MARKET BACKDROP
A review of what's happened in markets recently

MARKET OUTLOOK
Looking ahead to the coming months

SPOTLIGHT ON
Global reflation

The view
Winter 2020

architas

CONTENTS

Welcome

to The View – Winter 2020

Nearly all major asset classes rose over the quarter. Equities led the way, boosted by expectations of improved economic growth as a number of Covid-19 vaccines showed positive results and were submitted for approval.

The Winter edition of The View provides a step-by-step guide to how the political and economic environment has driven financial markets, and what this means for your investments.

With the global economy struggling during the pandemic, governments and central banks have been committed to a steady process of ‘reflation’— stimulus aimed at returning a weakened economy back toward normal, healthy levels. We delve into reflation strategies and highlight key takeaway points.

The titans of the US tech sector, household names such as Facebook, Amazon and Google, have been described as ‘too big to care.’ But the rush by regulators on both sides of the Atlantic to limit their dominant positions should now be ringing alarm bells. The threatened penalties, both fines and disposals, could cut these giants down to size. We take a look at the issues and the consequences.

Using multi-asset funds to get started is a solution growing in popularity if you are considering a longer-term investment of five years or more. Here we outline the top five benefits to this style of investing.

Jaime Arguello
Chief Investment Officer

Market BACKDROP

Nearly all major asset classes rose between October and December. Equities led the way, boosted by expectations of improved economic growth as a number of Covid-19 vaccines showed positive results and were submitted for approval.

This is despite the second wave of Covid-19 becoming established and a new strain unsettling investors. Promising results from a trio of vaccines against Covid-19 prompted a surge of market euphoria. Equity markets enjoyed a record breaking run. Vaccine optimism and hopes of an economic recovery next year have ignited sweeping gains in markets.

At the quarter end a further boost has come from a new US president's plans to reflate his economy. In December the US Senate voted to approve a stimulus package worth nearly $900billion, paving the way for the second-largest economic relief bill in American history.

ECONOMIC FACTORS

The final quarter of 2020 will be remembered for many reasons, but perhaps none more consequential than the realisation of at least three viable Covid-19 vaccines. Markets were cheered by the prospect of an end to the global pandemic and its weighty economic impact.

Focus on a green recovery. Governments and central banks have been flexing their green muscle to save the global economy from the coronavirus fallout and are preparing to deploy their firepower in another unprecedented battle - against climate change. With even China agreeing to improve green finance standards to support a carbon neutrality goal.

RISKS

A shift in world's economic power centre? A major pan-Asia trade deal agreement highlights the loss of influence of the US in the region. Known as the RCEP (Regional Comprehensive Economic Partnership) it groups 15 nations, including traditional trading rivals China, Japan and South Korea.

Debt binge risks years of pain. Many firms are in danger of being saddled with loans they will never be able to repay. Bank loans were made affordable by state-guarantees and central-bank stimulus to enable companies to survive lockdown cash flow problems.

FINANCIAL MARKETS

Vaccine roll-out pushed stocks to new highs despite some US election turmoil. Asia Pacific and emerging markets led the way as economic activity picked back up. US and European markets rose, but were volatile as fresh spikes in new Covid-19 cases sounded alarm bells.

Fixed income provided robust returns. Government bonds, a perceived safe haven, sold-off on the vaccine news but regained ground to finish the quarter higher as Covid-19 cases continued to rise. High yield and emerging market debt also benefited from investors' renewed appetite for risk.

CONCLUSION

2020 has been like no other. With the first wave of the pandemic triggering the biggest economic contraction in modern history. For the rest of the year, Covid-19 dominated headlines and markets. Globally policymakers took charge of an out of control situation and now most economies are looking forward to recovering to a great extent.

Investors overlooked rising deficits, debt and bloated central bank balance sheets believing it a necessary risk to take, and markets hit new highs and lifted spirits. As ever, we continue to believe that being diversified across a range of different asset classes is the best approach to take.

