



Monthly Update - September 2021

As at 31 August 2021

Summary: More economic growth again

- Global economic growth likely to pick up
- Low inventories worldwide: inventory rebuilding cycle and growth stimulus
- Significant improvement in US labour market and rising wages provide tailwind for consumers and economy
- Strong rise in global real estate prices: positive wealth effects
- Global monetary policy remains loose Fed still has no precise timetable for "tapering"; ECB securities purchases remain at elevated level
- Conditions support continued upward trends in inflation and interest rates
- Favourable environment for equity and credit markets remains: rising corporate earnings, but potential pressure on the US dollar

Significant changes compared to the previous month

- The global economy should regain momentum after a temporary slowdown in recent months due to an upcoming inventory rebuilding cycle. Owing to the pandemic, inventories are at a low level worldwide (especially in the automotive industry), but will be built up again in the medium term. Historically, inventory rebuilding cycles have always had a positive effect on economic growth.
- Other factors support solid economic growth: the US labour market is beginning to accelerate and wages are rising significantly. Unemployment is also falling in Europe. This leads to increased consumption potential. In addition, real estate prices worldwide have been rising strongly for some time. This results in wealth effects, which additionally supports the propensity to consume.
- Since monetary policy nevertheless remains very loose worldwide, the result is a strong reflationary environment. The Fed has announced a possible reduction in securities purchases ("tapering") before the end of the year. However, there is no precise timetable yet, and we therefore expect the first reduction to be very moderate. The ECB is also continuing its securities purchases (PEPP) at a high level (unchanged) for the time being, while the Chinese central bank (PBoC) has recently eased its monetary policy once more.
- This increased reflation of the system in the foreseeable future will still have a positive impact on equity and credit markets for the time being, but will lead to higher upward

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pressure on inflation (actual data and forward expectations) and long-term interest rates. Such an environment has historically been negative for the US dollar.

Current situation and positioning

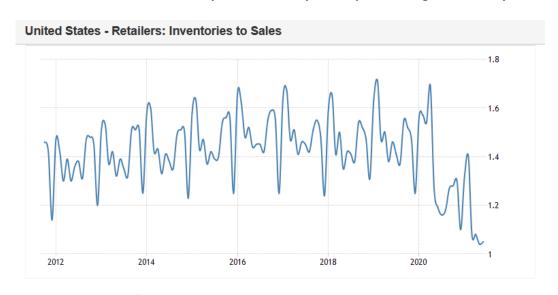
- The labour market in the US has already improved significantly in the past two months. However, certain restraining forces have been active thus far: on the one hand, pandemic unemployment benefit programmes are still running, discouraging many workers from looking for a job. On the other hand, schools are still closed. This forces many parents to stay at home and take care of children, which prevents them from starting a new job. These two factors expire at the end of September, which should further accelerate the US labour market.
- The number of job openings is at an all-time high of 10 million, which means that job seekers are very likely to find a job from September onwards. As a result, the unemployment rate in the US should continue to decline significantly. The high job supply is also likely to put upward pressure on wages. Many companies are desperately trying to fill vacancies.
- The labour market is currently the decisive factor with regard to US Federal Reserve policy. If the expected acceleration here is confirmed in the coming weeks, the pressure for tapering to begin before the end of the year will increase. However, such a development is already partly priced into market expectations. This means that major negative surprises on financial markets are not to be expected. Nevertheless, a significant improvement in the labour market is likely to reinforce the trends already emerging (higher interest rates, falling US dollar, rising inflation expectations) and dampen the upside potential in equity and credit markets.
- Rising corporate profits and stronger economic growth (by virtue of a healthy labour market, high consumption and positive wealth effects) should, however, prevent greater damage to the equity and credit markets, despite any rise in interest rates.
- The inflation rates in the US, which as expected have risen sharply in recent months, are already beginning to weaken slightly once more. Various purely temporary influences (base effects, pandemic-related supply bottlenecks, higher commodity and energy prices) should provide some albeit limited relief in the foreseeable future. The medium to longer-term inflation trend is subject to sustained upward pressure due to the continued strong global growth in money supply, tremendously high consumption potential (high consumer savings), rising real estate prices and easing deflationary pressure from China. However, inflation expectations are currently still moderate, which also serves to dampen the longer-term inflation trend (low base effect). However, a change in sentiment with considerable consequences can occur at any time. Therefore, the monitoring of inflation expectations (e.g. via inflation-linked swaps and TIPS) is crucial.
- The US Treasury plans to issue government bonds worth around USD 650 billion each for Q3 and Q4. This significantly exceeds the Fed's monthly purchase of government bonds and MBS of USD 120 billion. Together with a currently neutral government bond market, this should provide additional upward pressure on long-term US interest rates. If, given this starting position, a potential tapering towards the end of the year were to be added, this pressure would be further intensified.
- The current environment of rising government debt (not financed by the Federal Reserve),
 potentially higher interest rates, higher inflation and improved economic activity has

