Monthly Newsletter Savings and Investments

China's regulatory crackdown weights on global emerging markets

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Market overview

Developments in financial markets over the recent weeks showed a somewhat subdued investor optimism regarding global economic growth. While the very good second-quarter earnings results from US and European companies led to a rise in the MSCI World stock market index of almost 2%, much more investors' attention was drawn to the Chinese government's growing focus and potential constraints on local technology companies such as Alibaba and Tencent. This resulted in 13 percent drop for Chinese equity indices, which then dragged on the entire emerging market stock market down. In addition, the growing number of new COVID-19 infections in the world raised more questions about the sustainability of the current impressive growth rate of the global economy. According to preliminary data, in the second quarter of the year alone, the US economy grew by 1.6% and the euro area by 2%, which is a very solid result. However, the new wave of COVID-19 poses a significant risk that the global economy may slow down as winter season approaches. Increased vaccination has so far allowed governments to lift more and more economic restrictions, but there are also some indicators that warn of a slower growth in the future. For example, World Manufacturing PMI survey showed declining sentiment among manufacturing sector representatives for the second month in a row. And while in absolute terms the indicator still remains high and signals growth, historically consistent deterioration in expectations in the manufacturing sector has also led to a slowdown in economic growth.

Increased tensions in the market could also be evident in the bond markets, where, despite extremely low and often negative yields, demand for the safest bonds increased, leading to higher prices. For example, ten-year German government bond yields have risen from -0.10% in May to -0.5 per cent in July approaching the beginning of the year level. Falling bond yields (rising bond prices) is not typical for such a strong economic and equity market growth and may reflect two scenarios that investors are predicting: either a prolonged (and perhaps even more aggressive) ultra-loose central bank monetary policy or a much faster economic slowdown than current economic data tells. Therefore, as has become the norm, the fiscal and monetary policy measures in the world's major countries will continue to be a key factor in the markets. In July, the US Federal Reserve acknowledged that economic growth in the country was in line with its forecasts, but better economic indicators were still needed to tighten monetary policy measures, especially in the labor market.

Market tensions are likely to remain slightly higher in the near term compared to the extremely calm and positive first half of the year. Still, interest rates in high-quality bonds remain negative, and growing consumption and population mobility suggest good corporate performance in the third quarter as well. As a result, investors are likely to be more willing to take on more risk, even in a more turbulent period, which will favor riskier investments such as corporate stocks.

Stock market indexes' performance (until 31st July 2021)

Region	Index	Curr.	July	2021	3 months	1 year	3 year	5 year
World	MSCI World	EUR	1,8%	18,7%	6,39%	34,70%	48,09%	83,87%
World	MSCI Emerging Markets	EUR	-6,7%	3,4%	-2,95%	20,31%	24,07%	54,48%
US	S&P 500	USD	2,3%	17,0%	5,12%	34,37%	56,07%	102,21%
Europe	MSCI EURO	EUR	1,1%	16,0%	3,91%	31,65%	15,62%	38,91%
Eastern Europe	MSCI EM Eastern Europe	USD	-1,4%	14,4%	9,86%	27,34%	14,41%	50,30%
Asia	MSCI EM Asia	USD	-8,4%	-3,6%	-7,60%	16,35%	24,40%	61,39%
Latin America	MSCI EM Latin America	USD	-4,2%	2,4%	5,63%	21,41%	-7,14%	4,94%

Expectations

Economic recovery and GDP projections. Second quarter corporate earnings, which started to be published in July, showed a strong increase in consumption and general economic activity in many countries. This suggests that global economic growth will remain high and total world GDP is expected to return this year and even exceed pre-pandemic levels. World GDP is projected to grow by about 5.8 percent in 2021 and by 4.4 percent in 2022. The Baltic economies, which showed resilience last year, are expected to continue to outpace the euro area average, with the Baltic economies expected to grow by around 4.1% this year. this year is 4.4 percent. next year.

This year's risks. While rising inflation remains one of the most concerning issues in financial markets, the worsening pandemic situation has recently become more important again. For the time being, governments tend to continue to lift some of the economic constraints, but the spread of the delta variant may force them to turn back on a tightening path again. In this case, the economic growth rate could slow down at the end of the year significantly more than expected.

The US Federal Reserve (FED) is likely to announce the start of a bond-buying program tapering in the next couple of months, and this could also put some tensions in the markets, at least for a short time. However, the Fed has been trying to prepare investors for such a step for quite some time already, reiterating that any significant monetary tightening action (raising interest rates) is possible only if the US economy stands firmly on its feet.
