AZIMUT
DEFINING INVESTMENT DIRECTION

AZIMUT GLOBAL VIEW

12.04.21

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

US CPI – 13.04
The headline CPI is expected to reach 2.5%, while the core index only 1.5%. Any deviation from those levels may trigger significant market reactions

US RETAIL SALES – 15.04
The "control group" sub-index monitored by the FED is expected to increase by 7.2% MoM in March, supported by the stimulus checks

ECB MEETING – 22.04
Market participants do not expect any new measures, but will focus on the future path of PEPP purchases

MARKIT PMI – 23.04
The Markit April preliminary PMI data for US and Europe will provide a timely assessment of the corporate sentiment

THE MOMENT OF TRUTH

- **We are entering the most critical period for inflation and interest rates**
- **US may be the most affected country due to base effect, fiscal stimulus, fast vaccine rollout and improvement in the labor market**
- **For bonds, further spreads compression is possible, but better to hedge duration**
- **For equities, further rate increases above recent highs could lead to a consolidation**

For several months now, the market has been aware that the coming months are the ones that will be the most insidious for inflation and interest rates.

The impact on inflation due to the "base effect" (i.e. the distortion in a monthly inflation figure that results from abnormally high or low levels of inflation in the year-ago month) is the most obvious factor, and certainly does not represent a surprise. It can be estimated fairly easily by looking at the evolution of the CPI index and its components, in particular the commodities that have increased by more than 60% since the bottom reached in March 2020 (graph on the next page).

Much less predictable past development was the approval of two stimulus measures in less than three months, which included the payment of stimulus checks of $2,000 per household in January and March. Considering that the $600 stimulus checks paid in January resulted in an increase in Personal Consumption of nearly 4% (graph on the next page), the $1,400 payment in March could double such spending, even if the large part of the money will likely be spent in April. This increase in spending could be similar to that of May 2020, when the CARES act payments were received. The difference is that the payment then served to offset a drop in GDP due to the lockdown, while today it would only cause an exaggerated acceleration in GDP growth.

(continued)

Source: Bloomberg

Source: Bloomberg

Another element that was difficult to predict was the speed of vaccinations. The most advanced countries in the process (Israel, UK, USA) are all witnessing a sharp drop in new cases, allowing their economies to reopen quickly. The rest of the countries lagging behind are expected to see an increase in the pace as vaccine availability increases in the coming weeks.

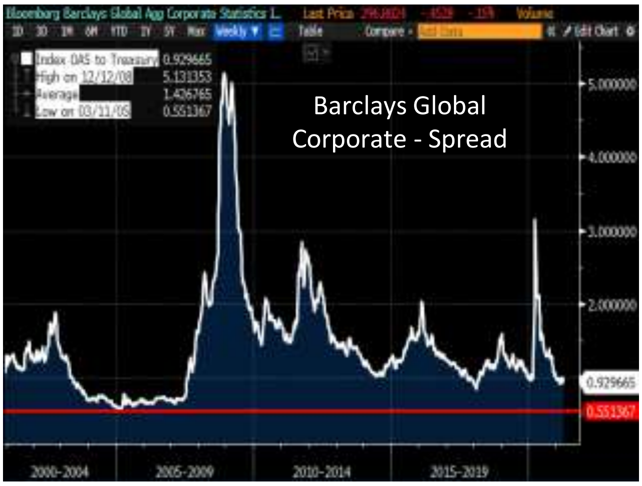
In the United States, where timely data are more available, the labor market is experiencing a rapid recovery with the majority of hiring occurring in the hardest-hit sectors where the bulk of the people lost their jobs due to the pandemic. This is an essential step towards normalization.

All these factors combined are already exerting pressures on prices. The Producer Price Index (the index with the longest historical series is shown below) stands at almost 6%, and is close to the maximum levels of the last decades. Similar indications come from the prices paid index calculated by the Institute for Supply Management (ISM), which is also close to the highest readings of the last 50 years.

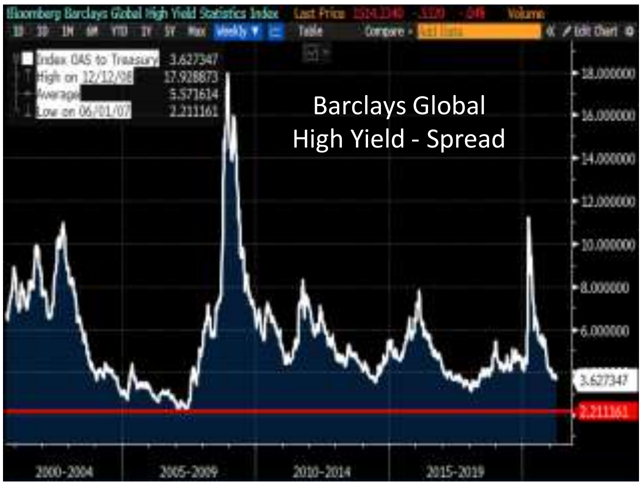
In Europe, the rise in inflation could arrive a few months later than in the United States, a situation ominiously similar to what's been observed in the distribution of the vaccine. It is possible that the highest CPI readings will be recorded between August and November 2021, while for a few more months inflation may not decisively exceed 2%.

(continued)

An important implication that can be drawn from our points is that it is advisable for the fixed income portfolios to maintain a prudent approach on duration by at least partially hedging it to the point permitted by the investment policy. Conversely, there should be no surprises from the spreads. The stronger-than-expected economic recovery could lead to a further spread compression, even to the historical lows.



