SEASPRAY PRIVATE
Wealth Management Solutions

Monthly Investment Update
Feb 2021

Executive Summary

Feb. 2021

Since our 2021 investment outlook in January, equity markets, depending on the region, have traded flat to slightly higher.

While this was not a completely smooth journey for risk assets, when we take a look back at the last couple of months we are reminded that opportunities are constantly presenting themselves within markets if we remain objective. In late January the US' VIX volatility index (chart below) briefly spiked above $37 for the first time since just before the US Presidential Election back in November.

This move came as many market participants turned their attention to the Reddit-fueled volatility in specific stocks, driven by massive groups of united retail traders, coupled with the emergence of new virus strains and growing arguments between the European Commission and AstraZeneca over vaccine supply cuts. This short-lived move higher in the VIX represented a pullback in most global equities at the end of January, not just the United States, and allowed us at Seaspray to add to our core positioning, given our medium to long term constructive view on equities and indeed the global economy.

Source: TradingView

Much of the news flow since the beginning of the year has served as a reminder to us that governments and central banks are fully committed to supporting the global economy with massive fiscal stimulus and very easy financing conditions.

We saw equity markets pull back last week as a continued rise in yields on longer-term US Treasuries spooked investors, resulting in February's largest sell-off as the S&P500 lost 4% from peak to trough, having since pared much of these losses.

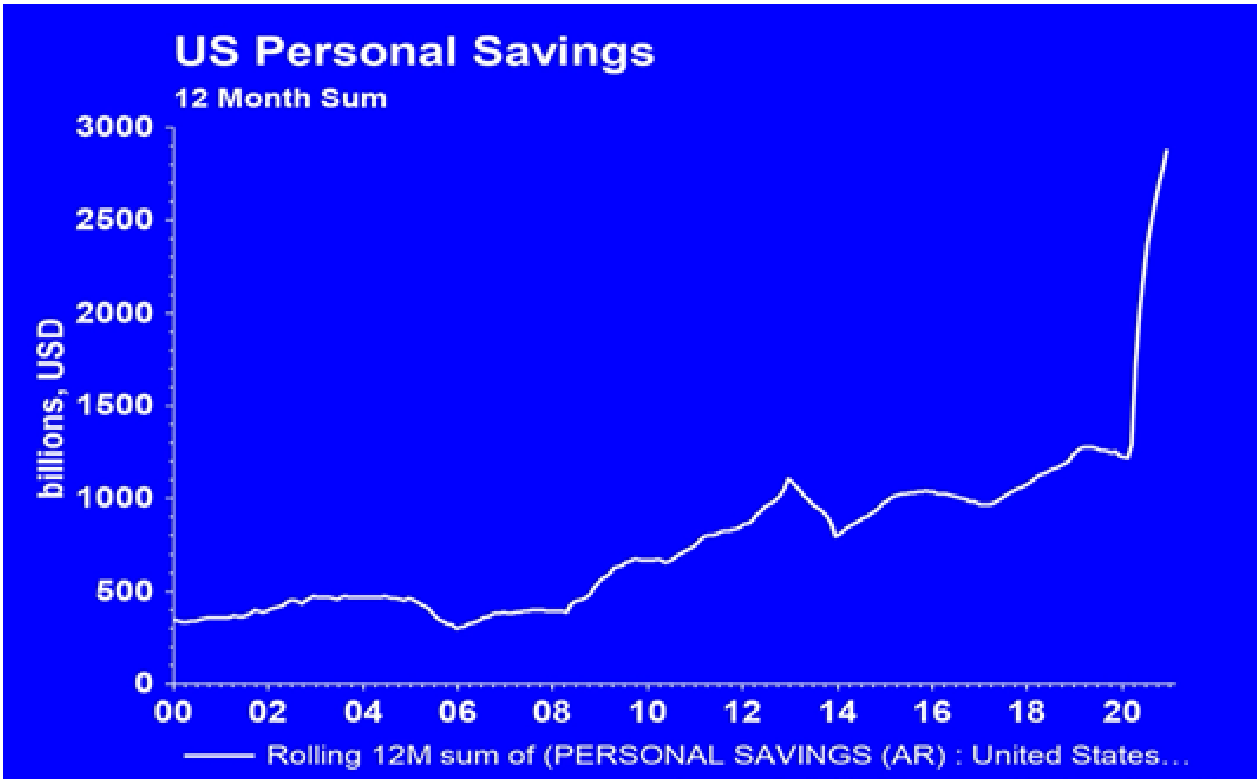
The yield on the benchmark US 10-year continued its recent rise to a high of about 1.6% last Thursday, its highest point in over a year and roughly three times the level it was at just nine months ago. As we have recently spoken about in our daily market commentary, this increase in government bond yields is a reaction by market participants to an expected rise in inflation due to pent up demand and a robust economic recovery. In our opinion, slightly higher inflation, a stronger-than-expected overall economic rebound, and consumer pent-up demand are all positive things for main street, however the arrival of all three simultaneously did temporarily spook Wall Street.

