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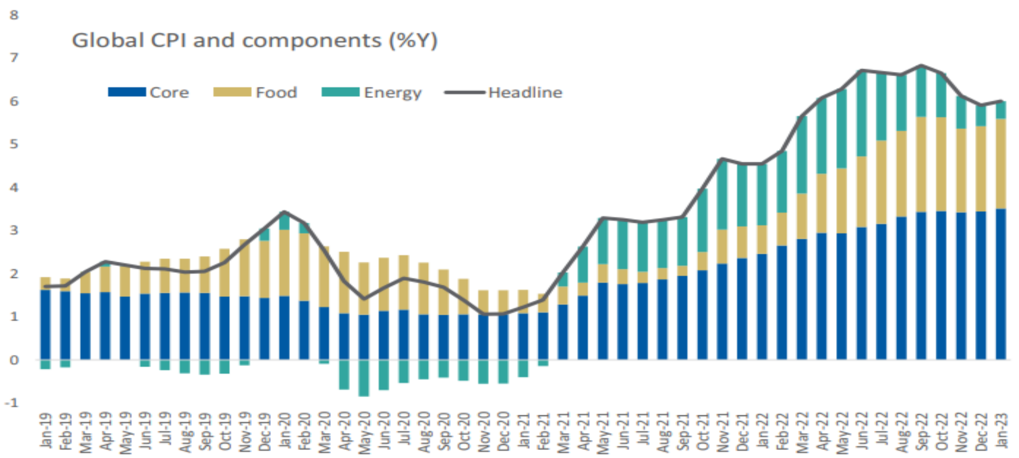
Macroeconomic Update

March 13, 2023

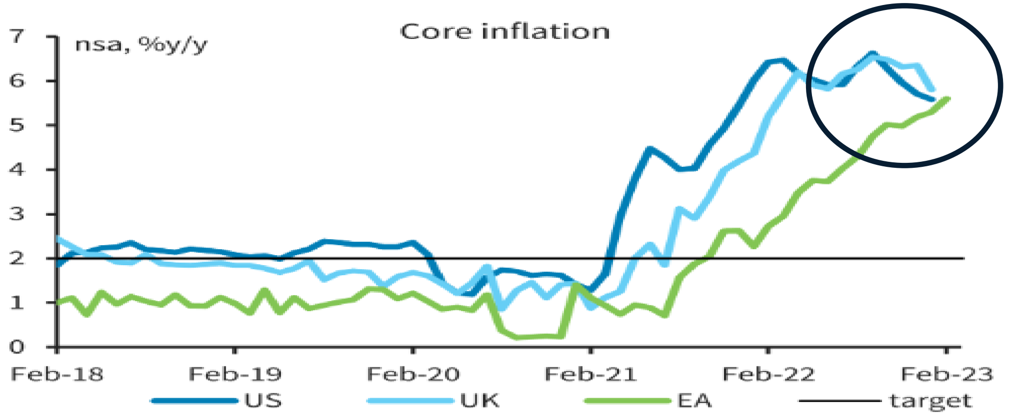
Global Macroeconomic Update

- **Treasury / Fed / FDIC Announced Emergency Measures Last Night to Nip Possible Banking Crisis in the Bud**
  - **Announced that all depositors at Silicon Valley Bank and Signature Bank would be fully protected**
  - **Decisive actions expected to stop depositor panic and limit risks to financial system**
- Macroeconomic highlights
  - Latest growth indicators for major DMs surpassing modest expectations
  - China’s reopening gaining momentum
  - Kuroda’s last meeting as BoJ Governor uneventful/ successor expected to unwind yield curve control
  - Central banks’ job of taming inflation not finished / core inflation still far above major DM central banks’ 2% target
  - Global inflation down from recent peaks but stubborn core inflation still far above central banks’ 2% target

Global Inflation[1]



Major DMs Core Inflation



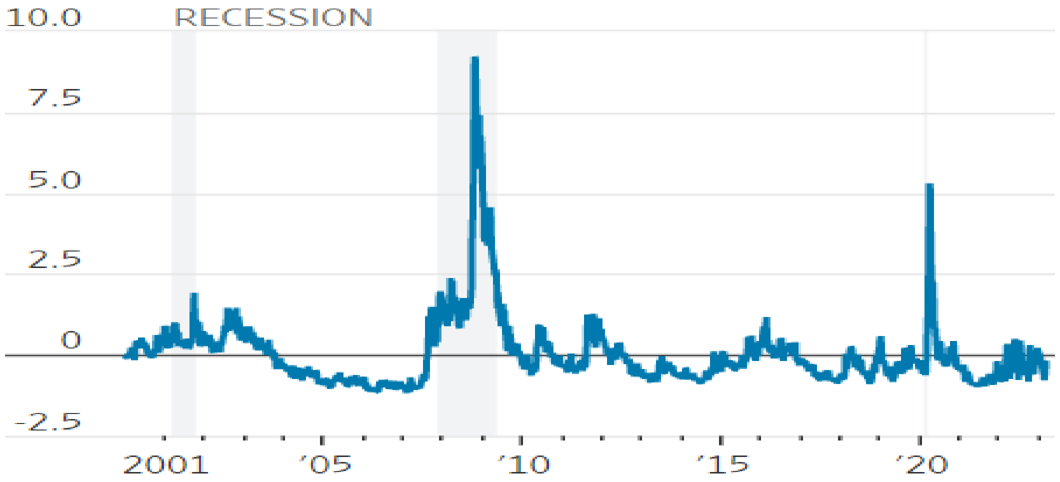
1. Global inflation excludes Russia, Ukraine, Turkey and Argentina

Source: Haver Analytics, MS, BLS, ONS, Eurostat

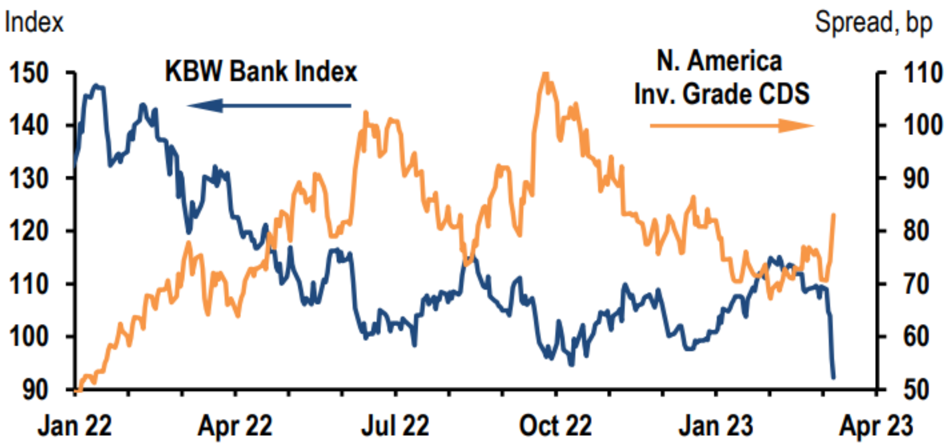
Country / Regional Briefs

- **US: Early February Data: Economy on Solid Ground / Moderating vs. January**
  - 311K increase in payroll employment strong but down from January’s blockbuster 504K increase
    - Insured unemployment claims, job openings, household survey data hinting labor markets starting to soften
  - Business surveys mixed: ISM services strong / new manufacturing goods orders soft
  - Silvergate Capital collapse not expected to systemic event --- banks well capitalized, signs of financial stress limited but …
    - Cap-weighted index of leading publicly-traded banks sold off in past week and investment-grade credit default swaps edged up
  - Strong recent data and stubborn inflation…
    - Generating upside scenarios and raising concerns higher rates will cause recession[1]

