Edwards Wealth Management AG
Switzerland

BOREAL
CAPITAL MANAGEMENT

Investment Policy

December 2020

Our market view in a nutshell – December 2020

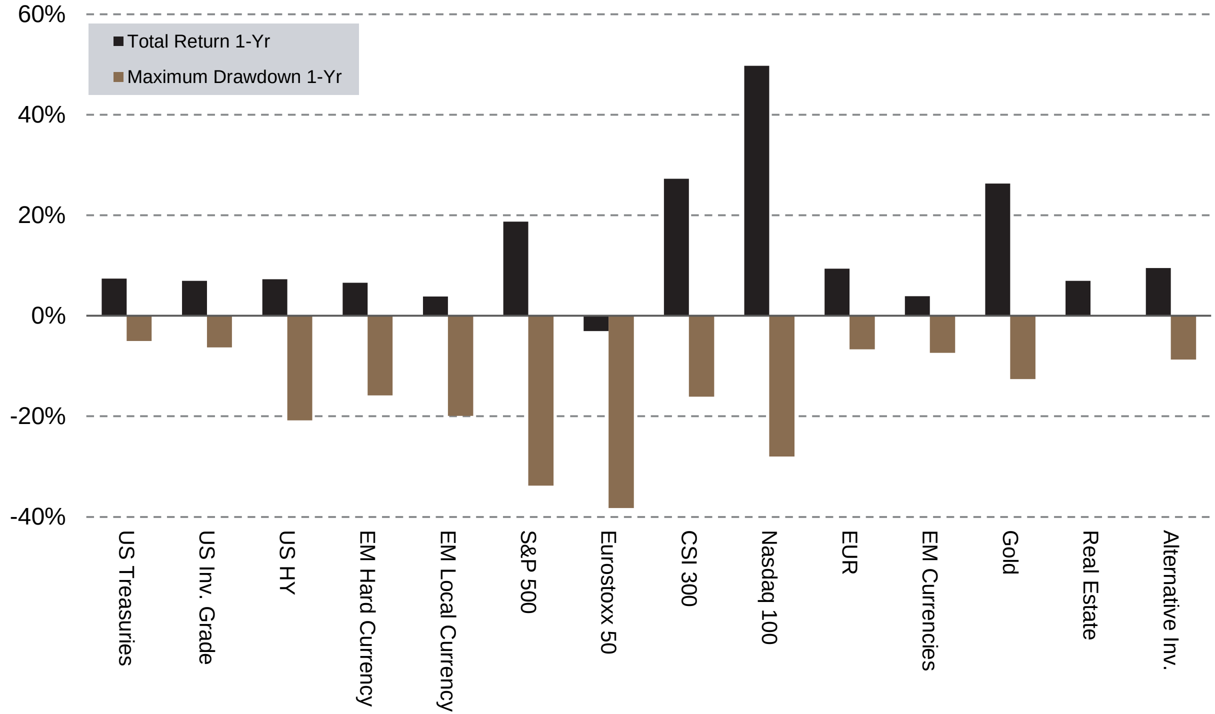
- **2020 will be an unforgettable year**. On the one hand, a sad and awkward year, in which many lives have been lost, many other people have suffered financial difficulties and we have all seen our freedoms curtailed. A powerful reminder that both life on the planet and our social order are very fragile. But on the other hand, a year in which we have also seen enormous displays of solidarity, and we have been able to marvel at how human inventiveness allows us to overcome problems
- Obviously, financial markets have not been immune to all this. **Panic and fear of the unknown caused markets to fall dramatically** in March; while **solidarity in the form of massive government relief packages made it possible for the economy not to fall into a depression**. Finally, corporate adaptability and business innovation allowed the economy to regain much of the lost ground, and **financial markets roared back** ending the year with strong gains
- **Looking ahead to next year**, it can be said that with regard to the economy, the main variable is the **evolution of the pandemic**, while for financial markets, it is all about **interest rates**. The pandemic has undoubtedly contributed to the collapse of interest rates, but it is not the only cause. **The biggest unknown for the near future is whether the almost certain economic recovery will bring with it an increase in interest rates and/or inflation**, which could negatively impact valuations
- At this point, **elevated equity multiples, coupled with low credit spreads, leave investors ill-equipped to deal with an eventual increase in risk aversion**. Add to this cocktail the fact that the risk-free rate is at a minimum, it must be accepted that **portfolio returns will be much lower in the future**
- **Stocks not only look much more attractive than bonds from a relative value perspective, but also from a risk management point of view**. If a strong economy causes interest rates to rise, corporate profits should rise in tandem; thereby providing some support to valuations. In the case of bonds, with credit spreads already so tight, the margin to cushion the negative impact of a rate hike is limited