Market OUTLOOK

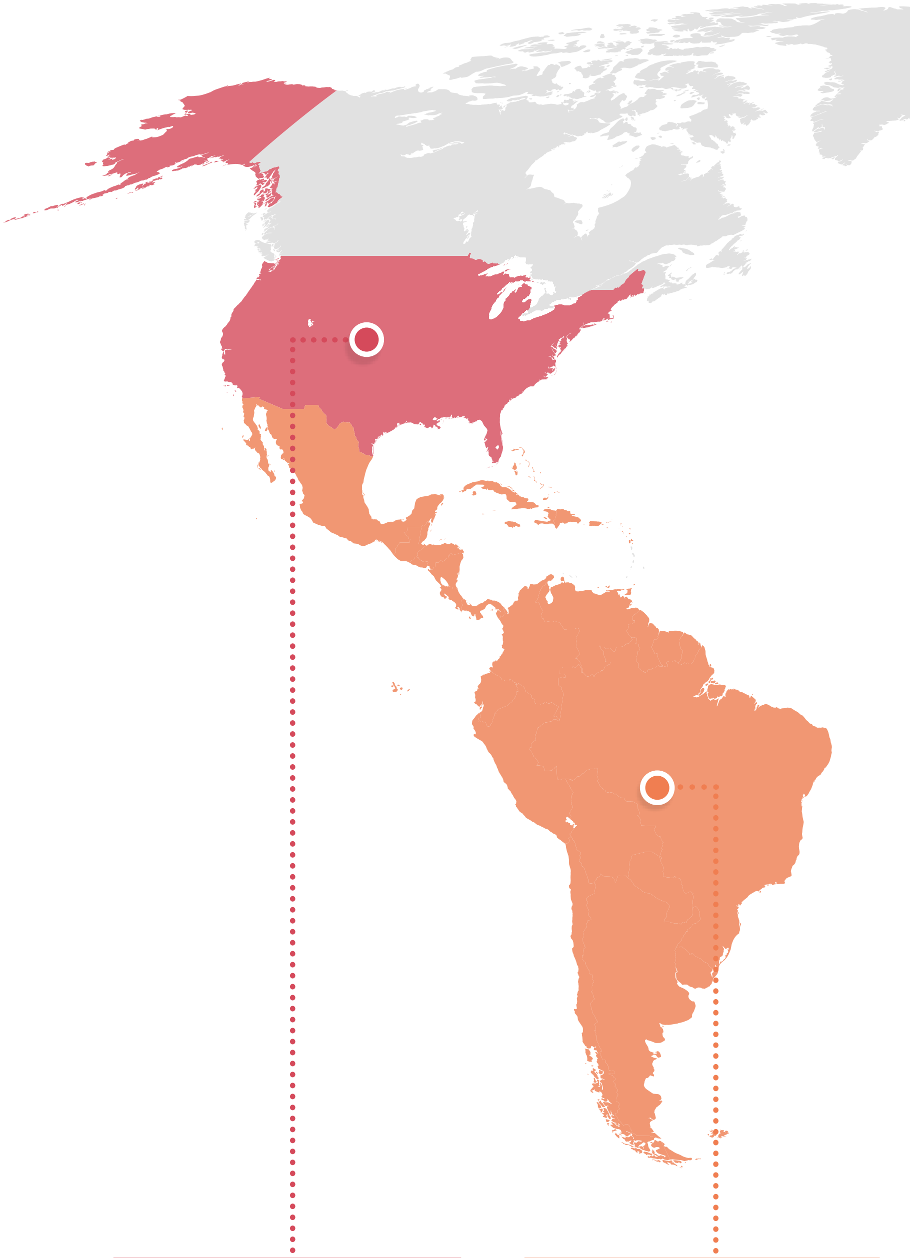
The start of the year has been promising despite many regional lockdowns. We have a global vaccine roll out, a strengthened Chinese economic recovery and the election of US President Biden. This should make 2021 a year of global economic recovery. The major risk now is the amount of investor optimism. Of course in addition, there's likely to be restart challenges, regional divergence and the much anticipated move away from big tech companies. All come with their own risks.

We believe that equity markets have priced in a lot of this good news, but more gains are possible as corporate profits rebound. In fixed income, despite high levels of debt, markets are stabilising. Aided by the unwavering support of central bank bond-buying-programmes across the globe, holding borrowing costs low and providing a backstop if investor demand falls.

With markets providing positive signals so far this year, we are wary of potential bumps in the road in the months to come. We, therefore, believe that taking a slightly more cautiously optimistic view is sensible while remaining diversified across a broad range of asset classes.

