IX-7 Asset Management SA

Q 03 / 2021

Quarterly Investment Review and Outlook

What comes afterwards?

Humanity has only about 1 billion years left on earth unless we find a way off this planet.

That's because the Sun is increasing in brightness by about 10 percent every one billion years. The increasing brightness will end life on Earth, oceans will evaporate, and the surface will become too hot for the ecosystem to exist.

So, we need more the kind of people like Jeff Bezos and Elon Musk to get us out and away to another promising planet.

Quarterly Report – Q03/2021

At a glance

Review – 3rd quarter of 2021

a) Macro

- Leading indicators, though high, have peaked. On the back of fiscal support and a cautious monetary policy, activity remains robust.
- The recovery phase is over and we have entered the expansion phase.
- China is decelerating as a result of government rectification and a "common prosperity" policy. The country has a very conservative health policy, which is supportive in this context.
- Inflation is high due to the persistence of bottlenecks. Its normalization will take time – we estimate 12 to 18 months.

b) Earnings

- Strong topline figures! Margins may be pinched by rising input costs, but due to strong demand, most companies are able to pass price increases on to their final customers.
- Earnings should decelerate progressively, in line with the normalization in the pace of activity.

c) Monetary policy

- The Fed is about to taper as the US job market is normalizing. Current Fed hike expectations (1-2 of 25bp in H2 2022 and 2 additional in 2023) look reasonable. However, the low level of real rates (~-1%) is surprising.
- The ECB reduces the pace of its asset purchases. The PEPP will end in March 2022 as planned. If needed, further asset purchases will be possible under the Asset Purchase Programme.

d) Geopolitical context

- US: Ongoing tough negotiations about budget and stimulus plans. Higher taxes remain a distinct possibility. Also, the federal debt ceiling needs to be raised and a stopgap funding bill passed.
- Germany: Mounting risk of a "traffic light" coalition as SPD gains momentum in the polls.
- France & Italy: Too early to worry about next elections.
- China: Blurred visibility. The rectification policy continues, weighting on investors' mood. India could be a big winner as a result of this readjustment.
- AUKUS alliance: In a very surprising move, a new meaningful alliance between 3 DM countries was formed to defend, safeguard, and surveil strategic economic connections, such inter-continental fiber-optics. It is a significant step-up to counter China's growing military presence in the West Pacific.

e) Main risks:

- Geopolitics (in particular, the fall of Kabul has to be digested); Health situation deterioration leading to renewed full lockdowns; Chinese slowdown; fierce partisan showdown in the US budget discussions.
- Investors' positioning on equities is elevated, it but has begun to shrink a bit. Any deleveraging from this level would increase the risk of a sizeable downturn in case of an (unexpected) negative event.
- On the back of variant AY3, Governments are stepping up their vaccination efforts to fight the 4th wave of contaminations. Yet, widespread lockdowns look unlikely in most developed countries.

Top-down view: September 2021

Macroeconomy

The global economy is now experiencing a fast recovery, with growth likely to approach 6% in 2021 (with a plausible range of 5.5-6.5%), and continue at 4.6% in 2022 (with a plausible range of 3.8-5.3%). The 2021 global real GDP growth forecast has remained unchanged relative to Q2, but this reflects an upgrade of 0.4 percentage points for advanced economies, offset by a downgrade of 0.4 percentage points for developing economies. Global output is estimated to have returned to its pre-pandemic level in mid-2021, but is expected to remain 2% below the pre-pandemic forecast level, even in 2023.

The recovery from the COVID-19 recession has shown strong rebound effects as compared to previous global recessions, with moderate longer-term economic activity losses expected. The pandemic may even boost medium to long-term economic growth by accelerating certain productivity-enhancing changes (e.g., the spread of e-commerce, workplace digital technology, e-healthcare).

Vaccination rates sufficient for approaching herd immunity are likely to be reached in advanced economies in Q3-Q4 2021, with progress constrained by vaccine hesitancy in certain groups. In developing economies, vaccination campaign progress remains too slow to approach herd immunity before the end of 2022 or even the first half of 2023. The baseline forecast is now assigned a 63-73% probability.

Asset allocation

Despite making positive gains, equities had a bumpier ride as compared to previous quarters. There were increasing concerns over the prospect of policy tightening, in response to stronger growth and inflation, by some of the key central banks.

This led investors to shift back into more defensive and growth-orientated markets. The S&P 500 led the way on performance, while Japanese equities were left behind. Both government bonds and credit made some positive returns.

The success of the vaccine roll-out, policy support and adaptability of many firms in operating with significant Covid-19 restrictions has led us to upgrade our global growth forecast. In the near-term, inflation is expected to be higher due to the rise in commodity prices and the re-opening of the service sector.

These factors should fade, but next year, we see inflation building as the output gap closes and capacity tightens. Against this backdrop, we expect the Federal Reserve to begin tapering asset purchases in December this year and start raising interest rates in Q3 or Q4 2022.

The greatest risk to our central macroeconomic view is a 'Boom and bust' scenario, in which there is a stronger than expected increase in growth. In this scenario, inflation also rises strongly, and monetary policy is tightened, resulting in a significant fall in economic activity next year.

Given the strong recovery in global growth, we maintain our overweight in equities linked to commodities. This asset also offers some protection from cost-driven inflation.

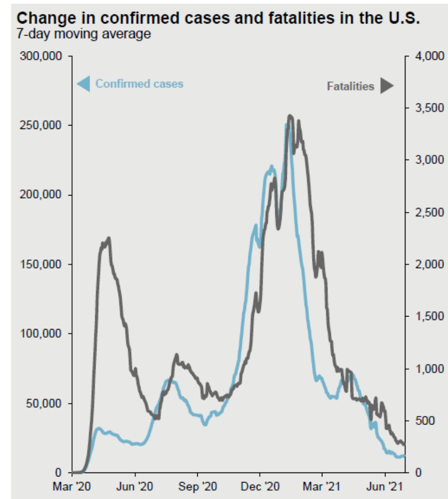
Meanwhile, we are still positive on equities, but underweight on government bonds, and we are neutral on credit. We have turned negative on US investment grade bonds due to very expensive valuations.

On equities, we expect that robust earnings growth will offset the impact of higher bond yields. Within equities, we prefer the less duration-sensitive areas of the market, such as Europe and the value sectors.

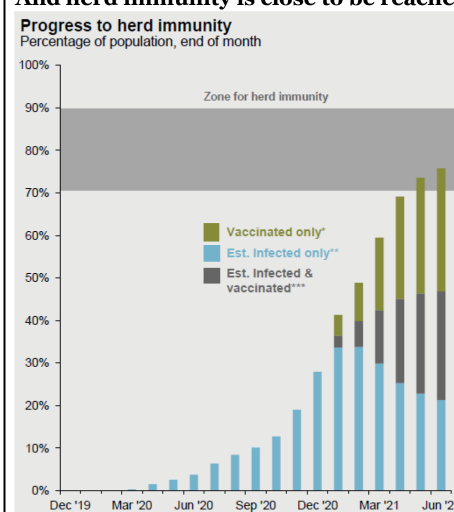
Currencies

Safe-haven buying has temporarily improved the USD valuation. We maintain our negative stance on the USD; for instance, versus the euro, the USD has a limited yield advantage. Furthermore, the US's large twin deficits are expected to rise further; the currency will therefore remain in a state of constant overvaluation.

Covid related fatalities are down



And herd immunity is close to be reached



Subjects of interest:

- US corporate debt is not yet a problem at the macro level. Corporate debt is high, but the interest burden is low, cash flows are high and margins have returned near-record highs.

- Inventories appear to be at close to record lows, the backlog of orders is at record highs, and inflation pressures keep developing in the early stages of the production process.

- Price pressures are mounting at the early stages of the production chain. At this stage, it is a global phenomenon of the economic cycle of US inflation: The peak has probably been reached, but normalization will take time, as sticky service components now begin to rise and demand rebounds more quickly than supply.

- US inflation: Probably no change in paradigm, even though long-term disinflation is likely to have come to an end.

- EPS remain well below their pre-crisis levels, but these have increased lately, both in absolute and relative terms.

- Reopening trades: After a strong rebound from November 2020 to March 2021, the reopening theme has been under-performing since mid-June, with a sharp drop in real interest rates following the June Fed FOMC (recall that this move was puzzling, as the Fed prepared the ground for a less accommodative monetary policy).

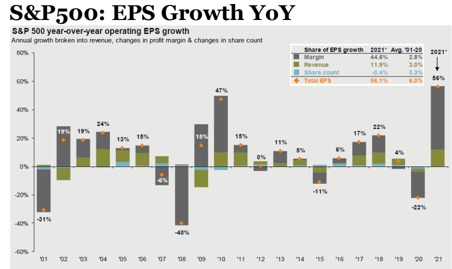
- Cybersecurity: The economy is becoming increasingly connected. The digital transformation, which has particularly accelerated during the pandemic, cannot be successful without any safe protection of data. The constant and uninterrupted growth of online services and digital solutions has exponentially increased opportunities for cybercrime. Financial gains or the desire to cause disruption are not the only motivations. Cyberattacks often involve the collection of information for political reasons, and cyberterrorism aims primarily at causing panic or fear by undermining electronic systems.

