Weekly Market Summary

July 17th, 2020

Summer Doldrums in 2020?! I Wouldn't Personally Bet on That!!

Fadi Nasser - Deputy Chief Investment & Treasury Officer

Latest Update on Coronavirus: Confirmed cases last at 13.98 million (from 12.42 million last week), with the death toll from the pandemic close to the 600,000 mark (593,457 last versus 558,092 deaths the week before). Hong Kong's new outbreak has surpassed the scale of its previous wave of infections in a warning that the worst of the pandemic is yet to come. In Spain, Barcelona's government urged residents not to leave their home unless necessary as countries around the world grapple with a fresh surge in infections. Earlier today, India became the third country to record more than a million cases while Brazil surpassed two million infections (confirmed deaths for both countries stand at 25,664 and 76,822 respectively). China has locked down housing compounds across Xinjiang's capital, Urumqi (with a population estimated at 4.37 million), amid fears of another outbreak immediately after the end of a recent spike in cases in Beijing.

Financial assets' movements in past days have suffered from summer doldrums, especially that news flows have remained light and markets overall stayed quiet. After all, money managers, brokers and traders are human beings (though a very greedy species!), and on warm, sunny summer days, many would rather plan their holidays to catch up with family and friends (almost impossible nowadays ☹). That in turn means investment professionals are less likely to buy and sell stocks, bonds, currencies and commodities, which could dampen volatility in the market place (though not a guaranteed outcome as reduced volumes could sometimes result in greater volatility with transactions completed having a bigger impact on the price of financial instruments). For Wall Street dealers, the summer doldrums extend throughout August and officially end after Labor Day (first Monday of September), when hedge fund managers and mutual fund gurus head back to work.

In the meantime. bond vigilantes are acting a lot less vigilant these days! There was a time, following the inflation crisis of the early 1980s, when the bond market, regardless of the Federal Reserve's policy, worked to keep a cap on bond prices (lower prices & higher yields) just to be sure the economy did not get too steamy. Whenever there were signs that the pace of growth was picking up, the so-called vigilantes would rush to sell, driving interest rates higher and acting as a brake on the economy. But if this July is any indication – not to mention the price action over the past 3 months - a new era may be upon us! The bond market continues to soar despite improving economic data and the return of substantial budget deficits in the US (at 18% of GDP in Fiscal Year 2020, the federal deficit is almost twice as large than at the worst of the Great Recession in 2009!). The yield on the benchmark 30-year US bond has plummeted this week to a low of 1.28% from the 2.40% level witnessed at the beginning of the year. More importantly, the average rate for a 30-year fixed loan fell yesterday to 2.98%, hitting a record low for the third straight week and the seventh time since the coronavirus outbreak began roiling financial markets. Low yields have fueled demand for homes, propping up prices and helping the housing market hold up better than expected amid the economic fallout from the pandemic. "*It's not a silver bullet for the economic woes we're experiencing, but it's night-and-day different than what the housing market was looking like during the last recession*," said Ralph McLaughlin, chief economist for Haus, a co-investment platform for homebuyers.

Behind the recent rally in fixed-income prices is a conviction among bond investors and traders that the Federal Reserve would not risk raising the US benchmark interest rate from its current target range near zero too fast (nor too far) until it is confident the economy has weathered recent events, as well as ensuring that growth/inflation are actually showing signs of holding up and are on track to achieve maximum employment and price stability goals (in other words, till infinity and beyond! 😊) Not to mention that US Fed officials continue pondering how to best update their public guidance on the

likely need to deploy a yield-curve control strategy over the short to medium term. "*Right now, I actually think that the guidance we do have in there - which is maybe more descriptive than formal forward guidance -- is serving us well*," New York Fed President John Williams said yesterday during an interview with Yahoo Finance. "*So, we do have some time to think about how we should evolve that guidance as we go forward*."

