NIC

— Nova Investment Club —

Newsletter

February 2020

NIC
Nova Investment Club

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Foreword

This Month:

In our Macro Overview section, Analysts from both divisions will cover broad macro themes while reviewing major economic news from the past month. In our Deeper Dive section, Marvin Breuer, elaborates on why profitability does not matter for Software as a Service (SaaS) valuations. Moreover, in our Regional View, Oliver Schoch, examines the impact of coronavirus on China's economy.

Our Investment Banking Division will guide you through January's M&A overall activity. Read about Siemens Ldt to acquire C&S Electrics, Visa Inc. acquisition of Fintech Startup Plaid and Volkswagen AG offering to buy the rest of Navistar International Corporation. Additionally, get a detailed overview on what happened to Tesla, as well as consider our opinion on 2020 global M&A outlook.

Our Financial Markets Division will present the monthly results of the NIC Fund, an active relative return fund investing across four different asset classes: Equities, Fixed Income, Commodities and Currencies. The analysts will also provide commentary on each of the four major asset classes through analysis of the past month's major market moves. The overall performance of the NIC Fund in January was slightly negative, with a cumulative return of -0.38%. This loss was mainly attributed to a decline in Equities and Commodities.

Lastly, Benedict Minker elaborates on the pre-trade deal implications for the UK economy after formal Brexit and, our President, Francisca Fernandes examines the impact of coronavirus on oil price volatility and the prospectus of the energy industry .

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NIC

Nova Investment Club

Macro Overview

Monthly

February 10th, 2020

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Market Moves

Market Moves

% change

	Last Close	-1W	-3M	YTD
S&P 500	3 226	-2,12%	6,19%	-0,16%
DJIA	28 256	-2,53%	4,47%	-0,99%
Nasdaq	9 151	-1,76%	10,35%	1,99%
MSCI World	3 045	-2,45%	2,67%	-2,03%
MSCI EM	3 848	-4,10%	2,18%	-3,79%
Russell 2000	1 614	-2,90%	3,30%	-3,26%
Euro Stoxx 50	3 641	-3,66%	1,01%	-2,78%
FTSE 100	7 286	-3,95%	0,52%	-3,40%
Nikkei 225	23 205	-2,61%	1,21%	-1,91%
Hang Seng	26 313	-5,86%	-2,21%	-6,66%
Dollar Index	97,39	-0,47%	0,04%	1,04%
EUR/USD	1,109	0,62%	-0,53%	-1,07%
GBP/EUR	1,190%	0,39%	2,57%	0,66%
GBP/USD	1,321%	1,02%	2,04%	-0,38%
USD/JPY	108,350	-0,85%	0,30%	-0,24%
USD/CHF	0,96	-0,84%	-2,33%	-0,33%
Brent Crude	58,160	-4,17%	-3,44%	-11,88%
Gold	1 582,9	0,70%	4,50%	3,93%

Generic Bond Yields

change in bps

	Last Close	-1W	-3M	YTD
US 10Y Yield	1,507%	-17,7	-18,4	-41,1
GER 10Y Yield	-0,434%	-9,9	-2,7	-24,9
JPY 10Y Yield	-0,066%	-4,6	6,7	-5,5
UK 10Y Yield	0,524%	-3,9	-10,5	-29,8
PT 10Y Yield	0,266%	-11,3	10,0	-17,6

**Source: Bloomberg, as of 2020-01-31*

In Focus

January

Coronavirus fears drive Chinese stocks sell-off. Mining and travel related companies were the most affected equities. Investors fear the government will not be able to control the outbreak, adding to the growing concerns over falling birth rates, weak consumer spending, slowing export growth, rising unemployment and the slowest GDP growth rate in 29 years (6.1% in 2019).

Germany's lowest growth in six years likely to increase political tensions. The country's GDP grew 0.6% in 2019, the slowest rate since 2013. German industrial production fell 3.5% in December, the largest decline in a decade, due to global trade tensions, Brexit, weak exports and an auto-industry facing climate-change challenges, such as new emission rules and a moving consumer trend towards electric vehicles. Political and business leaders continue to advocate for an increase in government spending, however, the government of Angela Merkel remains committed to balanced budgets.

IMF cut global economic growth forecasts for 2020. Predictions for this year dropped from 3.4% to 3.3% , just slightly above the 2.9% registered in 2019, which became the worst year for the global economy since the 2008 financial crisis. Economists at the IMF noted that without interest rate cuts from the Fed, the ECB and central banks other in Q3 and Q4 of 2019, the situation could have been worse, even reaching a recession.

After 47-years of being a member, UK leaves the EU. Following the 2016 referendum and years of uncertainty over the fate of the Brexit, it all came to an end on the 31st of January. No practical changes occurred right away, as a transition period was agreed until the end of 2020, which will include heavy negotiations over the future relationship between both parties, namely in what concerns a trade deal.

Six emerging market Central Banks cut rates in January. This group included South Africa, Malaysia, Argentina and Turkey. Policymakers aim to boost economic growth, making up for policy shortfalls over the past years. The monetary easing by the US Federal Reserve in 2019, made it possible for EM to cut rates without capital outflows concerns.

US and France reached a deal on digital tax. Talks over the World Economic Forum in Davos, resulted in an agreement between the two parties. US guaranteed the suspension of planned tariffs on USD 2.4 bn of French goods, while France accepted to stop digital tax collection. However, this is not the end of discussions over digital tax, as the UK and other countries plan to introduce these if a global agreement is not reached.

Shinzo Abe reinforces commitment to monetary easing by nominating dovish economist, Seiji Adachi, to Bank of Japan. In spite of increasing objections from banks, the BoJ aims to further ease monetary policy, striving for the 2% inflation target.

Donald Trump's signs the implementing legislation for USMCA. As the "phase one" deal advancements with Beijing decelerated, Trump's signature aims to show accomplishments ahead of the 2020 re-election campaign. The USMCA will replace Nafta, as the new trade deal between the US, Canada and Mexico.

Ukraine raises EUR 1.2 bn of debt at record-low borrowing costs. Taking advantage of the high optimism surrounding president Zelensky's reform programme and promises to suppress corruption, the new 10-year euro-denominated bonds were priced at a yield of 4.375%.

Corina Popa
Financial Markets Division

Deeper Dive

Software as a Service (SaaS) Valuations: Why Profitability Does Not Matter

Marvin Breuer
Investment Banking Division

“The ability to accelerate monthly revenues while decreasing monthly burn is the #1 thing I look for in a growth stage business.”

– Steve Schlenker, Managing Partner at DN Capital

The valuation multiples of Software-as-a-Service companies are at an all-time high. On average, a publicly listed SaaS company is currently trading at 11.99x revenue, the median is 9.5x. The difference of 2.5x between average and median implies that some particularly attractive SaaS companies are trading at significant premiums. Almost half of the companies are trading at a turnover of 10x or more - a record.

In the current market environment, growth stocks such as those of SaaS companies significantly outperform those of value stocks. While the latter, measured by the Russell 1000 Value ETF, recorded a return of +13.8% over the last 12 months, growth stocks in the Russell 1000 Growth ETF gained an astonishing +29.5%. This strong growth is mainly due to the low interest rate environment (e.g. Effective Federal Funds rate of 1.55%), resulting in the future cash flows of fast-growing companies being discounted at lower discount rates, which in turn leads to a significant increase in enterprise value and multiples.

These high valuations are particularly striking because hardly any SaaS company is profitable. Their high valuations are mainly determined by another variable: growth. But should not profitability be used as a benchmark? The answer is no. Instead, practitioners rely on other measures such as MRR (Monthly Recurring Revenue). In addition, subscription models play a crucial.

To determine the sustainability of revenue growth, the expansion MRR rate serves a key metric. It describes the additional recurring revenue generated by existing customers either through add-ons, up-sells or cross-sells. It shows whether the company is delivering increasing value to customers and whether it is able to monetize this value.

Especially in the long term, the ability to generate MRR for expansion is essential, as most later stage SaaS companies generate a significant portion of their growth with existing customers.

