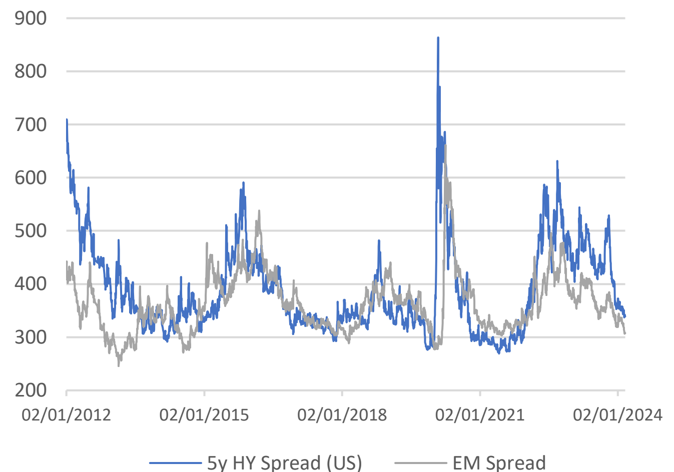


Figure 4: High yield and EM spreads



Source: : SAF&CO, Bloomberg

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