Investment Weekly

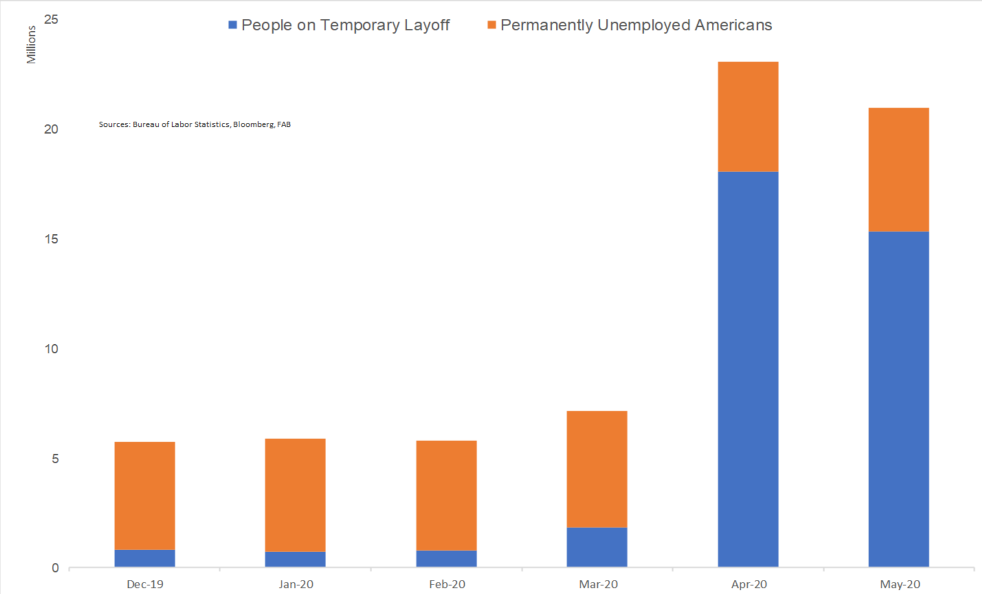
For inquiries related to this article, please contact:

Alain.Marckus@bankfab.com
Christofer.Langner@bankfab.com

7 June, 2020

Some Americans return to work, but millions remain jobless

- **The headline jobs figure on Friday indicated a 2.5-million increase in the number of employed Americans.**
- **That, however, was boosted by 2.7 million people being called back to work from furlough.**
- **Markets are optimistic that the worst in terms of headline unemployment may be in the rearview mirror.**
- **The indications are that US stimulus programs, particularly the Paycheck Protection Program, are working.**
- **The extent of the recovery depends on how many more go back to work, and what the unemployment rate is once the Paycheck Protection Program runs off next month.**
- **Ultimately, though, a considerable wall of cash and stimulus programs continue to support risk assets.**
- **The FAB AAC remains underweight in global equities and overweight gold.**



Last week brought evidence that some of the US government programs are working. The nonfarm payrolls report on Friday surprised positively, as it showed that 2.5 million Americans had gone back to work, whereas the consensus estimate was for the monthly survey of the Bureau of Labor Statistics to show that 7.5 million had lost their jobs. Markets rallied hard on the back of this economic data, with the Dow Jones Industrial Average ending Friday up by 3.15%, capping a week when it gained 6.8%. The index is now 9% away from its record. The NASDAQ Composite index, meanwhile, is up 9.4% for the year and a fraction below its all-time closing high.

The positive surprise, however, seems to be in large part a result of the Paycheck Protection Program. The initiative offered loans which could become grants to companies that kept their employees on payroll. The program channeled through the Small Business Administration (SBA) offered low cost loans to small companies and forgave them as long as the money is used for rent, mortgage costs or utilities, with the employer keeping its workers on the payroll for eight weeks. The SBA had approved US$555 billion of such loans as of last week, or 83% of the US$670 billion allocated to it.

The evidence that this particular program was a big driver for the unexpected job gains is in the details of the nonfarm payrolls survey report. The 2.5 million new jobs is very similar to the 2.72 million drop in the number of people who were identified as being in a temporary layoff. Unfortunately, however, the total number of people permanently jobless rose by 295,000 to 2.3 million.

