



“Shrinking money supply”

Our Opinion
July 2023

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Dear Readers

The article “Shrinking money supply” describes the impact a contraction of the money supply can have on the economy and inflation.

Looking for advice and support on financial matters? Our investment advisors look forward to hearing from you and will be happy to talk to you personally.

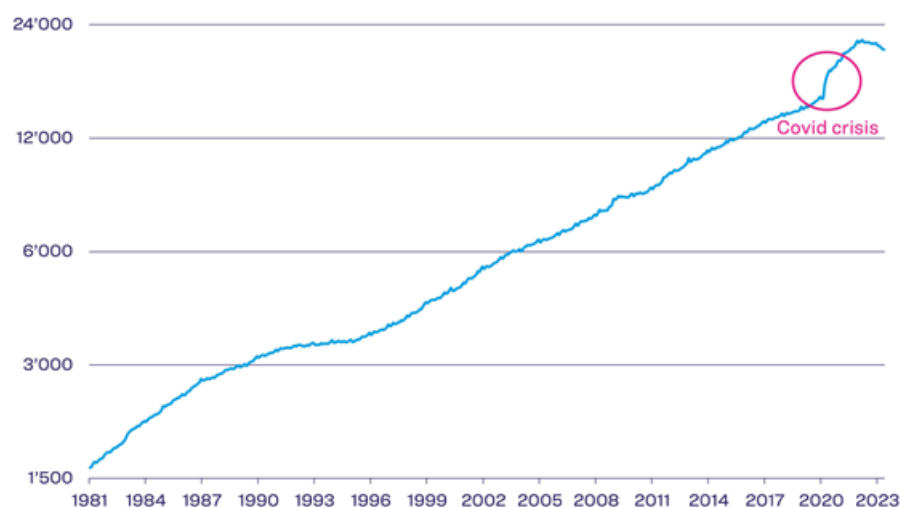
We wish you a pleasant read.
Your Advisory Team

“Shrinking money supply”

Economy

How much money is available to the global economy is determined by the central banks, given that they put legal tender into circulation. The M1 money supply is composed of cash and sight deposits at banks. The M2 money supply, which additionally includes time deposits at banks and money market funds, is considered by financial experts to be the most meaningful aggregate. Central banks can use the money supply to add or withdraw money from the market. As the following chart shows, our monetary system is built on the creation of money – as a rule, the money supply continuously increases.

