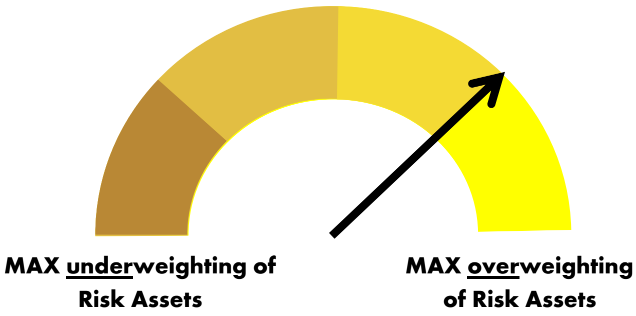
# ASSET ALLOCATION

## RB Asset Management 2Q/2021

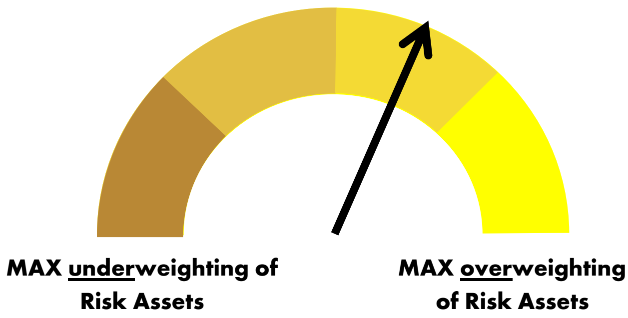
PĚTIHVĚZDIČKOVÁ BANKA
K VAŠIM SLUŽBÁM

KLIENTSKY
NEJPŘÍVĚTIVĚJŠÍ BANKA
2015–2019

**Current Asset Allocation**




**Expected Asset Allocation in 2Q/2021**




Source: Raiffeisenbank a.s., Asset Management, data valid as of 08.04.2021

Dear Clients,

Financial markets have entered the new year showing optimistic moods. The on-going Corona virus vaccination and envisaged strong economic recovery have led to growths in equity and alternative markets in particular. Equities have appreciated in the order of percentage units since the beginning of the year, while some indices have even reached their new historical highs (for example, the U.S. S&P500 Index). At the same time, though, anxiety has been increasing about potential higher inflation and higher interest rates. However, such concerns have already been played down by statements from central banks, the U.S. FED in particular. The FED voiced it many times before that it would tolerate higher inflation, and therefore it would not be necessary to raise interest rates in the foreseeable future.

While central banks influence short-term rates mainly by their reference rates, it is the market itself that affects medium-term and long-term rates. And it has been in this area that we have witnessed certain significant shifts: e.g., the yield of the ten-year U.S. sovereign bond has increased by almost one percent over the several few months, thus reaching its current rate of 1.70 percent. Such growths in bond yields reduce attractiveness of equities since investors consider the option of moving to safer waters of sovereign bonds.

A link between bond yields and stock returns will be important in the coming period as well. If bond yields continue to grow, this fact may represent a significant factor resulting in slower growths recorded on equity and alternative markets or potentially even corrections of their prices. Yet another limiting factor may be represented by higher corporate taxes imposed on U.S. firms by the Biden Administration. On the other hand, we will probably still be able to see strong economic data and very decent economic results reported by companies; the season for releasing results for the first quarter of this year begins these days.

We plan partial collection of profits from our equity positions in the coming period; we thus intend to make use of the currently high prices prevailing in equity markets, while taking into consideration slightly increasing risks. At the same time, though, we perceive a very strong positive trend existing on both equity and alternative markets, supported by similarly strong economic growths; therefore we shall maintain moderate overweighting in equities against bonds.

We wish you much success in the coming period.

