Marketing Material

MONTHLY HOUSE VIEW

March 2024

No landing?

Architects of Wealth

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NO LANDING?

Delphine
DI PIZIO TIGER
Global Head
of Asset Management

Dear Reader,

The S&P 500 – the flagship US equity index – topped 5'000 on 9 February, up more than 5% since the beginning of the year. Corporate earnings were better than expected and the economy is showing remarkable signs of strength and resilience. The market had expected job creation to slow to less than 200'000 in January, but the final figure came in at more than 350'000. Employment remains strong. This seems counterintuitive, particularly when the press is laser-focused on jobs lost because of the artificial intelligence (AI) revolution. And yet, the United States managed to create jobs, even with more than 30'000 AI-related layoffs (source: Layoffs.fyi) since the beginning of the year. Almost all sectors were hiring with the exception of mining and gas extraction. We note, for example, that chemical manufacturers hired nearly 7'000 people in January, the sector's strongest growth since 1990.

Real growth (excluding inflation) in the United States was an annualised 3.3% in the last quarter of 2023, and inflation came down to 2.6%[1] in December, close to the central bank's target of 2%. This decline in inflation is somewhat deceptive, however, as it was due mostly to volatile components such as food and energy which, when removed, lift the figure to 3%. This nevertheless led the markets to expect the Federal Reserve (Fed) to cut rates sharply this year, which lends weight to the US growth and market support argument.

The United States owes its robust post-COVID growth, at least in part, to its use of credit. While US public and private debt has almost doubled in 10 years and is approaching 100 trillion dollars, companies are now facing a negative scissors effect: higher costs with the end of free money (their debt stands at more than 20 trillion dollars) and a slowdown in the upward trend in profits.

In addition, the strength of manufacturing activity, boosted by measures to relocate strategic activities (IRA[2] and CHIPS Act for America[3]), is faltering and market leaders like TSMC and Intel have delayed the opening of their US plants by up to two years. The subsidies promised by the government have been slow to materialise.

On the demand side, the US consumer has been extraordinarily resilient, driven by real growth (excluding inflation) in wages, even though the additional savings accumulated post-COVID are now mostly spent. It is consumption in China that is raising questions in a depressed economic environment, where the liquidation of real estate giant Evergrande that was ordered at the end of January has added to the negative pressure.

Naturally, there are opposing forces that affect US growth, and the possible re-election of Donald Trump could be one of them. The good news is that, by being provocative now, with his talk of implementing a tariff of at least 60% on Chinese products and encouraging Russia to attack NATO member countries that have not met their military spending target, he is motivating Europeans to react and remain united.

AI is the driver that will remain resilient no matter what. According to a recent BCG survey, 89% of executives rank AI as a top tech priority for 2024. Capital expenditure expected by the market this year is at an all-time high for US tech giants, i.e. nearly 300 billion dollars for the "Magnificent 7"[4]. I hope you enjoy this issue, which takes a deep dive into the strength of the US economy.

1 - Personal Consumption Expenditures.
2 - Inflation Reduction Act.
3 - The CHIPS Act for America is a US federal law that provides funding and incentives to increase domestic semiconductor production and research.
4 - The "Magnificent 7": Apple, Alphabet, Microsoft, Amazon, Meta, Tesla and Nvidia.

WHY IS THE US ECONOMY SO ROBUST?

Nicolas MOUGEOT
Head of Investment Strategy
& Sustainability

The US economy has surpassed even the most optimistic forecasts from last year and is expected to remain strong this year. The primary contributor is undoubtedly the resilient US consumer, who remains healthy despite a 500 basis points (bps) rate hike by the Fed.

USD 500 BILLION
of excess savings left?

The Fed seems poised to achieve a soft landing, taming inflation while sidestepping an economic recession. This contradicts economic theories suggesting that in order to lower inflation, central banks raise rates to increase borrowing costs, subsequently reducing economic activity. Despite this, while inflation is decreasing, the US economy grew by 2.5% in 2023 and could expand by 3.3% (quarter-on-quarter) in Q1 2024, according to the Nowcast GDP indicator of the Federal Reserve Bank of New York. How can we explain this strength when the Fed has been tightening since March 2022, increasing its target rates by more than 5%, contrary to conventional economic wisdom? The key to this robust US economy lies in the resilience of the US consumer, bolstered by several favourable factors.

IT'S ABOUT EXCESS SAVINGS

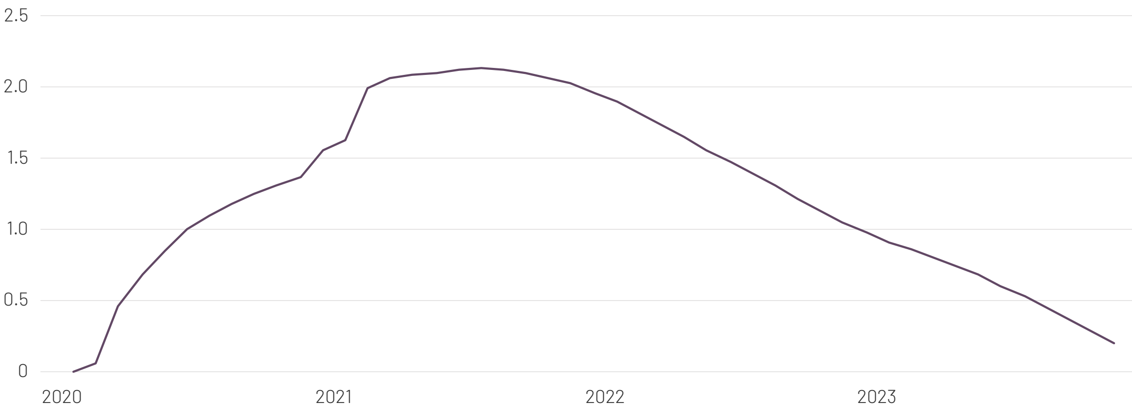
Firstly, US consumers accumulated excess savings during the COVID-19 era, spending less and benefiting from accommodative fiscal policies such as student loan forgiveness and stimulus checks.

As shown by Chart 1, economists at the San Francisco Federal Reserve estimated this excess savings reached over USD 2.1 trillion in August 2021 and has been diminishing since then. We estimate there is still approximately 500 billion of excess savings left, which should progressively vanish by year-end.

IT'S ABOUT WAGE GROWTH

Secondly, the US job market remains robust, with an unemployment rate at 3.7%, close to its lowest level in the past 50 years. This strength empowers US workers to demand wage increases. Nominal annual wages have risen by 4.5% over the past 12 months, outpacing the 3.4% increase in the headline CPI. This 1.1% real wage increase allows US workers to continue saving.

