RBMC

THE BHAR REPORT

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The Week in the Markets

Week of 17 April 2020 – Number 14

Weekly price change	S&P 500	Shanghai	US 10-YR	DXY	WTI	Gold	LMEX	LME Cu	LME Al	LME Ni	LME Zn	LME Pb	LME Sn
Last	2,886	2,838	0.64%	100.1	$18.7	$1,686	2,386	$5,171	$1,513	$11,696	$1,938	$1,674	$14,960
Change w-o-w	3.4%	1.5%	-0.08	0.7	-18%	0.1%	1.9%	2.8%	2.2%	0.8%	1.9%	-1.7%	0.0%

Macro Themes

The **Covid-19** pandemic has pushed the world into **recession**. For 2020 it will be worse than the global financial crisis. The economic damage is mounting across all countries, tracking the sharp rise in new infections and containment measures put in place by governments. As of 17 April, about 2.2mn cases have been confirmed worldwide, and the death toll has surpassed 146,000, according to Johns Hopkins University data. **China** posted a contraction in GDP of 6.8% y-o-y in Q120, the first contraction since records began in 1992.

As highlighted in **Chart 1**, central banks and governments are doing everything in their power to support the economy (and the stock markets), which will eventually lead to **inflation**. The **Fed** announced last week a broad $2.3tn stimulus package to help weather the pandemic and insulate the US economy from the worst of the shock. The package included the Main Street Lending Programme (MSLP) which is a $600bn scheme to help larger companies during the pandemic. The Fed's **balance sheet** now exceeds $6tn ($6.2tn to be exact). Governments and central banks have unleashed $8tn of fiscal stimulus measures, which is equivalent to 10% of global **GDP**. **Debt** levels, already very high, are increasing. The sale of gross government debt rose to a record high of over $2.1tn last month, more than double the 2017-19 average of $900bn, according to the IIF. That will weigh upon future economic activity and corporate revenues.

The scale of measures partly reflects lessons learnt during the 2008 crisis. Moves to stabilize the financial system that took months to be instigated then were launched much more rapidly in response to the economic disruption caused by Covid-19. **Swap lines** with foreign central banks were introduced almost immediately, **QE** programmes were restarted and the Fed has intervened in **money markets** and **corporate financing** to take the burden off banks in a time of stress. It is forecast that the Fed's balance sheet will reach $9tn by the end of the year, or about 40% of **US national income**. Proportionally, that would bring the Fed roughly into line with the ECB, but still far below the BoJ, whose assets amount to more than 100% of national income. Overall, these crisis-fighting measures appear to be working. The extraordinary monetary stabilization measures have halted the purely financial aspects of the crisis, stabilizing money markets and easing the **USD** funding squeeze: **S&P 500** has rallied 9% so far this month. Meanwhile, the **USD** index (DXY) has now eased from its highs (see **Dashboard**).

As a result of the pandemic, the **global economy** is projected to contract sharply by –3% in 2020, much worse than during the 2008–09 financial crisis (making this the worst recession since the **Great Depression** when global GDP fell by 10% during 1929-32), according to the latest **World Economic Outlook** report published by the *IMF ("The Great Lockdown")*. In a baseline scenario - which assumes that the pandemic fades in the second half of 2020 and containment efforts can be gradually unwound - the global economy is projected to grow by 5.8% in 2021 as economic activity normalizes, helped by policy support (see **Chart 2**). But the level of GDP will remain below the pre-virus trend, with considerable uncertainty about the strength of the rebound. There is extreme uncertainty around the global growth forecast says the *IMF*. The economic fallout depends on factors that interact in ways that are hard to predict, including the pathway of the pandemic, the intensity and efficacy of containment efforts, the extent of supply disruptions, the repercussions of the dramatic tightening in global financial market conditions, shifts in spending patterns, behavioral changes (such as people avoiding shopping malls and public transportation), confidence effects, and volatile commodity prices.

