

CEO Corner

Outlook 2021: A New Era



Daniel Zurbruegg
CEO BFI Infinity

Finally, 2020 is behind us. It was a year that probably no one among us will ever forget. The Covid pandemic has impacted all of our lives and created uncertainty for everybody. While the initial reaction was panic, we have started to deal with the situation, learned to go on with our lives and work towards solving the problem.

For financial markets, that initial reaction was rather dramatic, with equity markets falling between 30-50% within a matter of days. Soon after that, most of the western world went into some kind of lockdown. Work, travel, social interactions, entertainment, all the things we'd taken for granted were suspended, seemingly overnight, reminding us all that health and freedom are the most precious things in life. Last year was also challenging for us as a firm and as human beings and certainly for our clients too. Times like these are the ultimate stress test and that definitely also goes for any investment portfolio.

At BFI Infinity, we managed this stress test rather well. Since early January, most of our client portfolios were hedged and therefore the impact from the stock market crash was fairly limited. Of course, when we hedged the virus was not our biggest concern. Our decision at the time was more triggered by the increasing geopolitical tensions, especially between the US and Iran. However, as markets started to get more negatively impacted by the spread of the virus, we were certainly very happy to have those hedges in place, as they allowed us and our clients to control the stress that this new threat created on a global scale.

What initially looked like the perfect storm for financial markets took a more positive turn in April, when governments and central banks launched a broad-based

support and stimulus operation that, combined with declining Covid cases, led to a strong recovery in stock markets. We soon took profits on our hedges and continued to roll them forward, while holding a strong exposure to stocks and precious metals. Looking back, that really was the perfect move and we were able to capitalize on the market recovery which allowed us to deliver positive returns for the year. Our core strategies finished the year up 11.08% (Conservative), +12.25% (Balanced) and +18.97% (Dynamic). Our European/Swiss Single Stock strategy performed equally well with 14.48%, outperforming the Eurostoxx 50 (-5%) by almost 20 percentage points. Naturally, we are very pleased with these results, but we also realize this is no time for complacency, as new challenges are waiting for us in the year ahead.

So, here we are, in the first days of January 2021, with equity markets still on a positive trajectory, adding to the gains from 2020. In recent weeks, the momentum has shifted to more cyclical stocks and especially commodity-related stocks have been doing really well. This is a clear indication that the market expects the world to reemerge from the Covid trauma sometime in 2021. This expectation might seem a little odd, since most parts of the western world are again dealing with yet another round of lockdowns and restrictions. Yet, it's important to remember that the market is not a gauge of the present, but instead always looks ahead, trying to anticipate what might be unfolding in the near future.

In the short term, meaning in the coming weeks, there might be a bit more turbulence again and maybe even a small correction can't be ruled out, but ultimately, global growth is set to turn more positive and eventually global GDP will get back to its pre-crisis levels. Of course, this kind of complete global recovery might only fully materialize in 2022, but we already have many good reasons to support a more positive outlook for this year too. This is especially true now that the much-anticipated vaccines are coming to the market. Most countries have already started mass-vaccination programs and this should help drive down the number

of people that die with or from Covid or need to be hospitalized. It could thus alleviate the pressure on healthcare systems and lead to reduced restrictions on business, travel and social activities. We don't believe that the Covid situation will be entirely resolved until 2022, or maybe even later, but it won't be an issue anymore for the broader market and it will certainly be less of a focal point in the media. This should in turn allow people to focus on other things again and regain a sense of normalcy.

However, while the health effects of the pandemic might eventually come under control, the economic consequences will be with us for much longer. Central banks around the world have become very aggressive and money supply has exploded. All this generous money printing will certainly help with the most imminent pain of the crisis, but it will likely lead to continued asset price inflation down the road.

This has already been apparent over the last years, as the result of the last crisis response of central banks, and given the scale of the stimulus we saw being deployed this time around, we can expect an acceleration in the future. Significantly more funds chasing the same goods and services will ultimately lead to higher asset prices, higher levels of inflation and most likely

will cause a sharp decline in the value of fiat money, with the US Dollar being at the highest risk for a serious decline in coming years. This is not only because of the political turbulence that we have been seeing lately, but more closely linked to the chronic deficits and the total inability of the government to get the debt situation under control. We're bound to see serious pressure on the dollar at some point and this is why we feel that broad-based currency diversification is a key element in a successful investment strategy. This ultimately means that investors need to consider international investing and to allocate their money to countries that promise higher levels of growth in the coming years, which leads us to the topic of the second part of this update, namely the case for Asia.

