2021 Key Trends

1 From virus to vaccine
Click here

2 From lockdowns to living life again
Click here

3 From recession to mini-boom
Click here

4 From rally to rotation
Click here

5 From monetary to fiscal
Click here

Bank of Ireland

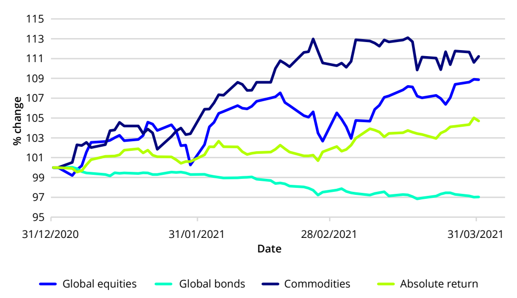
A history filled quarter
Q1 2021

Even by recent standards it has been an event-filled quarter. The world has shifted dramatically in the past three months of Q1, with a lot of history crammed into a short number of weeks; Brexit, the inauguration of President Biden, the arrival of vaccines, and the scale of fiscal policy now being enabled in the US are all now realities.

While the world continues to await the all clear from Covid-19, there is a growing consensus that the recovery is likely to prove stronger than anticipated only a matter of a few months ago.

Q1 2021 performance
Equities have delivered bumper returns this quarter (see figure 1 below) with +9% yet it was commodities and crypto-currency that were to the fore as the best performing asset classes.

Figure 1: Q1 2021 returns by major asset classes to 31/03/2021



Q1 2021 performances (to 31/03/2021)
- Global equities +9.0%
- Global bonds -3.0%
- Commodities +11.2%
- Absolute return +4.7%

Source: Bloomberg Finance LP 06/04/2021

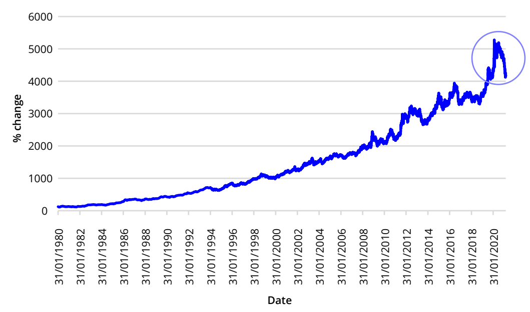
Equities record setting year
The anniversary of lockdown is a sobering moment. Yet it's also hard to believe that a year has passed since the Covid-19 pandemic inspired record lows in global stock markets. Since this time last year equity market performance has been exceptional. With growth of 63.2% in world equities (in euro terms) since the low[1], investors have seen a 12 month period that ranks as the strongest of the past half century. This is even ahead of the 12 month returns from the market lows of the Great Financial Crisis (9th March 2008).
Source: Bloomberg, 01 April 2021.

Bond markets take a beating as the focus shifts to inflation
Over Q1, we have seen an increase in economic growth forecasts (see figure 4 for more detail) and further news of fiscal stimuli, see overleaf for more, especially in the US, resulting in rising inflation expectations. As a consequence, global bond markets experienced dramatic falls in Q1 against the fear of rising inflation as it is now seen as the biggest risk in financial markets, ahead even of Covid-19[2].

In figure 2 we can see the experience that investors in long dated US government bonds have had. Losses of approximately 19% have been experienced by investors since last August[3], making it one of worst periods for holding these type of bonds. Losses across shorter-dated bonds and other markets have been less dramatic but nonetheless bond investors have experienced significantly negative performance in recent decades. **Simply put, low-risk assets had become very expensive and the prospects for the coming decade are for low returns as a consequence.**

Kevin Quinn,
Chief Investment Strategist, Investment Markets

Figure 2: US long bond index since 1980



Source: Bloomberg Finance LP 06/04/2021

[1] Measured by the MSCI World index in euros from 23 March 2020 to 31 March 2021. Source: Bloomberg Finance LP
[2] Measured by S&P500 Total return index from 23 March 2020 to 23 March 2021. Source: Bloomberg Finance LP
[3] Measured by US long bond index from 3/8/2020 to 31/3/2021. Source: Bloomberg Finance LP

WARNING: Past performance is not a reliable guide to future performance.