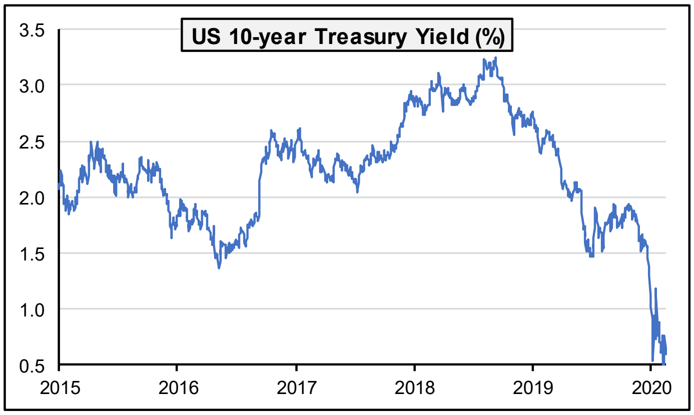
Precious Metals

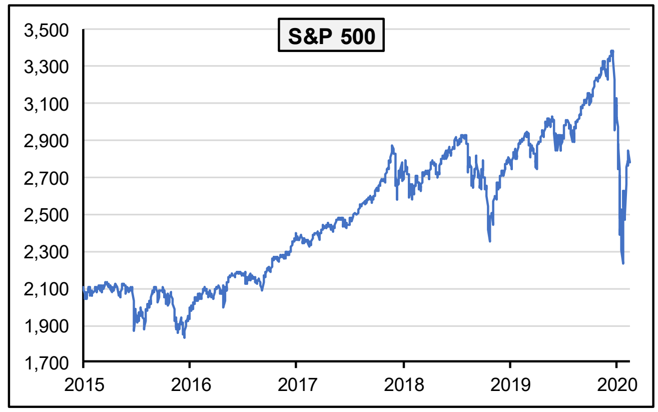
The massive influx of **liquidity** is a significant boost to **gold** as a hedge against inflation. Fed easing is likely to prompt real US interest rates (real rates capture the inflation-adjusted opportunity cost of holding gold in a portfolio) to dip deeper into negative territory and perhaps even test the post-GFC lows shown in **Chart 3**. Gold will remain underpinned by its two main drivers: **real US interest rates** and the **USD**. Looking back over the past 20 years, the negative relationship between gold and real rates has been strong. The highest gold prices were recorded in an environment of low or negative real rates and high rates tallied with low gold prices. If the IMF predictions were to materialize, continued fiscal and monetary support, weakening budgets, possible debasement of currencies and an increase in demand for gold are other bullish factors. **Technically**, gold broke above the March high at $1,704 and climbed to the highest level since October 2012. It has now closed above the 76.4% retracement level of the 2012 – 2015 fall at $1,714. This would suggest further extensions towards the $1,800 handle where the 2011-2012 highs converged followed by the all-time high at $1,921 set in September 2011. Below key price support at $1,453/46 is needed to change this view as this would mark a top, turning the risk lower as well as ending its bullish outlook. **Silver** is lagging gold as evidenced by the **gold:silver** ratio above 100; but its critical to tomorrow's green technologies, including solar panels and electric vehicles. Its green credentials have been widely known for decades, but it has been overlooked in recent years in favour of **PGMs** for their role in emissions reduction. Silver's use in solar panels increased from 6.1% of total silver demand in 2011 to 7.7% in 2018, whereas the proportion of **palladium** used in auto catalysts grew rapidly from 65% to 80% over the same period (*Heraeus)*.

