Julius Bär

# INVESTMENT GUIDE

## Market Outlook Q2 2020

MARKETING MATERIAL

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Julius Bär

# EDITORIAL

Dear reader,

The shock of the coronavirus pandemic came when the global economy was gradually accelerating. What we initially interpreted as a problem mainly in China, now seems to be leading us to the first global recession caused by an exogenous shock.

The current crisis is opening up on three fronts. Firstly, in the most-affected countries it is still unknown when the contamination figures will peak and/or when there will be an effective treatment or vaccine. Secondly, the financial system needs to stabilise. In this regard, the first signs are encouraging. Finally, and most critically, the pandemic is having an unprecedented impact on the real economy. Overnight, the income of many self-employed workers and small, medium-sized and even multinational companies fell to zero for an uncertain period of time. This phenomenon threatens to trigger a cascade of payment defaults. Unprecedented budgetary support measures are needed.

Depending on current governments' abilities to respond, the performance of the main asset classes will diverge dramatically in one direction or the other over the next 9 to 12 months.

With our second quarter Investment Guide, we hope to help you navigate through the current uncertainties successfully. Never before have we experienced a market context with so little visibility, but the market abounds with opportunities.

Yours faithfully,

**Yves Bonzon**

Group Chief Investment Officer

Member of the Executive Board

**Christian Gattiker**

Head of Research

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# A LOOK BACK AT Q1 2020

# MARKET REVIEW

## 2020 started so promisingly for financial markets and then the coronavirus came along. It is hard to believe that at one point the S&P 500 index was down 34% from the 2020 high. Let's delve deeper to see which areas fared best in the crisis.

## EQUITY REGIONS

| | 2015 | 2016 | 2017 | 2018 | 2019 | YTD | 5Y annualised |
|---|---|---|---|---|---|---|---|
| Emerging markets | -14.92% | 11.18% | 37.28% | -14.50% | 18.39% | -24.74% | -1.53% |
| Switzerland | 1.18% | -3.42% | 17.47% | -8.03% | 29.98% | -15.51% | 1.97% |
| Eurozone | 8.23% | 2.58% | 10.24% | -10.57% | 26.05% | -24.14% | -2.76% |
| USA | 0.69% | 10.89% | 21.19% | -5.04% | 30.88% | -23.79% | 4.83% |
| Japan | 9.93% | -0.74% | 19.75% | -15.15% | 18.48% | -15.30% | -2.00% |
| UK | -2.21% | 19.16% | 11.71% | -8.82% | 16.37% | -24.37% | -1.26% |

THE BEST: It's probably best to refer to the least poorly performing markets to date in Q1 2020, given the global impact of the coronavirus pandemic. Having contained the virus, China actually recorded the best performance in this period. Switzerland and Japan were close runners-up which is not unsurprising given that investors tend to focus on safe-haven currencies in times of stress.

THE WORST: Emerging markets, the UK, the eurozone and the USA have been contending with a wave of nervous investor selling since mid-February. Emerging markets were faced with a stronger dollar and in developed markets investors panicked as they faced the prospect of an unexpected and abrupt end to the longest economic cycle in history.

## EQUITY STYLES

| | 2015 | 2016 | 2017 | 2018 | 2019 | YTD | 5Y annualised |
|---|---|---|---|---|---|---|---|
| Quality | 3.71% | 4.55% | 25.96% | -5.50% | 36.08% | -19.20% | 6.49% |
| Value | -4.82% | 12.33% | 17.10% | -10.78% | 21.75% | -29.54% | -1.69% |
| Growth | 3.11% | 2.80% | 28.01% | -6.74% | 33.68% | -18.50% | 5.17% |
| Large cap | -0.96% | 7.51% | 22.21% | -7.75% | 27.73% | -23.06% | 2.32% |
| Small cap | -0.31% | 12.71% | 22.66% | -13.86% | 26.18% | -32.81% | -1.40% |
| Cyclicals | -0.13% | 10.58% | 27.54% | -9.83% | 31.54% | -22.80% | 4.70% |
| Defensives | -0.64% | 4.07% | 14.94% | -4.94% | 21.69% | -21.30% | 1.20% |
| High dividend | -3.20% | 9.29% | 18.14% | -7.56% | 23.15% | -26.03% | 0.18% |

THE BEST: Growth and Quality stocks performed marginally better than their alternatives. Doubtless their structural growth opportunities and first-class balance sheets, were the lure that nervous investors were looking for.

THE WORST: Small caps suffered because of their inherent higher risk of bankruptcy and tendency to behave in a more volatile manner in times of market stress; value stocks bore the brunt of dramatically falling bond yields; and high-dividend stocks were shed as investors feared dividend cuts.

# EQUITY SECTORS

| | 2015 | 2016 | 2017 | 2018 | 2019 | YTD | 5Y annualised |
|---|---|---|---|---|---|---|---|
| Information technology | 4.76% | 11.45% | 38.23% | -2.60% | 47.55% | -16.08% | 13.73% |
| Materials | -15.26% | 22.46% | 28.94% | -16.92% | 23.35% | -28.09% | -1.64% |
| Oil & gas | -22.80% | 26.56% | 4.97% | -15.84% | 11.45% | -46.84% | -13.01% |
| Industrials | -2.06% | 12.88% | 25.23% | -14.54% | 27.77% | -27.92% | 0.07% |
| Communications | 2.54% | 5.66% | 5.82% | -10.02% | 27.39% | -20.89% | 0.19% |
| Healthcare | 6.60% | -6.81% | 19.80% | 2.52% | 23.24% | -18.43% | 2.05% |
| Financials | -3.37% | 12.47% | 22.73% | -16.97% | 25.51% | -32.61% | -2.52% |
| Consumer cyclical | 5.48% | 3.14% | 23.69% | -5.51% | 26.57% | -22.19% | 2.69% |
| Consumer defensive | 6.36% | 1.63% | 17.04% | -10.10% | 22.80% | -18.31% | 1.74% |
| Real Estate | 0.23% | 2.82% | 14.64% | -6.36% | 22.96% | -26.92% | -2.13% |
| Utilities | -6.61% | 5.96% | 13.66% | 1.97% | 22.53% | -19.31% | 2.79% |

THE BEST: Information technology stocks remained the leaders of this pack in Q1 with consumer defensives and healthcare following closely on their heels. Given the advent of enforced home-office on laptops, children remote-learning, panicked food stockpiling and medics falling over themselves in the quest to find a cure for Covid19 it is no surprise why these stocks remained popular.

