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INVESTMENT OUTLOOK 03.2021

13 March 2021

In February equity markets continued to rally. Last week US President Biden signed another massive fiscal stimulus bill, this time of USD 1.9 tn, which brings total US stimulus measures to a staggering USD 6 tn since the pandemic broke out. The US federal deficit is likely to reach 15% of GDP in 2021.

The global reflationary policy, i.e., coordinated monetary and fiscal expansion, has finally led to rising inflation expectations and bond yields. US 10-year yields, for example, rose to 1.6% from 0.9% at the beginning of the year.

Rising yields were bad news for technology stocks, which came under selling pressure after having enjoyed an exceptional rally last year. Cyclical stocks started to outperform, driven by a better growth outlook and attractive valuations. As a result, European equity markets, which are more tilted towards cyclicals, outperformed the US.

Overall, we remain neutral on equities since we continue to see the risk of a market correction in the coming months as overall valuations look stretched and markets somewhat overheated.

Trauth

Thomas Trauth
CEO – IMT Asset Management AG

ANOTHER US FISCAL STIMULUS PACKAGE

Financial markets

Equity markets performed well in February, although part of the gains was erased in the last week of the month when markets sold-off. Market participants became concerned that rising bond yields might derail the positive outlook for stocks. Cyclical stocks started to outperform as the technology sector is more interest-rate sensitive. This could be the beginning of a more pronounced rotation within equity markets away from technology stocks into cyclical and value stocks. Since European equity indices have a higher weight of cyclicals, including energy and financials, European stock markets outperformed the US recently. The Chinese equity market came under selling pressure as markets worried that the Chinese government could reduce stimulus measures.

Bond yields continued to rise. US 10-year yields rose to 1.6% and European yields to -0.25%. The yield increase resulted from rising real rates as well as from rising inflation expectations. Uncertainties about the future direction of bond markets led to a sharp increase of fixed-income volatility. High yield spreads tightened further whereas credit spreads for emerging market bonds widened.

The price of gold fell significantly in February on the back of rising real rates. At the same time, oil and industrial metals rallied sharply due to better growth prospects. Oil was supported by the fact that OPEC+ countries kept oil supply tight. Saudi Arabia even cut its production voluntarily below the level agreed with OPEC+. REITS, which are often believed to be sensitive to rising interest rates, performed well in February. The Global REITS index climbed 3.7%. The expected economic normalization outweighed rising funding costs.

The USD continued to strengthen somewhat in February. The GBP continued to trend up strongly. The Chinese CNY took a breather and stabilized after a strong persistent upward trend since May 2020. The risk-on environment reduced the attractiveness of safe-haven currencies. As a result, the JPY and the CHF weakened. At the same time, the CAD and the AUD gained on the back of the commodities rally.

Covid-19

The pandemic has infected 120 m people with 2.7 m fatal outcomes. The rollout of the vaccines continues. Globally 345 m doses have already been administered, more than 100 m of these in the US alone. Europe is lagging behind with a slow start to the campaign. Meanwhile in many countries new, more infectious variants dominate among the new cases. The US congress finally approved Biden's USD 1.9 tn fiscal package to further support the economy.

Macroeconomics

Most growth indicators strengthened in February. The US ISM manufacturing index rose to 60.8 after 58.7 and the EMU manufacturing PMI to 57.9 after 54.8. US President Biden succeeded in pushing through his USD 1.9 tn stimulus package and signed it into law on 11 March. This will provide another strong boost for the US and global economy. US non-farm payrolls came in at a strong 379,000 and the unemployment rate fell to 6.2%. Most jobs were created in the hospitality and leisure sector.

Monetary policy

At its policy meeting on 11 March the ECB expressed its concern about the latest bond market sell-off, which threatens to tighten monetary conditions. In order to help stabilize yields the ECB decided to increase the pace of its PEPP (pandemic emergency purchase program) from EUR 15 bn to around EUR 20 bn per week through Q2. After the meeting bond and equity markets rallied. A major beneficiary were Italian government bonds. The Italian 10-year yield dropped 0.6%-points. As a result, the spread between German and Italian yields, a key measure for political risk, dropped to 0.94%. At the same time the ECB turned more constructive on the medium-term outlook for economic growth.

