Prague, 1 Dec. 2021

Omicron and FED Boost Financial Markets Fears

The most closely watched S&P 500 Index slightly declined by -0.9 percent in November 2021. Among the sectors, the best performing last month were the Technologies Sector (4.6 percent), the Consumer Durables Sector (-0.2 percent), and the Materials Sector (-0.5 percent). On the contrary, the worst-performing sectors included the Communications Sector (-6.3 percent), the Finance Sector (-5.8 percent) and the Energy Sector (-6.6 percent). The VIX Volatility Index has again exceeded its long-term averages following the discovery of the new Corona virus strain, which indicates stock market uncertainty. The 'Omicron' Corona virus strain might be more infectious, however, according to latest information, it should not cause such severe a course of the disease as its previous mutations have. Nevertheless, the 'Omicron' has not been completely investigated into as yet and vaccines have allegedly not been so effective against this virus strain.

The equity markets began correcting their previous growth trends upon the locating of the Corona virus strain. Such corrections have also been upheld by FED's boss, Jerome Powell, who has indicated that restrictions of 'quantitative easing' in the United States might be faster than originally expected. The FED head also mentioned it to have eliminated from his vocabulary the term 'transitional' inflation, since it would have been here with us during the entire year 2021 and it should not begin to fade until in the course of 2022.

Although inflation has been higher than envisaged by analysts, and not only in the United States but also in Europe, the yield of the ten-year U.S. sovereign bond slipped from 1.6 percent to approx. 1.5 percent at the end of November. The previous facts make it clear that investors have started to look for 'safe harbours' after some prolonged time. Drops in bond yields have helped technological equities and, on the contrary, they have harmed bank titles. Expectations have it that the Czech National Bank would respond to higher inflation by yet another hike of the base interest rate, which has now been set at 2.75 percent. In the Czech Republic, the yield of the ten-year sovereign bond dropped moderately in November as against October; it now fluctuates slightly under 2.6 percent.

The envisaged P/E of 21.4 in respect of the next 12 months is higher for the S&P 500 Index than its five-year average of 18.4 (*Source: FactSet*). Nevertheless, the yield of the ten-year U.S. sovereign bond remains relatively low, while the aggregated growth of the S&P 500 Index corporate profits stays high at 21.1 percent, y/y, also in the fourth quarter of 2021. According to expectations regarding this entire year, the aggregated S&P 500 Index corporate profits should go up by 44.9 percent, y/y, and revenues by 15.9 percent, y/y (*Source: FactSet*). Next year, both corporate profit and revenue are not expected to increase more than at a single-digit rate.

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The most significant change regarding our managed RIS portfolios in the past month was that of extending 'duration' (simply speaking: the average term to maturity relating to bonds that we have held). We were keeping it at a very low level for practically the whole year, as a result of which this year's (almost 8-percent) slump of the Czech bond market has only had relatively limited effect on the performance of RIS funds. However, as the markets have gradually began to abandon their expectations of continuing major rates hikes by the Czech National Bank over the past weeks, we have re-assessed our approach and decided to extend durations cautiously. Making use of attractive prices (following some previous deep drops) we have purchased in our portfolios, e.g., ten-year sovereign bonds with a fixed coupon and maturity in 2031. In contrast, we were selling, for example, variable coupon bonds linked to movements of short-term interest rates. We have seen that this strategy has been correct in the course of the last November week, having witnessed investors' fears regarding the new Corona virus strain, the Omicron, and resulting shifts of investments from high-risk assets (shares, etc.) to 'a relative safety' of sovereign bonds, particularly those with longer maturities.

We have made use of increased volatility in stock markets in order to realize some short-term trading profits. In this manner, we have managed to gain several percents of profit by purchasing and then selling after a couple of days (or vice versa), e.g., such instruments as 'iShares STOXX Europe 600 Banks UCITS ETF', and/or 'Lyxor MSCI Russia UCITS ETF'. In response to the last few days' developments, we have eased this year's successful over-weighting of shares from the Finance Sector, namely, by selling off shares in Komerční banka, whose growth potential has been exhausted to a large extent in our opinion, in view of the fading off expectations of major increases of the interest rates by the Czech National Bank (and/or, even their reduction in the second half of next year).

Summing up our investment strategies, we continue to over-weight equities in our managed portfolios and funds; at the same time, we keep buying regularly Czech sovereign bonds with longer maturities. As far as equities are concerned, we give priority to growth regions, such as the United States market, and growth sectors, such as Technologies, Long-term Consumption and Industry.

We wish you much success!

For the Asset Management team

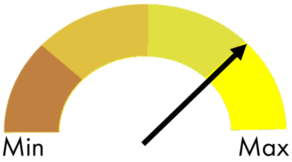
Mr Michal Ondruška

Summary of Investment Strategies:

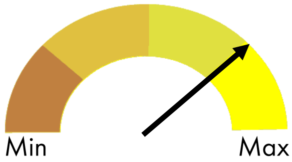
Tactical Allocation

Equity overweighted in portfolios

Current



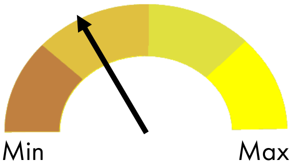
3M outlook



Interest Rate Risk

Average bond maturities (Duration)

Current



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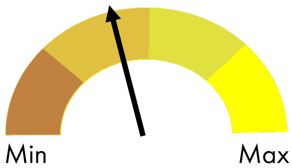
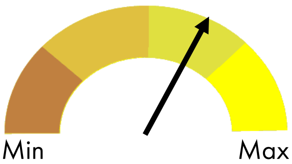


Credit Risk

Portions of, e.g., corporate bonds

Current



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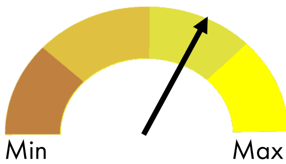
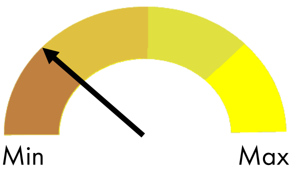


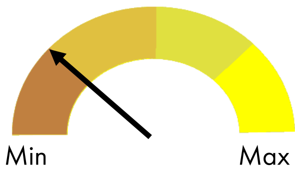
Currency Risk

Unsecured positions in foreign currencies

Current



3M outlook



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

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