THE WORST: Oil and gas stocks were bottom of the league, down more than 45% in the quarter. As the price of oil sank to its lowest levels in two decades, investors shied away from the structurally challenged oil & gas sector. OPEC's failure to reach an agreement with Russia was a black swan event but once oil prices turn the corner we would expect to see buyers returning.

# FIXED INCOME

| | 2015 | 2016 | 2017 | 2018 | 2019 | YTD | 5Y annualised |
|---|---|---|---|---|---|---|---|
| **Developed markets:** | | | | | | | |
| Government bonds | -3.29% | 1.65% | 7.29% | -0.38% | 5.59% | -1.00% | 2.19% |
| TIPS | -4.97% | 3.91% | 8.67% | -4.11% | 8.04% | -5.34% | 1.17% |
| High quality IG | -6.44% | -0.82% | 11.59% | -3.54% | 6.33% | -5.00% | 0.75% |
| Low quality IG | -5.91% | 3.63% | 11.94% | -3.90% | 12.52% | -9.56% | 1.59% |
| High yield | -2.72% | 14.27% | 10.43% | -4.06% | 12.56% | -18.87% | 0.86% |
| **Emerging markets:** | | | | | | | |
| EM hard currency | -0.18% | 9.00% | 9.61% | -3.02% | 12.13% | -11.09% | 2.29% |
| EM local currency | -10.38% | 5.86% | 14.27% | -3.40% | 9.47% | -8.85% | 0.99% |

TIPS = Treasury Inflation Protected Securities; IG = investment grade; EM = emerging markets

THE BEST: No surprises for guessing which part of the bond markets fared the best in these uncertain times. There was a veritable stampede into the benchmark of safe havens, government bonds, especially US Treasuries, which saw the yield on the 10 year benchmark fall to an unthinkable 0.54% at one stage.

THE WORST: High-yield bonds were the best performing segment in 2019 but unfortunately performed worst in Q1 2020. Investors piled out of risky names and into safer havens instead. This was driven not only by nervousness over the coronavirus and how it might impact highly leveraged companies, but also by the accompanying collapse in oil prices which hit the energy sector in high-yield bonds hard.

# COMMODITIES

| | 2015 | 2016 | 2017 | 2018 | 2019 | YTD | 5Y annualised |
|---|---|---|---|---|---|---|---|
| Brent Crude Oil | -34.97% | 52.41% | 17.69% | -19.55% | 22.68% | -59.33% | -13.51% |
| Natural Gas | -19.11% | 59.35% | -20.70% | -0.44% | -25.54% | -26.08% | -9.40% |
| Gold | -10.46% | 8.63% | 13.68% | -2.14% | 18.87% | 6.00% | 6.44% |
| Silver | -11.51% | 15.84% | 7.23% | -9.36% | 15.32% | -17.21% | -3.11% |
| Platinum | -26.24% | 1.11% | 3.62% | -14.80% | 22.05% | -25.37% | -8.60% |
| Aluminium | -17.90% | 12.52% | 33.31% | -19.28% | -1.84% | -15.15% | -2.92% |
| Copper | -24.44% | 17.35% | 31.73% | -20.28% | 6.31% | -20.13% | -4.70% |
| Iron Ore | -32.20% | 81.11% | -25.15% | 10.76% | 28.58% | 0.00% | 5.29% |

THE BEST: Gold has been the winner over the past six months as investors scrambled for safe-haven assets. It is the only asset on these pages to show a positive return YTD. Despite the gold price reaching multi-year highs on the back of global growth worries, we still see sustainable fundamental support for this commodity in the next quarter, especially as a recession now seems unavoidable

THE WORST: There are no prizes for guessing which commodity fared worst in the first quarter of the year. Having rallied nearly 23% in 2019, oil was off almost 60% YTD at the time of writing. With the double shock of pandemics and politics, the oil market is heading into a swelling surplus, pressuring prices and creating unprecedented uncertainty. The resulting tremors will burden the oil business for years to come.

**Source:** Bloomberg Finance L.P., Julius Baer Investment Publishing
Please see the appendix for more details on indices used. Annual performance numbers in USD except for equity regions, which are calculated in local currency. Year-to-date (YTD) numbers are as of close of business on 25 March 2020.
Past performance is not a reliable indicator of future results. Performance returns take into account all ongoing charges but not transaction fees. The value of your investment may fall as well as rise meaning that you may not get back your initial investment.

# SCORING OUR CALLS

In Q1 2020 we saw opportunities in value stocks and emerging market equities, put the focus on politics, looked for ways to deal with low rates and invested in innovators and disruptors.

