J.P.Morgan | Data Assets & Alpha Group

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ECONOMIC BACKDROP

- Global growth is 2% below pre-COVID levels and this should normalize in 2022. While goods demand has fully recovered, services is about 4% below pre-COVID levels. Expect growth to focus on Asia and US.
- US is approaching record low unemployment (3.9% vs. 3.5% record) with elevated inflation.
- In March, the Fed is expected to both end QE and to commence rate hikes. We see a total of 4 hikes in 2022.

Table 1: Global real GDP

% change annualized

	2021			2022		
	1H	3Q	4Q	1H	2H	4Q/4Q
Global (2.6)	**4.1**	**3.0**	**5.1**	**4.2**	**3.6**	**3.9**
DM (1.4)	**4.7**	**3.6**	**4.5**	**3.6**	**3.1**	**3.4**
US (1.5)	6.5	2.0	5.0	3.0	3.0	3.0
Euro area (1.3)	3.6	9.1	2.0	4.2	4.2	4.2
Japan (0.8)	-1.4	-3.0	8.5	4.7	1.2	3.0
UK (1.0)	8.3	5.1	5.2	3.2	2.0	2.6
EM (4.5)	**3.2**	**2.1**	**6.0**	**5.0**	**4.4**	**4.7**
EM ex China (3.4)	**2.0**	**6.5**	**7.7**	**4.2**	**3.4**	**3.8**
China (5.5)	4.6	-3.3	4.0	6.0	5.5	5.7
India (6.0)	-8.0	27.0	18.0	7.0	5.4	6.2
EMAX (3.0)	**3.7**	**0.1**	**10.2**	**5.4**	**4.2**	**4.8**
Korea (2.7)	5.1	1.2	5.0	4.0	2.5	3.2
EMEA EM (2.5)	**5.2**	**2.3**	**2.7**	**3.8**	**3.8**	**3.8**
CEE (3.3)	**5.8**	**5.8**	**3.3**	**5.6**	**4.8**	**5.2**
Russia (1.5)	4.4	0.8	2.3	2.7	2.1	2.4
Turkey (3.8)	6.3	1.6	0.8	3.0	6.6	4.8
South Africa (1.3)	4.4	-2.0	3.2	3.0	2.0	2.5
Latam (1.9)	**3.5**	**5.1**	**2.9**	**1.1**	**0.8**	**0.9**
Mexico (2.2)	5.3	-0.9	7.0	2.7	2.3	2.5
Brazil (1.5)	2.3	1.0	0.2	0.1	-1.1	-0.5

Source: J.P. Morgan Global Economics. Pre-pandemic potential in parentheses.

VIEW ON FED & RATES

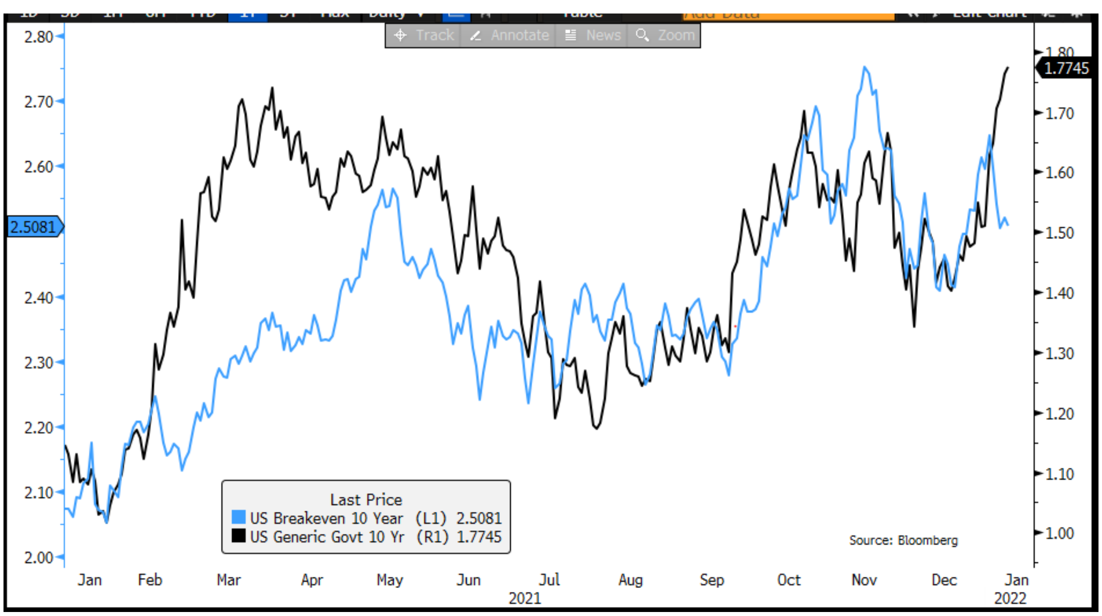
- Our Head of US Government Bond Strategy, **Jay Barry**, tells us to stay short the 10Y while he closes out his curve steepener trades, both 3s/7s and 10s/30s.
- Yields have converged to their fundamental drivers, with the 10Y yield remaining about 14bps from its model-implied fair value (10Y closed at 1.76% on Friday; FV = 1.90%).
- Positioning suggests that yields should go higher albeit at a slower pace than what we witnesses last week.
- Jay updated his Rates forecast and now sees **22Q1 closing at 1.90% and we finish the year at 2.30%.** Further, Jay tells us to **expect the yield curve to *flatten*,** approximately 40bps, with the bulk of this occurring from 2022Q2 onward.

