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PORTFOLIO UPDATE
AUGUST 2021

MONTHLY REVIEW

July proved to be a summer month with a wake-up call. The earnings season was picking up pace during July, while the markets had already begun the month at record highs in some cases. As a result, expectations regarding the quarterly numbers were high.

Before the earnings season really got under way, there were some rapid sell-offs on the equity markets that were accompanied by pressure on the yield curve. Yields of 10-year US Treasuries, which were already down on the prior month, swiftly dropped by a further 0.2 percentage points to 1.15%. Equity markets including Germany's DAX index shed in excess of 2% in a single day. It was a similar story on equity markets elsewhere. Once again, the reason for this – albeit short-lived – turmoil was Covid-19, or its variants to be precise. The persistent Delta variant sparked doubts among investors about the growth prospects that had been priced in, triggering a small sell-off on the broader market. At the same time, the shares of vaccine manufacturers hit fresh highs. The current significance of this segment of the pharmaceutical sector was underlined by the inclusion of Moderna in the S&P 500 benchmark index. The wave of selling was also fuelled by stop-loss orders being triggered as well as by snap decision-making among market participants. Investors who had bet on falling stock prices were then disappointed a day later, which saw them caught on the wrong foot. As a result, they were forced to buy stocks to cover their positions, in turn bolstering a rapid share price rally.

Financial markets 2021 total return

Equities	July	2021
S&P 500 (US)	2.4%	18.0%
Dow Jones Industrial Average (US)	1.3%	15.3%
EURO STOXX 600 (EU)	2.1%	17.5%
DAX (DE)	0.1%	13.3%
SMI (CH)	1.5%	16.3%
MSCI Emerging Markets (EM) in USD	-6.7%	0.3%
Fixed Income	**July**	**2021**
US Corporate Bonds Inv. Grade	1.4%	0.1%
US Corporate Bonds High Yield	0.4%	4.0%
Pan- Europe Corporate Bonds Inv. Grade	1.3%	1.2%
Pan- Europe Corporate Bonds High Yield	0.5%	4.0%
Alternative Investments	**July**	**2021**
Gold	2.4%	-4.2%
Oil (brent)	0.3%	47.3%

Sources: swisspartners, Bloomberg

This recovery was boosted by the quarterly earnings releases, which were predominantly good. As of the beginning of August, the majority of companies are expected to have submitted their figures. In spite of what were already high expectations, most companies comfortably beat the consensus forecasts in terms of both earnings and growth. However, based on the releases to date, the guidance issued suggests that pent-up and changing post-crisis demand – and therefore upside surprises to growth – cannot be maintained indefinitely. Investors should keep a close eye on the current reporting season as it is illustrating how the economy can recover from the various lockdowns and what the trajectory going forward might look like.

