# COMMENTARY ON CURRENT SITUATION FACING FINANCIAL MARKETS

*Prague, 25 May 2020*

**Equity Markets Wipe-Off First-Quarter Losses Step by Step**

The equity markets did well last week; for example, the American S&P 500 index increased by 3.2 percent. Such strengthening of the equity indices was supported by *Moderna* reporting last Monday some encouraging outcomes of the first-phase testing of its new vaccine. Nevertheless, the number of the tested people was relatively small and the potential vaccine will have to undergo further tests before it can be applied.

The cyclical sectors did best last week. The industries sector strengthened by 7.4 percent and the energy sector grew by 6.9 percent. On the other hand, the defensive sectors, such as consumer goods or health services, lagged behind last week. The season of disclosing the first-quarter economic results has practically been over in the U.S.A. The last five percent of the enterprises belonging to the S&P 500 index is expected to report their results this week. Out of the index, 64 percent of companies reported better than expected profit, and 57 percent of firms generated better revenues than they were expected to. In total, however, profits declined by 14.6 percent, y/y, in the first-quarter.

Investors will be watching plans for the opening up of the economies both in the U.S.A. and in Europe in the coming days. Out of the monitored economic data, information about consumer confidence and new home sales will be published this week, and the Fed will also publish its so-called 'Beige Book' on the State of the U.S. Economy. Investors will also be following development regarding the protests in Hong Kong triggered off by the new security bill. The U.S.A. threatens China with sanctions since the legislation as submitted does not comply with Hong Kong's current autonomy.

We leave the portfolios slightly overweighed. As regards the bonds side, the RIS funds participated in the primary subscription of bonds of the International Investment Bank multinational development bank, and, after a previous drop in the prices, they purchased some more Czech Republic's sovereign bonds with a variable coupon, due in 2027. On the other hand, we collected a portion of the yields from our sovereign bonds maturing in 2030, after their price reached a three-year maximum. Having in mind the CZK/EUR exchange rate of 27.50/1, we have selectively increased currency hedging of our EUR positions; on the other hand, we purchased U.S. dollars (following their temporary weakening) for 24.786 CZK per USD, in order to reduce the rate of hedging of some positions in the USD held in several of our funds.

The coming period may bring about higher volatility to markets, since a major drop in profits generated by enterprises is expected in the second quarter, even in excess of 40 percent (*Source:* FactSet). Nevertheless, the equity markets should be supported by negative real interest rates, together with higher profits expected to be generated by firms in the course of next year (*Source:* FactSet).

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**Summary:**

- The American S&P 500 index **has been traded close to its 200-day average price** (the value of the S&P 500 is approximately 3,000 points). We consider such value to represent an important so-called resistant level; nevertheless, if this limit is breached, a further strengthening of the stock index cannot be ruled out.
- As part of tactical regional allocations, we have been, so-called, **overweighing the regions of the U.S.A. and Europe**, while moderately under-weighing the Pacific region and the emerging markets.
- As part of tactical sector allocations, we have been **overweighing technologies and health services, and the dividend-bearing shares segment.**
- We consider the bond markets to be relatively expensive following major price increases (drops in yields); this applies in particular to the segment of fixed-interest sovereign bonds.
- As regards our managed portfolios, we continue to **overweigh moderately the equity portion of such portfolios** as against bonds.

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