HYPOSWISS
ADVISORS

Review & Outlook
July 2020

Review and Outlook

-Review
-Fixed Income
-Equity
-Currencies
-Economics
-Commodities
-Outlook
-Asset Allocation

-Thematic Investment idea

Mission Statement

Contact

Disclaimer

Hyposwiss Advisors SA

www.HyposwissAdvisors.ch

Q2 2020 Review

The most hated rally of all times

To the surprise of most investors, the second quarter 2020 ended with the strongest rally of stock markets in decades and resulted in a V-shaped recovery of most equity indexes from their COVID-19 crash lows in March. After the first half of 2020 is finished, the MSCI WORLD is down by only -6.6% YTD and the S&P 500 by -5.5%. As previously, the NASDAQ Composite is outperforming all other indexes and is trading at +10.0% YTD, while European markets are still lagging (EURO STOXX 50 –13.7%).

After this impressive Q2 rally, the situation has become somewhat astonishing: The Nasdaq Composite trades at all-time highs, the S&P 500 is only a low digit number below its pre-crisis level and the current P/E ratio of the US market is in the top 10% of its history. All these figures are in sharp contrast to the US economy which is in its worst 10% historically. In addition, various uncertain future parameters are looming - market participants dislike uncertainty – and on top there are evolving second waves of contagion in many parts of the world. To summarize: One is tempted to conclude that stock markets and the economy seem to be in a complete mismatch of historic proportion. Many investors have for these reasons stayed on the sidelines and are waiting for a clearer overall assessment of future economic trends and that is why the Q2 rally is called by many 'the most hated rally of all times'.

If stock markets and the economy are really in a mismatch is difficult to judge as typically markets are always right. The new reality however is that equity markets do price in a very optimistic economic scenario with a V-shaped recovery of global economies – which is one likely way-out from the crisis, but far from sure – and a clear understanding that central banks will continue to help out in case of damages by printing more money. The possibility that the pandemic cannot be controlled as second or more waves

emerge or negative feedback loops from financial markets occur is not discounted in current stock prices. The recent surge in gold can be seen as an indicator that some investors are exactly betting on such an outcome.

Central banks have acted forcefully to calm disrupted Fixed Income markets in order to keep the flow of credit open. Unprecedented fiscal measures are deployed to combat the negative impact from the pandemic. This will lead to substantial increases in the debt/GDP ratios with all the potential negative long-term consequences (such as inflation).

S&P 500 Index – 01.01.2020 – 30.06.2020
Source: FIS Market Map

The gold rally continued in June 2020 when gold reached a new multi-year high of USD 1'774, the corona-crisis being the driving seat of the (narrow) gold market.

Fixed Income

The money printing presses are working hard

The world's central banks have provided a record USD 7.5 trillion of monetary stimulus to revive the corona-virus hit economies, which is equivalent to 13% of global GDP. These unprecedented actions have given a strong boost to almost all Fixed Income asset classes and yields in many currencies and maturities are at all-time record lows.

> "Luck shouldn't be part of your portfolio."
>
> Expect the expected

The US Fed has been by far the most expansive central bank, with its quantitative easing program now also encompassing corporate bonds. The total liquidity injection this year will amount to some USD 2.4 trillion, effectively financing about 60% of the government deficit, which could reach USD 4 trillion by end-2020. While USD benchmark interest rates are unlikely to fall below zero – like in Euro or Swiss Francs – it can be expected that the Fed will adopt a Japanese-style yield control curve policy.

The Eurozone was also supported by heavy central bank stimulus programs. The German-French proposal for a Euro 750 billion recovery fund has led the spreads on bonds issued by Italy, Spain and Portugal to narrow considerably. Euro sovereign debt and high rated corporate bonds have become unattractive with yields deep into negative territory.

Emerging market local currency debt remains an attractive alternative to the low or negative yielding traditional currencies. Emerging markets like South Korea, Brazil or Mexico have an average inflation of 2.5% - a record low – and in many cases their sovereign debt is much lower than in the developed world. We continue

to like this FI segment but generally prefer ETF's and funds compared to single bonds to better diversify the risk of individual issuers.

We were entering the crisis with a neutral allocation in the Fixed Income asset class in USD bonds. Considering that yields will remain low for a few years, we keep our allocation mainly for capital preservation purposes. Given the current interest rate situation, we consider TIPS (Treasury Inflation Protected bonds) as a possible shield and protection towards the inflation in the medium future.

In the High Yield (HY) space, we kept most positions but have eliminated those holdings in sectors which will likely suffer for many years due to the crisis, particularly airlines and certain oil companies. Similar to the equity market, the HY sector has in the meantime recovered from its lows and offers selective opportunities with a favorable risk/reward ratio.

Equity

What's next after the V-shaped recovery?

