Marketing material

Investment outlook for Q4/2020

Following our quarterly strategy review, we are adding to our equity positions, while trimming our fixed-income quota. Despite a global V-shaped economic rebound, most investors seem to remain rather cautious and underinvested, which leaves room for further stock market gains in the coming months. We also keep a big overweight in gold as an alternative safe asset in an era that prioritizes reflation.

Last week we concluded our quarterly tactical asset allocation review and set our investment positioning for the quarter. We present an overview of the discussions and adjustments.

Economic outlook: a global V-shaped recovery has become visible

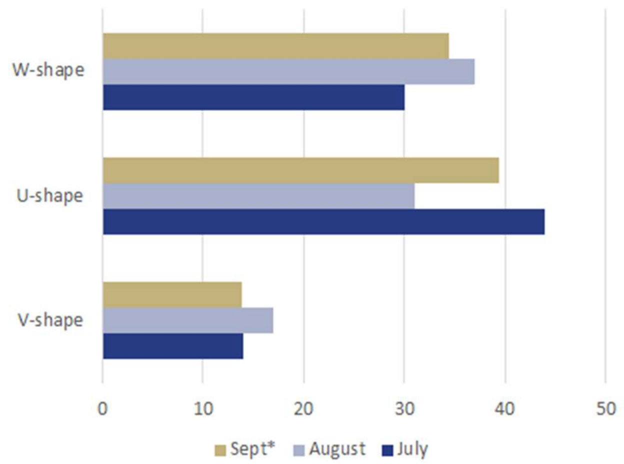
The past few months' economic data was stronger than expected, supporting the case of a V-shaped recovery. Pent-up demand with consumers and unprecedented support from governments and central banks have fueled an impressive rebound in numbers, ranging from retail sales to home buying to automobile production. The current economic activity indicators, which comprise a multitude of such high-frequency data, clearly illustrate that. Most major economies have been able to rebound in what is clearly a V-shape pattern (graph 1).

Graph 1
V-shaped economic rebound is visible around the globe
(Goldman Sachs monthly current economic activity indices)

Source: Bloomberg, Goldman Sachs, LGT Capital Partners

Looking ahead, the recovery could swiftly lead us back to above pre-crisis levels. The fact that most investors do not expect this (graph 2), insisting there is no V-shape recovery, only increases the room for positive market reactions if the recovery continues.

Graph 2
Only a minority of investors expects a V-shape
("What shape of economic recovery do you expect," %)



*Data for September are indicative, based on a Goldman Sachs poll. Data for August and July are from a Bank of America Merrill Lynch survey. Source: LGT Capital Partners

Granted, the continuation of the recovery depends primarily on the public health situation. The risk is that an effective and widely available vaccine fails to materialize such that parts of social life and economic activity might remain hampered for a longer period.

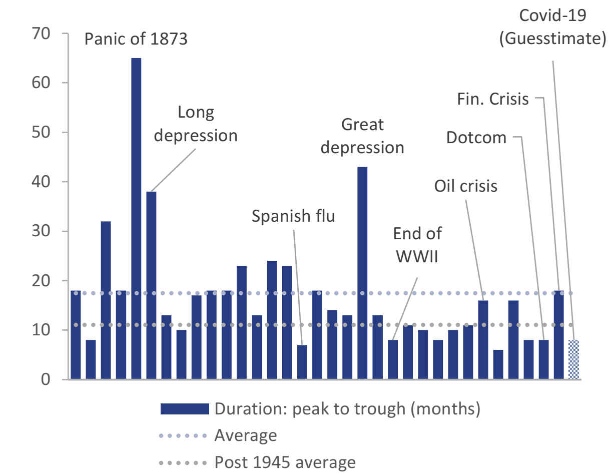
At the same time, economic policy will remain focused on providing monetary and fiscal support exactly for that reason, with policy makers in most advanced economies preferring to err on the side of largesse. In turn, this mitigates the risk of an extended public health crisis. On the other hand, while the worst of the economic damage caused by the pandemic and/or the lockdowns are behind us, some political event risks are emerging. In particular, financial markets could turn wobbly as the **US election date** (3 November) is drawing closer.