CHART 1: US CUMULATIVE AGGREGATE EXCESS SAVINGS



Source: Bureau of Economic Analysis, Federal Reserve Board of San Francisco, Indosuez Wealth Management.

85 %
of mortgage fixed for 30 years

These last two factors are pivotal for US economic growth, as when it comes to consumption, boomers and Gen X matter most. Chart 2 illustrates that Americans aged 45 to 55 are the highest spenders and earners, followed by the 34-44 and 55-64 age groups.

IT'S THE MORTGAGE MARKET AND THE GEN X

A third factor is the transformation of the mortgage market. Before the mortgage debt crisis of 2008, variable mortgage rates constituted about 30% of the US mortgage market. By 2021, less than 3% of mortgage applications were for variable-rate mortgages, with 85% of mortgages in 2022 fixed for 30 years. According to the Bureau of Economic Analysis, the effective rate of interest on outstanding US mortgage debt is only 3.8% on par with levels seen prior to COVID-19 crisis and well below the 7%+ rate on new mortgages. Consequently, US consumers with mortgages are less sensitive to rate fluctuations than 15 years ago and may have not changed their consumption habits despite the 500 bps rate hike by the Fed.

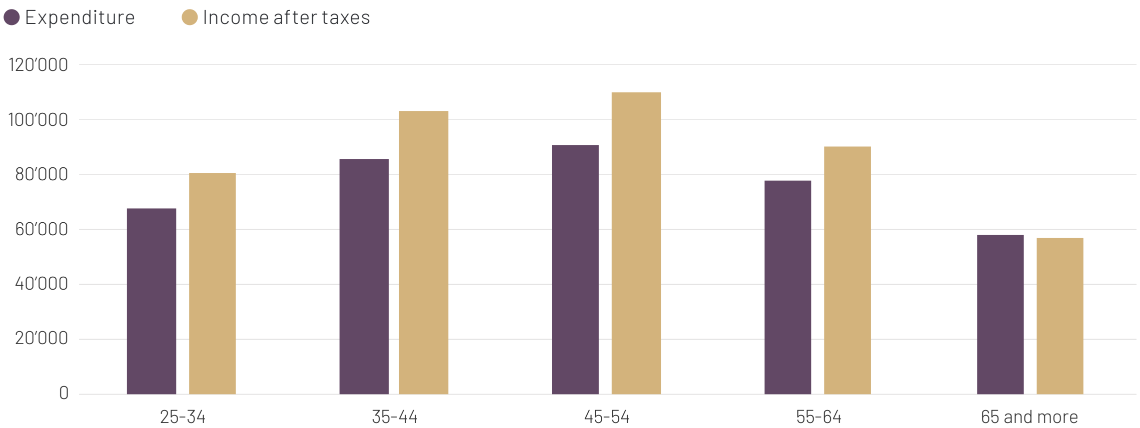
IT'S THE BOOMERS TOO

Lastly, higher rates could stimulate some US citizens to consume more. While that may sound counterintuitive at first, Nobel Prize Robert Merton and Arun Muralidhar argued in 2015:

"An alternate, more sophisticated approach to explaining why QE (quantitative easing) may not work to stimulate aggregate consumption is, perhaps, because the demographic mix of the US (and most parts of the developed world) has shifted toward older people. Unlike 30 or 40 years ago, the enormous baby boomer generation, and even retirees, are much wealthier (including human capital) than in the past, and they are wealthier than current generations earlier in their life cycle. Since the older cohort would surely assign higher importance to funding retirement, the funded status effect is more pronounced. When long rates go down, baby boomers start saving more instead of consuming, driving asset prices even higher (especially for risky assets, but not housing assets which they already own). So the wealth effect does not lead to an increase in consumption and, potentially, has the opposite outcome." Therefore, as long rates have increased, baby boomers should be less concerned of the funding status of their pension, save less and should consume more.

What to expect ahead? Overall, the excess saving may fade away sometime this year but the latter three arguments could hold up well. If this holds true, the US consumer would stay healthy and the US economy could remain robust, hopefully surprising us to the upside.

CHART 2: US TOTAL AVERAGE EXPENDITURE AND INCOME AFTER TAXES, BY AGE GROUP, USD



Source: US Bureau of Labor Statistics, Indosuez Wealth Management.

SO FAR, SO GOOD

Lucas MERIC
Investment Strategist

Inflation's return to around 3% seems to soothed the market. That said, US growth continues to outperform at a time when sticky services inflation and a solid labour market are highlighting the risks that persist in a reacceleration of the US economy. This strength is not, however, expected to hamper the ongoing disinflation trend.

NO TIME TO LAND…

As we wrote in our Global Outlook 2024, we anticipate a no-recession soft landing for the US economy in 2024. However, the latter exceeded all expectations in the second half of 2023 with annualised growth of 4.1%, while core PCE inflation hovered at 1.9% on a six-month annualised basis in December 2023. Consumption, the main driver of this resounding growth, accelerated by nearly 3% (annualised) in the second half of 2023, and for good reason: US consumers have benefited, since 2019, from a vast improvement in their purchasing power and net worth thanks to significant wealth effects on the financial and real estate markets. At the same time, the labour market remains extremely resilient and financial conditions have not been this loose since mid-2022. This consumer dynamism has led us to adopt an even more positive outlook for US growth and to revise our growth expectation to an annual average of 2.3% (+90 basis points) in 2024. Our high growth forecast also reflects a significant carry-over effect in 2024: zero growth in US GDP in the next four quarters would still bring the annual average to 1.3% in 2024.

We are REVISING US growth for 2024: 2.3% (+90 BPS)

…BUT THE SPECTRE OF A REACCELERATION LOOMS

The US economy is therefore expected to remain robust in the coming quarters, a trend that is bound to raise questions about the emergence of a possible reacceleration risk at a time when the labour market is still historically tight and the latest job creation, wage and inflation data have surprised sharply to the upside. In particular, where most of the components of inflation have decelerated significantly since peak inflation in 2022, thanks to the unwinding of major post-pandemic imbalances, services inflation continued to hover at 5.4% year-on-year in January 2024.

More specifically, services inflation excluding the housing component (which is lagging and does not yet reflect the decline in rents seen in the last few months in the United States) remains relatively sticky at 3.6% (year-on-year). In the context of robust growth and a resilient labour market, upside risks to wage inflation persist and could curb the ongoing disinflation in the services sector, where the wage bill represents 30% to 50% of companies' revenues. In that case, the last mile to the 2% target could prove more difficult and push the Fed to take a more restrictive stance. This is despite the pivot that began at the end of 2023, even as the markets have seemingly, since the beginning of the year, given little credence to a no-rate-cut scenario in 2024.

