

Jeromicron: Markets Face a One-Two Punch

WATCH LIST

Date		Period	Consensus		Previous
U.S.					
Tue 2/1	ISM Manufacturing	Jan	58.0	▼	58.7
Tue 2/1	JOLTS Job Openings	Dec			10562 K
Tue 2/1	Wards Total Vehicle Sales	Jan	12.60 M	▲	12.44 M
Wed 2/2	ADP Employment Change	Jan	208 K	▼	807 K
Thu 2/3	Nonfarm Productivity (Prelim. Est.)	4Q21	2.3%	▲	-5.2%
Thu 2/3	ISM Services Index	Jan	59.6	▼	62.0
Fri 2/4	Change in Nonfarm Payrolls	Jan	178 K	▼	199 K
Fri 2/4	Unemployment Rate	Jan	3.9%	-	3.9%
Fri 2/4	Labor Force Participation Rate	Jan	61.9%	-	61.9%
Europe					
Mon 1/31	EA GDP (Advance Est.)	4Q21	0.4% Q/Q	▼	2.2% Q/Q
Tue 2/1	EA Unemployment Rate	Dec	7.2%	-	7.2%
Wed 2/2	EA Consumer Price Index	Jan	4.0% Y/Y	▼	5.0% Y/Y
Thu 2/3	ECB Monetary Policy Meeting	Feb	0.0%	-	0.0%
Thu 2/3	Bank of England Bank Rate	Feb	0.5%	▲	0.25%
Fri 2/4	EA Retail Sales	Dec	-0.5% M/M	▼	1.0% M/M
Asia Pacific					
Mon 1/30 - Fri 2/4	China Markets Closed – Lunar New Year				
Sun 1/30	China Manufacturing PMI	Jan	50.0	▼	50.3
Sun 1/30	China Nonmanufacturing PMI	Jan	51.0	▼	52.7
Sun 1/30	Caixin China Manufacturing PMI	Jan	50.0	▼	50.9
Mon 1/31	Japan Retail Sales	Dec	0.4% M/M	▼	1.2% M/M
Mon 1/31	Japan Industrial Production (Prelim. Est.)	Dec	0.0% M/M	▼	7.0% M/M
Tue 2/1	Japan Jobless Rate	Dec	2.8%	-	2.8%
Tue 2/1 - Thu 2/3	Hong Kong Markets Closed – Lunar New Year				

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

U.S.

- We will watch the labor supply as **the January employment report** reveals the impact from Omicron. Meanwhile, **job openings data** is expected to show still-elevated labor demand.
- Q4 productivity growth** is expected to accelerate.

Europe

- If euro area CPI** does not show a steep decline, as expected, worries about runaway inflation would likely resurface in markets.
- We will watch the **BoE** for interest rate increases in response to rising inflation, and if the **ECB** signals any change to its accommodative stance.

Asia Pacific

- China manufacturing PMIs** for January should remain stable while **services PMIs** could deteriorate, given the rise in cases.
- The Beijing 2022 Winter Olympics** are scheduled to begin Friday, February 4, and run through February 20 (select events start Tuesday, February 2).

What This Week Means For Markets

Markets had a hawkish interpretation of the FOMC press conference, viewing rising inflation fears as a signal that risks are tilted toward more, rather than less, tightening. Markets are now pricing in five hikes this year, with 20% odds of a 50bps hike in March. This led to a risk-off tone in markets with yields rising, the curve flattening, equities lower, and the U.S. dollar index higher. Our central scenario maintains the Fed will strike **A Fine Balance** to ease inflation without unnecessarily slowing growth. Separately, ongoing tensions between Russia and Ukraine are boosting oil prices, with Brent reaching \$90/bbl. Please see our [Monthly Macro Dashboard](#).

IN REVIEW

PMIs Show Omicron's Hit to Supply & Demand

Preliminary Markit PMIs in the U.S. show Omicron weighed on consumer demand, labor supply, and supply chain disruptions in January. The composite PMI fell from 57 to 50.8—its lowest level in 18 months; declines were seen in services (January: 50.9 vs. December: 57.6) and manufacturing (January: 55 vs. December: 57.7). Businesses, which expressed concern about consumer responses to further price increases, also noted a modest rise in services employment, while manufacturing employment took a step back. Supply chain disruptions continued to weigh on growth, though deterioration slowed, leading to manufacturers' improved optimism and easing input price growth (which rose at the slowest pace since March). Supply chains need time to heal, but this is an encouraging sign for the inflation outlook.

