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MIRABAUD

MONTHLY NEWSLETTER
MIRABAUD WEALTH MANAGEMENT

Guilherme Barbosa
Investment Director

INTERNATIONAL

AND THE WINNER IS... SWITZERLAND

Last month we wrote about the impact of (mis)politics and how many developed countries have been trying to spend their way to buy without worrying about the subsequent fiscal impact.

Switzerland was ignored in last month's letter because the government runs prudent fiscal and monetary policies and has taken a different policy path. Boring, but good! And when you take a deep dive into the Swiss economy, it is far from boring and it's not only good, but great ! Before focusing on Switzerland, let's start with some negative news which is basically markets' performances in October.

The month brought us negative returns in equities and bonds with higher volatility due to the Presidential and Congressional elections in the United States. For US dollar based investors, the only safe haven during the month was the US dollar itself and gold.

The precious metal has risen during 8 out of the first 10 months of the year and is up 33% year-to-date. Global equities are delivering an above -average year and the usual tough September-October period was much better than feared with the S&P 500 rising 1% over two months and we should not forget that the index has risen 38% in the past twelve months.

Bonds struggled in October with higher yields in the USA as the economy continues to show strength and expectations of a Trump victory which may lead to higher growth and inflation.

« (…) WE ARE IN A SOFT LANDING SCENARIO WHICH WILL BE FOLLOWED BY AN EARLY CYCLE RECOVERY.»

PERFORMANCE OF THE MAIN FINANCIAL INDICES:

	Out.	Out.$	2024	2024 $	2023	2023 $	2022	2022 $	2021	2021 $
S&P 500	-0,92		21,0		26,3		-18,1		28,7	28,7
Stoxx 50	-3,30	-5,78	10,1	8,1	23,2	27,3	-8,5	-14,0	24,1	24,1
MSCI EM	-4,32		12,1		10,1		-19,9		-2,3	-2,3
SMI	-3,09	-5,42	9,3	6,0	7,1	17,6	-14,3	-15,0	23,7	19,5
Euro - USD	-2,25		-1,4		3,1		-5,8		-6,9	
US Dollar Index	3,17		2,6		-2,1		8,2		6,4	
Gold Spot - USD	4,15		33,0		13,1		-0,3		-3,6	
CHF - USD	-2,14		-2,6		9,9		-1,3		-3,0	
Global Aggregate	-3,35		0,1		5,7		-16,2		-4,7	
US Aggregate	-2,48		1,9		5,5		-13,0		-1,5	
US Treasury	-2,38		1,4		4,1		-12,5		-2,3	
US T Bills	0,37		4,5		5,1		1,3		0,0	
Global High Yield	-0,63		8,9		14,0		-12,7		1,0	
Euro Aggregate	-0,75		1,7		7,2		-17,2		-2,9	

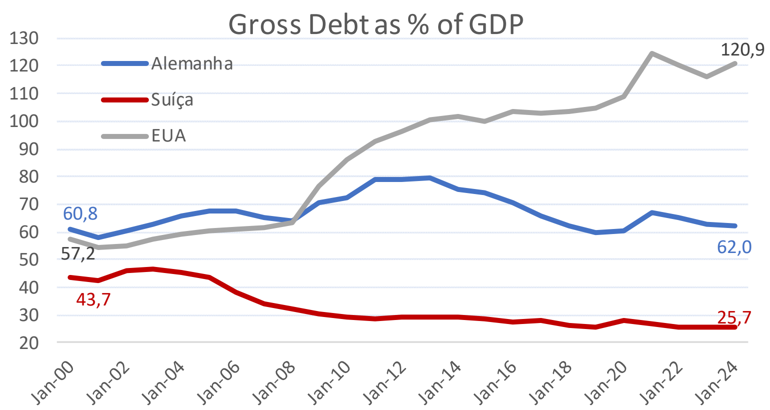
Before we speak about our views on the US elections, let's go back to Switzerland.

