2021 Perspective

PLURIMI

Patrick Armstrong, Chief Investment Officer

4 January 2021

2020 saw a major divergence between the economy and equity market performance. 2020 was a shocking year in many aspects but it ended up as a positive year for both risk assets and safe havens.

The initial months of 2021 may see muted growth as government imposed restrictions and a cautious population lead to a contraction in January. However for the year as a whole the global economy is set up to deliver a strong recovery. The path of consumer spending will be key. Initial improvements in Q42020, driven by a relaxation of social distancing measures and policy support are already clear.

Global outstanding debt, including that of governments, corporates and households, reached a record 265% of gross domestic product at the end of 2020. Governments will eventually come under pressure to reduce deficits when markets question sustainability and bond yields rise meaningfully. Fiscal austerity and tighter monetary policy are not going to be considered in 2021.

Central banks have unleashed a dizzying number of unconventional steps to cushion the economy from the impact of the coronavirus. The Fed's response to the virus has been robust and ongoing. Liquidity has been far more important than valuations in 2020, and we expect that continues to be the case in 2021. Growth remains scarce and assets which provide it will continue to demand premium multiples.

Negative real yields are the fuel for almost all risk assets. Central bank policy is designed to punish cash which stays on the side-lines and seemingly diverse assets such a gold, credit, equities, property all are driven by the same forces. While negative real yields provide the impetus for higher prices, anything which changes this dynamic is a major risk for all asset prices. A slow down in growth expectations or central banks letting 10 year yields rise are the two most obvious risks.

A weak USD, an improving economy, and negative real yields are positives for commodity prices in 2021.

2020 Review

Asset prices diverged with real economy on monetary and fiscal stimulus. Japan's Nikkei was strongest regional index while the UK's FTSE 100 was weakest.

Asset Allocation

Equities outside of the US are most attractive, led by Japanese equities which continue to offer the best value. Monetary policy and an economic recovery will continue to drive higher prices but valuations are stretched.

Global Economy p.4

We expect a slow start to the year due to continued lockdowns but a second half rebound based on containment of the virus, and proactive fiscal and monetary policy is very likely.

Debt p.9

G7 at record debt to GDP levels but consequences are not likely relevant in 2021.

Central Banks p.10

Rates lowered to zero everywhere and open ended QE, which includes corporate bonds. More purchases and possible yield curve control are next.

Equities p.13

Equities expensive again on most measures but compared to bonds they offer much better return potential. We prefer a blend of value and growth rather than making a big style call in 2021.

Fixed Income p.20

Investment grade credit has the support of central banks, and still offers moderately attractive spread. Bank debt offers best return for risk .

Commodities p.22

Most commodities have seen new supply slowing, while demand should jump as the economy re-opens. Broad based exposure makes sense with a positive economic backdrop and weak US$.

Currency p.22

The twin deficits, expected economic recovery and loose monetary and fiscal policy should lead to a weakening of the US$. The risk to this scenario is a shock which creates risk aversion and a bid USD.

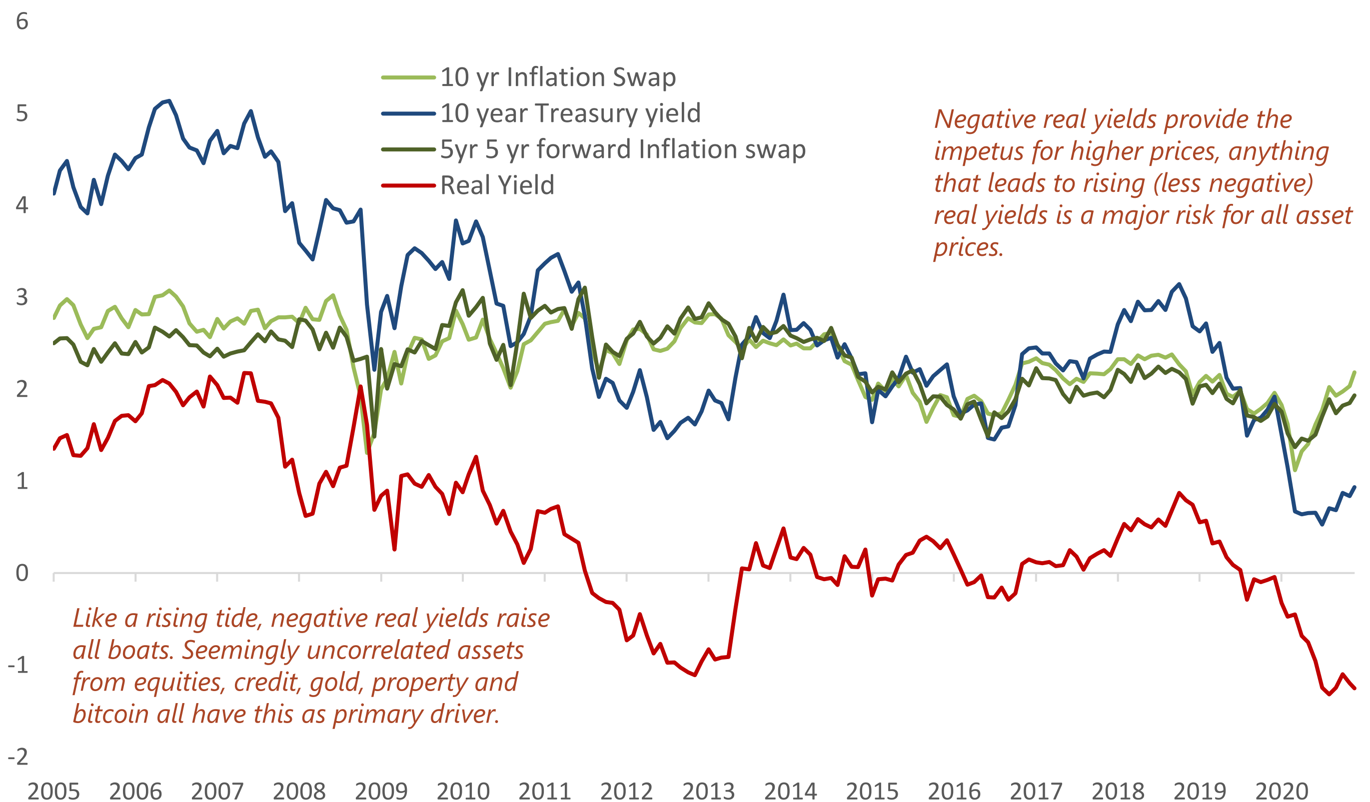
"Successful investing is anticipating the anticipations of others."

John Maynard Keynes, Economist and Financier. Father of Keynesian economic theory.

"Prediction is very difficult, especially if it's about the future."

Niels Bohr, Nobel laureate in Physics

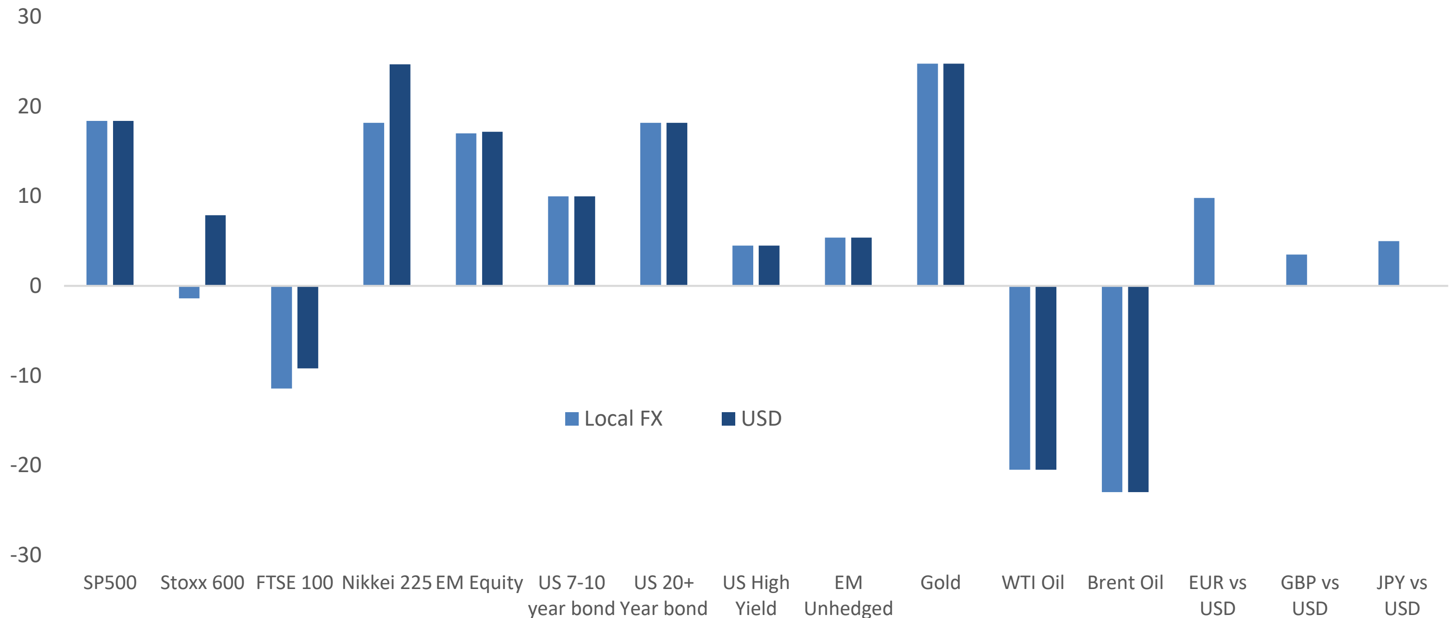
Most important chart for 2021: Treasury yield and Inflation swaps



Source: Plurimi Wealth LLP

2020

Performance by asset class (% USD)



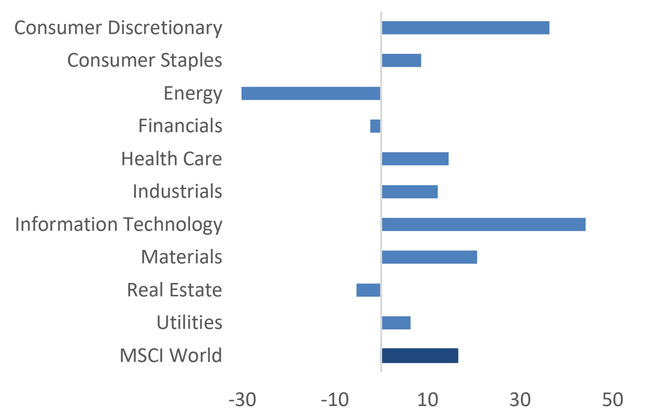
Source: Bloomberg, Plurimi Wealth LLP

2020 was a shocking year is many aspects but it ended up as a positive year for both risk assets and safe havens. The way the pandemic accelerated and the severity of the lockdowns were beyond anyone's expectations. The size of the government stimulus and the magnitude of the equity market rebounds were also unprecedented. Asset prices diverged from the real economy throughout 2020. Massive monetary stimulus led to very strong returns for almost all assets in the final three quarters of the year. Technology, and consumer discretionary, particularly social media and e-retailing, were the strongest equity sectors in 2020. These sectors saw their business models unimpeded, and in some cases rewarded by the lockdowns put in place to fight the pandemic. Oil saw increased production in the early months followed by plummeting demand once lockdowns began. This led to a short period where WTI prices moved into negative territory. Oil prices fell by more than 20% for the year. Government bond yields fell to record lows in the summer, as safe haven demand increased and central banks made aggressive purchases.