## THE MACRO PICTURE

| TOPIC | YTD RETURN |
|---|---|
| Emerging markets – China | -8.4% |
| European value stocks | -24.3% |
| Global value stocks | -26.2% |

## POLITICS

| TOPIC | YTD RETURN |
|---|---|
| Cross-asset solutions | 0.38% |
| Healthcare | -13.9% |

## DEALING WITH LOW RATES

| TOPIC | YTD RETURN |
|---|---|
| US crossover bonds | 0.32% |
| Flexible fixed income strategies | 0.32% |
| Subordinated bank debt | -9.39% |
| Asian high-yield bonds | -11.58% |
| High-dividend equities | -19.88% |

## (R)EVOLUTION

| TOPIC | YTD RETURN |
|---|---|
| Innovators and disruptors | -15.23% |

**Source:** Julius Baer Investment Publishing
Year-to-date (YTD) numbers are as of close of business on 30 March 2020.
The performance of our calls was evaluated on the basis of the performance of an underlying benchmark index which we feel best fitted the call. More information on these benchmark indices are shown in the appendix.
Past performance is not a reliable indicator of future results. Performance returns take into account all ongoing charges but not transaction fees. The value of your investment may fall as well as rise meaning that you may not get back your initial investment.

# 5 QUESTIONS ON ASSET ALLOCATION

## AN INTERVIEW WITH OUR CIO

The relentless cascade of news can become confusing for investors and make investment decisions challenging. So how should investors decide how to allocate assets across different asset classes? When should they make changes to their asset allocation? And in the current environment, particularly in light of the coronavirus outbreak, what should investors do?

Yves Bonzon, our Group CIO, shares his thoughts with us on these questions and more.

# 5 QUESTIONS ON ASSET ALLOCATION

## An interview with Yves Bonzon, Julius Baer's Group Chief Investment Officer.

### 1 LET'S START BY GOING BACK TO BASICS. WHAT DO INVESTORS NEED TO THINK ABOUT WHEN DECIDING HOW TO ALLOCATE THEIR PORTFOLIO ACROSS DIFFERENT ASSET CLASSES?

The fairly constant barrage of news that we face can become confusing for many investors and it's easy to understand why. The quantity of information available to us can be overwhelming and what we read and hear can influence our thought processes and investment decisions. The key for investors is to define precisely what level of risk they are willing to accept. Investors should think hard about the maximum drawdown that they can stomach without taking emotional risk reduction decisions. Stress testing one's strategic asset allocation in historical market downturns provides valuable information. If the strategy is well calibrated and portfolio construction robust, risk taking will prove fruitful over time.

### 2 BUT IS IT REALLY NECESSARY TO TAKE RISK?

Unfortunately yes, especially under zero or negative risk free rate regimes. In fact, the return of a portfolio exceeds the risk-free rate over time precisely because one accepts the short-term risks involved with investing. Ideally a portfolio should be built to weather various stages of economic cycles, combining assets that respond differently to various economic conditions. One should not shun risk. The objective I prefer is to take good risks and diversify them. Diversification is emphasised by most investment managers but we would argue that a balance needs to be found between excessive concentration and excessive diversification, especially at the asset allocation level. Furthermore, liquidity risks and counterparty risks should always be properly managed.

## 6 POINTS TO CONSIDER WHEN INVESTING

1) Time is your friend
2) Spend a lot of time on portfolio construction
3) The sum of the parts is far more important than each individual part
4) Don't average down bad investments. They become an increasingly small problem
5) Don't look at your portfolio more than once a quarter
6) Spot and mitigate your behavioural biases

### 3

### IN RECENT WEEKS, EQUITY MARKETS HAVE BEEN IMPACTED BY THE SPREADING OF THE CORONAVIRUS. SHOULD INVESTORS CHANGE THEIR ASSET ALLOCATION IN SUCH CASES?

Investors should clearly not change their strategic asset allocation. This should be reviewed only once a year and have a five year time horizon. It can be changed on an exceptional basis in between annual reviews if extreme valuation changes have taken place. In light of recent events and the surge in the forward-looking credit and equity risk premia, investors should actually increase risk assets if they review their strategic allocation and want to refresh it. If they are tempted to reduce risk assets then their strategic allocation was too risky before the corona crisis. At the tactical level, it's extremely hazardous to reduce or increase risk during such turbulent times, in particular in this case given the external nature of the trigger for the market decline. The truth is, that unlike in the Great Financial Crisis in 2008, no one knows when life will return to normal, how much damage private agents will have incurred by then and how comprehensively and effectively governments will have responded.

## 4 SO IN THE CURRENT ENVIRONMENT, WHAT SHOULD INVESTORS DO?

First and most critically, they should refrain from reacting emotionally to recent mark-to-market losses. Ideally, they should try not to follow markets day by day and take a medium-term perspective. They should remember that when uncertainty is as high as it is today, the prudent approach is to stay close to one's strategic asset allocation. This is not the time to crystallise losses by selling low or to throw good money after bad. If their actual portfolio has drifted significantly away from their target allocation, they might consider rebalancing at some point but being mindful of the fact that they will not have many such opportunities if the bear trend lasts longer then expected.

## 5 WHAT'S THE KEY TO ALLOCATING A PORTFOLIO OF ASSETS TO GENERATE THE MAXIMUM POSSIBLE RETURNS IN THE LONG-TERM?

The key is not to change course under market stress. This requires careful calibration of the asset mix and an understanding of the entire distribution of the portfolio's return - bad and good. In other words, always keeping in mind that this distribution has a left but also a right side. Missing out on strong days and markets costs far more than suffering short-term setbacks.

