Q3 2020 Perspective

PLURIMI

Patrick Armstrong, Chief Investment Officer

1 July 2020

Q2 2020 saw some of the most shocking economic headlines ever; 20 million US jobs were lost in a month, oil prices went negative, the US tensions with China increased, 500,000 people have died, and 10 million people have tested positive for the corona virus. Of course during the quarter equities moved higher by 15%! Government bonds, gold, corporate bonds also all saw significant gains, and spot oil prices moved from negative to almost $40 a barrel by quarter end. All boats rising together is the defining characteristic of a liquidity fuelled rally.

Central banks have provided a robust and extraordinary response to the economic stop produced by the measures that were put in place to combat the covid virus. Money supply measures are growing at faster pace than ever before, and interest rates are zero or negative throughout the developed world. Central bank policy may not create economic growth but it will create asset price inflation and mute growing volatility pressures.

The growth in debt, not the virus is the most important long term impact from the first half of 2020. The surge in government deficits has the G7 on a path to reach 122% debt-to-gdp. Generating nominal economic growth is the key to reducing debt–to-gdp ratios. Creating real growth given a difficult demographic profile has been challenging. The pandemic has not created the need to rebuild infrastructure like World War II did. The inflation component of nominal growth, while supressing interest rates is the most probable path of least resistance for governments. Populism has proved to be a winning political strategy, and helicopter money is the most populist policy there is. We expect this to be the eventual end game, and investors should keep this in mind when making long term decisions.

Gold prices have a near perfect back drop, a rapid increase in money supply, a range of geopolitical risks.

Q2 2020 Review

All assets moved higher on back of massive monetary stimulus.

Asset Allocation Trades p.4

Japanese equities offer best value. China already showing an economic recovery. Quality and growth is more attractive than cyclical value. Defensive equities with yield in safe haven currencies. Structures with payoff in gold, rather than currency.

Global Economy p.5

Leading indicators and high frequency data show the beginning of a recovery. We expect a second half rebound based on containment of the virus, and proactive fiscal and monetary policy.

Debt p.10

G7 heading to 120% debt-gdp!

Central Banks p.11

Rates lowered to zero everywhere and open ended QE, which includes corporate bonds. Is the helicopter next?

Equities p.14

Equities expensive again on most measures but compared to bonds they offer much better return potential. We prefer quality over cyclical while rates are zero and output gaps remain.

Fixed Income p.20

Investment grade credit has the support of central banks, and is already pricing a significant downturn. Credit still offers moderately attractive spread.

Commodities p.22

Gold prices have a near perfect back drop, a rapid increase in money supply, a range of geopolitical risks, negative real yields, central banks eager to diversify from the USD. A technical break out is possible if prices move above $1800/oz.

2020 Headlines

Coronavirus could leave 30% of US workers jobless, Fed official

"All the News That's Fit to Print"

The New York Times

Late Edition

VOL. CLXIX ... No. 58,688 NEW YORK, SATURDAY, MAY 9, 2020 $3.00

U.S. UNEMPLOYMENT IS WORST SINCE DEPRESSION

GULF WAR 3 FEAR

Britain could be d

San Francisco Chronicle

Riots, shooting rock Oakland

The Washington Post

ston Sunday Globe

Los Angeles Times

Coronavirus cases hit 10 million worldwide

NATIONAL LOCKDOWN

Only allowed out once a day & £30 fine for breaking emergency rules

Gatherings of 3 or more banned and non-essential shops are to shut

PM: Many more will die and only drastic action can help the NHS cope

ice Force's Troubled History

April's Rate of 14.7% Touches All Parts

RECESSION LIKE 'WE HAVE NEVER SEEN'

FREE FALL

Virus deals record battering to economy

In Flynn Cas Russia Inqui Is Barr's Tar

US national debt reaches record $26 trillion

Biggest market fall since 2008 crash

WALL STREET JOURNAL.

TUESDAY, APRIL 21, 2020 - VOL. CCLXXV NO. 93 WSJ.com $4.00

Oil Takes Historic Dive Below $0

Global markets recoil as Trump threatens US-China trade war

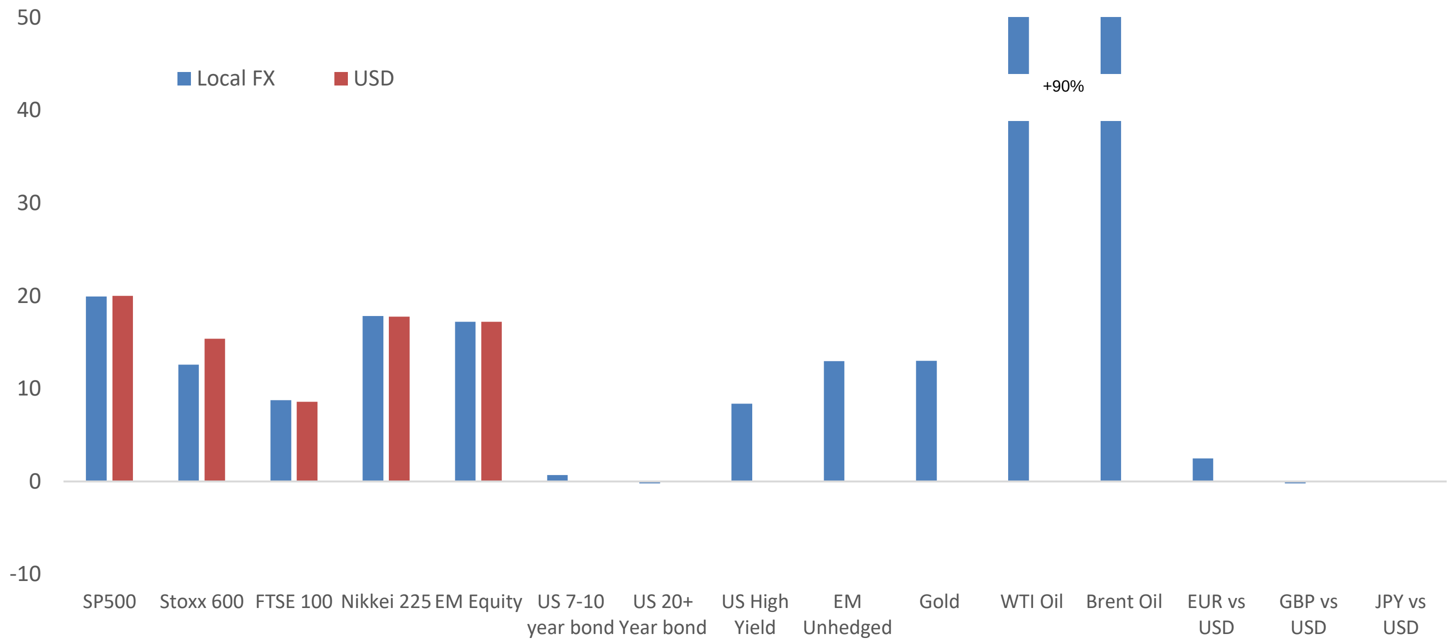
US president escalates attack on Beijing's handling of coronavirus pandemic

U.S. DEATHS NEAR 100,000,

Investors fear Italy is heading for 'junk' borrower status

Q2 2020

Performance by asset class (% USD)



Source: Bloomberg, PW

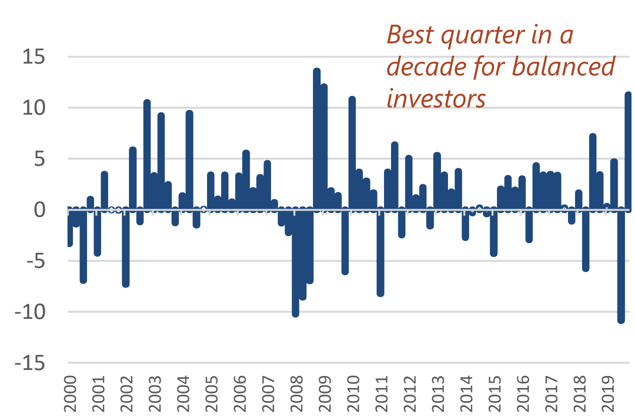
Q2 2020 produced some of the most shocking economic headlines ever; 20 million US jobs were lost in a month, oil prices went negative, the US tensions with China increased, and 500,000 people have died and 10 million people have tested positive for the corona virus. Of course during the quarter equities moved higher by 15%! Gold, corporate bonds also all saw significant gains, and spot oil prices moved from negative to almost $40 a barrel by quarter end. A rising tide lifts all boats, is the defining characteristic of a liquidity fuelled rally. Government bonds were roughly unchanged.

'A rising tide lifts all boats' is the defining characteristic of a liquidity fuelled rally.

An economy beginning to re-open combined with massive monetary and fiscal policy stimulus saw the S&P 500 rally by 20%, leading other regions yet again. Technology led the way as the Nasdaq Composite Index soared 31%, the most since 1999. European equities also moved significantly higher but lagged US equities. Gold traded near $1,800 an ounce to close the quarter up 13%. WTI oil had the most notable quarter, rising by 100% after briefly trading below $0 in April.

A balanced portfolio split between global equities and the global aggregate bond index would have risen by 11.4%, almost exactly offsetting the 10% loss from Q1 2020.

