BARINGS INVESTMENT INSTITUTE

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THE WEEK AHEAD

A Time to Tighten

WATCH LIST

Date		Period	Consensus		Previous
U.S.					
Wed 3/23	New Home Sales	Feb	814 K	▲	801 K
Thu 3/24	Markit Manufacturing PMI (Prelim. Est.)	Mar	55.0	▼	57.3
Thu 3/24	Markit Services PMI (Prelim. Est.)	Mar			56.5
Fri 3/25	Pending Home Sales	Feb	1.0% M/M	▲	-5.7% M/M
Europe					
Mon 3/21	Germany Producer Price Index	Feb			25% Y/Y
Wed 3/23	EA Consumer Confidence (Advance Est.)	Mar			-8.8
Wed 3/23	U.K. Consumer Price Index	Feb	5.9% Y/Y	▲	5.5% Y/Y
Thu 3/24	EA Markit Manufacturing PMI (Prelim. Est.)	Mar	56.0	▼	58.2
Thu 3/24	EA Markit Services PMI (Prelim. Est.)	Mar	55.0	▼	55.5
Asia Pacific					
Mon 3/21	China 1-Year Loan Prime Rate	Mar	3.70%	-	3.70%
Mon 3/21	South Korea Exports 20 Days	Mar			13.1% Y/Y
Thu 3/24	Jibun Bank Japan Manufacturing PMI (Prelim. Est.)	Mar			52.7
Thu 3/24	Jibun Bank Japan Services PMI (Prelim. Est.)	Mar			44.2

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

U.S.

- We will watch the **preliminary Markit PMIs for March** to see if and how the war in Ukraine is impacting inflation and affecting businesses and consumer demand.
- **We will continue to watch housing data** amid rising mortgage rates and still-low inventories.

Europe

- The **military and economic responses to Russia's war in Ukraine** continue to garner attention, as ongoing disruptions in oil and agriculture flows will add to inflation pressures in much of the world.
- **U.K. CPI for February** will confirm the rising challenge for the Bank of England.
- **March flash PMIs** will indicate the hit to activity from the start of the war in Ukraine.

Asia Pacific

- The **PBOC is expected to keep the 1-year loan prime rate** unchanged. Amid growing headwinds to the economy, however, it's likely more easing can be expected this year.
- **Japan PMIs for March** should show any lingering impact of the latest surge in COVID cases, particularly on services.

What This Week Means For Markets

Oil and commodity prices this week fluctuated but remain elevated, as does volatility, amid the continued war in Ukraine and unsuccessful diplomatic efforts to end fighting. On Wednesday, the FOMC kicked off its hiking cycle with a 25bp rise in the Fed funds rate. Comments at the press conference suggest the committee will prioritize inflation over growth, which led to further U.S. curve flattening amid growth concerns. The FOMC's message indicates achieving our "Fine Balance" scenario of taming inflation without crimping activity too much remains possible. However, we believe mounting risks to the outlook have significantly reduced the likelihood of this occurring. Please see our Macro Dashboard.

IN REVIEW

Weight of War Grows Heavier Every Day

Fighting remains active, and U.S. estimates suggest Russia has lost about 10% of its invasion force in the first three weeks. A protracted conflict seems increasingly likely, especially with the Ukrainian Air Force reportedly still operational, including drones. Diplomatic efforts to end hostilities remain in flux. Despite optimism earlier in the week of a negotiated "neutrality" deal, messaging from Russian officials has limited progress. China meanwhile continued to toe its own line of neutrality, affirming its relationship with Ukraine and promising it would never attack. Finally, there is added financial uncertainty, as coupons of two Russian eurobonds (2023 and 2043) totaling $117 million were due this week, with three others due later this month. Any missed payments will trigger the first sovereign default for Russia since 1998, a default on domestic debt.

Ready, Set, Liftoff…

The FOMC began its hiking cycle Wednesday, lifting the target range for the Fed funds rate 25bps to 0.25%-0.50%—as expected. The updated summary of economic projections (SEP) showed large upward revisions in members' expectations for inflation and rate hikes. Meanwhile, comments at the press conference suggest the FOMC will be weighing inflation over growth this tightening cycle.