In contrast to the profitability represented by net income, almost all of the SaaS companies have positive cash flows. An average SaaS company generates a positive cash flow 6 years after its founding. Especially the subscription model used by most Software-as-a-Service companies has important implications for the valuation. With subscription models, a software license is not sold once and booked as revenue, as was previously the case, but is made available to the customer for software services in return to, for example, a monthly fee.

If the customer pays in advance, deferred revenue is recognized, which reduces net working capital and thus increases cash flow from operations. Although the deferred revenue must be earned in the future, it can already be used to generate further sales. Thus, the customers' money finances the operations of the company. In this context, most public SaaS companies prefer to invest their money in faster growth at the expense of net income. In terms of valuation, it is argued that if the company wanted to generate a positive net income, it could simply stop investing in growth and wait for subscription payments.

Currently, companies in the SaaS market are rewarded for their growth regardless of profitability. If this changes in the future and positive cash flow and positive profitability are required in addition to positive cash flow, the growth rates of companies will have to decline significantly.

Marvin Breuer
Investment Banking Division

Regional View

The Coronavirus Has Infected China's Economy

Oliver Schoch
Financial Markets Division

"The coronavirus repercussions on the economy mark the latest in a series of setbacks in the economy over the past year, including a handful of bank failures sparking contagion fears, forcing the central bank to become ever more generous with the provision of liquidity to markets."

- Economist George Magnus, associate at Oxford University's China Centre

At the end of January, the upward movement of the markets with the S&P 500 and the DAX marking record highs, has come to a quick stop after the coronavirus outbreak and its contagiousness became public.

On Monday, the 3rd of February, everyday life should have slowly started up again in China after the Chinese New Year holidays was extended in an attempt to fight the spread of the coronavirus. Instead, streets in megacities such as Beijing and Shanghai, remained empty. Although holidays were officially over, most companies followed the recommendations from provinces to not resume business in order to limit the spread of the epidemic.

Only a few facilities and companies with special permissions have restarted operations. Telecommunication company Huawei, as well as the stock exchanges in Shanghai and Shenzhen got such permissions. Following the reopening of the stock markets was a plunge of up to nine percent during the course of the day. Prices were incorporating the bad news which accumulated while the stock exchanges were closed. The Chinese government had previously tried to calm the situation.

Prior to the reopening, the Chinese central bank supplied the markets with more liquidity. According to analysts, this helped at least to prevent worse from happening. The central bank provided commercial banks with CNY 1.2 tn (around EUR 156 bn) in liquid funds. This is the biggest support from the Chinese government to the economy since 2004.

The manufacturing industry has been so far less affected than the tourism sector. "One should not forget that after the Chinese New Year, production activity during this period is usually low and does not recover immediately" said Tao Wang, China chief economist at the Swiss bank UBS. An evaluation by the bank also shows that China accounts for one-fifth of global economic output and tourism spendings. Its share in world trade has more than doubled since 2003, when the sars epidemic broke out. Economists estimate that sars has cost the global economy around USD 40 bn; China alone lost USD 17.5 bn of its gross domestic product at the time. The coronavirus is also hitting the markets at a time when stock indices are rushing from record to record and valuations appear to be quite high already. This makes this virus more dangerous for financial markets than SARS was at the time, especially for cyclically sensitive sectors.

The World Bank has calculated that a pandemic like the Spanish flu after World War One, which killed at least 25 mn people, would cause the global economy to collapse by almost 5%.

Economists expect China's growth to slow down significantly in the first quarter of 2020. UBS, for example, forecasts economic growth of only 3.8%. In the fourth quarter of 2019 it was still at 6%. It is more difficult to predict how the consequences of the virus will affect the rest of the year. After the sars crisis was overcome, there had been a significant recovery of the markets. But this time coronavirus has already spread further than sars at the time although being less lethal. Depending on how quickly the situation returns to normality, UBS expects growth of 5.4% for the full year.

Goldman Sachs has reduced its growth forecast for China for the first quarter from 5.6% to 4.0%. Even under optimistic assumptions about the course of the epidemic, only 5.5% is expected for 2020, according to a study published on Monday instead of 5.9% as previously estimated. Despite the epidemic, global economic growth could still increase slightly to 3.25% in 2020. The forecasts are based on the assumption that governments will manage to bring the rate of new infections "sharply down" towards the end of the first quarter.

Oliver Schoch
Financial Markets Division

Macro Overview

Economic Calendar

Economic and Political Events

Trump's State of the Union Address

On the **5th** of February, during the annual message, Trump boasted booming employment, declining poverty and a strong economy. The speech was delivered on the floor of the House of Representatives, where he was impeached less than two months ago.

Ireland Election

Ireland held a general election on the **8th** of February. The vote revolved around questions regarding housing shortage, a healthcare crisis and inequality. The election results will likely lead to the formation of a coalition government.

US Iowa Caucus

On the **3rd** of February, Democrats in Iowa voted for the party's presidential nominee. The event was marked by chaos and delays due to software issues. Results showed Buttigieg narrowly winning the delegate race by 0.1%, with 26.2%, followed shortly by Sanders. Warren and Biden secured only 18% and 15.8% of the delegates, respectively.

Central Bank Decisions

Fed Monetary Policy Report

On the report submitted to Congress on the **7th** of February, coronavirus was announced as a new risk to the US and global outlook, as disruptions in China may heavily affect the rest of the world. The benchmark interest rate was left unchanged in January.

Bank of Russia Interest Rate Meeting

On the **7th** of February, the Bank of Russia cut interest rates by 0.25% to 6%. Moreover, there is a high probability of further monetary easing at the next meeting, in April. The Monetary Policy Report will be published on the **17th** of February.

New Zealand Monetary Policy Decision

The Reserve Bank of New Zealand will hold its monetary policy decision meeting on the **12th** of February. A cut rate is unlikely, keeping its policy "cash rate" at 1% as the Q4 2019 inflation reached 1.9% YoY, just below the 2% target.

Inflation and Deflation

Euro Zone Inflation

The annual inflation is expected to be 1.4% in January, up 0.1% from the figure in December. However, when excluding volatile energy and food prices, the rate is forecasted to drop to 1.1%. The complete figures will be made public on the **21st** of February.

Spain's Inflation

Spain's annual inflation rate will be released on the **14th** of February. It is expected to rise to 1.1% from 0.8% in December, following higher electricity, food and non-alcoholic beverages prices.

Update on Argentina's Inflation

January MoM figures on consumer prices will be published on the **13th** of February. Estimates are forecasting MoM inflation at 3.4% vs 3.7% in December, when the most affected sectors were health, communications and home maintenance equipment.

Labour Market

US Employment Readings

US job market figures were announced on the **7th** of February. Nonfarm payrolls rose 225,000 for the month, exceeding market expectations. The unemployment rate increased to 3.6%, positively affected by a 0.2% higher labor force participation.

UK's Labour Market

On the **18th** of February, UK will release its unemployment rate figures for December. In the prior three months, the rate stood at 3.8%, the lowest level since 1975. The IMF forecasts a narrow increase to 3.81%.

South Korean Alarming Labor Force

The figures for January's will be published on the **11th** of February, after gaining 0.2% to 3.8% in December. Economists are expecting poor figures despite various target-based incentives, adding to the current economic concern over slowing foreign direct investment and increased sovereign debt.

Corina Popa
Financial Markets Division

Investment Banking

M&A
Overall Activity

Global

The trend of weaker M&A activities did continue in January as well. An indicator for this the total number of deals amounted to 502 which is a 38.56% decrease compared to the previos month. However, if only taking a look at completed deals of the past month, the total number decreases to 188. Consulting firm Baker McKenzie forecasted global M&A to drop 25% this year, from USD 2.8 tr to USD 2.1 tr. More prosaic areas of business such as real estate, retail media or consumer products are supposed to be not highly targeted. It is expected that the most popular targets of this year will be tech companies.
Contraty, to this trend, the largest transaction of the month – which is not closed yet, is the merger of Hexcel Corp and Woodward Inc. for USD 6,556.8 m. Hexcel is a global leader in advanced composites technologies that is going to buy Woodward, a designer and manufacturer for aircraft engines, industrial engines and turbines. The largest deal that has been closed in the past month was the merger of Sonangol Sociedade Nacional, a parastatal that oversees petroleum and natural gas production in Angola that is to buy PT Ventures SGPS SA, a Portuguese company for USD 1,000.0 m.

