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Q 02 / 2020

Quarterly Investment Review and Outlook

Our central base-case scenario is that global growth begins to recover during the 4th quarter 2020.

The duration of the pandemic is unpredictable, but prompt and coordinated policy action and the absence of economic very important imbalances argue for sustainable recovery once the virus threat clears.

The COVID-19 pandemic has uncovered a number of weaknesses our global economic system has developed since 1982. However, changes which were burgeoning even before the pandemic suddenly started experiencing real economic interest, especially with respect to new technologies enabling streaming and IT security.

Market assessment - Market valuation June 2020

#	Date stamp	Event	Next window	Reliability	Market sentiment / Action taken	Equity market implication
1	12.19 - 01.20	Supply chain concerns arise because of the outbreak of virus COVID-19		Event occurred - fully accounted for	Market participants assumed that virus could be contained within China	Negative
2	beginning 02.20	Start of spread out of COVID-19 outside China		Event occurred - fully accounted for	Market participants assumed that impact would be minor - Chinese supply chain gaps were being successively closed	Market is worried
3	06.02.2020	Turning point of new cases in China		Event occurred - fully accounted for	Market participants accounted for 2 to 3 weeks of concerns only	Positive
4	18.02.2020	Loss of control in countries without reported cases and with underdeveloped healthcare systems (Iran, Kuwait, etc.)		Event occurred - fully accounted for	Market participants still thought the virus could not impact DM	Mildly negative
5	21.02.2020	Cases ramp up in countries outside China that have developed healthcare systems (for instance, Italy)		Event occurred - fully accounted for	Market participants started panic selling	Because of low liquidity, markets decline over-proportionally. Decline occurs across all asset classes, irrelevant of diversification
6	09.03.2020	Saudi Arabia slashed its forward price on crude, bringing the cost per barrel to under $40		Event occurred - fully accounted for	The stress situation in the market increased once more; in particular, the US HY market spread increased to reflect concerns of default situations.	Negative
7	mid 03.20	Virus spreads to Europe and the USA - countries are on lock-down and/or establish quarantine zones	Lifting of quarantine expected around April 20, 2020	Reliable, with differences between the different regions	Market participants move to a "Muddle through" approach. Investors gain some clarity.	**Positive**
8	18 / 19.03.2020	CBs consider emergency spending/budget		Event occurred - fully accounted for	Market participants step back into the market	**Because of low liquidity, markets increase over-proportionally**
9	**20.03.2020**	**Consider which economic scenario prevails (V,U,W, or L). Research will focus on consumers' capacity to spend and the assessment of CB policies to help kick-start the economic system**	**Report to be out by 10.04.2020 (target date)**	n/a	n/a	n/a
10	**weeks 13 & 14 / 2020**	**SWOT on asset allocation**	n/a	n/a	X-Ref: Asset Allocation Report 04/20	Mildly positive
14	Q2/2020	Soft portfolio restructuring (if required)		n/a	n/a	n/a
15	May/June 2020	Pandemic expected to have peaked as people start self-immunization process		Unknown	Many influencing factors, but mainly depending on countries' mitigation & containment measures	**Positive**
16	June	EU lifts a taboo - The European Recovery Fund is being set up	July 2020	High	https://www.irisos.ch/Community/Blog.aspx?blogid=1037&title=A-taboo-lifts--The-European-Recovery-Fund	**Positive**
17	May/June 2020	The pandemic is still a concern for vast regions around the globe (e.g., India, South East Asia, LATAM). Regional clusters were found in Germany and Switzerland, while in the US there were about 500 new regional clusters.	July 2020	High	Pandemic-related matters get less attention by the investment community – it became a kind of new normal.	**Neutral to mildly negative**
18	> Q2/2020	Evaluate long-term impact of event and re-orientate portfolio		Unknown	X-Ref: Asset Allocation Report 06/20	n/a

Asset Allocation SWOT 06/20

Which asset class is preferable?

Asset Type	Sub-Category	Actual Positioning	Opportunity	V-SRS	C U-SRS	C W-SRS	C L-SRS
Cash / MMF	all categories	n/a	n/a				
Bonds	Supra	No active exposure	A period of massive and global wealth destruction is normally followed by a period of higher inflation. In this context, although government bonds and supras maintain the nominal value, they will return much less than the rate of inflation. The apparent security does not yield as expected in most	Negative	Negative	Negative	Positive
	Corporate IG	No active exposure	The biggest risk to IG bonds is that the COVID-19 crisis becomes a prolonged period of subdued economic activity. In this case, the number of rating downgrades will increase over-proportionally. However, we believe that even without this scenario, rating reductions will occur, and present YTM do not account for this. Corporates with strong cashflows that belong to an "already downgraded sector are to be favored. The list of preferred names include": BP, Total, ConocoPhillips, Chevron, ECOPETROL, Gazprom, Petrobras, Rosneft, and Pemex.	Positive	Positive	Positive	Negative
	Corporate HY	Some selective names	One of our favorite sectors is Energy. We believe in companies with low production costs, comparatively strong fundamentals, and access to capital. In terms of regions, Gulf Cooperation Council nations and Russia are best positioned to weather lower energy prices. US shale issuers of interest: US212015AH47 and US20605PAG63.	Positive	Positive	Negative	Negative
Credit	Main	Profit taking on Long Main vs X-Over	Alongside with the equity market correction, credit spreads have reached an all-time high. In fact, spreads in the major indices have reached their widest level since the GFC and have traded as high as the 96th percentile of spread level, measured over a 15-year period. We believe that the default ratio in the Main (120 biggest companies) will be very limited and, have therefore taken advantage of these conditions. Once conditions begin to normalize, a mean version is expected to occur, thereby offering investors a compelling risk-adjusted return. Product opportunity:	Positive	Positive	Positive	Mixed
	X-Over		The X-Over segment will suffer from an above average rate of default.	Positive	Mixed	Negative	Negative
FX	USD vs other CCY	The level of the euro is of limited concern given that international trade is running at subdued levels and ultra-low oil prices are supporting economies	A clear strategy on how the commonly issued corona bonds are backed up is required. More importantly, there is a need for confirmation that the Eurozone is not breaking up, nor are weaker members such as Italy exiting. Yield spreads across the Eurozone are not as wide as they were in 2012; this is very comforting. A unified strategy to tackle the crisis would certainly help the euro to rise relatively quickly to 1.20 and above vs. the USD	USD Positive	USD Negative	USD Negative	USD Negative
V-SRS: V-Shape recover		W-SRS: V-Shape recover					
U-SRS: U-Shape recover		L-SRS: L-Shape recover					
- E&OE - subject to change according to market conditions – full disclaimer applies							

Asset Allocation SWOT 06/20

Which asset class is to be preferred?

Asset Type	Sub-Category	Actual Positioning	Opportunity	V-SRS	ur	U-SRS	ur	W-SRS	ur	L-SRS
Equities	**Top down view**	We have a proactive stance on companies with an above average growth opportunity.	We think it is too early to be outright bullish on the market, as many uncertainties in the supply chain will continue to exist for quite some time to come. Also, consumer demand still needs to be assessed.	Not likely		Likely		Most Likely		Likely
Sectors	Communication Services	Active exposure to "FANG-type" equities	Advertising spending is expected to slow, which in turn should benefit e-commerce and digital platforms. While economic growth has collapsed, we believe that e-commerce and digital platforms will continue to benefit from a well engaged secular trend. Favoured names: AMZN & GOOG.	Positive		Positive		Positive		Mixed
	Consumer Discretionaries	Active exposure to "Luxury"	The worldwide lockdown is “discretionary” negative. Furthermore, the lasting impact of higher unemployment rates across the DM will impact consumer spending. High-end product providers and e-commerce-enabled companies will most likely continue to perform. Favorite names: LVMH, NIKE, and ADS.	Positive		Positive		Positive		Negative
	Consumer Staples	Active exposure to "Food & Beverages"	Demand should remain relatively resilient for products that satisfy everyday needs, despite disruption to the economy. Consumer Staples appear to be expensive and having a short rebound capacity once the market returns to normal. Preferred Names: Nestlé, Coca-Cola, Pepsi, McDonalds	Negative		Negative		Positive		Positive
	Energy	Active exposure to "Services and Equipment"	Due to oversupply, the collapse in oil prices has generated its first victims in US shale oil development. A disrupted supply-demand balance inevitably leads to restrictions in R&D, lower capex, and therefore, fewer field developments. However, this will at some point drive up spot prices. But for now, conditions are challenging across all sub-sectors – smaller operators are most at risk. Preferred Names: Chevron, Schlumberger, BP, Total, Royal Dutch Shell.	Positive		Positive		Positive		Negative
	Financials	Active exposure to "Payments - FinTech"	The fall in interest rates and the sharp slowdown in the economy will drive a steep drop in profits for banks. Pre-COVID-19, banks had about twice the capital than before the GFC. The short-term outlook is subdued for the broader sector. We see some value opportunities in payments and e-commerce-related operators, as these services will be used in spite of underlying economic conditions. Our preferred names are: Mastercard,	Mixed		Mixed		Mixed		Mixed
	Healthcare	Active exposure to MedTech	Healthcare = Value trap? At present, attention is focused on the healthcare sector, but we believe for the wrong reasons. The trend that will persist beyond COVID-19 is a consumer-driven healthcare economy – that is, the way people interact with the healthcare system. This is rather a very strong secular trend, in spite of short-term events. Our preferred names: Straumann, Novartis, Roche, GlaxoSmithKline, Medtronic, and	Mixed		Mixed		Mixed		Mixed
	Industrials	Active exposure to Robotics and Automation	The sharp slowdown in the global economy hits this sector particularly hard. This, coupled with slowing Chinese growth and the transition to developing the industrial internet of things (IIoT), generates a huge execution challenge. Companies that are first movers or that generate meaningful economic value for their customers should be favoured. Our preferred names are Siemens, Safran, Rheinmetall, Zebra, Cyberdyne,	Positive		Positive		Negative		Negative

Asset Allocation SWOT 06/20

Which asset class is to be preferred?