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historically proved a drag on the US dollar. However, support for the greenback is currently coming from the ECB, which is maintaining an extremely loose monetary policy for the time being. However, discussions about possible adjustments to the PEPP and APP purchases are also intensifying here. It remains to be seen how the ECB will react to a Fed tapering and either compensate for this with even higher securities purchases in Europe or else follow suit and also reduce the purchase volumes.

Topics "on the radar"

Chart: Global inventories currently low – inventory build-up is boosting the economy



Source Trading Economics/United States Federal Reserve

In the US, the inventory cycle points to imminent stimulus for the economy and corresponding upward pressure on interest rates over several quarters. Currently, inventories are low in absolute terms, but also relative to consumer goods sales (see chart), especially in the automotive and manufacturing sectors.

This is not just an American but a global pandemic-related phenomenon. Restocking should lead to significant economic stimulus. In the US, for example, retail inventories are currently about 10 percent below normal or pre-pandemic levels (USD 600 billion versus USD 660 billion normally).

The demand for goods triggered by the inventory build-up is also further boosted by record high consumer cash balances, some of which is also flowing into consumption.

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Summary of FischView model outputs

	US	Europe	Japan	Asia ex- Japan	LatAm	CEEMEA	Key:	
Equities	+	+	0 ↓	o ↓	0 ↓	+ ↑	++	Strong positive
Government Bonds	-	-	-				+	Positive
Credit IG	0	0		+ ↑	+ ↑	+ ↑	О	Neutral
Credit HY	+ ↑	+ 1		+ ↑	+ ↑	+ ↑	-	Negative
Convertibles	0 ↓	+	0	o ↓				Strong negative
								-
Commodities	Energy	+	PrecMet	0 \	InduMet	+		

Notes regarding the table: Changes from prior month are indicated with \downarrow or \uparrow . i.e. "O \downarrow " means that the output has weakened from a prior value of + or ++.

The methodology for calculating model outputs, and how the various pieces fit together to form the big picture, is explained here.

Within government bonds, we consider the most important bonds for each region, e.g. German Bunds in Europe, and a representative group of countries for Latin America, Asia ex-Japan and CEEMEA (Central and Eastern Europe, Middle East and Africa).

Cross asset class preferences

This table combines top-down views with bottom-up analysis at the portfolio level.

	Most preferred	Least preferred
Convertible Bonds	 Cyclicals (industrials, materials) 	Interest rate sensitives (real estate)
Global IG Corporates	USD IGBasic Industry"Rising Stars"	EUR IGUtility'AA' rating segment
Global Corporates	Developed market HYSpread duration 5-10'BB' rating segment	Emerging market HYSpread duration >10'B' rating segment
Global High Yield	'B' rating segmentTelecomsBasic industryEnergy	BankingTransportationReal estate, especiallyChina
Emerging Market Corporates - Defensive	IndonesiaMexico	South KoreaTaiwan
Emerging Market Corporates - Opportunistic	High yield commoditiesMexicoIndia	BahrainQatar

Note: Preferred sectors/regions may differ between asset classes owing to respective performance drivers. In particular, equity exposure is the key performance driver for convertible bonds and is not relevant for corporate bonds.

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