The Nikkei outperformed the developed world in US$ terms, and emerging market equities saw strong relative performance from China and Korea, offset by poor performance from commodity exporting countries. UK equities were the significant regional laggard, hurt by an uncertain economic backdrop with Brexit unresolved until year end and a large weighting to the underperforming energy and banking sectors. Gold was up by 20% for the year and the euro was the strongest major currency rising by 7% vs the US$.

Tech & consumer stocks, the Nikkei and Gold were the leaders of 2020, while UK equities, energy stocks and oil lagged.

2020 MSCI World Sector performance (USD %)



Source: Bloomberg, PW

Global economic dashboard

Indicator	Derivative		Interpretation & outlook
	1st	2nd	
Growth			
Global leading economic indicator	+	0	Sharp improvement from very low base.
ZEW/IFO	+	0	Positive but down from decade high in September.
US ISM manufacturing new orders	+	0	Contractionary level but improving.
Consumer confidence	0	+	Still low but improving.
Business confidence	0	0	Neutral readings, stronger than the spring but below September.
Global PMI	+	+	Back to expansionary levels and trend is higher.
G7 employment	-	+	Unemployment still elevated but showing improvement
Global trade volume	0	+	Global trade fell sharply but is recovering.
Oil prices	0	0	Oil prices have stabilized below previous equilibrium. Positive for spending, but impacting employment in many countries
Policy			
Real policy rate	+	+	Global policy has been loosened sharply and looks to get looser still.
Nominal GDP-bond yield gap	-	+	Nominal growth has fallen by more than bond yields but will turn very reflationary in the second half.
G7 credit growth	+	+	Credit supply and demand is growing .
Financial stress	+	+	Ted spread narrowed from decade highs and credit spreads continue to narrow.
Fiscal thrust	+	+	Significant debt and deficits in response to virus and unemployment. MMT next?
Inflation			
Core CPI	-	+	Demand shock and falling commodity prices > than supply disruption, but inflation swaps are starting to move higher
Wage growth	0	0	Wage growth almost irrelevant with employment backdrop.

Growth indicators have turned positive or are quickly moving in that direction.

Central banks all-in

Inflation is not a 2021 story

Source: Bloomberg, Plurimi Wealth LLP

Global Economy

Vaccines pave path for growth but start of year will be weak

Our global economic dashboard shows an economy which is recovering from a sudden stop. It has the potential for very strong growth but the near term prospects are muddied by the second wave of the pandemic. In March 2020 the dashboard had red negatives everywhere, and over the recent quarters both columns have turned predominantly green. It appears that policy rates and fiscal stimulus have kept the economy from falling into a longer lasting recession. We expect the economy to make incremental progress in the early parts of 2021 and sharp growth when vaccines allow a rebound in services. The economy will benefit from significant monetary and fiscal thrust, as well as a recovery led by pent up demand from deferred expenditure. We expect policy will remain supportive for growth even after the economy begins its recovery. Strong global growth is likely in the coming year, but improving growth is not the same a strong economy. Fiscal policymakers across the major advanced economies stabilised the purchasing power of people who have lost their jobs or been furloughed. Monetary policymakers have managed to loosen financial conditions and many parts of the global economy are re-opening. All of this points to a continued expansion, but the coronavirus outbreak has rendered precise forecasting impossible and assessing the direction of trends is all that can be done with confidence for the moment.

We expect the economy to make incremental progress in the early parts of 2021 and sharp growth when vaccines allow a rebound in services

Europe and most of East Asia have shown more success in containing the virus, and this bodes well for their recoveries. While the trend is positive, there are very clear risks as well. The US has had less success containing the virus and new cases are as high as ever there. Part of this comes from the sharp increase in testing and part from re-opening economies in Southern states more aggressively. A rise in infections as the economy opens up further, might trigger renewed government restrictions or voluntary changes in behaviour that weigh on growth.

Global Economy

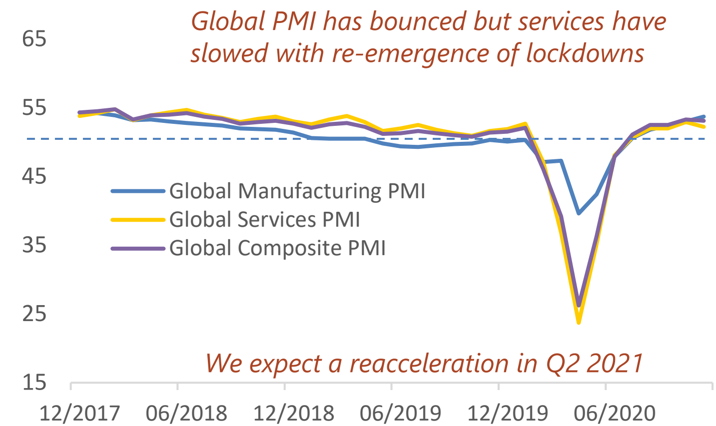
The initial months of 2021 may see muted growth as government imposed restrictions and a cautious population lead to a contraction in January. However for the year as a whole the global economy is set up to deliver a strong recovery. Fiscal stimulus will remain a tailwind but will lessen in importance as the global economy normalises from the lockdowns that plagued 2020. A range of Covid vaccines underpin our optimistic view. Uncertainties remain on logistics and the rollout timeframe but the vaccines reduce the downside risks for the global economy. The UK and US have already begun vaccinating their populations and we expect by the time Q3 arrives we will be on the track for herd immunity. We expect a sharp boost to global growth from Q2 as the virus begins to be controlled and lockdowns are no longer needed. We expect an eventual rotation from goods to services consumption as the need for social distancing diminishes. The biggest risk to this view is a slow pace of vaccination and a reluctance to be vaccinated.

Global growth of 6% and developed market of 5% are achievable levels in 2021. The 2020 economic collapse is largely reversible. Travel and entertainment were decimated and are likely to rebound sharply once governments re-open economies based on falling hospitalisations.

China serves as a case study for the rest of the world's recovery. In China GDP is almost back to the pre-pandemic trend, and the pace of growth remains quite robust. Policy has supported growth, and we expect the same to occur in the rest of the world as well. The Chinese economy has seen in industrial value added pick up to 7.0% y/y in November. Growth in manufacturing investment increased markedly to 10.8%. We expect the growth drivers in 2021 to shift towards consumption and corporate investment, away from infrastructure investment and to a lesser extent real estate investment.

Globally we will be watching for a continued recovery in employment, which should provide further impetus to household consumption growth. While we expect continued job growth we do not expect the US economy to regain the level of employment it had in early 2019 for several years. This is an area which could positively surprise us, but the vast number of layoffs across so many industries may be longer lasting than expected. Many companies have realised they can do more with less during the shutdown.

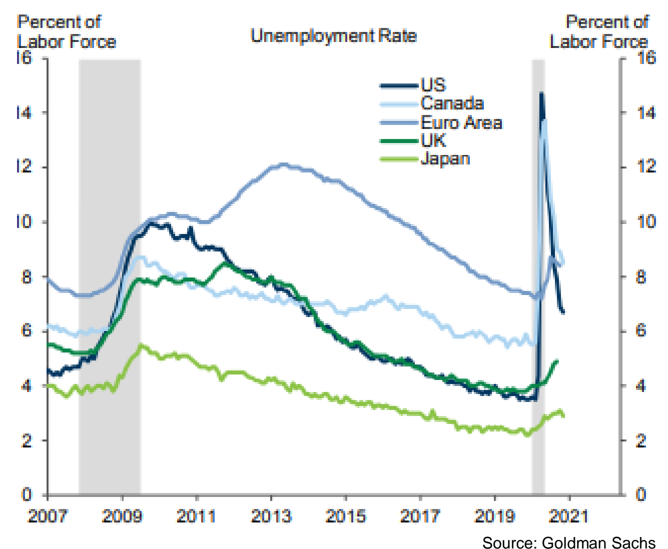
Global PMI



China Economic rebound

Source: Bloomberg, Plurimi Wealth LLP

Unemployment rate (%)

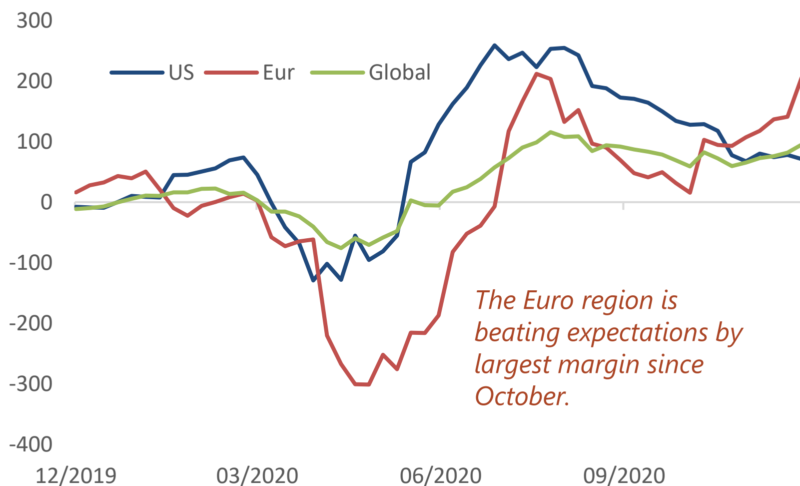


Source: Goldman Sachs

Consensus growth for 2021 is running at just over 5%. We think there is significant scope for the economy to grow at a faster rate than expectations. Consumption has been curtailed in 2020 and should show a sharp rebound in the second half of 2021. Pent up demand, improving employment, combined with continued fiscal and monetary stimulus is a powerful recipe for upside surprises. Travel and entertainment is almost certain to show sharp gains from a very low base and is likely to rebound once enough people are vaccinated.