Asset Type	Sub-Category	Actual Positioning	Opportunity	V-SRS	ur	U-SRS	ur	W-SRS	ur	L-SRS
	Information Technology	Active exposure to IIoT (Semi, 5G, Stay-at-home)	Valuation remains high compared to the broader market. IT valuations look vulnerable as enterprise business spending slows. While the sector's strong balance sheets offer some safe haven appeal, the broader sector is expected to underperform over a six-month period. The roll-out of 5G wireless network technology is happening at full speed and requires substantial follow-up commands. Streaming and “stay-at-home” companies are beneficiaries of this occurrence. Our favoured stocks: Palo Alto Networks, Cisco, Ericsson, and Oracle Corporation, Atos, Fastly, Limelight Networks, Cloudflare, Square, Fortinet.	Positive		Positive		Mixed		Positive
	Materials	Active exposure to miners	This sector is one of the most correlated to global industrial production. The near-term outlook for commodities is clouded by oversupply. However, the expected dynamic growth in electric vehicle (EV) demand, as well as progress toward grid parity in electricity production, point to strong longer-term demand for lithium, copper, and transformation capacities. Our favoured names: BHP, Rio, Air Products and Chemicals,	Positive		Positive		Mixed		Negative
	Real Estate	No active exposure	Current robust dividend yields do not cover an expected NAV adjustment. In particular, we see headwinds (short and longer term) in the retail rent property market	Mixed		Negative		Negative		Negative
	Utilities	No active exposure	This defensive sector is attractive during times of increased uncertainty and very low interest rates, even though relative valuations are higher than long-term averages. The sector is capital intensive and a very slow mover, most likely missing out on opportunities such as generation, storage, and distribution of alternative energy. The sector will lag when market volatility subsides. Preferred names: -	Negative		Negative		Negative		Positive

V-SRS: V-Shape recovery — W-SRS: V-Shape recovery

U-SRS: U-Shape recovery — L-SRS: L-Shape recovery

Quarterly Report - Q02/2020

At a glance

Review – 2nd quarter of 2020

1. Economic sentiment and earnings revisions have started to improve since mid-May, 2020. The global Economy is starting to show signs of bottoming out, helped by a surging money supply and a very aggressive fiscal stimulus.
2. Market participants are eagerly waiting for the first companies to publish the Q2 figures. We expect the number of earnings downgrades to be important. However, equity price-to-earnings ratios have rerated sharply from their March lows.
3. By now, most DM countries have lifted full lockdown measures, which could in turn result in the resurgence of new virus clusters. Nevertheless, we believe that market volatility will remain in range; we also assume that the March lows will not be revisited.
4. Market participants will focus on fundamentals again, but this is somewhat difficult with the revival of protectionist trade policy talks (US-China trade war), the US withdrawal from the architectural pillars of globalization (such as the Paris Agreement on Climate, the Trans-Pacific Partnership, the World Health Organization, traditional Atlantic alliances, and global tax talks regarding Multi-Nationals).
5. The US administration is being challenged with wrenching social turmoil; this in turn suggests that global US leadership is further challenged.
6. We expect a mixed economic impact from the virus; consumer discretionary-related industry sectors are expected to suffer more than industry sectors providing basic requirements and new technology opportunities. While global Central Bank policy actions have averted a massive market rout, consumers should now turn back to generating self-sustaining economic renewal.
7. Historically implemented higher capital requirements for banks and insurance companies have proven efficient. Bank mortgage lending has also been prudent, and consumer balance sheets are reasonably healthy.
8. In the case of a resurgence of COVID-19, central banks have very limited firepower compared to previous recessions. The U.S. Federal Reserve and the Bank of England are close to the zero-lower bound. The Bank of Japan and the European Central Bank are already there. All central banks have already committed huge amounts to QE – can they go any further and what is the impact on the valuations of assets? Please refer to the valuation assessment on page 7.
9. World GDP growth will drop to -5.6% in 2020.
10. US and Japan GDP growth will be around -6.4% in 2020.
11. Eurozone and UK economies are now expected to shrink by around 7.1% in 2020.
12. In emerging markets, excluding China, GDP growth is now expected to fall by around 6% in 2020.
13. Chinese GDP growth will be around -3% in 2020.
14. GDP Recovery is hindered by labor market rupture and ongoing social distancing, but not due supply chain disruption, as was initially expected.
15. Return to pre-virus GDP is expected to take more than two years in the US and Europe, despite huge stimulus programs.
16. "Old themes" are resurfacing, such as the US-China trade war, tensions between Hong Kong and China, and a no-trade-deal Brexit.
17. The proposed EU recovery fund is a crucial positive step in the right direction for fiscal cooperation in Europe.
18. Significant new German fiscal stimulus plans will further support the recovery.
19. Downside risks have been revised lower but still dominate potential for upside surprises on the macro front.

Risks to our forecast analysis are relatively high. They include the following: a) opening up "too early" may lead to virus resurgence and renewed restrictions, b) a second wave in the fall, c) larger than expected second-round impacts of defaults, d) business closures, and e) unemployment hysteria.

Market recovery – valuation assessment

One should expect global EPS growth to be significantly lower than what was expected at the end of last year. Still, global equities have strongly recovered from their March 2020 lows, while at the same time PE valuations have retreated. The question of "Is the market irrational?" is therefore warranted.

Clearly, to justify valuations, we could explain and develop valuation principles here for each industry, sector, and economic player. Key ratios and fundamentals can explain much, but not all. It is therefore worthwhile taking a look beyond principles of standard valuations in order to explain and understand current market valuations.

In the aftermath of the financial crisis of 2007/2009 and the subsequent QE, star investor Warren Buffet was asked how much money he had lost as a consequence of the FC. The normally very subtle investor from Omaha responded: "I had 10,000 shares of Coca-Cola before, and I still have 10,000 shares of Coca-Cola now." What was he trying to say? Probably that he sees the valuation of a company not in nominal terms, but rather in terms of what the company produces and owns and in terms of being a fractional owner of the infrastructure. The external valuation given to these investments is therefore a question of mathematical appreciation. And that brings us to the point.

Let's assume the following: you buy a bottle of Coca Cola for USD 1 before a market event. To cover for a liquidity crisis, the central bank increases the monetary base by 10%. This in turn devaluates your 1 dollar to 91 cents. However, let's consider the *value* of the bottle of Coca-Cola. Theoretically, your bottle of Coca Cola should sell for USD 1.10 (because the consumer will pay with a denomination that is worth 10% less).

In practical terms, this is called *inflation*, and in monetary management language, it is referred to as *debasement*. By debasing their currencies, governments believe they can meet their financial obligations more easily or have more money to spend on infrastructure and other projects. Debasement holds negative consequences for citizens, as the risk for uncontrolled inflation rises. This further benefits the government by making government debts easier to pay off.

Now, let us shift from this theoretical point of view, back to reality. Debasement – along with some nascent but potentially groundbreaking technologies and the integration of new applications for our day-to-day lives – caused market valuation to grow to present levels very rapidly. The market did not move because of "value companies," but rather because of promising new innovations that offer growth and sustainability for the future.

Example: the truck company Nikola (NKLA) is valued at an astonishing $23.1 billion. This is because of their hydrogen technology. However, they have not yet manufactured a single truck. In comparison, Ford is valued at $25.7 billion, but it works and produces cars with a technology that will be redundant in a few years. The technology NKLA develops is paramount and if successfully pushed to the market, will be groundbreaking. The present valuation therefore represents a fraction of the future, and as investors, we are willing to invest on the future outcome of an undertaking.

This and companies in areas like artificial intelligence (AI), the Industrial Internet of Things (IIoT), 3D printing, drones, automation and robotics, and big data are already providing a real glimpse of the future. In the wake of these new technologies, and together with debasement, the entire market was propelled very quickly to today's high but still reasonable valuations.

Investment recommendations by type

1. Equities:

Short-term view:	-	Neutral
Medium-term view:	-	The question is no longer whether there will be a recession, but rather, how long will it take to recover. We expect that it will take up to 2 years to regain pre-pandemic economic conditions. We believe that equity markets are truly at their fair value at present! We remain strongly positive on strong secular trends, and in particular, 5G, IT security, and IT Services.

2. Bonds:

Short-term view:	-	Neutral
Medium-term view:	-	With the market correction behind us, we favor BBB and single A debtors, yielding in the range of 6% p.a. We recommend a focus on companies with strong historic cash-flows, as weaker companies will experience a rating reduction.

3. Credit:

Short-term view:	-	**Highly Attractive**
Medium-term view:	-	With spreads at an all-time high and Central Banks rolling a renewed bond purchasing program, a sharp recovery in 6 to 9 months can be expected.