The US Fed is holding its policy meeting on Tuesday and Wednesday this week. It will be interesting to see if the Fed is also taking measures to lower bond yields.

Outlook

We remain constructive for this year's outlook . Enormous stimulus programs, especially extraordinary US fiscal packages, will set off a strong growth impulse later this year, which will also help to stimulate growth globally as US imports will rise.

Nevertheless, markets could take a breather and correct in the coming months as equity market valuations look stretched and the markets show signs of overheating. Therefore, we are retaining our neutral equity positioning.

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ECONOMICS

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Fig. 1: PMIs

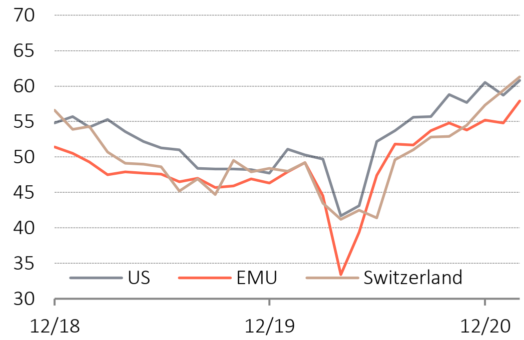


Fig. 2: PMIs

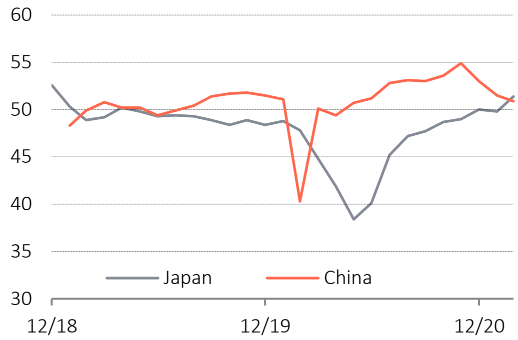


Fig 3: Consumer price inflation, in % YoY

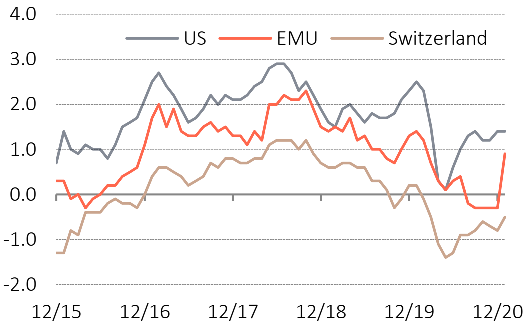