The relative pessimism among economists can be seen through the Citi Economic surprise index, which measures reported economic indicators vs expectations. Since the recovery began in the US during June economists have underestimated growth. Currently all regions are surprises to the upside, but the eurozone has been beating expectations by the largest amount since October.

Citi Economic Surprise Index



Source: Bloomberg, IMF, Plurimi Wealth LLP

The path of consumer spending will be the key to the shape of the economic recovery. Initial improvements driven by a relaxation of social distancing measures and policy support are already clear. Thereafter improvements in the employment trend, and confidence that excess savings will not be required for future economic setbacks will be required to push consumer spending higher. The U.S. savings rate was 32% in April and has fallen to a still above normal 13%. Savings can be viewed as healthy but it is also a sign of low confidence. A significant risk to consider is if savings do not unleash pent-up demand for goods and services, it will stifle the biggest engine of the U.S. economy.

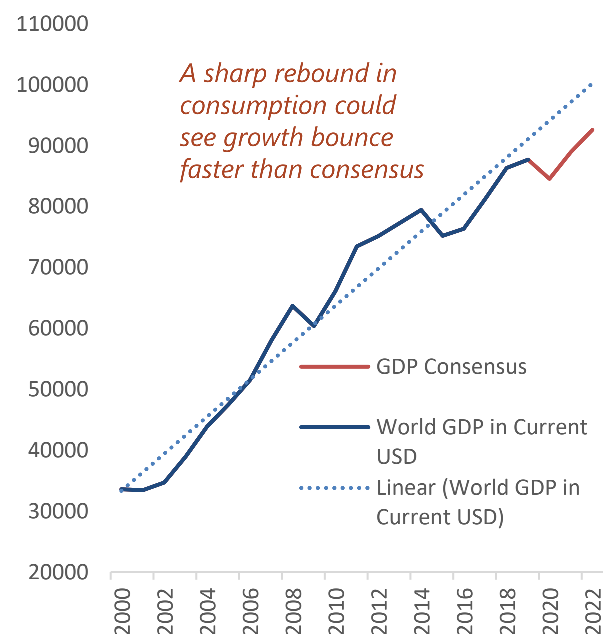
Consensus Global GDP Growth

	2019	2020e	2021	2022
World	3.1	-3.9	5.2	4.1
Developed	2.0	-4.9	4.8	3.9
Emerging	4.3	-1.1	7.2	6.0
US	2.2	-3.6	4.1	3.2
Euro	1.3	-7.4	4.7	3.6
UK	1.3	-11.2	5.5	4.6
China	6.1	2.0	8.2	5.5

Source: Bloomberg, OECD, Plurimi Wealth LL

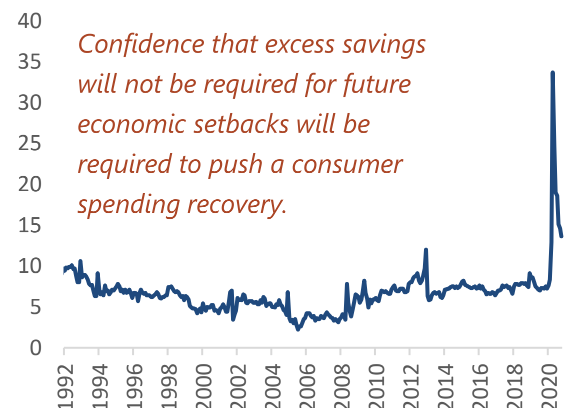
Although risks remain, we think there is upside to consensus forecasts.

Global GDP (USD $2019 $billions)



Source: Bloomberg, IMF, Plurimi Wealth LL

US Savings rates (% of disposable income)

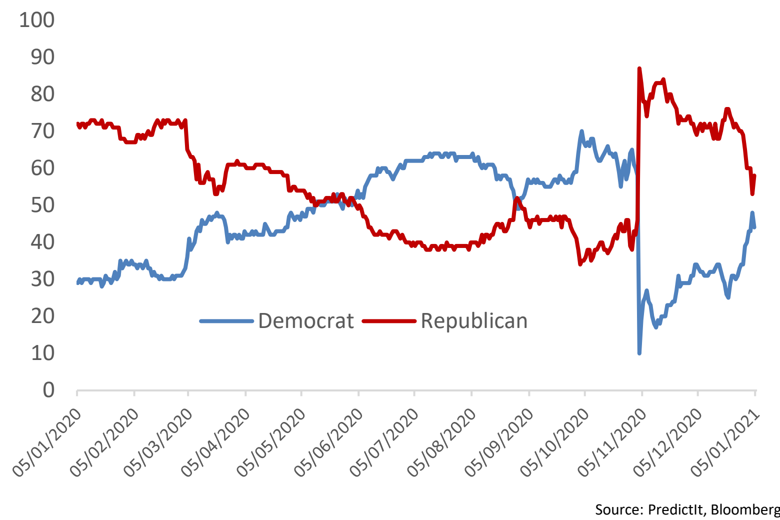


Source: Bloomberg, IMF, Plurimi Wealth LL

United States

The US has ended 2020 with very weak retail sales and jobs numbers. With a virus relief bill finally being approved at year end, the economy should receive some vital support which will put a floor under economic activity. Unfortunately the delay in stimulus together with the resurgence of the virus means that the economy faces a troubled winter. Consumers have already turned cautious, reining in spending in November, and the Christmas shopping season is looking anything but joyous. The bright spots amidst the dreary backdrop is the housing market and the start of immunizations, which sets the stage for a rebound over the second half of next year. The $900 billion (4% of GDP) relief package will result in higher disposable income and more could happen based on the outcome of the Senate runoffs in Georgia on January 5. Betting markets are showing a 40% probability of Democrats taking control of the Senate.

Prediction Markets of Senate Control



Source: PredictIt, Bloomberg

A surprise Democratic sweep of Georgia run-offs would add significant stimulus and new debt, and also likely mean higher taxes.

Eurozone

Europe's economy has suffered more than the US in 2020 due to stiffer lockdowns, but it may now be through the worst. The infection surge of early Q4 has slowed. November PMIs confirm the clear-divide between a more resilient export-oriented manufacturing sector and sluggish services. While the services PMI (up to 47.3 from 41.7) remained well below its historical average, the manufacturing PMI (up to 55.5 from 53.2) signalled an acceleration in activity. Notably, the German manufacturing sector, which strongly relies on global demand, continued to post markedly better numbers than the eurozone average. We expect Europe will see significant growth in 2021 driven by German manufacturing and the re-opening of services in the Southern countries. Europe agreed significant recovery stimulus in the summer and that money has yet to be put to work. Fiscal support with continued monetary stimulus should drive growth of more than 4% in 2021. The eurozone has seen its current account move higher during the year, and the resulting euro strength may pose a risk to the hoped for reflation.

Source: Pantheon

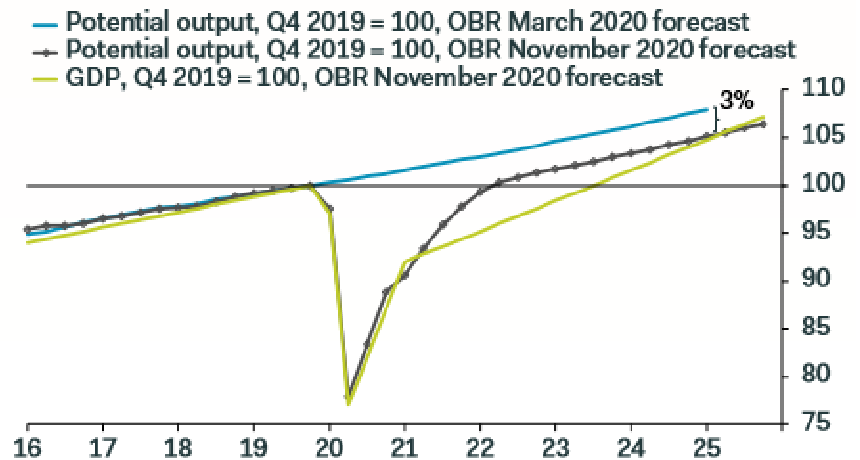
The eurozone has seen its current account move higher during the year, and the resulting euro strength may pose a risk for the hoped for reflation.

United Kingdom

We expect a particularly weak first quarter in the UK. New lockdowns which require hospitality, accommodation and leisure venues to close and the closure of non-essential shops in now cover all of England's population. Christmas celebrations likely boosted transmission of the virus everywhere. The Brexit trade deal was signed off just before Christmas. The agreement settles less than we expected and sets the stage for an endless process of further negotiation. The extension of the furlough scheme until the end of April may reduce job losses, but business surveys point to job losses over Q1 2021. After a likely dire Q1, the second quarter should be a turning point for the economy. The U.K. has already begun a roll out of Pfizer's and AstraZeneca's Covid-19 vaccines.

Thr UK may transition from massive stimulus in 2020 to tax hikes in 2022, as the next general election is due to be held in May 2024 and no Chancellor wants to hit voters' wallets in the run-up to polling day.