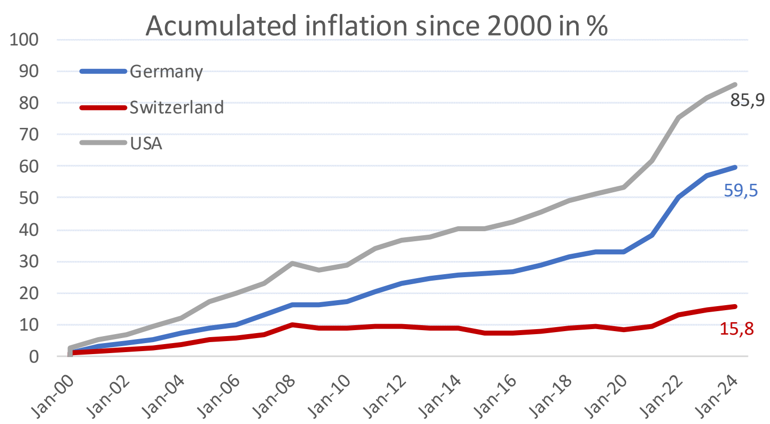
One of the things that amazes people the most when I speak about life in Switzerland is the fact that I have been living here for almost 20 years and the price of my haircut has not changed! Yes, you read that correctly. The cost of the annual highway toll has also not changed since 1995 and costs slightly more than my haircut which may explain why the highways are in a much better shape than my thinning hair.

At end of the gold standard in 1971, countries allowed their currencies to float which was has led to much higher debt levels and inflation globally. Switzerland did not follow this trend (you can see by the charts below which only go back to the year 2000) has been in place for over 50 years.

The Swiss inflation rate since 1971 has averaged only 2.14%! Back in 1971 (when I was born), one US dollar was worth about 4.3 Swiss Francs and the Suissie (FX trader lingo) had appreciated to 1.25 when I moved to Switzerland in 2005 and continued to appreciate to today's level of 0.86.

So my haircut costs the same in Suissie, but it has become 45% more expensive in US dollar terms. One could argue that my barber is practicing "shrinkflation" as he is charging the same amount of money, but is cutting fewer hair.





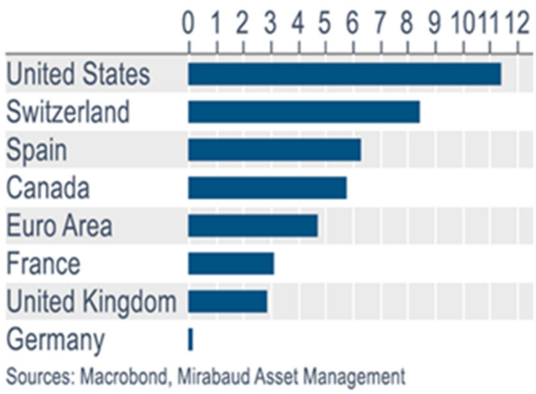
How does a country survive with such a strong currency and low fiscal expenditures?

Surely it is different to grow with such restraints, however, the "Safe Haven" country is also a growing economy when compared to other major European and North American countries (see chart below).

Education, innovation and the population are also actively involved in politics. Education leads to a highly qualified labor force. The steady appreciation of the Swiss franc forces the Swiss supplier and export sectors to be more innovative and more productive year in year out. Quality is the key differentiator of Swiss companies and products. The Swiss population votes on referendums about four times per year to approve decisions taken by the local, regional and federal governments.

So voters not only choose their politicians, but also vote on many important matters. Later this month Swiss will vote on whether to accept the extension of the highway grid and the Geneva population will vote on whether lowering personal income taxes.

Cumulative GDP growth since Q4 2019 (includes Covid):



And the Winner of the US election is… Trump

Most market participants and US voters were hoping for a quick and unquestionable result.

Any quick result is better than a repeat of the 2000 election when Democratic candidate Al Gore conceded on December 13th, thirty-six days after the election date and after having won the popular vote.

The 2024 Presidential election was a close-call and the Congressional election was also very close. Due to the election uncertainties and to protect portfolio performance, we reduced exposure to the US equity markets at the end of October.

The main reasons were that we expected more volatility and valuations were already at very high levels.

We keep our view that we are in a Soft Landing scenario which will be followed by an early cycle recovery.

On the monetary policy front, we expect the FED to cut rates by 25 basis points when it meets in November and again in December and moves in 2025 will depend on policies implemented by the new Administration.

