

Six Minute Strategy

Doing battle with the bond markets

19 March 2021

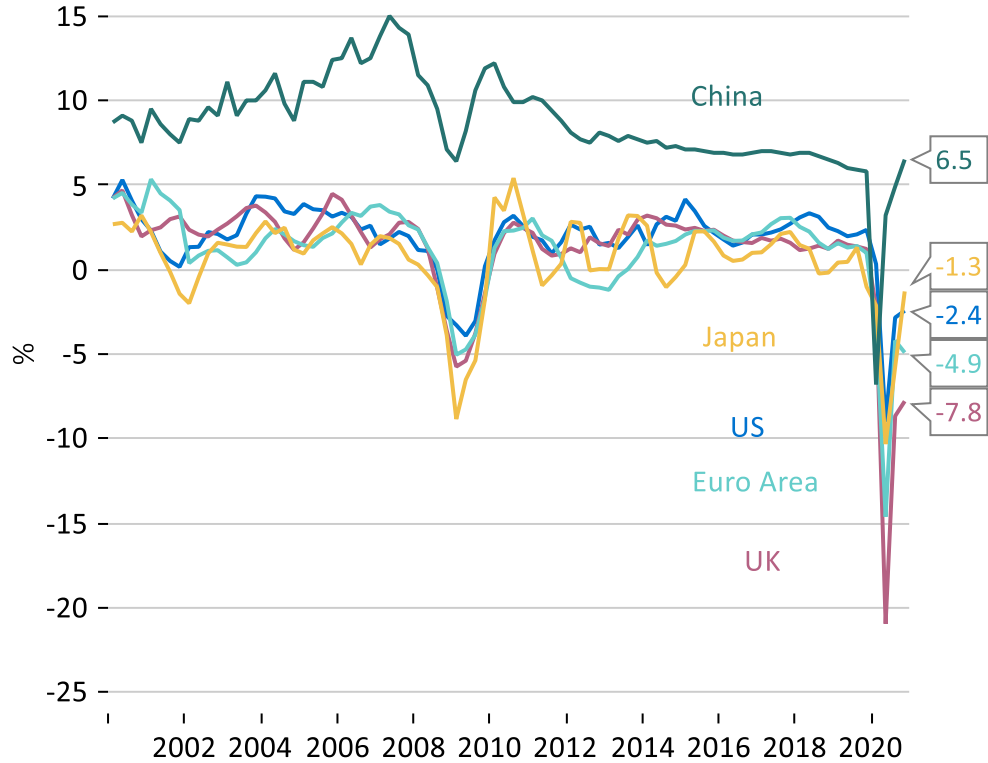


The world economic recovery is accelerating as optimism surges



Economic recovery is sharp but at widely differing rates

Annualised GDP Growth



Source: Macrobond, 19.03.21



Optimism on economic recovery at record levels

Exhibit 3: Record amount of FMS investors expect a stronger economy

Net % Expecting Stronger Economy



Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

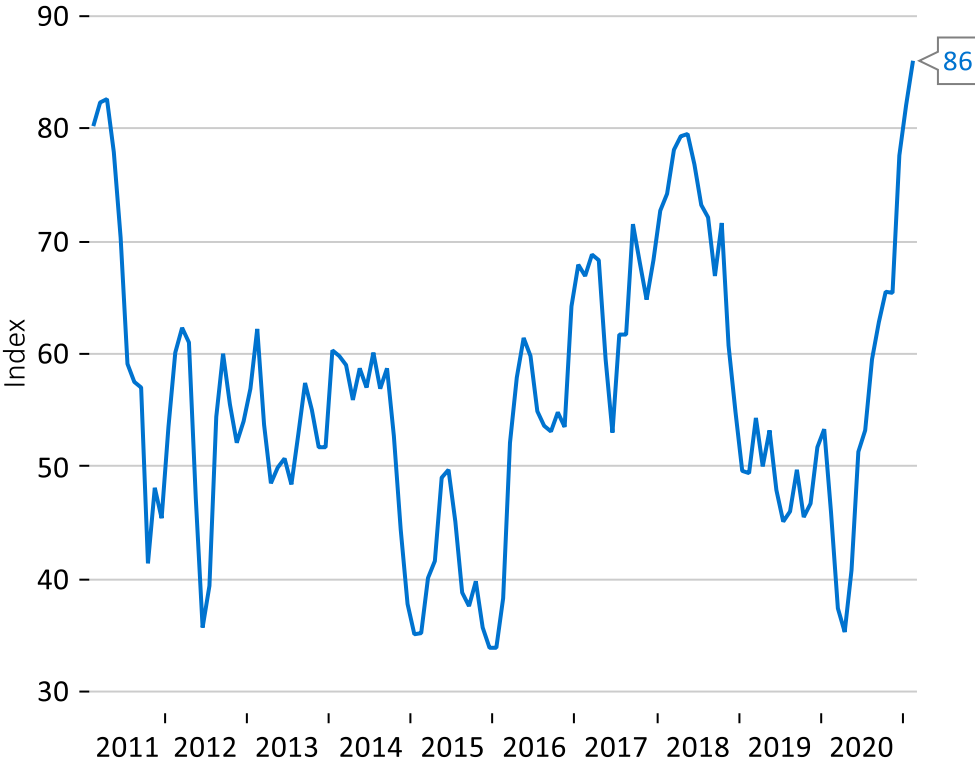
Source: BofA, March 2021

Global pricing pressures are also rising across US & global manufacturing



US manufacturing price surveys at 10 year high

ISM US Manufacturing Prices Paid, Index

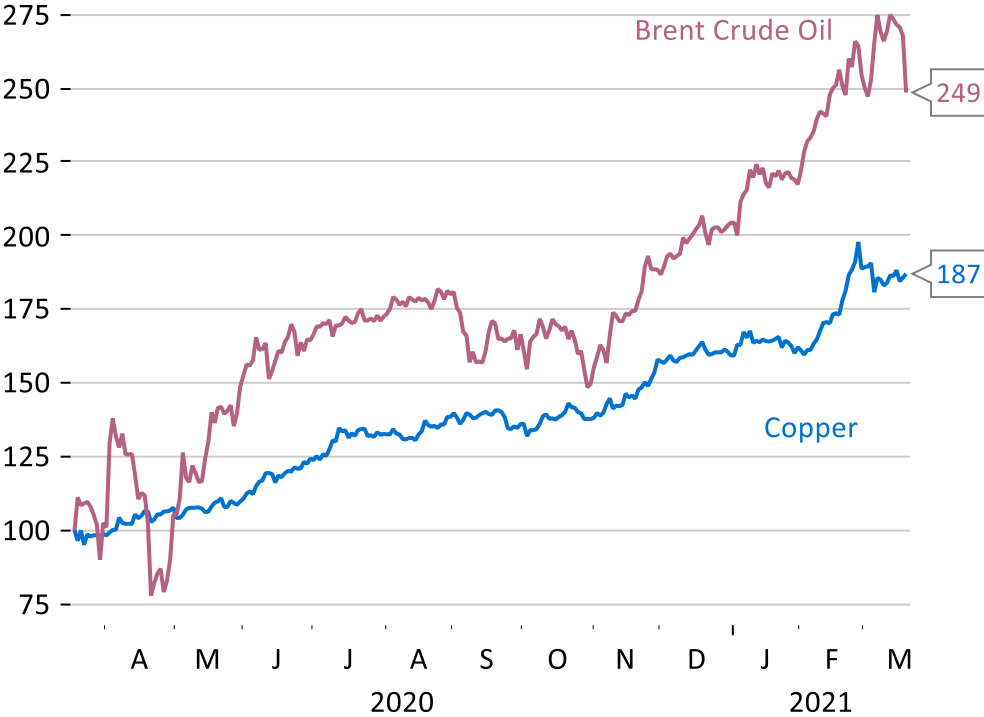


Source: Macrobond, 19.03.21



Extraordinary recovery in oil and copper prices

Metals & Energy returns last 12 months (rebased to 100)



