Commentary

FUNDAMENTAL OPTIMISM FOR THE YEAR AHEAD

In our New Year's greeting we wrote that farmer's almanacs used to say that April is the cruellest month, and so it could be this year on a wider perspective. It is the period when cupboards are empty because provisions from the prior year's harvest have run out, but the new season's green shoots have not yet appeared.

With the inability of many countries, including the US and the UK, to get the Covid-19 pandemic under control and the worry about more contagious variants abounding, it certainly seems that way today.

As we look forward to the New Year after the turmoil of last year, however, we believe that there is cause for optimism. We are in the process of overcoming many of the challenges that have confronted us over the past several years, including the pandemic.

In politics, the inauguration of President Biden despite the events of the past several weeks is testimony to the resilience of the US political system and should lead to a period of more constructive and predictable politics. The US has prospered under moderate and divided government and is likely to do so now, not least because it has never paid to bet against the US economy or to fight the Fed.

In Europe, the protracted Brexit process has come to its conclusion. The disruption to trade is significant, and the issues will be time consuming and costly to resolve. The political repercussions in the UK will carry on as well but are primarily a domestic issue. We continue to believe that market access for the UK will require a degree of alignment in order not to have an unfair advantage. We are prepared from a business perspective ourselves in any case.

Covid-19 has added to those challenge in an immeasurable way and its impact will be felt for years. Many have lost family and friends to the illness, or have had it themselves, and many more will be affected by the physical and psychological impacts of disrupted education, lost employment, social isolation, and concerns about the future.

It is clear, however, that the global effort to develop vaccines has succeeded and that the major vaccines work. These include the mRNA vaccines developed by BioNTech and Moderna, the Oxford/Astra vaccine despite its issues, the more traditional ones that are in development by Sanofi, Johnson & Johnson and others, but also the Sputnik V vaccine developed in Russia and rolled out in China and elsewhere. The rollout will be difficult, and it will take months to vaccinate the vulnerable, healthcare workers and over time the general population. It may be that vaccines have to be modified and taken annually. However, the effort will succeed and even though the situation looks dire as we start the year, it could change quickly if the numbers of those seriously ill and hospitalized drop, healthcare workers are no longer at risk and healthcare systems regain their capacity. We should also recall that Covid-19 is a somewhat seasonal disease so it should recede in the coming months as the weather improves.

The pandemic has hit the US and European economies where they are most exposed: services. In many countries restaurants, hotels, retail, personal services, healthcare, and other professional services are all heavily impacted or shut down. That is bad news because it is where the employment is and why governments have had to provide income support on an

J. Stern & Co
4 Carlton Gardens
London SW1Y 5AA
United Kingdom

Tel: +44 20 3478 1800
Fax: +44 20 3478 1799
info@jsternco.com
www.jsternco.com

unprecedented scale. It is however very good news for when the economies open up and people are able to provide and consume services again. The government payments to those who need it are an entirely Keynesian stimulus that is spent not saved, and pent-up demand will lead to significant growth.

Meanwhile it is clear that governments and central banks will do whatever it takes to support their economies through this period of challenge and distress. The current low, and in many cases negative, interest rate environment is likely to prevail for a prolonged period of time, not least because the high levels of unemployment mean that the wage inflation we saw just before the pandemic will be more limited, and will force investors to adjust their expectations of risk and reward from their investments.

During the past year our World Stars portfolio was resilient, increasing 21.4% in US dollar terms net of fees. Our approach to investing in quality and value for the long-term has led us to invest in companies that have the scale, resources, and balance sheets to prevail during the uncertainty.

As we said at the beginning of the year, we are optimistic because the fundamentals of our companies are strong. Those in technology and digital businesses that have been resilient will continue to do well. Others in consumer products, healthcare and industrials that have been impacted will rebound and are coiled for performance. Valuations for our companies are attractive even if markets are at the higher end of their ranges, and some of the biggest companies in the world that we do not own are clearly overvalued. We see no point in timing markets, but we think the turnaround during the year will come, possibly sooner than expected, in terms of disease numbers declining and economies opening-up, but almost certainly in terms of markets anticipating the reopening and repricing stocks. There will be setbacks, but the underlying fundamentals mean that any volatility in markets should be an opportunity for long-term investors.

World Stars Global Equities

Our World Stars Global Equities strategy ended the year up +21.4%, buoyed by a strong performance in December up +3.4%, both in US dollar terms. Our stocks outperformed global markets and proved the resilience of our investment approach during a challenging year.

Performance during the month was led by video game developer *Activision Blizzard*. The company has been a key beneficiary of the Covid-19 crisis as consumers sought alternative forms of entertainment whilst being confined to their homes. Activision's flagship *Call of Duty* franchise surpassed USD 3 billion in net bookings during the year. The company has a promising pipeline of new game introductions going forward and remains well placed to continue benefiting from its expanded user base and deeper consumer engagement.

Also performing strongly during the month were payment processors *Mastercard* and *Visa* as online retailing in the US posted a record 47% year-on-year growth rate during December in the run up to the critical holiday season. The strong growth of online retailing provided further evidence of the switch to online retailing fuelled by the pandemic, with brick-and-mortar sites remaining closed and consumers increasingly comfortable meeting their purchasing needs online.

Finally, luxury goods company *LVMH* continued to bounce back as shareholders of Tiffany's agreed to the USD $15.8 billion takeover of the company, solidifying LVMH's position as the undisputed leader in the industry.

