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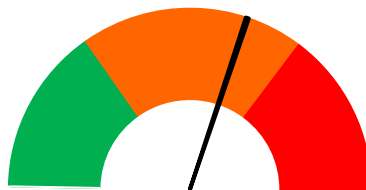
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- *Macro risks are omnipresent and come in multiple dimensions. They can stem from economies and markets, from various assets classes, and of course from geopolitics.*
- *In this publication we present a set of indicators to track economic momentum, event risk, market stress, asset valuation, and supply/demand imbalance that can flag potential pitfalls ahead in the macro landscape. We plan to provide quarterly updates of these indicators.*
- *Our surveillance lens spans macroeconomics and the four key asset classes (interest rates, currencies, credit, and equities). Given its geopolitical importance, we devote special attention to China.*
- *In the macro horizon, recent intensification of trade wars is threatening to undermine a nascent recovery in global trade. Positive data surprises are few and far between, while financial market volatility is on the rise.*
- *Equity and credit markets reflect no rush for the exit, but global fixed income markets are sounding alarm. US rates suggest rising recessionary risks with Fed rate cuts in the horizon. European markets see no end to negative rates.*
- *Despite risks stemming from rising tension between the US and Iran, oil prices are up only modestly. Beyond energy, the inflation picture is even more subdued, as reflected in declining breakeven inflation rates.*
- *FX volatility is on the way up, particularly in emerging markets, taking cue from the slide of the Chinese RMB.*
- *USD funding conditions are orderly, although not as comfortable as they were at the beginning of this year. Similarly, overall financial market conditions, having eased considerably in 1Q, have begun to tighten again as asset markets have turned restive.*
- *Our key concern involves credit markets in China and the US, given the substantial debt burdens. In China, onshore credit conditions remain stable thanks to PBOC's policy easing. But a weaker RMB and a decline in total social financing and loans could cause difficulties for corporates.*
- *US credit conditions are easy, but the debt burden is substantial. We remind our readers that seeds of financial crises usually reside in the intersection of high valuation and high debt.*

Composite Risk Score



Global Growth Momentum



Equities



DM Fixed Income



EM Fixed Income



EM FX



DM FX



DM Credit



EM Credit



Global Debt

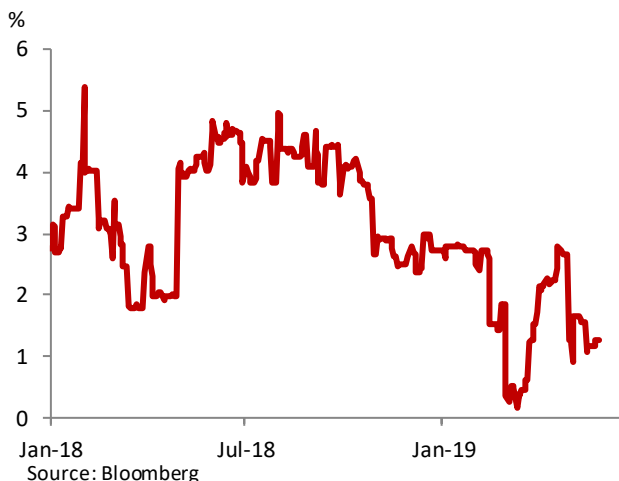


Note: The three-coloured speedometers above represent our conclusions on the outlook prevailing in various markets, as reflected in growth data, pricing, spread, and valuation metrics charted in the rest of this publication. The composite score is an unweighted aggregation of the nine sub-categories highlighted above. Note that bullish fixed income sentiments do not necessarily imply a positive outlook, although periodically they do. At the current juncture, negative government debt yields in Europe and very low yields in the US reflect very comfortable borrowing conditions, but they are likely in response to a weakening growth outlook (i.e. the outlook is red).

Global macro landscape

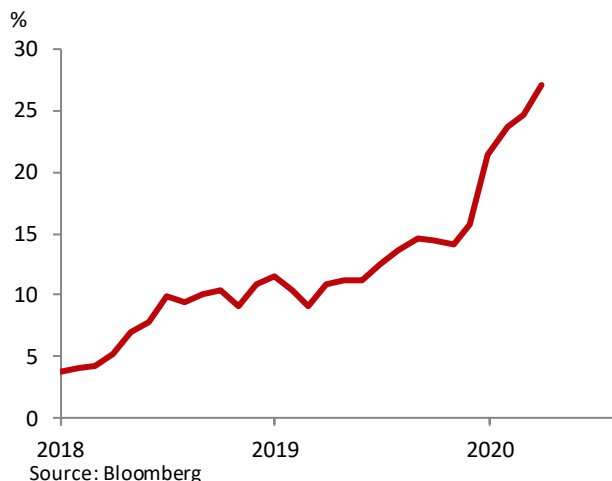
After a robust 1Q, US growth is softening as inventory accumulation hints at production slowdown

