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Weekly Investment Focus

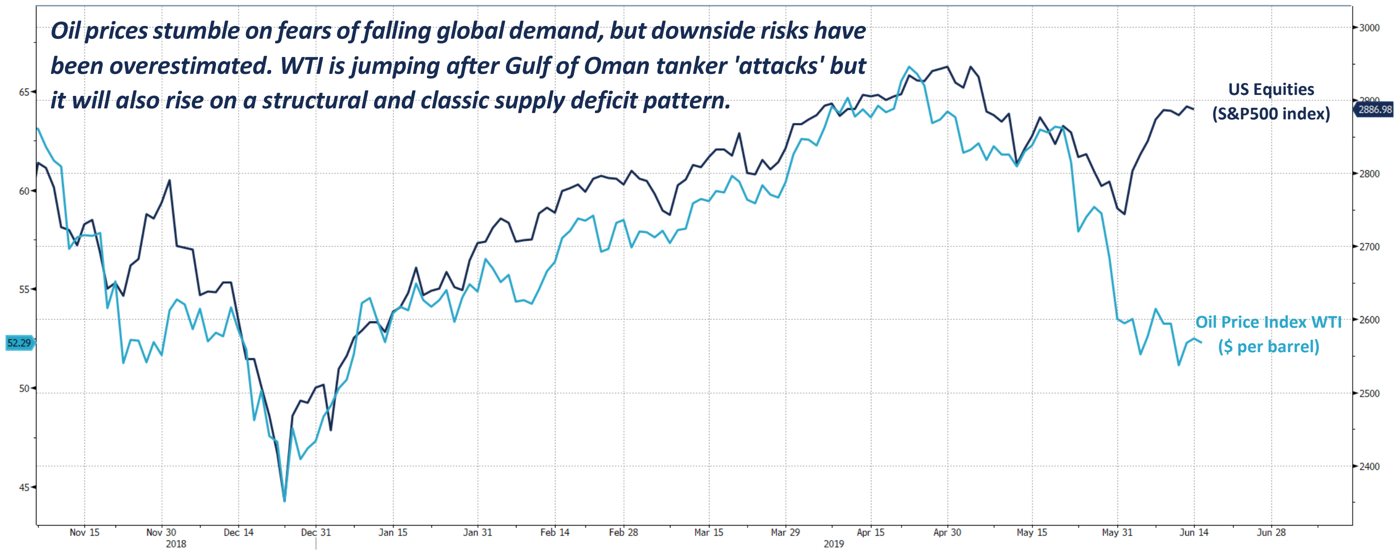
June 17, 2019

Headlines

- Oil prices have entered a bear market, but they will rebound and remain high for a long time
- First, the Fed has shown its strong commitment to supporting global economic growth
- Second, the classic supply deficit pattern will underpin a structural stabilisation of prices at a high level
- Third, geopolitical fears are currently driving up prices

Chart of the Week

“Oil prices must catch up with stock markets”



Source: Bloomberg, BoJ, ITAJ, Atlantic Financial Group, calculations assume an approximate. 67% weighting for Topix from October 2016

Commodity Market Analysis

“Bearish sentiment on oil masks bullish fundamentals”

In contrast to their very good start to the year, oil prices came under strong selling pressure, conceding $16 between 23 April and 5 June. Oil barrel prices were suffering from fears of weakening demand. The risk of a global slowdown and the Sino-American trade war are penalising economic activity, freight transport and, ultimately, driving down WTI and

Brent prices. Recently, prices have suffered from the announcement of an increase in crude oil trade reserves in the United States (+2.2 million barrels during the week ended June 7), indicating that supply remains abundant from the world's largest oil producer and consumer. In addition, Brent and WTI are struggling to take advantage of the fact that OPEC can formalise an extension of its agreements seeking to cap its production because Saudi Arabia has reported fears of an oil price of $40 per barrel.

However, three factors will stimulate investors to look at oil prices with the greatest interest: strong demand, low supply and geopolitical tensions.

