Blackshield Capital

06.04.24 – 12.05.24

WEEKLY INSIGHTS

Positive signals as a short-term market stimulus

Dynamics of key assets

Top charts of the week:

- results of the earnings season
- deterioration in the debt market
- resilience of corporate debt

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.

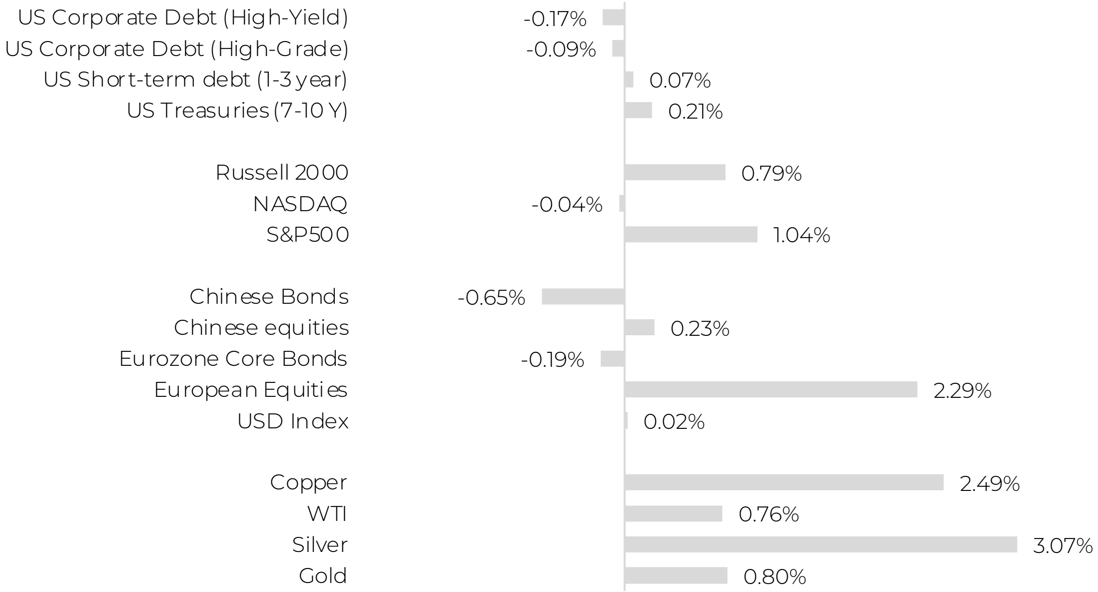
Our goal is to provide a deeper and clearer understanding of what is happening in the markets with an emphasis on illustrations, charts and visuals.

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.

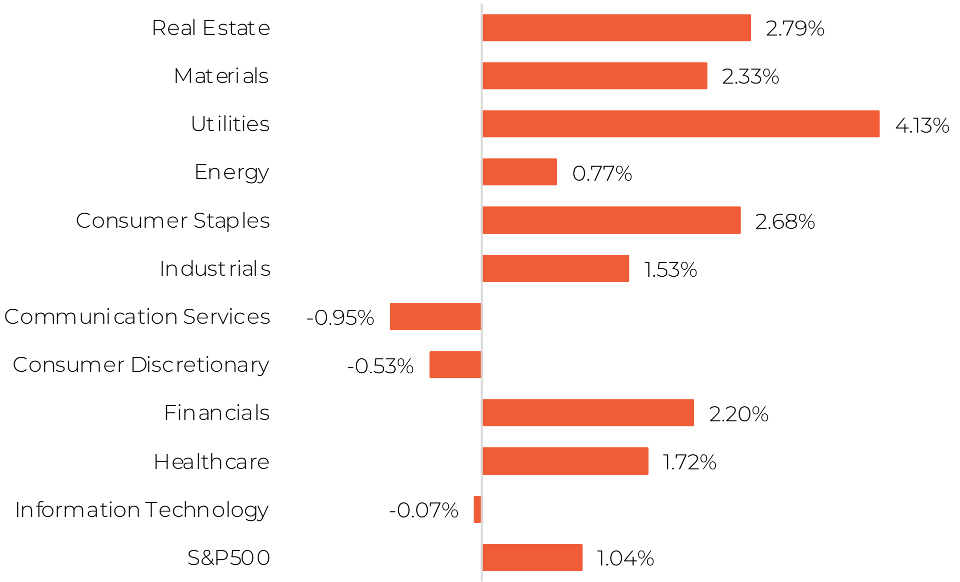
Dynamics of key assets

Last week, financial markets re-entered the growth phase and, for the first time in a year, recorded growth in most key assets amid growing optimism about global economic data, positive earnings season and dovish rhetoric from key central banks.

