March 5, 2021

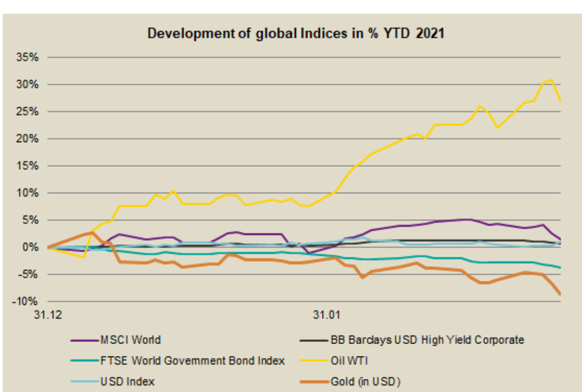
Vontobel Swiss Wealth Advisors

Investment Outlook – March 2021

Dr. Thorsten Krauss, CEFA
CIO
Vontobel Swiss Wealth Advisors

Investment Review

Despite occasional corrections, risk-assets continue to do well since the beginning of the current year. Cyclical stocks, bond yields, commodities, and commodity currencies have all been climbing in recent weeks. Steps towards further re-opening should provide a tailwind during the next months, as the acceleration in global growth moves from expectation to fact. As countries speed up their vaccination efforts and infections come down, the winter-wave of Covid-19 seems to fade out in the northern hemisphere, allowing for a relaxation of those restrictions with the most negative impact on mobility and economic growth. Since the beginning of 2021, most major equity indices delivered slightly positive returns. The S&P 500 Index gained around 1.7%, the Swiss SMI Index is down 4.6%, the Euro Stoxx 50 index rose 1.4% and the MSCI Emerging Markets index, as the best broad market index so far, returned 3.8%, all on a total return basis in USD terms. Government bond yields continued to anticipate a rebound in global economic activity and started to move higher across the board at the long end of the curve. Credit spreads continued to move sideways close to historic lows. As a result of rising bond yields, gold continued its downtrend and closed the month at $1733 per ounce.



[Source: Bloomberg, Vontobel Swiss Wealth Advisors (VSWA)]

At the most recent meeting of our Investment Committee we decided to stay the course and remain overweight equities in all multi-asset mandates. Early results from Israel, the U.S. and the U.K. all indicate a significant reduction of infection rates and hospitalizations among most vulnerable population groups already vaccinated. As most countries try to speed up vaccinations, several will have reached mass immunity among large groups of their population during the second quarter of the current year. This brightens the prospects for a strong economic recovery during the second quarter and thereafter, driven by pent-up demand and the easing of mobility restrictions. Rising economic momentum will also drive a strong recovery in corporate earnings, which is a prerequisite for further stock market upside. Inflation will likely rise in the second quarter due to base effects, but not become a longer-time issue as labor market slack prevails, and industrial capacities remain underutilized for the time being. As long as inflation remains below central bank targets, monetary policy will stay loose and further support economic stabilization across major regions.

Global Economy

As the expected growth recovery is moving into focus, stock markets have further increased and bond yields have finally moved higher at the longer end of the curve. As a result of rising yields across regions, investors started to worry if this development will potentially be disruptive for equities and other risk assets. The impact of rising yields on risk assets depends on whether this rise is largely driven by better growth prospects or by expectations of more hawkish central bank policies ahead. Given the current macroeconomic backdrop we strongly believe that the former is the case and that there will not be an immediate change in central bank support in most if not all developed countries. However, the same is not necessarily true for Emerging Markets, where policymaker rhetoric recently took a more hawkish turn on rising headline inflation and strong financial markets, signaling that hikes in target rates may be closer than expected.

U.S. real GDP growth for the fourth quarter of 2020 was revised up to 4.1%, which was slightly below consensus expectations. Upward revisions to business fixed investment and resident investment more than compensated for the downward revisions in personal consumption growth. Core and headline personal consumption expenditure inflation was 1.5% each for January, on a year-on-year basis. The Institute for Supply Management's manufacturing as well as the services index are at high levels, signaling that the U.S. economy is doing quite well, as some cities are easing restrictions on dining and other activities to help fuel consumer spending. Initial jobless claims declined much more than expected to 730k in the week ending 20th February. The recovery in the severely hit labor market should continue, aided by re-opening efforts, additional stimulus measures, a successful vaccination path and declining infection rates. On the basis of persistently strong macroeconomic data releases we are leaving our GDP growth estimates for the current year unchanged at 5.0%.

