Blackshield Capital

18.03.24 – 24.03.24

WEEKLY INSIGHTS

The gap between financial markets and the economy is expanding

Dynamics of key assets

Top charts of the week:
- changing expectations from central banks
- full risk-on prevails in the market
- decline in demand in the luxury segment

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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.

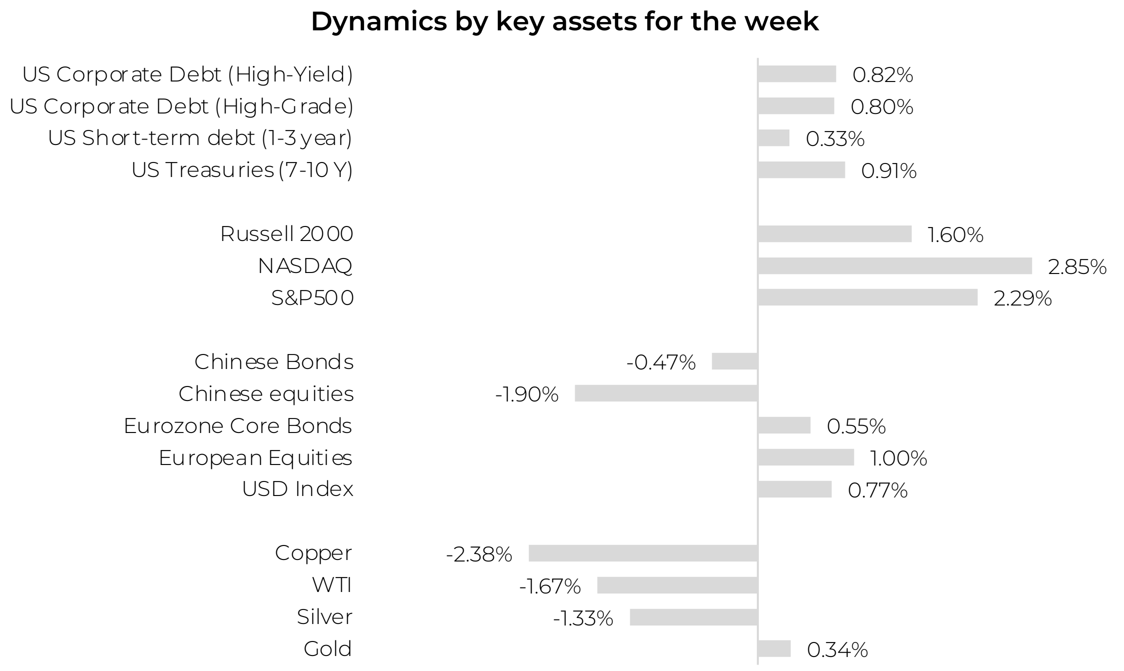
Interest rates, the real estate market, employment and unemployment, inflation and corporate profits are just a few of the variety of factors affecting asset and security pricing.

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.

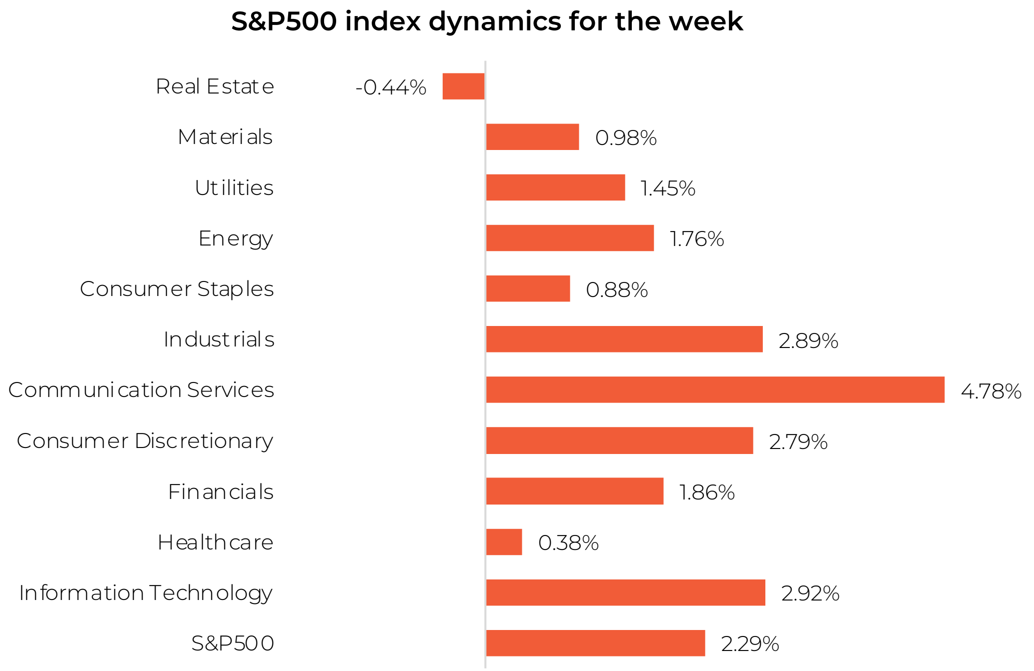
Weekly Insights will provide a more detailed look at industry specifics, delve into the nuances of price mechanics, and provide a more detailed understanding of our strategic vision offered in our quarterly strategic reports.