Financial Stress Index



Selected Financial Conditions Indications



1. Fed funds rate to remain above 5% well into 2024 to restore price stability which is likely to cause a recession. Frederic Mishkin, “Fed now on right track to restore price stability”, FT, 9 March 2023

Source: St. Louis Fed, Bloomberg, JPM

Country / Regional Briefs cont'd

- **Euro area: Latest Employment, PMIs, Retail Sales Data Strong but Inflation Core Inflation Needs to be Tamed**
  - Retail sales up 0.3% m/m in January / Germany's auto production rebounding
  - Another solid gain in-all-industry PMI in February
  - February flash inflation report signaled ECB has more work to do[1]
    - Headline: down 0.1%-pt to 8.5% yoy / core: up 0.3%-pt to 5.6% yoy

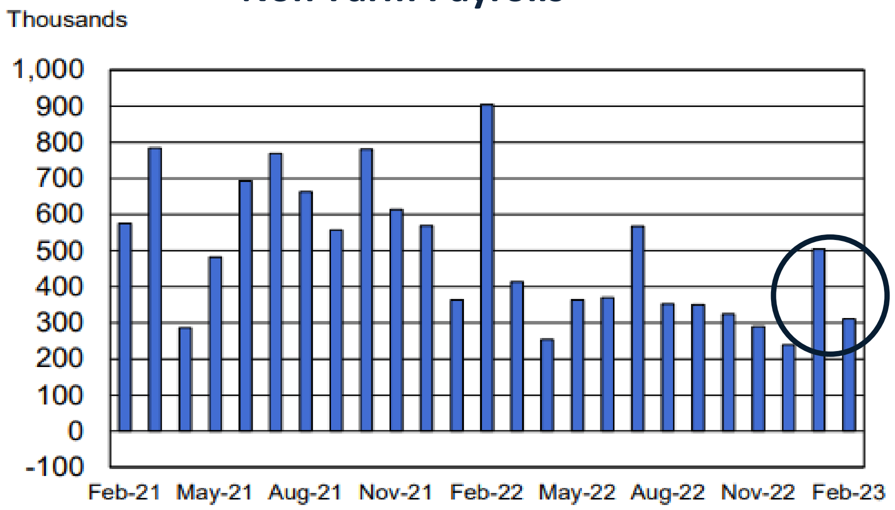
- **UK: Some Reassuring News but Wages & Inflation Continuing Challenge**
  - PMIs and January GDP report suggest economy expanding at modest pace[2]
  - Spring budget expected to provide modest lift to growth[3]
  - Interest-sensitive sectors impaired by higher rates
  - Governor Bailey's comment: "further tightening not foregone conclusion" seems optimistic
    - BoE's survey: wages growing at 5.7% pace / year – ahead CPI 5.9%[4]
  - Tentative agreement with EU re Northern Ireland potential long-term positive

- **China's new 5% Growth Target/Despite Strong Reopening Start…**
  - This year's growth objective lowest in decades
  - China Watchers[5]: target signals new era of caution
    - Leaders seemingly wanted attainable target
    - Acknowledges: property crisis, demographic challenges and exports expected to soften as interest rates rise

1. Christine Lagarde in recent interview indicated it is very likely ECB will raise rates another 50 basis points this month. Lagarde indicted that with employment robust and unemployment lowest ever, inflation is main concern currently. Thus, further increases are likely. Interview with Grupo Vocento, 5 March 2023
2. January GDP 0.3% m/m, February PMIs: overall manufacturing 49.3, composite services 53.5
3. GS: European Daily, 9 March 2023
4. BoE's DMP (Decision Maker Panel) survey for February
5. "China's lowest target for growth in decades…", FT, 7 March 2023

