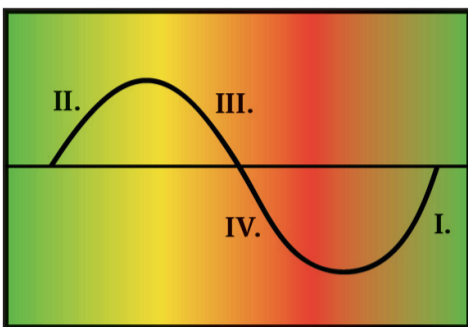


Month in Review

The S&P 500 ended January -0.2% giving up all of its gains in a month-end selloff over concerns that the deadly coronavirus would dampen global growth. Meanwhile, global liquidity has gone through the roof and business activity can be expected to follow. It's time to check our indicators to see how these conflicting forces have affected them. I have also provided a brief summary of my thoughts on the market going forward.

I. CREDIT CYCLE

PHASE II: EXPANSION



Credit conditions remain favorable but credit spreads have widened as the threat of a shutdown in China has spurred a flight to quality out of riskier bonds and into the safe haven of US Treasuries. The credit markets have been pricing in a strong rebound in global manufacturing but the epidemic has called that into question. The weight of the evidence still points to improving global growth, but it is more difficult to make that call until the full extent of the public health crisis is known.

II. RISK LEVEL INDICATORS



US STOCKS: GUARDED

The Risk Level for **US Stocks** is **GUARDED**. The combination of overbought markets and a potential “demand shock” emanating from China is a toxic brew. The OECD Leading Indicators for China, Europe and the US are all moving up which is positive for the stock market. However, the data does not reflect the impact from the Wuhan virus so it is less dependable. The short-term Swing Indicators are negative as well so we remain cautious.

INTERNATIONAL STOCKS: GUARDED

What a difference a month makes! As the New Year began, the world appeared to be entering a new cycle of synchronized global growth, and assets that traditionally benefit at this stage such as emerging markets and commodities had begun to outperform. Then the viral outbreak hit, forcing China to take measures that will have a severe effect on its economy. In response, the Risk Level for **International Stocks** has risen to **GUARDED** reflecting the high level uncertainty surrounding the situation.

US HIGH QUALITY FIXED INCOME: LOW

As noted earlier, high-quality bonds have benefited from a flight to quality and the Risk Level for **US Fixed income Quality** has dropped to **LOW**. Investors have rotated back to bonds as inflation expectations have fallen with oil prices and recession fears have resurfaced with the shuttering of the world’s second-largest economy. Once again, events abroad have conspired to keep inflation and interest rates low and money flowing freely from the Fed, all of which supports the bond market.

III. LOOKING AHEAD

Don’t Worry, Be Happy!

The fundamentals around the globe are turning up after a slowdown in 2019. Economic surprise indices are rising not only in the US but also in the Eurozone and even in the emerging markets. Global leading indicators and manufacturing purchasing managers’ indices are pointing to improving global growth. The earnings growth rate for companies in the MSCI World Index has started to rebound. Before the coronavirus scare, the stock, bond and commodity markets were all in sync and their message was “Don’t worry, be happy”. Since the scare, however, the markets are giving mixed messages with bonds and commodities warning of a potentially serious shock to the system while stocks go merrily on their way. Stocks have the wind at their back, but with oil prices and inflation expectations taking a hit it makes sense to hedge with bonds.

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