Prague, 20 April 2020

Commentary on Current Situation Facing Financial Markets

The equity markets kept strengthening also in the past week. The S&P 500 equity index also increased last week, having added more than 3 percent. The season of disclosing economic results has already been running at full speed. Banks recorded rather weaker results than expected. For example, JP Morgan created significantly higher provisions for loans than expected by the market, mainly due to potential defaults on the part of shale miners. It have particularly been the WTI oil prices that remain under strong selling pressure; at the current price below USD 15 per barrel, they are currently at their lowest level in the past twenty years. Among sectors, the best performance was recorded by the health sector, the durable goods sector, and the technology sector last week. For example, the following equities ranked among the best performing in those sectors: Amazon, Gilead Sciences, AMD, and Nvidia. It was particularly the good news from Gilead Sciences concerning the favourable effects of the medicine named 'Remdesivir' that helped not only the company's equities, but the entire S&P 500 Index, because an effective remedy would mean the end to the restrictive measures and the reopening of business, services, and a start-up of the global economy. However, we shall have to wait another while before we can confirm the results of the healing effects of the medicine.

In the week to come, close attention will be paid to disclosures of more economic results achieved in the first quarter by further American and European companies. We shall see which companies and sectors will have performed. We cannot exclude higher market volatility, which may result both from such economic figures in respect of the first quarter results, and as an effect of the continuing oil prices drop.

Also, markets may feel affected by insufficient *cash flows*, mainly as regards certain small companies in the U.S.A.; therefore, negotiations have been under way about a new package in assistance of those firms in the volume of USD 350 billion. Potential recession resulting from the high indebtedness of certain individual countries, mainly in Europe (Italy, Spain), represents yet another risk affecting growths of the equity markets.

We consistently followed our investment strategy throughout the past week: we remained moderately overweighed as regards equities and other high-risk assets. We have complemented our managed portfolios with both broadly diversified equity risk-bearing instruments and conscientiously selected bets on certain individual enterprises. As regards mutual funds, we took advantage last week of the improving sentiment on bond markets and we slightly reduced the share of Czech-crowns-denominated bonds with a non-investment grade.

Summary:

- In the context of stabilisation of the pandemic, more and more countries have announced their **plans for economic revival**; this is a very favourable piece of news for financial markets.

- A new important factor enters the scene: **oil prices**, which have dropped more than 60 percent since the beginning of the year. This drop in oil prices affects negatively the energy sector as well as many specific countries and regions where oil mining represents a significant portion of their budgets.
- Beside the energy sector, also certain **secondary sectors** may be hit, especially banks which finance such mining companies ➔ threat of default.
- On the other hand, **such low oil prices represent a significant leading indicator of future economic growth**. Low oil prices bring profit to oil importers (e.g., China, India) as well as to a number of sectors, such as industry, transport, etc., and households.
- Low oil prices press for **lower inflation and lower interest rates** – again, a positive piece of news for both enterprises and households.
- A **season of disclosing the first quarter economic results** by enterprises has been under way; such so-called *hard data* may represent yet another source of higher market volatility in the weeks to come.
- The coming period will be characterised by **sector distribution** (allocation) of our managed portfolios – many sectors have been on the move, sometimes even in completely opposite directions – see, e.g., energy (oil mining) vs. health care.
- We invest in mid-term perspectives in financially strong and stable companies; we continue to give preference to the **sectors of health care and technologies, including the segment of dividend-bearing shares**.
- As regards short-term tactical positions, **we remain moderately overweighed** in the area of high-risk instruments.

We wish you much success in the days to come.

For the team of your portfolio managers.

Michal Ondruška
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