J.P. Morgan interest rate forecast; %

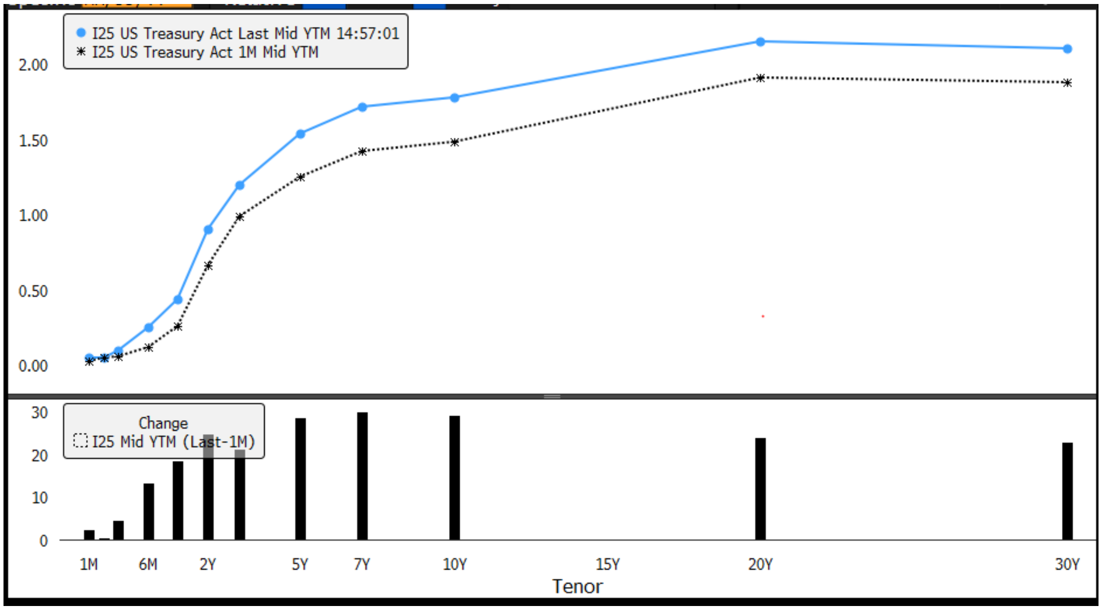
	Actual 7-Jan-22	1m ahead 7-Feb-22	1Q22 31-Mar-22	2Q22 30-Jun-22	3Q22 30-Sep-22	4Q22 31-Dec-22
Rates (%)						
Effective funds rate	0.080	0.10	0.35	0.60	0.85	1.10
SOFR	0.050	0.05	0.15	0.40	0.60	0.90
3-mo LIBOR	0.231	0.25	0.40	0.65	0.90	1.20
2-yr Treasury	0.87	0.90	1.00	1.25	1.50	1.70
3-yr Treasury	1.15	1.20	1.35	1.60	1.80	2.00
5-yr Treasury	1.50	1.55	1.65	1.85	2.05	2.20
7-yr Treasury	1.70	1.75	1.85	2.00	2.15	2.25
10-yr Treasury	1.77	1.80	1.90	2.05	2.20	2.30
20-yr Treasury	2.16	2.20	2.30	2.40	2.45	2.55
30-yr Treasury	2.12	2.15	2.25	2.35	2.40	2.50

