BNP PARIBAS WEALTH MANAGEMENT

2020 INVESTMENT THEMES POST COVID-19

BNP PARIBAS WEALTH MANAGEMENT

The bank for a changing world

Five of our investment themes 2020 confirm their potential

Focus on the medium-term approach

In March, the lockdown of almost half the world's population plunged the global economy into an unprecedented recession, and global stock markets shed 34% in 30 days. Although they bounced back strongly after the announcement of government measures (gradual exit from lockdown and economic stimulus policies), the short-term environment remains uncertain. It is possible that equity markets will retest recent lows: the end of lockdowns will likely see an isolated and temporary outbreak of the virus. The challenges to implementing economic policies, the impact of 'deglobalisation' and renewed trade tensions between the United States and China are likely to see episodes of increased volatility.

As a result, our central medium-term economic scenario involves a gradual recovery in the second half of the year, continuing into next year (a U-shaped recovery).

Some markets will benefit from an attractive valuation. Beyond short-term fluctuations in prices, it is important to look for opportunities to increase equity positions in the event of a fall in prices. In this context, a thematic approach should enable greater selectivity.

The Covid-19 virus crisis amplifies some trends

Structural trends now seem to be essential. The first is the search for yield in an environment of interest rates and bond yields that are likely to remain very low, for a long time to come. The expected returns on good quality bonds are now close to zero and investors are likely to move to other asset classes, while limiting risk-taking. Beyond this transition from bond markets to defensive stocks or alternative investments, some changes in the economy are also likely to generate more specific opportunities in equity markets in the medium term.

THEME 01 – High-quality stocks p.4

We must now favour companies which have high profitability, limited debt, low profit variability and large cash reserves.

THEME 02 - Defensive solutions p.5

The trend is to search for alternative returns via good quality corporate bonds, hedge funds and structured products.

THEME 03 - De-globalisation p.7

Protectionist trends and dependence on international supply chains are expected to lead to a stabilisation and even a decline in international trade in the long term. This 'deglobalisation' should provide opportunities for some companies or even for some countries. In particular, producers of goods and services which substitute imports are well positioned to benefit from this trend. The same is true for emerging market countries which compete with China.

THEME 04 - Digitalisation and technological innovations p.9

Alongside the trends in health care, this is one of the most marked trends: 5G and Artificial Intelligence will benefit from the increased communication and data needs generated by the crisis.

THEME 05 - Innovations in health care p.11

This sector is growing faster than the rest of the economy. Thanks to digitalisation, analytics, database management and Artificial Intelligence, the way treatment/care is given will change considerably at all levels and generate a wave of capital expenditure.

All the themes proposed at the beginning of the year remain attractive but will not be detailed in this document. However, an update on their performance since January is available at the end of this document.

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THEME 01 LONG-TERM MEDIUM RISK

QUALITY NEVER GOES OUT OF FASHION: INVESTING IN HIGH-QUALITY COMPANIES

The defensive virtues of quality stocks are brilliantly illustrated this year. In a world characterised by persistently high uncertainty and major structural developments, quality stocks remain a core holding of choice.

OUR RECOMMENDATIONS

- **This theme remains highly attractive. It is still an ideal core portfolio component. Global by nature, it can be applied in all equity markets.**
- **Companies with strong balance sheets, clear visibility on earnings growth and limited profit variability will remain in high demand.**
- **They will still be expensive amid weak economic growth and major structural changes.**

RISKS

- The outperformance of quality stocks has been strong (a wide spread above their 200-day moving average). This positive trend calls for a period of digestion.
- The high valuation of quality stocks is their biggest disadvantage.
- A normalisation of economic activity will revive risk appetite, temporarily overshadowing the advantages of quality stocks.

An exogenous shock highlights the strengths of quality stocks

Quality stocks have a reputation for delivering above-average returns in the late stages of the cycle and especially during recessions. They demonstrated this brilliantly in the first part of the year as the global economy could no longer function normally.

