RBMC

THE BHAR REPORT

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The Week in the Markets

Week of 29 May 2020 – Number 20

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	3,033	2,807	0.67%	98.0	$32.7	$1,728	2,447	$5,336	$1,537	$12,179	$1,935	$1,614	**$15,515**
Change w-o-w	**3.4%**	**-0.2%**	**0.03**	**-1.7**	**2.5%**	**-0.5%**	**-1.1%**	**1.4%**	**1.1%**	**-4.2%**	**-2.5%**	**-1.6%**	**0.1%**

Macro Themes

As of 29 May, about 5.8mn **Covid-19** cases have been confirmed worldwide, and the death toll has surpassed 360k, according to Johns Hopkins University data. Increasingly its apparent that re-opening will be gradual with testing and contact tracing needed until a vaccine has been developed (see **Chart 1**). The focus of the week was **China's NPC** and a proposal for an EU EUR500bn **recovery fund**. While the NPC's initial proposals appear to have fallen short of expectations, the restrained approach leaves room for policy to be adjusted if the outlook worsens. China also announced moves to impose a controversial Hong Kong security law.

China's top leaders convened for the annual **Two Sessions** meetings last Thursday, following over two months of delays due to the Covid-19 outbreak. The Two Sessions refer to the annual meetings of the Chinese People's Political Consultative Conference (CPPCC) – an advisory body of over 2,000 members – and the National People's Congress, China's top legislative body. They are China's most important annual political meetings, highlighted by the delivery of the **Work Report** by Premier Li Keqiang, which lays out the government's agenda and policy priorities for the coming year.

The **Work Report** placed more emphasis on job market stabilization and improving people's livelihoods. Its implications, however, could stretch beyond the current crisis, as 2020 is also the last year of the current **Five Year Plan**. As such, the way in which the rest of the year plays out – whether positively or negatively – could influence the drafting of the next Five Year Plan that will shape policies until 2025. No **GDP** growth target for 2020 was set, marking the first time the government did not set a target since records began in 1990. The government opted not to set a growth target because of the high level of uncertainty caused by Covid-19 and its effects on the global economy and global trade.

A **fiscal stimulus** package of almost RMB3.6tn ($506bn) was announced to lead China's economic recovery following the Covid-19 disruption. China's stimulus package is substantial and similar in size to its 2008 response, which came in at about RMB4tn ($572bn). However, China's economy is significantly larger than it was in 2008, meaning that this stimulus package is a much smaller percentage of GDP (approx. 6.1% of GDP compared to around 12-13% of GDP in 2008). Most of this stimulus will come in the form of bond issuance (e.g. special treasury bonds and local government special bonds), as shown in **Chart 2**. More stimulus could come later in the year, according to CRU. The **US**, in contrast, has already injected over US$3tn into its economy. Stimulus will be more targeted towards areas that will help China transition to a high-tech and service-driven economy. China built massive amounts of infrastructure during its economic boom, meaning that there are now diminishing returns to further infrastructure investments in new projects. Accordingly, government planners are focusing on investing in **"new infrastructure"** - infrastructure used for high-tech and sustainable purposes. This includes, for example, big data centers, high-speed rail, 5G infrastructure, and charging stations for new energy vehicles (NEVs), among other areas. China needs "smart" infrastructure that will help the economy operate more efficiently and sustainably.

