LMM COMPASS

Dear reader

Interest rates are one of the most important parameters of our economy. They influence not only the money and capital markets but also the investment activities of companies, the real estate market, rental prices or consumer behaviour. If one believes the current forecasts of most economists and market participants, we have already come close to the end of the current interest rate tightening cycle. In anticipation of a prolonged phase of high interest rates, we therefore highlight this time the compound interest effect in our specialist article.

Jürg Meier
Partner, CEO

Gerhard Seger
Member of the Management Board

THEMES

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MARKETS AND STRATEGIES

After a surprisingly positive first half-year on the capital market for many market participants, the tide has turned in the third quarter. In the USA, the Fed's signal that it would probably leave interest rates at a higher level for longer than generally expected drove yields on 10-year US government bonds to 4.5%, their highest level since 2007. Partly weaker economic data and continuing inflationary pressure caused increasing volatility. The global equity index lost 3.4%, while bonds fell by 3.6%. Gold, the classic "safe haven", also lost 3.7% in value. (Note: All in USD in Q3 2023)

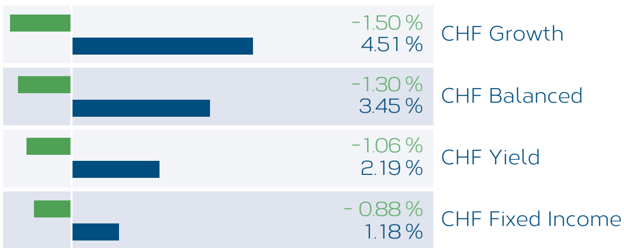
In the third quarter, all of our strategies recorded a negative performance. Since the beginning of the year, however, all of our strategies have also remained in positive territory and it is still true that the higher the equity exposure, the better the performance in the current year. The results for the first nine months range between +1.2% and +6.5% (note: reference currencies CHF and EUR).

		Value	% QTD	% YTD	Currency
Currencies	EUR / CHF	0.97	-0.77	-1.91	
	EUR / USD	1.06	-2.95	-0.79	
	USD / CHF	0.91	+2.25	-1.13	
	USD / JPY	149.22	+3.24	+13.10	
Bonds	Switzerland		+0.06	+3.63	CHF
	Europe		-1.63	+0.59	EUR
	USA		-3.23	-1.21	USD
	EMMA (Hard Currency)		-2.40	+1.06	USD
	Inflation Linked		-5.08	-2.58	USD
	High Yield		-0.17	+5.05	USD
	World		-3.59	-2.21	USD
Equities	Switzerland		-3.23	+3.89	CHF
	Europe		-2.06	+8.83	EUR
	North America		-3.18	+13.13	USD
	Pacific		-2.65	+5.51	USD
	EMMA		-2.93	+1.82	USD
	World		-3.40	+10.06	USD
Alternatives	Real Estate		-5.59	-4.10	USD
	Commodities		+3.31	-7.06	USD
	Gold		-3.68	+1.35	USD
	Private Equity (listed)		+4.52	+21.21	USD
	Hedge Fonds		+0.75	+1.38	USD

Calculation LMM; Period 01.01.– 09.30.2023

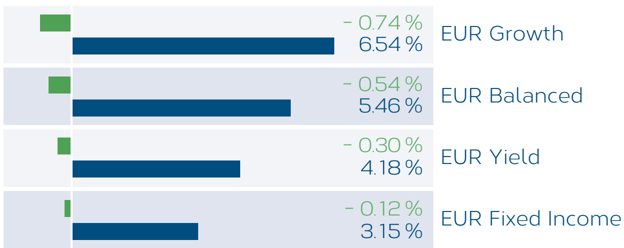
Investment strategies in CHF

QTD YTD



Investment strategies in EUR

QTD YTD



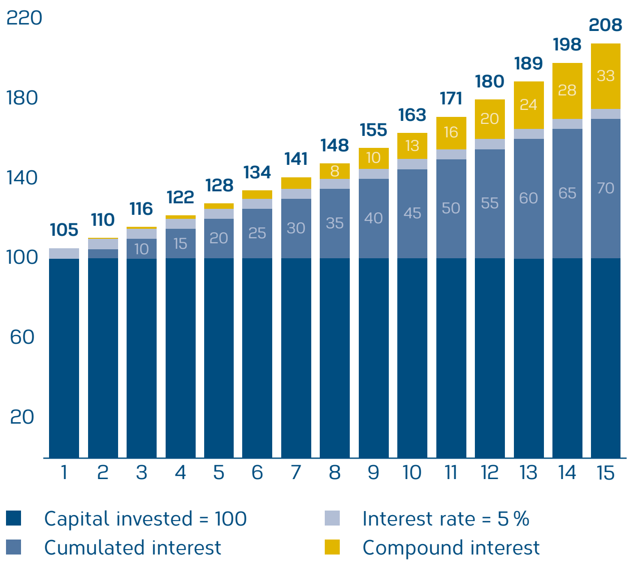
Note: the figures are before costs
Calculation LMM; Period 01.01.–09.30.2023