	1 Month	3 Month	YTD	1 Year
Equity Indices				
S&P 500	4.99%	7.67%	3.80%	31.96%
NASDAQ	3.50%	10.85%	4.89%	57.79%
DAX	4.32%	5.43%	2.14%	17.85%
EuroStoxx 50	6.47%	6.13%	4.33%	11.33%
ISEQ	6.68%	4.63%	1.92%	17.51%
FTSE	2.83%	5.14%	1.98%	0.12%
Multi-Asset Funds				
Aviva Cautious (Risk 3)	-0.51%	1.13%	0.07%	1.79%
Irish Life MAPS 3	-0.75%	1.70%	0.84%	1.31%
New Ireland iFunds 3	-0.16%	1.14%	0.40%	2.46%
New Ireland PRIME 3	-0.43%	0.69%	0.52%	-1.44%
Zurich Prisma 3	0.77%	1.88%	1.24%	4.58%
Aviva Strategic (Risk 4)	0.31%	3.43%	2.11%	2.82%
Irish Life MAPS 4	-0.81%	2.50%	1.31%	1.73%
New Ireland iFunds 4	0.00%	2.52%	1.52%	5.32%
New Ireland PRIME 4	-0.68%	2.11%	1.55%	-1.73%
Zurich Prisma 4	1.54%	4.00%	2.63%	9.72%
Aviva Dynamic (Risk 5)	1.10%	5.43%	3.84%	4.11%
Irish Life MAPS 5	-1.08%	3.78%	2.24%	3.98%
New Ireland iFunds 5	0.28%	4.38%	3.04%	8.35%
New Ireland PRIME 5	-0.69%	3.62%	2.65%	-1.17%
Zurich Prisma 5	2.19%	5.65%	3.68%	15.18%
Currencies				
EUR/USD	-0.80%	0.92%	-1.43%	9.18%
EUR/GBP	-2.32%	-3.36%	-3.11%	0.60%
GBP/USD	1.55%	4.46%	1.76%	8.53%
USD/JPY	2.02%	2.42%	3.47%	-1.18%
Fixed Income				
US 10yr	0.376	0.526	0.525	0.352
Bund 10yr	0.176	0.187	0.235	0.284
Irish 10yr	0.160	0.191	0.294	0.145
Gilt 10yr	0.428	0.398	0.558	0.342
Commodities				
Gold	-7.03%	-3.37%	-9.19%	8.64%
WTI Crude Oil	15.21%	32.64%	23.83%	34.23%

Source: Seaspray Private

Profits are headed up and have much further to go, while interest rates would have to move substantially higher for us to turn at all bearish. Yes, the 10-year Treasury yield in the US hit 1.5% last week, but it would have to go to at least 2.0% or higher before it'd be a headwind for equities, in our view.
At current levels, we believe certain areas within the market still represent reasonable value, supported by the Federal Reserve and other central banks globally who are continuing their accommodative stance, fiscal stimulus will boost economies by borrowing from the future, and vaccine rollout is becoming more promising.