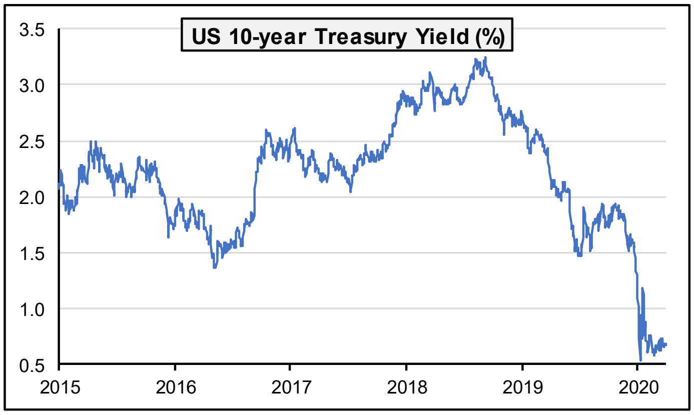
Precious Metals

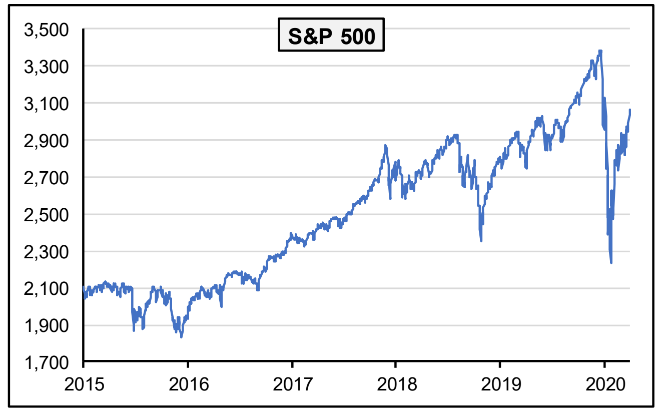
Gold is struggling to make new highs amid returning risk appetite but is holding above the $1,700/oz level on rising geopolitical tensions – not just the US-China trade tensions but also the US warning that it could no longer certify Hong Kong's political autonomy from China. Nonetheless, dips should continue to prove both shallow and short-lived amid record amounts of fiscal and monetary stimulus. The relationship between US M2 money supply and the price of gold is shown in Chart 3. The recent round of Fed stimulus is strongly supportive for gold. Investors continue to load up on physical gold, with total holdings in gold-back ETFs rising for the 23rd consecutive day, according to *Bloomberg* data. Physical demand in China and India remains weak and offtake is plummeting. **Silver** is playing catch-up to gold, as evidenced by the **gold:silver** ratio now trading below 100. Silver has gained 43% since the lows of around $12.2/oz were reached in late-March, no doubt helped by the overall pick-up in industrial metals. Silver mine production is increasingly threatened by pandemic hotspots, mainly in Central and South America. Mine supply is forecast to decline by 6.4% to 54.5moz this year (source: *The Silver Institute*). **Platinum** is likely to remain weak, with demand in 2020 forecast to be 6,950koz, 18% (-1,480koz) lower than in 2019 due to lower demand from all four demand segments: automotive (-413koz), jewellery (-315koz), industrial (-104koz) and investment (-647koz), according to the *World Platinum Investment Council* (*WPIC*). However, there is the potential for fuel cells to lift platinum demand in the coming years. With decarbonization firmly on the agenda, fuel cell and electrolyser demand has good growth potential, albeit from a low base today. Meanwhile, **palladium** buying has picked up now that car plants are returning to operation, but demand is expected to drop more than supply this year and a sustainable return above $2,000/oz looks ambitious.

