QUARTERLY HOUSE VIEWS

Q4 2020

The Second Wave

Macro

As autumn approaches, the coronavirus pandemic continues to spread globally, forcing governments to maintain or reinforce restrictions on activity. After a spurt of rapid growth as economies emerged from months of lockdown, we expect the pace of recovery to slow markedly in coming months, in particular in services as witnessed by the flash Purchasing Manager Index surveys of business confidence for September in the euro zone. However, we do not expect another series of nationwide lockdowns, which should keep economies on a path of gradual recovery. China remains a bright spot with retail sales now rising year-on-year (YoY) while industrial output growth has returned to trend.

Central Banks

Inflationary pressures remain generally in abeyance. Headline consumer price inflation in the euro zone fell -0.4% YoY in August while core prices – i.e., ex food and energy – only inched up +0.2%. This suggests that central banks can continue to focus on supporting growth via asset purchases and targeted support for bank lending. Indeed, the US Federal Reserve (Fed) recently shifted its policy framework in favour of employment and to signal greater tolerance of inflation over time. Moreover, the European Central Bank (ECB) and the Fed stand ready to ease further if activity begins to slide or if financial markets are gripped by turmoil.

Markets

We continue to prefer equities over other asset classes. Government bonds offer little value – given that yields are negative after inflation – with the exception of the additional yield (or “carry”) available on emerging market sovereigns. High quality corporate bonds (Investment Grade or IG) offer only a modest yield premium (or “spread”) over government bonds after registering strong outperformance in recent months. We expect a period of sideways trading in the euro against the dollar after the sharp summer rally. Finally, the recent pullback in gold prices offers an opportunity to add to positions.

Bottom line

We remain Neutral on equity markets in the absence of further easing plans from global central banks. Our preferred region now is emerging Asia where growth should prove resilient this year and valuations look less extended than in the developed world. Given the slowing recovery, we have downgraded euro zone equities back to Neutral. Within fixed income markets, we retain a preference for IG corporate issuers for the carry, even if further spread tightening looks unlikely. Finally, we have taken advantage of a recent bout of weakness to restore gold – our preferred diversification tool – to Overweight in portfolios.

In accordance with the applicable regulation, we inform the reader that this material is qualified as a marketing document.
CA159/H2/20

OUR STRONGEST CONVICTIONS

Diversification is key

Much of the rally from March's bear market lows has been driven by a small number of mega-cap US technology and internet stocks. Despite the obvious qualities and resilience of these businesses, their valuations have become stretched and we prefer a more diversified, balanced approach across sectors and markets. Similarly, allocations to high-quality corporate bonds, gold and hedge funds bring diversification benefits.

Better days for the euro lie ahead

The euro has given back much of July and August's advance against the US dollar, as risk aversion has grown. However, the fundamental drivers for the single currency remain strong – interest rate differentials with the dollar have collapsed, the current account remains in healthy surplus, valuations are attractive and the coming EU recovery fund should help dissipate fears of a euro zone break-up. After a period of consolidation, we expect the euro to resume its uptrend.

Investment Grade corporate bonds as the sweet spot

With $15.6 trillion outstanding in negative yielding bonds across the globe, fixed income markets are likely to prove challenging. On one side, government bonds no longer offer much in the way of diversification benefits – positive performance is hard to come by with negative yields. On the other, lower-quality High Yield bonds may see a rise in missed coupons and defaults, given the depth of the recession. That leaves Investment Grade corporate bonds as the sweet spot for portfolio construction.

Emerging Asian equities should outperform

With a second wave of new COVID-19 cases, hospitalisations and fatalities across much of Europe and the Americas, our Neutral equity weighting is justified by continued policy support from governments and central banks. The outlook is brighter across Asia-Pacific where authorities appear to be having more success in taming the virus, meaning that many economies may in fact register GDP growth this year. We have moved Overweight on emerging Asian equity markets.

Buying opportunity in gold

Gold prices hit overbought extremes at their all-time highs in early August and have since traded about 10% lower, in a move akin to the brief sell-off on margin call selling in March this year. We believe that the fundamental drivers for bullion remain strong – rates and yields are low to negative across fixed income markets, mine production has declined and demand from central banks and investors remains resilient. We have moved back Overweight.

Stay flexible

With recovery turning more sluggish and the pandemic continuing to spread globally, we expect that the next major move from central banks will be to ease policy again, most probably via enhanced asset purchase programmes. Moreover, the long-awaited US recovery plan may gain traction ahead of November's presidential election. These moves could well provide the trigger for another leg higher for risk assets and we recommend staying flexible to take advantage of opportunities as they arise.

OUR ASSET ALLOCATION

The table below presents the latest conclusions of our Global Investment Committee

			Summary house views					
			Strong UW	UW	N	OW	Strong OW	Change since last GIC
EQUITY		GLOBAL EQUITY			X			
		United States			X			
		Eurozone			X			-
		United Kingdom			X			
		Japan			X			
		Emerging				X		+
FIXED INCOME	SOVEREIGN	GLOBAL RATES		X				
		U.S. Treasuries		X				
		U.S. Breakeven			X			
		Bunds		X				
		EMU Breakeven			X			
		Gilts		X				
		Gilts Breakeven			X			
		JGBs		X				
		EM Govies ($)			X			
	CORPORATE	U.S. IG				X		
		U.S. HY			X			
		EMU IG				X		
		EMU HY			X			
		UK IG				X		
		UK HY			X			
		Duration USD*		X				
		Duration EUR*		X				
		Duration GBP*		X				
FOREX		EURUSD			X			
		USDJPY			X			
		GBPUSD			X			
		EURCHF			X			
		EM FX (vs. USD)			X			
CMDTY		Brent			X			
		Gold				X		+
ALTERNATIVE		ALT. STRATEGIES				X		
		L/S Equity		X				
		Event-Driven				X		-
		FI Arbitrage				X		
		Global Macro / CTAs			X			+
		Cash			X			

	Positioning	*Duration
O/W	Overweight	Long – 7-10 years
N	Neutral	Intermediate – 5-7 years
U/W	Underweight	Short – 3-5 years

EQUITIES	
United States	We expect the recovery to slow and also some additional volatility if the presidential election is hotly contested. We are Neutral.
Eurozone	Given the increasing number of new COVID-19 cases, further restrictions are likely to weigh on business confidence. We move from Overweight to Neutral.
UK	With the introduction of new restrictions on activity to subdue the second wave of coronavirus infections, we do not expect the UK's attractive valuations to hold much sway with international investors.
Switzerland	Given strong fundamentals, further outperformance from Swiss equities would not be a surprise.
Japan	We expect Japanese equities to perform in line with global markets as the new PM Suga is set to continue with "Abenomics". We are Neutral.
Emerging (EM)	Chinese growth is likely to continue to lift economies across Asia-Pacific. Given Asia's dominant weight in EM indices, we decided to move from Neutral to Overweight.