We do note that once the first half of the year is behind us, developed regions such as the Eurozone, UK, and US will likely be in a completely different place than we have known for almost a year now, and for the better this time. As the possibility to spend emerges with re-openings in the second and third quarters of 2021, we have a high conviction that consumers and producers are willing and able to spend excess savings as employment improves and consumer risk aversion drops. As we have noted in previous investment updates, global personal savings ratios are at the highest levels in decades for major developed economies such as Germany, Ireland, the UK and US (demonstrated in the below chart).



Source: Refinitiv Datastream, Fathom Consulting

"Global personal savings ratios are at the highest levels in decades for major developed economies such as Germany, Ireland, the UK and US"

Global Overview

Recent economic data releases over the last few weeks show that the recovery in the US economy is gaining momentum in early 2021, even before President Biden's proposed $1.9 trillion fiscal stimulus package is passed into law. The most eye-watering release was the 5.3% jump in US retail sales in January, which far exceeded the forecast rise of 1%, with broad based gains in household spending. Meanwhile, manufacturing output rose by 1% in the month and is now just 1% below its pre-pandemic level. Flash PMI data for both the manufacturing and services sectors remained at high levels in February also, despite much of the North America being in the grips of severe weather. In Europe, February's PMI data saw mixed results as most of the continent remained under relatively harsh restrictions designed to contain to virus. The Eurozone Manufacturing PMI came in at a robust 57.7 versus consensus expectations for 54.6. Conversely, the Services PMI result for the region was a contractionary 44.7 versus 45.9 forecasts.

The huge amounts of stimulus provided by central banks and governments during the pandemic have given rise to worries about the possible return of inflation after economies recover (assuming a successful vaccine rollout). This has been reflected in rising bond yields particularly in the US where 10-year Treasury yields are back to pre-pandemic levels (albeit only c.1.5%). We see some potential investment implications from higher US inflation expectations. Looking at data going back to 2009, we find that value-orientated equity regions like the UK and emerging markets typically outperform their global peers in a rising US inflationary environment. These markets benefit from their relatively high exposure to value sectors, such as financials, materials and industrials, and low valuations. Both the UK and emerging markets are also likely to profit from an easing in idiosyncratic risks. UK equity valuations should improve following the Free Trade Agreement in goods agreed with the EU at the end of last year, while emerging markets should gain from an expected multilateral approach by the US over trade policy.

Over the last month or so we have seen the British Pound continue its strong start to the year, EUR/GBP and GBP/USD trading below 0.86 and above 1.42 last week, respectively. As the United Kingdom has now vaccinated (first dose) over 31% of its population and Covid-19 cases continue to decline, more restrictions continue to be lifted. According to Boris Johnson's new plan for the nation to emerge from the pandemic, the UK could see all legal limits on social contact lifted by June 21st, ahead of any other European nation's timeline currently. In addition, we would like to point out that with the risk of a 'no deal' Brexit no longer hanging over markets, the persistent undervaluation of the Pound in recent years has recently, and should continue to, dissipate.

The corporate results season is almost over, but it is interesting to look at the trends given the huge disruption caused by the virus. If we look at the US, roughly 4 out of every 5 companies have beaten expectations this time around, with earnings growing by about 7% year-on-year. Revenue numbers have been less robust, but importantly still positive for the twelve months, growing by 2% on average. Turning to Europe, around 70% of reporting companies have beaten consensus, but here the numbers look less impressive with both earnings and sales down by around 15% from the previous year.