- Pet food & Pet care: The Pet Economy theme is a secular theme offering a lot of visibility. Growth is robust and crisis resistant. The global pet market is estimated to be between USD150-200bn and is growing by around 5% a year. Shifts such as a growing middle class, aging society and healthy living are contributing to the global growth of pet ownership. At the same time, changing consumer attitudes, particularly among millennials, play a role in increased spending on pets.

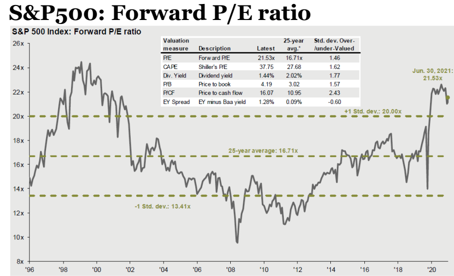
- Li-Fi: This is a wireless communication technology which uses light (visible light, ultraviolet and infrared) instead of radio waves to transmit information. The connection is thus established over frequencies ranging from 3THz to 300PHz, a spectrum 10,000 times wider than that of radio frequencies on which Wi-Fi is based.

  Opportunities via Li-Fi:
  - The encoding and data transmission works by flickering the light source very rapidly such that the change in light intensity remains unperceivable to the naked eye.
  - The main idea behind this technology is not a novelty; we have already seen cell phones equipped with infrared sensors and transmitters in the past, allowing for the exchange of multimedia files between users. Today, we can expect a broader use, thanks to greater speeds and a wider range. However, using LED lights for this purpose is fairly new and the idea is becoming more appealing to tech developers.

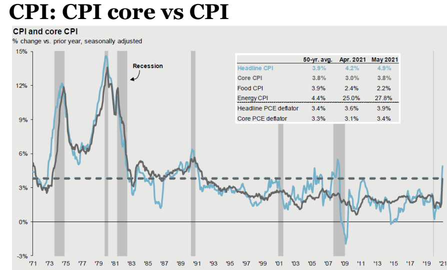
S&P500: EPS Growth YoY



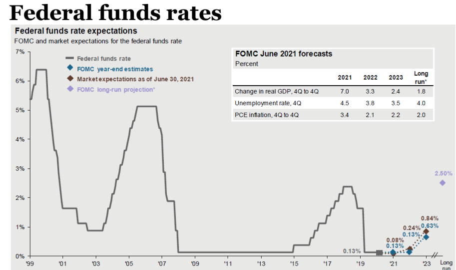
S&P500: Forward P/E ratio



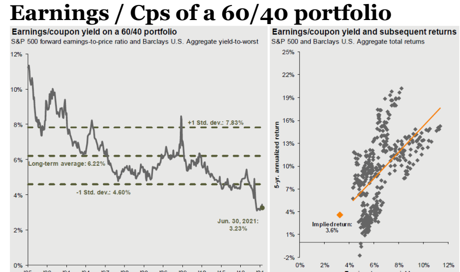
CPI: CPI core vs CPI



Federal funds rates



Earnings / Cps of a 60/40 portfolio



Evergrande:

Evergrande is a Chinese property developer. The company is probably "too big to fail" (but that's also what people said before Lehman in 2008). For the time being, the risk is more idiosyncratic than systemic. There's no sign of a liquidity squeeze in financial markets, but the situation remains very fluid.

Company pedigree:

- Evergrande is the biggest Chinese property developer (with a market share of 4-5% of homes built). Its assets total ~USD300bn. As a diversified conglomerate, the company also operates in many sectors (e.g., new energy and EV, health, water, property service, network, etc.).
- It is heavily indebted (according to the balance sheet of the company, USD 110bn at the end of 2020 – which is 0.7% of China's GDP). Debt is mostly short-term (~52bn due within one year, the rest within 5 years). Meanwhile, the company is running out of cash (the ratio of cash to short-term borrowing fell to 36% at the end of H1 21 versus 47% by the end of 2020).
- Should official data prove true, Evergrande would not present a systemic risk. However, it is possible that leverage is much higher than assumed (off balance sheet through wealth management products). This makes systemic risk almost impossible to quantify; it is only by unraveling the deals that they will they become public.
- Almost 80% of the funded debt (~USD 110bn) is onshore and senior.
- Supplier credit represents 45% of total liabilities.
- Debt is largely short-term (47% is within 1y, 31% is within 2y).

In its legitimate quest to avoid bubbles, China has probably squeezed its property market (and its economy) too far

- The Chinese authorities have been trying to cool down their economy since last fall. They targeted a 6% GDP growth rate for this year (versus the 8% expected by the cons). The red-hot housing sector has largely borne the brunt of the efforts, as regulators have tried to control developers' liquidity and borrowing ("three red lines" policy).
- The property market accounts for 25-30% of China's economy. It is likely to remain a headwind for growth next year. In August, home sales dropped 20% yoy in value terms.
- We expect a monetary loosening soon (RRR cut), in order to sustain activity growth, limit contagion and prevent systemic risk from spiraling out.
- The recent economic news flow has been ugly, but August data were stifled by covid-linked restrictions.

A Minsky moment for the Chinese authorities

On the positive side (in favor of intervention)

- Ripple effects would be expected on other home developers, domestic banks (Agricultural Bank of China, Industrial & Commercial Bank of China, China Minsheng Bank), suppliers and the whole economy through a negative housing wealth effect.
- Evergrande has presold projects across China to drum up cash. In the event of a default, 1.2 million people could become homeless. Buyers are protesting at construction sites, and authorities will try to avoid further social unrest. Housing is very important to the Chinese middle class (~75% of household wealth is tied up in real estate).
- Authorities saved the systemic Huarong Asset Management (USD 240bn liabilities) during the summer with a USD 7.5bn bailout package.

On the negative side (against intervention)

- Evergrande is a symbol of corporate excess, even as deleveraging and de-risking is one of the priorities of the government for 2021. In fact, earlier this year, authorities warned that they want to trim over-indebtedness in the real estate industry.
- Until recently, investors assumed the government would step in with a bailout in case of troubles, but Chinese authorities have made it clear that they want to increase moral hazard. Only economically important SOE will be rescued in the future, while others will have to default.
    - As a result, China's debt markets have seen a wave of defaults in 1H 2021 (25 defaults, totaling ~USD 10bn).

Bottom line:
The Chinese government will intervene at some point to avoid too much damage to the economy and local banking system, but it will try to save face and limit its intervention.

Haircut process and ramification:

- No bailout (or a minimal one). No bailout for offshore creditors (~20% of Evergrande's funded debt).
- Debt restructuring by lengthening in maturities. Banks are likely to be served before bond holders.
- Forced asset sales, even though the latter has been slow and at low prices to date.
- Liquidity injections by the PBoC in case of liquidity squeeze on the interbank market.

Is 2021 an outlier in terms of market valuation?

The summer saw some reversal of the "reflation trade" – a strong uptrend by economically sensitive stocks that kicked off with vaccine announcements last November. Concerns that earnings, valuations and gross domestic product (GDP) growth are at or near peak levels are warranted.

Given that earnings are stellar, especially amongst the more traditional industry participants, we want to take this opportunity to demystify some potential misconceptions.

When you drive from A to B, you may peak at 100km/h at some point, but you have not reached your destination. In the same context, economic activity can accelerate and decelerate pending consumer behavior, but consumers still won't fundamentally change their spending habits, they may spend less, but not stop it.

The average market view is that consumers will continue to spend on a better economic outlook and on improved sanitary conditions. While market valuation appears to be high, we advocate a focus on quality and stock selections that capture the benefits of secular growth trends.

Earnings

The earnings quality suggests an excellent corporate resilience. Companies have beat analyst expectations on both earnings per share (EPS) and revenue growth, with the latter being particularly strong. This suggests to us that even as inflation has been driving an increase in input costs, companies have the pricing power to offset it.

The data back to 2003 shows no historic precedent for sales growth to be sustained at this level. Nevertheless, recent results demonstrate corporate dynamism: Companies successfully managed costs through the crisis period. Q3/2021 earnings reports will be carefully watched Historic patters would suggest that they will be weaker than Q3 earnings, but by how much?

Fundamentals

The "Meme stock mania" suggests that fundamentals are less important today, but we disagree! Fundamentals are real, measurable and reflect a company's economic situation towards the outside. Any real market valuation is built upon fundamentals that interact with other elements of society. This is particularly true for corporations which have borrowed funds through the market. In this context, we note that credit spreads which represent the creditworthiness of companies remain at narrow levels. This, in turn, suggests that fundamentals are good.

Valuations

Stock valuations are high on a price-to-earnings (PE) basis, which values a stock relative to its prior or future earnings potential. We would make two points on this topic:

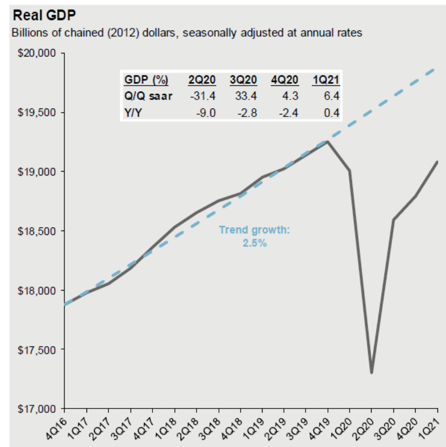
a) Analysis of PE multiples versus returns over different time horizons have shown that PE has little ability to predict near-term returns (think one to three years), but does have greater predictive power over the longer term (think five to 10 years). This makes sense in that EPS estimates are changeable, and the shorter the horizon, the greater the room for anomalies. This year will be such an outlier.

b) PE is a less informative measure than the equity risk premium (ERP), which values stocks based on the prevailing 10-year Treasury rate. The ERP gauges whether investors are compensated for the greater risk in equities versus "risk-free" government bonds. The ERP has been well above its long-term average for the past 10 years, suggesting stocks are undervalued for the relative risk/reward they offer.