The January **euro area** composite PMI declined to 52.4, from 53.3 in December and below consensus (52.6), due largely to COVID restrictions on services. The EA services PMI dropped to 51.2 in January (cons. 52.2), the slowest output growth since April. The manufacturing PMI rose to 59, a five-month high, a sign of easing supply constraints and staffing restrictions. A milder version of 2020–21 is unfolding: services suffer from COVID restrictions; manufacturing shows continued strength.

The **U.K.** composite PMI was 53.4 in January, below 53.6 in December and consensus (55). This lowest print since March shows the economy is losing momentum as restrictions weigh on services, Brexit impacts labor markets and trade, and financial conditions are tightening with increasingly hawkish BoE policies. Unlike the euro area, the U.K. manufacturing PMI fell to 56.9, below December and consensus (both 57.9).

Japan's manufacturing sector remained resilient in January as the service sector showed a sharp drop amid surging cases. The manufacturing PMI rose to 54.6, from 54.3, aided by output, new orders, and stocks of purchases. Omicron's rapid spread this year has caused a notable deterioration in services PMI, down to 46.6, from 52.1; it could fall more with new restrictions.

Fed Confirms a March Liftoff

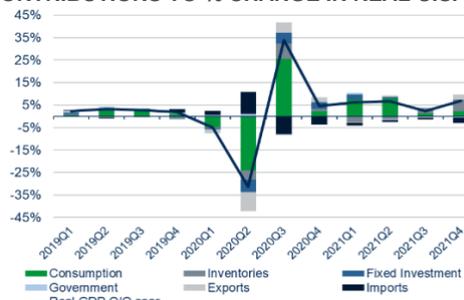
Inflation concerns from Chairman Jerome Powell at the January FOMC meeting led to a hawkish read by markets. Quantitative easing (QE) will end in early March, setting the stage for a liftoff, given elevated inflation concerns and FOMC members who see the labor market meeting maximum employment requirements. Expect the Fed to wait for liftoff before beginning quantitative tightening (QT). However, little guidance was given on the pace

of tightening as the FOMC will adjust policy as needed in response to the evolving economic environment. A March liftoff and QT this year were already priced into markets and in line with our central scenario, **A Fine Balance**. The FOMC will monitor two-sided risks: inflation remaining elevated for longer (**Runaway Train** scenario), and policy tightening that hurts the recovery (**Gravity Prevails** scenario). Powell is trying to strike a *fine balance* of normalizing inflation without hurting the recovery and appears to be more concerned about Runaway Train than Gravity Prevails—suggesting risks tilt toward more rate hikes, not less. Markets interpreted this as more hawkish, resulting in a risk-off tone with equities lower, yields higher, the curve flattening, and the U.S. dollar index rising.

U.S. GDP Accelerates in Q4

After the Delta-induced Q3 slowdown, U.S. Q4 GDP accelerated faster than consensus expected, up 6.9% Q/Q at an annualized pace (cons. 5.5%), bringing full-year 2021 growth to 5.5%—the strongest since 1984. Q4 growth was led by rising inventories (notably autos), personal consumption, exports, and business investment; government spending and imports were a drag.

CONTRIBUTIONS TO % CHANGE IN REAL U.S. GDP



Source: Bloomberg. As of January 27, 2022.

Omicron should slow 1Q22 growth, albeit temporarily. Strong consumer balance sheets and a continued inventory rebuild should support moderating but above-trend growth in 2022.

Earnings Still Outpace Expectations So Far

With 30% of S&P 500 companies reporting 4Q21 financials, earnings is on track to grow 22% Y/Y, representing a 2% beat over consensus, the weakest outperformance since the pandemic started. The largest earnings surprises were energy and financials, while industrials and real estate lagged. Inflation and COVID remain prominent, with labor and supply chain issues cited as risks. The strong U.S. dollar is becoming a small headwind to revenues. Expect profit margins to be the focus this season given increased cost pressures, historically high margins in Q3, and weak seasonality. Look for differentiation among companies with and without pricing power.

