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Investment Strategy

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. New lockdowns in Europe are changing the shape of the economic recovery that we now forecast as a W (instead of a U). But the hypothesis of a rebound in growth in 2021 remains intact, as lockdowns are less harsh, and monetary and fiscal policy support remains massive.

. US elections: we are still waiting for the results of the presidential election.

. Investment strategy unchanged: take advantage of periods of doubt to reinforce positions in risky assets

The new lockdown and our global economic outlook

The deterioration regarding new Covid-19 infections, hospitalizations (especially patients in intensive care), and the rising death toll in Europe led governments in France and Germany to order new national lockdowns on 28 October. Other European countries, such as Italy, Switzerland and the United Kingdom, have taken similar decisions in the last days, because their health situations are alike. Governments are seeking to have a more limited impact on the economy than during the first lockdown so the impact should be less severe. But the recessionary impact will be harsh on the service sectors, especially tourism, hospitality, air transport, restaurants/catering, etc. Moreover, economic agents have been through this situation before, so the adjustments will be less difficult to make. Furthermore, in the industrial sector in particular, activity picked up well in the third quarter thanks to the economic recovery in China, and in Asia generally. The shock will thus not be as synchronized in the fourth quarter as it was during the first lockdown. Therefore, we are not changing our overall scenario of a rebound in growth in 2021, but rather the shape of this rebound in 2020. We are no longer talking of a U-shape recovery, but a W. The third quarter is stronger than expected, notably thanks to China, while the fourth quarter will be weaker, particularly due to Europe. In the United States, we do not call into question the strength of the economy at this stage of the pandemic.

Economic policies offer key support for next year

There will be renewed measures on the economic policy front to limit the damage in key sectors. Monetary authorities will maintain (or even intensify) massive liquidity injections and quantitative easing. These bond-buying programmes in the markets could be increased and extended. The ECB meeting on 29 October did not lead to major changes. The Governing Council presented a more cautious economic outlook, with risks having shifted. In our view, an extension and increase in the size of the PEPP remains the mostly likely course of action for December, but the press conference suggested a higher chance of further options being activated. On the fiscal front, President Macron has maintained the “whatever it takes” approach: fiscal stimulus will remain key in Europe over the coming quarters. Similarly in the United States, we have no doubt that the Fed will pursue its monetary accommodation policy. After the elections, a new stimulus plan will most likely be voted.

The US Election

At 8am (Paris time) on Wednesday, 4 November, the outcome of the presidential election is highly uncertain because it will depend on a few swing states, so we may have to wait a few more days. At this stage, it would appear that Republicans will narrowly keep control of the Senate. In any case, there is no 'Blue Wave,' i.e. a Democratic tidal wave that the polls had predicted; the United States will not implement a big stimulus policy through infrastructure spending, financed by a tax hike, which is at the top of the Democratic agenda, hence the drop in US long rates that we are seeing this morning. The impact on equity markets is more unclear, and we will need to wait for the final outcome, which will hopefully be announced soon. The dollar is bouncing back in the face of this uncertainty and is playing its role as a safe-haven currency.

Take advantage of volatility

Despite a lack of positive drivers, the presence of political and coronavirus-related risks, as well as technical headwinds, equity markets were very resilient until the last week of October. The expectation and announcement of lockdown measures has led to a generalized market correction. The MSCI world index and S&P500 stand about halfway between the 50 and 200-day moving average. We think that the 200-day curve should offer a key support. Indeed, investors have not been too concerned by the US elections beyond short-term uncertainty. The second wave of the pandemic has become a threat for the economic outlook but as argued, the fact that the second wave is not synchronized and measures are more targeted suggest a much more limited impact compared with March. We remain optimistic on a US fiscal stimulus package even if the decision could take a number of weeks.