Source: J.P. Morgan

US 10Y BREAKEVEN vs. US 10Y YIELD



US YIELD CURVE, MoM



Source: Bloomberg; data as of Jan 10, 2022

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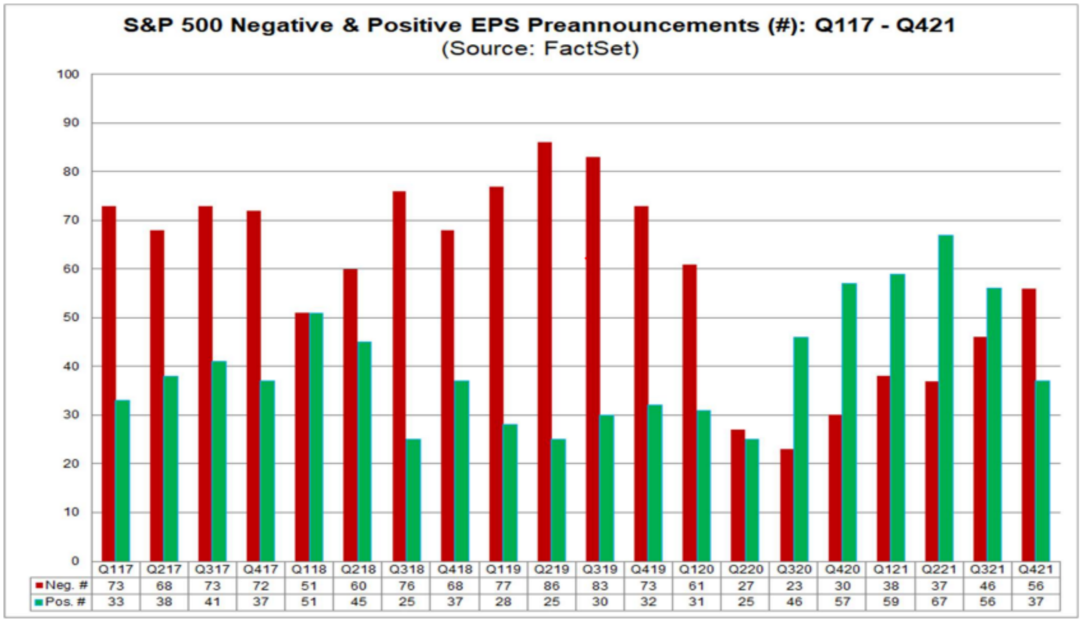
EARNINGS SEASON PREVIEW

FactSet details key metrics regarding expectations for 2021Q4 earnings season which kicks off this week:

- **Earnings Growth:** For Q4 2021, the estimated earnings growth rate for the S&P 500 is 21.7%. If 21.7% is the actual growth rate for the quarter, it will mark the fourth straight quarter of earnings growth above 20%.
- **Earnings Revisions:** On September 30, the estimated earnings growth rate for Q4 2021 was 20.9%. Six sectors are expected to report higher earnings today (compared to September 30) due to upward revisions to EPS estimates.
- **Earnings Guidance:** For Q4 2021, 56 S&P 500 companies have issued negative EPS guidance and 37 S&P 500 companies have issued positive EPS guidance.
- **Earnings Scorecard:** For Q4 2021 (with 20 S&P 500 companies reporting actual results), 15 S&P 500 companies have reported a positive EPS surprise and 18 S&P 500 companies have reported a positive revenue surprise.

Separately, FactSet notes that more companies are issuing negative guidance than positive guidance. This is the first time we have seen this since 2020Q2. However, the total number of companies issuing guidance is below the 5-year average.



