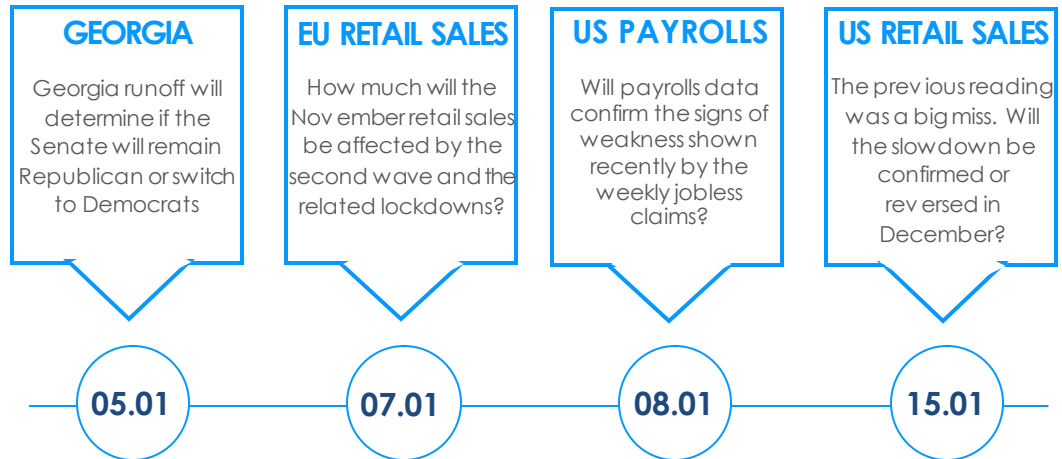


Main Events

Azimut Global Network

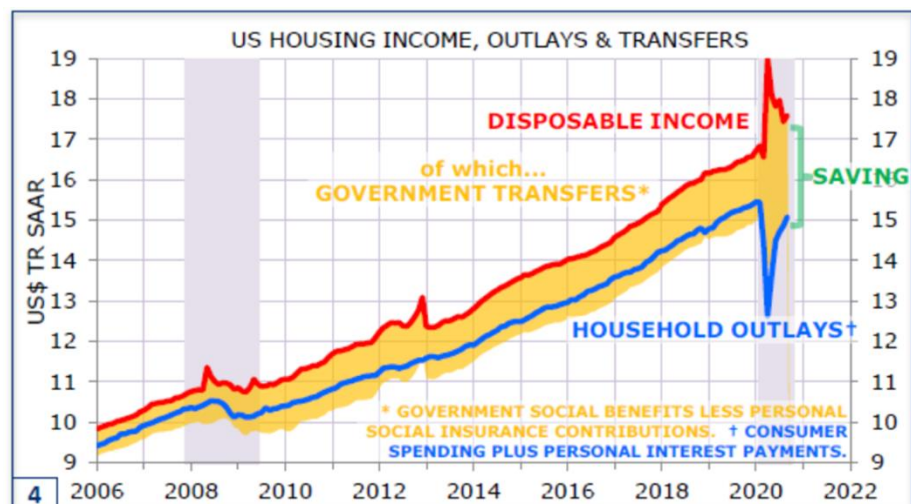
- * Milan
- * Abu Dhabi
- * Cairo
- * Dubai
- * Dublin
- * Hong Kong
- * Istanbul
- * Lugano
- * Luxembourg
- * Mexico City
- * Miami
- * Monaco
- * New York
- * Santiago
- * São Paulo
- * Shanghai
- * Singapore
- * Sydney
- * Taipei



Rates free to move

The end of the long term decline in risk-free rates has been called countless times in recent years and has never materialized. While saying "this time is different" often turns out to be wrong in finance, there are several reasons currently suggesting that in the near future it's better to remain more vigilant than ever.