Dynamics by key assets for the week



S&P500 index dynamics for the week



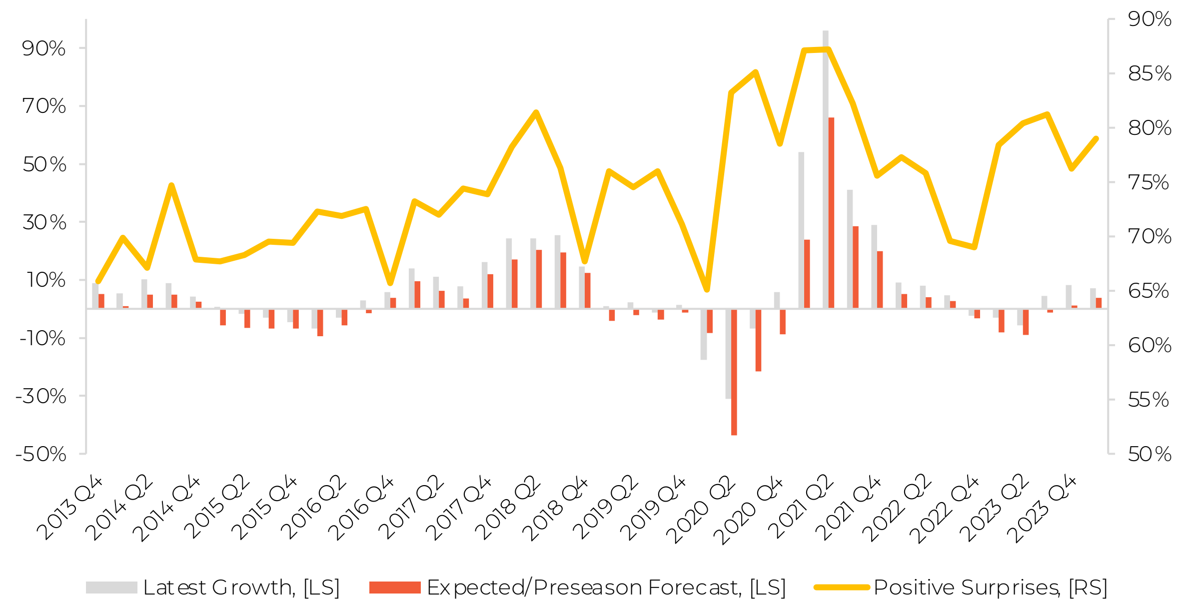
- Despite the controversy surrounding the new data, financial markets, particularly equity markets, again posted comparative gains last week.
- This surge in growth was primarily driven by a dovish rhetoric from the Federal Reserve, as well as better-than-expected nonfarm payrolls and a positive US earnings season.
- In addition, commodities resumed its growth, with gold, copper and silver, for instance, also nearing their peaks this week.

- Looking at S&P500 sector breakdown, almost all sectors of the economy have grown, although Utilities, Real Estate and Consumer Staples sectors were growth leaders. In particular, Utilities and Real Estate sectors were the main beneficiaries of a news renewal wave about a possible rate cut in September this year.
- It is also important that Energy and Financials sectors, which were outsiders two weeks ago, have returned to a positive trajectory.
- Despite this, Magnificent 7 traditionally had the greatest impact on S&P 500 quotations, as it continues to be at the peak of concentration within index.