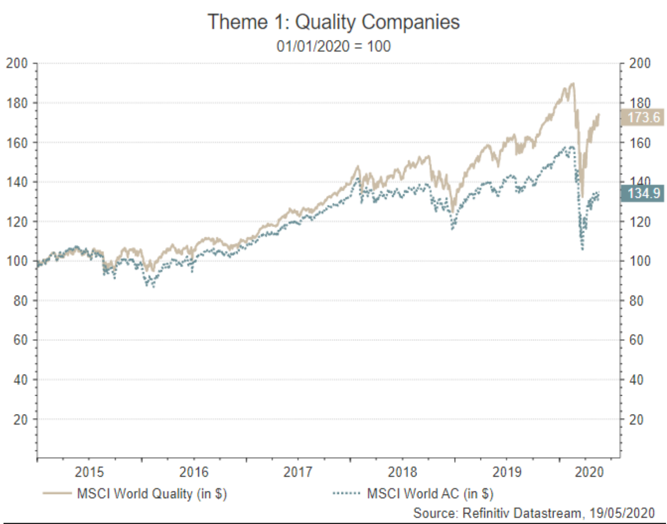
The health crisis has revived investor interest in stocks offering three advantages: limited gearing, high profitability and low profit variability. These three criteria characterise quality stocks.

A core holding in a post-pandemic world

The Covid-19 pandemic is a triple shock: human, production capacity and consumption. Companies will look to diversify their supply chains and digitise their processes. The shock on business volumes and cash flow generation will require limiting capital expenditure.

Adding to this will be a focus on health care, which will lead to a drop in ordinary household spending.

SHARP OUTPERFORMANCE OF QUALITY STOCKS



MSCI World Quality relative to MSCI World — 200D MA — 50D MA

Source: Refinitive, Datastream, 18/05/2020

All of these factors, along with the structural trends of deglobalisation and the need for deleveraging, will feed an ongoing appetite for quality stocks, and thereby maintaining their high price.

THEME 02 LONG-TERM MEDIUM RISK

DEFENSIVE DIVERSIFIERS: SEEKING LOW RISK YIELDS

Expected returns on good quality bonds are low. So investors will most likely move to other asset classes while limiting risk.

OUR RECOMMENDATIONS

- Diversification reduces the overall risk of the portfolio. Our recommendation: certain low-risk products or ones with a calculated risk like Investment Grade corporate bonds, alternative funds, and structured products.
- Such solutions benefit from the more volatile environment and the greater differences in the quality of companies.

RISKS

- Risks include: the sudden rise in interest rates, an issuer default, reduced liquidity from market tensions, or currency fluctuations.
- A broad diversification, short-term bonds and a choice of high-quality issuers can mitigate these risks.

THEME 02 LONG-TERM MEDIUM RISK

Opportunities in the fixed-income universe

The health care crisis and subsequent market corrections are creating new opportunities in fixed income markets:

- Yield spreads have widened sharply on quality corporate debt and on subordinated financial debt.

- The banking sector is well capitalised, especially in Europe.

- The default rate among Investment Grade issuers is low.

Risks lie in the potential deferral or non-payment of the coupon, and no redemption at the first call date.

Green bonds issued by US companies also merit attention. There is a good supply and yields are attractive. They behave like traditional bonds, the difference being that they finance projects primarily aimed at mitigating climate change.

Finally, Emerging Market bonds in local currency also have certain advantages.

Valuations are low and Emerging Market currencies are undervalued, assuming that central banks in developed countries will remain accommodative. Emerging Market bonds in local currency are also a good diversification tool in portfolios. Leveraged loans in Europe offer both an attractive risk/return profile and a natural protection against the risk of rising interest rates since the income generated is based on variable interest rates. This type of asset is not suitable for all risk profiles. Liquidity can be low, so we recommend investing over a long period.

