J.P.Morgan

Global Markets Strategy
23 May 2022

The J.P. Morgan View

Buybacks and month-end rebalances to provide support for equities

Cross-asset Strategy: We continue to see favorable China equity risk-reward, and remain OW Value vs. Growth, OW EM regionally, and OW the UK within DM. Consumer spending is likely to show resilience despite the squeeze on purchasing power, due to strong labor markets and wage growth, and an unused savings cushion. With ongoing cyclical concerns and market pricing of Fed hikes close to our forecast, we are N outright US duration and hold 5s/20s flatteners. ECB commentary expressed discomfort with the current monetary policy stance, suggesting front-loading of hikes, but we see a more gradual path relative to market expectations. European credit markets tried and failed to rally, reflecting a market primed to sell into strength. If the ECB has to maintain support for sovereign markets to avoid fragmentation, this could weigh on corporate markets and bank lending. Our EM client survey saw investors increasing cash balances to the highest levels since 2016. We see upside risk to current oil prices given higher summer demand, China reopening, and the potential for outages during the Atlantic hurricane season. We expect US gasoline prices to reach $6/gal by summer on summer demand, a lack of refining capacity, and low inventories.

JPM Clients' View: **Click here to take this week's survey**. This week we poll investors on recession risks, US housing markets and China growth, in addition to our running sentiment questions. Last week's survey results indicated: (1) equity exposure/sentiment among respondents is ~41st percentile on average; (2) 54% plan to increase equity exposure, and 51% to increase bond duration near-term; (3) 58% believe we're in the early stages of retail investors' unwind; (4) respondents would step in to buy, regardless of macro developments, on average if the S&P traded down to ~3500; (5) 82% believe we're in a crypto winter, but most (62%) don't believe there's material contagion between crypto & equities.

Disconnect in recession pricing from markets and economic indicators: While a slowdown seems clear, it remains an unsettled question whether we're headed for a mid-cycle slowdown or recession. Markets are increasingly pricing the latter, implying a much higher recession probability than economic data. There are currently great opportunities in segments such as Energy, small caps, high beta/cyclicals and EM, many of which trade at record valuation discounts. Even for the broad market, levels may be close to bottoming given positioning, flows and sentiment, with month-end rebalances providing support over the next week and buyback executions running at 3-4x higher than trend.

New Trades: Turned neutral on 2s/10s German curve, tactically UW €-supra, entered long 10Y Austria vs. France, entered Jun22/Aug22 MPC OIS curve flatteners (Bassi); took profit on US 5Y5Y inflation swaps shorts (White); add OW in PLN and 1x2 USDZAR put spread (Christovova); turned tactically N on JPY, added long CHF and added EUR-Scandi ratio put spreads (Meggyesi).

Upcoming catalysts: Fed speak & WEF in Davos (all week); flash PMIs (5/24); Powell speaks & BI (5/24); FOMC minutes, Lagarde speaks & RBNZ (5/25), CBRT (5/26).

Global Markets Strategy

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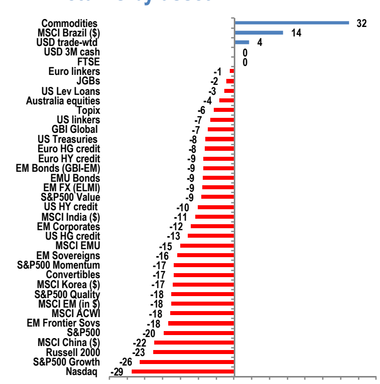
YTD returns by asset



Source: J.P.Morgan

Cross-Asset Strategy

Macroeconomic Outlook

The global expansion has displayed impressive resiliency. This message was underscored in last week's data but also in our US nowcast revision index, which has taken a notable step higher over the past month, and our nowcaster, which is tracking 4.2%ar 2Q22 GDP growth. That said, downside growth risks are building. Our model-based US 12M ahead recession probability has moved up to 25%. The model is picking up the tightening in US monetary conditions, a deterioration in US housing indicators, and a sharp drop in consumer confidence. Notably, it does not embed the potential reverberations from a contraction in China and the upward pressure on food and energy prices.

China contraction to spill over to global manufacturing weakness. In the near term, we expect downward pressure on global growth to be concentrated in manufacturing as a contraction in China demand and additional supply-chain problems spill over to the rest of the world. A 1pt drop in this week's DM flash manufacturing output PMI in May should confirm this downshift is underway. Higher inflation and tighter financial conditions also prompted downward revisions to our US GDP forecast and heighten risks of a broader downgrade to our global growth forecast.

As manufacturing slides, the services sector looks to be lifting. We expect the global expansion will pass the current resiliency test. In this regard, an important offset to weaker manufacturing should come from the interaction of reopening dynamics in services (outside China) and pent-up demand for labor (*GDW*, May 20th).

Equities

Reiterating more supportive China risk-reward; the consumer backdrop. In terms of positioning, our core view remains to be OW Value vs. Growth from a style and sector perspective, OW EM regionally, and OW the UK within DM. Historically one didn't see China missing its growth target, and given that most expect a miss anyway, the chance of a positive surprise is now much higher. In the least, China policymakers are likely to wheel out more and more stimulus, which will act to improve China risk-reward in 2H22. Discussions over stimulus policies gained momentum onshore last week, including proposals for: 1) special central government bonds in the low trillion RMB range, 2) consumption coupons to households, and 3) rural auto subsidy plan. Thematically, the consumer is seen by most to be in the eye of the storm, hurt by the dramatic purchasing power squeeze, which is expected to lead to a retrenchment phase. However, we believe a spending downturn isn't inevitable, unless labor markets deteriorate meaningfully. Wage growth is coming through, the cushion of unused savings can be used to smooth consumption, and high-frequency card spending data is resilient so far. A key for consumer fortunes is how the wedge between CPI and wages develops, and these variables could cross in a favorable way over the next 6M. Consumer cyclical plays started the year well, only to surrender the gains; their valuations are now near record lows (*Equity Strategy*, May 23rd).