Expected Market behavior after a Republican Sweep:

US ELECTIONS SCENARIO	Republican Sweep	
Macro Impacts	Inflationary Pressures	+
	US Fiscal Deficit	+
	Global Trade Growth	−
	World ex-US GDP Growth	−
	US GDP Growth	+
Financial Markets Impacts	US Equities	++
	EM Equities	−
	US Bonds	−
	EM Bonds	−
	Dollar	+
	US Small Cap	+
	US Industrials	+
	Clean Energy	−

Eric Hatisuka
CIO Mirabaud Brazil

BRAZIL

"LIFE CAN ONLY BE UNDERSTOOD BACKWARDS, BUT IT MUST BE LIVED FORWARDS" (SOREN KIERKEGAARD)

Kierkegaard (1813-1855), Danish philosopher, theologian and poet, considered the first existentialist philosopher, postulated that life, as an individual and unique experience for each person, should be lived realistically and concretely, in opposition to the naive idealism of Hegel and other philosophers of his time (note: do not confuse Hegel with Engels).

Kierkgaard proposed that "in the face of life's uncertainties, our choices will always be 'utilitarian'", which led to his concept of the "leap of faith": the most important decisions in our lives are made under complete uncertainty and can only be fully justified a posteriori.

In recent days, with the dollar-real exchange rate close to R$5.90 and interest rates on NTN-B's reaching 7% per year, I was reminded of Kierkgaard and his approach to decisions under uncertainty.

Making decisions under uncertainty is the job and the challenge of everyone who works with economic analysis, investments and financial markets and, as Nassim Taleb asserts throughout his seminal trilogy (Fooled by Randomness, The Black Swan and Antifragile), the useful tools for analyzing and making decisions under uncertainty do not lie in the economic sciences - or even in mathematics or statistics - but in the field of philosophy.

Taleb found his way into the Bed of Procrustes, Sextus Empiricus and the infamous barbell strategy. I, for my part, find some comfort in the thought of Kierkgaard and his cynical realism.

Life can only be understood backwards (…)

Since the implementation of the Brazilian macroeconomic tripod, i.e. inflation targets, a floating exchange rate and a balanced primary result for the public sector, NTN-B rates (sovereign bonds indexed to the IPCA) only reached their current levels of 7% per year during the institutional crisis of the Dilma Government, between 2015 and 2016.

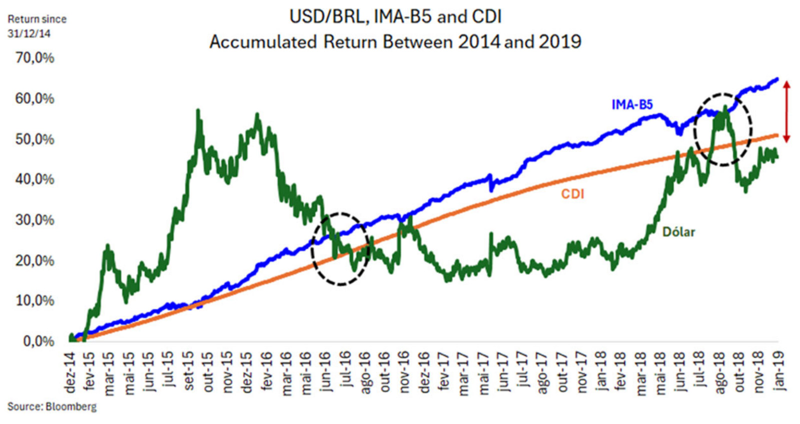
« (...) EVERY LEAP OF FAITH IS, IN FACT, A UTILITARIAN DECISION, WHICH IN OUR CASE IS BACKED UP BY THE HIGHEST LEVEL OF REAL INTEREST RATES IN ALMOST 10 YEARS »

In that two-year period of acute fiscal crisis, we experienced a harsh currency devaluation, alongside a huge loss of popular and congressional support for the newly re-elected Government, which was ultimately ousted through a noisy impeachment process in 2016.

As a result of the crisis, the country suffered the biggest recession in its history, with an accumulated drop of more than 7.5% in GDP between 2015 and 2016, showing that the country's new Achilles heel was definitely the fiscal balance, and no longer the external vulnerability that had plagued our economy in the 80s and 90s.

Between the end of 2014 and the beginning of 2016, the Real fell approximately 52% against the Dollar (from R$ 2.66 to R$ 4.04), but with the rise in inflation, interest rate hikes and fiscal stabilization that followed, the devaluation process was halted and those who invested in CDI and short-term NTN-B's during the period were also rewarded.

