Market Review

3 February 2020

Review of markets over January 2020

After a stellar 2019, risk markets began the new decade in a good mood, before volatility picked up towards the end of the month. Concerns over the coronavirus outbreak checked the stock market optimism that followed the signing of a phase one trade deal between the US and China. Markets were less perturbed by the brief flare-up in tensions between the US and Iran, which de-escalated swiftly. Economic data across regions continued to show signs of improvement and, with major central banks set to remain accommodative in the coming year, near-term recession fears appear to be subsiding.

With the turn in sentiment, safe havens performed well in January. The US dollar and Japanese yen both appreciated and government bonds outperformed equity markets – US Treasuries and euro government bonds returned 2.4% and 2.5% respectively. In a month where equities were down, the S&P 500 continued its leadership of major stock markets and was flat over the month. Emerging market equities were most affected by the coronavirus outbreak and fell 4.7%.

Exhibit 1: Asset class and style returns

2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Jan 2020
MSCI EM 79.0%	Small cap 26.6%	Global Agg 5.6%	Global REITS 23.0%	Small cap 32.9%	Global REITS 22.9%	Growth 3.5%	Small cap 13.3%	MSCI EM 37.8%	Global Agg -1.2%	Growth 34.1%	Growth 1.7%
Small cap 44.8%	Global REITS 22.8%	Global REITS 2.3%	MSCI EM 18.6%	Value 27.5%	Growth 6.6%	Global REITS 0.6%	Value 13.2%	Growth 28.5%	Global REITS -4.9%	DM Equities 28.4%	Global Agg 1.3%
Growth 33.9%	MSCI EM 19.2%	Value -4.9%	Small cap 18.1%	DM Equities 27.4%	DM Equities 5.5%	Small cap 0.1%	Cmdty 11.8%	Small cap 23.2%	Growth -6.4%	Small cap 26.8%	Global REITs 0.8%
Global REITS 32.6%	Cmdty 16.8%	DM Equities -5.0%	Growth 16.6%	Growth 27.2%	Value 4.4%	DM Equities -0.3%	MSCI EM 11.6%	DM Equities 23.1%	DM Equities -8.2%	Global REITS 24.4%	DM Equities -0.6%
DM Equities 30.8%	Growth 14.9%	Growth -5.1%	DM Equities 16.5%	Global REITS 2.3%	Small cap 2.3%	Global Agg -3.2%	DM Equities 8.2%	Value 18.0%	Value -10.1%	Value 22.7%	Small cap -2.8%
Value 27.7%	DM Equities 12.3%	Small cap -8.7%	Value 16.4%	MSCI EM -2.3%	Global Agg 0.6%	Value -4.1%	Global REITS 6.5%	Global REITS 8.0%	Cmdty -11.3%	MSCI EM 18.9%	Value -2.9%
Cmdty 18.9%	Value 9.8%	Cmdty -13.3%	Global Agg 4.3%	Global Agg -2.6%	MSCI EM -1.8%	MSCI EM -14.6%	Growth 3.2%	Global Agg 7.4%	Small cap -13.5%	Cmdty 7.7%	MSCI EM -4.7%
Global Agg 6.9%	Global Agg 5.5%	MSCI EM -18.2%	Cmdty -1.1%	Cmdty -9.5%	Cmdty -17.0%	Cmdty -24.7%	Global Agg 2.1%	Cmdty 1.7%	MSCI EM -14.2%	Global Agg 6.8%	Cmdty -7.4%

Source: Bloomberg Barclays, FTSE, MSCI, Refinitiv Datastream, J.P. Morgan Asset Management. DM Equities: MSCI World; REITs: FTSE NAREIT Global Real Estate Investment Trusts; Cmdty: Bloomberg Commodity Index; Global Agg: Barclays Global Aggregate; Growth: MSCI World Growth; Value: MSCI World Value; Small cap: MSCI World Small Cap. All indices are total return in US dollars. Past performance is not a reliable indicator of current and future results. Data as of 31 January 2020.

