

Letter from the CIO

7th of August, 2020

Dollar, Gold and other Records

The equity markets continued to rise during the month of July, still supported by massive injections of liquidity from central banks as well as by the various stimulus plans put in place or being prepared by the states. Second quarter earnings season of US companies also had its impact on markets the last couple of weeks. While the absolute figures have shown the extent of the impact of the COVID-19 crisis on the economic fabric, many companies have nonetheless beaten market expectations, the latter having been massively revised downwards during the last few months by analysts. To date, out of 60% of companies that have already published their results in the US, 84% of them beat consensus and generated profits above expectations for the second quarter. In aggregate, earnings per share are 20% higher than expected, which is totally unusual. In comparison, if this figure of 20% remains stable until the end of the earnings season, Q2-2020 would be the quarter having recorded the largest percentage in terms of earnings surprise since the start of this indicator in 2008 by FactSet data! Regardless, these better-than-expected numbers reassured investors, resulting into a more than 4% increase for the month for the S&P 500 index.

The same rise as in the US market was not reflected in other regions, with the European Stoxx 600 index and the SMI index posting respectively a performance of -0.9% and -0.3% over the month. The main culprit? The plunge recorded by the US dollar since March, which accelerated sharply in July. Indeed, the DXY index, which compares the value of the US dollar to a basket made up of the currencies of major developed countries, fell by more than 4%, registering its worst month in more than a decade. The deterioration of the balance of payments, the fall in real interest rates, and the uncertainty linked to the US elections in November are all factors weighing on investor's confidence in the currency. The downward movement is already well underway and a consolidation level around 1.20 against EURO is likely in the short term. The horizon is even darker in the long term for the main currency of reserves. As a result, an increase in monetary measures by the Federal Reserve could increase the pressure on US Treasury bill rates, and therefore further reduce the premium enjoyed by the US dollar against other "safe" currencies

DXY Index from January 2018 to July 2020



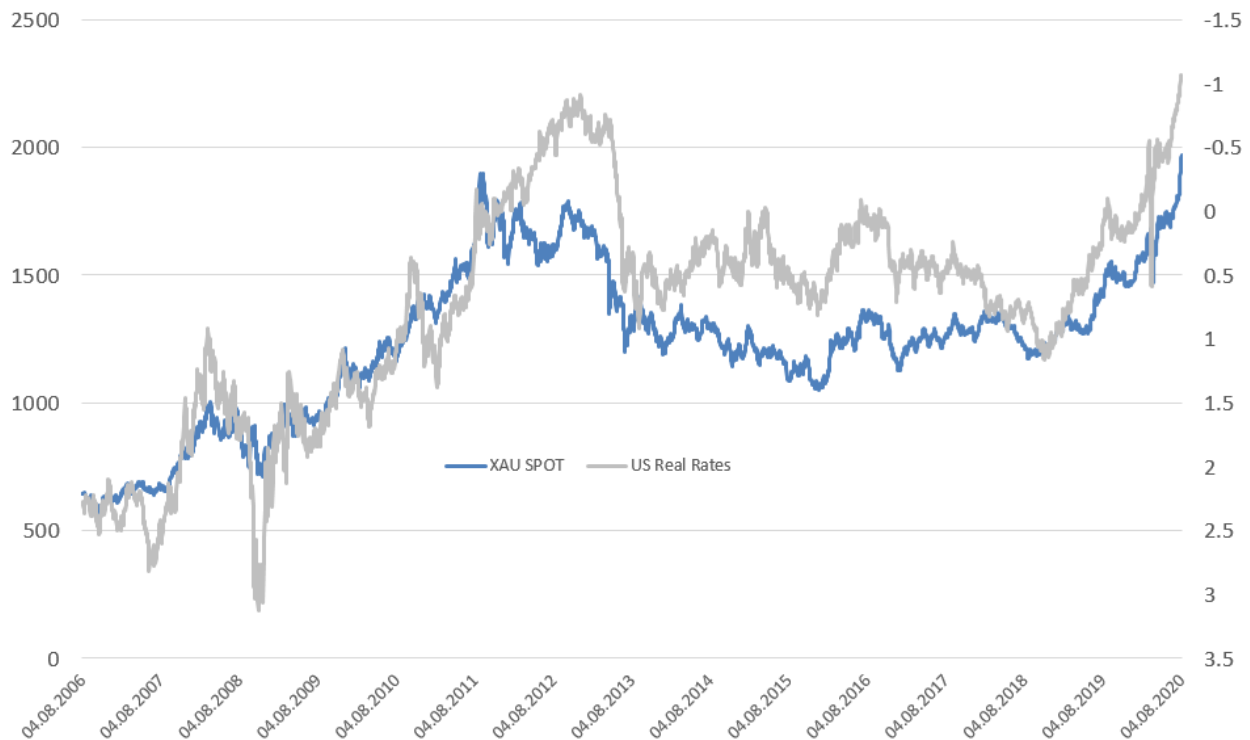
Source: Bloomberg / Banque Heritage



Another beneficiary of the US dollar's decline in July was gold, posting a 10% increase over the period. The precious metal has crossed an all-time high the USD 2,000 per ounce threshold as of this writing, and is up more than 30% since the start of the year. What's next? Gold is very strongly correlated with US real rates, and the latter are at their all-time low, a situation caused by the extremely accommodating policy of the Fed aimed at keeping nominal rates low along with inflation. Gold does not produce any income, but in this period of

unprecedented economic and sanitary crisis, the precious metal is mainly seen as a safe haven to protect against the ravages of the markets. The future upside potential will mainly depend on the effectiveness of monetary and fiscal policies put in place around the world to revive the economic engine. But in this period of great uncertainties, economically, politically and sanitary, it is very likely that gold will retain its attractiveness in the months to come!

Gold vs Real Rates (inverted)



Source: Bloomberg / Banque Heritage

Within our portfolios, the overweight of gold largely contributed to the positive performance recorded in July in our various profiles. We haven't had an active dollar bet open since the start of the year, which has also been a good contributor. We remain slightly underweight equities at the start of August, and maintain our bias on the technology and healthcare sectors. Finally, our Hedge Fund pocket continues to deliver stable positive performances, with our Long Short strategies as the main driver.

Have a nice summer everyone!

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