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INVESTMENT OUTLOOK 09.2021

15 September 2021

Global growth is slowing but remains strong. At the same time inflation is rising due to strong pent-up demand and supply-side restrictions. Many producers are faced with pandemic-related supply-chain disruptions. A notable example is the global scarcity of semiconductors.

The spreading of the Covid delta variant has led to rising infections. As a result, many countries are imposing new restrictions. In our view, however, it is unlikely that we will have more severe lockdowns in the coming months, as immunity has risen due to the vaccination roll-out and prior infections. Central banks have started to contemplate when to begin tapering, but have remained dovish overall.

Equity markets continued to rally in August. The MSCI World index, for example, increased by 2.3%. At the same time bond yields rose.

We remain neutral in equities and overweight in cyclical sectors, like industrials and financials.

Trauth

Thomas Trauth
CEO – IMT Asset Management AG

TAPERING WITHOUT TANTRUM

Financial markets

In August equity markets performed well. Both developed and emerging markets indices gained about 2.5%. The Indian NIFTY index even surged 8.7%. Also, the technology-heavy US NASDAQ index rose by 4%. It is very remarkable that in early September the Japanese Nikkei index rose 8% while most other equity indices fell. This is due to the expectations that the Japanese economy will be able to reopen soon. The vaccination roll-out in Japan was lagging behind that of most Western countries, but recently the pace of the roll-out accelerated sharply.

Short-term yields remained stable in August. While inflation expectation in Europe rose by 4 basis points, US inflation expectations fell by 6 basis points. It seems that market expectations confirm the notion of a temporary inflation spike. Bond yields at the long end of the curve rose by about 9 basis points. Credit spreads remained very stable

Gold was flat in August, while the broad commodity index fell by 0.3%. The price of silver dropped 6.3%. Oil prices also fell by about 4.5%, after a strong rally in previous months. Demand for oil is expected to recover as global growth remains strong. At the same time the OPEC 2.0 agreement keeps oil supply constrained. Nevertheless, upside potential for oil prices seems to be limited given the strong increase we have already seen this year. REITS and listed private equity continued to rally in August with the indices rising by 1.6% and 2.6%, respectively.

The USD has remained very stable recently, moving essentially sideways. This is true for the broad USD index as well as for EUR-USD and USD-CNY. Meanwhile, the CHF weakened in August, after it had appreciated by about 4% since early March.

Macroeconomics

The August PMI data confirm that growth has peaked, though it nevertheless remains very strong. The US ISM manufacturing index improved slightly to 59.9 after 59.5. The European Markit manufacturing PMI fell to 61.4 after 62.8. US non-farm payrolls were very disappointing. In August the economy created 235,000 additional jobs versus expectations of 733,000. An absence of new jobs was seen especially in the leisure and hospitality sector, a fact which probably already reflects the spreading of the delta variant. Eurozone's inflation rate jumped to 3% in August, clearly exceeding the ECB's inflation target of 2%.

In China the credit tightening continued. This coincides with a regulatory makeover by the Chinese authorities. The Chinese leadership feels that the private sector is not aligned with their social and political objectives. Major targets have been private education companies followed by technology companies. As a result, the China Information Technology Index has fallen by more than 20% since February.

Covid-19

The total number of cases reached almost 225 m and 4.6 m people have died of covid. 5.7 bn doses of vaccine have been administered and 2.3 bn people are fully vaccinated, i.e., almost 30% of the global population. The spreading of the delta variant has led to another wave of Covid cases. In the US, for example, hospitalization is back to the levels we last saw last winter. Many countries are imposing new restrictions to slow the spreading. We believe, however, that immunity has been growing due to vaccinations, prior infections, and booster shots. This will prevent economic activity from declining too severely.

Central banks

End August central banks gathered at their annual meeting in Jackson Hole. Fed chairman Powell said at the meeting that the Fed would scale back asset purchases later this year. He did not mention any details regarding the speed of the tapering. Since Powell embedded his announcement in dovish rhetoric, markets continued to rally after the speech. Powell clearly counterbalanced a vocal minority of board members, who have turned more hawkish in recent months and demand a much faster withdrawal of the stimulus measures to fight rising inflation.

