Julius Bär

CHANGING COST OF MONEY: HISTORY, IMPLICATIONS, AND RISKS

10TH CITY OF LONDON BIENNIAL MEETING
INVESTMENT BANKING AND FINANCE CONFERENCE

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US Treasury yields

US Treasury yields bottomed in summer 2020 and the 10-year yield has risen now from 0.53% to 3.74%, breaking above its long-term downtrend in March 2022

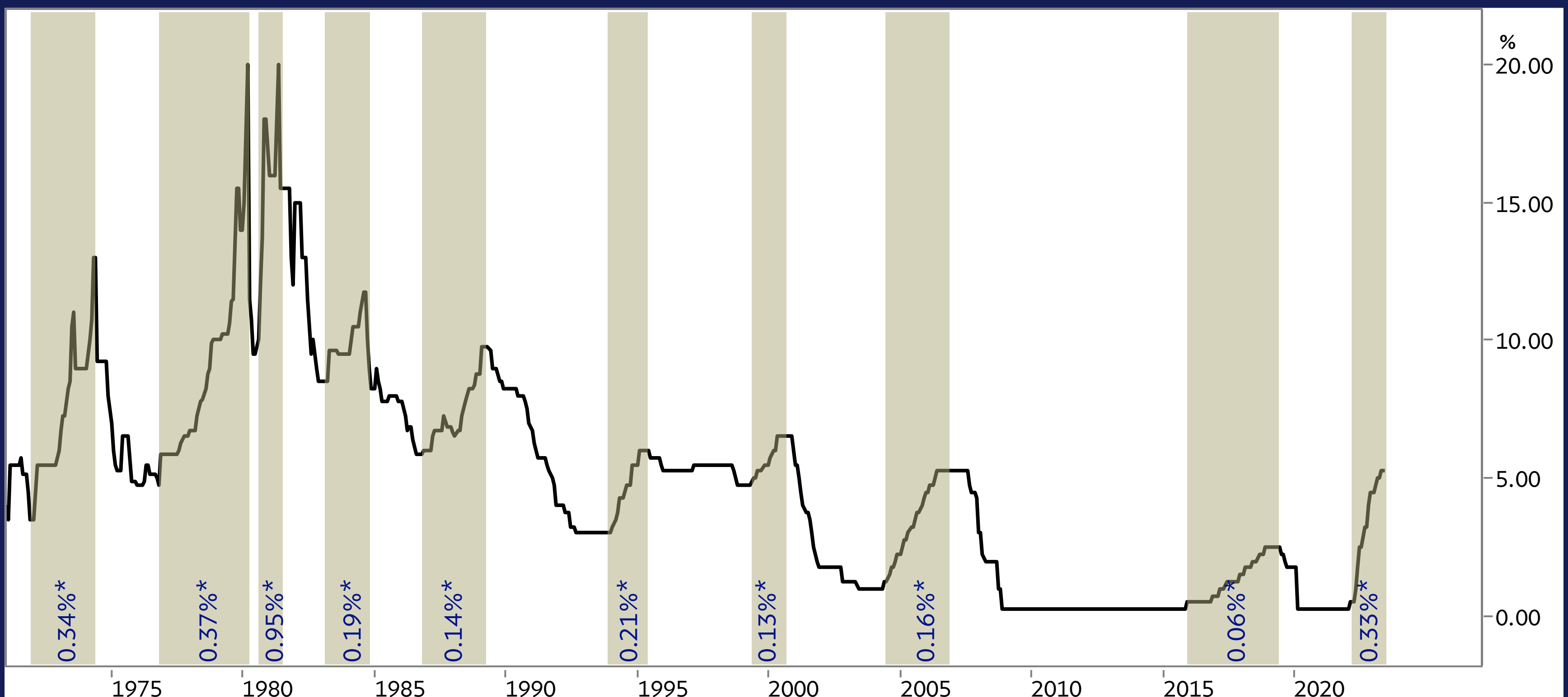
5-, 10- and 30-year US Treasury yields have been breaking above downtrend

Source: Bloomberg Finance L.P., Julius Baer
Past performance and performance forecasts are not reliable indicators of future results. The return may increase or decrease as a result of currency fluctuations. Technical analysis may be inconsistent with and reach different conclusions to fundamental analysis.

