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Biden plans to double the US capital gain taxes – US equity market sold off

The White House plans to double the capital gains tax rate for those earning USD 1 mil or more, from 20% to 39.6%. This would affect about 0.32% of all American taxpayers who report adjusted gross income of more than USD 1 mil and declared at the same time capital gains or losses on their tax statement.

This plan is not new, it was even on a prominent place on the home page of the Biden election campaign. But the Bloomberg headline which crossed the wire yesterday at around 7pm CET was enough to let US equity markets drop by a bit more than 1%. For a taxpayer in New York the total tax on capital gain including Obama tax and others would rise to 52% and in California it would even reach 57%. It is very unlikely that this plan passes both parliaments, but it is just the beginning of a series of expected Biden initiatives to increase taxes to finance the actual fiscal stimulus and the planned infrastructure and green deal packages.

Fig. 1: S&P 500 drops after the tax increase plan was published



Not all stocks were affected by the tax selloff. The new clean energy sector broadly closed sharply up due to Biden's plans to invest around USD 15 bn in EV-infrastructure and energy saving infrastructure projects. Solar and wind energy stocks together with hydrogen companies were among the biggest winners in Europa and US equity trading. Nevertheless, since the beginning of the year most of this new energy stocks lost value.

Fig. 2: New Clean energy stocks sold off since February 2021



On the 14 of January, we have pointed out the hydrogen sector shows some sings of euphoria, In the actual selloff they were hit the hardest, which is no surprise as for instance Plug Power was up almost 100% during the first 14 days of 2021.

Fig. 3: Hydrogen Shares are showing signs of euphoria (table from BFI 14.01.2021)

Company	Ticker	YTD	Y/Y
Plug Power	PLUG US	98%	1,541%
FuelCell Energy	FCEL US	75%	855%
ITM Power	ITM LN	19%	457%
Bloom Energy	BE US	23%	288%
NEL	NEL NO	15%	263%
Ballard Power	BLDP US	50%	258%
PowerCell	PCELL SS	25%	102%
Nikola	NKLA US	32%	95%
Average		42%	482%
S&P500 Index		1.3%	28.9%

Source: JPM

However, we do see potential in this sector. The wind energy and solar companies are already established, and most are profitable. In the hydrogen sector most companies are still loss making and it is unclear where this technology will be used in the coming years beside heavy trucks.

It is interesting that Asian shares are decoupled form US trading. For instance, China A-Shares have fallen to its 200-day average while the US markets reached new all-time highs. Now, however, we see the opposite, while Asian shares do recover, American shares start to consolidate and trend down. Technical indictor like the RSI shows that we are oversold in the CSI 300 index while we are at the same time overbought in the S&P 500.

Fig. 4: China A-Shares (CSI 300) have rebound from its recent lows



Bloomberg has recently published a study which shows that every time over the last 18-months the S&P 500 trades around 16% above its 200-day average we do see a pullback. So far, this countermove has not happened yet.

Fig. 5: S&P 500 at frothy levels



We therefore still expect that the US market will consolidate or even pullback around 10% over the coming weeks. A crash, i.e., more than 15-20% downside is not expected based on the ongoing fiscal and monetary stimulus and the expected acceleration of the global economy.

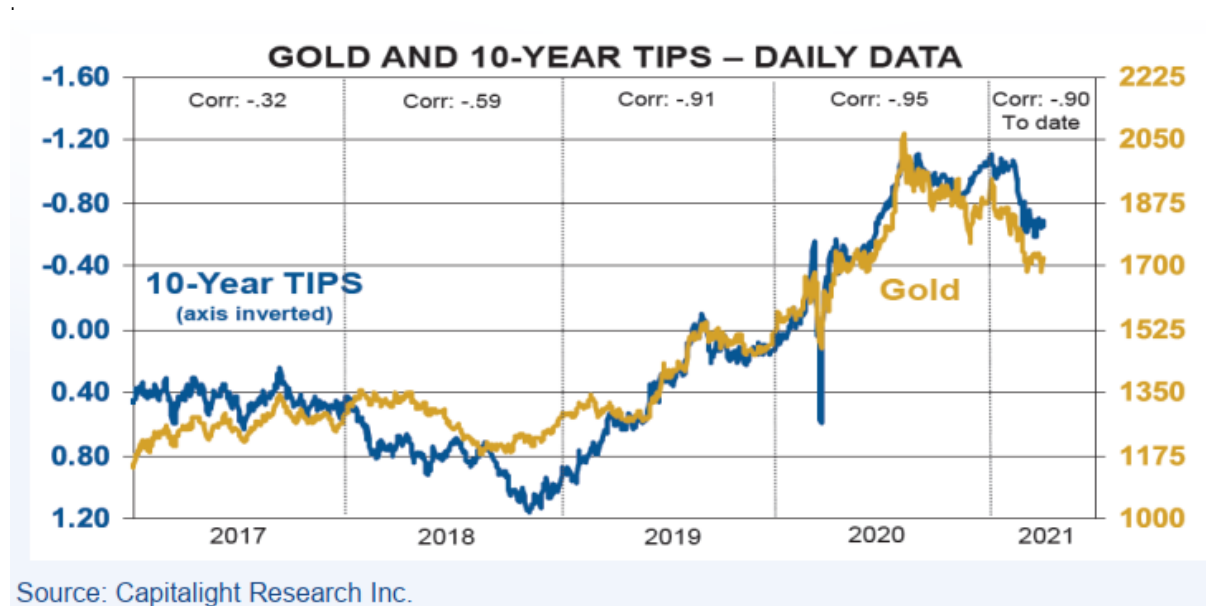
Since the US treasury 10-year yield has reached 1.77% we do see a consolidation and lower yields. We expect slightly higher US yields mid-term as the next data points of CPI and PPI will be higher due to a base effect. But it looks like treasury yields should not be reaching 2% soon. Recent published trading statistic has shown that China and Japan used yield levels above 1.7% to increase their holdings in treasuries, which in hindsight explains why we have seen a continuation of slightly lower US government bond yields.

Fig. 6: 10-year treasury yield continue to decrease



Speaking of gold we believe that the recent twice tested levels below USD 1'700 will mark the low and we might break through the USD 1'800 level over the coming months. If inflation goes up, gold gives a partial protection. There is a strong correlation between the TIPS yield and the gold price. When inflation goes up, we can expect that the TIPS yield drops, and we might see a higher gold price.

Fig. 7: Lower expected TIPS yield (due to inflation) should support a higher gold price



Overall, we must conclude that corporate bond markets and equity markets have moved to levels where a correction must be expected any time. Safer asset like US treasury and US IG corporate bond indices lost around 4% during 2021 and might lose more due to higher expected yields over the coming months.

Having said that we still believe that mid-term equities and real asset like gold should deliver some positive returns. Based on the positive global growth outlook, non-IG bonds might deliver at least an average coupon for the rest of the year as we do not expect a significant spread widening.

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