GLOBAL OUTLOOK

ECONOMY & FINANCIAL MARKETS

ANDBANK
Private Bankers

Andbank Monthly Corporate Review | Andbank Monthly Corporate Review – August / September 2020

Corporate Review

August / September 2020

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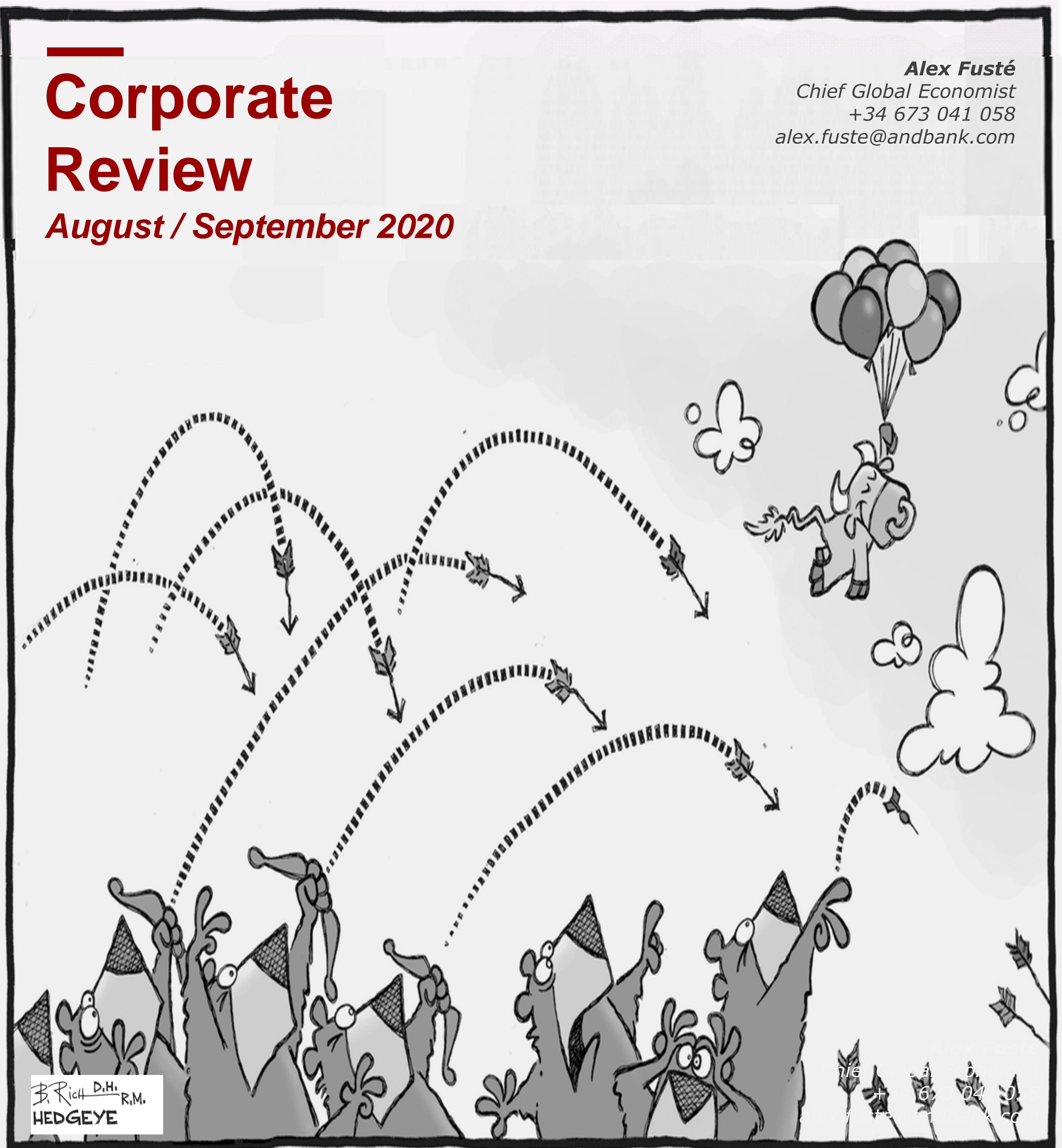
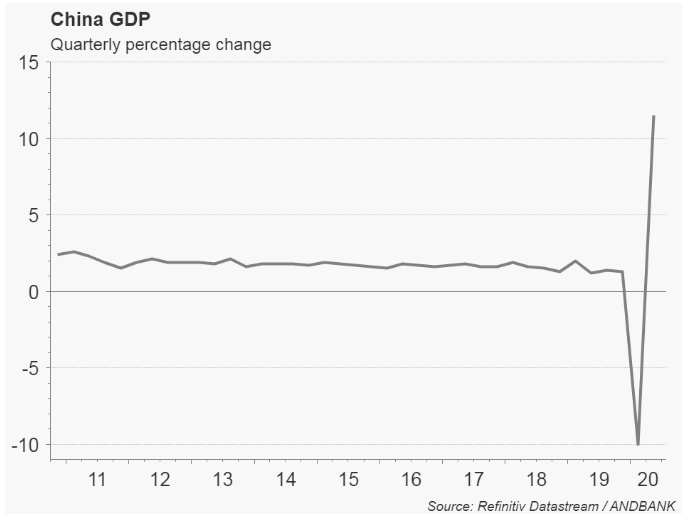


EXECUTIVE SUMMARY

CHART OF THE MONTH



Source: Refinitiv Datastream / ANDBANK

EQUITIES

Index	INDEX CURRENT PRICE	Current Fair Value (EPS 12 month fw)	2020 E[Perf] to Fair Value	Recomm	2020 Exit Point
USA S&P 500	3.258	2.962	-9,1%	MW	3.407
Europe - Stoxx Europe 600	362	340	-6,2%	MW/OW	408
Euro Zone - Euro Stoxx	355	330	-7,0%	MW/OW	395
Spain IBEX 35	7.047	7.764	10,2%	OW	8.541
Mexico IPC GRAL	37.721	36.374	-3,6%	MW	40.011
Brazil BOVESPA	105.605	102.027	-3,4%	MW/OW	112.230
Japan NIKKEI 225	22.339	19.878	-11,0%	MW/UW	23.854
China SSE Comp.	3.287	2.968	-9,7%	UW	3.265
China Shenzhen Comp	2.227	1.894	-15,0%	UW	2.083
India SENSEX	37.736	33.891	-10,2%	OW	40.669
Vietnam VN Index	801	864	7,8%	OW	1.037
MSCI EM ASIA	592	533	-9,9%	OW	640

FIXED INCOME GOVIES CORE & CORPORATE CREDIT (DM)

Asset Class	Indices	Current Price	Fair Value EPS 12m fw	Expected Performance to Fair Value 2020
Fixed Income	US Treasury 10 year Govie	0,56	1,20	-4,9%
Core countries	UK 10 year Gilt	0,10	0,80	-5,6%
	German 10 year BUND	-0,52	-0,20	-2,8%
	Japanese 10 year Govie	0,01	0,00	0,1%
Fixed Income	Spain - 10yr Gov bond	0,33	0,60	-2,0%
Peripheral	Italy - 10yr Gov bond	1,04	1,40	-2,4%
	Portugal - 10yr Gov bond	0,32	0,60	-2,1%
	Ireland - 10yr Gov bond	-0,13	0,30	-3,5%
	Greece - 10yr Gov bond	1,02	2,05	-7,8%
Fixed Income	Credit EUR IG-Itraxx Europe	59,94	70	-0,2%
Credit	Credit EUR HY-Itraxx Xover	363,25	400	0,2%
	Credit USD IG - CDX IG	71,80	70	0,5%
	Credit USD HY - CDX HY	454,24	450	2,2%

FIXED INCOME EMERGING MARKETS

Asset Class	Indices	Current Price	Fair Value EPS 12m fw	Expected Performance to Fair Value 2020
Fixed Income	Turkey - 10yr Gov bond (local)	12,66	11,75	12,6%
EM Europe (Loc)	Russia - 10yr Gov bond (local)	5,95	5,00	10,1%
Fixed Income	Indonesia - 10yr Gov bond (local)	6,76	6,00	8,9%
Asia	India - 10yr Gov bond (local)	5,82	6,80	-5,4%
(Local curncy)	Philippines - 10yr Gov bond (local)	2,82	3,00	-0,2%
	China - 10yr Gov bond (local)	2,93	2,75	2,7%
	Malaysia - 10yr Gov bond (local)	2,61	2,00	5,9%
	Thailand - 10yr Gov bond (local)	1,18	0,25	7,9%
	Singapore - 10yr Gov bond (local)	0,82	0,40	3,7%
	Rep. Korea - 10yr G. bond (local)	1,13	0,75	3,5%
	Taiwan - 10yr Gov bond (local)	0,30	0,00	2,5%
Fixed Income	Mexico - 10yr Govie (Loc)	5,66	6,20	-1,9%
Latam	Mexico - 10yr Govie (USD)	3,16	3,70	-3,0%
	Brazil - 10yr Govie (Loc)	6,49	8,20	-10,9%
	Brazil - 10yr Govie (USD)	4,36	4,20	3,1%

COMMODITIES & FX

Asset Class	Indices	Current Price	Fair Value EPS 12m fw	Expected Performance to Fair Value 2020
Commodities	Oil (WTI)	40,9	40,00	-2,2%
	GOLD	1.955,9	1.600	-18,2%
Fx	EURUSD (price of 1 EUR)	1,176	1,100	-6,4%
	GBPUSD (price of 1 GBP)	1,30	1,32	1,6%
	EURGBP (price of 1 EUR)	0,91	0,83	-7,9%
	USDCHF (price of 1 USD)	0,91	0,97	6,1%
	EURCHF (price of 1 EUR)	1,07	1,07	-0,7%
	USDJPY (price of 1 USD)	105,05	107,00	1,9%
	EURJPY (price of 1 EUR)	123,51	117,70	-4,7%
	USDMXN (price of 1 USD)	22,12	23,50	6,2%
	EURMXN (price of 1 EUR)	25,98	25,85	-0,5%
	USDBRL (price of 1 USD)	5,17	5,50	6,4%
	EURBRL (price of 1 EUR)	6,08	6,05	-0,5%
	USDARS (price of 1 USD)	72,19	90,0	24,7%
	USDINR (price of 1 USD)	74,82	74,00	-1,1%
	CNY (price of 1 USD)	7,00	6,90	-1,5%

USA
A targeted approach to virus control

Covid-19

The continued rapid spread of the virus has led some states to re-impose various types of restrictions, albeit taking a more preventive approach and considering both the health and economic aspects, therefore far from embracing a 100% health management approach and financially very painful. So far states have relied on two key policies: mandating mask wearing (with fines of $100 for citizens who do not wear them), and restricting high-risk social activity, such as restrictions on certain riskier activities like restaurants and nightlife. Based on this new approach, we are seeing some positive results in the control of the contagion curve (with four daily observations below the maximum observed on July 17).

About the severity of the situation: There are only four states at Level 0 (the most affected): Alabama, Nevada, Georgia and Texas, where their economies are still open, but with a limit on their corresponding service capacity. None of these states has reached saturation level in their health systems. Only Rhode Island and Alabama have a lower level of availability, with a 20% Covid patient occupancy rate, although they have the possibility to increase capacity through the provision of mobile hospitals. In summary, infections and daily death rates are stabilizing in a country that is trying to learn how to live with the virus and normalize this situation through the use of containment measures that are not highly damaging economically. Full lockdown is seen by states as a decision of last resort.

