

2021 THE YEAR OF RECOVERY

Developed Equity Committee – 2021 Outlook

Recovery

Is going to be the key theme of 2021. After one of the deepest recession in modern history the global GDP is set to regain some of the lost ground next year. Thanks to vaccinations and therapeutics being gradually distributed in the United States and Europe, the end of the health emergency appears to be in sight. The spending measures committed by the governments will do the rest in supporting the economy until there is a greater sense of normality. The jury is out, though, on what the pace of the economic recovery will be because much of it will largely depend on how fast the pandemic will be brought under control **[Saverio Papagno (Luxembourg)]**: “Our base case scenario is for herd immunity to be reached in the developed countries sometime around the summer. This will require a significant effort both in building the supply needed as well as the logistics, but we are confident that the G7 countries will succeed in this task. The gradual lifting of restrictions will kick start the rebound in GDP growth.”



Saverio Papagno
Senior Portfolio Manager
LUXEMBOURG

Consumption

[Giuseppe Pastorelli (Luxembourg)]: “Recovery will start from the Consumption picking up through a gradual global reopening of the economy. China, the first region to reopen, showed a remarkable and fast recovery on internal demand. But it was not just about China. During this summer even with limited mobility domestic demand was strong and up Year over Year both in US and in Europe. Due to the combined effect of total or partial lockdown that forced a reduction in consumption and the huge state transfers to citizens, total personal savings increased substantially bringing the US Real Disposable Income to above pre-Covid levels. This will allow for a strong future increase in spending.”



Giuseppe Pastorelli
Senior Portfolio Manager
LUXEMBOURG

Base Case

In 2021 the economic cycle will likely move from a recession period to a recovery phase. This will be characterized by a recovery in EPS driven by reflationary forces. US Dollar is probably going to remain weak and government bond yields will rise moderately. **[Marco Vironda (Luxembourg)]**: “The long-awaited rotation from growth to value could therefore materialize, but a fine balancing act is required. It will probably be more of a rotation from defensive into cyclical stocks. Growth stocks are incorporating structural winning companies that are less affected by the evolution of the Covid-19 crisis while cyclical value stocks are incorporating a lot of unprofitable companies in old and unsustainable



sectors. Therefore, a preference for quality is always warranted irrespective of the style and size characteristics.” **[Andrea Infurna (Luxembourg)]:** “The recovery pace from the last recession and reflationary pressures will drive the markets in 2021. Factor investing had been rewarding so far, leaving space for stock selection across different sectors. At the beginning of the cycle, the market rotation will face a challenging phase which will need support from the macroeconomic catalysts. Multi-factor approach is recommended in order to benefit from dynamic stock picking and avoid market peaks and concentrations which have been driving markets during the past few years.”

Deviations

From this base case scenario largely depend on two elements: how fast the pandemic will be brought under control and restrictions lifted and eventual path and scale of rising bond yields, if occurs.

A more upbeat scenario could unfold if the winter wave of Covid -19 ends up being milder than expected and the restrictions are lifted earlier than the market anticipates. Moreover the Democratic victory of the two Senate seats in Georgia on January 5th could lead to a stronger than expected fiscal impulse. Stronger than expected earnings recovery would boost small-cap and cyclically oriented stocks and we would probably see Europe overperforming US.

There are also some downside risks. If conversely the winter wave of Covid-19 turns out to be worse than expected resulting in forced new partial or total lockdowns, or the vaccines roll-out will be slower than projected, the expected recovery could be delayed. Under this scenario, we would probably see a negative performance of equity indices with US overperforming Europe, and large-cap defensive stocks overperforming the cyclical stocks.

A potential increase in long term risk-free rates can act as a headwind for equity markets. There are several factors that may contribute to this scenario. Firstly, under the base case assumptions described above, the economy will recover strongly with consumptions picking up thanks to the accumulated savings. This combined with the strong increase experienced in commodity prices since the 2nd quarter of this year may in turn lead to a higher inflation. Should this scenario materialize, some central banks may begin to consider a gradual exit from the ultra-accommodative monetary policies. In the context of rich multiples, this could put some negative pressure on equity indices.



