PICTET
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Conference Call
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Pictet Trading & Sales, Trading Strategy

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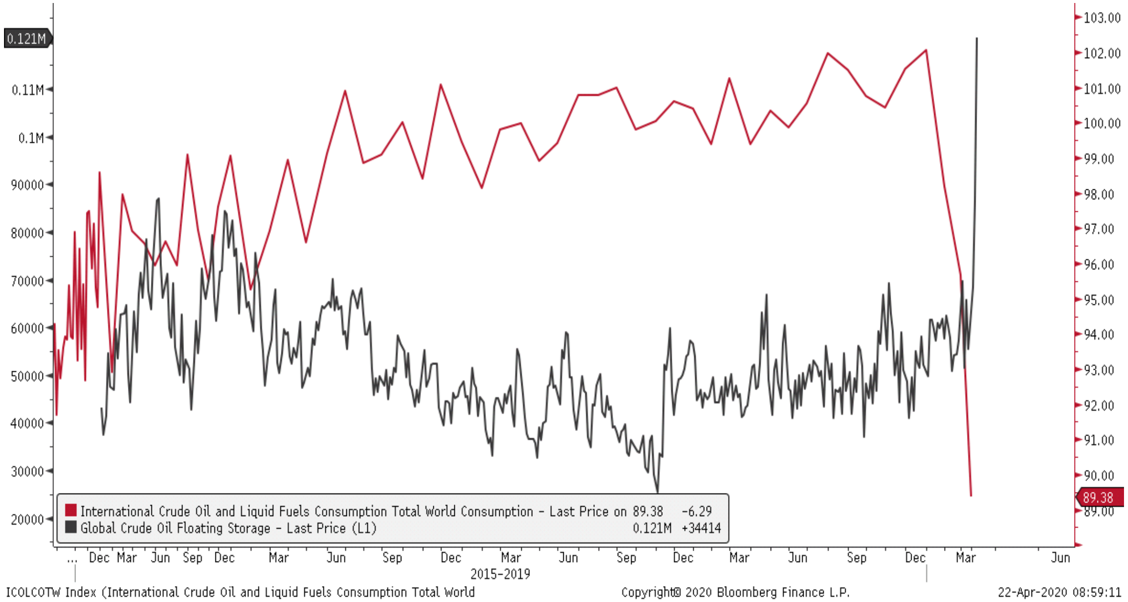
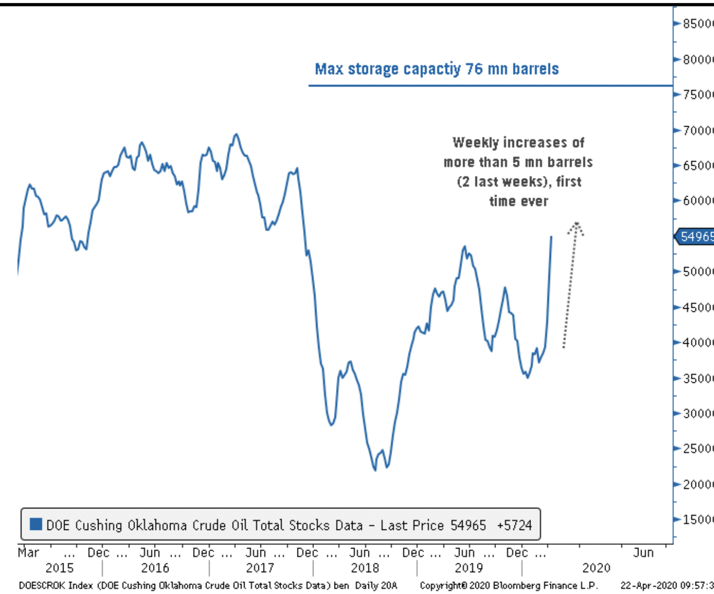
When the world stays at home, it does not need oil…

Global crude oil and liquid fuel consumption (red); crude oil in floating storage (black) and that at Cushing Oklahoma (blue)



Source:, Bloomberg Finance L.P. Pictet Trading Strategy– as of 22/04/2020



Source:, Bloomberg Finance L.P. Pictet Trading Strategy– as of 22/04/2020

- The May 2020 WTI crude oil futures contract went negative the day before expiry this week, sending the price of oil below zero for the first time in history on a combination of technicalities and thin volumes;
- The fundamental problem behind this remains the lack of demand (see our recent letter on oil);
- OPEC production cuts will be effective from 1 May but are unlikely to meet the lack of demand. As we write, the latest OPEC conference call has not brought any subsequent agreement, but further production cuts look inevitable as storage capacity approaches its limits (especially in the US);
- The economic recovery will take time, as will a resumption in oil consumption: crude will remain under pressure in the coming months;

A gradual easing of restrictions means a slow re-start

- According to Johns Hopkins University, the worldwide number of Covoid-19 cases has passed 2.5 million, and it has killed more than 184,500;
- Some European countries are beginning to ease lockdown measures (definitions vary); with others still in lockdown and considering in May;
- EU officials have set out recommendations for ending lockdowns and have asked governments to take a **gradual and coordinated** approach to reopening.

