Weekly Market Summary

May 29th, 2020

A Misleading Market Herd Behavior?! Coming Weeks Will Provide a Clear Verdict!
Fadi Nasser - Deputy Chief Investment & Treasury Officer

Latest Update on Coronavirus: Confirmed cases last at 5.93 million, with the death toll from the pandemic exceeding the 350,000 threshold (362,613 deaths last). The COVID-19 is currently affecting 213 countries and territories around the world. The death toll in India has lately surpassed the number of lives lost in China, while cases in Brazil, Russia and Mexico continue hitting daily records as hot spots shift to developing countries ill-equipped to contain the virus spread. The aviation industry's recovery from the coronavirus outbreak will be long and slow, with passenger numbers likely to stay below pre-pandemic levels through 2023, according the S&P Global Ratings. Various countries that have lately witnessed a steady or lower infection rate are moving fast to ease lockdowns, curfews and domestic travel restrictions between cities. Last, the Boston marathon has been cancelled - though a virtual event will be staged in September (all signed participants in the virtual race would run the marathon distance 26.2 miles sometimes between September 7th and 14th and upload data to a fitness app!)

It is often said that hope is not an investing strategy to live by! Yet most - if not all - of the past few weeks' stock market gains and run to a 3-month high have been built on hopes the worst of the coronavirus' infections/deaths are behind us (helping to ease lockdown restrictions globally), as well as the assumption that governments/central banks' gigantic stimulus measures will deliver immediate benefits. Jamie Dimon, JPMorgan Chase & Co. boss, put it well this week. "*This wasn't the bazooka*," he said, referring to Fed Chair Jay Powell's response to the coronavirus crisis. "*The Fed took out the whole military and applied it. Just announcing these programs reduced credit spreads in the market. It's going to save a lot of small businesses*." (it will surely unleash multiple asset bubbles and allow zombie firms/ investors to persist too!) As a result, the equity market's glass has gone from pretty much empty to at least half full (and more) with the Dow Jones industrial Average (DJIA) rallying more than 2300 points, or roughly 10%, in the past two weeks alone (the S&P and NASDAQ indices have jumped 8% and 6% respectively during that same period, though both led the move higher in past 2-months).

It is often assumed that markets have absurdly overvalued prices of financial assets and then precipitated the price reversal once they had realized the glaring disconnection between the economic reality and the valuation of those financial assets in question. The buzzword often used here or there to describe this phenomenon is the term Self-Fulfilling Prophecies. The latter refers to the socio-psychological phenomenon of someone "predicting" or expecting something, and later this "prediction" or expectation comes true simply because one believes it will, and the resulting investors' herd behaviour aligns to fulfil those beliefs (strongly suggests that peoples' beliefs influence their actions). For instance, if investors think the stock market will crash, they will buy fewer stocks or sell their equity portfolios – rapidly leading to a wider market selloff – and vice-versa on the upside.

As a matter of fact, markets nowadays are just focused on positives, with risk sentiment holding up and investors ignoring potential downside risks related to Trump's less market-friendly views, such as his persistent criticism of China and constant attacks on social media companies, as well as widespread rising economic, political and geopolitical concerns that will eventually preserve heightened market volatility. After all, Covid-19 continues to take its human and economic toll both inside and outside of the US. For instance, the US Labour department yesterday reported 2.123 million new initial jobless claims for the week ended May 23rd, whilst first-quarter gross domestic product (GDP) showed a revised fall of 5.0% (so -5%!) versus initial estimates for a 4.8% contraction – marking the biggest drop since the 2008 financial crisis.

At the same time, US confirmed coronavirus are now close to 1.77 million with the death toll surpassing 103.000. “American shares are as much as 16% overvalued at present levels, and a short position on the S&P 500 Index looks increasingly favourable,” said Daniel Grosvenor, Director of Equity Strategy at Oxford Economics. “Low bond yields aren’t sufficient to sustain equity valuations after the surge in shares from the March lows,” he added.

