



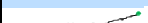









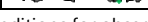
- Fund manager survey shows investors still bullish despite high equity valuations ([link](#))
- Global FX volatility reaches multi-decade low ([link](#))
- Rebound in German PMI boosts European equities ([link](#))
- Markets price in about a 50% probability of a BoE rate cut next week amid PMI data ([link](#))
- Nigerian central bank expected to keep policy rate on hold despite higher inflation ([link](#))

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Global markets rebound on improving data and easing virus concerns

Global equities are posting gains as better than expected earnings and preliminary PMI readings are providing early signs of some bottoming out of industrial activity and economic growth. Yesterday, the coronavirus threat continued to weigh on investor sentiment as US Treasury yields declined 1 to 4 bps across maturities and benchmark 10-year yields reached year-to-date lows at 1.73%. Crude oil prices fell sharply to their lowest level since December, which is around 12% below the height of the US-Iran confrontation earlier this month. However, this morning the release of preliminary PMI readings in Japan, the Eurozone, and UK showed a rebound in the manufacturing sector that was broadly better than expected and has provided encouraging signs that manufacturing PMIs appear to be moving away from contraction. European equity markets have rallied in response with most indices up over 1% and core sovereign yields inching up only slightly. The UK PMI readings bounced as business sentiment improved, but the results did not materially alter the markets expectations of around a 50% chance for a BoE policy rate cut next week. Asian stocks were little changed overnight with a number of markets closed for holidays, and EM assets have traded calmly with the broad EM equity index posting gains for the first time this week.

Key Global Financial Indicators

Last updated: 1/24/20 8:02 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		3326	0.1	1	3	26	3
Eurostoxx 50		3787	1.4	-1	0	21	1
Nikkei 225		23827	0.1	-1	0	16	1
MSCI EM		45	1.3	-2	1	9	0
Yields and Spreads			bps				
US 10y Yield		1.73	-3.7	-9	-17	-98	-18
Germany 10y Yield		-0.30	0.9	-8	-6	-48	-11
EMBIG Sovereign Spread		302	0	9	7	-64	9
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		60.8	-0.1	0	-1	-4	-1
Dollar index, (+) = \$ appreciation		97.9	0.2	0	0	1	2
Brent Crude Oil (\$/barrel)		61.8	-0.4	-5	-8	1	-6
VIX Index (% change in pp)		12.8	-0.2	0	0	-6	-1

Colors denote tightening/easing financial conditions for observations greater than ± 1.5 standard deviations. Data source: Bloomberg.