US GDP Forecast (Atlanta Fed)



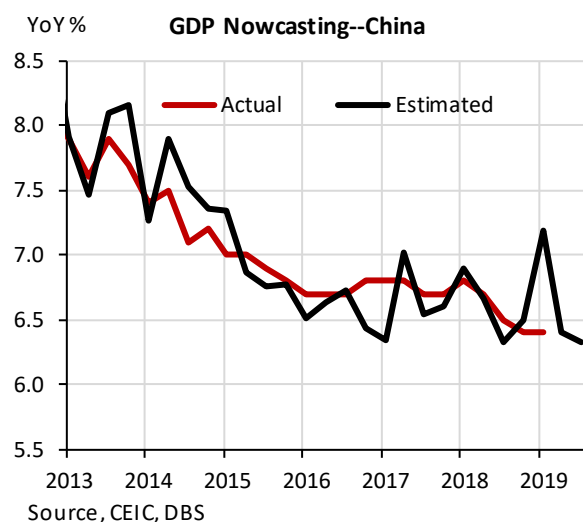
Note: Nowcasting model forecasts real GDP growth by aggregating statistical model forecasts of 13 subcomponents.

US recession probability is rising as the cycle ages
Recession Probability (New York Fed)



Note: Model uses the difference between 10-year and 3-month Treasury rates to calculate the probability of a recession in the United States twelve months ahead.

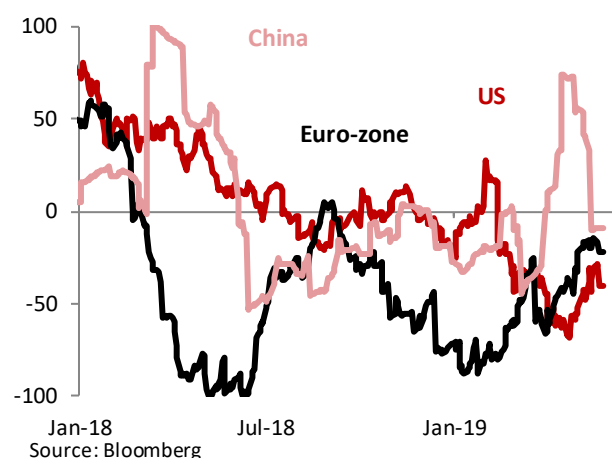
China is slowing sequentially despite large stimulus



Note: Nowcasting estimates real GDP based on a mix of latest available data (7 subcomponents) and model-based forecasts.

Positive economic surprises are few and far between

Economic Surprise Indices

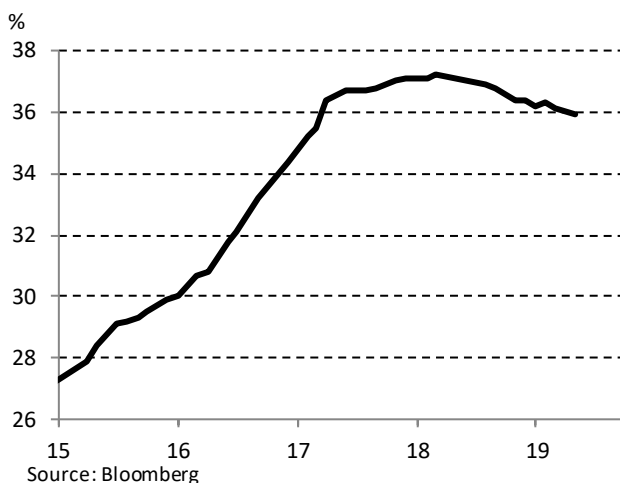


Note: Indices measure data surprises relative to market expectations. A positive reading means that data releases have been stronger than expected and a negative reading means that data releases have been worse than expected.