Overall, of course, that is good news for bonds and bondholders! (and in turn for equity investors, as economic theory and historical data show that low rates bolster stock prices). But it portends more volatility, and, somewhere down the road, perhaps some brutally painful losses. After all, recently released US data – including June figures for Non-Farm Payrolls, ISM Manufacturing and Non-Manufacturing, Retail Sales, Consumer Price Inflation and Industrial Production - has uniformly and largely surprised to the upside (in normal times that would have triggered a bond sell-off!). Yet, with a proxy of global money supply swelling above $87 trillion (Bloomberg tracking) - almost $6.5 trillion up from the beginning of the year and twice the average annual increase seen over the past decade - extra liquidity is splashing around to be deployed in various asset classes, including G-7 government bond (10-year UK Gilt yields traded to a record low of 0.14% this week, well below the 48 bps witnessed in late June 2016 following the UK vote to quit the European Union!)

Below is a coverage of other major stories that have shaped markets this week:

- ***OPEC+ Increases Oil Output:*** OPEC and its allies have decided to restore some oil supplies as planned next month! The 23-nation collation led by Riyadh and Moscow will taper the curbs to 7.7 million barrels a day in August from 9.6 million currently, Saudi Energy Minister Price Abdulaziz bin Salman and his Russian counterpart Alexander Novak said on Wednesday. That supply increase comes at a time fuel consumption is picking up worldwide with the lifting of lockdowns around the world and should be offset somehow as collation members that did not fulfil their commitments to cut output in May and June (such as Iraq and Nigeria) make up for it with extra reductions in August and September.

- ***Vaccines Remain the Next Pivot for Markets!*** Since February, there have been ongoing discussions as to whether vaccines for the coronavirus would arrive in 2020 or 2021. Dr. Anthony Fauci, director of the National Institute of Allergy and Infectious Diseases, had been initially skeptical of the 2020 projection, arguing in early march that "*it will take at least a year to a year and a half to have a vaccine we can use.*" Yet, as a result of record public funding and support for COVID-19 vaccine research, Fauci has now embraced a more optimistic assessment (Hurrah!! We shall now breathe a huge sigh of relief and buy more MRNA shares! 😊) This week, Moderna published a lengthy report detailing results of its Phase 1 trial, which showed the vaccine induced immune responses (neutralizing antibodies) to the virus that causes Covid-19 in all trial participants.

- ***ECB Won't Be Constrained in Fight Against Virus***: European Central Bank President Christine Lagarde said she would not let monetary policy be constrained as she fights to support the Euro area's economic recovery from the Coronavirus crisis. Lagarde added that the central bank currently expects to spend the full amount of its pandemic bond-buying program, in apparent contrast to some policy makers, who recently suggested that going that far may not be necessary. The ECB boss also insisted that officials will continue steering purchases toward the countries that most need support during the pandemic, such as Italy. That is an issue which is already causing consternation among some policy makers who fret that the central bank might be seen as breaching laws banning it from directly financing governments.

- ***Morgan Stanley Joins Wall Street Gold Rush on Record Profit:*** At a time surveys continue to reveal the extent businesses hurt from Covid-19, Morgan Stanley just wrapped a week of wins for Wall Street trading desks, capitalizing ("*knowingly*"*?*) on the Federal Reserve's extraordinary rescue measures with record profit. The gains bring the overall quarterly trading haul total for the five biggest U.S. investment banks (Goldman Sachs, Morgan Stanley, JP Morgan Chase, BoA and Citigroup) to a whopping $33 billion, a windfall that should help all of them survive the brunt of the coronavirus pandemic with profits intact. *A big thank you goes to the US Federal Reserve for supporting the trading activities of too-big-to-fail US financial institutions!* 😊

Disclaimer

It is important that you only use this report if you are the intended recipient of this report and you have satisfied yourself that you are eligible to receive such information. This report is provided to you because you are one of our esteemed customers and have previously shown interest in receiving the type of information contained in this report.

The Treasury and Investment Management department of Gulf International Bank B.S.C. ("GIB") have compiled the information in this report. GIB is incorporated in the Kingdom of Bahrain and is licensed by the Central Bank of Bahrain (the "CBB") as a conventional wholesale bank. GIB's head office is located at Al-Dowali Building, P.O. Box 1017, 3 Palace Avenue, Manama, Kingdom of Bahrain.

This report is intended for the accredited investors, as defined in the Investment Business Code of Conduct published by the CBB. This information has not been reviewed by the CBB or any other regulatory authority in any jurisdiction and neither CBB nor any other regulatory takes any responsibility for the correctness or accuracy for the information contained in this report.

