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Investment policy Q2/2021

English Version

BancaStato

THE GHOST OF INFLATION ON THE HORIZON

Investment Policy

The second wave of the Covid pandemic is followed by the third with more or less worrying variants of the virus, but expectations are growing for the positive results offered by the various vaccines and for a consequent, albeit gradual, return to normalization for the freedom of individuals and the activity of companies.

The new element that has intervened to condition the markets is the fear of a return of inflation, albeit to a limited extent, in the second half of the year. Reasons for this include the continuation of ultra-expansionary policies by the main national banks, fiscal stimulus implemented by various countries, and price increases in many raw materials, from energy and metals to agro-food products and technological components.

Adding to the tension are fears over pressure on the labor market in certain countries/sectors and concerns over the partial loss of the deflationary effect linked to globalization, as well as, obviously, the very high volumes of debt that are increasing. However, the emergence of inflationary pressure is curbed, among other things, by the low propensity to consume in many segments of the population and by labor markets that are still plagued by job insecurity and unemployment. Against this backdrop, the bond segment was penalized and the equity sector, which we still consider to be preferred, is suffering from increased volatility.

Outlook

Monetary policies that are still highly expansive, as recently announced by Jerome Powell regarding the strategy of the US Federal Reserve, fiscal initiatives, such as the 1.9 trillion dollar initiative launched by the Biden Administration, will support a recovery that, in the West, is nevertheless faced with high levels of debt and structural limits that require continuous recourse to stimulus. The situation is different in Asia, where China even closes an "annus horribilis" such as 2020 in positive territory at 2%, and other economies, from South Korea to Taiwan, from Singapore to Japan, appear well positioned in terms of both domestic consumption and exports. It is worth remembering the growing decorrelation of Asian areas from European and American economies thanks to the growth of internal trade within the Asia-Pacific area.

Macro

However, the recovery will bring benefits in terms of employment, except in Europe, where unemployment appears destined to rise. China's role as a driving force, the fruits of the RCEP (Regional Comprehensive Economic Partnership) program, as well as those brought to many emerging countries by higher commodity prices, together with progressive post-virus normalization, should lead to a mainly positive, albeit uneven, macroeconomic scenario, including within the European Union itself. GDP growth estimates for 2021 see a recovery of over 5% worldwide, with the more developed economies underperforming the emerging ones led by China (+8%) and India (+11%).

Fixed Income

In the USA, inflationary expectations and the potential effects of Washington's wide-ranging fiscal package have led to a not negligible increase in yields, which is clearly reflected in the curve of the ten-year Treasury Bond. For its part, the Federal Reserve continues its policy of bond purchases. In Europe, where it will be interesting to see the effect of the pressure on yields coming from across the Atlantic, the arrival of Mario Draghi as President of the Italian Council of Ministers has, at least for the time being, led to a further narrowing of yield differentials for "peripheral" bonds. However, in the future, structural problems, socio-economic destabilization linked to unsatisfactory use of the Recovery Plan, and further growth in debt despite the willingness of the ECB to purchase, could lead to investors demanding a higher risk premium. In the High Yield sectors, spreads have also improved, but the selection of issuers must be maintained due to the increasing risk of insolvency. Low rates and a weak dollar make the issues of many emerging markets attractive, starting with China, whose bonds, which now represent the second largest market in the world with approximately 13 billion dollars in volume, can provide a good opportunity for diversification. It is Beijing's intention to make government bonds in Yuan the third global benchmark alongside US Treasury Bonds and German Bunds. The complex and uncertain scenario we are facing may lead to stable reference rates for a few more years, however, in the face of inflationary fears that are pushing up market yields, making the yield curves even more steep, especially on the US dollar curve.

Equities

China remains the preferred stock market, and the "new course" defined in the last Five-Year Plan, with the development of domestic consumption alongside exports, the focus on digitalization and high-tech, the opening and liberalization of

financial markets, further favors Beijing's global position.
Japan has also returned to attract global investors, with the Nikkei reaching 30,000 again - after more than 30 years - thanks to good corporate earnings (among those in evidence, the successes of Toyota and Honda). We still maintain a positive approach, albeit slightly more cautious after the marked rally that Tokyo has recorded.
The U.S. market still presents good opportunities, especially after corrections such as those that occurred in some technology sectors. Despite possible volatile phases, we remain positive towards sectors more linked to the real economy as well as financial ones. E-commerce, which has experienced a strong rally thanks to the lockdown, also shows an excellent recovery after the consolidation phase. The average expectation on Wall Street is for a +10-15% at the end of the year.
Europe represents a short term investment opportunity thanks to attractive valuations, the normalization that vaccination procedures can bring and the political easing between the Atlantic shores that came with the election of Joe Biden. We prefer industrial, retail and automotive sectors with solid financial structures.
The Swiss market proves to be particularly interesting thanks to its industrial, luxury and pharmaceutical sectors.
In general, "green" mobility, demographic evolution and related products and services remain among the preferred themes. Environmental, social and governance factors, and the concepts of "sustainability" keep centre stage, stimulated by institutions which, in various countries, go so far as to set limits on management choices and which, in any case, influence the demand for "undesirable" companies, contributing to a transformation of the asset management industry which cannot be avoided.

Alternative Investments

The abundant liquidity and the fluctuations that have occurred in the bond and equity markets are also stimulating the action of alternative investment classes, such as hedge funds and, within them, those that pursue arbitrage strategies during corporate mergers and acquisitions, which are proving particularly successful.
In the commodities sector, the rise in oil prices was significant, thanks to the maintenance of the cuts made by OPEC+, despite the presence of creeping conflicts between Saudi Arabia and Russia, and the expectation of a normalization of demand to pre-Covid levels in the second half of 2021. Support also comes from the crisis in which the American shale oil sector finds itself, penalized by the political decisions to block the construction of the pipeline between Canada and the Gulf of Mexico and on the ecological limits envisaged for shale oil fields.
Among the industrial metals, copper, indicator of industrial and economic recovery in general, has shown an excellent recovery, as well as platinum, widely used in high-tech. Interesting is also the theme of secondary metals that are registering surges following their use in the green industry: platinum, cobalt in primis and rare earths of which Beijing has the almost-monopoly of processing.
Gold, the natural and preferred protection in the event of rising inflation, remains under pressure for the time being due to the marginal appreciation of the US dollar and above all the increase in its yields.

Currencies

As mentioned, the increase in yields on the greenback has blocked its depreciation and indeed caused it to rise slightly. Although debt and deficits are weighing on the currency, conditions may remain stable for the time being, barring a resumption of the downturn in the longer term.
The trend of the British pound is very positive, favored by the result of the anti-Covid action imposed by London and the "liberation" from the EU constraints in Brussels.
The Swiss National Bank is still expanding its balance sheet towards new historic highs, accumulating foreign currency in order to defend the franc from an undesirable appreciation, while many parties are calling for an "active" use of these reserves, for example with the establishment of a sovereign wealth fund capable of acquiring strategic holdings at an international level. A certain stabilization of the exchange rate with the euro just above 1.10 is to be expected.
Outside of the main currencies, for those seeking long-term returns, it may be interesting to diversify with Norwegian Kroner, which benefit from the rise in crude oil prices, with Australian Dollars, given the correlation with Chinese economic trends, and with the Yuan itself, which is now destined to play a greater role as a global currency.

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Axion SWISS Bank SA
Viale S. Franscini 22
CH 6901 Lugano
Switzerland

Tel: +41(0)91 910 95 10
Fax: +41(0)91 910 95 14
Web: www.axionbank.ch
Email: mail@axionbank.ch