First, the Fed has shown its strong commitment to supporting U.S. economic growth. After announcing in January that it would not raise its key rates this year, **it has just opened the door to a rate cut.** This double easing of monetary policy is powerful, especially since it takes place very early in the economic downturn. It should boost growth and inflation in the United States but also, as a ripple effect, in the rest of the world. Equity investors were satisfied. They are taking stock market indices to new heights. By simple correlation, it is possible to justify a WTI price above 60 dollars per barrel (see Chart of the Week).

Second, supply is constrained by the under-investment of recent years. Between 2015 and 2017, companies curbed their development spending, cutting their actual production capacity. The negative impact of the electric vehicles' development is overestimated. While the energy revolution in the car industry will significantly alter oil demand in the decades to come, this transformation will be gradual. It should not be a danger for several years. Ironically, just like the low price of oil did, it has slowed down the investment decisions of oil companies, which have preferred to play the card of prudence. Supply is therefore constrained: a very powerful factor in generating a structural increase in oil prices (see chart 2).

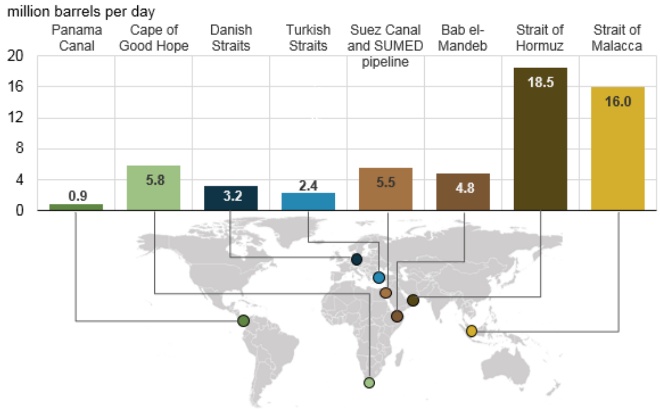
Chart 2 – Global Oil Supply & Demand

Third, geopolitical factors are currently driving up prices. US sanctions against Iran regularly lead to acts of sabotage of oil pipelines or tankers in the Middle East. This was the case again last week. Oil prices could rise sharply if there are major disruptions in the Strait of Hormuz or if the situation in the Gulf is exacerbated. Venezuela is also subject to US sanctions that prevent it from exporting its barrels, depriving the market of significant supply of crude oil.

Chart 3 – Strait of Hormuz Map

Source: MarketWatch, Atlantic Financial Group

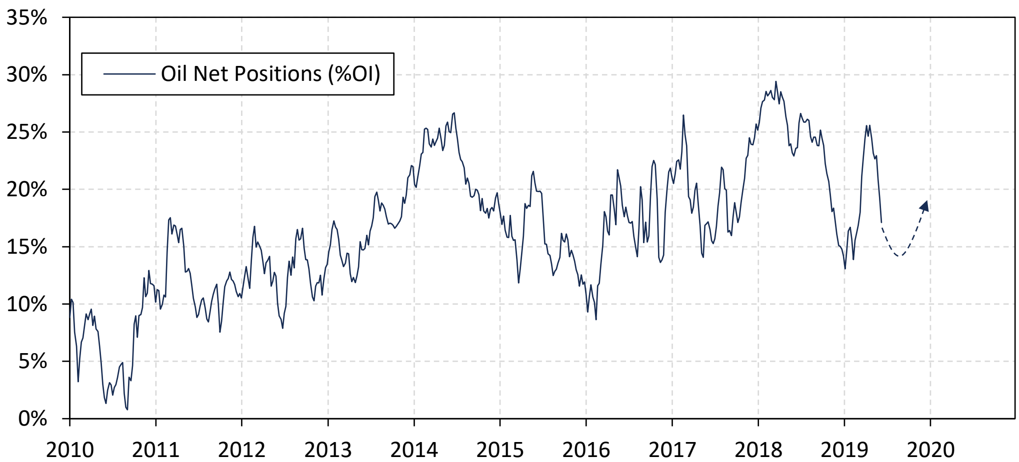
Chart 4 – Oil Transit Volume Through Maritime Routes



Source: EIA, Atlantic Financial Group

Finally, technically speaking, we believe that the major supports - at 50 dollars per barrel for WTI and 60 dollars for Brent - **should hold.** To the contrary, a break would be heavily bearish. As speculative long positions have declined significantly (see chart 5), any incremental positive oil-market news will easily result in an equally sharp upward rebound in crude prices.