In early September the ECB started tapering without causing a major market reaction. It has done so by carefully phrasing it, as follows ".. favourable financing conditions can be maintained with a moderately lower pace of net asset purchases under the pandemic emergency purchases programme (PEPP)". In addition, and probably more importantly this came after the ECB revised its policy framework in July and became clearly more dovish regarding the longer-term. The inflation goal was revised to a symmetric two-per cent target. This gives the ECB leeway to tolerate inflation above 2% for 18 months or longer without raising rates.

Outlook

The outlook has become a bit more uncertain. Growth is strong but slowing. Monetary policy is very accommodative but about to taper. Covid immunity is rising strongly due to the speed of the global vaccination campaign and because many people have recovered from infections, but new variants are raising renewed concerns.

On balance, we continue to see an environment which is very supportive for risky assets, and we remain positive on the outlook for the equity markets with an overweight of cyclical sectors. This is also due to the reflationary environment. Nevertheless, we may see increasing volatility and potential market corrections. In our view, bond yield will continue to rise and we expect US 10-year yields to reach 2-2.5% in the coming quarters.

The major risk to our outlook is more persistent inflation, which could unnerve markets and lead central banks to withdraw monetary support earlier than anticipated.

ECONOMICS

The August PMI data confirm that growth has peaked, though it remains very strong. The US ISM manufacturing index improved slightly to 59.9 after 59.5. The European Markit manufacturing PMI fell to 61.4 after 62.8. US non-farm payrolls were very disappointing. In August the economy created 235,000 additional jobs versus expectations of 733,000. An absence of new jobs was apparent especially in the leisure and hospitality sector, a fact which probably already reflects the spreading of the delta variant. Eurozone's inflation rate jumped to 3% in August, clearly exceeding the ECB's inflation target of 2%.

