

For inquiries related to this article, please contact:

Alain.Marckus@bankfab.com

Christofer.Langner@bankfab.com

12 April, 2020

Central banks go all out to fight recession

◆ US high-yield bonds see a historic rally after the Federal Reserve says it will begin to buy junk debt.

◆ The Fed announces a program to lend directly to small and medium-sized businesses.

◆ The Bank of England starts buying bonds directly from the government to fund the virus response.

◆ Regulators across the world relax rules to allow banks to lend more.

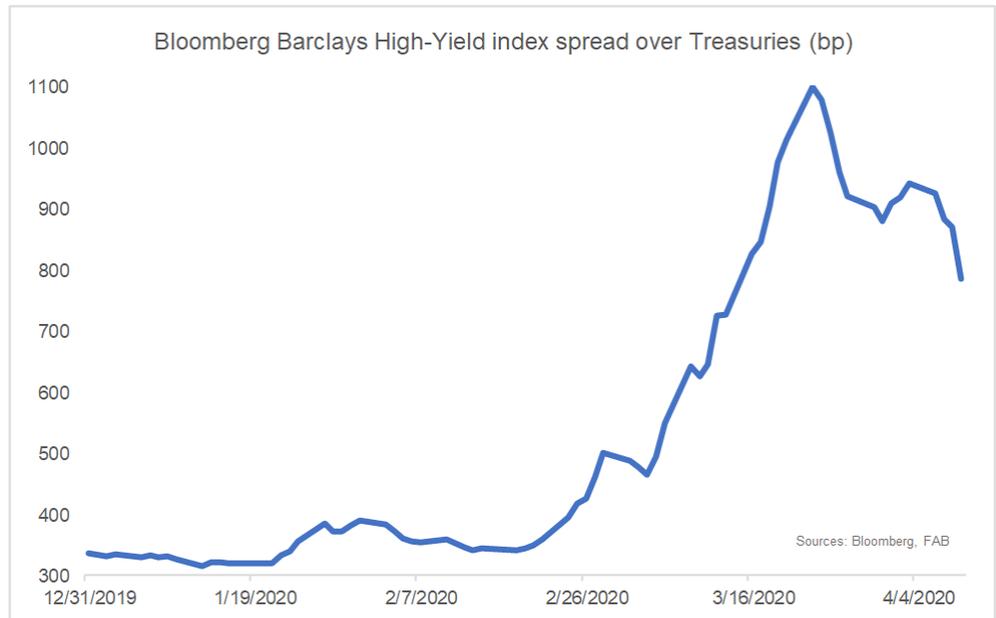
◆ More than 17 million American have filed for unemployment benefits in just three weeks.

◆ Abu Dhabi raises US\$7 billion in bonds and Dubai gets loan while it prepares its own bond deals.

◆ FAB AAC remains underweight equities and overweight gold amid continued uncertainty in markets

Central banks across the world are using every tool at their disposal to help steady the world economy pending the global lockdown being lifted in stages. The Federal Reserve on Thursday announced a new program to buy junk bonds that helped the Bloomberg Barclays US Corporate High-Yield index rally 3.1% that day, one of its biggest one-day rallies in the index's history. US bond markets were closed on Friday for a religious holiday.

The Fed's program is yet to start and will be broadly limited to higher-rated junk bond issuers, especially those that have recently lost their investment-grade status. Markets saw the intervention as a lifeline for the asset class.



The move comes after measures that showed the Fed and other central banks becoming increasingly aggressive in their efforts to stabilize financial markets. The US central bank had already announced unprecedented programs, such as buying corporate and municipal bonds, aside from new versions of other programs it had used in the 2008 crisis.

The result was indisputable. On 23 March, the average yield premium on the Bloomberg High-Yield index hit 1,100 basis points over US Treasuries, the highest since May, 2009. The Fed's forays into corporate bonds and now into junk brought that yield premium back down to 785 basis points on Thursday.

The central bank is not done, according to its governors. Last week's announcement is a program to lend directly to small and medium-sized businesses, Federal Reserve Vice-Chairman, Randal Quarles, said on Friday.