KEY

- Positive
- Negative
- Neutral



UNITED STATES

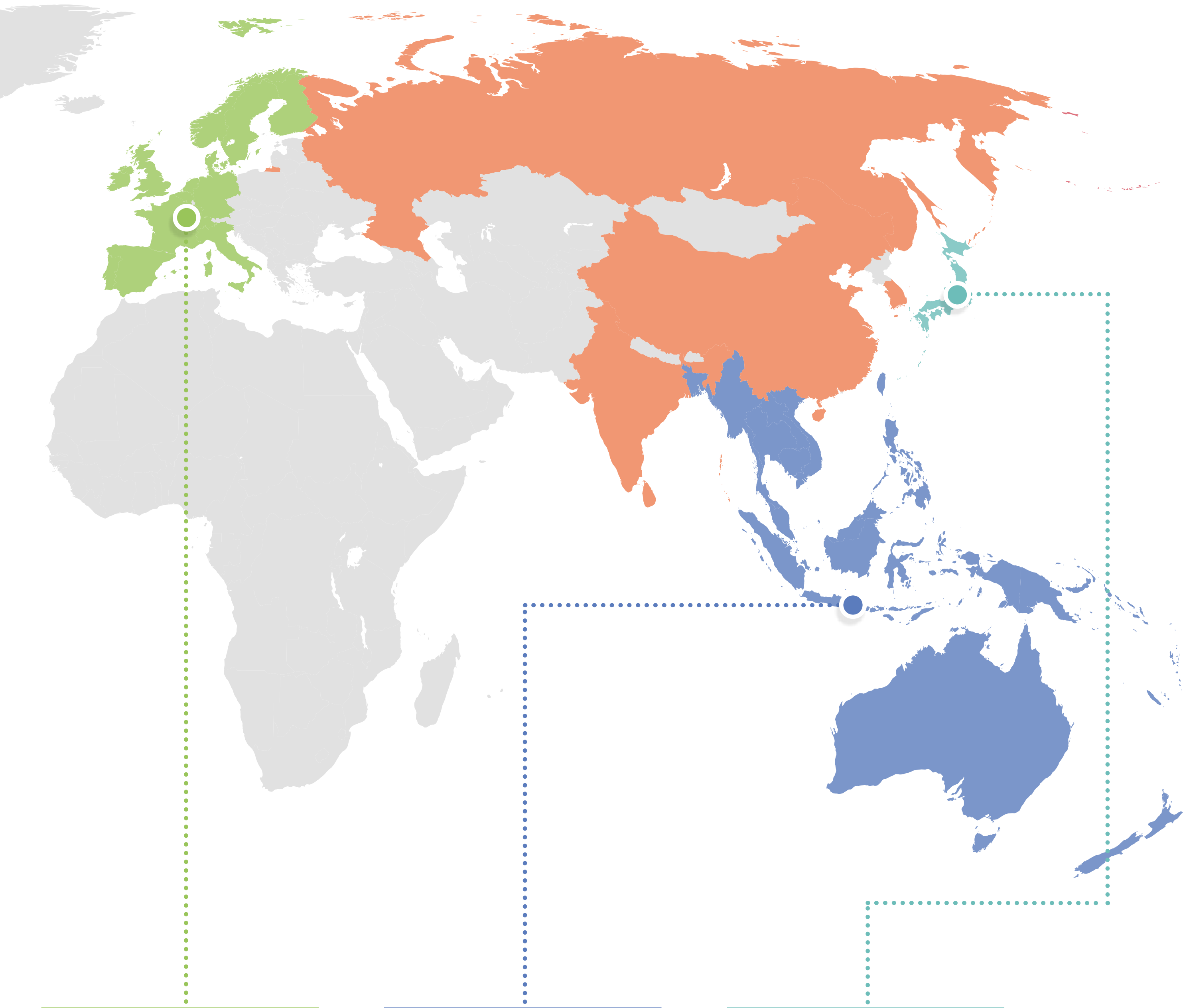
STOCKS (Neutral) BONDS (Positive)

- Buoyed by unprecedented fiscal stimulus and a new president market sentiment remains high. Although, US stocks are expensive and a shift away from growth stocks like big tech may weigh on returns.
- We like that US bonds are lower risk and can help balance out stock market turbulence, despite the high bond valuations.

EMERGING MARKETS

STOCKS (Neutral) BONDS (Positive)

- Emerging market stocks are best placed to benefit for the rest of the year. We view this asset class as a global barometer of risk appetite.
- We believe emerging market bonds are quite attractive, offering reasonable value relative to other areas of fixed income.



EUROPE

STOCKS ⊖ BONDS ⊖

- We are broadly optimistic; however there is little room for disappointment. Europe has a clear strategy of rolling out vaccines but stock prices are high and markets could go down if earnings disappoint.
- Overall we are neutral with a preference to corporate bonds over government bonds as these are better positioned to benefit more directly from monetary stimulus.

ASIA PACIFIC

STOCKS ⊖

- A strong Chinese economic recovery and the removal of the risks associated with Trump should benefit the region, as China's export activity is a big influence.
- After eight years of negotiations, Asia-Pacific countries formed world's largest trading bloc. The Regional Comprehensive Economic Partnership (RCEP) marks a major step forward for economic integration in the region.

JAPAN

STOCKS ⊖

- An encouraging development of the new prime minister, Yoshihide Suga, is his planned reforms to improve productivity levels. This will be an important watch point this year.
- Japan stands out for having one of the lowest Covid-19 infection rates. As such the rebound is likely to lag other developed economies.

