Outlook for February 2020

Key Market Drivers

Uncertainty Around the Coronavirus' Impact

The virus is a prime example of an "unknown" that can roil markets because of its uncertainty and the difficulty in analyzing the economic impact. China's economy and tourism industry will be the most affected in the near term, while the impact on global supply chains remains to be seen. Conservative estimates are calling for a 2.0% decline in China's first-quarter GDP. Historically, countries affected by a natural disaster or epidemic tend to recoup lost GDP growth in subsequent quarters when the economies return to normal. We are hopeful this will be the case with this disaster.

Slow Global Growth

The U.S. economy is expected to be reasonably strong this year. Continued capital spending on intellectual property and research & development should drive enhanced productivity and keep overall GDP near its current 2.0%-2.2% rate for all of 2020. Overseas, Europe remains mired in roughly 1.0% economic growth, although there are signs it may be bottoming. Easing U.S.-China relations and a Brexit resolution should spur growth in the region. However, these countries will likely need to expand their fiscal policies to lift their economies back to their potential growth rates. The increased consumption tax continues to weigh down Japan's economic growth. It could get a much-needed boost from the manufacturing sector now that global trade tensions have subsided. That said, a weaker yen and containment of the coronavirus would be necessary conditions for any improvement.

Our Perspective

Equity Markets

- A slight acceleration in earnings growth and low interest rates may fuel valuation expansion in U.S. markets and drive equity prices moderately higher.
- Despite slow growth in the Eurozone, the global nature of European businesses should allow equity prices to match U.S. returns.
- Japan's proximity to China and its spreading health risks is a headwind for equity markets. Japanese stocks should ultimately benefit from the trade détente and weakening currency.
- Successful containment of the coronavirus could present a buying opportunity in China and other emerging markets, which have seen a recent pullback.

Bond Markets

- The U.S. yield curve has flattened due to concerns about the virus. The positive economic outlook and the Fed's bias for monetary easing should prevent intermediate and longer-term rates from falling much further.
- Interest-rate spreads for high-yield bonds remain tight, and prices are relatively expensive. Low default rate expectations should prevent any downward price pressure. Municipal bonds should benefit from favorable supply/demand dynamics and outperform their taxable counterparts in the higher rate environment we're expecting this year.
- Negative interest rates and exhausted asset purchase programs have left bonds in developed markets vulnerable should rates increase even slightly.
- Relatively high-yielding emerging markets bonds could see some price appreciation thanks to mitigated trade risk, continued global growth, and a flat dollar. The degree of upward movement may be limited until the virus is contained.

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Our Perspective (Continued)	
Commodities	• Oil prices have suffered recently from the negative impact the coronavirus will likely have on China's energy demand. We expect OPEC and Russia to discuss and probably implement further supply cuts over the coming weeks in an effort to stabilize prices. • Gold has benefited from the growing global health scare. Additional upward pressure has come from the flat to slightly inverted U.S. yield curve and the Fed's dovish leanings. If the coronavirus is contained and interest rates hold steady, look for gold to give up most of its year-to-date gains. • Questions around Chinese demand have hurt many industrial metals prices over the last month. As these fears dissipate, reduced trade frictions and still relatively strong Chinese economic growth should allow prices to recover.
Monetary Policies/ Currencies	• The Fed appears content with its current policy but could cut rates 0.25% (25 basis points) if the economy slows too much in the first quarter. As of right now, we don't expect any interest rate changes in 2020. A dovish Fed should also constrain any notable advance in the U.S. dollar, which saw a recent spike due to the virus outbreak. Look for the dollar to settle into a tight trading range against other developed-market currencies. • The European Central Bank will maintain its negative interest rate and asset purchase programs through year-end. Inflation remains below the bank's 2% target. The chairwoman has called on governments to adopt fiscal policies that complement the accommodative monetary policy. • Fiscal policy expansion in Japan should keep the central bank on hold as it assesses both the effectiveness of this policy initiative and the impact of the consumption tax increase. • The Peoples Bank of China stands ready to inject needed liquidity into the economy to help the country weather the near-term impact of the coronavirus. Longer-term, the central bank has room to move rates lower to better control the magnitude of the economic slowdown.

What This Means for Investors

Expect heightened market volatility over the coming weeks until we receive better indications of the spread of the coronavirus and its impact on the global economy. Reduced global trade frictions and near potential US economic and corporate earnings growth should return as the prevailing narratives driving global markets. During periods of extreme price fluctuations, it's important to focus on your long-term goals. For more insights, contact a Cerity Partners advisor or visit ceritypartners.com.

Important Information

Benjamin Pace
Chief Investment Officer

Ben Pace is the Chief Investment Officer and a member of the Investment Committee. Prior to joining Cerity Partners, Benjamin Pace was Chief Investment Officer, and Head of Global Investment Solutions for Deutsche Bank Private Wealth Management in the U.S. Ben has more than 25 years of experience in investment management. Prior to joining Deutsche Bank in 1994, he managed equity income funds for two investment organizations.