MONACO ASSET MANAGEMENT

Investment Outlook

Q3 2020

Asset Class Returns

Emerging from one of the most unconventional crises, asset returns were positive across the board last quarter. The traditional barometers of economic growth, oil and copper, have already recovered a significant portion of their year-to-date losses, respectively rising by 91.7% and 22% in Q2. Concerns regarding both over-supply and falling demand somewhat disappeared.

Global equities were up +18.7% in Q2. Most regions rallied. The bounce off the March 2020 lows has been strong, suggesting investors were already looking beyond 2021 and pricing in a swift recovery.

Corporate bond spreads have contracted significantly from their highs in Q1. However, a decline in balance sheet quality, the recessionary environment, and low market liquidity continues to drag on markets. Corporate investment grade indices were up 9% and high yield indices rose by as much as 10%. US treasuries were flat in Q2. The search for yield in the second quarter has led emerging market bonds to outperform other regions, posting returns over of 10%.

On the other end of the spectrum, gold continued to build on its momentum (c.+12.9% in Q2) while assuming its inflation protection and safe-haven status by remaining the best performing asset class this year.

Chart 1. USD - Denominated Returns

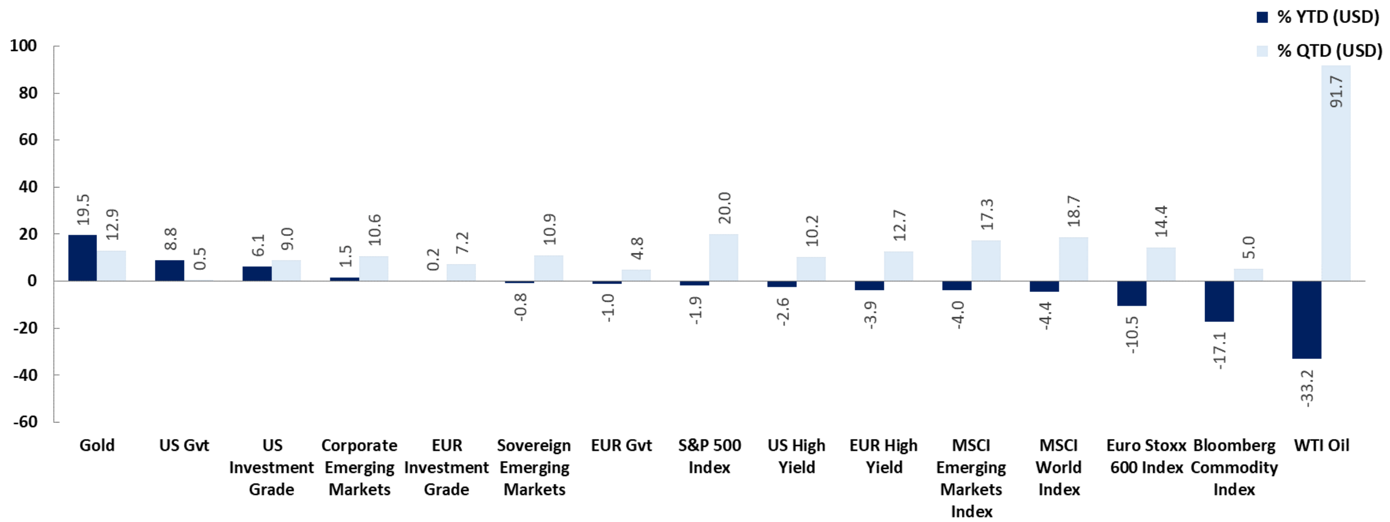
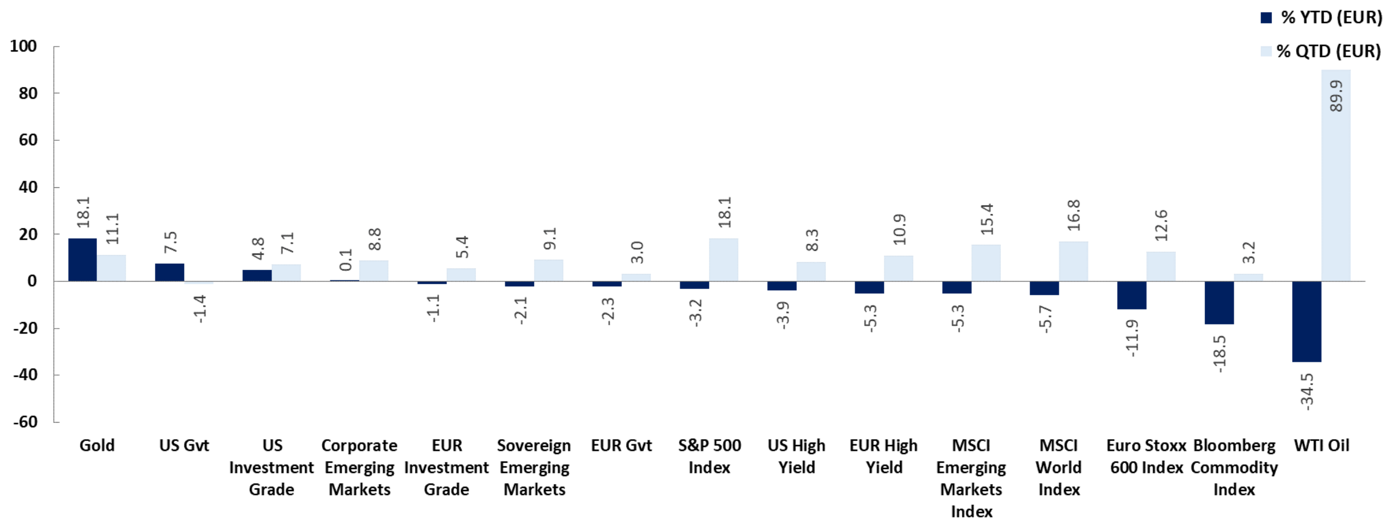