Economics: The virus resurgence has caused consumer activity to decelerate as a result of slightly tighter state restrictions and voluntary social distancing. Broader consumer activity stalled in many states, but according to hard frequency data, the economic impact has not been dramatic. Consumer spending slowed during the third week of July, although it remains flat since the start of July and about 2% above the average level in June. This temporary stalling of the economy threatens to inflict some longer-term damage on unemployment, as businesses like bars and restaurants are forced to close for a second time, which could lead to a jump in permanent closures. This is starting to be reflected in the jobless claims dynamics, with declines in initial jobless claims for unemployment insurance programs, becoming fairly modest in recent weeks after being substantially higher between the end of March and early June.

Public support

Lawmakers returned to Capitol Hill in the third week of July with the goal of drafting the next coronavirus stimulus bill. While democrats have proposed generous aid to Americans with a bill of $3 trillion, the Republicans want more targeted spending of around $1 trillion. Priorities for the talks include funding to speed up development of coronavirus vaccines and therapeutics to “Protect the American worker and those that employ individuals” and for the manufacturing sector, particularly bringing jobs back to the US from abroad.

Elections: What would Biden mean for the markets?

Some 106 days remain until the presidential elections in the US, where current polls point to a Biden victory, with an increasingly likely Democratic sweep on the legislative agenda, particularly tax/regulatory, and which we feel will be less favorable to growth. Biden’s call for greater federal coordination on Covid testing/tracing represents a good trade-off between economic damage and virus control. A China trade war will likely continue under both Biden and Trump, but Biden’s rebuilding of alliances elsewhere (vs. levying tariffs) may quell corporate uncertainty. While both of the national conventions this year will be no real contest, they will provide insight into the parties’ respective platforms and reforms. The Democratic National Convention will be held mostly virtually on August 17-20 in Milwaukee, Wisconsin, to formally nominate the party's candidate. The Republican Convention will be scaled back and held in Jacksonville on August 24-27. Three presidential debates are scheduled for this fall (Sept 29, Oct 15 and Oct 23) and Election Day is Tuesday, November 3, 2020.

Financial market assessment

Equities – S&P: MARKETWEIGHT (Target 2,962. Exit point 3,400)

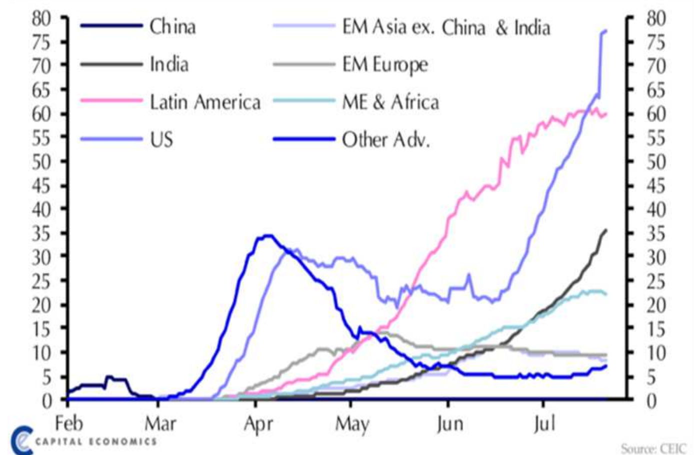
Bonds – Govies: UNDERWEIGHT (10Y UST Entry point 1.2%)

CDX IG: MARKETWEIGHT (Target Spread 70)

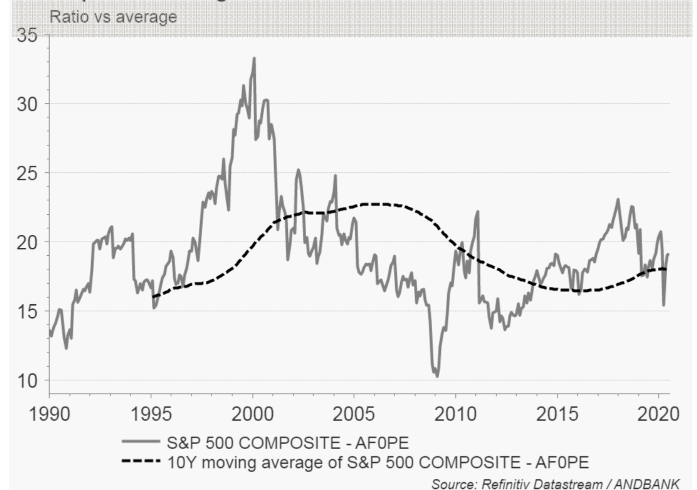
CDX HY: MARKETWEIGHT (Target Spread 450)

Forex – DXY index: MARKETWEIGHT

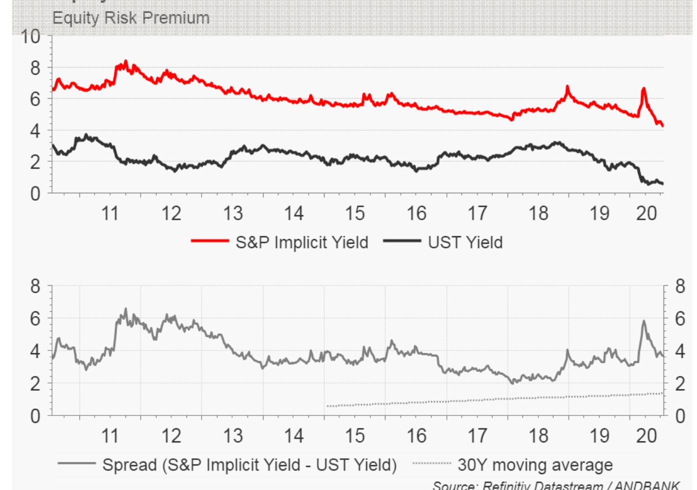
Total daily new infections by country/region (7d MA)



US price-to-earning ratio
Ratio vs average



Equity Yield & UST Yield
Equity Risk Premium



EUROPE

“We did it!” (Michel on the Recovery Fund)

Green light for the (greener) Recovery Fund

These are the final numbers of the agreement: €750 bn, 5.4% of 2019 EU-27 GDP (as expected), of which 52% will be in grants and the remaining 48% in loans (more biased towards loans than the Commission’s proposal). A total of 30% of the funding would be allocated to climate investments (vs. 25% originally suggested) at the expense of lower allocations for health spending, innovation, a smaller Just Transition Fund, the disappearance of a solvency instrument (focused on the recapitalization of European corporates to achieve a “level-playing field‘)... The Fund’s governance is the more controversial point as it increases political oversight and could delay or reduce the Fund’s flexibility. Financial assistance will have to be embedded into national recovery plans with “milestones and targets”, which will be scrutinized by the EU Commission and approved by the EU Council. If “serious deviations” are perceived (also referring to respect of the rule of law), individual countries could pass the matter on to the EU Council, which would decide within three months. In terms of commitments: 70% of the grants would be signed off during 2021-2022, and 30% in 2023. All in all, we view the agreement as positive. A step forward in integration with determination and ambition, and an overall acceptance of joint issuance as the financing instrument. Other European facilities are already being implemented, such as the SURE facility (Support to mitigate Unemployment Risks, €100bn in loans). A total of 18 member states have indicated interest in SURE loans for a total volume of €94.5bn.

Sharp recovery in the last month but could we see a cliff edge for September macro? The ECB’s stance.

There has been a sharp recovery in both the manufacturing and services surveys (almost back to pre-crisis levels), although consumer confidence lags behind. The best news is on the sentiment and consumer front (retail sales, labor figures), but further evidence remains to be seen from the external and industrial side. September could be a crucial month with a significant part of the guarantee schemes expiring, and unless activity genuinely recovers, there could be a cliff edge effect. This explains the ECB’s cautious economic approach, despite acknowledging the macro improvement, underlining the importance of phasing out the stimulus. Regarding Covid-19, we have seen some resurgence in European daily cases. Though still very early to classify it as a second wave, a risk of further restrictions (even lockdowns) in some countries (such as Spain) is not negligible. As expected, the last ECB meeting was a non-event with no new monetary measures announced. Using the full potential offered by the PEPP (Pandemic Emergency Purchase Programme) was the most relevant question. Lagarde’s reply was affirmative, saying this would happen “unless there were significant upside surprise.” However, we subsequently learned that there is no consensus around this issue. We also received an estimated impact of the ECB monetary boost on Eurozone macro aggregates: +1.3% in GDP and +0.8% in terms of HCIP until 2022. Tackling climate change is also embedded in the ECB’s next goals. Lagarde has committed to examine “greener” changes to all of the bank’s operations, including asset purchases.

European corporate bonds

Inflows continue into both investment grade and high yield. They are still higher in IG, but it is worth noting that the flows in HY€ have already offset the negative effect of sales in 1Q20. The primary market has been calmer lately due to the start of publication of results, and as inflows have continued so European debt spreads have continued to narrow. We expect lower issuance activity in 2H20 (although still historically high), highlighting the amount issued by non-financial companies (+30% YoY). Companies have positioned themselves in a more defensive way, increasing liquidity using different means: cost reduction, capex reduction, suspension of share repurchases, dividend or corporate operations, employment policies... We continue to see the ECB’s support for investment grade as a key factor for this segment, especially after considering that explicit support for HY “is not on the agenda”. In the financial sector, provisions will be the key to 2Q. S&P estimates them at around €115 bn in Europe in 2020 and 2021 (provisions in 2017, 2018 and 2019 were around €50 bn annually, and profits before provisions about €240 bn each year). In other words, overall the sector could continue to enjoy positive results. Although margin compression will persist (especially in financial companies involved in government aid programs), trading activities in banks with a greater investment bias will contribute positively. For all these reasons, we do not believe that financial spreads will suffer too much. Income will be lower, but supported by lower costs and capital ratios that are not concerning.

Financial market assessment

Equities – Stoxx Europe: MW-OW. Target 340. Exit 408

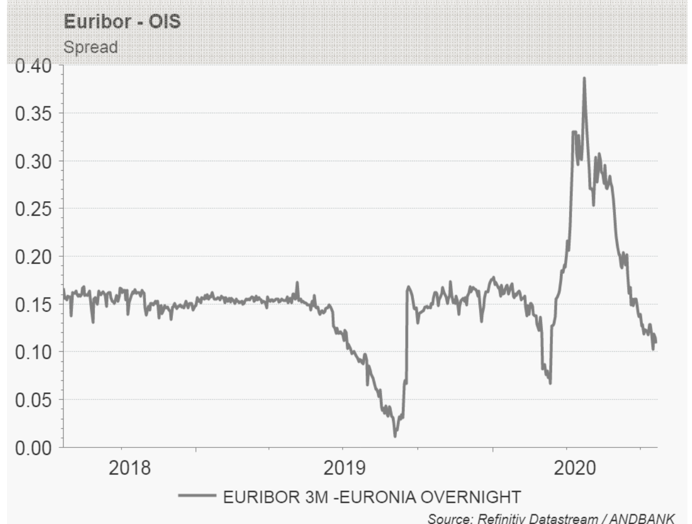
Equities – Euro Stoxx: MW-OW. Target 330. Exit 395

Bonds – Core governments: UNDERWEIGHT (Bund target –0.20%)

Peripheral – MW/UW: IT (1.4%), SP (0.6%), PO (0.6%), IE (0.3%), GR (2%).

Credit – Itraxx Europe (IG): MARKETWEIGHT (Target Spread 70)

Credit – Itraxx Europe (HY): MARKETWEIGHT (Target Spread 400)



CHINA

Beijing is heading awkwardly towards international isolation

Sanctions & the Hong Kong Bill

The WSJ reported this week that President Trump signed into law a bipartisan bill (the Hong Kong Sanctions Bill) that requires sanctions on Chinese officials who crack down on the rights of Hong Kong residents to free speech and peaceful assembly, as well as banks that do business with those officials. Trump also signed an executive order that ends preferential US treatment for Hong Kong, a blow to its status as an international financial center and putting it on equal footing to mainland China. What matters here is the bipartisan-in-nature agreement, which suggests that both Republicans and Democrats have said "enough" to China's expansionist policy in the region. The National Security Council spokesman, John Ullyot, suggested that "US President Donald Trump has not ruled out additional sanctions" on top Chinese officials, in addition to those contained in the law, to punish China for its handling of Hong Kong".