OBR forecasts show 5-6 year path back to potential



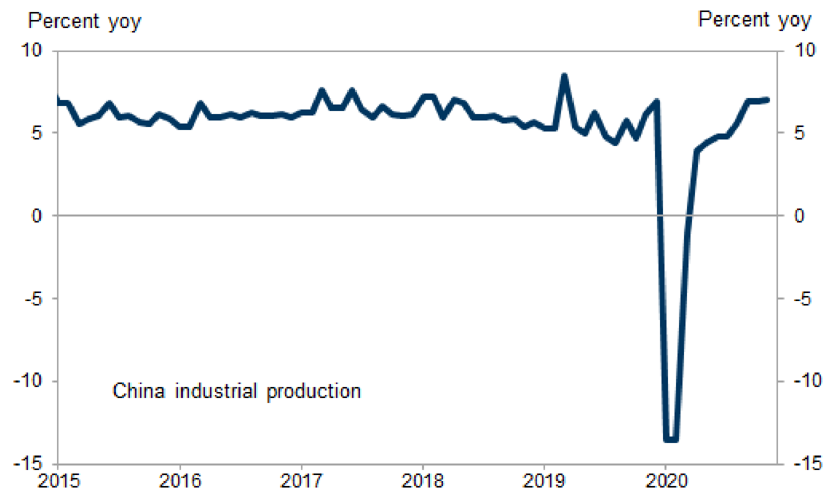
Source: Pantheon Economics

China

China has strong momentum heading into 2021. Manufacturing in China has rebounded to pre-Covid levels. We expect a continued acceleration in manufacturing activity to be driven by exports in 2021. The rest of the world will see strong growth in the second half of 2021 and it is possible a Biden administration moves away from some of Trump's protectionist policies. Strong exports help GDP and drive manufacturing employment. Construction activity has been driven by significant government stimulus. We expect this stimulus to slow during the year but the economy should be in strong enough position for this to happen without risking growth.

2021 is the first year of the Five-Year Plan. We expect measures which boost consumption and focus on aiding technological advancements. China ambitiously aims to double real GDP by 2035.

Chinese Industrial production



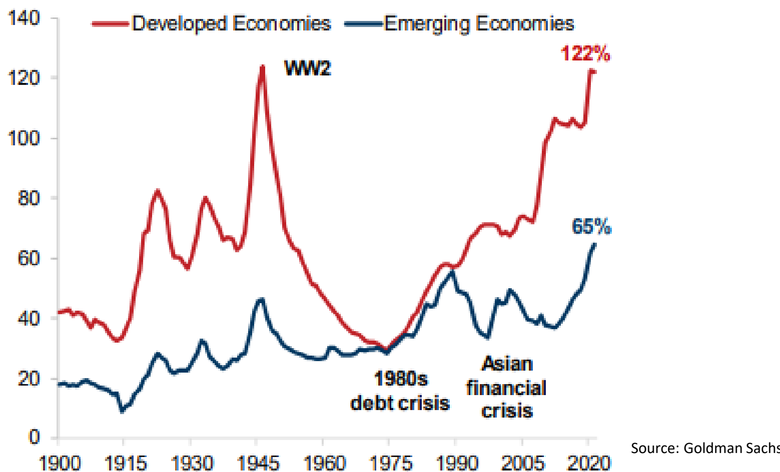
Source: Goldman Sachs

Sovereign Debt and Deficits

The most notable damage from the pandemic is rising government debt. 2020 saw developed global sovereign debt balloon to levels not seen since the end of World War II. Any announcement of stimulus saw markets rally during 2020. At some point the debt will matter to markets and the economy, but it may not be in 2021. We are not questioning if the debt is needed. The benefit of running large deficits is likely to far outweigh any eventual costs. The massive deficits seem necessary and are a much better alternative to a wave of personal and corporate bankruptcies, and a possible economic depression. However, the route governments take to deal with their growing debt is probably the most important question for investors in the long term.

Will debt be repaid through future austerity and taxes, with government surpluses? Will there be sovereign defaults? Will debt be monetised, or will perpetual negative real rates be the answer to manage and reward high debt levels. The path to deal with debt will determine if it will be deflationary or inflationary in the long term.

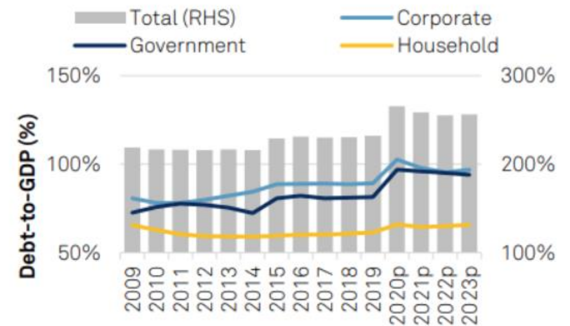
Median debt-to-GDP (%) IMF and Goldman Sachs



Source: Goldman Sachs

The path back to debt sustainability that was achieved in the 30 years following WWII may not be achievable this time. The post war euphoria and infrastructure build led to nominal GDP growing by 8.8% per annum (2.3% real and 6.5% inflation) in the decade after the war. The growth rate of nominal GDP was much higher than the 5% per cent average effective interest rate paid by the government on public debt. Generating nominal economic growth is the key to reducing debt to GDP ratios. Real growth given demographics has been difficult. The pandemic has not created the need to rebuild infrastructure like the war did. The inflation component of nominal growth, while supressing interest rates is the likely the path of least resistance. Populism has proved to be a winning political strategy, and helicopter money is the most populist policy there is. While interest rates are anchored near zero the sustainability of debt will likely be ignored by markets but should yields start to rise the debt may become the driver of markets and growth.

Global Debt

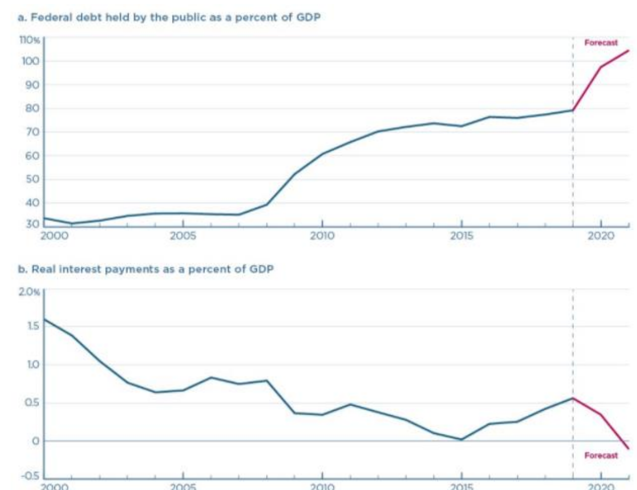


Source: S&P

S&P Global Ratings projects global outstanding debt, including that of governments, corporates and households, reached a record 265% of gross domestic product by year-end 2020, before levelling off in the coming years. The ratings firm estimates global outstanding debt will rise 10% to $200 trillion in 2020. A global debt crisis in the near term will likely be averted assuming that economies and private-sector demand recover, though that pick-up is predicated on wide availability of a Covid-19 vaccine by mid-2021 and easy monetary policy continuing.

Governments will eventually come under pressure to reduce deficits when markets question sustainability and bond yields rise meaningfully. Fiscal austerity and tighter monetary policy are not going to be considered in 2021.

Debt and cost to service it tell different stories.



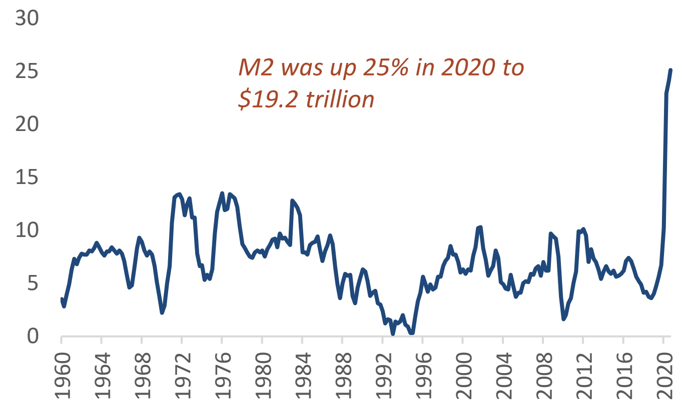
Source: Bloomberg

Central Banks **Unanimity on continued stimulus in 2021**

Central banks have unleashed a dizzying number of unconventional steps to cushion the economy from the impact of the coronavirus. The Fed's response to the virus has been robust and ongoing. Zero rates, corporate bond buying, and a promise to do whatever is necessary to ensure "smooth" functioning of markets has soothed markets. The Fed's QE program has purchased almost two thirds of government debt issuance since February. The ECB is doing whatever it takes and more is coming. The ECB is providing unlimited liquidity to the banking system, at negative rates, and expanded its balance sheet to almost €6 trillion by the end of 2020.

While interest rates are near zero or below at all the major central banks there is still likely more stimulus to come in 2021. For the year we expect the Fed remains on hold with a stable fed funds rate of 0-25 bp but we expect the Fed will increase the weighted average maturity of its Treasury purchases. In December it indicated it would make purchases of $80B per month Treasuries and $40B mortgages "until substantial further progress has been made toward the Committee's maximum employment and price stability goals". The yield curve should steepen modestly during the year but should 10 year yields rise to a level which threatens the Fed's reflation goals explicit yield curve control will become a more likely option.

US M2 ($19,226 billion)

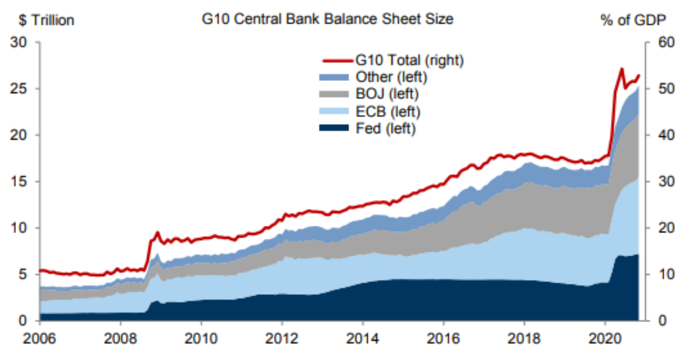


Source: Bloomberg, Plurimi Wealth LLP

Powell "the risk over overdoing it is less than the risk of underdoing it"

We expect central banks to continue to pursue aggressive policy even after the economy stabilises. Central banks do not intend to permanently to monetize the increase in the public debt required to fund the Covid-19 relief efforts, but they are now much more than the lender of last resort. When central banks buy securities from non-bank entities, they directly boost the money supply. The chart to the right shows this massive increase in money supply. Central banks have also shown a keen eagerness to boost liquidity at moments the stock market shows any weakness. The monumental surge in liquidity won't reverse anytime soon, and central banks will continue to pump up assets prices, as much as they provide stability to the monetary system. As of Nov. 30, the collective balance sheet assets of the Fed, ECB, BoJ and the BoE stood at 54.3% of their countries' total GDP, up from about 36% at the end of 2019.

