INFORMATION FOR INVESTMENT PROFESSIONALS

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Market updates

Investment team updates | 12 March 2021

US equities

Markets

- Following the recent weakness in US equities – especially the growth end of the market – equities have rallied back this week to the point where the S&P 500 reached an all-time high at the close of trading yesterday (11 March). The tech-heavy Nasdaq has not yet recovered its losses but is still up 3% this week to the end of Thursday 11, but down around 5% from its record close in mid-February. On a year-to-date basis the S&P 500 has a total return of 5.2% and the Nasdaq 100 has returned 1.4%. However, these are far behind the small cap Russell 2000 which has a positive return of 18.6% this year.
- Key drivers behind this move have been the approval of the $1.9 trillion stimulus package which was signed into law by President Biden on Thursday 11 together with better-than-expected jobs data and a weaker inflation report which eased concerns about rampant inflation. The seasonally adjusted CPI increased by 0.4% in February. And the recent advance in 10-year treasury yields also cooled off, as this had also been impacting the high-growth stocks given the impact of the higher discount rate for their valuations.
- Taking account of the latest stimulus package, the total value of stimulus since the start of the pandemic now stands at around $5.5 trillion, of which $2 trillion remains as excess household savings above the long-term trend. This latent spending power in the system provides a catalyst for the recovery given the amount of pent-up demand, even if only some of it is translated into consumption.
- Unsurprisingly, cyclical sectors have been performing best given the positive economic recovery which is underway. Last week, for instance, energy stocks fared best given the recent rally in crude prices. Consumer discretionary and materials stocks have outperformed the wider market this week, which is in keeping with a reopening story.
- Positive progress in the vaccination effort has also improved the economic outlook. Yesterday (11 March) President Biden said that every US adult would be eligible for a vaccination by 1 May with a view to returning to normality by the 4 July holiday weekend.
- With earnings season mostly over, we witnessed a return to sales and earnings growth in Q4 following three consecutive quarters of earnings declines. This recovery in earnings came significantly ahead of expectations given that initial estimates had been for a further contraction across the quarter. Overall in 2020, earnings were down by 12% but expectations for 2021 are for earnings growth of 20%-25%. One feature of this earnings season has been that positive earnings surprises have generally not been rewarded by stock price rises, which have on average remained flat.

European equities

- Higher inflation remains a risk and is a natural consequence if economies recover strongly. This has caused a retracement in bond markets, and the trend in equity markets has tended to favour cyclical stocks rather than long-term compounding growth holdings.
- IPO volumes are healthy, and there are interesting opportunities in this area, particularly for small cap funds.
- ESG (environment, social and governance) has been a strong theme recently, with VW rejoining the United Nations Global Compact, a voluntary initiative based on CEO commitments to implement universal sustainability principles, and the EU's new fund classification and disclosure regime taking effect.

Fixed income

News

- On Wednesday 10 March US Consumer Price Inflation (Core) came in at only +0.1% month-on-month and 1.3% year-on-year, the third lower-than-expected reading in three months. The long term average is 2%, and the debate about inflation has been centre to market moves this year. This data, the last before distorted data from Covid-19 policy effects feeds through, ought to sooth fears – to an extent.
- Also in the US, on Wednesday 10 the House of Representatives approved President Biden's $1.9 trillion fiscal plan. Meanwhile, the NFIB Small Business Optimism index improved slightly, rising to 95.8 in February. Initial jobless claims fell 42,000 to 712,000 in the week ending 6 March, which is the best figure since mid-Q420.
- On the back of the stimulus package, and the ongoing roll-out of vaccines, the OECD revised global growth estimates higher to 5.6%.
- In the eurozone, Q4 2020 GDP was revised lower to -0.7% quarter-on-quarter (from +12.4% in Q3) led by consumption. But there was conflicting data from individual countries: France saw strong industrial production, rising 3.3% month-on-month in January; while Germany saw weaker industrial production in January, falling 2.5% month-on-month.
- In the UK, the Bank of England governor Andrew Bailey sees the risk of inflation as "increasingly two sided".

Markets

- Government bond yields were down and up this week. The US 10-year started the week (8 March) at 1.55%, dipped to 1.51% on 10 March before finishing yesterday (11 March) at 1.59%. Germany ended the week at -0.31%, up from -0.33% on 10 March.
- In credit spreads, based on BofA Merrill Lynch Bond Indices, Global IG circled the 100bps mark all week, starting it (8 March) at 100bps and ending it (11 March) at 101bps. High yield, meanwhile, moved tighter from 389bps to 383bps.
- Oil finished last week (ending 5 March) at $66.9 per barrel before peaking over the weekend and tracking down to $63.5 on Tuesday 9 March, with production suffering no negative effects from the Saudi Arabia attack on 8 March. It finished Thursday 11 March at $65.6 a barrel.
- In FX the euro strengthened slightly over the week versus the dollar, moving from 1.189 on Monday 8 to 1.194 on Thursday 11.

Multi-asset

- The $1.9 trillion economic relief bill passed its final hurdle, being signed by President Biden on Thursday afternoon. Despite not being a surprise, treasuries were sharply weaker overnight.
- The broader sell-off in sovereign rates markets continues to stoke fears of a policy mistake from major global central banks. However, this week's dovish tone at the ECB – alongside the Fed's flexible average inflation-targeting approach – seems inconsistent with markets pricing a premature policy tightening.
- While we expect a transitory rise in inflation, we don't see any clear evidence of an end to the longer-term disinflationary trends. Indeed, our relatively punchy economic growth expectations would support the premise that higher yields are reflecting a better economic outlook and could still prove risk positive – provided company earnings deliver as they are expected to.
- No changes were made to asset allocation views where we continue to favour equities and credit over core fixed income, with a preference for those equity markets with superior earnings forecasted.

Note: all data as at 11 March 2021, unless otherwise specified. Source: Bloomberg.