The difference compared with the US is largely accounted for by the higher concentration of energy, resource and financial companies in the European indices compared with the US. America also has a much larger proportion of technology businesses which have fared relatively well in the Covid world. The global economic recovery is starting to look different to the ones we have become used to over the past decades. The strong focus of fiscal stimulus aimed at boosting the real economy instead of monetary stimulus focused on stabilizing the financial sector makes this more of an ‘old school recovery’, as we see it. Old school, as in the real economy gradually starts to take center stage in the macro news flow, spurred by positive multipliers from past and future extraordinary fiscal and monetary stimulus.

Monetary & Fiscal Policy

From an economic perspective, the most important events of the past month or so were President Biden’s proposed $1.9 trillion fiscal plan and Fed Chair Jerome Powell doubling down on his dovish policy framework. The former tries to push yields higher, the latter drags them lower. The winner, as we have seen, is the equity market. In 2017, following the previous US election, the S&P500 rallied 20% for the year with no more than a 3% pull back on a combination of the hope of a Trump stimulus package, loose monetary conditions and the so called “global synchronized recovery”. We must remember that 2021 will have a significantly larger global fiscal stimulus, substantially easier financial conditions, and a global economic recovery dwarfing anything seen in recent years.

From the monetary side: Last week we saw Fed boss Jerome Powell carry out his semi-annual testimony to Congress which was closely watched by investors, in which he told the House of Representatives Committee on Financial Services that the central bank won't change its extremely accommodative stance until the United States’ economy is clearly improving, particularly the labor market. We are confident that the central bank will thus look through any near-term spike in inflation. “Our policy is accommodative because unemployment is high and the labor market is far from maximum employment," Powell said during his statement last week.

The ECB recently also emphasized that it wants to maintain favourable financial conditions, and left open the possibility of recalibrating the size of asset purchases in its Pandemic Emergency Purchase Programme (PEPP), if required. The Bank of Japan announced plans to review its current policy tools in coming months with a view to making policy more effective and sustainable. Comments from the Bank of England suggested that while negative interest rates are a tool which should be at its disposal, associated costs for the banking sector could mean that these might not be introduced in the short term.

On the fiscal side: Over recent weeks market participants have been looking to the US. The scale of the proposed Biden fiscal stimulus is enormous at $1.9 trillion, sitting at circa 9% of GDP and almost three times the size of the estimated output gap, this is also taking place in an economy that is close to fully rebounding from the Covid-19 recession. As we have been saying for some time, interest rates will remain at or near zero for a long time to come, and governments around the world will be reluctant to curtail fiscal spending. Economic recovery is evident in the data, with very high excess savings amongst consumers and high cash levels on corporate balance sheets.

