

## Central Banks & Cheap Oil Keep on Rollin'

### IN REVIEW

- U.S. **nonfarm payrolls** rose a solid 273,000 in February and the unemployment rate slide to 3.5%. The labor market is holding up so far despite COVID-19, as initial claims slid 4,000 to 211,000. However, initial claims should be watched in the coming weeks as a first sign of weakness.
- The **NFIB small business optimism index** unexpectedly rose 0.2 point to 104.5 in February. However, we do not assign much weight to the improvement since most responses were gathered prior to the COVID-19 escalation.
- U.S. **CPI** rose 0.1% M/M in February while core was up 0.2% M/M. Food prices rose 0.4% M/M—the fastest pace in a year—while energy prices sank 2% M/M. While stockpiling of food should push food prices higher, lower energy and weaker services prices are set to weigh on headline inflation.
- The **EZ Sentix** plunged from 5.2 in February to -17.1 in March—the lowest level since April 2013—as the outbreak weighs on sentiment across Europe.
- The **BoE** cut its bank rate 50bps to 0.25%, launched a new Term Funding Scheme, and reduced a capital buffer to give banks more room to lend in coordination with a government stimulus package.
- **China CPI** slowed to 5.2% Y/Y in February. A 21.9% Y/Y increase in food prices was a boon, while prices for service items excluding healthcare were weaker. This trend is set to continue in March.

### WATCH LIST

| Date                |                                | Consensus   |   | Previous   |
|---------------------|--------------------------------|-------------|---|------------|
| <b>U.S.</b>         |                                |             |   |            |
| Tue 3/17            | Retail Sales                   | 0.2% M/M    | ▼ | 0.3% M/M   |
| Tue 3/17            | Industrial Production          | 0.4% M/M    | ▲ | -0.3% M/M  |
| Tue 3/17            | JOLTS Job Openings             |             |   | 6423       |
| Tue 3/17            | NAHB Housing Market Index      | 75          | ▲ | 74         |
| Tue 3/17            | AZ, FL, IL, & OH Primaries     | --          |   | --         |
| Wed 3/18            | Building Permits               | 1495k       | ▼ | 1551k      |
| Wed 3/18            | Housing Starts                 | 1500k       | ▼ | 1567k      |
| Wed 3/18            | FOMC Rate Decision             | 0.50%-0.75% | ▼ | 1.00-1.25% |
| Fri 3/20            | Existing Home Sales            | 5.55m       | ▲ | 5.46m      |
| <b>Europe</b>       |                                |             |   |            |
| Tue 3/17            | German ZEW Survey Expectations | -22.5       | ▼ | 8.7        |
| Tue 3/17            | U.K. Unemployment Rate         | 3.8%        | — | 3.8%       |
| Wed 3/18            | EZ Consumer Price Index        | 1.2% Y/Y    | — | 1.2% Y/Y   |
| <b>Asia Pacific</b> |                                |             |   |            |
| Mon 3/16            | Japan Core Machine Orders      | -0.8% M/M   | ▲ | -12.5% M/M |
| Mon 3/16            | China Industrial Production    | -3.0% Y/Y   | ▼ | 5.7% Y/Y   |
| Mon 3/16            | China Retail Sales             | -1.7% Y/Y   | ▼ | 8.0% Y/Y   |
| Wed 3/18            | Japan Trade Balance            | ¥970.0b     | ▲ | -¥1312.6b  |
| Thu 3/19            | Japan Consumer Price Index     | 0.5% Y/Y    | ▼ | 0.7% Y/Y   |
| Thu 3/19            | BOJ Rate Decision              |             |   | -0.1%      |

Arrows indicate consensus forecast compared to the previous period. Local dates of release.