FURTHER DISINFLATION STILL IN SIGHT

However, despite these risk signals, we still believe that inflation will continue to decelerate throughout the year while remaining above the Fed's target, with average annual inflation of 2.6% in 2024 and 2.4% in 2025. In parallel with this disinflation, the fed is expected to start cutting rates in Q2 2024, to avoid increasing the restrictiveness of its monetary policy because of automatically higher inflation-adjusted rates, thereby justifying a scenario of 100 basis points (bps) of rate cuts in 2024.

In particular, we expect services inflation to drive much of the disinflation in 2024. First, the housing component of services inflation (which accounts for one-third of total inflation) tends to track rental prices with a one-year lag. The latter had climbed nearly 16% (year-on-year) in 2022 before decelerating to around 3.5% (year-on-year) since then. This trend is reflected with some delay, which should drive the first leg of disinflation. Second, job creation surprised sharply to the upside in January, due mainly to seasonality, but the trend is clear: for several months, job creation has been driven mostly by non-cyclical sectors (government and healthcare) and companies continue to reduce the number of hours worked (a dynamic that tends to precede staffing cuts).

We therefore expect this deceleration trend in the labour market to continue in 2024, particularly as it appears to be nowhere near as tight as in 2022, when there were still nearly two jobs available per unemployed worker; this figure now stands at 1.5. This more accomodating market is reflected mainly in the sharp drop in the quits rate in the private sector and the normalisation of the pay increase gap between job switchers and job stayers. This rebalancing of the market should help ease pressure on wages, which also remain a function of actual and expected inflation. These have both decelerated sharply in recent quarters, which should also ease upward pressures.

We therefore expect wage dynamics to continue on the slowing trend seen in the Fed's preferred wage measure (the Employment Cost Index), which stood at 4.3% (year-on-year) and 3.6% (on an annualised quarterly basis) in the fourth quarter of 2023, just above the 3.5% level that Jerome Powell views as consistent with keeping US inflation at the 2% target. Moreover, given the sustained productivity that characterises the US economy, unit labour costs remain relatively contained (and even stagnated in the second half of 2023), thus enabling companies to maintain their profits without necessarily passing wage increases on to prices and thereby limiting inflationary pressures.

TABLE 1: MACROECONOMIC FORECAST 2023 - 2025, %

● Revised down since last month ● Revised up

	GDP			INFLATION		
	2023	2024	2025	2023	2024	2025
United States	2.5%	2.3%	1.7%	4.1%	2.6%	2.4%
Euro Area	0.5%	0.6%	1.2%	5.4%	2.5%	2.4%
China	5.2%	4.5%	4.2%	0.2%	1.3%	1.6%
Japan	1.9%	1.1%	1.5%	3.3%	2.0%	1.5%
India	6.5%	6.0%	6.0%	5.7%	5.9%	6.0%
Brazil	3.0%	1.3%	2.0%	4.6%	4.0%	3.5%
World	3.0%	2.8%	2.7%	-	-	-

Source: Indosuez Wealth Management.

INFLATION CONTINUES TO SURPRISE

Thomas GIQUEL
Head of Fixed Income

With the contribution
of the Fixed Income Team

With the Chinese New Year and the presidential elections in Indonesia now behind us, Japan's new fiscal year will be the last event on the calendar before the European elections in June. This gives the markets time to return to basics: the economy and anticipating future trends.

USD 188 BN & EUR 354 BN: investment grade issues shatter records

UNITED STATES: A TOUCH-AND-GO[5] ECONOMY

In keeping with the Monthly House View for January and February of this year, the fixed-income markets continue to reduce their US Federal Reserve (Fed) rate cut expectations.

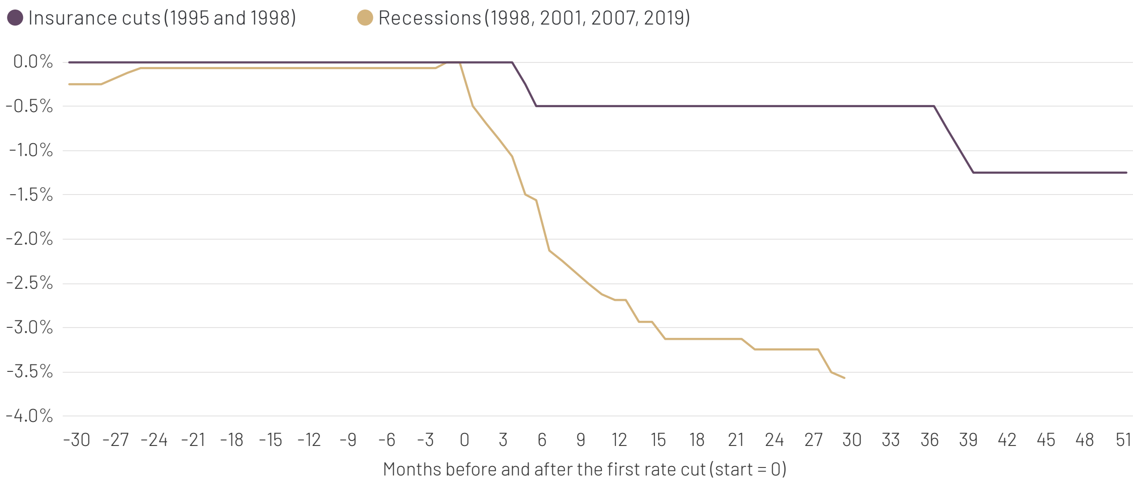
As you saw above in this month's focus, the US economy is showing no tangible signs of slowdown. However, if we look at changes in interest rates over a several-month period, we get the feeling that the world has changed. In October, the market was expecting US short-term rates of 5% at end-2024 and an implied default rate of 6% in US high yield. Today, year-end rates are close to 4.5% and risk premiums have normalised.

Inflation seems to have stabilised at around 3%, leading indicators point to a reacceleration of the economy, and there have been no lulls in the labour market.

In terms of portfolio management, we continue to anticipate four rate cuts this year. Unlike rate cut cycles that have occurred in recession periods, the coming cycle could be a plateau, or insurance cuts (Chart 3) on a smaller scale than in the past.