While some of the furloughs have been reversed, more people lost their jobs in the US

Put simply, many companies have started to reverse their furloughs as business reopens, but many continue to lay off their employees or simply close their doors.

Bankruptcies tend to lag in economic crises, with many still expected to come in the US. At least one big chain filed for bankruptcy protection every week of May, ranging from car rental company Hertz, to retailer JCPenney. While bankruptcy protection does not necessarily mean a company will cease operations, many do not survive after the filing. Larger companies have a better chance of doing so, but the odds for the smaller ones are slim. And the number of small companies filing for bankruptcy was already on the rise before the advent of Covid-19.

This helps explain why Federal Reserve economists still expect the year to end with the US unemployment rate at more than 10%, compared to 3.5% in February. After the 2008 crisis, it took seven years for the unemployment rate to recover to where it was before the recession.

Still, one thing seems clear: the worst of the economic slump is in the rearview mirror. That helps explain why the equity market is on a tear. Stocks usually pre-empt the economic performance, at least on the face of it they seemed to have far better predicted what the jobs report showed than economists' expectations (not a single one of those surveyed by Bloomberg came even close to the number reported).

The question now becomes how long it will take to bring the global economy back to where it was before the pandemic-driven lockdown. After the 2008 crisis, juiced by unprecedented stimulus, the US economy created about 1 million jobs a year. If, once the temporary layoffs are cleared from the data, five million jobs are lost in the US, it could take five years to create them again, using that as a measure.

Having so many people out of work impacts consumption. Disposable personal income data for April increased 12.9% mostly driven by stimulus checks sent to Americans that month, according to data from the Bureau of Economic Analysis. Those checks are not coming this month, however, and that could continue to impact retail sales, which have already seen record drops in both April and March.

This is one of the ways that company bottom lines could be hit by the current recession. The number of people unemployed in the US has an impact on the sales of companies in the S&P 500. In the 2008 crisis, for instance, revenues of companies in the index fell by 12% as the unemployment rate rose to 10% from 4.5%. This time, the unemployment rate has risen to 13.3% from 3.5%. If revenues are to drop by a commensurate amount, they could fall more than 20%.

This is one reason why the market looks expensive. The FAB Asset Allocation Committee has remained underweight in equities. Right now, the S&P 500 trades at 2.3 times the sales per share of its constituents over the past 12 months. In simple terms, it would take 2.3 years of the previous year's sales to pay back the aggregate market value of the stocks in the index. That is a high number.

The highest that ratio has been is 2.32. Hence if the aggregate sales of the companies in the index were to remain unchanged, the S&P 500 would be at an all-time high according to this measure if it rallies another 1%. That does not mean that it cannot go higher, even a lot more than that, in the weeks ahead. The risk-free interest rate is close to zero and that alone supports higher valuations. The previous period of zero rates in the US increased the average price-to-sales multiple by 0.2.

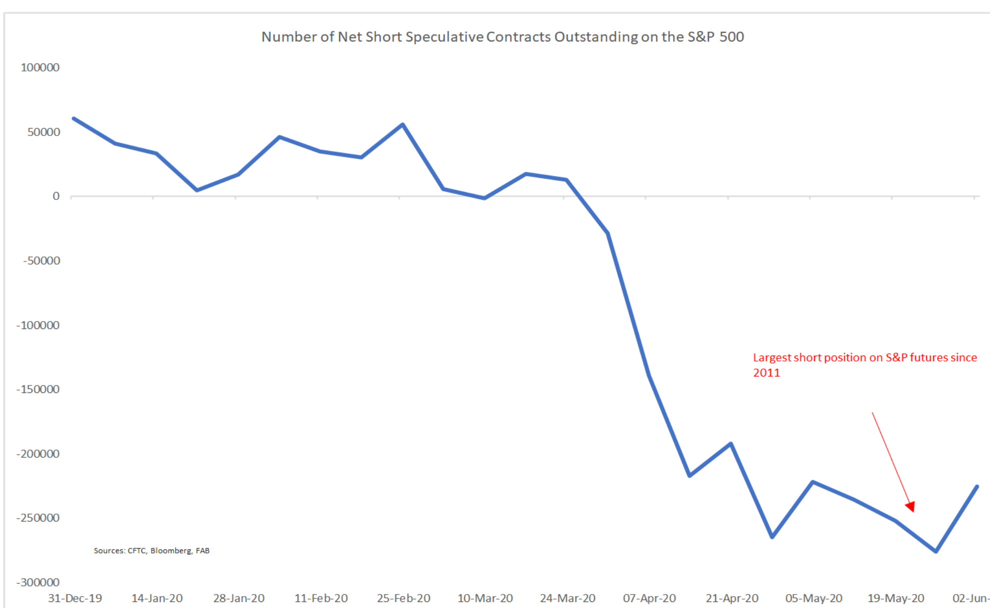
Since the March sell-off, equity funds have raised their average cash level to nearly 6%, according to Bank of America Merrill Lynch, the highest since 2008. That historically-high cash level has also been reflected in money market funds' assets under management, which have increased by about US$1.2 trillion in the past three months, to US$4.8 trillion. Much of that cash has to be deployed over time, and it seems as though some important technical barrier breaches being breached are emboldening fund managers to do so.