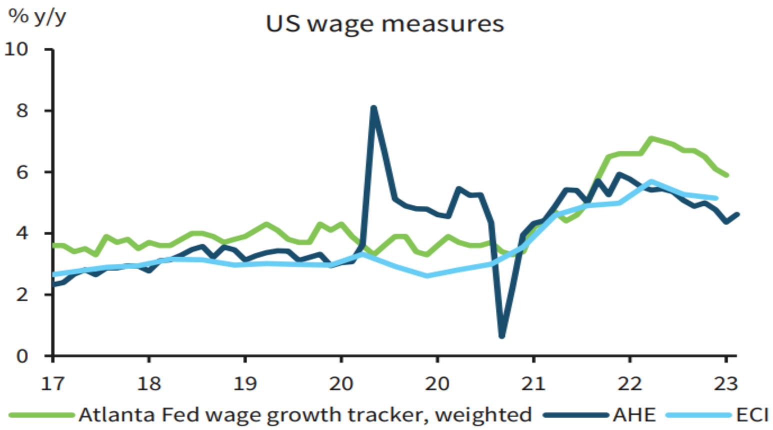
US February Employment Report

Non-Farm Payrolls

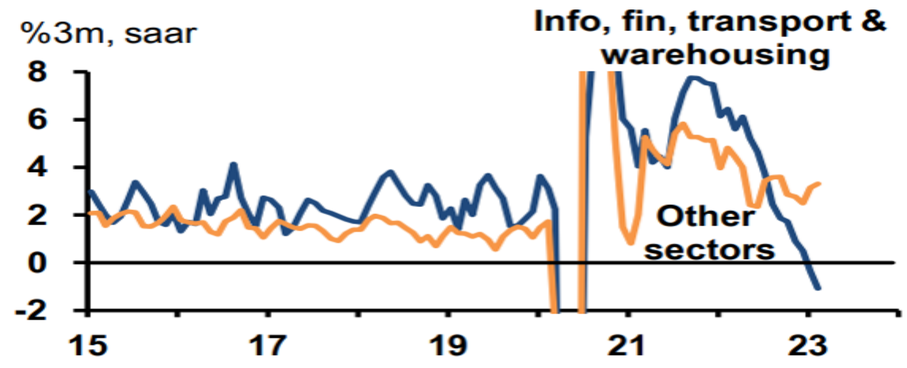


Higher Participation Unemployment Rates

Wage Gains Moderated but Still High



Employment Gains Concentrated in Certain Sectors



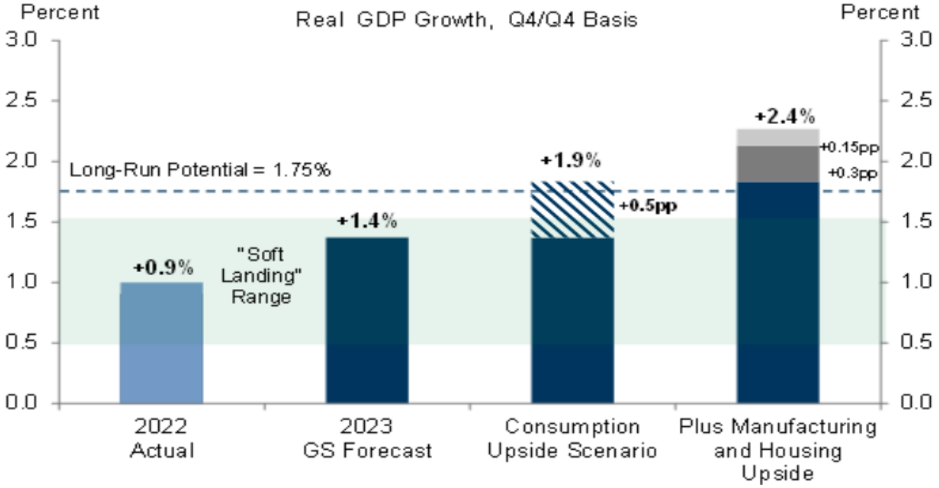
1. Notable job gains in leisure, hospital , retail trade, government and healthcare. Job losses in information, finance, transformation and warehousing.

Source: BLS, Atlanta Fed, Haver Analytics

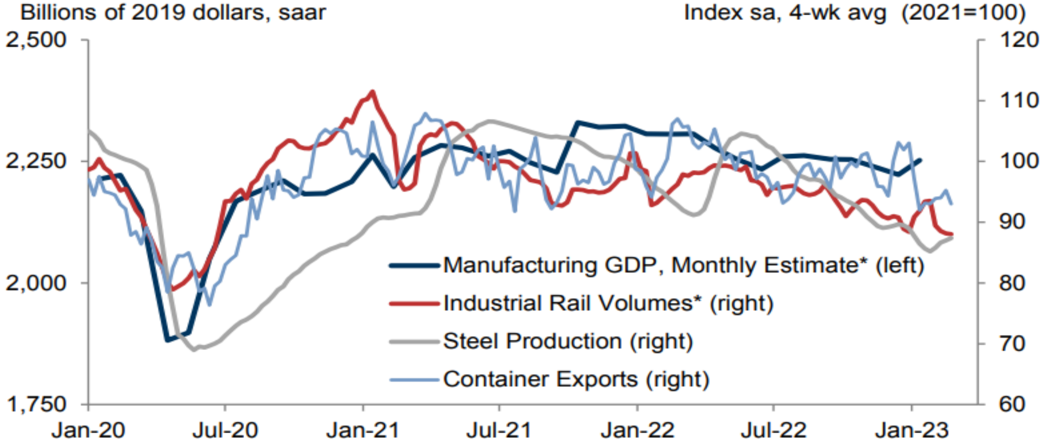
As of 28 February 2023

US: Upside GDP Scenario / Conflicting High Frequency (HF) Data

GS Upside Scenario



Recent HF Data Less Sanguine



- GS upside GDP scenario predicated on following:
- Consumer spending — driven by robust disposable income growth and draw down of excess savings — stronger than expected[1]
- Manufacturing receiving lift from China's reopening and brighten European outlook, while residential construction stops declining.

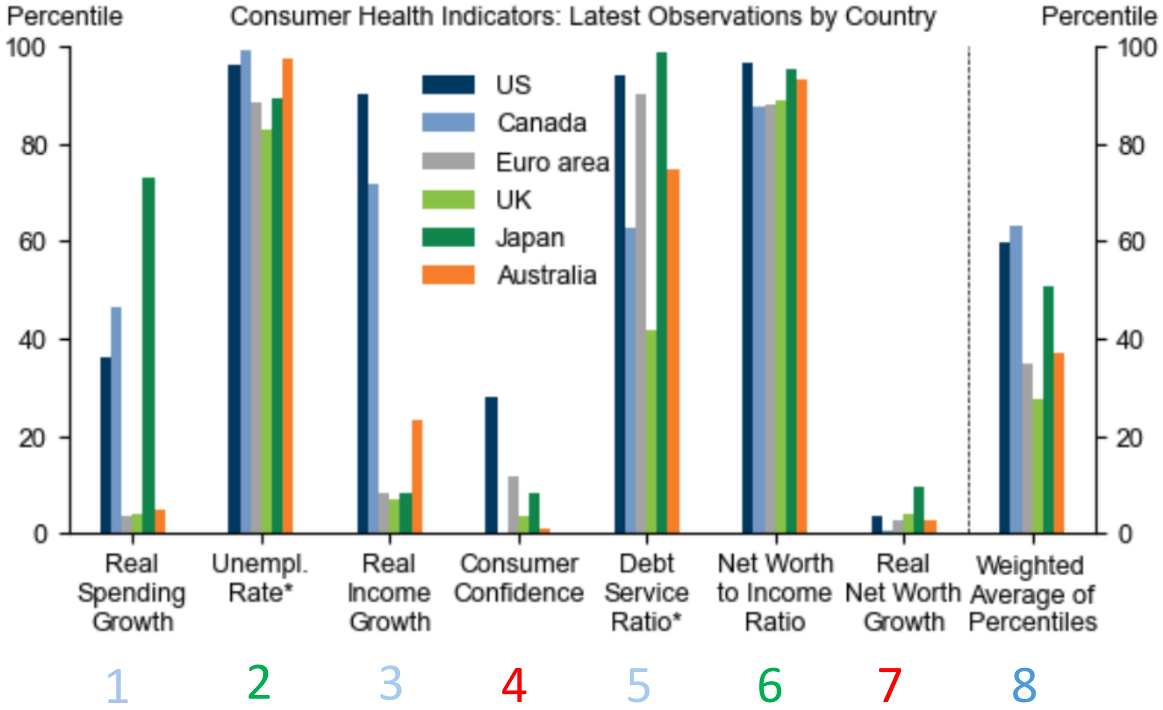
- Latest high frequency and mortgage data, however, suggest manufacturing and housing face significant headwinds
- Steel production and industrial freight activity point to continuing sluggishness in manufacturing, while rising mortgage rates and sapping buyer interest[2]

1. Disposable income in upside scenario benefits from continuing wage and unemployment gains, recent 9% social security increase, higher interest income, and reindexing of tax brackets
2. After declining from 7% in November to 6.1% in early February, average rate risen to 6.65% as of March 2.