Macro landscape (continued)

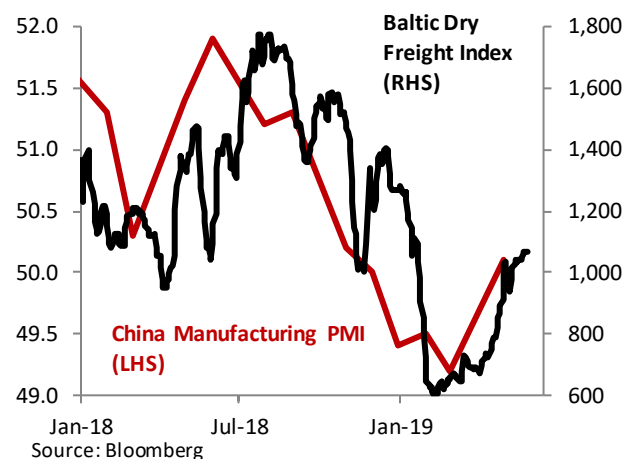
Major central bank balance sheets are no longer growing, although further policy tightening looks very unlikely in this cycle

Balance Sheet (% of GDP) - FED, ECB, BOJ, BOE



Latest data show a recovery in China's manufacturing activity and global trade, but for how long?

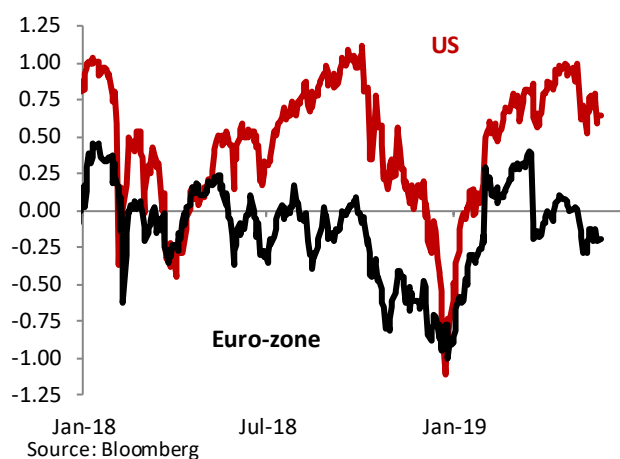
Baltic Dry Freight Index vs China Manufacturing PMI



Movements in the Baltic Dry Freight Index gives insights into the demand for metals, minerals, grains and building material. Index performs well as a leading indicator of global industrial production and economic activity.

Financial conditions rebounded at the beginning of the year, but have softened again due to trade wars and rise in geopolitical risks

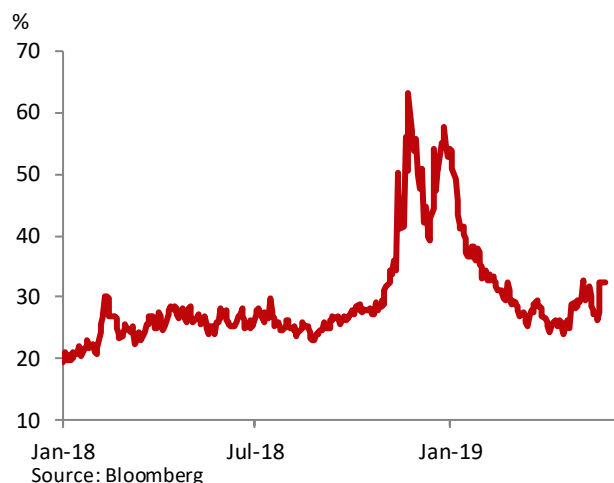
Financial Conditions Indices



Note: Indices track the overall level of financial stress in the money, bond, and equity markets to help assess the availability and cost of credit. A positive value indicates accommodative financial conditions, while a negative value indicates tighter financial conditions relative to pre-crisis norms.

Despite rising tensions over Iran, oil price is largely subdued

CBOE/NYMEX WTI Volatility Index

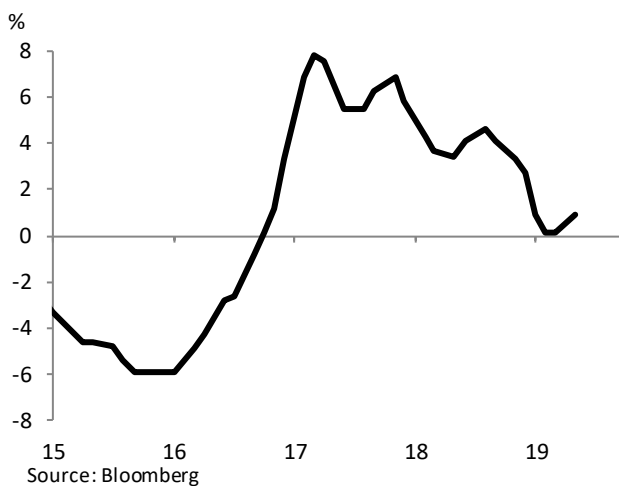


Note: Index measures the market's expectation of 30-day volatility of crude oil prices.