Minimizing the aftermath of the pandemic as much as possible can be said about the first fact because first time ever governments have resorted to massive direct transfers on a large-scale in support of individuals and corporations. This new policy tool has been implemented significantly more aggressively in the US than elsewhere to the point that US disposable income has increased dramatically instead of declining as in traditional recessions. This, coupled with the sharp drop in spending due to the lockdown allowed individuals to accumulate an impressive amount of savings that will allow for a sustained pick up in spending once the pandemic will be over.



Source: DoubleLine, Miniac

(continued)

This policy tool is much different from the “usual” stimulus measures of the past decade; the QEs. QEs effects remained mostly confined to financial markets with the effect of driving assets prices higher and higher. Instead of increased consumptions and higher CPI inflation, QEs led to asset inflation (and increased income and wealth inequality), but had limited positive effects on the real economy.

Government transfers should have a much more immediate and concrete effect on the economy. Thanks to the weekly payment of \$600 per person granted for most of 2020 (lowered to \$300 for the first quarter of 2021) and to the extraordinary PUA and PEUC jobless claims, most of the people received much higher compensation this past year than before the pandemic. Those earning the minimum wage saw their monthly income more than double. Putting money directly into people’s pockets will almost certainly lead to a pick-up in consumption. Also, it must be considered that the propensity to consume is higher in the lower income class. And higher consumptions typically result in higher inflation.

The rise in inflation will also be supported by recent increases in commodity prices. After the sharp drop following the first lockdowns, commodities entered a strong bull market. As the bottom in commodities occurred between March and May, starting from the second quarter 2021 the YoY increases will be substantial. Using Brent as a reference and not WTI (as WTI dipped as low as minus 40\$/bbl), we can see from the chart below that oil prices almost tripled from the lows and are up more than 70% vs. the average of the worst three months. If we look at industrial metals (copper, zinc, nickel, aluminum - no chart presented) YoY increases from the low ranges from +40% to +70%. Such increases will certainly put some upward pressure on inflation. And higher inflation will in turn put pressure on long term rates.

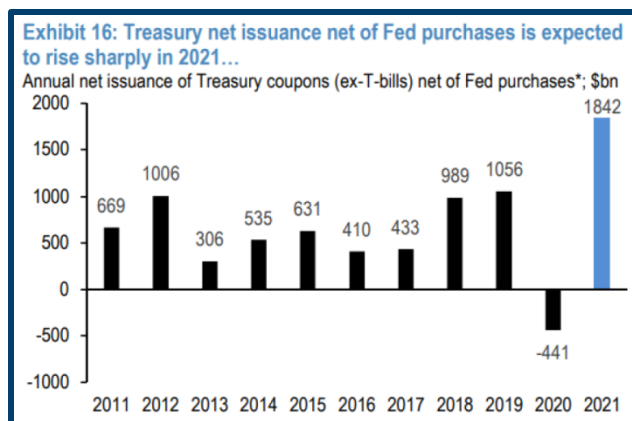
However, long term rates are not only threatened by higher inflation driven by a consumption and the commodity boom. Due to the swelling fiscal deficits (\$3.3 trillion in 2020) and the relatively modest QE by the Fed (80 billion of Treasury purchases per month) next year the market will be asked to absorb more than 1.8 trillion of Treasury bonds which constitutes the largest ever yearly net issuance. This again will put pressure on the US curve.

The picture is materially different in Europe, where the ECB is expected to monetize the entire net issuance of European government bonds through QEs.

It should also be considered that if the consensus baseline scenario (rapid vaccine rollout leading to herd immunity, full reopening of the economies, resumption of employment and consumption) will effectively take place, it is reasonable to expect that central banks will have to phase out the recent massive monetary stimulus making government bonds vulnerable to corrections, and hence rates to increases.



