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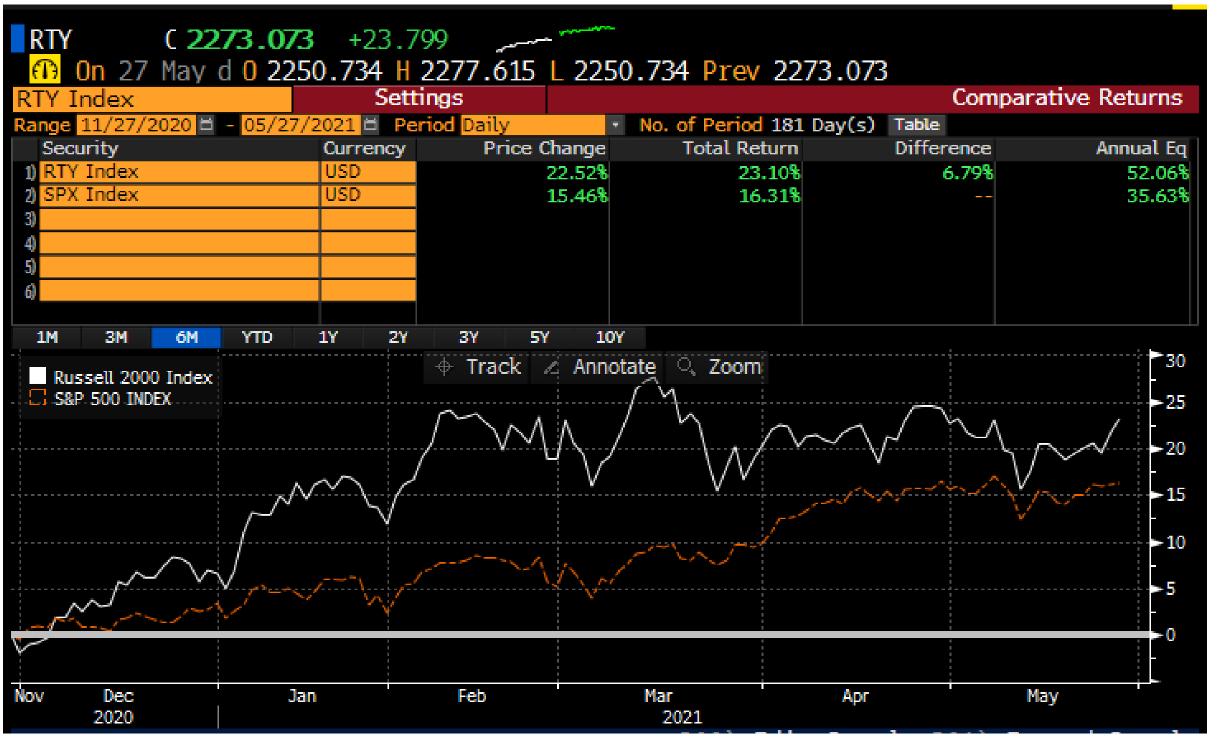
Biden's announcement of larger federal spending plan made US cyclical stocks rally

President Biden wants to increase the federal spending to USD 6 trn in 2022, which would push the debt to GDP ratio up to around 117%. This at first sight astonishing high figure is based on the already announced and known president's request of a minor increase of around USD 300 bn. The American Rescue Plan (ARP), the two-infrastructure packages of more than USD 4 trn and the pending request to Congress for USD 118 bn in addition to discretionary spending, sums already up to a total budget for FY2022 of around USD 5.7 trn. Therefore, this new announcement is just around USD 300 bn more. Nevertheless, this budget is unprecedented, and its financing is open. Short-term it will be financed with new issued US government debt. The plan to raise taxes for this will be opposed by the republicans in both US parliaments. We can also expect that not the whole amount of USD 6 trn will be approved by these parliaments.

But what is more important is how does the market react: We have seen steady prices in treasuries but rising US equity futures and already yesterday rising US small caps.