Chart 2. EUR - Denominated Returns



Investment Stance Overview

Conclusion. Within 6 months in 2020, we have lived a true roller-coaster experience on a personal level and in financial markets. Following the swift rally across all assets classes in Q2 2020, the starting point in Q3 is very different and complex. Financial markets will trade nervously over the coming weeks in response to elevated valuations, the potential for a second wave of the Covid-19 pandemic, the looming US fiscal cliff and the prospect of the US elections. That said, the US Congress will ultimately extend fiscal support for households and firms. Around the world, both fiscal and monetary policy will remain highly accommodative. Many institutional investors missed the rebound in stocks and are eager to get back in. This should provide a supportive backdrop for equity markets. As a result, we expect equity markets to trade within a +/- 7-10% range in Q3 2020. We keep an overall low allocation to equities while tactically adding to this asset class in market pull-backs. Our central thesis is that the pandemic was the unexpected growth and supply shock that will ultimately lead to longer-term inflation. In response to higher inflation expectations, global bond yields should rise modestly over the next few years. Credit looks unattractive to us on an absolute basis and relative to equities. The US dollar may be entering a bear market. A weaker US dollar will boost commodity prices and Emerging Markets assets. Complacency is running high in financial markets. It is time to remain vigilant; especially as Q3 (i.e. the summer months) is usually impacted by lower market liquidity.

	Investment Stance						Quarterly Change*
	Very Bearish	Bearish	Neutral	Bullish	Very Bullish		
SOVEREIGN BONDS						**BEARISH DM**	-
US							-
Europe (Core)							-
Europe (Periphery)							-
Emerging Markets							-
CORPORATE BONDS						**BEARISH DM**	-
US High Yield							-
US Investment Grade							-
EUR High Yield							-
EUR Investment Grade							-
Emerging Markets							-
CURRENCY						**BEARISH USD**	-
USD							-
EUR							-
EM							-
JPY							-
GBP							-
EQUITIES						**CAUTIOUS**	-
US							-
Europe							-
UK							-
Japan							-
Emerging Markets							-
COMMODITIES						**BULLISH**	-
Energy							-
Precious Metals							-
Agriculture & Livestock							-
ALTERNATIVES						**BULLISH**	-
Hedge Funds							-
Real Estate							-
Private Equity							-

** Change compared with previous months. One arrow means the stance has moved one place to the left or the right, two arrows means a move of two places, etc.*

Model Portfolios

The following model portfolios are based on current positioning at the start of Q3 2020. Considering the volatile nature of financials markets and our outlook, their compositions is likely to change throughout the quarter.

USD Based Portfolios

Asset Class	Last Price	Perf. 5D	Perf. MTD	Perf. YTD	MAM Outlook	Asset Allocation
Currencies						
Portfolio Bases						**97.0%**
EUR	1.13	0.9%	0.9%	1.1%	Bullish	10.0%
USD	96.38	-1.0%	-1.0%	0.0%	Bearish	87.0%
Others						**3.0%**
JPY	107.28	0.2%	0.6%	1.2%	Bullish	3.0%
Equities						**25.0%**
Developped Markets	**52.33**	**2.4%**	**2.4%**	**-10.0%**	Bearish	**18.0%**
Europe	367.53	-0.2%	2.0%	-11.6%	Bearish	5.4%
North America	3,169.94	2.2%	2.2%	-1.9%	Bearish	10.8%
Great Britain	6,121.92	-1.9%	-0.8%	-18.8%	Bearish	0.9%
Asia Pacific	22,529.29	1.7%	1.1%	-4.8%	Bearish	0.9%
Emerging Markets	**1,070.14**	**4.6%**	**7.5%**	**-4.0%**	Bullish	**5.0%**
Asia Pacific	615.62	3.9%	6.6%	0.3%	Bullish	3.3%
EMEA	213.14	0.6%	3.1%	-20.3%	Bullish	1.2%
South America	1,976.50	3.0%	5.9%	-32.3%	Bullish	0.5%
Thematic						**2.0%**
Asset Allocation	31.77	2.2%	2.2%	-5.1%	Bullish	2.0%
Fixed Income						**15.0%**
Europe						**0.0%**
Sovereign	221.32	0.1%	0.0%	0.8%	Bearish	0.0%
Investment Grade	250.14	0.2%	0.3%	1.3%	Bearish	0.0%
High Yield	391.17	0.3%	0.6%	-5.3%	Bearish	0.0%
North America						**3.0%**
Sovereign/Tips	2,764.12	0.5%	0.5%	7.7%	Bullish	3.0%
Investment Grade	3,439.58	0.9%	1.1%	6.1%	Bearish	0.0%
High Yield	2,126.12	1.0%	1.3%	-2.6%	Bearish	0.0%
Emerging Markets						**7.0%**
Local Currency	399.60	0.9%	1.2%	-0.8%	Bullish	7.0%
Hard Currency	1,215.00	0.7%	0.9%	0.5%	Neutral	0.0%
Others						**5.0%**
Convertible	865.62	0.5%	1.2%	4.2%	Bearish	0.0%
Trade Finance	110.40	0.0%	0.1%	2.6%	Neutral	0.0%
Broad Funds	530.12	0.5%	0.6%	3.6%	Bullish	5.0%
Commodities		**3.1%**	**3.4%**	**-17.0%**		**12.0%**
Agriculture	57.58	0.5%	2.4%	-16.0%	Bullish	1.7%
Energy	20.13	5.9%	5.6%	-43.5%	Bullish	1.7%
Industrials	109.68	4.8%	4.9%	-4.2%	Bullish	1.7%
Precious Metals	214.25	2.7%	1.3%	14.8%	Bullish	7.0%
Alternatives						**20.0%**
Hedge Funds	1,284.58	0.2%	0.5%	-0.6%	Bullish	15.0%
Real Assets	1,579.92	-1.3%	0.3%	-19.6%	Bullish	5.0%
Cash						**28.0%**

EUR Based Portfolios

Asset Class	Last Price	Perf. 5D	Perf. MTD	Perf. YTD	MAM Outlook	Asset Allocation
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MAM Actions

Equities

What have we done?

