DECEMBER 2019

Roadmap 2020

Will the bull continue to run?

Yes, most of the time

NORDIC INVESTMENT PARTNERS

Disclaimer

This document and its contents is for informational and educational purposes and should not be considered investment advice

There's no warranty for accuracy, completeness or timeliness in the information. As such there's no liability for errors, omissions, misuse or misinterpretation of any information contained in the document

It is subject to business confidentiality and may not be made accessible or handed out to third parties without the consent of the Nordic Investment Partner

Violations of the provisions of business confidentiality may result in sanctions being imposed

2020 roadmap summary

Summary roadmap for 2020

Roadmaps can be quite static as the route you see on a map is much different in reality. Without roadmaps it's difficult to navigate. A financial market roadmap gives directions, but you have to be open-minded to change route if road conditions or weather forecasts change substantially

1. Global economic activity to continue a good 3% pace with Europe around 1%, North America at 2% and Asia at 4% i.e. **the road is good**
2. Interest rates and inflation to stay at current historically low levels i.e. **fuel is affordable and plentiful**
3. Corporate performance is good and moderation on investments in 2019 could lead to higher activity in 2020 as trade jitters fade. Earnings in general should be able to grow 5% after a mild earnings recession in 2019 i.e.. **the vehicles are in good shape**
4. Valuation expansion will be a smaller driver in 2020 than in 2019, however low interest rates will continue to motivate capital to move from deposits and bonds towards equities i.e. **the price of vehicles is decent and there's buyers**
5. Stock markets are expected to provide 7-13% return in 2020. In a situation with negative interest rates a massive capital flow towards equities could result in a 15-20% return year i.e**.** **a good stretch of road lies ahead**
6. Risks factors that can trigger a major decline is obviously a recession or mistrust in the financial system. Both are slow moving events so there should be plenty of time to react. Another medium speed factor is higher interest rates; they can reverse the capital flow to stocks. In the last 50 years there has been 3 episodes of 40%+ declines and 9 episodes of 25%+ declines (MSCI World). A major decline has been absent since 2011, so if declines are evenly spread it's high time for a 25% episode in 2020 or 2021 i.e. **be prepared for bad weather or road works**

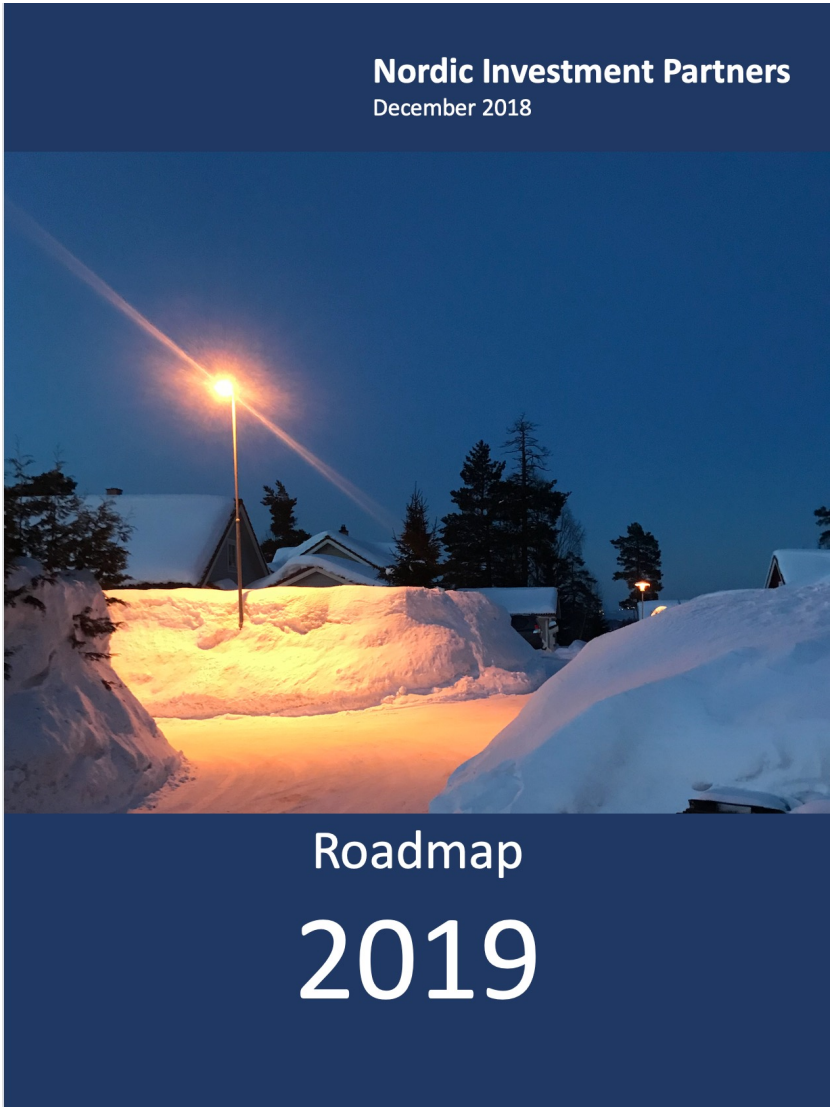
2019 roadmap and what actually happened

The roadmap for 2019 (from mid-December 2018) assumed 9% return with good road conditions, with the cost of driving a bit up, but nothing serious. It also assumed the vehicles being in good shape and good value of vehicles as they where not expensive. The obstructions for the year were recession fears in US, China slowdown, the dysfunctional Europe continuing to make trouble and the obvious trade war and Brexit jitters. You find 2019 roadmap here

Europe and US were computed for 9% returns, while Asia was for 3%. The outcome was above 20% returns and driven by higher valuations as bond yields declined to unprecedented lows.

Corporate earnings came in below expectations and a mild earnings recession was observed in 2019, but lower interest rates as well as increased likeliness of constructive outcome of various geopolitical agenda's lifted sentiment in the second half of 2019

In 2019 a lot of investments and projects where put on hold due to trade war and recession uncertainty. And inventories were kept low. Things are starting to clear up in the second half of 2019, which could feed into faster economic pace in 2020 as pent-up demand is released



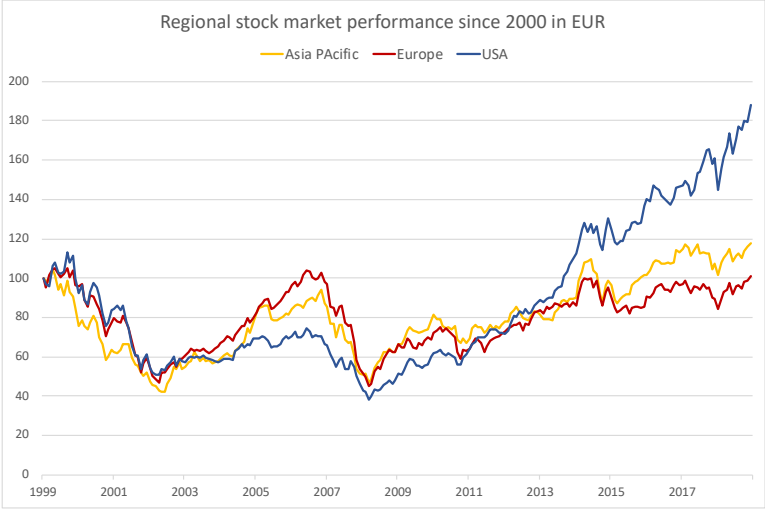
Performance of key assets

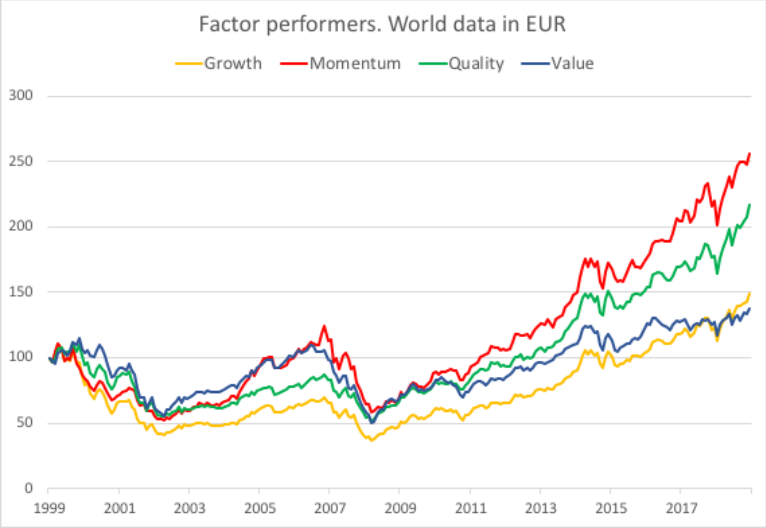
Regions
USA has been the clear winner in the 2010s. In the aftermath of the financial trouble in 2008 US reacted fast and coherent. In 2014 the US market reached the peak from 2000. In the latter part of 2010s US businesses have benefitted from aggressive capital discipline in a low interest rate world; stock buy backs, accretive M&A and a successful dozen of high growth global digital titans have boosted US stocks

Asia has some formidable tech companies but only in 2016 Asia managed to pass past peaks.