Source: Macrobond, 19.03.21

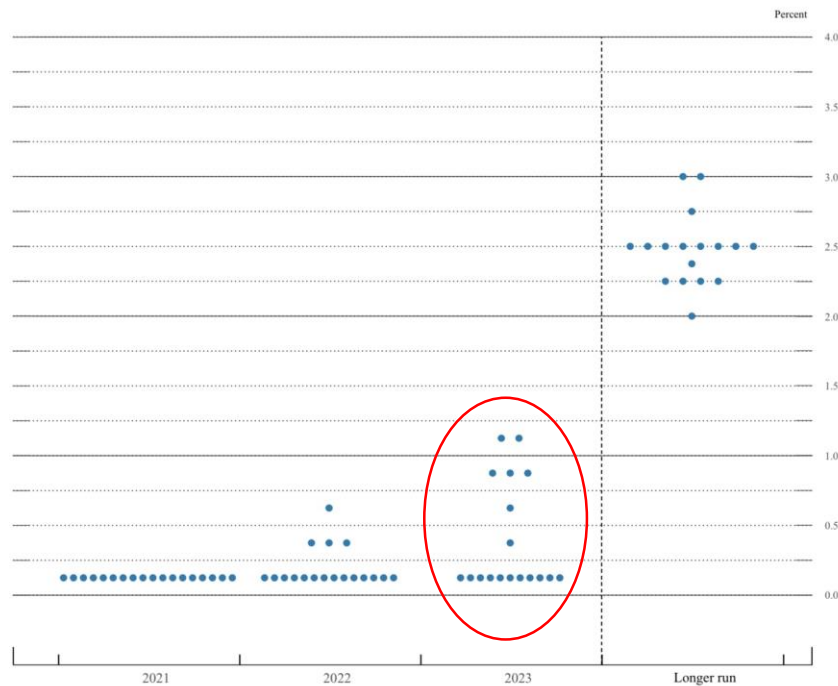
So, is the Federal Reserve's commitment not to raise rates before 2024 losing credibility?



FOMC Dot Plot, March 2021

For release at 2:00 p.m., EDT, March 17, 2021

Figure 2. FOMC participants' assessments of appropriate monetary policy: Midpoint of target range or target level for the federal funds rate

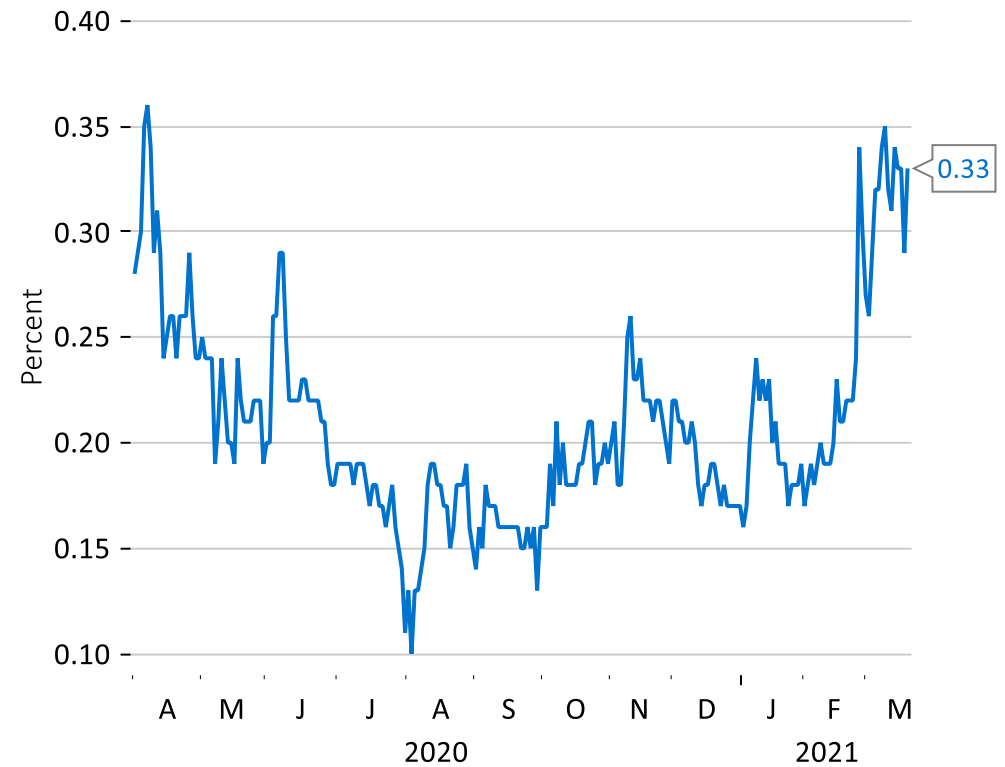


Source: US Federal Reserve, December 2020



Market expectations for rates to rise in 2023

3 Year US Government Bond Yield



Source: Macrobond, 19.03.21

March 2021 FOMC Forecasts (Dec in brackets)