Potential diplomatic & geo-political clash:

In parallel (according to the NY Times), the presidential proclamation about bans on travel to the US by members of the Chinese Communist Party and their families could also allow the US government to revoke the visas of party members and their families who are already in the country, leading to their expulsion. A move that would almost certainly prompt retaliation against Americans seeking to enter or remain in China. This move will exacerbate tensions. In an unusually direct challenge to Beijing, the US has also declared its formal opposition to a swath of Chinese claims in the South China Sea. Washington had previously said it sees Beijing's expansive sovereignty claims over most of the South China Sea as unlawful, but this latest step means that the US is now officially rejecting specific Chinese claims for the first time.

Business-economic clash

The Trump administration plans to shortly scrap a 2013 agreement between US and Chinese auditing authorities, a move that could foreshadow a broader crackdown on US-listed Chinese firms under fire for sidestepping American disclosure rules. The US watchdog has long complained of China's failure to grant requests for access to information, and the lack of transparency has prompted administration officials to lay the groundwork to exit the deal soon.

A de-facto end to the trade deal

President Trump told CBS News that he's "not interested" in engaging in a second round of trade negotiations with China following the Phase One trade deal reached in January. Trump argued that they had made a great deal and shortly after Chine "hit us with the plague", referring to the coronavirus pandemic. He also said he has "no plans to speak to" China President Xi Jinping.

The economy continues to recover

China's Q2 GDP growth was +3.2% YoY (well above the +2.5% consensus and the -6.8% seen in 1Q20). Other high frequency data pointed to continuity of the recovery, with June industrial production expanding at +4.8% YoY (vs +4.4% in prior month). Fixed asset investment (YTD) also improved on a monthly basis (as shown by the significant jump in the year-on-year figure, from -6.3% YoY in May to -3.3% YoY in June). Retail sales also improved (to -1.8% YoY vs -2.8% YoY in prior month). The unemployment rate improved to 5.7% vs consensus 5.9% and 5.9% in prior month. June new house prices were up +0.6% MoM (+0.5% in prior month) bringing annual price growth to +4.9% YoY.

Monetary authorities will remain vigilant and far from easing.

According to the PBoC, China will maintain ample liquidity in the financial system in the second half of the year as the economy recovers from the coronavirus, although it also said that "it will be necessary to consider withdrawing that support at some point". Meanwhile, the China Banking and Insurance Regulatory Commission stated that it will crack down further on illegal activities in the shadow banking sector as part of efforts to contain financial risks. The regulator has found problems, including violations of the new asset management rules during inspections, and urged all banks and insurers to rectify the problems found.

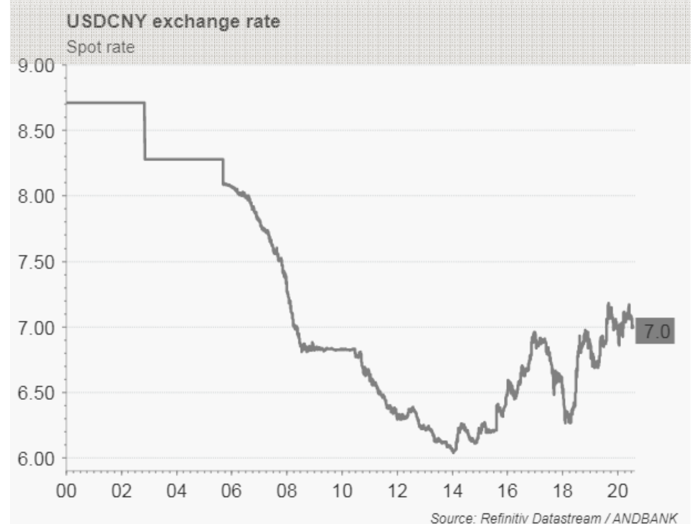
Financial market outlook

Equities – SHANGHAI Idx: UW (Fair value 2,968. Exit point 3,265)

Equities – SHENZHEN Idx: UW (Fair value 1,894. Exit point 2,083)

Bonds – Govies: MARKETWEIGHT (10Y Yield target 2.75%)

Forex – CNY/USD: OW (Target 6.90)



JAPAN

Economic forecasts tweaked. Equities near their exit point.

Covid-19

According to Kyodo, Japan reported a total of 622 coronavirus cases on Thursday, the highest in three months, as Tokyo itself marked a single-day record in cases, adding to evidence that the world is facing a resurgence of the virus after lifting a state of emergency in many countries, including Japan. Tokyo Governor Yuriko Koike announced that the city registered another 293 coronavirus cases on Friday 17, marking a new record. The average daily figure of newly confirmed infections in the capital over the past seven days stood at over 200. Koike said the rise in confirmed cases reflects an increase in virus tests being conducted in the capital, now at over 4,000 a day. The metropolitan government called for maximum vigilance after marking the seventh straight day of triple-digit increases. A health official warned that the average number of untraceable infections in the last seven days had doubled from the previous week, warning that such cases could reach around 1,200 a day in four weeks. Other prefectures such as Chiba, Kanagawa, Saitama and Osaka also saw their largest number of daily cases since the state of emergency was lifted on May 25. Japanese firms see no immediate fix for the virus pain. Some 49% of Japan's companies have no immediate plans in place to help counter the impact of the coronavirus pandemic, although 30% indicated they were looking to improve productivity to cushion the blow. The pain inflicted on the automotive sector was higher, with some 44% of transportation equipment makers having furloughed up to half their employees, versus 14% of overall firms.

Fiscal - Japan sees primary budget surplus delayed to 2028

Japan now expects to achieve a primary budget surplus in FY28, one year later than previously estimated due to fallout from the coronavirus crisis. This was the most optimistic of around four proposed scenarios which highlighted the impact of shorter or longer time frames before the pandemic ends, and higher and lower economic growth rates.

Monetary conditions in Japan continue to push a large volume of capital towards the carry trade

In international transactions for the week ended July 11, Japanese investors were net sellers of ¥3,639.0 bn in foreign equities (vs ¥210.4 bn of net purchases in previous week), but were net buyers of ¥1,065.7 bn in foreign long-term debt (vs a revised ¥520.7 bn of net sales in previous week).

BoJ - Economic forecasts tweaked

The BoJ voted 8-1 to leave short and long term rates unchanged, matching expectations. The reiterated guidance was that current policy settings will remain as long as necessary to keep the 2% inflation target stable, and the Bank will not hesitate to ease further if needed under the expectation that policy rates will remain at present or lower levels. The updated outlook report showed FY20 GDP forecasts revised to show a deeper contraction, while FY21/22 was revised higher. The inflation forecast ranges were generally trimmed. In summary, expectations of a gradual recovery from H2 this year, though only at a moderate pace amid lingering coronavirus effects. The stressed outlook is extremely unclear and dependent on coronavirus developments. As such, the Bank sees risks to both economic activity and prices skewed to the downside. Foreign visitors to Japan fell by 99.9% YoY in June for the third consecutive month. Kyodo cited official data showing foreign travelers to Japan fell in June to 2,600 amid the coronavirus pandemic. This follows 1,700 in May, which was the lowest figure on record going back to 1964. Japanese nationals departing the country in June also fell 99.3% to around 10,700 from 1.52 million a year earlier.

Corporates

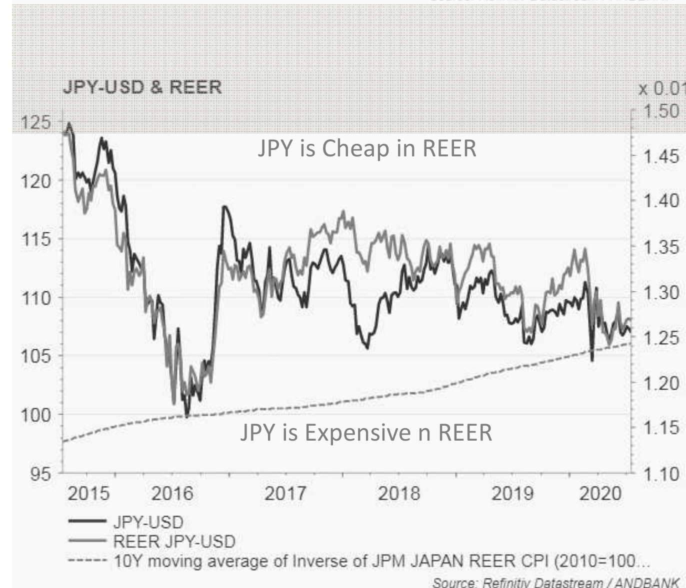
Facebook and Sony are preparing to increase output of upcoming gaming devices by as much as 50%, showing how big tech companies are profiting from consumers' thirst for home entertainment during the global coronavirus pandemic. Facebook's Oculus is eyeing growth of at least 50% from a year ago for its latest version of the head-mounted VR devices, pushing production to 2 million units. Sony has also raised production orders for its upcoming PlayStation 5 to around 9 million units, from the roughly 6 million units it had planned in the spring.

Financial market outlook

Equities – N225: MW-UW (Target 19,878, Exit 23,854)

Bonds – Govies: MARKETWEIGHT (Target yield 0.00%)

Forex – USD-JPY: MARKETWEIGHT (Mid-term target 107)



INDIA
On the verge of a strategic reorientation towards the United States?

Geopolitics

India is joining other democracies in pushing back against Beijing, and is set to deepen its strategic partnerships with the US and other like-minded countries such as Japan and Australia after the border clash with Chinese troops on June 15. In fact, India started with the suspension of some Chinese imports and the banning of TikTok, a wildly popular Chinese video-sharing app. This could be painful for India in the short-term, as annual bilateral trade with China is worth nearly US$100bn, and Chinese firms have invested at least US$15bn in India. However, last month's deadly brawl in Ladakh's Galwan Valley has undone this hard work. China has released no details of its side of the story, and the available accounts agree that Chinese forces instigated the confrontation. Beijing also objected last year to India's designation of Ladakh, formerly part of the quasi-independent state of Jammu and Kashmir, as a separate territory under central government control. Ladakh's formal borders include Aksai Chin, an area of Chinese-held territory viewed by Beijing as vital to the stability of its western frontier. Why should India end its era of "strategic autonomy" and join other democracies in enhanced military alliances? Beijing is exploiting the pandemic to make strategic gains in its neighborhood, motivated by its desire to dominate Asia. China is attempting to consolidate the regional pecking order while the US is both weak and distracted due to a pandemic and political crisis. Note how in addition to slapping down India on June 15, Beijing has forced through the new national security law in Hong Kong, buzzed Taiwan with fighter jets, and stepped up its aggressive campaign in the South and East China Seas. India maintains strategic relations with a number of countries, but potentially the most consequential relationship is with the US, which has delivered vocal public support to India after the clash with China, in addition of providing arms and military intelligence. Washington also maintains long-term regional alliances with Japan, South Korea, the Philippines and Australia, and has long wanted to bring India into a broader security network to limit Chinese expansionism in the Indian Ocean. Recall some of these efforts to lure India into the North-American orbit: In 2005 George W. Bush signed a bilateral nuclear deal with India. Barack Obama signed a Joint Strategic Vision to cooperate on security in the Indian Ocean and western Pacific. Even the Trump administration's first National Security Strategy, released in 2017, pushed for a "free and open Indo-Pacific" anchored by India as the principal US military partner in the Indian Ocean. The most probable outcome is that India will take a more multilateral approach, possibly enhancing its currently loose alliance with the US, Japan and Australia within the Quadrilateral Dialogue, a maritime security grouping conceived by Japan in 2007 as a coalition of "like-minded democracies". Of course, Beijing will see the move as a "quadrilateral military alliance" aimed at isolating China. That now looks a done deal, given Indian media reports that an invitation from Australia to join naval exercises was in the offing, even before the Galwan standoff. India and Australia are also set to sign a Mutual Logistics Support Agreement, allowing reciprocal use of each other's military bases for exchange of fuel and provisions. With both countries currently bruised by Chinese aggression, there should be no shortage of motivation for closer military ties. Australia announced last week that it will significantly boost military spending, including purchasing its first long-range strike missiles from the US. Recent meetings of a "Quad Plus," including South Korea, Vietnam and New Zealand, suggest that it may evolve into a broader grouping. Can this deeper cooperation evolve towards a formal military alliance? That will depend on China's own actions, which for the moment, are not on the right track. As India's rupture with China plays out, it will be economically painful for India. Just how painful will depend, in part, on how the military confrontation in Ladakh is resolved. If Chinese troops fall back to the position they occupied before the summer incursion, Modi can claim a victory of sorts and will be in a position to urge caution and make a less radical policy break. But if China makes a tougher stand, Modi will be under enormous pressure to take a hard line and the economic impact will be higher.