Saudi & Iraq raise capacity growth on the back of strong oil demand; stay OW Energy. At a recent conference, the oil ministers of Saudi Arabia and Iraq highlighted continued tightness in the oil market, and the importance of maintaining spare capacity in managing price spikes. Saudi and Iraq each plan to raise capacity by ~1mb/d by 2027. In contrast, outside of the GCC, supply growth continues to fall short of expectations: we estimate the total OPEC+ undershoot vs quotas reached 1.8mb/d in April, with the group's spare capacity 'buffer' declining concurrently to just 8%. In our view, this means that, while OPEC+ production is growing in absolute terms, the group's ability to influence price is diminishing. We believe this creates upside risk to current prices, particularly in the context of expected higher summer demand, China reopening, and the potential for outages during the Atlantic hurricane season (*Global Energy Strategy*, May 17th).

We continue to see SMid benefitting from a superior medium- to long-term outlook, while also being less exposed short-term to the volatility brought about by passive funds. We remain OW on Energy, Materials and Leisure (*SMid Alpha*, May 17th).

Bonds

Bonds were mixed last week, amid cross currents from strong inflation and labor market data, and flight-to-quality flows given weakness in risky assets. In the **US**, Fed Chair Powell acknowledged a trade-off between the two sides of its mandate but clearly stated inflation is the priority. With ongoing cyclical concerns, market pricing of Fed hikes not far from our forecast and close to fair valuations, we stay neutral duration outright and hold a bearish proxy via 5s/20s flatteners.

In the **Euro area**, recent ECB commentary suggests an increasing discomfort with the current monetary policy stance. While this justifies a front-loading of hikes, we see a more gradual path relative to market expectations. We keep long 5Y Germany vs. US and stay short 3Mx5Y EUR gamma. We stay short 10y Italy vs. Germany. In the **UK**, we stay long 5Y SONIA vs. USD OIS as we see the recent GBP underperformance as overdone.

In **EM**, an ongoing tightening of financial conditions, concerns over growth, and high volatility remain strong headwinds. We stay UW local market duration, and are UW Malaysia, Thailand, Hungary, Poland, Romania, Chile, and Colombia (*EM Fixed Income Focus*, May 19).

Credit

European credit markets tried and failed to rally last week. In general, we get the sense that the market is now primed to sell into strength. There is a risk that the ECB will have to maintain some support for sovereign markets to prevent fragmentation, which could put even more of the burden on corporate markets and bank lending instead. While this is not a big concern yet, it could become a talking point if inflation keeps beating expectations. Altogether, then, we continue to think it is too early to call the wide in spreads. While we would no longer recommend being outright short or UW, given the cost in foregone carry, we continue to prefer focusing on RV trades rather than directional calls. Our main preferences at the moment are for corporate hybrids over high yield, HY / IG decompression, and OW Financials vs Non-Financials. In High Yield spreads are discounting a worse default outcome than has been realized at any time since 2009. That said, we think a large risk premium is justified and are not tempted to call the wides just yet. Our three major sector themes for 2H22 are: i) OW non-cyclicals; ii) OW commodity producers vs consumers; and iii) UW sectors with large 2022/23 funding needs (*European Credit Weekly*, May 20th).

Our EM client survey shows investors increased cash balances to highest level since 2016. Our May 2022 EM client survey had participation from 232 investors with \$1.4Tr in EM fixed income and currency AUM. Investors retraced last month's reduction in EM sovereign exposure; while cash balances jumped to the highest level since Nov'16; UW rates positioning remained unchanged and investors moved further UW FX. EM retail bond funds had \$11.3bn of outflows since the last survey, surpassing the four-week outflows observed back in March. Nearly 50% of participants think EMBIGD spreads will end tighter between 400-449bps by year-end (*EM Client Survey*, May 19th).

Currencies

The most meaningful change for FX has been a shift from US exceptionalism to a global slowdown that encompasses the US. This does not challenge our bullish dollar stance vs. high beta FX, but it raises questions on whether USD should continue to outperform other reserve currencies. Stay short EUR/USD due to multiple regional vulnerabilities, but tactically trim exposure on JPY. Several central banks—SNB, Riksbank, Norges Bank—have the incentive and the ability to out-deliver the ECB. Conviction remains highest for CHF, reinforced by SNB's Jordan, relative to the Scandi currencies given growth risks.

We remain long USD but reduced overall exposure by turning tactically N on JPY as lower equities have corresponded with lower US yields. Stay core short GBP and add long CHF on SNB signaling preparedness to act. Hold EUR shorts given policy constraints and regional risks; add EUR-Scandi ratio put spreads. Hold strategic NZD shorts ahead of RBNZ**.** We remain UW EM FX (*FXMW*, May 20th).

Commodities

Seasonal natural gas storage injections lift global inventories off historic April lows. China continues destocking. Tradeable commodity inventories (ex-China) increased from historical lows in April, due to a seasonal increase in US natural gas storage, with largely unchanged inventories elsewhere. Despite increasing this month, tradeable commodity stocks remain critically low (~1.1z below average), and the abundance of available inventories in leading commodity consumer and importer China remains sizeable. China currently holds ~80% of global copper, 68% of corn, 49% of wheat, 36% of soybeans, 25% of oil and 24% of aluminum inventories, according to our sources (*Global Commodities*, May 20).