SPOTLIGHT ON...

global reflation

With the global economy struggling during the pandemic, governments and central banks have been committed to a steady process of 'reflation'— stimulus aimed at returning a weakened economy back toward normal, healthy levels of growth and inflation.

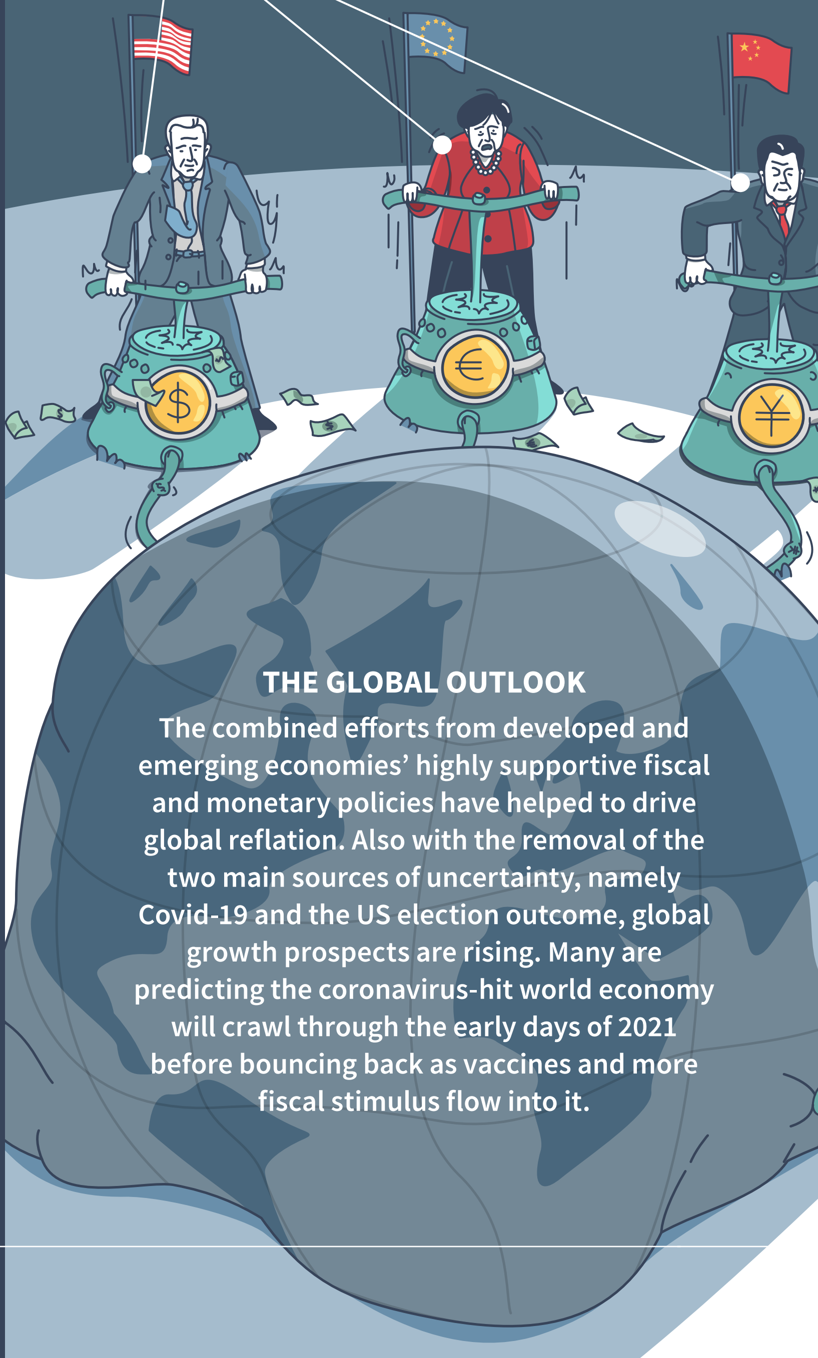
REFLATION VS. INFLATION

Don't confuse reflation with inflation. Importantly, reflation is not bad - it is a time of price increases when an economy is striving to achieve full employment and growth. Inflation, on the other hand, is often considered bad, characterised by rising prices during a period of full capacity. However, prices rise gradually during a period of reflation and fast during a period of inflation. As a result, reflation can be described as controlled inflation.

