PVI – The Global Investment Newsletter

October 21st, 2020

The Upcoming US Presidential election

With the US Presidential election being only 2 weeks away, investors should position themselves cautiously. In the polls up to today, Mr. Biden is clearly ahead of the incumbent Mr. Trump. In the 2016 elections, Mr. Trumps victory came as a surprise to many Europeans, as the European media strongly favored Hillary Clinton and spun the news coverage accordingly. This lead to an underestimation of the power behind Donald Trump and a "surprising" victory. In the US many people were not so surprised – as Hillary Clinton was disliked by many voters who then simply turned to Donald Trump. The stock market futures sold off strongly in early European trading, when most traders were shocked that Donald Trump had won. But once the US traders woke up and saw the result, they started buying and the stock market started a big rally with the election of Donald Trump, who – running for the Republican Party – had promised to bring tax cuts to corporate America.

This time around, we think that the chance that Joe Biden will win the election is clearly higher than for Trump to win. The reason is that now Mr. Trump's rhetoric and tactics are much better analyzed by the old political establishment (Biden is their candidate) and their strategists. Further, most importantly the still-ongoing Corona-Virus crisis and the mismanagement of it will be overshadowing Mr. Trump's campaign.

Further, it seems likely that the Democrats will rule Parliament and Senate and could enjoy a strong presidency for at least 2 years.

Implications of Biden winning the elections:

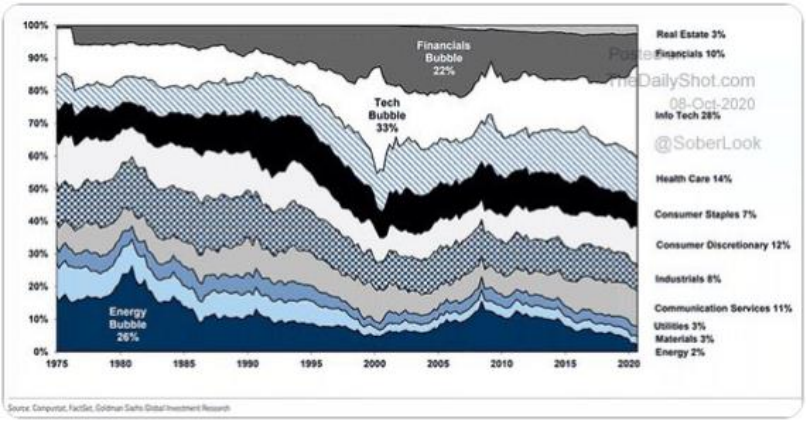
A shift to a more democratic-looking economic policy would include:

- Partial reversal of the Trump tax cuts for corporations
  Even a minimum tax of 15% for large companies is in talks
- Recommitting to the global warming thesis and strong incentives for Renewable Energy
- A more (rhetorically) diplomatic approach in relation to China
- More fiscal spending, more Coronavirus-related stimulus

In light of the already elevated levels of the S&P 500 and the especially the FAANG basket stocks, the impact on asset prices is therefore not easy to foresee, since the failed stimulus packages could start to come in, but – on the other hand – the tax increases would immediately start weighing on market multiples.

Also, hopes of an end to the trade war could prove wrong, as Donald Trump actually had even Democratic support for his tariff increases. The rhetoric will change and this could bring temporary relief, but we foresee that the rising economic and also military power of China will more and more clash with the dominant status of the US. Therefore the trade rivalries will be with us for many years to come.

While the oil&gas sector would not welcome Mr. Biden, we would still be looking to buy such investments after the election with a 2-3 year horizon. Energy is now down to the lowest S&P500 weighting in decades and drilling has totally collapsed due to the corona crisis. Therefore, there could be an up cycle starting in the energy shares soon.



Source: Liz Ann Sonders, Twitter

Also, renewable energy investments should benefit from Mr. Biden becoming president. While hydrogen stocks (such as Ballard Power) have had enormous run-ups over the last few months and should be traded carefully due to their lofty valuations, the general trend for clean technology looks very favorable. We will highlight opportunities as they come along.

Precious Metals should – in general – be in uptrend for the next few years. We note here, that a positive correlation with the S&P500 has more and more formed, which means, that any set-back in the S&P500 would also lead to a set-back in precious metals. If such were to occur in November, we would take the opportunity to buy.

Trading Recommendations:

With the elections approaching, we are still taking a more careful approach and will initiate only one new position after having exited all positions over the last few weeks.

Bayer AG (WKN: BAY001, ISIN: DE000BAY0017)

A good trading opportunity has formed in shares of Bayer AG, the German company that took over Monsanto a few years ago.

Bayer is world leader in crop seeds and crop treatment and also has a large pharmaceutical operation. The stock has been under pressure ever since they bought Monsanto for a high price (in hindsight). The lawsuits brought up against Bayer in conjunction with the weed killer Glyphosate (which is claimed to cause cancer) have lead to several lawsuits which are now nearing final settlement for around 10 Bio. Euros (or about 2x annual net profits). The recent cut in outlook for its Agri-Business, lead to a final sell-off into the 45 Euro range. The shares have also been sold by dividend-Investors who might have been spooked by the announced lowering of the dividend-payout. Beneath all that short-term issues is a highly profitable company, which is generating enormous free cash flows. In a sum of the parts analysis, even the most cautious analysts will value Bayer AG at minimum at 70 Euros per share. More bullish analysts have valuation targets of over 100 Euros per share.

Source: www.finanzen.net

While analytical calculations are one thing – which may or may not hold true over the long term – the stock has now so much negativity discounted into it, **that we foresee a rebound in the stock price over the next 2-6 months into the 55 – 65 Euro range, giving us a potential gain of 20 – 50%.**

This should be driven by **1)** good news about the final settlement of the lawsuits **2)** potential resurgence of activist investors such as Elliott who will push for a break-up of the company and **3)** the realization that the weakness in growth in the Agri-Business is only temporary and is driven by the Corona-Crisis which lead to falling corn prices this summer, which in turn weighted on farmers budgets.

With a current P/E ratio of 7 (about 9 including the lawsuits settlements), the stock seems much undervalued for a world market leader with growing secular trends. **Looking out longer term, we foresee the stock trading into the 70ies and even 80ies (in a 2-3 year time-frame).** As such this trade seems to be a low risk entry with multiple profitable exit opportunities.

Traders experienced in using knock-out certificates may use such with a barrier at around 35 Euros (e.g. WKN: HR25P7, ISIN: DE000BAY0017, emitting bank: Unicredit). Options are currently quite pricey (due to the stock's recent volatility spike). Still option traders could look at the options issued from Unicredit (WKN: HZ8JGG, ISIN: DE000HZ8JGG9, strike: 34 Euros, expiration 15.12.2021)

Trading Recommendations:

Buy Bayer AG, Current price: 44 Euros,

Target 55-65 Euros, Timeframe: 2 – 6 Months, Stopp/Loss 35 Euros

Current Model Portfolio: (starting value on 01/01/2020: 100.000 Euro)

YTD return: +23,25%*

98.250 Euro Cash

25.000 Bayer AG (purchase price: 44 Euro)

123.250 Euro Total Value as of 10/20/2020

*the model portfolio assumes a flat tax rate of 25% on profits generated