PRESS RELEASE

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Saxo Q1 Outlook: The Great Climate Shift

Saxo Bank, the online trading and investment specialist, has today published its Q1 2020 Quarterly Outlook for global markets, including trading ideas covering equities, FX, currencies, commodities, and bonds, as well as a range of central macro themes impacting client portfolios.

“For the first time since WWII we sense a shift in which climate and the environment – not growth – will become the priority of governments and their citizens, as shortages of food, clean water and air become existential questions.” **says Steen Jakobsen, Chief Economist and CIO at Saxo Bank.**

“The long-term reality is that the changing climate is telling us that the cost of the present ‘model’ of economic growth is turning negative. Not only at the margin, but probably full-blown negative in terms of the costs to society and the environment.”

“It is increasingly clear that our measures of economic growth are inadequate in predicting the total costs of our activity when factoring longer-term resource depletion and environmental harm. This is coupled with the lack of price discovery over the last decade, as central banks have kept our unsustainable economic activity levels at maximum throttle to avoid a reset – eroding the long-term potential of our economies and a harmful lack of productivity.

“The consensus economic forecasts for 2020 rely on a cocktail of promises, including low inflation and low rates forever, an abolishment of price discovery, a full acceptance of monopolies in technology and non-commitment to reduce inequality. The output of this increasingly toxic cocktail is permanently low growth, close to zero productivity and a monetary policy with no exit path, as seen recently as the US Fed became not only lender of last resort for the repo market but also tilted toward full monetisation of the US federal deficit.

“In 2020 there are three factors that will change the status quo: Firstly, a change of US President would create a new impulse both politically and economically. Secondly, credit failures as the blown-out value of the market becomes an issue, the loss of control over repo by the Fed generates massive event risk in credit space with the US shale sector being most exposed. Finally, the combination of climate sending a signal of distress – raising the cost of food, water and clean air – with an enormous underinvestment in infrastructure means the market has become complacent and increases the risk of a spike in volatility when the next disaster strikes.”

Against the backdrop of a growing climate crisis, Saxo’s main trading ideas and themes for Q1 include:

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Climate awareness will drive a green mega trend in equities

Climate crises such as the Australian bush fires are mobilising individuals, businesses and governments to fight climate change. The growing shift in policy and behaviour coupled with technological advancement lowering the cost of green technologies is making green stocks increasingly attractive but carry risks. Cyclical sectors such as solar, wind and EVs are likely to be more heavily impacted in a recession, while nascent industries such as fuel cells, bioplastic and food present more idiosyncratic risks. Green stocks have significant potential but investors should carefully weigh-up their investments.

Peter Garnry, Head of Equity Strategy, said "With millennials demanding action on climate change, we are sensing the beginning of a new period that creates great opportunities in equities.

"Governments will increase investments and subsidies for "green" industries, starting a new mega trend in equity markets. We believe that these green stocks could, over time, become some of the world's most valuable companies — even eclipsing the current technology monopolies as regulation accelerates during the coming decade. Investors should consider tilting their portfolios towards green stocks so they don't miss this long-term opportunity.

"Meanwhile, central banks and governments have decided to throw out the old playbook of not adding stimulus in the late stage of an expansion in which the labour market is tight. Both monetary and fiscal policy is readily being deployed in 2020 across all the world's largest economies. This is not the time to be underweight equities."

The US dollar is a tough one to turn

The dollar is looking resilient in Q1 2020 on the back of solid US economic performance in 2019 which saw overall GDP growth averaging 2.4% for the first three quarters of the year. However, the prospect of a slowing US economy, budget deficits and an election could weigh on the dollar's prospects.

John Hardy, Head of FX Strategy, said: "The US dollar is starting off 2020 in resilient shape. It has defied expectations that the Fed's turnaround over the course of 2019 and acceleration into year-end would have resulted in a far weaker currency, especially considering that it has outpaced the easing from central banks elsewhere.

