AZIMUT
DEFINING INVESTMENT DIRECTION

AZIMUT GLOBAL VIEW

19. 07. 21

Main Events

ECB MEETING — New ECB monetary policy goals will be unveiled by Mrs. Lagarde — **22.07**

MARKIT — Will Markit business confidence data be affected by the Delta's spread and worries about a possible slowdown? — **23.07**

FOMC — Will the Fed change its stance that it's still too early to scale back monetary simulus and that further substantial progress is needed? I — **28.07**

US PAYROLLS — Will the expiration of the extraordinary unemployment benefits trigger a pick up in hiring? — **02.08**

Azimut Global Network

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

HOW BAD IS BAD?

- **Governments and central banks have been sounding alarms lately, contributing to the recent gyration of financial markets**
- **The risks associated with the Delta variant's spread may be overestimated**
- **The Fed's concerns about a possible slowdown could actually trigger it**

Contrary to what normally happens, governments and central banks have recently stressed how things could take a turn for the worse in the near future. In particular, governments worldwide have put a lot of emphasis on the Delta variant's spread, while Mr. Powell pointed out that the economy could significantly slow down as fiscal stimuli wane during his semi-annual testimony to the Congress.

In the G20 meeting held ten days ago in Venice - the first in person since February 2020 - in addition to topics such as global minimum tax and climate change, the Delta variant was widely discussed. Since then, this variant has gained significant attention by the governments and media worldwide. In some countries, new restrictions have been announced, including travel ban and limitations for the unvaccinated people.

How well-founded are these fears? Especially with regards to the countries where vaccination has been progressing rapidly? If we focus on United Kingdom as a reference, the first western country where the delta variant started spreading and data coming out could be considered reliable and complete. Public Health England, a British executive agency sponsored by the Department of Health and Social Care, periodically publishes statistics on the covid-19 development in the UK. According to the latest available report (source: https://assets.publishing.service.gov.uk), the delta variant is highly transmissible as it accounts for almost all new cases, but its fatality rate is much lower than the alpha variant, the original one.

(continued)

Table 3. Number of confirmed (sequencing) and probable (genotyping) cases by variant as of 5 July 2021

	All cases					Cases with at least 28-day follow-up[2]		
Variant	**Confirmed (sequencing) case number[1]**	**Probable (genotyping) case number**	**Total case number**	**Proportion of total cases**	**Deaths**	**Cases**	**Deaths**	**Case Fatality Rate** (95% confidence interval)[2]
Alpha	220,173	5,691	225,864	56.6%	4,264	224,131	4,264	1.9% (1.8 to 2.0%)
Beta	898	62	960	0.2%	13	905	13	1.4% (0.8 to 2.4%)
Delta	82,450	87,613	170,063	42.6%	259	45,136	112	0.2% (0.2 to 0.3%)
Eta	443	0	443	0.1%	12	425	12	2.8% (1.5 to 4.9%)

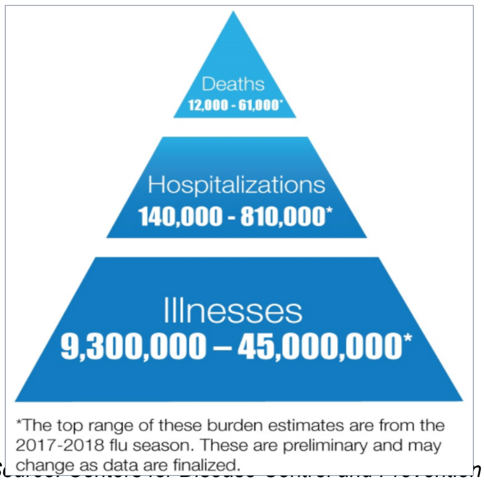
Source: Public Health England

For those people who have been infected within the 28 days follow up period (thus excluding all those who are in the initial phase of the infection and for whom it is not yet possible to know what the course of the disease will be), the mortality rate of the Delta variant was about 0.2%, almost one-tenth of the 1.9% of the Alpha variant.

