BARINGS INVESTMENT INSTITUTE

WEEKLY UPDATE

23 August 2019

Overview

CBO Raises Deficit Projection: *The Congressional Budget Office updated its 2019 budget and economic projections, forecasting the federal budget deficit will be $960 billion in 2019 and averaging $1.2 trillion between 2020 and 2029. The current 2019 deficit is $63 billion more than the previous forecast in May. Recently enacted legislation accounts for the bulk of the increase, mainly due to the higher discretionary funding limits for 2020 and 2021. Deficits are expected to range between 4.4-4.8% of GDP over the next decade. This will likely result in the debt/GDP ratio rising from 79% in 2019 to 95% in 2029 - the highest level since just after World War II.*

Volcker Rule Changes: *The final rule changes seek to provide lenders a much clearer picture of which trades are prohibited and puts the burden on regulators to determine compliance. While prop trading is still banned, market-making activities are likely to increase as banks can set their own risk limits based on internal models. The rule change should give banks' more flexibility on investments and reduce compliance costs.*

Italian PM Resigns: *Italian Prime Minister Giuseppe Conte resigned in response to the League's no-confidence motion. Interior Minister and League leader Matteo Salvini withdrew his support for the government, causing its collapse. President Sergio Matterella will give Five Star and the Democratic Party time to form a new coalition government, which would push the League into opposition. Italy's bond yields seemed to shrug off the political turmoil, tumbling on expectations that any political crisis would be short-lived as a new, more market-friendly coalition government could be formed in the near future which would remove the uncertainty of snap elections.*