China

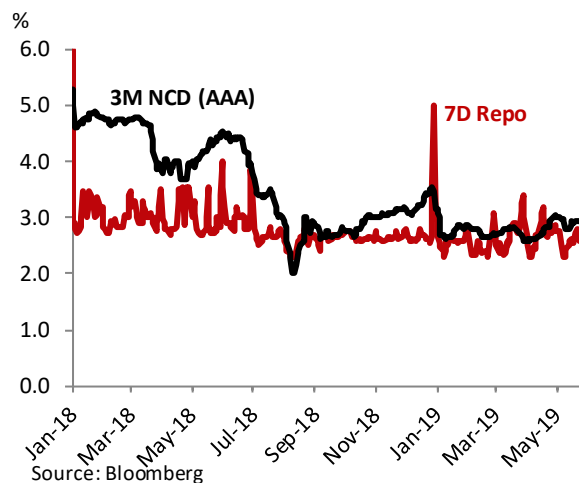
China's Producer Price Index reflects domestic demand condition, which looks subdued

China PPI



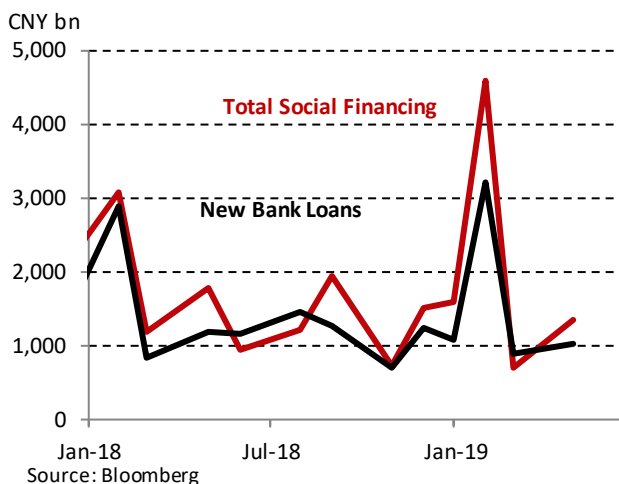
On-shore funding rates are stable, although the frequency of periodic tightness has increased

Key Onshore Funding Rates



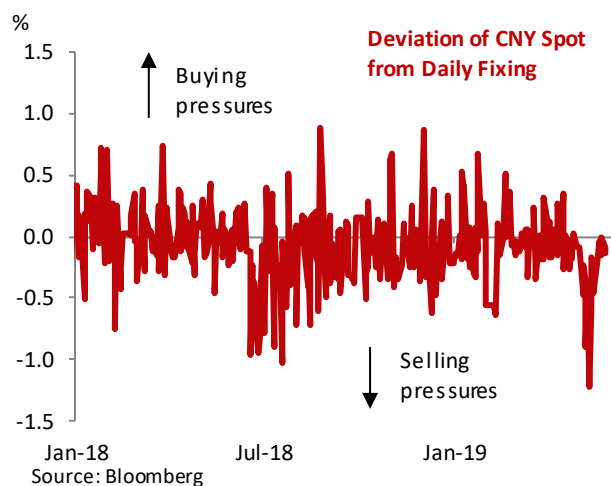
After a strong pick-up in early-2019, credit creation has eased considerably

Credit Growth and Liquidity



Escalation of trade war has manifested in higher RMB volatility, forcing PBOC to respond