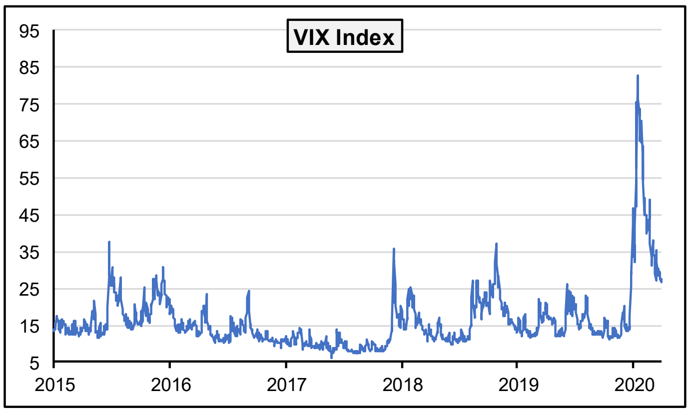
Base Metals

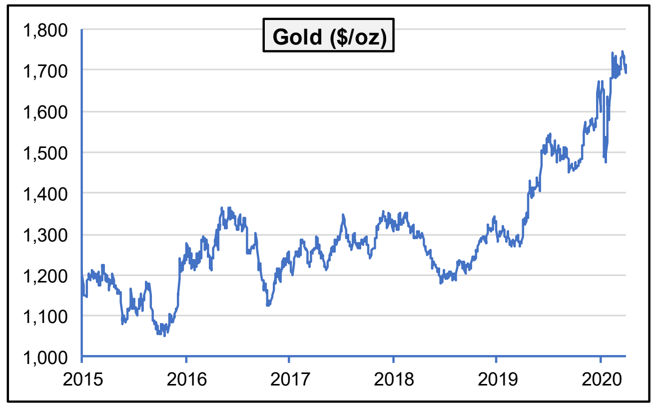
A risk-on tone to markets underpinned the **base metals** complex, but rising trade tensions and easing supply disruptions capped rallies. The **LMEX** is up 10% from its March lows but is still 14% lower than at the start of the year. China's NPC was largely ignored. As a percentage of GDP **China's** fiscal stimulus this time around is much smaller than that seen in 2008 and more targeted towards "new infrastructure" rather than the old fashioned infrastructure booms of the past. Rather than boosting the economy the government is mindful of the huge debt burden the economy has accumulated (*IIF* puts China's debt-to-GDP ratio now at 317%). In light of this issue, the central government has been leading a multi-year debt de-risking campaign and has attempted to reduce reliance on government spending for growth. Thus, there remains uncertainty over how far they will go to stimulate the economy. It may also be a signal that the government is prepared to accept a low level of growth in 2020. With the country consuming half the world's industrial metals, a lower level of growth means weaker demand and subdued prices in 2020. A return to stronger growth in 2021 should see prices boosted significantly. As a result, industrial metals are unlikely to be significantly boosted as was the case in 2008-09. Metals **prices** (LMEX) have picked up from late-March lows as the global economy slowly recovers in the wake of the Covid-19 pandemic and China's fiscal stimulus should assist in underpinning prices over coming months. **The International Lead and Zinc Study Group** (**ILZSG**) released preliminary data for world **lead** and **zinc** supply and demand during Q120. Zinc demand fell by 4% YoY and lead by 7.4% in Q120; lead supply fell by a similar amount, but zinc production rose by 3.2% YoY. As a result, both lead and zinc markets were in surplus to the tune of 19kt and 239kt, respectively (see **Chart 4**). Charts with moving averages are shown on **The Backpage**.

