COMMENTARY ON THE CURRENT SITUATION FACING FINANCIAL MARKETS 02/2021

Prague, 1 Feb. 2021

Year Start Brings Higher Volatility to Equity Markets

Such higher volatility marking the equity markets has been contributed to lately by, in particular, minor investors who – upon mutual consultations on social networks – have been purchasing via low-cost brokers (e.g., Robinhood) low market capitalisation companies (e.g., GameStop), thus causing prices boosting in the order of hundreds of percent. Such activities have already hit badly even some hedge funds that were required to close down their short positions, suffering significant losses as a result. The Securities and Exchange Commissions (SEC) has already commenced investigations into such activities on the ground of suspicions of market manipulations.

Yet another factor causing uncertainty includes concerns about the size of the proposed fiscal incentives in the United States, to the tune of USD 1.9 trillion; such incentive could rather be lower, following an agreement to be reached between the Republicans and the Democrats. Also slow and insufficient distribution of vaccines and mutations in the virus, which can reduce their effectiveness, add up to a lack of peace of mind. The Volatility VIX Index increased to the value of 33 at the end of the month, which development indicates higher unrest on the part of investors.

The best watched S&P 500 Index has declined by -1.1 percent since the beginning of the year. Among the sectors, the best performing last month were the energy sector (+3.75 percent), the consumer durables sector (+0.77 percent) and the health services sector (+1.4 percent). On the other hand, the short-term consumption sector (-4.9 percent), the industry sector (-4.3 percent) and the financial sector (-1.8 percent) have ranked among the worst performing sectors.

Currently, investors have been focusing on last year's corporate economic results. The season of result disclosing has been in full swing, approximately half of U.S. companies have already published their economic results. So far, the aggregated decline in profits in respect of the S&P 500 Index has reached -12.3 percent, y/y, while revenues dropped -1.5 percent, y/y, (*Source: FactSet*); this figure, though, remains better than analysts' estimates. Judging from economic results so far published, 86 percent of the S&P 500 Index companies generated better than envisaged profit, while 82 percent of such companies also collected higher than estimated revenues in the fourth quarter of last year.

Moreover, analysts have improved their estimates regarding increases of both profits and revenues in 2021. This year, the aggregated profit increase in the S&P 500 Index is expected to reach 22.6 percent, y/y, while revenues should grow by 8.3 percent, y/y. At the same time, analysts anticipate rotations of sectors resulting from higher growth of profits generated by the cyclical sectors and a somewhat steeper yield curve.

Mr Michal Ondruška
Manager, Asset Management

The estimated P/E of 22.5 for the S&P 500 Index for the next 12 months is greater than its five-year average of 17.6 (*Source: FactSet*). Although the yields of the ten-year U.S. sovereign bond has improved from 0.9 percent to approximately 1.1 percent, its value remains low, which plays into the hands of equity markets.

The risks facing the markets remain those as before: Covid, potential increases in corporate taxes, stricter regulation, and/or the rift in the U.S.-China trade relations. Also, technical correction of the equity markets cannot be excluded, resulting from their major growths in the past months. If the markets were really corrected, we shall be seeing it as an opportunity for increasing some selected positions.

Higher volatility in equity markets in January allowed for achieving some profit from short-term deals in the fund portfolios. This applied, for example, to the exchange-traded Gold Miners ETF (GDX US). As far as new acquisitions are concerned, we have continued to apply the strategy of overweighting the U.S. equity markets and certain emerging markets, particularly those in the East Asian regions. We have also carried on purchases of companies capable to profiting from expansion of alternative resources. On the bond side, we have acquired – primarily due to maintaining diversification – some high-quality U.S. corporate bonds with short-term and medium-term maturities, and also – to a lesser extent – the U.S. sovereign bonds, which can participate in rising inflation (so-called TIPS),. On the contrary, January was very calm as regards the crown-denominated bonds market. Worth mentioning is only the purchase of a new bond issue of Net4gas Holding s.r.o. with maturity in 2028, and investment rating of BBB.

We do not expect to alter our investing strategy in the immediately coming period. We continue to overweight equity instruments; as regards regions, we will still prefer the U.S. markets and the emerging markets (primarily in Asia), while underweighting Europe and the developed Pacific region. In respect of sectors, we give priority to cyclical titles (e.g., industry, financial and IT corporations/ETF) to the detriments of defensive sectors (everyday consumer goods, public services, etc.). As concerns our strategies in the bond market, we overweight shorter and medium-term maturities and corporate bonds.

We wish you much success in the coming days.

For the Asset Management team

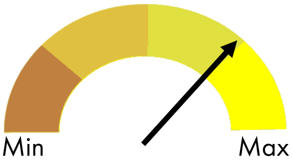
Mr Michal Ondruška

Summary of Investment Strategies:

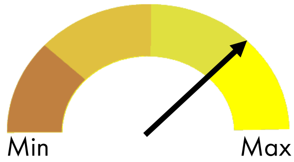
Tactical Allocation

Equity overweighed in portfolios

Current



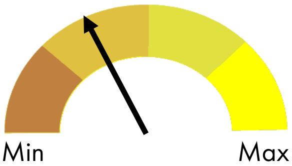
3M outlook



Interest Rate Risk

Average bond maturities (Duration)

Current



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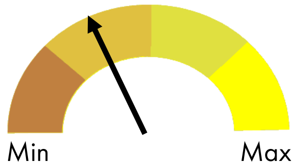
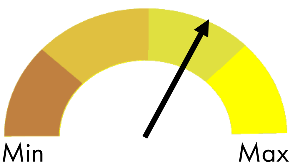


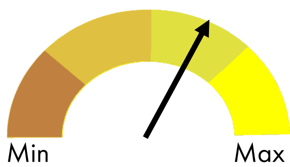
Credit Risk

Portions of, e.g., corporate bonds

Current



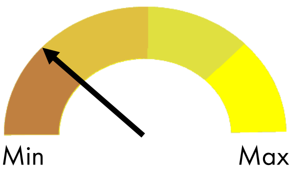
3M outlook



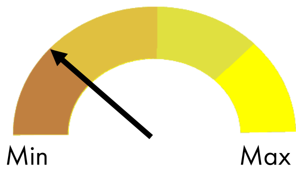
Currency Risk

Unsecured positions in foreign currencies

Current



3M outlook



Source: Raiffeisenbank, a.s., Asset Management, data valid as of 1 February 2021

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