DECALIA

Wealth Management
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INVESTMENT INSIGHTS

MONTHLY ISSUE #76 | 1st May 2021

THE NEW KID ON THE BLOCK

EDITORIAL VIEW

The new kid on the block

- NFTs could be more than just the latest "get rich fast" craze
- The three big auction houses are embracing the concept…
- … boosting the recognition (and market value) of digital artists

FAANG, TINA, SPAC, PIPE, FOMO… you thought you were up to date on Wall Street acronyms? Well, here's the latest one to be making headlines: NFT. Which stands for non-fungible token or, in layman terms, data stored on the blockchain certifying that a digital asset is unique. Beyond the current buzz, could NFTs, which in effect serve as a bridge between the world of cryptocurrencies and more mainstream markets such as art, entertainment or sport, be the next step in the blockchain revolution?

A year ago, NFTs were known to only a (lucky?) few, essentially crypto enthusiasts and gamers. It was really with the first Christie's auction, mid-March, that saw US graphic designer Beeple's monumental collage of 5000 daily digital pictures sell for a whopping $69 million, that the NFT market gained a much broader audience. By some estimates, total transactions have now breached the $1 billion mark.

What distinguishes NFTs is their uniqueness, a feature made possible by blockchain technology. Which in turn explains why, although just about anything can be (indeed is) sold in this form, digital art is a prime candidate. For the past few decades, digital creators could not monetise their work because it was too readily duplicable. With NFTs, they have gained a status more at par with traditional painters or sculptors. Collectors are assured of the authenticity and provenance of the works they buy. With one important difference though: digital images generally remain visible on the internet, even when sold as NFTs. Put differently, buyers get the thrill of owning a unique piece – and hope that it will soar in value – but not the exclusivity of exposing it.

The original use of NFTs was in the gaming industry, where various kinds of artifacts tend to be collected. *CryptoKitties*, in particular, a game by Dapper Labs that consists in collecting, breeding, adopting and selling cartoon cat images, helped popularise the concept. NFTs were then also embraced by the sporting world: the NBA's officially licensed *Top Shot moments* video clips – shaped as the sports cards kids used to collect – have for instance garnered more that $390 million since their launch last October.

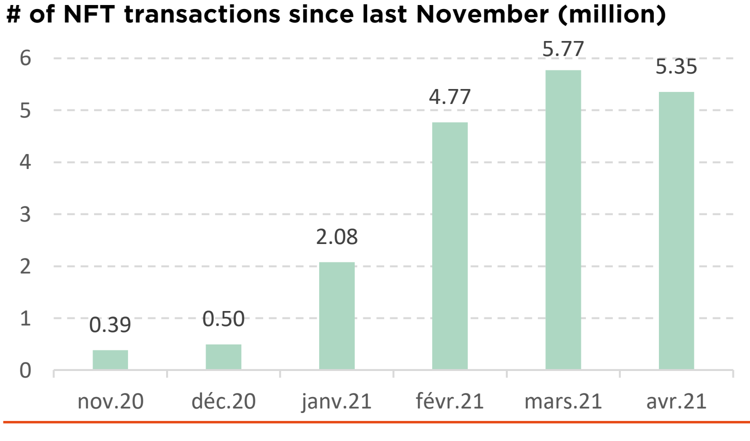
Like any traditional collectible, NFTs are not really about rational investing, but more about having a (sometimes expensive!) crush. Scarcity obviously plays a part in pushing up values and the pandemic, by keeping much of the global population stuck at home behind computers for months on end, no doubt also contributed to fuelling the mania. The recent IPO of Coinbase, the largest US cryptocurrency exchange, also proved particularly opportune.

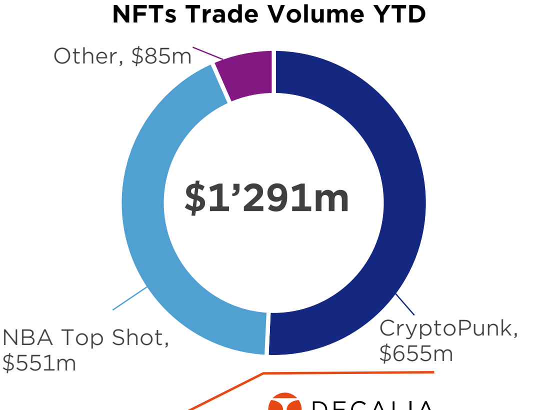
Beyond dismissing NFTs as yet another bubble, detractors point to the climate-unfriendly nature of the blockchain, which consumes huge amounts of computer power. Concerns are also voiced about the legislative framework falling behind the curve, about potential hacking, and about the barriers to entry – NFT platforms take a cut on sales and require a degree of tech savviness.

This mix of excitement and concerns swirling around cryptos, NFTs and other blockchain related "instruments" is reminiscent of the advent of the internet three decades ago. At this point in time, no one knows how all this will develop. But it could just be that NFTs go down in history as an important milestone in the blockchain revolution and eventually extend to many other areas, including healthcare or insurance. That said, interested investors, or should we say speculators, have few direct means today of gaining exposure. Save perhaps for *Aavegotchi*, a cryptocurrency that lies at the very intersection of decentralised finance, gaming and… art.

