NEWSLETTER

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The dusk of 2020 gives way to the dawn of 2021

The yearend featured a series of positive announcements, including a Brexit deal between the European Union and the UK, an agreement in the US between Republicans and Democrats on a new stimulus plan, and the start of Covid-19 vaccinations in developed countries in general. On the other hand, the pandemic continued to expand rapidly, and new social distancing restrictions are expected (in the UK, Japan and Germany, among others). Central bank support remains essential. The Fed is therefore continuing its asset purchases pending “significant further progress” in the recovery, and the ECB announced the expansion and extension of its bond purchases and refinancing operations.

Market trends

Global equities gained 4.2% in December, with emerging markets (+7.4%) outperforming Europe (Stoxx 600: +2.6%). In the United States, small caps continued to lead the way (Russell 2000 +8.7%, vs S&P 500 +3.8%), while the Value vs Growth rotation did not last into a second month (-1.8%). US yields rose slightly (US 10Y +7bps to 0.91%). After declining in November, gold rallied (+6.8%) and the dollar weakened further (DXY -2.1%, EUR/USD +2.3% at 1.2225). In Switzerland, the LPP pension fund indices *(indices de la prévoyance professionnelle)* ended the year in positive territory at +3.2% for the LPP25+ and +3.1% for the LPP40+.

Market performance as of 31 December 2020

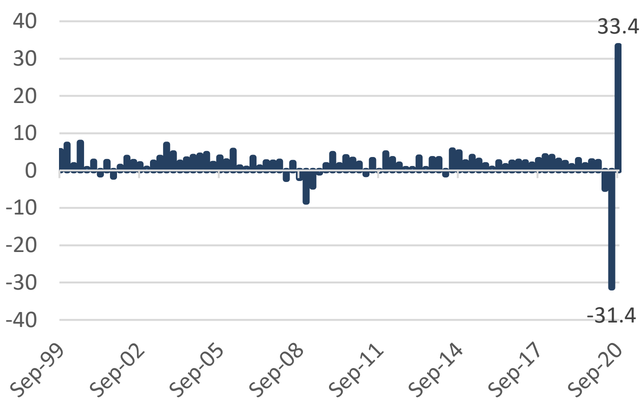
STOCKS MARKETS	LEVEL 31.12.2020	CHANGE SINCE 30.11.2020	CHANGE SINCE 12.31.2019
Index			
MSCI World	2690.0	4.24%	15.90%
USA			
Dow Jones Ind	30606.5	3.41%	9.72%
S&P 500	3756.1	3.84%	18.40%
Nasdaq Comp	12888.3	5.71%	44.92%
Europe			
Euro Stoxx 50	3552.6	1.77%	-3.21%
SPI (Switzerland)	13327.9	2.50%	3.82%
CAC 40 (France)	5551.4	0.71%	-5.57%
DAX (Germany)	13718.8	3.22%	3.55%
FTSE 100 (UK)	6460.5	3.28%	-11.58%
Japan + Emerging			
Nikkei 225	27444.2	3.93%	17.80%
CSI 300 (China)	5211.3	5.07%	29.62%
MOEX Index (Russia)	3289.0	6.28%	13.78%
S&P BSE Sensex (India)	47751.3	8.18%	17.16%
Ibovespa (Brazil)	119017.2	9.30%	2.92%

BONDS & ALTERNATIVES MARKETS	LEVEL 31.12.2020	CHANGE SINCE 30.11.2020	CHANGE SINCE 12.31.2019
Rates			
Germany 10 y	-0.57	0 Bps	-38 Bps
France 10 y	-0.34	-1 Bps	-46 Bps
Italy 10 y	0.54	-8 Bps	-87 Bps
US 10 y	0.91	7 Bps	-100 Bps
Debt			
Investment Grade US	343.37	0.52%	8.96%
Investment Grade Europe	266.21	0.17%	2.77%
High Yield US	2338.05	1.88%	7.11%
High Yield Europe	420.19	0.79%	1.76%
Emerging Debt	933.68	1.79%	5.88%
Currencies			
EUR/USD	1.22	2.42%	8.94%
EUR/CHF	1.08	-0.26%	-0.40%
USD/CHF	0.89	-2.61%	-8.42%
Commodities			
Crude Oil (WTI)	48.52	7.01%	-20.54%
Gold	1898.36	6.83%	25.12%

Economic highlights

A year of superlatives. After suffering an unprecedented drop, the equity markets rallied robustly, cheering the outcome of the US elections and prospects that vaccinations would soon bring the pandemic to an end. All in all, robust asset class performances have contrasted sharply with the worst recession in post-war history.

US gross domestic product (GDP) growth (quarterly basis, in percentage)



Sources: Bloomberg, Pâris Bertrand

A "Great Dispersion" in all asset classes. As of the end of December, there was a noteworthy gap between the top sectors (consumer discretionaries at +49.9% and information technology at +45.6% in the US) and the laggards (financials at -2.8% and energy at -35.1%). Among commodities, precious metals, gold (+25.1%) and silver (+47.9%) held a wide lead over energy, with WTI down 20.5%.

A return to normal in sight? Ultimately, in the fourth quarter, most cyclical sectors (energy, financials, materials and industrials) took over from those sectors that had held up best since the start of the pandemic, i.e., technology, healthcare, consumer staples and utilities. Japan and Europe made up some of the ground they had lost to the US. The market's concentration on a small number of stocks (albeit blue chips) remained a source of instability (with the S&P 500's five biggest stocks accounting for more than 20% of the index). Even so, we see the market's broadening to other sectors as an "internal" factor in support.