REFLATION STRATEGIES

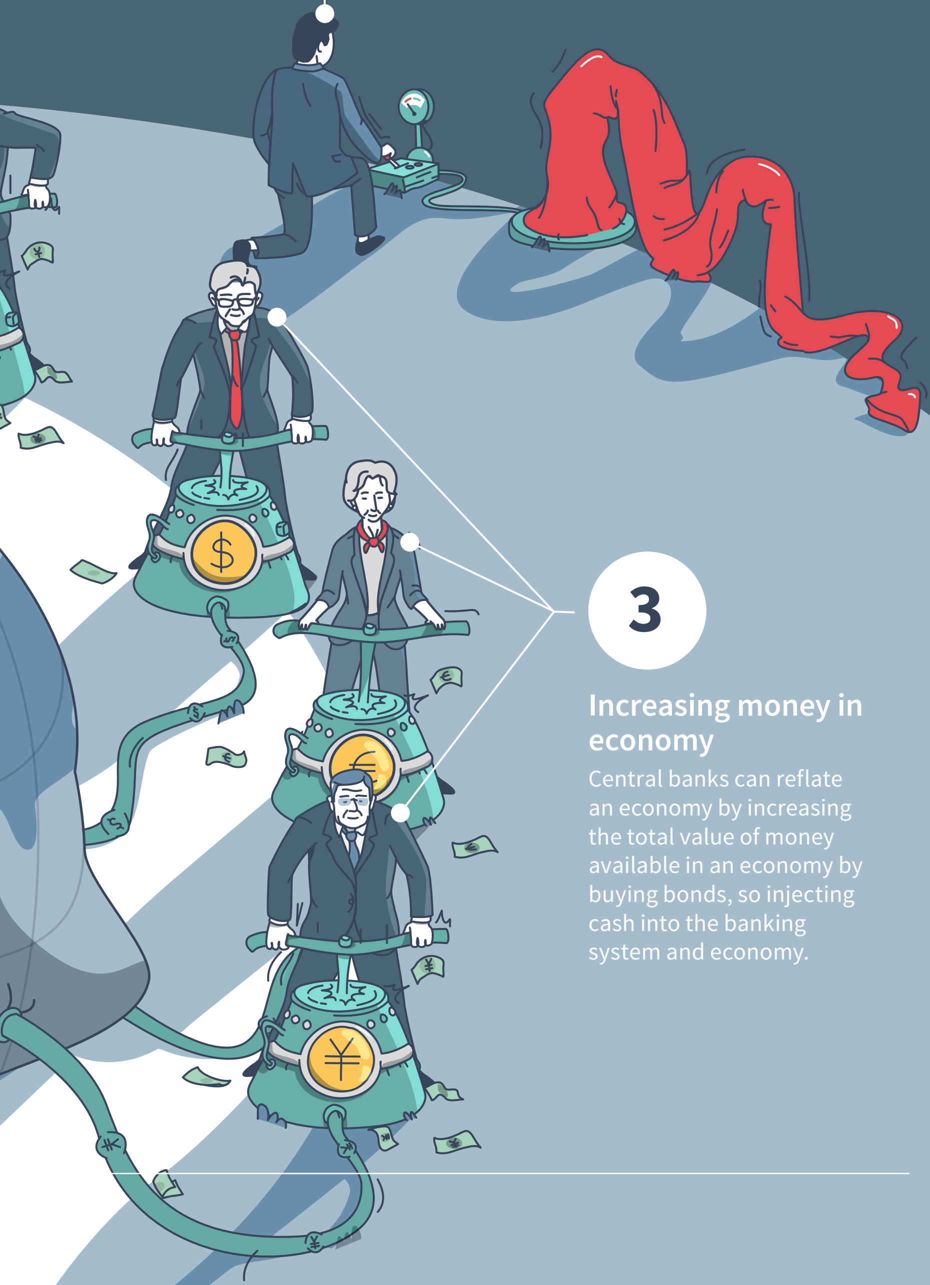
Reflation is the intentional reversal of deflation through a fiscal or monetary policy by central banks and governments. Faced with the prospect of deflation or a massive slowdown policymakers globally have taken the following steps:

1 **Huge government spending**
Unprecedented global fiscal support of over $10 trillion. Direct support to workers, tax cuts, public sector loans and guarantees.



THE GLOBAL OUTLOOK

The combined efforts from developed and emerging economies' highly supportive fiscal and monetary policies have helped to drive global reflation. Also with the removal of the two main sources of uncertainty, namely Covid-19 and the US election outcome, global growth prospects are rising. Many are predicting the coronavirus-hit world economy will crawl through the early days of 2021 before bouncing back as vaccines and more fiscal stimulus flow into it.



2 Cutting interest rates

Making it cheaper to borrow money and less rewarding to stow capital away in savings accounts. This encourages people and businesses to spend more freely.

3 Increasing money in economy

Central banks can reflate an economy by increasing the total value of money available in an economy by buying bonds, so injecting cash into the banking system and economy.

THE STATS

After a sharp decline, global GDP in 2020 is estimated to be around **-4.2%**, rising by **4.2%** in 2021 and a further **3.7%** in 2022*.