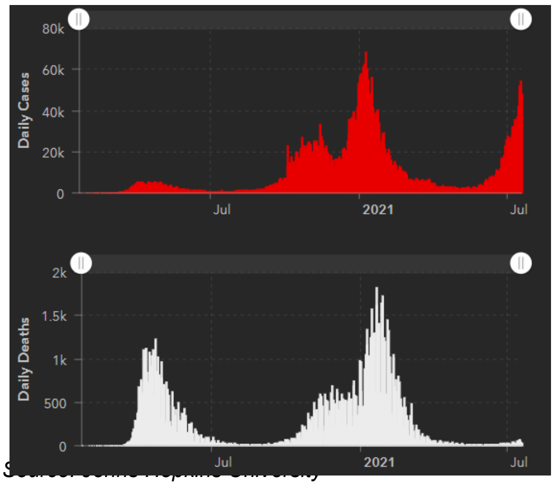
For comparison, below are the reported statistics on seasonal flu mortality rate in the decade 2010-2020 (https://www.cdc.gov/flu/about/burden/index.html), calculated by the US Centers for Disease Control and Prevention (CDC). The mortality rate of seasonal influenza in the US was 0.13% (12k deaths vs 9.3 mln of cases, or 61k deaths vs 45 mln of cases), which is barely lower than that of the Delta variant, at least based on the data available so far. It should also be noted that the majority of deaths caused by the Delta variant is common amongst unvaccinated people, or those who only received their first shots. As the vaccination campaign continues, mortality can be expected to decline further.

Finally, the current numbers should be read in conjunction with those of previous waves. The graph on the bottom right shows the data relating to infections (above) and deaths (below) in the UK since the beginning of the pandemic. The number of deaths in the second wave in early 2021 was slightly higher than in the first wave in April 2020, although the number of infections in the second wave was ten times higher than in the first wave. Although there is always a certain time lag between infections and deaths, no significant increase in deaths has been seen to date.

This is also confirmed by the expectation of the UK scientific advisers, who foresee between 100 and 200 deaths a day at the peak of the current wave (source: https://www.bloomberg.com). This represents one-tenth of the previous peak, in line with the mortality rate of the table above.



Source: Centers for Disease Control and Prevention (CDC)



Source: Johns Hopkins University

(continued)

If confirmed, the numerical evidence presented so far suggests that the Delta variant may be far less worrisome than feared. The risk, therefore, is of an overreaction both on the part of citizens and businesses, delaying the normalization process, and on the part of governments which could impose new restrictions on mobility, also with a negative impact on economic growth. Of course, we fully support prudent and responsible behavior in the fight to eradicate covid-19, but the economic and social fallout caused by the new restrictions should be assessed.

Let us turn our focus to central banks and the Fed in particular. Over the past few weeks, Powell and several other Fed governors have reiterated the need to maintain monetary stimulus due to fears that the economy will slow too much once the fiscal stimulus ends.

Certainly the real GDP growth rate of the US economy will drop from the + 8% (real) expected for the quarter just ended towards more normal values. Nonetheless, the reopening process is just beginning and thanks to the savings accumulated over the last year, US consumers can keep spending for a few more quarters.

The point is that expectations play a key role in determining what will actually happen in the real economy and in financial markets: the more central banks talk about a possible economic slowdown and governments about new restrictions, the more they contribute to the materialization of that economic scenario that perhaps would not have occurred without all this emphasis on what can possibly go wrong.

The data published last Friday is a good indicator to validate this point. The first release was the retail sales for June where the “slowdown” narrative was not yet mainstream. The consensus expectations announced only a few days earlier were influenced by this narrative, and were pointing to a weak reading. The actual data published was instead a very strong one on an absolute basis and also well above consensus expectations, even considering a moderate downward revision for the previous month. Later in that day, the University of Michigan Consumer Sentiment index was also published. The poll was run in July when the slowdown narrative was more widespread and not surprisingly, the index came out well below expectations.

Probably, the real risks related to the current wave of Delta-variant are being overplayed by policymakers to give an extra push for vaccination before the next winter. Let's hope they get the desired effect without the economy being unduly affected.

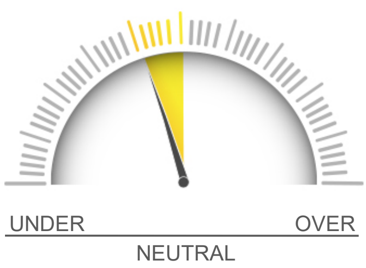
Asset Allocation View

	Under	Neutral	Over
Equity			
Developed Markets	■		
Emerging Markets	■		
Fixed Income			
Developed Markets Sovereign	■		
Developed Markets Corporate		Upgrade	
Emerging Markets		■	
Commodities			■
Currencies	*Commentary below*		

UNDER NEUTRAL OVER

Equity

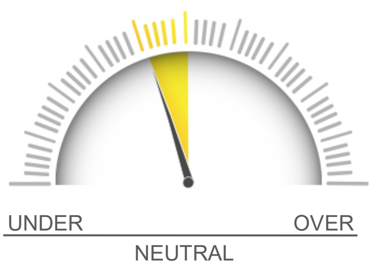
Developed Markets



We maintained our recommendation on Developed Markets Equities to **Slightly Underweight**. The spread of the delta variant is currently the main concern for equities, as valuations, which are already at high levels, would become more stretched if earnings expectations were to be revised downwards. On the other side, falling sovereign yields and deeply negative real rates are supportive for equities. As a consequence, while we are increasingly cautious on the asset class, we are only recommending a slightly underweight position. Within equities, we have a preference for more defensive ones.