Equities

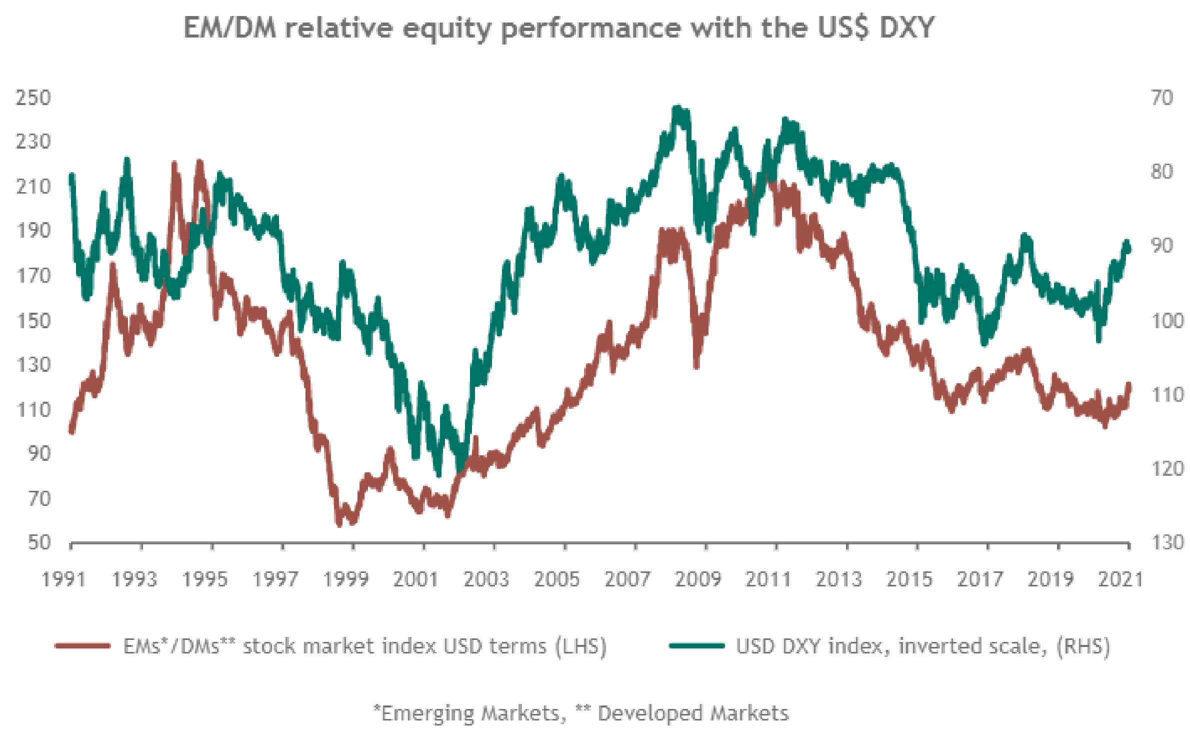
As we alluded to in our recent 2021 investment outlook, we remain overweight specific equities and sectors versus core bonds, as we, along with market participants around the globe, look through the near-term drag of the virus and slow vaccine supply, and instead focus on a resilient global economy with grounds for greater optimism for the second half of 2021. We believe that stocks in value-oriented sectors will strongly outperform bonds and 'growth' stocks this year thanks to the general global economic recovery and the compelling prospects of a resolution to the pandemic.

While equity markets may seem expensive in absolute terms, we reiterate that they remain attractive in relative terms, given the low and in some cases negative yields available on assets such as bonds and cash. Despite their rise in recent weeks, government bond yields still remain near or at generational lows and in our view justify higher-than-average valuations in equity markets. With the global economy in the initial stages of a new cycle and strong economic and earnings growth forecast over the next two years, upside of at least mid-to-high single digits in global equities is expected for the remainder of 2021, from current levels. Potential risks to this bullish outlook include a near-term resurgence in global Covid-19 cases and a failure to contain the virus; vaccines proving to be ineffective against a number of Covid variants, which would threaten the improving growth backdrop; fiscal and monetary supports being reduced; or a significant rise in bond yields, which would diminish the relative valuation case for equities. The probability of most of these occurring is viewed as being very low. We acknowledge that smaller bouts of volatility could remain a feature in markets if any of these issues become a cause for concern over the course of 2021, with little to no chance of a repeat of the extreme volatility that we witnessed during the beginning of the pandemic.

As we head into March and towards the end of the first quarter of the year, equities remain our favoured asset class, we strongly believe in the reopening theme and that we are in the early stages of a new economic cycle. We currently see any 'bubble' talk as premature, under the circumstances which we find ourselves in as investors. Firstly, rates are still exceptionally low and are expected to remain so on a tactical horizon. Secondly, valuation ratios are positively correlated to net earnings upgrades, which are typically seen in the early recovery phase of a business cycle. We expect a return to trend level earnings during the second half of 2021 as economies reopen, implying a global EPS growth of at least 20%, with risks to the upside. Lastly, piercing potential financial bubbles are of lesser concern for central banks at this juncture, as they are fully focused on their role as fiscal financier to meet their mandates (2% inflation and full employment).

The outlook for stocks for the next 6-12 months looks bright as we move closer to full vaccination and the lagged effects of fiscal and monetary stimulus peak. In the short term, some cautiousness may be warranted given exuberant sentiment levels within certain sectors and regions, positioning squeezes and weaker macro momentum.

