Outlook for January 2020

World Economy

United States

- Signs of easing trade tensions between the U.S. and China may spur business spending, which has been lagging.
- The consumer should continue to benefit from job and wage growth in the new year. Productivity gains are vital to sustaining this record expansion.
- The housing sector should help fuel GDP in 2020, given lower mortgage rates, greater affordability, and a better match between builder supply and consumer demand.

Developed Markets

- Fiscal stimulus measures are needed to push continental Europe towards its long-term growth potential. While Germany's reluctance to incur budget deficits may restrain the recovery, a potential trade war between the U.S. and Europe is of greater concern.
- The new conservative-led U.K. government is likely to enact expansionary fiscal initiatives and provide more certainty about the economic implications of leaving the European Union.
- Reduced trade tensions between the U.S. and China should help Asian economies, especially Japan. Increased exports could blunt the negative effects of the country's higher value-added tax.

Emerging Markets

- While government policy intervention has helped control China's economic slowdown, these initiatives may be causing oversupply in certain sectors. More investment by private-owned enterprises, as opposed to state-owned, is needed to boost labor productivity and domestic consumer spending.

Monetary Policy & Currencies

United States

- The Fed is expected to keep rates steady for all of 2020. More importantly, the central bank will refrain from tightening until there is substantial inflationary risk. Given the Fed's stance, monetary policy should not be a growth headwind this year.
- The dollar should settle into a tight trading range against other developed market currencies in 2020. However, some depreciation against emerging market currencies could occur due to reduced trade tensions and increasing global growth.

Developed Markets

- The European Central Bank should remain accommodative. But before making further cuts, it will explore any unintended consequences of negative rates.
- Even though the Bank of England will have a new governor in 2020, the country's monetary policy will still depend primarily on the impact of Brexit. As the year progresses, the bank may shift towards tightening, given the expected fiscal stimulus.
- The Bank of Japan would prefer not to reduce rates further because of the enormity of its asset purchase program. However, future rate cuts can't be ruled out due to the uncertain impact of fiscal-tightening initiatives.

Emerging Markets

- Fed ease has given the Peoples Bank of China more breathing room to ease further without provoking unwanted currency depreciation and capital outflow.

Outlook for January 2020

Bond Markets

United States

- Expectations for 2% economic growth in 2020 have helped resolve the yield curve inversion. They should also push intermediate to long-term yields higher, steepening the curve.
- The interest rate spreads on high-yield bonds are at levels that provide more than fair value for the risk incurred. Default pressure, outside of the energy space, remains low.
- Municipal bonds should benefit from favorable supply/demand dynamics and outperform their taxable counterparts in a rising rate environment.

Developed Markets

- Negative yields on the intermediate portion of various global yield curves should dissipate over the year, making developed market international bonds particularly vulnerable to price depreciation.

Emerging Markets

- As global growth improves and the risk of significant currency depreciation against the dollar declines, local-currency debt may offer more value than dollar-denominated emerging market bonds.

Equity Markets

United States

- After a stellar performance in 2019, equity returns should be more muted, but comfortably positive in 2020. Earnings growth should accelerate slightly, and price/earnings ratios mildly expand, as cash and fixed-income returns remain historically low.

Developed Markets

- Even though slower growth is expected in Europe than the U.S., the global scope of revenues of large European companies should help close the valuation gap between U.S. and international equities.
- Easing trade tensions may provide a significant tailwind to Japanese equities, where the market has considerable exposure to export-sensitive and cyclical industries. The recent consumption tax increase may hinder smaller and more domestically oriented companies.

Emerging Markets

- Reduced trade tensions, a strong Chinese economy, and rising commodity prices could spur emerging market equities. While this sector has started to outperform developed market equities, the valuation gap is still significant.

Commodities

Oil

- Oil prices benefitted from the impact the U.S.-China phase one trade agreement should have on global demand. Better than expected Q4 economic growth here and abroad pushed oil demand higher, while major producers showed continued supply resolve at the recent OPEC meeting. U.S. shale producers remain the biggest wild card as they have the ability, and apparent willingness, to flood the market when prices rise to certain levels.

Gold

- Fed ease and uncertainty over the outcome of the trade conflicts drove gold prices higher through much of 2019. Look for gold to decline from current levels now that these catalysts have subsided, and there's scant inflationary pressure.

Industrial Metals

- Copper is leading industrial metals prices higher, a sign that the global economy may be experiencing a cyclical rebound. Chinese and European economic growth could be robust enough to propel prices higher in the first quarter.

Important Information

Benjamin Pace
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Ben Pace is the Chief Investment Officer and a Partner in the New York office. He leads the firm's Investment Committee and is a member of the Executive Committee. He has more than thirty years of experience in investment management. Ben has been featured in the Wall Street Journal and Reuters, and is a frequent commentator on Bloomberg TV and radio, Fox TV and CNBC, appearing regularly on network programs such as Power Lunch, The Closing Bell, Squawk Box, and Worldwide Exchange.