### U.S.

- The **FOMC** is expected to cut the fed funds rate at its Wednesday meeting, following a 50 bps inter-meeting cut on March 3. The consensus forecast is for a second 50bps cut in March, while markets are pricing in a 75bps cut. With lower oil prices and weaker demand due to the virus outbreak, subdued inflation will give the Fed more wherewithal to conduct stimulative policies.
- Lower interest rates are a boon to refinancing activity and the **housing market**. With rising mortgage applications and a labor market that is still in good shape, strong demand will continue to support strong housing market data next week.

### Europe

- We expect to see further talks of **fiscal stimulus** packages in Europe to aid their economies against the outbreak, as most countries have enough fiscal space to act.

### Asia Pacific

- The **BoJ** will likely enact accommodative policy at their meeting—such as expanding asset purchases—but odds are that they will stop short of dragging their rate further into negative territory.

13 March 2020 / *The Week Ahead*

## THE HIGHLIGHTS

### **The ECB Policy Theory**

The ECB announcement is pure lacework, although the measures are so focused and targeted that they may not be immediately understood by markets. By unanimous decision, the ECB announced a significant relaxation of financial conditions for the euro area centered around a massive injection of liquidity. With a view supporting the continued provision of credit to households and corporates, in particular SMEs, the ECB is providing unlimited access to long-term refinancing operations, cutting rates on operations starting in June 2020 to -75bps, 25 bps below the policy rate. It also relaxed banks' capital buffers to free lending resources. The ECB also created an envelope of 120 billion euros to purchase public and private sector bonds, without monthly limits within this envelope. The ECB is also trying to incentivize governments to show leadership and implement large fiscal policy measures to remedy the economic impact of the coronavirus crisis. The ECB appears ready to do what it takes should governments fail to deliver.

### **Theory vs. Reality: Monetary & Fiscal Responses**

**Theory:** COVID-19 has resulted in both a negative supply and demand shock to the economy. Theory has taught us that a negative supply shock lowers the quantity supplied and increases prices, while a negative demand shock lowers output and prices. Given this, it depends which shock is larger to determine where prices end up. In theory, if the negative demand shock were bigger and permanent, a central bank would cut rates; otherwise it would not do anything.

Monetary and fiscal stimulative policies are generally demand management—not meant to deal with supply shocks. Fiscal policies, i.e. tax cuts and government spending, boost growth through consumption or government-spending routes, while monetary policies boost growth through the investment channel—via lower interest rates. Today, where interest rates are very low and the shock is temporary, price stability may require more liquidity support targeted toward SMEs, while trying to avoid bailing out already insolvent companies.

**Reality:** COVID-19 shocks aren't textbook variety. Given the dynamics of the current demand shock, orthodox fiscal policies such as tax cuts won't be as effective—quarantined people who aren't working don't collect paychecks, and providing consumers more disposable income won't help, as the outbreak should keep them from going out and spending. Moreover, neither fiscal nor

monetary policies can 'fix' a supply shock. Until supply shock abates, output will remain below prior levels, even if fiscal and monetary policies boost aggregate demand.

Central banks across the globe have eased, including recent moves from the BoE and ECB. The U.K. and Germany announced fiscal measures this week; the U.S. is discussing further spending. There is still fiscal space in Europe to act. While fiscal and monetary policies should combat demand shock to varying degrees of success they'll do less for supply shock.

### **Policy**

**U.S. Voters** are clearing the way for Joe Biden, though Bernie Sanders is not mathematically eliminated. Tuesday contests in Florida, Ohio, Illinois, and Arizona could effectively end it. Current delegate count: Biden, 860; Sanders, 710 (1,991 delegates needed).

**Digital Taxes of 2%** take effect in the UK April 1 on search engine revenues, social media services and online marketplaces that derive value from UK users. The Digital Services Tax (DST) involves all digital services with global revenues of £500m (\$647m) or more, with at least £25m (\$32m) from users in the UK. U.S. companies such as Facebook, Google and Amazon will be affected. Apple's core UK revenues are from consumer sales, which will not be impacted by the tax (entertainment, streaming and credit card services likely will). US treasury secretary Steven Mnuchin signaled a retaliatory tax on UK car exports to the US – if the 2% levy were imposed. One in five vehicles manufactured in the UK are exported to the US, worth £8.4bn, from manufacturers such as Jaguar, Land Rover, and Aston Martin. France won't collect the tax until EOY after threats of US Tariffs.