4. Metals:

Short-term view:	-	Neutral
Medium-term view:	-	Neutral to negative: Historically, metals are a refuge play; however, that has only partially materialized.

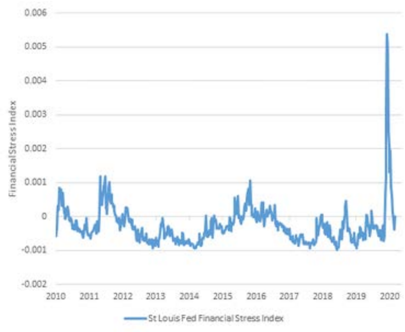
4. Commodities:

Short-term view:	-	Neutral
Medium-term view:	-	In the oil market, supply will outpace demand (because of lower economic activities).

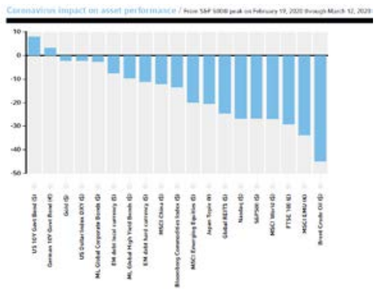
5. Structured solutions:

Short-term view:	-	With the market back to levels of prior to 2016 and an increased level of volatility, conditional capital guaranteed products offer an ideal risk/reward.
Medium-term view:	-	Longer-term investors should consider taking profit on the combined strategy of "Main versus X-over" and switching to a single credit strategy of "Main" only. The recent expansion in credit spread, coupled with the announced QE activity of CBs, is an ideal low-risk opportunity.

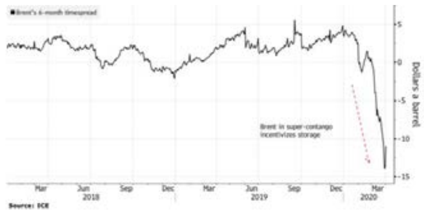
Financial stress level



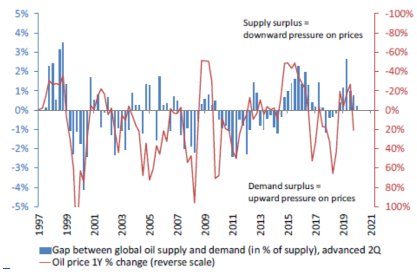
Market performances



Unsold oil impacting the spot price.



Excess of supply vs. demand before the crisis!



Investment recommendations by theme

We expect the global recession to be the deepest one in our lifetime; we won't be back to normal any time soon. Global GDP is projected to contract 3.8%, more than double 2009's -1.8% drop.

Economic activities are likely to remain severely constrained well into Q4/2020, even while assuming new infections in Europe and the US will have peaked in May/June.

Sharply rising unemployment and permanent income losses will limit consumption growth and thus weigh on economic growth beyond 2020. It is therefore opportune to focus on true **economic secular trends** and its key players, since these companies are best equipped to generate EPS growth over a prolonged period of time.

1. **Globalization 2.0:**

Short-term view:	-	Mixed
Medium-term view:	-	More than ever, we have entered in an adjustment of Globalization 1.0, resulting in excellent opportunities. In the near-term, the following issues need clarification: a) the US presidential election, and b) the political backdrop of COVID-19 for Europe. The creation of European Recovery Fund is the first step towards more a global European fiscal consolidation.

2. **From monetary policy to fiscal policy**

Short-term view:	-	Neutral
Medium-term view:	-	Fiscal and monetary policies are expected to be very accommodating for the quarters to come.

3. **Volatility**

Short-term view:	-	Neutral
Medium-term view:	-	Renewed volatility spikes can occur at any time, especially with the resurgence of concerns around the US-China trade war.

4. **Global order – a quick shift**

Short-term view:	-	Neutral
Medium-term view:	-	The impact of COVID-19 will not be over quickly, as there is substantial damage to consumer confidence, which will impact the global order. Globalization is entering a period of unparalleled adjustments that promise to transform industries for years to come.

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Reality checks

Valuations

The short-term pull-back in stock prices starting 2nd week June occurred on the back of persistent virus concerns in the US. In other regions, such as Latin America, India, and South East Asia, the management of the sanitary crisis appears to be more complex. All that together is a good reminder that markets have anticipated a return to normal for to early.

On the economic side, China's month-of-May data showed a relatively fast rebound on the supply side of the economy, but a much slower take-off in consumption, suggesting an L- shaped recovery of industrial activities, rather than the V-shaped one markets have been pricing. We are therefore more cautious on equities. Further short-term challenges lie ahead, such as Q2 corporate earnings, although **upcoming vaccine trials could diminish fears about a "second wave" of the pandemic in the coming weeks.**

Against a background of gloomy predictions, Chairman Jerome Powell committed to rock-bottom rates until at least 2022. Powell seemed unconcerned about the risk of "moral hazard" stemming from an accommodative rate policy. Back in 1996, Alan Greenspan's allusion to "irrational exuberance" was taken as a hint that the stock market might be overvalued. Back then, the aggregate forward 12-month price-earnings ratio for the S&P 500 was around 16x, compared to over 21x today. However, there is a crucial difference: back in the 1990s (and at the time of the bursting of the dot-com bubble in 2000), 10-year Treasury bond yields were over 6%, compared with below 1% today. Valuations are high, especially for growth stocks, but do not look so expensive relative to the discount rate and when taking into consideration the outlook for these stocks, which is better today than it was in the past. Based on these factors and as long as bond yields remain low, **higher equity multiples may be justified.**

An important European Council meeting is being held this week, during which we will see how strong opposition to the European Commission's proposals for a symbolically important recovery fund that includes non-refundable grants is. Even if no consensus is reached this week on the fund, we believe Angela Merkel is eager to leave a positive political legacy, meaning there is a good chance we will move forward on burden sharing in the euro area. This would make euro assets fully investable again.

Supply chains

Global supply chain management means that the world economy will only be as strong as the weakest link. Therefore, global trade could be the ultimate loser.

Companies particularly exposed to China and its manufacturing sector experienced outsized damage in the early days of the coronavirus outbreak. The fallout eventually spread around the world as supply chains were disrupted.

While China has since largely recovered, while still facing new clusters, other regions have not yet returned to past supply-chain efficiency. Even with COVID-19 resolved, China isn't out of the woods, as renewed US-China trade tensions can occur at any time.

Tech is king

Among the few sectors that largely weathered the coronavirus plunge, tech stocks have since driven major indices to their current levels. The sector's strong performance is likely to continue with the pandemic speeding up the global transition to remote work and to greater use of streaming services.

The tech-led rally comes with its own risks. Retail investors' exposure to technology stocks was elevated before the outbreak of coronavirus; they then massively reduced their exposure across all instruments. As of today, the market rally experienced since in the 2nd quarter mostly occurred without retail investors. Crumbly retail investors have yet to join new secular trends such as "stay-at-home" and "Digital-All." Still, tech giants aren't immune to negative earnings surprises, and some major tech names may falter at some point. That may have collateral effects on the entire market.

Market-by-Market View

United States:

US economic activity: a long slog back toward the new normal!

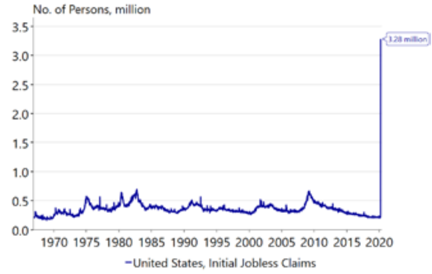
With lockdowns slowly being relaxed, economic activity has begun a long slog toward "normal." For example, Google mobility statistics at the end of May show activity at "retail and recreation" locations down 25% from January levels, an improvement compared to the trough in early April when the series was 45% below January. Similarly, the Dallas Fed Mobility and Engagement Index shows a gradual uptick from the bottom in April, though at a pace that varies widely across the country. Even while writing this report, Apple and other high frequency stores announced renewed store closures in some pandemic hot-spot regions. Such high micro-indicators remain key in tracking the speed and shape of recovery.

Meanwhile, lagged traditional macro data are beginning to confirm the depth of the unprecedented economic collapse in late March and April, which was foreshadowed by the various mobility and lockdown indices over the past few months. Our baseline real GDP outlook remains unchanged, with a forecasted 5.3% (global) contraction in 2020 and only a partial rebound of 4.2% next year. We expect economic activity to remain about 5% below its pre-COVID level until a vaccine is widely available.

Key takeaways:

- Our forecast for **a 6.4%** (USA) real **GDP contraction** in 2020 is unchanged.
- With lockdowns gradually relaxing, activity has begun a long slog back toward "normal."
- Downside risks remain elevated for the US, mainly from virus developments, but also from any re-escalation of US-China tensions.
- Reopening in the US is occurring earlier in the virus curve compared to many other developed countries, heightening the risk of new waves of infection.
- Meanwhile, May's labor market trends point to some upside risk from a faster-than-expected return to work.
- April consumer spending was severely hampered by lockdowns; an uptick in consumer confidence and vehicle sales in May provide evidence of a start in recovery.
- Purchasing manager surveys indicate an improvement in activity in May from the April trough, though the indices still remain in contractionary territory.
- In contrast to the previous recession, housing markets are likely to be among the less affected sectors this time.
- The Federal Reserve's attention is soon expected to turn from putting out fires toward supporting the budding economic recovery.

Rise of unemployment in the US



Europe:

A deep plunge resulting in a number of highly favorable coordinated policy responses!