Covid

Bharat Biotech has started the first phase of human clinical trials for India's first coronavirus vaccine candidate Covaxin, which is being developed by Hyderabad-based Bharat Biotech in collaboration with the Indian Council of Medical Research (ICMR). Covaxin has been in news since ICMR director-general shot off a letter on July 2 to twelve hospitals and research centers asking them to enroll subjects for human trials of Covaxin, so that the vaccine is ready for public use by August 15.

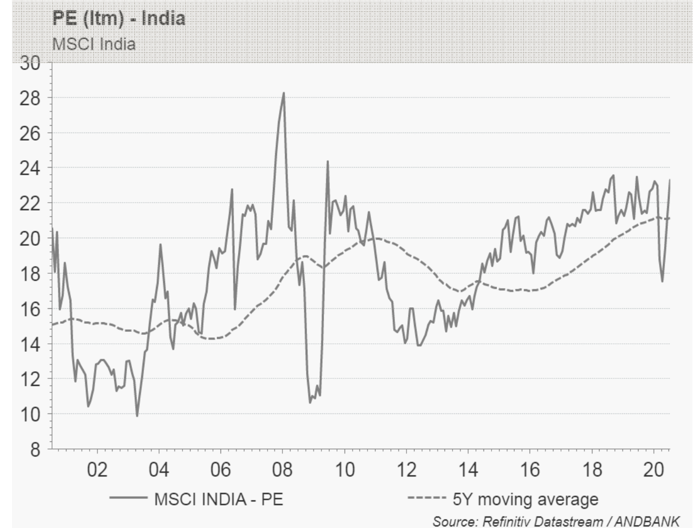
Financial market outlook

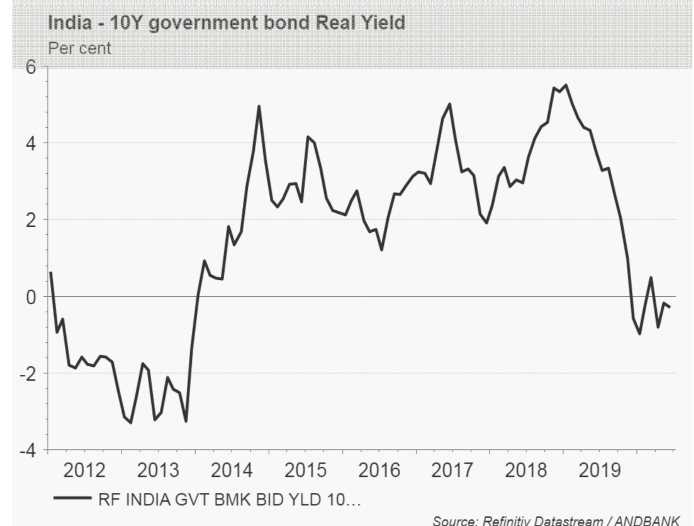
Equities – SENSEX: OVERWEIGHT (Target 33,891. Exit 40,669)

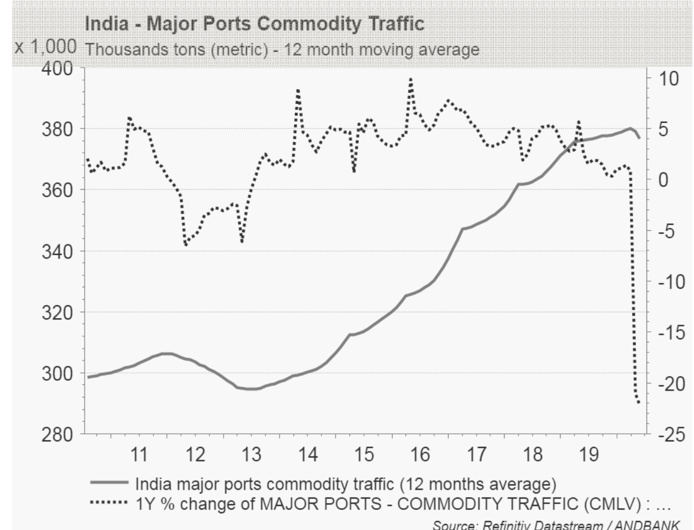
Bonds – Govies: UNDERWEIGHT (Target yield 6.8%)

Bonds – Corporates: MW-UNDERWEIGHT

Forex – INR/USD: MARKETWEIGHT-OW (Target 74)







ANDBANK Private Bankers

MACRO ECONOMY

ISRAEL

Equities & currency are expensive. Bonds fair valued

Covid - Indo-Israeli scientists to work on four Covid tests

A special flight of Israeli scientists is heading to India this week to work with their counterparts to finalize four breakthrough pandemic-related technologies to detect the presence of the SARS-CoV-2 pathogen that causes coronavirus. These include two Covid-19 tests that could give results in minutes from a saliva sample. A third that could tell if a person has incipient Covid by listening to their voice. And a fourth, a virus detector that uses radio waves on a breath sample. The Israelis will work out of AIIMS in the national capital Delhi. "The first phase of testing of these technologies was done in Israel. The last stage will now be carried out in India," said Israel's ambassador to India, Ron Malkin.

Equity Market, Neutral

Since our last update, the TLV 125 index has continued its decline, down -2.3%. The driving forces are "Corona correlated stocks" whose businesses are negatively impacted by the virus. These stocks are mainly related to commercial real estate, financial institutions and shopping malls. Some of the trends determining stock performance include the shift towards home-working (decrease in demand for renting offices), low number of shoppers in shopping malls, and bad debts associated with financial institutions (due to closure of many small businesses). On the other hand there are many companies enjoying a boost in demand due to the epidemic (pharma companies, producers of non-woven fabrics etc.); and hi-tech and bio-med stocks still enjoy a positive trend.

Bond market: Positive

The most significant factor that affected the Israeli financial markets in July was the huge jump in Covid-19 infections, from 300 new cases per day one month ago, to over 2,000 a day. The Israeli government initially started to re-impose a small part of its restrictions, but due to the relatively small number of hospitalized patients, the government did not order a new lockdown and decided to give the public another chance to reduce the infection rate by voluntary social distancing, personal hygiene practices and the mandatory use of face-masks. However, in the last few days, the government has decided to close restaurants, bars, stores and fitness centers at weekends. Unemployment is growing, and the government will shortly announce a new support plan to help those badly affected by the Covid-19 pandemic, as well as giving 750 NIS (~192 Euro) to every Israeli citizen. The Israeli central bank is aggressively stepping up its financial aid for the struggling economy. The central bank renewed its program that gives commercial banks access to 3-year loans at 0.1% interest, as long as they pass on the capital in small-business loans. For the first time ever, the central bank will accept mortgages from commercial banks as collateral, and more importantly, will start buying corporate debt totaling 15 billion NIS (4.5% of the Israeli corporate debt market). The purchases will be done over time, but only corporate bonds issued in NIS with a rating of A- and above will be eligible. The credit spread in the CPI linked TelBond60 index dropped to 1.67%, compared to 1.9% in mid-June and pre-Covid-19 crises spread levels of 1.2%-1.25%. The credit spread in the non-CPI linked TelBond Shikli50 dropped to 1.71%, compared to 1.91% in June and pre-Covid-19 spread levels of 1.3%-1.35%.

Economy & Central Bank

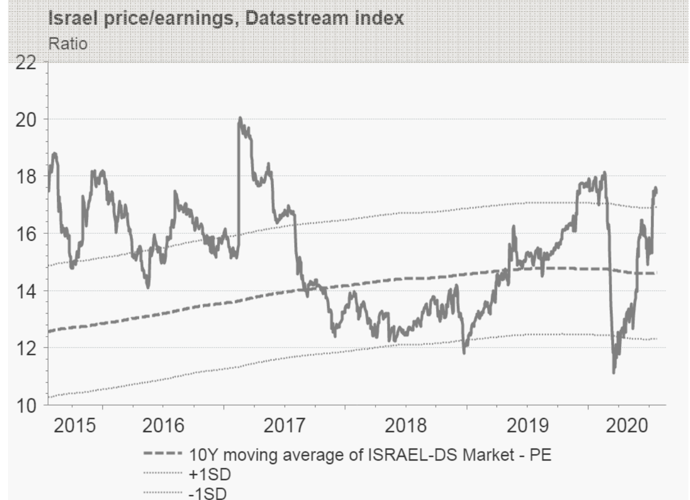
Israel's central bank is expected to leave short-term interest rates unchanged during the last week of July, although analysts believe the chances of a rate cut have risen due to fears of more economic damage from a spike in Covid-19 infections. A total of 13 of the 15 economists polled by Reuters believe the monetary policy committee (MPC) will keep its ILINR=ECI benchmark rate at 0.1%. Two others project a cut to 0%. The April job survey showed that as the first wave of the coronavirus began spreading and the quarantine kept everyone at home, the number of employee positions fell by 27.5% MoM and the average wage went up by 14.15% MoM. The housing market survey recorded its second consecutive decline with a 0.7% fall MoM in May, after a 0.1% decline in April. Israeli foreign trade showed imports declining by 18.7% YoY but rising 3.6% MoM, while exports fell by 34.11% YoY and 25.92% MoM.