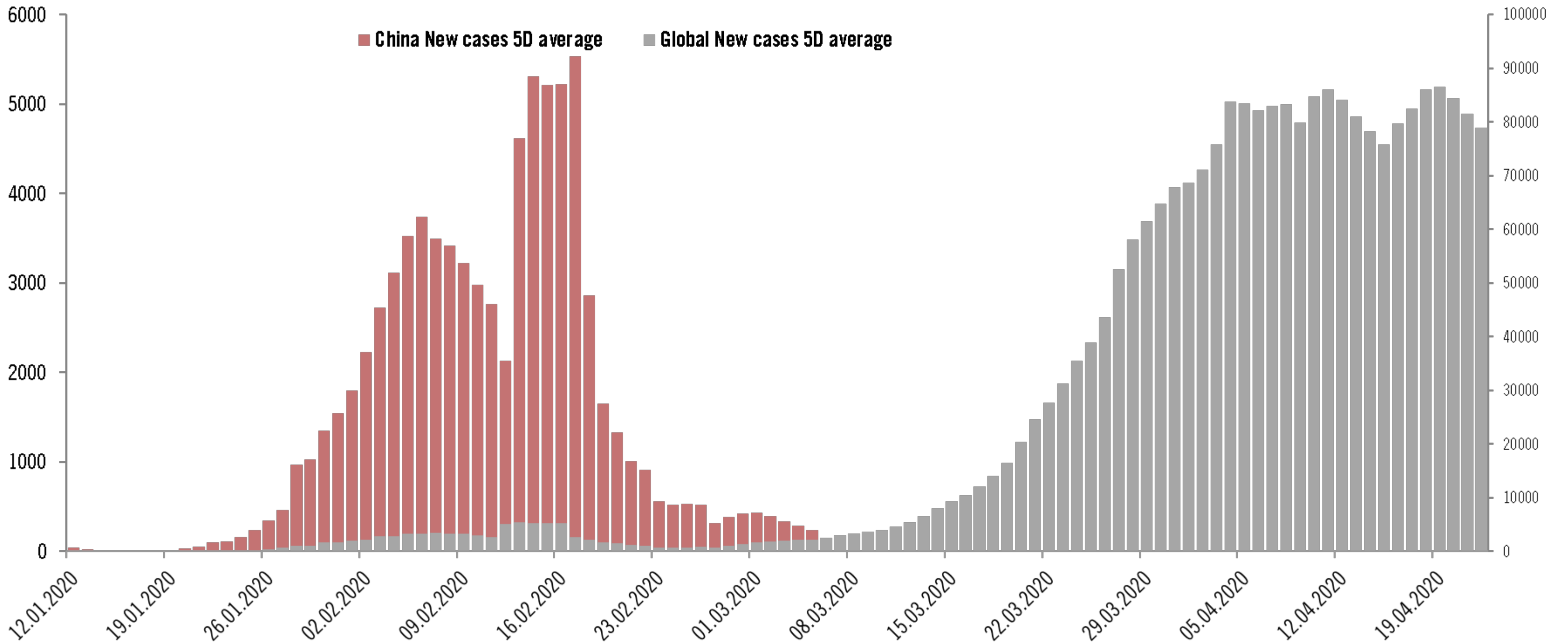
EASING RESTRICTIONS – A DELICATE BALANCING ACT

- **China (lockdown of Wuhan 23 January – followed by other cities) -** Lockdown lifted 8 April although some restrictions remain;
- **Europe – non-essential travel banned 16 March for at least 30 days,** further coordination under discussion;
- **Italy (lockdown 9 March): EASING.** Gradual re-opening planned for **4 May**; yet bookshops, laundries, stationery shops and children's clothing can reopen (some regions have decided to hold-off). Conte has said more plans will be released at the end of this week;
- **Spain (lockdown 14 March): LOCKDOWN.** Some factories and construction sites have already re-opened – but lockdown now extended to **3 May**;
- **France (lockdown 16 March): LOCKDOWN.** Measures extended to **11 May**, at which point schools could gradually reopen but restaurants would stay closed;
- **Germany (lockdown 20 March): EASING.** Restrictions extended to **3 May**, but some smaller shops and small businesses re-opening; schools to gradually re-open from 4 May. Large gatherings banned at least until 31 August;
- **Austria (lockdown 17 March): EASING.** Has opened garden centres, DIY stores and small shops; more to open from **1 May;**
- **Denmark (lockdown 11 March) EASING.** Schools gradually reopening; next date **10 May;**
- **Switzerland (lockdown 17 March) EASING.** A three-phase re-opening 27 April (some small businesses), then 11 May (compulsory schools, shops and markets) and 8 June (upper schools, leisure establishments); timetable to be reviewed 29 April;
- **UK (lockdown 23 March) LOCKDOWN.** Measures not expected to be lifted until early May if not later that month;
- **US**: Governors in Georgia, South Carolina and Tennessee have announced plans to ease; President Trump says he will temporarily suspend the issuance of green cards;

Source: Government authority press releases; definitions vary; all are subject to change.