We came into Q2 with a relatively high indirect exposure to equities. In mid-March 2020 our indicators were showing extreme pessimism in the market and oversold technicals. Equity market volatility was historically high. This, despite policymakers scrambling for monetary and fiscal policy support. We decided to take advantage of high volatility by selling put options on indices and single stocks in Europe and the US. This created the opportunity to earn some premium while owning the underlying at a cheaper price should markets continue to fall. Once over 75% of the potential premium had been earned we decided to unwind these option strategies in order to crystallize gains. We clearly didn't anticipate the strength and magnitude of the historic rally in Q2 2020. We used market pullbacks to place tactical longs in the S&P 500 Index and Euro Stoxx 50 Index; either via ETFs or the sale of put options. We also used the strength in Tesla to sell all the remaining units of the Dispersion Note we launched in February 2019. The last units of this dispersion note were sold at c. $2000, which represents a +395% return based on the unit cost of $404.

Our strategy going forward?

We believe that equity markets will remain range-bound in a c. 7-10% band for the best part of Q3. We will remain disciplined by placing tactical trades in an eventual market pull-back. We are likely to use a combination between ETFs and the sale of index/ single stock put options. We are on the look-out for asymmetric trades such as the dispersion note to put in place during the quarter. We are also looking at different option strategies to take advantage of heightened volatility expected during US elections and into year-end.

Fixed Income

What have we done?

We have been consistently negative Investment Grade and High Yield corporate bonds in EUR and USD. We didn't materially change our allocation to bonds in Q2 2020. However, we reduced our exposure to consumer and corporate lending funds such as Orchardway and Fasanara. Our view that the economic recovery will take longer than expected suggested these funds are at risk of seeing loan losses rise and as a result mark-down their NAVs. We prefer to avoid these funds for now with a view of re-investing once the economic environment stabilizes.

Our strategy going forward?

We are unlikely to change our underweight credit anytime soon unless credit spreads widen substantially. We are looking at different ways to play a steepening of the US yield curve as a way to express our positive outlook for inflation. An alternative is to gain exposure to Treasury Inflation Protected Notes (TIPS). We continue to like EM credit and will add on pull-backs.

Commodities

What have we done?

We have used technical to trade in and out of precious metals throughout the quarter. However we tended to keep a constant allocation of c. 5% to Gold and Silver.

Our strategy going forward?

We will continue trading around precious metals positions while also looking for new investment opportunities in Commodities; especially in energy (oil and natural gas) which could see upside potential over the coming months.

Currencies

What have we done?

We kept FX allocations broadly unchanged in Q2 2020 as our thesis of a weaker USD played out.

Our strategy going forward?

Our medium-term view of a weaker USD warrants little change in portfolios currently. We will look for singular FX plays potentially in Emerging Markets or commodity-related currencies.

MAM Actions (cont.)

Hedge Funds

What have we done?

Where adequate, we added exposure to the newly launched Helikon Long/Short Equity Fund whose Management team has a great track record in alpha generation. They are off to a good start. We also added exposure to the Tyrus Secondary PE Fund V & Mantra III for increased exposure in Private Equity.

MAM is managing two internal Hedge Funds: Io Macro Fund Limited and Macro Hedge Fund. Both are displaying strong positive performance YTD. We continue to believe that adding exposure to these two funds where possible is an added value proposition. In the Macro Hedge Fund, we have been extremely active in trading across equity, credit, currency, and commodity markets.

Our strategy going forward?

We will continue to look for opportunities to invest in funds or hedge funds that have a track record of delivering alpha. We will increase our focus on Emerging Market credit and Commodities; two areas we believe offer attractive opportunities longer-term.

Events

Covid-19 Update

Over the past few weeks, countries have been progressively reopening their economies as the number of new cases continued to drop. Yet, the virus is not gone and a second wave of infections is not only a clear possibility but almost a near certainty now with Melbourne already entering a six weeks lockdown in Australia. In the United States, the trend and scope of the virus continues to be worse than in other western countries. The reproduction rate there remains at 1.1 (vs. 1.05 two weeks ago), while the epidemic doubling time is still decreasing This is an indication the spread is accelerating **(Chart 3)**. As noted in our latest MAM Insights research, a second wave of infections in most western countries is inevitable in autumn 2020. We can argue its severity may be lesser than the first one considering the populations have been briefed and accustomed to sanitary measures, remote working is now widespread, and masks are easily accessible. However, most governments have much to lose should another wave infections become uncontrollable. Restricted travel, and reduced consumer spending should continue to put a lid on the global economic recovery. Moreover, there is a major event in Q4 2020 which is at risk due to Covid-19: US election.

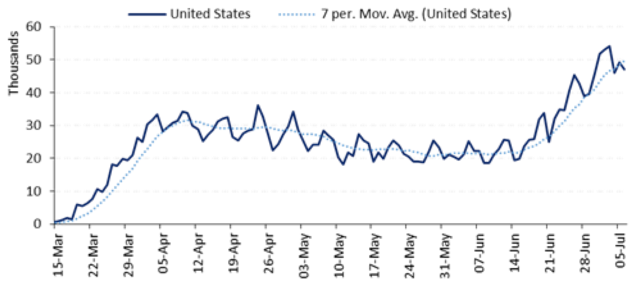
US Presidential Election

As we stand a little under five months away from election night **(Chart 4)**, support for the incumbent president is fading in areas where the virus is spreading. Former vice-president Joe Biden is the presumptive Democratic nominee to challenge the outgoing president and is running on one of the most progressive platforms since L.B. Johnson with meaningful tax increases and expansion of government involvement in healthcare. In contrast, the Republican candidate's agenda revolves around additional tax cuts and reinforced immigration restrictions. Each candidate stresses the need for a firmer stance and approach to the US-Sino relationship.