Key Financial Indicators						As of:	8/21/2019
Rates	**Yield**	**1 W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
Fed Funds	2.25%	0 bps	-25 bps	-25 bps	-25 bps	25 bps	-25 bps
3 Month USD Libor	2.15%	-2 bps	-11 bps	-38 bps	-50 bps	-16 bps	-66 bps
3 Month Euribor	-0.42%	-2 bps	-5 bps	-11 bps	-11 bps	-10 bps	-11 bps
3 Month U.S. T-Bill	1.97%	5 bps	-5 bps	-37 bps	-43 bps	-7 bps	-43 bps
2-Year U.S. Treasury	1.57%	-1 bps	-25 bps	-67 bps	-96 bps	-104 bps	-93 bps
10-Year U.S. Treasury	1.58%	0 bps	-47 bps	-84 bps	-111 bps	-127 bps	-110 bps
10-Year German Bund	-0.68%	-4 bps	-34 bps	-60 bps	-77 bps	-98 bps	-89 bps
10-Year U.K. Gilt	0.46%	-9 bps	-38 bps	-68 bps	-78 bps	-92 bps	-88 bps
10-Year JGB	-0.24%	-2 bps	-10 bps	-19 bps	-20 bps	-33 bps	-24 bps
Fixed Income	**Yield**	**OAS**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
Barclays Capital U.S. Government-Treasury	1.63%	N/A	0.0%	3.0%	5.6%	9.9%	8.1%
Barclays Capital U.S. TIPS	1.74%	N/A	-0.2%	1.6%	4.4%	6.7%	8.2%
Barclays Capital U.S. Aggregate	2.21%	50	0.1%	2.3%	5.0%	9.6%	8.6%
Barclays Capital Global Aggregate	1.23%	47	-0.1%	1.7%	5.0%	7.6%	7.2%
Barclays Capital U.S. ABS	1.94%	35	0.1%	0.8%	2.0%	5.5%	4.1%
Barclays Capital U.S. MBS	2.42%	53	0.2%	0.6%	2.6%	6.8%	5.2%
Barclays Capital U.S. Corporate Investment Grade	2.87%	119	0.3%	3.2%	7.1%	12.6%	13.4%
BAML Euro Corporate Investment Grade	0.26%	110	0.1%	1.2%	3.6%	6.1%	6.2%
Barclays Capital U.S. Corporate High Yield	5.79%	397	0.8%	0.4%	1.9%	6.2%	10.4%
BAML European Currency High Yield Non-Financial	3.29%	394	0.6%	0.6%	2.1%	4.0%	4.4%
CS U.S. Leveraged Loans	6.19%	474	0.0%	-0.1%	0.3%	3.4%	7.0%
CS Western European Leveraged Loans Non-USD	4.67%	423	0.0%	0.2%	0.7%	2.9%	4.4%
JPM CEMBI Broad Diversified	5.12%	358	0.3%	0.5%	3.4%	10.9%	8.1%
JPM EMBI Global Diversified	5.35%	365	0.4%	0.5%	4.8%	12.6%	7.9%
JPM GBI-EM Global Diversified	5.35%	N/A	0.2%	-2.7%	5.3%	11.4%	0.9%
Equities	**Price**	**Div Yield**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
S&P 500	2,924.43	1.89%	3.0%	-1.6%	2.6%	4.2%	18.2%
Euro STOXX 600 (Local)	375.80	2.92%	2.6%	-3.0%	-1.0%	-2.2%	11.3%
U.K. FTSE 100 (Local)	7,203.97	4.55%	0.8%	-4.1%	-1.7%	-4.8%	7.1%
Japan Nikkei 225 (Local)	20,618.57	2.27%	-0.2%	-4.0%	-3.1%	-7.2%	3.0%
China Shanghai Composite (Local)	2,880.33	2.44%	2.5%	-1.5%	-0.9%	5.4%	15.5%
MSCI AC World (Local)	510.17	2.59%	2.4%	-2.4%	1.5%	2.1%	6.4%
MSCI Emerging Markets (Local)	983.14	2.99%	1.9%	-4.4%	0.7%	-1.3%	-4.4%
Commodities/Currencies	**Price**	**1 W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
S&P GS Commodity Index	400.02	0.5%	-3.8%	-9.7%	-6.6%	-11.9%	6.9%
WTI Crude ($/bbl)	55.65	0.9%	0.4%	-11.7%	-2.3%	-17.3%	23.3%
Copper ($/lb)	2.58	-0.2%	-5.9%	-5.2%	-11.1%	-4.0%	-1.8%
Gold ($/oz)	1,503.25	-0.7%	4.4%	18.3%	12.9%	26.2%	17.5%
U.S. Dollar Index	98.30	0.3%	1.2%	0.2%	1.7%	3.2%	2.2%
Euro (USD/EUR)	1.11	-0.5%	-1.1%	-0.8%	-2.2%	-3.7%	-3.0%
British Pound (USD/GBP)	1.21	0.5%	-3.0%	-5.1%	-7.2%	-5.7%	-4.8%
Japanese Yen (Yen/USD)	106.47	0.6%	-1.2%	-3.7%	-3.8%	-3.6%	-3.0%
Chinese Yuan (CNY/USD)	7.06	0.7%	2.7%	2.1%	5.2%	3.2%	2.9%

Source: FactSet and Bloomberg

Economics

UNITED STATES

FOMC Minutes: Minutes of the July 31 FOMC meeting show many participants viewed their rate cut as insurance to counter the downside risks of weak global growth and trade policy uncertainty, and to promote a faster return of inflation. Members generally agreed it was important to maintain flexibility to determine the future path of interest rates.

PMI: The preliminary reading of Markit's August manufacturing and services Purchasing Managers' Index (PMI) surveys were below expectations. The manufacturing PMI dipped just below the expansion/contraction line at 49.9, from 50.4 in July, as new orders contracted and inventories declined. The service sector PMI fell to 50.9 from 52.6 in July on weaker prices.

Housing: Although July data was mixed relative to expectations, there were some underlying positives for the sector. The key single-family segment showed starts rose for the second consecutive month and permits increased for the third month in a row. Sales of existing homes reached a five-month high, supported by a sharp drop in mortgage rates this year.