Selected Regions

North America
M&A Dealmaking stumbles out of the gates in January 2020 in the United States with transactions being down 11% for the month compared to the same period last year. According to Dealogic, the year's sluggish start with just 730 announced deals in the U.S. in January becomes even more obvious when compared to the historic average for the month between 2010 and 2019, 953.

EMEA
After a year of slow M&A activity in EMEA in 2019 with only 12 megadeals compared to 16 in 2018, M&A activity is expected to pick up speed according to a report by J.P. Morgan. Whilst Brexit inevitably caused great uncertainty and with it a significant drop off in M&A activity, there is a growing sense amongst industry experts, that M&A activity is going to ramp up again as a result of the greater certainty due to the fact that the U.K. officially left the EU in January.

Asia
M&A activity in Asia-Pacific excluding Japan occurred at its slowest pace in five years in 2019 as concerns about a slowing global economic outlook and the ongoing US-China trade war weighed on deal bankers and companies, according to data from Dealogic. Interestingly, Japan outspent Chinese rivals for the second year in a row to be the biggest dealmaking force in Asia in 2019, and the buying is set to continue into 2020.

M&A
Deals of the Month

Announnced Date	Target	Buyer	Target region	Target business	Value (USD m)	Premium (%)
12 Jan 20	Hexcel Corp	Woodward Inc	USA	Adhesive manufacturing company	6556.75	-
22 Jan 20	Capitaland Commercial Trust	Capitaland Mall Trust	Singapore	Real estate investment	6069.31	-
09 Jan 20	Veeam Software Group GmbH	Insight Venture Partners LLC	Switzerland	Information Technology Company	5000.00	-
27 Jan 20	CenterState Bank Corp	South State Corp	USA	Personal and small corporate banking	3219.97	-
30 Jan 20	Navistar International Corp	TRATON SE	USA	Holding company (busses and trucks)	2954.07	-
16 Jan 20	Global Blue SA	Far Point Acquisition Corp	Switzerland	tourism shopping tax refund company	2564.27	-
28 Jan 20	Delphi Technologies PLC	Borgwarner Inc	UK	Technologies (powertrain)	1497.00	-
10 Jan 20	Dermira Inc	Eli Lilly & Co	USA	Pharmaceuticals	1042.56	-
24 Jan 20	PT Ventures SGPS SA	Sonangol Sociedade Nacional	Portugal	Telecommunications	1000.00	-
10 Jan 20	Sorrento Therapeutics Inc	Undisclosed Acquiror	USA	Biotechnology	993.10	-

**Source: Mergermarket, Dealogic*

Paulina Michel & Alexander Keil
Investment Banking Division

M&A: Top Deals

Siemens Ldt to Acquire C&S Electrics

24th of January 2020, Siemens has signed an agreement to acquire 99% of the equity share capital of India-based electrical equipment manufacturer C&S Electric for approximately RS 21.0 bn (USD 294.0 m).

Buyer vs Seller

Siemens is one of the world largest company focusing on electrification, automation and digitalization. Siemens Ldt is a Natl India listed subsidiary that has its operations in the transportation sector it delivers high speed trains, in the lighting sector it manufactures small light bulbs. In fiscal 2019, which ended on 30th of September 2019, Siemens generated revenue of EUR 86.8 bn. C&S Electric is amongst the leading suppliers of electrical equipment in India and is India's largest exporter of industrial switchgear.

Industry Overview

The electrical equipment manufacturing market expected to reach a value of nearly USD 1429.2 bn by 2022. Which represent a significant growth of 8.1% during the forecast period. The growth in the electrical equipment manufacturing market is due to rapid urbanization and rising disposable income. The market will grow even more significantly in the developing countries according to the Electrical Equipment Manufacturing Global Market Report 2020.

Peers	Currency	Market Cap (CUR m)
Schneider Electric SE	EUR	55,483.12
General Electric Co	USD	113,099.34
ABB Ltd	CHF	51,775.29
United Technologies Corp	USD	135,161.52
3M Co	USD	93,759.90

Deal Rationale

The announcement of Siemens Ldt's takeover of New Delhi-based C&S Electric Limited has emerged as an evidence as the synergies between the two companies are so important. Furthermore, deal has been signed in a step for Siemens Ltd to meet the increasing demand for electrification across industry, infrastructure and buildings in India. The acquisition of one of the leading providers of electrical and electronic equipment for infrastructure, power generation, transmission and distribution, will strengthen Siemens' position as a key supplier of low-voltage power distribution and electrical installation technology.

Market Reaction

Siemens Ltd (SIEM:IN)

The announcement, 24th of January, had no effect on the stock. The small decline in the share price is due to cyclical macroeconomic factors.

C&S Electric Limited

C&S Electric Limited is an unlisted company, so it is very difficult to find financial information about it. Nevertheless, C&S Electric is a leader on its regional market and should satisfy the market. Its founder and chairman R N Khanna said: "Having been a leading participant in the Indian switchgear market since 1966, we are now extremely delighted to be part of the Siemens family, an organisation that has pioneered and developed the switchgear market in India and globally for many decades."

Future Challenges

Siemens India managing director and CEO Sunil Mathur said: "The addition of C&S Electric's products, sales network, manufacturing units and a highly competent employee base will complement and strengthen the range of Siemens' offering. " The future challenge for Siemens Ldt will be to integrate properly the company in order to bolster its portfolio not only in India but also for export to competitive international markets in line with their growth strategy.

Raphael Salimi
Investment Banking Division

M&A: Top Deals

Visa Inc. Acquires Fintech Startup Plaid for USD 5.3 bn

Payments mammoth Visa Inc has decided to buy financial services API company Plaid for an amount double its last valuation (USD 2.65 bn as of late 2018). Visa is paying USD 4.9 bn in cash, plus USD 400 m in retention and deferred equity.

Buyer vs Seller

Visa Inc. is a payments technology company connecting consumers, merchants, financial institutions, businesses, strategic partners and government entities to electronic payments. The company's core business includes processing infrastructure, transaction processing services, digital products, merchant products, and risk products. On the other hand, Plaid helps start-ups and banks share financial information more easily among themselves contributing to the success of neo banks and fintech apps.

Industry Overview

The financial technology realm is undergoing a substantial shift as consumers swap traditional cards and bank accounts by novel digital apps to conduct payments and monitor savings and spending. Such move generated a new market need of linking traditional banks legacy systems and capabilities with emerging consumer-focused technological players. This deal seals Plaid's position as the market leader in the upcoming market.

Peers	Currency	Market Cap (CUR m)
Xignite, Inc.	USD	Not Public
Finicity Corporation	USD	Not Public
Yodlee, Inc.	USD	Not Public
TrueLayer Limited	GPB	Not Public
figo GmbH	EUR	Not Public

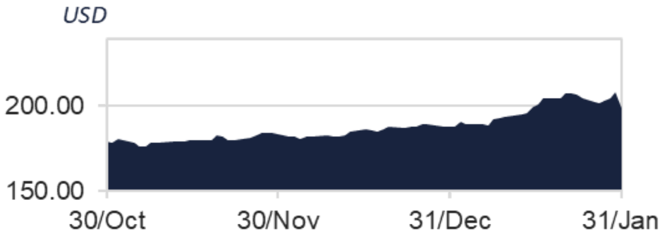
Deal Rationale

This deal aligns with Visa long term strategy of complementing traditional card-transaction services - Visa is the largest U.S. card network, handling $3.4 trillion of credit, debit and prepaid-card transactions in the first nine months of 2019 – and strengthens its presence in the electronic payments segment where trillions of dollars are sent between bank accounts globally each year. Plaid's B2B model enables Visa to step closer into business-to-business payments, a segment in which Visa has been trying to seize a bigger role as it is considered untapped compared with consumer payments.

Market Reaction

Visa Inc

After announcement, stock price increased 0.7% to USD 196.62. Market sentiment is sweet and sour. While the deal makes perfect sense for Visa's business strategy some shareholders argue it was too expensive.