Historically, equities tread waters ahead of close presidential elections although Joe Bien is currently polling ahead of Trump since early March when the virus began to spread in the US **(Chart 5)**. Fiscal policy (deficit spending, inflationary impulse, tax change) and US-China escalation skew risks to the downside. The weight of uncertainty on risk appetite and corporate investments could be a major source of headwinds. Tax and fiscal stimulus are likely to be what matters most to fundamentals. Government policy expectations should be a key driver of US rates with the election of a united government more likely to move markets than a divided one.

Trump is looking for re-election with significant headwind due to elevated unemployment. Yet a lot can change in five months. While the spread of the virus could interfere with the normal process of the election and force voters to submit mail-in ballots, it is nearly impossible for the election to be delayed as per the US constitution's 20th Amendment. Many voting systems across the states are still shaky and unprepared for a massive surge in mail-in ballot. Cyber hacking, disinformation, and the pandemic are new threats. As a result, concerns are mounting over the integrity of the US election with a growing number of experts anticipating a remake of 2000 in 2020. America is at the door of an election that could make the shenanigans of Bush vs. Gore look like child's play. Twenty years ago, in the 5 weeks of contestation, equity markets declined by nearly -7% and continued to drop for the remainder of the year. President Trump has already set the tone for what is going to be a dispute election on twitter *(please see tweet on the right)*.

Chart 3. US Daily Infection Rate



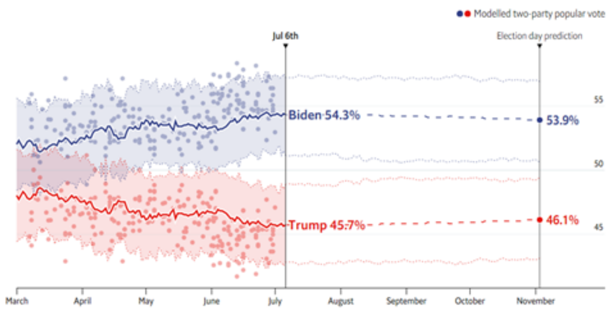
Source. MAM Research, Bloomberg

Chart 4. Us Presidential Election Polls Evolution

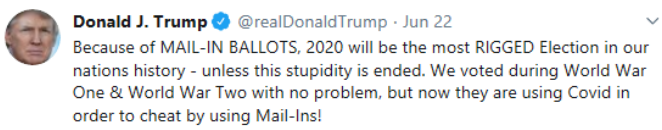
17-Aug	Democratic National Convention
24-Aug	Republican National Convention
29-Sep	First Presidential Debate
07-Oct	The Only Vice President Debate
15-Oct	Second Presidential Debate
22-Oct	Third Presidential Debate
03-Nov	Election Day
14-Dec	The electoral college meet to formally vote

Source. MAM Research

Chart 5. Us Presidential Election Polls Evolution



Source. The Economist



Economics & Rates

Conclusion. Inflation Return. We continue to believe a "swoosh" shaped economic recovery is the most likely path ahead and estimate advanced economies will be able to revert back to pre-pandemic long-term output growth levels by end-2022 (please see "MAM Flash Outlook" for further details) . The risk of higher inflation is growing. While the financial community seems attentive to this thesis, we believe long-term inflation risk is under-priced. Ready to take advantage of an inflationary environment unseen in decades, we remain on the lookout for yield curve steepening trades and ready to gain exposure to TIPS. As the global search for yield intensifies, we continue to like EM local currency bonds where there is still monetary policy flexibility.

Although the thesis can take some time to materialize, when we combine supply chain disruptions and higher demand from a gradual economic recovery through 2022, we see true risk for higher inflation within the next 1-2 years.

Today, long-term inflation is under-priced. CPI swap markets currently expects inflation to remain subdued for decades to come **(Chart 6)**. While it is not an imminent risk, we need to be ready to invest in an inflationary environment, something unseen in over a decade. Although central banks do not want inflation to spiral out of control, they would like to see it rise from current levels. In fact, heavily indebted governments would also favour higher inflation to higher interest rates. The former would erode the real value of debt while the latter would either require tax dollars to be diverted from social programs to bondholders, fiscal austerity, or tax increases.

The structural forces that have been putting down pressures on inflation over the past few decades should also abate, if not reverse course. When looking at demographics, from the mid-1970s onward the ratio of workers-to-consumers ("support ratio") started to steadily increase **(Chart 7)**. An increase in the number of workers to the number of consumers is equivalent to an increase in the amount of production to consumption. As a result, a rising support ratio is deflationary. With the baby boomers' generation leaving the labour force, consumption should naturally increases while global savings would actually dissipate, putting upward pressure on prices. We may be entering an economic phase similar to the 1970's which experienced high and sustained levels of inflation.

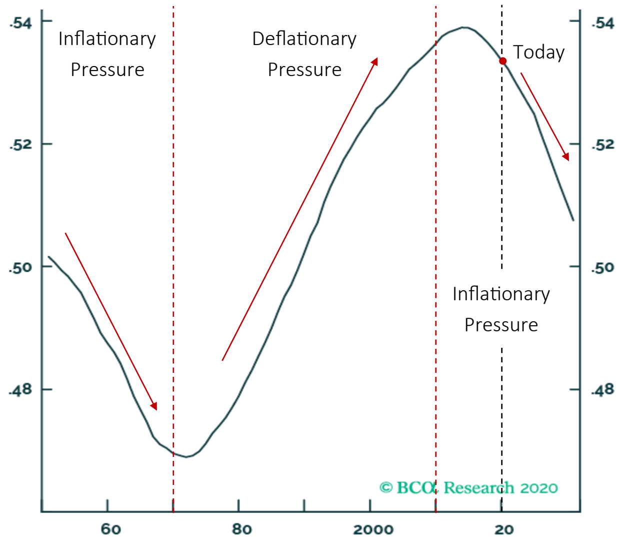
The US yield curve **(Chart 8)** has started to steepen. Yet, the curve (current level: 50bps) remains very far from the highs seen in 2016 (125bps) or 2010 (280bps). As a result, we like yield curve steepening trades notably when the curve flattens temporarily on bad economic indicators or US election concerns. Exposure to 5-Year duration Treasury Inflation Protected Securities (TIPS) is a viable alternative to express the inflation thesis.

