BARINGS INVESTMENT INSTITUTE

WEEKLY UPDATE

20 September 2019

Overview

Global Growth: *The OECD lowered its 2019 global growth forecast again in September, to 2.9% from 3.2%, after downgrading the growth outlook four months ago. The 2020 growth forecast was lowered to 3% from 3.4%. The OECD argued weaker growth prospects reflect escalating trade policy tensions that are taking a toll on confidence and investment, adding to policy uncertainty and weighing on risk sentiment in financial markets. While monetary policy is expected to remain accommodative in advanced economies, the OECD called for more fiscal policy support.*

Repo Squeeze: *A scarcity of cash caused overnight repo levels to spike earlier in the week. While elevated overnight repo levels typically occur near quarter-end or year-end when dealer balance sheets are constrained, there were a confluence of events this week that led to the volatility. The main drivers were a corporate tax payment whereby money market investments that matured on the day the taxes were due were liquidated to pay the tax bill and not reinvested. At the same time, a significant amount of new issue Treasuries settled requiring cash to fund the purchases. The combined effect was a scarcity of cash in the system, which caused repo rates to spike. The Fed responded by injecting liquidity into the system and lowering the IOER and overnight repurchase rate by 30 bps at the Wednesday FOMC meeting to alleviate money-market strains.*

FOMC Meeting: *The Fed cut the funds rate by 25 bps to a range of 1.75%-2.00%, as expected. The policy statement was little changed, although the vote was 7-3 to lower rates, with two members preferring no cut and one member seeking a 50 bps cut. The updated dot plot shows no further rate cuts for 2019 and 2020. Despite concern about the growth outlook, the median GDP projection for 2019 increased .1 to 2.2%, while the inflation target of 2% is not expected to be reached until 2021. The tone of the press conference was not as dovish as the market wanted, but Fed Chairman Jerome Powell said more extensive cuts may be needed if the economy weakens.*