Fig. 4: Consumer price inflation, in % YoY

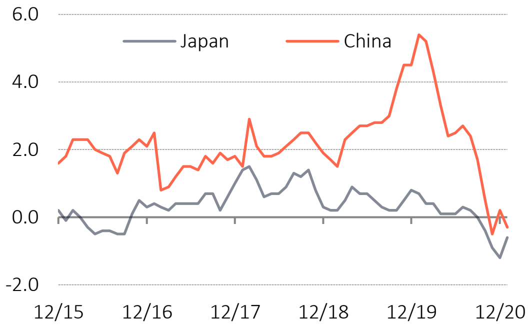


Fig 5: Unemployment rates, in %

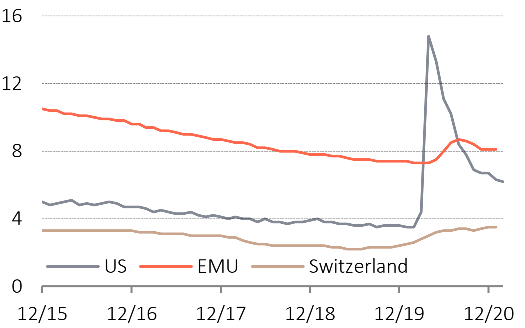
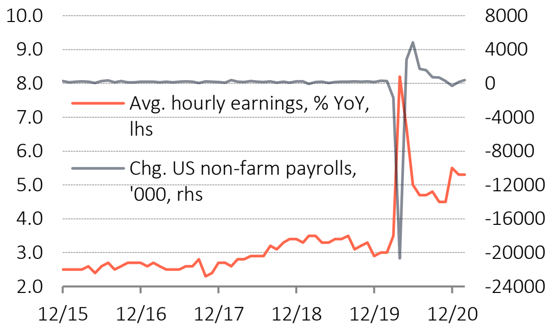


Fig 6: US labor market



FIXED INCOME

Bond yields continued to rise. US 10-year yields rose to 1.6% and European yields to -0.25%. The yield increase resulted from rising real rates as well as from rising inflation expectations. Uncertainties about the future direction of bond markets led to a sharp increase of fixed income volatility. High yield spreads tightened further whereas credit spreads for emerging market bonds widened

Fig.7: 2Y government bond yields

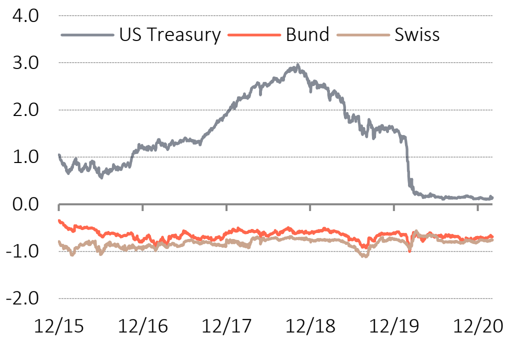


Fig. 8: 10Y government bond yields

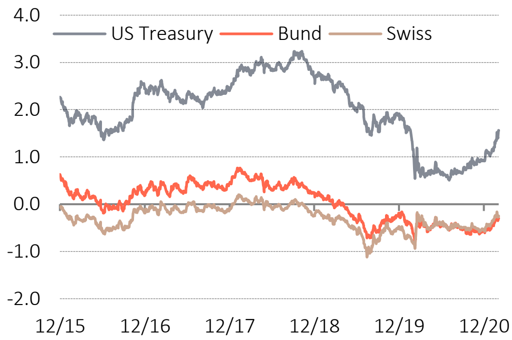


Fig 9: 10Y break-even inflation

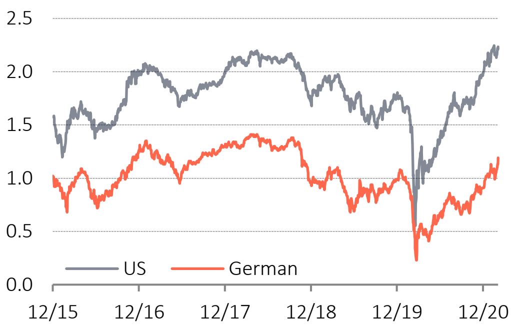


Fig. 10: Credit spreads, 5Y credit default swaps

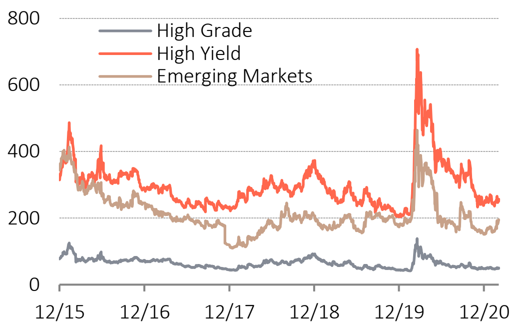


Fig 11: Money market spreads (3M-2Y)