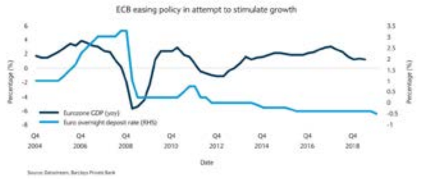
The euro area looks set to experience a short but very deep recession, with **full-year GDP** growth for 2020 expected **to decline by around 8%.** The level of activity looks set to fall around 20% (non-annualized) during the first half of 2020, before starting to normalize. For reference, the peak-to-trough decline in the euro zone's quarterly GDP was around 6% in 2008–2009.

While we forecast robust gains in the GDP in the second half of 2020, these gains are built on weak starting points, implying that by year's end, activity will still be around 5% below its 2019 peak and is unlikely to rebound to pre-COVID levels until 2022. This slow normalization comes from the need to relax lockdowns gradually, as well as from the collateral damage of the crisis through behavioral changes, damaged animal spirits, corporate defaults, and higher unemployment.

Some of this collateral damage will be mitigated by policy responses. We think euro area governments may end up tripling current fiscal easing efforts of around 2% of GDP in aggregate, which will be added on top of nearly 20% of GDP worth of guarantees and liquidity measures for companies. The euro area fiscal deficit is expected to rise to above 10% of the GDP, reasserting the need for the European Central Bank (ECB) to continue to anchor sovereign balance sheets. The ECB will do what is needed, extending its purchase programs if necessary. Expectations for a centralized pan-European fiscal effort are high, but the all-too-common political dealings may somewhat delay implementation.

Uncertainties around these macro estimates are high; the outcome depends on how quickly consumer behavior rebounds. All things considered, we view risks as skewed to the downside given the following factors: possible delays in containing the virus, the risk of a second wave of infections, and the potential for a slower recovery on the back of damaging second round effects from the crisis. Still, we believe the European continent will be less affected by a 2nd wave than others, since adherence to government instructions is higher than elsewhere.

ECB easing policy in attempt to stimulate growth



A large hit to growth, followed by an incomplete recovery

The coronavirus pandemic has seriously affected consumer spending, industrial output, investment, trade, capital flows and supply chains. The announced progressive relaxation of containment measures should pave the way for recovery. However, no recovery is expected from losses suffered this year by the EU economy before the end of 2021. Structural investments will remain modest and the labor market will not recover entirely.

Efficient policy measures at the EU and national levels in response to the crisis will be crucial to limiting economic damage and facilitating a swift, robust recovery that sets economies on the path of sustainable and inclusive growth.

In the Eurozone, the unemployment rate is forecast to rise from 7.5% in 2019 to over 10% in 2020, before declining again to 8.5% in 2021. More importantly, unemployment will hit people in developed regions with weak environments harder than elsewhere, which accelerates the trend of structural unemployment across the continent.

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Sector Analysis

Basic Materials

The Materials sector is very sensitive to fluctuations in the global economy. Concerns about the US-China trading relationship and now the impact of COVID-19 are relevant here. Accommodative monetary and fiscal policies have begun to improve prospects for global economic growth. This has allowed the U.S. dollar to trend lower, which historically provides a strong tailwind for the sector. In fact, recent relative performance has been quite strong, as the market shifted to a more cyclically oriented phase—even though the sector has not behaved this way in the past.

However, the sector still faces challenges. Global growth is not expected to provide an enduring tailwind to industrial metals or a demand for chemicals (the largest industry in the sector). Gas prices have rebounded off lows recently, along with the price of crude oil; weakness in demand for gasoline continues to weigh on ethanol demand and corn prices, further reducing demand for agriculture chemicals. Even moderately cheap oil prices and reduced cost of production will not make up for weak ongoing demand for chemicals.

Relative valuations are ranked average, as other sectors continued to see earnings expectations fall. While the underlying fundamentals remain challenged, earnings and revenue expectations have begun to recover amid budding global economic optimism—albeit from a very low base. Putting it all together, the sector is to perform sideways.

Investment opportunities:

The materials sector is also driven by better growth prospects, but it continues to suffer from weak earnings momentum amid a challenging commodity price environment. Within the sector, we have a positive stand towards Chemicals (Air Products, Linde, Sherwin-Williams) and Metals and Mining (Vale, BHP, Rio), as they tend to act as early cyclicals.

Consumer Staples

Due its composition, the Consumer Staples sector does normally outperform the average market during periods of economic slowdown and moments of stress.

Over the past years, retailers have aggressively restructured operations. In general, retailers have limited pricing power; the only way to improve returns is to efficiently manage costs.

COVID-19 related stocking of food and household goods has resulted in few negative earnings revisions, supporting the fundamental outlook. While our current view is for interest rates to remain low (which is a positive) the sector’s low sensitivity to the overall market would be a drag if the market continues to rally—leaving macro factors at negative.

Overall, the Consumer Staples sector is expected to perform in line with the average market, as no new impetus can be expected short-term. Volatility within the sector is thought to be above the average market, as assessing consumer behavior remains highly difficult.

Investment opportunities:

Longer-term Investment Trend - Nutrition

While both areas of interest include a large part of big data technologies and the Industrial Internet of Things (IIoT), it can be expected that producers that incorporate new technologies should grow faster than the GDP. However, because of very fast-changing consumer sentiments, earnings variability will be low. Therefore, their present development stage is close to venture capital but is part of sustainable investing strategies.

Traditional trends:

Preference is given to companies with predictable organic growth without the need to accelerate topline trends through acquisition, etc. In addition, we look for names that don't have the need to step up investment spend, as they have maintained a high level over time and margin expansion is being derived from sales growth rather than cost cutting. Companies with exposure to faster growing EM should be advantaged over companies with a strong DM exposure (BATS, KO, LISN, NESN, OREP, PEP, PG, WMT).

Key figures for Europe:

Target values:

Present fair value (DJStoxx600): 360
E12 months value (DJStoxx600): 390
Upside potential: +8.3%

Key economic ratios:

GDP Growth 20 (E)	-8.2
GDP Growth 21 (E)	6.2
CPI 20 (E)	0.3
CPI 21 (E)	1.0
P/E 2020 (E)	15.7
P/E 2021(E)	14.3
Div. Yield 2020	3.1
Div. Yield 2021	3.3

Most likely next short-term move:

DJStoxx600	flat/up
DJStoxx50	flat/up
SMI	flat/up
DAX	flat/up

Key names to look at:

Strong intellectual property:
- Roche
- Novartis
- Amadeus

High competitiveness:
- Siemens
- Daimler
- Gemalto
- Richemont
- Swatch

Sustainable dividends:
- ABN-Amro
- Imperial Tobacco
- Altria
- Philip Morris

Technology

Above all, we like the Information Technology sector's prospects, but remain concerned about some negative near-term factors, including the impact of the coronavirus epidemic and some ongoing supply chain issues. The phase-one trade deal between the U.S. and China, combined with a new trade pact with Mexico and Canada to replace NAFTA, have at least temporarily eased uncertainty.

Demand fluctuations related to COVID-19 (positive for personal computers, but negative for wireless phones and capital expenditures) are compounded by supply uncertainties surrounding any residual impact from the pandemic on supply sourcing, which could reignite trade policy risks.

The high valuation of the technology sector is justified because of above average growth opportunities and strong fundamentals relative to other sectors. Revenues and earnings were expected to grow over the next two years, but near-term estimates have declined due to virus-related concerns. Still, relative to other sectors downward revisions have been mild.

U.S. consumers had been willing to spend more on technology, but consumer confidence has begun to fall significantly. There is elevated uncertainty regarding incoming data, but the unemployment rate has dramatically risen above levels seen in the 2008-09 crisis, and is likely to sap demand for consumer products. On the corporate side, IT capex should remain high, especially as many institutions need to upgrade employees to more efficient and secure "work-at-home" conditions.

Balance sheets in the Information Technology sector appear solid, with large cash balances and relatively low debt. Companies have increased dividend payments, but there is an expectation for buybacks to slow amid the economic turmoil.

Capital expenditures have been below trend for several years, and a return to more normal spending levels would boost the sector. If one of the results of the pandemic is to partially reverse globalization, companies may turn to technology to replace increasingly expensive human workers.

The sector has lagged recently, as other cyclical sectors have taken the lead since mid-May; however, longer-term momentum remains strong. We believe the sector's risks are currently balanced with its return potential, and that a market perform rating on the Information Technology sector is appropriate for the time being.

Investment opportunities:

Retail exposure: A structural shift is occurring in consumer behavior, with spending on experiences increasing. People want to belong to a community and to share their experiences, which is reflected in the vibrant growth rates of social media networks. Increased demand for experiences will play out through greater spending on travel and entertainment, life-streaming services (leisure and conferencing), gaming, social media, restaurants, and food delivery. According to the IDC, digital data is enjoying exponential growth, with the global digital universe expected to cross 44 zettabytes by 2020, a more than 50-fold increase from 2010. We expect that this constant growth will continue well into the next decade; enablers are companies that will grow in terms of size and in terms of profits above the average market. Companies best covering these opportunities: CLDR, FSLY, NET

Corporate exposure: The near-term is highly uncertain due to COVID-19, and we believe investors should focus on technology companies that have attractive longer-term growth opportunities due to established franchises in large and secularly growing addressable markets, such as software, cloud, and security. The middle class is rising fast, especially in EMs. The aspiration to belong to a community is driving consumption, which mainly occurs online in these regions. It can be expected that e-commerce activities will grow on average by 15% annually during the next 10 years. This is possible because smartphone and internet penetration is very high and consumer-based platforms are becoming ever more user convenient.