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5 Trends for 2021

At the start of 2021, we highlighted five key trends which we believe will impact investors over the year. Against the current focus that the market has on recovery (positive) and the potential for inflation (rising), below we analyse the current status of these trends:

1 From virus to vaccine

At time of writing, 132 million people have suffered from Covid-19 around the world and 2.87 million have died[4]. As at the end of March 2021, 5 months after the 5th November 2020 vaccine announcements, nearly two-thirds of a billion vaccine doses have been administered around the world, at a rate of 12.2 million a day according to latest data[5]. Vaccine roll-out in the developed world has dramatically outpaced the developing world. This has been led in particular by large economies, namely, the US and UK who have, at this stage, reached 49 and 54 doses per 100 people respectively[6]. EU numbers, including Ireland, remain someway behind this at typically 17 -18 doses per 100 people[6]. However with further acceleration anticipated it is to be expected that there is very clear light at the end of the tunnel.

For investors, the remaining uncertainty about the timelines has become a lesser concern even if there remains a long journey ahead. Rather the worry remains that developing economies need to be made safe also, as further variants will emerge as we have seen most recently in India.

2 From lockdowns to living life again

Numerous EU governments have been forced, once again, to tighten restrictions which is likely to cause growth to once again slow across the continent for the first half of 2021. However, life is returning to normal in other major economies.

- China is amongst the most advanced with economic growth expectations of 8.5%[7] for this year.
- Smaller economies (eg. Israel) where vaccination levels have reached much greater penetration are also seeing the beginnings of normalisation.
- Indeed Israel is providing a very clear case study of the benefits of rapid vaccination and already showing a strong rebound in spending. For example for the week ended 22 March, the value of credit card transactions was 15% ahead of January 2020 levels while footfall in supermarkets and chemists was also ahead of that same period last year[8].

What makes this experience different and important for the rest of the world is an absence of an uptick in infection levels which was symptomatic of previous re-openings and augurs well for a widespread global economic rebound.

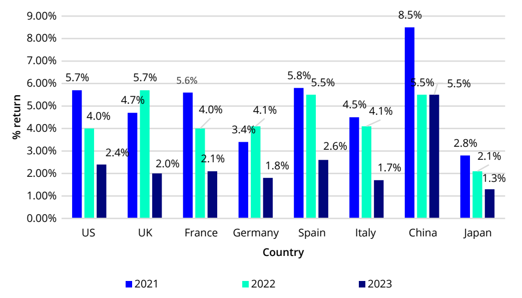
3 From recession to mini-boom

Forward looking estimates for most parts of the world have begun to look more optimistic. The US Federal Reserve (Fed) in its most recent statement has upgraded its economic growth expectations for the US to 6.5% for the full year 2021[9] (see figure 3). This has also been supported by strengthening key forward looking survey data from the US. Purchasing Managers Indices (PMIs), a measure of future production, are reaching multi-year highs[10].

Added to this is the scale of saving by consumers all around the world. This has now reached gigantic proportions (in the US it is estimated to have reached approximately $2 trillion in incremental savings during the pandemic)[11].

Central Bank liquidity, fiscal bounty and a consumer stockpile of savings combine to give the conditions for exceptional strong economic growth later this year.

Figure 3: Economic growth estimates 2021 to 2023



Source: Bloomberg Finance LP 31/03/2021

WARNING: These figures are estimates only. They are not reliable guide to the future performance of your investment.

[4] Source: www.worldometer.com 06/04/2021
[5] Source: Bloomberg Covid-19 vaccine tracker 25/03/2021
[6] Source: www.ourworldindata.org 06/04/2021
[7] Source: Bloomberg 25/03/2021
[8] Source: Investec April 2021
[9] Source: US Federal Reserve March 2021
[10] Source: Bloomberg April 2021
[11] Source: BCA Research 01/04/2021