Balanced global equity & bond (% quarterly growth)



50% Barclays Global Aggregate and MSCI World (USD)
Source: Bloomberg, PIM

Asset Allocation

Overall	--	-	N	+	++
Equities			■		
Fixed Income		■			
Cash	■		←		
Commodities	→	■			
Alternatives					■

Regional Equities	--	-	N	+	++
Australia		■			
Canada		■			
Euro Area				■	
Ex- Germany				■	
Germany				■	
Hong Kong		■	←		
Japan				■	
Sweden			■		
Switzerland				■	
U.K.	■				
U.S.	■				
Emerging Markets				■	
Commodity Exporters			■		
Commodity Importers				■	

Global Equity Sectors	--	-	N	+	++
Consumer Discretionary			■	←	
Consumer Staples		■			
Energy	■				
Financials		■			
Health Care					■
Industrials		■			
Information Technology				■	
Materials		■			
Real Estate			■		
Communications				■	
Utilities		→	■		

Commodities	--	-	N	+	++
Gold					■
Oil		■			
Agriculture		■			
Industrial Metals		■			

Fixed Income	--	-	N	+	++
Duration		■			
Government Bonds	■				
Yield Curve				■	
Inflation Protection				■	
Investment-Grade					■
High-Yield			■		
EM Sovereign USD				■	
EM Sovereign Local				■	

Government Bonds	--	-	N	+	++
Australia				■	
Canada				■	
Euro Area			■		
Ex- Germany				■	
Germany	■				
Japan			■		
New Zealand				■	
Norway				■	
Sweden			■		
Switzerland			■		
U.K.		■			
U.S.		■			

Currencies vs USD	--	-	N	+	++
Australia		■			
Canada		■			
Euro Area				■	
Japan				■	
New Zealand		■			
Norway		■			
Singapore			■		
Sweden			■		
Switzerland				■	
U.K.			■		
Emerging Markets				■	

Alternatives & Structured Opps.	--	-	N	+	++
Dispersion/ Long Vol				■	
Dividends EuroStoxx				■	
Gold Twin Win				■	

Source: PW

→ Increase from previous quarter

← Decrease from previous quarter

Global economic dashboard

Indicator	Derivative 1st	Derivative 2nd	Interpretation & outlook
Growth			
Global leading economic indicator	-	+	Sharply improving from very low base.
ZEW/IFO	-	+	Negative everywhere but bouncing.
US ISM manufacturing new orders	-	+	Contractionary level but improving.
Consumer confidence	-	+	Low and improving, but did not fall to previous recessionary lows.
Business confidence	-	+	Low and improving.
Global PMI	-	+	May contractionary but sharply higher than April.
G7 employment	-	+	Unemployment still extremely elevated with some improvement
Global trade volume	-	0	Global trade has fallen sharply on economic crash and closed borders.
Oil prices	+	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 is turning reflationary in the second half.
G7 credit growth	+	+	Credit demand is growing, but for safety rather than growth
Financial stress	+	0	Ted spread narrowed from decade highs and credit spreads have narrowed dramatically.
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
Wage growth	0	0	Wage growth almost irrelevant with employment backdrop.

All growth indicators are red, but rate of change is sharply positive

Central banks all-in

Inflation is not a 2020 story

Source: Bloomberg, PW.

Global Economy

World in a steep recession, but a second half rebound is in the cards

Our global economic dashboard shows an economy which shuddered to a sudden stop, and is now showing signs of a sharp recovery. The dashboard three months ago had red negatives everywhere, and over the last quarter the second derivative column has turned uniformly 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 month on month for the remainder of the year. The economy will benefit from significant monetary and fiscal thrust, as well as a recovery led by pent up demand on 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 months, 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 incremental growth month on month for the remainder of 2020

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, which might trigger renewed government restrictions or voluntary changes in behaviour that weigh on growth.

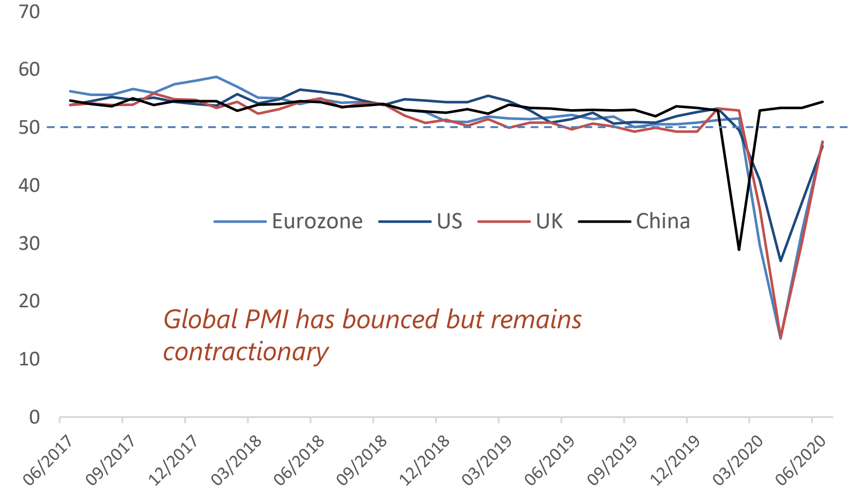
Global Economy

Q2 2020 saw what appears to be the end the most sudden economic collapse in activity since WWII. The prevention and social distancing measures relating to the COVID-19 virus have led to an extremely sharp hit to the global economy. As these restrictions have begun to be lifted, leading indicators have started to improve. Composite PMI readings now show a recovering economy. While many indicators remain in contractionary territory, the end of Q2 was much stronger than the start. The composite PMI index only measures change from the previous period, and a bounce from a record low in March was inevitable as workers returned to factories after an unprecedented shutdown.

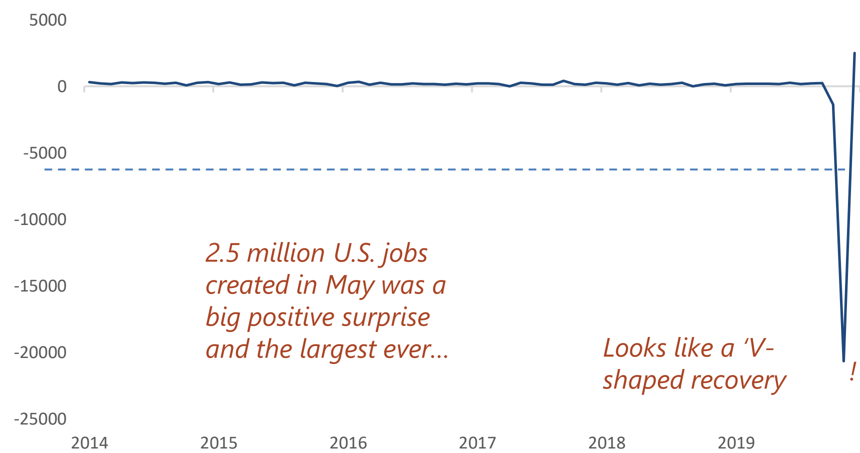
Jobs tell a similar story. The US saw unemployment rise to 14.7%, before a surprise 2.5 million jump in US non-farm payrolls in May, while almost all economists were predicting further job losses. While the 2.5 million is the largest monthly gain ever, it is still only a small percentage of the 20 million jobs that were lost in previous months. As of the end of May US unemployment stood at 13.3%, which is probably understated due to ambiguities relating to 'workers' who held jobs but did not work.

The UK and the rest of Europe saw an uptick in unemployment, but nowhere near the extent of the US because of government sponsored furlough schemes. The UK has seen jobless claims of 3 million since the virus lockdown, but they would have been far worse had the government not taken unprecedented action to keep people in their jobs. The UK taxpayer is now paying the wages for almost 12 million jobs at a cost of more than 28 billion pounds ($36 billion) in an effort to prevent a wave of mass unemployment over the summer. The UK Office of National Statistics said there were some signs of stabilization, with Adzuna data showing vacancies picking up slightly in early June to 45.6% of the 2019 average. That increase is expected to be reflected in official estimates published next month. In the three months through May, vacancies plunged by a record 342,000, with the retail and hospitality sectors posting the biggest declines. The number of hours worked fell by almost 9%.

Global Composite PMI

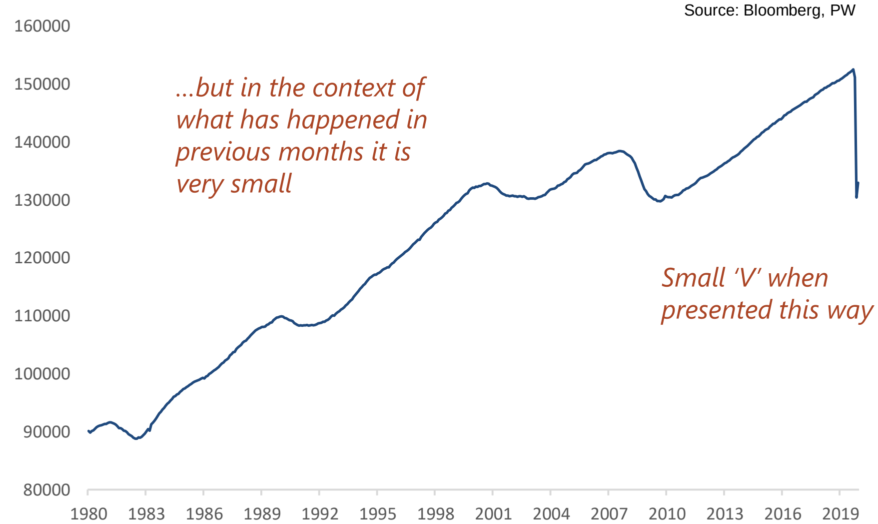


US non-farm payrolls (monthly change '000s)



US non-farm payrolls (total 000's)