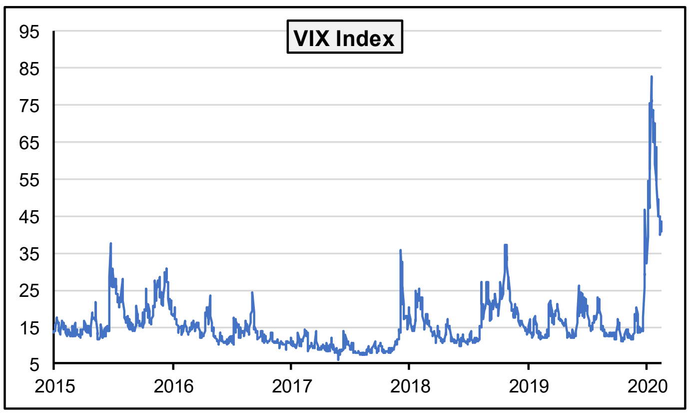
Base Metals

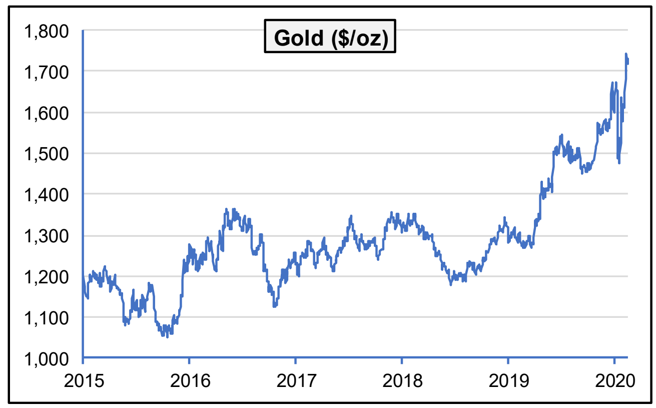
The **base complex** made modest gains on a combination of more mining production cuts (large copper mines in Peru including Antamina, Cerro Verde and Las Bambas), a deal on an oil supply cut, better Chinese trade data that showed imports were only down by 0.9% y-o-y in March (unwrought copper imports were up 9.1% y-o-y in Q120), and ebbing virus concerns in other regions, including the US and Europe. **Copper** is at 4-week highs, despite weak Q120 **China GDP**, but prices are still 10% lower than earlier in March. Meanwhile, **aluminium**, languishes because there have been no production cuts. This suggests a lengthy and painful road to recovery, just as we saw a decade ago. **Nickel**, **lead**, **zinc** and **tin** are recovering in response to output cuts of varying extent. Based on the scenario in the *IMF WEO*, metals **prices** should see a strong rebound in 2021 after bottoming out in Q2/Q3 2020. The latest **Reuters analysts' poll** (*COLUMN-How low can we go? Analysts slash base metals forecasts: Andy Home, 14 April*) suggests such a scenario. The median forecast for copper over the next four quarters for example is $4,700/t, $5,000/t, $5,500/t and $5,750/t respectively, a pattern that holds true of all six metals traded on the LME. RBMC price forecast reflecting a base case scenario (a strong rebound in 2021 after bottoming out in Q2/Q3 2020) is shown in **Chart 4**. A further and more prolonged slowdown in metal-intensive sectors' economic activity remains the most significant downside risk for metal prices, while supply stoppages present an upside. Charts with moving averages are shown on **The Backpage**.