Alternative funds

Alternative strategies have suffered in the general risk aversion environment but once again demonstrated their diversification properties. Asset managers in this area can benefit from the increase (or decrease) in asset prices.

We favour 'Macro' and 'Long-Short Equity' strategies as the Covid-19 shock, trade tensions and populism are putting pressure on certain sectors, and generating volatility and therefore opportunities. 'Event-Driven' strategies also offer attractive prospects given the expected growth in non-performing loans and devalued assets.

Structured Products

The sharp increase in volatility since the beginning of the pandemic offers a more favourable environment for structuring products selling volatility with attractive asymmetric payoffs. These products quite frequently have partial capital protection. They are structured on very different underlyings, with varying degrees of complexity, from a simple stock market index to term contracts, options or interest rate spreads.

Structured products are portfolio diversification tools that can improve risk/return.

THEME **03** LONG-TERM HIGH RISK

DEGLOBALISATION: BENEFICIARIES OF THE REVERSAL IN GLOBAL TRADE

The Covid-19 crisis will accelerate the deglobalisation trend. There are more signs that the supply chain disruptions due to lockdowns have led governments and companies around the world to reconsider their production models.

OUR ***RECOMMENDATIONS***

- **Reshuffle of global supply chains and the creation of new production hubs**

New production hubs with Taiwan & South Korea for upstream tech-related components/products, and Southern Asia for low-end consumer goods

- **Beneficiaries in the US and Europe**

High value-added industries, a wide range of service providers and education

- **Political/geopolitical uncertainty**

Hedge with safe-haven assets (such as gold, JPY and tactical long USD opportunities)

RISKS

The trend of globalisation re-escalates again as:

• a comprehensive US-China trade deal is agreed;

• global trade tensions ease significantly;

• disruptive innovations in digital technologies substantially increase cross-border trade flows

Extended lockdown measures and a second wave of the outbreak lead to a deeper and prolonged global recession in 2020. Investors continue to be 'risk-off' which hurts equity performance, while safe-haven assets should perform nicely.

THEME 03 LONG-TERM HIGH RISK

The pandemic accelerates a reshuffle of global supply chains

The Covid-19 pandemic has exposed the massive risks of sudden stoppages of economies and supply chain disruptions. It also highlights how dependent global companies are on Chinese manufacturing.

As a result, some governments have started to incentivise the 're-shoring' of the production process:

- Japan announced that it would allocate USD 2.2 billion of its record USD 993 billion stimulus package to help its manufacturers shift production out of China and either back home or to Southeast Asia.
- The Trump administration is considering paying the moving costs of American manufacturers that leave China.
- An EU trade commissioner commented recently that the bloc would seek to reduce its trade dependencies and ensure the EU's strategic autonomy.

New production hubs

Post crisis, there could be more social pressure to re-shore some strategic areas and ensure self-sufficiency (medical supplies or other health care needs, for example). Manufacturing companies are also likely to put more emphasis on production base diversification as well as industrial digitalisation and automation. We expect the redistribution of supply chains to benefit Southern Asian countries for low-end consumer products, as well as Taiwan and South Korea for sophisticated tech-related components/products.

In the US and Europe, the trend towards repatriating production capacities is accelerating. Its birth resulted from a combination of technological innovation (allowing shorter supply chains) and rising wages in emerging countries. The great winners are the high value-added industries. Now, the wish to reduce dependency and tackle inequality is strengthened. Investment in education should be ramped up. Deglobalisation is also helped by the rising share of services in global GDP.

To sum up, key beneficiaries of deglobalisation in developed economies are higher value-added industries, a wide range of service providers, and education.

We remain positive on South Korea equities and upgraded Taiwan equities from neutral to positive in early May. Valuations of both markets became more attractive after the corrections. The tech-heavy Taiwan market will be a beneficiary of its 'homecoming' policy and global manufacturers' demand for technology upgrades amid the technology disruption megatrend in 5G, IoT and AI. There is already growing evidence of a domestic Capex cycle.