In this vein, we highlight Microsoft, Palo Alto Networks, Salesforce.com, Splunk, and Accenture.

Expected Streaming Growth

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Communications Services

The Communications Services sector is concentrated in a handful of cutting-edge companies with which nearly 60% of world's population have contact on a daily basis—including search engine and social media companies, streaming services, and wireless telecommunications companies.

So far, COVID-19 has had a modestly positive impact on the sector, as some bigger companies within the key segments have had a tailwind from stay-at-home orders, which have increased demand for streaming entertainment. However, there has been a mixed impact on integrated telecom, as those with a primarily wireless product line have far outpaced those with business land-line services, which are expected to be negatively impacted by the recession. Meanwhile, multimedia, theme parks and traditional advertising-focused broadcasters have faced significant headwinds.

The larger companies that enjoy significant competitive advantages due to their dominance in their respective business lines—search engines, social media and telecom—also face emerging antitrust risks and other cross-border issues as international tax liabilities.

The rollout of fifth-generation (5G) cellular wireless technology could increase demand, as 5G is expected to increase speeds and allow for more exposure to the "Internet of Things" and automated car technologies—increasing growth potential. However, upgrading networks is capital intensive and not all providers will be able to keep up with the newest technology standards.

From a qualitative perspective, there is clearly a combination of positives and negatives to consider. When we assess the pros and cons through a more quantitative lens, we get a similarly mixed picture. The sector has been more sensitive to broad market moves historically, so a continued rally from the March 2020 lows would be a macro tailwind. In terms of relative valuations, the few individual companies that compose more than 50% of the sector are difficult to assess. Besides, the current Communication Services sector was only launched in 2018, replacing the narrower Telecommunication Services sector, so a comparison against the sector's own history is not practical. We *can* compare some of the fundamentals—such as return on equity and earnings revisions—with other sectors, and they are about average for the group.

We believe that many Communication Services companies face unique risks, but their strong competitive advantages within the industry also afford them potential rewards. However, balancing that against macroeconomic, value, fundamental and relative strength factors are neutral, in our view.

Investment opportunities:

The economy is progressing at a pace that is almost beyond belief. The fourth industrial revolution is in process of transforming our daily activities, the manufacturing sector, and the entire service industry (which is strongly interconnected with the communication service sector). In fact, we have two distinctive ecospheres: the digital world and our physical one. The result is that we have one global economy built on the back of bytes (content) and another composed of bricks and mortar (pure infrastructure).

The best way to understand structural trends that shape our daily lives is to take a deeper look into the companies and their activities that ultimately deliver the products and services we consume. From an investment point of view, these trends clearly offer above-average growth potential; however, by nature, the success of a company's technology decisions cannot be predicted since ultimate approval/disapproval is dictated by the consumer. Focus on strong content providers such: FB, GOOG, NFLX, DIS, CMCSA.

Real Estate

Over recent years, the Real Estate sector's constant uptrend and relatively high payout ratio have made it attractive, particularly in an environment of low and falling interest rates. Low interest rates enable real estate investors to leverage property with relatively "cheap" money.

However, during periods of financial stress like we've experienced with the COVID-19 pandemic, real estate investment trusts (REITs) tend to struggle. Funding has dried up, and commercial property demand is falling. In some cases, as the economy has shut down for more than two months, the risk of lease defaults or relocations to smaller spaces may become part of a new trend. While net debt for the sector is low by historic standards, the risk to cash flow puts many REITs and real estate operators in a difficult position.

Retail space is under significant stress, as many companies cannot pay rent and may become insolvent. Health care facilities are under stress, with revenues sharply lower on delayed elective care and expected higher costs for extended and senior care facilities. Shared office space demand is sharply lower, and multi-family lease defaults are expected as unemployment has risen to very high levels.

The outlook for the sector will be highly dependent on the speed at which the economy recovers. While government support payments to businesses and newly unemployed workers will help, a slow, drawn-out recovery would become a longer-term headwind for the sector. However, if the economy recovers more quickly, people get back to work, and interest rates stay low as the Federal Reserve maintains accommodative monetary policy, the Real Estate sector stands to benefit. In a low-interest-rate environment combined with renewed economic growth, investors' search for yield would be a strong tailwind for the sector.

Given the high level of uncertainty regarding the path of the economy, however, we are maintaining a negative outlook for the sector.

Investment opportunities:

At the present, the risk for long and lasting recession are moderate as the more cyclical components of GDP are below their long run average; this is fundamentally positive for the real estate sector. However, we believe investors should avoid new engagements into the sector, as too much uncertainty exists regarding commercial leases.

Still, we believe that specific sub-segments of the real estate sector are worth looking at, such as Datawarehousing. As the economy is changing, data centers (cloud capacities) are required. This shift has significant ramifications for the global economy across all industry segments. Some real estate companies will experience a higher growth rates than others. Companies to look at: AREIT, GMG, GLPJ, 3283.

Energy

The energy sector had been under extreme pressure due to the massive supply/demand imbalance perpetuated by the pandemic-related economic shutdown, pressuring oil prices to record lows (even briefly negative at one point). This paints a very poor fundamental backdrop for the sector, given questions as to when the oil market will rebalance. Plus, the speed of the deterioration makes valuations almost impossible to assess.

The supply side tries to adjust quickly. However, mothballing a rig reduces future output capacity. The production reduction erased pressure on constrained storage capacity, and demand may stabilize as the economy slowly begins to reopen. Additionally, with relatively stronger balance sheets and access to cash, large energy companies are in a much better place than the entire oil patch, which is facing high insolvency risk.

We expect volatility to persist; stock prices for these companies could fall further, and we think that the S&P 500 Energy sector may have at least a short-term low. Because it is far from clear how long it will take for the oil market to rebalance supply and demand, the sector may continue to be subject to high volatility. We cannot trust metrics for valuations, as earnings forecasts are being cut sharply, and the fundamentals of the sector are still quite negative. The recent fall in the U.S. dollar has been positive for the sector; if the overall market continues to rally, the sector's high sensitivity to it could be a strong macroeconomic tailwind, which has been confirmed by the strong short-term relative performance. Therefore, we are maintaining a market perform rating on the sector.

Goldman Sachs commented that the present crisis is most likely a game-changer for the industry, as it is impossible to shut down that much demand without large and persistent ramifications to the supply side.

The demand slump is being exacerbated by former OPEC+ allies Saudi Arabia and Russia pumping as much crude as they can in a battle for market share, heaping additional pressure on shipping, tanks and pipelines. Goldman sees around 20 million barrels a day flowing into storage in April, while IHS Markit expects the world will run out of space to store oil by the middle of the year.

Integrated oil companies are large producers of oil and natural gas, but their diversified business segments reduce their earnings' sensitivity to changes in commodity prices. This, combined with strong balance sheets, makes integrated oils the most defensive subsector within energy. We believe integrated oils are appropriate as core holdings for long-term energy investors. In uncertain times, investors may seek integrated oils for their defensive qualities.

Investment opportunities:

The energy sector, which is one of the worst performing sectors YTD because of global uncertainty, is expected to continue to lag other sectors. We estimate that the full turn-around of the sector may take several years. While there was some outperformance recently, we believe that it is too early to consider engaging any funds. Investors requiring exposure to the sector are advised to focus on the highest-quality and financially strong names, as they are best-positioned to endure the oil price downturn.

In terms of names to look at, we favor global up- and down-stream operators, as they are most likely the only players who can endure lasting changes. We favor names such as: BP, RDSA, BKR, CVX, COP, XOM, SLB

Financial Services

The sharp economic contraction due to COVID-19 and the global Central Bank stimulus—including slashing interest rates and buying Treasuries and mortgage-backed securities—had pushed interest rates dramatically lower. Lower short-term and long-term rates weigh on lenders' net interest margins. Typically, when the yield curve flattens—that is, when longer-term yields and short-term yields are relatively similar—it's detrimental for financial institutions, which generally borrow at short-term rates and lend at longer-term rates. This has a strong impact on revenue growth, which is further stymied by post-2008 crisis regulatory burdens. Areas like asset management and brokerage services are suffering from severe price competition and low short-term interest rates.

However, the markets seem to have shifted to a more cyclical phase. If the recent trend of higher interest rates and the overall market rally continues, the sector's high sensitivity to interest rates and equities would be a tailwind. Additionally, the Fed's massive support of financial conditions could alleviate concerns about risks to banks' balance sheets due to indirect exposure to leverage in the loan market. As expectation of a quicker economic recovery seems to be emerging, we expect the mean reversion from sharp underperformance this year and an improved (albeit still negative) fundamental picture to continue to provide a strong tailwind to performance.

With the macroeconomic backdrop improving, financial services are expected to enter into a catch-up phase. The tailwind for this strength in stocks is now being augmented by a more optimistic view on the economy that is nudging longer-term interest rates up and the short rapid re-establishment of standard market conditions. The fundamentals for the sector are still challenged, with headwinds of still-low interest rates and heighted loan-loss uncertainty. But strong balance sheets and the Federal Reserve's stimulus efforts are positives. And if analysts' earnings expectations are honing in on reality, then valuations for the sector remain quite attractive from an absolute and relative perspective.