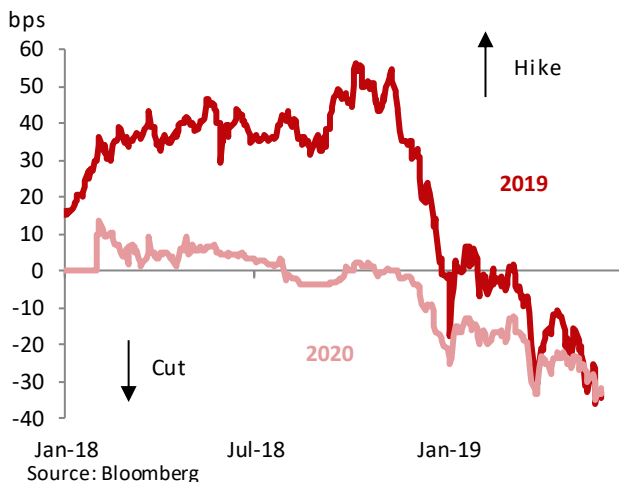
Measure of CNY stress



Interest rates

Rates market is pricing in several rates by the Fed between now and 2020

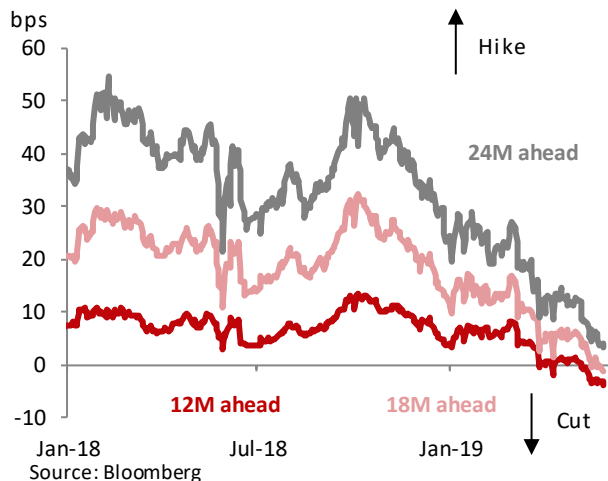
Fed Hike/Cut Pricing



Note: 2019 pricing is calculated as the spread between Jan19 and Jan20 Fed Fund futures. 2020 pricing takes the spread between Jan20 and Jan21 futures.

ECB rate adjustment expectations have evaporated

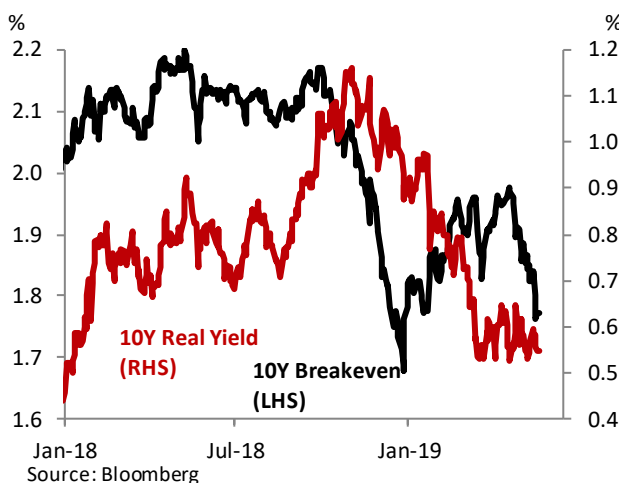
ECB Hike/Cut Pricing



Note: 12M ahead pricing is calculated as the spread between 1M forward 1M Euro overnight index average (Eonia) and 12M forward 1M Eonia. Extended for 18M and 24M.

Inflation expectations keep declining, despite tariffs and threats to oil price stability

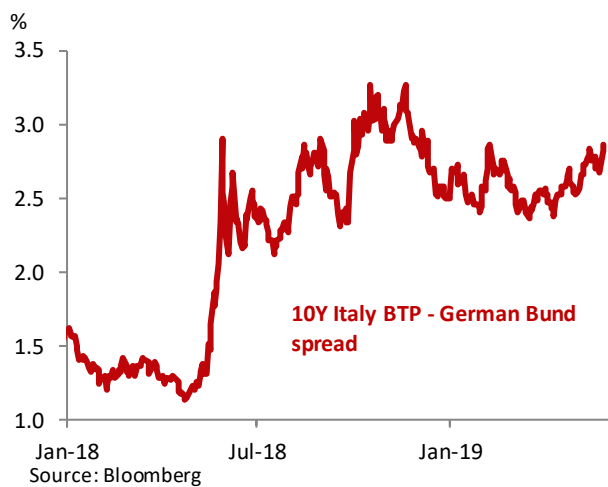
10Y US Real Yield vs Inflation Compensation



Note: 10Y real yield is calculated as the spread between 10Y US Treasury nominal yields and 10Y breakeven. Breakevens are the expected future inflation rates implied from Treasury Inflation-Protected Securities (TIPS).