Source: Bloomberg

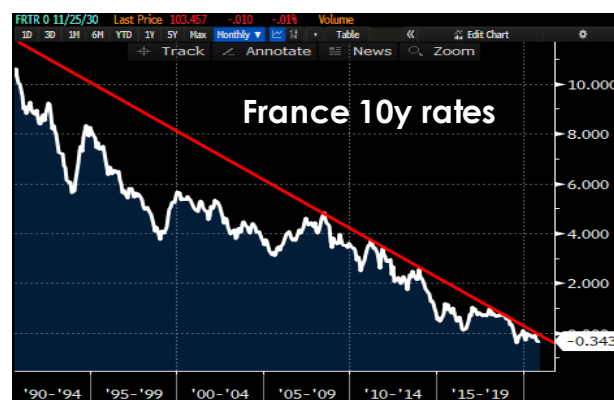
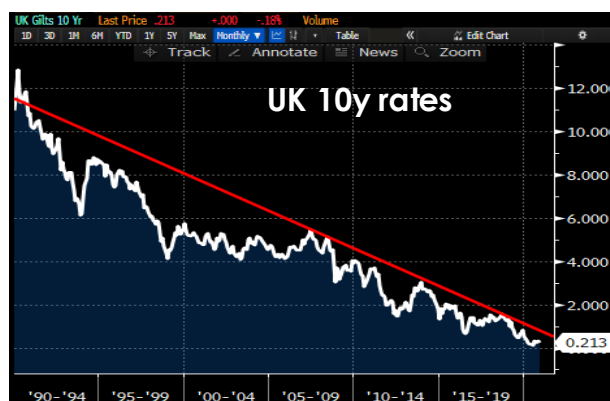
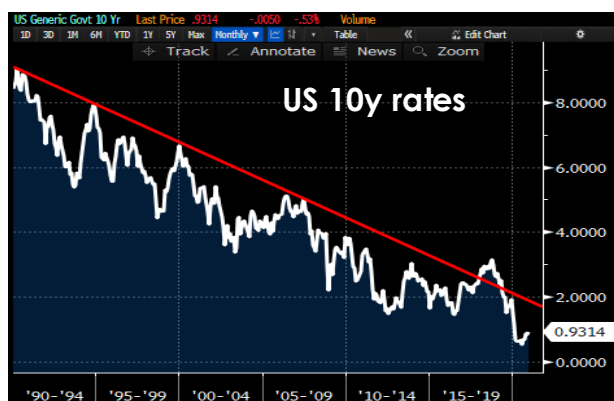


Source: DoubleLine, JPMorgan, Federal Reserve, US Treasury

(continued)

The issue is that even a small increase in European rates may trigger the breakout of long-term downward trendlines that have repelled any attempt of trend reversal in the past decade. From a technical analysis standpoint any breach of those long-term trend lines can trigger major sell-offs in government bonds (with rates moving higher).

The picture is quite different for the US where that downward trendline was breached in 2018 when the Fed attempted to normalize rates as the economy was progressively reaching full employment. At that time the equity markets negatively reacted to the higher rates and the Fed was forced to take a U-turn. The trade war with China and the pandemic led to a further drop in the 10-year US rates. As a consequence, now there are no major resistance near the current level of US rates.



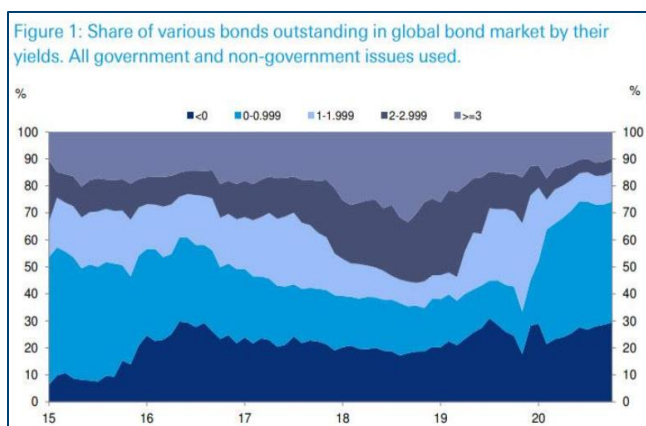
Source: Bloomberg

Should market participants actually begin to fear an increase in risk-free rates, the demand for duration hedging (i.e., opening short positions on long term government bond futures) may be massive.