Top charts of the week – results of 1Q 2024 earnings season

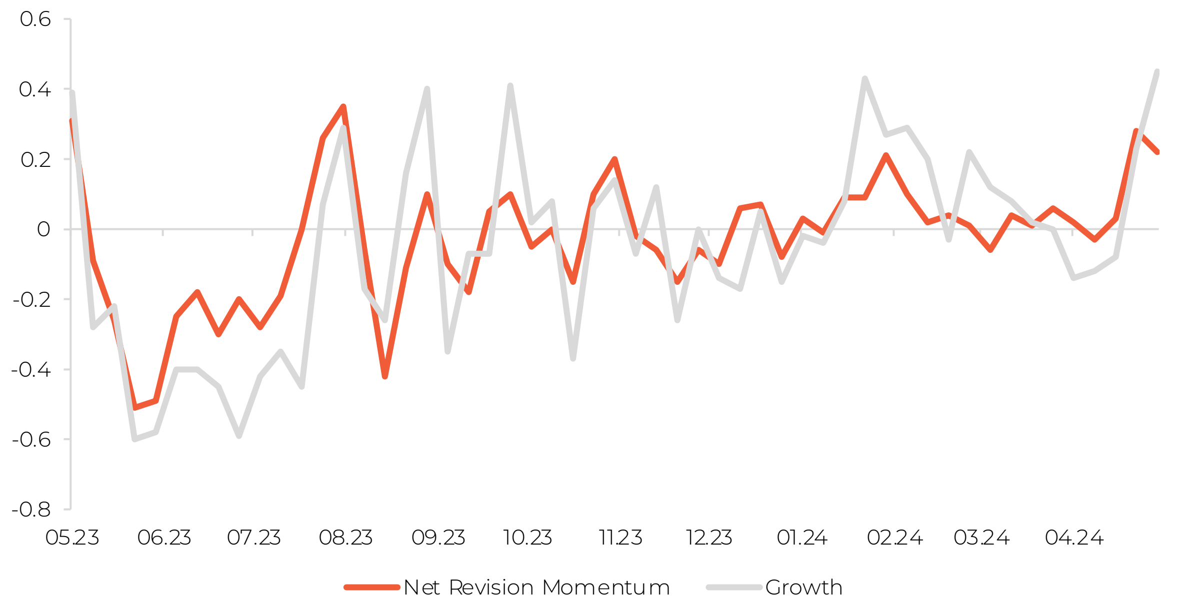
1Q 2024 earnings season was positively viewed by the market, as S&P 500 EPS growth exceeded both expectations at the beginning of the season and the forecasts in January 2024, which was largely due to EPS growth in Growth category.

Dynamics of S&P 500 index EPS growth and EPS Surprise levels



- Summarizing Q1 2024, companies exceeded expectations for EPS growth - 7.1% YoY versus expected 3.8% YoY at the beginning of the 1Q 2024 earnings season.
- In general, the number of companies that exceeded investors' expectations is 79.0% of the total number in S&P 500 index, which is higher than the long-term average.
- Comparing results with the forecasts at the beginning of the year, the actual growth was slightly higher than market expectations (7.1% YoY compared to 6.8% YoY). However, forecasts for the next quarters were still negatively revised, which may indicate that expectations that were formed in January 2024 were too high.