- **Improving outlook**. Late last year investors were rushing into emerging markets and commodities, two barometers of confidence in an improving economic outlook.
- **Removal of key risks**. A successful roll out of the vaccine could push a rotation out of relative safe havens, bonds, cash and growth stocks, and into riskier assets.
- **Debt is piling up**. Reflation has added extraordinary levels of debt and in 2021 there is likely to be a renewed focus of debt accumulated by companies and governments.
- **The journey may not be smooth**. Any delay in implementation towards mass vaccinations could hamper a smooth reopening of economies and with the potential to chip away at upbeat growth and corporate profit estimates.

*All GDP forecasts provided by the OECD's (Economic Cooperation and Development) December 2020 economic outlook.

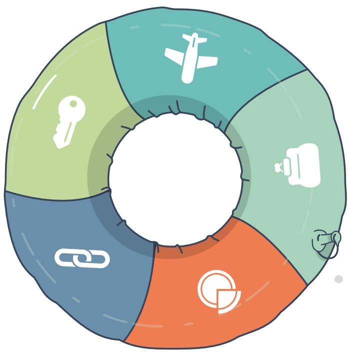
KEY TAKEAWAYS:

- Governments and central banks are on track to reflate the global economy
- Reflation is not bad and it doesn't have to lead to high inflation
- There have already been signs of a positive market response
- Nothing is certain so prepare for short-term market ups and downs

AN INTRODUCTION TO
USING MULTI-ASSET FUNDS

If you are considering a longer-term investment of five years or more, and are comfortable with the risks involved, then the next step might be deciding how to get started in investing. Learning the pros and cons of the world's various markets and assets can be time-consuming and difficult. That's why many people leave these decisions to experts. One solution could be to opt to invest in a multi-asset fund.

At Architas, we are experts in multi-asset, and we believe there are many benefits to investing in a multi-asset fund:



A diverse range of assets

Multi-asset funds can provide investors with exposure to a broad range of asset types. You can further increase this 'diversification' by blending geographies and sectors.

Potential for smoother returns

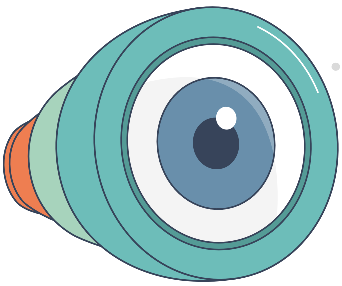
Asset classes don't tend to all fall in value at the same time. So multi-asset investors are, to some extent, more insulated from the highs and lows of individual asset markets.

Ongoing expert monitoring

Generally, multi-asset investing comprises complex asset allocation decisions supported by risk reduction strategies by a team of experts who collaborate to search for the best mix for your investments.

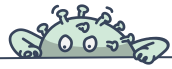
Simple to understand

And finally, multi-asset funds package a diversified, complex portfolio balancing risk and reward, but presented in a simple-to-understand way.

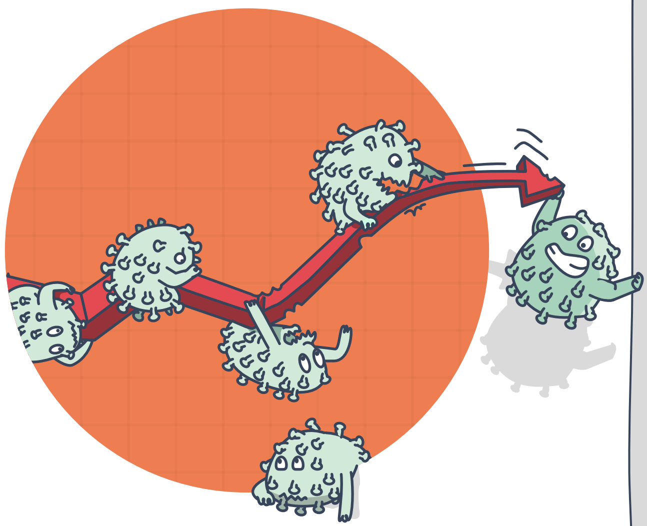


Targeting outcomes

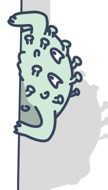
Selecting a multi-asset fund that matches your attitude to risk can be a good tool to help investors achieve their financial outcomes while ensuring they do not take on more risk than they are comfortable with.



MULTI-ASSET DURING THE COVID CRISIS



The coronavirus outbreak crossed borders through the first quarter of 2020, sneaking up on investors.