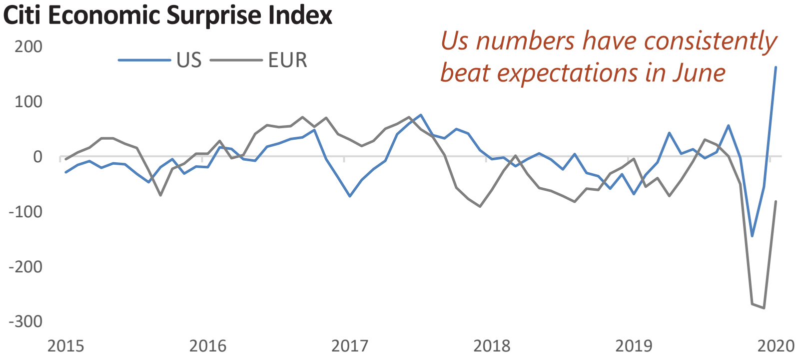
Source: Bloomberg, PW



Source: Bloomberg, PW

Forecasting global growth with any precision is impossible given the unprecedented nature of the imposed contraction due to distancing measures. No one knows when the virus will be contained. We also do not know if containment will be permanent or if it will flare up again? A large and rapid response from global central banks and governments has already taken place. If containment measures are effective, this may well be sufficient, but more will be needed if a second wave necessitates more 'lockdowns' in future quarters. The speed and durability of the second half rebound depends on the virus, the central banks, and government policy. We expect a clear rebound in growth in Q3 and a further increase in Q4, but the economy will be much smaller at the end of the year than before the virus outbreak, and the downside risks are increasing. As the virus appears to be contained throughout most of the developed world, it is with high confidence that we expect global growth to rebound in the second half of 2020 and continue throughout 2021. The economy will benefit from a very significant monetary and fiscal thrust, as well as a recovery led by pent up demand on deferred expenditures. We expect policy will remain supportive for growth even after the economy begins its recovery. New treatments, and a vaccine are likely developments in the coming quarters and we remain optimistic that life, the economy and markets will recover from the current pandemic. However while we expect growth to rebound sharply we do not expect the economy to recover to last years levels in the near future.

Citi Economic Surprise Index



Source: Bloomberg, IMF, PW

The US economy has positively surprised in growth numbers and in policy action. A strong jobs data and resilient retail sales has seen the US Citi economic surprise index move to its highest level since its 2003 inception. European data continues to miss expectations but not by as much as it has earlier in the year.

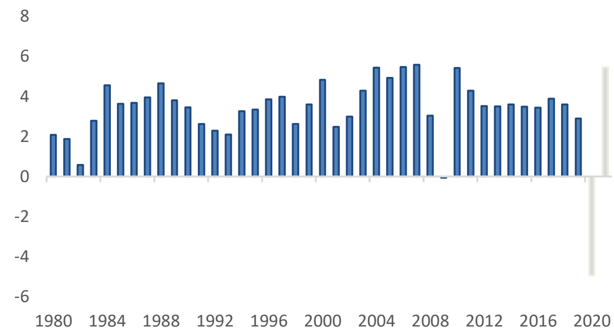
The path of consumer spending will be the key to the shape of the economic recovery. Initial improvements, driven by a relaxation of social distancing measures and policy support are already clear. Thereafter improvements in the employment trend, and confidence that excess savings will not be required for future economic setbacks will be required to push consumer spending. The U.S. saving rate was 23% in May after surging to a record 32% in the prior month as nationwide lockdowns kept people home. Savings can be viewed as healthy but is also a sign of low confidence. if it doesn't unleash pent-up demand for goods and services, it will stifle the biggest engine of the U.S. economy.

Global GDP Growth

	2018	2019	2020e	2021e
World	3.7	3.1	-4.5	5.0
Developed	2.3	2.0	-6.0	5.5
Emerging	5.1	4.3	-1.0	6.0
US	2.9	2.2	-4.5	5.0
Euro	1.9	0.9	-9.0	7.0
UK	1.3	1.4	-10.0	7.0
China	6.6	6.0	2.5	7.0

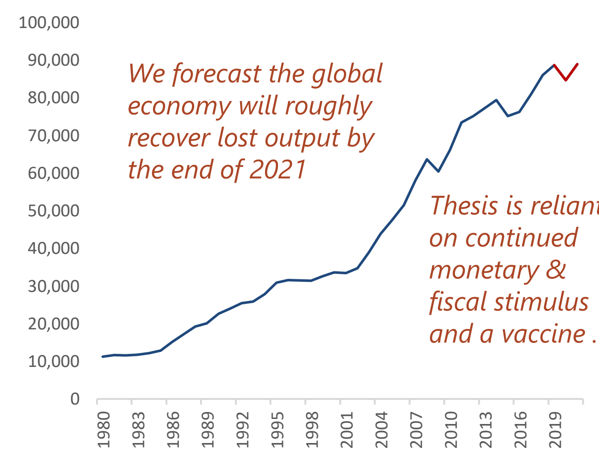
Source: Bloomberg, OECD, PW

Global GDP Growth



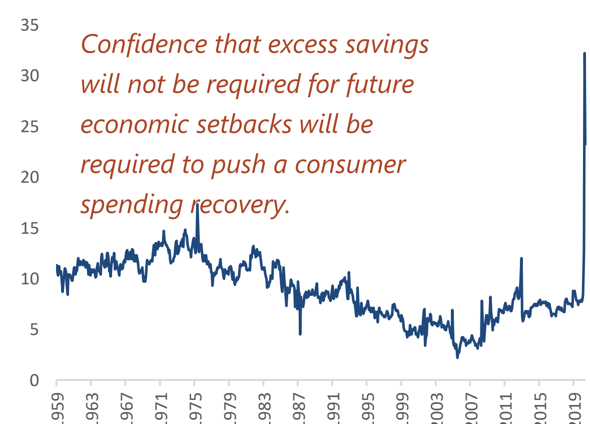
Source: Bloomberg, IMF, PW

Global GDP (USD $2018 $billions)



Source: Bloomberg, IMF, PW

US Savings rates (% of disposable income)



Source: Bloomberg, IMF, PW

The speed and intensity of the virus driven recession has rendered many traditional economic indicators out of date before they are published. To provide a timelier read on the depth of the downturn, and early indicators on the recovery, we monitor a number of high frequency, alternative, and market measures. The overall picture looks less bleak than it did a few weeks ago. Indicators for a number of major economies have come off the floor.

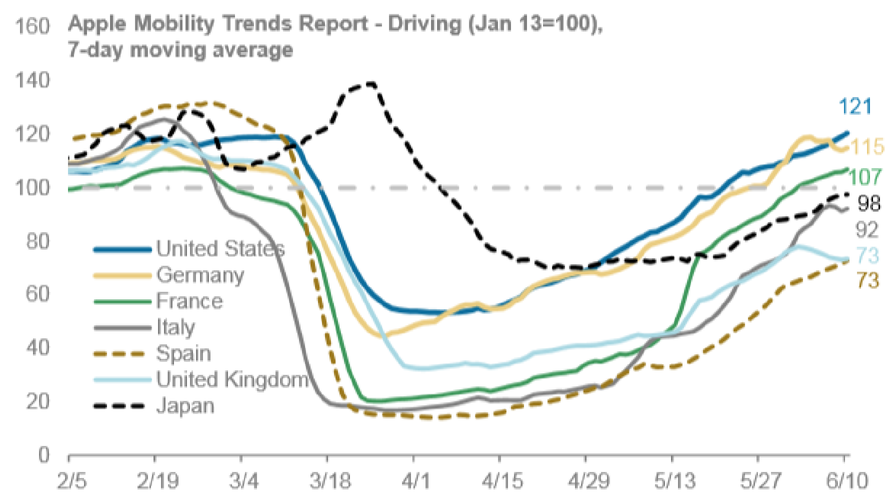
In China and Germany, some gauges show activity back to pre-virus levels. Traffic levels in some of the world's major cities have edged off their lows - a hopeful sign of reviving activity. The services sector; restaurants, hotels, cinemas and tourist sites that make money from the consumer crowd is bearing the brunt of social distancing measures. Data from OpenTable, a booking app that supports 60,000 restaurants across the U.S., Germany, U.K. and a few other countries, show the number of people eating out fell to zero in March and stayed there in April. The most recent few weeks show the beginning of a revival. Germany and Australia appear to be leading the way. The volatility of the series flags caution in interpretation. It's also possible that new rules requiring advance booking are impacting the series.

Trade flows have slowed. Relative to developments elsewhere in the global economy, though, they appear surprisingly robust. The volume of goods arriving at U.S. ports in the four weeks through June 11 is down 5% from January levels.

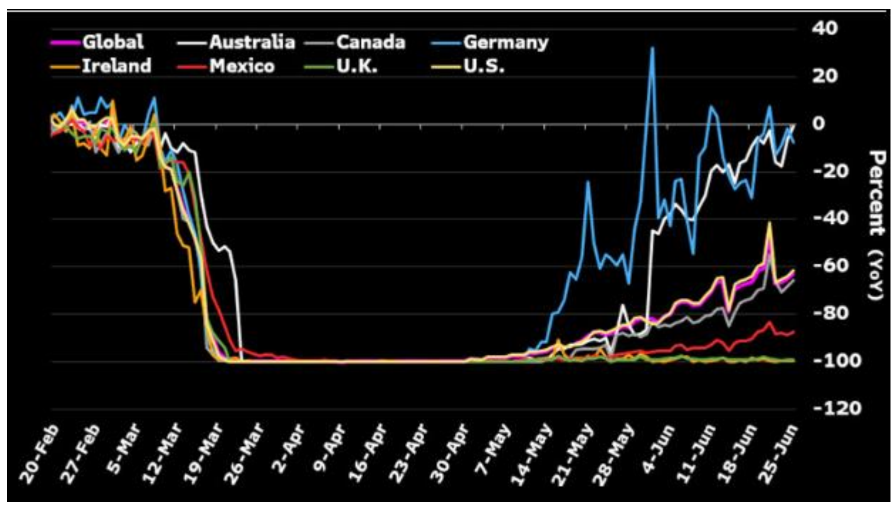
High frequency economic indicators are consistent with rebound in other leading indicators

The number of shoppers on Europe's high streets plunged more than 80% during the height of the virus crisis. The latest data from ShopperTrak shows foot traffic in France and Germany paring the decline, with high street foot traffic in the most recent data down about 20% and 30% respectively from a year earlier. Numbers for the UK remain more depressed.