"Why the US dollar has not weakened perhaps speaks to the residual strength in the US economy relative to global peers. While its manufacturing sector has suffered under the weight of Trump's tariffs and a slowdown in US shale oil and gas development, the dominant services sector remained resilient and Trump's aggressive trade stance saw US trade deficits narrowing sharply in the second half of 2019.

“Many of the USD-positive drivers noted above look well entrenched as 2020 gets under way, but we still look for a low ceiling to what has effectively been a flat US dollar over the last 18 months. As the year wears on, we would look for a slowing US economy, a related chopping of US interest rates, ongoing Fed monetisation of US budget deficits and, not least, the US presidential election to weigh on the US dollar’s prospects.

“Another potential headwind comes from the Fed’s actions to shore up liquidity in late 2019. The provision of Fed liquidity and the risk that this eventually results in inflation and more highly negative US real rates look enough to finally turn the USD lower.”

Climate-driven volatility will drive green supply and demand

Climate change is driving volatility and having a significant negative impact on Asian cities. Floods, droughts and wildfires are likely to drive consumer demand in sustainable companies and supply spurred through government action on climate change. Investors should therefore look to get exposure on sustainability and impact investing themes.

Kay Van-Petersen, Global Macro Strategist, said: “It seems like each year volatility in temperatures, seasons and weather become more extreme. In Asia for example, mega-cities such as Jakarta are now at risk of sinking and Delhi experienced freezing temperatures in December.

“Climate disasters tend to act like volatility in the markets, whereby volatility begets more volatility. One disaster raises the probability and potential magnitude of another type of disaster.

“This increasing volatility is driving at least two key structural driving forces. The first will be demand driven. More and more consumers will want to use their spending capital to vote for companies that practice sustainability. For instance, probably about 5% of the US’s 330 million people are currently vegetarians, but that ratio that is likely to grow. Companies and entrepreneurs that are proactive with regard to consumer sustainability lifestyle choices will thrive and move ahead.

“The second will be supply driven. Governments are coming to fully understand that we are likely past the tipping point where the cost to do nothing with regard to sustainable growth is much greater than the cost of addressing it now. To put it another way, governments need to be proactive on the climate crisis - spurring innovation, R&D and investments through subsidies, grants and tax breaks.”

Commodities in the crosshairs of climate and inflation

Global commodities face a potentially volatile 2020, given the combination of growth concerns, geopolitical tensions, climate change and inflationary pressures. While demand for key cyclical commodities remains weak, we see the supply side also facing multiple challenges due to social unrest and climate change.

Ole Hansen, Head of Commodity Strategy, commented:

- **Agriculture:** "We have witnessed several years of ample supply with stable-to-lowering prices. In fact, the last period of tightness among the key crops was back in early 2010 when soaring wheat prices helped trigger the Arab Spring. While global demand and supply have both risen during the past decade, the global supply chain will be left vulnerable to a sudden weather-related drop in yields.

  "As we enter 2020, ample supply and weak price action have resulted in negative returns on most exchange-traded funds with broad-based exposure to key agricultural commodities."

- **Gold:** "We see gold further building on last year's strong 18.5% gain as the technical and fundamental outlook continues to improve. However, after racing higher at the beginning of January, we may see the metal spend most of the first quarter consolidating above $1500/oz before moving higher to peak at around $1625/oz later in the year. The short-term consolidation also takes into consideration the elevated level of hedge fund positions. These have become quite extended near record levels and, in the short term, could act as a drag on price."

- **Brent crude:** "Brent crude oil is likely to remain stuck in the $60s through the first half of 2020, before moving higher in the second. The December 6 OPEC+ decision to maintain and deepen production cuts through the first quarter is likely to offset any potential growth concerns or renewed US-China trade worries.

  "We see Brent crude oil at $75/b by year-end, as inflation picks up and the dollar weakens. Any short-term weakness, perhaps from speculators exciting speculative long positions, is likely to be limited. With continued threats to supply from the Middle East and Libya, the market is unlikely to reduce by much."