The Fed's entry into junk bonds helped reduce their yield premium further

In similar fashion, the Bank of England provided the UK government with an overdraft through which it will buy bonds from the UK Treasury. In simple terms, the BoE is printing money and giving it to the government in return for IOUs.

While that may draw criticism from many economists, it is hardly new. In fact, two years after the Bank of England had been created, in 1696, the bank issued GBP765,000 in new money used to buy government debt, with that sum backed by only GBP36,000 in collateral, according to Murray Rothbard. Inflation jumped in the decade after that, and the bank needed to intervene, historical data shows. The times are different, but the tool works the same way.

By 'printing money', the Fed and the Bank of England are increasing the supply of cash in the hope that an amount of it ends up with common people that need it in what is shaping up to be the worst global economic recession since World War II.

Indeed, while markets have seemingly been recovering from the March sell-off, in reality the jury is still out on whether they are truly out of the woods, especially given the economic data has become more dire by the minute. On Thursday, the US saw a third consecutive week of near-record weekly jobless claims. The Department of Labor revealed that 6.6 million Americans filed for welfare benefits in the week ended 4 April. As a result, a total of 17.2 million people in the US have filed for such benefits since the beginning of March.

To put that in perspective, during the 10 years to 31 January this year the US had created 22.5 million new non-farm jobs. One more week of more than 5 million initial jobless claims will have erased all the jobs the US economy generated in a decade. That spells out a deep recession.

Considering that every worker contributes a fraction of GDP growth, the 15% drop in people employed implies a commensurate drop in activity. A simple extrapolation would see US\$3.2 trillion less production in the US economy this year, or a nearly 15% economic contraction. Obviously it is not that simple, and the contraction may be far less severe by year-end. Still, the US is staring at its worst economic conditions since the end of World War II.

The Organization for Economic Co-operation and Development recently estimated that every month of movement restrictions reduces global GDP growth by up to 2 percentage points. Most countries are still grappling with when to lift lockdowns. Italy, for one, extended the closures to 3 May after new cases accelerated last week again, while the UK has no timeline to lift its own closures.

The extent to which that will impact stock markets will become more apparent

starting this week, as US and European companies begin to report first quarter results. Most of them have withdrawn profit and revenue guidance for the year, while many have canceled buyback programs and cut executive pay. In addition, further dividend cuts are to be expected in several sectors, which could fuel a further reassessment of the value embedded in the stock market right now.

As at 27 March, the dividend yield on the S&P 500 was at 2.35%, its highest since 2009, while the same metric for the European STOXX 600 stood at 4.1%, also the highest in nearly a decade. Those yields looked staggering when compared to benchmark bonds. The 145 basis points of additional yield offered by US stocks on that date was the highest such premium in the past 60 years, at least. From that standpoint alone, stocks should be unbelievably attractive, unless dividends are cut, which is likely to happen.

Perhaps for a timely read on the global economy, investors should watch the oil market instead. Brent crude prices are

down 52.3% this year, despite having rallied 36.8% last week alone on hopes that the OPEC+ group would reach an agreement to cut oil output by 10 million barrels/day. The accord was on tenterhooks over the weekend as Mexico refused to meet its output reduction quota, even after Saudi Arabia and Russia, two of the world's biggest producers, accepted the size of the cut proposed.

Without that agreement, oil prices could be looking at a further significant drop. Spot prices for Brent oil for delivery in Europe was already at US\$26.3/barrel on Friday, 11.9% down on the week, while the nearest futures contract on the same quality of crude was at US\$31.48/barrel.