Furthermore, after announcing a much lower tax for new manufacturing companies relocating to India in September last year, the Indian government reportedly reached out to more than 1,000 US companies (prioritising medical equipment suppliers, food processing units, textiles, leather and auto part makers) in April, offering incentives to manufacturers seeking to move out of China. Although the country is currently suffering from the lockdown, the proactive policy to stimulate its manufacturing sector is a positive factor for supporting the economy in the medium term.

Dealing with political/geopolitical uncertainty

The accelerating trend of deglobalisation could create persistent political/geopolitical uncertainty. There has been mounting global backlash against China over its alleged handling of the Covid-19 outbreak in the early days. The Trump administration has publicly assigned China varying degrees of responsibility for the pandemic and has threatened new tariffs.

We recommend investors to hedge their portfolios with some safe-haven assets such as gold, the Japanese yen and/or some tactical long USD positions when opportunities arise.

THEME 04 LONG-TERM HIGH RISK

BENEFITING FROM DISRUPTION: 5G AND ARTIFICIAL INTELLIGENCE INNOVATIONS

Some themes are joining heavy trends, known as 'structural' or 'secular'. They are thus deployed with little sensitivity to the economic cycle. This is the case of 5G and Artificial Intelligence. The strength of this theme has been seen in its clear outperformance during the health crisis. The outlook remains excellent.

OUR RECOMMENDATIONS

- This theme has gained in importance with the Coronavirus crisis, which revealed major constraints on networks and businesses: digital transformation must accelerate.
- This theme is global and can be applied to all equity markets.
- A long-term investment horizon is required due to the structural nature of these disruptions.
- This is an aggressive investment: volatility well above average and higher capital risks

RISKS

- Innovation is developing at such a fast speed that the idiosyncratic risks are very high. Broad diversification is necessary.
- The Coronavirus crisis is weighing heavily on the capacity of companies to invest (cash flow contraction) and this could create delays in capital expenditure.
- Risks of a political nature exist, since 5G and AI are seen as key to the competitiveness of nations.

THEME 04 LONG-TERM HIGH RISK

The Coronavirus crisis: an accelerator of trends

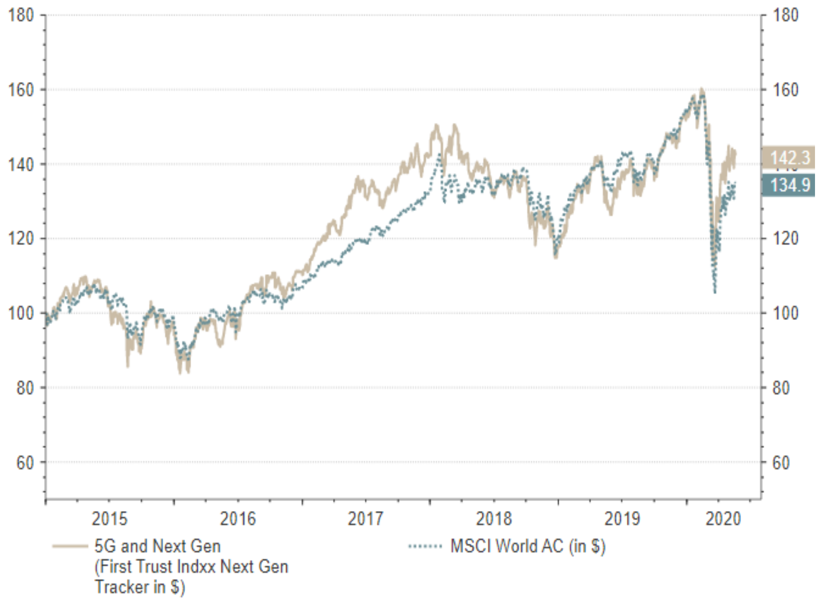
Lockdown imposed on people on all five continents led to an intensive use of the internet. In the United States, for example, surfing has exploded by 50% over the past two months. Various services, such as Netflix or Facebook, were forced to reduce the quality of their streaming by 25%. Consequently, the need to modernise communications infrastructure has become more than urgent.