The pandemic situation: a lasting peak?

Covid-19: Number of new cases: 5D daily averages (Global in grey, China in red):

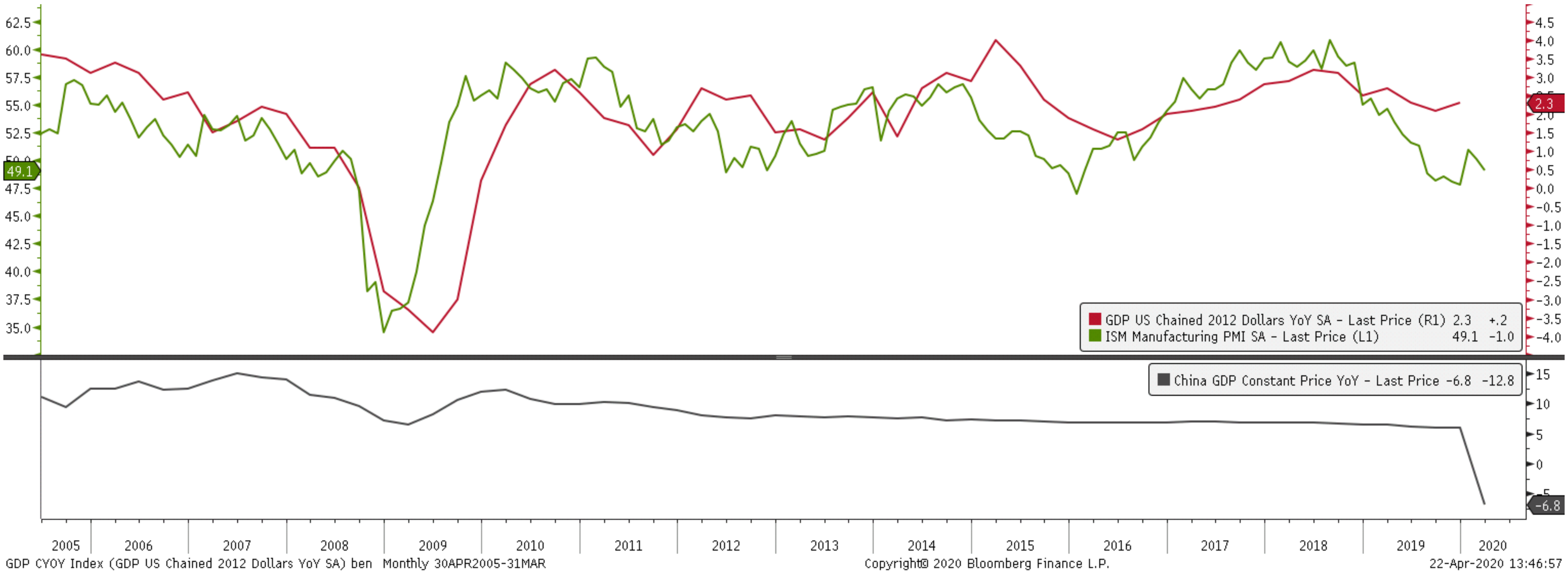


Source: John Hopkins, Bloomberg Finance L.P. Pictet Trading Strategy– as of 23/04/2020

- Global cases of Covid-19 have now topped 2.5m with more than 184,500 fatalities worldwide;
- The number of new cases reported daily has now stabilized (flattening of curves), yet the absolute number of new cases is yet to start to decrease (i.e. “this might be the end of the beginning but it is not yet beginning of the end”;
- In the US, the situation has eased in NYC but most states are lagging (with cases growing in Michigan, Illinois and California to name a few)S;

The macro picture: “There will be blood…”

US GDP growth YoY % (red), ISM manufacturing (green) and Chinese GDP growth YoY % (grey):



Source:, Bloomberg Finance L.P. Pictet Trading Strategy– as of 22/04/2020

- China is likely to provide an indication -once again- on the degree of GDP contraction that will occur during H1 2020. There the pandemic was at its worst in Q1, when GDP contracted -6.8% YoY;
- On 14 April the IMF revised its 2020 GDP forecast sharply lower: global GDP is now expected to contract -3% in 2020 (-5.9% for the US, -7.5% for the Eurozone and 1.2% for China);
- For most developed economies (ex. China), the pandemic effect is likely to be felt worst in Q1 and Q2, with the sharpest contraction in GDP expected in Q2. Recovery should start end of H1 but will be slow;

The US 10-year Treasury yield is capped

Technical chart: US 10-year Treasury yield: long and short-term*

Source: FactSet – Pictet Trading Strategy - as of 22.04.2020 *criteria explained in the endnotes
The target price presented in the chart is based upon chart analysis. This is not the product of any Pictet financial research unit.