Plaid Inc

Plaid is the leading player in the financial services APIs sector. Founded in 2013 it counts with more than 200 m user accounts connected to more than 11 k financial institutions. User base CAGR was 115% between 2015 and 2019. To put things into perspective, Plaid serves more than 80% of US's fintech applications. The company has raised USD 309.3 m before acquisition and currently has a 450 headcount.

Future Challenges

A key point will be how Visa can profit from Plaid's fintech customer base without cannibalizing the latter's business model in the long run – Visa's current customer base is comprised of banks and traditional financial institutions, while Plaid focuses on neo banks and novel fintech players who are exactly trying to lure away deposits and clients from traditional banking. This apparent conundrum suggests Visa and Plaid might be headed to business and culture integration headwinds.

Rafael Santos
Investment Banking Division

M&A: Top Deals

VW's Offer to Acquire Navistar

On 30th of January 2020 Volkswagen AG has offered to buy the rest of Navistar International Corp. in a USD 2.9 bn bid. Volkswagen's commercial truck unit Traton has offered to pay USD 35 per share to acquire the portion it doesn't already own.

Buyer vs Seller

VW's heavy-truck division was created from acquisitions of Germany's MAN and Sweden's Scania. Navistar's major stake is currently owned by the entrepreneur Carl Icahn. The board of directors of Navistar has received the offer and it did not guarantee an offer acceptance. Traton's and Navistar's advisors were not disclosed.

Industry Overview

The truck-makers industry is currently struggling due to the recent changes in the automotive industry. The automotive market is living an economic downturn, Navistar International Corp, and other truck-maker companies have announced thousands of job cuts in a restructuring plan to be completed by the end of 2020. New alliances are sought in order to reduce operational costs.

Peers	Currency	Market Cap (CUR m)
Spartan Motors Inc	USD	634.14
Blue Bird Corp	USD	544.91
PACCAR Inc	USD	26,301.49
Wabash National Corp	USD	643.16
Cummins Inc	USD	24,460.06

Deal Rationale

Volkswagen has had a strong interest in acquiring Novistar since 2016, when it completed a 16.6% acquisition (later grown to 16.8%). The expansion has been holden back by the 2015 eco-scandal in which Volkswagen was involved. The rationale of the deal in 2016 was driven by the will to have market share in the truck industry in North America. While the offer was placed at a 7.3x EDIBTA multiple it is believed that there will not be an auction process due to the lack of third-parties and anti-trust scrutiny. Mr. Icahn is currently the major source of uncertainty regarding the outcome of the deal.

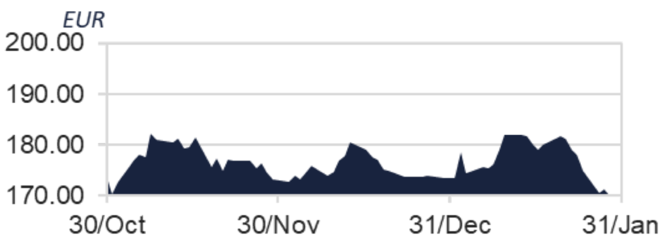
Market reaction

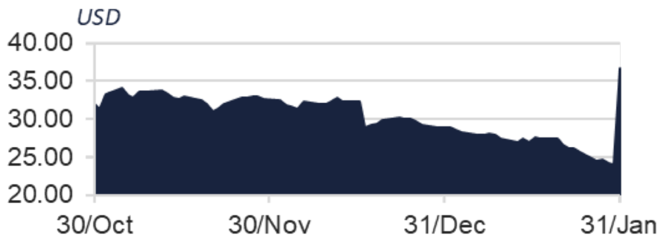
Volkswagen

VK's stock price has increase upon announcement of the acquisition with a 1.7% change. On the following days the price stabilezed to the previous value.

Navistar International

Navistar's shares saw an increase of 50% after the announcement of the proposal. This suggests that investors believe in a sweeter deal than the one proposed by Traton.





Future Challenges

In case of a successful deal, VW will have to implement the restructuring process of Navistar while dealing with an economic downturn of the industry. The acquisition will also reduce the reliance of Volkswagen on Traton SE unit for the EMEA and LATAM markets. In case of failure, instead Volkswagen would have to deal with a complex macroeconomic situation in an industry already been disrupted by electric vehicles.

Michele Marcaccio
Investment Banking Division

What Happened To

Tesla

Tesla, Inc. is an American electric vehicle and clean energy company based in Palo Alto, California. Among electric vehicle manufacturing and battery energy storage, the company founded by the visionary Elon Musk also manufactures solar panels and solar roof tiles through its subsidiary SolarCity. It counts more than 45,000 employees worldwide.

Corporate News

Tesla's share price has more than doubled since the start of the year. The strong performance is being caused by the seemingly boundless enthusiasm of Tesla's supporters. Moreover, after negative results in the first half of last year, the fourth quarter saw a turnaround, generating USD 1 bn in cash after capex and reaching its second straight quarterly profit. Analysts are confident that the company has a lock on the growing battery electric vehicle market and the global expansion strategy was well received by investors. Analysts agree that Tesla demonstarted the ability to build cars generating cash, and with best-in-class profit margins. However, the rating on the stock remains neutral for many alnalysts. The inability to generate enough cash from car sales made many investors betting against Tesla but the recent turnaround seems to have quieted some of the critics. Tesla stock still remains one of the most shorted stocks, though much less than it was in the recent past.

Price (31 Jan 20, USD)	**748.64**
Target Price (USD)	423.00
3M Performance	137.72%
Market Cap (USD m)	134,937.63
Enterprise Value (USD m)	143,580.63
**Target Price is for 12 months*	

Valuation Analysis

Tesla was, on the day this article was written, trading at USD 748.96 in the US. It was trading at the upper side of its 52-week range, figuring at USD 176.99 – 968.99. Even though some forecast predicted a 5-year-term price at USD 7,000, most of the analysts recommended to hold the stock, giving a neutral opinion. Tesla stock could also be benefiting of stock squeeze and investors who betted against the car manufacturer are now helping to drive it far higher. Given the stock boom, short-sellers are buying the shares to hedge themselves from potential future losses. If enough investors do this, it could push the price higher, leading to even more short-sellers to buy. This effect creates losses on current short positions and deters new investors from betting against the stock.

The global electric-vehicle (EV) industry continues to expand rapidly. Regional performance varies but, overall, global EV-sales volume are becoming large enough to lead to discrete profits for leading suppliers. EV sales grew to more than two million units globally in 2018. China leads the table with an 85% growth over the prior year. The European market saw a moderate growth with different pictures according to the country and North America got an electric-vehicle boost mainly because of strong sales performance of Tesla's Model 3. Nevertheless, regulatory developments will have a major impact on sustainable market growth and will probably determine the future of the EV industry.

Peers	Currency	Market Cap (Cur m)
Fiat Chrysler Automobiles NV	USD	20,821.99
Ford Motor Co	USD	32,334.01
General Motors Co	USD	48,328.85

Federico Farina
Investment Banking Division

NIC's View On

2020 Global M&A Outlook

Tobias Berberich
Investment Banking Division

"While investor preference for corporate clarity and business focus has long been observed, we have seen that companies are even more likely to restrict acquisitions to core competencies as the economic cycle enters later stages."

- JP Morgan

In last months newsletter we reviewed global mergers and acquisitions activity throughout 2019. Hence, it is only fitting to provide the clubs outlook for 2020 to kick off the year.

With prolonged, heightened global uncertainty it is to be expected that companies will seek, and investors reward strategically driven acquisitions to bolster organizations for increasingly likely troubled waters ahead. Horizontal mergers are expected to be a continued driving force to enhance free cash flow and eliminate earnings volatility. Riskier M&A deals of conglomerate nature we expect to decline, continuing the 2019 trend of a slowly diminishing appetite for risk.

The strength of M&A activity in 2020, in our view is predominately depended on the materialisation of recession fears into reality. With the US economic expansion entering its 128th month and several indicators such as the yield curve and unemployment figures suggesting that we are in the latter stages of the cycle, fear about the timing and severity of the next recession as been rampant. Whilst, bearish investors have been sounding the alarm bells for some time now, there appears to be an increasingly cohesive narrative that a market reversal is occurring sooner rather than later.