The most benign outcome would be a constellation wherein Republicans and Democrats continue to constrain and balance each other out, whether it is on tariffs, taxes or any other agenda. A blue or red sweep could thus be viewed as more problematic and increase volatility. By far the worst scenario would be a potentially contested election, with a prolonged period of political uncertainty. Although not very likely, it remains a tail risk at this point.

Meanwhile, the **European Union** has taken a big step towards fiscal union and hence alleviated the risk of fostering national breakaway longings. The long-decided separation of the United Kingdom and the union, meanwhile, is entering a critical phase. Recent British legislative plans to regulate matters of joint concern on the island of Ireland have increased the risk of a hard Brexit by the year's end.

In **China**, stimulus measures have probably peaked, as the cyclical economic normalization is at least a quarter ahead of the other major economies in terms of its return to growth. Lastly, many other **emerging markets** are running a precarious laissez-faire pandemic strategy, refraining from hard measures to contain the spread of the virus, as well as from injecting enough funds to support their economies. While our assessment of the emerging economies has also improved, we con-

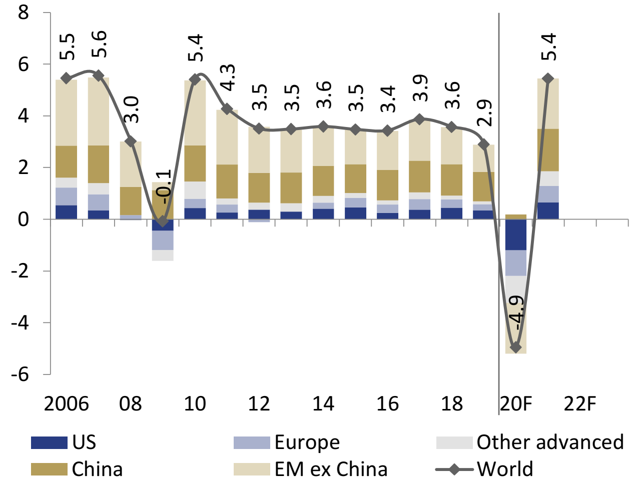
Graph 3
On track for a very short recession
(US recessions, National Bureau of Economic Research)



Source: NBER, LGT Capital Partners

tinue to view the developed markets as more attractive, due to the significantly higher level of economic support and the weight of crisis-resistant technology companies. Overall, the US economy is on track to register one of the shortest recessions of the past 150 years (graph 3), while China has already returned to a modest expansion. This sets the global economy up to the strongest growth rate since 2010 (graph 4).

Graph 4
Strongest growth in a decade due next year
(International Monetary Fund estimates, real GDP)

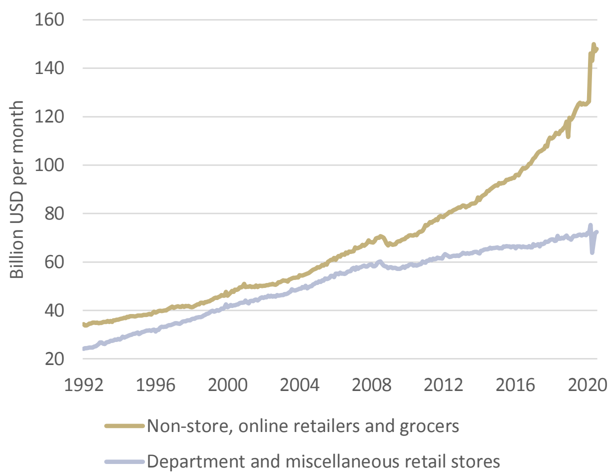


Source: International Monetary Fund, LGT Capital Partners

The pandemic made the strong even stronger

Formally, the longest bull market in history ended in the first quarter. From the viewpoint of the market's anatomy, however, the strong rebound since the March lows looks very much like a continuation of the preexisting risk-friendly regime. All the prevalent themes and drivers are ostensibly the same: full economic policy support, very low interest rates, the hunt for yield, the supremacy of the digitalization of business, and so on. Thus, the pandemic crash of February and March has not caused a paradigm shift, nor ushered in a new market regime. If anything, it has accentuated the old one. For one thing, there has been a clear divergence in the paths of online and highly digitized businesses on the one hand, and traditional store-based retail sales on the other (graph 5).