Looking back at 2020 we think it is particularly noteworthy to see how broad-based our performance was, reflecting the resilience of our holdings across sectors amidst the unprecedented social and economic crisis that Covid-19 unleashed.

Our holdings within the digital and technology space emerged as key beneficiaries of the switch to online, whether through purchasing, entertainment and socialising activity by consumers, or advertising and selling activity by businesses. Within healthcare, several of our holdings emerged as key solutions providers in the fight against Covid-19, providing critical testing kits to monitor the virus' spread, but also equipment and solutions that powered the vaccine development, which will ultimately bring the virus under control.

Within industrials, companies quickly pivoted their businesses to take advantage of new customer needs, whether that was sensors for ventilators and patient monitoring equipment, connectors for communication systems to meet the surge in bandwidth requirements, warehouse automation equipment to meet the increase in online shipments, or PPE equipment to shield healthcare workers. At the same time, construction related companies benefited from the expectation of robust construction activity going forward as governments announced infrastructure plans to help reignite battered economies.

Finally, within the broader consumer space our companies benefitted from stable demand for consumer products in food, flavour & fragrance as well as cosmetics, skincare and haircare, all of which were resilient as customers shifted their consumption due to the social distancing measures put in place.

On the weaker side during the year were some of the businesses affected by the Covid-19 related disruption. That included most notably aviation, where the halt in commercial travel weighed on the company's results, despite the resilience of the defence business. Similarly, our holdings in spirits companies came under pressure as restaurants and pubs remained shut, whilst demand for lenses and sunglasses was affected by the closure of retailing sites globally. Another affected area was medical devices as hospitals globally struggled to deal with the surge in Covid-19 patients and elective procedures kept being cancelled, affecting some of our holdings.

Our holdings were shielded by the strength of their balance sheets and cash flows as well as the swift cost cutting measures that managements instigated. Many were able to use their financial strength to reinforce their competitive positions and are well placed as vaccinations are rolled out globally, normality returns and demand rebounds. We see these holdings as best placed to lead performance in 2021 as their revenues and earnings recover sharply.

Multi-Asset Income

2020 finished on a strong note, with the Multi-Asset Income strategy up +2.5% in US dollar terms for the month of December, taking the year-to-date performance to +9.9%. This represents a +7.4% annualised net return since inception. In line with the previous few months, all asset classes performed strongly. Equities led the charge, up +3.6% for the month and +26% for the whole year. The fixed income and non-correlated funds were respectively up +2.2% but still down -3.4% for the year and +1.1% (up +1.5% for 2020, although the final figure is likely to be higher due to the lag effect in the reporting of some of the funds).

The portfolio generated a continuous cash yield in a year where cash generation remained a challenge because of the very low interest rate environment.

Risk assets were supported by the positive news flow on the vaccination front and the prospects of a substantial economic stimulus package being agreed by the US Congress.

Despite the significant volatility last year, we stuck to what we knew best and used the opportunity offered by the volatility to increase our exposure to the companies we were most comfortable with, as a result improving the underlying quality of the overall portfolio.

Our credit portfolio suffered from the liquidity movements on the downside, in common with other asset classes, but did not benefit as much as equities on the upside. However, most fixed income names saw a strong recovery, especially energy issuers like *YPF*, *Pemex* and *Tullow* as oil prices had strong momentum towards the end of the month. Despite this improvement, the fixed income portion of the portfolio still looks very attractive going into this year, with a current yield of 7.2% and a yield to maturity of 9.5%, and a duration of below two years.

The income portfolio remains firmly focused on generating a solid cash yield with low relative volatility. Following a challenging year, we look at this New Year in a positive light, seeing through the current difficult environment as the fundamental prospects for most of our holdings appear extremely positive, with strong secular growth for some and exciting recovery potential for the others.

Emerging Markets Bonds

2020 was a year fraught with unanticipated challenges. The Covid-19 pandemic raised significant questions about the potential collapse of healthcare systems and the inability of economies to deal with the crisis. Market concerns quickly turned to whether we would experience a full-blown credit crisis, with the ensuing panic resulting in a brutal sell-off across markets and asset classes. The speed at which markets sold off was record breaking.

Guided by the experience of the global financial crisis, governments were quick to react, however, and highly accommodative monetary policy from developed economies pulled markets back from the brink almost as quickly, with the recovery eventually feeding into demand for emerging market bonds. By the end of 2020, record low rates, improved investor sentiment and the search for yield pushed spreads of emerging market bonds back towards pre-Covid levels.

Our emerging market bond strategy was not immune to the volatility we experienced early on in 2020, with the portfolio declining -19.2% in March. Despite this, it is encouraging to note that it ended the year down just -1.1%, almost fully recovering these losses. We also capitalised on the opportunity created by the volatility to improve its overall quality by buying a number of high-quality corporates that had been on our wish list, but were previously too expensive and did not offer enough yield.

The portfolio ended the year on a high note with another strong month in December, returning 1.6%. Once again, performance was driven by the cyclical, higher-beta names with

YPF and Pemex returning 10.1% and 9.0% respectively as the oil price continued its recovery on the prospect of increased activity and travel in 2021.

We are constructive for the outlook for 2021 and see it as a year of recovery as vaccines are rolled out over the coming quarters. New vaccine approvals will accelerate this positive trajectory. We expect global interest rates to stay lower for longer and the accommodative polices of central banks to continue along with further fiscal stimulus.

This environment, combined with a weaker US dollar and higher commodity prices, creates a positive backdrop for emerging markets, and with our portfolio currently yielding 6.6%, we are confident in its ability to generate solid income and total return in the year ahead.

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