Hedge funds with large speculative shorts on stocks have been forced to buy

Having so much cash on the sidelines should put a floor under any potential downside, and many managers may actually be waiting for the next sell-off to put some of it to work.

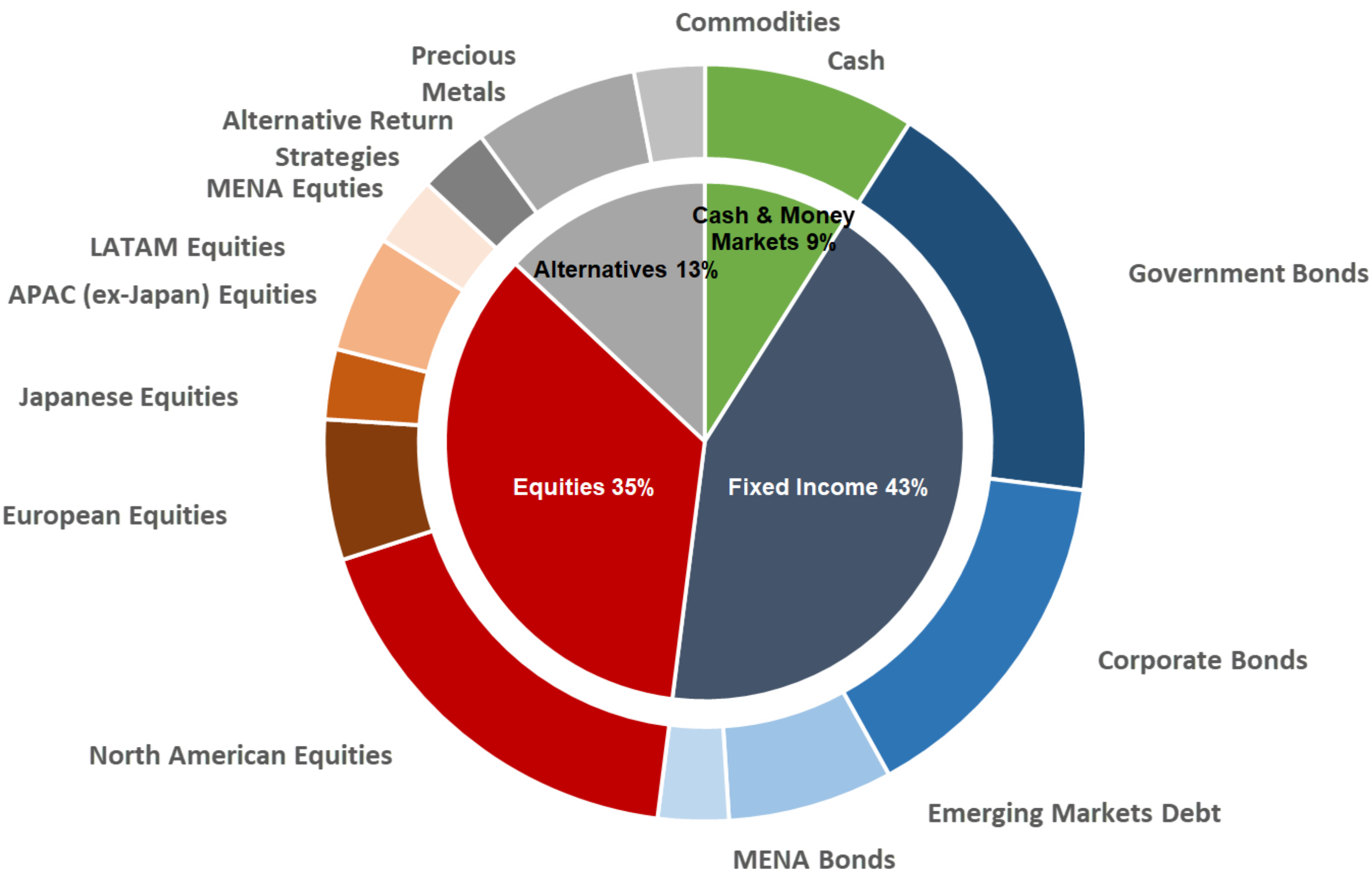
On the flip-side, hedge funds seem increasingly convinced that the market cannot continue to be so disconnected from the real world for much longer. Commodities and Futures Trading Commission data last week showed the largest speculative short position in S&P 500 futures contracts since 2015. That, may support another leg up in US stocks. If the market rally continues, those short positions will become even more painful and will have to be covered.