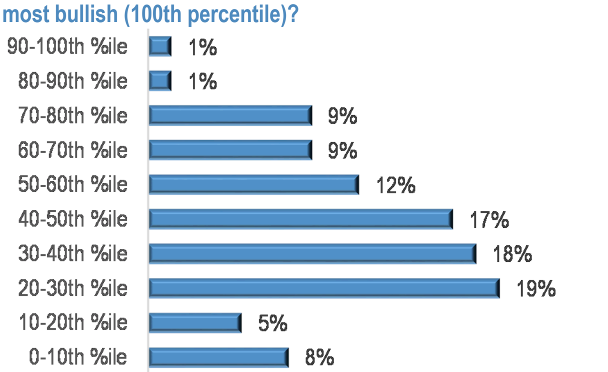
US gasoline prices to break above \$6. The national average US retail gasoline price topped \$4.50 a gallon for the first time last week, up ~50c from a month ago, and a massive jump from \$3.04 per gallon a year ago. With expectations of strong driving demand, US retail price could surge another 37% by August to a \$6.20/gal national average. As peak US summer driving season begins, diesel is taking a back seat to gasoline. Toward the end of April, US diesel prices peaked at a \$1.63/gal premium to US gasoline, the highest diesel premium ever. Over the following two weeks, US gasoline prices climbed to close that gap and today gasoline is trading at a 15 cents per gallon premium to diesel. Typically, refiners produce more gasoline ahead of the summer road-trip season, building up inventories. But this year, since mid-April, US gasoline inventories have fallen counter seasonally and today sit at the lowest seasonal levels since 2019. Gasoline balances on the East Coast have been even tighter, drawing to decade lows (*Global Commodities Oil Flash Note*, May 17th).

JPM Clients' View

Click here to take this week's survey

This week, we poll investors on recession risks, US housing markets and China growth, in addition to our running survey questions on equity positioning/sentiment, and intentions for near-term changes to equity allocation and bond duration. The results from the last survey are shown below[1].

Figure 1: What is your current equity positioning or sentiment in historical terms, expressed from most bearish (0th percentile) to most bullish (100th percentile)?

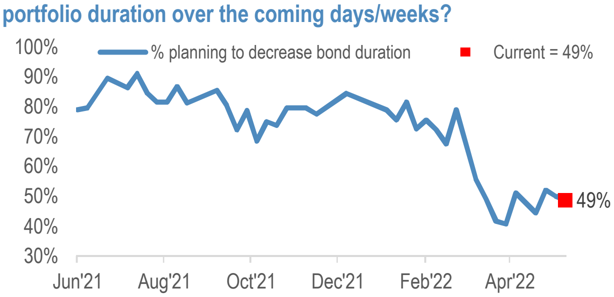


Source: J.P. Morgan.

Figure 2: Are you more likely to increase or decrease equity exposure over the coming days/weeks?

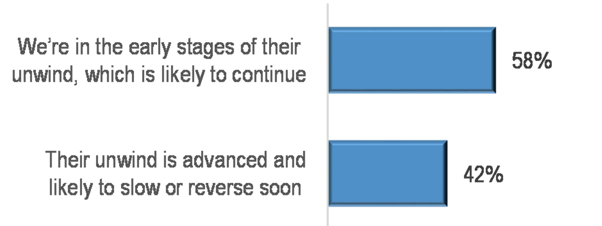
Source: J.P. Morgan.

Figure 3: Are you more likely to increase or decrease bond portfolio duration over the coming days/weeks?



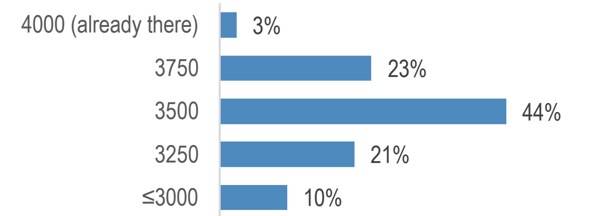
Source: J.P. Morgan.

Figure 4: What is the current state of retail investors?



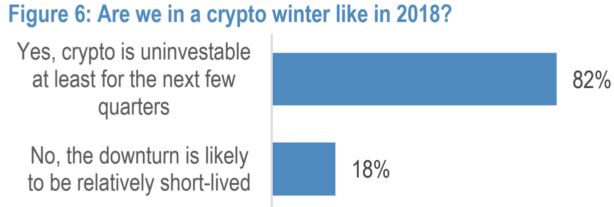
Source: J.P. Morgan.

Figure 5: If we continue to sell off, at what level on the S&P 500 would you step in to buy, regardless of macro developments?



Source: J.P. Morgan.

Figure 6: Are we in a crypto winter like in 2018?



Source: J.P. Morgan.

Figure 7: Do you believe there is material contagion between crypto and equity markets?

Source: J.P. Morgan.