## SECULAR TRENDS – OVERVIEW

**MACROECONOMIC TRENDS**

- Bipolar Sino-US World
- Energy abundance
- Reshoring
- Stakeholder economy
- Unorthodox macro policies
- Life science disruptions

**CAPITAL MARKET TRENDS**

- Late-stage US dollar bull market
- China becoming a core asset class
- Rise of political triggers and decline of market signals
- Public equities challenge median private equity returns

**KEY RISK FACTORS**

- Dormant systemic risk
- Rise in cyber risk
- Global political risk
- China-US decoupling

**Source:** Julius Baer Investment Management

# THE MACRO PICTURE

## Economic rebound after the heart attack

After a growth shock in the first half of 2020, we expect the economy to gain traction again, driven by specific sectors. A lavish monetary and fiscal policy should support the acceleration of growth. The main uncertainty currently revolves around how long and how widespread the abrupt halt in economic activity will be until the recovery starts. That said, the rise in unemployment will result in some consumption restrain and caps the economic recovery potential.

We have asked the opinion leaders of Julius Baer about how they see the second quarter of 2020 and where investors can find the best opportunities in the current environment.

# THE MACRO PICTURE

Christian Gattiker,
Head of Research

## WAITING FOR STABILISATION

“The virus shock most likely ended the current cycle. Yet major concerted stimulus both from central banks and governments should avoid the economic fallout of the crisis turning into a global depression. Financial markets have priced in a recession by and large at the end of Q1 2020. A new cycle will start in the wake of this period of stabilisation. Timing the low in economic activity and the subsequent rebound is clearly outside the scope of any economic analysis.”

## SUPPORTIVE GOVERNMENTS AND CENTRAL BANKS

“Policy makers around the world are now taking action to combat the recession. Governments and central banks have already announced massive support measures to help cushion the blow from the virus. We are convinced that central banks will use all their available policy options to limit the economic fallout. As monetary easing cannot do it alone, coordinated action with more expansionary fiscal policies is crucial to avoid a global depression.”

Sophie Altermatt,
Economist

David Kohl,
Head of Currency Research

## ECONOMIC UNCERTAINTY

“The increasingly harsh containment measures to slow the spreading of the virus, implemented in more and more economies, are stifling consumer and investor demand. The main uncertainty currently revolves around how long and how widespread the abrupt halt in economic activity will be and how much damage will be caused by the stoppage.”

Markus Allenspach,
Head of Fixed Income
Research

## FLIGHT TO SAFETY

"The coronavirus has turned the 'hunt for yield' into a 'flight to safety' with government bond yields plunging to unseen lows. The more credible the policy response to the crisis is, the faster we will return to the era of financial repression which is supportive for the riskier segments of the bond market."

## ATTRACTIVE ENTRY-POINTS

"Historically, all major virus outbreaks that resulted in tangible equity market corrections have been attractive entry-points for long-term investors. As of today, we think that the economic shortfall related to the coronavirus could be a buying opportunity for investors with an investment horizon beyond six months."

Patrik Lang,
Head of Equity Research

Vanessa Peter,
Head of Investment Advisory
Premium Zurich

## NO CHANGE IN MARKET LEADERSHIP

“Talking about sectors, I see no change in sight in terms of market leadership. Cyclical stocks remain our focus – especially industrials and information technology (IT). Undoubtedly, the sharp equity market correction in response to the coronavirus has negatively impacted cyclical equities. However, information technology stocks have been the key driver of the equity bull market, and sector leadership does not usually change quickly. It’s important to note that we expect the economy to rebound in the second half of 2020.”

## CHINESE EQUITIES ARE A CORE HOLDING

“We stick to our medium-term favourable backdrop for Chinese equities. Chinese policymakers continue to support the economy and private consumption with strong easing measures. Since the coronavirus outbreak, numerous easing measures have been announced, ranging from liquidity injections to credit support and tax relief. After investing a lot into physical infrastructure over the last years, the Chinese Politburo has now announced the build-out of new economy infrastructure such as data centres, artificial intelligence or the ‘internet of things’. We think that Chinese equities should be a core holding in an investor’s portfolio.“

Mark Matthews,
Head of Research Asia

Philipp Lienhardt,
Head of Single Equities
Research

## HEALTHCARE – A FIELD OF INNOVATION

“The Healthcare sector is well positioned to profit in the current environment, as it has less sensitivity to the economic cycle. The tragic coronavirus epidemic is also a reminder of the merits of holding a strategic exposure to biotech companies, as this disruptive technology is one of the fastest innovation fields globally. During previous US presidential election campaigns, healthcare stock price weakness often represented a buying opportunity.“

Marc Blunier,
Head of Investment
Publishing & Solutions

## EXOGENOUS SHOCK

“The rapid spread of the coronavirus and the corresponding quarantine measures turned out to be a huge exogenous shock and represent a significant risk for earnings growth over the coming months. In our base scenario, we do not see broad-based bankruptcies but sector-specific stress. The situation is exacerbated by other factors of insecurity, such as the oil politics dispute between Russia and Saudi Arabia and the outcome of the US presidential elections.”

## RECESSION AHEAD

“The window of opportunity for the timely and successful containment of a recession has narrowed sharply, as the recent large liquidity injection of central banks will not suffice to compensate for the short-term – but eventually widespread – demand loss. As the massively necessary fiscal stimuli take time to materialise, our recession scenario will become reality.”

