Blackshield Capital

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BLACKSHIELD WEEKLY INSIGHTS

Dynamics of key assets

Top charts of the week:

- The FED and the fight against inflation
- fragility of the labor market
- low level of risk premium

Have a question for the team? CONTACT US

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One of **the most important tasks of an investment firm is** to respond in a timely manner to the challenges of the economy and market conditions. While many risks of a geopolitical and financial nature cannot be predicted, it is worth staying informed to understand what is happening in a meaningful way.

Interest rates, the real estate market, employment and unemployment, inflation and corporate profits are just a few of the variety of factors affecting asset and security pricing.

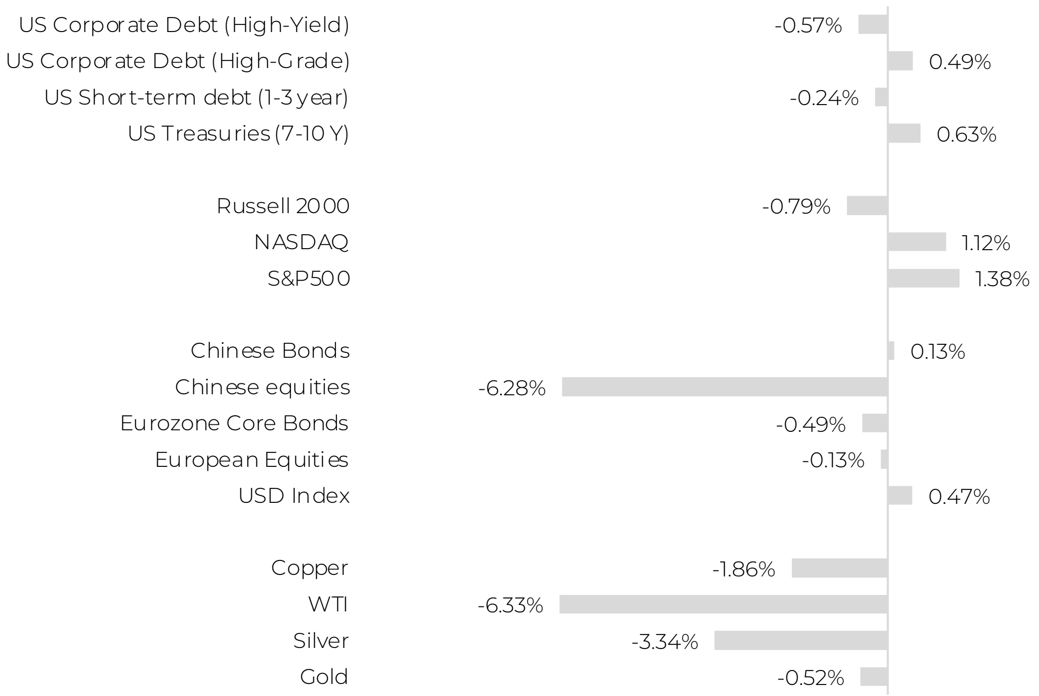
Our goal is to provide a deeper and clearer understanding of what is happening in the markets with an emphasis on illustrations, charts and visuals.

Weekly Insights will provide a more detailed look at industry specifics, delve into the nuances of price mechanics, and provide a more detailed understanding of our strategic vision offered in our quarterly strategic reports.