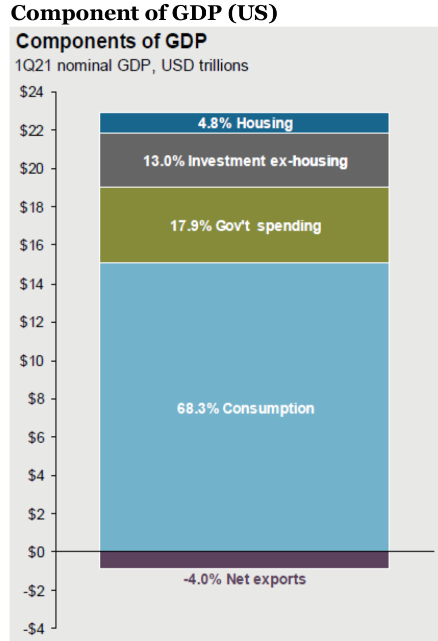
Adjustments to ratios can come from multiple directions. We expect that this time around, while equity prices will remain at elevated levels, the underlying key measurements will be adjusted, thereby bringing ratios to lower levels.

Previous long-term trends of the US stock market (S&P 500)

Real GDP



Component of GDP (US)



Investment recommendations by type

1. Equities:

Short-term view: - Neutral to positive

Medium-term view: - With the market rotation behind us, we believe equity markets are truly at their fair value at present! We remain strongly positive on strong secular trends; in particular, 5G, IT security, e-commerce, and payments.

2. Bonds:

Short-term view: - Neutral

Medium-term view: - With the market recovering, we favor BBB and single A debtors from emerging markets, yielding in the range of 3% p.a. We recommend a focus on companies with strong historic cash-flows and government related corporations that benefit from a quasi-government guarantee.

3. Credit:

Short-term view: - **Attractive**

Medium-term view: - With spreads at low levels and while Central Banks keep the bond purchasing program in place, continued good performance may be expected for the next 6 to 9 months.

4. Metals:

Short-term view: - Neutral to positive

Medium-term view: - Neutral to positive: Historically, metals are a refuge play; however, this has only partially materialized.
- The demand for EV is now continually increasing; to cover the long-term demand, new facilities need to be added. This should be price supportive.

4. Commodities:

Short-term view: - Neutral to positive

Medium-term view: - Commodities are attractive in case of a prolonged period of high inflation.

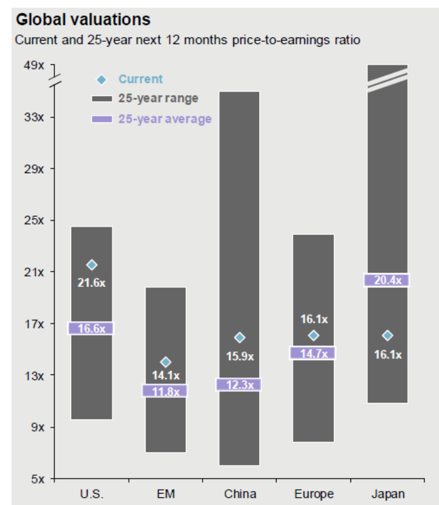
5. Structured solutions:

Short-term view: - Conditional capital guaranteed products offer an ideal risk/reward, as markets have corrected while volatility remains elevated.

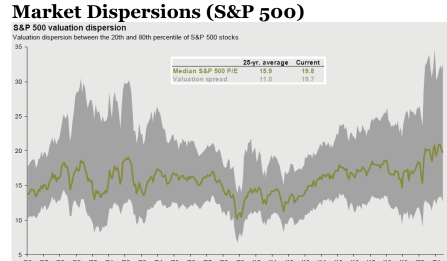
Medium-term view: - Longer-term investors should consider capital guaranteed long-short strategies that benefit from the increased dispersion between technology-related business opportunities and traditional business models.

Global earning growth

Global valuations



Market Dispersions (S&P 500)



Investment recommendations by theme

1. **Globalization 2.0:**

Short-term view: - Mixed

Medium-term view: - **With interest rates stable until at least 2023, a risk-on strategy is warranted.**

More than ever, we believe we have entered into a reversal of Globalization 1.0, and that excellent opportunities will result.

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: - Volatility is at a historically low level – temporary spikes may occur, but we do not expect them to reach very high levels.

At present, there are few triggers left that could further disrupt the market. Volatility is relatively low and investors can take advantage of buying volatility.

4. **Global order – a quick shift**

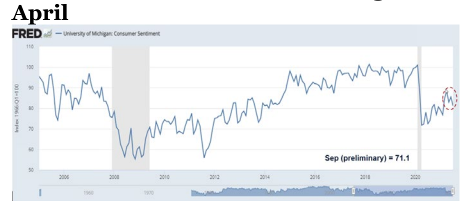
Short-term view: - Neutral

Medium-term view: - The impact of COVID-19 will not be over quickly, as substantial damage to consumer confidence will impact the global order.

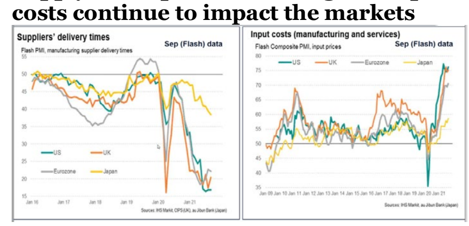
The gigantic amount of debt added in the last few quarters will force states to prioritize decisions differently as compared to the last GFC.

The present crisis highlights the limits of restless globalization. Now that excesses have been realized, we now expect that globalization is entering a period of unparalleled deconstruction that promises to transform industries for years to come.

Consumer confidence is declining since April



Supply disruptions and higher input costs continue to impact the markets



Asset class view:

- The current cycle, value and sentiment investment decision-making process in late June 2021 has a moderately negative medium-term outlook. Value is expensive across most markets, except for UK equities, which are at near fair value. Sentiment is near overbought levels but not signaling dangerous levels of euphoria. The cycle is risk-asset supportive for the medium-term. Central bank tightening, led by the Fed, seems unlikely for the next two years, and the major economies are in the early recovery phase from the 2020 lockdown recession.

- We prefer US equities to non-US equities. The post-vaccine economic recovery should favor undervalued cyclical value stocks over expensive technology and long-duration stocks. Within growth stock segment, we favor companies that belong to a strong secular trend. Relative to US investors, the rest of the world is predominantly overweight in cyclical value stocks.

- Emerging markets (EM) equities have been laggards so far this year. They have been held back by the high weighting toward technology stocks in the emerging markets benchmark, with concerns about slowing credit growth in China and the slow rollout of COVID-19 vaccines. This should start to reverse early next year. We also expect Chinese credit growth to stabilize and vaccines to become more available across emerging markets.

- High yield and investment grade credit are at fair value on a spread basis. We expect that the segment will continue to benefit from a positive cycle view that supports corporate profits growth and keeps default rates low. US dollar-denominated emerging markets debt is close to fair value in spread terms and should gain support on US dollar weakness.

- Government bonds are expensive, and yields should come under upward pressure as output gaps close and central banks look to taper back asset purchases. We expect the US 10-year Treasury yield to trade in the 1.5% to 2.0% range over the second half of the year.

- Real assets: Real Estate Investment Trusts (REITs) have rebounded in anticipation of economic re-openings, and have recovered all their pandemic loss. They are no longer cheap but should still benefit from the pandemic recovery trade. Listed infrastructure has lost most of its valuation disadvantage to REITs and should benefit from the global recovery, boosting transport and energy infrastructure demand.

- The US dollar has been supported this year by expectations for early Fed tightening. It should weaken once investors have fully priced in Fed-tightening expectations and as the global economic recovery becomes more entrenched. The dollar typically gains during global downturns and declines in the recovery phase. The main beneficiary is likely to be the euro, which is still undervalued. We also believe the British Pound and economically sensitive commodity currencies such as the Australian Dollar, the New Zealand Dollar, and the Canadian Dollar, amongst other emerging market currencies, can make further gains, though most of these currencies are no longer undervalued from a longer-term perspective.

The long-term downtrend of US TB-Yield has probably reached a turning point.

Market-by-Market View

United States:

We expect strong economic growth in the United States through the second half of this year. Real gross domestic product (GDP) growth of around 7% for 2021 would mark the best outcome for the US economy since 1984. Corporate earnings are rocketing higher. S&P 500 earnings growth shattered expectations in the first and second quarter earnings season (52% actual vs. 24% expected). We expect the results for the third quarter to remain strong on the back of re-opening progress. Strong earnings delivery is important for the U.S. market, which scores as expensive on a range of standard valuation measures.