Dynamics of key assets

Last week was positive for both the US and European stock markets. The main reason for this was the Fed's generally unchanged attitude since the last meeting, which gave a boost to positive sentiment among investors.



- The major US stock indices, the S&P500 and NASDAQ, continued to update their all-time highs amid the Fed's dovish rhetoric, continued rate forecasts for 2024, and market reassurance that the situation in the economy was under control.
- Such positive rhetoric also affected the debt market, where yields on major government debt instruments declined in anticipation of the first rate cuts.
- Commodity prices declined, particularly for copper, oil, and silver. As for copper, despite positive fundamental signals, the spot market slightly reduced demand this week, which brought prices down.



- Taking a closer look at the movements on the US stock market, the general bullish sentiment prevailed in all sectors of the economy, except for Real Estate. Stock prices in this segment slightly corrected after being at their highest levels in a year.
- The greatest optimism, of course, prevailed in the cyclically sensitive sectors of the economy (Industrials, Financials, Consumer Discretionary) and the IT sector.
- The so-called Magnificent 7 group of companies once again outperformed the market, recording growth of 3.77%, which is higher than the market. The main growth leaders: Nvidia, Meta and Microsoft.

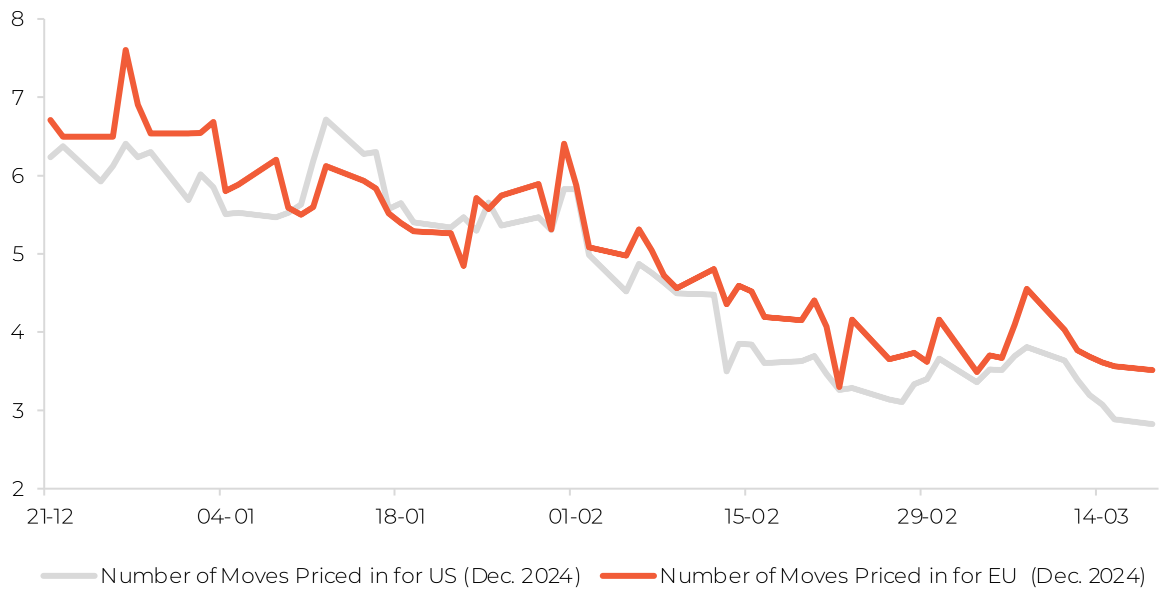
Top charts of the week – changing expectations from central banks

According to the initial market forecasts (from the end of 2023), the March meetings were supposed to be a turning point in the monetary policy of the 2 key central banks. However, a number of economic data postponed these decisions, which was confirmed at March meetings.