FIXED INCOME	
Sovereigns	Government bonds remain unattractive, offering negligible or negative yields to investors. We are Underweight.
Duration*	We prefer shorter-dated bonds across markets.
Inflation-linked	Inflation is likely to remain low for now. We are Neutral.
Investment Grade	Despite a recent rise on COVID-19 worries, IG credit spreads should remain low helped by central bank purchases.
High Yield	High Yield bonds remain more vulnerable to the economic challenges, especially the weakest issuers.
Emerging debt (in € and $)	We continue to recommend a Neutral position, with a particular focus on Asian issuers given better macro fundamentals.

CURRENCIES	
EUR/USD	The single currency remains undervalued, but we expect it to remain range-bound near current levels, before heading higher next year.
GBP/USD	Sterling has weakened over the last few weeks and is expected to trade in a range around current levels until the end of the year. We are Neutral.
EUR/GBP	Brexit negotiations are likely to dominate EUR/GBP trading in the near term. No major moves are expected.
USD/JPY	Near term, USD/JPY is likely to remain in the 106-110 range, but we expect the yen to strengthen modestly next year.
EUR/CHF	The Swiss National Bank has been less active in its FX interventions over the summer and the franc has edged lower against the euro. Looking ahead, we expect further modest franc weakness.
Emerging	Many emerging market countries face a worsening health crisis and resulting economic risks, while Asia appears to be firmly on an improving path. Overall, we are Neutral.

ALTERNATIVES	
Hedge funds	We remain constructive on hedge funds, with a particular preference for Merger Arbitrage, Long/Short Credit, Discretionary Macro traders and emerging market Global Macro specialists.
Gold	September's correction in gold prices offers an opportunity to add to gold holdings and we have moved Overweight.
Oil	We expect oil prices to trade sideways in the short term.

Source: SGPB, 25/09/2020
* Duration: short = 3-5 years, medium = 5-7 years, long = 7-10 years
HY = High Yield bonds (higher return but greater risks), IG = Investment Grade bonds (higher quality but lower return)

ECONOMIC OUTLOOK

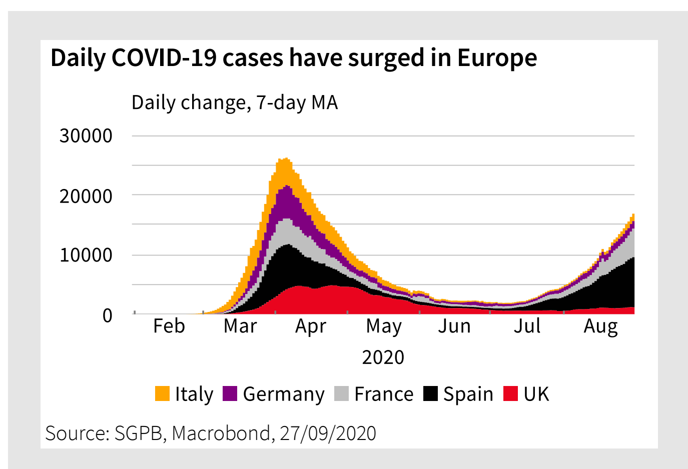
The Second Wave

This has been a strange year to say the least. We have witnessed negative oil prices, only months after an iconic Iranian general was killed in a US airstrike. A decade-long bull market and economic expansion cratered into the fastest bear market in history and a recession to rival the Great Depression. Risk assets then rose phoenix-like from the ashes as the economy staged a rapid rebound. Underlying much of this has been a once-in-a-century pandemic.

This month's market activity reflects this extraordinary year. In early September, global equity markets hit all-time highs. Since then, a resurgence in virus fears has led equities lower and volatility higher. For example, in the 17 trading days between September 1 and 23, global equities moved by more than 1% – up or down – eight times. For context, over the entire year in 2017, the global equity market moved by +/- 1% or more on just five occasions!

Such gyrations have not been the sole preserve of equity markets. So far this month, the price of gold has gone from $2,000 to $1,850, the euro has reversed months of strength to fall from about $1.20 to $1.16 while the price of oil tumbled some -13%, before stabilising. Explanations abound, but it simply boils down to risk assets drawing breath: since this year's late-March trough, global equities had bounced 50% at their recent highs led by mega-cap tech stocks like Apple, up 100%.

Despite this backdrop of heightened volatility, we recognise there has been fundamental change in the macro environment since the spring. One, we do not think that governments will reinstate full-scale economic lockdowns to fight the pandemic's second wave. While we are far from out of the COVID-19 woods – cases are surging again in Europe, for example – better protection of the vulnerable and improved therapeutics have kept death rates subdued. Many experts also expect a vaccine to be available later this year.



Source: SGPB, Macrobond, 27/09/2020

Two, economic recovery appears well entrenched, especially in the US, the world's anchor economy. The US Federal Reserve's latest GDPNow estimate for Q3 GDP growth is a seasonally adjusted annual rate of 32%! While the US economy remains well off the Q4 2019 peak, following dives of -5% and -32% in Q1 and Q2 respectively, the recession is probably over.

Three, while volatility is clearly heightened, some froth blown off stretched valuations is no bad thing, especially should momentum remain in an uptrend.

As always, we are guided by our investment process:

Economic regime: Leading economic indicators suggests the global economy has moved from a regime of "contraction" into one of "recovery". We believe there is sufficient strength in the recovery to not topple back into recession, but the path will be slow and deeply uneven.

Valuations: Valuations for equities – the largest source of risk and long-term expected returns in most portfolios – remain stretched in absolute terms. However, with global interest rates near zero and low government bond yields, there is a case for tolerance for higher-than-usual valuations.

Momentum: The global equity market remains in positive territory.

Sentiment: Of the indicators we follow, some, such as the trade-weighted US dollar, imply bullishness. Others, such as net speculative positions on ten-year US Treasuries, suggest more bearishness. Overall, sentiment is neutral.

Bottom line. We recognise the current market backdrop is more uncertain than usual and volatility is elevated – therefore we are treading cautiously and remain neutrally positioned vis-a-vis risk, despite the improving macro backdrop.

Past performance should not be seen as an indication of future performance. Investments may be subject to market fluctuations, and the price and value of investments and the income derived from them can go down as well as up. Your capital may be at risk and you may not get back the amount you invest.