MANDATE RETURNS GROSS

	Euro			Swiss Franc			US Dollar			British Pound		
	Cons	Bal	Dyn	Cons	Bal	Dyn	Cons	Bal	Dyn	Cons	Bal	Dyn
2012	6.6%	7.4%	10.5%	4.3%	6.5%	10.9%	5.9%	8.4%	11.8%			
2013	1.5%	6.5%	13.5%	1.9%	8.3%	16.7%	2.9%	9.4%	18.5%			
2014	6.1%	8.0%	10.2%	4.9%	6.5%	9.2%	1.6%	2.2%	3.1%			
2015	2.7%	6.3%	9.9%	-0.8%	0.0%	1.8%	-0.3%	0.0%	1.0%			
2016	2.3%	5.3%	7.1%	1.3%	3.9%	5.7%	2.8%	6.2%	7.2%	4.6%	9.5%	12.1%
2017	3.5%	7.3%	10.8%	4.3%	8.9%	15.0%	7.1%	12.7%	18.1%	4.7%	8.7%	14.2%
2018	-4.3%	-9.0%	-10.5%	-5.6%	-10.1%	-12.1%	-2.5%	-7.9%	-9.8%	-3.3%	-8.6%	-10.4%
2019	9.2%	15.7%	21.6%	8.3%	14.8%	19.6%	11.5%	17.5%	22.0%	9.4%	15.3%	19.8%
2020	3.2%	5.3%	8.6%	2.6%	5.5%	9.0%	6.7%	9.7%	13.6%	4.6%	6.5%	10.3%
Jan 21	0.2%	0.3%	0.8%	0.2%	0.2%	0.8%	0.0%	0.1%	0.5%	0.0%	0.0%	0.3%
Feb 21	0.3%	1.3%	2.1%	0.7%	1.8%	2.6%	0.3%	1.3%	2.1%	-0.1%	0.6%	1.4%
Mar 21	0.9%	2.1%	2.8%	1.1%	2.4%	3.1%	0.2%	1.1%	1.6%	0.4%	1.5%	2.2%
Apr 21	1.4%	2.2%	3.0%	1.2%	2.0%	2.7%	2.0%	3.1%	4.0%	1.9%	2.9%	3.9%
May 21	0.5%	0.6%	0.6%	0.5%	0.6%	0.6%	0.9%	1.2%	1.2%	0.3%	0.3%	0.2%
Jun 21	0.8%	1.4%	2.1%	0.7%	1.3%	2.0%	0.1%	0.4%	0.9%	0.7%	1.3%	2.0%
Jul 21	0.3%	0.0%	0.2%	-0.2%	-0.7%	-0.6%	0.4%	0.0%	0.2%	0.2%	-0.2%	0.0%
2021	4.4%	8.0%	12.1%	4.2%	7.7%	11.7%	4.0%	7.3%	11.0%	3.5%	6.5%	10.4%

Actual portfolio returns may differ from the values shown above owing to the level of implementation, costs and restrictions on implementation.

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Portfolio Update

August 2021

Transactions in June & July

For a detailed overview of the transactions for each strategy, please do not hesitate to contact us.

Positioning

Liquidity (neutral)	Conservative 3.5% Balanced 4.5% Dynamic 3.5%	Outside of the US dollar investment universe, there are few opportunities to avoid the negative interest rates applied by the central banks. If necessary, we are parking excess liquidity in cash and accepting a negative return, which is partially passed on to customers, especially as there are no other risk-free alternatives. Short-dated bond and trustee investments offer opportunities in US dollars.
Bonds (underweight)	Conservative 48.0% Balanced 25.0% Dynamic 6.0%	In light of increasing debt levels in the public and private sectors, we favour bond issuers with solid balance sheets, a healthy business model and correspondingly good credit ratings. At the same time, however, the only way of achieving a positive yield to maturity is to take positions outside of the AAA/AA rating segment. Within the asset class, we utilise various bond types and market segments to maintain a cautious approach, including in the lower rating categories. As scope for further rate cuts is limited, we are keeping the duration (interest rate risk) low in the portfolio, which affords greater protection against sudden rises in interest rates. Given the recent rise in bond yields, opting for a low duration has worked out well. The current level now offers potential leeway to generate better returns on the fixed income front.
Equities (overweight)	Conservative 27.5% Balanced 52.0% Dynamic 76.5%	The Covid-19 pandemic maintains a firm grip on the global economy and the stock markets. While vaccines are being administered throughout the world and the level of vaccination coverage is constantly rising, new variants of the virus pose a risk to the economic recovery. Investor attention is currently focusing on southern European countries and Asia, where delays to the easing of restrictions are stalling the prospects of a return to normality. Nonetheless, the prevailing mood remains upbeat as the latest scientific guidance shows that mRNA vaccines provide adequate protection against the virus. Other reasons for maintaining an overweight position in equities include ultra-loose monetary policy, the vast fiscal policy support programmes implemented by governments, the dearth of alternative investment options on the financial markets and better-than-forecast company results so far. If these supports are removed, the situation will have to be reassessed. In particular, it is worth keeping a close eye on the upcoming reporting season.
Alt. investments (overweight)	Conservative 21.0% Balanced 18.5% Dynamic 14.0%	A broadly diversified portfolio of gold, cat bond funds, market-neutral equity and credit strategies, global macro, commodities and option-based arbitrage/volatility hedging strategies. In contrast to traditional asset classes, these instruments exhibit low levels of correlation and offer a degree of protection from geopolitical risks. In normal market conditions, the aim is to achieve a positive market yield while minimising volatility. A high level of liquidity is a fundamental requirement.