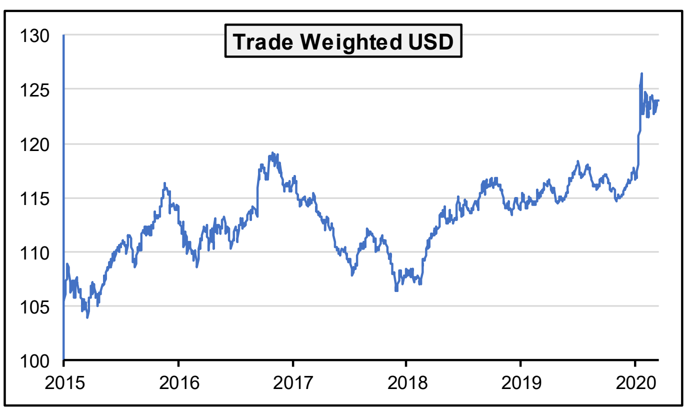
Dashboard – What You Need to Know

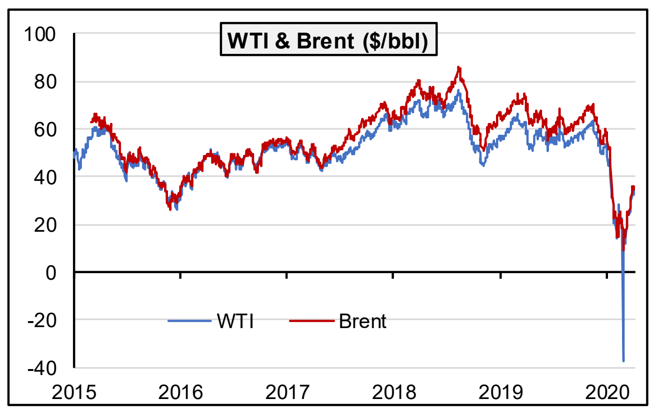


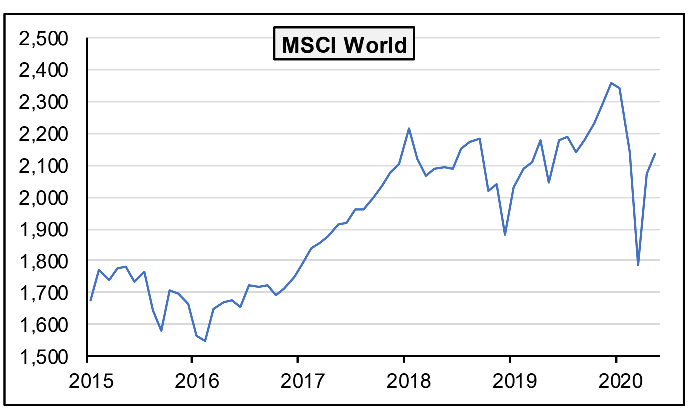


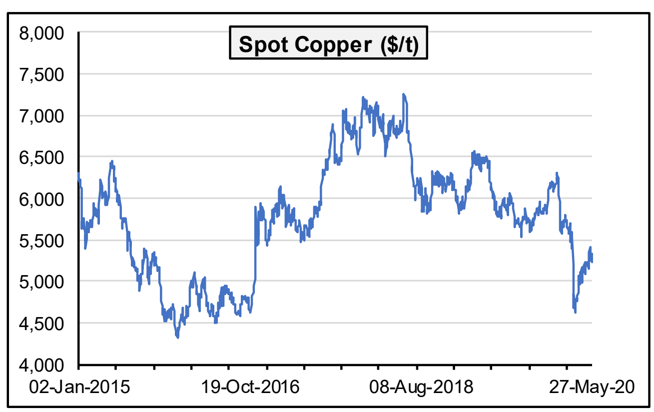












Source: Federal Reserve Bank of St. Louis, Trading Economics

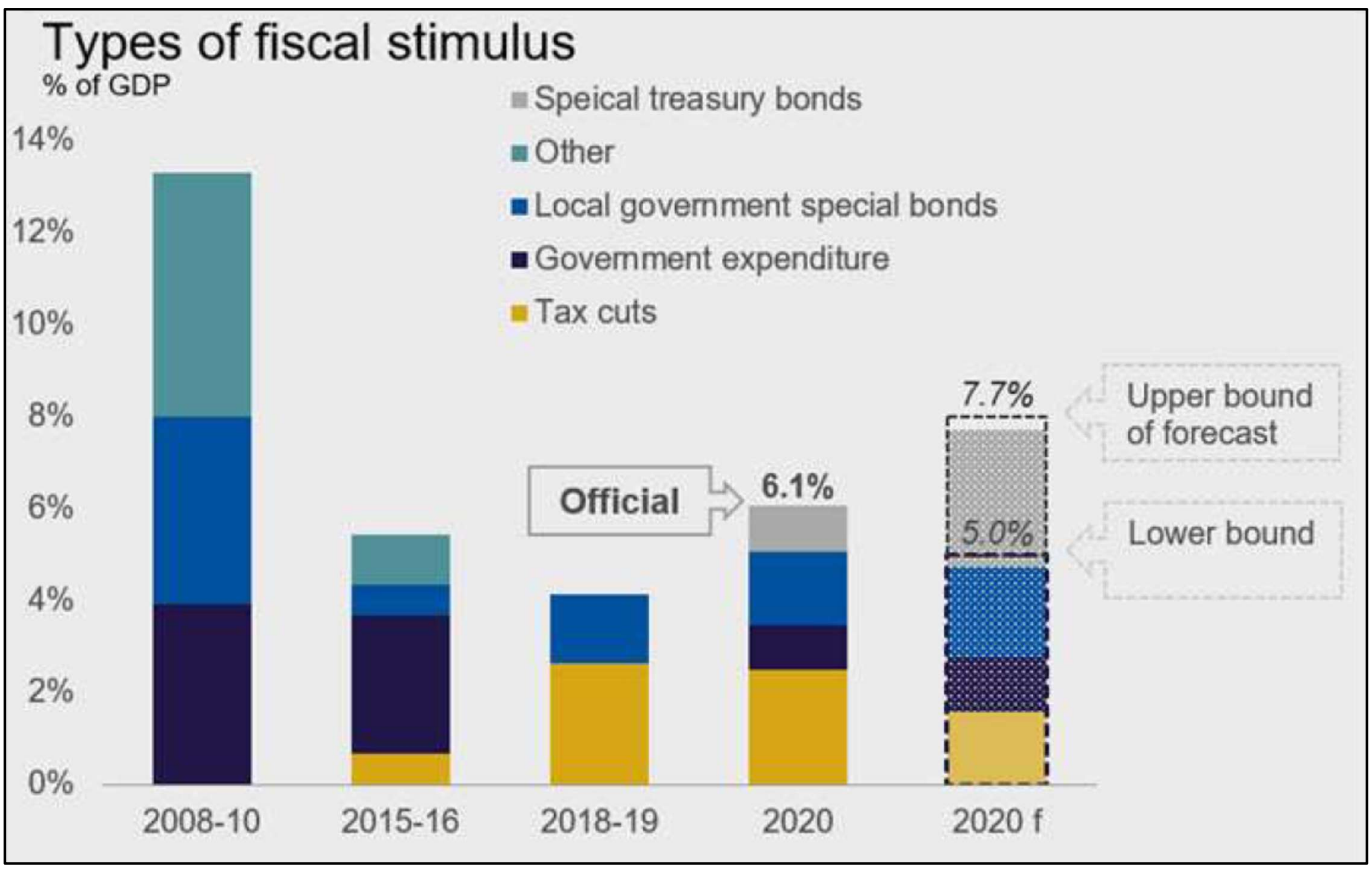
Charts of the Week

Chart 1. So far so good, but early days on reopening

Factors needed for quick and robust recovery	Recent news	Looking ahead
Infection contained (travel restrictions can be eased)	Vaccine race, testing being ramped up Infections still slowing in Continental Europe, now in UK and US	Reopening does not lead to resurgence of infections Stabilisation in infection rates in EM
Policy response - Fiscal stimulus of sufficient size and nature - Central bank backstop - Absence of 'nationalism' and political scapegoating	ECB dismissed German Court ruling Franco-German proposal for EUR 500bn recovery fund dispersed in grants (details announced today) China NPC – focus on stability	Brexit negotiation extension US and China tensions US election implications Fed policy beyond crisis mode
Economic resilience - proof of 'suspended animation'	Little evidence of structural behavioural changes in places that are reopening WHEN infections still low	Increased discussion of conditional loan forgiveness? Monitoring unemployment