FIXED INCOME

Low yields and credit spreads

Government bonds remain unattractive, offering negligible or negative yields to investors. “Credit” markets – i.e., corporate or emerging market debt – offer more value but great selectivity is required. We maintain a preference for Investment Grade (IG) issuers over High Yield (HY).

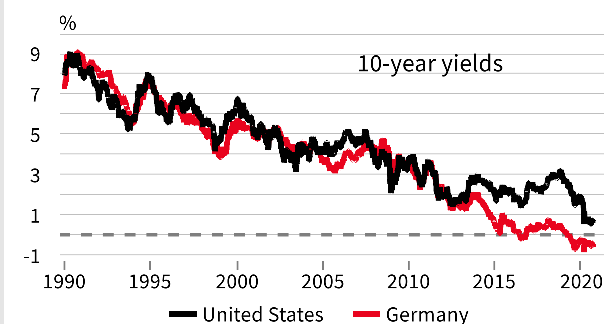
September’s sell-off in risk assets has seen money flow into sovereign bond markets helping maintain yields close to their lows. However, rising risk aversion has put pressure on credit markets, especially lower quality HY bonds where high leverage and recession conditions mean elevated default risk. Although their pace of buying has slowed in recent weeks, central banks are set to remain active investors in sovereign and corporate bond markets, which should contribute to keep bond yields low and credit spreads tight.

Sovereigns

US. Treasury yields collapsed to historic lows during the pandemic-induced turmoil in Q1 and have since settled into a narrow trading range between 0.60% and 0.80%. The Fed’s recent update to its policy framework signalled greater tolerance for inflation but, perhaps surprisingly, implied expected inflation has since fallen back to trade at 1.58% at present. We expect that inflationary pressures will remain low and that the Fed will continue asset purchases, keeping 10-year yields close to today’s levels.

Eurozone. July’s green light for the EU recovery fund has helped keep a cap on periphery “spreads” (i.e., the difference in yields between 10-year German bunds and Italian, Spanish or Portuguese bonds) as investors have concluded that euro zone breakup risk has diminished. Moreover, the ECB continues its asset purchases, buying around €20bn on average each week across its programmes. We conclude that 10-year yields and periphery spreads are likely to remain low for the foreseeable future.

Government bond yields remain historically low



Source: SGPB, Macrobond, Bloomberg, 25/09/2020

UK. The Bank of England governor Andrew Bailey recently made clear that negative interest rates were not imminent in the UK. However, with hard Brexit risks rising and tighter coronavirus restrictions, we expect monetary policy to remain extremely accommodative and 10-year sovereign yields to stay close to zero.

Credit

US. With COVID-19 cases continuing to spread and equity markets coming under pressure, corporate bond “spreads” (the yield differential over sovereign bonds) have risen in recent weeks. However, issuance of IG bonds by non-financial companies has soared 79% year-on-year to all-time highs, as companies take advantage of low borrowing costs, and shows no sign of slowing down. We continue to prefer IG credit to HY. The former benefit from direct Fed purchases and offer positive real yields while the default risk for the latter has been exacerbated by the recession.

Eurozone. Despite historically low borrowing costs, IG issuance remains well below 2009’s highs. This is largely due to the decline in new issues by financial companies – normally the mainstay of euro zone credit – which have fallen to the lowest point since 2003 and may soon be surpassed by non-financial issuance for the first time ever. IG spreads have remained low, helped by ECB purchases, while HY spreads have risen on worries about deteriorating credit quality. In this context, IG credit remains the cornerstone within fixed income portfolios.

UK. Sterling credit spreads also widened modestly in September, in line with the dollar and euro markets. Here again, we mark a preference for IG over HY issuers. Credit quality for the latter is likely to come under pressure from the recession and lingering fears about a “no-deal” exit from the EU’s single market at year-end.

Emerging debt

A number of EM sovereign issuers – such as Argentina or Turkey – face rising inflation and current account deficits, putting pressure on their currencies against the dollar. Moreover, the pandemic continues to spread across emerging economies. Nonetheless, EM government bonds offer a 340 basis point pick-up in yields over US Treasuries and we continue to recommend a Neutral position, with a particular focus on Asian issuers given better macro fundamentals.

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EQUITIES

Overweight Asia

Global equities have suffered a -5.2% correction in September but still remain close to end-2019 levels. With the pandemic still not under control in Europe and the Americas, we suggest an Overweight position in emerging Asian equities within an overall Neutral allocation in portfolios.

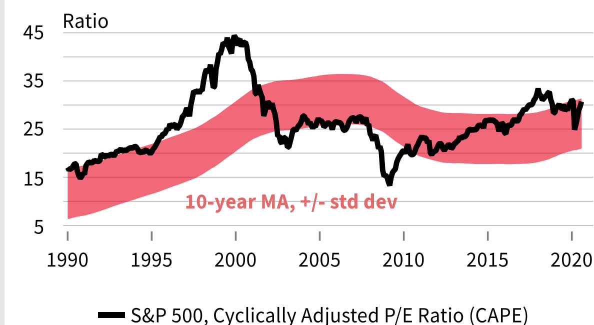
US. After a sharp August rally, US equities have traded lower over much of September as worries emerged over extended valuations and mixed economic data. Q2 earnings vastly outperformed consensus expectations, but now forecasts for Q3 earnings-per-share (EPS) have been revised higher, leaving limited room for more positive surprises. Looking ahead, we expect the recovery to slow and also some additional volatility if the presidential election is hotly contested.

September's dip in prices has done little to improve valuations which remain close to two-decade highs. Moreover, the market remains heavily dependent on a small number of mega-cap technology and internet stocks, which have dominated index performance over recent years and which trade at almost twice their 10-year median price to earnings ratio. Regarding sector preferences, we continue to balance exposure to IT with more defensive, cheaper plays like Healthcare, Utilities and Consumer Staples while Industrials should benefit from the gradual cyclical upturn.

Eurozone. Analysts have continued to revise 2020 earnings expectations lower over the summer as rising COVID-19 cases have raised concerns about new lockdowns and restrictions. Forecasts for next year call for a 52.6% rebound, but they are also likely to be revised downwards. Although we do not expect nationwide lockdowns to be reimposed – which should help economies avoid a double-dip recession – further restrictions are likely to weigh on business confidence, especially in services as demonstrated by September's flash business confidence surveys.

Recent changes to the members of the flagship Euro Stoxx 50 index have boosted the weight of growth sectors like IT at the expense of undervalued areas like banks. Despite cheap valuations, we expect Financials to continue to lag the broader market, in the absence of any likely increase in rates or bond yields ahead. Our preferred sectors are Healthcare and IT, while we would also Underweight areas like Energy and Communication Services.