[1] Results are based on 78 responses received from clients in our survey conducted May 16-23rd

Disconnect in recession pricing from markets and economic indicators

Last week, risk markets were down. Equities globally were down (MSCI ACWI -1.7%) and the US was the worst performing region with some notable weak earnings reports on a few bellwether companies. EM was up (+3%) with gains in Asia and Latam. In China, despite bad data earlier in the week an unexpected policy easing announcement helped Chinese stocks (+4.5%). Credit spreads were generally wider (JULI spread +8.5bp) and HY/HG ratios widened. Hawkish rhetoric from central banks remained present with some remarks from Powell but weaker risk markets weighted on the belly of the yield curve. As a result, curves generally flattened last week and 10Y UST yield was down 14bp. In Europe, aggressive selloff on the front-end (2Y Gilts +25p, 2Y Bunds +22bp). Overall Commodities were up last week and the move was led more by metals (Gold +1.9% and Copper +2.8%). The trade-weighted dollar was down (-1.1%). Losses were broad-based as the USD was down across all G10 pairs. High volatility persisted. VIX averaged 28 last week while rates volatility in the US remains at post-GFC highs. The worst start to the year for risk-markets in decades has been accompanied by some intensification of recession, inflation and stagflation fears as the increase in story counts for these terms reveal (Figure 8).

A question that often comes up is at what level to buy the market? We first think this is the wrong question to ask, as there is tremendous dispersion between market capitalization segments, sectors and styles. As such, the better question is 'which segments should I be invested in?' There are currently great opportunities in some market segments such as Energy, small caps, high beta/cyclicals and EM, many of which trade at record valuation discounts, while others still appear expensive and poised to underperform such as bond proxy sectors. **However, even for the broad market, levels may be close to bottoming given positioning, flows and sentiment. In particular, we see record buyback announcements YTD with estimated 3-4x higher than average executions in recent weeks.** S&P 500 companies have announced $429B of buybacks YTD (stronger pace than 2019 and 2021) as companies continue to generate strong cash flow on healthy margins. In the latest sell-off, JPM estimates 3-4x higher buyback executions than trend, which implies the corporate put remains active. Based on 1Q results, buybacks were up 45% y/y and 3% q/q, led by Tech ($62B in 1Q22), Financials ($49B) and Healthcare ($39B). Notably, Energy has significantly ramped buyback activity to $9.5B compared to only ~$500M in 1Q21. In the short term, the buyback trend remains well-supported as more companies come out of blackout (still ~15% within the window). Additionally, investor sentiment remains terrible (e.g. AAII still near post-GFC lows) and we see a supportive environment from investor positioning and flows. On the latter point, we note systematic strategy positioning is in its bottom decile, and month-end rebalances are expected to drive ~1-3% of equity outperformance over the next week as pensions shift allocations from bonds to equities.

The slowdown is obvious now but in our view the important question is to understand if what comes next is a recession or more of a mid-cycle slowdown. More importantly, is the risk-premium built-into markets excessive relative to what comes next?

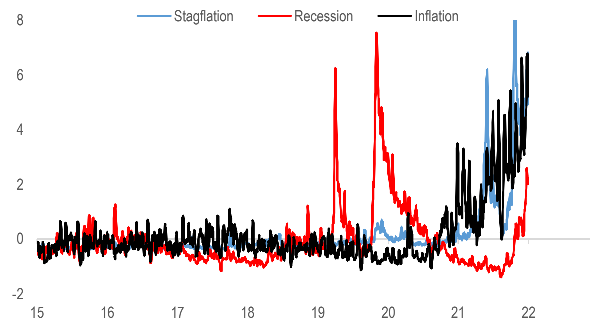
Some indicators are worrisome but healthy fundamentals and a strong incoming dataflow are encouraging. Fundamentals are strong and suggest resilience as private sector balance sheets look healthy and a large reservoir of excess savings are acting as an important cushion for households against a rising CPI basket. We also highlight a few common recession indicators. First, housing starts and building permits have held up well (Figure 9), thanks to robust housing demand paired with stubbornly low inventory. Second, on consumer confidence, while the Michigan survey numbers have never really been strong in this cycle, the reading from the Conference Board (which also includes employment related variables) are still quite elevated (Figure 10). Third, is the message from the labor market. The Sahm recession rule, which has been recently referenced by Dudley at the Fed, signals the start of a recession when the three-month moving average of the national unemployment rate (U3) rises by 0.50 percentage points or more relative to its low during the previous 12 months. Needless to say, we are not there yet (Figure 11). Finally, we look at two versions of our 1Y ahead recession probability model. The first is based on near-term economy indicators while the second relies on medium-term risk indicators (Figure 12). To us, the low probability of recession from the former signals the strength of the incoming dataflow. This message is also echoed by our US nowcaster which is tracking 4.2%ar 2Q22 GDP growth and gives a reason to expect more of a mid-cycle correction or at worst a mild technical recession. The background risk measure is more concerning but usually a worse dataflow is required.

The year-to-date rise in Fed fund rates probably understates the true extent of monetary tightening. This is at least the conclusions we would get by comparing changes in Chicago NFCI with previous normalization episodes (Figure 13). This relates also to the rapid spike we have seen in US mortgage rates so far in 2022, and the risk is that this may start to crack the housing indicators we commented on earlier. We might be already witnessing the early signs of this with a downward trend for home sales and disappointing result in the NAHB survey. What remains to be seen is whether these tighter financial conditions start feeding into the labor market. So far, we saw only a small uptick in Initial Claims. Should the labor market worsen, this could produce the sharp drop-off in confidence one sees ahead of recessions. A second risk relates to Energy prices. Household balance sheets are impacted by the prices of fuels, not wholesale crude prices. Usually the two move in tandem but in recent months we have seen some decoupling. A combination of low inventory levels, low refining capacity, and still-recovering demand drove fuel prices up with crude oil in late February and up further since then, with risks of prices topping $6/gal this summer as we discuss in the Cross-Asset Strategy section above.

