BARINGS INVESTMENT INSTITUTE

13 May 2022

THE WEEK AHEAD

Russian Gas Flows Face New Obstacles

WATCH LIST

Date		Period	Consensus		Previous
U.S.					
Tue 5/17	Retail Sales	Apr	0.9% M/M	▲	0.5% M/M
Tue 5/17	Industrial Production	Apr	0.4% M/M	▼	0.9% M/M
Tue 5/17	NAHB Housing Market Index	May	75	▼	77
Wed 5/18	Building Permits	Apr	1805 K	▼	1873 K
Wed 5/18	Housing Starts	Apr	1760 K	▼	1793 K
Thu 5/19	Existing Home Sales	Apr	5.65 M	▼	5.77 M
Europe					
Tue 5/17	U.K. Unemployment Rate	Mar	3.8%	-	3.8%
Wed 5/18	U.K. Consumer Price Index	Apr	9.1% Y/Y	▲	7.0% Y/Y
Fri 5/20	EA Consumer Confidence (Advance Est.)	May			-22.0
Fri 5/20	U.K. Retail Sales	Apr			-1.4% M/M
Asia Pacific					
Sun 5/15-Thu 5/19	PBOC Policy Rate Decision	May			
Mon 5/16	China Industrial Production	Apr	0.5% Y/Y	▼	5.0% Y/Y
Mon 5/16	China Retail Sales	Apr	-6.2% Y/Y	▼	-3.5% Y/Y
Mon 5/16	China Fixed Asset ex Rural, YTD	Apr	7.0% Y/Y	▼	9.3% Y/Y
Mon 5/16	Japan Producer Price Index	Apr	9.4% Y/Y	▼	9.5% Y/Y
Wed 5/18	Japan GDP, annualized (Prelim. Est.)	1Q22	-1.8% Q/Q	▼	4.6% Q/Q
Fri 5/20	Japan Consumer Price Index	Apr	2.5% Y/Y	▲	1.2% Y/Y

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

U.S.

- We will watch **April retail sales** to gauge how consumers are responding to higher prices for necessities.
- **April and May housing data** should help show to what extent the jump in the 30-year mortgage rate—which has risen to the highest level since 2009—is weighing on demand.

Europe

- The **Russian invasion of Ukraine** and its spillovers remain at the top of the watch list as disruptions in energy and stiffening EU sanctions continue.
- **U.K. inflation** is expected to increase further, keeping pressure on the BoE to raise rates.
- **EA consumer confidence** will show the health of household spending before entering into a slowdown phase.

Asia Pacific

- The **People's Bank of China (PBOC)** will announce the medium-term lending facility rate, with a 5bp cut expected for the 1-year loan prime. Stabilizing growth is authorities' top priority, though rising prices may complicate this.
- **Japan 1Q22 GDP** is likely to contract, given the impact of virus restrictions.

What This Week Means For Markets

The risk-off tone and heightened volatility in markets continued this week. Disruptions in European gas supplies (see page 2) led the euro to depreciate against the U.S. dollar, approaching 2016 lows. Meanwhile, elevated inflation data in the U.S. buoyed stagflation fears and expectations of an aggressive Fed tightening path, leading equities and the U.S. 10-year yield lower. In China, renminbi weakness continues, given more hints of policy easing. Sunac China Holdings—a large property developer—defaulted on its dollar bond amid lockdowns and ongoing property regulation tightening. While COVID cases are easing in Shanghai, restrictions are tightening elsewhere across the country. Given elevated inflation across the globe, tightening monetary policy, and rising risks to growth, we remain with our central Stagflation Shock scenario. Please see our latest Macro Dashboard.