US equities still look overvalued



Source: SGPB, Macrobond, 25/09/2020

UK. The recent introduction of a bill which could cancel part of the UK's Withdrawal Agreement from the EU has cast doubt on successful conclusion of ongoing trade talks, further heightening uncertainties for business. And with the introduction of new restrictions on activity to subdue the second wave of coronavirus infections, we do not expect the UK's attractive valuations to hold much sway with international investors.

Switzerland. Swiss equities have continued to outperform other regional markets, thanks to the resilient outlook for corporate earnings. Analysts only expect a 9.6% decline this year followed by a 17.0% bounce in 2021, while valuations are currently much cheaper than for euro zone equities. Moreover, net profit margins for MSCI Switzerland members have remained solid, as has their return on equity. Given these strong fundamentals, further outperformance would not be a surprise.

Japan. Tokyo outperformed global equity markets in September, despite the surprise resignation of Prime Minister Abe, the architect of Abenomics stimulus policies. The outlook for corporate earnings remains strong – the consensus expects 42.9% growth next year after -8.3% this year – and the ratio of prices to cyclically-adjusted earnings remains close to multi-decade lows. With new PM Suga set to continue with Abenomics, we expect Tokyo to perform in line with global markets.

Emerging Markets. EM equities have failed to rise above their 2007 highs in recent years while earnings have continued their upward trend (see chart). Moreover, analysts expect only a -9.2% decline in EPS this year followed by a 31.7% bounce in 2021. Much of this resilience is set to come from Asia, where Chinese growth is likely to continue to lift economies across Asia-Pacific. Given Asia's dominant weight in EM indices – China, Taiwan and South Korea alone represent 64.8% of MSCI's Emerging Market Index – we now Overweight EM equities, still with a strong Asian bias, within a Neutral allocation to global equities.

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INVESTMENT IDEA

Redefining the future of payments

The payments industry is changing rapidly with the development of new payment methods, advances in technology and through mergers and acquisitions. The share of global transactions carried out digitally has risen steadily over the last few years at the expense of cash, despite the increase in value of bank notes and coins in circulation. COVID-19 – this year's major disruptor – has accelerated the shift. Consumers have been forced to turn to digital means of payment with many shops closed and many retailers reluctant to accept cash because of virus-transmission risks. Capgemini expects non-cash transactions to grow at a compound annual rate of 14% from 2020 to 2022, creating new growth opportunities for the sector.

Four main factors are responsible for the switch towards digital payments. There has been a shift in consumer behaviour which Nielsen researchers have dubbed "the Quest for Convenience". People tend to migrate towards the quickest and most efficient solutions, and buying things with mobile phones or smart watches certainly fits the bill. A survey across Europe conducted by ING showed that 58% of respondents said they use less cash this year than last, and we expect this structural shift away from cash payments to continue. Moreover, e-commerce's share of retail sales is set for continued rapid growth as disruptors completely redefine the customer experience with new services like Amazon Pay, Alipay or WeChat Pay. And as the adoption of mobile devices has grown over the past few years, so has the number of consumers using them for payments. According to CardKnox, 75% of the Generation Z cohort use a digital payment application. Finally, governments and central banks are encouraging the switch to digital – it helps limit the size of the black economy and to ensure higher levels of tax collection.

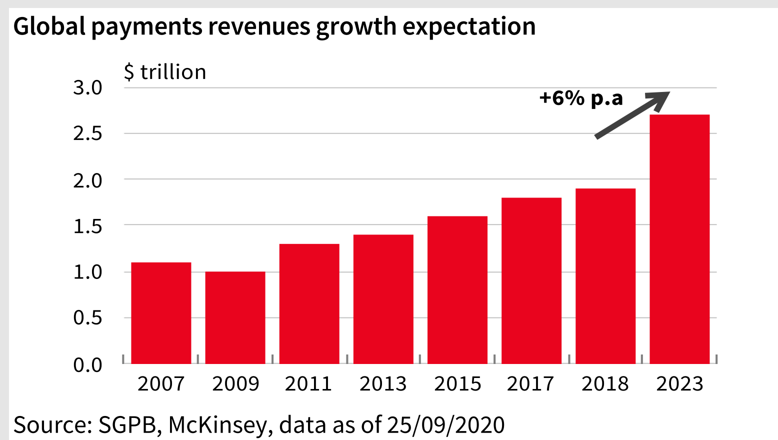
The shift from physical cash to digital has meant steady annual revenue growth for global payments of around 6% – 2017 was an outlier when growth hit 11%, driven by a sudden rise in Chinese liquidity. And according to McKinsey's latest Global Payments Report, growth should continue at this steady rate over the next few years, well ahead of International Monetary Fund projections for global GDP growth.

From an ESG perspective, the shift to digital payments could lead to the financial exclusion of those without access to the banking system, particularly in emerging markets. However, major card networks are aware of this and have undertaken to help unbanked people access electronic payment accounts – for instance, Visa set itself a goal to reach 500 million new users by 2020 and met it well ahead of schedule. Moreover, technology can bring innovative solutions – for example, Safaricom's M-Pesa enables 40 million users across Africa to send and receive payments securely via basic smartphones, generating over 11 billion transactions per annum.

However, a completely "cashless" world may prove out of reach – many people have a strong affinity to cash and are reluctant to leave a digital trace of all their purchases. Moreover, lack of global standards for cross-border payments and payment security issues remain major constraints on global digital payments growth.

Bottom line. As consumer behaviour and technology evolve, we expect continued strong growth in global payments services, in particular via digital and mobile applications. This trend should provide ample growth opportunities for the global payments ecosystem, from card networks to mobile apps, from mobile phone makers to digital currency issuers.

Global payments revenues growth expectation



Source: SGPB, McKinsey, data as of 25/09/2020

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INVESTMENT IDEA

The Changing Consumer

The COVID-19 pandemic lockdown saw shops shuttered across much of the world. Overnight, the concept of "retail therapy" – shopping for pleasure – became outmoded. Many independent retailers quickly found themselves in difficulty meeting rent payments and paying suppliers, while having to rely on government furlough schemes to meet part of their wage bill. Many larger chains also stumbled with several household names filing for creditor protection. What will the consumer landscape look like in coming years?