At present we are concentrated on the laggards of the 2020 rally, with an overweight position in Europe, Japan, and emerging markets, as they will benefit most from a global cyclical recovery in a weaker dollar regime. So far in 2021 the Eurozone market has lagged its US and Asian counterparts as the speed of the region's vaccine rollout has been frustratingly slower. While we accept that lockdowns here are unlikely to be lifted until a significant proportion of the population is inoculated, we see earnings momentum as positive in the region and leading economic indicators suggest the damage to the economy may not be as bad as forecast. We also favour certain UK equities on a tactical basis. The removal of uncertainty over a Brexit deal should see the risk premium on UK assets attached to that outcome erode. We see sector-specific UK large-caps as a relatively attractive play on the global cyclical recovery as it has lagged peers. We note that the US Dollar has weakened by around 9% (DXY index) since the start of the pandemic as the Federal Reserve sought to stimulate demand by cutting interest rates. The chart below shows how emerging market equities tend to outperform their developed market peers when the dollar weakens.



Source: Refinitiv Datastream, Smith & Williamson Investment Management LLP

Although so far this year the dollar has strengthened marginally, we expect it to resume its downtrend as US inflation picks up relative to the rest of the world. Allied with lower valuations, this should drive continued outperformance of emerging market equities, particularly in Asia, where the impact of the coronavirus has been more muted.

Despite our regional and sectoral picks for the year, we see a strong likelihood that the across-the-board equity momentum from 2020 will continue throughout this year. Our expectation for more upside is supported by 1) above-trend, above consensus global growth, 2) double-digit earnings catch-up, 3) limited structural imbalances and scarring effects, 4) a predictable, macro-guided Federal Reserve, and 5) a near-zero policy rate. Compositionally, earnings growth may drive returns more than valuation, as is common in expansionary phases.

At Seaspray we employ an active management approach with regard to our regional, sectoral, and specific equity exposure. We invest in a high conviction, global portfolio of companies with the aim of maximizing its total return to our clients over the long term. We look for strong, well run businesses which offer the best potential durable growth and income opportunities for the future. With regard to our core stock list, we think in terms of owning companies rather than renting shares and look to select investments based on an individual company or fund's fundamental characteristics.

A long-term approach is taken, we choose to analyse using a range of questions which aim to assess: the strength of management, a company's competitive and financial positions, the customers' perspective, prospects for sales and margins, current and potential valuation, how the market and our own views differ and what will happen after five years.

In summary, in our view, despite the stretched sentiment levels, there is reason to remain constructive on risk assets going forward, especially equities and commodities. We expect an 'old school' recovery, driven by pent-up consumer demand as well as corporate investments later in 2021. The old school recovery will undoubtedly be beneficial for the equity market, as it magnifies the expected spike in earnings growth.

