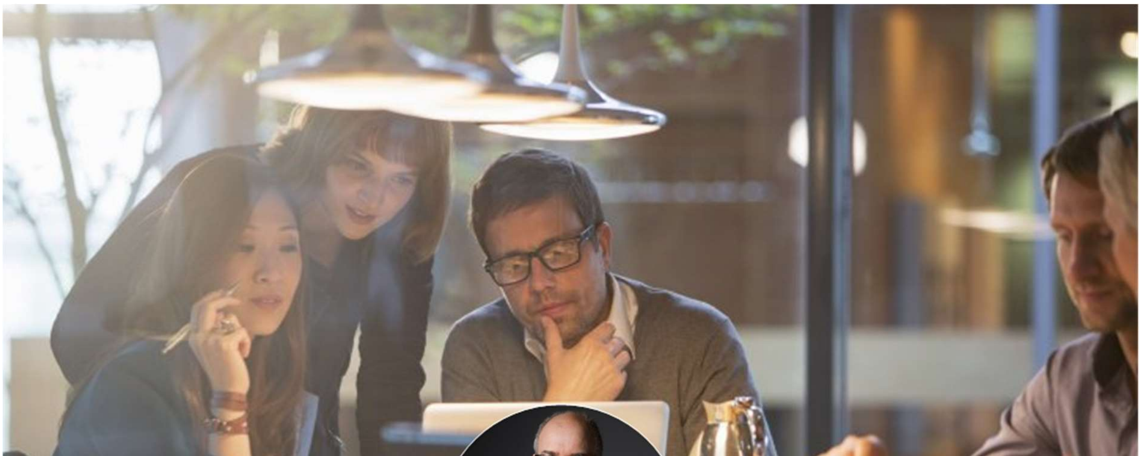
COVID-19: 30 MARCH UPDATE

30 March 2020



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IN A WORD:

There is huge uncertainty about the progression of the pandemic and its economic consequences. Market volatility remains significant. Last week stock markets recovered well overall, despite Friday's decline. This morning (30 March) equity markets are still on a downward path (-2% on the Eurostoxx, -0.8% on US futures).

The Covid-19 pandemic is an unprecedented health crisis for the past century. To date, there are 723,000 confirmed cases, 34,000 deaths and some 3 billion people in (more or less) strict lock-down depending on the country. In Asia, the peak of the health crisis seems to be behind us in the first countries hit by Covid-19. The number of new cases is tiny, and are imported cases from Europe or the United States, requiring new strict lock-down measures for those individuals. The risk of a second wave exists, and is being closely monitored by the authorities.

Europe is the current epicentre of the pandemic. Italy is the worst affected country in Europe, and the first to have implemented draconian lock-down measures three weeks ago. The figures for new infections and deaths are tragically high, albeit stabilising. Italy seems to be approaching a 'plateau', which suggests a decline that we hope will occur in the next few days. Italy is 8 to 10 days ahead of Spain and France in the spread of the virus. The peak of the epidemic in Europe is approaching, and could be reached around Easter.

In the United States, on the other hand, the epidemic is accelerating at a staggering speed. The World Health Organization fears that the United States will be the next epicentre of the epidemic, taking over from Europe. Lock-down measures are not in place everywhere, are decided by each State, and are often not harsh. The European case tends to show that only rigorous measures are effective after three weeks of lock-down. So we need to monitor the situation in the US because it is worrying.

Oil prices are at a 17-year low. The WTI is trading at $20.2, the Brent at $22.9 per barrel, respectively -5.8 and -8.2%. Year-to-date, the price of Brent crude has plummeted by 65%. The Covid-19 pandemic and the lock-down of some 3 billion people are resulting in an unprecedented drop in oil demand, of around -20%. At the same time, a price war has been declared. Saudi Arabia and Russia are seeking to gain market shares, particularly from the US, the world's largest producer owing to shale oil. However, the US shale oil business is not profitable at current prices. We therefore expect a drop in US production, and cascading bankruptcies in the shale oil sector. This sector accounts for 12% of the High Yield corporate bonds segment so the default rate in this market segment will need to be watched.

The decline in oil prices is a major event this year: it will have a negative impact on oil-producing countries but will benefit importing countries. We expect a rebound in oil prices in the second half of the year (around $45-55 for the Brent) along with a recovery in economic growth and demand for crude when the lock-down period ends. Meanwhile, production capacity will have been adjusted downwards. A more optimistic scenario: if producer countries stop their price war, prices would rebound earlier than expected.

Equity markets remain volatile and are likely to remain so until the uncertainty surrounding the pandemic disappears. This will obviously take time. The consequences of the pandemic are a sharp global recession, the duration of which is unknown. A particular focus will be on Chinese economic data, which will give an idea of the speed of the rebound. In early April, Chinese authorities will lift lock-down on Wuhan, the first region in the world to implement it.