There were two main drivers for US equities – which were followed by all markets globally in different degrees – to surge in Q2 to end up in a V-shaped curve: The hope of an economic upturn in the run-up to the US Presidential election, as a result of the fiscal stimulus programs and the enormous liquidity that the Fed provided. Its chairman Jerome Powell has stated that the FED stands ready to buy as much debt as needed to support economic recovery. Stock markets reacted accordingly with the strongest quarterly gains in decades.

The next element to be followed will be the earnings season and it will be interesting to see whether earnings number will push the pandemic out of market focus. Overall, the motto for profit numbers is "how bad?", and the best outcome could be "not as bad as feared". The drop in earnings is expected at about -45% for S&P 500 companies compared to last year's Q2. Many seasoned CEO will take this opportunity to get rid of any legacy issues, such as goodwill or other intangible assets. Covid-19 will serve as an excuse for any clean-up whatsoever. The corporate guidance for the second half of the year – if they provide any – will be more relevant for the stock price reaction than the numbers of the past quarter.

Outside the USA, Europe was again lagging in Q2. Further east, in China, July 2020 started with an unexpected rally in both Hong Kong (H) and mainland (A) shares, driven by different factors: China reported strong PMI data in June (50.9), raising hopes of a sharp past-Covid recovery. The CSI 300Index broke through its old resistance levels, drawing retail demand. The pandemic health situation seems to be better in control than in the west and at last valuations

in China are much cheaper than in the USA: The CSI 300 Index members are trading at a forward P/E ratio of only 14x, whereas the USA MSCI is at 23x. We had a fairly high exposure to Chinese equities of 3-5%, depending on the risk profile of each profile and intend to increase it further over time.

We have entered this corona-virus market crisis with a neutral equity allocation. We did not sell positions during the panic selloff in March for our discretionary mandates and therefore fully participated in the V-shaped recovery. Going forward we intend to take some profits and re-allocate some positions into Asia / Emerging Markets and to future "trends and thematic investments", while a reduction of the European allocation is being analyzed.

Currencies

USD is losing its appeal

The appeal of the US dollar has lost momentum for three different reasons:

As lockdown measures are eased, the rebound of economic activity in the USA and in Europe appear to be in lockstep. Different economic indicators from both sides of the Atlantic confirm that growth seems to return at an equal rate following the relaxation of lockdown measures and is more in step than originally feared.

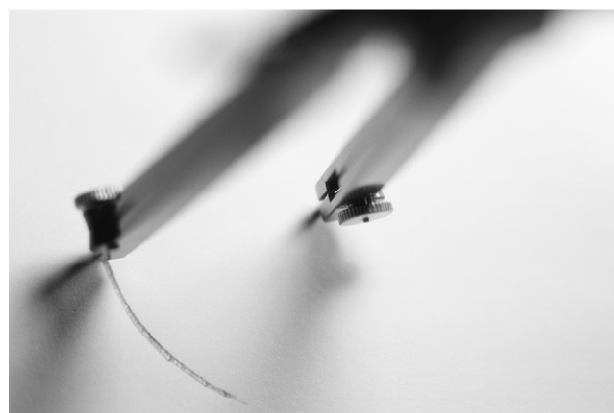
Secondly, the US Federal Reserve holds rates close to zero, and a restart of quantitative easing as well as guidance to control the front end of the yield curve limits the upside of the US dollar over the coming months. The interest rate advantage of the US dollar versus the Euro and the Yen, which was one of the main drivers of the dollar rally, has been reduced significantly but has not yet completely disappeared.

Thirdly, the USD is fundamentally overvalued, and the current account balance and the trade balance are both negative. These facts however are true already for many years.

The old reasons for the strength of the dollar however remain valid which are its status as a structural safe-haven currency and the superior profitability of US companies relative to the rest of the world, which serve as a magnet for capital.

To sum up, the USD is at a crossroad. It has been flat since Q1 2015, during which time it has made three attempts to start a new trend which all failed. It is too early to declare that the USD is heading into a secular downtrend but it's a possibility to be taken into account.

The Chinese CNY is in recovery mode, in line with positive signs of a continued economic recovery, plus the yield advantage towards other currencies as China has eased monetary policy less than other countries. Rising uncertainty in US-China relations offer downside potential for the CNY, and even long-term, independent of the US election result, the anti-China rhetoric in the US will likely persist, as the unfavorable view of China is bipartisan and widespread among American people.



Economics

Global economic activity is expected to recover during 2020

The Purchasing Manager Indices (PMI's) in most countries for both the manufacturing and the services sectors confirmed that economic momentum improved further in June, thanks to the easing of many of the coronavirus containment measures, lifting the global PMI to 47.8 (from 42.4 at end of May).