EWM Investment Policy

Asset Class		View	Rationale
Fixed Income	US Treasuries	=	Treasuries offer protection from a slowdown in growth, but we believe that current long-term yields are unattractive, hence preferring shorter maturities
	US Credit	=	The incoming economic downturn will undoubtedly lead to an increase in the number of corporate defaults. Although credit spreads already reflect this risk, we favor Investment Grade over High Yield.
	European Sovereign	–	High quality debt in Euros presents a very unattractive combination of risk and return as current yields offer very little cushion to weather potential interest rates increases
	European Credit	=	In European credit we only see value in subordinated debt, asset-backed securities and short-duration high yield
	Emerging Markets	–	A weaker dollar should help emerging markets, but both currencies and credit spreads have only partially reacted to the risk that the Covid outbreak represents for these countries. In addition, the oil price war will harm exporting countries
Equities	US	+	After a sharp sell-off, valuations have improved. We have therefore increased our exposer to US equities, mostly through quality and growth oriented companies
	Europe	–	The European economy has been more affected by Covid than that of the US or Asia. Relaunching it will require a greater fiscal effort, which will have to be financed by new debt. A repeat of the sovereign debt crisis is a real risk
	Japan	=	Japanese stocks are the cheapest in developed markets, but have suffered recently due to sluggish growth, and concerns about global trade
	Emerging Markets	–	Emerging markets, in general, will lack sufficient fiscal freedom to stimulate the economy after the pandemic
	Sectors & Themes	+	Beyond our core call for quality-growth companies, we favor Real Estate, Infrastructure and Biotechnology
Alternative Investments	Multi-Strategy Hedge Funds	–	Multi-strategy / multi-manager hedge funds with daily liquidity are having disappointing performance, particularly when compared with other less risky alternatives, like short-term corporate bonds
	Commodities	–	In the present late-cycle environment, with inflation pressures remaining subdued, we see limited upside for commodities. However, we favor gold in the current negative real interest rates environment.
	Private Equity	=	Investing in late-stage private equity provides access to the asset class with liquidity provision up to a certain degree

\+ Overweight – Underweight = Neutral

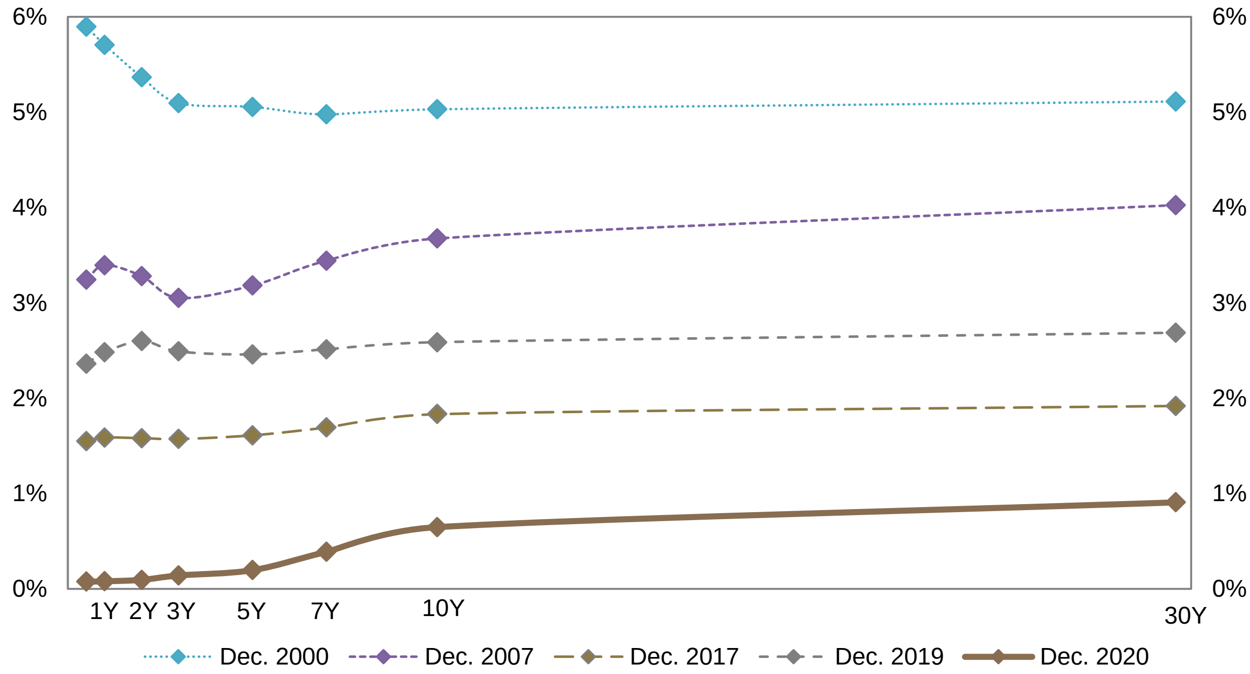
A year like no other



- This year we have witnessed the **largest swing ever experienced in financial markets**. The downfall was caused by investors panic at having to face an event for which there is no valid frame of reference in modern times. The **rebound was fueled by massive fiscal and monetary support**
- **Investors also lack a frame of reference to assess the long-term consequences** of such policies, so we continue to write completely novel chapters in the history of finance