The information contained herein is not directed at or intended for use by any person resident or located in any jurisdiction where (1) the distribution of such information is contrary to the laws of such jurisdiction or (2) such distribution is prohibited without obtaining the necessary licenses or authorizations by the relevant branch, subsidiary or affiliate office of GIB and such licenses or authorizations have not been obtained. The recipient of such information is responsible for ensuring that this information has not been received by it in breach of laws and regulations of any jurisdiction.

This report contains publicly available information only, which has only been complied by GIB. The information provided herein is on "as is" and "as available" basis and without representation or warranty of any kind. GIB hereby disclaims any representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability, fitness for any particular purpose or non-infringement of any of such information. In no event shall GIB or its subsidiaries, affiliates, shareholders or their directors, officers, employees, independent contractors, agents and representatives (collectively, "GIB Representatives") be liable (1) for any inaccuracy, delay, loss of data, interruption in service, error or omission or for any damages resulting there from, or (2) for any direct, indirect, incidental, special, compensatory or consequential damages arising from any use of information or arising from any error (negligent or otherwise) or other circumstance or contingency within or outside the control of GIB or any GIB Representative, in connection with or related to obtaining, collecting, compiling, analyzing, interpreting, communicating, publishing or delivering any such information. The information here is, and must be construed solely as, compilation of information (unless expressly stated otherwise) and not statements of fact as to credit worthiness or recommendations or opinions of GIB.

This report does not provide individually tailored investment advice. Any materials contained herein have no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. The document is provided for information purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. GIB makes every effort to use reliable, comprehensive information, but we do not represent that it is accurate or complete. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the materials, nor are they a complete statement of the securities, markets or developments referred to herein. Recipients should not regard the materials as a substitute for the exercise of their own judgement. Any opinions are subject to change without notice and may differ or be contrary to opinions expressed by other business areas or groups of GIB as a result of using different assumptions and criteria. GIB is not under any obligation to update or keep current the information contained herein.

The value of, and income from, your investments may vary because of changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of companies or other factors. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realised.

The information contained in this report is just for informational purposes. Information does not constitute a solicitation, an offer, or a recommendation to buy or sell any investment instruments, to effect any transactions, or to conclude any legal act of any kind whatsoever. GIB does not intend to provide investment, legal or tax advice through this report and does not represent that any securities or services discussed are suitable for any investor. When making a decision about your investments and business, you should seek the advice of professional advisors.

The report may contain statements that constitute "forward looking statements". While these forward looking statements may represent GIB's judgment and future expectations, a number of risks, uncertainties and other important factors could cause actual developments and results to differ materially from GIB's expectations. GIB is under no obligation to (and expressly disclaims any such obligation to) update or alter its forward-looking statements whether as a result of new information, future events, or otherwise. The historical information is provided for information purposes only. Performance figures are calculated before tax (if any) and after deducting ongoing fees and expenses. The performance figures are historical and past performance is not necessarily an indication of future results. Certain amounts (including %ages) included in this document may have been subject to rounding adjustments. Accordingly, figures may not be an exact arithmetic aggregation of the figures to which they relate. The values and forecasts shown represent our current indicative valuations and forecasts of the relevant transactions, currencies, interest rates, commodities or securities as at the date shown. Any value or forecast shown herein is not an indicative price quotation. We expressly disclaim any responsibility for the accuracy of the values or forecasts shown, any errors or omissions in the report

With the exception of information regarding GIB and save as otherwise specifically indicated, the information set out in this report is based on public information. We have, where possible, indicated the primary source of information. We strongly recommend the recipients consult the primary source of information. Facts and views in this report have not been reviewed by, and may not reflect information known to, professionals in other GIB business areas.

This Report, and the information contained herein (save to the extent that such information is publicly available) is confidential and may not be disclosed by you to any other person outside of your organization without our consent.

GIB retains all right, title and interest (including copyrights, trademarks, patents, as well as any other intellectual property or other right) in all information and content (including all text, data, graphics and logos) in this document. All recipients must not, without limitation, modify, copy, transmit, distribute, display, perform, reproduce, publish, license, frame, create derivative works from, transfer or otherwise use in any other way for commercial or public purposes in whole or in part any information, text, graphics, images from this document (excluding publicly available information) without the prior written permission of GIB.