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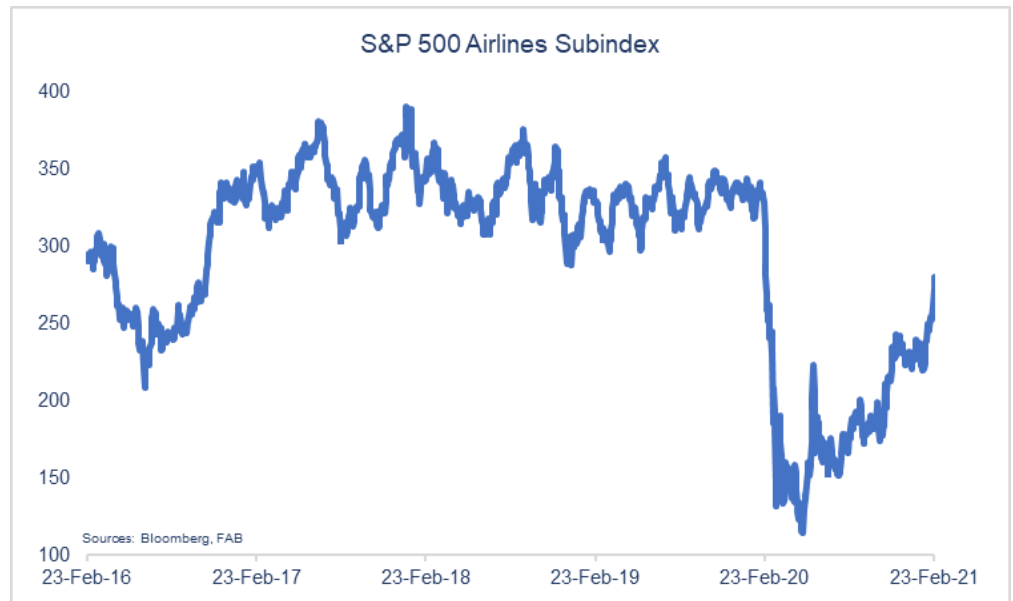
The reflation trade could hurt some of the reopening trades

◆ Some of the sectors favoured by investors as potential winners once global lockdowns are lifted are highly sensitive to fuel prices, for one.

◆ Higher food and fuel prices could add pressure to wages, and impact one of the most important inputs for the services sector.

◆ Airlines, cruise operators and hotels face higher costs just as the prospect of reopening business returns.

◆ The FAB AAC is overweight in equities, IG and EM bonds, and gold, and is underweight in alternatives.



Since pharmaceutical companies gave signs that they could create and mass-produce a vaccine for the coronavirus faster than expected, a group of industries which had been badly hit by the pandemic has started to recover.

Most stocks of airlines, hotels, cruise operators and restaurant franchises are still behind where they were before the pandemic, but the recovery of the so-called 'reopening' sectors in markets has still been breathtaking.

The S&P 500 Airlines subindex is up 45% since 15 May, when it bottomed, and has gained 22.1% so far this year. The index is up 6.95% in the past two days alone as investors got excited about more fiscal stimulus in the US and the progress of the global vaccination campaign.

The S&P 500 Hotels, Resorts and Cruise Lines subindex is up 162.55% since 3 April, its recent bottom, and has gained 14.51% year-to-date.

The recent excitement seems valid, given that countries that have been effectively in lockdown for nearly a year, such as the UK, are talking seriously about a broad reopening calendar as they vaccinate a growing proportion of the population.

More than 177 million people have been vaccinated around the world, and the early indications from countries such as Israel, where a large part of the population has already been inoculated, indicate that the vaccine is effective in controlling the virus.

Adding to the excitement, the US Food and Drug Administration today said that a Johnson & Johnson vaccine is "safe and effective", paving the way for the approval of the first vaccine that requires a single shot. This may push the reopening stocks even higher today.

However, the excitement is also pushing oil, food and market yields higher, all of which will increase the costs of some of these industries reopening for business.

The S&P 500 Airlines subindex has rallied 45% since it bottomed on 15 May, 2020

Airlines and cruise line operators are particularly sensitive to higher oil prices, and Brent crude is up 27.13% year-to-date. Hotels are not immune to that either, as they use quite a bit of energy to heat or cool down their premises.

Food prices also impact all three industries, though they may be better able to pass on those costs to consumers. The trouble is they may increase the wage pressures as employees seek higher salaries to cope with more inflation.

These three industries also tend to lease their airplanes, ships and buildings, and the cost of those leases goes up with market yields. While there is plenty to be excited about the reopening trade, the reflation trade could also hurt it.

Investment Strategy Update

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