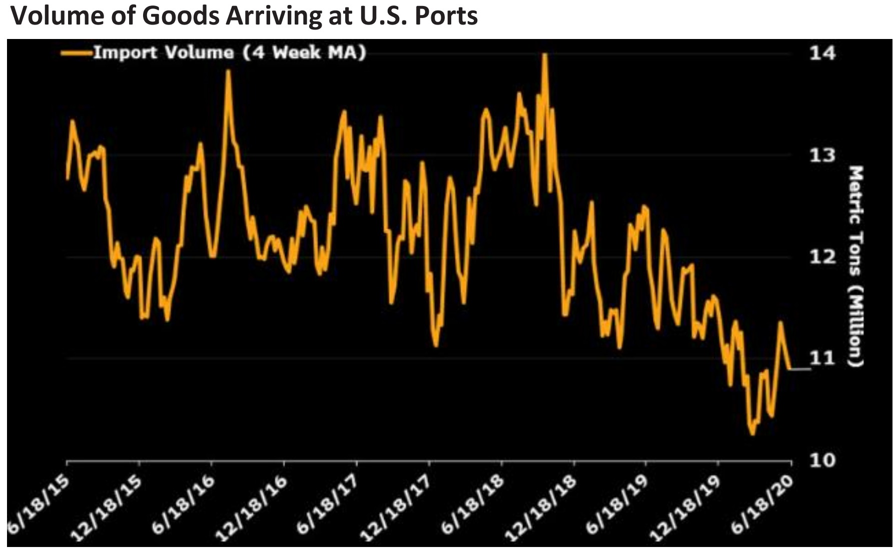
Driving trends



Global Restaurant bookings



Volume of Goods Arriving at U.S. Ports

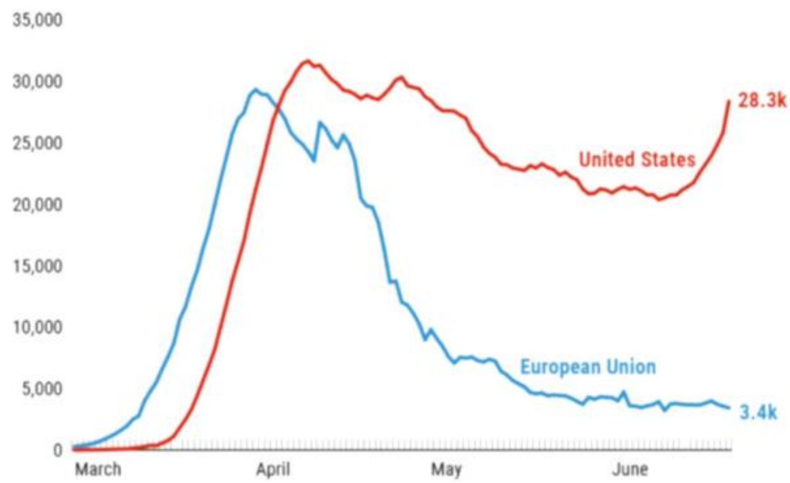


Source: Morgan Stanley , Bloomberg, Apple

While we expect significant recovery in economic growth in the second half, that does come with significant risks. New Covid-19 infections and hospitalisations are rising rapidly across large parts of the Southern states. New cases increase the likelihood of further regional lockdowns and also negatively influence consumer and business confidence. In Europe the risk of a second wave is low, for now. Should a second wave occur in Europe we think lockdowns are more likely than they may be in the US, but they will probably be less stringent than those earlier this year. Authorities are becoming better at dealing with hot spots as they occur, and treatments are also improving.

There is also a small risk that fiscal stimulus will be delayed or slowed because of political spats. The US government has so far passed relief bills totalling $2.9 trillion, but some of the key measures, notably enhanced unemployment benefits, are set to expire at the end of July, and support for state and local government has been insufficient. The House has passed a further $3T-plus bill, but Republicans in the Senate want to do much less. Additional fiscal stimulus will be need to keep recovery on track. We expect new measures, greater than $1 trillion to be passed by early August.

7 day average number of new cases



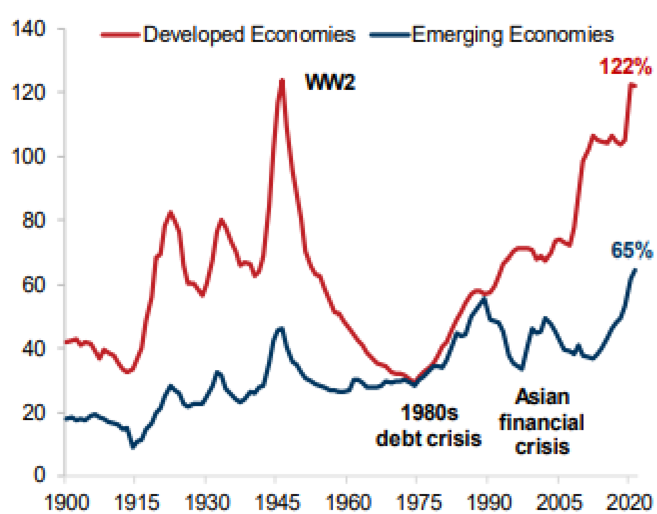
A second wave is an economic risk to be aware of, but it should not have the same impact as first wave

Debt and Deficits will continue to balloon

With a substantial element of unpredictability in economic growth over the coming quarters, there is one thing that is certain, the debt and deficits of all the major economies will reach levels not seen since World War II. We are not questioning if the debt is needed. The benefit of running large deficits today likely far outweighs 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.

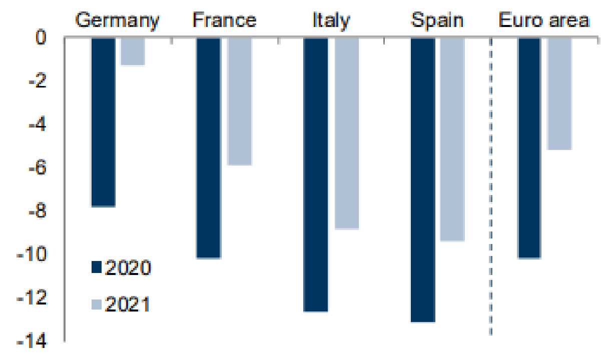
Will debt be repaid through future austerity and taxes, with government surpluses? Will there be sovereign defaults? Will debt be monetised, or will perpetual negative real rates be the answer to manage and reward high debt levels. The path to deal with debt will determine if it will be deflationary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

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



The surge in government deficits has the G7 on path to reach 122% debt-to-gdp and in Emerging Markets to reach their highest level in history. The path back to debt sustainability that was achieved in the 30 years following WWII may not be achievable this time. From 1946-1976 the UK government ran balanced primary budgets. The post war euphoria and infrastructure build led to nominal GDP growing by 8.8% per annum (2.3% real and 6.5% inflation). 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.

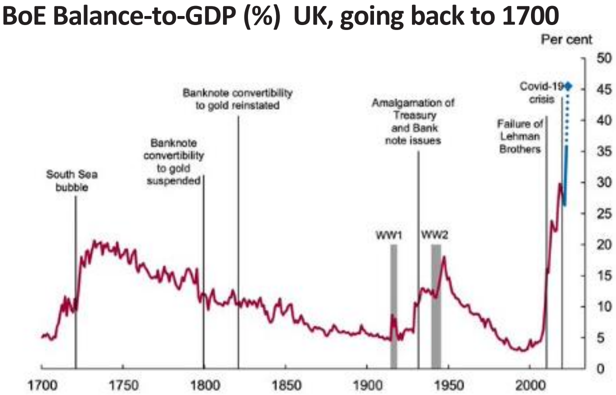
Euro Deficits



Source: Goldman Sachs

The Euro area will likely see its economy contract by double digits in 2020 and the EC's proposal for a EUR 750bn Recovery Fund raises deficits but it also increases the likelihood of further fiscal integration. As the year progresses, we expect the PEPP to be increased, which helps the economy recover in the near term but adds fiscal stress. Goldman Sachs estimate budget deficits to rise to ~13% of GDP in Italy/Spain, ~10% in France and ~8% in Germany.

BoE Balance-to-GDP (%) UK, going back to 1700

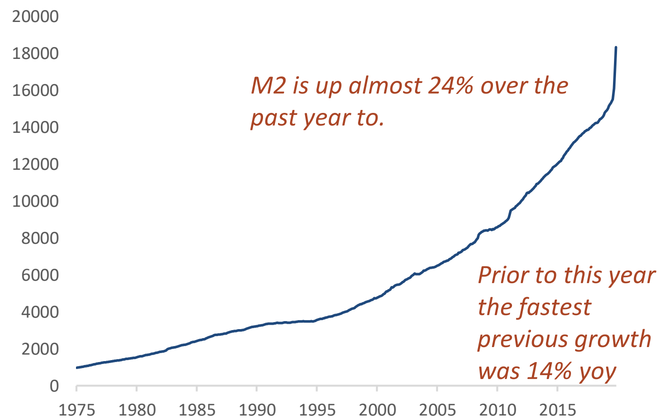


The BoE has provided us with a long term chart of their balance sheet to GDP. It appears the country has made its decision on austerity vs. monetisation of debt. Prime Minister Boris Johnson vowed the U.K. will spend large sums on hospitals, schools and roads to jump-start the economy as it emerges from the coronavirus lockdown that has plunged the country into what may be the worst recession in three centuries. Johnson says he has rejected a return to the austerity policies that followed the 2008 financial crisis and said the country will "build our way back" from the crisis through "shovel-ready" projects. "The lesson is to act fast and we're going to make sure that we have plans to help people whose old jobs are not there any more to get the opportunities they need. We are absolutely not going back to the austerity of 10 years ago".

