

EU Outlook Brighter, but Watch the News in Rome

WATCH LIST

Date		Period	Consensus		Previous
U.S.					
Tue 2/9	NFIB Small Business Optimism	Jan	96.5	▼	95.9
Tue 2/9	JOLTS Job Openings	Dec	6450K		6527K
Wed 2/10	Consumer Price Index	Jan	0.4% M/M	-	0.4% M/M
Fri 2/12	University of Michigan Sentiment (Preliminary Estimate)	Feb	80.7	▲	79.0
Europe					
Wed 2/10	U.K. Industrial Production	Dec			-0.1% M/M
Wed 2/10	U.K. GDP (Preliminary Estimate)	4Q20			16.0% Q/Q
Thu 2/11	European Commission Published Economic Forecasts		--		--
Fri 2/12	EZ Industrial Production	Dec	0.0% M/M	▼	2.5% M/M
Asia Pacific					
2/8-2/15	China Aggregate Financing (CNY)	Jan	4570.0B	▲	1720.0B
Wed 2/10	China Consumer Price Index	Jan	-0.1% Y/Y	▼	0.2% Y/Y
Wed 2/10	China Producer Price Index	Jan	0.3% Y/Y	▲	-0.4% Y/Y
Wed 2/10	Japan Machine Tool Orders (Preliminary Estimate)	Jan			9.9% Y/Y
Wed 2/10	Japan Producer Price Index	Jan	-1.6% Y/Y	▼	-2.0% Y/Y

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

U.S.

- While **consumer sentiment has remained near pandemic lows, preliminary data will give a sense** of whether government support and vaccines are easing consumer worries.
- **The January consumer price index is expected to remain tame.** While we could see a temporary rise in the coming months due to base effects, underlying inflation pressures should remain at bay, which will give the FOMC room to remain accommodative this year.

Europe

- **The European Commission’s forecasts will provide insight** into Europe’s future, as the Commission has reviewed governments’ recovery spending and reform plans.
- **Next week should reveal if ex-ECB President Mario Draghi will lead the next Italian government.** Risks loom large for EU markets. Success means peripheral bonds and stock markets will likely rally. Failure—a low probability—would bring shock and doubt over Italy’s use of the EU Recovery Fund to reform and accelerate growth.

Asia Pacific

- **China aggregate financing for January will be released next week.** We expect credit growth will continue to ease and be calibrated to grow in line with nominal GDP growth. While the PBOC is committed to financial de-risking, the latest COVID resurgence could alter the pace of policy normalization.
- **Preliminary Japan machine tool orders for January will be released on Wednesday.** As its economy continues to lag behind, we watch to see if external demand remains a source of strength.

Institute’s Central Scenario

U.S. large-cap earnings are on track to show growth last quarter, illustrating that the recovery remained intact despite greater restrictions in 4Q20. Elsewhere, euro area 4Q20 GDP came in better than expected, showing that consumption and investment remain resilient. Risks to China’s outlook have emerged with the resurgence in COVID cases. January PMIs expanded less than expected, which we see as a slowdown, and not derailment, of the recovery. Please see our [Monthly Macro Dashboard](#).

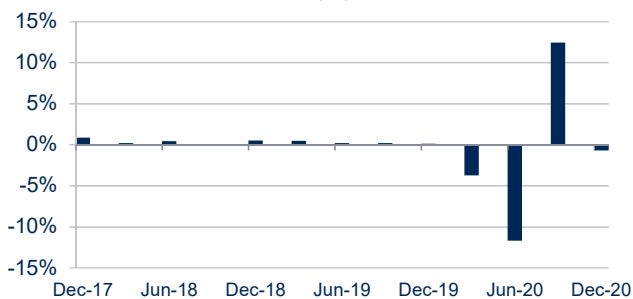
IN REVIEW
Perverse Price Reactions to Earnings

More than half of the S&P 500 have reported 4Q20 financials and earnings are up 6% Y/Y, with the largest gains in Real Estate and Materials. For the index as a whole, earnings are tracking to grow 2.4% Y/Y for the quarter, compared to consensus expectations that had called for a decline of 8.8%. Despite generally positive surprises—with earnings coming in 14% higher than consensus, above the 6% five-year average—equity price action immediately following release has been negative. The extent of these perverse price reactions was not unlike those seen in 2000, during the peak of the Tech Bubble, when stretched-valuation concerns were also in focus.