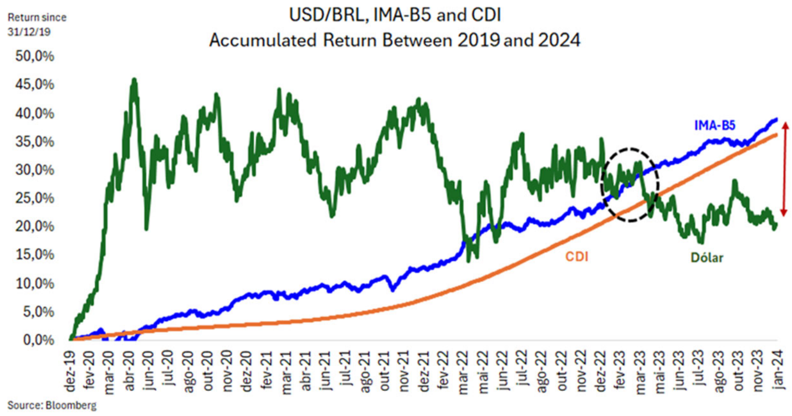
The graph below shows how, at the end of the 4-year period, the accumulated return on the CDI and the IMA-B5 (a theoretical portfolio made up of NTN-B's with up to 5 years to maturity, i.e. short-term NTN-B's) were equivalent to the return on the dollar.



Similarly, in 2020, with the shock to the markets caused by the closure of global economies in the advent of the Covid-19 pandemic, the Real fell approximately 30% against the Dollar (from R$ 4.02 to R$ 5.20) in the calendar year.

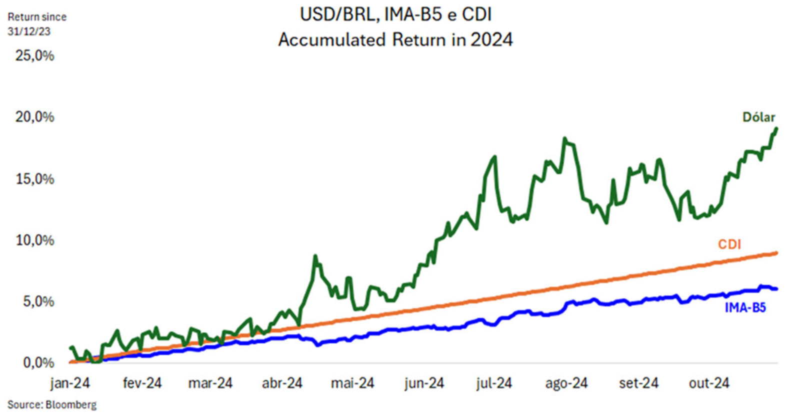
Unlike the 2015/16 episode, the 2020 devaluation was caused by a global (health) crisis, and even so, after the shock period, with the increase in interest rates needed to contain the inflationary effects of the economic disruptions, the return on the CDI and IMA-B5 ended up rewarding those who stayed invested in these assets for the period.

The graph below shows how, at the end of the 4-year course, the accumulated return of the CDI and the IMA-B5 were equivalent to the return on the Dollar, and even surpassed it at the end of 2023.



Now, in 2024, in the face of a new prospect of fiscal lack of control, the Real is once again devaluing against the dollar, as can be seen in the graph below, shorter than the previous ones.

As in previous episodes, at first the dollar rises, responding to the perceived increase in the country's risk of insolvency; then, with the pass-through of the currency devaluation to imported prices, the IPCA rises, increasing the return on NTN-B's, then causing basic interest rates and the CDI to rise, which follow in its wake.



(...) but it must be lived forwards.

Much has been said about the disciplining power of financial markets over governments. In fact, the more sophisticated and developed the economy, the greater the impact of public policies on the markets and the greater the cost in terms of popularity for governments when the markets deteriorate.

The recent devaluation of the Real against the Dollar is yet another eloquent sign that the markets are losing patience with the government and its preference for fiscal leniency.

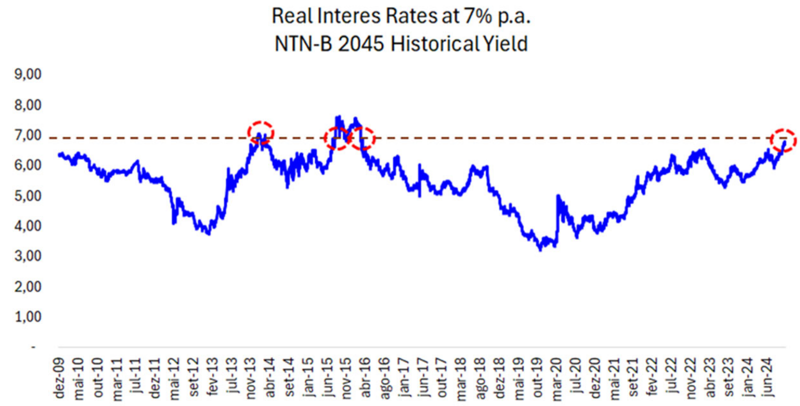
With two years to go until the 2026 general elections, there is more than enough time for the rise in the dollar to contaminate inflation, economic activity, productive investment and the labor market, which would leave the government in a very fragile position in the face of its run for re-election.