Marco Vironda
Senior Portfolio Manager
LUXEMBOURG



Andrea Infurna
Portfolio Manager
LUXEMBOURG



Usa

[Saverio Papagno (Luxembourg)]: “We have a 4,000 year-end target for the S&P 500 under the Base Case scenario with a projected earnings growth of 21%. We favor a barbell approach applied to the equity portfolio that includes high quality Cyclical and secular winners, large caps and small & mid caps. For this reason, we prefer Consumer Discretionary and Industrials to find high quality cyclical companies and the Information Technology for many of the secular winners. We expect digitalization of the economy, both on consumption and production side, to remain as a key structural theme also in 2021. In particular, we expect digitalization to start developing beyond e-commerce and affect new areas like healthcare, manufacturing, and finance.”

Europe

[Andrea Abouchacra (Luxembourg)]: “We share the view of a progressive return to growth under the assumptions of a steady lifting of containment measures and a timely distribution of the vaccine. We expect the “out of home” service spending to accelerate throughout the year along with a recovery of businesses investments. Our base case scenario assumes a 30% rebound in European companies’ profits and a 435 target for the STOXX Europe 600 Index. Looking at broader sectors, we do have a preference for Industrials and Consumer Discretionary where Europe has a competitive edge in areas such as engineering and luxury goods amongst others.”

Italy

[Andrea Colombo (Milan)]: “We believe that Italian Equity markets are fairly priced; valuations on 2021 are not particularly compelling and earnings will still be around 20% below 2019 levels. We continue to see upside in the long term with possible positive revisions for earnings in 2022. We prefer companies with a global exposure (Industrials and Consumer Discretionary) to play macro themes like China’s recovery, US economic growth, and EU recovery Fund.”

Energy Transition

[Matteo Facchi (Luxembourg)]: “In 2021 we will see remarkable developments in the energy transition trends globally. We do expect further steps forward on the policy and financial support side with new targets and plans being adopted around the world, and an acceleration in the implementation of the ones already in place. In Europe for example the Green Deal is taking shape with the first actual projects awaited in 2021.

These kinds of measures also determine the rising power consumption expectations enhancing further investments themselves. We will see a supportive environment for green-related investments benefiting from a combination of growth and visibility rarely seen in the past.”



Andrea Abouchacra
Portfolio Manager
LUXEMBOURG



Andrea Colombo
Senior Portfolio Manager
MILAN



ESG

[Marco Vironda (Luxembourg)]: “Mitigating ESG related risks is a key part of the global government agenda and will drive further capital into sustainable initiatives, leading to a foreseeable rapid increase of ESG fund offerings across the asset management industry. This represents a fundamental shift of capitalism towards a more sustainable form.

To be considered a high-quality company not only requires a strong balance sheet and a superior business model, but also a high ESG rating. ESG improvers (companies that are showing positive ESG momentum) will probably represent the most attractive opportunity within every economic sector. This will allow to take advantage of the future ESG premium on companies that are increasing their ESG rating. A combination of ESG leader and ESG improvers will probably represent a powerful combination for every portfolio solution.

ESG is clearly becoming one of the most remarkable shifts for the whole financial industry, exactly like UCITS was for the harmonization of mutual funds products and their rapid adoption by every asset wealth manager.”



Matteo Facchi
Portfolio Manager
LUXEMBOURG



Andrea Rocca
Senior Portfolio Manager
IRELAND

M&A

[Andrea Rocca (Ireland)]: “The year 2020 saw a decline in merger and acquisition deals due to the Covid-19 pandemic. The risk of an increased corporate tax in the medium term could be the driver that will persuade many companies to sell and convince the healthy companies to accelerate their growth through an acquisition. M&A will be one of the key drivers of the markets, especially in the consumer field, where the earnings were hit harder, and in new technologies which have accelerated during the pandemic and have increased the appetite of growth towards big-cap.”

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