Janwillem Acket,
Chief Economist

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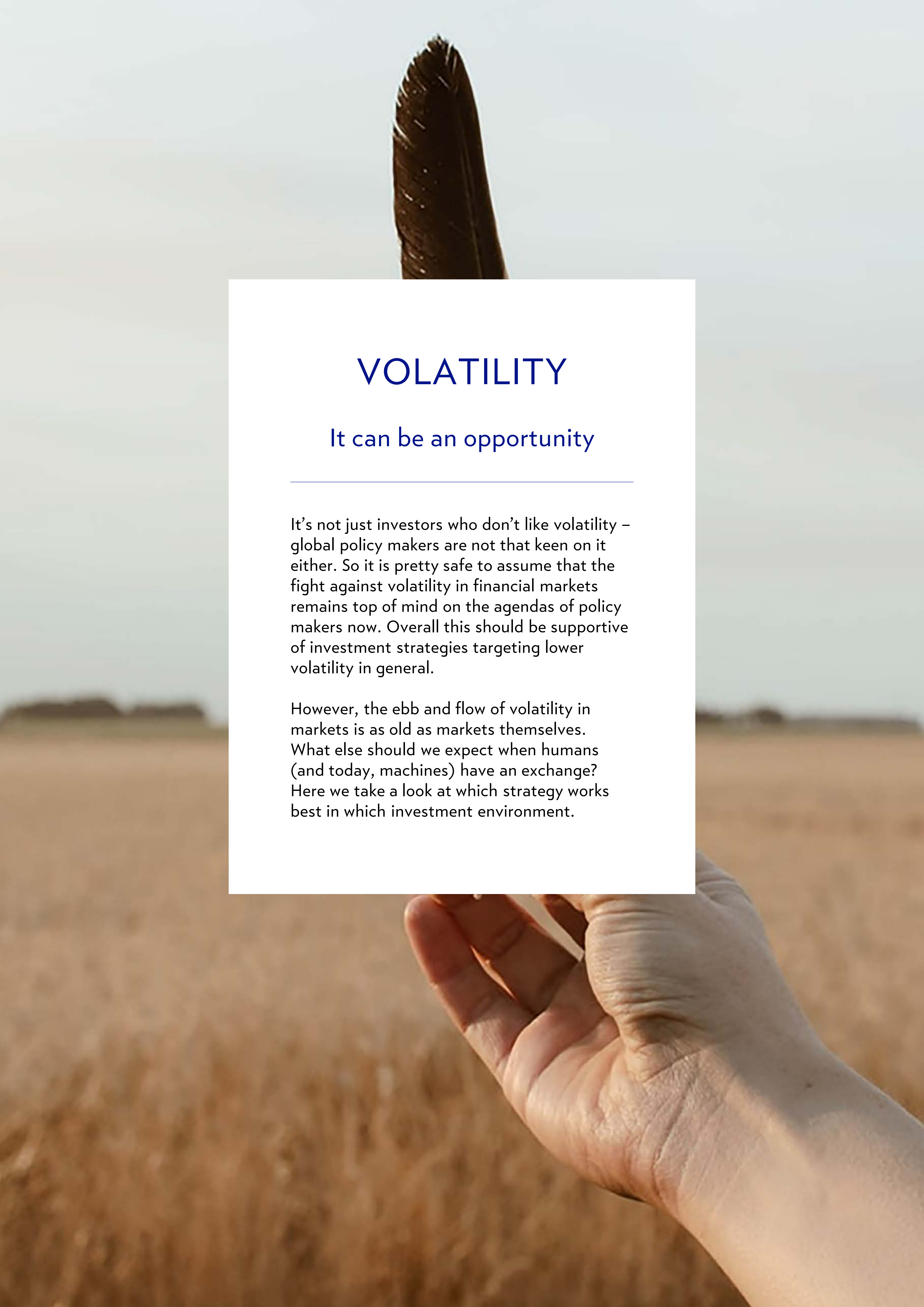

# VOLATILITY

## It can be an opportunity

It's not just investors who don't like volatility – global policy makers are not that keen on it either. So it is pretty safe to assume that the fight against volatility in financial markets remains top of mind on the agendas of policy makers now. Overall this should be supportive of investment strategies targeting lower volatility in general.

However, the ebb and flow of volatility in markets is as old as markets themselves. What else should we expect when humans (and today, machines) have an exchange? Here we take a look at which strategy works best in which investment environment.

## THE HUMAN TOUCH IN MARKETS

- "I have to own this painting at any price" is what can drive prices at an art auction to the sky, and beyond what the 'experts' would view as reasonable. In financial markets too the price at which an asset changes hands can be affected by many facets of investors' psychology – euphoria, despair, ignorance, greed and fear to name just a few human traits. This is the focus of behavioural finance.
- While the literature on behavioural finance is large and diverse, one notable investment behaviour is herding. It refers to the observation that investors tend to follow the actions of other investors and this in turn creates demand ('buy') or supply ('sell') volume.
- Who has not at least played with the thought that if everybody is buying, why not join the bandwagon? If enough investors think and act alike, their action moves prices – in this case higher. On the flipside, when prices tumble as investors sell, other investors are likely to follow. After all, the pain of a loss exceeds the joy of a gain. These examples go to show that herding can in fact accentuate trends both on the upside as well as the downside.

## HOW EMOTIONS DRIVE INVESTMENT DECISIONS


S&P 500 Index performance between 23 March 2018 and 31 July 2019
**Source:** Julius Baer Investment Publishing

# VOLATILITY – IT CAN BE AN OPPORTUNITY

Stock markets hit the headlines when they nosedive and fear prevails. And so volatility is tarred with a negative connotation. But volatility does not need to be a foe – it can also be a friend.

"Be fearful when others are greedy and greedy when others are fearful."

Warren Buffett

## VOLATILITY EXPLAINED

Imagine getting a price indication for your property each day. How would you react to seeing the price drop day after day? It is unlikely that you would sell your property as this would involve high logistical and emotional costs. Contrast this to financial assets which can be bought and sold at a whimper. The price movements which result from this trading activity can be labelled as volatility.

Volatility is one measure used to quantify the risk of an asset. It is the standard deviation of an asset's returns, which measures how far away the current price trades relative to its mean. If returns move far away from the mean, volatility and risk are considered to be high.