Source: J.P. Morgan Asset Management

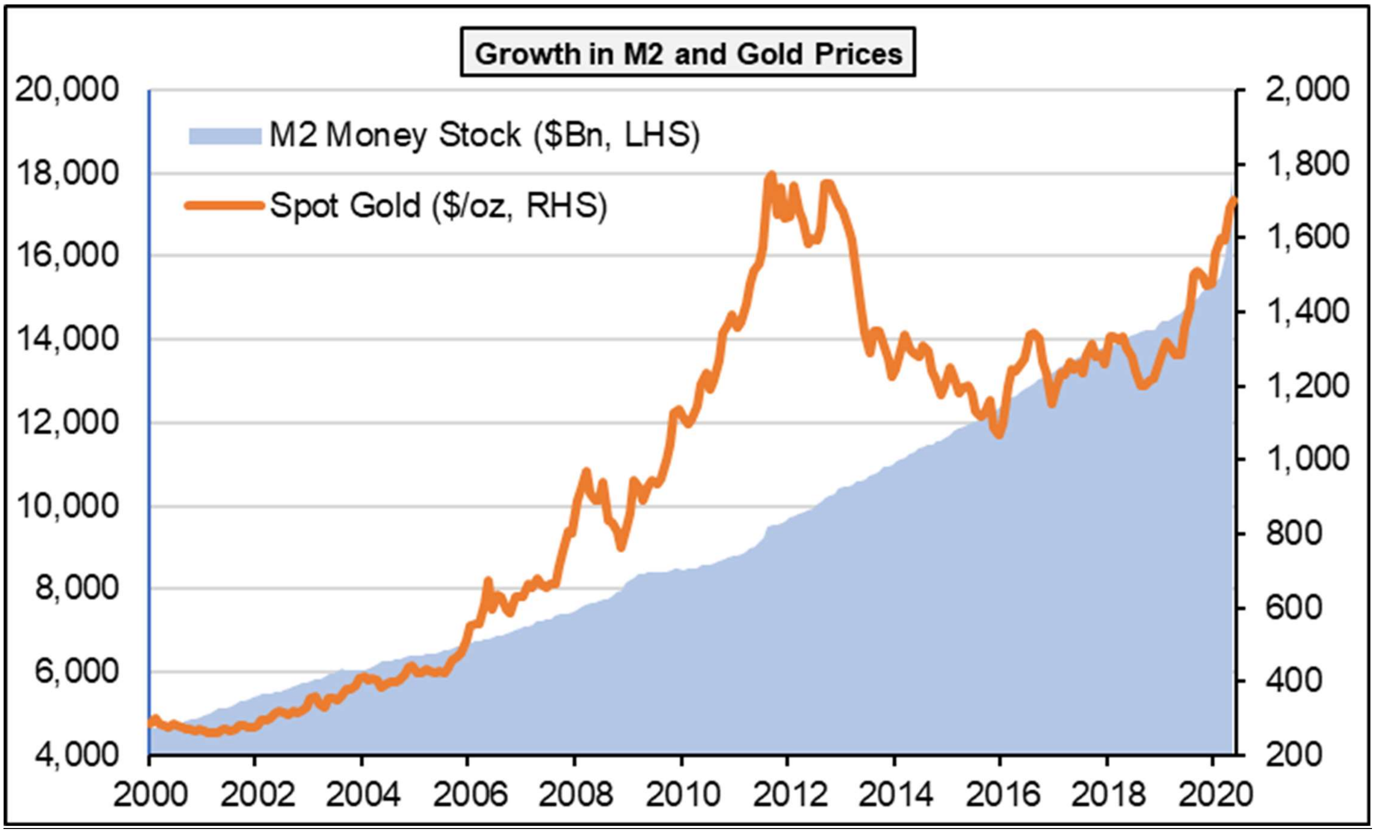
Chart 2. 2020 China fiscal stimulus smaller than in 2008-10