- No macro drivers for a sustainable pick-up in yields (depressed growth expectations);
- Central banks are cutting interest rates and are unlikely to change policies in the short-term;
- US inflation is low: CPI YoY is down at 1.5% (from 2.5% in January), CPI core is at 2.1% and core PCE is at 1.8%. The drop in consumption unlikely to boost prices and crude prices are likely to remain under pressure for several months: even with massive central bank intervention we expect this crisis to be deflationary (in the short-term at least);
- Rising government indebtedness is unlikely to be sustainable with higher interest rates;
- Looking at the technical chart, the break below 1% sent a solid bearish signal, and attempts to bounce back have failed. On the short-term chart, the upper band of the downtrend channel marks a significant resistance at around 1.5%.

Diverging fortunes in Europe

Relief rallies in European equity indices have diverged

Region	YTD perf	Perf since bottom	Retracement 2020 top	Distance to its 200d SMA	RSI	Current PE	10-year median	Diff vs average	2020 EPS revisions	2020 EPS growth
Germany	-24.0%	25.7%	40.6%	-13.7%	54.5	14.1	12.4	13.5%	-25.1%	-15.4%
Spain	-28.3%	11.1%	17.1%	-23.9%	44.4	13.7	12.7	7.8%	-37.3%	-30.8%
Italy	-28.1%	13.4%	19.1%	-23.4%	42.9	11.0	10.7	3.3%	-30.9%	-26.0%
UK	-26.2%	22.2%	40.1%	-12.6%	56.9	13.5	12.6	7.0%	-28.3%	-24.0%
Eurozone	-19.1%	21.0%	33.8%	-16.9%	51.0	15.0	13.3	12.5%	-21.7%	-15.9%
World	-18.9%	25.9%	49.9%	-8.1%	56.7	17.4	15.6	11.7%	-21.0%	-13.4%
France	-27.3%	19.7%	31.4%	-18.6%	49.8	15.0	13.2	13.9%	-31.8%	-23.7%
US	-17.6%	27.0%	52.6%	-5.7%	57.4	19.1	15.5	23.8%	-20.0%	-12.7%
Switzerland	-10.9%	19.0%	49.9%	-3.7%	55.4	17.1	15.6	9.5%	-12.0%	-3.6%

Source:, Bloomberg Finance L.P. Pictet Trading Strategy– as of 21/04/2020

- Resilience during the selloff has generally been more significant than the strength of the rebound. To explain the YTD outperformance, the most significant criteria seems to be:
  - High quality / low financial exposure;
  - Financial strength;
  - Degree at which the pandemic affected the country;
- In this regard, the correction has exacerbated prior weaknesses and strengths:
  - Swiss, US and large-cap EU names more generally are among the outperformers: low death rate (Germany, Switzerland) / quality & financial strength (Switzerland and the US);
  - Italy and Spain have been lagging (high death rate & weaker fundamentals);

Seeking out defensive names

European equity indices (MSCI) sector breakdown (%)

	US	Europe	Germany	France	UK	Switzerland	Italy	Spain
Discretionary	10.3	9.7	15.9	20.5	6.0	3.1	15.1	10.4
Staples	7.8	15.9	3.5	12.5	19.7	27.6	0.0	0.0
Energy	2.8	5.2	0.0	6.5	12.0	0.0	11.1	4.1
Financials	10.6	14.8	15.9	7.9	17.7	13.6	29.7	23.7
Healthcare	15.7	17.1	13.7	10.0	14.3	40.0	0.0	3.4
Industrials	7.9	12.8	12.5	19.7	10.7	7.2	8.3	10.5
Technology	25.4	7.0	15.9	6.5	1.3	0.6	0.0	7.4
Materials	2.4	7.2	8.5	5.9	8.6	6.3	0.0	0.0
Real Estate	3.0	1.3	4.6	1.9	1.2	0.6	0.0	0.0
Telecoms	10.6	4.2	5.1	5.4	4.4	1.1	2.3	11.8
Utilities	3.5	4.8	4.3	3.1	4.1	0.0	29.8	28.8
Cyclicals	46.0	36.7	52.9	52.7	26.6	17.2	23.4	28.3
Defensives	40.6	43.4	31.2	32.9	43.7	69.3	32.2	43.9
Div yield	2.1	3.8	3.5	3.7	5.3	3.5	5.2	4.7

Source:, Bloomberg Finance L.P. Pictet Trading Strategy– as of 22/04/2020

- European indices are generally more defensive;
- Among most defensive: Switzerland, Spain and the UK;
- Among most cyclical: Germany and France;
- Italy has more defensive names than cyclicals but is overexposed to financials;
- See our recent daily letter on Europe again here.