***Mr Michal Ondruška, Manager, Asset Management***

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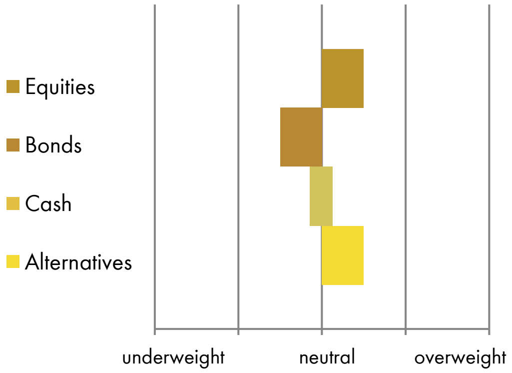
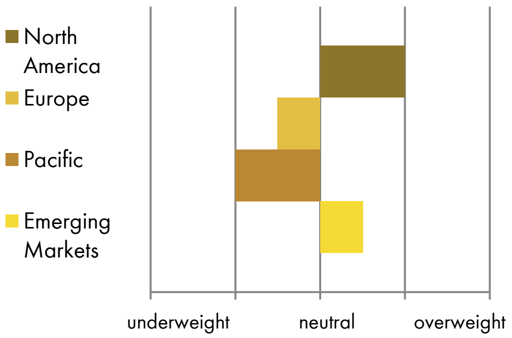
## TACTICAL ASSET ALLOCATION – ASSET CLASSES



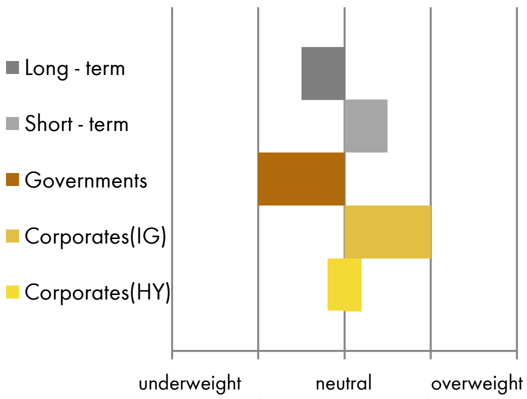

The individual incentives for economic recovery as mentioned in the previous report have been positively reflected in higher estimates of economic growth, especially in the United States, where the rate of vaccination also significantly exceeds the European pace. This trend boosts inflation expectations and increases as a result sovereign bond yields; specifically the U.S. 10-year Treasury offers a yield of 1.7 percent, which is 0.8 percent more than the figure used to be at the beginning of the year. Although stock indices have been breaking historical records, the strength of the current economic recovery and expected profits generated by companies represent good reasons for such developments. According to RBI estimates, profits reported by companies listed on stock exchanges in Europe and in the United States will grow by more than 25 percent this year and therefore they may well exceed the levels recorded before the crisis. As part of our tactical allocation, we continue to prefer equities and other risk assets against sovereign bonds. In view of increasing bond yields, their attractiveness is higher than before; therefore we have reduced the overweight rate. Alternative investments, for example, in commodities and in private equity, will serve as tools for portfolio diversification.

## TACTICAL ASSET ALLOCATION – EQUITY REGIONS




We continue to be overweight in the United States and in emerging markets in our models. On the other hand, we have been underweight in the Pacific and still less in Europe. Our exposition in the U.S. equity markets represents approximately 62 percent of the risk portion of our portfolios. We hold around 10 percent in the Nasdaq technology index. At the same time, we are overweight in the Financial, Industrial, Health Services, and the Consumer Durables Sectors. Also, we have been represented in enterprises with low market capitalisation ('small caps'). Our stakes in the European equity markets equal 14 percent. And we hold 5 percent in the Pacific, including Japan, and approximately 19 percent in the emerging markets.

## TACTICAL ASSET ALLOCATION – BONDS




The chief global central banks (FED and ECB) have repeatedly assured markets about their intentions to do their utmost in order to maintain low costs of financing and to supply the financial system with liquidity, even to tolerate potential higher inflation for a certain period of time. Different speed of vaccination in the United States and in Europe brings about differences in the expected pace of recovery, and/or inflation, thus resulting in varying shapes of bond yield curves, which are significantly steeper in the United States. The yield curve of Czech sovereign bonds has also been shifted upwards, since the yield of the 10-year bond jumped over 2 percent. The Czech National Bank has commenced making the market ready for increased rates, probably not later than some time this year.

As compared to the benchmark, we have been maintaining shorter average term to maturity (so-called 'duration') and we have been tactically overweight as regards the share of creditworthy corporate bonds.

Source of data in charts: Raiffeisenbank a.s., Asset Management, dtata valid as of 8. 4. 2021.