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Exhibit 2: Fixed income government bond returns

2012	2013	2014	2015	2016	2017	2018	2019	Jan 2020
Italy 20.5%	Spain 11.1%	Spain 15.9%	Italy 4.8%	UK 10.7%	Global 7.5%	Spain 2.5%	Italy 10.6%	UK 3.8%
Spain 5.4%	Italy 7.2%	Italy 15.2%	Spain 1.7%	Spain 4.1%	US 2.3%	Germany 1.9%	Spain 8.3%	Italy 3.2%
Germany 5.0%	Japan 2.1%	UK 14.6%	Japan 1.2%	Germany 3.4%	UK 2.0%	Japan 1.0%	UK 7.1%	US 2.4%
UK 2.9%	Germany -1.7%	Germany 9.0%	US 0.8%	Japan 3.2%	Spain 1.1%	US 0.9%	US 6.9%	Germany 1.9%
US 2.0%	US -2.7%	US 5.1%	UK 0.5%	Global 1.7%	Italy 0.8%	UK 0.5%	Global 5.6%	Spain 1.6%
Global 2.0%	UK -4.2%	Japan 4.5%	Germany 0.4%	US 1.0%	Japan 0.2%	Global -0.7%	Germany 3.1%	Global 1.3%
Japan 1.7%	Global -4.3%	Global -1.0%	Global -3.7%	Italy 0.8%	Germany -1.0%	Italy -1.3%	Japan 1.7%	Japan 0.4%

Source: Bloomberg Barclays, Refinitiv Datatsream, J.P. Morgan Asset Management. All indices are Bloomberg Barclays benchmark government indices. All indices are total return in local currency, except for global, which is in US dollars. Past performance is not a reliable indicator of current and future results. Data as of 31 January 2020.

China

January saw the outbreak of the latest coronavirus, originating in Wuhan, China. At the time of writing, more than 17,000 people have contracted the disease, with 362 confirmed fatalities. In comparison, the SARS outbreak of 2003 infected over 8,000 people, with 774 deaths. Increased travel over the Lunar New Year celebrations is likely to have aided the spread of the disease, and 26 countries outside of China have now reported cases.

As we are still in the early stages of the outbreak, and given the incubation period of up to 14 days (before symptoms present), it is hard to gauge exactly how the situation will develop and the subsequent economic impact. It is likely that this will be a near-term drag on growth in China and its neighbours, as infrastructure networks shut down and more people remain at home. A concerted policy response from the Chinese authorities seems likely, which may assist a recovery in the coming quarters. The prospect of a weaker global economy in the near term and associated weaker demand for oil led to an 11.9% fall in the price of Brent crude oil over the month.

The outbreak comes at a time when economic data suggests that the Chinese economy is stabilising in response to accommodative monetary and fiscal policy. China grew at 6.0% year on year (y/y) in the fourth quarter of 2019. December retail sales continued to grow at 8.0% y/y, while industrial production picked up 0.7 percentage points to 6.9% y/y.

Exhibit 3: Fixed income sector returns

2013	2014	2015	2016	2017	2018	2019	Jan 2020
Euro HY 8.8%	Euro Gov. 13.1%	Euro Gov. 1.6%	US HY 17.5%	EM Debt 9.3%	Euro Gov. 1.0%	EM Debt 14.4%	Euro Gov. 2.5%
US HY 7.4%	EM Debt 5.5%	EM Debt 1.2%	EM Debt 10.2%	Global IG 9.1%	US Treas. 0.9%	US HY 14.4%	US Treas. 2.4%
Euro Gov. 2.2%	Euro HY 5.5%	US Treas. 0.8%	Euro HY 10.1%	Global IL 8.7%	US HY -2.3%	Global IG 11.5%	Global IL 2.2%
Global IG 0.3%	US Treas. 5.1%	Euro HY 0.5%	Global IG 4.3%	US HY 7.5%	Global IG -3.6%	Euro HY 10.7%	EM Debt 1.7%
US Treas. -2.7%	Global IL 3.4%	Global IG -3.6%	Global IL 3.9%	Euro HY 6.1%	Euro HY -3.6%	Global IL 8.0%	Global IG 1.6%
Global IL -3.2%	Global IG 3.1%	US HY -4.6%	Euro Gov. 3.2%	US Treas. 2.3%	Global IL -4.1%	US Treas. 6.9%	US HY 0.0%
EM Debt -6.6%	US HY 2.5%	Global IL -5.0%	US Treas. 1.0%	Euro Gov. 0.2%	EM Debt -4.6%	Euro Gov. 6.8%	Euro HY -0.0%

Source: Bloomberg Barclays, BofA/Merrill Lynch, J.P. Morgan Economic Research, Refinitiv Datastream, J.P. Morgan Asset Management. Global IL: Barclays Global Inflation-Linked; Euro Gov.: Barclays Euro Aggregate Government; US Treas: Barclays US Aggregate Government - Treasury; Global IG: Barclays Global Aggregate - Corporates; US HY: BofA/Merrill Lynch US HY Constrained; Euro HY: BofA/Merrill Lynch Euro Non-Financial HY Constrained; EM Debt: J.P. Morgan EMBIG. All indices are total return in local currency, except for EM and global indices, which are in US dollars. Past performance is not a reliable indicator of current and future results. Data as of 31 January 2020.

