Perspectives
Financial Markets

SwissLife
Asset Managers

Annual outlook 2024

Interest rates & bonds
Investment grade bonds set to perform well in 2024

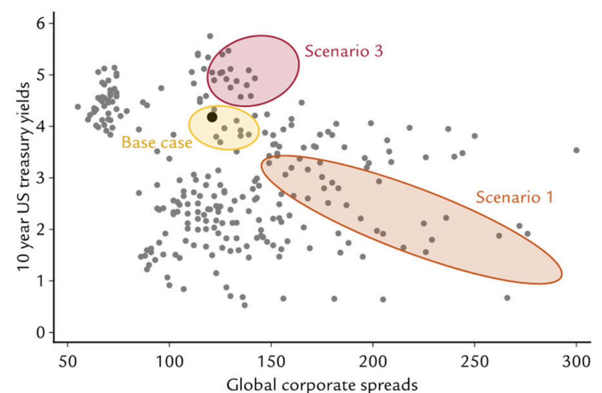
USA
- In the US, a downward revision in the expected supply of Treasuries, coupled with easing inflation and subdued economic growth data, has led to a sharp decline in rates and credit spreads in November.
- Given the anticipated decrease in growth and inflation, we expect the US Federal Reserve to cut policy rates in the course of 2024, a move that should be beneficial for corporate bonds despite slightly higher expected credit spreads.

Eurozone
- In the Eurozone, inflation has materially eased as the economy is stagnating. In response, the ECB has adjusted its messaging, which has contributed to lower government bond yields and credit spreads.
- With headline inflation approaching the ECB target and the economy still showing signs of weakness, the ECB may soon ease its restrictive monetary policy. We expect rates to fall over the course of 2024, with credit spreads expected to trend slightly higher.

UK
- While the UK has seen lower government bond yields similar to other major economies, its macroeconomic environment is less favourable. This is primarily due to core inflation remaining high at 5.7% in October, despite subdued economic growth.
- Among major central banks, we expect the Bank of England to be the last to cut rates, which constrains any recovery of the UK economy. Nonetheless, we expect a downward trajectory for interest rates, albeit less pronounced than in the US and the Eurozone.

Switzerland
- In Switzerland, inflation remains under control, and while economic growth is set to remain below potential in 2024, we do not expect a recession.
- The SNB is in a comfortable position to start reducing rates in 2024. This should support long-duration and risk-on positions in the Swiss bond market, given the attractive carry.

Spread and rate paths under different economic scenarios



In 2023 many investors were positioned for a US recession that ultimately did not materialise. Despite many challenges such as a banking crisis in the USA, geopolitical tensions, and a real estate crisis in China, the global economy was resilient and risky assets performed well. Year-to-date, credit spreads declined by around 20 basis points (bps), while government bond yields rose by about 30 bps in the US and fell by 40 bps in Europe. Due to high all-in yields, EUR and USD-denominated credit enjoyed solid returns of 6.3% and 5.2% respectively. In 2024, lower growth and inflation could set the stage for a global easing of monetary policies (base case). However, this is largely priced by markets, which could lead to significant volatility in rates and spreads if upcoming data deviated from that scenario. If both inflation and growth exceeded expectations, this could be detrimental for investors as spreads and rates would likely rise from current levels (scenario 3). Conversely, a global recession could still yield attractive returns, as any increase in credit spreads is expected to be counterbalanced by a more pronounced decrease in interest rates (scenario 1). In the current environment, investment grade credit is one of the most attractive asset classes. High all-in yields and the potential for lower interest rates, set against a generally benign economic backdrop, positions this asset class for potentially high total returns in 2024.

Equities

Excellent year in 2023 but lower expectations for 2024

USA

- The US market gained 24.7% so far in 2023 (all data as at 13 December) after a loss of 19.8% in 2022.
- This excellent performance is mainly due to the so-called "Magnificent 7" (i.e. the big tech stocks) which gained more than 100% due to an AI-hype.
- The performance of different equity styles varied a lot. An equally weighted composite of all stocks in the S&P 500 gained only 10% while value stocks were up 4.5% and high dividend stocks lost 1%. Small caps also trailed the broad index by 10%.
- We think that it is unlikely that the Magnificent 7 will have another great year and we note that the valuation of the US market is clearly expensive.