Source: Department of Commerce, GS, Federal Reserve

DM Consumers: Confidence Low / Finances Still Sound[1]

Consumer Health Measures



- DM consumers still appear to be in relatively sound position based on…
  - (8) Weighted average of latest monthly readings for six key measures (bars on extreme right)
- Impressive strength across DM unemployment rates (2) and net worth (6)
- Real spending (1) and real income growth divergent (3) [2]
- Debt service ratios strong / manageable (5)

1. Unemployment rate (*) is an inverted scale. Percentiles cover monthly observations over 20+ year. US data since 1980; other countries data since 2000.
2. Selected percentile reading for latest real consumer spending growth: US ~38th, UK ~75TH, Euro area < 5th. Income real percentiles: US ~85th (distorted by social security increase), UK < 10TH, Euro area ~25th.

Source: Haver Analytics, GS. As of 9 March 2023.

Global Manufacturing Expectations Improving

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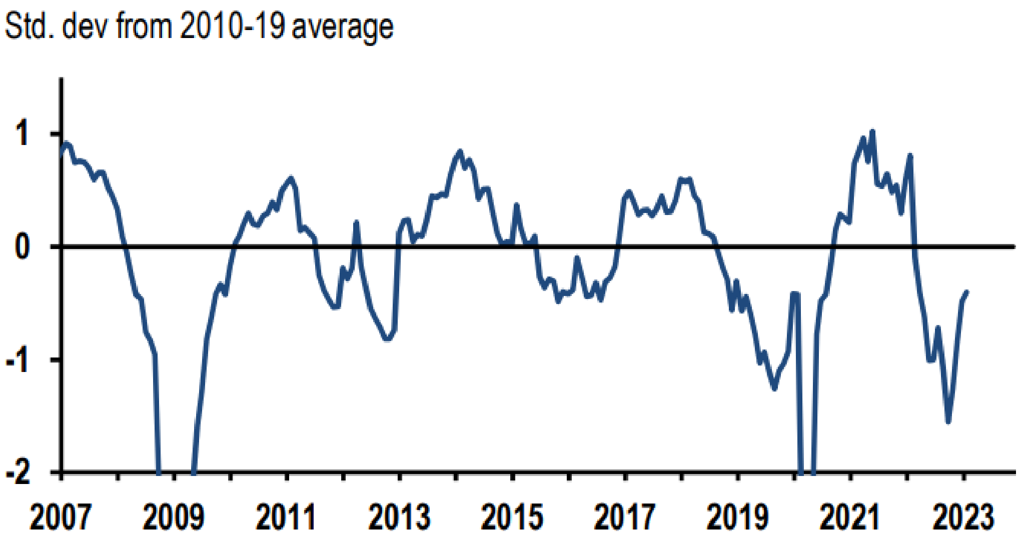
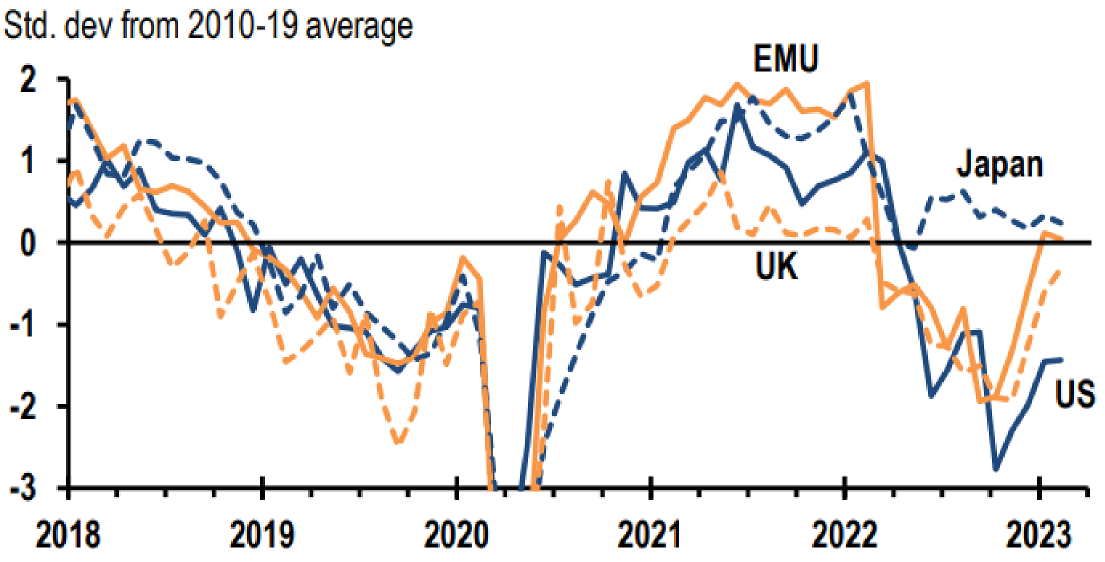
Global Manufacturing Expectations



DM Manufacturing Expectations



- Global manufacturing expectations recorded their fourth consecutive monthly increase in February
- Index, however, still implies that manufacturing expectations are low in historical context — 0.4 standard deviations below their pre-Covid average

- DM manufacturing expectations up from recent lows in February but mixed versus pre-covid average
- Euro area's & Japan's expectations -- benefitting from China's reopening — in line with pre- Covid average
- UK expectations are slightly below average, while US expectations are still lit standard deviations below average

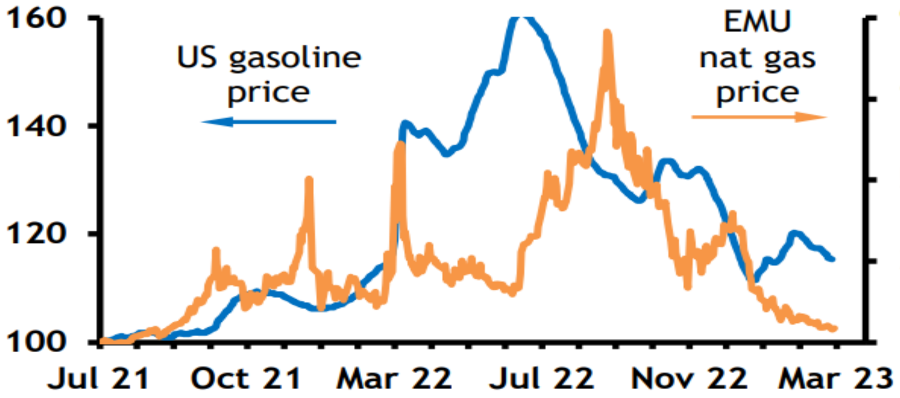
Source: S & P Global, National Sources, JPM
AS of 9 March 2023