**Oil Markets:** Saudi Arabia will boost oil production to 13 million bpd, a massive boost from February's 9.7 million. The proposed output is higher than Aramco's sustained maximum production of 12 million bpd, implying the kingdom is going to add from inventories to dump as much crude into the market in response to no Russian deal to reduce production. Delivering capacity beyond 12 million bpd may take years and cost \$20 billion but shows Crown Prince Mohammed bin Salman has no signs of yielding from his response to OPEC's breakdown alliance with Russia. Russia increased production by another 500,000 bpd while bringing forward foreign currency sales to protect further battering of the ruble. Iraq, OPEC's second-largest producer behind Saudi Arabia, is also cutting prices. Lower oil prices weigh on inflation, particularly in Europe, which could lead ECB and BoE to be more accommodative.

13 March 2020 / The Week Ahead

## KEY FINANCIAL INDICATORS

| Rates  | Yield     | 1 W Change | 1M Change | 3M Change | 6M Change | 12M Change | YTD Change |
|--|-----------|------------|-----------|-----------|-----------|------------|------------|
| Fed Funds  | 1.25%     | 0 bps      | -50 bps   | -50 bps   | -100 bps  | -125 bps   | -50 bps    |
| U.S. SOFR  | 1.15%     | -8 bps     | -43 bps   | -39 bps   | -100 bps  | -123 bps   | -40 bps    |
| 3 Month USD Libor                                | 0.77%     | -23 bps    | -93 bps   | -111 bps  | -135 bps  | -184 bps   | -114 bps   |
| 3 Month Euribor                                  | -0.48%    | -2 bps     | -9 bps    | -9 bps    | -5 bps    | -17 bps    | -10 bps    |
| 3 Month U.S. T-Bill                              | 0.40%     | -31 bps    | -118 bps  | -117 bps  | -156 bps  | -204 bps   | -115 bps   |
| 2-Year U.S. Treasury                             | 0.52%     | -11 bps    | -90 bps   | -108 bps  | -115 bps  | -195 bps   | -105 bps   |
| 10-Year U.S. Treasury                            | 0.83%     | -17 bps    | -76 bps   | -96 bps   | -91 bps   | -181 bps   | -109 bps   |
| 10-Year German Bund                              | -0.77%    | -14 bps    | -38 bps   | -45 bps   | -20 bps   | -82 bps    | -58 bps    |
| 10-Year U.K. Gilt                                | 0.26%     | -12 bps    | -34 bps   | -53 bps   | -37 bps   | -94 bps    | -56 bps    |
| 10-Year JGB                                      | -0.07%    | 8 bps      | 0 bps     | -6 bps    | 14 bps    | -3 bps     | -4 bps     |
| Fixed Income                                     | Yield     | OAS        | 1W Return | 1M Return | 3M Return | 12M Return | YTD Return |
| Barclays Capital U.S. Government-Treasury        | 0.84%     | N/A        | 1.2%      | 4.9%      | 6.5%      | 13.7%      | 7.1%       |
| Barclays Capital U.S. TIPS                       | 1.19%     | N/A        | -3.2%     | -0.5%     | 0.9%      | 7.9%       | 1.1%       |
| Barclays Capital U.S. Aggregate                  | 1.69%     | 77         | -0.5%     | 2.0%      | 3.7%      | 11.3%      | 3.8%       |
| Barclays Capital Global Aggregate                | 1.06%     | 64         | 0.2%      | 2.7%      | 3.6%      | 9.3%       | 3.2%       |
| Barclays Capital U.S. ABS                        | 1.03%     | 44         | 0.2%      | 1.5%      | 2.5%      | 6.2%       | 2.5%       |
| Barclays Capital U.S. MBS                        | 2.00%     | 91         | -0.3%     | 0.7%      | 1.8%      | 6.9%       | 1.6%       |
| Barclays Capital U.S. Corporate Investment Grade | 2.75%     | 183        | -3.2%     | -1.1%     | 1.2%      | 12.5%      | 1.2%       |