The narrowing of risk premiums and declines in long-term rates in the market have done some of the Fed's work. We began the year with a cautious stance on long-term rates for valuation reasons. We remain cautious, but now for reasons related to the fiscal deficit and the noise around the US presidential election. The return of the term premium, in the absence of a recession, is a likely scenario. Volatility in long-term rates will remain sustainably higher than in the 2010s (Chart 4, page 9).

CHART 3: FED FUNDS RATE: RECESSION CUTS VERSUS INSURANCE CUTS, %



Source: Bloomberg, Indosuez Wealth Management.

5 - A term used in aviation.

EUROPE: THE WEAK LINK IN GLOBAL GROWTH

Inflation has chipped away at European consumers' purchasing power due to sticky-up wages. Financial conditions in the region are tight and surveys by the European Central Bank (ECB) point to weak demand for credit. At the fiscal level, Germany generated a primary surplus in 2023. The reinstatement of stability rules for all countries, which had been put on hold during the COVID-19 epidemic, will prevent renewed *momentum* in 2024 or 2025.

As we write this, the markets are expecting the first rate cut at the 6 June meeting and 125 bps of cuts by the end of the year, taking into account only the 25 bps steps. These expectations are slightly more aggressive than the 100 bps of cuts that we expect in 2024.

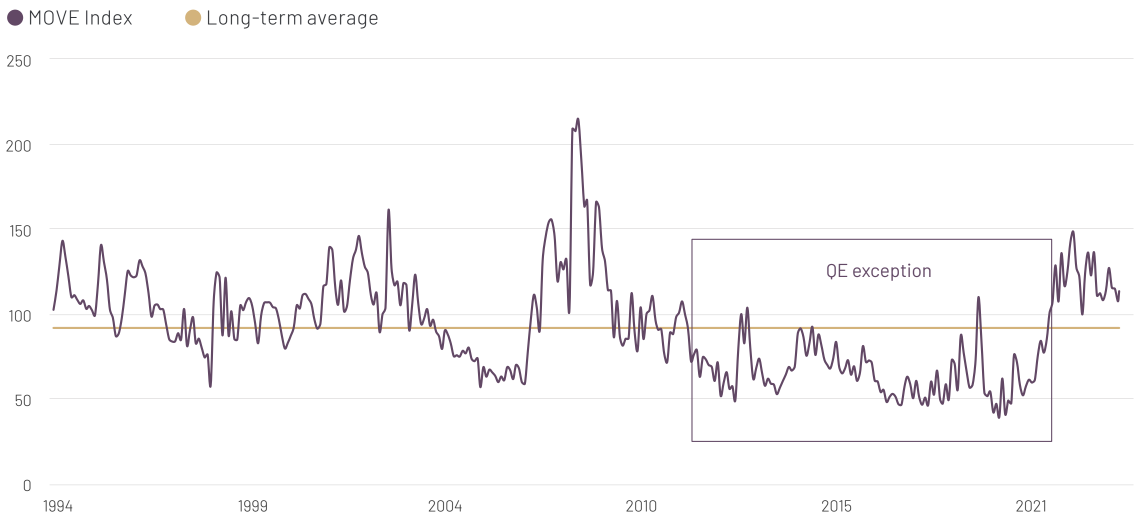
In terms of portfolio positioning, bond managers continue to favour short to medium maturities which have the benefit of providing carry with limited volatility. Conversely, the long ends of the curve (10 years or more) are, for now, still more volatile and under the influence of the US market, on which we are – you guessed it – cautious.

CREDIT MARKETS

The capital markets were wide open in January, to provide funding for all companies on both sides of the Atlantic. Investors have answered the call to absorb supply – investment grade, high yield, all maturities – since the beginning of the year. Subscriptions flowed into funds as long-term investors (pension funds, insurers) acted on their need for duration. Against this backdrop, managers have renewed confidence in this market, as dispersion continues to exist and has created opportunities. In light of the very sharp narrowing of risk premiums since October, it makes sense to be selective again, particularly on the European high yield market. Tail risks have disappeared from the markets. Since the beginning of the year, the real estate sector has outperformed in the Euro Area, driven by rate cut expectations. In contrast, concerns about the dispersion of the risk of a decline in US commercial real estate are affecting the European banks – German banks in particular – that are involved in this market.

We end this monthly review by noting that our managers in Asia have lowered their outlooks for their domestic markets for valuation reasons. In comparison, technical aspects support the market: unlike the United States and Europe, the primary market is not very active, forcing investors to maintain their positions.

CHART 4: VOLATILITY IN THE US BOND MARKET



Source: Bloomberg, Indosuez Wealth Management.

US EQUITY MARKETS SET NEW RECORDS

Laura CORRIERAS
Equity Portfolio Manager

With the contribution
of the Equity Team

Hopes of a Fed rate cut in March are dimming, but this has not dampened the US markets which are hitting new all-time highs. They have been supported, in particular, by fading recession fears and a rather resilient fourth-quarter 2023 corporate earnings season.

75%
of US companies reported
HIGHER-THAN-EXPECTED EPS

EARNINGS REPORTS VARY BY REGION AND SECTOR

The season has generally been favourable in the United States: 75% of companies reported higher-than-expected earnings per share (EPS) (above the 10-year average). Companies proved they can preserve their margins in a disinflationary environment, and some have resumed their massive investment plans, including certain tech companies (with the "Magnificent 7" at the top of the list).

The earnings season was more mixed in Europe. The banking sector suffered from profit-taking due to a slowdown in profits in a lower rate environment. In contrast, some companies surprised to the upside, such as the "GRANOLAS"[6], which posted above-market earnings growth and high and stable margins, and who also plan to increase their investments thanks to their cash generation.

EUROPE

After a sluggish start to the year, the European markets regained some ground, buoyed by the tech sector and consumer discretionary. From a geographic standpoint, the Euro Area market has fared much better than other European countries since the beginning of the year, driven mainly by strong earnings reports from companies in France (notably luxury goods) and Italy (automotive).

Valuations have risen slightly but remain below their long-term average for Euro Area indices and are, in particular, deeply discounted versus the United States, even after sector adjustments.

UNITED STATES

The US markets continued to outperform in early 2024, enabling the indices to reach new all-time highs (the S&P 500 recently topped 5'000 points, well above the previous records set in January 2022).

The market is once again being driven by the same themes as last year, with growth and tech stocks continuing to propel it upwards. And the recent earnings season reassured investors on that point: the tech sector posted the highest earnings growth and companies' comments indicate that they intend to spend heavily on technology, in particular on cybersecurity, artificial intelligence (AI) and the cloud.

6 - GSK, Roche, ASML, Nestle, Novartis, Novo Nordisk, L'Oreal, LVMH, AstraZeneca, SAP and Sanofi.