European equity market ranking (from low to high)*

Country	Cyclicality*	Bank exposure*	Price mom	Fund flows	EPS mom	Value	Quality	Country rank
Switzerland	100%	83%	100%	83%	100%	0%	100%	1
UK	67%	33%	50%	100%	50%	83%	33%	2
Europe	33%	67%	83%	50%	83%	33%	67%	3
Germany	0%	50%	67%	33%	67%	67%	50%	4
France	17%	100%	33%	50%	17%	17%	83%	5
Italy	83%	0%	17%	17%	33%	100%	0%	6
Spain	50%	17%	0%	0%	0%	50%	17%	7

Source:, Bloomberg Finance L.P. Pictet Trading Strategy– as of 22/04/2020

- Switzerland ranks first with its high quality, large defensive exposure, favourable momentum and stable fund flow;
- The UK benefits from a defensive stance and stable fund flows and is currently "cheap". But it is still behind the curve on handling the pandemic and faces other longer-term headwinds (Brexit). Some large defensive domestic names might be of interest;
- Large European defensive (and domestic oriented…) stocks are also worth considering;

Peripheral spreads have widened excessively

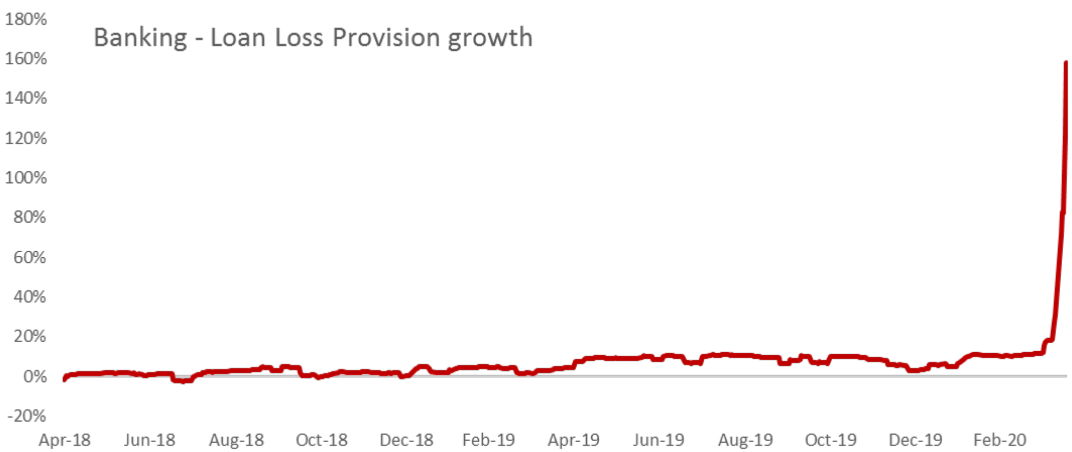
Peripheral spreads widening (10Y Italy vs Germany, black and 10Y Spain vs Germany, blue)

Source:, Bloomberg Finance L.P. Pictet Trading Strategy– as of 23/04/2020

- As we write, EU leaders continue to try and reach agreement on a clear, collective and collaborative response to the potential economic impact of the coronavirus, and this has driven peripheral spreads higher;
- While Italian debt sustainability, as well as rising Euroscepticism and associated political noise, are likely to remain key themes, we think short-term spreads should start narrow again because:
    - ➢ if EU leaders find an agreement on how to structure the funding of relief this will bring positive surprise; and
    - ➢ if they don't, the ECB is likely to step in more (and despite Lagarde's remarks at the beginning of the crisis);

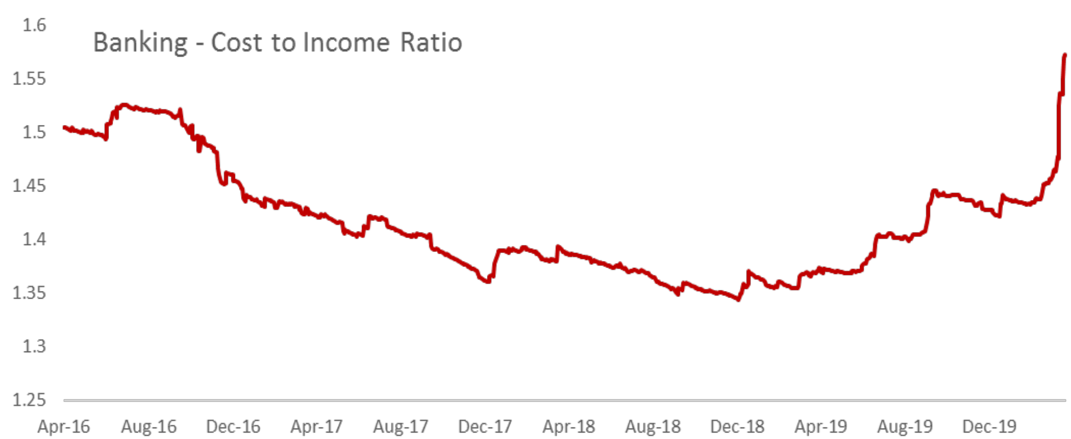
US Banks: falling profitability, and loan provisions…