Fig. 1: Russel 2000 surge outpace the S&P 500 after Bidens new spending plan

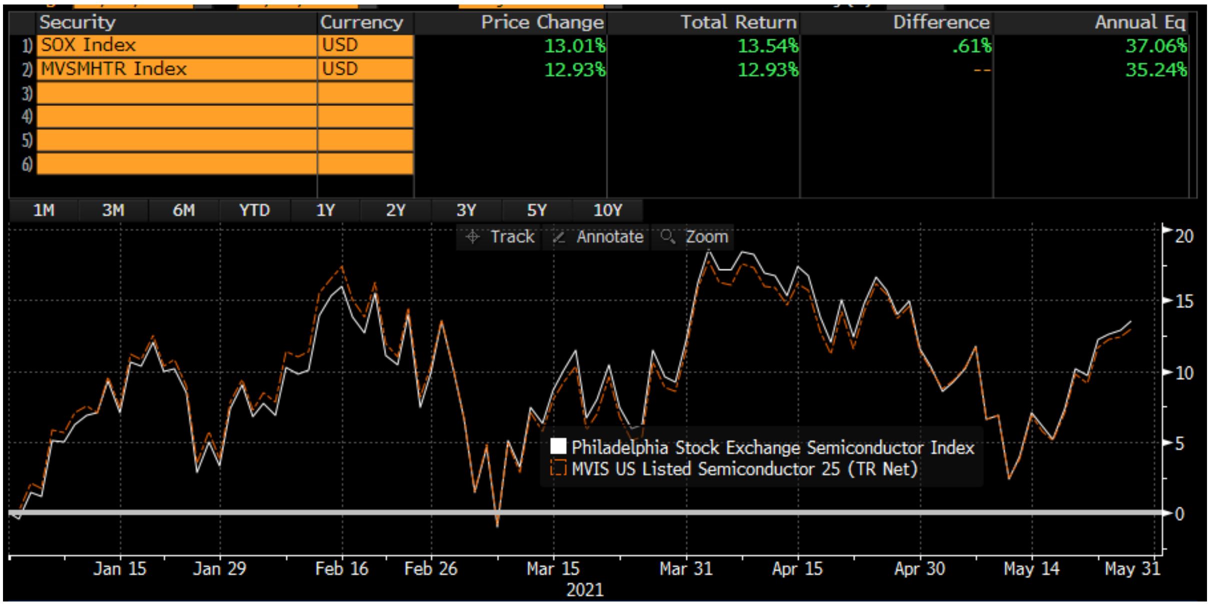


The spending plan had as well an impact on industrial metals which rallied after the news was released. In Europe stocks are rising due to the hope that the ECB will not curb stimulus. This is mirrored in Stoxx Europe 600 which has reached a new record level. Similar pictures in the DAX and the SMI. In Germany market watchers expect that we are going to see more M&A

activities like the merger between the two largest German real estate companies and more spinoffs like Siemens has done over the last years. Both would imply higher Dax prices

Fig. 2: Dax on its way up to 20'000?

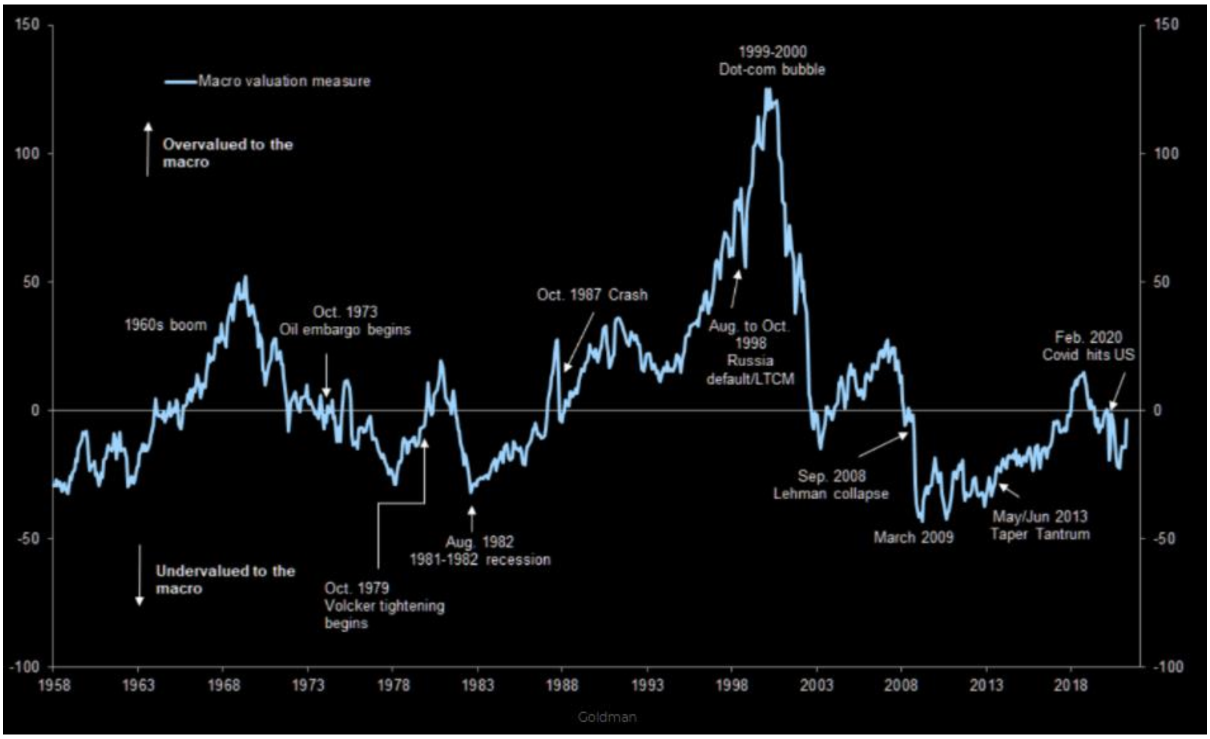
Fig. 3: Semiconductor Indices before a new record?