Source: CRU

Charts of the Week

Chart 3. Gold supported by Fed's stimulus

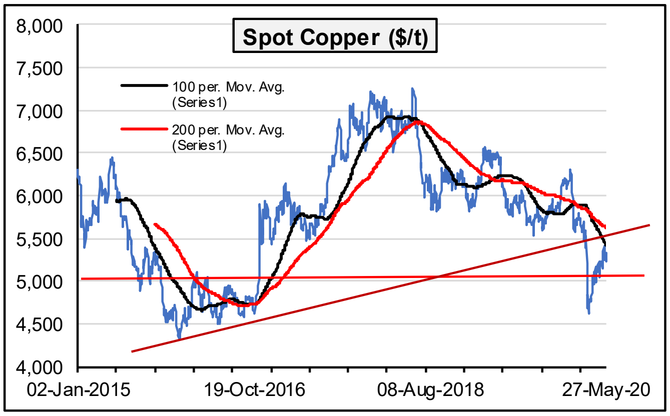


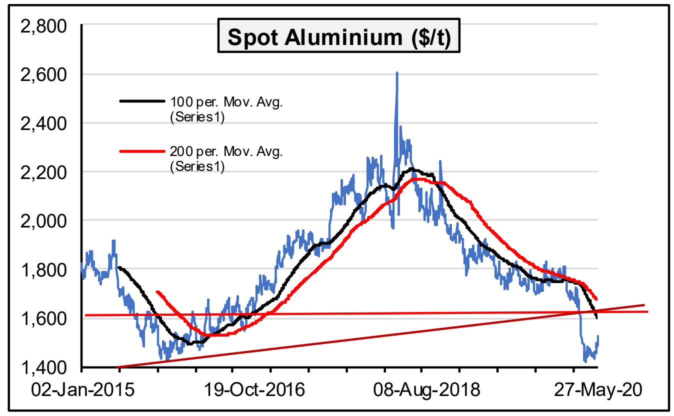
Source: Federal Reserve Bank of St. Louis, LBMA

