SYZ PRIVATE BANKING

THE IMPORTANCE OF DEFENSIVE PLAYS AS INVESTORS WEIGH NEW RISKS

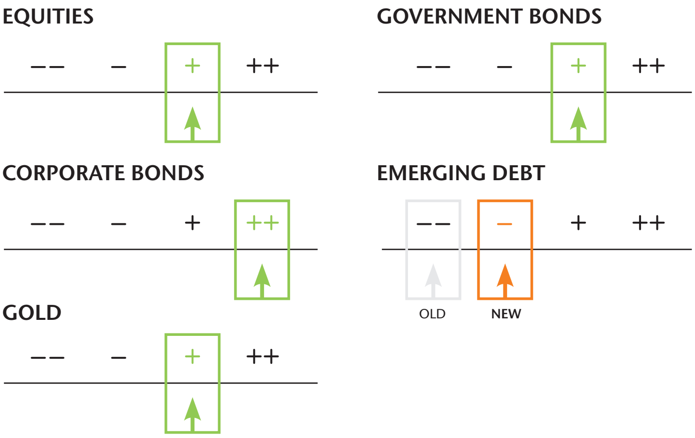
While we remain in the shadow of the pandemic, it is important to remember markets are, by nature, forward looking. Spiking coronavirus cases in the US and local country outbreaks in Europe are cause for concern, but the broader picture is one of a tentative recovery.

There is no doubt the global economy has experienced an unprecedented brutal and steep recession, but this is a 'known known', and the recovery is already underway. Our central base case scenario puts the probability of a short but steep recession at 60%. If Developed market countries will still all leave the year with their GDP figures in the red, China's robust recovery is likely to save them from a negative end of year tally.

Still darkening the global picture is also high levels of unemployment and its uncertain impact on consumption. A second wave may well materialise indeed, but we don't see another lock-down on the scale of the first outbreak. What matters most, is that the trough in GDP is behind us and we are now in the recovery phase, albeit from a low base. As much in life, it is the direction of travel that ultimately matters.

The second half of 2020 may well be remembered for continual spikes in volatility. With this in mind, we have ensured diverse sources of protection from uncorrelated assets – from equity puts to long-term US treasuries.

ASSET ALLOCATION VIEWS



WILL EARNINGS DERAIL THE NASDAQ?

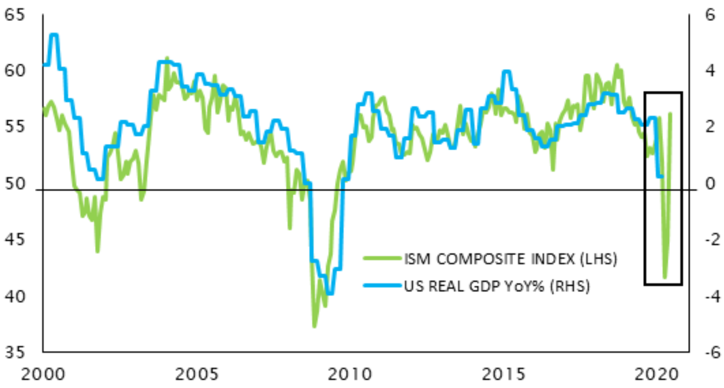
The macro economic backdrop supports the investment case for equities. There are still low levels of household debt and, most importantly, a global central bank commitment to stimulus. That said, investors need to be discerning and we continue to focus on stocks that exhibit both quality and liquidity characteristics.

While the relentless negative news cycle around Covid-19 has injected further volatility into market broadly, some areas have been remarkably resilient. As the pandemic has impacted sectors, such as energy, that have seen a lacklustre fightback, many quality Nasdaq-listed names have seen soaring returns in recent weeks.

This performance has fuelled speculation of another tech-driven crash. Our view, is that while some tech-focused stocks are priced to perfection, this is a very different situation to the dotcom boom. Underlying the investment cases for firms like Amazon are high cash flows, healthy balance sheets, and monopoly-like positions.

So while the multiples are certainly high, the main drivers of strength and domination are not only still in place, but have been accelerated by this crisis. For many of these companies, the next earnings season is an acid test. Some less robust businesses may be brought down to Earth, but we are confident that the more robust cash-generative tech players can continue to thrive long into the post-Covid era.