We expect Private Equity to remain active in the M&A space. Funds remain ready, armed with ample equity and debt capital. In case of an adverse economic environment a play on distressed assets could become relevant. With valuations and multiples currently being on the upper end of the spectrum, some funds may seek to exit their investments prematurely, generating vast discounts. Add-on acquisitions offering potential for multiple arbitrage due to their inherently lower valuations are expected to remain the driving deal rational for PE funds.

Looking towards Europe. With Brexit on its way at last, we expect M&A activity to decline slightly due to a challenging geopolitical environment and continued uncertainty surrounding the final terms of the withdrawal agreement Mega deals are expected to decline further, only announcing 12 deals of such magnitude in 2019. A major concern is the fading relevance of Europe as an economic powerhouse. Industry consolidation through M&A has fallen far behind North America, reducing competitiveness on a global scale.

We expect Chinese cross-border activity to remain robust in 2020. Driven by the pursuit of establishing a stronger footprint in America and Europe. However, it remains to be seen what impact regulatory and political pressures will have on the M&A arena. Western apprehensiveness of allowing Chinses organisations to acquire essential corporations due to fears of Chinese government involvement has become the norm.

Date	Recent News
07 Feb 20	States Blocking T-Mobile deal would disrupt U.S. Merger Policy. ***Source:*** *Bloomberg*
07 Feb 20	Goldman Sachs to raise new $8 Billion for new buyout fund. ***Source:*** *Forbes*
06 Feb 20	Celtics Expected to be major players in buyout market ***Source:*** *SP*
05 Feb 20	Foamix and Menlo announce shareholder approval of proposed merger ***Source:*** *Yahoo*

Tobias Berberich
Investment Banking Division

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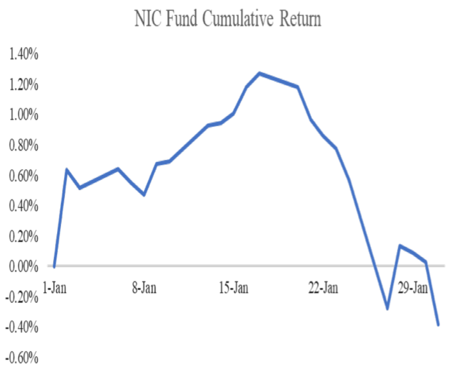
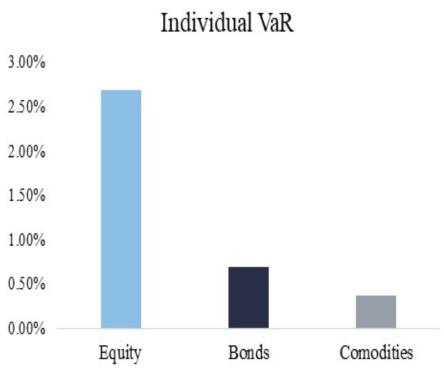
Portfolio Overview



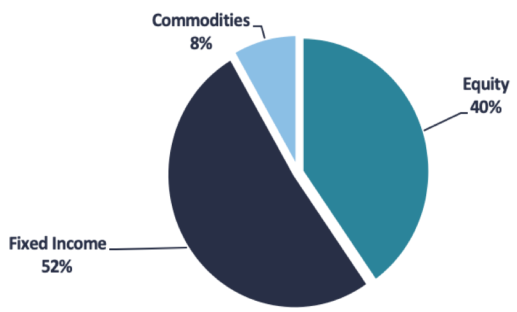
Portfolio Statistics	
Cumulative Return	-0.38%
Annualized Return	-4.60%
Daily St. Dev	0.21%
Period St. Dev	0.97%
Annualized St. Dev	3.37%
Info Sharpe	-1.37
Skew (Daily)	-0.48
Kurtosis (Daily)	1.90

Benchmark	
iShares 3-7 Year Treasury Bonds	55%
MSCI World ETF	30%
Invesco DB Commodity Index	10%
MSCI Emerging Markets ETF	5%



Portfolio Snapshot

Throughout January, the NIC Fund remained invested in three asset classes: Equities (40%), Fixed Income (52%) and Commodities (8%), with no significant changes in its composition relative to December.
Within Equities, 20.16% was roughly equally distributed among 19 individual stock picks, while the remaining 20.76% were allocated to several ETFs, namely MSCI World, S&P 500 Value Index, MSCI Emerging Markets and FTSE 100 Index.
Regarding Fixed Income and Commodities, we remained slightly underweighted in relation to the benchmark in both asset classes.



Return Metrics

The overall performance of the portfolio was slightly negative, with a cumulative return of -0.38%. This loss is mainly attributed to a decline in Equities and Commodities, with a contribution of -0.51% and -0.72% to the overall performance of the Fund, respectively. The upswing in fixed income, caused by a decrease in world yields, with a contribution of 0.48%, however, lowered the overall loss of the fund. Looking at the ETFs, MSCI World and MSCI Emerging Markets registered the highest losses, decreasing the overall performance by -0.13% to -0.14%.

Individual stock picks resulted in a cumulative return of -0.07%, where the information technology sector notably boosted the funds performance with 0.25%, especially Everbridge (Total return of 16.07%). However, as the Energy, Financial and Material sectors performed very poorly last month due to fear of coronavirus and a warm winter, the overall performance of the fund was lowered by -0.46% by these sectors in January.

Risk Metrics

In terms of risk, when taking into account the benefits of diversification, our portfolio registered a daily VaR of 2.21%, falling below December`s VaR as a result of a lower discrete VaR of Equity. During the same period, the non-diversified VaR was at 3.75%, significantly above the maximum established threshold of 2.5%.

Equities depicted the highest individual VaR, which was around 2.67%, while Bonds and Commodities displayed slightly lower VaRs of 0.69% and 0.37%, respectively.

Valentina Heimann
Financial Markets Division

NIC Fund

Assets in Brief

Asset Class	Symbol	Comments
US Equity	**EEM**	The iShares MSCI Emerging Markets ETF was the worst performing Fund in the portfolio, yielding -6.15% total return. This heavy downswing compared to last months up resulted mainly from the fear of the coronavirus in China and its implications on global markets.
US Equity	**AMZN**	Despite the overall market weakness, Amazon's outstanding performance of 8.71% in January was mainly caused by the astonishing earnings report, which positively surprised investors and pushed the stock price up. Amazon web services were up 34%, subscriptions up 32%, and ‘other’ up 41%.
US Equity	**MELI**	Mercadolibre’s share price almost doubled in 2019 and anticipations on the earnings release on the 3rd of February hiked the price even further in January. High growth expectations on the online shopping trend and the general high degree of untapped potential for Mercadolibre’s marketplace in Latin America, such as an increase in internet access for the overall population, has held investors expectations on the release high. The introduction of the online payment service in 2003 generated significant growth for the stock.
US Equity	**EOG**	EOG Resources Inc. suffered in January just like the overall energy market and delivered a total return of -12.67%. As an energy stock, EOG is closely tied to oil prices, which were off their worst start since 1991. Indeed, WTI crude slumped 4.9% in the last week of January, capping a 15.6% January swoon, meanwhile Brent dropped nearly 12% last month. This drop was mainly caused by demand concerns in part because of the mild winter and in particularly by the fear of a coronavirus pandemic.
US Equity	**BNP**	The financial sector performed overall in January quite poorly. BNP Paribas was not an exception with a total return of -10.16% in January. The sector has mainly suffered from weakening oil prices and concerns around the coronavirus.
US Equity	**EVBG**	Everbridge Inc., which sells communications services for notifications of emergencies, is one of the few stocks that took great advantage of the anxiety around the coronavirus with its business model. Since the coronavirus outbreak in Wuhan on the 31st of December, Everbridge stock gained 16.09% over January, recovering from the rough December performance.
Commodity	**DBC ETF**	Our primary commodities index, DBC tracks a basket of 14 commodities. The ETF had negative performance over the last month, mainly driven by a slump in oil prices as result of less demand for oil in the energy market due to a mild winter and the fear of spreading corona virus.
US Equity	**V**	Visa Inc., an American multinational financial services corporation, positively performed over January with a total return of over 5%. Despite the coronavirus outbreak in China, the share price rose following a report that the payment company was planning big changes to its fee structure. Rates will decrease for some types of merchants while increasing for others, according to a report from Bloomberg.