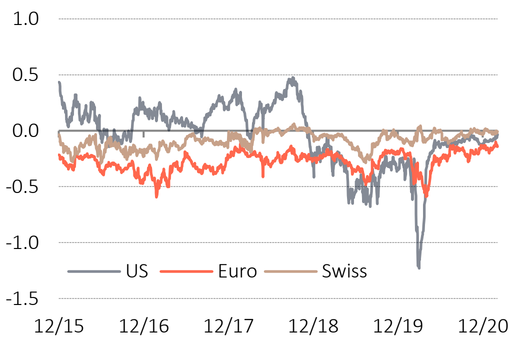
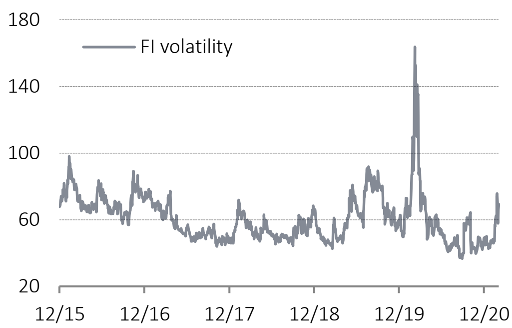


Fig 12: Merrill Lynch volatility index (MOVE)



EQUITIES

Equity markets performed well in February, although part of the gains was erased in the last week of the month when markets sold-off. Market participants became concerned that rising bond yields might derail the positive outlook for stocks. Cyclical stocks started to outperform as the technology sector is more interest-rate sensitive. This could be the beginning of a more pronounced rotation away from technology stocks into cyclical and value stocks. The Chinese equity market came under selling pressure as markets worried that the Chinese government could reduce stimulus measures.