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POSITIONING

- HF net flows have remained more positive lately. As we see it, cumulative net flows into cash equities by HFs are positive in aggregate over the past week. Furthermore, the 5-day z-score of net flows in N. America (where we had seen stronger selling around the middle of last week) is only at -0.7z through Monday vs. a level of -1.4z on 12/17/2021 or -2.2z on 12/3/2021.
- **Performance** – L/S challenges remain, but others fare better: After rebounding in the second half of Dec to gain about 2-3% for the month, L/S performance took a hit again this week due to the same driver that's been ailing them for a while – weak long returns amidst a risk-off undertone in the market. Even though shorts have been moving in the right direction, the weakness in longs meant that the weighted average return was -2.7% in the first 4 days of the year. N. America continues to be the pain point as European L/S performance appeared to be close to flat in early 2022. In contrast, non-Equity L/S funds (of which the biggest components are Multi-Strat and Quant Equity funds), appear to be flat to slightly up in early 2022, after a

solid gain in Dec of ~3%. Furthermore, the Long-Short spreads among these funds continue to rise as shorts underperform further

- **Leverage** – Nets fall again with L/S nets back near mid-Dec lows: After declining into year-end, across All Strategies, gross leverage was up 3.3% WoW (Thurs to Thurs) to the 41st %-tile over the past 12 months. Net however fell 1.3% WoW to the 49th %-tile on a 12M basis. Among Equity L/S funds, gross fell ~2% WoW to the 63rd %-tile on a 12M basis and is down 6 % points from mid-Nov highs. L/S net lev also fell 3.6% WoW, reversing most of the late Dec increase and putting it back near the lows we saw in mid-Dec—it's down 9 % points from mid-Nov high and just the 2nd %-tile on a 12M basis. While some of the net decline could be due to selling in recent days, it also seems likely that underperformance of L/S longs is contributing to the net decline as long leverage also fell back to around 12M lows.

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US MARKET INTELLIGENCE CURRENT TRADING VIEWS

I hold a bullish view on markets, driven by above-trend GDP growth, strong and improving fundamentals, and elevated shareholder distributions.

Since 1986, there have been 24 occasions where GDP exceeded 2.0% (long-term trend growth is 1.75 – 2%). Here is how major indices finishes in those years.

		AVERAGE RETURN (%)		
	# UP-YEARS	UP-YEAR	DOWN-YEAR	ALL OCCURRENCES
SPX	**20**	**14.0**	**(4.7)**	**9.9**
NDX	**22**	**24.1**	**(18.9)**	**18.3**
CCMP	**20**	**20.9**	**(12.9)**	**14.4**
RTY	**18**	**14.6**	**(6.6)**	**9.7**

Source: JPM Market Intelligence

- **Long QQQs** – FANG+ make up 42% of the NDX and QQQs are the most liquid instrument. These names make up the majority of SPX EPS growth since GFC. Further, they are also top quartile in terms of buybacks.
- **Long JPAMCONR** – I like this basket to play the Reopening trade, which also expands beyond the Epicenter stocks (airlines, casinos, cruise lines, and hotels). The US Consumer still has a

considerable amount of savings, \$2.4T or \$19k per household, and we have yet to see mobility fully normalize.

- **Long Energy** – choose from among XLE, XOP, OIH, and USO; pick whichever combination best fits your risk profile. I would ride the momentum within the Energy sector. Seasonality is strongest in the first half of the year, over the last 15 years. Supply/Demand dynamics are favorable to the bull case.
- **Long XME** – a cyclical play on global growth that is also tied to the China economic reboot. China is about 50% of global demand for base metals. The expectation is for an increasing amount of stimulus to be put into the economy. Recently, CCP stated it may look to accelerate projects under the 14th Five-Year Plan to boost growth.
- **Long IYT** – another beneficiary of global growth but also of easing supply chains. These companies will continue to benefit from above trend goods demand, as well as from increased energy demand (coal and oil).
- **Hedges: SPY**, **LQD**, and **XLP** – LQD is my preferred hedge and think it is also an alpha short. XLP may underperform in both a Growth-led and/or Value-led market. I think the bias to markets is higher especially considering we should see earnings support.

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CATALYSTS, OPPORTUNITIES, & RISKS

- **CATALYSTS** – (i) March FOMC; (ii) Earnings; (iii) China stimulus watch
- **OPPORTUNITIES** – (i) EM Equities; (ii) Reopening 2.0
- **RISKS** – (i) weaker than expected GDP growth, driven by inflation-induced demand destruction; (ii) weaker than expected earnings; (iii) multiple compression; (iv) geo-politics; (v) new COVID variant that is resistant to existing therapies.

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