Dynamics of key assets

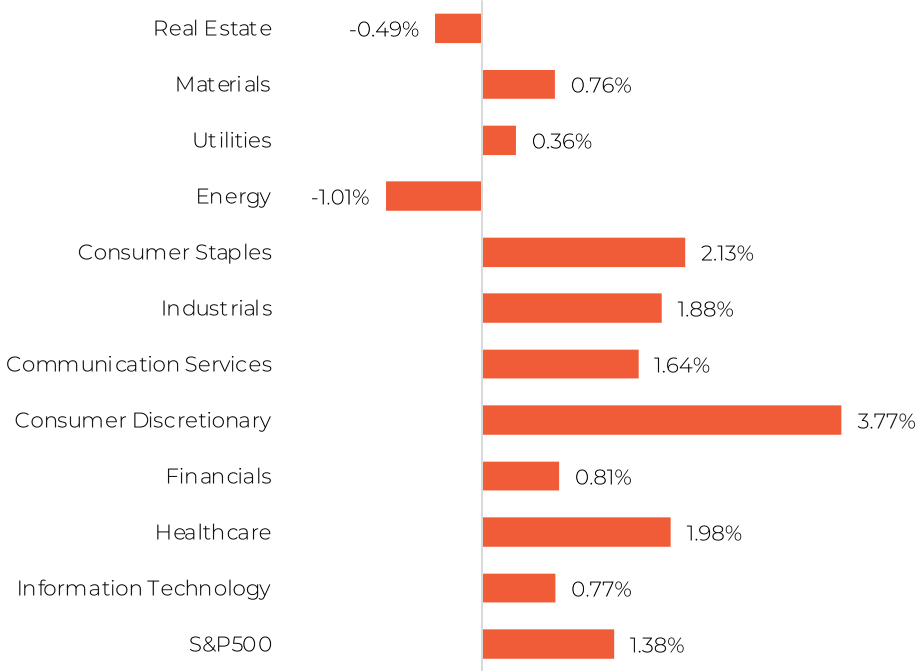
The last week for the markets was quite interesting - it started with rather weak results from large IT companies (MSFT, GOOGL), negative news from the Fed meeting, and market growth amid strong reports from Facebook and Amazon.

Dynamics by key assets for the week



- A global pause in the positive dynamics of the markets was the main characteristic of the past week.
- Of course, each asset class has its own reasons for decline or growth. For us, the most significant is the decline in oil prices as a potential inflationary factor as a result of OPEC agreements. Also, the fall of the Chinese market, the correction of metal prices and the growth of the US stock market amid fairly good reports from major IT companies.