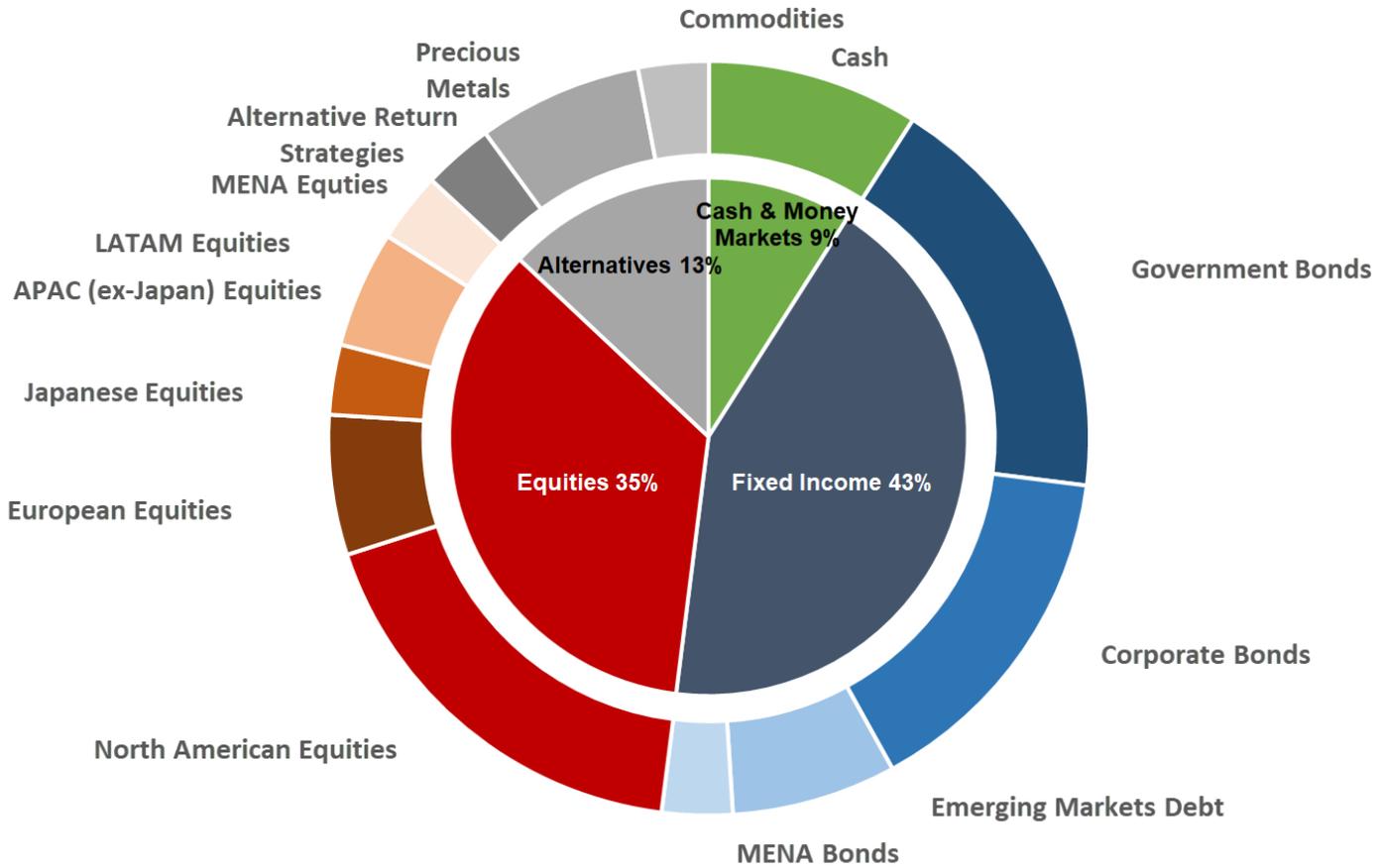
Investors must remember that some of the most impressive rallies can be seen during bear markets, and most analysts are still attempting to come to grips with the extent of falls seen until a few weeks ago.

The extent of the bounce seen since then, and in the face of such dire economic metrics, suggests that caution should remain the watchword for the time being. It is encouraging that global financial authorities have been prepared to throw such huge amounts of cash at the collective problem. The question, however, is just how much of that cash will stick.

One month of lockdowns probably erased all the jobs created in the US since 2010



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

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 unauthorised 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 investment 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 risks, 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.