Inflation Outlook: Current Positives Include:

Energy Prices and Core Goods &Import Prices

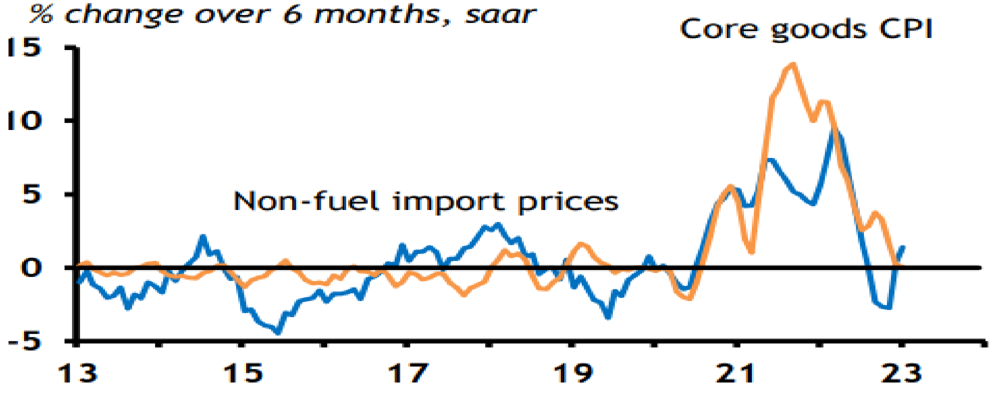
Energy Prices

Index: 01 July 2021 = 100; both scales



Source: Bloomberg, JPM

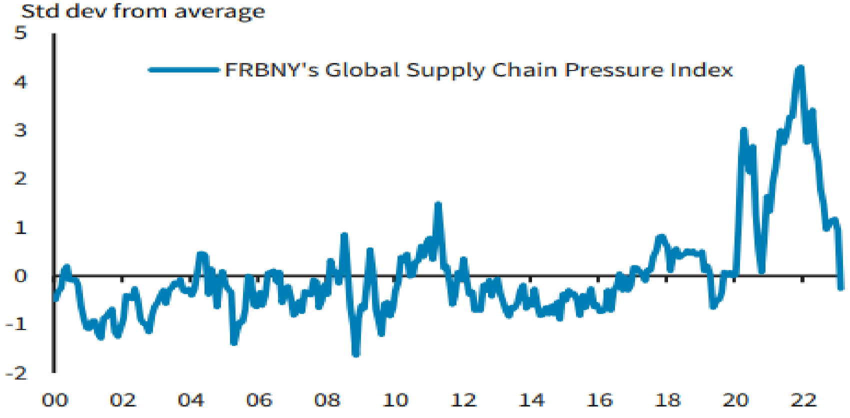
Core Goods & Import Prices



Source: Natural Sources, JPM

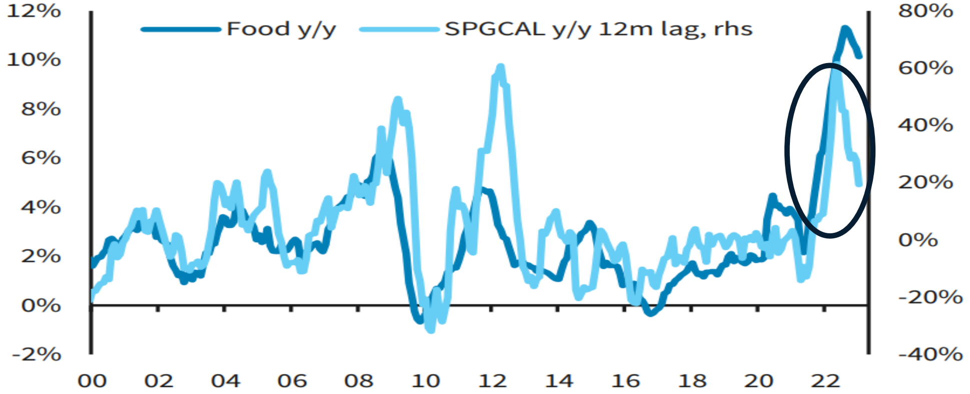
Factors in Place for Continuing Core Goods and Food Disinflation

Supply Bottlenecks Resolved



Source: FRBNY, Bloomberg

CPI Food and Agricultural Prices[1]



Source: BLS, Bloomberg, Barclays

1. S& P's global agricultural and livestock commodity index (SPGCAL) -- last plot January 2023 yoy -- ~ 20% increase, down from ~60% a few months ago. Given lagged transmission to retail food prices, this decline presages or slowdown in CPI food inflation. Barclays inflation report, 8 March 2023.

Inflation Outlook: Continuing Headwinds Include:

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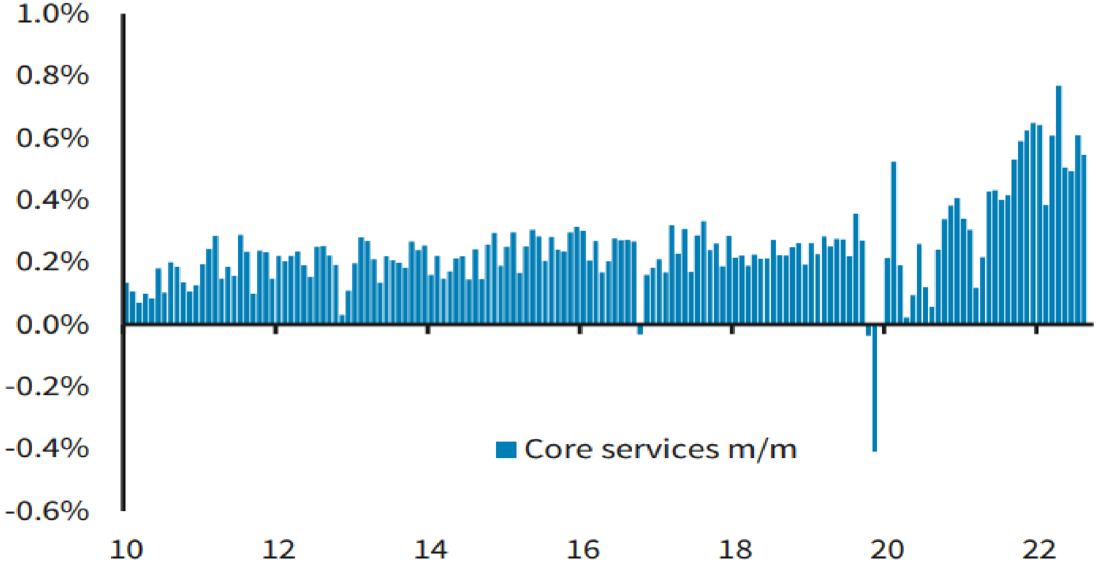
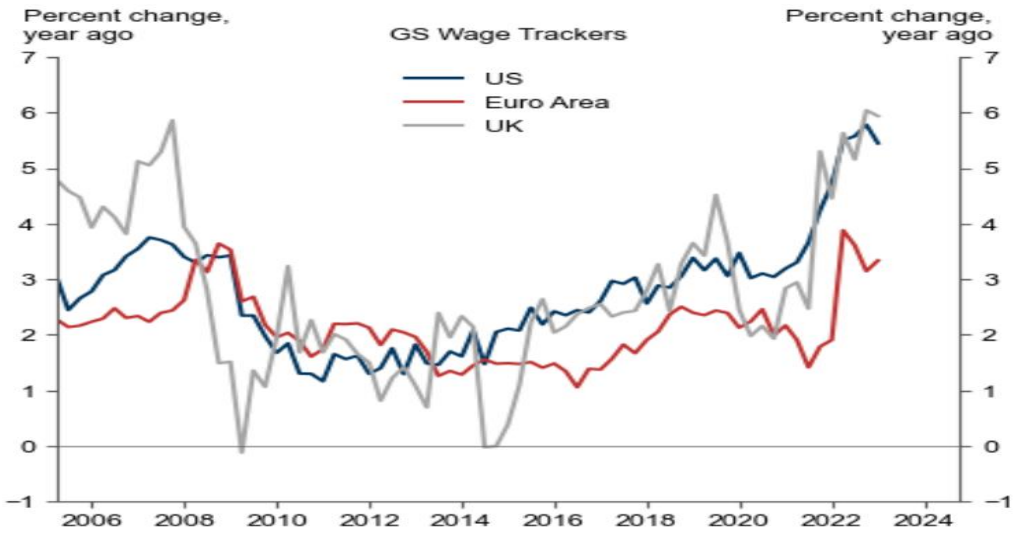
Sticky Service Prices



Wage Increases Above CB's Inflation Target



- Aside from service prices, factors seemingly in place for taming inflation in major DM
- Principal concern is service prices excluding shelter market-based rents point to significant slowing in US service prices

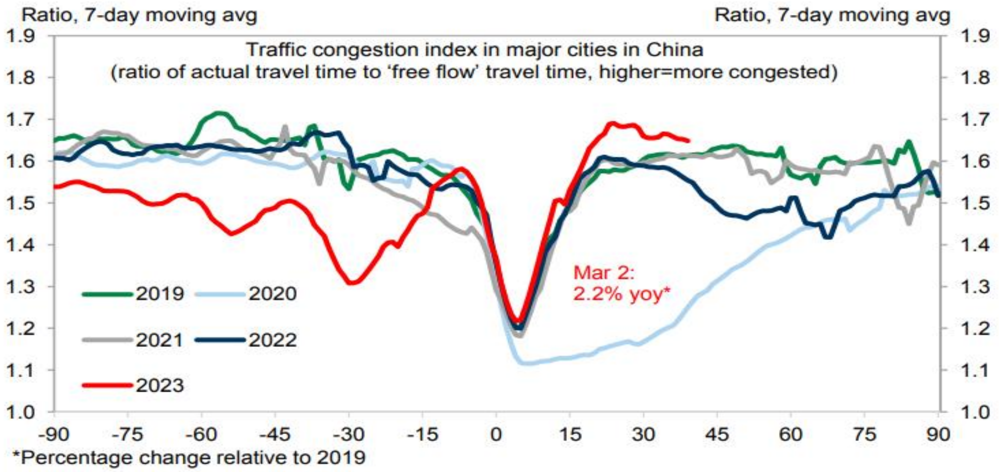
- Wages currently rising at 5.5% - 6% rate in US and UK and about 3.5% rate in Euro rate
- Wages increases in 3% - 3.5% range would be consistent with central banks (CB) inflation targets

1. Core service prices (ex shelter) account for ~25% of US CPI and 30% of PCE price index.
2. Average hourly earnings in February were up 4.6% y/y and 0.2% m/m

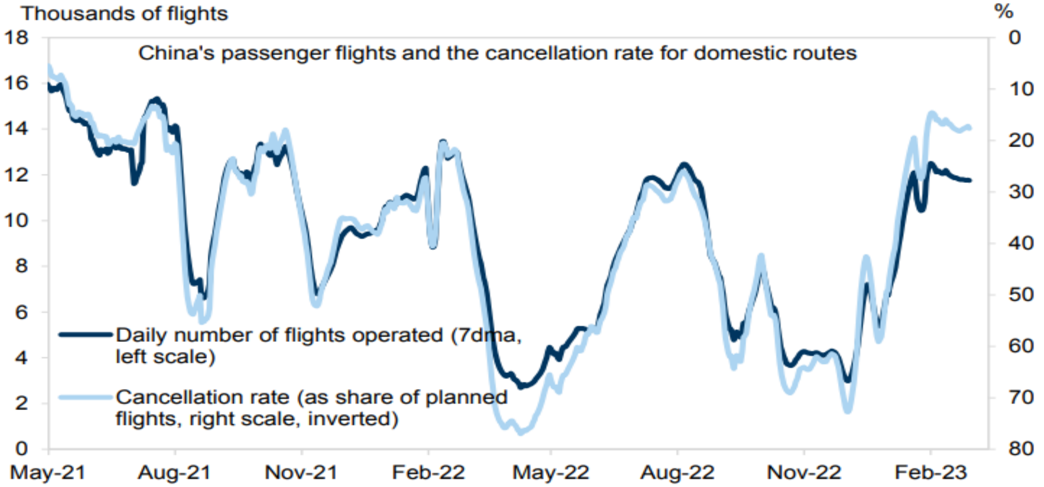
Source: BLS, Haver, Bloomberg, GS

China Reopening Charts[1]