Fig. 1: PMIs

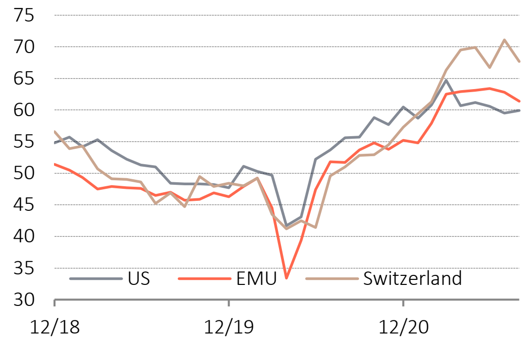


Fig. 2: PMIs

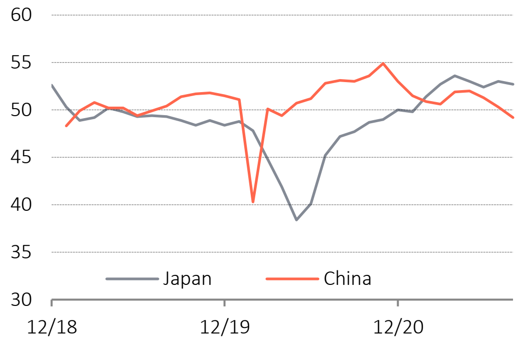


Fig 3: Consumer price inflation, in % YoY

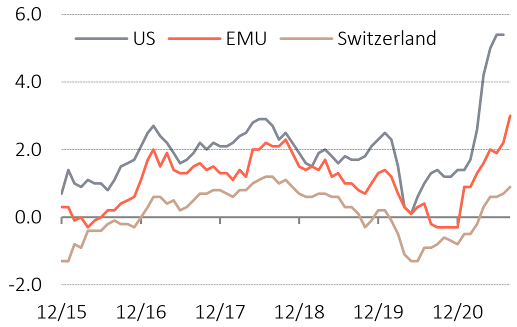


Fig. 4: Consumer price inflation, in % YoY

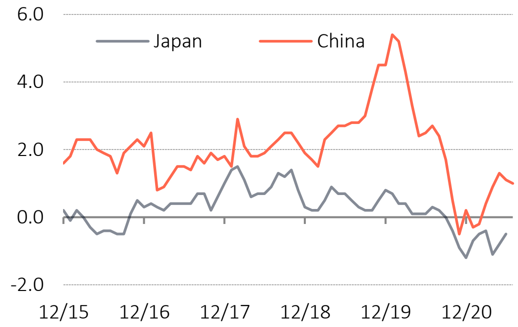


Fig 5: Unemployment rates, in %

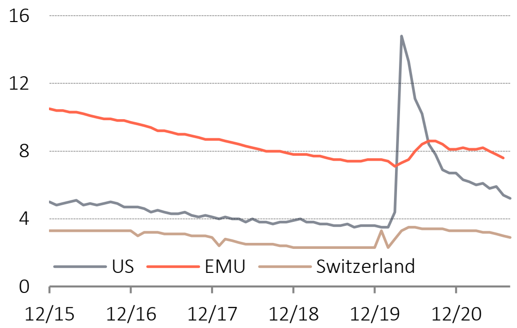
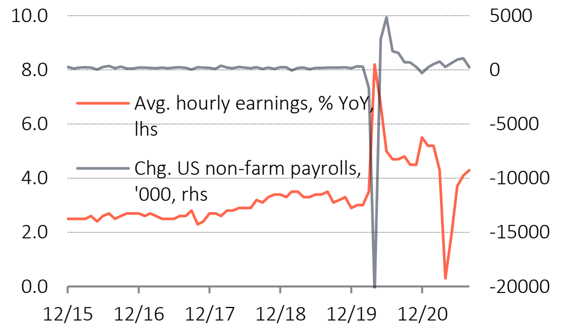


Fig 6: US labor market



FIXED INCOME

Short-term yields remained stable in August. While inflation expectation in Europe rose by 4 basis points, US inflation expectations fell by 6 basis points. It seems that market expectations confirm the notion of a temporary inflation spike. Bond yields at the long end of the curve rose by about 9 basis points. Credit spreads remained very stable.

Fig.7: 2Y government bond yields

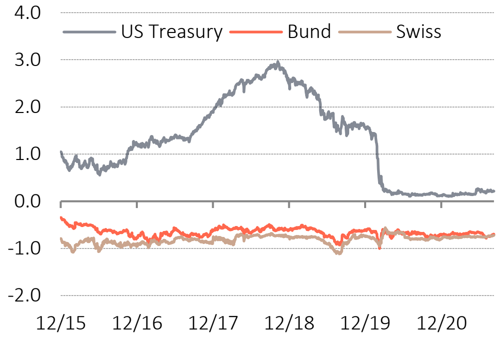


Fig. 8: 10Y government bond yields

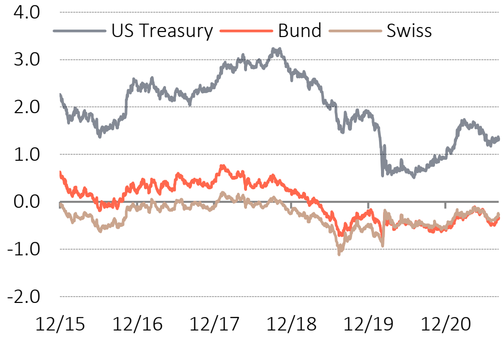


Fig 9: 10Y break-even inflation

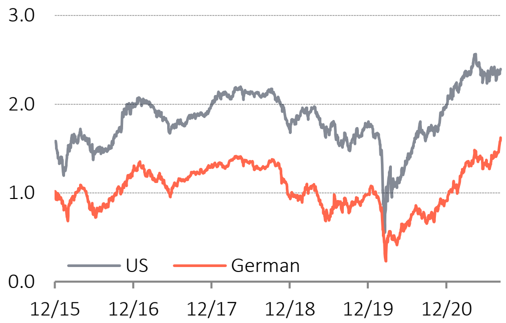


Fig. 10: Credit spreads, 5Y credit default swaps

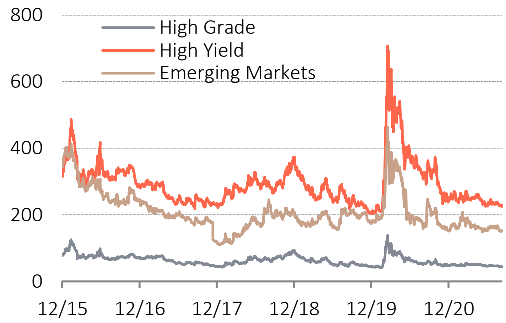


Fig 11: Money market spreads (3M-2Y)