Outlook

China cracks down

Investors who put their money into Chinese equities in 2020 were rewarded with bumper gains of 30% or more. The returns were even more bountiful for those who predominantly backed China-based companies that are listed abroad, as the chart below shows. It is worth bearing in mind that all of this occurred in the year in which the world was first ambushed by the coronavirus pandemic.

Early this year, the overwhelming consensus among analysts was that investments in China would also be highly lucrative in the longer term thanks to the country's robust economic growth. Less than seven months later, analysts are now less vociferous in offering their opinions, projections are more restrained and portfolio holdings have shrunk markedly (also shown in the chart below). Yet for once, the crisis is not attributable to an ailing economy, but the measures taken by a government that feels increasingly under threat.

NASDAQ Golden Dragon China equity index

(publicly traded in US but majority of business in China)

Sources: Bloomberg

Following the recent penalisation of internet giant Alibaba, entertainment firm Tencent, online taxi provider Didi and takeaway delivery company Meituan, private education providers have become the latest targets of a regulatory crackdown by the Chinese authorities. Rags-to-riches careers and growth stories along the lines of Microsoft have become more than purely western phenomena for some time now as a result of digitalisation, with private firms worth billions of dollars mushrooming in China too. Lately, these companies have been putting public-sector businesses in the shade due to their soaring market valuations, making them a potential problem for the Chinese government. The customer base, data archives, market power and influence of these companies have grown on a scale that the Chinese Communist Party now seems unable to tolerate.

Social inequality and the challenges created by the demographic shift towards an ageing population in China are key drivers behind the party's recent interventions. While other nations have already reached high levels of income, China remains dependent on above-average economic growth. One way to achieve this is via population growth and a resultant boost to employment. But the mounting cost of education due to profits being maximised by private providers, which is one of the factors dissuading parents from having a second child, is precisely what drove the Chinese government to upend the whole sector and force its withdrawal from the international capital markets.

Share prices in the health care and real estate sectors have also plummeted in response. Costs have soared to astronomical levels in both sectors over the last few years, giving families all the more reason to limit the number of children they have. Thus, the equity market may well have been quick to anticipate further regulatory measures in these sectors. In any case, it is advisable to proceed with caution at present. Anything that undermines the party's growth policy, promotes social inequality or distorts competition is at risk of being reined in by the Chinese government. The list of examples will only become longer.

Nonetheless, we recommend holding on to existing investments. The relative growth potential, increasing market power, diversification aspects and current attractive valuations are just some of the reasons why it will be worth retaining an allocation in the portfolio. The crucial question is how to do so. In this respect, it is important to avoid individual positions for the most part, while taking advantage of the diversification potential offered by collective investments. This would lessen the impact of any near wipe-outs, such as that suffered by TAL Education Group stock (TAL US), thanks to the cushioning of other investments. Caution is also advised with regard to ETFs, especially where positions are weighted in line with the market capitalisation of the underlying companies. It is well known that large – and therefore heavily weighted – companies tend to enjoy a monopolistic position on the market, which makes them potential victims of the Chinese regulators. In general, passive investment products should only be favoured in a liquid, transparent and efficient market.

When selecting fund products in the current setting, it would be best to opt for those with active managers who know which sectors and companies to over- or underweight thanks to their many years of local expertise. Compared to passive investments, experienced investors have been achieving significant added value – particularly in 2021 – as they have accurately predicted the actions of government authorities. It goes without saying that we are always on hand to support our clients in selecting the right fund investment.

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