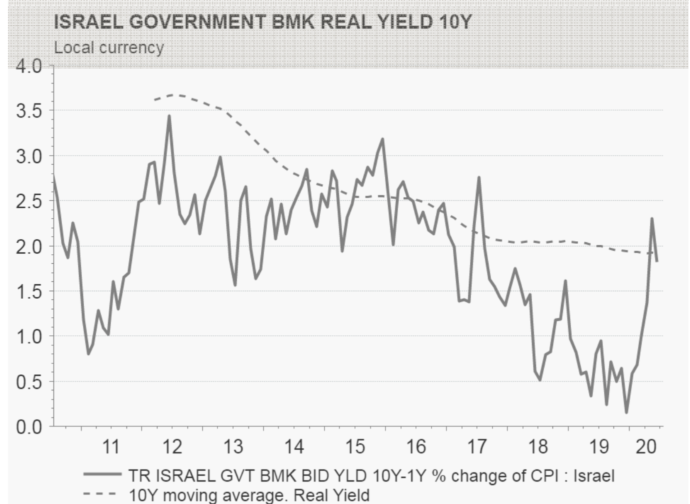
Financial market outlook

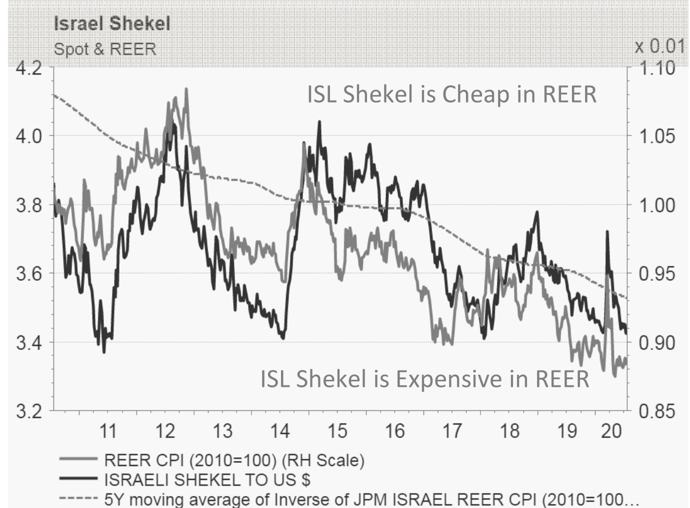
Equities – TLV35 Index: UW / MARKETWEIGHT (Expensive)

Bonds – 10Y Gov: MARKETWEIGHT (Fairly valued in real terms)

FX – ISL vs USD: UNDERWEIGHT (Expensive in REER)







MEXICO

Market weight Equities. Underweight Bonds. Slightly cautious in MXN (target 23.5)

Covid, Economics & Rating outlook

The rate of infections and deaths in Mexico has not changed track and the curve continues to be upward as of July 20. The gradual policy of reopening the country remains in place, with 18 states classified as red and 14 orange, which allows activities such as restaurants, cinemas and office work to operate at 30% capacity. The most recent surveys put the level of acceptance of the López Obrador government over 50%, with his handling of the pandemic and public security being the main cited weaknesses.

Accumulated fiscal income from VAT and other taxes fell by around 30% in May, compared to the cumulative level last year from January to May. There is still an increase in budget income, but below the expected level. Public spending also grew and the primary surplus has fallen to 0.2%. The forecast remains for a deficit of 0.4% of GDP for FY 2020. The Debt-GDP ratio has reached 50% of GDP and is expected to continue to rise as estimates of a double-digit decline in economic activity for the year remain in place. June inflation hit an annual rate of 3.33%, compared to 2.84% in May, above analysts' forecast. Recent analysis by BofA and JP Morgan predict the loss of the country's investment grade between 2021 and 2022.

Monetary environment remains supportive

Banxico cut its interest rate by an additional 50bp to leave rates at 5%. The decision was unanimous and further cuts were not ruled out as stimulus measures for the economy are needed due to the pandemic. The median level from local surveys points to a rate in the 4-4.50% range at the end of 2020, while forecasts are for rates to remain unchanged in 2021.

Mexican Equities

Uncertainty affecting the business sector remains high. For 2H 2020, the possibility of a severe economic decline with a slow and short recovery represents one of the biggest risk factors, as well as the possibility of a public finance imbalance, which could put pressure on key financial variables such as average funding costs due to negative actions by rating agencies. We project a -18% YoY fall in EPS in 2020. Over the next twelve months, EPS could reach 2,553 MEX. Using a PE multiple of 14,25x, we fix our fair value target for the IPC Equity Index at around 36,000 with an exit point at 40,000.

Mexican Bonds

The spread between peso and dollar rates for Mexican bonds has continued to recover since their highest point in March. Peso-denominated bonds currently trade at 518 basis points, following the effects of the cuts in the Banxico yield curve rate and the lower global risk aversion that has favored emerging markets. When it comes to dollar-denominated bonds, spreads have remained much more stable, at around 330 basis points. We have lowered our target spreads for the local bond (to 500 bp, versus its 10-year average of 425) and plowed the dollar bond (to 250, versus its 10-year average of 200). This is based on the fact that despite the lack of economic direction by the AMLO administration, in reality we have not seen a fiscal deterioration, which works in favor of country risk as the US is indeed implementing large spending programs, and we believe this could continue in this way. **Forex - Target at 23.5:** The exchange rate has fluctuated between 22 and 22.70 against the dollar, in a period of lower volatility. However, the peso remains one of the weakest currencies this year, despite the fact that rates in Mexico have been kept higher compared to other economies. This has not been enough to prompt a greater inflow of capital. On the contrary, holdings of peso assets by foreigners are at levels not seen since 2016, while the positioning on Mexico in futures markets is balanced between short and long. Target for MXN-USD at 23.50.

Financial market outlook

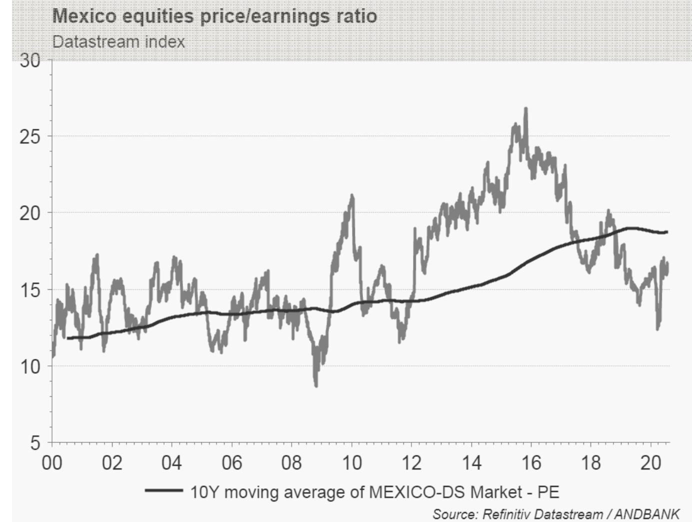
Equities – Mex IPC: MARKETWEIGHT. Target 36,374. Exit 40,011

Bonds – Govies Local: UNDERWEIGHT (Yield 6.2%. Spread 500)

Bonds – Govies USD: UNDERWEIGHT (Yield 3.7%. Spread 250)

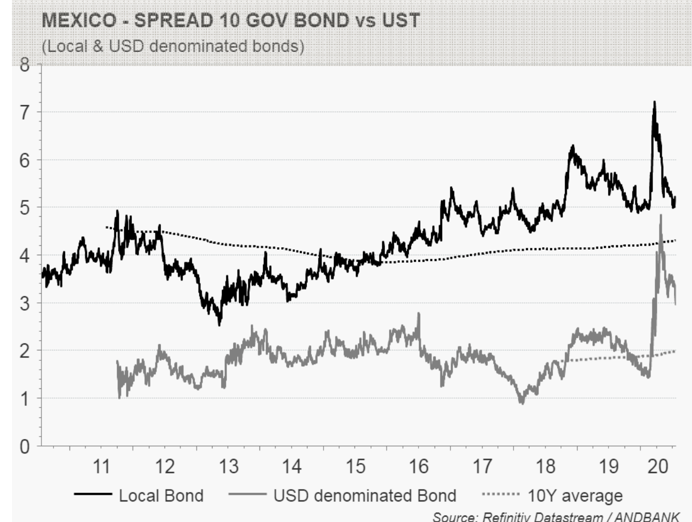
FX – MXN/USD: UNDERWEIGHT (Mid-term target 23.50)

Mexico equities price/earnings ratio
Datastream index



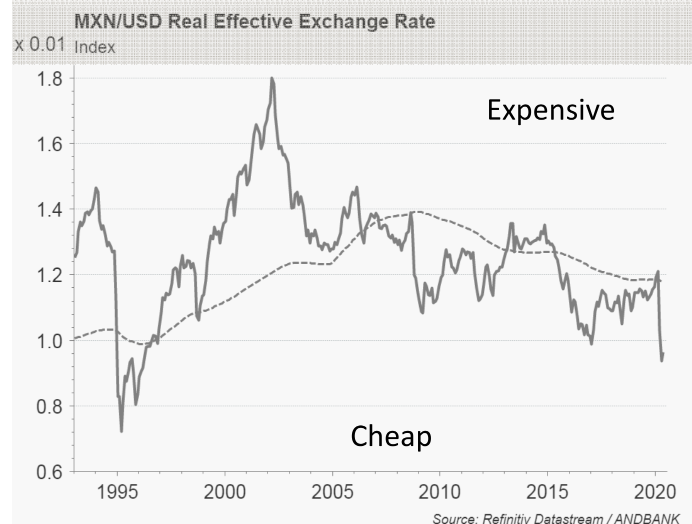
Source: Refinitiv Datastream / ANDBANK

MEXICO - SPREAD 10 GOV BOND vs UST
(Local & USD denominated bonds)



Source: Refinitiv Datastream / ANDBANK

MXN/USD Real Effective Exchange Rate
x 0.01 Index



Source: Refinitiv Datastream / ANDBANK

ARGENTINA

Debt restructuring: New offer. Closer but not there yet.

On Monday 6 July, Argentina published its second official offer and the fourth since negotiations started with a considerable improvement compared with the first offer (53 vs 39 USD NPV @10% yield). The offer includes the following improvements: i) Higher coupons, shorter maturities and no grace period; ii) New 2030 1% bond for past-due interest, up to settlement date for those who tender, and until 04/22 for holdouts dragged by CACs; iii) Introduction of a minimum participation threshold: (A) 2/3 of aggregate, (B) or for each Indenture: b.i) 50% holders or b.ii) 60% including holdouts dragged by CACs; iv) 2005 Indenture holders receive securities with same Indenture; v) Allow EUR and CHF holders to subscribe USD bonds.

Argentina set August 4 as the deadline and in a *Financial Times* interview, president Alberto Fernandez stated that there is not going to be another offer, “We can’t do any more”.

The three largest creditor groups rejected the offer and united to present a joint counteroffer with “significant economic and legal concessions from all three groups…”. The offer is worth 56.1 USD (@10% yield) with economic differences explained by higher coupon rates for the bonds.

The government also filed a draft bill to Congress addressing local law USD debt restructuring (US$41.7 bn & with 34% of private bondholders), with the same terms as those offered to international law bondholders and an option to swap shorter maturity bonds for inflation-linked bonds. It is important to highlight the inclusion of a RUFO clause in case there is an improved offer to international law bondholders.

Provinces & Corporates

Mendoza announced the modification of its debt exchange offer for its international bond (Mendoz24; US$590M). Including the consent payment offered (US$4.18) the NPV of the offer is US$80 with 10% yield (+27% vs 63 USD original offer). Despite the improvement, the bondholders group (with a 40%+ position) rejected the offer.

After several months without activity in international markets, two of the biggest Argentinian companies announced liability management operations: i) YPF exchange offer for US$1bn 8.5% Notes due 2021 for 92.5 of new 8.5% 2025 bonds plus US$12.5 in cash for US$100 of the old notes; ii) Telecom Argentina plans to issue up to US$520M in new 2025 8.5%, which can be subscribed with the bonds that mature in 2021 (US$70 New notes + US$32 in cash for each US$100 nominal value).

Inflation accelerating slightly; Activity not bottoming out yet

The CPI rose 2.2% in June (vs 1.5% May), and accumulated a rise of 42.8% in the last 12 months (+43.4% YoY). Seasonal prices increased most (+4.8%), followed by Core prices (+2.3%) and adjusted by only +0.7% (half the CPI), reflecting the freeze on most tariffs. Food items registered a 1% MoM rise, well below the general index.

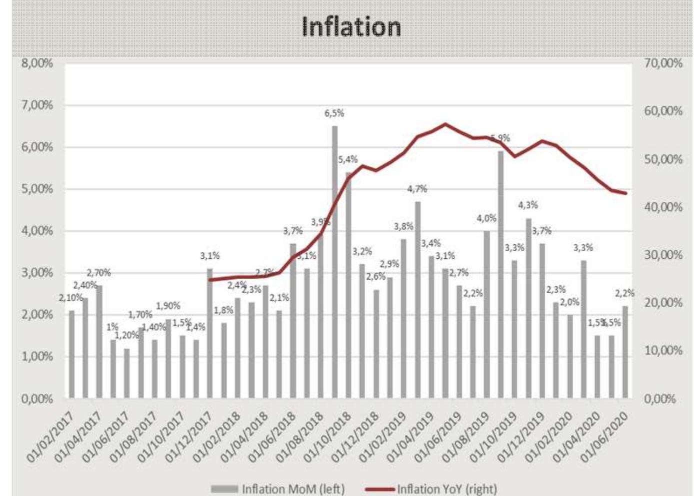
Activity in April declined 17.5% MoM (-10.3% in March) and contracted 26.4% YoY (-11.4% in March) according to the Monthly estimator. This is the first data point with a complete lockdown.