US equity valuation levels are admittedly quite high relative to other geographic regions, but they are backed by solid earnings outlooks, particularly in the tech segment which is driving the rise (Chart 5). Bear in mind that US companies benefit from their technological dominance but invest massively to maintain it.

ASIA

Although sentiment on China remains negative, the perception is different for the rest of Asia. Major players in the semiconductor/server supply chain in Taiwan delivered encouraging messages. In South Korea, a value-up corporate governance reform, similar to the one implemented in Japan, could be a strong catalyst for Korean domestic stocks. Lastly, stock market and earnings *momentum* in India remains strong despite high valuations in certain sectors.

We remain cautions on China in the short/medium term; some growth companies currently offer attractive value propositions. Finally, *momentum* from support measures has been strong.

The "Chinese national team" bought massive amounts of domestic equities through local ETFs in recent weeks. This sent a rather positive signal in a generally tight equity market. However, certain challenges still need to be addressed.

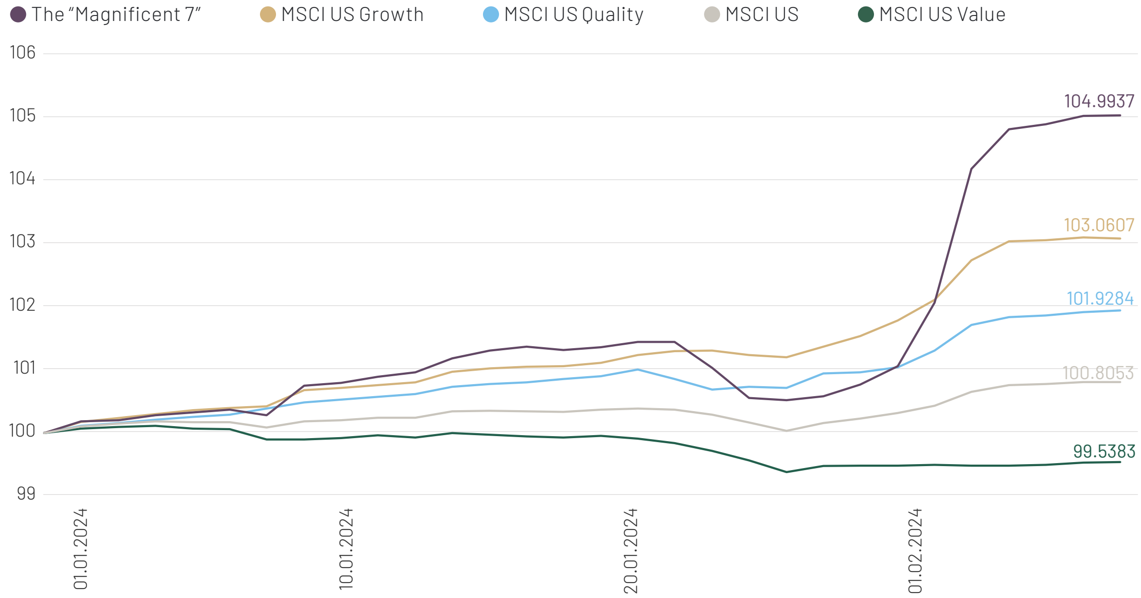
INVESTING STYLE

Quality/Growth stocks continue to outperform the rest of the market in both the United States and Europe. While we await the central banks' rate cuts, which are expected in the second quarter of 2024, we maintain our exposure to companies with resilient business models that have been able to deliver consistent earnings and margins in a high-rate and inflationary environment.

Similarly, we maintain our exposure to growth stocks with artificial intelligence exposure, which continue to be driven by higher earnings growth than the rest of the market.

Lastly, if the Fed pivot is confirmed in a Goldilocks scenario, it may be appropriate to get back into small and mid caps, which enjoy a deep valuation discount, as well as the cyclical sectors (industry, basic resources, etc.) later in the year, after the PMIs change direction.

CHART 5: EARNINGS REVISIONS IN THE UNITED STATES BY INVESTMENT STYLE YEAR TO DATE



Source: Bloomberg, Indosuez Wealth Management.

DOLLAR NOT EASILY DETHRONED

Maxime GARCIA
Investment Strategist

The dollar is expected to hold on to its crown this month, while the euro will continue to suffer from a negative growth differential with the United States. The Swiss National Bank (SNB) has been advocating for a lower franc and could soon take action. The yen, however, will remain dependent on the Fed. We maintain our interest in gold but are waiting for a correction before coming back into the asset.

BULLISH VIEW on the DOLLAR, driven by the outperformance by the US economy

USD

Positive *momentum*

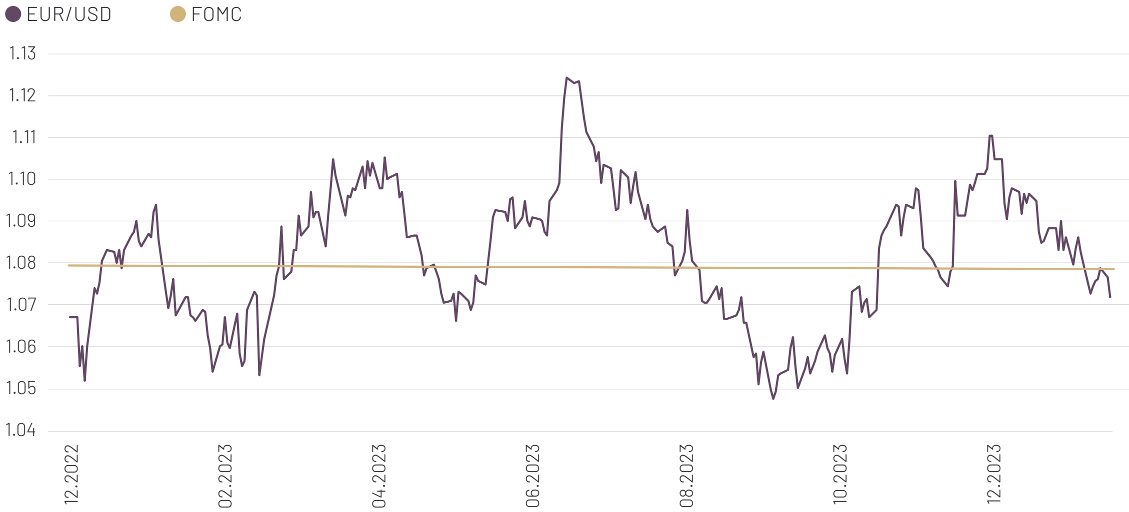
The USD has risen to the top of the G10 currency rankings, posting a performance of +3.6% since the beginning of the year. It is supported, on the one hand, by US macroeconomic dynamics and, on the other, by the readjustment of expectations for the Fed's future rate cuts. For the USD to wobble a bit we would first have to see a slowdown in the US economy or the Fed's first rate cut, i.e. two things we do not expect to happen next month. We therefore maintain our bullish view on the dollar, which should continue to benefit from the outperformance by the US economy and which remains an attractive asset to hold as a hedge against the risk of a further acceleration in inflation. In the longer term, we still believe the dollar will lose ground, particularly at the start of the Fed rate cut cycle, supporting pro-risk sentiment and thus impacting the more cyclical currencies.