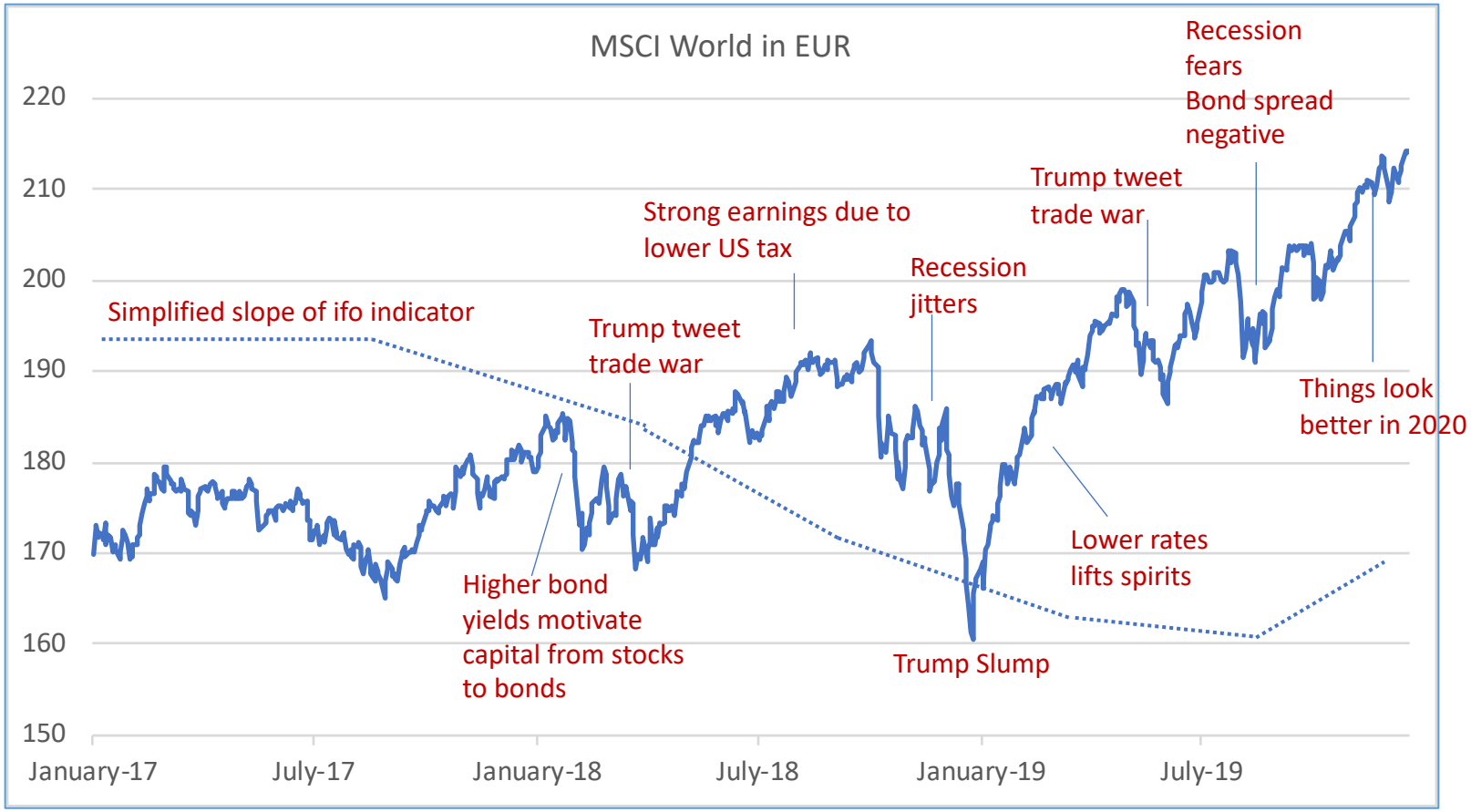
Europe with the EU setting limits on budget deficits has had a decade with low growth, troubled banks and moderate exposure to future digital growth areas has kept European stock prices below the 2000, 2008 and 2015 peaks

Factors
In the past the main factors where Growth and Value. As data has become better all sorts of company profiles have been factor identified. For simplicity just the most popular are shown to the right. Momentum has been very successful in 2010s. It's a simple strategy of being invested in companies with rising moving average stock price as the key selection criteria
The clear message is Momentum factor seems to work best and it's probably a function of more and more computers do the investment work.





The run up for 2020 in one chart



Key investment view towards 2030

Economic pace in 2010s have been highly dependent on fiscal and monetary stimulus provided in the aftermath of the 2008 crisis. The stimulus have however created imbalances such as government debts. This will probably continue even as it gets beyond sustainable in some countries

Global economic growth has been declining from 6% in 1960s to around 3% in late 2010s. Productivity and population growth points towards lower economic growth in the coming decades. The underlying growth in global affluence will however continue and with Emerging Markets in lead as those economies grow double the speed of developed markets

There's nothing wrong with modest GDP growth, but many investors have been accustomed to 8% annual earnings growth, while the realistic forward growth is more likely to be around 4-5%. Dividends of 2% comes on top. Annual swings are likely to remain in the 15-20% interval, so the occasional declines will continue

In an investment world on those conditions **Advice Capital Vision Fund** focus on identifying companies and business clusters with unique multi-year structural growth drivers and then invest in these when growth/profitability/valuation triangulation justifies it. The investment focus in Advice Capital Vision Fund is on identifying, holding and harvesting multibaggers based on these principles. Good stewardship and ESG applies to the companies invested in.

The traditional business and inventory cycle still applies, so from period to period growth and inflation will change. In a world with evermore data and analytics the efficiency of eco systems will likely reduce the magnitude of economic swings as end-to-end value chains reduce slack and inefficiency. Risks of financial mis-allocation of capital is the same

Middle of the road forecasts for 2020

Asset	Price Dec 2019	End 2020 objective	Comment
MSCI World	560	600	Consensus is for 9% EPS growth, which seems too optimistic. With 5% EPS20-21 growth to 33.50$ and 36.80$ and a 16.0x multiple its 10% return objective
S&P500	3.220	3.400	EPS20 of 172$ and EPS21 of 184$ with an 18.5x multiple gives objective of 3.400 plus 1.8% in dividends for return of 8%
Stoxx600	418	465	EPS20 of 28.40€ and EPS21 of 30.70€ with an 15.5x multiple gives objective of 472 plus 3.4% in dividends for return of 14%
MSCI Asia Pacific	170	185	Lower P/E of 15x due to governance issues, but still 11% price upside plus 2.5% dividends is 11% objective
$/DKK	6.75	7.00	US economic pace and interest rates higher than in Europe, so flows still towards USD
US 10 year bond yield	1.92%	2.25%	Activity levels higher. Could motivate stock capital flows to stall
German 10 year bond yield	-0.25%	0.00%	Europe growth pace slow, so stimulation needed into the 2020s
Brent oil	66.00$	65.00$	Increased supply from Norway, US and Brazil match a slight increase in demand. Strong economy lift it 80$

All data from 21 December 2020

Risks and upside surprises

One thing is a forward road map. Another thing is how things unfold. The factors that can really move things in a big negative direction can be condensed down to three factors;

1) Recession in economy or earnings
2) Valuations gets out of sync with reality and then normalize
3) Shock to the system like war, terror, epidemics or lack of trust in financial system

Things to look out for in 2020 are;