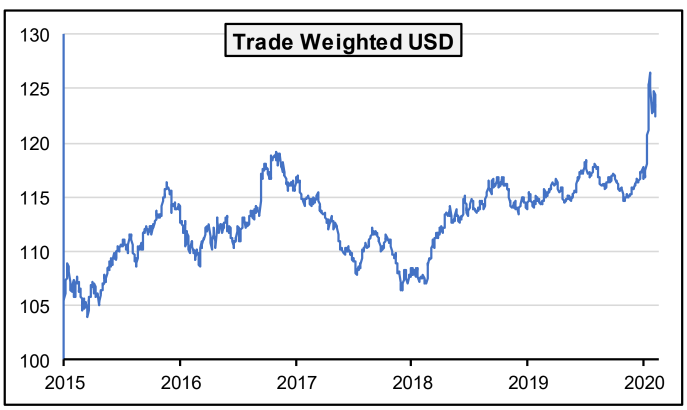
Dashboard – What You Need to Know

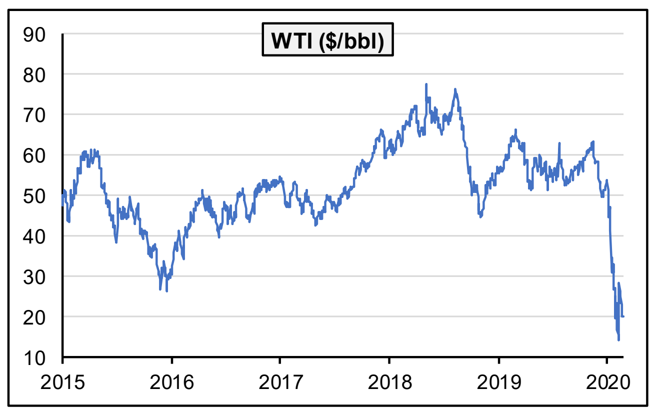


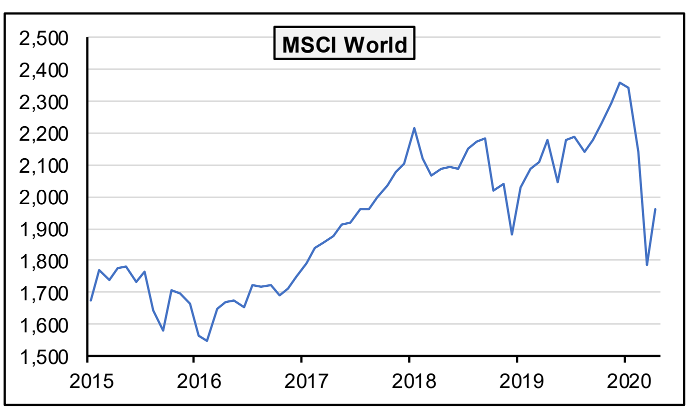


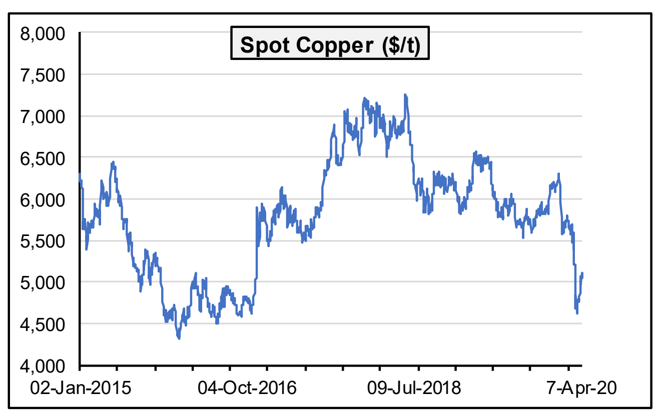












Source: Federal Reserve Bank of St. Louis, Trading Economics

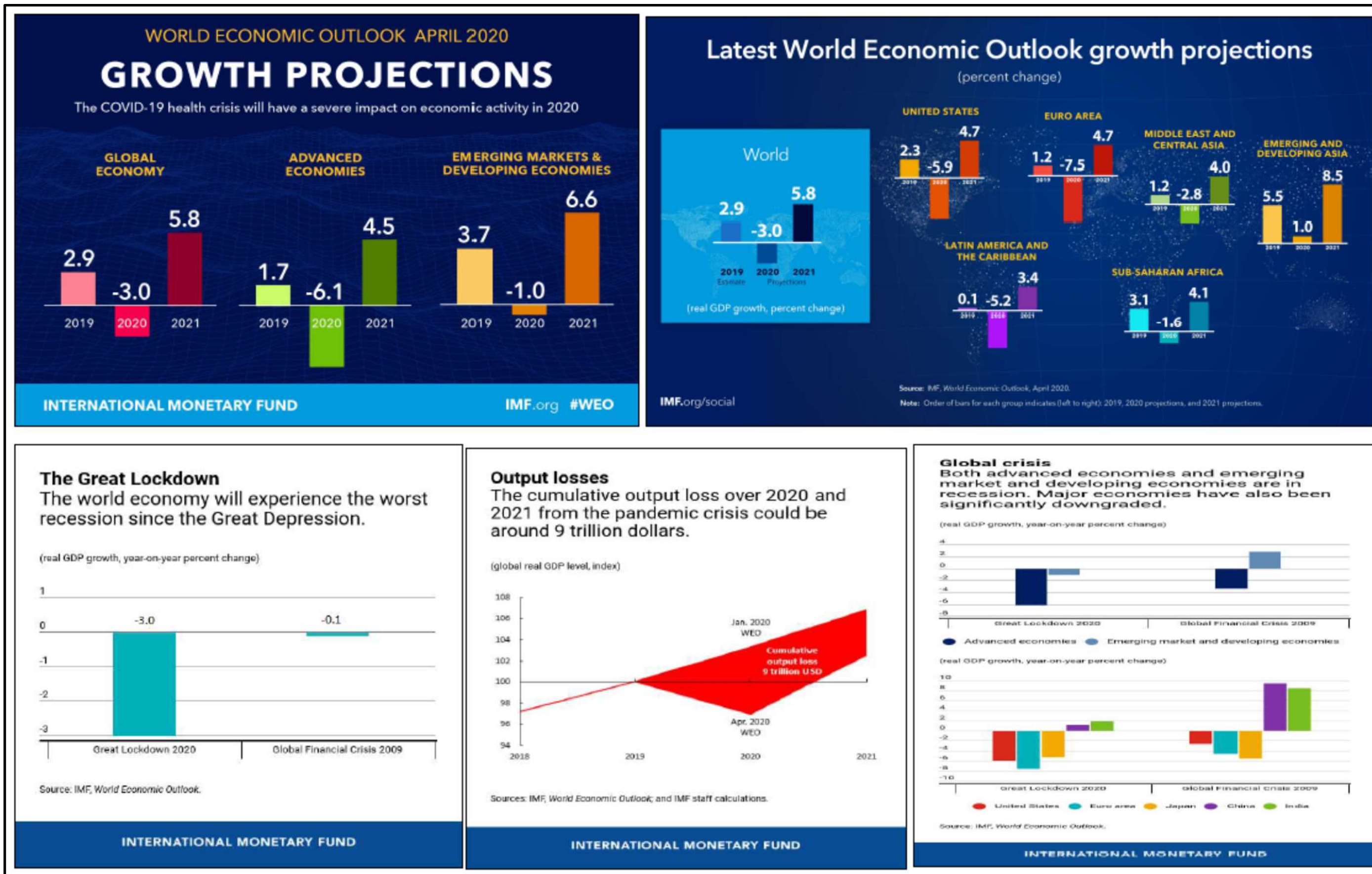
Charts of the Week

Chart 1. Shutdowns work, but exiting them likely to be gradual

Factors needed for quick and robust recovery	Progress	Further progress needed
Infection contained (travel restrictions can be eased)	China/ S. Korea infection rate not re-accelerating meaningfully Infections slowing in Europe and US	Ex-China EM situation doesn't escalate Exit strategy that balances speed against risk of second wave
Policy response - Fiscal stimulus of sufficient size and nature - Central bank backstop	Fed's interventions helping high yield and investment-grade corporate bonds	Joint eurozone solution More encouraging signs that SMEs can access government facilities
Economic resilience - proof of 'suspended animation'	US unemployment so far deemed 'temporary' Furlough schemes being well utilised in Europe	Sanguine earnings guidance Tracking unemployment