Source: Bloomberg

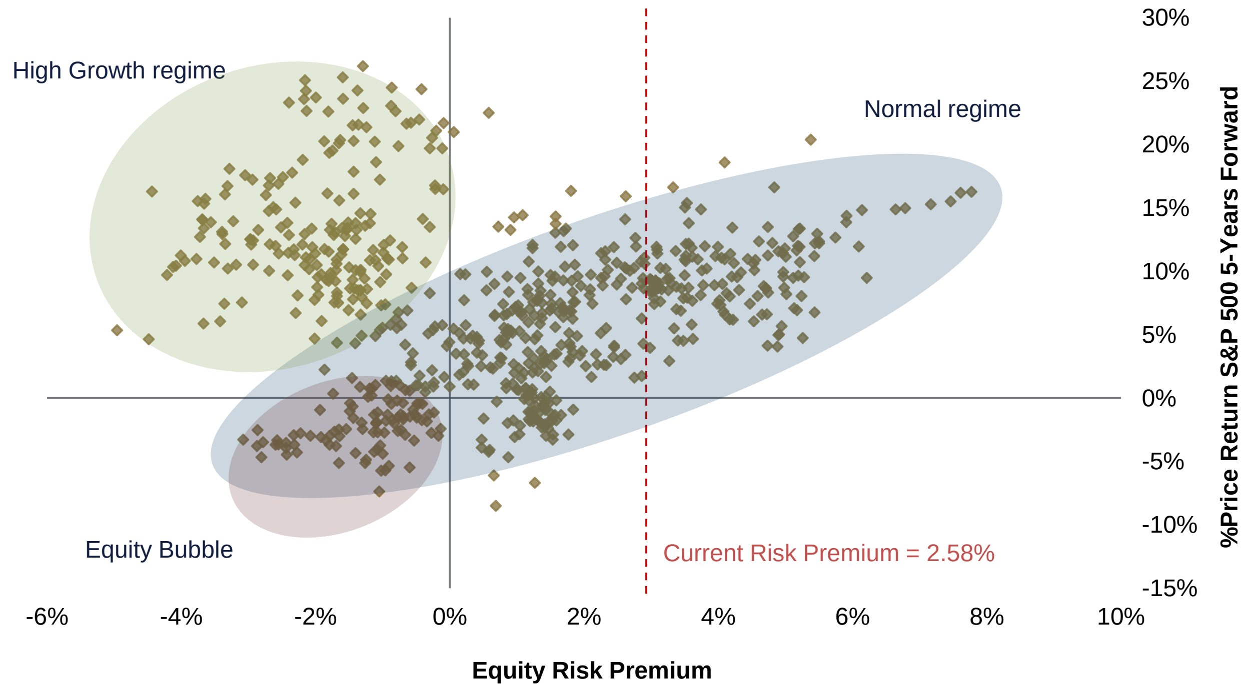
The great collapse



- The current **valuations can only be explained by the collapse in interest rates, which predates the pandemic**. In fact, it started long before central banks began to inject huge amounts of liquidity into the market after the financial crisis
- After the **Fed showed its inability to continue normalizing monetary policy in early 2019**, long-term interest rates have completed what could be their last leg down. This means that it is very likely that **investors will no longer enjoy the tailwind that has propelled markets over the past decades**

Source: Bloomberg

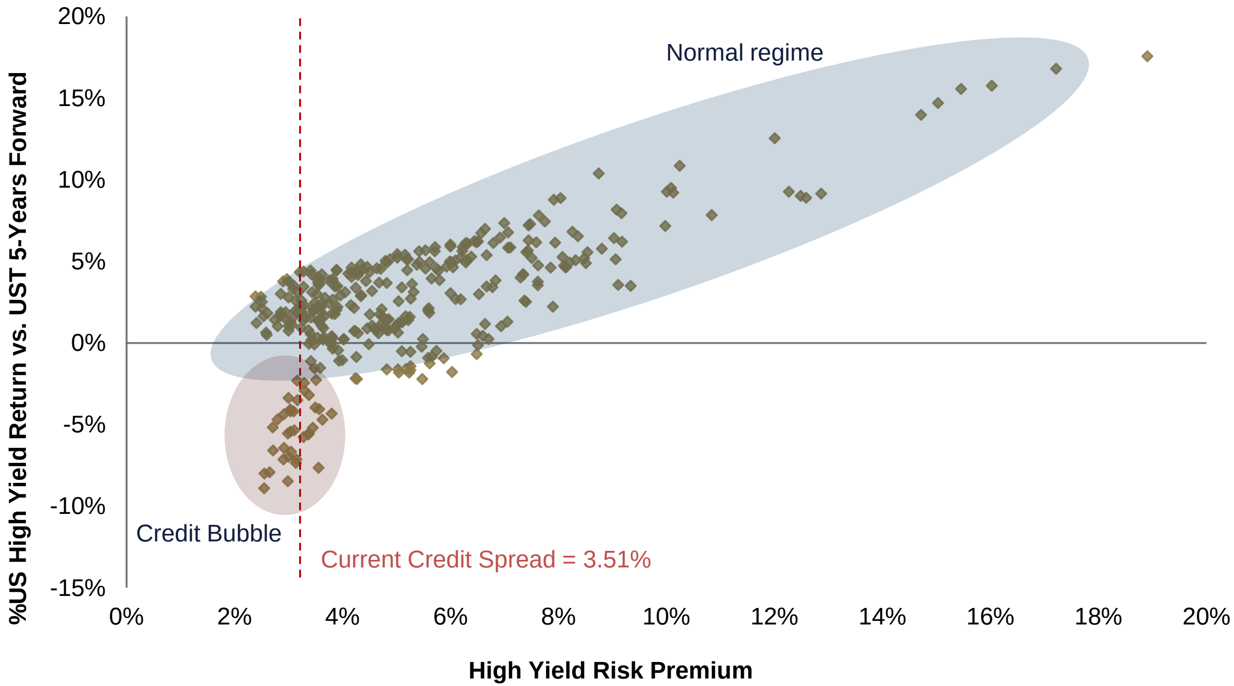
How much safety cushion in equities?



