LMM COMPASS

Dear reader

The capital market was not for the faint-hearted in 2020. Not only shares but also bonds were affected by the violent price movements. We discuss the extent to which they still fulfil their function as a stabiliser in the portfolio in our specialist article.

For 2021, we wish you good health and a lot of confidence on the way back to normality!

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THEMES

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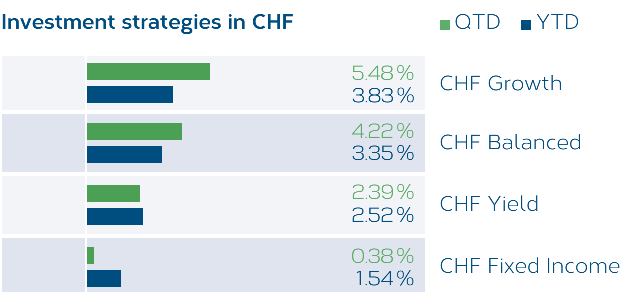
MARKETS AND STRATEGIES

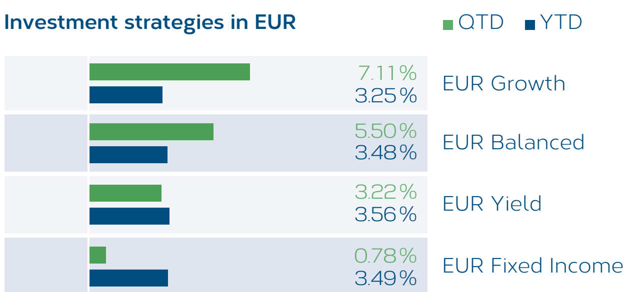
As was the case throughout the year, the fourth quarter of 2020 was a rollercoaster of emotions. After the economic outlook darkened in October due to the second Corona wave, optimism regained the upper hand in November thanks to success stories from vaccine manufacturers and the election results in the USA. As a result, both equities and bonds posted strong gains. Only gold saw a consolidation after its strong rise in the first half of the year. Despite high uncertainty and volatility, diversified and fully invested portfolios were able to close 2020 on a positive note.

		Value	% QTD	% YTD	Currency
Currencies	EUR/CHF	1.08	+0.39	-0.50	
	EUR/USD	1.22	+4.34	+9.00	
	USD/CHF	0.88	-3.79	-8.72	
	USD/JPY	103.24	-2.17	-5.00	
Bonds	Switzerland	141.93	+0.52	+0.90	CHF
	Europe	275.36	+1.26	+4.05	EUR
	USA	2392.02	+0.67	+7.51	USD
	Emerging Markets	468.52	+5.00	+7.11	USD
	Inflation linked	401.16	+4.88	+12.67	USD
	High Yield	1513.97	+7.66	+7.03	USD
	World	558.73	+3.28	+9.20	USD
Equities	Switzerland	3285.05	+4.14	+1.91	CHF
	Europe	235.89	+10.80	-3.32	EUR
	North America	10520.79	+13.01	+20.73	USD
	Pacific	7639.07	+16.72	+11.93	USD
	Emerging Markets	624.13	+19.70	+18.31	USD
	World	328.20	+14.68	+16.25	USD
Alternatives	Real Estate	4345.88	+13.49	-8.18	USD
	Commodities	78.05	+10.17	-3.50	USD
	Gold	1898.36	+0.66	+25.12	USD
	Private Equity	3564.16	+24.71	+10.61	USD
	Hedge Fonds	1380.48	+5.11	+6.81	USD

reference date 31.12.2020

In the fourth quarter, the investment strategies were also able to catch up strongly thanks to good bond and equity returns. The main drivers were once again equities, which meant that the riskier investment strategies were also able to close the year in the black.





Calculation LMM: Period 01.01.–31.12.2020

Note: the figures are before costs (exclusive of custody- and management fees)

BONDS AS A RISK BUFFER?

For a long time, bonds were considered a stabilising factor in a portfolio. In many cases, they were able to dampen the fluctuations or price declines of shares and protect them during market corrections. Last year, many investors realised that this assumption is only valid to a limited extent. Many portfolios also recorded considerable losses in bonds in March.

What is the reason for this and what should be considered in the future?