Graph 5
Digital economy emerged even stronger from pandemic
(Monthly retail sales in US dollars)



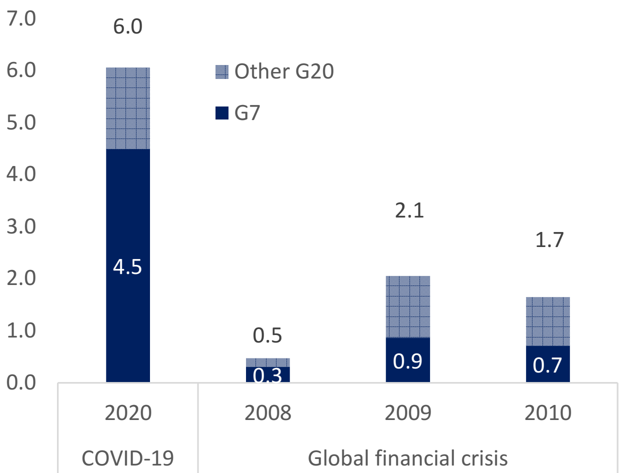
Source: Bloomberg, LGT Capital Partners

It is also worth noting that even traditional sales have returned very close to pre-pandemic levels. Due to their sheer size and scope, the effects of the global stimulus measures (graph 6) may well outlast the burden of the pandemic. Therefore, our market outlook is rather upbeat. We therefore assess the market recent weakness in technology stocks as a healthy correction of consolidation of this year's rapid gains, rather than a premonition of a bursting bubble.

Graph 6

Not messing around with deficit-spending this time

(Fiscal growth support programs, % of economic output)



Only government revenue- and spending-relevant items are considered. Credit and credit guarantees, which can become budget relevant later, are excluded. Source: International Monetary Fund, UBS AG, LGT Capital Partners

Investor cash positioning still near COVID panic peaks

Furthermore, despite the general run-up in prices and valuations, investors' sentiment and positioning in risk assets is cautiously optimistic at best – and certainly not outright bullish. In fact, the actual level of cash holdings of both retail and institutional investors in the US has barely declined by any meaningful magnitude (graph 7). Specifically, institutional investors' cash position peaked at $3.34 trillion on 18 May, and have fallen by $285 billion since (i.e. less than 1% of the S&P 500's market capitalization.

Hence, we are raising our equity holding to a moderate overweight, at the expense of fixed income. We also maintain our significant tactical position in gold. As a result, our model portfolio is fully invested (i.e. no cash reserves) and does not contain any tactical currency pair trades. In particular, going into the new quarter, we implement the following tactical positioning:

- **Equities overall are now at a modest overweight with a clear preference for developed markets.** We have added to our positions in US and European equities. In the medium to longer term, the leadership of US tech companies will likely remain a dominant market force, and we strive to continue participating in those structural themes. In the near term, however, the powerful economic rebound and the resulting steepening of yield curves could support a rotation into more traditional cyclical sectors and value stocks, which have hitherto lagged. The latter argument favors investment in the European indexes, among others. Conversely, we keep equities in emerging markets at a small underweight. These economies continue to face headwinds due to inadequate crisis responses (with some notable exceptions in Asia), while valuations are not very compelling when compared to the developed markets.