Fig. 13: MSCI equity indices – major regions

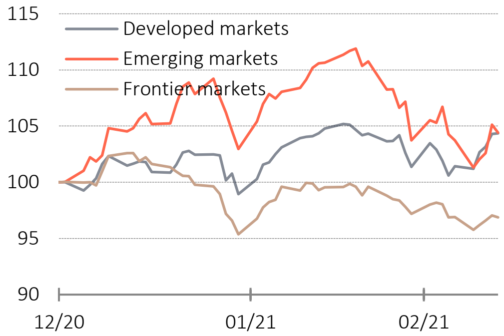


Fig.14: Equity indices – major developed markets

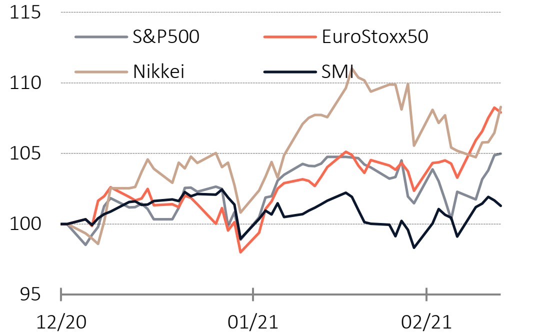


Fig 15: Equity indices – major emerging markets

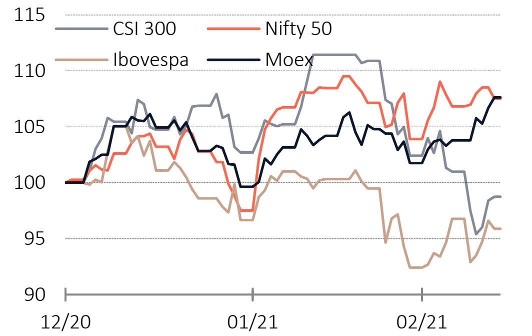


Fig. 16: Sector performance, MSCI Europe, YTD

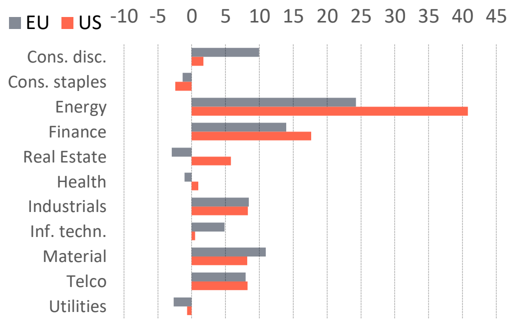


Fig 17: Price-earnings ratios

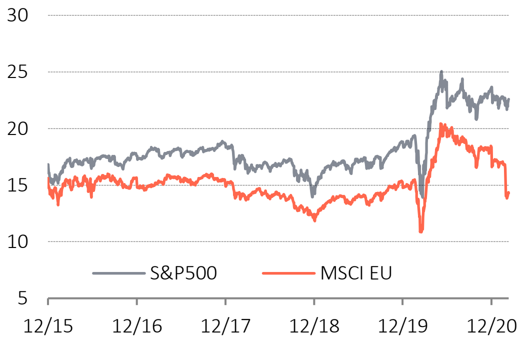
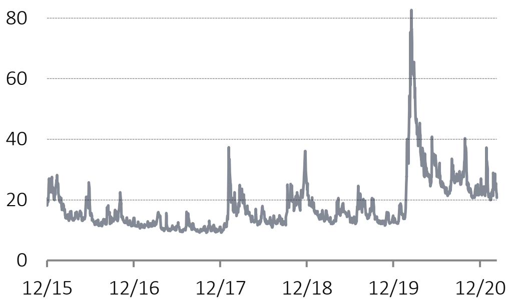


Fig 18: Equity volatility – S&P500 VIX index



ALTERNATIVE INVESTMENTS

The price of gold fell significantly in February on the back of rising real rates. At the same time, oil and industrial metals rallied sharply due to better growth prospects. Oil was supported by the fact that OPEC+ countries kept oil supply tight. Saudi Arabia even cut its production voluntarily below the level agreed with OPEC+. REITS, which are often believed to be sensitive to rising interest rates, performed well in February. The Global REITS index climbed 3.7%. The expected economic normalization outweighed rising funding costs.

Fig. 19: Gold price, USD/oz

Fig.20: Brent oil price, USD/bl

Fig 21: Bloomberg commodity indices

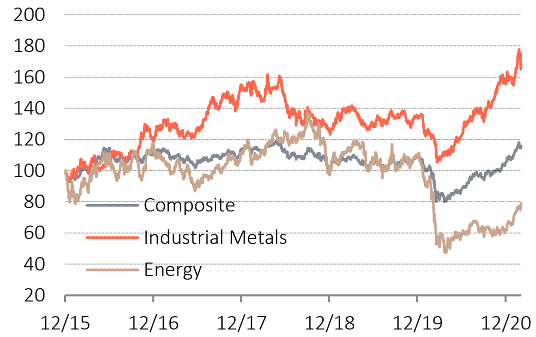


Fig. 22: HFRU hedge fund indices

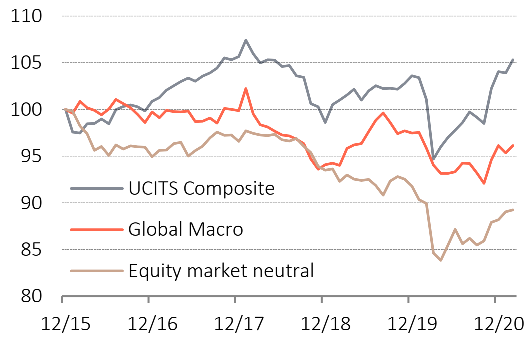


Fig 23: FTSE EPRA/NAREIT global REITS index

Fig 24: LPX global listed private equity

CURRENCIES

The USD continued to strengthen somewhat in February. The GBP continued to trend up strongly. The Chinese CNY took a breather and stabilized after a strong persistent upward trend since May 2020. The risk-on environment reduced the attractiveness of safe-haven currencies. As a result, the JPY and the CHF weakened. At the same time, the CAD and the AUD gained on the back of the commodities rally.