In the Eurozone, the final PMI data (47.4) came in stronger than the previously released figures and some parts of the economy have already returned to expansion.

In Asia, manufacturing activity is still subdued in most export-oriented countries, as weak global demand keeps production muted. The exception is China which is already in growing territory (manufacturing PMI at 50.9). The Chinese economy was dragged down by -6.8% y/y in Q1 2020, but its recovery has emerged quite swiftly, includes all important segments of the economy, and is clearly ahead of Europe and the US. China was first to enter the correction and is the first to exit.

The USA is also rushing ahead, with the manufacturing ISM shooting back up to 52.6 (from 43.1), despite rising virus cases in various states. In June, the US saw the strongest surge in new jobs in many decades, as previously shut-down services and goods producers stepped up their rehiring. The surge in new virus cases in some southern states and the following lockdowns however are an indication that the unemployment situation in the near future will not improve much further.

Overall, the global economy has definitely passed its April trough and the current data bodes well for a V-shaped recovery to emerge – similar to the stock markets – with growth resurfacing in Q3. However, most economies will not return to their pre-crisis output levels until late next year or even 2022. Should a second wave of contagions emerge, one can expect that most countries are better prepared now and the future containment measures will be better targeted and more specific, thereby reducing the risk of another economic paralysis.

Commodities

Oil: Back to normal

After reaching record lows during the heat of the corona-virus crisis, oil prices are trending sideways lately. The latest weekly US oil market statistics showed declining storage, rising refinery activity and normalizing road fuel use. On top, the distortive element of temporarily elevated Saudi crude oil arrivals at US shores is

dissipating, while oil product exports are picking up.

The corona crisis has offered some oil producers an opportunity to adjust their long-term price projections to reality. On a long-term view, oil demand is peaking globally regardless the current crisis and the real key for the future oil price will be at which level USA shale-oil production cost will stand (today around USD 50) as shale supply can adjust flexibly and responsively to oil demand swings, and therefore oil will most probably no longer trade much higher than this level.

Gold: The sky is the limit

Gold prices (XAU ounces) in USD – 01.01.2019 – 30.06.2020
Source: FIS Market Map

The corona crisis is the driving seat for the gold market and prices reached a high of USD 1'817 at the beginning of July. Maybe it is worth remembering that during the peak of the crisis in March 2020 and in-line with stock and bond markets, the gold ounce also took a dive to USD 1'460.

Safe-haven demand stays strong as gold continues to move in lockstep with real US bond yields, which fell to record lows, reflecting both growth worries and risk aversion. Gold enjoys upside momentum and trend followers and technical traders have entered the market.

Gold demand, in particular for jewelry, is weak indicating that the surge was done by investors willing to pay every price for the metal and pushing it easily trough the resistance level of USD 1'800. Maybe it is worth remembering that the global gold market is narrow compared to equity and bond markets and prices can be moved by relatively small amounts. Another figure to consider in this context is the gold production costs which vary between USD 700 in Peru and up to USD 1'400 in South Africa.

Gold could be in overbought territory but its outlook looks positive as it remains a good hedge against long-term inflation, historically trades upwards in times of low interest rates and is an insurance policy against geopolitical disasters. We held a gold position of 5-6% in our portfolios and intend to increase it to approximately 7% in due time. We think gold could retest the old highs of USD 1'920 (2011) within the next 12 months.

Outlook

Navigating through the second coronavirus wave

It must be assumed that second waves of the virus will hit most countries in different degrees. Luckily, treatment possibilities have improved over the past few months, as medical professionals have learned more about the virus. Hospitals have also built up capacity to deal with the influx of patients. Mask wearing also has become more common not just in Asia but worldwide which was one key reason why Asia suffered far fewer casualties than elsewhere.

All this suggests that while a second wave will weigh on global growth over the coming months, we are unlikely to see the sort of broad-based economic dislocations experienced during the first wave in March. However it will probably be several years before spending in the sectors most affected by the virus – travel, lodging, bars and nightclubs, big sports, etc. – will return to pre-pandemic levels.

Attention towards autumn will turn to the outcome of November's US presidential election. The market has probably not yet completely priced in a scenario with a Biden win and the Democrats taking control of the Senate. This could mean that Trump's corporate tax cuts would be challenged, which would lower the EPS for many companies. However it could also result in higher spending – resulting in a fiscal stimulus – and less trade tensions with China.

Equity markets will trade nervously over the coming weeks as second waves might emerge, but less because of disappointing corporate results in the upcoming earnings season as investors lock behind the current recession. TINA ('There Is No Alternative') rules on a longer-term view, as Equities offer a higher return mix than Fixed Income instruments which have negative real (net of inflation) returns.