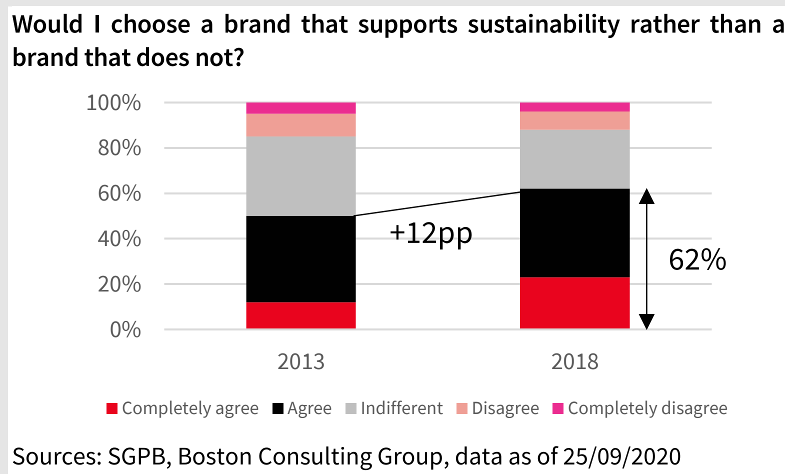
Of course, much has already changed for consumers in recent decades – the building of the world wide web enabled many transactions to shift online and companies like Amazon to grow from start-up in 1994 to the world's second-largest company today. But this year has seen a step-change for e-commerce – according to Forbes, the pandemic has accelerated growth by 4 to 6 years. Moreover, rising concerns about climate change have forced a rethink about the carbon footprint laid by many consumer goods, with many shoppers deciding to change their habits.

Looking ahead, we see a number of structural changes in what we consume. In the near term, the pandemic has forced a shift from international travel to domestic tourism but, longer term, we expect another shift towards fewer but longer trips more focused on the quality of the travel experience. In terms of consumer goods, both hardware and foodstuffs, the future will see more importance placed on provenance and products' ecological impact, on organic, natural produce and on "nutraceuticals", i.e., foodstuffs with health benefits. In luxury goods, we see increased scope for collaborations – with lifestyle brands, influencers and celebrities – along the lines of Louis Vuitton X Supreme, LVMH's venture with the New York streetwear brand. And while Generation Z consumers have shown themselves to be heavily influenced by collaborations, they are also keen to establish the sustainability and the social responsibility of brands, another long-lasting trend for the future.

We also see a number of changes in how we consume. Many of these changes will of course be enabled by digital technology and mobile communications. In sports, culture and entertainment, home viewing and virtual events will increasingly complement live sporting events, concerts, theatre and cinema – for example, 2019's League of Legends championship generated 478m hours of viewing on Twitch and YouTube, making it one of last year's major events. In health and wellness, the marriage of technology with healthcare enables wearable devices like Fitbits or the Apple Watch to monitor our health metrics while today's telecommunications tools allow remote consultations with practitioners. Many companies will have to increase cooperation with bloggers, influencers and celebrities – 95% of Generation Z consumers use social media to interact through them with luxury brands according to BCG. And finally, we will also see increasing convergence between entertainment and education – already 35% of Netflix subscribers use it to access educational content according to YouGov.

Bottom line. Taken together, the changes in what and how we consume will revolutionise consumer spending in coming years, creating new growth opportunities for the manufacturers and retailers who are able to update their business models. For investors, this will offer new opportunities in areas like mobile technology, luxury and fast-moving consumer goods, foodstuffs, education, leisure, gaming and social media.

Would I choose a brand that supports sustainability rather than a brand that does not?



Sources: SGPB, Boston Consulting Group, data as of 25/09/2020

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CURRENCIES

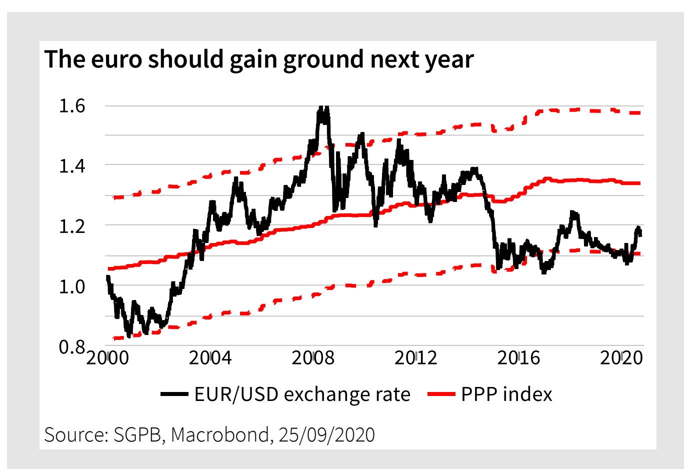
Running out of steam

We expect the recent dollar rally to run out of steam as investors begin to fret about the presidential election. Euro zone break-up risk has diminished, which should help the single currency recover from the recent bout of weakness. Emerging currencies look set to remain at low levels, with the singular exception of the Chinese renminbi.

Dollar Index. With its yield advantage diminished, unprecedented monetary stimulus, enormous twin deficits, imminent elections and rising equity markets, this is not a bullish environment for the US dollar. Moreover, Jerome Powell recently stated that the Fed would be happy for inflation to run above 2%, signalling that rates will likely stay super low for a very long time. After September's gains, we expect the US dollar to trade sideways for now, but the longer term picture is not one conducive to USD strength.

EUR/USD. The Fed has essentially told markets that rates aren't going anywhere for a very long time, removing one of the dollar's props. Nonetheless, EUR/USD has fallen from 1.20 in August to around $1.16, still well above where it began the year. ECB members recently expressed concerns about the euro strength and will likely be pleased by the recent weakness. Overall, the single currency remains undervalued, but we expect it will remain range-bound near current levels, before heading higher next year.

GBP/USD. GBP/USD has weakened from August's two-year highs at almost 1.35, as the harsh realities of hard Brexit risks and very weak growth data have brought Sterling back down below $1.28 – a slide of almost 5% in a few short weeks. Although we are seeing signs of stabilisation at these levels, the recent spike looked overdone in our view. For the last quarter of 2020, we expect GBP/USD to trade in a range around current levels.



Source: SGPB, Macrobond, 25/09/2020

USD/JPY. Since April, USD/JPY has traded within a narrow range between 104 and 110. Yen volatility has been low, compared with other safe havens such as gold. Considering the US dollar weakness over most of this time and resurgent virus fears, it is perhaps surprising that the yen hasn't strengthened beyond current levels near ¥106. Nonetheless, we expect the yen to continue to offset other risks in portfolios, especially in times of market turbulence.