Inflation came in much hotter than expected for the first half of 2021. The combination of supercharged demand (from federal stimulus checks) and disrupted supply (bottlenecks and pandemic impacts) has created inflationary pressures in the short-term. However, as demand moderates in 2022 and the supply side heals, we expect core inflation to moderate back to the Fed's target. We will watch five-year/five-year forward inflation expectations and wage growth for signs that inflation is more persistent than anticipated. Our outlook for US interest rates has been tweaked slightly, with our baseline for Fed liftoff pulled forward from March 2024 to December 2023. Otherwise, our US outlook largely remains unchanged from last quarter.

Public debt ceiling

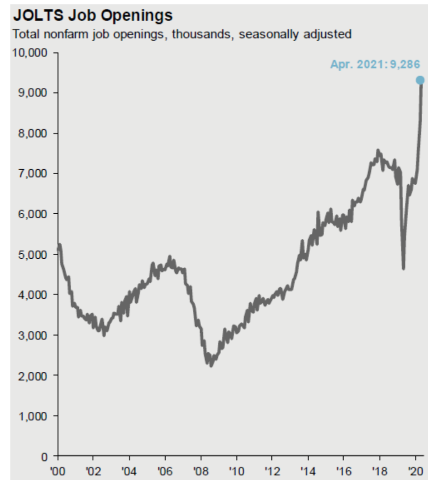
There is a statutory constraint on the amount that the US Treasury may borrow to fund federal operations. The debt limit is determined by Congress, which can either increase it (i.e., fix a new limit) or suspend it for a certain period (from several weeks to years).

- The Bipartisan Budget Act of 2019 suspended the debt limit until August 1, 2021.
- Since early August, the US Treasury has been using cash on hand and extraordinary measures to meet its financial obligations, as there has been no agreement in Congress.
- If the debt limit remained unchanged, the ability to borrow using those measures would ultimately be exhausted, and the Treasury would probably run out of cash, most likely in October or November, according to CBO's estimates. If that occurred, the government would be unable to pay its obligations fully, and it would delay making payments for its activities, default on its debt obligations, or both.

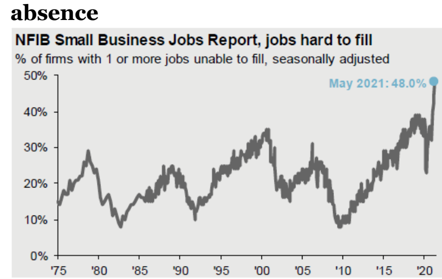
The failure of increasing the public debt ceiling

- There is no question – the debt ceiling will eventually be raised.
- The question is *when* and *with how much damage*?
- We expect a fierce partisan showdown beginning in mid-September.
- A bipartisan deal (requiring a supermajority of 60 votes in the Senate) looks highly unlikely.
- The only remaining solution would be to use the reconciliation process for a party-line increase in the ceiling. This will not be easy:
  - The current reconciliation bill (USD 3.5bn) proposed by the Democrats does not include an increase in the debt ceiling. This means that Democrats would need to amend their bill to include an increase in the debt ceiling.
  - Democrats can propose a separate bill to raise the limit.
  - Both solutions are time consuming, and in the meantime, uncertainty will remain elevated.
- While the last increases in the debt ceiling happened without any melodrama, this was not the case in 2011 or 2013. Instead, volatility sharply rose on financial markets, and equities and bond yields went down.
  - In 2011, the process was accompanied with a downgrade of the US sovereign debt.
  - In 2013, the process was accompanied by a government shutdown.
- Fierce debates over the debt limit may reduce growth through a drop in consumer and business leader confidence and a tightening in financial conditions. This was the case in 2H 2011, according to the US Treasury.

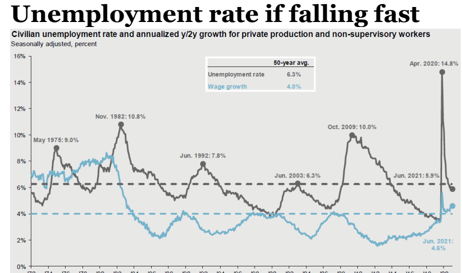
US labor market – people are not returning to work!



SME suffer most from the workforce absence



Unemployment rate if falling fast



Europe:

- With the full state of recovery, the equity market currently feels comfortable, but the picture is expected to become more mixed and nuanced for the remainder of the year.

- Inflation remains the greatest debate. A battle between the market's expectations for inflation and employment data, combined with Central Bank market intervention and forward guidance, has the market in a quandary.

- The recent rise in inflation across Europe is expected to remain a temporary phenomenon; we believe inflation will remain under control.

- Overall, the complex and nuanced environment at both a macro and company level is a positive one for stock selection, making a wide dispersion of returns across sectors and companies likely.

- Inflation and rising yields will continue to worry bond investors in the coming quarters, and investors should be prepared for possible drawbacks in their fixed income holdings.

Europe's vaccine rollout has gathered pace, and a more sustained reopening of economies is on track for the second half of the year. The EU's recovery fund will help countries in southern Europe maintain their rebound. Grants and loans from this fund are equal to 12% of the GDP for Italy and Spain and 19% for Greece.

At the time of writing this report, Germany's left-leaning Greens are polling strongly in advance of the federal elections. The most likely outcome looks to be a coalition between the Greens and the conservative Christian Democratic Union, in which the Greens would push for a more expansionary fiscal policy. However, this coalition is a traffic-light coalition, and we doubt it will be sustainable over time.

The region's post-lockdown recovery is likely to be extremely strong, with the GDP bouncing back by around 5% this year, following last year's nearly 7% decline.

We expect the MSCI EMU Index, which reflects the European Economic and Monetary Union, to outperform the S&P 500 in 2021. Europe's exposure to financials and cyclically sensitive sectors such as industrials, materials and energy, as well as its relatively small exposure to technology, gives it the potential to outperform in the post-vaccine phase of the recovery, when economic activity picks up and yield curves in Europe steepen.

Growth is gathering speed
Major early economic indicators for the Eurozone have reported values unseen in years, if not decades. The Purchasing Managers' Index for June indicated that the Eurozone grew at the fastest rate of the last 15 years. This is due to two developments. First, the export-oriented manufacturing sector benefitted from booming world trade. Second, the Eurozone's services sectors have recovered strongly – tourism and travel sectors have seen an especially sharp increase in sentiment since May, with travel restrictions easing in Europe. This is welcome news for southern European countries, which rely heavily on tourism. In Spain, for example, tourism contributes almost 12% to the Spanish GDP.

After a disappointing first quarter and a difficult second one, the Eurozone is moving toward a robust bounce-back. We expect a growth rate of 4% in 2021 in its baseline scenario, which would be the highest since the Eurozone's inception. However, while an even stronger consumer boom, driven by accumulated savings, is a clear upside scenario, risk factors persist. The Delta variant of the coronavirus has spread in Europe, especially in the Netherlands and Spain, where some restrictions had to be reintroduced. If rising infection rates lead to a new round of lockdowns and new travel restrictions, the Eurozone's growth prospects would fade substantially. Also, continued shortages of semiconductors and other inputs pose a risk. Despite these factors, the economic situation and outlook for the Eurozone look better than at any time during the COVID-19 crisis.

Emerging Markets/China:

China:

Chinese economic data has been mixed and continues to bank on a base case scenario with solid growth throughout this year. The credit impulse has deteriorated slightly more quickly than expected, but we suspect that most of the slowdown has been brought forward to the first five months of the year. There is still some catch-up potential from domestic consumption, and the production side of the economy should benefit from the global economic recovery.

Chinese equities have struggled over the last couple of months, in part due to increasing regulation on Chinese technology companies – particularly their foray into financial services. Forecasting regulation measures is a difficult task, but our base assumption is that for now, most of the regulation changes are behind us.

Of course, we would be remiss to discuss the outlook for China without touching on tensions between the US and China. The two sides have recently met, with nothing substantial arising. The agreement on climate initiatives was a minor positive, but we think that tensions are likely to remain elevated.

Other EM:

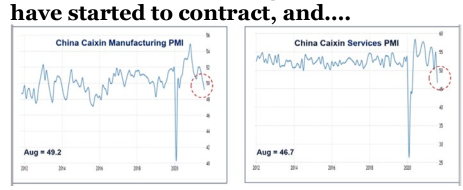
The market anticipated a synchronized GDP growth rebound for 2021. Duly, all 27 EM countries are expected to deliver positive real GDP growth for the first time since the global financial crisis. While developed market governments have resorted to significant fiscal stimulus by way of unemployment benefits or furlough schemes, EM governments have by and large been more restrained. Inflation has been benign due to a combination of demand destruction and lack of avenues for consumer spending, whereas the drop in imports helped strengthen current account balances in some countries. We believe monetary and fiscal policy will remain supportive in most emerging markets in 2021.

