TURNING POINTS?

Investment policy
July 2021

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Turning points?

July 2021, Benjamin Schoch and André Kistler

Economy

The temporary shock of coronavirus to the economy last year has resulted in significant catch-up potential for the global economy, and we are currently right in the middle of this catching-up process. Not only is the export industry experiencing a strong upturn but the service sector, which has been hit by government restrictions, is also expecting to see a recovery soon.

The significant variation in the speed and strength of developments globally has resulted in temporary shortages of goods and supply difficulties. The current pricing pressure is not only coming from rises in raw materials prices caused by speculation, but, in particular, also to the elimination of industrial overcapacity and to businesses reducing their inventories to a minimum before the coronavirus pandemic broke out.[1]

In the highly interconnected global economy, this economic shock has all the more impact because just-in-time production means only the amount that was just ordered is produced, and an (overly) high inventory is avoided as an unnecessary capital commitment. Are the price trends worrying? No. Firstly, the majority can be explained by the one-off factors described. Secondly, the structural trends of digitalisation, globalisation and overindebtedness, which were already at work before the crisis, are creating deflationary pressure.

However, it is fair to say that inflation – and closely associated with this also interest rates – have reached their lowest point after steadily falling over a decades-long process. A decreasing labour supply, record government spending programmes and tax increases will create a certain upward pressure on inflation and interest rates. Real interest rates will, however, continue to oscillate around the zero mark for several more years

Outlook

The risks for rising interest rates abroad have increased slightly. For equity markets and also heavily indebted countries, only significantly higher interest rate levels are worrying. We are not expecting this scenario. Industrialised countries are outdoing each other with record spending programmes, and the "whatever it takes" mentality seems to have become a firm fixture. Pent-up economic demand is high and being strengthened even further by government spending programmes. Next year at the latest, the leading central banks will have to consider withdrawing their bond purchase programmes so as not to lose their credibility and control.

The major themes of the last decade have been globalisation, digitalisation, ageing of the population and debt. These factors will persist. Digitalisation in particular will continue to establish itself as one of the most important long-term economic drivers. We are only at the start of a world that is increasingly being shaped by automation, quality improvements and productivity increases in almost all areas. The business world has demonstrated fantastic performance and stability over the last decade due to digitalisation. This will continue.

Conclusions for our investment policy

The prospects for higher company profits have improved markedly in the aftermath of the coronavirus shock. Demand for the stocks of successful and secure companies will continue to increase at the expense of fixed-income securities. The stocks of these first-class companies have significantly higher return potential than all other asset classes and therefore also justify current valuations in view of their expected performance. We are maintaining an overweight position in equities.

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[1] See 02/2020 investment policy: Disrupted global supply chains

See 04/2020 investment policy: Temporary shock

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