Among fiscal stimulus measures, spending on 'new' infrastructure - with a strong focus on technology - should be a top priority.

For businesses, relocation and digitalisation are becoming a real priority.

Theme 4: 5G and digital

01/01/2020 = 100



Source: Refinitiv Datastream, 20/05/2020

Investing in the most disruptive trends

5G - the fifth generation of wireless technology - represents a powerful catalyst for digital transformation. It is multiplying the possibilities of Artificial Intelligence, the Internet of Things, Industry 4.0 and Cloud Computing. These prospects are made possible by a huge leap forward in terms of velocity, throughput and minimum latency time. Another important asset is the sharp reduction in energy consumption.

Artificial Intelligence is considered as a technology that can be embedded in almost every stage of a company's value creation process.

It can benefit numerous sectors: media, telecom operators, consumer staples, financial services and health care. Its main advantages are improved productivity, lower costs and human-machine collaboration.

THEME 05 LONG-TERM HIGH RISK

INNOVATIONS IN HEALTH CARE: TECHNOLOGY MULTIPLIES DISCOVERIES AND NEW APPLICATIONS

The health care sector is growing faster than the rest of the economy. This trend has accelerated because of the global pandemic, a heightened awareness of the importance of the sector and the need for rapid progress in this area.

OUR RECOMMENDATIONS

- **This theme is aimed at dynamic investors who are willing to take some risk, because innovation does not always produce the desired results. A long-term horizon is recommended.**
- **Parallel to investing in stocks of a handful of leading companies, in the riskier sub-segments, we like investing in diversified funds, which are managed by highly-specialised professionals.**

RISKS

- The health crisis being a catalyst, the health care sector has already performed well of late and several stocks have reached new highs. The price-to-earnings ratio for the MSCI USA Health Care Index has also risen from 16.8x at the beginning of the year to 18x currently.
- Moreover, even if this debate has been ruled out with the pandemic, receiving treatment is very expensive in the US and there is regularly pressure to lower costs in the health system.

THEME **05** LONG-TERM HIGH RISK

Advances in technology improve the quality of health care

With the aid of new technologies, considerable improvements are being made in product research and development processes. New (types of) medical treatments, tools and services are constantly emerging. The management of therapies and care centres has become much more efficient through the more optimal use of large amounts of quality data.

The health crisis ushers in more innovations in the sector

Amid fears of new diseases, health-related spending is expected to soar in the coming years and support numerous developments in:

- Prevention, hygiene, vaccines and testing;

- Remote diagnostics (several companies active in laboratories, testing and online/remote diagnosis have seen their share price rally in recent times);

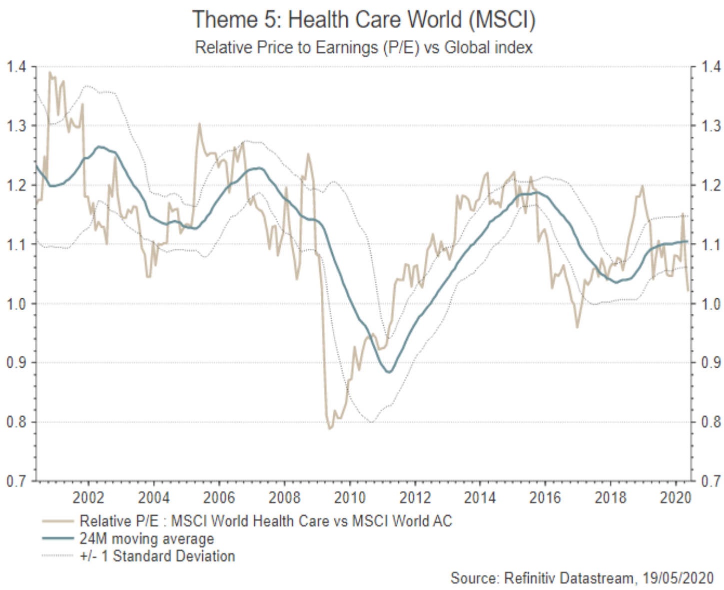
- Treatments in general and more specifically for viruses (attentive investors will have observed good progress on the stock market by promising companies developing potential treatments and vaccines for Covid-19);