| BAML Euro Corporate Investment Grade             | 0.70%     | 157        | -1.6%     | -1.7%     | -0.9%     | 3.2%       | -0.7%      |
| Barclays Capital U.S. Corporate High Yield       | 7.44%     | 646        | -6.0%     | -6.8%     | -4.7%     | 1.4%       | -6.0%      |
| BAML European Currency High Yield Non-Financial  | 5.08%     | 579        | -5.4%     | -6.9%     | -5.8%     | -0.7%      | -6.5%      |
| CS U.S. Leveraged Loans                          | 7.18%     | 655        | -4.1%     | -5.2%     | -4.0%     | -0.8%      | -4.7%      |
| CS Western European Leveraged Loans Non-USD      | 6.00%     | 583        | -3.1%     | -4.1%     | -3.2%     | -0.8%      | -3.5%      |
| JPM CEMBI Broad Diversified                      | 5.01%     | 422        | -3.4%     | -2.9%     | -0.3%     | 7.4%       | -1.1%      |
| JPM EMBI Global Diversified                      | 5.66%     | 475        | -7.0%     | -6.2%     | -3.4%     | 4.1%       | -4.5%      |
| JPM GBI-EM Global Diversified                    | 5.07%     | N/A        | -5.4%     | -5.7%     | -4.5%     | 2.0%       | -6.9%      |
| Equities   | Price     | Div Yield  | 1W Return | 1M Return | 3M Return | 12M Return | YTD Return |
| S&P 500  | 2,741.38  | 2.09%      | -12.4%    | -18.2%    | -12.3%    | 0.4%       | -14.8%     |
| Euro STOXX 600 (Local)                           | 333.17    | 2.97%      | -13.8%    | -22.2%    | -18.0%    | -10.8%     | -19.9%     |
| U.K. FTSE 100 (Local)                            | 5,876.52  | 5.65%      | -13.8%    | -21.6%    | -18.6%    | -17.6%     | -22.1%     |
| Japan Nikkei 225 (Local)                         | 19,416.06 | 2.35%      | -8.0%     | -18.0%    | -17.0%    | -8.1%      | -17.9%     |
| China Shanghai Composite (Local)                 | 2,968.52  | 2.24%      | -1.4%     | 2.3%      | 1.5%      | -1.9%      | -2.7%      |
| MSCI AC World (Local)                            | 473.55    | 2.85%      | -11.7%    | -17.5%    | -13.2%    | -3.3%      | -15.5%     |
| MSCI Emerging Markets (Local)                    | 946.62    | 3.02%      | -7.7%     | -11.4%    | -8.1%     | -4.1%      | -11.9%     |
| Commodities/Currencies                           | Price     | 1W Change  | 1M Change | 3M Change | 6M Change | 12M Change | YTD Change |
| S&P GS Commodity Index                           | 313.29    | -15.4%     | -18.5%    | -25.5%    | -22.5%    | -26.1%     | -28.2%     |
| WTI Crude (\$/bbl)                               | 32.98     | -29.5%     | -34.0%    | -43.9%    | -40.7%    | -41.9%     | -46.1%     |
| Copper (\$/lb)                                   | 2.51      | -3.1%      | -3.0%     | -9.7%     | -3.3%     | -13.4%     | -10.1%     |
| Gold (\$/oz)                                     | 1,653.75  | 0.7%       | 5.3%      | 12.7%     | 10.9%     | 27.9%      | 9.2%       |
| U.S. Dollar Index                                | 96.51     | -0.9%      | -2.2%     | -0.9%     | -2.2%     | -0.7%      | 0.1%       |
| Euro (USD/EUR)                                   | 1.13      | 1.2%       | 3.3%      | 1.7%      | 2.6%      | 0.5%       | 0.5%       |
| British Pound (USD/GBP)                          | 1.29      | 0.5%       | -0.5%     | -2.2%     | 4.4%      | -1.6%      | -2.7%      |
| Japanese Yen (Yen/USD)                           | 104.85    | -2.3%      | -4.6%     | -3.5%     | -2.7%     | -5.7%      | -3.5%      |
| Chinese Yuan (CNY/USD)                           | 6.95      | 0.2%       | -0.4%     | -1.3%     | -2.4%     | 3.3%       | -0.2%      |