Eurozone countries will most likely be faced by a double-dip recession in the first quarter, as tighter mobility restrictions take their toll on consumer spending. The expected dip in Germany's GDP will be exacerbated by the semiconductor shortage, which acts as a drag on automobile industry growth. Economic activity in France has held up better compared to the rest of Europe, as restrictions are less severe than in other major countries. However, current infections are at uncomfortably high levels, implying the risk of rules being tightened sooner or later. We assume that restrictions will be gradually eased during March, April and May and that curbs on public life will be lifted almost entirely in summer on decelerating infections and significant vaccination progress. Once restrictions are lifted we expect activity to rebound strongly on rising consumer demand. We reduce our real GDP growth forecast for the Eurozone from 4.7% to 4.3% for 2021.

Switzerland's economy unexpectedly expanded in the fourth quarter of 2020, with GDP increasing 0.3% compared to the previous quarter. The second wave of the virus had much less of an impact on the economy than the first wave did in spring 2020, as foreign demand for Swiss goods helped to offset the impact of lockdown measures. The Swiss economy will likely shrink in the first quarter of this year, as the government shut down restaurants and leisure facilities late in 2020 to cope with rising infections. The defensive and well-diversified Swiss industry structure certainly helped Switzerland to do better than most neighboring countries during the crisis. Significant government aid programs helped to support consumer spending and kept unemployment rates at low levels. Our real GDP growth forecast for 2021 remains unchanged at 3.4%.

Our core scenario of a substantially improving growth outlook in the course of the current year, based on a positive vaccination path, pent-up demand, and the normalization of currently high savings rates is still valid. Our forecast for global GDP growth remains unchanged at 5.5%.

GDP growth (in %)

	2019	2020	Current	Forecast 2021	Forecast 2022
Eurozone	1.3	-6.8	-5.0	4.3(4.7)	3.3
USA	2.2	-3.5	-2.5	5.0	3.5
Japan	0.3	-4.9	-1.1	2.6	1.8
UK	1.4	-9.9	-7.8	5.0(5.5)	4.8
Switzerland	1.1	-3.5	-1.7	3.4	2.8

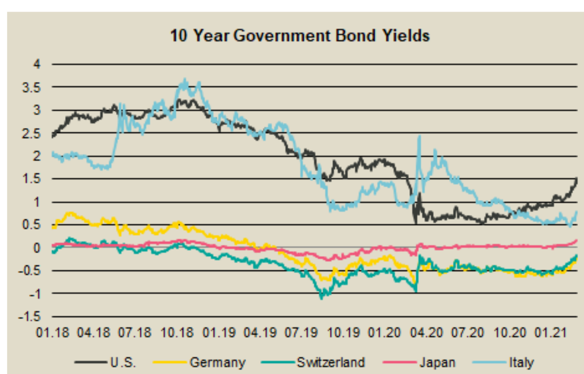
VSWA Forecast; () old forecast

Bonds

Recent data releases for January show that U.S. inflation, as recorded by the Core Consumer Price Index (CPI), which excludes the more volatile food and energy prices, increased by 1.4% compared to the previous year. The Personal Consumption Expenditure Deflator (PCE) paints a similar picture, increasing 1.5% compared to January one year ago. Apparently, the large scale fiscal and monetary stimulus, which was injected during the past 12 months, has had little impact on prices so far. Both, plenty of slack in the labor market and the underutilization of industrial capacities seem to hold inflation below the FED target of 2%. In his recent testimony to the Senate Banking Committee, FED Chairman Jerome Powell stressed that the central bank would keep short-term interest rates pinned near zero and continue to purchase bonds "until substantial further progress" had been made towards the main goals of maximum employment and 2% inflation.