Peripheral Eurozone risk is somewhat elevated

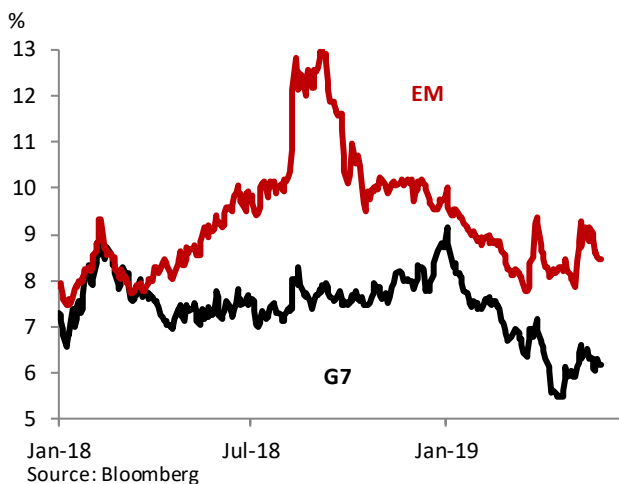
Eurozone Periphery Risk



Currencies

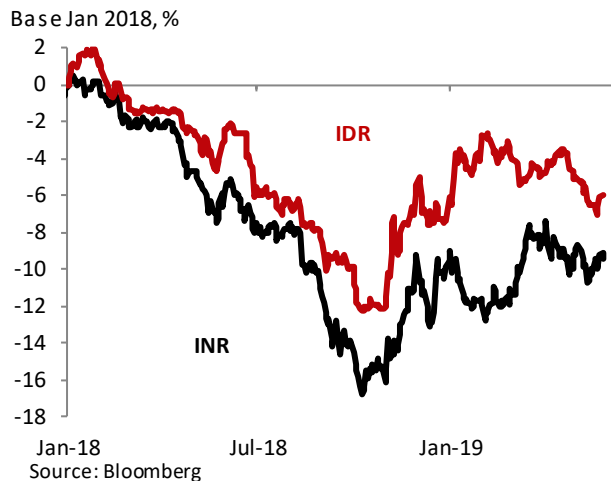
Rise in trade tensions have pushed up FX vols

Currency Vols (Implied)



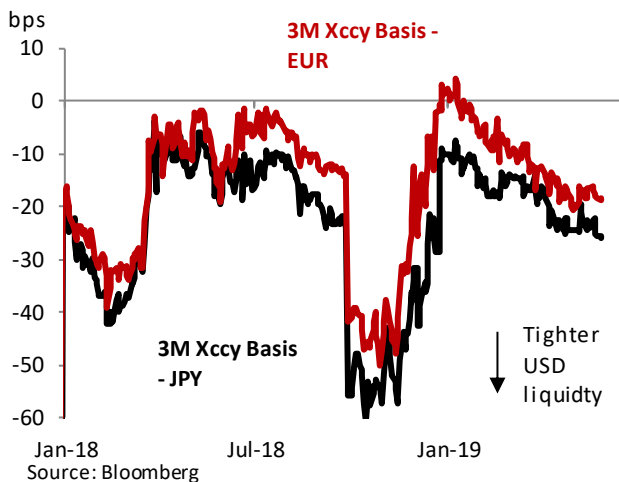
Asia's two high-yielding currencies, IDR and INR, remain vulnerable to external funding risks

Risk-Sensitive Currencies - Asia



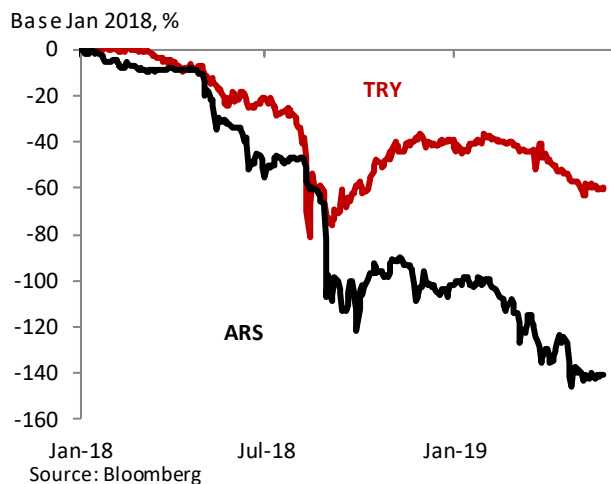
USD funding conditions have begun to tighten