Inflation & Bond Yields

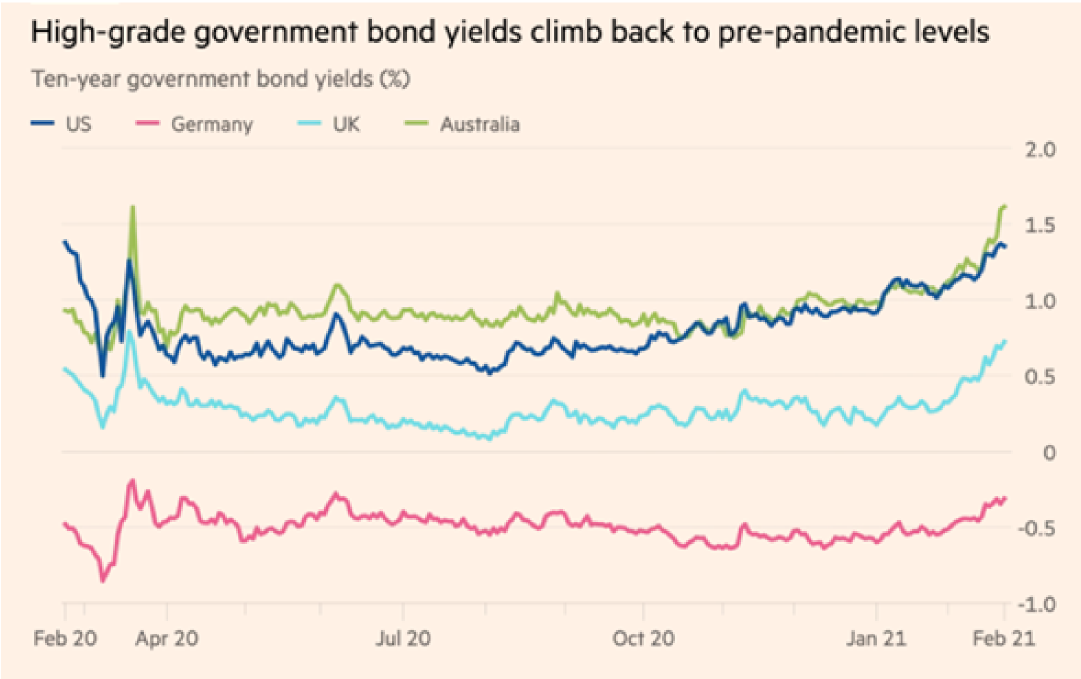
The direction of inflation, and particularly in the US, is likely to be an important determinant for relative equity market performance. US 5-year inflation expectations have swung round from below 0.5% per annum when the pandemic hit last March to almost 2.5% currently, the highest rate the reading has been at for a decade (see chart below). This is consistent with the Fed's policy change last summer to encourage higher inflation. We also believe that the macro backdrop appears a little more inflationary at present. Given high involuntary household savings rates from fiscal stimulus, pent-up cyclical consumer demand could absorb slack in the economy, as a result of the pandemic easing relatively quickly. While significant policy easing is typically cause for inflationary concern, sizeable slack in the economy from depressed capacity rates and elevated unemployment levels should keep inflation relatively contained in 2021. Although inflation is expected to receive a boost from base effects mid-year given Covid-driven weakness mid-last year, we anticipate this rise to be transitory, with the US Core PCE inflation reading expected to end the year at circa 1.8%.

Source: Refinitiv Datastream

As investors have been growing in confidence that the rollout of Covid-19 vaccines will boost economic growth and inflationary pressures, the global bond market is suffering its worst start to a year since 2015. In terms of total return terms (accounting for price changes and interest payments), the Bloomberg Barclays Multiverse Index which tracks $70tn worth of debt has lost 1.9% since the end of last year. If this performance is sustained it would be the sharpest first-quarter setback since 2015 for the index and the worst quarterly performance since 2018. Longer term US treasuries have lost over 9% on a total return basis this year according to a Bloomberg Barclays Index of US Government bonds. In terms of shorter duration, US 2-Year yields have hardly moved and have in fact tested their all-time lows in recent weeks, suggesting very few prospects of an increase in short-term growth. But the 10-Year is sending a very different signal having crossed the 1.5% yield threshold in February and continuing to steadily creep higher in response to the massive fiscal support package to come in the States.

As we alluded to in our 2021 investment outlook, we expect medium-longer duration yields to grind higher from here, driven by higher inflation expectations and the resumption of the global economic recovery.

Duration risks are much higher for both longer-dated corporate and government bonds. In addition, improving economic momentum will translate into a sharp increase in company earnings, limiting worries about coverage ratios and leverage. Yet, at current spread and yield levels, high yield bonds offer little protection against adverse circumstances which hamper the economic recovery. With the already significant impact that Covid-19 has had on corporate health, default risk could start to rise quickly if the recovery falls short. Hence, we remain neutral in global high yield bonds.