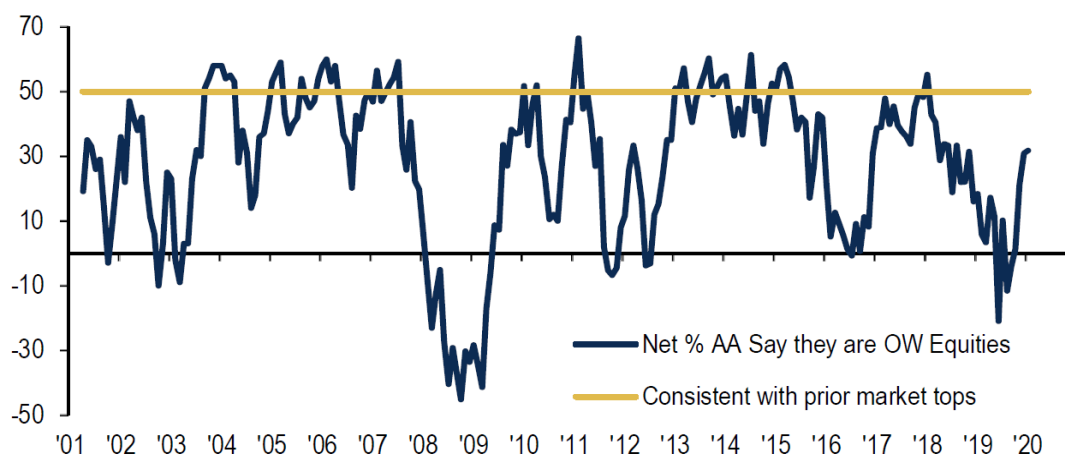
United States

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Worries about the virus continued to unsettle markets around the world. Yesterday, sizeable selloffs in Asia were followed by another negative close in Europe. Safe haven assets continued their rally as benchmark 10-year US Treasury yields fell to a new low for the year (1.73%) and its lowest level in over seven weeks. However, US equity markets staged an intra-day rebound to end little changed on the day as the worst of the negative sentiment appeared to dissipate by the end of the session. Moreover, volatility across major asset classes remains subdued and many global bourses remain in positive territory for the year, suggesting that most still expect the impact of the virus to be relatively moderate.

Global fund managers are getting more bullish about equities, but their bullish sentiment has not yet reached unsustainable levels, according to the latest survey data from the Bank of America. Since August 2019, investors went from 19% underweight in their equity allocations to 32% overweight in the current survey, the largest bullish shift in positioning since 2011. History shows that market rallies tend to stall when the equity overweight nears 50%. A key source of investor optimism derives from their view that there will be strong global growth over the next 12 months.

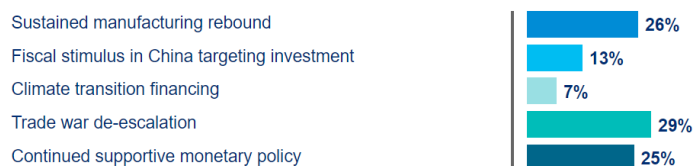
Exhibit 3: FMS equity allocation not yet at euphoric levels



Source: BofA Global Fund Manager Survey

A poll by Citi corroborates the overall optimistic tone of investor sentiment, as its survey also finds that a global rebound is widely expected. The de-escalation of the trade war had the biggest positive impact on sentiment, but the continued support from major global central banks was also a major factor boosting markets. The poll predicts that a manufacturing rebound will be a key driver of positive global growth. However, the possibility of a US recession or a flareup in geopolitical tensions were identified as the biggest downside risks. Although the poll did not address it, contacts who discussed the results flagged rising concern about the impact of the virus as the wildcard with potentially significant implications for China and the broader global economy if the impact is not contained.

What is the greatest upside risk for the global outlook?



Readers' poll results (open through 22-Jan-2020).

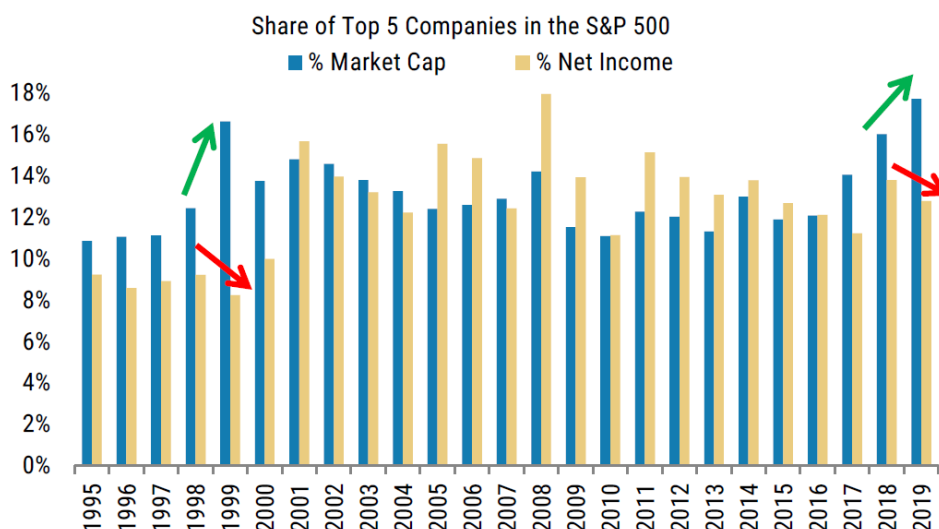
What is the greatest downside risk for the global outlook?