1. the US trade term negotiations with China and Europe. If they are constructive it's fine. If not it's a game changer.
2. US election and the Democrats moves
3. Global debt is getting unsustainable in several places, so monitor ability to maintain payments and credit risk movements
4. Labor markets are tight, so wage increases will hold earnings growth down
5. And obviously keep an eye on economic pace

Upside surprises

Event	How it unfolds	Action plan
Global stocks rise more than 20%	In 2019 investors realized the force of very low interest rates have on stock market appetite. 2020 sees more of the same traffic	Stay fully invested. If valuations gets above 25x earnings be careful
Investors realize interest rates will be very low for ages	Demographics and productivity growth suggest we're in long term patch of lower economic pace. Assets with positive return profile gets even more flow	Sell bonds, remove deposits in banks and invest in real assets and stock market
Economic pace picks up	Inventory levels are low and lots of projects have been put on hold in 2019. As clarity emerge business show inventory increases and start delayed projects	Cyclical sectors such as automotive, materials and consumer durables start to perform. Load up in those
Geopolitical uncertainty is reduced	Since Ukraine issues in 2014 the global geopolitical climate has deteriorated. Constructive dialogue and communiques create a sense of better visibility	Less tensions lowers risk and hence gives more fuel for Emerging Markets assets. Oil will flow more freely so will decline in price
Political agreement of lower carbon footprint	Political leaders unexpectedly agree on path and provide economic motivation and means for massive investments	Go long all companies providing renewable infrastructure equipment and services

Risks

Event	How it unfolds	Action plan
Global stocks decline more than 20% (version 1)	US want to change the terms of global trade and do not create a constructive framework with China, Europe and Americas	This risk has been cooking for a while, but if it escalates; have zero exposure to exporters and businesses with significant part of activities exposed to USA
Global stocks decline more than 20% (version 2)	The economy overheats and the central banks put on the brakes. Interest rates rise and motivate capital flows back to bonds	This will happen slowly so reduce equity exposure and increase cash and bonds that no longer have negative yields
Global stocks decline more than 20% (version 3)	Global government debt is record high. If ability to repay becomes a worry point a massive financial crisis could occur	This is a glacier speed phenomenon. But when glaciers calve its noisy and violent and you stay far away
Financial market collapse due to algorithms and robot trading running out of control	Daily trading volume is dominated by automated trading algorithms. On top comes various AI asset allocation operators primarily using momentum and trend signals	This can happen without warning like the 'flash crash' in 2010. Stock exchange authorities must pull the power plug from all connected computers and stop trading activities
Epidemic, cyber attacks and solar storms crate major havoc	Epidemic happen relatively slowly, the others just happen	You can't prepare for this, so just have it as a distant blip on your radar
Geopolitical upheaval	Unpredictable news from North Korea, Venezuela or increase in China/India trade issues	Will happen with short notice and will increase risk premiums. Evaluate the facts before making major decisions

Always remember that the biggest risks are the ones you didn't imagine

ROADMAP IN MORE DETAILS

NEXT BIG THINGS FOR 2020s

Traditional economic forecasts

Global growth was expected at 3.3% by the beginning of 2019. As the year progressed it was clear that the uncertainty related to trade war, Brexit and a volatile political agenda had its impact on sentiment.

Companies delayed new investments and projects, they reduced inventories and consumers got a bit more cautious.

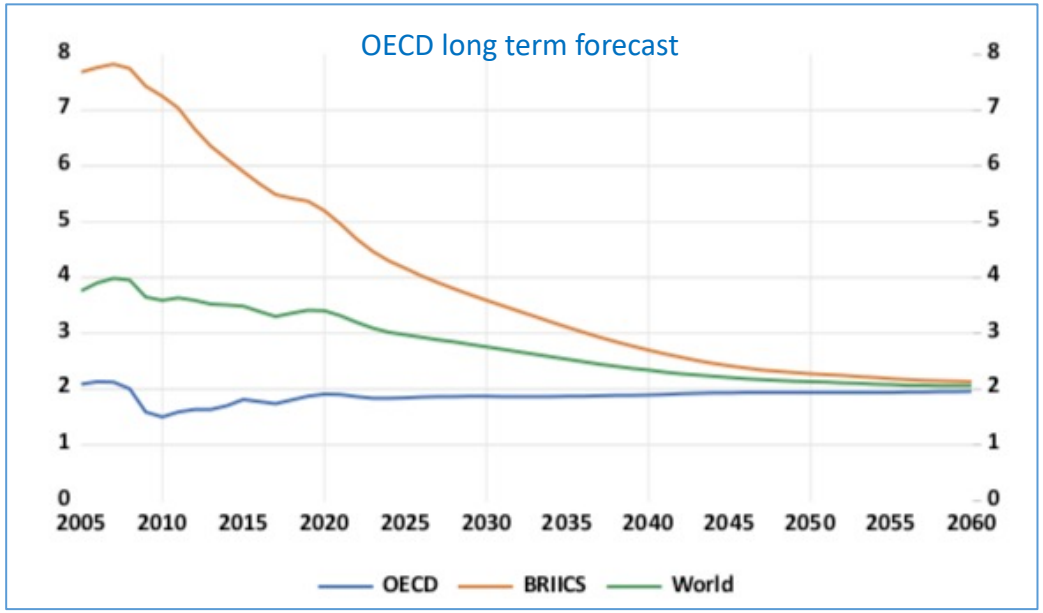
At the end of 2019 it looks like a 2.9% growth year and the 0.4%-point reduction equals 340bn $ or an economy the size of Denmark.

OECD and IMF see a steady pace around 3% for 2020 and 2021. There could be an upside surprise if delayed business investments are activated.

The long term view is for lower economic growth as explained on slide # 6. And OECD provides a rough roadmap in their 2060 projection

Key economic indicators	Size	2017	2018	2019	2020	2021
US GDP	20.5trl$	2,4	2,9	2,3	2,0	2,0
Euro area GDP	19.8trl$	2,7	1,9	1,2	1,1	1,2
China GDP	13.6trl$	6,8	6,6	6,2	5,7	5,5
Global GDP	85.8trl $	3,7	3,6	2,9	2,9	3,0
Inflation rates						
US inflation		1,8	2,1	1,5	2,1	2,1
Euro inflation		1,5	1,8	1,2	1,1	1,4
China Inflation		1,5	1,9	2,5	2,2	1,9

Source: IMF and OECD and annual change in percent



Other forecast shaping the world

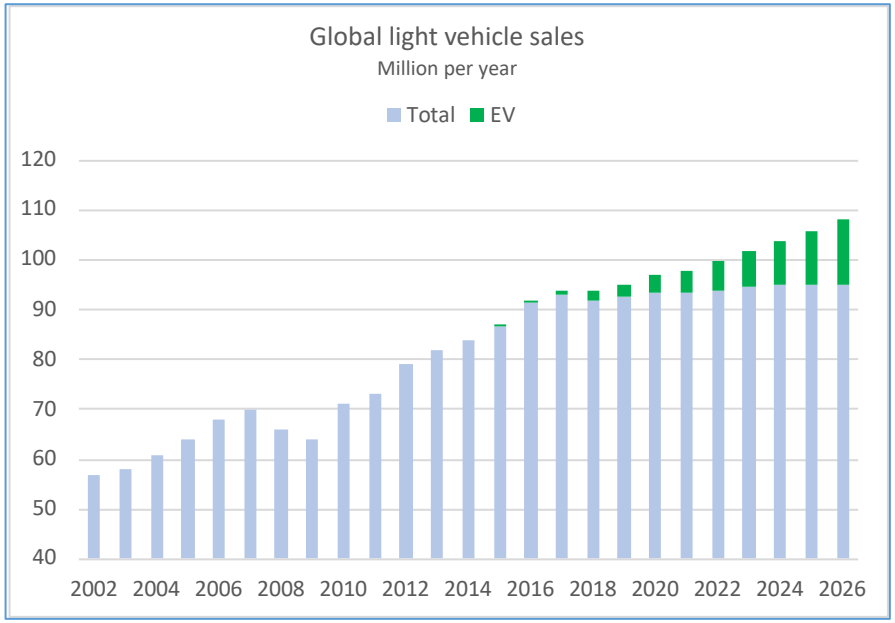
Item	Measure	2015	2016	2017	2018	2019	2020	2021	….2025
Smartphones	Units m	1.298	1.470	1.458	1.457	1.480	1.500	1.525	1.650
Global light vehicle sa	Units m	90	92	94	94	93	96	98	108
Semiconductor sales	USD bn	335	339	412	469	423	448	475	600
Data center traffic	Zetabytes	14	18	25	33	40	52	68	175

Economic activity is not always caught in useful way in statistics. However, tangible data like smartphone sales, car sales, data center traffic and semiconductor sales serves a better picture of how things develop in 2010s and 2020s

As example; newspapers are in decline and digital media increase. Overall media use is up, but the value added from news print is fading and replaced by more intangible services.