Chart 5 – Speculative Positions on Oil



Source: Bloomberg, Atlantic Financial Group

Oil companies will also benefit substantially. The five Majors are well positioned: BP, Chevron, ExxonMobil, Royal Dutch Shell and Total. Well prepared for these volatile markets and for the transition risks, they should be the clear outperformers. Refiners are able to meet stricter regulations to limit pollution, while stocks of refined oil products are at low level. Among the refiners are companies such as Andeavor, Marathon, Phillips 66, Valero in the United States, Repsol in Europe, Tupras in Turkey, BPCL, Reliance, S-Oil, Thai Oil in Asia. Oil services have not been rewarded but they will benefit in the near future from the recovery in capital expenditures. This sector includes companies such as Schlumberger, CGG, Hunting, PGS, Saipem, TechnipFMC and Tenaris.

Conclusion:

Tight supply was overwhelmed by rising fear for demand. A further correction in prices is possible, especially if the probability of a recession in the United States were to increase, but it will remain subdued. Downside risks have been overpriced. Oil demand will continue to grow at a sustained pace in the coming quarters, supported by ultra-expansionist monetary policies. On the other hand, supply is limited by past under-investment and geopolitical tensions. Oil prices will rise and stay high for a long period of time.

For any bespoke investment solutions, feel free to contact your personal portfolio or relationship manager.