Readers' poll results (open through 22-Jan-2020).

The US equity market exhibits a very uneven distribution of returns, with the top five companies in the S&P 500 accounting for 18% of the return to the index last year. Morgan Stanley points out that this is the most extreme deviation in history, and that all top five companies are technology firms (Apple, Google, Microsoft, Amazon and Facebook). In addition, the gap between the return on the index and the net income of the member corporations has grown very wide, approaching the level last seen in 1999 before the dotcom crash. Some analysts point to these unusual circumstances and warn that they suggest an unsustainable situation for the US market. A major negative surprise in the technology sector could have spillover effects to the broader market, and earnings expectations for the corporate sector overall may be too optimistic given the weakening trend in net income. The contribution of the bad news from Apple to the major selloff in 2018 was cited as an example. With valuations even more stretched today, the downside could be much greater. However, some observers are skeptical about comparisons to 1999, pointing out that dotcom-era profits were non-existent, but today's tech giants are among the most profitable corporations in history.

Exhibit 5: There is a growing divergence between top 1% market cap and net income concentration

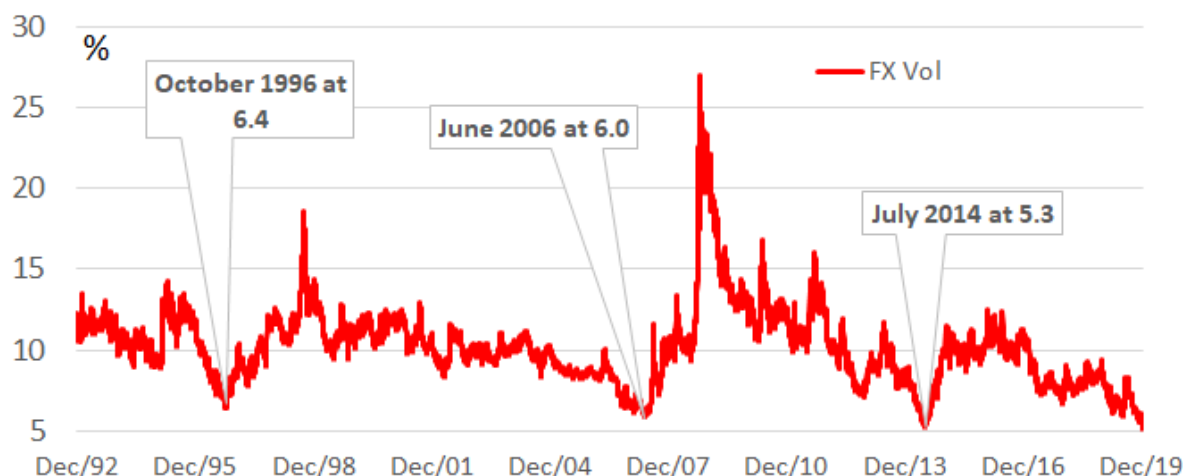


Source: Bloomberg, Factset, Morgan Stanley Research

Currency Markets

Global FX volatility fell to a multi-decade low this week. Contacts believe that lower cross-country data dispersion has contributed to this trend. In other words, the world grows/slow and eases/hikes in lockstep. Second, central bank actions have dampened volatility as the distribution of potential outcomes (including tail risks) have been greatly reduced. Finally, contacts argue that the absence of yield vis-à-vis investors' return objectives and perceived policy puts have led to the systematic selling of volatility.