US

The signing of a phase one trade deal between the US and China on 15 January was welcome news, representing a thawing in tensions, but it is important to remember that significant tariffs will remain in place and that the structural issues to be tackled in the next phase are not likely to be resolved easily. The agreement means the US will suspend its next planned round of tariffs, as well as cutting the existing tariff rates on around USD 110 billion of Chinese imports from 15% to 7.5%. In exchange, China has committed to boost its imports from the US by around USD 200 billion over the next two years; allow greater access to its markets for financial services companies; enforce intellectual property protections; and be more transparent in its currency management practices.

The key now will be to watch upcoming economic data releases to see whether global businesses feel empowered by the deal to restore investment plans that were postponed in 2019. We do not expect a vigorous bounce back in activity, since ongoing trade concerns, coupled with the uncertainty caused by the presidential election in November, are likely to keep firms hesitant (see our *On the Minds of Investors – How will the 2020 US presidential election affect markets?*).

The US economy grew at an annualised pace of 2.1% in the final quarter of 2019 and broadly remains on solid footing. Manufacturing remains weak, with the December release of the Institute for Supply Management's (ISM) manufacturing survey showing that the sector continues to contract. However, the services side of the economy remains resilient, and the ISM non-manufacturing survey picked up 1.1 points to 55.0 in December. And the consumer, the bedrock of the US economy, is still in good shape, with confidence rising significantly in January.

Growth in jobs (non-farm payrolls) moderated in December. The three-month average pace of job growth now sits at 184,000 per month. This is well above the 100,000 that we would generally regard as concerning however, the number of job openings warrants monitoring since it fell significantly in November.

With the economy evolving broadly in line with the Federal Reserve's outlook of moderate economic growth and a strong labour market, the decision to keep the key interest rate unchanged at the January meeting came as no surprise to markets.

The US earnings season for the fourth quarter of last year is well underway, with companies so far doing better than expected. Earnings per share and sales are growing at 6% and 2% year on year, respectively for the S&P 500.

Exhibit 4: World stock market returns

2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Jan 2020
MSCI EM 79.0%	MSCI Asia ex Japan 19.9%	US S&P 500 2.1%	MSCI Asia ex Japan 22.7%	Japan TOPIX 54.4%	US S&P 500 13.7%	Japan TOPIX 12.1%	UK FTSE All-Share 16.8%	MSCI Asia ex Japan 42.1%	US S&P 500 -4.4%	US S&P 500 31.5%	US S&P 500 -0.0%
MSCI Asia ex Japan 72.5%	MSCI EM 19.2%	UK FTSE All-Share -3.5%	Japan TOPIX 20.9%	US S&P 500 32.4%	Japan TOPIX 10.3%	MSCI Europe ex UK 9.1%	US S&P 500 12.0%	MSCI EM 37.8%	UK FTSE All-Share -9.5%	MSCI Europe ex-UK 27.5%	MSCI Europe ex-UK -1.0%
UK FTSE All-Share 30.1%	US S&P 500 15.1%	MSCI Europe ex UK -12.1%	MSCI Europe ex UK 20.0%	MSCI Europe ex UK 24.2%	MSCI Europe ex UK 7.4%	US S&P 500 1.4%	MSCI EM 11.6%	Japan TOPIX 22.2%	MSCI Europe ex UK -10.6%	UK FTSE All-Share 19.2%	Japan TOPIX -2.1%
MSCI Europe ex UK 29.0%	UK FTSE All-Share 14.5%	Japan TOPIX -17.0%	MSCI EM 18.6%	UK FTSE All-Share 20.8%	MSCI Asia ex Japan 5.1%	UK FTSE All-Share 1.0%	MSCI Asia ex Japan 5.8%	US S&P 500 21.8%	MSCI Asia ex Japan -14.1%	MSCI EM 18.9%	UK FTSE All-Share -3.2%
US S&P 500 26.5%	MSCI Europe ex UK 5.1%	MSCI Asia ex Japan -17.1%	US S&P 500 16.0%	MSCI Asia ex Japan 3.3%	UK FTSE All-Share 1.2%	MSCI Asia ex Japan -8.9%	MSCI Europe ex UK 3.2%	MSCI Europe ex UK 14.5%	MSCI EM -14.2%	MSCI Asia ex-Japan 18.5%	MSCI Asia ex-Japan -4.4%
Japan TOPIX 7.6%	Japan TOPIX 1.0%	MSCI EM -18.2%	UK FTSE All-Share 12.3%	MSCI EM -2.3%	MSCI EM -1.8%	MSCI EM -14.6%	Japan TOPIX 0.3%	UK FTSE All-Share 13.1%	Japan TOPIX -16.0%	Japan TOPIX 18.1%	MSCI EM -4.7%

Source: FTSE, MSCI, Refinitiv Datastream, Standard & Poor's, TOPIX, J.P. Morgan Asset Management. All indices are total return in local currency, except for MSCI Asia ex-Japan and MSCI EM, which are in US dollars. Past performance is not a reliable indicator of current and future results. Data as of 31 January 2020.