Traffic Congestion

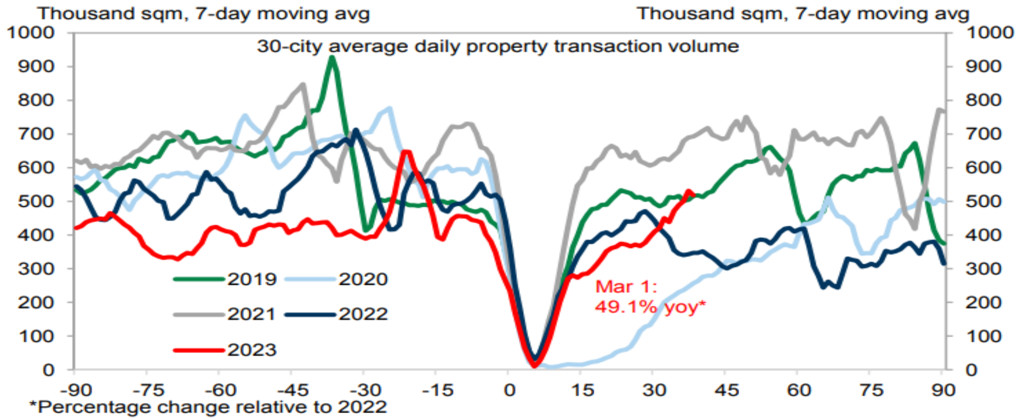


Domestic Passenger Flights



Steel Production

Property Transactions



1. Day 0 is first day of Lunar New Year

Source: Wind, GS, Mysteel

Japan's Yield Curve Control (YCC) : What's Next? Different Perspectives

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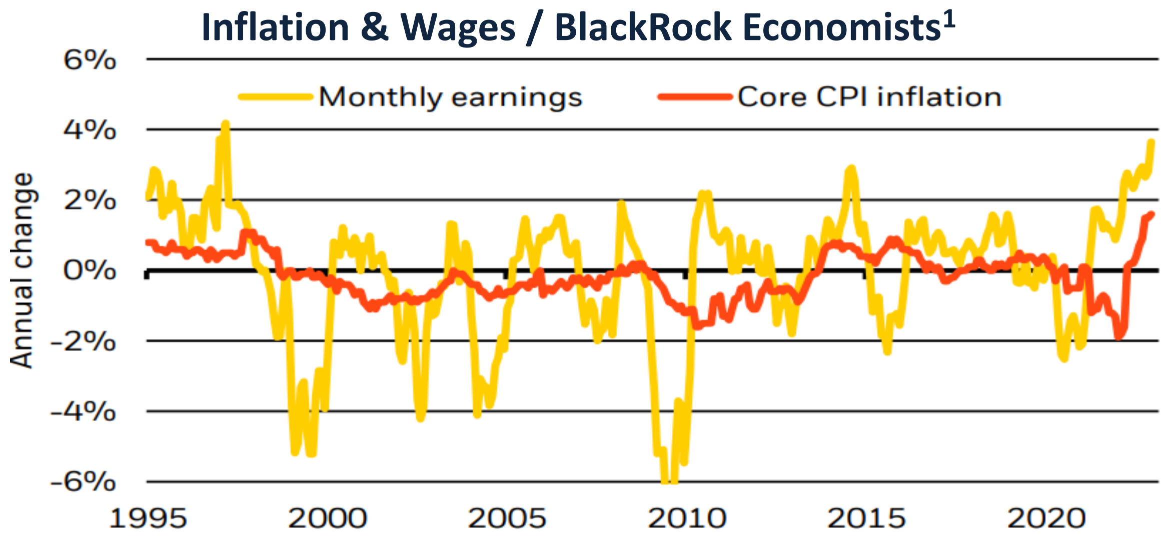
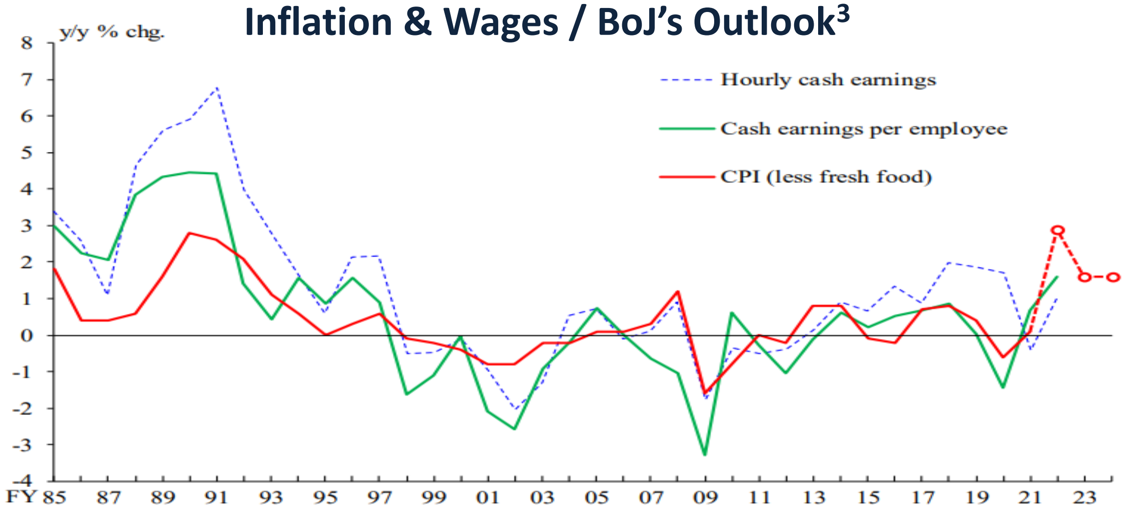


Source: Haver, Refinitiv, BlackRock



Source: BoJ

BoJ's fore. 1.6%

- Japan's recent CPI and wage increases highest in 40 years[2]
- BoJ appears set to change its ultra-loose policy
- BlackRock economists warn that expected rise in Japan yields will entail significant spillover risks for global yields
- Recent price surge due largely to higher energy prices and weaker yen
- BoJ economists seemingly less concerned re inflation risks. With global energy prices declining, inflation forecast to moderate to 1.6% in '23 & '24
- Wage growth expected to approximate 3% over cyclical horizon, consistent with price stability objective

1. "Preparing for Japan central bank shift," BlackRock Investment Institute, February 13, 2023.
2. "Toward Achieving the Price Stability Target in a Sustainable System and Stable Manner, Accompanied by Wage Increases," Governor Kuroda, December 26.2022
3. BlackRock's chart based on December data. Wages jumped 4.1% in December due to surge in bonuses. Recently released January data more subdued. Monthly (cash earnings) rose only 0.8% y/y in January

Different Views on What's Next for YCC

- **BlackRock Investment Institute Economists**
  - Wage and price dynamics suggest current ultra-loose policy about to run its course …
  - BoJ could widen band on 10-year yield target again or abandon its yield curve control at any moment
  - Central bank owns more than half of Japan's government bonds and could shrink its outsized balance sheet
  - Policy change would raise domestic yields and stroke rate volatility
  - Global spillovers would be likely, particularly if Japanese investors cut their large-foreign bond holdings