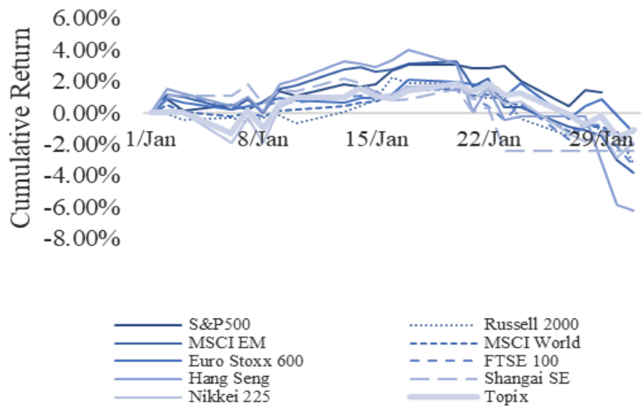
Valentina Heimann
Financial Markets Division

NIC Fund

Equities

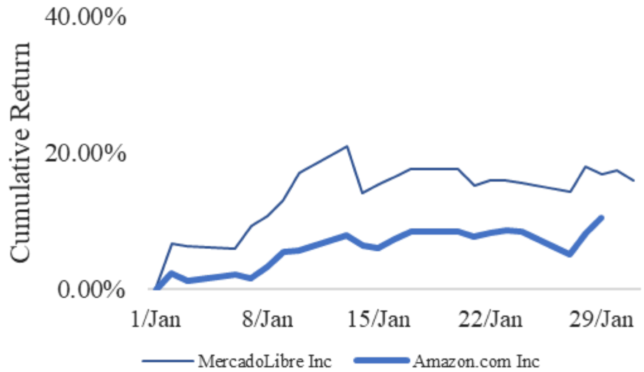
World Equities

Following 2019, Global Equities had a rather wavy January amid uncertainties of a US Senate impeachment trial, the coronavirus outburst in China and the approval of a much turbulent Brexit on January 31st. The FTSE100 closed January at 7,286, or 1.3% lower than at the beginning of the month as fears of the fast-spreading coronavirus have triggered a selloff by UK investors. Despite most of these events, the S&P500 went on to hit another all-time high on January 22nd at 3,337.77 but closed the month with a -0.16% return, whilst tech-heavy Nasdaq ended January just over 2% higher. The MSCI All Country World Index had a downward move of -0.68% for the period. On the other side of the world, Asian markets were also affected by the coronavirus, the NIKKEI 225 closed -0.49% lower at 23,205.18. The Hang Seng Index and SSE Composite Index took the biggest hits in the period, dropping by 6.66% and 10.93%*, respectively.



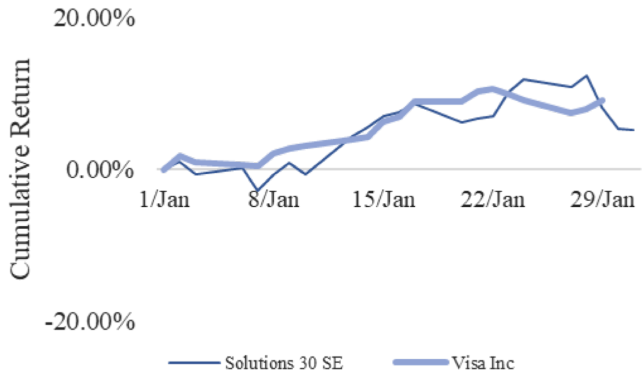
In Depth: Coronavirus Outbreak

The coronavirus has hit equity markets across the globe since January 20th, when China acknowledged the new virus could be transmitted from human to human. It has infected over 20,000 people worldwide and its death toll has exceeded 400 cases in China. As equity markets predict a slowdown in production and consumption, stocks of manufacturing, materials, and consumer goods companies were the mostly negative affected. The People's Bank of China (PBoC) lowered short-term interest rates and pumped CNY 150 bn into the Chinese economy as an attempt to relieve some of the pressure. During Chinese New Year, on January 31st, the World Health Organization classified the coronavirus as a global emergency, which led the index to its biggest drop since 2015, a 7.7% downward move. The winners so far have been healthcare and e-commerce stocks, as these industries are expected to be positively affected by eventual city lockdowns across the Chinese territory. Indeed, the SSE Health Care Index closed January 0.90% upward versus -11.4% for the overall index in the same period.



Our Performance

Geopolitical events negatively affected equity markets. As a result our portfolio performed poorly in January, with a negative return of -0.35%. Technology and e-commerce firms persisted the scenario, which led Mercadolibre Inc. to be the biggest equity contributor to our portfolio, with a monthly return of 15.92%. Other strong performers were Amazon, with an upward move of 8.71%, and Visa Inc. with a monthly return of 4.11%, following a 16% gain of the past three months. The iShares MSCI Emerging Markets, led by many Chinese companies such as Alibaba Group, Tencent, China Construction Bank Corporation, was damaged by the abovementioned coronavirus and had a negative return of -6.15%, dragging down our portfolio performance by 0.13%.



**Due to the unusual scenario of the coronavirus outbreak during the Chinese New Year, the first trading day of February was considered for the monthly return of SSE Composite*

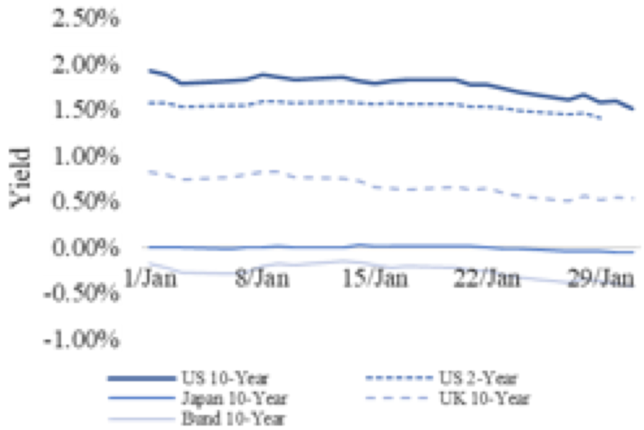
Henrique Oliveira
Financial Markets Division

NIC Fund

Fixed Income

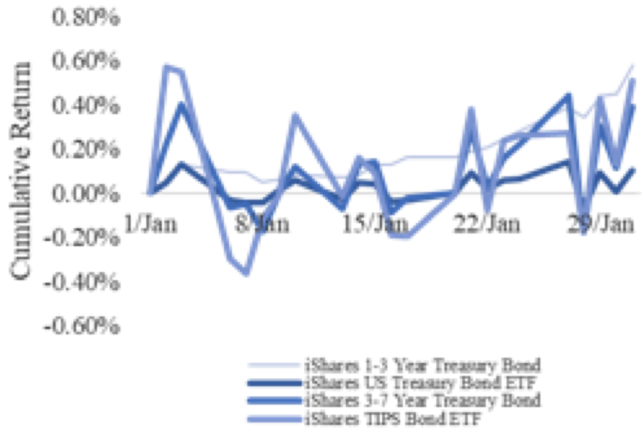
World Yields

Global yields continued to fall amid the spread of Coronavirus. The fear of a future pandemic and the isolation measures taken in China to stop the spread of the virus will have negative affect on trades and travel. The pessimist news is expected to harm the already crawling Chinese economy a few days after the ease in trade war and to led risk-averse investors to shy away from high-yield bonds to instead allocate their wealth into safe-haven assets.
T-bill yield curve inverted, 10-year yield dropped by 16 bps to 1.52% at month-end, falling short of the the 1.55% 3-month yield. Meanwhile in the Eurozone, disappointing economic data caused a decrease in Italian bonds, 10-year yields 0.94%, 29bps fewer than end-year levels. Similarly, the German bund slipped 9 bps to – 0.43% whilst the 10-Year UK Gilt remained was steady at 0.52%.