COMPOUND INTEREST EFFECT

The most important central banks have turned the interest rate screw vigorously in recent months and the expected interest rate hikes have now become reality. The market assumes that interest rates have already peaked, or at least have almost peaked. Moreover, looking at the yield curves, the expectation is gaining ground that interest rates will probably remain at elevated levels for some time to come. This means that investors can expect substantial interest income again. And thus the compound interest effect, which had almost been forgotten, is gaining in importance again. Or as Albert Einstein put it:

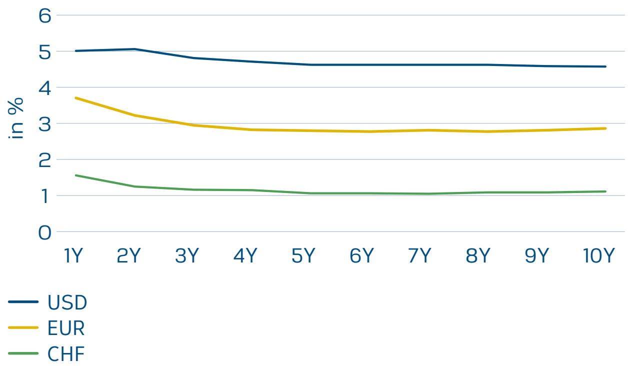
"The compound interest effect is the eighth wonder of the world. Those who understand it earn money and those who don't, pay for it."

In the past period of low interest rates, investors have come to terms with the fact that risk-free investments do not yield a return. In the coming years, things will look very different, as the following example illustrates.



Graph 1: Compound interest effect/source: LMM

Example: We assume an invested capital of 100 and assume a constant interest rate of 5% over the next few years (note: the interest rate assumption roughly coincides with the USD interest rate curve as of 30.09.2023, see graph 2).



Graph 2: Interest rate curves as of 30.09.2023 CHF, EUR, USD/source: Bloomberg, LMM

The performance of our investment can be divided into three components.

- The first component is the invested capital, which remains constant at 100 and is paid back at the end of the term.
- The second component is the annual interest of 5%, which adds up linearly over the entire investment period and will amount to 75 after 15 years.
- The third component, compound interest, assumes that the interest received can be continuously reinvested at the interest rate of 5%. Compound interest (marked in yellow) then develops exponentially and contributes more and more to the overall performance over time. In the example, it grows from practically 0 in the first years to a total of 33 after 15 years.

SPECIALIST ARTICLE

If we look at the total return over time, we see a doubling of the invested capital after about 14 years. As a rule of thumb, the rule of 70 can also be used to calculate the time needed to double the invested capital.

Rule of thumb: $\frac{70}{\text{Yield in \%}} \approx$ Number of years

Example: $\frac{70}{5} \approx$ 14 years

In summary, it can be said that in the current interest rate environment and with the help of the compound interest effect, interest income cannot be neglected. However, in order to achieve a real increase in value, the admixture of other asset classes (especially shares) will continue to be necessary.

LMM INSIDE

Our service requires a trusting relationship with our clients. Our employees are the key to this.

In our "LMM Inside" section, we therefore want to regularly introduce you briefly to members of our team.

RALF VETSCH

Ralf Vetsch has been part of LMM Investment Controlling Ltd. since 2023. In his position as Investment Controller he is responsible for private und institutional clients. He possesses a comprehensive education and long-term professional experience in the field of risk, financial und investment controlling at various financial institutions in Liechtenstein.

Content:
LMM Investment Controlling Ltd. (Head office)
Zollstrasse 32 · P.O. Box 174 · LI-9490 Vaduz

www.lmm-ic.com

LMM Investment Controlling Ltd. is an independent provider of investment controlling services and represents the interests of private and institutional clients vis-à-vis banks and asset managers. In addition to its headquarters in Vaduz, it has offices in Baar, Frankfurt, Vienna, Dubai and Sydney.