EUROPE

ECB Minutes: Minutes of the July 25 ECB meeting seemed to indicate that a stimulus policy package, including a combination of rate cuts and asset purchases, will be forthcoming at the September meeting to help meet its inflation goal.

EZ PMI: Leading indicators continue to signal a feeble euro area growth outlook even as Markit's preliminary August PMI surveys were slightly above estimates. The manufacturing PMI remained in contraction territory as global trade uncertainty and auto sector troubles continued. The service index moved further into expansion territory, but new business measures fell

EZ Inflation: Headline inflation was weaker than initially reported in July with CPI rising 1% Y/Y. The core rate decelerated to .9% Y/Y, which should only embolden the ECB to move forward with aggressive stimulus in September.

ASIA - PAC

Japan PMI: The Markit manufacturing PMI was little changed in August, remaining in contraction territory for the fourth-consecutive month at 49.5. The services index rose to 53.4 from 51.8 in July, reaching its highest reading since October 2017.

RBA Minutes: Minutes of the August 6 RBA meeting showed the Australian central bank saw little evidence of inflation pressure and warned of a spillover of weak wage growth to household spending. Members would consider further monetary policy easing if incoming data suggests this was needed to support economic growth.

South Korea Trade: Exports in the first 20 days of August declined 13.3% Y/Y and imports fell 2.4% over that same period. Export data is considered a bellwether for global trade and signals the full month figures will likely show the string of Y/Y declines in exports extends to every month this year.

Policy

UNITED STATES

Tax Cuts: President Donald Trump announced, and later retracted, that the administration was examining various tax cut proposals, including a reduction on capital-gains taxes by indexing them to inflation, in a bid to bolster the economy. President Trump also suggested that such a move could be done through regulatory action instead of going through Congress. Other measures allegedly discussed included cutting payroll taxes and a reduction of the corporate tax rate.

Antitrust: A group of about 20 state attorneys general is expected to move forward with a joint antitrust investigation of big technology, beginning as soon as next month. The probe will likely focus on whether dominant technology platforms such as Google, Facebook, Amazon and Apple use their marketplace powers to stifle competition.

Huawei: The U.S. has extended for another 90 days a set of exemptions that seek to protect rural networks and other U.S. customers from a ban on doing business with China's Huawei technologies. While the move doesn't exactly address the wide national-security concerns about Huawei, the gesture is seen as encouraging the long-awaited trade deal with China.

Volcker 2.0: Federal regulators have voted to allow a rewrite of the Volcker rule that would ease trading restrictions of mid-size banks and streamline compliance for larger banks. Once the remaining three regulators sign off, the rule is scheduled to go into effect January 1, with a compliance date set for January 1, 2021.

Housing: The Department of Housing and Urban Development released a proposed rule that would make it more difficult for plaintiffs to claim unintentional discrimination under the Fair Housing Act. Also known as disparate impact, these lawsuits do not require proof of an intent to discriminate but hold businesses and governments liable for practices that disproportionately affect members of a protected class. The proposal also gives defendants more leeway in rebutting a claim.

GLOBAL

Italy: Prime Minister Guiseppe Conte has resigned, effectively declaring the end of the current governing coalition between the anti-immigration League and the anti-establishment Five Star Movement. Italian President Sergio Mattarella is expected to gather party leaders see whether a new coalition can be assembled. If he is unsuccessful, snap elections could likely take place in late October or early November.

Chinese Loans: The PBOC has announced that new loans must be priced "mainly" with a revamped reference benchmark rate called Loan Prime Rate, which tracks the price of credit to banks' best customers. The rate is also linked to the price the central bank charges lenders for cash over one year. The move is seen as a push to prod borrowing costs lower.

Germany: Finance Minister Olaf Scholz suggested Germany could spend an extra €50 billion ($55 billion) in an economic crisis. The move came amid increased pressure for the government to consider suspending its balanced-budget policy.

IMPORTANT INFORMATION

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