In terms of earnings forecasts, the downward revisions are massive: the 'Citi Earnings Revision Index' is down 84% in Europe. The previous record dates back to October 2008 (-76%). The news is terrible, but is no longer a surprise to anyone.

In this negative context for growth and corporate profits, the economic stimulus policies are massive, in the United States, Europe and emerging countries, both in monetary and fiscal terms. These measures will take time to produce a positive effect. We detail these measures in the table.

<table>
<tr><th></th><th>Tax measures</th><th>Monetary policy measures</th></tr>
<tr><td>Germany</td><td>Easy access to short-term employment
Support for corporate liquidity through tax deferrals
State loan guarantees to the most vulnerable companies (€500 bn)
Development of existing guarantee systems provided through public bank KfW
Additional expenditure of €1 bn for the Ministry of Health
Increase in public investment in 2021-24 (€12 bn)
Additional fiscal package of €750 bn
€156 bn of new debt issuance to finance additional spending related to the crisis (debt brake temporarily lifted)
Funds of €600 bn with €400 bn of loan guarantees, €100 bn of the KfW and €100 bn of equity investments in companies</td><td rowspan="4">The ECB has taken strong measures similar to those taken in the 2008 crisis:
Increase in the bond purchase programme by €750 bn (6% of eurozone GDP) bringing the Pandemic Emergency Purchase Programme (PEPP) to €1.1 trn
The ECB lifted the limit of buying no more than 33% of a single country's debt
Purchase of Greek sovereign debt and short-term corporate bonds (commercial papers)
The ECB will accept loans from small and medium sized companies as collateral
Refinancing facility (TLTRO) for commercial banks (negative rate -0.25% or very negative -0.75%)</td></tr>
<tr><td>France</td><td>Subsidies for short-term employment
Late payment of taxes and social security contributions
Suspension of the new tax on the use of temporary contracts
Increase of loan guarantee schemes for SMEs (€300 bn)
Solidarity Fund for small businesses</td></tr>
<tr><td>Italy</td><td>Tax package of over €25 bn
Postponement of all tax payments until 31 May
Compensation of 60% of corporate property rental costs
Mortgage adjustment for the self- employed
Commercial loan guarantee scheme (measure not detailed to date)
Increased support for short-term employment
Household support for childcare
Debt repayment holiday
Support for the health care system (€1.5 bn)</td></tr>
<tr><td>Spain</td><td>Fiscal package of €17 bn
Tax and social security credits
State loan guarantees (€100 bn)
Debt repayment holiday
€3.8 bn in government support to the health care sector</td></tr>
<tr><td>UK</td><td>£30 bn fiscal package
£12 bn (0.5% of GDP) for targeted support measures (£5 bn emergency fund to support utilities, £7 bn of measures to help households and businesses)
£18 bn earmarked to longer-term measures to be implemented later this year
But also:
£20 bn of tax cuts and grants to corporates £330 bn of government-backed loans to corporates
Debt repayment holiday
£50 bn of additional measures:
-Take over 80% of the wages of workers whose jobs are at risk.
-Deferral of VAT payment for the next quarter (£30 bn)
-Unlimited 12-month interest-free loans for businesses
-£7 bn in additional social aid
-£1 bn in assistance to tenants</td><td>The Bank of England cut rates by 65bp to historical low levels (0.1%)
Increase of the bond purchase programme for £200 bn for a total of £645 bn
Support programme in the short maturity corporate bond market (CCFF)
Reduction of the countercyclical capital buffer rate to 0% for UK banks highly exposed to impacted borrowers</td></tr>
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USA	**1st fiscal package voted by the Congress (6 March) of $8.3 bn** for US health authorities (CDCP, PHSSEF and NIH) -**Emergency programme ($300-500 bn)** for the payment of employees on forced unpaid leave, sick leave and unemployment benefits -**Fiscal package of $2.2 trn** Direct financial assistance to households, loans to small and medium enterprises ($400 bn), support to the hardest-hit industries and large companies ($500 bn) with $25 bn for airlines and $100 bn for hospitals	**The Fed cut rates by 150bp to 0-0.25%** **New programme of bond purchasing and lending to companies** (unlimited volume and extended scope) $300 bn credit program for businesses (purchases of corporate bonds in the primary -PMCCF- and secondary market -SMCCF) and households (support for student loans and consumer credit markets) Support measures to reduce stress in the commercial paper market (CPFF) The Fed launches a programme to support money market mutual funds New launch of financing facilities for large corporates Resumption of a dollar swap policy with other central banks to ensure dollar liquidity

Sources: Financial Times, UBS, Deutsche Bank, les Echos, BNP Paribas

We stick to our essential message. Economic policy instruments are very powerful and should not be underestimated. The U-shaped profile we are expecting on economies, interest rates and stock markets seems to be setting in motion. Valuation levels for risky assets are attractive today, but the valuation does not give the timing of the rally. This timing will depend on news about the pandemic that is inherently unpredictable. Opportunities are emerging from a medium-to long-term investment perspective, but the short term remains uncertain.

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