2021 GDP 6.5%(4.2), Unemployment 4.5(5), Core Inflation 2.2 (1.8)

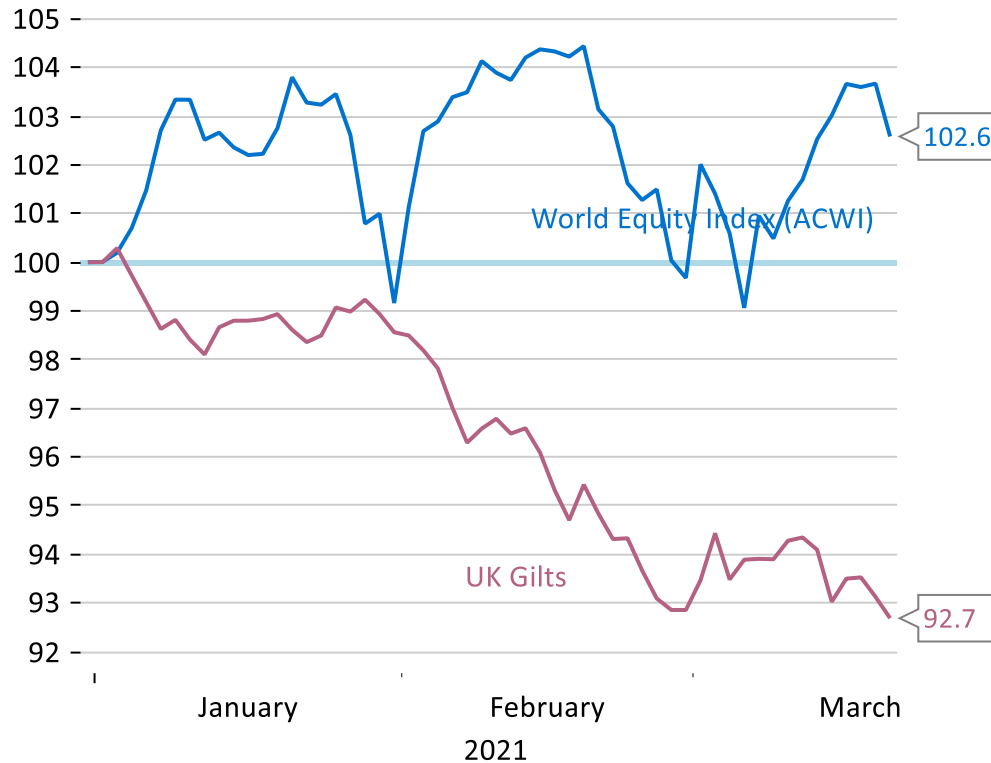
Market performance 2021 to date

Market leadership reverses – UK equities rally - Value recovers – Bonds fall



Equities rally, bonds decline