- **Low interest rates allow for higher multiples, which in turn depresses the implied equity yield**. As long as the latter is higher than the risk-free rate (which is currently very low), equities remain attractive. But **as investors pile into stocks in the absence of better alternatives, the safety cushion diminishes**
- The **risk premium currently stands at a level that has historically proven to be safe enough to be a good entry point**; however, taking into account how sensitive valuations are to changes in interest rates, it is important to **remain highly selective**

Source: Bloomberg

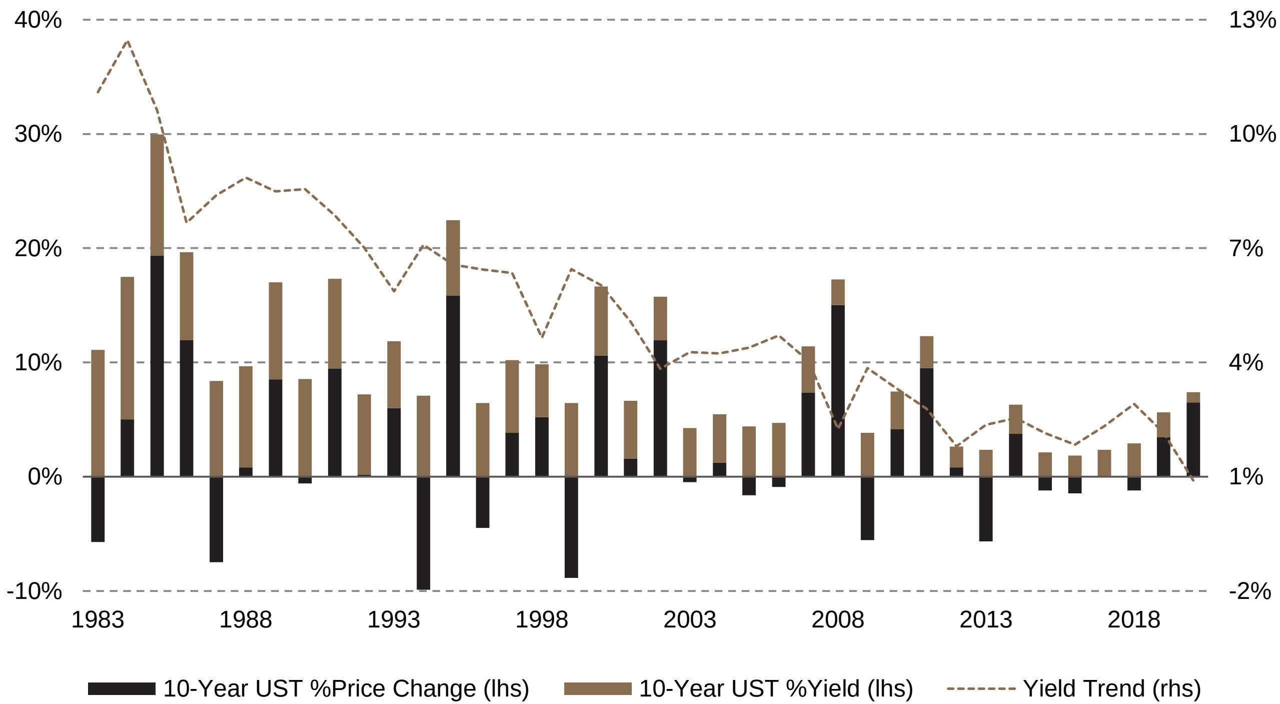
The search for yield may end in a precipice



- **Credit markets, by contrast, have much less room** to weather future bumps along the way. These could arise as a result of an economic slowdown, or an increase in risk aversion
- **Unlike stocks, the return on a bond is limited**. An increase in corporate profits translates into an increase in the price of a share, which in principle, is unlimited. However, in the case of bonds, it only causes a reduction in the probability of a default

