15 January 2021

THE WEEK AHEAD

Is a Blue Wave Enough to Deliver Blue Skies?

WATCH LIST

Date		Period	Consensus		Previous
U.S.					
Mon 1/18	Markets Closed for MLK Day		--		--
Wed 1/20	Inauguration Day		--		--
Wed 1/20	NAHB Housing Market Index	Jan	86	-	86
Thu 1/21	Building Permits	Dec	1600K	▼	1639K
Thu 1/21	Housing Starts	Dec	1562K	▲	1547K
Fri 1/22	Markit Manufacturing PMI (Prelim)	Jan	56.5	▼	57.1
Fri 1/22	Markit Services PMI (Prelim)	Jan			54.8
Fri 1/22	Existing Home Sales	Dec	6.55M	▼	6.69M
Europe					
Wed 1/20	U.K. Retail Sales	Dec	1.5% M/M	▲	-3.8% M/M
Thu 1/21	ECB Monetary Policy Meeting	Jan	0.0%	-	0.0%
Fri 1/22	EZ Markit Manufacturing PMI (Prelim)	Jan	54.9	▼	55.2
Fri 1/22	EZ Markit Services PMI (Prelim)	Jan	45.5	▼	46.4
Asia Pacific					
Mon 1/18	China GDP	4Q20	6.2% Y/Y	▲	4.9% Y/Y
Mon 1/18	China Industrial Production (YTD)	Dec	2.7% Y/Y	▲	2.3% Y/Y
Mon 1/18	China Retail Sales (YTD)	Dec	-3.9% Y/Y	▲	-4.8% Y/Y
Mon 1/18	China Fixed Assets ex. Rural (YTD)	Dec	3.2% Y/Y	▲	2.6% Y/Y
Wed 1/20	PBOC Meeting	Jan	--		--
Thu 1/21	BOJ Policy Rate	Jan			-0.1%
Fri 1/22	Japan Consumer Price Index	Dec	-1.3% Y/Y	▼	-0.9% Y/Y
Fri 1/22	Jibun Bank Japan Manufacturing PMI (Prelim)	Jan			50.0
Fri 1/22	Jibun Bank Japan Services PMI (Prelim)	Jan			47.7

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

U.S.

- **January Markit flash PMIs will give a glimpse** at how services and manufacturing fare amid Lockdown 2.0. Its more-targeted nature should weigh heavily on in-person services.
- **Housing data are expected to remain strong** given robust demand and record-low mortgage rates.

Europe

- **The ECB meeting should be fairly uneventful** given sufficient policy. The negligible impact of the Italian government crisis on European bond yields is a testament to effective policy.
- **January Markit flash PMIs will show the damage** from renewed restrictions (but less than in 2020).

Asia Pacific

- **China Q4 GDP is set to accelerate** as China leads the global recovery.
- **The PBOC will likely signal that it remains on its path** towards policy normalization. Meanwhile, the **BOJ will likely continue** its accommodative stance in-line with renewed fiscal support.

Institute's Central Scenario

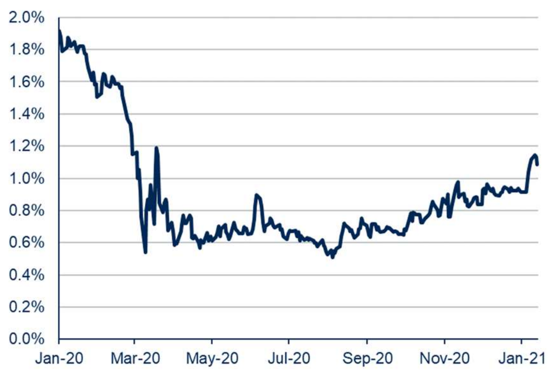
Disappointing U.S. employment data this week aligns with our central scenario of the "Not Quite Recovery," which foresees slowing momentum amid rising cases before growth picks up on the backs of greater fiscal stimulus and vaccine deployments. Georgia's election results lower the Fiscal Cliff scenario odds, as more stimulus is expected. While U.S. inflation expectations rose in response, labor market slack will likely keep inflation increases at bay, and we watch for longer-term labor market scarring. Improving data in China confirms the PBOC can pursue its path of less accommodative policy. Please see our Monthly Macro Dashboard.