Fig. 25: EUR-USD exchange rate

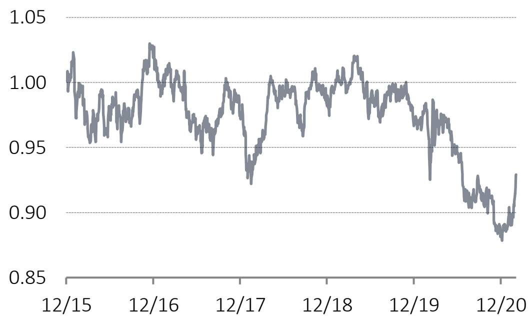
Fig. 26: GBP-USD exchange rate

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 pandemic has infected 120 m people with 2.7 m fatal outcomes. The rollout of the vaccines continues. Globally 345 m doses have already been administered, more than 100 m of these in the US alone. Europe is lagging behind with a slow start to the campaign. Meanwhile in many countries new, more infectious variants dominate among the new cases. The US congress finally approved Biden's USD 1.9 tn fiscal package to further support the economy.

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

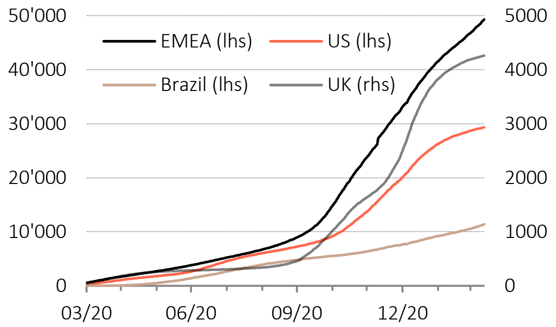


Fig. 32: New cases per day (7-day average)

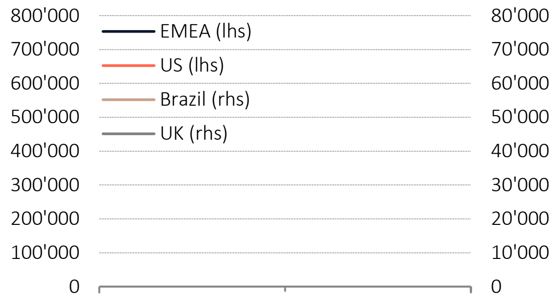


Fig 33: Global vaccination campaign (doses per 100 people)

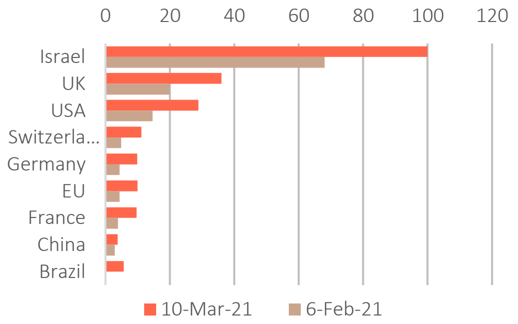


Fig.34: Central bank total assets (indexed)

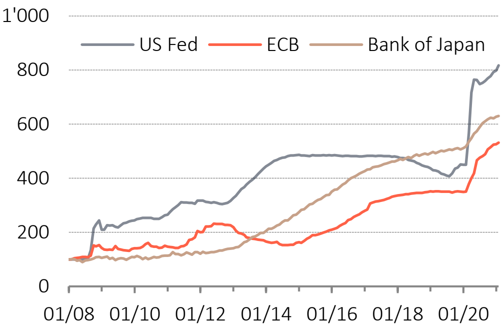
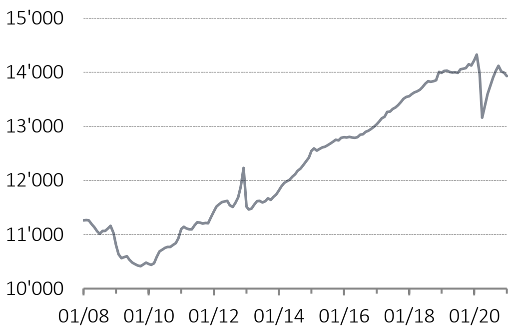


