AZIMUT
DEFINING INVESTMENT DIRECTION

AZIMUT GLOBAL VIEW

20.07.20

Main Events

Azimut Global Network

- **Milan**
- Abu Dhabi
- Cairo
- Dubai
- Dublin
- Hong Kong
- Istanbul
- Lugano
- Luxembourg
- Mexico City
- Miami
- Monaco
- Santiago
- São Paulo
- Shanghai
- Singapore
- Sydney
- Taipei

MARKIT PMI — 24.07
All Markit PMI are expected to move above 50, the threshold that separate expansion from contraction

FED FOMC — 29.07
No changes are expected in the US monetary policy.

2Q GDP — 30.07
US and Germany will publish the first reading of the second quarter GDP. How deep the contraction will be?

JOBLESS CLAIMS — 30.07
If jobless claims continue to remain above 1 million per week, the August payrolls data may disappoint

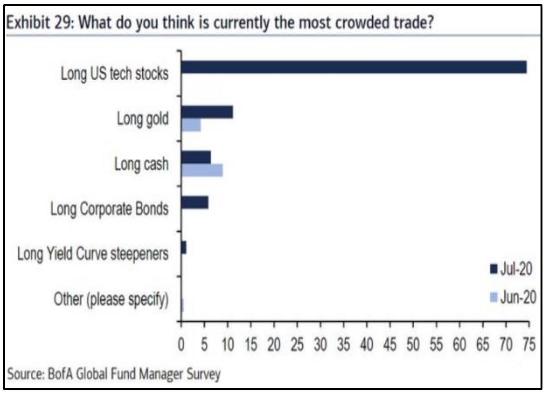
TIME FOR A PAUSE?

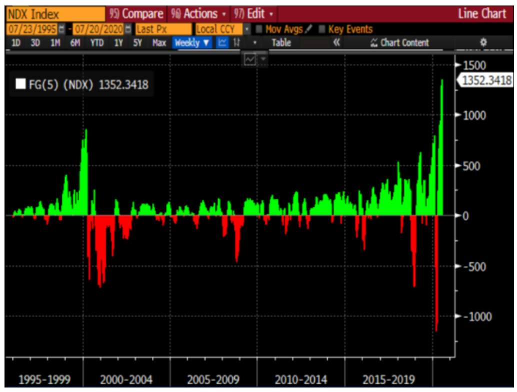
"Be Fearful When Others Are Greedy and Greedy When Others Are Fearful"
Warren Buffett

Since the beginning of the year, technology stocks are the clear winners (again), with all the remaining sectors lagging far behind. Year-to-date the Nasdaq 100 index is up 25% whilst S&P500 is barely flat and the Dow Jones down more than 6%. Similarly, MSCI World Information Technology index is up 20% in dollar terms whilst the generic MSCI World index is slightly negative.

According to the latest Global Fund Manager Survey of Bank of America, long US technology stocks is currently the most crowded trade, according to 74% of the respondents (graph below on the left). This reading is the highest on record.

The Fear-Greed index on the Nasdaq 100 index (see graph below on the right) is currently at its historical high, which means investors have never been so greedy before. If we correct the index by the closing value of the Nasdaq 100 index, the indicator is just slightly below the 2000 high.





Source: Bank of America Global Fund Manager Survey *Source: Bloomberg*

(continued)

Are we entering again a phase of "irrational exuberance" as in the late nineties? Not exactly. At that time technology stocks were start-ups with a lot of debt and promises, but no sales and profits. Let's look at the numbers. The chart below shows the growth of the earnings per share ("EPS"). In green the MSCI World index, and in red for the MSCI World Information Technology index.

Source: Bloomberg

Since 2011 the EPS of the MSCI World Information Technology index doubled (+97%), whilst the EPS for the broad MSCI World Index has been slightly negative. If we had excluded the technology sector, the contraction of the EPS for the MSCI World index would have been much more negative.

Therefore, much of the outperformance of the technology stocks in the past years has been absolutely rational. We could expect that the investments on existing and new technologies will continue to underpin a solid earning growth in the coming years.