Graph 7

Investors remain skeptical: record high liquidity levels

(Billion US dollars, weekly data)

Source: Bloomberg, Federal Reserve, LGT Capital Partners

- **In fixed income, we remain underweight duration, corporate credit and emerging market sovereign risk.** The investment grade holdings (governments and corporates) have risen in value in recent months. We have now trimmed these investments again to finance our equity purchases, and because the macro policy outlook favors somewhat steeper yield curves. Our fixed income team, meanwhile, is taking profit on their overweight of inflation-linked issues. This step comes on the heels of a phase of strong performance relative to nominal bonds. However, the long-term inflation potential still warrants an anchor allocation to linkers in our view. Lastly, corporate bond issuance has set records this year as companies built up a cash cushions to weather the public health-induced activity crisis. As a result, the lower spreads, or risk premia, combined with the higher default rates, and the scaling back of central bank purchases as the worst of the pandemic shock has fades, prompt us to remain underweight for now.

- **In currencies, we take no active position this time, but retain our long-standing tactical position in gold.** Gold serves us as a portfolio diversifier in the case of unforeseen geopolitical events, general risk-off periods, as well as possible spikes in inflation expectations. It also serves as an alternative store of value, as current central bank policy keeps fears of classic currency debasement alive.

END OF REPORT

LGT Capital Partners: tactical asset allocation

The tactical asset allocation (TAA) is set quarterly with a time horizon of up to six months and adjusted in the interim if necessary; it shows our current positioning versus the strategic allocation (SAA) of the LGT Endowment, or Princely Strategy.

- **Equities: raised to a moderate overweight in favor of developed markets, in particular the US**
- **Fixed income: further cut in duration, corporate credit and emerging market debt, partly to fund equity position**
- **Alternatives and currencies: big tactical position in gold maintained, but no active currency positions**

	Asset class	SAA	underweight ----	---	--	-	Tactical allocation versus SAA +	++	+++	overweight ++++
Fixed income	Short-term investments	0.0%								
	Investment grade bonds*	24.0%		■	■	■				
	High yield bonds	5.0%			■	■				
	Emerging market bonds	7.0%			■	■				
Equities	Global defensive	7.5%								
	Global developed	23.5%								
	North America						■	■		
	Europe	*1.0%*					■			
	Japan	*0.0%*					■			
	Emerging markets	*6.0%*			■	■				
Alt. / Real	Listed private equity	4.0%								
	Hedge funds	12.0%								
	Insurance-linked securities	*6.0%*								
	Real estate (REITs)	*5.0%*								
	Gold	*0.0%*					■	■	■	■

	Currency[2]	SAA	----	---	--	-	+	++	+++	++++
Currencies	USD	87.0%								
	EUR	0.0%								
	CHF	0.0%								
	JPY	0.0%								
	AUD	1.0%								
	NOK	0.0%								
	Others	12.0%								

Reference portfolio: LGT GIM Balanced (USD). The TAA is valid for all similar portfolios but various restrictions or liquidity considerations can lead to deviations in implementation. In currencies, "others" represents indirect exposures resulting from unhedged positions in markets against the base currency. * Includes global government, inflation-linked and corporate bonds.

Performance of relevant markets

		1 month	3 months	Year to date	3 years, p.a.[1]	5 years, p.a.[1]
Fixed Income						
Global government bonds	USD	0.0%	0.6%	5.9%	5.3%	4.5%
Global inflation linked bonds	USD	0.4%	2.2%	3.5%	3.4%	3.3%
Investment grade corporate bonds	USD	0.3%	2.4%	5.9%	5.2%	4.7%
High yield bonds	USD	0.6%	5.6%	1.5%	4.1%	6.2%
Emerging markets [2]	USD	0.1%	3.3%	-1.2%	2.1%	5.7%
Equities						
Global	USD	-0.5%	8.5%	0.8%	8.2%	9.9%
Global defensive	USD	-0.8%	5.4%	-3.0%	6.9%	9.3%
North America	USD	-0.8%	10.7%	5.0%	11.6%	12.7%
Europe	EUR	0.7%	4.7%	-9.3%	1.1%	4.7%
Japan	JPY	0.5%	4.2%	-3.2%	2.9%	4.2%
Emerging markets	USD	0.0%	11.6%	-0.4%	2.1%	8.7%
Alternative and real assets						
Listed private equity	USD	-2.3%	5.5%	-10.4%	4.5%	7.9%
Hedge funds	USD	2.0%	5.9%	-1.2%	1.7%	2.2%
Insurance linked securities (ILS)	USD	1.0%	3.5%	4.7%	5.2%	4.0%
Real estate investment trusts (REITs)	USD	-0.8%	0.9%	-11.2%	2.6%	5.9%
Gold	USD	0.1%	12.8%	28.3%	13.5%	11.9%
Currencies (vs. rest of G10) [3]						
US dollar	USD	-0.2%	-4.4%	-1.9%	1.7%	0.2%
Euro	EUR	0.0%	1.4%	4.5%	1.6%	1.3%
Swiss franc	CHF	0.0%	0.8%	5.2%	4.0%	1.7%
Japanese yen	JPY	0.4%	-3.0%	0.8%	3.2%	3.1%
Australian dollar	AUD	1.5%	2.0%	2.2%	-1.8%	0.7%
Norwegian krone	NOK	-1.5%	3.2%	-4.4%	-3.2%	-1.9%
Emerging market currency index [4]	USD	1.2%	0.2%	-9.5%	-7.8%	-3.9%
British pound	GBP	-2.2%	-1.8%	-5.2%	0.2%	-3.8%