Investment opportunities:

The fall in interest rates to global-financial-crisis-era lows, along with the sharp slowdown in the economy, will drive a steep drop in profits for banks. But banks are well-capitalized and should see a sharp rebound when market volatility subsides.

We continue to have particular interest in secular growth companies that should emerge from the crisis with strong long-term growth prospects. Our preference goes to American Express, Intercontinental Exchange, MasterCard and Visa.

Longer-term Investment trend – FinTech
Ever-evolving consumer behavior is driving the disruption in the financial sector. The global fintech industry is at an inflection point and is set to drive a major digital transformation in the financial services industry, in our view. We expect global fintech revenues to grow from USD 150bn in 2018 to USD 500bn in 2030.

Healthcare
The pandemic is having an unprecedented impact on both the global economy and the various equity sectors—including the breakdown of many historic relationships within the markets. While the virus has been disruptive, the Healthcare sector has so far maintained many of its traditional non-cyclical properties amid the deep decline in economic activity.

In regard to the pandemic, there has been an assumption by many that the Healthcare sector should fundamentally benefit. However, while there are pockets within the sector that have benefited, there is a mixed impact. Some companies benefited from increased sales of over-the-counter drugs, as people stocked up on cold and flu medicines and other personal care items. Pharmacies have seen prescriptions pick up significantly as people shifted from 30-day to 90-day supplies. However, sales were simply brought forward and should equalize with a slowdown in sales going forward.

Mass job losses means insurance-premium income will decline. Many of the unemployed will be covered by Medicaid, which pays out claims for drugs and care at a much lower rate. With the sharp drop in doctor visits and delays in elective surgeries, insurance companies will make up for some of the lower premium income with lower claims payouts. However, fewer visits translate into fewer diagnostic tests and drug prescriptions, resulting in hospitals with lower billable services and surgeries. As economies slowly reopen, we should see some of this reverse, but downward earnings revisions have ensued for the healthcare equipment and service industry group—which constitutes a large proportion of the Healthcare sector. In others words, one could argue that the health care sector operates with a constant overcapacity which needs to be filled at any price.

Some companies within the biotech and pharma industries stand to benefit if they produce tests and vaccines for the virus, but at a high cost and with potential delays of other trials. And much of the benefits may have already been priced in.

Beyond the COVID-19 impact, however, the Healthcare sector has many long-term positives, including an aging global population and a growing middle class in emerging markets, all of whom will demand more extensive drug treatments and medical care over time. And balance sheets in the Healthcare sector remain flush with cash, increasing the possibility of higher dividend payments, share-enhancing stock buybacks, and mergers and acquisitions.

2020 is an election year in the U.S., and this may spell volatility for the sector. In general, we believe the risk of major legislative changes is relatively low, as potential changes under discussion are well known. However, in the event of a sweep by either party, this sector may be one of the most exposed to political risks.

In terms of valuations, comparison with other sectors is difficult, because the depth and breadth of the recession make it difficult to forecast earnings and other fundamentals. However, when we compare the Healthcare sector relative to its own history, most valuation metrics reflect decent valuations.

The sector's macro impact is neutral, as it has tended to trade in line with the market in recent years (notwithstanding the last few months). We think attractive relative valuations are a positive, but the sector's fundamental ranking has dropped as other sectors have seen relative improvements in earnings revisions in recent weeks. Finally, the sector has underperformed recently, as some of the more cyclical sectors have taken the lead. While we like the long-term perspective of the sector, there is more short-term potential elsewhere.

Key figures for the USA:

Target values:

Present fair value S&P 500:	3'100
E12 months value S&P 500:	3'000
Upside potential:	flat

Key economic ratios:

GDP Growth 20 (E)	-5.3
GDP Growth 21 (E)	3.7
CPI 20 (E)	1.0
CPI 21 (E)	1.6
P/E 2020 (E)	20.1
P/E 2021 (E)	18.2
Div. Yield 2020	1.9
Div. Yield 2021	2.0

Most likely next short-term move:

S&P 500	flat
Nasdaq	float

Key names to look at:

Strong intellectual property
- VISA
- Mastercard

Technology:
- Microsoft
- Micron Technology
- Nvidia
- Apple
- IBM

Financials:
- VISA

Average ROI of Banks recovered but remains stable!

Investment opportunities:

Longer-term Investment Trend – Healthcare

The healthcare sector is on the verge of some fundamental changes, as a result of COVID-19. Not only were hospitals under-used during the lockdown period (read: during normal business conditions hospital capacities are filled-up with cosmetic cases - people were not less ill during the pandemic period), but also, the time-to-market for new medicine is too long. Three opportunities to make progress in this line include the following:

a) Genetic therapies modify genetic information with the intent of curing disease. Replacing defective DNA can remove the cause of illness and restore health. This represents a paradigm shift away from traditional drug treatment, which generally slows disease progression or relieves symptoms.
b) Generics are a pillar of affordable healthcare. Demand is supported by demographic trends and budget constraints: aging and population growth drive greater healthcare use, while health spending as a share of GDP is rising. Health systems are focusing more on value for money, supporting demand.
c) MedTech and hospitality management: An aging population and rising healthcare costs put more pressure on health systems to deliver better care at a lower overall price point. Digital technologies can help reduce waste and fraud, better target treatments, and support the shift to value-based care.

Industrials

The Industrials sector has suffered significantly from the global economic downturn, with industrial output faltering as a manufacturing slump has broadened globally. While defense spending is safe, the sharp retrenchment in the economy and travel has weighed on airlines and the transportation industry in general. Together, this has prompted business leaders around the world to put nearly all capital spending on hold, stalling revenue growth.

There are now improving prospects for economic growth and markets have begun to trade as would be typically seen in an early stage of the business cycle. While the path of the economy remains highly uncertain, this provides a nice macroeconomic tailwind for the sector. A strong rebound in airline industry—which was decimated earlier this year—has resulted in very strong short-term relative performance.

However, valuations remain poor, as 2020 earnings expectations have been slashed by more than 50% in recent months. While earnings revisions have stabilized, the fundamentals for the sector remain challenged amid uncertainty surrounding global growth and trade

The sharply negative earnings revisions pushed fundamentals into the negative category, but corporate balance sheets are relatively cash-rich. Once a potential economic recovery emerges, low manufacturing inventories and investment in more-efficient equipment to help offset weaker productivity is likely. Additionally, the sector has historically had higher-than-average sensitivity to the overall market—suggesting a tailwind if the rally continues.

Investment opportunities:

Longer-term Investment Trend – Industry 4.0

The industry revolution “Industry 4.0” is expected to transform the future of manufacturing. More importantly, it allows DM companies to relocate their production facilities in a fashionable manner closer to consumers. Also, full automation and robotics will allow companies to adequately address rising wages and challenging demographic developments.

Longer-term Investment Trend – EM Infrastructure

Much was already being done, but only around mega-metropolitan regions. Yet, by 2040, 80% of the world’s metropolitan areas will be in Asia. This growing urbanization and the expansion of megacities in emerging markets are driving demand for infrastructure investment. As a result, EM infrastructure spending will comprise two-thirds of global infrastructure spending well beyond 2025.

Companies to look at: SIEG, RHMG, SAND, CSX, LMT, UPS

Consumer Discretionaries

Consumer discretionaries is—unsurprisingly—one of the more cyclical sectors. As the name implies, it is dominated by companies that produce products and services that consumers often do without—e.g., new clothes, new cars or entertainment—when under financial stress or worried about job security. The sector has a number of industries with a high degree of exposure to COVID-19 business shutdowns and shelter-in-place orders that have been under sharp pressure—particularly hotels and leisure, autos and auto components, and apparel industries. However, those industries are counterweighted by the internet retail industry—Amazon, in particular—which constitutes the about 40% of the sector's market cap.

Amid rapidly deteriorating fundamentals for many of the industries, we judge fundamentals to be negative for the Consumer Discretionaries sector overall, as sales and earnings expectations for the internet retailing industry have deteriorated recently.

The valuation factors we assess are negative for the sector, as an average of multiple indicators ranks Consumer Discretionaries near the bottom of the pack. Much of this can be attributed, once again, to internet retailers. However, given the massive dislocations in the economy, these factors may be of little use.

Despite the historically pro-cyclical nature of the sector, a tailwind by the internet retailing sector has mitigated the negative fallout from the recession. The sector has outpaced the overall equity market recently and has historically had a modestly high sensitivity to the equities. However, weakness in the dollar can work against the sector, leaving the macro component negative. Relative strength factors are positive.

Investment opportunities:

After a decent start to the year, consumption of discretionary goods has significantly dropped due to the outbreak of the pandemic. Consumer confidence may remain low in the short term, but fiscal stimulus should help sales recover.

We are attracted to strong brands/content with pricing power and companies that are aligned to the needs of the millennial consumer, given the outsized impact that this demographic will have on consumption trends for years to come. In addition, we look for companies with leading e-commerce and omni-channel capabilities and international exposure, particularly within emerging markets. We favor names like the following: AAP, ADS, AMZN, ITX, LVMH, MCD, NKE, and PRTP.

Utilities

The Utilities sector has tended to perform better when growth and trade concerns resurface and to underperform when those concerns fade. That's partly because of the sector's traditional defensive nature—people need water, gas and electric services during all phases of the business cycle—and these are domestic goods and services, so it has very little international exposure.