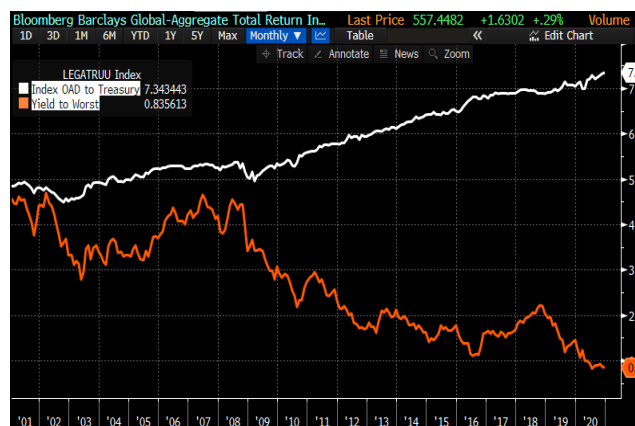
Due to the extraordinary interventions by central banks during 2020, yields have never been so compressed. The chart on the next page shows that as of today about 30% of all outstanding bonds have negative yields. To the contrary, the proportion of bonds yielding more than 2% is as little as 15% (and only 10% of bonds yield more than 3%).

The second chart on the next page shows the duration and yield to maturity of the Barclays Global Aggregate Bond Index, the broadest benchmark for fixed income, which includes all government and corporate bonds of developed market issuers. With a duration of 7.3 years and a yield of 0.8%, should rates increase by 1%, the 1 year total return on such a portfolio will be a loss of 6.5% (-7.3% due to the duration component, plus 0.8% deriving from the yield to maturity at the time of the purchase).

(continued)



Source: Bloomberg Finance LP, Deutsche Bank



Source: Bloomberg

According to the International Capital Market Association, as of August 2020 the overall size of the global bond markets in terms of USD equivalent notional outstanding is estimated to be approximately \$128.3 trillion (source: <https://www.icmagroup.org>). These figures do not include fixed income derivatives.

Considering the total size of the bonds market, even if a limited portion of market participants decide to hedge part of their duration risk, the flows they could generate may easily outweigh any central banks' purchases through QE.

If the baseline scenario effectively take places, we could be in an unprecedented and never before seen situation as we had many powerful triggers for higher rates altogether: 1) government transfers directly to citizens, which should translate in a consumption boom 2) substantial increases in commodities 3) central banks that could be forced to phase out monetary stimulus 4) potential breakout of long term downward trendlines in 10-year rates 5) demand for duration hedging.