Finally, the earnings season has started with a large proportion of positive surprises, despite the fact that expectations had been brought to elevated levels. Consensus expectation for earnings in 2021 is a rate of growth of 29%. We see that as too optimistic. Given that the prospective PE of 19 times is already at its highest level since the tech bubble period, any disappointment could be a source of volatility. Beyond the questions about the timing of a wide distribution of the vaccines (and their acceptance), there is probably not enough consideration given to a coming wave of bad news regarding corporate restructurings and bankruptcies. Equity markets could be volatile in the coming weeks/months.

Investors should take advantage of volatility: any market movement towards the 200-day moving average should be used to buy. Above all because the world is on a recovery path, but also because high valuations limit upside potential and therefore require paying attention to purchase prices. Another reason is the dearth of opportunities in fixed income markets and a gradual rise in investor interest for assets that give protection to rising inflationary pressures. That is a more long-term consideration though.

We like US, EU, EM: China, Taiwan, India, South Korea, Singapore and Indonesia. We like Materials, Industrials, Pharma & biotech, Insurance, EU tech & EU energy.

Summary of our main recommendations

Asset class	View	Segment	View	Comments
EQUITIES	+	GLOBAL	+	• **Cracks are appearing in the resiliency of equity markets.** Downside risks should be limited by coming treatment/vaccine news, economic activity remaining positively oriented and a reduction in political uncertainties. • **Play the reflation game!** The 200-day moving average should be a good area where to practice the buy on dip approach. Fine-tuning purchase prices is important given that valuations limit the upside potential.
		MARKETS	+	• **US stocks remain among our favourites.** • **Attracted to the pro-cyclical profile of Euro Area stocks.** • **Positive on Emerging Markets,** based on a superior earnings growth profile and room for further re-valuation. Preference for Asian markets (China, Taiwan, South Korea, India, Singapore and Indonesia).
		SECTORS	+	• Positive on these pro-cyclical sectors: **Materials, Industrials and Insurance**. • Positive on this defensive sector: **Healthcare. (pharma and biotech)** • **In Europe:** positive on **Technology and Energy.**
BONDS	-	GOVIES	-/= +	• We are **negative on German govies**, whatever the maturity, and on long-term US govies. • We are **positive on the front-end of the US yield curve for USD-based investors** as short-term yields have limited upside. • We **are positive on periphery debt** (Portugal, Italy, Spain, Greece) **on a buy on weakness strategy**.
		INVEST. GRADE	+	• We **prefer corporate bonds** over government bonds. • We **like EUR and US IG bonds with a duration at benchmark** (5 and 8 years, respectively). • We are **positive on eurozone convertible bonds**.
		HIGH YIELD	=	• **We are neutral on both US and eurozone HY.**
		EMERGING	+/=	• **We are positive on EM local currency bonds,** for both USD and EUR based investors, and **neutral on EM hard currency bonds (sovereigns and corporates)**.
FOREX	/	EURUSD	=	Given the worsening environment in Europe, we believe in the USD strength short-term, and see further correction towards 1.16 before the resumption of the USD weakness near term.
		USDTRY	=	We see the Turkish lira remaining under pressure short term. We revised our 3 and 12 month targets to 8.20 and 8.00 respectively.
COMMOS	+	OIL	+	• As the Covid resurgence is threatening the demand recovery, the OPEC+ hinted that they will continue to balance the market. Reduced investments in the shale oil industry but also in classical oil fields will weight progressively on the supply and push crude price higher in 2021
		GOLD	+	• Gold fundamentals remain bullish as real interest rates should remain extremely low for longer. Gold is seen as a hedge against the depreciation of the fiat currencies due to excessive money creation. Expected trading range to for the coming 12 months: $1900/2100/oz
		BASE METALS	+	• Prices are underpinned by the economic rebound underway in China the leading buyer and by the pro-cyclical policies in Europe and US. The energy transition is supporting copper and nickel prices.
ALTERNATIVES	/	Alt. UCITS	/	• Positive on Relative Value, Macro and Long-Short equity. Neutral on Event-Driven.

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