### **ASSUMPTION:** POLICYMAKERS CANNOT COUNTER VOLATILITY SPIKES

**OUR VIEW:** In times of market turmoil, all eyes are on policy makers. In a first move, they tend to cut interest rates decisively. In addition, policy makers may make use of new policy tools, including liquidity injections, balance sheet extensions and the opening up of fiscal channels (spending, tax credits, etc.). Thus, while policy makers cannot prevent volatility spikes or even at times a recession, their tools allow them to mitigate the negative effects and have shown to be very effective in moving markets into calmer waters over time.

### **ASSUMPTION:** VOLATILE MARKETS ARE A BAD TIME TO INVEST

**OUR VIEW:** The VIX index measures the 30-day expected S&P 500 index volatility and it is also referred to as the 'fear gauge' – a thermometer of investors' fear levels. It might surprise you to know that when the fear level is very high (VIX index above 40 vs. average 19), the index has an average 12-month forward return of 14% – far outpacing its long-term return of 6% to 8%. Importantly, in 80% of all observations the index would have posted a positive return. Thus, this assumption is highly challengeable.

**ASSUMPTION:** IN VOLATILE MARKETS THE BEST STRATEGY IS TO BE IN CASH

**OUR VIEW:** There is a saying, that to make money in the market, you have to be invested in the market. Missing out on the best five days in the S&P 500 index since January 1992 would have resulted in an initial investment of USD 100 rising to 'just' USD 380 compared with USD 600 over the entire period. What a difference five days can make. Our records show that the best days in equity markets were almost exclusively 'recovery days' after a correction when market sentiment was depressed and volatility at peaks.

# DEALING WITH VOLATILITY – TODAY'S STRATEGIES

With volatility being an indictor of risk in financial markets, it should be no surprise that the level of and changes in volatility – or risk for that matter – can impact the performance of various investment strategies in a meaningful way.

Below we introduce investment strategies that we view as being attractive and put them in the context of volatility.

## Income-oriented strategies

In the ongoing low interest-rate environment in which policy makers are dedicated to fighting volatility spikes by introducing targeted measures, we consider taking on measured credit risk and investing in high-dividend equity strategies to be attractive. The resulting periods of rising risk appetite accompanied by declining volatility precisely favour such strategies. Over time, investors should be compensated for taking on equity and credit risk within a diversified portfolio.

## A flexible fixed-income strategy – for every market

As abrupt changes in bond yields and credit spreads are the main sources of volatility in fixed income markets, investors may consider flexible fixed income strategies. By taking long and short positions in fixed income markets, these can perform well both in different volatility and risk scenarios.

## Behavioural equity strategies – the human touch in markets

In times of increased market volatility, the action of market participants tends to be driven by emotions and behavioural biases. This opens up opportunities for dedicated long-short equity strategies that aim to capture opportunities in single stocks.

Additionally, many investors tend to sell their winners too early (and losers too late), ignoring the fact that stocks that have performed well in the past are likely to perform well going forward. This is an opportunity for momentum strategies.

## Benefit from higher volatility

Investors can hedge equity risk with put options, similar to buying fire insurance on a house. Just as fire insurance is most expensive after a house has burnt down, hedging equity risk with equity put options is most expensive once markets are on their knees.

In this environment, investors can get an attractive premium (yield) by selling put options to take advantage of the higher risk. Alternatively, structured solutions (such as reverse convertible) can also be considered to generate an attractive yield with a risk buffer. These strategies perform best when volatility moves lower over time.

Please contact your Julius Baer representative if you would like to learn more about this or other topics mentioned in this section.

## INTERESTED?

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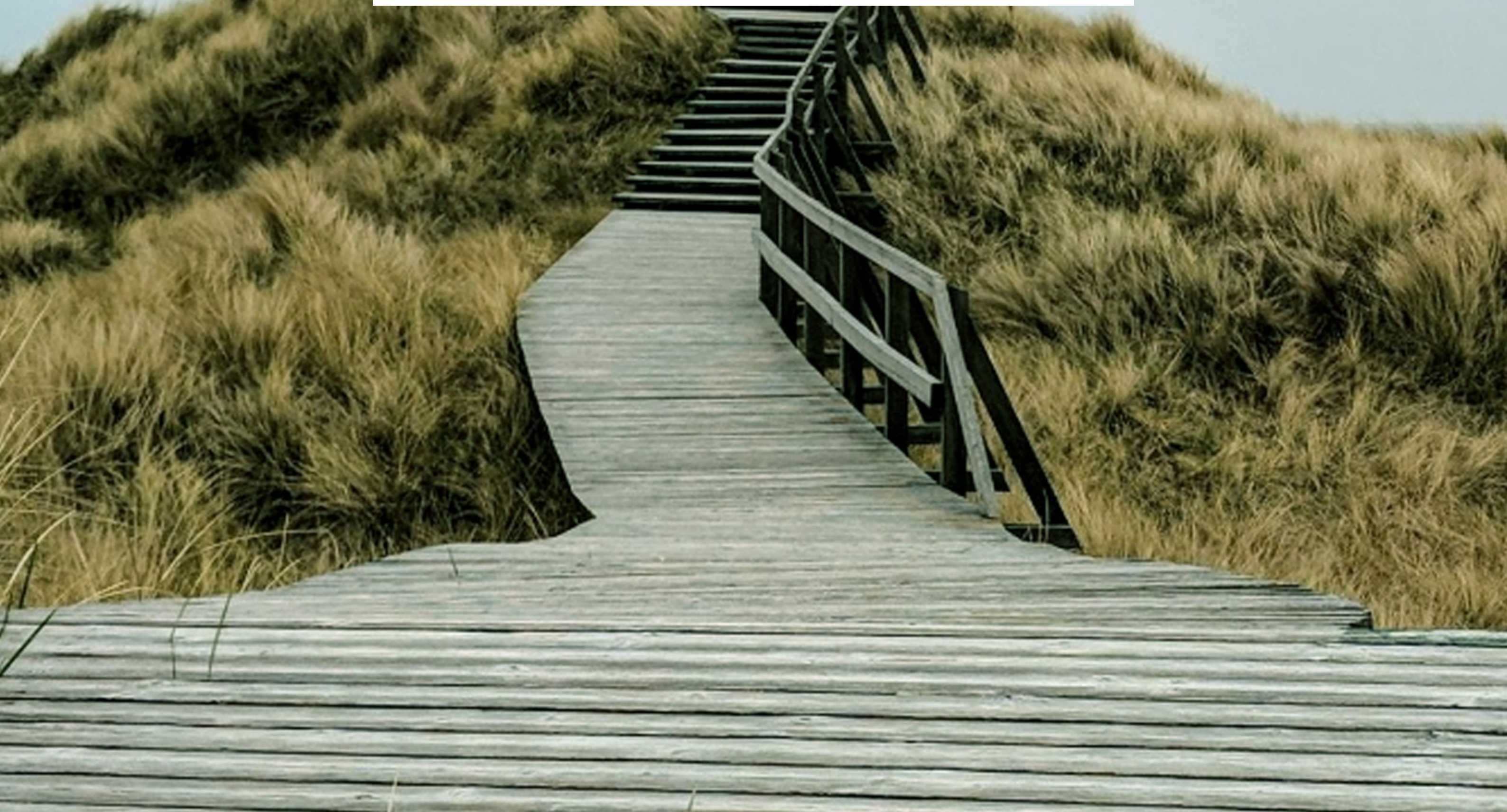
# DIGITAL HEALTH