Eventually, however, after the cash is deployed and the speculative positions are closed, investors will still have to cope with the reality of the latest new normal. Until then, even if it seems irrational, the rally may yet continue for longer.



Investment Weekly

Current Tactical Asset Allocation



Asset Class	Positioning	Detail
Cash	Overweight	After taking profits on some equity positions.
Fixed Income	Overweight	Keeping slightly overweight focused on EM dollar debt and corporate investment grade bonds
Equities	Underweight	After taking profits on part of the US and European equity exposures
Alternatives	Underweight	However, overweight on precious metals specifically

Investment Weekly

First Abu Dhabi Bank

Disclaimer: *This report has been prepared and issued by Products & Services - Elite & Private Banking ("P&S-EPB") of First Abu Dhabi Bank PJSC ("FAB") outlining particular services provided by P&S-EPB. This report is for general informational purposes and does not constitute or form part of any offer or invitation to sell, or any solicitation of any offer to purchase or subscribe for, any shares in FAB or otherwise or a recommendation for a particular person to enter into any transaction or to adopt any strategy nor shall it or any part of it form the basis of or be relied on in connection with any contract therefore. Anyone proposing to rely on or use the information contained in this publication should independently verify and check the accuracy, completeness, reliability and suitability of the information and should obtain independent and specific advice from appropriate professionals or experts.*

This report is provided on a confidential basis for informational purposes only and is proprietary to P&S-EPB. This report may not be disclosed to any third party or used for any other purpose without the prior written consent of P&S-EPB. The manner of circulation and distribution may be restricted by law or regulation in certain countries, hence any unathorised use or disclosure of this document is prohibited.

The information in this report reflects prevailing conditions and our views as of this date, which are accordingly subject to change. In preparing this report, we have relied upon and assumed, without independent verification, the accuracy and completeness of all the information available from public sources or which was otherwise reviewed by us. FAB PJSC makes no representation or warranty, expressed or implied, as to the accuracy, timeliness or completeness of the information in this report. FAB PJSC shall have no liability to the Customer or to third parties for the quality, accuracy, timeliness, continued availability or completeness of any data or calculations contained and/or referred to in this report nor for any special, direct, indirect, incidental or consequential loss or damage which may be sustained because of the use of the information contained and/or referred to in this report or otherwise arising in connection with the information contained and/or referred to in this report, provided that this exclusion of liability shall not exclude or limit any liability under any law or regulation applicable to FAB PJSC that may not be excluded or restricted.

Past performance is not a guarantee of future performance and should not be seen as an indication of future performance due to a variety of economic, market or other factors. The information contained in this report does not purport to contain all matters relevant to any particular investment or financial instrument and all statements as to future matters are not guaranteed to be accurate. Any projections of potential risk or return are illustrative and should not be construed as limitations of the maximum possible loss or gain. Data included in this report may not take into account all potentially significant factors, such as market risk, liquidity risk and credit risk. Undue reliance should not be placed on forward looking statements in making an invewstment decision.