Central Banks — To zero and beyond

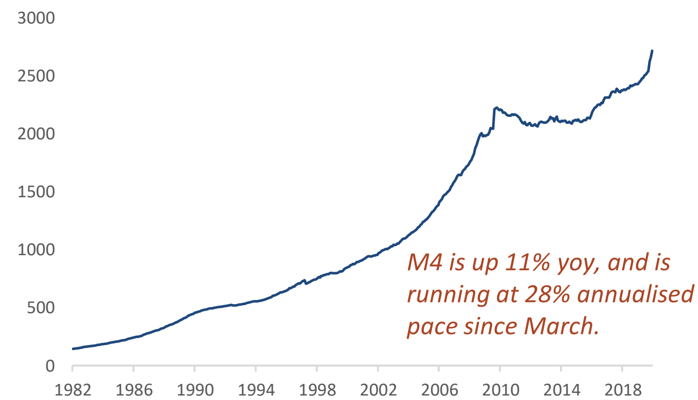
Central banks are 'all-in'. They have unleashed a dizzying number of unconventional steps over the past three months to cushion the economy from the impact of the coronavirus. The Fed's response to the virus has been robust and ongoing. Zero rates, corporate bond buying, and a promise to do whatever 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 looks to be on track to track to expand its balance sheet to almost €6 trillion by the end of 2020. We expect future increases to the PEPP will see it grow close to €2 trillion. In the UK policymakers have succeeded in funnelling cash to businesses and preventing a wave of corporate insolvencies. Broad money, M4, leapt by £177 billion form the ned of February to the £2,705 billion at the end of May, a record 28% annualised pace. The PBoC abandoned the rigid aim to sync M2 and nominal GDP growth, and monetary conditions responded. M2 growth has accelerated to its fastest in three years, boding well for the medium term. The PBoC probably is done cutting interest rates, though reductions to reserve requirements are likely to continue. The Bank of Japan has seen its balance sheet swell to more than 115% the size of its economy, and it now owns 75% of all Japanese listed etf's.

US M2 ($18,344 billion)



Source: Bloomberg, PW

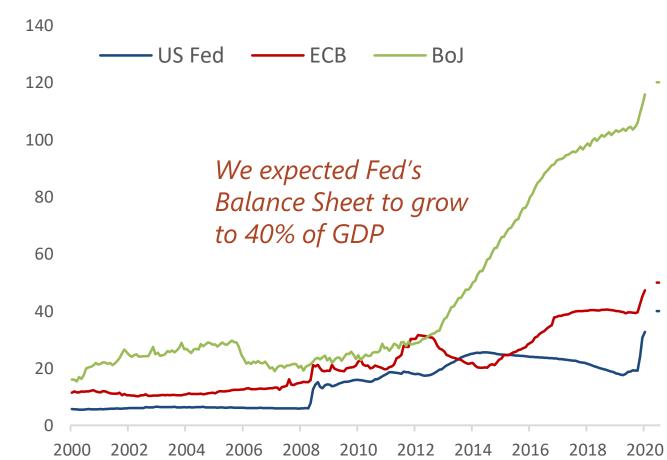
UK M4 (£2,715 billion)



Source: Bloomberg, PW

We expect central banks to continue to push forward with aggressive policy and keep policy very loose 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 charts above show 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.

Major CB balance sheet (% GDP)



Source: Bloomberg

Thematic — Covid crash triggers possible regime change

The scale of the economic downturn and size of policy response to the pandemic likely triggers an investment regime change.

Globalisation and disinflation turn to protectionism and stagflation. Since the late 1980's the world has moved from a highly inflationary and regionally isolated world towards a world with globalised supply chains which improved productivity, reduced costs and created a secular disinflationary backdrop to the global economy. Global exports have grown to 35% of GDP and Treasury yields have fallen from the high teens to less than 1% over that period.

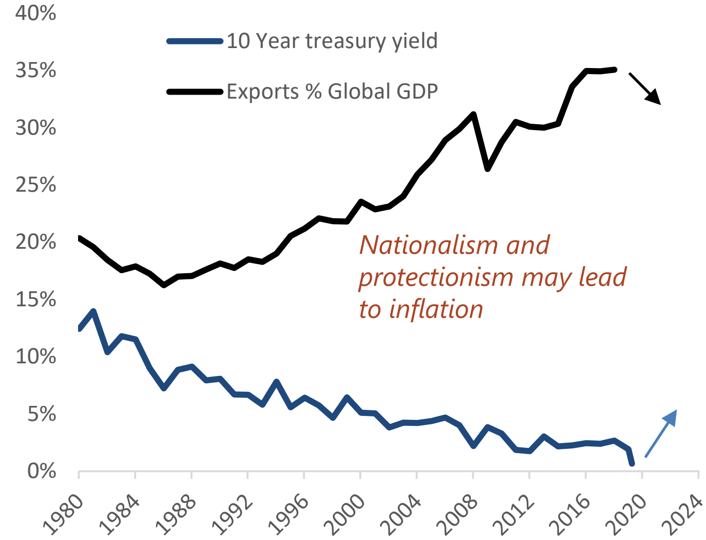
New regime: Nationalism wins out over globalism. Countries protect supply chains from foreign threats and gain security over price. *Implications are stagflationary, own real assets that are not cyclical.*

Monetary passes baton to ever increasing fiscal: Monetary policy has been dominant driver of policy over fiscal policy. Since the Fed initiated QE1, central bank policy has muted economic cycles and been the driver of asset class performance. With central bank policy approaching its limits a new investment regime will emerge. Fiscal thrust has now arrived. Populism has already been a successful political strategy, and helicopter money is as populist as you can get. *Implications: Massive build up of sovereign debt. Initially deflationary, but monetisation of government spending and debt eventually lead to rapid inflation.*

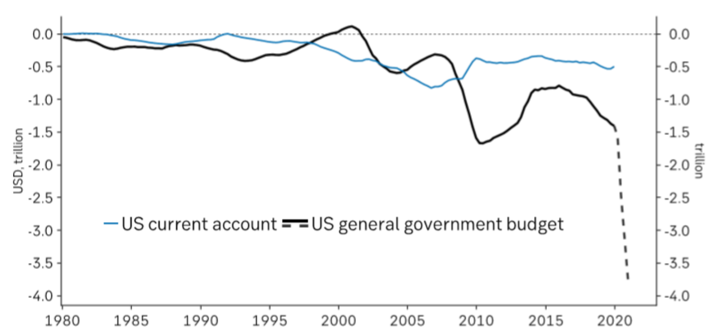
Return of the cycle: We have become used to living in a world with low macro volatility low earnings volatility, and equity volatility. The VIX was often below 12 for much of the past seven years. We are entering a new regime where we do not know if the policy response has been enough, or if more is needed. We are seeing a massive contraction in GDP and we expect a significant expansion to follow. *Implications: Big swings in growth and policies that cannot be fine tuned because of uncertainty should mean more volatility and higher risk premiums required on cyclical assets.*

The West becomes German: We expect a significant rebound in economic activity once we get past the pandemic Another scenario is a jump in savings and a very muted consumption bounce. Many individuals may have woken up to their limited financial safety net as a result of the Pandemic. A more cautious consumer, that avoids unnecessary debt is a very possible outcome. *Implications: Debt driven consumerism dies.*

Regime of increasing trade and falling interest rates over?

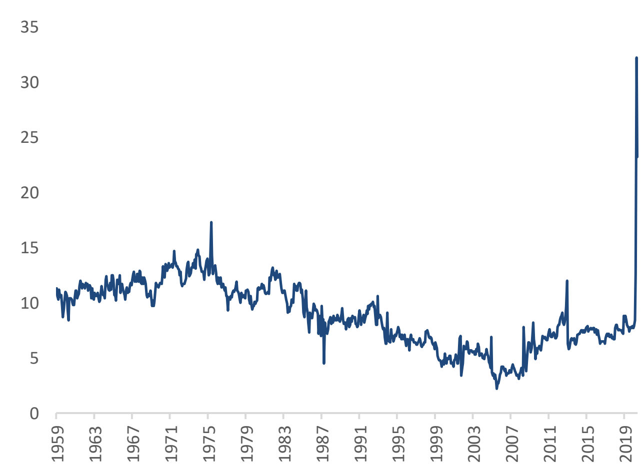


Deficits and debt will be greater than predicted.



Source: Bloomberg, SocGen, Plurimi

US Savings rate (% of disposable income)

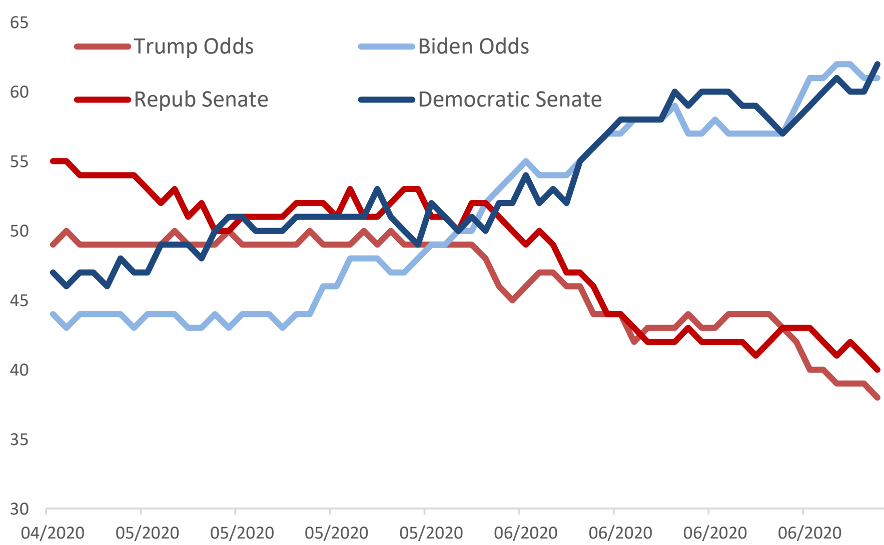


Source: Bloomberg, SocGen, Plurimi

Thematic **US Election**

At the start of the year Donald Trump looked to be in a strong position for re-election. Betting odds had him as the favourite on the back of low unemployment, strong economy, and strong stock market. Following the economic slow down, protests and riots around the Black Lives Matter movement and what appears to be a second wave of the virus in the southern states Biden is now the front runner on betting odds. The US Senate seemed certain to stay under Republican control in January, and that is now looking to go marginally towards Democratic control.