Dynamics of EPS Momentum of S&P 500 index and Growth companies

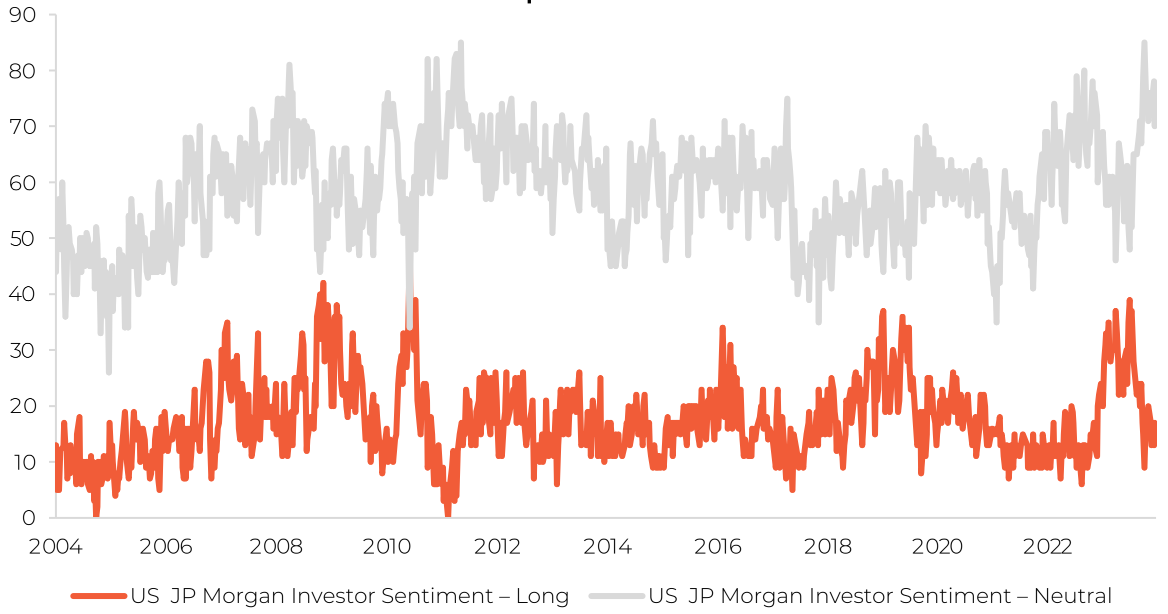


- In addition, the ratio of positive to negative revisions for the next 12 months EPS growth (EPS Momentum) rose to its highest level since September 2023.
- Such dynamics can be explained by the fact that the main drivers of positive revisions were Growth companies, in particular - IT sector, which became a leader according to the data on exceeding expectations for Q1 2024.
- However, it is worth noting that in recent weeks, EPS Momentum has also been growing among Value companies (relatively stable undervalued large companies), which was positively noted by the market.

Top charts of the week – deterioration in the debt market

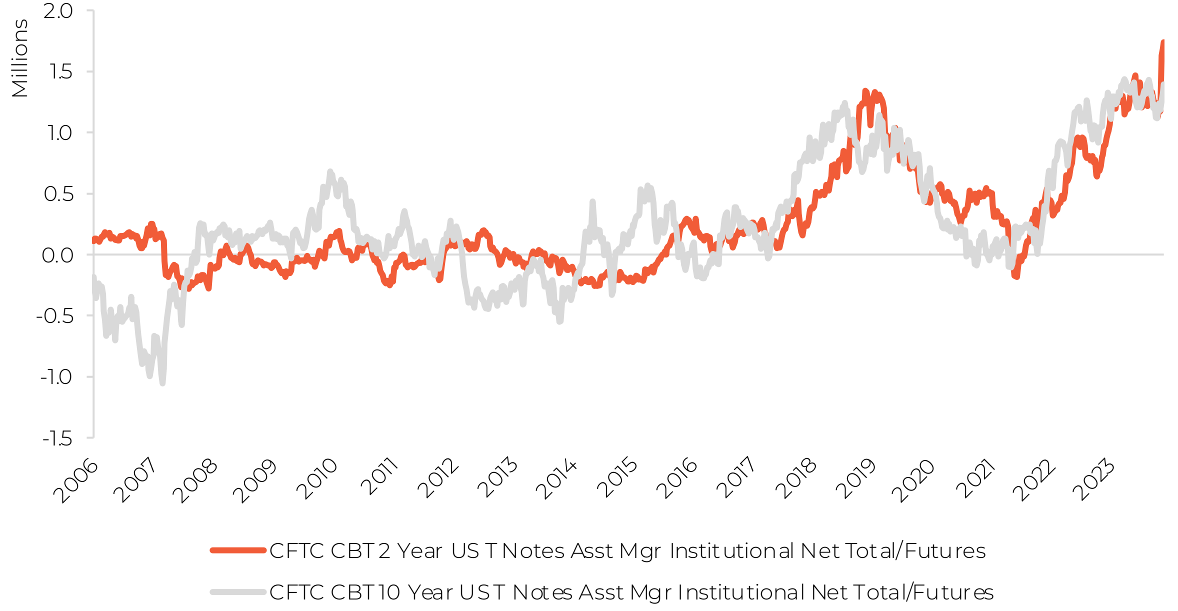
Due to negative yields on the debt market, cautious investor sentiment continues to grow, as evidenced by both an overall decline in investment and investor preferences for medium-term government securities.

Dynamics of investor sentiment in the bond market: % of Long and Neutral positions



- The bond market continues to generate negative yields, which is a consequence of the controversy of the Fed's monetary policy.
- As a result, we are currently experiencing one of the highest levels of neutral investor positioning (a small number of both long and short positions), as reflected in the JPMorgan Investor Sentiment index.
- At the end of February, the Neutral Investment Sentiment reached a record high over the past 20 years. Currently, an indicator is slightly below its maximum, but since the end of April, it has continued to grow, indicating that investors are cautious about investing in the bond market.

