CARMIGNAC
INVESTING IN YOUR INTEREST

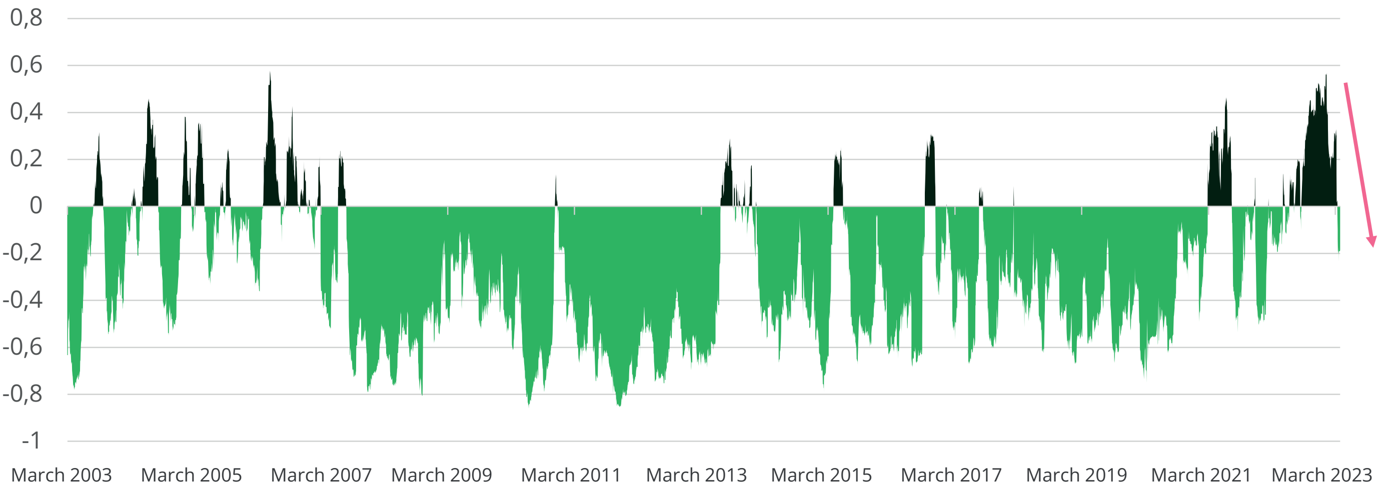
CARMIGNAC'S NOTE

ARE STOCKS AND BONDS ONCE AGAIN A WINNING COMBO?

Diversification should be among the guiding principles for investors in 2023

11/04/2023 | KEVIN THOZET

3-month price correlation between US stocks and 10-year Treasuries



Source: Carmignac, Bloomberg. 3-month correlation between the closing price of the S&P 500 and that of 10-year Treasury bonds future.

The first quarter of 2023 has been a hectic one, between hopes of a Goldilocks economy*, talk of a no-landing scenario, and upheaval in the banking sector. While the wide range of economic forecasts gave rise to significant financial-market volatility in first quarter, **stocks and bonds returned to a negative correlation**, right when investors needed it most – during a time of significant market stress.

Diversification and its benefits have made a comeback. While safe-haven assets had all but disappeared a year ago, today investments in core bonds are helping offset losses of risk assets in the wake of the turmoil in banking stocks. Financial markets had been administered by central bankers for years, and after a year of adjustment as monetary policymakers withdrew their unconditional support in 2022, it's the fundamentals that are again dictating movements in asset prices.

The current environment calls for investment portfolios that combine performance drivers (such as equities and credit) with sources of diversification (such as US and German sovereign bonds).

From a performance driver perspective, beyond the relief rally as investors saw that the banking-sector defaults were limited to some specific players, equities should continue to be supported in the coming months by the disinflation trend that began in the autumn. What's more, investors are particularly, if not excessively, conservatively exposed. The same applies in some segments of the credit market where spreads are already at levels consistent with a recession, meaning investors have priced in a deterioration in the economic outlook.

From a diversification perspective, the main factor that will eventually weigh on investors' risk appetite in the coming months relates primarily to the increasing recessionary pressure. Such bleak expectations will eventually weigh on stock and credit markets, but also fuel demand for defensive assets, thus supporting the prices of highest-rated bonds. On the other hand, recent cracks in the banking system (the failures of regional US banks and a large Swiss bank) and the slowdown in GDP growth are putting a cap on further rises in interest rates.

A window of opportunity has opened to invest in both stocks and bonds in the coming months, and it's important to seize it – especially since further developments could close that window down the line. The evolving energy equation and a pivot by the US Federal Reserve could erode the negative correlation between these two asset classes.

As active portfolio managers, we intend to proactively adapt our portfolio construction to the different phases of the economic cycle and pull together assets with complementary profiles, while effectively taking into account the potential for regime changes.

**A Goldilocks economy is one where GDP growth is neither too strong (so that it doesn't fuel inflation) nor too weak (so that it doesn't trigger a recession).*

Carmignac Gestion - 24 place Vendôme - 75001 Paris. Tél : (+33) 01 42 86 53 35
Société de gestion de portefeuille agréée par l'AMF. SA au capital de 15,000,000 € - RCS Paris B 349 501 676.
Carmignac Gestion Luxembourg - City Link, 7 rue de la Chapelle – L-1325 Luxembourg. Tél : (+352) 46 70 60 1
Filiale de Carmignac Gestion. Société de gestion de fonds d'investissement agréée par la CSSF. SA au capital de 23 000 000 € - RC Luxembourg B67549.