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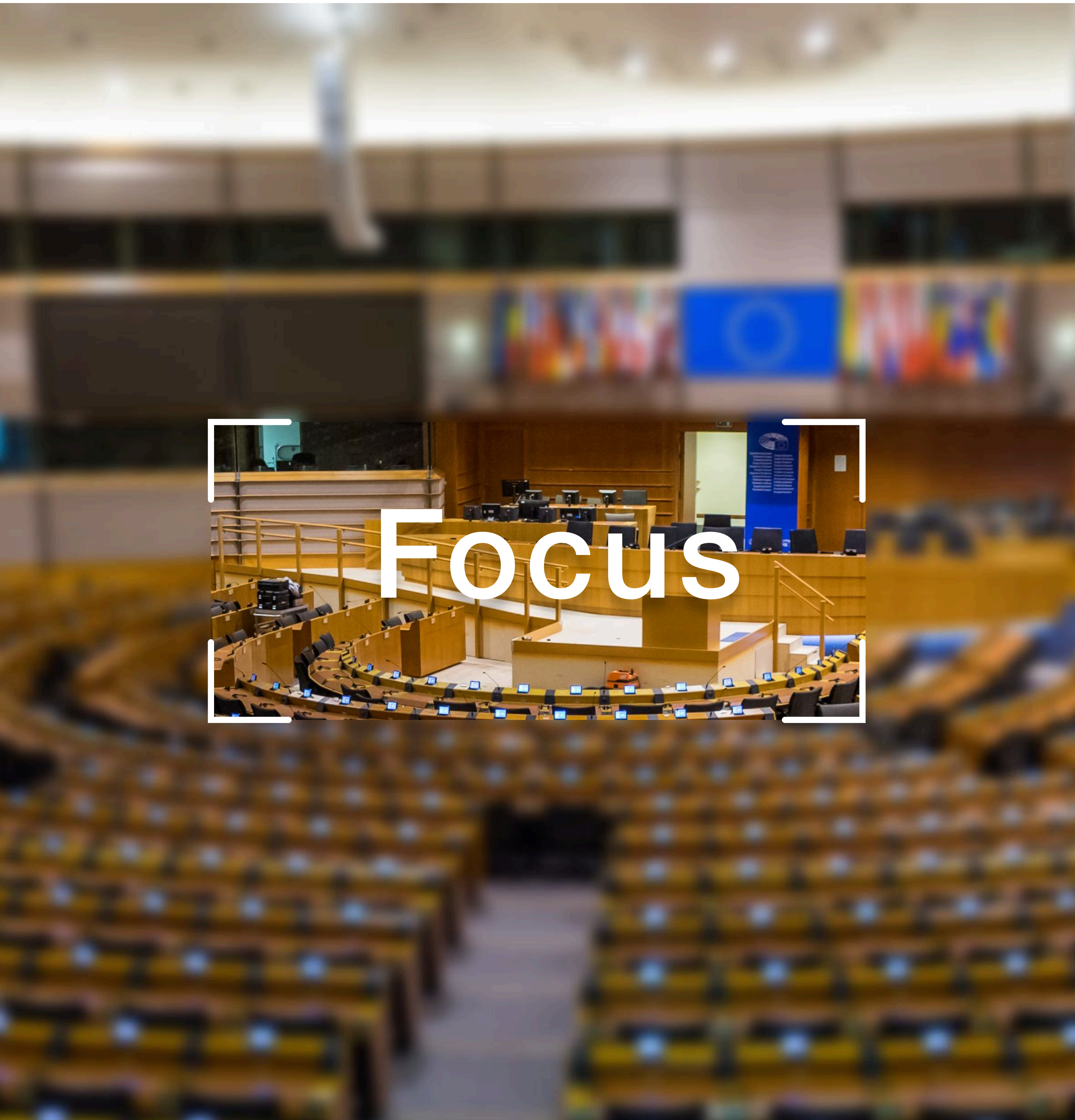
From Europe to Korea: Managing Risks in a Politically Volatile World

December 9th, 2024

CREATIVITY WITHIN EXCELLENCE



From Europe to Korea: Managing Risks in a Politically Volatile World

2024 was expected to be a year of significant political turmoil, with nearly half the world's population heading to the polls. As the year draws to a close, however, it is clear that much of the political turbulence was due to unforeseen events, while many of the expected elections proceeded without major disruption. A prime example is the U.S. election which was concluded quickly and decisively, with no uncertainty or violence.