In the short term, though, there are few elements suggesting that technology and growth stocks could be vulnerable to a consolidation. The first with the demand for online services (teleconferencing, entertainment, online shopping) exploded during the lockdown. Investors seem to have projected endlessly this incremental demand for tech/growth companies. Traditional businesses, instead, suffered from the lockdown and either withdrew or sharply cut the guidance for 2020 earnings. Currently expectation are so high for tech/growth companies that it could be difficult for them to beat the consensus. To the contrary, expectations are so low for traditional companies that even modest results could top analysts estimates. As the investor positioning is so extreme (see previous page) a reversal of fortune could lead to abrupt adjustments.

The second element is that the valuations of tech/growth are reaching levels that are quite difficult to justify on an absolute basis. As tech/growth companies tend to focus on the growth of sales more than the growth of the EPS, the price-to-sales ratio is a much more appropriate metric for evaluating those stocks.

From the chart on the right that reports the evolution of the P/S ratio for the MSCI World Information Technology it could be easily appreciated that we are reaching levels not seen since the tech-bubble of 2000.

Source: Bloomberg

(continued)

Another element that could support a temporary pause of tech stocks is that most of those stocks are favored by retail investors. However as the temporary enhanced unemployment benefit (payment of additional 600$ per week on top of the traditional unemployment benefits) are going to expire this week, it could well be that the willingness of retail (and unemployed) investors to invest additional money in the stock markets could decrease sharply.

Finally, there is a pure technical element that could call for a temporary retracement of growth stocks. With the recent outperformance, the ratio between the Nasdaq 100 and the S&P500 and the Dow Jones Industrial (respectively the first and the second graph below) is also approaching levels similar to those reached during the peak of the tech bubble in early 2000.

Source: Bloomberg

In light of all the considerations above, the incoming reporting season will be of the utmost importance for the tech sector. Only strong results will be able to sustain the current absolute and relative levels. If it's not the case, a short or mid-term correction is likely to follow.

We are not advocating a change the long term perspective of the technology sector, which is expected to continue to grow at higher speed than the traditional/cyclical sectors. If presents itself, a correction in the tech/growth names should be considered as a long term buying opportunity.

Asset Allocation View

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

− UNDER = NEUTRAL + OVER

Equity

Developed Markets

UNDER OVER
NEUTRAL

We kept the slightly underweight recommendation. Upbeat macro data, positive developments on the European Recovery fund, large monetary and fiscal stimulus are supporting a positive view on the market. On the other hand, current market valuations at levels that are in the upper range of the historical ranges suggest that some caution is needed. Within developed markets, we reiterate the unanimous positive view on European equities. A few portfolio managers are becoming cautious on growth/tech stocks for the reasons explained in the general commentary.

US	−	Europe	+	Japan	−

Emerging Markets

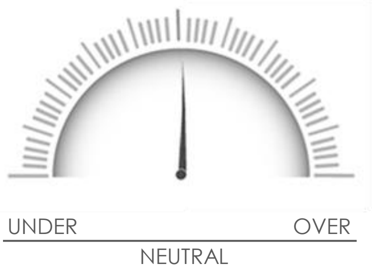
UNDER OVER
NEUTRAL

We kept our recommendation on Emerging Markets to Neutral, with a strong preference for the Asia ex-Japan region, and China in particular. The main catalyst is the recent spike in polls by Joe Biden. If elected, he is expected to halt and possibly even reverse the policy of Trump vs China. This could lead to a sharp rerating of Chinese stocks, that have been sharply sold off over the past few years. Valuations of Chinese stocks are currently about half the US markets, and technology companies trade at much more reasonable multiples. Unchanged the view on the other regions. A weaker dollar (which is the common expectation of the committee in the short/mid term) could constitute a further element of strength for emerging markets equities.