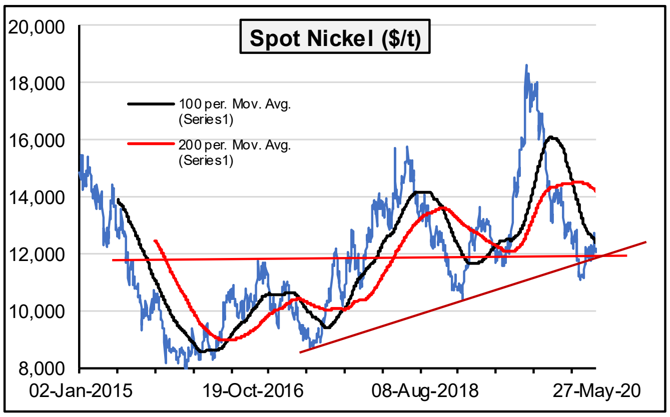
Chart 4. Lead & Zinc in Q120

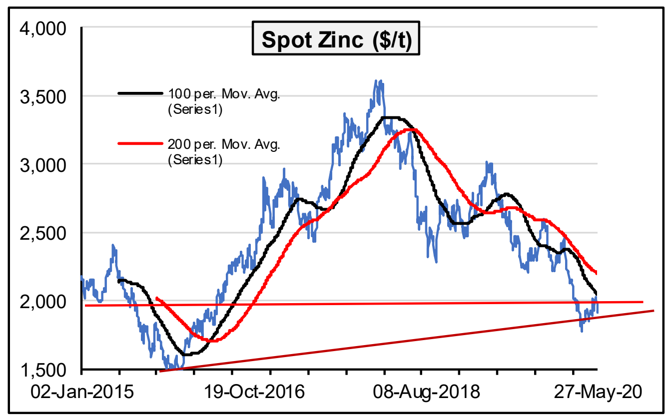
Source: ILZSG

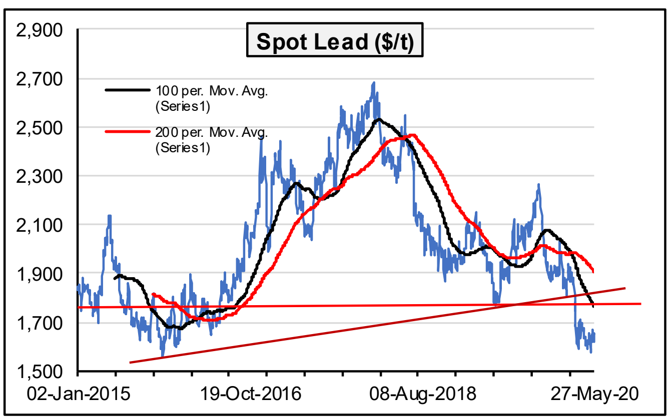
The Backpage – Industrial Metals

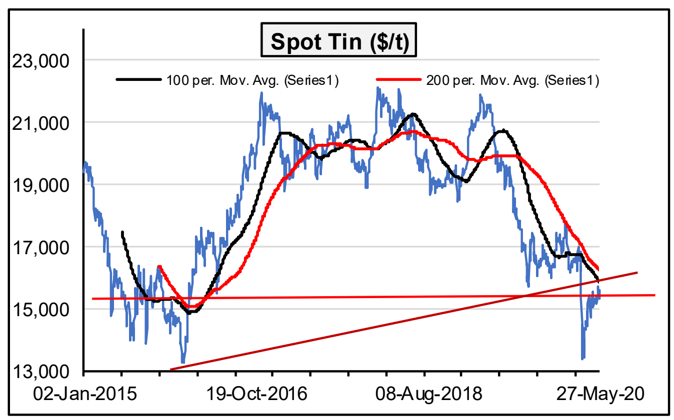


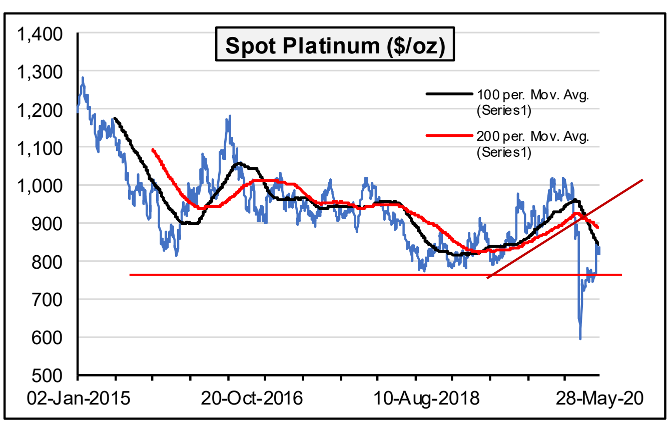


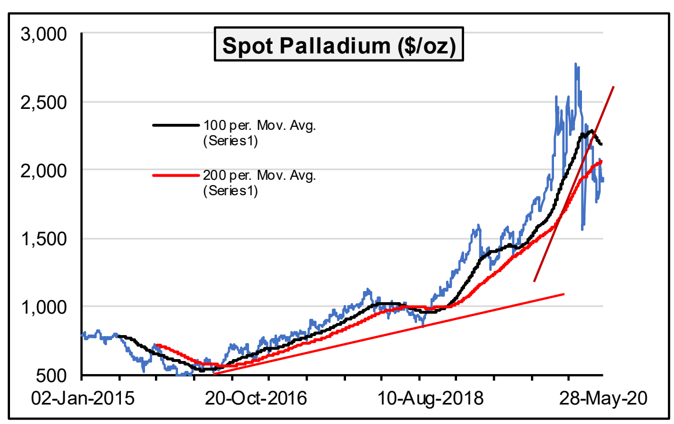












Source: LME, LBMA, LPPM

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