In Depth: Green Bond Issuance hit Record in 2019

Global green bonds and loan issuances surged to a USD 255 bn in 2019, almost 50% more than 2018 according to Reuters. The trend is set to persist in the next few years as the current offer cannot satisfy investors demand, especially millennials who are particularly engaged in investing their wealth in companies or states committed to reduce their environmental footprint. CBI forecasts 2020 market issuance as high as USD 400 bn for 2020. Sovereign green bonds are considered a good investment opportunity as they tend to yield more than traditional government bonds and favor the transition to a low-carbon economy. France for instance was the first triple A rated country to issue EUR 7 bn green bonds with a 22-year maturity yielding 1.75% in 2017. Today it only yields 0.04% and rates could even go below 0 following other non-green bonds issued by the French government that are already deep into negative territories. Following the strong interest, the country is set to issue an additional EUR 8 bn in 2020.
Green bonds are also of interest for corporations as it allows large firms such as Apple to borrow at even lower rates than mainstream corporate bonds. The Californian tech company issued EUR 2 bn in green bonds last November. A 6-year zero-coupon bond yielding 0.032% and a 12-year bond that will yield 0.565%. This is significantly lower than their AA+ 10-year note which yields 2.27% issued on the same day.



Our Performance

The decrease in world yields, especially in American bonds, led bond prices to surge in January. Thus, fixed income funds had a strong performance. As a result, our fixed income holdings that account for nearly 51% of our portfolio were the best contributors to NIC Fund's performance, in a month where equities damaged our return. Indeed, iShares TIPS Bond and iShares 3-7 years T-bills ETFs respectively returned 2.14% and 1.84% last month.

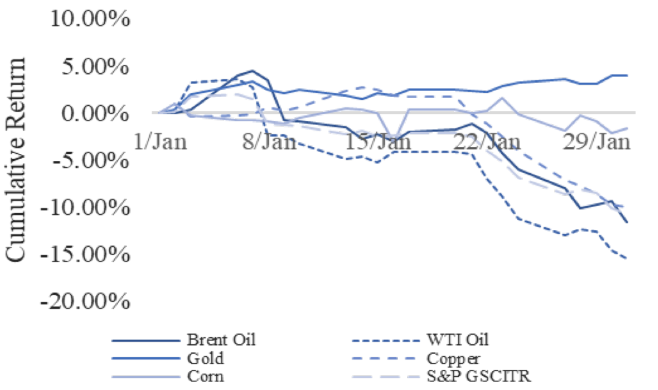
Maxime Hozé
Head of Financial Markets Division

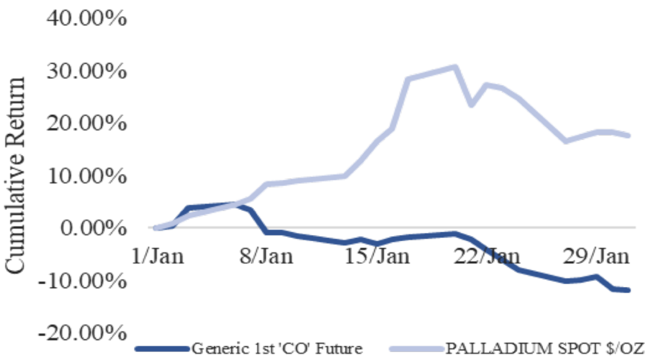
NIC Fund

Commodities

January Round-Up

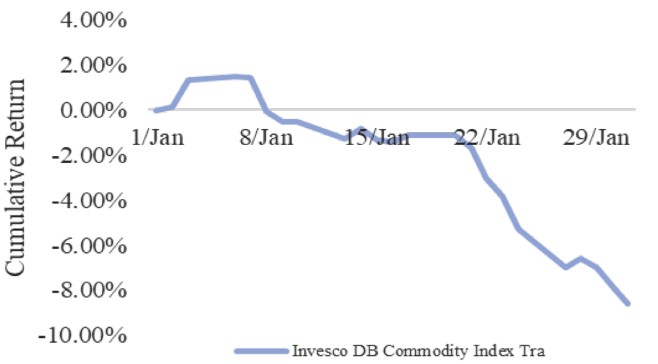
During the month of January, the S&P GSCI Total return index, the world's leading measure for commodity prices and inflation movements, has declined by 10.9%. Commodity prices have come under heavy selling pressure amid growing concerns that the outbreak of the coronavirus will hit China's economy. The Goldman Sachs index of commodity prices has dropped 6.4% since the 17th of January, when headlines about the virus began to spread across international media. Copper, an industrial metal that is seen by many investors as an economic bellwether, declined for 12-straight sessions, the longest sell-off on Bloomberg records of trade on the London Metal Exchange dating back to 1986. Oil prices fell on Friday 31st of January and were on track for a fourth consecutive weekly loss, as markets grew more concerned about the economic damage of the new highly contagious virus. Brent crude fell 21 cents to USD 58.08 per barrel. US West Texas Intermediate crude fell 58 cents, or 1.1%, to settle at USD 51.56. WTI posted a fourth straight week of losses, its worst month since May. "In our view, there still remains considerable uncertainty on the duration and economic impact of the virus," said Harry Tchilinguirian, global oil strategist at BNP Paribas London. In contrary to these movements, gold prices edged higher at the end of the month and were on track for their biggest monthly gain since September, as arising concerns of an economic slowdown supported the safe-haven metal. Spot gold rose 0.75% to USD 1,585.8 per ounce. The metal gained 4% so far in January, on course for its best month since August. US gold futures rose 0.1% to USD 1,590.8 an ounce. Palladium was down 0.7% at USD 2,294. Prices were set to gain 18% this month, the best since November 2016, but were down 5.7% in the last week of January.





Outlook for February

The Organization of Petroleum Exporting Countries (OPEC) wants to extend oil production cuts from March until at least June, and could deepen the reductions should demand for oil in China be significantly reduced by the spread of the virus, OPEC sources said. The OPEC+ group is also considering holding a ministerial meeting over Feb. 14-15, one of the OPEC sources said, ahead of a previously scheduled meeting in March. "The market needs assurances that the supply/demand equation remains in balance for prices to hit a floor. This suggests a commitment from OPEC not just to extend oil supply cuts, but even implement deeper ones beyond March," said FXTM analyst Hussein Sayed.



Our Performance

In January, we maintained an allocation of 7.70% in the Invesco DB Commodities Benchmark ETF, which is 0.74% below our benchmark weight of 8.44%. The index's poor performance diminished the return of our portfolio by 0.72%. Moreover, just like the overall energy market, EOG Resources Inc. suffered in January delivering a total return of -12.67%.

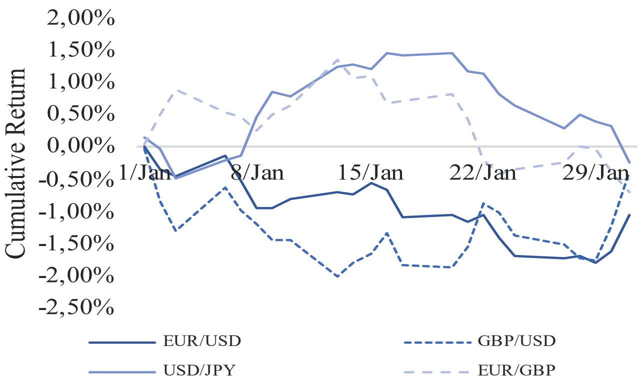
Francisca Fernandes
Financial Markets Division