Global Asset Class Returns 2020 (£) to date

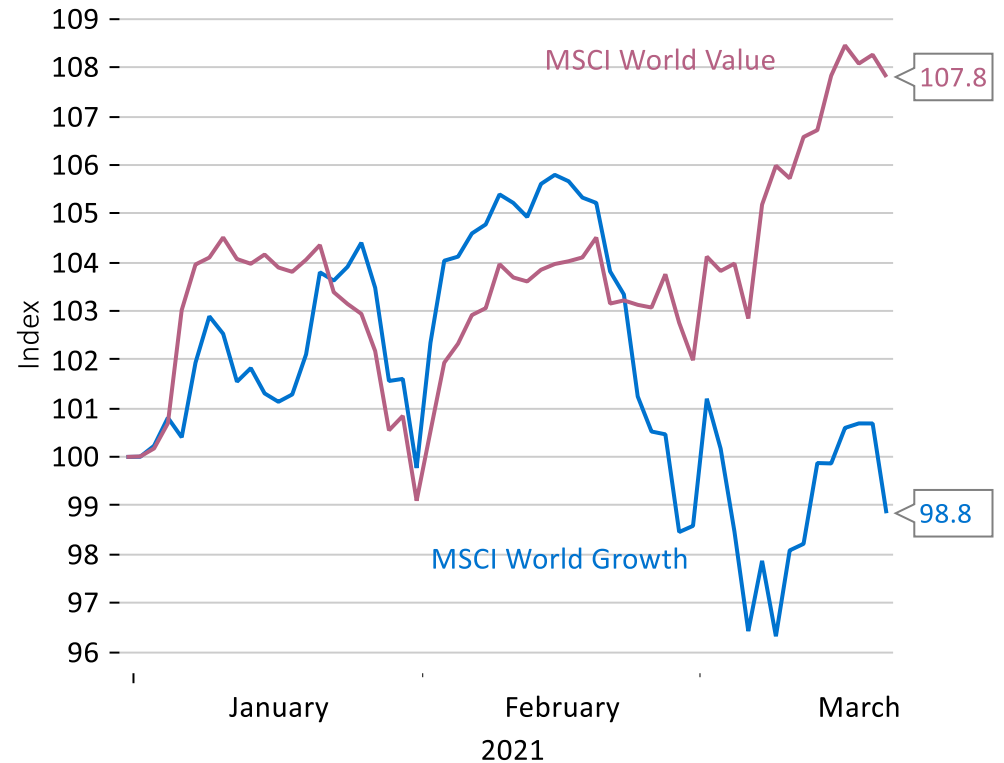


Source: Macrobond, 19.03.21



Value leads global markets

World Equity Style 2021 (£) to date



Source: Macrobond, 19.03.21

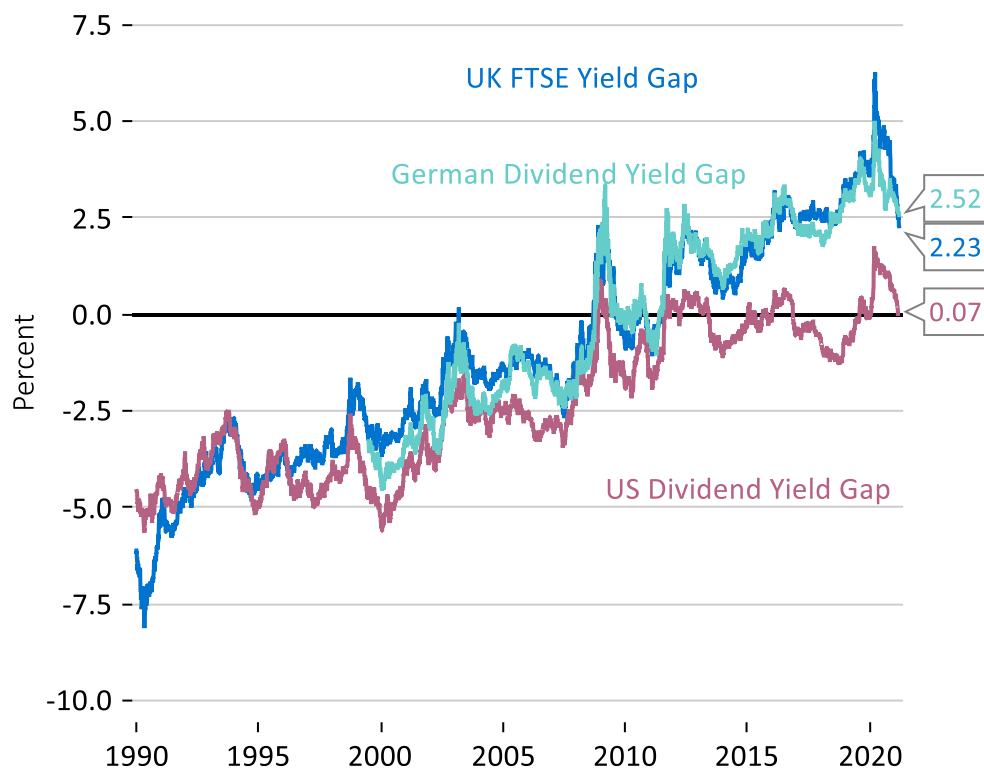
Are there alternatives to bonds?