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Key Financial Indicators						As of:	9/18/2019
Rates	**Yield**	**1 W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
Fed Funds	2.25%	0 bps	0 bps	-25 bps	-25 bps	25 bps	-25 bps
3 Month USD Libor	2.16%	3 bps	2 bps	-23 bps	-48 bps	-18 bps	-65 bps
3 Month Euribor	-0.40%	3 bps	2 bps	-7 bps	-9 bps	-8 bps	-9 bps
3 Month U.S. T-Bill	1.96%	1 bps	13 bps	-21 bps	-43 bps	-17 bps	-44 bps
2-Year U.S. Treasury	1.75%	8 bps	27 bps	-11 bps	-70 bps	-104 bps	-75 bps
10-Year U.S. Treasury	1.78%	5 bps	24 bps	-27 bps	-82 bps	-127 bps	-90 bps
10-Year German Bund	-0.51%	6 bps	21 bps	-21 bps	-58 bps	-95 bps	-75 bps
10-Year U.K. Gilt	0.64%	1 bps	8 bps	-22 bps	-58 bps	-90 bps	-69 bps
10-Year JGB	-0.17%	4 bps	7 bps	-4 bps	-12 bps	-28 bps	-16 bps
Fixed Income	**Yield**	**OAS**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
Barclays Capital U.S. Government-Treasury	1.83%	N/A	-0.3%	-1.5%	2.0%	9.7%	6.9%
Barclays Capital U.S. TIPS	1.98%	N/A	-0.2%	-1.2%	1.9%	6.9%	7.3%
Barclays Capital U.S. Aggregate	2.37%	46	-0.2%	-0.9%	2.2%	9.7%	7.8%
Barclays Capital Global Aggregate	1.37%	43	0.0%	-1.0%	1.8%	7.1%	6.2%
Barclays Capital U.S. ABS	2.12%	33	-0.1%	-0.3%	0.9%	5.2%	3.9%
Barclays Capital U.S. MBS	2.55%	45	-0.1%	0.0%	1.4%	7.6%	5.3%
Barclays Capital U.S. Corporate Investment Grade	3.02%	114	-0.1%	-1.0%	3.4%	12.3%	12.1%
BAML Euro Corporate Investment Grade	0.42%	110	-0.2%	-0.7%	1.5%	5.9%	6.5%
Barclays Capital U.S. Corporate High Yield	5.58%	356	0.2%	1.9%	2.3%	6.8%	11.7%
BAML European Currency High Yield Non-Financial	3.13%	362	0.3%	1.5%	2.0%	4.7%	8.9%
CS U.S. Leveraged Loans	6.33%	471	0.2%	0.6%	1.0%	3.5%	6.4%
CS Western European Leveraged Loans Non-USD	4.62%	414	0.1%	0.5%	1.0%	2.9%	3.6%
JPM CEMBI Broad Diversified	5.15%	339	0.1%	0.6%	2.3%	11.3%	10.4%
JPM EMBI Global Diversified	5.23%	332	-0.1%	0.4%	2.5%	13.5%	13.2%
JPM GBI-EM Global Diversified	5.25%	N/A	0.7%	0.9%	2.5%	13.7%	8.9%
Equities	**Price**	**Div Yield**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
S&P 500	3,006.73	1.85%	0.2%	4.3%	3.6%	5.6%	21.7%
Euro STOXX 600 (Local)	389.41	3.20%	-0.1%	5.4%	1.2%	2.8%	15.3%
U.K. FTSE 100 (Local)	7,314.05	4.50%	-0.3%	2.8%	-1.7%	0.2%	8.7%
Japan Nikkei 225 (Local)	21,960.71	2.14%	1.7%	7.6%	4.7%	-6.2%	9.7%
China Shanghai Composite (Local)	2,985.66	2.33%	-0.8%	5.7%	3.3%	10.6%	19.7%
MSCI AC World (Local)	526.31	2.52%	0.3%	4.7%	2.3%	4.8%	18.5%
MSCI Emerging Markets (Local)	1,021.36	2.91%	0.3%	4.9%	0.4%	3.4%	9.6%
Commodities/Currencies	**Price**	**1W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
S&P GS Commodity Index	417.01	3.2%	5.3%	1.6%	-4.0%	-10.9%	11.4%
WTI Crude ($/bbl)	58.07	4.3%	5.9%	7.8%	-1.7%	-16.9%	28.6%
Copper ($/lb)	2.60	-0.1%	0.2%	-4.1%	-10.6%	-4.3%	-1.2%
Gold ($/oz)	1,503.50	0.9%	-0.8%	12.1%	15.2%	25.3%	17.6%
U.S. Dollar Index	98.56	-0.1%	0.4%	0.9%	2.1%	4.1%	2.5%
Euro (USD/EUR)	1.11	0.6%	-0.4%	-1.1%	-2.5%	-5.5%	-3.3%
British Pound (USD/GBP)	1.25	1.1%	2.8%	-0.5%	-5.6%	-5.1%	-2.0%
Japanese Yen (Yen/USD)	108.23	0.4%	1.7%	-0.3%	-2.9%	-3.7%	-1.4%
Chinese Yuan (CNY/USD)	7.09	-0.4%	0.6%	2.3%	5.6%	3.3%	3.2%

Source: FactSet and Bloomberg

Economics

UNITED STATES

Regional PMIs: Regional PMIs were mixed relative to consensus estimates. The Empire Manufacturing Index fell more than expected in September as readings for new orders and shipments deteriorated. The gauge of capital spending expected six months from now tumbled the most in three years. The Philadelphia Fed Index decreased less than expected in September as domestic activity indicators were resilient while sentiment deteriorated.

Consumer Sentiment: The initial reading of the University of Michigan consumer sentiment survey for September increased more than forecast. The rebound from a plunge in August shows consumers remain resilient, supported by a strong labor market and strength in August retail sales, which increased more than forecast.

Housing: New home construction was better than expected in August with housing starts and building permits hitting a 12-year high. A solid labor market and lower mortgage rates are supporting sales and construction activity. Existing home sales unexpectedly increased in August as improved affordability offset uncertainty over the economic outlook.

EUROPE

EZ Inflation: Euro-area inflation held steady in August as CPI increased 1% Y/Y. The core rate was also unchanged from July at .9% Y/Y. Weak inflation well below the ECB target suggests a prolonged period of accommodative monetary policy.