## Technology could redefine healthcare

The coronavirus outbreak has exposed the woeful shortcomings of some healthcare systems in developed and developing countries alike. But the crisis should serve as a wake-up call.

Governments and healthcare institutions will be compelled to strengthen their healthcare systems and make them more efficient by adopting better digital health technologies.



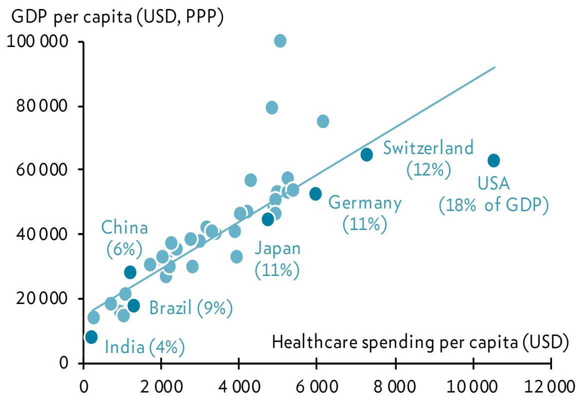
# DIGITAL HEALTH

## The current pandemic is hitting many countries unexpectedly and hospitals are reaching their limits, but digital healthcare solutions might help hospitals to be more efficient.

Beyond the massive economic implications, the current coronavirus pandemic has revealed the vulnerabilities of our healthcare systems and the inequalities in access to health services despite ever-growing medical costs.

Looking at the US, Americans spend a disproportionate amount of money on their health relative to their wealth. But despite higher spending on healthcare, roughly 28 million Americans do not have healthcare insurance at all and nearly 90% of those who do, are underinsured. This forces some to go to work despite being unwell.

### AMERICANS PAY MOST FOR HEALTHCARE SERVICES




16 March 2020
**Source:** World Bank, Julius Baer Next Generation Research

The coronavirus crisis will inevitably lead authorities and healthcare organisations to review the robustness of their national healthcare systems. To free up capacities at hospitals, they might look at digital healthcare solutions.

As described by the World Health Organization, digital health today includes the use of mobile and internet technologies, as well as areas such as telemedicine, apps, wearable devices, robotics, artificial intelligence and genomics.

Telemedicine, specifically online medical consultation, is a great example of technology being put to good use in healthcare. Most recently, it has become a popular source of healthcare advice among Chinese consumers during the coronavirus crisis.

In summary, digital health is not only capable of reducing healthcare costs and making healthcare services more affordable, but also of making hospitals more efficient. The ongoing pandemic therefore serves as a wake-up call for governments and institutions to ramp up their investments in digital healthcare solutions.

## INTERESTED?

Please contact your Julius Baer representative for further information on products that best suit your needs.

# SUSTAINABLE INVESTING

## ESG leaders make a difference

Sustainability has entered the mainstream of investing, not least thanks to people having a more risk-focused and ethically-minded philosophy.

Incorporating environmental, social and governance (ESG) factors in the investment decision process, alongside traditional financial analysis, provides a powerful insight into businesses, ultimately identifying those that are likely to outperform their peers in the long run.

# SUSTAINABLE INVESTING

## A challenging cyclical backdrop such as we have had in the first quarter of 2020 is a reminder of how important secular investment themes are.

How companies score in terms of environmental, social and governance (ESG) criteria has become increasingly relevant for investors. Companies today are expected to pay attention to the interests of society as a whole.

Sustainable earnings growth in the long-term goes hand-in-hand with business practices that incorporate stakeholder interests. Investors believe that industry trends, regulatory changes and consumer demands are driven by a general desire to reduce the environmental footprint, achieve a more equitable society and create corporate transparency and accountability.

Living these values requires excellent management and sound business practices that encompass aspects such as strategic guidance and accountability. ESG leaders usually come with sustainable cash flows, good financial health and the ability to return capital to shareholders.