Elsewhere in rates we continue to like Emerging Markets local currency bonds. Emerging Market economies are better equipped to weather the impact of the Covid-19 crisis. Local Central Banks have room to cut interest rates further. Local Emerging Market currencies are cheap relative to the US dollar. The global search for yield should continue to push fund flows into this asset class over time.

Chart 6. Long-Term Inflation Expectations, CPI Swap Rates

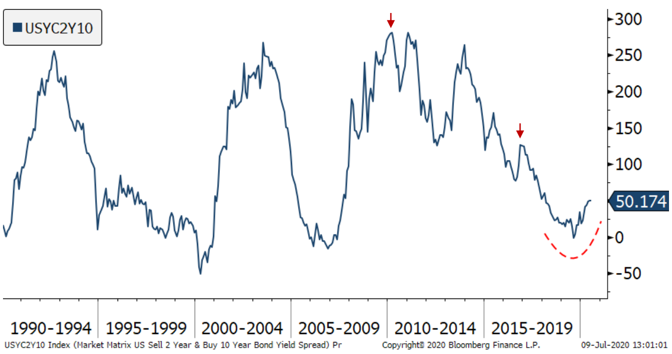
Source. MAM Research, Bloomberg

Chart 7. World Support Ratio



Source. MAM Research, BCA Research

Chart 8. US 10-2 Yield Curve (Weekly)



Source. MAM Research, Bloomberg

Credit

Conclusion. Bearish DM. We have been relatively negative on corporate credit for some time now and remain so to-date. We believe corporate bonds, especially in the US, offer unattractive risk-reward to investors after the recent swift spread contraction. Although central banks policy support is here, we remain cautious on the liquidity levels in the market. We are also progressively observing a degradation in the balance sheet quality of companies. Historically, when interest coverage ratios across the asset class reached those low levels, spreads widened progressively in the following years. Within DM, and despite negative outlook, we prefer European HY bonds falling under the ECB purchasing program. There, we believe central bank-provided liquidity and "backing" bring sufficient support and allow for more attractive risk-rewards. Generally, we continue to look for short-duration bonds (i.e. 2022-2023). Should our inflation thesis develop, we will then look to invest in floating rate notes. Elsewhere, we continue to like Emerging Markets local currency bonds thanks to supportive central bank policies and relatively cheap currencies.

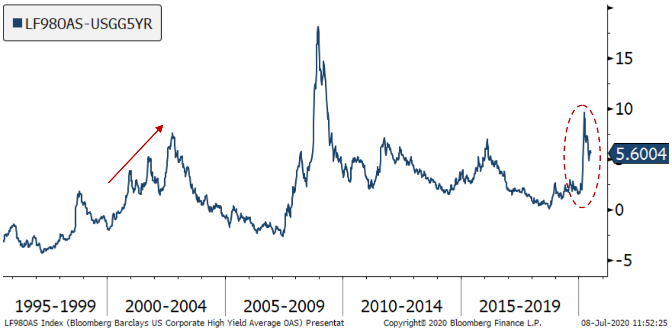
Over the next couple years, once unemployment reverts back closer to pre-pandemic levels and inflation takes off, central banks should be slow to raise rates because they target higher inflation levels and governments will pressure them to keep rates low in order to avoid having to redirect tax revenue. As expressed earlier, with markets under-pricing the chances of inflation, we believe yields have seen their lows for this cycle and the yield curve is likely to steepen. The observable deterioration in balance sheet quality (i.e. median interest coverage ratio in US high yield corporates falling to the lows of the early 2000s **(Chart 10)**) should force some spreads widening. When it reached those lows back in 2001, spreads actually went on to widen significantly more in the following years **(Chart 9)**. As a result, we continue to dislike the risk reward at current spread levels.

While we remain cautious when investing in corporate credit, we do find some seldom opportunities within the European high yield bond market **(Chart 11)**. There, we favour bonds that fall under the ECB's purchase program. We believe bonds falling under said program benefit from the additional liquidity and "backing" of the central bank thus offering better risk-reward to investors.

Should our aforementioned inflation thesis develop, we will look for opportunities in floating rates notes. Generally, we also look for short-duration bonds (i.e. 2022-2023 maturity) as those are less likely to be the first impacted by higher inflation expectation on the back-end of the crisis as a result of the wave of stimulus seen globally.

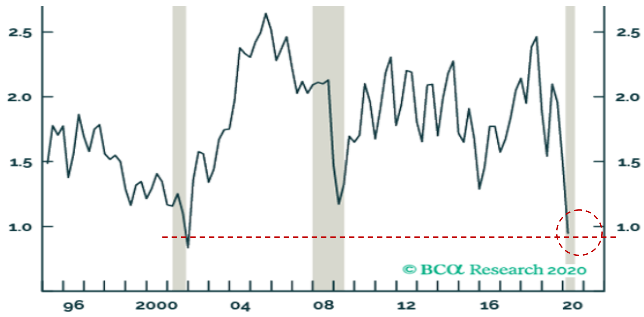
Emerging Markets (EM) corporate credit continues to offer attractive yields to investors. EM currencies continue to look cheap from a valuation stand point. Our long-term view on rising global inflation and our positive outlook for commodity prices are both supportive of higher economic growth in emerging market countries. Additionally, central banks in those regions still have sufficient room to cut interest rates to mitigate the impact of the pandemic and pair some of the economic losses that could be hindered by a second wave. As a result, we continue to favour local currency EM bonds **(Chart 12)** over hard currency ones.