S&P 500 Banks: loan loss provision growth YoY %



- Unsurprisingly, Q1 earnings showed a sharp contraction in net interest income;
- The main diversified banks have put aside huge cash reserves on fears of loan defaults (the 5 largest diversified US banks by market capitalisation (JPM, Bank of America, Wells Fargo, Citigroup, and USB Bancorp) are reported to have set aside around USD25bn;

S&P 500 Banks: cost-to-income ratio:

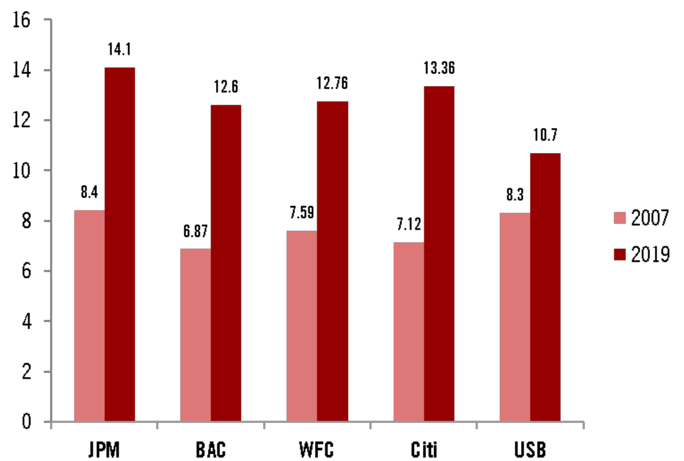


Source (both):, FactSet. Pictet Trading Strategy– as of 22/04/2020

- Cost-to-income ratios have jumped for most banks, showing the steepest increase since 2011, but they are still below 2008/2009 levels;
- See our recent letter on banks "A very real stress test";

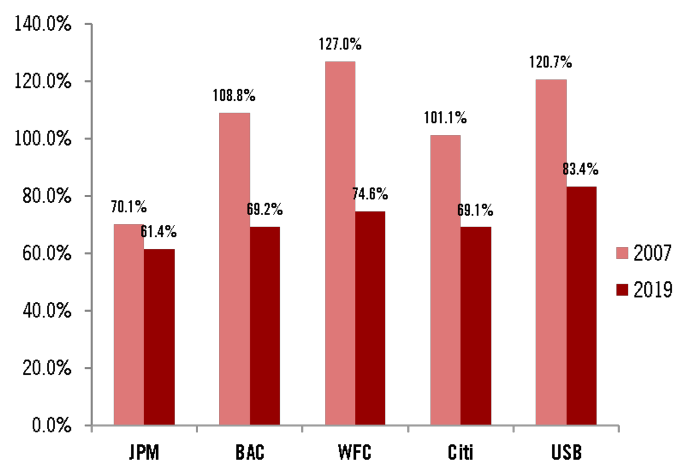
…but they are in much better health than they were in 2008/2009

Main US banks: Tier-1 Capital Ratio (2007 vs 2019):



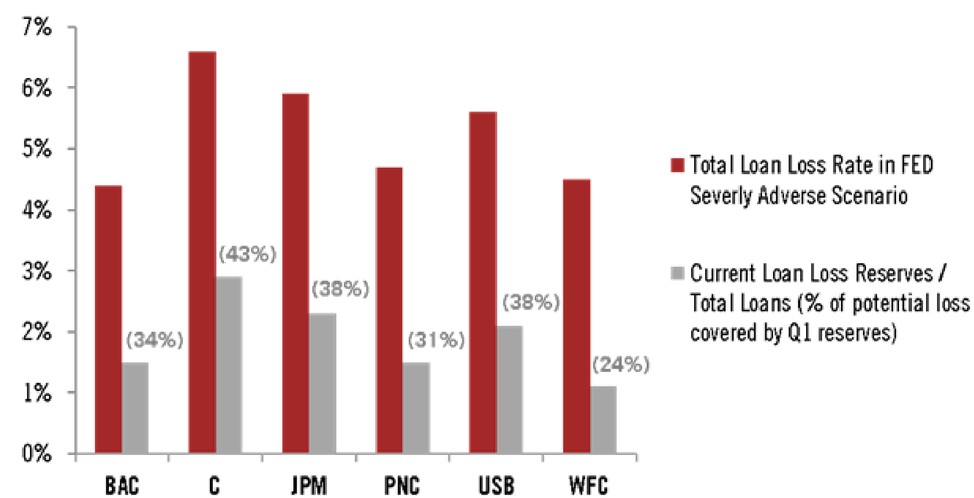
- While it is easy to hark back to 2008, the situation is different from the Global Financial Crisis: current circumstances have been brought about by an exogenous shock to global economic activity rather than by a systemic banking crisis;
- The GFC and subsequent regulatory requirements have made banks reinforce their liquidity and capital ratios. US Banks are also now much less leveraged now (see left charts);
- When looking at the Fed's 2019 "severely adverse stress test" (a scenario that could be not dissimilar to 2020) major banks have already raised reserves that would account for between 30% and 50% of potential loan losses See our recent study on US banks "A very real stress test";

