KATHREIN PRIVATBANK

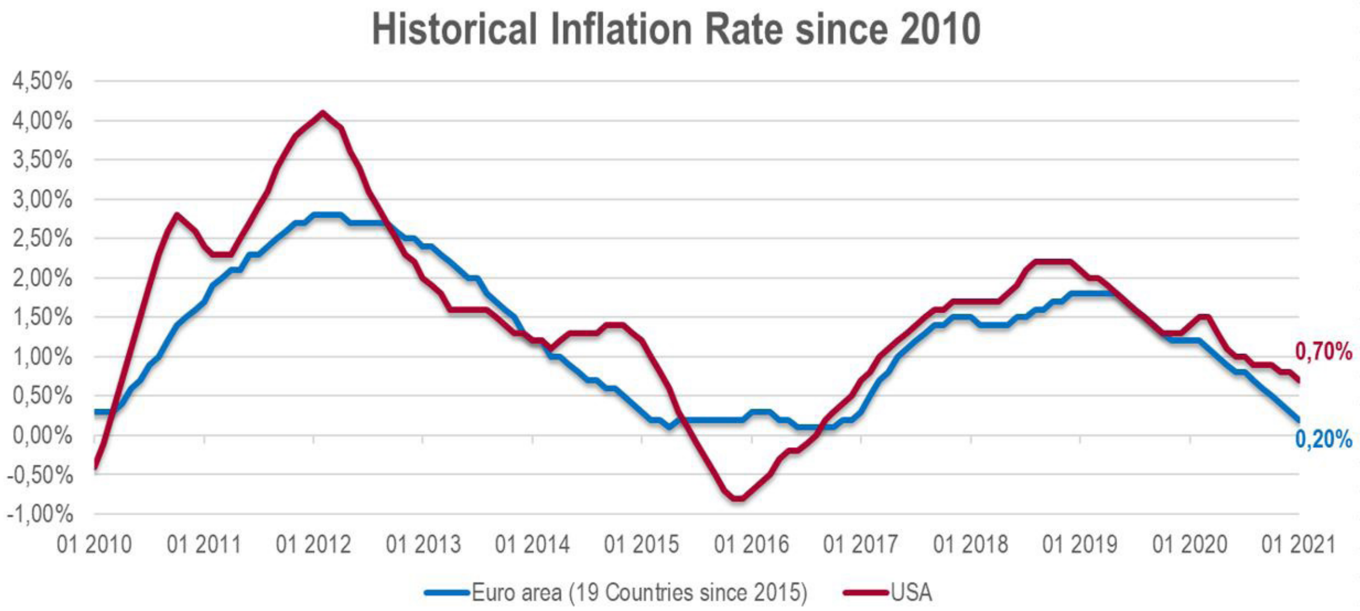
15th of March 2021

Investors' worries: From inflation to bankruptcy

As mentioned in our last stock market commentary and the subsequent ad hoc release, the spectre of inflation is once again making its appearance after a long time. Some investors are reacting with nervous selling and/or reallocations of their portfolios. Since, in our view, the fear of a sudden, very sharp rise in inflation seems unlikely for a variety of reasons, we maintain a positive outlook for the capital market.

But what is driving up inflation concerns again and what are the implications for the capital market?

The USD 1.9 trillion US fiscal package, which is expected to be officially signed by Joe Biden on Wednesday, is not only fuelling economic optimism, but is also raising concerns about rising inflation.



Source: Eurostat

In addition, commodity prices have risen sharply, and, above all, the money supply is playing a major role. In the Eurozone, this increased by 11.7 per cent compared to the previous year and in the USA by more than 25 per cent. In general, this was already historically high due to the current negative or low interest rate environment.

However, if one looks at the actual level of inflation, it is still relatively low in both the USA and the Eurozone:

But what if lockdowns become a thing of the past?

This is where investors' fears come into play again: they fear higher inflation in the short term if savings and deferred investments find their way back into the real economy. However, if Jerome Powell (Fed President) and Christine Lagarde (ECB President) are to be believed, so far it does not look as if the central banks will reduce their support purchases - let alone stop them completely. Given the generally high level of public debt, there are very few reasons from an economic point of view why this should happen.

Is the wave of bankruptcies coming?

After the lockdowns and the disappearance of state support, insolvencies will probably increase sharply. This will probably also lead to an increase in defaults in the bond sector. However, we see this risk primarily in small and medium-sized enterprises. Our strategy in our bond portfolio is to focus on quality and to hedge. We invest mainly in solid large corporations and use our models to take a critical look at the probability of default. With these methods, we keep the risk-return ratio within a reasonable range.

Where do we go from here?

At the beginning of the year we already pointed out that short-term setbacks on the stock markets were to be expected. Provided that no exogenous events affect the market (environmental catastrophes, terrorism, political instability, etc.), we do not see any significant change in the upward phase that has continued so far and, by the way, is still quite young. Therefore, we will use phases of weakness in the stock market for additional purchases. The spectre of inflation no longer seems to scare other market participants. The broad indices from the USA and Europe climbed slowly again last week.

Kathrein: Quality and opportunity

By the way, with Kathrein Privatbank's active asset management you can concentrate on other things than inflation. Our portfolio management observes a multitude of other important indicators and is supported by signals from various capital market models and findings from empirical market analysis. For more than 20 years, our team of experts has been constantly optimising portfolios in all market situations. It is best to ask your personal private banker about the diverse and individual possibilities of Kathrein wealth management.

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