Source: FactSet and Bloomberg. As of March 11, 2020.

**13 March 2020 | The Week Ahead**

*Barings is a \$338+ billion\* global financial services firm dedicated to meeting the evolving investment and capital needs of our clients and customers. Through active asset management and direct origination, we provide innovative solutions and access to differentiated opportunities across public and private capital markets. A subsidiary of MassMutual, Barings maintains a strong global presence with business and investment professionals located across North America, Europe and Asia Pacific.*

#### IMPORTANT INFORMATION

Any forecasts in this document are based upon Barings opinion of the market at the date of preparation and are subject to change without notice, dependent upon many factors. Any prediction, projection or forecast is not necessarily indicative of the future or likely performance. Investment involves risk. The value of any investments and any income generated may go down as well as up and is not guaranteed by Barings or any other person. **PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS.** Any investment results, portfolio compositions and or examples set forth in this document are provided for illustrative purposes only and are not indicative of any future investment results, future portfolio composition or investments. The composition, size of, and risks associated with an investment may differ substantially from any examples set forth in this document. No representation is made that an investment will be profitable or will not incur losses. Where appropriate, changes in the currency exchange rates may affect the value of investments. Prospective investors should read the offering documents, if applicable, for the details and specific risk factors of any Fund/Strategy discussed in this document.

Barings is the brand name for the worldwide asset management and associated businesses of Barings LLC and its global affiliates. Barings Securities LLC, Barings (U.K.) Limited, Barings Global Advisers Limited, Barings Australia Pty Ltd, Barings Japan Limited, Baring Asset Management Limited, Baring International Investment Limited, Baring Fund Managers Limited, Baring International Fund Managers (Ireland) Limited, Baring Asset Management (Asia) Limited, Baring SICE (Taiwan) Limited, Baring Asset Management Switzerland Sarl, and Baring Asset Management Korea Limited each are affiliated financial service companies owned by Barings LLC (each, individually, an "Affiliate").

**NO OFFER:** The document is for informational purposes only and is not an offer or solicitation for the purchase or sale of any financial instrument or service in any jurisdiction. The material herein was prepared without any consideration of the investment objectives, financial situation or particular needs of anyone who may receive it. This document is not, and must not be treated as, investment advice, an investment recommendation, investment research, or a recommendation about the suitability or appropriateness of any security, commodity, investment, or particular investment strategy, and must not be construed as a projection or prediction.

Unless otherwise mentioned, the views contained in this document are those of Barings. These views are made in good faith in relation to the facts known at the time of preparation and are subject to change without notice. Individual portfolio management teams may hold different views than the views expressed herein and may make different investment decisions for different clients. Parts of this document may be based on information received from sources we believe to be reliable. Although every effort is taken to ensure that the information contained in this document is accurate, Barings makes no representation or warranty, express or implied, regarding the accuracy, completeness or adequacy of the information.

Any service, security, investment or product outlined in this document may not be suitable for a prospective investor or available in their jurisdiction.

#### Copyright and Trademark

Copyright © 2020 Barings. Information in this document may be used for your own personal use, but may not be altered, reproduced or distributed without Barings' consent.

The BARINGS name and logo design are trademarks of Barings and are registered in U.S. Patent and Trademark Office and in other countries around the world. All rights are reserved.

\*As of December 31, 2019  
20-1118279