MAPM: Markets Weekly

23rd July 2021

Summary

- Equity markets recovered from jitters early in the week to end up +0.5%.
- Natural disaster costs at 10-year high as floods hit Europe and China.
- “Pingdemic” begins to cause food shortages as over 600,000 people are instructed to self-isolate.
- The ECB hold interest rates steady and looks for signs of durable inflation.

Market and Economic review

Markets started the week by getting out of bed on the wrong side. Largely driven by boisterous concerns around the ever-spreading COVID-19 Delta variant, equity markets had their worst 1 day fall in 2 months of around -2-2.5%. The single day moves did not warrant portfolio changes but are a fresh reminder of the volatility MAPM have been indicating over the last few weeks. Markets snapped back as participants took the opportunity to add risk during what appeared an overreaction against a backdrop of strong Q2 earnings from the US, and ended the week in positive territory. US 10-year bond yields fell through the risk asset sell-off, falling 15bps to 1.15%, but duly rallied as markets shrugged off Monday’s concerns and ended the week at 1.28%. Finally, after an OPEC+ agreement to increase oil production by 400,000 barrels per day from August and by two million barrels per day by the end of the year, crude oil prices fell on market weakness before also ending the week higher at $73 a barrel.

Insurance broker Aon reported natural disasters cost insurance companies $42bn in the first half of 2021, a 10-year high. 35% was linked to the big freeze in America in February but doesn’t account for other recent tragedies. Heavy rain across Germany and Belgium caused devastating flooding and 180 deaths. In the Chinese province of Henan, floods killed at least 33 people and displaced 200,000 more after record breaking rain flooded streets and damaged dams. Scientists suggest that higher air temperatures enable the atmosphere to hold more moisture and decelerating high-level winds due to Artic warming caused storms to move more slowly; meaning more rain was dumped in a smaller area. Unfortunately, climate change means this is likely to become more prevalent. In the US, more than 80 wild fires impacted nearly 1.3 million acres of land in recent weeks and Canadian fire crews battled 1,145 blazes, three times the 10-year average.

The “Pingdemic” is becoming an increasing concern as latest figures shows over 600,000 people were ‘pinged’ by the NHS app last week and instructed to self-isolate, a 17% increase on the week before. To put that number in to context, 2.4m people are currently on furlough meaning a further 25% of individuals are potentially being pulled from the labour force. Companies ranging from Greene King to Iceland to Vauxhall have been vocal about the impact it is having on operations. The UK Government have so far refused to make changes to the track-and-trace app but have made some supermarket depot workers and food manufacturers exempt from quarantine rules. As COVID-19 cases rise it would be natural to see further increases in isolation requests which could impair the UK’s economic recovery. Unless of course the app is mysteriously deleted or contact tracing is turned off, which apparently has occurred amongst one third of people, including half of 18-24 year olds.

This week the ECB met for the first time since modifying its mandate replacing its 2% inflation ceiling with symmetric inflation targeting (as well as placing more emphasis on climate change). Unsurprisingly there was no change in the policy but Christine Lagarde, the ECB’s President, embarked on a new era of so-called plain English communication. The ECB is committed to keeping rates low until it sees ”durable” inflation for the ”rest of its projection horizon”. Whilst growth is rebounding strongly, economic activity will not return to pre-crisis levels until Q1 2022 - there was also a nod to the risks carried by the Delta variant which could push this recovery off track. Markets have fully priced in a European rate hike in Q4 2024.

Data in brief: US initial jobless claims unexpectedly rose (419k vs. 350k exp). UK retail sales rose in June by +0.5%. UK PMI data for July came in at 57.7 (exp. 61.7) which was a large negative surprise. Whilst still in growth territory, as indicated by a reading above 50, headwinds in the services sector appear to be denting confidence. In the Eurozone PMI data rose from 59.5 to 60.6, beating expectations, as the area continues to build economic momentum as the Service sector re-opens.

Later today sees the release of US PMI data. Next week the Federal Reserve meet and whilst we would be surprised if there are any policy changes, their voting and rhetoric will be watched just as acutely. We also get the first glimpse of Q2 GDP numbers for the US (exp.8.0% annualised) and Eurozone (exp.13.2% y-o-y) alongside updates on Eurozone inflation (exp. 2.0%) and unemployment (7.9%).

Movers

Equity	Current Level	WoW	YTD	YoY
MSCI DM	723	0.50%	11.84%	29.86%
MSCI EM	1,326	-1.02%	2.68%	23.07%
S&P500	4,367	0.93%	16.28%	33.32%
FTSE 100	7,011	0.04%	8.52%	12.95%
Eurostox	4,084	1.20%	14.96%	21.17%
FTSE MIB	24,986	0.78%	12.39%	21.30%
US Value vs Growth	--	-0.68%	6.95%	7.21%
Government bond				
US 10 year Yield	1.28%	-1.2	36.5	68.1
US 2 / 10 Spread	1.08%	0.9	28.6	63.2
Germany 10 Year Yield	-0.41%	-5.6	16.0	8.1
UK 10 Year Yield	0.58%	-4.7	38.2	45.9
Italy / Germany 10 Year Yield	1.04%	-1.9	-7.1	-48.5
Credit Spreads				
Barclays £ Corp TR Index	1.07%	1.9	-4.6	-52.2
Eur High Yield Spread (XOVER)	2.35%	-3.6	-7.8	-108.8
US High Yield Spread (CDX HY)	2.85%	-2.1	-8.5	-168.8
EM $ Spread (CDX EM)	1.62%	-0.1	10.7	-7.7
Currency				
USD Index	92.85	0.18%	3.24%	-2.25%
GBPUSD	1.3741	-0.19%	0.50%	7.91%
GBPEUR	1.17	0.04%	4.26%	5.96%
EM FX Spot (JPM Index)	56.43	-0.43%	-2.22%	0.92%
Other				
Crude (1st Future)	73.66	0.10%	42.20%	66.31%
Vix index	17.28	-1.2	-5.5	-7.0
Treasury Vol index (SMOVE)	65.45	3.6	16.0	15.7

Source: Bloomberg as at 09:13 on 23/07/2021

Outlook

Given the strong rally in equities year to date and the increasingly uncertain outlook for inflation and interest rates, we moved tactical positioning back to neutral in Equities and Fixed Income, while maintaining a diversifying overweight to Alternatives. This also coincides with the summer trading months, which tend to see much lower volumes traded as markets pause for a holiday break. We feel we are therefore well positioned to deploy capital where and when opportunities present themselves. As ever, we continue to monitor the changing outlook and respond accordingly.