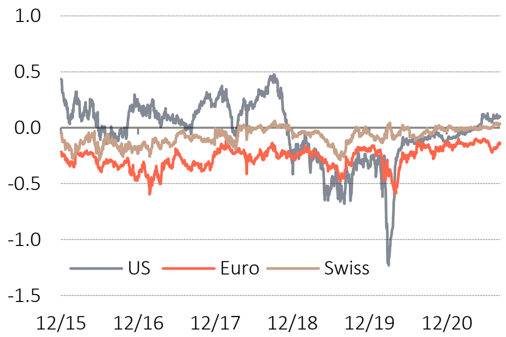
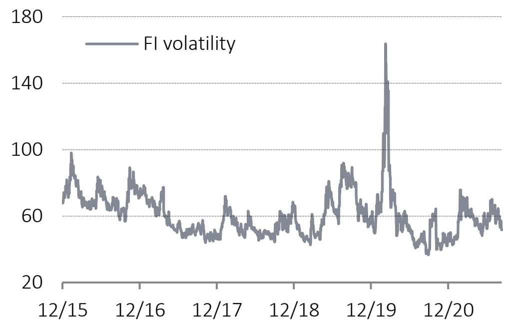


Fig 12: Merrill Lynch volatility index (MOVE)



EQUITIES

In August equity markets performed well. Both developed and emerging markets indices gained about 2.5%. The Indian NIFTY index even surged 8.7%. Also, the technology-heavy US NASDAQ index rose by 4%. It is very remarkable that in early September the Japanese Nikkei index rose 8% while most other equity indices fell. This is due to the expectations that the Japanese economy will be able to reopen soon. The vaccination roll-out in Japan was lagging behind that of most Western countries, but recently the pace of the roll-out accelerated sharply.