Source: Refinitiv, Financial Times

We remain strategically underweight nominal government bonds as their ability to act as portfolio ballasts are diminished with yields near lower bounds and rising debt levels may eventually pose risks to the low-rate regime. This is part of why we are not huge fans of government debt at present. We prefer inflation-linked bonds as we see risks of higher inflation in the medium term. Although interest rates are gradually increasing as economies recover from the pandemic and vaccines are being rolled out, we don't expect a sharp pick up. The upward move will probably be slow and drawn out, in our view. We continue to prefer emerging market bonds because of attractive valuations, the likely support from a weaker US Dollar, and hopes that the Biden administration will enact a friendlier policy towards trading partners.

Warning: The value of your investment may go down as well as up and you may lose some or all of the money you invest**. Warning:** Past performance is not a reliable guide to future performance. **Warning:** Investments denominated in a currency other than your base currency may be affected by changes in currency exchange rates.

https://seasprayfinancialservices.ie/important-disclosures/

This material is approved for distribution in Ireland by Seaspray Financial Services Ltd .It is intended for Irish retails clients only and is not intended for distribution to, or use by, any person in any country where such distribution or use would be contrary to local law or regulation. Seaspray Financial Services Ltd Ire ("SFS") is regulated by the Central Bank of Ireland.

Where SFS wishes to make this and other Seaspray Financial Services Ltd research available to Retail clients, such information is provided without liability and in accordance with our terms and conditions that are available on the SFS website.

No report is intended to and does not constitute a personal recommendations or investment advice, nor does it provide the sole basis for any evaluation of the securities that may be the subject matter of the report. Specifically, the information contained in this report should not be taken as an offer or solicitation of investment advice, or to encourage the purchased or sale of any particular security. Not all recommendations are necessarily suitable for all investors and SFS recommend that specific advice should always be sought prior to investment, based on the particular circumstances of the investor either from your SFS investment adviser or another investment adviser.

SFS takes all responsibility to ensure that reasonable efforts are made to present accurate information but SFS gives no warranty or guarantee as to, and do not accept responsibility for, the correctness, completeness, timeliness or accuracy of the information provided or its transmission. This is entirely at the risk of the recipient of the report. Nor shall SFS, its subsidiaries, affiliates or parent company or any of their employees, directors or agents, be liable to for any losses, damages, costs, claims, demands or expenses of any kind whatsoever, whether direct or indirect, suffered or incurred in consequence of any use of, or reliance upon, the information. Any person acting on the information contained in this report does so entirely at his or her own risk

All estimates, views and opinions included in this research note constitute Seaspray Financial Services judgment as of the date of the note but may be subject to change without notice. Changes to assumptions may have a material impact on any recommendations made herein.

Unless specifically indicated to the contrary this research note has not been disclosed to the covered issuer(s) in advance of publication.

Past performance is not a reliable guide to future performance. The value of your investment may go down as well as up. Investments denominated in foreign currencies are subject to fluctuations in exchange rates, which may have an adverse affect on the value of the investments, sale proceeds, and on dividend or interest income. The income you get from your investment may go down as well as up. Figures quoted are estimates only; they are not a reliable guide to the future performance of this investment.

Conflicts of Interest & Share Ownership Policy

It is noted that research analysts' compensation is impacted upon by overall firm profitability and accordingly may be affect ed to some extent by revenues arising other Seaspray Financial Services Ltd business units including Investment Management and Corporate Finance. Revenues in these business units may derive in part from the recommendations or views in this report. Notwithstanding, Seaspray Financial Services Ltd is satisfied that the objectivity of views and recommendations contained in this note has not been compromised. Nonetheless Seaspray Financial Services Ltd is satisfied that the impartiality of research, views and recommendations remains assured.

Analyst Certification

Each research analyst responsible for the content of this research note, in whole or in part, certifies that: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research note.

We have assessed the publication and have classed it as Research under MIFID II. All charges in relation to this publication will be borne by Seaspray Financial Services Ltd

EON.