[1] Annualized return [2] Equal-weighted hard and local currency total return indices [3] Bloomberg correlation-weighted currency indices of a currency versus its nine major counterparts [4] J.P. Morgan Emerging Market Currency Index Live Spot in USD | Source: Bloomberg

Economic and corporate fundamentals

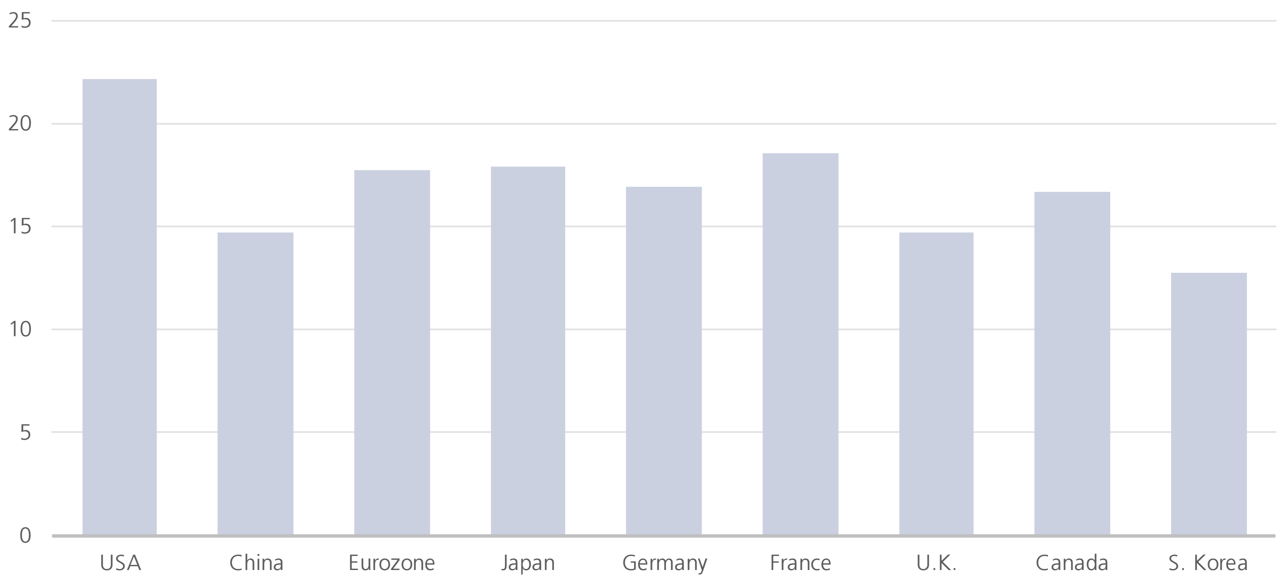
		USA	China	Eurozone	Japan	Germany	France	U.K.	Canada	S. Korea
Gross domestic product (GDP)										
Nominal, this year[1]	bn USD	22,322	15,270	13,678	5,413	3,982	2,772	2,717	1,812	1,627
Per Capita, purchasing power parity[1]	USD, PPP	67,427	20,984	40,965	46,827	55,306	48,640	48,169	52,144	46,452
Real growth this year[1]	Consensus	-4.6%	2.1%	-8.1%	-5.5%	-6.0%	4.2%	-10.0%	-6.5%	-1.0%
Real growth next year[1]	Consensus	3.7%	8.0%	5.5%	2.5%	5.0%	-5.3%	6.4%	4.8%	3.2%
Real growth current quarter	Annualized	-31.7%	54.6%	-39.4%	-28.1%	-9.7%	-13.8%	-20.4%	-38.7%	-3.2%
Unemployment this year	Consensus	8.5%	4.2%	8.1%	3.0%	6.0%	8.5%	5.7%	9.6%	4.1%
Inflation this year	Consensus	1.1%	2.7%	0.4%	0.0%	0.5%	4.8%	0.8%	0.7%	0.4%
Purchasing manager index (comp.) [2]	Neutral: 50	54.6	55.1	51.9	45.2	54.4	49.8	55.2	55.1	48.5
Structural budget balance/GDP	IMF	-6.3%	-6.2%	-0.9%	-2.1%	1.0%	-2.5%	-1.4%	-0.8%	-0.3%
Gross government debt/GDP	IMF	108.0%	60.9%	82.3%	237.6%	55.7%	99.2%	84.8%	85.0%	43.4%
Current account balance/GDP	IMF	-2.6%	0.5%	2.6%	1.7%	6.6%	-0.7%	-4.4%	-3.7%	4.9%
International currency reserves	bn USD	43.4	3,164.6	408.8	1,315.4	37.3	53.3	137.0	77.5	398.6
Govt bond yield 2yr [3]	% p.a.	0.13%	2.81%	-0.61%	-0.12%	-0.72%	-0.66%	-0.13%	0.26%	0.82%
Govt bond yield 10yr [3]	% p.a.	0.67%	3.11%	-0.26%	0.02%	-0.49%	-0.21%	0.18%	0.55%	1.51%
Main policy interest rate [4]	% p.a.	0.25%	4.35%	0.00%	-0.10%	0.00%	0.00%	0.10%	0.25%	0.50%