We still like non-cyclical companies with solid balance sheets which can weather any economic downturn and also invest into ETF's with long-term thematic trends such as Cloud Computing, Cyber Security, Automation and Robotics to name a few. We keep bonds and TIPS mainly for capital preservation and hold a certain clearly defined and closely monitored amount of HY bonds to generate income.

We also have invested a small amount into alternative investments where prices should behave independently of traditional market movements and we have a fairly high gold position as a protection in these uncertain times.

Our portfolios are constructed to withstand any upcoming second waves and the ongoing economic downturn and will still participate in the big global thematic trends of the 2020 decade.

Walter Küng – Senior Portfolio Manager

Asset Allocation

USD Reference – Balanced

Thematic investment idea

Medical Devices

"Don't let your money work for you. Because it doesn't."

Expect the expected

Investing in a future megatrend

Medical Devices include Orthopedic Devices, Cardiovascular Devices, Diagnostic Imaging, IVD (In-Vitro Diagnostic), MIS (Medical Information System), Wound Management, Diabetes Care, Ophthalmic Devices, Dental and Nephrology and the end users are hospitals & ambulatory surgical centers and clinics. The global medical devise market size was valued at USD 425 billion in 2018 and is expected to reach USD 612 billion by 2025.

Medical devices offer several advantages to patients by helping health care providers treat and diagnose patients and assisting patients in improving their quality of life. The global medical devices market is projected to boost and grow strongly going forward for the following reasons:

- The rising geriatric population
- The growing prevalence of chronic conditions
- Growth in surgical procedures and complex surgeries
- Technological advancements and rising demand for innovative therapies to overcome up to now unmet needs
- Business expansion into in-mature markets such as China, India and other EM

The global medical devices market is highly fragmented and there is no clear dominant global player. The biggest companies include Medtronic, DePuy Synthes, Fresenius Medical Care or Philips Healthcare, to name a few.

For investors, this is an opportunity to invest in a secular trend with a huge potential: Medical Devices. We prefer to invest in a diversified basket of securities and have selected proven active funds and ETF's. Should you want to know more, please feel free to contact your Relationship Manager.

"Luck shouldn't be part of your portfolio."

HYPOSWISS
ADVISORS

Expect the expected

Rue de Hesse 7, 1204 Geneva – Switzerland
Hufgasse 17, 8080 Zürich – Switzerland
Tel. +41 22 310 76 40, www.hyposwissadvisors.ch

Mission Statement

- Hyposwiss Advisors' mission is to offer **personalized asset management services and financial advice** to high net worth individuals and families based in the **USA** and **Canada** with the overriding objective of **capital preservation** and **asset growth** performance oriented.

- Investments in compliant global assets are used to construct a **diversified balanced portfolio** tailored to the investor's requirements and deposited with **international banks** acting as qualified custodians.

Contact

Hyposwiss Advisors SA

www.HyposwissAdvisors.ch
info@advisors.hyposwiss.ch

Head Office
Rue de Hesse 7
1204 Geneva - Switzerland
Mr. Elio Barzilay

Tel.: +41 22 310 76 40
Fax: +41 22 310 76 39

Representative Office
Hufgasse 17
8008 Zurich - Switzerland
Mr. Michael Bösch

Tel.: +41 22 310 76 35
Fax: +41 22 310 76 39

Disclaimer

All the contents of publications of Hyposwiss Advisors SA or its affiliates are for information purpose only. Information contained herein does not constitute a solicitation or offer or recommendation to buy or sell any investment instruments, to effect transactions or to conclude any legal transaction of any kind whatsoever.

The information contained and the opinions expressed herein by Hyposwiss Advisors SA are subject to change without notice. No guarantee or undertaking is offered regarding completeness, reliability or accuracy of the information given. Financial instruments and securities or any other investments mentioned in this document may involve significant risks including the possible loss of principal. No assurance is given that the investment objective of any product will be achieved. Past performance should not be taken as an indicator or guarantee of future performance. Hyposwiss Advisors SA or any of its affiliates may or may not at any time hold a position in or with respect to the investments which could be mentioned herein.

This document may not be reproduced, distributed or published without the prior written consent from Hyposwiss Advisors SA.

Access to the information may be restricted by laws or regulations to which the individual user is subject. As a consequence, this document is not directed at, or intended for distribution to or access by any person or entity who is a citizen or a resident of any jurisdiction where the information in question would be prohibited by law or regulations.

Hyposwiss Advisors SA does not render tax, legal or accounting advice. Clients are encouraged to seek their own competent independent professional legal, tax and accounting advice.

Registrations with the US Securities and Exchange Commission and the Canadian Securities Administrators do not imply a certain level of competence, education, skill or training. The protections of the US and Canadian rules and regulations are only available to residents of the respective country, province or territory.

■ ■ ■ ■ ■

© 16 July 2020 – All rights reserved.