Source: J.P. Morgan Asset Management

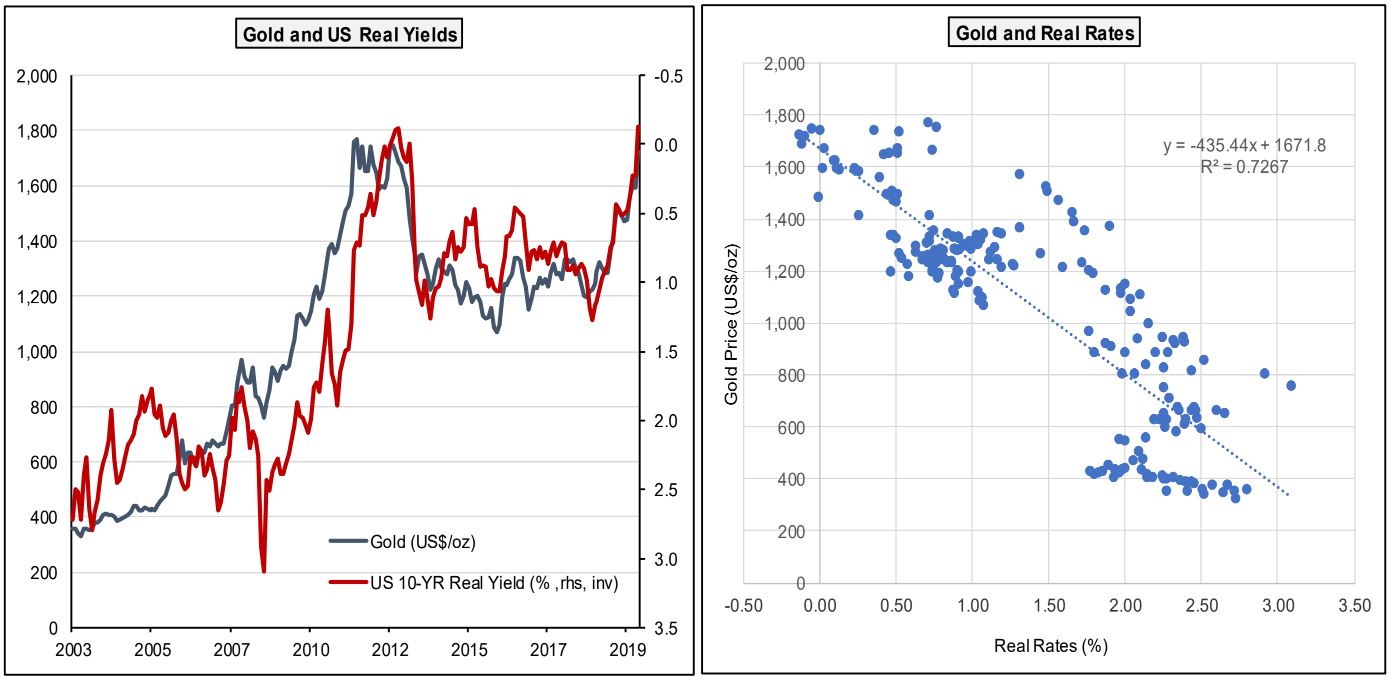
Chart 2. IMF World Economic Outlook



Source: IMF

Charts of the Week

Chart 3. Gold Tracking Real Rates



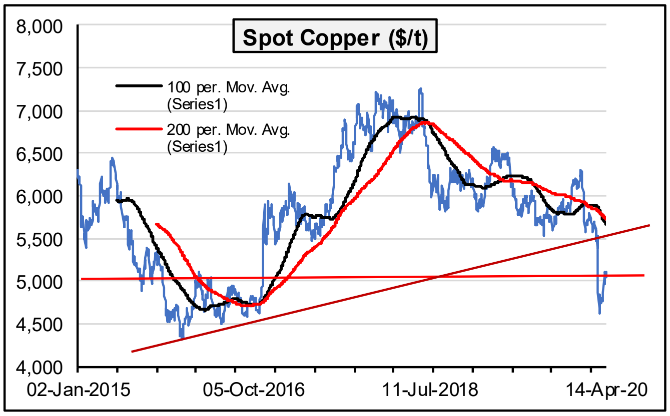
Source: Federal Reserve Bank of St. Louis