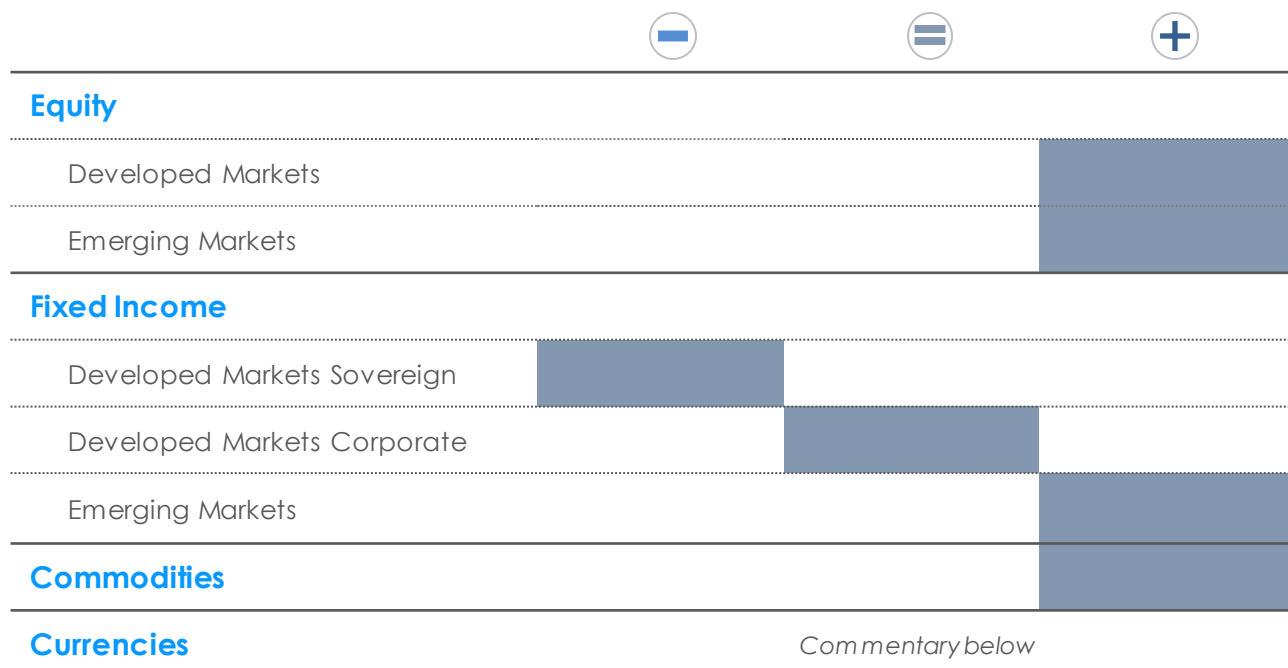
Since the risk-free rates are the basis for correctly pricing every other asset class, keeping an eye on their behavior is of the utmost importance.

For equities, increases in long term rates will put downward pressure on prices. As Powell recalled in his latest post-FOMC conference, absolute valuations are quite expensive, but the equity risk premium is still at a normal level. If the long-term risk-free rates move significantly higher, stocks may be vulnerable to corrections (even with strong GDP numbers) in order to keep the equity risk premium unchanged.

Most importantly, if rates rises and the base-case scenario unfolds, we could assist to significant rotation in market leadership. Over the past few years, characterized by decreasing rates and GDP contracting, we have had US, mega cap, and the so called "long duration equities" (like tech, consumer discretionary, etc.) largely outperforming the rest of the markets. If we move to a scenario where rates will rise and economic activity will strengthen, then Europe, emerging markets, value/cyclicals and small-cap may be the best performers.

This doesn't mean that we need to aggressively rotate the portfolios right now. As of today there are many lockdowns in place, vaccine rollout has just started and consumer confidence is still at low levels. Currently, we just need to be aware of what may happen and be ready to act if and when there will be more clarity. As uncertainty is still very high, the best advice for the moment is to be as much diversified as possible.

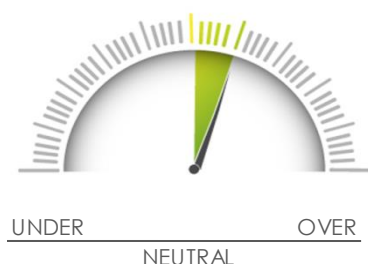
Asset Allocation View



⊖ UNDER
= NEUTRAL
⊕ OVER

Equity

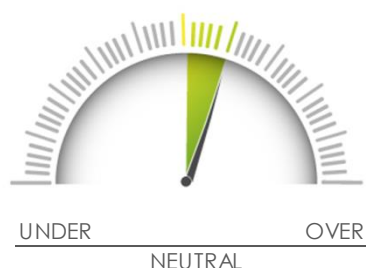
Developed Markets



We keep our stance on Developed Markets Equities as slightly positive. We still recommend to increase equity exposure, should a decent correction occur, as the long term constructive view on equity remains unchanged. There are several catalysts which could ingenerate such retracement, like heightened risk of new lockdowns in Europe, overbought conditions and extremely bullish sentiment. In case Democrats win both seats in the Georgia's run-off, then a further leg up in the US markets is to be expected. However, in this scenario the USD may weaken, therefore the US outperformance could be dented by the greenback depreciation.