Source: Bloomberg



Source: Bloomberg

Equities, unlike bonds, are benefiting from all of the above dynamics. Stock markets have therefore already reached the price targets expected for the end of 2021, and the sentiment has been extremely bullish. Should interest rates rise above the recent highs driven by the above-mentioned macroeconomic data, they could be the pretext for a healthy correction.

Asset Allocation View

	−	=	+
Equity			
Developed Markets			■
Emerging Markets		■	
Fixed Income			
Developed Markets Sovereign	■		
Developed Markets Corporate	■		
Emerging Markets		■	
Commodities			■
Currencies	*Commentary below*		

− UNDER = NEUTRAL + OVER

Equity

Developed Markets

We reduced our recommendation on Developed Market equities to slightly positive. The recommendation is conditioned upon the rates not moving past their recent highs, which may happen anytime over the next week due to the strong spending data and CPI print – both expected in the near future due to the fiscal stimulus and the base effect. If rates continue their upward move, then the risk of a retracement becomes material. In terms of geographical allocation, we continue to prefer Europe, which is much more "value" than US, and trade at multiples which are lower than the historical averages for MSCI World.

US	=	**Europe**	+	**Japan**	=

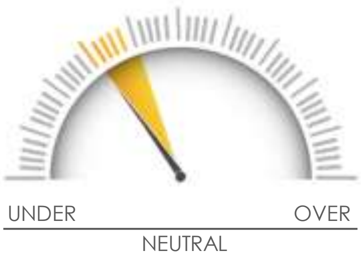
Emerging Markets

We maintained the neutral indication for Emerging Markets Equities. Traditionally, Emerging Market returns tend to be negatively correlated with US rates, which are expected to remain at the current or higher levels considering the reopening of the US economy and the recently approved fiscal stimulus. Therefore, even if in the long term Emerging Markets continue to grow faster than Developed Markets, we prefer to maintain a more cautious approach in the short term.

Asia ex-Japan	=	**EEMEA**	=	**LATAM**	=

Fixed Income

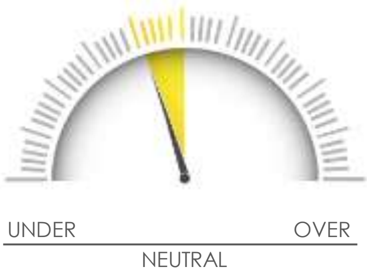
Developed Markets Sovereign



We lowered our overall recommendation on Developed Markets sovereign bonds to underweight. Over the next few weeks & months, the CPI is expected to increase materially due to the base effect, and most Americans are expected to spend their stimulus checks rather quickly as seen in previous occasions, boosting the personal spending data. Additionally, the strengthening of the labor market together with the fast vaccine rollout should contribute to the further acceleration of global growth. In this environment, rates could continue their increase to new highs past their recent peak. Within Developed Market sovereign bonds, we have a negative view across all regions with no preference for one over another (the "=" signs below should be read as there is no relative preference among them).

EU Core	=	**EU Periphery**	=	**US Treasury**	=	**Japanese JGB**	=

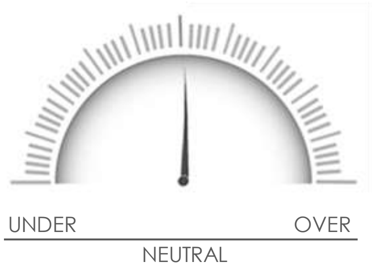
Developed Markets Corporate



We kept our negative recommendation on Developed Markets Corporates. The recent move in risk-free rates has not been extended enough to make investment grade bonds attractive again and the high yield spreads remained broadly unchanged. We stick to our view that further spread compressions could be possible 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 recommendation to neutral, because Emerging Markets bonds tend to be negatively affected by the increase in risk-free rates, in particular the US curve. The move in US rates may continue due to the strong CPI and consumer spending readings expected in the near future. Additionally, some Emerging Markets Central Banks have been hiking rates adding pressure to the EM bond prices.

Local Currency	+	**Hard Currency IG**	=	**Hard Currency HY**	=

Commodities

We maintain our bullish view on the asset class. In the short term we turned more bullish on precious metals as they tend to be influenced by US real rates. US real rates increased over the past few month due to the increase in US rates, with CPI reading being stable. For the next month, the CPI should increase materially due to the base effects and real rates may decrease favoring a bullish move on precious metals. The bull case on precious metals is also supported by the ample liquidity and the surge in fiscal deficits.

Precious	+	**Energy**	+	**Industrial**	=

Currencies

We maintain our neutral view on the Euro, mainly because on one hand the expectation for a stronger economic growth should sustain the demand for cyclical/value stocks that are more represented in EU vs. the US, and on the other hand the slower vaccine rollout may temper the expectation of the Eurozone recovery.

We kept the view on the US Dollar to neutral. While the US dollar may weaken over the long term because of the unsustainable pace of fiscal deficit expansion over the past year, in the short term the widening gap between US rates and those of the rest of the world should be supportive for the greenback.

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

On Emerging Markets currencies, we maintained our neutral view. A further increase in US risk-free rates may put downward pressure on Emerging Market currencies, but on the other hand some EM central banks are starting to increase their rates as well which should provide support for their currencies.

Euro	=	**USD**	=	**Yen**	=	**Emerging**	=