Returns on Financial Assets

Total return performance by asset class

Markets Performances (local currencies)	Last Price	1-Week (%)	1-Month (%)	2019 Year-to-Date (%)	2018	2017
Equities						
World (MSCI)	511.1	0.3%	1.7%	13.7%	-8.9%	24.7%
USA (S&P 500)	2 887	0.5%	2.1%	16.3%	-4.4%	21.8%
USA (Dow Jones)	26 090	0.5%	2.5%	13.2%	-3.5%	28.1%
USA (Nasdaq)	7 797	0.7%	0.9%	18.1%	-2.8%	29.7%
Euro Area (DJ EuroStoxx)	367.5	0.3%	1.1%	14.9%	-12.1%	13.4%
UK (FTSE 100)	7 351	0.3%	2.0%	11.8%	-8.8%	12.0%
Switzerland (SMI)	9 856	1.0%	4.9%	20.6%	-7.0%	17.9%
Japan (Nikkei)	21 124	1.1%	0.2%	6.6%	-10.3%	21.3%
Emerging (MSCI)	1 015	0.9%	0.5%	6.2%	-14.3%	37.8%
Bonds (FTSE)						
USA (7-10 Yr)	2.11%	0.0%	2.6%	5.4%	0.8%	2.9%
Euro Area (7-10 Yr)	0.30%	0.1%	2.2%	5.6%	1.4%	1.2%
Germany (7-10 Yr)	-0.25%	0.0%	1.4%	3.7%	2.4%	-1.4%
UK (7-10 Yr)	0.85%	-0.3%	1.9%	3.7%	1.5%	1.8%
Switzerland (7-10 Yr)	-0.47%	-0.2%	0.9%	2.7%	n.a.	n.a.
Japan (5-10 Yr)	-0.12%	0.1%	0.5%	0.8%	0.7%	0.2%
Emerging (5-10 Yr)	5.67%	0.2%	2.5%	8.8%	-4.2%	9.3%
USA (IG Corp.)	3.36%	0.3%	1.7%	7.9%	-2.5%	6.4%
Euro Area (IG Corp.)	0.69%	0.2%	0.6%	4.5%	-1.3%	2.4%
Emerging (IG Corp.)	5.25%	0.3%	1.0%	7.4%	-1.9%	8.0%
USA (HY Corp.)	6.13%	0.1%	0.6%	8.9%	-2.1%	7.5%
Euro Area (HY Corp.)	3.92%	0.2%	0.5%	6.3%	-3.8%	6.9%
Emerging (HY Corp.)	7.56%	0.4%	1.8%	8.0%	-4.7%	9.5%
World (Convertibles)	286.5	0.1%	0.5%	8.9%	-4.0%	16.5%
USA (Convertibles)	340.2	0.1%	0.0%	12.2%	-1.8%	17.3%
Euro Area (Convertibles)	3 772	0.1%	-0.1%	4.6%	-5.2%	7.0%
Switzerland (Convertibles)	185.2	-0.1%	0.1%	2.0%	-0.3%	0.6%
Japan (Convertibles)	184.6	0.5%	0.5%	0.2%	-5.0%	6.1%
Hedge Funds (Crédit Suisse)						
Hedge Funds Indus.	602.6	n.a.	-1.0%	4.3%	-3.2%	7.1%
Distressed	838.8	n.a.	-1.6%	2.7%	-1.6%	7.3%
Event Driven	657.2	n.a.	-1.1%	5.7%	-3.9%	6.3%
Fixed Income	349.5	n.a.	0.2%	2.8%	1.1%	6.5%
Global Macro	964.3	n.a.	-0.9%	3.1%	-0.1%	2.1%
Long/Short	741.2	n.a.	-2.4%	4.8%	-4.6%	13.4%
CTA's	299.5	n.a.	-0.6%	5.3%	-6.7%	3.3%
Market Neutral	269.3	n.a.	1.7%	1.8%	-5.0%	8.5%
Multi-Strategy	598.5	n.a.	0.0%	4.1%	-1.1%	6.8%
Risk Premia						
AQR Risk Premia	107.1	1.3%	2.1%	-1.2%	-9.7%	7.3%
AXA Multi-Risk Premia	101.75	0.2%	2.8%	2.9%	-4.8%	n.a.
BlackRock Risk Premia	109.1	1.0%	0.7%	2.9%	-4.8%	1.5%
BoAML Risk Premia	340.4	-0.3%	3.7%	6.1%	-7.5%	8.5%
ERAAM Premia	1 033	0.3%	1.8%	2.5%	-4.2%	n.a.
GAM Risk Premia	9.740	0.5%	-0.2%	2.5%	-6.3%	0.7%
Goldman Sachs RP	8.788	1.2%	0.9%	2.1%	-17.3%	n.a.
LFIS Vision - Premia	1 169	0.1%	0.3%	2.6%	-1.8%	2.0%
R CFM Diversified Fund	105.1	1.4%	3.7%	3.4%	-7.4%	8.6%
Uni-Global Risk Premia	959.2	1.0%	1.4%	0.9%	-8.4%	n.a.
Hedge Premia	894.3	-0.7%	-1.7%	-12.1%	2.0%	-5.1%
Volatility						
VIX	15.28	-6.3%	-15.4%	-39.9%	130.3%	-21.4%
VSTOXX	14.61	-3.7%	-18.2%	-39.8%	76.6%	-25.4%
Commodities						
Commodities (CRB)	393.3	0.6%	0.6%	0.7%	-7.1%	0.0%
Gold (Troy Ounce)	1 334	0.5%	4.4%	4.0%	-1.6%	13.1%
Oil (WTI, Barrel)	52.51	-1.4%	-15.0%	15.6%	-24.8%	12.5%
Oil (Brent, Barrel)	62.43	-2.1%	-12.2%	18.3%	-20.4%	20.6%
Currencies (vs USD)						
USD (Dollar Index)	97.520	0.8%	-0.5%	1.4%	4.4%	-9.9%
EUR	1.1214	-0.9%	0.5%	-2.2%	-4.5%	14.1%
JPY	108.58	-0.1%	1.4%	1.0%	2.8%	3.8%
GBP	1.2587	-0.8%	-1.1%	-1.3%	-5.6%	9.5%
AUD	0.6873	-1.3%	0.1%	-2.5%	-9.7%	8.3%
CAD	1.3413	-1.1%	0.3%	1.7%	-7.8%	6.9%
CHF	0.9994	-1.0%	1.2%	-1.7%	-0.7%	4.5%
CNY	6.9258	0.1%	-0.1%	-0.7%	-5.4%	6.7%
MXN	19.152	0.3%	0.1%	2.6%	0.0%	5.4%
EM (Emerging Index)	1 623.2	0.0%	0.2%	0.5%	-3.8%	11.4%

Source: Bloomberg, Atlantic Financial Group

Performance (Negative \ Positive)

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