Economic forecasts from the ECB and the Fed, YoY

	Mar-24			Comparison with Dec 2023 forecast		
	2024	2025	2026	2024	2025	2026
ECB - Real GDP	0.6%	1.5%	1.6%	-0.2%	0.0%	-0.1%
FED - Real GDP	2.1%	2.0%	2.0%	0.5%	0.2%	0.1%
ECB - Inflation	2.6%	2.1%	2.0%	-0.1%	-0.2%	-0.1%
FED - Inflation	2.6%	2.2%	2.0%	0.2%	0.0%	0.0%
ECB - Unemployment	6.7%	6.6%	6.6%	0.1%	0.1%	0.2%
FED - Unemployment	4.0%	4.1%	4.0%	-0.1%	0.0%	-0.1%

Number of projected rate cuts in the US and EU by the end of 2024



- As at every meeting of the central bankers, key macroeconomic forecasts were revised, which provide a basis for understanding how the central bank will move forward - towards easing or holding rates.
- The rhetoric of the two central banks is somewhat different: the ECB aims to cut rates as early as June (according to Lagarde) due to a noticeable slowdown in inflation, which is reflected in the current forecasts (the inflation rate was revised upward). However, there is uncertainty in the market about the first steps taken by the ECB, which has historically tended to work in tandem with the Fed.
- As for the Fed, in our view, the situation is somewhat more complicated, as the Fed is not so confident in the prospects for a rapid decline in inflation, which forced it to revise its forecasts and postpone the first rate cuts.
- The difference in the reach of inflation reduction is clearly reflected in the number of possible rate cuts: according to the latest data, the market expects almost 4 rate cuts in 2024, while the Fed expects about 3 cuts of 0.25% each.
- Nevertheless, the US futures market for the first time coincided with the official expectations of the Fed: the rate cut is projected at 0.75% in 2024. This was one of the most significant reasons for market optimism in recent days.

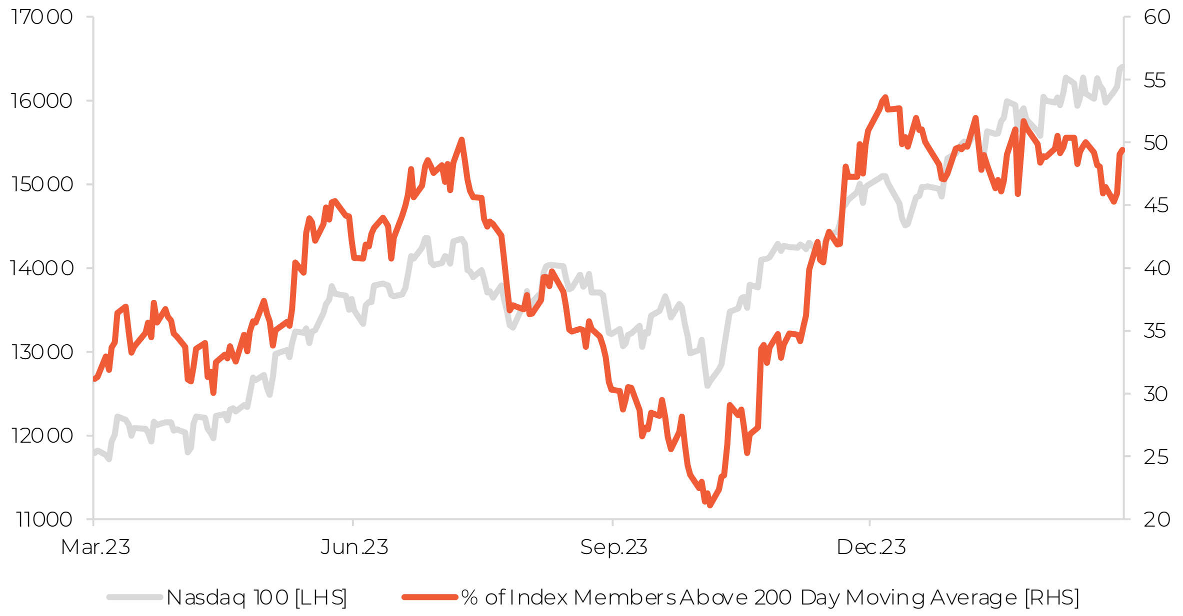
Top chars of the week – full risk-on prevails in the market