MARCH FOMC SUMMARY OF ECONOMIC PROJECTIONS

Variable	2022	2023	2024	Longer run
GDP	2.8%	2.2%	2.0%	1.8%
Unemployment Rate	3.5%	3.5%	3.6%	4.0%
PCE Inflation	4.3%	2.7%	2.3%	2.0%
Federal Funds Rate	1.9%	2.8%	2.8%	2.4%

Source: Federal Reserve. As of March 17, 2022.

While there was wide dispersion among estimates, the median dot suggests seven rate hikes in 2022 and four in 2023—in line with what markets had priced in ahead of the meeting. Our baseline outlook calls for inflation above the FOMC's median Summary of Economic Projections (SEP); therefore we think risks are skewed towards more, rather than less, hikes. In fact, comments by Chairman Jerome Powell at the press conference pointed to his continued hawkish pivot, signifying a vote in favor of a 50bps hike later this year is well within reason. While neither a timeline nor details for quantitative tightening (QT) were announced, Powell's comments suggest the green light will likely be given at the next meeting in May. While it was noted that Russia's invasion of Ukraine could further snarl supply chains and weigh on activity, the chance of a recession or serious slowdown in growth was downplayed. The FOMC message is one of being able to achieve the Fine Balance scenario: bringing down inflation without unnecessarily slowing growth. However, as risks to the outlook mount, achieving this feat is no longer our central scenario (see link on page 1).

Dovish Tightening by the Bank of England

The Bank of England delivered a well-expected 25bps rate hike, raising the policy rate back to its pre-pandemic 0.75% level—but its dovish tone surprised markets. It emphasized the daunting trade-off between growth and inflation, noting that "some further modest tightening in monetary policy may be appropriate in the coming months, but [that] there [were] risks on both sides of that judgement depending on how medium-term prospects for inflation evolve." The Bank saw the cost-of-living shock from rising inflation as disinflationary, perhaps hinting that much more tightening may not be needed. It has frontloaded tightening compared to the U.S., which may allow less tightening later. Markets are pricing the policy rate to peak at 2.25% in 18 months, which sounds like too much in light of Thursday's statement.

Too Early to Sound an All-Clear in China

Activity data in the January-February period surprised notably to the upside. This was due in large part to ongoing policy easing, a swift containment of this year's initial COVID wave, the "staying local" initiative allowing for a quicker resumption of industrial activity, and an easing in supply-side constraints. Fixed asset investment grew 12.2% Y/Y in the two-month period, led by robust gains in manufacturing, infrastructure, and real estate investment. Industrial production also stayed firm, growing 7.5% Y/Y, while retail sales beat expectations, increasing 6.7% Y/Y. Despite the strong start, however, significant downward pressures risk derailing growth this year. However, a recent and sharp resurgence of new COVID cases this month, separate from the increase in December, is bringing varying levels of new restrictions in several cities, including Shanghai and the tech-hub Shenzhen (Guangdong). Cities flagged as high- or medium-risk now cover nearly 25% of China's GDP. So far, the impact on supply chains has been minimal, with Chinese port congestion at levels broadly similar to last year. Nevertheless, there are concerns lockdowns could hit output in key industries such as electronics and machinery, especially as Guangdong accounts for 23% of China's exports. Against this backdrop, and an ambitious growth target this year, it's likely more fiscal and monetary policy support is needed to sustain the growth momentum.