Eurozone

- Eurozone stocks advanced by 18.4% in 2023 after a loss of 12.5% in 2022.
- The good performance is much more broad-based than in the US. In Europe, value and growth stocks performed in line with the broad market.
- The valuation of the European market is low and the discount vs. the US market is very high. This valuation gap should become narrower at some point, but currently, a trigger for a convergence is missing.

UK

- The UK market only gained 5.0% in 2023 and is one of the weakest performers in the developed world.
- However, the UK market benefits from the lowest valuation and the highest dividend yield of all major developed markets.

Switzerland

- The Swiss market went up by 5.6% in 2023 and it lagged the global market by about 9% in CHF terms.
- Among the major stocks, Roche (-10%) and Nestlé (-5%) were especially weak. They account for around 29% of the Swiss Market Index (SMI).
- The Swiss equity market is the second-most expensive market after the US market.

Emerging markets

- Emerging Market equities were up 4.3% in 2023. The main detractor was China with a performance of -13.6% (in USD terms). China accounts for around 30% of the index.
- The market is around its fair value and earnings growth for 2024 is estimated to be around 18% – the highest of all major markets.

Valuation grid of global equities (current level 9670)

Price-Earnings Ratio	Expected Earnings Growth -20%	-15%	-10%	-5%	0%	5%	10%	15%	20%
10	4'203	4'466	4'728	4'991	5'254	5'516	5'779	6'042	6'304
11	4'623	4'912	5'201	5'490	5'779	6'068	6'357	6'646	6'935
12	5'043	5'359	5'674	5'989	6'304	6'619	6'935	7'250	7'565
13	5'464	5'805	6'147	6'488	6'830	7'171	7'513	7'854	8'196
14	5'884	6'252	6'619	6'987	7'355	7'723	8'090	8'458	8'826
15	6'304	6'698	7'092	7'486	7'880	8'274	8'668	9'062	9'456
16	6'725	7'145	7'565	7'985	8'406	8'826	9'246	9'667	10'087
17	7'145	7'591	8'038	8'484	8'931	9'378	9'824	10'271	10'717
18	7'565	8'038	8'511	8'984	9'456	9'929	10'402	10'875	11'348
19	7'985	8'484	8'984	9'483	9'982	10'481	10'980	11'479	11'978
20	8'406	8'931	9'456	9'982	10'507	11'032	11'558	12'083	12'609
21	8'826	9'378	9'929	10'481	11'032	11'584	12'136	12'687	13'239
22	9'246	9'824	10'402	10'980	11'558	12'136	12'714	13'291	13'869
23	9'667	10'271	10'875	11'479	12'083	12'687	13'291	13'896	14'500
24	10'087	10'717	11'348	11'978	12'609	13'239	13'869	14'500	15'130
25	10'507	11'164	11'820	12'477	13'134	13'791	14'447	15'104	15'761

Source: Bloomberg, Swiss Life Asset Managers. Last data point: 14/12/2023

Our macroeconomic outlook calls for softer US growth in the first half of 2024 and for declining inflation and interest rates in the developed world. Based on this economic outlook, we estimate that the global equity market has a realistic performance potential of 3-7% (total return including dividends) in 2024. Such a return is consistent with expected earnings growth and assumes that valuations stay broadly where they are currently. This positive view for the full year is based on our expectation that central banks will start to lower policy rates in the second quarter. Other points which speak for positive single-digit returns are the relatively low valuation of global stock markets outside the USA and the fact that stocks have historically done well when the US Fed ended the hiking cycle and only a shallow recession or a soft landing ensued. On the negative side, we currently have a very tight monetary policy stance and a valuation which does not take a potential recession into account. In addition, bonds and cash have become very attractive vs. stocks as their yields are now close to the earnings yield for stocks (primarily in the US). How much of a downside is there? The table above shows a grid with valuation (price-to-earnings ratio P/E) and earnings growth as variables. The currently expected earnings growth is around 10% while the current P/E ratio is around 18. Based on these two assumptions, the theoretical value of the global stock market is around 8% above the current level. If earnings growth was 5% (in our view the more realistic assumption) the fair value is around 3% higher than the current value. If the P/E ratio and/or expected earnings were to moderate, significant losses may occur. We have a neutral view over a 1 and 3 month horizon and a positive view for the full year 2024. The recent action by the US Federal Reserve is clearly positive, however the market has already appreciated a lot in anticipation of lower interest rates.