G4 CB balance sheet (% GDP)

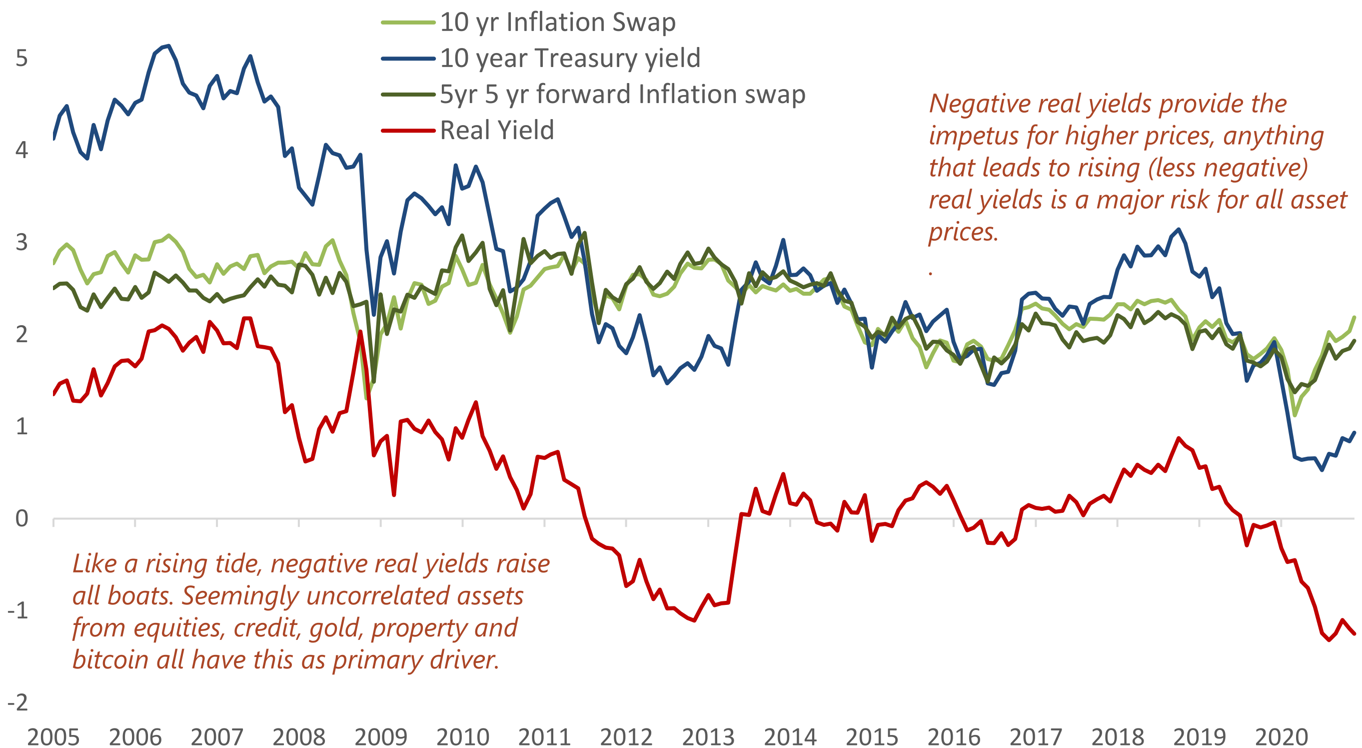


Source: Goldman Sachs

In December the ECB announced additional easing via an extension of the pandemic QE programme (PEPP) and its targeted longer-term refinancing operations (TLTRO). They also updated their growth forecast for 2022 to 4.2%, and lowered the inflation projections to 1.4% by 2023. This seems to indicated that ECB may need to do more if it expects to achieve its inflation targets. We expect the BoE will try to keep their base rate from falling below zero but they have indicated that it is an option they will consider if needed.

Liquidity has been far more important than valuations in 2020, and we expect that continues to be the case in 2021. Growth remains scarce and assets which provide it will continue to demand premium multiples. We have a positive outlook for the global economy and corporate earnings. While economies recover but remain below their potential an extended period of low inflation, low-interest rates favour equities over bonds. Lofty valuations and generally bullish consensus create longer-term trepidations, but vaccines are being distributed, a Brexit deal has been done and policy will be supportive for all of 2021. We are positive on risk assets as we begin the new year.

Most important chart for 2021: Treasury yield and Inflation swaps



Source: PW

As 2020 began inflation swaps and 10 year Treasury yields all were priced at 1.9%. All moved lower during the March lock downs, but inflation swaps started to move higher on fiscal stimulus and aggressive central bank policy while 10 year yields stayed lower as central bank buying and anticipated new easing measures put a lid on treasury yields. Negative real yields are the fuel for almost all risk assets. Central bank policy is designed to punish cash which stays on the side-lines and seemingly diverse assets such a gold, credit, equities, property all are driven by the same forces. While negative real yields provide the impetus for higher prices, anything which changes this dynamic is a major risk for all asset prices. A slow down in growth expectations or central banks letting 10 year yields rise are the two most obvious risks.

Political uncertainty has been an overhang on markets throughout much of 2020, and should be less of an issues in 2021. Fiscal stimulus continues and central banks have committed to keeping the liquidity taps open and interest rates low for a long time. The main concern is that valuation already factors in plenty of good news and investor sentiment is very optimistic. This means markets are vulnerable if the improvements listed above turn out to be in doubt, especially the assumption about effective vaccines. However, our base case is that they do work and that extremely low real yields will sustain high valuations at least in the first year of an earnings rebound.

Asset Allocation

Our tactical asset allocation is based on a vaccine underpinning a strong economic rebound in 2021, and continued monetary and fiscal support. Offsetting the expected economic growth are extreme valuations.

Equities: Neutral
Underweight US, Overweight World ex-US

Fixed Income: Underweight
Underweight Government bonds, Neutral on credit

Commodities: Overweight
Own precious metals, and sell put options on cyclical commodities

Alternatives: Overweight
Private Equity, infrastructure, dividend futures and structured notes on thematic investments

	-		Neutral		+
Equity			■		
US		■			
Japan					■
UK			■		
Europe				■	
Emerging				■	
Fixed Income		■			
Government	■				
Credit			■		
EM			■		
Inflation protected			■		
Commodities				■	
Precious Metals				■	
Energy				■	
Agricultural			■		
Industrial Metals				■	
Alternative				■	
Private Equity				■	
Dividend Futures				■	
Long Short Equity Funds				■	
IPO funds				■	

Risks to outlook:

1) **Vaccine risks :** Regulatory approvals, manufacturing & distribution logistics, and willingness of population to be vaccinated are all assumed in our base case but are not ensured. Mutations of the virus may also impact efficacy.
2) **Diminishing Monetary Stimulus:** We have assumed continued monetary and fiscal policy will push assets higher. With guidance to date we have a high confidence this will be the case, but given its importance to our thesis this is a risk which must be considered.
3) **Regulation, taxation:** Both the US and China have taken anti-trust measures against their large cap tech and consumer companies in recent months. We do not expect this will change the business models significantly but a correction could loom if regulatory pressures increase.
4) **Inflation leads to a steeper yield curve**. With all asset beings driven higher by negative real yields, a move to positive real yields leads to lower valuations across the board.

Equities

World (Neutral)

MSCI WORLD	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	33.27	98	21.19	20.07
BEst P/E Ratio	21.47	92	16.15	15.84
Long Term Price Earnings Ratio	26.47	81	22.16	21.83
Price to Book Ratio	2.96	88	2.39	2.35
Price/EBITDA	14.05	100	7.82	7.38
Price to Sales Ratio	2.20	100	1.33	1.32
Enterprise Value/EBITDA	16.80	100	10.78	10.68
Profit Margin	5.84	39	6.19	6.52
Operating Margin	9.04	20	10.40	10.36
Dividend Yield	1.81	18	2.25	2.25
10Y Yield	0.92	3	3.79	3.83

Source: Bloomberg. Jan 1995 to Dec. 2020

Following the significant rally in 2020 global equities are back to record multiples on most measures. The rise in equity markets amid a weaker earnings has resulted in multiples which will dampen the long-term potential return from equities. The fall in 10Y UST yields has more than offset the negative impact of a rising equity market and weaker earnings trajectory. The best thing about equities is bonds. While equities trade at 94th percentile on average, compared to very low treasury yields, equities still offer a significant risk premium of 5.3%. The low and anchored bond yields during the recovery is atypical and has pushed yield investors into equities. Equities should be able to digest gradual increases in bond yields better than fixed income provided they come alongside better growth.

Key inputs for Global ERP

Risk premium	5.3%	Consensus growth ’21	27.3%
Normal	4.1%	Consensus growth ’22	15.0%
Min	1.6%	Medium-term growth	5.7%
Max	7.5%	Long-term growth	3.4%
10 year bond	1.0%	Pay-out ratio	40%
IRR	6.3%		

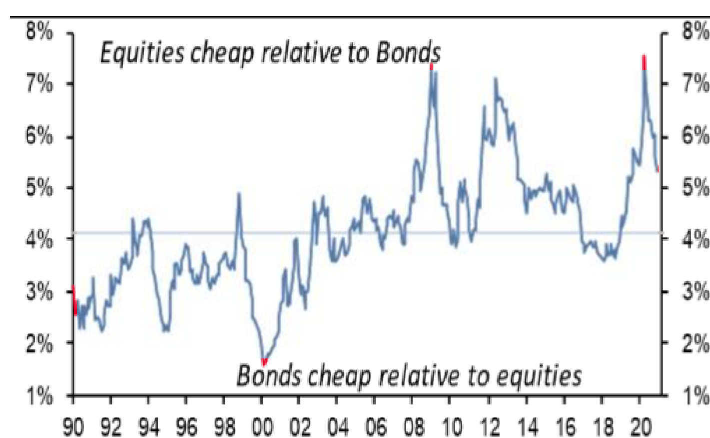
Factors favouring equities

- Stimulus measures have been coordinated across countries and combine a significant monetary and fiscal impetus for the economy.
- In absolute terms and especially relative to bonds equities are now cheap enough that outsized returns will be achieved for long term investors.
- As the economy rebounds strong earnings growth will be delivered.