Eurozone

Growth in the eurozone remains positive but tepid, at 0.1% in the final quarter of 2019. The consumer remains supported by a healthy labour market – unemployment in the region fell 0.1 percentage point in December to 7.4%.

More encouragingly, the manufacturing side of the economy showed a significant rebound. Should international trade improve on the back of the phase one trade deal, then the manufacturing hubs of Germany and Italy, which both have about a fifth of their employment in manufacturing, stand to benefit.

Christine Lagarde's second meeting in charge of the European Central Bank (ECB) was a low-key affair. Policy rates were left unchanged, but, more significantly, a comprehensive review of monetary policy strategy was announced. The review will include an assessment of the monetary policy toolkit, including its effectiveness and potential side effects, how the ECB approaches price stability, and environmental sustainability. Importantly, we do not believe the review will conclude that negative interest rates should be reversed.

Lagarde also reiterated her call for more fiscal stimulus, in particular to countries more able to borrow than others, saying a good fiscal support would give much more effect to our monetary policy.

UK

The UK officially exited the EU on 31 January 2020. But those hoping that this marks the curtain call for this long Brexit performance will surely be left disappointed. The UK and EU will now need to negotiate a new free trade agreement during the 11 months of transition. As a result, talk and risk of a hard Brexit will persist to some degree, and may intensify by mid-year.

Economic data deteriorated notably ahead of the December election, but there has been some rebound in the subsequent data. Employment grew by 208,000 in the three months to November. The flash purchasing managers' index releases for January, the first major data points since the election, pointed to a sharp improvement in both manufacturing and services, with the composite rising from 49.3 to 52.4.

This was sufficient for the Bank of England to judge that interest rates should be kept on hold. We believe interest rates will be held at 0.75% as the downside risks to global growth fade and the domestic economy is supported by a sizeable fiscal tailwind.

We think that the UK stock market may be poised for a comeback, especially given the attractive yield UK stocks offer in an income-starved world (see our *On the Minds of Investors – Three reasons investors could return to UK stocks post Brexit*).

Conclusion

The outbreak of a coronavirus and a brief flare-up in US-Iranian tensions in January have served as a timely reminder that as well as positioning for the risks on the horizon – the known unknowns – investors also need to prepare their portfolios to be able to weather the unknown unknowns. This is best achieved through a broad approach to portfolio diversification across and within fixed income, equities and alternative assets (see our *Investment outlook 2020* for a more detailed discussion on portfolio construction).

Exhibit 5: Index returns for January 2020 (%)

INDEX	GBP	USD	JPY	EUR	LOC
Equities (MSCI)					
MSCI World Index	-0.1	-0.6	-0.8	0.7	-0.2
MSCI USA	0.7	0.2	-0.1	1.5	0.2
MSCI Europe ex-UK	-1.6	-2.0	-2.3	-0.8	-1.0
MSCI United Kingdom	-3.3	-3.8	-4.0	-2.5	-3.3
MSCI Japan	-0.9	-1.4	-1.6	-0.1	-1.6
MSCI AC Asia ex-JP	-4.0	-4.4	-4.7	-3.2	-3.9
MSCI EM Latin America	-5.1	-5.6	-5.8	-4.4	-1.2
MSCI EM (Emerging Markets)	-4.2	-4.7	-4.9	-3.4	-3.3
Bonds					
Bloomberg Barclays Global Aggregate	1.8	1.3	1.0	2.6	n/a
Bloomberg Barclays US Aggregate	2.4	1.9	1.7	3.2	1.9
Bloomberg Barclays Japan Aggregate	1.2	0.7	0.4	2.0	0.4
Bloomberg Barclays UK Aggregate	3.2	2.7	2.4	4.0	3.2
Bloomberg Barclays Euro Aggregate	1.2	0.7	0.4	2.0	2.0
Currencies					
Sterling	n/a	-0.5	-0.7	0.5	n/a
US dollar	0.5	n/a	-0.3	1.3	n/a
Yen	0.7	0.3	n/a	1.6	n/a
Euro	-0.5	-1.3	-1.5	n/a	n/a

Source: Bloomberg Barclays, MSCI, Refinitiv Datastream, J.P. Morgan Asset Management. Past performance is not a reliable indicator of current and future results. Data as of 31 January 2020.

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