In the flash inflation release for February, Eurozone headline slightly increased to 0.94% year-over-year, while core inflation fell to 1.10%. The Swiss Core Consumer Price Index increased from -0.4% in December to exactly 0.0% in January compared to a year ago. This leaves room for policy makers to apply and continue various forms of fiscal and monetary stimulus. ECB President Lagarde stressed the Governing Council's determination to keep financing conditions favourable, which may imply a step up in government bond purchases in the coming weeks. Corporations and governments find themselves in a very comfortable situation, as they are able to raise debt capital at record low rates.

However, over the course of February, markets began to worry about a possible increase in inflation. Reflation first became a topic last November, when positive headlines about vaccines sparked the hope of a strong economic recovery in 2021. The success of the vaccine rollout in the U.K., the U.S. and notably Israel increased investor's confidence in an economic rebound scenario. This led to a steepening of the yield curves across all major economies. 10-year yields rose sharply, while the front end of the curve remained unchanged. The 10-year US Treasury yield rose from 1.05% to 1.50% in February, while movements were less pronounced in the Eurozone and Switzerland. Generally speaking, rising bond yields are a sign of an improving macroeconomic backdrop and they also allow bond investors to deploy capital at a better expected return.



[Source: Bloomberg, VSWA]

As the market participant's confidence in the "return to normality" increased, credit spreads continued to remain tight in February. Investment grade as well as high yield spreads trade close to all-time lows, indicating low expected defaults and an improving economy for the years to come. In our mandates we seized the opportunity and selectively added corporate bonds with longer durations and higher expected yields to our client's portfolios.

The rise in longer term yields lead to a heated discussion in financial media about the possibility of rising inflation and potential spill-over effects to equity markets. In our view, rising yields are a natural adjustment of the bond market, which starts to price in higher economic growth over the next years. Investors can profit from this steepened yield curve by selectively adding longer dated corporate bonds. In our multi-asset class mandates we remain underweight fixed income and favor corporates over government bonds.

Key interest rates (in %)

	2019	2020	Current	Forecast 3 months	Forecast 12 months
EUR	-0.50	-0.50	-0.50	-0.50	-0.50
USD	1.75	0.25	0.25	0.25	0.25
JPY	-0.10	-0.10	-0.10	-0.10	-0.10
GBP	0.75	0.10	0.10	0.10	0.10
CHF	-0.75	-0.75	-0.75	-0.75	-0.75

VSWA Forecast; () old forecast

10-year government bond yields (in %)

	2019	2020	Current	Forecast 3 months	Forecast 12 months
EUR (Germany)	-0.2	-0.6	-0.3	-0.4(-0.5)	-0.3
USD	1.9	0.9	1.5	1.3(1.1)	1.6(1.4)
JPY	0.0	0.0	0.1	0.1	0.1
GBP	0.8	0.2	0.8	0.5(0.3)	0.7(0.5)
CHF	-0.5	-0.6	-0.3	-0.3(-0.5)	-0.2(-0.3)