Is the equity market vulnerable to a correction? Will investors witness a large move lower over the coming days/weeks? Until that happens, we provide below a coverage of the main stories that have shaped markets this week:

- ***Europe’s Consolidated Stimulus Package Sparks “Mother of All” Market Dreams!*** The most audacious fiscal plain in Eurozone history is creating bullish hopes amongst bankers, traders and asset managers across the Old Continent. The European Commission’s $750 billion Euro (roughly $825 billion) package of grants and loans has raised the spectre of deeper fiscal integration among investors, a scenario few might have considered just weeks ago! It is also fuelling an optimistic mood in the market and helping the Euro, along with riskier European assets, climb higher. To be sure, bailout packages from the European Commission don’t involve full mutualization of debt, and would still require approval from sceptical nations (Netherlands, Austria, Denmark, Sweden, ..). EUR/USD last bid at 1.1130 after trading to a low of 1.0775 just two weeks back!

- ***Russia and Saudi Arabia Pledge Coordination Ahead of OPEC+ Meeting***: Both countries have agreed to closely coordinate on the status of OPEC+ output cuts two weeks ahead of a crucial meeting of the Group on June 9-10th. The talks between President Vladimir Putin and Saudi Crown Prince Mohammed Bin Salman come as Russia was said to be determined to start easing oil output cuts in July, as agreed by OPEC+ in April. The June discussions amongst OPEC+ members – via online meetings – will focus on whether they should extend their record production cuts or start tapering them. Brent oil future - for August delivery – was last trading at $35 a barrel, whereas August WTI was hovering close to $33.

- ***Will Trump Announce a Major Set of Sanctions Against China?*** Investors today are waiting nervously for the US President’s latest set of sanctions against China (spelled Chi Na 😊). Trump has said that he will announce some new policies at a press conference on Friday following the National People’s Congress (NPC) near unanimous vote to introduce a sweeping security legislation which bans secession, subversion of state power, terrorism, foreign intervention and allows mainland China’s state security agencies to operate in the city. Yesterday, Larry Kudlow - Trump’s top economic adviser and director of the US National Economic Council – said China has made a “huge mistake” in passing the new national security law regarding Hong Kong. “*Essentially they have robbed Hong Kong of their freedom,”* Kudlow told CNBC. “*We can’t let this go unnoticed and they will be held accountable for that!”*

- ***US President Signs Social Media Order***: President Trump signed yesterday evening an executive order that he said would limit liability protections social-media companies currently enjoy. Under existing law, companies like Twitter and Facebook Inc. are protected for users’ posts. Trump’s move comes after Twitter Inc. began selective fact checks of his posts on the platform, labelling two of his posts about mail-in voting ”*potentially misleading*” and providing links to news coverage of his comments. The US President responded with outrage, accusing the social media company of censorship and election interference and threatening to possibly shut down the service.

- ***UK Lockdown Has been Eased .. Dominic Cummings on the Way Out?*** UK Prime Minister Boris Johnson recently announced that the UK lockdown will be eased to allow small gatherings in parks and private gardens. However a survey from King’s College London found that 41% of adults left their homes fewer than five times in a seven-day period, despite the evolution of the government message from “*Stay Home*” to “*Stay Alert*” and the gradual easing of lockdown restrictions. One in seven adults, or 14%, did not leave their homes once during the week of the survey, whilst 23% of parents said their children were also permanently at home (the psychology of coronavirus fear and the power of herd mentality!). One fellow that never bothered staying at home after suffering coronavirus related eyesight problems is Dominic Cummings, the UK Prime Minister’s most senior aide and previously the director of the Vote Leave campaign (& the “gentleman” with the “GBP 350 million weekly UK paycheck to the EU" invention!). Cummings' decision to move 260 miles from London to Durham at the peak of the pandemic has been dominating UK political events for the past week and led many politicians from different political parties to call for his immediate ousting. It was this journey that Durham policy decided may have breached the rules, though no further action will be taken against Mr. Cummings.

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.