EUR

Suffers from the comparison with its US neighbour

The euro is yielding ground to the dollar, having lost 3% since the beginning of the year, and we think this trend could continue in the short term. First, the EUR/USD is holding just below the level observed before the December FOMC meeting (Chart 6), and the differential in key rates expected by the market for June, between the ECB and the Fed, is currently only a few basis points off from where it was then. However, consensus on Euro Area growth has diverged negatively from that of the United States since December, and we believe this will soon be reflected in the EUR/USD price. In addition, the Economic and Monetary Union (EMU) tops the list of regions likely to experience difficulties in the face of the emergence and continuation of tensions in the Middle East. We therefore maintain our slightly bearish view in the short term, with a target close to 1.065. In the longer term, the start of the rate cut cycle by developed country central banks could favour the euro.

CHART 6: EUR/USD



Source: Datastream, Indosuez Wealth Management.

CHF

Downward pressure

After outperforming in 2023, the Swiss franc is losing its lustre. Inflation has continued to slow, coming in at 1.3% year-on-year in January, below the central bank's target and economists' expectations. This movement is notably driving investors' expectations for future rate cuts by the SNB, which amplifies the already negative rate differential with the euro and the dollar and weighs on the CHF. In addition, the central bank has been commenting more frequently on the undesirable implications of an excessively strong CHF. The most recent statement to date is from the chairman of the Swiss National Bank, who said it represents a drag on growth. Consequently, although we do not yet have any confirmation that the SNB will intervene to depreciate its currency, this scenario is likely to materialise soon. This leads us to maintain our short-term bullish view on the USD/CHF (which is expected to hover between 0.88 and 0.90 during the month), particularly as the pair continues to trade at a low level despite the recent underperformance by the Swiss franc, leaving room for upside potential.

JPY

Continues to flirt with its all-time lows

The JPY weakened in January, caught between the readjustments to US rates and the Bank of Japan's warning that rates are not necessarily likely to increase quickly once the negative interest rate policy ends, in keeping with our scenario. We remain neutral in the short term.

The risk of a further acceleration in inflation could accentuate the yen's underperformance against the dollar, but we should bear in mind that a USD/JPY above 150 could increase the likelihood of an intervention by Japan's central bank. In the longer term, the JPY will continue to be influenced mainly by developments in the United States.

As such, the Fed rate cut expected in the second quarter should ease the pressure weighing on the Japanese currency. We will therefore wait for the USD/JPY to reach around 152 before selling the pair in anticipation of a move towards 142.

GOLD

Waiting for a better entry point

Headwinds have mounted for gold: a strong dollar, rate expectations pushed back, and outflows from ETFs. However, the yellow metal remains close to 2'000 dollars/ounce and seems impervious to factors that could erode its performance. Central banks' massive purchases as part of their currency reserve diversification strategy and the persistence of geopolitical risk in an election year are acting as important supports. At the current level, we prefer to wait for a better entry point, at around 1'930-1'950 dollars/ounce, before buying gold with a target of 2'050-2'100 dollars/ounce.

INVESTMENT SCENARIO AND ALLOCATION CONVICTIONS

Grégory STEINER
Global Head of Multi Asset

Adrien ROURE
Portfolio Manager

Upward revision to
US GROWTH

INVESTMENT SCENARIO

- **Growth:** we revised up our growth assumptions for the US economy for 2024 and 2025 to +2.3% and +1.7%, respectively. The reasons for this upgrade are, first, a higher carry-over effect for 2024 and, second, the strength of consumption and the labour market in the United States. However, we have left our scenario for the Euro Area unchanged, with growth forecast to be modest but supported by an improvement in household purchasing power. Emerging countries continue to drive global growth.
- **Inflation:** we are still of the belief that the disinflation process will continue in the coming months, although we expect to enter a less linear and more volatile phase for price changes. Upside risks remain, particularly within services, as seen in the January US inflation figures. We are also keeping an eye on the potential consequences of the current tensions in the Red Sea for the price of goods but, at this stage, we believe the impact on inflation remains limited.
- **Central Banks:** as we had anticipated, the fixed-income markets have adjusted in recent weeks and moved close to our scenario of 100 bps of rate cuts by the Fed and the ECB in 2024, with the first cut expected in the second quarter.
- **Corporate earnings:** the recent earnings season confirmed our expectation that US companies (particularly those in the tech sector) will be better able to deliver on earnings forecasts for 2024. In contrast, their European counterparts are seeing downward revisions.
- **Risk environment:** we think the likelihood of a recession scenario is now relatively low and believe, conversely, that the main market risk comes from a reacceleration of inflation. The other external factors we are monitoring include the sustainability of public debt and the (geo)political situation around the world.

ALLOCATION CONVICTIONS

Equities

- The latest macroeconomic data released confirm our scenario of a soft landing for the global economy, thanks in particular to the resilience of US economic activity. These developments, combined with companies' strong financial health, notably for large caps, lead us to maintain a strategically positive view on the equity markets in the medium term. Technical and investor positioning indicators nonetheless prompt us to put off adding to any of our exposures at this stage.
- Unsurprisingly, we favour exposure to US-listed equities in our allocations, as they benefit from both a more robust macroeconomic environment and an upward revision to earnings forecasts for 2024. These stocks are also most likely to benefit from the spread of artificial intelligence.
- European equities look less attractive to us on a relative basis. We prefer to wait for earnings dynamics to turn around and for better visibility on economic growth before adding to our existing exposures.
- Lastly, we maintain a constructive view on emerging market assets. However, a diversified view is preferable, given the idiosyncratic risks in the emerging world. Broader exposure will also allow us to take advantage of certain specific stories, such as South Korea, which is benefiting from the turnaround in the semiconductor cycle.