IN REVIEW

Georgia Runoffs Boost Spending Hopes & Yields

More fiscal stimulus as direct payments to consumers, expanded unemployment insurance benefits, and state and local aid looks likely after the Georgia Senate runoff elections gave Democrats slim control of the federal government. This will likely be the new administration's first priority and could be passed in February, particularly as the current extension of UI programs is set to expire mid-March. Other spending and tax policy changes are probable but would likely come later through the reconciliation process on the fiscal year budget. Greater fiscal spending is set to aid growth this year. Bond yields broke higher, reaching a high of 1.19% amid rising inflation expectations. While inflation expectations rose, other factors like the term premium and real yields also moved higher, reflecting an optimistic outlook and potential for less monetary support.

U.S. 10-YEAR TREASURY RATE



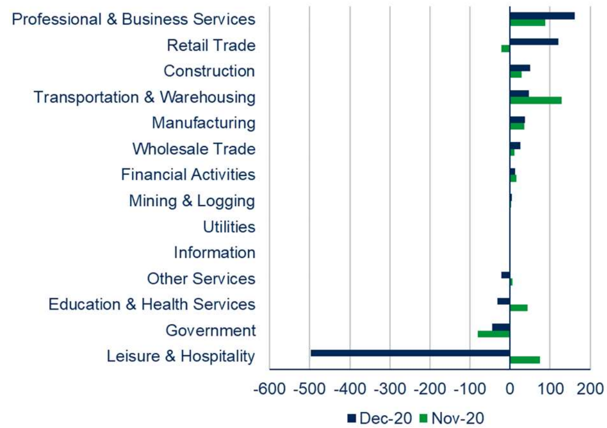
Source: Bloomberg. As of January 13, 2021.

However, we don't see a large, sustained jump in inflation in our baseline scenario—due in part to the significant labor market slack, which should limit wage pressures. Moreover, FOMC leadership messaging suggests a commitment to remaining accommodative for as long as possible—especially as the labor market is far from full-employment and unemployment remains concentrated in sectors that won't improve until the vaccination campaigns successfully conclude and restrictions lift (see next section). With vaccine deployment in the early stages, it is hard to imagine any QE tapering before 4Q21 or 2022, at the earliest.

U.S. Employment is Not Immune to COVID

U.S. jobs numbers joined the fray of deteriorating economic data during the winter months. While scarring remains a concern amid rising long-term unemployment, a future poised with vaccines and fiscal support looks brighter.

CHANGE IN U.S. NONFARM PAYROLLS, THOUSANDS



Source: Bloomberg. As of January 14, 2021.

Nonfarm payrolls fell 140,000 in December amid rising COVID cases, new restrictions and fiscal stimulus delays. Lockdown 2.0 is much different and more targeted than last year's, as the decline was concentrated in in-person services, such as leisure and hospitality, while other sectors like construction and manufacturing continued to expand. The unemployment rate held steady at 6.7%. The loss of low-wage jobs artificially boosted average hourly earnings due to compositional bias. However, the Employment Cost Index for wages and salaries shows wage pressures remain at bay and should continue, as there are 5.5 million more people not in the labor force than pre-crisis—signaling much slack in the labor market.

While the jobs print disappointed, additional fiscal stimulus should provide some support, as it provides about half the support as the CARES Act. The poor jobs print also increases odds of greater fiscal stimulus from the new administration.

China Inflation Data Won't Deter the PBOC

Economic data out of China supports the PBOC's stance to normalize policy. The producer price index eased from -1.5% Y/Y in November to -0.4% Y/Y in December as the economy recovers. The consumer price index came in stronger than expected, though cold weather pushed food prices higher—the temporary nature of which points to possible inflation volatility in the coming months. This shouldn't impact the PBOC's policy decisions. Policy normalization was apparent in credit growth data, down in December. Targeted support could come to SMEs in the near-term. Policy normalization shouldn't derail growth in China, but missteps and the resulting unintended consequences are possible.