Chart 9. US High Yield Credit Spread Index (Weekly)



Source. MAM Research, Bloomberg

Chart 10. Median Interest Coverage Ratio (US HY) (Weekly)



Source. BCA Research

Chart 11. EU High Yield Credit Spread Index (Weekly)

Source. MAM Research, Bloomberg

Chart 12. EM Local Currency Bonds USD Unhedged (Weekly)

Source. MAM Research, Bloomberg

Currencies

Conclusion. Structurally Bearish USD. The US dollar index is up 57bps YTD, but down 6% from its peak in March 2020. We continue to be structurally bearish the greenback currency. Many, if not all, roads should lead to a lower dollar in the next economic cycle. Economic recovery are usually a sign of capital flying out of the USD into relatively more pro-cyclical currencies such as the Euro and Emerging Market currencies. Additionally, while a second wave of outbreaks should provide short-term support, a coinciding double dip recession would imply further fiscal and monetary stimulus at a time when state finances are already on the edge. Hence, longer-term the structural headwinds to the dollar should continually exert pressures. Within the G10 currencies, we like the Euro and the Japanese Yen. The former for its pro-cyclical attributes and the latter for its inflation “protection” and “safe-haven” nature. With valuations looking cheap, a weaker USD, and a rising commodity prices thesis, EM currencies look compelling. However, timing remains complex.

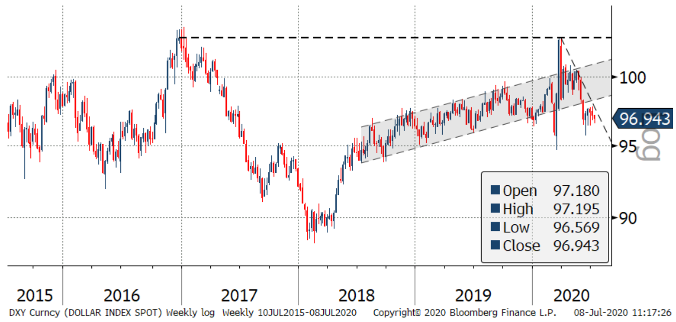
The dollar remains a counter cyclical currency that tends to move in the opposite direction of the global business cycle. After peaking in March, the greenback dropped 6% **(Chart 13)**. Unlike last year, it is no longer benefiting from higher interest rates. US real rates have now fallen below those of many partner countries in part because US inflation expectations are higher than in other regions. The loss of relative carry attractiveness and higher growth expectations in partner countries will continue to weigh on the currency. A double dip recession would imply further US stimulus while finances are already borderline and should therefore exert additional pressure on the currency. We could be at the dawn of a dollar bear market unseen since the early years of the new millennium but timing remains complex.

While the dollar prevails as a counter cyclical currency, it has also acted as a risk-off/”safe-haven” asset in recent months to the detriment of the Euro **(Chart 14)**. However, with risk appetite resurging and investors becoming increasingly more bullish on European assets, we should begin to see a continued appreciation of the Euro against the dollar. Technically, the Euro broke out of its 3-Year wedge formation. Flow and positioning present early signs of this. On top of being long the currency, investors have actually been adding on to their positions. This is a good sign.

The Japanese Yen continued to trade within its range in the absence of significant market turbulence since late March **(Chart 15)**. We continue to like the currency and its ability to provide a hedge in times of market stress with the threat of a second wave of outbreaks still looming and already showing up in some regions (i.e. Australia). Additionally, the currency continues to be relatively cheap, trading slightly more than 1 standard deviation cheap on a Real Effective Exchange Rate (REER) basis.

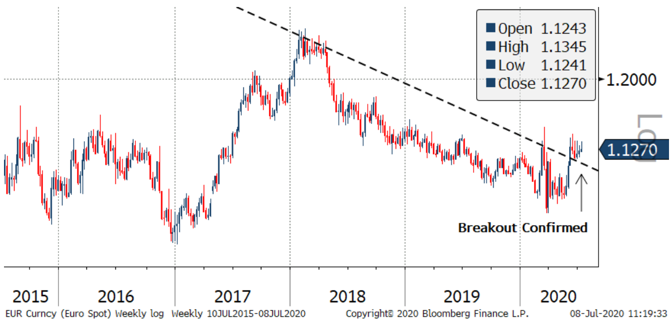
When the fear of a second wave abates, the structural headwinds threatening the dollar should prove supportive to commodities. The early weakening of the dollar has already been positively received by EM currencies since the end of March with the EM Currency Index up 5.4% since then **(Chart 16)**. Considering emerging markets economies rely extensively on exports and their currencies tend to be positively correlated to commodity prices, we begin to find some potential opportunities in the emerging market currency complex. Valuations are starting to look compelling with notably the Mexican peso, Brazilian Real, and South African Rand trading over 2 standard deviations cheap looking back 10 years.

Chart 13. US Dollar Index (Weekly)



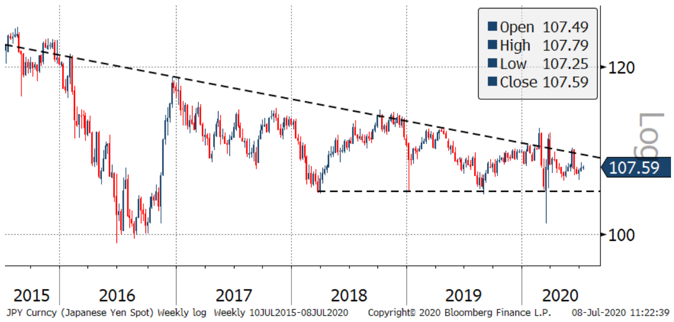
Source. MAM Research, Bloomberg

Chart 14. EUR vs. USD Currency (Weekly)



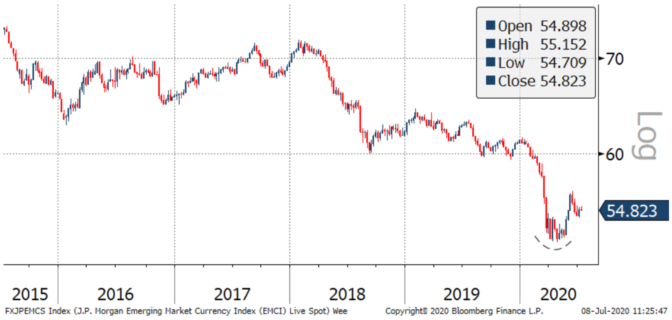
Source. MAM Research, Bloomberg

Chart 15. JPY vs. USD Currency (Weekly)