US M2 money supply in USD billion



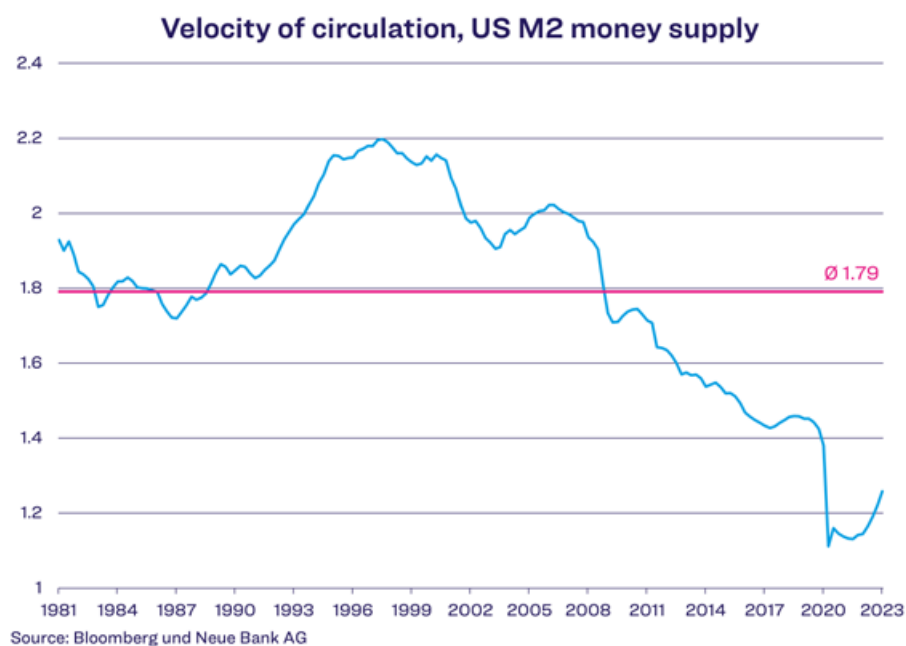
Source: Bloomberg and Neue Bank AG

Last year and this year have seen a rare occurrence: The US M2 money supply has shrunk by 1.4% and 3.7%, respectively. It is very unusual for the money supply to contract by this extent. The last time a comparable reduction of liquidity was observed was in the 1930s. In the past, a significant slowdown in the growth of the money supply has often led to a recession. During the covid pandemic, however, liquidity was expanded dramatically, leading to a significant increase in M2 (see chart above).

The current reduction in the money supply can accordingly be described as a return to normal and should not cause any major damage, given that – despite the decline – there is still sufficient liquidity available to the economy. For this reason, the historically sharp reduction in the money supply does not necessarily have to lead to a recession.

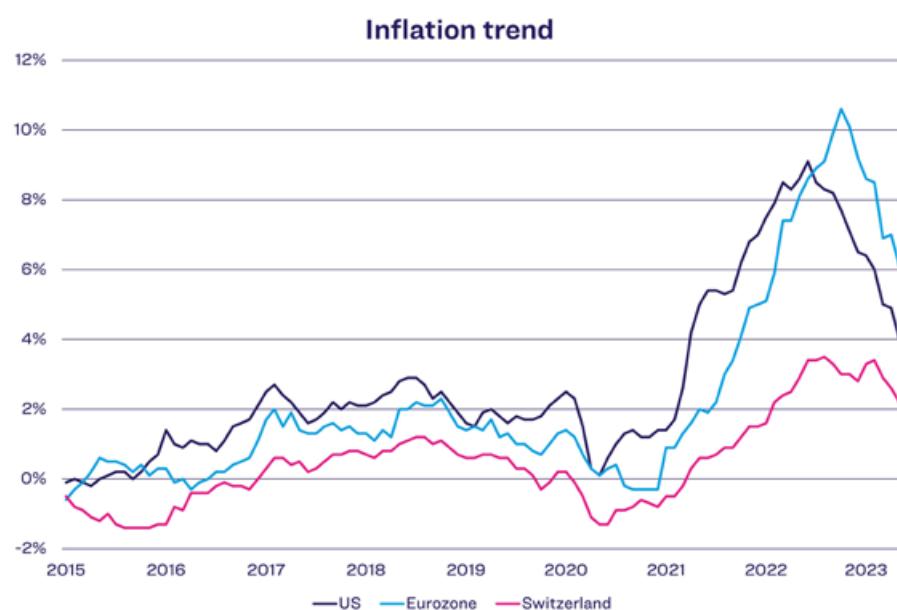
Bonds

The extreme liquidity glut during the pandemic certainly contributed to the subsequent sharp rise in inflation. However, not only the money supply, but also the velocity of circulation has an inflationary effect. The more frequently money issued by the central bank changes hands, the more the economy accelerates, fuelling inflation. As the following chart shows, the velocity of circulation has been increasing since the pandemic.



Nevertheless, it is still below its long-term average of 1.79. A shrinking money supply and a historically low velocity of circulation should continue to have a disinflationary effect for now, assuming that the velocity of circulation does not increase sharply in future. This decline in inflation is already clearly reflected in the inflation figures.

Falling commodity prices and recovering supply chains also indicate that the worst of the price pressure is over. The nightmare scenario of a price-wage spiral has not materialised so far. Investors cannot yet relax



Source: Bloomberg und Neue Bank AG

Neue Bank traffic light

- strongly bearish
- bearish
- neutral
- slightly bullish
- bullish
- strongly bullish

completely, however, given that inflation is still above the target of 2% and the biggest current price drivers – rents and housing as well as services – have so far eased only marginally. If the disinflationary trend continues, bonds with a good credit rating could become very interesting for investors, given that no further sharp interest rate hikes should then be expected.