It is imperative that the government begins to address solutions to the country's fiscal problems, under the threat of facing a much tougher electoral contest if the economic fundamentals deteriorate before then.

As already mentioned, real interest rates on NTN-B's have reached 7% per year, which is comparable only to the worst period of the Dilma Government, in yet another sign that things are not going well for the current Government.

This is the moment of the Kierkgaardian leap of faith: rational logic leads us to believe that the Government no longer has the political and economic space to continue evading the fiscal framework. However, uncertainty remains, because we know that the Government (like any government) would like to be able to spend unlimitedly and infinitely.

As Kierkgaard proposed, every leap of faith is, in fact, a utilitarian decision, which in our case is backed up by the highest level of real interest rates in almost 10 years (graph below).



"Our life always expresses the result of our dominant thoughts". (Soren Kierkegaard)

The recently confirmed election of Donald Trump to the presidency of the United States has become an additional factor of uncertainty for the Brazilian economic scenario, especially because of his protectionist trade policy and his predilection for a deficit fiscal policy.

With the also confirmed 'red sweep', i.e. the formation of a Republican majority in the House and Senate, it is expected that we will have two years of 'Trumponomics' in full swing.

As expressed in our February Monthly Letter, Trump's economic playbook in his previous term, or 'Trumponomics', was deficit prone, protectionist and inflationary; factors that, combined, tend to generate higher interest rates and a stronger dollar, with deleterious implications for the flow of capital to emerging economies in general, and to deficit run countries like Brazil in particular.

Brazil is not currently dependent on external financing, which puts us at risk, but if our fiscal policy continues on a path of open deficits, this dependency will arise.

It has become more urgent than ever for the Government to resolve once and for all the doubts hanging over the markets about its commitment to fiscal balance.

The Trump administration will not be an obstacle to Brazil's development, but it will certainly reduce the room for leniency, carelessness and miscommunication.

PERFORMANCE OF THE MAIN FINANCIAL INDICES:

Renda Fixa		31/10/24	MTD	3M	YTD
CDI	-	84,50	0,93%	2,53%	8,99%
IMA-B	-	9.923,22	(0,65%)	(2,08%)	0,16%
IMA-B 5	-	9.522,69	0,74%	1,02%	6,08%
IMA-B 5+	-	11.113,63	(1,66%)	(4,11%)	(4,23%)
IRF-M	-	18.682,14	0,21%	0,54%	4,12%
IMA-S	-	6.981,87	0,98%	2,64%	9,26%

Índices Globais	País	31/10/24	MTD	3M	YTD
Ibovespa	BRL	129.713,33	(1,60%)	3,55%	(3,33%)
Dow Jones	USD	41.763,46	(1,34%)	7,91%	10,81%
S&P 500	USD	5.705,45	(0,99%)	10,01%	19,62%
NASDAQ	USD	19.890,42	(0,85%)	11,15%	18,21%
Euro Stoxx 50	EUR	4.827,63	(3,46%)	5,60%	6,77%
FTSE 100	GBP	8.110,10	(1,54%)	1,27%	4,87%
MSCI Emerging	EM	44,45	(3,07%)	9,97%	11,31%
MSCI World	World	3.647,14	(2,04%)	9,11%	15,08%

Moedas	País	31/10/24	MTD	3M	YTD
Dólar/Real	USD	5,79	(6,20%)	(1,13%)	(19,16%)
Euro	EUR	1,09	(2,25%)	(0,62%)	(1,40%)
Franco Suíço	CHF	0,86	(2,14%)	(1,38%)	(2,63%)
Libra Esterlina	GBP	1,29	(3,56%)	0,96%	1,32%
Bitcoin	BTC	69.937,51	9,65%	28,57%	66,77%

Hedge Funds	País	31/10/24	MTD	3M	YTD
Ind. de Hedge Funds	BRL	5.216,53	0,29%	2,14%	3,92%

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