Source: Bloomberg

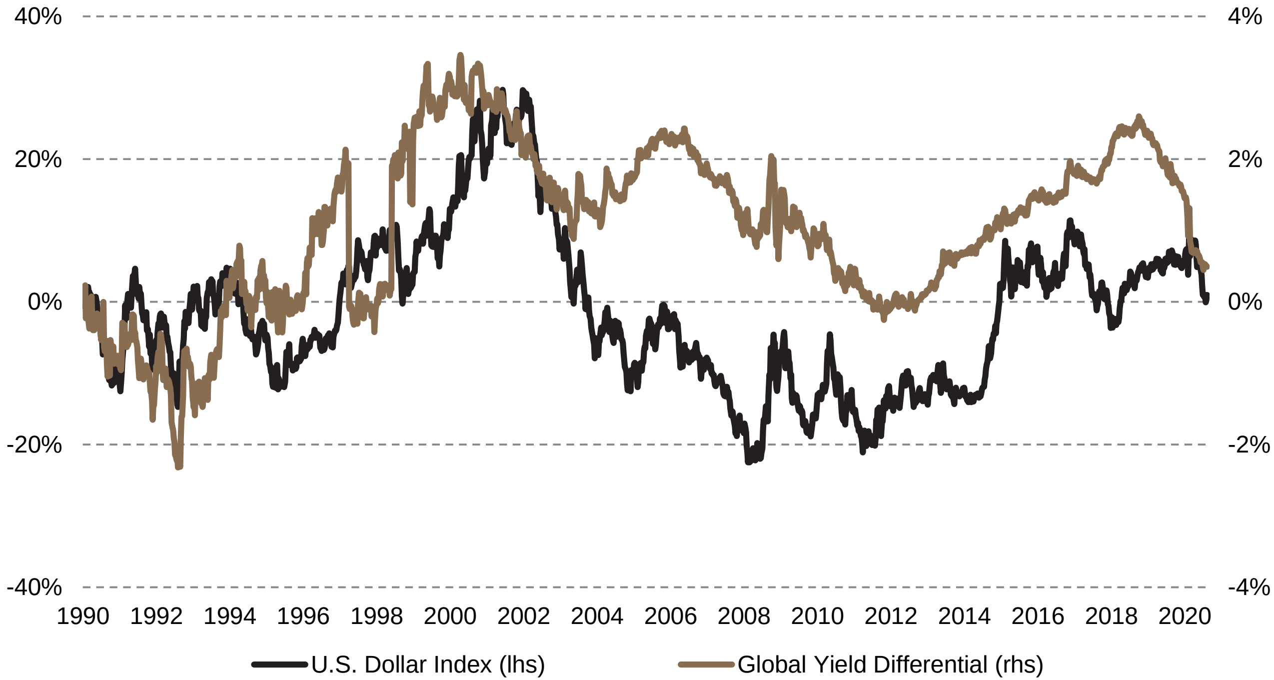
Loss of carry aggravated by risk-free rates



- **To further complicate matters for bond investors, the other component of the carry, the risk-free rate, is at record lows**. This means that bond investors have virtually no protection against inflation or growth shocks.
- **Portfolio diversification becomes more difficult** as bond investments are deprived of carry, while in turn all asset classes become increasingly dependent on interest rates; this forces us to rethink traditional asset allocation

Source: Bloomberg

Monetary policy convergence drives FX markets



- **The collapse of the US yield curve has also been felt in currency markets**. With the interest rate differential narrowing considerably, **the attractiveness of the US dollar has diminishe**d. Currently, the dollar is trading close to fair value in purchasing power parity terms against the Euro
- However, **economic growth differentials will become increasingly important**, favoring the dollar and the Chinese yuan, which is progressively gaining recognition as a reserve currency

Source: Bloomberg

Investment scenarios

	Scenario 1 "U" Recovery	Scenario 2 "V" Recovery	Scenario 3 "W" Recovery
Drivers	• Global depression caused by the unprecedented sudden stop of economic activity • Lockdowns extend longer than initially anticipated and restrictions on movement and commerce prevent a normal return of activity • Fiscal support packages prove to be insufficient, and countries with a lesser fiscal latitude suffer prolonged recessions	• Global recession caused by the unprecedented sudden stop of economic activity • Lockdowns can be lifted earlier, or on a geographical basis, and economic activity is largely resumed, with some adaptations to control the spread of the disease • Fiscal and monetary support allow the economy to rebound strongly, while low interest rates make the debt burden manageable	• Deep recession followed by a rapid but failed recovery • There is some return to normality by the summer, but return of the virus in Autumn causes intermittent lockdowns until a vaccine is available • Countries with a stronger fiscal position may be able to provide further stimulus and avert a "W" recovery
Market impact	• Credit spreads remain high, fueled by a wave of corporate defaults. Weak sovereign bonds underperform significantly • Corporate earnings struggle to reach pre-crisis levels, and equity returns remain lackluster • Sovereign and high-quality benefit from the flight to quality, as well as the continuation of an ultra-loose monetary policy worldwide • USD neutral as flight to quality is offset by low interest rates • Commodities fall further	• Equities appreciate moderately, as TINA ("There Is No Alternative") lure investors back to stock markets, but there is wide dispersion across sectors • Credit spreads remain tight but do not recover to pre-crisis levels, as investors will favor companies with strong balance-sheets • Wide dispersion between both sovereign bonds and currencies, as yield curves will likely steepen as governments flood the market with new debt • Commodity prices will stabilize	• Wide dispersion in both equity and credit markets, with stronger companies recovering and weak companies lagging behind • Credit spreads remain elevated as the market remains highly volatile and defaults increase • Wide dispersion between both sovereign bonds and currencies, as yield curves will likely steepen as governments flood the market with new debt • Relatively strong USD as the US economy turns the corner faster. The Euro may suffer a remake of the sovereign debt crisis
Probability	10%	60%	30%