Tightness of USD Funding - Secured



Key EMFX risks are in Argentina and Turkey

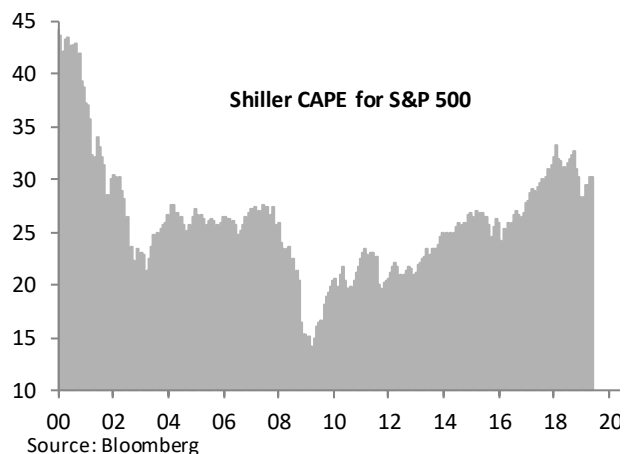
Risk-Sensitive Currencies - Global EM



Equities

US equity market is expensive by historical standards, although given low rates, higher equity premium may be somewhat justified

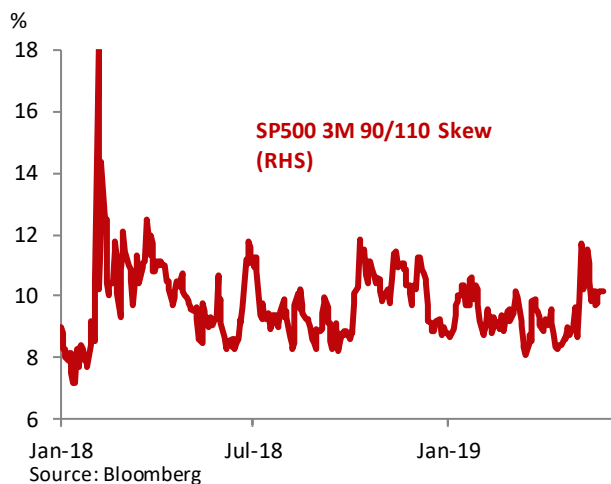
Measure of Equity Valuations



Note: Shiller PE ratio for the S&P 500 is based on average inflation-adjusted earnings from the previous 10 years, known as the Cyclically Adjusted PE Ratio (CAPE).

Risk aversion is still surprisingly low

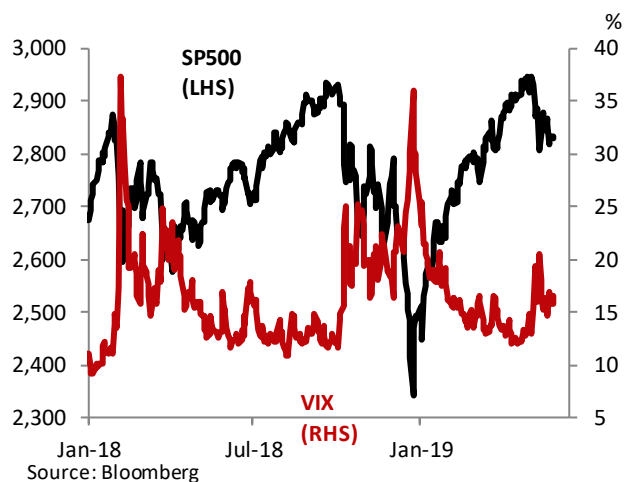
Measure of Risk-Aversion in Equities



Note: Vol skew acts as a risk-aversion measure by comparing demand for protective puts relative to bullish calls.

Despite a trade war escalation and considerable exposure to Chinese demand, US stock price and vols have not yet reacted sharply