US =	Europe =	Japan =
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Emerging Markets

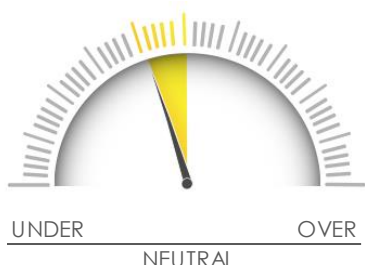


We keep our slightly positive recommendation on Emerging Markets unchanged. Even if, in the short term, the overbought conditions may lead to potential retracement, the expectation of a rebound in global growth will propel EM GDP growth. Currently we keep an equal recommendation across EM. Emerging Europe and Latam will be more volatile and sensitive to both the acceleration in global GDP growth and the demand for commodities. Asia is expected to continue its steady growth path. Democrats winning both seats in the Senate run-off should lead to a weaker dollar, which would make Emerging Markets equities more appealing.

Asia ex-Japan =	EEMEA =	LATAM =
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Fixed Income

Developed Markets Sovereign



We kept our slightly underweight recommendation for Developed Markets sovereign bonds. We expect that the short end of the curves will remain fairly anchored, while the long end could be more exposed to the risk of rising yields considering the risk of a spike in inflation amid the pick up in consumption. In case of Democratic victory in Georgia we expect that the US Treasury could suffer with yields rising in expectation of additional fiscal deficits.

EU Core



EU Periphery



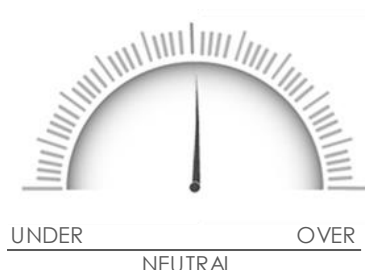
US Treasury



Japanese JGB



Developed Markets Corporate



We kept our recommendation on Developed Markets corporates as neutral. High grade bonds' spreads have compressed substantially and now yields are barely above that of sovereign bonds. At the same time the duration of IG benchmarks is very high usually around 7-8 years. This means that there's a concrete risk of capital losses should rate starts to rise, which is not adequately compensated. There are still opportunities in the segment between investment grade and high yield, in particular in subordinated bonds.

IG Europe



IG US



HY Europe



HY US



Emerging Markets



We kept our bullish recommendation on the asset class. EM bonds should benefit from the expectation of a vaccine driven strong global economic recovery. Moreover, the environment of USD18 trillion of negative yielding debt should bode well for EM bonds, especially considering the chase for higher yields. It is projected that EM bonds could benefit both from a spread compression and a recovery in the value of their currencies.

Local Currency



Hard Currency IG



Hard Currency HY



Commodities



We maintain our bullish view on the asset class. Precious metals could be sustained by the ample liquidity and could serve as a hedge against the debasement of most currencies after the massive monetary interventions of this year. Energy and industrial metals should benefit from the expectation of a quick and prompt recovery as soon as the vaccines are distributed that will enable people to return to pre-Covid-19 living conditions.

Precious



Energy



Industrial



Currencies

We maintained our neutral view on the Euro after the recent appreciation. In the short term further lockdowns in Europe are the main reason that may be used as an excuse for profit taking. Instead, a Democratic victory in the Georgia run-off should lead to an appreciation of the euro vs the US dollar.

We keep the view neutral also on the USD. As detailed just above, the main driver of the USD in the short term will be the outcome of the election in Georgia.

We kept the neutral view on the Japanese Yen as the country may attract foreign investments if the focus on value stocks, which are well represented in the main equity indices, continues in the near future.

On Emerging Markets currencies, we maintain our positive view considering that any episode of short term volatility will not change the long term positive perspectives for the asset class.

Euro		USD		Yen		Emerging	
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