Source. MAM Research, Bloomberg

Chart 16. Emerging Markets Currency Index (Weekly)



Source. MAM Research, Bloomberg

Equities

Conclusion. Cautious. The MSCI World has rallied +42% since the March lows, a historic move. The valuation starting point in Q3 2020 is very different to Q2 2020. The MSCI World Index trades on a 2021 P/E ratio of 19.5x. This is over 2-standard deviations expensive. Earning expectations have barely moved up from the lows in March 2020. The Q2 earnings season starting in a few weeks may dampen investors' optimism on a fundamental recovery in H2 2020. Equity markets tend to fall c. 5% 2-3 months ahead of a US election. We expect equity markets to trade mostly in a range with the S&P 500 Index between 3200 and 2800. As such, we remain cautious at current levels and would use market pull-backs to place tactical trades.

Equity market valuations are getting extreme in some areas such as in the US. The S&P 500 Index trades on a 2021x P/E ratio of 19.6x. This is the highest level since 2001. The lion share of this equity market re-rating is due to the impact of lower discount rates and Central Banks keeping interest rates low for a prolonged period of time. While the discount rate is a crucial factor, shorter-term earnings expectations can also have an impact on equity markets. Earnings expectations 12-months forward have not changed materially over the last few weeks. The earnings season starting at the end of July can be a catalyst for weaker markets as corporates provide guidance on what seems like an unclear trajectory in H2 2020.

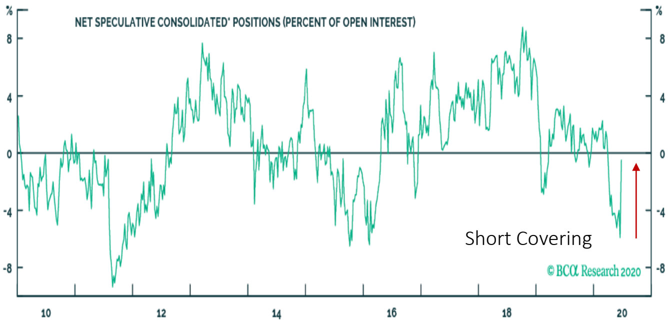
In addition to the upcoming Q2 earnings season, market seasonality can have an impact. We analysed US equity markets behaviour before US elections in the last 20 years. Historically, equity markets tend to sell-off around -5% 2-3 months ahead of elections **(Chart 18)** as investors reduce their exposure into what is usually a high volatility event. Considering our views on elections (please see "events" section), we expect a similar trend of pre-event profit-taking.

Despite the bearish arguments put forward above, we have to acknowledge that we are in the midst of the most hated bull market rally in recent times. Despite the +42% rally from the March lows, investor participation remains light. The BAML Fund Manager Survey shows that mutual funds are still overweight cash. Hedge Funds have covered their short S&P futures positions but have yet to show any meaningful Long positioning. Such "light" market positioning **(Chart 17)**, combined with a lack of investing alternatives, suggests that market sell-offs of 5-10% are likely to find a floor. The "buy the dip" mentality is likely to prevail for the time being. We intend to use such market dips to place tactical trades.

Within equity markets we favour non-US exposure, i.e. European and Emerging Market equities, for their relative valuation cheapness and our preference for their respective currencies. Europe's swifter management of the Covid-19 crisis should lead to a quicker recovery of corporate earnings. We expect strong volatility in the Growth/Value factors **(Chart 19)** over the coming weeks as the tug of war between deflation (pro-Growth) and inflation (pro-Value) intensifies. While we would keep some exposure to the US technology sector, we would also balance this exposure with energy, industrials, and financial stocks.

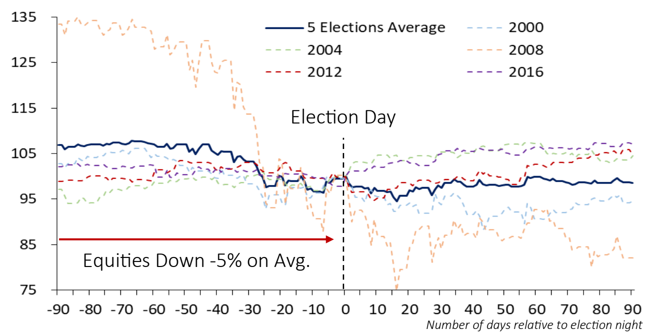
Overall, at current market levels, our recommendation is to keep a low exposure to equities (c. 25%) in order to take advantage of potential market dislocations in Q3 and Q4 2020.

Chart 17. Equity "Light" Market Positioning



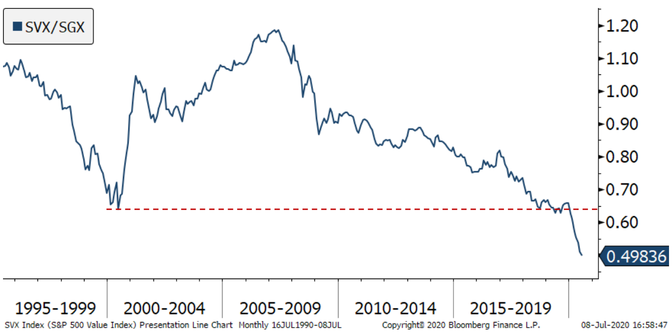
Source. BCA Research

Chart 18. S&P 500 Index Seasonality Ahead of Elections



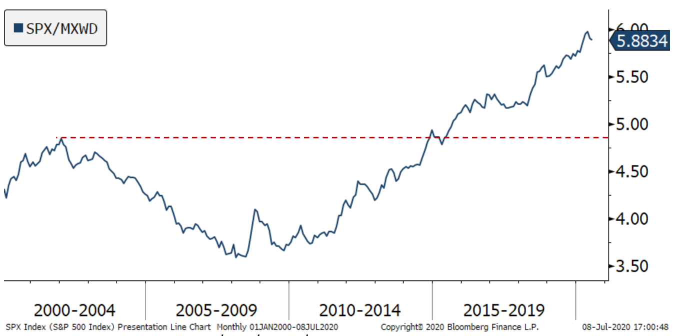
Source. MAM Research, Bloomberg

Chart 19. S&P Value vs. Growth (Monthly)