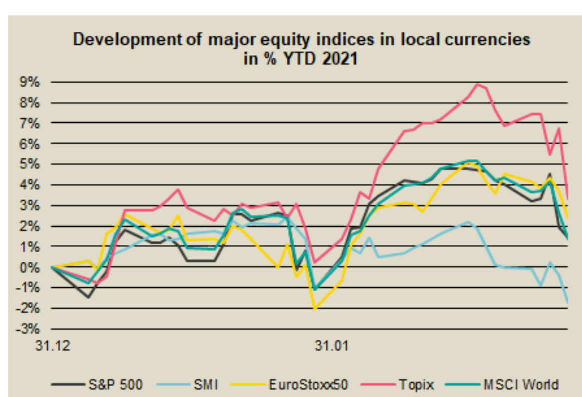
VSWA Forecast; () old forecast

Equities

Many investors start to worry about signs of increasing speculative behavior in markets and fear that a bubble in risk assets may be about to build. Early signs of too much risk taking can be found across many sectors of the market. The recent speculation of retail investors on heavily shorted stocks, the spectacular gains of cryptocurrencies, as well as the boom in IPOs and SPACs are all signs of exuberance. While rising risk tolerance is worrying, stock valuations are not pointing to a broad based bubble across equity markets. During the technology bubble of the late 1990s, the five biggest U.S. stocks traded at a PE ratio of 55 on average. Despite the massive surge of many technology related businesses, the most dominant U.S. companies of today are much cheaper now than compared to typical bubble periods in the past. Based on estimates for the current year, Amazon, Apple, Facebook, Google and Microsoft are trading at a PE ratio of 34.6 on average. These companies are expected to grow by 22% on average over the next 3 years. All of these companies profited from products, which remained in strong demand despite the recession and which will likely continue to attract consumer and business spending in the future. Thus, the price return of these companies is fully driven by strongly rising earnings. Bubbles certainly exist in fast growing small-caps of the technology space, where much future growth optimism is already reflected in high current valuations. During the technology bubble of the late 1990s, the yield of U.S. Treasuries with 10 years maturity was above 6%, now it is below 1.5%. During this period, the dividend yield of broad stock market indices has remained quite stable. If there is a bubble, it may be in bonds and not in equities.

Based on consensus estimates for 2021, Price-to-Earnings (PE) ratios for major stock market indices are 18.2 for the Eurozone, 17.8 for Switzerland and 22.8 for the S&P 500. The U.S. market trades approximately 15% above its longer-term average, whereas the Eurozone and Switzerland are valued in-line or even below their 10-year average. Compared to bond markets, current equity valuation multiples seem justified. Despite the strong rally from March 2020 lows, the aggregated earnings yield as well as the dividend yield of major stock market indices is way above the low yields of government bonds or investment grade corporate bonds. As the forward guidance of major central banks suggests, the current low-yield environment will persist for several years.

Higher stock market valuations point to lower than average returns over the medium term. However, this doesn't mean that equities are in a bubble, which is about to burst. If 10-year yields rise, which should be expected in an economic recovery after a recession, equity valuation multiples will start to normalize. This process usually takes time and happens in the context of rising earnings. Strongly rising earnings should usually be able to compensate for the negative impact of valuation multiple compression, allowing stock market indices to rise further over the years. Consensus growth estimates for aggregated earnings of all S&P 500 members are 38%, 15% and 11% for 2021, 2022 and 2023, respectively. Earnings estimates for the next 12 months continue to rise across major markets. Strong reports for the past quarter show that analysts underestimate the positive impact of the improving underlying economy on company earnings. The current reporting season has been one of the best on record. So far, almost 80% of U.S. companies and close to 70% of Eurozone firms reported earnings above estimates and the average earnings beat was significant. In our view, we are still in the early innings of a new business cycle with plenty of potential for rising company earnings during the next years.



[Source: Bloomberg, VSWA]

Equity market valuations

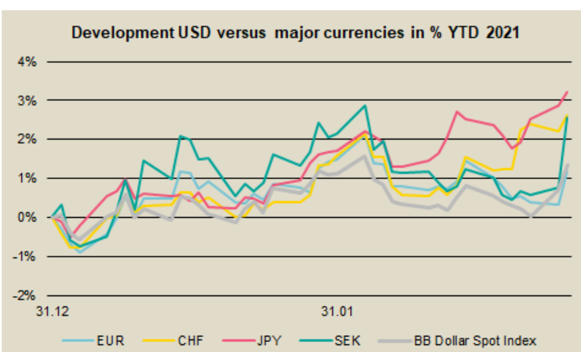
	Price to earnings ratios			Price to Book	Dividend yield %
	Expected 2021	Expected 2022	10 year average	2021E	2021E
USA	22.8	19.8	19.9	4.0	1.5
Eurozone	18.2	15.6	19.5	1.8	2.9
Switzerland	17.8	16.0	17.6	2.7	2.9
UK	14.8	12.7	21.9	1.6	3.8
Japan	22.7	17.0	17.1	1.4	1.8

VSWA Forecast; () old forecast

Despite higher-than-average valuations in certain stock market segments, the overall risk premium in equities is high. We will most likely see a strong and synchronized global growth backdrop in 2021 and 2022, driven by rebounding consumer spending, unchanged monetary policy and strong fiscal support. This will drive strong corporate earnings growth over the next years. Thus, our preference for equities as the most attractive asset class remains unchanged.