Fig 35: US bankruptcy index

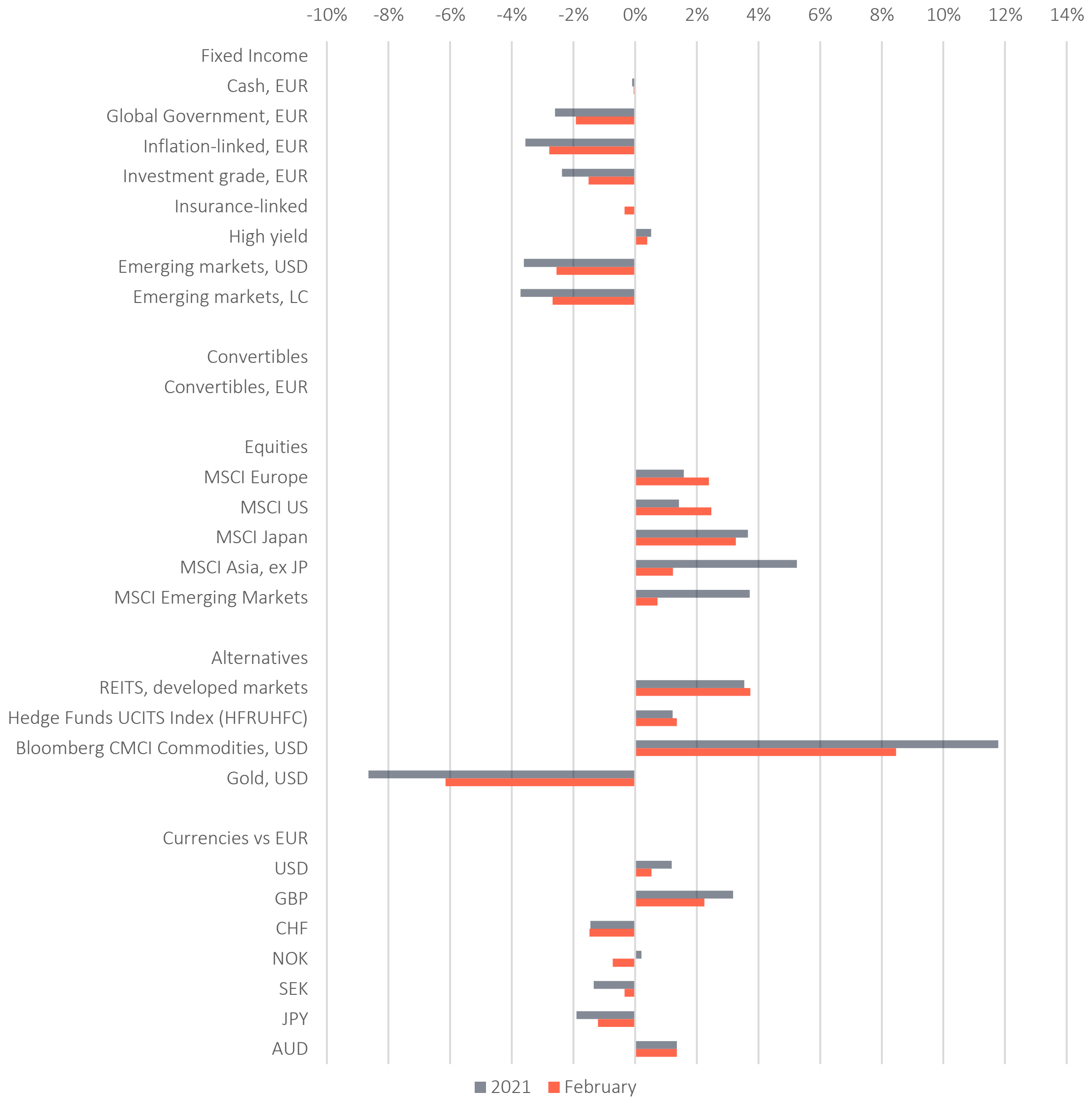
Fig 36: US personal income, excl. transfers (USD bn, 2012 prices)



ASSET ALLOCATION

Risky assets, especially equities and commodities, performed well in February, driven by better growth prospects. At the same time, inflation expectations rose, which pushed bond yields higher and bond prices down. Rising yields proved to be challenging especially for technology companies, since discount rates have a significant impact on valuations in this sector. Despite rising yields REITS performed well in February. Gold sold off and lost about 6% in the month. The USD and the GBP appreciated vis-à-vis the EUR.

