Investment Strategy Update

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GCC countries sell bonds as oil, credit markets recover

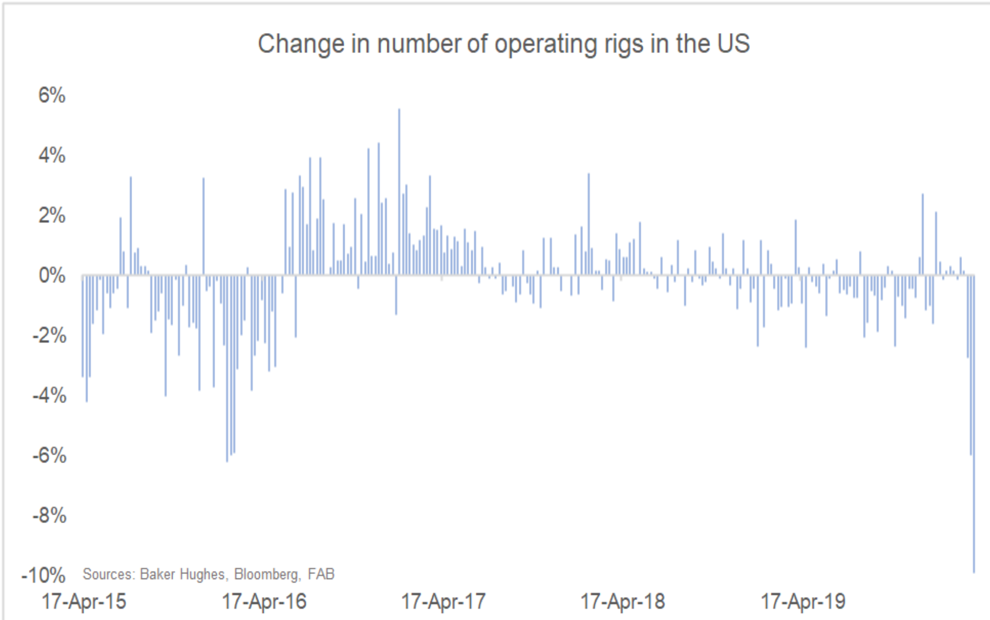
♦ Gulf sovereign bonds find strong demand as they reopen credit markets in the region.

♦ Oil prices also find some footing as investors weigh impact of US production drop and prospects of an OPEC output cut deal.

♦ Virus news, however, remains sad, with deaths increasing in developing nations and in New York.

♦ The French Central Bank also estimated that the country's economy will shrink 6% in the first quarter, with every week of closure shaving off 1.5 percentage point of growth.

♦ FAB AAC remains underweight in equities and overweight in gold.



Gulf Cooperating Council countries were taking advantage of the reopening of credit markets with a couple of sovereign bond transactions that were finding very strong demand. Investors seemed to be taking up the bonds of highly-rated countries in the Middle East as they offered much better yield premiums than they would have just a few months ago.

The demand for the region's bonds was also getting a boost from speculation that oil prices may be finding a floor. The expectation was that the OPEC could agree to cut output in a meeting expected to happen tomorrow. One of the points in the way of the deal was OPEC's request that the US also cut output. That issue, however, may have been mitigated as the US Energy Information Administration (EIA) cut its forecast for US production this year by 1 million barrels/day. That would hardly make a serious dent to the 13 million barrels/day that the US currently produces, but it may be a starting point.

In any event, there are clear signs that US production is falling fast. The number of rigs operating in the country fell by 56, the steepest weekly drop since 2014, according to data provider Baker Hughes. That came a week after the Dallas Fed manufacturing activity index dropped to minus 70 in March from a positive number in February, indicating that oil and gas companies are closing their doors in the US's biggest energy producing state.

Yet, even if the OPEC and the US reduce output by the amount being envisioned, the oil glut remains significant. The EIA recently said that demand had fallen by at least 20 million barrels/day since the Covid -19 pandemic started. The drop has been reflected in overflowing storage tanks, with data provider API reporting yesterday that US crude stockpiles had increased by 11.9 million barrles in the week ended 1 April.

Last week saw the biggest drop in the number of US operating oil rigs since 2014

The broader Department of Energy data will be out later today and could show inventories reaching 480 million barrels.

Such buildup is not surprising amid the worst economic slowdown since World War II. France gave evidence of how bad it is as the Central Bank indicated it expects the country's economy to shrink 6% in the first quarter. It also calculated that every week of lockdown shaves off 1.5% of GDP growth. Factories in the country were operating at 56% capacity, the lowest utilization rate since the 1940s. With death rates still soaring in New York and in other countries, it remains unclear when countries will emerge from the lockdown. Until economic activity returns to normal, oil demand will lag.

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