Amplia Monthly Investment Letter

2020 – a moody year that accelerated change

2020 will be remembered as a mercurial and peculiar year. The COVID-19 outbreak stole the limelight and sometimes one had the impression that there was no life beyond the pandemic.

2020 however also put an end to some central themes that had dominated the world politics and, as a result, framework for capital markets for a long time. In Europe, the European Union emerged from the crisis stronger than ever. The outbreak of the virus cast the usually quarrelsome member states in front of a new breed of crisis: something that was not just about agricultural subsidies, acceptance of new member states or loan guarantees to the peripheral countries. For the first time, the crisis was considered so imminent that sweeping policy unity was achieved. The swift policy response meant a considerable leap towards a fiscal union with greater common liabilities and centralised budget discretion. It however also meant a stronger commitment to foster a greener future, with sustainability strings attached to the long-term growth funding. The policy response also served as a subtle signal towards China, Russia and the US about the Union's new ability to response with greater determination to developments it regarded as threatening.

2020 also put a lid on the arduous Brexit process that had weighed on currencies and stock markets for four and a half years. The unhappy marriage is over, and the divorce settlement is known. The British got back their sovereignty at a considerable price, with free trade resuming only in goods but not in services. Notably, the UK has a comparative disadvantage in the former and a comparative advantage in the latter. Still, everyone can be happy about the trade deal, as the alternative would have been an abrupt end to all free trade amid the pandemic. Also, whilst Brexit left the door open for new independence votes in Scotland and Northern Ireland, the negotiation process showed that the EU was a formidable opponent thanks to its economic size. The bloc did not have to make many concessions on key questions. This will also have repercussions for countries like Switzerland who will see clearer demands from Brussels to fully align their regulation to a "level playing field" instead of just picking parts of it to keep the access to the single market for various products and services.

In addition, 2020 saw the end of the Trumpian era. The new Biden administration has signalled its determination to return to multilateralism. This turnaround in the US will be greeted by international organisations such as the UN and WHO that became the target of fierce criticism and funding cutting threats by Mr. Trump and his staff. On the other hand, a harder stance towards China is likely to stay, with both the EU and the US staying more vigilant and suspicious towards Chinese firms and suppliers. This, combined with the supply chock from idle factories during the pandemic, might have a long-lasting impact on global supply chains, and globalisation as a whole.

Most importantly, if the US re-joins the Paris Climate Agreement, it will give a massive boost to green investment. A US version of the "Green New Deal" may see parliamentary tailwinds when the public opinion gradually shifts towards acknowledging the climate change. At any rate, we are likely to see European-style state aid to projects and investment that tackle the climate change.

Finally, the digitalisation of our lives took a big step forward during the pandemic lock-downs. Increased home office and virtual meetings are here to stay. E-commerce and food delivery platforms gained considerable market share. Video streaming and gaming markets grew at a high pace. Hence, the winners from the pandemic 2020 are those firms that either contribute to a greener society or digitalise our everyday life.

2021 – a new beginning

With virologists mostly agreeing about a gradual fade-out of COVID-19 by the second half of 2021, one can be optimistic about the new year. Political risks are receding. Both monetary and fiscal authorities have pledged their willingness to keep the policies accommodative well into the future, practically as long as needs be. Realised GDP numbers from 2020 did not come out as negative as initially feared, nor did swaths of bankruptcies ever materialise.

For 2021, the consensus forecasts assume the US real GDP to grow by 3.9%, Eurozone by 4.6%, the UK by 5.4% and China by a whopping 8.2%. Combine this with the globally loose monetary policy and stock market valuations that are not so far off their historic means, we feel optimistic about the prospects of equities in 2021.

How should investors build their equity portfolios then? In our view, the core should be formed by combining monopolistic companies with those that address one of the megatrends of our time. Monopolistic companies would include dominant firms with high operating margins such as Microsoft, Alphabet, ASML and LVMH, whereas the latter group comprises of firms with answers to themes such as climate change, automation, 5G, urbanisation or aging.

On the tactical side, especially British and Chinese (both Hong Kong and mainland) shares offer plenty of value both in relative terms and compared to their historical averages. For instance, FTSE 100 is trading at a forward P/E of 14.7 (based on 2021 earnings) which is low compared to any other developed world major stock index. The British index ended 2020 -14.3%, which sharply contrasts with the high double-digit gains of the most Northern American indices. Meanwhile, the uncertainty from the EU trade negotiations is gone and the UK interest rate policy will remain accommodative well into the future. A step further would be the mid-cap index FTSE 250, whose companies derive half of the earnings from the domestic economy. FTSE 250 is a cyclical index as financials, industrials and consumer services are heavily presented in it.

Considering the improving world economy and falling risk premia, it is increasingly difficult to find moderately priced bonds. Gold rallied 6,2% in December so we are increasingly neutral on it as well. At present, portfolio diversification tools are best found in traditional, long-term good quality bonds, if any.

On 4th January 2021,

with kind regards

Juho Kivioja

Juho Kivioja, CFA | Chief Investment Officer | Amplia & Co. AG | Münstergasse 18 | CH – 8001 Zurich | Switzerland