Export Linkages

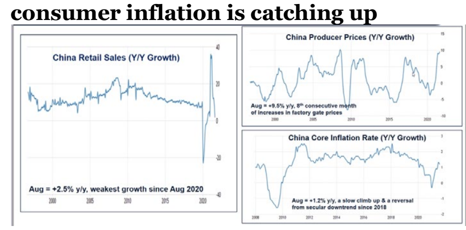
A gradual recovery in developed-market business activity should be good news for EM exports, and another catalyst for growth in these countries. In past cycles, an export recovery would have been driven primarily by commodity-heavy industries in EM countries. This is less so now that these sectors account for only ~15% of the MSCI EM Index. There will, however, be an impact through consumer and financial companies in commodity exporting regions such as Latin America, the Middle East and Russia. Even so, we think this will most likely play out through the semiconductor cycle. We are witnessing a surge in demand due to remote working arrangements, alongside well-entrenched long-term trends of 5G infrastructure, data centers, automation and artificial intelligence. This makes for a supportive environment for earnings growth to recover from its current very low levels over the next two years.

We also note that EM countries have become more and more domestically oriented, with lower reliance on commodities and DM than in previous cycles. Given the rising purchase power of domestic consumers, we still consider EM to be undervalued by about 20%. EM equities have seen record inflows since last year, as investors continue to close their underweight positions. For those wondering whether the train has left the station, we would point out that if investors were to revert to historical average allocations, the bulk of the inflows would still be ahead.

Chinese Manufacturing and Services have started to contract, and....



...retail sales remain weak and consumer inflation is catching up



Basic Materials

The Materials sector is sensitive to fluctuations in the global economy, the US dollar, and inflationary pressures. Accommodative monetary and fiscal policies are underpinning global economic growth and pricing power. However, the US dollar has trended higher recently, which is historically a headwind for the sector.

Cyclical-value characteristics – which tend to do well amid improving global growth and strong demand for industrial metals – have been a tailwind, though the latter appears to be moderating recently amid weaker demand in China. Significant supply chain bottlenecks are a concern. The Biden administration's clean energy and infrastructure initiatives could sustain the boom for industrial metals and materials, although tougher regulations are a risk. And demand for chemicals (the largest industry in the sector) may continue to increase as oil demand improves, but oil rig counts have been slow to rise. Finally, the run-up in industrial and agricultural commodity prices may have run its course.

Positives for the sector:

- Improving global economic growth has supported industrial metals and chemical prices, but appears to be moderating somewhat amid slowing economic growth in China.
- The cyclical value sector tends to be favored in the expansion phase of the business cycle, though this has faded somewhat recently.
- Improving global economic growth is supportive of chemical demand and pricing power.
- Strong gold demand is supportive of precious metals mining.
- Relative strength is improving.
- US clean energy and infrastructure spending could create a surge in demand for industrial materials.

Negatives for the sector:

- Longer-term global growth is expected to be lukewarm, providing only modest growth in demand.
- The slow recovery in the oil rig count is a headwind for oil-fracking chemicals.
- Significant supply chain bottlenecks and new work environment (pandemic related restrictions) may be constraining economic growth

Risks for the sector:

- Global COVID-19 cases could rise.
- Potential for increasingly stringent environmental regulations and/or reversal of the 2017 corporate tax cuts.
- The recent appreciation of the USD could impact negative economic growth.

Investment opportunities:
This sector is one of the most correlated to global industrial production.

The sector is highly leveraged to an improvement in manufacturing sentiment. As economic data strengthens, sentiment should improve and be a positive driver. However, higher materials pricing (e.g., steel) is likely unsustainable at current levels, and could lead to future stock underperformance.

Earnings momentum has continued to improve, supported by accelerating industrial production and rising commodity prices. Valuations have re-rated and are now relatively expensive versus history, but remain reasonable relative to other cyclical sectors. We also expect the chemicals and construction materials sub-sectors to benefit from the EU's sustainable investment plans.

At present, we favor material companies from Europe versus the US. Names to consider: Air Liquide, BASF, DSM, and Linde Plc.

IX-7 Asset Management SA

Consumer Staples

The ongoing recovery in the economy and the shift toward cyclical sectors has resulted in underperformance of the consumer staples sector since the market low in March 2020, as would be expected for a defensive sector whose constituents are typically less affected by changes in the business cycle. However, with the prospects of reduced social distancing and a full reopening of restaurants, food wholesalers that service restaurants have regained some footing, but at the expense of some big-box stores. In general, retailers within the sector have aggressively cut costs, leaving them in reasonable financial condition. But limited pricing power in a low-interest-rate environment gives them less-than-exciting top-line growth potential – though this could change if inflationary pressures prove to be enduring and higher costs can be passed on to consumers.

With the ongoing impact of fiscal stimulus, increased vaccinations, and accommodative monetary policies, we think that economic growth is likely to continue. However, the pace of growth has likely peaked. At this stage of the business cycle, the consumer staples sector typically underperforms the overall market, but the emergence of various risks could spark volatility that would favor this defensive sector.

Positives for the sector:

- It typically has a stable earnings profile
- Companies have engaged in aggressive cost-cutting
- During periods of strong economic growth, Consumer Staples can leverage their strong pricing power

Negatives for the sector:

- Historically, an improving economy and strong stock market have typically made this defensive sector relatively less attractive to investors
- Companies tend to have limited pricing power in a low-inflation environment
- Companies in the sector tend to face higher input costs, without any real opportunity to adjust for alternative solutions

Opportunities for the sector:

- Additional government stimuli and successful distribution of COVID-19 vaccines could further support the economy and reduce stay-at-home food and staples demand.
- The sector could perform better than expected if inflationary pressures enable significantly more pricing power.
- Risks to the economy, such as the COVID-19 Delta variant, could favor this defensive sector more than is currently expected.

Investment opportunities:
The sector has been one of the best performers since equities began to plummet after the February 19 peak. Demand should remain relatively resilient for products that satisfy everyday needs, despite disruption to the economy. However, other sectors of the market appear better positioned if markets begin to bottom.

Given the overall competitive outlook for the sector, investors should seek companies with strong balance sheets, low financing costs, and a strong focus on products and services. Because of high absolute valuation and limited upside potential, high yield dividend stocks are at risk; companies to consider include AD, ABI, BAT, NESN, EL, MO, and PM.

Key figures for Europe:

Target values:
Present fair value (DJStoxx600): 395 (29.09.21)
E12 months value (DJStoxx600): 448
Upside potential: +13.4%

Key economic ratios:

GDP Growth 21 (E)	0.8
GDP Growth 22 (E)	1.2
CPI 21 (E)	1.2
CPI 22 (E)	1.3
P/E 2021 (E):	20.5
P/E 2022 (E):	15.7
Div. Yield 2021:	3.1
Div. Yield 2022:	3.4

Most likely next short-term move:

DJStoxx600	flat/down
DJStoxx50	flat/down
SMI	flat/down
DAX	flat/down

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

The technology market outlook has turned more positive. More and more people are vaccinated in DM, businesses are starting to welcome employees back into the office, stores and restaurants have fully reopened. Based on research data, companies are expected to increase tech-related budgets by 7.4% for 2021, and another 6.7% next year.

All categories of tech budgets are expected to see growing demand in 2021 and 2022. Software related spending is expected to be especially strong, with growth accelerating to almost 10% in 2021, and just over 11% in 2022. Tech consulting services and tech outsourcing services will also experience increased spending, while computer and communications equipment will fluctuate.

Three key trends emerge:

1. On-premises technologies persist
2. Pure cloud solutions face increased competition from hybrid cloud offerings
3. Customer software development stages a renaissance, using new middleware platforms

Other headlines of interest:

- Software will be the star performer in the 2021–2022 US tech market outlook
- Single-instance cloud becomes a competitor to software as a service (SaaS)
- Tech services will ride the coattails of software demand
- Equipment and telecommunications services will see moderate growth

Positives for the sector:

- Companies generally have strong balance sheets and earnings growth potential, with low funding costs
- Home office, financial services technology, and surging online retail are supporting cloud computing infrastructure and software
- There are long-term growth tailwinds, as businesses enhance productivity with tech investment

Negatives for the sector:

- Valuations are very stretched relative to the historical average, making higher interest rates a significant headwind
- Capital expenditures are weak, albeit improving
- Semiconductor prices are rising amid low supply and hoarding
- The sector is highly concentrated in a few stocks

Risks for the sector:

- Continued high unemployment could weigh on consumer technology revenues
- There is the potential for antitrust suits in the US and Europe
- There is the potential for a reversal of the 2017 corporate tax cuts which have benefited the sector

Investment opportunities:

Although the near-term is highly uncertain due to COVID-19, we believe investors should focus on technology companies with attractive longer-term growth opportunities due to established franchises in large and secularly growing addressable markets such as software, cloud, and security.

Secular trends remain strong and tech profits will likely recover to peak 2019 levels more rapidly than any other sector. However, valuations are high and the sector's defensive behavior during the pandemic gives us less certainty that it will outperform in the ensuing economic recovery.

In this vein, we highlight Microsoft, Palo Alto Networks, Salesforce.com, Splunk, and Accenture. Investors looking for small cap exposure, may look at Okta, Twilio, Pinterest, Zuora, and Etsy.

Communications Services

Pandemic-related stay-at-home behaviors have been good for some companies in the sector, as it has led to increased use of social media and demand for streaming entertainment – though the pace of enrollments is likely to ebb as traditional entertainment options reopen. With the shift from traditional TV and cable, advertisers have struggled, but are quickly pivoting toward online mediums. Wireless service revenues and equipment sales are being supported by the initial rollout of fifth generation (5G) cellular technology.