EUR/CHF. On the back of the European Council's green light for the EU recovery fund, traders' fears of euro zone break-up risk have dissipated, helping take some upward pressure off the Swiss franc. Accordingly, the Swiss National Bank has been less active in its FX interventions over the summer and the franc has edged lower against the euro. Looking ahead, we expect further modest franc weakness.

EM currencies. Many emerging market countries face a worsening health crisis and resulting economic risks which we fear will negatively affect local currencies. Since mid March, commodity-linked currencies have been hit particularly hard, especially the Brazilian peso and Russian rouble, as have inflation-beset currencies like the Argentinian peso and Turkish lira. The JP Morgan index of emerging currencies remains close to all-time lows, but lasting recovery is unlikely for now.

USD/CNY. US/China trade relations remain on a knife edge, with each country giving very little ground. That said, USD/CNY has been falling steadily since late May, with recent dollar strength having little impact – the USD still buys less than 7 renminbi. Looked at in isolation, this isn't good for the Chinese economy as it makes exports more expensive. However, the central bank seems unworried and has put in place domestic counterbalances such as fiscal spending and bank lending to reduce any negative impact.

Past performance should not be seen as an indication of future performance. Investments may be subject to market fluctuations, and the price and value of investments and the income derived from them can go down as well as up. Your capital may be at risk and you may not get back the amount you invest.

ALTERNATIVES

Reinforcing gold

September's correction in gold prices offers an opportunity to add to gold holdings and we have moved Overweight. Oil should trade sideways in coming months. We remain constructive on hedge funds, with a particular preference for Merger Arbitrage, Long/Short Credit, Discretionary Macro traders and emerging market Global Macro specialists.

Commodities

Oil

Crude oil prices corrected in September as the pandemic continued to spread globally and new restrictions on activity put a damper on mobility and demand for oil. The International Energy Agency (IEA) now expects total global oil demand to fall 8.4 m barrels per day (mb/d) in 2020 before recovering 5.5 mb/d next year, still leaving it well below 2019 levels. On the other hand, global supply is set to shrink by 7.1 mb/d this year, meaning that oversupply is likely to persist.

In this context, OPEC and Russia held talks in mid-September to shore up support for the output cuts – currently set at 7.7 mb/d – which are due to run until year-end in order to put a floor under prices. In the longer term, further production cuts could be driven by oil majors in developed markets. For example, BP announced plans in August to cut hydrocarbon output by 40% by 2030 while boosting low-carbon investment 10-fold.

In the short term however, we expect oil prices to trade sideways.

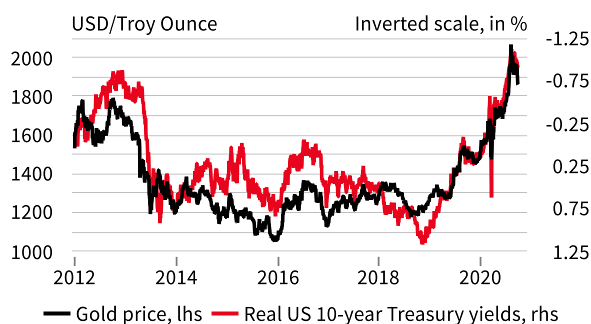
Gold

As the Dollar Index bounced and equity markets sold off in September, gold prices tumbled, down some -10% from August's all-time high. The decline was reminiscent of the brief correction in March this year when margin selling to raise cash pushed equities and gold down together. We now expect gold to resume its uptrend, just as it did from April onwards.

Demand for gold from investors remains strong. Inflows into gold-backed ETFs have triggered 938 tonnes (t) of bullion purchases so far this year, taking total holdings to a new all-time high of 3,824t at end August. On the other hand, central bank purchases hit the lowest monthly level since December 2018. However, physical demand for gold showed signs of life in August – wholesale demand picked up in China and Indian imports hit a nine-month high – while gold supply fell -6% in the first half on coronavirus disruption.

The recent correction in gold prices offers an opportunity to increase exposure at an attractive level.

We expect gold to resume its uptrend



Source: SGPB, Macrobond, 25/09/2020

Hedge funds

Long/Short (L/S) Equity

In the run-up to November's presidential election, we expect volatility to rise across equity markets, especially if the result is close-fought. This should favour variable bias managers over Market Neutral L/S funds, which will also be hit by the continued decline in dispersion between individual stocks' returns, a key source of their returns.

Event Driven

We have downgraded Event Driven funds from Overweight to Neutral, to reflect a deterioration in the outlook for Special Situations specialists. These managers tend to run portfolios with relatively high exposure to the direction of stock prices, a source of risk ahead of the elections. Opportunities for Merger Arbitrage still look attractive on the other hand.

Fixed Income Arbitrage

Conditions for L/S Credit Arbitrage managers are likely to improve – the COVID-19 recession has put pressure on corporate balance sheets and the dispersion of returns between stronger and weaker issuers will offer ample arbitrage opportunities. Moreover, their strong credit analysis and robust risk controls should help smooth returns.

Global Macro / CTAs

With higher asset price volatility expected, Discretionary Macro traders should benefit given their highly tactical approach and we have moved Overweight. In addition, the carry (additional yield) available in EM-focused Global Macro funds is attractive in today's low yield environment. On the other hand, more systematic strategies like trend-following (known as CTAs) may struggle in this context.

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TACTICAL AND STRATEGIC THEMES

