Raiffeisen BANK
Client inspired banking

Prague, 27 April 2020

Commentary on Current Situation Facing Financial Markets

We have witnessed gradual growths of the equity markets during the several past weeks; also the bond markets have shown a significant easing. Financial markets have received major support – not for the first time and obviously not for the last time, either – from central banks, in the forms of liquidity provisions, incentive interventions, and drastic interest rate cuts. The S&P 500 equity index first weakened at the beginning of last week. The reason behind such decline was primarily the unprecedented drop in the prices of May supplies of oil, down to a historic USD minus-40 per barrel. On the other hand, the equity markets began growing commencing in the middle of the week, supported by a U-turn in the oil prices, which have found (at least for now) a foot-hold in the form of a transition to a new benchmark contract with delivery in June. It was particularly the energy sector that performed best in the past week, having strengthened by almost 2 percent. Nevertheless, oil tanks at all refineries have remained practically full and the demand for oil has declined; this is why oil prices may continue to fluctuate in the short run.

The season of disclosing economic results has already been running at full speed and the results generated by individual companies have not been so bad so far, as against expectations. Such economic results have so far been disclosed by some 24 percent of the companies belonging to the S&P 500 index. Out of them, 60 percent of the enterprises generated better profit and revenues than expected. In total, profits dropped by 15.8 percent, y/y, in the first quarter, mainly due to falling bank profits.

This week, some giants are supposed to publish their economic results, such as PepsiCo, AMD, Microsoft, Alphabet, Boeing, GE, FB, Starbucks, Amazon, and Apple. At the same time, Fed plans to be in session on Tuesday and Wednesday. No changes in the interest rates are expected. The Fed benchmark rate has been set at 0.25 percent. The Bank of Japan will disclose its monetary decision on Tuesday. It is expected that the Japanese will keep their negative benchmark interest rate unchanged at -0.1 percent. Of special interest will be the first-quarter GDP figure in the U.S.A., to be published on Wednesday.

Raiffeisen Bank International (RBI) has increased its expectations regarding the values of certain selected equity indices; e.g., as regards the S&P 500 index, RBI now anticipates that it could reach 3,100 points at the end of this coming September. FactSet believes that the overall EPS (equity per share) of the enterprises belonging to the S&P 500 index will drop from approximately USD 165 to some USD 138 this year; nevertheless, such EPS will be boosted by more than 23 percent, y/y, next year, up to USD 170.4; this also represents a piece of good news for investors.

We have, so-called, overweighed the equity component of mixed funds in almost the entire past month. As a result, we have recorded higher participation in the increases generated by the equity markets. Last week, we proceeded to modestly collect some profits, by way of partial sales of major stock indices in Europe and in the U.S.A. As regards bond positions, we have also made advantage of higher prices of corporate issues and sold a portion of them; we have purchased some sovereign bonds instead. However, we remain relatively optimistic and maintain our portfolios slightly overweighed.

Summary:

- The impact of the current crisis on the corporate sphere begins to show in clearer outlines, **the expected values of corporate profits/revenues become more accurate** as regards the years 2020 and 2021.
- This is a favourable piece of news from the point of view of the financial markets because it indicates gradual **disappearance of uncertainties in the form of "unknown" effects** of the crisis. At the same time, it represents relatively **favourable figures**.
- **We continue to consider certain high-risk instruments as interesting investment opportunities**, both in the context of very low interest rates and yields of sovereign bonds, which may be less attractive in terms of expected return and risk.
- We expect the markets to remain volatile. This will at the same time create opportunities for **active trading** with mutual funds – see, e.g., selected profits last week.
- **We keep the portfolios slightly overweighed** as regards higher-risk instruments.

We wish you a pleasant and successful week.

For the team of your portfolio managers.

Michal Ondruška
Manager, Asset Management

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