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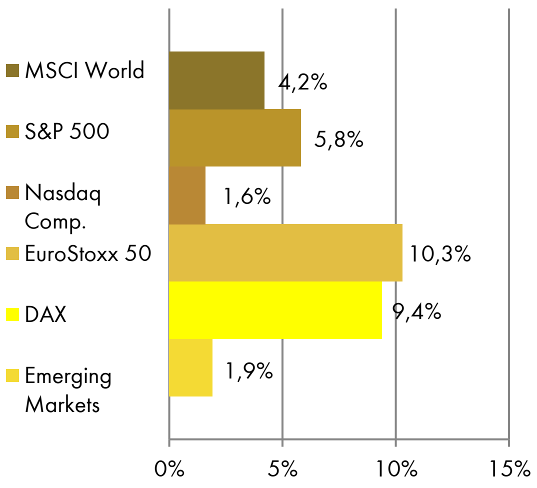
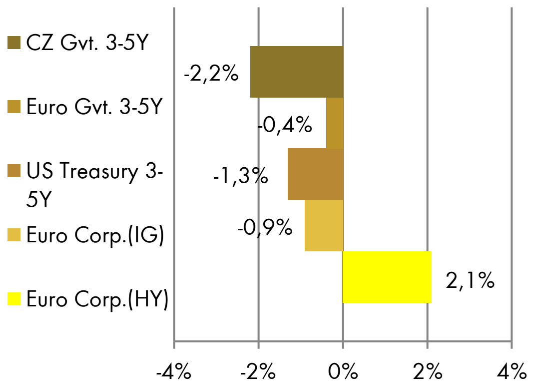
# ECONOMIC SITUATION AND MARKET TRENDS



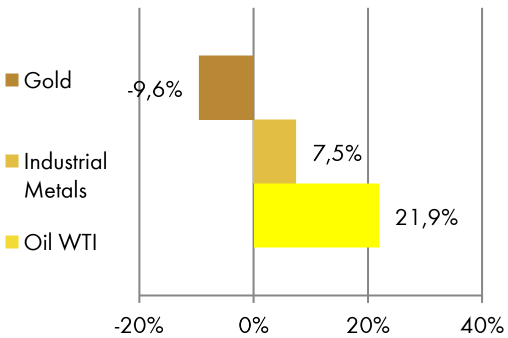

## EQUITY

Equities followed the positive sentiment experienced at the end of the previous year in the first quarter of this year. The markets regarded positively any envisaged significantly increased corporate profits and the economic revival. All equity indices of importance have reported profit. The largest global equity market (that in the United States) has added decent 5.8 percent, measured by the S&P 500 Index. The Nasdaq Index of technological firms, following a correction applied in the course of the quarter, has increased a mere 1.6 percent. The equities 'rallye' was dominated in the past quarter by European shares, with the Euro Stoxx Index gaining 10.3 percent and the German DAX index adding 9.4 percent. Emerging market equities performed slightly less, with their index gaining 1.9 percent.




## BONDS

The awaited rapid economic recovery, combined with the threat of higher inflation, had a negative impact on some bond prices. Czech sovereign bonds, in particular, were under pressure this past quarter, having written off 2.2 percent due to the expected early rate hike. A similarly negative trend was also characterised for European corporate bonds (-0.9 percent) and prices of European (-0.4 percent) and U.S. sovereign bonds (-1.3 percent). On the other hand, perhaps surprisingly good performance was reported in respect of European high-risk bonds. The High Yield Bond Index added 2.1 percent.




## COMMODITIES

The first quarter experienced an interesting development regarding prices of gold. The yellow metal wrote off 9.6 percent over the period in question. Investors probably decided to get rid of it due to the calming down of the situation around the Corona virus, so they shifted funds in favour of shares or bonds. A relatively favourably 'expanded' industry boosted demand for industrial metals, which trend was reflected in prices (+7.5 percent). The oil prices increased fairly significantly, as the U.S. WTI added 21.9 percent, having ended up at the price of 59.16 USD per barrel.

| | **31/12/20** | **31/03/21** |
|---|---|---|
| EUR/CZK | 26,24 | 26,12 |
| USD/CZK | 21,47 | 22,27 |
| EUR/USD | 1,2216 | 1,1730 |

## CURRENCIES

The Czech koruna (crown) weakened against the dollar by 4 percent in the course of the quarter. It was traded at the end of the quarter for a roughly similar price for the euro as it did in December, when the trading ended at the rate of 26.12 CZK per 1 EUR. The dollar added up approximately 4 percent against the euro in the period in question. It would be interesting to watch the relationship of this currency pair and how it will be affected by the growing interest rate differential between the euro area and the United States.

