Valvest

Year-End Report 2017

Economy

Shares and the global economy had a good year in 2017. The majority of companies are doing well. Having posted record breaking revenues, while maintaining stable margins, we see increased corporate spending for the first time in two years. Stabilizing commodity prices have particularly helped to reverse the negative trend in expenditures in this sector. This is especially relevant as the commodity sector accounts for roughly 20% of total investments. Expenditures in the technological and industrial sector continue to grow. That is not only a consequence of the improved economic environment, but also due to the nearly infinite availability of inexpensive liquidity.

The historically low interest rates also have side effects. Europe's debt burden has temporarily been relaxed and the fragile European Union has stabilized. However, the low interest rate phase was not used to reduce the overall debt levels, which would have been possible thanks to savings on the interest cost side. Instead, the governing bodies inefficiently grew favoured by low interest rates. With Brexit, the referendum in Scotland or Catalonia and the election of President Trump, voters in various parts of the world are signalizing that they are no longer satisfied with their governments.

In Switzerland, government debt is not the problem. However, the Swiss National Bank (SNB) has been forced to weaken its currency by massively buying foreign currencies and securities. These foreign funds have in the meantime made their mark on the balance sheet, so that the SNB could be seen as the largest hedge fund in the world. Future generations could profit from these investments, similarly to the Norwegian state fund. Unfortunately, a large part of bonds are Euro denominated, whose structural problems are likely to lead to losses in value in the future.

While companies have largely made use of the low interest rate environment to structurally improve their business, the opposite can generally be said for governments. It is undisputed that record-low interest rates over several years stimulate the economy, investment and consumption, but also encourage excesses. Rising interest rates will yet have to fully unveil the latter.

Continuing global economic growth and rising commodity prices have stabilized both inflation and interest rates in the key economic regions. With no signs of a slowdown in economic growth, we expect both to continue to rise slightly.

Conclusion

Even with interest rates rising slightly, we remain in a low interest rate environment. In combination with rapid technological advancement and persevering globalization, these factors will continue to shape the economic environment in 2018. This is positive for equities.

In view of this environment, we generally consider the valuation of the stock market to be appropriate. The undervaluation of technology stocks at the beginning of last year, which we had mentioned in our July review, has been somewhat adjusted due to the outperformance of the sector. However, given the sustained potential, we still consider the sector very interesting.

In the current environment, our active investment approach continues to allow us to find attractive valuations thanks to the individual analysis of each sector and company. Shares thus remain our preferred investment class for 2018.

Zurich, January 2018