- Rapid data exchanges and processing (Artificial Intelligence);

- Medical and robotic equipment, for example to treat infected patients remotely;

- And by extension, the entire hospital and technological infrastructure that supports these improvements.

Despite the outperformance of the Health Care sector in 2020 (often better than the expected 1Q20 financial results), and particularly 'Health Technology', relative valuations are generally not expensive.

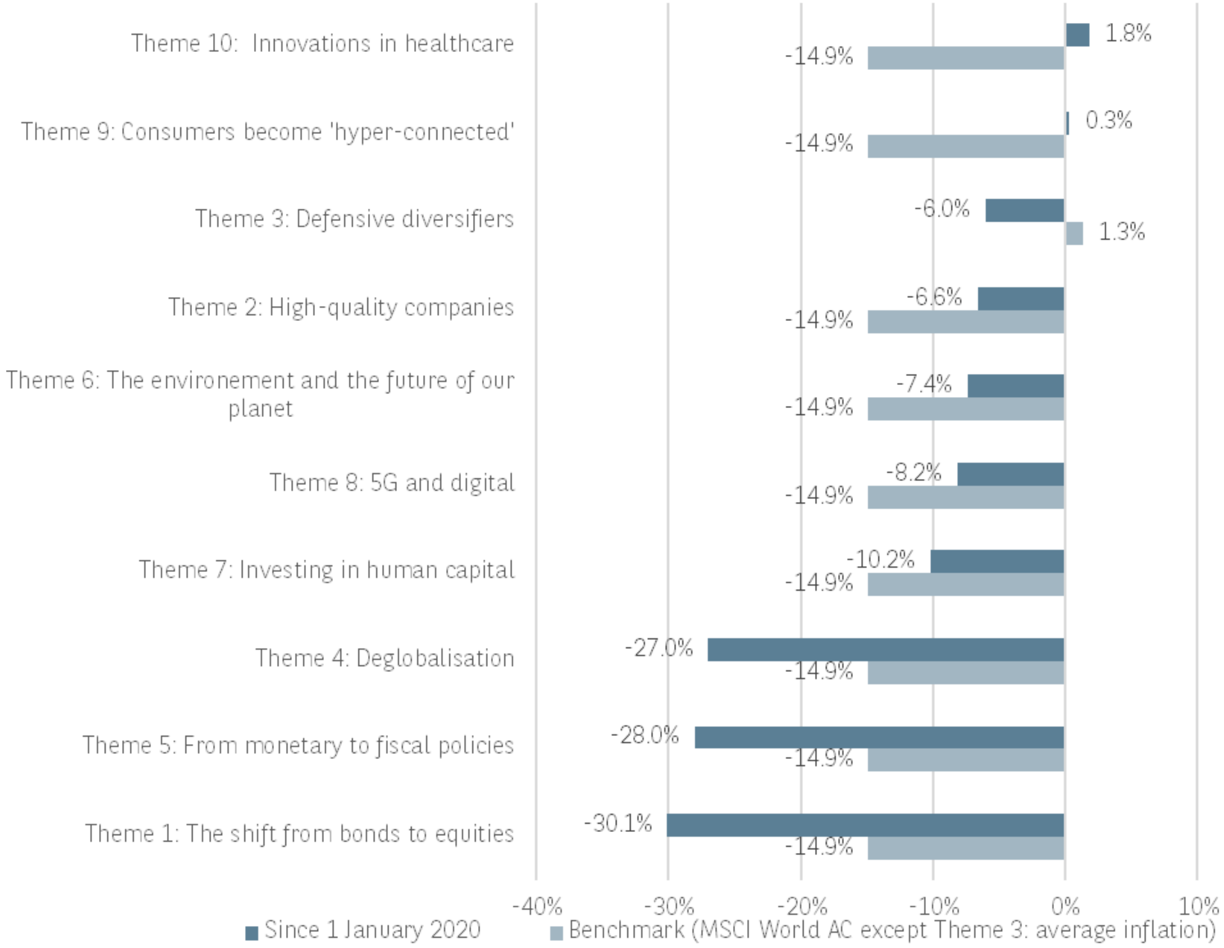


Source: Refinitiv, Datastream, 11/05/2020

Conversely, while a genuine 'war effort' is being deployed to defeat Covid-19, some industry players are suffering from this redeployment. Non-urgent operations, such as fitting artificial limbs, are being postponed.
The shares of some medical equipment-makers are under pressure. But these operations cannot be constantly delayed and a certain normalisation should take place.

PERFORMANCE OF INVESTMENT THEMES PUBLISHED IN JANUARY 2020

Performance vs Benchmark*



Source:
Refinitif Datastream, 13.05.2020
* For Theme 3 we use average inflation as a benchmark

Theme	Comments
Theme 1. There is no alternative (TINA): the shift from bonds to equities	High dividend stocks suffered from the Covid-19 crisis as some governments asked companies to suspend dividends. The theme posted a loss of 30.1% while the global equity index was -14.9%.
Theme 2. Quality never goes out of fashion: investing in high-quality companies	This theme held up really well in light of its defensive properties. It logically beat its benchmark index (global equities: -14.9%), but still posted a negative performance of -6.6%.
Theme 3. Defensive diversifiers: seeking low risk yields	Corporate bonds suffered from the temporary rise of risk premiums. Newcits funds held up better than the equity markets despite posting a fall. The performance of this theme was -6.0%. In this case, the benchmark index is average inflation between the US and Europe. It posted a rise of 1.3%.