PredictIt 2020 betting odds



A Democrat presidency creates some risk to tax cuts, but wont change the central bank policy that's driving assets higher

The Trump administration has proven to be very stock market friendly. The tax cuts and de-regulation that has been put in place may come under threat with a Biden win and Democratic Senate. Goldman Sachs currently estimates the S&P 500 will earn $170 per share in 2021. They would reduce that estimate to $150 per share in a scenario where the tax cuts are reversed. We think small cap stocks would be most at risk in this scenario. They have a much higher effective tax rate. We think the election is something to be aware of, but do not expect a Biden presidency will be anywhere near as left wing as a Sanders or Warren presidency would have been. Central bank policy is the driver of the stock market at this point in time, and we expect that to remain the case regardless of who the next US president is.

Equities World (Neutral)

MSCI WORLD	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	21.41	59	20.96	19.77
BEst P/E Ratio	23.01	97	15.95	15.78
Long Term Price Earnings Ratio	22.21	56	22.10	21.79
Price to Book Ratio	2.47	64	2.38	2.34
Price/EBITDA	10.18	98	7.71	7.31
Price to Sales Ratio	1.68	93	1.32	1.32
Enterprise Value/EBITDA	12.49	92	10.67	10.60
Profit Margin	7.35	65	6.21	6.57
Operating Margin	10.52	51	10.44	10.46
Dividend Yield	2.26	49	2.26	2.31
10Y Yield	0.66	1	3.85	3.84

Source: Bloomberg. Jan 1995 to April 2020

Following the significant rally in Q2, global equities are back to expensive on most measures. The best thing about equities is bonds. While equities trade at 80 percentile on average, compared to record low treasury yields, equities still offer a significant risk premium of 6.6%.

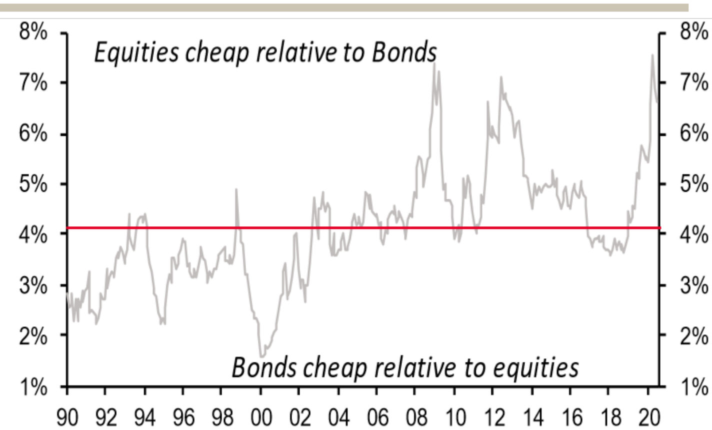
Key inputs for Global ERP

Risk premium	6.6%	Consensus growth '20	-17.4%
Normal	4.1%	Consensus growth '21	27.0%
Min	1.6%	Medium-term growth	15.1%
Max	7.4%	Long-term growth	3.8%
10 year bond	0.8%	Payout ratio	40%
IRR	7.4%		

Factors favouring equities

- Strong economic news is unexpected, but it will be market moving.
- 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.
- Economic growth is moving forward, and next year's earnings will be much higher than this year's with any growth.
- Pharmaceutical companies remain focused on developing vaccines and treatments for the virus. Betting against equities is betting against human ingenuity

Global equity risk premium



Source: Bloomberg, SocGen, Plurimi

Factors working against equities

- Optimism on re-opening may be over done and 2nd wave not priced in.
- Broad market is back to near peak valuations.
- Significant output gaps remain and will curtail economic growth and profits.
- Debt and cyclicality are a toxic combination in a recessionary or low growth world.

Equities World (Neutral)

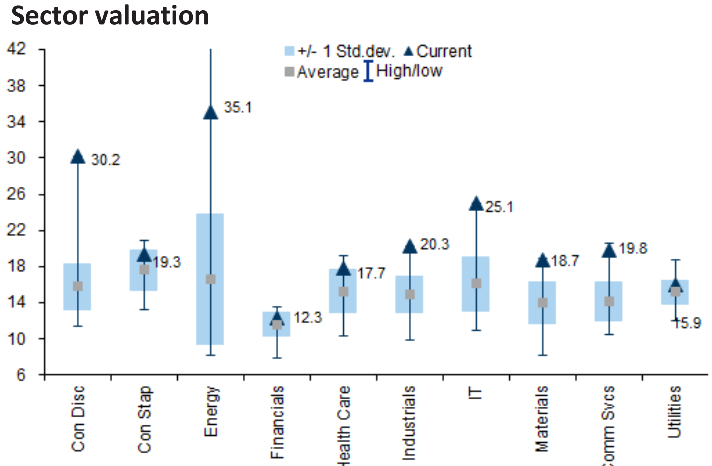
Analysts have cut earnings estimates sharply, with 25-40% downgrades this year. Negative revisions are still occurring, but are slowing. Global PMI has rebounded from a steep contraction and will likely continue to improve. Composite PMI has been a strong predictor of equity earnings, and we expect an opening economy will support the reduced earnings estimates.

Growth stocks have dominated value stocks over the past decade. We thing think forces that have led to such strong performance will stay in place this year. While interest rates remain near zero, the future cash flows of growth stocks are worth as much as current cash flows from value stocks. If discount rates approach zero, then multiples for growth stocks have no upper bound. The traditional value industries are more exposed to economic shocks, and generally have more debt. A 90% economy, where things are getting better, but never getting good will favour dominant companies with profitable business models. Stocks that look cheap will get cheaper. The earnings outlook for these industries is structurally impaired. We have seen what happens to banks in Europe when interest margin is removed, and growth is subdued.

Auto and airlines still have far too much capacity and competition destroys earnings potential. Indebted industrials need the economy to reach potential to extract profits because of financial operational gearing.

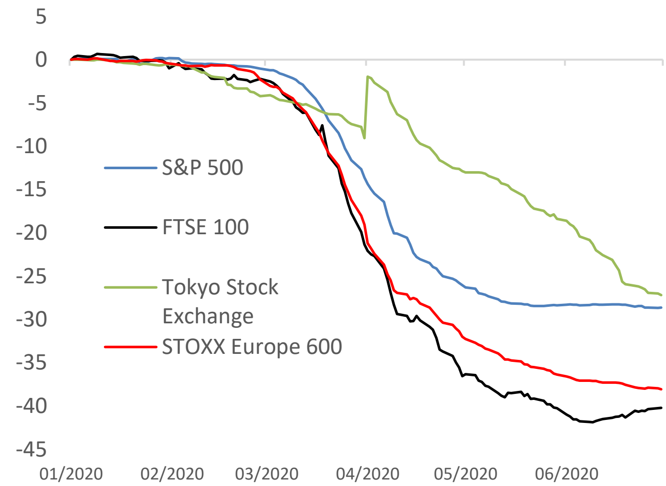
On a sector basis, financials, staples and utilities are the only sectors within 1 standard deviation of their average multiple, but they are nearer to the top than bottom of that range. We continue to prefer sectors that can grow their way into the expensive multiple. Quality growth companies have often seen their business models only mildly impacted and even rewarded by social distancing. We prefer to pay 30x forecast earnings that will be achieved, than 22x earnings which are at significant risk.

Sector valuation



Source: Goldman Sachs

Regional Earnings revisions YTD



RUSSELL 1000 GROWTH INDX	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	35.76	91	24.55	22.32
BEst P/E Ratio	32.70	96	20.37	19.50
Long Term Price Earnings Ratio	50.23	92	33.68	31.15
Price to Book Ratio	11.08	100	5.18	4.60
Price/EBITDA	21.18	97	11.72	10.85
Price to Sales Ratio	4.19	98	2.24	2.07
Enterprise Value/EBITDA	21.65	96	13.45	12.63
Profit Margin	11.06	93	8.22	8.53
Operating Margin	14.24	79	13.42	13.30
Dividend Yield	0.96	23	1.22	1.22
10Y Yield	0.66	1	3.85	3.84
	From:	Jan 1995	To:	Jul 2020

RUSSELL 1000 VALUE INDEX	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	17.05	59	16.86	16.44
BEst P/E Ratio	21.76	100	15.09	14.74
Long Term Price Earnings Ratio	17.01	49	17.16	17.02
Price to Book Ratio	2.05	52	2.06	2.04
Price/EBITDA	8.72	88	6.13	5.60
Price to Sales Ratio	1.50	83	1.26	1.25
Enterprise Value/EBITDA	11.65	88	9.99	10.07
Profit Margin	6.70	43	6.36	6.95
Operating Margin	9.81	16	11.16	11.32
Dividend Yield	2.82	84	2.51	2.43
10Y Yield	0.66	1	3.85	3.84
	From:	Jan 1995	To:	Jul 2020

Source: PW, Bloomberg

Equities **US (Underweight)**

S&P 500	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	21.81	75	19.69	18.78
BEst P/E Ratio	24.92	97	17.10	16.55
Long Term Price Earnings Ratio	25.49	74	22.39	21.45
Price to Book Ratio	3.55	86	2.89	2.78
Price/EBITDA	12.33	100	7.90	7.47
Price to Sales Ratio	2.24	97	1.51	1.52
Enterprise Value/EBITDA	14.19	99	10.69	10.78
Profit Margin	8.55	69	6.80	7.35
Operating Margin	11.68	36	11.76	12.26
Dividend Yield	1.95	46	2.07	1.97
10Y Yield	0.66	1	4.40	4.35

Source: Bloomberg. Jan 1995 to June 2020

US equities trade at elevated multiples vs. the rest of the world, and it remains expensive vs. its own history. Offsetting valuation is the weighting towards world leading companies in sectors which are most likely to outperform in the recessionary environments; 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%.