Currency markets: JP Morgan Index for Global FX volatility



Note: Index tracks levels of implied volatility of G-7 and EM currencies (turnover weighted).
Source: Bloomberg and IMF Staff

Europe [back to top](#)

Equities (+1.2%) gained. European bank stocks are up +0.9%. The euro edged lower against the USD. Core yields were little changed today.

A rebound in German PMI data in January drove the improvement in sentiment. German composite PMI rose to 51.1 (50.5 expected, from 50.2) with manufacturing rising to 45.2 (44.5) and services to 54.2 (53 expected). **Despite gains in Germany, euro area composite PMI data was unchanged from December at 50.9** (51.2 expected) reflecting disappointing services in France (at 51.7 compared to 52.2 expected) due to strikes.

European rates edged lower following yesterday's ECB press conference. President Lagarde acknowledged that inflation expectations have ticked up slightly but added that inflation pressures remain muted with growth risks still tilted to the downside despite "some stabilization in euro area growth dynamics." President Lagarde also reiterated that the ECB must use the tools it has available, including negative rates, and pushed back against an easy comparison with the Riksbank's return to zero policy rates.

Speaking at Davos today, **ECB President Lagarde warned investors not to assume that the ECB is on autopilot, reminding investors that policy is fact-dependent.** A Bloomberg survey (taken on 10-16 Jan) found that ECB watchers expect the ECB to run its current QE program till end 2021Q1 and do not expect the ECB to change rates till early 2022.

ECB Timeline

Economists see policy makers taking action by the following dates

December 2020	Change in forward guidance
4Q 2021	End of quantitative easing
2Q 2022	First interest-rate increase

Source: Bloomberg survey of economists conducted Jan. 10-16

Bloomberg

Expectations for euro area inflation, growth and unemployment remain broadly unchanged in the 2020Q1 ECB Survey of Professional Forecasters. Forecasts for annual HICP inflation average 1.2%, 1.4% and 1.5% for 2020, 2021 and 2022, respectively. Respondents reported a decline in overall uncertainty but the balance of risks for inflation and GDP growth remains to the downside.

United Kingdom

Markets are pricing in a 50/50 probability of a BoE rate cut next week as some analysts argue that survey data have not showed enough improvement to alleviate concerns of MPC members. The composite PMI rose to 52.4 in January (50.7 expected, from 49.3). The services PMI increased to 52.9 (51.1 expected, from 50). Manufacturing PMI also rose to 49.8 (48.8 expected, from 47.5). **The British pound is 0.3% weaker against the USD and equities are up 1.6%.**

Other Mature Markets

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Japan

The yen erased initial gains to end the day a touch weaker (-0.1%) while equities were little changed in a quiet session. JGBs were mixed; shorter-dated bond yields were mostly steady while longer-dated tenors fell. The 2-year yield was unchanged at -0.14% and the 30-year bond yield fell 1 bp to 0.40%.










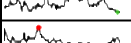



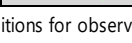
Emerging Markets

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Currencies and equities were little changed amid subdued trading as a number of markets – including China and Korea – were closed for the Spring Festival. Concerns about the spread of the coronavirus continued to weigh on investor sentiment, with authorities in China widening the travel ban to the surrounding cities beyond Wuhan. The Indonesian rupiah paced gains (+0.4%). Foreign purchases of Indonesian assets, particularly bonds, have supported the rupiah, which posted gains against the dollar since late November to its longest level of IR 13583/USD since February 2018. By contrast, the Thai baht underperformed, losing 0.2% against the dollar on the day. **EMEA** bourses were mixed, with the largest gains in South Africa (+0.7%) and the Czech Republic (+0.6%), and the largest losses taking place in Turkey (-0.6%) and Qatar (-0.5%). Currencies were stable. **Latin American** equities retreated yesterday, sliding by -2% in Argentina, -0.4% in Chile and -0.6% in Peru. The region's bright spot for the day was Brazil as the Bovespa gained 1%. Currencies depreciated in Colombia (-0.9%) and Chile (-0.6%) and stood almost flat in the other countries. Sovereign yields saw a mixed day, with local currency yield curves

trending up in Brazil and Chile (+8 bps to a 2.1% yield at the 3-year maturity), particularly at shorter maturities. USD debt yields remained flat, except for an increase by 6 bps to 1.15% on Mexican 3-year USD debt and a renewed upward shift in the Argentine USD debt yield curve (+37 bps at 2-year maturity).

