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Markets continue to cheer lifting of lockdowns

◆ Global stocks rise for a second day as investors continue to celebrate more news of reopening.

◆ The S&P 500 implied volatility index, the VIX, traded below 32 for the first time since 4 March.

◆ Brent crude recovered after plunge driven by ETFs shifting their exposure to longer-term futures contracts.

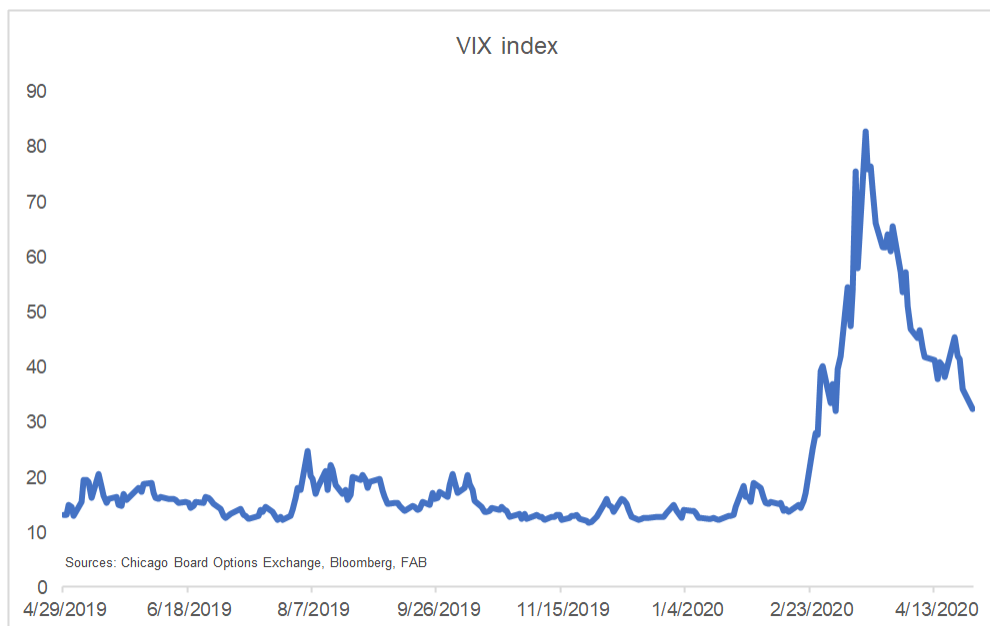
◆ Libor rates move closer to their historical relationship with the Fed Funds rate.

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

Stock markets were rising for a second consecutive day this week, and pushing some indices to the highest since early March as investors cheered more news of a gradual lift to the lockdown of several major economies.

Spain and France are set to announce plans to ease the social distancing measures as early as today, while New Zealand allowed factories and construction sites to resume work. This came one day after US President Donald Trump unveiled a strategy to expand testing in the country. Meanwhile, the number of new infections in Germany fell below 1,000 for the first time in more than five weeks.

Investors are now trying to glean how the recovery will be. They are also showing signs of optimism that the world economy will pick up speed driven by record stimulus, despite the bad current numbers. This comes as unemployment across developed economies reaches the highest since World War II.



Consumer and business confidence measures for Europe continued to plumb new lows and a report by the Dallas Federal Reserve yesterday showed manufacturing activity at -73 in Texas, the lowest since the institution began to publish the index.

While that is bad news for the second largest state economy in the US, it probably offers some support to oil prices. The steep drop suggests the main driver of activity in Texas, energy, is ailing.

Indeed, the number of active oil rigs in the US has dropped 45% since the beginning of March, according to Baker Hughes. That suggests a drop of more than 2 million barrels/day of output and may help the recovery in oil prices. Brent crude was up 2% today after dropping 6.8% yesterday, when it was pulled down by a 24.6% drop in WTI crude. The latter came under pressure as large funds sold their near-term futures positions.

The VIX broke a key technical barrier and approached levels closer to its historical normal

More importantly, the CBOE VIX index, which measures the expected volatility in the S&P 500, traded briefly below 32.00 for the first time since 4 March. Such a level remains high compared to the 15.13 average of the five years preceding 31 December 2019, but it is a very significant improvement compared to the 82.69 closing high of 16 March.

The issue is the risk-reward of adding positions now. The MSCI World index has rallied 26.2% since its 23 March low and is now 14.3% below where it started the year. The outlook for earnings, however, has shifted materially since the beginning of the year, suggesting the upside is limited. The potential downside if there is a negative surprise, however, is significant.

Investment Strategy Update

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