That said, market pricing is pessimistic and already includes substantial risk premium. The rolling 12m drawdown on a representative multi-asset portfolio is already below the lows seen in outside of recession in the past 20 years, and this includes mid-cycle slowdowns (Figure 14). Similarly, our recession probability model based solely on financial indicators (e.g. S&P500, credit spreads, and yield curve) now exceeds 41% and is quite above the 15% level implied from near-term economic indicators alone. What's important to bear in mind is that the market is discounting a much higher probability than that implied from economic data, and using financial indicators alone has produced false positives (Figure 15).

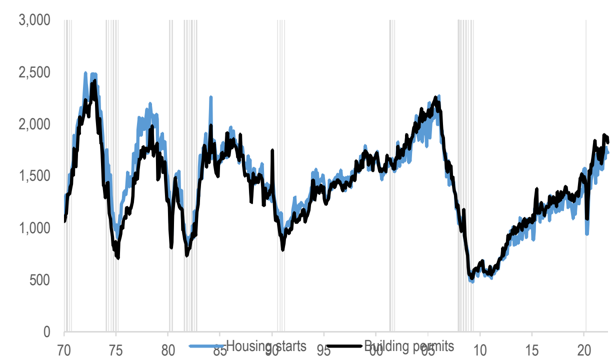
Are Bonds back to be good portfolio hedges? On the positive side, something has changed in recent weeks as bond yields pulled back off the highs. This is the normal function that bonds would offer, acting as a cushion in the event when risk markets correct. But this has not been the story so far in 2022 as monetary normalization has been the main shock hitting the economy, bringing down both Equities and Fixed Income markets. So we have gone from a situation where both stocks and bonds were sold on the back of de-leveraging, to a situation where bonds rallied as stocks fell, nudging stock/bond correlations toward a more normal (negative) levels. We do indeed think this is where things could be gradually heading, but we acknowledge this is not likely to play out in a linear way. As we argued in our May GAA, we remain of the view that the growth/inflation/liquidity regime of the next few quarters still seems to be conducive to higher yields, but the expectation is now that the peak in UST yields might not be much higher than the peak we saw earlier this month (3.2%). Usually bond yields rise during a hiking cycle and often peak 50-75% of the way through. The fact that OIS 2y1m have now stabilized reinforces this sense.

Figure 8: Story count "recession", "inflation" and "stagflation" has intensified



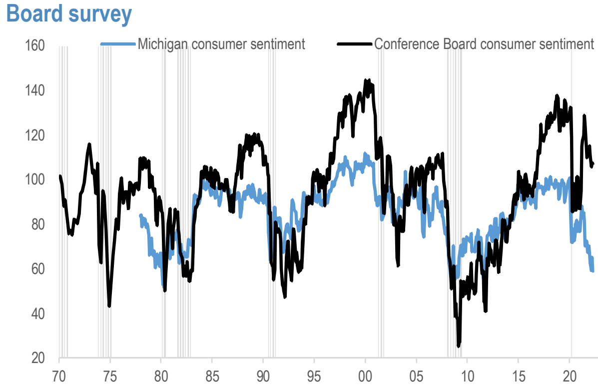
Source: J.P. Morgan.

Figure 9: Housing is holding up well so far



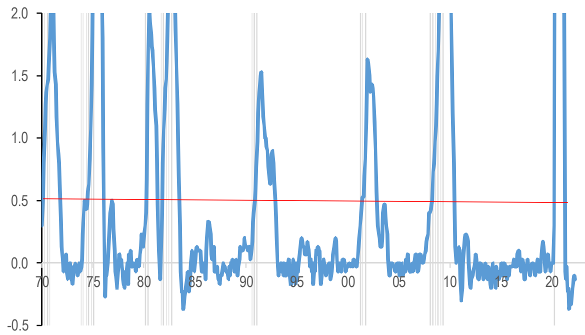
Source: J.P. Morgan.

Figure 10: Consumer confidence is still high on Conference Board survey



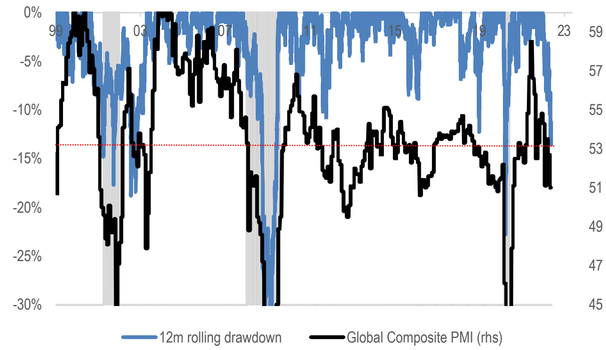
Source: J.P. Morgan.