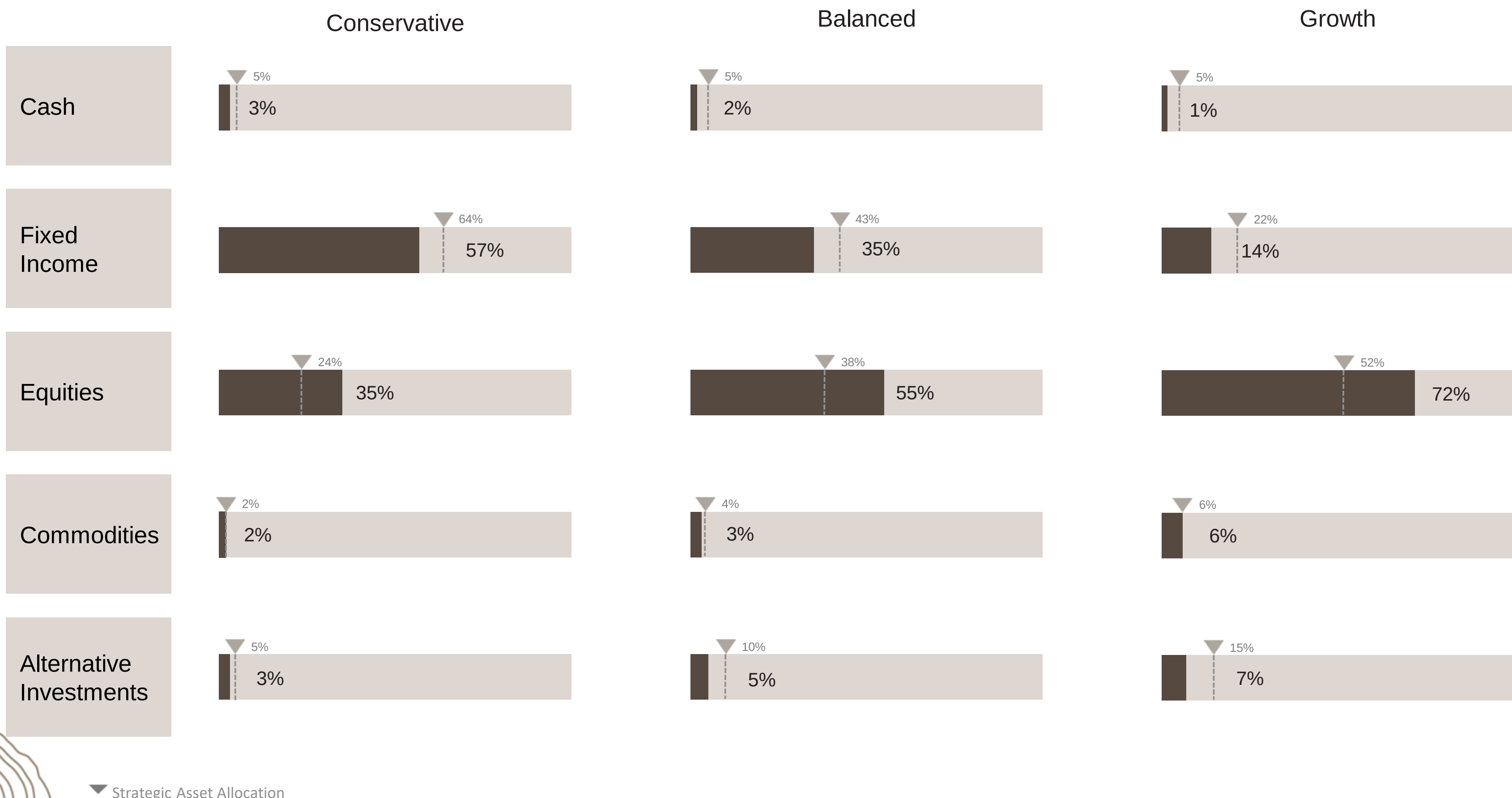
Short-term catalyzers

Fiscal stimulus in the US, improvement in macro-data globally, lower geopolitical tensions