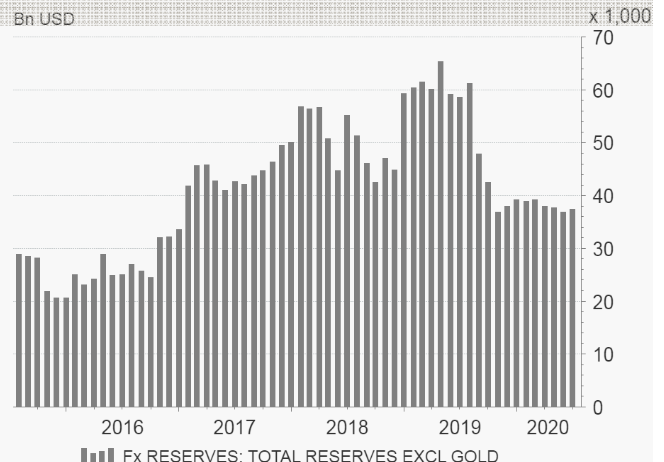
The central bank is carrying a crawling peg depreciation above inflation to avoid the widening of the exchange gap but at the same time doing this at a moderate pace to prevent a surge in inflation. The gap between the official FX rate (71.47) and the BCS (117.63) & black market FX (128) is 64.5% and 79% respectively.

Financial market outlook

Bonds – 10YGov USD: NEUTRAL
FX – USD-ARS: NEGATIVE (2020 year-end target 95)

Source: Refinitiv Datastream / ANDBANK





Source: Refinitiv DatastreamThomson Reuters Datastream / ANDBANK

GLOBAL EQUITY INDICES

Fundamental assessment

Index	Projected EPS Andbank 2020	Projected EPS Andbank 2021	Projected EPS Andbank Fw 12m	Projected EPS Growth Andbank 2020	Projected EPS Growth Andbank 2021	Current PE fw EPS 2020	Current PE trailing EPS 2019	Projected PE EPS nxt 12m	INDEX CURRENT PRICE	Current Fair Value (EPS 12 month fw)	2020 E[Perf] to Fair Value	Recomm	2020 Exit Point	Margin	E[Perf] to Exit point
USA S&P 500	132	165	148	-20,0%	25,00%	24,75	19,80	20,00	3.258	2.962	-9,1%	MW	3.407	1,15	4,6%
Europe - Stoxx Europe 600	19,5	24	22	-25,0%	25,00%	18,59	13,94	15,50	362	340	-6,2%	MW/OW	408	1,2	12,6%
Euro Zone - Euro Stoxx	18,9	24	21	-25,0%	25,00%	18,76	14,07	15,50	355	330	-7,1%	MW/OW	395	1,2	11,5%
Spain IBEX 35	498	697	597	-30,0%	40,00%	14,17	9,92	13,00	7.050	7.764	10,1%	OW	8.541	1,1	21,1%
Mexico IPC GRAL	2.320	2.785	2.553	-18,0%	20,00%	16,26	13,33	14,25	37.721	36.374	-3,6%	MW	40.011	1,1	6,1%
Brazil BOVESPA	5.984	7.181	6.582	-18,0%	20,00%	17,65	14,47	15,50	105.605	102.027	-3,4%	MW/OW	112.230	1,1	6,3%
Japan NIKKEI 225	1.063	1.276	1.169	-20,0%	20,00%	21,02	16,81	17,00	22.339	19.878	-11,0%	MW/UW	23.854	1,2	6,8%
China SSE Comp.	226	249	237	-10,0%	10,00%	14,53	13,08	12,50	3.287	2.968	-9,7%	UW	3.265	1,1	-0,7%
China Shenzhen Comp	75,1	83	79	-10,0%	10,00%	29,64	26,68	24,00	2.227	1.894	-15,0%	UW	2.083	1,1	-6,5%
India SENSEX	1.576	1.813	1.695	-15,0%	15,00%	23,94	20,35	20,00	37.736	33.891	-10,2%	OW	40.669	1,2	7,8%
Vietnam VN Index	53,6	62	58	-10,0%	15,00%	14,96	13,46	15,00	801	864	7,8%	OW	1.037	1,2	29,4%
MSCI EM ASIA	35,4	41	38	-10,0%	15,00%	16,70	15,03	14,00	592	533	-9,9%	OW	640	1,2	8,1%

ANDBANK ESTIMATES

POSITIONING, FLOW & SENTIMENT ANALYSIS

Outlook: Overall assessment still constructive

Andbank's Assessment: +1.5 (in a –7/+7 range)

Aggregate (MW-OW bias): Our overall assessment remains mildly positive.

Market Positioning (MW bias): Asset allocation in equities is neutral and we are keeping our MW review. The Put-Call ratio also indicates also that investors are not hedging their portfolios. Finally, the skew in positive territory reflects that a fear of a more violent downside movement is still present.

Flow Analysis (MW-OW bias): Sentiment from investors is still negative and our contrarian reading therefore remains positive.

Surveys & Sentiment Analysis (MW-OW bias): Sentiment from investors is still negative; our contrarian reading remains positive.

TECHNICAL ANALYSIS

Trending Scenario. Supports & Resistances

	Name	Ticker Reuters	View 1 month	Principal Support 2020	Principal Resistance 2020	Support 1 month	Resistance 1 month	Target (TA) 2020	@	Return to Target (TA)
INDICES	Euro Stoxx Index	.STOXXE	Lateral	252,89	443,29	335,39	391,00	443,00	366,27	20,95%
	Euro Stoxx 600	.STOXX	Lateral	268,57	433,90	344,91	403,72	441,75	372,71	18,52%
	Ibex	.IBEX	Lateral	5.814,50	10.100,00	7.062,90	7.992,70	8.375,60	7.440,40	12,57%
	S&P	.SPX	Lateral	2.191,86	3.393,52	2.965,66	3.337,75	3.393,52	3.224,73	5,23%
	Japón	.N225E	Lateral	16.358,19	24.448,00	21.529,83	24.116,00	24.116,00	22.717,48	6,16%
	China	.SZSC	Lateral bullish	1.458,00	2.000,00	1.931,02	2.377,00	2.441,38	2.216,70	10,14%
	India	.BSESN	Lateral	24.833,00	42.273,00	33.887,25	40.066,31	42.273,87	37.020,14	14,19%
	Brasil	.BVSP	Lateral	57.600,00	119.593,00	90.147,92	106.650,00	119.593,10	102.888,25	16,24%
	México	.MXX	Lateral	30.000,00	45.955,00	35.277,54	40.030,95	41.388,00	36.327,84	13,93%
OTROS	Oil West Texas	WTCLc1	Lateral	10,37	51,00	34,37	42,27	50,00	40,56	23,27%
	Gold	XAU=	Lateral bullish	1.445,18	1.920,00	1.742,84	1.920,30	1.920,00	1.808,90	6,14%
	Treasury 10Y USA	US10YT=RR	Lateral	0,1289%	1,3210%	0,5430%	0,7430%	0,8658%	0,6225%	39,08%

Bullish ->+3.5%; Lateral bullish -> (+1.5% , +3.5%); Lateral -> (−1.5, + 1.5%); Lateral bearish -> (−3.5%, −1.5%); Bearish <-3.5%

FI **FIXED INCOME - GOVERNMENTS**

DEVELOPED MARKETS

Fundamental assessment

US Treasury: Floor 1.47%. Fair value 2.32%. Ceiling 2.5%

Swap spread: The swap spread was fixed at -1.1bp. For this spread to normalize at +3bp, with the 10Y swap rate anchored in the 1.5% area (our LT inflation expectation), the 10Y UST yield would have to move towards 1.47%.

Slope: The slope of the US yield curve (10-year minus 2-year bond yield) was fixed at 43bp. With the short-end normalizing towards 1%, to reach the long-term average slope (of 132bp), the 10Y UST yield would have to move to 2.32%.

Real yield: A good entry point in the 10Y UST would be when the real yield hits 1%. Given our long-term CPI forecast of 1.5%, the UST yield would have to rise to 2.5% to become a "BUY".

GER Bund: Floor 0.30%. Fair value 1.11%. Ceiling 1.5%

Swap spread: The swap spread was fixed at 25bp. For the swap spread to normalize at 20bp, with the swap rate anchored in the 0.5% area, the Bund yield would have to move towards 0.30% (entry point).

Slope: The slope of the EUR curve (10-year minus 2-year bond yield) was fixed at 24bp. If the short-end normalizes at 0%, to reach the 10Y average yield curve slope (111bp), the Bund yield would have to move to 1.11%.

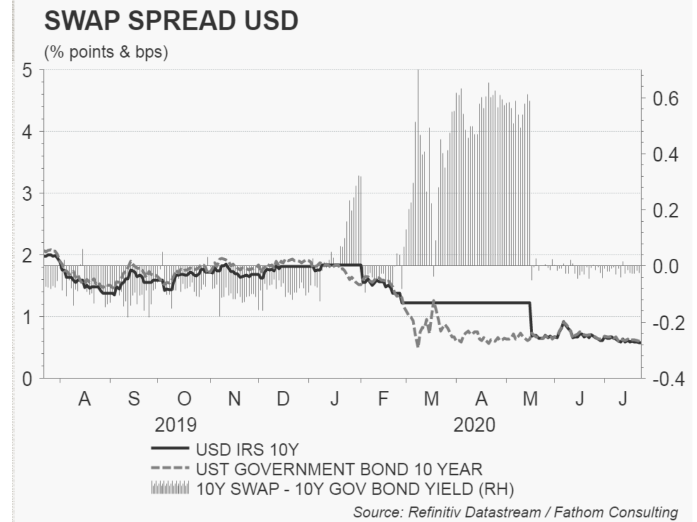
Real yield: A good entry point in the German Bund would be when the real yield hits 0.5%. Given our CPI mid-term forecast of 1%, the Bund yield would have to rise to 1.5% to become a "BUY".

UK Gilt: Floor 1.4%. Fair value 2.3%. Ceiling 2.5%

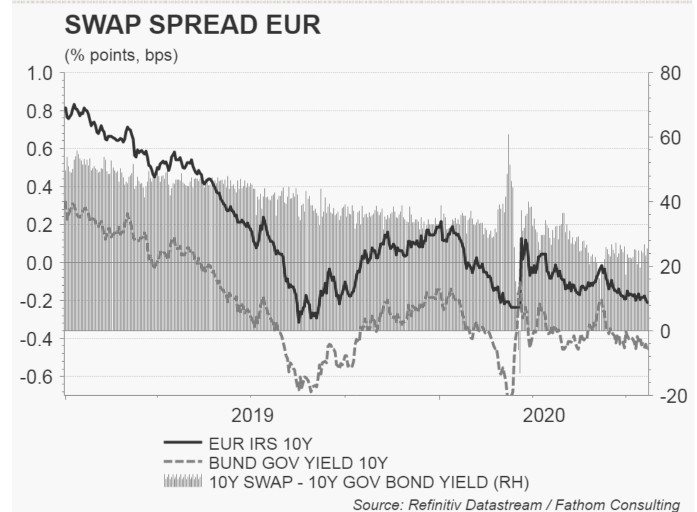
Swap spread: The swap spread was fixed at 20bp. For the swap spread to normalize at 11bp, with the swap rate anchored in the 1.5% area, the 10Y UK Gilt would have to shift to 1.4%.

