



EDMOND
DE ROTHSCHILD

ASSET ALLOCATION STRATEGY

MARKET ANALYSIS AND PRINCIPAL INVESTMENT THEMES

NOVEMBER 2020

THE CHANCES
OF A BIG
MARKET SHIFT
ARE
INCREASING



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KEY POINTS

We have raised
exposure to European
equities and also
US domestic and
cyclical equities

We have reduced
exposure to US
Treasuries

► There is still a lot of uncertainty over the new state of play in US politics -as well as the chances of a vaccine in the coming weeks- but we could be about to clear two economic and financial hurdles.

Bear in mind, however, that neither Donald Trump nor most of the Republican party have conceded defeat to Joe Biden. We cannot rule out more writs contesting the result even if they look like they have only a slim chance of succeeding. More importantly, the Senate majority will only be declared in January after two run-offs in Georgia.

We have always felt that in today's uncertain environment it would have been better for the administration to have a majority in Congress giving it the fiscal leeway to deal with any fresh economic shock. However, markets seem perfectly happy with the prospects of Republicans retaining control of the Senate. Any stimulus plan may be less ambitious but Donald Trump's tax cuts would be safe. Mitch McConnell, Senate majority leader, has now said the Senate will prioritise work on a stimulus plan, suggesting that the recent deadlock was due to the approaching elections. The current Senate majority's determination will have a much bigger impact on segments like GAFA stocks, financials and energy than on the S&P500 as a whole. It will also mean only a moderate impact on long Treasury bond yields as a Democrat clean sweep would have meant a bigger stimulus package, a steep rise in the minimum wage and therefore more pressure on bond markets. We are still contending with record levels of unknowns, but most of the uncertainty is now over.

Pfizer's announcement of a 90% success rate for its vaccine in phase III trials is excellent news. The vaccine should receive FDA approval by end November but there are still key questions to be answered: adverse effects could appear; storage is complex as the vaccine has to be kept at ultra-low temperatures and the price has to be decided. It is also not clear how easily populations will accept a new vaccine nor for how long immunity lasts. So it would be premature to reach conclusions on the vaccine's ability to change the pandemic's trajectory. That said, Pfizer's move could see other pharma companies follow suit with their own vaccines, poten-

tially causing a shift to a more optimistic scenario. We could be moving into a phase, from the second half of 2021, where the epidemic could be easier to control. Major developed countries are now sitting on a mountain of savings, some of it forced, so a sharp rebound in demand is now a real possibility. Amid persistently expansionist fiscal policies and accommodating monetary stances, investors are increasingly embracing the idea of a “perfect scenario”, especially as we could be seeing a fresh stimulus package in the US.

The sheer size of the recent rally may be surprising as US political risk and vaccine uncertainties have not gone away. However, we should remember that election uncertainty and a rapid resurgence in Covid cases in Europe and the US had left investors somewhat underweight equities. No doubt many had to quickly readjust portfolios, causing a spike in indices. What remains after the rush? A new stimulus package is taking shape in the US. It would be even bigger if Democrats were to win a majority in the Senate in January. And a vaccine allowing some control over the pandemic's trajectory would lift economies. These hopes are, of course, in sharp contrast to the situation today. Economies are set to buckle in the current quarter due to European lockdowns and the rapid spread of new Covid cases in the US. In other words, volatility could resurface over the short term as the perception pendulum swings between a declining economy and rising vaccine hopes.

Against this backdrop, we have raised exposure to European equities and also US domestic and cyclical plays which are still being snubbed by investors. These stocks will reap the full benefit of a vaccine and the stimulus package. Given the possibility of a game changer in 2021, we think it important to have portfolios which are well-balanced in both sector and factorial terms. This is why our allocation is now more weighted towards cyclicals. Nobody knows if Pfizer's vaccine will bring the epidemic under control but we are entering a period where other pharma companies will be offering

their own solutions and keeping hopes alive. International portfolios are generally underweight cyclical, value and domestic stocks so repositioning could trigger big price swings.

We have also once again reduced exposure to US Treasuries where risk now looks asymmetrical.

	OUR CONVICTIONS FOR NOVEMBER*	CHANGES COMPARED TO THE PREVIOUS MONTH
ASSET CLASSES		
Equities	+	↑
Fixed Income	=	→
Cash	-	↓
EQUITIES		
US	+	↑
Europe (ex-UK)	+	↑
UK	=	↑
Japan	+	→
China	+	→
Global Emerging	=	→
Convertibles	=	→
SOVEREIGN BONDS		
US	-	↓
Euro Zone	-	→
Emerging Markets	+	→
CORPORATE BONDS		
US Investment Grade	=	→
Euro Investment Grade	=	→
US High Yield	=	→
Euro High Yield	+	→

*Range of investment committee ratings on the asset class/geographical zone (from -/- to +/+). Source: Edmond de Rothschild Asset Management (France). Ratings at 09/11/2020.

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