The latest dynamics of the most volatile assets on the market indicates that investors are increasing their appetite for risk. For example, the difference between the dynamics of the main cryptocurrency (BTC) and TQQQ (3x ETF on NASDAQ) has increased, which directly confirms this thesis.

Bitcoin surpassed the technology sector in terms of growth

- TQQQ is an ETF that reflects the dynamics of the NASDAQ 100 index with a multiplier of 3. That is, in fact, TQQQ is 300% of QQQ, for those who do not find enough volatility in the classic Nasdaq index.
- Over the past few years, Bitcoin and TQQQ have been moving in tandem, but news about the institutionalization of cryptocurrencies, as well as the atypical appetite of market participants for risky assets, have led to more dynamic growth of BTC.
- There is still a fair question of normalizing the relationship, as both assets are classified as high-risk: there is a high probability that instead of the exponential growth of TQQQ, we will get a tactical volatile decline in large-cap crypto assets.

The percentage of trending stocks in the Nasdaq 100 is declining

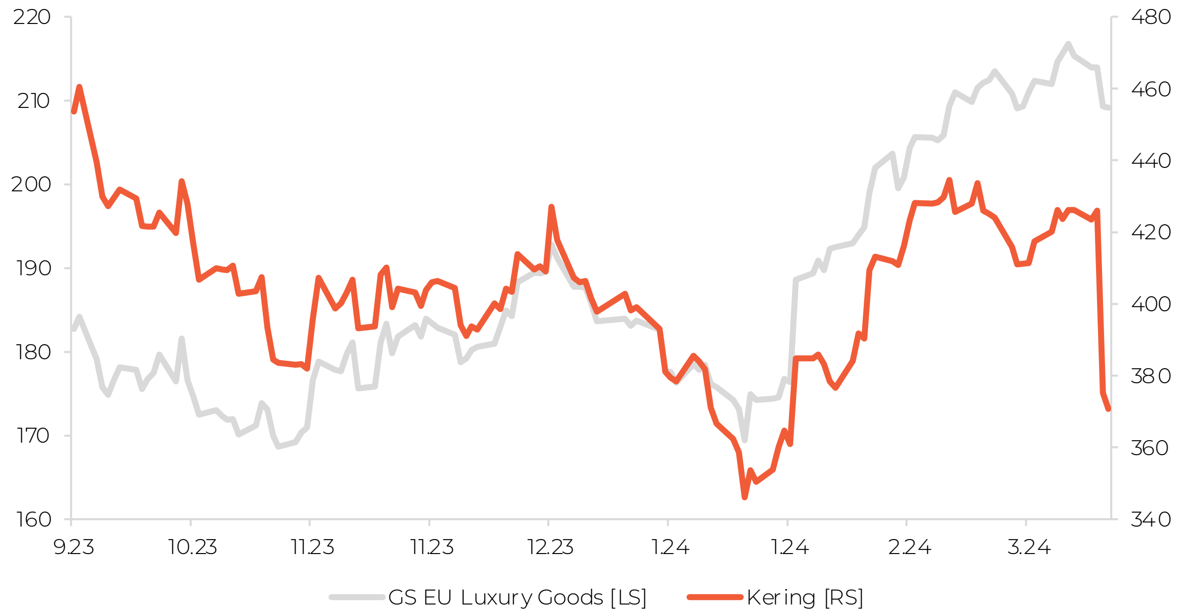


- At the same time, the technology sector index continues to grow amid conditionally positive macroeconomic data. Investors' tolerance tends to seek positive signals from the Fed and the economy.
- Along with a decrease in the number of companies in the index that showed growth in 2024 (currently 60%), the number of companies above the long-term average is currently less than 50% (declining since the end of 2023).
- Such a balance of power is far from a concentration of growth as in the S&P 500 index, but it indicates a partial loss of growth momentum and in most cases such dispersion of power leads to increased volatility.