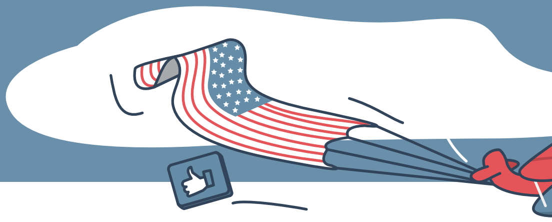


The initial market reaction resulted in an indiscriminate sell off across all asset classes. Even bonds or equities issued by high quality companies and developed world governments saw their prices marked down on some days during the sell-off, as the dash for cash dried up liquidity in markets.

However over the year multi-asset helped to provide diversification. Now in 2021, investors have started to rethink the role of bonds, tech and ESG after a chaotic year. As ever, this emphasises that protecting portfolios from large market spikes is possibly more important than ever.

Big Tech attack

WHAT'S THE BIG STORY?

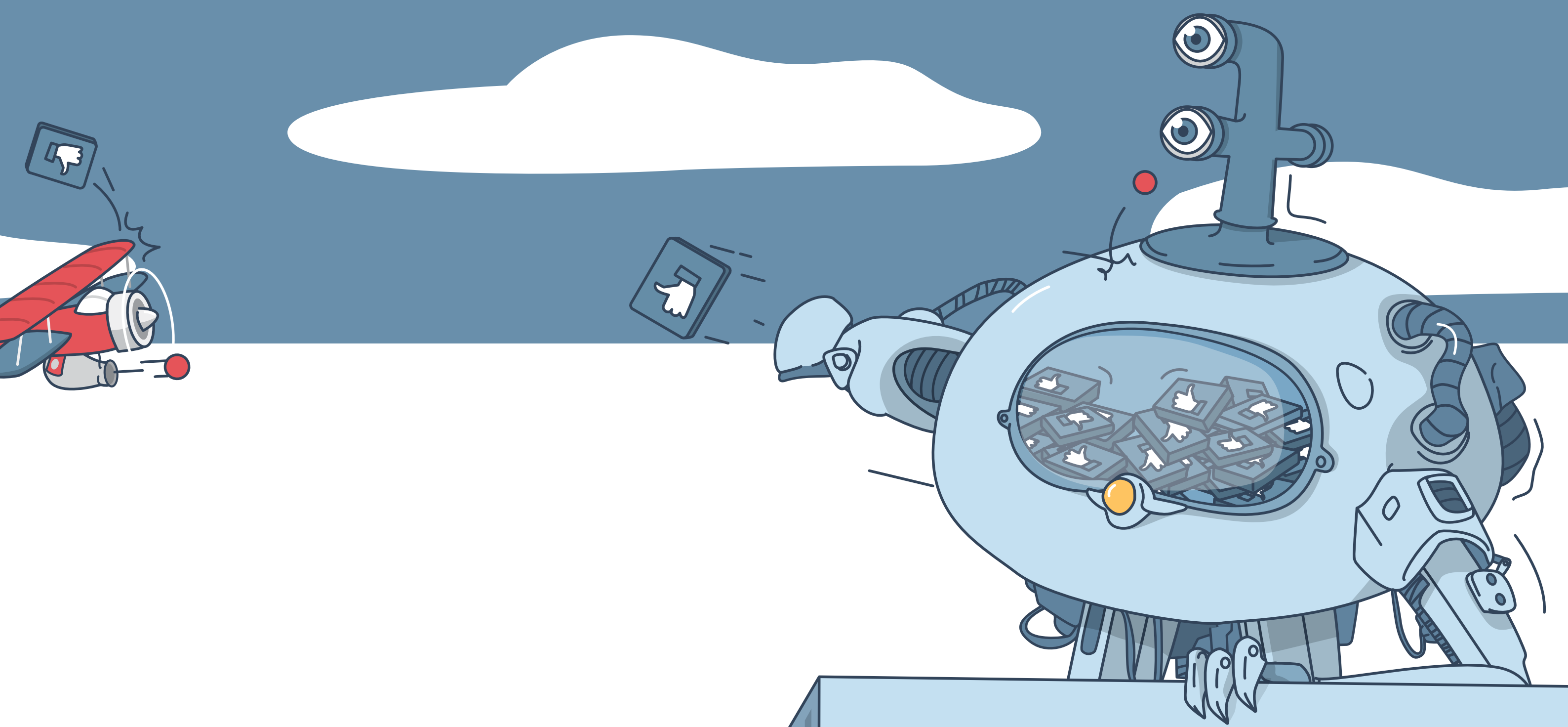


The titans of the US tech sector, household names such as Facebook, Amazon and Google, have been described as 'too big to care.' But the rush by regulators on both sides of the Atlantic to limit their dominant positions should now be ringing alarm bells. The threatened penalties, both fines and disposals, could cut these giants down to size. We take a look at the issues and the consequences.