Source of data in charts: Bloomberg. Performance of individual assets is measured in the primary currency of the given instrument in the first quarter of 2021.

## FUTURE OUTLOOK

The most closely monitored S&P 500 Index increased by 5.8 percent in the first quarter of this year and it has thus reached its new historical high. Among the sectors, the best performing in the past quarter were the Energy (+30.8 percent), Financial (16.0 percent), Industrial (11.5 percent) and Telecommunication Services Sectors (+8.8 percent). On the contrary, the worst performing sectors listed the Utilities (+3.7 percent), Health Services (+3.3 percent), Technologies (2.3 percent) and the Short-term Consumption Sectors (+1.8 percent).

The VIX Volatility Index has reached the value of under 20 after some long time, which indicates a certain calming down of the equity markets and a gradual return to normal. Rumours had it at the end of March that some banks (e.g., Credit Suisse, Nomura) might report less favourable economic results because they had failed to sell in time some shares following the 'margin call' from the Archegos Capital hedge fund, which had not managed to supply banks with sufficient cash required to cover its losses from equity positions held on debt. Allegedly, the U.S. banks Goldman Sachs and Morgan Stanley were able to sell out their stock positions in time.

Investors remain to be focused on global inflation. The yields of the ten-year U.S. sovereign bond increased in one month by more than 0.20 percent, thus reaching in excess of 1.70 percent. Similarly, the yields of the ten-year Czech sovereign bond exceeded 2 percent. While the FED does not plan any increases of the interest rates either this or next year, the Czech National Bank has already indicated possible double increases in the second half of this year.

Investors will focus this month on economic results recorded by firms in the first quarter of 2021. The envisaged aggregated increases in profits generated by the S&P 500 Index companies has reached 23.8 percent, y/y, and in the case of revenues, the figure stands at 6.3 percent, y/y, in the first quarter of 2021 (*Source: FactSet*).

As regards the entire year, expectations have it that an aggregated increase of profits of the S&P 500 Index corporate profits should amount to 25.9 percent, y/y, and of revenues by 9.9 percent, y/y. At the same time, analysts anticipate rotations of sectors resulting from a higher growth of profits generated by the cyclical sectors and a somewhat steeper yield curve as against last year.

The expected P/E of 21.9 in respect of the next 12 months is higher as regards the S&P 500 Index than its five-year average of 17.8 (*Source: FactSet*). Although the yield of the ten-year U.S. sovereign bond has increased to the current approximately 1.70 percent, its value still remains relatively low, something which – combined with higher profits – should further support stock markets, too. Both in the United States and in Asia, the number of people infected with the Corona virus has been decreasing, and also the vaccination process of their inhabitants has been relatively quick, which has resulted in a gradual return to normal.

Our portfolios were overweight in the first quarter and, in view of the possibility of higher rates being imposed, we have kept shorter average maturity of bonds in the whole in our portfolios, as against 'benchmarks'. We plan to reduce our overweight high-risk instruments in the coming quarter. The markets still see prime risks in potential increases of corporate taxes in the U.S.A., stricter business regulation, and subsequent slowing down of economic growth. Yet another risk for the equity markets and corporate bond markets has been still seen in slow distribution of sufficient quantities of the Covid-19 vaccine or its lack of effect on new virus mutations, and potential rift in the U.S.-China trade relations.

Outlook by Raiffeisenbank a.s., Asset Management, regarding the individual asset classes in 2Q/2021:

| EQUITIES | BONDS | CASH | ALTERNATIVES |
|---|---|---|---|
| USA, EMM Asia | Bonds < 3Y | Cash, Term deposits, Savings accounts | Energy, crude oil |
| Technology, Healthcare, Finance, Industrials, Consumer Discretionary, Dividend-paying shares segment | Bonds> 3Y | | Real property |
| | Credit | | Gold |

| KEY: | POSITIVE EXPECT. | NEUTRAL EXPECT. | NEGATIVE EXPECT. |
|---|---|---|---|

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Officer in charge: Mr Michal Ondruška, Manager, Asset Management.