We therefore expect that the Dax will break out of its sideways channel and might overpass the 16'000 level in the coming weeks. Germany is also profiting from the expected cyclical recovery which will support its export companies which are mainly summarized in the MDAX and SDAX. If this unfolds semiconductor producers will as well profit from this general growth trend and from the overhang of demand for microchips. The US semiconductor index or its global pendant have surge over the last trading days. Both indices are still below their record levels and these stocks are valued compared to their own history at attractive levels.

Turning to valuation, the 2022 S&P 500 PE ratio has fallen below 20x down from around 25x in January. Shiller PE on the other hand stands at 37x which is the 2nd highest level on record. Only in Spring 2000 we have seen higher levels of around 43x, Goldman Sachs has just published a valuation indicator for the S&P 500 and makes the point that US large caps are not overvalued. We therefore continue to see more upside for US stocks. The elephant in the room is what will happen once the Fed starts reducing its bond purchasing program. Recent "Fed talks" about possible reduction of the buying program caused positive reaction on US equity markets and US treasury markets.
Therefore, we might just see a hick up once the Fed starts its tapering talks.

Fig. 4: US stocks look attractively priced based on this Goldman Sachs model



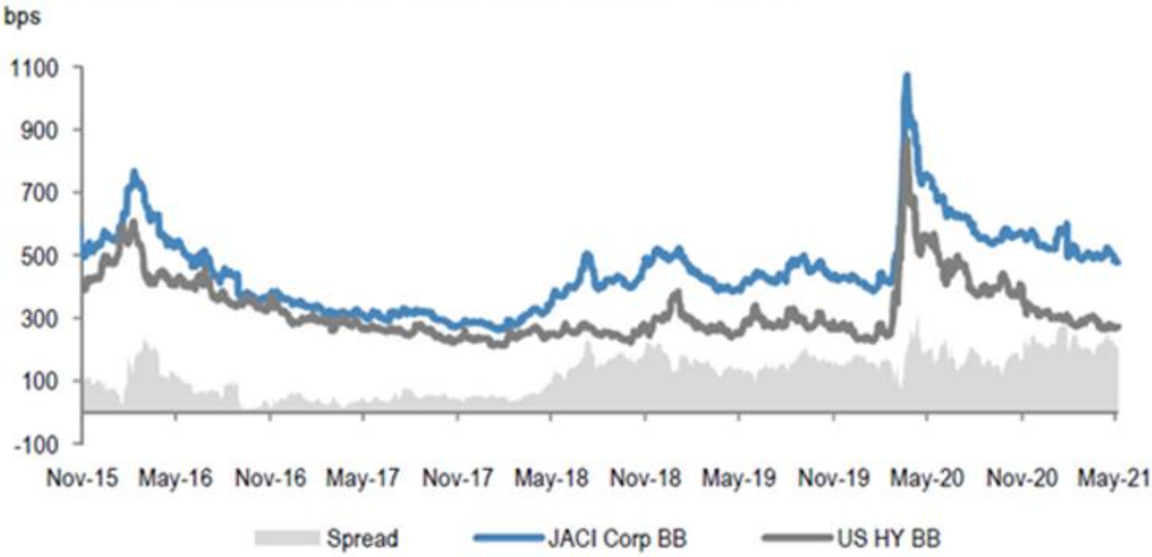
Gold has overcome its resistance levels below USD 1'900 faster than expected. There were rumors that recent inflows into Gold ETFs came from sellers of bitcoin products. From a technical standpoint gold has a clear uptrend and rising fears of higher inflation should support a further rise.

Corporate US HY bonds keep surprising with tight credit spreads and a positive return in 2021. The outlook for defaults has significantly improved due to the strong expected US recovery. We do not expect any significant turbulences in this market as long as the economy keeps growing at this strong pace. However, we do see in the BB space more opportunities in Asia than in the US. The yield pickup is still around 2% and the duration of 2.3 years almost 2 years shorter than in the US.