Strategies still open

Launched	Conviction	Strategy description	Time horizon
27/11/14	Blue gold (Water)	Many regions of the world face large water supply disruptions. Water remains underpriced.	Strategic
06/10/17	Convertible Bonds – Yin and Yang	CB combine the attributes of different asset classes in one security. As long as their credit quality is not impaired, they can offer unlimited upside with downside protection.	Strategic
08/12/17	Insurance-Linked Securities – Marching to a Different Drum	ILS represent a source of uncorrelated returns for bond portfolios. The recent drawdowns linked to US hurricanes create a new opportunity in this segment.	Strategic
29/03/18	Artificial Intelligence: from fiction to reality	Global spending on artificial intelligence is expected to rise from $12bn in 2017 to $57.6bn in 2021. As investment increases, AI should bring transformation to nearly every sector.	Strategic
07/12/18	Cybercrime – the omnipresent risk	As internet connectivity in the global economy has become indispensable, the scale of cyber risks means sustained investment in cybersecurity.	Strategic
20/03/19	Bridging the gender gap	Gender equality represents a strategic advantage from which businesses can draw lasting benefits. Investing in such companies should allow investors to reap those rewards.	Strategic
21/06/19	5G Technology: a breakthrough for telcos	The 5G revolution could create attractive investment opportunities for network suppliers and businesses able to leverage the capabilities offered by the new network.	Strategic
21/06/19	Africa's business revolution	Africa is the new frontier in terms of growth and investment. Rapid expansion across the continent is creating attractive opportunities for risk-taking entrepreneurs and investors.	Strategic
21/06/19	Climate change – stepping-up decarbonisation	The global transition to a low-carbon economy offers investment opportunities in a wide range of sectors.	Strategic
21/06/19	Green (Bond) shoots	With improving liquidity, green bonds are a promising asset class offering both positive impact and long-term sustainability.	Strategic
18/09/2019	Food for Thought – Sustaining the World	The challenge of feeding the world creates investment opportunities in companies making food production healthier and more sustainable.	Strategic
29/11/2019	The Final Frontier – Space investment lifts off	Rapid technological progress in satellites and rockets and the proliferation of start-up entrants are opening up an investment frontier.	Strategic
29/11/2019	The HealthTech Revolution – Investing for a healthier future	Rising costs and growing needs will force disruption of healthcare by technology insurgents.	Strategic
30/03/2020	ESG – Sustainability for the Long Term	We believe that high sustainability and ESG standards will prove a key competitive advantage for long-term success	Strategic
26/06/2020	Waste not, want not	Reducing, reusing and recycling waste products will ensure growing demand for waste management specialists	Strategic
26/06/2020	Reinventing the factory	The wake-up call served by COVID-19 will force increasing numbers of industrialists to embrace the Industry 4.0 revolution	Strategic
29/09/2020	Redefining the future of payments	COVID-19 will accelerate the shift from cash and traditional means of payment to the dominance of digital solutions in global payments systems.	Strategic
29/09/2020	The Changing Consumer	With Millennials giving way to Generation Z consumers, profound changes are are sweeping consumption patterns.	Strategic

Sources: Societe Generale Private Banking, Datastream. Data as at 25/09/2020 * Strategic: 1-3 years. Tactical: 3-12 months

☐ Denotes a change from our previous Quarterly

Strategies closed

Launched	Conviction	Closing rationale	Type
15/06/16	How demographic changes shape future spending	With Millennials giving way to Generation Z consumers, profound changes are are sweeping consumption patterns. Time to switch to The Changing Consumer.	Strategic
06/07/17	Millennials: Redefining the rules	With Millennials giving way to Generation Z consumers, profound changes are are sweeping consumption patterns. Time to switch to The Changing Consumer.	Strategic

Sources: Societe Generale Private Banking, Datastream. Data as at 25/09/2020

GLOBAL ECONOMIC FORECASTS

Growth and inflation

YoY changes in %	Real gross domestic product growth					Consumer price indices				
	2018	2019f	2020f	2021f	2022f	2018	2019f	2020f	2021f	2022f
World (Mkt FX weights)	3,2	2,6	-4,0	5,0	2,4	3,0	2,8	2,1	2,2	1,6
World (PPP weights)**	3,7	3,0	-3,6	5,3	2,5	3,8	3,7	3,1	2,9	1,7
Developed countries (PPP)	2,2	1,7	-5,4	4,3	1,9	1,9	1,4	0,7	1,2	1,4
Emerging countries (PPP)	4,6	3,9	-2,5	5,9	2,8	5,0	5,2	4,6	3,9	1,9
Developed countries										
US	3,0	2,2	-4,2	3,4	2,3	2,4	1,8	1,2	1,7	2,0
Eurozone	1,9	1,3	-6,6	4,8	1,8	1,8	1,2	0,3	0,8	1,2
Germany	1,3	0,6	-5,6	3,0	2,2	1,9	1,3	0,5	1,3	1,2
France	1,8	1,5	-7,4	6,7	1,3	2,1	1,3	0,4	0,5	1,2
Italy	0,7	0,3	-9,0	5,2	1,6	1,2	0,7	-0,1	0,4	1,0
Spain	2,4	2,0	-10,4	8,1	2,4	1,7	0,8	-0,3	0,6	1,0
UK	1,3	1,5	-10,3	7,8	2,4	2,5	1,8	0,6	0,9	1,5
Japan	0,3	0,7	-4,4	4,5	1,8	1,0	0,5	0,1	0,5	1,5
Switzerland	2,7	1,2	-4,7	2,6	1,9	0,9	0,4	-0,8	-0,7	0,2
Australia	2,8	1,8	-3,5	3,5	4,0	1,9	1,6	0,8	1,5	1,6
Emerging countries										
China	6,7	6,1	2,5	7,5	5,0	2,1	2,9	2,8	1,8	2,3
South Korea	2,9	2,0	-1,0	2,9	2,7	1,5	0,4	0,4	1,1	1,3
Taiwan	2,7	2,7	1,2	3,2	2,7	1,0	0,8	-0,2	0,9	1,4
India* **	6,6	4,9	-7,9	7,1	4,2	4,0	3,7	5,8	3,0	4,0
Indonesia	5,2	5,0	-1,5	6,0	5,4	3,2	2,8	2,2	2,5	2,9
Brazil	1,2	1,1	-5,7	3,8	2,0	3,7	3,7	2,7	3,0	3,2
Mexico	2,2	-0,3	-9,5	4,9	2,5	4,9	3,6	3,4	3,4	3,3
Chile	3,9	1,1	-6,4	6,1	2,8	2,7	2,3	2,7	1,9	2,5
Russia	2,5	1,3	-4,3	3,0	2,0	3,1	4,2	3,6	4,0	3,9
Slovakia	3,9	2,4	-8,0	7,6	3,9	2,5	2,8	2,4	1,9	2,3
Czech Republic	3,2	2,3	-5,0	6,0	3,0	2,1	2,8	3,0	1,7	1,7

Sources: SG Cross Asset Research / Economics, IMF, 25 September 2020
* (f: forecast)
** PPP: Purchasing Power Parity
*** In India, the numbers are averaged over the Fiscal Year, ending in March.

Forecast figures are not a reliable indicator of future performance.