Figure 11: The Sahm unemployment rule is not signaling the start of a recession



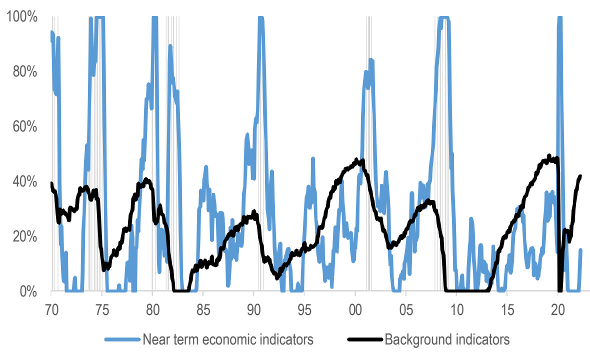
Source: J.P. Morgan

Figure 14: Drawdowns for a multi asset portfolio already exceeds what has been seen in earlier mid-cycle slowdown



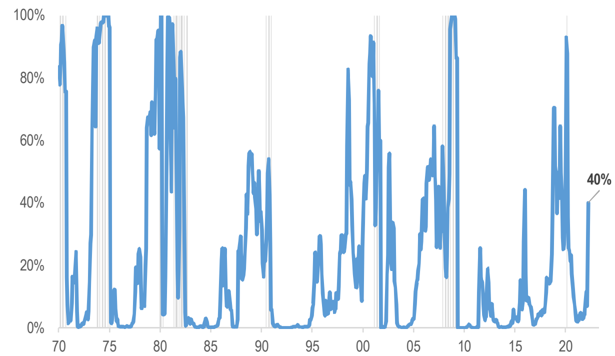
Source: J.P. Morgan.

Figure 12: Probability from near term economic indicators does not confirm message from background indicators



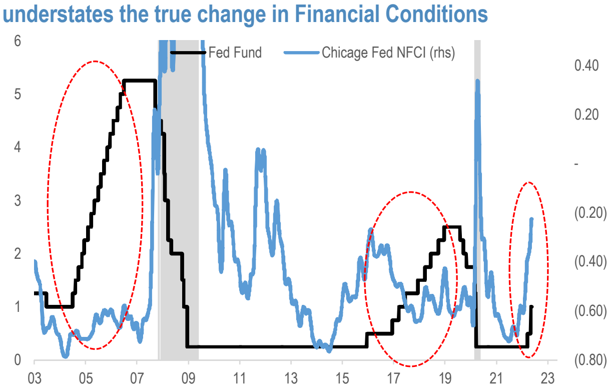
Source: J.P. Morgan.

Figure 15: Recession probability from financial indicators alone is around 40%, with many false positives



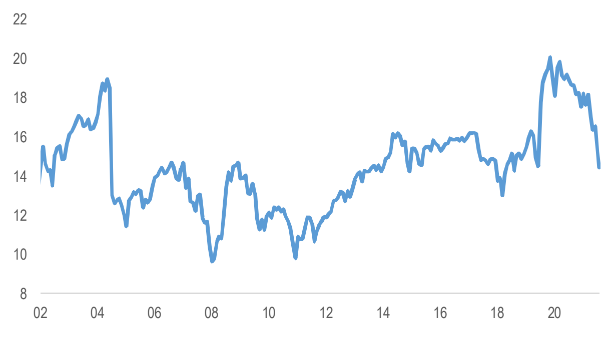
Source: J.P. Morgan.

Figure 13: The change in Fed Fund rates so far this year understates the true change in Financial Conditions



Source: J.P. Morgan.

Figure 16: MSCI ACWI 12m forward P/E



Source: J.P. Morgan.

Global Research Digest

Macro & Cross-Asset Views

Flows & Liquidity: Another rebalancing is approaching, Nikolaos Panigirtzoglou

We estimate the potential equity buying by the end of May due to monthly rebalancing by balanced mutual funds to be between $34bn and $56bn. By quarter-end the potential equity buying due to rebalancing grows by an additional $40bn due to Norges Bank/GPIF/SNB and an additional amount by US defined benefit pension funds with an upper bound of $167bn. Narrow liquidity will keep contracting due to QT but it will likely take some time before the QE stock effect is unwound.

Equity Strategy: Peak Fed hawkishness is starting to get traction; Assessing valuations and the earnings momentum, Mislav Matejka, CFA

The Fed has likely reached the point of peak hawkishness, and this is getting confirmed in bond yields which are lower since the Fed meeting, especially the 2-year, and the yield curve is steeper. We think that the closing of the gap between breakevens and bond yields, that we were advocating, is getting largely done, and that inflation is showing a turn lower, for the first time in a while, suggesting that the Fed might not be seen to be significantly behind the curve anymore. As the Growth part of the equity market has been very weak in the past months, losing 23% vs Value from highs, the potential peak aggressiveness by the Fed should act to support the broader equity indices.

Global Economics and the Recovery from COVID-19

US: Don't fight it—the Fed wants slower growth, Michael Feroli

We have lowered our expectations for growth in 2H22 and 2023 due to tightening in financial conditions that has occurred in recent months, and given that the Fed will do what it takes to make sure growth slows. If growth is on track to exceed our forecast, increasing pressure in the labor market, we think the Fed would respond with additional tightening intended to slow the economy. Moreover, the Fed's response to an economy performing worse than we anticipate is less clear and would likely depend largely on inflation pressures.

Seigniorage: Inflation's gift to the budget, Jahangir Aziz

We assess whether in the current inflation spike, declining seigniorage can be relied upon to provide some relief to strained budgets. High inflation and increased real money balances increased seigniorage revenue to 1.9% of GDP. Based on 2022-23 inflation forecasts, the inflation tax sources would reach on average 2.1% of GDP for LatAm, 1.4% for EM Asia, and 2.2% for EMEA EM. Admittedly, estimates assume real money demand will remain stable, which might not be the case given the ongoing monetary tightening. We thus take a more conservative view that the real monetary base converges to the pre-COVID average by 2023.