While larger social media companies (Alphabet/Google and Facebook) enjoy significant competitive advantages due to their dominance in their respective business lines (search engine and social media) they also face emerging antitrust risks and headwinds from Apple's ad-blocking feature, as well as potential market saturation.

Longer term, we believe the continued expansion of 5G could further increase growth within the sector, as it continues to increase demand for equipment and services. Upgrading networks will require substantial capital investment, but federal government infrastructure initiatives could result in subsidies and investment.

Positives for the sector:

- Social media has a competitive advantage.
- 5G rollout should boost growth potential, but companies face near-term high capital expenditures; government subsidies and investment may help.
- Social distancing has accelerated a shift toward streaming entertainment content, but we expect that demand has peaked for now.

Negatives for the sector:

- The antitrust regulatory trend is negative for search engine and social media companies.
- There is potential for increased social media regulation (for example, the Section 230 legal shield is under scrutiny).
- Streaming services risk market saturation.

Risks for the sector:

- Sector market capitalization is heavily concentrated in the top two stocks — Facebook and Google — whose movements can significantly influence the sector overall.
- Recent developments in process flow management are pushing towards more and more DIY operations. We see companies entering uncharted territories, with potential legal precedents to follow and the potential for an increase in lawsuits and provisions for customer losses.
- Apple's inclusion of ad-blocking features could weigh on ad revenues for social media.

Investment opportunities:

The sector should continue to benefit from the shift of ad dollars to digital platforms. However, due to the defensive nature of telecom companies (around 20% of the sector), combined with uncertainty related to antitrust issues, the sector is more likely to perform in line with the market in an economic recovery.

We believe that many Communication Services companies currently face risks that outweigh their potential rewards, which is why we have a "hold" rating on most of the sector's companies (GOOG, DI, NFLX, FB, AMZN).

IX-7 Asset Management SA

Energy

The rise in oil to a price well above the average break-even level – even after the recent volatility – may threaten energy companies' resolution to be more disciplined with expenses and investment. Meanwhile, the US dollar has rallied, which is generally inconsistent with higher oil prices, and investor sentiment appears to have become too optimistic.

Since the low point of the COVID-19 crisis in 2020, the Energy sector has lagged the sharp rise in the price of oil and is well below the historical average of that relationship – though the clean energy movement may have loosened the relationship somewhat. This is still likely an intermediate-term tailwind for the sector, as it could provide a buffer for energy stocks if the price of oil were to weaken. Additionally, even with the sharp rise in oil, capital expenditures have not been ramped up, as has been done historically. Therefore, if there is a significant decline in oil, oil companies are less exposed to stranded assets (investment that becomes obsolete).

Valuations in the Energy sector, though above the historical average, are still attractive relative to the other sectors. Despite strong gains in energy stocks since the market lows in 2020, they have not kept up with rapidly rising earnings expectations. This is not surprising, as investors have remained wary of the boom/bust sector, while equity analysts found optimism amid the combination of rising oil prices boosting revenues, and restrained expense growth.

Finally, oil inventories have declined. With the reopening of the global economy, the recovery in demand for oil has outstripped supply by cautious producers – both OPEC and US producers alike – driving inventories lower. A continued decline in inventories against the backdrop of higher demand is inherently supportive for oil and potentially, for energy companies.

Positives for the sector:

- Oil is priced above the level at which the average company can cover expenses
- Supply has declined with lower production and OPEC compliance
- Large diversified energy companies have strong balance sheets
- The ongoing recovery of the global economy bodes well for returning oil demand

Negatives for the sector:

- Oil demand is still down significantly
- Valuations are opaque
- There is weak long-term stock price momentum

Risks to the sector:

- New or expanded regulations could inhibit company growth potential; this would be harder on small companies, as larger oil and gas companies can better navigate regulations.
- OPEC's current supply agreement could fail if prices rise much higher
- Clean-energy initiatives may eventually dampen demand for oil

Investment opportunities:

The collapse in oil prices due to the inability of Saudi Arabia and Russia to agree on a production cut darkens the sector's outlook. The current barrel price recovery occurs on the back of lower production capacities, as a good number of E&P have gone bankrupt or closed low-capacity rigs.

Relative to oil prices, the sector looks cheap. Free cash flow yields are very attractive, capital discipline has improved, and the sector should benefit as demand recovers. In our view, it will take many years before the shift away from fossil fuels begins to crimp industry cash flows.

In terms of sector approach, we favor global upstream and downstream operators as most likely the only players to endure a lasting price war with Saudi Arabia.

We favor names such as BP, RDSA, BKR, CVX, COP, XOM, SLB

Financial Services

The Financials sector still has many favorable attributes, but several red flags have emerged. Macroeconomic conditions remain favorable for cyclical value stocks, which are heavily represented in the financial sector. However, this interest-rate-sensitive sector has faced headwinds recently, with rates under pressure. While we think that rising rates may again become a tailwind for the Financials sector, it could take some time for this to happen.

In general and according to the latest stress tests, companies in the financial sector still boast strong balance sheets, with ample capital to withstand even a significant rise in loan defaults. While the expiration of stimulus payments will likely contribute to an uptick in loan defaults, reserves for a large spike in loan loss were set aside last year– but not needed. Many banks are now able to reverse some of those reserves, which were booked as expenses.

Valuations are still attractive relative to other sectors, but forward earnings expectations have flattened out. Unless forward estimates turn higher, any significant price rise in the Financials sector would increase the price/earnings ratio, eroding the attractiveness of its valuations.

Many of the sector's favorable attributes – a strong financial position, cyclical tailwinds with higher interest rates, and attractive valuations – drove Financials' outperformance during the past year. However, investors' enthusiasm for the sector had become too frothy, pushing it to an overbought level that has historically been followed by price consolidation.

Positives for the sector:

- Institutions are generally in a strong financial position due to stringent post-2008 regulations
- Economic recovery and fiscal stimulus are tailwinds for loan demand
- Cautious Central Banks, along with improving growth prospects, have started to steepen the yield curve
- The sector has attractive valuations relative to its historical average and other sectors
- High loan-loss reserves are being released (which supports earnings growth)

Negatives for the sector:

- Despite long-term interest rates trending higher, in general, rates are expected to remain low by historical standards.
- Longer-term price momentum has been weak, though it has improved recently.

Risks for the sector:

- A surge in inflation could cause rates to rise sharply or for the Fed to tighten monetary policy, stalling economic growth.
- Banking regulations have increased.

Investment opportunities:

A recent stress-test shows that banks are well-capitalized and should see a sharp rebound when market volatility subsides.

Bank earnings are recovering swiftly as provisions for expected loan losses wind down. They are also key beneficiaries of higher interest rates, which drive an improvement in profitability and signal a potential pickup in loan growth. The Central Banks have lifted capital transactions, which should help boost earnings per share and return on equity. The sector remains attractively valued.

We continue to have a 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.

Moreover, investors seeking deeply discounted valuations with strong expense leverage and robust capital should consider an engagement in Ameriprise, Capital One, and State Street.

Key figures for USA:

Target values:

Present fair value S&P 500:	4'360 (29.09.21)
E12 months value S&P 500:	4'600
Upside potential:	+5.5%

Key economic ratios:

GDP Growth 21 (E)	5.7
GDP Growth 22 (E)	4.7
CPI 21 (E)	3.3
CPI 22 (E)	2.7
P/E 2021 (E):	31
P/E 2022 (E):	22
Div. Yield 2021:	1.3
Div. Yield 2022:	2.4

Most likely next short-term move:

S&P 500	down
Nasdaq	down

Key names to look at:

Strong intellectual property
- VISA
- Mastercard

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

Financials:
- VISA

From a technical point of view, still a valid entry point, with short-term downside limited to +/10 %

Healthcare

Heading into the 2020 election, the Democratic Party's healthcare proposal seemed to be a major source of angst. President Joe Biden's proposed "public option" – a more affordable or free alternative to private health insurance – along with enhancements to the Affordable Care Act (ACA), raised questions about the sustainability of profit growth in the healthcare sector.

However, Democrats have a razor-thin majority in the Congress, and division between progressive and moderate Democrats could very well result in many of the more contentious healthcare initiatives being tamed down or blocked altogether.

These more benign scenarios open the potential for renewed outperformance based on the 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. Valuations are relatively attractive, and balance sheets in the sector are generally in good shape, increasing the possibility of higher dividend payments, share-enhancing stock buybacks, and M&A.

There are still risks, however. Any legislation to control drug prices or raise corporate taxes could weigh on pharmaceutical companies' profits – though promising pipeline drugs can mitigate these risks. Additionally, the Supreme Court recently ruled that the individual mandate provision of the ACA is constitutional, thwarting efforts to repeal the entire ACA.

Positives for the sector:

- Balance sheets are strong, with ample cash for dividends and M&A.
- Positive long-term demographic trends may support the sector, including an aging global population and a growing middle class in emerging markets.
- Demand is returning for elective procedures, drug sales, medical equipment and diagnostics.
- Valuations are attractive relative to the sector's historical average.

Negatives for the sector:

- High unemployment reduces healthcare insurance enrollment.
- Extended-care facilities have seen a decline in enrollments and are likely to see higher costs related to virus-mitigation requirements.