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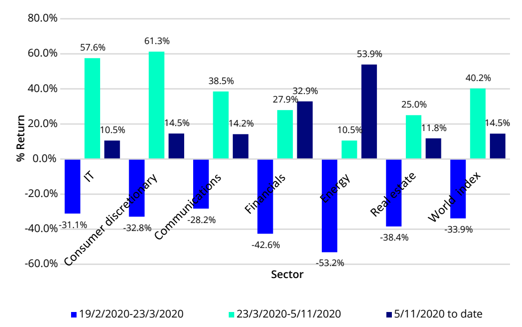
5 Trends for 2021 (Cont'd)

4 From rally to rotation

Last year's rally was dominated by the industries that fared best from the so called 'Stay at home trade' – the IT sector and related industries that benefitted from how we all had to live in 2020 and into 2021. Since the vaccination announcements of November 2020 this has changed with a rotation towards the industries that stand to recover most from normalisation, especially financials and energy related companies.

We can see this in evidence clearly in figure 4. This tracks the period of collapse (blue), the period of recovery (green) and finally the period of sector rotation (navy) of the performance of sectors since the vaccine announcements last November (05/11/2020)[11].

Figure 4: Sectoral performances during the pandemic



Source: Bloomberg Finance LP 31/3/2021

5 From monetary to fiscal

The US Fed is managing to walk a tightrope by increasing the US economic growth forecast considerably while leaving interest rates untouched. In so doing its Governor has signalled his intent to allow the US economy to run 'hotter' as rising inflation is expected to be a transitory phenomenon (traditionally a rise in interest rates would temper demand and reduce inflationary pressures).

Perhaps more importantly however have been the moves in US fiscal policy. President Biden has secured the first $1.9 trillion leg of his fiscal plans and at the end of Q1 his administration announced a further $2.25 trillion expenditure on infrastructure. Ultimately most commentators believe this will reach as high as $3 trillion once other expenditure is included. Source: Investment Markets, 01 April 2021.

Bottom line, the US policy landscape has been radically changed in Q1. The US is setting out on a fiscal expansion, some might say experiment, of unprecedented scale while monetary policy remains highly supportive. As a consequence markets have begun to shift attention from Covid-19 towards the resulting higher than expected economic growth – and its potential for inflation. With increasing inflation expectations, so too come interest rate increases – at least that's the normal pattern. Some argue that we are in the foothills of a significant and permanent increase in inflation – akin to what began in the mid 1960's.

Others, the Fed included, believe it will be a short term 'transitory' phenomenon expecting to see a spike in inflation followed by its return to a low risk factor in the financial system. This tension between what Central Banks are saying and what the market thinks will be a very significant focus for investors for the coming months – and its resolution will have a significant impact on investment returns in the coming decade.

[11] Source: BCA Research 01/04/2021

Summary outlook

- The big gains from financial assets of the last 12 months (to 01 April 2021) looks certainly to be behind us with a record breaking year that will be talked about for many reasons in the history books.
- The bond market is struggling as growth in economies exceeds expectations.
- Cash rates remain negative and will be at these levels for some years yet. It also appears that Central Banks are going to allow economies to run 'hotter' than they ordinarily would.
- Add in a dramatic level of fiscal stimulus and pent up savings and it remains likely risk assets can continue to deliver.

Appendix 1: Index returns for past 5 years

	2016	2017	2018	2019	2020
Global equities	11.09%	8.89%	-5.50%	28.93%	6.65%
Global bonds	2.39%	0.99%	-1.19%	5.35%	4.91%
Cash	0.54%	0.38%	0.33%	0.28%	0.22%
Property	7.9%	8.3%	7.5%	3.2%	-1.8%
Commodities	14.8%	-11.6%	-8.7%	7.5%	-11.4%
Absolute return funds	3.34%	-9.30%	4.30%	6.44%	-5.65%

Sources:Equities are measured by the MSCI All Country World Index expressed in euros. Bonds are measured by the FTSE World BIG Index hedged into euros. Cash rates sourced with ECB. Property is a 50/50 split of UK and Irish performances sourced with MSCI. Commodities are measured by the Bloomberg Commodity Index expressed in Euros. Absolute Return funds are measured using the performance of the HFR Absolute Return Fund Index expressed in euros.

For more information:

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WARNING: The value of your investment may go down as well as up.

WARNING: If you invest in these funds you may lose some or all of your investment.

WARNING: These funds may be affected by changes in currency exchange rates.

April 2021

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