

EDOUARD CARMIGNAC'S LETTER

Edouard Carmignac writes on current economic, political and social issues each quarter.

Paris, January 12, 2021

Dear Investor,

What an extraordinary year! Due to its violence, global reach and uncertain duration, the Covid-19 pandemic has both disrupted how we live and profoundly impacted financial markets.

We are of course distressed at the high price being paid by victims of the virus, in terms of their physical and mental health and the future of their livelihoods. But we must still try to assess how the pandemic is producing lasting changes in our way of life and the investment outlook. With that in mind, I'd like to review three key observations that I have conveyed in my three preceding quarterly letters.

I already argued back in April that the pandemic would soon surprise us as **an accelerator of history**. While it took ten years for e-commerce to rise from 5% to 17% of total retail sales in the United States, an additional 7% jump was recorded in the first weeks of this past spring alone. Similarly, the remote working arrangements previously tried out by just a few pioneering companies are now becoming an acceptable or even recommended practice. And as the prospects for a forthcoming return to normalcy grow increasingly dim, these shifts will become less and less reversible. We are thus likely to be conducting a rising share of our daily activities online: work, shopping, payments, gaming and even medical consultations.

In July, I emphasised **our refusal to accept insecurity** as a new paradigm in developed countries. Whole economies have been shut down in response to a somewhat mild pandemic when compared with plague or cholera. The risk of recession has been warded off by widespread zero or negative interest-rate policies and huge government spending programmes. Tackling the current crisis will

cost the wealthy countries close to an astronomical 10% of their GDP. Eradicating the public health menace will certainly clear the decks for an economic upturn, which should not, however, lead any time soon to a substantial reduction in fiscal spending. There are two reasons for this. Sluggish vaccine rollout and the virulent nature of Covid-19 are likely to ensure that the recovery will be gradual. In addition, governments will be concerned with income maintenance for the less fortunate members of society, who have been particularly hard-hit by the public health crisis. This is notably a major plank in Joe Biden's programme.

More recently, in October, I identified **the introduction of the notion of Immaculate Conception into finance** as one of the least expected changes brought about by the pandemic. Throwing all rules of fiscal orthodoxy to the wind, governments in developed countries have sent their budget deficits sky-high – and yet obtained the required funding with total impunity, hardly experiencing a dent in either their credit ratings or currency exchange rates. Will this state of bliss endure? Most decidedly not. Or, to be more precise, it will endure as long as the pandemic's effects are still with us. As long as all countries are affected by the virus in roughly equal measure, the twin imperatives of safeguarding public health and safeguarding employment will take precedence.

Ironically, equity and fixed-income markets will thus wind up fearing the end of the pandemic. The first signs of selling pressure on long-dated US Treasuries and the dollar already reflect investor apprehension over the sustainability of Uncle Sam's fiscal and trade deficits. Though there are still opportunities to be had in stocks and bonds, let's keep a level head at this time of market euphoria. Coming out of this pandemic will require at least as much risk management as coping with its unexpected arrival.

As this most unusual year gets underway, I wish you all the best and hope in particular that you will regain your former freedom in short order.

Yours truly,



Edouard Carmignac