IN REVIEW

European Gas Prices Fluctuating More

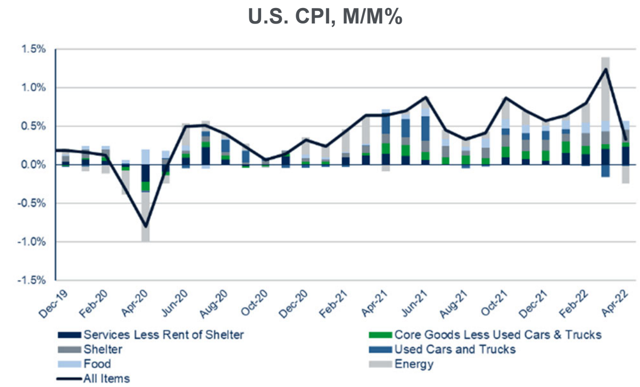
Ukraine this week shut down a Russian natural gas pipeline system, Gas TSO of Ukraine, that carried gas to Western Europe, claiming war actions by separatists controlling the Luhansk region were interfering with the station's operations and that the operator has no control over the station. The company indicated it reported the threats to flow to Gazprom, the Russian gas exporter, but Gazprom did not react. One-third of Russian gas going through Ukraine to Western Europe passes through this station. The immediate effect of the shutdown should not be dramatic; Russia has access to other pipelines and Europe relies on a variety of suppliers. However, this is the first war-related disruption to gas supply and the gas market interpreted it as a vulnerability, as spot gas prices rose 4% at the open of the trade. Analysts say most but not all of the gas can be redirected through other pipelines. Moreover, the gas this pipeline delivers accounts for a small percent of the overall European gas supply, when considering imports and domestic production.

The Kremlin also put sanctions on Gazprom Germania, a set of companies formerly held by Gazprom that were seized by Germany's energy regulator last month, a move that now prohibits Russian entities from selling gas to a number of Gazprom Germania companies. This had an immediate impact on supply and caused European gas prices to jump again. Germany plans to use this event as an initial step away from Russian energy and toward expanding renewable capacity. It remains unclear how this will affect long-term gas availability and prices in Europe, but worries are growing as the conflict escalates.

Sticky Inflation Keeps Pressure on the Fed

U.S. inflation remains elevated and broad-based. Even with headline CPI easing modestly from 8.5% Y/Y to 8.3% Y/Y, core CPI and the Atlanta Fed's sticky price component both edged higher over the month. Together with a tight labor market, the FOMC should remain on track for hikes greater than 25bps at the next several meetings. While there will be another CPI print before the next FOMC meeting, it raises the question of whether a 75bp hike could be back on the table.

April CPI rose 0.3% M/M and 8.3% Y/Y (cons. 0.2% M/M and 8.1% Y/Y). Following the surge in energy prices in March given the war in Ukraine, the energy component fell 0.2% M/M. Excluding energy and food, core CPI was up 0.6% M/M and 6.2% Y/Y. The largest contributors over the month were owners' equivalent rent (OER), airfares, and food at home. Meanwhile, prices for energy, used cars, and apparel eased. Rising services inflation should limit any downward trend in inflation this year.



Source: Bloomberg and Barings calculations. As of May 12, 2022.

Meanwhile, though the April employment report was a mixed bag, overall it shows a labor market that remains tight given that the number of open jobs outpaces the number of unemployed by a record amount. While we may be passing the peak imbalance between the demand for and supply of labor, it could still keep wages elevated in the near-term. These data points are discomforting for the FOMC, which is hoping to reel in inflation, and support our Stagflation Shock scenario, in which high inflation and an aggressive tightening cycle weigh on growth.

Q1 Earnings Show a Solid Beat, But Concerns Ahead

With over 90% of the S&P 500 having reported, 1Q22 earnings growth is tracking 9.2% Y/Y, better than consensus expectations of 5.2%. Energy and materials led in terms of earnings growth, while financials and consumer discretionary lagged, with markets generally rewarding positive surprises, though that reward has been slightly smaller than average. Looking ahead, however, corporate guidance has suggested sentiment has plummeted amid concerns on weak demand, possibly pointing to downside earnings risks in the coming quarters. Inflation also remains a concern among management teams given its impact on margins, despite consensus expecting record margins through Q3. There are also signs the labor-constrained environment is easing, with most companies citing better labor market conditions; Amazon in particular noted it is quickly transitioning from being understaffed to overstaffed, resulting in lower productivity. While high growth has allowed companies to protect margins against rising inflation so far, risks are increasing as growth slows. See our analysis on which sectors are better situated in different inflation-growth environments.