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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	0 bps	0 bps
U.S. SOFR	0.04%	-1 bps	-1 bps	-1 bps	-1 bps	1 bps	-1 bps
3 Month USD Libor	0.28%	2 bps	6 bps	14 bps	15 bps	6 bps	7 bps
3 Month Euribor	-0.55%	0 bps	3 bps	0 bps	-1 bps	-2 bps	2 bps
3 Month U.S. T-Bill	0.19%	2 bps	12 bps	14 bps	15 bps	12 bps	14 bps
2-Year U.S. Treasury	1.07%	6 bps	38 bps	62 bps	87 bps	95 bps	35 bps
10-Year U.S. Treasury	1.84%	1 bps	34 bps	22 bps	56 bps	80 bps	33 bps
10-Year German Bund	-0.08%	-7 bps	17 bps	4 bps	33 bps	46 bps	10 bps
10-Year U.K. Gilt	1.19%	-8 bps	26 bps	7 bps	61 bps	93 bps	22 bps
10-Year JGB	0.14%	-1 bps	8 bps	4 bps	13 bps	11 bps	7 bps
Fixed Income	Yield	OAS	1W Return	1M Return	3M Return	12M Return	YTD Return
Barclays Capital U.S. Government-Treasury	1.61%	N/A	-0.2%	-2.2%	-1.7%	-3.9%	-2.3%
Barclays Capital U.S. TIPS	1.77%	N/A	0.2%	-2.1%	-2.3%	2.6%	-2.9%
Barclays Capital U.S. Aggregate	2.14%	35	-0.3%	-2.3%	-2.1%	-3.4%	-2.4%
Barclays Capital Global Aggregate	1.53%	36	-0.2%	-1.5%	-2.0%	-5.7%	-1.6%
Barclays Capital U.S. ABS	1.43%	30	-0.1%	-0.5%	-0.8%	-1.0%	-0.6%
Barclays Capital U.S. MBS	2.32%	22	-0.1%	-1.8%	-2.0%	-2.9%	-1.9%
Barclays Capital U.S. Corporate Investment Grade	2.78%	100	-0.6%	-3.2%	-3.1%	-3.6%	-3.5%
BAML Euro Corporate Investment Grade	0.62%	104	0.2%	-0.9%	-1.0%	-1.7%	-0.7%
Barclays Capital U.S. Corporate High Yield	4.98%	315	-0.7%	-1.7%	-1.0%	2.8%	-1.9%
BAML European Currency High Yield Non-Financial	3.32%	355	-0.4%	-0.6%	-0.5%	1.9%	-0.7%
CS U.S. Leveraged Loans	5.51%	426	-0.1%	0.7%	1.0%	4.4%	0.5%
JPM CEMBI Broad Diversified	4.93%	312	0.0%	-1.4%	-1.8%	-0.6%	-1.5%
JPM EMBI Global Diversified	5.74%	383	0.3%	-2.7%	-3.5%	-3.7%	-2.9%
JPM GBI-EM Global Diversified	5.90%	N/A	-0.2%	0.1%	-1.9%	-7.8%	-0.1%
Equities	Price	Div Yield	1W Return	1M Return	3M Return	12M Return	YTD Return
S&P 500	4,349.93	1.34%	-4.0%	-7.9%	-4.6%	14.6%	-8.7%
Euro STOXX 600 (Local)	467.31	2.66%	-2.8%	-3.2%	-1.8%	14.6%	-4.2%
U.K. FTSE 100 (Local)	7,469.78	3.34%	-1.6%	1.3%	2.6%	12.3%	1.2%
Japan Nikkei 225 (Local)	27,011.33	1.76%	-1.7%	-6.2%	-7.2%	-5.4%	-6.2%
China Shanghai Composite (Local)	3,455.67	2.08%	-2.9%	-4.5%	-3.9%	-3.2%	-5.1%
MSCI AC World (Local)	701.13	1.88%	-3.5%	-6.3%	-4.5%	9.4%	-6.9%
MSCI Emerging Markets (Local)	1,211.45	2.47%	-2.1%	-0.7%	-4.6%	-8.8%	-1.6%
Commodities/Currencies	Price	1W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
S&P GS Commodity Index	619.55	1.4%	11.0%	3.6%	15.7%	42.8%	10.4%
WTI Crude (\$/bbl)	87.35	0.6%	18.2%	2.0%	21.1%	66.0%	16.0%
Copper (\$/lb)	4.50	0.9%	2.7%	0.4%	-1.8%	24.2%	1.1%
Gold (\$/oz)	1,835.95	0.5%	1.7%	2.8%	2.0%	-1.1%	1.7%
U.S. Dollar Index	95.95	0.5%	-0.1%	2.1%	3.6%	6.4%	0.0%
Euro (USD/EUR)	1.13	-0.6%	-0.4%	-2.7%	-4.5%	-7.3%	-0.8%
British Pound (USD/GBP)	1.35	-0.9%	0.7%	-2.0%	-2.3%	-1.7%	-0.3%
Japanese Yen (Yen/USD)	114.33	0.0%	-0.1%	0.1%	3.6%	10.3%	-0.7%
Chinese Yuan (CNY/USD)	6.32	-0.5%	-0.7%	-0.9%	-2.5%	-2.4%	-0.8%

Source: FactSet and Bloomberg. As of January 26, 2022.

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