Fig. 5: Momentum speaks for a further rise of the Gold price

Fig. 6: Asian BB has a better risk / return than US BB corporates

Figure 3: Asia BB Corporates (ex-FINANCIAL) vs US BB Corporates

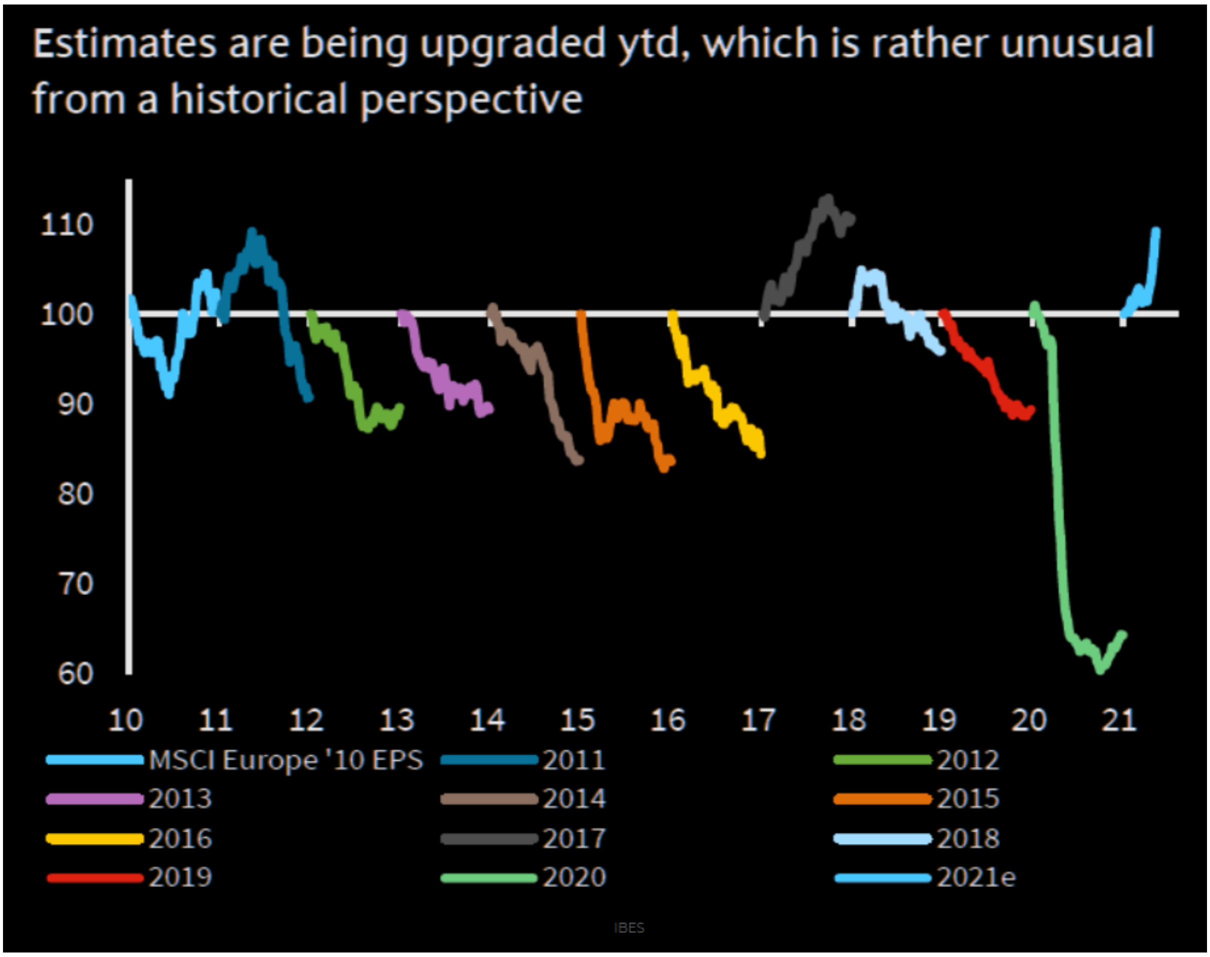


Source: J.P. Morgan. Data as of: May 7, 2021.

	SOT to worst	Dur to worst	YTW, %
JACI Corp BB	479	2.3	5.2
US HY BB	271	4.1	3.4

Note: SOT refers to spread over US-Treasuries

Fig. 7: Earnings estimates are upgraded after Q1 releases



Overall, our assessment that corporate bonds and global equity markets have moved to levels where a correction can be triggered any time stays unchanged. Having said that we would expect that into the summer we do see positive market developments. The earnings season in the US and in Europe was very strong and the aggregated EPS estimates for 2021 have further risen. This is very unusual, last time we had such a situation was in 2017 where the S&P 500 rose 19% without any significant correction and the Vix collapsed.

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