2020 will mark the year for wider usage of 5G communication and this could trigger a faster than expected replacement cycle of smartphones. That is not part of the estimates for 2020 and can surprise on the upside.

Also, many car owners have probably delayed buying an electric vehicle so the many new models coming to market might trigger a faster replacement cycle. However, various survey suggest traditional vehicles will continue to dominate the roads



Source: IHS Markit

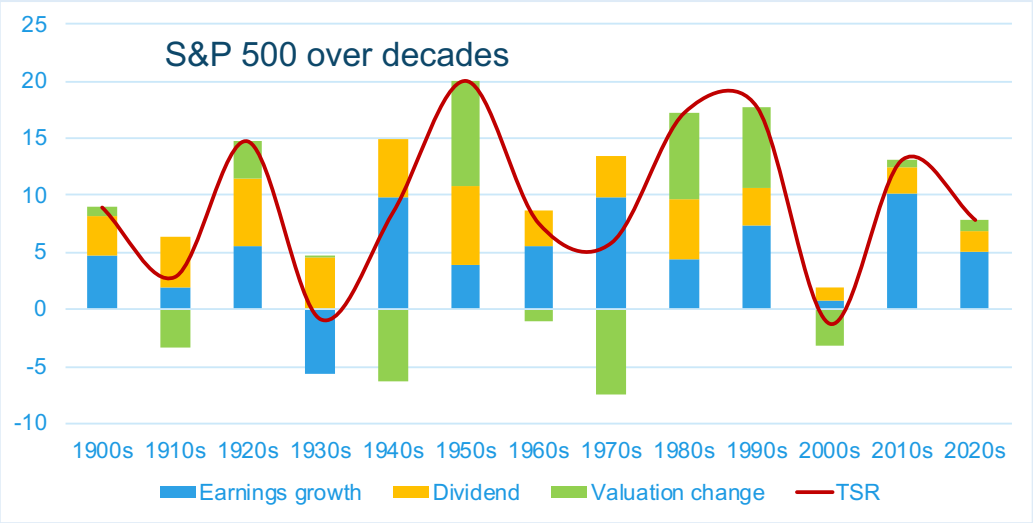
USA stock market has provided 9.4% annual return since 1900

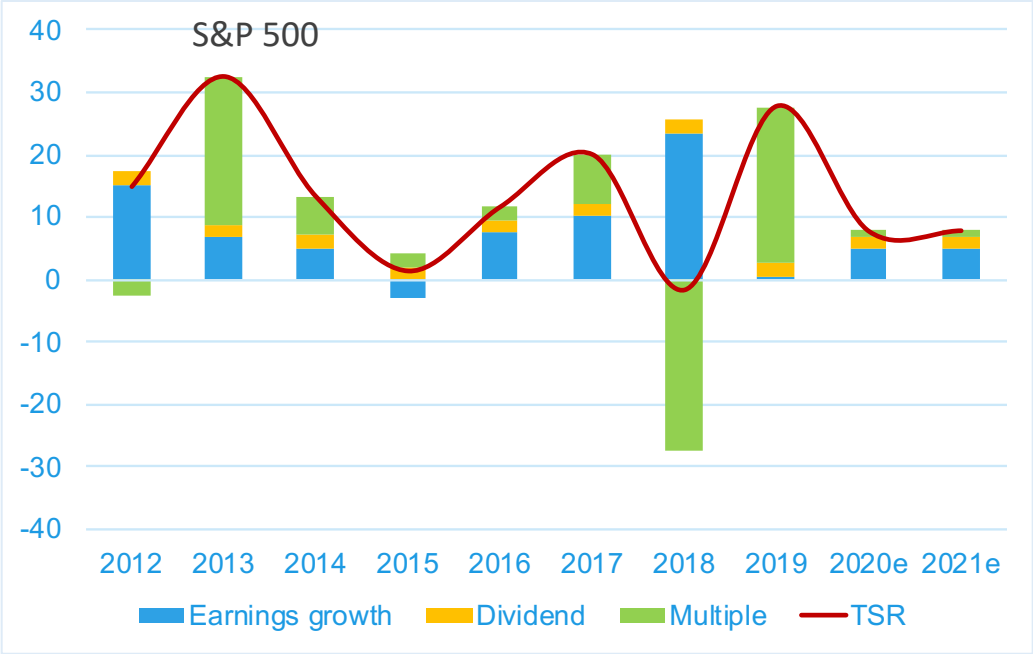
Over the last 12 decades US stocks have generated 9.4% return per year incl dividends. When you break each decade into the key drivers (earnings growth, dividend growth and change in valuation) you get the average annual return per decade as seen in top figure

For the US 2020 looks like a 8% year if earnings grow 5%, dividends give 2% and low interest rates push valuation 1% higher

Current consensus suggest 10% earnings growth in 2020, but analysts tend to be too optimistic hence the 5% rate seems more realistic

And if there's no major recession then 2021 looks to continue at same pace, which by the end of the 2020s decade looks like a decent 8% total return per year



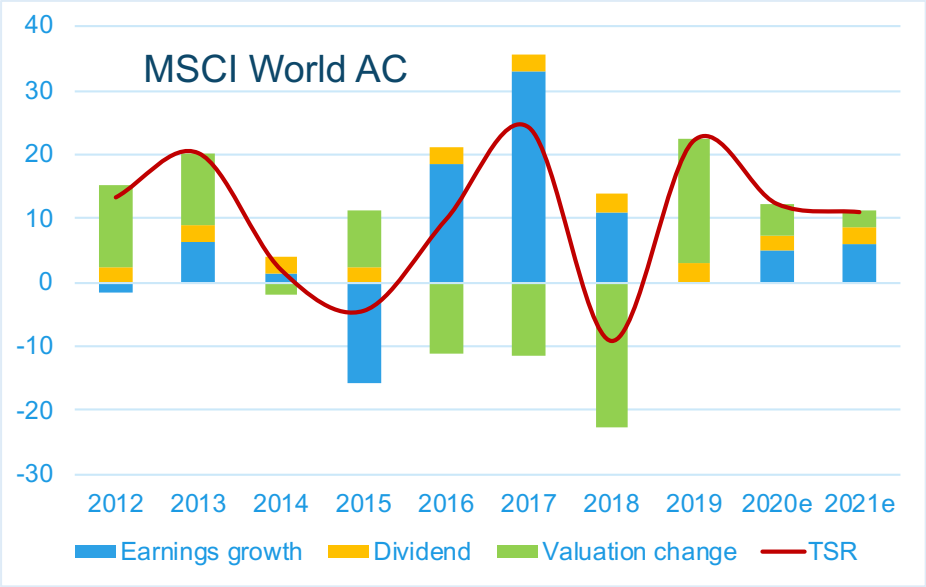


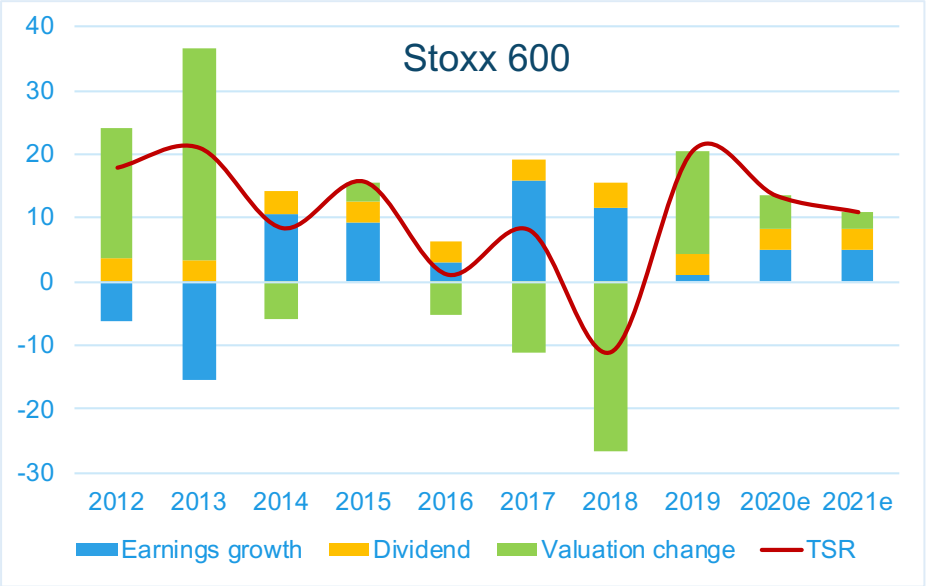
World and Europe can deliver 13% in 2020

