MAPM: Markets weekly

25th March 2021

Summary

- Stock markets move lower with DM equities outperforming EM, with LatAm leading the losses
- The oil price whipsaws as COVID-19 lockdowns and Suez canal blockages play a growth narrative tug-of-war
- Global sovereign yields retreat, with US 10-year Treasuries around 1.65%
- Turkish President Recep Erdogan, surprises the market with the firing of another central banker governor

Market and Economic review

The week started off well with a rebound in global equities, driven by technology stocks, following the surge in bond yields last week. However, as the week progressed there was news of the ramping-up of COVID-19 lockdowns, most notably in Europe. In Germany, Angela Merkel took the unusual step of announcing Easter lockdowns, before U-turning on the decision days later. This week Belgium reintroduced stricter lockdown measures in response to a surge in new infections. The Eurozone has faced criticism of their slow response in procuring and the rollout of vaccines, as EU states have seen some of the deadliest outbreaks of the pandemic, with Italy recording more than 106,000 deaths, France 93,000, Germany 75,000 and Spain 73,000. Recent figures show just 12.9 doses of vaccine have been administered per 100 people in the EU compared with 44.7 in the UK and 37.2 in the US.

President Erdogan of Turkey surprised markets by ousting his hawkish central bank governor, the third change in as many years. The Turkish lira dropped c.10% vs the US dollar and Turkish equities fell 19% as fears of external capital flight and financial stability came back to haunt Turkish assets. As some may remember from a similar episode in 2018, European banks, which have Turkish subsidiaries were down, especially in Spain.

Switching focus to the US, news headlines were abuzz with potential $3trn additional fiscal spending above the $1.3trn already in train, in particular on infrastructure projects. Treasury Secretary Janet Yellen said the US economy remains in crisis from the pandemic even as she defended developing plans for future tax increases to pay for new public investments. Yellen said, with "a huge problem of joblessness" following the loss of employment due to the pandemic, "but once the economy is strong again President Biden is likely to propose that we engage in long-term plans to address longstanding investment shortfalls...in infrastructure, investment to address climate risk, investments in people, R&D, manufacturing," she said. Fed chair Powell has maintained his accommodative rhetoric, even as inflation fears rise which can be seen by the increase in breakeven inflation rates. Despite the positive fiscal and monetary policy news, risk-off sentiment remained. US equities broadly ignored the positive growth rhetoric from Yellen and Powell and edged lower – with energy and industrials being the worst performing sectors. Energy markets were also affected by sharp price moves in the oil price. As news of COVID-19 lockdowns were released, Brent fell c6% and on Wednesday as the Suez canal blockage became apparent, Brent was up 5%. Over the week, oil is down c.4.5% at about $61.5 a barrel. The rotation into Value stocks also took a pause for breath exemplified by the Russell 2000 index down c,9% from its 2021 high of 10 days ago. The US dollar continued its recent strength, benefitting this week from the risk-off sentiment.

Global government yields fell this the week benefitting from the risk-off sentiment, as opposed to being the cause of it. There were three Treasury auctions this week, which were relatively uneventful. There was solid demand for the $60bn 2-year auction, and average demand for the five-year notes. Thursday's 7-year bond auction echoed a similarly poor auction last month, which had been touted as a contributory factor behind the steep increases witnessed in government bond yields. This week's issuance came 2.5bps above the note's yield, which indicates weak demand relative to issuing it at par. Against this backdrop, 10-year yields moved 5bps higher this week to 1.65%.

Global PMIs releases were positive. In Europe, the Markit Composite PMI increased from 52.5 (vs expected 48.8) in March driven particularly by its manufacturing component. There was a slight decrease in the US PMI from 59.5 to 59.1, but it remains firmly in growth territory. In the UK, the unemployment rate decreased to 5% in January and CPI inflation fell to 0.4% (YoY) in February, with the main driver being the fall in clothing sales.

Movers

Equity	Current Level	WoW	YTD	YoY
MSCI DM	664	-1.13%	2.71%	55.25%
MSCI EM	1,288	-3.62%	-0.26%	54.02%
S&P500	3,910	-0.09%	4.09%	57.92%
FTSE 100	6,725	0.25%	4.10%	18.23%
Eurostox	3,859	0.57%	8.62%	37.80%
FTSE MIB	24,354	0.64%	9.54%	41.24%
US Value vs Growth	--	-0.14%	10.58%	5.03%
Government bond				
US 10 year Yield	1.66%	-6.3	74.5	79.1
US 2 / 10 Spread	1.52%	-4.4	73.3	99.2
Germany 10 Year Yield	-0.36%	-6.1	21.4	-9.3
UK 10 Year Yield	0.76%	-7.6	56.5	31.7
Italy / Germany 10 Year Yield	0.97%	1.1	-14.3	-83.6
Credit Spreads				
Barclays £ Corp TR Index	1.13%	-1.6	1.2	-170.5
Eur High Yield Spread (XOVER)	2.69%	25.1	26.2	-262.7
US High Yield Spread (CDX HY)	3.01%	-0.1	8.3	-356.2
EM $ Spread (CDX EM)	1.81%	-0.7	29.1	-121.8
Currency				
USD Index	92.75	0.90%	3.12%	-8.22%
GBPUSD	1.3768	-0.75%	0.70%	15.91%
GBPEUR	1.17	0.29%	4.43%	7.02%
EM FX Spot (JPM Index)	56.23	-1.83%	-2.58%	4.45%
Other				
Crude (1st Future)	63.43	-1.70%	22.45%	131.58%
Vix index	19.56	-1.4	-3.2	-44.4
Treasury Vol index (SMOVE)	62.76	-6.9	13.3	-25.7

Source: Bloomberg as at 09.00 on 26/03/2021

Outlook

Our positioning has remained largely unchanged in 2021 with an overweight to a diversified global equity basket. This is based on our continued positive view on risk assets and our belief that we are in the midst of a synchronised cyclical recovery. We maintain a small overweight to Emerging Market Debt, offering superior yields relative to US IG, where we moved underweight at the start of the year. We are closely focussed on the increased volatility in and level of US government bond yields. While absolute levels of yields are low compared to history, when such yields experience higher levels of volatility this unnerves markets. US Government Bond Yields represent the global discount rate for risky assets, and high levels of uncertainty about the level of this discount rate can dent sentiment in global markets. This week the risk-off sentiment was focused more around COVID-19-related news as opposed to rising yields (and yields were down over the week).

We maintain our view that a continued gradual increase in rates driven by an improving macro picture could be digested without material issue by risk assets. Equity markets should react positively to the increased US fiscal spending, especially as it ramps up as opposed to disappointing markets. However, continued volatility, and increased uncertainty about the stability of the discount rate may dent sentiment once again. We continue to watch our signals for a material change as it is clearly one of the key risk to markets in 2021.

Next week we US inflation and unemployment data, Japan's Tankan Survey, Euro Area inflation data and the Bank of England's credit data.