US	Neutral	**Europe**	Over	**Japan**	Neutral

Emerging Markets

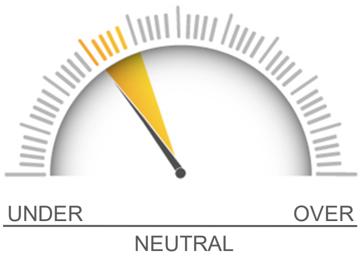


We lowered our recommendation on Emerging Markets Equities to **Slightly Underweight**. Due to the spread of the delta variant, global growth is expected to slow down, weighing in particularly on emerging markets. Consequently, among regions we no longer favor EEMEA and Latin America, the regions most exposed to global growth as they are important commodity exporters. On the contrary, we are turning more positive on Asia, as last week China took the first market-friendly step in a few months, lowering the reserve requirement ratio (RRR) to provide liquidity to the economy.

Asia ex-Japan	Neutral	**EEMEA**	Neutral	**LATAM**	Neutral

Fixed Income

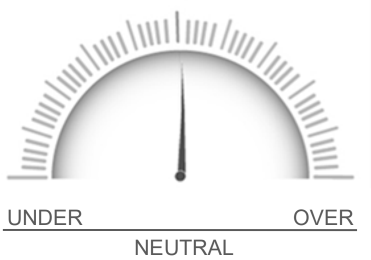
Developed Markets Sovereign



We maintained our overall **Underweight** recommendation on Developed Markets Sovereign Bonds. The recent decrease of nominal rates has been mostly due to concerns about the Delta variant and the expected slowdown in the GDP growth because of the waning effects of the fiscal stimuli. Over the medium term, we still expect to see higher rates due to eventual tapering by central banks, a not-so-transitory inflation and more limited than expected fallouts from the delta variant. In terms of regions, we are taking profit on the overweight on EU Periphery bond.

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

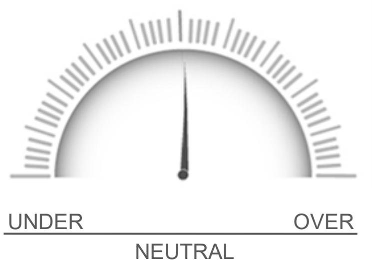
Developed Markets Corporate



We upgraded our recommendation to **Neutral** on Developed Markets Corporates. Within DM Corporates we prefer bonds on the short-end of the curve with acceptable ratings to mitigate the current phase of possible increase in risk aversion on financial markets. We continue to dislike long dated IG bonds due to their yields not being so different from sovereign bonds, and are therefore exposed to downside when rates will normalize. Considering the increasingly uncertain scenario priced in by the sovereign bonds, we prefer to move to a more cautious stance in the crossover/high yield segments, even if central banks monetary policies remain fully supportive.

IG Europe	=	IG US	=	HY Europe	=	HY US	=

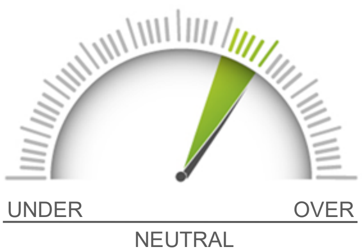
Emerging Markets



We kept our recommendation as **Neutral**. Emerging Markets Bonds spreads have compressed less than the developed market bonds with similar risk. Considering the reduction in the long-end US rates and the fact that the Fed will wait some time before tapering, Emerging Market bonds could still be attractive even considering the possibility of a slower reopening due to the delta variant. For the EM Hard Currencies, we have a preference for low duration strategies.

Local Currency	=	Hard Currency IG	=	Hard Currency HY	=

Commodities



We increase our **Positive** view on the asset class. In particular we are getting more positive on precious metals as they should benefit from lower risk-free rates and rising inflation. Additionally, they could serve as an hedge in case of increased risk aversion. On the other commodities the view is more cautious, as the fear of a slower reopening and normalization due to the delta variant could cause a short term consolidation.

Precious	+	Energy	=	Industrial	=	Agricultural	=

Currencies

We have a neutral stance an all the currencies.

On the US Dollar, the huge fiscal deficits and deeply negative real rates are counterbalanced by the risk-off that is starting to develop in financial markets which usually triggers margin calls in USD.

The Euro is supported by a more favorable real rate differential against the USD, but it’s the region where governments may more likely impose additional mobility restrictions due to the Delta variant.

The Yen is no longer serving as an hedge during phases of risk aversion, as it has been trading around 107 +/-5 USD for about three years.

Emerging Market currencies are also expected to remain fairly stable, as the risk of a slower global growth is offset by lower US risk free rates.

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