Focus: So go asset prices, so goes household wealth, Peter B McCrory

Wealth shock is set to drag on growth in the coming year given that consumer spending typically falls by 2 cents over the course of a year for each dollar drop in financial wealth. We estimate that household wealth in the form of debt, equity and real estate has, on net, fallen by somewhere between $5tn and $8tn since the beginning of the year. The crypto-market drop coupled with a presumptive drop in the value of other non-crypto household assets (excluding debt, equity, and real estate) suggests that total drop in household wealth through 2H22 could be as much as $9tn though we view this more as an upper bound on the loss.

China: An unusual asymmetric LPR cut, Haibin Zhu

The PBOC's unusual decision to keep LPR unchanged can be due to policy aims to provide some cushion against weak housing market activities which could provide meaningful support to free up more disposable income for consumption given recent Omicron outbreak has hurt the labor market. There is room to promote the affordable rental market or public housing market more aggressively this year, to partially offset the weakness (not only cyclical but also structural) in the commodity housing segment.

ECB: The tricky challenge of an anti-fragmentation tool, Greg Fuzesi

If an anti-fragmentation tool is launched by the ECB, we would expect it to have some conditionality via a link to the EU surveillance processes (i.e., NextGenEU and European semester) and we would expect any liquidity injected through its purchases to be sterilized. Purchases could also be restricted to not cover some longer-term bonds. Legally, the ECB could justify targeted asset purchases without explicit conditionality. Further, the ECB may struggle to reach internal agreement on trigger levels for yields and/or spreads, unless they rise abruptly and sharply.

UK: BoE's Pill hawkish, as spending shows resilience, Allan Monks

Following BoE's Chief Economist hawkish sounding speech, we remain confident the MPC will hike 25bps in June and, barring a downside surprise in the data, continue with another hike in August. The timeliest data most relevant for tracking near-term spending are not flagging a recession or unexpected weakness. We remain cautious due to growing external headwinds, but the main risk appears to be that the MPC will need to continue hiking at every meeting this year. This partly reflects increasing evidence of domestic inflation pressures, but also resilience in the activity data to date.

Global Market Implications

Global Commodities Oil Flash Note: Cruel summer: US gasoline prices to break above $6, Natasha Kaneva

With expectations of strong driving demand—traditionally, the US summer driving season starts on Memorial Day, which lands this year on May 30, and lasts until Labor Day in early September—US retail price could surge another 37% by August to a $6.20/gal national average. Since mid-April, US gasoline inventories have fallen counter seasonally and today sit at the lowest seasonal levels since 2019. A major driver in these counter-seasonal draws in gasoline is higher-than-normal exports mostly to Mexico and the rest of Latin America.

Asia Equity Macro Roundtable: The YEN move and its ramifications, Wendy Liu

The EM Asia macro perspective suggests that stronger USD and weaker EM Asia currencies tend to signal weaker exports to the US. The Japan view attributes the structural weakness in the Yen to continued outbound FDI by Japanese corporates since 2013-2014 and limited repatriation of overseas income. Over the 25 years since the AFC, when the Yen weakened by >5% vs the USD, ASEAN equities posted a median US$ 3% loss.

EM Fixed Income Focus: EM fixed income technical support is not as broad as assumed, Jonny Goulden

Ongoing tightening of financial conditions, concerns over growth amidst falling industrial metals prices, and high volatility in risky assets leave us with a still-defensive stance in EM fixed income (UW EM FX and local rates). While EM fixed income faces many challenges, we had considered the lack of inflows into major EMs as an important technical support. There have already been meaningful fund outflows and a clean-up of investor positioning in EM, but there is still some way to go for an eventual cyclical trough in flows.

Frontier Local Markets Guide: We introduce the inaugural edition of the J.P. Morgan Frontier Local Markets Guide, Ayomide O Mejabi & Saad Siddiqui

We cover the local markets of 20 Frontier countries (and regions) in detail, and for each country we provide a background of both monetary and debt management policy, foreign exchange market developments, an overview of the main benchmarks for local bonds, derivatives markets, as well as clearing and settlement issues. We highlight key benchmark instruments and characteristics such as market size, auction conventions, liquidity, transaction costs and tax regimes.

Sector Level Views

Broadlines & Hardlines Retail: Quick Thoughts on What We Learned the Past Two Days, Christopher Horvers, CFA

The drivers of sales softness were mostly weather and share of wallet. Gross margin pressures most acute to those with high imports/discretionary mix that came into 2022 heavy given in-stocks were a premium in 2H21 with our large companies getting more involved with logistics.

Cost of Living: Views from 5,000 consumers, Georgina Johanan, ACA

We asked 5k consumers in the UK, France, Germany, Spain and the US, about their spending plans as the cost of living crisis takes hold. Despite 70% of UK and French respondents saying their homes are now more important to them, the net balance of expected spending on home improvement (vs. pre-pandemic) was negative: UK –16% and France –5%.

China Internet: Stage 2 earlier than forecast: Revisiting short- and long-term fundamental outlook, Alex Yao

In Stage 2 of our three-stage investment model, significant uncertainties facing the sector should begin to abate on the back of recent regulatory announcements. We expect early-cycle sectors such as digital entertainment, local service, and ecommerce to be the first batch of outperformers. Late-cycle verticals such as travel and ads should lag the early-cycle ones by 1-2 quarters. Our sector pecking order is Meituan, NetEase, Tencent, Kuaishou, Alibaba and PDD.

