KEHRLI & ZEHNDER

INVESTMENT COMMENT July/August 2020

- **Disconnection I: Wall Street vs Main Street**

  The correction in financial asset prices in the wake of the Covid-19 pandemic was dire and fierce. The correction of the correction was even stronger, taking many by surprise. Why should the market be valued higher than at the beginning of the year given the impact of a temporary global lockdown on full year earnings, unemployment rates and consumer sentiment? The GAMA tech giants –Google, Amazon, Microsoft and Apple – are each valued more than one trillion dollars setting significant new price highs. The pandemic has accelerated the inevitable path toward digitization and these companies are enablers of this trend.

- **Disconnection II: USA vs China**

  Sadly, the world's two largest economies do not get along these days. The U.S. sees China as a growing threat to its status as global hegemon and China has become increasingly assertive given its rapid ascent and its rapidly growing global economic power.

  On July 1st, China enacted a new security law in Hong Kong which grants China broad powers to crack down on vaguely defined political crimes within and outside Hong Kong. It is rather typical of Chinese laws to be ambiguous and unspecific, which leads to the public imagining the worst-possible outcomes.

  While commentators in the West view this as an assault on the handover agreement between the UK and China, China sees it as its right and duty to re-establish stability in Hong Kong. After all, Hong Kong is part of China since 1997 as "one country – two systems", implying that the ultimate sovereignty for security and safety lies with China.

- **Asset Allocation**

  Going into the summer, we remain slightly underweight **equities**, although with a bias towards increasing exposure. We continue to expect market volatility near-term, especially if a second wave should get out of hand. However, due to enormous amounts of cash sitting on the sidelines, we expect moderate sell-offs to be met quickly by institutional and private investor buying.

  The Fed-Put helped stabilize **fixed income** markets across regions and credit ratings. But by giving out money for free the Fed also created market conditions that will keep bad business models and money-losing companies out of Chapter 11 – for the time being. Zombie companies and moral hazard cannot provide a recipe for a prosperous future. This will be detrimental for careless creditors. We recommend therefore to stay with high-quality issues and reduce foreign currency exposure.

  Gold and especially gold miners will continue their rise. Relentless printing by global central banks and by this debasing fiat currencies and a very supportive macro environment renders gold as a very viable alternative as a store of value.

  The secret to survival in any uncertain environment is to spread our bets. We suggest **diversification** across asset classes, geographies, issuers, instruments, durations and thought processes. We continue to see merits in selective alternative investments.

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