MARKET PERFORMANCE

Developed market equities	Performance – total return (in local currency)								
	Current level	1m	3m	YTD	12m	2Y	3Y	4Y	5Y
S&P500	3237	-4,6%	3,8%	1,6%	10,3%	14,9%	37,2%	61,9%	84,8%
DJ Euro Stoxx 50	3180	-2,4%	-3,1%	-13,0%	-7,6%	-1,2%	-0,9%	19,8%	22,6%
FTSE100	5899	-1,6%	-5,8%	-19,8%	-16,7%	-14,7%	-9,0%	0,2%	19,4%
Topix	1644	2,5%	3,8%	-3,1%	4,4%	-4,3%	6,0%	33,6%	25,9%
MSCI AC World ($)	552	-3,2%	4,0%	-0,7%	7,7%	9,8%	22,0%	45,0%	62,5%

Developed market bonds	Performance - total return (in local currency)								
	Yield to maturity	1m	3m	YTD	12m	2Y	3Y	4Y	5Y
BAML Corp Euro IG	0,58%	0,0%	2,0%	0,7%	0,3%	6,2%	6,5%	7,0%	14,2%
BAML Corp Euro HY	4,12%	0,2%	2,9%	-2,0%	-0,4%	4,8%	6,0%	14,0%	22,3%
BAML Corp US IG	2,05%	-0,3%	2,3%	7,1%	8,5%	22,6%	20,9%	23,7%	33,9%
BAML Corp US HY	6,12%	-0,4%	2,8%	-0,5%	1,7%	8,7%	12,0%	22,3%	34,7%
BAML Corp UK IG	1,80%	0,1%	2,1%	5,2%	4,7%	16,7%	17,1%	16,8%	35,3%
FTSE US Sovereign 3-7y		0,1%	0,5%	7,2%	7,3%	16,6%	14,3%	13,6%	17,3%
FTSE Germany Sovereign 3-7y		0,0%	0,1%	0,6%	-0,9%	1,7%	1,6%	0,5%	3,0%
FTSE UK Sovereign 3-7y		0,1%	0,1%	3,1%	2,1%	6,4%	6,3%	4,9%	10,6%
FTSE Japan Sovereign 3-7y		0,2%	0,0%	0,0%	-1,0%	0,1%	-0,3%	-0,7%	0,4%

Emerging market equities	Performance – total return (in USD)								
	Current level	1m	3m	YTD	12m	2Y	3Y	4Y	5Y
MSCI EM	1078	-1,1%	7,2%	-1,4%	9,0%	8,3%	6,2%	30,9%	55,9%
MSCI EM Asia	599	-0,3%	10,3%	7,8%	19,7%	16,2%	16,6%	45,0%	72,9%
MSCI EMEA	207	-3,7%	-2,3%	-20,3%	-13,9%	-10,1%	-14,3%	-1,8%	7,8%
MSCI Latam	1834	-5,7%	-6,6%	-35,8%	-29,3%	-23,0%	-32,1%	-13,2%	14,3%

Emerging market bonds	Performance – total return (in USD)								
	Yield to maturity	1m	3m	YTD	12m	2Y	3Y	4Y	5Y
BAML EM Sovereign	4,90%	-1,7%	3,0%	-1,1%	0,9%	10,8%	6,5%	12,1%	28,2%
Asia	3,12%	-1,5%	4,4%	4,2%	4,7%	20,6%	17,8%	21,6%	40,3%
EMEA	4,92%	-1,2%	1,6%	-1,4%	0,4%	12,4%	8,6%	15,1%	26,9%
Latam	5,83%	-2,6%	4,0%	-3,5%	-0,5%	4,0%	-1,0%	4,1%	24,5%
BAML EM Corp	3,91%	-0,3%	3,1%	3,5%	5,7%	17,9%	16,2%	19,3%	29,9%
Asia	3,27%	0,0%	2,8%	5,5%	6,9%	17,0%	14,9%	20,4%	33,3%
EMEA	3,85%	-0,2%	2,9%	3,3%	6,1%	13,2%	11,3%	22,3%	40,4%
Latam	5,32%	-1,1%	3,9%	-0,2%	3,0%	16,3%	14,8%	18,8%	28,4%

Source: Societe Generale Private Banking, Bloomberg, Datastream (data as of 24/09/2020), YTD = year-to-date

BAML: Bank of America Merrill Lynch
Corp: Corporate
EM: Emerging Market
EMEA: Europe, Middle East, Africa
IG: Investment Grade
HY: High Yield
LatAm: Latin America
Gvt: Government

MARKET PERFORMANCE AND FORECASTS

		Forecasts		Performance					
Currencies	**Current**	**3 months**	**12 months**	**YTD**	**12m**	**2Y**	**3Y**	**4Y**	**5Y**
EUR/USD	1.17	1.18	1.21	4,0%	6,1%	-0,8%	-2,5%	3,9%	4,2%
USD/JPY	105	106	103	-3,0%	-2,0%	-6,4%	-5,9%	4,3%	-12,4%
EUR/CHF	1.08	1.08	1.11	-0,7%	-1,0%	-4,3%	-7,0%	-1,1%	-1,7%
GBP/USD	1.27	1.27	1.31	-4,0%	2,4%	-2,7%	-5,7%	-1,9%	-16,5%
EUR/GBP	0.92	0.93	0.92	8,5%	3,6%	2,0%	3,5%	5,9%	24,9%

		Forecasts							
10-year yields	**Current**	**3 months**	**12 months**	**YTD (bps)**	**12m**	**2Y**	**3Y**	**4Y**	**5Y**
USA	0.7%	0.7%	0.9%	-123	-103	-239	-159	-94	-148
GER	-0.5%	-0.5%	-0.2%	-32	8	-96	-95	-42	-110
UK	0.2%	0.2%	0.5%	-61	-33	-133	-114	-51	-157

		Forecasts							
Commodities	**Current**	**3 months**	**12 months**	**YTD**	**12m**	**2Y**	**3Y**	**4Y**	**5Y**
Gold in USD	1869	1900	2050	22,9%	22,5%	56,0%	44,2%	39,5%	65,2%
Oil (Brent) in USD	41.8	42.5	46.0	-36,9%	-35,0%	-47,0%	-26,4%	-11,9%	-13,8%

		Forecasts							
Equities	**Current**	**3 months**	**12 months**	**YTD**	**12m**	**2Y**	**3Y**	**4Y**	**5Y**
S&P 500	3237	3350	3550	1,6%	10,3%	14,9%	37,2%	61,9%	84,8%
Euro Stoxx 50	3180	3300	3600	-13,0%	-7,6%	-1,2%	-0,9%	19,8%	22,6%
FTSE 100	5899	6050	6300	-19,8%	-16,7%	-14,7%	-9,0%	0,2%	19,4%
Topix	1644	1675	1775	-3,1%	4,4%	-4,3%	6,0%	33,6%	25,9%

Source: Societe Generale Private Banking, Bloomberg, Datastream (data as of 25/09/2020), bps = basis points

BAML: Bank of America Merrill Lynch
Corp: Corporate
EM: Emerging Market
EMEA: Europe, Middle East, Africa
IG: Investment Grade
HY: High Yield
LatAm: Latin America

Forecast figures are not a reliable indicator of future performance.

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