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Investment policy Q1/2021

English Version

BancaStato

"THE YEAR AFTER": shooting tests

Investment Policy

Although the so-called "second wave" of the Covid pandemic is still affecting the economic scenario, the arrival of vaccines is helping to generate confidence and optimism, together with the monetary and fiscal initiatives adopted by the various countries. In the USA, there is currently a great deal of expectation regarding the choices made by the new Biden Administration, not only in the economic and financial field, but also in the geopolitical one. Whilst in Europe the dangers remain for the conclusion of the process of divorce of the United Kingdom from the European Union.

Between the ominous 2020, which was however relatively positive in terms of financial market performance after the spring slump, and the start of 2021, there are several issues under debate. First of all, there is the alleged "decoupling" between the performance of the financial markets and the still uncertain, or even critical, state of the economy in various countries. However, this argument does not take into account the fact that markets, by their very nature, anticipate the cycle, which is expected to pick up in the New Year, albeit in different ways in different areas. In reality, recovery is already underway, and in a sustained manner, in China, and is also manifesting itself in the rest of the North Asian region, i.e. Taiwan, Korea and Japan.

China is also the subject of the second theme, the result between health and economic decision-making choices: the Dragon Empire comes out the winner by a wide margin, but the comparison with Western competitors must be weighed on the basis of the different political-institutional systems.

A third theme, increasingly relevant, is that of ESG investments (acronym of Environment, Social, Governance), i.e. sustainable in environmental and social terms, and in terms of ethics and accountability of governance and management: is this just a fad, an imposition destined to grow on the part of institutions, or a real trend for the future, also considering the different financing costs between ESG and non-ESG companies? The future will provide the answer, which in our opinion will be predictably positive but certainly not without controversy, both because many groups operate in different sectors and because many companies are transforming their business model, for example in the energy field.

Last, but certainly not least, the issue of debt dominates, which the pandemic has helped to further expand both for governments and for many private entities.

Our investment policy reflects all these points with a focus also on the political and geopolitical developments in which military actions are increasingly being replaced by economic and financial operations, as well as cyber attacks. At the turn of the New Year, the equity sector inevitably remains the one on which to focus.

Outlook

In 2021, a recovery is expected in a diversified form and more or less accentuated depending on the areas, with North Asia (China, Taiwan, South Korea, Japan) in the lead. In the United States, the new Biden administration is expected to launch new fiscal support plans, while the Federal Reserve is expected to continue for a long period with reference rates around zero. There is also expectation about Joe Biden's attitude towards open geopolitical issues, such as relations with Iran, which is escalating its actions in the Gulf, particularly with Saudi Arabia, with North Korea, and with Russia.

The European Union is in the process of launching the Recovery Fund, which creates many expectations especially among countries with more fragile economies, such as the peripheral ones, and the European Central Bank has further expanded its programs for purchasing securities and financing the banking system at ultra-favorable conditions. The question remains as to how much of the new liquidity created will benefit the real economy, i.e., businesses and households.

The major themes on the investment scenario are the "new" Green Economy, China, advanced and personalized pharmaceuticals, medical technology and communications.

Macro

The recovery will bring benefits in terms of employment, except in Europe, where unemployment appears destined to rise. This trend, together with the impoverishment of various segments of the population, may fuel social turbulence with political repercussions in the most fragile areas, such as Italy.

The year 2021 will bring the first benefits of the important RCEP (Regional Comprehensive Economic Partnership), a historic agreement with which 15 Asian countries, in addition to Australia and New Zealand (together almost a third of the entire world GDP), have signed a free trade agreement covering a myriad of areas, from intellectual property, goods and services, including financial, e-commerce, telecommunications, investments, health measures and standardization so as to break down all trade barriers. The agreement favors, for obvious reasons, especially Beijing's exports and supports the "dual circulation strategy" of President Xi Jinping. Now it will be interesting to see how other regions will react, starting with the USA, which risks losing its leadership position in the Pacific, and Europe.

An interesting aspect of the year that is about to begin certainly concerns the unknown factor of inflation: although the central banks will tend to maintain an interest rate policy close to zero, or negative, for a long time to come, slight inflationary tendencies could nevertheless arise in the second quarter due to strong QE policies, rising commodity prices and pressure on the labor market in the USA. What will be the effect on bond risk premiums and equity trends?

Fixed Income

If the Chinese stock market is increasingly a protagonist on the world stage, the bond segment, with it's almost 15 trillion dollars, has also become the second most important in the world and Beijing intends to soon make it a competitor for US Treasuries and German Bunds.
Moreover, the weak dollar and low interest rates generally favor issues from emerging countries, in particular from the Asian region or border countries.
In the European Union, the latest interventions of the ECB have contributed to a further reduction of spreads on peripheral issues, e.g. Italian BTPs, but have also led to an increased distortion of risk factors.
In the USA, yields on government bonds are marginally on the rise, but, as mentioned, they have to deal with potential inflation and the sustainability of economic growth, which could create a steeper American curve.
In the Corporate sector, spreads have almost all returned to pre-COVID-19 levels, primarily due to the "default" risks mitigated by political will aimed at stabilizing the market and central bank purchases.

Equities

Equity investment will also remain a compulsory choice in 2021, dictated by good growth themes and a lack of alternatives to other asset classes. We must therefore try not to get too enticed by a very positive market consensus and try to understand when it will be the right moment to turn defensive.
Geographically, China, "the place to be" also thanks to the possible new policy of openness of the White House, and other North Asian markets (including Japan, with many stocks decidedly undervalued) among the favorites.
Wall Street always in the limelight thanks to the support of macroeconomic data, liquidity and possible fiscal initiatives by the government. The growth potential for the year is 10-15%, but according to many analysts the market could positively surprise with much better results.
Europe remains an interesting opportunity in terms of valuations, despite the political-institutional risks. To be considered are the sectors of telecommunications, utilities and those industrial realities with a global footprint and good financial fundamentals.
The Swiss market maintains its interest thanks to the defensive nature provided by the pharmaceutical, food and industrial components.
One of the most important themes to remember is that of ecological mobility linked to the Green Revolution encouraged by governments at a global level, and that of activities linked to the medical sector and the ageing population.

Alternative Investments

The performance of many raw materials is recovering, from industrial metals, copper and platinum in the lead, to soft agro-foods and oil. The recent agreement at the enlarged OPEC has supported the market, as well as the fall in investments in recent years and the US shale oil crisis, but doubts remain about the trend in demand. The US shale oil crisis has led to difficult situations for issuers, who are heavily indebted, while the energy shares sector has to deal with ESG criteria that end up conditioning investments, starting with those of institutional operators.
Gold, after a good comeback, appeared under pressure at the end of 2020 but its prospects remain positive, thanks to the negligible if not zero rates, the weakening of the US dollar and geopolitical tensions.
Among the alternative strategies to be evaluated are Event Driven or Merger Arbitrage, which could benefit most from the acquisition dynamics linked to the large amounts of liquidity present on the markets.

Forex

For its part, the Swiss National Bank continues to expand its balance sheet in order to avoid an excessive appreciation. The stabilization with the euro appears to be in the 1.05-1.10 area while with the dollar it must accept a strengthening under the 0.90 threshold. The pressure on the Japanese yen as a safe haven currency has eased, the currencies of emerging countries offer long-term yield opportunities, subject to the relative risks.
Caution should be exercised with regard to the British Pound while awaiting the conclusion of the Brexit process. Bitcoin has touched new highs and is of increasing interest, along with blockchain technology, not only to private but also to institutional investors. Even some central banks, such as the Swedish one, are turning to it to evaluate virtual currency issues.

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