### INTERESTED?

Please contact your Julius Baer representative for further information on products that best suit your needs.

Studies of ESG investing and its performance also provide evidence supporting the concept that ESG leaders are operationally and financially more successful. Having a stakeholder perspective benefits shareholder returns, a relationship studied in an extensive and growing body of literature on this important trend.

### WHAT DO THE ESG FACTORS STAND FOR?

The **environmental** dimension includes assessing a company's interdependencies with climate change, pollution, biodiversity or water and the related risk-mitigation strategies.

In terms of the **social** dimension, product safety, working conditions, employee diversity and community engagement are in focus.

For **governance**, executive compensation, accounting practices, board structures and business ethics are topics under watch.

**Source:** Julius Baer Investment Publishing

# FURTHER INFORMATION

# FURTHER INFORMATION

Please find below further information on benchmarks and indices used in the review section of this Investment Guide.

## MARKET REVIEW

### EQUITY REGIONS

| REGION | INDEX | REGION | INDEX |
|---|---|---|---|
| **Emerging markets** | MSCI Emerging Markets Net Total Return USD Index | **USA** | MSCI USA Net Total Return USD Index |
| **Switzerland** | MSCI Switzerland Net Return CHF Index | **Japan** | MSCI Japan Net Return JPY Index |
| **Eurozone** | MSCI Europe Net Total Return EUR Index | **UK** | MSCI United Kingdom Net Return GBP Index |

### EQUITY STYLES

| STYLE | INDEX | STYLE | INDEX |
|---|---|---|---|
| **Quality** | MSCI World Quality Net Total Return USD Index | **Cyclicals** | MSCI World Cyclical sectors Total Return USD |
| **Value** | MSCI World Value Net Total Return USD Index | **Defensives** | MSCI World Defensive Sectors Total Return USD |
| **Growth** | MSCI World Growth Net Total Return USD Index | **Small caps** | MSCI World Small Cap Net Total Return USD Index |
| **High dividends** | MSCI World High Dividend Yield Net Total Return Index | **Large caps** | MSCI World Large Cap Net Total Return USD Index |

### EQUITY SECTORS

| SECTOR | INDEX | SECTOR | INDEX |
|---|---|---|---|
| **IT** | MSCI World Information Technology Net Total Return USD Index | **Financials** | MSCI World Financials Net Total Return USD Index |
| **Materials** | MSCI World Materials Net Total Return USD Index | **Consumer cyclical** | MSCI World Consumer Discretionary Net Total Return USD Index |
| **Oil & gas** | MSCI World Energy Net Total Return USD Index | **Consumer defensive** | MSCI World Consumer Staples Net Total Return USD Index |
| **Industrials** | MSCI World Industrials Net Total Return USD Index | **Real Estate** | MSCI World Real Estate Net Total Return USD Index |
| **Communications** | MSCI World Communication Services Net Total Return USD Index | **Utilities** | MSCI World Utilities Net Total Return USD Index |
| **Healthcare** | MSCI World Health Care Net Total Return USD Index | | |

## FIXED INCOME

| SEGMENT | INDEX | SEGMENT | INDEX |
|---|---|---|---|
| **DM government bonds** | Bloomberg Barclays Global Agg Treasuries Total Return Index Value Unhedged USD | **DM High yield** | Bloomberg Barclays Global High Yield Total Return Index Value Unhedged USD |
| **DM TIPS** | Bloomberg Barclays Global Inflation-Linked Total Return Index Value Unhedged USD | **EM hard currency** | Bloomberg Barclays EM Hard Currency Aggregate TR Index Value Unhedged USD |
| **DM high quality IG** | Bloomberg Barclays Global Agg Aa Total Return Index Value Unhedged USD | **EM local currency** | Bloomberg Barclays EM Local Currency Government TR Index Unhedged USD |
| **DM low quality IG** | Bloomberg Barclays Global Agg Baa Total Return Index Value Unhedged USD | | |

DM: developed markets, EM: emerging markets, IG: investment grade

## COMMODITIES

| COMMODITY | FUTURE | COMMODITY | FUTURE |
|---|---|---|---|
| **Brent Crude Oil** | Generic 1st Crude Oil, Brent | **Platinum** | Generic 1st Platinum |
| **Natural Gas** | Generic 1st Natural Gas | **Aluminium** | Generic 1st Primary Aluminium |
| **Gold** | Generic 1st Gold | **Copper** | Generic 1st Copper |
| **Silver** | Generic 1st Silver | **Iron Ore** | Generic 1st Iron Ore |

# SCORING OUR CALLS

| TOPIC | BENCHMARK INDEX USED | TOPIC | BENCHMARK INDEX USED |
|---|---|---|---|
| **Global value stocks** | MSCI World Value Net Total Return USD Index | **US crossover bonds** | Barclays 3 month USD LIBOR Cash Index |
| **European value stocks** | STOXX Europe Large 200 Net Return EUR | **Asian high-yield bonds** | Bloomberg Barclays EM Asia USD Credit High Yield TR Index Value Unhedged USD |
| **Emerging markets - China** | MSCI World Health Care Equipment & Services Net Total Return Index | **Flexible fixed income strategies** | Barclays Benchmark Overnight USD Cash Index |
| **Healthcare stocks** | MSCI World Health Care Equipment & Services Net Total Return Index | **Subordinated bank debt** | ICE BofA Euro Financial Subordinated & Lower Tier-2 Index |
| **Cross-asset solutions** | Barclays 3 month USD LIBOR Cash Index | **High-dividend equities** | MSCI USA High Dividend Yield Net Total Return USD Index |
| **Innovators & dirsuptors** | MSCI ACWI Growth Net Total Return USD Index | | |

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