Fig. 13: MSCI equity indices – major regions

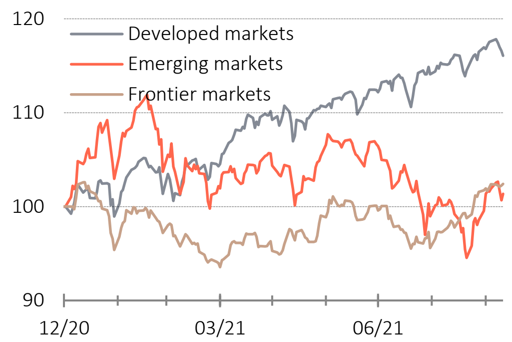


Fig.14: Equity indices – major developed markets

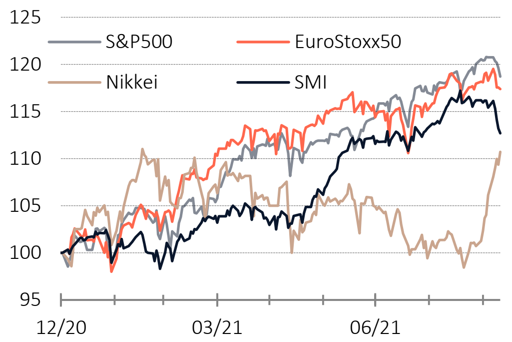


Fig 15: Equity indices – major emerging markets

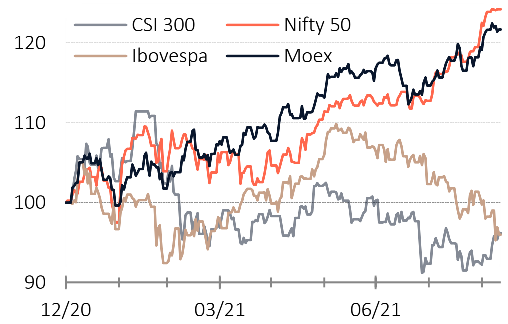


Fig. 16: Sector performance, MSCI Europe, YTD

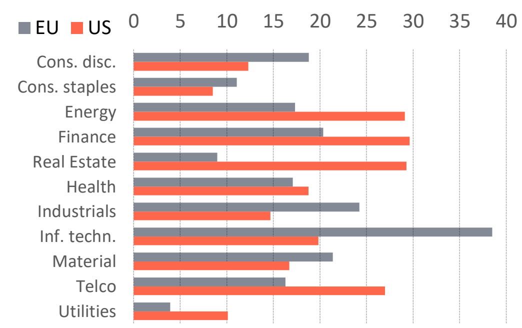


Fig 17: Price-earnings ratios

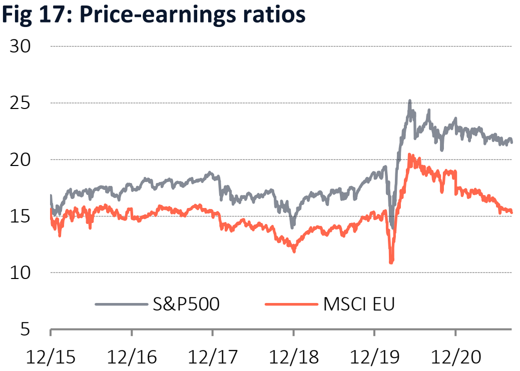
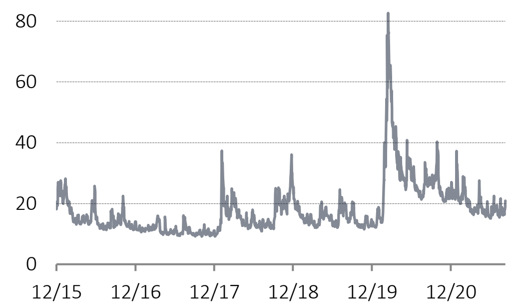


Fig 18: Equity volatility – S&P500 VIX index



ALTERNATIVE INVESTMENTS

Gold was flat in August, while the broad commodity index fell by 0.3%. The price of silver dropped 6.3%. Oil prices also fell by about 4.5%, after a strong rally in previous months. Demand for oil is expected to recover as global growth remains strong. At the same time the OPEC 2.0 agreement keeps oil supply constrained. Nevertheless, upside potential for oil prices seems to be limited given the strong increase we have already seen this year. REITS and listed private equity continued to rally in August with the indices rising by 1.6% and 2.6%, respectively.

Fig. 19: Gold price, USD/oz

Fig.20: Brent oil price, USD/bl

Fig 21: Bloomberg commodity indices

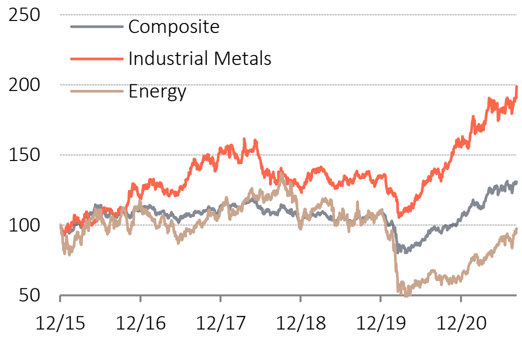


Fig. 22: HFRU hedge fund indices

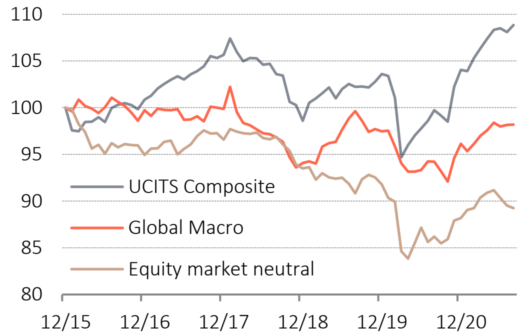


Fig 23: FTSE EPRA/NAREIT global REITS index

Fig 24: LPX global listed private equity

CURRENCIES

The USD has remained very stable recently, moving essentially sideways. This is true for the broad USD index as well as for EUR-USD and USD-CNY. Meanwhile, the CHF weakened in August, after it had appreciated by about 4% since early March.

