COMMENTARY ON THE CURRENT SITUATION FACING FINANCIAL MARKETS 03/2021

Prague, dated 1.3.2021

Inflation Fears Boost Investor Uneasiness in Financial Markets

The closest watched S&P 500 Index dropped by -1.0 percent in February. Among the sectors, the best performing were the energy sector (+18.2 percent), the finance sector (+8.1 percent), and the industrial sector (+4.0 percent). On the other hand, not so well performing were the utilities sector (-8 percent), the consumer durables sector, and the short-term consumption sector (-5.5 percent and -4,6 percent, respectively).

The VIX Volatility Index went up to the value of 29 towards the end of the month, which indicated more disquietude on the part of investors. This restlessness mainly resulted from fears of potentially growing global inflation. For example, the yield of a 10-year U.S. sovereign bond increased in the course of month by a significant +0.40 percent, thus reaching the value of 1.50 percent. Such rapid growth of bond yields has also caused slight corrections occurring in the stock market, but also, for example, in the price of gold. Investors' fears of inflation have also been supported by rising commodity prices, such as those of oil, electricity and industrial metals (e.g., copper, nickel), and – last but not least – by rising transport costs. All this has boosted the prices of both input raw materials and final products and services. In addition, fiscal packages adopted by individual governments will have caused more money to circulate, which may also push inflation upwards.

Investors have also been eyeing closely economic results generated by corporations last year. Some 96 percent of U.S. firms have already disclosed their economic results. So far, the aggregated decline of profits of the S&P 500 Index firms amounts to -11.2 percent, y/y; as regards last year's revenues, the figure stands at -1.0 percent, y/y (*Source: FactSet*), which, however, means a lesser decline than expected by analysts. In the last quarter of the previous year, 79 percent of the companies included in the S&P 500 Index generated better than expected profits and 76 percent firms collected better than expected revenues. Moreover, analysts have improved their expectations regarding increases of both profits and sales this year.

The anticipated S&P 500 Index P/E of 21.5 in respect of the future 12 months is higher than its five-year average of 17.7 (*Source: FactSet*). Although the yield of the ten-year U.S. sovereign bond has increased from approximately 1.1 percent at the end of January up to the current 1.50 percent, its value remains low, something which should further support stock markets.

The markets has still seen risks in potential increases of corporate taxes and stricter business regulation, and subsequent slowing down of economic growth in the United States. Yet another risk for the equity markets and corporate bond markets has still been viewed in slow distributions of sufficient quantities of the Covid-19 vaccine or its lack of effect against on new mutations.

Mr Michal Ondruška
Manager, Asset Management

We remain overweight in equities as regards discretionary portfolios. We overweight U.S. equities and those from emerging markets, in particular those in Asia. We prefer cyclical sectors, we overweight technologies, finance, Industry, and consumer durables. As concerns bond strategies, we stick to short durations; we see this strategy as suitable and effective, especially during these days characterised by growing yields. At the same time, we overweight the share of corporate and so-called high-yield bonds as against sovereign bonds.

Also the investment strategy applied to the funds managed by RIS was not altered in February. The funds, as compared to their so-called neutral distribution, were also overweight in equities against bonds – e.g., as regards strategies with neutral stakes of equities at the level of 30 percent of the total assets, their portion stagnated month-to-month at 39 percent; at the same time, it fluctuated in the interval of 38-40 percent in the course of the reported period. This decision, combined with suitably selected territorial and sectoral allocation of the stock portion of the portfolio, has so far contributed to better absolute as well as relative performances as compared to the market. As regards bonds, because of fears of the speeding up of inflation after the end of the Pandemic and because of fears of rather earlier increases of the key interest rates published by (not only) the Czech National Bank, we continue to prefer short-term and medium-term bonds as against their counterparts with longer maturities. We have also tried to make use of the stronger feelings of uneasiness on the part of investors and prise fluctuations in respect of, in particular, higher risk instruments, in order to profit from short-term trading. In this manner, we were repeatedly purchasing and selling for higher prices in February, e.g., stocks issued by the manufacturer of graphic cards Nvidia or ETFs focused on shares of gold miners VanEck Vectors Gold Miners. As regards the bond portion of our portfolios, it is worth to mention purchases of CZK bonds issued by Banco Santander of Spain, with the yield of 1.65 percent p.a. After the Czech crown depreciated against the EURO by almost 2 percent, which occurred in the second half of February, we increased the rate of currency hedging applied by us at the rate of 26.2 CZK/EUR at the very end of the month.

We wish you much success in the days to come.

For the Asset Management team,

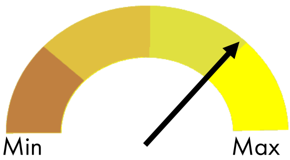
Mr Michal Ondruška

Summary of Investment Strategies :

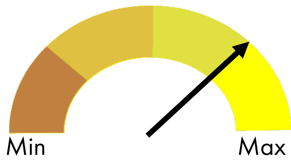
Tactical Allocation

Equity overweight portfolios

Current



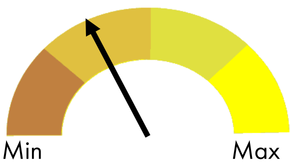
3M outlook



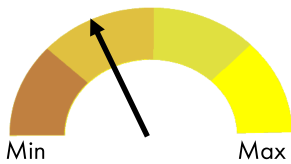
Interest Rate Risk

Average bond maturities (Duration)

Current



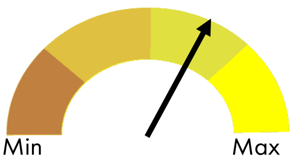
3M outlook



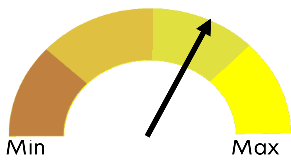
Credit Risk

Portions of, e.g., corporate bonds

Current



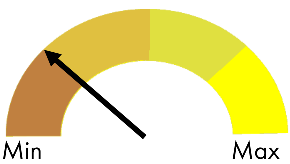
3M outlook



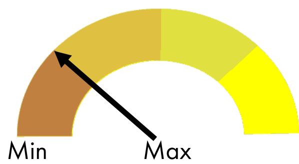
Currency Risk

Unsecured positions in foreign currencies

Current



3M outlook



Source: Raiffeisenbank, a.s., Asset Management, information valid as of 1.3.2021

Raiffeisenbank a.s. Hvězdova 1716/2b, PO box 64, 140 78 Praha 4, tel.: +420 234 401 111, fax: +420 234 402 111, e-mail: info@rb.cz, www.rb.cz, IČ: 49240901, zapsaná v obchodním rejstříku vedeném Městským soudem v Praze, oddíl B, vložka 2051

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