KEY FINANCIAL INDICATORS

Rates	Yield	1 W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
Fed Funds	0.25%	0 bps	0 bps	0 bps	0 bps	-150 bps	0 bps
U.S. SOFR	0.08%	-2 bps	0 bps	-1 bps	-2 bps	-146 bps	1 bps
3 Month USD Libor	0.24%	1 bps	2 bps	0 bps	-3 bps	-159 bps	0 bps
3 Month Euribor	-0.55%	1 bps	0 bps	-4 bps	-11 bps	-16 bps	0 bps
3 Month U.S. T-Bill	0.10%	0 bps	2 bps	-1 bps	-4 bps	-145 bps	2 bps
2-Year U.S. Treasury	0.14%	0 bps	2 bps	-1 bps	-3 bps	-144 bps	2 bps
10-Year U.S. Treasury	1.09%	5 bps	21 bps	37 bps	46 bps	-76 bps	18 bps
10-Year German Bund	-0.52%	3 bps	12 bps	4 bps	-10 bps	-35 bps	6 bps
10-Year U.K. Gilt	0.31%	7 bps	14 bps	8 bps	13 bps	-46 bps	12 bps
10-Year JGB	0.03%	1 bps	2 bps	0 bps	0 bps	3 bps	1 bps
Fixed Income	**Yield**	**OAS**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
Barclays Capital U.S. Government-Treasury	0.67%	N/A	-0.1%	-1.0%	-1.5%	6.5%	-1.0%
Barclays Capital U.S. TIPS	0.82%	N/A	-0.1%	0.3%	1.0%	9.8%	-0.5%
Barclays Capital U.S. Aggregate	1.20%	37	0.0%	-0.5%	-0.1%	6.3%	-0.7%
Barclays Capital Global Aggregate	0.87%	35	-0.4%	0.1%	2.3%	8.8%	-0.6%
Barclays Capital U.S. ABS	0.45%	30	0.0%	0.0%	0.3%	4.2%	0.0%
Barclays Capital U.S. MBS	1.27%	25	0.0%	0.2%	0.2%	3.5%	-0.1%
Barclays Capital U.S. Corporate Investment Grade	1.85%	93	0.4%	-0.4%	1.3%	8.2%	-1.1%
BAML Euro Corporate Investment Grade	0.23%	90	0.0%	-0.2%	1.3%	2.7%	0.1%
Barclays Capital U.S. Corporate High Yield	4.25%	354	0.0%	1.0%	4.9%	6.7%	0.1%
BAML European Currency High Yield Non-Financial	2.93%	354	0.1%	0.7%	4.8%	3.0%	0.5%
CS U.S. Leveraged Loans	4.82%	456	0.7%	1.5%	4.2%	3.2%	1.1%
CS Western European Leveraged Loans Non-USD	4.46%	440	0.4%	0.8%	3.4%	3.0%	0.6%
JPM CEMBI Broad Diversified	4.17%	325	-0.4%	0.1%	3.0%	5.7%	-0.5%
JPM EMBI Global Diversified	4.76%	358	-0.8%	-0.5%	2.6%	3.2%	-1.4%
JPM GBI-EM Global Diversified	4.30%	N/A	-1.0%	0.1%	7.4%	1.9%	-0.8%
Equities	**Price**	**Div Yield**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
S&P 500	3,809.84	1.49%	1.7%	4.1%	8.9%	18.0%	1.5%
Euro STOXX 600 (Local)	409.07	2.05%	0.7%	4.9%	10.3%	-2.2%	2.5%
U.K. FTSE 100 (Local)	6,745.52	3.51%	-1.4%	3.0%	13.0%	-11.4%	4.4%
Japan Nikkei 225 (Local)	28,456.59	2.22%	5.2%	6.8%	20.6%	19.3%	3.7%
China Shanghai Composite (Local)	3,598.65	1.97%	1.3%	7.5%	7.1%	15.5%	3.6%
MSCI AC World (Local)	661.49	1.77%	2.0%	4.9%	11.8%	15.6%	2.6%
MSCI Emerging Markets (Local)	1,364.07	1.71%	3.9%	8.8%	17.9%	23.2%	5.9%
Commodities/Currencies	**Price**	**1W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
S&P GS Commodity Index	433.33	2.5%	10.1%	20.9%	28.9%	1.7%	5.8%
WTI Crude ($/bbl)	52.91	4.9%	13.6%	32.2%	32.1%	-9.0%	9.4%
Copper ($/lb)	3.62	-0.9%	2.6%	18.9%	22.9%	26.4%	2.9%
Gold ($/oz)	1,858.85	-3.8%	0.9%	-1.7%	2.8%	19.9%	-1.5%
U.S. Dollar Index	90.36	0.9%	-0.7%	-3.4%	-6.3%	-7.2%	0.5%
Euro (USD/EUR)	1.22	-1.0%	0.4%	3.5%	7.0%	9.2%	-0.6%
British Pound (USD/GBP)	1.36	0.6%	3.2%	5.0%	8.1%	5.1%	-0.2%
Japanese Yen (Yen/USD)	103.94	0.5%	0.0%	-1.5%	-3.1%	-5.5%	0.7%
Chinese Yuan (CNY/USD)	6.47	0.1%	-1.2%	-4.0%	-7.7%	-6.2%	-1.1%

Source: FactSet and Bloomberg. As of January 13, 2021.

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*As of September 30, 2020
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