French political crisis

The situation in France is more complex. After the European elections, President Macron called for early parliamentary elections, which resulted in a fragmented parliament divided into three blocs. As a result, he formed a coalition government in early September that appeared fragile and lacked a parliamentary majority.

As expected, the government led by Prime Minister Michel Barnier did not survive the budget process in the French Assembly. On December 4, he was ousted following a "motion of censure" passed by a coalition of the far right and far left as the government attempted to implement a deficit-cutting budget.

The new government (which hasn't even been appointed yet) will face the same difficult parliamentary equation, especially given France's limited tradition of coalition building. As a result, the country is likely to suffer months of political, fiscal and regulatory uncertainty. This could undermine consumer and investor confidence, with France's risk premium likely to remain elevated, corporate investment weak and GDP growth potentially impacted[1].

France is in an "excessive deficit procedure" initiated by the European Commission, but the sustainability of its public debt is not in question. The situation is not comparable to the Greek debt crisis or the Truss mini-budget that triggered a debt crisis in the UK in 2022. France's ability to collect taxes is intact and several parties share a genuine willingness to reduce the budget deficit. In addition, France continues to benefit from a strong institutional investor base, with all bond sales oversubscribed. Investors are demanding a premium to sanction France's political uncertainty, lack of public spending efficiency and fiscal discipline.

Breakup of the German coalition, for the better?

Like its runner-up, Germany, the eurozone's largest economy, is struggling with political uncertainties. On November 6, the Social Democratic Chancellor, at odds with his liberal allies over economic and budgetary policy, fired his finance minister, C. Lindner, after he refused to suspend the debt rule to allow for more aid to Ukraine. Therefore, M. Scholz has decided to call for a vote of confidence in parliament, which will take place on 16 December and is expected to trigger early general elections at the end of February 2025.

The situation in Germany seems similar to that in France, but the stakes are different. Germany is facing cyclical and structural economic difficulties, partly due to the debt brake rules. With the CDU indicating flexibility on the debt brake, there is hope that the rule could be modified in 2025, paving the way for higher public investment to help modernize infrastructure, raise productivity and increase potential growth.

A trial for South Korea's democracy

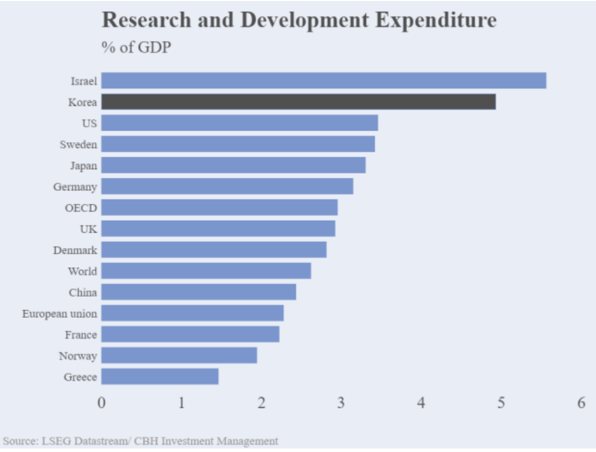
Meanwhile, the Korean president's attempt to impose martial law failed. Just six hours after declaring military rule, the parliament voted it down. President Yoon survived an impeachment vote (six opposition parties failed to secure a two-thirds majority). He is now under investigation on charges of treason and abuse of power but remains in office as part of a deal with his party.

This episode triggered a foreign exchange and liquidity crisis, forcing the Bank of Korea to intervene to increase short-term liquidity and take measures to stabilize the Foreign Exchange market. The Korean won has been under

[1] *We invite you to read our in-depth analysis of the potential economic impact of the political turmoil in France, published in July: [Focus: France's political turmoil - Potential economic impacts - CBH Bank | Compagnie Bancaire Helvétique]*

pressure since the beginning of the year and this political drama has triggered another sell-off.