Risks for the sector:

- The Supreme Court is considering the constitutionality of the Affordable Care Act (ACA), the impact of which is unclear.
- There is bipartisan support for prescription drug price controls.
- There is a possibility of a reversal of the 2017 corporate tax cut.
- A potential resurgence of the pandemic could reduce demand for elective medical care.

Investment opportunities:

The healthcare market is fragmented as its players strive to increase their market share through such strategies as improvements to existing solutions and software platforms, development of new platforms, and strategic alliances with other market players. Therefore, several players account for significant individual shares in the market.

While political risks for the sector have improved as prospects fade for Medicare for All, there is still uncertainty about the outlook for drug price regulation.

IX-7 Asset Management SA

Industrials

With the economic recovery and continued growth, the markets have been trading as would be typically seen in the early and now expansion stages of the business cycle – which could be positive for this historically pro-cyclical Industrials sector. Additionally, prospects for an increase in infrastructure and clean-energy investment will likely support the machinery and building materials industries.

Transportation and air freight have benefited from a return in demand as economies reopen. On the other hand, higher fuel costs, port congestion, and a lack of truck drivers are tempering the situation.

The aerospace and defense industry continues to face significant headwinds amid expected low airliner demand, production issues, and uncertainty surrounding the political appetite for defense spending. But the fundamentals of the sector remain positive overall. While the path of the economy is providing a nice macroeconomic tailwind for the sector, valuations are extended.

Positives for the sector:

- Capital expenditures are likely to increase if global growth continues to improve.
- The sector tends to outperform early in the business cycle.
- Many companies in the sector have cash-heavy balance sheets.
- Strong global trade and an increase in online shopping are spurring demand for transportation.

Negatives for the sector:

- Capital expenditures have been tepid.
- Aircraft demand is likely to be weak until business and leisure travel resume.
- Valuations of the peer groups inside the sector are relatively unattractive

Risks for the sector:

- While we are currently neutral on the sector, if there is a stronger-than-expected surge in global growth or a massive infrastructure stimulus, then the sector could perform better than expected.

Investment opportunities:

The sharp slowdown in the global economy hit this sector particularly hard. As lockdowns have eased, economic data has improved. Still, the sector has lagged the improvement in manufacturing sentiment indices and looks poised to catch up. The accelerating vaccine rollout should be a major boost for aerospace, which has lagged and is a significant end-market for US industrials.

Medium-term investors may look at the following: CSX, Siemens, Easy-Jet, Lockheed Martin, and Stanley Black & Decker.

Real Estate

The near-complete shutdown of international travel was very damaging to both hotels and prime retail. This is particularly true for Asia and Europe, which have become increasingly reliant on high spending consumers from emerging economies such as Mainland China. Chinese consumers have shifted to buying luxury goods locally, and even when travel picks up again, we think that a proportion of Chinese spending on luxury items will stay local.

Although the reopening has boosted retail and consumer service activity, it has caused a drop in e-commerce. Still, e-commerce spending remains significantly ahead of where it would have been, based on pre-pandemic trends. Appetite for logistics remains at near record levels as retailers and third-party logistics providers invest in their supply chain networks. According to Prologis, online fulfilment uses three times the space of traditional retail distribution due to a larger number of goods and the facilitation of returns. Whilst logistics demand should remain strong, the diminishing number of suitable sites (particularly in urban areas), point to a potential reduction in the amount of new supply being developed. This should provide further support for rental growth above inflation.

Office sector fundamentals have been severely shaken by the pandemic, as leasing came to a standstill in early 2020 and remains well below trend in Q2 2021. In many cities (most notably in the US and the UK) vacancy rates are at their highest levels in decades. Having made considerable investment in providing staff with the technology to work remotely, many firms are making long-term commitments to flexible working and reducing their office space.

Along with logistics, alternative sectors have also benefitted from resilient leasing activity during the pandemic. One of the most prominent is the life sciences sector, which combines offices with lab space for R&D-focused healthcare businesses. The virus has put a spotlight on a sector which was already growing as a result of aging demographics, recent scientific breakthroughs, and plenty of expansion funding from venture capital funds.

Positives for the sector:

- Low interest rates are positive for funding and make REIT dividends more attractive to investors.
- Warehouses, data center providers, and telecom towers are benefiting from technology trends.
- Long-term demographics support the recovery of extended-care and assisted-living facilities.

Negatives for the sector:

- High unemployment can lead to multi-family lease defaults.
- De-urbanization is a negative for multi-family housing.
- Short-term uncertainty about workers returning to the office exists.

Risks for the sector:

- A quicker-than-expected rise in interest rates could be a sharp headwind.
- A permanent rise in the work-from-home model could reduce demand for office real estate.

Investment opportunities:

The sharp slowdown in the global economy hit the sector particularly hard, with the exception of valuations, which have merely moved. While valuations are attractive, it may take time to assess the long-term impact of the pandemic.

Even so, there are sub-segments that are less exposed to the sharp downturn. In fact, we have two distinctive eco-spheres: the digital world and the tangible physical world. The blur is important and results in one global economy built on the back of bytes, and another composed of bricks and mortar.

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 higher growth rates than others. Names to look at: Sergo, Goodman Group, GLP, Nippon Prologis, A-Reit, Mapletree Logistics, Equinix.

Key figures for Asia:

Target values:

Present fair value MXAPJ:	714 (29.09.21)
E12 months value MXAPJ:	820
Upside potential:	+14.8%

Key economic ratios:

GDP Growth 21 (E)	7.1
GDP Growth 22 (E)	5.4
CPI 21 (E)	2.2
CPI 22 (E)	2.7
P/E 2021 (E):	22.5
P/E 2022 (E):	12-7
Div. Yield 2021:	2.1
Div. Yield 2022:	2.4

Most likely next short-term move:

MXAPJ down

Key names to look at:

- Tencent
- Alibaba

Hang Seng approach oversold territory

Consumer Discretionaries

The Consumer Discretionary sector – typically sensitive to swings in the economy – had its winners and losers with the onset of the COVID-19 pandemic. The massive stimulus efforts and stay-at-home orders spurred a surge in spending on home improvement and e-commerce sales early in the crisis, and the related stocks led the equity market rally.

Now, with the ongoing vaccine distribution, many of the most battered stocks in the sector – those in the apparel and hotel industries, for example – have recovered much, if not all of the crisis-related stock price losses. The cruise industry and some hotels are the exceptions, as the Delta variant remains a headwind. But these industries are often overshadowed by bigger companies in the sector, like Amazon and Tesla, which constitute more than 40% of the sector's market cap. The longer-term trend toward e-commerce and electric vehicles is likely to continue to support the fundamentals of these growth industries, but investor enthusiasm may have pushed valuations too high.

Additionally, a severe semiconductor shortage is an ongoing risk to the production of vehicles.

Positives for the sector:

- Vaccine distribution and ongoing economic recovery are positive for many of the more traditional discretionary industries.
- The shift away from brick-and-mortar is likely to continue to support fundamentals for online retailers.
- Pro-cyclical macroeconomic tailwinds when the economy is strong, though the sector hasn't traditionally been a strong performer in the expansion phase of the business cycle.

Negatives for the sector:

- The sector is overly concentrated in internet retail and automobiles.
- Valuations and investor enthusiasm appear stretched; higher interest rates may weigh on both.
- The semiconductor shortage weighs on auto and consumer electronics.

Risks for the sector:

- Antitrust action is possible for the largest online retailer.

Investment opportunities:

Consumer discretionaries are key beneficiaries of reopening the economy. Nearly USD 2 trillion in excess consumer savings looks poised to be unleashed as the pandemic winds down. The sector is also benefiting from strong secular growth in ecommerce. Low mortgage rates bolster the outlook for housing-leveraged segments.

We favor companies that benefit from the "stay-at-home" trend, such as Amazon, Nike, Deckers Outdoors, Adidas, LVMH, Inditex, Porsche, and Hugo Boss, amongst others.

IX-7 Asset Management SA

Utilities

The Utilities sector has tended to perform relatively better when concerns about slowing economic growth resurface, and to underperform when those worries fade. That's partly because of the sector's traditional defensive nature and steady revenues – after all, people need water, gas and electric services during all phases of the business cycle. Meanwhile, the low interest rates that typically accompany a weak economy provide cheap funding for the large capital expenditures required in this industry.

However, while interest rates are low from a historical perspective, they are expected to rise as the economy continues to expand. On the flip side, there is potential that a renewed decline in the economy could push rates even lower, or there could be significant government funding to Utilities as part of clean-energy initiatives that would benefit the sector's profit outlook.

Positives for the sector:

- Revenues are generally stable.
- Investors often turn to utilities for dividend income when prevailing interest rates are low.
- Low yields provide low funding costs for this capital-intensive sector.

Negatives for the sector:

- The sector has not acted as defensively during recent periods of market weakness as in the past.
- Valuations are high relative to the sector's historical average
- Economic recovery makes the sector less attractive relative to other sectors.
- Interest rates are expected to recover from the recent decline, which will make the cost of capital more expensive.
- Poor price momentum
- Weakening balance sheets with rise in debt and negative free cash flow
- Energy transitions toward a zero emission standard are proving a true challenge for a sector that has not been exposed to structural challenges for the last century.
- Poor valuations

Risks for the sector:

- There remains uncertainty regarding potential clean-energy legislative funding.
- Interest rates could rise due to an unexpected rise in inflation.