S&P 500 index sectors dynamics for the week

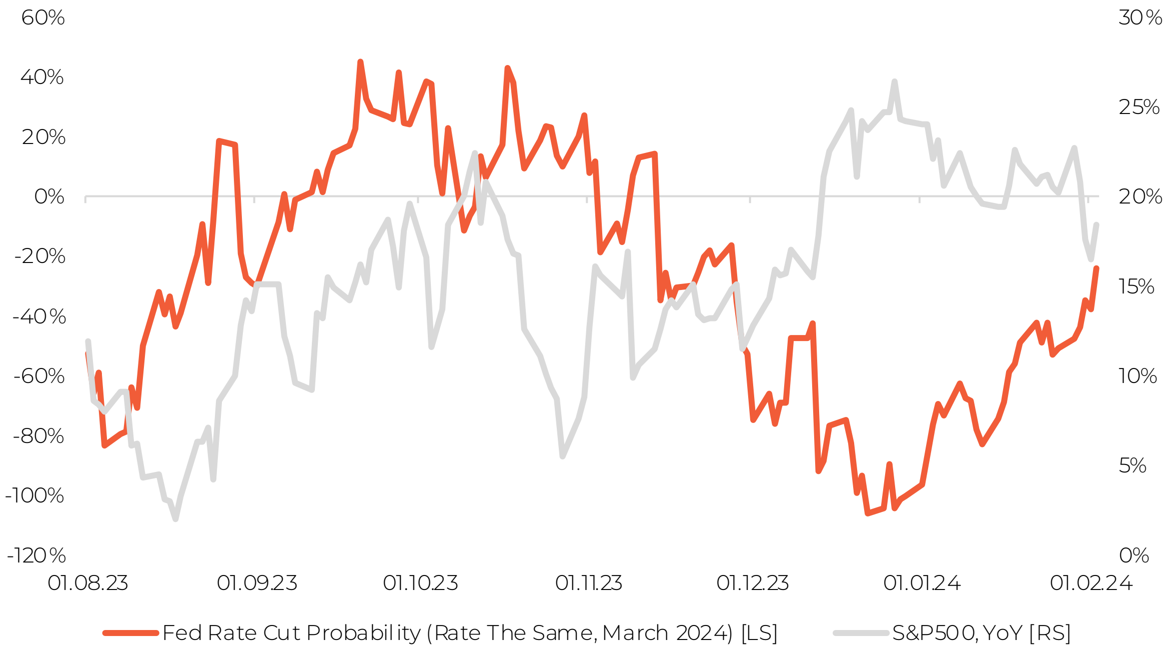


- The main sectors of the economy that saw above-market growth this week were Consumer Discretionary (mostly due to a good Amazon report), growth in defensive sectors of the economy due to higher level of uncertainty about the macroeconomics, and the Industrials sector.
- In general, this had a positive impact on the index, which gained 1.4% due to the positive change in the prices of Facebook and Amazon shares, which were the main reason for the growth of the index at the end of last week.

Top charts of the week – The FED and the fight against inflation

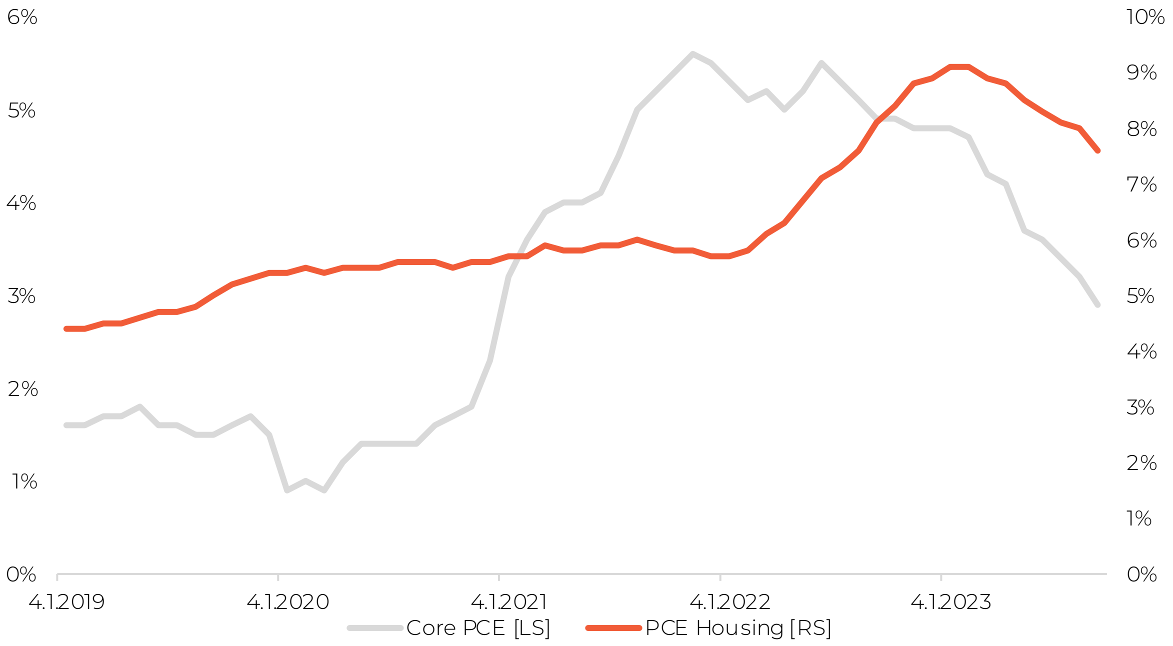
The key topic of the week was the Fed meeting, from which the market did not expect an interest rate cut, but the messages about what the regulator's further actions would be were important. As a result, the market did not find confirmation of the optimism it had expected at the beginning of the year.

Expectations of a Fed rate cut and market dynamics



- Despite the fact that, as expected, the rate will remain unchanged in the range of 5.25-5.50%, attention was focused on the rhetoric concerning the decline in market optimism regarding the pace of rate cuts. After all, according to the Fed Chairman, the regulator lacks the basic data to make a decision on a 0.25% rate cut in March, which is contrary to market expectations from the beginning of December 2023.
- As always, the main focus is on inflationary dynamics, which we expect to have less than 100% optimistic basis. Moreover, the next meeting will see the release of a single inflation figure, which is not enough to confirm the trend.