Top charts of the week – decline in demand in the luxury segment

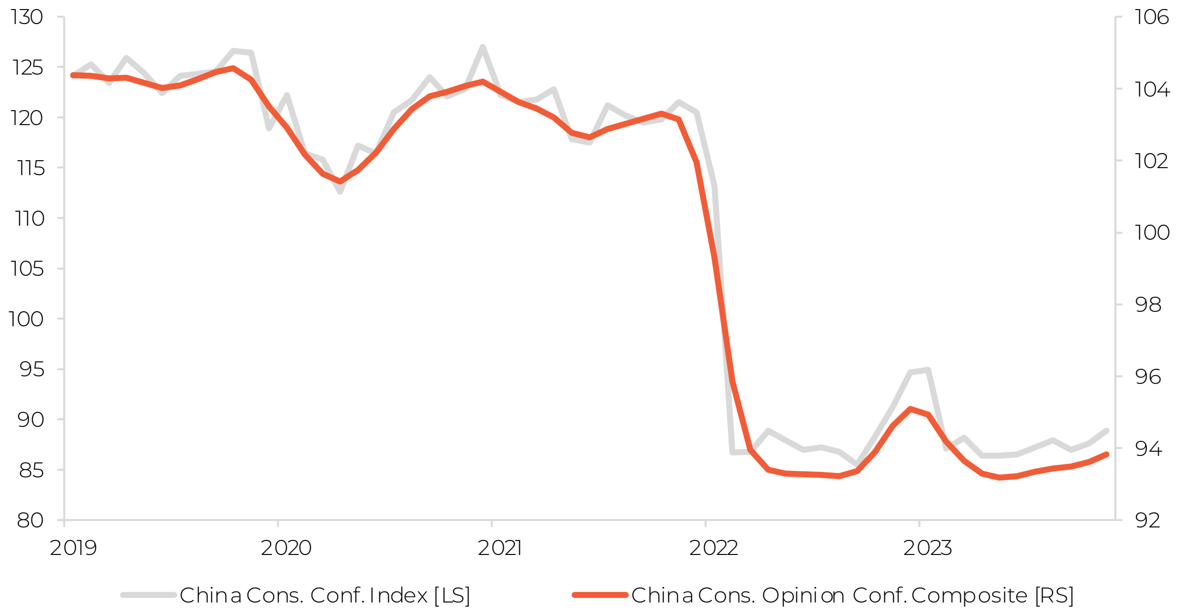
Kering, which has published its preliminary report for Q1, was one of the first to point to a decline in demand for its products in the Asian region. This fact is a pessimistic indicator for the global economy, as it indicates a decline in demand from the high-income segment of the population.

Share price dynamics of "luxury" companies



- It was Kering's reporting that triggered a revision of forecasts for all European luxury companies, which led to a 3% correction in the group's share price in one day. In turn, Kering itself declined in its valuation by 15% in one day of trading.
- The reason for the decline was the revision of forecasts for revenue growth in 2024, primarily due to the dynamics of sales in the Asian market, where the main market is China. According to forecasts, the company's sales will decline by 10% yoy, while the Gucci brand will decline by 20%. The news stirred up the market because, according to economic theory, the luxury segment is more resilient during economic downturns. Therefore, such dynamics directly indicate more serious problems in the economy than might have been expected.

Dynamics of consumer confidence in China



- Such dynamics is primarily explained by the general state of the Chinese economy, which, after overly high expectations for 2022-2023, is experiencing a certain decline. Moreover, there is a noticeable outflow of Chinese consumers in the "luxury" segment from the Chinese to the European market, where it is possible to buy these products on a tax-free basis.
- The reason for this decline is both the problem in the real estate market and the prolonged decline in the stock market, which directly affects the so-called "wealth effect". For example, this is directly reflected in the general consumer sentiment, which, according to the latest dynamics, is at its lowest level in the last year.

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ON WHAT MATTERS MOST

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