"External" support factors are still in place. The confirmation of Joe Biden's election to the US presidency (following the Electoral College vote) and his appointment of Janet Yellen as Treasury Secretary suggest that fiscal and monetary policies will remain active and coordinated. The Fed has kept its USD 120bn monthly asset-buying programme in place, while the ECB has expanded its programme from EUR 500bn to EUR 1,850bn. Over the full year 2020, the Fed expanded its balance sheet by USD 3,200bn and the G4, its aggregate balance sheet by USD 8,500bn (a more than 50% increase in consolidated GDP terms). Meanwhile, the US has spent an estimated 17%-plus of its GDP on economic support in response to the pandemic. France and Germany have spent more than 20% and 30%, respectively, of theirs, and Japan, 55% of its, Japan being the country that has spent the most in fiscal support measures.

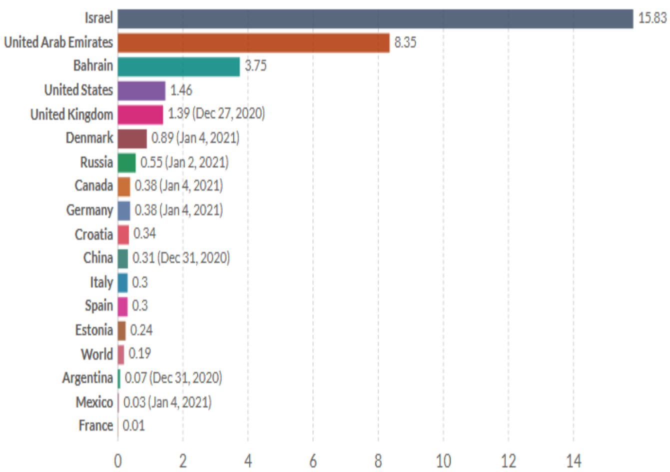
Brexit: Santa Claus leaves a deal under the tree. After four and a half years of bargaining and about-faces, the EU and UK at last reached an agreement guaranteeing trade without customs duties or quotas. In the US, Congress passed a second, USD 900bn stimulus plan. Biden said that the plan was a good first step but that more would be needed. A further extension is therefore possible in 2021. Vaccination campaigns have begun in almost all developed countries, opening the door to a gradual reopening of economies at some point in the first half of 2021. **The year 2020 ended with a series of favourable announcements.**

What is the impact of the pandemic? Social distancing measures that are more closely targeted and less severe than during the first wave have softened the blow to the economy and the labour market. Current lockdowns have slowed economic activity but without smothering it completely. Companies are better prepared, supply chains are intact, households have adjusted, and vaccination of the most vulnerable persons will lower the number of hospitalisations.

Supply, storage and wariness: the challenges of vaccination. Covid-19 vaccination roll-outs are a true logistics conundrum. In Switzerland, for example, 70,000 doses would have to be administered each day for six months to be able to vaccine 6 million persons twice. On top of the organisational aspects, the task is made even more challenging by the fact that fewer than half of the Swiss population says it is willing to be vaccinated (even though the vaccine will be free of charge) and that the acceptance rate could be even lower elsewhere in the world (in the United States and in France in particular).

We closely monitored the spread of the pandemic in 2020. In 2021, we will be keeping a close eye on vaccinations. To date (6 January), more than 15 million persons have already been vaccinated worldwide. Switzerland officially began its campaign on 4 January.

Number of Covid-19 vaccines administered per 100 persons



Source: Our World in Data

A double Democratic victory in Georgia. Biden had already thwarted prognosticators in this state that has been dominated by the Republicans since 1984. Then, on 5 January, both Democratic candidates won run-off Senate elections. The Democrats will now be in de facto control of the Senate. What a surprise and what a setback for the Republicans and Trump.

Good visibility on the economic recovery scenario in the second quarter after the relaxing of social distancing measures. Most investors have already priced in this scenario. We will see an improvement in traditional cyclical sectors and those services hardest hit by Covid-19. Small and midcaps also offer attractive prospects during this phase of the recovery.

What are some potential disruptions? Biden's victory is unlikely to create any great shifts in the balance of power with China, something that carries trade, technological and financial stakes for the US. The year has begun with stretched equity valuations. Markets are therefore vulnerable to any disappointment in earnings, as forecasts are already demanding. Interest rates are an additional risk. As they pass through to the real economy, will reflation measures evolve into an inflationary risk? A spike in interest rates could strike a blow to the two major asset classes of bonds and equities.

Investment decisions

The prospect for effective vaccines is a game changer. Our conviction is that the recovery will continue to unfold in the coming quarters. However, this assumption will depend on the pandemic's spread as vaccinations are rolled out, and will also be adjusted to the phasing out of economic support. In 2021, markets will be driven by corporate profits, rather than valuation multiples, which had already risen high in 2019 and 2020.

The recovery boosted other regions outside North America. In equities, we continue to recommend a diversified regional exposure in emerging markets, Japan and Europe, which offer cyclical exposure and benefit from a weak dollar. Selectiveness remains key, and we continue to prefer quality companies with solid balance sheets and competitive business models. We have added to our cyclical exposure with US small and mid caps.

We are maintaining a proper risk balance in our bond allocation between high-quality credit and the quest for higher-yielding debt. Domestic Chinese bonds, which continue to serve attractive yields, have been added to our portfolios. We are cautious on the long end of the curve, which is likely to rise.

Our portfolio construction also includes real assets such as gold and real estate round out, in order to address the imperatives of the macroeconomic and financial environment without undermining participation in market gains.

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