While USA constitute 56% of global stock market value its 49% of global earnings, which are expected to reach 3.075bn $ in 2020

The non-US part of the world has not seen their stock prices perform like the US in the 2010s. Measured on 2020 earnings they trade at 13.8x or an earnings yield of 7.2%. That's is attractive in a world where bonds and deposits give you negative rates

The multiple contraction from 2016-18 is likely to turn into multiple expansion in the coming years. Combine that with 5% earnings growth and 3% dividend and we're in for double digit returns in the early part of 2020s



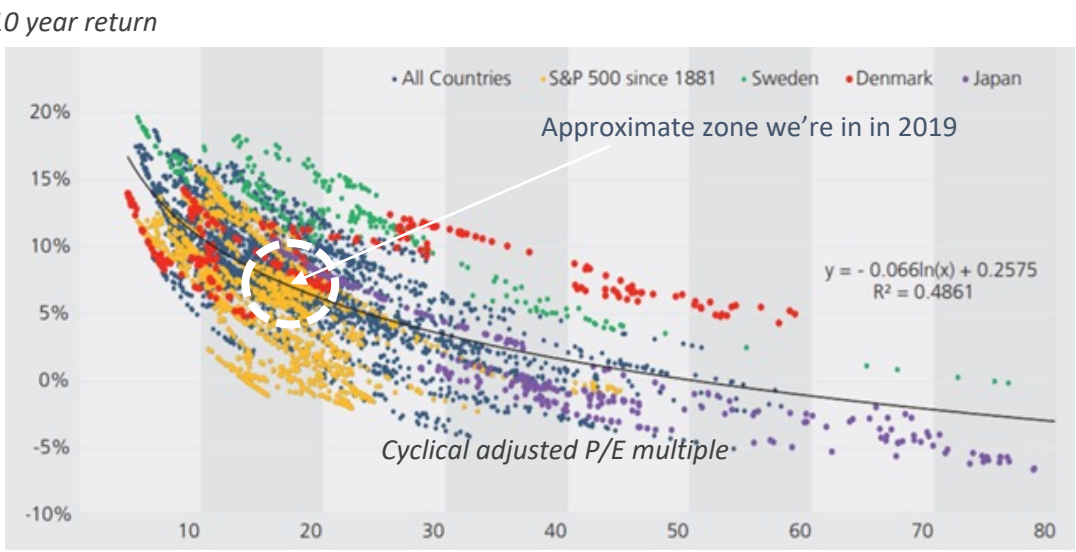


A general observation on valuation and performance

Financial markets data is getting better and better. And investigative researchers remake the historical price and fundamental data going back more than 100 years.

All this data is sorted and analyzed and one finding which should not surprise is that when valuation measured on P/E exceed 40x, then the subsequent 10-year performance is lower than when P/E is closer to 10x (Shiller research)

The current valuation of 14-18x is consequently not in any danger zone. And in 2020 the 10 year rolling average for earnings will exclude the 2008-09 down turn then earnings will be supportive of higher prices and probably also valuations



How to read the figure

Each dot is a month so if you bought one of the dark purple Japan dots to the right when Japan traded at 70x earnings, your subsequent 10 year and annualized return was minus 7%

On the other hand, if you bought one of the green dots (Sweden) during a crisis like 2008 then your subsequent annualized 10-year return would be 20%

Clusters with below 10x P/E multiples are hard to find after a 10 year bull market. There's millions of investors trying to find gold nuggets, but it's difficult and many of the objectively low value assets are likely to be business models that will see decline in the coming decade. I.e. tobacco stocks are lowly valued, but the number of tobacco users is in terminal decline, hence earnings is heading the same direction

Capital flows

2019 has been a very strange year in terms of stock price performance and capital flows.

Flows data shows capital is leaving the markets, while share buy backs are smaller than last year. But stock markets are up up in 2019, so who bought?

There's several players that do not provide data such as Sovereign Wealth Funds, some hedge funds and retail flows are estimates from the banks. And these non-reported sources are the most likely buyers in 2019

Going forward the biggest source of potential new flows are reinvested dividends what contribute 1.5 trillion $ - that's larger than the global pharmaceutical industry annual revenues

If 2020 estimates are correct its supportive for the 10%+ return scenario

Who is buying and selling stocks?

Activity in bn $	2017	2018	2019	2020e
Stock buy backs	700	1.200	850	900
Dividends	1.255	1.378	1.430	1.500
Insti net demand est	629	400	-200	300
Private net demand est	350	850	-600	500
Issue of new shares	762	659	627	650
M&A activity all kinds	4.590	4.400	4.470	4.500

Source: Janus and FT

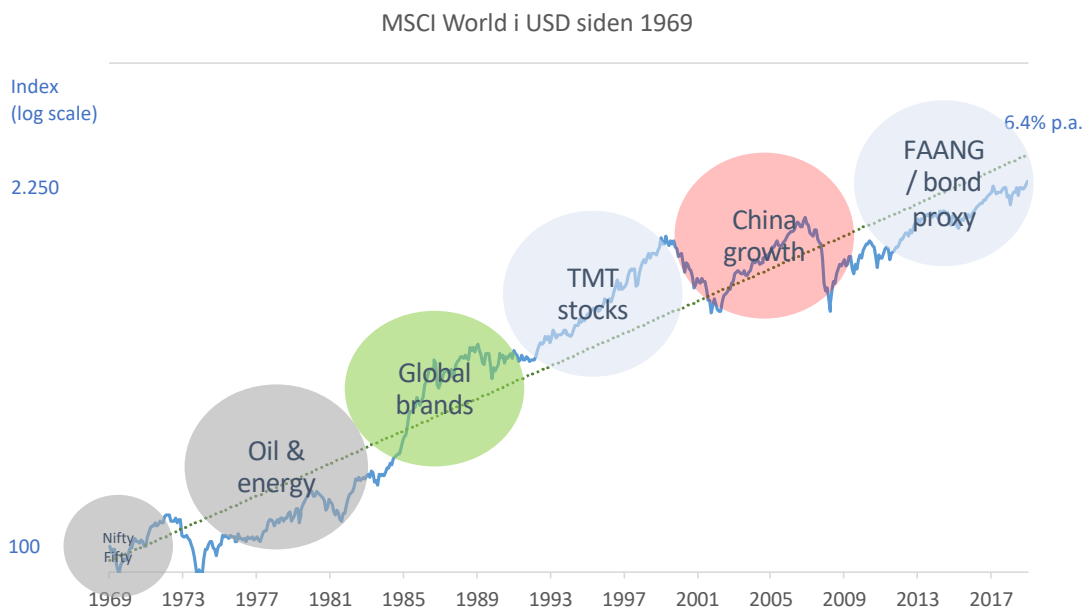
Outperformance pockets in the past decades

The past 50 years have seen outperformance by clusters of sectors and company profiles. The stock market apparently 'sees' the pockets with superior sales and earnings growth and honors it with solid outperformance

The leadership period ends from two reasons;

1) valuation comes out of sync with the underlying fundamentals and/or
2) the underlying fundamentals deteriorate due to overly optimistic new investments

Good examples are the TMT in late 1990s and subsequent IT bubble bust in 2000-02. And the Emerging Market outperformance in the 2000s



2020s: The Asia and digital decade

Things that will take off in 2020s – decade of disruption

Many traditional businesses have been cautious about investments in expansion since 2010. At the same time we have seen new products and services we didn't know in 2010. iPad, Tesla, Uber and Netflix are good examples of things we didn't know much about in 2010. Yet, these new business models disrupted the consumption patterns.

