INFORMATION FOR INVESTMENT PROFESSIONALS

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Market updates

Investment team updates | 11 June 2021

US equities

Markets and economy

- Over the past two weeks (eight trading days to 10 June, with the market closed on 31 May for Memorial Day), the S&P 500 has mostly traded sideways, though was up yesterday (10 June) following the release of the CPI inflation numbers. Over this period the S&P 500 is up by 0.9%, bettered slightly by the Nasdaq and Russell 2000 which returned 2% and 1.9% respectively.
- Growth has outperformed value lately, although both made positive returns over the period. However, since the start of the year value is still comfortably ahead by around 8%.
- The main news this week was the release of the CPI inflation numbers on 10 June. On a year-on-year basis inflation was up 5% – the highest reading since the depths of the financial crisis in August 2008. Core CPI rose 3.8%, its highest level since 1992.
- With this elevated inflation backdrop in view, all eyes are on the US Federal Reserve and whether they will begin to introduce tapering, which will precede rate hikes. The majority of Fed officials remain confident that the present inflation surge is transitory and that it's too early to introduce tapering until further "substantial progress" has been made in the labour market, especially after two months of weak prints for non-farm payrolls. A gradual unwinding of the asset purchase programme could begin by the end of this year or early 2022, but rates are likely remain pinned near-zero until well beyond this.
- As President Biden looks to get his infrastructure deal through Congress, he has recently signalled his willingness to be flexible on tax increases, even to the point where he reduces the overall size of the package without a need for an increase in the headline corporate tax rate – a major sticking point for Republicans. Instead, a minimum 15% rate may be applied to ensure more companies pay a minimum level of tax instead of the situation where some US companies shift their tax liabilities to lower tax jurisdictions. Whether or not bipartisan negotiations succeed remains to be seen, especially as many Democrats will not be willing to accept the substantial reduction in the size of the package being proposed by Republicans.
- As the economy reopens, we are forecasting GDP growth in excess of 6% for this year, well ahead of the long-term trend growth rate, and which would mean the economy would recover to its pre-pandemic peak by the middle of this year. On a quarterly basis we will likely see the peak of growth occurring in Q2 on a year-on-year basis before starting to slow into the back half of the year as Covid support measures roll off.

Companies and earnings

- There have recently been a few company developments of note. Firstly, the acquisition of QTS Realty by private equity company Blackstone earlier this week. QTS is a real estate company with particular exposure to data centres and colocation within that market, which allows companies to rent space in data centres which are close to their physical sites.

Blackstone has come in with a 21% premium to the closing price on Friday 4 June for a valuation of $6.7 billion.

- Biogen this week announced that the Food and Drug Administration (FDA) had approved its treatment for Alzheimer's, which will be the first new drug to target the disease in nearly 20 years. The FDA ruling was very much a binary outcome and consequently the stock was up 53% on Monday 7 June and closed out the week at a record +38%. Eli Lilly, which is developing its own therapy for Alzheimer's, subsequently rose 10% on Monday on the back of the Biogen news and has continued to rise in the days since.
- Looking ahead to the Q2 earnings season, we are expecting the excellent year-on-year earnings growth to continue, especially in cyclical sectors given the greater degree of operating leverage. Market expectations, according to Factset, are for earnings growth rates to peak in Q2 with estimated growth of 60%.

European equities

- Brexit remains centre stage and has caused ructions in Northern Ireland politics and coloured the G7 meeting in Cornwall. French president Emmanuel Macron's intransigency poses challenges to UK negotiators.
- There seems to be little impact on quoted stocks, with the exception of the financial services sector, where the lack of a clear agreement and risks to UK businesses are causing uncertainty.
- M&A is rife, particularly in the UK market. Corporate results have tended to be strong, as the benefits of vaccination programmes and the relaxation of lockdowns feed through. However, hospitality and travel is suffering from the risk to the summer holiday season.

Fixed income

News

- In the US, Consumer Price Inflation rose more than expected. The headline May figure was up by 0.6% against an expectation of 0.5%. Core CPI rose 0.7% against an expected 0.5%, with the year-on-year rate now at 3.8%. Used cars (+7%), lodging, airfares and eating out all contributed to the rise. Meanwhile, the initial jobless claims fell slightly to 376,000 from 385,000.
- Also in the US, small business confidence dipped a little in May, though 40% of firms reported the ability to pass on higher prices, which is the highest since the early 1980s.
- In Europe, the European Central Bank upped its growth and inflation forecasts as expected, and pledged to keep buying bonds at the present pace. "Periphery" bonds were supported by this news.
- In the UK, GDP rose 2.3% in April – a slight miss on the 2.5% expectation. RICs housing data, meanwhile, continues to point to strength. BRC Retail Sales remain strong, up 28% year-on-year.
- In Germany, industrial production fell surprisingly in April by 1%, In the eurozone as a whole, meanwhile, Q1 GDP was revised higher to -0.3% from -0.6%.
- China, meanwhile, reported much higher Producer Price Inflation, +9% year-on-year, but with no/little pass through to consumer prices, which rose 1.3% year-on-year.

Markets

- The Q2 bond market rally continues, with yields moving lower again, led by falling inflation expectations and thoughts that growth may be slowing a touch. The US 10-year started the week (Monday 7 June) at 1.55% and ended it (on Thursday 10 June) at 1.43%. In Germany it moved from -0.21% (7 June) to -0.28% (10 June).
- In credit markets, based on BofA Merrill Lynch Bond Indices, it was a case of "nothing to see here". Global IG started and ended the week at 92bps with zero movement in the interim, while Global HY was at 356bps on Monday 7 June and ended the week (10 June) at 355bps having touched 353bps on 9 June.
- Euro HY is the best-performing market year-to-date – spreads are 18% tighter with US HY at -15%. Euro IG has tightened -9% year-to-date but is lagging the US at -11%.
- Oil started the week (7 June) at $68.8 a barrel and climbed over the week to $70.4. It's up around 45% this year so far.
- In FX, little changed for the euro over the week versus the US dollar at 1.219.

Note: all data as at 10 June 2021, unless otherwise specified. Source: Bloomberg.