Fig. 25: EUR-USD exchange rate

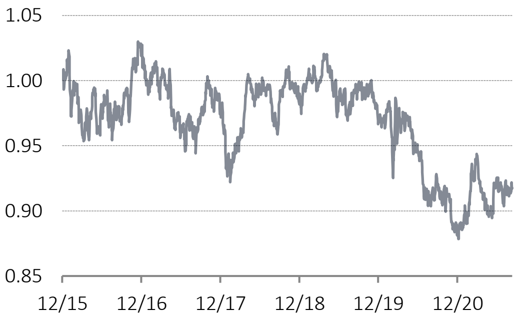
Fig. 26: GBP-USD exchange rate

Fig 27: USD-JPY exchange rate

Fig. 28: USD-CNY exchange rate

Fig 29: EUR-CHF exchange rate

Fig 30: USD-CHF exchange rate



COVID-19

The total number of cases reached almost 225 m and 4.6 m people have died of covid. 5.7 bn doses of vaccine have been administered and 2.3 bn people are fully vaccinated, i.e., almost 30% of the global population. The spreading of the delta variant has led to another wave of Covid cases. In the US, for example, hospitalization is back to the levels we last saw last winter. Many countries are imposing new restrictions to slow the spreading. We believe, however, that immunity has been growing due to vaccinations, prior infections, and booster shots. This will prevent economic activity from declining too severely.

Fig. 31: Total Covid-19 cases (x 1000)

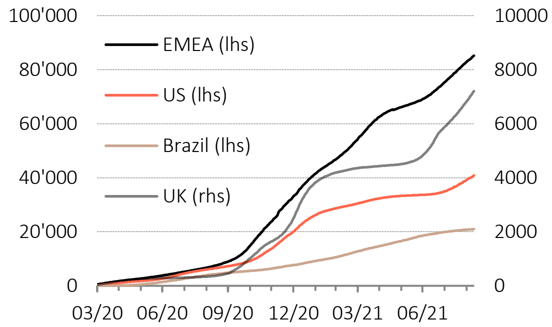


Fig. 32: New cases per day (7-day average)

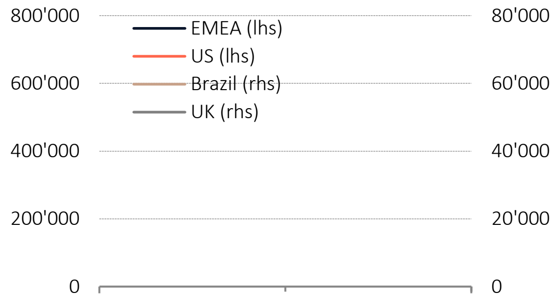


Fig 33: Global vaccination campaign
(doses per 100 people)

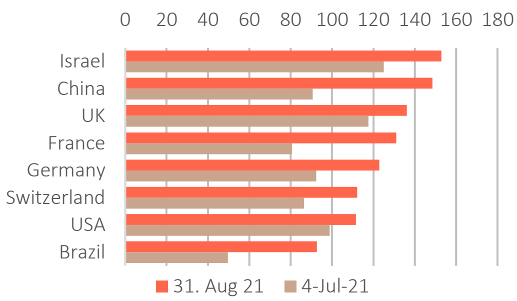


Fig.34: Central bank total assets (indexed)

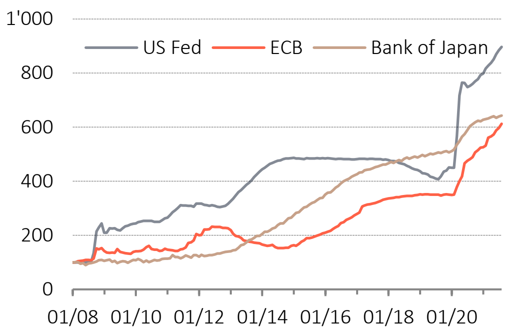


Fig 35: US bankruptcy index

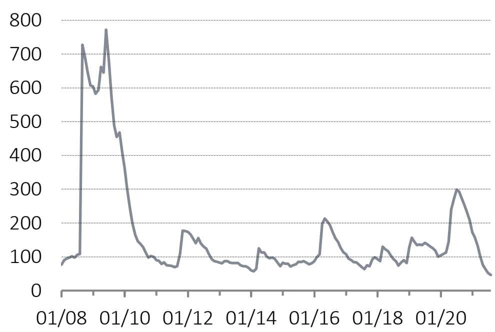
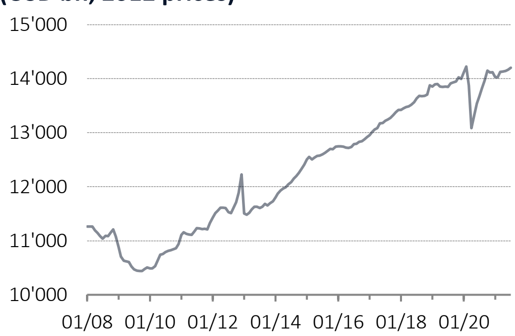