Written by Hussein Nassereddine, Portfolio Manager of DECALIA Muse

GRAPH OF THE MONTH





Complacency, what else?

- US growth momentum is peaking, watch out for a European catch-up in Q3
- Virus mutation, policy errors and excessive optimism are still the main risks
- So, sell in May? Given the low volatility, tactical hedging seems wiser

Global daily new Covid-19 cases have risen to record levels amid a strong resurgence in some populous EM countries, while the situation now appears under control in DM. Even though we expect Europe to lift most restrictions before July, the worldwide situation will remain challenging for as long as the virus continues to spread/mutate.

Turning to the economic backdrop, global growth remains strong but uneven, led mainly by a roaring US economy and booming manufacturing sector. Services activity is resilient despite the lockdowns, with an improving dynamic. Europe stands to accelerate strongly in Q3 – and even outperform the US in H2 – as its economy re-opens and services catch up. At this point, we are not concerned by China's slowing momentum, it being deliberately orchestrated by policymakers to bring credit growth back in line with nominal GDP growth. The situation of most other EM is more challenging and will remain a worry until the pandemic has been brought under control.

Overall inflation rates are moving up because of base effects. We expect this to be only a transitory trajectory, with a return to a more subdued trend after the summer. That said, risks do remain tilted to the upside given the accommodative stance in DM and currency depreciation risks in most EM. Speaking of central banks, we fear that the ECB may soon appear less dovish than the Fed, the latter having deliberately opted to fall behind the curve.

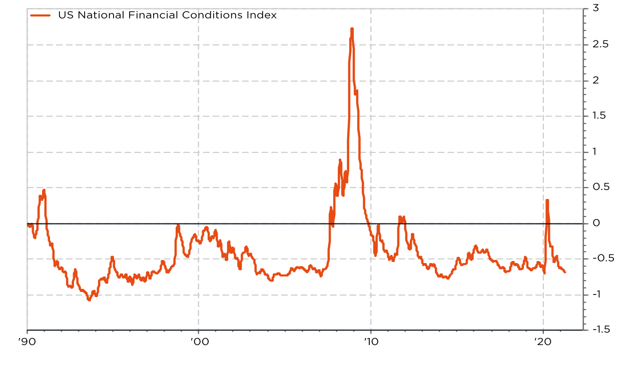
On markets, performances since mid-March, both across and within asset classes, have generally been positive and less polarised. The reflation trade has taken a breather after the strong run that begun in November. A second leg could take place soon, when Europe (and EM) re-opens. In the meantime, the exceptionally favourable narrative, combining a sharp recovery in earnings, historically easy financial conditions, an accelerating vaccine rollout, ample liquidity, strong corporate and household balance sheets, and pent-up demand expectations, remains in place, pushing down the equity risk premium and – obviously – inducing complacency. Admittedly, excessive optimism represents a risk but, in and of itself, says nothing about when the markets will turn south. In our view, outside of a few specific segments that trade at extreme multiples, valuations are not excessive. Still, given the current low volatility levels, we are again considering tactical hedging strategies (derivatives) on an opportunistic basis.

All told, we maintain a pro-risk stance in our asset allocation. In particular, we continue to favour equities (slight overweight) over bonds (underweight). During the past few months, we have reshuffled our equity allocation, adding selective satellite assets in order to recalibrate sector/style biases towards a more cyclical positioning, such that portfolios be able to better withstand further market rotations typical of a reflationary environment. Within fixed income, we maintain a contained target duration, alongside a relative overweight of credit.

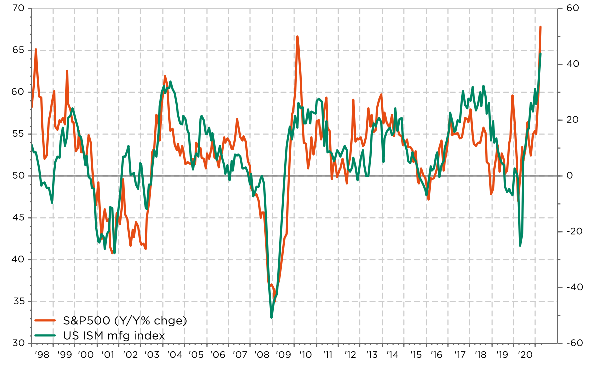
Elsewhere, we confirm our underweight on gold, as the inflation upmove will be short-lived. And we retain a near-term cautious stance on the greenback: its relative rate and growth advantage will not last forever, while the US twin deficit is likely to stay a burden. We also remain cautious on EM currencies (outside of Asia), yield differentials and relative cheapness not being sufficient to offset inherent risks. Conversely, AUD prospects seem more encouraging: it is relatively cheap, offers the highest 10-year rate among AAA issuers, boasts sound structural fundamentals and may continue to benefit from rising commodity prices.

By Fabrizio Quirighetti, CIO, Head of multi-asset and fixed income strategies

US Financial Conditions: Take It Easy... Again



US ISM mfg index and S&P500 (Y/Y %)



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External sources include: Refinitiv Datastream, Bloomberg, FactSet, Dappradar, The Block

Finished drafting on 30 April 2021