Investment opportunities:

The recent spike in volatility may have encouraged investors to seek the perceived safety of the utilities sector, but we still believe that this is the wrong move. A growing economy and rising interest rates do not make for utilities performance, and we therefore believe underperformance will likely continue.

For those who still wish to 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.

Foreign exchange

Currencies

Stay structurally bearish on the USD

Since early June, the US dollar has been staging a recovery, boosted by strong global economic data. Further impetus for USD has come from the monetary side, with the market pushing forward the timing of expected Fed hikes and anticipating the start of tapering in the coming months. A slightly more volatile equity market, with a slowing upward trend, also reinforced USD purchases, due to the currency's safe haven character. Looking ahead, we believe that the deceleration of growth in the mid-cycle stage (already witnessed in China) and Fed tapering will probably support the US dollar against the main G10 currencies, allow for USD strength against EUR, and require a selective approach in Emerging markets (EM).

However, the upside we foresee for USD should be gradual and only mild. The dollar has always been a countercyclical currency and has historically performed well in periods with slowing global growth, but the growth slowdown we foresee is also mild in nature. Relative to 2018, USD upside may be less pronounced, as the support at that time was exacerbated by the US-China trade conflict (which pushed RMB down more than 10%) and by negative EM news flow (e.g., Turkey). This time, aside from increased regulatory risk and recent related market volatility in China, we think EM fundamentals and sentiment are much healthier. We therefore keep a neutral stance, but with a selective approach in the EM space, with a preference for BRL and MXN.

Investment considerations:

We see a clear bias for EUR/USD to drop below 1.15 in the near term. But the tide should turn for the euro in 1H20, due either to easing trade tension and improving global growth or to more pronounced Fed easing.

In the coming months, we recommend positioning for a 1.30 upside barrier and a downside of around 1.15.

One risk is an unexpected rebound in US inflation and growth, which brings the possibility of Fed rate hikes coming back into the picture earlier than expected. This would lift the greenback. Another risk would be a US recession after escalating trade disputes, which could weaken the USD earlier and faster, since the Fed would likely cut rates aggressively.

Target values in 3 months:

EUR/USD:	1.1500 - 1.2000
GBP/USD:	1.3250 - 1.3750
USD/CHF:	0.9000 – 0.9500

Target values in 12 months:

EUR/USD:	1.17 - 1.25
GBP/USD:	1.35 - 1.40
USD/CHF:	0.95 - 1.00

Purchase power parities:

EUR/USD:	1.30
GBP/USD:	1.64
USD/CHF:	0.84
EUR/CHF:	1.15

Most likely next move:

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

Target values in 3 months:

Oil:	$75 - $82
Gold:	$1,750

Target values in 12 months:

Oil:	$80 - $90
Gold:	$1,900

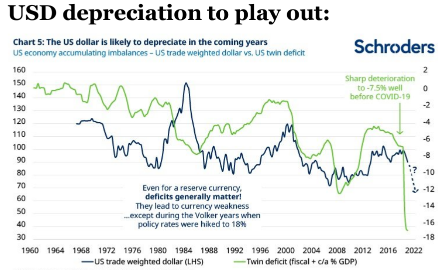
Upside potentials:

S&P GSCI	up
Oil	up
Gold	up

Next most likely move:

S&P GSCI	up
Oil	up
Gold	up

USD depreciation to play out:



Capital market assumptions

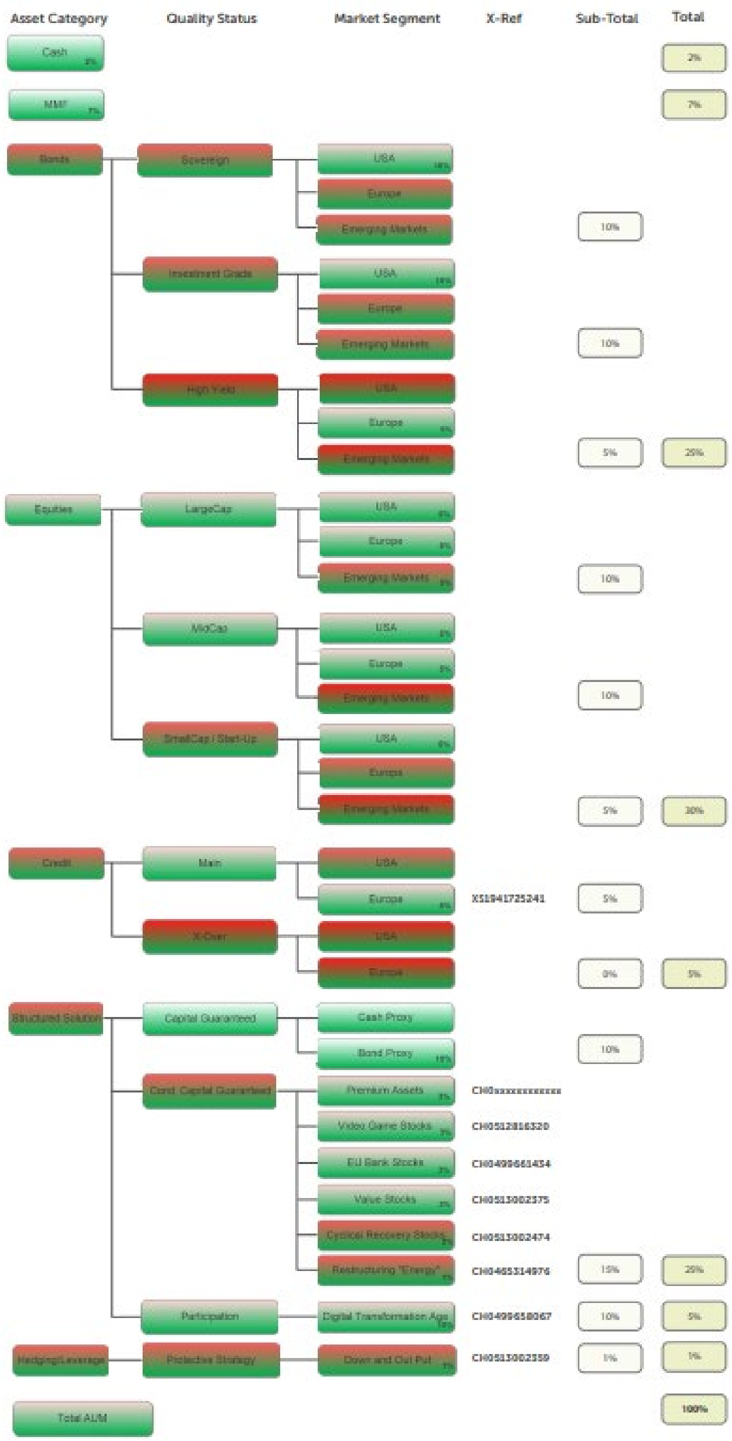
Return forecasts

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.

IX-7 Asset Management SA

Asset Allocation Preferences – September, 2021

Sector	Region	Fundamental	Risk/Reward	Investment case
Basic Materials	Americas	○●○○○	■■■□□	The Materials sector has been sensitive to fluctuations in the global economy, as well as to 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. After a sharp contraction in 2020, earnings are expected to recover 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	○○●○○	■■■□□	Historically, the sector has 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 relative 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 upbeat.
	Europe	○○●○○	■■■□□	
	EM	○○○●○	■■■□□	
Energy	Americas	○○●○○	■■■□□	The renewed rise in the value of the US dollar also has pressured the energy sector amid the pullback in oil prices, resulting in weak relative performance, compounding multi-year underperformance. The secular issues that the sector faces – concerns about slow global growth – are yet another headwind to the sector. While this has led to attractive valuations from a historical perspective, poor fundamentals and the relatively small size of the sector are negatively impacting the investment decision-making process.
	Europe	○●○○○	■■■■□	
	EM	○○○●○	■■□□□	
Healthcare	Americas	○○●○○	■■■□□	While there was 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 such as asset management and brokerage services suffer from severe price competition and low short-term interest rates. Additionally, the sector's sensitivity to interest rates and the stock market could translate into sharp underperformance if we see a significant pullback in the market. 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, while stalling revenue growth. Although 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. The rebuilding of 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 another outbreak of 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, thereby increasing growth potential. However, upgrading networks will require substantial capital investment. This forces Communication Services companies to face unique risks.
	Europe	○●○○○	■■■■□	
	EM	○○○●○	■■□□□	
Utilities	Americas	●○○○○	■□□□□	Utilities stocks are among the most positively affected by falling interest rates as investors seek higher yields, because the sector has high fixed costs, while 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 not. In fact, they have risen to well above historical levels, both on an absolute basis and relative to the other sectors.
	Europe	●○○○○	■□□□□	
	EM	●○○○○	■□□□□	

Expected costs of running investment strategies with our company

Estimates based on yearly activities (in % of total AUM)	Conservative	Balanced	Dynamic	Custom
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 to market conditions, product strategies, currency diversification, and product turnover. Figures are indicative only and not binding by any means.

Disclaimer

Sources:
Analysis and comments: Bloomberg, Reuters, Natixis, UBS, BNP-Parisbas
Data and graphics: Bloomberg, Reuters

IX-7 Asset Management SA