Dynamics of the volume of opened positions in 2 and 10-year US government bonds by institutional investors

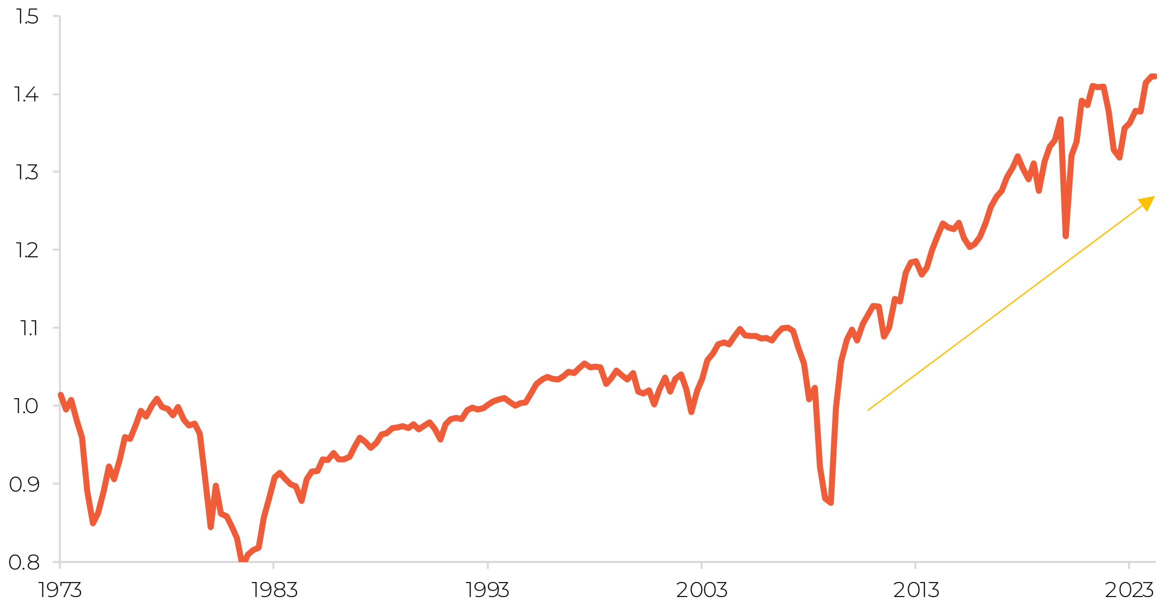


- Also we have observed that the level of investments in 2-year Treasuries reached its maximum last month, but continues to grow according to CFTC data.
- At the same time, investments in long-term debt securities are also growing, but they are much smaller than increases in investments in medium-term bonds and short-term securities.
- Such dynamics are further evidence of investors' cautious expectations about the Fed's possible policy, which, to a large extent, doesn't allow for stable expectations of a rate cut in the middle of the second half of 2024.

Top charts of the week – resilience of corporate debt

Another recent phenomenon is the exceptional resilience of corporate debt relative to the overall market. However, outside of large-cap companies, the interest and debt burden on the corporate sector is significant, which is currently hardly reflected in prices.

Dynamics of U.S. Corporate-to-Government Bond Index Ratio



- It is particularly remarkable that, after Covid period, the ratio of corporate securities to US government bonds is extremely high. And unlike the stock market, this ratio is not a typical condition, as corporate debt usually carries proportional risks along with higher yields.
- This is partly due to both economic stimulus amid rising interest rates and investor confidence in the corporate sector's ability to withstand potential problems.
- However, high interest rates are a heavy burden for small and medium-sized businesses, as the cost of refinancing of their debt is rising.

Dynamics of US High-Yield Bonds Z-Spread, bp

- In this context, the dynamics of high-risk corporate bonds is even more striking, as ratio to similar government securities is close to historical lows.
- First of all, this ratio indicates that the prices of high-risk bonds do not reflect any real risk that can be practically realized, which has been repeatedly confirmed in the historical context.
- Another problem is that the dynamics of the stock and debt markets are synchronized and ignore any real risk factors. This indicates a potential accumulation of unrealized risk in the debt sector.

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ON WHAT MATTERS MOST

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