Raiffeisen BANK
Client inspired banking

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Commentary on Current Situation Facing Financial Markets

As regards developments in the equity markets, last week was less successful that its predecessors. For example, the U.S. S&P 500 index lost 2.3 percent and the DAX of Germany wrote off almost 4 percent. Both the energy and the real estate sectors failed to perform, while the health care sector, as the only one, marked some growths. Equities prices declined because some investors had decided to collect their accrued profits. Even, the markets were not upheld by a comment made by the FED chief in mid-week who had warned that "the *liquidity crisis* has been addressed, but the *solvency crisis* is still raging". Nevertheless, unless a second wave of the pandemic occurs, the head of FED would expect a gradual revival in the course of the second half of this year.

On Friday, data were published about the April retail sales in the U.S.A.; they dropped by 16.4 percent, as against the expected 'mere' 12 percent. If unfavourable indicators continue to show, the weeks to come may see higher market volatility. The situation, however, should improve step by step. The annual horizon outlook also presumes a relatively strong economic recovery, including a sharp rise in corporate profits (*source:* Bloomberg).

Both equity markets and corporate bond markets, however, will face dangers in the form of the second wave of the corona virus pandemic coming in this year's autumn or winter, and the increasing rupture in the commercial ties between the U.S.A. and China. Yet another risk facing markets is represented by a potential victory of the Democratic candidate in the U.S. presidential election in the autumn of this year, and a possible increase in corporate taxes. The elections will be taking place in the U.S.A. at the beginning of November this year.

As regards our managed portfolios, we continue to maintain a slight overweighing of the equities portion against the bonds. The gradual, and possibly faster than expected opening of the main economies, renders investors moderate optimism. Therefore, the past week experienced only some minor modifications in the portfolios of our funds. We see as worth mentioning a reduction of the stake of the ČEZ shares (collection of profit) and a purchase of equities of Total for prices close to several-weeks' lows. In the bond portion, we have paid attention to a new issue of bonds by BNP Paribas. Since the Czech sovereign bonds currently offer very low yields, we have assessed this issue to be offering an interesting 'risk-revenue' opportunity, and we have decided to include it in the portfolios of some funds.

Summary:

- The flow of unfavourable economic data will probably continue. In particular, so-called 'lagging indicators' (such as the GDP, industrial production, household consumption, etc.) will still show very low values. In such cases, expectations have it that **the markets will be more volatile in the coming weeks**.
- It is the future outlook that is important. **The expected strong economic growth and increased corporate profits in the annual horizon** (*source:* Bloomberg) will support the equity markets.
- On the other hand, it will be important to monitor **valuations of equities**; an excessively strong growth of the equity markets might result in their overvaluation.

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- The gradual and **faster than expected opening of the main economies** bestows on investors moderate optimism.
- **A threat has been posed by a potential second wave of infections**. This, however, is opposed by the time factor, which is important as regards the development and approval of a new vaccine. Over time, probability of successful application of a new remedy increases.
- We continue to **maintain slight overweighing of the equity portion** as against bonds in our managed portfolios.

We wish you nice and successful week.

For the team of your portfolio managers.

Michal Ondruška
Manager, Asset Management

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