Slope: With the 2Y bond normalized at 1%, to reach the average slope at 1.3%, the 10Y Gilt would have to move to 2.30%.

Real yield: Given our CPI mid-term forecast of 1.5%, the Gilt yield would have to rise to 2% to become a "BUY".



Source: Refinitiv Datastream / Fathom Consulting



Source: Refinitiv Datastream / Fathom Consulting

EUROPEAN PERIPHERAL BONDS

Tactical targets – 10Y yields

Spanish bono: Target yield at 0.6%
Italian bond BTPI: Target yield at 1.4%
Portuguese Gov bond: Target yield at 0.6%
Ireland Gov bond: Target yield at 0.3%
Greek Gov bond: Target yield at 2.0%

EMERGING MARKET BONDS

Fundamental targets

To date, our rule of thumb for EM bonds has been "buy" when the following two conditions are met: 1) The US Treasury real yield is at or above 1%; and 2) EM bond real yields are 1.5% above the UST real yield.
Assuming that the first condition is met, we should only buy those EM bonds offering a real yield of 2.50% or more. The markets (and government bonds) that meet such requirements are shaded gray.

		10 Year Yield Nominal	CPI (y/y) 3 month Mov Avg	10 Year Yield Real	Projected change in Yield	Target Yield
EM ASIA	Indonesia	6,76%	2,08%	4,68%	-1,00%	5,76%
	India	5,82%	6,59%	-0,76%	1,00%	6,82%
	Philippines	2,82%	2,30%	0,52%	0,00%	2,82%
	China	2,93%	2,44%	0,49%	0,00%	2,93%
	Malaysia	2,61%	-2,52%	5,12%	-1,00%	1,61%
	Thailand	1,18%	-2,54%	3,72%	-1,00%	0,18%
	Singapore	0,82%	-0,72%	1,54%	-0,50%	0,32%
	South Korea	1,13%	-0,20%	1,33%	-0,50%	0,63%
	Taiwan	0,30%	-0,97%	1,26%	-0,50%	-0,21%
EME	Turkey	12,66%	12,01%	0,65%	0,00%	12,66%
	Russian Fed	5,95%	3,10%	2,85%	-0,75%	5,20%
LATAM	Brazil	6,49%	2,20%	4,29%	-1,00%	5,49%
	Mexico	5,66%	3,02%	2,64%	-0,75%	4,91%
	Colombia	5,29%	2,49%	2,80%	-0,75%	4,54%
	Peru	4,47%	1,66%	2,81%	-0,75%	3,72%

ENERGY – OIL

Fundamental view (WTI): Target range USD35-45bbl.

Buy < USD35; Sell >45

Short-term drivers

(Price Negative) – Resurgent coronavirus could derail recovery in global fuel demand: While fuel consumption and oil prices had recovered some ground from spring lows, that recovery is stalling amid a surge of coronavirus infections in the US and other major economies like Brazil and India. US gasoline demand fell for two straight weeks through July 11, the first time that had happened since lockdowns began in March. India now has more than 1M Covid-19 cases and Brazil has ~2M, while Australia, Spain, China and the UK have also enforced lockdowns in recent weeks to control outbreaks.

(Price Positive) – Russia's Novak sees significant demand improvement in August: Russian Energy Minister Novak said he expects global oil demand to recover significantly in August and improve to 10% below pre-pandemic levels (vs the 25% drop seen in April). The OPEC+ producer group had been cutting 9.7M bpd through July (or ~10% of global supply) but will taper those cuts to 7.7M bpd beginning in August.

(Price Neutral-Negative) – OPEC+ committee not expected to recommend extending record cuts into August, but producer group believes output hikes will be "barely felt": OPEC+'s Joint Ministerial Monitoring Committee (JMMC) is set to meet virtually, though multiple sources have said no recommendations have been made to continue July's 9.7M bpd cuts into August (but instead taper down to 7.7M bpd). The OPEC+ cartel believes that despite its plans to ease record-high production cuts in August, the extra production should not hurt oil's price recovery, with Saudi Energy Minister Abdulaziz saying the impact will be "barely felt" and that the world's growing oil demand will consume the extra barrels. The article notes that the market is not expecting a full 2M barrels in extra output given that pact laggards such as Nigeria and Iraq have said they would over-comply in August to make up for above-target production in May and June. It adds that fully offsetting the shortcomings of all the delinquent nations would require 842K bpd in extra cuts in August and September. Platts also notes the group said in a communiqué that while there could be some new or re-imposed Covid-19 lockdowns, the recovery signs are clear in both the physical and futures markets.

(Price Positive) – EIA sees US shale output dipping in August: The last Drilling Productivity Report from the US Energy Information Administration forecasts that total US shale-oil production will drop by 56K bpd to 7.49M bpd, in what would be the lowest overall level in two years. Output from the Permian basin is expected to fall for the fifth straight month, while the Bakken region is the only area expected to see increases.

(Price Positive) – Dakota Access can stay open during legal fight: A US appeals court ruled yesterday that the 570K bpd Dakota Access pipeline, ordered shut and emptied by a federal district court on July 6, can continue to operate while the court battle continues. The operator Energy Transfer (ET) has said it would cost ~$27B to drain the pipeline, and that it stands to lose as much as $1.4B if the line is shut for all of 2021.

(Price Negative) – **CFTC looking at commodity funds**: The US Commodity Futures Trading Commission (CTFC) is examining disclosures by managers of commodity funds popular with retail investors, voicing concerns that purchasers have not been provided with up-to-date information about underlying investments and strategies. It adds that the CTFC is preparing a report about April's oil-price crash, and the agency is looking at the timing of certain April trades (though the CTFC cautions supply and demand factors could explain the steep price declines).

(Price Positive) – Trump administration scaling back environmental reviews: President Trump is expected to announce a first-in-decades rewrite of the rules governing how agencies scrutinize the environmental impact of development projects. The new rules may limit the scope of agency reviews as well as what projects warrant that scrutiny. While the White House cannot change the underlying law, it can alter the way that statute is implemented by putting deadlines on agency reviews, including ruling out analysis for non-federal projects with minimal federal funding or involvement.

Long-term drivers

(Price Negative) – Alternative energies picking up the baton: Conventional producers must bear in mind that the value of their reserves is dictated by the amount of time they can pump before alternative energies render oil obsolete. In order to push back this deadline as far as possible, it is in producers' interest to keep oil prices low for as long as possible (keeping the opportunity cost of alternative energy sources as high as possible).

(Price Negative) – Growing environmental problems will gradually tighten legislation over production levels. The value of producers' reserves depends on the amount of time they can pump at current levels before tougher environment-inspired regulations come in. With growing environmental problems, which will likely continue to put a lot of pressure on the market for fossil fuels over the coming decades, OPEC's most serious risk is of sitting on a big chunk of "stranded reserves" that it can no longer extract and sell. Producers therefore have a powerful incentive to monetize as much of their reserves as soon as they can.

(Price Negative) – Are OPEC producers able to structurally fix prices? While it is true the agreement between the Saudis and Russia to strangle the global energy market has worked well in achieving a considerable increase in the price of oil, this has been at the cost of a loss of market share, meaning that OPEC producers are no longer able to easily fix prices without bearing costs. Back in the 1970s and the early 2000s, the exporters cartel agreed to cut output and the approach worked well, as the principal competition was among conventional oil producers (in particular between OPEC and non-OPEC producers). Today's biggest threat to any conventional oil producer comes from non-conventional producers and alternative energy sources. Energy cuts from conventional oil should therefore easily be offset (in theory) by a rapid increase in shale oil production.

PRECIOUS METALS - GOLD

Fundamental price for gold at US$1,800 – US$2,000/oz.

Positive drivers for gold

Gold is not a crowded trade: In spite of a 55% surge over the past two years, this rally has garnered limited headlines, unlike the tech sector. Accordingly, the total market of the precious metal and mining sector is small enough to keep running without hitting the big numbers problems. The sector's size is only US$550bn (roughly what Amazon has added to its market value in one year).

Gold bull markets usually feeds on their own momentum for quite a while: The 1976-80 rally ended when US short rates were jacked up to break inflation causing a rise in the USD. The 1985-88 rally ended when Germany pulled out of the Accord Plaza deal and US rates started to rise, and with rates, also the US Dollar. In the 2001-11 period, president George W. Bush's "guns & butter" policies spurred a rise in EMs, that became a new gold buyers. This ended in 2011 when the USD started to strengthen. Looking at this history, when gold bull markets get going, they usually feed on their own momentum for quite a while, and only end when facing higher nominal rates, a stronger USD or a rise in real rates. These are the 3 threats to the unfolding gold bull market. **1) Higher nominal rates:** It is almost impossible to find an OECD central banker even thinking of raising interest rates in his or her lifetime. **2) Stronger USD:** The US current account balance has been gradually improving, leading to a shortage of dollars and a rise in its price. We do not foresee a jump in this current account balance that will boost the USD again. Rather, the balance (deficit) could remain stable at around 2% of GDP, and keep the USD well supported but stable, far from a strong rebound that could end gold's bull market. **3) A rise in real rates:** So if nominal rates are not going to rise, the only way OECD countries can experience surging real rates is through an already low inflation rate collapsing more. But how? Collapse in energy or real estate prices? Alternatively, a collapse in the Renminbi? There are few signs of such shocks unfolding permanently. With this in mind, it seems that a surge in real rates is not an immediate threat.

About momentum: Gold bull markets may build up over multi-year periods. In the 2001-2011 period, it was the new wealth being created in EMs, with a strong affinity for gold, that pushed gold prices higher. In contrast, in the 2011-2020 decade, most of the world's wealth has been created in campuses on the US-West coast, by people with scant interest in this "relic" and with EM growth having been much more moderate. Despite this, the gold price has ripped higher and is showing strong momentum. Imagine now if EMs thrive again, led by Asia… what a tailwind that would be for gold.

Gold as the new anti-fragile asset: Gold, like the US Treasury bond, is an anti-fragile asset. Investors should therefore always carry out the exercise of deciding which anti-fragile asset should be kept in the portfolio to hedge against demand or supply shocks or inflation shocks. The answer will have a lot to do with the perception of which of the two anti-fragile assets is likely to perform better in the future. This, in turn, will depend on the relative supply of the two anti-fragile assets. The one with the lower relative supply will be the one that will perform better and will better display its quality as an anti-fragile asset in the face of a shock. In this respect, we are very clear that the supply of US Treasury bonds will be almost unlimited, whereas the supply of gold will remain very limited over the next decade.

Negative yields still make gold attractive: The disadvantage of gold compared to fixed income instruments (gold does not offer a coupon) is now neutralized, with negative yields in a large number of global bonds (>US$13tn of face value is yielding negative rates).

Relative share of gold: The total value of gold in the world is circa US$6.9tn, a fairly small share (3.2%) of the total global cash market (212tn). The daily volume traded on the LBMA and other gold marketplaces is around US$173bn (just 0.08% of the total in the financial markets).

Gold to the S&P500: This ratio stands at 0.56x, just shy of the LT average of 0.62x. Given our estimated fair value price for the S&P of US$2,962 the price of gold must approach US$1,836 for this ratio to remain near its LT average.

Negative drivers for gold

Gold is 1 standard deviation above its 200-day moving average price.

Gold in real terms: In real terms, the price of gold (calculated as the current nominal price divided by the US Implicit Price Deflator-Domestic as a proxy for the global deflator) is US$1,600. Therefore in real terms, gold continues to trade well above its 20-year average of US$956. Given the global deflator (now at 1.13543), for the gold price to stay near its historical average in real terms, the nominal price (or equilibrium price) must remain near US$1,085.