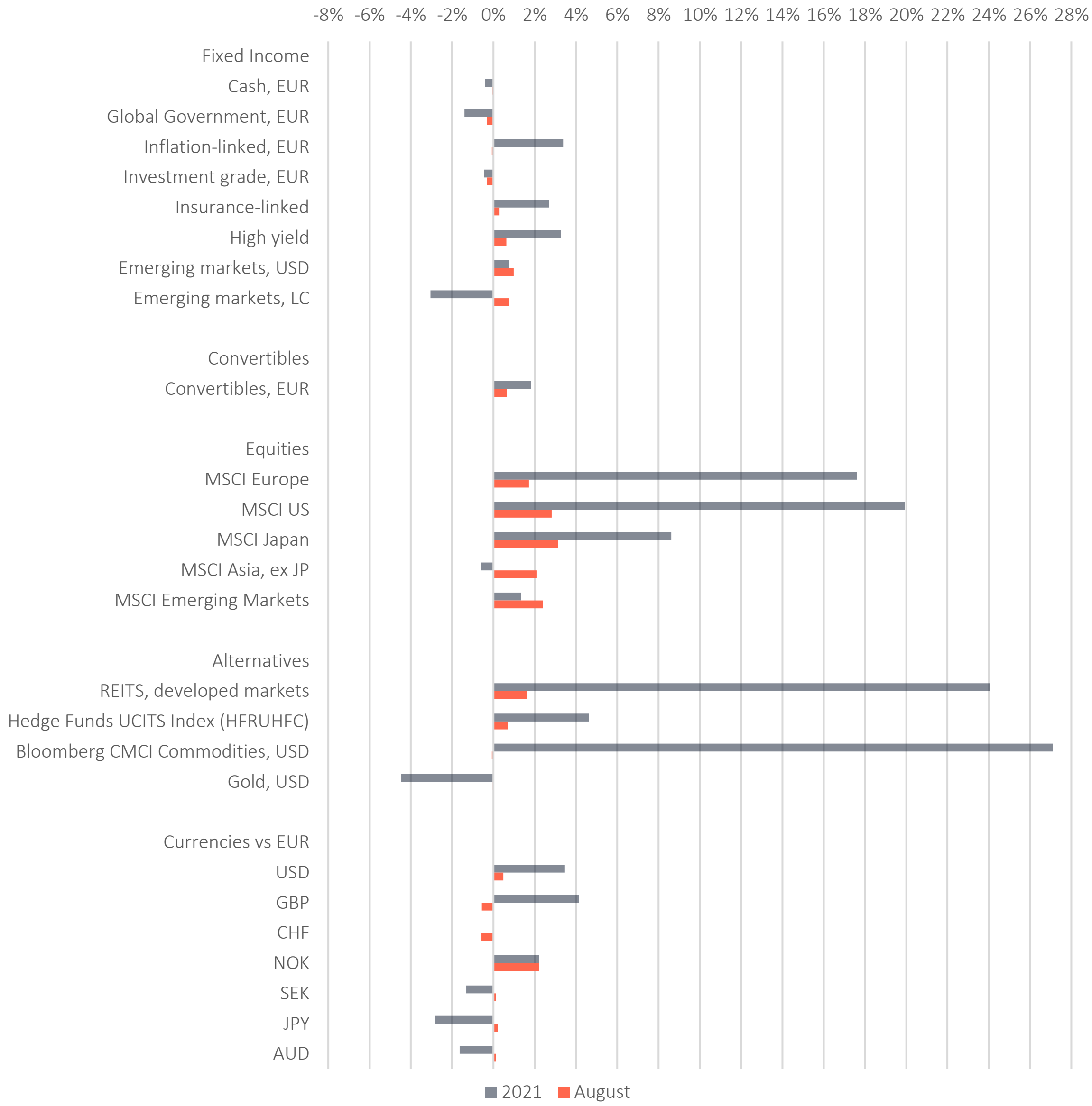
Fig 36: US personal income, excl. transfers (USD bn, 2012 prices)



ASSET ALLOCATION

August was another good month for multi-asset class portfolios. Risky assets, especially equity markets, performed well. Also, emerging market assets recovered, both fixed-income and equities. The broad commodities index as well as gold remained flat. The USD appreciated while the GBP and CHF fell vis-à-vis the EUR.