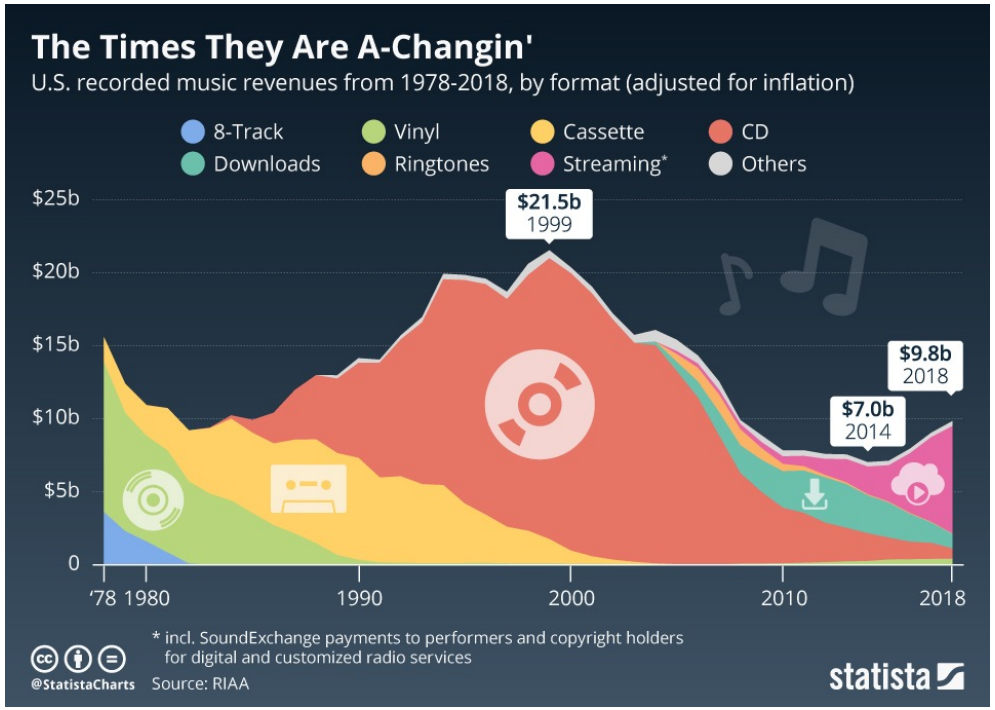
We still remember where the local Blockbuster video store was in 2010, but things change. And fast.

Disruption will accelerate in 2020s, but it can be difficult and dangerous to go into those investments just because they are disruptive.

Watch out for capital flows into new businesses as over investment into low return business models could be a big risk.

Also, watch out for traditional businesses that manage to embrace and grow their format in a digital world.

The next pages are some of the larger pockets of new businesses to be seen in 2020s.



The music industry serves a good example on disruption impact. Industry sales peaked as CD's where replaced by downloads that consumers often didn't pay for. Only with new infrastructure and streaming has the industry and artists been able to recoup some of the lost ground.

In the 2020's we will likely see even more disruption by digital inventions so stay tuned in and be open minded.

5G

5G super fast mobile data was launched in 2019. Coverage is being built out and this will accelerate in 2020-23 as communication providers install new infra structures.

2G is like walking

3G is like bicycling

4G is like driving a car

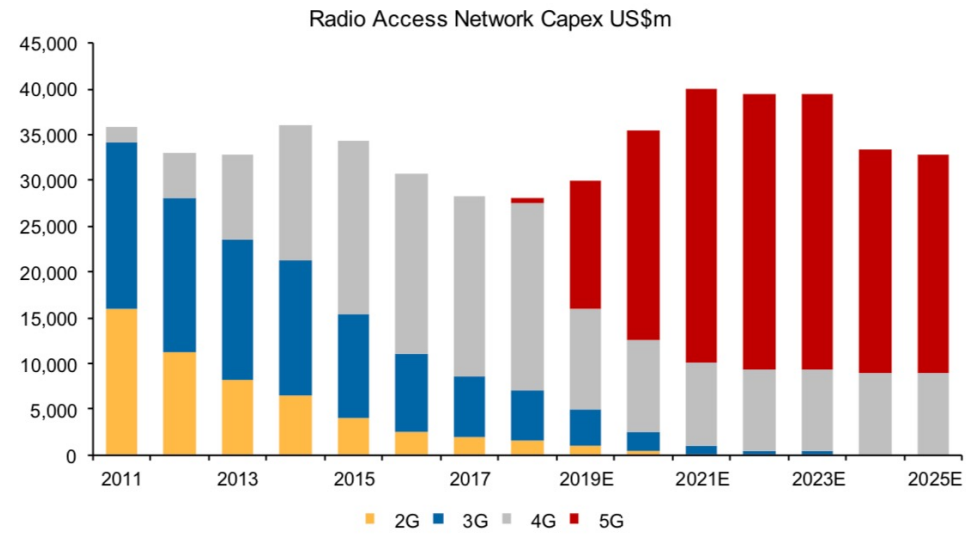
5G is like flying a fighter jet

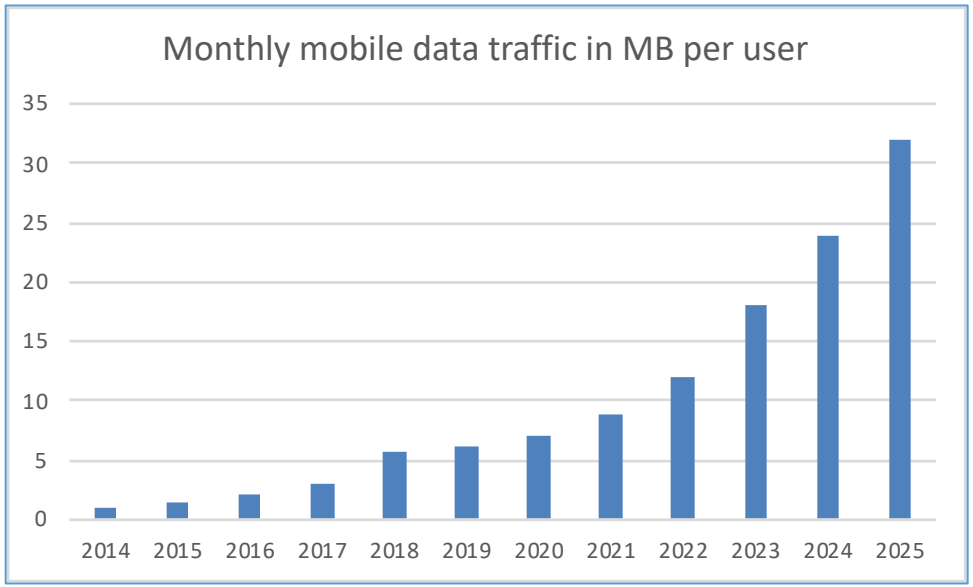
The user experience will change communication consumption patterns even more. Internet of things will be enabled with 5G so the amount of data to be sorted, analyzed and used for decisions will exponentially grow

2020 will be the first break-thru year and the Olympics in Japan, World Cup in Qatar etc will set new standards for how communication will work

This is an interesting investment space and on the infrastructure equipment there's only a few players; Ericsson, Huawei and Nokia dominate the market place

Fig 2 Telecom Capex is entering the 5G cycle





Smartphones

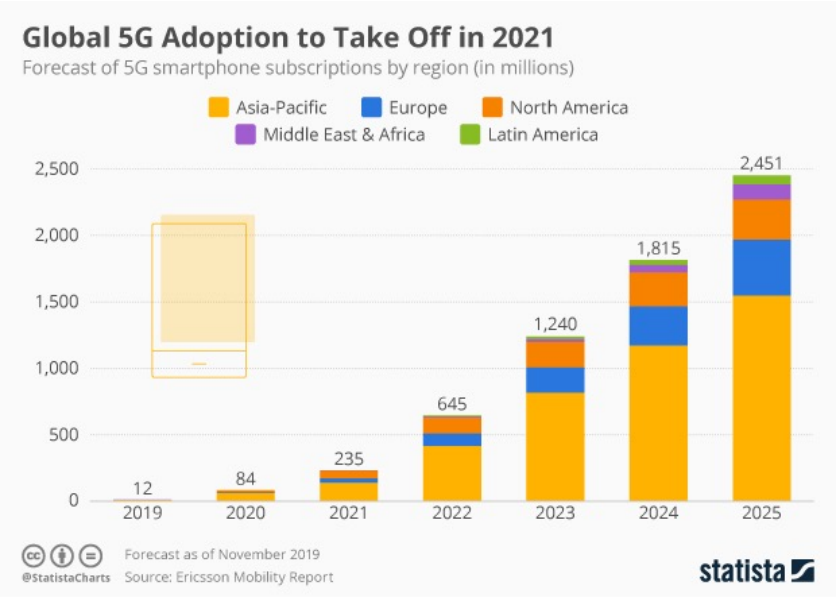
Global smartphone sales run at around 1.5 billion units per year. And the number of data cards in operation is around 5.5bn globally.