Inflation: what are the future expectations

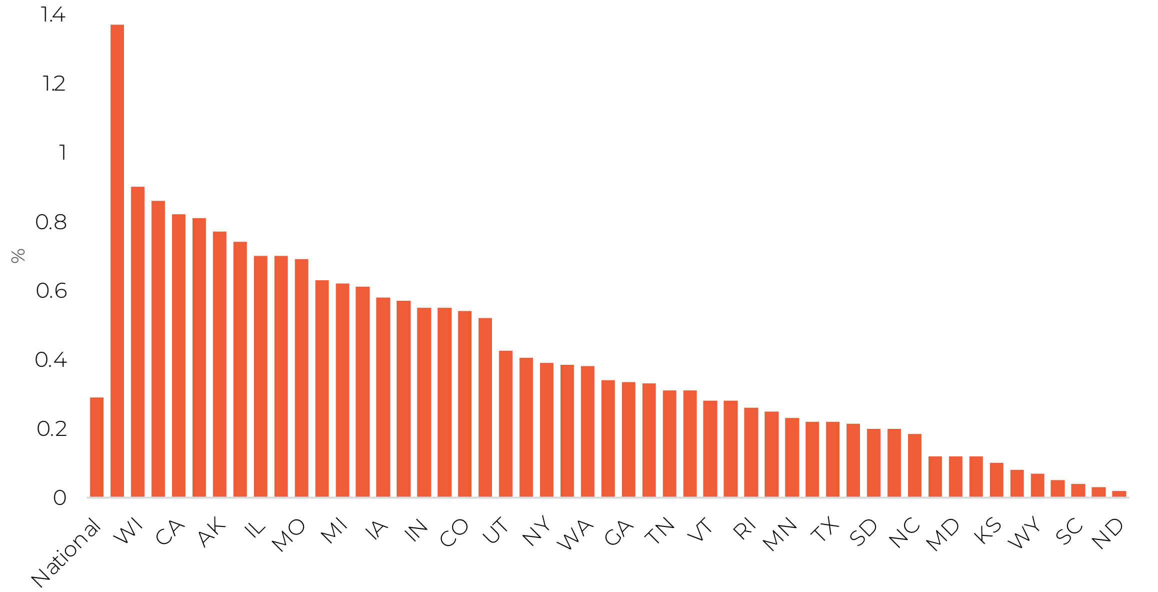


- Referring to the Fed chairman's words, there is indeed not enough data to make an important decision. After all, we are currently witnessing a general decline in inflation to values close to 2%. For example, the 6-month annualized value is at 1.8%, which is already below the target level.
- However, there are still open questions about such large categories as real estate prices, which make up one of the largest shares in the PCE structure, which is above 7%. Factors such as rising oil prices or steady wage growth remain risks for a new round of inflation.

Top charts of the week – fragility of the labor market

According to the latest data, we see a low unemployment rate of 3.7% with significant changes in non-agricultural employment (+353 jobs in January). However, the more reactive indicators are in stark contrast to the available information on the labor market.

Unemployment growth is observed in all states



- Looking at narrower metrics, we see some downward shifts in the labor market, which could be a negative factor for the market, given its current optimism about a soft landing in the economy.
- For example, the so-called Sahm Rule, which is one of the main indicators of a recession (statistically, a 3-month moving average growth of 0.5% indicates a further sharp rise in unemployment), shows this trend in 19 states. This indicates a worsening of the situation, and the number of states with rising unemployment is expected to increase.

Unemployment in Michigan is a leading indicator of the overall state of the labor market

- Another interesting fact is the state of Michigan, which actually accounts for only 2.4% of the total US economy, but the economic specifics of this region indicate its leading properties (a larger number of businesses are cyclical).
- For example, for almost 40 years, all recent sharp increases in unemployment in the United States have been preceded by an increase in unemployment in Michigan.
- Currently, this trend continues, and, based on the latest data, the unemployment rate in Michigan increased by 0.7% (to 4.3%) over six months, while the overall unemployment rate in the US increased by 0.2% (to 3.7%).