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

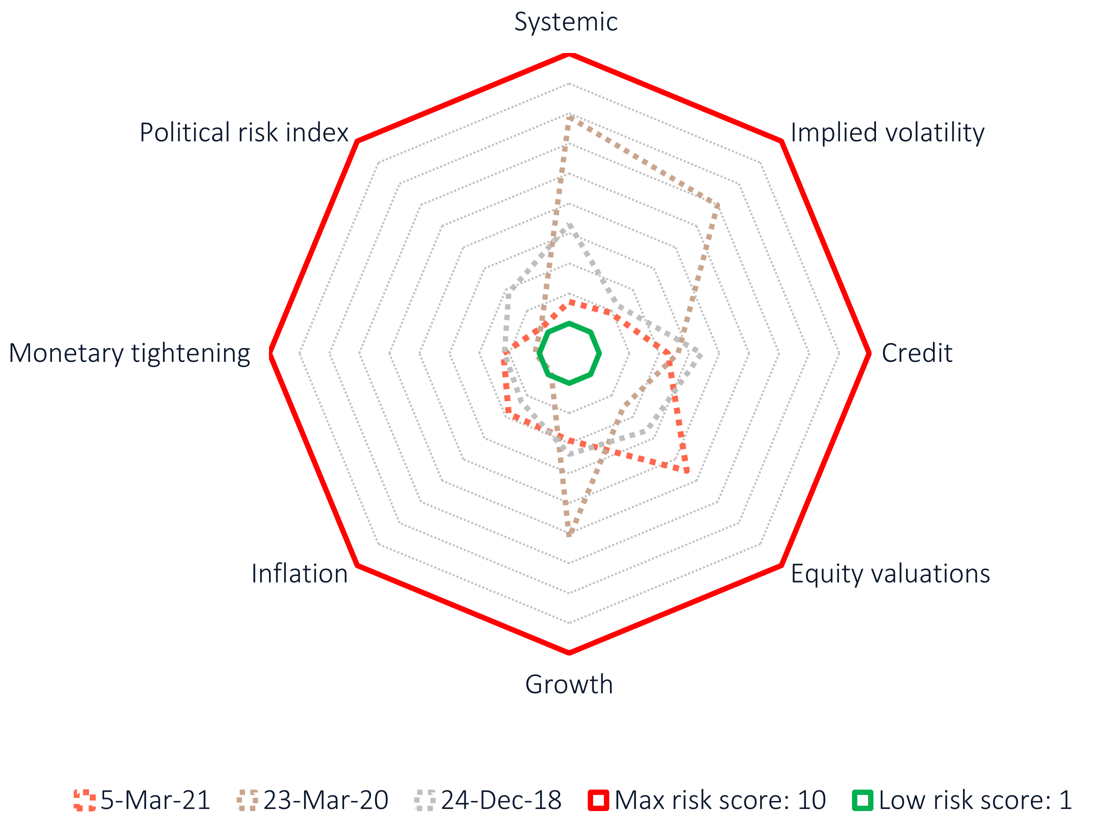


RISK MONITOR

Equity valuation risks remain elevated, although index levels disguise major differences between sector-specific valuations. While technology companies exhibit very rich valuations, there are certain sectors, especially cyclical sectors with more attractive valuations. Recently growth risks subsided, whereas inflation risks have been rising. Political risks remain low. The new US administration has helped to reduce geopolitical risks significantly.

Fig. 38: IMT Risk Monitor

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



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