US stocks closed at all-time highs led by Technology and Consumer Discretionaries on the day Joe Biden disclosed his infrastructure plan and the first quarter of the year came to an end. The yield on the 10-year Treasury note and Brent crude were little-changed, gold regained the $1,700/oz level and the dollar recorded minor losses. One might suspect that US long-dated yields may now go through some fatigue following the significant quarterly rise and the consensus bearish sentiment on Treasuries. Also, Technology, Discretionaries and gold, to different degrees sensitive to rates, provided constructive signals in yesterday’s session.

The quarterly performance across asset classes was marked by the reflation trade, which usually sees equities outperform all asset classes alongside commodities, credit spreads tighten, long-dated yields rise and gold lose ground, as they did. The behaviour of the US dollar has shown less consistency during recoveries and this time was in keeping with newfound US exceptionalism. In the three months through Thursday European equities rose by almost 9%, followed by the S&P 500 +6% and EM stocks, +2.2%. High-yielding bonds outperformed higher-quality peers, although EM Sovereign credit recorded mid-single digit losses being more negatively exposed to the duration factor. Gold lost almost 10%, Brent crude surged by 23% and the US dollar was up by 3.5%.
One can be tempted to conclude that the easy money on the reflation trade has been made and views going forward can be more uncertain. Will the Cyclical-versus-Defensives and Value-versus-Growth trade in equities continue? Probably not as forcefully. Will the rise in yields be sustainable and the yield curve steepen significantly? Probably not if the recovery turns out to be mainly stimulus-driven and lack own momentum. Will the dollar appreciate further? Probably not for the longer term if US exceptionalism fades. The message in the end is simple: once the recovery trades or any trades for that matter become more obvious, they deliver smaller and less consistent returns, unless powered by strong and lasting trends. And it seems that one long-lasting driver is going to be provided by the infrastructure push announced by Joe Biden today.

Biden proposed investments of about $1.7tn in physical infrastructure and research and development to be spread out across 10 years. Another $500bn would be spent for workforce incentives and Medicaid benefits, bringing the total package to $2.2tn as expected. Another proposal, related to interventions in childcare, healthcare and education, is to be outlined in April increasing the total price tag further. Technically, the package could be approved by means of the so-called reconciliation process, which means that the Democratic majority would be sufficient to push it through Congress. Two points are important: the spending should take a few years to ramp up, as it is usually the case with infrastructure plans; the package would be paid for with an increase in the corporate tax rate to 28%, the tackling of corporate tax loopholes and to a lesser extent by increasing also the personal tax rate. Details about proposed taxes changes will anyway be provided in May.

Stay safe.

MAURICE GRAVIER
Chief Investment Officer
Wealth Management
Emirates NBD.
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