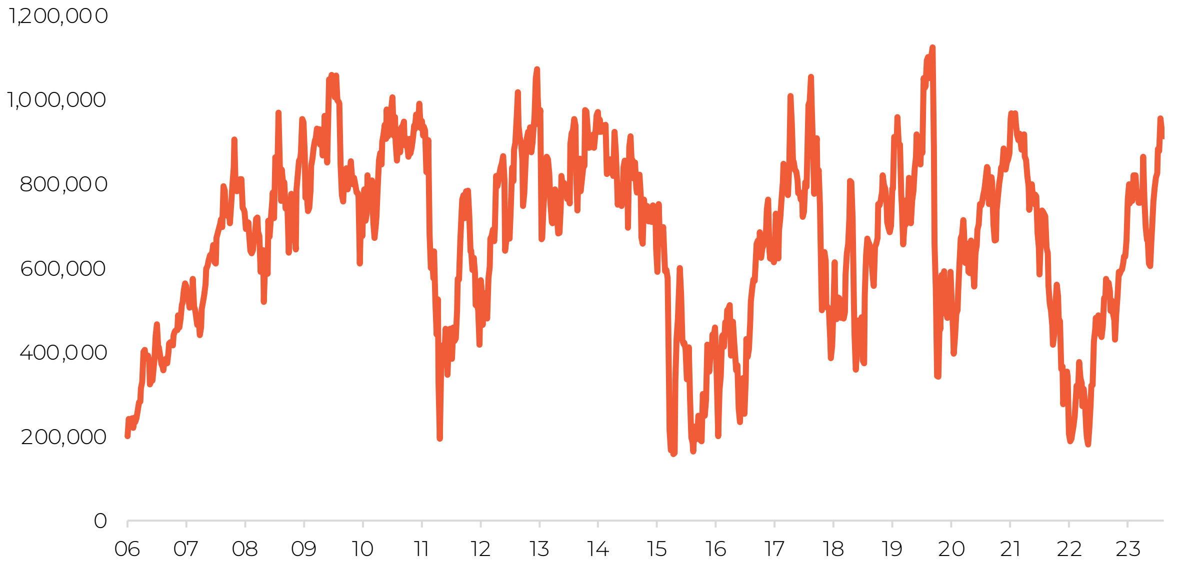
Top charts of the week – low level of risk premium

The market has seen a certain decline in trading activity, which can primarily be explained by the low risk premium, which continues to decline. At the same time, we are seeing the highest levels of positioning in US stocks in 10 years.

Market risk premium

- The risk premium is essentially a reflection of whether a stock is currently attractive to investors. After all, this value indicates whether the risks that an investor takes when buying shares are compensated for.
- In general, there are a dozen approaches to calculating the risk premium in stocks, but the most basic of them indicate rather low values, which in fact indicates a low investment attractiveness of stocks for investors.
- Since the beginning of the year, we have seen a further decline in the risk premium, which rose slightly at the end of 2023 amid declining government bond yields.

Buyside positioning in US stocks



- At the same time, there is a certain saturation or overbought condition in the market, which is clearly reflected in the data on the net positioning (long-short positions) of large funds in US equities.
- Currently, we observe that buyside positioning in equities has increased quite sharply over the past few months. At the same time, it is slightly higher than the peak values of January 2018 and February 2020.
- In essence, this confirms the thesis that the stock market is generally less attractive, which points to the importance of a more selective approach, in particular, buying stocks with defensive-quality characteristics.

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LET US HELP YOU TO FOCUS **ON WHAT MATTERS MOST**

hello@blackshield.capital

+41 43 456 25 92

Bahnhofstrasse 10, 8001
Zürich, Switzerland

Volodymyrska St, 4, 02000
Kyiv, Ukraine