The 5G take-off started small in 2019 and 2020 should be the first 'best seller' year and exceeding 100m units would not surprise

For the general smart phone market and observing 2-3 year life time for a device, then the replacement cycle in 2020 could be much higher than estimated, which adds to the rapid 5G roll-out

Looking further down the road then the faster speed of communications goes hand in hand with faster data processing. In 2019 we spend hours at a key board, which essentially is a leftover from a typewriter invented in 1867.

In 2025 the the first microLED screens are expected and with touch, voice and eye data users will be able to communicate, work and read in a new modus. Some even suggest mind as a communication tool of the future…



Using senses for internet and communication is coming

Source: Ericsson

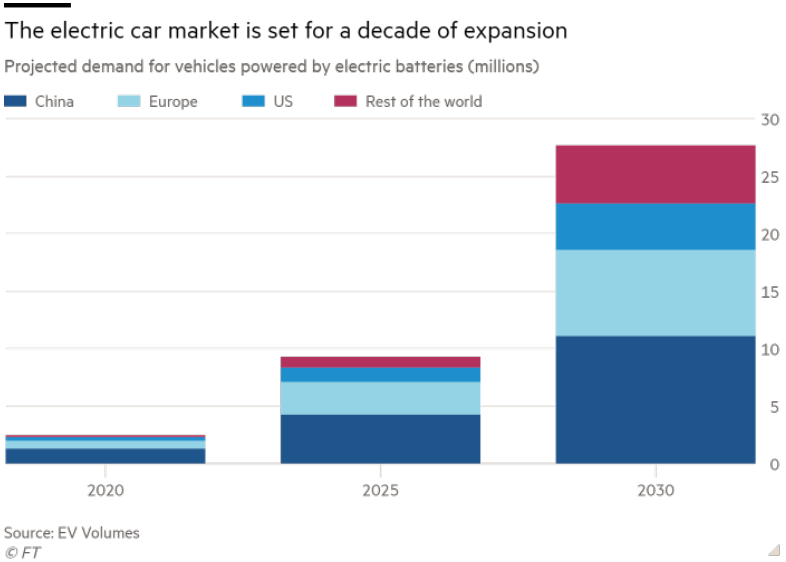
Electric vehicles

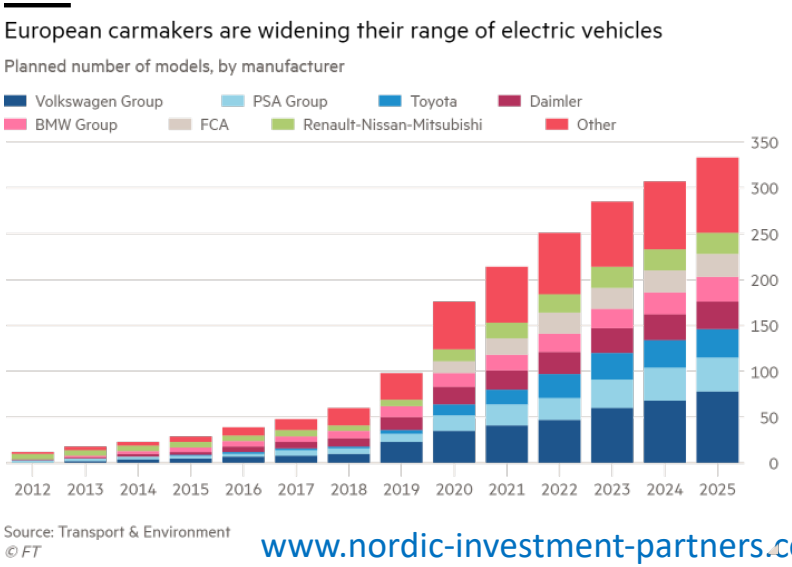
Electric cars are gradually but surely replacing fossil fuel engine vehicles. It's a long journey and below 2% of all new cars sold are EV's

2020 is however seeing acceleration in cars to choose from, which in turn will stimulate end-user demand. By the end of the 2020 decade EV's will probably have exceeded current estimates of 28% share of the total market.

The journey requires enormous investments in new car-production facilities and infrastructure, which initially will not provide very high returns. But it will undoubtedly happen and the first movers will be the first ones to harvest their efforts.

Tesla is a trailblazer and up against resource rich traditionalists. If the traditionalsts get their act together as it seems from the model program in illustration, then Tesla can take the honor of kick-starting the EV wave, but it's far from cerrain Tesla can take the market like Apple have taken the smarthone market





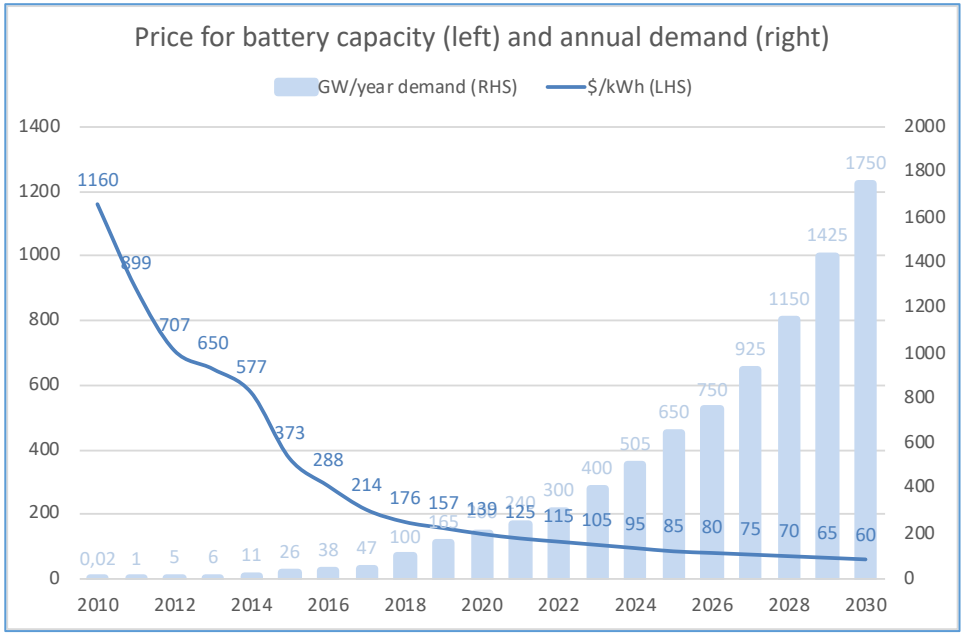
EV impact

EV's need energy storage and batteries are the choice of the day. And the key driver is electric vehicles

The figure to the right shows the average cost for a kWh battery and how the installed base grows towards 2030. It's an industry in the early days and resemble the smartphone industry standing in 2009 and looking ahead.

The iPad was launched in April 2010 and changed data/internet usage platforms significantly. So expect some surprises in the battery / energy storage market too going through the 2020s

Lower carbon emission is a priority. And it's possible to monitor the price of carbon rights. They are trading at 27$ per tonne and the political agenda is for much higher prices going forward. Higher price for carbon emission will motive and speed up the move towards EV's and renewable forms of energy. So monitor carbon prices to get a sense of the disruption speed



www.nordic-investment-partners.com

Hydrogen fuel and storage of solar power

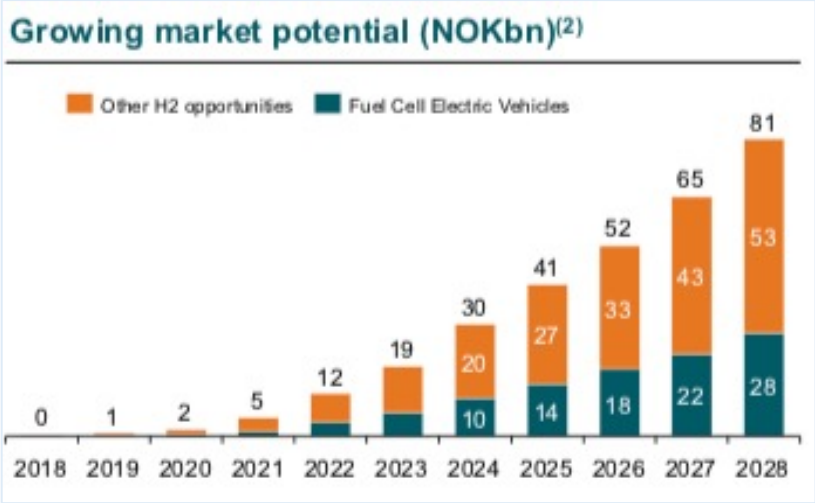
A less crowded energy storage space is hydrogen.

