Investment Report for the 12 Months to 31st December 2020

KBIGI

Market Background

In the 12 months to 31st December 2020, the MSCI world equity gross return index rose by 6.3% in euro terms, and the ML over 5-year EMU Government Bond Index rose by +7.4%

From a regional perspective, North American equities increased by 10.0%, Pacific ex Japan equities decreased by 2.2% as European equities declined by -1.0%. Emerging markets rose by 8.5%, ending with a very strong final quarter in 2020. All sectors ended in positive territory, as the IT sector made significant gains while the Energy sector was the weakest sector. The Bloomberg Commodities Index fell by 11.1%. On the currency front, the euro strengthened against the US Dollar by 9.0% and against Sterling by 5.6%, reflecting political uncertainties in the US elections and relating to Brexit uncertainties in the UK during 2020.

Stock investing was a rollercoaster in 2020. Arguably more the ever, the wrenching reality of radical uncertainty dominated all. From the pandemic-induced collapse in Q1 to the sharp stock market recovery following it, it was an extraordinary year. Policy makers' aggressive policy responses early on, and the rapid vaccine development spurred investor confidence following Q1 as markets remained largely bullish the rest of the year. From a style perspective, growth heavily outperformed value, as the dislocation between share prices and underlying fundamentals continued to widen, and the continued rally in tech stocks was sustained through 2020. More recently in Q4 we have seen a reversal of this trend with value outperforming growth and signals of a rotation in the market towards more cyclical stocks. In contrast to stock markets, many economies entered a recession during 2020 with unemployment levels reaching record highs in some areas. China was the only major economy to report economic growth over the year.

2020 marked one of the hottest years on record, 1.25C hotter than pre-industrial levels. Commitments to emission reductions were widespread across countries such as China and the EU. Against this backdrop, global ESG funds surged over 2020 as supporting regulation increased, including the finalisation of the EU Sustainable Finance Disclosure Regulation and the Biden administration re-joining the Paris agreement putting climate change action back on the US agenda.

Investment Strategy

We enter 2021 with much hope and confidence for a return to 'normal' following a turbulent 2020. While Covid news continues to dominate global headlines, global markets entered 2021 with the same optimism that dominated the final months of last year. This optimism, fuelled by the strong combination of central bank liquidity, increasing signs of governments opening their fiscal taps and, now, the very tangible evidence of vaccine rollout that will only continue to accelerate.

Our central scenario is that from late spring onwards the global economy and company earnings will experience strong recoveries from the pandemic-induced declines of last year. We expect investor rhetoric to be very different to 2020 as we now speak of vaccine and not virus; fundamentals-driven rather than liquidity-driven; reflation rather than deflation; re-opening rather than closing; return to work rather than from work from home etc. Such an outcome is consistent with further positive returns from global equities while expecting fixed income markets to struggle and underperform

The performance of the year ahead will be very dependent on investor confidence in the recovery envisioned above, but also importantly that the recovery is sustained into 2022 and beyond. This central assumption provides strong fundamental conditions for active managers to find investment opportunities in a rotation towards new winners such as value sectors, smaller capitalisation stocks and, for example, non-US developed as well as emerging markets.

Undoubtedly challenges remain, not least potential delays in vaccine rollout and/or further severe Covid relapses. Inflation may grab more attention which could itself pressurise low bond yields, resulting in a steepening of yield curves, and consequently undermining of equity markets. We will also continue to monitor geo-political fallout from Brexit and the myriad of US political events.

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