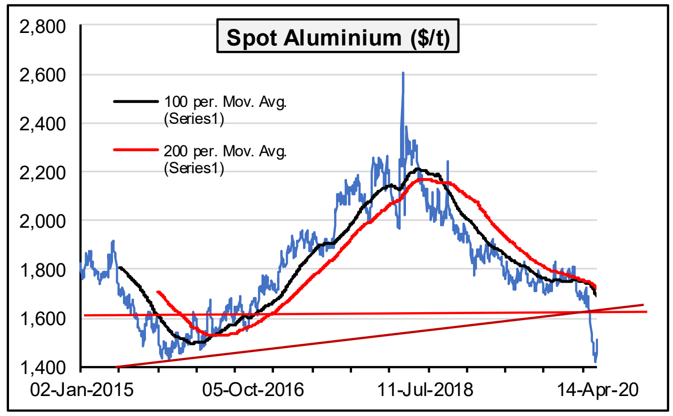
Chart 4. Global/China GDP Growth & Metals Prices, RBMC Forecast

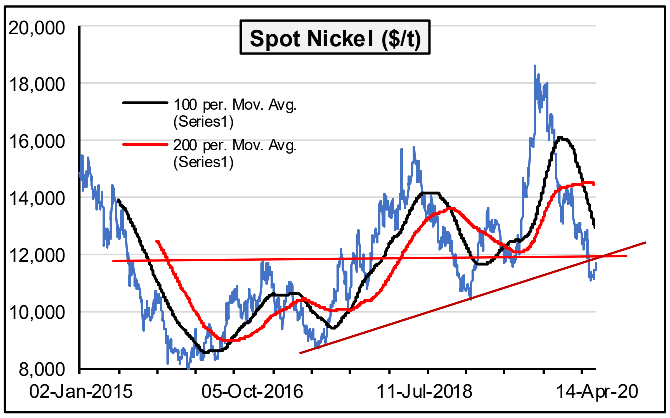
	2020					2021				
	1Q	2Q	3Q	4Q	Year	1Q	2Q	3Q	4Q	Year
Cu	5,638	4,900	4,500	5,000	5,010	5,500	5,750	6,250	6,500	6,000
Al	1,690	1,550	1,525	1,635	1,600	1,650	1,700	1,650	1,700	1,675
Ni	12,723	11,000	11,000	13,275	12,000	14,000	14,500	14,500	16,000	14,750
Zn	2,128	1,850	1,820	2,000	1,950	2,000	2,150	1,950	2,100	2,050
Pb	1,847	1,600	1,700	2,054	1,800	2,100	2,200	2,150	2,350	2,200
Sn	16,278	14,000	13,995	15,725	15,000	16,000	17,000	17,000	18,000	17,000