[1] IMF estimates [2] Manufacturing PMI for Korea [3] Currency swap rates for China and Brazil and closest ESM/EFSF bond for Eurozone [4] Max target rate for Fed

		USA	China	Eurozone	Japan	Germany	France	U.K.	Canada	S. Korea
Exchange capitalization*	bn USD	36,103	15,132	7,884	6,111	2,342	730	2,742	561	1,934
Growth in earnings per share, estimated (MSCI)										
12 months forward / trailing 12 months	Consensus	21.0%	30.5%	165.1%	49.1%	140.2%	142.3%	603.5%	35.3%	74.8%
Next fy / 12m fwd	Consensus	6.8%	6.1%	11.0%	17.1%	10.5%	13.6%	10.8%	7.1%	10.0%
Growth in revenue per share, estimated (MSCI)										
12m fwd / trail 12m	Consensus	6.1%	21.8%	2.5%	3.4%	7.5%	-0.3%	-1.0%	-10.6%	4.4%
Next fy / 12m fwd	Consensus	2.5%	4.2%	3.5%	3.7%	1.8%	2.4%	3.7%	0.1%	2.6%
Valuations (MSCI)										
Price-Earnings Ratio (est 12m fwd)	Consensus	22.1	14.7	17.8	17.9	17.0	18.6	14.7	16.7	12.7
Price-Sales Ratio (est 12m fwd)	Consensus	2.5	1.6	1.1	0.9	0.9	1.2	1.1	1.9	0.8
Dividend yield	Consensus	1.7%	1.7%	2.7%	2.3%	2.5%	2.7%	3.9%	3.3%	2.0%

* China market cap includes Hong Kong | Source: Bloomberg   Data per: 15.09.2020

Price earnings ratios based on expected earnings



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