Asia ex-Japan	+	EEMEA	=	LATAM	=

Fixed Income

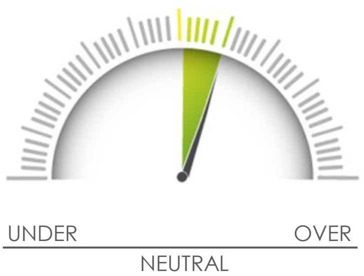
Developed Markets Sovereign



No change in the neutral view on sovereign bonds of developed markets. The Fed is apparently applying a yield curve control, even if not officially declared, as long term rates remain within a very narrow range for several weeks now. In general, we reiterate the view that the ongoing QEs by all the major central banks should keep rates close to the current levels for all markets. There is little value to be found now, but this does not imply that there is downside risk either, at least in the short term. Considering that the EU leaders seem more and more close to reaching an agreement on the European Recovery fund, the spread of peripheral bonds could continue to narrow.

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

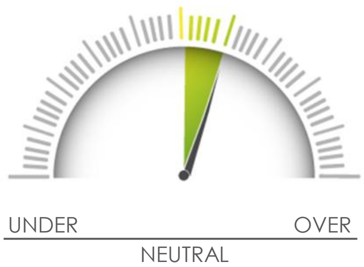
Developed Markets Corporate



We keep our overweight stance. Unfortunately as in many other asset classes, the levels reached by the spreads are not particularly attractive anymore. Notwithstanding this, because of the various QEs, investment grade corporates are as protected as sovereign bonds, but offer a slightly higher yield. In the Fixed Income space, investment grade bonds appear to be the best place in terms of risk/reward. We reinforced our underweight stance on EU and US high yields as their spreads contracted too much, also considering the expected increase in the default rate.

IG Europe	+	**IG US**	+	**HY Europe**	−	**HY US**	−

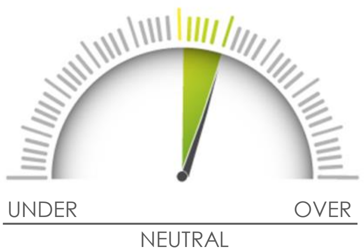
Emerging Markets



We maintained the recommendation on EM bonds to slightly overweight as these bonds did not enjoy the same fast recovery of other segments of the credit markets. They were left behind because EM central banks are not doing QE on their bonds, therefore investors have been more cautious in buying those. Considering the low levels of the risk-free rates, the compression of the spreads in developed market corporates and the rebound of commodities, there is room now for a catch up of emerging bonds. Among them, we have a strong preference for local currency bonds.

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

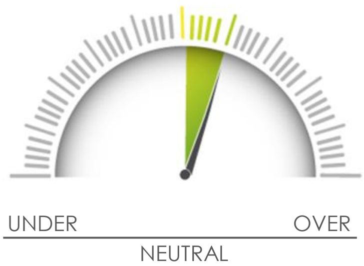
Commodities



We have a neutral stance with a positive bias. We continue to prefer precious metals because of the low yield environment, and as a hedge against unexpected turbulence. Because of the possibility that the Euro will continue to be quite strong in the short term for the reasons explained in the currency section, for Euro-based investors precious metals could be a less attractive investment solution as any strength in the Euro will dent on performances.

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

Alternative Strategies



We keep our recommendation to neutral on liquid alternative strategies, because of the diminished expected returns on other asset classes. This implies that other asset classes have now higher downside risk and could be vulnerable to volatility as well. Therefore alternative/decorrelated strategies are more attractive on a relative basis.

Low Volatility	+	**Medium Volatility**	=	**High Volatility**	−

Currencies

We reinforced the positive view on the euro, as the agreement on the European Recovery fund is expected to be reached in the short term, and there are no signs of a second wave of the coronavirus.
We change to outright negative view on the US dollar mostly because of the expected strength in the euro. The spike in the new cases in US after the reopening, the rise of Joe Biden in the polls (who is expected to implement policies which could be less market-friendly than those of Trump), and breakout of the EUR/USD exchange level above some technical levels are all supportive of a weaker dollar, at least in the short to mid term period.
We maintain our slightly negative view on the Japanese yen, as there are no positive catalysts in sight for the currency.
On emerging markets currencies, we have a constructive view as most of them appear to be undervalued and the yields offered by those currencies are more and more attractive as YTM continues to fall in developed markets.

Euro	+	**USD**	−	**Yen**	−	**Emerging**	+