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	0.05%	0 bps	0 bps	0 bps	0 bps	4 bps	0 bps
3 Month USD Libor	0.95%	20 bps	46 bps	73 bps	83 bps	76 bps	74 bps
3 Month Euribor	-0.49%	0 bps	4 bps	10 bps	6 bps	5 bps	9 bps
3 Month U.S. T-Bill	0.46%	8 bps	7 bps	41 bps	42 bps	44 bps	41 bps
2-Year U.S. Treasury	1.97%	30 bps	45 bps	136 bps	175 bps	183 bps	124 bps
10-Year U.S. Treasury	2.19%	24 bps	14 bps	77 bps	85 bps	57 bps	67 bps
10-Year German Bund	0.38%	18 bps	11 bps	73 bps	69 bps	72 bps	56 bps
10-Year U.K. Gilt	1.64%	12 bps	11 bps	86 bps	91 bps	86 bps	67 bps
10-Year JGB	0.20%	3 bps	-1 bps	16 bps	16 bps	11 bps	13 bps
Fixed Income	**Yield**	**OAS**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
Barclays Capital U.S. Government-Treasury	2.16%	N/A	-1.3%	-1.1%	-4.8%	-3.0%	-4.7%
Barclays Capital U.S. TIPS	2.29%	N/A	-1.8%	1.8%	-1.3%	5.0%	-2.2%
Barclays Capital U.S. Aggregate	2.75%	47	-1.3%	-1.5%	-5.6%	-3.8%	-5.5%
Barclays Capital Global Aggregate	2.02%	47	-1.4%	-2.7%	-6.3%	-6.9%	-5.9%
Barclays Capital U.S. ABS	2.49%	59	-0.6%	-1.0%	-2.4%	-2.6%	-2.3%
Barclays Capital U.S. MBS	2.84%	31	-1.3%	-1.2%	-4.3%	-4.4%	-4.3%
Barclays Capital U.S. Corporate Investment Grade	3.60%	136	-1.2%	-2.6%	-8.2%	-4.6%	-8.4%
BAML Euro Corporate Investment Grade	1.52%	152	-0.7%	-1.8%	-5.8%	-5.6%	-5.2%
Barclays Capital U.S. Corporate High Yield	6.29%	386	-1.0%	-1.7%	-5.2%	-1.3%	-5.8%
BAML European Currency High Yield Non-Financial	4.82%	459	0.1%	-2.6%	-5.6%	-4.0%	-5.7%
CS U.S. Leveraged Loans	7.22%	492	-1.3%	-1.7%	-1.2%	1.8%	-1.4%
JPM CEMBI Broad Diversified	6.41%	422	-0.6%	-6.9%	-9.0%	-7.7%	-9.1%
JPM EMBI Global Diversified	6.98%	469	1.2%	-6.9%	-10.6%	-8.7%	-10.6%
JPM GBI-EM Global Diversified	6.19%	N/A	0.1%	-9.2%	-6.6%	-11.7%	-8.0%
Equities	**Price**	**Div Yield**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
S&P 500	4,357.86	1.35%	1.9%	-2.5%	-6.3%	11.5%	-8.3%
Euro STOXX 600 (Local)	448.45	2.44%	3.2%	-4.1%	-5.9%	5.1%	-8.1%
U.K. FTSE 100 (Local)	7,291.68	3.39%	1.4%	-4.1%	0.4%	7.2%	-1.3%
Japan Nikkei 225 (Local)	25,762.01	1.90%	4.2%	-6.2%	-11.4%	-13.9%	-10.5%
China Shanghai Composite (Local)	3,170.71	2.25%	-2.6%	-8.5%	-13.7%	-8.0%	-12.9%
MSCI AC World (Local)	683.17	1.93%	1.9%	-3.5%	-7.0%	4.9%	-8.3%
MSCI Emerging Markets (Local)	1,081.00	2.62%	-0.6%	-10.9%	-9.4%	-15.2%	-10.3%
Commodities/Currencies	**Price**	**1W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
S&P GS Commodity Index	684.42	-8.2%	5.6%	25.3%	26.1%	39.6%	22.0%
WTI Crude ($/bbl)	95.04	-12.7%	1.3%	31.4%	30.7%	46.6%	26.2%
Copper ($/lb)	4.59	0.5%	1.0%	6.7%	7.2%	12.5%	3.0%
Gold ($/oz)	1,913.20	-3.8%	2.7%	6.5%	9.5%	10.3%	5.9%
U.S. Dollar Index	98.62	0.7%	3.0%	2.7%	6.1%	7.4%	2.8%
Euro (USD/EUR)	1.10	-0.5%	-3.3%	-2.8%	-6.5%	-7.6%	-3.3%
British Pound (USD/GBP)	1.31	-0.5%	-3.6%	-1.8%	-4.9%	-5.7%	-3.3%
Japanese Yen (Yen/USD)	118.50	2.3%	2.7%	4.2%	8.1%	8.7%	2.9%
Chinese Yuan (CNY/USD)	6.35	0.5%	0.2%	-0.3%	-1.5%	-2.4%	-0.4%

Source: FactSet and Bloomberg. As of March 17, 2022.

IMPORTANT INFORMATION

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