MetLife

LEGG MASON
GLOBAL ASSET MANAGEMENT

# Legg Mason QS Commentary

## Monthly review

In January, global equity markets fell for the first time in five months - largely driven by the coronavirus outbreak, which led investors to a "risk off" sentiment. Within the U.S., large caps outperformed small caps, returning -0.0% versus -3.2%. U.S. equity volatility, as measured by the VIX Index, increased +36.7% to 18.8 – this level is in-line with the long-term average of 19.2. Abroad, developed stocks outperformed emerging markets, returning -1.2% versus -3.3%.

In January, risk-off currencies (USD, CHF and JPY) outperformed their risk-on counterparts. Over the month, geopolitical tensions and the coronavirus led to concerns around global growth. The USD rose +0.9% and was supported at the beginning of the month by a U.S. drone strike killing an Iranian general. On the last day of the month, the USD weakened after the Chicago PMI reading fell to 42.9 versus a 48.9 forecast.

The U.S. ten-year yield fell forty-one basis points and ended the month at +1.5%. The significant drop was driven by geopolitical tensions, the coronavirus outbreak and a weaker than expected non-farm payrolls report. The month ended with the spread between the three-month and ten-year yield inverting.

The price of crude oil declined -15.6% after rising +10.7% in December. China is the world's largest importer of crude oil, and the outlook for demand drastically declined due to the coronavirus. Crude oil received marginal support from supply falling in Libya due to a blockade in the country's export terminal.

Gold prices rose +3.9% and reached a several year high over the month. Gold retained it's "safe haven" status as geopolitical tensions and coronavirus concerns were top of mind. The U.S. and China signed the "phase one" trade deal during the month, however this had minimal impact on the markets as it had been announced in December of last year. The U.S. agreed to suspend additional tariffs and reduce the existing tariffs on $110bn of Chinese imports from 15% to 7.5%.

## Short Term Market Outlook

Our proprietary leading economic indicator declined month-over-month and remains in negative territory. This was driven by continued weakness in global trade and manufacturing.

Our outlook for U.S. stocks versus investment grade bonds remains in neutral territory. The weakness in the QS leading economic indicator has been offset by valuations (equity earnings yield compared to ten-year treasury yield) and the decline in treasury yields.

In U.S. fixed income, we forecast that high yield will underperform investment grade bonds over the near term. Within the model, the widening of the spread between these assets and a rise in equity volatility have tilted our model towards investment grade bonds.

We believe that U.S. stocks are positioned to underperform versus their international-developed market counterparts. This view is supported by valuation, which compares the forward price to earnings ratio in the U.S. versus their international counterparts. Options market data also shows greater demand for price protection in the U.S. versus international-developed markets. The options market data (where we measure the demand for put options versus call options) supporting international-developed markets is at its strongest level in several years.

European stocks are forecasted to outperform European bonds in our model. Valuation, as measured by comparing European equities earnings yield to the ten-year government yield, and equity price momentum continues to support stocks. European leading economic indicators now prefer European stocks for the first time in nearly two years.

Source: Bloomberg, QS Investors


**Important Information:**

This material is intended for informational purposes only and it is not intended that it be relied on to make any investment decision. It was prepared without regard to the specific objectives, financial situation or needs of any particular person who may receive it. It does not constitute investment advice or a recommendation or an offer or solicitation and is not the basis for any contract to purchase or sell any security or other instrument, or QS Investors, LLC to enter into or arrange any type of transaction as a consequence of any information contained herein. QS Investors, LLC does not give any warranty as to the accuracy, reliability or completeness of information which is contained in this document. Except insofar as liability under any statute cannot be excluded, no member of QS Investors, LLC, the Issuer or any officer, employee or associate of them accepts any liability (whether arising in contract, in tort or negligence or otherwise) for any error or omission in this document or for any resulting loss or damage whether direct, indirect, consequential of otherwise suffered by the recipient of this document or any other person.

The views expressed in this document constitute QS Investors' judgment at the time of issue and are subject to change. The value of shares/units and their derived income may fall as well as rise. Past performance or any prediction or forecast is not indicative of future results. This document is only for professional investors. Investments are subject to risks, including possible loss of principal amount invested.


Global Equities represented by the MSCI ACWI Gross Total Return Local Index; Emerging Market Equities represented by the MSCI EM Gross Total Return Local Index; International Equities represented by the MSCI Daily TR Gross EAFE USD Index; U.S. Equities represented by the S&P 500 Total Return Index; Japanese Equities represented by the MSCI Daily TR Gross Japan Local Index; U.S. Dollar (USD)represented by the Bloomberg Dollar Spot Index; Global Fixed Income represented by the Bloomberg Barclays Global Agg Total Return Index Value Unhedged USD; U.S. Fixed Income represented by the Bloomberg Barclays U.S. Agg Total Return Index Value Unhedged USD; U.S. Treasuries represented by the Bloomberg Barclays U.S. Long Treasury USD


**This information is only for use by professional clients, eligible counterparties or qualified investors. It is not aimed at, or for use by, retail clients.**