NIC Fund

Currencies

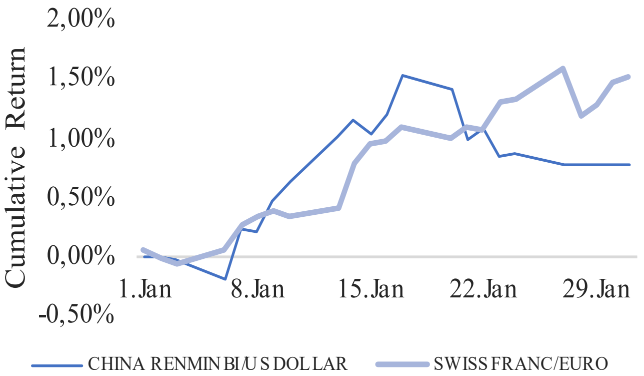
World Currencies

As we enter the new year we unsurprisingly receive the news that the ECB will continue with its dovish policies, having the rise in inflation as their main focus. Combined with the rest of Europe's slowing growth, in part attributable to the consequences of the ongoing trade war, the downtrend continued for a fifth consecutive week for the euro, pressuring it to fall by 1.07% relative to the dollar, closing the month at 1.102 USD. With Brexit finally happening at the end of the month and the BOE deciding to leave the rates unchanged at 0.75%, the pound rose to 1.189 EUR and 1.321 USD. Its value is expected to remain relatively stable until further developments on the trade deal with Europe come to light, leaving the possibility for a lot of volatility. Whether an agreement will be reached by the end of the year, as aimed to by prime minister Boris Johnson, remains to be seen. Despite performing rather well in January against the Euro and the pound, forecasts for the Dollar are less optimistic for the rest of 2020. As major central banks have stopped cutting rates, the gap to US interest rate yields closes down and in addition investors seem to be leaning towards safe-haven currencies such as the Japanese yen. This is reflected in the 0.24% loss in value of the dollar relative to the yen for January.



In Depth

One month down and 2020 has already kicked off with enough incidents going on to cover an entire year. With talks on the trade war, Trump's impeachment, conflicts with Iran and Brexit happening at the end of the month, it was surprisingly the looming threat of the Coronavirus that stole the show. Just as equity and fixed-income markets reacted to it, so can we see it's effect on foreign exchange. As the World Health Organization officially declared the Coronavirus as a global emergency, investors rushed to buy safe-haven assets and commodity-linked currencies such as the Australian dollar, Canadian dollar and the New Zealand dollar. Yet with volatile oil prices due to fear of the economic impact of the virus, these currencies have also taken part in the January roller coaster. Other classic safe-haven currencies have also seen strong demand over the month, with the Swiss franc gaining 1.53% on the euro and the Japanese Yen strengthening against the US dollar. Meanwhile, as China's economy is showing some signs of stabilization and combined with the efforts of monetary and fiscal policy, the yuan appreciated by 0.76% against the US dollar, but the full effect of the fears surrounding the Coronavirus are yet to take a hit on the Chinese currency, leaving it vulnerable to possible downward slides until the crisis passes.



Our Performance

We currently hold no currency related assets in our portfolio.

Patricio Drexhagen
Financial Markets Division

Extras

Hot Topic

Pre-trade Deal Implications for UK Economy After Formal Brexit

Benedict Minkner
Investment Banking Division

"The UK answer will be fundamental to the level of ambition of our future relationship and the UK must know this. It will be up to the UK to decide."

– Michael Barnier
EU Brexit negotiator

After the UK has formally left the European Union, speculations and predictions about consequences for both involved parties are now reignited. Particularly, economic effects on UK are subject of discussion. What does the future hold for the British economy?

Clearly, leaving the EU will introduce new costs of trade between the UK and the EU that make it harder for UK firms to do business with the rest of Europe. However, the extent to which trade barriers increase will depend upon the nature of the post-Brexit relationship the UK agrees with the EU.

Boris Johnson's Conservative Party proposes a deal in which the UK will leave the single market and the customs union while maintaining tariff-free and quota-free trade with the EU for almost all products. Estimations suggest that this will lead to a 6.4% decline income per capita ten years after the implementation of the deal relative to the no-Brexit scenario. For comparison, the Labour-favoured soft Brexit scenario that keeps the UK in the customs union and perhaps also in the single market is estimated to cause a 4.3% decline.

Against those estimations one line of argumentation insist that Brexit will be an economic disaster while more optimistic positions around Chancellor Sajid Javid claim that UK economy will continue to grow by 2.7% a year or faster, which exceeds the 2% average since the 2008 financial panic.

Followers of the *secular stagnation* argument argue that economic downturn in Britain as in every other developed country will be inevitable due to productivity collapses caused by unfavorable demographic conditions. Therefore Brexit should be executed as soft as possible to prevent disastrous economic stagnation. In the last decade UK's productivity growth was primarily realized by labor force expansion. However, this trend is expected to wind down soon, particularly if Brexit will mean extensive immigration limitation as suggested by Prime Minister Boris Johnson.

Conservative Javid on the other side emphasizes that instead policies such as tax and regulatory reform will enable the UK to foster growth. Somewhat similar to Trump's policies in the US, it is believed that job creation and unlocked business investments through smart policy making can offset a Brexit shock and beyond generate larger growth levels.

Yet, the final conditions of UK's parting and thus its economic implications are to be negotiated upon until the end of December 2020. In this early *chest-beating* phase both parties are to be expected to continue to stand firm and appeal to domestic audiences. In the end, surely "the U.K. will have to move a lot and the E.U. will have to move a little", as Sam Lowe from the Centre of European research states.

Benedict Minkner
Investment Banking Division

Extras

Hot Topic

Deadly Coronavirus Continued to Disrupt the Volatility of Oil Prices

Francisca Fernandes
Financial Markets Division

"I think we have to prepare for a tough and uncertain macro. We do that in our company by making sure that our investments are resilient […] I think that's the best way to inoculate ourselves against an uncertain future" management."

– Ben van Beurden, CEO of Royal Dutch Shell

After sharp losses around the world, investors continue to assess the long-term economic effects of the coronavirus epidemic. The deadly virus is having a huge impact on stock markets and even more on oil prices, which have been under pressure following the its rapid spread. The magnitude this will have on crude demand remains still unclear, but Chinese energy executive said that oil consumption in the country in February could be 25% lower than a year earlier, being equivalent to 3% in global consumption.

Both Brent and West Texas Intermediate crudes suffered losses amid the coronavirus outbreak, but things could still get worse. According to Andy Lipow, president of Lipow Oil Associates, "There could be another $5 a barrel downside in this because we simply don't know the extent of the virus and how long it's going to last."

The change in demand and the drop in prices are jolting the OPEC led by Saudi Arabia and ally producers including Russia into action to support prices. The group's advisory body has recommended that they accelerate their existing supply cuts by an additional 600,000 barrels a day to a total of 2.7m b/d for the first half of 2020.

Citigroup energy analysts cut their price expectations for crude from the high USD 60s for Brent this year to the USD 50s, including an average of USD 54 for the first quarter and USD 50 for the second quarter. It is getting harder to find optimism as there is no guarantee that the proposed cuts will rid the oil market of its current malaise.

The impact of the spread of coronavirus can also be seen on Junk-rated energy bonds. Oklahoma-based Laredo Petroleum's USD 600 m bond, which was priced at 100 cents on the dollar in mid-January, dropped to as low as 90 cents after just a week of trading. Energy and natural resources companies accounted for the largest share of defaults in the US bond market through to the end of the third quarter last year according to S&P Global. The probability of further defaults rose over the past month, according to Credit Benchmark.

Laredo Petroleum Inc. LPI and Range Resources Corp. RRC were two of the energy companies that raced to borrow in a newly emboldened speculative-grade, or junk-bond, market. But as news out of China worsened, bonds from the two companies traded as much as 10% lower, and after rallying a bit still were fetching average prices of only about 92 cents on the dollar, according to MarketAxess

The CEO of Royal Dutch Shell is preparing for a tough and uncertain energy market. "I think we have to prepare for a tough and uncertain macro. We do that in our company by making sure that our investments are resilient […] I think that's the best way to inoculate ourselves against an uncertain future" said Ben van Beurden.

All else aside, a growing part of stakeholders is pushing asset managers to reduce their exposure to fossil energy producers to address climate risks. BlackRock said earlier this month it would exit investments with "high sustainability-related risk" like thermal coal and would launch new fossil-fuel investment products. These kinds of corporate moves, along with amplifying rhetoric from activists calling for a low-carbon economy, are harming the oil industry.

Francisca Fernandes
Financial Markets Division

Thank you!

Visit www.**novainvestmentclub.com** for more updates.

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