Bonds

- Our scenario continued to materialise with the ongoing upward rate adjustment trend, following higher-than-expected US inflation figures. We are now more comfortable with the rate levels we are seeing, but believe it is still too soon to significantly increase our sensitivity to bond risk as long as the disinflation path remains uncertain. For these reasons, we reiterate our positive recommendation on sovereign bonds with short maturities (up to five years) as opposed to longer, more volatile, and lower-return maturities.
- In the credit segment, we reiterate our preference for high-quality corporate debt with short maturities, which we believe offers the best risk/return. We continue to steer clear of high yield bonds, as we prefer to consume risk within the equity allocations.
- From a diversification perspective, we maintain a strategically positive view on emerging market debt in local currencies.

Forex market

- Last month we tactically raised our recommendation on the dollar, as the market appeared to have been too aggressive in pricing in the Fed's future rate cuts. While the greenback benefited substantially from the adjustment to US rates in recent weeks, we believe the trend could continue in the short term. In the medium term, various structural factors could nevertheless weigh on the currency.
- We have left our recommendation on the Swiss franc unchanged. It no longer enjoys the support of the SNB while the disinflation process appears to be well underway locally.
- The Japanese currency was recently hurt by the rise in rates in the United States and is now approaching the Bank of Japan's previous intervention thresholds. The yen could, as the case may be, benefit from its central bank's interventionism. Nonetheless, the change in parity in the medium term remains constrained by future Fed monetary policy developments.

KEY CONVICTIONS

	TACTICAL VIEW (ST)	STRATEGIC VIEW (LT)
FIXED INCOME		
GOVERNMENTS		
EUR 2-Year	=	=
EUR 10-Year	=/-	=
EUR Periphery	=	=/-
US 2-Year	=/+	+
US 10-Year	=/-	=
EUR Breakevens Inflation	=/+	=/+
US Breakevens Inflation	=/+	=
CREDIT		
Investment grade EUR	=/+	+
High yield EUR	=/-	=
Financials Bonds EUR	=	=/+
Investment grade USD	=	=/+
High yield USD	-	=/-
EMERGING DEBT		
Hard Currencies	=	=/+
Local Currencies	=	=/+
EQUITIES		
GEOGRAPHIES		
Europe	=/-	=/-
United States	=/+	=/+
Japan	=	=
Latin America	=	=
Asia ex-China	=/+	=/+
China	=	=/-
STYLES		
Growth	=/+	=/+
Value	=	=
Quality	=/+	=
Cyclical	=	=
Defensive	=/-	=/-
FOREX		
United States (USD)	=/+	=/-
Euro Area (EUR)	=/-	=/+
United Kingdom (GBP)	=/-	=
Switzerland (CHF)	=/-	=
Japan (JPY)	=	=/+
China (CNY)	=	=
Gold (XAU)	=/-	=/+

Source: Indosuez Wealth Management.

OVERVIEW OF SELECTED MARKETS

DATA AS OF 22 FEBRUARY 2024

GOVERNMENT BONDS	YIELD	4 WEEKS CHANGE (BPS)	YTD CHANGE (BPS)
US Treasury 10-year	4,32%	20,23	44,16
France 10-year	2,91%	13,40	35,60
Germany 10-year	2,44%	15,00	41,80
Spain 10-year	3,34%	14,80	36,10
Switzerland 10-year	0,88%	0,00	17,50
Japan 10-year	0,71%	-2,50	10,60

BONDS	LAST	4 WEEKS CHANGE	YTD CHANGE
Government Bonds Emerging Markets	35,89	-0,47%	-2,26%
Euro Government Bonds	201,30	-0,68%	-1,39%
Corporate EUR high yield	218,09	0,35%	0,81%
Corporate USD high yield	334,73	0,19%	-0,07%
US Government Bonds	304,42	-0,81%	-1,17%
Corporate Emerging Markets	44,16	0,14%	0,07%

CURRENCIES	LAST SPOT	4 WEEKS CHANGE	YTD CHANGE
EUR/CHF	0,9527	1,30%	2,56%
GBP/USD	1,2660	-0,38%	-0,56%
USD/CHF	0,8802	1,51%	4,61%
EUR/USD	1,0823	-0,21%	-1,96%
USD/JPY	150,53	1,94%	6,73%

VOLATILITY INDEX	LAST	4 WEEKS CHANGE (POINTS)	YTD CHANGE (POINTS)
VIX	14,54	1,09	2,09

EQUITY INDICES	LAST PRICE	4 WEEKS CHANGE	YTD CHANGE
S&P 500 (United States)	5'087,03	3,94%	6,65%
FTSE 100 (United Kingdom)	7'684,49	2,06%	-0,63%
STOXX 600	495,10	3,46%	3,36%
Topix	2'660,71	5,09%	12,44%
MSCI World	3'329,86	3,66%	5,07%
Shanghai SE Composite	3'486,68	4,30%	1,62%
MSCI Emerging Markets	1'029,44	4,16%	0,56%
MSCI Latam (Latin America)	2'570,02	1,70%	-3,48%
MSCI EMEA (Europe, Middle East, Africa)	203,44	1,82%	1,33%
MSCI Asia Ex Japan	644,96	4,66%	0,53%
CAC 40 (France)	7'911,60	5,99%	4,88%
DAX (Germany)	17'370,45	2,74%	3,69%
MIB (Italy)	32'356,26	7,29%	6,60%
IBEX (Spain)	10'138,90	2,24%	0,36%
SMI (Switzerland)	11'386,17	1,58%	2,23%

COMMODITIES	LAST PRICE	4 WEEKS CHANGE	YTD CHANGE
Steel Rebar (CNY/Tonne)	3'843,00	-0,36%	-4,88%
Gold (USD/Oz)	2'024,39	0,18%	-1,87%
Crude Oil WTI (USD/Bbl)	78,61	1,62%	9,71%
Silver (USD/Oz)	22,78	-0,62%	-5,41%
Copper (USD/Tonne)	8'584,50	0,19%	0,30%
Natural Gas (USD/MMBtu)	1,73	-32,63%	-31,11%

Source: Bloomberg, Indosuez Wealth Management.
Past performance does not guarantee future performance.