EZ GDP Shows Lockdowns Hurt Less This Time

Fourth-quarter GDP surprised strongly on the upside, showing the region contracted 0.7% Q/Q, less than the 2% consensus. The second COVID wave is delaying the recovery, as expected, but the economic damage has been smaller than in Q2 (when GDP dropped 11.2% Q/Q). In most Member States, growth beat estimates. Higher-frequency data, such as manufacturing PMIs, show an industrial sector that is holding up. In addition, retail sales turned positive Y/Y in December, and credit growth remains buoyant. This bodes well for investments and exports that should pull the eurozone economy out of the doldrums. The supply chain squeeze increasing Asia freight costs is likely to feed into some inflation and foster the debate on central bank tapering. January inflation was indeed above consensus (+0.9% M/M vs. +0.5% cons.) but way below the 2% target. We believe the ECB will look through these temporary inflation dynamics and stay focused on the need to support the still-fragile recovery, amid structural disinflationary forces.

EURO AREA REAL GDP GROWTH
Q/Q



Source: Eurostat, Haver. As of December 31, 2020.

U.S. Income and Spending Ready for Takeoff

U.S. consumer spending fell at the end of 2020 amid the COVID resurgence and delayed passage of fiscal support. However, incomes and spending are ready for liftoff in 1Q21 as fiscal support is disbursed. Moreover, an elevated savings rate will support the medium-term outlook once vaccines are widely distributed.

In December, personal spending fell for the second-consecutive month, down 0.2% M/M. Sectors most susceptible to the pandemic, such as recreational goods and vehicles, food services, and accommodations, felt the largest impact. While the new round of fiscal support should boost spending on goods, services will likely continue to suffer until the vaccines are readily available.

Personal income rose 0.6% M/M, largely due to unemployment benefits. While wages and salaries rose, wage growth remains below pre-crisis trend. Wage pressure will likely remain tame due to a large amount of labor market slack.

The personal savings rate rose at year-end. Even though most of the pent-up savings is held by higher-income earners (with lower propensities to consume), the elevated-savings rate will support spending post-vaccine.

Given the weak employment and consumer confidence backdrop, more support will be needed when the current fiscal package expires in mid-March; luckily, it appears more should be passed around this deadline. The brighter outlook for fiscal support given the modest Democrat control led us to upgrade the U.S. medium-term growth outlook in our baseline scenario.

COVID Resurgence Weighs on China PMIs

China has proven it is not immune to COVID. January PMIs showed China's expansion slowed more than expected due to the recent increase in COVID-19 cases. Similar to other major economies, the more-targeted nature of containment measures led the slowdown to be greater for services than manufacturing. The underlying details were also weak, with an easing in the pace of labor market recovery. Elevated cases elsewhere in the world were also a weight, as the new export business sub-index fell one percentage point to 50.8.

Our baseline scenario does not see this derailing the economic recovery in China. However, the higher case counts and restrictions will likely weigh on consumption and the pace of growth in the near-term, particularly as it coincides with the Lunar New Year.