However, amid the drop in stocks in February and March, the historically low-equity-beta Utilities sector simply didn't play its traditional relative safe-haven role. The sharp drop in interest rates would normally be expected to provide relative support to this sector, which relies on high levels of debt and tends to pay relatively high dividends—often an attraction for investors when yields on fixed income investments are low. However, there were unique circumstances that outweighed these historical relationships.

For one thing, because some investors had already been reaching for yield prior to the crisis, the high-dividend-paying Utilities sector had been bid up to record high valuation levels. Even underperformance year-to-date hasn't fully reversed those relatively high valuations, so we're not confident the sector will return to its defensive roots if markets sell off again.

Additionally, with improving prospects for economic growth, longer-term yields have begun to nudge higher, which further reduces the sector's attractiveness. The fundamentals of the sector remain relatively strong, owing to still-low interest rates supporting capital expenditure needs and the stability of earnings growth expectations. However, the sector's short-term relative performance has lagged amid a turn towards more cyclical sectors. Therefore, we are underweighting Utilities, despite expected bouts of volatility in the overall market.

Key figures for Asia:

Target values:

Present fair value MXAPJ:	650
E12 months value MXAPJ:	700
Upside potential:	+7.5%

Key economic ratios:

GDP Growth 20 (E)	-1.4
GDP Growth 21 (E)	6.9
CPI 20 (E)	2.4
CPI 21 (E)	3.3
P/E 2020 (E)	14.4
P/E 2021 (E)	12.8
Div. Yield 2020	2.4
Div. Yield 2021	2.5

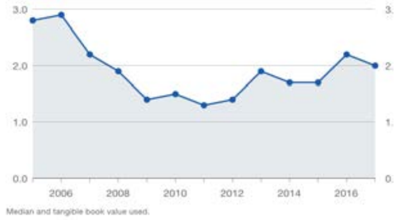
Most likely next short-term move:

MXAPJ Up

Key names to look at:

- Tencent
- Alibaba

Average Market-to-book ratio



Investment opportunities:

Longer-term Investment Trend – Waste Management
By 2050, three billion people will belong to the middle class. They will have sufficient disposable income to purchase products in a way comparable to people in high-income countries today. By 2050, waste volumes are expected to more than double. This is an SRI opportunity; therefore, it will be opportune for income-seeking investors.

Longer-term Investment Trend – Water
Climate change is a threat to our planet, impacting water supply and in particular, quality, quantity, and timing aspects. An inadequate water supply threatens the viability of the global economy, the environment, and human life.

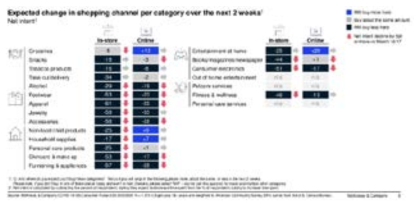
While water is abundant around the globe, it is not always well managed or managed at all. Only 3% of global water resources are consumable, and close to 70% of that is locked in ice. More importantly, regions like India and China dispose of very limited resources of high quality water. To solve this equation, important investments are required, mainly infrastructure related. In DM, the water distribution system is rapidly aging; future demands in new and adequate infrastructure are therefore about the same as in EM.

The secular trend behind this investment theme is highly “utility related,” and therefore complies with the requirements of SRI opportunities very well.

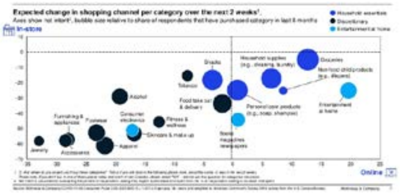
For those who seek exposure to the sector, it may be opportune to consider the following names: in Europe, Centrica, Fortum, E.On, and RWE; in the US, American Water Works, DTE Energy, Excelon, and Nextera Energy.

Stay-at-home to become a winner

... details of the expected shopping channel changes ...



... with basics and entertainment to shine.



Foreign exchange

Currencies

What makes a currency go up and down?

The currency market is setting the equilibrium between two forces—domestic economic fundamentals and foreign perceptions of a nation's strength or weakness. Domestic economic fundamentals include interest rate outlook, savings rate, household debt, GDP growth, and wage inflation, amongst others.

Ever since the end of WWI, the USD has been the predominant currency. The USD became the world's reference currency on the back of a widely accepted presumption of American exceptionalism. This was true in many ways, as nowhere else on the globe saw the mass population achieving such success. This occurred in a number of related matters: a fast-growing population (on average, yearly population growth of over 2 million for the last 50 years) and the USD as the predominant currency for borrowing funds in emerging countries (cheaper to borrow in US dollars than in local currencies). These facts created a virtuous cycle: cheap US dollars were used to build factories in Ems, which then provided US consumers with ready-made products at ever-cheaper prices.

However, the equilibrium is shifting; the US is suffering from a profound shortfall in domestic savings. In Q1/2020, the net national saving rate fell to 1.4% of the national income. The historic average is around 7%.

The rising government budget deficit (the federal budget deficit is likely to soar to a peacetime record of 17.9% of the gross domestic product in 2020) is not helping either. Protectionist trade policies, withdrawal from the architectural pillars of globalization (such as the Paris Agreement on Climate, Trans-Pacific Partnership, World Health Organization, and traditional Atlantic alliances), and some mismanagement during COVID-19, together with wrenching social turmoil not seen since the late 1960s, suggest that the US global leadership is on the decline. In other words, the intense downward pressure on the USD (devaluating about 4% p.a. since 1980) could accelerate and further weigh down the local economies.

Key takeaway: In a well-balanced business relationship, each deal is a give-and-take relationship. Being unwilling to compromise and imposing on trading partners with a self-sufficient attitude does not bode well over time. Even so, there is still time to gain an understanding of circumstances, and things may still turn for the better for the USD.

Investment considerations:

We see a clear bias for EUR/USD to appreciate towards 1.20 medium term. But the tide should turn slowly in 2H20, either due to easing trade tensions and improving global growth or due to more pronounced Fed easing.

In the coming months, we recommend positioning for a 1.15 upside barrier and for a downside of around 1.10.

Target values in 3 months:

EUR/USD:	1.1250 - 1.1750
GBP/USD:	1.2000 - 1.3000
USD/CHF:	0.9250 – 0.9750

Target values in 12 months:

EUR/USD:	1.17 - 1.25
GBP/USD:	1.30 - 1.40
USD/CHF:	0.90 - 1.00

Purchase power parities:

EUR/USD:	1.28
GBP/USD:	1.56
USD/CHF:	0.93
EUR/CHF:	1.19

Most likely next move:

EUR/USD	down
GBP/USD	down
USD/CHF	down

Target values in 3 months:

Oil:	$40 - $50
Gold:	$1,800

Target values in 12 months:

Oil:	$45 - $55
Gold:	$1,600

Upside potentials:

S&P GSCI	up
Oil	up
Gold	up

Next most likely move:

S&P GSCI	up
Oil	up
Gold	up

Commodity related stocks:
n/a

Capital market assumptions

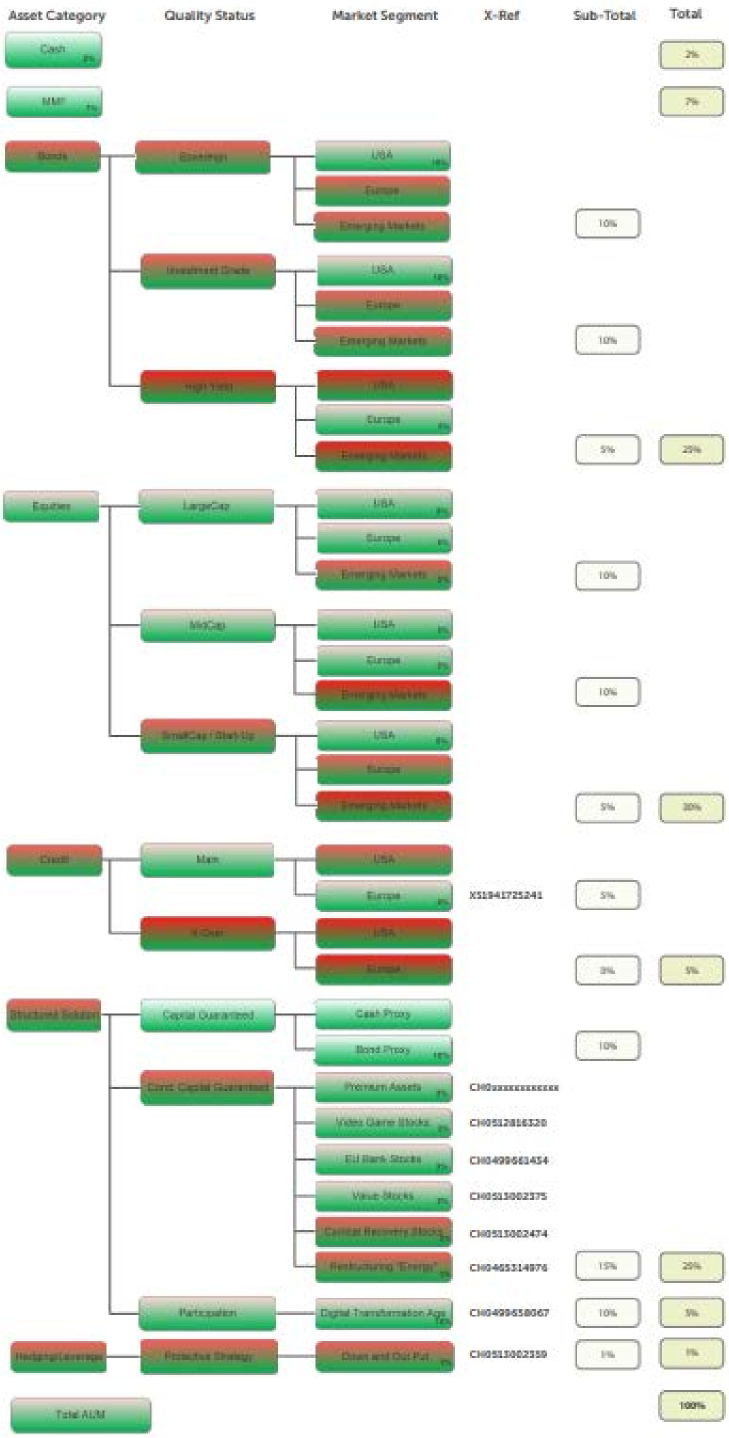
Return forecasts

Forecasts are in local currency (except EM equities); all figures are annualized.