- **Japan Watchers (Ito and Baba) Have More Measured View[1]**
  - Last December's YCC shift prompted by currency management, not inflation
  - Wage-demand inflation that achieves 2% target would be welcomed
  - But persistently higher-than-expected inflation could prompt more policy normalization
  - Based on BoJ's forecast, CPI inflation is expected to fall below 2% target in '23-'24…
  - Central bank should be able to proceed cautiously and gradually

- **Incoming BoJ Governor Ueda Agrees that YCC Has to Change in Some Way…[2]**
  - If outlook for the price trend improves significantly…
    - We will move toward normalization including review of YCC and if…
  - Inflation expectations do not pick up, we will …
    - Continue easing measures, while reducing yield caps market-distorting effects[3]

1. "(Japanese) bonds, bonds,bonds", GS Top of Mind, February 23, 2023. Takatoshi Ito, Columbia prof and former MoF Minister; Naohito Baba, GS Chief Japan Economist
2. "Ditching bond yield cap will be trick for new BoJ governor", FT, February 24.2023
3. BoJ options include widen band on 10-year yield target, target short-term maturities --- e.g., 5-year or abandon YCC

Market Performance

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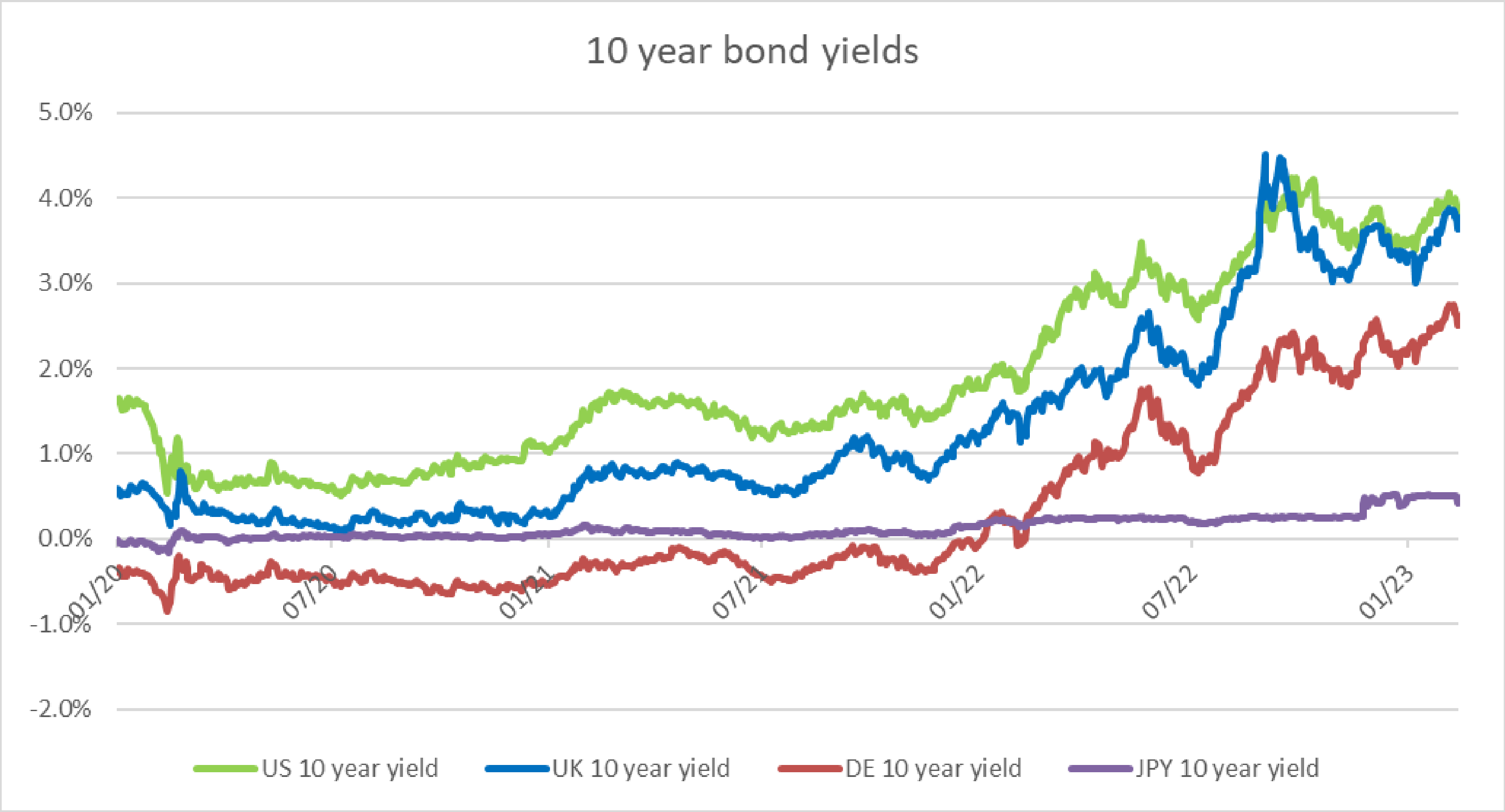
(USD)	MTD	YTD	2022	2021	2020
Equities					
MSCI ACWI	-4.37%	3.43%	-18.36%	18.54%	16.26%
MSCI EAFE	-2.00%	6.51%	-14.45%	11.26%	7.82%
MSCI EM	-7.05%	1.39%	-20.09%	-2.54%	18.31%
MSCI US	-4.79%	2.56%	-19.85%	26.45%	20.73%
Fixed Income					
BarCap Global Agg Total Return (Hedged)	-1.91%	0.68%	-11.22%	-1.39%	5.58%
Citi US 10+ Govt Bond Index	-5.33%	2.57%	-29.75%	-4.63%	17.72%
BarCap US High Yield Total Return (Unhedged)	-1.99%	2.17%	-11.18%	5.26%	7.05%
Oil					
WTI Crude	-0.27%	-4.98%	18.71%	47.90%	-10.62%
Brent Crude	0.01%	-3.57%	19.39%	44.38%	-12.39%
Currency					
USD/EUR	2.16%	-0.21%	6.62%	7.57%	-8.25%
USD/GBP	1.85%	-0.63%	12.64%	0.86%	-3.07%
USD/JPY	3.92%	1.73%	14.68%	11.52%	-4.99%
USD/CNH	2.47%	-0.12%	8.79%	-2.11%	-6.73%
USD/TRY	0.81%	1.30%	40.75%	78.97%	24.88%
USD/ARS	7.16%	13.33%	72.38%	22.11%	40.55%
USD/RUB	8.64%	5.18%	-3.41%	1.35%	19.10%
Returns to 03/10					

Source: Bloomberg

Sovereign Bond Yields



Source: Bloomberg
As of 10 March 2023

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