1. Equity dividends



Global equity markets still offer yield premium to bonds

Equity dividend yield less local 10 year bond yield

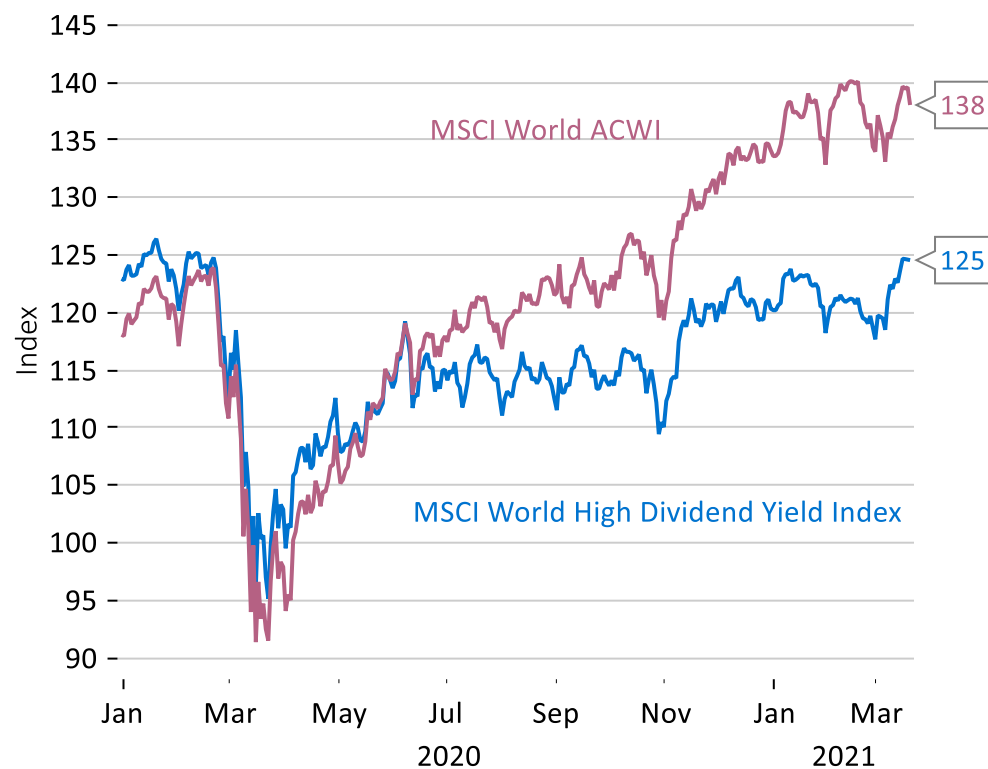


Source: Macrobond, 19.03.21



Higher dividend styles have underperformed since Covid19

World Equity Style 31/12/2019 (£) to date



Source: Macrobond, 19.03.21

Bond alternatives:

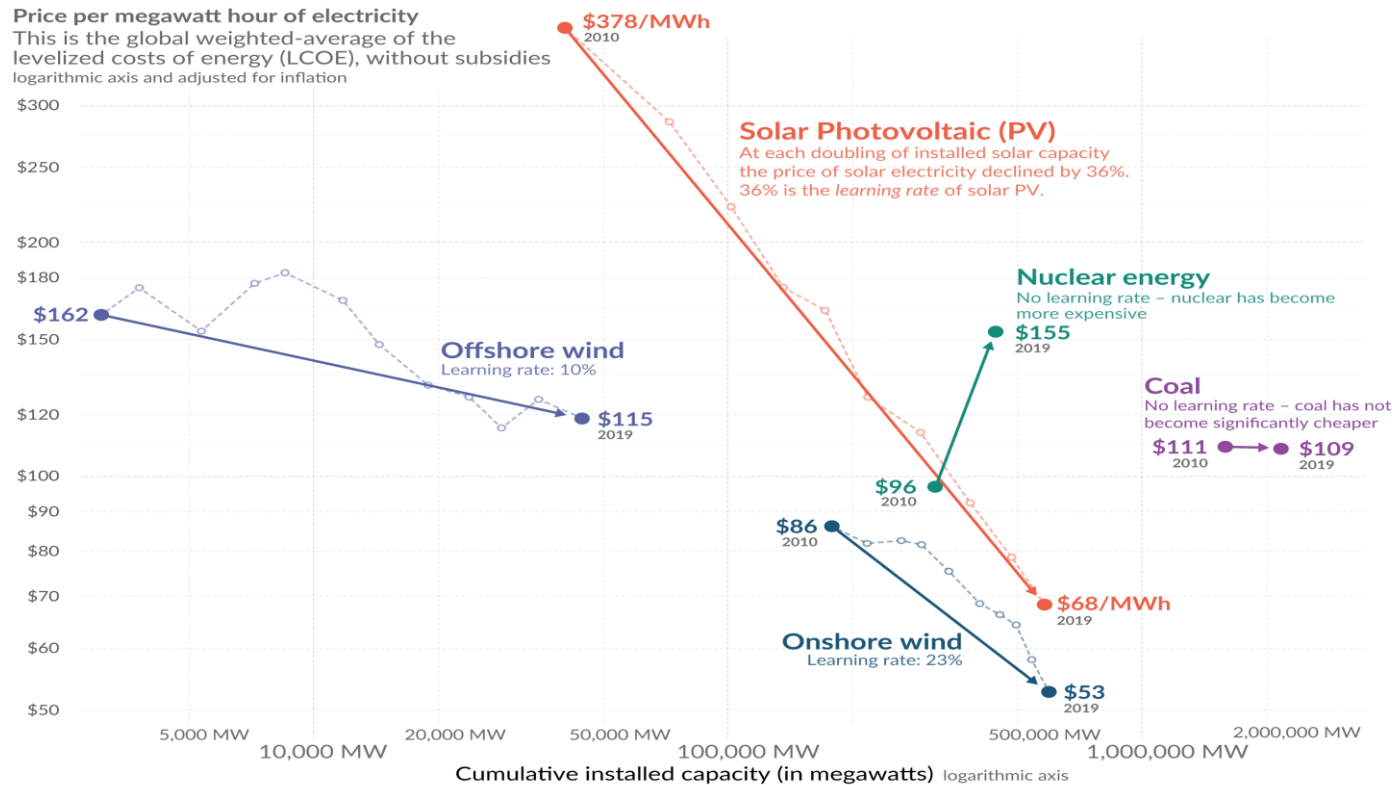
2. Renewable energy infrastructure



Technological change and manufacturing efficiency has transformed the competitiveness of renewables

Electricity from renewables became cheaper as we increased capacity – electricity from nuclear and coal did not

Our World in Data



Source: IRENA 2020 for all data on renewable sources; Lazard for the price of electricity from nuclear and coal – IAEA for nuclear capacity and Global Energy Monitor for coal capacity. Gas is not shown because the price between gas peaker and combined cycles differs significantly, and global data on the capacity of each of these sources is not available. The price of electricity from gas has fallen over this decade, but over the longer run it is not following a learning curve.

OurWorldinData.org – Research and data to make progress against the world's largest problems.

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Source: Our World in Data, March 2021

Vaccine aids recovery - central banks remain supportive

Fiscal and monetary policy the most expansionary in post-war history



Global strategy update March 2021

Bonds	Underweight <ul style="list-style-type: none">• UW Government Bonds – upward drift in US and global yields in 2021 - US 10 Yr. Treasury fair value 1.50%• UW investment grade credit – after a strong H2 2020 spreads offer little compensation for post COVID risks
Equities	Overweight <ul style="list-style-type: none">• OW Global equities – equity risk premium attractive, earnings have scope to surprise on the upside in 2021• OW UK equities – valuations attractive, flow of funds back to UK probable on Brexit deal• OW EM equities – China centric Asia managed COVID well –commodity/energy rally supports other EM
Alternatives	Overweight <ul style="list-style-type: none">• OW Other Alternatives– infrastructure and renewables beneficiaries of fiscal spend - liquidity issues remain• Neutral Uncorrelated Alternatives - Gold a hedge against policy error but vulnerable to any reset in rates
Cash	Underweight <ul style="list-style-type: none">• Central Bank commitment to zero or negative yields for multi-year period• No currency preference
Risks	Current: Resurgence in virus variants in 2021, disorderly bond markets Longer-term: Economic and social scarring from lockdown, valuations stretched, balance sheet impairments only clear in 2021 and beyond

Important information

If you are a private investor, you should not act or rely on this document but should contact your professional advisor.

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SARASIN & PARTNERS

Juxon House
100 St Paul's Churchyard
London
EC4M 8BU

T: +44 (0) 20 7038 7000
www.sarasinandpartners.com