US Federal Reserve rate hike periods since 1971

We are currently experiencing the fastest rate hike since 1980/1981 (0.33% per month), bringing the US consumer price index year-on-year down from 7.5% to 4.9%

Fed funds target rate – hiking periods



Source: Bloomberg Finance L.P., Julius Baer
*Average percentage increase per calendar month

Rate hikes and asset/index performance

Historic performance of different assets/indices during rate hike periods and 12 months after the hiking stopped

Rate hike cycles highlighting the two best and two worst performers

Rate hike period	Feb 72 May 74		Nov 76 Mar 80		Jul 80 May 81		Apr 83 Aug 84		Nov 86 Feb 89		Jan 94 Feb 95		May 99 May 00		May 04 Jun 06		Nov 15 Dec 18		Feb 22 May 23
Asset / Index	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR	12-month return after hike	CAGR
S&P 500 Index	-8.8%	4.4%	1.2%	33.2%	8.6%	-15.6%	0.7%	13.2%	7.5%	14.9%	3.4%	31.4%	10.8%	-11.6%	6.2%	18.4%	8.6%	28.9%	-3.6%
Consumer staples											12.7%	35.7%	-14.9%	12.1%	3.5%	12.2%	2.6%	24.0%	-2.4%
Healthcare											18.1%	48.8%	15.5%	5.3%	1.8%	16.6%	8.0%	18.7%	-1.4%
Financials											-0.4%	43.0%	-6.0%	13.9%	7.0%	11.8%	8.8%	29.2%	-14.4%
Technology											22.7%	43.9%	58.1%	-47.4%	-2.3%	25.1%	15.4%	48.0%	5.7%
Nasdaq 100									10.3%	13.1%	6.8%	44.0%	72.1%	-45.9%	1.3%	22.8%	13.2%	38.0%	0.1%
Dax	-12.6%	16.2%	-0.8%	1.8%	1.9%	2.9%	9.0%	44.0%	-4.3%	40.4%	-10.4%	17.9%	32.9%	-13.9%	18.7%	40.9%	-0.6%	25.5%	6.6%
Hang Seng	6.8%	-20.0%	25.4%	74.9%	54.1%	-15.6%	-1.2%	78.7%	9.7%	-2.0%	-22.1%	33.6%	30.1%	-10.5%	16.5%	33.8%	7.8%	9.1%	-16.1%
Gold	64.5%	2.3%	49.8%	3.9%	-32.9%	-32.1%	-14.5%	-4.3%	0.0%	5.3%	2.1%	6.3%	6.5%	-2.3%	24.6%	5.5%	7.1%	18.3%	2.2%
Copper									-14.0%	-18.0%	47.6%	-10.3%	27.3%	-7.0%	60.7%	-0.3%	10.2%	6.3%	-14.8%
Brent Crude Oil									44.6%	18.8%	19.5%	5.3%	90.6%	3.6%	39.4%	-2.9%	10.9%	22.7%	-23.2%
Bloomberg Commodity Index	58.6%	11.0%	19.4%	-4.4%	-30.8%	-26.1%	-5.9%	-10.9%	10.1%	8.6%	7.1%	13.0%	30.4%	3.2%	8.1%	-2.1%	-0.1%	5.4%	-11.8%
Baltic Dry Index									40.5%	3.3%	68.7%	-33.1%	58.4%	-11.3%	0.0%	111.8%	4.3%	-14.2%	-44.5%
US M2 money supply	8.8%	7.1%	8.8%	8.3%	9.7%	8.7%	7.4%	9.3%	4.7%	5.9%	0.4%	4.5%	6.1%	7.8%	4.7%	6.4%	5.3%	7.1%	-3.1%

Data as of: 08/06/2023 16:28

Source: Bloomberg Finance L.P., Julius Baer
CAGR = Compound Annual Growth Rate

Current environment and risks…

… and their effect on banks' performance and business models

Recent easing inflation pressure could pause/stop the rate hikes, but a fast return to the previous low interest rate levels and inflation regime is not expected

Inflation drivers
- Sanctions, war
- Deglobalisation (nearshoring)
- Policies
- 'Greenflation'
- Tightness in the labour market due to demographics
- Further financing of debt

Risks for businesses
- Banks will tighten credit because of poor balance sheets
- Business models need to compete with the risk-free rate again, weak models might become insolvent
- Increased cost cannot be passed on in some areas

Risks for banks
- Adjustment to steep rise in interest rates
- Matching borrowing with lending duration and interest rates
- Effects on the performance of banks
- Slowdown in credit/mortgage activity
- Commercial real estate facing headwinds

Market risks
- Possible deflationary shock in the short term
- Second-round inflation due to persistent higher interest rates and lagged price rises

Source: Julius Baer

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C	Closing price	H	High price	L	Low price
ST	Short-term (2-8 weeks)	MT	Medium-term (8-26 weeks)	LT	Long-term (> 26 weeks)
MAV	Moving average				
Momen-tum	Momentum is derived from different rate of change calculations based on the underlying instrument.				

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