The rise of Asia and especially China is a reality that cannot be reversed, whether we like it or not. Of course, this rise will not be without problems and frictions, both internal and international ones. In fact, the ongoing trade dispute between China and the US might be seen as just an early indication that we are at the start of a new era, where trade disputes, and even all-out trade wars, could become the norm. These dynamics are unlikely to change much under the Biden administration. It is clear that the US will seek to renew and to reinforce its ties with Europe, in order to form a strong

Annual change in M2 money supply in the US



Source: Federal Reserve, Bloomberg

alliance against China. Exactly how all this will unfold in the coming years is hard to say, but we don't expect it to spell the end of global trade. It will more likely bring about a changed form of global trade and with it, more of a "regionalization of globalization", something that is already reflected in the strong Pan-Asian trade. The implication for us as investment managers is that we expect to focus on and find more interesting opportunities in Asia in the future.

Despite some short-term concerns due to the "second wave" of the pandemic that hit some regions harder, we do expect a gradual improvement in the global economy and also a continued upward trend in global stocks. There is no way around real assets such as stocks, precious metals, commodities and real estate. The enormous amounts of fiscal and monetary stimulus fueling the recovery can temporarily push growth rates up significantly and of course, support the continued climb of asset prices.

Nevertheless, there are longer term concerns to bear in mind, as most of this stimulus is financed by additional debt that can only be financed as long as rates are kept very low. Low rates also give governments an incentive to spend even more. Increasingly popular ideas like "green deals", Universal Basic Income (UBI), or "job guarantees" by the state for everyone, all demonstrate just how much some politicians have lost touch with reality and how eager they've become to spend money they don't have. We remain very skeptical about these policy trends, especially as they're gaining traction in many places, particularly in the western world.

Investors, whether they like these developments or not, have no other choice but to position themselves accordingly and to invest in areas that will benefit from this great reflation, which will ultimately come at the cost of destroying the purchasing power of money. This means that stock markets, precious metals, cryptocurrencies, commodities might have much more upside in the coming years. Typically, most people would expect that such a reflation will lead to a sharp increase of inflation, however, there are a lot of strongly deflationary forces in the global economy that might keep inflation low for longer. A huge increase of productivity through innovation and technology could be an especially important factor in this regard.

Overall, we welcome the new year with a positive attitude and hope for better times ahead. These are very interesting times with a lot of opportunities to offer, but we are also dealing with a lot of new challenges.

We look forward to exploring and navigating all of these together and wish you all only the very best for a healthy and successful New Year. Feel free to contact us directly at info@bfiwealth.com, we look forward to hearing from you.

Asia's promising outlook for 2021 and beyond



Dirk Steinhoff
Chief Investment Officer

The covid crisis has been very different from past downturns and recessions in many ways. Its onset, its driving forces and the global response to it have significantly set it apart from previous crises and it's thus not surprising that the recovery from it might also present some in-

teresting and historically unusual opportunities too. These investment opportunities will exist in several areas, but in this issue of the InSights we would like to discuss one of them in more detail: Asia. And when we talk about Asia we don't limit ourselves to China. We're also looking at markets like Vietnam, India, and Indonesia that, unlike China, haven't received the investor attention they arguably merit.

For a long time, conventional wisdom held that it was wise for investors to largely steer clear of Asia during crises and recessions. Historically, the impact tended