Key Emerging Market Financial Indicators

Last updated: 1/24/20 8:06 AM	Level		Change				
	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks			%				%
MSCI EM Equities		44.96	1.3	-2	1	9	0
MSCI Frontier Equities		31.28	0.3	1	3	12	3
EMBIG Sovereign Spread (in bps)		302	0	9	7	-64	9
EM FX vs. USD		60.77	0.0	0	-1	-4	-1
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.94	-0.5	-1	1	-2	0
Indonesian Rupiah		13583	0.4	0	3	4	2
Indian Rupee		71.33	-0.1	0	0	0	0
Argentine Peso		60.31	-0.4	-1	-1	-38	-1
Brazil Real		4.18	-0.2	0	-2	-10	-4
Mexican Peso		18.78	0.0	-1	1	1	1
Russian Ruble		61.78	0.2	0	0	6	0
South African Rand		14.37	0.2	1	-1	-5	-3
Turkish Lira		5.94	-0.1	-1	0	-11	0
EM FX volatility		6.06	0.0	0.1	-0.4	-3.0	-0.5

Colors denote tightening/easing financial conditions for observations greater than ± 1.5 standard deviations. Data source: Bloomberg.

China

China's markets are closed for the week-long Spring Festival.

Argentina

Fitch followed the prior's day rating action of S&P and downgraded Argentina's local currency sovereign debt. Fitch reduced the Argentine sovereign debt rating for long-term local currency debt from CC and the one for short-term debt rating from C to restricted default. The rating agency elaborated that the currently attempted debt exchanges can be seen as a prevention of traditional defaults, without actually resolving the elevated probability for future defaults. The modest uptick in the level of the Argentine sovereign USD debt yield curve demonstrated that markets had already priced in the respective economic drivers in the previous days' changes in yield levels.

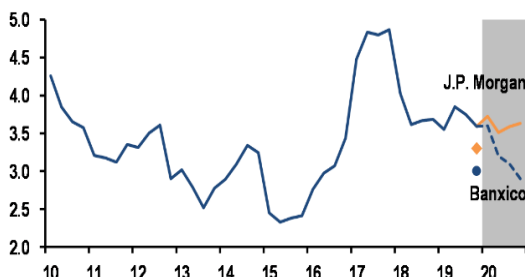
Inflation trends in Brazil and Mexico

Mixed inflation signals in Brazil and Mexico raised mixed expectations for monetary policy decisions. The expectations for moderate Brazilian inflation rates driven by weekly inflation figures for Sao Paulo were not entirely confirmed on the federal level. CPI figures came in at 0.71% m/m and 4.3% y/y, almost on par with expectations, but the CPI figure for metropolitan areas rose by 8 bps to 0.56% m/m, more than anticipated. Mexican inflation figures printed just a tick above expectations with 0.27% 2w/2w and 3.2% y/y, both slightly up from their prior values. JP Morgan analysts see Mexico's inflation slightly above the trend projected by Banxico, which would imply that inflation can be expected to limit the country's

space for rate cuts going forward. Contradicting this view, Bloomberg analysts suggest that both countries headline inflation figures almost met expectations and the recent appreciation trend in the Mexican peso provides room for future monetary relaxation.