KEY FINANCIAL INDICATORS

Rates	Yield	1W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
Fed Funds	1.00%	50 bps	50 bps	75 bps	75 bps	75 bps	75 bps
U.S. SOFR	0.78%	48 bps	48 bps	73 bps	73 bps	77 bps	73 bps
3 Month USD Libor	1.42%	2 bps	40 bps	92 bps	127 bps	126 bps	121 bps
3 Month Euribor	-0.41%	1 bps	2 bps	11 bps	15 bps	12 bps	16 bps
3 Month U.S. T-Bill	0.90%	1 bps	19 bps	54 bps	85 bps	89 bps	85 bps
2-Year U.S. Treasury	2.64%	2 bps	15 bps	112 bps	213 bps	249 bps	191 bps
10-Year U.S. Treasury	2.91%	0 bps	14 bps	97 bps	136 bps	130 bps	140 bps
10-Year German Bund	1.05%	4 bps	25 bps	78 bps	128 bps	122 bps	123 bps
10-Year U.K. Gilt	1.89%	-12 bps	7 bps	39 bps	97 bps	107 bps	93 bps
10-Year JGB	0.25%	2 bps	1 bps	2 bps	18 bps	17 bps	18 bps
Fixed Income	**Yield**	**OAS**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
Barclays Capital U.S. Government-Treasury	2.87%	N/A	0.0%	-0.9%	-5.6%	-7.3%	-8.5%
Barclays Capital U.S. TIPS	3.09%	N/A	-0.9%	-1.5%	-2.7%	-1.4%	-6.2%
Barclays Capital U.S. Aggregate	3.47%	50	-0.1%	-1.3%	-6.3%	-8.4%	-9.5%
Barclays Capital Global Aggregate	2.60%	50	-0.5%	-3.4%	-9.2%	-13.7%	-11.9%
Barclays Capital U.S. ABS	3.28%	64	0.2%	0.1%	-2.1%	-3.7%	-3.3%
Barclays Capital U.S. MBS	3.57%	39	0.1%	-0.9%	-5.5%	-8.3%	-8.1%
Barclays Capital U.S. Corporate Investment Grade	4.34%	139	-0.3%	-2.5%	-8.4%	-10.5%	-12.9%
BAML Euro Corporate Investment Grade	2.24%	166	-0.5%	-2.8%	-5.9%	-8.9%	-8.7%
Barclays Capital U.S. Corporate High Yield	7.51%	441	-1.9%	-3.5%	-6.3%	-7.3%	-10.1%
BAML European Currency High Yield Non-Financial	5.89%	514	-1.0%	-4.3%	-6.4%	-7.9%	-8.9%
CS U.S. Leveraged Loans	8.20%	521	-1.3%	-1.9%	-2.0%	1.1%	-1.5%
JPM CEMBI Broad Diversified	6.44%	350	-0.7%	-2.6%	-9.7%	-11.0%	-11.7%
JPM EMBI Global Diversified	7.70%	471	-1.5%	-5.6%	-13.8%	-16.6%	-16.7%
JPM GBI-EM Global Diversified	7.06%	N/A	-2.0%	-6.7%	-15.4%	-19.3%	-14.1%
Equities	**Price**	**Div Yield**	**1W Return**	**1M Return**	**3M Return**	**12M Return**	**YTD Return**
S&P 500	3,935.18	1.51%	-8.5%	-10.7%	-10.6%	-3.9%	-17.0%
Euro STOXX 600 (Local)	427.59	2.40%	-3.1%	-6.7%	-8.9%	-2.1%	-12.3%
U.K. FTSE 100 (Local)	7,347.66	3.47%	-1.9%	-3.6%	-4.1%	5.8%	-0.5%
Japan Nikkei 225 (Local)	26,213.64	2.08%	-2.3%	-2.3%	-5.4%	-8.4%	-9.0%
China Shanghai Composite (Local)	3,058.70	2.34%	0.4%	-3.4%	-11.7%	-11.1%	-16.0%
MSCI AC World (Local)	619.54	2.17%	-6.8%	-10.3%	-12.7%	-5.5%	-15.1%
MSCI Emerging Markets (Local)	1,011.22	2.87%	-4.4%	-7.9%	-14.5%	-17.2%	-14.1%
Commodities/Currencies	**Price**	**1W Change**	**1M Change**	**3M Change**	**6M Change**	**12M Change**	**YTD Change**
S&P GS Commodity Index	745.66	-3.3%	5.5%	16.0%	28.0%	42.2%	32.9%
WTI Crude ($/bbl)	105.71	-2.0%	12.2%	13.5%	29.8%	61.9%	40.3%
Copper ($/lb)	4.21	-2.7%	-9.0%	-6.5%	-4.4%	-11.8%	-5.4%
Gold ($/oz)	1,851.95	-0.6%	-5.1%	1.1%	-0.3%	1.2%	2.6%
U.S. Dollar Index	103.85	1.2%	3.9%	8.1%	9.1%	15.2%	8.2%
Euro (USD/EUR)	1.05	0.0%	-3.2%	-7.5%	-8.1%	-13.3%	-7.3%
British Pound (USD/GBP)	1.23	-1.3%	-5.4%	-9.3%	-7.8%	-12.8%	-8.9%
Japanese Yen (Yen/USD)	130.29	0.2%	3.8%	12.4%	14.3%	20.1%	13.1%
Chinese Yuan (CNY/USD)	6.73	2.1%	5.6%	5.8%	5.1%	4.7%	5.6%