	Forecasts for the next 7Y			Average returns over the past 10Y	
	Return	Vol		Return	Vol
Cash USD	2.50%	0.00%		0.80%	0.40%
Cash EUR	0.30%	0.00%		0.10%	0.50%
Fixed income					
USD High grade bonds 5-10Y	2.60%	5.00%		5.00%	4.10%
EUR High grade bonds 5-10Y	-0.20%	4.20%		4.40%	3.90%
USD Inflation linked bonds	2.40%	4.70%		3.00%	3.30%
USD Corp bonds (IG)	3.30%	4.40%		4.80%	2.90%
USD High yield bonds	4.70%	9.70%		8.40%	6.10%
EUR High yield bonds	2.30%	8.70%		8.70%	7.30%
USD Senior loans	5.70%	6.90%		5.50%	3.50%
EUR Senior loans	3.50%	6.30%		6.00%	3.10%
EM Sovereign bonds (USD)	4.90%	8.60%		7.40%	6.30%
Equities					
US	5.70%	15.20%		13.50%	12.70%
EM (USD)	9.20%	20.70%		3.70%	17.00%
Eurozone	5.10%	17.30%		7.30%	14.40%
UK	6.00%	16.30%		7.30%	11.50%
Japan	4.60%	19.30%		7.80%	17.20%
Switzerland	4.50%	14.00%		8.40%	11.00%
Alternative Solutions					
HF (FOF, USD)	3.50%	5.20%		2.90%	3.90%
Alternative, other risks (USD)	7.20%	10.00%		7.80%	7.20%
Alternative, Private Estate (USD)	7.90%	9.20%		9.40%	5.10%
Alternative, Private Equity (USD)	10.20%	14.50%		13.90%	8.10%
Alternative, Private debt (USD)	8.20%	4.50%		10.20%	4.70%

Bloomberg, JPMorgan, MSCI, HFRL, BAML, UBS, IRISOS

Base-case Allocation USD Balanced



Disclaimer: Allocation may change as a result of the risk optimization; past performance is no guarantee of future returns.

IRISOS
Knowledge is power.

Asset Allocation Preferences – June 2020

Sector	Region	Fundamentals	Risk/Reward	Investment case
Basic Materials	Americas	□ ■ □ □ □	■■■□□	The Materials sector has been sensitive to fluctuations in the global economy, as well as concerns about US-China trade and COVID-19. Accommodative monetary and fiscal policies may eventually support global economic growth. Recent trade agreements have eased some trade uncertainty, but the sector still faces significant challenges. Earnings are expected to recover after a sharp contraction in Q1 and grow moderately, boosting profit margins, yet wage costs are expected to rise as skilled-labor shortages occur in certain segments of the market.
	Europe	□ □ □ ■ □	■■■■□	
	EM	□ □ ■ □ □	■■□□□	
Consumer Staples	Americas	□ □ ■ □ □	■■■□□	The sector has historically outperformed during periods of economic slowdown and uncertainty, as investors are attracted by the perceived relative stability of the group. After all, consumers tend to buy food, soap and laundry detergent regardless of economic conditions. However, the sector's relative safety has prompted investors to push valuations to above-average levels. A supply-chain disruption related to the coronavirus could affect already slim margins in much of the space.
	Europe	□ ■ □ □ □	■■■□□	
	EM	□ □ □ ■ □	■■■□□	
Consumer Disc.	Americas	□ □ □ ■ □	■■■□□	The sector has a number of industries with a fair amount of exposure to China, such as hotels and leisure, autos and auto components, and apparel. However, those industries make up a relatively small weight in the sector, which also includes internet retail. Despite the overconcentration of internet companies in the sector and a weakening sales outlook, we judge fundamentals to be positive for the Consumer Discretionary sector, as some of its core underpinnings remain very upbeat.
	Europe	□ □ ■ □ □	■■■□□	
	EM	□ □ □ ■ □	■■■□□	
Energy	Americas	□ □ ■ □ □	■■■□□	A weaker US dollar is sector positive. The energy sector was pressured by the pullback in oil prices, resulting in weak relative performance, compounding multi-year underperformance. With the secular issues that the sector faces, concerns about slow global growth is yet another headwind to the sector. While this has led to attractive valuations from a historical perspective, very poor fundamentals lead us to believe that it is a value trap.
	Europe	□ ■ □ □ □	■■■■□	
	EM	□ □ □ ■ □	■■□□□	
Healthcare	Americas	□ □ ■ □ □	■■■□□	While there has been strong relative performance recently, the current discount to the overall market in numerous valuation metrics remains attractive; the sector has generally traded at a premium to the market over the past 15 years. The durability of Healthcare sector earnings during economic downturns tends to lead to outperformance during periods of economic weakness. We think that solid macroeconomic factors and attractive relative valuations mean an outperform rating for the sector is appropriate.
	Europe	□ □ □ ■ □	■■■■□	
	EM	□ □ □ ■ □	■■■□□	
Financial Services	Americas	□ □ □ ■ □	■■■□□	Topline revenue growth may prove to be elusive as regulatory burdens remain high, and areas like asset management and brokerage services suffer from severe price competition and low short-term interest rates. Additionally, if we see a significant pullback in the market, the sector's sensitivity to interest rates and the stock market could translate into sharp underperformance. Payment services remain attractive investment opportunities.
	Europe	□ □ □ ■ □	■■■□□	
	EM	□ □ ■ □ □	■■■□□	
Industrials	Americas	□ □ ■ □ □	■■■□□	The sector has suffered from concerns about slowing global economic growth, with industrial output faltering as a manufacturing downturn has broadened globally. This has prompted business leaders around the world to put capital spending on hold, whilst stalling revenue growth. While fundamentals were extremely good pre-crisis, corporations are expected to continue to work on more efficient equipment to help offset weaker productivity once COVID-19 has passed. Rebuilding inventories could signal the start of new cycle.
	Europe	□ □ □ ■ □	■■■■□	
	EM	□ □ □ ■ □	■■□□□	
IT	Americas	□ □ □ □ ■	■■■■■	Capital expenditures have been below trend for several years, and a return to more normal spending levels would boost the sector. Rising wages, including an increased minimum wage, could accelerate this trend, as companies may turn to technology to replace increasingly expensive human workers. Consumer confidence has generally remained strong, but we are waiting for new data that might reflect the outbreak of the coronavirus, which might disrupt the replacement market for mobile applications.
	Europe	□ □ □ □ ■	■■■■■	
	EM	□ □ □ □ ■	■■■■□	
Com. Services	Americas	□ □ ■ □ □	■■■□□	While these companies enjoy significant competitive advantages due to their dominance in their respective business lines, there are also emerging antitrust risks. The rollout of fifth-generation (5G) cellular wireless technology could increase demand, as 5G is expected to increase speeds and allow for more exposure to the "Internet of Things" and automated car technologies, increasing growth potential. However, upgrading networks will require substantial capital investment. This means that the Communication Services companies face unique risks.
	Europe	□ ■ □ □ □	■■■■□	
	EM	□ □ □ ■ □	■■□□□	
Utilities	Americas	■ □ □ □ □	■□□□□	Utilities stocks are among the most positively affected by falling interest rates because investors seek higher yields, the sector has high fixed costs and the underlying activities are capital intensive. The sector has experienced good momentum relative to the other sectors – both on a short- and long-term basis – which could continue if interest rates continue to fall. While defensiveness can be attractive in uncertain times, valuations are n0t. In fact, they have risen to well above historical levels, both on an absolute basis and relative to the other sectors.
	Europe	■ □ □ □ □	■□□□□	
	EM	■ □ □ □ □	■□□□□	

Expected total costs of running investment strategies with IRISOS:

Estimates based on yearly activities (in % of total AUM)	Conservative	Balanced	Dynamic	Tailor-Made
Year with low activity *	1.20	1.49	1.78	2.03
Year with average activity *	1.39	1.68	2.15	2.55
Year with high activity *	1.78	2.86	3.53	3.63

***** Subject to change according market conditions, product strategies, currency diversification, size of AUM, and product turnover.
Figures are indicative only and not binding, by any means, for the company.

Disclaimer

Sources:
Analysis and comments: Bloomberg, Reuters, Natixis, UBS, BNP-Parisbas, Charles-Schwab
Data and graphical items: Bloomberg, Reuters