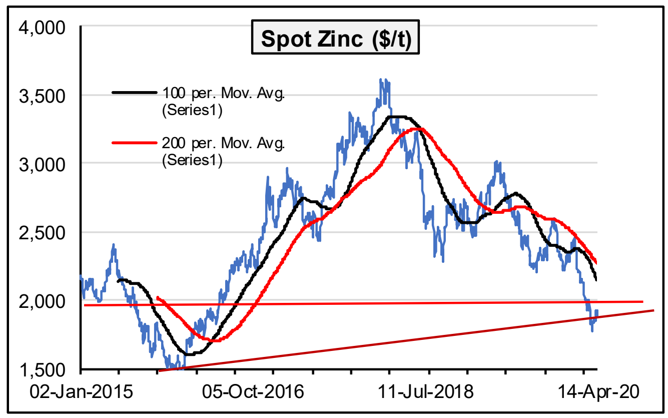
Source: World Bank, IMF, LME, RBMC

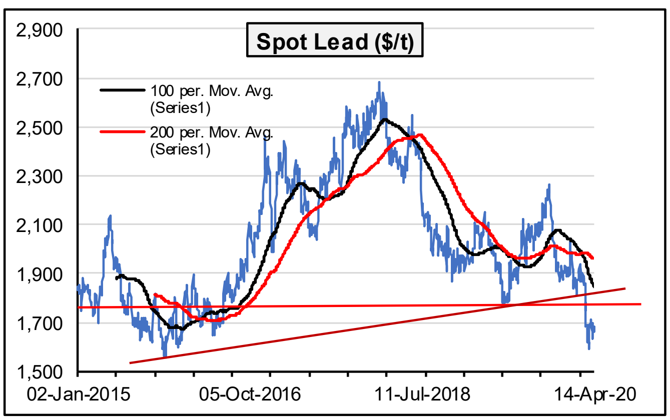
The Backpage – Industrial Metals

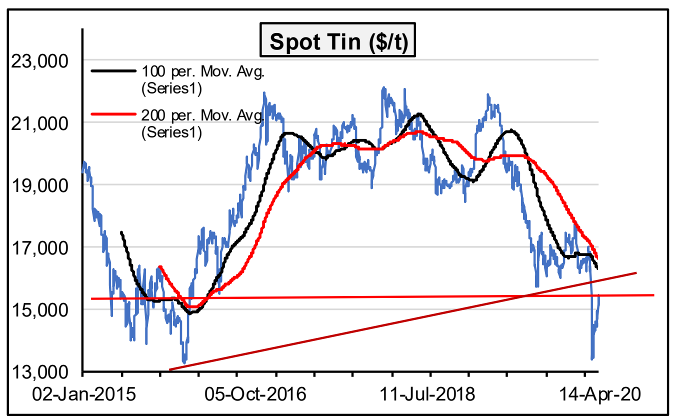


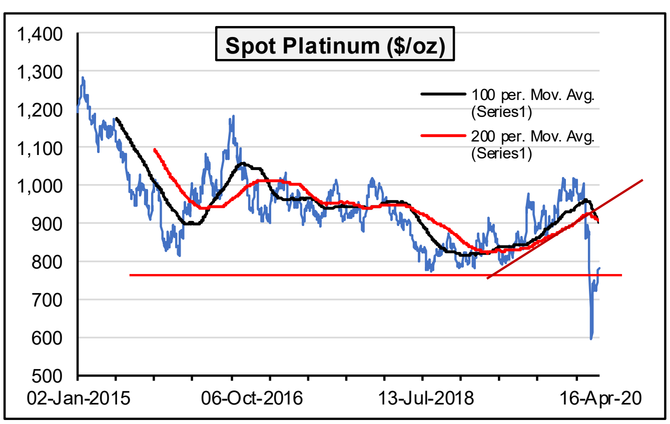


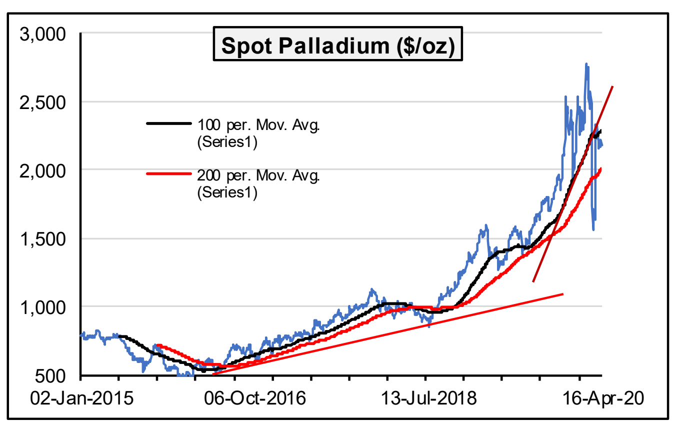












Source: LME, LBMA, LPPM

For more commentary see my blog on www.rbmc.world
Comments, suggestions and feedback is welcomed