Source: FactSet and Bloomberg. As of May 12, 2022.

IMPORTANT INFORMATION

Any forecasts in this document are based upon Barings opinion of the market at the date of preparation and are subject to change without notice, dependent upon many factors. Any prediction, projection or forecast is not necessarily indicative of the future or likely performance. Investment involves risk. The value of any investments and any income generated may go down as well as up and is not guaranteed. Past performance is no indication of current or future performance. PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS. Any investment results, portfolio compositions and or examples set forth in this document are provided for illustrative purposes only and are not indicative of any future investment results, future portfolio composition or investments. The composition, size of, and risks associated with an investment may differ substantially from any examples set forth in this document. No representation is made that an investment will be profitable or will not incur losses. Where appropriate, changes in the currency exchange rates may affect the value of investments. Prospective investors should read the offering documents, if applicable, for the details and specific risk factors of any Fund/Strategy discussed in this document. For Professional Investors/Institutional Investors only. This document should not be distributed to or relied on by Retail/Individual Investors. Barings LLC, Barings Securities LLC, Barings (U.K.) Limited, Barings Global Advisers Limited, Barings Australia Pty Ltd, Barings Japan Limited, Baring Asset Management Limited, Baring International Investment Limited, Baring Fund Managers Limited, Baring International Fund Managers (Ireland) Limited, Baring Asset Management (Asia) Limited, Baring SICE (Taiwan) Limited, BaringAsset Management Switzerland Sàrl, and Baring Asset Management Korea Limited each are affiliated financial service companies owned by Barings LLC (each, individually, an "Affiliate"), together known as "Barings." Some Affiliates may act as an introducer or distributor of the products and services of some others and may be paid a fee for doing so.

NO OFFER: The document is for informational purposes only and is not an offer or solicitation for the purchase or sale of any financial instrument or service in any jurisdiction. The material herein was prepared without any consideration of the investment objectives, financial situation or particular needs of anyone who may receive it. This document is not, and must not be treated as, investment advice, an investment recommendation, investment research, or a recommendation about the suitability or appropriateness of any security, commodity, investment, or particular investment strategy, and must not be construed as a projection or prediction. In making an investment decision, prospective investors must rely on their own examination of the merits and risks involved and before making any investment decision, it is recommended that prospective investors seek independent investment, legal, tax, accounting or other professional advice as appropriate. Unless otherwise mentioned, the views contained in this document are those of Barings. These views are made in good faith in relation to the facts known at the time of preparation and are subject to change without notice. Individual portfolio management teams may hold different views than the views expressed herein and may make different investment decisions for different clients. Parts of this document may be based on information received from sources we believe to be reliable. Although every effort is taken to ensure that the information contained in this document is accurate, Barings makes no representation or warranty, express or implied, regarding the accuracy, completeness or adequacy of the information.

OTHER RESTRICTIONS: The distribution of this document is restricted by law. No action has been or will be taken by Barings to permit the possession or distribution of the document in any jurisdiction, where action for that purpose may be required. Accordingly, the document may not be used in any jurisdiction except under circumstances that will result in compliance with all applicable laws and regulations. Any service, security, investment or product outlined in this document may not be suitable for a prospective investor or available in their jurisdiction.

22-2199523