The speed and durability of the second half rebound depends on three factors, namely, the virus, the Fed, and Congress. We expect a clear rebound in growth in Q3 and a further increase in Q4, but the economy will be much smaller at the year-end than prior to the virus, and the downside risks are increasing. Our US holdings have much stronger balance sheets than the broad market, and usually have significantly higher profit margins.

S&P P/E estimate

We own: *Apple, Alphabet, Facebook, Barrick, Biogen, Visa, Mastercard, Mondelez, Lulu Lemon, Best Buy, Corteva.*

We short: *AIG, Capital One, Edison International, GE, Lyondellbassell, Met Life, Wells Fargo, Well Tower*

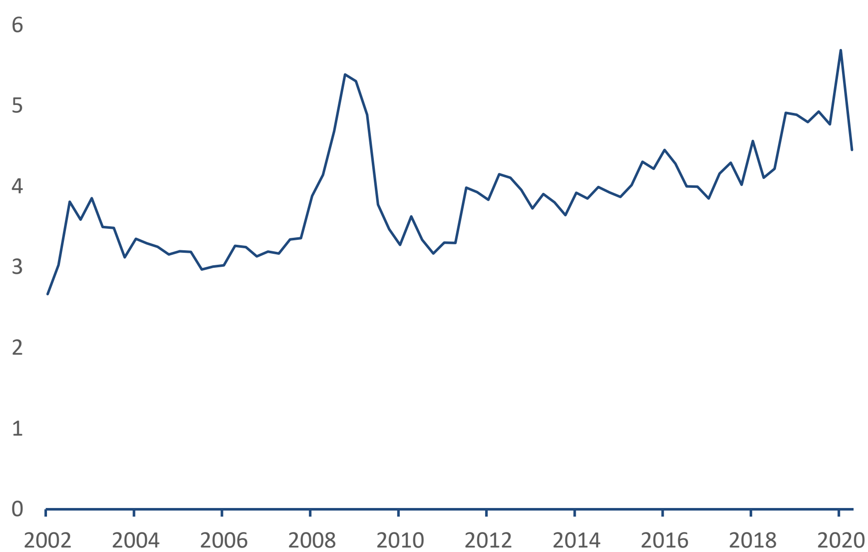
Equities UK (Underweight)

FTSE 100	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	22.22	68	24.75	17.62
BEst P/E Ratio	18.46	99	12.86	12.73
Long Term Price Earnings Ratio	14.15	43	16.22	14.84
Price to Book Ratio	1.47	3	1.93	1.88
Price/EBITDA	6.74	24	7.40	7.25
Price to Sales Ratio	0.92	7	1.17	1.17
Enterprise Value/EBITDA	9.36	70	9.11	8.87
Profit Margin	4.19	20	6.85	7.13
Operating Margin	7.66	18	10.40	9.89
Dividend Yield	4.45	84	3.84	3.81
10Y Yield	0.17	0	2.99	3.02

Source: Bloomberg. Jan 1995 to June 2020

UK equities are as cheap as they have ever been on book value, but are more expensive than ever on earnings. A 4.5% 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%. The U.K. economy has been one of the worst hit by Covid-19. GDP in April was 25% below its January 2020 peak and probably still was down by about 20% in May. The collapse in activity has been particularly large partly because the U.K. is more reliant than other European countries on services and working parents. The country's poor response to the virus has meant that the downturn has been deeper for longer than it needed to be. Population-adjusted new infection numbers and deaths remain the highest in Europe. This has necessitated a more gradual lifting of restrictions on business activity than in other countries. We underweight the region, but it will be an area to allocate towards when positioning for a durable cyclical recovery. Within the UK we prefer healthcare, and technology.

FTSE 100 Dividend yield



Source: Plurimi , Bloomberg

We own: *AstraZeneca, Avast, Plus500*

We short: *Rolls Royce, Royal Bank of Scotland, BP, RD Shell, Compass Group*

Equities **Europe (Neutral)**

Stoxx 600	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	18.76	50	22.32	18.76
BEst P/E Ratio	21.01	100	13.61	13.68
Long Term Price Earnings Ratio	18.04	53	17.68	17.67
Price to Book Ratio	1.66	27	1.85	1.82
Price/EBITDA	6.99	64	6.55	6.33
Price to Sales Ratio	1.06	45	1.08	1.10
Enterprise Value/EBITDA	9.17	49	9.14	9.25
Profit Margin	5.75	43	6.17	6.31
Operating Margin	9.10	40	10.11	9.58
Dividend Yield	2.91	25	3.39	3.39
10Y Yield	-0.46	2	2.28	2.56

Source: Bloomberg. Jan 1995 to April 2020

European equities have jumped from an attractive 1.2x book value last quarter to 1.7x currently. They are down significantly this year, but are still trading 50% above their typical estimated p/e. The main thing working for equities is that the speed and depth of the collapse in economic activity is now being matched by aggressive policy support. The ECB is providing unlimited liquidity to the banking system—at negative rates. Equities will be at risk if the virus returns violently, but otherwise equities will likely have the wind in their sails. European equities often do best in the early stages in the recovery, when the official data still looks terrible, and liquidity is turning up.

Analysts have cut estimates sharply this year, but they now look achievable.

Earnings revisions by year

Source: Goldman Sachs

We own: *Cap Gemini, Deutsche Wohnen, UCB, Novo Nordisk, Neste, Roche, Vestas, Euronav.*

We short: *ABI Inbev, Galagos, Societe General, Sodexo, Delivery Hero, E.On, Telephonica.*

Equities — Japan and Asia (Overweight)

Topix	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	18.78	38	57.58	21.65
BEst P/E Ratio	18.09	66	20.11	15.72
Long Term Price Earnings Ratio	18.19	15	27.80	23.81
Price to Book Ratio	1.15	19	1.56	1.48
Price/EBITDA	6.56	61	7.02	6.23
Price to Sales Ratio	0.72	57	0.70	0.69
Enterprise Value/EBITDA	8.90	30	10.58	9.65
Profit Margin	3.86	67	2.30	2.64
Operating Margin	6.13	55	5.33	5.65
Dividend Yield	2.47	93	1.45	1.16
10Y Yield	0.02	9	1.40	1.32

Asia ex-Japan	Current	Percentile	Average	Median
Price Earnings Ratio (P/E)	13.58	72	12.33	12.08
BEst P/E Ratio	13.02	74	12.01	11.78
Long Term Price Earnings Ratio	15.89	45	16.54	16.07
Price to Book Ratio	1.46	28	1.62	1.57
Price/EBITDA	8.08	86	6.56	6.19
Price to Sales Ratio	1.66	73	1.49	1.47
Enterprise Value/EBITDA	9.54	87	7.73	7.29
Profit Margin	12.75	47	12.62	12.78
Operating Margin	15.08	56	14.90	14.95
Dividend Yield	2.47	29	2.75	2.62
10Y Yield	0.60	0	2.47	2.41

Japanese equities have had a relatively strong first half of the year. At the end of Q1 they were the cheapest they have ever been on earnings and cash flow. Trading at less than 1.2 price to book, the country still offers valuation upside. A significant rally has pushed some multiples higher, but the country still offers the best value in our opinion. Japanese GDP growth will resume in the second half of 2020, after three straight quarters of contraction. The Covid-19 hit hasn't been as severe as other developed markets, as its lockdown has been relatively mild.

Chinese equities are the strongest performer year to date, delivering zero return in USD. China's economic recovery is several months ahead of the West, but for the first time in years, no GDP growth target was set for 2020. This was more an admission of the high level of uncertainty than a lack of ambition to stimulate growth. Monetary conditions have responded well to the PBoC's restrained easing. Abandoning the rigid aim to sync M2 and nominal GDP growth was a game-changer, partly because it would have called for countercyclical policy. M2 growth has accelerated to its fastest in three years, boding well for the medium term. M1, our main leading indicator for GDP, has firmed up, too, pointing to brisk growth at the turn of 2021. Chinese equities should benefit from stimulus and a rebound in growth.