SP500 - Price vs Vol

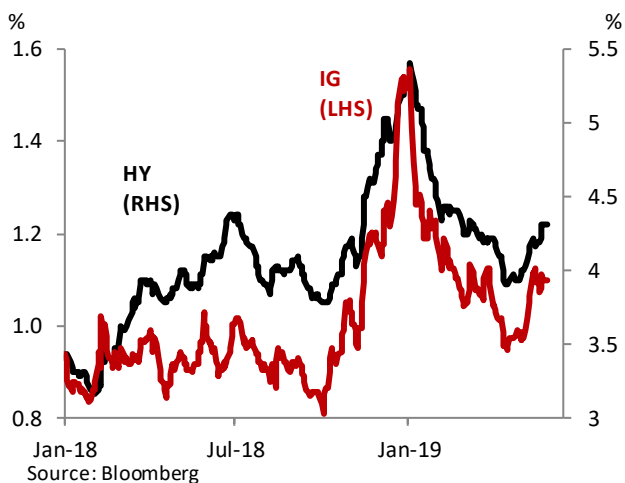


Credit

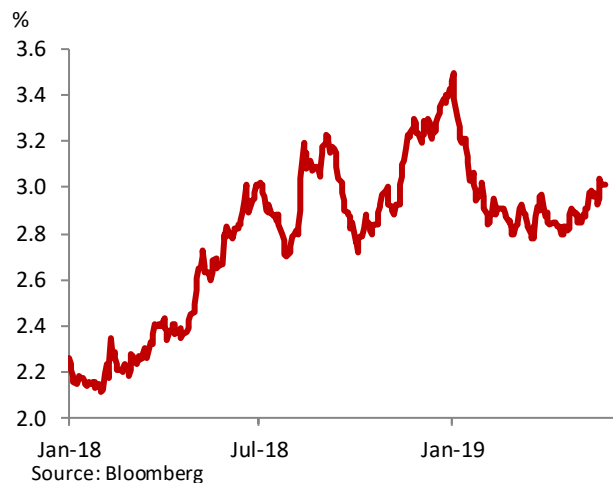
US credit spreads are rising again, perhaps reflecting concerns about pipeline economic slowdown

EM hard currency corporate debt markets are beginning to tighten

Credit Spreads - US Corporate

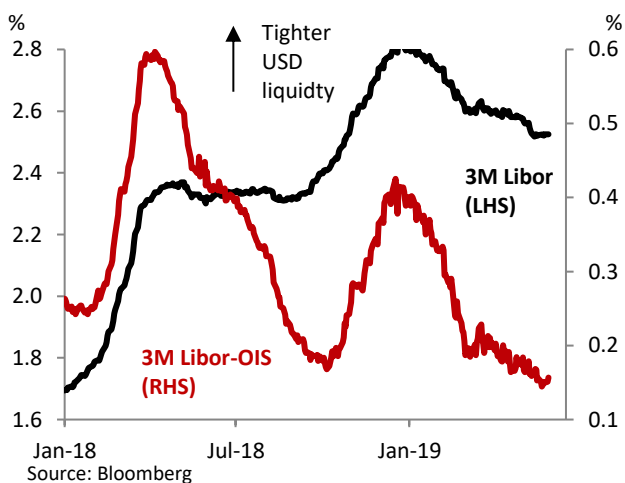


Credit Spreads - Emerging Markets USD



Liquidity is still orderly

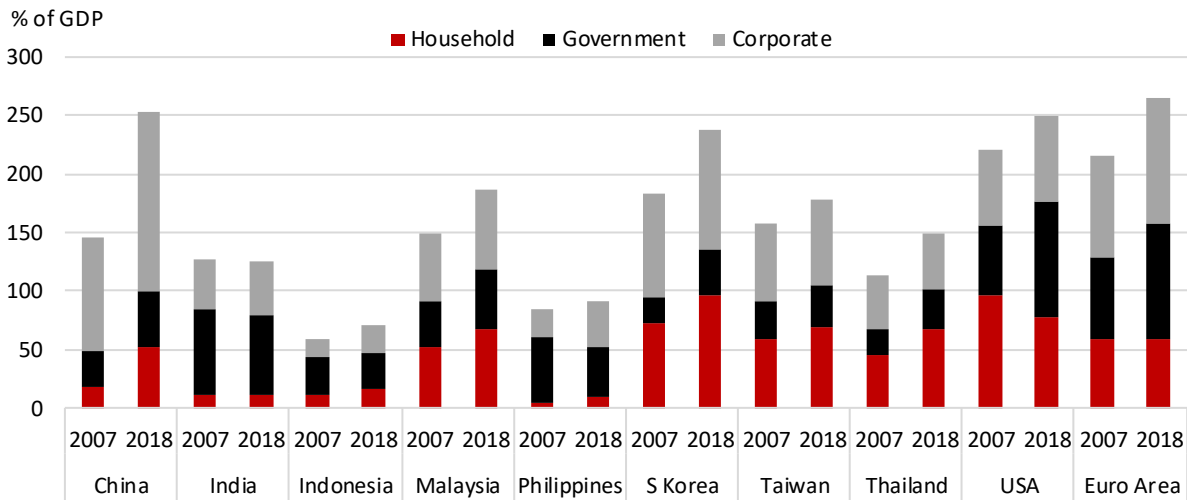
Tightness of USD Funding - Unsecured



Note: Measures USD liquidity in the commercial paper market.

Debt

Debt levels have risen worldwide since the 2008 GFC, particularly in China, US, and EU. The impetus therefore is to keep rates low, which in turn can fuel asset market bubbles, and make the next downturn very difficult to navigate



Source: CEIC, BIS, DBS

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