Marko Kolanovic, PhD; Nikolaos Panigirzoglou; Bram Kaplan, CFA; Thomas Salopek; Federico Manicardi; Mika Inkinen; Amy Ho

Strategy & Forecasts

GAA Long Only Model Portfolio

Asset Classes		Active Weights	UW | OW
Equities		12%	
Govt. Bonds		-12%	
Corp. Bonds		-5%	
Commodities		7%	
Cash		-2%	
Sectors		**Active Weights**	**UW | OW**
Equities	US	-3%	
	EMU	-3%	
	Japan	0%	
	UK	1%	
	EM	5%	
	Other	0%	
Govt. Bonds	US Nominal	-2%	
	US TIPs	0%	
	Europe Core	1%	
	Europe Periphery	-1%	
	Japan	2%	
	UK	0%	
	EM Local	0%	
	Australia	0%	
Corp. Bonds	US HG	0%	
	Europe HG	-2%	
	UK HG	0%	
	US HY	2%	
	Europe HY	-1%	
	US Loans	1%	
	EM Sovereigns	2%	
	EM Corporates	-2%	
Commodities	Energy	4%	
	Industrial metals	0%	
	Agriculture	2%	
	Precious metals	-4%	
	Livestock	-2%	

Equity sector recommendations and YTD returns

	US		Europe		Japan		EM	
Energy	48%	OW	30%	OW	32%	N	-23%	OW
Materials	-8%	N	-5%	OW	-3%	N	-11%	OW
Industrials	-16%	N	-18%	OW	-8%	OW	-11%	N
Discretionary	-31%	N	-23%	N	-11%	OW	-25%	OW
Staples	-8%	UW	-9%	UW	-8%	N	-14%	UW
Healthcare	-10%	OW	-3%	UW	-8%	UW	-28%	UW
Financials	-16%	OW	-8%	OW	5%	OW	-7%	OW
Technology	-26%	N	-26%	N	-16%	N	-23%	N
Comm Service	-28%	N	1%	OW	10%	UW	-20%	N
Utilities	0%	UW	0%	N	29%	UW	-3%	UW
Real Estate	-19%	UW	-17%	UW	2%	N	-8%	N
Overall	**-18.8%**		**-9.7%**		**-6.1%**		**-17.1%**	

Source: J. P. Morgan, Bloomberg Finance L.P.

JPM Forecasts

Rates	Current	Jun-22	Sep-22	Dec-22	Mar-23
US (SOFR)	0.79	1.05	1.85	2.45	2.95
10-year yields	2.79	3.05	3.15	3.20	3.25
Euro area (depo)	-0.50	-0.50	0.00	0.25	0.50
10-year yields	0.94	0.85	0.80	0.75	0.80
Italy-Germany 10Y (bp)	206	160	170	180	180
Spain-Germany 10Y (bp)	114	85	90	95	95
United Kingdom (repo)	1.00	1.25	1.50	1.75	2.00
10-year yields	1.89	1.80	1.90	1.95	2.00
Japan (call rate)	-0.10	-0.10	-0.10	-0.10	-0.10
10-year yields	0.24	0.20	0.20	0.20	0.25
EM Local (GBI-EM yield)	6.93			6.52	
Currencies	**Current**	**Jun-22**	**Sep-22**	**Dec-22**	**Mar-23**
JPM USD Index	127	130	131	132	132
EUR/USD	1.05	1.02	1.00	1.01	1.02
USD/JPY	128	130	131	132	133
GBP/USD	1.25	1.18	1.14	1.15	1.16
AUD/USD	0.70	0.69	0.71	0.73	0.75
USD/CNY	6.69	6.85	6.90	6.95	6.95
USD/KRW	1268	1270	1290	1310	1330
USD/MXN	19.89	20.90	21.20	21.40	21.60
USD/BRL	4.88	5.00	5.20	5.30	5.30
USD/TRY	15.91	16.50	17.50	18.50	19.50
USD/ZAR	15.90	16.00	16.25	16.50	16.75
Commodities	**Current**	**Jun-22**	**Sep-22**	**Dec-22**	**Mar-23**
Brent ($/bbl, qtr end)	112	104	104	101	95
WTI ($/bbl, qtr end)	113	101	101	98	91
Gold ($/oz, qtr avg)	1,841	1,850	1,800	1,720	1,670
Copper ($/ton, qtr avg)	9,436	10,650	10,000	9,750	9,400
Aluminum ($/ton, qtr avg)	2,902	3,550	3,300	2,900	2,850
Iron ore (US$/dt, qtr avg)	134	150	140	125	
Wheat ($/bu, qtr avg)	11.7	15.0	14.0	12.0	11.5
Soybeans ($/bu, qtr avg)	17.1	18.5	17.0	16.0	15.5

Credit		Current	Dec-22
US High Grade (bp over UST)	JPM JULI	172	125
Euro High Grade (bp over Bunds)	iBoxx HG	187	175
US High Yield (bp vs. UST)	JPM HY	533	350
US Lev Loans (bp vs. 3Y Index	JPM Lev Loans	564	380
Euro High Yield (bp over Bunds)	iBoxx HY	542	525
EM Sovereigns (bp vs. UST)	JPM EMBIGD	486	350
EM Corporates (bp vs. UST)	JPM CEMBI	352	260
Equities		**Current**	**Dec-22**
S&P 500		3,823	4,900
MSCI Eurozone		233	275
FTSE 100		7,390	8,150
TOPIX		1,877	2,200
MSCI EM ($)		1,015	1,300
MSCI China		66	116
MSCI Korea		791	1,060
MSCI Taiwan		627	780
MSCI India		1,845	2,000
Brazil (Ibovespa)		107,371	133,000
Mexico (MEXBOL)		51,470	59,000
MSCI South Africa (USD)		441	521

Source: J.P. Morgan, Bloomberg Finance L.P., Datastream.