Factors working against equities

- Optimism on re-opening and strong economic news is expected.
- Broad market is back to near peak valuations.
- Significant output gaps will remain and will curtail economic growth and profits.
- Potential regulation headwinds to large cap US and Chinese technology.
- Potentially rising bond yields, or any change of tone from central banks.

Global equity risk premium



Source: Bloomberg, SocGen, Plurimi Wealth LLP

Equities

World Styles and themes

The announcement of several successful COVID-19 vaccines in November has led to a market rotation away from growth stocks towards more cyclical value stocks. Technology stocks saw higher revenues as consumers worked from home, made technology purchases to facilitate this, and spent online. The fall in bond yields and real yields was just as important. Long-duration technology stocks benefitted from zero interest rates which meant future earnings are just as valuable as current earnings. A strong economic recovery may see a continued rotation away from technology stocks but while interest rates are low their growth remains attractive and will justify premium multiples. We expect growth will determine the style winner in 2021 and a strong cyclical backdrop could lead to value growing faster than 'growth'. The equities most at risk of a correction are the unprofitable stay-at home technology stocks, as they do not have earnings which underpin their elevated valuations.

A strong recovery and steepening of the yield curve would entrench a value rotation, but we are not sure central banks are ready to let that happen. Any unexpected headwinds to the recovery will favour growth stocks. A sustained value rotation based on the post-vaccine recovery should help the more cyclical European and Asian markets vs the tech heavy US. While US value is cheaper than growth, it is at record multiples vs. its own history.

We expect a thematic approach to equity investing is appropriate at this stage of the market cycle. Sectors with clear regulatory tail winds, or benefitting from new technologies vs. incumbents with broken business models are positioned to deliver outsized growth as the recovery matures. Clean energy, fintech and 5G are three themes we have recommended in 2020 and continue to favour in 2021.

US Value vs Growth

RUSSELL 1000 VALUE INDEX	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	24.70	99	16.99	16.58
BEst P/E Ratio	23.28	100	15.23	14.77
Long Term Price Earnings Ratio	21.06	84	17.22	17.09
Price to Book Ratio	2.41	81	2.06	2.04
Price/EBITDA	12.04	100	6.23	5.61
Price to Sales Ratio	1.91	100	1.27	1.25
Enterprise Value/EBITDA	15.49	100	10.09	10.09
Profit Margin	5.10	18	6.33	6.95
Operating Margin	7.87	5	11.09	11.28
Dividend Yield	2.25	24	2.51	2.43

RUSSELL 1000 GROWTH INDX	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	42.23	95	24.86	22.35
BEst P/E Ratio	35.23	97	20.64	19.54
Long Term Price Earnings Ratio	60.48	96	34.17	31.39
Price to Book Ratio	12.35	100	5.30	4.63
Price/EBITDA	25.16	99	11.95	10.87
Price to Sales Ratio	5.01	99	2.29	2.07
Enterprise Value/EBITDA	26.31	98	13.68	12.74
Profit Margin	11.53	94	8.28	8.54
Operating Margin	14.43	82	13.44	13.31
Dividend Yield	0.81	14	1.21	1.21

Source: Bloomberg. Jan 1995 to Dec. 2020

Favoured Investment themes:

Clean Energy technology: Clean tech has a major role to play in the economic recovery and fiscal spending and regulatory tail winds should spur lasting growth in this sector. Shareholders emphasis on 'ethical and green' also support share prices.

Fintech: Mobile payments, e-commerce, and infrastructure for crypto currencies are all growing rapidly. The traditional banking model is unprofitable without interest rate margin and disruptive financial technology companies are taking market share.

5-G infrastructure and business beneficiaries: Companies providing infrastructure for the 5G rollout, new smart phones and busines models based on rapid connectivity all are positioned to deliver outsized growth on the back of 5G high speeds and low latency.

We offer a range of actively managed strategies on these themes. Constituents of these baskets can also make attractive components in structured notes. Your RM will have the updated baskets.

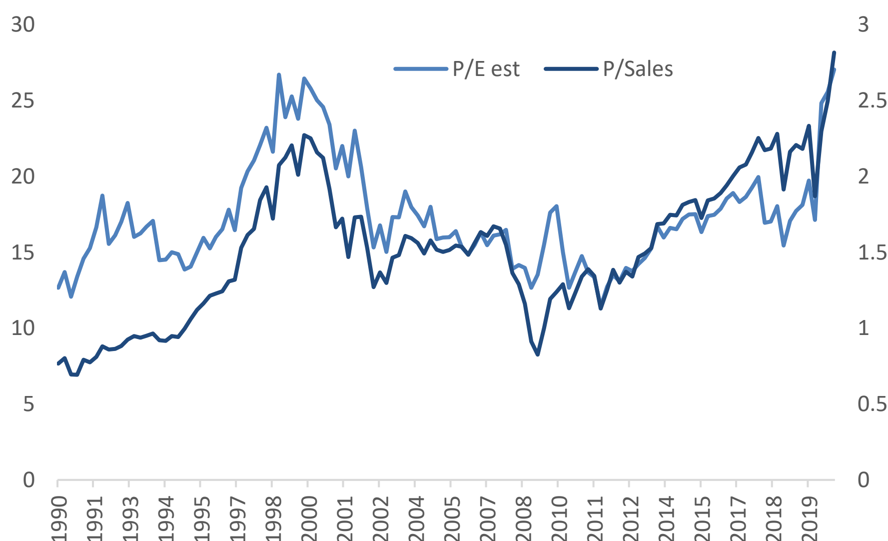
Equities US (Underweight)

S&P 500	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	29.91	100	19.83	18.83
BEst P/E Ratio	27.04	100	17.19	16.56
Long Term Price Earnings Ratio	31.42	90	22.54	21.48
Price to Book Ratio	4.17	92	2.90	2.78
Price/EBITDA	16.35	100	7.99	7.47
Price to Sales Ratio	2.82	100	1.52	1.52
Enterprise Value/EBITDA	18.67	100	10.77	10.80
Profit Margin	7.55	54	6.80	7.37
Operating Margin	10.26	23	11.71	12.17
Dividend Yield	1.57	15	2.08	1.97
10Y Yield	0.92	2	4.35	4.30

Source: Bloomberg. Jan 1995 to December 2020

US equities trade at elevated multiples vs. the rest of the world, and it also remains expensive vs. its own history. Offsetting valuation is the weighting towards world leading companies in sectors which have delivered strong growth regardless of the economic backdrop. Technology, Healthcare, Communication services, and Staples which make up more than half of the S&P 500. Energy, materials and industrials make up a little over 10%. With real GDP growth in excess of 5% forecast for 2021, we do not think investors need to avoid cyclicals, and this should favour the world–ex US. Factors supporting the bullish view are the Fed continues to maintain an ultra-accommodative policy stance and stimulus cheques seem to make their way into the stock market. The Fed's focus on generating an inflation overshoot leaves plenty of space for the economy to rebound and asset prices being inflated further.

After their strong resilience to the economic shock this year and outperformance, we expect new tech stocks to lose some of their lustre as cyclical stocks start to deliver growth. The mega-cap profitable stocks should outperform, as their dominant market position allows them to extract profits. This biggest risk to this thesis in increased regulation and anti-trust action.



Source: Plurimi Wealth LLP, Bloomberg

We own: *Apple, Activision, Corteva, Ebay, Estee Lauder, Humana, Mckesson, Skyworks*

We short: *Digital Realty, State Street, Zoom Communications, Kinder Morgan, RingCentral, Welltower*

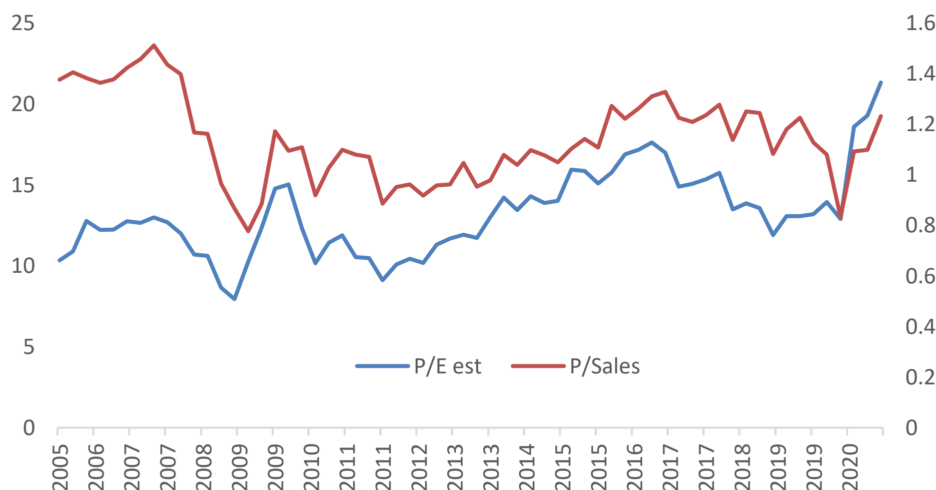
Equities **UK (Neutral)**

FTSE 100	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	174.65	98	29.39	17.73
BEst P/E Ratio	21.31	99	13.10	12.77
Long Term Price Earnings Ratio	15.68	54	16.18	14.84
Price to Book Ratio	1.67	17	1.92	1.87
Price/EBITDA	8.81	88	7.44	7.31
Price to Sales Ratio	1.23	63	1.17	1.17
Enterprise Value/EBITDA	12.07	96	9.19	8.90
Profit Margin	0.84	0	6.66	6.90
Operating Margin	4.27	1	10.21	9.86
Dividend Yield	3.28	23	3.84	3.81
10Y Yield	0.19	1	2.92	2.85

Source: Bloomberg. Jan 1995 to Dec 2020

The FTSE 100 has been the worst-performing regional index in 2020. UK equities are cheap vs. the world, but not vs their history. A 3.3% dividend yield is attractive, but the energy and financials weighting makes it questionable. Sector exposure which is weighted towards sectors that have been hit the hardest during the pandemic; Energy, Banks and materials, make up almost 40%. A rotation towards these cyclical sectors could drive off a catch-up rally but The UK has issues beyond the global economy. COVID and Brexit uncertainty have battered the UK in 2020, and neither are completely resolved yet. The vaccines and the Brexit deal pave the path to a solution, but the economy still is hurt from their fallout. Longer-term, the non-tariff barriers on trade in services, are a likely to be drag on growth. The Bank of England is likely to keep rates on hold during the recovery phase and the government will be keen to push pro-growth policies to show the positive impact from its new independence.