MONTHLY INVESTMENT RETURNS, PRICE INDEX

FTSE 100 · Topix · MSCI World · MSCI EMEA · MSCI Emerging Markets
STOXX 600 · S&P 500 · Shanghai SE Composite · MSCI Latam · MSCI Asia Ex Japan

	NOVEMBER 2023	DECEMBER 2023	JANUARY 2024	4 WEEKS CHANGE	YTD (22.02.2024)
BEST PERFORMING +	12.99%	7.74%	7.81%	5.09%	12.44%
	9.21%	4.81%	1.59%	4.66%	6.65%
	8.92%	4.71%	1.39%	4.30%	5.07%
	7.86%	4.42%	1.14%	4.16%	3.36%
	6.86%	3.77%	-1.02%	3.94%	1.62%
	6.45%	3.75%	-1.33%	3.66%	1.33%
	6.32%	3.71%	-4.68%	3.46%	0.56%
	5.38%	3.35%	-4.85%	2.06%	0.53%
	1.80%	-0.36%	-5.49%	1.82%	-0.63%
− WORST PERFORMING	-2.14%	-1.86%	-6.29%	1.70%	-3.48%

Source: Bloomberg, Indosuez Wealth Management.
Past performance does not guarantee future performance.

Basis point (bps): 1 basis point = 0.01%.

Blockchain: A technology for storing and transmitting information. It takes the form of a database which has the particularity of being shared simultaneously with all its users and generally does not depend on any central body.

BLS: Bureau of Labor Statistics.

BNEF: Bloomberg New Energy Finance.

Brent: A type of sweet crude oil, often used as a benchmark for the price of crude oil in Europe.

CPI (Consumer Price Index): The CPI estimates the general price level faced by a typical household based on an average consumption basket of goods and services. The CPI tends to be the most commonly used measure of price inflation.

Cyclicals: Cyclicals refers to companies that are dependent on the changes in the overall economy. These stocks represent the companies whose profit is higher when the economy is prospering.

Defensives: Defensives refers to companies that are more or less immune to the changes in the economic conditions.

Deflation: Deflation is the opposite of inflation. Contrary to inflation, it is characterised by a sustained decrease in general price levels over an extended period.

Duration: Reflects the sensitivity of a bond or bond fund to changes in interest rates. This value is expressed in years. The longer the duration of a bond, the more sensitive its price is to interest rate changes.

EBIT (Earnings Before Interest and Taxes): Refers to earnings generated before any financial interest and taxes are taken into account. It takes earnings and subtracts operating expenses and thus also corresponds to non-operating expenses.

EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortisation): EBITDA takes net income and adds interest, taxes, depreciation and amortisation expenses back to it. It is used to measure a company's operating profitability before non-operating expenses and non-cash charges.

ECB: The European Central Bank, which governs the euro and Euro Area member countries' monetary policy.

Economic Surprises Index: Measures the degree of variation in macro-economic data published versus forecasters' expectations.

Economies of scale: Decrease in a product's unit cost that a company obtains by increasing the quantity of its production.

EPS: Earnings per share.

ESG: Non-financial corporate rating system based on environmental, social and governance criteria. It is used to evaluate the sustainability and ethical impact of an investment in a company.

Fed: The US Federal Reserve, i.e. the central bank of the United States.

FOMC (Federal Open Market Committee): The US Federal Reserve's monetary policy body.

GDP (Gross Domestic Product): GDP measures a country's yearly production of goods and services by operators residing within the national territory.

Growth: Growth style refers to companies expected to grow sales and earnings at a faster rate than the market average. As such, growth stocks are generally characterised by a higher valuation than the market as a whole.

IEA: International Energy Agency.

IMF: The International Monetary Fund.

Inflation breakeven: Level of inflation where nominal bonds have the same return as inflation-linked bonds (of the same maturity and grade). In other words, it is the level of inflation at which it makes no difference if an investor owns a nominal bond or an inflation-linked bond. It therefore represents inflation expectations in a geographic region for a specific maturity.

Inflation swap rate 5-Year, 5-Year: A market measure of what 5-Year inflation expectations will be in five years' time. It provides a window into how inflation expectations may change in the future.

IPPC: The Intergovernmental Panel on Climate Change.

IRENA: International Renewable Energy Agency.

ISM: Institute for Supply Management.

Japanification of the economy: Refers to the stagnation the Japanese economy has faced in the last three decades, and is generally used to refer to economists' fears that other developed countries will follow suit.

Metaverse: A metaverse (portmanteau of meta and universe) is a fictional virtual world. The term is regularly used to describe a future version of the internet where virtual, persistent and shared spaces are accessible via 3D interaction.

OECD: Organisation for Economic Co-operation and Development.

Oligopoly: An oligopoly occurs when there is a small number of producers (supply) with a certain amount of market power and a large number of customers (demand) on a market.

OPEC: Organization of the Petroleum Exporting Countries; 14 members.

OPEC+: OPEC plus 10 additional countries, notably Russia, Mexico, and Kazakhstan.

PMI: Purchasing Managers' Index.

Policy mix: The economic strategy adopted by a state depending on the economic environment and its objectives, mainly consisting of a combination of monetary and fiscal policy.

Pricing power: Refers to the ability of a company or brand to increase its prices without affecting demand for its products.

Quality: Quality stocks refers to companies with higher and more reliable profits, low debt and other measures of stable earnings and strong governance. Common characteristics of Quality stocks are high return to equity, debt to equity and earnings variability.

Quantitative easing (QE): A monetary policy tool by which the central bank acquires assets such as bonds, in order to inject liquidity into the economy.

SEC (Securities and Exchange Commission): The SEC is an independent federal agency with responsibility for the orderly functioning of US securities markets.

Spread (or credit spread): A spread is the difference between two assets, typically between interest rates, such as those of corporate bonds over a government bond.

Secular stagnation: Refers to an extended period of little or no economic growth.

SRI: Sustainable and Responsible Investments.

Stagflation: Stagflation refers to an economy that is experiencing simultaneously an increase in inflation and stagnation of economic output.

TPI: An addition to the Eurosystem's toolkit that can be activated by the ECB to counter unwarranted, disorderly market developments if these pose a serious threat to the smooth transmission of monetary policy across the euro area. The ECB Governing Council approved the instrument on the 21 July 2022.

Uberisation: Term derived from the name of US company Uber which develops and operates digital platforms that connect drivers and riders. It refers to a new business model that leverages new digital technologies and is part of the sharing economy, insofar as it puts customers in direct contact with service providers, at a reduced cost and with lower prices.

Value: Value style refers to companies that appear to trade at a lower price relative to its fundamentals. Common characteristics of value stocks include high dividend yield, low price-to-book ratio, and a low price-to-earnings ratio.

VIX: The index of implied volatility in the S&P 500 Index. It measures market operators' expectations of 30-day volatility, based on index options.

WTI (West Texas Intermediate): Along with Brent crude, the WTI is a benchmark for crude oil prices. WTI crude is produced in America and is a blend of several sweet crude oils.

WTO: World Trade Organization.

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Edited as per 22.02.2024.