UNITED STATES - MONTHLY ACTIVITY INDEX (ISM) AND REAL GDP YEARLY CHANGE



SOURCE: SYZ, FACTSET. DATA AS OF 23.07.2020.

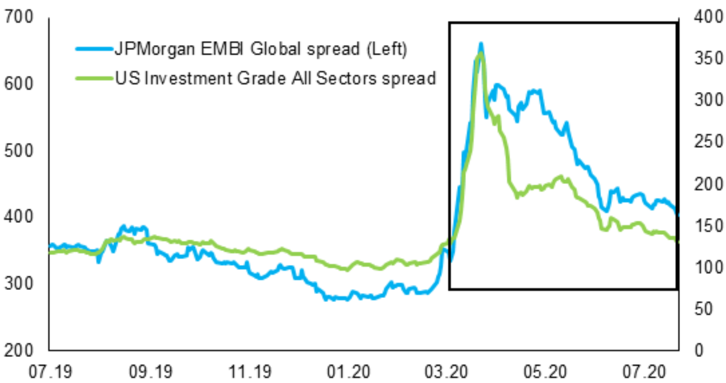
FIXED INCOME STILL OFFERS OPPORTUNITY

The meteoric impact of the crisis afforded us with unique opportunities in fixed income markets. But as Investment grade spreads have tightened, the return profile has lowered. This phenomenon is particularly pronounced in developed markets. Against this backdrop, we have slightly increased our exposure to emerging market bonds in hard currency, but the focus remains on quality in investment grade.

We have also recently increased our preference for duration. This is supported by the 'lower-for-longer' outlook, and diminished risk of rate increases at the long end, given central bank intervention.

We remain cautious on high yield, having exited our positions in late February due to the unfavourable risk reward dynamics. Sectors such as energy will remain under pressure in H2, given mounting debt and stretched balance sheets.

MACRO ECONOMIC IMPROVEMENTS WARRANT NOW TO ADD SELECTIVELY SOME EXPOSURE TO EM DEBT



SOURCE: BLOOMBERG. DATA AS OF 22.07.2020.

BIDEN STIRS MARKET CONCERNS

While the coronavirus is not going anywhere in the near-term, markets are starting weigh up new risks. Six months ago, markets priced in a Trump victory, but now Biden is significantly ahead. His programme advocates for higher tax brackets, and to raise corporate tax to 28% – but he is not promising a full socialist mandate advocated by more left democrats.

A Biden win would adopt a more consensual approach. He is far more in the centre than either Sanders or Warren. And while healthcare would be impacted, but the effect will be limited, as Biden may not be able to fully implement reforms. This is already reflected in price movements. Democrats have been campaigning on anti-trust issues – and this may impact some of the tech titans. But for example, we would be happy to hold dismantled Alphabet shares. However, the reality is this kind of issue might not be on the top priority of a democrat president with more direct issues, especially with the unlimited funding provided by the Fed and the lower public concern for deficits.

Ultimately, US elections will certainly add volatility to the market but won't change the fact the virus and stimulus will remain key drivers of the market. And in the long-run, Biden would be more predictable for markets, but China tensions may not dissolve. He may be more multilateral, but putting pressure on China is more about shifting balance of trade, not stopping it – and this means flexing American muscle.

PROTECTION ADDS BALANCE

Given the competing drivers of volatility, and a backdrop of second wave fears, we continue to apply defensive instruments to our portfolios, while maintaining exposure to the recovery through quality equity and fixed income security selection.

At the end of June, we created new equity protection on the S&P 500 which is valid until end of year to limit the negative impact of the potential pick-ups and future drawdowns. It also means we never have to fire sale quality assets in the face of indiscriminate selling.

We still hold our allocation in gold which is performing well in risk-off conditions. We will bank profits if it moves higher. We also maintain a position on long bonds, as central banks maintain their commitment to monetary intervention. At a time, where sentiment swings violently between negativity and positivity, balance is vital.

CONTRIBUTORS

ADRIEN PICHOUD, CHIEF ECONOMIST & SENIOR PORTFOLIO MANAGER
E. adrien.pichoud@syzgroup.com

FABRICE GORIN, SENIOR PORTFOLIO MANAGER
E. fabrice.gorin@syzgroup.com