Main US banks: Loan-to-deposit ratios(2007 vs 2019):



Source:, Bloomberg Finance L.P.. Pictet Trading Strategy– as of 22/04/2020

Loan loss rates under the Fed's "severely adverse" scenario 2019:



Key points

- The coronavirus pandemic may now be being brought under control, with evidence that curves are flattening (but not falling). “It might be the end of the beginning, but it is still not the beginning of the end”;
- The easing of lockdown measures is likely to be slow and progressive in Europe and this will limit the speed of the economic recovery. Crude oil is also an indicator on this (the historical negative price reached by US futures notwithstanding); demand remains key;
- Yields are likely to remain capped due to central bank policy and possible deflation (at least on the short-term) driven by slower consumption and lasting sluggish aggregate demand;
- We remain defensive regarding equity markets, with a preference for European large-cap names – particularly in Switzerland and also some domestic-oriented UK companies;
- While the crisis has exacerbated the ongoing challenges among the European periphery, (resurgence in euroscepticism, financial weakness…) we consider peripheral sovereign debt spreads exaggerated as we think the ECB is likely to step in more if needed (and EU leaders could surprise positively by coming to agreement over the structuring of relief);
- In the US, banks Q1 2020 earnings results show falling profitability and massive loan loss provisions. However they are much more resilient than they were in 2008 and we don’t expect a systemic banking crisis;

Endnotes: References for Trading Strategy publications (1/2)

Model performance data is not a reliable indicator of future returns

Model performance calculation has a number of limitations and the results do not represent the results of actual trading using client assets. The data provided is gross of fees and other commissions. Fees and charges will apply and will reduce the final return. No representation is being made that the model portfolios illustrated will or are likely to achieve results similar to those shown and there are often sharp differences between model performance results and actual results achieved.

The Equity quantitative grades

Growth Grade: The Growth Grade is a proprietary formula made up of earnings revisions momentum, past earnings growth, earnings stability, and current and long-term earnings growth. A grade above 55 is considered bullish on a 3-month basis, bearish below 45 and neutral between 55 and 45.

EPS Grade: The EPS Grade is a proprietary formula consisting of current and forward EPS growth, change and surprise data. An EPS grade above 60 or below 40 is considered predictive for future out/under performance.

Sales Grade: The Sales Grade is a proprietary formula made up of current and next year's sales momentum, past sales growth, sales stability, and current and long-term sales growth. A grade above 55 is considered bullish on a 3-month basis, bearish below 45, and neutral between 55 and 45.

Value Grade: The Value Grade is a proprietary formula made up of estimated P/E, P/B, P/S and P/CF ratios. 40% of the grade is based on historical values and 60% on current market data. A grade above 55 suggests a stock is cheap, below 45 expensive, and neutral between 55 and 45.

Quality Grade: The Quality Grade is a proprietary formula that focuses on the balance sheet (i.e. change in accruals, change in free cash flows and profitability). A grade above 55 suggests a stock with a good balance sheet.

Credit Grade: The Credit Grade focusses on the passive side of the balance sheet. It is divided into three sub-components to assess both short and long-term solvency. A grade above 55 suggests a strong capital structure, while a grade below 45 suggests a weak one.

Money Flow Grade: The Money Flow Grade is a proprietary formula that gives the accumulation/distribution based on the volume flows of a stock. A grade above 55 indicates good money flow and a grade below 45 suggests weak money flow.

Smart Sentiment Grade: The Smart Sentiment grade is a contrarian indicator based on investor positioning measures such as the days to cover ratio, the put call ratio, and the short interest ratio. A weak grade suggests 'too much' optimism.

Relative Strength (RS) Grade: The RS grade measures the price momentum of a stock over its 1-year price performance.

Global Grade: The Global Grade is a weighted average of the Growth, EPS Sales, Value, Quality, Credit, Money Flow and Smart Sentiment Grades.