***We own:** Chugai, NTT, NTT Docomo, Nexon, Shin-Etsu, Kao, Keyence, Tokyo Electron. Tencent, Enn Energy*

***We short:** Mitsubishi Heavy Industries, Ana holdings, Asahi, Kansai Electric, West Japan Rail.*

Fixed Income

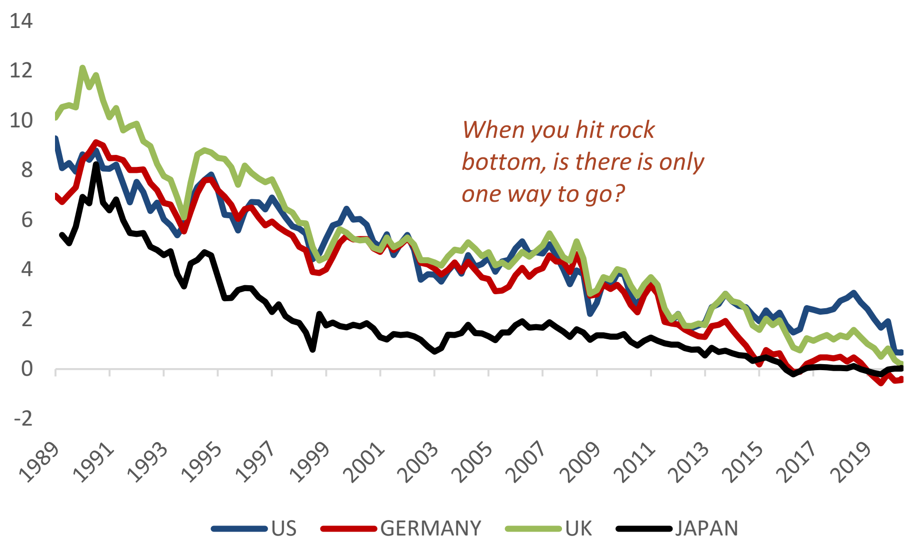
Long duration does not offer value and the insurance has already been paid

We are continuing to underweight G7 government bonds, based on the long term valuation. Bond yields have fallen to levels that reflect a deep recession, a future deflation shock and permanently distorted monetary policy. These macro outcomes are possible, but are not our base case. Anything better than this is a risk to bond prices. Governments a running massive deficits and approaching record debt levels will eventually see debasement as the base case.

The overvaluation partially (possibly almost completely) reflects central bank policy distortions. Central banks have been the bond market's best friend. This is likely to persist and ensure that bond yields remain below our traditional "fair value" for some time. However, we think there is now risk that the US Treasury market has moved to yields so low that any pick up in growth or hint of inflation will see significant sell off. A return to 2% yields would see an almost 20% capital loss for these bonds. Inflation swaps have proved to be relatively sticky, despite falling bond yields. US inflation swaps dropped significantly, but rebounded once open ended QE was announced by the Fed, and the government put a $2 trillion stimulus package in place.

While government bonds offer negative real yields, corporate bond spreads remain somewhat attractive, but the aggregate yield is back to record lows.

10 year sovereign bond yields



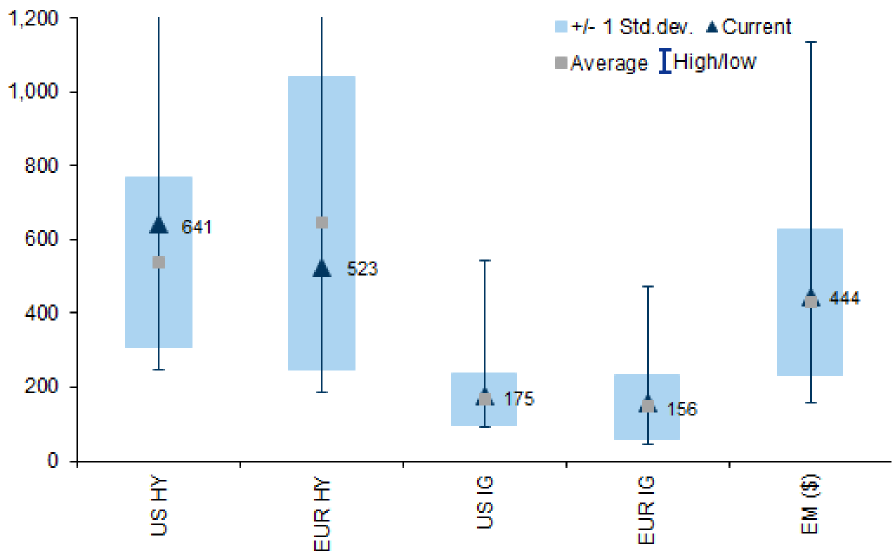
Source: PW Bloomberg

5 year inflation break even

Source: PW Bloomberg

Credit markets sharply re-priced following the trillions in monetary and fiscal stimulus. The combination of liquidity and recovering oil prices have seen all credit spreads narrow massively over the quarter. US IG spreads have almost made the full round trip this year, rising from less than 1% to over 3% at the end of Match, and are back to a moderately attractive spread of about 150 basis points.

Credit Spreads



Source: Haver Analytics, Goldman

USD Spreads

IG	151
IG Fin	140
IG Non-Fin	156
High Yield	594

EUR Spreads

IG	153
IG Fin	164
IG Non-Fin	147
High Yield	514

Source: Goldman

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

Central banks have acted swiftly and aggressively to ensure a liquid bond market and a functioning financial system. The Fed cannot create credit quality, but it will ensure liquidity in bank paper. The Fed is not just buying bank debt, but is expanding its QE to buy corporate bonds, and etfs as well. At quarter end the Fed was the third largest holder in the i-Shares Investment grade ETF.

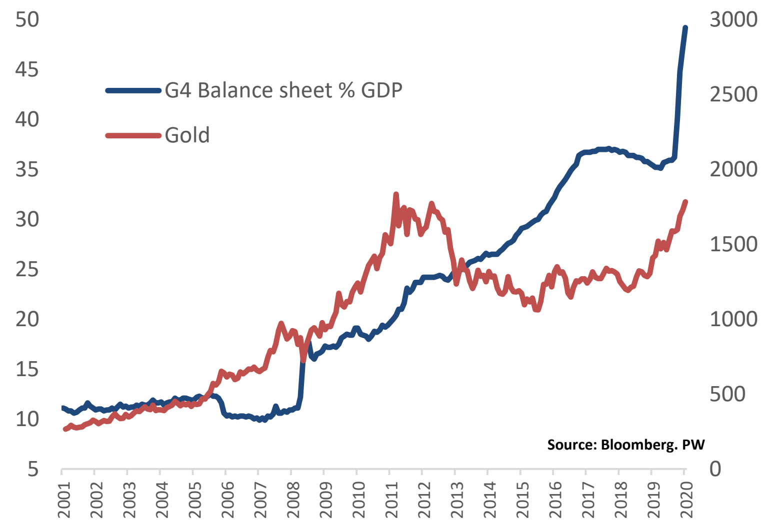
Commodities Gold shines, oil remains over supplied

The environment for gold prices is almost perfect. Money supply us growing at faster rates than when the economy had very high inflation in the 80's. There are a range of geopolitical risks, too many to list, that have the potential to make gold prices spike higher. Price appreciation for zero yielding debt in geo-political shocks is limited, but not for gold. Almost all government debt is offering negative real yields, which is a strong tail wind for gold prices. Global central banks are eager to diversify from the USD, for political reasons and to protect against a potential debasement strategy form the US to deal with its massive debt. As the quarter ended gold was hovering right around $1800/oz, which may set it up for a technical break in Q3. The only missing ingredient would be current inflation, but that is more likely a story for 2022.

Apart from precious metals, commodities are likely to endure further declines in 2H, in our view, with bear-market bounces leaving crude oil and copper particularly vulnerable to an economy that will continue to run output gaps for several years. Oversupply is a primary theme amid a global recession and should continue to pressure grains and agriculture.

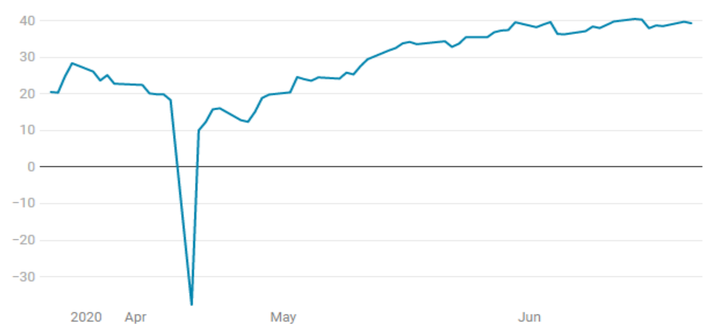
Oil prices had the most notable Q2 I have ever witnessed. WTI was up by 90% for the quarter, after falling by more than 200% in April. Who would have thought that was possible? After the strong recovery energy prices are more likely to than rise further in our view. Along with central-bank easing and fiscal stimulus, OPEC production cuts are responding to decreased demand to help rebalance markets. Renewed and sustained consumption is typically required for enduring appreciation in crude-oil prices. Weak demand prior to the pandemic keeps our price bias tilted to the downside with elevated risks to equity prices.

Gold ($/oz) rhs , g4 Balance sheets (% GDP) lhs



Source: Bloomberg. PW

WTI oil roller coaster ride. ($/bbl)



Source: Bloomberg. PW

Almost unimaginable that oil prices went negative, and then finished the quarter 90% higher than the start.

Ideas **Own Gold & growth and quality in equities. Short cyclical value.**

- Trillions in deficits, and new government debt will make monetisation of debt the possible end game. We continue view **gold** very favourably. **Barrick Gold** is our preferred producer. Structured notes with the payoff converted into gold rather than a fiat currency make sense.

- **Quality Stocks** we like which are benefitting from stay at home economy: **Activision, Nexon, Tencent, Apple, Amazon, Facebook, Alphabet.** **Healthcare** offers best combination of value and growth.

- **EuroStoxx dividend futures** as an inflation hedge, and still at a somewhat depressed entry point. Dividends rise with nominal economic growth. (Real growth and inflation). If central banks print money the long term dividend potential of companies will rise. Longer dated dividend futures benefit from natural selection as well : poorly performing companies fall out of the index, and replacements are better performing companies – usually with higher dividend potential. The pandemic will lead to cuts in 2020 dividends, but very unlikely to impact 2024 dividends. The policies put in place now may end up improving those dividends.

- Investment grade bonds remain more attractive than sovereign debt. Selling put options on investment grade ETFs is also attractive as implied volatility is 20% on the large ETFs. Don't fight the Fed which is backing investment grade , and even buying investment grade ETFs.

- Highly indebted cyclical companies have seen their stocks fall the most. It is too early to rotate into cyclical value, look for quality companies with less debt. **Be underweight indebted cyclicals and banks.**

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