
In 2021, we will once more be talking about valuations, in all asset classes and for all sectors
PAG 62 Venture Capital with wind in its sails
PAG 68 Sustainability is also a must for AIM Italia
PAG 73 Real Assets, not just real estate
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Investments, it is time change your approach

The economic paradigm is no longer the same, and, in order to manage portfolios well, we must go beyond traditional asset classes.

Francesco D'Arco

It is important for investors who can allow for a medium-to-high risk profile, to be increasingly more aware that, in recent months, the paradigm that drives economies has changed. It is fundamental that we understand that 2021 will not be a carbon copy of 2020 on an economic level. The sectors that drove the economy last year will not necessarily be the leaders in the next twelve months. So says **Luca Riboldi**, Director of Investments at **Banor SIM**, which is asking private bankers to lead their customers towards a new world which, for starters, sees bonds abandoning their role as a defensive asset class. Plus, a cultural change is required in terms of ESG.

Technology, healthcare, ESG. Are these still the topics for 2021 or is it time to change our tune?

I do not think that these are the main topics for 2021. Sectors such as digitisation, e-commerce, renewable energies and electric cars have seen 5 years of progress in just 12 months, recording high performances supported by new professional and personal habits brought on by the pandemic. It will now be important to reflect on the trends that emerged in 2020 in order to understand how to consolidate them and turn them into long-term trends.

How can these trends be stabilised and become long-term opportunities?

Let's consider digitisation for a moment. With the pandemic, we all discovered remote working, an intelligent way of organising work, which proved to be highly productive, because once the full lockdown was over it pushed everyone to better manage journeys between home and the office.
In order to maintain this approach to organising our work even after the pandemic requires a significant digitisation process for Italy, which will require long-term investment. So, I expect more limited but also more stable and long-term growth compared to 2020.

So, what kind of performance can we expect in 2021 from the major topics of technology, renewables and healthcare?

They will still be relevant, but I do not think that they will perform better in 2021 than they did in 2020. They have come a long way, but it is not necessarily the case that all the companies in these sectors will grow. “Uncertainties” are emerging across the board.
Staying on technology, as I was saying before, the topic remains central, but we must choose carefully. The major players will maintain an important role in our lives and, even if they now have lower multiples than last year, they should, in some areas, manage the “regulator” risk. Basically, in 2021, we will once again be talking about valuations, which we had forgotten about last year. I do not mean that technology is now stuck in a headwind, but it is important to know that the wind is no longer as strong, so we must identify the true market leaders, those companies that are well managed.

In terms of technology, should we fear a bubble risk?
In reality, we are already in the midst of a bubble. In my view, there are companies at an inexplicable value (trading at over 15/20 times their turnover and losing money) and which will likely fall a great deal before returning to their real value.

Is this also the case for renewables and healthcare?
Renewables had already achieved unrealistic valuations during 2020, but a number of them still have attractive valuations in addition to being market leaders, Enel and ERG, for an example. Let’s say that the rule is to watch from a highly critical and selective perspective. It is no longer sufficient to merely follow a trend in order to make a profit.

In healthcare, given the ongoing health crisis, do you not think that there are similar opportunities to those seen last year, for example with technology?
On this front, there is often a valuation error linked to the conviction that the vaccines are driving the sector. This is not the case. On the contrary, a number of big pharma companies did not do well last year because they were negatively impacted by the interruption to checkups, the lower number of people affected by seasonal bugs and a long series of factors linked to the various national lockdowns. The real consideration to make for the sector is not how much it will profit from the vaccines; the turning point for the sector will be when we return to normality. Let’s not forget that, in Europe and the United States, enormous investments are required in this sector in order to improve many aspects of the hospital systems in individual nations. Again in this case, however, the rule for 2021 must be “selectiveness”.

Moving on to the topic of ESG, everyone now “boasts” an ESG label. How can we move from a purely commercial message/approach to a “cultural” one?
We are definitely facing a highly “fashionable” topic. But ESG investments are not a trend. Like Sir Ronald Cohen said some time ago, “Within 10 years, profit itself will be looked at as something dirty”. This is the genuine issue underpinning the ESG world. Those who only think about profit without considering the environmental aspect, human rights or a governance system are unlikely to have a future. A wider outlook is needed, one which goes beyond the “fashionable” approach.
For example, it is easy to say that a company that produces carbon has a low rating, but if 100,000 people work at that company, what is the most “ethically” correct choice? Should we be promoting the environmental issue to the detriment of the social issue? There is clearly no one answer, but it is necessary to closely assess every aspect in order to find a true balance between E, S and G.

How can we achieve this evaluation?
By going well beyond the social responsibility report prepared by a company. By overcoming the superficial approach that often accompanies those claiming to be part of the ESG world. What Banor does is to meet with companies, deepening our knowledge of them with a series of interviews that allow us to carefully assess the real approach of managers and companies towards ESG. People often fall into the mistake of only checking whether the company in question has taken insufficient action. But it is no longer the time to make decisions by process of elimination alone. We must reflect on a company's vision of the future. In this regard, I believe that the coming into force of the new SFDR legislation is essential for bringing cultural change in terms of ESG.

At this point, at asset class level, other than the world of stocks and bonds, which other routes should we take?
Let's start with considering the asset class of bonds, which are highly attractive for Italians. Is it truly a defensive asset class? Not any more, in my opinion. I do not believe that bonds are able to hedge inflation and so we cannot consider them to be defensive. However, they can still play an important role in portfolios, but the issues taken into consideration should be assessed carefully since they are not risk-free investments.

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Bonds do not defend and they are riskier than usual. So, what should we do to manage our portfolio well and protect our assets?
We are leaving behind over ten years of positive results on the equity and bond fronts, so I think that, today, maintaining a portion of assets in cash is, in part, a wise thing to do. Alongside more traditional investments in stocks and bonds, then, I would add 7-10% in commodities. I would also look at alternative investments.

What are you referring to when you say alternative investments?
In the first instance, I mean long/short funds, which are attractive because they hedge equities better. Since, in the last two years, valuations have been useless, we now need careful analysis work to find value and generate alpha through equity investments. But I see other two branches in the portion of the portfolio dedicated to alternative instruments.

What are they?
The first is private equity. This category includes instruments that require long-term investment and therefore guarantee portfolio stability, in a sense. The second branch is alternative M&A Arbitrage funds, a valid solution for those who do not want to only be exposed to corporate bonds, and these are instruments that, in recent years, have seen performance close to 5 percentage points with the same volatility as bonds. They are much less volatile funds than the world of corporate bonds. What is important is that, particularly, the investors who can afford to have a medium-to-high risk profile are increasingly more aware that, in recent months, the paradigm that drives economies has changed. The liquidity created by the central banks in response to the crisis caused by the pandemic is associated with an attempt to generate inflation in the system, because enormous public debt has been created in every country in the world. Now, governments and the central banks cannot afford for the cost of debt produced in order to bring economies out of the crisis to increase too much. So, I am expecting some form of control over the maximum return on bonds, thus leading to the importance of considering investment avenues other than the traditional asset classes. I think that this is the fundamental message to convey to private customers today.