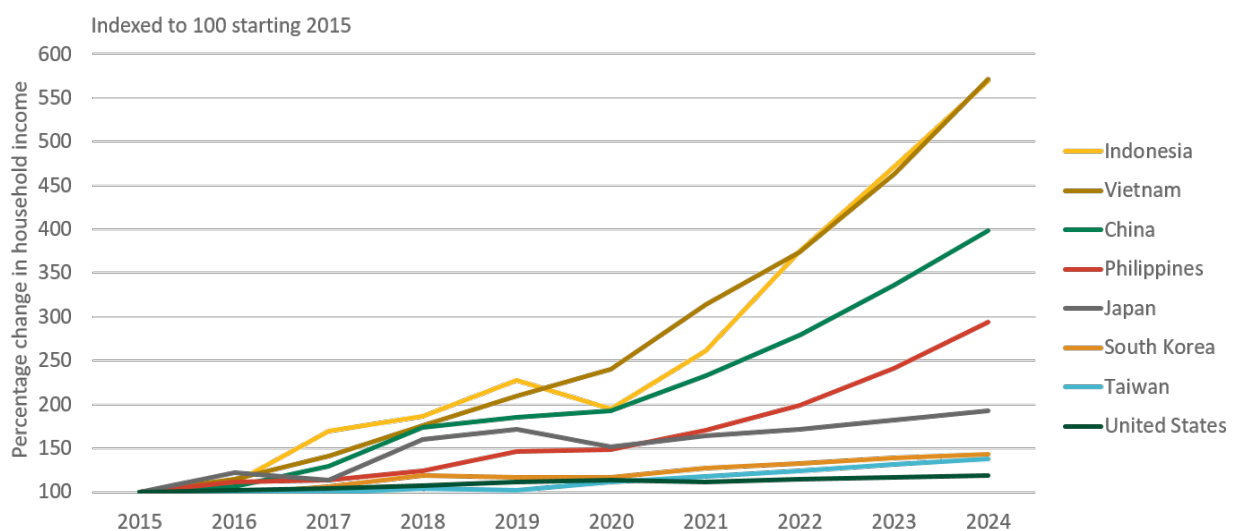
to be more severe and the destabilizing effects much more pronounced, so this skepticism was entirely prudent and justified. In past crises, many economies in the region saw their domestic currencies collapse, while massive capital flight further amplified the impact of any recession and ensured a protracted and painful path to recovery. There were also serious vulnerabilities and concerns around institutional integrity, inadequate infrastructure and political instabilities that shook investor confidence, while the legal frameworks and business protections were also seen as insufficient, especially amid a crisis.

However, the outlook this time has substantially changed, with the region presenting some very attractive opportunities and numerous good reasons to expect above average growth.

Long-term trends and reforms

A lot has changed in the Asian region since the last global recession and the developments over the last decade have successfully transformed its position and outlook in the aftermath of the Covid crisis and beyond. The most important of these changes are

Growth in household income (\$35,000+)



Source: Fitch Connect

found in the progress and improvements made in local infrastructure, supply chain shifts, workforce skills, and productivity. Many nations in the region also now offer a more stable and business-friendly legal environment. Corporate and investment protections were established, along with many other important reforms, as noted in the “Doing Business 2020” report published by the World Bank. Furthermore, a 2020 analysis of more than 36,000 businesses in 17 Asian economies conducted by the Asian Development Bank revealed that strong property rights and rule of law enabled and motivated entrepreneurs to formalize their businesses, and that this growth in formalized businesses was also associated with increased innovation. Political stability, along with supportive policies that encourage international investments, also helped improve investor sentiment and promote trust in government and regulatory institutions.

This wave of modernization, liberalization of domestic economies and capital markets and solid advances in the private sector has been evident in varying degrees in many countries in the region, but the net result was the creation of a much more supportive environment for international business, as well as domestic entrepreneurship and innovation.