In addition, our analysis are not and do not purport to be appraisals of the assets, stock or business of the recipient and has been prepared without taking into account the objectives, financial situation or needs of particular person. Even when this presentation contains a kind of appraisal, it should be considered preliminary, suitable only for the purpose described herein and not be disclosed or otherwise used without the prior written consent of P&S-EPB. FAB clients may already hold positions in the assets subject to this report and may accordingly benefit from the buying or selling of such assets as referred to in this report. This document does not purport to set out any advice, recommendation or representation on the suitability of any investment, transaction or product (as referred to in this document or otherwise), for potential purchasers. In receiving this report, the client is fully aware that there are risks associated with investment activities. Potential purchasers should determine for themselves the relevance of the information contained in this document and the decision to purchase any investment contained herein should be based on such investigation and analysis as they themselves deem necessary. Before entering into any transaction potential purchasers should obtain the investment offering materials, which include a description of the riks, fees and expenses and ensure that they fully understand the potential risks and rewards of that transaction (including, without limitation, all financial, legal, regulatory, tax and accounting consequences of entering into the transaction and an understanding as to how the transaction will perform under changing conditions) and that they independently determine that the transaction is appropriate for them given their objectives, experience, financial and operational resources and other relevant circumstances. Potential purchasers should consider consulting with such advisers and experts as they deem necessary to assist them in making these determinations.

FAB is acting solely in the capacity of a potential arm's-length contractual counterparty and not as a financial adviser or fiduciary in any transaction unless we have otherwise expressly agreed so to act in writing. FAB does not provide any accounting, tax, regulatory or legal advice. FAB is licensed by the Central Bank of the UAE.

London: *FAB London Branch is Authorized by the Prudential Regulation Authority. Subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from FAB London branch on request. Registered in England & Wales: Company No: FC009142: VAT No: GB245 3301 91.*

Paris: *FAB Paris Branch is licensed by the French Prudential Control Authority as a credit institution. FAB Paris is registered in France under the company number: RCS Paris B 314 939 547.*

Switzerland: *This publication is for informational purposes only and is not intended as an offer, or a solicitation of an offer, to buy or sell any investment or other specific product. Certain services and products are subject to legal restrictions and cannot be offered worldwide on an unrestricted basis and/or may not be eligible for sale to all investors. This report is for distribution only under such circumstances as may be permitted by applicable law. All information and opinions expressed in this document were obtained from sources believed to be reliable and in good faith, but no representation or warranty, express or implied, is made as to its accuracy or completeness. All information and opinions as well as any prices indicated are currently as of the date of this report, and are subject to change without notice. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. At any time the First Abu Dhabi Bank PJSC and/or FAB Private Bank (Suisse) SA may have a long or short position, or deal as principal or agent, in relevant securities or provide advisory or other services to the issuer of relevant securities or to a company connected with an issuer. Some investments may not be readily realizable since the market in the securities is illiquid and therefore valuing the investment and identifying the risk to which you are exposed may be difficult to quantify. Futures and options trading is considered risky. Past performance of an investment is no guarantee for its current or future performance. Some investments may be subject to sudden and large falls in value and on realization you may receive back less than you invested or may be required to pay more. Changes in foreign exchange rates may have an adverse effect on the price, value or income of an investment. First Abu Dhabi Bank PJSC and/or FAB Private Bank (Suisse) SA expressly prohibit the distribution and transfer of this document to third parties for any reason. First Abu Dhabi Bank PJSC and/or FAB Private Bank (Suisse) SA will not be liable for any claims or lawsuits from any third parties arising from the use or distribution of this document.*

Singapore: *First Abu Dhabi Bank P.J.S.C., Singapore Branch is regulated by the Monetary Authority of Singapore and holds a Wholesale Bank license.*

For more details relating the investment products, please refer to the Prospectus and/or offering document on https://www.bankfab.ae/en/invest

Please contact your relationship manager for information relating to subscription, redemption, dividends, client eligibility and/or any other information relating to the investment products.