Fig. 37: Performance of major asset classes, based on our EUR portfolio strategy

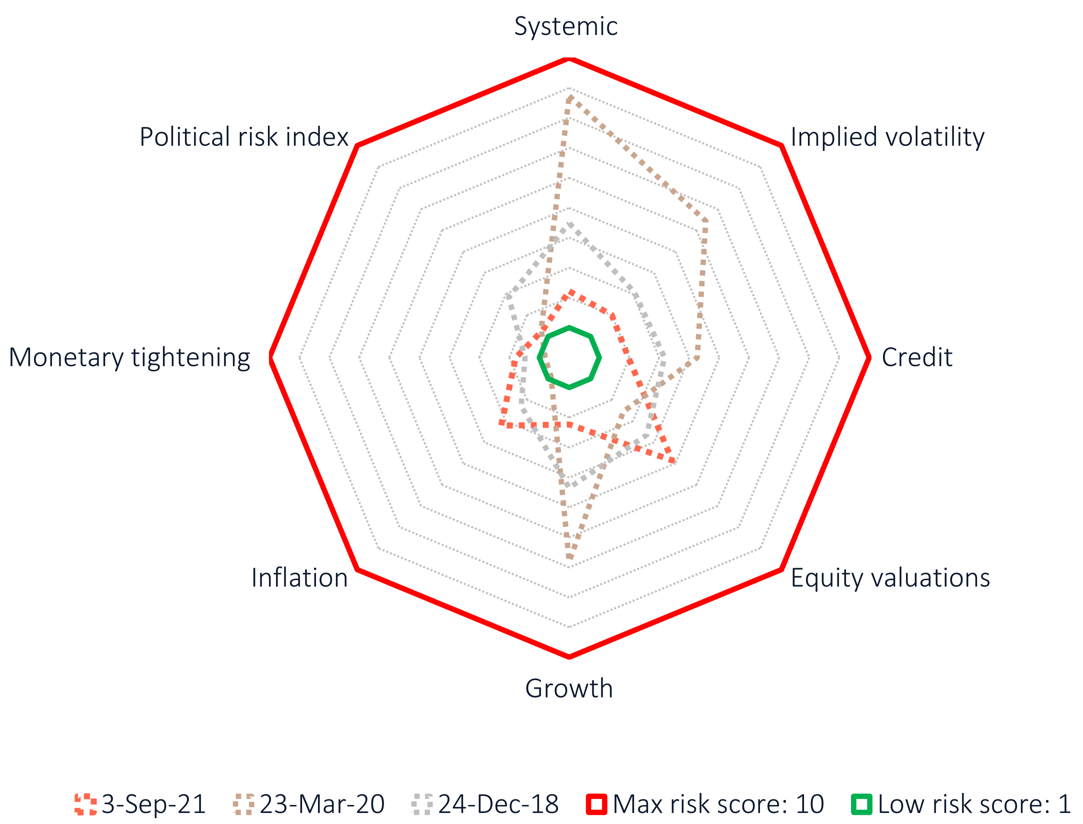


RISK MONITOR

Our risk indicators are little changed compared to the last few months. Most risk areas remain at very low levels. The notable exceptions are equity valuation and inflation risks.

Fig. 38: IMT Risk Monitor

23-Mar-2020: Global pandemic
24 Dec 2018: Growth and monetary tightening fears



DISCLAIMER

Source for all graphs: IMT Asset Management AG, Bloomberg, Real Clear Politics, for Fig 36 Statista (de.statista.com), for Fig. 38, the political risk index: "Measuring Geopolitical Risk" by Dario Caldara and Matteo Iacoviello at https://matteoiacoviello.com/gpr.htm.