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8 June
2020

BONHÔTE
BANQUIERS DEPUIS 1815

FLASH BOURSIER

A FORECAST-BUSTING WEEK

Highlights:

European banks index surges

US jobs report surprises market

Overview

Economic data turned up sharply in May, while the prospect of more fiscal and monetary splurges is stoking investors' risk appetites. Last week, cyclical sectors and stocks – those which took the worst hit during the lockdown – continued to build on earlier gains. The European banks index soared by 20%, driven by abundant liquidity and renewed steepening on yield curves. Oil companies were also in demand. Despite high stock multiples and the prospect of earnings downgrades, liquidity from central banks continues supporting markets.

Spooked by possible deflation, the ECB last Thursday increased the size of its Pandemic Emergency Purchase Programme (PEPP) by EUR 600 billion to EUR 1,350 billion and extended it to June 2021, while also stating that the proceeds from maturing issues would be reinvested. The ECB is especially scared of a sharp decline in Eurozone GDP. In the bond market, massive inflows led to tighter credit spreads in investment-grade and high-yield segments. Long-dated yields on government bonds have risen across the board (10-year US Treasury at 0.92%). Spreads on peripheral sovereign debt also narrowed.

The US jobs report for May took investors by storm. Job additions clocked in at 2.5 million whereas the consensus had expected the economy to shed 7.5 million jobs. The unemployment rate fell to 13.5%. No doubt it will take time for analysts to come to terms with their gigantic forecasting blip as they try to make sense of the numbers. One explanation may lie in the discrepancy between the 43 million initial jobless claims and the 21 million who actually receive any benefits. This will need to be followed up. But in the meantime, risk assets have the wind in their sails. The Fed meets this week and is not expected to renege on its largesse.

OPEC last week agreed to extend production cuts by 10m barrels per day and will strengthen checks on the many who game the system by not respecting quotas. If everyone does stick to the plans (which is rarely the case), this will pave the way for more cuts to absorb the backlog of reserves run up during the Covid-19 pandemic and restore the minor supply gap in the market.

Lastly, the plunge in Germany's industrial production – 25.3% year-on-year in April – startled observers as the lockdown took its toll on the economy. China booked a record trade surplus in May (USD 62.9 billion vs. the USD 41.4 billion expected). Exports fell by 3.3% and imports – reflecting lower oil prices – dropped by 16.7% year-on-year.

The SMI is likely to take time out and hover around 10000 points this week.

Key data

	USD/CHF	EUR/CHF	SMI	EURO STOXX 50	DAX 30	CAC 40	FTSE 100	S&P 500	NASDAQ	NIKKEI	MSCI EMERGING MARKETS
Latest	0.96	1.09	10'190.37	3'384.29	12'847.68	5'197.79	6'484.30	3'193.93	9'814.08	22'863.73	1'002.65
Trend	➡	⬆	⬆	⬆	⬆	⬆	⬆	⬆	⬆	⬆	⬆
%YTD	-0.55%	0.09%	-4.02%	-9.64%	-3.03%	-13.05%	-14.03%	-1.14%	9.38%	-3.35%	-10.05%

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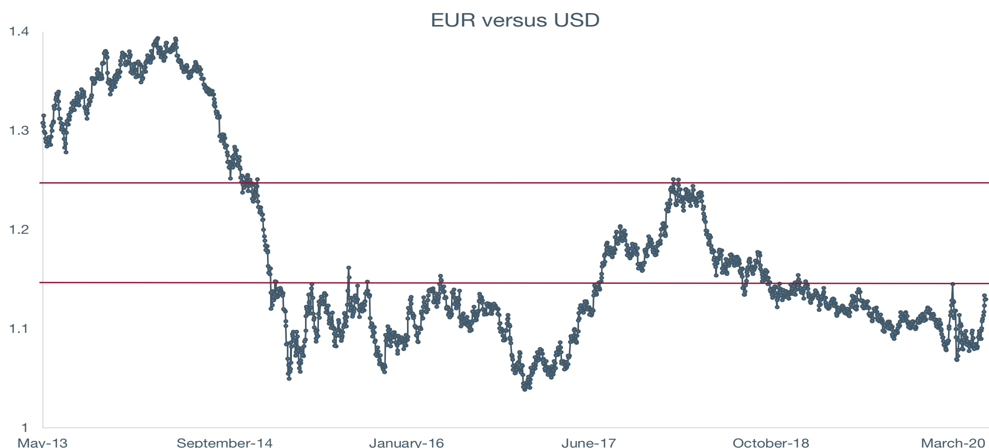
EURO PERKS UP



The euro has long been dogged by the fragility of the Eurozone itself.

There are several reasons why it has constantly traded with a risk premium. For one, European countries have struggled to form a common front against the two economic superpowers which are China and the US. Next, it lacks a common budget. There is no fiscal union to match the currency union. Then each Member State tends to defend its own interests above those of the group, especially for electioneering purposes. And then there's Brexit.

Today, however, four reasons are together propelling up the euro against the US dollar.

1. Europe is emerging from the coronavirus crisis more quickly than North America.
2. Valuations in Europe are more attractive than those of US firms. This is luring capital to our shores just as US rates have become less attractive and yield curves are steepening again. Steeper yield curves help financials, which are more heavily represented in the pan-European index.
3. The Fed's balance sheet is growing at a faster rate than the ECB's. This ought to push down the dollar, as whoever prints the most currency is likely to depress its value going forward.
4. Though still requiring national approval, talks about debt pooling in Europe represent a paradigm shift: a major step towards integration which could reduce the risk premium on the euro.

The euro is trending up. A target of 1.24 versus the US dollar now looks within reach.

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