Source. MAM Research, Bloomberg

Chart 20. S&P 500 Index vs. MSCI World Index



Source. MAM Research, Bloomberg

Commodities

Conclusion. Bullish. Commodities remain one of our preferred asset class. Valuations continue to trade at record lows. The unprecedented wave of global stimulus, the return of economic activity in Asia and Europe, and a weaker US dollar outlook are all supportive to the commodity complex. We remain long gold with a price target of $1,950/oz. (+8%), but continue to favour silver with a target of $30 (+67%) given the ongoing mean reversion in the silver-to-gold ratio and supportive industrial application (i.e. photovoltaic panels). With prices near or recently bouncing off of decade lows, we continue to believe in some tactical long trades on energy commodities such as natural gas. With the Chinese economy reopening, manufacturing activity picking up, and demand recovering across Europe, copper has retraced all of its losses **(Chart 24)** which should be seen as a positive for other commodities. In fact, we continue to carefully monitor agricultural commodities for targeted trading opportunities. Early signs of China demand for US Agricultural goods (excess of trade deal quotas) could indicate some market imbalances.

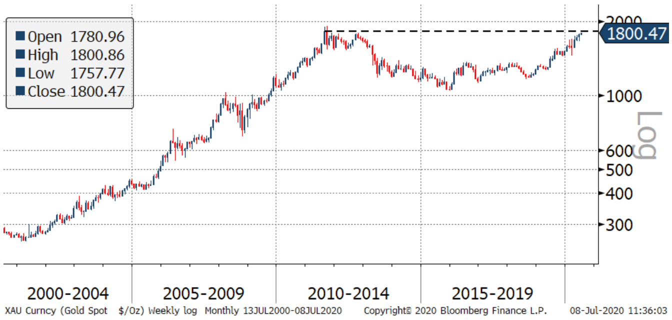
The amount of fiscal and monetary stimulus introduced to support the global economy in the aftermath of the pandemic should, as mentioned earlier in our note, provide support for higher inflation and a weaker dollar. The intrinsic nature of the yellow precious metal makes it a good inflation hedge in an inflationary environment. Additionally, it should prove resilient once more in the wake of a second wave of new cases later in the fall. As such, we continue to favour the commodity and actually decided to raise our price target to $1,950 from $1,800. We believe despite breaking above the $1,800 mark **(Chart 21)**, prices still have a long way to go before they reach a ceiling. We continue to recommend adding it to portfolio should spot prices fall below $1,700-$1,750 on momentary sell-offs (i.e. margin call, liquidity driven).

Although the two precious metals share some fundamental characteristics, silver has both a wider and deeper range of industrial applications. It is those fundamental divergences that partially explain why the commodity has underperformed its precious metal counterpart in the first half of the year **(Chart 22)**. However, the push for more environmentally friendly projects and notably greener sources of energy should prove more supportive to silver than gold. The technology currently used in photovoltaic panels require the use of silver in the cells. While base need per cell is declining, the growing demand for residential and utility photovoltaic panels will be one of the driver for higher prices. Those combined characteristics are why we continue to favour silver over gold, but also why we believe the precious metals bull market is just starting.

Admittedly, we may have called the price recovery of natural gas prices a little bit early this year. Especially in light of the pandemic which impaired seasonal demand and led to higher inventories. However, rather similarly to what is currently expected to happen in the oil market, a gradual pick up in demand along with continued supply shutdowns among US producers with rising Covid-19 cases in the country and a higher degree of production discipline from market participants should prove supportive. We currently expect natural gas price to recover to low $3s **(Chart 23)** in a first stage before rising higher later in the year, ahead of winter 2021.

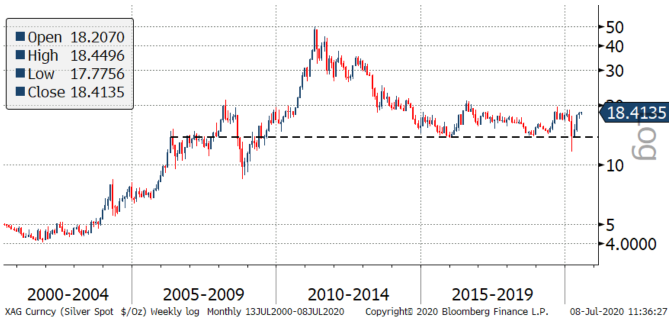
The stellar price recovery of copper **(Chart 24)** up 39% since March 2020 lows is a positive sign the global economy has begun to recover. This happens to be positive for our bullish commodity thesis.

Chart 21. Gold Spot Prices (Monthly)



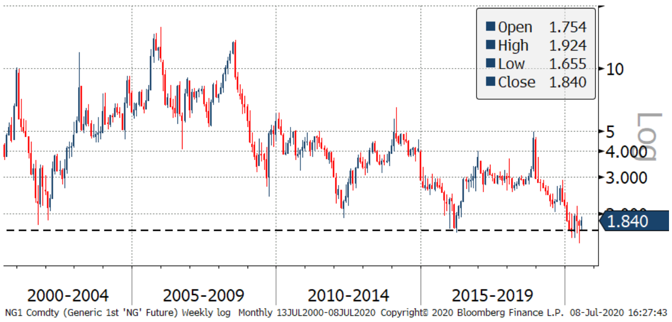
Source. MAM Research, Bloomberg

Chart 22. Silver Spot Prices (Monthly)



Source. MAM Research, Bloomberg

Chart 23. Natural Gas Front Month Futures Prices (Monthly)



Source. MAM Research, Bloomberg

Chart 24. Copper Front Month Futures Prices (Weekly)

Source. MAM Research, Bloomberg

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