Europe is getting ready for green QE

As climate consciousness fuels public acceptance for more active fiscal and monetary policy, we see the foundations for the implementation of a massive monetary and fiscal climate package and political change being laid by the ECB in 2020. This shift should be reinforced by national governments as climate change influences political choices – as a result, we also think that Germany turning green will be the main political gamechanger in the coming years.

Christopher Dembik, Head of Macroeconomic Analysis, said: "2020 will lay the foundations for a massive European monetary and fiscal climate package likely to be implemented in 2021. Over the past months, most central banks have pointed out the importance of climate change, such as the Bank of England which has warned of "a climate Minsky moment".

"However, green QE from the ECB is not going to save the planet and decarbonize the economy by itself. The ECB has mostly three options to launch green QE: First, favoring green bonds as part of the revived QE programme (although there is just not enough issuance out there yet). Second, applying a punitive "haircut" to bank collateral assorted to high carbon intensity activities (although this would further weaken the European banking sector). Thirdly, targeting transition bonds for dirty companies that try to become greener (although this raises concerns among climate activists).

"Contrary to what has happened over the past 10 years, central banks cannot be the only player in town to fight climate change. Governments will need to step in —and the current evolution of the yield curve is creating a very attractive environment for fiscal stimulus oriented to fund green projects."

Building a sustainable finance ecosystem

As we begin 2020, we are on the cusp of an inflection point where the economic and environmental losses and social impact of maintaining the status quo are unsustainable. While pressure mounts, climate action could be one of the most transformative and disruptive challenges faced by the global economy.

Eleanor Creagh, Market Strategist, commented: "Creating a sustainable finance ecosystem requires a huge reallocation of capital. Investors and corporates who do not gear their portfolios towards more sustainable business models risk facing large losses in the coming decades: regulatory changes could leave many current operating models unviable. Over a third of global capital already has some form of ESG mandate, putting many companies and countries on the wrong side of that mandate on the backfoot. If companies fail to adjust, they will cease to exist.

"The green transformation will also drive many positive advances as the need for adaptation spurs the adoption of policy solutions aimed at funding clean energy projects, water security, sustainable infrastructure developments and green technological innovations such as emissions capture and energy storage breakthroughs.

"These new climate industries not only provide jobs and economic gains but also generate a positive impact by providing cleaner air, preserving delicate ecosystems and improving human health. The climate crisis is defining a future generation, and as the cohort of millennial and Gen-Z investors grows financial performance will no longer be the only investment goal, increasing demand for positive impact investments that align with broader sustainable objectives."

To access Saxo Bank's full Q1 2020 outlook, with more in-depth pieces from our analysts and strategists, please go to: www.home.saxo/insights/news-and-research/thought-leadership/quarterly-outlook

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About Saxo Bank

Saxo Bank Group (Saxo) is a leading Fintech specialist focused on multi-asset trading and investment and delivering 'Banking-as-a-Service' to wholesale clients.

For 25 years, Saxo's mission has been to democratise investment and trading, enabling clients by facilitating their seamless access to global capital markets through technology and expertise.

As a fully licensed and regulated bank, Saxo enables its direct clients to trade multiple asset classes across global financial markets from one single margin account and across multiple devices. Additionally, Saxo provides wholesale institutional clients such as banks and brokers with multi-asset execution, prime brokerage services and trading technology, supporting the full value chain delivering Banking-as-a-Service (BaaS).

Saxo's award winning trading platforms are available in more than 20 languages and form the technology backbone of more than 100 financial institutions worldwide.

Founded in 1992 and launching its first online trading platform in 1998, Saxo Bank was a Fintech even before the term was created. Headquartered in Copenhagen Saxo Bank today employs more than 1500 people in financial centers around the world including London, Paris, Zurich, Dubai, Singapore, Shanghai, Hong Kong and Tokyo.