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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	0.07%	4 bps	0 bps	-3 bps	-3 bps	-152 bps	0 bps
3 Month USD Libor	0.20%	-2 bps	-4 bps	-3 bps	-5 bps	-155 bps	-4 bps
3 Month Euribor	-0.55%	0 bps	0 bps	-3 bps	-8 bps	-15 bps	0 bps
3 Month U.S. T-Bill	0.04%	-5 bps	-4 bps	-6 bps	-7 bps	-152 bps	-4 bps
2-Year U.S. Treasury	0.11%	-1 bps	-1 bps	-6 bps	0 bps	-125 bps	-1 bps
10-Year U.S. Treasury	1.13%	12 bps	21 bps	25 bps	57 bps	-39 bps	21 bps
10-Year German Bund	-0.47%	8 bps	10 bps	15 bps	5 bps	-5 bps	10 bps
10-Year U.K. Gilt	0.36%	10 bps	17 bps	10 bps	26 bps	-20 bps	17 bps
10-Year JGB	0.05%	2 bps	3 bps	1 bps	3 bps	13 bps	3 bps
Fixed Income	Yield	OAS	1W Return	1M Return	3M Return	12M Return	YTD Return
Barclays Capital U.S. Government-Treasury	0.68%	N/A	-0.7%	-1.3%	-1.1%	4.0%	-1.3%
Barclays Capital U.S. TIPS	0.79%	N/A	0.0%	0.2%	2.4%	9.1%	0.2%
Barclays Capital U.S. Aggregate	1.21%	35	-0.5%	-1.0%	0.1%	4.4%	-1.0%
Barclays Capital Global Aggregate	0.90%	34	-0.7%	-1.5%	1.4%	6.5%	-1.5%
Barclays Capital U.S. ABS	0.40%	27	0.0%	0.1%	0.4%	3.6%	0.1%
Barclays Capital U.S. MBS	1.23%	15	0.0%	0.0%	0.4%	3.2%	0.0%
Barclays Capital U.S. Corporate Investment Grade	1.90%	95	-0.7%	-1.7%	1.4%	5.5%	-1.7%
BAML Euro Corporate Investment Grade	0.25%	90	-0.1%	-0.1%	0.9%	1.5%	-0.1%
Barclays Capital U.S. Corporate High Yield	4.12%	342	0.4%	0.8%	6.0%	7.8%	0.8%
BAML European Currency High Yield Non-Financial	2.85%	340	0.6%	1.1%	5.5%	3.8%	1.1%
CS U.S. Leveraged Loans	4.79%	454	0.0%	1.2%	4.6%	3.7%	1.4%
CS Western European Leveraged Loans Non-USD	4.37%	431	0.1%	0.9%	4.2%	3.2%	1.0%
JPM CEMBI Broad Diversified	4.13%	319	0.1%	0.1%	3.8%	5.6%	0.1%
JPM EMBI Global Diversified	4.71%	347	0.2%	-0.9%	3.2%	2.8%	-0.9%
JPM GBI-EM Global Diversified	4.26%	N/A	0.8%	-0.8%	7.0%	2.3%	-0.8%
Equities	Price	Div Yield	1W Return	1M Return	3M Return	12M Return	YTD Return
S&P 500	3,830.17	1.47%	2.1%	2.1%	14.1%	20.0%	2.1%
Euro STOXX 600 (Local)	407.27	2.05%	1.1%	2.1%	14.4%	-1.1%	2.1%
U.K. FTSE 100 (Local)	6,507.82	3.53%	-0.9%	0.7%	12.5%	-11.2%	0.7%
Japan Nikkei 225 (Local)	28,646.50	1.42%	0.0%	4.4%	23.0%	24.7%	4.4%
China Shanghai Composite (Local)	3,517.31	2.01%	-1.6%	1.3%	7.5%	28.1%	1.3%
MSCI AC World (Local)	662.97	1.77%	1.8%	3.2%	13.9%	16.9%	3.2%
MSCI Emerging Markets (Local)	1,392.64	1.77%	1.7%	8.6%	20.9%	31.8%	8.6%
Commodities/Currencies	Price	1W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
S&P GS Commodity Index	445.62	2.8%	8.8%	27.9%	29.3%	16.9%	8.8%
WTI Crude (\$/bbl)	55.69	5.5%	15.2%	48.7%	36.4%	11.2%	15.2%
Copper (\$/lb)	3.58	0.2%	1.8%	15.9%	23.1%	42.4%	1.8%
Gold (\$/oz)	1,835.45	-0.4%	-2.8%	-3.8%	-6.3%	16.6%	-2.8%
U.S. Dollar Index	91.17	0.6%	1.4%	-2.5%	-2.3%	-6.8%	1.4%
Euro (USD/EUR)	1.20	-0.6%	-1.8%	2.4%	2.3%	8.6%	-1.8%
British Pound (USD/GBP)	1.36	-0.4%	-0.2%	4.4%	4.7%	4.9%	-0.2%
Japanese Yen (Yen/USD)	105.08	0.9%	1.8%	0.5%	-1.0%	-3.3%	1.8%
Chinese Yuan (CNY/USD)	6.46	-0.2%	-1.3%	-3.5%	-7.5%	-8.1%	-1.3%

Source: FactSet and Bloomberg. As of February 03, 2021.

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*As of December 31, 2020
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