Theme 4. Deglobalisation: beneficiaries of the reversal in global trade	Companies in this theme were badly hit by revisions to global growth forecasts. This theme delivered a really negative performance of -27.0%, lagging behind the benchmark index for global equities (-14.9%).
Theme 5. From monetary to fiscal policies: opportunities in infrastructure spending	The sectors of the economy relating to this theme also suffered from substantial downward growth revisions and announcements of government Capex plans with no precise details. This theme shed a substantial 28.0% while the global equity index lost 14.9%.
Theme 6. The environment and the future of our planet: focusing on water and waste management	Themes linked to the environment held up nicely. Investors seem to be convinced that these themes offer more stable trends. The theme posted an absolute performance of -7.4% whereas its benchmark index for global equities was down 14.9%.
Theme 7. Investing in human capital: 'Best employers', education and healthy living	This theme, which is part of the UN Sustainable Development Goals, also held up better. Investors seem to be looking beyond the present crisis to the long-term trends. The theme recorded a performance of -10.2%, thus better than global equities (-14.9%).
Theme 8. Benefiting from disruption: 5G and Artificial Intelligence innovations	Less-adverse investors were selective, above all by favouring themes linked to new technologies and innovation. The absolute performance of this theme (-8.2%) thus outperformed global equities (-14.9%).
Theme 9. Consumers become 'hyper-connected': new trends in digital consumption	The digital consumption theme attracted even more investors than theme 8. Indeed this theme posted a positive performance (+0.3%), particularly thanks to the success of blockbuster stocks such as Amazon and Ebay. Here again, the performance must be compared with the benchmark (-14.9).
Theme 10. Innovations in health care: technology multiplies discoveries and new applications	The theme linked to the health care sector posted the strongest performance in the list of 10 themes, both in absolute and relative terms (+1.8% year-to-date versus -14.9% for the benchmark index).

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