Currencies

"King dollar" regaining power in 2024

USA

- In 2023, the USD was very much driven by the ups and downs of monetary policy expectations and Treasury yields, ending the year with a mixed performance (all data as at 13 December). Among the losers in 2023 were currencies of commodity exporters, while Latin American currencies as well as CHF, GBP and EUR appreciated against the USD.
- We expect the USD to appreciate against most major developed market currencies in the course of 2024, despite the expected policy rate cuts by the Federal Reserve. Other developed market central banks except for the Bank of Japan are likely to ease monetary policy as well, and the interest rate advantage ("carry") generally remains in favour of the USD.

Eurozone

- The EUR appreciated slightly against the USD in 2023, but lost against GBP and CHF, leaving the trade-weighted exchange rate almost unchanged.
- We expect the EUR to remain weak in 2024 amid weak growth, falling inflation pressure and the resulting need to ease monetary policy.

UK

- Despite weak economic growth, GBP appreciated against USD and EUR as stubborn inflation pressures kept monetary policy settings very tight.
- In line with our view of a strong USD, we expect GBP/USD to weaken somewhat in 2024.

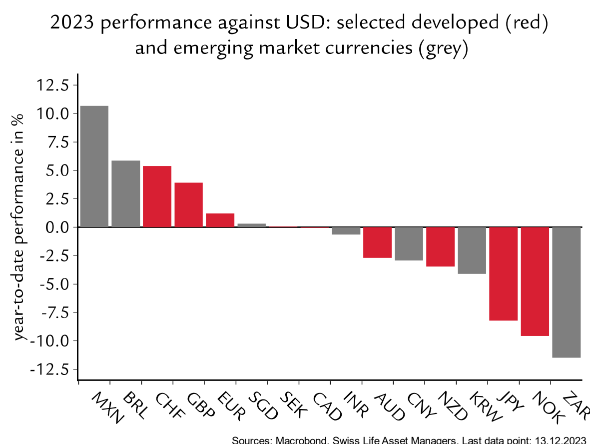
Switzerland

- CHF appreciated against all other developed market currencies in 2023.
- Despite the carry disadvantage of CHF, we see the downside risk to be very limited, as CHF likely remains the safe haven currency of choice.

Japan

- Apart from NOK, JPY had the weakest 2023 performance of all major currencies as the Bank of Japan stuck to its negative interest rate policy.
- We do not expect monetary policy to be normalised enough in 2024 to make the JPY an attractive proposition due its significant carry disadvantage.

2023: a mixed year for the USD



One year ago, we predicted that the "USD supercycle" would end in 2023, and indeed, after the year 2022 in which the USD outperformed almost all currencies, the 2023 performance table looks mixed for the greenback so far (see above). As in the year before, the Mexican peso (MXN) and the Brazilian real (BRL) topped the 2023 table, but CHF, EUR and GBP were the developed market currencies that slightly appreciated against the USD at the time of writing. For 2024, we have a constructive view on the USD. Even though we expect economic dynamics to weaken in the US in 2024, the economic state of Europe looks more problematic after one-and-a-half year of stagnation, while inflationary pressure has eased significantly. We thus think that the ECB is in a position to deliver slightly more policy rate cuts in 2024 than the US Federal Reserve, a scenario not entirely priced by markets even after the re-pricing caused by the dovish 13 December FOMC meeting. Interest rate differentials between the US and the Eurozone might thus widen in 2024. This "carry advantage" was a major support for the USD over the past years and is the main reason for our constructive view. This is also why we see the outlook for the JPY less positive than the consensus. Despite the expected abolition of the Bank of Japan's negative interest rate policy, the carry disadvantage against the USD remains significant, limiting the appreciation potential for JPY vs. USD. The carry argument weighs, however, less on the CHF than on JPY. The CHF was the safe haven currency of choice in 2023, and we think this is unlikely to change in 2024, where both economic uncertainty as well as (geo-)political uncertainty remains very elevated.

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