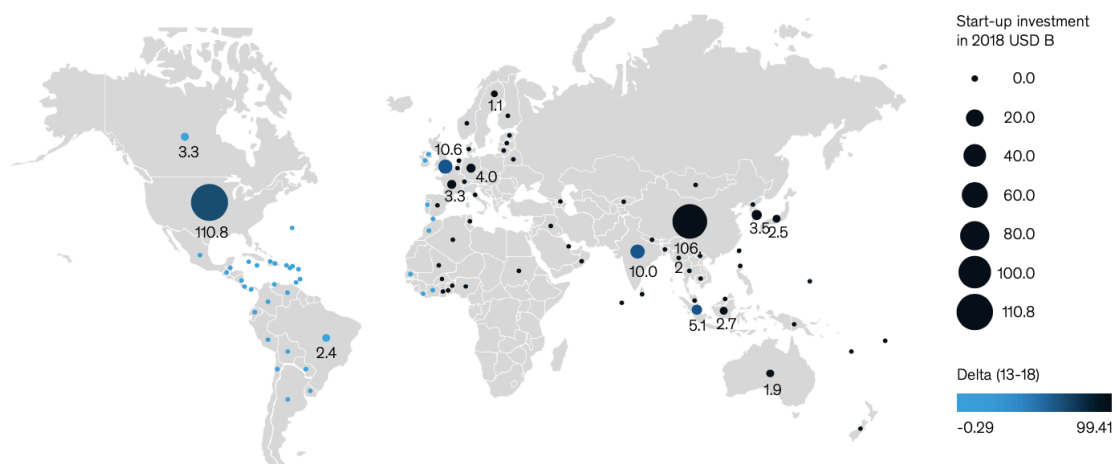
This also contributed to the emergence of a vibrant and competitive corporate ecosystem, with many Asian companies now ranking among the world’s largest. A considerable share of revenues still comes from international exports, but as Asian economies evolved, they decreased their reliance on manufacturing for the West, and pivoted to the increasingly resilient and sophisticated domestic and regional markets.

Important strides were also made in technology and in the digital economy. For instance, since 2014, Indonesia and India have been well ahead of the rest of the world in digital adoption rates, with the number of internet subscribers in India almost doubling by 2019 and mobile data consumption growing by over 150% annually, more than twice the rate of the US. Also, with Asia accounting for over half of the world’s total internet users, e-commerce has exploded, and so has the inflow of venture capital in the region’s start-ups, as can be seen in the graph below.

Another major long-term trend is the steady decline in global poverty rates. This has played a particularly crucial role in Asia, as it transformed national and intraregional consumption patterns. Wage growth and a rapidly expanding middle class have fueled

By 2018, Asia already accounted for nearly half of global investment in start-ups

USD Billion, 2018, 2013-2018



Source: Preqin, McKinsey Global Institute analysis

local demand and according to McKinsey projections, the region will account for more than half of global consumption growth by 2030.

There's also a strong argument to be made based on the region's fundamentals. Coming into this crisis, the finances of many Asian countries were significantly healthier than most of their Western peers. There are of course exceptions, like Japan, but a lot of Asian nations tended to carry less debt and exercise stricter budget discipline. According to the UN's Economic and Social Commission for Asia and the Pacific (ESCAP), public debt was at sustainable levels before the onset of the crisis, "with a regional median at about 40% of GDP". This meant that the region was overall better positioned to sustain the impact of the Covid crisis, but also to handle the costs of the fiscal support measures that were deployed to combat the effects of the pandemic.

This tendency toward more financial prudence is also present in the region's companies that, in general, also tend to have stronger balance sheets, something that was highlighted in recent reports by PineBridge Investments and UBS as an advantage for Asian equities going into 2021. There are advantages on the monetary front as well, with interest rates being relatively higher in many Asian countries than in most advanced economies, which gives them more room for monetary stimulus, but also makes them more attractive for investors. In fact, we saw this interest pick up significantly over the past decade and even more so over the past year, with Asian bonds being among the fastest-growing segments in the global bond market.

Last, but certainly not least, there's the impact of the US dollar and shifts in the region's dependence on it. The USD has long been the dominant currency not only in international trade and intraregional transactions, but also as a reserve currency and as a reference in domestic policy making. Historically, this reliance on the USD, although a practical necessity, has rendered Asian economies particularly vulnerable, as highlighted during past crises. Thus, a wider "de-dollarization" drive, originally led by China, has been gaining traction over the last decade. In recent years, we saw some meaningful developments on

