Equity market trends: the stock exchanges are split

After having closed the month of July on a negative note, the equity markets saw an improvement in August. Investors' sentiment continues to be rather positive. American equities were performing better (in local currencies) than European. The S&P 500 exceeded the level of February in August, thereby setting a new historical record. On balance, the European equity markets are experiencing a horizontal trend since June. The market continues to be supported by a rather favorable results season in the United States and a further improvement in the economic figures. The absence of a new support package in the United States, and the tensions between the US and China (TikTok, Huawei), did not have a significant impact on investors' sentiment.

However, the activity in some of the sectors (such as, tourism) continues to be much more dependent on the development of the coronavirus than others (for instance, technology). This split is becoming ever more pronounced in the equity markets, where sectoral performances are differing significantly. Technology continues to outperform by far, while cyclic sectors lag behind. The advance of technology equities strongly determines the performance of the market as a whole. This is reflected in the American market's performance, where the weight of technology stocks is greater than the European market. The increasing importance of these stocks in US indices also means that the performance of indices as the S&P 500 is becoming increasingly dependent on the performance of a limited number of stocks.

Equity Markets	August	3 months	Since 31/12	12 months
MSCI EMU NR	3.5%	7.1%	-10.6%	-2.5%
MSCI EUROPE NR	2.9%	4.6%	-11.5%	-2.9%
MSCI USA NR	6.3%	8.2%	4.2%	13.3%
MSCI JAPAN NR	6.4%	-1.5%	-7.7%	1.4%
MSCI EM. MARKETS NR	1.1%	11.2%	-5.7%	5.4%
MSCI AC WORLD NR	4.9%	7.2%	-1.7%	7.3%

(Performances in EUR dd. 31/08/2020) (Source : Bloomberg)

Bond market trends: rising inflation expectations in the United States

In August, the risk-free returns rose, but remain within the range in which they have fluctuated for several months. The German and US reference bond rates reached respectively -0.40% and 0.75% at the end of the month. The (implicit) volatility of bonds is, as with equities, very low in a historical perspective, which can also be attributed to central bank purchases and their communication on future policy rates.

Striking in the United States is the considerable rise of the investors' inflation expectations. After having fallen by more than half following the coronavirus outbreak in March, the inflation expectations have re-reached their pre-coronavirus level again in the United States (around 1.75% based on the 10-year inflation-linked bonds). This evolution reflects the improved economic situation on one side, and on the other, the Fed's communication, to tolerate inflation above the 2% target for some time into the future. In the eurozone, market inflation expectations have only recovered just over half of the lost ground.

The spreads on higher risk issuers were lowered even more in August, both in respect of the governments (southern countries in the eurozone) and the companies. The February (pre-coronavirus) level has not been fully achieved.

Government Bond Yield 10 yr	Current	August	3 months	Since 31/12
Belgium	-0.14	0.08	-0.12	-0.23
France	-0.10	0.10	-0.02	-0.21
Germany	-0.40	0.13	0.05	-0.21
Italy	1.09	0.08	-0.38	-0.32
Greece	1.10	0.01	-0.43	-0.37
Spain	0.41	0.07	-0.15	-0.06
United States	0.70	0.18	0.05	-1.21
Japan	0.05	0.03	0.05	0.06

(Evolution until 31/08/2020) (Source : Bloomberg)

Central banks: new inflation objective of the Federal Reserve

During the annual symposium of central bankers in Jackson Hole, Federal Reserve chairman Jerome Powell announced the - expected – change in the definition of the inflation objective. From now on, the Fed will use an average inflation objective. Up to now, the Federal Reserve sought to keep inflation in the medium term around 2%. However, since the inflation objective was implemented in 2012, inflation has too often stayed below that objective. Using an average inflation objective, the central bank would seek to keep the inflation for a given period (an undetermined period, for instance, an economic cycle) on average at the 2% objective level. Suppose the inflation remains below the target during a certain time. In that case, the central bank can tolerate that inflation rises above the target again to achieve the average on the whole period. This evolution means that if inflation were to rise above 2%, the central bank would not tighten monetary policy directly, which means an implicit relaxation of the monetary policy.

Central Bank Rates	Current	Latest adjustment	Date
Fed funds	0.0-0.25%	-1.00%	mar. 2020
ECB deposit rate	-0.50%	-0.10%	Sept. 2019

(Situation on 31/08/2020) (Source : Bloomberg)

Currencies: dollar continues to be weak

After its sharp depreciation in July against the euro, the dollar remained relatively stable against the common currency in August. Since May, the dollar has depreciated against the euro by 10%. The decline of the dollar is due to structural factors (budget deficit, current account deficit) and more recent factors (reduced interest rate differences, also highlighted by the Fed's new inflation objective).

The pound Sterling remains relatively stable despite new messages that hardly any progress is made in the negotiations between the United Kingdom and the EU about their future trading relationship after the transition period has ended on 31 December. The Japanese yen weakened slightly after the unexpected departure of the Japanese Prime Minister Abe.

In the emerging markets, the Brazilian real depreciation continues unabated, mainly due to the government's possible loosening in the budgetary discipline.

Currencies	Current	August	3 months	Since 31/12
USD	1.194	-1.3%	-7.6%	-6.4%
GBP	0.893	0.8%	0.9%	-5.5%
JPY	126.39	-1.3%	-5.6%	-3.6%
CHF	1.078	-0.2%	-1.0%	0.6%

(Evolution versus EUR until 31/08/2020) (Source : Bloomberg)

Commodities: more volatility for gold

The gold price rose to 2,050 dollars per ounce at the beginning of August, a historical record price. However, after the considerable rise of the last few months, the precious metal could not keep its level above 2,000 dollars, due to temporarily higher risk-free bond rates. But the redefinition of the Fed's inflation target could support the price of gold over the medium term if inflation expectations rise at a time when nominal rates remain at current low levels.

The oil demand is recovering, but both the International Energy Agency and the OPEC have lowered their expectations for the oil demand due to the weakening recovery of mobility (and air traffic in particular). OPEC + production limitations have been reduced by 2 million barrels to 7.7 million barrels per day in August. The oil price increased slightly more in August, but on balance fluctuated around 45 dollars per barrel.

The rebound of industrial metals continued in August. Prices are supported by the rapid recovery of industrial and construction activities in China.

Commodities	Current	August	3 months	Since 31/12
Commodities (GSCI)	358.21	5.4%	16.7%	-17.9%
Oil (Brent)	45.28	4.6%	28.2%	-31.4%
Gold	1971.90	-0.4%	13.0%	29.9%

(Evolution in USD until 31/08/2020) (Source : Bloomberg)