Markets fear a power vacuum at the top of the government and question the resilience of South Korea's democracy. However, Korea offers quality names - globally competitive companies in key growth areas - and a favorable macroeconomic backdrop. Thanks in part to a diversified industrial base and high private and public investment in R&D spending, the economy has been officially upgraded to developed status by the United Nations Conference on Trade and Development in 2021. Korean government bonds are scheduled to join the FTSE Russell World Government Bond Index in November 2025.



Moving forces

Domestic political turmoil and geopolitical risks are moving forces. While risks in the Middle East have de-escalated thanks to the ceasefire between Israel-Hezbollah, the fall of the Assad regime in Syria has thrown the region into uncertainty. Elsewhere, the polarization between the United States and China is increasing, with implications for supply chain organization and third countries. Korea is a prime example. The country has to navigate a new geographical course and may have to choose sides.

Geopolitical and political risks have a significant impact on growth, commodity prices, currencies, inflation, financial markets and the supply chain. We expect political and geopolitical risks to remain high in the coming years due to structural shifts at play, including demographic and technological megatrends, geopolitical tectonic forces, and deteriorating bilateral relations.

While geopolitical tensions and political uncertainties can be challenging, they also present both risks and opportunities for investors. Effective risk management through diversification is essential to mitigate the impact of such events, as is the ability to assess contagion risks promptly and accurately. Additionally, maintaining a focus on quality stocks with strong balance sheets and diversified operations enhances portfolio resilience. On the opportunity side, periods of market volatility driven by geopolitical events often create attractive entry points, where asset prices deviate significantly from their intrinsic value. Active and structured management is key to navigate these complexities, positioning discretionary management services as a valuable tool for confident and informed decision-making in a dynamic global environment.

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Geneva

Headquarter CBH Bank
Bd Emile-Jaques-Dalcroze 7
P.O. Box 1211 Geneva 3, CH cbhbank.com
t +41 22 839 01 00

Zurich

Branch Office
CBH Bank
Bahnhofstrasse 82
P.O. Box 1213
8021 Zurich, CH
cbhbank.com
t +41 44 218 15 15

Luxembourg

SICAV 1618
Investment Funds
106, route d'Arlon
L-8210 Mamer
Grand Duché de Luxembourg
1618am.com

London

Subsidiary
CBH Wealth UK Limited
2-4 Cork Street, London
W1S 3LG, UK,
cbhbank.com t +44 207 647 1300

Hong Kong

Subsidiary CBH Asia Limited
Suite 2001, 20th Floor,
K11 ATELIER, 18-24
Salisbury Road, Tsim Sha Tsui, Kowloon, Hong Kong, HK
cbhbank.com
t +852 2869 0801

Nassau

Subsidiary
CBH Bahamas Ltd.
CBH House, East Bay Street
P.O. Box N-1724
Nassau, N.P., Bahamas
cbhbank.com
t +1 242 394 61 61

Rio de Janeiro

Subsidiary 1618 Investimentos
Av. Ataulfo de Paiva, 204 Salas 305 a 308
Leblon, Rio de Janeiro/RJ
CEP: 22440-033, Brazil
1618investimentos.com
t +55 21 3993 6901

Sao Paolo

1618 Investimentos Subsidiary
Rua Iguatemi, 192
Itaim Bibi, São Paulo -SP
CEP: 01451-010 Brazil
1618investimentos.com
t +55 11 4550 4401

Tel Aviv

Representative Office
CBH Bank
Rehov Tuval 40
Ramat Gan 5252247
Israel
cbhbank.com
t +972 73 793 62 22

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All data as of of December 9th, 2024
Published on December 9th, 2024

Creativity within Excellence

CBH | Compagnie Bancaire Helvétique

Asset Management
Boulevard Emile-Jaques-Dalcroze 7
P.O.Box
CH - 1211 Geneva 3

am@cbhbank.com
www.cbhbank.com