As an example, the European Commission has taken aim at the 'very large' tech platforms, specifically those with more than 45 million customers. They are labelled 'digital gatekeepers', because their huge and expanding scale is keeping competitors out of the game. It's become a global issue. Last year Google, Facebook and Amazon together grabbed more than 70 per cent of all online advertising. In essence, they are not 'in the market' they have 'become the market'.

Why does that matter? In the old world, market dominance meant control of pricing and fat profits. In the digital age this has little meaning, as many services appear to be provided free of charge. But are they? Users are in fact paying for these services with their personal data. It's a very valuable commodity and one that the digital gatekeepers value highly. Control of consumers' data brings even greater market dominance.

And it's not only in the US and Europe that Big Tech is under scrutiny. In recent months the Chinese regulator has moved against its own giants, such as Alibaba and Tencent. The reasons are similar. Increasing concentration of online platforms, dominant market positions and an ever widening reach. Perhaps the reason why the $37 billion IPO of Ant Group, a technology vendor turned major player in online banking, was recently pulled.



So what happens to Big Tech next? At the very least investigations of business practices and acquisitions, possibly stretching back a number of years. If wrongdoing is found then financial sanctions are likely, including huge fines of up to 6% of annual turnover. In the extreme, forced divestments could break the companies up. It seems the digital gatekeepers now find their businesses and their profits under siege.

Big Tech presents a problem for investors as well as regulators. Apple, Microsoft, Netflix, Amazon, Alphabet and Facebook now represent a quarter of the S&P 500. The S&P 500 is supposed to represent a broad cross section of large US companies, giving index investors an attractive way to diversify their money. That's no longer the case. A ratio like this is unprecedented, even during the tech bubble, dominating end investments and risking overexposure to investors.

However, tech's reign over the US stock market may well be tested in 2021 as the global economy recovers. With a shift away from investments that benefitted from the pandemic and lockdowns - like US shares, technology and health care stocks and bonds - to investments that will benefit from recovery - like resources, industrials, tourism stocks and financials. And tech stocks can often be the most volatile, so the same dynamic that's led to such huge gains could result in large losses. 2021 may not be the year for Big Tech in more than one way. Highlighting the need for not keeping all of your eggs in one basket.

Facts & Figures

QUARTERLY DATA

Asian (but not Japanese) stocks	Emerging market stocks	UK stocks	European (but not UK) stocks	Japanese stocks	US stocks
20.1%	**19.8%**	**19.1%**	**15.3%**	**13.5%**	**12.1%**
MSCI Pacific excluding Japan Index	MSCI Emerging Market Index	FTSE All-Share Index	FTSE All World Developed Europe excluding UK Index	TOPIX Index	S&P 500 Composite Index

Global high yield bonds	UK corporate bonds	European corporate bonds	Emerging market bonds	US corporate bonds	Global government bonds
7.5%	**7.1%**	**6.4%**	**5.5%**	**3.0%**	**2.1%**
ICE Bank of America ML Global High Yield Bond Index	Bloomberg Barclays Sterling Aggregate Bond Index	Bloomberg Barclays European Corporate Bond Index	JP Morgan Global Emerging Market Bond Index	Bloomberg Barclays US Corporate Bond Index	FTSE G7 Index

To highlight the unpredictability of markets, the table below details the performance of global equity and fixed income indices over the past five years (in dollar terms).

This table demonstrates how volatile markets can be, and shows the benefits of diversifying your investment, or in other words, not putting all your eggs in one basket.

Index percentage growth (%)	1 Jan 20 - 31 Dec 20	1 Jan 19 - 31 Dec 19	1 Jan 18 - 31 Dec 18	1 Jan 17 - 31 Dec 17	1 Jan 16 - 31 Dec 16
US stocks	18.4	31.5	-4.4	21.8	12.0
European (but not UK) stocks	12.3	25.3	-14.4	28.3	0.3
UK stocks	-6.9	24.0	-14.8	23.8	-2.1
Japanese stocks	10.4	16.3	-15.6	23.9	1.2
Asian (but not Japanese) stocks	6.6	18.5	-10.2	26.0	8.0
Emerging market stocks	18.7	18.9	-14.2	37.8	11.6
Global government bonds	9.6	5.8	-0.4	6.3	1.8
Global high yield bonds	8.0	13.7	-3.3	10.2	14.8
US corporate bonds	9.9	14.5	-2.5	6.4	6.1
European corporate bonds	12.0	4.3	-6.0	16.6	1.7
Emerging market bonds	5.9	14.4	-4.6	9.3	10.2
UK corporate bonds	11.8	12.2	-6.0	12.4	-7.1

Past performance is not a guide to future performance. Rebased in US dollars where appropriate, i.e. all index returns are recalculated based on exchange rates to give returns for a dollar investor. Source: Morningstar Direct, January 2021.

Important INFORMATION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