Equities

2022 was the year for cheaply valued stocks – referred to as value stocks – especially in the energy and commodities sectors. In the first half of 2023, however, the tide turned again in favour of growth stocks – especially in the technology sector. In the US market, the four companies with the largest capitalisation are among the strongest winners. Apple's share price has risen 45% since the beginning of the year, Microsoft's by 40%, Amazon's by 54% – and all are eclipsed by NVIDIA, with a share price increase of 185% (as of 27 June 2023). The rally was fuelled by falling bond yields, because lower interest rates benefit those companies most that are expected to make profits over the long term. Last year also appears to have been an exception. Over the past 13 years, growth stocks have always outperformed value stocks, with the exception of 2016. Whether this trend will continue in the second half of the year is in doubt, given that the possibility of a recession is still not off the table. Moreover, both value and growth stocks would incur losses in a downturn. Here, we are counting on the right signal from our

Neue Bank traffic light, which should then recommend us to hedge our equity exposure. The traffic light is still showing amber/yellow, which means neutral equity exposure.

Currencies

In mid-June, the Nikkei 225 rose to its highest level since 1990. At the same time, the Japanese yen fell to an all-time low against the Swiss franc. This interaction – strong equity market, weak currency – happens very often with Japanese equities. Using our currency indicator, we try to identify those times and then hedge our JPY positions. Since December 2019, the signal has indicated a hedge versus the Swiss franc. At that time, the JPY/CHF was at 0.90, while it is now at 0.62. As an investor in Swiss francs, this means a considerable loss of 30%. In the same period, the Nikkei gained 40%. After deducting the currency loss, this leaves a gain of only 10%. In our CHF mandates, we have consistently hedged the JPY positions since receiving the signal, which has enabled us to avoid the strong currency loss.

Alternative investments

Despite the announcement by Saudi Arabia at the beginning of June that it would cut oil production by 1 million barrels per day, the oil price is trending weaker and has lost about 15% since the beginning of the year (Brent and WTI). The reasons for this negative trend might include high inventories and the risk of a possible recession. The clear trend towards greater climate protection might also contribute to weaker oil demand in the longer term, given that OECD countries are increasingly aiming to replace fossil energy sources with cleaner alternatives.

PRIMUS–ETHICS

With the PRIMUS-ETHICS asset management mandate, we give investors the opportunity to incorporate environmental and social considerations into their investment decisions alongside financial aspects. We invest your assets in ethically and morally sound companies and apply professional approaches to their implementation. Scientific studies prove the positive effects of sustainability on economic success. Neue Bank AG's client advisors will be happy to show you the special features of this asset management solution in a personal meeting.

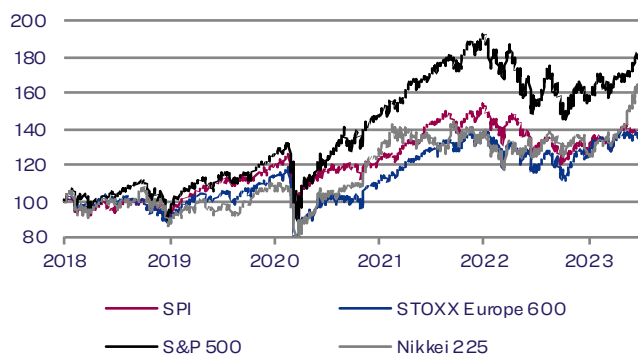
Key Performance Indicator in USD¹

| | 30.06.2023 | 2022 | 2021 | 2020 | 2019 | 2018 |
|-------------------------------------|------------|---------|--------|--------|--------|--------|
| PRIMUS-ETHICS Equities World | 19.25% | -28.69% | 31.27% | 23.34% | 31.89% | -4.76% |
| Peergroup | 12.19% | -23.66% | 17.85% | 22.56% | 26.63% | -9.71% |