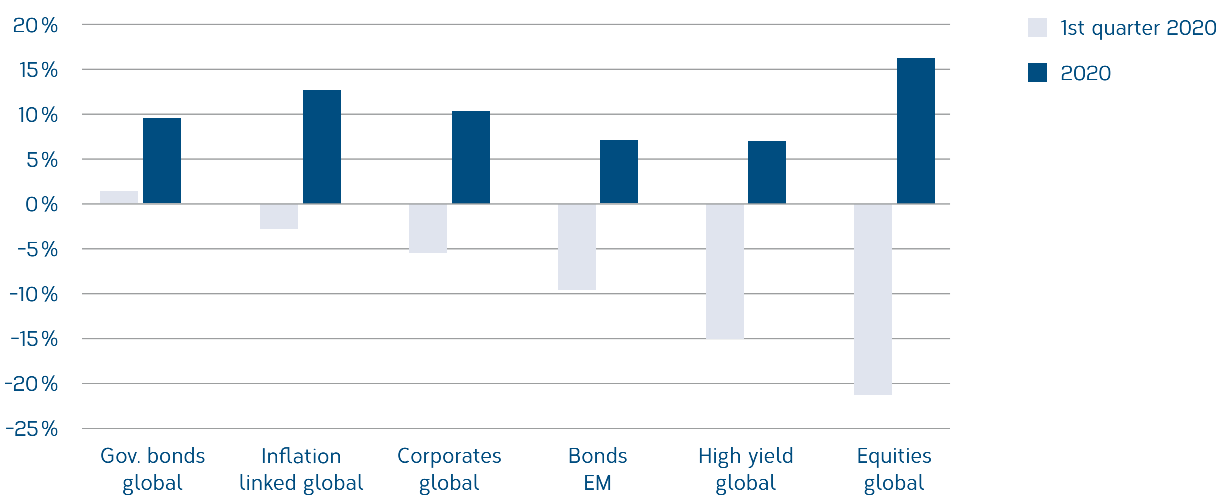
The continuing low-interest phase has led to more and more government bonds showing negative yields even with long maturities of up to ten years. Investors have therefore increasingly turned to corporate bonds. But here, too, investors were forced to make more and more concessions on the creditworthiness of the issuer in order to achieve attractive or positive yields. Financially sound issuers such as Nestlé with ratings in the A range are currently showing negative yields even with longer maturities. In search of yield, more and more managers have therefore moved into the lower rating segments.

March 2020 has shown that corporate bonds close to "non-investment grade" are increasingly "equity-like" risks. In market corrections, they do not have a stabilising effect, but can even increase volatility. The following chart shows the development of various bond segments in 2020. The chart illustrates that only quality bonds with long durations offered protection in March 2020. US bonds have also benefited from the decline in interest rates. Corporate bonds, especially those with lower credit ratings, have suffered significant losses in the meantime. It is therefore advisable to keep an eye on the risks when so-called "yield picking" takes place. One thing is always true: the higher the yields, the higher the default risk.

What alternatives do investors have in this environment?

Interest rate differentials have narrowed further. The advantage of this is that currency hedging has become cheaper. Investors thus have access to more bond segments, which increases the possibilities for diversification. However, the fundamental problem of low or negative interest rates remains.

Performance of bonds in 2020 (in USD)



SPECIALIST ARTICLE

How are the professionals in asset management acting?

It can be observed that banks and asset managers are increasingly recommending other asset classes instead of bonds. Gold, Hedge Funds, insurance-linked securities (ILS) and Private Debt are mentioned as attractive alternatives (complementary asset classes). Investors should be aware that each asset class has a different risk/return profile and should be assessed in the portfolio context. Transparency and costs are other factors that should always be kept in mind.

The bond market has become increasingly unattractive for investors. In many segments, one is not compensated for the risks taken with an adequate return. Caution is advised when shifting into alternative asset classes, especially with investment solutions that offer little transparency. Moreover, in addition to the risks, the costs should also be examined.

LMM INSIDE

In December 2020, we supported the foundation platform stiftung-nextgen (www.stiftung-nextgen.at) with our know-how in the conception and implementation of the annual survey "Stiftungsmonitor 2020". The results in the area of investment organisation and investment results were not only of interest for the 100+ participants in the Austrian foundation sector. Please find some individual results:

- 77% of the portfolios are invested conservatively or moderately.
- Only about half of the participants stated that they carry out regular cost controls.
- The controls are mainly carried out by the board of directors (67%)
- 81% of the portfolios are underperforming the benchmark in the current year (time of survey)

The reasons for the underperformance can be manifold, ranging from different guidelines to high costs or disadvantageous decisions by the asset manager. The results show the need for an objective performance assessment.

You can access further results of the survey at www.stiftung-nextgen.at.

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