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2021 – welcoming the new normal

On the markets, 2020 is ending on a more hopeful note than the one that prevailed during the year. Good news on the economy and coronavirus vaccines has pushed up both share prices and investor expectations. Next year, the full extent of the coronavirus damage will be revealed, and we will see how the economy fares without stimulus efforts. High expectations will pave the way for at least some disappointments as the markets adapt to the new normal.

The last investment year has offered something for everyone. Doomsayers predicting a market crash had their moment in the spring, when the coronavirus sent risk-laden markets into their deepest plunge ever. Yet those who believe in the never-ending growth of share prices have been rejoicing since the spring, as shares have made an exceptional rebound since fears of a coronavirus recession have eased, and gigantic money flows have pursued returns on stock markets. Over the whole year, shares will be bringing in a "normal" return of 5–10%. At the end of this "year of horrors", investors can look back on a massive rollercoaster of markets and emotions, as well as quite reasonable returns, now that even bonds are making money.

Will we be rid of the coronavirus?

The sentiment for the new year is clearly more positive than during the current year. This year, the coronavirus shook the whole world, which means the new year is all about bringing the coronavirus under control. If the coronavirus keeps wreaking havoc, there will be no lasting economic recovery. Hopes for a vaccine against the coronavirus grew during the summer, and the world finally received good news from a number of drug companies in November. They announced that their effective vaccines could be administered rapidly.

The news about the vaccines meant that the market effects of the second wave during the autumn have been modest. Investors have not been too concerned about the worsening situation recently, because they are confident that the pandemic will be put to rest once and for all next year. It will still take a while before the coronavirus is eliminated from the world, and there is still some uncertainty about the vaccines. However, the worst fears of a permanent plague are easing. Once again, science has proved its power to benefit humanity.

Life after the coronavirus

What will the post-coronavirus world look like for investors next year? Will the economy flourish as soon as the vaccine is distributed, or are we looking at a more long-term economic squeeze? These are the questions that will define stock markets in the coming year.

The coronavirus did less damage to the economy and the financial markets than feared. One major reason for the economic resilience was the massive support measures of unprecedented proportions taken by governments and central banks. The tab is still open for economic stimulus measures, because everyone agrees that an immediate crash must be avoided at all costs. This objective has been achieved very well.

However, more difficult times lie ahead next year, when the stimulus budgets are gradually cut. However, no drastic changes should be expected in the general direction of stimulus efforts. Money is still being printed, and governments are getting more deeply into debt, but the pace will slow. In this situation, we will see how firm the ground under the economic growth is. Will the economy find its own feet, or will it stall when support is gradually reduced?

Baseline scenario

Generally speaking, 2021 will start in a hopeful – if tense – atmosphere. The world is going in the right direction. Yet for the investor, this does not necessarily mean huge returns. If everyone thinks the world is recovering, this expectation is already reflected in stock prices. So our baseline scenario for next year does not expect very high returns on investments. If expectations are already sky-high, there is little room for positive surprises. Having noted this, despite occasional disappointments, we still expect shares, high-risk bonds and real estate to yield the highest returns for patient investors next year too.

Positive scenario

Interest rates are low and will remain low in the future, which means that investors will be seeking better profits from other markets. If the economy picks up, but stimulus measures continue at full throttle, money will continue to seek high-risk investments next year. The markets could give investors a positive surprise should the investment craze continue in a similar vein to this autumn's. In this bubble-forming environment, rising share prices would boost further growth, as more and more investors would rush to the markets in search of quick profits. This would mean great returns for next year, but risks associated with the bubble could also start to accumulate.

Negative scenario

On the other hand, we should bear in mind that economic development after the coronavirus and mega-stimulus efforts is an entirely new beast. There is a risk that economic damage will be greater than feared. For example, a wave of bankruptcies will freeze the economy as subsidies are cut. Even a mild recession would be enough to push share prices into a brisk decline, because investors are currently prepared for a significant improvement of the economy. Returns from low-risk bonds will not soar in this scenario either, but they would still offer the best returns if other markets go into the red. This year has been yet another reminder of how markets can surprise us. Good diversification remains an important way of balancing portfolios in every circumstance.

A power shift on the stock markets

We are entering the new year with asset classes in neutral weight. The good outlook is already largely priced into the markets, which means there are both positive and negative market risks. In the long term, shares still continue to be the most interesting asset class. Emerging countries seem the best-positioned on the stock markets. Damage from the coronavirus has remained limited in many emerging countries like China. Furthermore, the recovery of the world economy and trade will provide strong support for emerging economies. Valuations differ between countries, but emerging markets offer plenty of interesting and reasonably priced investment opportunities.

In addition to emerging countries, we favour shares that are lagging behind others in price development. US growth shares have been the stars of the year, but more traditional sectors that are sensitive to economic development were given a new boost in November. These value stocks have long dragged behind, but news of an economic recovery and vaccines has given them fresh momentum. The picking up of value stocks has given a boost both to European shares, which we raised to neutral weight in October, and to the selection of companies in many of our other stock portfolios.

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In fixed income, return prospects in relation to risks are not great. Interest rates have sunk to historic lows on a broad front, yielding little reward for risk taking. We are therefore continuing to use fixed-income investments mainly to stabilise our portfolios, and we are keeping eurozone government bonds, which have yielded strong returns this year, overweight. They benefit not only from investors pursuing returns in a low-interest rate environment, but from supportive purchases by the European Central Bank.

Best regards,

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