Currencies

Since the beginning of 2021, currencies of countries with higher commodity exposure, such as Australia or Canada, gained versus the U.S. Dollar. This was partly driven by rising commodity prices but also by increasing yield spreads compared to U.S. Treasuries at the longer end of the curve. Safe heaven currencies, such as the Swiss Franc or the Japanese Yen, depreciated versus the Greenback on rising confidence in the expected economic normalization. We continue to expect the USD to weaken against most G10 currencies, driven by an improving macroeconomic growth backdrop over the next months, as the vaccination and reopening process plays out and the U.S. front end remains low. A major risk to this view would be a larger-than-expected steepening of the U.S. yield curve as well as a sooner-than-expected beginning of FED tightening.



[Source: Bloomberg, VSWA]

Investors seem to be shifting funds out of the Swiss Franc, contrary to what happened during the first half of 2020. Instead, fund flows into international equities have increased in recent weeks. Currency outflows are a welcome development for the Swiss National Bank, which has kept key rates below zero for the past six years to discourage safe heaven purchases of the Swiss currency. Global risk sentiment tends to be a major driver of CHF crosses, while positive domestic macro developments of a small economy tend to be ignored in the short term. However, key structural drivers of currency pairs, such as differences in inflation rates and current account balances, clearly speak in favor of the CHF in a longer-term perspective.

Currencies

	2019	2020	Current	Forecast 3 months	Forecast 12 months
CHF per EUR	1.09	1.08	1.10	1.08	1.10
CHF per USD	0.96	0.88	0.91	0.89	0.87
USD per EUR	1.12	1.22	1.21	1.21	1.26
JPY per USD	108	103	106	103	101
USD per GBP	1.32	1.37	1.39	1.37	1.39

VSWA Forecast; () old forecast

Commodities

Crude oil is currently supported by strong Asian demand and the expectation of an economic reflation in the rest of the world. In addition, U.S. shale production continues to disappoint and Saudi Arabia holds back as much supply as necessary to support prices. All policy decisions taken so far from the Biden administration, such as higher fiscal stimulus, the stop of the Keystone Pipeline project, the decision to halt new oil drilling on federal lands as well as the prolongation of Iran sanctions, are supportive for the oil price. The global oil market rebalancing continues, with demand growth likely outpacing supply growth at least until the end of the first half of 2021. We increase our 12 months forecast for WTI from 60 to 65 $/bbl.

Since the beginning of the current year, gold continued its correction, which started by mid-2020. Key drivers of this correction have been rising nominal and real yields, waning safe heaven demand as perceived market risk and volatility fell, subdued central bank demand, and the strong rotation into risky assets on the back of a repricing of global growth assumptions. As these factors are still in play, gold's short-term potential may be limited. A strongly expanding global monetary base resulting from quantitative easing, large and persistent fiscal deficits, as well as rising inflation expectations are certainly supportive and should limit the downside potential. However, the key structural drivers for rising gold prices in the longer term are still in play. Government debt as a percentage of GDP across major countries reached the highest level since WWII. As a result, interest rates are kept at artificially low levels to ensure a cheap refinancing of public debt.

Commodities

	2019	2020	Cur-rent	Forecast 3 months	Forecast 12 months
Crude oil (WTI, USD/barrel)	61	48	62	55	65(60)
Gold (USD/ troy ounce)	1517	1897	1'721	1800(1900)	1900
Copper (USD/ lb.)	2.80	3.50	4.14	4.20(3.65)	4.50(3.65)

VSWA Forecast; () old forecast

We reduced the gold quota in all multi-asset-mandates in August 2020 but remained overweight. Gold offers strong diversification benefits as it protects from potential USD

weakness, as well as from negative inflation surprises and it is usually negatively correlated with risk-assets. Growth in Emerging Markets also benefits gold as the purchasing power of retail buyers rises over time. Rising EM wealth was the major driver behind gold's move from $250/oz to $750/oz between 2000 and 2007. Thus we leave our 12 months target of $1900/oz unchanged.

Vontobel Swiss Wealth Advisors AG
Phone: +41 (0)44 287 81 11
Phone (from the U.S.): 011 41 44 287 81 11
info@vontobeladvisors.com

www.vontobeladvisors.com