FTSE 100 (P/E and P/Sales)



Source: Plurimi , Bloomberg

We own: *AstraZeneca, Ashtead, Plus500*

We short: *BP, Compass Group, Ocado*

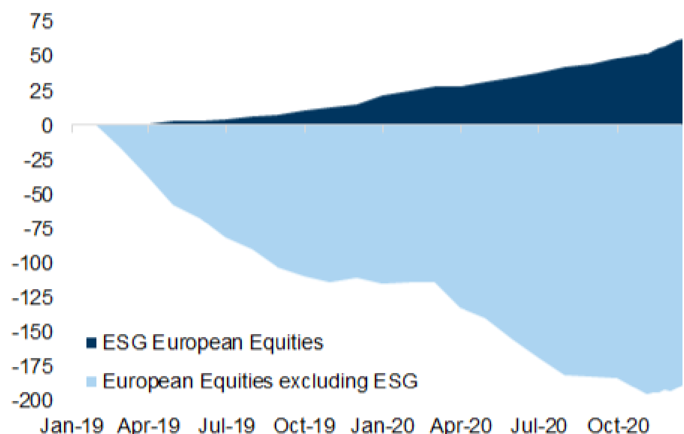
Equities **Europe (Overweight)**

Stoxx 600	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	51.42	93	23.10	19.19
BEst P/E Ratio	23.70	99	13.89	13.73
Long Term Price Earnings Ratio	20.36	76	17.72	17.78
Price to Book Ratio	1.96	71	1.85	1.82
Price/EBITDA	10.07	100	6.66	6.36
Price to Sales Ratio	1.40	99	1.09	1.11
Enterprise Value/EBITDA	14.30	100	9.28	9.34
Profit Margin	3.15	13	6.08	6.23
Operating Margin	6.78	2	9.99	9.48
Dividend Yield	2.34	1	3.37	3.38
10Y Yield	-0.57	2	2.20	2.28

Source: Bloomberg. Jan 1995 to December 2020

The new lockdowns are working in Europe but they remain a larger economic headwind in Europe than in most parts of the world. We expect Europe is poised for a strong post-vaccine recovery. Europe is more exposed to global trade than the U.S. and we view that is a positive. It has just signed an investment deal with China and will be a beneficiary of growing Chinese demand. We expect European equities should outperform in 2021 based on a rebound in global trade, and reasonable valuations. Should the bond curve ever steepen, European banks will offer attractive value. The expected EU approval of the recovery fund and the green deal in Q1 should also boost stock prices. Europe has significant exposure to ESG stocks and this segment of the market has seen the most inflows. Apart from the same risks facing the world, Europe's political risks, debt sustainability and regional differences are always lurking in the background.

Global ESG flows to Europe equities growing steadily, while all others are seeing outflows



Source: Goldman Sachs

We own: *Cap Gemini, Novo Nordisk, Neste, Roche, Vestas, UBS, Worldline.*

We short: *Airbus, Fortem, Deutsche Wohnen, EQT.*

Equities — Japan (Overweight)

Topix	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	31.48	66	56.99	21.96
BEst P/E Ratio	23.33	85	20.16	15.79
Long Term Price Earnings Ratio	21.03	39	27.63	23.51
Price to Book Ratio	1.28	38	1.56	1.43
Price/EBITDA	8.54	81	7.04	6.23
Price to Sales Ratio	0.88	89	0.70	0.70
Enterprise Value/EBITDA	11.25	72	10.58	9.68
Profit Margin	2.88	52	2.31	2.67
Operating Margin	5.27	44	5.33	5.57
Dividend Yield	2.04	78	1.46	1.18
10Y Yield	0.02	9	1.38	1.31

Source: Bloomberg. Jan 1995 to Sep 2019

The Nikkei was the strongest performing major regional market in 2020. It is geared to a growth recovery, but also has a significant technology exposure. With fiscal policy expanding, and monetary policy continuing we expect investors will continue to buy Japanese equities. The country also has an ambitious reform agenda, and plans equity friendly deregulations. The Japanese government has unveiled a "green growth strategy" aiming for the country to reduce greenhouse gas emissions effectively to zero by 2050. Consensus expects 6.8% earnings growth for the country in fiscal 2021, we think there is upside potential to that. At 1.3x book value it trades below all of the other major markets.

Topix P/B

Source: Plurimi Wealth LLP, Bloomberg

We own: *NTT, Shin-Etsu, Keyence, Tokyo Electron, KDDI.*

We short: *GMO Payment, Toshiba, Kansai Electric*

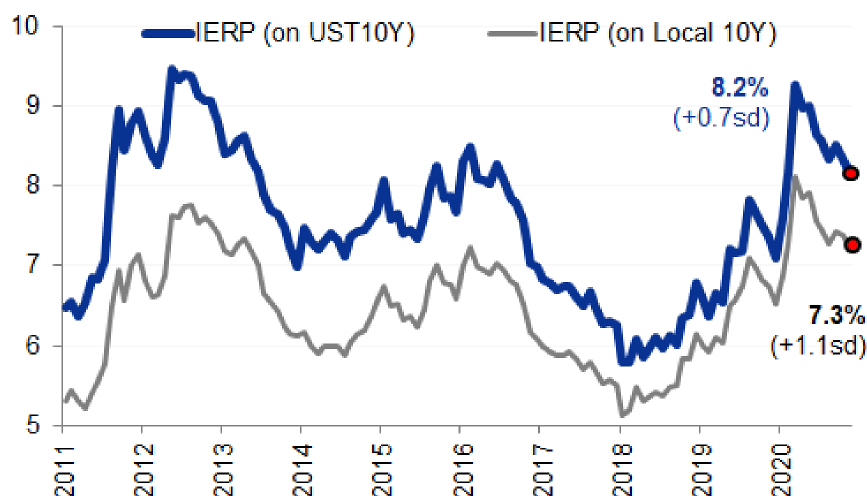
Equities **Asia (Overweight)**

Asia ex-Japan	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	26.55	100	12.88	12.35
BEst P/E Ratio	18.99	97	12.41	11.97
Long Term Price Earnings Ratio	25.03	99	16.83	16.47
Price to Book Ratio	2.58	100	1.65	1.58
Price/EBITDA	16.27	100	6.94	6.28
Price to Sales Ratio	3.14	100	1.55	1.52
Enterprise Value/EBITDA	16.99	100	8.10	7.33
Profit Margin	12.52	44	12.60	12.76
Operating Margin	15.00	51	14.90	14.93
Dividend Yield	1.31	0	2.70	2.60
10Y Yield	0.92	6	2.37	2.38

Source: Bloomberg. Jan 1995 to Dec 2020

The MSCI Asia ex-Japan market outperformed the developed world in 2020. China's economic recovery is ahead of the West and has more successfully contained the virus. Following the strong performance, the region is at record highs, but we think the growth gap between emerging and developed markets justifies it. Compared to local and US treasury yields the region still offers a significant risk premium of 7.2% and 8.2% respectively. Stocks driven by China's domestic economy continue to offer outsized growth potential. Korea is another country which has contained the virus and offers a range of high growth companies.

Equity risk premium looks attractive relative to its history based on both US and local rates



Source: Goldman Sachs

We own: *Tencent, LG Corp, China Feihe, ENN Energy.*

We short: *Ping Insurance, Meituan*

Fixed Income **Underweight**

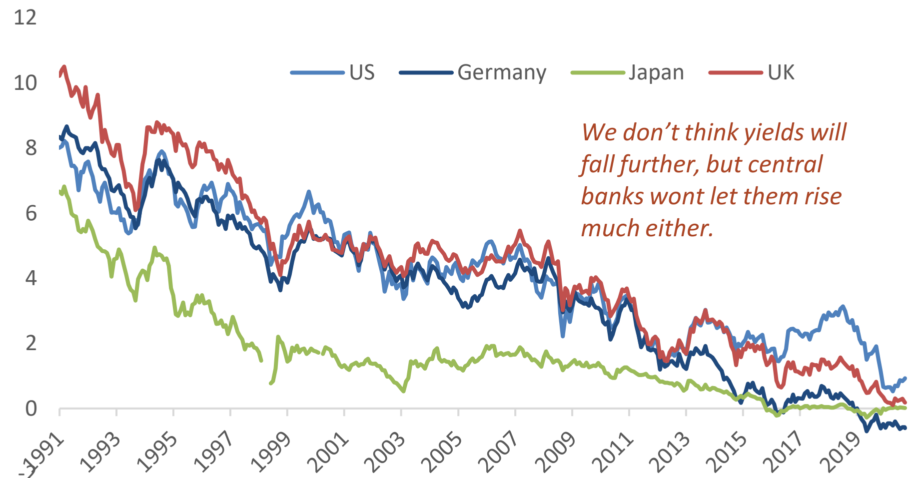
We are continuing to underweight G7 government bonds, based on the long-term valuation. Bond yields have fallen to levels that reflect permanently distorted monetary policy. This is a possible outcome, but we think that eventually, loose monetary policy will lead to higher long-term yields. Governments running massive deficits and record debt levels will eventually see debasement as their base case.

