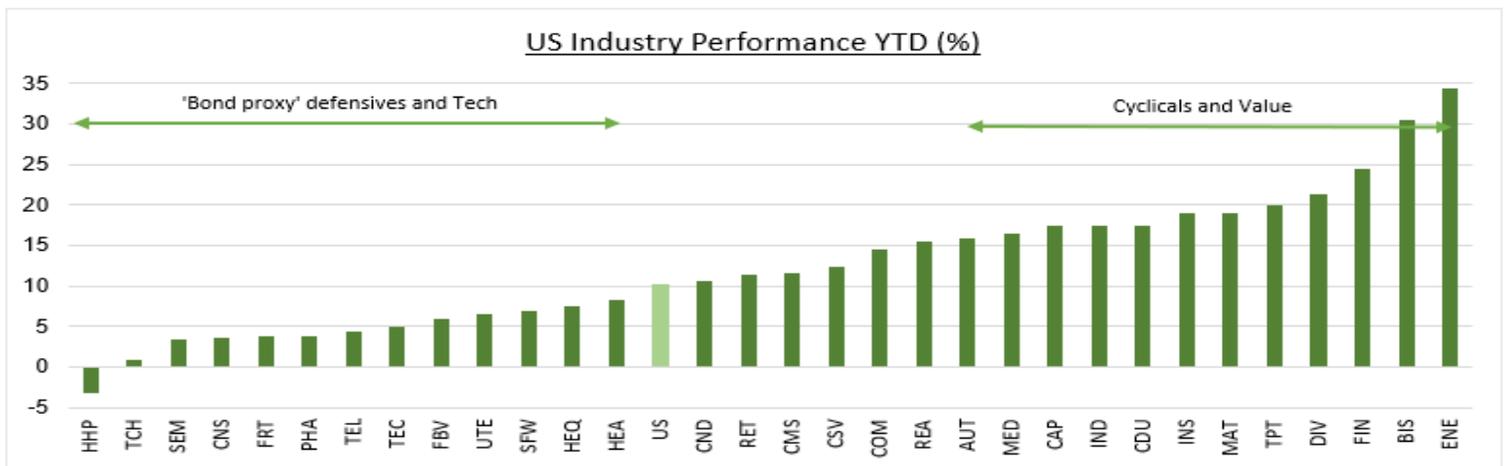




Daily Macro Insights: Let's talk sector rotation

06/05/2021

- 1) **SECTOR ROTATION:** We have three thoughts on US industry performance YTD - see chart. a) Cyclical and value have led, powered by energy (XLE) and financials (XLF). We think this has further to go as the GDP recovery keeps surprising, earnings leverage is high, valuations much cheaper, and investor positioning light after a decade of underperformance. Financials is by far the cheapest US sector, at a 40% 12m forward P/E discount to market. b) Bond proxy segments such as consumer staples (XLP) and healthcare, along with tech, are likely to keep lagging given rising bond yields, high valuations, and lower leverage to the GDP improvement (<2.5x EPS vs revenue growth vs 4x+ for cyclicals and value). Their fundamentals are strong, but more longer term structural, than here-and-now cyclical. c) This has been an 'everything' rally, with more breadth than last year. Equal-weight S&P 500 outperformance is at a decade high. This is healthy but also shows the small number of large underperforming sectors holding back the rally. Tech (XLK) and healthcare (XLV) are the two largest US sectors, with an overall 40% weight. *We see further US equity upside, led by cyclicals and value.*
- 2) **COST OF CARBON:** Europe's ETS carbon price reached a symbolic EUR50/t, up 50% YTD, and c25x higher than the estimated global average price imposed on CO2 pollution. Europe has taken the lead in pricing carbon pollution, but the direction of travel for the rest of the world is clear given the current low pollution cost and ever increasing emission cut targets. This is a growing boost for renewables (ETFs such as TAN), and headwind for polluters. *A costing of current global pollution levels at the European ETS price would cut global earnings c25%.*
- 3) **TODAY:** UK in focus with a chance the Bank of England follows the Bank of Canada in moving to temper its bond purchases, reflecting the strong vaccine-driven GDP recovery underway now. This could be a positive for sterling (GBPUSD), and offset possible headlines from the Scottish local elections, where a strong SNP showing would raise the chance of an eventual second independence referendum. *Tapering to be the sterling focus.*



Source: MSCI, Refinitiv, Etoro calculations

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