Today most of the hydrogen production is made by burning natural gas, but as solar power production increases then the ability to produce lots of cheap energy increases. You can store power in batteries and use the eV cars for back-up, but you can also convert solar power into hydrogen.

The amount of energy stored in a hydrogen tank is many times more that of a battery and hence it's a huge opportunity

2020 is still early days for hydrogen, but as the electrolyzer technology expand and improve the market starts to grow. It's a market with few players and not nearly as crowded as the battery business.

There's several projects such as Hamburg hydrogen trains and Norwegian fuel cell hydrogen ferries starting to trail blaze this business opportunity



www.nordic-investment-partners.com

Renewables power

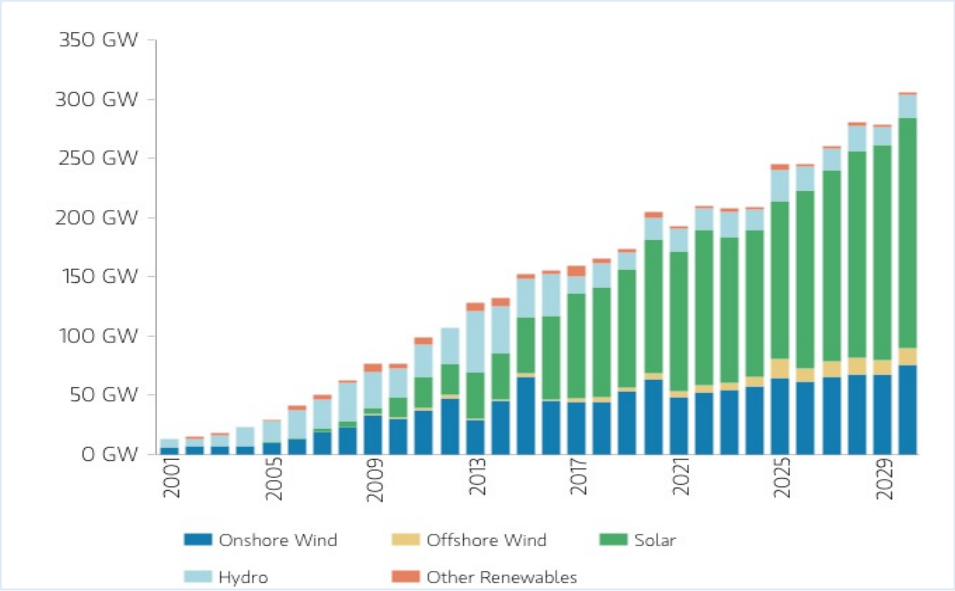
Global sustainability and using the given resources on the Planet is high on the agenda.

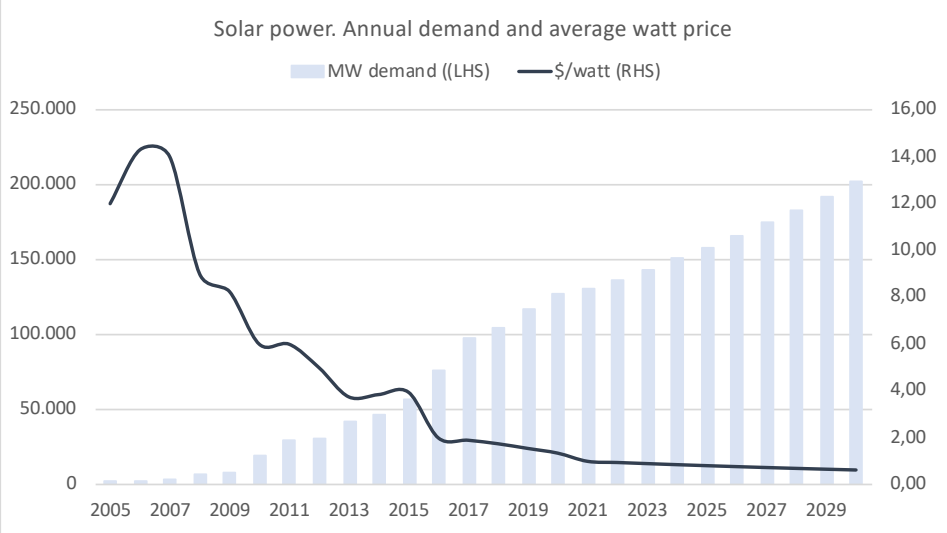
In the early days of street light the fuel was oil from whales. Fortunately for the whales Mr Rockefeller industrialized oil drilling and refining of petroleum and since then the primary source of energy has been fossil fuels. There's plenty of oil and gas of the planet for hundreds of years, but the very long term it's unsustainable. Hence the rationale for renewables is good, but the energy source has been expensive.

Looking ahead the cost of renewables, especially solar, has come down to levels where it's the cheapest source of energy. And when the economic rationale is good, then things normally take off.

The 2020s will see a rapid expansion of solar and wind power and it's likely the annual GW capacity additions will exceed current forecast

Annual addition (new GW capacity)





www.nordic-investment-partners.com

Asia – the region with the biggest absolute growth

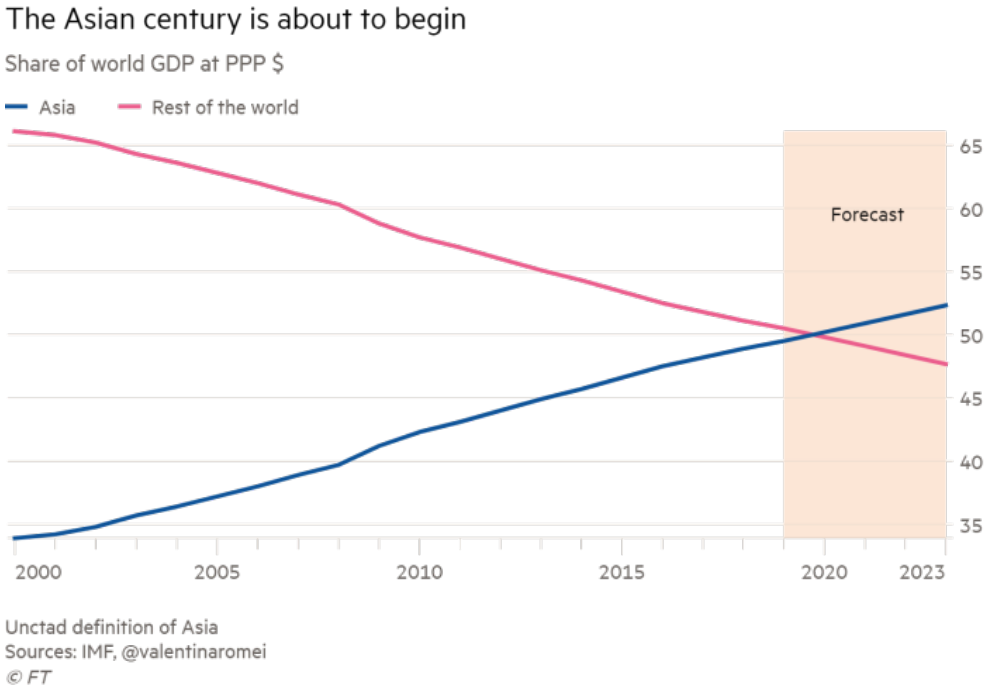
Out of the 7.5 billion people on Earth, 4 billion live in Asia

The living standards in Asia as on a rapid rise and inspired by the performance seen in Japan, Taiwan and Korea since 1960s

The level of affluence will increase faster in the 2020s and hence Asia as such offers the biggest absolute growth and will overtake the rest of the world

The pendulum of economic gravity hence swings to the East

Enjoy the journey




HAPPY NEW YEAR 2020