Gold to Silver (Preference for store of value over productive assets). This ratio is at 91.94 and still remains well above its 20-year average of 65.64x, suggesting that gold is expensive (at least relative to silver). For this ratio to reach its long-term average, assuming that silver is better priced than gold (which is highly probable), then the gold price should go to US$1,297/oz.

Gold to Oil: This ratio is at 44.53, still well above its 16-year average of 16.6x. Considering our fundamental long-term target for oil of US$40 pb (our central target for the long term) and that the utility of oil relative to gold will remain unchanged, the price of gold must approach US$664 for this ratio to remain near its LT average.

EXCHANGE RATES

Flow analysis & Fundamental targets

EUR-USD: Target 1.10
USD-JPY: Target 107; **EUR-JPY**: Target 117.71
GBP-USD: Target 1.32; **EUR-GBP**: Target 0.83
USD-CHF: Target 0.97; **EUR-CHF:** Target 1.07
USD-MXN: Target 23.5; **EUR-MXN:** Target 25.85
USD-BRL: Target 5.50; **EUR-BRL:** Target 6.05
USD-ARS: Target 90
USD-INR: Target 74
CNY: Target 6.90
RUB: NEUTRAL
AUD: NEUTRAL
CAD: NEUTRAL

Currency	Mkt Value of Net positions in the currency (Bn $)	Change vs last month (Bn $)	3-yr Max (Bn $)	3-yr Min (Bn $)	3-yr Avg (Bn $)	Current Z-score 3-yr
USD vs All	-19,37	-3,10	32,1	-28,2	0,9	-1,08
USD vs G10	-18,98	-3,41	32,7	-25,4	2,1	-1,18
EM	0,40	-0,31	5,2	-0,8	1,7	-0,85
EUR	18,02	1,53	23,4	-15,5	7,9	0,97
JPY	2,26	-0,31	4,0	-15,0	-6,3	1,45
GBP	-1,20	0,06	4,3	-6,5	-1,1	-0,05
CHF	0,99	0,78	1,2	-6,0	-1,9	1,41
BRL	-0,21	0,03	0,7	-0,9	-0,2	0,00
MXN	0,22	-0,28	4,6	-0,5	1,5	-0,99
RUB	0,39	-0,06	1,2	-0,3	0,4	-0,16
AUD	-0,02	0,44	6,1	-5,2	-0,7	0,22
CAD	-1,24	0,64	6,1	-5,0	0,1	-0,47

Positive
Neutral-Positive
Neutral-Negative
Negative

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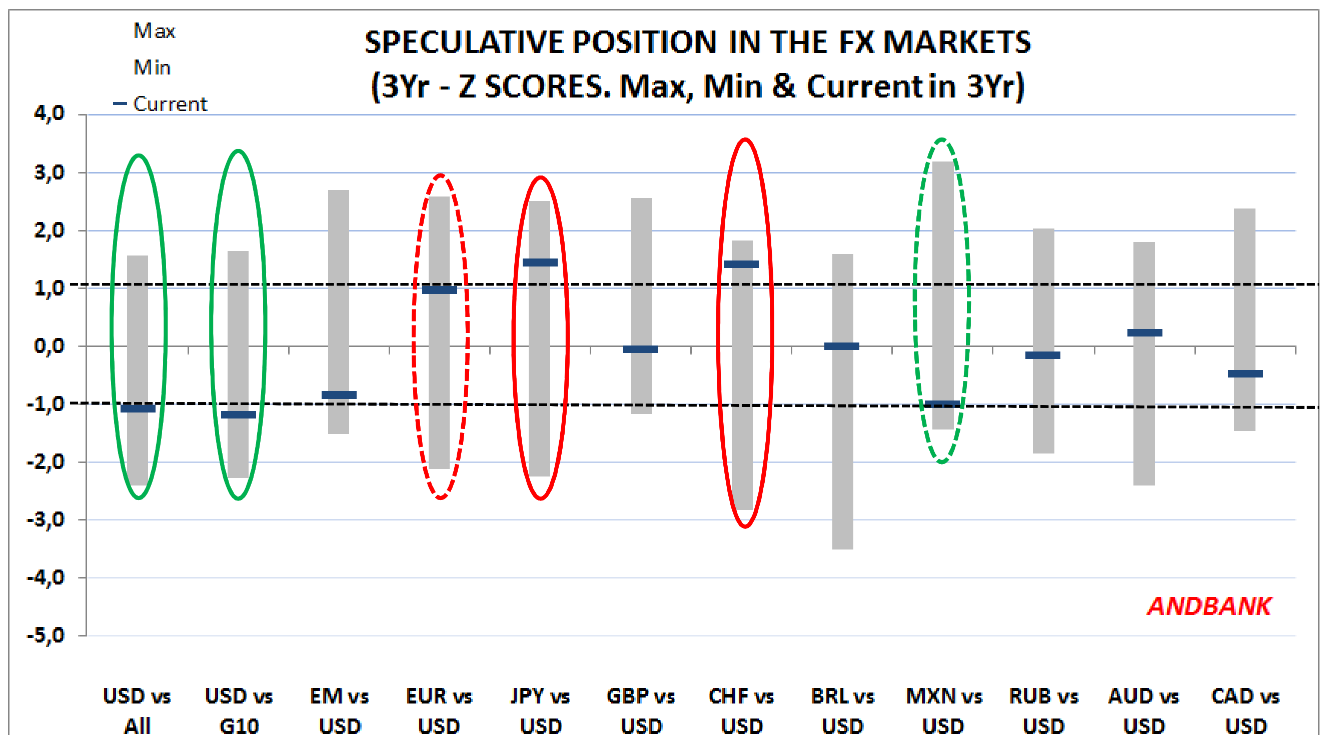

The currencies we technically favor are circled in green

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SUMMARY TABLE OF EXPECTED RETURNS

Asset Class	Indices	Performance Last month	Performance YTD	Current Price	Fair Value EPS 12m fw	Expected Performance to Fair Value 2020
Equity	USA - S&P 500	5,1%	0,9%	3.258	2.962	-9,1%
	Europe - Stoxx Europe 600	0,6%	-11,6%	363	340	-6,2%
	Euro Zone - Euro Stoxx	0,5%	-10,6%	355	330	-7,1%
	SPAIN - IBEX 35	-2,4%	-24,5%	7.055	7.764	10,1%
	MEXICO - MXSE IPC	0,0%	-13,4%	37.721	36.374	-3,6%
	BRAZIL - BOVESPA	11,1%	-8,7%	105.605	102.027	-3,4%
	JAPAN - NIKKEI 225	-3,5%	-5,6%	21.507	19.878	-7,6%
	CHINA - SHANGHAI COMPOSITE	10,1%	8,0%	3.287	2.968	-9,7%
	CHINA - SHENZEN COMPOSITE	12,7%	29,3%	2.227	1.894	-15,0%
	INDIA - SENSEX	8,1%	-7,7%	37.736	33.891	-10,2%
	VIETNAM - VN Index	-2,9%	-17,7%	801	864	7,8%
	MSCI EM ASIA (in USD)	9,3%	4,5%	592	533	-9,9%
Fixed Income Core countries	US Treasury 10 year Govie	0,8%	12,0%	0,56	1,20	-4,9%
	UK 10 year Gilt	0,6%	6,2%	0,10	0,80	-5,6%
	German 10 year BUND	0,5%	2,5%	-0,52	-0,20	-2,8%
	Japanese 10 year Govie	0,0%	-0,3%	0,01	0,00	0,1%
Fixed Income Peripheral	Spain - 10yr Gov bond	1,1%	1,3%	0,33	0,60	-2,0%
	Italy - 10yr Gov bond	2,2%	3,4%	1,04	1,40	-2,4%
	Portugal - 10yr Gov bond	1,1%	1,0%	0,32	0,60	-2,1%
	Ireland - 10yr Gov bond	1,0%	1,8%	-0,13	0,30	-3,5%
	Greece - 10yr Gov bond	1,2%	3,9%	1,02	2,05	-7,8%
Fixed Income Credit	Credit EUR IG-Itraxx Europe	0,2%	-0,4%	59,94	70	-0,2%
	Credit EUR HY-Itraxx Xover	1,0%	-4,0%	363,25	400	0,2%
	Credit USD IG - CDX IG	0,2%	0,6%	71,80	70	0,5%
	Credit USD HY - CDX HY	2,3%	-2,5%	454,24	450	2,2%
Fixed Income EM Europe (Loc)	Turkey - 10yr Gov bond (local)	-9,1%	0,9%	12,66	11,75	12,6%
	Russia - 10yr Gov bond (local)	0,4%	5,7%	5,95	5,00	10,1%
Fixed Income Asia (Local curncy)	Indonesia - 10yr Gov bond (local)	3,8%	6,0%	6,76	6,00	8,9%
	India - 10yr Gov bond (local)	0,9%	9,6%	5,82	6,80	-5,4%
	Philippines - 10yr Gov bond (local)	-0,1%	15,4%	2,82	3,00	-0,2%
	China - 10yr Gov bond (local)	-0,4%	3,4%	2,93	2,75	2,7%
	Malaysia - 10yr Gov bond (local)	3,6%	7,5%	2,61	2,00	5,9%
	Thailand - 10yr Gov bond (local)	-0,1%	2,8%	1,18	0,25	7,9%
	Singapore - 10yr Gov bond (local)	0,5%	8,2%	0,82	0,40	3,7%
	Rep. Korea - 10yr G. bond (local)	0,7%	4,4%	1,13	0,75	3,5%
	Taiwan - 10yr Gov bond (local)	0,2%	2,9%	0,30	0,00	2,5%
Fixed Income Latam	Mexico - 10yr Govie (Loc)	1,5%	13,4%	5,66	6,20	-1,9%
	Mexico - 10yr Govie (USD)	4,3%	3,3%	3,16	3,70	-3,0%
	Brazil - 10yr Govie (Loc)	2,1%	6,4%	6,49	8,20	-10,9%
	Brazil - 10yr Govie (USD)	4,1%	0,9%	4,36	4,20	3,1%
Commodities	Oil (WTI)	4,2%	-33,0%	40,9	40,00	-2,2%
	GOLD	9,8%	28,9%	1.955,9	1.600	-18,2%
Fx	EURUSD (price of 1 EUR)	4,7%	4,9%	1,176	1,100	-6,4%
	GBPUSD (price of 1 GBP)	4,7%	-2,1%	1,30	1,32	1,6%
	EURGBP (price of 1 EUR)	-0,1%	7,0%	0,91	0,83	-7,9%
	USDCHF (price of 1 USD)	-3,5%	-5,6%	0,91	0,97	6,1%
	EURCHF (price of 1 EUR)	1,0%	-1,0%	1,07	1,07	-0,7%
	USDJPY (price of 1 USD)	-2,7%	-3,3%	105,05	107,00	1,9%
	EURJPY (price of 1 EUR)	1,9%	1,4%	123,51	117,70	-4,7%
	USDMXN (price of 1 USD)	-3,8%	16,9%	22,12	23,50	6,2%
	EURMXN (price of 1 EUR)	0,2%	22,6%	25,98	25,85	-0,5%
	USDBRL (price of 1 USD)	-5,4%	28,6%	5,17	5,50	6,4%
	EURBRL (price of 1 EUR)	-1,0%	34,9%	6,08	6,05	-0,5%
	USDARS (price of 1 USD)	2,7%	20,6%	72,19	90,0	24,7%
	USDINR (price of 1 USD)	-1,0%	4,9%	74,82	74,00	-1,1%
	CNY (price of 1 USD)	-0,9%	0,6%	7,00	6,90	-1,5%

** For Fixed Income instruments, the expected performance refers to a 12 month period*

UPWARD REVISION DOWNWARD REVISION

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