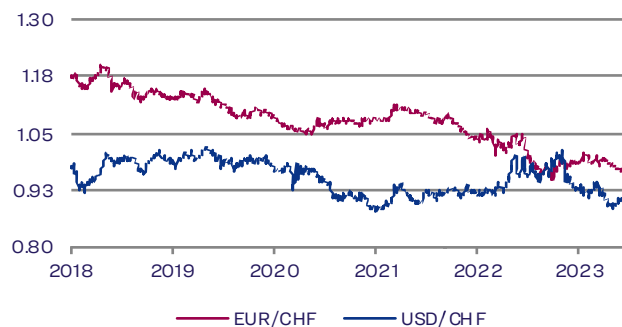
¹ Past performance is not an indicator of future performance and offers no guarantee of success in the future. The presentation of performance is gross without taking into account your individual tax liability. The net performance is lower due to fees. You can also find Our Opinion on our website: www.neuebankag.li S.E.& O.

Market data

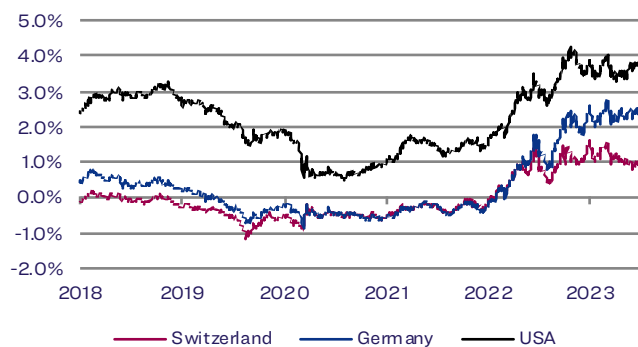
Stock market (indexed)



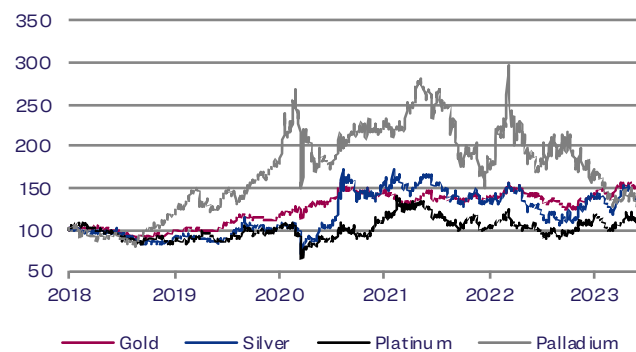
EUR/CHF and USD/CHF



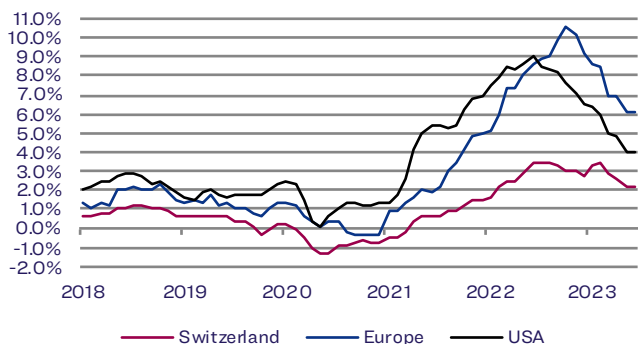
10-year government bond yield



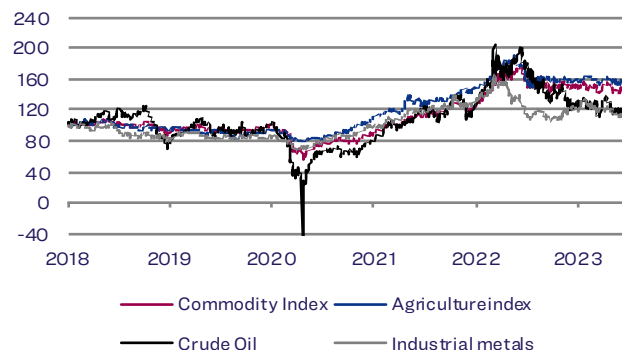
Precious metals (indexed)



Inflation rate



Raw materials (indexed)



The price developments are shown over 5 years.

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