Core CPI projection

%oya, quarterly

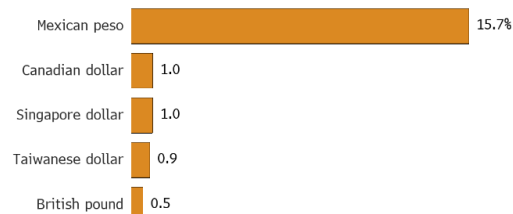


Source: Banxico, INEGI and J.P. Morgan forecasts (markers refer to forecasts at start of 2018).

King of Carry

Mexico's peso leads major currencies in carry since AMLO's inauguration

Carry return



Source: Bloomberg

Note: Carry return shown for Nov. 30, 2018 to Jan. 21, 2020

Bloomberg

Nigeria

The Nigerian central bank is expected to keep rates on hold today even as inflation rises. The consensus forecast is that the CBN will maintain its main policy rate at 13.50% despite the recent increase in headline inflation to 12% in December. Although the increase in prices has been largely driven by higher food costs, observers also point out that inflation has been running above the 9% upper target of the central bank for over 4 years. The Naira was trading 0.2% weaker to the dollar today – at 362.00 – ahead of the central bank's decision.

Nigerian inflation is at a 20-month high as food prices continue to surge

Headline inflation (YoY) Food inflation (YoY)



Source: National Bureau of Statistics





















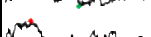

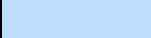



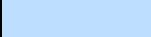


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Global Financial Indicators

Last updated: 1/24/20 8:03 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
United States		3326	0.1	1	3	26	3
Europe		3787	1.4	-1	0	21	1
Japan		23827	0.1	-1	0	16	1
China		2977	-2.8	-3	0	15	-2
Asia Ex Japan		74	-1.0	-2	1	10	0
Emerging Markets		45	1.3	-2	1	9	0
Interest Rates			basis points				
US 10y Yield		1.73	-3.7	-9	-17	-98	-18
Germany 10y Yield		-0.30	0.9	-8	-6	-48	-11
Japan 10y Yield		-0.02	-0.3	-2	-3	-3	-1
UK 10y Yield		0.59	0.0	-4	-18	-67	-23
Credit Spreads			basis points				
US Investment Grade		101	1.7	0	-1	-29	3
US High Yield		405	8.6	17	12	-36	12
Europe IG		44	-1.2	1	-1	-33	-1
Europe HY		214	-3.9	7	5	-114	7
EMBIG Sovereign Spread		302	0.0	9	7	-64	9
Exchange Rates			%				
USD/Majors		97.86	0.2	0	0	1	2
EUR/USD		1.10	-0.2	-1	-1	-2	-2
USD/JPY		109.6	-0.1	0	0	0	-1
EM/USD		60.8	-0.1	0	-1	-4	-1
Commodities			%				
Brent Crude Oil (\$/barrel)		62	-0.4	-5	-8	1	-6
Industrials Metals (index)		112	-0.6	-4	-3	-1	-2
Agriculture (index)		40	-0.9	0	-1	-6	-2
Implied Volatility			%				
VIX Index (% change in pp)		12.8	-0.2	0.5	0.1	-6.1	-1.0
10y Treasury Volatility Index		4.1	0.2	0.4	0.0	0.0	0.0
Global FX Volatility		5.3	0.0	0.1	-0.2	-2.6	-0.7
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		161	-3.4	-2	-9	-236	-4
Italy		156	-0.3	-3	-11	-92	-4
Portugal		70	-1.2	-1	4	-77	7
Spain		68	1.1	0	0	-38	2

Colors denote **tightening**/**easing** financial conditions for observations greater than ± 1.5 standard deviations.

Data source: Bloomberg.