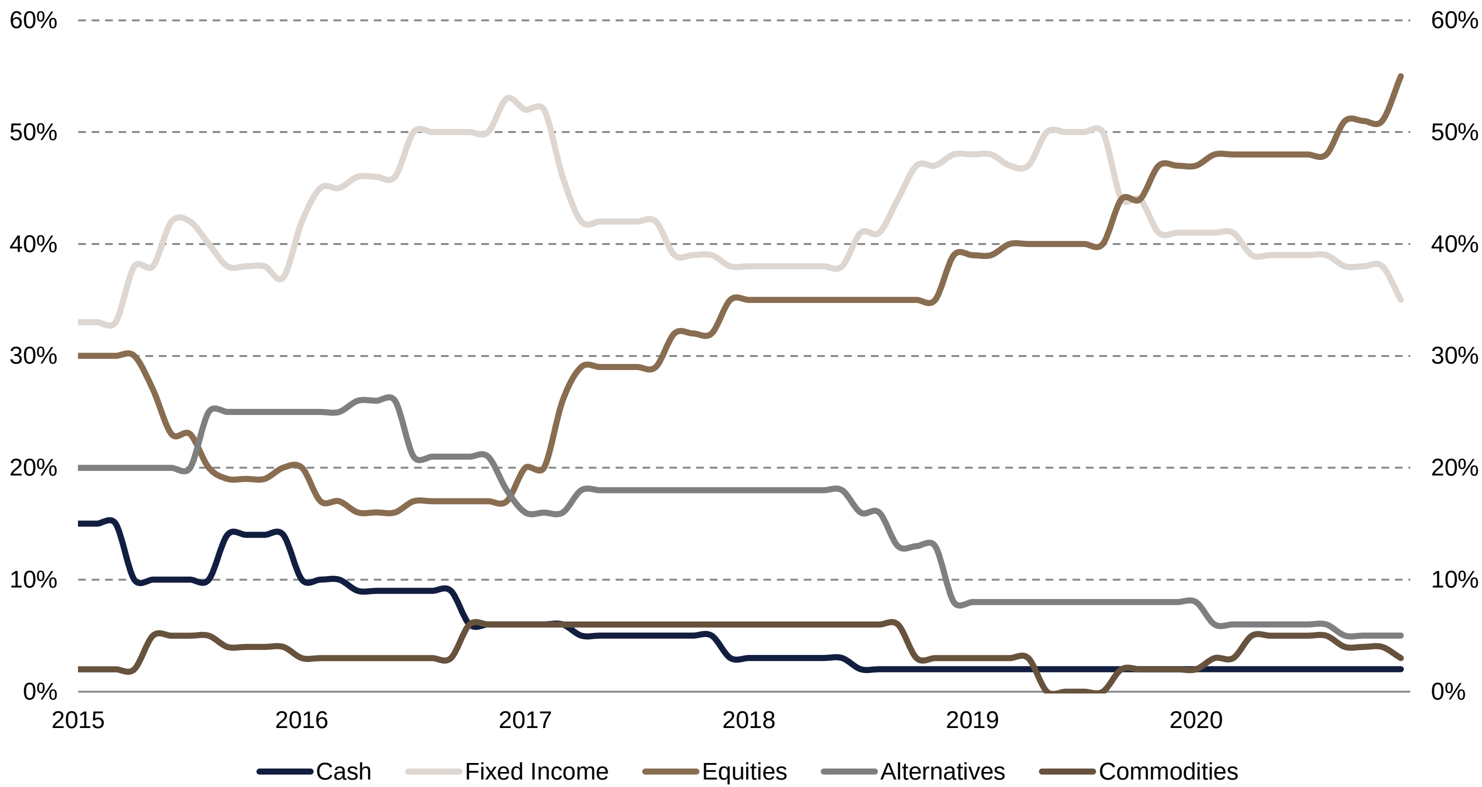
Other risks

Trade wars, Spread of populist political parties, China slowdown, Terrorism

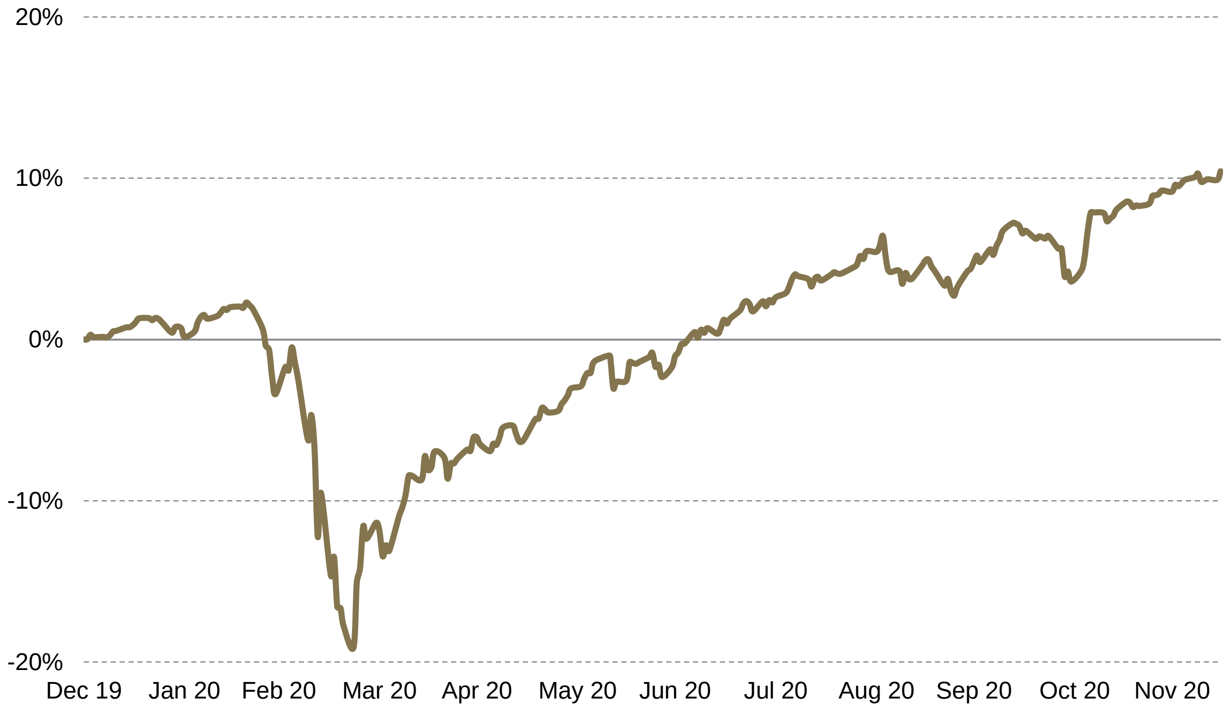
EWM Investment Profiles



EWM Model Portfolio – Asset Allocation evolution



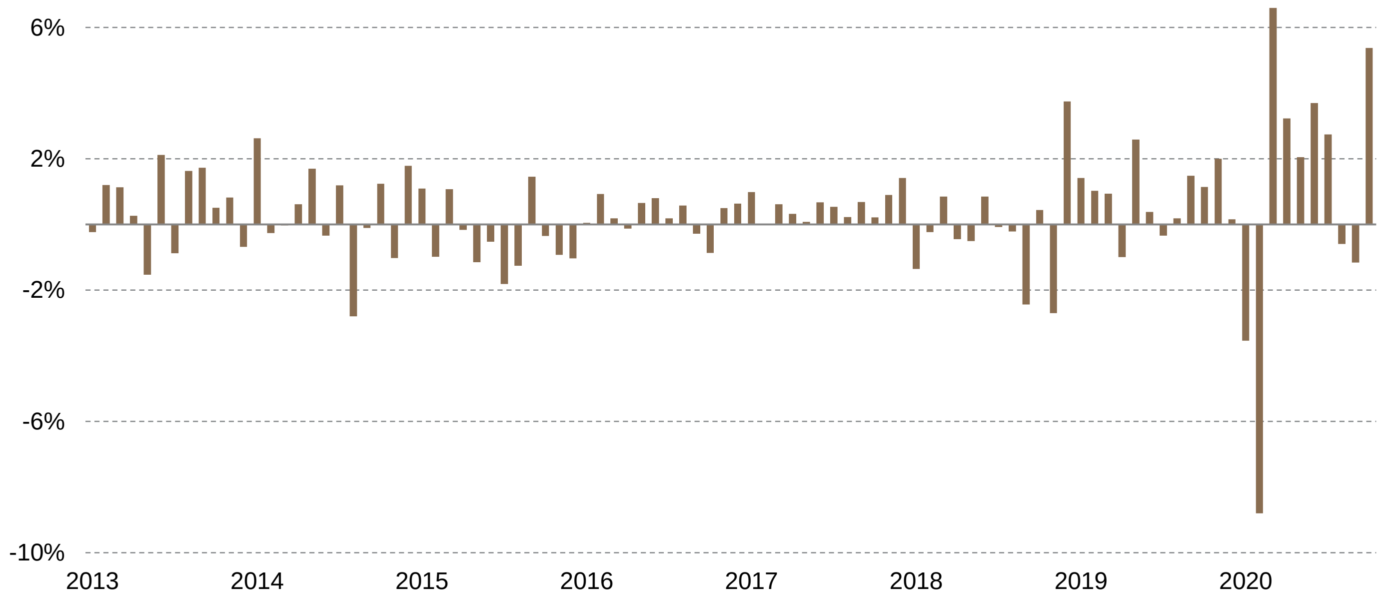
EWM Model Portfolio – Ytd performance



- **Total Return** (Ytd[1]): **10.43%**
- **Standard Deviation** (Ytd[1]): **15.52%**
- **Downside Risk** (Ytd[1]): **12.21%**
- **Sharpe Ratio** (Ytd[1]): **0.77**

[1] As of December 15, 2020

EWM Model Portfolio – Historical performance (1)



- **Total Return** (1 year[1]): **11.79%**
- **Total Return** (3 year[1]): **22.09%**
- **Total Return** (Since Jan 13[1]): **42.85%**

[1] As of December 15, 2020

EWM Model Portfolio – Historical performance (2)

	2013	2014	2015	2016	2017	2018	2019	2020
Return	9.58%	2.05%	-1.80%	1.57%	6.06%	-4.62%	14.67%	10.43%
Std. Deviation	3.82%	3.59%	3.67%	2.08%	1.45%	3.77%	3.78%	15.52%
Sharpe Ratio	2.54	0.58	-0.48	0.62	3.57	-1.70	3.49	0.77

Annualized Return: 4.58%
Annualized Std. Dev: 6.21%

[1] As of December 15, 2020

Boreal Balanced Portfolio – Historical performance (2)

	2013	2014	2015	2016	2017	2018	2019	2020
Return	9.58%	2.05%	-1.80%	1.57%	6.06%	-4.62%	14.67%	10.43%
Std. Deviation	3.82%	3.59%	3.67%	2.08%	1.45%	3.77%	3.78%	15.52%
Sharpe Ratio	2.54	0.58	-0.48	0.62	3.57	-1.70	3.49	0.77

Annualized Return: 4.58%
Annualized Std. Dev: 6.21%

[1] As of December 15, 2020

Edwards Wealth
Management AG
Switzerland

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