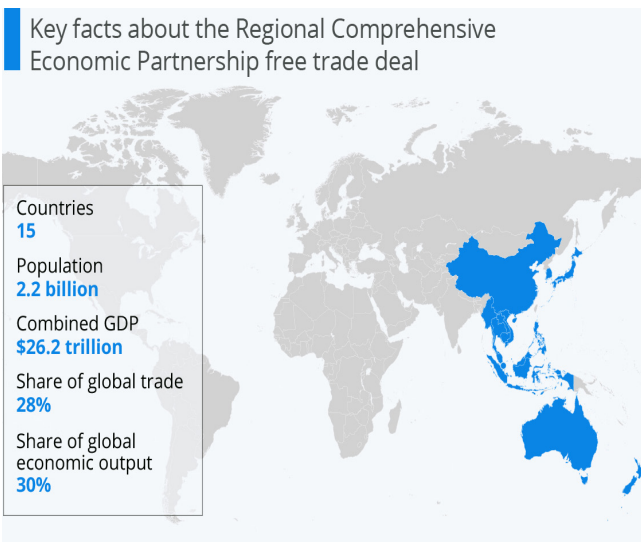
that front emerging from Sino-Russian deals, with the two nations agreeing to reduce their dependence on the dollar. According to the Financial Times, in the first quarter of 2020, the dollar's share of bilateral trade fell below 50% for the first time on record. China has also been inking similar deals with Asian partners to promote the use of local currencies, like it did with Indonesia last September. The use of the Chinese yuan has seen a significant boost in recent years in trade, but also as a reserve currency. This is a trend that Morgan Stanley analysts expect to continue, predicting that the currency will account for 5% to 10% of global foreign exchange reserve assets by 2030, making it the third largest reserve currency in the world, after the US dollar and the euro. Meanwhile, other local currencies have also been enjoying wider use, as domestic consumption and inter-Asian trade continue to strengthen.

Accelerators and triggers

Apart from slower-moving shifts such as the ones outlined above, there were also some key events that served as triggers and further boosted the regions' prospects. Chief among them was the Covid pandemic. Although in some cases the measures taken did not fit the western understanding of personal freedom and self-determination, the way that it was handled by many Asian nations proved to be very effective. Asian experience with previous outbreaks arguably played an important role in this. The quick government response, efficient testing campaigns, swift border closures, all contributed to a faster containment and to an earlier resumption of economic activity. This provided a valuable head start to the recovery and a clear advantage going into the new year, with the IMF predicting a strong growth rebound to 6,6% in 2021.

The US-China trade war was another interesting accelerator, as it was smaller Asian economies that arguably reaped the spoils. For example, US imports from Vietnam kept growing throughout the trade crisis. By 2019, they were up nearly 40% year on year, while those from China had sunk by more than 20% and in the summer of 2020, the US trade deficit with Vietnam surged to an all-time

RCEP: The world's largest trade bloc



Source: Bloomberg, Statista

high. Overall, according to UBS analysts, the Vietnamese economy now presents “one of the brightest outlooks in Asia”, with growth set to rebound to 6,8% in 2021. Supporting this positive view is the EU-Vietnam free trade agreement, signed in 2020, that scrapped almost 99% of customs duties and is expected to spur foreign direct investment.

Of course, when it comes to Asian trade deals, we couldn't fail to take into account the largest and most consequential of them all, namely the Regional Comprehensive Economic Partnership (RCEP). Signed in November 2020, after 8 years of negotiations, it created the largest trading bloc in the world. Consisting of 10 Southeast Asian countries, as well as China, Japan, South Korea, Australia and New Zealand, members of the RCEP make up nearly a third of the world's population and account for almost 30% of global GDP. The RCEP aims to eliminate tariffs within 20 years, but also includes provisions that help streamline trade rules and supply chains. This deal is expected to provide a remarkable boost for the region and to strengthen its economic and geopolitical position on a global scale.

Investment implications

At BFI Infinity, we see Asia's bright outlook as a great investment opportunity. Overall, Asian markets have now matured and are quickly catching up with the West. They no longer present merely speculative attractions, but are now ripe for sound investments and can offer both value and growth, often at very attractive price levels. We can see this in equity markets, where Asian stocks appear cheaper compared to the current valuations in the US and Europe, and in the debt market too, where Asian high yield and investment grade bonds both offer better yields than their developed market counterparts. The currency diversification which comes with these investments might positively add to the performance as well.

Of course, Asia shouldn't be seen as a homogenous block and there are still structural, political, geopolitical and economic issues that vary from market to market and that need to be taken into consideration. Nevertheless, with a careful and diligent selection process, investors can find excellent opportunities in the year ahead, especially given Asia's head start in the recovery stage after the Covid crisis.



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