The Regional MATRIX grades

The Regional Matrix grades range from -100% to +100%: We consider a grade above 50% to be very bullish, a grade above 25% to be bullish, and a grade between 0% and 25% to be neutral. A grade between 0% and -45% we consider bearish and a grade below -45% very bearish.

Regional Grade: The Regional Grade (-100 to +100) is an indicator of a structural bull market or not. It is calculated by combining and applying weight to each of the other grades that make up the Regional Matrix (Trend, Overbought/Oversold, Valuation, Liquidity, Economics, and Sentiment). If we believe equities to be in a structural bull market, we use 15 years of data to assess Valuation.

Trend Grade: The Trend Grade (-100% to +100%) is based on a moving averages model adjusted according to the overbought/oversold conditions of the region's main indices.

Valuation Grade:

The Valuation Grade (-100% to 100%) is based on the percentile rank of the regional Index stocks' P/E ratios since 1995 (current year estimated).

Economics Grade: The Economics Grade (-100% to 100%) is based on a combination of manufacturing and non-manufacturing PMIs and the Citigroup Surprise Indices. The Citigroup Economic Surprise Indices are an objective and quantitative measure of economic news and are defined as weighted historical standard deviations of data surprises (actual releases vs. Bloomberg survey median). A positive reading of the Economic Surprise Index suggests that economic releases have on balance beaten the consensus.

Sentiment Grade: The Sentiment Grade (-100% to 100%) is based on various contrarian and non-contrarian indicators.

Reversal date in the Trend: If the trend has reversed, we give the reversal date and indicate the direction of the reversal.

Endnotes: References for Trading Strategy publications (2/2)

Factor trends: We look at the performance of 5 theoretical long-short selections, each built around one of our quantitative grades (i.e. growth (EPS momentum), price momentum (RS), quality, sentiment and value), and each long the top decile and short the bottom decile of stocks within the respective region in our equity universe in terms of exposure to each specific score.

Model Long Only & Absolute return regional Allocation: The Regional Allocation shows the advised net exposure in total and per region. It is calculated by multiplying the MSCI regional weight by the Regional Grade (we use the structural bull market regional grade).

Trading Strategy Exposure: The Trading Strategy Exposure shows the actual net exposure in total and per region, based on our trades.

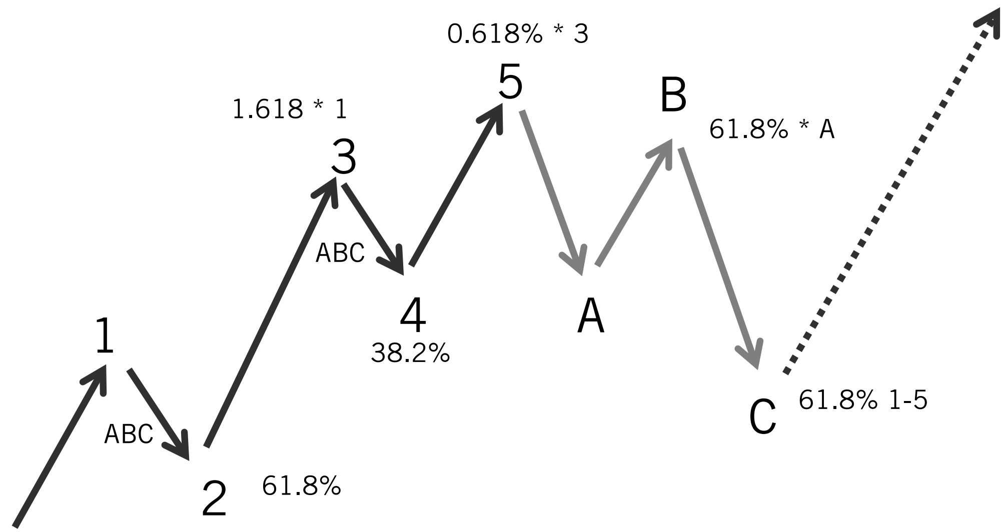
Time Horizon
Short-Term: 1 to 4 weeks
Medium Term: 1 to 3 months
Long Term: more than 3 months

PTS: Pictet Trading Strategy

Technical Analysis
The technical analysis used in this presentation combines traditional technical tools: graphical analysis (trend lines, support lines, continuation and reversal patterns) which determines the tendency, mathematical indicators (moving averages, RSI, MACD) used as numeric filters and Elliot wave theory which allows us to build a scenario with target levels and invalidation points.

Elliott Wave Theory
According to Elliott Wave Theory, markets move in impulse waves – with five sub-waves (numbered 1-5 or I-V) following the direction of the main trend, followed by three corrective sub-waves (A-B-C) (example below). These waves follow a set of specific rules and are linked to each other by target and retracement ratios based on the Fibonacci sequence, and the characteristics of each wave form an integral part of the reflection of the mass psychology it embodies.

Elliott Wave Theory



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