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Emerging Market Financial Indicators

Last updated: 1/24/2020 8:06 AM	Exchange Rates						Local Currency Bond Yields (GBI EM)							
	Level		Change (in %)				YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
	vs. USD		(+) = EM appreciation					% p.a.						
China		6.94	-0.5	-0.9	1	-2	0		3.0	-2.0	-9	-16	-4	-11
Indonesia		13583	0.4	0.5	3	4	2		6.8	-1.3	-17	-40	-146	-31
India		71	-0.1	-0.4	0	0	0		6.9	-1.9	-5	-1	-70	-1
Philippines		51	0.3	0.2	0	4	0		4.3	-0.6	-1	-1	-156	-5
Thailand		31	-0.3	-0.6	-1	4	-2		1.6	-1.1	-2	-9	-106	-5
Malaysia		4.06	0.3	-0.1	2	2	1		3.1	-1.4	-14	-25	-89	-21
Argentina		60	-0.4	-0.6	-1	-38	-1		53.8	111.1	-22	-714	3256	-880
Brazil		4.18	-0.2	-0.4	-2	-10	-4		6.1	0.8	-12	-26	-180	-17
Chile		776	0.1	-0.4	-3	-14	-3		3.3	3.3	-2	2	-119	5
Colombia		3364	-0.1	-0.9	-2	-6	-3		5.7	-0.3	-5	-27	-93	-27
Mexico		18.78	0.0	-0.6	1	1	1		6.9	-2.8	-4	-11	-176	-5
Peru		3.3	-0.2	0.1	0	1	0		4.4	-0.7	-6	-9	-137	-14
Uruguay		37	0.1	0.5	-1	-13	0		10.5	-6.4	-27	-45		-42
Hungary		305	0.1	-0.5	-2	-7	-3		1.3	-4.2	7	21	-85	14
Poland		3.86	-0.5	-0.9	0	-2	-2		2.0	-1.6	-3	14	-27	12
Romania		4.3	-0.2	-0.6	-1	-3	-2		3.9	-1.0	1	-12	-60	-11
Russia		61.8	0.2	-0.3	0	6	0		6.0	-1.4	-3	-26	-214	-17
South Africa		14.4	0.2	0.7	-1	-5	-3		9.5	5.8	-1	2	-3	1
Turkey		5.94	-0.1	-0.9	0	-11	0		10.2	-9.3	-16	-181	-617	-150
US (DXY; 5y UST)		98	0.2	0.3	0	1	2		1.55	0.3	-7	-16	-100	-14

	Equity Markets							Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)				YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
									basis points					
China		2977	-0.1	-3	0	15	-2		174	0	1	-2	-8	-2
Indonesia		6244	-1.3	-1	-1	-3	-1		168	1	6	8	-34	12
India		41613	12.0	-1	0	15	1		127	0	1	0	-56	2
Philippines		7623	-4.2	-1	-3	-5	-2		72	0	1	2	-25	6
Malaysia		1573	-2.0	-1	-2	-7	-1		104	0	1	-7	-36	-8
Argentina		41140	-1.7	-3	3	18	-1		2001	1	169	140	1338	232
Brazil		119528	0.2	1	3	22	3		219	0	9	5	-23	4
Chile		4653	0.8	-5	-1	-14	0		147	1	7	7	1	14
Colombia		1648	0.6	0	-1	16	-1		174	1	6	8	-24	11
Mexico		45476	-0.1	0	3	4	4		298	1	3	1	-18	6
Peru		20545	-0.8	0	1	4	0		116	0	7	6	-34	9
Hungary		44792	10.6	1	-3	10	-3		97	0	6	9	-39	11
Poland		58798	1.9	0	2	-3	2		24	-1	4	7	-41	6
Romania		10220	10.7	1	3	43	2		185	3	6	12	-32	12
Russia		3152	13.1	-1	4	27	3		143	1	5	10	-74	12
South Africa		57204	3.0	-3	0	7	0		340	-1	11	14	22	20
Turkey		121394	20.7	0	7	19	6		365	0	-5	-42	-44	-36
Ukraine		505	-4.2	0	-1	-8	-1		369	-6	13	-48	-289	-51
EM total		45	1.3	-2	1	9	0		302	0	9	7	-64	9

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

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