BOE Meeting: As expected, the BOE kept its current policy settings on hold and warned of an adverse impact from a no-deal Brexit. Rates may rise if the U.K. and EU reach a deal but could fall under a no-deal scenario or more delays.

U.K. Inflation: Inflation accelerated less than expected in August. Headline CPI increased 1.7% Y/Y, down from 2.1% in July. The core rate slowed to 1.5% Y/Y from 1.9% in July, dragged lower by recreation and clothing costs. The lack of inflation pressure gives the BOE flexibility as they expect inflation to remain below target until the end of 2020.

ASIA - PAC

China Activity: Economic activity weakened more than expected in August. Industrial production slowed to 4.4% Y/Y from 4.8% in July. Fixed asset investment growth fell to 5.5% YTD from 5.7% in July and retail sales disappointed, slowing to 7.5% Y/Y. The weaker data suggests the slowdown is deepening and more policy support may be needed.

BOJ Meeting: The BOJ kept policy settings unchanged, as expected. The next policy meeting on October 31 is a key event as the central bank will be able to analyze economic and price developments from the October 1 sales tax hike.

Japan Trade: Exports declined for the ninth-consecutive month in August, falling 8.2% Y/Y. Weaker demand in Asia for autos and semi-conductor equipment continues to weigh on exports. Imports declined 12% Y/Y in August, marking the fourth-straight month of decline. Trade uncertainty and weakness in China's economy remain downside risks for Japan.

Policy

UNITED STATES

EU Tariffs: The World Trade Organization has cleared the U.S. to impose tariffs on the EU as part of a long-running dispute over subsidies Airbus has received from France, Germany, Spain and the U.K. While it is not yet clear at what rate the tariffs will be set, the USTR has already published two lists of $25 billion worth of imports each that could be affected by the tariffs. The EU has a parallel case against Washington state subsidies for Boeing, with they are expecting a final decision on that case in the coming months. This development comes amid the U.S. stance that this time is being treated as an opportunity to "reset" the relationship amid a new EU Commission taking office on November 1.

Japan Trade: The U.S. and Japan are nearing a trade deal, with recent media reports suggesting a joint statement by Prime Minister Shinzo Abe and President Donald Trump is forthcoming at a meeting later this month. Under the deal, Japan will abolish duties on U.S. beef, pork and wheat, aligning them with the TPP. In return, the U.S. will promise not to impose additional tariffs or quotas on autos, while relaxing restrictions on Japanese beef imports.

Bank Regulation: The FDIC approved a proposal to eliminate Obama-era rules that required banks to hold margin against swap and derivative trades with their own affiliates. The move is expected to free an estimated $40 billion among the largest swap dealers. Industry lobbyists have long argued for a revocation of the rule amid its redundancy.

Emission Regulation: President Trump is revoking California's ability to set vehicle emission standards in lieu of a single federal standard that aims ease requirements originally set under the Obama administration in 2012, in effect lowering auto prices but increasing gas consumption. A court challenge is expected once the formal documentation is released.

GLOBAL

Saudi Arabia: A weekend drone attack on Saudi Arabia oil facilities cut about a half of productive capacity for the country, or about 5% of global supply, the single biggest disruption on record. Repairs are underway and Aramco officials have signaled that they aim to restore most of regular production by the end of the month. While Yemen's Houthi rebels have claimed responsibility, the U.S. has alleged that Iran is behind the attack.

Israel Elections: Prime Minister Benjamin Netanyahu's bloc fell short of receiving the majority of votes in a parliamentary election held this week, putting his leadership at odds with his chief rival, Benny Gantz. Netanyahu's coalition of right-wing and religious parties has tied with Gantz' block of centrist, left-wing and Arab parties. To obtain a majority, either would need the help of the small party, Yisrael Beiteinu, which is calling for a unity government.

Spain: New elections in November are now expected after opposition parties were unable to form a minority government around caretaker Prime Minister Pedro Sánchez, with his chances for power now slim-to-none. Currently, the Socialists have 123 seats in the 350-member chamber of deputies. They would not be able to form a government if the 42-strong Podemos grouping abstains (as they've signaled) and Ciudadanos and the center-right Popular party vote against.

IMPORTANT INFORMATION

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