Investment Strategy Update

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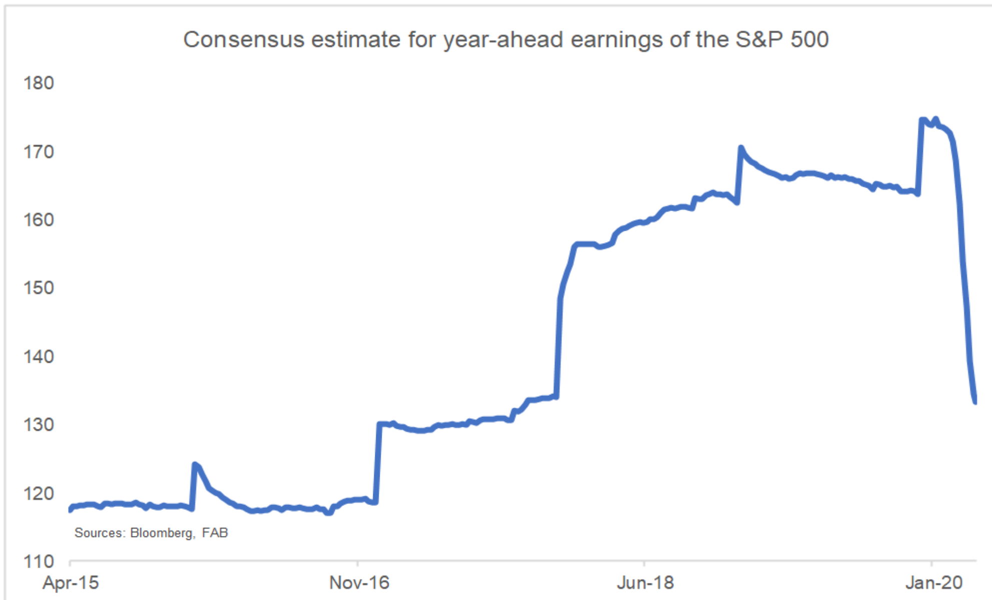
Stock market stages a comeback after worst day in three weeks

- **Stocks in Europe and Asia rallied today and US futures pointed at a stronger open.**
- **Gold gets back on gaining path after a small correction yesterday.**
- **Yield premiums for riskiest bonds, however, continues to rise as investors brace for rising defaults among smaller oil producers.**
- **Brent crude continues its descent as it catches up with West Texas Intermediate.**
- **FAB AAC remains underweight in equities and overweight in gold.**



Stock markets were taking a breather today after US equities had their worst sell-off in three weeks yesterday. Futures contracts for the S&P 500 were in the green, as were most European and Asian indices. Gold prices were also rising after having dropped marginally yesterday, while the yield on the 10-year US Treasury increased 1.4 basis point.

The signs of renewed risk appetite are happening in spite of the continued rout in oil prices. Brent crude was down 8.4% as of 13:30 in Dubai, trading at US$18.4/barrel, and 46% below the US$34.1/barrel at which it was traded on 3 April, when OPEC agreed to cut their output to deal with slower demand across the world.

The recent rout in oil prices (with one contract negative for the first time), was probably partly behind the stock market and gold price drop seen in the past two days. The sell-off could have triggered margin calls for some investors, who sold other assets to meet them.

The fact that markets are bouncing today, therefore, suggests any such leveraged positions may not have been so big to prompt a further correction. Investors also seem to be taking heart of the increased news flow suggesting that more countries are looking at lifting their lockdowns and restarting their economies.

Germany started to reopen some venues and signaled that it may even restart the Bundesliga football matches next month as cases dwindled. Italy is expected to unveil a detailed plan for its own reopening this week. Meanwhile, in the US, a growing number of protesters have taken the streets to ask states to lift quarantines, prompting hopes of a reopening in the near future.

Investors also took heart from some earnings reports yesterday, especially of technology companies, which came in better than expected. To be sure, most of the companies reported worse numbers than forecast and many have withdrawn their guidance for the year as they grapple with what is shaping up to be the worst recession since World War II.

The consensus expectation for S&P 500 earnings has already fallen more than 23% this year

These earnings cuts have pushed expectations of earnings growth for stocks further down, with the consensus expectation now being that on average the S&P 500 will see profits drop 8.5% this year. In line with that, companies are also starting to cut dividends, with at least 165 of the components of Europe's STOXX 600 having announced they are reducing regular payouts to shareholders.

With so much potential bad news still to be weighed, today's bounce could be short-lived and investors should watch out for a follow-through before getting excited.

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