Central banks have been the bond market's best friend. This is likely to persist for years and will likely ensure that bond yields remain below our traditional "fair value" for some time. However, we think there is now risk that government bonds yields have moved so low that any pick-up in growth or hint of inflation will need very proactive communications from central banks to avoid a major selloff.

Bond yields can rise next year, but not by much. The global industrial cycle upswing will lift Treasury yields but the Fed will likely ensure that it doesn't go too far. The Federal Reserve's readiness to run the economy hot until after inflation actually materialises will put pressure on other central banks to do the same. We expect government bond yields to move gently higher moderated by central bank action which could include further balance sheet expansion and eventually yield curve control if required. We forecast modestly higher yields across most of the world, with Treasuries yielding 1.3%, Germany -0.4%, Japan 0.10% and UK 0.4% by year end.

US Inflation swaps have started to price in higher prices while bonds have not. Japan and Germany continue to show stagnant prices for year to come. While government bonds offer negative real yields, corporate bond spreads remain somewhat attractive, but the aggregate yield has fallen to record low levels.

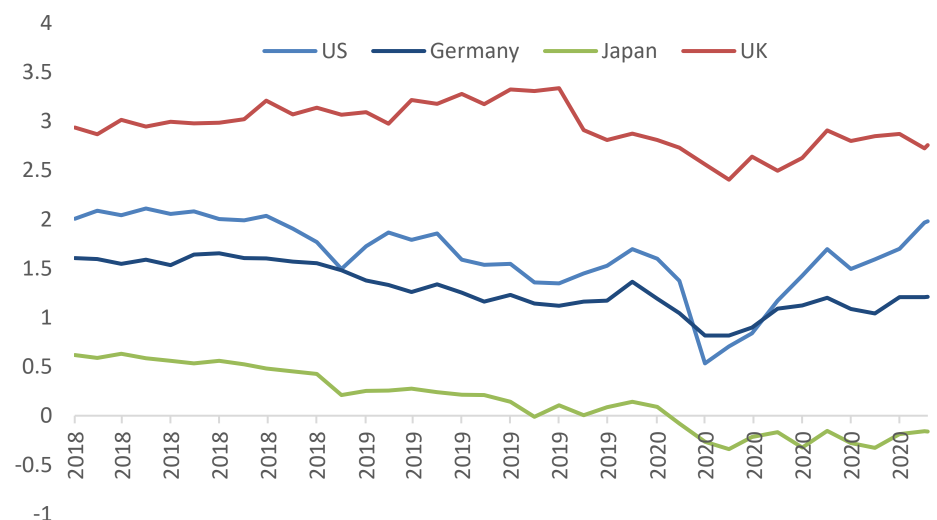
10 year sovereign bond yields



Source: PW Bloomberg

We expect some steepening with the economic recovery, but central banks will not let it go too far.

5 year inflation break evens

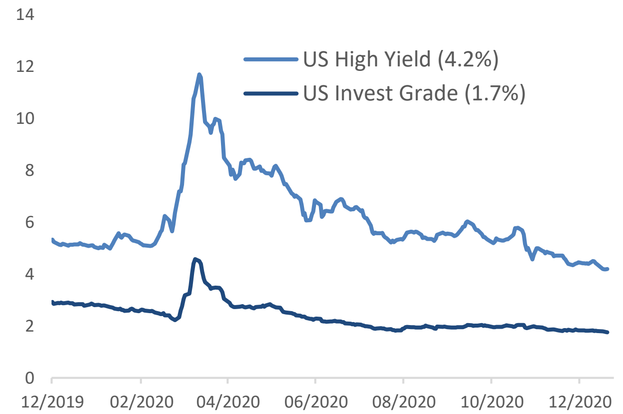


Source: PW Bloomberg

Credit markets sharply re-priced following the trillions in monetary and fiscal stimulus. The combination of liquidity and recovering oil prices has led to all credit spreads narrowing massively. US IG spreads have made the full round trip in 2020, starting below 1%, rising to over 3% at the end of Match, and are back to record lows. Commercial credit now has direct central bank support, which should put a floor not far below current prices. Central banks have acted swiftly and aggressively to ensure a liquid bond market and a functioning financial system. Asset flows into credit outpaced other asset classes in the summer, but investors have started to look for higher returns elsewhere as the year progresses. The Fed cannot create credit quality, but it will ensure liquidity in bank paper. The path of least resistance is further tightening in spreads.

Within credit European bank debt remains our preferred exposure. The banks are well capitalised and suspension of equity dividends and buybacks added to that capital buffer in 2020.

US High Yield, and Investment Grade Yield to worst

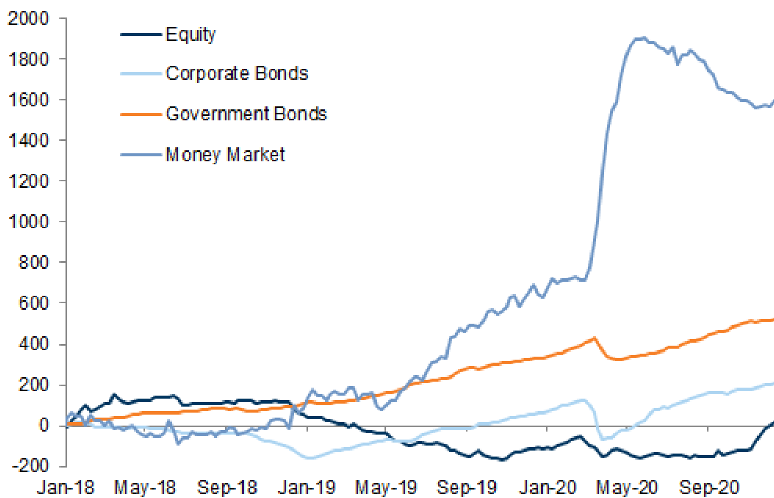


Source: Bloomberg, PW

With central banks effectively putting a backstop under investment grade debt, we think the risk premium remains somewhat attractive.

Yields are now at record lows in credit and will rely on further narrowing to generate meaningful returns.

Cumulative US fund flows by asset class ($ billion)



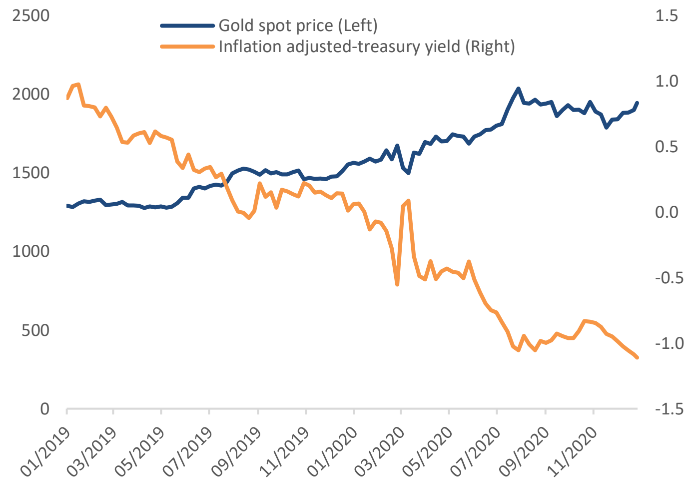
Source: Haver Analytics, Goldman

Commodities — Overweight

A weak USD and cyclical rebound set the stage for a broad based commodity rally in 2021. China's rebound in manufacturing and trade have been highly supportive to commodity prices in the second half of 2020 and should continue to drive demand in 2021. Structural under-investment in commodity exploration and production has meant that most commodities are now in deficit despite being early in the demand rebound. Apart from cocoa inventories were drawn down throughout 2020. Given that inventories are drawing this early in the cycle, a strong leg up for commodities in 2021 is expected. Crude will benefit from both supply-side discipline and a recovery in oil demand. We expect Brent prices at $55 by year end. OPEC will likely curtail supply in scenarios where oil prices fall below $45. The majority of OPEC members, including Saudi Arabia, opposed Russia's proposal for a February supply hike.

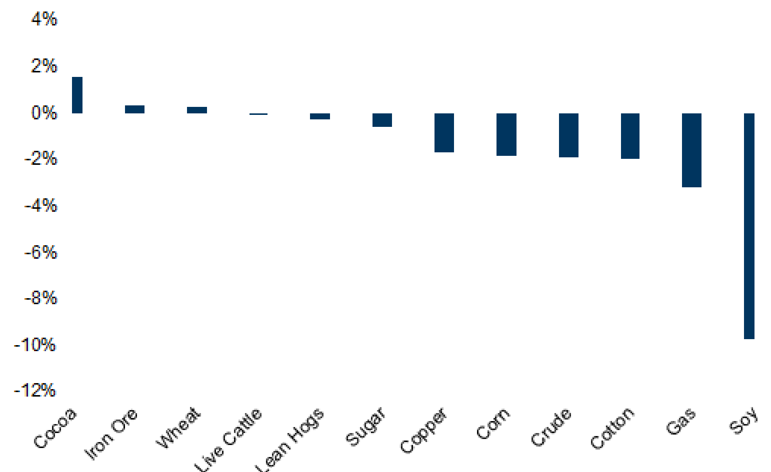
Gold will likely strengthen as global central banks maintain extremely accommodative conditions and global fiscal stimulus will remain plentiful. Negative real yields will continue to drive gold prices. Gold prices will be vulnerable in an economic expansion that reduces risk aversion and steepens the yield curve. The perfect scenario for gold is a deficit driven recovery where central banks limit bond yields. Iron ore and copper will benefit from infrastructure spending and copper additionally from electric vehicle demand.

Gold ($/oz) and real yields



Source: Bloomberg. PW

Yoy change in inventories as a % of US/global demand



Source: Goldman Sachs

Currency

The dollar remains overvalued and will likely weaken in our base case scenario of strong second half global growth. The country's twin deficits weight on the dollar and the Fed policy will remain easy. Our central scenario is for a gradually weaker U.S. dollar, more aggressive monetary measures, such as yield curve control would accelerate broad-based downward pressure on the dollar. We expect EM currencies to strengthen with the rebound in the global economy. The risk to our weak dollar view is in risk aversion scenarios where the dollar gets bid, but we prefer the euro and yen as cheaper safe-haven currencies in that scenario.

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